

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 51517 / April 11, 2005**

**ACCOUNTING AND AUDITING ENFORCEMENT**  
**Release No. 2231 / April 11, 2005**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-11891**

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**In the Matter of**

**GLOBAL CROSSING LTD.,**  
**THOMAS J. CASEY,**  
**DAN J. COHRS, and**  
**JOSEPH P. PERRONE,**

**Respondents.**

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**ORDER INSTITUTING CEASE-AND-DESIST  
PROCEEDINGS, MAKING FINDINGS,  
AND IMPOSING A CEASE-AND- DESIST  
ORDER PURSUANT TO SECTION 21C  
OF THE SECURITIES EXCHANGE ACT OF 1934**

**I.**

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act"), against Global Crossing Ltd. ("GX" or the "company"), Thomas J. Casey ("Casey"), Dan J. Cohrs ("Cohrs"), and Joseph P. Perrone ("Perrone") (collectively, the "Respondents").

**II.**

In anticipation of the institution of these proceedings, Respondents have submitted Offers of Settlement ("Offers"), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Cease-and-Desist Proceedings, Making Findings, and Imposing a Cease-and-Desist Order Pursuant to Section 21C of the Securities Exchange Act of 1934 ("Order"), as set forth below.

**III.**

On the basis of this Order and the Respondents' Offers, the Commission finds that:

## A. SUMMARY

This case concerns the failure of GX and its senior management to ensure that the company provided complete and accurate disclosure to investors concerning certain significant transactions entered into by the company in the first half of 2001. Because of GX's inadequate disclosure, investors were not given the opportunity to fairly judge the quality of GX's financial results and the likelihood that its past performance would be indicative of its future performance. These significant transactions involved GX's sales of telecommunications capacity to other carriers that were linked to, and in some cases dependent on, its purchase of capacity from the same carrier. GX referred to these transactions as "reciprocal transactions." In early 2001, GX was increasingly reliant on the reciprocal transactions as a substantial source of GX's announced "pro forma" results, i.e., results of operations that were prepared on a basis defined by GX, and that were not in accordance with generally accepted accounting principles ("GAAP"). For example, GX had a pro forma measurement called "Cash Revenue" that GX defined as revenue calculated in accordance with GAAP, plus the cash portion of the change in deferred revenue. Without these reciprocal transactions, GX would not have met securities analysts' estimates for its first and second quarter 2001 pro forma results.

In its quarterly filings with the Commission for the first and second quarters of 2001, GX included the money it received from the reciprocal transactions in its pro forma results, and it included the money it received and paid in its statements of cash flows. Because GX included the cash it received from reciprocal transactions in its pro forma results and its statements of cash flows, it was required to disclose completely and accurately material information regarding the reciprocal transactions and the effect of that information on the interpretation of its financial results. While GX did disclose (i) that GX sold telecommunications capacity to carriers from which GX also purchased capacity, (ii) the gross dollar amounts of the sales and purchases of capacity, and (iii) that the cash derived therefrom was a significant component of GX's pro forma results, GX's disclosure was nevertheless inadequate.

Specifically, in the Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") portion of its first and second quarter of 2001 Forms 10-Q, GX failed adequately to disclose:

- That the transactions were reciprocal in nature, i.e., that GX's sale depended in whole or in part on GX's purchase from the same carrier;
- That GX's pro forma results were increasingly dependent on these reciprocal transactions, and that, given market trends, GX likely would not be able to sustain these results in the future;
- In presenting its statements of cash flows, that the reciprocal transactions did not enhance GX's liquidity; and
- Material information concerning GX's purchase of capacity as part of certain reciprocal transactions that affected GX's ability to integrate the purchased capacity into the GX network, including that (1) GX and certain contra parties still had to negotiate and agree upon important additional issues, (2) GX purchased certain capacity that would not be ready for service for a substantial time after the end of the quarter, (3) in certain reciprocal transactions GX had not designated the specific capacity to be purchased, and (4) GX had purchased certain capacity with the stated purpose of reselling the capacity.

This information was material to investors because GX ultimately could not sustain its heavy reliance on deriving cash revenue from the reciprocal transactions, as these transactions did not enhance

GX's liquidity and, ultimately, GX could not fund the capital commitments required to integrate the purchased capacity into the GX network and thereby derive future service revenues. Thus, investors were denied material information not contained in its financial statements but nonetheless necessary for a fair understanding of GX's financial performance and condition in light of the circumstances, namely in light of the pro forma financial information and the information reflected in its statements of cash flows that GX disclosed.

