

**UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF TEXAS  
HOUSTON DIVISION**

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**SECURITIES AND EXCHANGE COMMISSION,**

Plaintiff,

v.

**GARY V. MORRIS,**

Defendant.

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**COMPLAINT**

Plaintiff Securities and Exchange Commission (“Commission”) alleges as follows:

**SUMMARY**

1. Gary V. Morris, while serving as the Chief Financial Officer (“CFO”) of Halliburton Company (“Halliburton” or “the company”), was responsible for ensuring the accuracy and completeness of the financial information Halliburton disclosed to the public. During 1998 and 1999, Morris failed to discharge that responsibility. Along with others, Morris was responsible for Halliburton’s disseminating materially misleading financial information in its public filings with the Commission, in earning releases and in analyst teleconferences.

2. In the second quarter of 1998, Halliburton changed its accounting principles and practices, as well as its accounting estimates (hereinafter, collectively, “accounting change”) to recognize as income claims – arising from cost overruns – that Halliburton had not resolved with its customers. Previously, the company recorded income from a claim only after the claim was resolved with the customer. Since at least 1993, Halliburton had set forth this approach to recording income from claims in its periodic filings with the

Commission. The departure from Halliburton's prior conservative claims accounting resulted in enhanced income for Halliburton. For example, by including unresolved claims as income in its financial statements, Halliburton's audited pre-tax income for 1998 was 46% greater than it would otherwise have been without the claims.

3. Over six reporting periods, spanning approximately 18 months between 1998 and 2000, Halliburton failed to disclose the accounting change, or its impact on Halliburton's income. In the absence of any disclosure, the investing public was deprived of a full opportunity to assess Halliburton's reported income – more particularly, the reliability of that income, and/or its comparability to Halliburton's income in certain prior periods. It was not until March 2000 that Halliburton, in its 1999 Form 10-K, disclosed its accounting policy change.

4. From the second quarter of 1998 through the third quarter of 1999 (the "relevant period"), Morris was negligent in editing, signing, and causing to be filed with the Commission Halliburton periodic reports that failed to disclose the accounting change, and its impact on Halliburton's reported income. Morris was also negligent in causing the preparation of, and his review of earnings releases and analysts' teleconference scripts that failed to disclose the accounting change, and its impact on Halliburton's reported income.

5. In the interest of protecting the public against the reporting of misleading financial information by public companies, the Commission brings this action against Morris, seeking a civil injunction against future violations of the federal securities laws and a civil money penalty.

## **JURISDICTION AND VENUE**

6. This Court has jurisdiction over this action pursuant to Section 22(a) of the Securities Act of 1933 (“Securities Act”) [15 U.S.C. § 77v(a)] and Section 27 of the Securities Exchange Act of 1934 (“Exchange Act”) [15 U.S.C. § 78aa].

7. Venue lies in this Court pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Section 27 of the Exchange Act [15 U.S.C. § 78aa] because Halliburton is headquartered and Morris resides in Houston, Texas.

8. Defendant Morris has, directly and indirectly, made use of the means or instrumentalities of interstate commerce and/or the mails in connection with the transactions described in this Complaint.

## **DEFENDANT**

9. Morris, age 51, resides in Houston, Texas. Throughout the relevant period, Morris was an executive vice president and the CFO of Halliburton. As CFO, Morris was responsible for Halliburton’s accounting and financial reporting. During the relevant period, Morris was a licensed CPA.

## **RELEVANT ENTITY**

10. Halliburton is a Delaware corporation and its securities are registered with the Commission under Section 12(b) of the Exchange Act and trade on the New York Stock Exchange. During the relevant period, Halliburton had two primary reporting segments: the Engineering & Construction Group and the Energy Services Group, which was involved in the exploration, development and production of oil and gas. Brown and Root Energy Services (“BRES”) was a business unit of the Energy Services Group.

11. Halliburton conducted a debt securities offering pursuant to a Form 424B3 filed with the Commission on September 30, 1998. Halliburton also conducted a stock offering pursuant to a Form S-4, filed with the Commission on May 18, 1998. The Form 424B3 and Form S-4 incorporate by reference Halliburton's 1997 Form 10-K and Halliburton's Forms 10-Q for the second and third quarters of 1998. The material misleading statements and omissions, described below, were made in connection with Halliburton's offer or sale of the above-described securities.

