

Carleton, Norman

From: Carleton, Norman
Sent: Tuesday, November 20, 2001 4:43 PM
To: Wiedman, Mark; Nickoloff, Peter; Cetina, Jill; Sharer, James; Berardi, Steve; Pietrangeli, Fred; Schultheiss, Heidilynne; Whaley, Jean
Subject: FW: Bloomberg: Enron Falls Amid Concern Debt Threatens Dynegy Bid (Update5)

-----Original Message-----

From: Carleton, Norman
Sent: Tuesday, November 20, 2001 4:41 PM
To: Roseboro, Brian; Bair, Sheila; Bitsberger, Timothy
Subject: Bloomberg: Enron Falls Amid Concern Debt Threatens Dynegy Bid (Update5)

11/20 16:06

Enron Falls Amid Concern Debt Threatens Dynegy Bid (Update5)

By Stacie Babula

Houston, Nov. 20 (Bloomberg) — Enron Corp. shares and bonds dropped after the energy trader disclosed it may have to pay \$9.15 billion in debt due by 2003, suggesting the company may run out of cash before its takeover by Dynegy Inc. can be completed.

Shares of Enron fell \$2.05, or 23 percent, to \$7.01. Earlier they touched \$6.55, the lowest price in more than a decade. Enron's 6.4 percent notes due in July 2006 were bid as low as 69 cents on \$1 of face value and offered at 73 cents, down more than 13 percent in light trading, traders said.

Enron, whose dealings with affiliated partnerships led to earnings restatements, credit-rating cuts, a federal investigation and a management shakeup, said in a regulatory filing that it has less than \$2 billion in cash or credit lines. Dynegy plans to complete its buyout by October, and Enron may have to ask lenders to restructure payment schedules to survive.

"This filing shows that Enron is in a precarious financial situation," said Commerzbank Securities analyst Andre Meade, who rates Enron shares "hold" and doesn't own them. "They have to stay afloat for the Dynegy deal to go through, and that now looks difficult."

Enron and Dynegy wouldn't comment on the stock drop today. Standard & Poor's Investors Service said that Enron's credit rating remained on negative watch, indicating it would not immediately downgrade the company's debt.

\$690 Million Surprise

"Enron's near-term liquidity position is . . . expected to be sufficient to carry the company through the completion of its proposed merger with Dynegy," S&P said in a report.

Investors were concerned the debt, including a \$690 million note that Enron disclosed it may have to pay off next week, would lead to a cut in Enron's credit rating, analysts said.

The filing was a "distraction" that will not threaten the merger, said Todd Shipman, a director at S&P who follows Enron.

"Our approach to this has been on the basis that the Dynegy deal is a good thing for credit quality," Shipman said.

Moody's Investors Service, which didn't issue a statement on Enron's debt today, kept the company's credit rating at investment grade on Nov. 9, the day Dynegy announced it would buy Enron in a deal now valued at \$25 billion.

The ruling came after executives from Lehman Brothers Holding Inc., J.P. Morgan Chase & Co. and Citigroup Inc.'s Salomon Smith Barney lobbied the credit-rating company, people familiar with the situation said.

Avoiding Junk

A junk rating would have led Dynegy to abandon the acquisition, Dynegy Chief Executive Officer Charles Watson said. It would also have triggered debt repayment of at least \$3.9 billion, Enron said in a Securities & Exchange Commission filing

yesterday.

Enron shares are selling for almost 32 percent less than the value of Dynegy's offer, showing investors have doubts the deal will be completed. Dynegy shares fell \$1.90 to \$41.70 today.

"It's become more clear that the chances of this deal going through aren't 90 percent, but much closer to fifty-fifty," said Edward Paik, who helps manage the Liberty Utilities Fund, with 1.6 million Enron shares. "There's just so much information that is unknowable" about Enron's financial position, he said.

Most of the \$9.15 billion in debt is due before the end of the third quarter, when the Dynegy buyout is scheduled to close, Enron said yesterday in a third-quarter filing with the SEC.

Asset Sales Planned

Last week, Enron Chief Operating Officer Greg Whalley said the company will sell assets of "non-core businesses" to raise money. It has \$8 billion invested in the businesses, including broadband telecommunications and the Dabhol power plant in India. Enron expects to get "billions" from the sales, Whalley said, without being more specific.

Enron reported yesterday that its U.S. operations had \$1.2 billion in cash left. It has added at least \$5 billion since Sept. 30 from credit lines, loans and a \$1.5 billion investment from ChevronTexaco, part owner of Dynegy.

Enron used \$1.9 billion of the money it raised to retire commercial paper, which is short-term debt. It gave no details on how it spent the remaining \$3.1 billion.

Enron Chief Financial Officer Jeffrey McMahon said last week that the company also was looking to get another \$500 million to \$1 billion from private investors.

Asset sales valued at about \$800 million are expected to close by the end of this year, according to the SEC filing. Enron spokeswoman Karen Denne wouldn't comment on whether it could sell assets fast enough to keep current on its debts.

Dynegy will have to help Enron sell assets, said Mitchell Stapley, who manages \$3.5 billion in fixed-income assets including Enron bonds for Fifth Third Investment Advisors Inc.

Dynegy and ChevronTexaco Corp., which owns 26 percent of Dynegy, also will have to help Enron negotiate with its lenders, said Kathleen Vuchetich, who helps manage the \$1.4 billion Strong American Utilities Fund, which is 5 percent Dynegy shares.

Debt Questioned

"I never dreamt (the \$9.15 billion) would be that large, coming due all at once," Vuchetich said. "It calls into question their decision to schedule it that way in the first place."

ChevronTexaco, the second-largest U.S. oil company, is providing \$2.5 billion in cash as part of the Enron buyout. It provided the first \$1.5 billion a week ago.

Shares of ChevronTexaco, based in San Francisco, rose \$3.62 to \$86.53.

Enron yesterday reduced third-quarter results by 3 cents a share, bringing the period's loss to 87 cents, or \$664 million. On Nov. 8, Enron lowered earnings back to 1997 by \$586 million to reflect losses by affiliated partnerships that were wrongly kept off the books. That included a third-quarter reduction of \$17 million.

A drop in Enron's senior unsecured debt rating to "BBB-" by Standard & Poor's on Nov. 12 may force Enron to pay off a \$690 million note by Nov. 27 if it doesn't find collateral to guarantee the debt taken on by an affiliated partnership that owns Brazilian natural-gas assets, the filing said.

Without repayment or collateral, investors can begin to liquidate the partnership's assets, Enron said. The company said it's working with lenders to come up with an acceptable agreement on the debt.

Making good on debt owed by its Whitewing affiliated partnership may cut Enron's fourth-quarter earnings, Enron said. Enron is obligated to back Whitewing by issuing junior convertible preferred stock. Because Enron's stock has plunged, it may have to write down its assets by \$700 million, the filing said.

Tracking:

Recipient	Delivery	Read
Wiedman, Mark	Delivered: 11/20/01 4:43 PM	read: 11/20/01 4:58 PM
Nickoloff, Peter	Delivered: 11/20/01 4:43 PM	read: 11/20/01 4:43 PM
Cetina, Jill	Delivered: 11/20/01 4:43 PM	Deleted: 1/3/02 10:55 AM
Sharer, James	Delivered: 11/20/01 4:43 PM	read: 11/20/01 5:25 PM
Berardi, Steve	Delivered: 11/20/01 4:43 PM	read: 11/21/01 8:07 AM
Pietrangoli, Fred	Delivered: 11/20/01 4:43 PM	read: 11/21/01 9:11 AM
Schultheiss, Heidlynn	Delivered: 11/20/01 4:43 PM	read: 1/2/02 11:48 AM
Whaley, Jean	Delivered: 11/20/01 4:43 PM	read: 11/21/01 9:54 AM

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By Stacie Babula

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Tracing:

Recipient
Cesbora, Brian

Delivery
Delivered: 11/20/01 4:41 PM

Head
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recipient

Bair, Sheila
Bitsberger, Timothy

Delivery

Delivered: 11/20/01 4:41 PM
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read

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read: 11/20/01 4:53 PM

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 9:18 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron

October 29, 2001

Money & Investing

Enron Is in Discussions With Banks For Credit Line of up to \$2 Billion

By JATHON SAPSFORD and JOHN EMSHWILLER

Staff Reporters of THE WALL STREET JOURNAL

Enron Corp., scrambling to restore confidence in its finances, is negotiating with banks for a new credit line of between \$1 billion and \$2 billion, and is likely to close a deal within days, according to officials familiar with the matter.

The new credit line is intended to bolster Enron's financial condition and head off a potentially devastating loss of investor and business confidence. The new credit would supplement existing lines, which are largely tapped out after **Enron** last week drew down about \$3 billion to increase cash reserves and calm fears in the stock, bond and energy markets.

An **Enron** spokesman confirmed that the company is negotiating a new credit line, but said he couldn't supply any further details. Houston-based **Enron** is the nation's biggest energy trader and a principal in nearly one-quarter of all electricity and natural-gas trades. Once a favorite of Wall Street, the company now is in the unfamiliar position of convincing a deeply concerned investment community that, despite difficulties, its finances remain sound.

Confidence in Enron's situation was shaken after **Enron** earlier this month announced a \$618 million third-quarter loss and disclosed a \$1.2 billion erosion of shareholder equity related to controversial transactions it had done with entities connected to its then-chief financial officer, Andrew Fastow.

[Enron]

Last week, **Enron** replaced Mr. Fastow and said that the Securities and Exchange Commission was looking into the transactions. The company has consistently said that the transactions were proper and legal.

Enron's stock price fell again Friday. As of 4 p.m., in composite trading on the New York Stock

Exchange, **Enron** was down 95 cents at \$15.40. **Enron** has fallen 50% in the past two weeks and is down 83% from a Sept. 18, 2000, high of \$89.63.

Late last week, **Enron** tapped its existing credit lines, with part of that money being used to redeem nearly \$2 billion of its outstanding commercial paper, or short-term corporate IOUs. Ron Barone of credit-rating agency Standard & Poor's said he believes that **Enron** was "getting a bit more resistance" recently in rolling over its commercial paper as it came due. Thus, **Enron** probably decided it would be easier simply to redeem the paper outstanding, he said.

The **Enron** spokesman Sunday said that paying off the commercial paper and still leaving the company with an additional roughly \$1 billion cash on hand would give it more financial flexibility.

Also last week, credit-rating agencies warned investors they were reviewing Enron's debt and commercial-paper ratings for a possible downgrade. A lower rating could hamper Enron's core trading businesses.

Behind the worries among these agencies, in part, is the loss of investor confidence, which one of the rating companies, Fitch, said in a report last week could impair "Enron's financial flexibility and access to capital markets, therefore impacting its ability to conduct its business."

The **Enron** spokesman said the company's trading partners are doing business with **Enron** on "essentially the same terms" as they have in the past. "There has been no significant change in the credit conditions," he said. Trading partners demanding significantly stricter terms from **Enron** would be a sign of further deteriorating confidence in the energy giant's finances. The banks involved in the negotiations, including J.P. Morgan Chase & Co. and Citigroup Inc., are asking **Enron** for stricter covenants on the new credit line than they had asked for in the past, one official said.

Bankers involved with the company say the goal of the new credit line is to show the investment community that **Enron** can meet its commitments. "Confidence in this company was lost," said one bank official involved in the negotiations for a new credit line. "But confidence will be restored."

Corporations of Enron's size commonly establish credit lines only to demonstrate to the investment community that in case of an emergency, they have access to cash. In practice, few companies actually make use of these lines. Thus, drawing down credit lines, while providing immediate cash, also illustrates the pressure **Enron** is feeling.

Write to Jathon Sapsford at jathon.sapsford@wsj.com <<mailto:jathon.sapsford@wsj.com>> and John

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 9:20 AM
To: Schultheiss, Heidlynn; Nickoloff, Peter
Subject: WSJ:Enron

October 29, 2001

Manager's Journal

How Enron Ran Out of Gas

By Paul Kedrosky. Mr. Kedrosky is a professor of business at the University of British Columbia.

Is troubled **Enron** Corp. the Long Term Capital Management of the energy markets, or merely yet another mismanaged company whose executives read too many of their own press releases? Or is poor **Enron** just misunderstood? Those are the questions after another week of Chinese water torture financial releases from the beleaguered Houston-based energy concern.

A year ago **Enron** was the hottest of the hot. While tech stocks were tanking, Enron's shares gained 89% during 2000. Even die-hard **Enron** skeptics -- of which there are many -- had to concede that last year was a barnburner for the company. Earnings were up 25%, and revenues more than doubled.

Not bad, considering where the company came from. A decade ago 80% of Enron's revenues came from the staid (and regulated) gas-pipeline business. No longer. **Enron** has been selling those assets steadily, partly fueling revenues, but also expanding into new areas. By 2000, around 95% of its revenues and more than 80% of its profits came from trading energy, and buying and selling stakes in energy producers.

The stock market applauded the move: At its peak, **Enron** was trading at around 55 times earnings. That's more like Cisco's once tropospheric valuation than the meager 2.5 times earnings the market affords **Enron** competitor Duke Energy.

But **Enron** management wanted more. It was, after all, a "new economy" Web-based energy trader where aggressive performers were lucratively rewarded. According to **Enron** Chairman and CEO Ken Lay, the company deserved to be valued accordingly. At a conference early this year he told investors the company's stock should be trading much higher -- say \$126, more than double its price then.

Then the new economy motor stalled. The company's president left under strange circumstances. And rumors swirled about Enron's machinations in California's energy markets. Investors pored over Enron's weakening financial statements. But **Enron** analysts must have the energy and persistence

of Talmudic scholars to penetrate the company's cryptic financials. In effect, Enron's troubles were hiding in plain sight.

It should have been a warning. Because of the poor financial disclosure there was no way to assess the damage the economy was doing to the company, or how it was trying to make its numbers. Most analysts blithely concede that they really didn't know how **Enron** made money -- in good markets or bad.

Not that **Enron** didn't make money, it did -- albeit with a worryingly low return on equity given the capital required -- but sometimes revenues came from asset sales and complex off-balance sheet transactions, sometimes from energy-trading revenues. And it was very difficult to understand why or how -- or how likely it was **Enron** could do it again next quarter.

Enron's financial inscrutability hid stranger stuff. Deep inside the company filings was mention of LJM Cayman, L.P., a private investment partnership. According to Enron's March 2000 10-K, a "senior officer of **Enron** is the managing member" of LJM. Well, that was a puzzler. LJM was helping **Enron** "manage price and value risk with regard to certain merchant and similar assets by entering into derivatives, including swaps, puts, and collars." It was, in a phrase, Enron's house hedge fund.

There is nothing wrong with hedging positions in the volatile energy market -- it is crucial for a market-maker. But having an **Enron** executive managing and benefiting from the hedging is something else altogether, especially when the **Enron** executive was the company's CFO, Andrew Fastow. While he severed his connection with LJM (and related partnerships) in July of this year -- and left **Enron** in a whirl of confusion last week -- the damage had been done.

As stories in this paper have since made clear, Mr. Fastow's LJM partnership allegedly made millions from the conflict-ridden, board-approved LJM-Enron relationship. And recently **Enron** ended the merry affair, taking a billion-dollar writedown against equity two weeks ago over some of LJM's wrong-footed hedging. Analysts, investors, and the Securities & Exchange Commission were left with many questions, and very few answers.

To be fair, I suppose, **Enron** did disclose the LJM arrangement more than a year ago, saying it had erected a Chinese wall between Fastow/LJM and the company. And in a bull market, no one paid much attention to what a bad idea that horribly conflicted relationship was -- or questioned the strength of the wall. Now it matters, as do other Enron-hedged financings, a number of which look to have insufficient assets to cover debt repayments due in 2003.

We didn't do anything wrong is Mr. Lay's refrain in the company's current round of entertainingly antagonistic conference calls. That remains to be seen, but at the very least the company has shown terrible judgment, and heroic arrogance in its dismissal of shareholders interests and financial transparency.

Where has Enron's board of directors been through all of this? What kind of oversight has this motley collection of academics, government sorts, and retired executives exercised for **Enron** shareholders? Very little, it seems. It is time Enron's board did a proper investigation, and then cleaned house -- perhaps neatly finishing with themselves.

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 9:21 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: DJ: Enron

October 28, 2001

Enron Asks Banks For Additional Credit -FT

NEW YORK -- **Enron** Corp. (ENE) is attempting to persuade banks to provide additional credit, The Financial Times reported on its Web site Sunday.

The company was also due to hold a special board meeting Sunday to consider confidence-building measures after surprise financial disclosures damaged its reputation among U.S. investors, The Financial Times reported.

The Financial Times quoted **Enron** spokesman Mark Palmer as saying he hoped the company could have something to announce in coming days as a result of its latest effort to "establish additional lines of liquidity."

"Once we are able to the liquidity position shored up, that will put a lot of fears of the unknown to rest," The Financial Times quoted Palmer as saying.

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 9:23 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron sues Microsoft

October 26, 2001

Enron Sues Microsoft Over Failed Broadband Services Deal

By **MICHAEL RIEKE**

OF DOW JONES NEWSWIRES

HOUSTON -- In a July conference call with analysts when Jeff Skilling was still chief executive of **Enron Corp.** (ENE), he threw out a ray of hope for his company's foundering broadband business.

Enron Broadband Services had just signed a long-term deal to provide bandwidth for MSN, Microsoft Corp.'s (MSFT) online Internet service, Skilling said. **Enron** would give more details on the deal later.

After three months without farther word on the deal, **Enron** has broken its silence by suing Microsoft.

In a suit filed Thursday in the district court of Harris County, Texas, **Enron** claimed Microsoft has failed to live up to terms of the deal.

The agreement, signed June 25, called for **Enron Broadband** to develop and provide network capacity and other services to support Microsoft's offering of high-speed Internet service, according to the lawsuit.

Microsoft was required to develop an electronic ordering and billing system for use with all regional Bell telephone companies during an initial phase of the deal, according to the lawsuit.

Microsoft has failed to provide that system and other items required in the deal, so **Enron** isn't required to deliver operational broadband services for the deal, the lawsuit said.

Microsoft sent **Enron** a letter dated Oct. 23 saying that if **Enron** didn't provide an operational broadband system by Oct. 25, **Enron** would have breached the contract, the lawsuit said. Microsoft then would be entitled to recover damages.

The suit also said Microsoft failed to provide monthly subscriber growth forecast required by the deal.

In a third breach of the contract, the suit claimed, Microsoft made public announcements about the subject of the agreement without getting **Enron's** prior approval.

An **Enron** official told Dow Jones Newswires that Microsoft had issued a press release Oct. 15 about the service but that **Enron** wasn't mentioned in the release.

A Microsoft news release dated Oct. 15 announced what the company calls MSN 7, a new version of the MSN network which includes high-speed, or broadband, access to the Web. The service was to be available on Oct. 25.

The Microsoft release said MSN 7 would deliver "state-of-the-art" video and audio through "dramatically improved" broadband technology. The new service would extend MSN broadband service "to more than 29 million households in 45 markets."

By the end of the first quarter of 2002, the Microsoft release said, the MSN broadband service would be available to more than 90% of U.S. households capable of using high-speed digital subscriber line access.

The **Enron** lawsuit asked that Microsoft be declared in breach of contract. It also asked that **Enron** be allowed to recover unspecified damages as well as costs stemming from the lawsuit.

Neither **Enron** nor Microsoft have responded to requests for comment on the lawsuit.

The Microsoft deal is the second failed broadband agreement. In July 2000, **Enron** and Blockbuster Video, a unit of Viacom Inc. (VIA), announced a deal to deliver movies over the Internet.

That deal fell apart in March of this year when Blockbuster said Enron's fiber-optic network couldn't deliver the service on a dependable basis. **Enron** countered that Blockbuster couldn't deliver the quality and quantity of movies needed for a successful video-on-demand service.

-By Michael Rieke, Dow Jones Newswires; 713-547-9207; michael.rieke@dowjones.com

Because of the failure of the **Enron** Broadband Services-Microsoft deal, MSN will have to temporarily limit delivery of its new high-speed Internet services to the 14 states covered by Qwest Communications International Inc. (Q), said Bob Visse, director of MSN marketing.

Those 14 states are Arizona, New Mexico, Colorado, Wyoming, Idaho, Iowa, Minnesota, South Dakota, North Dakota, Montana, Nebraska, Oregon, Utah and Washington.

The **Enron** deal was to provide backbone services outside of the Qwest area, Visse said. Backbones provide longhaul services that connect smaller areas of networks.

An analyst, who didn't want to be identified, expressed shock when told that the disagreement would limit the new MSN broadband services to the 14-state Qwest region. That calls into question the performance of the entire **Enron** broadband network, he said.

Many different companies can provide the necessary backbone services and MSN will find one, MSN's Visse said.

The new service was just launched Thursday so there weren't existing customers in the areas outside the Qwest region, he said.

Visse wouldn't comment on the lawsuit filed by **Enron** because Microsoft hasn't reviewed it in detail. Commenting would violate the nondisclosure agreement Microsoft has with **Enron**, he added.

"We do believe we have fully upheld the terms of the agreement," he said.

Microsoft hasn't filed a lawsuit against **Enron** relating to the deal, he added. He wouldn't comment on

the possibility of such a suit.

In recent trading, shares of **Enron** were down 66 cents, or 4.04%, to \$15.69. Shares of Microsoft were off 15 cents, or 0.25%, at \$62.63.

-By Michael Rieke, Dow Jones Newswires; 713-547-9207;

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Subject: WSJ 10/26 Enron

October 26, 2001

Money & Investing

Enron's Financial Troubles Reverberate to Its Bonds

By **JATHON SAPSFORD** and **SUZANNE MCGEE**

Staff Reporters of THE WALL STREET JOURNAL

NEW YORK -- **Enron** Corp.'s bonds have held up better than its battered stock amid escalating financial woes at the energy-trading powerhouse.

Not for long, some bond traders say.

In trading Thursday, the Houston energy-trading company's five-year bond, a \$250 million issue due in July 2006 carrying a coupon of 6.4%, was quoted at 82 cents on the dollar, down from a bid of 88 late Wednesday, and representing a 16% drop during the past two weeks.

Still, that is far less than the 50% decline in Enron's stock price since the Oct. 16 disclosure of a \$1.01 billion charge linked to soured investments, resulting in a \$618 million third-quarter loss. But the fall in the bond's price translates to a yield of 7.7 percentage points above bellwether U.S. government bonds, which is a widening from about three percentage points two weeks ago. Although **Enron** still is an investment-grade credit, that kind of "spread" is more characteristic of a junk bond with a credit rating of single B or lower.

At the same time, it is becoming nettlesome to trade big blocks of **Enron** bonds. Thursday's 82 bid, for instance, was for a block of less than \$2 million in bonds, a small percentage of a typical trade. This poor liquidity underscores the uncertainties affecting not only **Enron** but the market as a whole.

Driving the bond-price drop are fears among investors that credit-rating concerns will lower ratings on **Enron** debt after it conceded earlier during the week a number of troubles, including losses in the wake of questionable investments, a Securities and Exchange Commission investigation, and the sudden resignation of its chief financial officer.

"Even at these levels, there's very little buying interest," said Harold Rivkin, a principal at distressed-debt trader H. Rivkin & Co. in Princeton, N.J.

In one sign of the ripple effects, the price investors pay to protect themselves from losses on **Enron** debt was surging. The cost of a "default swap" -- in which an investor pays another investor to take a chunk of debt at face value in the event of default -- rose to 10% of the size of the credit being insured. That was up from 8% a day earlier, and more than holders of Lucent Technologies Inc. debt had to pay at the height of that technology company's troubles earlier during the year.

Even with its woes, **Enron** remains an investment-grade company. Most credit-rating agencies rate Enron's senior unsecured debt at several notches above the noninvestment-grade level.

Yet Fitch said Thursday it put Enron's credit rating on watch for a possible downgrade, following a similar move by Moodys Investors Service earlier during the week. (Standard & Poor's, a division of McGraw Hill Cos., stopped short of putting the company on its Creditwatch list, opting instead to revise its long-term ratings outlook to "negative," citing concerns about the company's financial flexibility.)

Meanwhile, the weak bond prices are a sign that the markets are bracing for the worst. "These are investment-grade bonds that are migrating toward distressed levels," said Glenn Reynolds, an analyst at Credit Sights Inc., an independent fixed-income research firm in New York.

If Enron's credit ratings fall, it would have implications far beyond the company's ability to raise money. As an energy trader, a credit downgrade sends a signal to other participants in crucial markets about its ability to make good on its commitments.

Enron makes markets in a variety of commodities. Though it is best known for trading electricity and natural gas, the company also is a huge force in the markets for other commodities such as lumber, metals, bandwidth capacity and steel. As a market maker matching buyers and sellers, **Enron** handles about a quarter of all the trading in the nation's energy and gas markets.

Enron's credit-worthiness is hugely important. The better its credit rating, the cheaper it can hedge, or offset, its positions in all these commodities markets through derivatives and pass on savings to customers. Without that credit rating, the cost of this high-margin, high-volume business starts to rise. A derivative is an instrument whose value is linked to, or derived from, that of an underlying security or asset, such as a stock, bond or commodity.

"Even if the company does retain its investment-grade rating, the perception that this might be at risk will start to affect their core businesses," said Mr. Reynolds at Credit Sights Inc. "Any prudent risk [manager] at Enron's counterparties" -- any institution on the other end of a financial agreement with **Enron** -- "is going to be examining their exposure to **Enron**, and looking for ways to minimize it or offset it," Mr. Reynolds said.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:19 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: More Enron

October 26, 2001

Tech Center

Enron Sues Microsoft in Spat Over Deal to Support MSN

A WALL STREET JOURNAL ONLINE News Roundup

HOUSTON -- **Enron** Corp. sued Microsoft Corp., accusing the software giant of failing to live up to the terms of a deal in which **Enron** agreed to provide bandwidth for the MSN online service.

The suit was filed Thursday in the district court of Harris County, Texas.

According to the lawsuit, the deal called for Enron's broadband unit to develop and provide network capacity and other services to support Microsoft's offering of high-speed Internet service.

Microsoft, in return, was required to develop an electronic ordering and billing system for use with all regional Bell telephone companies during an initial phase of the deal. **Enron** charges that since Microsoft has failed to provide that system and other items required in the deal, **Enron** isn't required to deliver the broadband services required of it.

The suit also said Microsoft failed to provide monthly subscriber growth forecast required by the deal, and that Microsoft made public announcements about the subject of the agreement without getting Enron's prior approval.

An **Enron** official said Microsoft had issued a press release Oct. 15 about the service, but that **Enron** wasn't mentioned in the release. A Microsoft news release dated Oct. 15 announced what the company calls MSN 7, a new version of the MSN network which includes high-speed access to the Web. The service was to be available on Oct. 25. The release said MSN 7 would deliver "state-of-the-art" video and audio through "dramatically improved" broadband technology. The new service would extend MSN broadband service "to more than 29 million households in 45 markets."

By the end of the first quarter of 2002, the Microsoft release said, the MSN broadband service would be available to more than 90% of U.S. households capable of using high-speed digital subscriber line access.

According to the lawsuit, Microsoft sent **Enron** a letter dated Oct. 23 saying that if **Enron** didn't provide an operational broadband system by Oct. 25, **Enron** would have breached the contract and Microsoft would be entitled to recover damages.

The **Enron** lawsuit asked that Microsoft be declared in breach of contract and that **Enron** be allowed to recover unspecified damages as well as costs stemming from the lawsuit.

Neither **Enron** nor Microsoft responded to requests for comment on the suit.

The deal was signed June 25 and announced by Enron's then-chief executive Jeffrey K. Skilling in a July conference call with analysts. It came as a ray of hope for his company's foundering broadband business.

Mr. Skilling promised more details would be in the offing, but none came. Mr. Skilling stepped down as CEO in August, citing personal reasons, but analysts suggested a sharp decline in the Houston firm's stock might have spurred his departure. Enron's stock price was hurt as the federal government tried to curb high power prices that had helped **Enron** achieve record earnings. Meanwhile, investors had also cooled on Enron's aggressive push beyond its gas-pipeline business into broadband telecommunications markets, a strategy identified with Mr. Skilling.

Since then, the news has only gotten worse for **Enron**: Its stock has been hammered amid heavy losses and news that the Securities and Exchange Commission is conducting an inquiry into billions of dollars of transactions it did with entities connected to its former chief financial officer. On Thursday, the company drew down about \$3 billion -- the bulk of its available bank credit lines -- in a bid to restore confidence in its financial strength and liquidity (see article).

Mr. Skilling had taken over from the CEO spot from Kenneth Lay in late 2000 after a long stint as president and chief operating officer. Before that, he advised Mr. Lay as a McKinsey & Co. consultant. The two men were largely credited with building **Enron** into a formidable commodities market player over the past decade, trading everything from electricity to weather derivatives. In doing so, **Enron** shed many of its power-production assets, a tactic advocated by Mr. Skilling.

Enron and several other big energy companies have spent billions of dollars building fiber-optic networks, which they can string along their utility rights of way. But Enron's ambitions were always even larger -- in July 2000, for example, the company signed a 20-year exclusive agreement with Blockbuster Inc. to deliver movies on demand to U.S. and European homes via high-speed phone lines. That deal fell apart in March: Blockbuster said Enron's fiber-optic network couldn't deliver the service on a dependable basis, and **Enron** countered that Blockbuster couldn't deliver the quality and quantity of movies needed for a successful video-on-demand service.

—Michael Rieke of Dow Jones Newswires contributed to this article.

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:21 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron: Heard on the Street

October 26, 2001

Heard on the Street

Despite Losses, Complex Deals Analysts Remain High on Enron

By **SUSANNE CRAIG** and **JONATHAN WEIL**

Staff Reporters of THE WALL STREET JOURNAL

Enron: Rarely have so many analysts liked a stock they concede they know so little about.

In recent years, Wall Street researchers have been overwhelmingly -- critics would say blindly -- enthusiastic about **Enron**, even as they acknowledge not always understanding the complex financial transactions that accounted for its soaring profits. Now, **Enron** is reporting steep losses from some of its most complicated transactions, which many on Wall Street still can't figure out.

In a research note Wednesday, Goldman Sachs analyst David Fleischer conceded that scant corporate disclosure at the Houston energy trader makes it difficult to value the company. The company's "lack of disclosure and transparency," he says, is "a longstanding **Enron** hallmark."

So is this a stock to avoid, in his view? Hardly. Goldman on Wednesday did bump **Enron** off its "U.S. Select List," which consists of a few dozen top stock picks -- but Mr. Fleischer continued to keep the stock on the firm's larger but prestigious "Recommended List" of 200 or so favored stocks, where it has been since he joined Goldman in 1993.

"Just because I can't be specific in being able to create a simple model ... doesn't mean that you write off that industry and say 'I can't analyze it' or 'I can't figure it out,'" says Mr. Fleischer, who owns an undisclosed number of **Enron** shares. "If that were the case, there would be an awful lot of industries we couldn't follow."

Enron's shares have dropped about 50% since last week.

"Every sell-side analyst we spoke to early in 2001 admitted that this was a black box," says Jim Chanos, principal of Kynikos Associates in New York, who has been selling **Enron** stock short -- trading it with an eye to profiting from its fall -- throughout this year. "It was really a trust-me story, when all the evidence was mounting that there was reason to question that level of trust."

True, no stock picker is immune from bad calls. And Wall Street analysts long have been criticized for their overwhelmingly bullish bias, particularly on stocks in hot sectors with lots of investment-banking deals to be had.

But **Enron** stands apart, precisely because so many of the analysts still recommending the stock have acknowledged that the company's disclosure practices are lacking. Which raises the question: How can an analyst recommend that others purchase a stock when key information about the company's operations is so often either unavailable or indecipherable?

Concerns about the way that **Enron** runs its business aren't new. Many of the issues now plaguing Enron's stock were first raised more than a year ago by bearish hedge-fund managers and independent accounting experts. Yet time and again, Wall Street analysts dismissed as unimportant many of the lingering questions about the company's various partnership transactions.

Besides those partnerships, **Enron** also has been dogged by concerns about the secretive valuation techniques it uses to record its assets and earnings.

Through it all, most analysts have stuck by this onetime stock-market darling, publicly dismissing questions about the firm's accounting practices and level of disclosure. As of Thursday, of the 17 analysts who following the stock, 10 had a "strong buy" or equivalent rating on the stock, according to Thomson Financial/First Call. Five others rated the stock a "buy," though not strongly.

Only Prudential Securities, which downgraded the stock this week, has a "sell" rating on **Enron**.

The bullish treatment is the latest and one of the most high-profile examples of Wall Street taking a glass half-full stance, despite what in retrospect seems to be ample warning that a less-enthusiastic approach was warranted.

Over the past year in the wake of the Nasdaq Composite Index's general collapse, analysts have been widely assailed for a lack of independence -- particularly those who, like Goldman's Mr. Fleischer, own shares in the companies they cover. Regulators have raised concerns that analysts have compromised themselves to help their firms land lucrative investment-banking fees and other revenue.

[Go]Enron Officials Sell Shares Amid Stock-Price Slump

[Go]Enron Taps \$3 Billion From Bank Lines in Pre-Emptive Move to Ensure Liquidity

Enron has spread the wealth across many Wall Street firms. For instance, for one \$865 million equity offering in 1999 led by Credit Suisse First Boston, **Enron** retained seven co-managers, including Donaldson Lufkin & Jenrette, Lehman Brothers and Merrill Lynch.

"**Enron** is a big company, and I don't think you're going to find a firm that hasn't been involved," says Credit Suisse First Boston analyst Curt Launer, who still rates the stock a "strong buy" with a \$40 price target. "They pay a lot of investment-banking fees to Wall Street."

He adds, "We do our analysis every day based on the information we have. Are we here strictly to defend companies? That's ludicrous. We're here to provide information to investors. ... Yes, I have the wrong recommendation on the stock. I don't think my analysis has been as wrong as the stock has performed."

Mr. Fleischer, whose firm also has served as an investment banker to **Enron**, calls his holding "a meaningful investment" that is "not small." But he disputes any suggestion that his objectivity is compromised. Mr. Fleischer says his clients "are happy to know" he has a stake in **Enron**, because it shows he puts his money where his mouth is.

In his research note Wednesday, Mr. Fleischer called for complete disclosures of Enron's off-balance sheet partnerships. Despite the resulting difficulty he acknowledged facing in developing financial models for the company, he wrote that he and many other investors historically "have given **Enron** the benefit of doubt because of its strong growth in earnings" and position as an industry leader.

"There's not information to really model this and be able to predict accurately where revenues are going to come from and where they're going to make their money, but every quarter they do," he says. "It's hard to get inside to know all the transactions, but they do deliver."

CSFB's Mr. Launer also has been a longtime defender of the company, occasionally issuing research reports to rebut critical stories about **Enron** in the financial press. On Monday, he wrote that he expects questions about Enron's partnerships and accounting disclosures to continue, but that he remains "confident in the businesses and operating growth prospects for [**Enron**] and an ultimate recovery in the share price."

"I know I'm wrong on the stock," Mr. Launer says. But he says that at these prices, he isn't ready to throw in the towel because he figures that even in a worst-case scenario – under which he envisions **Enron** having to issue as much as \$2 billion worth of shares, diluting current holders – the stock doesn't have much further to fall.

Clearly, Messrs. Launer and Fleischer aren't alone. "Even in relative terms, analysts remain very bullish on this stock," says Chuck Hill, director of research at Thomson Financial/First Call. The average rating for a stock on Wall Street is 2.2, or slightly shy of a "buy" rating. **Enron** scores a 1.6. "This may turn into a classic case of locking the barn door after the bad news is out," Mr. Hill says.

In downgrading the stock this week, Prudential analyst Carol Coale bumped it to "sell" from "buy," with a brief stop at "hold." While she is the only analyst to recommend investors sell the stock, she openly concedes her recent downgrades come "too little, too late."

Ms. Coale says **Enron** has been difficult to cover for years. She says the company's disclosure practices fall far short of ideal, and senior executives are often evasive, even when presented with direct questions. For instance, she says three weeks ago she asked **Enron** management if the company was under investigation by the Securities and Exchange Commission. They said "no," she says.

In light of the company's acknowledgment this week of an SEC "inquiry," she asked **Enron** about the previous denial. "They told me it is an inquiry, not an investigation," she says. An **Enron** spokeswoman says the company learned of the SEC's inquiry only last Wednesday.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:22 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron Official Sell Shares

October 26, 2001

Money & Investing

Enron Officials Sell Shares Amid Stock-Price Slump

By THEO FRANCIS and CASSELL BRYAN-LOW
Staff Reporters of THE WALL STREET JOURNAL

Officials at Enron Corp., whose unusual transactions with its chief financial officer are under regulatory scrutiny, have steadily sold sizable amounts of their holdings of company stock as the share price has fallen this year.

Corporate officials had sold 1.8 million shares valued at about \$106 million through July, as the stock fell to less than \$45 a share from \$83 at the start of the year. Since July, the stock has plummeted an additional 63% to \$16.35, including a 50% plunge since the beginning of last week.

Kenneth Lay, chief executive of the Houston energy-trading company, cashed in shares for \$25.7 million so far this year, usually in transactions paired with options exercises. He sold 429,614 shares, leaving him with some 2.8 million shares as of July, the latest data available on his sales, according to Thomson Financial/Lancer Analytics.

The dollar amount for his 2001 sales is approaching the total for all Mr. Lay's sales of Enron shares for 2000, which reached \$30.7 million. In 1999, he sold shares for a total of \$26 million.

In Houston, an Enron spokeswoman declined to comment on the figures, saying the company doesn't keep a running tally of stockholdings by corporate officials. Enron also wouldn't comment on the number of options held by company insiders and called the sales "a personal decision." Many sales by Enron insiders were concurrent with options exercises or sales followed soon after option exercises.

Strong selling by company officers and directors amid share-price declines should raise red flags for investors, says Jonathan Moreland, research director of InsiderInsights.com, who uses insider-trading data to zero in on investment ideas.

[Go]Enron Taps \$3 Billion From Bank Lines in Pre-Emptive Move to Ensure Liquidity

[Go]Despite Losses, Complex Deals Analysts Remain High on Enron

[Go]Enron's Financial Troubles Reverberate to Its Bonds

Among other insiders selling during the year, Kenneth Rice, former chairman and CEO of Enron's broadband unit, sold shares for \$23.7 million. Mr. Rice has sold 456,966 shares of the 1.5 million shares he was listed as owning in Enron's March proxy filing. Former Enron Chief Executive Jeffrey Skilling -- who resigned in August -- sold 160,000 shares for \$9.8 million during the year. In March, Mr. Skilling owned 1.9 million shares.

Messrs. Rice and Skilling couldn't be reached to comment.

Overall, Enron's insiders were busier selling shares last year, when they sold 5.8 million shares for about \$449 million. During 1999, insiders sold 3.4 million shares for \$123.1 million.

Since December 1999, only one Enron executive has reported buying company shares. The buyer was Andrew Fastow, who was ousted during the week as Enron's chief financial officer after the company disclosed it was under a Securities and Exchange Commission investigation into financial ties between the company and Mr. Fastow.

Mr. Fastow reported purchasing 10,000 Enron shares in August at \$36.98 each, or a total of \$369,800. Today, those shares are valued at \$163,500, based on Enron's stock price of \$16.35 in 4 p.m. New York Stock Exchange composite trading. After the purchase, Mr. Fastow owned 110,586 shares, Thomson Financial/Lancer Analytics says.

Enron said Mr. Fastow wasn't available to comment.

On Monday, a New York law firm filed suit in U.S. District Court in Houston, alleging that Enron misrepresented its performance by failing to disclose problems with its broadband division and failing to properly write down the value of investments in limited partnerships managed by Mr. Fastow. The suit, which seeks class-action status, also says Enron insiders sold \$73 million of their own Enron holdings during parts of 2000 and 2001.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:24 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron Taps

October 26, 2001

Money & Investing

Enron Taps \$3 Billion From Bank Lines In Pre-Emptive Move to Ensure Liquidity

By JOHN R. EMSWILLER, REBECCA SMITH and JATHON SAPSFORD

Staff Reporters of THE WALL STREET JOURNAL

Enron Corp. drew down about \$3 billion, the bulk of its available bank credit lines, in a bid to restore confidence in its financial strength and liquidity.

Enron will use part of the money to offer to redeem about \$1.85 billion of outstanding commercial paper -- short-term corporate IOUs -- according to a person familiar with the matter, with the remainder providing the energy concern with a cash cushion. Some observers believe the move is a pre-emptive step by Enron to ensure that it had adequate liquidity should its access to bank lines be interrupted. The person also said Enron was talking to its banks about a new, multibillion-dollar credit line.

Enron insists its business operation and financial condition remain strong. But, "when the market is reacting as irrationally as it has been the last few days, we thought that cash was better than a commitment from a bank," said an Enron spokesman. In a statement, the company's new chief financial officer, Jeff McMahon, said that by drawing down the bank lines, "we are making it clear that Enron has the support of its banks and more than adequate liquidity to assure our customers that we can fulfill our commitments."

The move underscored the tumultuous conditions that have been sweeping over the Houston energy-trading concern in the past 10 days. Enron is the nation's largest energy trader and is a principal in nearly one-quarter of all electricity and natural-gas trades. Thursday, for example, Enron was involved in about \$4 billion of deals through its EnronOnline unit.

[\[Go\]Despite Losses, Complex Deals Analysts Remain High on Enron](#)

[\[Go\]Enron Officials Sell Shares Amid Stock-Price Slump](#)

[\[Go\]Enron's Financial Troubles Reverberate to Its Bonds](#)

Since early last week, Enron's share price has plummeted 50%. Last week, it reported a \$618 million third-quarter loss and a reduction in shareholder equity of \$1.2 billion. It also disclosed that the Securities and Exchange Commission is conducting an inquiry into billions of dollars of transactions it did with entities connected to its former chief financial officer, Andrew S. Fastow, who was replaced Wednesday.

The draw-down of the credit facilities came as one rating agency, Fitch, put Enron on review for a possible downgrade, while another, Standard & Poor's, changed Enron's credit outlook to negative from stable. Moody's Investors Service already has said it is looking at a possible downgrade of Enron. In order to fall below investment grade, Enron's credit rating would have to fall several notches.

If that were to happen, however, a host of bad consequences could follow. Together with the sharp decline in its stock price, a noninvestment-grade rating would throw the company into default on obligations involving billions of dollars of borrowings. In that event, Enron could be forced to issue millions of shares of stock to holders of that debt, diluting the value of existing shares. At 4 p.m. Thursday in New York Stock Exchange composite trading, Enron was down six cents at \$16.35.

Liquidity is a key issue for Enron, which handles energy-trading volumes more than triple its next-biggest competitor, American Electric Power Co. Enron's EnronOnline Internet-based trading platform has transacted more than \$884 billion of trades since it was created in November 1999.

The company's wildly successful wholesale unit has been dragged down by underperforming assets elsewhere in the company, chiefly the approximately \$6.5 billion of international assets such as its Dabhol power project in India. Raising cash and retiring debt largely is a timing issue. The cash needs of its trading operation are immediate; it takes time to sell assets, particularly in today's slower economy.

The company also is suffering from a string of disclosure controversies that have damaged its credibility, particularly in connection with its dealings with Mr. Fastow, the former chief financial officer. Internal documents related to one of the Fastow partnerships disclose that Enron also did as much as hundreds of millions of dollars of business with an entity connected to another company official, who has since left Enron. While Enron disclosed its Fastow-related transactions in SEC filings, a computerized search of the SEC's database of public filings produced no reference to this other employee-related entity known as Chewco.

Chewco was established in 1997 "with approximately \$400 million in capital commitments" to buy an interest in Enron assets, according to one of the partnerships documents. The document didn't further specify what assets were purchased, and it didn't disclose the financial impact of the transactions for either Chewco or Enron. Chewco was being run by Michael Kopper, a managing director in Enron's Global Equity Markets Group, according to the document.

Enron, which has maintained that its complex financial transactions with employee-related entities were legal and properly disclosed, didn't have any comment regarding its dealings with Chewco.

Mr. Kopper, who Enron says left the company this year to focus on helping to run the Fastow-related partnerships, didn't return phone calls. A person at his office in Houston Thursday said Mr. Kopper was traveling. In response to questions about Chewco, an Enron spokesman would say only that "Michael Kopper was never an executive officer of Enron." Mr. Fastow repeatedly has declined interview requests. He severed his relationships with the partnerships in July.

