1. The probability of discovery is low enough and the estimated damage too great; therefore we find a way to quietly and quickly reverse, unwind, write down these positions/transactions.
2. The probability of discovery is too great, the estimated damages to the company too great; therefore, we must quantify, develop damage containment plans and disclose.

I firmly believe that the probability of discovery significantly increased with Skilling's shocking departure. Too many people are looking for a smoking gun. . . . There is a veil of secrecy around LJM and Raptor. Employees question our accounting propriety consistently and constantly. This alone is cause for concern. . . . I have heard one manager-level employee from the principal investments group say, "I know it would be devastating to all of us, but I wish we would get caught. We're such a crooked company." . . .[1]

Another group of Enron insiders who were in position and had a responsibility to protect investors from fraud was Enron's Board of Directors, and particularly the Board's audit committee. In theory and in law, the board's primary responsibility is to represent the interests of shareholders. In practice, the board seemed less than vigilant in fulfilling these responsibilities. Enron's board approved of Andrew Fastow's violation of the corporate conflicts of interest prohibition when he negotiated contracts between Enron and the SPEs in which he was heavily invested and from which he profited tremendously. As Benjamin Neuhausen, one of Andersen's Enron accountants, claimed, the "idea of a venture entity managed by CFO is terrible from a business point of view. Conflicts of interest galore. Why would any director in his or her right mind ever approve such a scheme?"

The final line of defense against corporate fraud should be government officials and regulators. Arthur Levitt, chairman of the SEC throughout the 1990s, strongly criticized the dual auditing and consulting activities of the big accounting firms as involving conflicts of interest. Congress ignored his advice, apparently convinced by the lobbying efforts of the accounting profession to allow audit firms to continue working as consultants to the firms they audited.

The federal government was also actively dismantling a wide range of financial regulatory protections during the 1990s. During the first Bush Administration, the federal government deregulated the energy industry, ostensibly to spur economic growth according to free market principles. One of the leading advocates for this deregulation was Wendy Gramm, who at the time was chairwoman of the U.S. Commodity Futures Trading Commission. Gramm's husband is Phil Gramm, then U.S. Senator from Texas and a member of the Senate banking, finance, and budget committees that supported this deregulation. Senator Gramm had received over $100,000 in campaign contributions from Enron during his last two Senate campaigns. When Wendy Gramm left government in 1992, she joined Enron's Board of Directors as a member of their audit committee.

Questions

1. What responsibilities did David Duncan owe to Arthur Andersen? To Enron's management? To Enron's stockholders? To the accounting profession?
2. What are the ethical responsibilities of a corporate attorney, such as Nancy Temple, who works for an "aggressive" client wishing to push the envelope of legality?
3. Under what conditions should an employee such as Sherron Watkins blow the whistle to outside authorities? To whom did she owe loyalty?
4. To whom does the board of directors owe their primary responsibility? Can you think of any law or regulations that would help ensure that boards meet their primary responsibilities?

5. What responsibilities do government regulators owe to business? To the market? To the general public?
6. Are accounting and law professions or businesses? What is the difference?

NOTES

1. From a report released by the U.S. House of Representatives Energy Committee, February 2002.