

Ethical Conflicts at Enron:

MORAL RESPONSIBILITY IN CORPORATE CAPITALISM

Sherron S. Watkins

I have spoken to a wide variety of audiences across the country about my experiences at Enron. I have shared my personal opinions not only on what I think went wrong at Enron, but on what I think is wrong with the whole system that this country's equity market relies upon to function properly.

In January of 2002, Congress found and then released my memos to the then CEO of Enron, Ken Lay. My life has sure changed since then. I am actually trying to figure out exactly what to do with my career from here out. I left Enron this past November. Being a somewhat well-known whistleblower can hinder your job prospects; not to mention that my résumé has 3 companies—Enron, Arthur Andersen, and Metallgesellschaft. (Metallgesellschaft is the 125-year-old German company that was brought down by a \$1.3 billion oil trading scandal in late 1993.) I am afraid that in a very short period of time, I will not have an employer on my résumé that still exists. On the flip side, I guess I won't have to worry about reference checks.

It would appear that despite the new corporate fraud and accounting bill, the Sarbanes-Oxley Act that was passed and signed into law in the summer of 2002, the average investor still needs more of a voice. The Act won't have much meaning unless the SEC gets its budget increased. The Senate has approved the budget increase called for in the Act, from \$438 million to approximately \$750 million, but the House and the White House are stalling. The White House recently said it would double the SEC's budget, but the proposal is for 2004.

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What we really need, in effect, is more policeman on the street—we need to see the SEC increase their staffing and their ability to track these things down.

The Sarbanes/Oxley Act has no meaning without changes and budget increases at the SEC—and investors seem to realize that. We've just come off the third year of a declining S&P, and that hasn't happened since the 1939-1941 time period. This country's equity market is in a decline that some liken to the great depression. Certainly we are looking at the worst bear market this country has seen in the last 60 years. Investors, business leaders, Congress, and regulators all seem stuck; no one seems to have a clear-cut plan for restoring confidence in this country's stock markets. Worse yet, this stalling game with the SEC's budget and the kick-off of a new public company accounting oversight group seems to have only solidified investor concerns that the market is not a fair place for the small guy to play.

I have been telling my story in the hopes that I could raise awareness about the pressures in the everyday workplace, the weaknesses in the watchdog groups that are in business in this country to protect investors, and the need for real reform and real change—not only in the accounting industry, but also on Wall Street.

My Personal Background and Role at Enron

I started working at Enron in late 1993. I worked in a variety of roles at Enron, but in mid-2001, after struggling with the pressures of managing work and a two-year-old at home, I accepted what I thought would be a non-taxing commercial support position with Andy Fastow, Enron's Chief Financial Officer. Andy Fastow had been Enron's Chief Financial Officer for a number of years, but in June of 2001 he also became responsible for the mergers and acquisitions group. I joined Andy's M&A group in late June of 2001 to help prioritize Enron's asset sale efforts.

The Discovery of Raptor Problems

At this point, Enron was looking to divest itself of a number of assets and I was in charge of prioritizing that effort. I was charged with reviewing all assets that Enron considered for sale and determining the likely economic impact of a sale. As part of the sale analysis, I reviewed the book values and estimated market values of each asset—a fairly simple job. Little did I know where it would lead.

A number of assets were hedged with these entities called Raptors. Any asset that was hedged should, for the most part, have a locked-in sales value for Enron—meaning that despite current market prices, Enron should realize the

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hedged price with the Raptors. The Raptor special purpose entities were owned by LJM, the now infamous outside investor partnership run by Andy Fastow.

In completing my work, it became obvious that certain hedged losses incurred by the Raptors were actually coming back to Enron. The general explanation was that the Enron stock that had been used to capitalize the Raptor entities had declined in value such that the Raptors would have a shortfall and would be unable to pay back what they owed to Enron. When I asked about third-party money or outside equity at risk, I never heard reassuring answers—basically the answer was that it just wasn't there. I was highly alarmed by this fact. My understanding as an accountant is that a company could never use its own stock to directly generate a gain or, as in Enron's case, avoid a loss on its income statement. I just couldn't imagine that "accounting" rules had gotten that creative.

