

# THE FINANCIAL COLLAPSE OF ENRON—Part 1

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HEARING  
BEFORE THE  
SUBCOMMITTEE ON  
OVERSIGHT AND INVESTIGATIONS  
OF THE  
COMMITTEE ON ENERGY AND  
COMMERCE  
HOUSE OF REPRESENTATIVES  
ONE HUNDRED SEVENTH CONGRESS  
SECOND SESSION

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# THE FINANCIAL COLLAPSE OF ENRON—Part 1

TUESDAY, FEBRUARY 5, 2002

HOUSE OF REPRESENTATIVES,  
COMMITTEE ON ENERGY AND COMMERCE,  
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS,  
*Washington, DC.*

The subcommittee met, pursuant to notice, at 10 a.m., in room 2322, Rayburn House Office Building, James C. Greenwood (chairman) presiding.

Members present: Representatives Greenwood, Stearns, Burr, Whitfield, Bass, Tauzin (ex officio), Deutsch, Stupak, DeGette, John, Rush, and Dingell (ex officio).

Also present: Representatives Barton and Green.

Staff present: Tom DiLenge, majority counsel; Mark Paoletta, majority counsel; Michael Geffroy, majority counsel; Jennifer Safavian, majority counsel; Casey Hemard, majority counsel; Brendan Williams, legislative clerk; William Carty, legislative clerk; Peter Kielty, legislative clerk; Chris Knauer, minority counsel; and John Cordone, minority counsel.

Mr. GREENWOOD. This hearing of the Energy and Commerce Committee, the Subcommittee on Oversight and Investigations will come to order. The Chair recognizes himself for purposes of an opening statement.

Today, we engage in the first part of a multi-day hearing into the financial collapse of the Enron Corporation. The principal focus of this stage of our investigation will be a series of transactions between Enron and several partnerships created and controlled by senior Enron officers and employees. By now, some key events that precipitated Enron's collapse have become familiar, though not yet fully understood by the public. These events serve as the point of entry into our hearing today.

In October, Enron, which until recently was considered to be one of America's largest and most profitable corporations, announced an unexpected after-tax charge against earnings of more than \$500 million and a reduction in shareholder equity of more than \$1 billion. The losses stem from Enron's transactions with an entity about which we will hear a great deal over the next few days: LJM2. It was an entity whose name was formed using the initials of the spouse and children of its creator, Andy Fastow, who at that time was Enron's chief financial officer.

The news of this financial bombshell and the curious role played by Enron's CFO in it prompted immediate concern in the market and in the media and resulted in the SEC opening an inquiry into the transactions involving LJM2. Enron's CFO was put on leave

and subsequently fired, in Ken Lay's words, quote, "To restore investor confidence."

Already reeling from this management debacle and with its stock trading at sharply lower levels, Enron suffered an even greater embarrassment when in November of last year the corporation was obligated to restate its financial statements for the years 1997 through 1999. Now, instead of showing a strong balance sheet, the company was reporting multibillion dollar losses in earnings and in equity. The accounting practices, behind which these losses had until then been hidden, had also been used to mask huge losses in two other partnerships inspired by Mr. Fastow. These were the LJM Cayman partnership, also known as LJM1, and yet another related party entity, known as Chewco Investments.

The second admission by Enron's corporate team effectively forfeited any remaining market for investor confidence in the company. Enron's stock took its final plummet, forcing yet more debts to come due. In a matter of weeks, a firm which had until only recently been hailed as a shining example of American enterprise was now forced to declare bankruptcy. An astounding \$70 billion in market value evaporated seemingly overnight, bringing financial ruin to thousands of employees and investors.

In recent weeks, committee investigators have sorted through Enron's wreckage, and in particular the Chewco, LJM1, LJM2 and associated deals, to learn what happened. We have discovered that while thousands of hardworking employees suffered terribly, there was a small group at the top who carted away millions from these very deals that ultimately led to Enron's collapse. And we have discovered a disturbing pattern of activity that directly contributed to the demise of this company: a web of apparent misrepresentations, half truths, deceit and self-dealing in which a significant number of company leaders became entangled.

You will have an opportunity to hear explanations from some of those in positions of responsibility at the continuation of this hearing on Thursday, but today we will focus on the findings of Enron's Special Investigative Committee. The Special Investigative Committee was set up by Enron's Board of Directors to conduct an independent examination of the very transactions the committee is now investigating. Its 200-page report released over the weekend draws a very disturbing picture of Enron's activities which, sadly, appears to confirm our own findings to date.

The report describes a series of highly questionable transactions that enriched a small number of corporate bigwigs at the expense of the company and of its shareholders. More disturbing still, it describes a complicated set of transactions by these individuals which were portrayed at the time as actions designed to guard against Enron's future losses. But its own true purpose was to hide large and increasingly unmanageable amounts of debt and liability.

The report uses the word "obtuse" to describe investor disclosures that failed miserably to accurately convey the true financial state of the company or the risks attendant to the off-the-book dealings with various partnerships. It exposes a troubling lack of governance and management oversight and the failure on the part of outside advisors, the accountants and legal experts responsible for evaluating these transactions to make clear to investors what inde-

pendent experts now comprehend. Enron's accounting tactics went well beyond the aggressive, apparently violating or circumventing several of the accounting professions most basic rules.

Clearly, there is much troubling information in this report for us to consider as we move forward. Our sole witness today is William C. Powers, Dean of the University of Texas Law School. Dean Powers was appointed to Enron's Board of Directors just this past October to Chair this special committee. He has graciously accepted our invitation to testify as to the report's troubling findings. I am certain that Dean Powers' informed testimony will contribute to the factual backdrop for subsequent hearings with current and former Enron and Andersen officials. I thank him for his hard work in preparing this report in such an expedited time schedule and for his testimony today.

The Chair recognizes the ranking member of this subcommittee, the gentleman from Florida, Mr. Deutsch.

Mr. DEUTSCH. Thank you, Mr. Chairman, and I want to thank you for holding this very important hearing, and I also want to thank our staffs, both the majority and minority, who are working very closely together. We actually know more than we knew last week when this subcommittee held the first hearing on the demise of Enron, and I am sure we will know more by the end of the week as well.

This is some of the things that we are disclosing—or uncovering at this point in time. This is from Enron's documents that our staff uncovered, and it is a simplified diagram of 1 of the 4,000 partnerships. I mean a simplified diagram is almost comical to try to understand that one partnership.

You know, I have had the opportunity to read through a large part of the report, as well as the summary, and obviously it is extensive. It is extensive in terms of understanding of what happened, but I am going to quote from something I read this morning that Arthur Levitt (ph) just wrote: "Yet for all their excesses, analysts don't have a fiduciary duty to shareholders; board of directors do." Enron's board failed the smell test. Millions lost money and careers were destroyed while the company and its directors began to question mutual beneficial arrangements.

The SEC and stock exchanges must now revisit the issue of board and audit committee responsibility. Consulting contracts for directors should be barred as well as seductions in the form of corporate jet usage and support for directors' favorite charities. Most important, at least half of every board must be independent by the most rigorous definition of the term.

I think what we know at this point is that these partnerships were used as a deception for people to understand what the status of the company was. And what this report, Mr. Powers' report, does is lays out some of these interlocking relationships between management and people who got direct benefits by these partnerships. And one of the questions—and it is not just understanding Enron, but I think the issue for the committee and for the Congress and really beyond that, for the country as well, is, No. 1, are there other Enrons out there? Because if Enron and the people involved in Enron figured out the use of these partnerships as a way to effectively get millions, in fact, collectively, billions of dollars in per-

sonal theft, then the motivation is probably out there for other companies to be doing the same thing.

But the system should not allow it. I mean I think what is clear from your report is that both management and the board of directors had to have been knowing what was going on. And, in fact, if officers claim they don't know the truth, they are not telling the truth. No one has ever accused these people of being stupid.

Now, Business Week recently wrote, "This is corruption on a massive scale. Tremendous harm has befallen innocent employees who have seen their retirement savings disappear as a few at the top cashed out. Terrible things have happened to the way business is conducted under the scope of deregulation. Serious damage has been done to ethical codes of conduct held by once trusted business professionals."

It is difficult not to contrast professionalism of modestly paid fire fighters and police doing their duty on September 11 with the secretive and squirrely behavior of 6- and 7- figure accountants, lawyers, CEOs, bankers, financial analysts who failed at their duty with Enron. And, again, I emphasize their duty because the system is set up for this never to have happened in the first place.

Mr. Chairman, after reading this report, I do not believe that Enron can emerge from bankruptcy until its entire top management has been removed. They all played a role in creating the environment that allowed this debacle, and they cannot be expected to now change their stripes.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the chairman of the full committee, the gentleman from Louisiana, Mr. Tauzin.

Chairman TAUZIN. Thank you, Mr. Chairman, and my particularly thanks, first, to Mr. Dingell again for the extraordinary corroborative work that our investigative teams are doing in a bipartisan fashion on this issue, and to Dean Powers for taking on this awesome responsibility and for executing within the limits of his capabilities. We have noted very carefully you had not the power to subpoena or to compel testimony of witnesses or documents. You didn't have access to all the partnership papers, and you mentioned that your report is only as good as the information provided to you. But you have done an excellent job and your report tracks what our investigators on both sides of the aisle are finding in this case, and I want to thank you for that.

But what you have basically found, and we will get into it a lot more tomorrow and Thursday, is an aberration, I hope, in American corporate history, an extraordinary aberration. But it is an old story. It is a story of insider theft, just using new wrapping and new forms and procedures to carry it out. It is a story, as you point out over and over again in your report, of the failure to follow accounting principles, to circumvent the accounting principles, to organize these structures improperly. Time after time you talk about the fact that had they followed the rules this wouldn't have happened, that Chewco was improperly constructed and JEDI failed for the same reason, and all of these structures that were created to put debt off the balance sheets ended up being shams at the end, because they didn't follow the integrity of the accounting principles

that everyone else in the country, every other corporation in American tends to follow.

I want to use the rest of my time in opening, Mr. Chairman, however, to speak directly to Mr. Ken Lay. Mr. Lay, wherever you are, I am sorry your attorneys were offended by anything Mr. Dorgan and I had to say on Meet the Press this weekend. I have got a little excuse for being tired. I got rear-ended by a drunk driver that night and then attended the Washington Mardi Gras until 2 a.m. in the morning before I read your report, Mr. Powers. But Mr. Dorgan was not tired, and neither he nor I misstated the facts.

Your report, Mr. Powers, points to the high probability of security fraud at Enron. And your report lays the blame for what happened on a host of parties, and you didn't leave Mr. Lay out. You reminded him of his responsibility as the head of the organization, to be a better supervisor, to actually know what was going on if he didn't.

And I am sorry if that offended your lawyers, Mr. Lay, but let me, please, ask you to consider for your own good, if when Sherron Watkins reported to you in August of 2001 in a lengthy meeting that Enron was about to implode in an accounting scandal, if Sherron Watkins was kind enough to tell you in that memo in 2001 in a private meeting with you, Mr. Lay, that your company had been robbing the bank and for the last 2 years was trying to pay it back, that is how bad things were, that is how big the cancer was eating away at the Enron Corporation, its employees and everyone who counted and trusted in it and invested in it, if that wasn't enough for your lawyers to be concerned about your testimony before a congressional committee, get yourself some new lawyers, sir.

If when the SEC announced it was beginning an informal inquiry and then a formal inquiry into the operations of the security trading at Enron and the sham proceedings that went on there, if your lawyers weren't sufficiently concerned about your potential liability and involvement in this matter, get yourself some new lawyers, sir.

If when the Justice Department announced that it was conducting a formal Justice inquiry into illegalities, potential illegalities at Enron and when the FBI arrived in Houston to look at your books and at Arthur Andersen books only to find out that Shredco had been hired by Enron to destroy documents and Enron's officials—Arthur Andersen officials, rather, had put out a retention and destruction policy that went right through the SEC subpoena, if that wasn't enough to warn you and your attorneys that there was real problems for all of you, get yourself some new attorneys.

And if when Dean Powers, hired by Enron, by you and the Board of Directors at Enron to find out what went wrong and who wrote this report indicating that accounting principles were ignored, circumvented and violated right and left in all these dealings and the American public was told that you had a billion dollars of income you didn't have and debt was hidden from investors who should have known that the value at Enron wasn't there, if all of that wasn't enough for you to understand you had legal problems, and testifying in front of Congress was a risky business, then get yourself some new lawyers.

And I have got a suggestion for you. Maybe your family is right, maybe you are broke, and maybe you can't afford to hire some law-

yers, maybe you can sell a house in Aspen and buy yourself some new lawyers. But if that doesn't work, maybe you ought to get a hold of Mr. Fastow and Mr. Skilling and they can put together another little partnership for you and get some investors in and get yourself some lawyers, sir, because somebody is going to need some lawyers in this case, somebody needs them desperately. And it took Mr. Dorgan and I on Meet the Press to say the obvious, that the Powers report indicates the high probability of security fraud in this case, this awful aberration in corporate America, that accounting principles were flaunted, ignored and circumvented right and left to the detriment of every investor and every employee of this company, if it took that, if took Mr. Dorgan and I saying that on television for you to understand that you were at some risk coming to testify in Congress without the benefit of legal counsel or perhaps even the Fifth Amendment, then get yourself some new lawyers, sir.

Mr. Powers, thank you for your contribution. As you point out, this is just the beginning. Your report would change dramatically if you had all the facts. We have got the advantage of subpoena power, we have got the advantage of compelling the production of documents, those that haven't been destroyed, and we are going to find out who owns those partnerships and those special entities, and we are going to find out what happened, because we have some powers working with the FBI and the SEC that perhaps you didn't have. But you did a heck of a job for us already, and we thank you for it. Thank you.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes for an opening statement the ranking member of the full committee, Mr. Dingell.

Mr. DINGELL. Mr. Chairman, thank you for the courtesy. I commend you again for this hearing, and it is my hope that this hearing will lead to a complete inquiry into the matters that are now before us, including legislative and administrative changes that need to be made in the process.

I wish to begin by thanking you, Mr. Powers, and your counsel for presenting a very useful report on the related party transactions and other matters. You have done a fine job. I am troubled that some of those who were involved refuse to cooperate. I believe that raises questions into which the committee must go. I am also concerned about the limitations raised by the participation of Mr. Herbert Winokur, a long-time director. I will note the report is a devastating document. It outlines an extraordinary web of corporate chicanery and deceit. It provides a very useful starting point for this committee and a significant road map for this committee's efforts to unravel this sorry mess.

I will observe that it reminds me of what used to be said by one of baseball's greats, "This is deja vu all over again." It brings me back to the days of Mr. Sam Insel and also, perhaps, to Mr. Ponzi and other people of this kind. For those who don't remember Mr. Insel, and I have only vague remembrance of him, he was a fellow who built enormous pyramids, which he built and milked for the benefit of himself and his friends. It led to significant changes in the law, including the creation of the SEC, the passage of the different securities laws, the Public Utility Holding Company Act and

a wide array of other statutory changes to protect investors, consumers, employees and pensioners. And it looks like something of that kind has to be done again to address the efforts of those who have brought Enron, its investors, its employees, and its pensioners to such a sorry state today.

Your report, in often numbing detail, describes some of the financial sleights of hand that Enron executives used to hide the result of either stunningly inept business decisions or outrageously corrupt behavior by themselves and their friends. It also describes the disgusting self-enrichment by senior executives who sold out their fiduciary duties to the shareholders. And, it describes an extraordinary laxity, if not worse, of those responsible for keeping such behavior in check.

One must ask, how were senior Enron executives able to use the company as their personal financial plaything? First, because of a massive failure of corporate governance. Was the highly paid board of directors simply asleep, or was it corrupt, or was it both? Second, because of an extraordinary failure by accounting and legal professionals to provide objective, independent, and forceful advice. Why were they acting like trained seals to the management? Again, were they incompetent, were they corrupt? We hope that this proceeding and others will lead us to some intelligent answers. Third, because of a massive failure by so-called experts in the credit rating agencies, the investment banks and the brokerage houses. Why didn't they ask tough questions?

What we learn today will set the stage for a much more extensive inquiry into these matters. For example, we will also need to learn much more about whether weakness in government regulation of markets for financial instruments and vital commodities may have allowed this rascality to flourish. And we will need to re-examine the special protections that the Congress provided accountants in the Private Securities Litigation Reform Act of 1995, which came forth from this committee with the enthusiastic support of some of the people who are still on the committee. I am sure that they will enjoy explaining their support of that proposal and also their support of proposals which have constrained the SEC in its efforts to lead to a more vigorous, truthful, effective, and public accounting industry.

In any event, Mr. Powers, we are grateful to you for a very useful report, and for your appearance here today. Mr. Chairman, I thank you.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentleman from North Carolina, Mr. Burr, for an opening statement.

Mr. BURR. Thank the chairman. Dean Powers, welcome.

Mr. POWERS. Thank you.

Mr. BURR. This almost makes law school seem fun, doesn't it? Clearly, you have gone through some tough changes since October; so have the employees of Enron and the confidence of the investor in America. Let me commend you for the work of your committee.

I think there were many that thought that reports that came out on Enron's downfall might have a lot to do about the definition of shredding or the definition of revenues or debt. And in fact what you found in your investigation, the only 3 months it took, was

more than, in fact, the auditors found in 4 years. It took them 4 years to make some of the changes that you identified in 3 months. It took the Enron management 4 years to fess up to real revenue and debt numbers that you found accurately in a three-month period. These revisions contributed greatly to the lack of confidence that the investors had in Enron as a company.

I am convinced that there was one thing that you did uncover: That at Enron there was a two-headed coin. On both sides of that coin was Mr. Fastow. No matter how you flipped it he always won. He won because of his presence at Enron, he won because of his presence at the partnerships that were created, and Mr. Fastow apparently looked after one person, that person who was on both sides of that coin. He profited when everybody else lost. Mr. Kopper profited when everybody else lost. A select few profited when everybody lost.

I am confident that this committee and this Congress will not quit until we get all the facts. I am confident that the law enforcement that is appropriate will not quit until they find the guilty parties. I am confident that it is not going to be fun to be a board member at Enron during that period. But I want to thank you for your willingness to go through the process that you have just gone through and to encourage you to be diligent as we complete this process, however long it takes. Thank you, Dean Powers.

Mr. POWERS. Thank you.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentleman, Mr. Stupak, for an opening statement.

Mr. STUPAK. Thank you, Mr. Chairman. Mr. Chairman, 2 weeks ago, we heard from Arthur Andersen and their role about shredding documents associated with the collapse of Enron. Today, we hear from Mr. Powers about many of the questionable and oftentimes repulsive financial dealings that occurred within Enron leading up to their bankruptcy. Mr. Chairman, we have learned through the media that even Enron has shredded documents. I hope that this committee will have a hearing on Enron's shredding of documents, what documents were shredded?

We have only focused on Enron's role here in the United States but what about Enron's worldwide holdings, corporations, limited partnerships overseas? Who got bilked overseas, who cooked the books overseas? I hope this committee will explore these rooms in Enron's house of cards through the committee's jurisdiction under the Foreign Corrupt Practices Act. We certainly must review these aspects on Enron's dealings, not only here in the U.S. but also overseas.

I appreciate the fact that Mr. Powers has the gumption to come here before our committee to tell us what he and his colleagues found in their review of Enron's accounting schemes. It is no wonder they had so many schemes when we have learned they have had close to 1,000 accountants working at Enron. While I believe that Mr. Powers had the best intentions in providing the Enron Board with a comprehensive picture of Enron's business practices over the last 5 years, I am troubled by the fact that the report does not include full disclosure, input from Mr. Fastow and Mr. Kopper, who had key roles in creating and managing the special-purpose entities of LJM and Chewco, which contributed to massive

misstatements of Enron's financial security. The report focuses on only a few of these special-purpose entities, and I have been told that Enron has had literally thousands of them.

The Powers report, even without full cooperation of many of the key Enron employees and without the full cooperation of Andersen officials or Enron's outside auditors, provides us with an extremely disturbing tale of greedy executives, lax oversight by senior management and a board of directors, or maybe we should call them "board of enablers" who appear to have not taken their roles very seriously.

The board of directors gave serious flexibility, serious, dangerous flexibility to Mr. Fastow, allowing him to establish the LJM and by not following up on the few strings that they attached to Mr. Fastow's deal. The report shows how they robbed Peter to pay Paul and in some cases, relating to asset transfers, then transferred back to Peter again. As I stated in the hearing we had with Andersen officials 2 weeks ago, I believe the Securities Litigation Reform Act of 1995, or the Securities Rip-off Act, as many of us refer to it, had significant impact on the way corporations approach their business deals.

Prior to the so-called reform, companies would likely not have risked many of the transactions in these aggressive accounting techniques, because they knew there was a very good chance they would be held accountable. Now, however, corporations are willing to take additional risk in their business dealings, because the 1995 reform bill insulated them from legal actions by putting up so many roadblocks for shareholders and employees to take legal action against them.

Mr. Chairman, I fear the Powers report, even with its very serious admonitions, only scratches the surface of what is a thick layer of deceit atop perhaps the worst case of corporate officer malfeasance in recent memory. In their wake lies thousands of Enron employees and retirees with shattered financial lives, while many of the corporate executives, many of whom who are still working at Enron, have lined their pockets. It will be difficult, if not impossible, for Enron to emerge as a credible company from bankruptcy without a comprehensive purging of Enron executives and board members who were at the helm during this debacle. They must be held accountable. I hope the investors in Enron will get themselves a new board of directors and a new senior management team.

I look forward to having the opportunity to question Andrew Fastow, Michael Kopper, Richard Causey and others later this week with regard to the issues in the Powers report. I hope they will come before our committee on Thursday and be open, honest and as aggressive in answering our questions as they were in pursuing their own financial futures. I thank you, Mr. Chairman, and I thank our witness for being here today.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentleman from Kentucky, Mr. Whitfield, for an opening statement.

Mr. WHITFIELD. Mr. Chairman, thank you very much. Mr. Powers, we appreciate you being here today. I don't think any of us would have very many compliments for the Board of Enron, but I think that they obviously were forced into a situation where they

asked you to Chair a group that would do an investigation and come forth with findings.

We understand, obviously, that you did not have any subpoena powers and that you were not able to go in as much detail as you would like to have done, but I think the thing that comes out of this investigation, as in your own words, it is appalling to think that Mr. Fastow walked away with \$30 million. In one instance, he put down \$25,000 and less than 2 months later walked away, or his family's foundation did, with \$4.5 million. Mr. Kopper put down \$5,800 or so and walked away with \$1 million in 2 months. In order to try to meet the code of ethics of Enron, knowing full well that they did not comply with those codes, removed Mr. Kopper and put in his domestic partner in some of these transactions. So I think it is very clear that these people were not stunningly inept but they knew precisely what they were doing, and it is a pure example of corporate greed. And it is really sad because it has basically wiped out the pension funds of thousands of employees who were depending upon this upon their retirement.

So I am delighted that you are here today, and I look forward to your testimony. I yield back the balance of my time.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentlelady from Colorado for an opening statement.

Ms. DEGETTE. Thank you very much, Mr. Chairman, and I would ask unanimous consent to put my entire opening statement in the record.

Mr. GREENWOOD. Without objection.

Ms. DEGETTE. Thank you. When I read the report Mr. Powers and his colleagues put together this weekend, I was stunned both by the duplicitous nature of these deals, these limited partnerships, which were designed to mask losses and to accentuate profits. I was also stunned by the breathtaking oblivion, apparently, evidenced by the Enron Board of Directors when they looked at these. The report indicates that Mr. Fastow and also Jeffrey Skilling, who was Enron's former CEO and at times COO, misled the board of directors by not appropriately disclosing their ownership in special-purpose entities. In particular, today, I would like to discuss the gap between the level of ignorance displayed by the board and the basic fiduciary duties of any corporation.

What jumped out at me when I was reading the Powers report was how little the board of directors seemed to know about the special entities transactions. We know now from the report, and we are all very grateful to Mr. Powers and a little amazed he was able to do what he was without subpoena power or any of the other powers, but nonetheless the board waived Enron conflict of interest rules for Mr. Fastow to allow him partial ownership and managerial duties in Chewco and LJM while still on the payroll of Enron as a senior executive. A provision of the waiver approval included a set of conditions that Mr. Fastow would be required to meet, but Mr. Skilling was supposed to oversee Mr. Fastow's activities—a little like the fox guarding the henhouse, I may add. The report contends, though, that the board had no knowledge of the inappropriate nature of certain related party transactions. It is hard for us to believe that today, in retrospect, but perhaps, Mr. Chairman,

when the committee receives the information we will be able to get with our subpoena power, we will be able to add to this knowledge.

