The Jamie Olis Case

An Investigation-in Progress by Roger Donway

(The following represents a current summary of my research into the Jamie Olis case. While I believe that this account is both true and fair, my investigation of the case is on-going and further research may change my understanding and evaluation of certain aspects of the case.—RD)

On March 25, 2004, Jamie Olis was sentenced in Houston, Texas, to more than 24 years in prison—with no possibility of parole. He was not a rapist, or a murderer, or a sleeper terrorist who had plotted to kill thousands. His sentence would likely have been lighter if he had been. Olis’s crime was just this: For three years he had worked diligently as a middling tax lawyer at a middling energy company—and he happened to work at the time of the great Houston rich-hunt.

Following the collapse of Enron in December 2001, the city of Houston became the center for prosecutions of executives in the oil and gas industry. Men and women—innocent and guilty—were paraded before howling mobs and dragged into prejudiced courts, with no effort to determine whether they were con artists or wheeler-dealers, whether they had schemed to commit frauds or had merely run afoul of convoluted securities regulations. Prosecutors, politicians, and the press—flouting their own codes of conduct—ignored all such distinctions and whipped up mass hysteria against the suspects, denouncing them as barely human creatures who had conspired in secret to ruin ordinary people, in order to slake an insatiable lust for wealth. Someday, I have no doubt, historians will write about Houston’s twenty-first century “rich-hunt” trials as they now write about Salem’s seventeenth-century witch-hunt trials. And when they do, I feel sure, they will say that the single most egregious persecution of all was the first of the post-Enron prosecutions: the one conducted against Jamie Olis.

Olis and Dynegy

Jamie Olis was born in 1966, in South Korea, to a Korean mother and an American soldier who abandoned his wife even before Jamie was born. When Jamie was five, the family immigrated to Texas, but with little improvement in Jamie’s life. His mother, Ok Cha Hwang, became involved with an abusive man, and Jamie was packed off to a series of foster homes. Finally, in 1975, Jamie’s mother married Bill Olis, an army sergeant who proceeded to adopt her children and began to tutor Jamie. Soon, Jamie was attending high school in Killeen, Texas, the home of Fort Hood, approximately 150 southwest of Dallas. Graduating fifth in his class, Jamie won a full scholarship to St. Mary’s University in San Antonio. There, he became a certified public accountant and married his college sweetheart, Monica. After graduating, the two moved to Houston, where Jamie earned a law degree.

In 1998, Jamie Olis joined Dynegy, a Houston-based energy company, as the senior director of tax planning, at a salary of $110,000. Above him were Gene Foster, the vice president
in charge of the tax department; chief financial officer Richard Doty; and long-time chief executive officer Chuck Watson. Eventually, Olis would acquire the title of vice president for tax planning, with a salary of $162,000 and a bonus of $110,000, although he also made a couple hundred thousand dollars from stock options. This ordinary remuneration, as we shall see, was the entire basis for the claiming that Jamie Olis “profited” from his supposed crime: He did his mid-level job as best he could and he got paid for it. There was no allegation that he had received suitcases of money under the table. There was no suggestion that he had set up some sweetheart deal for himself. Because he was paid to do his job and because one of the innumerable tasks assigned to him was later declared part of a corporate “fraud,” the prosecution portrayed Olis as the venal profiteer of fraudulent undertakings.

Arthur Andersen’s Tax Plan

Early in 2000, Dynegy’s outside accounting firm Arthur Andersen, sent four employees (Ted McElroy, Kelvin Kelm, and Sean Muller from the firm’s Houston tax department; plus Keith Kechik from the Chicago tax department) to sell Dynegy on a tax-reduction proposal. At a meeting with CFO Doty, vice-president for taxes Gene Foster, and Jamie Olis (then senior director for tax planning under Foster), Andersen suggested something that it called a Commodity Basis Enhancement Strategy (CBES).

The project involved another Andersen client, Integrated Capital Associates (ICA), which had losses it wished to erase. The plan was for Dynegy and ICA to form a five-year partnership that would buy natural gas at a discount during the first year and sell it on the spot market. The profits would accrue to ICA, offsetting its losses. During the next four years, the partnership would buy natural gas at a premium and sell it on the spot market, yielding losses that would accrue to Dynegy and that it could deduct for tax purposes, reaping a $79 million in tax savings. ICA would earn $15.7 million from the deal, and Arthur Andersen would get about half of the sum, $7.8 million, if the deal were successfully completed.

Of course, for the arrangement to work, the Dynegy/ICA partnership would have to have a counterparty who would agree to sell the natural gas at a discount in the first year and then at a premium in the remaining four years. But that was no problem. The loss incurred by selling gas at discount in the first year would be balanced (and a bit more) by the gain from selling the gas at a premium in the remaining four years.

In April of 2000, however, Dynegy broke off these discussions because an article by a leading tax-newsletter writer (Lee Shepard) was critical of such arrangements, and critical articles by Shepard had in the past resulted in the IRS’s disallowing the arrangements he criticized.

Citibank’s “Prepaid” Gas Contract

At about the same time as they were meeting with Andersen’s representatives (that is, early in 2000), executives at Dynegy were concerned that the company’s cash flow was receiving criticism from some people in the investment community and the business media. The problem arose from the nature of the firm’s business, and particularly from those risk-management activities by which the firm attempted to secure future supplies at reasonable prices. To take an example: A natural gas company (like Dynegy) might enter into a contract to buy natural gas at a certain price ten years in the future. But mark-to-market accounting rules required the company to
estimate, at the end of each quarter, the current fair market value of that long-term contract. As the price of natural gas rose or fell, therefore, the company would use a proprietary mathematical formula for calculating the effect of the change on the long-term contract’s current value. Any rise or fall in the value would then be added to or subtracted from the company’s net earnings for the quarter. Of course, when these unrealized gains were being booked as earnings, there was no actual cash coming in from the deal, and uncertainty over how much these projected gains were contributing to reported earnings made investors nervous. Some companies—and Dynegy was one—disclosed each quarter how much they were adjusting their cash flow statements to reflect the unrealized gains that were being booked as earnings. But knowing the facts was not necessarily comforting. It might be that unrealized gains, calculated who-knew-how, were a very large part of reported earnings.

All of these concerns were brought before the public, and thus multiplied many fold by a Wall Street Journal story of September 20, 2000: “Energy Traders Cite Gains, But Some Math Is Missing.” Reporter Jonathan Weil, after laying out the logic of the problem, focused in on Dynegy (precisely because its records were transparent) and wrote: “For all of 1999, Dynegy recorded $115 million in unrealized gains, accounting for 51% of its earnings.”

During the summer, Citibank’s Patrick Boultinghouse discussed a plan for a prepaid gas contract that would help Dynegy meet its disconnect between cash-flow and earnings. The idea was that Dynegy would be paid now to deliver gas in the future, an arrangement that would obviously improve its current cash flow. Sitting in on this meeting were CFO Doty, Rich Gould (Dynegy’s Director of Finance), and Helen Sharkey (an accountant who worked for Controller Mike Mott). The Dynegy people were clearly interested but wondered if Citibank’s prepaid gas contract could somehow be merged with Andersen’s CBES, so that the firm could get both cash-flow benefits and the tax benefits. At a further meeting (with representatives of Arthur Andersen participating by phone), Citibank was represented by Boultinghouse and his colleague Steve Wagman; Dynegy by Finance Director Rich Gould, Vice President of the Tax Department Gene Foster, and by Foster’s subordinate for the last two years, Jamie Olis. At the end of the meeting, Citibank approved the plan in principle.

Project Alpha

For the rest of 2000, Arthur Andersen, Dynegy, Integrated Capital Associates, Citibank, other banks (including Credit Suisse and Deutsche Bank), as well as outside lawyers representing the various parties, struggled to arrange the details of this complex plan. Somewhere along the line, Gene Foster gave the whole muddle a name, Project Alpha, in the expectation that it might be the first of several such programs. During the next six months, it seemed that everything about the project was changing—except for its tendency to get ever more complex. Ultimate authority over the project rested with CFO Doty, but Gene Foster viewed himself as the coordinator of the effort. During a month of intense negotiations in New York City, with the participants working fourteen-hour days, the deal finally came together and it was signed on April 10, 2001.

According to the agreement, a special purpose entity (SPE) called ABG Gas Supply would be set up to buy gas at market prices and sell it to a Dynegy-ICA partnership (DMT Supply) at a discount for nine months (the remainder of Dynegy’s reporting year). DMT would

then sell the gas on the spot market. For the following 51 months, ABG Gas Supply would buy
gas at market prices and sell it at a premium to DMT, which would then sell it on the spot mar-
ket. Under mark-to-market accounting, the deal was a wash and so would not affect Dynegy’s
earnings. But it would give Dynegy a positive $300,000,000 boost in cash-flow over the first
nine months. (The negative $300,000,000 cash-flow being spread over the following 51 months
apparently did not worry the company as much.) Then there was the tax angle. The profits of the
first nine months would be attributed to ICA, thus offsetting its large losses. The losses over the
following 51 months would be attributed to Dynegy, thus giving it a $79 million tax break.