Events Leading to My Memos to Mr. Kenneth Lay

To be perfectly honest, it didn't take long to discover the flaw in the Raptor transactions. The Raptor deals expired sometime in 2003 and 2004. It was like staring at a time bomb. When I discovered the problems with the Raptors, my first reaction was to leave Enron as fast as I could. This was some of the worst accounting fraud I had ever seen. I could no longer take pride in working there. As I testified in front of Congress, when then CEO Jeff Skilling resigned on August 14, 2001, I realized that the situation was very likely worse than I had first thought. I felt I had to warn Ken Lay. In my initial one-page anonymous letter to Lay, I said, "Skilling looked down the road and knew this stuff was unfixable and would rather abandon ship now than resign in shame in two years." I felt like Lay deserved to know what he was facing when he was stepping back in as CEO.

Within a week, I was meeting with Ken Lay armed with more memos I had drafted to help explain the problems facing the company. My main point to Ken Lay was that by this time, the Raptors owed Enron in excess of \$700 million under certain hedging agreements. My understanding was that the Raptor entities basically had no other business aside from these hedges; therefore, they had collectively lost over \$700 million. I urged Lay to find out who lost that money. If he discovered that this loss would be borne by Enron shareholders via an issuance of stock in the future, then I thought we had a large problem on our hands.

Enron Conclusion

For my part, when I met with Ken Lay, concerned that Enron's accounting for certain related-party transactions had crossed the line and might very well be fraudulent, I not only expected that a thorough investigation would occur, but I also expected Enron to establish a crisis management team to address the financial peril Enron would face when the accounting was exposed—which in my opinion was sure to happen. In the long run, companies rarely

get away with “cooking the books.” However, no other top executives came forward to back me up and Ken Lay gravitated towards good news and didn’t quite accept what I was saying.

Enron and its team of investigative attorneys decided nothing was amiss, but that we should unwind the transactions that I had questioned because the optics weren’t good and they were a distraction from core business. That unwind wiped out \$1.2 billion from shareholders’ equity and started Enron’s free fall ultimately ending in bankruptcy, roughly 6 weeks after the press release announcing the unwind.

I certainly believed that Ken Lay was going to act differently, that he would take me seriously. I thought others would back me up. I was naïve. I was too optimistic. I have explained to a number of audiences, including Congress, that the whole sorry mess was incredibly similar to “The Emperor’s New Clothes.” First, there is an Emperor who is vain and is focused on his appearance rather than on running his kingdom. There are the swindlers who are there to rip off the kingdom by making the Emperor new clothes from non-existent cloth, which they say you must be worthy to be able to see and if you are stupid or not fit for office, you will not be able to see it. The Emperor’s insecure ministers don’t want to appear stupid or unfit for office so they lie and say they can see the cloth. Then, when the Emperor is about to go on parade with his “new clothes,” the ministers realize they are being swindled but by then it was too late, and they would have to admit to lying and be fired. That’s what happened at Enron when I tried to tell Ken Lay that we’ve got big problems, and he turned to his executive management team and to a man they all said “Don’t ask me, I thought Arthur Andersen had signed off on this, I’m certain it’s been blessed, they’ve scrubbed it, and you’ll just have to ask someone other than me.” That wasn’t their water cooler conversation, but when face to face with the CEO to say that I was probably right meant that they were in jeopardy of being fired because when Jeff Skilling was CEO, they had not come forward and said anything about these structures.

In hindsight, my efforts were probably too little to late. There might have been things we could have done and survived by calling in outside law firms and the SEC, and since we had so much bank debt, the banks might have tried to keep us alive. However, since these structures had been blessed all the way up to the board, I was in effect asking upper management to fall on their swords, because they probably all would have had to resign.

