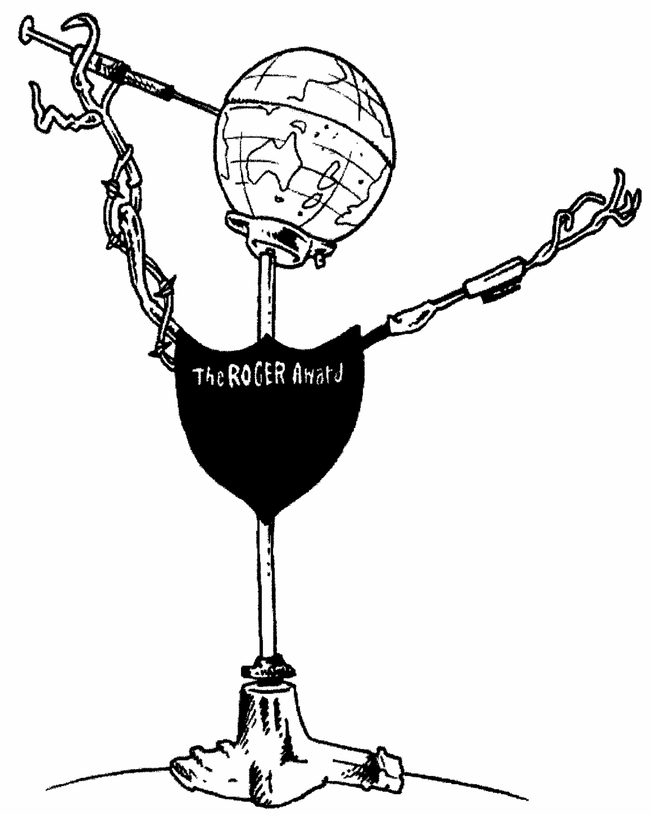
Roger Award 2004

For the worst Transnational Corporation operating in Aotearoa in 2004



Winner
Telecom

Organised by
Campaign Against Foreign Control of Aotearoa (CAFCA)
GATT Watchdog

STATEMENT FROM THE JUDGES
April 2005

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Introduction

There are seven finalists for the Roger Award for the worst transnational corporation operating in Aotearoa/New Zealand in 2004. These finalists in alphabetical order are: Contact Energy, Ernslaw One, McDonalds, Mitsubishi, Telecom, Toll Holdings and Westpac.

The judges' task was to consider the activities of these seven corporations against the criteria for the award which cover areas such as unemployment, abuse of workers, profiteering, political interference, cultural imperialism, and negative impacts on tangata whenua, women, and the environment.

We thank those who entered nominations – some companies received several – and for the time and effort they made to develop detailed and comprehensive background material as evidence to justify each nomination.

In the judges' view each of the finalists exhibits policies and practices which are well outside the behaviour our community has a right to expect from any company operating in New Zealand. Unfortunately, as with past years, it was a particularly strong field of candidates and it is unfortunate also perhaps that there can be only one winner! In their own unique ways each of the finalists deserves the denunciation of the community.

Government Protection

In reading through the evidence against each company however, what struck the judges was not just the nastiness of the companies' practices but the lack of government action to curb their worst excesses. It seemed clear that if we were to have a government focussed on the protection of people and the environment, rather than on protecting corporate profit making then there may be no need for the Roger Award.

For this reason the judges would like to issue a special award to the government. This award is entitled the "**Special Roger Award for Protection of Profit and Privilege"** and is awarded to the Prime Minister on behalf of the government. The reasons for this award will become evident as we describe the activities of the nominee companies.

The Decision

This judges' decision ranks the "Top Four" companies but, before doing so, we would like to comment on the three other companies whose practices and policies appalled the judges and justified their nominations.

The three multinationals which missed the final four places are:

Mitsubishi

In 2004 Mitsubishi Motors in Japan acknowledged that it systematically covered up defects in its vehicles. Despite recalls of vehicles in Japan, Mitsubishi in New Zealand made no effort to find out the problems and arrange recalls here in New Zealand. This was left to the Land Transport Safety Authority which recalled hundreds of Mitsubishi buses – including school buses – and cars in June last year for urgent safety checks and repairs.

Mitsubishi in New Zealand initially refused to pay the full cost of repairs and only agreed to do so when community pressure meant it thought its "brand" might be adversely affected.

In this way Mitsubishi avoided its safety responsibilities and put New Zealanders lives at risk. It fully deserved its Roger nomination.

Toll Holdings

Toll Holdings is the successor to Tranz Rail and immediately gained a nomination in its first year in New Zealand!

In the space of a single week Toll challenged the right of Auckland rail workers to remain under their existing collective agreement and created a storm on the ferries with unilateral changes to rosters before the collective agreement had even expired. This Australian based corporation has displayed an absolute contempt for New Zealand workers.

Toll were also in negotiations with the government last year after Tranz Rail bailed out on what was left of our rail network after a decade of private ownership and undisguised neglect. Naturally Toll has established a deal which will ensure they can tap into large profits in New Zealand at taxpayers expense. This the judges felt was entirely the fault of the New Zealand government which should have re-nationalised the entire rail network along with the management of this community resource. Rail operations should run as an income earning service for the community rather than as a cherry-picking opportunity for yet another private profit seeker.

