POLITICAL EMBEDDEDNESS, EXECUTIVE AUTONOMY, CORPORATE CHARACTERISTICS, AND FINANCIAL MALFEASANCE IN LARGE TELECOMMUNICATIONS COMPANIES

A Thesis

by

BRYCE HANNIBAL

Submitted to the Office of Graduate Studies of Texas A&M University in partial fulfillment of the requirements for the degree of

MASTER OF SCIENCE

December 2011

Major Subject: Sociology
Political Embeddedness, Executive Autonomy, Corporate Characteristics, and Financial Malfeasance in Large Telecommunications Companies

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ABSTRACT

Political Embeddedness, Executive Autonomy, Corporate Characteristics, and Financial Malfeasance in Large Telecommunications Companies. (December 2011)

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This thesis examines the causes of financial malfeasance in the largest U.S. telecommunications corporations between 1995 and 2004. Specifically, it examines whether or not the executive compensation package influences the likelihood that a corporation will falsify its financial statements. The methods used are both qualitative and quantitative. I approach the question form a historical point of view and attempt to identify certain salient characteristics within the telecommunications industry that may influence of unethical or illegal activity. The findings support organizational-political embeddedness theory, which suggests that differential social structures create dependencies, incentives, and opportunities to engage in financial malfeasance. The historical analysis shows that neoliberal policies enacted in the mid-1990s resulted in organizational and political structures that permitted managers to engage in financial malfeasance while limiting the efficiency of regulatory bureaucracies. The quantitative analysis yields mixed findings, many of which are consistent with previous research on white-collar crime and financial malfeasance. This thesis adds to existing literature by outlining significant public policy shifts and the results those shifts may have on specific
industries. These findings have important implications for political officials and corporate oversight organizations.
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1. INTRODUCTION AND RESEARCH QUESTION

The twenty-first century began with a series of financial collapses of large corporations within various industries; Enron lead the way followed by WorldCom, Adelphia, and Tyco. Political officials, corporate managers, and popular media have attributed, and continue to attribute, the origin of the collapse to individual characteristics such as greed and envy, instead of explaining why investors were unaware of executive financial decisions (Prechel and Morris 2010). While individuals’ unsavory ideals and morals may be partially responsible for any economic crisis and recession (Hooks et al. 1994; Mitchell et al. 1996; Stavros 1998), stating that the cause of a phenomenon of such magnitude is a consequence of the actions of a few individuals is an insufficient explanation at best. Other observers claim that the diminishing profits of stock holders and the lost retirement funds of employees were largely a result of lack of financial transparency and irresponsibility of executive managers (Hooks et al. 1994; Russell and Finnerman 1995; Holmes et al. 2002; Harris and Bromiley 2007).

Studies of white-collar crime and corporate malfeasance suggest that organizational characteristics, company size, enforcement strategies, budget restrictions, and economic conditions affect organizational deviance and corporate crime (Jensen and Meckling 1976; Clinard and Yeager 1980; Simpson 1986; Leatherwood and Spector 1991; Tillman and Pontell 1995). Prechel and Morris (2010: 350) recently showed that differential corporate structure (i.e., the multilayer-subsidiary form) enables corporate

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This thesis follows the style of *American Sociological Review*. 
Managers to “engage in and conceal financial malfeasance.” Understanding the causes of white-collar crime is needed in order to protect the investing public and to ensure capital growth and stability (Fama and Jensen 1983). I suggest that the combined influences of differential social structures, political embeddedness and corporate characteristics are important factors in the study of corporate malfeasance. To examine if this is the case I focus my research on telecommunications companies, in the period following the enactment of the Telecommunications Act of 1996.

With the expansion of the internet and World Wide Web, corporate executives in the telecommunications industry acknowledged the profit-making opportunities associated with expansion in this industrial sector. However, regulatory policies limited the capacity of corporations to realize such goals.

Advocates of deregulation maintained that telecommunications needed to be “unshackled so that the United States could properly enter the information age” (Horwitz 1989: vii). In response, the Telecommunications Act of 1996 was enacted to establish “the terms for competition within local telephony, for a range of telecommunications services, for competitive video services provision, and for expansion of broadcast service” (Aufderheide 1999: 61)
2. THEORETICAL PERSPECTIVES

Previous studies on executive compensation and forms of corporate malfeasance have focused on behavioral and agency theories as well as individual characteristics to explain executive action (Schnatterly 2003; Harris and Bromiley 2007; Simon 2008). However, organizational sociologists have suggested that studies on the individual have not resulted reliable and accurate conclusions because individual and corporate actions are constrained through capital dependencies (Mizruchi and Stearns 1994), other resource dependencies (Pfeffer and Salancik 2003) and corporate structures (Prechel and Morris 2010). Understanding and analyzing individual morals and values, therefore, cannot sufficiently explain individual or corporate action.

Schnatterly (2003: 588) states that the research conducted on organizational malfeasance is insufficient and there is a need to more thoroughly link corporate malfeasance research to organizational theory. Therefore, the conceptual framework I will use draws from organization-political embeddedness theory, which (1) “identifies historical conditions that structure corporate actors’ motives and actions, and (2) maintains that corporate-state relations cannot be separated from one another in modern society because state policies give form to corporate structure” (Prechel and Morris 2010: 332). I employ this framework to examine the following research question: How do organizational characteristics, including corporate structures, financial performance, and executive compensation, affect a corporation’s likelihood of involvement in financial malfeasance?
This study is important because it also tests widely accepted explanations in the field of economic sociology. Jenson and Murphy (1990) imply that incentives offered to a chief executive officer (CEO) may be unimportant to production and market performance. Others suggest that because executives may have inside knowledge to shifting market values they will undoubtedly act strategically and opportunistically (Boyer 2010), even if the strategies used to do so are illegal or unethical. Boyer (2010) further states that executives are able to maximize individual profit through casual use of insider information; the use of such information is illegal when used for personal gains at the expense of other investors.

2.1 Organizational and Political Embeddedness

In the 1980s a revival of the use of comparative historical sociological methods raised questions about theoretical explanations which ignore historical variation and disregard historical breaks and changes. Ahistorical sociological research and analysis causes a separation of theory and history. This separation yields invalid discovery because such research “denies or masks important features of historical reality” (Isaac and Griffin 1989: 873). Following this theoretical logic, organizational-political embeddedness theory posits that historical conditions affect an executive’s decisions and actions (Prechel and Morris 2010). Studying historical variation is important because economic and state regulations vary over time. Corporate actors are enabled or constrained by events and circumstances internal and external to their companies.

