

III.

FACTS

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

A. Summary

Between 1999 and 2001, William Olatin, Ashland Inc.'s Director of Environmental Remediation, reduced the cost estimates for remediating environmental contamination at dozens of chemical and refinery sites for which Ashland had responsibility. Ashland used those estimates to determine its environmental reserve, which Ashland disclosed in the periodic reports that it filed with the Commission. Olatin had no reasonable basis for reducing these cost estimates, which had been developed by a team of Ashland engineers, an outside consultant, and a computer program.

Ashland's process for setting its environmental reserve did not establish adequate guidelines for, or require documentation or review of, adjustments to the cost estimates. Ashland included the estimates that Olatin had reduced in its reported environmental reserve. As a result, Ashland materially understated its environmental reserve and overstated its net income in annual and quarterly reports filed from 1999 to 2001.

Ashland violated the reporting, books and records, and internal controls provisions of the Exchange Act, Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) and Rules 12b-20, 13a-1, and 13a-13 thereunder. Olatin caused Ashland's violations, and also violated Rule 13b2-1 of the Exchange Act.

B. Respondents

1. **Ashland Inc.** is a Fortune 500 chemical company incorporated in Kentucky. Ashland's common stock is registered with the Commission under Section 12(b) of the Exchange Act and is listed on the New York and Chicago Stock Exchanges under the symbol "ASH." During the relevant period, Ashland's primary businesses included chemical production and distribution, such as its Valvoline motor oil division, highway and bridge construction, and petroleum refining and marketing. Ashland is responsible for cleaning up environmental contamination at locations throughout the country. Ashland's fiscal year ends on September 30 and, in 2005, Ashland reported revenue of \$9.9 billion and operating income of \$746 million. Ashland's environmental reserve was a significant item in its financial statements from 1998 to 2005, ranging from a low of \$152 million to a high of \$178 million.

2. **William Olatin**, age 55, resides in Dublin, Ohio. Olatin was Ashland's Director of Environmental Remediation from 1996 until April 2006, when Ashland reassigned Olatin as a project manager within the Engineering Department. Olatin has a B.A. from Marietta College, Ohio in biology and geology and a B.S. from the University of Michigan in natural resources.

C. Relevant Accounting Principles

As a public company, Ashland is required to fairly, accurately, and timely report its financial results and condition. To ensure fair and accurate reports, the federal securities laws and the Commission's regulations require public companies, such as Ashland, to prepare and present their reports and financial statements in conformity with Generally Accepted Accounting Principles ("GAAP"). Under GAAP, items listed in financial statements must be reliable, *i.e.*, sufficiently faithful in their representation of the underlying obligations and sufficiently free of error and bias to be useful to others making decisions based on the financial statements.¹ Financial statements filed with the Commission that are not prepared in accordance with GAAP are presumed to be misleading or inaccurate. Ashland represented in its Commission filings that its financial statements complied with GAAP.

Ashland's expenditures for environmental compliance have a significant effect on its businesses. As required by GAAP, Ashland accrues an environmental reserve for future costs that it expects to incur to remediate contamination.² Ashland explained in its annual reports and the notes to its financial statements that the reserve reflects the company's "estimates of the most likely costs which will be incurred over an extended period to remediate identified environmental conditions for which the costs are reasonably estimable[.]"

D. Ashland's Process for Estimating the Environmental Reserve

From 1999 through 2001, Ashland's environmental remediation efforts were managed by the Remediation Group within the company's Environmental, Health and Safety Department ("EH&S"). As the director of Ashland's Remediation Group, Olatin was responsible for Ashland's determination of its future environmental liability. Olatin supervised a group of six environmental engineers who managed remediation at various sites and determined the initial liability estimates used to set the reserve.

Although Olatin was responsible for the accuracy of all estimates, Olatin's Remediation Group provided estimates for only some categories, including the chemical and refinery sites. For other categories, Olatin reviewed estimates forwarded to him by other Ashland divisions and consultants.

Olatin's Remediation Group used a "decision tree" method for determining the cleanup cost estimates for remediating the chemical and refinery sites. Each spring, the engineers in the

¹ FASB Concepts Statement No. 5, *Recognition and Measurement in Financial Statements of Business Enterprises*, paragraphs 63 and 75.

² Financial Accounting Standard No. 5, *Accounting for Contingencies* ("FAS 5"), requires Ashland to accrue for future remediation costs if it is probable that the company has incurred a liability and it can reasonably estimate the amount of the loss. The American Institute of Certified Public Accountants' Statement of Position 96-1, *Environmental Remediation Liabilities*, identifies future remediation costs that must be included in the company's environmental reserve, such as pre-cleanup activities and performance of remedial action.

