

COMMENTARY:

## McCain Defends 'Enron Loophole'

by Jason Leopold

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**Chronicle**  
&  
**Sentinel**

**May 19, 2008**—Sen. John McCain says he opposes the \$307 billion farm bill because it would dole out wasteful subsidies, but his chief economic adviser Phil Gramm also wants to stop its proposed regulation of energy futures trading, a market that was famously abused when Enron Corp. manipulated California's electricity prices in 2001.



Clearing the way for that California price gouging, Gramm, as a powerful Texas senator in 2000, slipped an Enron-backed provision into the Commodities Futures Modernization Act that exempted from regulation energy trading on electronic platforms.

Then, over the next year, Enron – with Gramm's wife Wendy serving on its board of directors – worked to create false electricity shortages in California, bilking consumers out of an estimated \$40 billion.

Gramm left the Senate in 2002 but now has emerged as what Fortune magazine calls "[McCain's econ brain](#)," not only filling the Arizona senator's acknowledged void on economic expertise ("I don't know as much about the economy as I should") but recognized as one of McCain's closest friends in politics. The two men talk daily.

A McCain aide told me that the Arizona senator opposes the farm bill because it "rewards lobbyists" by granting rich farmers lucrative subsidies, although he would support "a reasonable level of assistance and risk management to farmers when they need America's help."

But the aide, who spoke on condition of anonymity, acknowledged that the presumptive Republican presidential nominee also opposes the farm bill because Gramm advised McCain that he should resist its regulatory language on the energy futures market.

Democrats have dubbed that gap in energy futures regulation the "Enron loophole," but it played a part, too, in the more recent attempt by the Amaranth Advisers hedge fund to corner the national gas market by shifting trades to the unregulated "dark markets" of the Intercontinental Exchange.

The "Enron loophole" also has become part of the debate over the soaring price of oil. Last week, a study sponsored by Sen. Carl Levin, D-Michigan, concluded that speculative futures markets were partly to blame for the surge in oil prices that have pushed gas at the pump toward \$4 a gallon.

At a May 15 news conference, Levin said the skyrocketing price of oil is "not the result of supply and demand. Speculators have taken over most of the futures market."

However, the 673-page farm bill, containing the regulatory provisions on electronic energy trading, still faces obstacles amid overall concerns about the bill's largesse to farmers at a time of rising food prices.

President George W. Bush has vowed to veto the bill, although it cleared the House and Senate by margins wide enough for an override, assuming Republicans don't rally behind Bush and McCain, their

current and future standard bearers.

## **Gramm and Enron**

The battle over the "Enron loophole" also could draw attention to McCain's dependence on Gramm as his chief economic adviser and Gramm's key role in passing legislation that let Enron trade commodities on electronic platforms without federal oversight.

In 2000, with the Republicans in charge of Congress and Gramm chairing the Senate Banking Committee, the exemption on electronic trading was approved without a Senate hearing.

Internal Enron documents, which were released in 2002, revealed that the Houston-based company helped write the legislation, which was signed into law by President Bill Clinton in December 2000.

Freed from regulatory interference, Enron then used manipulative trading practices to game the California electricity market and drive up electricity prices across the state.

While California consumers were getting fleeced, the new Bush administration shielded Enron from early accusations of market manipulation. President Bush personally joined the fight against imposing caps on the soaring price of electricity, buying additional time for Enron although the company's house of cards collapsed anyway in fall 2001. [For details, see Consortiumnews.com's "[Bush's Enron Lies](#)."] ]

In 2006, the "Enron loophole" allowed Amaranth Advisers hedge fund to shift its trades from the regulated New York Mercantile Exchange (NYMEX) to the unregulated Intercontinental Exchange (ICE) in Atlanta.

That let Amaranth corner the natural gas market, betting that futures prices would rise. The hedge fund lost about \$6 billion and imploded as natural gas prices fell to a two-year low in September 2006.

Last July, the Federal Energy Regulatory Commission and the Commodity Futures Trading Commission charged that Amaranth manipulated prices paid in the physical natural gas markets. FERC has proposed \$291 million in penalties and the forfeiture of "unjust profits."

"Unregulated markets are known as 'dark markets' because there is very little oversight of the trades," said Rep. Bart Stupak, D-Michigan, chairman of the subcommittee on Oversight and Investigations, during a hearing on energy speculation last December.

By trading on the "dark" ICE market, traders can avoid the Commodity Futures Trading Commission's rules which are in place to prevent price distortions or supply squeezes.

Stupak said trading volumes on ICE "have skyrocketed in the past three years and are now as large or even larger in some months, than the volumes traded on the regulated futures market."