As explained below, organizational-political embeddedness theory further maintains that differential social structures create dependencies, incentives, and
opportunities to engage in financial malfaisance. This theory suggests that forms of executive compensation (i.e., stock holdings or stock options) create incentives to falsely represent the companies’ financial data to increase executive financial gains.

2.2 Dependencies

Organizational structure theories maintain that corporations become resource dependent, meaning that much of an organization’s actions occur in response to the world or other organizations (Pfeffer and Salancik 2003), when externally constrained or controlled (Prechel and Morris 2010). Resource dependency encourages corporations to enhance autonomy and pursue self-interests. A company’s market and regulatory environments, and its resource dependencies promote competition and create uncertainty that constrains corporate action and threatens a corporation’s survival (Pfeffer and Salancik 2003; Boyer 2010). Capital dependencies, or borrowed monies (Mizruchi and Stearns 1994), affect how a corporation manages its finances and creates incentives to change its organization and structure (Greve 1998; Prechel and Morris 2010). To illustrate, during the 1980s corporations changed from a multi-divisional form to a multilayer-subsidiary form due to capital dependence and tax benefits (Prechel and Boies 1998; Boyer 2010). A multi-divisional form is one company structured as various sections based on areas of focus. The multilayer-subsidiary form is made up of legally independent companies nested under a holding or parent company. The parent company owns majority of the stock of the subsidiaries and acts as a financier to them.
2.3 Incentives

Economist and other social scientists have disputed the effectiveness of various executive incentive structures for decades. A topic of debate is the commonly accepted pay-for-performance plan. The plan implies that individual behaviors resulting in awards or other incentives tend to be repeated (Hamner 1975). Behavioral scientists have long supported this principle, as it has been adhered to by large corporations and small businesses who have implemented an executive pay-for-performance or merit pay system (Jensen and Murphy 1990).

Research on executive incentives typically falls into two categories: bonuses and stock awards (Harris and Bromiley 2007). Bonuses are past incentives and serve only as a proxy indicating what an executive might earn in the future. Stock awards, on the other hand, are future incentives that can be monitored and, because of insider knowledge, partially predicted by an executive. By the late 1990s, compensation in stock options was widely practiced. In 1997, 71.8 percent of firms gave some kind of stock offering as a part of their executive compensation package (Monks and Minow 2004).

According to March and Simon (1993) when monetary rewards are dependent on performance, the consequences of increasing production are more favorable. Well established incentive ties will influence managerial actions and decisions. When executives are compensated in or awarded stock options, they share corporate profit and goals with the shareholders. This compensation creates incentives for managers to act more like owners and implement strategies for long-term increase in shareholder value. Boyer (2010) stated that “[aligning] the interests of shareholders and managers” was the
motto of the 1990s. Much of the increase in stock-options payment was due to the “new economy” start-up companies who offered modest salaries with a significant number of stock options. This tactic allowed companies to keep production costs low and show higher profits because stock options were not required to be included in company costs (Boyer 2010).

2.4 Information Asymmetries and Opportunist Behavior

Economic sociological theory states that a realistic description of market action assumes that market actors are subject to bounded rationality and market opportunism (Baker 1984). Bounded rationality assumes that human cognitive ability is limited by a person’s ability to make decisions under conditions of complexity and uncertainty. This limitation occurs when (1) individual actors are not able to comprehend the complexity of various situations or the business environment in general (Williamson 1975) or (2) information necessary to make prudent financial decisions (such as, amount of debt) has been purposely withheld by corporate individuals.

Investors are entitled, however, to sufficient financial data prior to investing. Consequently, corporations are required to divulge financial information that accurately represents a company’s financial standing. In the mid-1990s corporate managers reported inaccurate financial information to regulatory bureaucracies. Consequently, investors made important financial decisions as if the information were accurate and fully disclosed (Malik 2003). Their exposure to risky financial situations defined by uninformed decisions resulted in financial losses.
Organizational-political embeddedness theory likewise posits that varying historical conditions create incentives for executives to act opportunistically and not divulge sufficient financial information to the investing public. Acting opportunistically is described as self-interested action that is not trustworthy in pursuit of financial profit (Williamson 1975). A market opportunist will “take advantage of others, provide false or misleading information, break agreements, and so forth” (Baker 1984: 778). The combination of market opportunism paired with information asymmetries and uncertainty are especially critical in creating a vulnerable marketplace for investors. These conditions pose, however, little financial risk for an opportunist executive (Williamson 1975). The opportunistic executive may exploit any level of investor risk to further his/her individual motives.
3. CASE STUDY AND HISTORICAL CONTEXT

3.1 The Telecommunications Industry

Telecommunications has undergone substantial innovation, expansion, and change since the end of the First World War. Prior to 1921, in a time known as the era of competition, consumers saw increasing utility prices for low quality products and service. Small locally driven telecommunications companies emerged in competition with Bell Telephone Company (Bell). However, because Bell controlled the cost of switch-board use, many small companies raised consumer prices drastically in order to maintain profitability and secure sufficient finances for company survival. Local governments responded by regulating what small companies could charge for telephone services (Sterling et al. 2006).

During the First World War, the federal government assumed control over parts of communications service, but relinquished its involvement in 1919. The Postmaster General and Navy officials convinced Congress that only public ownership could ensure low prices of telecommunications services. Prior to 1921, Congress allowed telecommunications companies, primarily American Telephone & Telegraph (AT&T) and Bell, to pursue market acquisitions and consolidation (Sterling et al. 2006). However, because only AT&T and Bell were in a position to take advantage of this opportunity, the Willis-Graham Act of 1921 ended the early competitive era.

The significance of the Willis-Graham Act of 1921 is that it provided a transition whereby the government accepted the idea that monopoly, not competition, was the proper structure for the telecommunications industry. Additionally, the Act redefined
telecommunications to be a public utility (Sterling et al. 2006). Government officials and economists viewed competition in the nation-wide service as wasteful of natural resources and AT&T was the only telephone operator not banned from providing local and long distance services (Aufderheide 1999). The Federal Communication Commission (FCC) identified the telecommunications industry as a natural monopoly, which implied that telecommunications services were more effective and efficient when offered by only one company (Sterling et al. 2006).