All of this may sound so complex as to be suspicious, but it was not from any of the ar-
rangements described above that trouble arose for Project Alpha. And that is an important point
to keep in mind. People who are only vaguely aware of the Jamie Olis case often assume that
Dynegy’s arrangement to buy gas first at a discount and later at a premium, so as to improve Dy-
negy’s present cash flow without affecting earnings, was somehow wrong. But it was not. In-
deed, the specified non-tax purpose of the deal was precisely stated to be improving Dynegy’s
cash flow, which was a legitimate purpose under IRS and SEC rules.

The wrinkle that caused problems for Project Alpha was this: According to SEC rules, an
SPE is “independent” of a parent company only if some outsider has at least 3 percent of equity
or risk capital in it. The banks were willing to put up the money for ABG Gas Supply to conduct
its commodity trading, but they were not willing to put up risk capital. Banks did not engage in
commodity speculation; that was simply not their business. But if the banks’ money was not at
risk, then it would be merely a loan to ABG Gas Supply; the SPE would not be an independent
corporation; and the deal would not “work,” in accounting jargon.

The answer that the negotiators came up with was to create another SPE: ABG Gas Hold-
ing, which would be the owner of ABG Gas Supply. The banks’ would invest money in second
SPE, which was not itself speculating in commodities, and ABG Holding would hedge the banks’
investment by means of a swap. [Au: Be more specific.] (A swap is an exchange of streams of
payment over time. In this case, ABG Holding agreed to pay the banks a fixed stream of money,
based on their holding in ABG Supply, in return for the amount of money the banks received as
investors in ABG Supply.) Citibank also wanted to protect its investments in ABG Gas Supply
and DMT Supply, and the parties’ external counsel suggested the use of tear-up agreements,
which are hedges of hedges. If something went wrong with its swaps, Citibank would have the
right to “tear up” the swap and negotiate a new one.

The only problem with the deal as thus structured was that Arthur Andersen’s on-scene
representative (James Hecker) said that, despite the distance created by ABG Gas Holding, the
swaps and the tear-ups make the deal look like a loan to him. People, then and later, disagreed
with Hecker, and he admitted that the question was a difficult one, but he would not budge. One
of Dynegy’s lawyers said to his team, sotto voce, that other representatives of the Arthur Ander-
sen accounting firm had allowed other companies to use tear-ups. But Hecker balked. Fatefully,
the contract was signed without the hedges and tear-ups, and Hecker gave it Andersen’s okay.
Then the tear-ups were added back, through amendments that were not shown to Hecker.
Project Alpha was completed on April 10, 2001, and Dynegy’s quarterly reports during the next nine months reflected its effects, namely, an improved cash flow. Ironically, the market did not respond to this carefully contrived good news, and at two points during late 2001 the price actually dropped. When the company issued its annual report the following year, showing increased cash-flow, its stock declined.

Enter the Wall Street Journal

In April 2002, the anticapitalist news department of the Wall Street Journal was following up its crusade against Enron by investigating other energy companies’ use of special-purpose entities. Of course, SPEs were entirely valid corporate structures. But they were so thoroughly hedged about with arbitrary accounting rules that they tended to become unintelligibly complex and every attempt to set one up made it look like those involved were gaming the system. In fact, the rules were so arbitrary that there was no such thing as not gaming the system. Why should 3 percent make an SPE an independent entity? Why not 1 percent? Why not 50? As a result of this arbitrariness and gaming, all attempts to structure SPEs sounded to the press and public to be inherently sneaky. And of course an SPE lay at the heart of Dynegy’s Project Alpha.

On April 3, 2002, the Wall Street Journal’s news department published an article that screamed exposé from the start: “Dynegy Addressed Cash-Flow Fears With Complex Accounting Tactics.” By the headline alone, the accused firm had two strikes against it. First, there was guilt by association. Dynegy was a Houston-based energy company, like the now-bankrupt Enron. In fact, just four months earlier, Dynegy had been prominently in the news for its attempt to play the white knight for Enron at the very end, via a proposed merger. Secondly and relatedly, to Journal readers the words “complex accounting” now meant only one thing: Enron-like.

The set-up of the headline was neatly cashed in with the article’s opening. The reporters (Jathon Sapsford and Paul Beckett) found a quotation in which Dynegy CEO Chuck Watson compared his company to Enron and said that Dynegy always made sure “its numbers are real.” The next paragraph began: “But. . . .” And the two reporters then launched into their long recital of innuendos.

Energy traders, they explained, must assign a current value to contracts that will be exercised in the future. Dynegy, they said, used “highly subjective estimates.” As the value of Dynegy’s contracts soared, “cash flow from operations wasn’t keeping up.” “Eventually,” the reporters fantasized, some analysts “might” decide that the worth of Dynegy’s contracts were less than projected. In sum, the typical Journal reader’s impression at this point would likely be: “Dynegy is lying about the value of its contracts. And they are afraid low cash-flow will expose their lies.”

To solve their problem, the story said, Dynegy executives have created Project Alpha, which uses “bold” accounting. Worse still: “Independent accounting experts say they see little business justification for the Alpha transaction apart from improving the appearance of the company’s books and lowering its taxes.” Of course, improving near-term cash-flow was, precisely and admittedly, the non-tax object of the arrangement. Call that “improving the appearance” of the company’s books if you like. But Dynegy’s executives had excellent business reasons for wanting to achieve it: They needed to calm the storm stirred up by the Journal’s last anti-Dynegy piece.
In one last twist of the knife, the Journal reporters asserted: “The Internal Revenue Service generally disapproves of transactions designed to reduce taxes with no separate business or economic purpose.” What the reporters did not say is, first, that is an IRS attitude, not the law. And second, more importantly: Project Alpha had a business purpose apart from tax reduction—improving cash flow.

Technically, Sapsford and Beckett had made no charge that the company had done anything wrong. But on the day that the story appeared, the company’s stock closed down 4.3 percent. Analysts were much less impressed by the Journal’s attack. According to a story that ran the next day in the Houston Chronicle, “John Olson, an energy analyst with Sanders Morris Harris in Houston and an outspoken critic of accounting irregularities at Enron Corp., said he didn’t plan to change his forecast for the company. ‘It [Project Alpha] has some aspects that are unconventional,’ Olson said. ‘But the way it’s being written about in this post-Enron environment gives it higher sensitivity than it deserves.’”

Unfortunately, investment analysts who shrugged off the Journal’s exposé failed to reckon with the power of the media-regulatory complex. Stung by its failure to detect flaws at Enron, the SEC dared not ignore any media warnings from the ferociously anticapitalist news pages of the Wall Street Journal. And so, on April 25, 2002, the Journal was able to report that the SEC was “looking into” Dynegy’s Project Alpha and that the company’s stock had fallen by 30 percent as a result of the announcement. Moody’s, in response, had placed Dynegy on review for possible downgrade.

Early in May, the SEC elevated its inquiry to a formal investigation, and on May 28, Dynegy’s legendary founder and CEO, Chuck Watson was forced to resign. Three weeks later, CFO Richard Doty was ousted, and there was no one left at Dynegy with any motive to defend Project Alpha or those who had assembled it.

**The Disgruntled Informant**

In the course of their initial story, WSJ reporters Sapsford and Beckett had referred to “internal, undated Dynegy documents.” Obviously, something more was at work than mere enterprise journalism. Sapsford and Beckett were relying on a Dynegy informer who was seeking money and revenge: Ted Beatty.

At the beginning 2002, Ted Beatty had been a management trainee at Dynegy, receiving a handsome salary of $84,000. But in February, after failing to get promoted to the $100,000-a-year post he coveted, Beatty resigned. And with him, he took documents relating to Project Alpha. Apparently, when Beatty had first run across these documents, they were beyond his understanding (no wonder: everyone agrees the arrangement was immensely complex). Now unemployed, with no outside source of income, and having recently gone through bankruptcy, Beatty tried to profit from his pilfering.

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2 Tom Fowler, “Dynegy’s shares rocked by deal, but analysts not,” Houston Chronicle, April 4, 2002.
He began by relating his suspicions to a friend, Jack Pitts, who worked at a New York hedge fund, Steadfast Capital, which had recently begun shorting Dynegy. At the end of February, Pitts emailed Beatty that any news of possibly suspicious accounting at Dynegy would send the company’s stock plummeting. Simultaneously, Pitts wrote to his colleagues at Steadfast: “I think my friend Ted can really help us on Dynegy.” At one point, it seems, Pitts (jokingly or not) told Beatty that he would be famous when his news broke, and might make the cover of Time magazine. (In fact, Time’s “Person of the Year” in 2002 was “The Whistleblowers,” but Beatty was not mentioned, and the cover featured only women.) Beatty alleges that Steadfast promised to hire him as a consultant. But Steadfast, which admits to having made money shorting Dynegy, denies it.

Beatty and his wife, in an attempt to profit from his stolen goods, then bought $8,000 worth of Dynegy puts in her name, knowing that they would make money if the stock fell as they expected. Very soon, however, suspecting that they were violating insider-trading laws, Mrs. Beatty sold the options—at a loss of $2,400, because the stock had actually risen. In the meantime, Beatty had begun contacting newspapers, looking to get paid for his information. Told that respectable newspapers do not pay for information, he finally agreed to talk anyway, and the Wall Street Journal’s April 3, 2002, story was the result. Yet it had no tremendous effect on the company’s stock.