All of us know that boards of directors of corporations are required to serve in a fiduciary capacity. They are entrusted with the responsibility of acting in the best interest of shareholders and their employees, and when you look at the minutes of the Enron board meetings, dating back to 1997, it appears that the board's knowledge of questionable transactions involving Chewco, LJM, Raptor and other special entities that are detailed in the Powers report as having substantial problems.

Now, I was looking at the structures of a lot of these transactions, and it is pretty amazing to me that the board would actually approve these. Mr. Deutsch showed the simplified Whitewing transaction. Here is the Chewco transaction. And if you look at those, those transactions are both structured completely differently in ways which are designed, in my opinion and I think in probably Mr. Powers' opinion, to mask losses and to maximize profits. This is a diagram, it looks elegant in its simplicity compared to the other two, of the Rhythms transaction, which I am interested in because it involves—it is the first transaction, and it involves a Colorado-based company.

What strikes me is all of these transactions were approved by the Enron Board, and I was trying to think about the investors who had Enron stock in their 401(k) programs and their other programs. And to think about an unsophisticated investor trying to review Enron's financial status and trying to understand these very complex leveraging transactions. It is clear to me that when you have a corporation as large as Enron and when you have transactions as complex as these, it is incumbent upon the board of directors to exercise their fiduciary duty and to review these transactions in depth, not to simply rubber stamp these things, and especially when corporate employees and officers have financial interest.

This is what we need to learn as a committee, both today and as we go forward, what did the board know and was it simple negligence on a breathtaking level or was there much more there? And so I look forward to hearing Mr. Powers' testimony today. I promise, Mr. Powers, I will not ask you to analyze each of these transactions in depth for us at this hearing, we only have 5 minutes to question, but perhaps at a later date. Thank you, Mr. Chairman.

Mr. GREENWOOD. The Chair thanks the gentlelady and recognizes the gentleman from Florida, Mr. Stearns.

Mr. STEARNS. Thank you, Mr. Chairman, and welcome, Dean Powers. We appreciate your coming here to speak. I read your report yesterday, and I looked for the word "criminal" in the report, and obviously I would not find that, and I understand that. In fact, this committee here is not here to look for criminality but to investigate and let the Justice Department, and we are well aware of what our function is, is to highlight the problem.

But I did look at some of your testimony yesterday, and it was reported in the Washington Post where you said, "Dealing with the Raptor partnerships," this is what you said, "Enron hid the problem and, 'gave the false impression that Raptor had enough money to pay Enron what they owed,'" Now, that is euphemistically for

not only did they hide the fact but they didn't tell the truth. Obviously, you are dean of the law school there at the University of Texas, and you understand when they don't tell the truth that is lying. So the euphemistic statements you are using there are something I think the committee and the American public should realize that even within your report, while you are not using the word "criminal," you are indicating indirectly that these people were not telling the truth.

When you have a report like this, which is based upon volunteers, it is not going to get to the substance of this case, and that is why this committee and the Banking Committee and the Senate committees are making the right decision to have these folks come forward and to speak the truth under oath. This whole Enron thing is much like a financial Hindinburgh (ph). It was a marvel in the eyes of Wall Street, yet ultimately went up in flames, with employees and investors getting burned. And I think it is also apparent that this staff on this committee has done an excellent job in trying to extricate the facts here, and I think your report, Dean Powers, is helping also.

But reading through your report, I also had the feeling of the would have, could have, should have type of philosophy. When you have people who are volunteering to give information they are going to present, which is basically people not telling the truth, self-enrichment, failures at many level, they are going to give a picture which is not totally accurate. So as much as your report is helpful, it is really just very, very first step here.

You mentioned that there is failures of many levels and many people. I am not sure that it was a conspiracy that involved people right down to the middle or lower management. I think, based upon what we heard earlier in hearings on this committee and oversight, there were some people at the very top steering this whole basic series of misstatements and actually in violation of Enron's own code of conduct. You point out in the report that the Enron chief accounting officer failed to provide complete information to the Audit Committee, Enron's senior risk officers failed to adequately scrutinize these transactions for economic risk, and the board of directors, the board of directors failed to provide adequate oversight, and yet they were making large sums of money, and they had a fiduciary responsibility to make sure that they had proper oversight, and, last, of course, Arthur Andersen failed to provide objective accounting judgment. So this is a flawed, flawed company.

I am concerned that because the Special Investigative Committee lacked the power to compel parties, Dean Powers, that some of this information, while very good, is not necessarily going to be as relevant as it should, but I do commend for your honest effort here, and I appreciate, again, you coming here this morning. Thank you, Mr. Chairman.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes for an opening statement the gentleman from Louisiana, Mr. John.

Mr. JOHN. Thank you, Mr. Chairman, and also thank you for convening this hearing into the findings of the SIC, the Special Investigative Committee.

I believe before this committee or any other person prejudices what went wrong at Enron, who is to blame and what Congress can do about it, I think common sense dictates that we closely review all of the available facts. The report produced here today by Mr. Powers is an important piece of the puzzle that our constituents, Americans and certainly former Enron employees are demanding that we solve. I think it is very apparent and clear from the report that, at a minimum, a systematic failure of checks and balances within Enron and between the company and its outside advisors allowed certain of its current and former employees and officers to engage in related party transactions that put self-enrichment before the interests of the company and its shareholders. It seems unimaginable to me that and many Americans and anyone who is following what has gone on that so many people involved, from the directors, senior management, auditors and lawyers, could have been completely unaware of what was happening and that the blame rests with only a few bad actors.

Beginning with the formation of Chewco, Enron became a Ponzi scheme of self-dealing partnerships which were designed, in your own words, to mislead investors about the true financial state of the company and ultimately resulted in its financial implosion. Mr. Chairman, the investigative report clearly shows that there was not simply a worm in Enron's apple; it was instead rotten to the core.

The question for this committee is why thousands of employees and investors had to lose just about everything that they owned before anyone knew of this mess. Either the accounting system did not provide warnings of Enron's troubles or it was too easy to manipulate the rules to hide information from public scrutiny. Either way, I believe this report raises many more questions than it provides answers.

Mr. Chairman, I look forward to working with you to find out the answers of what has gone on here, and I thank Mr. Powers for his report; it was very enlightening.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentleman from New Hampshire, Mr. Bass.

Mr. BASS. Thank you, Mr. Chairman, and thank you, Mr. Powers for being here today, and I will be brief so you can get on with your testimony.

To say that your report is troubling would probably be the understatement of the century, and, as you know, market confidence is based on expectations of firm accounting principles and honorable corporate governance, both of which obviously have not occurred in this particular situation. Legal and management structure of entities like Enron, accounting entries, accounting restatements and so on, really need to become known to this committee. It is part of a fact-finding nature of what we are attempting to do. But I also believe that we need to, as quickly as possible, develop the facts, find out what went wrong, find out who is to blame, but what is more important about this subcommittee's and full committee's challenge is to come up with policy recommendations for changes to make sure that, first of all, this sort of thing isn't going on as we speak still, and, second, that we can take action legislatively if necessary to make sure that the public is protected and the capital markets'

confidence is regained so that we can move forward in 2001 and 2002 with more confidence.

So I appreciate your taking the time, which will be quite a lot of time, to be here today. I appreciate the efforts that you have undertaken as a member of the Board of Directors of Enron to produce this report, which is long and thorough. We will get to the bottom of this, and hopefully we will move forward with something that will be productive in the very near future. Thank you, Mr. Chairman.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentleman, Mr. Rush.

Mr. RUSH. Thank you, Dean Powers, for your attendance here and for your report, and I want to thank you, Mr. Chairman, for holding this hearing on the findings of the so-called Enron Powers Report, or in Superbowl terminology, the Enron play-by-play book.

Mr. Chairman, I, like most observers of the Enron collapse, was appalled to hear that thousands of Enron employees whose savings disappeared while top Enron executives cashed in their stock for millions with the release of the Powers report that shock has turned to utter outrage and disbelief. This report is a crucial piece to the puzzle of Enron in that it reveals a culture where every self-imposed standard enacted by Enron was broken. All of this was simply done in an attempt to satisfy a gluttonous appetite for corporate wealth.

In particular, I commend the Powers Committee for its unflinching criticism of Kopper and Fastow who created a profiteering network of friends and associates designed to bleed Enron at the expense of its investors. And while I believe that this criticism is well-deserved, I am also interested in the degree to which the board of directors have escaped close scrutiny and criticism.

In raising this issue, I do not question the integrity of Mr. Powers, who I know is a well-respected legal scholar. What I do question is the betrayal of Ken Lay who holds a Ph.D in economics as a naive and absent-minded professor who simply goofed by not spotting all of the evil-doings going on all around him. In the case of LJM transaction, I question the casting of the board of directors as a group of well-meaning and trustworthy corporate Governors who, despite their negligence, were unwitting victims of Andy Fastow and Michael Robert Kopper.

That said, I await the various detailed responses that this report will certainly bring about from Arthur Andersen and others. I also await testimony from those parties who refuse to participate in this study, and with those responses I am certain that a more full and accurate picture of who knew what and when will emerge.

Mr. Chairman, at the end of the day, I suspect that Mr. Lay and the rest of the Enron board will not be viewed as a hapless bunch of know-nothings, but rather as a group of well-educated, well-seasoned and shrewd business people who intentionally blinded themselves to a situation which reeks so badly that it couldn't help but be detected by even the most novice of business student.

Whether Enron was a ship of pirates, a ship of fools or a combination of the two, it is my hope that today's hearing takes us a step closer to enacting bold, new legislation. Indeed, that legislation should ensure that no ship which is destined to sink with the

life savings of thousands of innocent investors ever, ever, ever sets sail again in this nation. Thank you, and I yield back the balance of my time.

Mr. GREENWOOD. The Chair thanks the gentleman, and the Chair thanks Mr. Powers for your forbearance this morning. Mr. Powers, you are aware that the committee is holding an investigative hearing and when doing so has had the practice of taking testimony under oath. Do you have any objection to testifying under oath?

Mr. POWERS. None whatsoever.

Mr. GREENWOOD. Appreciate that. The Chair then advises you that under the rules of the House and the rules of the committee you are entitled to be advised by counsel. Do you desire to be advised by counsel during your testimony today?

Mr. POWERS. No, I don't.

Mr. GREENWOOD. Okay. In that case, if you would please rise and raise your right hand, I will swear you in.

[Witness sworn.]

Mr. GREENWOOD. Appreciate that. You are now under oath, and you may give a 5-minute summary of your written statement. We thank you.

**STATEMENT OF WILLIAM C. POWERS, JR., CHAIRMAN OF THE  
SPECIAL INVESTIGATIVE COMMITTEE OF THE BOARD OF DI-  
RECTORS OF ENRON CORPORATION**

Mr. POWERS. Thank you, Mr. Chairman. Mr. Chairman, distinguished members of the subcommittee, my name is William Powers, and I am the dean of the University of Texas Law School. As you know, for the last 3 months, I have served as the chairman of the Special Investigative Committee of the Board of Directors of Enron, and I very much appreciate the opportunity to come here today and testify.

During October of last year, questions were raised about Enron's transactions with partnerships that were controlled by its chief financial officer, Andrew Fastow. In the middle of October, Enron announced that it was taking an after-tax charge of more than \$500 million against earnings because of transactions with one of those partnerships. Enron also announced a reduction in shareholder equity of more than a billion dollars.

At the end of October, the Enron board established a special committee to investigate these matters. It then asked me if I would join the board for the purpose of chairing that committee and conducting that investigation. With the help of counsel and professional accounting advisors, we have spent the last 3 months doing that, conducting the investigation we were charged to conduct.

Our committee's report was filed on Saturday. It covers a lot of ground and I hope it will be a helpful starting point for the necessary further investigations by congressional committees, by the Securities and Exchange Commission and by the Department of Justice. As several members of the subcommittee have noted in their statements, we see this report as just a start, merely a beginning. A copy of the executive summary of our report is attached to my statement here.

Many questions currently part of the public discussion, such as questions dealing with the employees' retirement savings—and let me add, matters dealing with the employees' retirement savings and their loss of their savings nest egg is one of the most tragic aspects of this story—that is an important issue that requires much investigation. Also public questions about sales and trading in securities of Enron by Enron insiders, those also are important public questions. There were, however, questions beyond the scope of the charge we were given, and they are questions beyond what we could do in a 3-month period. Again, these are matters of vital importance, but they were not matters we addressed in our report, and they need further study by relevant congressional committees, the Department of Justice and other agencies.

What we were charged with was investigating transactions between Enron and partnerships controlled by its chief financial officer, or people who worked in his department. That is what our report discusses. And, frankly, Mr. Chairman, as I said before, what we found was appalling.

First, we found that Fastow, and other Enron employees involved in these partnerships, enriched themselves, in the aggregate, by tens of millions of dollars that they should have never received. Fastow got at least \$30 million, Kopper at least \$10 million, two others \$1 million each, and still two more in amounts that we believe were in the range of hundreds of thousands of dollars. So there was self-enrichment.

Second, we found transactions that were improperly structured. But if they had been structured correctly, Enron could have kept assets, under accounting rules, especially debt, off of its balance sheet. But Enron did not follow those accounting rules.

Finally, we found something more troubling than individual instances of misconduct or a failure to follow accounting rules. We found a systematic and pervasive attempt by Enron's management to misrepresent the Company's financial condition. Enron management used these partnerships to enter into transactions that it could not, or would not, have done with unrelated commercial entities. Many of the most significant transactions apparently were not designed to achieve bona fide economic objectives.

As our report demonstrates, these transactions were extremely complex. And I won't try to describe them in detail here, but I do think it would be useful if I could give just one example. It involves efforts by Enron to hedge against losses on investments that Enron had.

Enron is not just a pipeline and energy trading company. It also had large investments in other businesses, some of which had appreciated substantially in value. These were volatile investments, and Enron was concerned because it had recognized the gains when these investments appreciated, and it didn't want to recognize the losses if the investments declined. Therefore, Enron purported to enter into certain hedging transactions in order to avoid recognizing losses from the investments. The problem was that the hedges weren't real. The idea of a hedge is normally to contract with a creditworthy outside party that is prepared, for a price, to take on the economic risk of an investment. If the value of the investment goes down, that other party will bear the loss, but that

is not what happened here. If you cut through the complexity of these partnerships and transactions, here Enron was essentially hedging with itself.

The outside parties with which Enron hedged were the so-called Raptors. The purported outside investor in them was a Fastow partnership. In reality, these were entities in which only Enron had a real economic stake, and whose main assets were Enron's own stock. The notes of Enron's corporate secretary, preparing for the minutes from a meeting of the Financial Committee of the board, a meeting that was regarding these Raptors, captures the reality of these transactions. Those notes say, quote, "Does not transfer economic risk but transfers P+L volatility."

If the value of Enron's investments fell at the same time that the value of Enron stock fell, the Raptors would be unable to meet their obligations, and the hedges would fail. This is precisely what happened in late 2000 and early 2001 when two of these Raptor vehicles lacked the ability to pay Enron on the hedges. Even if the hedges had not failed, though, in the sense I just described, the Raptors still would have paying Enron with the stock that Enron had provided in the first place; that is, Enron would simply be paying itself back.

By March 2001, it appeared that Enron would be required to take a charge against earnings of more than \$500 million to reflect the inability of the Raptors to pay. But then rather than take that loss, Enron compounded the problem by making even more of its own stock available to the Raptors—\$800 million worth. It gave the false impression that the Raptors had enough money to pay Enron on the money it owed, on the money that the Raptors owed. This transaction was apparently hidden from the board, and it certainly was hidden from the public.

Let me say that while there are questions about who understood what concerning these many very complex transactions, there is no question that virtually everyone knew, everyone from the board of directors on down, everyone understood that the company was seeking to offset its investment losses with its own stock. That is not the way it is supposed to work. Real earnings are supposed to be compared to real losses. As a result of these transactions, Enron improperly inflated its reported earnings for a 15-month period, from the third quarter of 2000 through the third quarter of 2001. It overstated its earnings or inflated its reported earnings by more than \$1 billion. This means that more than 70 percent of Enron's reported earnings for this period were not real.

Now, how could that have happened? The tragic consequences of the related-party transactions and accounting errors were the result of failures at many levels, by many people: a flawed idea, self-enrichment by employees, inadequately designed controls, poor implementation, inattentive oversight, simple, and not-so-simple, accounting mistakes, and overreaching culture that appears to have encouraged pushing the limits.

Whenever this many things go wrong, it is not just the act of one or two people. There was misconduct, to be sure, by Fastow and other senior employees of Enron, there were failures in the performance of Enron's outside advisors, and there was a fundamental default in leadership and management. Leadership and manage-

ment begin at the top, with the CEO, Ken Lay. In this company, leadership and management depended as well on the chief operating officer, Jeff Skilling. And the board of directors failed in its duty to provide leadership and oversight of the company.

In the end, this is a tragedy that could and should have been avoided. I hope that our report is a first step. It will take from the committee and other agencies, but I do hope that our report and the work of this committee will help reduce the danger that this tragedy will happen again to some other company. Thank you, Mr. Chairman.

[The prepared statement of William C. Powers, Jr. follows:]

PREPARED STATEMENT OF WILLIAM C. POWERS, JR., CHAIRMAN OF THE SPECIAL INVESTIGATIVE COMMITTEE OF THE BOARD OF DIRECTORS OF ENRON CORPORATION

Mr. Chairman and distinguished Members of the Committee. My name is William Powers. I am the Dean of the University of Texas Law School. For the past three months, I have served as Chairman of the Special Investigative Committee of the Board of Directors of Enron Corporation. I appreciate the opportunity to come and testify before you today.

As you know, during October of last year, questions were being raised about Enron's transactions with partnerships that were controlled by its Chief Financial Officer, Andrew Fastow. In the middle of October, Enron announced that it was taking an after-tax charge of more than \$500 million against its earnings, because of transactions with one of those partnerships. Enron also announced a reduction in shareholder equity of more than a billion dollars. At the end of October, the Enron Board established a Special Committee to investigate these matters, and then asked me if I would join the Board for the purpose of chairing that Committee, and conducting that investigation. With the help of counsel and professional accounting advisors, we have spent the last three months conducting that investigation.

Our Committee's Report was filed on Saturday. It covers a lot of ground and will, I hope, be a helpful starting point for the necessary further investigations by Congressional Committees, by the Securities and Exchange Commission, and by the Department of Justice. A copy of the Executive Summary of our Report is attached to my Statement here.

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First, we found that Fastow—and other Enron employees involved in these partnerships—enriched themselves, in the aggregate, by tens of millions of dollars they should never have received. Fastow got at least \$30 million, Michael Kopper at least \$10 million, two others \$1 million each, and still two more amounts we believe were at least in the hundreds of thousands of dollars.

Second, we found that some transactions were improperly structured. If they had been structured correctly, Enron could have kept assets and liabilities (especially debt) off of its balance sheet. But Enron did not follow the accounting rules.

Finally, we found something more troubling than those individual instances of misconduct and failure to follow accounting rules. We found a systematic and pervasive attempt by Enron's Management to misrepresent the Company's financial condition. Enron Management used these partnerships to enter into transactions that it could not, or would not, do with unrelated commercial entities. Many of the most significant transactions apparently were not designed to achieve bona fide economic objectives.

As our Report demonstrates, these transactions were extremely complex. I won't try to describe them in detail here. But I do think it would be useful to give just one example. It involves efforts by Enron to "hedge" against losses on investments it had made.

Enron was not just a pipeline and energy trading company. It also had large investments in other businesses, some of which had appreciated substantially in value. These were volatile investments, and Enron was concerned because it had

recognized the gains when these investments appreciated, and it didn't want to recognize the losses if the investments declined in value.

Therefore, Enron purported to enter into certain "hedging" transactions in order to avoid recognizing losses from its investments. The problem was that the hedges weren't real. The idea of a hedge is normally to contract with a credit-worthy outside party that is prepared—for a price—to take on the economic risk of an investment. If the value of the investment goes down, that outside party will bear the loss. That is not what happened here; here, Enron was essentially hedging with itself.

The outside parties with which Enron "hedged" were the so-called "Raptors." The purported outside investor in them was a Fastow partnership. In reality, these were entities in which only Enron had a real economic stake, and whose main assets were Enron's own stock. The notes of Enron's corporate secretary, from a meeting of the Finance Committee regarding the Raptors, capture the reality: "Does not transfer economic risk but transfers P+L volatility."

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By March 2001, it appeared that Enron would be required to take a charge against earnings of more than \$500 million to reflect the inability of the Raptors to pay. Rather than take that loss, Enron compounded the problem by making even more of its own stock available to the Raptors—\$800 million worth. It gave the false impression that the Raptors had enough money to pay Enron what they owed. This transaction was apparently hidden from the Board, and was certainly hidden from the public.

Let me say that while there are questions about who understood what concerning many of these very complex transactions, there's no question that virtually everyone, from the Board of Directors on down, understood that the company was seeking to offset its investment losses with its own stock. That is not the way it is supposed to work. Real earnings are supposed to be compared to real losses.

As a result of these transactions, Enron improperly inflated its reported earnings for a 15-month period—from the third quarter of 2000 through the third quarter of 2001—by more than \$1 billion. This means that more than 70 percent of Enron's reported earnings for this period were not real.

How could this have happened? The tragic consequences of the related-party transactions and accounting errors were the result of failures at many levels and by many people: a flawed idea, self-enrichment by employees, inadequately-designed controls, poor implementation, inattentive oversight, simple (and not-so-simple) accounting mistakes, and overreaching in a culture that appears to have encouraged pushing the limits.

Whenever this many things go wrong, it is not just the act of one or two people. There was misconduct by Fastow and other senior employees of Enron. There were failures in the performance of Enron's outside advisors. And there was a fundamental default of leadership and management. Leadership and management begin at the top, with the CEO, Ken Lay. In this company, leadership and management depended as well on the Chief Operating Officer, Jeff Skilling. The Board of Directors failed in its duty to provide leadership and oversight.

In the end, this is a tragedy that could and should have been avoided. I hope that our Report, and the work of this Committee, will help reduce the danger that it will happen to some other company.

Mr. GREENWOOD. Thank you, Dean Powers. We appreciate your testimony, and we know you testified just yesterday, and expect you will be testifying for days to come.

The Chair recognizes himself for 5 minutes for purposes of inquiry. Chewbacca, JEDI Capital, Kinobi Holdings, Obi Wan Holdings, Enron executives seem to have had a fascination with Star Wars. My question, Dean Powers, is this: Is Ken Lay the Luke Skywalker of this of this tale or is he the Darth Vader?

Mr. POWERS. Well, he is not the Luke Skywalker. He certainly is responsible for allowing this to happen. I think there were red

flags that certainly should have indicated to him that this was happening.

Mr. GREENWOOD. Well, let me go right to your testimony. One of the things you just said was that, "Virtually everyone from the board of directors on down understood that the company was seeking to offset its investment with its own stock. This is not the way it is supposed to be. Real earnings are supposed to be compared to real losses." So I take it from that you mean that Ken Lay knew that.

And if you look at the law, the law is pretty clear about what is deceptive. It is deceptive to employ any device, scheme or artifice to defraud, to make any untrue statement or material fact or to admit to state a material fact necessary in order to make the statements made in the light of the circumstances under which they were made, et cetera. So connect the dots, it seems to me, that here was a company that in its financial statements was misleading and that everyone knew, including Ken Lay, that it was misleading its investors in its financial statements. So how do we get beyond the assumption, the conclusion, that Mr. Lay is guilty, as guilty as anyone else of intentionally defrauding his investors?

Mr. POWERS. Well, it is absolutely true that Mr. Lay fully understood that they were using their own stock to offset these losses in their other investments. And that is the problem.

Mr. GREENWOOD. Not only that they were doing that, but they were not sharing that reality with their investors.

