TESTIMONY OF CALIFORNIA STATE SENATOR JOSEPH DUNN
BEFORE THE COMMERCE, SCIENCE & TRANSPORTATION COMMITTEE
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Good morning, Chairman Hollings, Ranking Member McCain, Senator Boxer and members of the Committee on Commerce, Science and Transportation. Thank you for the opportunity to present testimony to the Committee on Enron's role in influencing the structure and function of California's deregulated energy market and its role in the energy crisis.

Since last March I have chaired the California State Senate Select Committee to Investigate Price Manipulation of the Wholesale Energy Market. The Committee is conducting an extensive investigation into all aspects of the California energy crisis. We have held numerous hearings, taken countless depositions, conducted various interviews and meetings with experts and interested parties and reviewed millions of documents throughout the United States.

Our Committee has had protracted and at times, acrimonious, dealings with Enron. I hope my experience in dealing with Enron and my intimacy with the California energy crisis will provide insight into decisions your Committee and Congress must address.

I preface my testimony with the admonition that my Committee has documents to prove the claims made herein. Because of confidentiality agreements reached with market participants, however, I am limited in my ability to share many of these documents without a formal request by you or your Congressional investigators. I encourage you, Senators, to make a formal request if you wish to view these documents.

My comments today speak to the pivotal role Enron played in influencing the design of California's deregulated wholesale market, its behavior as a market participant as the market grew more and more dysfunctional in 2000 and 2001 and the part Enron's conduct played in the huge price spikes California experienced.

Let me begin by saying that there has never been a "power shortage" in the state of California. The state has always had a sufficient supply of electricity to meet its need. That some have said the state experienced periods where demand outstripped supply is one of the many myths of the energy crisis. What California experienced in 2000 and 2001 was not a crisis in electricity, it was a crisis in economics. Enron and its team of economists knew this better than most.

ENRON'S EARLY FORAY INTO CALIFORNIA

Enron was involved in the California electricity market well before the inception of the deregulated market. In fact, Enron was the most pivotal (future) market participant in shaping the regulatory and political environment that gave birth to the commoditization of electricity.

Enron testified before and submitted comments to the California Public Utilities Commission (CPUC) more than a dozen times before 1996, the year legislation was passed that authorized "deregulation." This is a critical point – *Enron's sophisticated lobbying efforts helped create the very market it would later exploit*. To be clear: I do not believe there is anything wrong with lobbying public officials on behalf of one's business interests. Done properly, it is good business and a democratic right. However, Enron's lobbying consisted of hyperbolic promises that its internal predictions do not appear to support.[1]

For example, former Enron CEO Jeff Skilling, then the President of Enron Capital & Trade, told the CPUC on June 14, 1994, that California would save billions in a few short years under a deregulated market.

> In this industry in California, the potential savings are enormous…More specifically, in California, our view is that California is an industry run amok. If California consumers were paying even the same costs as surrounding states' consumers are paying, the state would save about $8.9 billion per year. If you had $8.9 billion that you wanted to spend, let me tell you what you can buy every year. You can triple the number of police in Los Angeles, San Francisco, Oakland and San Diego, and you could double the number of teachers in Los Angeles, San Francisco, Oakland and San Diego. You could pay all the interest on the California state debt. You could pay full interest in debt service for all three bond issues that failed last year [1993] and you'd have enough pin-money left over to cover the CPUC's budget. And you'd have another billion dollars a year left over.

With California facing a more-than $15 billion budget deficit this year, the hollowness of this prediction is not wasted on anyone in my state.

Beyond what some might label insignificant grandstanding, Enron lobbied for very specific market rules that stood to benefit its business at the expense of consumers. Two months after giving that testimony, and again in October 1994, Mr. Skilling appeared before the CPUC to argue for the superiority of an "OpCo" electricity market versus a "PoolCo" market that was modeled on similar markets in other countries, including the United Kingdom.

OpCo and PoolCo refer to competing approaches of market management. In each model, the respective guardians of each approach – a Power Exchange for the PoolCo method and a Power Marketer for the OpCo method – promise an optimization of market efficiency. Efficiency is achieved by the PoolCo method through a transparent "pool" system in which buyers and their "bids" are pooled

[1] To the extent that Enron knowingly published any false statement to affect the wholesale electricity market is worthy of further investigation, as it is a violation of California law (Penal Code § 395).

and sellers and their "asks" are pooled. The two pools are then overlaid, and buyers and sellers are matched. The ultimate price is posted, and participants in the "auction" use this pricing information to make "efficiency decisions" on their own, such as the when and where of committing their generation units.