GX's Chief Executive Officer, Thomas J. Casey, its Chief Financial Officer, Dan J. Cohrs, and its Executive Vice President of Finance, Joseph P. Perrone, knew material information regarding the reciprocal transactions and their past and likely future effect on the company's financial condition and results of operations. Casey, Cohrs, and Perrone reviewed and approved the MD&A portion of GX's periodic reports which failed to disclose this information. Although GX's counsel, independent auditor, and audit committee chairman participated in reviewing the MD&A, Casey, Cohrs, and Perrone each had particular knowledge because of their respective positions that the reciprocal transactions would cause GX's reported financial information not to be necessarily indicative of its future operating results or financial condition. The Respondents therefore knew or should have known that the disclosure was inadequate and failed to satisfy their affirmative obligation to ensure that the disclosure was complete and accurate.

As a result, GX violated, and Casey, Cohrs, and Perrone caused violations of, the reporting provisions of Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder because GX's MD&A in its first and second quarters Forms 10-Q contained inadequate disclosure regarding the reciprocal transactions.

## **B. RESPONDENTS**

**1. Global Crossing Ltd.** is a Bermuda corporation with its principal offices in Hamilton, Bermuda and Florham Park, New Jersey, and formerly in Madison, New Jersey and Beverly Hills, California. GX was founded in 1997, and its initial public stock offering was in 1998. At all relevant times, GX's common stock was registered with the Commission under Section 12(b) of the Exchange Act. Currently, GX's common stock is registered with the Commission under Section 12(g) of the Exchange Act and trades on the Nasdaq Stock Market. GX's common stock previously traded on the Nasdaq Stock Market from August 1998 through November 5, 2000, on the New York Stock Exchange from November 6, 2000 through January 28, 2002, and through the OTC Bulletin Board from January 29, 2002 through January 21, 2004. On January 28, 2002, GX and certain of its affiliates filed bankruptcy under Chapter 11 of the United States Bankruptcy Code and coordinated proceedings under Bermuda law. On December 26, 2002, the bankruptcy court entered an order confirming a Joint Plan of Reorganization. On December 9, 2003, GX emerged from bankruptcy.<sup>1</sup>

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<sup>1</sup> Prior to emergence from bankruptcy, GX filed with the Commission a Form 10-K for the year ended December 31, 2002 which included, among other things, audited financial statements as of and for the years ended December 31, 2002, 2001 and 2000 and selected quarterly data required by Item 302(a) of Regulation S-K, for 2002 and 2001, not having filed a Form 10-K for the year ended December 31, 2001. After emergence from bankruptcy, a newly formed Bermuda company named Global Crossing Limited ("New GX") filed Exchange Act reports as successor issuer to GX under the Exchange Act. On December 23, 2003, New GX filed with the SEC a Form 8-K which contained an audited balance sheet as of the date of emergence. On December 23, 2003, New GX filed with the SEC a Form 10-Q for each of the quarters (footnote cont.)

2. **Thomas J. Casey** was GX's CEO from October 2000 to October 2001, a GX managing director from September 1998 to October 2000, and a GX vice chairman from December 1998 to October 2001. In addition, from September 1998 to October 2000, Casey was president and a managing director of a private merchant bank. He previously was an investment banker at a major registered broker-dealer and a partner at two major law firms. He also was an attorney at the Federal Communications Commission and at the U.S. Department of Justice. Casey received a B.A. from Boston College and a J.D. from George Washington University Law School.

3. **Dan J. Cohrs** was GX's CFO from May 1998 to July 2003, Senior Vice President from May 1998 to December 2000, and a GX Executive Vice President from December 2000 to July 2003. Previously, Cohrs was an officer in the finance departments at several major corporations. Cohrs also was an assistant professor of finance at the business school of a major university. Cohrs received a B.S. from Michigan State University and a Ph.D. in Finance from Cornell University, Johnson School of Management.

4. **Joseph P. Perrone** was GX's Executive Vice President, Finance from December 2000 to November 2002 and its Senior Vice President, Finance from May 2000 to December 2000. He was GX's Executive Vice President, Business Performance until August 2003. Previously, Perrone worked for over 30 years at a major accounting firm, at which he was a partner. He is a certified public accountant licensed in New Jersey. Perrone received a B.S. in accounting from Seton Hall University.

