

Road Map for Real Enron Investigation: Give Up Faked 'Recovery' Myth

by John Hoefle

The recent revelations about how Enron and its fellow energy pirates manipulated the electricity market in California, combined with the disclosure of fraudulent bookkeeping and phony trades, confirm in spades this publication's contention that the energy pirates were engaged in criminal behavior, and that the business was never viable. With each passing week, more dirty deals are revealed, which show that not only were the companies crooks, but that the regulators who were supposed to oversee them were at best doing nothing, and sometimes implicitly aiding the very activity they were supposed to be stopping.

Most of the energy pirate companies, like the telecom companies, reported as revenues their gross sales, rather than their net revenues from those sales. That is, they would buy a block of energy for \$100,000 and sell it for \$125,000, and book the entire \$125,000 as revenue, instead of the net \$25,000. Throw in the "round-trip" trading in which these companies would sell a block of energy to another trader, then immediately buy that energy back at the same price, and you have the makings of a real revenue machine. Such shenanigans made Enron No. 5 five on the Fortune 500 for 2001, followed by American Electric Power at 13, Duke Energy at 14, El Paso at 17, Reliant Energy at 26, and Dynegy at 30.

Where were the regulators? Where was the much-hyped "industry self-regulation"?

The telecommunications companies were running a similar scam by leasing capacity on their networks to each other to artificially inflate revenue.

These tricks, along with hiding debt and losses in off-balance-sheet entities, booking the entire amount of multi-year sales income in the first year, overstating the values of assets held, have led to serious over-statements of corporate profits in recent years. Despite record numbers of corporate profit restatements in the last couple of years, only the tip of the iceberg has been revealed.

No Real Profits, Then or Now

Even so, with all the tricks, the reported level of corporate profits is declining in the United States. U.S. corporations reported \$767 billion in net profits in 2001, down from \$876 billion in 2000. Heaven only knows what it would be, were honest numbers reported.

Many useful details are pouring out of the various Con-

gressional and regulatory investigations into the Enron affair, showing a level of corruption which is shocking to many Americans, but at the same time, a cover-up is in place, which hides the true authorship of the institutions and policies which created and organized the piracy.

The way the cover-up works, is that the investigations are directed at so-called rogue elements within the companies, rather than examining the larger network of which these companies are a part. In the case of Enron, the focus has been put on just a handful of nearly 3,000 off-balance-sheet entities and affiliates run by a small group of company executives. From the day the Enron scandal broke last October, the financial press, led by daily stories in the *Wall Street Journal*, focussed public attention on a handful of entities with names like LJM2, Raptor, and Chewco. Then the Enron board hired two new directors and put them on a special committee with a long-time member of the board, to launch an investigation of these same entities. This special committee produced a report, which was then used as the basis for several Congressional investigations. Throughout the entire process, investigatory and public attention has largely remained riveted on the same handful of entities with virtually no investigation of the remaining group.

Such a method of investigation is virtually guaranteed to fail to find the networks which really pulled the crime. The real perpetrators get away, while a few scapegoats get nailed.

Southern Strategy, Inc.

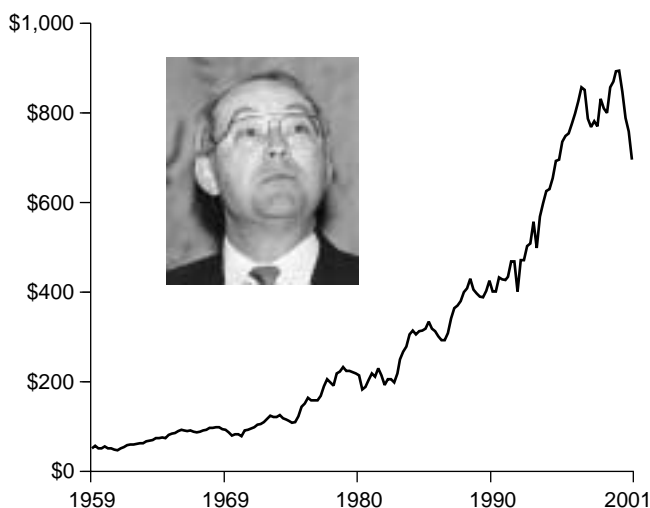
Enron did not operate in a vacuum; it was not a rogue operation run by a few greedy insiders, but rather part of a network of energy firms, banks, law firms, accountants, and consultants, which created and ran the energy pirate phenomenon with support from a corrupt Congress which systematically stripped regulatory barriers to the piracy and provided political protection in exchange for hefty campaign contributions and other perquisites.