The OpCo method championed by power marketers relies on a different underlying assumption: i.e., "competitive markets need help in performing efficiently."[2] The "value-add" of a marketer lies primarily in its risk management, founded on superior understanding of market fundamentals, including price, bidding and demand history. Enron argued that the resulting efficiency wrought by power marketers, in the end, benefits consumers.

Many economists have noted that this premise is faulty. "Generators wish for a high price paid to generators, and consumers want to see low prices paid by loads, but power marketers want the opposite of both. They want to buy low (from generators) and sell high (to consumers). Power marketers are a new breed and they have different objectives….they are mistakenly viewed as market makers….Currently power marketers often find themselves in the position of trading wholesale power while adding very little value. In this case their principle opportunity for profit exists at being a better speculator in the market."[3] Speculating for profit is not what California consumers needed to ensure an efficient delivery of energy.

In arguing for the OpCo approach, Mr. Skilling referred to Enron-generated forward price curves.[4] Enron confidently predicted that the benefit of a liquid futures market for electricity would bring stability, efficiency and competition – but only in an OpCo-modeled market. A PoolCo method would lead to volatile and unpredictable prices, which was bad for the consumer, he told the CPUC. Ironically, Enron would later create volatility for profit.

But in the early days of deregulation, Enron's apparent losses were always mitigated by subtle gains: California instituted a modified-PoolCo approach by creating the California Power Exchange (CalPX) and the California Independent System Operator (CAISO), but made key concessions to Enron in the process. For example, the CalPX was required to follow a strict set of protocols in its auction procedure that no power marketer was similarly saddled with. The result in every instance was to make Enron and other power marketers more nimble, more flexible to buyers and sellers in ways the CalPX could not be.[5]

[2] Steven Stoft's April 29, 1997 study, "What Should a Power Marketer Want?" I ask whether this is an unintentional concession that a deregulated model does not work.
[3] Stoft.
[4] Despite a subpoena compelling their production and specific conversations about this data, our Committee has never received copies of these price curves or the staff work that gave rise to them. Mr. Skilling has also refused to testify before the Committee to address this and other issues.
[5] In fact, consider the decision to separate ISO and PX as an example of the concession. One of the most important advantages of a PoolCo system is the historic database available to the PoolCo of pool prices and demand, information that is not available to any single power marketer. In creating a separate ISO to manage this information,

Needless to say, economists characterize OpCo and PoolCo as incompatible and to this end, the two models are seen as competitors.[6] As early as 1997, a number of economists, including Steven Stoft, correctly predicted that these concessions would give Enron and other power marketers the tools to bankrupt the CalPX.[7]

Given this, it is not surprising that the success of the CalPX seemed to be inversely correlated with the success of Enron, and, not coincidentally, the success of the CalPX was directly correlated with low wholesale electricity prices. When the CalPX teetered on the edge of solvency, Enron thrived and wholesale prices skyrocketed.

On May 13, 1998, the California Senate Committee on Energy, Utilities and Communications issued a statement that demonstrated this relationship. The committee credited the CalPX with "buying electricity at substantially lower prices than expected." Shortly before the release, Enron announced that it "suspended" its involvement in the California residential service market, though it did not publicly acknowledge the relationship between the success of the CalPX and its own failure.

ENRON AND THE DEREGULATED MARKET

The state's deregulated market opened on March 31, 1998. Enron's misconduct in the day-ahead market was first discovered in May 1999. Through the CalPX day-ahead auction, Enron successfully purchased the right to sell 2900 megawatts over a 16-hour time period. The company then proceeded to schedule all 2900 megawatts over a line with a 15-megawatt capacity. Enron unabashedly admitted that the company intentionally congested the line.[8]

Despite claims from Enron CEO Ken Lay that Enron "believes in conducting business affairs in accordance with the highest ethical standards,"[9] the company maintained internally that the intentional congesting of the power line was a "test" and was "not a big deal."[10] The CalPX maintained that the "test" resulted in a $6 million detrimental impact on the market. Amazingly, Enron was fined just

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the CalPX was stripped of an inherent advantage. "If equal treatment includes taking away PoolCo's ability to make use of its advantage, then the experiment has been rigged," Stoft wrote.