Toll's behaviour was appalling and it deserved its nomination but the government acquiescence was gutless and embarrassing.

Westpac

New Zealand has the highest degree of foreign bank ownership in the world – 99% of assets are in foreign owned banks with 85% of that in Australian banks. These foreign banks - of which Westpac is one - are creaming big fat profits from New Zealand. In the year to 31 October 2004 they made a combined profit of $2 billion. At the same time Reserve Bank figures show that the banks are paying an effective tax rate of just 6.7% when the normal corporate rate is 33%. Finance Minister Michael Cullen described it as a "legitimate form of tax avoidance!" Tell that to our cash-strapped schools!

In the case of Westpac it does not release accounts for its NZ operations so we can't be sure if they pay even the trivial rate of the other banks…

Meanwhile Westpac's share of the banking profit from New Zealand amounted to $617million – a 36% increase on the previous year.

The banks were in the news in 2004 for their outrageous and unjustifiable charges added to international credit card transactions.

What distinguishes Westpac from the other banks however is that it is the only bank which is run as a branch from Australia. This exposes New Zealand depositors to higher risk as a bank collapse would inevitably mean Australian creditors being paid out first using New Zealand money! The same could well apply to staff cuts. When the bank lays off staff it will most likely do so in New Zealand before Australia since the trend is towards greater centralisation of services when staff cuts are made.

The judges felt that poor regulation of banks and little attention to their activities by the government deserved sharp criticism alongside the well deserved nomination of Westpac itself as a representative of a such a grim bunch of foreign racketeers!

The "Top Four"

The "Top Four" companies follow in order of the judges decision – beginning at the bottom and them working our way down!

McDonalds

4th place getter was McDonalds.
The judges were appalled at the extent to which McDonalds fits the Roger Award categories. McDonalds involves -

- high stress, low pay, low security employment
- serious political interference through its advertorial funding of dentistry in poorer communities – the Far North – and its insidious placement of food outlets in hospitals. This demonstrates an unhealthy political influence with area health boards etc
- environmental damage – through production of massive amounts of unrecyclable wrappings and the resultant littering
- "cultural imperialism" through their efforts to destroy small food businesses and food diversity. They exhibit a "US centred-ness" in their operational practices rather than acting like a New Zealand enterprise.
- high fat and high sugar foods impacting on community health in negative ways – in relation to low income communities particularly.

This company has rightly become an international symbol of low quality, large volume fast food and its multi-million dollar campaigns – paid for by its customers – to buy its way into community favour. McDonalds was a strong finalist for this award.

Ernslaw One

3rd place getter is Ernslaw One. Ernslaw One has forestry and milling operations in New Zealand. It scored highly on abuse of workers, environmental damage and cultural imperialism.

This company is an offshoot of the gargantuan Asian logging company Rimbunan Hijau, owned by the Tiong family of Malaysia. Rimbunan Hijau is well known throughout Asia for its abuse of sustainable logging practices and massive environmental damage. Ernslaw One's clear felling practices here are entirely in keeping with their overseas activities.

Here in New Zealand Ernslaw One is having a big impact on workers – Maori on the East Coast especially – with thousands of job losses projected. These East Coast forestry workers have managed to stave off massive jobs cuts – one third of the workforce was to be scrapped - in the short term by a campaign of united action in the face of this ruthless multinational.

Ernslaw One also scored highly for its impact on health and safety of the public - based on their proposal for a saw milling complex near Whangapoua Harbour. Waste discharges from large saw milling operations are generally harmful to public health.

It is difficult to separate its impact here from its impact on Papua New Guinea and all the other countries where it is active. The judges expressed their support for the PNG communities and Greenpeace campaign against Rimbunan Hijau. (One of the judges had met independently with PNG activists last year and seen barely believable pictures of the destruction caused by the company's operations)

Throughout Asia Rimbunan Hijau is associated with illegal logging and theft of natural resources. To its credit the New Zealand Timber Importers Association expelled Lumberbank – a wholly owned subsidiary of Ernslaw One – from the NZTIA for breaking rules concerning importing illegal timber into New Zealand.

Rimbunan Hijau and its subsidiaries are a nasty bunch wherever they operate. They have no place in New Zealand. Nor anywhere else!

Contact

The runner up to the Roger Award winner for 2004 is Contact Energy. Contact was nominated for its vociferous opposition to the Kyoto Treaty (formerly the Kyoto protocol) - a treaty important to life on the planet. The judges were convinced on the evidence that Contact has run an ideological campaign against Kyoto and the use of renewable energy sources. For example they have spent some $2million running a crusade to convince the public that coal-fired power stations are the only option for a secure future energy supply. This is in sharp contrast to its lack of investment in education on the impact of coal-fired electricity generation. Their aim is to control the direction and define the terms of the national debate over sustainable uses of energy.

It has demonstrated strong lobbying power with the government and has consistently dictated to the Taranaki Regional Council what it expects from what should be a responsible community watchdog.