Despite its overblown reputation for market and political power, Enron did not have the clout to put the pirate operation in place. What power Enron wielded, originated elsewhere, on Wall Street and in the City of London, where bankrupt financial institutions were desperately trying to cover their own losses by stealing from the pockets of consumers of electricity. These are the institutions which created the deregulation movement, sold it to the American people, then stole them blind. They pulled the strings which made Enron jump.

EIR has identified the network which created and deployed Enron and its fellow pirates as "Southern Strategy, Inc.," a nexus of financiers and corporations operating through the Confederate oligarchic ideology of the Nashville Agrarians of Harvard's William Yandell Elliott. Chief among the organizers of this corporate group is the Schlumberger/Lazard intelligence operation, though its base in Houston. Under the cover of a global oil-field service company, Schlumberger is host to one of the oldest and most powerful oligarchic intelligence networks in the world, while the La-

U.S. Corporate Profits, 1959-2001 (3Q)

(\$ billions)



Source: Federal Reserve.

This graph shows clearly, that taking official government figures which reflect all the sham accounting tricks and inflated earnings for the "New Economy boom" is now infamous, U.S. corporate profits still have been falling since 1997. Imagine what honest earnings reports would have shown! Republican Sen. Phil Gramm (inset) is leading efforts to block any changes in corrupt accounting rules, to protect the "recovery" fraud.

zard investment bank has played a crucial role in shaping the U.S. financial bubble. Together, Schlumberger and Lazard, with help from the Morgan and Rothschild networks, created and control the swamp which produced Enron.

A few investigative leads help make the point.

Earlier in May, Dynegy, the Houston-based energy pirate, came under investigation by the Securities and Exchange Commission (SEC) for making a pair of "round-trip" trades, in which the company simultaneously sold and repurchased at the same price, huge blocks of electricity. The two trades accounted for one-third of Dynegy's trading for the fourth quarter of 2001, and involved 20,000 megawatts of electricity—enough power, according to Bloomberg news service, "to dwarf the Hoover Dam's annual output and light the city of Houston for a year." Dynegy's partner in the trades was CMS Energy, of Dearborn, Michigan.

A week later, Reliant Resources—the energy-pirate arm of Houston's Reliant Energy—revealed that it, too, had engaged in round-trip trades, many with CMS Energy.

What are these firms? Reliant Energy, which grew out of what was once known as Houston Lighting & Power, is a firm that until recently had the elder Bush's Administration's Secretary of State, James A. Baker, on its board (after he left Washington, Baker was a consultant for Enron, using his political connections to land business for the firm). Members

of Baker's family law firm, Baker & Botts, have not only held positions on the board of Schlumberger, but Baker & Botts represented Dynegy in its aborted attempt to buy Enron. CMS Energy, whose main unit is Consumers Energy Company, is also tight with Schlumberger; CMS chairman William T. McCormick, Jr. is on the board of Schlumberger, as is another CMS director, former CIA chief John Deutch. Dynegy was founded by Morgan Stanley and the Akin Gump law firm, and is now controlled by ChevronTexaco.

CMS admitted that its round-trip trading accounted for 72% of its electricity-trading volume in 2001, and 78% in 2000. The firm said that round-trip trading boosted its revenue by \$4.4 billion over those two years. Furthermore, 98% of its round-trip volume came from 13 deals, two with Dynegy valued at about \$1.7 billion, and the rest with Reliant, valued at \$2.7 billion.

The Federal Energy Regulatory Commission (FERC), which sat on its hands while the pirates looted California, has belatedly launched an investigation into round-tripping and other manipulations of the energy market, so more horror stories are expected.

