

PRIVILEGE

REQUEST FOR COMMISSION ACTION

Control No.: DS-0:

Enron Corpor

DETERMINED TO BE AN ADMINISTRATIVE MARKING
E.O. 12065, Section 6-102
By JMV NARS, Date 5/2/2012

response and of the

SUB

February 1, 2002

ACTION MEMORANDUM

TO: The Commission
FROM: Office of Congressional and Intergovernmental Affairs *BSA*
RE: In the Matter of Enron Corp.

Congressional request for a briefing and documents concerning Enron Corporation ("Enron").

RECOMMENDATION: That the Commission (1) authorize submission of a letter and memorandum of response and documents attached thereto substantially in the form attached to Chairman W.J. "Billy" Tauzin, Chairman of the House Energy and Commerce Committee ("the Committee"), and (2) authorize SEC staff to further brief the Committee and its subcommittees and their staff on non-public information relevant to this matter and to provide briefing updates upon further request from the Committee.

ACTION REQUESTED BY: 3:00 pm, Friday, February 1, 2002

SUNSHINE ACT STATUS: Not applicable.

PRIOR COMMISSION ACTION: On December 12, 2001, pursuant to authority delegated to the Director of the Division of Enforcement, the Commission filed a subpoena enforcement action against Andrew S. Fastow.

On December 14, 2001, the Commission authorized a prior briefing and access to documents and SEC staff for the Committee.

NOVEL, UNIQUE OR COMPLEX ISSUES: None

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**OTHER OFFICES OR
DIVISIONS CONSULTED:**

Division of Enforcement/Linda Thomsen 942-4501
Office of the Chief Accountant/Bob Burns 942-4400

Office of Corporation Finance/Bill Tolbert 942-2891

Office of General Counsel/J. Gordon Seymour 942-0932

SOURCE OF CASE: Not Applicable.

SMALL ENTITY STATUS: Not Applicable.

PERSONS TO CONTACT:
Bill Tolbert 202-942-2891
Peter Kiernan 202-942-0015

I. BACKGROUND

On December 7, 2001, Chairmen Tauzin and Greenwood wrote to Chairman Pitt (see letter at Attachment A) regarding the Committee's interest in "the apparent collapse" of Enron, including "the loss of substantially all of the equity value in Enron, ...the loss...of sizeable portions of...retirement savings in Enron's 401(K) plan...(and) the lack of transparency in Enron's derivative positions in the energy market." They indicated that the Committee is conducting a full review of the issues surrounding Enron's collapse "as well as the accounting issues that have arisen in the recent disclosures."

The December 7 letter asked for (1) answers to a series of questions about the SEC staff's reviews of Enron's filings and the accounting rules applicable to portfolio holdings of energy derivatives and Special Purpose Entities; (2) information (i.e., documents) relating to all Commission reviews of Enron filings on Forms 10-Q and Forms 10-K for the period beginning January 1997 until the date the SEC began its formal inquiry into Enron and any proposed adjustments to Enron's filings submitted by Enron's auditors; (3) access to SEC employees who reviewed and commented on Enron's filings; and (4) a private briefing, by December 14, 2001, covering the details of the Commission's investigation of Enron.

On December 14, the Commission approved a response from David Becker, General Counsel, to Chairman Tauzin offering to provide the requested information, documents, access to SEC staff, and briefing, and that letter was sent on December 17. (See letter at Attachment B).

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On January 23, 2002, Chairman Tauzin wrote again to Chairman Pitt (see letter at Attachment C) acknowledging Mr. Becker's December 17 letter and asking a series of detailed questions as to what Enron Forms 10-K and Forms 10-Q filings for the period from 1997 to 2001 the Commission had examined, as to the Commission's policy for selecting company filings for review and whether a non-review of Enron filings violated that policy, and concerning any Commission reviews of Enron filings during the first quarter of 2001 "to ensure that investors were in fact provided with material necessary to make informed investment decisions." Chairman Tauzin's letter also requested copies of any comments made on certain of Enron's filings.¹ Chairman Tauzin asked for a response to this request by February 1, 2002.