Contact was also in the news in 2004 for the lies it told customers about the need for price rises for electricity. No less that 8,250 customers were involved! It blamed increases in electricity prices on increased charges from the lines companies when in fact the line charges had *decreased.* This resulted in a prosecution under the Fair Trading Act and a settlement award made against Contact.

The evidence viewed by the judges also exposes Contact as responsible for environmental damage and wilful negligence regarding health and safety of the community. These conclusions came from the impact of Contact's existing operations on the Waikato river, its apparent lack of concern about how its newly converted oil-fired power station will impact on the health of nearby New Plymouth residents, as well as the global impact of its CO_2 emissions.

The judges were not convinced of Contacts claims of no responsibility for the land subsidences occurring around the Wairakei area and were alarmed at its plans to increase geothermal extraction.

Contact should be ashamed of its appalling record in 2004.

Telecom

You will realise now by a process of elimination that the winner of the Roger Award for 2004 is Telecom.

The massive profit figures which this company posts year by year are a national scandal.

Last year this company made another massive profit which amounts to $188 for every man, woman and child living in New Zealand. This is staggering. The $750 million involved should be in the community coffers but instead is in the back pockets and under the control of wealthy foreign and local shareholders.

Telecom is given free rein by the government to set their own operating rules and pricing structure as an effective monopoly over much of New Zealand's telecommunications industry. Because of their dominance of the New Zealand sharemarket the government kow-tows to them as if their economic health rests the economic health of the sharemarket!

This is a company whose name is a byword for the failure of privatisation. It is the largest community parasite in New Zealand and its stifling, negative impact cannot be underestimated.

Despite the massive profits the true community colour of Telecom comes through with its impact on low income communities. For example it refuses to reduce charges for not-for-profit organisations - including those with charitable status. This has a negative impact on all community groups such as those working with youth, Maori and women.

Their real "community concern" is emphasised with a quick look at their "me-first" sponsorship criteria.

Last year the Roger judges gave a **"Special Award for Monopoly Profiteering"** to Telecom. In making the award the judges commented –

> *"Factors in this award include their monopoly of telephone lines; outrageous charges to competitors to interconnect; exorbitant charges to rural customers; a 15% hike in line rentals; misleading advertising to lure customers from competitors; boosting non-regulated wiring maintenance costs as part of residential bills; bringing the billing cycle forward a week; and disconnecting 8000 customers without warning at the very end of 2002"*

The same practices outlined a year ago were also evident throughout 2004.

The company's fleecing of New Zealanders stands in sharp contrast to the obscene salary of $2.82 million paid to CEO Theresa Gattung. She now receives weekly earnings of $53,270 – earning more in a single week than the average New Zealand earns in an entire year.

Telecom has betrayed the trust and hopes placed in it to run our telephone and telecommunications systems. It is a New Zealand made disaster rather than an imported one and has been allowed to run unchecked for 15 years.

This is a friendless, rapacious company with well established and unmediated parasitical practices.

Telecom is a worthy winner of the Roger Award for 2004.

The Roger award is more necessary than ever, in light of the new Overseas Investment Bill which will make transnational corporate takeover of New Zealand that much easier. Reviewing the finalists for the 2004 Roger Award reminds us of the huge crime perpetrated on the people of New Zealand by a system that permits our country to be converted into a backwater branch office of the corporations that rule the world.
Murray Horton (CAFCA)

Roger Award 2004 Report

On the nature of business

Don Polly

These seven Roger Award finalists have much in common, as do all the nominees. They all are repeat offenders; amoral exploiters of everyone and everything in their headlong rush to profit and they all go well beyond the expectations of local acceptable business practice (whatever that is) even for foreign transnational corporations.

They also have a curious sense of righteous indignation when confronted with the effects of their destructive behaviour.

Some would say it's in the nature of things business. And they're probably right.

So the judges' comments about "the lack of government action to curb their worst excesses" may be obvious, but it needs repeating. If New Zealand had "a government focused on the protection of people and the environment, rather than on protecting corporate profit… there may be no need for the Roger Award."

Which, of course, makes this year's long-overdue Special Award for "Protection of Profit and Privilege" to the government so relevant. It is appropriate too, that this award is given to the Prime Minister on behalf of government.

In a real sense, the government's acquiescence (read participation) is worse if only because the government purportedly exists solely to serve the interests of New Zealand and New Zealanders. It is not in the nature of big business to even want to do so. I congratulate the judges on making the point so emphatically.

One would assume however, that the nature of such corporations all share similar arrogant attitudes toward employees and their unions, the environment, and potentially awkward rules and regulations. These aspects of business (particularly industrial relations) seem to have registered strongly with previous Roger winners.

It was a bit of a surprise, therefore, when the judges' statement didn't mention the industrial relationships that Telecom, Contact, Westpac and Mitsubishi have with their employees. Surely there is no new level of understanding between corporate thinking and the shop floor.

Of course, the attitudes haven't changed. In fact, the judges did select and detail the most glaring failings of this year's finalists, which happened not to be industrial relations. The truth is there aren't that many shop floors in New Zealand today anyway. Our shop floors of Petone and South Auckland have moved into a myriad of Asian sweatshops.