## C. **FACTS**

### 1. **Background**

#### a. **GX's Business and Reciprocal Transactions**

GX is a telecommunications company whose business plan, as it evolved over time, was to construct and/or acquire a state-of-the-art global fiber-optic network and to sell fiber optic capacity and telecommunications services (collectively "capacity") on that network to other providers and users of telecommunications services. GX sold this capacity through contracts in the form of "Indefeasible Rights of Use," or "IRUs." An IRU is an irrevocable right to use a specific amount of capacity for a specified time period. GX also purchased specific capacity in the form of IRUs and used that capacity in part to extend and enhance its network.

By early 2001, an increasing number of GX's carrier customers were requesting that GX buy capacity from them, and it was becoming increasingly difficult for GX to sell capacity to carrier customers unless, at the same time, GX purchased a similar dollar amount of capacity from the same carrier. In other words, GX's ability to sell capacity often became linked to, and in some cases dependent on, GX's simultaneous purchase of a nearly equal dollar amount of capacity. GX referred to the simultaneous purchase and sale of capacity with other carriers as "reciprocal transactions."

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(footnote cont.)

ended March 31, 2003, June 30, 2003 and September 30, 2003, with GX not having filed Forms 10-Q since the quarter ended September 30, 2001. GX has informed the SEC that it and New GX have made such filings under the Exchange Act as are described above.

The purchase and sale of capacity was documented through separate and independent contracts. These contracts typically provided for the purchaser to immediately pay the seller the full purchase price. Accordingly, except in two instances, GX and the other carrier exchanged cash for the IRUs, even if the amounts exchanged were the same or similar. The purchase and sale contracts did not contain cross-default provisions; thus, they created independently enforceable rights and liabilities as to each party.

**b. GX's Reporting of GAAP and Pro Forma Financial Information**

GX announced its operating results in periodic reports filed with the Commission (as well as in earnings press releases disseminated to the public). In Forms 10-Q and earnings releases for the first and second quarters of 2001, GX reported financial information that it stated was prepared in accordance with GAAP. The Forms 10-Q included GAAP balance sheets, statements of operations (income statement), and statements of cash flows, while the earnings releases included GAAP results of operations.

In addition to its GAAP financial statements, GX also reported "pro forma" financial results. GX reported to the public two principal measurements of its pro forma financial results – "Cash Revenue" and "Recurring Adjusted Earnings Before Interest, Taxes, Depreciation, and Amortization," also known as "Recurring Adjusted EBITDA." GX stated in its Forms 10-Q and earnings releases that Cash Revenue consisted of revenue calculated in accordance with GAAP, plus the cash portion of the change in deferred revenue, and that Recurring Adjusted EBITDA consisted of operating income or loss plus goodwill and intangibles amortization, depreciation and amortization, non-cash cost of capacity sold, stock related expense, merger-related expenses, certain other non-recurring expenses, and the cash portion of the change in deferred revenue. Securities analysts who covered GX analyzed the company's performance and established target operating results based primarily on its Cash Revenue and Recurring Adjusted EBITDA pro forma results.

The principal difference between GX's pro forma results of operations (i.e., Cash Revenue and Recurring Adjusted EBITDA) and its GAAP results of operations was that Cash Revenue and Recurring Adjusted EBITDA included the entire amount of cash that GX had collected during the period from GX's IRU sales to other carriers (i.e., the cash portion of the change in deferred revenue). By comparison, GX's GAAP revenue did not include the entire amount of cash that GX had collected during the period from IRU sales. Rather, GX recorded a liability (deferred revenue) corresponding to the amount of cash collected during the period from an IRU sale and recognized GAAP revenue ratably over the term of the IRU (often in excess of 20 years) once the circuit was activated. GX realized little to no GAAP net income from reciprocal transactions because GX amortized revenues from IRU sales over many years, and because the revenues recognized from reciprocal sales were in similar amounts to its depreciation of expenses for IRU purchases over the term of the IRUs.

GX's Forms 10-Q also included statements of cash flows that it stated were prepared in accordance with GAAP. In the statements of cash flows, GX included the cash it received from the reciprocal transactions in its cash flows from operating activities and the cash it expended in the reciprocal transactions in its cash flows from investing activities.