[6] Enron later explicitly acknowledged this during an investigation of misconduct by the CalPX. "We are mystified that our competitor, the CalPX, believes that it has the authority to be judge and jury…Enron and the CalPX are direct competitors." Ironically, the Committee heard testimony from a CalPX executive who denied that Enron was viewed as a competitor.

[7] Stoft predicted the CalPX's demise "less than a year after the requirement is lifted on January 1, 2003 that the three major IOUs must trade through the CalPX." The FERC effectively moved the January 2003 date forward with its December 15, 2000 order. (The order spelled out in detail the FERC's elimination of the mandatory buy-sell requirement into the CalPX.) The CalPX ceased trading six weeks later on January 31, 2001.

[8] Undated internal Enron memorandum, "Main Messages."

[9] November 23, 1999 letter to the CalPX.

[10] Internal memo provided to the Committee.

$25,000 for the incident.

The CalPX was not the only regulator to cite Enron for market misconduct. In 2001, CAISO released a study about market behavior between May and November 2000. The report asserted that Enron Energy Services strategically bid into the market with the intent of manipulating the price of electricity. The company's "economic withholding" of megawatts resulted in excessive profits of nearly $28 million in ISO's real-time market.[11] The cost of this behavior among all the companies implicated in the report was over $1 billion.

CAISO asserted that Enron was able to charge "excessive rents" because it was able to exercise market power, an anti-competitive behavior in which a single company can determine a price the market is compelled to accept. I maintain, as I have since the beginning of the crisis, that market power is at the heart of California's dysfunctional market. The astronomical prices of 2000 and 2001 have been blamed on many things, and I agree that a confluence of factors contributed to the crisis. However, California spent billions of dollars on electricity because a cadre of companies led by Enron were, in industry parlance, "price makers."[12]

MARKET POWER AND THE ROLE OF TRADING

How did Enron acquire and exercise market power? As I mentioned earlier in my testimony, this is a question of economics and is not easily sorted out. I believe that Enron's fiscal improprieties, still the subject of numerous federal probes, drove Enron's strategy and behavior in the California electricity market. Thus, it is impossible to dissect Enron's manipulation of the California market without understanding its aggressive culture and potentially fraudulent accounting practices.

There are three important prongs to Enron's business in California as: 1) a direct access provider to large commercial and industrial entities, such as the University of California; 2) a trader and marketer of electricity; and 3) an unregulated auctioneer in the electricity and, more importantly, the natural gas market.

I have already discussed the relationship between Enron and the CalPX, but I will add another distinction between the two: the role of volatility.

In theory, Enron would not necessarily need volatility in the market to succeed as a trader of electricity. Bond traders, for example, make money trading and speculating in a very stable, liquid commodity. In fact, Enron VP Steve Kean told our State Senate Energy Committee in January 2001 that Enron "sell[s] protection from price volatility to both producers and end users. Consequently our interest in

[11] Dr. Anjali Sheffrin, Ph.D., "Empirical Evidence of Strategic Bidding in California Real Time Market," March 21, 2001.
[12] In a functional market, participants serve as "price takers," indicating that the price is dictated by what the market will bear. In a dysfunctional market, participants act as "price makers," indicating that they have the ability to set the market price above a competitive level. This is a common test for market power by economists.

California's power market is to ensure that the market works effectively…Enron has no interest in high power prices."[13]

This simply is not true. Enron was like a glass-repair business that advertises on bricks thrown through windows: "Buy protection from the volatility we create!" In practice, Enron *did* require high prices, because high prices were a symptom of a volatile market. Not only did Enron need high prices, it worked to ensure them, in order to do two things: 1) SELL "protection from volatility" and 2) undermine the CalPX, in order to establish itself as the primary market maker.

Let me state this another way. In a regulated electricity industry, protection from the impacts of unexpected price movement is the responsibility of regulators. Since Enron sold volatility management products, anything that increased volatility was good because it created a demand for Enron's products. Thus, during the height of the energy crisis when California was requesting that the Federal Energy Regulatory Commission (FERC) impose price caps, Enron and its sister traders opposed them because price caps would staunch volatility and undermine the trading operation, which provided 90 percent of Enron's revenues.[14]

The success and stability of the transparent CalPX market worked against Enron. Market participants did not need to buy or sell "protection" from Enron when the CalPX was already operating efficiently enough to mitigate volatility. Enter the traders.