I was extremely disappointed about the events of that fall. About the only consolation for me were the hundreds of e-mails, phone calls, and letters from both former and current Enron employees who are so grateful that my memos exist. There was just an overwhelming feeling that justice would prevail, that the people responsible would have less chance to get away with it once my memos came to light.

Some commentators initially argued that the capitalist system worked. That the marketplace caught Enron in the act of presenting less than honest financial results and punished the company. That doesn’t hold water for me.

We have laws and regulations in place to stop abuses before they occur. We need protections for the rank-and-file employees, for the average investor. Over 4,000 employees were let go with virtually nothing in the way of severance, a scant 3 weeks before Christmas. Many more employees lost all of their retirement savings, trusting that Enron would always be a winner for them. Investors lost over \$60 billion on Enron in just under 2 years. Enron went bankrupt without ever reporting a poor quarter relative to recurring earnings.

Many speculate that the top executives at Enron either had culpability in the accounting shenanigans themselves or chose to ignore them because they did not want the gravy train of money coming to them (in the form of bonuses and stock option sales) to stop.

Corporate Watchdog Groups

It's clear now that there were problems in the executive suite at Enron, but what happened to all the watchdog groups who are in the business of protecting investors?

Enron's financial reporting and disclosures appear to have been fraudulent with regard to the Raptor transactions; however, even in Enron's legitimate business transactions, its reporting was less than clear and forthright. On November 19, 2001, Enron met with its lenders in New York to review its deteriorating situation. At that meeting, Enron reported that while it had \$13 billion of debt on balance sheet, another \$25 billion was off balance sheet, bringing total debt to \$38 billion. At the end of 2000, Enron's debt-to-equity ratio was close to 70%—add this additional off-balance-sheet debt and the debt-to-equity ratio would be over 250%. I'm all for the use of legitimate non-recourse off-balance-sheet structured finance deals, but Enron went overboard. I sure hope most companies don't have more than twice their reported debt levels hidden in off-balance-sheet structures described in arcane footnote disclosures.

Somewhere along the way, the financial accounting system in this country has morphed into something akin to the tax code. A company can pick and chose a set of accounting rules that it thinks relates to its line of business, follow those rules, and—no matter how illogical the outcome—feel justified in reporting the results of its operations according to those rules. The idea that a set of financial statements and disclosures is supposed to fairly represent the financial condition of the company appears to have gone out the window.

I believe we truly need reform and change in the U.S. accounting system. We need a principle-based system, but we've gotten so rules-based that we might as well start over.

In Houston, Enron Treasurer Jeff McMahon told me that Enron decided which rules got them the results they wanted and the message to Andersen was "this is the way we're booking this, we won't change it unless you show us specifically where we've broken the rules." McMahon spent over 2 years in our London office and he said he could never get away with the same approach. In

the U.K. they are more principle-based and, best of all, the auditor has the final say. If the auditor thinks the results are squirrely and not representative of the true financial picture, then the auditor's decision holds—not the company's—if that company wants a clean opinion.

Clearly the auditing watchdogs failed to prevent Enron's financial reporting lapses, but what of the other watchdog groups this country's capital system relies upon? The majority of investment analysts had Enron ranked as a buy as late as October 2001. The analysts glowing reports about Enron were clearly not objective—they appear to be severely conflicted by the investment banking fees generated by the analysts' sister operations. A simple review of Enron's annual and quarterly filings would have highlighted some glaring problems:

- cash flow from operations that was virtually nonexistent until the 4th quarter of each year,
- predictable earnings declining significantly from 1997,
- a steady stream of top executives leaving,
- related party disclosures that were indecipherable, and
- a Yahoo message board filled with insider tips to stay away.

These were the obvious ones. More subtly, someone should have noticed that Enron was a breeding ground for potential problems:

- an accommodating and passive board,
- an unhealthy drive to meet earnings targets, and,
- probably the most damaging, a penchant for hiring only the best and brightest and rewarding them like spoiled rock stars while at the same time demanding that they "innovate, innovate, innovate."