## **2. GX's Reciprocal Transactions in the First and Second Quarters of 2001**

GX's reciprocal transactions reached their peak in the first and second quarters of 2001. In the first quarter of 2001, GX entered into 43 IRU transactions in which GX sold capacity to other carriers. Nine of these transactions were reciprocal transactions, and they accounted for \$375 million of the \$567 million (or 66%) of the IRU sales included in Cash Revenue and Recurring Adjusted EBITDA that GX reported in the quarter. Reciprocal transactions accounted for 23% of Cash Revenue and 85% of Recurring Adjusted EBITDA for the quarter. As part of these reciprocal transactions, GX committed to make capital expenditures totaling \$625 million, purchasing \$383 million in capacity from the other carriers in the first quarter and committing to spend in future quarters another \$242 million to purchase additional new capacity from the carriers and to possibly construct a new fiber optic system on which another carrier had committed to purchase capacity. Without these reciprocal transactions, GX would not have met securities analysts' estimates for Cash Revenue and Recurring Adjusted EBITDA in the first quarter.

In the second quarter of 2001, GX entered into 45 IRU transactions in which GX sold capacity to other carriers. Fourteen of these transactions were reciprocal transactions, and they accounted for \$516 million of the \$567 million (or 91%) of IRU sales for the quarter. Reciprocal transactions accounted for 32% of Cash Revenue; without the reciprocal transactions, GX's Recurring Adjusted EBITDA for the quarter would have gone from the reported \$472 million to a negative \$43 million. As part of these reciprocal transactions, GX paid cash or agreed to pay cash totaling \$437 million to purchase capacity from its carrier customers in the second quarter. Without these reciprocal transactions, GX would not have met securities analysts' estimates for Cash Revenue and Recurring Adjusted EBITDA in the second quarter.

## **3. The Process By Which GX Came to Disclose the Reciprocal Transactions**

Because GX's reciprocal transactions had increased significantly in the first quarter of 2001, Perrone came to the conclusion that separate disclosure of the reciprocal transactions should be made. Various internal discussions among GX management and the chairman of GX's audit committee ensued during March 2001. Eventually, at an audit committee meeting on April 11, 2001, GX management (including Casey, Cohrs, and Perrone) reviewed the list of IRU transactions provided to the committee and recommended that the reciprocal transactions be separately disclosed, and the Chairman of the Board, the audit committee, the in-house general counsel, and GX's independent auditor concurred. The Chairman of the Board stated, and the audit committee concurred, that the chairman of the audit committee should review and approve the disclosure. The disclosure was also raised at a full Board meeting that same day, and the Board also asked that the audit committee or its chairman review the disclosure.

Various GX employees participated in drafting the proposed disclosure regarding the first quarter 2001 reciprocal transactions. In preparing the disclosure, GX employees, including Casey, Cohrs, and Perrone, sought review by GX's in-house counsel, GX's outside counsel, GX's independent auditor, and the chairman of the audit committee, among others. None of those consulted raised any objection to the proposed disclosure with Casey, Cohrs, or Perrone.<sup>2</sup> The respondents thus relied on a process that had been established for the preparation of the disclosure.

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<sup>2</sup> This process was not repeated in preparing the second quarter 2001 disclosure, as the second quarter's disclosure essentially mirrored that of the first quarter.

Eventually, Casey, Cohrs, and Perrone reviewed and approved the disclosure for the first and second quarters of 2001. As discussed below, this disclosure was inadequate in several important respects.

#### **4. GX's Disclosure Regarding the Reciprocal Transactions**

##### **a. First Quarter 2001**

In a Form 10-Q filed on May 15, 2001 (as well as in an earnings release issued on May 9, 2001, and a conference call with analysts and investors on May 10, 2001), GX reported its first quarter 2001 financial results and made various statements regarding GX's IRU sales and purchases.

GX stated in the Form 10-Q and the earnings release that its quarterly Cash Revenue was \$1.613 billion, Recurring Adjusted EBITDA was \$441 million, and Recurring Net Loss was \$608 million, or \$0.69 per share. These results exceeded the securities analysts' consensus estimates. The earnings release further reported that Recurring Adjusted EBITDA was up 43% and Cash Revenue was up 39% from the first quarter of 2000.

In the footnotes to the financial statements in the Form 10-Q as well as in the earnings release, GX further stated that the Cash Revenue and Recurring Adjusted EBITDA amounts included \$375 million received from significant carrier customers who signed contracts during the quarter to purchase \$500 million of capacity on GX's network and to whom GX "made substantial capital commitments during the quarter."