Enron argued to the CPUC that in an OpCo model, power marketers would make the market more efficient. This was supposed to be because "risk management" trading companies like Enron were better able to interpret market fundamentals than other market participants. Generators, for example, would pay a premium for Enron's expert analysis of the market instead of relying on their own interpretation of the neutral information in a transparent pool. Once the CalPX was operating, however, the point was moot. The CalPX handled the vast majority of the trades, so no matter how brilliant Enron's interpretations were, they were based on a small percentage of the overall transactions done in the market.

This created a dilemma. How could Enron, as an individual company, compile a larger database of price, bidding and demand history than the CalPX? The simple answer was to book more trades. Since the price of energy in each bilateral contract was a proprietary secret, the more Enron traded, the

[13] Jeff Skilling echoed this view at various points in time. Skilling told *Business Week* that, Enron benefits from volatility, not high prices (Feb 12, 2001). And Enron's 2001 Q3 earnings release points to a direct relationship between "a low level of volatility" and "flat" profitability. Generators also benefit from volatility. Duke, Dynegy and Williams executives have all acknowledged the correlation between company profits and market volatility.

[14] Thus, the FERC and California's combined Spring 2001 efforts to reduce Western price volatility had a significant negative impact on Enron's 3rd quarter 2001 financial results, confirming the claim by Anderson's CEO that Enron's demise was at its heart a business failure. This paragraph (including footnote) is taken directly from a February 6, 2002 letter from California State Senator Steve Peace to Rep. Henry Waxman.

greater its market share became, and the more its traders became the resident experts about the future price of electricity.

The dimension of trading is critical in understanding market manipulation because markets are manipulated by influencing traders' expectations about the future. Those expectations establish the forward price curves, which in turn affect the cost of long-term electricity contracts. Since the future is uncertain, an electricity user trying to minimize costs must decide whether to buy a long-term contract or commit itself to costs that might be higher in the spot market.

Traders themselves have a preference for long-term contracts because "mark-to-market" accounting rules benefit a company in the near term, an issue I will discuss later. Enron attempted to transfer the long-term contract trading approach it developed in natural gas to marketing electricity. In natural gas, Enron had already developed innovative long-term contracts, modeled on financial hedge contracts, that allowed customers to purchase "insurance" against future price and quantity risks, a.k.a. "risk management." The cost of this "insurance" was based upon traders' perception of the risk that the future could be different.

Its ability to sell the concept of risk management was limited by the success of the CalPX market. So Enron had to beat the CalPX price, which was published daily. This is the reason why contracts such as those signed with the University of California called for a discount to the CalPX price. In order to profit from such deals, Enron had to be able to purchase electricity at an even greater discount to the CalPX price. This meant finding suppliers willing to sell to Enron power for less than they could receive selling it to the CalPX. Since this was virtually impossible, Enron's California operations as a direct access provider were a big money loser as long as the Power Exchange was in business. That was all the motivation Enron needed to find ways to discredit the CalPX and the market it operated.

Enron's desire to undermine the CalPX meshed with a well-documented pressure from management to show profits on its books. Enron traders found that the way to do both was to extend the "liquidity" of the futures market in California.[15] It took to trading "bundled energy" as far out as 2020, a market so far in the future that many wondered how it was possible to predict the price of electricity that far in advance – especially because the more established natural gas market was liquid only to about five years.

In order to make it work, Enron did two things. One, it leveraged its intellectual capital and marketing expertise to sell itself (and specifically, its traders) as the "experts" on the long-term future price of electricity. This was no small feat, since the future price was uncertain – economist Robert McCullough

[15] Liquidity in markets means the degree of ease and certainty of value with which a security can be converted into cash. Liquid markets are heavily traded, meaning it is easy to find a buyer or seller for your position. Imagine you have a desire to sell energy tomorrow. There would be many buyers willing to offer you money to buy that energy. Tomorrow is a liquid market. Now imagine you want to find a buyer for energy you want to sell in 30 years. There are fewer interested buyers, if any, making the market for such a transaction illiquid.

called such predictions "highly subjective." Two, it booked thousands of trades. The company developed a reputation for buying and selling everything it could, with price justifications based exclusively on Enron's mysterious, omniscient price curves, each used to justify thousands of trades.