Unfortunately, the dark side of innovation is fraud. The Department of Justice has two guilty pleas from Enron executives involved with the finance schemes, has another guilty plea associated with market manipulation of energy prices in California, and has indicted Andy Fastow, Enron's former CFO. The rumor around Houston is that there are possibly over 2 dozen more indictments to come. The problem is the complexity and the veil of propriety that Enron put on its financial statement manipulations. In nearly each case, Andersen, outside law firms, and Enron's own board approved the transactions.

The Department of Justice (actually quoting from a *New York Times* reporter) has said the Enron case is like calculus and all the other corporate scandals of late are like third-grade math in comparison. Additional indictments are expected, but it will take a while. Arrests have been made at Adelphia, Tyco, ImClone, and WorldCom, but the alleged fraud at these companies is relatively easy to understand:

- at Adelphia, the top guys borrowed company money for personal uses;
- at Tyco, the CEO evaded sales tax and also stole from the company;
- at ImClone, it was insider selling in advance of a Federal rejection of a major new drug; and

- in the easiest of them all, WorldCom simply shifted expenses to the balance sheet.

None of that would do for Enron. We had the best and the brightest on these Raptor transactions. It takes a rocket scientist to figure them out. The diagrams of the Raptor structures look like a complex and mind-numbing maze. In fact, when Enron finally did conduct a thorough investigation of the Raptor transactions, the investigative group consisted of Bill Powers (the dean of the University of Texas law school), Bill McLukas (a 19-year SEC veteran and lead enforcement lawyer now at Wilmer, Cutler), and scores of lawyers and accountants from Wilmer, Cutler and Deloitte Touche. The group was hired in late October and got started the first of November of 2001. They were given an unlimited budget and complete access to documents and people.

Bill Powers told me that it took over 6 weeks of examining documents and over \$4 million in fees to conclude that Andy Fastow's LJM partnerships and the Raptor vehicles functioned solely "to accommodate Enron in the management of its reported financial results." The Raptor structures were designed to "give the appearance of a hedge" when in fact Enron was hedging with itself. The investigation was completed in 3 months with the issuance of the Powers Report on February 1, 2002. Bill Powers testified in front of Congress that month, concluding that what they had discovered at Enron was both shocking and appalling.

The Department of Justice has a tough job on its hands because Enron's schemes were so complex. Plus, I suspect that it is hard to get your arms around all the Enron executives that personally enriched themselves from these structures, or at least condoned the behavior and reaped the rewards less obviously from performance bonuses and stock option sales that were higher because of the soaring stock price. Many ex-Enron employees are anxiously awaiting the additional indictments that will surely come.

Of course the problem is that it's too late for so many—retirement savings have been decimated, jobs lost, and careers ended. Frankly, many former employees are upset with the whole system that failed at Enron. They are upset with the outside accountants, with Vinson & Elkins (the outside lawyers), and with the Wall Street analysts. Additionally:

- Where were the credit rating agencies? They downgraded Enron well after the horse had left the barn. The rating agencies more or less tracked the flight of capital from Enron and then determined that the company was not credit worthy. Thanks for the timely advice.
- The traditional bankers kept lending to Enron despite large exposures and now it has come to light that certain lending practices were akin to aiding and abetting Enron's financial statement manipulations and off-balance-sheet schemes.
- The worst abuse comes in the form of the lobbying efforts done by both the business and accounting communities. Campaign contributions by

both big business and the accounting industry appear to have stymied former SEC Chairman Arthur Levitt's efforts at reforming the accounting industry in 2000.

- The Financial Accounting Standards Board's 1994 efforts at forcing companies to expense stock options was weakened to a mere footnote disclosure after facing unprecedented pressure from Congress, which had been lobbied by the high-tech sector (among others) that such a move would be detrimental to the capitalist system.

What's Next?