This statement is an apparent reference to SEC disclosure regulations regarding related-party transactions. Under SEC rule S-K, a company has to report any transaction that exceeds \$60,000 and involves "any director or executive officer." By contrast, Mr. Fastow, as CFO, would have fallen into that category, but Mr. Kopper, as managing director of a business unit, presumably wouldn't have.

However, reporting guidance issued by the Financial Accounting Standards Board seems to have a broader definition, one that might include Mr. Kopper. According to FAS Statement 57, a related-party transaction involves a "material" piece of business between the company and a member of management. The statement defines management as directors, top officers, vice presidents in charge of major business units and "other persons who perform similar policy-making functions. Persons without formal titles may also be members of management."

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From: Carleton, Norman
Sent: Monday, October 29, 2001 11:26 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron and Calpine

October 26, 2001

Calpine:No Exposure To Enron; No Calif Pwr Contract Talks

(This article was originally published Thursday)

NEW YORK -- Calpine Corp. (CPN) has no credit exposure to trading partner **Enron** Corp. (ENE), Calpine said Thursday in an earnings conference call. And the company hasn't been contacted by the state of California about renegotiating the billions of dollars in long-term supply contracts the company signed with the state earlier this year.

Calpine's diluted net earnings for the third quarter were 88 cents a share compared with 48 cents for the same quarter last year. Setting Calpine's consistent earnings growth aside, Wall Street analysts in Thursday's conference call focused their questions on trouble spots in the energy industry, like **Enron**, California, and whether the U.S. will have a surplus of electric power stations in a few years.

Moody's has put Enron's credit on watch for possible downgrade, and some of the company's debt is trading like junk bonds in the secondary market this week. Trading partners like Calpine have been asked about their exposure to **Enron**.

"We continue to assess the situation, but right now don't have any net exposure to **Enron**," said Calpine's vice president of corporate risk management, Paul Pasoli. "We continue to trade with them. We will adjust our credit threshold based on how their bonds are trading and their credit rating."

When asked if there would be any exposure to **Enron** if trading were to be halted immediately, Pasoli said that, in fact, Calpine would owe **Enron** a little money.

In another energy industry area of concern, Calpine was asked about the state of California's stated desire to renegotiate tens of billions of dollars of long-term power contracts. Calpine is by far the biggest supplier under those contracts, which on a mark-to-market basis are worth far less now than when California bought this past winter and spring.

"Nobody has come to us directly or indirectly with regard to the Calif contracts. In general, we respect our contracts and expect our counterparties to do so as well," said Calpine chief executive, Peter Cartwright. "If there are any contract renegotiations that can result in a win-win, we would be happy to look at that, if California asks. We've done that many times."

As for future power prices, Calpine said that it's going forward with its program to build a portfolio of 70,000 megawatts of generation, which is about three times its current capacity and would be about 7% of all U.S. capacity. The critical determinant of profitability in power

generation is the difference between natural gas prices and power prices, and Calpine said that difference, or "spark spread," has grown the past few months. Furthermore, the company executives said they are holding to a requirement that all projects generate an after-tax return of 18% on the investment.

As a result, the company expects earnings to grow at least 40% annually

through 2005. Calpine will fund near-term cash needs in the debt markets and won't issue new stock until its stock price rises substantially.

-By Mark Golden, Dow Jones Newswires; 201-938-4604; mark.golden@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:30 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron Replace CFO

October 25, 2001

Major Business News

Enron Replaces Fastow as Finance Chief; Move Follows Concerns Over Partnerships

By REBECCA SMITH and JOHN R. EMSHWILLER

Staff Reporters of THE WALL STREET JOURNAL

Enron Corp. replaced its embattled chief financial officer, Andrew S. Fastow, capping a tumultuous day in which the huge energy company saw its stock price again fall sharply and help pull down the share prices of other major energy-trading companies.

Investors appeared worried that Enron's recent woes could have a destabilizing effect on the energy-trading market. The Houston energy powerhouse, with annualized revenue topping \$150 billion and assets of more than \$60 billion, handles transactions representing roughly one-quarter of the nation's traded-electricity and natural-gas volumes. In less than two years of operation, its EnronOnline trading platform has become a central marketplace for the energy business and already has handled more than \$880 billion in transactions.

"**Enron** makes the market. Make no mistake about that," said Merrill Lynch analyst Donato Eassey. "There's not a trader out there that doesn't use EnronOnline." As such, **Enron** enters into thousands of transactions every day in which the company's credit-worthiness is critical. **Enron** said its business operations were functioning normally Wednesday. The company also has consistently said it is financially strong and liquid.

Enron said its new chief financial officer is Jeffrey McMahon, the 40-year-old head of the company's industrial-markets division. His selection may be intended, in part, to raise the company's credibility. People familiar with the matter say Mr. McMahon left his job as treasurer last year after voicing concerns within the company about Mr. Fastow's role in running two limited partnerships that were involved in billions of dollars worth of transactions with **Enron**. Internal partnership documents indicate Mr. Fastow and possibly a handful of associates made millions of dollars from the partnerships. Mr. Fastow severed his ties with those partnerships in July in the face of increasing conflict-of-interest concerns being expressed by Wall Street analysts and major **Enron** investors. On Monday, **Enron** announced that the Securities and Exchange Commission was looking into the Fastow-related transactions.

[Go] **Enron** May Have to Issue Stock to Cover Possible Shortfalls in Investment Portfolio (Oct. 24)

[Go] SEC Seeks Information on **Enron** Dealings With Partnerships (Oct. 23)

[Go] **Enron** CFO's Tie to a Partnership Resulted in Big Profits (Oct. 19)

[Go] **Enron** Says Its Links to a Partnership Led to \$1.2 Billion Equity Reduction (Oct. 18)

While **Enron** as recently as Tuesday strongly defended Mr. Fastow, as well as the company's dealings with the partnerships, controversy over those arrangements clearly played a role in the executive's departure. "In my continued discussions with the financial community, it became clear to me that restoring investor confidence would require us to replace Andy as CFO," said Chairman and Chief Executive Kenneth Lay in a prepared statement.

Enron said Mr. Fastow "will be on a leave of absence from the company." He couldn't be reached for comment.

It remains to be seen how much Mr. Fastow's removal will assuage an increasingly restive investment community. The action came after the 4 p.m. market close and followed a day in which **Enron's** stock once again plunged. As of 4 p.m. Wednesday in New York Stock Exchange composite trading, **Enron** shares were at \$16.41, down \$3.38, or 17%. It topped the Big Board's most active list at nearly 76 million shares, more than twice the volume of the second-most-active stock. Several trades Wednesday involved blocks of 800,000 shares or more, possibly indicating that some institutional holders are souring on **Enron** stock.

Enron's shares are down about 50% from the beginning of last week. Earlier this year, the stock was above \$80 a share.

In an apparent ripple effect, the stocks of other energy-trading companies, which do business with **Enron**, also fell sharply Wednesday. For instance, Dynegy Inc. shares on the Big Board were off \$5.45, or 13%, at \$37.26. A number of the energy companies hit by the selloff have business strategies much different than **Enron's**, which rely heavily on complex and highly structured investment vehicles.

Prudential Securities analyst Carol Coale said Mr. Fastow's departure could be seen as evidence that "management does care" about investor concerns. However, she adds, the move also could be viewed by some investors, coming as it did two days after the announcement of the SEC inquiry, as "an admission of guilt." Ms. Coale Wednesday issued a sell recommendation on **Enron** largely because of uncertainties about the company's extremely complex financial structure.

Enron has consistently denied any wrongdoing in its Fastow-related dealings.

Worries and rumors about **Enron's** financial strength could be found in the stock market Wednesday. Goldman Sachs analyst David Fleischer said he heard people voice concerns about a possible "death spiral" in which increasing credit concerns about **Enron** would decrease the number of people willing to do business with the company, which would in turn weaken its finances and lead to further business reductions. Mr. Fleischer, a longtime fan who still has a buy recommendation on the company, said he hasn't yet seen any evidence of such a problem.

However, Mr. Fleischer said, **Enron** needs to disclose more information about its myriad of financial transactions with related partnerships and other entities. **Enron** is facing a problem with "trust and credibility. It's not easy to regain something as basic as trust," he said.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:32 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron May Have to Issue Stock

October 24, 2001

Major Business News

Enron May Have to Issue Stock to Cover Possible Shortfalls in Investment Portfolio

By REBECCA SMITH and JOHN R. EMSWILLER

Staff Reporters of THE WALL STREET JOURNAL

Enron Corp. might have to come up with several hundred million dollars or more during the next 20 months to cover potential shortfalls in investment vehicles it created. Covering such shortfalls could involve issuing additional **Enron** shares, diluting the position of current shareholders.

However, **Enron** Treasurer Ben Glisan said in an interview Tuesday that the company believes it can repay about \$3.3 billion in notes that were sold by those investment vehicles without having to resort to issuing more stock. The notes were sold to investors during recent years by several entities -- known as the Marlin Water Trust II, the Marlin Water Capital Corp. II, the Osprey Trust and Osprey I, Inc. The notes are coming due during the next 20 months.

Mr. Glisan said assets from the entities could be sold to pay off some of the notes. Also, **Enron** is selling other assets. Proceeds from those transactions also could go toward repaying the notes, which ultimately are guaranteed by **Enron**.

He said it appears that asset sales will raise at least \$2.2 billion by the end of next year. This amount includes cash proceeds of \$1.55 billion from the previously announced sale of **Enron's** Portland General Electric utility unit. **Enron** hopes to complete that sale by the end of 2002.

[\[Go\]SEC Seeks Information on **Enron** Dealings With Partnerships Recently Run by Fastow \(Oct. 23\)](#)

[\[Go\]**Enron** CFO's Tie to a Partnership Resulted in Big Profits for the Firm \(Oct. 19\)](#)

[\[Go\]**Enron** Says Its Links to a Partnership Led to \\$1.2 Billion Equity Reduction \(Oct. 18\)](#)

[\[Go\]**Enron** Posts Surprise 3rd-Quarter Loss After Investment, Asset Write-Downs \(Oct. 17\)](#)

"There are a number of other assets we believe will raise sufficient proceeds" to repay the notes, Mr.

Glisan said. "But if we are wrong, we will issue equity." Mr. Glisan said a worst-case scenario would involve issuing as much as \$1 billion in stock. **Enron** said it has about 850 million shares outstanding.

Making up any shortfall with equity has become more expensive because of the drop in Enron's share price. In 4 p.m. New York Stock Exchange composite trading, **Enron** shares were down 86 cents to \$19.79. The stock was once again one of the most actively traded with about 27 million shares changing hands. Early this year, **Enron** stock was more than \$80 a share.

During the past week, shares of the energy-trading giant have dropped more than 40%. Early last week, **Enron** reported a \$618 million third-quarter loss, resulting from \$1.01 billion in write-offs. The company also disclosed a \$1.2 billion reduction in shareholder equity for the quarter as a result of terminating certain transactions related to a partnership that for a time was headed by **Enron** Chief Financial Officer Andrew S. Fastow. In July, Mr. Fastow ended his connection to the partnership in the face of growing concerns by analysts and major investors. On Monday, **Enron** disclosed that the Securities and Exchange Commission was looking into the transactions related to Mr. Fastow. **Enron** has said its dealings with the partnership were proper.

The turmoil of the past several days prompted **Enron** to schedule a conference call Tuesday morning with Wall Street analysts and others in an effort to reassure investors. **Enron** Chairman and Chief Executive Kenneth Lay said while "we are extremely disappointed with our stock price ... our businesses are performing very well." Mr. Lay and other executives said **Enron** has adequate liquidity to meet its needs.

Mr. Fastow, the chief financial officer, took part in the conference call. But neither he nor Mr. Lay would answer any questions concerning the Fastow-related partnership, which was known as LJM2 Co-Investment LP. Mr. Lay said the SEC was in the midst of an inquiry concerning that partnership arrangement, which has raised conflict-of-interest questions among analysts and others. Mr. Lay cited shareholder suits filed recently as another reason not to discuss the partnership questions. Mr. Lay said he was "very concerned about the way Andy's character has been loosely tossed about." He added "we continue to have the highest faith and confidence in Andy."

Internal LJM2 documents indicate that Mr. Fastow and perhaps a handful of fellow **Enron** officials made millions of dollars in management fees and capital increases from running the partnership. Billions of dollars of **Enron** assets and stock were involved in LJM2-related transactions, according to **Enron** SEC filings.

During the conference call, analysts -- even some who have been longtime **Enron** fans -- challenged executives about the Fastow partnership arrangement and the company's often opaque financial reports. "There's the appearance you are hiding something," said Goldman Sachs analyst David Fleischer. "You need to do everything in your power to demonstrate to investors that your dealings are above board."

Mr. Lay responded, "We're trying to be as transparent as we can."

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:35 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: SEC Seeks Information on Enron

October 23, 2001

Money & Investing

SEC Seeks Information on Enron Dealings With Partnerships Recently Run by Fastow

By REBECCA SMITH and JOHN R. EMSWILLER
Staff Reporters of THE WALL STREET JOURNAL

Enron Corp. said it has been contacted by the Securities and Exchange Commission seeking information on the energy giant's controversial dealings with partnerships that were set up and run until recently by its chief financial officer, Andrew S. Fastow.

Following Enron's announcement Monday morning of the SEC inquiry, the company's stock took another big slide, falling more than 20% in New York Stock Exchange trading. As of 4 p.m., Enron shares were trading at \$20.65, off \$5.40, knocking about \$4 billion off Enron's market capitalization. Volume topped the Big Board's most-active list at about 36 million shares. A week ago, Enron stock was trading at about \$33 a share. Subsequently, the company announced a \$1.01 billion third-quarter write-off that produced a \$618 million loss.

Analysts also voiced concerns Monday about possible other bad news lurking amid Enron's vast and extremely complex operations. The company has dealings with a number of related entities. Under certain circumstances, if Enron's credit rating and stock price fall far enough, the company would be obligated to issue tens of millions of additional shares to these entities, diluting the holdings of current shareholders.

[\[Go\]See a timeline of events](#)

Enron has previously acknowledged the provisions but said its business is strong and it feels confident that there will be no defaults.

In a statement, Enron Chairman and Chief Executive Kenneth Lay said the company "will cooperate fully" with the SEC inquiry and "look(s) forward to the opportunity to put any concern about these transactions to rest." Enron has consistently said that it believes its dealings with the Fastow-related partnerships were proper and properly disclosed. The company has said it put billions of dollars of

assets and stock into partnership-related transactions as a way to hedge against fluctuating market conditions.

The SEC inquiry came from the agency's Fort Worth, Texas, regional office. According to a person familiar with the matter, this would indicate that the inquiry comes from the SEC's enforcement arm, as opposed to its corporate-finance section. The participation of the enforcement branch would indicate that the agency is looking into whether there were possible violations of securities law. However, enforcement-branch inquiries often don't produce any allegations of wrongdoing. It also appears that the SEC hasn't yet taken the step of launching a formal investigation, which would be a sign that the agency believes securities laws might have been violated. The SEC declined to comment.

[Enron]

Certainly, there have been questions and concerns about those partnership transactions, which contributed to a \$1.2 billion reduction in shareholder equity last week as part of Enron's efforts to unwind the deals. Mr. Fastow, who has declined repeated interview requests, resigned from the partnerships, known as LJM Cayman LP and LJM2 Co-Investment LP, in late July in the face of rising conflict-of-interest concerns by Wall Street analysts and major company investors.

Since then, internal partnership documents have shown that Mr. Fastow and perhaps a handful of Enron associates made millions of dollars last year in fees and capital increases as general partner of the LJM2, the larger of the two partnerships.

Mr. Fastow's partnership arrangement caused some unhappiness inside Enron, according to people familiar with the matter. For instance, these people say, sometime after the creation of the partnerships in 1999, Enron Treasurer Jeffrey McMahon went to company president Jeffrey Skilling and complained about potential conflicts of interest posed by Mr. Fastow's activities. Mr. Skilling didn't share Mr. McMahon's concern, these people say, and Mr. McMahon requested and received reassignment to another post.

Mr. Skilling resigned as Enron president and chief executive in mid-August, citing personal reasons and the fall in Enron's stock price, which peaked at about \$90 a share last year. Mr. McMahon and Mr. Skilling haven't responded to repeated interview requests.

Investors are also concerned about potential problems arising in Enron's dealings with other related entities. In some cases, Enron could be required to issue large amounts of stock to noteholders in some of the entities if certain so-called double trigger provisions occur.

For example, last July Enron helped create the Marlin Water Trust II, which sold \$915 million in notes that are due July 15, 2003. However, Enron can be considered in default, in advance of that date, if its stock price falls below \$34.13 for three trading days and its senior debt is downgraded to below investment grade by either Moody's Investors Service or Standard & Poor's.

Currently, Enron debt is still investment-grade at both ratings agencies and would have to be lowered by several notches to fall into a noninvestment grade category. Last week, Moody's put Enron on review for a possible downgrade. However, observers believe that even if Moody's lowers Enron's rating, the company will still be investment-grade.

Oct. 16: Enron takes \$1.01 billion charge related to write-downs of investments. Of this, \$35 million is

attributed to partnerships until recently run by CFO Andrew Fastow. Enron also discloses it shrank shareholder equity by \$1.2 billion, as a result of several transactions including ones undertaken with Fastow's investment vehicle.

Oct. 17: SEC sends letter to Enron saying it was beginning an "informal inquiry."

Oct. 19: The Wall Street Journal discloses that general partners of Fastow partnership realized more than \$7 million last year in management fees and about \$4 million in capital increases on an investment of nearly \$3 million in the partnership, set up principally to do business with Enron, according to internal partnership document. Enron's board meets to discuss SEC inquiry.

Oct. 22: Enron announces SEC will begin a probe of company's "related party transactions," including those with Fastow partnerships. Enron says it will fully cooperate.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:39 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron's CFO's Tie

October 19, 2001

Money & Investing

Enron CFO's Tie to a Partnership Resulted in Big Profits for the Firm

By REBECCA SMITH and JOHN R. EMSWILLER

Staff Reporters of THE WALL STREET JOURNAL

A limited partnership organized by **Enron** Corp.'s chief financial officer, Andrew S. Fastow, realized millions of dollars in profits in transactions it did with **Enron**, according to an internal partnership document.

The partnership, in some instances, benefited from renegotiating the terms of existing deals with the Houston energy company in ways that improved the partnership's financial positions or reduced its risk of losses.

Mr. Fastow, and possibly a handful of partnership associates, realized more than \$7 million last year in management fees and about \$4 million in capital increases on an investment of nearly \$3 million in the partnership, which was set up in December 1999 principally to do business with **Enron**.

[enron]

The profits from the deals were disclosed in a financial report to investors in the partnership, LJM2 Co-Investment LP, that was signed by Mr. Fastow as the general partner and dated April 30. In one case, the report indicates the partnership was able to improve profits by terminating a transaction early.

The LJM2 arrangement has become controversial for **Enron**, as shareholders and analysts have raised questions about whether it posed a conflict by putting the company's chief financial officer, who has a fiduciary duty to **Enron** shareholders, in a position of reaping financial rewards for representing LJM2 investors in business deals with **Enron**. Investors in LJM2 include Wachovia Corp., General Electric Co.'s General Electric Capital Corp. and Credit Suisse Group's Credit Suisse First Boston.

Attention has focused on Mr. Fastow's partnership activities at a tumultuous time for **Enron**, which over the past decade grew enormously by becoming the nation's biggest energy-trading company.

This year, though, it has been hit by a string of troubles, from soured business initiatives to executive departures. On Tuesday, **Enron** announced a \$618 million third-quarter loss, because of a \$1.01 billion write-off on investments in broadband telecommunications, retail energy services and Azurix Corp., a water company. A small chunk of that write-off, about \$35 million, was attributed to ending certain LJM2-related transactions. That termination also produced a \$1.2 billion reduction in **Enron** shareholder equity as the company decided to repurchase 55 million shares that had been part of LJM2 deals.

[Go]Enron Says Its Links to a Partnership Led to \$1.2 Billion Equity Reduction (Oct. 18)

At 4 p.m. Thursday in New York Stock Exchange composite trading, **Enron** was down 9.9%, or \$3.20, to \$29 a share. Within the past year, the stock had topped \$80 a share.

Enron officials didn't have any comment about the LJM2 partnership document. **Enron** has consistently said its dealings with LJM2 have been proper. They said the LJM2 deals, like ones done with other parties, were aimed at helping hedge against fluctuating market values of its assets and adding sources of capital.

Mr. Fastow has declined several requests for an interview about LJM2. In late July, he formally severed his ties with LJM2, as a result of what **Enron** officials said was growing unease by Wall Street analysts and major shareholders. Mr. Fastow has been finance chief of **Enron** since 1997 and has been with the firm 11 years, which included extensive work setting up and managing company investments.

Michael Kopper, a former **Enron** executive who an **Enron** spokesman said is now helping to operate LJM2, declined to comment. He also wouldn't describe his relation to LJM2.

In his April 30 report, Mr. Fastow said the partnership, which raised \$394 million, had invested in several Enron-related deals involving power plants and other assets as well as company stock. The document said LJM2 sought a 29% internal rate of return. That was down from a 48% targeted rate of return at the end of 2000, which the document said was due in part to a decline in the value of LJM2's investment in New Power Co., an Enron-related energy retailer. In some transactions, LJM2 did much better than the 29% target, though this sometimes involved renegotiating individual deals.

In September 2000, the partnership invested \$30 million in "Raptor III," which involved writing put options committing LJM2 to buy **Enron** stock at a set price for six months. Four months into this deal, LJM2 approached **Enron** to settle the investment early, "causing LJM2 to receive its \$30 million capital invested plus \$10.5 million in profit," the report said. The renegotiation was before a decline in Enron's stock price, which could have forced LJM2 to buy **Enron** shares at a loss of as much as \$8 each, the document indicated.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:41 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron -- \$1.2 Billion Equity Reduction

October 18, 2001

Money & Investing

Enron Says Its Links to a Partnership Led to \$1.2 Billion Equity Reduction

By REBECCA SMITH and JOHN R. EMSWILLER
Staff Reporters of THE WALL STREET JOURNAL

Enron Corp. shrank its shareholder equity by \$1.2 billion as the company decided to repurchase 55 million of its shares that it had issued as part of a series of complex transactions with an investment vehicle connected to its chief financial officer, Andrew S. Fastow.

Enron didn't disclose the big equity reduction in its earnings release issued on Tuesday, when the Houston-based energy giant announced a \$1.01 billion charge to third-quarter earnings that produced a \$618 million loss. But the company briefly mentioned it in a subsequent call with security analysts and confirmed it in response to questions Wednesday. As a result of the reduction, Enron's shareholder equity has dropped to \$9.5 billion, the company said.

In an interview Tuesday, Enron Chairman Kenneth Lay said that about \$35 million of the \$1.01 billion charge to earnings was related to transactions with LJM2 Co-Investment LP, a limited partnership created and run by Mr. Fastow. In a conference call Wednesday with investors, Mr. Lay said that the 55 million shares had been repurchased by Enron, as the company "unwound" its participation in the transactions. In the third quarter, the company's average number of shares outstanding was 913 million.

According to Rick Causey, Enron's chief accounting officer, these shares were contributed to a "structured finance vehicle" set up about two years ago in which Enron and LJM2 were the only investors. In exchange for the stock, the entity provided Enron with a note. The aim of the transaction was to provide hedges against fluctuating values in some of Enron's broadband telecommunications and other technology investments. Mr. Causey didn't elaborate on what form those hedges took.

Subsequently, both the value of Enron's stock and the value of the broadband investments hedged by the entity dropped sharply. As a result, Enron decided essentially to dissolve the financing vehicle and reacquire the shares. When Enron reacquired the shares, it also canceled the note it had

received from the entity.

In addition, Enron was receiving increasing criticism from analysts and major shareholders concerning the apparent conflict of interest involving the role of its chief financial officer in the partnership, from which he stood to make millions of dollars. In July, Mr. Fastow formally severed his connections to LJM. Mr. Fastow has declined to be interviewed.

Given all the complexities of the LJM-related financing vehicle and the questions it raised outside the company, "the confusion factor wasn't worth the trouble of trying to continue this," Mr. Causey said.

Enron downplayed the significance of the share-reduction exercise. Mark Palmer, an Enron spokesman, described it "as just a balance-sheet issue" and therefore wasn't deemed "material" for disclosure purposes.

Jeff Dietret, an analyst for Simmons & Co. in Houston, said that a large reduction of equity could be "a flag for the rating agencies" because it could adversely affect a company's debt-to-equity ratio. Enron said Wednesday that as a result of the equity reduction, its debt-to-equity ratio rose to 50% from 46% previously.

On Tuesday, after Enron reported its big quarterly loss, Moody's Investors Service Inc. put Enron's long-term debt on review for a possible downgrade. Moody's said the move was related to "significant write-downs and charges reflecting substantially reduced valuations" in several of Enron's businesses. In recent years, Enron had moved aggressively into broadband telecommunications and the water business, both of which failed to produce expected returns.

Enron, which as of June 30 had \$33.6 billion in current liabilities and long-term debt, has lately been attempting to shed assets to pay down debt.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:44 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron Posts Surprise

October 17, 2001

Money & Investing

Enron Posts Surprise 3rd-Quarter Loss After Investment, Asset Write-Downs

By **JOHN EMSWILLER** and **REBECCA SMITH**

Staff Reporters of THE WALL STREET JOURNAL

Enron Corp. Tuesday took a \$1.01 billion charge mostly connected with write-downs of soured investments, producing a \$618 million third-quarter loss. The loss highlights the risks the onetime highflier has taken in transforming itself from a pipeline company into a behemoth that trades everything from electricity to weather futures.

In addition to the size of the charge, a particular slice raises anew vexing conflict-of-interest questions. The slice is connected with a pair of limited partnerships that until recently were run by **Enron's** chief financial officer. The company said the charge connected with the partnerships is \$35 million and involves the "early termination ... of certain structured finance arrangements."

Two years ago, the chief financial officer, Andrew S. Fastow, entered into the unusual arrangement with his employer. With the approval of the board of **Enron**, Mr. Fastow set up and ran the partnerships that stood to make him millions or more, according to partnership documents. While the company says that this arrangement was proper, some corporate-governance watchdogs have questioned whether a chief financial officer, who is responsible for overseeing the financial interests of the company, should have been involved in such a partnership that was, among other things, looking to purchase assets from **Enron**.

The two partnerships, LJM Cayman LP and the much larger LJM2 Co-Investment LP, have engaged in billions of dollars of complex hedging transactions with **Enron** involving company assets and millions of shares of **Enron** stock. It isn't clear from **Enron** filings with the Securities and Exchange Commission what **Enron** received in return for providing these assets and shares. In a number of transactions, notes receivable were provided by partnership-related entities.

Mr. Fastow's role as chief financial officer made him privy to internal asset analyses at **Enron**. An offering memorandum for the LJM2 partnership said that this dual role "should result in a steady flow of opportunities ... to make investments at attractive prices." Mr. Fastow would find his interests "aligned" with investors because the "economics of the partnership would have significant impact on

the general partner's wealth," according to this document.

In a written statement in response to questions, **Enron**, based in Houston, said "there never was any obligation for **Enron** to do any transaction with LJM. **Enron** and its Board established special review and approval processes with its senior management and external audit and legal counsel to ensure that each transaction with the LJM partnership was fair, in the best interest of **Enron** and its shareholders, and appropriately disclosed."

Mr. Fastow, through an **Enron** spokesman, declined to be interviewed.

In announcing the third-quarter loss, **Enron** said the partnership-related write-offs were part of a larger \$544 million charge related to the diminished value of investments in a retail-power business, broadband telecommunications and technology. In addition, there was also a \$287 million write-off resulting from its investment in Azurix Corp., a water company **Enron** spun off and then repurchased. In all, **Enron** posted a third-quarter loss of 84 cents a share, compared with a gain of 34 cents a share in the year-earlier period. Revenue rose 59% to \$47.6 billion.

At 4 p.m. Tuesday, Enron's stock was up 67 cents a share to \$33.84 in composite trading on the New York Stock Exchange, but remains far below its 52-week high of \$84.88. On Monday, the day before the earnings announcement, **Enron** stock dropped by about 7%.

[Enron]

In an interview, Enron's chairman and chief executive, Kenneth Lay, said the write-offs were designed as part of an effort to "find anything and everything that was a distraction and was causing a cloud over the company."

The quarterly loss is the latest in a series of setbacks faced by **Enron** recently after years of almost unbroken success. There have been mounting problems from expensive moves into the water and telecommunications businesses.

And there has been a steady stream of executive departures, most notably the surprise resignation in August of Enron's president and chief executive, Jeffrey Skilling, who said he left for personal reasons and because of the fallen stock price.

The partnership arrangement involving Mr. Fastow, the highly regarded chief financial officer, first surfaced in an **Enron** SEC filing in 1999, but only recently has it attracted Wall Street's concern. In late July, Mr. Fastow severed his relations with the partnerships, according to a company SEC filing. Company officials said that move was partly related to questions raised by analysts and large **Enron** shareholders.

Little about the inner workings of the LJM partnerships has been disclosed to date. Private partnership documents reviewed by The Wall Street Journal indicate that **Enron** agreed to a partnership arrangement with potentially huge financial rewards for Mr. Fastow.

The LJM Cayman partnership raised a relatively modest \$16 million, according to the documents. The more ambitious LJM2 aimed to raise at least \$200 million, the documents show. Among investors were Credit Suisse Group's Credit Suisse First Boston, Wachovia Corp. and General Electric Co.'s General Electric Capital Corp. The Arkansas Teachers Fund committed \$30 million, of which \$7.4 million had been tapped by late last month. Bill Shirron, a fund manager there, said the LJM arrangement had "already returned \$6 million to us." It's been "a home run so far," Mr. Shirron

added.

According to the LJM2 offering document, the general partner, made up of Mr. Fastow and at least one other **Enron** employee, received a management fee of as much as 2% annually of the total amounts invested. Additionally, the general partner was eligible for profit participation that could produce millions of dollars more if the partnership met its performance goals over its projected 10-year life. In exchange, the general partner was obliged to invest at least 1% of the aggregate capital commitments.

In an interview earlier this year, Mr. Lay said the LJM arrangement didn't produce any conflicts of interest. Such related-party transactions, involving top managers or directors, aren't unusual, he said. "Almost all big companies have related-party transactions."

Typically, related-party transactions involve dealings with partly owned affiliates or a contract with a firm tied to one of the company's outside directors. It is rare for a top executive to be in a position where he could have conflicting fiduciary responsibilities. The LJM2 offering document states that the responsibilities of Mr. Fastow and other partnership officials to **Enron** could "from time to time conflict with fiduciary responsibilities owed to the Partnership and its partners."

Some institutions approached as potential LJM investors demurred partly because of such potential conflicts.

Enron has publicly stated that the partnership deals were aimed to help it hedge against fluctuating values for its growing portfolio of assets. In the past decade, **Enron** has seen its asset base rocket to more than \$100 billion. As a result of this rapid growth, **Enron** has at times been strapped for capital and has sought ways to bring in outside investors to help bolster its balance sheet.

Charles LeMaistre, an outside **Enron** director and president emeritus of the M.D. Anderson Cancer Center at the University of Texas, said he viewed the partnership arrangement partly as a way of keeping Mr. Fastow at **Enron**. "We try to make sure that all executives at **Enron** are sufficiently well-paid to meet what the market would offer," he said.

Enron's interest in retaining Mr. Fastow may have been heightened by an exodus of top managers who were cashing out large stock-option grants after the company's success in 1999 and 2000. Mr. Fastow's yield from options for the 12 months through Aug. 31 was \$4.6 million, according to disclosure reports compiled by Thomson Financial. Mr. Lay netted about \$70 million from exercising options during this period, while Mr. Skilling, the former president, realized nearly \$100 million.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, October 29, 2001 11:46 AM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: Enron Meets #Q Estimates Excluding Hefty Charge

October 16, 2001

Dow Jones Newswires

Enron Meets 3Q Estimates Excluding Hefty Charge

By **CHRISTINA CHEDDAR**

OF DOW JONES NEWSWIRES

NEW YORK -- **Enron** Corp. (ENE) posted a third-quarter loss after accounting for a \$1.01 billion charge to write off impaired assets at its Azurix Corp. water services unit and a number of other investment losses.

The Houston energy trader reported a loss of \$618 million, or 84 cents a share, compared with earnings of \$292 million, or 34 cents a share, a year ago.

Revenue, meanwhile, jumped 59% to \$47.61 billion from \$30.01 billion.

Enron's charges, which totaled \$1.11 a share, consist of \$287 million related to asset impairments recorded by Azurix, \$180 million associated with the restructuring of broadband services and \$544 million related to losses associated with certain investments, including those at New Power Holdings Inc.'s (NPW) The New Power Co. unit.

Excluding the charge, **Enron** was able to meet Wall Street's expectations as reported by Thomson Financial/First Call, with recurring earnings of \$393 million, or 43 cents a share.

"After a thorough review of our businesses, we have decided to take these charges to clear away issues that have clouded the performance and earnings potential of our core energy businesses," **Enron** Chairman and Chief Executive Kenneth Lay said in a press release.

There are two ways to view the charge, according to Commerzbank analyst Andre Meade.

With a "positive spin," one could view the charge as a clearing of the books, he said. However, Meade said he also feels the charge could be seen as the "other shoe" investors were waiting to drop after ex-Chief Executive Jeffrey Skilling's abrupt resignation this summer.

"Skilling hinted pretty well that there wasn't going to be a charge," Meade said.

Although Meade said it was no secret that businesses such as Azurix and broadband services were experiencing difficulties, the charge "certainly calls into question (Enron's) ability to add to their successful" core wholesale energy business, he said. "They have invested in steel and pulp and paper, and we have no indication that they will create value in these businesses."

Enron shares were recently trading at \$33.79, up 62 cents, or 1.9%, which is down from its intraday high of \$34.90.

In the wake of the departure of Enron's Skilling, the company had promised to provide more detail in its earnings reports, and the third quarter was its first chance to put the plan in action.

Many believe **Enron** delivered on the promise. The company broke down the reporting of its wholesale services business into two segments, Americas and Europe and other commodity markets.

In the Americas, third-quarter income before interest, minority interests and taxes rose 31%, driven by a 6% increase in natural gas volumes and 77% surge in power volumes. In Europe and other commodity markets, **Enron** said low volatility in the gas and power markets caused profitability to remain flat.

However, **Enron** stopped providing detail about the value of contracts it is signing in its retail services segment, where third-quarter income before interest and taxes rose to \$71 million from \$27 million a year ago.

J.P. Morgan Chase analyst Anatol Feygin said the detail was "a very good metric" to measure future earnings potential.

Others who follow the company were also pleased with Enron's changes.

"There was clearly a need to increase the level of transparency," said Glen Hilton, manager of the Montgomery New Power Fund, which has 2% of its approximately \$100 million in assets invested in **Enron**. "This is a pretty good step in the right direction."

The third quarter also marked the first time **Enron** broke out its global assets into a separate category, and the company provided additional information about its pipeline business.

Still, **Enron** investors and analysts continue to be concerned about the potential for future charges because of continuing losses in Enron's broadband services unit and other uncertainties.

Montgomery Asset Management's Hilton said the third-quarter charge is "clearly not the last."

During the company's conference call, Enron's Lay agreed uncertainty remained at broadband services as well as with the lingering issues related to the California power crisis, and in India, where **Enron** is locked in a dispute with Dabhol Power Co.'s sole buyer, the Maharashtra State Electricity Board. However, Lay said charges weren't needed for these areas because Enron's exposure to California is "adequately reserved," and it is "actively pursuing" its legal remedies in India.

At **Enron** Broadband Services, third-quarter losses before interest and taxes widened to \$80 million from \$20 million a year ago, reflecting lower investment-related income and lower operating costs. Lay said the broadband market conditions continue to be hurt by the "lack of creditworthy counterparties."

UBS Warburg analyst Ronald Barone said he is concerned by the cash-burn rate of the unit. **Enron**

has addressed this by restructuring the unit. The effort resulted in \$180 million of the third-quarter charge. The item included severance costs, a loss on the sale of inventory and an impairment charge to reflect the reduced value of Enron's content services business.

However, since **Enron** has invested so much in the business, analysts believe it is possible further impairment charges will be needed if broadband doesn't begin to turn around.

Lay addressed these concerns during the company's conference call.

"We tried to clean up anything we needed to clean up," he said.

The "cleanup" also included a \$544 million charge related to Enron's investments.

According to Lay, half of the investment charge was related to Enron's investment in the New Power Co., a provider of electricity and natural gas to the households and small businesses. New Power shares have fallen to about \$1.88 from its 52-week high of \$20.88 last October.

The remainder of Enron's investment charge is tied to both investments in other broadband and technology companies, including the now-bankrupt Northpoint Communications Group Inc. (NPNTQ), and the early termination of a structured finance arrangement.

The significant charge prompted credit rating agency Moody's Investors Service to review **Enron** for a downgrade.

According to Lay, adjustments related to the third-quarter charge will increase Enron's debt-to-capital ratio to 50%, but that level will be reduced to 40% by the end of 2002 by proceeds from pending asset sales.

"I'm very comfortable with our liquidity position," Lay said.

Even if Moody's downgrades Enron's debt, it is likely it will remain investment grade. However, the move would increase the cost of capital for the company.

Looking ahead, **Enron** reaffirmed its prior earnings forecasts. The company expects to earn 45 cents a share in the fourth quarter, \$1.80 in 2001, and \$2.15 for fiscal 2002. Analysts surveyed by Thomson Financial/First Call expect the company to earn 47 cents a share in the fourth quarter, \$1.81 in 2001 and \$2.14 in 2002.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, October 30, 2001 12:02 PM
To: Schultheiss, Heidilynne; Nickoloff, Peter
Subject: WSJ on Enron

October 30, 2001

Money & Investing

Moody's Downgrades Enron's Debt, Maintains Review; Stock Drops 10%

By **JOHN R. EMSWILLER** and **MICHAEL SCHROEDER**

Staff Reporters of THE WALL STREET JOURNAL

In another potentially serious blow to **Enron** Corp.'s finances, Moody's Investors Service Inc. lowered its ratings by one notch on the energy company's senior unsecured debt and kept the company under review for a possible further downgrade.

It also was learned that the Securities and Exchange Commission has moved its inquiry into Enron's finances to the agency's Washington headquarters from its regional office in Fort Worth, Texas. The change is a sign that the probe is being treated as a high priority, according to a person with knowledge of the inquiry. An SEC spokesman declined to comment.

Moody's reduction on Enron's senior unsecured long-term debt to Baa2 from Baa1 leaves the company's credit rating two levels above noninvestment grade. If the energy-trading giant's ratings were to fall to a noninvestment-grade level, there could be serious consequences for **Enron**. It could throw the Houston company into default on obligations involving billions of dollars of borrowings and force it under the terms of various financial agreements to issue millions of shares of stock to holders of that debt, which would dilute the value of existing shares.

While **Enron** still has some room before hitting noninvestment-grade status, there have been concerns among analysts and investors that the company's recent troubles could escalate. During recent days Enron's bonds have traded at levels similar to securities that carry a noninvestment-grade rating. Prices of the company's bonds improved somewhat Monday, though its stock price continued to fall sharply. In 4 p.m. New York Stock Exchange composite trading, **Enron** stock was at \$13.81, down \$1.59 or 10%, and topped the most-active list with 36.4 million shares changing hands. Enron's share price has fallen more than 50% during the past two weeks.

[Go]Enron Is in Discussions With Banks for Credit Line of up to \$2 Billion (Oct. 29)

[Go]Enron Officials Sell Shares Amid Stock-Price Slump (Oct. 26)

[Go]Enron May Have to Issue Stock to Cover Possible Shortfalls in Investment Portfolio (Oct. 24)

An **Enron** spokeswoman said the company is "working diligently" to keep an investment-grade credit rating. Among other things, the nation's biggest energy-trading firm is in negotiations with its banks on a new \$1 billion to \$2 billion credit line to bolster its liquidity. **Enron** repeatedly has said its business operations remain strong.

Monday's ratings downgrade is the latest piece of bad news for a company that has been engulfed in turmoil during the past two weeks. Confidence in its financial situation was shaken after **Enron** earlier this month announced a \$618 million third-quarter loss and disclosed a \$1.2 billion erosion of shareholder equity related to transactions it had carried out with entities connected to its then-chief financial officer, Andrew Fastow. Last week, **Enron** named a successor to Mr. Fastow and said the SEC was looking into the deals.

The SEC is looking into whether **Enron** violated federal-securities laws regarding its handling and disclosure of the transactions connected to Mr. Fastow, the person familiar with the probe said. Generally, the SEC's headquarters office has more resources to apply to complex, high-profile cases than regional offices do. Moving the **Enron** inquiry to headquarters indicates that the SEC is looking to make a decision relatively quickly about whether or not to allege securities-law violations by the company, this person said.

Enron repeatedly has said the transactions were proper and legal. Monday, the **Enron** spokeswoman said the company is continuing to cooperate with the SEC probe and is gathering and sending the agency information that it requested.

Moody's said the downgrade was "prompted by the deterioration in Enron's financial flexibility," which has contributed to "a substantial loss in investor confidence." Going forward, Moody's said it will focus on **Enron** management's "success in lining up further liquidity support and on their ability to retain credit availability" from major trading partners. **Enron** is a principal in nearly one-quarter of all electricity and natural-gas trades in the nation.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, November 01, 2001 2:01 PM
To: Roseboro, Brian; Gross, Jared; Bitsberger, Timothy; Schultheiss, Heidilynne; Nickoloff, Peter; Cetina, Jill; Sharer, James
Subject: Economist Article on Enron: "Houston, we have a problem"

A financial black hole

Houston, we have a problem

Nov 1st 2001 | HOUSTON, LONDON AND NEW YORK
From The Economist print edition

AP

AP

The troubles of Enron, a Texan powerhouse in the energy markets, could result in a new financial crisis

JUST last year, visitors to Enron's glittering headquarters in Houston were greeted by a giant banner that proclaimed the firm, "The world's leading energy company". That annoyed Enron's smaller energy-trading rivals, many of which have offices only a stone's throw away in Houston's Energy Alley, but not as much as what came next—a new banner, declaring Enron "The world's leading company". In recent weeks, as the company has been engulfed by a financial crisis, that banner has quietly been removed.

The heady mix of audacity, ambition and arrogance revealed by the banners is as good a guide as any to Enron's remarkable rise and fall. Forged in the 1980s by the merger of two troubled gas-pipeline firms, Enron drove the development of the sophisticated spot-and-derivatives markets in energy that it has come to dominate. Indeed, such is the scale of its operations, and its dealings with many of the world's financial institutions, that some observers see parallels with Long-Term Capital Management (LTCM), the hedge fund that failed in 1998—and not just because seemingly brilliant financial alchemists have been humbled. Were Enron to go bust—unlikely, but in the current nervous climate, not impossible—might a crisis ensue?

Troubles in California's politically crazed power market, an ill-advised foray into telecoms bandwidth trading and concerns about management badly dented Enron's share price earlier this year, prompting the departure of Jeffrey Skilling, the firm's newish chief executive, in August. Kenneth Lay, an avid free-marketeer, friend of George Bush and visionary chairman of the firm, was obliged to resume hands-on control.

This has not slowed Enron's decline. Day by day, it seems to be sinking deeper into a financial quagmire that is largely of its own creation. Not least thanks to its lack of transparency, the firm's credibility with the markets has eroded to the point that talk of a possible takeover or even bankruptcy is widespread.

Enron's reputation for financial wizardry has been turned from an asset to a liability since its third-quarter results came out in mid-October, showing a \$1 billion write-off on water distribution, broadband trading and other investments. Worse, disclosed only in passing by Mr Lay in a conference call with analysts, the firm suffered a \$1.2 billion reduction in capital, stemming from a hedging deal with a related private-equity fund called LJM. The charge was due to Enron's forced sale of 55m of its own shares when the partnership was unwound this summer. Almost nobody outside Enron had been aware of the terms of the deal with LJM, a "structured finance vehicle".

Enron's failure to offer details about the risks from other related partnerships have led many to fear the worst about its huge balance sheet. Its shares plunged by 19% on October 30th alone (see chart), before recovering a bit the next day.

Andrew Fastow, who was replaced as chief financial officer on October 24th, was a general partner in LJM. Jeffrey McMahon, his successor, has much to do to restore confidence. Questions abound. Were the trusts run at arm's length? What did Mr Fastow earn from the partnership? Ominously, the Securities and Exchange Commission (SEC) has now launched a formal inquiry.