This monopolized service was also heavily regulated by federal and state governments. Laws and regulations during the 1920s and 1930s were concerned with quality of service and rate of return, not corporate governance and dishonesty. Regulatory bureaucracies’ primary focus was ensuring that AT&T offered an affordable-quality service under its protected status as a monopoly (Aufderheide 1999). The rate-of-return regulation limited what AT&T could charge consumers for its services while ensuring the prices charged were sufficient to cover the company’s expenses.

The FCC and federal government were forced to adapt communication policies and regulations to the social and professional lifestyles of the public, regardless of marketplace involvement (Aufderheide 1999). For nearly 40 years the FCC and communications policy underwent very few changes. The monopolized industry opened competition to long distance and international calling and telephone equipment in the early 1970s. Competition created painful pricing challenges because local and long distance cost had been politically, instead of economically, established between the FCC and AT&T prior to the 1970s. Aside from the pricing dilemma, the switch from a
monopoly to a competitive long distance market was relatively smooth and unproblematic. There were other times of budding competition but wartime interruptions, partisan changes, and other factors secured AT&T’s position as a market leader (Sterling et al. 2006). Other policy changes made to the telecommunications industry were minor and oriented toward upholding the liberties given by the first amendment in the U.S. Constitution (Aufderheide 1999).

In 1985 domestic telecommunication companies sustained significant financial losses due to inconsistencies in accounting and billing procedures related to long distance and international calls. When the FCC was informed of these financial losses, it began negotiating with foreign telecommunication companies and facilitating long distance and international calling competition among domestic and foreign companies. Telecommunications monopolies in Britain and France responded by instituting privatization or liberalization in the mid-1980s (Sterling et al. 2006). Through the late 1980s, continual increases occurred in domestic telecommunications long distance competition and in discussions by regulators of reinstituting widespread competition in the telecommunications industry. Industry-government negotiations started the process of deregulation in 1985.

In the early 1990s, telecommunications innovation and expansion was becoming unavoidable. A broadly accessible communication service was evolving into what we now know as the internet and the World Wide Web. Initially, governmental regulations on industrial expansion impeded communications infrastructural development
(Aufderheide 1999; Sterling et al. 2006). In response, this industrial sector mobilized politically in order to promote expansion of services and profit making.

3.2 Changes in Corporations’ Political Embeddedness: The Telecommunications Act of 1996

In the early 1990s, incompatibilities emerged between the technical and economic realities of a digital industry and among regulatory laws that were based on analog technology (Horwitz 1989; Sterling et al. 2006). Corporate managers in large telecommunications companies maintained that regulatory requirements prevented them from expanding product lines and services and lobbied to change the political-legal arrangements in which the telecommunications industry was embedded.

In response, Congress enacted the Telecommunications Act of 1996, which transformed a largely monopolistic industry controlled by government regulation to an industry characterized by market competition and economic growth (Aufderheide 1999; Malik 2003; Sterling et al. 2006). The stated purpose of the Act was to “create a regulatory platform that would permit broad competition among different kinds of telecommunication service providers, encourage innovation, and recognize rapid technological change” while preserving the strength and vitality of an already established industrial sector (Aufderheide 1999: 8). In addition, the legislation was designed to create and encourage telecommunication competition on local scenes as well as in the stock market (Sterling et al. 2006).

The Telecommunications Act of 1996 enabled market expansion and competition in the industry while new technologies, such as the internet and World Wide
Web, created excitement and anticipation among executives and investors (Malik 2003). The Act brought many new small businesses into competition which increased demand for telecommunications hardware and services. Smaller retail companies sold the services of larger telecommunications corporations which allowed for expansion of the large corporations. The public demand in the late 1990s further enabled large companies to grow through mergers, acquisitions, and hostile takeovers (Malik 2003).

After the Act was passed by the Congress, corporate managers pushed company expansion and offered investment opportunities to new investors and company employees (Jeter 2003). With the enactment of the legislation, initial public offerings (IPO’s) were pursued at a record-setting pace by stock brokers, bankers, and Chief Executive Officers (CEOs) inside and outside of the telecommunications industry (Malik 2003).

This legislation was followed by record profits in the telecommunications industry. In addition, the market value of multiple companies sky-rocketed. Twenty-five year old billionaires were common at international telecommunications conferences (Malik 2003). Executives such as Bernard Ebbers of WorldCom and John Sidgemore of UUNet increased the industry’s market performance by over-stating levels of internet use, which stimulated further expansion by most telecommunication companies (Malik 2003). Ebbers and Sidgemore along with many other executives took every opportunity to exaggerate internet usage stating that “internet use was doubling every 100 days” (Malik 2003: xiv). The result was investors’ massive buying of stock in various telecommunications companies and an increase in the production of communication
hardware. In one quarter of 1997, WorldCom’s stock market value increased by 66 percent (Jeter 2003). Ebbers, Sidgemore, and other executives successfully created the great telecommunications myth - a perception of an endless demand for bandwidth. While Ebbers and Sidgemore created the myth, Wall Street analysts, notably Jack Grubman, successfully sold the myth to investors. Executives continued to profit from rising market values well into the decline of the industry.

The illusion of telecommunications growth was further emphasized through “flashing.” “Flashing” was a strategy used by telecommunications executives and sales managers (most popularly used within Qwest) which exaggerated the prices of sales within the corporation (Malik 2003). In press conferences, sales managers would casually announce or “flash” a $30,000 sale for $275,000. “Flashing” kept investors interested, although misinformed, in rapid growth as companies like Qwest scrambled to increase profits in any way possible.

The fiber-optics and internet boom and the subsequent market collapse of the telecommunications industry were results of opportunistic executives using insider information to bilk private investors (Malik 2003). During inflation of the internet and the fiber-optics bubble, executive managers purposely withheld vital financial information (i.e., value of company debt) and exaggerated the telecommunication industry’s rate of expansion. As a result, investors were misinformed or not informed about the dubious soundness of the telecommunications market (Malik 2003). Asymmetric information and executive autonomy created one-sided beneficial relationships between executives and investors. Although investors were confused by
new technologies, such as broadband, they continued to trust in Wall-Street analysts and executives and became more excited about industry expansion. The revolution of new technological products stirred public confidence.