Mr. POWERS. Absolutely, that is correct. Well, can I just—

Mr. GREENWOOD. You interviewed Mr. Lay. About how much time did you spend interviewing Mr. Lay?

Mr. POWERS. I think it was a couple of hours. Four hours.

Mr. GREENWOOD. Four hours? Okay. And so on this direct line of questioning about what Mr. Lay understood and when he understood and, as Mr. Tauzin said, certainly we know in August he was advised of this, what was Mr. Lay's story about—how did he defend himself from this obvious line of questioning, which is did he in fact—was he complicit in intentionally defrauding his investors?

Now, it seems to me when you look at motive, we sort of understand some of Mr. Fastow's motives, because there was self-dealing involved. Mr. Fastow seems to be the Betty Crocker of cookbooks. But Mr. Lay also had a motive, it would seem, for the investors not to understand that the stock was overvalued, and that is because he was a holder of millions of dollars of stock.

Mr. POWERS. Well, when we interviewed Mr. Lay, he certainly understood that as elaborate as these schemes were, ultimately they were using Enron stock to hedge against these investment losses. He understood that. I can tell you what his story was: He didn't understand or appreciate that there was anything wrong with that. I don't know whether that is credible; I am saying that was his story, that he didn't—the story was the accountants had signed off on it; he assumed it was an okay accounting device.

Mr. GREENWOOD. Was it credible to you? Do you think it is credible?

Mr. POWERS. It is very hard—we did present him with documents and in a sense cross examine, but we did not have the devices available to us, and that is a reason why our report is a first

start. It certainly is something that people would want to go into a great deal further. It raises questions, I agree.

Mr. GREENWOOD. You repeatedly note in your report that Andersen, Enron's outside auditor and internal consultant on these transactions, refused to fully cooperate with your inquiry by making certain documents and persons available for your review. Can you be more specific about what Andersen provided you with and what they would not, both in terms of persons and documents?

Mr. POWERS. Okay. When we started the investigation, we started asking Andersen if we could see documents and interview—see their work papers and interview their accountant. We wanted to do that after we developed the basic understanding, but as we went forward with the investigation, they would say, “Well, we will do that,” but we never got to interview their accountant. We did see some of their work papers, we did not see the work papers for 2001, which are crucial; we did not see those. We did see some of the papers. We asked for copies. A few days later, Enron fired Andersen, and we were told that at that point Andersen would no longer cooperate. By that point, we had not been able to talk and get their explanations of these work papers. We have not been able to talk with their accountant.

Mr. GREENWOOD. Thank you, Mr. Powers. The Chair recognizes the gentleman from Florida, Mr. Deutsch, for purposes of inquiry.

Mr. DEUTSCH. Thank you, Mr. Chairman. One of the mandates of your committee was to recommend discipline at Enron. What discipline is the committee going to recommend?

Mr. POWERS. We did not recommend discipline in the end, and the reason was we have been going non-stop getting this done. My testimony had been requested, we wanted to get this report out, and thought that, frankly, being exhausted at the end of it, we didn't want make judgments about discipline. And I think the facts speak for themselves, and others are going to have to make those judgments. But we did not, in the end, recommend any discipline, but we did not mean to imply by that that there should not be discipline imposed here.

Mr. DEUTSCH. Let me follow-up on some of the comments that the chairman was mentioning. If the company keeps billions of dollars of potential liability off of its balance sheets so that its shareholders and investors don't know about it, as Enron did, isn't that fraud?

Mr. POWERS. Well, there are legitimate accounting devices that—I am not an expert in the area of securities fraud—but that companies use to keep transactions and debt, using structured financing, off their balance sheets. And if they don't use the proper structures and don't reveal the proper structures, then there are serious questions about fraud.

Mr. DEUTSCH. So, again, I mean what you are really saying is that as good the—you are really not an expert in securities fraud.

Mr. POWERS. That is correct, or enforcement of what penalties should be imposed here.

Mr. DEUTSCH. Let me go directly to the Raptor transactions. You stated, and I am quoting, “Virtually everyone from the board of directors on down understood the company was seeking to offset its investment loss with its own stock. That is not the way it is sup-

posed to work,” closed quote to your statement. If everyone understood that except the shareholders, and it is wrong, isn’t it fraud on the shareholder?

Mr. POWERS. I don’t feel I am in a position to, under the securities law, answer that question. The shareholders—there was not transparent disclosure of what was going on in these transactions with the shareholders, absolutely.

Mr. DEUTSCH. Let me just stop. By any definition of common usage would you say it is fraud? Putting away your attorney’s hat and a securities lawyer, which you are not, I mean I think that is in a sense what our job is, because that is clearly our intention in the statute, and fraud is fraud.

Mr. POWERS. Right.

Mr. DEUTSCH. I mean if people don’t understand it—your quote of not understanding it except for the shareholders, the whole purpose of the system is the shareholders are supposed to know what is going on.

Mr. POWERS. Absolutely. My only hesitation is fraud normally requires a certain state of mind, and I am not in a position to ascertain the state of mind of every one of these individuals. If there is a state of mind—

Mr. DEUTSCH. And it doesn’t necessarily require state of mind, because if you have an instance inferring to that, then you can infer the state of mind. You said that when an additional \$800 million of stock was added to the Raptor accounts by Enron so it wouldn’t have to show a loss, it was, quote, “apparently hidden from the board,” close quote. What do you mean? Did you interview all the board members to determine what they knew and what they didn’t know?

Mr. POWERS. Yes. We interviewed—formally interviewed nine board members. That was a restructuring deal that—much else was known by the board, but that was a restructuring deal in early 2001 that there was agreement, as the evidence showed, that was not brought before the board.

Mr. DEUTSCH. And can the company issue \$800 million in stock without the approval of the board?

Mr. POWERS. They couldn’t issue the stock. This was stock that was already owned by the company because of contracts it had with outside parties. And that avoided the necessity to actually issue new stock. They transferred stock the company owned to these structures, and I am sure that is why already-owned stock was used.

Mr. DEUTSCH. So, again, I mean clearly an intention to keep that information from the board itself?

Mr. POWERS. Absolutely. I have no doubt that that was intentional by the people that restructured—Fastow and others. It was intentionally keeping that from the board, and therefore keeping it from the public, absolutely.

Mr. DEUTSCH. Let me ask one question, and, again, I didn’t see it in the report, but it just is a disturbing issue, and, again, you mentioned the limitations specifically on the 401(k) issue. But as someone who has spent 3 months—the last 3 months looking at Enron, one of the real disturbing issues, not just the lock-out provision on Enron stock but the switching of the managers of the

401(k)s to basically have a 60-day additional lock-out, which, again, from an outside-looking-in perspective, I mean there is different levels of evil that have occurred in this process. I mean that is about at the highest level that I can think of. I mean have you looked at that decisionmaking process at all or you were just not able to look at that?

Mr. POWERS. We did not look at that. We did a great deal. We reviewed, I think, over 400,000 pages of documents, interviewed 60 people, and we did not look into the 401(k)s and the lockout.

Mr. GREENWOOD. The time of the gentleman has expired. The Chair recognizes the chairman, Mr. Tauzin.

Chairman TAUZIN. Thank you, Mr. Chairman. Dean Powers, when I was attending law school at LSU, it was apparent to me that Latin was going to be important to me, and in preparation for that, I took a non-credit Latin course. And the reason I did was because in the law we use Latin, because it is so precise. Terms like *res judicata* and *res ipsa loquitur* have special meanings in the law and jurisprudence. But I want to help get away from that, and I hope you will help me, as dean of law school, to put this in lay terms so we can understand it in a layman's sense.

Basically, what you have presented to us is a report that details how these partnerships and the deals, some two dozen deals structured by either Chewco or LJM1 and 2—LJM1 and 2, by the way, I think were the initials of the wife and children of Mr. Andrew Fastow.

Mr. POWERS. That is correct.

Chairman TAUZIN. Structured by him. These deals structured by this partnership failed the basic test of structural compliance and operational compliance with current accounting principles; is that right?

Mr. POWERS. That is right, and their whole concept was flawed.

Chairman TAUZIN. Now, just for a second, let us think about what would be a legitimate function of a special-purpose entity, an SPE, or a partnership like LJM. Legitimately, Enron had some problems, it had some assets like Rhythms, which they put \$10 million in and all of a sudden it was worth \$500 million because of inflation and the value of the stock market and the run-up of the stocks. Like many corporations holding a risky stock like that, they probably had a need to put that risk off, to share that risk with someone else if the stock fell dramatically so it didn't hurt their own stock. That is a legitimate function that corporations use special-purpose entities and they use partnerships in some cases to do. Isn't that premised upon the notion, however, that there is a real independent sharing of the risk, that the company really gives the risk over to someone else to either take, in whole or in part, in order to hedge potential loss to its own stockholders if a company like Rhythms suddenly lost its value, which it did, which it eventually did? Isn't that, in layman's terms, what occurs in these partnerships, in these SPEs?

Mr. POWERS. I can't add anything that would clarify it more than your statement; that is absolutely correct.

Chairman TAUZIN. Now, what you found and we have been finding is that, No. 1, in the case of Chewco, it was structured wrong. They didn't have enough outside investment to meet the standards

of independence. And you also found some clear questions. We have found many, many clear questions of how independent these operations were. On Thursday, we will detail, for example, how these sweetheart deals were being struck between the partnerships and the corporation, how managers of the partnerships were actually threatening people at Enron with firing if they aggressively negotiated for Enron. They threatened others with loss of their bonuses. We had a weird situation where the bonus came from the partnership, and the salary came from Enron. Incredible conflicts of interest where employees were invited in to share in the profits of some of these outside ventures and profits guaranteed at 2,500 percent in one case and where the risk to Enron and its shareholders was never really properly transferred. In fact, Enron continued to guarantee the losses to the partnerships. The only person protected was the manager of the partnerships. It was guaranteed they could take their money out, plus profit.

So what we have at Enron, as I see from your report, and as we are beginning to see, is a failure of the independence of these organizations, or these deals, or these SPEs and the failure to properly shift the risk away from the corporation when a hedge fund was created or a put was attempted, if you will, on stock that was kind of risky, that they were concerned about, in a scheme that guaranteed money to the managers of the partnership but nevertheless left the stockholders of Enron completely at risk, all the while creating the impression that Enron was making money and was free of debt when the debt was still there.

Now, if I were a corporation in America using one of these vehicles legitimately, then my company would be protected from that loss when it occurred; I would have shared that risk with the partnership, or the special-purpose entity, and my shareholders would have been the better off for it. But in the case of these entities that were created and these deals that were cut, where the risk did not transfer, can you give me any purpose for doing that, other than to hide debt from investors, other than possibly to enrich the managers of the business, the account that was doing it, or to create a false impression of income to the corporation? Can you give me any other reason to do it?

Mr. POWERS. I cannot, and I would just add that the statement that you just made, Congressman Tauzin, is exactly correct.

Chairman TAUZIN. So, Mr. Chairman, if I can, and I will conclude, what you are concluding is what I have concluded, that if your facts are correct, and if our investigation continues to bolster the evidence of the situation as I have just described it, there was no legitimate purpose in the construction of some of these deals, except the defrauding of investors who were putting their money into Enron, and in some cases, the defrauding of investors who were putting their money into these partnerships, because we have also found, by the way, that some banks were told they would get special bond deals if they would put the money up to fund the partnership.

And I want to end it maybe with this and see if you agree with me. What we really have here, as I said earlier, is a case of inside theft. It is a deal where whoever managed the deal was using the credit of the corporation, which remained liable for the deal, to bor-

row money from other investors to the partnership so that they could take it and go home with it, while the corporation remained fully at risk, not only for the new loans but for all the risk of the stock, such as Rhythms, which might decline in value, and eventually collapse the corporation.

Mr. POWERS. These partnerships were definitely using Enron's assets and credit to then create partnerships that enriched themselves.

Chairman TAUZIN. And they were benefited two ways. One way, they got money out of it. Enron was borrowing money, in effect, that they took home. Enron had debt, but it was called income, miraculously, under these plans. And, second, because they kept the investing public and the employees of Enron who had their 401(k) plans tied to the Enron stock, because they kept them in the dark as to what was going on, Enron stock kept inflating in value, because we all thought it had a billion dollars of income it didn't have, and it had a lot less debt than it had.

So they benefited twice. Their stock values are going up. They can then sell, even though the employees couldn't sell it. And they were sucking money out of the partnerships that Enron was putting up the credit for. Now, how can anybody look at all that and conclude that the FBI doesn't need to be over there with the search warrant and a potential set of handcuffs is beyond me. If there isn't consumer fraud here, I don't know where we are going to find it. Thank you very much.

Mr. GREENWOOD. The Chair thanks the chairman and recognizes the ranking member of the full committee, Mr. Dingell, for purposes of inquiry.

Mr. DINGELL. Mr. Chairman, Mr. Powers, I begin by complimenting you on a fine report. I have limited time so I have got to ask you questions in a way that you can respond pretty much with a yes or no, and I say that with apologies to you because of the respect I have for you.

Now, I would like to go to Vincent & Elkins. Isn't it true that they helped to structure many of the deals that were the subject of your investigation?

Mr. POWERS. They did work on the deals. As I point out in the report, I disqualify myself from making judgments about those, but they did work on these deals.

Mr. DINGELL. Now, Vincent & Elkins concluded that they facts in its preliminary investigation revealed it did not warrant, and I now quote, "further widespread investigation by an independent counsel or auditors." Is that right?

Mr. POWERS. I believe they did say that in their conclusion.

Mr. DINGELL. Now, if you were in Mr. Lay's position with Mr. Watkins' letter in your hand, would you have asked the law firm that represented your company in many of these transactions to review these same transactions?

Mr. POWERS. If I were in Mr. Lay's position, I would have asked for a much more extensive investigation.

Mr. DINGELL. And by somebody who was in fact independent as opposed to somebody who had been involved in the structuring of the deal; is that not so?

Mr. POWERS. If I had been Mr. Lay, I certainly would have considered that.

Mr. DINGELL. That would have been the proper way. Now, Mr. Jordan Mintz, then general counsel of Enron Global Finance, was so concerned about the LJM deals that he sought outside counsel to investigate the structure and the propriety of these transactions. Were you aware of that fact?

Mr. POWERS. Yes.

Mr. DINGELL. Did you know that Mr. Mintz went out of his way to hire a firm other than V&E because of the conflicts inherent in the firm's relationship with Enron?

Mr. POWERS. Yes. Mr. Mintz did use another firm.

Mr. DINGELL. Do you believe that V&E should have had the professional judgment to recuse itself from the investigation because of its role in structuring many of these controversial partnerships?

Mr. POWERS. Well, I disqualified myself from evaluating those, and I don't think I have enough information to make a judgment on that.

Mr. DINGELL. So it would not seem improper that they should have done the same thing.

Mr. POWERS. I would have to focus on those facts more than I have.

Mr. DINGELL. All right. Now, isn't it true that most of Ms. Watkins' concerns related to accounting issues?

Mr. POWERS. Yes.

Mr. DINGELL. Isn't it also true that V&E agreed with Enron management that it wouldn't examine accounting issues as a part of its investigation into the Watkins memo?

Mr. POWERS. I would have to go back and look at the letter, because, again, I haven't focused on that.

Mr. DINGELL. Factually, it would appear to be correct, however.

Mr. POWERS. I don't have any reason to disagree.

Mr. DINGELL. Does this instill in you great confidence in the V&E investigation?

Mr. POWERS. Again, I disqualified myself from making judgments on that, and so I am not informed enough about it.

Mr. DINGELL. Would I be unfair in assuming that they should have followed your wisdom in these matters?

Mr. POWERS. They weren't asked to do the kind of investigation that I was asked to do.

Mr. DINGELL. Now, how much V&E bill Enron for the investigation?

Mr. POWERS. I don't know.

Mr. DINGELL. Mr. Baxter committed suicide, as you well know, several weeks ago—a very tragic event. Did V&E ever interview Mr. Baxter as a part of its investigation into Ms. Watkins' allegations?

Mr. POWERS. I don't know whether they did or not.

Mr. DINGELL. Did your committee interview Mr. Baxter?

Mr. POWERS. Yes, we did.

Mr. DINGELL. Ms. Watkins alleged—I wonder why you would and they would not interview Mr. Baxter.

Mr. POWERS. Well, we conducted a very thorough 3-month investigation.

Mr. DINGELL. Are you telling me they did not?

Mr. POWERS. They didn't conduct a 3-month investigation, I don't think.

Mr. DINGELL. Now, Ms. Watkins alleged numerous accounting failures, but Enron and Vincent & Elkins agreed not to look at these transactions. How can we call this a complete report?

Mr. POWERS. Our report or—

Mr. DINGELL. No, the Vincent & Elkins report, which did not look at accounting failures and accounting matters?

Mr. POWERS. Again, I did not myself pursue what they looked into and what they didn't. Other people on the committee did.

Mr. DINGELL. Do you have any reason to believe that anyone at Enron took Ms. Watkins' allegations seriously?

Mr. POWERS. Well, they responded to some extent. The management at Enron didn't take it seriously enough.

Mr. DINGELL. It is also clear that people at Enron were told not to worry because Vincent & Elkins was reviewing them; isn't that right?

Mr. POWERS. I don't remember, but I have no reason to disagree with that.

Mr. DINGELL. Can you think of another reason why they might not have taken them seriously?

Mr. POWERS. I am sorry, why the management didn't take the—

Mr. DINGELL. Seriously Ms. Watkins' allegations.

Mr. POWERS. Well, they were very troubling allegations.

Mr. DINGELL. They were.

Mr. POWERS. Yes.

Mr. DINGELL. But were they taken seriously? Did you find any evidence in your inquiry that these allegations were taken seriously by Enron?

Mr. POWERS. I think they were not taken seriously enough, certainly.

Mr. DINGELL. Did you find any evidence that Vincent & Elkins went into these allegations?

Mr. POWERS. Again, I did not, myself, personally. The report deals with that. I disqualified myself from that, because Vincent & Elkins has done a tremendous amount of pro bono work for the law school and has been a supporter of the law school, and I thought it would be better for the report if I didn't participate in that.

Mr. DINGELL. Well, I applaud that, but I am just curious of did they—well, never mind. Mr. Chairman, I thank you for your kindness. Mr. Powers, I have asked you some rather not so nice questions, but you continue to enjoy my respect.

Mr. POWERS. Well, thank you very much.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentleman from North Carolina, Mr. Burr.

Mr. BURR. Thank you, Mr. Chairman. Dean Powers, you noted in your report that there were individuals that you did not have the opportunity to have Q&A with. Was that—that was requested of those individuals, they just denied to participate; is that correct?

Mr. POWERS. Yes, especially Fastow and other people in these partnerships. We tried to interview them and they declined.

Mr. BURR. You also referred to a limited amount of Andersen documents. Did you make requests for documents from Andersen that they denied you access to those documents?

Mr. POWERS. We asked them for all of their work papers over this period of time.

Mr. BURR. And did they produce all their work papers?

Mr. POWERS. They did not. They did not produce work papers over the period of 2000. We negotiated with them, it dragged on, and we did not get them.

Mr. GREENWOOD. Will the gentleman yield just for 5 seconds. To put a point on Mr. Burr's question on interviewing Mr. Fastow, I believe, according to your report, you had a brief interview with Mr. Fastow.

Mr. POWERS. Yes, that is correct.

Mr. GREENWOOD. Clarify that.

Mr. POWERS. At some point, Mr. Fastow's lawyer said that he would be interviewed, and I was not personally there, but I think it was an extremely short interview, because he simply wouldn't cooperate.

Mr. GREENWOOD. How short?

Mr. POWERS. Well, I think the—it took an hour, but I don't think there were—very little information was forthcoming. Can I correct, the work papers that we didn't get were from 2001.

Mr. BURR. And for the papers that you didn't get, did Andersen give you an explanation as to why they couldn't produce them or wouldn't produce them?

Mr. POWERS. It dragged out, and then finally we—the company discharged them, and they called us back and said, "We won't cooperate any further."

Mr. BURR. So Andersen refused to cooperate.

Mr. POWERS. From that point on. That was in January.

Mr. BURR. Dean, your committee, in 3 months, discovered a tremendous amount. They discovered some things that it took Andersen 4 years to correct or amend in financial statements. Based on the information you have, was Andersen misled by Enron management?

Mr. POWERS. I am not in a position to say that they were never misled by Enron management on any details. They certainly had a great deal of information about the structure of these transactions.

Mr. BURR. Were they in collusion with Enron management?

Mr. POWERS. I don't think I have the information from our investigation to know that. They certainly were working contemporaneously on the accounting of these structures.

Mr. BURR. Were they competent to handle the Enron audit?

Mr. POWERS. I think Arthur Andersen is a competent accounting firm.

Mr. BURR. Let me ask you, Dean, going back to Mr. Dingell's questions, relative to V&E and specifically their investigation, and I understand where you are on it, but there is a news report that says that individuals from Enron limited greatly what they asked V&E to look at, that they didn't ask them to look at accounting structures; as a matter of fact, the told them not to. Is that your

understanding of the instructions that were given by Enron management to V&E on that investigation?

Mr. POWERS. I think that is in our report, yes.

Mr. BURR. And you also referred to others within the committee that looked at V&E, not you.

Mr. POWERS. Yes.

Mr. BURR. Those others were on your special committee?

Mr. POWERS. Yes, that is correct, the other two members and counsel.

Mr. BURR. And what they found, relative to V&E's participation, would be found in your report?

Mr. POWERS. Oh, yes, absolutely.

Mr. BURR. In its entirety.

Mr. POWERS. And the committee investigated that and interviewed people. I just recused myself from it.

Mr. DINGELL. Mr. Chairman, would the gentleman yield, because he has raised a question, and I think it is valuable?

Mr. GREENWOOD. Be happy to.

Mr. DINGELL. Here is reading from Vincent & Elkins' document entitled, "Preliminary Investigation of Allegations of an Anonymous Employee." It says, as follows, in the second page: "In preliminary discussions with you, it was decided that our initial approach would not involve second-guessing the accounting advice and treatment afforded by AA and that there would be no detailed analysis of each and every transaction and that there would be no full-scale, discovery-style inquiry." The letter is directed to Mr. James B. Derrick, Jr., and I believe it would be useful, Mr. Chairman, it goes in the record at a suitable place. And I thank the gentleman for his patience.

Mr. GREENWOOD. Without objection.

[The information referred to follows:]

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# Vinson & Elkins

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October 15, 2001

**Privileged and Confidential:  
Attorney-Client Communication  
and Attorney Work Product**

Mr. James V. Derrick, Jr.  
Executive Vice President and General Counsel  
Enron Corp.  
1400 Smith Street  
Houston, Texas 77002

Re: Preliminary Investigation of Allegations of an Anonymous Employee

Dear Jim:

You requested that Vinson & Elkins L.L.P. ("V&E") conduct an investigation into certain allegations initially made on an anonymous basis by an employee of Enron Corp. ("Enron"). Those allegations question the propriety of Enron's accounting treatment and public disclosures for certain deconsolidated entities known as Condor or Whitewing and certain transactions with a related party, LJM, and particularly ~~transactions with LJM~~ known as Raptor vehicles. The anonymous employee later identified herself as Sherron Watkins, who met with Kenneth L. Lay, Chairman and Chief Executive Officer of Enron, for approximately one hour to express her concerns and provided him with materials to supplement her initial anonymous letter. This letter constitutes our report with respect to our investigation and sets forth the scope of our review, the activities undertaken, the identification of primary concerns, and our analysis and conclusions with respect to those concerns.

### 1. Scope of Undertaking

In general, the scope of V&E's undertaking was to review the allegations raised by Ms. Watkins' anonymous letter and supplemental materials and to conduct an investigation to determine whether the facts she has raised warrant further independent legal or accounting review.

By way of background, some of the supplemental materials provided by Ms. Watkins proposed a series of steps for addressing the problems she perceived, which included retention of independent legal counsel to conduct a wide-spread investigation, and the engagement of independent auditors, apparently for the purpose of analyzing transactions in detail and opining as to the propriety of the accounting treatment employed by Enron and its auditors Arthur Andersen

HOUSTON HOUSTON BEIJING DALLAS LONDON MOSCOW NEW YORK SINGAPORE WASHINGTON D.C.

Confidential Treatment Requested By Wilmer, Cutler & Pickering

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Mr. James V. Derrick, Jr.