Remediation Group met for two days with an independent, outside consultant to analyze each remediation site. Olatin did not participate in these sessions because of the independent consultant's concern that Olatin could bias the input of the engineers. At the sessions, the engineers presented possible remediation strategies for each site and the estimated costs for each remedy. The group critiqued each strategy and cost estimate. The independent consultant, who had a doctorate in engineering and 25 years of environmental remediation experience, facilitated the discussion by asking for justifications for the engineers' estimates and keeping the group within a set of "ground rules," which described the types of costs that should be accrued and listed assumptions that Ashland used in the process.

After the engineers reached a consensus for each site, the consultant entered the estimates into a computer program called "Crystal Ball," which generated a probability range of the total future cost estimates for each site. The Crystal Ball output was forwarded to Olatin for his review. Ashland considered it appropriate for Olatin to correct mistakes in the estimates or otherwise adjust them, as long as he had a reasonable basis for doing so. After his review, Olatin provided the cost estimates to an accountant who worked for Ashland as a contractor. The accountant compiled all estimates into a single report, which Olatin then forwarded to an assistant controller. The assistant controller used the estimates to determine Ashland's environmental reserve, which Ashland recorded in its books and records and reported in its Commission filings.

Ashland conducted this process once each year, and recorded any resulting change to its environmental reserve during the fourth quarter. In the first three quarters of each following year, Ashland carried forward the prior year's reserve estimate, after making adjustments based on expenditures during the quarter and any unusual developments.

E. Olatin's Reductions

Between 1999 and 2001, Olatin made multiple reductions to the cost estimates determined by the team of engineers and the independent consultant that Ashland used to set its environmental reserve. Olatin had no reasonable basis and no supporting documentation for these reductions, which generally were across-the-board reductions of various sites by the same large percentage.

In 1999, after reviewing the Crystal Ball output, Olatin directed the accountant to reduce by 25% the Crystal Ball calculations for fourteen of the chemical and refinery sites whose costs were estimated through the decision tree process – including seven of the ten largest sites. Olatin then directed the accountant to reduce the reserve for all chemical and refinery locations whose costs were estimated through the decision tree process (more than fifty sites) "across the board" by an additional 25%, including the fourteen sites already reduced. There is neither a documented basis for Olatin's reductions nor any evidence that each site's estimate was overstated by the same percentage.

Olatin's reductions decreased Ashland's reserve by over \$12 million, which reduced the reserve for Ashland's chemical and refinery sites whose costs were estimated through the decision tree process by 33% and decreased Ashland's total reserve by 6.9% to \$166 million. Ashland's annual report and financial statements for 1999 contained the misstated reserve. Olatin's reductions also increased Ashland's fourth quarter net income by 6.7%, to \$114 million.

In 2000, Olatin used a two-step process to adjust the estimates for more than 40 chemical and refinery sites whose costs had been estimated through the decision tree process. First, Olatin reduced the estimates for 20 sites by approximately 25%, and reduced the estimates for an additional five sites by approximately 44%, the equivalent of two 25% reductions. Olatin also reduced the estimates for nine sites, including three of the five largest, by 38% to 73% to round number estimates.³ Olatin also increased the estimates for five sites. Second, Olatin reduced the estimates for 38 sites by an additional 3%. Revised Crystal Ball data reflecting the first series of adjustments was maintained, but no documentation exists to justify the reductions, or to indicate that multiple sites were overstated by the same percentage.

Olatin's reductions in 2000 decreased Ashland's reserve by over \$12 million, which reduced the reserve for chemical sites whose costs were estimated through the decision tree process by 41% and reduced Ashland's total reserve by 7% to \$163 million. The adjustment also increased Ashland's annual net income before charges for one-time items for 2000 by 2.65% to \$292 million, and increased net income after charges for one-time items by 12.1% to \$70 million.⁴ The adjustment increased Ashland's fourth quarter net income by 9% to \$96 million.⁵

In 2001, Olatin made an across-the-board, 10% reduction to estimates for 40 sites, reducing the reserve by \$1,904,000 to \$176 million. There is no documentation supporting these reductions. Olatin's 10% reduction had the effect of keeping constant the total reserve for the chemical sites that he managed, and reduced Ashland's total environmental reserve by approximately 1%.

Olatin also considered both a 24% and a 10% reduction in 2002, but abandoned the planned reduction when Ashland's internal auditors commenced an internal audit at approximately the time the reduction would have been finalized. A week before the internal auditors interviewed Olatin, the Crystal Ball program was re-run to remove the planned adjustment.⁶

³ Olatin reduced three of the five largest estimates from \$2,968,000, \$2,446,000, and \$2,324,000 to \$800,000, \$1,000,000, and \$1,000,000, respectively.

⁴ Ashland incurred one-time charges in 2000 for a discontinued operation and debt retirement.