An uninformed and inexperienced investing public was drawn into the telecommunications market that was made accessible by deregulation policies and initial public offerings (Aufderheide 1999). Regulatory bureaucracies were not sufficiently prepared for the rapid growth of telecommunications companies resulting in a lack of regulatory oversight (Aufderheide 1999). These historical conditions created opportunities for executives to take advantage of new technology, information asymmetries, market exuberance, and limited regulation to pursue their profit-making agendas with limited oversight or governmental interference.
4. HYPOTHESES

Researchers have been studying organizational crime for nearly a century (Sutherland 1940; Lane 1953). During this time, they have offered multiple explanations of corporate crime. An important sociological contribution toward understanding white-collar crime has been explanations of how differential social structures create dependencies, incentives, and opportunities to participate in financial malfeasance (Clinard and Yeager 1980; Tillman 2009; Prechel and Morris 2010). My thesis will build on Prechel and Morris’ (2010) research by incorporating individual-level variables with corporate characteristics. My objective is to augment and further explanations of financial malfeasance.

In this study, I use U.S. Securities and Exchange Commission (SEC) litigations against corporate financial wrongdoing as the dependent variable. The SEC is a federal regulatory bureaucracy primarily responsible for enforcing federal securities laws and regulating the securities industry. Its mission is to “protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation” (Securities and Exchange Commission 2011). By focusing on SEC litigation I narrow the broad definition of corporate crime. Companies report financial data to the SEC by financial statements. If the SEC determines there are discrepancies or suspects misrepresentation in the data, litigation is filed against the company. The SEC may also investigate a company’s financial records if they suspect illegal or unethical action. After Global Crossings went bankrupt in January 2002, the media began to scrutinize other large telecommunications companies. When the media began questioning executives at WorldCom, they were
informed that the SEC was already examining their financial statements. Legal action and financial investigation from the SEC followed, which resulted in various fines and disgorgements, prison sentences, and other penalties on the individuals held responsible. Prevalence of SEC litigation is a reliable and efficient indicator of financial malfeasance.

I selected the telecommunications industry to study because: (1) it has led the development of technological innovations and the transition into the information age since the 1990s, (2) the industry changed substantially due to changing governmental legislation, (3) in 2002, Fortune Magazine stated “the fall of telecom ranks as the biggest wreck in corporate history,” and (4) previous research has shown that industry-specific effects of financial malfeasance were statistically significant in the telecommunications industry (Prechel and Morris 2010). I test seven hypotheses based on organizational-political embeddedness theory, as it includes historical developments within the telecommunications industry.

4.1 Opportunities Hypothesis: The Multilayer-Subsidiary Form

In the 1980s the federal government passed legislation that allowed a change from the multi-divisional corporate form (i.e., various divisions are legally connected to one company) to the multilayer-subsidiary form (i.e., companies are legally independent from the parent company). This form created opportunities for companies to misrepresent financial data because the Tax Reform Act of 1986 allowed a parent company to make internal capital transfers between its subsidiaries (i.e., companies owned by the parent company) and the parent company (Boies and Prechel 2002;
Prechel and Morris 2010). This allowed the parent company to report revenue that might have been actually debt.

Boards of directors are charged with a variety of duties (i.e., monitor executive performance, ensure corporate growth, protect shareholder’s interest, etc.) (Monks and Minow 2004). One of the most important roles of the board is the regulation and oversight of executive and corporate action (Zahra and Pearce 1989). However, the efficacy and relevance of a board of directors’ governance has been scrutinized for over a century (Dwight 1907). Some researchers have even suggested that governance provided by boards of directors has been so poor in recent decades that corporations are in need of a different oversight structure (Mak 2009).

Early in the twentieth century, corporations in select states were permitted to change from a multi-divisional form to a holdings company form, which resembles the multilayer-subsidiary form outlined above (Prechel 2000). As corporate structure has changed, boards of directors have failed to adequately govern company action (Cohan 2002). The decentralized nature of the American corporate structure isolates the board of directors and filters information as it travels to the board room (Dwight 1907; Tashakori and Boulton 1983; Zahra and Pearce 1989; Cohan 2002). Mak (2009) states that as businesses expand into various sectors and industries, it becomes nearly impossible for boards of directors to fully comprehend and govern its actions. In the late 1990s the telecommunications corporations (i.e., Qwest, WorldCom, etc.) grew rapidly through mergers and acquisitions. With the continual increase in corporate size during those years, boards of directors experienced significant difficulties in governing the
actions of executives and the corporation as a whole. As a result, executives were able to make important financial decisions quickly without the board of directors being fully informed of the extent of the decision.

The multilayer-subsidiary form allows executives to bridge organizational gaps using information asymmetries to distort their companies’ financial. Telecommunications executives hid questionable financial transactions from the investing public and oversight agencies, and complex corporate structures alienated the board of directors from executive action. As the number of subsidiaries expands the corporate structure and increases corporate complexity. The more complex the corporation the easier it is for corporate executives to hide questionable financial transactions (Prechel and Morris 2010).

The hypothesis states:

$H_1$: In the telecommunications industry, companies with more subsidiaries have a higher likelihood of receiving SEC litigation than corporations with fewer subsidiaries.

4.2 Corporate Growth Hypothesis

Profit maximization is a necessary goal for all companies’ survival. However, other goals (i.e., corporate expansion) may take precedence over profit maximization depending on external constraints and varying historical circumstances. When profits are sufficient to satisfy expectations of shareholders, executives, and other prominent corporate individuals, a company may shift its main focus to acquisitions, increasing market share, or other forms of growth. A shift from profit maximization to company
expansion would be equally, if not additionally beneficial, to executive managers resulting in a taller managerial hierarchy, additional capital flow, bonuses and promotions among other company and individual benefits (Clinard and Yeager 1980).

Telecommunications companies grew significantly in the mid-1990s, announcing expansions costing up to $300 million for individual companies (Malik 2003). Rapid corporate growth has been associated with the commission of corporate crime (Clinard and Yeager 1980; Tillman and Pontell 1995; Prechel and Morris 2010). Evidence of this is seen in WorldCom, Qwest and other large telecommunications companies in the late-1990s (Malik 2003). When corporations or organizations expand rapidly, their executives and managers’ actions exceed the capacity of regulatory agencies to adequately monitor their activities (Tillman and Pontell 1995). Additionally, Clinard and Yeager (1980) suggest further that the size of a corporation increases the likelihood of financial malfeasance because taller managerial hierarchies in large corporations distance executive managers from illegal action giving them plausible deniability. Large telecommunications companies were not sufficiently regulated in the mid-1990s due to deregulatory acts and technological innovation. Corporate confusion resulted from lack of clarity about legalities and regulatory policies surrounding emerging technology. The industry required the attention of government regulatory officials, especially if ethical behavior was expected or assumed (Aufderheide 1999).