II. THE COMMISSION STAFF'S REVIEW OF ENRON'S FILINGS AND REVIEW POLICIES

The letter from Chairman Tauzin requests information about the Division of Corporation Finance's examinations of Enron filings from the first quarter of 1997 until the second quarter 2001 and the Division's review policies. During that period of time the Division examined the filings of Enron Corp. on six occasions.

On August 14, 1996, a merger proxy statement was filed confidentially by Portland General Corp. for a stock-for-stock merger with Enron Corp. The Division completed a full review of that filing and declared the registration statement effective on October 10, 1996. On May 16, 1997 Enron filed a post-effective amendment to this merger transaction to reflect changes in the consideration paid to Portland General Corp. shareholders. The staff of the Division of Corporation Finance completed a full review examination of this filing on May 16, 1997. In completing this full review the Division examined the Forms 10-K for fiscal years ended December 31, 1995 and December 31, 1996 and the Form 10-Q for the first quarter of 1997.

On September 3, 1997 Enron Corp. filed a merger proxy for the stock-for-stock acquisition of Enron Global Power and Pipelines LLC. Enron Global Power and Pipelines LLC was a 52% owned consolidated subsidiary of Enron Corp. at the time. The Division completed a full review of this merger proxy and declared it effective on October 17, 1997. In completing this full review the Division examined the Form 10-Q for the second quarter of 1997.

On September 12, 1997 Enron Corp. filed a Form S-3 registration statement for an unallocated shelf offering for \$1 billion. The Division monitored this filing for compliance with the comments it raised on Enron Corp.'s periodic reports in the Enron Global Power and Pipelines LLC merger transaction.

¹ "If the Commission commented on any filing other than the Enron Corporation 10K for the fiscal year ended 12/31/97 and 10Qs for the first, second and third quarters of 1998, please include a copy of those comments with your response."

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On August 7, 1998 Enron International CPO Inc. and Enron International CPO LP filed an initial public offering. These entities were special purpose entities formed for the purpose of providing construction loans on international energy projects sponsored by Enron. The Division selected this filing for a full review. In its comment letter to Enron International CPO, the Division raised a comment regarding the need to provide Enron Corp.'s financial statements in this registration statement. Since the Division was requesting the financial statements in the filing, it also completed a financial statement review of Enron Corp.'s Form 10-K for fiscal year 1997 and the Forms 10-Q for the first two quarters of 1998. This information was provided to the Committee on Energy and Commerce on December 17, 2001 in response to its prior request. Enron International CPO never responded to the Division's comments and eventually withdrew its filings.

On January 12, 1999, Enron filed a Form S-3 registration statement for an unallocated shelf offering for \$1 billion. The Division monitored this filing for compliance with the comments issued on the Form 10-K for fiscal year 1997. As part of this process, the Division also reviewed the financial statements and the management's discussion and analysis on the Form 10-Q for the third quarter of 1998.

On April 4, 2000, Enron filed a Form S-3 resale registration statement. The Division limited its review of this filing to the legal opinion attached as Exhibit 5 to the filing.

Review Policy

It is believed that prior to 1980, the Division of Corporation Finance reviewed nearly all filed documents. The documents examined by the Division are comprised of initial public offerings, other transactional filings, such as offerings of securities or merger transactions, and periodic reports, such as annual and quarterly reports. In 1980, as a result of the increase in the amount of transactional filings and the number of public companies, the Division determined to implement a "selective review" system. This system acknowledges that all filings cannot be examined by the Division and establishes criteria, which allow the Division to use its resources most productively.

The selective review system contemplates that almost all new entrants into the disclosure system will be fully reviewed. Filings, other than initial filings, are chosen for examination based upon specific criteria. The types of reviews completed by the Division include a full review, a financial statement review and a limited review, commonly referred to as a monitor. A "full" review is a complete examination of the filing. A "financial statement" review is a review of a company's financial statements and its supplementary analysis of those financial statements, known as management's discussion and analysis. A "monitor" is a limited scope review of a specific legal, accounting or other disclosure item or items. A substantial number of filings are not subject to any staff review.