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L.L.P. ("AA"). In preliminary discussions with you, it was decided that our initial approach would not involve the second guessing of the accounting advice and treatment provided by AA, that there would be no detailed analysis of each and every transaction and that there would be no full scale discovery style inquiry. Instead, the inquiry would be confined to a determination whether the anonymous letter and supplemental materials raised new factual information that would warrant a broader investigation.

## 2. Activities Undertaken

Our preliminary investigation included the review of selected documents provided to us by Enron and from our internal sources, interviews with key Enron and AA personnel and discussions with V&E attorneys who are familiar with legal issues addressed by Enron in connection with the subject transactions. The focus, of course, was to identify background information, disclosures and personal views with respect to the Condor/Whitewing and Raptor vehicles and Enron's relationship with LJM.

Documents reviewed in this process included excerpts of meetings of Enron's Board of Directors, including minutes of meetings of the Audit and Finance Committees of the Board, various public filings of Enron (annual reports, 10-K's, 10-Q's), documents relating to Enron's transactions with LJM, including Deal Approval Sheets and Investment Summaries, and various miscellaneous materials in the nature of presentations and memoranda. The focus of our document review was to determine whether the requisite approval of the transactions referenced in the anonymous letter had been obtained from Enron's Board and its committees, the nature of the disclosures made with respect to the transactions and relationships questioned by the anonymous letter and supplemental materials and to provide general background information.

Interviews were also conducted with various Enron personnel based either on their connection with the transactions involving Condor/Whitewing, LJM and Raptor, or because they were identified in materials provided by Ms. Watkins as persons who might share her concerns. Those persons interviewed were: Andrew S. Fastow, Executive Vice President and Chief Financial Officer; Richard B. Causey, Executive Vice President and Chief Accounting Officer; Richard B. Buy, Executive Vice President and Chief Risk Officer; Greg Whalley, President and Chief Operating Officer (formerly Chairman of Enron Wholesale); Jeffrey McMahon, President and Chief Executive Officer, Enron Industrial Markets (formerly Treasurer of Enron); Jordan H. Mintz, Vice President and General Counsel of Enron Global Finance; Mark E. Koenig, Executive Vice President, Investor Relations; Paula H. Rieker, Managing Director, Investor Relations; and Sherron Watkins, the author of the anonymous letter and supplemental materials.

Interviews were also conducted with David B. Duncan and Debra A. Cash, both partners with AA assigned to the Enron audit engagement.

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In addition to the foregoing formal interviews, discussions were likewise held with Rex Rogers, Vice President and Assistant General Counsel of Enron, and Ronald F. Astin of V&E regarding general background information and the identification of specific issues relating to the matters raised by the anonymous letter and supplemental materials.

After completing interviews with all of the foregoing individuals, supplemental interviews were conducted with Andrew S. Fastow and Richard B. Causey of Enron and David B. Duncan and Debra A. Cash of AA to confirm certain information learned in the overall interview process.

As we initially discussed, we limited our interviews (with the exception of the AA partners mentioned above) to individuals still employed with Enron. Therefore, we did not interview individuals no longer with Enron mentioned in the anonymous letter or supplemental materials or any third party related to LJM.

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3. Identification of Primary Concerns

Our preliminary investigation revealed four primary areas of concern expressed by Ms. Watkins' anonymous letter and supplemental materials. Accordingly, our document review and interview process focused on those areas of concern and whether the facts raised by Ms. Watkins' anonymous letter and supplemental materials presented any new information as to those matters that may warrant further independent investigation. Those areas of primary concern are as follows:

- a. the apparent conflict of interests by Mr. Fastow's ownership in LJM;
- b. the accounting treatment accorded the Condor and Raptor structures in Enron's financial statements;
- c. the adequacy of public disclosures of the Condor and Raptor transactions; and
- d. the potential impact on Enron's financial statements as a result of the Condor/Whitewing and Raptor vehicles because of the decline in value of the merchant investments placed in those vehicles as well as the decline in the market price of Enron common stock.

Our findings and conclusions with respect to each of these areas of concern are set forth separately below.

4. Conflict of Interest

Mr. Fastow actually organized two separate investment partnerships. The first, LJM-Cayman L.P. ("LJM1"), was launched in June, 1999. The LJM concept appears to have been fully discussed

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with the Office of the Chairman and was presented to and approved by Enron's Board of Directors at a special meeting on June 28, 1999. That approval included the Board's waiver of Enron's code of ethics to permit Mr. Fastow to act as the general partner of LJM1. The primary purpose for the organization of LJM1 was to establish a non-Enron entity with which Enron could enter into a swap transaction to hedge its investment in Rhythms NetCommunications. It was likewise recognized that LJM might negotiate to purchase additional assets in Enron's merchant portfolio. LJM raised \$16 million in outside equity, invested in a Raptor vehicle that entered into a swap for Rhythms NetCommunications and also purchased a sufficient portion of Enron's equity in the Cuiaba power plant in Brazil to allow Enron to deconsolidate that project.

The second investment partnership - LJM2 Co-Investment, L.P. ("LJM2") - was organized in October, 1999.<sup>1</sup> At an October 11, 1999 meeting of the Finance Committee of the Board of Directors, Enron's activities with LJM1 were reviewed and the proposal for transacting business with LJM2 was discussed and approved. The Board of Directors, at its meeting on October 12, 1999, waived Enron's code of ethics to permit Mr. Fastow to serve as general partner of LJM2 and established guidelines for Enron's transaction of business with LJM2. Those included: (i) no obligation to do transactions between Enron and LJM2; (ii) the Chief Accounting and Risk Officers would review, and where appropriate, approve transactions with LJM2; (iii) there would be an annual review by the Board's Audit Committee of completed transactions or recommendations, as appropriate; and (iv) there would be an annual review as to the application of the Company's code of ethics to assure that such transactions would not adversely affect the best interests of the Company.

The LJM2 partnership raised \$349 million in equity from investors ranging from commercial and investment banks, insurance companies, public and private pension funds and high net worth individuals. LJM2 has engaged in approximately 21 separate transactions with Enron.

Pursuant to the Board's guidelines, special procedures were adopted and utilized for the transaction of business with LJM. Those procedures included the preparation of a special LJM2 Deal Approval Sheet ("DASH") that would be prepared for every Enron/LJM2 transaction generally describing the nature of the commercial transaction and the relevant economics. Approval was also required by a variety of senior level commercial, technical and commercial support professionals. DASH was supplemented by an LJM approval process checklist testing for compliance with Board directives for transactions with LJM2, including questions addressing the following:

- alternative sales options and counter-parties.

<sup>1</sup> The initial LJM partnership was then referred to as "LJM1." LJM1 and LJM2 will be referred to jointly as "LJM" unless there is a particular reason to distinguish between the two investment partnerships.

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- determination that the transaction was conducted at arm's length.
- disclosure obligations, and
- review of the transaction by Enron's Office of the Chairman, Chief Accounting Officer and Chief Risk Officer.

As part of these procedures, it also appeared that several additional controls were adhered to. These included LJM senior management professionals never negotiating on behalf of Enron; Enron professionals negotiating with LJM reporting to senior Enron professionals other than Mr. Fastow; Enron Global Finance commercial, legal and accounting monitoring of compliance with procedures and controls for regular updates for Chief Accounting and Risk Officers, and internal and outside counsel regularly consulted regarding disclosure obligations and review of any such disclosures.

Based on our review of the LJM Deal Approval Sheets and accompanying checklist, it appears that the approval procedures were generally adhered to. Transactions were uniformly approved by legal, technical and commercial professionals as well as the Chief Accounting and Risk Officers. In most instances, there was no approval signature for the Office of the Chairman except for several significant transactions. It also appeared that the LJM transactions were reviewed by the Audit Committee on an annual basis. At the February 7, 2000 meeting of the Audit Committee, all LJM transactions occurring prior to that date were reviewed. A review of all the LJM transactions during the following year was made at the February 12, 2001 meetings of both the Audit and Finance Committees.

Based on our interviews with various Enron representatives, and notwithstanding the foregoing guidelines and procedures that were adopted, concerns were expressed about the awkwardness in LJM's operating within Enron and two potential conflicts of interest. The awkwardness arose from the fact that LJM's professionals – primarily individuals reporting to Mr. Fastow and Michael Koppers – were also Enron employees who officed in Enron space and worked among Enron employees. Transactions were negotiated between Enron employees acting for Enron and other Enron employees acting for LJM. Within Enron, there appeared to be an air of secrecy regarding the LJM partnerships and suspicion that those Enron employees acting for LJM were receiving special or additional compensation. Although there was a Services Agreement between Enron and LJM pursuant to which LJM compensated Enron for the services of Enron personnel and use of Enron's facilities, this fact did not quell the awkwardness of the Enron employees "wearing two hats." Much of this awkwardness should be eliminated on a going-forward basis, however, by reason of Mr. Fastow's sale of his ownership interest in LJM effective July 31, 2001 to Mr. Koppers (who resigned from Enron prior to the transaction) and the complete separation of LJM's employees and facilities from Enron.

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The first area of potential conflict of interest voiced by several individuals was the risk that undue pressure may be placed on Enron professionals who were negotiating with LJM because those individuals would ultimately have their performance evaluated for compensation purposes by Mr. Fastow in his capacity as Chief Financial Officer. In particular, Jeffrey McMahon stated that while he was Treasurer of Enron he discussed this conflict directly with Mr. Fastow and Jeffrey Skilling, and that the conflict was not resolved prior to his acceptance of a new position within Enron. Mr. McMahon stated, however, that he was aware of no transaction where Enron suffered economic harm as a result of this potential conflict.

The second potential conflict of interest identified by several individuals was that investors in LJM may have perceived that their investment was required to establish or maintain other business relationships with Enron. Although no investors in LJM were interviewed, both Mr. Fastow and Mr. McMahon stated unequivocally that they told potential investors that there was no tie-in between LJM investment and Enron business. Moreover, Mr. Fastow stated that Merrill Lynch was paid a fee for marketing LJM2 partnership interests and that a number of investors, such as private and public pension funds and high net worth individuals, had no business relationship with Enron.

In summary, none of the individuals interviewed could identify any transaction between Enron and LJM that was not reasonable from Enron's standpoint or that was contrary to Enron's best interests. Conversely, the individuals interviewed were virtually uniform in stating that LJM provided a convenient alternative equity partner with flexibility that permitted Enron to close transactions that otherwise could not have been accomplished. Moreover, both the awkwardness and potential for conflict of interest should be eliminated on a going-forward basis as a result of Mr. Fastow's divestment of his ownership interest in the LJM partnerships.

#### 5. Accounting Issues

As stated at the outset, the decision was made early in our preliminary investigation not to engage an independent accounting firm to second guess the accounting advice and audit treatment provided by AA. Based on interviews with representatives of AA and Mr. Causey, all material facts of the Condor/Whitewing and Raptor vehicles, as well as other transactions involving LJM, appeared to have been disclosed to and reviewed by AA. In this regard, AA reviewed the LJM solicitation materials and partnership agreement to assure that certain safeguards were provided that would permit LJM to be a source of third party equity in transactions conducted with Enron. AA likewise reviewed specific transactions between Enron and LJM to assure that LJM had sufficient equity in the transaction to justify the accounting and audit principles being applied.

The relationship between Enron and AA was an open one and, according to Mr. Causey, Enron consults AA early and often on accounting and audit issues as they arise. AA concurs with this statement, but points out that in certain of its accounting and audit treatment, it must rely on

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Enron's statement of the business purpose for specific transactions and Enron's valuation of assets placed in the Condor/Whitewing and Raptor structures.

Enron and AA representatives both acknowledge that the accounting treatment on the Condor/Whitewing and Raptor transactions is creative and aggressive but no one has reason to believe that it is inappropriate from a technical standpoint. In this regard, AA consulted with its senior technical experts in its Chicago office regarding the technical accounting treatment on the Condor/Whitewing and Raptor transactions, and the AA partners on the Enron account consulted with AA's senior practice committee in Houston on other aspects of the transactions. Enron may also take comfort from AA's audit opinion and report to the Audit Committee which implicitly approves the transactions involving Condor/Whitewing and Raptor structures in the context of the approval of Enron's financial statements.

Following our initial interview with AA representatives you agreed with us that it was desirable and appropriate to provide them with Ms. Watkins' anonymous letter and supplemental materials so that AA could comment directly on specific allegations contained in those materials. AA identified two allegations in particular that, if accurate, would affect their accounting and audit treatment. Those allegations were, in effect: (i) There was a handshake deal between Mr. Skilling and Mr. Fastow that LJM would never lose money on any transaction with Enron; and (ii) LJM received a cash fee in the Raptor transactions that completely recouped its investment and profit.

Mr. Fastow adamantly denies any agreement with Mr. Skilling or anyone else that LJM would never lose money in transactions with Enron, and he recognized that such an agreement would defeat the accounting treatment that was the very objective for the formation of LJM. Mr. Causey is unaware of any such agreement and has seen no evidence of it.

Both Mr. Fastow and Mr. Causey acknowledge that LJM was to receive a cash fee for its management of the Raptor vehicles in an amount not to exceed \$250,000.00 annually for each company, for a total of \$1,000,000.00 for the four entities. AA was aware of Enron's payment of these fees as well as other organizational costs of the Raptor entities, but these fees fall far short of recouping LJM's investment in the Raptor entities. Both Mr. Fastow and Mr. Causey were quick to point out, however, that in each Raptor vehicle the first transaction was a "put" of Enron shares which was settled favorably to LJM prior to maturity, and as a result thereof, distributions were made to LJM in amounts equal to or greater than its initial investment in those Raptor vehicles. AA is aware of these transactions and is comfortable that, by reason of the applicable special purpose entity accounting rules, the transactions do not undermine LJM's equity investment in the Raptor vehicles.

When questioned about her basis for these two allegations in her anonymous letter and supplemental materials, Ms. Watkins acknowledged that she had no personal, first hand knowledge of either allegation. Both were based solely on rumors that she heard during the two months she was working in Enron Global Finance, and she was uncertain about any details of the alleged cash fee

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allegation. Notwithstanding the lack of any solid basis for the allegations, we think it is likely that AA will seek some kind of assurance from Enron and perhaps from Messrs. Fastow and Causey that no such agreement or cash fee payment occurred.

#### 6. Adequacy of Disclosures

Notwithstanding the expression of concern in Ms. Watkins' anonymous letter and supporting materials regarding the adequacy of Enron's disclosures as to the Condor/Whitewing and Raptor vehicles (which, to a large extent, reflect her opinion), AA is comfortable with the disclosure in the footnotes to the financials describing the Condor/Whitewing and Raptor structures and other relationships and transactions with LJM. AA points out that the transactions involving Condor/Whitewing are disclosed in aggregate terms in the unconsolidated equity affiliates footnote and that the transactions with LJM, including the Raptor transactions, are disclosed in aggregate terms in the related party transactions footnote to the financials.

The concern with adequacy of disclosures is that one can always argue in hindsight that disclosures contained in proxy solicitations, management's discussion and analysis and financial footnotes could be more detailed. In this regard, it is our understanding that Enron's practice is to provide its financial statements and disclosure materials to V&E with a relatively short time frame within which to respond with comments.

#### 7. Potential Bad Cosmetics

Concern was frequently expressed that the transactions involving Condor/Whitewing and Raptor could be portrayed very poorly if subjected to a Wall Street Journal exposé or class action lawsuit. Factors pointed to in support of these concerns included (i) the use of Enron stock to provide equity necessary to do transactions with Condor/Whitewing and Raptor; (ii) recognizing earnings through derivative transactions with Raptor when it could be argued that there was no true "third party" involved in those transactions; (iii) because both merchant investment value and Enron stock have fallen, the Raptor entities may not be able to satisfy their obligations to Enron, thus raising the question "Who ultimately bears this loss?"; (iv) the apparent conflict of interest issue raises questions as to the valuation of assets sold to or that were the subject of transactions with Raptor and the timing of those transactions, (generally at a point when the valuation was at a historical high point).

#### 8. Conclusions

Based on the findings and conclusions set forth with respect to each of the four areas of primary concern discussed above, the facts disclosed through our preliminary investigation do not, in our judgment, warrant a further widespread investigation by independent counsel and auditors.

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Our preliminary investigation, however, leaves us with concern that, because of the bad cosmetics involving the LJM entities and Raptor transactions, coupled with the poor performance of the merchant investment assets placed in those vehicles and the decline in the value of Enron stock, there is a serious risk of adverse publicity and litigation. It also appears that because of the inquiries and issues raised by Ms. Watkins, AA will want additional assurances that Enron had no agreement with LJM that LJM would not lose money on transactions with Enron and that Enron paid no fees to LJM in excess of those previously disclosed to AA. Finally, we believe that some response should be provided to Ms. Watkins to assure her that her concerns were thoroughly reviewed, analyzed, and although found not to raise new or undisclosed information, were given serious consideration.

We have previously reported verbally to Mr. Lay and you regarding our investigation and conclusions and, at your request, have reported the same information to Robert K. Jaedicke, in his capacity of Chairman of the Audit Committee of Enron's Board of Directors. At Dr. Jaedicke's request, we gave a verbal summary of our review and conclusions to the full Audit Committee. Should you desire to discuss any aspect of this written report or any other details regarding our review of this matter, please do not hesitate to contact us at your convenience.

Very truly yours,

VINSON & ELKINS L.L.P.

By: Max Hendrick III  
Max Hendrick, III

C: Joseph C. Dilg  
*Margery partner at V&E*

... THE ONE ...

Mr. BURR. Reclaiming my time, Dean, it is my understanding that under Enron's code of conduct Mr. Fastow would have to have received the blessings of Mr. Lay, who was then CEO and chairman of the board, to participate in the partnerships. Certainly, their accounts might have been out of your report, but Mr. Lay said he was not asked and did not grant his blessings. Is that your understanding?

Mr. POWERS. My understanding is that he would have to get approval by the Office of the Chair.

Mr. BURR. And——

Mr. POWERS. And that included——

Mr. BURR. [continuing] Mr. Lay was the Chair.

Mr. POWERS. He was the Chair, but there were three people in what was called the Office of the Chair.

Mr. BURR. Did you find any of those three that granted permission to Mr. Fastow?

Mr. POWERS. Even though the structure was to go to the Office of the Chair, they actually took that to the board on LJM1 and LJM2, and the board made the findings necessary to permit Mr. Fastow to participate in those partnerships.

Mr. BURR. So the board of directors actually signed off on it.

Mr. POWERS. Yes.

Mr. BURR. And did they also sign off on Mr. Kopper's involvement in partnerships?

Mr. POWERS. No.

Mr. BURR. Was he not under the same code of conduct at Enron, that he would have had to have received the chairman, CEO or board's permission to participate in the partnerships.

Mr. POWERS. Yes, but he did that surreptitiously, I believe.

Mr. BURR. So he got nobody's approval——

Mr. POWERS. Correct.

Mr. BURR. [continuing] to participate in the partnerships.

Mr. POWERS. That is correct.

Mr. BURR. How much did Andersen play in the actual structure of the partnerships?

Mr. POWERS. We don't know how much they actually—whether they designed them. They were contemporaneously to the development; that is, before, for example, Raptor was put in place. They were doing accounting work—it is hard for us to know exactly what they were doing. We have their bills, but whether it was actually designing, doing the accounting, approval work, but they were doing it contemporaneously to the design of these structures, not simply after they had been year-end and being audited.

Mr. GREENWOOD. The time of the gentleman has expired.

Mr. BURR. I would ask unanimous consent for 1 additional minute.

Mr. GREENWOOD. Without objection.

Mr. BURR. I thank the Chair. Let me clear up one thing. Now, Mr. Kopper participated in partnerships, not with the approval of the CEO, the chairman or the board, but it is my understanding that Mr. Fastow and Mr. Skilling were aware of his participation in these partnerships. Is that also your understanding?

Mr. POWERS. Skilling told us that he knew about Chewco and Kopper's involvement in Chewco.

Mr. BURR. So he would have to have known——

Mr. POWERS. And Fastow knew, yes.

Mr. BURR. So both of them would have to have know of Mr. Kopper's involvement.

Mr. POWERS. Yes.

Mr. GREENWOOD. And signed off on it?

Mr. POWERS. Not in anything that is—he may have verbally said, “Go ahead and do it.” He didn't sign off on it in a way that the approval is supposed to be obtained.

Mr. GREENWOOD. In a document.

Mr. POWERS. Yes.

Mr. BURR. On 10-6, Enron took a \$544 million after-tax charge. They also, at the same time, reduced shareholder equity by \$1.2 billion. Less than a month later, Enron restated its financial statement for 1997 through 2001 because of, and I quote, “accounting errors” relating to the transactions with these different partnerships. Who made the accounting errors, Enron, the partnership, Andersen or everybody?

Mr. POWERS. Enron, and to the extent that Andersen was doing the audits, Andersen and Enron.

Mr. GREENWOOD. The time of the gentleman has expired. The Chair recognizes the gentleman from Michigan, Mr. Stupak.

Mr. STUPAK. Thank you, Mr. Chairman. Thank you, Mr. Chairman. Mr. Powers, if your committee isn't going to make any recommendations of discipline to the Board of Directors of Enron, then who is going to make disciplinary or who is going to put forth disciplinary charges against these people?

Mr. POWERS. Well, I think whether the government brings charges, the appropriate government officials are going to have to make, I don't think—one, frankly, we ran out of time, but I think many of these questions as to what Enron would do to these people will become moot. If they don't, somebody is going to have to make that determination. We did not.

Mr. STUPAK. Whether it does or does not, I guess, sitting from where we are sitting, it sort of seems like we have seen all the egregious actions. Someone has a responsibility here to hold people accountable, at least from an employment setting, but yet we are looking the other way and let someone else deal with it, and that seems to be the attitude with Enron——

Mr. POWERS. Yes.

Mr. STUPAK. [continuing] we will just look the other way and let these things go.

Mr. POWERS. Well, I don't think—I doubt if Enron is going to be able to look the other way on these. Enron came out with a press release, I believe, on Saturday, it might have been Sunday, that appointed a committee to restructure—to look into restructuring the board, and I would anticipate that process will go forward with the cooperation of the Creditors Committee.

Mr. STUPAK. Was the—the charge you received in your committee to do this investigation, was that one of your charges, to make recommendations as to any action that should be taken?

Mr. POWERS. Yes, it was. I believe the understanding would be that it would be an ongoing company when we finished our investigation, and that turned out not to be true.

Mr. STUPAK. Well, will your investigation continue now and look at any of this possible disciplinary action, at least from an employment setting?

Mr. POWERS. We haven't made that determination. I will take the opportunity to say being the dean of the University of Texas Law School is a demanding, full-time job, and my fervent hope is I can return to that task.

Mr. STUPAK. But even—and I am sure you will return and do an incredible job there, but will you remain on the board then at Enron?

Mr. POWERS. I anticipate that I will not.

Mr. STUPAK. Okay. Well, I guess, you know—

Mr. POWERS. I would like to—I need to fulfill my obligations to the SEC, and I will do that. But otherwise I anticipate that I will not.

Mr. STUPAK. Okay. Well, we just don't want—you know, I guess I said in my opening statement, there are a lot of these people who are responsible for this whole debacle who are still sitting there—still drawing salaries, still sitting on boards, still sitting in key senior management positions. And I would think if we are ever going to clean this thing up and come out of bankruptcy as a credible company, the board and, as I said in my opening, maybe senior management should be replaced. I just thought it was odd that your committee had an opportunity to at least make some recommendations like that, and once again it was sort of left at the wayside.

Mr. POWERS. But by not doing that, we did not in any way mean to indicate that what you are suggesting is not the appropriate outcome.

Mr. STUPAK. So other than the SEC, who else would take disciplinary action or action against these individuals?

Mr. POWERS. The Department of Justice I think will be looking into these.

Mr. STUPAK. Okay. You indicated to Mr. Dingell's question that in fact you did talk to Cliff Baxter.

Mr. POWERS. I didn't personally, but the committee did.

Mr. STUPAK. Your committee did. And he was the vice president in Mr. Lay's office. You said there were three people in there?

Mr. POWERS. He was, for a time, a vice chairman and part of the Office of the Chair.

Mr. STUPAK. Okay. And, actually, in the Watkins memo, I believe she said that you should talk to Mr. Baxter, especially on the LJM and Raptor transactions.