We now know the folly of many of these trades, which propped up Enron's gross misstatements of earnings. Enron traders would sell "bundled energy," multi-year agreements for the future delivery of power, booking *uncollected* future revenues as *collected* revenues in the current quarter. This process, called "mark-to-market accounting," has been labeled "an incentive to abuse" by recognized economist Robert McCullough.

In 2000, however, Enron's accounting practices had not yet been exposed. The company may have been losing money on these trades – the traders called it "selling negatives" – but the market only recognized at that time that Enron was a willing and active trader of electricity. If you wanted to buy it or sell it, Enron was there. We know from the Daily Position Reports, which Enron provided our Committee, that as the summer of 2000 approached, Enron's traders had taken increasingly "long" positions in the market, meaning they had a growing amount of electricity to sell.

Diminishing reserve margins expected for 2000 caused some consultants to encourage such long positions. One consultant was unequivocal: "Go long with every dollar you have in the West."[16] As Enron acquired control of more and more energy through trades, it gained a commensurate amount of control of the market. By May 2000, Enron already controlled enough of the market to withhold power until the "last minute," i.e., the spot market.

By offering to sell its electricity only at unacceptable, high prices in the CalPX day-ahead market, Enron effectively forced buyers (primarily the investor-owned utilities) to take a pass on the CalPX market and seek a better deal at a later time. The better deal never came. As real-time approached, Enron's leverage increased, and in real-time, it was CAISO buying power – without regard to price.

We heard testimony from CAISO executives who acknowledged that the directive of the CAISO did not include a consideration of price. The CAISO Board in 2000 disagreed. It repeatedly voted to ratchet down the price cap on electricity in order to mitigate the exercise of market power by Enron and other market participants. The board's final vote on the subject, in October 2000, prompted Ken Lay himself to write to the FERC imploring a reversal of the board's edict. The FERC ruled to overturn the board the following day.

By December 2000, Enron's goals clicked off like a falling row of dominoes. Enron got the tacit buy-in of complicit generators, the counter-parties involved in Enron's money-losing, long-term trades. None of them blanched at the notion of a liquid electricity market because they were getting sweetheart deals; the energy bundled in those deals that was to be delivered in 2000 helped establish Enron's market power,

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[16] ICF Consulting offered this advice in July 1999.

which in turn allowed Enron to force the market out of the now-irrelevant CalPX, which in turn raised the price of electricity, which in turn created volatility, which in turn created the very condition from which Enron said all along it was in the market to protect buyers and sellers.

Enron's culture of aggressiveness permeated the company no matter if there were sound business fundamentals underlying the endeavor or not. Its electricity plan was waiting to be replicated in other markets as well. "The Opportunity," one memo reads, is that "there is a lack of liquidity" in the credit risk market. "Our response: We offer to transact on more companies than anyone else by a significant margin."

Enron took pride in the aggressiveness that helped drive it to bankruptcy. I do not think it is a stretch to argue that this same aggressiveness dictated its behavior in the California market to the detriment of California.

NATURAL GAS AND ENRON ONLINE

My Committee has heard repeatedly from generators and other market participants, as well as regulators and market managers such as CAISO, that the price of natural gas was largely responsible for the run-up in electricity prices in Fall and Winter 2000. The crisis reached its nadir, they testified, in early December 2000 when natural gas prices at the California border were running five times higher than prices at Henry Hub. Henry Hub usually provides the country's most accurate baseline for natural gas prices in the spot market.

During the course of our investigation, I have been appalled at the lack of skepticism employed by those regulators and market managers in simply accepting this relationship as gospel truth. Why was the price of natural gas so high? Could expensive natural gas justify expensive electricity so completely? Was there a certainty that generators "passing on" the cost of natural gas into the wholesale price of electricity were *actually* paying the spot market price? Had generators failed to hedge natural gas by entering into long-term contracts for gas?

These questions were answered in December 2000 when the price of electricity and the price of natural gas stopped tracking each other. With price caps lifted by CAISO request and the FERC order, electricity prices continued to rise. Meanwhile, the natural gas market stabilized and ultimately prices returned to historic norms. I ask you to consider whether it is unrealistic to consider the possibility that gas prices were artificially high in order to "justify" a regulatory decision to remove electricity price caps. Evidence suggests this possibility.