The hypotheses state:

\[ H_2: \text{ A positive relationship exists between a company's change in asset value and the likelihood that they will receive SEC litigation.} \]
A positive relationship exists between the size, measured in total assets, of telecommunications companies and the likelihood that they will receive SEC litigation.

4.3 Incentives: Executive Compensation Hypotheses

The majority of research conducted on executive compensation attempts to explain relationships and discrepancies between the amount executives earn and prior years of company performance (Jensen and Murphy 1990; Boyer 2010). My thesis incorporates executive compensation variables, along with previously tested causal factors of organizational crime, in an attempt to identify relationships between executive compensation and organizational crime.

Financial incentives have increased rapidly over the past few decades. They have jumped from approximately 100 times the average worker’s pay in 1990 to between 350 and 570 times currently in the United States (Harris and Bromiley 2007). For this reason, CEO’s annual incomes have been scrutinized by all forms of media since the early 1990s. Executives were criticized by economists, politicians, and shareholders because no explanation was given as to why a CEOs annual income increased so much when profits and shareholder value remained static or decreased from the previous years (Monks and Minow 2004). For example, Monks and Minow (2004) state that the annual income of Rand Araskog, CEO of International Telephone & Telegraph (ITT), increased 103 percent in 1991 as shareholders watched the company’s market value decrease by 18 percent.

In the mid-2000s, CEOs were criticized for being awarded large bonuses with government bailout monies or taxpayer dollars. Endthebailouts.com states that 86
percent of the $125 billion dollars given to investment banks in 2008 was used for executive bonuses (Green 2008). These controversial actions by executives cast doubt to the legal and ethical appropriateness of executive behavior. However, contrary to the popular focus given by the media, i.e., how much a CEO is paid, diverts attention from the real problem of executive compensation – how executives are paid (Jensen and Murphy 1990).

While in some corporations executive salaries and bonuses are substantial, the majority of cash in an executive compensation package comes from bonuses, stockholdings, and stock options (Jensen and Murphy 1990). The value of executive stock can be valued up to nearly 20 times the base salary (Harris and Bromiley 2007). Towers Perrin, a financial consulting company, found that the average value of stock options awarded to CEOs had doubled between the mid-1980s and mid-1990s (Monks and Minow 2004). More than 71 percent of firms offer stock options as a part of the compensation packages in an attempt to (1) align the goal of profit maximization between the executives and the shareholders, (2) encourage executives to behave more like owners, and (3) strengthen the link between pay and performance (Monks and Minow 2004). Increased profits, then, result in increased cash from stockholdings and options for shareholders and executives.

Executives maximize profits from stock options only if market value of their company is increased before the option is exercised. When executive managers are unable to maximize market value and company profits, the value of the compensation package and their job security is at risk. When executives fail to maximize corporate
profits, shareholders may want to change executives’ compensation plan so that it will vary respectively with the company’s market performance (Monks and Minow 2004). However, the growing trend of “mega-grants” has practically eliminated return risk and uncertainty for executives. A mega-grant is any equity grant that exceeds 500,000 stock options (Barr 2009). Mega-grants are becoming more popular in large corporations while economists view them as having conflicting results in regard to executive performance (Jensen and Murphy 1990). Additionally, research results identifying a relationship between mega-grants and financial malfeasance are insufficient.

While the award of a large amount of shares nearly guarantees a cash return to executives, it also encourages as a more direct incentive the increase of market value (Jensen and Murphy 1990; Monks and Minow 2004; Harris and Bromiley 2007). A compensation analysis by Jensen and Murphy (1990) states that CEO salary is affected minimally by company growth and increased market value. Their analysis of 250 executive compensation packages yields that for every $1,000 change in shareholder value a CEO should expect to receive a 3.3 cent change in salary and bonus. However, for the same increase in corporate market value an executive will see, on average, a 14.4 cent change in exercised stockholdings. To illustrate, according to Jensen and Murphy (1990) if a CEO’s annual salary is two-million dollars, his or her salary will increase $66,000 (2,000,000*.033), for every $1,000 increase the corporation’s in market value. At the same time, a share worth $50 can be expected to increase to $57.20 dollars (50*.144) with the same $1,000 increase in market value. Subsequently, a CEO who owns 500,000 shares would expect a $3,600,000 increase (500,000*7.20) in the value of
the exercised shares, excluding options. Therefore, I focus on stock options because the change in payout to executives is significantly more than the change in salary and bonus value.

The increase in stockholdings may create enough CEO incentive to maximize corporate profits. When executives are awarded with large amounts of stock and stock options, the return is more directly affected by their actions and performance. Therefore, a positive relationship exists between the number of shares owned and rate of cash return, thus more directly aligning the profit maximization goals of executives and shareholders (Monks and Minow 2004). The mega-grant, then, ensures that an increase in corporate value will largely profit executives.

As discussed above, large portions of an executive managers’ compensation package lie in a profit-shared plan. This plan directly associates executive compensation with the overall financial progress and market value of the corporation. By connecting executive pay to market stock value growth an incentive is created to raise or inflate the overall worth of the company. Such inflation results in higher dividends to shareholders and shareholding executives. While there are legitimate means to attain market growth, financial constraints are felt by executives in times of economic uncertainty. These constraints create an incentive to illegitimately inflate a corporation’s financial data for subsequent personal financial gain (Varian 2002).

The hypothesis states:
\( H_4: \) A positive relationship exists between the value in dollars of options exercised by telecommunication executives and the likelihood of receiving SEC litigation.

Recent research suggests a positive relationship exists between strategies used to increase share value and corporate malfeasance (Prechel and Morris 2010). When legitimate action to increase share value does not result in a desired financial outcome, executive managers might use unethical and/or illegal action. “Failure to increase shareholder value may cause investors to divest from the company, withhold future investments, and/or attempt to replace top management” (Prechel and Morris 2010: 333). Although shareholders may not be able to maximize corporate profits, executives, on the other hand, can utilize multiple strategies to raise market value in an attempt to increase share profit to shareholders.

The hypothesis states:

\( H_5: \) A negative relationship exists between earnings per share and the likelihood of a telecommunications company receiving SEC litigation.