The lack of oversight "makes it difficult for regulators to detect excessively large positions which could lead to price manipulation," Stupak said.

## **Advising McCain**

Gramm, who is now a vice chairman of financial services company UBS, began advising McCain in 2005 when the Arizona senator indicated he planned to run for President.

Since then, McCain has adopted much of Gramm's anti-tax, anti-regulatory agenda. Most strikingly, McCain shifted to support Bush's tax cuts, which McCain had voted against in 2001 and 2003. He now vows that, if elected President, he would make them permanent.

Yet Gramm's influence over McCain's economic agenda – and the checkered political-business history of Gramm and his wife Wendy – have largely escaped media scrutiny.

Gramm received more than \$34,000 in campaign contributions from Enron and served as one of the company's key legislative allies in Washington, including his help in 2000 removing federal oversight from energy trades on electronic platforms.

At the height of the Enron scandal in January 2002, Gramm's press secretary Larry Neal told [The New York Times](#) that Gramm did not "recall a conversation" he apparently had with Enron's chairman Ken Lay in 2000 to discuss that Enron legislative priority.

An internal Enron [e-mail dated Aug. 10, 2000](#), under the subject "CFTC Reauthorization" – sent by Enron's top lobbyist Richard Shapiro to Steve Kean, Enron's executive vice president – said the company needed to get Lay on the phone with Gramm so the bill could be passed.

"The bill is not moving quickly in the Senate due to Senator Phil Gramm's desire to see significant changes made to the legislation (not directly related to our energy language)," Shapiro said.

"Last week at the [2000] Republican Convention, I asked the Senator about the bill and he said they were working on it, but much needs to be changed for his support. More telling perhaps, were Wendy Gramm's comments that she would rather the current bill die if a better bill can be passed next year.

"What this means is that we must, at the least, remove Senator Gramm's opposition to the bill to move the process and more importantly seek to gain his support of the legislation."

Shapiro added: "However, with less than 20 or so legislative days left, we need Senator Gramm to engage.

"A call from Ken Lay in the next two weeks to Senator Gramm could be an impetus for Gramm to move his staff to resolve the differences. Gramm needs to fully understand how helpful the bill is to Enron.

"Let me know your thoughts on this approach. I am prepared to assist in coordinating the call and drafting the talking points for a Ken Lay/Sen. Gramm call."

Several other internal Enron e-mails briefed company staffers on the status of Gramm's position and Enron's lobbying of the senator. Gramm finally removed a "hold" on the bill in December 2000, reintroduced the bill under a different number, and forced a vote on it without floor debate.

It was then attached to an appropriations bill that was signed by President Clinton on Dec. 21, 2000.

## **California Crisis**

Less than a month later, California began to experience rolling blackouts due to artificial electricity shortages which, according to documents later released by federal energy regulators, were the result of manipulative trading practices employed by Enron.

The California crisis centered on Enron's energy trades through a new platform called EnronOnline, which had been freed from regulatory oversight by the legislation pushed by Gramm.

In April 2002, Gramm blocked an amendment by Sen. Dianne Feinstein, D-California, that would have closed the loophole that Gramm had helped open.

Gramm's wife, Wendy, also had played a role in the anti-regulatory policies that contributed to the Enron scandal.

On Jan. 14, 1993, in the final days of the first Bush administration, Wendy Gramm – as chairwoman of the Commodity Futures Trading Commission – pushed through a key regulatory exemption removing energy derivatives contracts and interest-rate swaps from federal oversight.

That was a major financial boon to Enron, where Wendy Gramm landed five weeks later as a member of the board of directors. She also became a member of the audit committee that signed off on another one of Enron's fraudulent schemes, partnerships that hid the company's growing debt.

Even after Enron had collapsed in fall 2001, Sen. Gramm continued to resist congressional efforts at tightening up the rules.

In 2002, despite the accounting scandals at Enron, WorldCom and other major companies, Sen. Gramm objected to the Sarbanes-Oxley corporate reform bill designed to hold executives accountable for inaccuracies in financial reports.

Now, the Gramm family's anti-regulatory agenda is returning via McCain's presidential campaign.

As Fortune's editor-at-large Shawn Tully wrote, "economic conservatives should take heart. McCain's chief economic adviser – and perhaps his closest political friend – is the ultimate pure play in free market faith, former Texas Sen. Phil Gramm. ... Most of [McCain's] current positions are vintage Gramm indeed." [[Fortune, Feb. 19, 2008](#)]

The first test of McCain's commitment to Gramm's anti-regulatory purity may come in the looming battle over the "Enron loophole" that the farm bill seeks to close.

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