And for those workers still employed locally, there is outsourcing. Employees become contracted workers – effectively casualised - either individually or in many small firms where the concept of the collective is difficult to realise.

The history of Telecom and trade unions is spelled out by Tony Wilton, one of the top officials in one of the largest trade unions in the country.

"Telecom set out to de-unionise as far as they could possibly do so followed by a policy to contract out all they employees they could. They used the anti-employee provisions of the Employment Contracts Act to the maximum…

"Telecom refused to negotiate, delegates were made redundant, they refused to consider a national collective. They had a collective non-enhancement policy, which meant union members were not to advance in the company," Wilton says.

"In the late nineties, four Telecom workers intercepted a management email that detailed the policy of non-enhancement. The union took the case to court and won. The company was found to be in breach of the employment contract and was penalized and the workers paid compensation.

"It didn't seem to matter," Tony Wilton says. "Today the company has largely rid itself of workers. There aren't a lot of employees apart from an excess of managers and sales people."

Trade union organiser Dave Jarrett in Levin believes that "today we represent maybe only 10 – 15% of Telecom workers. When it was the old Post Office & Electrical Workers union, or even the Communication and Energy Workers which came after, we used to cover the lot."

This lack of union support has serious side effects for workers. Up until about 2002, Occupational Overuse Syndrome or OOS was a huge issue with Telecom, even featuring on TV One's *60 Minutes*. One case went to the Privy Council. But the problem has largely disappeared, not necessarily a good thing.

EPMU Health and Safety Officer Fritz Drisner explains. "The number of cases we can represent has dropped over the last few years for a number of reasons. There has been a huge technical improvement in workstations. The harsh working environment has gone, and of course, ACC is pushing very hard, and Telecom knows that.

"This doesn't mean the attitude has improved," Drisner says. "A large number of line workers are called out on their own in dangerous circumstances. Unfortunately they are almost all on contract to outside firms or are working for themselves. This is casualisation at its worst, and seriously affects Health and Safety in the workplace.

"Even then, Telecom should show some responsibility for Health and Safety as the Principle Employer, but they tend to let the self-employed and secondary employers carry the can," Fritz Drisner says.

Westpac started as the Bank of New South Wales in 1861. Labour intensive work and long hours were the keys to success in those days. In 1920 a staff demand for mechanical adding machines was refused by management who wanted "young bank officers to practice their long additions without assistance."

By 2004, it was still labour intensive and long hours. But now there were both employees and a union. Surveys by the bankers union Finsec found that more than half the Wespac workers surveyed admitted to being bullied, threatened or intimidated every week usually by a manager or team leader.

"The culprit is the management system (at Westpac)," said a Finsec union organizer at the time. "It imposes low staffing levels, then puts extreme pressure on staff to perform." The union said the cure needed to focus on the management system, not any one individual bank.

In July of last year, more than 100 Westpac bank officers went on strike. The bank almost immediately agreed to some changes including reduced hours and more regular shifts. Some of the practice changed, but none of the attitude. That's still to come.

Thirty years ago, newly-built Mitsubishi's Todd Motors in Porirua, the largest car assembler in the country was riding the crest of NZ manufacturing which boasted 70,000 cars assembled and sold in 1979, even if it was only a kit-set screwdriver industry.

Ten years later, Rogernomics and the corporate rot set in. Todd Motors disappeared. The Coachmakers Union disappeared. Mitsubishi went home to Japan. Both Ford and General Motors in the Hutt Valley closed their doors. There was widespread unemployment in New Zealand.

For several decades, Mitsubishi policy covered-up a number of serious vehicle design defects in its cars, trucks and busses. When confronted, recalls were few and far between. Mitsubishi New Zealand blamed Mitsubishi Japan and vice versa, and both refused to take responsibility.

Things came to a head in 2004, as safety defects, especially in school busses, forced authorities in each country to act. In New Zealand, there were more than 1,300 vehicle recalls. It left the disgraced company in tatters, and again threatened the jobs and wages of hundreds of New Zealand workers involved with Mitsubishi products. Around the world, one out of four Mitsubishi workers were to lose their jobs to pay for the company's dishonesty.

Only weeks after the company admitted to covering-up further manufacturing defects over a number of years involving several truck crashes and at least one death, company executives decided to own up to the problem. A spokesman for Mitsubishi New Zealand admitted, "It's been a tough few weeks, but we are working to ensure the people inconvenienced by recalls are back on the road."

Shortly after, Mitsubishi Chief Executive Yoichiro Okazaki in Tokyo breezily declared, “We have now come clean.” Issue closed. Later, the corporation said it felt “aggrieved at having been singled out,” citing larger recalls from Ford and Mazda in the United States. There’s that “righteous indignation”.

We noted earlier, and it still holds true. Exploitive and arrogant behaviour with these companies differs only in degree and circumstance. Such is the nature of big business, and Contact Energy is no exception.

During the coming election campaign, the huge NZ Grey Power Federation will focus on two major issues affecting elderly people. One of these is Energy, and the specific concerns are a.) disclosure and transparency on power bill charges, b.) better long-term generation planning, and c.) more government control over industry profit.