In the MD&A portion of the Form 10-Q and in the earnings release, GX stated that it had entered into several agreements with various carrier customers for the purchase of capacity "in order to acquire cost-effective local network expansions; to provide for cost-effective alternatives to new construction in certain markets in which [GX] anticipates shortages of capacity; and to provide additional levels of physical diversity in the network as [GX] implements its global mesh architecture." The Form 10-Q and the earnings release further stated that GX's capital commitments under these contracts totaled an estimated \$625 million.

In the statement of cash flows included in GX's Form 10-Q, GX reported a positive \$21 million in net cash from operating activities, which included an increase in cash from the sale of IRUs as compared to the first quarter of 2000. With respect to cash flows from investing activities, GX reported increases over the prior period in its purchases of property and equipment and net cash used in investing activities primarily as a result of GX's continued expansion of its network.

##### **b. Second Quarter 2001**

In a Form 10-Q filed on August 14, 2001 (as well as in an earnings release issued on August 1, 2001, and a conference call with analysts and investors on August 2, 2001), GX reported its second quarter 2001 financial results and made various statements regarding GX's IRU sales and purchases.

GX stated in the Form 10-Q and the earnings release that its quarterly Cash Revenue was \$1.620 billion, Recurring Adjusted EBITDA was \$472 million, and Recurring Net Loss was \$607 million, or \$0.69 per share. These results were close to the analysts' consensus estimates of \$1.674 billion for Cash Revenue

and \$464 million for Recurring Adjusted EBITDA. The earnings release further reported that Recurring Adjusted EBITDA was up 33% and Cash Revenue was up 26% from the second quarter of 2000.

The Form 10-Q and the earnings release further stated that Cash Revenue and Recurring Adjusted EBITDA included \$345 million received from significant carrier customers who signed contracts during the quarter to purchase \$381 million of capacity on GX's network and to whom GX made substantial cash commitments during the quarter.

Elsewhere in the disclosure, including in the MD&A portion of the Form 10-Q, GX stated that it had entered into several agreements with various carrier customers for the purchase of capacity. The Form 10-Q and the earnings release again explained that GX entered into these contracts "in order to acquire cost-effective local network expansions; to provide for cost-effective alternatives to new construction in certain markets in which [GX] anticipates shortages of capacity; and to provide additional levels of physical diversity in the network as [GX] implements its global mesh architecture." The Form 10-Q and the earnings release also stated that GX's cash commitments under these contracts totaled an estimated \$358 million.

GX also reported in the Form 10-Q its statement of cash flows for the six months ended June 30, 2001. GX reported a positive \$677 million in net cash from operating activities, up from \$330 million for the same period in 2000, with the increase "primarily due," among other reasons, to "an increase in revenue from [its] . . . carrier business[] resulting from . . . an increase in the number of capacity agreements executed by [GX's] carrier customers." With respect to cash flows from investing activities in the first and second quarters, GX reported that it had increased its capital spending from the prior year to purchase capacity to build out and complete its network.

In reporting the amounts received in reciprocal transactions, GX excluded a reciprocal transaction with one carrier. GX included, however, this transaction in its pro forma metrics, Cash Revenue and Recurring Adjusted EBITDA. This reciprocal transaction related to an earlier IRU transaction between GX and the other carrier. In the second quarter, however, GX and the other carrier renegotiated the earlier transaction and entered into new reciprocal agreements to purchase capacity, under which GX sold \$170 million in capacity to the other carrier and committed to purchase \$79.2 million in capacity from that carrier. Had GX included this transaction in its totals for reciprocal transactions, the amount that GX received from significant carrier customers for capacity would have been \$515 million (instead of \$345 million), a 49% increase, and the amount that GX paid these carrier customers for capacity would have been \$436.9 million (instead of \$358 million), a 22% increase.

## **5. The Inadequate Disclosure**

GX's first and second quarters Forms 10-Q were inadequate in the following respects:

### **a. Reciprocal Nature of the Transactions and GX's Increasing Reliance on Them**

In its disclosures regarding IRUs, GX disclosed that it had sold substantial amounts of capacity to customers to whom it had also made substantial cash commitments. GX also disclosed the gross dollar amounts of these purchases and sales. This disclosure, however, was inadequate. GX's disclosure failed to state explicitly that these IRU transactions were reciprocal in nature, i.e., that GX's IRU sale depended at least in part on GX's simultaneous purchase of a similar dollar amount of capacity from the same carrier.