Moody's, a rating agency, last week cut its rating on the company's debt to barely above "junk" level. Further downgrades might unleash claims from other off-balance-sheet partnerships. Those known about, such as Atlantic Water and Marlin Water, do not seem big enough to bankrupt Enron, but speculation is rife about what other obligations might lurk secretly in other structured vehicles.

A lower credit rating could destroy Enron's core franchise as the leading energy middleman, by scaring away customers and freezing the wholesale energy markets. That might have nasty consequences in other markets. Enron acknowledges that it is a large participant in the derivatives market, holding a portfolio with a notional value of \$21 billion. Rightly or wrongly, many traders believe that figure vastly understates Enron's presence. If the firms on the other side of Enron's trades start to fear that payment is not coming, they might curb their other trading, producing a knock-on effect. Where this could end up is a subject of much conjecture.

Utilities that trade energy could be hit. So could the commodity and derivative operations of large commercial and investment banks. The ties are notably tight between Enron and J.P. Morgan Chase, according to Ventana Capital, a research firm. Not only does J.P. Morgan provide innumerable separate credit arrangements for Enron; it also has the largest derivative operation of any bank, as well as a large business trading commodities. There is "no doubt" that Enron is on the other side of many J.P. Morgan trades, says Ventana.

Were Enron to fail, Ventana thinks "it has the potential to cause a major financial crisis", worse, in some ways, than what occurred after LTCM. That merely froze the debt markets temporarily, whereas Enron deals in the building-blocks of the American economy. Imagine gridlock in the markets for gas, timber, coal, metals, fertiliser, bandwidth or indeed any of the products Enron deals in.

As yet, this all seems unlikely. Many big traders were happy to deal with Enron this week, although at shorter maturities and with less complex structures than in the past. Trading on EnronOnline <http://www.enrononline.com/jsp/marketing/homepage/index.html> was reportedly strong. Jim Donnell of Duke Energy, a big energy trader, described "a huge dichotomy" between the collapse in confidence in Enron in the equity and credit markets and the "business as usual" attitude taken by big commodity trading firms when considering Enron as a counterparty.

Yet as questions about Enron's credit-standing spread this week, it began to have difficulty making markets in some instruments. Few firms would accept Enron's name as guarantor of a credit derivative. In its core energy markets some big trading counterparties refused the Enron name. On the InterContinental Exchange (ICE), two houses reportedly specified that they would not take Enron's credit.

The biggest credit exposure appeared to be with banks, whose \$3 billion of back-up lines to Enron were drawn down last week. J.P. Morgan arranged an additional \$1 billion emergency credit-line this week. This back-up, it is widely assumed, is needed mainly to meet margin calls triggered by the ratings downgrade.

Too big to fail?

Is Enron too big and too important to be allowed to fail? Philip Verleger, an energy economist, thinks that Enron is so central to energy markets that it could not easily be replaced. Enron's rivals mostly disagree, unsurprisingly.

But even Enron's worst enemies do not (yet) expect the firm to die from its current crisis. Most traders seem keen that it should live. "Nobody likes to see a wholesale trader disappear," says one. They admire Enron's armies of traders and their ability to do deals. EnronOnline is one of the Internet's few success stories, assuming its huge trading volumes do indeed generate big profits, as the firm claims.

Enron's, and the financial system's, problems could worsen if doubts grow about its ability to meet its obligations. On the surface it is rich in assets, if not cash. But its lack of transparency leaves uncomfortable room for doubt. In June 2000, *The Economist* challenged Mr Lay to reply to accusations of arrogance, high-handedness and a propensity to push the limits of the law. His response was revealing. To show that such charges were baseless, he pointed to another firm unfairly maligned by critics: Drexel Burnham Lambert, an investment bank that rose from obscurity to market prominence in the junk-bond boom of the 1980s. Drexel was accused of arrogance, he groused, but it was only being "very innovative and very aggressive". Drexel was not bailed out: Michael Milken, its star, ended up in jail, and Drexel collapsed in a heap of bad debts and ignominy.

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, November 02, 2001 2:50 PM
To: Schultheiss, Heidilynne; Nickoloff, Peter; Pietrangeli, Fred; Berardi, Steve; Ludwick, CM; Cetina, Jill; Sharer, James; Whaley, Jean
Subject: Slate Article: "Enron's Transparent Problems"

moneybox

Enron's Transparent Problems

By Rob Walker

Updated Thursday, October 25, 2001, at 3:49 PM PT

On Wednesday, the CEO of Enron, Kenneth L. Lay, expressed the "highest faith and confidence" in his chief financial officer. Yesterday, he announced that his CFO has been replaced.

Enron is having a transparency problem. I don't mean that it's easy to see what has gone so drastically wrong in the firm's numbers lately but rather the opposite. In fact, it's the maddening opacity of certain aspects of Enron's financial dealings that has positively crushed its share price recently. It's not that someone has found, or even claimed knowledge of, some smoking gun-it's that no one even seems certain how to look for such a thing.

The trouble apparently began with a remark by Lay during the firm's most recent quarterly conference call with analysts: Enron planned to repurchase 55 million shares issued as part of a transaction with a "structured finance vehicle," and as a result its shareholder equity would shrink by \$1.2 billion. This hadn't been mentioned in the company's actual earnings release, and people started asking questions.

The investment "vehicle" was funded by Enron and a limited partnership created by Andrew Fastow-the erstwhile CFO who is now technically on a "leave of absence." This and transactions with similar partnership vehicles were part of a hedging strategy to balance Enron's technology investments. The strategy doesn't seem to have worked out very well, but the *Wall Street Journal* has reported that Fastow seems to have done OK, getting millions in partnership management fees. This week an SEC probe was announced.

Enron says it did nothing wrong and followed all the appropriate disclosure rules. That may well be the case-and, ultimately, the problem. It turns out that analysts and others who follow Enron have always found some elements of its financial structure to be rather bewildering, "hard to understand," even "impossible." But its announced earnings-which leave out some balance-sheet items-looked pretty good, and the stock was a superstar, jumping almost 200 percent over the two-year stretch ending in the summer of 2000. Having peaked at about \$90 back then, it's closer to \$17 now. And because those hedging arrangements are apparently tied to the health of Enron shares, it's now getting to the point that the fallout may well affect the company's debt rating and its actual bottom line.

In any case, it seems that plenty of investors (large and small) were willing to overlook what they didn't understand as long they liked what they *did* understand. This, I suspect, is not such an unusual investor attitude. And Enron's case, all that confusing stuff didn't really matter-right up until the moment that it did. Now that it does, Enron is left with not only the task of explaining itself clearly, but also of trying to convince shareholders to have more "faith and confidence" in the firm than the firm

itself has turned out to have in its CFO. Even the Goldman Sachs analyst who has been a great enthusiast for the firm urged its management to overcome "the appearance that you are hiding something." That is, the company has to not only be open with investors, but also to seem open. Doesn't that make it sound like Enron's future still depends as much on appearance as reality? Sure. But that's always true with stocks. Transparently so.

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, November 05, 2001 12:15 PM
To: Roseboro, Brian; Bitsberger, Timothy; Schultheiss, Heidilynne; Nickoloff, Peter; Gross, Jared; Sharer, James; Cetina, Jill
Subject: DJ: Enron Sr. Unsecured Debt Cut To Triple-B-Minus By Fitch

November 5, 2001

Enron Sr. Unsecured Debt Cut To Triple-B-Minus By Fitch

NEW YORK -- Fitch downgraded **Enron** Corp.'s (ENE) senior unsecured debt ratings Monday to triple-B-minus from triple-B-plus, putting the Houston energy and trading giant's credit rating just one notch above noninvestment-grade or junk status.

In its action, the rating agency was more aggressive than Moody's Investors Service and Standard & Poor's, both of which lowered Enron's long-term corporate credit ratings one notch last week to Baa2 and triple-B, respectively.

Fitch said its rating action Monday reflects the difficulties **Enron** faces in managing its liquidity position in the face of an erosion in investor confidence. This follows the recognition of a substantial diminution in value of its global merchant investments, which were partly financed with an aggressive use of off-balance sheet vehicles, the rating agency said.

Enron, though, should be able to manage through this challenging environment, ultimately recognizing the values of the company's core businesses, Fitch said.

In other rating actions, Fitch lowered Enron's subordinated debt to double-B from triple-B, while Enron's preferred stock was lowered to single-B-plus from triple-B-minus. Fitch cut Enron's commercial paper to F3 from F2.

Fitch also took action on the senior unsecured debt ratings of Enron's pipeline subsidiaries. The ratings of those units, Northern Natural Gas Co. and Transwestern Pipeline Co., were lowered to triple-B-minus from single-A-minus. The assets of Northern Natural and Transwestern were pledged last week to help **Enron** secure a new \$1 billion secured bank facility.

The rating agency said all of the ratings remain on "Rating Watch Negative" status.

Fitch said it would consider further downgrades if **Enron** was unable to make progress in reducing debt, if its wholesale marketing and trading business were to show signs of material deterioration, or if expenses and charges related to the disposition of non-core businesses and investments exceed present estimations.

A management priority is debt reduction and the exiting of problem businesses. Clearly, these actions, if completed as envisioned will reduce risk and improve the company's credit profile, Fitch said.

However, the targeted transactions have varying degrees of execution risk, particularly the divestiture of assets in emerging market countries, the rating agency said.

An additional uncertainty is the Securities and Exchange Commission's investigation of certain Enron-sponsored partnerships. The outcome and potential impact of the SEC activity is difficult to predict, Fitch said.

-By Joe Niedzielski, Dow Jones Newswires, 201-938-2039;

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, November 05, 2001 12:19 PM
To: Schultheiss, Heidlynnne; Nickoloff, Peter; Pietrangeli, Fred; Berardi, Steve; Whaley, Jean
Subject: WSJ: Enron Short Seller Detected Red Flags in Regulatory Filings

November 5, 2001

Heard on the Street

Enron Short Seller Detected Red Flags in Regulatory Filings

By CASSELL BRYAN-LOW and SUZANNE MCGEE

Staff Reporters of THE WALL STREET JOURNAL

In October 2000, short seller James Chanos labored through **Enron Corp.**'s annual report, underlining complicated passages and scribbling exclamation points and question marks.

The exercise set in motion an ultimately lucrative investment for the 43-year-old money manager, whose Kynikos Associates Ltd. long has been one of the largest and most visible of the firms that make bets that a stock will fall. Enron's books may have been hard to figure out. But Mr. Chanos spotted enough to bet that the then-highflying stock ultimately should tumble, because the company's success appeared to him less than met the eye.

Mr. Chanos, like any analyst either on the bull or bear side, isn't always right, of course. But he got this one right -- **Enron** shares have plummeted 86% this year to \$11.30 -- and the details of how he did it are illuminating. Over time, he would build up an 18-inch stack of regulatory filings and other material about **Enron**. While even he found the filings hard to understand, to him they raised multiple red flags. As it turns out, **Enron** shares have been hammered by some of the very things that alarmed Mr. Chanos as he sat in his 43rd-floor Manhattan office a year ago.

In Mr. Chanos's view, **Enron** had plenty of assets such as pipelines and utilities businesses, but it appeared to him to be a "hedge fund in disguise." Specifically, much of Enron's growth came from taking positions in the trading of energy contracts. To Mr. Chanos, that was similar to how a hedge fund -- those largely unregulated investment pools for the wealthy -- or a brokerage firm trades securities. But with one important qualification: By Mr. Chanos' measure, it wasn't as profitable as the average hedge fund. So why was it such a pricey stock? Mostly, Wall Street loved it because it consistently met or beat earnings targets.

No longer, of course. **Enron** stunned investors on Oct. 16 when it announced a third-quarter loss, and since then it has revealed a regulatory probe into its complex transactions with off-balance-sheet partnerships, some involving the company's own executives. **Enron** says its board has formed an

independent committee to review the transactions.

Mr. Chanos, president of Kynikos, declines to discuss specifics of his gains from shorting **Enron** stock (which entails selling borrowed shares and replacing them later with cheaper ones), other than to say it has been a successful move. He continues to maintain a short position, declining as well to comment on whether it has been or is now being scaled back. His short-only funds -- about half of the total \$1 billion under management -- boast returns of 24% so far this year, according to people familiar with the returns. That is a big contrast to some of the tough years endured during the raging bull market of the 1990's. For the past decade, the return is a negative 4.5%. (One of his bad calls: America Online, whose stock price soared after he bet that it would fall.)

Of short sellers such as Mr. Chanos, an **Enron** spokeswoman says: "It was in their financial interest to drive the stock price down, and they raised whatever doubts and whatever issues they could to further their own financial gain."

But Mr. Chanos says he was simply crunching whatever numbers he could find. "What struck us was, despite their market-leadership position, just how poorly they were doing in terms of returns." Mr. Chanos calculated that the company's return on invested capital, including debt, was roughly 7% for the year through Sept. 30, 2000, below his estimate of the company's cost of capital, between 9% and 12%. He felt the return on capital should be three to five points above the cost of capital to justify an investment. **Enron** has dismissed comparisons with a trading company in the past; it had no immediate comment Friday.

Enron shares were trading at about six times the company's book value in late 2000. By comparison, Wall Street brokerage firms typically trade at two or three times book value and hedge funds in effect are priced at book value.

Among the pages of the 1999 report that Mr. Chanos marked with yellow Post-it notes and scribbled comments was one detailing the related-party transactions. He underlined a sentence stating that one of **Enron's** senior officers is the "managing member" of a private investment company with which **Enron** had entered into a series of transactions. "We read the disclosure over and over and over again, and we just didn't understand it -- and we read footnotes for a living," he says. But at the time, he concedes, "it was just an odd footnote to us."

He started telephoning analysts at Wall Street firms to determine what aspects of the bulls' case he was missing. What he heard excited him further. Part of the bullishness focused on **Enron's** strategy of trading broadband-network capacity. Mr. Chanos, who already had placed bearish bets on some telecommunications bandwidth providers, was convinced that the industry already suffered from overcapacity and that the situation would only get worse. His conclusion: if **Enron** "couldn't see the looming train wreck coming in telecom, what else were they missing? Maybe they weren't as infallible in the energy area as people had thought."

Another warning signal was insider stock sales through the second half of 2000, he says. That sat awkwardly with the common refrain from Wall Street analysts that investors had to just trust management given the difficulty of analyzing how earnings were derived. The company didn't immediately comment on the sales on Friday.

"You look for patterns in my business," says Mr. Chanos. "The fact that this was a 'trust me' story, while management was voting with its feet was another check. While we didn't have a smoking gun, we certainly saw a reason to perhaps not trust management at its word that these earnings were what they said they were."

Those factors led Mr. Chanos to begin shorting the stock in late November of last year, when it was fluctuating between \$65 and \$80; he won't provide details. Overall, the level of short interest, or short-selling positions not yet closed out, on **Enron** shares jumped 2.2 million shares to 7.9 million shares for the month through mid December, from the same period in the previous month.

As other red flags surfaced, in February Mr. Chanos and other short sellers significantly ramped up the bearish positions. Mr. Chanos first discussed his view of **Enron** with those outside the firm that month in Miami, where he hosted his annual "Bears in Hibernation" conference. Attendees bring two ideas to present, and one of his was **Enron**.

With Enron's stock trading at \$72 at that time, or roughly 40 times 2001's per-share earnings estimates, "the market is priced for perfection here," Mr. Chanos told the 25 or so attendees, "whereas it looks like things may be anything but."

Back in New York, Mr. Chanos arranged a second round of sessions with bullish analysts. "Here's our thesis," he told them. "What are we missing?"

Mr. Chanos came out of those meetings with a "heightened conviction that we were right." For one thing, he sensed frustration brewing about the level of trust required with **Enron**.

As the spring progressed, Mr. Chanos became increasingly confident, adding to his short position. On a widely reported conference call in April, Jeffrey Skilling, then Enron's chief executive, responded to another short seller's criticism that **Enron** hadn't provided a balance sheet by calling him an "a--h---." For the first time, "I got a sense that the company was now getting tough questions and was not happy about it," Mr. Chanos says.

For their part, Wall Street analysts argue that they have limited time and resources for the in-depth research that Mr. Chanos prefers. Many cover dozens of companies. Still, some say they have learned lessons from Enron's fall from grace. Salomon Smith Barney analyst Raymond Niles, for one, says he will "pursue warning signs relentlessly and go by gut instinct" when he senses a looming problem. Says Mr. Niles, who covers **Enron**: "I think shorts play a very valuable role in the market, reminding us of what can go wrong."

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Oct. 16: **Enron** takes \$1.01 billion charge related to write-downs of investments. Of this, \$35 million is attributed to partnerships until recently run by CFO Andrew Fastow. **Enron** also discloses it shrank shareholder equity by \$1.2 billion, as a result of several transactions including ones undertaken with Fastow's investment vehicle.

Oct. 17: SEC sends letter to **Enron** saying it was beginning an "informal inquiry."

Oct. 19: The Wall Street Journal discloses that general partners of Fastow partnership realized more than \$7 million last year in management fees and about \$4 million in capital increases on an investment of nearly \$3 million in the partnership, set up principally to do business with **Enron**, according to internal partnership document. Enron's board meets to discuss SEC inquiry.

Oct. 22: **Enron** announces SEC will begin a probe of company's "related party transactions," including those with Fastow partnerships. **Enron** says it will fully cooperate.

Oct. 23: Enron's treasurer acknowledges the company may have to issue additional shares to cover potential shortfalls in investment vehicles it created, although he says the company believes it can repay about \$3.3 billion in notes that were sold by those investment vehicles without having to resort to issuing more stock.

Oct. 24: **Enron** replaces Fastow as CFO with Jeffrey McMahon, the 40-year-old head of the company's industrial-markets division. **Enron** shares fall 17% on heavy volume ahead of the announcement.

Oct. 25: The company draws down about \$3 billion, the bulk of its available bank credit lines, in a bid to restore confidence in its financial strength and liquidity. The Fitch rating agency puts **Enron** on review for a possible downgrade, while another, Standard & Poor's, changes Enron's credit outlook to negative from stable. A noninvestment-grade rating would throw the company into default on obligations involving billions of dollars of borrowings.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, November 05, 2001 12:23 PM
To: Schultheiss, Heidilynne; Nickoloff, Peter; Pietrangeli, Fred; Berardi, Steve; Whaley, Jean
Subject: WSJ: Enron Transaction With Entity Run by Executive Raises Questions

November 5, 2001

Money & Investing

Enron Transaction With Entity Run by Executive Raises Questions

By JOHN R. EMSWILLER

Staff Reporter of THE WALL STREET JOURNAL

In a transaction that raises new questions about **Enron** Corp.'s financial dealings with its management, the company in March made a \$35 million purchase from an entity run by a company officer.

That payment appears to have been the last step in a complex series of transactions that allowed **Enron** to keep hundreds of millions of dollars of debt off its balance sheet for the past three years, during which the Houston-based energy-trading giant has grown rapidly. In recent weeks, Enron's labyrinth of financial transactions, particularly with members of company management, has come under intense scrutiny from investors and regulators, who are seeking information about the impact of the transactions on the company and whether **Enron** adequately disclosed the deals to the public. **Enron** last week disclosed that the Securities and Exchange Commission had begun a formal investigation.

Enron officials have said repeatedly that all their actions were legal and properly disclosed. They have promised to cooperate with the SEC probe.

Enron officials wouldn't discuss the \$35 million transaction. What has been learned about it was gleaned from interviews with others familiar with the matter, snippets from **Enron** SEC filings and private partnership documents. Based on these sources, the **Enron** officer involved in the transaction was Michael Kopper, a former managing director of the company's **Enron** North America unit. The entity receiving the \$35 million was Chewco Investments LP. It wasn't clear from the available information what form the payment took or what, if any, gain Chewco or Mr. Kopper realized.

Mr. Kopper, who a company spokesman says left **Enron** in July, didn't return phone calls seeking comment. In the past, he has declined to be interviewed.

At **Enron**, Mr. Kopper was an associate of Andrew Fastow, the company's chief financial officer until

last month. In 1999, they set up and subsequently ran a private partnership known as LJM2 Co-Investment LP, which was involved in billions of dollars of transactions with **Enron**, according to private-partnership documents and company SEC filings. Those partnership documents indicate Mr. Fastow and possibly a handful of **Enron** associates, including Mr. Kopper, made millions of dollars in fees and investment gains from LJM2.

Last month, in response to mounting controversy over the partnership dealings, **Enron** replaced Mr. Fastow as chief financial officer. Mr. Fastow hasn't responded to numerous interview requests.

Chewco is mentioned in a brief biography of Mr. Kopper that is part of a 1999 offering memorandum for the LJM2 partnership. The document said Mr. Kopper, besides being a "principal" of LJM2, "manages the general partner of Chewco, an investment fund with approximately \$400 million in capital commitments that was established in 1997 to purchase from **Enron** an interest in a defined pool of **Enron** assets." The document doesn't specify what assets were purchased.

Chewco's name also appears as the debtor in a 1997 filing with the office of the Texas secretary of state. The secured party, and presumably the lender, on that debt was a limited partnership called Joint Energy Development Investments LP.

Known as JEDI, this limited partnership was created in 1993 by **Enron** and the huge California Public Employees' Retirement System to make energy-related investments. According to **Enron** SEC filings, the company and Calpers each put in \$250 million and an **Enron** affiliate served as JEDI general partner and operator.

Besides bringing in outside equity, entities such as JEDI allowed **Enron** to borrow large sums for asset purchases without that debt showing up on **Enron**'s balance sheet. In recent years, top **Enron** officials have said publicly that keeping down debt load was vital to protecting the company's credit rating and sustaining its tremendous growth. At the end of 1995, **Enron** had \$13.2 billion in assets; as of June 30, it had \$63.4 billion.

Messrs. Kopper and Fastow had "extensive involvement in the organization, investment activity and operations" of JEDI, according to the 1999 LJM2 private-offering memorandum. JEDI invested \$2.1 billion in 63 separate transactions, the document said. After accounting for JEDI's \$500 million in equity, this indicates the partnership borrowed as much as \$1.6 billion.

In 1997, Calpers sold its interest in JEDI back to **Enron** for about \$375 million. At about the same time, Calpers put \$500 million into a new **Enron** partnership, known as JEDI II.

At this point, **Enron** could have held on to all of JEDI, but that probably would have entailed consolidating the partnership and its debts into the company's financial statements.

That, apparently, is where Chewco came in. (Chewco got its name, says one person familiar with the matter, from the character Chewbacca in the "Star Wars" movies, where Jedi warriors also roamed.) Chewco bought from **Enron** the JEDI interest formerly held by Calpers, according to documents and interviews. It couldn't be determined what the terms of that transaction were. However, the fact that Chewco shows up as a debtor to JEDI in the Texas state filing suggests that money for the purchase was borrowed from JEDI itself.

The available information on the chain of transactions raises questions about how separate JEDI and Chewco really were from **Enron** and whether JEDI's assets and liabilities should have been folded into the company's financial statements.

In a March 2000 SEC filing, **Enron** makes a brief reference to its new JEDI partner, which **Enron** doesn't identify but presumably is Chewco. The filing said "an officer of **Enron** has invested in the limited partner of JEDI and from time to time acts as agent on behalf of the limited partner's management." While the officer isn't named, the description is similar to that given for Mr. Kopper in relation to Chewco in the LJM2 offering memorandum.

In March of this year, **Enron** moved to purchase the balance of JEDI that it didn't already own. In an SEC filing earlier this year, **Enron** said it acquired for \$35 million "the limited partner's interests" in JEDI. Again, the partner wasn't named, but presumably was Chewco.

Enron consolidated JEDI's assets and liabilities into the company. The SEC filing said JEDI's holdings included 12 million shares of **Enron** stock. **Enron** said it also paid off about \$620 million of JEDI "third-party debt." The third party or parties weren't named.

Oct. 16: **Enron** takes \$1.01 billion charge related to write-downs of investments. Of this, \$35 million is attributed to partnerships until recently run by CFO Andrew Fastow. **Enron** also discloses it shrank shareholder equity by \$1.2 billion, as a result of several transactions including ones undertaken with Fastow's investment vehicle.

Oct. 17: SEC sends letter to **Enron** saying it was beginning an "informal inquiry."

Oct. 19: The Wall Street Journal discloses that general partners of Fastow partnership realized more than \$7 million last year in management fees and about \$4 million in capital increases on an investment of nearly \$3 million in the partnership, set up principally to do business with **Enron**, according to internal partnership document. Enron's board meets to discuss SEC inquiry.

Oct. 22: **Enron** announces SEC will begin a probe of company's "related party transactions," including those with Fastow partnerships. **Enron** says it will fully cooperate.

Oct. 23: Enron's treasurer acknowledges the company may have to issue additional shares to cover potential shortfalls in investment vehicles it created, although he says the company believes it can repay about \$3.3 billion in notes that were sold by those investment vehicles without having to resort to issuing more stock.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, November 05, 2001 12:27 PM
To: Schultheiss, Heidilynne; Nickoloff, Peter; Whaley, Jean; Pietrangeli, Fred; Berardi, Steve
Subject: WSJ: Arthur Andersen Could Face Scrutiny On Clarity of Enron Financial Reports

November 5, 2001

Money & Investing



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Arthur Andersen Could Face Scrutiny On Clarity of Enron Financial Reports

By **JONATHAN WEIL**

Staff Reporter of THE WALL STREET JOURNAL

As **Enron Corp.**'s independent auditor, Arthur Andersen LLP has the job of making sure the Houston energy trader's financial statements not only are accurate and complete in all material respects, but also are understandable.

Now for the really tricky part: Understandable to whom?

For Andersen, this isn't just an academic question. Once again, the accounting practices of one of the Big Five firm's most prized clients have come under intense scrutiny from regulators and shareholders. Questions could well turn to whether Andersen fulfilled its obligation to protect investors' interests. And an important focus is likely to be whether Andersen should have required **Enron** to better explain its dealings with partnerships run by former Chief Financial Officer Andrew S. Fastow before agreeing to bless the company's financial statements.

Enron revealed last month, in a conference call, that its shareholder equity had fallen by \$1.2 billion during the third quarter as a result of transactions in which a partnership controlled by Mr. Fastow was at least at times involved, fueling a steep dive in the stock price amid growing concerns about the company's financial health. Many Wall Street analysts, including die-hard **Enron** bulls, long have grumbled that parts of Enron's financial statements are indecipherable.

"The heart of disclosure is intelligibility," says Alan Bromberg, a professor of securities law at Southern Methodist University in Dallas. "If the people to whom it's addressed can't understand it, it hasn't been adequately disclosed. There's clearly a qualitative, as well as a factual, component to disclosure."

Under generally accepted accounting principles, the rules for disclosing related-party transactions

seem straightforward enough. Among other things, companies must describe the "information deemed necessary to an understanding of the effects of the transactions on the financial statements." But the nation's accounting-standard setters never have offered any clear guidance on whether companies' disclosures should be understandable to a broad audience or merely to financially sophisticated individuals with specialized training. And even sophisticated investors are prone to being stumped now and then.

To be sure, the adequacy of a company's related-party disclosures can be determined only when all the information about the transactions is out in the open. For its part, **Enron** -- which is hardly the only large energy company with complex partnership dealings -- maintains its off-balance-sheet transactions were legal and properly disclosed. "They comply with reporting requirements," says **Enron** spokeswoman Karen Denne, adding that Andersen was aware of the transactions and reviewed them. "To the extent that an investor doesn't understand them, they are able to ask questions." And in the end, she notes, investors who didn't understand the transactions didn't have to buy **Enron** stock.

Enron's disclosure practices stand out, however, because they have been a source of complaints for so long. Even some top-flight accounting professors say they can't make heads or tails of the company's transactions with Mr. Fastow or **Enron's** motives for entering them. If they can't figure them out, it raises the question of whether any outsider could.

One thing is certain: The stakes for Andersen could be high. Since **Enron's** disclosure of the reduction in shareholder equity, its stock has plunged 67% to \$11.30 as of 4 p.m. in New York Stock Exchange composite trading Friday -- a drop that wipes \$20 billion off the company's market value and potentially exposing **Enron** and Andersen to massive shareholder liability. Already, **Enron's** dealings with the partnerships are the subject of a formal investigation by the Securities and Exchange Commission. That creates the possibility that Andersen itself could become a focus of the probe at some point, should regulators find **Enron's** accounting and disclosure practices deficient. Meanwhile, the law firm for a special committee set up by **Enron's** board has hired accounting firm Deloitte & Touche LLP to help review the partnerships' activities.

An Andersen spokesman, David Tabolt, says the firm "will continue to cooperate with [**Enron's**] special committee, lawyers and accounting advisers" and "will also cooperate with other official investigations as requested." So far, he says, the SEC hasn't told Andersen it is a subject of the **Enron** probe. Beyond that, he declines to comment on **Enron**, citing client-confidentiality obligations.

How murky are the related-party disclosures in **Enron's** audited financial statements? Here is a summary of a section in **Enron's** 2000 year-end financial statements describing certain transactions with the Fastow-operated partnerships. The company said it transferred assets valued at \$1.2 billion, including \$150 million in notes payable, 3.7 million restricted **Enron** shares and the right to receive as many as 18 million **Enron** common shares in March 2003, subject to certain conditions. It also transferred to the partnerships other assets valued at \$309 million, including a \$50 million note payable and "an investment in an entity that indirectly holds warrants convertible into common stock of an **Enron** equity method investee."

In return, **Enron** said it received "economic interests in the entities," \$309 million in notes receivable and an additional \$1.2 billion in notes receivable as part of a "special distribution." The disclosure went on to mention a series of purchases by **Enron** of "share-settled options from the entities" on shares of **Enron** common stock.

The raw numbers may all be there. But "any objective person would be hard pressed to understand the effects of these disclosures on the financial statements," says Douglas Carmichael, an

accounting professor at Baruch College in New York. "The quality of the disclosure is low, which creates uncertainty about the quality of their accounting."

Further, he says, Enron's explanation of why it entered the transactions "seems to defy imagination." In the year-end financial statement, **Enron** said the purpose was "to hedge certain merchant investments and other assets," a category that includes energy assets whose values are prone to wide price fluctuations. Yet the disclosure shows that **Enron** chose to use shares and options of its own stock as its chief hedging instrument, even though their price movements wouldn't appear to be directly related to the value of the investments **Enron** was trying to hedge.

"I don't see how that possibly hedges any of Enron's risks or assets," Mr. Carmichael says. Indeed, the disclosures have given rise to widespread speculation that Enron's actual purpose was to use its off-balance-sheet transactions to shift losses off its books to avoid running them through its income statement. Asked whether that was Enron's purpose, Ms. Denne declines to comment. She says **Enron** stands by its earlier statement that **Enron** was trying to hedge certain investments.

To date, Andersen hasn't been named as a defendant in any of the numerous shareholder lawsuits filed against **Enron**, which paid Andersen \$52 million last year, including \$25 million in audit fees. Enron's woes come during a year already filled with embarrassments for Andersen. In June, the SEC fined Andersen and three partners \$7 million over their audits of Waste Management Inc.'s financial statements, the largest SEC fine ever against an accounting firm. Andersen, which neither admitted nor denied the SEC's fraud allegations, paid \$75 million in 1998 to settle its portion of a shareholder lawsuit over the Houston-based garbage hauler. Also this year, without admitting wrongdoing, Andersen agreed to pay \$110 million to settle a shareholder lawsuit over audits it conducted for Sunbeam Corp.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, November 07, 2001 3:05 PM
To: Nickoloff, Peter; Schultheiss, Heidilynne
Subject: DJ: Calpers Board To Meet On Enron Investments Next Week

November 7, 2001

Calpers Board To Meet On Enron Investments Next Week

By JASON LEOPOLD

OF DOW JONES NEWSWIRES

LOS ANGELES -- The board of California's Public Employees' Retirement System plans to meet next week to discuss how best to protect its investments in **Enron Corp.** (ENE), a Calpers spokesman said Wednesday.

Calpers, which holds 3 million shares in the Houston energy company and a \$500 million stake in an **Enron** partnership called Joint Energy Development Investments II, has a history of shareholder activism, but it's too early to speculate on what steps the board may take, spokesman Brad Pacheco said.

Theoretically, the board could decide to take a more activist approach, because the energy company's stock is "underperforming," Pacheco said.

"If a company is underperforming, we focus on the board structure and sit down with the directors of the company and say these are the issues," Pacheco said. "If the company does not cooperate, we increase our shareholder propriety and we could move forward with several actions, including litigation, to say the board has breached its fiduciary responsibility."

Enron's shares fell to a low of \$7 Wednesday before rebounding on a Wall Street Journal report the company was in talks with Dynegy Inc. (DYN) for a cash infusion and potentially a full merger.

Concerns about the company's dealings with off-balance sheet partnerships like JEDI II have driven the decline, which has erased three-quarters of the company's share price since mid-October. Enron's credit ratings have also been downgraded.

Calpers hasn't yet approached **Enron** executives to discuss the plunge in the company's stock and the quality of its investment, Pacheco said.

Last week, California state Sen. Steve Peace, D-El Cajon, wrote Calpers Chief Executive James Burton urging the pension fund to take steps to defend its investment in **Enron**.

"Calpers may play a significantly larger and more active role in the governance of **Enron** to ensure that **Enron** directors do not have conflicting interests, that **Enron** adheres to a policy of full financial

disclosure and transparency and that Enron's board is comprised of a substantial majority of truly independent directors who understand their accountability to shareholders," Peace wrote in the Oct. 30 letter.

Calpers' board will discuss the letter in a closed-session meeting scheduled for Tuesday in Pasadena, Calif., but isn't bound to act on it because Peace isn't a boardmember, Pacheco said.

Calpers is the nation's largest public pension fund, with assets totaling approximately \$151 billion.

-By Jason Leopold, Dow Jones Newswires; 323-658-3874;

Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, November 13, 2001 12:51 PM
To: Nickoloff, Peter; Schultheiss, Heidilynne; Cetina, Jill; Sharer, James; Adams, Fred; Pietrangeli, Fred; Berardi, Steve; Anderson, Helen; Ludwick, CM; Whaley, Jean
Subject: Nice work if you can get it

Enron CEO May Get at Least \$60.6 Million After Buyout (Update2)

By Margot Habiby

Houston, Nov. 13 (Bloomberg) -- Enron Corp. Chairman and Chief Executive Officer Kenneth Lay may get \$60.6 million or more in severance if he leaves after Enron's sale to Dynegy is completed, according to a regulatory filing.

Lay is entitled to receive a lump sum payment equal to \$20.2 million, multiplied by the number of full calendar years remaining on his contract, if he terminates his employment under certain circumstances, such as the acquisition by Dynegy, Enron said in a filing with the U.S. Securities and Exchange Commission.

Dynegy says its buyout of Enron, the biggest energy trader, is expected to close in 2002's third quarter. Lay's contract expires at the end of 2005. His contract provides that he also receive an amount to cover tax penalties if the payment he gets is considered an "excess parachute payment," the SEC filing said.

Enron agreed on Friday to be acquired by rival Dynegy for at least \$23 billion in stock and assumed debt, ending a financial crisis that threatened to bankrupt Enron and disrupt U.S. power and natural-gas markets. Lay has said he won't be an active manager in the new company, which will be led by Dynegy Chairman and CEO Chuck Watson.

Lay's contract was extended by two years, to the end of 2005, when he resumed the CEO's job following the departure of Jeffrey Skilling in August. If Enron's buyout by Dynegy were to close this year, or if there were another form of "change of control" at Enron, Lay may receive \$80.8 million, the Enron filing indicates.

Pay Package

Enron more than tripled Lay's pay package last year to \$18.3 million following the company's best share-price performance in 20 years, according to a proxy filed in March with the SEC. Enron shares have plunged 90 percent this year. Lay made \$5.97 million in 1999, according to Enron's proxy statement filed with the SEC.

Lay also received options to buy 782,830 shares over seven years, most at \$47.31 each, the March filing said. Those options are now worthless because Enron's stock price is below the price at which they could be exercised. Lay had gains of \$123.4 million from the exercise of options in 2000.

Enron's has been battling a cash crunch and a loss of investor confidence this year because of questions about partnerships it started and put under the control of its senior executives.

After the Enron acquisition, top managers at Dynegy will include Dynegy's Steve Bergstrom as president and chief operating officer, Dynegy's Robert Doty as chief financial officer and Enron's Greg Whalley as executive vice president. Whalley is Enron's president and chief operating officer.

Shares of Enron rose 21 cents to \$9.45 in midday trading. Dynegy rose 91 cents to \$45.22. Both companies are based in Houston.

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, November 14, 2001 10:22 AM
To: Roseboro, Brian; Bitsberger, Timothy; Nickoloff, Peter; Schultheiss, Heidilynne; Gross, Jared; Cetina, Jill; Sharer, James
Subject: Dow Jones Newswires: EnronOnline Competitor Reports Record Trading Volumes

November 13, 2001

EnronOnline Competitor Reports Record Trading Volumes

NEW YORK -- IntercontinentalExchange, an Internet-based energy and metals trading operation, saw record trading volumes last week, due in part to troubles at **Enron Corp. (ENE)**, an ICE press release said Tuesday, without mentioning **Enron** by name.

Investors have been watching to see if Enron's trading partners in its core business - North American gas and power marketing - significantly reduce activities with the financially troubled top energy marketer. ICE is considered a primary alternative to Enron's Internet-based commodities market, EnronOnline.

ICE's volume of North American bulk power trades last week totaled a record 54 million megawatt-hours, a 34% increase over the October weekly average. North American natural gas volumes rose 13% from October to 950 billion cubic feet last week. Oil trading rose 45% to a record 55 million barrels, and metals trading volumes was up 66%.

"We believe that this has resulted, in part, from the uncertainty that has been exhibited in several key energy trading venues over the past several months," said ICE chief executive, Jeffrey Sprecher.

EnronOnline is different from ICE because EnronOnline is a mechanism for companies to buy from, and sell to, **Enron**. ICE is a neutral multiparty exchange, allowing energy trading companies to trade with all other members.

ICE's trading system, which has been installed in 7,000 desktops worldwide, covers 600 commodity and derivative contract types. ICE also owns the International Petroleum Exchange of London, Europe's largest energy futures exchange.

ICE is owned by companies including American Electric Power (AEP), Aquila Energy (ILA), BP Amoco PLC (BP), Deutsche Bank AG (G.DBK), El Paso Corp. (EPG), Goldman Sachs Group (GS), Morgan Stanley Dean Witter & Co. (MWD), Reliant Energy (REI), Royal Dutch/Shell Group (RD), Societe General SA (F.SGF), Mirant Corp. (MIR) and TotalFina Elf SA (TOT).

-By Mark Golden, Dow Jones Newswires; 201-938-4604; mark.golden@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, November 14, 2001 10:34 AM
To: Roseboro, Brian; Bitsberger, Timothy; Cetina, Jill; Sharer, James; Schultheiss, Heidilynne; Nickoloff, Peter; Gross, Jared
Subject: Dow Jones Newswires: Enron-Dynegy Deal Has Nov. 30 2002 Walkaway Date

November 14, 2001

Enron-Dynegy Deal Has Nov. 30 2002 Walkaway Date

WASHINGTON – Dynegy Inc.'s (DYN) proposed \$7.8 billion acquisition of **Enron** Corp. (ENE) carries two breakup fees and must be completed by Nov. 30, 2002, unless extended, or either party can walk away.

The proposed merger agreement can be terminated at any time by the mutual consent of both parties, according to a filing Wednesday with the Securities and Exchange Commission.

If the deal is terminated because Enron's board withdraws its recommendation to shareholders or opts for a superior proposal, **Enron** would have to pay \$297.5 million to Dynegy and \$52.5 million to ChevronTexaco Corp. (CVX), as well as \$10 million for expenses.

ChevronTexaco, which owns about 26% of Dynegy, has agreed to invest \$2.5 billion into Dynegy in conjunction with the acquisition of **Enron**, a Houston-based utilities and communications company.

Dynegy would have to pay a \$350 million breakup fee, plus \$10 million for expenses, if the deal is terminated because of a change in the board's recommendation or a superior proposal.

Under the terms of the deal, announced Tuesday, **Enron** shareholders will receive 0.2685 a Dynegy share for each **Enron** share.

-Robert L. Grant; Dow Jones Newswires; 202-393-7851 robert.grant@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, November 16, 2001 9:13 AM
To: Roseboro, Brian; Bair, Sheila; Gross, Jared; Nickoloff, Peter; Schultheiss, Heidilynne; Pietrangeli, Fred; Berardi, Steve; Bitsberger, Timothy; Novey, Michael; Eichner, Matthew; Hammer, Viva
Subject: The Economist: Enron -- See you in court

Enron

See you in court

Nov 15th 2001 | NEW YORK
From The Economist print edition

The company's trials have just begun

LAWYERS are swarming all over Enron's old financial statements and press releases in the hope of reaping huge fees from securities litigation. More than 20 class-action lawsuits have been filed in recent weeks, and new ones are popping up every day. A formal process has been started to consolidate litigation in Houston, where the troubled energy company is based, with all lawyers interested in the case required to stake their claims by December 21st.

The broadest accusations will be of fraud and material misstatement, legal ways of saying that the company's financial statements were garbage. This week, Enron's founder and chairman, Kenneth Lay, decided to forgo a severance package worth over \$60m while admitting that the company's problems "had been exacerbated by the extensive use of debt capital, both on and off the balance sheet". America's Financial Accounting Standards Board (FASB) is looking again at off-balance-sheet financing, having fretted about it on and off for a decade.

There will also be charges of insider trading, because even as Enron was issuing securities amid glowing profits reports, top executives were dumping over \$1 billion of Enron shares to "unsuspecting investors", a group that includes anybody who, however briefly, has held one of the company's 750m shares in the past two years. "The number of class members will be huge," says Maurice Pessa, a lawyer at a New York firm that has filed a claim.

There are, however, limits to the company's liability. It has already restated its results going back five years, but federal law restricts litigation to the past three. Moreover, Enron will not take the rap alone. Its auditor, Arthur Andersen (now plain Andersen), is also named as a defendant in at least one of the complaints already filed. The litigation comes after a rough decade for Andersen. It has had to pay hundreds of millions of dollars in settlements after sloppy audits on such companies as Waste Management, Sunbeam and Discovery Zone.

Because Enron evolved from an energy company into a financial firm, it became much like an unregulated bank. The lack of supervision meant that the role of the company's auditor was crucial. Andersen was certainly paid as if it was. In 2000, it collected \$25m for auditing Enron's books and another \$27m for consulting services. Now how do you account for that?

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, November 16, 2001 9:37 AM
To: Roseboro, Brian; Bitsberger, Timothy; Gross, Jared; Nickoloff, Peter; Schultheiss, Heidi; Pietrangeli, Fred; Berardi, Steve; Cetina, Jill; Sharer, James; Novey, Michael; Eichner, Matthew; Hammer, Viva
Subject: NYT: Did Ken Lay Understand What Was Happening at Enron?

November 16, 2001

FLOYD NORRIS

Did Ken Lay Understand What Was Happening at Enron?

What a tangled web was weaved by Enron. Both investors and managers seem to have been misled.

"Enron became overleveraged," Kenneth L. Lay, Enron's chairman and chief executive, said this week, adding that things went wrong in ways that "I could not have ever contemplated." He pointed to investments that "performed far worse than we ever could have imagined."

That was the first time that Enron had admitted it had a leverage problem, and it came only after the brutal reality had become apparent to many others. Mr. Lay says he understood what was going on, but I suspect he had left crucial details to others who have since departed and did not fully grasp the reality that was obscured by Enron's soothing financial statements.

When Enron was riding high, it could easily have sold stock to raise capital that it now desperately wants. Mr. Lay and other executives sold stock, but the company did not. Just a month ago, Mr. Lay spoke enthusiastically of how great the company's continuing earnings were.

The leverage was not easy to find. A lot of it was carried off Enron's balance sheet. Partnerships and special-purpose entities that Enron set up borrowed money and funneled the cash to Enron. Enron guaranteed the debt but did not have to show it on its own balance sheet because it could meet its obligations by issuing stock. As undisclosed losses built up in those entities, it became more likely they could not pay their bills, leaving Enron to do so.

It is also clear that the bond rating agencies did not understand Enron's plight until the last couple of weeks. When they figured it out, it took a \$1.5 billion equity infusion that is part of the Dynegy (news/quote) takeover to keep Enron's rating above junk level.

Now Enron has a board committee investigating various transactions, and promises to release details as they are uncovered. Officials speak as if they are learning what happened for the first time, and perhaps they are. Jeffrey Skilling, Mr. Lay's protégé, was Enron's chief financial engineer until he quit this summer. And Enron's chief financial officer and treasurer were ousted as Enron unraveled.