Derivatives Dealing

Enron was also well connected to the world's largest derivatives banks through the International Swaps and Derivatives Association (ISDA), the trade group for the over-the-counter (OTC) derivatives market. Mark Haedicke, managing director and general counsel of Enron Capital & Trade Resources, was on the board of the ISDA in the late 1990s, and moderated a panel on energy, weather, and bandwidth trading at the ISDA's annual meeting in Washington, D.C. in April 2001. At the same meeting, Enron director Wendy Gramm, wife of Sen. Phil Gramm (R-Tex.), gave a presentation on public policy issues in the derivatives markets, and Enron President Jeffrey Skilling gave a keynote speech on building the global market for derivatives.

As a director of the ISDA, Haedicke rubbed elbows with the cream of the derivatives crop, including representatives of J.P. Morgan, Chase Manhattan, Citigroup, and Merrill Lynch, all of which played roles in the Enron scam.

In April 1997, testifying on behalf of the ISDA before the House Agriculture Committee's Subcommittee on Risk Management, Haedicke was one of a slew of speakers who complained that the derivatives market was oppressively over-regulated. In particular, Haedicke complained of "legal uncertainties that continue to exist" in the off-exchange OTC market, because the law "flatly prohibits off-exchange futures contracts."

"If certain swaps transactions were ever classified as 'futures contracts,' " Haedicke said, "they would be illegal and unenforceable as a matter of law." That, he declared with the characteristic Enron arrogance, "is obviously unacceptable in the global marketplace," and Congress must change the law.

It took a while, but Senator Gramm gave Enron what it wanted, with the Commodity Futures Modernization Act of

2000, which legalized the regulatory loophole his wife had opened in 1993 as chairman of the Commodity Futures Trading Commission.

Haedicke's name turned up in Congress again on May 15, in a hearing of the Senate Commerce Committee's Consumer Affairs subcommittee on Enron's role in the manipulation of the energy markets in California. Among the subjects of the hearing was a memo written by Stephen Hall of the Portland law firm Stoel Rives and former Enron attorney Christian Yoder, which detailed some of Enron's market-manipulation strategies (e.g., "Get Shorty," "Death Star," and "Fat Boy"). Yoder testified that in early December 2000, he gave a copy of the report to his immediate boss at Enron North America, Mark Haedicke, the very man who complained to Congress about over-regulation.

The Harvard Cover-Up

Members of the special committee that the Enron board created to investigate reports of corruption within the company had (at least) one thing in common: They were all graduates of Harvard. Herbert "Pug" Winokur, a director of Enron since 1985, is chairman and chief executive of Capricorn Holdings of Greenwich, Connecticut, and is also a director of the Harvard Corp., the university's seven-member executive governing board. Joining Winokur were former Lazard banker Raymond Troubh and William Powers, dean of the University of Texas Law School. Powers, the junior man of the group, noted that he had to recuse himself from discussions in any area involving Vinson & Elkins, given the firm's tight relationship to his law school.

The Powers report, as the committee's report was called, put the focus squarely on the same group of entities targetted by the *Wall Street Journal*.

Winokur, as chairman of the Enron board's finance committee, was one of several board members who testified at a hearing by the Senate Governmental Affairs investigative subcommittee on May 7. Winokur absolved himself of all responsibility for the Enron fiasco, claiming that he did not know what the company was doing. "We cannot, I submit, be criticized for failing to address or remedy problems that were concealed from us," Winokur claimed.

Also testifying was Enron's longest-serving director, John H. Duncan, chairman of the executive committee since 1986. Duncan and his brother, former Energy Secretary Charles W. Duncan, were closely allied to the late Dominique Schlumberger de Menil, the notorious cultural warfare specialist and Schlumberger heiress, whose husband Jean de Menil was involved in the assassination of John F. Kennedy.

While it is clear that Enron executives violated the law and should be punished, the idea that they acted alone, or that they took advantage of the Wall Street sharks, defies credibility. This article provides a road map for a serious investigation of the "Enron affair," should Congress develop the wisdom and the guts to abandon their blowhard posturing and go after the real perpetrators of this crime.