As a result, investors were not provided with the information necessary to adequately judge the quality of GX's financial results. In addition, investors were not informed that GX's future sales growth was limited by its ability to incur future capital expenditures.

Moreover, GX also did not specify that it was becoming increasingly reliant on the reciprocal transactions as a source of Cash Revenue and Recurring Adjusted EBITDA. In the first and second quarters of 2001, GX's Cash Revenue and Recurring Adjusted EBITDA from reciprocal transactions increased significantly from the corresponding periods of 2000.

**b. The Reciprocal Transactions' Effect on Liquidity**

One measure of a company's liquidity is its cash flows from operating activities in its statements of cash flows. In its first and second quarters Forms 10-Q, GX included the cash that it received from the reciprocal transactions in the cash flows from operating activities and included the cash it spent in the reciprocal transactions in its cash flows from investing activities. By presenting the reciprocal transactions in the statements of cash flows in this manner and not disclosing adequately the reciprocal nature of the transactions, GX failed to disclose that the reciprocal transactions did not enhance its liquidity from operating activities.

Specifically, GX disclosed in its statements of cash flows net cash provided by operating activities of \$21 million for the first quarter and \$677 million for the first and second quarters. GX, however, did not disclose adequately in its MD&A that these amounts included as proceeds from reciprocal transactions \$375 million in the first quarter and \$890 million in the first and second quarters and that, without these reciprocal transactions, GX would have had a negative cash flow from operating activities of \$354 million in the first quarter and a positive cash flow from operating activities of only \$213 million in the first and second quarters.

With respect to GX's cash flow from investing activities, GX reported purchases of property and equipment of \$1.262 billion in the first quarter and \$2.286 billion in the first and second quarters. GX, however, did not disclose adequately in the statements of cash flows, or in the notes to the financial statements, that these items included the amounts disclosed as the cash commitments made in connection with reciprocal transactions (\$383 million (or 30% of the total) in the first quarter and \$819 million (or 35% of the total) in the first and second quarters).

**c. Information Concerning the Purchased Capacity**

GX's disclosure regarding its purchases of capacity was also deficient because it failed to disclose material information about those transactions. First, in five reciprocal transactions, although GX had written arrangements which GX regarded as binding with its contra parties, GX and the contra party still had to negotiate and agree upon important additional operational or business issues, including, in some cases, what capacity was to be exchanged between the parties and when they were to do so.

Second, in eight reciprocal transactions, GX purchased capacity that would not be ready for service until sometime after the end of the quarter, and in some cases not for weeks, months or, occasionally, even a year or more, because the capacity was not yet constructed, was still under construction (including in one instance because the carrier was in severe financial difficulty and in danger of declaring bankruptcy), required governmental approvals, and/or required substantial future additional capital expenditures by GX.

Third, in four reciprocal transactions, GX had not designated the specific capacity that it was purchasing at the time of the purchase. Rather, GX entered into commitments to purchase capacity anywhere on the other carrier's network, on certain segments of those networks, or for certain types of capacity, the specifics of which GX would designate in the future. Under these transactions, GX had substantial amounts of time to designate the actual capacity.

Finally, in five reciprocal transactions, GX purchased capacity in which the stated purpose for the capacity was to resell it to other carriers. In some of these reciprocal transactions, GX was, at the time of the purchase, negotiating with other carriers to resell the capacity; however, GX never completed these negotiations and did not resell any of this capacity.

GX did not disclose this information in its first and second quarter 2001 Forms 10-Q. This information was material to investors because it affected GX's ability to integrate the purchased capacity into the GX network and thereby derive future revenues. Moreover, GX failed to disclose to investors that, in light of GX's increasing dependence on reciprocal transactions for the sale of IRUs, the limitations on its ability to integrate its purchased capacity could adversely impact its ability to sustain its increasing reliance on reciprocal IRU transactions.

## **6. The Individual Respondents' Knowledge of the Reciprocal Transactions and Responsibility for the Disclosure**

Casey, Cohrs, and Perrone knew of GX's reciprocal transactions and of the business purposes for the purchases and understood that in many instances GX could not sell the capacity to the other carriers without also concurrently purchasing capacity from the other carriers. Casey and Cohrs also knew that a factor in determining whether to buy capacity from another carrier was the fact that the other carrier was concurrently buying capacity from GX. Casey, Cohrs, and Perrone were also aware of the amount of reciprocal transactions in the first and second quarters, and that in most of the reciprocal transactions, the amount of GX's sale was close to the amount of GX's purchase. Casey, Cohrs, and Perrone knew that GX needed the reciprocal transactions to meet analysts' estimates in the first and second quarters of 2001.