Steadfast Capital did try to help Beatty, by putting him in touch with a Steadfast investor named John Stout. As Stout remembered the conversation, he agreed to put Beatty in touch with a lawyer who would help him deal with the numerous legal claims that Dynegy obviously had against him for his behavior. But the lawyer (Randall Steinmeyer of Milberg Weiss) was less interested in Beatty than in his documents. And once he had them, Milberg Weiss—a notorious member of the plaintiff’s bar—filed a shareholder lawsuit against Dynegy. According to Beatty, Steinmeyer told him that Milberg Weiss would need to hire him as a consultant during the long course of the lawsuit and that Beatty would “end up making more money than he [Steinmeyer] did.” Steinmeyer denies saying any such thing. By the time Beatty last recounted his tale, Milberg Weiss had paid him $9,250.

**The Persecution Begins**

In May 2002, Chuck Watson, Dynegy CEO for 17 years, was forced to resign. In June, CFO Doty was ousted. In September, the SEC filed a securities fraud case against Dynegy, and the company, without admitting guilt, agreed to restate the cash-flow improvement that it had reaped as a result of Alpha, and to pay a middling $3 million fine. (In April 2002, the SEC had fined Xerox $10 million for accounting tricks that misstated earnings.) In October, Dynegy exited the energy-trading business, and Watson’s successor as CEO was eased out. By the end of November, Dynegy shares had dropped from $30 prior to the WSJ story to about $1. [Au: Check.] At last, the short-sellers tipped off by Beatty had made their killing.

In February 2003, Dynegy fired Foster, Olis, and Sharkey. On June 10, 2003, the U.S. Attorney in Houston, Michael T. Shelby, had the three arrested. Shelby had been appointed in December 2001, on the recommendation of Texas senator Kay Bailey Hutchinson. He had always been a prosecutor, moving from assistant D.A. of Harris County, Texas; to assistant U.S. attorney in Houston; to assistant U.S. Attorney in Phoenix; and then to the top job back in Hou-
ston. When Enron collapsed in December 2001, Shelby would normally have taken the lead role in prosecuting any crimes involved, but he had to recuse himself because his brother-in-law was an Enron lawyer. Given the national press’s over-the-top portrayal of Dynegy and CEO Chuck Watson as the corporate good guys, so different from the shysters of Enron, one cannot help but wonder if the contrast prompted a vindictive reaction in Shelby.

In any case, the indictment against Foster, Olis, and Sharkey contained six counts: one count of conspiracy to commit mail and wire fraud; one count of securities fraud; another count of mail fraud based on sending Arthur Andersen’s opinion to David R. Roth, the Vice President and Assistant General Counsel of Dynegy; and three additional counts of wire fraud based on material transmitted to the SEC, namely, the quarterly reports for the second and third quarter of 2001 and the annual report for 2001. On June 20, Olis hired attorney Terry Yates.

The vast majority of the facts alleged against the defendants by the government are stated in the first count and then merely referred to in the remaining counts. Paragraph 12 of the first count sets up the motive for the conspiracy, namely, the WSJ article of September 20, 2000. There then follows Part B. of count 1, entitled “The Conspiracy.” In its first paragraph (Paragraph 13), “The Conspiracy” simply alleges the existence of a conspiracy in the necessary legal language of the relevant statute. For example, sub-paragraph (a) says that the conspirators did “knowingly devise and intend to devise a scheme and artifice to defraud, and for obtaining money by means of false and fraudulent pretenses, representations, and promises, and to knowingly use and cause to be used the United States mails and private and commercial interstate carriers for the purpose of executing the scheme and artifice to defraud in violation of U.S.C. § 1341.”

Paragraph 14 then says: “The Defendants, and their coconspirators and agents, would and did interpret the above mentioned Wall Street Journal article as identifying a serious and increasing ‘gap’ or ‘disconnet’ between Dynegy’s earnings and its cash flows from energy trading, or ‘risk-management,’ activities. The Defendants, and their coconspirators and agents, decided to respond to and fend off the Wall Street Journal’s criticism by improving the ‘risk-management activities’ line of the ‘cash flows from operating activities’ section of the cash flow statement in Dynegy’s quarterly (Forms 10-Q) and annual (Form 10-K) reports filed with the SEC. Dynegy’s cash flows from risk-management activities line had been consistently negative in previous reporting periods. This approach in responding to the Wall Street Journal article was referred to as a way to better ‘match’ cash flow to earnings.”

Paragraph 15 of the indictment gets to the heart of conspiracy: “To better ‘match’ Dynegy’s earnings and operating cash flows, the Defendants, and their coconspirators and agents, would and did conceive, design and execute a plan to borrow money: that is, to engage in a ‘financing activity’ but make it appear that the borrowed funds were cash flow from Dynegy’s ‘risk-management activities’ to create the false impression and illusion that Dynegy’s cash flows from risk management activities were much improved and that its earnings were of sufficient quality to justify, maintain and increase Dynegy’s stock price, and to avoid the potentially adverse effect of a downgrade of Dynegy’s credit rating.”

Paragraph 16 declares: “The Defendants, and their coconspirators and agents, called the plan ‘Project Alpha.’” Paragraphs 17 and 18 essentially describe the workings of Project Alpha,
but stress that the lenders (Citibank, Deutsche Bank, and Credit Suisse First Boston) “expected and required full repayment, with interest, or a similarly assured return.” Project 19 refers to the hedging strategy and the tear-ups, and concludes: “Thus, as the Defendants and their coconspirators and agents well knew, intended, and believed, Project Alpha was, in fact, a loan structured to appear as a 5-year natural gas contract that should have been disclosed as cash flows from financing activities: that is, as a loan (debt) rather than as cash flows from risk-management (operating) activities in Dynegy’s financial statements (10-Q and 10-K) for the 2nd, 3rd, and 4th quarters of, and for the year, 2001.”

Paragraph 20 declares that the Defendants “knew and understood that Generally Accepted Accounting Principles (GAAP)” that an SPE had to be an independent entity and those funding it had to bear some risk. It declares that “Dynegy’s auditors had warned that either a 100% hedging strategy or ‘tear up’ language would prevent Dynegy from reporting the cash flow from risk-management activities in its publicly-filed financial statements. Notwithstanding the warning of Dynegy’s auditors, the Defendants, and their coconspirators and agents, intended to, decided to, and did implement a 100% hedging strategy and did include ‘tear up’ language in the Project Alpha document to protect and ensure that the Project Alpha Lenders would not lose money.”

Paragraph 21 says that the Defendants kept the hedging strategy and “tear up” language secret from “Dynegy’s auditors, the SEC, Rating Agencies, lenders, market and securities analysts, and the investing public.” “In doing so, the Defendants, their coconspirators and agents, knew and intended that Dynegy would and did falsely report to the SEC, Rating Agencies, lenders, market and securities analysts, and the investing public, by means of electronic filing of Quarterly Reports (“Forms 10-Q”) and an annual report (“Form 10-K”) that approximately $300,000,000 of “cash flows from financing activities” were “cash flows from operating activities,” or, more specifically, “cash flows from Risk-management activities,” throughout the last 9 months of the year 2001.

Paragraph 22 says that the Defendants caused Arthur Andersen to mail an accounting opinion advising that Dynegy could report Project Alpha cash flow as operating cash flow. This opinion, as the Defendants intended, did not reflect the hedging and tear-up language of Project Alpha. Paragraph 23 quotes snatches of an email that circulated among the Defendants on May 10, 2001, that allegedly contained documentation regarding the hedging and tear-ups language and that said such documentation should not go to anyone else.

Paragraph 24 concludes: “In this manner, by the use of the means and instrumentalities of interstate commerce, including interstate wire communications and the mails, including interstate wire communications and the mails, the Defendants, and their coconspirators and agents, caused Dynegy’s cash from operations, and more specifically, from Risk-management activities, to be materially overstated in the second, third, and fourth quarters. Paragraph 25 concludes with a list of the various concrete acts by which the Defendants allegedly carried out their conspiracy.

And that concludes the first 16 pages of the indictment against Jamie Olis, Gene Foster, and Helen Sharkey. The remaining three and half pages simply refer to the same facts and declares them to violations of other rules and regulations, resulting in one charge of securities fraud.
(“making untrue statements of material facts”), one count of mail fraud, and three counts of wire fraud.

The reason for elaborating the indictment in such minute detail is this: To demonstate that the government clearly obligated itself to prove beyond a reasonable doubt that Project Alpha resulted in Dynegy’s misstating cash flow from financing operations (from a bank loan) as cash flow from operating activities. Because the amazing truth is that the government did no so thing. As we shall see, it did not even try.

The Government Goes Thug

When the federal government targets a businessman, conviction is not a certainty. But that is the way to bet. In the Olis case, as one newspaper noted, “the government had prosecu-
tors, Federal Bureau of Investigation agents, postal inspectors, and accounting experts to work the case.” There were also twelve million pages of documents produced as evidence. Just to have a copy of the documents printed would cost $100,000. And of course the government had the requisite software to search through the documents.