No fools, these Grey Heads. A couple of excerpts taken from the 18 point Executive Summary of Grey Power’s Energy Policy pretty much tell how it is – and how it should be.

- The present arrangements in the electricity and gas supply industries disadvantage domestic and small business consumers.
- Both the allowable valuation method and rate of return for Line Companies as determined under the present information Disclosure Regulations are excessive and unreasonably inflate prices.
- Grey Power takes issue with unethical practices such as generators manipulating the market to create shortages, thus causing the high spot prices in the market.

There are three State Owned retail electricity suppliers, one Community Trust and Contact Energy, the only privately foreign-owned supplier, and the second largest company on the NZ Stock Exchange. A Grey Power energy spokesman admitted that, “Contact Energy is by far the toughest nut. They won’t give away anything!”

The Engineers Union has made some headway into several Contact Energy worksites, “but not without facing a lot of company resistance,” an organizer said. “The company was surprised we were able to get so many members – we had to do it on the sly. When we approach management over issues, they sometimes threaten to close our site and move to another in South Island. I know it’s not going to happen, but it scares the younger workers with families.

“The company tapes all the call-centre phone calls and maintains a heavy supervisory presence. Contact hires special consultants to do their negotiating for them. No room for movement. These people were disgusting….

“It’s not so bad now. The company is more cooperative, at least on the surface. But I wouldn’t trust them. They can be difficult, hardnosed buggers.”

Around the world, McDonald’s has the highest transnational corporate profile. The company seems to work on the principle there is no such thing as bad publicity.

There are exceptions, such as John Vidal’s book *McLibel*, published in 1997. It is a detailed story of the lengthy legal battle between McDonald’s and five London protesters who were passing out leaflets about the unhealthy quality of McDonalds fast food. This has to be the height of “righteous indignation” we mentioned earlier.

Mention McDonald's anywhere. It's a 40-plus billion dollar business. The universal image, together with Ronald McDonald and Golden Arches is unhealthy fast food and low paid, casual labour.

McDonald's opened its first restaurant in New Zealand in Porirua 29 years ago. There are now some 150 McDonalds in New Zealand (one in every town with a population of more than 15,000). More than one and a half million McDonald's burgers are sold each week in New Zealand. Today, these are being bolstered with dozens of new McCafes, catering to cappuccino sipping mums and dads.

McDonald's target audience is children. In fact, it is a concerted appeal to parents through their children. For many, it is insultingly obvious and inappropriate.

Last month, the government and the District Health Boards were criticized for approving plans to have McDonald's sponsor mobile dental healthy clinics around New Zealand. This, only a month after McDonald's moved its restaurant out of Starship Children's Hospital under controversy.

Next to oil companies, the corporation that is probably responsible for more damage to the environment is Malaysian-owned Rimbunan Hijau with operations in four continents and the western Pacific. (Contact Energy tries hard, but it's no match.)

It's not just the illegal, clear felling of endangered hardwoods, the water pollution, and virtual genocide of remote forest dwelling people. It is the accompanying human rights abuses, and the strong-arm, stand over, thug-like tactics of armed, private police that go with it.

Rimbunan Hijau's subsidiary in New Zealand is Ernslaw One, and has already received government license to base its operations in the East Coast, Coromandel and Otago. Ernslaw One is now the country's third biggest forest plantation owner. A show of force last year by East Coast Maori loggers using logging trucks and a bulldozer stopped a planned 30 per cent redundancy call by the newly arrived corporate transnational.

Accompanied by an especially bad reputation, already involved in NZ Environment Court battles, and facing a reasonably well unionized and resistance-tested forestry workforce, the company is not likely to pillage New Zealand to the extent it has Papua New Guinea, remote parts of Russia, Africa and South America.

But it has nothing to offer New Zealand. The company has no intention of sustaining its felling rate with new plantings, and the planned processing of 200,000 cubic metres of logs per year will be measured mainly in profit to Ernslaw One.

If there ever was a transnational corporate that should not be operating in New Zealand it would be 117-year old Toll Holdings Limited from Australia. Not that its behaviour is any worse (or better) than other nominees. Rather that the government had every opportunity and obligation to re-nationalise the entire rail network and "gutlessly and embarrassingly" failed to do so.

In its first year of operation, and following in the footsteps of a less than illustrious predecessor, Toll Holdings announced rail passenger closure for more than a half-dozen stations on the main trunk line. These are all well-known historical rail towns such as Te Awamutu, Waiouru, Taihape, Otaki and

Waikanae (sound familiar?) For some, it could be the equivalent of the loss of the town's Post Office all over again.

Tolls says the cuts will slice 40 minutes off the Auckland-Wellington journey. Anyway, the company says, "the number of passengers were too low to justify keeping the service going."

That's not the point. This is New Zealand, and there are values. Like Taihape and Otaki. You are not running the Osaka-Tokyo 200kph express, mate.

But closure is not likely to happen to any potential freight depots. Already, Toll is setting all-time records for highly profitable freight tonnage. Moving from Napier to Christchurch? Send your whole household by rail. The family can hitchhike.