Now that Enron's problems have been replicated elsewhere, with Congress or the SEC investigating over a dozen companies, it has become popular again for Congress to act in favor of the small investor. The Sarbanes-Oxley Act clearly takes aim at the rampant abuses that have shaken investors. It represents a broad overhaul of corporate fraud, accounting, and securities laws:

- Criminal Fraud has been defined to include engaging in any "scheme or artifice" to defraud shareholders. The maximum sentence for defrauding pension funds has been raised to 10 years. (A fair number of people at Enron want the *minimum* to be 10 years.)
- Chief Executives and Chief Financial Officers of publicly traded companies must certify their financial statements and will face up to 20 years in jail if they "knowingly or willfully" allow materially misleading information into their financial statements.
- Wall Street investment houses cannot retaliate against research analysts who criticize investment banking clients of the firm.

The bill goes along way to restoring teeth needed to curb unfettered corporate greed.

Corporate America's Ills and Conclusion

It is imperative that the goals of this bill are embraced by today's business leaders. We must all work to restore confidence in the marketplace. The average investor today has a distrust of the accounting numbers and a disdain for the exorbitant pay packages given to top management. The compensation packages of top executives have been creeping up over the past several years and have been fully disclosed; however, average investors didn't notice or didn't complain as long as their own stock investments rose in value. Now, investors view these quasi-guaranteed multi-million dollar compensation packages as evidence enough of wrongdoing.

I actually have a problem with Jack Welch's retirement package. His current divorce proceedings brought to light a very lucrative annual package for Jack Welch's retirement years, including corporate jet services, a Manhattan

apartment, tickets to sporting and cultural events—the list is too numerous to recount. Welch's explanation is that the terms were part of a negotiated compensation package from several years ago. He had foregone current compensation back then for these perks now. He says he's willing to pay for some of these services now that they've been disclosed to the public. Isn't that interesting? Was his contract structured that way originally because the SEC requires the annual disclosure of CEO compensation, but not the compensation of retired executives? It appears the SEC will now have to add a new disclosure requirement, including retired executives as well so that shareholders understand what their company is truly paying its top executives.

I would like to see the new generation of business leaders embrace that tried and true ethical litmus test: if a transaction or activity will not pass muster on the front page of the *Wall Street Journal*, then just don't do it. In our capitalist system, we rely on the proper disclosure of financial and operating information in order to have a proper allocation of resources among businesses. The drug company with a new and important discovery enjoys a higher stock price, giving it access to funds to develop and bring that drug to market. A company with a product line that has gone stale sees its stock price decline. We send a message by economically rewarding those companies that are outperforming their peer group and vice versa. To report misleading financial results is dishonest and amounts to nothing less than theft.

There can be no successful capitalist system without trust; we expect honesty in our everyday dealings. Investors have to have faith that their business leaders strive to be ethical and to comply with existing laws and regulations in spirit and in substance, not just form. In order to flourish however, a successful capitalist system must be predicated on fairness, honesty, and integrity. In fact, many scholars describe the capitalist system as a three-legged stool—economic freedom, political freedom, and moral responsibility. A weakness in any one and the stool topples.

It is unfortunate that we must now regulate the moral responsibility part, but to borrow E.J. Dionne's words from a *Washington Post* column he wrote on Enron in January of 2002, he quoted from James Madison in the *Federalist Papers*: "If Men were Angels, no government would be necessary." E.J. Dionne added: "If capitalists were angels, we could deregulate everything." Clearly capitalists are not angels, I don't think anyone ever thought they would be, but it would appear that we have to put some teeth back in existing governmental oversight if we are to protect this country's capitalist system. We must not lose this opportunity to ensure that the appropriate safeguards are in place so we can all be comfortable again investing our hard earned dollars in this country's equity market place. It's also time for our business leaders to do the right thing and recognize the moral responsibility part of our capitalist system and live up to that.

Questions and Answers

Q.: Given all you've seen, what do you think is the fundamental reason for this suspension of morality by the business community that has occurred over the last five years.

