Statement of Congressman Ron Paul House Financial Services Committee, Capital Markets Subcommittee Monday, February 4, 2002

Mr. Chairman, the collapse of Enron has so far been the cause of numerous hearings, as well as calls for increased federal control over the financial markets and the accounting profession. For example, legislation has been introduced to force all publicly traded companies to submit to federal audits.

I fear that many of my well-meaning colleagues are reacting to media reports portraying Enron as a reckless company whose problems stemmed from a lack of federal oversight. It is a mistake for Congress to view the Enron collapse as a justification for more government regulation. Publicly held corporations already comply with massive amounts of SEC regulations, including the filing of quarterly reports that disclose minute details of assets and liabilities. If these disclosure rules failed to protect Enron investors, will more red tape really solve anything? The real problem with SEC rules is that they give investors a false sense of security, a sense that the government is protecting them from dangerous investments.

In truth, investing carries risk, and it is not the role of the federal government to bail out every investor who loses money. In a true free market, investors are responsible for their own decisions, good or bad. This responsibility leads them to vigorously analyze companies before they invest, using independent financial analysts. In our heavily regulated economy, however, investors and analysts equate SEC compliance with reputability. The more we look to the government to protect us from investment mistakes, the less competition there is for truly independent evaluations of investment risk.

The SEC, like all government agencies, is not immune from political influence or conflicts of interest. In fact, the new SEC chief used to represent the very accounting companies now under SEC scrutiny. If anything, the Enron failure should teach us to place less trust in the SEC. Yet many in Congress and the media characterize Enron's bankruptcy as an example of unbridled capitalism gone wrong. Few in Congress seem to understand how the Federal Reserve system artificially inflates stock prices and causes financial bubbles. Yet what other explanation can there be when a company goes from a market value of more than $75 billion to virtually nothing in just a few months? The obvious truth is that Enron was never really worth anything near $75 billion, but the media focuses only on the possibility of deceptive practices by management, ignoring the primary cause of stock overvaluation: Fed expansion of money and credit.

The Fed consistently increased the money supply (by printing dollars) throughout the 1990s, while simultaneously lowering interest rates. When dollars are plentiful, and interest rates are artificially low, the cost of borrowing becomes cheap. This is why so many Americans are more deeply in debt than ever before. This easy credit environment made it possible for Enron to secure hundreds of millions in uncollateralized loans, loans that now cannot be repaid. The cost of borrowing money, like the cost of everything else, should be established by the free market- not by government edict. Unfortunately, however, the trend toward overvaluation will continue until the Fed stops creating money out of thin air and stops keeping interest rates artificially low. Until then, every investor should understand how Fed manipulations affect the true value of any company and the level of the markets.

Therefore, if Congress wishes to avoid future bankruptcies like Enron, the best thing it can do is repeal existing regulations which give investors a false sense of security and reform the country's monetary policy to end the Fed-generated boom-and-bust cycle. Congress should also repeal those programs which provide taxpayer subsidies to large, politically-powerful corporations such as Enron.

Enron provides a perfect example of the dangers of corporate subsidies. The company was (and is) one of the biggest beneficiaries of Export-Import Bank subsidies. The Ex-Im bank, a program that Congress continues to fund with tax dollars taken from hard-working Americans, essentially makes risky loans to foreign governments and businesses for projects involving American companies. The Bank, which purports to help developing nations, really acts as a naked subsidy for certain politically-favored American corporations- especially corporations like Enron that lobbied hard and gave huge amounts of cash to both political parties. Its reward was more that $600 million in cash via six different Ex-Im financed projects.

One such project, a power plant in India, played a big part in Enron's demise. The company had trouble selling the power to local officials, adding to its huge $618 million loss for the third quarter of 2001. Former president Clinton worked hard to secure the India deal for Enron in the mid-90s; not surprisingly, his 1996 campaign received $100,000 from the company. Yet the media makes no mention of this favoritism. Clinton may claim he was "protecting" tax dollars, but those tax dollars should never have been sent to India in the first place.

Enron similarly benefited from another federal boondoggle, the Overseas Private Investment Corporation. OPIC operates much like the Ex-Im Bank, providing taxpayer-funded loan guarantees for overseas projects, often in countries with shaky governments and economies. An OPIC spokesman claims the organization paid more than one billion dollars for 12 projects involving Enron, dollars that now may never be repaid. Once again, corporate welfare benefits certain interests at the expense of taxpayers. The point is that Enron was intimately involved with the federal government. While most of my colleagues are busy devising ways to "save" investors with more government, we should be viewing the Enron mess as an argument for *less* government. It is precisely because government is so big and so thoroughly involved in every aspect of business that Enron felt the need to seek influence through campaign money. It is precisely because corporate welfare is so extensive that Enron cozied up to DC-based politicians of both parties. It's a game every big corporation plays in our heavily regulated economy, because they must when the government, rather than the marketplace, distributes the spoils.

This does not mean Enron is to be excused. There seems to be little question that executives at Enron deceived employees and investors, and any fraudulent conduct should of course be fully prosecuted. However, Mr. Chairman, I hope we will not allow criminal fraud in one company, which constitutionally is a matter for state law, to justify the imposition of burdensome new accounting and stock regulations. Instead, we should focus on repealing those monetary and fiscal policies that distort the market and allow the politically powerful to enrich themselves at the expense of the American taxpayer.