Mr. POWERS. Yes, that is correct.

Mr. STUPAK. So what did Mr. Baxter say then about—did you ask him about these two transactions or your committee ask him about these two transactions in particular?

Mr. POWERS. We interviewed him, and he was troubled by these transactions and expressed that in his interview as well.

Mr. STUPAK. How long did this interview take place? You said the one with Mr. Fastow was an hour.

Mr. POWERS. People think a couple of hours. I am not sure the person who interviewed Mr. Baxter.

Mr. STUPAK. Would these interviews be recorded or would there be notes of these interviews available?

Mr. POWERS. Yes.

Mr. STUPAK. Would you make them available to the committee?

Mr. POWERS. I certainly would. I would support that. Much of this is the property of the company, and I am not in a position to authorize releasing it. I personally, and the committee would certainly support releasing those; we want to cooperate in every way we can and provide information to this committee.

Mr. STUPAK. It may be something that we have to talk to the chairman later, if need be. To cover everyone's grounds here, we may have to do a subpoena or something like that. It just looked like he was a critical part in the Watkins memo, and unfortunately we will never have a chance to talk with him. So if there is some interview there that we can review that may give us more leads, it would probably be prudent—

Mr. POWERS. From my point of view, I am happy to do what I can to bring that about.

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentleman from Kentucky, Mr. Whitfield?

Mr. WHITFIELD. Dean, from your discussion with those people who did interview Mr. Baxter, was there anything particular that stood out with the committee as to your interview with him? Was there any—

Mr. POWERS. One would not have looked through all of the interviews and thought this is somebody who particularly would be in danger.

Mr. WHITFIELD. Now, what are your areas of expertise in the law?

Mr. POWERS. I teach torts and products liability, I teach some legal philosophy, and then I have also taught contracts and some other subjects.

Mr. WHITFIELD. I see.

Mr. POWERS. Insurance law.

Mr. WHITFIELD. In your report, you talk about the two characteristics of SPEs: One, there must be 3 percent equity by an independent group, and, two, that there not be any control by Enron. And there were a number of those transactions that obviously did not meet that criteria, which meant that the financial statements should be consolidated. From your information or from your knowledge, is that a violation of any law?

Mr. POWERS. I don't know. Whether it is just a violation of accounting principles or law—if it is misrepresented on the financials, that might pick up the securities reporting laws, but just the mere accounting violations, I don't know the answer to that question.

Mr. WHITFIELD. So you are not aware of that?.

Mr. POWERS. I am not, correct.

Mr. WHITFIELD. Now, Vincent & Elkins is no longer legal counsel for Enron; is that correct?

Mr. POWERS. I don't know the answer to that.

Mr. WHITFIELD. I thought that you had indicated to me that they had been dismissed by Enron.

Mr. POWERS. No, Andersen. I do know that Andersen was dismissed by Enron, because that was the reason they gave us for not cooperating further.

Mr. WHITFIELD. What was Mr. Fastow's position with Enron?

Mr. POWERS. He was the chief financial officer.

Mr. WHITFIELD. Do you happen to know what his salary was?

Mr. POWERS. I don't know myself. It was very substantial, but I don't have the figure in my head right now.

Mr. WHITFIELD. But from these independent transactions that he was involved in, you said that he received at least \$30 million from those.

Mr. POWERS. That is what the evidence indicates to us, yes.

Mr. WHITFIELD. And when he realized that he was not going to be able to manage Chewco, he did bring in Mr. Kopper; is that correct?

Mr. POWERS. Yes.

Mr. WHITFIELD. And Mr. Kopper did report directly to Mr. Fastow; is that correct, at Enron?

Mr. POWERS. Yes, at Enron, that is correct.

Mr. WHITFIELD. And then once Mr. Kopper took his management position in the SPE, at some point Enron entered into negotiations to purchase back the interest of Chewco; is that correct?

Mr. POWERS. Yes, that is correct.

Mr. WHITFIELD. And the gentleman that was negotiating for Enron on behalf of Enron's interest, did he also report to Fastow at Enron?

Mr. POWERS. It was Fastow himself who negotiated that, I believe.

Mr. WHITFIELD. Oh, Fastow himself negotiated with Kopper?

Mr. POWERS. Yes.

Mr. WHITFIELD. But wasn't there one incident in another transaction where an employee of Enron was negotiating with Kopper and Mr. Fastow intervened?

Mr. POWERS. Yes.

Mr. WHITFIELD. And that person reported to Mr. Fastow, correct?

Mr. POWERS. I believe that is correct, yes.

Mr. WHITFIELD. And Mr. Fastow basically ordered him or told him to accept the terms as Mr. Kopper offered it; is that correct?

Mr. POWERS. Right, correct.

Mr. WHITFIELD. Do you know the name of that employee?

[Pause.]

Mr. POWERS. Thank you for your indulgence, Congressman. There is a lot of detail here, and it is hard to keep it all straight, and I want to be accurate. In one of them, it was Bill Brown.

Mr. WHITFIELD. Bill Brown?

Mr. POWERS. Yes. In the other, we would want to go back and check the records, if we have that.

Mr. WHITFIELD. But Bill Brown did report to Fastow at Enron.

Mr. POWERS. Yes.

Mr. WHITFIELD. Did Mr. Fastow's wife work at Enron?

Mr. POWERS. Yes, she did.

Mr. WHITFIELD. Was she in the same general area of the company that he was in or do you know?

Mr. POWERS. I am not sure. She was in the finance area, generally.

Mr. WHITFIELD. Okay. So she was in the finance area with Mr. Fastow?

Mr. POWERS. Yes.

Mr. WHITFIELD. And—I see my time has expired here anyway, so—

Mr. GREENWOOD. The Chair thanks the gentleman and recognizes the gentlelady from Colorado, Ms. DeGette.

Ms. DEGETTE. Thank you, Mr. Chairman. Mr. Powers, it looks to me from Martindale Hubble that your specialty is really products liability.

Mr. POWERS. Yes.

Ms. DEGETTE. That is your academic specialty, right?

Mr. POWERS. That is one of them.

Ms. DEGETTE. Okay. Certainly not securities issues.

Mr. POWERS. Absolutely.

Ms. DEGETTE. And Wilmer, Cutler & Pickering was your legal counsel and Deloitte and Touche was your accounting firm.

Mr. POWERS. Yes, that is correct.

Ms. DEGETTE. Are these three gentlemen behind you with one or the other of those firms?

Mr. POWERS. They are from Wilmer, Cutler & Pickering.

Ms. DEGETTE. I know you have been getting advice from them today, and I am wondering if you can identify for the record who they are?

Mr. POWERS. Yes. Bill McLucas, Chuck Davidow and Joe Brenner.

Ms. DEGETTE. Thank you very much.

Mr. POWERS. And I have just been trying to get factual information from them.

Ms. DEGETTE. No, you are doing great. You are doing a lot better than I could do in your position, certainly.

Mr. POWERS. Thank you.

Ms. DEGETTE. I want to follow up on a couple of questions that Chairman Tauzin asked you about Rhythms. In your report, you noted that the Rhythms transaction was the first business dealing that Enron had with the LJM partnership, and that it is significant because, No. 1, it was the first time Enron transferred its own stock to an SPE and used the SPE to hedge an Enron investment. No. 2, it was the first and perhaps most dramatic example of how the purportedly arms-length negotiations between Enron and the LJM partnerships resulted in economic terms skewed toward LJM and enriched Fastow and others. And, third, because in Rhythms the investors included Enron employees who were secretly offered financial interests by Fastow, right?

Mr. POWERS. Yes, that is correct.

Ms. DEGETTE. Okay. I want to walk through this a minute, because I thought the chairman got us to a good point, but I think we need to talk about why this was inappropriate. The first thing that happened was in March 1998, Enron invested \$10 million in Rhythms, which was a privately held company, correct?

Mr. POWERS. Yes, that is correct.

Ms. DEGETTE. And then on April 7, 1999, Rhythms went public at \$21 a share, and then it spiked up to \$69 that day.

Mr. POWERS. Yes.

Ms. DEGETTE. Right?

Mr. POWERS. Yes.

Ms. DEGETTE. The second thing that happened was by May 1999, Enron's investment in Rhythms was worth about \$300 million, but Enron was prohibited from selling its shares by the end of 1999, right?

Mr. POWERS. Yes, that is correct.

Ms. DEGETTE. And so then what happened was Skilling was afraid that because Rhythms was so volatile he wanted to hedge the position to capture the value already achieved and to protect against further volatility, right?

Mr. POWERS. Yes, that is correct.

Ms. DEGETTE. And, in fact, I can tell you Rhythms was a very volatile company, because it just went out of business last year.

Mr. POWERS. Yes.

Ms. DEGETTE. So it was very volatile. All of those would be generally accepted business practices.

Mr. POWERS. Absolutely. There is nothing wrong with that if the hedges were proper.

Ms. DEGETTE. Right, there is nothing wrong with that. But here is where the problem came in and here is where the beginning of the precedent for the later partnerships started. Enron wanted to take advantage of the increase in value in Enron stock, but it can't—under general accounting principles, it can't recognize an increase in its own value of its stock as income, right?

Mr. POWERS. Yes, that is absolutely correct.

Ms. DEGETTE. So what it wanted to do was look at this as a trapped value, right?

Mr. POWERS. That is what they wanted to do.

Ms. DEGETTE. So then what happened is Fastow and others developed a plan to hedge the Rhythms investment by taking advantage of the value in Enron shares covered by the forward contracts, and that is when they created the limited partnership, SPE, right?

Mr. POWERS. Yes, that is correct.

Ms. DEGETTE. And it was capitalized with the appreciated Enron stock, right?

Mr. POWERS. Yes.

Ms. DEGETTE. And that is where the hedging transaction created the problem, and that is where the problem was, right?

Mr. POWERS. Absolutely.

Ms. DEGETTE. And that is against general accepted accounting principles, as far as we know, right?

Mr. POWERS. Yes. You have captured it exactly.

Ms. DEGETTE. And SEC law too, as far as we know.

Mr. POWERS. I would have to look at SEC law, but it certainly ought to be looked into.

Ms. DEGETTE. Right. Okay. And this was kind of the model then for what happened afterwards.

Mr. POWERS. Yes.

Ms. DEGETTE. Okay. Let me talk to you for a few minutes about Rick Causey. He is Enron's chief accounting officer, was and still is today, right?

Mr. POWERS. I have heard newspaper reports that he—I heard reports when I presented this document to the board on Saturday that he had resigned the week before.

Ms. DEGETTE. Okay. But he was up until a—

Mr. POWERS. Up until last week.

Ms. DEGETTE. [continuing] couple of days ago.

Mr. POWERS. And I don't know that he—that report may be accurate. I am just saying I got that report.

Ms. DEGETTE. Okay. You mean you don't always trust the press. Based on the accounting advice your investigation received, you concluded in your report that Mr. Causey's accounting judgment, "went well beyond the aggressive."

Mr. POWERS. Yes.

Ms. DEGETTE. What does that mean?

Mr. POWERS. I think Mr. Causey was not providing proper accounting supervision in the company.

Ms. DEGETTE. That, in your view, is well beyond the aggressive?

Mr. POWERS. Yes.

Ms. DEGETTE. Thank you. Thank you, Mr. Chairman.

Mr. GREENWOOD. The Chair thanks the gentlelady and recognizes the gentleman from Florida, Mr. Stearns.

Mr. STEARNS. Thank you, Mr. Chairman. I am just curious, the chairman opened up his questions with a reference to Star Wars and Luke Skywalker and Darth Vader. When you and your colleagues interviewed Kenneth Lay, did he feel like he was Darth Vader? I mean did he feel like he was a bad guy?

Mr. POWERS. He certainly did not indicate that to us.

Mr. STEARNS. Did he feel like he was a noble public servant and doing the right thing?

Mr. POWERS. That certainly was the attitude he conveyed.

Mr. STEARNS. So all during the 4 hours, he felt that he had done nothing wrong.

Mr. POWERS. I think he felt that he had not been watching carefully enough, but he certainly indicated that he thought he—I am reporting what he said—that—

Mr. STEARNS. Well, that is what I am asking you to do.

Mr. POWERS. [continuing] he had been betrayed and should have looked more carefully.

Mr. STEARNS. So his position has been that he was betrayed, he was high above and didn't know all the details.

Mr. POWERS. That was the position, yes.

Mr. STEARNS. Okay. Mr. Winokur served as chairman of Enron's Finance Committee.

Mr. POWERS. Yes.

Mr. STEARNS. Did you folks interview Mr. Winokur regarding his role as chairman of the Finance Committee?

Mr. POWERS. Yes, we did.

Mr. STEARNS. And you went into his understanding of the LJM transaction?

Mr. POWERS. Yes.

Mr. STEARNS. Okay. Your committee reports, quote, “We have identified some evidence that in three of the transactions where Enron ultimately bought back LJM’s interest, Enron had agreed in advance to protect the LJM partnerships against loss.”

Mr. POWERS. Yes, we say that.

Mr. STEARNS. Okay, you say that. That is on page 12.

Mr. POWERS. And that is correct.

Mr. STEARNS. Okay. How did Enron do this, and if that was true, and Mr. Winokur is chairman of the Finance Committee, is that something that he could accept in his role to have them, as you say, protect LJM’s partnership against loss by guarantying?

Mr. POWERS. Well, we didn’t have any evidence that the Finance Committee, or the Chair of the Finance Committee, was aware of those sort of side agreements to buy back from LJM1.

Mr. STEARNS. But wasn’t his role to understand these transactions?

Mr. POWERS. Our understanding was that these were informal side assurances that don’t worry—

Mr. STEARNS. Well, wait a second. On October 11, 1999, Mr. Winokur presented the LJM2 proposal to the board of directors.

Mr. POWERS. Yes.

Mr. STEARNS. Okay. That is what the minutes show. And he said that he put in controls, indicated he discussed the controls that would be used to guaranty LJM/Enron’s transaction would be fair to Enron.

Mr. POWERS. Yes.

Mr. STEARNS. And so he had some knowledge of this, although you are just saying—

Mr. POWERS. Well, he had knowledge of the structure, and he had knowledge of the kinds of transactions that would take place between Enron and LJM, and the committee put in controls to attempt, unsuccessfully, to mitigate the risks of conflict.

Mr. STEARNS. Okay. What kind of controls did he put in place to, as you say, mitigate, to prevent the loss?

Mr. POWERS. Causey and Rick Buy and Skilling were supposed to look at these transactions and approve them to ensure that they were either arms length, or similar to arms length transactions and were not sweetheart deals. Those were the controls that were put in place.

Mr. STEARNS. Well, it is one thing to put in controls, but then you have got to implement them. So what did he do to make sure and go back—trust and verify, as we would say? What did he do?

Mr. POWERS. Right. I think the board and the committee did not—I am not saying they did not do anything to go back, but they certainly—the controls were not followed.

Mr. STEARNS. So you admit that he had no trust and verify of his controls in place.

Mr. POWERS. Well, I wouldn’t say no trust and verify, inadequate trust and verify.

Mr. STEARNS. On page 105 of the report, it notes that Jeff Skilling’s signature is missing from the LJM2 approval sheet for Raptor I. What knowledge did Skilling have of the Raptor I transaction?

Mr. POWERS. Skilling certainly knew about the transaction that set up the Raptors.

Mr. STEARNS. But why wouldn't he sign it?

Mr. POWERS. I am sorry?

Mr. STEARNS. Why wouldn't he sign it?

Mr. POWERS. This is an approval sheet for hedging—individual hedging deals between the Raptors and Enron after the Raptors had been set up. It wasn't an approval sheet to approve the setting up of the Raptors. The board did that.

Mr. STEARNS. So in your opinion, his signature wasn't needed?

Mr. POWERS. I am sorry. This was an approval sheet for setting up that Raptor. He didn't sign it; he was at the board meeting that approved it.

Mr. STEARNS. And so why didn't he sign it? I mean I am not asking you.

Mr. POWERS. Right.

Mr. STEARNS. I mean just don't you think that that shows something?

Mr. POWERS. Right.

Mr. STEARNS. And what do you think that shows, the fact that he doesn't sign it, as a lawyer?

Mr. POWERS. He was at the board meeting that approved it. He was at the board meeting that approved it. I really don't know whether—I don't know why he didn't sign it.

Mr. STEARNS. But the thing that strikes me here is Winokur was, as chairman of the Finance Committee, he was responsible for putting in the controls and then making sure the controls were implemented. Now, wasn't he part of this report? Wasn't he on your board on this report?

Mr. POWERS. He was. He did recuse himself from the judgments about the board. Mr. Troubh and I had several conversations with counsel independently without Mr. Winokur when we made our conclusions about the board.

Mr. STEARNS. Do you think Skilling knew about these side agreements that were protecting these partnerships and ensuring that Enron would guaranty them?

Mr. POWERS. From the evidence that I have seen, I don't know that I can answer that. There is a great deal of evidence that he knew about the transactions.

Mr. STEARNS. And you are saying Mr. Winokur had no idea also about these side agreements, and he never followed up with a trust and verify, he never did some verification of the controls that he put in place?

Mr. POWERS. I think these are going to take further investigation. I can say what we were able to ascertain from our interviews and evidence, and we don't have any evidence that he was aware of those side agreements.

Mr. STEARNS. Thank you, Dean.

Mr. GREENWOOD. The time of the gentleman has expired. The Chair recognizes the gentleman from Louisiana, Mr. John.

Mr. JOHN. Mr. Powers, on Friday, the Wall Street Journal reported that Mr. Lay told other Enron officials that he had never heard of Chewco. In your 4-hour interview with him, did he indicate anything to that effect or did he tell you that? Chewco.

Mr. POWERS. He was at the Executive Committee meeting that approved the transaction. He did say at his interview that he didn't recall the name.

Mr. JOHN. Thank you. The rest of my questions really are going to be focused on the accounting side with Mr. Causey, because I think that it is very important. Your report specifically states that Mr. Causey was charged by the board of directors with a substantial role in the oversight of Enron's relationship with the LJM partnerships; in fact, he was supposed to review and approve every transaction—

Mr. POWERS. Yes, that is correct.

Mr. JOHN. [continuing] within LJM to determine if it was in the best interest of Enron.

Mr. POWERS. Yes.

Mr. JOHN. And then he was supposed to report that to the board of directors, correct?

Mr. POWERS. Yes.

Mr. JOHN. Mr. Causey told the board everything was fine, even though his approvals came after the deals were finalized. Without Mr. Skilling's signature and your report concludes that many of the most significant transactions apparently were designed to accomplish favorable financial statement results, not to achieve bona fide economic objectives or a transfer of risk. Again, according to your report on page 4, the transactions did not follow the applicable accounting rules. What was Mr. Causey's excuse in your interview with him for not carrying out these duties?

Mr. POWERS. In this interview, he said that he thought he was responsible only for signing off on the accounting, which, in our view, was not consistent with what his charge was by the board.

Mr. JOHN. But he was in fact the chief accounting officer.

Mr. POWERS. He was.

Mr. JOHN. In fact, in one instance, involving a Fastow partnership named Talon, on page 108 in your report—

Mr. POWERS. Yes.

Mr. JOHN. [continuing] Mr. Causey actually backdated a document of a swap so that Enron would not have to show about \$75 million on its quarterly financial statements. Backdating documents to hide losses from shareholders, is that fraud?

Mr. POWERS. Well, backdating is extremely serious. I would have to trace through what was then reported to the shareholders to determine—and backdating the intent does seem easy. And I don't—I need to check. There was backdating, we did find evidence of backdating in some of these transactions, which is, individually, very serious. I would have to check.

Mr. JOHN. As it relates to Talon.

Mr. POWERS. Yes. That is the first Raptor vehicle, and there were hedges with the Raptor vehicle, and we found very compelling evidence that some of those transactions were backdated.

Mr. JOHN. And in your own words, these are very serious when you—

Mr. POWERS. Yes, very serious.

Mr. JOHN. Mr. Powers, Mr. Causey told our investigators here that he didn't see the collapse of Enron coming and awoke to it once the Wall Street Journal began reporting on the company's

troubles in October of last year. In your expert opinion, shouldn't the chief accounting officer and the person responsible of approving every single transaction with Mr. Fastow's entities, have identified some warning signs? Don't you think there should have been some warning signs before October of last year.

Mr. POWERS. Absolutely.

Mr. JOHN. If so, what do you think he should have seen or did not come—what do you think—give me maybe an idea of what maybe he should have at least notified the board of, or Mr. Fastow, or alerted them?

Mr. POWERS. Well, as we document in the report, these were not real transactions, and he was the chief accounting officer, and should and I think did—he certainly knew about the nature of the transactions. And has subsequently turned out, that structure made the company extremely fragile economically, because it wasn't solidly backed, and he should have warned the board about that, he should have talked to senior management about it. He was the chief accounting officer, he should have done something about it.

Mr. JOHN. Real quick, if you could summarize, I guess, Mr. Causey's failures as the lead accountant of the company, how would that summary read?

Mr. POWERS. He was not an effective check on Mr. Fastow, and the accountant needs to be an effective check.

Mr. JOHN. Was it a lack of his credentials and his training and background?

Mr. POWERS. Not to my knowledge.

Mr. JOHN. Thank you.

Mr. GREENWOOD. The time of the gentleman has expired. The Chair recognizes the gentleman from New Hampshire, Mr. Bass.

Mr. BASS. Thank you, Mr. Chairman. Dean Powers, you have obviously overseen a very detailed report here, an investigation, and in the very end of your testimony, in the last very paragraph, in the first sentence, you say, "In the end, this is a tragedy that could and should have been avoided." Without getting into the kind of detail where you are discussing what individuals did or didn't do, who signed what, who was reporting to who, who transferred money from here to there, how could this tragedy have been avoided, in your opinion?

Mr. POWERS. Well, as somebody who invests at a very, very modest level myself, I see the idea of statements to the public that there should be transparency in the financial condition of a company. And if there was more transparency about the finances of Enron, the market would have reacted to that and, frankly, adjusted in ways that wouldn't have let Enron get away with it, if there had been more transparency.

Mr. BASS. Well, then what, in your opinion, aspects of the regulatory structure created an environment in which there wouldn't be the kind of transparency that should have been with Enron?

Mr. POWERS. I want to give the judgments that I feel I can give. I am not, in any way, an expert in securities regulation and how that regulatory structure would have or might have detected some of these problems.

Mr. BASS. Well, is, in your opinion, the Enron investigation, in general, then, primarily a criminal or a justice-related investigation dealing with individuals who may have broken the law? Or are there thematic conclusions from your report that require increased or more aggressive oversight on the part of either regulators or policymakers, like the Congress?

Mr. POWERS. Well, I think there certainly was individual wrongdoing that needs to be investigated by the proper authorities. But I think there are larger issues that are raised by what we found in our report.

Mr. BASS. What larger issues are you thinking about?

Mr. POWERS. Yes, they deal with 401(k) plans, they deal with the accounting industry. Not having looked into them and not being an expert, I don't know that I have particular suggestions, but I do think those are important issues that the Congress and the committees need to look into.

Mr. BASS. This may be a repetitive question, but the second sentence in your last paragraph says that you hope that our report and the work of your committee will help reduce the danger that it will happen to some other company. How do you think that?

Mr. POWERS. Well, I think by bringing to light what happened, I hope that your committee, other congressional committees at least have a starting point as to some of the problems, and that this will help, in a small way, to focus attention on some of these problems and that our Congress, State legislators, other regulatory and policymaking groups will respond to some of these problems.

Mr. BASS. One last question, Dean Powers. Were there any questions that—are there any questions that have come about as a result of the report that you are presenting or the investigation that you conducted that you don't have answers to at this point?

Mr. POWERS. You mean with respect to the particular events?

Mr. BASS. Yes.

Mr. POWERS. Oh, absolutely. Much more needs to be done. Who knew what when? We, again, did not have subpoena power, did not have true cross examination power, and I think this report is just a start.

Mr. BASS. Thank you, Mr. Chairman.

Mr. GREENWOOD. The Chair thanks the gentleman. The gentleman from Florida, Mr. Stearns, made reference to a document that I would, without objection, enter into the record. It is an excerpt from the October 11 and 12, 1999 Enron Corporation Board of Directors meeting.