This attitude pays off in some circles. Little more than a month ago, the managing director of rail operator Toll Holdings, Paul Little, was named Business Leader of the Year in the first Transtasman Business Awards. Toll was described as the pre-eminent provider of transport and logistics services. Probably worth noting the award for Business of the Year was Sky City Entertainment Group, a previous Roger Award Finalist.

The Roger Award has been going since 1997, and like an accounting of most anti-social type behaviour, recidivism is a problem. The unruly do reappear again and again.

Both McDonald's and Contact Energy have been nominated before. This is Telecom's fifth showing (plus a Special Award for Monopoly Profiteering in 2003), Westpac's second showing. Carter Holt Harvey made the list four times. For six years Tranzrail appeared on every finalist list (outright winner three times), and was finally relegated to the permanent Hall of Shame to make room for new deserving aspirants.

Finally, there is the government. That too, is part of the nature of business.

Telecom: What a winner!

Sue Newberry

Telecom New Zealand Ltd emerged from the corporatisation and subsequent privatisation of the telecommunications functions provided through the Post Office until 1986. In 1990, Telecom's shares were sold for NZ$4.25 billion to a consortium comprising two major US companies, Ameritech and Bell Atlantic. As part of the deal, Ameritech and Bell undertook to sell down their holdings to no more than 49.4% within three years.

Ameritech and Bell earned significant profits from a public float in 1991, in which they sold 31% of Telecom's shares, and from the sale of more Telecom shares in 1993. In April 1997, Telecom commenced the public issue of debt in the form of capital notes (called "Telenotes") to finance the repurchase of up to NZ$1 billion of shares. By this time, Ameritech and Bell had already recouped their original investments in Telecom from the earlier share sales in 1991 and 1993 and through dividends. In 1999, Telecom issued more Telenotes, to finance more share repurchases and refinance the earlier Telenotes.

As Ameritech and Bell have sold down their shares, share ownership in Telecom has increasingly shifted to New Zealand and Australia. Today, Telecom is New Zealand's largest listed company, and it comprises about 26% of the weighting of the share-market index for the top 50 companies. It is highly influential in the New Zealand share market, not only in its own right, but it is also influential on the value of listed funds, especially those that track the share market index. This is because the share investments held by the fund managers are likely to be weighted according to that index, so about 26% of the investments are likely to be in Telecom shares. Telecom is also listed on the New York Stock Exchange, and in Australia, Berlin, Frankfurt and Munich.

The judges' report calls Telecom's reported profit figures a national scandal and accuses Telecom of monopoly profiteering. Telecom's own analysis showing its financial activities by geographical segment lends some support to this accusation. Telecom identifies its geographical segments as New Zealand, Australia, and other. Table 1 contains the figures Telecom reports in the detailed notes to its accounts for each segment's earnings before interest and taxation, and total assets. The percentage returns on assets, which are calculated from those figures, suggest that Telecom's monopoly profits in New Zealand prop up less successful activities overseas.

Table 1: Telecom's geographical segment information
(All in NZ$ millions)

	2001	2002	2003	2004
Earnings before interest and tax (NZ)	1,318	1,465	1,499	1,538
Total assets (NZ)	5,327	4,886	6,363	6,002
% return on assets (NZ)	24.7%	30%	23.6%	25.6%
Earnings before interest and tax (Australia)	56	41	24	35
Total assets (Australia)	1,922	1,553	1,377	1,215
% return on assets (Australia)	2.9%	2.6%	1.7%	2.9%
Earnings before interest and tax (Other)	307	22	24	6
Total assets (Other)	982	1,411	868	1,062
% return on assets (Other)	31.3%	1.6%	2.8%	0.6%
Total earnings before interest and tax (before eliminations)	1,681	1,528	1,547	1,579
Total assets (before eliminations)	8,231	7,850	8,608	8,279
% Return on assets (total before eliminations)	20.4%	19.5%	18.0%	19.0%

The totals "before eliminations" give totals for all segments, and in the published financial reports these totals are then reconciled back to the figures reported in the main financial statements. The earnings before interest and tax figures reported for segments are higher than the net profit figures reported each year because the net profit is calculated after deducting interest and tax. I am sceptical about the net profit figures Telecom reports in the main financial statements, especially those reported over the last four or five years. That scepticism means I am also doubtful about the earnings before interest and tax figures shown in Table 1, but those figures do at least show that Telecom's activity outside New Zealand is marginal at best.

Telecom's listing on the New York stock exchange means it has to reconcile its financial results according to New Zealand requirements (NZGAAP) with those reported in the United States according to US requirements (USGAAP). The reconciliation is shown in the detailed notes to the accounts, and Table 2 provides a comparison of reported profits and shareholders funds.

Table 2: Telecom profits and shareholders funds: as per NZ requirements and compared with US requirements
(All in NZ$ millions)

	1995	1996	1997	1998	1999	1999 3mth	2000	2001	2002	2003	2004
Net profit (NZGAAP)	620	717	581	820	822	202	783	643	-188	709	754
Net profit (USGAAP)	614	715	675	762	768	163	773	342	-410	839	157
Shareholders funds (NZGAAP)	2090	2148	1642	1062	1085	1086	1130	1997	1325	1765	2205
Shareholders funds (USGAAP)	2434	2358	1963	1276	1325	1286	1321	1746	1043	1653	1541

Take particular note of the comparative results from 2001 onwards. Net profits reported in New Zealand (NZGAAP) between 2001 and 2004 totalled NZ$1,918 million, more than double the net profits reported for the same period according to US requirements (USGAAP). The profits according to US requirements totalled NZ$928 million. That's a difference of $1 billion over just four years. A similar difference shows up in shareholders' funds, where a NZ$700 million gap has opened up.