## **FACTS**

### **Introduction**

12. During the relevant period, BRES conducted a substantial portion of its business using "fixed-fee" contracts. Fixed-fee contracts provide an agreed fee for all reasonable costs foreseen at the time of the contract's execution; the contractor's profit equals the margin by which the fee exceeds the contractor's costs. If costs exceed the fee, the contractor incurs a loss on the contract.

13. In mid-1997, BRES commenced several large fixed-fee Engineering, Procurement and Construction ("EPC") projects. The earliest of these projects involved the construction of a gas production plant in the Middle East at a cost of approximately \$169 million.

14. By the fourth quarter of 1997, BRES' cost overruns on the Middle East project resulted in Halliburton's recording \$20 million of losses in that quarter. The losses gave rise to a corresponding \$20 million reduction in Halliburton's fourth quarter 1997 operating income. BRES projected continued cost overruns on certain EPC contracts throughout 1998 and 1999.

### **Halliburton's Accounting Change**

15. For at least five consecutive years, dating back to 1993, Halliburton disclosed in its annual reports filed with the Commission (Forms 10-K) that "claims for additional compensation are recognized during the period such claims are resolved." Before a claim was resolved, the company recorded losses caused by cost overruns; the company recognized the claim as an offset against cost overruns only after the claim was resolved with the customer.

16. In the second quarter of 1998, the company implemented the accounting change by offsetting cost overruns on the BRES EPC contracts with estimated recoveries on claims that had not been resolved with customers. Although permitted under Generally Accepted Accounting Principles ("GAAP") in appropriate circumstances, this practice deviated from Halliburton's longstanding conservative practice of recognizing income only from resolved claims.

17. As a result of the accounting change, losses from cost overruns on several EPC contracts in the BRES business unit were reduced or eliminated.

### **The Accounting Change Increased Halliburton's Reported Income**

18. The undisclosed accounting change resulted in a material increase in Halliburton's publicly disclosed income, as reported in its public filings with the Commission (second and third quarter 1998 Forms 10-Q, 1998 Form 10-K, and first, second and third quarter 1999 Forms 10-Q). The change also resulted in more favorable quarter-to-quarter income comparisons between 1997 and 1998. The impact of the accounting change is set forth in the table below:

**Impact on Pre-tax Income (in millions)**

Year	Filing	Reported Pre-Tax Income	Reported Pre-Tax Income Without Component of Unapproved Claim Revenue	\$ Difference	% Difference
1998	Form 10-Q [Q2]	\$228.70	\$183.30	\$45.40	24.8%
	Form 10-Q [Q3]	(\$609.50)	(\$646.20)	\$36.70	5.7%
	Form 10-K	\$278.80	\$190.90	\$87.90	46.1%
1999	Form 10-Q [Q1]	\$149.00	\$129.80	\$19.20	14.8%
	Form 10-Q [Q2]	\$146.00	\$135.80	\$10.20	7.5%
	Form 10-Q [Q3]	\$103.00	\$92.30	\$10.70	11.6%

**Halliburton did not Disclose the Accounting Change**

19. From the second quarter of 1998 through the filing of Halliburton's 1999 Form 10-K in March 2000, Halliburton, through Morris and/or those acting at his direction, failed to inform the investing public of the accounting change.

20. In its 1999 Form 10-K, Halliburton first informed investors that the unresolved claims on the BRES EPC contracts were a component of the company's earnings. In the prior six quarters, none of Halliburton's periodic Commission filings disclosed the accounting change, or its impact on the company's income.

21. Additionally, in Halliburton's 1998 Form 10-K, the company removed the claims recognition statement that had appeared in earlier Halliburton Forms 10-K. Halliburton did not explain in the filing, or in any other public statement, the reason for its removal. Moreover, Halliburton did not, in its 1998 Form 10-K, replace the claims recognition statement with a disclosure of the company's accounting change.

22. Halliburton's statement of its historical claims recognition practice was not expunged from the mix of public information, because Halliburton incorporated the statement by reference in its Forms 10-Q for the second and third quarters of 1998. Thus,

the only statement of Halliburton's claims recognition practice in the public domain during the second and third quarters of 1998 was that the company recognizes claims "during the period such claims are resolved." This statement of accounting practice, out-of-date with respect to the BRES EPC contracts, was incorporated by reference in, and rendered materially misleading the public information Halliburton issued regarding its income in its second and third quarter 1998 Forms 10-Q, earnings releases and analysts' teleconferences.