⁵ The 2000 adjustment was carried forward during the first three quarters in 2001. Ashland began disclosing its environmental reserve in quarterly reports in the second quarter of 2001. As a result, the reduction in 2000 decreased the environmental reserve that Ashland reported in its quarterly reports for the second and third quarters of 2001 by 7.5% in the second quarter and 6.3% in the third quarter.

⁶ Ashland's reserve for the chemical sites that were the subject of Olatin's reductions increased considerably when his reductions stopped after 2001. From 2001 to 2005, Ashland's reserve for the chemical onsite locations grew from \$18 million to over \$36 million.

F. Ashland's Internal Controls

During the relevant period, Ashland's internal controls for setting the company's environmental reserve depended on detailed, documented support for the engineers' estimates, as well as the peer critique session led by the independent consultant. Ashland maintained specific, written procedures describing this process. However, Ashland's internal controls were inadequate because they did not establish guidelines for, or require documentation or review of, adjustments to the engineers' cost estimates. Olatin helped design these controls.

Prior to 2001, Ashland's written procedures did not provide a process for adjusting the cost estimates generated by the Crystal Ball process. In 2001, Ashland changed the written procedures to indicate that the "management team" might adjust the estimates produced by the engineers. However, the revised procedures did not identify the "management team" and did not establish any guidelines setting forth when or how an adjustment could be made. In addition, unlike the documented, factual basis required for the original estimates, the procedures did not require documentation or review of any adjustments.

G. Ashland Receives Complaints in 2002

In 2002, three engineers who worked for Olatin raised questions about Olatin's conduct regarding the process of setting the environmental reserve in their confidential responses to an internal Code of Conduct Questionnaire and Certification Statement. One engineer specifically alleged, among other things, that Olatin was improperly reducing the reserve through "management adjustments."⁷

In response to these reports, Ashland's law department informed the internal audit department about the first engineer's complaints and asked it to conduct an audit. Consistent with the audit department's normal practice, the internal audit was designed to evaluate internal controls, not to determine whether Ashland's reserve conformed with GAAP. The internal auditors did nothing to familiarize themselves with the accounting rules for an environmental reserve.

The internal auditors reviewed only fiscal years 2001 and 2002, and discovered Olatin's 10% reduction in 2001. The auditors asked Olatin about the 2001 reduction, and Olatin said that he reduced the estimates because, in his judgment, they were approximately 10% too high and he did not have time for a site-by-site review. The auditors asked Olatin for documentation or other support for the reduction in 2001, but he said there was none. The auditors also reviewed individual adjustments that Olatin made in 2002, and asked Olatin and the remediation engineers responsible for the sites in question about the adjustments. Olatin explained the reasons for the adjustments, and the engineers agreed that the adjustments were proper. The auditors did not find the planned across-the-board reductions for 2002. The auditors concluded that the 10% reduction in 2001 (which amounted to less than \$2 million) was not quantitatively material and recommended changes to Ashland's environmental reserve process, including documentation and tracking of all changes to cost estimates, and review and approval by the engineers of any change made to site estimates. Ashland implemented these recommendations.

⁷ Olatin himself referred to his reductions as "management adjustments."

A few days after responding to a preview of the internal audit report, Olasin told the first engineer (whose identity he had learned) that his performance was suffering and that he should spend the weekend thinking about whether he wanted to stay with the company. The engineer ultimately left Ashland because he believed that he was being subjected to retaliation.⁸ Ashland learned about the engineer's concerns about retaliation, including Olasin's instruction that the engineer should consider whether he wanted to continue working at Ashland. Ashland did not discipline Olasin for this conduct, but his supervisor told him that it was wrong. In April 2006, after the Commission staff's investigation was complete, Ashland reassigned Olasin as a project manager within Ashland's Engineering Department and removed him from the reserve setting process.

H. Legal Analysis

1. Reporting Violations

Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder require issuers with securities registered under Section 12 of the Exchange Act to file annual and quarterly reports with the Commission, and the obligation to file such reports includes the requirement that they be true and correct. Rule 12b-20 further requires that such reports contain any additional information necessary to ensure that the required statements in the reports are not, under the circumstances, materially misleading. Financial statements in Commission filings that do not comply with GAAP are presumed to be misleading. Regulation S-X, 17 C.F.R. 210.4-01(a)(1).

GAAP required Ashland to maintain an environmental reserve, and Ashland identified the reserve in its Commission filings as important to its business. As discussed above, Ashland's annual reports and notes to the company's financial statements filed on Form 10-K for 1999 and 2000 materially understated Ashland's environmental reserve and overstated its net income. Ashland also materially understated the company's environmental reserve in its quarterly reports for the second and third quarters of 2001, filed on Form 10-Q. The misstatements ranged from 7% to 12%. As a result of this conduct, Ashland violated Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder. Olasin caused Ashland's violations by improperly reducing the cost estimates used to determine Ashland's environmental reserve.