Still, Dynegy was committed, both by its laws of incorporation and by its severance agreement with Jamie Olis, to pay his legal fees, even after he was fired. So, the cost of the de-
fense must not have been an issue in Olis’s conviction, right? Unfortunately, not so. According to the Wall Street Journal, “Dynegy stopped paying his legal fees after it was pressed by the government to cut Olis off.”

The history of this behavior goes back to 1999 and to a document called Federal Prosecu-
ction of Corporations, issued by then Deputy Attorney General Eric Holder (now the Attorney General). This so-called Holder Memorandum offered guidance to federal prosecutors regarding the factors to be considered in deciding whether to prosecute a corporation. Among the factors was this one: “Whether the corporation appears to be protecting its culpable employees and agents.” But which employees are “culpable” and which are not? Isn’t the rule “innocent until proven guilty”? Not in the case of businessmen and their companies, evidently. (On January 20, 2003, the Holder Memorandum was replaced by the Thompson Memorandum, issued by Deputy Attorney General Larry D. Thompson. The language regarding “cooperation” was repeated, but it was now made binding on federal prosecutors.)

On January 10, 2003, U.S. Attorney Michael T. Shelby presented the newly installed Dy-
negy CEO, Bruce Williamson, with a copy of the Holder Memorandum, noting its provisions regarding a corporation’s “willingness to cooperate in the investigation of its agents.” In particu-
lar, the memorandum said that “a corporation’s support to culpable employees and agents . . . through the advancing of attorney’s fees . . . may be considered by the prosecutor in weighing the extent and value of a corporation’s cooperation.” Williamson was convinced that an indict-
ment of Dynegy would destroy the company. Ten days later, Shelby took the opportunity of the newly issued Thompson Memorandum to twist the knife in Williamson by sending him a copy.

On June 10, 2003, Olis was indicted and on June 20, he hired attorney Terry Yates. In Ju-
ly, the government learned that Dynegy was still paying Olis’s legal costs, and attorneys from the U.S. Attorney’s office called Dynegy’s outside criminal counsel, Larry Find, to demand to
know why. Finder told them that under Illinois law (the state where Dynegy was incorporated), the company was obliged to do so, and he faxed them a copy of the relevant provision. The government attorneys said that they thought there was a way to get around the law. Dynegy could “advance” Olis’s fees as required but put them in an escrow account so that he couldn’t use them, on the plea that they wouldn’t know whether Olis fully met the conditions for having his fees paid until after the trial was over. As it happened, this action may also have breached the contractual agreement that Dynegy and Olis reached at the time of his severance, but at this time Olis was hardly in a position to initiate a civil suit against Dynegy.

After Williamson explained the escrow ruse to Shelby, the latter replied: “I think it in neither of our interests to have the company pay for the defense of individuals whose actions were so egregious.” (p. 42) On July 23, Dynegy’s Board of Directors authorized the escrow plan, and Williamson told Finder to share the resolution with the U.S. Attorney’s office “as a show of good faith that we were trying to get as close to the standard of cooperation under the Thompson memo as we could.” On August 5, Foster and Sharkey agreed to plead guilty to one count of conspiracy to commit securities fraud. News stories at the time said that Foster and Sharkey were facing sentences of up to five years in prison, and that is surprising. Traditionally, people who went to trial and were convicted of securities fraud might receive a sentence of five years, so this “deal” looked like no deal. And since people did not yet realize how drastically the fall of Enron would change sentencing patterns, it seems likely that Foster and Sharkey had been assured that their potential sentence was really much lower than five years—so long as they delivered Jamie Olis, and then other Dynegy executives. As we shall see, their sentences were indeed much lower.

On August 13, 2003, Dynegy formally notified Olis of its escrow plan and stated that it would pay his legal fees only through August 18, 2003. In the event, however, it paid Yates’s initial bill for June 2003 work and then no more before the trial.

The Trial

On November 20, 2003, the trial of Jamie Olis opened in federal district court, in Houston, Texas. The Judge overseeing Jamie Olis’s trial was Simeon “Sim” Lake, who is perceived by Houston lawyers as being mildly pro-prosecution but generally fair. Perhaps more to the point in the Olis case, Lake apparently has an absolutely rule-bound mentality. The story is told that at his annual New Year’s Eve party, he goes so far as to allow his guests to use some small fireworks (which is technically illegal). But according to neighbor Rick Callaway, “He won’t so much as hold a sparkler. He usually goes back inside.” It was not a good sign for a case involving the pragmatic, rule-breaking world of big business.

The prosecution strategy in the Olis case was simple: Ignore all the accounting issues regarding the Alpha project and just keep repeating that Olis had failed to tell accountant James Hecker the whole truth. The downside of that approach, of course, was that the indictment of Olis had clearly rested on the assertion that Project Alpha was bad accounting and that all statements based on it were therefore false. Keeping secrets, and even deceiving other people, is not a crime. To be sure, given that the securities industry is now hedged about with ten thousand commandments, a regulation could no doubt have been found to cover the case. A regulation could probably have been found to criminalize any form of insincerity on Olis’s part, from brag-
The strategy employed by Olis’s lawyer was to say that he had acted and spoken as he did because he, justifiably, relied on the advice and opinions of others more knowledgeable. In particular, of course, he had relied on Dynegy’s top executives. For example, Dynegy’s controller, Mike Mott (Helen Sharkey’s boss), testified to the SEC in a separate case that he had disagreed with Hecker’s assessment and believed that Dynegy’s interpretation of Project Alpha was financially valid. (Mott was never indicted.) Gene Foster—Olis’s boss and the prosecution’s chief witness—testified in the same case that he and Dynegy’s internal accountants believed the accounting treatment was proper. Olis, a relatively new guy to the corporate world, simply accepted that he was learning how big businesses got deals done when they ran into a pig-headed individual. Dynegy’s top executives evidently assured him there was nothing wrong in going around your accounting firm’s representative if he was being pig-headed, so long as you were certain that he was wrong and the accounting was right.

One could argue, I suppose, that Olis should have distrusted the advice of all his colleagues and bosses at Dynegy, since they had an interest in getting Project Alpha done. But even if Olis should have been skeptical of all Dynegy’s executives (which is asking a lot), was he not reasonable in relying on the prestigious Houston law firms that had drawn up the agreement: Vinson & Elkins, which was working for Dynegy; Andrews Kurth, which was working for some of the banks? They knew all the details of Project Alpha, including the hedges and tear-ups that had been added into the amendments. They knew that Dynegy’s Andersen representative was withholding his approval. Yet no one at any of these firms had told Olis that the project could not go ahead. Didn’t Olis have reason to think that they agreed Hecker was just being unreasonable and should be kept in the dark? And what about the lawyers working for Citibank (Bracewell & Patterson, and Millbank, Tweed, Hadley & McCloy)? They did not tell Dynegy to stop. Those law firms went ahead and drew up the deal, and the banks, including Citibank, agreed to go ahead with the project. In fact, Arthur Andersen itself said that it wanted to be made aware only of certain things. Wasn’t it reasonable of Olis to think that the accounting firm too was saying it wanted to work around its obstinate agent, to get the deal done, and to reap its $8 million profit?

After eight days of prosecution testimony, Olis’s attorney apparently believed that he had established grounds for reasonable doubt, and he called no witnesses. In retrospect, this was clearly a terrible mistake. Perhaps he was motivated by the knowledge that Jamie Olis was a very sensitive man and tended to lose his composure when put under severe pressure. Whatever his reason, he could hardly have done worse for his client. During the testimony, several jurors had appeared to nod off, according to a report in the *Houston Chronicle* (November 5). And the *Chronicle* reporter herself acknowledged that the testilymony was so complex as to be hard to follow (11/05/03). So, in the end, the jury went for the simple narrative: Olis had kept Hecker in the dark; surely, that was for some nefarious purpose; therefore, it must have been for some criminal purpose. The jurors found Olis guilty in less than two hours.
So, Jamie Olis had been found guilty of committing Project Alpha. The next question was: What would his sentence be?

Gene Foster had been, by his own admission, “the coordinator” of Project Alpha, and he was facing an absolute maximum of five years in jail. But then Foster had cooperated in nailing Jamie Olis, even portraying himself as a perjurer in order to do so. Olis had refused to cooperate in nailing anyone. He had stood by his innocence, and Michael Shelby obviously hated people who thought they were innocent. So, what sentence would Olis receive? That was the question he faced as he went before Judge Lake in March 2004.

The imposition of Jamie Olis’s sentence took place at a time when demagogues had stirred up a frenzied rich-hunt among Americans. But the background had been set earlier. In the 1980s, a large bipartisan group of politicians wanted to bring uniformity to federal sentencing. To do this, Congress had set up the United States Sentencing Commission (USSC) and charged it with issuing strict guidelines that judges would be required to follow. At the same, federal prisoners would no longer be eligible for parole, although those sentenced to more than one year could, through good behavior, get 15 percent taken off their sentences. (Hence, the frequency of “year and a day” sentences.)