Casey, Cohrs, and Perrone also knew that in some of the reciprocal transactions, GX had purchased capacity (1) that would not be ready for service until substantially after the end of the quarter; (2) in the first quarter from another carrier that then was in severe financial difficulty; and (3) that GX could designate for use in the future. In addition, Perrone knew that in some of the reciprocal transactions, although GX and the contra party had written arrangements that Perrone regarded as binding, GX and the contra party had yet to negotiate and agree upon important additional operational or business issues.

Casey, Cohrs, and Perrone reviewed and approved the disclosure regarding the reciprocal transactions. Although they knew that GX's counsel, its independent auditor, and its audit committee chairman had also participated in reviewing the disclosure and had not expressed any objections to them or anyone else at GX about the disclosure, they had an affirmative obligation to go beyond the established procedures (including the legal and accounting advice they received) to ensure the accuracy and completeness of GX's periodic reports. In light of their particular knowledge about the reciprocal transactions and their past and likely future effect on the company's financial condition and results of operations, the respondents knew or should have known that the disclosure was inadequate.

**D. LEGAL ANALYSIS: VIOLATIONS OF THE REPORTING PROVISIONS OF SECTION 13(a) OF THE EXCHANGE ACT AND RULES 12b-20 AND 13a-13 THEREUNDER**

Section 13(a) of the Exchange Act and Rule 13a-13 thereunder require issuers of securities registered pursuant to Section 12 of the Exchange Act, like GX, to file certain quarterly reports with the Commission. Implicit in these provisions is the requirement that the reports accurately reflect the issuer's financial condition and operating results. See SEC v. IMC Int'l, Inc., 384 F. Supp. 889, 893 (N.D. Tex.), aff'd mem., 505 F.2d 733 (5th Cir. 1974). Rule 12b-20 under the Exchange Act further requires the inclusion of any additional material information that is necessary to make required statements, in light of the circumstances under which they were made, not misleading. A fact is material if there is a substantial likelihood that a reasonable investor would consider the information important in making an investment decision. Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1988); TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976). Information concerning a company's financial condition is material. See, e.g., SEC v. Murphy, 626 F.2d 633, 653 (9th Cir. 1980). No showing of scienter is required to establish a violation of Section 13(a) of the Exchange Act. See SEC v. Savoy Indus., Inc., 587 F.2d 1149, 1167 (D.C. Cir. 1978).

Form 10-Q requires MD&A disclosure that includes information required by Item 303 of Regulation S-K. 17 C.F.R. § 229.303. Item 303 requires that management discuss and analyze the registrant's financial condition, changes in financial condition, and results of operations, with a specific focus on "material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition." 17 C.F.R. § 229.303(a), Instruction 3. Among other things, Item 303 requires management to (1) "[i]dentify any known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way"; and (2) "[d]escribe any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations." 17 C.F.R. § 229.303(a)(1), (3)(ii).

The purpose of MD&A is "to give the investor an opportunity to look at the company through the eyes of management by providing both a short and long-term analysis of the business of the company." SEC Interpretation: Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, Exchange Act Release No. 26831 (May 18, 1989) ("MD&A Release"); see also In re Caterpillar Inc., Exchange Act Release No. 30532 (Mar. 31, 1992). As the Commission has stated, "It is the responsibility of management to identify and address those key variables and other qualitative and quantitative factors which are peculiar to and necessary for an understanding and evaluation of the individual company." MD&A Release.

One of MD&A's primary objectives is to enhance overall financial disclosure and provide the context within which financial information should be analyzed. In the absence of complete and accurate MD&A, a company's financial statements and accompanying footnotes "may be insufficient for an investor to judge the quality of earnings and the likelihood that past performance is indicative of future performance." MD&A Release.

While counsel, an auditor, or other third party may review the MD&A section, the substance of the MD&A remains firmly the non-delegable responsibility of management. See MD&A Release. "Management has a unique perspective on its business that only it can present." Interpretation:

Commission Guidance Regarding Management’s Discussion and Analysis of Financial Condition and Results of Operations, Exchange Act Release No. 48960 (Dec. 29, 2003).