Some investors would say none of that matters now, that the only important fact is that Dynegy is buying Enron anyway. Chuck Watson, Dynegy's chief executive, is convinced that Enron's energy trading business is a gem that more than justifies the price Dynegy is paying. He figures the losses from the bad investments can be contained.

The big question now may be whether Mr. Watson will retain his enthusiasm after his people study Enron's trading positions. Enron has always said it hedged its big derivative positions - positions that can contain huge leverage that does not show up on the balance sheet - but some of that hedging was with affiliated companies. If big surprises are found, Dynegy could back out of the deal.

There is plenty of blame to go around here, and suits have been filed against Enron, its current and former officials, and its auditor, Arthur Andersen. But investors also bear responsibility. Enron's financial statements were, as Mr. Lay conceded this week, "opaque and difficult to understand." Investors and analysts knew they did not know what was going on. They bought anyway.

Enron was viewed as a company that always made its numbers. An old-line gas pipeline company had been transformed into a brilliant trader that could apply its magic around the world. Investors did not care how Enron made the numbers. Now, when it is too late, they do.

Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, November 20, 2001 4:43 PM
To: Wiedman, Mark; Nickoloff, Peter; Cetina, Jill; Sharer, James; Berardi, Steve; Pietrangeli, Fred; Schultheiss, Heidilynne; Whaley, Jean
Subject: FW: Bloomberg: Enron Falls Amid Concern Debt Threatens Dynegy Bid (Update5)

-----Original Message-----

From: Carleton, Norman
Sent: Tuesday, November 20, 2001 4:41 PM
To: Roseboro, Brian; Bair, Sheila; Bitsberger, Timothy
Subject: Bloomberg: Enron Falls Amid Concern Debt Threatens Dynegy Bid (Update5)

11/20 16:05

Enron Falls Amid Concern Debt Threatens Dynegy Bid (Update5)

By Stacie Babula

Houston, Nov. 20 (Bloomberg) -- Enron Corp. shares and bonds dropped after the energy trader disclosed it may have to pay \$9.15 billion in debt due by 2003, suggesting the company may run out of cash before its takeover by Dynegy Inc. can be completed.

Shares of Enron fell \$2.05, or 23 percent, to \$7.01. Earlier they touched \$6.55, the lowest price in more than a decade. Enron's 6.4 percent notes due in July 2006 were bid as low as 69 cents on \$1 of face value and offered at 73 cents, down more than 13 percent in light trading, traders said.

Enron, whose dealings with affiliated partnerships led to earnings restatements, credit-rating cuts, a federal investigation and a management shakeup, said in a regulatory filing that it has less than \$2 billion in cash or credit lines. Dynegy plans to complete its buyout by October, and Enron may have to ask lenders to restructure payment schedules to survive.

"This filing shows that Enron is in a precarious financial situation," said Commerzbank Securities analyst Andre Meade, who rates Enron shares "hold" and doesn't own them. "They have to stay afloat for the Dynegy deal to go through, and that now looks difficult."

Enron and Dynegy wouldn't comment on the stock drop today. Standard & Poor's Investors Service said that Enron's credit rating remained on negative watch, indicating it would not immediately downgrade the company's debt.

\$690 Million Surprise

"Enron's near-term liquidity position is... expected to be sufficient to carry the company through the completion of its proposed merger with Dynegy," S&P said in a report.

Investors were concerned the debt, including a \$690 million note that Enron disclosed it may have to pay off next week, would lead to a cut in Enron's credit rating, analysts said.

The filing was a "distraction" that will not threaten the merger, said Todd Shipman, a director at S&P who follows Enron.

"Our approach to this has been on the basis that the Dynegy deal is a good thing for credit quality," Shipman said.

Moody's Investors Service, which didn't issue a statement on Enron's debt today, kept the company's credit rating at investment grade on Nov. 9, the day Dynegy announced it would buy Enron in a deal now valued at \$25 billion.

The ruling came after executives from Lehman Brothers Holding Inc., J.P. Morgan Chase & Co. and Citigroup Inc.'s Salomon Smith Barney lobbied the credit-rating company, people familiar with the situation said.

Avoiding Junk

A junk rating would have led Dynegy to abandon the acquisition, Dynegy Chief Executive Officer Charles Watson said. It would also have triggered debt repayment of at least \$3.9 billion, Enron said in a Securities & Exchange Commission filing yesterday.

Enron shares are selling for almost 32 percent less than the value of Dynegy's offer, showing investors have doubts the deal will be completed. Dynegy shares fell \$1.90 to \$41.70 today.

"It's become more clear that the chances of this deal going through aren't 90 percent, but much closer to fifty-fifty," said Edward Paik, who helps manage the Liberty Utilities Fund, with 1.6 million Enron shares. "There's just so much information that is unknowable" about Enron's financial position, he said.

Most of the \$9.15 billion in debt is due before the end of the third quarter, when the Dynegy buyout is scheduled to close, Enron said yesterday in a third-quarter filing with the SEC.

Asset Sales Planned

Last week, Enron Chief Operating Officer Greg Whalley said the company will sell assets of "non-core businesses" to raise money. It has \$8 billion invested in the businesses, including broadband telecommunications and the Dabhol power plant in India. Enron expects to get "billions" from the sales, Whalley said, without being more specific.

Enron reported yesterday that its U.S. operations had \$1.2 billion in cash left. It has added at least \$5 billion since Sept. 30 from credit lines, loans and a \$1.5 billion investment from ChevronTexaco, part owner of Dynegy.

Enron used \$1.9 billion of the money it raised to retire commercial paper, which is short-term debt. It gave no details on how it spent the remaining \$3.1 billion.

Enron Chief Financial Officer Jeffrey McMahon said last week that the company also was looking to get another \$500 million to \$1 billion from private investors.

Asset sales valued at about \$800 million are expected to close by the end of this year, according to the SEC filing. Enron spokeswoman Karen Denne wouldn't comment on whether it could sell assets fast enough to keep current on its debts.

Dynegy will have to help Enron sell assets, said Mitchell Stapley, who manages \$3.5 billion in fixed-income assets including Enron bonds for Fifth Third Investment Advisors Inc.

Dynegy and ChevronTexaco Corp., which owns 26 percent of Dynegy, also will have to help Enron negotiate with its lenders, said Kathleen Vuchetich, who helps manage the \$1.4 billion Strong American Utilities Fund, which is 5 percent Dynegy shares.

Debt Questioned

"I never dreamt (the \$9.15 billion) would be that large, coming due all at once," Vuchetich said. "It calls into question their decision to schedule it that way in the first place."

ChevronTexaco, the second-largest U.S. oil company, is providing \$2.5 billion in cash as part of the Enron buyout. It provided the first \$1.5 billion a week ago.

Shares of ChevronTexaco, based in San Francisco, rose \$3.62 to \$86.53.

Enron yesterday reduced third-quarter results by 3 cents a share, bringing the period's loss to 87 cents, or \$664 million. On Nov. 8, Enron lowered earnings back to 1997 by \$586 million to reflect losses by affiliated partnerships that were wrongly kept off the books. That included a third-quarter reduction of \$17 million.

A drop in Enron's senior unsecured debt rating to "BBB-" by Standard & Poor's on Nov. 12 may force Enron to pay off a \$690 million note by Nov. 27 if it doesn't find collateral to guarantee the debt taken on by an affiliated partnership that owns Brazilian natural-gas assets, the filing said.

Without repayment or collateral, investors can begin to liquidate the partnership's assets, Enron said. The company said it's working with lenders to come up with an acceptable agreement on the debt.

Making good on debt owed by its Whitewing affiliated partnership may cut Enron's fourth-quarter earnings, Enron said. Enron is obligated to back Whitewing by issuing junior convertible preferred stock. Because Enron's stock has plunged, it may have to write down its assets by \$700 million, the filing said.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, November 20, 2001 5:06 PM
To: Roseboro, Brian; Bair, Sheila; Wiedman, Mark; Gross, Jared; Cetina, Jill; Sharer, James; Nickoloff, Peter; Schultheiss, Heidi Lynne; Berardi, Steve; Pietrangeli, Fred; Whaley, Jean; Lori Sanatamarena (E-mail); Novey, Michael; Hammer, Viva; Eichner, Matthew; Gabilondo, Jose
Subject: Dow Jones Newswires: Energy Cos Limit Business With Enron After 10Q -Traders

November 20, 2001

Energy Cos Limit Business With Enron After 10Q -Traders

Dow Jones Newswires

By Mark Golden
Of DOW JONES NEWSWIRES

NEW YORK – Many energy trading companies were unwilling to sell power and natural gas for next day delivery to **Enron Corp.** (ENE) Tuesday morning, a result of heightened credit concerns following the release of Enron's quarterly financial report Monday, traders and other sources said.

For weeks, companies have limited both buying and selling with **Enron** for future deliveries. But for the first time since Enron's troubles began a month ago, energy companies weren't selling to **Enron** in the spot markets for fear that **Enron** might not be able to pay its bills as soon as next month.

"It's pretty well accepted in the industry that people are staying away for now," said Charlie Sanchez, energy market manager for Gelber & Associates in Houston.

Traders at all of the major companies contacted said they couldn't sell to **Enron** Tuesday morning. Several spokespeople for energy companies confirmed the situation, but declined to say so on the record.

"Nobody will take **Enron**," one western electricity broker said. After struggling, however, that broker eventually found a utility that was willing to sell to **Enron** Tuesday morning.

Calpine, a prominent independent power producer and trader, said it was willing to sell power to **Enron**.

"We continue to sell power to **Enron** and are monitoring the situation closely," spokeswoman Catherine Potter said.

The situation Tuesday morning was fluid. One utility that refused to sell to **Enron** in the morning was willing to do so in the afternoon, a person at the company said. That company's trading, however, was still limited to the spot markets.

Credit concerns about the once-dominant energy trading company were heightened with Enron's filing of its third quarter annual report Monday evening with the U.S. Securities Exchange

Commission.

Enron may have to pay \$690 million on a note that became a demand obligation with the company's most recent credit-rating downgrade, **Enron** said in Monday's filing. The company also warned that its profits in the fourth quarter could be hurt by credit concerns, a decline in asset values and reduced trading activity.

"The 10Q in and by itself is a document that could raise concerns," Fitch analyst Ralph Pellecchia said. "We have a lot of questions outstanding relative to disclosures that were new to us and their strategies of how they are going to manage the situation."

Companies are willing to buy from **Enron** in the spot gas and power markets, because taking delivery on commodity and paying for it a month later poses no credit risk for the buyer

An **Enron** spokesman didn't respond to a request for comment.

Reliant Resources (RRI) and the Bonneville Power Administration, the federal government's western power marketer, both said their organizations are continuing to "do business" with **Enron**. But when asked specifically if they were selling spot power or gas to **Enron**, spokesmen for both declined to comment.

"We're watching the situation very carefully," said Reliant spokesman Richard Wheatley. "There is a lot of speculation because of the filing yesterday."

Energy companies began shying away from **Enron** over the past month, as concerns about its finances precipitated a 75% drop in its stock price and left its bonds trading at levels typically associated with junk-rated debt.

Traders and their companies have said consistently that until Enron's credit ratings improve, they will continue to watch their exposure to **Enron** carefully, with trades limited to short-term deals.

Moody's Investors Service, Standard & Poor's and Fitch all rate **Enron** one notch above speculative grade. Moody's has Enron's ratings on review for a downgrade, and S&P has **Enron** on negative credit watch. Fitch calls Enron's credit rating "evolving." Enron's ability to do business in the energy markets depends on its maintaining investment-grade ratings.

The manager of one hedge fund that follows **Enron** closely said Tuesday that several trading companies expressed strong concerns about Enron's financial viability. But the manager thought those concerns weren't proportionate to Enron's position.

"They have nine days to work out the \$690 million debt payment, and if they can't work it out, they have the cash to make the payment," the manager said.

Dynegy Inc. (DYN), which has agreed to buy **Enron** in a stock-swap currently worth about \$10 billion, injected \$1.5 billion into **Enron** last week. **Enron** has also closed on \$1 billion worth of revolving credit lines with J.P. Morgan Chase & Co. (JPM) and Citigroup (C) in the past week, with \$450 million of that amount closed Monday.

Developments with **Enron**, however, have raised enough concerns that energy companies aren't willing to extend themselves into positions that have even the appearance of vulnerability, Sanchez of Gelber & Associates said.

"The industry has been shell-shocked by their recent announcements, and they're not ready to go back to trading with them," said Sanchez of Gelber & Associates.

Some traders wondered why Dynegy hasn't stepped in to buy energy from sellers and then sell that product to **Enron**. Such a move, known as "sleeving" in energy markets, serves as an ad hoc form of credit guarantee one transaction at a time.

Dynegy didn't return phone calls on the matter.

-By Mark Golden, Dow Jones Newswires; 201-938-4604; mark.golden@dowjones.com

(John Edmiston in Houston, Kristen McNamara in New York and Jon Kamp in Chicago contributed to this article.)

Reached later, Dynegy made clear it wouldn't take any extraordinary measures to support **Enron** in the market.

"We will operate as two separate companies until the merger is completed," Dynegy spokesman John Sousa said. "We have to act independently."

Mirant Corp. (MIR), a major trader of North American power and gas, has trimmed its business with **Enron**.

"We're trading on a very limited basis," said spokesman Chuck Griffin, who wouldn't be more specific.

Cinergy Corp. (CIN), a mid-sized energy trading company, said it is buying and selling gas and power with **Enron**.

-By Mark Golden, Dow Jones Newswires; 201-938-4604; mark.golden@dowjones.com

(John Edmiston in Houston, Kristen McNamara in New York and Jon Kamp in Chicago contributed to this article.)

Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, November 20, 2001 5:11 PM
To: Roseboro, Brian; Bair, Sheila; Wiedman, Mark; Bitsberger, Timothy; Gross, Jared; Schultheiss, Heidilynne; Nickoloff, Peter; Berardi, Steve; Pietrangeli, Fred; Whaley, Jean; Novey, Michael; Eichner, Matthew; Hammer, Viva; Gabilondo, Jose; Lori Sanatamarena (E-mail)
Subject: DOW JONES NEWSWIRES: Dynegy Won't Comment On Merger Partner Enron's 10-Q

November 20, 2001

Dynegy Won't Comment On Merger Partner Enron's 10-Q

By CHRISTINA CHEDDAR

OF DOW JONES NEWSWIRES

NEW YORK -- Dynegy Inc. (DYN) declined Tuesday to comment on whether its merger with **Enron** Corp. (ENE) would be affected by the contents of Enron's quarterly filing with the Securities and Exchange Commission late Monday.

In the 10-Q, which was filed five days past the SEC deadline, **Enron** revised its third-quarter earnings downward by 3 cents a share, and disclosed it may have to pay off a \$690 million note owed to an affiliated partnership because a clause in a financial agreement was triggered by the reduction in Enron's senior unsecured debt rating to triple-B-minus by Standard & Poor's a week ago.

The amount will have to be paid by Nov. 27 if **Enron** doesn't find collateral to guarantee the debt, the company said in the filing. **Enron** is working to come up with an acceptable agreement on the debt, but didn't disclose who holds the note.

Enron used partnerships in order to hedge its investment risk, and in some cases to keep the debt off its balance sheet. The practice is being investigated by the SEC and by an internal committee **Enron** has named.

In the filing, **Enron** also said it may have to take a \$700 million pretax charge to earnings for the declining value of assets held by another partnership, Whitewing LLP.

When asked if Dynegy had known about the collateral call on the debt or about the decline in Whitewing's value, a Dynegy spokeswoman declined to comment.

"We are referring all questions about the **Enron** 10-Q to **Enron**," said the spokeswoman. Representatives of **Enron** weren't immediately available for comment.

Dynegy agreed to buy **Enron** earlier this month. Earlier Tuesday, the deal was worth about \$11.97 billion in stock, but **Enron** shares were trading at a 32.5% discount to the offer price earlier Tuesday morning, which is a sign of the uncertainty surrounding the transaction.

Enron shares were recently trading at \$7.86, down \$1.20, or 13.2%, while Dynegy shares changed hands at \$43.29, down 31 cents, or 0.8%.

A ChevronTexaco Corp. (CVX) official wasn't immediately available to comment on the matter.

ChevronTexaco, San Francisco, owns 26% of Dynegy and is providing \$2.5 billion in cash to Dynegy as part of the buyout. Last week, an initial payment of \$1.5 billion was transferred to Dynegy and then to **Enron** to help meet Enron's immediate cash needs.

Dynegy's merger agreement with **Enron** contains several provisions beyond the standard "material adverse change" provision that would allow the deal to be terminated. Still, some question whether Dynegy was able to fully assess Enron's liabilities prior to striking the deal.

Investors have expressed frustration with Enron's lack of disclosure, and even marvelled at the fact that the 10-Q included material that could have been mentioned in previous filings or company conference calls.

-By Christina Cheddar, Dow Jones Newswires; 201-938-5166
christina.cheddar@dowjones.com

(Corrected 1:50 PM)

Later, Dynegy spokeswoman Jennifer Rosser said Enron's filing Monday was an "important step" in the due diligence process Dynegy was undergoing as part of its pending acquisition of **Enron**.

"This kind of filing is exactly what due diligence is about," she said.

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, November 21, 2001 12:08 PM
To: Roseboro, Brian; Bair, Sheila; Gross, Jared; Bitsberger, Timothy; Nickoloff, Peter; Schultheiss, Heidilynne; Whaley, Jean; Pietrangeli, Fred; Berardi, Steve; Novey, Michael; Hammer, Viva; Eichner, Matthew; Lori Sanatamarena (E-mail); Cetina, Jill; Sharer, James
Subject: Dow Jones Newswires: Enron Dn 20%; Goldman Doubts Ability To Recover Business

November 21, 2001

Enron Dn 20%; Goldman Doubts Ability To Recover Business

Dow Jones Newswires

By Michelle Rama
Of DOW JONES NEWSWIREs

NEW YORK -- Investors bailed out of **Enron** Corp. (ENE) as shares continued their dismal descent Wednesday, falling more than 30% for a second day of declines after a company filing revealed even more financial problems than previously disclosed.

Enron's 10-Q filing Monday with the Securities and Exchange Commission prompted at least one analyst to downgrade the company's shares.

Goldman analyst David Fleischer cut Enron's shares to market perform from its recommended for purchase list, citing "concerns about ENE's ability to recover the significant business that has been lost and new and major liquidity issues raised in Monday's 10Q filing."

"The cash infusion from Dynegy appears inadequate to restore the confidence of **Enron** customers and we now question the accretion to Dynegy in a combination and valuation of energy convergence shares during the current uncertain period," Fleischer said in the note.

If the deal's potential earnings accretion to Dynegy is questioned, investors may doubt whether Dynegy will buy **Enron**. Enron's ability to stay in business is questionable if Dynegy backs out of the deal.

Enron officials weren't immediately available for comment.

Shares of **Enron** recently changed hands at \$4.99, down 28.6%, or \$2, on volume of 32.5 million. Average daily volume is 19.7 million shares.

Dynegy shares recently traded at \$39.16, down \$2.54, or 6.1%, on volume of 5 million. Average daily volume is 3.2 million shares.

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, November 21, 2001 1:14 PM
To: Roseboro, Brian; Bair, Sheila; Gross, Jared; Wiedman, Mark; Cetina, Jill; Sharer, James; Pietrangeli, Fred; Berardi, Steve; Whaley, Jean; Nickoloff, Peter; Schultheiss, Heidilynne; Novey, Michael; Hammer, Viva; Eichner, Matthew; Bitsberger, Timothy
Subject: Bloomberg: Enron Gets Extension on \$690 Mln Note Due Next Week (Update1)

11/21 12:38

Enron Gets Extension on \$690 Mln Note Due Next Week (Update1)

By Mark Johnson

Houston, Nov. 21 (Bloomberg) — Enron Corp., whose shares had dropped 92 percent this year amid a financial crisis, said lenders extended to mid-December the payment date on a \$690 million note due next week.

Enron, which agreed to be bought out by rival energy trader Dynegy Inc. in a transaction now valued at more than \$23 billion, said earlier this week a drop in its credit rating may force it to repay the \$690 million note. The repayment would strain cash reserves Enron needs to back its trading operations, investors and analysts said.

The Houston-based company didn't say in its release who holds the note, which is owed by an affiliated partnership that owns Brazilian natural-gas assets and was backed by Enron.

The note is held by a group of banks led by the Citibank unit of Citigroup Inc., Standard & Poor's said in a press release yesterday.

Enron also is in discussions with other lenders on a restructuring of its debt, the company said in a statement distributed by PR Newswire.

"We believe the interests of Chase and Enron's other primary lenders are aligned in this restructuring effort," James Lee, vice president of JP Morgan Chase & Co., said in the Enron statement. "We will work with Enron and its other primary lenders to develop a plan to strengthen Enron's financial position up to and through its merger with Dynegy." Morgan has been advising Enron on its merger with Dynegy.

Enron said yesterday it may have to pay \$9.15 billion in debt due by 2003, suggesting the company may run out of cash before the merger closes. Dynegy has said the merger should close before the end of the third quarter of 2002.

Enron said in a regulatory filing that it has less than \$2 billion in cash or credit lines.

Shares of Enron, the most active stock in U.S. trading, fell \$1.79, or 23 percent, to \$5.20 in midday trading. Before the announcement that it had renegotiated the \$690 million note, its shares had fallen as much as 42.78 percent, the lowest level in more than a decade.

Dynegy fell \$2.50, or 6 percent, to \$39.20. Shares of ChevronTexaco Corp., which owns 26 percent of Dynegy, rose 49 cents to \$87.02

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, November 21, 2001 1:22 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: Dow Jones Newswires: Enron Closes On \$450M Secured Credit Line

November 21, 2001

Enron Closes On \$450M Secured Credit Line

HOUSTON -- **Enron** Co. (ENE) closed on the remaining \$450 million of a previously announced \$1 billion in secured credit lines and said it is in active discussions to restructure its debt to improve liquidity.

In a press release Wednesday, **Enron** said the \$450 million credit facility is secured by the assets of Enron's Northern Natural Gas Co.

A \$550 million credit facility, secured by the assets of Enron's Transwestern Pipeline Co., closed Nov. 16. The proceeds are being used to supplement short-term liquidity and to refinance maturing obligations.

The company said the maturity on its \$690 million note payable obligation will be extended to mid-December.

Dow Jones Corporate Filings Alert reported Monday that **Enron** is currently preparing a restructuring plan aimed at taking aggressive steps to rationalize the company's existing cost structure, accelerating the process of divesting noncore businesses and assets and restructuring scheduled maturities of debt and other obligations.

Enron's credit lines are from J.P. Morgan, the investment-banking arm of J.P. Morgan Chase & Co. (JPM), and Salomon Smith Barney, the investment-banking arm of Citigroup Inc. (C).

Enron also reaffirmed its commitment to the merger with Dynegy Inc. (DYN). On Nov. 9, **Enron** and Dynegy signed a definitive merger agreement that would give **Enron** shareholders 0.2685 share of a Dynegy share. The merger is expected to close by the end of the third quarter of 2002.

On Monday, **Enron** filed its Form 10-Q for the third quarter, which reflected a wider loss by 3 cents a share. The energy company previously reported a loss of \$618 million, or 84 cents a share, on revenue of \$47.6 billion for the third quarter ended Sept. 30.

-Stephen Lee; Dow Jones Newswires; 201-938-5400

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, November 23, 2001 12:13 PM
To: Nickoloff, Peter; Schultheiss, Heidilynne; Whaley, Jean
Subject: WSJ article on Enron accounting, Last two paragraphs mention Wendy Gramm

November 9, 2001

Heard on the Street

Enron's Accounting Violated Accepted Financial Practices

By JONATHAN WEIL

Staff Reporter of THE WALL STREET JOURNAL

What could Arthur Andersen have done to protect the investing public from Enron? Brushing up on a basic accounting textbook might have helped, some critics say.

Confirming investors' fears, the Houston energy trader Thursday filed a lengthy disclosure document with the Securities and Exchange Commission declaring that its financial statements going back to 1997 "should not be relied upon" and will have to be restated. Among other problems, Enron acknowledged overstating its net income by a total of \$586 million, or 20%. Enron's financial statements long have been widely assailed as indecipherable. Now, it turns out, they were just plain wrong.

But what is most striking about the latest disclosures is that they show Enron's misstatements weren't limited merely to judgment calls and gray areas for the green-eyeshade crowd to debate. Portions of Enron's accounting practices amounted to violations of elementary accounting principles, some accounting specialists say.

Citing client-confidentiality rules, an Andersen spokesman, David Tabolt, declines to comment on his firm's work for Enron, which on Friday agreed to be bought by crosstown rival Dynegy. He calls Enron's disavowal of its previous financial statements an "unfortunate situation" and says Andersen is cooperating with the SEC's Enron investigation and the special committee formed by Enron to investigate the company's accounting and disclosure practices.

[Go]Dynegy's Enron Deal Faces Uncertainties

Consider the primary reason for the \$1.2 billion reduction in shareholder equity that Enron revealed in mid-October, sparking much of the downdraft in the company's shares. At the time, Enron said the reduction came about because it had decided to unwind certain transactions with some limited partnerships with which it had done business. On Thursday, however, Enron acknowledged that the

original accounting for the transactions violated generally accepted accounting principles.

Starting in early 2000, the company said last week, Enron issued shares of its own common stock to four "special-purpose entities," in exchange for which it received a note receivable. Enron said it had increased both its note-receivable assets and shareholder equity, a move the company called "an accounting error" that it is correcting. Under GAAP, the payment a company receives when issuing stock only counts as equity if it is cash. As a result, Enron's 2000 audited financial statements overstated the company's notes-receivable assets and shareholder equity by \$172 million. And Enron's 2001 unaudited statements overstated them by \$828 million. The \$1 billion overstatement represents 8.5% of Enron's previously reported shareholder equity as of June 30.

"It is basic accounting that you don't record equity until you get cash, and a note doesn't count as cash," says Lynn Turner, a former chief accountant for the SEC. "The question that raises is: How did both partners and the manager on this audit miss this simple Accounting 101 rule?" Adds Douglas Carmichael, an accounting professor at Baruch College in New York: "Anyone that's an accountant looking at the entry should have known" it violated GAAP.

An Enron spokesman, Vance Meyer, says, "The accounting error was just that -- an error," explaining that, "We believed it was not material. However, it was, of course, corrected ... And we did make the correction with Andersen's concurrence." He says Andersen "performed limited quarterly reviews" of the company's unaudited financial statements and reviewed the entries that resulted in the shareholder-equity overstatements "to the extent they deemed necessary."

To some who follow the accounting world closely, this has a familiar ring to it. During the past few years, every Big Five auditor has been hit by multiple accounting debacles at high-profile clients. For Andersen, Enron joins a list including Waste Management Inc. and Sunbeam Corp. While the names of the clients may change, the issues remain largely the same.

For instance, Enron had reported net income of \$105 million for 1997, a figure that Enron last week said will be reduced to \$9 million in its upcoming restatement for that year. Enron said the reduction is mostly because of \$51 million in various unexplained "audit adjustments and reclassifications" that its auditors had proposed in 1997 but at the time had determined to be "immaterial." Cumulatively, those immaterial adjustments added up to nearly half of Enron's net income for 1997 and now will be included in the company's restatements.

That looks a lot like what happened at Sunbeam. According to the SEC's May settlement order with Sunbeam, Andersen auditors had routinely dismissed so many violations of GAAP as immaterial that they eventually piled up to produce significant distortions in Sunbeam's financial statements, making the barely solvent consumer-products maker look handsomely profitable. Sunbeam filed for Chapter 11 bankruptcy-court protection this past February. In May, the SEC filed a civil lawsuit against five former Sunbeam executives and the Andersen partner in charge of the company's audit, accusing them of engaging in a massive financial fraud; all six defendants have denied the SEC's allegations. Andersen itself wasn't named as a defendant and has said it believes the lawsuit against its partner was an unjustified action over questions of professional judgment.

Under GAAP, misstatements aren't immaterial simply because they fall beneath a numerical threshold, according to an SEC accounting bulletin. Under certain circumstances -- and it remains to be seen if they apply in the Enron case -- the SEC says intentional immaterial misstatements are unlawful. One reason is that when immaterial misstatements are combined with other misstatements, they can "render the financial statements taken as a whole to be materially misleading."

Enron, which paid Andersen \$25 million last year in audit fees and \$27 million for other services, is

one of Andersen's biggest clients. So far, Mr. Tabolt, the Andersen spokesman, says the SEC hasn't told Andersen it is a subject of the Enron probe.

Enron's disavowal of its previous financial statements also is a major embarrassment for the directors who sit on the Enron board's audit committee, which serves as the overseer of Enron's financial reporting, internal controls and compliance processes. Among the committee members is **Wendy Gramm**, a former chairman of the Commodity Futures Trading Commission and the wife of U.S. Sen. Phil Gramm (R., Texas). Ms. Gramm also was a member of the audit committee of IBP Inc., a meatpacking company that earlier this year became engulfed in an accounting debacle that prompted an SEC investigation and nearly derailed Tyson Foods' since-completed plan to buy the company.

Enron last week said its audit committee had been responsible for conducting annual reviews of the transactions between Enron and the partnerships run by former Chief Financial Officer Andrew S. Fastow. The company said its special committee is investigating "whether those controls and procedures were properly implemented." Through an Enron spokeswoman, Ms. Gramm declined to comment.

Write to Jonathan Weil at jonathan.weil@wsj.com <<mailto:jonathan.weil@wsj.com>>

Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, November 29, 2001 6:09 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark; Bieger, Peter; DeMarco, Edward; Dorsey, Karen; Elett, Martha; Ellis, Dina; Huffman, Lucy; Hughes, Gerry; McGivern, Tom; McInerney, Roberta; Salladin, Anne; Smith, Amy; Sutton, Gary; Tishuk, Brian
Subject: A Dow Jones Newswires Column: Enron's Derivatives Could Test Courts (discusses bankruptcy netting issues)

November 29, 2001	
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IN THE MONEY: Enron's Derivatives Could Test Courts

By CAROL S. REMOND and PHYLLIS PLITCH

A Dow Jones Newswires Column

NEW YORK -- Prepare for the largest test in bankruptcy history of safe harbors designed to protect the liquidity of the nations' financial system.

Enron Corp.'s (ENE) much-anticipated bankruptcy filing, if it indeed comes, is certain to be precedent setting. First, in terms of sheer magnitude, we're talking about \$62 billion in assets. But also because it's likely to involve hundreds, if not thousands, of counterparties intertwined with **Enron** in various financial and energy derivative transactions.

Unlike other creditors whose claims will be stayed under U.S. bankruptcy laws, those counterparties will vie to unwind their trades, may they be "power forwards" or credit derivative contracts, in order to find more worthy hedging partners.

Built in the bankruptcy code are exemptions for securities or commodities contracts. These safe harbors were developed over the years as a sort of security blanket for the vital hedging functions that these transactions provide.

"These special rules are designed to avoid a domino effect," said a bankruptcy lawyer, who like many contacted for this column, declined to be identified given the likelihood that he'll end up representing one or many parties involved in Enron's expected Chapter 11 filing.

Counterparties claiming redress through these exemptions should be able to net out their various derivative contracts with **Enron**, attempting to use whatever collateral was pledged under those transactions to quantify how much money they owe to or are owed by **Enron**. All of that is normally done on the side, without prior bankruptcy court approval.

The problem is that **Enron** will likely question attempts to unwind those trades and take issue with the manner in which its counterparties netted their exposure to the company, observers say.

Given the large number of parties involved and the magnitude of Enron's recent losses, the treatment of derivative contracts could be further complicated by the market's lack of understanding of just how much value is left in Enron's assets. That's an issue that will permeate the proceedings with all of Enron's stunned creditors. On top of its derivative exposure, **Enron** is on the hook for roughly \$13 billion in debt.

As part of its energy trading operations, **Enron** was a party to billions of dollars of derivative contracts designed

to enable the company and its trading partners to hedge, among other things, against rapidly fluctuating energy prices and foreign exchange volatility - stabilizing otherwise uncertain markets. By its own account, as of December 2000, **Enron** was involved in roughly \$20 billion of derivative contracts on which it owed its counterparties. More recent numbers aren't available.

Thoughts of an **Enron** bankruptcy jogged memories of past filings, such as the case of Drysdale Government Securities Inc., which involved public entities being left on the hook for millions of dollars in uncollateralized government repurchase agreements.

But bankruptcy laws have evolved significantly since the 1982 collapse of Drysdale sent shockwaves through the financial community and forced banks to pay out tens of millions of dollars to cover Drysdale's obligations to other government securities firms.

More recently, Orange County's 1994 bankruptcy following its derivatives debacle and the bitter dispute surrounding German's Metallgesellschaft Ag for breach of forward petroleum contracts suggests that acrimonious and lengthy litigations might be in the offing. In the latter case, many counterparties settled out of court and took "haircuts" after a judge ruled that independent petroleum marketers who entered into long-term hedging contracts as protection against escalating fuel prices could sue the metals and engineering conglomerate for breach of contract.

But the extent to which those cases provide any lessons for **Enron** and its derivative counterparties remains to be seen, experts said, depending on what sticky and complex issues might arise in potential court actions.

Meanwhile, although **Enron** has yet to file for bankruptcy, most of its derivative counterparties are likely already scrambling to exit their trades.

That's because Dynegy Inc.'s (DYN) decision Wednesday to abandon its plan to rescue **Enron** all but sealed the fate of the ailing Houston energy trader which has been hobbled by accounting irregularities and unquantified off-balance-sheet liabilities. **Enron** shares plummeted from about \$90 a share last summer to 36 cents Thursday.

Derivative contracts are built around master agreements developed by the International Swaps and Derivatives Association. As far as its power purchase deals go, **Enron** is said to have favored master agreements drafted by the Edison Electric Institute, which draws heavily on ISDA's blueprint.

Those master agreements include certain events under which a counterparty can terminate a transaction. Among those are failure to pay, failure to deliver and, of course, bankruptcy.

Whether counterparties will be able to claim exemption from the automatic stay that prevents anyone from terminating contracts with a company that filed for bankruptcy will hinge on the type of deals they're a party to and whether they meet certain statutory requirements. Although **Enron** and its lawyers are likely to nitpick the unwinding of each and every contract involving the company, legal experts noted that **Enron's** fondness for EEI agreements should help those entangled in power purchase agreements to liquidate their positions since these contracts treat all participants as forward contracts merchants. Such merchants are exempt from the stay stipulated by section 362A of the bankruptcy code.

Key to how well or poorly counterparties will make out now that **Enron's** business has been all but dried out, is how much if any collateral protects their transactions.

So far, it's unclear how much of **Enron's** derivative transactions were collateralized. But lawyers familiar with the matter said it was likely that a large amount of those contracts were not collateralized.

That's likely to be bad news for some counterparties. Because if they're owed money by **Enron** on their netted derivative exposure, they'll have to join other unsecured creditors, likely receiving little of their claims. The bonds and bank debt of **Enron** took a nose dive after Dynegy rescinded its merger offer, with trading levels

indicating that those mostly unsecured creditors thought they would recoup only 20% to 25% of the money loaned to **Enron**.

-By Carol S. Remond, 201-938-2074; Dow Jones Newswires; carol.remond@dowjones.com

(Phyllis Plitch contributed to this column.)

Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, November 29, 2001 6:13 PM
To: Bair, Shella; Bieger, Peter; Bitsberger, Timothy; DeMarco, Edward; Dorsey, Karen; Ellett, Martha; Ellis, Dina; Gabilondo, Jose; Gross, Jared; Huffman, Lucy; Hughes, Gerry; McGivern, Tom; McInerney, Roberta; Nickoloff, Peter; Roseboro, Brian; Salladin, Anne; Schultheiss, Heidilynne; Smith, Amy; Sutton, Gary; Tishuk, Brian; Berardi, Steve; Cetina, Jill; Eichner, Matthew; Hammer, Viva; Lori Sanatamarena (E-mail); Novey, Michael; Pietrangeli, Fred; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: IN THE MONEY-2:Collateral Key To Counterparties Recovery

November 29, 2001

IN THE MONEY-2:Collateral Key To Counterparties Recovery

Dow Jones Newswires

Thoughts of an **Enron** bankruptcy jogged memories of past filings, such as the case of Drysdale Government Securities Inc., which involved public entities being left on the hook for millions of dollars in uncollateralized government repurchase agreements.

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-By Carol S. Remond, 201-938-2074; Dow Jones Newswires; carol.remond@dowjones.com

(Phyllis Plitch contributed to this column.)

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Sent: Thursday, November 29, 2001 6:16 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DOW JONES NEWSWIRES: Bank Regulators See No Systemic Risk From Enron Collapse

November 29, 2001

Bank Regulators See No Systemic Risk From Enron Collapse

By REBECCA CHRISTIE

OF DOW JONES NEWSWIRES

WASHINGTON -- U.S. bank regulators say the financial collapse of energy giant **Enron** should have little lasting impact on the banking industry.

None of the four major bank regulators expressed concern Thursday that Enron's meltdown would snowball into systemic problems.

"It's something we are looking at. We have not identified anything that would concern us a great deal," said Mark Schmidt, assistant director of supervision for the Federal Deposit Insurance Corporation, of possible ripple effects from Enron's difficulties. "Obviously the **Enron** situation is something we and other regulators are following closely."

Bank regulators generally don't comment on specific banks. Schmidt said the banks the FDIC has been contacted haven't expressed undue concern about Enron's crisis. Schmidt said regulations and internal guidelines generally limit bank exposure to any one company and even any one industry.

"We are not aware of any individual bank that house outsized direct exposure to **Enron**," Schmidt said. "Obviously, there will be some losses suffered."

Citigroup was one of the banks with the closest ties to Enron's failed deal with Dynegy Inc., which scotched its buyout bid Wednesday as financial ratings agencies lowered **Enron** to junk status. Citigroup is regulated by the Office of the Comptroller of the Currency, which had no specific comment on that bank but expressed confidence in the banking industry's ability to weather the storm.

"The OCC continually monitors market conditions and banks are always in the process of taking profits and losses," said a spokesman for the Office of the Comptroller of the Currency. "The OCC is confident that any losses due to market conditions can be accommodated with minimum impact."

Another major would-be dealmaker, JP Morgan Chase, is regulated by the Federal Reserve. The Fed had no specific comment on banks' exposure to **Enron**, but a spokesman for the Federal Reserve

Bank of New York noted Wednesday that "the markets are functioning normally."

The Office of Thrift Supervision, whose members generally lend to homebuyers and smaller businesses, also was not expecting a major ripple effect.

"It looks like the **Enron** deal would have no broad-range effect on the thrift industry," said Office of Thrift Supervision spokesman Sam Eskanazi, who noted that thrifts tend to lend to smaller businesses. Still, he said OTS was "monitoring the situation carefully."

-By Rebecca Christie; Dow Jones Newswires; 202 862 9249; rebecca.christie@dowjones.com

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From: Carleton, Norman
Sent: Thursday, November 29, 2001 6:19 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark; Bieger, Peter; DeMarco, Edward; Dorsey, Karen; Ellett, Martha; Ellis, Dina; Huffman, Lucy; Hughes, Gerry; McGivern, Tom; McInerney, Roberta; Salladin, Anne;
Subject: Enron's Financial Woes Ripple Out Across Asia

November 30, 2001

Major Business News

Enron's Financial Woes Ripple Out Across Asia

By **JASON BOOTH, HENNY SENDER and RICHARD B. SCHMITT**

Staff Reporters of THE WALL STREET JOURNAL

The sudden deep financial troubles of U.S. energy giant **Enron Corp.** sent ripples of concern across Asia, damaging investments in Japan and potentially undermining businesses in South Korea and Australia.

The uncertainty for Asia is likely just beginning. If **Enron** files for protection under Chapter 11 of the federal Bankruptcy Code in the U.S., as many investors and financial experts now expect, it is likely to be one of the messiest, most complex bankruptcy cases ever, lawyers say. That is because of the multifaceted nature of Enron's once highflying operations, which combined a global energy business with a massive financial-trading operation involving tens of billions of dollars in complex contracts. A filing by **Enron**, with about \$13 billion in debt, would rank among the largest bankruptcy filings ever. **Enron** has about 800 trading partners or creditors.

The scale of the **Enron** collapse is huge, experts say. "There is nothing to compare it to," said Edward Tillinghast, a bankruptcy specialist with Coudert Brothers in New York. "The business was so large. There were so many different kinds of operating entities under the **Enron** umbrella."

On Wednesday, as the last-ditch merger with Dynegy Inc. unraveled, the company's credit was downgraded to "junk" status by rating agency Standard & Poor's Corp. The stock market, signaling that a bankruptcy filing is expected, hammered **Enron** stock, which was halted for a time on Wednesday, and knocked lower some of its financial backers' shares. **Enron** shares closed at 4 p.m. in New York Stock Exchange composite trading at 61 cents, down \$3.50, or 85%. Thursday morning in New York, **Enron** was trading down 33%, or 20 cents, to 41 cents. On Wednesday, **Enron** bonds also fell sharply, dropping to 50 cents on the dollar from around 55 cents, reflecting concerns over

how much creditors might receive if the company does seek bankruptcy-court protection.

Enron spokeswoman Karen Denne said the company is exploring its options and wouldn't comment on whether it has retained bankruptcy counsel.

The fallout in Asia was felt immediately on Thursday. The biggest news was in Sydney, where **Enron** Australia said it was suspending operations pending further developments regarding its U.S. parent. "We are now waiting for clarification about Enron's situation globally and will advise the local market once we have received that advice," legal counsel Rob McGrory said.

The announcement followed a warning by Standard & Poor's about counterparty exposure in the Australian electricity market, citing the overnight downgrade of **Enron**. "The recent developments with **Enron** serve as a further example of the credit risks faced by energy market participants as they seek to manage their market risks in Australia's volatile power market," said Laurie Conheady, an associate director at Standard & Poor's.

Similarly, Enron's presence in South Korea appears to be nearing an end. According to officials at SK Corp., **Enron** plans to sell its 50% stake in joint venture energy distribution firm SK-Enron Co. SK-Enron was formed in 1999, and controls about 25% of South Korea's natural-gas market, according to the firm's Web site.

Analysts said that **Enron** had offered to sell its stake to SK Corp., yet the Korean partner said it has no plans to buy the shares. "We already hold 50% ... we don't need the rest," said a company spokesman, Daniel Youn.

Enron was also considered a potential buyer of power generation assets from South Korean government-controlled Korea Electric Power Corp. Kepco is looking to sell assets as part of a wider privatization drive.

Pressure elsewhere in the region was felt primarily in the financial markets. In Tokyo, the value of money management funds Nikko Asset Management Co., UFJ Partners Asset Management Co., Japan Investment Trust Management Co. and Sumisei Global Investment Trust Management Co., fell due to their exposure to **Enron** debt, which amounted to about 40 billion yen (\$324.9 million). **Enron** news also sparked volatility in the copper and U.S. dollar market, according to traders.

Other financial backers of **Enron** were negatively effected as well. J.P. Morgan Chase and Citigroup, which have invested hundreds of millions of dollars in hopes of keeping the Enron-Dynegy deal alive, saw their stocks fall on Wednesday trading in the U.S. On Thursday morning Citigroup shares posted slight gains, rising 19 cents to \$47.99, while J.P. Morgan Chase shares were flat at \$37.50. J.P. Morgan Chase said in a statement it has about \$500 million of unsecured exposure to **Enron** entities, including loans, letters of credit and derivatives. It said it also has secured exposures, including \$400 million in loans secured by **Enron** pipelines.

Besides banks and bondholders, dozens of companies, municipalities and utilities in the U.S. that had signed multiyear power contracts with **Enron** may be left in the lurch. Over the years, the likes of retailer J.C. Penney Co., and shopping-mall company Simon Property Group signed on with **Enron**, as it undercut local utilities in newly deregulated markets.

-- Rebecca Smith and Robin Sidel contributed to this article.

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From: Carleton, Norman
Sent: Friday, November 30, 2001 3:44 PM
To: Salladin, Anne; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamorenna (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: Enron's Global Reach

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Enron's Global Reach



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North America

Purchases, markets and delivers natural gas, electricity and other commodities, and runs a broad range of price, risk management and financing services.

Latin America

Has interests in natural gas, crude oil and products pipelines and a transmission system for the distribution of electricity.

Europe

Delivers physical commodities, price risk management and financing services; operates several power plants.

Asia/Pacific

Owns interests in electricity-generating plants and distribution of natural gas liquids; conducts commodity risk management and finance services.