[The information referred to follows:]

**EXCERPT FROM OCTOBER 11-12, 1999  
ENRON CORP. BOARD OF DIRECTORS MEETING**

Mr. Winokur then discussed information concerning an unaffiliated investment partnership, LJM 2, and stated that the partnership could possibly provide the Company with an alternative, optional source of private equity to manage its investment portfolio risk, funds flow, and financial flexibility. He noted that Mr. Andrew S. Fastow would be acting as the managing partner of LJM 2 and discussed Mr. Fastow's role in the LJM 2 partnership. He commented on the controls that would be put in place to manage any transactions between the Company and LJM 2 and noted that the Company and LJM 2 were not obligated to one another in any way. He noted that the controls include review and approval of all transactions by the Chief Accounting Officer and the Chief Risk Officer of the Company. He stated that the Audit and Compliance Committee would, on an annual basis, review all transactions completed within the past year and make any recommendations they deemed appropriate. He stated that the Company's Conduct of Business Affairs Policies (relating to investments and outside business interests of officers and employees) would prohibit Mr. Fastow from participating in LJM 2 as managing partner due to his position as Executive Vice President and Chief Financial Officer of the Company, absent appropriate reviews and waivers from the Board and a finding that such participation does not adversely affect the best interests of the Company. He recommended that such review and findings be made in this instance, his motion was duly seconded by Mr. Urquhart, and carried, and the following resolutions were approved:

WHEREAS, Andrew S. Fastow serves as the Executive Vice President and Chief Financial Officer of the Company;

WHEREAS, Mr. Fastow has the opportunity to participate in the formation of an investment partnership (the "Partnership") that would not be affiliated with the Company;

WHEREAS, it is anticipated that Mr. Fastow will serve as the managing partner/manager of the Partnership;

WHEREAS, it is anticipated that the Partnership will invest in energy and communications-related businesses and assets, including businesses and assets of the Company;

WHEREAS, the Partnership, as a potential ready purchaser of the Company's businesses and assets or as a potential contract

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counterparty, could provide liquidity, risk management, and other financial benefits to the Company;

WHEREAS, the Office of the Chairman of the Company has determined, for the foregoing reasons, that Mr. Fastow's participation as the managing partner/manager of the Partnership will not adversely affect the interests of the Company;

NOW, THEREFORE IT IS RESOLVED, that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Conduct of Business Affairs/Investments and Outside Business Interests of Officers and Employees that participation of Mr. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

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**EXCERPT FROM OCTOBER 11, 1999  
ENRON CORP. FINANCE COMMITTEE MEETING**

Mr. Winokur called upon Mr. Fastow to present the Chief Financial Officer's report. Mr. Fastow reviewed the Company's key financial ratios and long-term liability analysis, noting the mix between fixed and floating rate liabilities and on-balance and off-balance sheet debt. He discussed the Company's stock trading portfolio and noted changes since the beginning of the year. He reviewed the investments made year-to-date by each business unit and compared them to the plan amount. He discussed the status of capital commitments year-to-date and commented on the transactions the Company had taken or would be taking to fund the cash outflows and noted the importance of funds flow to the Credit Rating Agencies. He distributed a handout on funds flow, a copy of which is filed with the records of the meeting. He discussed issues impacting funds flow and how the Company was managing funds flow, including vehicles currently in place and the strategy for the future. A copy of Mr. Fastow's report is filed with the records of the meeting.

Mr. Fastow then updated the Committee on a financing structure approved earlier in the year, LJM 1, and discussed the benefits that the Company had incurred since the transaction closed on June 30, 1999. He recommended that the Company continue to syndicate capital investments to address the funds flow issue. He presented information concerning an unaffiliated investment partnership, LJM 2, and discussed the rationale and benefits of the proposed partnership. He stated that the partnership could possibly provide the Company with an alternative, optional source of private equity to manage its investment portfolio risk, funds flow, and financial flexibility. He noted that he would be acting as managing partner of LJM 2 and discussed his role in the LJM 2 partnership and how it would benefit the Company. He commented on the differences between LJM 1 and LJM 2, the controls that would be put in place to manage any transactions between the Company and LJM 2, the fund fees and promote, and any required disclosure. He noted that the controls include review and approval of all transactions by the Chief Accounting Officer and the Chief Risk Officer of the Company. He stated that the Audit and Compliance Committee would, on an annual basis, review all transactions completed within the past year and make any recommendations they deemed appropriate. He noted that the Company's Conduct of Business Affairs Policies (relating to investments and outside business interests of officers and employees) would prohibit him from participating in LJM 2 as managing partner due to his position as Executive Vice President and Chief Financial Officer of the Company, absent appropriate reviews and waivers from the Board and a finding that such participation does not adversely affect the best interests of the Company. He asked that the Committee recommend to the Board that such review and findings be made in this instance to allow his participation. Messrs. Causey, Fastow, and Skilling answered questions from the Committee concerning the role of other partners, the review by Arthur Andersen LLP, and the benefits to the Company, which included having another potential buyer of assets and provider of capital, of having Mr. Fastow act as managing partner. Following a discussion, upon

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motion duly made by Mr. Meyer, seconded by Mr. Blake, and carried, the proposed waiver of the aforementioned policy, including findings of no adverse effects to the best interests of the Company related to Mr. Fastow's involvement in LJM 2, was approved for recommendation to the Board. A copy of Mr. Fastow's report is filed with the records of the meeting.

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Mr. GREENWOOD. The Chair recognizes the gentleman from Illinois, Mr. Rush.

Mr. RUSH. Thank you, Mr. Chairman. Mr. Powers, I want to commend you on your stamina. This has been a very long session, and you have certainly stood up quite well.

Mr. POWERS. Thank you.

Mr. RUSH. Again, I commend you for your stamina. Our investigators were also told that Enron had more than 900 accountants reporting to Mr. Causey, and I think that my colleague from Louisiana, Mr. John, pointed to this direction. And this 900 accountants does not include the nearly 100 accountants that Arthur Andersen supplied to audit Enron. How is it possible that Mr. Causey could not see this train wreck coming when he apparently had almost 1,000 accountants on the Enron work force?

Mr. POWERS. I think it is that Mr. Causey, as the chief accountant, would have seen these problems.

Mr. RUSH. You think that he actually saw this problem.

Mr. POWERS. I think he certainly should have, and I would expect that he would have.

Mr. RUSH. Okay. Well, with all these accountants, 900 accountants of its own, who had access to all these internal records, in your opinion, how can Enron blame Arthur Andersen alone for not revealing the accounting shenanigans that were taking place? And are Enron's accountants simply incompetent or not well trained or shouldn't they have known Enron's numbers even more than Andersen should?

Mr. POWERS. We certainly did not intend to, and I don't think we have, made judgments or, as you put it, blamed Andersen alone. I think the Accounting Department within Enron and people outside the Accounting Department, including all of the people in management and the board, bear responsibility for this.

Mr. RUSH. Well, I want to return quickly, if I could, back to Mr. Fastow. One conclusion surfaces from our investigation into Enron is that on one was minding the store. It was almost like the fat rat was in the cheese factory, and the cat was on vacation. No single person appeared willing to come forward and say it was their job to take a big picture view of the multitude of deals and transactions taking place to assess how much risk the company was assuming. Shouldn't that job have been the chief financial officer's job or Mr. Fastow's job?

Mr. POWERS. Well, I think the chief financial officer—I am sorry, the chief financial officer or the chief accounting officer?

Mr. RUSH. The chief financial officer.

Mr. POWERS. The chief financial officer. Well, the chief financial officer is certainly responsible for the financial aspects of the company, and certainly these were within the financial areas of the company. The problem with Mr. Fastow wasn't in a position to mind the store, because he was personally and directly involved in these transactions.

Mr. RUSH. Well, isn't it true also, according to your report, you term Mr. Fastow as a, quote, "walking conflict of interest," and that Mr. Fastow got more income from his outside businesses in 2 years than he did from Enron; is that accurate?

Mr. POWERS. He certainly got very substantial income from these outside investments.

Mr. RUSH. Mr. Fastow, I call him "Fast Andy," Fast Andy was known to curse and abuse people who got in the way of his partnerships. He told Mr. Jeff McMahon, the treasurer, that he couldn't work with him because McMahon was, quote, "screwing up his deals." Where was the chairman at in all of this? Why didn't the chairman put a stop to this?

Mr. POWERS. Well, McMahon went and complained to Skilling, and Skilling then transferred McMahon to another part of the company. And Skilling, from our information, then didn't do anything about McMahon's very accurate and serious issues that he had raised with Skilling.

Mr. RUSH. I have one final question, Mr. Chairman, if I could. I want to get back to the Talon transaction. Mr. Fastow negotiated directly with Mr. Causey, putting together a deal that gave LJM2 \$41 million for basically nothing, according to your report on page 108; is that right?

Mr. POWERS. I want to clarify this.

[Pause.]

Mr. POWERS. I think it was Ben Glisan who was involved in that negotiation, and I don't want to be inaccurate about the other person involved in it. I would have to go back and look more carefully.

Mr. RUSH. Thank you, Mr. Chairman. I yield back.

Mr. GREENWOOD. The Chair thanks the gentleman. The gentleman from Texas, Mr. Green, is recognized for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman, and, again, I would like to thank you for your courtesy as allowing me as the member of the full committee but not of the subcommittee to come in and ask questions. I want to continue following up what my colleague from Chicago mentioned on that LJM2, the \$41 million. Sorry, I didn't hear the answer. Do you think he violated Mr. Fastow—by negotiating directly, Mr. Causey violated an agreement not to negotiate with these entities?

Mr. POWERS. I think Fastow was negotiating on LJM. There is lots that Fastow did wrong, but in that negotiation, I believe he was negotiating on LJM's side. He was not negotiating—

Mr. GREEN. On Enron's side.

Mr. POWERS. [continuing] on Enron's side. Now, the idea of Fastow and Causey doing a real arms-length negotiation is very problematic.

Mr. GREEN. Okay. And Mr. Causey, by representing Enron, could have stopped that negotiation, I guess.

Mr. POWERS. Well, that kind of negotiation with LJM had been approved. He and others could have identified the inappropriate nature of the conflict of the whole structure.

Mr. GREEN. Who else is in a position to stop or disagree with the inappropriateness, as you said, of the whole structure? Our staff was told yesterday anyone with an understanding of how general partners are paid would have quickly understood that Mr. Fastow would get at least \$15 million from the LJM2 alone. Was anyone at Enron or his board, were they that inexperienced in the world of finance that they couldn't do the same calculations?

Mr. POWERS. That is certainly a question that we had. LJM1, I think the board looked into more carefully. It was a much smaller partnership, and those calculations came to a much more reasonable number. When LJM2 was set up, it was a much larger partnership. I think there was a sense that it was like LJM1, therefore let us go ahead and approve it. The problem was it was a much larger partnership, and if one had run these numbers, it would have suggested that Fastow might have a quite substantial return.

Mr. GREEN. On page 43 of your report, it indicates Mr. Fastow had planned to merge Chewco until he was told that the participation be revealed in Enron's proxy statement.

Mr. POWERS. Yes, that is correct.

Mr. GREEN. And at that point, Mr. Fastow substituted Mr. Kopper?

Mr. POWERS. Yes.

Mr. GREEN. If anyone in the company knew this, do you think the board knew it?

Mr. POWERS. I don't—

Mr. GREEN. And why do you think they knew it?

Mr. POWERS. We don't have any evidence that they did.

Mr. GREEN. What are the—a CFO in a corporation, I know they have typically defined, particularly a company as large as Enron, have defined responsibilities. Isn't that person the person the investors and the shareholders depend on to give a credible picture of the company's finances?

Mr. POWERS. Well, the chief financial officer and the chief accounting officer, yes.

Mr. GREEN. If Mr. Fastow was doing his job properly, would this train wreck would have happened?

Mr. POWERS. If Mr. Fastow had been doing his job properly, it would have substantially reduced. I can't say in hindsight whether it would have prevented it. They would have never gotten into these deals if he had been—if he had been raising questions about them, I think there is a substantial likelihood that this train wreck would not have happened.

Mr. GREEN. So the debt just kept piling up. So Enron had too much debt, and too many bad investments kept piling up.

Mr. POWERS. It had a great deal of debt, and it had—I think if they had taken the—well, one can't tell what had happened. It wasn't just that they didn't take the loss on the investments and as they were happening take charges. They had these hedging arrangements that, in a sense, were acting as though those losses were not there.

Mr. GREEN. Did your committee specifically find out what actions Mr. Fastow failed to do, to take, as CFO, that might dramatically have mitigated the events that overtook Enron?

Mr. POWERS. Well, he should have come forward and disclosed that he was self-dealing with the company on a much larger scale than he had ever indicated.

Mr. GREEN. Thank you, Mr. Chairman.

Mr. GREENWOOD. The time of the gentleman has expired. The Chair would note his intention to initiate another round of questions. Mr. Powers, are you good for another half hour or so, or would you like a break?

Mr. POWERS. No, I am fine, Mr. Chairman.

Mr. GREENWOOD. Okay. In that case, the Chair recognizes himself for 5 minutes. Mr. Powers, on page 43 of your report, it reads, "Fastow told Enron employees that Jeffrey Skilling, then Enron's president and chief operating officer, had approved his participation in Chewco as long as it would not have to be disclosed in Enron's proxy statement." Who are the employees that Fastow told that to? How do you know that? If you need to consult—

Mr. POWERS. Well, let me read the statement. Could I—

Mr. GREENWOOD. Please.

Mr. POWERS. One of the people he told was Bill Brown, who I mentioned before, and Mr. Brown has notes that reflect that.

Mr. GREENWOOD. Do you have those notes that you could share with us?

Mr. POWERS. We don't have them here, and, again, I will support cooperating in every way, and I think the company will as well. I don't, myself, have the authority to dispose of the company—

Mr. GREENWOOD. Do you know what Skilling said about that? Did Skilling comment on that observation?

Mr. POWERS. I believe Skilling said that he didn't—

Mr. GREENWOOD. There is a footnote that says, "Skilling told us that he recalled Fastow—

Mr. POWERS. Yes. Thank you.

Mr. GREENWOOD. [continuing] proposing that the Chewco outside investors be members of Fastow's wife's family, and Skilling told Fastow he did not think that was a good idea."

Mr. POWERS. Correct.

Mr. GREENWOOD. Okay.

Mr. POWERS. Thank you.

Mr. GREENWOOD. The Special Committee's report states Jeff Skilling appeared to be entirely uninvolved in the review of the Chewco transactions, despite, quote, "representations made to the board that he had undertaken a significant role."

Mr. POWERS. Yes.

Mr. GREENWOOD. That is from page 10. What were these representations and who made them?

Mr. POWERS. I believe these are the LJM transactions. Chewco was more of an investment fund, and the LJM transactions were the transactions where there was more self-dealing. And Skilling represented to the board, or to the Finance Committee, I would have to clarify that Fastow represented to the board that these controls would be put in place. Skilling was at that board meeting when those representations were made, and the representations were that Skilling and Causey and Buy would review the transactions to make sure that they were at arms length and not self-enriching to Fastow.

Mr. GREENWOOD. The Special Committee's report states that the critical piece of missing information relating to the Chewco transaction was the side agreement for the \$6 million Enron collateralization of the partnership outside \$11.4 million equity investment by Big River Funding, LLC, which is a partnership controlled by Michael Kopper and his domestic partner, William Dodson. At least one Enron official, Ben Glisan, knew of these facts. Andersen says it knew nothing about this aspect of the

Chewco transaction. What evidence did you uncover about who knew what and when with respect to this side agreement on Chewco?

Mr. POWERS. Well, we were able to ascertain that Glisan was involved in setting up—in doing the work around Big River and Little River. And he would have known that the loans from Barclay's were being backed by reserve accounts that had been provided by distributions from JEDI, but let me make sure I get this right. I am told we don't have notes that definitely pin that down.

Mr. GREENWOOD. How did you discover this side agreement? Who found out about that?

Mr. POWERS. Well, when these issues—there is some unclarity as to whether we have those notes or not. Let me just clarify. I am sorry. We do have notes that show that Glisan was at meetings where the reserve accounts were described.

Mr. GREENWOOD. And we would ask that you share those notes with our staff.

Mr. POWERS. The same thing.

Mr. GREENWOOD. Thank you.

The Special Committee's report also states that if Glisan in fact knew about the \$6 million side agreement, it is, "implausible that he or any other knowledgeable accountant would have concluded that Chewco met the 3 percent standard." That is from page 53. Since the Special Committee's report concludes that Glisan knew about the side agreement, are you in effect saying that he knowingly approved faulty accounting for this transaction?

Mr. POWERS. To the extent he was at that meeting and to the extent that he knew, our view is that a knowledgeable accountant like Glisan would know that was faulty accounting. We did not come across anyone who, once they understood the Big River and Little River loans were backed by essentially Enron disbursements from JEDI, everybody agreed immediately that that was an improperly funded SPE.

Mr. GREENWOOD. My understanding is that the \$6 million side agreement was not discovered until late October of 2001, after Enron started to look more closely into this transaction. Do you know who at Enron discovered this side deal and how the discovery actually took place?

Mr. POWERS. No, I am sure we do.

[Pause.]

Mr. POWERS. I want to clarify one thing. It may very well be that people at Enron knew about this before it came up in October. The larger Enron group, the accounting and legal staff, went back and started looking into it as events started to unfold in October. And I don't have the individuals, but, again, I think—

Mr. GREENWOOD. Was it found in Enron's documents? Was it found in Vincent & Elkins' documents?

Mr. POWERS. In Enron's documents and I think both.

Mr. GREENWOOD. Both? Okay. The Chair recognizes the gentleman from Florida, Mr. Deutsch.

Mr. DEUTSCH. Thank you, Mr. Chairman. I know we have been talking about Mr. Powers, so let me just go back to a question. Actually, Mr. Fastow widely reported questionable activities, directly or indirectly, paramount to fraud on Enron stockholders. It was his

concealment of the lack of independent equity in these partnerships that kept the losses off Enron's books for at least 2 years. Isn't that fraud on the shareholders?

Mr. POWERS. My only hesitation is I don't know myself the securities definition of fraud because that is not my field. It is misrepresenting things to the shareholder.

Mr. DEUTSCH. All right. The Wall Street Journal reported last week that Mr. Fastow and Mr. Skilling dreamed up all of these partnerships to hide debt and hedge losses. Mr. Fastow was required under the company's code of conduct to reveal his interests in these partnerships in writing to Mr. Lay and Mr. Skilling. Did Mr. Skilling receive such a document in writing, as required under the agreement?

Mr. POWERS. The evidence we have is that Skilling got a handwritten note from Fastow.

Mr. DEUTSCH. Have you seen it?

Mr. POWERS. Yes—oh, no. That is just reported to us.

Mr. DEUTSCH. Did Mr. Skilling ever ask for legal advice, either from inside or outside the company, on the procedures for waiving the code of conduct and what was appropriate and what was not?

Mr. POWERS. I don't know. Not to my knowledge.

Mr. DEUTSCH. Did Mr. Skilling ever consider that an officer's loyalties might be conflicted if he was receiving more income from his non-Enron business than from his Enron job?

Mr. POWERS. Did he consider that?

Mr. DEUTSCH. That is correct.

Mr. POWERS. The interview with Fastow did not reveal much information where we could get an answer to that question.

Mr. DEUTSCH. Right, but it would seem Mr. Skilling, in terms of evaluating where his loyalties would be.

Mr. POWERS. Oh, I am sorry. Yes, certainly, Mr. Skilling and everyone involved in approving LJM1 and LJM2 understood that there would be a conflict of loyalties that Fastow had.

Mr. DEUTSCH. And Mr. Skilling and the board could have required Mr. Fastow to share his offering documents and reveal his fee structure; is that correct?

Mr. POWERS. That is correct. I believe the board and management could have done that.

Mr. DEUTSCH. And why didn't they?

Mr. POWERS. Their explanation is that they wanted to make the LJM partnerships as, "independent" as possible, and looking into the financial structure of the partnerships would somehow be inconsistent with that. We still think they could have gotten K-1s and other information about Mr. Fastow's remuneration.

Mr. DEUTSCH. Right. And, again, it seems as if your concern is really a conflict, that would be almost a requirement to understand that.

Mr. POWERS. I would think, at a minimum, you would want to know what the compensation for Ms. Fastow would be.

Mr. DEUTSCH. Did Mr. Skilling ever ask to see any of the offering papers of the Fastow entities?

Mr. POWERS. Not to my knowledge.

Mr. DEUTSCH. According to a Fortune magazine article, Mr. Skilling errantly responded to those who questioned how Enron

made its money by saying, "People who raise questions are people who have not gone through our business in detail and who want to throw rocks at us." Based upon your own investigation, don't you think that as chief executive officer, Mr. Skilling himself knew how Enron was cooking the books?

Mr. POWERS. I think Mr. Skilling knew a great deal about these transactions and how losses were being hedged with Enron's own stock, yes.

Mr. DEUTSCH. And in fact, Mr. Powers, doesn't your report state that Skilling, and I quoted from the report, "had direct responsibility for ensuring that those reporting to him performed their oversight responsibilities properly and that Skilling did not appear to have given much attention to these duties." Are you saying that Mr. Skilling was inattentive and didn't understand his own company or—I mean is that the answer or is this again a case of fraud?

Mr. POWERS. Well, at a minimum, he wasn't attending to his own company. He claims in his interview that he knew very little about them. Causey and others say that he was very involved in them. And to answer that question, I think the proper investigators and authorities are going to have to ascertain what his state of mind was.

Mr. DEUTSCH. Right. And the last question: Mr. Skilling was supposed to review and sign off on each of these deals, these are the partnerships. He didn't, but he allowed Mr. Causey to tell the board that everything was fine. As CEO and also president and chief operating officer, wasn't Mr. Skilling's primary obligations, again, I mean violated by that action?

Mr. POWERS. Yes. I don't think he performed his function.

Mr. DEUTSCH. Thank you.

Mr. WHITFIELD [presiding]. The gentleman's time has expired. At this time, we will call on the chairman of the entire committee, Mr. Tauzin.

Chairman TAUZIN. Thank you, Mr. Chairman. Dean Powers, the New York Times reports that Mr. Skilling may not have been aware of what was happening, but he was certainly, and this is a quote, "in no mood to hear anybody question what went on at Enron." The quote is, "In early April, when Enron reported its freshly scrubbed, and apparently falsified, first quarter profits, Mr. Skilling bristled when one questioner on the conference call tried to ask questions about the company's balance sheet. He used a vulgarity to describe the question, stunning many who were listening to the call." We produced documents indicating that when members in the corporation sent signatures sheets around to indicate approval of all these transactions that LJM1 and LJM2 were conducting, and everybody signed except one person. There is one signature missing—Jeffrey Skilling's. Did you see those documents? Did you have any questions about why Mr. Skilling didn't sign those approval documents?

Mr. POWERS. Yes.

Chairman TAUZIN. What did you learn?

Mr. POWERS. He didn't explain it. He was at the board meeting, though, that voted on it.

Chairman TAUZIN. Yes. You do know that Jordan Mintz sent him a memo saying, here are all the documents. Please sign them.

Mr. POWERS. Yes.

Chairman TAUZIN. Did he explain why he didn't sign them? Three times I think he tried to call. Mintz was doing everything he could to get Mr. Skilling on the record as saying these deals were okay and everything was honkey-dory, and Mr. Skilling wouldn't sign them.

Mr. POWERS. Absolutely. I understand he should have signed them, it was his responsibility to sign them, and he didn't sign them.

Chairman TAUZIN. And we just don't know why.

Mr. POWERS. He didn't explain that to us.

Chairman TAUZIN. I will take you to page 95, because the question of corporate self-dealing and profiteering is a pretty interesting one. In the report you issued, on page 95, you talk about the—I think it is the South Hampton deal.

Mr. POWERS. Yes.

Chairman TAUZIN. In which a group called the Fastow Family Foundation, which was composed of people like Glisan. We just heard about Enron employee, Mr. Glisan, who later became treasurer of Enron.

Mr. POWERS. Right. It was the Family Foundation and Glisan.

Chairman TAUZIN. And also Mordaunt.

Mr. POWERS. And Mordaunt.

Chairman TAUZIN. And Mordaunt and Glisan were part of the Family Foundation, as well as separate investors, right?