### **Misleading Statements and Omissions**

23. Morris was responsible for ensuring the accuracy of Halliburton's periodic reports, which he reviewed, edited and signed during the relevant period. Morris, however, failed to ensure that Halliburton disclosed the accounting change, and its impact on Halliburton's income. He also failed to ensure that Halliburton's former claims recognition policy was not incorporated by reference in its second and third quarter 1998 Forms 10-Q.

24. Morris was responsible for the failure of Halliburton's second and third quarter 1998 Forms 10-Q, 1998 Form 10-K, and its 1999 Forms 10-Q to conform with the requirements of the Commission's Regulation S-X. Specifically, Regulation S-X required the disclosure of the accounting change. The failure to disclose the accounting change, and correlated failure to comply with Regulation S-X, gave rise to a material omission that caused Halliburton to be in violation of the Commission's reporting provisions under Section 13(a) of the Exchange Act, and in violation of rules promulgated thereunder.

25. Moreover, Morris was responsible for the material misrepresentation, in Halliburton's second and third quarter 1998 Forms 10-Q, 1998 Form 10-K, and its 1999

Forms 10-Q, that the disclosures in the filings were prepared in accordance with GAAP and Regulation S-X. In fact, the disclosures in the filings were not prepared in accordance with the disclosure requirements of GAAP and Regulation S-X, due to the company's failure to disclose the accounting change. These disclosure requirements of GAAP and Regulation S-X include, without limitation: the American Institute of Certified Public Accountants' Statement of Position ("SOP") 81-1(.65); the Accounting Principles Board Opinion ("APB") No. 20; and Rule 4-01(a)(1), Rule 10-01(a)(5), and Rule 10-01(b)(6) of Regulation S-X. The material misrepresentation, that the disclosures in Halliburton's filings were prepared in accordance with GAAP and Regulation S-X, was materially misleading, and caused Halliburton to be in violation of the Commission's reporting provisions under Section 13(a) of the Exchange Act, and in violation of rules promulgated thereunder.

26. During the second and third quarters of 1998, Morris and others prepared Halliburton's earnings releases and analyst teleconference scripts. The documents contained materially misleading information about the company's income in those quarters. Moreover, Morris attended the teleconferences, at which the company's president read aloud the misleading information in the scripts regarding the company's income. Morris never cautioned the president about the misleading statements, either before or after a teleconference; nor did Morris recommend a retraction or corrective statement.

#### ***The Second Quarter 1998 Form 10-Q***

27. Halliburton's Form 10-Q for the second quarter of 1998, filed on June 30, 1998, did not disclose that the offset of cost overruns by unresolved claims resulted in

income to the company in the second quarter 24.8% greater than without the offset. In addition, the Income Statement in the filing reflected a 34% quarter-to-quarter increase in Halliburton's net income during 1997-1998; without taking into account unresolved claims, the quarter-to-quarter increase would have been only 6.7%. The company also stated in the filing's "Results of Operations" discussion that Energy Services Group (the division encompassing BRES) experienced a 24%, quarter-to-quarter increase in operating income from 1997-1998. The filing contained no disclosure that, without unresolved claims, Energy Services Group's operating income would have actually decreased 4.5%.

### ***The Second Quarter 1998 Earnings Release***

28. The second quarter earnings release dated July 22, 1998, omitted the same information as the second quarter Form 10-Q. The company's second quarter 1998 earnings release, issued July 22, 1998, is entitled: "Halliburton 1998 Second Quarter Net Income Up 34 Percent." As previously mentioned, without unresolved claims, Halliburton's net income increased only 6.7%. The company also stated in the release: "The Energy [Services] Group's 1998 second quarter operating income increased 24 percent to \$198.3 million compared to the prior year period." The release contained no disclosure that, without unresolved claims, the Energy Group's operating income actually decreased 4.5%.

29. Halliburton also stated in the earnings release, "for the six-month period ending June 30, 1998, net income increased 38% to \$254.3 million." The release contained no disclosure that without unresolved claims, net income over the six-month period would have increased only 22.4% in 1998, as compared to 1997, not 38%.