GLOBAL SPRAWL

A look at where Enron's major assets, operations and interests lie:



Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, November 30, 2001 3:49 PM
To: Nickoloff, Peter; Schultheiss, Heidilynne; Eichner, Matthew
Subject: Article on Enron and Arthur Andersen

November 30, 2001

SEC Starts Probe of Enron Audits Conducted by Arthur Andersen

By JONATHAN WEIL

Staff Reporter of THE WALL STREET JOURNAL

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The Securities and Exchange Commission's investigation of energy trader Enron Corp. has now expanded to include the actions of the company's auditor, Arthur Andersen LLP.

The SEC has subpoenaed records from Arthur Andersen as part of the agency's formal investigation into Enron's accounting and financial-disclosure practices.

That Andersen's actions would become a focus of the SEC's investigation isn't surprising, accounting and securities-law specialists said. This month, Enron disavowed its financial statements going back to 1997, and Enron's market value has plunged more than \$75 billion since it peaked last year. However, until Thursday, Andersen's public position was that the SEC hadn't told the firm it is a subject of its investigation into Enron.

Given the subpoenas, the delivery of which Andersen spokesman David Tabolt confirmed in an interview Thursday, the Big Five accounting firm now has concluded that the "work of our engagement team is a subject of the SEC investigation," Mr. Tabolt said. The subpoenas cover a litany of documents, mainly working papers generated by the Andersen team of auditors assigned to Enron, he said.

CNBC Dow Jones Business Video

Media <http://www.cnbc.com/djbusiness/November_01/112901/asx/1129watr.asx>

Lost Credibility:

Dynegy CEO Chuck Watson says Dynegy was given Enron's third-quarter financial report only three hours before it was filed, and was surprised by Enron's disclosures.

Learn About CNBC/Dow Jones Business Video <<http://www.cnbc.com/djbusiness/>>

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However, he declined to be more specific about what information the SEC sought. He also declined to say when the subpoenas were issued or whether SEC officials had begun conducting interviews of Andersen personnel.

An SEC spokesman declined to comment.

Andersen likely will face questions on a host of fronts. Among them are whether Andersen should have required Enron to better explain its dealings with several partnerships operated by former Enron officers before agreeing to bless the company's financial statements. Securities-law specialists said Andersen likely will face questions about why it agreed to sign off on Enron's decision not to consolidate several off-balance-sheet financial vehicles whose debts ultimately were Enron's responsibility.

The firm likely will also face questions about whether it was unduly influenced by the unusually large fees Enron paid Andersen over the years. In 2000, Enron paid Andersen \$52 million, including \$27 million for consulting services, making Enron Andersen's second-largest U.S. client.

Further, some of Enron's accounting violations appear to have amounted to basic violations of generally accepted accounting principles. Enron, for example, earlier this month acknowledged improperly boosting its shareholder equity by \$1.2 billion by swapping shares of its own stock for a note receivable from a limited partnership tied to one of its former officers. Additionally, Enron boosted its earnings over the years by declining to make certain audit adjustments that Andersen had proposed. But at the time, Andersen determined those adjustments to be "immaterial." In 1997, for instance, those adjustments added up to nearly half of Enron's net income. And other questions about Andersen's level of responsibility could well arise as investigators dig deeper into the case.

[\[Go\]See full coverage of the rise and fall of Enron](#)

Alan Bromberg, a securities-law professor at Southern Methodist University in Dallas, said Andersen could face stiffer-than-usual sanctions from the SEC, depending on what investigators find, because of the firm's recent brushes with the SEC over audit failures at Sunbeam Corp. and Waste Management Inc. Among the possible sanctions the SEC may consider, he said, are prohibitions against Andersen taking on new audit clients for a period of time and prohibitions on certain firm partners from practicing accountancy before the SEC.

Mr. Tabolt said Andersen will cooperate with all government investigations, but declined to comment on them in detail.

Andersen's role in the Enron probe also could present sticky issues for SEC Chairman Harvey Pitt, whose former law-firm clients include Andersen and the other Big Five accounting firms. In a June letter to the SEC's ethics officer, Mr. Pitt said he wouldn't take part in decisions by the commission related to his former law-firm clients for a year.

An SEC spokesman declined to comment Thursday when asked if Mr. Pitt will recuse himself from the Enron probe.

In an interview earlier this month, the SEC's general counsel, David Becker, said commission officials are "not going to comment on a commissioner's choice in any particular case." But he added: "I do think the public is safe in assuming that the chairman, like all the other commissioners, is quite aware of his ethical obligations and will behave consistently with them."

Separately, U.S. Rep. Billy Tauzin (R-La.), chairman of the House Commerce Committee, Thursday asked his committee staff members to begin investigating Enron's collapse. Mr. Tauzin, whose committee has oversight over accounting standards and practices, said he expects to hold hearings on the matter in the near future, focusing in large measure on Enron's financial misstatements. Mr. Tabolt said Andersen will cooperate with the committee's investigation.

Accounting for Its Accounting

With the broadening of the Securities and Exchange Commission probe into Enron to include the work of auditors Arthur Andersen, regulators would be likely to ask the following sorts of questions, according to some accounting professors:

- Were financial-statement disclosures regarding Enron's transactions with company insiders too opaque to understand?
- Were Andersen auditors aware that certain off-balance-sheet partnerships should have been consolidated into Enron's balance sheet, as they were in the company's recent restatement?
- Did Andersen auditors knowingly sign off on some "immaterial" accounting violations, ignoring that they collectively distorted Enron's results?

Congressional scrutiny won't be limited to Andersen and Enron either. In a statement Thursday, the House Commerce Committee's leading Democrat, John Dingell of Michigan, said his focus will also turn to, among other groups, the Financial Accounting Standards Board, adding that "our accounting and auditing system and its oversight are seriously broken and need immediate reform."

Critics of Enron have long complained that Enron was able to aggressively boost its earnings through loopholes in the board's current standards. For instance, the board has been working on a project for more than a decade to tighten the rules governing when companies must consolidate certain off-balance sheet "special purpose entities" like the kinds utilized by Enron that kept billions of dollars of debt off its balance sheet. And the board says it still isn't close to finishing the project.

Also, over the past two years, as Enron emerged as a highflying symbol of the New Economy, many investors didn't realize that much of its reported profits were noncash unrealized gains. Those gains depended on a multitude of undisclosed assumptions about future market factors that were subject to later revision, such as changes in electricity and natural-gas prices.

At the heart of those gains is an accounting technique that allows energy traders to include as current earnings those profits they expect to realize from energy-related contracts and other derivative instruments in future periods, sometimes stretching over more than 20 years, even in situations where markets aren't well established and quoted prices aren't readily available. To date, the accounting-standards board has given energy traders almost boundless latitude to value their energy contracts as they see fit.

Analysts and investors already have begun calling for greater disclosure by other energy traders of the assumptions underlying their noncash gains. In a research note Thursday, for instance, Goldman Sachs analyst David Fleischer said, "Investors are likely to be asking much more difficult questions and to be dissatisfied with less than full answers and anything but radically enhanced disclosures."

At the accounting-standards board, research director Tim Lucas declined to comment on Enron

specifically. But he said he expects the board will face increased calls to revise its standards for consolidations of affiliated entities and its disclosure requirements for companies reporting unrealized gains from derivative contracts.

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Subject: DJ: Enron Collapse Could Weigh Heavy On Some Insurers

November 30, 2001

Enron Collapse Could Weigh Heavy On Some Insurers

By CHAD BRAY

OF DOW JONES NEWSWIRES

NEW YORK -- The insurance industry didn't need **Enron** Corp.'s (ENE) problems, particularly when it comes to reinsurance prices.

Primary insurers could be on the hook for as much as \$2 billion in claims against directors and officers policies, surety bonds and financial guarantees related to the Houston energy trading firm, which, among its options, is considering seeking Chapter 11 bankruptcy protection. Some insurers also will likely take a hit in their investment portfolios if **Enron** defaults on its bond payments.

The loss would be material, but not devastating for the industry. However, amid the backdrop of the World Trade Center disaster, Enron's impact could pressure some firms going forward, particularly if most of their **Enron** risk was ceded to reinsurers. "This event is likely to exacerbate the (reinsurance) capacity shortfall in the market that already exists, making 2002 one of the more, if not the most, powerful pricing years in recent history," said Alice Schroeder, a Morgan Stanley insurance analyst.

Reinsurance prices were rising prior to the Sept. 11 terrorist attacks. Rates are expected to rise dramatically in light of the events as reinsurers get a handle on how to insure this new risk in the U.S.

Aviation rates, for example, have already climbed 200% to 300% in some cases. Reinsurers also are willing to take on less risk, forcing primary insurers to keep more of the coverage or write policies offering less coverage.

Chubb Corp. (CB), a Warren, N.J., insurer, said it was reviewing its surety bonds related to **Enron** and could have a maximum net pretax exposure under outstanding surety bonds of about \$220 million. The firm said its after-tax exposure is \$143 million, or 82 cents a share.

A company takes out a surety bond in the event it can't fulfill a contractual obligation. Typically, surety bonds would pay out any monetary guarantees if a company was unable do so. Surety bonds are often used to improve a firm's credit rating.

The insurer was unable to estimate the actual amount, if any, that they may be required to pay or the

timing of those payments because of contingencies, including the actions of others, possible judicial rulings or the amounts that Chubb may recover under surety bond documents. No claims have yet been filed under the surety bonds.

Jay Cohen, a Merrill Lynch analyst, said Chubb's surety bond obligations in regards to **Enron** generally guaranteed the delivery of natural gas to energy producers, such as utilities. Each bond could have different defined events that would trigger a claim, such as a bankruptcy, Cohen said.

"The **Enron** loss will likely be a very sizable one in the surety line, a line that was not particularly effected by the Trade Center attack," Cohen said. "The loss will likely exceed \$1 billion and we note that the industry wrote surety premiums totaling \$3.5 billion in 2000. We would expect this loss to have an effect on insurers' risk appetite pertaining to surety obligations."

Cohen said Chubb likely has reinsurance for its losses and that its gross exposure is "above the \$220 million maximum net exposure."

Ron Frank, a Salomon Smith Barney analyst, said, while the **Enron** situation is clearly "unusual," the loss should be viewed relative to Chubb's overall financial condition, which is quite solid. He said Chubb's historical profitability in surety is "very good even including **Enron**."

Frank noted the Chubb announcement didn't address any other exposure to **Enron**, such as directors and officers liability. "Management did comment to us that if they saw another exposure material to earnings per share, it would have been released," Frank said. "We infer from this that reinsurance and reserves will meaningfully mitigate such exposures."

Large surety writers include St. Paul Cos. (SPC), American International Group (AIG), CNA Financial (CNA), Act Ltd. (ACE), Safeco Corp. (SAFC) and the Travelers unit of Citigroup Inc. (C). However, not all large writers of surety obligations necessarily have an exposure to **Enron**.

At the same time, a major **Enron** loss could inhibit some traditional property-casualty insurers from writing financial guarantee-related risk in the future, said Schroeder, the Morgan Stanley analyst.

Schroeder noted that could be a positive for traditional financial guarantors in terms of less competition, but could also be a concern.

For example, Ambac Financial Group Inc. (ABK) and MBIA Inc. (MBI), both traditional financial guarantors, have been able to "wrap" lower levels of risk on certain collateralized debt obligation deals with traditional P&C insurers, while taking the higher, or less risk prone, layers for themselves. Being conservative in nature, they might not be willing to take on the more risky layers in the future.

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From: Carleton, Norman
Sent: Friday, November 30, 2001 3:58 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: Enron Still Considering Options, Sources Say

November 30, 2001

Enron Still Considering Options, Sources Say

Dow Jones Newswires

By Christina Cheddar and Janet Whitman
Of DOW JONES NEWSWIRES

NEW YORK – **Enron Corp.** (ENE) is still considering all of its options, including the likelihood of filing for bankruptcy protection under Chapter 11, people close to the matter said.

Such a decision, however, will not come until next week, these people said.

Some **Enron** employees are being told not to expect any action over the weekend, these people said.

Although the people familiar with the situation insist an all-out liquidation - known as a Chapter 7 filing - isn't in the cards, some industry observers continue to speculate that the beleaguered company may be forced to go that route.

With its energy trading business crippled on Wednesday by the downgrade of its debt to junk status and a buyout by Dynegy Inc. (DYN) nixed later that day, Enron's fortunes have been in a downward spiral.

Enron's once high-flying stock has also nose-dived, swapping hands recently at 30 cents a share. The stock had traded above \$90 a share last year, and, all told, equity shareholders have lost over \$60 billion. Meanwhile, Enron's outstanding bonds trade at prices of around 15 cents on the dollar.

The weakness in Enron's bonds - down from the upper 50-cent range before Wednesday's developments - suggests bondholders don't expect much if any recovery on their investments.

There is little doubt that any proceedings will be complex and time-consuming, given the nearly \$62 billion in assets on Enron's balance sheet (as of its last quarterly financial report). Also, the court would have to wade through and untangle many items not listed on its balance sheet. Those financing vehicles are what sparked the company's troubles last month.

Enron's liabilities are still a matter of debate. The company has an estimated \$13 billion in debt on its

balance sheet, and a further \$7 billion in financings off the balance sheet. However, there may be other obligations lurking in connection with its investment partnerships.

Then, too, what kind of company **Enron** would be under a bankruptcy reorganization is also uncertain.

Since the debt downgrade, Enron's trading business appears damaged beyond repair. Without a viable credit rating, the company no longer has access to the reams of cash it needs to run that business.

Underscoring Enron's woes, the company told some of its trading partners on Friday that it will default on some of its deliveries of wholesale electricity under contract for Sunday and Monday, people familiar with the situation said.

Some observers had expected **Enron** to file for bankruptcy protection as early as this week. But the people close to the situation said the complex business structure is slowing the process. And where the company would file is also a question: The Houston-based company could file where it's headquartered, but it's also incorporated in Oregon, and many companies look to the favorable courts of Delaware whenever possible.

Enron hired restructuring and bankruptcy specialist Blackstone Group late last week to advise it on corporate matters and to help restructure its debt.

The company also is being advised by law firm Weil Gotshal & Manges, a bankruptcy specialist.

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Subject: Bloomberg: Enron Fires U.K. Workers, Plans Bankruptcy Soon (Update1)

Enron Fires U.K. Workers, Plans Bankruptcy Soon (Update1)

By Mark Lake

New York, Nov. 30 (Bloomberg) -- Enron Corp. fired 1,100 employees in the U.K. as the energy trader sought to line up financing for the largest U.S. bankruptcy reorganization.

Enron's bankers, led by J.P. Morgan Chase & Co. and Salomon Smith Barney Inc., sought to arrange more than \$1 billion of loans to help Enron trade while in bankruptcy, said people familiar with the situation. The debtor-in-possession financing may be secured in part by \$1.8 billion in proceeds Enron expects to receive by selling its Portland General Electric Co. unit.

Enron is also considering using its Northern Natural Gas Co. pipeline, which analysts estimate is worth \$2.7 billion, as collateral for new loans. Dynegy Inc. said it would seek to block such a move by exercising an option to purchase the pipelines.

"This whole thing is going to be in the courts," said Kathleen Vuchetich, who helps manage \$1.4 billion in assets. The firm owns Dynegy shares in the Strong American Utilities fund that Vuchetich helps run.

Enron will have 250 U.K. workers after the dismissals, according to a statement by PricewaterhouseCoopers, which is overseeing the company's British operations. Enron has 6,800 workers in Europe and 21,000 total.

More firings are likely in the U.S. after its \$23 billion acquisition by Dynegy collapsed earlier this week. That failure, and a credit-rating downgrade to junk, left the company short of cash needed to pay its \$15 billion of debt.

Enron, with less than \$2 billion in cash as of last week, needs to pay \$690 million to lenders by mid-December and is responsible for another \$3.9 billion in debt owed by affiliated partnerships.

Pipeline Debate

Dynegy said it plans to take over Enron's Northern Natural Gas pipeline on Dec. 12, even if Enron files for bankruptcy. Dynegy invested \$1.5 billion in Enron as part of the merger plan, giving it preferred stock in Northern Natural Gas. Dynegy backed out of the takeover Wednesday.

Enron likely will go to court to argue that Dynegy didn't have the right to end the merger, so it shouldn't get the pipeline, New York bankruptcy lawyer Robert Christmas said. Enron needs collateral for loans to stay in business.

Enron pledged assets of Northern Natural Gas and Transwestern Pipeline as collateral for \$1 billion in loans from J.P. Morgan and Salomon this month. The banks may not back Enron's claim, as they are more likely to be repaid by Dynegy, said Fahnestock & Co. analyst Fadel Gheit.

"I expect to see Enron, J.P. Morgan, Citibank and Dynegy all in court fighting over who owns the pipeline," said Jon Kyle Cartwright, a fixed-income senior analyst at Raymond James & Associates. "At this point we put our chips on Dynegy. We suspect they had the time and expertise to perfect their purchase."

Biggest Pipeline

Dynegy will assume \$950 million of Northern Natural debt with the purchase. Enron can buy the pipeline back if it pays Dynegy \$1.5 billion, plus interest, within 180 days of the merger's collapse, Dynegy Chairman Chuck Watson said

yesterday. Watson said he would rather get the pipeline than recoup the investment.

Northern Natural Gas, the biggest of Enron's four gas pipelines, stretches from the Permian Basin in Texas to the Great Lakes. Dynegy's right to buy it "is not dependent on Enron's agreement to our right to terminate the merger," Dynegy Chief Financial Officer Rob Doty said today in a statement.

Shares of Enron fell 9 cents to 27 cents in early afternoon trading. They had fallen 99 percent since mid-October. Dynegy fell \$2.34, or 7 percent, to \$31.31. Enron's unsecured bonds were bid at 18 cents on the dollar this morning, down about 3 cents from yesterday, traders said.

Enron, which got its start as a natural-gas pipeline company, was transformed in the past decade into the biggest competitor in the business of trading energy. As part of the company's strategy, it shifted its focus from developing assets such as pipelines and power plants to developing markets for commodities. As a result, Enron has few assets it can use as collateral for loans.

On the Brink

Enron has been unable to raise enough cash to ensure it can pay debts and is having trouble financing daily operations. Dynegy's decision to back out of the acquisition left Enron on the brink of bankruptcy.

Northern Natural Gas can't take any action, including filing for bankruptcy, without the consent of Dynegy as a preferred stockholder, Dynegy said in the statement.

"From what I understand, Dynegy has as strong a legal claim to the pipeline as they can have," said Commerzbank Securities analyst Andre Meade. "They structured the deal in a way, with bankruptcy as a likely scenario, to have good legal standing."

Meade rates Enron "sell" and Dynegy "buy" and doesn't own shares of either company. He values Northern Natural at \$2.7 billion, more than the \$2.47 billion that Dynegy is paying, including debt.

"Dynegy paid fair market value (for the pipeline), and they have the law and the facts on their side," said John Olson, research director for Sanders, Morris, Harris Group Inc., a Houston financial-services firm.

Watson said yesterday he hopes that Northern Natural employees won't quit after the takeover. Enron and Dynegy are both based in Houston.

"Dynegy has contacted Enron to begin a transition of the pipeline's management and expect Enron's full cooperation," Doty said today.

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, November 30, 2001 7:19 PM
To: Salladin, Anne; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamorenna (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: Dow Jones Newswires: Enron To File For Bankruptcy Mon. Or Tues -Report

November 30, 2001 [WSJ.com]

Enron To File For Bankruptcy Mon. Or Tues -Report

Dow Jones Newswires

NEW YORK -- **Enron** Corp. (ENE) will file for bankruptcy protection on Monday or Tuesday, according to a report on CNBC that cited an **Enron** employee as its source.

According to CNBC, the employee was told the news by his unit vice president.

The **Enron** employee also said the Houston energy trading company would lay off 95% of the company's staff at that time, and provide employees two weeks severance for each year of service, according to the television network.

Enron wasn't immediately available for comment.

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From: Carleton, Norman
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To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidllyne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: An Energy Giant Falls: Recap Of Dow Jones' Enron Coverage

December 3, 2001

An Energy Giant Falls: Recap Of Dow Jones' Enron Coverage

Dow Jones Newswires

Enron Corp. (ENE) ended days of speculation and filed for Chapter 11 protection from creditors Sunday, the biggest such filing in U.S. history. Simultaneously, the Houston-based energy firm sued Dynegy Inc. (DYN) for "not less than \$10 billion," accusing it of wrongfully terminating a merger deal last week that the two firms had reached just two weeks earlier.

Dow Jones Newswires coverage of this fast-moving story can be found under the stock symbol ENE.

Dynegy CEO Says Enron Lawsuit Is "Without Merit"

Dynegy said Enron's lawsuit against it "has no merit whatsoever in law or in fact," calling the suit "one more example of Enron's failure to take responsibility for its demise."

Private Illinois Firm Claims To Make Tender Offer For Enron

Standard Power & Light Inc., a privately held company that buys and develops power plants, plans to hold a tender offer to acquire at least a majority stake in bankrupt Enron. **Standard Power** said it expects the tender offering price to be less than \$1 a share, depending on several issues, including the final result of Enron's failed merger with Dynegy Inc.

NYSE Reviews Enron's Continued Listing Status, Cites Bankruptcy Filing

The New York Stock Exchange is reviewing Enron's continued listing status. The Big Board plans to continue trading Enron's stock, as the company still meets NYSE quantitative listing standards, but the exchange isn't limited by those standards and can seek a stock delisting if it believes continued listing is "not advisable."

Enron Corp.'s DIP Financing Expected Monday

Enron expects to receive debtor-in-possession financing as early as Monday, according to a person familiar with the matter. Enron said it is in "active discussions and expects to complete these discussions shortly."

Enron Bankruptcy Wouldn't Push S&P To Cut Energy Co Ratings

The bankruptcy filing by Enron is unlikely to trigger downgrades of debt issued by U.S. oil and gas explorers and producers rated by Standard & Poor's, said S&P analyst Bruce Schwartz.

Enron Likely Pullout Won't Hurt Japan Energy Deregulation

Japanese energy deregulation may be about to lose its single biggest advocate, as Enron decides whether or not to fold its businesses there in the wake of its bankruptcy filing in New York Sunday.

Enron Collapse Could Weigh Heavy On Some Insurers

The insurance industry didn't need Enron Corp.'s (ENE) problems, particularly when it comes to reinsurance prices. Primary insurers could be on the hook for as much as \$2 billion in claims. Some insurers also will likely take a hit in their investment portfolios if Enron defaults on its bond payments. The loss would be material but not devastating for the industry.

Enron Woes May Pressure Pricing For Broadband Services

Problems at Enron, which has a nationwide broadband fiber-optic network, could eventually translate to greater downward pressure on pricing of broadband telecommunications services, according to some experts.

Stories about companies with exposure to Enron:

- Barclays Has \$126M 'Trade Debt' In Enron Filing - WSJ
- Chase Manhattan Has \$113M 'Trade Debt' With Enron - WSJ
- John Hancock Financial Confirms Enron Exposure At \$320M
- Royal & Sun Signals It Doesn't Have Large Enron Exposure
- XTO Energy Sees Minimal Exposure To Enron
- TXU Says Potential Exposure To Enron Less Than \$20M
- UtiliCorp Says It has Limited Enron Exposure
- Genesis Energy Says Potential Net Enron Exposure Is About \$21M
- Covanta Energy Sees 'No Exposure' To Enron
- Constellation Energy: No Direct Credit Exposure to Enron
- Southern Union Co Has No Material Fincl Deals With Enron
- Spinnaker Exploration Announces Enron Exposure \$2.2M
- International Power's Enron Exposure Is Less Than GBP2

Min

- U.K. Prudential Has Virtually No Exposure To Enron

Other stories related to Enron:

- Fitch Lowers Enron Ratings To 'D' >ENE
- IntercontinentalExchange To Enter UK Gas, Power Markets

By End of Dec.

- Dutch Tennet Excludes Enron From Import Capacity Auctions
- Amsterdam Power Exchange: Enron's Departure Not Affecting

Spot Power Trade

- Enron's India Unit Reviewing Dispute With Sole Buyer
- Enron Considering "All Possible Options" For Japanese Ops
- Enron Australia Appoints Administrator, Seeks Buyer
- Creditors Holding 20 Largest Unsecured Enron Corp. Claims
- Largest Unsecured Enron Broadband Services Inc. Claims
- Ten Largest Unsecured Enron Energy Services Inc. Claims
- Largest Unsecured Enron Power Marketing Inc. Claims
- Largest Unsecured Enron North America Corp. Claims

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From: Carleton, Norman
Sent: Monday, December 03, 2001 12:07 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidi; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: WSJ: Credit-Derivatives Market Faces Stiff Test After Collapse of Enron

December 3, 2001

Credit-Derivatives Market Faces Stiff Test After Collapse of Enron

By **HENNY SENDER**

Staff Reporter of THE WALL STREET JOURNAL

The collapse of Enron Corp. casts a spotlight on a little-known but highly complex market in credit derivatives, a market that has swelled from almost nothing five years ago to a face value of more than \$1 trillion today, according to estimates from Goldman, Sachs & Co.

Now, as Enron files for protection under Chapter 11 of the Bankruptcy Code, the credit-derivatives market faces the biggest test of its young life. The way the market functions over the next few weeks will have significant consequences in determining who will bear the potentially massive losses, how widely those losses will be distributed and whether any one institution took overly risky bets by having significant concentrations of unhedged exposure to Enron. Whether Enron's collapse takes any other institutions down with it will probably be decided in this marketplace.

Enron was a big presence in this market. For one thing, since Enron had a voracious appetite for capital and raised so much debt -- \$13 billion in bonds and loans on the parent's balance sheet alone, and much more off -- numerous financial institutions needed to hedge their Enron bonds and loans. And then, because Enron was such a huge dealer itself, especially in longer-dated, thinly traded securities where few others made markets as boldly, it became Wall Street's counterparty on everything from oil to weather to credit derivatives.

"Enron showed up everywhere," says the head of the credit-derivatives desk at one major bank in New York. "Everyone had exposure to it."

[\[Go\] See full coverage of the rise and fall of Enron](#)

In recent weeks, before its debt crumbled to a small fraction of its face value on news of the company's loss of its investment-grade status, hundreds of Enron's lenders, bondholders and counterparties sought to buy protection against possible default by Enron through one significant segment of the credit-derivatives market, called credit-default swaps (a complicated name for what was essentially insurance in case Enron defaulted). Indeed, the demand for protection against a default by Enron was so great that the price was far higher than it should have been, given its then-

high credit rating. At the same time, it was tempting for many parties to offer that insurance. The business seemed an easy way to earn fees; only if Enron defaulted would the seller have to make any payments. And, given Enron's longstanding investment-grade status and \$62 billion in assets, default seemed a remote possibility.

There are other ways in which Enron cast a huge shadow in this market. For example, Enron's own debt was a big piece of the many packages of securities others assembled and sold to investors. Now, the credit of the whole package becomes weaker. Moreover, Enron packaged securities itself, through special-purpose vehicles on which it provided guarantees, as part of its ambitions to be a financial powerhouse.

To be sure, the market has already had some experience with defaults. Three years ago, there was the Russian debt crisis; this year the market has already absorbed such shocks as the Chapter 11 filings of Pacific Gas & Electric Co. and financial-services company Consec Inc. and the collapse of Swissair Group. But the three combined don't begin to approach the magnitude of an Enron.

Part of the problem is the uncertainty; nobody yet knows the full scale of Enron's involvement in the market or how much insurance was written against a default by Enron. Because credit derivatives aren't exchange-traded, and the deals are off-balance-sheet, the market is relatively opaque. Standard & Poor's put out an analysis Friday suggesting various Enron exposures in the credit-derivatives market could amount to more than \$6 billion. But that number just reflects the securities that happen to have been rated; Nik Khakee, who heads S&P's structured Finance Derivatives group, concedes that those securities are a small part of the total. "If the recovery value is zero, there will be huge losses for investors," Mr. Khakee says.

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Subject: WSJ: Finance Firms Stand to Gain Share Of Markets Enron Once Dominated

December 3, 2001

Finance Firms Stand to Gain Share Of Markets Enron Once Dominated

By **RANDALL SMITH** and **HENNY SENDER**
Staff Reporters of THE WALL STREET JOURNAL

Although financial-services firms are on the hook for billions owed to them by Enron Corp., there also are some winners among Wall Street firms that stand to pick up market share in the energy trading markets that Enron dominated.

Both Goldman Sachs Group Inc. and Morgan Stanley & Co., for example, hold leading positions in numerous energy markets, and both Wall Street experts and some executives at the firms said they should stand to benefit in increased trading volume.

Van Hesser, a credit analyst at Credit Suisse First Boston, noted in a report Friday that both Goldman and Morgan Stanley "have meaningful energy-trading operations." He cautioned that those firms might incur "some additional risk [from] their exposure to smaller, less-sophisticated trading firms that may be stressed by their own exposures to Enron." But, Mr. Hesser added, "they are experienced hands and know how to hedge and how to structure collateralized trading agreements."

John Shapiro, head of global energy trading at Morgan Stanley, agreed that his firm would likely be one of the financial-services firms whose trading activity could benefit from the reduction in Enron's market activity. Other participants that could also benefit include the trading units of J.P. Morgan Chase & Co., Bank of America Corp., Societe Generale SA and Deutsche Bank AG.

[\[Go\] See full coverage of the rise and fall of Enron](#)

Although Goldman doesn't break out its commodity-trading revenue, Morgan Stanley does. For the fiscal year that ended in November 2000, Morgan Stanley's principal transaction commodity trading revenue rose 34% to \$579 million, helped by higher revenue for energy-related products including electricity, natural gas and crude oil.

One barometer of the impact of Enron's reduced market presence has already been seen at Intercontinental Exchange, an online energy marketplace that has trailed a competing platform, EnronOnline. In an interview Thursday with Dow Jones Newswires, ICE Chief Executive Jeffrey

Sprecher said, "Our volumes are just soaring." Traffic on the ICE system has doubled in the past two weeks, and, Mr. Sprecher added, "I'd attribute all that to Enron's problems."

ICE's financial-services partners include Goldman, Morgan Stanley, Deutsche Bank and Societe Generale.

Although Morgan and Goldman have both fielded calls from parties that traded with Enron and want to shift some of their activity to those firms, an executive of one of the firms said the possibility of a bankruptcy-law filing had deterred dealers from taking over any of Enron's trading books or assets. That is because any such transactions could be disrupted or canceled in the course of a bankruptcy proceeding -- a step Enron took Sunday.

Enron's relations with Wall Street firms had shifted in recent years from that of a favored client to a rivalry as well, as Enron's trading ambitions grew and it began trading more and more on Wall Street's turf. Enron moved from trading securities closely related to its natural-gas business into oil derivatives and then to instruments closer to Wall Street's core, such as credit derivatives and packaging securities.

One securities firm that won't benefit as much as some might believe is the Salomon Smith Barney unit of Citigroup Inc. Although Salomon used to engage in more sizable energy-trading activity through its Phibro commodities arm, the firm has wound down much of those activities, and doesn't have anywhere near the market presence of Goldman or Morgan Stanley.

-- *Stephen Parker contributed to this article.*

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To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: WSJ: Energy Traders Scramble to Pick Up Market Share After Enron's Collapse

December 3, 2001

Energy Traders Scramble to Pick Up Market Share After Enron's Collapse

By ALEXEI BARRIONUEVO and SILVIA ASCARELLI

Staff Reporters of THE WALL STREET JOURNAL

A half dozen of Enron Corp.'s biggest former rivals are gearing up to grab chunks of the dominant share the energy concern held in the natural gas and power-trading markets.

But, the benefits could flow more slowly than those companies hope, analysts say, because Enron's demise likely will put the brakes on the fast-growing energy-trading industry and make some big energy customers more reluctant to rely on trading firms to guarantee supply and manage risks. Energy-trading companies play the role of middleman between producers and wholesale purchasers, moving and delivering commodities and managing price risks for customers.

"Eventually there will be winners, but until then, you will have a lot of turmoil," says Michael Barbis, an analyst at research and brokerage house Fulcrum Global Partners LLC. "A lot of players, such as utilities and hospitals, will be reluctant to sign long-term contracts with these trading companies, after seeing the best-capitalized player go out of the market."

Enron became a marketing colossus without spending on such hard assets as power plants or pipelines; instead, it mostly relied on locking up contracts with other parties for supply, capacity and storage that it would use for its trading operations. Now, the companies most likely to benefit from Enron's collapse will be those that have strong asset bases, putting investors, customers and creditors more at ease.

"Right now, the name of the game is credit-quality," says Paul Patterson, an analyst with Dutch investment bank ABN-Amro. "A balance sheet that is based upon assets is easier for creditors and investors to value than one based on intangibles."

When the Enron dust settles, top marketing firms such as American Electric Power Inc., of Columbus, Ohio; Duke Energy Corp., of Charlotte, N.C.; Williams Cos., of Tulsa, Okla., and Enron's crosstown neighbors in Houston -- El Paso Corp., Dynegy Corp. and Reliant Energy Inc. -- are best-positioned to grab pieces of Enron's 20% to 25% share of energy-trading volume.

In Europe, where Enron was considered one of the two biggest players in the Continent's nascent

power-trading industry, a mix of U.S. and European companies are poised to scoop up Enron's business.

Who gets what slice will depend on each company's heft, its trading sophistication and the strength of each business's assets in different regions, say analysts and company executives.

"Because of this meltdown, you will see companies move in that have assets in the area" to expand their trading activities, says Steve Malcolm, president and chief operating officer at Williams. While companies are prohibited from sharing information between their marketing and interstate-pipeline affiliates, "clearly you are looking to gain and extract intelligence from the marketplace to allow you to take more well-thought-out positions," he said.

El Paso will likely expand its natural-gas trading on the West Coast, where it owns significant pipeline assets, and in the Northeast. Duke and Reliant, already big traders on the West Coast, could grab even bigger chunks there, where they own generating capacity. Dynegy would likely be able to pump up in the Midwest, where it already is a strong power marketer and generator. In the Mid-Atlantic, American Electric's power-generation facilities would give it an edge.

American Electric, which has muscled up into the second-biggest trader of power and natural gas behind Enron, is viewed as a major beneficiary of Enron's decline. The company is the nation's top generator, with slightly less than 40,000 megawatts of capacity. Enron was trading about twice as much combined gas and power as AEP. "We are going to be one of the firms that picks up the slack," says Eric van der Walde, AEP's executive vice president of trading and marketing.

Asset-rich companies with plenty of cash to take on big trading positions include El Paso, which has the largest interstate pipeline in the country. El Paso also is one of the top five producers of natural gas in the U.S. and has contracted a huge amount of pipeline storage capacity on other people's lines, particularly in the West. Dynegy, which had most closely mirrored Enron's asset-light approach, has been adding generating assets and has a sizable pipeline capacity. El Paso and Williams have the biggest contract positions in natural-gas storage.

Williams is more focused on long-term risk-management contracts with producers and end-users seeking to hedge their exposure to volatile commodity prices. The company, which already has the second-largest pipeline system in the U.S., will spend about \$5 billion on pipeline projects through 2004.

While company executives say confidently that any gains in market share will easily counteract any losses resulting from uncollected money owed by Enron, some analysts say the Enron debacle may continue to depress the stocks of companies with big trading businesses.

Across the Atlantic, U.S. firms such as AEP and Duke, which have small operations in Europe, are likely to face stiff competition from Europeans such as RWE Trading GmbH, a unit of German power giant RWE, Belgium's Electrabel and Innogy PLC, the second-largest generator of electricity in England and Wales.

Most of Innogy's trading is in the United Kingdom, but the demise of Enron might spur it to expand its operations more quickly in Europe, said Brian Senior, Innogy's director of trading and asset management.

RWE Trading, barely one year old, is considered the most-aggressive European player, with trading activities in London and Essen, Germany; it plans to open an operation in Houston early next year.

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Sent: Monday, December 03, 2001 12:16 PM
To: Salladin, Anne; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamorenna (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidi; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: WSJ: Enron's Big Investments in Brazil Contributed to the Firm's Collapse

December 3, 2001

Enron's Big Investments in Brazil Contributed to the Firm's Collapse

By MIRIAM JORDAN

Staff Reporter of THE WALL STREET JOURNAL

SAO PAULO, Brazil – Enron Corp. bullishly stormed into Brazil, only to have trouble beating a retreat from Latin America's biggest energy market.

For example, in 1998, Enron offered \$1.27 billion for a Sao Paulo state electricity distribution company, nearly double the auction's minimum price. Two years later, the Houston company was trying to sell the distributor, Elektro-Eletrificacoes e Servicos SA, and other projects in Brazil, where Enron says it invested more than \$3 billion.

Even before the company's collapse in the U.S., Enron executives had admitted that its Brazilian investments weren't working out as planned. "The prospect of selling Brazilian assets has been something we have been looking at even before the current problems," says company spokesman Keith Miceli in Houston.

Enron's Brazil operations have suffered from a shift in the company's global strategy toward trading rather than producing or distributing energy, local regulatory challenges, a sharp currency devaluation and the country's energy shortage. "Brazil is obviously not the reason for Enron's downfall," says a former senior executive of Brazilian operations. "But it definitely contributed." The executive said that Enron is operating with a loss in Brazil. The company, which once had 300 corporate staffers in Sao Paulo, now has only 100.

In 1993, Enron envisioned a single energy market spanning southern South America in which Enron would be the dominant player. It moved aggressively into Brazil as of 1994, betting on its size, growth prospects and new privatization drive. Brazil has installed power capacity of 75,000 megawatts, and will require an additional 25,000 over the next five years. Its energy requirements are already four times greater than those of neighbor Argentina and the same as Britain's. They will surpass Germany's in five years.

The key to Enron's ambitions was a 1,870 mile, \$2 billion pipeline to bring natural gas from Bolivia to

Brazil's industrial heartland. Rebecca Mark, then president of Enron's international unit, crisscrossed South America trying to gain approvals for the pipeline and for a string of new power projects that it would feed. Enron bought stakes in power plants, natural gas distributors and in 1998, Elektro.

Enron's problems were, from the start, almost as big as its ambitions. A \$550 million project in the central Brazilian state of Mato Grosso to build three power plants fed by Bolivian gas overran its budget by \$200 million and its construction deadline by two years. The 400-mile pipeline needed for the project was held up when Brazilian environmental officials forced a 62 mile diversion so as not to disturb a rare species of bat. What's more, only one of the three power plants is operating and until September had to run on more expensive diesel fuel until the natural gas pipeline was finished.

Brazil's volatile economy also hurt Enron, as well as other foreign energy investors. Elektro distributes electricity to about 40% of Sao Paulo, Brazil's largest and wealthiest state. But the devaluation of the Brazilian currency in 1999 has been a blow to Elektro. The government controls electricity rates and has resisted companies' pleas to pass on dollar-based costs, including corporate debt, to consumers. Electricity rates in Brazil are half as much as those in neighboring Argentina, for example, industry officials say. Making matters worse, Brazil imposed energy rationing in June, reducing Elektro's revenue by 30%, said an energy specialist who advised Enron in Brazil.

The Brazil-to-Bolivia pipeline, in which Enron has a minority stake alongside state companies, hasn't turned out to be much of a salvation for energy starved Brazil either. Few of the power plants that it was to feed have been built due to investor concerns about the regulatory environment. As a result, demand for gas from the pipeline is less than expected.

Even the more opportunistic moves by Enron haven't worked out. Earlier this year, the company built, in just six months, a \$300 million natural gas power plant outside Rio de Janeiro to capitalize on the country's acute energy shortages. But the local spot market for energy remains plagued by operational and financial-settlement problems. So far, Enron hasn't received a cent for the energy it has sold from the plant. What was supposed to be a "cash cow" has turned out to be "a disaster," says an Enron executive.

Enron has found a buyer, so far, only for its 25% and 34% stakes, respectively, in Companhia Estadual de Gas and Companhia Estadual de Gas-Rio de Janeiro, two gas-distribution companies serving the city and state of Rio. Enron and Brazilian state oil company Petroleo Brasileiro SA signed a deal on April 30. Closure is imminent, Enron says.

"They have been shopping around for a while and not found the prices they wanted," says UBS Warburg energy analyst Ronald J. Barone of Enron's Brazilian assets. "The fact that the situation is dire now means ... they will get low-ball bids because people know they are desperate."

Write to Miriam Jordan at miriam.jordan@wsj.com <<mailto:miriam.jordan@wsj.com>>

Southern Exposure

Enron's Latin American assets and interests include:

-- **Elektro (Brazil):** Power distribution company in Sao Paulo.

- **Gaspart (Brazil):** Significant stake in the gas distribution companies of seven coastal states.
- **CEG and CEGRIO (Brazil):** Equity interest in both gas distribution companies which were previously government-owned.
- **Cuiaba (Brazil):** A 480 megawatt (MW), combined-cycle natural gas power plant in Cuiaba.
- **Bolivia-Brazil Pipeline:** Partnership in the 3,000-km pipeline stretching from Santa Cruz de la Sierra, Bolivia to Porto Alegre, Brazil.
- **Eletrobolt (Brazil):** A 380 MW natural gas power plant located near the city of Rio de Janeiro.
- **Transportadora de Gas del Sur (Argentina):** An ownership interest in the 6,604-km pipeline system, the largest pipeline system in South America.
- **Central Termica Modesto Maranzana (Argentina):** A thermal power plant, located in the city of Rio Cuarto, province of Cordoba.

Source: The company

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, December 03, 2001 12:20 PM
To: Bair, Shella; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidi Lynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: WSJ: Enron Customers Seek Backup, Check Contracts for Out Clauses

December 3, 2001

Enron Customers Seek Backup, Check Contracts for Out Clauses

By RHONDA L. RUNDLE

Staff Reporter of THE WALL STREET JOURNAL

THE DEAL MAKER		
Enron's major customers for retail energy services, under 10 year contracts.		
COMPANY	YEAR ANNOUNCED	VALUE (IN MILLIONS)
Owens-Illinois	2001	\$2,200
Simon Property	1999	\$1,500
Quebecor World	2000	\$1,000
Owens Corning	1999	\$1,000
IBM	2000	\$610
Chase Manhattan	2000	\$750
Pilkington North America	2001	\$500

Source: Enron Corp.'s Enron Energy Services subsidiary

Enron Corp.'s commercial and industrial customers, including some big manufacturers, technology firms and hotel chains, are scrambling to line up alternative suppliers in case the collapsed energy company isn't able to supply power or meet other obligations under its long-term contracts.

A sense of urgency spread last week among corporate customers of Enron, which filed Sunday for Chapter 11 bankruptcy-court protection. Some customers of Enron, Houston, are scouring their contracts for language they are hoping may allow them to legally break those pacts, energy consultants said. Customers who signed long-term accords at prices above current market also have an economic incentive to drop them, the advisers added.

A spokeswoman for the Enron subsidiary that serves commercial and industrial companies, Enron Energy Services, which was one of the Enron units that also filed Chapter 11, declined to discuss its customers' intentions. She said she wasn't aware of one that has recently switched to a rival supplier,

and she said there haven't been any service interruptions. "The customers are calling, and we're calling them. We're doing everything possible to assure that they receive power and gas, and it's a very difficult situation," she said.

Enron Energy Services offers a broad spectrum of energy-management services, and can take over nearly all aspects of a customer's energy-related activities. This "outsourcing" role includes monitoring power meters, paying energy bills, installing efficient air-conditioning, heating and lighting systems and even designing and constructing energy infrastructure projects.

Enron Energy Services is known as an innovator that has grown rapidly since it began operations in 1997. The Enron unit was "an icebreaker into the executive suite of corporate America to show how they could unlock the value of energy expenditures," said Craig Sieben, chief executive of Sieben Energy Associates, a management consulting firm in Chicago. Enron doesn't disclose how many customers it has, but says the total value of its long-term contracts has mushroomed to about \$50 billion.

Nobody knows what is going to happen to all those contracts in the wake of the bankruptcy filing. "What the clients are hearing from everybody, including us, is that if you have any other options, look at them," Mr. Sieben said.

"We're monitoring the situation very closely. We do have contingency plans in place if we need to use them," said a spokesman for PepsiCo Inc.'s Quaker Oats Co. unit, which recently entered into a 10-year energy management agreement with Enron. A spokeswoman for another major customer, Starwood Hotels & Resorts Worldwide Inc., said the hotelier is watching the situation, but doesn't expect to be affected.

[Table]

California's universities and state colleges, which signed a high-profile agreement with Enron in 1998, are in negotiations to extend that contract beyond its expiration in March. But as Enron's financial picture has worsened, the talks have lagged, said Pat Drohan, an assistant vice chancellor at the state college system. "We are looking at alternatives to try and counteract any unfortunate collapse at Enron," he said. In addition to providing electricity, Enron is the prime contractor on construction of a new heating system at a facility in Stockton, Calif., he said.