Mr. POWERS. No, I don't think they were part of the Family Foundation.

Chairman TAUZIN. Well, let us go back to your report on page 93: "The limited partners were the Fastow Family Foundation, signed by Fastow, the director, Glisan, Mordaunt"—you mean they were separate investors.

Mr. POWERS. Yes.

Chairman TAUZIN. They were not part of the foundation.

Mr. POWERS. We don't know who was in the Family Foundation.

Chairman TAUZIN. We don't know.

Mr. POWERS. Yes.

Chairman TAUZIN. But the Family Foundation puts up 25 grand. Big Doe Foundation, whatever that is, puts up another bunch of money, and Glisan and Mordaunt, as well as some of the other Enron employees, including Yaeger Patel, I think, who was married—at the time some of the negotiations were going on, they were engaged, the two Patels. They later signed as marriage partners, and they were operating on different sides of the table. Talk about a sweetheart deal, that was really interesting.

But these players, Glisan and Mordaunt, put up \$5,800 each. Within 6 weeks, they each received \$1 million, and they apparently told you they don't know—nobody explained to them why they got such a big return in 6 weeks, but they took the money. And you asked the question, "The magnitude of these returns raises serious questions as to why Fastow and Kopper offered these investments to other employees." I think the answer comes in the next paragraph. You talk about what those other employees did. You have Glisan who has presented to the Raptor I transaction to the board. He was called the business unit originator and the person negoti-

ating for Enron. He is the guy on the other side of the table, and Fastow says, "Come on in and be an investor on this side of the table, and you make a million dollars as a result in 6 weeks." And you asked the question why they offered him this deal?

You also asked the question why Mordaunt was involved? Well, we find out Mordaunt was a lawyer. She was involved in the initial Rhythm transaction, general counsel structured finance. She becomes later the general counsel of Enron Communications and later the Enron Broadband Services Board where all this broadband capacity was transferred out to one of these partnerships in an attempt to show a lot of profit that never existed. And you asked why they were interested in bringing her in and letting her earn a million dollars? Isn't the answer quite obvious?

Mr. POWERS. Well, let me say why we asked the question.

Chairman TAUZIN. Yes.

Mr. POWERS. We tried to be very careful in this report—

Chairman TAUZIN. I know.

Mr. POWERS. [continuing] not to draw surmises and conclusions, but certainly this is extremely suggestive as to why this happened. We understand that, and we tried to lay out the facts as best we could.

Chairman TAUZIN. And I alluded to it, and we are going to discuss it more on Thursday, but you, too, discovered, as we did, that in some cases, other than offering them a chance to invest, partnerships in some cases actually threatened employees with firings and losses of bonuses; is that correct?

Mr. WHITFIELD. The gentleman's time is expired.

Mr. POWERS. We did find pressure, yes. The exact nature of it I would have to go back and check, but we did find pressure.

Chairman TAUZIN. I think we got some of your answers. Thank you.

Mr. WHITFIELD. The gentleman from Michigan is recognized for 5 minutes.

Mr. DINGELL. Mr. Chairman, I thank you for your courtesy. I find at page 9 of your report this footnote which says this: "One member of the Special Investigative Committee, Mr. Herbert S. Winokur, Jr., was a member of the board of the directors and the Finance Committee during the relevant period. The portions of the report describing and evaluating the actions of its board and its committees are solely the views of the other two members of the committee, Dean William C. Powers, Jr., the University of Texas Law School, and Raymond S. Troubh." What does that mean, and why is that there, and what does it tell us?

Mr. POWERS. Well, when the committee was set up, in fact when it was originally set up, there were no new directors. I was brought in to Chair the committee and then Mr. Troubh was brought in to be on the committee. Other members were taken off the committee, and Mr. Winokur was left on the committee, so that there was a majority on the committee of outside, that is, new directors that didn't have any involvement in these transactions. We felt that Mr. Winokur was a very good source of information about the backgrounds of some of these transactions, and it was invaluable to have that information. When it came time to—

Mr. DINGELL. You could have gotten that from him under the cooperation you were promised from the company, could you not?

Mr. POWERS. Well, the interviews were for a period of time and couldn't go back, and there were lots of—especially early on, there was a great deal of information that we needed. When it came time to judging the board, we thought the report would speak more forcefully if Mr. Troubh and I made those judgments. That was a judgment we made as to how to best go forward with this investigation. And I think the report hopefully indicates we had an unvarnished position.

Mr. DINGELL. I don't criticize the report, but doesn't it indicate that Mr. Winokur was essentially participating in an investigation of himself?

Mr. POWERS. Well, it was an investigation of a number of things, and it did include himself. And when it came to judgments about the board Mr. Troubh and I had independent meetings of the committee with counsel and approved and decided what would go in the report about the board.

Mr. DINGELL. Thank you. Mr. Winokur told the board he was familiar with and recommended approval of a plan by Mr. Skilling and Mr. Fastow to sell 50 percent interest in JEDI, an affiliate of Enron and Chewco; isn't that correct?

Mr. POWERS. Yes.

Mr. DINGELL. The minutes record that Mr. Winokur states he was going to meet further with Mr. Fastow the next day, presumably on this matter since it was the only one on the agenda involving Mr. Fastow. Did that meeting occur?

Mr. POWERS. During his interview—we did interview Mr. Winokur; he didn't recall whether that meeting occurred.

Mr. DINGELL. Okay. According to the board's minutes, Mr. Fastow reviewed the economics of the project, the financing arrangements, the corporate structure of the acquiring company with the board. I presume this had previously been reviewed with the Finance Committee; is that correct?

Mr. POWERS. I believe so. Yes.

Mr. DINGELL. Now, Mr. Fastow told the board that Chewco was a special purpose vehicle not affiliated with the company or CalPERS, since the board was approving a bridge loan of \$383 million and a corporate guaranty of \$250 million loan to Chewco, an unknown entity. Did Mr. Winokur or any board member ask who controlled Chewco?

Mr. POWERS. I would have to go back to the particular—that was the Executive Committee, it wasn't the Finance Committee, and we don't know whether they asked those questions.

Mr. DINGELL. Was due diligence done by the Enron board officers or counsel?

Mr. POWERS. I don't know if I am in a position to say whether the diligence was due. That is a very complicated legal question, and—

Mr. DINGELL. It should have—

Mr. POWERS [continuing] we tried to lay out what happened.

Mr. DINGELL. Due diligence should have been done on this matter, should it not?

Mr. POWERS. Due diligence should be done on all corporate matters.

Mr. DINGELL. Now, Chewco understood that it did not have the necessary—in your report, you state Enron employees involved in Chewco understood that it did not have the necessary 3 percent in outside equity required to stay off Enron's books. If the employees understood that, did Mr. Winokur and the Finance Committee also understand it?

Mr. POWERS. I think that when Chewco was originally set up, it was widely understood that it did not have the 3 percent equity.

Mr. DINGELL. Did it ever get the 3 percent equity?

Mr. POWERS. Well, then the idea was that it would be reconstituted or restructured to get the 3 percent equity.

Mr. DINGELL. Did it ever get the 3 percent—

Mr. POWERS. And then they attempted to but did not because of the guarantees that were given to the loans, to Big River and Little River.

Mr. DINGELL. Did Mr. Winokur or any other member of the Finance Committee ever ask who was providing the outside equity?

Mr. POWERS. I don't know.

Mr. WHITFIELD. The gentleman's time is expired.

Mr. DINGELL. Mr. Chairman, I thank you. There are a lot of other fine questions here.

Chairman TAUZIN. Would the Chair—I ask unanimous consent that the gentleman have 30 seconds that could be yielded to me just to put a fact in the record.

Mr. DINGELL. I yield to my friend, if I get the time.

Chairman TAUZIN. I thank the Chair. I simply wanted to make sure I had in the record that in the South Hampton deal, the \$25,000 investment in March by the Fastow Family Foundation paid back \$4.5 million in May to that foundation.

Mr. POWERS. Yes, that is correct.

Chairman TAUZIN. Thank you, Mr. Chairman.

Mr. WHITFIELD. The gentleman from North Carolina is recognized for 5 minutes.

Mr. BURR. Thank you for your patience and your willingness to go through all this. You have helped us to sort out a lot of things.

Mr. POWERS. Thank you, Congressman.

Mr. BURR. I am going to try to clarify some things that we have already been over, so be patient with me. Did your committee interview Sherron Watkins?

Mr. POWERS. We asked to, but she wouldn't.

Mr. BURR. She declined.

Mr. POWERS. Right, she declined.

Mr. BURR. Do you or do the folks who are with you know the reason that she chose to decline?

Mr. POWERS. I don't know if she stated it. We communicated with her lawyer, and he said that she was going to be interviewed by a lot of other people and did not want to be interviewed by us, which I must say I don't fault her for.

Mr. BURR. To your knowledge, or the knowledge of your committee, was Sherron Watkins interviewed in any way, shape or form by V&E when they carried out their investigation?

Mr. POWERS. Yes.

Mr. BURR. And do we know the specifics of whether they agreed or disagreed with the claims that she had made in the letter to Mr. Lay?

Mr. POWERS. Well, they wrote a letter to Mr. Lay reporting on that.

Mr. BURR. Were you—

Mr. POWERS. I am sorry, to Jim Derrick, who was the chief financial officer—who was the general counsel.

Mr. BURR. Is it true that the lawyers for V&E were told not to review the underlying accounting for the partnerships or the very area that Ms. Watkins had raised questions about?

Mr. POWERS. That is what I understand from the letter. Again, I haven't looked into that carefully.

Mr. BURR. So what would a law firm hired to investigate ask Ms. Watkins if her claims were about the underlying accounting procedures and the lawyers were told not to investigate that? What could you possibly glean from it if you can't ask her about the accusations that she made, or at least you were instructed not to?

Mr. POWERS. Right.

Mr. BURR. Is that not your understanding, though, of what they were told?

Mr. POWERS. It is my understanding from what I have heard today. I did not focus on what Vincent and Elkins did.

Mr. BURR. Let me go back to the special-purpose entities, if I could, and I think you agreed with Chairman Tauzin earlier that there was no economic purpose for the creation of the SPEs in their structure that they eventually ended up, am I correct?

Mr. POWERS. Well, the deals made with the Raptors are where we say there was—the hedges, there was no economic purpose. SPEs are very common in business, and there are legitimate reasons to use SPEs.

Mr. BURR. And I realize that, and I think that it will become a very common word used in the next several months. But, specifically, the way these were designed, is it safe to say that the architect of these SPEs would have known it is not for economic purposes?

Mr. POWERS. Well, I would distinguish between Chewco and the Raptors.

Mr. BURR. Okay.

Mr. POWERS. When we found out what the Raptors were about, it is apparent to us and our conclusion is they weren't for economic purposes. And so somebody who is knowledgeable in accounting that designed them, I would say they would know that these were for accounting rather than economic purposes. Chewco I think is different.

Mr. BURR. In layman's terms, they were designed to hide debt, weren't they?

Mr. POWERS. Well, the Raptors were designed to offset losses and therefore show other earnings on the income statement and other than that didn't have an economic purpose.

Mr. BURR. Is it safe to say that anybody that participated in the architecture of these SPEs would have known what the intent was of creating them?

Mr. POWERS. I would think that the architect, the people that put together the Raptors understood why they were being put together.

Mr. BURR. Let me ask you if your committee looked at who participated in the compensation packages for Fastow and his involvement in the partnerships, Kopper or any other individual? I mean Fastow didn't create his own compensation package within the partnership, did he?

Mr. POWERS. I assume that was a negotiation with the limited partners in those partnerships, and we have not had access to those materials.

Mr. BURR. I think alluded, at least in some of the SPEs that the board signed off on it, the Board of Enron.

Mr. POWERS. Well, the board signed off on the creation, and we are told that the LJM compensation to Fastow was LJM business, and they didn't look into it.

Mr. BURR. And is that common practice for a board not to have interest or did the board not know of Enron's backdoor exposure?

Mr. POWERS. Well, I think there was interest on the board on Fastow's compensation. The thought was, the explanation was that it would be somehow inappropriate to pierce LJM, because they were supposed to be independent. We don't agree with that.

Mr. BURR. Did you have any—

Mr. WHITFIELD. The gentleman's time has expired.

Mr. BURR. If I could finish this question, Mr. Chairman. Were you aware of whether Skilling knew of the compensation package?

Mr. POWERS. He says he—well, we don't know.

Mr. BURR. Lay?

Mr. POWERS. He said he didn't know. Both knew that Fastow would be getting some return, but the magnitude of the compensation package Lay says to us he didn't know.

Mr. BURR. And the board would be a no.

Mr. POWERS. The board did not know. The board says they didn't know.

Mr. BURR. I would only say this, Mr. Chairman, in concluding: I find it unusual, and I hope you do, Dean Powers, that in this case the two CEOs and chairman of the board could have the structure of what was created here and, one, been ignorant of the structure and, two, been ignorant of the compensation package that went along with it, because, in essence, it was Enron's money. I thank you.

Mr. POWERS. Thank you.

Mr. WHITFIELD. The gentleman from Michigan is recognized for 5 minutes.

Mr. STUPAK. Thank you, Mr. Chairman, and, Mr. Powers, thanks again for being here and being patient with all of our questions.

Mr. POWERS. Thank you.

Mr. STUPAK. You said earlier in some testimony that Mr. Lay did not understand that hedging with Enron stock was not okay and that accountants told him it was okay, therefore he went along with the accountants; is that right?

Mr. POWERS. I said that is what he said to us.

Mr. STUPAK. Okay. That is what he said to you. Did he say who the accountants were who told him it was okay? Would that be Mr. Causey?

Mr. POWERS. Certainly Mr. Causey, and I think Andersen.

Mr. STUPAK. Andersen Consulting, or the Andersen the firm.

Mr. POWERS. Yes, Arthur Andersen. I believe that is what he said in his interview.

Mr. STUPAK. Okay. Michael Kopper, who is he at Enron?

Mr. POWERS. He was in the Finance group, and I don't know exactly what his job was. He was not senior management.

Mr. STUPAK. Wasn't he a former vice president involved in these partnerships like Chewco and a couple others?

Mr. POWERS. Well, he was involved—he did have an interest in Chewco, yes, absolutely.

Mr. STUPAK. Okay. And that is the deal that went from \$125,000 to, what, \$10 million? Mr. Kopper took \$125,000 investment into Chewco, and it went to \$10 million?

Mr. POWERS. Yes, that is correct.

Mr. STUPAK. How could that—I mean how is that conceivable? I mean how is that—is that even legal to—I mean the return on that is astronomical in a short period of time.

Mr. POWERS. That is an extremely abnormal rate of return.

Mr. STUPAK. How quickly did that turn around to \$10 million?

Mr. POWERS. A little more than 3 years.

Mr. STUPAK. Can you think of any legal way in which you could do that, take \$125,000 and turn it into \$10 million in 3 years at Enron, in the partnerships—

Mr. POWERS. Not without taking on a tremendous amount of risk, and we don't see that he did take on risk.

Mr. STUPAK. They took no risk, because it was all backed up by Enron stock, right?

Mr. POWERS. Well, I can't say that he took no risk. These are very complex transactions. There were ways in which the investors could lose money. There were options on Enron stock, but little risk.

Mr. STUPAK. If it is a possibility, did any investor in any of these partnerships lose any money?

Mr. POWERS. Not that I am aware of.

Mr. STUPAK. Okay. Mr. Kopper also received up to \$2 million in management fees relating to Chewco, and yet in your review, you were unable to identify, and I am going to quote now, "how these payments were determined or what, if anything, Mr. Kopper did to justify these payments."

Mr. POWERS. Yes.

Mr. STUPAK. How is it possible to have an employee make in excess of \$2 million and no one knows what he did to earn it?

Mr. POWERS. Well, these were investment funds, and they were simply managing these investments, and the work would have been relatively simple back office work, and it was never explained to us why that would justify a \$2 million fee.

Mr. STUPAK. This \$2 million, whose money would that be?

Mr. POWERS. That would be—

Mr. STUPAK. It is relating to Chewco and—

Mr. POWERS. It is very complicated. It would have been paid out of JEDI—

Mr. STUPAK. Okay.

Mr. POWERS. [continuing] which was another one of these entities, not related parties, so we didn't probe into JEDI. It was paid out of JEDI, but ultimately that is coming out of the interest of Enron. So when you track it all back, Enron is effectively paying.

Mr. STUPAK. So when we go through this simplified Whitewing leveraging transaction, all those pyramids and circles and boxes and squares and parts of South America and all over this country, that is really—when it is all said and done, that is really Enron's money.

Mr. POWERS. Well, there are some outside investors in these, this 3 percent rule, et cetera, but Enron has very substantial interests in these entities.

Mr. STUPAK. And Enron is really the employees' 401(k) plan, their pension plan and the shareholders who invested in Enron. They are really the ones who really are left here—after we get done with all these nice pyramids and everything else, they are the guys who are left holding the empty promises.

Mr. POWERS. The employees and the shareholders and the people with their retirement nest eggs and the 401(k) plans are tragic and terrible victims of this.

Mr. STUPAK. So whether Kopper made \$10 million over 3 years or \$2 million for consulting on Chewco, it was those investors—the bottom line, it was really their money that got—

Mr. POWERS. They were the ones that got hurt.

Mr. WHITFIELD. The gentleman's time has expired. The gentleman from Florida is recognized for 5 minutes.

Mr. STEARNS. Thank you, Mr. Chairman. Dean Powers, you and I talked a little bit about Mr. Winokur and his responsibilities, as he is a board member. Now, I would like you to go to Rick Causey who was, I understand, the chief accounting officer, an officer of Enron himself, and then Rick Buy who, as I understand, his title was chief risk officer.

Mr. POWERS. Yes.

Mr. STEARNS. So now we are moving into the corporate officers, the people who worked, the employees of Enron, and I just want to go into a little bit about what their responsibilities were, and did you interview both these individuals?

Mr. POWERS. I didn't personally, but the committee, yes, it did interview those individuals.

Mr. STEARNS. And were they forthright with you?

Mr. POWERS. They certainly answered our questions.

Mr. STEARNS. Causey and Buy stated they participated in the LJM transaction reviews in a limited capacity.

Mr. POWERS. Yes, that is what they said.

Mr. STEARNS. And they said this is, I guess, that we on the committee are having a little trouble understanding. Buy stated that the Global Finance Group made the strategic decisions regarding the deals, and that his risk review had nothing to do with the big picture. Causey stated that his review of the transaction was to make sure that the accounting treatment was accurate, and he did

not participate in the strategic decisions. So we have an idea what they feel. What do you think they did?

Mr. POWERS. I think they had very limited review of the transactions between Enron and LJM2, and that they were charged with the responsibility of having much more robust and substantial review.

Mr. STEARNS. So who charged them with this responsibility? Did the board of directors?

Mr. POWERS. The board, yes.

Mr. STEARNS. The board of directors, in your opinion, charged them with the responsibility to have a thorough understanding of these LJM transactions.

Mr. POWERS. And ensure that there were transactions that would be for the benefit of Enron.

Mr. STEARNS. Why didn't these two officers who were employees of the corporation and had the great title of chief accounting officer and chief risk officer, I mean I would think if you or I had those titles of risk and accounting, that we would not think, well, we are not really here to make sure these agreements are accurate. We don't participate in strategic decisions. If you are going to be in charge of risk, you have got to understand what the strategic decisions. So where do you think—am I missing something or as a dean do you think we are missing something? The board thought they had the responsibility and yet they are telling you they didn't have that responsibility or authority.

Mr. POWERS. Right. In my view, they didn't fulfill their responsibilities with respect to review of these transactions.

Mr. STEARNS. And why do you think that was?

Mr. POWERS. We don't know that for certain. I think they were unwilling to stand up to Andy Fastow.

Mr. STEARNS. And what about—do you think—you think that is it, that Fastow intimidated them that much; is that it?

Mr. POWERS. I don't know Fastow. I have talked to people around the company. He was a very aggressive person and was in charge. I don't know this to be the case. The most plausible explanation to me—we don't have any evidence that Causey or Buy participated. Something may come out later, but we didn't find any evidence of that.

Mr. STEARNS. Dean Powers, in all deference to you, it sounds like you are suspending disbelief here. I mean either they were intimidated by him or they are complicit in the operation.

Mr. POWERS. Well, I think they certainly understood how LJM wanted to and how the Raptors were working; certainly, Causey did. So complicit in that sense I agree with. We didn't find any events of financial participation, which does not mean that—

Mr. STEARNS. No, I understand.

Mr. POWERS. [continuing] we will come out. I think they were intimidated by Fastow.

Mr. STEARNS. That is what you think.

Mr. POWERS. Partly.

Mr. STEARNS. I am just curious why they didn't mention the problem, the accounting problem or the risk problem to the Audit and Compliance Committee and the Finance Committee.

Mr. POWERS. Because doing so would have brought down scrutiny on these deals that Fastow was participating in, and for whatever reason they didn't do that.

Mr. STEARNS. The board of directors was similarly not informed on March 2001 that Raptor deficit grew to approximately \$500 million or that it would require a charge against Enron's earnings in that quarter if not addressed prior to March 31, 2001. The board of directors was not informed that the Raptors SPEs were restructured on March 26, 2001 to avoid the anticipated charge to earnings. And the board was not informed about the transfer of approximately \$800 million of Enron stock contracts that was part of the restructuring. Causey and Buy were aware of the deficit and restructuring. Why did they fail to mention them to the board? And you are saying they were totally intimidated. That is what you are conjecturing.

Mr. POWERS. They wanted to—I think at that point, at the point that you are describing with the restructuring, I think now they would have a motivation—I don't know what happened—of not having come out all the structures that had been there before.

Mr. STEARNS. Dean Powers, my last question.

Mr. POWERS. Yes.

Mr. STEARNS. Did you ever ask him the same questions I am asking you? Why didn't they refer—based upon all this restructuring and all this loss and this \$800 million of Enron stock contracts as part of the restructuring, did your group ever say to Mr. Causey and Mr. Buy, "Hey, fellas, why didn't you tell the board of directors?"

Mr. POWERS. We did ask them that question—

Mr. STEARNS. And what was his answer?

Mr. POWERS. [continuing] and his answer, what he said was by the time of the next board meeting, they had fixed the problem; in fact, they had and it kept going on. But by the time of the next board meeting, they thought they fixed it, so they didn't mention it. I do not think—

Mr. STEARNS. Who said they fixed the problem?

Mr. WHITFIELD. The gentleman's time has expired.

Mr. STEARNS. Okay. Thank you.

Mr. WHITFIELD. The gentlelady from Colorado is recognized for 5 minutes.

Ms. DEGETTE. Thank you, Mr. Chairman. Mr. Powers, I assume you are familiar with the corporate governance guidelines of the Board of Directors of Enron, are you?

Mr. POWERS. Yes.

Ms. DEGETTE. I was just looking over these a little while ago. Dr. Jaedicke, as I understand, is the chairman of the Audit and Compliance Committee, or was during the relevant time; is that right?

Mr. POWERS. Yes, and I believe still is.

Ms. DEGETTE. Okay. And what these guidelines say is the Audit and Compliance Committee serves as the overseer of Enron's financial reporting process, system of internal controls and corporate compliance process, and it provides reasonable assurance that Enron conducts its business in conformance with appropriate legal and regulatory standards and requirements. Do you think that the Audit and Compliance Committee met those standards?

Mr. POWERS. If I could just preface it, that the committees of the board are entitled to rely on statements by management, unless they have reason to believe those statements by management are unreliable.

Ms. DEGETTE. Well, yes, I understand, but—

Mr. POWERS. So whether they met that obligation I don't know. I don't think the board generally looked hard enough into these very complicated transactions, knowing of these conflicts of interest.

Ms. DEGETTE. Well, and case in point, annually the Audit and Compliance Committee was given a deal approval sheet by which they were supposed to look at the related party transactions, right?

Mr. POWERS. Yes.

Ms. DEGETTE. And that is the sheet we were talking about before where everybody signed it but Skilling, right?

Mr. POWERS. No.

Ms. DEGETTE. No?

Mr. POWERS. There is an approval of LJM—

Ms. DEGETTE. Right.

Mr. POWERS. [continuing] which Skilling was supposed to approve—was at the board, he did approve it, he just didn't sign off on the sheet.