A.: I think you have to recognize human nature and the power of money as a corrupting influence. There were some safeguards in the system that have been removed in the last ten years. One of these was in 1991, the SEC used to require that top executives could not do a cashless stock option exercise. They had to exercise stock options with money coming out their own pocket and hold the stock for six months. In 1991, they changed that to say that if you held the stock options for six months, you could do a cashless exercise just like regular employees, exercise the option and sell the stock that very day.

Well, what happened slowly over time was that executives used to sell their stock in advance of good news because they were going to be at risk for six months. Once that holding period was changed, they now tend to exercise in advance of bad news. Global Crossing's CEO has \$700 million and the company is bankrupt. I could see where a six-month holding period could have put the brakes on some of Enron's behavior, because if the top executives knew that they were using highly aggressive accounting practices, and they knew that they might be exposed by any number of employees in the next six months, they all of a sudden are trapped. They can't sell their stock options, they can't get rich. They would have to clean up their accounting before they can take that six-month risk. That is just one tiny change that might curb the realities of easy money. Another issue was a 1993 tax reform: The IRS said you could no longer deduct salaries above \$1 million, so more stock options and stock grants were given top executives. Maybe we ought to reverse that: if someone is worth \$2 million or \$3 million, pay them that and don't weight it so heavily on stock options and stock grants.

I'm sure that at some point in time, there are some people at Enron who tried to persuade you to stop talking about what you had found. I'm wondering if you could relate some of your experiences with that and whether there was some support that you did find at Enron for bringing everything to light.

There was not a lot of support when the heat really got turned up. What you hear about all the whistleblower stereotypes is true. You really get treated like a pariah and had Enron lived, it would have been the typical case with me where they would have really given me no responsibilities, nothing to do, and I would have seen the handwriting on the wall and found another job. When I testified in front of the House, I found out that two days after I met with Ken Lay, Vinson & Elkins sent a memo to the company about the plusses and minuses of firing me, so that was Ken Lay's first response. But lucky for me, they said that it probably would bring up more trouble than it was worth. While there was no private sector whistleblower protection, the fact that I might have enough of a leg to stand on meant that if I sued, some of these sensitive materials might become known. They then tried to bully the market by writing

these things off in the third quarter. And then they didn't have a good, adequate explanation as to what had happened. Everything went downhill from there.

Define accountability. We all talk about it, but we have to talk about punishment. How are we going to make people feel: "I am going to be accountable, I can't just walk away and maybe make some money afterwards."

As far as accountability, I think we've seen a sea change and it's popular for the Department of Justice to be chasing white-collar criminals. The wheels of justice might move slowly, but I think people in Houston think there will be at least 25 indictments relating to Enron when it's all said and done. Jail time works. If you make \$700 million and you have to give up \$100 million, that doesn't work and we've seen that. Chainsaw Al, with the Sunbeam problems, is a \$300 million man and I think he settled all his cases for under \$100 million. There needs to be something serious like jail time.

Could you describe what you think McKinsey's role in the Enron debacle was and if you think they knew what was going on.

I think part of the problem with McKinsey is similar to Enron and Andersen. Jeff Skilling was a McKinsey partner. A lot of our upper-level accounting executives were from Arthur Andersen and they know how to game their own system, they know how to push the buttons at those firms to get what they want accomplished. For McKinsey, Enron was a \$10-million-a-year client and Skilling was not a person who wanted to hear things that didn't agree with where he was going. So whether they had discussions or comments or wanted to say that this was crazy, most people say that it is absolutely ludicrous to waive your code of conduct and start to do business with a partnership your CFO is running.