One complication for Enron's California customers is that the state passed a law this summer that prohibits new "direct access" contracts between power companies and commercial users. And in the time since Enron signed many of its contracts in the state, power prices have risen by 40% to 80%, raising the prospect that if Enron customers are forced to rely anew on the state's utilities, they suddenly will be paying much higher prices. In other states, the situation is almost the opposite: Customers abandoned by Enron might now find they can buy power more cheaply given the drop in the price of natural gas, which fuels many U.S. power plants.

Arthur Gelber & Associates has been contacted by at least eight of Enron's customers, but "we haven't assumed any contracts," said Mr. Gelber, owner of the Houston-based advisory and consulting firm, which is a smaller Enron competitor. Each contract is unique and different, but "some I've reviewed have an 'adverse material change' clause and may be terminated," he said. He declined to identify any of the customers or contracts.

Other rivals in the management business are getting calls from Enron's customers. "Have our phones been ringing more recently? Yes, of course they have," said Bob Dickerman, president of Sempra

Energy Solutions, a unit of San Diego-based Sempra Energy. "But this isn't a simple business. It involves credit risk for the customer. You don't switch a customer with a phone call," he said.

Write to Rhonda L. Rundle at rhonda.rundle@wsj.com <mailto:rhonda.rundle@wsj.com>

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, December 03, 2001 12:31 PM
To: DeMarco, Edward; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: WSJ: Enron Failure Likely to Burden Insurers And Further Increase Soaring Premiums

December 3, 2001

Enron Failure Likely to Burden Insurers And Further Increase Soaring Premiums

By CHRISTOPHER OSTER

Staff Reporter of THE WALL STREET JOURNAL

Enron Corp.'s collapse is expected to cost insurance companies more than \$3.5 billion and most likely will further increase skyrocketing insurance rates.

About \$2 billion of the losses is expected to be shouldered by property-casualty underwriters, who are expected to pay \$40 billion to \$70 billion in claims from the Sept. 11 terrorist strikes. Those claims already have touched off a run-up in premium rates. The losses would make next year's price increases among the biggest in recent history for insurers, if not the biggest, said Alice Schroeder, a property-casualty insurance analyst at Morgan Stanley. Such losses work to siphon off capital from the insurance market, reducing price competition.

The damage to individual property-casualty insurers is "virtually impossible" to assess at this point, but Ms. Schroeder said a "material impact" on the sector is likely. The losses are expected to result from claims against directors-and-officers liability policies, surety bonds and financial-guarantee coverage. Directors-and-officers liability policies protect a company from lawsuits stemming from the actions of its executives and surety bonds are bonds that insure the completion of a transaction or a project.

Life insurers, meanwhile, are expected to report that the values of their investment portfolios have dropped by more than \$1.5 billion, related to holdings of Enron debt, which has plunged in value in recent weeks along with the company's stock price. Investors' confidence in the company has sunk amid earnings restatements and revelations about related-party transactions.

Nontraditional financial-guarantee insurance and surety bonds could prove the source of some of the biggest losses, analysts said. Enron obtained coverage for such purposes as enhancing the value of Enron's guarantee of certain debt of Enron-related projects as well as the company's guarantees on the execution of certain derivative contracts. Analysts said the payments on the policies would be triggered immediately upon a default event -- for example, a missed payment or bankruptcy filing by Enron. "We understand that some contracts may have already been triggered," Ms. Schroeder said.

On Friday, Chubb Corp., Warren, N.J., said it was reviewing its surety bonds related to Enron and estimated its maximum exposure at \$143 million. The property-casualty underwriter said it is unable to estimate the actual amount, if any, that it may be required to pay and that thus far it hadn't received any claims under the surety bonds.

Ms. Schroeder estimated that a maximum of \$300 million in directors-and-officers liability coverage likely is involved, divided among several insurance companies. Already, Enron faces multiple shareholder-driven lawsuits because of the steep drop in the company's stock price.

Jason Zucker, a life-insurance analyst at Banc of America Securities, said the Enron exposures would "pressure bond portfolios in this recessionary environment."

Among those with big holdings is John Hancock Financial Services Inc., according to insurance analyst Colin Devine of Salomon Smith Barney, who expects the company to incur a loss of \$120 million this quarter on the bonds. A John Hancock spokeswoman declined to comment on the estimate.

Mr. Devine said Principal Financial Group Inc. and Lincoln National Corp. also have substantial Enron bond holdings. In a news release, Principal said the company is reviewing its approximately \$171 million "exposure to Enron" and expects to take a write-down this quarter of a size not yet estimated. Principal said it also is reviewing an additional exposure of \$50 million from investments in Enron-related entities. A spokeswoman for Lincoln National said the company had \$25 million of Enron Corp. debt and \$70 million from its subsidiaries. "We may take a charge of some of the exposure related to the parent, but we won't know until we get closer to the end of the quarter."

Write to Christopher Oster at chris.oster@wsj.com <<mailto:chris.oster@wsj.com>>

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, December 03, 2001 2:38 PM
To: Salladin, Anne; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamorenna (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schulltheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: Enron Canada To Ask Court To Enforce Energy Contracts

December 3, 2001

Enron Canada To Ask Court To Enforce Energy Contracts

By Dina O'Meara
of DOW JONES NEWSWIRES

CALGARY -- **Enron** Canada Corp. will ask an Alberta court Wednesday to prevent its trading counterparties from exiting their contracts for 30 days, according to documents obtained by Dow Jones Newswires.

The action is needed to ensure **Enron** Canada - which wasn't included in **Enron** Corp.'s (ENE) filing for bankruptcy-court protection Sunday - can continue to operate, Rob Milnthorp, president and CEO of the Calgary-based company, said in a Dec. 2 letter to counterparties.

"**Enron** Canada is solvent and is able to continue to pay its obligations as they become due, provided the arms-length counterparties who have entered into contracts with us continue to perform their obligations," Milnthorp said.

Enron Canada first sought a stay from the Court of Queen's Bench of Alberta on Friday, but was ordered first to notify its counterparties.

If the court doesn't grant the stay, **Enron** Canada may request an order appointing a liquidator under Canadian law, a lawyer for **Enron** Canada said in a letter to the court.

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, December 03, 2001 2:46 PM
To: Salladin, Anne; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: Enron Hint On Other Affiliates Comes From Court Motion

December 3, 2001

Enron Hint On Other Affiliates Comes From Court Motion

NEW YORK -- **Enron** Corp. (ENE) suggested Monday that some of its affiliates beyond those who have already filed for Chapter 11 bankruptcy protection may do so in the future.

In a motion filed with the New York federal bankruptcy court hearing Enron's Chapter 11 case, the company said it "anticipate(s) that certain of (Enron's) non-debtor affiliates may also file voluntary petitions under Chapter 11."

An **Enron** spokesman couldn't immediately be reached for comment.

Enron and 13 related entities filed for Chapter 11 protection Sunday. Not all of Enron's businesses filed, however, and the statement in Monday's motion raises the possibility that some of them might file down the line.

The statement came in the context of a request by **Enron** for the court to extend the deadlines for filing several documents it must file under bankruptcy law, including schedules of its assets and liabilities and statements of its financial affairs. The company said that other affiliates might file for Chapter 11, and that if they did, the extended deadlines should apply to those entities too.

The company didn't say which affiliates might file, or when, or how likely it was to happen.

-By Michael Rapoport, Dow Jones Newswires; 201-938-5976; michael.rapoport@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, December 03, 2001 2:49 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Celina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: CMS Energy Refutes Enron Creditor Claim; Owes Enron Money (Confusion over who owes)

December 3, 2001

CMS Energy Refutes Enron Creditor Claim; Owes Enron Money

By CHRISTINA CHEDDAR

OF DOW JONES NEWSWIRES

NEW YORK -- In an illustration of just how complex **Enron Corp.**'s (ENE) bankruptcy case will be, CMS Energy Corp. (CMS) said it shouldn't be listed among **Enron North America Corp.**'s largest unsecured creditors.

According to CMS Energy spokesman Kelly Farr, CMS Energy, a Dearborn, Mich., operator of electric and gas utilities, owes **Enron** money when all of its forward trading positions are "netted out."

Farr declined to say how much it owes **Enron**.

In the court filing for Enron's marketing and trading unit, **Enron North America** said it owes the energy marketing unit of CMS Energy \$13.6 million for trading debt.

An **Enron** spokesman wasn't immediately available to comment.

Enron filed for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code late Sunday night in the U.S. Bankruptcy Court for the Southern District of New York. The initial hearing on the case is scheduled for 4 p.m. EST Monday.

Enron North America, one of the 14 **Enron** units included in the filing, was said to have \$13.74 billion in assets, and \$8.84 billion in debts, not including any off-balance sheet or contingent obligations.

-By Christina Cheddar, Dow Jones Newswires; 201-938-5166; christina.cheddar@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, December 03, 2001 3:09 PM
To: Bair, Shella; Berardi, Steve; Bitsberger, Timothy; Celina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidllynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: Enron Delivering Same Message To Customers As To Wall St

December 3, 2001

Enron Delivering Same Message To Customers As To Wall St

Dow Jones Newswires

NEW YORK -- **Enron** Corp.'s (ENE) message to its customers, partners and vendors is similar to its message to Wall Street: We've filed for Chapter 11, we're working to recapitalize the company and, in the meantime, we're doing what we can to minimize disruptions.

Enron has sent a version of that message to seven parties affected by its bankruptcy filing: trading partners, transportation customers, **Enron** Energy Services customers, broadband customers, international customers, vendors and the Houston community.

Each individual message can be found in the "news and press room" of Enron's Web site. Enron's press room portion of its Web Site is at <http://www.enron.com/corp/pressroom/>

The most extensive letter was written to Enron's Energy Services customers. The message, written in a Q&A format, attempts to answer general customers questions about their contracts, services and operations.

For example, one question listed is "Since you filed Chapter 11, do I have the legal right to get out of my contract?"

Enron's answer, "As long as we are providing contracted for services, we expect the contract to remain in effect."

By George Stahl; Dow Jones Newswires; 201-938-5163.

Nickoloff, Peter

From: Carleton, Norman
Sent: Monday, December 03, 2001 6:44 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: WSJ: Enron Secures \$1.5 Billion in Financing

December 3, 2001

Major Business News

Enron Secures \$1.5 Billion in Financing, Plans to Cut About 4,000 Jobs in the U.S.

A WALL STREET JOURNAL ONLINE News Roundup

NEW YORK -- **Enron Corp.** secured \$1.5 billion in much needed "debtor in possession" financing late Monday.

Separately, **Enron** will cut about 4,000 jobs in the U.S., or nearly 20% of its world-wide work force, with the bulk of the staff cuts in Houston, a company spokeswoman said Monday.

The "debtor in possession" or DIP financing was seen as critical for **Enron** to continue operating and especially crucial for the company to protect its trading operations.

The loan, provided by Enron's two lead banks, J.P. Morgan Chase & Co. and Citigroup Inc., is collateralized by all of Enron's assets, including \$1.8 billion in proceeds for the sale of Enron's Portland General Electric to Northwest Natural Gas Co., and Enron's two pipelines, the Northern Natural Gas pipeline and the Transwestern pipeline.

A person familiar with the matter said that as part of the financing package, **Enron** will receive \$250 million immediately. Another \$250 million will become available as soon as J.P. Morgan Chase and Citigroup approve a business plan submitted by **Enron**. That's expected in the next couple of weeks.

The release of the remaining \$1 billion is contingent upon syndication and final court approval, the person familiar with matter said.

J.P. Morgan Chase and Citigroup, which had loaned \$1 billion to **Enron** while the company struggled to stabilize its spiraling finances, will get some of their investment back through the debtor-in-possession financing.

As a condition of the financing package, **Enron** will use some of the cash injection to repay a \$550 million loan backed by Enron's Transwestern Pipeline, the person familiar with the matter said.

That will allow **Enron** to use cash flow from that pipeline to finance its operations rather than have it be part of the bankruptcy estate and thus reserved for creditors.

The structure also allows J.P. Morgan Chase and Citigroup to recoup some of their loan exposure to **Enron** since DIP financing is senior to all other claims in bankruptcy court.

Enron's DIP financing was approved by a bankruptcy judge in an initial court hearing late Monday.

The person familiar with the matter said J.P. Morgan Chase and Citigroup will move to syndicate all of the loan. Disbursement of the last \$1 billion is expected in about a month.

Enron, which has filed for bankruptcy-court protection, employs about 21,000 workers, with two-thirds of the staff in the U.S. and one-fifth in the United Kingdom. The energy trader has employed 7,500 workers in Houston, where it is based.

The company plans to ask a bankruptcy court to provide its workers with medical and other benefits, plus \$4,500 each in severance, the **Enron** spokeswoman said. She wouldn't elaborate on layoffs at the company's U.K. operations.

Enron Europe Ltd. cut roughly 1,100 jobs in the U.K. after its European energy-trading arm last week sought protection from creditors by appointing PricewaterhouseCoopers as an administrator to Enron's European holding company.

The U.K. job cuts came as analysts said that the suspension of **Enron** Europe from trading on a number of power markets could make it more difficult for the already struggling energy company to get out of its positions as it seeks to unwind operations.

On Sunday, **Enron** filed for protection from creditors in a New York bankruptcy court, the biggest such filing in U.S. history.

The petition came less than seven weeks after **Enron** began a calamitous fall that led to the collapse of its once-lofty stock price into penny-stock territory. The decline reflected a loss of confidence in the company caused by big losses in the third quarter, repeated restatements of earnings and revelations, now being investigated by the Securities and Exchange Commission, that some of its employees participated in partnerships designed to keep debt off the balance sheet, but which produced still more losses.

Besides **Enron**, 13 major subsidiaries are named in the filing under Chapter 11 of the U.S. Bankruptcy Code in the Southern District of New York.

Though based in Houston, **Enron** picked the New York court because it has enough room on its calendar for a complex case and because it has handled other high-profile bankruptcy filings, including Armstrong Holdings Inc., Bethlehem Steel Corp. and Iridium LLC, an **Enron** attorney said.

Simultaneously, **Enron** has sued crosstown rival Dynegy Inc. for "not less than \$10 billion," accusing it of wrongfully terminating a merger deal last week that the two firms had reached just two weeks earlier.

Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, December 04, 2001 10:01 AM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: House Staff To Meet With SEC Staff On Enron; Jan Hearing

December 4, 2001

House Staff To Meet With SEC Staff On Enron; Jan Hearing

Dow Jones Newswires

(This article was originally published Monday.)

WASHINGTON -- U.S. House Energy and Commerce Committee staff have scheduled a series of meetings this week - including one with Securities and Exchange Commission staff - in preparation for a hearing sometime in January on the financial collapse of **Enron** Corp. (ENE).

"The committee will be moving very aggressively to try and pinpoint what went wrong and what, if anything, Congress can do to prevent this type of thing from happening again," said Ken Johnson, spokesman for Rep. Billy Tauzin, R-La., the committee's chairman.

Johnson disclosed the meeting schedule for the week: The committee staff will meet with key Securities and Exchange Commission staff Tuesday. The agency is investigating the off-the-books transactions that appeared to lead to **Enron** overestimating its earnings and contributed to a collapse in the company's stock equity.

The committee staff will meet Wednesday with officials from Arthur Anderson, Enron's outside auditor, and the Financial Accounting Standards Board. On Thursday, the committee staff will travel to Houston to meet with top **Enron** executives.

The committee expects the hearing and any potential legislative action on the **Enron** debacle to primarily address accounting and bookkeeping matters, assuming the investigation doesn't find other issues were involved, Johnson said.

-By Bryan Lee, Dow Jones Newswires; 202-862-6647; Bryan.Lee@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, December 04, 2001 11:10 AM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidi Lynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: WSJ: Enron Secures \$1.5 Billion in Financing, Lays Off About 4,000 Workers in the U.S.

December 4, 2001

Major Business News

Enron Secures \$1.5 Billion in Financing, Lays Off About 4,000 Workers in the U.S.

By MITCHELL PACELLE, JATHON SAPSFORD and ANN DAVIS

Staff Reporters of THE WALL STREET JOURNAL

Turning to some of its largest creditors as potential saviors, Enron Corp. secured as much as \$1.5 billion in new financing from J.P. Morgan Chase & Co. and Citigroup Inc., and was deep in negotiations for an additional lifeline to salvage its flagship energy-trading operations.

The new agreement for debtor-in-possession financing, which will rank senior to most of Enron's existing debt obligations, represented a critical first step to keeping the company alive as it reorganizes under bankruptcy-court protection. The Houston-based energy firm is laboring to devise a plan to navigate the Chapter 11 process without being forced into a hurried liquidation. The developments came as the Justice Department, following a recent similar move by the Securities and Exchange Commission, began a criminal probe into Enron's dealings, a person familiar with the matter said.

Enron has been negotiating with three money-center banks -- J.P. Morgan, Citigroup's Salomon Smith Barney unit, and UBS AG -- for a separate deal to pump capital into its trading operations through a joint venture that would likely result in one of the banks controlling a new trading company, according to people involved in the matter. A spokesman for Citigroup said, "We are not at this time interested in the trading business." The other banks declined to comment.

Enron's advisers consider it vital to keep alive these wholesale energy-trading operations -- once considered the crown jewel of Enron -- if the company is to have any hope of continuing to operate. In recent days, trading has ground almost to a halt, with the exception of trades with counterparties who want to unwind positions. Enron Monday laid off 4,000 people in Houston -- roughly 20% of its world-wide work force of 21,000 people.

Late Monday afternoon, in the company's first hearing in the U.S. Bankruptcy Court, Southern District

of New York, Judge Arthur J. Gonzalez, who will handle the case, approved a series of routine requests by Enron lawyers to make \$48 million of payments on everything from rent at its skyscraper in Houston to severance for employees who will be laid off.

Enron's plan for bankruptcy seems to be shaping up as a multifront effort. The company first hopes to calm the markets with its new debtor-in-possession financing, then revive its crippled trading arm by putting it under the control of a new, credible partner. Chapter 11 bankruptcy protection temporarily shelters a company from creditors to provide time for the company to reorganize.

Once some assets are sold to generate cash, the plan is to reorganize – or "skinny down," one adviser said – into a new, smaller Enron around several core assets, such as its pipeline business. Enron has agreed to sell its Portland General utility.

The company will have to clear a number of major hurdles. For starters, it will have to convince creditors they stand to recover more by keeping the company operating, at least for a while, than by liquidating the company in a fire sale.

According to one **bankruptcy lawyer** who has been contacted by several creditors, it isn't yet obvious to creditors "that recoveries will be higher by keeping the company going."

The list of creditors in the case, the largest bankruptcy filing ever with more than \$31 billion in reported debt and billions more in as-yet unreported off-balance-sheet liabilities, runs to more than 50 pages, and the most powerful of the bunch are expected to maneuver aggressively for control of the official creditors' committee. All told, Enron's top 10 bank lenders account for between \$7.5 billion and \$8.5 billion of on- and off-balance-sheet debt, one person involved in the workout said.

Among those with the most exposure are J.P. Morgan, Citigroup, Deutsche Bank AG, Credit Suisse Group's Credit Suisse First Boston, Royal Bank of Scotland Group PLC and Bank of America Corp., according to a senior banker involved in the workout. Some of these banks have exposure of as much as \$1 billion, the banker said, in a variety of loans or other forms of credit, including both secured and unsecured. J.P. Morgan has confirmed its exposure within that range. The other banks declined to comment, citing client privilege.

"There will be jockeying between and among the bank creditors, the bondholders, and the trade creditors," predicted one lawyer who has been contacted by several clients involved in the process. The creditors who control the committee, which is expected to take as long as several weeks to be formed, will be able to steer the creditors' positions in court.

As all of this is going on, the Justice Department has decided to open a criminal investigation into the company, a person close to the matter said, leading to competition among federal attorneys' offices that want to take the lead. Offices in New York, San Francisco, Los Angeles and Houston have all expressed interest. The probe comes in addition to an SEC investigation into Enron and Arthur Andersen LLP's audit work for the company.

Keeping the Lights On

Enron is maneuvering to continue operating as it seeks to reorganize under Chapter 11 bankruptcy protection. In the latest developments:

- Enron has secured debtor-in-possession financing of \$1.5 billion to fund operations while it is in Chapter 11 proceedings.
- Enron is searching for a joint-venture partner to recapitalize the company's wholesale energy-trading business.
- Dynegy files suit against Enron, reasserting its claim over the Northern Natural Gas pipeline in exchange for its \$1.5 billion investment; the move comes after Enron's \$10 billion suit against Dynegy filed Sunday for breaching its merger agreement.
- Enron lays off about 4,000 employees mostly among its 7,500 employees in its Houston head office. The layoffs come in addition to 1,100 jobs in London cut Friday.
- Congress steps up its probe of Enron, with House Commerce Committee staff set to meet this week with the SEC and in Houston with Enron executives.

House members in Washington are also gearing up for an investigation. Ken Johnson, a spokesman for the House Energy and Commerce Committee, said committee representatives will be briefed by the general counsel and enforcement chief of the SEC Tuesday. Wednesday, top officials from Arthur Andersen and the Financial Accounting Standards Board are meeting with committee staff in separate venues and on Thursday, three committee investigators are headed to Houston to speak with Enron executives. "The committee is moving aggressively to pinpoint what went wrong with Enron to see what if anything Congress can do to make sure it doesn't happen again," Mr. Johnson said.

For Enron, the key to survival may well be its ability to convince creditors not to rush the process. One bankruptcy expert noted that creditors of Drexel Burnham Lambert Inc., a securities company that sought bankruptcy protection a decade ago, agreed to a multiyear unwinding of assets, which led to higher recovery to creditors than initially expected.

The debtor-in-possession financing will be doled out to Enron in three installments, beginning with a \$250 million piece this week, which was approved by the court Monday. That money, which will be syndicated to other bank lenders, will be used in part to repay some of an existing \$1 billion credit line extended earlier by Citigroup and J.P. Morgan.

The new money will be secured by Enron assets, including proceeds from its sale of the Portland General utility, and by other pipeline assets. A senior banker involved in the deal said despite assumptions in the market that Enron has pledged all of its assets to raise money, the banks in this latest round have had little problem finding available assets for further financing.

In the court hearing, Enron's lawyers said the company has \$500 million in cash.

The bankruptcy filings of Enron and its affiliates reveal a dizzying array of creditors, ranging from banks to telecommunications firms such as Level 3 Communications Inc. and 360networks Inc. Enron's loans, in some cases, have been syndicated to as many as 100 lenders and investors.

As a result, the pain for banks is likely to be felt widely, but not necessarily deeply. The hit to the top lenders with as much as \$1 billion in exposure to Enron is likely to be a fraction of their loan portfolios, which are measured in the hundreds of billions of dollars.

Yet while wide distribution helps limit the damage to each lender, it can make the bankruptcy process even more complicated. "When you have a syndication that large, you often have large constituencies forming sometimes with cross purposes," said Walter Einhorn, president of Sunrock Capital Corp., an asset-based lender with experience in workouts. "You never know who's going to upset the apple cart."

Another potential stumbling block to Enron's restructuring effort is the myriad off-balance-sheet partnerships that were key to many of Enron's transactions. Creditors have yet to receive a clear picture of these liabilities, which bankers involved in the process have put at around \$27 billion.

-- Michael Schroeder and John Emshwiller contributed to this article.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, December 04, 2001 11:20 AM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidi Lynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: Bloomberg: Enron Takes 1st Steps in Bid to Negotiate Bankruptcy (Update5)

12/04 09:52

Enron Takes 1st Steps in Bid to Negotiate Bankruptcy (Update5)

By Jeff St.onge

New York, Dec. 4 (Bloomberg) — Enron Corp. is working to survive history's biggest Chapter 11 reorganization, lining up a \$1.5 billion bankruptcy credit line, getting permission to spend money to keep operating and firing 4,000 workers.

An Enron attorney told U.S. Bankruptcy Judge Arthur Gonzalez the company is talking with backers to revive its energy-trading business under new ownership. The operation, Enron's most profitable, unraveled after the Houston-based company in October posted a third-quarter loss of \$1.01 billion.

While the line of credit eliminated one immediate threat, trading partners are hard to find, rival Dynegy Inc. is seeking to take over an Enron pipeline and federal authorities are investigating what sent the biggest energy trader into bankruptcy. Competitors such as Suez SA, the second-biggest water company, are looking at buying company assets as Enron raises money.

"The key issue now for Enron's creditors is whether the company can salvage material value from its trading operations before their critical mass of personnel, expertise and reputation dissolves," said Jeff Werbalowsky, senior managing director at Houlihan Lokey Howard & Zukin.

In an indication that unsecured creditors don't expect to be repaid in full, Enron's 6 3/8 percent bonds due in 2003 traded around 24 cents on the dollar, according to Bloomberg data.

Shares of Enron rose 39 cents to 79 cents. Shareholders are last in line to be paid in Chapter 11 cases and typically get nothing if other creditors aren't fully reimbursed.

Business Challenges

Enron is courting investors to revive its crippled trading business, even as it loses customers who fear the company will be unable to make good on its obligations. The company is in talks with financial institutions to fund the wholesale trading business "under new ownership," Chief Operating Officer Greg Whalley said in a statement.

Enron is negotiating with J.P. Morgan Chase & Co., Citigroup Inc.'s Salomon Smith Barney and UBS AG about a possible joint venture to run the energy-trading operations, the Wall Street Journal said, citing unidentified sources.

The trading business is the most valuable part of Enron, analysts say. "If they don't resurrect it, they have an extreme problem," said Jon Kyle Cartwright, an analyst with Raymond James & Associates. "Cash alone won't save the operation, they need someone to run it" because of Enron's low credit ratings and deteriorated credibility, he said.

At EnronOnline, the Web site that once handled \$2.8 billion in commodity transactions a day, trading has plunged, raising doubts that Enron will be able to rescue the business. Enron customers such as Mirant Corp. and Aquila Inc. have taken business elsewhere.

"Until we've seen the fallout from this bankruptcy, I don't think you're going to find a lot of entities that are prepared to trade with" Enron, said Daniel Gordon, head of commodities trading at Hagerstown, Maryland-based Allegheny Energy Inc., which owns utilities in five states.

Meanwhile, European companies began scrutinizing Enron's assets. Suez is interested in some of Enron's holdings, said Jacques Van Hee, a spokesman for its energy unit. Glencore International AG yesterday said it was considering Enron's metals- trading business.

Legal Threats

Enron's woes come at a time when the U.S. economy is in its first recession in about a decade and the European and Japanese economies are also shrinking. As of last month, a record 224 publicly traded companies had filed for bankruptcy in the U.S. this year, 27 percent more than last year's record 176, according to BankruptcyData.com, a Boston-based Web site. Filers range from Bethlehem Steel Corp. to Polaroid Corp.

Lawsuits and federal investigations are adding to Enron's difficulties. The U.S. Department of Justice has started a criminal probe of Enron's dealings, the Wall Street Journal reported Monday, citing unidentified sources.

Dynegy is suing in a Texas court to gain control of Enron's Northern Natural Gas Co. pipeline. Enron went to court first, seeking \$10 billion over its rival's abandonment of a \$23 billion merger.

Enron's nosedive -- its shares have lost 99 percent of their value -- has also placed a spotlight on Arthur Andersen LLP, the company's auditor. Enron said last month it overstated its 1998 income by \$113 million. The Securities and Exchange Commission is investigating.

Enron workers are suing over losses to their retirement accounts.

\$1.5 Billion Loan

With just \$500 million left to fund operations, Enron yesterday won Gonzalez's permission to draw \$250 million of the \$1.5 billion in Chapter 11 financing from a bank group led by J.P. Morgan Chase and Citigroup Inc.'s Citibank. A hearing to approve use of the full amount was set for Jan. 7.

The company will use more than a third of the \$1.5 billion credit line to repay an earlier \$550 million unsecured loan from J.P. Morgan Chase and Citibank to Enron's Transwestern Pipeline unit.

The new loan would be paid out ahead of all previous debts. The unit will likely file for bankruptcy once its debts have been repaid, said Donald S. Bernstein, an attorney for J.P. Morgan Chase.

Enron also got Gonzalez's permission to spend as much as \$40 million to complete construction of its office tower in Houston and as much as \$8 million for Internet access and other expenses critical to trading energy.

Firing Workers

Seeking to cut costs, Enron eliminated 4,000 jobs at its Houston headquarters, more than half its staff there. The company had about 21,000 employees at the end of September, two-thirds in the U.S., about a fifth in the U.K. and the rest in other parts of the world. It fired 1,100 workers in the U.K. last week.

Judge Gonzalez approved Enron's request to pay fired employees from \$4,500 to \$15,000 in severance.

Enron Chairman and Chief Executive Officer Kenneth Lay said he will try to keep workers who are running trading operations, which used to provide 97 percent of Enron's revenue.

Enron and at least 13 units declared bankruptcy Sunday, listing total assets of \$49.8 billion and debts of \$31.2 billion. The company's Enron Gas Liquids Inc. unit on Monday filed for bankruptcy, adding more assets to the case.

More Enron units will file for bankruptcy "in the days ahead," the company's attorney Martin Bienenstock told Gonzalez in court yesterday.

"We do not today have every 'i' dotted and every 't' crossed," in preparing the Chapter 11 reorganization, he said.

Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, December 04, 2001 12:57 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: NYT: Collapse of Enron May Reshape the Battlefield of Deregulation

December 4, 2001

BUSINESS

Collapse of Enron May Reshape the Battlefield of Deregulation

By JOSEPH KAHN and JEFF GERTH

WASHINGTON, Dec. 3 - The bankruptcy of Enron (news/quote) has Washington debating the way it oversees the \$200 billion power industry. But there is no consensus on erasing the legacy of deregulation that the company's political largess helped forge.

Congressional leaders and top regulators are moving forward on what had been Enron's No. 1 objective: a push to reduce local control of electricity transmission lines so that energy merchants like the Enron Corporation can use them to transport and sell power.

But the politics of power are shifting, and some of Enron's longstanding opponents - chief among them the Southern Company of Atlanta, which owns many local power monopolies - see a fresh chance to slow deregulation, or even roll it back.

Among those who have called for inquiries into Enron's collapse are Representative Billy Tauzin, a prominent Republican from Louisiana who is chairman of the House Energy and Commerce Committee; the Senate majority leader, Tom Daschle, and Senator Jeff Bingaman, a Democrat of New Mexico who is chairman of the Senate Energy and Natural Resources Committee.

All are vowing to get to the bottom of one of the most precipitous business reversals in history. And some members of Congress say Enron's downfall, on the heels of California's energy meltdown early this year, proves that Washington must demand more disclosure from energy traders, holding them at least to the standards of Wall Street firms.

"Enron is the sequela to California, it's all part of the one-year story line," said Representative Edward J. Markey, Democrat of Massachusetts, who focuses on energy regulatory issues in the House. "We can't leave energy products in the regulatory shadows. It hurts both investors and consumers."

Other influential officials are in no rush to turn back the clock on deregulation.

"We have had a number of false starts, and it would be crazy not to take a look at the lessons we can learn," said Nora Brownell, one of President Bush's appointees this year to the Federal Energy Regulatory Commission. "But we should not leap to the conclusion that competitive markets do not work."

The Bush administration, along with some Democrats - including Mr. Bingaman and William Massey, a Democrat on the energy commission - continue to favor plans advanced by Enron that would pry open regional electricity markets.

"We have to look carefully at the causes of consequences of Enron's collapse," Mr. Bingaman said. "But I don't see anything in this that would keep us from moving ahead with open transmission access and these types of things."

The durability of such views is a sign of how effective Enron was during the last decade in keeping Washington at bay as the company pushed to restructure the electricity industry and limit government oversight of new energy markets.

Enron and its employees were the largest contributors to President Bush's campaigns over the years, and Enron gave more money to politicians in the last election cycle than did any other energy company. Since 1993, its employees and its chairman, Kenneth L. Lay, have donated nearly \$2 million to Mr. Bush. In the 2000 election cycle, more than \$1 million was donated to federal political campaigns, most of it to Republicans.

Mr. Lay also had powerful friends. He recruited Wendy L. Gramm, the top commodities regulator in the administration of President Bush's father and the wife of Senator Phil Gramm, Republican of Texas, to serve on Enron's board in 1993. The appointment came just five weeks after Ms. Gramm helped push through a ruling at the Commodity Futures Trading Commission that exempted many energy contracts from regulation.

Last year, as Congress and the Clinton administration debated whether to exercise more oversight of the financial instruments used by Enron and other companies to trade energy contracts, Mr. Lay courted Linda Robertson, a senior Treasury official who was the department's liaison with Congress.

Ms. Robertson twice accepted paid trips to talk with company executives while she was still employed at the Treasury, her financial disclosure shows. The measure that became law, the Commodity Futures Modernization Act of 2000, specifically exempted energy trading from the regulatory scrutiny applied to brokers of money, securities and commodities.

Ms. Robertson, who became the head of Enron's Washington office, did not return a phone call seeking comment.

Last spring, when the Bush administration drafted a new national energy policy, Mr. Lay had a 30-minute meeting with Vice President Dick Cheney to discuss the report. The policy blueprint endorsed breaking up monopoly control of electricity transmission networks, an Enron goal that was spelled out in a memorandum Mr. Lay discussed during his meeting with Mr. Cheney.

Enron also had an unusual opportunity to influence Mr. Bush's choices for the Federal Energy Regulatory Commission, which oversees the markets in which Enron operates. Mr. Lay met Mr. Bush's personnel adviser, Clay Johnson, to discuss nominees. When Mr. Bush picked people to fill two vacant Republican slots on the five-member commission, both had the backing of Enron as well as other companies.

Enron did not always get its way in Washington. It failed to win regulatory exemptions for some futures products it wanted to trade, for example. And with Enron now discredited, its longtime nemeses like the Southern Company hope to turn the regulatory agenda in a direction that favors their interests.

The Southern Company has long been Enron's main challenger for influence in Washington. The company has nurtured a loose coalition of Southeast lawmakers - the Senate minority leader, Trent Lott of Mississippi, most prominent among them - in support of its view that the states should retain leeway in deciding the pace and scope of energy deregulation.

So far this year, its political action committees have outspent all other energy companies, including Enron and big oil companies like Exxon Mobil (news/quote), in supporting members of Congress, according to the U.S. Public Interest Research Group. Southern strongly opposes efforts to diminish the power of local regulators to supervise electricity pricing, production and transmission.

"We have long felt that Enron's vision of open markets does not work with electricity," said Dwight Evans, executive vice president of the Southern Company. "I think our credibility has been enhanced by recent events."

Mr. Evans said that the Federal Energy Regulatory Commission under Mr. Bush had tried to "design systems that meet what Enron needs." Congress should slow the commission, Mr. Evans argued, or risk a fresh bout of instability and volatile prices.

Some states have halted the introduction of open markets for electricity. Nevada, Oklahoma and New Mexico are among those that have put off deregulation, while California and a few other states that once promoted unfettered competition are debating ways to reimpose regulatory control.

Enron's assiduous efforts to keep its energy trading free of government interference could be another casualty of its collapse.

As the value of energy contracts soared into the hundreds of billions of dollars - at one point up to half all electricity and natural gas transactions passed through Enron's trading operation, by some estimates - Enron scrambled to hold off Congress and regulators.

But some regulatory experts now say that Enron's collapse is reminiscent of the failure of Long-Term Capital Management. Long-Term Capital was the hedge fund based in Greenwich, Conn., that operated without direct federal oversight and, by some accounts, threatened world markets when its elaborate portfolio of derivatives crumbled in late 1998.

With its exemption from scrutiny in hand, Enron revealed relatively little about its trading portfolio, leaving analysts guessing how it had made its profits. Enron's secrecy was one factor that caused investor confidence to plummet in recent weeks, after the company revealed some unorthodox financial arrangements that benefited top executives.

"Enron was getting very heavily into derivatives, and along with Wall Street banks, they went to bat to keep us away," said Michael Greenberger, who was director of trading and markets at the Commodities Futures Trading Commission until September 1999. "This should be as scary for regulators and Congress as Long-Term Capital was."

Representative Markey agreed that Congress should demand more oversight of energy trading. He said regulators should begin requiring transparency from companies like Enron, while examining the adequacy of their capital and the stability of their trading portfolio, much as banking and securities

regulators do for companies in their domain.

"We'll do it now," he said, "or we'll do it when we get the next shock."

Nickoloff, Peter

From: Carleton, Norman
Sent: Tuesday, December 04, 2001 1:01 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: Reuters: House Energy Panel Sets Enron Meetings This Week

December 3, 2001

House Energy Panel Sets Enron Meetings This Week

By REUTERS

Filed at 4:43 p.m. ET

WASHINGTON (Reuters) - A congressional panel looking into the disintegration of energy giant Enron Corp. said on Monday it would meet this week with executives from the company and representatives of the Securities Exchange Commission and auditing firm Arthur Andersen.

The meetings scheduled by the House Energy and Commerce Committee indicate the panel is moving quickly to investigate the collapse of Enron, a company which until a few weeks ago dominated U.S. natural gas and electricity markets.

The committee's chairman, Louisiana Republican Rep. Billy Tauzin, directed his staff to meet with the SEC, Enron financial auditor Arthur Andersen and top Enron executives, a panel spokesman told Reuters.

"The committee will be moving aggressively to pin down what went wrong and what, if anything, Congress can do to prevent this type of thing from happening again," said a spokesman for Tauzin.

On Tuesday, committee staff will meet with the SEC's head of enforcement and general counsel, the spokesman said.

The following day, the House panel's investigators will interview representatives of Arthur Andersen and the Financial Accounting Standards Board.

On Thursday, three committee staffers will travel to Houston to meet with top Enron officials "to begin laying the groundwork for a hearing," the staffer said. Enron Chairman Kenneth Lay was not asked by the panel to participate in the meeting, he added.

Enron filed the biggest U.S. Chapter 11 bankruptcy case in history on Sunday. The company listed assets of \$49.8 billion and debts of \$31.2 billion. Tauzin launched the House panel's investigation last Thursday.

Enron's rapid tumble began several weeks ago when news surfaced of off-balance-sheet transactions that led to a \$1.2 billion write-down in shareholder equity and contributed to a \$1 billion charge. The company's plunging share price led to a series of credit downgrades, and a failed attempt by Dynegy Inc. to rescue the company.

The Democratic-led Senate Energy Committee also plans to investigate the impact of Enron's financial troubles on the overall U.S. energy market.

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 10:33 AM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Cetina, Jill; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, HeidiLynne; Sharer, James; Whaley, Jean; Wiedman, Mark
Subject: DJ: Enron Hearing Set For Dec. 12 Before Two House Panels

December 5, 2001

Enron Hearing Set For Dec. 12 Before Two House Panels

WASHINGTON -- Two subcommittees of the House Financial Services Committee have scheduled a joint hearing next Wednesday on the collapse of Enron (ENE) and the impact on investors and financial markets.

Witnesses invited to testify at the Dec. 12 hearing include Securities and Exchange Commission Chairman Harvey Pitt, Enron CEO Ken Lay, and Arthur Andersen CEO Joe Berardino.

Issues to be examined at the Enron hearing by the Subcommittee on Capital Markets, Insurance and Government-Sponsored Enterprises and the Subcommittee on Oversight were identified by the panels as including "the impact on commodity markets, the reasons behind Enron's overstated earnings, mishandling of the employee 401(k) plan, potential securities fraud, and accounting irregularities."

Rep. Richard Baker, R-La., chairman of the Capital Markets panel, said, "It looks to me like a whole bunch of innocent people got crushed here. Obviously we've got a lot of questions. We need to find out whether the retirement savings of Enron workers and the mutual funds of a lot of other people were victims of fraud or from violations of any existing securities laws. Do we need better disclosures and accounting standards to give investors the real picture?"

"What I'd also like to know, to begin with, is how this happened, could it have been avoided, where were the warnings from the experts, and how do we avoid a similar collapse in the future?" added Baker.

-By **John Connor**, Dow Jones Newswires; 202-862-9273; John.Connor@dowjones.com

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Subject: WSJ Front Page Story on Enron (For those who don't read the WSJ and are interested)

December 5, 2001

Page One Feature

Behind Enron's Fall, a Culture of Secrecy Which Cost the Firm Its Investors' Trust

By JOHN R. EMSWILLER and REBECCA SMITH

Staff Reporters of THE WALL STREET JOURNAL

HOUSTON -- Around the beginning of October, **Enron Corp.** executives visited credit-rating-agency officials for talks about the company's third-quarter results. Those results contained what turned out to be a bombshell.

Enron mentioned in the talks that shareholders' equity, the difference between the company's assets and its liabilities, would be reduced by \$1.2 billion because of transactions with certain partnerships, says a person familiar with the matter. Some of the credit analysts, regarding this as so significant it needed to be disclosed, privately urged Enron to report it to the Securities and Exchange Commission, this person says.

But Enron didn't do so, nor did the company explain it in its nine-page earnings announcement in mid-October. The only public inkling came during an earnings-report conference call, in a reference by the company chairman so fleeting that some analysts say they missed it.

It was vintage Enron: minimal disclosure of financial information that, in retrospect, was central to understanding the complex company. Only a few months ago, Enron was wowing Wall Street with its growth and innovation, racking up large, steady earnings gains as it pioneered the global trading of everything from power to weather contracts. But virtually unseen until the end was an Enron culture that contained the seeds of its collapse, a culture of highly questionable financial engineering, misstated earnings and persistent efforts to keep investors in the dark.

Senior Enron executives flouted elementary conflict-of-interest standards. The company hired legions of lawyers and accountants to help it meet the letter of federal securities laws while trampling on the intent of those laws. It became adept at giving technically correct answers rather than simply honest ones.

One senior Wall Street official recalls recently asking Enron officials whether the company had retained bankruptcy counsel. He was told no. He later found out that while Enron hadn't formally retained such representation, it had met with bankruptcy lawyers. "If you don't ask the absolute right question, you don't get the right answer," he says. "Enron does that a lot."

Yet public trust, above all, was what Enron had to have, in order to conduct its business as a trader and party to thousands of contracts. Once doubts began to seep into the public realm, thanks partly to that mysterious hit to equity and Enron's waffling about what it meant, other suspicious Enron moves began to emerge.

The company had transactions with certain partnerships that were run by its own officers -- but treated by Enron as separate. It offered only murky and fragmented information about these partnerships. One partnership, whose existence Enron didn't reveal for four years, was part of an arrangement that inflated earnings by several hundred million dollars during that period.

And the company's debt level was much higher than it revealed, thanks to the partnerships, which allowed Enron to keep some debt off its books. Meanwhile, executives made repeated public assurances that Enron's finances and business operations were healthy, only to have those statements refuted by subsequent revelations. Ultimately, these disclosures created a crisis at Enron, sending its stock plunging and its partners and clients fleeing.

While Enron has acknowledged that a loss of investors' confidence was at the root of its woes, company officials have consistently defended their actions as legal and proper. An Enron spokesman reiterated Tuesday that the company made every effort to put out accurate information. When something was found to be inaccurate, Enron took prompt steps to correct it, the spokesman said.

On Sunday, Enron filed for bankruptcy-law protection in New York federal court -- the biggest such filing ever. It simultaneously filed a multibillion-dollar suit against a company that last week backed out of a rescue pact, rival **Dynegy** Inc. Enron's stock, which touched \$90 a share last year, closed Tuesday on the New York Stock Exchange at 87 cents.

Top officials now are the targets of some two dozen shareholder suits. They face a formal SEC investigation, a Justice Department criminal probe and congressional inquiries. The company, now struggling to avoid liquidation, has tapped existing credit facilities and lined up fresh capital exceeding \$7 billion in recent weeks, and is looking for more.

Not every detail of this tangled tale has yet been fully unraveled. It's still not clear whether concealment and financial engineering were a central strategy at Enron for years, or just a last desperate resort when earnings were falling short. Questions also still surround the sudden midsummer resignation of Chief Executive Jeffrey Skilling, whose role in Enron's collapse remains uncertain.

What is clear, though, is that rarely in the annals of American business has an enterprise so mighty and so highly regarded fallen so far so fast.

Led by its chairman, Kenneth Lay, Enron during the 1990s morphed from a nondescript gas-pipeline company into the nation's biggest energy trader, matching utilities, power suppliers and other investors in a vast unregulated marketplace. It gradually turned into a trading juggernaut that increasingly disdained long-term ownership of hard assets.

Moving far beyond energy, Enron pioneered hundreds of different types of trading contracts, ranging from commodities such as water to exotic new financial instruments. The company assembled an

immense pool of financial and trading talent among its 21,000 employees.