Ms. DEGETTE. Right, but he didn't sign it.

Mr. POWERS. Then there are the—once LJM was set up, there are the individual hedging deals between Enron.

Ms. DEGETTE. Okay. Right, right. You are right, you are right. But did the Audit Committee review those?

Mr. POWERS. They had a meeting where Causey said, "Here are the transactions," and they didn't do anything more than that.

Ms. DEGETTE. They didn't do anything more than that.

Mr. POWERS. Correct.

Ms. DEGETTE. That would seem to me, if I were one of the small investors who had all my 401(k) invested in this Enron stock, I would think that that would not provide me with reasonable assurance that these deals were being conducted in conformance with appropriate legal and regulatory standards and requirements. I don't know.

Mr. Winokur was the chairman of the Finance Committee, which under the guidelines reviews and makes recommendations to the board and management on matters concerning both current and long-range financial strategy and planning, including, without limitation, budgets, dividends, equity offerings, debt and other financing, foreign exchange policy, investment policy and trading limits policy, correct?

Mr. POWERS. Yes, that is correct.

Ms. DEGETTE. Now, in reviewing everything you have reviewed, do you think the Finance Committee fulfilled its obligation?

Mr. POWERS. Not knowing the details of the standards of securities law, I don't know the answer from a legal point of view.

Ms. DEGETTE. Yes, but Mr. Powers, you know what happened here with these financial—

Mr. POWERS. I don't think they oversaw these transactions sufficiently.

Ms. DEGETTE. Thank you. Now, do you have any idea what were the limits of the directors and liabilities insurance that the Enron Board had? That might be of interest to many of the board members.

Mr. POWERS. I think I do, but I would like to check.

Ms. DEGETTE. Thank you.

Mr. POWERS. I am not absolutely sure. My understanding is it is \$350 million.

Ms. DEGETTE. Thank you. Now, quickly, I just want to talk about the South Hampton deal, because we had mentioned that before. And in your report, you talked about Ms. Mordaunt who is the lawyer—in-house lawyer for Enron, Kathy Lynn, who is an employee in the finance area, and Ann Yaeger Patel, who is also an employee at Enron Global Finance. You said that they appeared to have violated Enron's code of conduct by accepting interest in the South Hampton Place deal without the consent of Enron's chairman and CEO, correct?

Mr. POWERS. That is correct.

Ms. DEGETTE. Can you talk for a minute about what the South Hampton deal was, briefly?

Mr. POWERS. When the Rhythms net was unwound, there was a partnership formed to take the distributions from that transaction, and this was a partnership formed to take in some of the distributions from that unwind.

Ms. DEGETTE. Now—

Mr. WHITFIELD. The gentlelady's time has expired.

Chairman TAUZIN. Mr. Chairman, could I ask unanimous consent the gentlelady have 2 additional minutes? I think she is on a good trail here.

Mr. WHITFIELD. Without objection, the gentlelady has 2 additional minutes.

Ms. DEGETTE. Thank you very much, and thanks to the chairman of the full committee. Didn't some of these employees also work for LJM and get bonuses from that partnership?

Mr. POWERS. I believe so, yes.

Ms. DEGETTE. And that is the partnership you just said a few minutes ago in which Mr. Fastow, in exchange for \$25,000, got \$4.5 million for his Family Foundation, right?

Mr. POWERS. That was the South Hampton partnership, yes.

Ms. DEGETTE. Right, that is the one we are talking about right here.

Mr. POWERS. Yes, exactly.

Ms. DEGETTE. Now, on page 16 of your report, you also say that two other employees who each invested \$5,800 in the South Hampton deal each received a million dollars in the same time period, correct?

Mr. POWERS. Yes.

Ms. DEGETTE. Who were those two employees, and how did they get those returns, if you have any idea?

Mr. POWERS. That was Yaeger—I am sorry, Glisan and Mordaunt.

Ms. DEGETTE. Okay.

Mr. POWERS. Glisan and Mordaunt.

Ms. DEGETTE. Now, Mordaunt is a lawyer who worked on some of these deals for Enron, correct?

Mr. POWERS. Yes.

Ms. DEGETTE. And now when she talked to committee staff, it is my understanding that she never asked Mr. Kopper what the investment was, because it was such a small amount of money. Then 1 day Mr. Kopper said, "Where do we wire the money," and then low and behold it was a million dollars. She didn't ask questions then either. Now, as an attorney for Enron, Mr. Powers, don't you think that Ms. Mordaunt had an ethical responsibility to know where the money was coming from and if it conflicted with her client's interests?

Mr. POWERS. Yes.

Ms. DEGETTE. Thank you. No further questions.

Chairman TAUZIN. But would the gentlelady—

Ms. DEGETTE. Oh, happy to yield.

Chairman TAUZIN. Before that, the gentlelady yield. Didn't Ann Yaeger, later Ann Yaeger Patel, contribute \$2,900 and take about \$500,000 back?

Mr. POWERS. Yes, that is my understanding.

Chairman TAUZIN. And didn't Kathy Lynn, another Enron employee, contribute \$2,330 and take back about \$500,000 as well?

Mr. POWERS. Yes.

Chairman TAUZIN. And they were in the same position as these two employees that the gentlelady just discussed; is that right?

Mr. POWERS. They weren't lawyers.

Chairman TAUZIN. They weren't lawyers, but they were employees of Enron—

Mr. POWERS. Absolutely.

Chairman TAUZIN. [continuing] in violation of the code of ethics, investing in a partner to whom Enron was dealing and taking out an extraordinary rate of return. Did you ask them if they ever questioned why they got so much money back?

Mr. POWERS. Yes. They declined to be interviewed.

Chairman TAUZIN. Who do they work for?

Mr. POWERS. They work for Enron.

Chairman TAUZIN. But for whom at Enron?

Mr. POWERS. They work for LJM now.

Chairman TAUZIN. Now, but who did they work for at the time?

Mr. POWERS. They worked for Enron in the Finance Group.

Chairman TAUZIN. In the Finance Department.

Mr. POWERS. Yes.

Chairman TAUZIN. And who was their immediate supervisor?

Mr. POWERS. I don't know who their immediate supervisor was. Fastow was—

Chairman TAUZIN. I am thinking it was Michael Kopper; is that correct?

Mr. POWERS. It may be, but I don't—

Chairman TAUZIN. I would like you to supplement that answer, if you can determine it, for the record.

Mr. POWERS. Okay.

Chairman TAUZIN. Thank the gentlelady.

Mr. WHITFIELD. The gentleman's time has expired.

Ms. DEGETTE. Reclaiming my time.

Mr. DINGELL. Could I ask unanimous consent the gentlelady have 1 additional minute?

Mr. WHITFIELD. Is the gentleman asking that the chairman have an additional minute or the lady from Colorado?

Mr. DINGELL. The gentlewoman from Colorado.

Mr. WHITFIELD. Without objection, the gentlelady from California is recognized for 1 additional minute.

Ms. DEGETTE. Colorado, please.

Mr. WHITFIELD. I mean Colorado. What did I say?

Ms. DEGETTE. I yield to my friend from Michigan.

Mr. DINGELL. And I thank my dear friend. I have a curiosity. How many of these people have cooperated with you and been fully—of those mentioned, and have been fully forthcoming in terms of all of the events and the production of records?

Mr. POWERS. Of these people we are talking about? Mordaunt did talk with us, and I think Mordaunt, even before she talked with us, did go to talk to the general counsel of the company.

Mr. DINGELL. How about the others?

Mr. POWERS. The others have not cooperated with us.

Mr. DINGELL. Would you name then those who have not cooperated?

Mr. POWERS. I think Glisan, Yaeger, Patel—

Ms. DEGETTE. Lynn?

Mr. POWERS. Yes, Lynn and of course Kopper has not either.

Mr. DINGELL. And I gather that Andersen has not permitted the committee to review all its working papers too; is that right?

Mr. POWERS. Well, yes. Andersen—we had long negotiations with Andersen. We have seen some of their papers, we haven't seen other papers. We never got to interview them. When Enron finally discharged them, they then said, "We are not"—we had been discussing interviewing their employees and then they finally said no.

Mr. DINGELL. Did Andersen tell you why they are not cooperating with you?

Mr. POWERS. Well, they told us they weren't cooperating with us because Enron discharged them. That was what they said.

Mr. DINGELL. Do they not have a continuing fiduciary duty to their former client to discuss matters which went on between Andersen and Enron?

Mr. POWERS. To be honest, after discharge, whether they do or not, I don't know the answer to that question.

Mr. DINGELL. What does your logic tell you?

Mr. POWERS. I think they ought to cooperate fully with getting to the bottom of this. Legally, whether their fiduciary ends, I just don't know the answer to that.

Mr. WHITFIELD. The gentleman's time has expired.

Mr. DINGELL. And I thank the gentlewoman; I thank the Chair.

Mr. WHITFIELD. The Chair will now grant himself 5 minutes. Dean Powers, this relates to the Chewco transaction, and I think Mr. Greenwood touched on this, but on the issue of trying to meet the reserve account for the Barclay's Bank, in your report, you stated that others told us that those matters involving the \$6 million side agreement and reserve accounts were known openly and discussed. Could you tell me who those others were, the names of those others?

Mr. POWERS. I am not sure we know, other than people said that it was being discussed. Of the people that told us, Shirley Hudler is one person.

Mr. WHITFIELD. Shirley Hudler?

Mr. POWERS. Yes. I think there may have been other people that have told us that I don't recall now.

Mr. WHITFIELD. Okay.

Mr. POWERS. There were also notes from meetings where this issue was discussed to some extent, and I don't know now whether there is an indication of who was at those meetings or if there was, who they were.

Mr. WHITFIELD. We would ask that you supply those notes. Can you do that?

Mr. POWERS. The same thing. It is not my property to dispose of, but we will certainly address that to Enron.

Mr. WHITFIELD. Okay. You will talk to Enron.

Mr. POWERS. And we will support that request.

Mr. WHITFIELD. Okay. Now, let me ask you this: Do you think that the transfer by Mr. Kopper of his ownership interest in Chewco's limited partner to his domestic partner, William Dodson, resolved the accounting and disclosure issues, as Enron, Andersen and Vincent & Elkins apparently all did?

Mr. POWERS. I am not sure we know whether he was his domestic partner at the time, which would be relevant to this. Kopper and Dodson didn't talk with us. If it was his domestic partner at the time, that certainly raises an issue of whether Kopper still had control.

Chairman TAUZIN. Would the chairman yield?

Mr. WHITFIELD. Yes.

Chairman TAUZIN. My understanding is our investigators have determined that they were. I believe that they were.

Mr. POWERS. Yes. I am not saying they weren't. That was a fact that we were unable to track down.

Chairman TAUZIN. Thank you.

Mr. WHITFIELD. Did you find any evidence that despite this transfer of ownership interest that Mr. Dodson actually exercised any control over the limited partners or exercised control?

Mr. POWERS. I don't think we know what Mr. Dodson did.

Mr. WHITFIELD. So you don't have any evidence on that. Now, on page 61 of your report, you discussed the buyout of Chewco by Enron, in which Enron paid Chewco Kopper \$10 million. Did you find any evidence of improper influence by Fastow or others on Kopper's behalf in that transaction?

Mr. POWERS. Yes. Fastow is the one that negotiated with Kopper on this deal.

Mr. WHITFIELD. So he was negotiating with the person that reported to him at Enron?

Mr. POWERS. Yes.

Mr. WHITFIELD. Okay. And what did Mr. McMahon tell you about his involvement in this transaction and the conversations he had with others about it, including Mr. Fastow?

Mr. POWERS. I believe he knew about these negotiations and had complained that \$10 million was too much.

Mr. WHITFIELD. Did he indicate what he would consider to be the appropriate price?

Mr. POWERS. My recollection is about a million dollars, but—

Mr. WHITFIELD. A million dollars.

Mr. POWERS. About a million dollars.

Mr. WHITFIELD. So he was aware of that then, okay. You have already indicated that your conversations with Fastow were quite short, and that is correct, right?

Mr. POWERS. It took about an hour, but there is very little information.

Mr. WHITFIELD. Did he tell you about his involvement in this deal at all? Did he talk about his involvement in that transaction?

Mr. POWERS. He gave—sorry.

Mr. WHITFIELD. On page 61, footnote 17, it indicates that, “Fastow told us that he had not participated in these negotiations.”

Mr. POWERS. Right. And then we had a document that demonstrated that wasn’t true, and at that point he stopped talking to us, or meaningfully talking to us.

Mr. WHITFIELD. And what was that document?

Mr. POWERS. It was a document that demonstrated he had participated in these negotiations.

Mr. WHITFIELD. And you have that document.

Mr. POWERS. Yes.

Mr. WHITFIELD. Okay. And we would also like to have that, and if you would talk to Enron about that and—

Mr. POWERS. Okay.

Mr. WHITFIELD. [continuing] support us in our efforts.

Mr. POWERS. And I will say we will support providing whatever information and backup of this information the committee needs.

Mr. WHITFIELD. And we appreciate that very much. The Special Committee’s report states how facetious earnings from the Raptors accounted for more than 80 percent of Enron’s earnings from the last two quarters of the year 2000. Even if no one knew about the problems lurking with the Raptors at that time, wouldn’t the very fact that 80 percent of earnings are coming from transactions with a partnership headed by Enron’s CFO have been enough to send off alarms in the investor and analyst communities?

Mr. POWERS. Yes. I think it was a little over 70 percent, but, yes, I would think that would be something that would have set off concerns in the investor community.

Mr. WHITFIELD. Okay. And what was Enron’s Board of Directors’ understanding regarding the Enron/LJM2 services agreement?

Mr. POWERS. The board members that we talked to said they understood—well, some said they didn’t know about that. Those who did said they assumed it was a very minor services agreement for back office booking of transactions, and that it was not significant.

Mr. WHITFIELD. And did the members of the board of directors understand that Enron’s own employees were negotiating on behalf of LJM2 against Enron?

Mr. POWERS. Yes. They understood that Fastow was representing LJM1 and LJM2.

Mr. WHITFIELD. Any others, other than Fastow, that they understood?

Mr. POWERS. They say that they didn't know that other Enron employees were then over on the services agreement working for Fastow and negotiating on the basis of LJM.

Mr. WHITFIELD. But the entire board was aware of Fastow's involvement.

Mr. POWERS. Yes, yes.

Mr. WHITFIELD. Okay. All right. That is the end of my questions. I recognize the gentleman from Illinois for 5 minutes.

Mr. RUSH. Thank you, Mr. Chairman. Mr. Powers, I want to get back to this question of bona fide economic objectives. And in your estimation, how common is it for corporations to misuse SPEs merely to accomplish favorable financial results and not achieve bona fide economic objectives or risks—or transferring risk? And is this abuse specific to certain industries? And I also would like for you just to give us some examples of what you would call a bona fide economic objective or transfer of risk.

Mr. POWERS. Okay. In answer to the first part of your question, I don't know how widely used, how they are used by other companies, and I hope and I am quite sure other companies are looking into how they are using.

I think there are two different kinds of transactions here. One is a hedging transaction, and there is nothing inappropriate about a hedging transaction to take risk from a company. We all do it, in a sense, when we buy insurance, as long as you are really buying insurance, rather than just setting up something to look like a hedging transaction that isn't accomplishing that purpose. That is the first issue.

The second are these SPEs to, as we say, put debt off the books, and I would just give two examples. If I buy 100 shares of Ford Motor Company, I risk the value of my equity but not all the balance sheet of the Ford Motor Company when I consolidate it into my financial statements, and that seems appropriate. If I own almost—you know, if I own all of the Ford Motor Company, maybe it should be different. When I lease equipment rather than buy equipment, one of the considerations I may take into account is I don't want to have the debt on the equipment on my balance sheet. So these are extremely difficult policy questions for the accounting industry, for Congress, for the Securities and Exchange Commission to sort out how these ought to be used. But I do think it would be unfair to come away with the Enron experience thinking that all hedges or all special-purpose vehicles are inappropriate. They are not; they are often and I desperately hope by most people in the country used in appropriate ways.

Mr. RUSH. With that in mind, I know you are not a securities expert—you have testified about that on more than one occasion this afternoon—but do you have an opinion or opinions in terms of how we, as Members of Congress, can avoid the abuses of SPEs that were perpetuated by Enron without doing away with what you have clearly defined as the more legitimate purposes and benefits of SPEs?

Mr. POWERS. Well, I look at it, from a non-securities expert, as a fairly simply issue: There ought to be transparency. To the extent that the problem here is that the existing laws might have been enforced, then enforcement. To the extent that the existing laws

aren't requiring enough transparency, then maybe the existing laws need to be changed. But transparency is absolutely crucial, and that was one of the problems here.

Mr. RUSH. I want to try to get quickly back to the question of Mr. Richard Buy here, who is the Enron senior risk officer. In staff interviews with Mr. Buy, he suggested, similar to the findings of your report, that his group was not charged with the responsibility of evaluating Enron's big picture risk as it related to all of these activities in total. What then is the role of someone who is the risk management officer, the risk manager, is it just to look at a risk change here or a risk change there or a willy nilly look at this or do they have to be more focused and more concerted in their efforts?

Mr. POWERS. As I indicated at the outset of my testimony, Enron isn't just a pipeline and energy trading company; it has a very significant investment portfolio. And a primary, if not only, job of the risk assessment group was to evaluate the risks of those investments, diversification, what doing due diligence on the investments and things like that. I am not an expert on this, but as an investment manager, that was one of the roles.

Mr. RUSH. Mr. Chairman, one additional question here. According to your report, the board of directors also charged Mr. Buy with a substantial role in the oversight of Enron's relationship with the LJM partnerships, and he was supposed to review and sign off every deal. Why then was Mr. Buy not in a position to see the multitude of problems and conflicts facing these partnerships and Enron? Do you any thoughts on that?

Mr. POWERS. Well, I think he was in a position to see that these were not arms-length deals.

Mr. RUSH. So you say he was in a position.

Mr. POWERS. He might not have been in a position to see the complexities of the underlying transactions, but he was in a position to monitor the arms-length nature of many of these deals.

Mr. RUSH. Thank you, Mr. Chairman. I yield back.

Mr. WHITFIELD. The gentleman's time has expired. The gentleman from Texas is recognized for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman. First, Mr. Powers, I appreciate you spending all this time with the subcommittee this afternoon. I may be the last questioner, but let me ask you some questions about Arthur Andersen accounting firm. In your report, it stated that, "Evidence available to us," and I am quoting, "suggests that Andersen did not fulfill its professional responsibilities in connection with its audits and Enron's financial statements or its obligations to bring to the attention of Enron's Board concerns about Enron's internal controls." What specifically should Andersen have been doing that it was not doing?

Mr. POWERS. Well, we have, throughout the morning and afternoon, talked about many, many things in the accounting, including the overall structure of hedging with one's own stock that were, we think inappropriate, but at a minimum very questionable. And in their audit should have brought those to the attention of the Audit Committee.

Mr. GREEN. Since Arthur Andersen earned \$5.7 million in consulting fees to set up the LJM deals, how could they not have known about the outside equity was bogus?

Mr. POWERS. Well, they may have known that, but the source of the money to back the Big River and Little River loans was from Barclay's, and the only reason it wasn't equity was it was backed with a reserve account that came from a distribution from JEDI in a very complicated way, and I must say, it is not possible, even in a thorough audit, to see every little movement of money. Again, I am not an accountant who goes through these audits. I would not be surprised by that claim that we didn't know that. I don't know whether it is true or not. And I don't think—in the report, we have not stated otherwise. We don't know whether Andersen was aware that the Big River and Little River loans in Chewco were backed by reserve accounts, which made them not equity but debt.

Mr. GREEN. You also mentioned that Andersen participated in the structuring and accounting treatment of the Raptor transactions and charged again over a million dollars for its services, yet it apparently failed to provide the oversight to prevent those transactions from going forward. Was Andersen purely—and I hate to say this about such a great company I thought of so many years, their partnership—was it purely incompetent in its duties or simply taking advantage of a company that appears to be out of control? In other words, was Andersen there as a whistleblower or to earn fees?

Mr. POWERS. Well, I don't know why Andersen did not recognize these issues. What we do say is that as the Raptors, for example, were being developed, Andersen was providing accounting services of some sort, whether we call them consulting, or real-time accounting. They were providing real-time accounting as those were being developed, and they did not bring to the attention of the board—they did not bring independent judgment to bear on those transactions. If they did, they didn't do it adequately.

Mr. GREEN. I guess it is frustrating being from Houston and seeing the tragedy and the devastation from Enron and the collapse, and I guess—and I have read lots of articles—I guess Enron could be the Michael Milken in a tall, shiny skyscraper in downtown Houston. And it is just such a shock to watching a company over 15 or 16 years grow and be so successful and aggressive but aggressive to the point where they created these multiple partnerships. It is just astonishing, I guess.

Mr. POWERS. Well, Congressman, being not too far up the road from Houston and being in Houston quite a bit—

Mr. GREEN. Hundred and sixty-two miles; I have driven it lots of times.

Mr. POWERS. [continuing] this is a terrible tragedy for Houston and our part of the country. Yes, there is a lot of technical material we have talked about today, but I think you are absolutely right to bring that point that this is a great human tragedy for many individuals.

Mr. WHITFIELD. The gentleman's time has expired.

Mr. GREEN. Thank you, Mr. Chairman.

Mr. WHITFIELD. I understand the chairman of the entire committee seeks recognition?

Chairman TAUZIN. I seek recognition with the consent of the members to do something on behalf of our investigation, collectively, and ask the gentleman a few more questions, if you don't mind. Would the gentleman yield?

Mr. WHITFIELD. Without objection.

Chairman TAUZIN. On behalf of our investigation, Dean Powers, has the alleged shredding of documents at Enron impeded the investigation of your committee in any way?

Mr. POWERS. I don't think so. We haven't seen some hole that, "Where is that?" Having said that—and we haven't had the opportunity to go through a lot of documents. We haven't been able to download a lot of e-mail. So there is a great deal of material.

Chairman TAUZIN. Do you admit going in that you had limited access to documents?

Mr. POWERS. Correct.

Chairman TAUZIN. Are you aware of why shredding is occurring at Enron as late as January and what is being shredded? Why did they hire a company called Shredco to come in and do all this shredding?

Mr. POWERS. I don't know. I can't answer that.

Chairman TAUZIN. Well, you have not asked that question in the purview of your investigation? Didn't it disturb you that all this shredding is going on while you are trying to do this investigation for the board?

Mr. POWERS. Well, I mean I read about it in the paper, and we did ask, are there areas of documents that we are not getting, are there transactions that we can't understand? And we came to the conclusion that we were trying to move ahead expeditiously, that there were not gaps in our—

Chairman TAUZIN. Did you ask the question, why is all this shredding going on?

Mr. POWERS. We did talk to the FBI about that and cooperated with the FBI and—

Chairman TAUZIN. This is going on while the FBI is there in Houston?

Mr. POWERS. No, no. They came in after the—

Chairman TAUZIN. After the shredding?

Mr. POWERS. [continuing] after the shredding had started.

Chairman TAUZIN. Just to put in this perspective, my understanding from the investigators, Mr. Dingell, is that the web site of the shredding company, Shredco, opens up with a statement, "You think you got rid of it, now you are being sued. Call us, we guarantee destruction." And Enron would hire a company with that as their invite to come in and shred documents in the middle of all this. Doesn't that disturb you?

Mr. POWERS. Well, I agree these allegations of shredding are extremely serious allegations that the FBI ought to look into.

Chairman TAUZIN. And to put this in perspective, because you had limited access to documents anyhow, you can't know whether documents were being shredded that may have aided and assisted you in understanding the intricacies and the involvement of parties in these affairs.

Mr. POWERS. Right. We can't know whether some of those documents would have helped us or whether even if they had not been shredded we would have gotten them.

Chairman TAUZIN. Thank you, Mr. Chairman.

Mr. WHITFIELD. Dean, I know you will be disappointed, but that probably concludes the hearing. And on behalf of the committee, I want to thank you so much for being here today and testifying. Your report of the Special Investigative Committee has been particularly helpful to us as we continue our efforts to get to the bottom of this and to determine what we can do from preventing this in the future. So thank you very much for joining us.

Mr. POWERS. Thank you.

[Whereupon, at 2:45 p.m., the subcommittee was adjourned.]