First you must understand the regulatory environment Enron negotiated in order to operate as it did in the natural gas market. Enron was the benefactor of a momentous regulatory ruling in its favor by the Commodity Futures Trading Commission (CFTC). I will not delve into the details of the political processes and money trail implicated in these rulings except to say that the cozy relationship between

CFTC commissioners and Enron provides, at a minimum, the appearance of impropriety.

The import of the legislation and CFTC ruling must be acknowledged. The first, in 1992, exempted Enron's trading of futures contracts in response to a request for such an action by Enron that same year. The second, an amendment to a Senate banking bill in December 2000, allowed Enron to operate an unregulated power auction – EnronOnline – that gained market share in the natural gas market almost overnight.[17]

Internal documents provided to the Committee by Enron indicate a colossal reversal of traditional market share over the span of just five quarters. In Q4 1999, Enron was responsible for trading roughly 23% of the natural gas and power transactions in North America. One year later, in Q4 2000, EnronOnline claimed to have a 74% market share, easily outpacing the "traditional" market. Competitors independently claim that Enron was involved in somewhere between 50-75% of the trades in the natural gas market.[18]

The reason this is so important is because of Enron's admitted role as a speculator/trader in this market. Imagine if you will if the New York Stock Exchange were a for-profit company that operated the NYSE as an unregulated exchange. Every bid, every ask, every market trend, every individual stock trade, would be viewed by the omniscient company responsible for making the market. If the NYSE was trying to generate revenue, it would be logical to use this information to speculate on market trends.

This is precisely what Enron was allowed to do, and what it used EnronOnline to accomplish. EnronOnline was the de facto exchange and Enron was the market maker. Enron's traders logically used the "inside information" available to them from facilitating these trades to speculate on natural gas futures.

Thus, when El Paso Natural Gas (El Paso) "went long" on gas in 2000, Enron spotted the movement in the market and mirrored the move. Staggering shifts – a veritable sea change – from short to long positions are found in Enron's own books. Enron clearly had the motivation to ensure demand for natural gas, though we do not know the extent to which the company was able to restrict pipeline capacity or delivery. Was Enron merely profiting on speculation or was it aiding and abetting physical withholding?

El Paso is under investigation for this very thing. When natural gas capacity is purchased, the process is regulated. But when unused or unneeded capacity is returned, the capacity can then be sold to unregulated subsidiaries of the same company that can use the capacity as they wish. The subsidiary distinction is a paper distinction only. The subsidiary is housed in the same building, on the same floor

[17] Public Citizen, "Blind Faith: How Deregulation and Enron's Influence Over Government Looted Billions from Americans," December 2001.
[18] Interviews conducted with an Enron competitor also revealed that Enron was on the opposite sides of many trades.

and the employees "play on the same softball team," as one witness describes the relationship. The question for investigators is, given the motivation of a long position, did these unregulated subsidiaries have the ability to restrict capacity? And did they do that in Fall 2000?

The natural gas market is a pivotal piece to understanding price manipulation in the California market, and I believe the deregulated gas market is itself in dire need of oversight and investigation into past abuse. Alleged misconduct has been the subject of investigation by the FERC, but no investigation has provided an adequate description of Enron's ability to speculate on gas prices and to buy back unused capacity as an unregulated entity.

POLITICAL SOPHISTICATION

It is impossible to deny that Enron had a keen grasp of the political and regulatory environments necessary to carry out this plan. As the first state to deregulate, California was the laboratory for Enron's plan to trade energy in a destabilized energy market, a model they wanted to replicate in more states across the country.

An Enron memo from October 1996 indicates the obvious import: "The California market is the largest in the nation and California is the sixth largest country [sic] in the world. If Enron doesn't do well in California, Enron will have a difficult time convincing anyone outside California that they are capable of and committed to providing power services."

To accomplish this, the company had a comprehensive and well-executed strategy to gain political influence when and where it was necessary to: a) create new markets; and b) be left alone in those new markets. A memo from Ken Lay and Jeffrey Skilling in October 1998 codified what was already a standing practice in the company: "Our activism in the political and regulatory process is essential to our continued success…."