4.4 Political Involvement Hypothesis

Political Action Committees (PAC’s) have become increasingly important in corporate and political policy. The involvement of corporate monies in governmental policy enactment and enforcement increases corporate opportunities to engage in buffering: strategies used to reduce the effects of political-legal arrangements within corporations (Prechel and Morris 2010). PAC’s allow corporations to access government officials who are influenced to push deregulatory policies and weaken
oversight bureaucracies, among other actions that would benefit a company or industry. A lack of oversight allows a company to act autonomously and create opportunities for financial malfeasance.

The hypothesis states:

\[ H_5: \text{A positive association exists between the amount of monies telecommunications companies contribute to PACs and the likelihood of receiving SEC litigation.} \]
5. RESEARCH DESIGN

5.1 Sample

The data set includes the largest publically traded U.S. telecommunications companies as identified in Fortune magazine’s list of 500 largest U.S. publicly traded parent companies in 2002. In this study, cases are company-years. Thus, for each company, all data are separated in annual increments for the duration of the time period of study. The dataset includes twenty-one companies. The time period of study begins in 1995 and ends in 2004 resulting in 115 company-years. The choice of time period also gives telecommunications management sufficient time to respond to the Sarbanes-Oxley Act of 2001. The Sarbanes-Oxley Act requires CEOs and CFOs to sign financial statements personally attesting to the validity and accuracy of a company’s financial statements’ contents. The Act was passed after public demand for governmental oversight increased after a series of corporate scandals, many of which occurred in the telecommunications industry. The Act was an attempt to ensure the financial accountability and transparency of corporations (Bing 2007). Financial transparency means the full disclosure of financial action must be made on corporate balance sheets. Transparency is achieved when corporations adhere to the Generally Accepted Accounting Principles (GAAP). Sarbanes-Oxley also created incentives for executive managers to adhere to financial regulations because the penalties for knowingly or willfully submitting falsified statements were increased up to 20 years of imprisonment with the possibilities of a fine as well (Sarbanes Oxley Act of 2002). Additionally, if a company is required to restate its financial data due to misconduct, its executives may be...
forced to give up bonuses or profits gained from selling their shares. These penalties limit the risk of misreporting because they provide sufficient motivation to restate any previous misleading financial data.

The year 2001 is used as the sample selection year because corporations are likely to have altered their behavior after Sarbanes-Oxley was passed. Also, several corporations that engaged in financial malfeasance (e.g., Enron, Tyco and WorldCom) were eliminated from the Fortune 500 after that year (Prechel and Morris 2010).

Nevertheless, several corporations were excluded from Fortune’s list because they are partnerships, private companies, or subsidiaries of foreign companies. Partnerships and privately owned companies were excluded because they are not required to adhere to the same financial disclosure requirements as publicly traded companies. Foreign corporations’ subsidiaries were excluded because the holding or parent company must adhere to the financial requirements and political-legal arrangements in the varying countries in which they are located. Companies who had merged were identified by the company which took managerial control, while companies which went private were excluded from the dataset.

5.2 SEC Litigation: A Dependent Variable

I focus on financial accuracy and transparency through SEC litigations as the dependent variable. By using SEC litigation as a dependent variable I am able to focus specifically on financial misconduct. Publically traded companies are required to submit financial data annually to the SEC. These data are also made available to investors so they may make informed investment decisions of the overall financial health and
strength of the company (Tillman 2009). If those financial data are purposefully inaccurate or other unethical relationships have benefited the company and are not disclosed, the SEC will take legal action, known as litigation.

SEC litigation is a dummy variable measuring whether or not a corporation received litigation in a given year. It is coded: “1” if the company did receive litigation and “0” if not. The data of whether or not the company received SEC litigation data were obtained by Prechel and Morris (2010) from SEC documentation. I use a dummy of SEC litigations instead of total number of litigations because researchers have shown that the first malfeasance event is the most important (Clinard and Yeager 1980). This does not assume, however, that all first incidences of malfeasance are equal in severity.

5.3 Independent Variables

The corporate structure variable measures how many companies are nested in the second level of the multi-layer subsidiary form (i.e., structured with the parent company acting as primary share holder financial operator of legally separate subsidiary companies nested within the parent company). I use these data instead of a dummy variable of corporate structure because 98 percent of the telecommunications companies were structured in the multilayer-subsidiary form in the time period of study. Using a dummy variable, therefore, results in perfect association in the analysis. These data were collected from Dun & Bradstreet (1995 to 2004), the SEC, and various corporations’ web sites (Prechel and Morris 2010).

Measures of corporate financial characteristics between the years 1995 and 2004 were collected by Prechel and Morris (2010) from the Compustat dataset. I measure
change in asset value change as total assets from the previous year and measure the corporation’s size as the natural log of the company’s total assets.

Earnings per share is measured before expenses for extraordinary items and discontinued operations are deducted. Executive compensation is measured as the value, in U.S. dollars, of the exercised shares awarded to a CEO. The value is reported by multiplying the number of exercised options by the share price at the end of a calendar year.

I measure political activity by the amount of U.S. dollars parent companies and their subsidiaries contributed to political action committees between 1995 and 2004, in thousands of dollars. These data were collected by the firm Open Secrets, which compiles data acquired from the Federal Election Commission.

I use additional variables which have been identified as causal indicators of organizational crime as control variables in my study. Previous research shows a company’s age, measured in years, has been correlated with corporate crime (Tillman and Pontell 1995; Crutchely et al. 2007) and is used as a control variable. These data are available from Dun and Bradstreet and corporate websites. Additionally, capital dependence on banks affects corporate behavior (Prechel 2000). Therefore, rate of return on equity, or profits, is measured in percent rate of return and was obtained from the Compustat database.

5.4 Estimation

For the quantitative analysis, I use a logit model for discrete-time event history analysis. An events-history analysis allows me to incorporate time sensitive variables
(company-year units) to account for the probability of event occurrence\(^1\) (Zhou and Hou 1999). The logit analysis is appropriate because the dependent variable, SEC litigation, is a binary variable. The multivariate logit regression allows me to determine the probability that a company with particular characteristics or underlying conditions would have received SEC litigation. I used the VIF command in Stata, to identify issues with multi-collinearity.

