

trades for illegitimate purposes would be inclined to use methods that did not create a single electronic record of both transactions. The alternatives might include direct bilateral negotiation of both trades by telephone, or completion of one leg by telephone or an alternate electronic platform while completing the other leg on EOL. Our definition of wash trading considers trades that occurred within the same product, at the same price, in the same volume, and at nearly the same time (within 2 minutes of one another).

It should be recognized that a company might enter an offsetting pair of trades on EOL for legitimate business purposes. For example, a company anticipating unseasonably warm weather might purchase a quantity of power, only to resell it later as actual weather conditions are milder. Therefore, it is possible that this report includes some “false positives”—paired trades that appear to be inappropriate wash trades but were not. However, given the facts in the specific examples of wash trading described herein, we believe the manipulative nature of these examples is obvious.

Choice Markets

EOL market makers are traders assigned to always quote both a bid price and an offer price, representing Enron’s willingness to always buy or sell gas during market hours. Our data analysis and interviews with market makers indicate that they sometimes elected to set the bid-offer spread to zero, which they referred to as making a “choice market.” Choice markets may, in effect, have been an invitation to EOL customers to engage in wash trading. The raw data used in our analysis do not include bid and ask quotes, so it is not possible to directly identify periods of choice (zero spread) markets. However, Staff identified all sequences of trades that occurred during likely choice markets based on the following criteria: (1) all trades in the sequence occurred at identical prices, (2) at least one trade in the sequence was an EOL buy and at least one was an EOL sell, (3) the sequence contained at least four trades, and (4) all trades in the sequence are for the same product at the same volume.

Tables VII-1 and VII-2 provide information about EOL trading activity during choice market periods. Table VII-1 reports activity by calendar month, revealing that choice market trading on EOL increased steadily over time. In fact, 45 percent of all choice market trading in gas products and 54 percent of all choice market trading in electricity markets occurred during the last 3 months (September to November 2001) of the 21-month sample. These 3 months coincide with the period of time leading up to Enron’s filing for bankruptcy.