The guidelines that the USSC came up with worked as follows. First, there was a column of “offense levels,” numbering 1 to 43, from least serious to most serious. Above this column, and running at a right angle to it, there was a row of six criminal-history categories (I through VI), which were defined according to a point system that the USSC had contrived. (e.g., 2 points for a previous sentence between 2 and 13 months; 3 points for a previous sentence exceeding a year and a month; and so on). Category I of criminal history was for people with 0 points or 1 point; category VI for those with 13 or more points. The offense levels and criminal history levels thus formed a gridwork of 258 cells (43 x 6), each of which contained an allowable range of sentences, specified in months (except for Offense Level 43, which required a life sentence).

Thus, if a judge had to sentence a person who had been convicted of a crime at offense level 6, and if that person had a criminal history that gave him either 0 points or 1 point of criminal-history (Category I), then the judge was permitted to sentence the person to a prison term of between 0 and 6 months in prison. On the other hand, if the person’s criminal history gave him 13 or more points (Category VI), then the judge had to sentence him to a term of between 9 and 15 months.

But the USSC was not finished. It next added a procedure for enhancing or reducing what came to be called the “Base Offense Level.” That is, a judge sentencing a person convicted of armed robbery would see that the crime itself had a “Base Offense Level” of 18, which entailed a 27 to 33 month sentence. But the criminal’s offense level would be raised by 1 point (to 19) if he had brandished a pistol in the course of the crime, by 2 points (to 20) if he had used the pistol to threaten, and by three points (to 21) if he had actually fired it. At offense level 21, he had to receive a sentence of between 37 and 46 months. Which factors applied in a particular crime committed by a particular person was a matter that was determined by members of the U.S. Probation Department, although ultimately the judge in the case was responsible for accepting their reasoning. There was then one final step: the whole gridwork of sentencing cells was divided into four “zones” (A, B, C, and D), which specified what part of a sentence might be in the form of proba-
tion rather than incarceration. Offenses in Zone A might be punished through probation only; offenses in Zone D had to be punished with at least the minimum of the allowable months being served in prison.

Given the crime of which Jamie Olis was convicted, his base offense level was 6. Under the November 1, 2001, amendments to the Sentencing Guidelines, this meant that his crime was considered to be approximately as heinous as possessing less than four ounces of marijuana without intent to distribute (offense level 6). As he had no criminal history, the required sentence for such an offense level was 0 to 6 months, and all of it could be served as probation.

But then the persecuters went to work. His crime had involved a “sophisticated means,” they determined: that added 2 points to the offense level. His crime, they decided, had involved the use of a special skill (accounting): that added another 2 points to the offense level. And surely, they said, his crime had affected more than 50 people: that added 4 points to the offense level. Lastly, and most devastatingly, they alleged that his crime had caused more than $100 million in losses: that added 26 points to the offense level. In sum, the U.S probation department declared, Jamie Olis’s offense ranked at offense level 40—not on a par with possessing less than four ounces of marijuana for personal use, but above the offense level for raping a child under 12 (offense level 31), for premeditated murder (offense level 33), and for passing national defense information to a foreign country (offense level 37). A crime at the offense level of 40 required a sentence of between 292 to 365 months in prison: from 24 years and 4 months to 30 years and 5 months.

One might argue about the first two additions to Olis’s “offense level.” (If he used a special skill to commit a fraud wasn’t it double-counting to say the scheme was “sophisticated?”) And one might ask just who were the 50-plus people Project Alpha defrauded. Back in 1934, when the U.S. government was prosecuting the great utility executive Samuel Insull for securities fraud, it actually put twenty-five individuals on the stand and had each one had to tell his individual story of deceit, investment, and loss. Where were Olis’s victims?

But the worst of the “enhancements” to Olis’s “base offense level” was clearly the assumption that it entailed more than $100 million in losses. Prior to Olis’s sentencing, prosecutors argued that his actions had actually resulted in investor losses of at least $500 million and maybe a billion. Legally, it wouldn’t have mattered. Once the figure went over $100 million, no more “enhancements” were made to the offense level. So, what prosecutors were trying to do, most likely, was persuade the judge to pick a prison sentence at the upper end of the permissible range set by the probation officials—somewhere nearer 30 years in prison than 25. Olis’s lawyers, disputing the $100 million figure, argued for a sentence of 5 to 10 years. To settle the matter, Judge Lake lit upon the allegation, which had been made in the course of the trial, that the University of California’s retirement fund had, by itself, lost $105 million on Dynegy stock. Citing that and only that as the loss would kill multiple birds with one stone. The retirement fund was a clearly identifiable victim. It clearly represented more than 50 people, thus giving the prosecution its needed maximum of victims. And it allegedly had lost more than $100 million, again giving the prosecution its needed maximum. Thus, there was no need to speculate about when anonymous traders might have bought Dynegy stock and when they might have sold it.
Having decided to accept the recommendation of Offense Level 40, Judge Lake chose the minimum figure at that level: 292 months, 24 years and 4 months. There then remained only the arbitrary process of dividing the predetermined sentence among the six counts of the indictment: 60 months for the conspiracy charge; 120 months for the security fraud charge, 60 months for mail fraud charge—all to be served consecutively. Fifty-two months was assigned for each of the three counts of wire fraud, but they were all to be served concurrently. Five years; ten years; five years; four years and four months. With 15 percent off for good behavior, Jamie Olis might plan to see the light of day in 20 years and 9 months.

Olis’s boss Dynergy, Gene Foster, “the coordinator” of Project Alpha, would eventually be sentenced to eighteen months in prison; Olis’s colleague, Helen Sharkey, to thirty days.

Reaction

The first reaction to the Olis sentence came from Judge Lake himself. The sentence, he said, “reflects Congress’s intent that white-collar corporate fraud defendants receive harsh sentences.” He added: “I take no pleasure in sentencing you to 292 months, but my job is to follow the law.” Why did Judge Lake say he took no pleasure in crucifying Jamie Olis? Judicial retribution, when it is just, is a necessity of civilized society, and a person may legitimately take pride in doing that job well, even as an executioner may take pride in wielding his axe well. But judicial retribution is never an act in which a human being should take pleasure, for it requires treating a fellow human as a brute, something that a healthy nature will resist.

But certainly Judge Lake was correct when he said that Congress wanted “white collar criminals” to receive harsh sentences. And certainly he was correct again when he said that his job was following the law. Yet not even the rule of law can turn a person into a robot. Judge Lake was not bound to sentence Jamie Olis to 292 months, or indeed to any months at all. He could have—quit. He could have washed his hand of the crucifixation of Jamie Olis and underlined his resignation by calling for a presidential pardon. He could have denounced the Congressional “rich hunt” that had brought Jamie Olis before him. And he could have said from the bench that “following orders” is not an unlimited excuse, either for him or for any man. Of course, he did none of those things. That he claimed to “take no pleasure” in sentencing Olis provides him no redemption.

The next reaction to Olis’s 20-year sentence came from the man who was responsible for prosecuting him, U.S. Attorney Michael T. Shelby. Unlike Judge Lake, Shelby was unflinching in what he had accomplished. He could not even bring himself to call the Olis case “a tragedy,” as did his assistant U.S. attorney Jimmy Sledge, who had conducted the case in the courtroom. Instead, Shelby declared: “Today, Mr. Olis was held accountable for the harm his actions have caused so many.” Shelby claimed to represent “tens of thousands” of victims, who had lost money because of Olis.

And yet, one wonders how genuine Shelby’s posture of righteousness was. After all, at his recommendation, Olis’s superior at Dynegy, Gene Foster—the man who named Project Alpha and considered himself its coordinator—was sentenced to only 18 months in prison. At his recommendation, Olis’s colleague Helen Sharkey was sentenced to only 30 days in prison. One suspects that Michael Shelby wished to crucify Olis less because of “the harm his actions have
caused so many” than because Olis had refused all plea bargains. Consider something very odd that Shelby said about Olis: “We have been rebuffed at every turn. I would ask the question: ‘Why don’t you help us?’” Michael Shelby had worked for prosecutors his entire professional life and he surely thought that he knew how to “make an offer he can’t refuse.” Could it be that he was personally affronted that Olis could refuse?

Consider what transpired following Olis’s conviction. He was offered a second chance to save himself. Prosecutors told him that if he would only give Shelby the testimony he needed to go after higher-ups at Dynnergy, such as CFO Richard Doty and CEO Chuck Watson, the government would argue for his receiving a reduced sentence. Olis took a weekend to think it over. His first child was not yet 6 months old. If his current sentence stood, she would be an adult when he was released—assuming he did not die in prison. On the following Monday, he gave his answer: No. "What they wanted was for me to tell the story that I and everyone else engaged in a conspiracy. And I couldn't ruin those people's lives. I'm Catholic. And I can't do that.” Might Shelby’s snarling satisfaction at Jamie Olis’s 24-year prison sentence reflect less a sense of justice than a sense of frustration at being blocked by Olis’s self-confident innocence?

It is one of the many ironies in this case that Michael Shelby was struck with a fatal cancer in September 2005. Unable to face his own dark tragedy with the same stoic nobility that Jamie Olis was then facing a lifetime in prison, Shelby committed suicide. After his death a former colleague said, “Mike had prosecution in his blood, the same way I do. When you experience the joy of helping people who have been victims and get to do something about the perpetrators of crime, it's so rewarding that it's intoxicating.” The love of justice is an excellent thing, no doubt. But “prosecuting while intoxicated” creates as many victims as it helps.