\(^1\) For a more detailed explanation of the logit model for discrete-time event history analysis, see Zhou and Hou (1999).
6. FINDINGS

The descriptive statistics are presented in Table 1. Because I analyze a panel dataset, the unit of analysis is a company-year. In the 115 company-years, various companies received SEC litigation in 11 percent on the company-years. Additionally, six of the twenty-one of the companies involved received SEC litigation, some received up to 11 litigations in one year. Because the telecommunications companies in the sample come from Fortune’s list of the 500 largest companies, the potential impact of these litigations is substantial for the investing public.

Ninety-two percent of the companies in the time period of this study are structured in the multilayer-subsidiary form and the average number of second-level subsidiary companies is 38. The mean rate of total asset growth is -6.01 percent and the log-value of total assets is 9.81. The average value of exercised stock options is $6,830,114. The mean earnings per share is $.42 and the mean contribution to political action committees is $419,030. Finally, the mean age of the companies is 32.7 years and the mean return on equity is -$38.20.

Table 2 presents the multivariate findings. Coefficients in Table 2 represent the likelihood that an SEC litigation would occur. I also present several coefficients as the
percent change in the odds ratio, which is calculated by subtracting 1 from the antilog \( e \) to the power of the logit coefficient multiplied by 100 \((\Omega-1\times100)\).

Model 1 examines seven variables regarding corporate structure and financial characteristics. There are two important findings in this model. The first is that the value of a company’s total assets increases the likelihood that a company would receive SEC litigation. For every one unit increase in the natural log of total assets, the likelihood of that company receiving SEC litigation increases by 355 percent \([e^{1.393} - 1] \times 100\]. Larger companies are more likely to engage in risky capital activity because they have the power and financial resources to survive the potential economic loss (Morris 2005). Further, risky financial investments carry the probability of financial loss and increase the likelihood of participating in illegal or unethical transactions. This finding supports existing literature on size as a causal indicator of financial malfeasance, and supports Hypothesis 3.
The second important finding is the coefficient of the earnings per share variable.

The concept of shareholder value is based on the assumption that when executives are compensated in profit-shared plans (i.e., stock options), an incentive is created to act in the interest of the shareholders or owners and not engage in unethical or illegal behavior.

In agreement with the theory, I hypothesized that the coefficient of earnings per share would be negatively correlated with SEC litigation and statistically significant. I found,
Table 2. Coefficients and Standard Errors for Predictors of Securities and Exchange Commission Litigation

<table>
<thead>
<tr>
<th>Variables</th>
<th>Model 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-18.472**</td>
</tr>
<tr>
<td></td>
<td>(-7.516)</td>
</tr>
<tr>
<td>Corporate Characteristics</td>
<td></td>
</tr>
<tr>
<td>Number of level-two Subsidiaries</td>
<td>-0.004</td>
</tr>
<tr>
<td></td>
<td>(.013)</td>
</tr>
<tr>
<td>Total Asset Growth</td>
<td>.003</td>
</tr>
<tr>
<td></td>
<td>(.003)</td>
</tr>
<tr>
<td>Total Assets</td>
<td>1.393*</td>
</tr>
<tr>
<td></td>
<td>(.709)</td>
</tr>
<tr>
<td>Financial Characteristics</td>
<td></td>
</tr>
<tr>
<td>Earnings Per Share</td>
<td>-0.113</td>
</tr>
<tr>
<td></td>
<td>(.153)</td>
</tr>
<tr>
<td>Control Variables</td>
<td></td>
</tr>
<tr>
<td>Company Age</td>
<td>-0.009</td>
</tr>
<tr>
<td></td>
<td>(.035)</td>
</tr>
<tr>
<td>Return on Equity</td>
<td>0.018</td>
</tr>
<tr>
<td></td>
<td>(0.039)</td>
</tr>
<tr>
<td>N of Companies</td>
<td>21</td>
</tr>
<tr>
<td>N of Company Years</td>
<td>115</td>
</tr>
<tr>
<td>Likelihood Ratio $\chi^2$</td>
<td>0.381</td>
</tr>
<tr>
<td>$\chi^2$ Goodness of Fit Ratio</td>
<td>6.39</td>
</tr>
</tbody>
</table>

*p < .05; **p < .001 (two-tailed test)
however, earnings per share, although negatively correlated, is not statistically significant on whether or not the company received SEC litigation. In the telecommunications industry, earnings per share does not influence the likelihood of participating in illegal or unethical activity. This result does not support Hypothesis 5.

The remaining results in Table 2 indicate that the multilayer-subsidiary form and total growth in assets are not significant indicators of whether or not a telecommunications company received SEC litigation during the time period of study. These results do not support Hypotheses 1 and 2.

When data on executive compensation and PAC contributions are added into the multivariate analysis presented in Table 2, the number of company-years declines from 115 to 61. I examined the data and discovered that there is a substantial amount of missing data on the executive compensation variable.\(^2\) When I remove the executive compensation variable and let the PAC contributions variable remain in the equation, the number of company-years falls below 100, which jeopardizes the accuracy of the model. The low number of company-years does not yield reliable findings for these two variables when they are included in the multivariate analysis. Consequently, I conduct two one-tailed t-test analyses to determine whether or not these data are significant indicators of receiving SEC litigation. These data are presented in Tables 3 and 4.

\(^2\) The majority of missing data belongs to corporations who were involved in SEC litigation and Department of Justice (DOJ) proceedings (i.e., WorldCom, Adelphia, Sprint, Qwest, etc.). I contacted the SEC and was informed that if there are still pending arrangements with the DOJ these data would not have been made available to the public.
Table 3. T-test for Value of Stock Options on SEC litigation

<table>
<thead>
<tr>
<th></th>
<th>t-score</th>
<th>t-critical (one-tail; p &lt; .05)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value of Exercised Stock Options</td>
<td>1.06</td>
<td>1.66</td>
</tr>
<tr>
<td>Means</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Received Litigation</td>
<td>13,459.21</td>
<td></td>
</tr>
<tr>
<td>No litigation received</td>
<td>6,114.35</td>
<td></td>
</tr>
<tr>
<td>Difference in Means</td>
<td>-7,314.86</td>
<td></td>
</tr>
<tr>
<td>Degrees of Freedom</td>
<td>94</td>
<td></td>
</tr>
</tbody>
</table>

* p < .05 (One-tail test)

The results indicate whether or not the value of exercise stock options and PAC contributions are significantly different between those companies which received SEC litigation and those that did not. Statistically significant differences would justify the collection of these data unreported by other companies.