30. The company further stated in its second quarter earnings release that "Halliburton Company report[ed] 1998 second quarter net income of \$136.5 million (\$.51

per share diluted), an increase of 34 percent compared to \$101.9 million (\$.40 per share diluted) earned in the 1997 second quarter.” The earnings release contained no clarification that, without unresolved claims Halliburton’s earnings-per-share would have been \$.41, not \$.51, which was the analysts’ consensus earnings-per-share estimate.

### ***The Second Quarter 1998 Analyst Teleconference***

31. The company’s statements in the second quarter analyst teleconference conducted on July 22, 1998, which were based on a prepared script, omitted material information regarding unresolved claims as an offset against cost overruns. The company stated that its net income “was up 34%” as compared to the second quarter of 1997. But without unresolved claims, Halliburton’s net income in the quarter increased only 6.7%.

32. The company also indicated in the teleconference that the Energy Services Group’s second quarter 1998 operating income increased 24% to \$198.3 million, compared to the second quarter of 1997. The public was not told that without unresolved claims, the Energy Services Group’s operating income would have actually decreased 4.5%, as compared to the second quarter of 1997.

33. Halliburton further claimed that the company’s earnings-per-share for the quarter was \$.51. The company failed to disclose that without unresolved claims, Halliburton’s earnings-per-share would have been only \$.41.

34. The company also reported in the teleconference BRES’ operating results. The company stated that BRES’ operating income had increased 40% over the second quarter of 1997. There was no disclosure that without unresolved claims, BRES’ operating income would have actually decreased approximately 148%. Moreover, the company

failed to clarify that the 5.5% operating income margin for BRES would have been -2% without unresolved claims.

### ***The Third Quarter 1998 Form 10-Q***

35. Halliburton's Form 10-Q for the third quarter of 1998, filed on September 30, 1998, did not disclose that the offset of cost overruns by unresolved claims resulted in income to the company in the third quarter 5.7% greater than without the offset. In addition, the company included in the Management Discussion & Analysis section of the filing, entitled "Results of Operations," a statement that "Energy Services Group's operating income decreased 8% to \$262.7 million in the third quarter of 1998 compared with \$287 million in the same quarter of the prior year." There was no disclosure in the Form 10-Q that without the unresolved claims, the Energy Services Group's operating income would have actually decreased 21% in 1998, compared to the third quarter of 1997.

### ***The Third Quarter 1998 Earnings Release***

36. The third quarter earnings release dated October 29, 1998, omitted the same information as the second quarter Form 10-Q. In the earnings release, the company states: "The Energy Services Group's 1998 third quarter operating income was \$263 million, off eight percent from the 1997 quarter." The release contained no disclosure that without unresolved claims, Energy Services Group's operating income would have decreased 21% to \$226 million.

37. The company also stated in the release: "Halliburton Company announces that the company earned \$195 million (\$.44 per diluted share) in the 1998 third quarter, compared to \$218 million (\$.50 per diluted share) in the 1997 third quarter, before

recognition of special charges.” The company did not mention in the release that without unresolved claims, Halliburton would have earned only \$172 million – a difference of 13.3%. And the earnings release contained no clarification that, without unresolved claims Halliburton’s earnings-per-share for the quarter would have been \$.39, not \$.44, which was the analysts’ consensus earnings-per-share estimate.

### ***The Third Quarter 1998 Analyst Teleconference***

38. The company’s statements in the third quarter analyst teleconference, conducted on October 29, 1998, and again based on a prepared script, omitted material information regarding the unresolved claims component of Halliburton’s earnings. The company stated: “from an operating income standpoint for the Energy Services Group, operating income declined 9% to \$263 million for the quarter.” Investors were not told that without unresolved claims, the Energy Services Group’s operating income would have declined 21%.

39. The company also reported “our [Halliburton’s] earnings per share were \$.44.” The company failed to disclose that, without unresolved claims, Halliburton’s earnings-per-share would have been only \$.39.

40. The company further stated at the teleconference, “revenues for this group [BRES] are up 33%. We continue to be very, very pleased with the direction and growth of this aspect of our business even in a down market. And I think it [BRES] continues to be one of the real hidden stars within the Halliburton portfolio of businesses that we have.” The company did not mention that unresolved claims, which offset cost overruns, were a positive component of Halliburton’s earnings.