**Appeals**

Naturally, Olis appealed both his conviction and his sentencing. Unfortunately, once a jury has found a person guilty that verdict becomes extremely difficult to overturn on a merely factual basis. As the appeals court noted, it could not overturn a verdict “unless the record demonstrates that a rational jury could not have found each of the elements of the offense beyond a reasonable doubt.” Olis’s appellate lawyer argued that the evidence was insufficient to suggest beyond a reasonable doubt he had “conspired to conceal two critical features of Project Alpha from Dynegy’s outside auditor, Arthur Andersen.” Those “two critical features” were the “parent hedge” and the “tear ups.” But Foster had testified that he and Olis “wrongly agreed to the tear-ups and the parent hedge and hid them from Arthur Andersen.” And Jim Hecker “testified that he advised Dynegy against tear-ups, and Dynegy subsequently did not reveal this aspect of Project Alpha to him.” The appeals court noted that it was required to construe all evidence and all inferences from that evidence in a manner most favorable to the jury’s verdict. In this case, it said, the testimony of Foster and Hecker, taken together with some incriminating e-mails, show that a jury “could easily have found Olis guilty beyond a reasonable doubt of all the charged crimes.” Indeed, the court remarked, that Olis’s lawyer’s contention to the contrary was almost perfunctory.

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4 Ibid., p. 4.
6 Ibid., p. 5.
7 Ibid., p. 4
When it came to reviewing Olis’s sentence, however, the appeals court was on a very different footing. Judge Edith Jones, without rebuking Judge Lake, thoroughly demolished both his sentencing procedures and the sentence. As to the procedures: There was a line of Supreme Court cases, going back to the year 2000, that spoke to the way in which sentence enhancements could be determined. The first of these cases, *Apprendi v. New Jersey* (2000), held that the Sixth Amendment prohibited judges from enhancing sentences beyond the statutory maximum based on facts other than those determined by a jury, under the standard of “reasonable doubt.” *Blakely v. Washington* (2004) which dealt with mandatory sentencing guidelines provided by state law, held that the Sixth Amendment prohibited judges from enhancing sentences based on facts that were neither determined by a jury nor admitted by the defendant. At the time, the Court said it was not addressing the validity of the mandatory federal sentencing guidelines, but it was hard to see any reason for thinking the federal guidelines were not marred by the same flaw, and six weeks later (during the summer) the Court agreed to hear a case challenging the federal guidelines. (The judge in the Martha Stewart case let Stewart remain free pending her appeals explicitly because of “the turmoil resulting from the Supreme Court’s decision in *Blakely v. Washington*.” Olis asked for the same consideration but was denied.) The Supreme Court heard the case of *United States v. Booker* on the first day of its 2004 term and issued its decision on January 12, 2005. Predictably, it concluded that, in the case of the federal sentencing guidelines, mandatory enhancements had to be based on facts found by the jury or admitted by the defendant.

Two possible remedies were thus hand: Keep the mandatory sentencing guidelines, but require a jury hearing on the facts to be applied. Or continue to let the judge weigh mitigating and exacerbating circumstances, but make the guidelines advisory only. Looking to the legislative record, the Supreme Court decided that Congress would not have passed the guidelines if it had believed it was adding an entirely new realm of jury hearings to the judicial world. Therefore, the guidelines would henceforth be advisory only.

Now, Olis was sentenced on March 25, 2004, just two days after the Supreme Court heard oral arguments in the *Blakely* case. And *Blakely* wasn’t decided until June 24, 2004. Thus, Judge Lake was not bound to consider *Blakely* as a precedent, much less *Booker*, which had not even been scheduled for a Supreme Court hearing. But he was bound to consider the Sixth Amendment objection that Olis raised and that the Supreme Court later found to be valid in *Blakely* and *Booker*. It was his (erroneous) rejection of that valid argument that the appeals court was now considering. Because his rejection was erroneous (as we know from the Supreme Court’s *Booker* decision), the appeals court could not let Olis’s sentence stand unless Lake’s error was harmless to the defendant. “In this case, the Government points to no evidence proving beyond a reasonable doubt that the district court would have sentenced Olis to nearly twenty-five years in prison had it acted under an advisory Sentencing Guidelines scheme as required by *Booker*. Therefore, we vacate Olis’s sentence and remand for resentencing.”

But the appeals court was not yet finished with Judge Lake. They decided that he needed to be instructed on the proper method of calculating the economic “loss” that would count toward an enhanced sentence, even if he took the guidelines as advisory.

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In the case of securities fraud, the court said, “there is no loss attributable to a misrepresentation unless and until the truth is subsequently revealed and the price of the stock declines. Where the value of a security declines for other reasons, however, such decline, or component of the decline, is not a ‘loss’ attributable to the misrepresentation.” Now, there are several types of securities fraud, the court said, but the type “most analogous to the one before us concerns fraudulent transactions that ‘cook the books,’ and prop up a company’s stock but do not . . . render the company completely worthless. Sentencing decisions in these cases acknowledge that because a company’s stock price is affected before and after the fraud, by numerous extrinsic market influences as well as the soundness of other business decisions by the company, the calculation of loss attributable to securities fraud requires careful analysis.” In particular, the court noted a case in which “the Government’s use of stock prices the day before and the day after the revelation of the fraud did not account either for the actual price at which most holders purchased the company’s shares or for the influence of outside factors on the change in price.”

But hadn’t Judge Lake avoided all these difficult questions of market losses by concentrating on a single investor, the University of California Retirement System? Not so, as it turned out. During the trial, Jeffrey Heil, a former investment advisor for the University of California Retirement System, testified that UCRS had lost something more than $100 million on Dynegy stock. But that was the amount UCRS lost during the period it owned Dynegy stock: 2001 and 2002. Of course, that was a period that included, apart from Project Alpha: the terrorist attacks of 9/11, the collapse of the energy giant Enron and Dynegy’s failed attempt to rescue that company’s wreckage, plus California’s electricity crisis. As the Los Angeles Times reported in 2004, Heil was never asked how much of UCRS’s loss was attributable to Project Alpha. When a Los Angeles Times reporter asked him that question, three and a half months after Olis’s sentencing, Heil replied: “To be truthful, I would not have known the figure.” A little late to say so.

In light of this, the appeals court went on: “The court elected to rely solely on the Heil’s testimony concerning the purchase and sale of UCRS stock as a measure of the loss caused by Olis’s offense. [But] when Heil’s testimony was offered at trial to prove [Olis’s] guilt, Olis’s counsel was not placed on notice that the same evidence might later pertain to the guidelines loss calculation. For that reason, other significant extrinsic causes of the UCRS loss were not explored, much less quantified, at trial.”

For example, Judge Jones said: UCRS bought most of its Dynegy holdings at the top of the market, [and] ... two-thirds of the drop in Dynegy's price occurred either before the revelation of Project Alpha's problems or more than a week after the announcement of the restatement of earnings caused by Project Alpha. Taken on the court's own terms, a substantial portion of the entire loss on the UCRS investment in Dynegy, over $100 million, could not have been caused by Olis's work on Project Alpha.”

10 Ibid., p. 15.
11 Ibid., p. 15.
12 Ibid., p. 17.
13 Ibid., 17-18.
During sentencing, moreover, Olis offered the expert report of a Rice University expert, Professor Bala Dharan, which explored numerous forces at work on the Dynegy stock price during the relevant periods. The court refused to consider the report, … [yet] Professor Dharan’s report demonstrates that Dynegy stock declined during the period covering Project Alpha in tandem with the stocks of other publicly traded companies in the energy marketing and trading business. Further, Dynegy's stock was negatively affected, even before the restatement of Project Alpha's cash flow impact, by the company's failed bid to acquire the faltering Enron. These factors and others cited in the report suggested that attributing to Olis the entire stock market decline suffered by one large or multiple small shareholders of Dynegy would greatly overstate his personal criminal culpability.

In the end, there was not much left of Judge Lake’s historic sentence. Unfortunately, in a footnote to the appeals decision, the appeals court wrote: “The Government’s alternative theory, which purported to measure as ‘gain to the defendant,’ Dynegy’s tax benefit from Project Alpha, need not be considered unless actual loss proves impossible to measure.” The Court of Appeals for the Fifth Circuit had utterly destroyed U.S. Attorney Shelby’s raging about the “tens of thousands” of victims who had been so terribly harmed by Jamie Olis. But it had left the Government this bizarre theory as an out: Jamie Olis and “his” Project Alpha had “profited” by a Dynegy tax shelter: the tax shelter that had originally been brought to them ready-made by Arthur Andersen, the tax shelter that did not require hedges or tear-ups—or Project Alpha.

Resentencing

Judge Lake’s office scheduled a January 5, 2006, hearing for resentencing. Interestingly, the court docket showed that Gene Foster and Helen Sharkey were also scheduled to be sentenced on the same day. Although the two had pleaded guilty in August 2003, prosecutors may have wanted to wait until Olis’s conviction had been upheld on appeals, to make sure the two were still under pressure to testify a second time if a new trial were ordered. At the same time, Judge Lake rejected the request made by Olis’s attorney that he be released from jail until his resentencing. This was taken as a sign that the judge did not intend to sentence Olis to time served. Indeed, the judge said that Olis has “a number of years to serve even under the most liberal interpretation of the Law.”