2. Record Keeping and Internal Controls Violations

Section 13(b)(2)(A) of the Exchange Act requires Section 12 registrants to make and keep books, records, and accounts that accurately and fairly reflect the transactions and dispositions of their assets. Section 13(b)(2)(B) of the Exchange Act requires such registrants to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that, among other things, transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP and to maintain the accountability of assets. Exchange Act Rule 13b2-1 prohibits the direct or indirect falsification of any book, record, or account subject to

⁸ The engineer filed a complaint with the Department of Labor under the whistleblower protection provisions of Section 806 of the Sarbanes-Oxley Act of 2002, and eventually reached a settlement with Ashland.

Section 13(b)(2)(A).

Ashland violated Section 13(b)(2)(A) because its books and records contained inaccurate cost estimates that were used to determine the company's environmental reserve in fiscal years 1999, 2000, and 2001. Olasin caused Ashland's violations by reducing the cost estimates without a reasonable basis and documentation. Ashland's internal controls were deficient, and the company violated Section 13(b)(2)(B), because the company had no guidelines, documentation, or review requirements for adjustments of the cost estimates developed by the team of Ashland engineers. Olasin caused Ashland's violations because he helped design Ashland's controls for the decision tree process. By reducing the engineers' estimates without any reasonable basis, Olasin also caused Ashland's books and records to be falsified and thereby violated Exchange Act Rule 13b2-1.

IV.

UNDERTAKINGS

- A. Ashland undertakes to implement the following revisions that it has made to its policies and procedures for determining its environmental reserve:
1. Document all adjustments to the environmental remediation reserve estimates and the reasons for each adjustment to create a clear audit trail of the estimates.
 2. Retain all records relating to environmental remediation reserve estimates for a period of seven years following the period to which the reserve estimates relate.
 3. Require the manager of Ashland's Environmental Remediation Group, or his or her equivalent or successor, to consult with the remedial engineer or other individual responsible for the environmental remediation estimate for a given site before deciding whether to adjust the estimate of that site.
 4. Include in Ashland's Business Responsibility Questionnaire and Certification (or equivalent or successor document) sent to the Environmental Remediation Group and Accounting Department, or to their equivalents or successors, questions concerning whether the individual is aware of any failure to follow the Environmental Remediation Group's (or its equivalent's or successor's) reserve-setting procedures or of any misstatement in Ashland's books and records concerning any environmental remediation reserve.
 5. Conduct an annual best practices review with Ashland's outside auditor for the purpose of discussing and, when appropriate, modifying the company's policies and procedures for determining its environmental reserve, including the policies and procedures identified in this Section IV.A or instituted as a result of the undertaking identified in Section IV.C, below. This review

shall include a comparison of each site's reserve estimate to the site's annual budget and historical expenditures.

6. Require a report to Ashland's board of directors or an appropriate committee of the board on an annual basis regarding compliance with these provisions.
- B. Ashland undertakes to preclude Olatin from participating in the determination of Ashland's environmental reserve, the creation and maintenance of Ashland's books and records, and the preparation of Ashland's financial statements.
 - C. Ashland undertakes to retain PricewaterhouseCoopers LLP to review:
 1. Ashland's policies, procedures, and internal controls relating to the company's determination of its environmental reserve.
 2. Ashland's policies, procedures, and internal controls relating to solicitation and investigation of internal complaints, and measures to prevent retaliation against complainants.

Ashland will require PricewaterhouseCoopers to submit to the audit committee of Ashland's board of directors and the staff of the Division of Enforcement a written report fully documenting its findings and proposed recommendations. Within 90 days after receipt of such report, Ashland's audit committee, or board of directors, as appropriate, will adopt and implement such recommendations; provided, however, that as to any recommendation that Ashland believes is unduly burdensome or impractical, Ashland may suggest an alternative policy or procedure designed to achieve the same objective, submitted in writing to PricewaterhouseCoopers and the staff of the Division of Enforcement. Ashland will require PricewaterhouseCoopers to reasonably evaluate any alternative policy or procedure proposed by Ashland, and Ashland agrees that it will abide by the decision of PricewaterhouseCoopers regarding such alternative proposals.

V.

Based on the foregoing, the Commission finds that:

- A. Respondent Ashland violated Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder.
- B. Respondent Olatin violated Exchange Act Rule 13b2-1 and caused Ashland's violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder.

VI.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondents' Offers.

Accordingly, pursuant to Section 21C of the Exchange Act, it is hereby ORDERED, that:

A. Respondent Ashland cease and desist from committing or causing any violations and any future violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder.

B. Respondent Olatin cease and desist from committing or causing any violations and any future violations of Exchange Act Rule 13b2-1 and from causing any violations and any future violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder.

C. Respondent Ashland shall comply with its undertakings set forth in Section IV above.

By the Commission.

Nancy M. Morris
Secretary