Corporate officers have “affirmative responsibilities . . . to ensure that the shareholders whom they serve receive accurate and complete disclosure of information required by the proxy solicitation and periodic reporting provisions of the federal securities laws.” Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 Concerning the Conduct of Certain Former Officers and Directors of W.R. Grace & Co., Exchange Act Release No. 39157 (Sept. 30, 1997). “Officers . . . who review, approve, or sign their company’s proxy statements or periodic reports must take steps to ensure the accuracy and completeness of the statements contained therein, especially as they concern those matters within their particular knowledge or expertise.” Id. “To fulfill this responsibility, officers . . . must be vigilant in exercising their authority throughout the disclosure process.” Id.

**1. GX**

GX violated Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder, which require issuers of securities registered pursuant to Section 12 of the Exchange Act, like GX, to file accurate and not misleading quarterly reports with the Commission. GX failed to adequately disclose material events, trends, and uncertainties relating to its past and future financial condition and results of operations. GX thus failed to provide the context within which financial information should be analyzed. As a result, investors did not have the ability to judge the quality of GX’s financial results and the likelihood that its past performance would be indicative of future performance.

Specifically, GX omitted to disclose in its MD&A in the first and second quarters Forms 10-Q the reciprocal nature of a substantial amount of its IRU transactions, its increased use of reciprocal transactions, and its increasing reliance on such reciprocal transactions as a source of Cash Revenue and Recurring Adjusted EBITDA.

In addition, in presenting its statements of cash flows, GX omitted to disclose that the reciprocal transactions did not enhance GX’s liquidity from operating activities. By including reciprocal transaction sales in the cash flows from operating activities, GX reported cash flows from operating activities of a positive \$21 million for the first quarter and \$677 million for the first and second quarters. GX did not disclose in its statements of cash flows that a substantial amount of the cash flows from operating activities resulted from reciprocal transaction sales and that the reciprocal purchases were reported as part of cash flows from investing activities.

GX also omitted to disclose that in the reciprocal transactions, it often purchased capacity that would not be able to be integrated into its network, and thereby derive future service revenues, for some time. In particular, GX failed to disclose that in certain of these reciprocal transactions, GX had not completely negotiated important operational and business issues, including what was to be exchanged between the parties and when they were to do so; GX had purchased capacity that would not be ready for service until sometime after the quarter, and in some cases not for weeks, months or, occasionally, even a year or more; in the first quarter, GX had purchased capacity from another carrier that was then in severe financial difficulty and in danger of declaring bankruptcy; and GX had purchased capacity that GX could designate for use in the future.

The omitted information was material because it was necessary for a complete understanding of GX's financial results, the quality of its financial results, reasons for purchasing assets, and its ability to integrate the purchased capacity into the GX network and thereby derive future service revenues. Reasonable investors would have considered this information important in making an investment decision.

## **2. Casey, Cohrs, and Perrone**

Casey, Cohrs, and Perrone were a cause of GX's violations of Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder. Casey, Cohrs, and Perrone knew that a substantial amount of GX's IRU sales in the first and second quarters were part of reciprocal transactions and, as discussed above, that in certain of the reciprocal transactions, GX (1) had purchased capacity that would not be ready for service until sometime after the quarter; (2) in the first quarter, had purchased capacity from another carrier that was then in severe financial difficulty; (3) had purchased capacity that GX could designate for use in the future; and/or (4) had not completely negotiated important operational or business issues. Casey, Cohrs, and Perrone also knew that GX needed the reciprocal transactions to meet analysts' estimates for the first and second quarters of 2001. Despite knowing this information, they reviewed and approved the disclosure in the MD&A in the Forms 10-Q that omitted this material information.

### **E. GX'S COOPERATION**

During the course of its investigation, the Commission staff received significant cooperation from GX, including waivers of the attorney-client privilege concerning certain key transactions and the company's public disclosure process.

## **IV.**

In view of the foregoing, the Commission deems it appropriate to impose the sanctions specified in the Respondents' Offers.<sup>3</sup>

Accordingly, it is hereby ORDERED that:

A. GX cease and desist from committing or causing any violations and any future violations of Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder.

B. Casey, Cohrs, and Perrone cease and desist from causing any violations and any future violations of Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder.

By the Commission.

Jonathan G. Katz  
Secretary

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<sup>3</sup> Casey, Cohrs, and Perrone have each agreed to pay a \$100,000 civil penalty in connection with a parallel civil action.