In its brief to Judge Lake, the U.S. Attorney’s office continued to demonstrate a greater ability to handle rhetoric than to handle facts. It described Project Alpha as “a historically significant securities fraud that shook the confidence of the nation and the world.” In fact, few would ever have heard of the Dynegy case but for the extreme persecution of Jamie Olis. In its conclusion, the government asked for a sentence of 188+ months, which is to say something more than 15 years and three months, on two grounds: First, unlike Foster and Sharkey, Olis “refused to take responsibility for his action,” and, second, he had caused more than $20 million in losses to Dynegy stockholders. But Olis was not “refusing to take responsibility for his actions.” On the contrary, he alone was taking responsibility. He alone was not placing responsibility for his actions on someone else. It was Gene Foster, the government’s hero, who was refusing to take responsibility, by supporting the government’s theory that Alpha was “Jamie’s project.” What the government really objected to, of course, was precisely that Olis would not join Foster in trying

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14 Houston’s Clear Thinkers, December 3, 2005.
to place the blame elsewhere, specifically on higher-ups such as CFO Doty and CEO Watson, whom the government lusted to prosecute. Olis accepted responsibility, but he refused to accept blame, and that was because he did not believe Project Alpha involved blameworthy actions. As for Olis’s causing $20 million in losses to Dynergy stockholders, the government said nothing in its initial brief about how it arrived at that figure. It merely spoke of “a universe of victims,” although it did allude to “the employee beneficiaries of the University of California Retirement System.”

Said blogger Tom Kirkendall: “In what can only be described as an over-the-top and spiteful request, the prosecutors in the sad case of Jamie Olis requested yesterday that U.S. District Judge Sim Lake resentence Olis to a 15 year jail sentence that is exceeded in its absurdity by only the 24 year sentence that the prosecutors improperly obtained in Olis’ original sentencing hearing.”

By the time Judge Lake got around to resentencing Olis, both sides had submitted estimates of the “loss” supposedly caused by Project Alpha. The government submitted a report by Frank C. Graves (June 12, 2006) of the prestigious Brattle Group in Cambridge, Mass. But after summarizing Graves’s reasoning, Judge Lake concluded: “A number of confounding negative announcements made on each of the days for which he identified abnormal returns, i.e., April 25 and May 8, 2002, required him to base each of the numerous calculations that underlie his estimate of actual loss on unprovable and often unexplained assumptions. ... the multiplicity of confounding announcements made both by and about Dynegy on April 25–26, and the lack of reliable or specific information about the number of damaged shares held by either institutional or non-institutional investors posed methodological difficulties that required Graves to rely on unprovable assumptions at every step of the equation used to estimate the loss attributable to corrective information about Project Alpha. Absent guidance from the sentencing commission or the court of appeals on how to decide when results produced by methodologies that are necessarily based on a series of unprovable assumptions that yield speculative results are nevertheless reasonably certain estimates of actual loss caused by a defendant’s unlawful conduct, the court is compelled to conclude that the confounding announcements and the unprovable assumptions on which Graves necessarily relied in reaching his estimate of actual loss demonstrate that it is not possible to estimate with any degree of reasonable certainty the actual loss to shareholders caused by the corrective disclosures about Project Alpha made on April 25, 2002.”

That is a remarkable statement, and well worth pausing over. The government guidelines for economic loss in the case of fraud fall into fourteen categories. The lowest is (A) $5,000 or less. From there they proceed: (B) More than $5,000; (C) More than $10,000; (D) More than $30,000; (E) More than $70,000; (F) More than $120,000; (G) More than $200,000; (H) More than $400,000; (I) More than $1,000,000; (J) More than $2,500,000; (K) More than $7,000,000; (L) More than $20,000,000; (M) More than $50,000,000; (N) More than $100,000,000. Clearly, Judge Lake was not required to specify “actual loss” to the penny. Except for the first level, the guidelines do not have upward borders; rather, they are inclusive. If one suspects, but cannot estimate with reasonable certainty that the actual loss was more than $100,000,000, can one say

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15 Sentencing Memorandum of the United States, p. 6.
16 HCT, December 21, 2005.
“with reasonable certainty” that the actual loss to shareholders was “more than $50,000,000”? No? Well, can one say “with reasonable certainty that it was “more than $1,000,000”? More than $120,000? How about “More than $5,000”? And if, with all the assistance of a high-powered consulting firm like the Brattle Group, one cannot say “with any degree of reasonable certainty” that the “actual loss” was “more than $5,000,” how could this have been “a historically significant securities fraud that shook the confidence of the nation and the world”? Obviously, it could not have been. So was it about Jamie Olis’s case that motivated government officials to gloat over sending a first-time white-collar offender to prison for 25 years? Was it perhaps his determination to prove his innocence that drove them round the bend? And if so, what would that say about the regime of business regulation under which we live?

At this point, perhaps, Olis might have begun to hope that he would be sentenced to “time served.” But that hope was quashed by Judge Lake’s refusal to grant Olis bail while awaiting resentencing, and by his assertion that Olis had “a number of years to serve even under the most liberal interpretation of the Law.” How could he say that, prior to assessing the guidelines under the rules laid down by the appeals court? That court had authorized adding points for a “sophisticated scheme” and a “special skill.” But that brought the offense level up to only 10, which is to say, 6 to 12 months. The court had likewise opined that there were surely “50 or more victims,” though who those victims were now had become murky since Judge Lake had refused to find any “actual loss” to shareholders. Still, throw in “50 or more victims,” and the offense level rises to 15 to 21 months. By the time of Judge Lake’s resentencing decision, Olis had been in prison for 28 months, because Judge Lake had not permitted him to go free on bail while awaiting resentencing. Having refused bail, it would be embarrassing in the extreme for Judge Lake now to sentence Olis to less than time served.

So, Judge Lake had to come up with some way to hand Olis a lengthy sentence. But the way he used was truly bizarre. The court of appeals opinion had spent eight of its twenty pages carefully delineating the various proper and improper means of calculating actual loss in a securities fraud case such as it considered Project Alpha. In footnote 13, the court observed that the government had employed an economic study to separate stock losses caused by Project Alpha from stock losses caused by other factors, but that the study (the court said) wrongly looked at gross market loss rather than actual losses to shareholders. The court then added, in one throwaway sentence that, because the proper method of calculating shareholder losses had not even been attempted by the government, the appeals court did not need to consider the government’s alternative theory, “which purports to measure as ‘gain to the defendant,’ Dynegy’s tax benefit from Project Alpha.”

On page 23 of his 34-page resentencing memorandum, Judge Lake put behind him 15 pages of futile attempts to establish “actual loss” to shareholders and turned, perhaps with relief, to this off-the-cuff footnote. In less than one page, it solved all his problems. “Since [Gene] Foster’s uncontroverted testimony establishes that Olis expected the fraudulent accounting treatment accorded to Project Alpha to reduce the taxes that Dynegy would otherwise have owed to the United States Treasury by $79 million, the court concludes that $79 million is a reasonably certain estimate of the pecuniary harm that the defendant intended to result from his offense.”

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18 Memorandum Opinion, September 22, 2006,
There are so many strange turns here that it is hard to know where to begin. The government had indicted Olis for phony accounting, specifically, treating cash from a loan as cash from operations. The prosecutors had then turned around and tried Olis for keeping facts from Jim Hecker, to wit, the facts that Hecker thought turned the cash from operations into a loan. Now Olis was being sentenced on the grounds that had nothing to do with the accounting of cash-flow. It was alleged that he had “profited” because Dynegy hadn’t paid $79 million in taxes. But the indictment had said not a single word about the filing of false tax returns. There was no mention of the IRS or the Treasury as one of Olis’s victims. No wonder Foster’s testimony about taxes was “uncontroverted.” No one thought it was anything more than part of the back-story of Project Alpha. And, of course, in the final irony, the tax scheme was the plan that Arthur Andersen had brough to Dynegy.

Given the nature of this “offense,” Lake threw out the “more than 50” victims enhancement, but used the “more than $50 million” enhancement of 24 points. With 34 points used to calculate the defendant’s sentence, Judge Lake sentenced Olis to 6 years in prison. It was precisely the same sentence that Andy Fastow would receive four days later for single-handedly bringing down Enron, America’s fifth largest company, thereby causing investors to lose billions of dollars, and thousands of people to lose their jobs—tens of thousands if one counts the collapse of Arthur Andersen as well. Many in the media clucked their approval at the new Olis sentence, glad to be rid of the insane 24-year sentence that threatened to discredit white-collar prosecutions as such, but well content with the merely unjust sentence of six years.

Prison Assignment

On December 10, 2006, Tom Kirkendall’s blog narrated how the government was managing to make Jamie Olis suffer every extra measure that it could dish out.

Olis reported to prison on May 20, 2004, and was originally assigned to the Bastrop unit, about an hour and a half away from San Antonio where his wife and young daughter are living. However, in January 2005, Olis was inexplicably yanked out of the Bastrop unit and transferred to a much harsher medium security prison in Oakdale, Louisiana, 400 miles away from his family.