Media reports and campaign finance disclosures have revealed the close relationship between President Bush, members of Congress and Enron. The company lobbied successfully at the highest levels for regulatory change that would further its strategy. For example, Enron was responsible more than any other company for the provisions of the 1992 Energy Policy Act that altered the historic structure of the nation's electricity industry. Enron was also responsible for sweeping deregulation approved by the Commodity Futures Trading Commission (CTFC) that paved the way for Enron to trade electricity futures.

Enron was even part of the very commissions responsible for oversight. For example, Enron was a sitting member of the CAISO board in November 1999, when the board decided to set CAISO's damage control price cap at $750. When the price cap was lowered during a series of votes in Spring and Summer 2000, Enron lobbied to have the cap remain at $750. That a $750 cap provides a much larger window for volatile pricing than the $250 cap ultimately adopted during its board tenure was not wasted on Enron.

Enron executives had unprecedented access to high-ranking public officials at both the federal and state levels. We know from our document review of Enron's government affairs department how much the company relied on political relationships. On the one hand, California's legislative leaders appealed directly to Enron for contributions and on the other received explicit instruction about specific legislation. It remains to be seen how close Enron executives were to the California Legislature, but documents seem to suggest the two were very close.

ENRON UNCOOPERATIVE WITH STATE INVESTIGATION

My Committee's experience with Enron has been contentious, at best. Enron has engaged in delay tactics, arrogant displays of defiance and unabashed non-compliance. Enron has defied the state's authority to investigate and has continued to stand in the way of lawful investigations of its business, including a probe by the California attorney general.

When our investigation was launched last April, we asked Enron to produce voluntarily several categories of documents. It refused. We then requested that Enron enter into a non-destruct agreement with the Committee to ensure that documents critical to the investigation were preserved. Enron again refused.

This issue has been a prominent problem for my Committee since well before Enron and Arthur Andersen were ever implicated in reports of document destruction. In a typical display of Enron's hubris, the company's counsel represented "as an officer of the court" that my Committee had entered into a non-destruct agreement with Enron. This is patently false. The claim, made before a San Diego judge during a civil proceeding against the company, was intended to deter a court-ordered imposition of a non-destruct agreement.

When the Committee served Enron with a document subpoena in June 2001, Enron told the Committee it still would not hand over documents. Enron sued the Committee, arguing that my committee "had no authority to investigate" Enron and its role in the energy crisis. The company relented only when threatened with a contempt finding and a substantial financial sanction by the California State Senate.

Enron has openly defied the Committee in numerous ways. Enron has failed to produce documents pursuant to our June 2001 subpoena and did not produce a company representative pursuant to a January 2002 deposition subpoena. Nor has Enron explained its role in the destruction of documents by Arthur Andersen or by its own employees as reported in the media.

Even in bankruptcy, Enron has managed to stand in the way of our investigation. Multiple visits to Enron's Houston headquarters resulted in inadequate document production and inappropriate assertions of privilege.

The most troubling behavior, however, has been Enron's deliberate destruction and/or concealment of documents. The Committee has not been provided documents it has compelled since June 2001. Coupled with reports that Enron documents have been destroyed, I believe Enron has committed criminal obstruction of justice.

This belief has been affirmed by our latest review of electronic documents provided to my Committee in the last week. Our technical consultant confirmed this week that emails, schedules, correspondence and other electronic documents have been overwritten in order to destroy evidence we presume is relevant to our investigation. We can only assume the destroyed documents demonstrate at best information unhelpful to Enron's case and at worst, criminal activity. In either case, Enron should be subject to criminal prosecution if this is true.

In light of the many reports of shady accounting practices exposed in the last few months, Enron's conduct over the last year should come as no surprise. From my perspective, however, Enron's recently exposed shady accounting practices come as no surprise in light of Enron's conduct over the last year.

CONCLUSION

Electricity deregulation has engendered heated debate since the first seeds were sown for an end to utility monopolies in the 1980s. I cannot recommend a complete reversal of the deregulation concept at this time. However, the current model is untenable.

Electricity is a unique commodity. It cannot be stored, demand is inelastic and the barriers to entry are sizable. There has been no worthwhile oversight of the industry by the federal agency charged with policing its bad actors. "This" deregulation, borne of Enron, adopted by regulators and foisted on the public, has proven to be the greatest fraud ever perpetrated on the American consumer. The public interest is not being served. Until there are fundamental changes in the present approach, I believe we are simply biding time for the next Enron to emerge.