As Enron concentrated on trading of complex instruments, it came to resemble a vast financial-services empire, handling billions of dollars of other people's money. But to analysts and investors seeking to understand it, Enron wasn't very informative. Officials could be dismissive of inquiries, even rude. Closely questioned during a conference call last spring, Mr. Skilling called one company critic an "ah."

Many Wall Street analysts admitted to not fully understanding chunks of Enron, a company that had 3,500 subsidiaries and affiliates spread across the globe. During the booming 1990s, as Enron delivered plump earnings and stock gains, this didn't matter. Investors "were scared not to be in it," says Paul Patterson, an analyst at ABN Amro.

A Sudden Departure

The confluence of events that changed perceptions began in August with the sudden resignation of Mr. Skilling.

The former McKinsey & Co. consultant, who is 48, had become president in 1997. Last February he became CEO as well. Remaining chairman was his mentor, Mr. Lay, a friend and financial backer of President Bush and Vice President Cheney. In the early days of the Bush administration, Mr. Lay, who is 59, had been widely expected to take a cabinet post.

Messrs. Lay and Skilling made a formidable team. The courtly and amiable Mr. Lay had wide-ranging experience in government, academia and business, and his opinion was frequently sought in the energy world. Mr. Skilling, a Harvard M.B.A., was a brash, fiery figure who spoke rapidly and peppered his conversations with financial jargon.

Without warning, Mr. Skilling resigned on Aug. 14. He initially cited "personal reasons." But in an interview the next day he said his own frustration over Enron's weakening share price -- then about \$43 -- played a major role in his decision. "I don't think I would have felt the pressure to leave if the stock price had stayed up," he said.

The abrupt departure forced Mr. Lay to retake the reins. He was reassuring to the public. "I can honestly say the company is in the strongest shape it's ever been in," Mr. Lay said at the time. He also promised that in the future, Enron would be more open and accessible to investors. Mr. Lay acknowledged that the company had "lost some credibility" with investors.

Dealings With Partnerships

The day of the announcement, Enron filed its report with the SEC for the three months ended June 30. Tucked in the 36-page document were several paragraphs describing deals involving hundreds of millions of dollars between Enron and unnamed partnerships headed by and partly owned by an unnamed "senior officer" of the company. The filing added that the officer had sold his partnership interests in July and "no longer has any management responsibilities for these entities."

But it wasn't Mr. Skilling who ran the two partnerships, known as LJM Cayman LP and LJM2 Co-Investment LP. It was Chief Financial Officer Andrew S. Fastow, a Skilling protégé who was still very much with the company. The "LJM" came from the first initials of Mr. Fastow's wife and two sons. A company spokesman said the dealings between Enron and Mr. Fastow's partnerships were perfectly proper and had been done to help Enron protect its assets against fluctuating market prices.

The partnerships had been around for two years and appeared in Enron SEC filings during that time. But the manner in which they were disclosed, with different pieces of information appearing in different filings, made it difficult to learn such basics as which senior executive was running the partnerships.

Worse, there was no way from the available information to understand just what the partnerships were doing or what impact they had on Enron's finances. Some stock and credit analysts say they had never heard about the LJM's until they read about them in the newspapers in recent weeks.

Mr. Fastow's LJM dealings were, however, well-known within Enron and a magnet for criticism. Part of LJM's activities involved buying Enron assets, and some officials balked at doing deals that could enrich a senior executive at the company's expense, say people familiar with the matter. At least two senior officials complained internally about the potential conflicts of interest. The concerns were turned aside by top management, say the people familiar with the events.

The anger might have been greater had those who complained known the extent of Mr. Fastow's financial gains from LJM. Internal partnership documents show that the CFO made millions of dollars a year from LJM, far more than his corporate compensation.

One private document for LJM2's successful effort to raise nearly \$400 million boasted of "preferred access" to Enron deals and said that Mr. Fastow's economic interests would be "aligned" with the partners'. Late last year, Mr. Fastow and Enron were laying plans for a \$1 billion LJM3 fund, though it never came to fruition. Enron later estimated that Mr. Fastow made more than \$30 million from the LJM partnerships.

Mr. Fastow has declined repeated requests to be interviewed. His attorney points to Enron statements saying that all of the company's dealings with the partnerships were proper and thoroughly vetted by the board and top management.

In September, Enron faced questions from The Wall Street Journal about the partnerships. According to a person familiar with the matter, there were sharp internal disagreements over whether to make top officials available for interviews. This person says that at one point, Mr. Fastow shouted that he saw no "upside" to talking.

A Cryptic Reference

Then came Enron's Oct. 16 report of its third-quarter earnings. Although a \$1 billion write-off for telecommunications and other ventures produced a big net loss, the company trumpeted a 26% increase in "recurring earnings" due to "very strong results" of its "core" businesses. The stock posted a gain for the day.

The news release contained a cryptic reference to a charge relating to the "early termination ... of certain structured finance arrangements with a previously disclosed entity." This seemed to be Enron code for LJM. In response to questions, the company said the LJM-related charge was \$35 million.

Mr. Lay himself tried to put the LJM matter to rest. "I don't think we need to say anything more about that," he said in an interview at the time.

Later, however, an Enron SEC filing on Nov. 8 disclosed that the actual charge related to LJM dealings was \$462 million. The \$35 million figure represented cash paid to LJM in the termination, company officials now said, with the other hundreds of millions reflecting declines in the value of Enron assets held by LJM-related entities.

"It was not our intent to mislead," said Mr. Lay's chief of staff, Steve Kean, in mid-November.

On Oct. 17, the Journal revealed some of the partnerships' inner workings, their dealings with Enron and the fact that Mr. Fastow stood to make millions from his participation. Shortly afterward, Enron's stock began tumbling.

That same day, word of the \$1.2 billion reduction in shareholders' equity started rippling through Wall Street. On Oct. 18, the Journal reported for the first time that the equity reduction stemmed from transactions related to the LJM partnerships.

During the earlier discussions with credit-rating agencies, Enron had attributed the equity reduction to an "accounting error," says the person familiar with those discussions. However, in an Oct. 17 interview with the Journal, Enron Chief Accounting Officer Rick Causey didn't mention an accounting error. He said that as part of its dealing with the partnerships, Enron had put up 62 million of its own shares. In return, it gained a \$1.2 billion note receivable from the partnerships. When the arrangements were terminated, he explained, Enron simply canceled the note and retired the stock. The retirement of so many shares accounted for a \$1.2 billion reduction in shareholders' equity.

A spokesman added that Enron didn't see this as a material transaction that needed to be publicly disclosed. The spokesman Tuesday said that he had been told by company officials at the time that it was "a balance-sheet issue" and didn't need to be included in the third-quarter earnings discussion.

However, in a Nov. 8 SEC filing, Enron declared that the equity reduction was largely due to an accounting error -- one that required the company to restate prior-year financial reports.

The SEC within a few days started an informal inquiry. It soon grew into a formal investigation, which meant the agency had power to subpoena witnesses and documents. At the same time, credit-rating agencies were beginning to put Enron on review for possible downgrade.

That was worrisome. Keeping an investment-grade rating was vital for the health of the trading operation, which produced more than 90% of Enron's third-quarter operating earnings. Moreover, a fall to "junk" status would trigger accelerated repayment of billions of dollars of obligations.

Fastow Out

In an effort to stanch the bleeding and restore confidence, Mr. Lay and other top officials, including Mr. Fastow, held a conference call on Oct. 23. Sparring with analysts and investors, the executives seemed defensive and even hostile at times. Mr. Lay wouldn't let Mr. Fastow answer questions about the partnerships, but expressed his "highest faith and confidence" in his chief financial officer.

The next day, the company announced Mr. Fastow was no longer Enron's CFO. Mr. Lay said the about-face was necessary to "restore investor confidence."

After the conference call, Enron top brass retreated from the public arena. Behind the scenes, Enron was frantically looking for a rescue strategy, approaching both competitors such as Dynegy and wealthy investors such as Warren Buffett for a cash infusion. So intense was the quest that one Enron attorney, a member of the Weil, Gotshal & Manges law firm, flew from Dallas to Houston for a planned two-hour meeting and didn't get back for two weeks.

Dynegy was intrigued by the notion of taking over a company that was five times its size and had long overshadowed it. Dynegy President Steve Bergstrom, an Enron alumnus, had a scheduled

social lunch with an old friend, Stan Horton, who runs Enron's pipeline business. Mr. Horton asked if he could bring Enron Vice Chairman Mark Frevert and President Greg Whalley. In a private room at Houston's Plaza Club, Mr. Whalley popped the question: Would Dynegey be interested in buying Enron? "I was flabbergasted," says Mr. Bergstrom. "We were like the little kid on the block to them." He remembers thinking, "They're in worse trouble than I thought."

Mr. Bergstrom suggested having Mr. Lay call Dynegey Chairman and founder Chuck Watson, and within hours the two talked. Then they met face to face and privately Oct. 27 at Mr. Lay's home in Houston's exclusive River Oaks neighborhood, hammering out major points of a deal.

Dynegey's biggest shareholder, **ChevronTexaco Corp.**, approved a \$2.5 billion investment in Dynegey that Dynegey would use to give Enron a cash infusion. The first \$1.5 billion would come right away and the rest at the closing. **J.P. Morgan Chase & Co.** and Citibank arranged a further \$1 billion of credit, so that on Nov. 9, the two sides were able to announce a \$9 billion all-stock betrothal. Mr. Lay, deflecting questions about Enron's woes, said the combination "is all about the future."

But amid the optimistic talk, new bombshells were exploding at Enron. Its Nov. 8 SEC filing disclosed for the first time company dealings with an entity called Chewco Investments LP. Just four days before the filing, the company had refused requests by The Wall Street Journal to discuss the entity or even acknowledge its existence.

As it turned out, Enron had plenty of reason to be sensitive about Chewco, named for the "Star Wars" character Chewbacca. Chewco had been set up in late 1997 during a rocky period for Enron, when the company was missing its quarterly earnings targets and losing a bit of its Wall Street credibility. Prudential Securities analyst Carol Coale recalls a meeting with Mr. Skilling during this period when, she says, he promised "some strong earnings growth" in the coming quarters.

Now it's known that between 1997 and the end of last year, Enron's dealings with Chewco and a related partnership known as JEDI (for Joint Energy Development Investments) kept hundreds of millions of dollars of debt off Enron's books. Moreover, business deals with the partnerships also allowed Enron to book \$390 million in net income, roughly 13% of reported profits for the period, according to the Nov. 8 SEC filing.

Although Enron treated Chewco as an independent third party, there were lots of indications to the contrary. Chewco was managed by Michael Kopper, an Enron officer who later helped Mr. Fastow run the LJM partnerships. Early Chewco funding of \$383 million came almost entirely via Enron through loans it arranged or guaranteed.

In its Nov. 8 filing, Enron said that Chewco and JEDI should never have been treated as separate parties. Retroactively folding them back into Enron was the principal cause of a restatement that slashed Enron earnings for the prior four years by \$586 million, or 20%. The company said its financial statements for those years could no longer be relied upon.

These disclosures further rocked an already-shaken investment community. If Enron officials knowingly created and controlled Chewco as a sham third party to boost profits, they could be in violation of federal fraud statutes, says Jacob Frenkel, a former SEC attorney and federal prosecutor. At the very least, says Ronald Barone, head of Standard & Poor's energy and utility group, Chewco represented "financial engineering on the razor's edge."

Mr. Kopper, who last summer left Enron to run the LJM operation, declines to be interviewed. According to Enron, he bought out Mr. Fastow's partnership interests. A recent visit to LJM's offices, across the street from Enron's Houston headquarters, found no one willing to talk.

During the years in which Enron was issuing earnings statements it now says were incorrect, Mr. Lay, Mr. Skilling and other top executives of Enron sold hundreds of millions of dollars in Enron stock. Partly as a result, they and others face a raft of shareholder suits. Some Enron traders complained angrily at a company meeting last month about \$62 million in severance the Dynegy deal would bring Mr. Lay. After a day of giving out conflicting signals, Mr. Lay announced he wouldn't take the severance.

Revelations about Chewco and LJM fueled concern about other surprises that might be hidden in dozens of other partnerships with which Enron did business. One problem: Millions of shares of Enron stock provided the underpinnings for at least some of those partnerships. As Enron's stock price fell, the stability of those structures was threatened, says one Enron insider, who speculates that Mr. Skilling's decision to resign might have been influenced by this development. "When he saw the stock price falling, I think he knew a crisis was coming," this person says.

Mr. Skilling won't talk about Chewco or anything else having to do with Enron. Since leaving in August he has remarried, grown a beard and hired a lawyer to help handle the mess. On a recent morning, outside his newly built mansion in Houston's River Oaks neighborhood, Mr. Skilling reiterated his desire to be left alone but didn't seem angry about being approached. "I understand it's a big story," he said in a soft voice.

On Nov. 19, Enron revealed more bad news. In another SEC filing, it said it could be forced to take a further \$700 million pretax hit to earnings because of a plunge in the value of assets at yet another investment partnership. In addition, Enron said its declining credit rating had triggered \$690 million in accelerated payments to investors.

Trading partners began to back away. The stock plunged anew, falling to about \$5 a share by Thanksgiving.

One Last Effort

Dynegy executives say the Nov. 19 filing was pivotal in changing their thinking about the merger. Enron appeared to be burning through cash at a frightening rate, says Mr. Bergstrom, Dynegy's president, and it kept coming up with unpleasant surprises. "I think they knew more than they were telling," he says. Enron spokesman Mark Palmer replies that "if they had done their due diligence, they would have known about" Enron's condition.

The companies made one last stab at saving the deal over the Thanksgiving weekend, huddling at a resort in Westchester County, N.Y.

They slashed the deal's price to \$4.17 billion. But in an ominous sign for Enron, neither of Dynegy's top two executives attended. And the revised deal was never made final. Analysts estimated that at least \$4 billion more cash was needed to bolster trading partners' confidence, and no one was willing to put up that kind of money. A week ago, Enron's world caved in. Standard & Poor's, tired of waiting for the negotiations to produce a new rescue of Enron, dropped its credit rating below investment grade.

Other rating agencies followed. Later the same day, Dynegy formally called off the acquisition, and Enron traders walked away from their screens. About 4,000 Enron employees already have been laid off, with \$4,500 in severance pay. Many face a further hit as retirement accounts, heavy with Enron shares they weren't allowed to sell, are decimated. After the collapse of the merger, some of the 7,500 headquarters employees headed to Houston bars to blow off steam.

One took the time to remove Dynegy's stock symbol and stock price from the electronic tote board in the Enron lobby. Left behind was Enron's stock price, by then measured in dimes, and the constantly replaying message at the bottom of the board: "Enron ... endless possibilities."

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Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 2:42 PM
To: Bitsberger, Timothy; Gross, Jared; Pietrangeli, Fred; Berardi, Steve; Nickoloff, Peter; Schulltheiss, Heidilynne
Subject: DJ: Another Enron 'Rally' As Shorts Close Out Positions

December 5, 2001

Another Enron 'Rally' As Shorts Close Out Positions

By CHRISTINA CHEDDAR

OF DOW JONES NEWSWIRES

NEW YORK -- Even as more **Enron** Corp. (ENE) units succumb to bankruptcy, the Houston energy trader's stock has bounced up over 30% Wednesday in heavy volume.

Buyers of the stock Wednesday included professional investors and traders closing out short positions as well as some retail investors.

The movement comes even though **Enron** shares will likely be worthless by the time its bankruptcy court case is through. This is because there is a strict hierarchy that is followed in a bankruptcy proceeding, and the last in line to get paid are the common shareholders of Enron's stock.

Standing at the front of the line are the lenders who provided the company with debtor-in-possession financing. In Enron's case, this is the \$1.5 billion it received from Citigroup Inc. (C) and J.P. Morgan Chase & Co. (JPM).

Next in line are secured lenders and bondholders whose claims are backed by the company's assets. Behind them are unsecured creditors such as Enron's trading counterparties and vendors seeking to be paid.

Anything left over after all of that goes to the company's stockholders.

The original 14 **Enron** units that filed for bankruptcy on Sunday had more than \$18 billion in combined liabilities, without accounting for any of its off-balance-sheet obligations, which is what got **Enron** into trouble in the first place.

The Wall Street Journal, citing information provided by bankers involved in the process, said the off-balance-sheet liabilities could add another \$27 billion in debt.

Tuesday's bankruptcy filing by another three units of the company - **Enron** Net Works LLC, **Enron** Global Markets LC and **Enron** Industrial Markets LLC - added \$439 million in debt.

And there is no assurance, **Enron** won't make additional bankruptcy filings.

A quick look at Enron's bonds shows the skepticism in the market. Enron's bonds are trading at about 25 cents on the dollar, which means bondholders are expecting to get only partial payment for their investment, or are expecting that payment to be far off in the future.

To be sure, some investors who specialize in trading distressed stocks have been making profits on **Enron** shares as the stock popped back up. Some of these investors may have shorted Enron's stock and are buying to close out their positions.

However, some of the activity may come from amateur investors, who think that there still could be hope for a rebound.

"PG&E didn't go to zero," said Andre Meade, an analyst at Commerzbank, referring to the stock of PG&E Corp. (PCG). Burdened by debt from California's high-flying power prices, PG&E's Pacific Gas & Electric Co. unit filed for bankruptcy protection in April. "But there was a good chance its shareholders would get paid. In my opinion, Enron's equity is likely to go to zero, and even bondholders will not be paid."

Enron shares recently traded at \$1.15, up 28 cents, or 32.2%, on volume of 154.6 million compared with average daily volume of 42.2 million.

-By Christina Cheddar, Dow Jones Newswires; 201-938-5166; christina.cheddar@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 2:49 PM
To: Gross, Jared; Roseboro, Brian; Wiedman, Mark; Bitsberger, Timothy; Nickoloff, Peter; Schultheiss, Heidi; Pietrangeli, Fred
Subject: WSJ op-ed piece by CEO of Enron

December 4, 2001

Commentary

Enron: A Wake-Up Call

By Joe Berardino, a managing partner and CEO of Andersen.

A year ago, **Enron** was one of the world's most admired companies, with a market capitalization of \$80 billion. Today, it's in bankruptcy.

Sophisticated institutions were the primary buyers of **Enron** stock. But the collapse of **Enron** is not simply a financial story of interest to major institutions and the news media. Behind every mutual or pension fund are retirees living on nest eggs, parents putting kids through college, and others depending on our capital markets and the system of checks and balances that makes them work.

Our Responsibilities

My firm is Enron's auditor. We take seriously our responsibilities as participants in this capital-markets system; in particular, our role as auditors of year-end financial statements presented by management. We invest hundreds of millions of dollars each year to improve our audit capabilities, train our people and enhance quality.

When a client fails, we study what happened, from top to bottom, to learn important lessons and do better. We are doing that with **Enron**. We are cooperating fully with investigations into **Enron**. If we have made mistakes, we will acknowledge them. If we need to make changes, we will. We are very clear about our responsibilities. What we do is important. So is getting it right.

Enron has admitted that it made some bad investments, was over-leveraged, and authorized dealings that undermined the confidence of investors, credit-rating agencies, and trading counterparties. Enron's trading business and its revenue streams collapsed, leading to bankruptcy.

If lessons are to be learned from **Enron**, a range of broader issues need to be addressed. Among them:

- *Rethinking some of our accounting standards.* Like the tax code, our accounting rules and literature have grown in volume and complexity as we have attempted to turn an art into a

science. In the process, we have fostered a technical, legalistic mindset that is sometimes more concerned with the form rather than the substance of what is reported.

[Illustration]

Enron provides a good example of how such orthodoxy can make it harder for investors to appreciate what's going on in a business. Like many companies today, **Enron** used sophisticated financing vehicles known as Special Purpose Entities (SPEs) and other off-balance-sheet structures. Such vehicles permit companies, like **Enron**, to increase leverage without having to report debt on their balance sheet. Wall Street has helped companies raise billions with these structured financings, which are well known to analysts and investors.

As the rules stand today, sponsoring companies can keep the assets and liabilities of SPEs off their consolidated financial statements, even though they retain a majority of the related risks and rewards. Basing the accounting rules on a risk/reward concept would give investors more information about the consolidated entity's financial position by having more of the assets and liabilities that are at risk on the balance sheet; certainly more information than disclosure alone could ever provide. The profession has been debating how to account for SPEs for many years. It's time to rethink the rules.

- *Modernizing our broken financial-reporting model.* Enron's collapse, like the dot-com meltdown, is a reminder that our financial-reporting model -- with its emphasis on historical information and a single earnings-per-share number -- is out of date and unresponsive to today's new business models, complex financial structures, and associated business risks.

Enron disclosed reams of information, including an eight-page Management's Discussion & Analysis and 16 pages of footnotes in its 2000 annual report. Some analysts studied these, sold short and made profits. But other sophisticated analysts and fund managers have said that, although they were confused, they bought and lost money.

We need to fix this problem. We can't long maintain trust in our capital markets with a financial-reporting system that delivers volumes of complex information about what happened in the past, but leaves some investors with limited understanding of what's happening at the present and what is likely to occur in the future.

The current financial-reporting system was created in the 1930s for the industrial age. That was a time when assets were tangible and investors were sophisticated and few. There were no derivatives. No structured off-balance-sheet financings. No instant stock quotes or mutual funds. No First Call estimates. And no Lou Dobbs or CNBC.

We need to move quickly but carefully to a more dynamic and richer reporting model. Disclosure needs to be continuous, not periodic, to reflect today's 24/7 capital markets. We need to provide several streams of relevant information. We need to expand the number of key performance indicators, beyond earnings per share, to present the information investors really need to understand a company's business model and its business risks, financial structure and operating performance.

- *Reforming our patchwork regulatory environment.* An alphabet soup of institutions -- from the AICPA (American Institute of Certified Public Accountants) to the SEC and the ASB (Auditing Standards Board), EITF (Emerging Issues Task Force) and FASB (Financial Accounting Standards Board) to the POB (Public Oversight Board) -- all have important roles in our profession's regulatory framework. They are all made up of smart, diligent, well-intentioned people. But the system is not keeping up with the issues raised by today's complex financial issues. Standard-setting is too slow. Responsibility for administering discipline is too diffuse and

punishment is not sufficiently certain to promote confidence in the profession.

All of us must focus on ways to improve the system. Agencies need more resources and experts. Processes need to be redesigned. The accounting profession needs to acknowledge concerns about our system of discipline and peer review, and address them. Some criticisms are off the mark, but some are well deserved. For our part, we intend to work constructively with the SEC, Congress, the accounting profession and others to make the changes needed to put these concerns to rest.

- *Improving accountability across our capital system.* Unfortunately, we have witnessed much of this before. Two years ago, scores of New Economy companies soared to irrational values then collapsed in dust as investors came to question their business models and prospects. The dot-com bubble cost investors trillions. It's time to get serious about the lessons it taught us.

Market Integrity

In particular, we need to consider the responsibilities and accountability of all players in the system as we review what happened at **Enron** and the broader issues it raises. Millions of individuals now depend in large measure on the integrity and stability of our capital markets for personal wealth and security.

Of course, investors look to management, directors and accountants. But they also count on investment bankers to structure financial deals in the best interest of the company and its shareholders. They trust analysts who recommend stocks and fund managers who buy on their behalf to do their homework -- and walk away from companies they don't understand. They count on bankers and credit agencies to dig deep. For our system to work in today's complex economy, these checks and balances must function properly.

Enron reminds us that the system can and must be improved. We are prepared to do our part.

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 2:52 PM
To: Roseboro, Brian; Bitsberger, Timothy; Gross, Jared; Wiedman, Mark; Nickoloff, Peter; Schultheiss, Heidilynne; Pietrangeli, Fred
Subject: Letters on Berardino's op-ed

Voices

Enron's Alarm

RE: ("Enron: A Wake-Up Call") Mr. Berardino misses the point. Our financial accounting model is not broken, it is being abused. Sure Generally Accepted Accounting Principles (GAAP) are complicated, so is our economy. Focusing on historical performance is what we do in our profession; speculating on future performance is not. Personal integrity and character are what we should focus on. Companies that engage in off-balance-sheet transactions to subvert GAAP and mislead the financial community should be exposed, not praised for creating "sophisticated financing vehicles." Company executives holding equity positions in partnerships that compete with and benefit from transactions with their employer corporations are guilty of a clear conflict of interest. They should be discredited and legally pursued when they put their interests above the interests of the stockholders', whose assets they are entrusted to manage. Performing audits for clients like these can only end badly for auditors. Financial analysts who can't understand complex disclosures should admit it and get out of the business. Finally, any investor who hears the word "sophisticated" associated with an investment should immediately substitute the word "speculative," and adjust their expectations and investment strategies accordingly.

Robert L. Paretta, Ph.D., CPA

The writer is an associate professor of accounting and MIS at the University of Delaware

Mr. Berardino presents a dispassionate and reasoned response to the titanic misrepresentations of the financial circumstances surrounding the "sinking" of the good ship **Enron**. I can only believe that the style is a attempt to pre-empt outrage from investors and employees. Declaring a need for the good old boys in the accounting profession to get together on a solution after an \$80 billion dollar "error" understates the nature and magnitude of the crime. If the accounting industry knows how to reduce the misrepresentations, as stated in the editorial, then why weren't controls put in place long ago. Compare this situation to safety in manufacturing plants, where laws with teeth assure that safety issues receive appropriate management attention and capital investment, and get priority over profitability. Rather than a need for a wake-up call, I would ask: Who audits the auditors?

*Paul Haerberlen
Houston*

The accounting profession and especially the "big 5", very much influence the accounting and auditing standards. The fact that the profession has allowed the accounting and auditing standards and their practical application to spin out of control, must be the fault of the profession. The profession that it has allowed giant conflicts of interest to exist. Accountants should make sure they are not only independent, but seen to be independent, and provide an independent view which can be relied upon by third parties. If the auditing profession does not correct itself, then it must expect that others will take the lead.

*Angus McDowell
New York*

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 2:54 PM
To: Roseboro, Brian; Bitsberger, Timothy; Gross, Jared; Wiedman, Mark; Nickoloff, Peter; Schultheiss, Heidilynne; Pietrangeli, Fred
Subject: WSJ Article on Enron and Mark to Market Accounting

December 4, 2001

Heard on the Street

'Mark to Market' Accounting Is Under Increased Scrutiny

By JONATHAN WEIL

Staff Reporter of THE WALL STREET JOURNAL

With their industry's pioneer in bankruptcy court, the legions of energy companies that followed **Enron's** lead into the go-go world of commodity trading are finding their own profits and accounting practices under scrutiny as well.

What ultimately triggered the collapse of investor confidence in **Enron** were its indecipherable disclosures for related-party transactions, compounded by its admitted financial misstatements and massive off-balance-sheet liabilities. But many critics say disclosure issues of a different sort dog the financial statements of most companies that trade electricity, natural gas and the like -- with the approval of the nation's accounting-rule makers.

At issue is a technique called "mark to market" accounting, under which the Financial Accounting Standards Board has given energy traders wide discretion to include as current earnings those profits they expect to realize in future periods from energy-related contracts and other derivative instruments.

For many energy-trading companies, significant chunks of earnings in recent years have come from recording unrealized, noncash gains through such accounting entries. Often, these profits depend on assumptions and estimates about future market factors, details of which the companies don't provide. And because of the minimal disclosure standards, it is difficult for investors to assess whose assumptions might be too aggressive, or what market changes might invalidate the assumptions -- and force earnings revisions.

"Whenever there's a considerable amount of discretion that companies have in reporting their earnings, one gets concerned that some companies may overstate those earnings in certain situations where they feel pressure to make earnings goals," says ABN Amro analyst Paul Patterson, who follows energy-trading firms.

[Go]See full coverage of the rise and fall of **Enron**

Mark-to-market accounting is required whenever companies have outstanding energy-related contracts on their balance sheets, either as assets or liabilities, at the end of a quarter. For example, these could be agreements to sell electricity or buy natural gas over time at certain prices. Under the rules, companies estimate the fair values of the contracts. Quarterly changes in value -- representing unrealized, noncash gains and losses -- then are run through the companies' income statements.

One way to gauge the size of some companies' past unrealized gains is to dig through their cash-flow statements, which sometimes specify the noncash portion of trading gains. At **Enron**, unrealized trading gains accounted for slightly more than half of the company's \$1.41 billion of originally reported pretax profit in 2000 and about a third of its originally reported pretax profit of \$1.13 billion in 1999.

At **Dynegy**, unrealized gains accounted for nearly half its \$762 million in 2000 pretax profit and about half its \$227 million in 1999 pretax profit. **Dynegy** executives say there isn't anything wrong with the quality of their company's earnings. And they point to financial reports for the first nine months of 2001 showing that none of the company's reported earnings for this year came from unrealized gains.

Other energy traders whose earnings have been boosted in recent years by mark-to-market gains include American Electric Power, Duke Energy, El Paso, Entergy, Mirant, Pinnacle West Capital and Williams Cos.

How much discretion do energy traders have in valuing their contracts? The rule, pretty much, is that there aren't many rules.

For instance, during a conference last week sponsored by the FASB and the American Accounting Association, attendees were shown a hypothetical example under which the fair value of a power contract could range from \$40 million to \$153 million, depending on which assumptions of future trends were used.

And the mark-to-market rules that do exist for energy contracts were crafted in large part on approaches that **Enron** and other traders lobbied for. "We developed those rules," **Enron's** chief accounting officer, Richard Causey, said in an August interview.

Over the past three years, members of the FASB's Emerging Issues Task Force have extensively debated the subject of how to value energy-related contracts. What they have decided is that companies should be left to their own discretion, though the task force recognizes that could create problems. In a June 2000 report, for instance, the group noted that two companies in similar circumstances might apply different methods to estimate the fair value of their energy contracts, resulting in widely different valuations. "Those differences lead to the question of whether some of the methods in practice yield estimated amounts that are not representative of fair value," the report said.

The task force's chairman, Tim Lucas, says it simply is too difficult to draft a one-size-fits-all solution: "There's no one way to do it. There are various models, and we think it requires professional judgment to assess." Further, he says, requiring companies to disclose all the estimates underlying their earnings would produce disclosures so voluminous that they would be of little value.

That is in line with the industry's longtime position. In a June 2000 letter to Mr. Lucas, for instance, Mr. Causey said "the valuation process should be determined by individual companies," and the task force "should not address the valuation methodology for energy or energy-related contracts."

In its financial filings, Dynegy explains that when market-price quotes aren't available for certain long-term contracts, "the lack of long-term pricing liquidity requires the use of mathematical models to value these commitments." As a result, actual cash returns may "vary, either positively or negatively, from the results estimated."

Quoted market prices offering independent guidance on many short-term energy contracts have become more readily available in recent years. Even then, there aren't rules specifying which market quotes companies must use. For instance, should companies mark their contracts based on the "bid" price, which is the price a market maker would offer to pay for a given contract? Or should they use the "ask" price, which is the price at which a trader is willing to sell? Or somewhere in between? Currently, individual companies decide for themselves.

On most contracts for short-term deliveries of natural gas, bid-ask spreads are fairly small, about 1% or so. But even for some short-term electricity contract prices quoted on Enron's now-shuttered online trading portal, spreads of 20% were common. On contracts for short-term delivery of telecommunications bandwidth, **Enron** often posted "ask" prices that were as much as eight times the posted "bid" prices.

For other long-term derivatives, such as electricity contracts stretching 20 years or longer, market quotes don't exist. In such cases, companies are allowed to base contract valuations on their own undisclosed estimates, covering everything from future commodity prices to credit risks and discount rates.

"It would seem wise for energy companies in this highly skeptical environment to provide the disclosures necessary for financial statement readers to understand the quality of their earnings, and provide the disclosures voluntarily," says Tom Linsmeier, an accounting professor at Michigan State University.

For now, however, energy traders aren't stepping up their disclosures. Dynegy's senior vice president and controller, Michael Mott, for instance, says his company "is committed to full disclosure and to eliminate any cloudiness around these disclosures." But he says Dynegy won't disclose any information about the market assumptions or methodologies underlying the unrealized gains it has recorded over the years. He says that would place Dynegy "at a competitive disadvantage in the marketplace."

-- John R. Emshwiller contributed to this article.

Write to Jonathan Weil at jonathan.weil@wsj.com <<mailto:jonathan.weil@wsj.com>>

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 5:30 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: DJ: Enron Maintains Suspension Of Trading On Online Platform

December 5, 2001

Enron Maintains Suspension Of Trading On Online Platform

Dow Jones Newswires

NEW YORK -- **Enron** Corp. (ENE) on Wednesday maintained its suspension of business on its Internet platform EnronOnline, directing counterparties to call its trading desk if they wanted to do deals, the company said.

Enron, which continues to post prices on the system, also cut the number of products for which it put up bids and offers to 100 from 127 Tuesday and 1,700-2,000 before the company began its spiral into bankruptcy court, spokesman Eric Thode said.

The suspension and the number of products for which EnronOnline is posting prices could change daily, Thode said.

The point-and-click system, which once handled as much as a quarter of the volume in North American natural gas and power markets, is now all but ignored as the energy markets have moved on to other counterparties and other platforms. What trade is being done with **Enron** is attributed to continued efforts to flatten positions or is chalked up to companies that, on balance, owe **Enron** money.

"Certainly, on a day-to-day basis, it's evident it's significantly down," Thode said of Enron's trading activity. He wouldn't reveal precise volumes.

In the past, **Enron** pushed its traders to present aggressive bid-offer spreads for a full range of products on EnronOnline in a successful effort to win market share.

Closing down trade on the system, on which **Enron** is the counterparty to every deal, really just removes one means of doing business with the Houston-based company. The switch to telephones, however, would give **Enron** traders a choice whether to complete deals.

J.P. Morgan Chase & Co. (JPM), Citigroup Inc. (C) and Swiss banking giant UBS AG (UBS) are considering some form of a joint venture under which UBS' subsidiary UBS Warburg alone would take over Enron's trading operations, Dow Jones Newswires reported, citing people familiar with the matter.

Thode confirmed **Enron** was in talks with potential partners for a joint venture under which Enron's

trading operation could be revitalized, but wouldn't name the parties to the talks.

-By Andrew Dowell, Dow Jones Newswires; 201-938-4430; andrew.dowell@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 5:33 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamorenna (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: DJ: IN THE MONEY: Enron Needs JV Now To Up Recovery Value

December 5, 2001

IN THE MONEY: Enron Needs JV Now To Up Recovery Value

By CAROL S. REMOND

A Dow Jones Newswires Column

NEW YORK -- The race is on to save **Enron Corp.**'s (ENE) energy-trading business.

Enron and its creditors have to move quickly to try to preserve as much of the business as possible now that the Houston company has filed for bankruptcy and customers have begun migrating in droves to other trading partners and dealing platforms.

First, Enron's lead banks, J.P. Morgan Chase & Co. (JPM) and Citigroup Inc. (C), arranged for \$1.5 billion in interim financing to help **Enron** get going again. Now, they and others appear to be hustling to shore up one of Enron's most significant assets, its EnronOnline trading system.

So far, details are scant. But people familiar with the matter said that J.P. Morgan Chase & Co., Citigroup Inc. and Swiss banking giant UBS AG (UBS) are considering some form of a joint venture under which UBS' subsidiary UBS Warburg alone would take over Enron's trading operations. The joint-venture partners would share any revenues.

UBS has well-established businesses in trading and risk management, but the bank has virtually no presence in the energy trading market.

People familiar with the matter said that UBS is doing due diligence on Enron's trading operations, attempting to figure out what value, if any, could be restored to the once mighty trader.

J.P. Morgan declined to comment on the matter. A spokesman for Citigroup's Salomon Smith Barney's unit wasn't immediately available for comment.

But a person familiar with the matter said that under one option under review, UBS would take over Enron's trading business. That person said that the plan was likely to have been discussed during a UBS board meeting that took place in Zurich earlier Wednesday.

Banks Look To Get Something Back

J.P. Morgan, Citigroup, and other financial institutions have a lot riding on **Enron**, having loaned billions of dollars to a company that not so long ago dominated by far the U.S. energy trading

landscape.

Enron's bankruptcy filing is the largest in U.S. history, with more than \$31 billion in reported debt and perhaps billions more in as-yet unreported off-balance-sheet liabilities. Citing a person involved in the reorganization, The Wall Street Journal reported that Enron's top 10 bank lenders account for between \$7.5 billion and \$8.5 billion in on- and off-balance-sheet debt.

Creditors' desire to maximize recovery value and UBS's longing to take a foothold in the energy trading business could be what's behind the idea of a joint venture to revive the now moribund EnronOnline. (UBS has a relatively small \$74.3 million exposure to **Enron**, which the banking giant says is fully hedged.)

Until recently, EnronOnline accounted for 25% of all wholesale energy trading in the U.S., representing about 60% of Enron's trading volume. But as Enron's financial troubles mounted, ultimately leading to a Chapter 11 filing in New York Sunday, this crown jewel has rapidly been deteriorating.

And with trades almost at a standstill, customers have been moving to competing trading platforms like Dynegy Inc.'s DynegyDirect, TradeSpark or the Intercontinental Exchange, known as ICE. ICE said Tuesday that trading volume more than doubled in the two last weeks of November.

What's certain is that if Enron's major creditors and UBS want to resuscitate EnronOnline, they have to move quickly.

"The customer list is very ephemeral," said Art Gelber of Gelber & Associates, energy advisers and consultants in Houston. "Whomever gets enough liquidity will get it and become the chosen platform."

Gelber and others said that UBS, or any other interested parties, have the benefit of the upcoming holidays, a time when trading slows. But they say that if no new ownership is in place by the middle of January, any value to EnronOnline operations will have likely vanished forever.

Just how much of Enron's prior market share UBS would be able to reclaim is unclear. But even a portion would give the bank a sizable entry into the energy market.

It's also unclear whether UBS' interest in EnronOnline would extend to physical contracts that were also offered by the trading platform in addition to financial contracts. If so, UBS would have to quickly develop a presence in the pipeline and power-grid market in the U.S. and likely Europe. (Indeed, a big question for any Wall Street firm or bank considering an investment in energy trading is whether to simply be a broker or actually take and make physical delivery of power and other commodities.)

Energy adviser Gelber said given the relative openness of the energy industry in the U.S., it would be pretty easy for UBS to get in the physical delivery business if it chose to.

Introduced in 1999, EnronOnline is a trading platform that provided customers with price discovery and point- and-click transaction ability. The platform offers trading in natural gas, power, oil, other refined products, coal, chemicals and metals, among others. Unlike rival platforms like ICE, which merely match customers, **Enron** was a party to every transactions taking place on EnronOnline. Therein is another question: would an **Enron** joint-venture partner also want to take on counterparty risk?

Whatever firm, if any, steps in, the resulting joint venture would have to be approved by the

bankruptcy court and possibly even the Federal Energy Regulatory Commission.

-By Carol S. Remond; Dow Jones Newswires; 201 938 2074;
carol.remond@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 7:18 PM
To: Cetina, Jill; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: FT: Enron probe will examine industry-wide impact

Enron probe will examine industry-wide impact

By Gwen Robinson in Washington and Andrew Hill in New York

Published: December 5 2001 19:22 | Last Updated: December 6 2001 00:03

US lawmakers signalled on Wednesday that investigations into the Enron case would go beyond the collapse of the energy trader and dig deep into the implications for companies, markets and the accountancy profession.

Investigators from the House of Representatives energy and commerce committee - one of the most powerful congressional panels - will meet Enron officials on Thursday in Texas as part of their probe into the company, which filed for bankruptcy protection on Sunday.

Billy Tauzin, the Louisiana Republican who chairs the committee, said his investigators "intend to be very aggressive" and would begin hearings next month.

"This is just the beginning," said an official involved with the hearings. "These issues go way beyond Enron to securities law and financial markets regulation - and the role of auditors."

"Too many people were hurt by this," Mr Tauzin said, adding that he wanted to know how Enron manipulated accounting procedures and would examine the impact of the company's failure on energy markets.

Although Mr Tauzin said he could not say right away whether Congress needed to take action, an official involved with the probe predicted that "at the very least" it would lead to tighter regulation of accountants and ensure more transparency in commodities trading.

The "Big Five" accountancy firms including Andersen, Enron's auditor, issued a joint statement on Wednesday that responded to growing criticism over the the quality and objectivity of Andersen's audits and promised to react to the implications of the Enron collapse.

The energy committee, which conducted a comprehensive investigation into last year's controversy over defective Firestone tyres on Ford Explorer vehicles, is promising an equally thorough inquiry into Enron.

The committee's investigators met on Wednesday with the Financial Accounting Standards Board and senior executives of Andersen. Wednesday's talks with Enron in Texas will centre on the company's accounting procedures and its relationship with Andersen. The committee this week asked Enron and the SEC to hand over documents on the company's accounts and the SEC's investigation.

Michael Oxley, the Republican chairman of the House financial services committee, said on Tuesday

that two of its subcommittees would "move past the headlines and get the facts on Enron" in their joint hearings planned for next Wednesday.

Meanwhile, Enron continues to hive off non-core operations. PwC, which is acting as the administrator for Enron Europe, said it intended to sell the group's European metals, commodity trading and credit derivatives business, having agreed the sale of Enron Direct, the UK-based gas and power supplier, on Tuesday.

At the same time, the parent company is trying to salvage its stricken core north American trading business. UBS, the Swiss banking group and JP Morgan Chase have both registered an interest in forming a joint venture.

The latest of at least two dozen lawsuits was filed on Wednesday against Enron executives and board members, together with a request for an order to freeze their assets.

Bill Lerach, lead attorney for the new suit said: "Our investigation is revealing to us the fraud thus far disclosed was the tip of the iceberg."

Additional reporting by Elizabeth Wine and Sheila McNulty

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 7:21 PM
To: Cetina, Jill; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamorenna (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: FT: 'Big Five' back Andersen over Enron collapse

'Big Five' back Andersen over Enron collapse

By Adrian Michaels in New York and FT.com staff in London

Published: December 4 2001 20:35 | Last Updated: December 5 2001 20:28

Enron logo

The "Big Five" accountancy firms joined forces to suggest reforms to accounting standards in the light of the collapse of Enron.

In a joint statement, the firms appeared to close ranks around Andersen, Enron's auditors, by arguing "other market participants" had to "engage in self-scrutiny" over their role in the collapse of the stricken energy trading company.

KPMG, Deloitte & Touche, PricewaterhouseCoopers and Ernst & Young, together with Andersen, said the firms were committed to learning lessons from the failure of Enron. The statement came hours after Joe Berardino, Andersen's chief executive, had defended his firm's role as Enron's auditor in the affair.

According to the joint statement issued late on Tuesday night: "When businesses fail and public confidence wanes, all involved ... have a responsibility to actively seek to understand the core problems and pursue meaningful solutions. We encourage other market participants to engage in self-scrutiny and take significant steps."

The statement added: "The process of accounting standard-setting is too cumbersome and slow in today's economy. Working with others, we will find ways to streamline and modernise the system."

Andersen has faced questions over the competence and objectivity of its work for Enron, first for not raising the alarm over the company's finances, and then after it emerged that it had earned \$25m for its audit last year and \$27m for other services.

The firm is now being investigated by the Securities and Exchange Commission and faces lawsuits and a probe by its rival Deloitte Touche Tohmatsu. It could be hit by fines and bans.

Mr Berardino wrote in Tuesday's Wall Street Journal that when a client failed, Andersen sought to learn important lessons.

"We are co-operating fully with investigations into Enron. If we have made mistakes, we will acknowledge them. If we need to make changes, we will."

Mr Berardino's response, thought to be unprecedented in a case of this kind, quickly moves on to discuss failings in the financial accounting system that are making it hard for investors to judge

companies.

He said a rethink was needed of accounting standards, saying that the rules have grown too complex.

He added that the financial reporting model was broken.

"We can't long maintain trust in our capital markets with a financial reporting system that delivers volumes of complex information about what happened in the past, but leaves some investors with limited understanding of what's happening at the present and what is likely to occur in the future."

Mr Berardino also called for reform of the regulatory environment, saying standard-setting was too slow, responsibility for administering discipline too diffuse and punishment not sufficiently certain.

The scrutiny of Enron's accounting is the latest setback for the big professional services firms as they seek to reassure over perceived conflicts of interest.

Andersen, along with similar firms, says it has internal controls to prohibit such conflicts between audit and consultancy.

