

Opening Statement of Maureen Hendricks
Before the Senate Permanent Subcommittee on Investigations
July 23, 2002

Thank you Mr. Chairman and Members of the Committee.

My name is Maureen Hendricks. I am currently a Senior Advisory Director at Salomon Smith Barney. I have spent almost three decades as an investment banker covering companies in the energy sector. I began my career in 1973 at Morgan Guaranty Trust – which later became JP Morgan – and then joined Salomon Brothers in 1997 – which then became Salomon Smith Barney. From 1999 until May 2001, I was the head of Salomon Smith Barney’s Energy and Power Group, with responsibility for the Enron account.

As head of that group, I managed Salomon Smith Barney’s investment banking relationship with Enron. As SSB’s lead investment banker on the Enron account, I worked with Enron representatives and SSB product specialists to determine how we could best address Enron’s investment banking needs. In that capacity, I worked with the client on such investment banking projects as raising money in the capital markets or merger and acquisition activity.

As you have no doubt heard quite often, Enron was a significant user of structured finance – which is simply a way of providing cash to a company through means other than traditional bank loans. And far from being faulted for it, at the time Enron was celebrated for its innovative financing techniques. The

structured financings for which Enron was applauded were done exclusively with banks since they have requisite expertise. The general capital markets – such as bond purchasers – prefer simplicity and generally will not purchase highly structured products.

One project that I worked on for Enron, along with others at SSB, was the Yosemite structure, which, in overly simplified terms, was designed as a way for Enron to do structured finance in the capital markets. The Yosemite notes were offered under SEC Rule 144A, which permits them to be sold only to the largest, most sophisticated institutional investors.

As it happened, the structured financing underlying the Yosemite offerings were prepaids. Prepaids are commodity-based structured financings that were widely-used in the energy sector. In fact, they have a very long history.

Production payments, which I structured in the 1970s when I worked in the petroleum group at Morgan, are precursors of the prepaid at issue here today. Production payments were financings that enabled an energy company to “monetize” – that is, extract the expected future cash flow – its future revenues from oil or gas production. The companies received cash upfront from a financing counterparty, in exchange for a promise to repay that amount with future revenues from production. In order to protect themselves from the movement of commodity prices, banks that entered into such financings would secure collateral that exceeded the value of the repayment obligation. As with the prepaids at issue

here, production payments originally had certain accounting advantages over straight loans.

Over the following three decades, structured finance has evolved considerably and is used in many forms by many industries. One evolution was that the market developed more sophisticated ways of limiting, or hedging, the commodity price risk associated with the company's obligation. By using derivatives, a bank could hedge out commodity price much more efficiently, without requiring posting of collateral.

We understood from Enron that Arthur Andersen had fully vetted the accounting treatment for prepaids and that, under the governing accounting rules, prepaids would have advantageous treatment similar to the earlier production payments. Specifically, Enron's obligation on the prepaids would not be recorded as debt (but as a "price risk management liability") and the upfront cash received would not be treated as cash flow from financing, but as cash from operations.

At the time that we structured the Yosemite deals for Enron, I had absolutely no reason to believe that there was anything wrong with prepaids or with Enron's proposed accounting treatment for them. Indeed, it appeared very familiar.

I was among the people responsible for shepherding the Yosemite offering to market. In that connection, I oversaw the due diligence that we conducted of Enron, in close cooperation with our outside counsel. We received

an opinion from Enron's outside counsel and a comfort letter from Enron's auditor. I believe that we asked the company the right questions. I regret to say that it appears from all that has recently been disclosed that we were not provided with the right answers by Enron management. It also appears that the audited financial statements, upon which we relied, were not accurate and did not fairly present Enron's financial condition.

Beyond supervising due diligence, I also was involved in the presentation of the Yosemite offering to the SSB Investment Grade Debt Commitment Committee. This Committee is charged with responsibility for reviewing, evaluating and, if appropriate, approving any transaction in which SSB acts as an underwriter or agent in connection with the sale of newly issued securities. It is the guardian of our reputation and our franchise. In this particular instance, the Commitment Committee conducted a searching evaluation of the Yosemite offering and approved those offerings.

I believe the decision to approve these transaction was an appropriate one, based on the information that had been provided to me and my team. I continue to believe that structured finance – if used by honest companies whose books are reviewed by responsible auditors – serves a valuable function in our nation's economy. However, with the benefit of hindsight and the raft of recent disclosures about Enron and its financial misdeeds, I deeply regret that our firm ever entered into transactions with this company.

Thank you.