And I'm sure McKinsey, behind closed doors, thought that that was one of the worst things they'd ever seen, but do you want to anger your \$10-million-a-year client? I think that becomes problematic because with too many consulting shops, if you are auditing the company or you have a lot of other business with them, it's hard to be objective and honest and these things are very subtle. From what I can tell when I look back on Enron, that was clearly the tone at the top, and you can have no ethical lapses at the top. Ethical lapses at the top permeate throughout the organization and you have much larger problems throughout with middle management and lower management. I think that can't be ignored; boards should pay attention. Enron has a pristine code of ethics, code of conduct, and corporate governance procedures, but they weren't following the spirit of their own procedures and that's a huge warning flag.

You describe yourself as naïve and optimistic before this whole unraveling occurred. I can sense that you must have gone home at nights, feeling like the world was horrible, that people were evil, and that there was no hope; or maybe that's my interpretation about how I would have felt in that situation. Can you speak to that? You seem very positive. How did you maintain that?

I really felt like I was swimming upstream by myself. Enron's in-house lawyers had actually told me that they were going to use my memos as a defense of Ken Lay and the board. An employee raised some concerns, we hired an outside law firm, and they did an investigation and said nothing was wrong, so aren't we great guys. I had one of them say, "You need to get with this other law firm, he's hired an accounting firm and you're pushing it. Because this accounting stuff is probably not that off-kilter, it probably doesn't violate any rules."

The best thing for me was the Powers Report that was made public on February 2, 2002. I felt all by myself until that report came out, which was just so scathing. It named names. It criticized the Chief Accounting Officer, the Chief Risk Officer, obviously Skilling and Lay and the board and Vinson & Elkins and Andersen. For a lawyer to get in front of Congress and use words like "shocking" and "appalling," it's pretty strong language. That was probably the best feeling, to have that kind of turn-of-events happen.

The press has focused a lot on the importance of teaching ethics in MBA programs. I think places like Haas have done a great job of responding to that and I certainly don't disagree with that as a focus. But my sense from what we've read about Enron and Tyco and these other companies is that perhaps the culture is what was responsible for a lot of the behavior. What was the culture like at Enron? Do you feel like that may have been responsible for breeding this misbehavior? What can be done to reverse that? Is it in training? Is it in hiring and checking? Is it in MBA programs or is it in kindergarten?

It's probably a little bit of everything, kindergarten up to MBA programs. Nowhere was it seen more than this past year when thousands—by now, it's at least 6,000 at Enron, more at WorldCom, 85,000 Andersen people—have had to scramble. Although the numbers were good with Andersen early on, most of the Final Four grabbed up partners and staff in order to get the clients. After this busy season, I think you're going to see a lot of those Andersen people, especially the partners, asked to leave wherever they ended up last year. The penalty for being in a less-than-ethical shop is extreme and maybe people will pay more attention to it.

One example that many of the Enron books have discussed is that Ken Lay had Enron as well as Arthur Andersen and Vinson & Elkins use his sister's travel agency. That gave millions of dollars to that agency and it was a wretched travel agency. The service wasn't even good and I can speak to that because I have some horror stories about their travel scheduling. This went on for years and years and years. Now, if you take someone like Andy Fastow who does not appear to have a good sense of right-and-wrong, that's telling him that "hey, my partnerships are helping Enron meet their financial statement targets so why shouldn't I carve some out for myself because Ken Lay has been carving some out for his sister?"

I think when you see an ethical lapse like that, you ought to leave the company, because if it's at the top, something bad is going to happen somewhere down the line. You want ethical leaders at the top. It bothers me reading about

the Bausch and Lomb CEO who lied on his résumé about his degrees and no one seems to be alarmed about that. He apologized, saying that he's on various boards and those boards misprinted his bios, so he's sorry, please excuse him. He should have proofed those bios better. He's not apologizing for lying on his résumé. If you're lying on your résumé, what's the next step? Pushing the financial statements doesn't seem to be far off. I think you can't ignore tiny things like that. They're not so tiny. They speak to a person's character and I'm not going to ignore them any more.

Have you lost many friends in Houston?