41. The script further stated “for [BRES], operating income increased 17% over the prior year. Margins are now starting to get back into the territory that we thought they would toward the end of the year with its [BRES’] margins for the third quarter being 8.6%.” There was no disclosure that, without unresolved claims, BRES’ operating income would have actually decreased approximately 54% (from \$52.7 million to \$24 million), not increased 17% (from \$52.7 million to \$60 million). Moreover, without unresolved claims, BRES’ operating margins would have been only 3.6%.

### **1999 Forms 10-Q**

42. In each of Halliburton’s 1999 quarterly filings with the Commission, the company continued to include unresolved claims as income without disclosing the accounting change.

43. Similar to its filings in 1998, Halliburton’s first, second and third quarter Forms 10-Q for 1999 also included income from unresolved claims. For example, in the 1999 first quarter Form 10-Q, Halliburton included \$19.20 million of unresolved claims or 14.8% of reported pre-tax income; the 1999 second quarter Form 10-Q included \$10.20 million of unresolved claims or 7.5% of reported pre-tax income; and the 1999 third quarter Form 10-Q included \$10.70 million of unresolved claims or 11.6% of reported pre-tax income.

### **Halliburton’s Ultimate Disclosure Was Misleading**

44. Ultimately, in the 1999 Form 10-K Halliburton filed with the Commission on March 14, 2000, Halliburton disclosed for the first time the change it had made, six quarters earlier, in its accounting for unresolved claims. In the filing, the company stated

that, in 1998, the company accrued \$89 million in unresolved claims, and in 1999, \$98 million in unresolved claims.

45. The company, however, did not disclose in the 1999 Form 10-K \$34 million of unresolved claims that the company recognized in 1999 in connection with joint venture projects. This omission flattened the ascending curve of unresolved claims recognized by the company: instead of reporting \$132 million in unresolved claims in 1999, the company reported \$98 million – a \$9 million, as opposed to \$43 million increase over the 1998 figure.

### **FIRST CLAIM**

#### **Violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act**

46. Paragraphs 1 through 45 are realleged and incorporated by reference.

47. Morris, directly or indirectly, singly or in concert with others, in the offer or sale of securities, by the use of means or instruments of transportation or communication in interstate commerce, or by the use of the mails, has: (1) obtained money or property by means of untrue statements of material facts or omissions of material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; and (2) engaged in transactions, practices or courses of business, which operated or would operate as a fraud or deceit upon the purchaser.

48. Morris engaged in the above-referenced conduct in a negligent manner.

49. By reason of the foregoing, Morris violated Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)].

## SECOND CLAIM

### **Aiding and Abetting Halliburton's Violations of Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1 and 13a-13 Thereunder**

50. Paragraphs 1 through 45 are realleged and incorporated by reference.

51. Section 13(a) of the Exchange Act [15 U.S.C. §78m(a)] requires issuers such as Halliburton to file periodic reports with the Commission containing such information as the Commission prescribes by rules and regulations. Exchange Act Rule 13a-1 [17 C.F.R. § 240.13a-1] requires issuers to file annual reports and Exchange Act Rule 13a-13 [17 C.F.R. § 240.13a-13] requires issuers to file quarterly reports. Under Exchange Act Rule 12b-20 [17 C.F.R. § 240.12b-20], the reports must contain, in addition to information expressly required, such further information as is necessary to ensure that the statements made are not, under the circumstances, materially misleading.

52. Based on the conduct alleged herein, Halliburton violated Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)], and Rules 12b-20, 13a-1, 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-13] thereunder.

53. Morris, acting alone or in concert with others, in the manner set forth above, knowingly provided substantial assistance to Halliburton in its violations of, and thereby aided and abetted Halliburton in its violations of, Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 12b-20, 13a-1 and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1 and 240.13a-13].

## PRAYER FOR RELIEF

The Commission respectfully requests that the Court:

**I.**

Find that Morris committed the alleged violations.

**II.**

Permanently restrain and enjoin Morris from violating, or aiding and abetting, directly or indirectly, the provisions of law and rules alleged in this Complaint.

**III.**

Order Morris to pay a civil money penalty, plus post-judgment interest, pursuant to Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)] and Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)] in an amount to be determined by the Court.

**IV.**

Grant such other relief as to which the Commission shows itself entitled and this Court deems just or appropriate.

Respectfully submitted,

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