Enron's Skilling Contends Hedges Didn't Hide Losses (Update3)

April 12 (Bloomberg) -- Enron Corp. didn't use off-the-books partnerships to hide losses, former Chief Executive Officer Jeffrey Skilling testified today, seeking to counter the government's charges that he conspired to defraud investors.

Skilling said hedges set up through the partnerships were created to protect investment profits rather than manipulate the company's earnings. He's on the witness stand for a third day defending himself from accusations that could earn him and former Chairman Kenneth Lay prison terms of at least 25 years.

``This was about protecting gains, not hiding losses,'' Skilling told jurors in federal court in Houston. Prosecutors are expected to begin cross-examining him next week.

The government contends Lay, 63, and Skilling, 52, conspired to use the partnerships created by former Enron Chief Financial Officer Andrew Fastow to hide debts and losses to deceive investors.

Fastow, who pleaded guilty to fraud in connection with some of those deals and faces 10 years in prison, testified that Skilling agreed to use the partnerships to hide troubled assets and generate earnings to meet quarterly targets.

Lay's and Skilling's lawyers counter their clients were deceived by unscrupulous subordinates such as Fastow. The defense contends the former finance chief stole at least $25 million from Enron in connection with several partnership deals.

Normal Business

The defense also hopes to persuade jurors no fraud occurred at Enron and that the government seeks to criminalize normal business practices. They contend prosecutors used threats of lengthy prison terms to strong-arm former Enron executives into pleading guilty and testifying against Skilling and Lay.

One of those executives, former Treasurer Ben Glisan, told jurors three weeks ago that Skilling and Lay approved the so- called Raptor hedges to hide losses from the company's auditors and investors.

Enron officials used the company's stock and cash from Fastow's LJM partnerships to set up the hedges. Fastow's partnerships then got back their investment in the entities plus profit and Enron used the vehicles to insure against future investment losses. The company also used the Raptors to create inflated valuations for hedged assets to generate earnings, prosecutors allege.

Glisan said Skilling told Enron's board he liked the hedging strategy because it allowed the company ``to circumvent accounting rules.'' Under cross-examination, Glisan said while he couldn't be sure Skilling used those exact words, ``the only reason to do it was for an accounting benefit.''

Glisan Disputed

During his testimony today, Skilling said the hedges were created to limit ``volatility'' from investments in high-tech companies. He disputed Glisan's recollections of his statements about their advantages.

``Mr. Glisan says you thought this was a good idea because you could circumvent accounting rules,'' Daniel Petrocelli, one of Skilling's defense lawyers, said. ``That's not true,'' the former CEO responded.

Skilling said Arthur Andersen LLP, Enron's auditor, signed off on the hedges and no one ever alerted him to problems with the entities' structures.

Skilling's testimony is designed to buttress the defense's contention he and Lay relied on the expertise of lawyers and accountants who approved the structures of the hedges and Fastow's partnerships. They'll argue jurors shouldn't convict the pair for relying on that advice.

Fastow testified Skilling urged him to use the partnership to help ``juice'' the company's earnings and personally guaranteed Fastow's partnerships wouldn't lose money in some company-related deals.

`Good Team'

Skilling said today it was Fastow who asked for profit guarantees that his LJM partnerships, named for his wife and children, wouldn't lose money on Enron's 1999 sale of its interest in a Brazilian power plant.

``I declined'' to give those guarantees, Skilling told jurors.

Skilling also told jurors he and Lay ``made a good team'' as Enron's top executives and they didn't conspire to defraud investors.

``Did you and Ken Lay ever enter an agreement to do illegal things together?'' Petrocelli asked. Skilling said they didn't.

Skilling also disputed earlier testimony by David Delainey, ex-head of Enron's energy-trading unit, that Enron rolled its loss-plagued retail energy division into its cash-flush trading operation in early 2000 in order to hide losses.

Delainey said Skilling lied when he told analysts the combination was done for ``efficiency.''

`Silly'

During today's testimony, Skilling said it was ``silly'' to have duplicate power-trading functions in Enron's retail and wholesale energy units. The subsidiaries wound up competing against each other, he noted. Having one trading desk for both operations made the most sense, Skilling said.

Although Delainey testified he told Skilling hiding the retail unit's losses among trading profits ``lacked integrity,'' Skilling said today Delainey supported the idea.

``I asked Mr. Delainey, `Do you want to do this, are you sure you want to do this?''' Skilling said. ``And he said yes.''

Skilling also took issue with Delainey's testimony that Enron improperly boosted its second quarter 2000 earnings by tapping into almost $1 billion of ``cookie jar'' reserves generated by the California power crisis.

``We had always been aware of the need to specify reserves for specific purposes,'' Skilling said to rebut Delainey's contention. ``There were no cookie jar reserves at Enron.''

`Kiss Kiss'

Skilling noted that Enron maintained reserve accounts for specific circumstances and he was pleased when Delainey re- instituted one such account.

``I was thrilled because I was uncomfortable when I heard we'd done away with the account,'' Skilling testified. ``I may have kissed him.''

``It was not a kiss kiss,'' Skilling hastened to add, as laughter broke out in the courtroom. ``I was happy.''

The case is U.S. v. Skilling, 04-cr-25, U.S. District Court, Southern District of Texas (Houston).

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