When my memos were released, there was an enormous swell of support because there was a feeling that the top guys weren't going to get away with it any more, that there was some evidence that they knew about problems. Of course, there is the complaint that I should have gone to the SEC or the financial press with my information. I think that would have just killed the company quicker. Where I've lost friendships is seeing how the corrupting influence of stock options and big bonuses made people that I thought were highly ethical not do the right thing, and that's been very disappointing.

What advice would you give Haas students, say, out three years on the job and they come into a situation not exactly like yours, which doesn't come along that often, but what advice would you give them based on your experience? Also, what would you have done differently? Can you give them any guidance on that?

I think that when it's a problem that is confined to one division, one group's first step in the wrong direction, then by all means say something. But what I would do in hindsight is I would get more people to try and stand with me. I've since found out that one of the in-house lawyers, Jordan Mintz, had asked Fried, Frank to do a study of these partnerships and he was on the exact same page as I was. Maybe it would have been a different outcome had we gone together to meet with Ken Lay. I also think that I should have gone to the audit committee of the board instead of just to Ken Lay, especially when I found out that they were using Vinson & Elkins to do the review of my concerns.

But in almost all of my speaking engagements across the country, where it's not a student group, where it's a working audience, I've had one or two people come up to me with horror stories about doing a whistleblowing type of activity and getting summarily fired. So, you've got to make sure you think of your family situation. I think if you see a lapse at the top, leave the organization.

I know that the correlation has been made in the media before, but with the three whistleblowers all being women, I was curious as to how you think the impact of yourself being a woman and a mother in a stereotypically man's corporate world affected you either in the way you acted or in the way you were treated after protesting the practices.

It's hard for me to say. I can talk about *my* deal. There were men that were trying to raise red flags. Jeff McMahon met with the COO at the time very concerned about these partnerships. Jordan Mintz met with the General Counsel, and they didn't get anywhere. Also, what happened with Jeff McMahon is

that he got shoved over to a business-origination unit and started making large bonuses. I wasn't part of the core circle. Probably neither was Jeff McMahon, but he kind of got let in once he complained.

It's hard to say whether it's a female/male thing. On paper, there are as many whistleblowers that are men. But clearly at WorldCom, Enron, and the FBI, women are not really in the top management. Many have said, we could still keep our outside values, we were still close enough to the top to critique operations, but we were not in that inner circle. It is harder to believe a friend has gone that far, if you really are that close. I've had friends that were in trouble with the Department of Justice. I can't believe they did what they did. It's still hard for me to believe it, so if you have worked with someone for ten years, it might be harder to see where they have stepped over the line.

There was a time when you realized what was going on, that moment where you could say well, I just want to step aside, I'd just like to get transferred somewhere else. What moved you to do what you did?

It was Jeff Skilling's resignation. I felt that as long as he was still there as CEO, trying to come up and say anything was just pointless. But when he quit, I felt like maybe it was a moment where we could straighten things out and also let Ken Lay know what he was stepping back into. I had always thought ill of his sister's travel agency policy, but in hindsight, when I look back at what happened at Enron, I blame that a lot. I still thought he was a man of integrity and would do the right thing, but that didn't quite happen.

I'm a Berkeley student and in honor of the Free Speech Movement, I feel a duty to ask this question. As a community, what is the most important thing to protest, outside of the state or federal capitol or outside of the corporate headquarters?

The teeth that have been removed from existing regulation need to be put back in, similar to the hold on stock options, potentially expensing stock options, getting a sense that boards truly have a fiduciary responsibility to shareholders. The capitalist system makes this the wealthiest country in the world. When you look at what it can do for people who have come here with nothing, who have second-generation people going to expensive universities, it can be a wonderful system. But we've got to make sure the moral responsibility part of the leg of the stool is just as strong as the economic freedom and political freedom legs. It's a shame that you have to legislate that but when you look through history—there was child labor abuse, environmental pollution—capitalists and human nature will abuse and try to make more money for themselves. It's human nature and you have got to try and make sure that the right regulations are in place and that the right teeth are in those regulations.