Table 3 indicates that the t-score of 1.06 for the value of exercised stock offerings does exceed critical t-value area, 1.66, with 94 degrees of freedom. The respective difference of means of the companies that did and did not receive SEC litigation are not significant. These data do not support Hypothesis 4.

Table 4 indicates that the amount of PAC contributions is not a significant indicator of the likelihood that a telecommunications company received SEC litigation during the time period of study. The t-score of .73 does not exceed the critical t-value of 1.65 with 128 degrees of freedom. Although the data for this variable do not result in
Table 4. T-test for PAC Contribution on SEC Litigation

<table>
<thead>
<tr>
<th></th>
<th>t-score</th>
<th>t-critical (one-tail; p &lt; .05)</th>
</tr>
</thead>
<tbody>
<tr>
<td>PAC Total Contributions</td>
<td>0.731</td>
<td>1.66</td>
</tr>
<tr>
<td>Means</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Received Litigation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>No litigation received</td>
<td>494,780.10</td>
<td></td>
</tr>
<tr>
<td>Difference in Means</td>
<td>407,638.70</td>
<td></td>
</tr>
<tr>
<td></td>
<td>-87,141.40</td>
<td></td>
</tr>
<tr>
<td>Degrees of Freedom</td>
<td>128</td>
<td></td>
</tr>
</tbody>
</table>

* p < .05 (One-tail test)

statistical significance among telecommunications companies between 1995 and 2004, it is interesting to note that every company contributed PAC monies in every year of the study period. These data do not support Hypothesis 6.
7. CONCLUSIONS

The statistical analysis yields mixed findings in the research of financial malfeasance. The telecommunication industry underwent substantial change in the late 1990s and early 2000s. The Telecommunications Act of 1996 revolutionized the structure of the industry and had substantial effects on the relationships within telecommunications and multiple other industries (Malik 2003). The data analyzed in this thesis are not comprehensive of the affects produced by the Telecommunications Act of 1996 on the U.S. economy. The Telecommunications Act of 1996 allowed executive managers to act with limited regulatory oversight which enabled companies to grow rapidly and executives to create financial contracts through asymmetric information (Aufderheide 1999; Malik 2003). Because of the rapid increase of stock prices in 1998 and 1999, executives falsely reported growing revenues to match rising market values. The complexity of the post-Act telecommunications industry enabled executives to falsify financial data with little regulatory oversight.

Organizational-political embeddedness theory suggests that historical conditions influence executive action. Industry-wide problems in telecommunications existed between 1996 and 2003. Reliable and valid conclusions about this industry require identifying how historical conditions influenced corporate behavior. As a result of legislation changes, multiple companies declared bankruptcy, various malfeasant activities occurred, many of which resulted in prison sentences, fines, and removal of executive officers in several telecommunications companies (Jeter 2003; Malik 2003).
The Telecommunications Act of 1996 offers important insight for politicians pushing for deregulation and pro-business policies. Ultimately, the lack of regulatory oversight gave executive managers too much autonomy in an industry fueled by greed (Aufderheide 1999). Some executives were not concerned with increasing shareholder value to please investors, but, instead, were concerned with protecting themselves anyway they could especially when the industry began to fail (Malik 2003). The Act was supposed to increase public confidence and investment in the industry. Instead, the post-Act unethical and illegal actions of corporate executives weakened investor confidence that were made vulnerable to risky financial actions due to asymmetric information form telecommunication executives.

Prechel and Morris’ (2010) argument of corporate structure yields important conclusions in the literature of corporate malfeasance. They demonstrate that companies structured in the multilayer-subsidiary form are more likely to engage in financial malfeasance. This finding is very important in my study as 92 percent of telecommunications companies are structured in the multi-layer subsidiary form. Additionally, my findings differ from Prechel and Morris’ (2010) because their article focuses on financial restatements as a dependent variable while I focus on SEC litigation as a dependent variable. I also use a different measure of multilayer-subsidiary form because within the telecommunications industry 98 percent of companies involved were structured in this form. Using a dummy variable to identify corporate structure resulted in perfect association in the quantitative analysis.
The data provided in this thesis are insufficient to yield any statistically significant findings of the influence executive compensation might have had on financial malfeasance in telecommunications companies between 1995 and 2004. Due to the number of missing cases I am unable to state definitive conclusions that executive compensation may or may not be a significant indicator of corporate malfeasance in the telecommunications industry. Efforts to collect these data are being made in extending this research in the future.

Nevertheless, organizational-political embeddedness theory still has usefulness in explaining corporate and executive behaviors. The Telecommunications Act of 1996 had significant consequences on the health of the telecommunications industry and market. The theory and the research demonstrate that there were increased levels of executive autonomy due to the limited resources and efficacy of regulatory bureaucracies. Whether or not awards in stock options to executives increased the likelihood of financial malfeasance within the telecommunications industry between 1995 and 2004 has yet to be determined with statistical significance. The executive compensation package is very complex and additional study and research is warranted before definitive conclusions can be made on how it influences illegal or unethical behavior.

This thesis is a starting point and a call for future research in the telecommunications industry and understanding the causes of corporate crime. While significant research has been done examining the effectiveness of the board of directors, much of this research has been oriented toward furthering understanding financial
growth, not regulating corporate action. The widespread malfeasance that occurred in the early 2000s in corporations like Enron, WorldCom, and Tyco warrants further research on the effectiveness of oversight abilities within the board of directors. However, the failed oversight of large companies does not rest solely on the board of directors. Governmental bureaucracies have been charged with maintaining fair, orderly, and efficient markets for investors. The efficacy of these bureaucracies must be increased in order to protect the investing public. Laws and regulations calling for increased financial transparency within corporations will allow regulators to be more effective in their work. By strengthening oversight agencies (i.e., the SEC) and laws and penalties for corporations (i.e., the Sarbanes-Oxley Act), corporate managers may increase individual and corporate focus on ethical and legal behavior. Such behavior will increase public confidence and promote stable growth within financial markets.

The continuation of this research project would focus on the efficiency of internal and external corporate regulation. Some studies have examined characteristics of executives and focused on greed as a fatal flaw in corporate America (Gray et. al 2005; Simon 2008). However, executives are under significant pressures to maximize profits. It is then up to the regulatory organizations (i.e., the SEC and the board of directors) to monitor corporate activity. The efficacy of corporate governance continues to be an important area of political and economic research and is necessary to restore economic stability and facilitate continuous economic growth.
7.1 Funding

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