From the mid-1990s, the Securities Exchange Commission in the United States and the US accounting standard-setter worked hard to deal with problems they faced there with aggressive earnings management. Listed companies were under pressure from the analyst community to "make their numbers", and that pressure was unreasonable and unrealistic. One response to that pressure was aggressive earnings management. This involves not merely "making the numbers", but "making up the numbers" using a variety of means including dubious deals and accounting devices. The collapse of Enron amid financial scandals in late 2001 was not an isolated incident. This was made apparent in the year that followed with a wave of collapses and earnings restatements, in which "errors" in earlier financial reports were admitted. In New Zealand, the misleading impression given was that the same thing could not and would not happen here, but listed companies are under the same pressure here. Scrutiny of some of Telecom's transactions reveals their dubious nature and raises questions about the validity of Telecom's reported profits over recent years.

Capacity swaps

In the late 1990s, Telecommunications companies had been laying fibre-optic cable which they expected to bring about a massive increase in telecommunications traffic. Maybe it will, eventually, but the increase wasn't immediate and the companies were under pressure to maintain and increase their reported profits. One way of increasing reported profits was by two companies swapping approximately equal amounts of the unused capacity in their cables. They might have swapped cheques as well, and these would be for approximately the same amount of money. This deal resulted in each company reporting an increase in profits by the amount of cable capacity “sold” to the other, and an increase in their assets by the amount of cable capacity “bought” from the other. This aggressive method of accounting is now considered fraudulent in the US. Telecom was named as a counter-party to Global Crossing in some of these capacity swap deals. Global Crossing had used that aggressive method in the US, but Telecom had not. Telecom did, however, use that aggressive method of accounting here and these capacity swap deals added $29 million to Telecom’s profits reported in New Zealand in 2002. When Global Crossing’s accounting came under scrutiny in the US, the Securities Commission here looked at Telecom’s reporting in New Zealand. Global Crossing was charged with fraudulent accounting in the US, while Telecom’s accounting here was cleared as acceptable.

Cross border leases

Cross border leases are largely tax-driven deals. They involve leasing major assets to a US counter-party, and then leasing them back through a tax haven. The deal is intended to bring large tax benefits to the US counter-party and the non-US party typically receives about 5% of the gross amount of the deal for its trouble. At the same time, if the deal is structured right, the non-US party can gain tax benefits in its own country. The cross border leasing industry is renowned for setting up leases which allow double-dipping (claiming the same tax benefits in two countries) and even triple-dipping (claiming the same tax benefits in three countries). Typically, the transaction passes through at least one tax haven. Cross border leases added $20 million to Telecom’s reported profits in 2001 and $34 million to Telecom’s reported profits in 2002. The amount of tax benefits, if any, Telecom gained in New Zealand as a result of these cross border leases is not known.

Off-balance sheet entities

Group financial reports must include all entities that are controlled. Under some circumstances other entities may be created that are controlled but not included in the group reports. The US version of these is known as a special purpose entity and Enron made these notorious, mainly because it used them to hide some of its losses and debt. In the August 2004 Watchdog (www.converge.org.nz/watchdog/06/03.htm), I explained how Southern Cross Cables Holdings Ltd, which is registered in the Bermuda tax-haven, came to be Telecom’s New Zealand version of an off balance-sheet entity. I also explained how, in 2001, Telecom improved its own reported results after tax by $221 million (52%) simply by bouncing money out and back to Southern Cross (The before tax amount was $245 million).

At the time, Southern Cross was clearly identified as loss-making, and Telecom seemed to be using Southern Cross to conceal its losses as well. In 2004, in its USGAAP financial reports, Telecom was required to include Southern Cross’s losses. That showed us that since 2001, Telecom has incurred losses of $604 million in Southern Cross which have not been reported in its New Zealand results. That requirement also revealed a higher level of indebtedness than was apparent in Telecom’s reports. This is shown by the increase in liabilities as a percentage of assets (Table 3).

Table 3: Telecom’s assets and liabilities
(All in NZ$ millions)

	Telecom excluding Southern Cross	Telecom including Southern Cross
Assets	7,500	8,869
Liabilities	5,292	7,264
Liabilities as % of assets	**70.1%**	**81.9%**

Intellectual property

And then there's the goings on with Telecom's intellectual property. I still don't quite follow that. In 2003, Telecom "sold" intellectual property to a subsidiary for $2.14 billion. Because it had never recorded that IP before, the whole $2.14 billion was regarded as profit. Because that transaction occurred within the Telecom group, it did not affect profit in the group accounts. To that point, although the transaction seemed odd, there was nothing to question.

