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# Qwest Pays the Piper

## SEC levies fines for executive wrongdoing

By Joshua E. Barbach



Qwest is making the kind of news that's all too common in telecom. The LEC recently settled with the SEC for $250 million to settle a fine levied for Qwest's overstatements of $3.8 billion in revenue from 1999-2002. This news is not four months removed from settlements by two former Qwest executives. Though neither denying nor confirming allegations, they were alleged to have approved and executed secret deals involving fiber-optic cable sales to improperly record millions in revenue. A SEC statement filed on October 26 declared that several former Qwest executives remain targets for continuing prosecution against the company.

The SEC's statement of claims against Qwest includes a variety of offenses including breaches where "accounting rules, policies, or controls that interfered with meeting revenue targets were stretched or ignored outright." Qwest misrepresented its growth through false and misleading projections and earnings releases, and also made false or misleading statements about its management's investments in Qwest's vendors. Throughout this period, Qwest's former executives sold off stock at greatly over-inflated values. The SEC statement contains some colorful references and strong accusations. Some of the more troubling ones detailed an environment in which fraud was promoted to that point that it was essentially a mandate. Internal emails acknowledged that the strategy being used to book fraudulent sales was not sustainable. Yet suggestions to the COO at the time to "reset expectations and put on the best face" were rejected.

Questions around Qwest's stock value go back to its acquisition of US West, where the purchase agreement called for Qwest to issue $69 in common stock for each US West share. There was a "collar" provision that required Qwest stock to trade between $28.26 and $39.90 per share. This provision began the artificial manipulation of the stock's value. Qwest was able to acquire US West by using its common stock's value, which, the SEC now details, was significantly inflated. Further, at that time current Qwest's CEO, COO and President, and CFO were set to control the surviving company.

The charges of greatest concern may be those regarding Qwest's vendors. The statement alleges that Qwest used its leverage over equipment and service vendors to engage in gross misconduct. Qwest is alleged to have refused to do business with vendors unless the vendor allowed Qwest to invest before or at IPO. The benefit of Qwest's commitment to purchase those equipment or services was considered essential to the success of the IPOs. In a desire to gain equity positions in vendors, Qwest executives purchased millions of dollars of equipment they knew they never intended to use.