Then, after the Fifth Circuit set aside Olis’ original 24-year sentence on October 31, 2005, U.S. District Judge Sim Lake ordered Olis transferred to the Federal Detention Center in downtown Houston. The Detention Center is essentially an interim facility containing small jail cells that are most commonly used to hold prisoners before the Bureau of Prisons assigns them to a federal prison where they will serve their sentence. It has nominal inmate facilities (it doesn’t even have a prison yard) and is ill-equipped to hold a prisoner for longer than a couple of weeks. Although closer to San Antonio than Oakdale, the Houston facility is still a four-hour drive for the Olis family.

In transferring Olis to the Detention Center, Judge Lake probably thought that the resentencing would occur quickly and that it would be more expeditious to have Olis in Houston. However, the prosecution engaged in a series of delaying tactics over most of the past year that delayed Olis’ resentencing until September 22, almost 11 months after the Fifth Circuit ordered it.

To make matters worse, Olis has now endured almost a year in his cramped Detention Center cell and still has not been assigned to a prison unit to serve the balance of
his sentence. This, despite the fact that he was resentenced three months ago [strictly, eleven weeks] and a number of federal criminal defendants sentenced after Olis--including [Jeff] Skilling, [Andy] Fastow, and [Richard] Causey [of the Enron case], have already been assigned to prisons where they will serve their sentences.

And still it would not end. Kirkendall was back two months later to update the story:

Former Dynegy executive Jamie Olis--whose only “crime” may have been some-what faulty judgment in doing what his bosses told him to do in attempting to bolster Dy-negy’s finances--continues to sit in a dank, cramped jail cell in downtown Houston’s Federal Detention Center awaiting reassignment to a federal prison. … It has now been four months since Olis had his absurd original 24-year sentence reduced to a still egre-gious six years. . . . [O]lis has now been in the Federal Detention Center--essentially a holding tank for federal prisoners--for going on 14 months since the Fifth Circuit tossed out his 24-year sentence. Olis has now served 40% of the time that he has been in prison in a jail facility not meant or equipped to hold prisoners serving lengthy sentences. The [Houston] Chronicle’s Tom Fowler follows with this story [URL] about Olis’s ordeal, in which a governmental official observes that Olis’s reassignment has been “slowed be-cause of the holidays and the recent spate of bad weather.” Uh, Olis was re-sentenced over two months before the holidays. And I don’t recall the weather being all that bad over that period.

It’s understandable if Olis and his family are reluctant to request that the federal court examine what on earth is going on at the Bureau of Prisons that it can’t manage to assign Olis to an appropriate federal prison. Hell, the way this ordeal is going, the BOP in response to such a request might just throw away the keys to Olis’s cramped cell. But the deal in reassigning Olis has now moved well beyond the realm of reason and is beginning to resemble the brutal nature of his original sentence. Is the BOP simply impervious to such matters?

Perhaps the publicity from the Houston Chronicle finally got someone’s attention. On February 11, Kirkendall was able to report. “Yesterday, the Bureau of Prisons finally transferred Olis from the downtown Houston Federal Detention Center to the Bastrop, Texas, federal prison unit.” He also noted that it “is thankfully the most convenient location for Olis’s family member to visit him.”

O’Quinn Takes Over

But the Olis case had one more surprise in store. On October 5, 2007, Houston’s famed plaintiff’s lawyer John O’Quinn filed a 106-page brief with Judge Lake. O’Quinn was perhaps best known for his $100 million lawsuit against Dow Corning and its silicone breast implants. He was also involved in the tobacco litigation, winning $17.3 billion for the state of Texas. The best—the absolute best—that can be said about those lawsuits is that they were horribly mis-guided. But be that as it may. O’Quinn had been following the story of Olis’s case through the blog of fellow Houstonian Tom Kirkendall. Why he had not acted sooner is unclear. But in the fall of 2007, he brought his formidable talents to the Olis’s cause, free of charge, and his words were good to hear:
In the radioactive environment following the collapse of Enron, Petitioner Jamie Olis was
the first person to be tried in a criminal case arising from the business transactions of a
Houston gas trading company. For reasons that could not have been known to this Court,
Olis’s was a fundamentally flawed and unfair prosecution. As a result, an innocent man
stands wrongfully convicted. It is time for the Court to remedy that injustice.

O’Quinn had an uphill battle. If it is difficult to get the facts of a case reconsidered on
appeal, it is likewise difficult to get the legal issues of case reheard after it has been considered
on appeal. It is usually necessary to show that some fundamental, usually constitutional, error
has been committed. Thus, the basis for O’Quinn’s brief lay in the three most basic issues that
have been detailed in this article’s narrative, and his points will need little elaboration.

(1) O’Quinn argued that the government had prevented Dynegy from fulfilling its obliga-
tion to provide Olis with the funds he needed to defend himself in this enormous complex case.
In the time since 2003, courts had ruled that this behavior violated the consitutional rights of
defendants. In New York, Judge Lewis Kaplan had proclaimed, and the Second Circuit Court of
Appeals had agreed, that the government’s technique of bludgeoning corporations into abandon-
ning former employees, contrary to the corporations’ promise, was a denial of the employees’
Fifth and Sixth Amendment rights.

(2) O’Quinn also brought out the fact that, in its indictment, the government had charged
Olis with a specific crime (phony accounting), based on specific facts. Yet when the case came
to trial, it pretended that Olis’s crime was something quite different (keeping secrets from an ac-
countant) and based on a quite different set of facts. Constitutionally, the government is not al-
lowed to prosecute an individual for a crime other than the one specified in the indictment.

(3) Because neither of these points had been raised on appeal, O’Quinn was virtually
forced to argue that Olis’s representation had been deficient to a degree that prejudiced the case
against Olis.

On the basis of these facts, O’Quinn said, Olis asks that his conviction be set aside, and
the charges against him dismissed. Alternatively, Olis asks that his conviction be set aside and
that he be given a new trial in which his constitutional rights are not violated.

On March 3, 2008, Judge Lake responded to Olis’s brief. Although setting aside several
of Olis’s requests, such a request for release on bail while his petition was being heard, Lake did
order the government to file a response to his main points, which it did on March 31.

In response to the claims about Dynegy’s withholding fees, the government argued that
Olis’s attorney had had sufficient information to raise that issue at the time of the trial and his
failure to do so precluded its being raised after conviction.

As for the prosecution’s changing the crime charged, the government responded that the
“fraud” statute is so broad as to effectively criminalize any “manipulative” devices in connection
with the purchase of sale of a security. The government crowed: “Criminal liability under section
10(b) of the Securities Exchange Act does not require deception of and reliance by an identifie-
ble buyer or seller of securities.” Indeed, a “scheme” “may be fraudulent even though no affirmative misrepresentation of facts be made.” Consequently, “a jury in this case could have found that Olis and his coconspirators intentionally and materially misled investors even if Olis were able to obtain an expert to testify that booking the transaction as cash flow from risk management activities could comply with GAAP if the hedges were with a holding company and the tear-ups only indirectly linked the entities.” (56)

So, this is what is left of all that long indictment from June 2003, with those twenty-five paragraphs about the Defendants, their coconspirators and agents; about the *Wall Street Journal* article; about the emergence of Project Alpha; and about “cash from financing” versus “cash from risk-management.” In the end, the government said: “A jury in this case could have found that Olis and his coconspirators intentionally and materially misled investors even if Olis were able to obtain an expert to testify that booking the transaction as cash flow from risk management activities could comply with GAAP if the hedges were with a holding company and the tear-ups only indirectly linked the entities.” (56) And in fact, we know, Olis could obtain an expert of the highest authority to state just that. After Project Alpha had been brought into question, Dynegy had hired PricewaterhouseCoopers--one of the Big Four accounting firms--to review the arrangement, and that firm had said that “in form” it was compatible with Generally Accepted Accounting Principles.

On November 21, 2008, Judge Sim Lake rendered his judgment: Olis was entitled to no relief, not even a hearing on the issues that had been raised. He admitted that Olis had learned about the government’s behavior too late to raise the issue that Dynegy was withholding funds from him under threat. Therefore, Lake said, Olis does have a right to raise the issue at this late date. But, having raised it, does it matter? Judge Lake said no. The Fifth Circuit held that Foster’s testimony and the incriminating emails “and a wealth of other evidence” were enough to convict Olis. As for the “constructive amendment” of the indictment, the judge agreed with the government that it did not have to prove any violation GAAP in order to prove a violation of the securities law.

**The End**

On August 7, 2009, Jamie Olis was released from prison, although adding to the bizarreness of this case, he still had three years of probation to serve.

Shortly after Olis’s release, his long-time defender Tom Kirkendall wrote: “The prosecution and barbaric sentencing of Jamie Olis represents a festering wound for anyone who believes in principles of limited government and innocent until proven guilty. That the judicial system allowed the executive branch to bully Dynegy into serving up Olis as the initial sacrificial lamb of business corruption in the wake of Enron’s collapse is a frightening example of how little protection citizens have from dubious prosecutions.”