In the 2004 financial year, something to do with a "brand financing transaction" occurred. It involved several other parties including JP Morgan New Zealand Financing LLC, and ABN AMRO Bank NV. Subsidiaries were formed and then dissolved shortly afterwards. Presumably this brand financing transaction passed through them. If this was a tax-driven deal similar to the cross border leases, Telecom might be expected to earn about 5% of the $2.14 billion, or about $107 million for its involvement. Some link might also be expected to taxation benefits for Telecom, possibly related to royalties.

At the same time as these events occurred, Telecom reduced the debt it reported on its balance sheet by about $126 million. Whether there is any link between the two events is not clear.

Conclusion

New Zealand's largest company seems to have an exemplary record for its financial reporting. Telecom has established a consistent record as a prize winner in the Institute of Chartered Accountants' (ICANZ) annual report awards, winning prizes in 2000, 2001, 2003 and 2004. In 2003, Telecom's report won the supreme award. Only in 2002 did Telecom miss out on a prize. That was the year Telecom's financial reporting came under scrutiny following publicity over its involvement in some of Global Crossing's questionable deals, and for its cross border leasing activities.

Closer scrutiny of Telecom's financial reports reveals the extent of the difference between the story Telecom tells its shareholders in New Zealand and the story it tells its shareholders in the United States. In the United States, Telecom's total reported profits for the last four years are less than half of those reported in New Zealand. Telecom's financial reporting of its capacity swaps and its use of Southern Cross Holdings as an off balance sheet entity explains much, although not all, of the difference between the results reported in the two countries. It is not possible to say categorically that one country's practices are "right" and another's "wrong", but I've always respected the US standard-setter's efforts and prefer the US approach with these.

Perhaps it is not surprising, given the differences between results reported in the US and those reported in New Zealand, especially over recent years, that today we are witnessing a significant pattern change in Telecom's shareholding. Foreign investors are selling down their shares while New Zealanders and Australians take them up. Here in New Zealand, Telecom is trumpeting its improved profits and its intention to pay out as dividends an amount no less than 75% of its reported profits. Telecom's chairman says Telecom's "sound position" has been brought about through Telecom's strong operating performance, reduction in debt and its excellent prospects for further improvement in the balance sheet. The problem is that Telecom's performance doesn't look nearly so strong if you look at what it reports in the United States, and the sustainability of its proposed dividends has to be questioned. The profit figures taken from Telecom's financial reports may be compared with past dividend payouts (Table 4).

Table 4: Telecom profits according to US requirements, NZ requirements, and comparison with dividends
(All in NZ$ millions)

	1995	1996	1997	1998	1999	1999 3mth	2000	2001	2002	2003	2004
Net profit (USGAAP)	614	715	675	762	768	163	773	342	-410	839	157
Net profits (NZGAAP)	620	717	581	820	822	202	783	643	-188	709	754
Dividends paid	597	727	831	859	910	227	906	303	423	428	488

For the ten years of this review, Telecom's profits as reported in New Zealand totalled NZ$6,464 million, while the profits as reported in the United States totalled considerably less at NZ$5,398. The dividends paid out amounted to NZ$6,698 million. This gives a total dividend payout of 103.6% of reported profits as reported in New Zealand, but 124.1% of reported profits as reported in the US. Looking more closely at the last four years which are of particular concern, Telecom's profits as reported in New Zealand totalled NZ$1,918 million, while the profits reported in the United States totalled only $928 million. The dividends paid out amounted to $1,642 million. That is a payout of 86% of the profits reported in New Zealand but, as already explained, I am sceptical about those profit figures. It is 177% of the more believable profit figures reported in the United States.

In New Zealand, the promotion of Telecom's shares, the trumpeting of improved profits, and the promise of increased dividend payouts as a percentage of reported profits all seem to help boost Telecom's share price and demand for its shares. Telecom's geographical segment analysis (Table 1) shows that the profits Telecom reports here come from Telecom's monopoly position here in New Zealand. Further, that segment analysis relates to the profits reported in New Zealand, but the more believable profit figures are the lower ones reported in the US. For example, Table 1 shows that in 2001 Telecom reported $307 million as earnings before interest and tax (other). That is the year Telecom "improved" its before tax profits reported in New Zealand by $245 million through the transaction with its Bermuda-based off-balance sheet entity, Southern Cross Cables Holdings Ltd. Telecom did not include that $245 million in the profits it reported in the United States, and I don't think it should have included it in New Zealand either. It seems unlikely that Telecom's overseas activities are profitable at all.

There is a practice called "pump and dump", which is well-known in the United States but not so well known in New Zealand. Pump and dump occurs when existing investors who know something is wrong with a company promote the shares as a great buy (pumping the shares) while they sell off (or dump) their own shares in that company. As became evident with Enron, some analysts get involved in this as well, either by accepting the pumping story without closer scrutiny or, perhaps, because they stand to earn more from their ongoing relationships with the company and its senior executives than from individual shareholders. Eventually, the company's poor state is revealed and the share prices collapse, but not before the investors in the know have dumped most or all of their shares onto unsuspecting buyers at a good price.

New Zealand investors seem convinced that Telecom's shares are good to buy. Time will tell whether they are right.

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