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The Division makes a review decision based on a summary examination ("screens") on all incoming transactional filings and, on a time available basis, on Forms 10-K to determine if they fall within the screening criteria, which may trigger one of the levels of review detailed above. The characteristics that would lead to a filing being selected for review are established periodically in discussions among the Division's senior staff. The selection criteria vary over time and reflect changing market and economic conditions as well as then current known legal, accounting and disclosure issues. The screening criteria are also designed to identify companies whose financial information suggests on its face that they are experiencing financial difficulty or whose filings on their face based on the screening process appear most to warrant examination. When screening annual reports on Form 10-K, the Division also considers the amount of time that has passed since the last review of the company's financial statements.

To determine which companies are having financial difficulty, the Division considers liquidity ratios and profit and performance ratios. Also, the Division subscribes to a software database that identifies issuers with financial characteristics similar to those of pre-bankrupt entities. This software database also detects those companies that significantly outperform or under-perform their industry based on return on assets ratios.

The Division may also select filings containing specific legal issues, particular accounting issues and various transactions, such as management-led cash buy-outs, for review. The screening criteria in these areas are dynamic and change as companies offer different types of securities or employ novel financing techniques, transactions become more complex, and new trends develop.

If companies meet any of the profiles outlined in the three preceding paragraphs, they are generally selected for a full review, assuming the Division has sufficient resources to complete that review in a timely manner.

Representative Tauzin's letter asks if not reviewing Enron Corp.'s Form 10-K in the last three years violated our screening policy. Enron Corp.'s transactional filings were screened in each of the years since its last review was completed on March 5, 1999. On each occasion, the screening process for the filings did not result in a selection for review, with the exception of the April 2000 Form S-3 relating to the legal opinion. As mentioned above, a major component of our screening criteria is whether a company's financial statements were recently reviewed. The Division's review goal seeks a review of financial statements at least every three years. The three-year goal is not always met. In Enron Corp.'s case since the Division had looked at Enron Corp.'s financial statements up to the period ended September 30, 1998, this screening criterion was not triggered and would not have been triggered until September 30, 2001. Prior to the time the September 30, 2001 Form 10-Q was due, November 14, 2001, our Division of Enforcement had begun its investigation.

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III. RECOMMENDATION

The proposed response letter and memorandum (see Attachment D) provides the answers to the questions posed by Chairman Tauzin in his January 23 letter and summarized in (1) above.

The documents to be provided under part (1) of our recommendation are responsive to Chairman Tauzin's request for copies of comments on Enron's filings as described above and in his January 23 letter.

We are also seeking authorization to conduct non-public briefings of the Committee and Subcommittee and their staff. While the committees have not requested a briefing at this time, we anticipate that they may have follow-up questions concerning the Division's reviews of all comments on Enron's filings. In addition, the Commission should be aware that the Wall Street Journal reported on January 18, 2002 that the Commission had not reviewed Enron's annual reports "for at least three years". The Journal attributed this information to "people with knowledge of the process." The staff believes that the source of this information may have been Committee staff. To our knowledge, the Committee and Subcommittee and their staff were the only people outside the Commission with whom this information had been shared at that time. The Committee and Subcommittee have been the source of a number of recent press reports concerning Enron.

Notwithstanding this, the staff recommends that the Commission authorize the staff to provide this response and documents. We do so because the information contained in the memorandum will not in our view, interfere with the Commission's investigation or its conduct of its full disclosure program, even if publicly released or leaked to a reporter.

The proposed staff response, a number of the documents to be provided, and the proposed staff briefings all will contain nonpublic information, making Commission authorization necessary because members and employees of the Commission may not divulge nonpublic information without such authorization.²

The proposed response letter indicates that the information being provided contains nonpublic and sensitive information. The letter requests that the Committee not publicly disclose this information without prior consultation with the Commission.

² Rule 3-7 of the Commission's Rules of Conduct, 17 C.F.R. § 220.753-3(b)(7), applies generally to all requests for nonpublic information. Rule 3-7 requires Commission authorization for disclosure for any nonpublic Commission documents, and information contained in such documents, or any confidential Commission information

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ATTACHMENTS:

- (A) December 7, 2001 request from Chairmen Tauzin and Greenwood.
- (B) David Becker's response of December 17, 2001 to the December 7 request.
- (C) January 23, 2002 request from Chairman Tauzin.
- (D) Proposed response of David Becker to January 23 request.