Opening Statement of David Bushnell

Before the Senate Permanent Subcommittee on Investigations

July 23, 2002

Mr. Chairman and members of the Committee, thank you for the opportunity to speak to you today.

My name is David Bushnell. I am a Managing Director at Citigroup's Global Corporate & Investment Bank and its head of Global Risk Management, which functions as an independent control over our business units and is responsible for monitoring market and credit risk. In that capacity, my department ensures that risks – including market risk, credit risk, and risks to reputation – are identified, measured, and evaluated by our institution before we commit capital or become a party to any transaction or new type of business. My division establishes and monitors trading and credit limits, and, where appropriate, approves exceptions. In addition, the firm's risk management committees report to me.

Our institution recognizes the importance of the work that this Committee is doing with respect to its examination of Enron's collapse. Enron's failure was a pivotal event for American business. In the space of a few short months, Enron went from an investment grade credit ranked 7th in the Fortune 500 to bankruptcy. Like many other market participants, Citigroup lost money as an Enron lender. More importantly, investors have lost money, employees have lost jobs and the public has lost confidence in our financial markets. The integrity of our markets, and the integrity of our borrowers and their financial statements, is of the utmost importance to us. We therefore commend the Committee's efforts to understand the factors that caused or permitted Enron's stunning collapse, and we encourage changes in accounting or other rules that will protect against what happened here.

During our business relationship with Enron, we thought we were dealing with honest managers who had a legitimate business purpose for the transactions we did with them. We believed that Enron was making good-faith accounting judgments that were reviewed by Arthur Andersen, which was then the world's premier auditing firm in this sector. We believed that the Audit Committee of Enron's Board exercised meaningful supervision over the company's accounting policies and procedures. The facts that are emerging about Enron's business and accounting practices, including the facts that have come to light through the work of this Committee, are very disturbing to us. They no doubt are disturbing to other financial institutions as well, because Enron had similar relationships with most of the large firms on Wall Street.

The emerging facts suggest that Enron was not the company we thought it was. If what has been reported turns out to be the case – large-scale self-dealing, inflated assets, management that was inattentive or worse, a subservient Board, and a failure of auditing controls – we would not have done the business we did with Enron. To the extent that Enron was able to manipulate and abuse good-faith financing efforts, our industry must understand how this happened – and do everything possible to prevent it from ever happening again – so that investor confidence can be restored.

But let me be clear. While we regret our relationship with Enron, we acted in good faith at all times. Our employees, including the bankers who are here today, are honest people doing honest business. They did transactions that were common throughout Wall Street, and they believed those transactions were entirely appropriate.

The focus of this hearing is structured finance, and the accounting rules that apply to the types of structured transactions that Enron used. My colleagues will talk to you about some of the specific financing structures at issue, but I want to emphasize that, like every other institution in this business, we design financing structures for diverse businesses with unique needs against a background of accounting, tax, and legal rules. Some of those accounting rules are complicated and subject to interpretation by accounting experts. If specific rules do not work the way they should, then they should be fixed. Moreover, changes are needed to increase accounting oversight and the reliability of a company's financials. Clear accounting rules rigorously applied by businesses and their auditors are necessary predicates for investor trust. I must stress, however, that we do not dictate our clients' accounting practices. Once we are satisfied that a client's proposed tax and accounting treatment seem reasonable, the accounting judgments are left to the client and its accounting professionals who have access to complete information.

This, I would submit, is as it should be. It has always been the law and accepted practice that companies are permitted to rely on the certified financial statements of the party on the other side of a transaction. Our financial system assumes that all market participants must be able to rely on a company's financial statements and the representations of its outside auditors. The auditors are the experts in understanding the accounting rules – for example the 800 pages of rules that govern accounting for derivative transactions. And the auditors are in possession of detailed information about the company's entire financial picture, not just specific transactions. Recent regulatory initiatives appreciate that responsibility for the accuracy of financial statements must rest with company management and auditors, as evidenced by the recent SEC Rule requiring CEOs and CFOs to certify the accuracy of financial statements, and legislative proposals strengthening the independence and oversight of the auditing function.

At Citigroup, I oversee a sophisticated and comprehensive process for reviewing structured finance transactions. Two of our key approval committees are the Global Commitment Committee and the Capital Markets Approvals Committee (CMAC). The Commitment Committee is responsible for reviewing equity and fixed income securities underwritings. The overall mission of the Commitment Committee is to ensure that we are comfortable selling newly issued securities so that we protect our reputation for high-quality financings and retain investor confidence. To that end, the Commitment Committee meets with the bankers who worked on the transactions, and reviews the issuer's accounting and disclosure statements, among many other factors.

The CMAC reviews structured financing products, among other things. Senior representatives from our market risk, credit risk, legal, accounting, and tax departments (as well as other departments) sit on the CMAC to evaluate proposed transactions from each of these perspectives. The CMAC approves only those transactions that it concludes are appropriate. For example, the Yosemite transactions, about which this Committee has expressed interest, were reviewed and approved by the CMAC.

We pride ourselves on our reputation for being an institution with integrity. If a transaction raises potential accounting, tax, legal, compliance, regulatory, or appropriateness issues for us or our clients – or otherwise exposes us to reputational risk – the CMAC evaluates the risks to ensure that our institution is comfortable in completing the transaction. This is not to say we substitute our judgment for that of our clients, or their tax, accounting, and legal advisors; responsibility for those judgments remains with them.

Thus, when we agreed to structure prepaid transactions for Enron, we relied heavily on its assurances that its outside auditor, Arthur Andersen – which at the time was a market leader – had reviewed these transactions. Enron told us that Andersen believed the proposed accounting treatment for the prepaids – that is, accounting for the cash the transactions generated as cash from operations rather than as cash from financing, and accounting for the resulting obligations as price risk management liabilities rather than as debt – was appropriate. And while I am not an accounting expert (no one on this panel is), this accounting treatment seemed reasonable to the members of the CMAC.

I am sure that the Committee understands that at the time these transactions were done, Arthur Andersen was one of the "Big Five" – a preeminent auditing firm whose word carried weight and gave comfort. Certainly now, with all of the information that has come to light about Arthur Andersen, it is easy to question Andersen's review. And, indeed, the information contained in this Committee's recent report and the related exhibits on Enron's Board is striking for what it reveals about Andersen's own concerns about the overall risk of Enron's accounting methodologies. The report indicates that Arthur Andersen shared its concerns with the Audit Committee of Enron's Board. But we learned about Arthur Andersen's reservations only after the fact. Legitimate questions can and should be asked about whether the three institutions charged with ensuring that Enron's financials were properly stated – Enron's management, auditors, and Board – failed to live up to their obligations to the investing public.

The sobering facts about Enron set forth in this Committee's recent report make clear that much stronger oversight of the accounting profession is needed, and that controls must be put in place to ensure that auditors are truly independent of their clients. The report also suggests that a rule-based accounting system such as American GAAP, which creates narrow pigeonholes for classification, may be too susceptible to abuse. It perhaps should be supplemented by more of a principle-based system. And we would certainly support rules requiring greater management accountability, more stringent Board oversight, and greater Board independence. We welcome debate on these issues. It is essential that we reestablish the trust that is necessary to the efficient functioning of our economy.

Thank you. I look forward to answering your questions.