Nickoloff, Peter

From: Carleton, Norman
Sent: Wednesday, December 05, 2001 7:24 PM
To: Cetina, Jill; Bair, Shella; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamorena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: FT: Statement by the heads of the 'Big Five' accountancy firms on the collapse of Enron

Statement by the heads of the 'Big Five' accountancy firms on the collapse of Enron

Published: December 5 2001 13:02 | Last Updated: December 5 2001 13:21

Issued on behalf of the following:

Joseph F. Berardino, Andersen
Stephen G. Butler, KPMG
James E. Copeland, Jr., Deloitte & Touche
Samuel A. DiPiazza, PricewaterhouseCoopers
James S. Turley, Ernst & Young

"As with other business failures, the collapse of Enron has drawn attention to the accounting profession, our role in America's financial markets and our public responsibilities. We recognize that a strong, diligent, and effective profession is a critically important component of the financial reporting system and fundamental to maintaining investor confidence in our capital markets. We take our responsibility seriously.

"The issues are broad and complex. When businesses fail and public confidence wanes, all involved in the capital markets have a responsibility to actively seek to understand the core problems and pursue meaningful solutions. We encourage other market participants to engage in self-scrutiny and take significant steps.

"Working together, our five firms are committing our attention and resources to evaluate and chart a course to address issues important to investors. We are also committed to future action based on insights gained from current events.

Enhancing Financial Reporting

"We are developing specific recommendations to the SEC for improved disclosure guidance on related party transactions, special purpose entities (SPEs), and issues related to market risks, including those relating to energy contracts. We will work with the profession to submit these recommendations by the end of the year, and urge that this additional information be available to investors in 2001 annual reports.

"On a broader scale, we will work with the SEC as it begins the process of modernizing our financial reporting system, which is long overdue. Too often, financial statement disclosures are plentiful but may lack meaning. Many different streams of information - not just earnings - are needed for informed decision-making, and backward-looking financial statements delivered on a periodic basis no longer are sufficient to communicate real value and risk.

"The process of accounting standard-setting is too cumbersome and slow in today's economy. Working with others, we will find ways to streamline and modernize the system.

Enhancing Audit Effectiveness

"In light of the current challenging business environment, we are preparing an assessment of risk factors that may be important for financial statement preparers, audit committees and auditors to consider during the current reporting cycle.

"Last year, the independent Panel on Audit Effectiveness issued a comprehensive report on audit process improvements. Many of the recommendations have been put into place and the others are under active consideration. We are committed to timely implementation.

"As we learn more from the lessons of current events, we will work with others in the profession to evaluate its self-regulatory mechanism. We recognize that the profession must maintain the confidence of investors. Self-regulation is right for investors, the profession, and the financial markets, and we know that changes are needed. We will work to make the right improvements in a timely way."

Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, December 06, 2001 4:15 PM
To: Roseboro, Brian; Bitsberger, Timothy; Wiedman, Mark; Gross, Jared; Gabilondo, Jose; Sutton, Gary; Nickoloff, Peter; Schultheiss, Heidilynne; Novey, Michael; Hammer, Viva; Eichner, Matthew
Subject: CAPITAL VIEWS: New SEC Chairman Gets A 'Dingell-Gram' (Enron mentioned at end)

December 6, 2001	
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CAPITAL VIEWS: New SEC Chairman Gets A 'Dingell-Gram'

By JOHN CONNOR

A Dow Jones Newswires Column

WASHINGTON -- Perhaps inevitably, Harvey Pitt, the new chairman of the Securities and Exchange Commission, has Rep. John Dingell, D-Mich., on his case.

Dingell, the ranking minority member and former chairman of the House Energy and Commerce Committee, has been spreading apprehension if not outright terror through the nooks and crannies of the federal bureaucracy for decades with what have come to be known as Dingell-grams. Now he has fired one off to Chairman Pitt.

"On October 22, 2001, in your first speech as chairman of the Securities and Exchange Commission, you observed to an audience of accountants that the SEC 'has not, of late, always been a kinder and gentler place for accountants,'" Dingell wrote in a Dec. 5 letter to Pitt.

The missive (maybe missile is a better word) was released by the Congressman Thursday.

"After noting your representation of the AICPA (American Institute of Certified Public Accountants) and each of the Big Five Accounting firms for the past two decades, you lamented that 'somewhere along the way, accountants became afraid to talk to the SEC, and the SEC appeared to be unwilling to listen to the profession,' and you vowed that 'those days are ended,'" Dingell recounted, laying the groundwork for what came next.

"I am deeply troubled by the tone and tenor of your remarks," the Congressman said. "Your choice of words sends the wrong message to auditors, to the SEC staff, and to the investing public. Your message appears to be that the rules will not be implemented as vigorously as they should be. I trust this is not what you meant to convey and that you will correct any misunderstanding at the earliest possible time. This is critical, given the plummeting confidence of investors in the integrity of financial reporting at this time.

"You may choose to repudiate the legacy of your predecessor, Arthur Levitt," Dingell continued. "But make no mistake about it: his tenure, and that of his team on these issues - former Chief Accountant Lynn Turner and former Director of Enforcement Richard Walker - represent a high mark at the SEC in fighting financial fraud, and the standard against which you will be measured."

We'll await Pitt's full response, which no doubt will come in due course.

Having dispensed with the pleasantries or lack thereof, the Congressman served up a number of questions that he asked Pitt to consider in the course of the SEC's investigation into the Enron matter.

Dingell's first question reads as follows: "Enron Corp. set up a complex web of off-balance sheet special purpose entities. What was the underlying business purpose and substance of each of these entities and of Enron's transactions with them? Enron's current report on Form 8-K dated November 8, 2001, still does not

provide an explanation to investors, years after some of these entities were formed. How did the Securities and Exchange Commission fail to require adequate disclosures over those years?"

His second question (there are 15 in all) referenced FASB statement No. 57, "Related Party Disclosures," and wondered in part: "How did Enron avoid making these disclosures and how did Arthur Andersen fail to require adequate disclosures?"

And so on. Dingell's last question was: "Who profited from Enron's complex business structure? Where did all the money go?"

Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, December 06, 2001 4:19 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidlynnne; Whaley, Jean; Wiedman, Mark
Subject: DJ: Rep. Dingell Asks SEC For Details On Enron Partnerships

December 6, 2001

Rep. Dingell Asks SEC For Details On Enron Partnerships

Dow Jones Newswires

WASHINGTON – U.S. Rep. John Dingell, D-Mich., is asking the Securities and Exchange Commission for detailed explanations of complex derivative transactions that led to the financial collapse of **Enron Corp.** (ENE).

"Where did all the money go?" Dingell asked in a Dec. 5 letter to SEC Chairman Harvey Pitt, echoing a question on the minds of thousands of **Enron** investors who've seen billions of dollars in equity vanish virtually overnight.

"Who profited from Enron's complex business structure?" Dingell demanded.

The House Energy and Commerce Committee, where Dingell is the ranking minority member, has launched an investigation into the accounting practices of **Enron**.

Enron entered into complex derivative hedging arrangements with two private investment limited partnerships established by **Enron** executives. The transactions helped **Enron** keep its debt off its books and overstate its earnings.

"I intend to fully cooperate with and participate in (the committee's) probe, which is being conducted on a bipartisan basis," Dingell told Pitt.

Committee staff investigators traveled to Houston Thursday to meet with top **Enron** executives. Earlier in the week, the committee met with key SEC staff involved in that agency's investigation of Enron's business practices, and officials from Arthur Andersen, Enron's outside auditing firm, and the Financial Accounting Standards Board, known as FASB.

The committee plans to hold a hearing early next year delving into Enron's accounting practices, which could set the stage for a legislative response affecting corporate auditors.

In his letter, Dingell voiced concern with comments Pitt made before the American Institute of Certified Public Accountants shortly after he became SEC chairman, which the Michigan Democrat said suggested "the rules will not be implemented as vigorously as they should be."

Dingell suggested Pitt was seeking to "repudiate" the legacy of the SEC under former chairman Arthur Levitt, when the commission's record in fighting financial fraud represented a "high mark" that Pitt's tenure will be measured against.

"I trust that this is not what you meant to convey and that you will correct any misunderstanding at the earliest possible time," Dingell wrote.

"I expect you and your agency to conduct a vigorous and fair investigation of the **Enron** matter and of any and all other matters involving your former clients," Dingell said, noting that Pitt, as an attorney in private practice, represented the AICPA and the Big Five accounting firms.

Dingell noted that **Enron** failed to disclose and describe the nature of its relationship with the private investment partnerships, apparently in violation of FASB's standard No. 57 addressing "related-party disclosures."

"How did **Enron** avoid making these disclosures and how did Arthur Andersen fail to require adequate disclosures?" Dingell demanded of the SEC.

"It does not appear to be that Andersen was misled by management fraud, as the disclosures in prior filings should have alerted Andersen to the existence of these transactions. This appears to be similar to Andersen's behavior in Waste Management Inc. (WMI), where Andersen identified issues during the audit, but then failed to require the company to correct them," the letter said.

Noting that Andersen received \$52 million in fees from **Enron** last year for auditing and consulting services, Dingell asked: "Could that million dollars a week have played a role in their clouded judgment here?"

The letter went on to ask the SEC for details regarding what third parties the partnerships did business with, how Enron's board and internal oversight committees approved of the transactions, why past auditing adjustments weren't recorded, how the capitalization structure of the partnerships evolved, and why Andersen allowed "improper accounting" practices to help **Enron** misstate its equity by \$1 billion.

Citing Enron's SEC filings, the partnerships were established to enrich company management, hide debt from investors, and create "fictitious profits," Dingell suggested.

"Did Andersen help **Enron** 'financially engineer' these types of transactions to get around the accounting rules?" Dingell asked the SEC. "What law firms or firms were involved in structuring or engineering, and providing legal opinions, with respect to these entities, transactions and disclosures?"

Dingell asked the SEC to explain any patterns of insider stock selling in late 2000 and early 2001 that may have been related to management's knowledge of Enron's true financial condition.

The letter also sought the SEC's suggestions for what reforms of accounting rules may be needed.

-By Bryan Lee, Dow Jones Newswires; 202-862-6647;
Bryan.Lee@dowjones.com

Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, December 06, 2001 4:23 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: DJ: Judge Mulls Freezing Accts Of 29 Enron Officers, Directors

December 6, 2001

Judge Mulls Freezing Accts Of 29 Enron Officers, Directors

Dow Jones Newswires

HOUSTON -- A law firm representing Amalgamated Bank said a judge will consider freezing the accounts of 29 officers and directors of **Enron Corp.** (ENE) accused of fraud at a hearing on Friday.

Amalgamated Bank filed a lawsuit Wednesday against **Enron**, alleging that through "false and misleading" financial reports and statements, certain officials - including **Enron** Chief Executive Kenneth Lay, former CEO Jeffrey Skilling, and former Chief Financial Officer Andrew Fastow - pumped up Enron's stock price and took advantage of that to "dump" a total of 17.3 million shares for more than \$1.1 billion.

In a press release Thursday, Milberg Weiss Bershad Hynes & Lerach, the firm representing Amalgamated, said the judge will hear the bank's request for unusual "expedited discovery" powers to open up personal records of the 29 defendants and reveal the extent of additional liquidations and limited partnerships not currently made public.

Amalgamated Bank submitted the ex parte application for a temporary restraining order and injunction after filing the lawsuit.

Amalgamated, a union-owned bank whose Longview funds own **Enron** shares, charges it lost \$10.3 million due to the decline of **Enron** stock and bonds.

An **Enron** spokesperson wasn't immediately available for comment.

Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, December 06, 2001 4:25 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: DJ: Enron's \$1.5B DIP Loan Syndication To Start Next Week

December 6, 2001	
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Enron's \$1.5B DIP Loan Syndication To Start Next Week

By CAROL S. REMOND

OF Dow Jones Newswires

NEW YORK -- **Enron** Corp.'s (ENE) \$1.5 billion interim financing package will be marketed for syndication beginning next week.

A final term sheet for the deal, which was preliminarily approved by the bankruptcy judge who oversees Enron's reorganization on Dec. 3, is now in the process of being finalized, people familiar with the matter said Thursday.

J.P. Morgan Chase & Co. (JPM) and Citigroup INC. (C), Enron's two lead banks, have been organizing the rescue loan, known as debtor-in-possession, or DIP, financing.

That money is needed for the company to continue to operate and to protect any value left - value that could be crucial for creditors to recoup any of their losses.

Under the terms of the deal, **Enron** has already received \$250 million from J.P. Morgan Chase and Citigroup. Another \$250 million is expected to become available in the next couple of weeks, after Enron's lenders approve the company new business plan.

The final \$1 billion in funding is contingent on final approval of the court and successful syndication of the loan. Some of that last installment will be used to repay a \$550 million loan extended by Citigroup and J.P. Morgan Chase to **Enron** last month.

Although Enron's rapid fall has left a number of financial institutions exposed to the company's fiscal and accounting woes, the people familiar with the matter said they expected most syndicate players to be interested in taking on some of the DIP financing. In a loan syndication, lead lenders offload a large part of the loan onto other banks, thereby sharing the risk with the so-called syndicate group.

Most banks are willing to take on DIP lending because such exposure is senior to all other claims in bankruptcy court. DIP loans are also attractive because they carry higher interest rates.

In the case of **Enron**, DIP financing comes at a cost of 350 basis points (3.5 percentage points) over the London Interbank Offered Rate, or LIBOR. That's 100 basis points wider than the rate under which Citigroup and J.P. Morgan Chase recently loaned \$1 billion to **Enron**, which consisted of a \$550 million loan secured by Enron's Transwestern pipeline and a \$450 million loan secured by the company's Northern Natural Gas pipeline.

The final DIP package is scheduled to be approved by the bankruptcy judge on Jan. 7.

Meanwhile, J.P. Morgan Chase and Citigroup are said to continue working with UBS AG (UBS) on a plan to form a joint venture under which UBS' subsidiary UBS Warburg would take over Enron's trading operations.

Such a venture would help shore up EnronOnline which was once one of Enron's most valuable asset.

Spokesmen for J.P. Morgan Chase, Citigroup and UBS declined to comment officially. A spokesman for **Enron** wasn't immediately available.

Enron filed for bankruptcy protection on Dec. 2 after its debt was downgraded to junk status and investors and clients lost confidence in the company over accounting irregularities and off-balance-sheet liabilities. The Chapter 11 filing is the largest in U.S. history, with more than \$31 billion in reported debt and billions more in as-yet unreported off-balance-sheet liabilities.

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Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, December 06, 2001 4:26 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: DJ: US Power Markets Showing Few Scars From Enron's Fall

December 6, 2001

US Power Markets Showing Few Scars From Enron's Fall

By **JON KAMP** and **KRISTEN MCNAMARA**

of DOW JONES NEWSWIRES

NEW YORK -- U.S. electricity markets continued to hum along Thursday without **Enron Corp.**'s (ENE) formerly dominant presence, and with few signs the energy giant's sudden departure is having any impact on prices.

The unwinding of trading positions with **Enron** has caused some prices to fluctuate recently. But such trading activity has waned, and fundamental factors like weather conditions and natural gas prices have regained their place as key market drivers, traders said.

"I think everybody's done unwinding," said one power trader, who noted that Enron's Web-based trading platform wasn't showing any prices Thursday. "There's not a market open on EnronOnline."

Enron wouldn't comment on the status of its trading operations or EnronOnline Thursday.

Even in the Northeast U.S., one area where forward power prices were moved recently by Enron's troubles, prices were once again moving on normal market conditions, traders said.

"Right now, everything's back to normal," a New York trader said, with "no influence at all" from **Enron**.

Prices for Northeast electricity scheduled for delivery months from now fell late last week, as traders sought to resell power previously contracted with **Enron** into an already saturated market. Early this week, traders who had purchased electricity from **Enron** and dissolved those contracts emerged as buyers, sending prices back up. That trend seemed to end Thursday, as traders finished flattening positions with **Enron**.

Stronger natural gas futures prices bolstered so-called forward power prices in the Northeast Thursday. The price of natural gas, fuel for a growing number of power plants, is often a major influence on forward electricity markets.

The price for power scheduled for delivery in New York City during summer 2002 traded at \$72 per megawatt-hour Thursday, up \$1 from the price seen for the same contract the previous day. Prices for winter power also rose \$1 in New England, pushed up by with natural gas, to trade at \$38/MWh.

A similar increase in Midwest and Southeast forward power trading - linked by some traders to unwinding **Enron** positions - also appears over with little impact seen on prices, traders said.

Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, December 06, 2001 4:29 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: DJ: Vast Dealings With Enron Helped Diversify Risk, Some Say

December 6, 2001	
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Vast Dealings With Enron Helped Diversify Risk, Some Say

By JOE NIEDZIELSKI

OF DOW JONES NEWSWIRES

NEW YORK -- **Enron** Corp.'s (ENE) financial dealings rippled throughout global financial markets, but in some ways, the spread of risk among hundreds of institutions has softened the blow from the biggest bankruptcy in U.S. history.

At a time when many companies are putting their house in order with regards to **Enron** - for example, by disclosing bond holdings or closing out derivatives contracts - Standard & Poor's noted Thursday that credit exposure to **Enron** isn't concentrated in any one institution, country, or even industry.

Total credit exposure to **Enron** likely exceeds the \$33 billion on **Enron** Corp.'s balance sheet, but those exposures come in many forms, not all of which are equally risky, S&P said. "The good news is that while some of the exposures may be material, they do not appear, at least on the basis of initial reports, to be life threatening to any institution," the rating agency said.

The tone of S&P's remarks Thursday echoes that of some reports this week from Wall Street fixed-income firms. Merrill Lynch said almost every global financial entity has derivative contracts outstanding with **Enron**. "This is actually a positive as risk to **Enron** is spread over a large number of counterparties," Merrill said.

But what's been difficult for agencies like S&P to get at, is the full picture of Enron's exposure throughout financial markets, such as derivatives. Enron's liabilities to counterparties, or the amount it owed to third parties under derivatives contracts, was around \$18.7 billion as of Sept. 30, according to Swaps Monitor, the New York firm that tracks over-the-counter derivatives.

A lot of Enron's derivatives counterparties who didn't want to keep the full share of their **Enron** exposure on their trading books may have offloaded some of the risk in the credit derivatives market, or through surety bonds issued by insurers. That in turn created more financial contracts or synthetic bonds that use credit derivatives exposed to an **Enron** failure.

"We, by no means, have gathered the complete picture of who's holding the bag," S&P's Tanya Azarchs told Dow Jones Newswires.

Last week, S&P noted about a \$3.3 billion notional, or face value, of **Enron** credit exposure in the synthetic collateralized debt obligations, or CDOs, that it rates. In these deals, the credit risk of a portfolio of obligors is transferred to a swap counterparty and to investors who buy notes ranging from high credit quality to slightly speculative. **Enron** also was a swap counterparty on some \$3 billion face value worth of deals rated by S&P.

And **Enron** was among the more actively-traded names in the single name credit default swap market, insurance-like contracts between two counterparties that protect against defaults and other credit events like

restructuring. Estimates from CreditSights in New York put the counterparty exposure to **Enron** in the default swap market in the range of \$8 billion to \$10 billion.

But Enron's credit exposure isn't concentrated among financial institutions like it may have been at one time, S&P said Thursday.

The bonds are held mostly by insurance companies, pension and mutual funds, and CDO structures, which, in turn, may be held by insurance and banking organizations, S&P said.

Among banks, the highest exposures in dollar terms are to be found at Enron's lead banks, J.P. Morgan Chase & Co. (JPM) and Citigroup Inc. (C), S&P said. But much of that exposure is secured.

As of Thursday, the estimated direct exposure of U.S. insurers' asset portfolios to securities issued by **Enron** and its affiliates is more than \$3.5 billion, which is not likely in itself to "negatively affect" the ratings of those insurers, S&P added.

The derivatives exposures present the more "complicated and incomplete" picture. But **Enron**, prior to its demise, was a triple-B-rated counterparty, meaning that institutions on the other side required higher levels of collateral.

And S&P added that those with **Enron** exposure often sought to protect themselves by obtaining credit protection on the **Enron** name in the form of credit default swaps, letters of credit, or bank guarantees. This transferred the risk beyond the natural counterparties on derivative transactions, which are otherwise a relatively small group of companies.

"The mechanism of diversifying risk, by laying it off in a variety of markets, worked," Azarchs said.

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Sent: Thursday, December 06, 2001 4:34 PM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: DJ: POWER POINTS Special: Reconstituted Enron A Pipe Dream

December 6, 2001	
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POWER POINTS Special: Reconstituted Enron A Pipe Dream

By MARK GOLDEN and JASON LEOPOLD

A Dow Jones Newswires Column

LAS VEGAS -- The idea that **Enron Corp.** (ENE) can find the financial backing to fence off its profitable North American gas and power trading operation in a joint venture with other partners is near fantasy, energy traders and Wall Street analysts said.

The fantasy of salvation is understandable. If Enron's energy trading operation shuts down, the most valuable piece of **Enron** will be lost.

How valuable? Enough that some counterparties wouldn't mind seeing **Enron** default. One Northwest municipal utility, for example, is buying power long-term from **Enron** at prices much higher than today's market. But the utility can't walk away from **Enron** and into the cheaper market, because **Enron** continues to deliver.

"Somehow, every day, they've scraped together the power and delivered so far," a buyer for that utility said while attending an energy trader conference this week in Las Vegas. "I wish they would default someday, so we could get out of the contract."

That situation can be multiplied perhaps thousands of times. If Enron's trading operation deteriorates, the company's creditors could eventually recover even less of what they're owed.

But deteriorate it will, observers said, even if **Enron** finds backers for a new venture.

"Most counterparties seem very hesitant about doing business with **Enron** again," said Steve Fleishman, energy industry analyst for Merrill Lynch. "Financial backing would help, but lack of clarity on Securities Exchange Commission review and litigation lingers as an uncertainty."

Brute Force

Much of the strength of Enron's traders came from the brute force that big-swinging **Enron** executives encouraged in order to meet earnings growth targets. The company for a couple of years overcame huge losses in disastrous investments overseas and in telecom with ever larger bets on just three markets: North American gas, Eastern U.S. power and Western U.S. power.

Only a few senior **Enron** traders really had the power to make market calls. Those traders had excellent fundamental analysis, and they were usually right in their bets on the direction of prices. **Enron** went long Western power and gas last year as prices in those markets skyrocketed. It shorted those markets this year as demand was killed by mild weather, a recession and delayed approval of higher utility rates.

Enron's market power was so great that its positions were somewhat self-fulfilling. If a trader for another

company heard that **Enron** had started buying something, he started buying. Or at least he didn't sell, which would be like stepping in front of a moving train.

On those occasions when the market moved against **Enron**, the company allowed its senior traders to sit on positions that were losing hundreds of millions of dollars in market value, so long as the senior trader could justify his analysis. For example, when gas futures on the New York Mercantile Exchange unexpectedly started to rise in October from about \$2.25 per million British thermal units to \$3.25, **Enron** stayed short, even as its gas profit and loss statements deteriorated daily.

But **Enron** was right. Gas futures have since declined to their pre-October levels.

Unlimited Free Risk Capital

No other trading company would have allowed a trader to sit on even fraction of that position, a senior trader with a merchant energy company said. And no deep-pocketed partner, if one were to infuse an **Enron** energy trading venture with enough money to obtain an investment-grade credit rating, would allow **Enron** traders to swing for the fences as in the old days.

Enron traders had unlimited risk capital for free. No bank partner is going to provide that kind of backing, according to the senior trader (who also might not mind seeing **Enron** go away, due to some long-term gas supply contracted from the company at prices much higher than today's market).

Besides, other energy companies have learned from **Enron's** collapse that it's too risky to do so much business with one company.

"Even if it regained footing and credibility, the market will not allow another company to have 25% market share like **Enron** once did," Fleishman said. "Market share would be a fraction of the past."

Couldn't **Enron's** talented traders still turn some decent profits and keep **Enron's** current good contracts running, even if kept on a much shorter leash? After all, the company still has its trading book, talent, systems and technology.

The answer: Not likely. **Enron's** excellent market analysis was in no small part due to the information it had from its huge deal flow. Without that market information, **Enron's** ability to correctly call price directions would deteriorate.

What's more, without the ability to bully the market, **Enron's** traders may not be that good. They have little experience trading within value-at-risk limits standard at other companies, the senior trader said.

Enron may have trouble hanging on to its best traders anyway. Its senior traders have clauses in their contracts that prevent them from jumping to the competition, but speculation is that Texas' right-to-work laws could make enforcement of those clauses difficult for a company in bankruptcy.

"Time is critical, as more talent will walk out the door and trading book will shrink," Fleishman said. "I would say something needs to be announced very soon and at full speed by year end."

At the traders conference in Las Vegas, not even that glimmer of hope is evident. The most common sentiment is "**Enron's** done."

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(Jason Leopold contributed to this article.)

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From: Carleton, Norman
Sent: Thursday, December 06, 2001 4:37 PM
To: Nickoloff, Peter; Schultheiss, Heidilynne; Bitsberger, Timothy; Gross, Jared; Wiedman, Mark; Cetina, Jill; Novey, Michael; Eichner, Matthew; Hammer, Viva
Subject: DJ: Europe's 1st Exchange-Traded Weather Futures Launch Mon

December 6, 2001

Europe's 1st Exchange-Traded Weather Futures Launch Mon

By **MARK LONG**

OF DOW JONES NEWSWIRES

LONDON -- The first exchange-traded weather futures in Europe start trading Monday, adding to the host of products that are springing up around deregulating energy and agricultural markets in the region.

The London International Financial Futures and Options Exchange, or Liffe, said Thursday that it acknowledged activity will be modest on the first day, but it remains confident that energy and insurance companies will boost liquidity and encourage interest from other sectors down the line.

Liffe said last month that it was to launch the first exchange-based weather futures market on Dec. 10 in order to provide a means for the many industries affected by weather to manage risk.

The U.K. Meteorological Office suggested last month that U.K. firms could save more than GBP7.6 billion a year if they were able to fully mitigate the effects of weather on their business, according to Liffe's Thursday briefing for reporters.

The initial listing of six Liffe weather futures contracts will be settled against the monthly and winter season indexes which Liffe introduced earlier this year.

The Liffe monthly weather indices are based on the mean of the daily average temperature for every calendar day of the month for each of three locations: London Heathrow, Paris Orly and Berlin Tempelhof. The index is expressed from a basis of 100 to ensure positive figures.

For the monthly weather futures contracts, twelve delivery months will be available at any one time and the first delivery months available to trade will be January to December 2002, inclusive.

For winter season contracts, two delivery months will be available starting with winter 2002, stretching from November-March.

The Liffe weather futures contracts are valued at GBP3,000, or EUR3,000, per one degree change. The tick size is 0.01, or one hundredth of a degree Celsius, giving each tick a value of GBP30 or EUR30.

So, a U.K. company could buy 50 lots of the January contract at 105 to hedge against warmer weather. If the January temperature is two degrees warmer than average - making the index 107 - the company would make GBP300,000. (50 lots times 200 index points times GBP30.) This could help offset, for example, a lower price received for the electricity it wanted to sell in the same timeframe.

The contracts will be cleared through the London Clearing House, "which gives a great deal of comfort to those market participants," said Ian Dudden, director of non-financial products for Liffe.

Exchanges all over the energy and commodities sectors have been quick to point out the higher credit quality

they offer relative to over-the-counter participants like **Enron Corp.** (ENE), which spectacularly collapsed last week leaving many of its counterparties badly exposed.

While energy and insurance companies are expected to dominate early weather trading activity, the retail, travel and tourism, agricultural and leisure sectors are expected to follow suit.

In addition, products more tailored to specific market sectors, based on the Liffe trading system, may be designed by others in the future, Dudden said.

There is no intention to have larger participants acting as market makers in weather futures initially, Dudden said, adding the exchange will be constantly evaluating the response to the trading system and adjusting methods accordingly.

Also, Liffe will seek to add additional weather trading markets in the U.S. and Asia. These markets would likely have summer season contracts in addition to winter season contracts.

"This is really about building the market," Dudden said. "As we do that it'll become more and more apparent where we need to channel our energies. This is not the sort of market where you can dip one toe in and then jump right out again."

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Sent: Thursday, December 06, 2001 4:39 PM
To: Bitsberger, Timothy; Gross, Jared; Wiedman, Mark; Nickoloff, Peter; Schulltheiss, Heidilynne

December 6, 2001	
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TradeSpark Adds Energy Products After Enron's Collapse

NEW YORK -- TradeSpark LP, an electronic marketplace for energy, has added hourly power and balance-of-the-day instruments to its product suite, spokeswoman Deanna Cox said Thursday.

The Internet-based trading platform is initially offering on-peak and off-peak physical hourly power instruments for all 24-hour periods at major interconnects within the West Coast, Mid-Continent and South regions. It's also offering on-peak and off-peak financial hourly power, including balance-of-the-day strips, for all 24-hour periods at major East Coast interconnects, Cox said.

"The market is becoming increasingly interested in and dependent on electronic multilateral platforms like TradeSpark, and we believe that the addition of these products will be one more reason customers will come to us to execute their trades," TradeSpark Managing Director Mike Williams said in a release.

TradeSpark and other online competitors of **Enron** Corp.'s (ENE) EnronOnline platform have expanded product offerings as Enron's troubles deepen. Questions arose in October about Enron's creditworthiness, leading to the collapse of its share price last week. **Enron** filed for bankruptcy protection Sunday. It suspended trade on EnronOnline this week.

TradeSpark competitors IntercontinentalExchange and the New York Mercantile Exchange have seen their energy volumes grow as traders move business over from EnronOnline.

TradeSpark is a partnership formed by eSpeed Inc. (ESPD), Cantor Fitzgerald LP, Coral Energy, Dominion Resources Inc. (D), Koch Energy Trading Inc., TXU Corp. subsidiary (TXU) TXU Energy Trading, and Williams Cos.' (WMB) Williams Energy Marketing and Trading Co. unit.

Active TradeSpark marketplace participants include Dynegy Inc. (DYN) and Entergy Corp. (ETR).

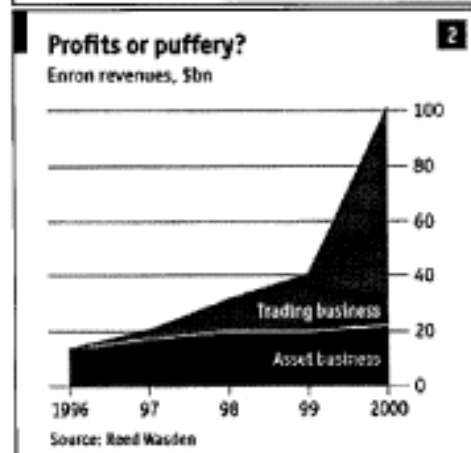
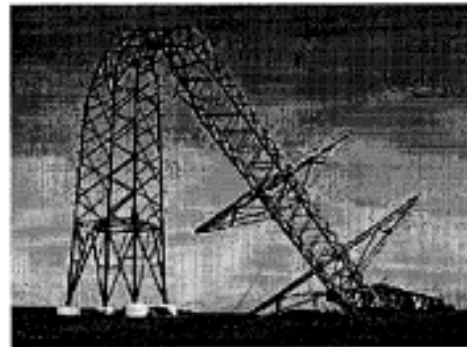
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Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, December 06, 2001 4:51 PM
To: Sharer, James; Cetina, Jill; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamorenna (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: Economist Magazine: Enron -- The amazing disintegrating firm

Enron

The amazing disintegrating firm



From The Economist print edition

The tragedy of one company's rise and fall

PRECISELY a year ago, Enron unveiled its master plan for domination of the universe. Not content with changing from an obscure gas-pipeline concern into the world's biggest energy trader, Enron's bosses set their sights higher. Jeffrey Skilling, then president, vowed to skyrocket past ExxonMobil to become the world's leading energy firm—quite an ambition, given that Exxon had just posted a quarterly profit of over \$4 billion. But even that was not enough for Mr Skilling. He had a business insight so powerful that it

would transform Enron into the world's leading company, period: the "disintegration" of the traditional corporation.

Mr Skilling believed that deregulation and market forces would force traditional, asset-heavy companies to break up into thousands of niche players. Rather than being vertically integrated, companies would be "virtually integrated"-by enterprises such as Enron that would "wire those thousands of firms back together cheaply and temporarily."

As things have turned out, it is Enron that has disintegrated. The company filed for Chapter 11 bankruptcy on December 2nd. The story behind the most spectacular corporate roller-coaster ride in memory is impossible to tell in full detail yet, thanks to the secrecy and opacity for which Enron is notorious. The principal actors involved are staying mum, though the dozens of lawsuits and official investigations now under way should eventually shine a fiery spotlight on Enron's murky doings. Even so, a rough outline is now clear.

Pride before the fall

What drove Enron into bankruptcy in what seems like just a matter of weeks? In fact, signs of trouble had surfaced much earlier. Rebecca Mark, a rising star in the 1990s, launched Enron on ill-fated forays into asset-heavy businesses overseas such as the Dabhol power project in India and Wessex Water in Britain. During the first half of this year, Enron's shares fell to around half their peak of \$90, after the firm was burned in the fallout from California's botched power deregulation and from losses on its investments in such exotica as bandwidth trading.

These events raised questions about Enron's direction under the brash Mr Skilling, who had become chief executive in February. But he disliked criticism: when, during a conference call, one analyst dared to ask a pointed question, Mr Skilling snapped that he was an "asshole". Unable to take the heat, and perhaps seeing an even worse financial crisis ahead, he unexpectedly resigned in August. That forced Kenneth Lay, the chairman, to take back day-to-day control of the company he had founded a decade and a half ago.

Shareholders hoped that the return of Mr Lay, who promised more financial disclosure, would revive Enron. But within weeks, it was mired in a financial scandal that rapidly ran out of control. By October, it was on the brink of collapse, and had to accept a most unpalatable notion: a takeover by Dynegy, a smaller energy-trading rival based down the road in Houston.

The biggest crack in the façade came with the release of third-quarter results in mid-October that showed a \$1 billion write-off on broadband, water and other bad investments. Worse, Mr Lay slipped in the news that Enron had taken a \$1.2 billion reduction in equity capital, stemming from a hedging deal with a related private-equity fund. Almost nobody outside Enron was aware of the terms of the deal with this "structured-finance vehicle", which turned out to be just one of many off-balance-sheet devices. Enron's failure to offer details about the risks from these murky partnerships led many to fear the worst about its finances.

Accounting for growth

The bad news kept coming. Enron's chief financial officer, Andrew Fastow, who had set up and profited from some of these partnerships, was pushed aside. The company restated its accounts for the past five years, and in the process wiped out nearly \$600m of profits, about a fifth of the total. The news triggered an investigation by the Securities and Exchange Commission. Yet the firm still refused to come clean. More than any actual financial liability, that obfuscation proved the last straw.

Once investors and counterparties started to doubt-even slightly-that Enron was profitable, its survival became an immediate issue. Enron had been able to raise loans because its debt was rated as investment grade; but the loans had clauses requiring Enron to make additional payments if it was downgraded. As this prospect loomed nearer, the idea of this highly leveraged company having to raise fresh money scared

off even more customers.

The proposed merger with Dynegy should have restored confidence, and thus halted the unwinding of Enron's trading book. In the event, Dynegy took a closer look inside Enron's black hole and decided not to proceed—making the downgrading of Enron's debt and its bankruptcy inevitable. Chuck Watson, Dynegy's boss, argues that even another \$1.5 billion would not have saved Enron, given the management's refusal to be open about its financial position even with its rescuer. "It is incredible that they continued in this manner...Enron never understood that business is not just about numbers and the balance sheet: it's about your brand, and the confidence you inspire."

How did Enron manage to pull off its confidence trick?

This potted history may tell what happened, but it raises a question: how did Enron manage to pull off its confidence trick? The key to understanding its collapse is contained in its annual report for 2000. The company, the report says, "is laser-focused on earnings per share (EPS), and we expect to continue strong earnings performance." EPS is a number that is watched obsessively by investors and analysts, and so is often crucial to share performance. It is also relatively easy to manipulate.

It now seems clear that growth in EPS became ever harder for Enron to deliver. So its laser focus switched to looking for accounting fiddles that would make it look as if EPS was going up, and also hide debt off its books. To that end, several off-balance-sheet entities were set up. These were not wholly independent of Enron, but were judged sufficiently separate that their profit or loss did not have to be consolidated into the company's results. Assets, or portfolios of assets, were then "sold" to these entities.

For example, swaps were created on Enron's balance sheet that would compensate the buyer of assets in the event of an unexpected loss. Sometimes the quality of the assets sold was doubtful (a block of Internet shares, say); sometimes the third-party entity would pay using a loan from Enron, which then booked the interest on the loan as income. For illiquid assets, Enron had considerable discretion in deciding what constituted a fair price. According to *Off Wall Street*, a consultancy, around 28% of Enron's EPS in 2000 came from gains on sales of securitised assets, mostly to third parties connected with Enron.

Andersen, Enron's auditors, may have allowed these transactions because they were considered too small to be material. But a combination of bigger losses to hide and the success of the disguise meant that the partnerships soon grew so big that it now seems surprising, to put it no stronger, that the auditors did not revisit their accounting treatment and legality.

The thorniest question of all is why Enron ever had to resort to these financial shenanigans. Perhaps evidence of simple, criminal activity will be found. Yet greed was surely not the only factor. Although Enron's accounts remain a black box, there are growing suspicions that even its energy-trading business—the jewel that Dynegy wanted so badly—may not have been as impressive as it seemed.

This is not to deny that Enron's traders were formidable. Harvey Padewer of Duke, an American utility that was a big rival of Enron's, concedes that "Enron had the biggest and strongest energy-trading business in North America." The company accounted for 15-20% of gas and power trading in the region. John Martin, an economist at Baylor University, reckons that the internal risk management of the trading business was basically sound.

But did high volumes really add up to big profits? At first, yes. However, partly as a result of Enron's success in expanding competitive markets, dozens of rivals flocked into trading. There proved to be few barriers to entry in energy trading; and Enron's skilled employees were snapped up in droves by rivals.

One indication of Enron's growing difficulties was the declining returns on extra revenues. Revenues grew by \$10 billion from 1998 to 1999, and then jumped by another \$60 billion to \$100 billion in 2000. Profits before tax, on the other hand, rose by \$1 billion in 1998, and by rather under \$500m in both 1999 and 2000. Enron's return on capital was only 6.6% in 2000, less than rivals such as Williams and Dynegy.

More pointedly, notes Cary Wasden of Reed Wasden, an investment firm that has long been sceptical of Enron, the firm's trading margins collapsed, from 5.3% in early 1998 to less than 1.7% in the third quarter of this year. He notes that "margins have fallen in spite of the company's practice of selling fixed assets (ie, generation plants) and booking the gains as operating revenues."

Whether Enron pumped up its trading revenues is a crucial question. As chart 2 shows, the spectacular growth of the past year or so was due almost entirely to Mr Skilling's embrace of the "disintegrated", asset-light trading model. Dean Girdis of the Petroleum Finance Company, a consultancy, points to other possible wheezes. He reckons Enron may have used limited partnerships and other financial vehicles to inflate profits. Another technique he points to is the lumping of assets such as pipelines into its trading business. In fact, profits from hard assets may have masked the shrinking margins of Mr Skilling's virtual trading business and encouraged him to bet the company on his radical, risky view that Enron could create markets in just about anything.

With margins shrinking, Mr Skilling tried to stretch the brand into new areas. Enron grew to have contracts with some 8,000 counterparties, in hundreds of business lines ranging from credit insurance to metals trading. In practice, this meant taking ever bigger bets, such as trading telecoms bandwidth.

As these bets started to go horribly wrong all at once, Enron may have felt compelled to pump up its revenues and profits using ever more ingenious tactics. Dynegy's Mr Watson puts it this way: "Enron tried to be a worldwide commodities broker and market maker to the world, open 24 hours a day, with just a BBB rating, unlike banks, which have a much stronger balance sheet-and the market fell for it."

The limits to markets

In one sense, the saga is far from over. In bankruptcy, Enron can borrow from banks, which know that fresh loans will be senior to old ones. The plan now seems to be to sell what assets it can (the ownership of its main gas pipeline is disputed by Dynegy), so as to keep alive the core trading business and the Internet operation, EnronOnline <<http://www.enrononline.com>>, perhaps with a view to selling them to a bank.

Yet it looks unlikely that Enron can stay alive, even in truncated form. A buyer of its trading and online operations would surely ditch such a besmirched brand. In any case, the company may be crippled by lawsuits that are likely to drag on for years. A better strategy for a would-be buyer might simply be to hire away Enron's best staff and start a new business.

That points to the most ironic twist of all in this morality tale. Mr Lay had always described himself as "passionate about markets". That fervent belief in the invisible hand led him to spot one of the most powerful trends of the past decade: the deregulation of commodity markets. He would often forge ahead fearlessly into newly deregulating markets, bully recalcitrant regulators into speeding reforms and develop clever financial vehicles that pressed to the very edge of the law. In the end, though, Enron appears to have overstepped the mark. The resultant backlash comes as a bitter reminder that the market forces that Mr Lay once worshipped can prove a double-edged sword.

Nickoloff, Peter

From: Carleton, Norman
Sent: Thursday, December 06, 2001 5:48 PM
To: Sharer, James; Cetina, Jill; Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamora (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: Economist: The ripples spread

The ripples spread

Dec 6th 2001
From The Economist Global Agenda

The collapse of Enron, the world's biggest corporate bankruptcy, has created ripples through financial markets around the world. The Bank of Japan has had to step in to avert a crisis there. But rival oil companies see it as an opportunity to acquire assets on the cheap

AP



Lay is down

AS DOWNFALLS go, it has been spectacular. In February, Enron was worth \$60 billion. Its founder, Kenneth Lay, was a close friend of George Bush and his family. Now the energy trading giant has filed for the world's biggest-ever corporate bankruptcy and is fighting a host of lawsuits. But it may be too soon to bury Enron, known as the most innovative and aggressive of energy traders. On December 3rd, a day after it filed for bankruptcy following the withdrawal of a merger offer by Dynegy, a smaller rival, it had lined up \$1.5 billion in additional funding. If secured—and its key bankers, J.P. Morgan Chase and Citigroup, need to persuade other banks to join the syndicate—it could mean that the energy-trading firm survives in America. Whether the Enron name survives is another matter. Meanwhile, rivals are circling to pick up the pieces of its other businesses elsewhere in the world.

The new \$1.5 billion loan will, unsurprisingly, be secured against the company's assets. It already has a long list of unsecured creditors seeking repayment. Following approval by the New York bankruptcy court overseeing Enron, the company has received \$250m immediately. It will get another \$250m when it completes a business plan, with the rest dependent on the syndication of the loan to other banks. Whether any banks will be keen to take on new Enron debt while so many of their number are nursing write-offs, is another matter. Enron hopes that the cash injection will enable it to keep its core wholesale energy-trading business afloat while it secures other partners. J.P. Morgan Chase and UBS Warburg, both investment banks, have said that they are in talks with Enron. Citigroup has also not ruled out a trading alliance. It is vital that a deal is done soon if the trading operation is to survive. Enron's lawyers revealed that the trading operation's net equity has almost halved from \$12 billion to around \$6 billion since the crisis began in mid-October. That was when Enron failed to explain a \$1.2 billion write-down in its third-quarter earnings.

Enron was the dominant trader in the markets for energy that had been spawned by electricity deregulation in America. It bought and sold contracts on gas and electricity, among other things, and made markets in financial derivatives related to the energy markets. Increasingly, though, it traded purely

financial products, including credit derivatives. Enron, in effect, abandoned its roots as an energy provider in favour of becoming a Wall Street trader that just happened to be based in Houston, Texas-in effect, a hedge fund with a gas pipeline on the side.



Grinning and bearing it

While Enron has struggled to survive this week, its bankruptcy has created ripples in financial markets around the world. Its troubles have weighed on both equity and credit markets in the weeks since its problems first emerged in October. However, some of the problems hidden by Enron's opaque accounting are only now emerging. In Japan, there has been a near panic after it was revealed that four asset-management companies were big holders of a ¥105 billion (\$848m) bond issued by Enron. Money-market funds, of the sort where the bonds were held, are marketed as "safe" assets, and so news of Enron's imminent demise triggered massive redemptions. In the way of these things, the redemptions have run at well over the level of the holdings of the bond-they have been around ¥1,000 billion, or almost ten times the value of the bond-and the scale of redemptions forced the bonds below their face value. In addition, many Japanese banks have lent to Enron. Three admitted that their combined exposure exceeded ¥60 billion (\$485m). The Bank of Japan was forced to step in and has injected more than \$200 billion into its banking system to offset the liquidity problems arising from Enron's collapse. This is its largest ever injection of funds into the system.

The FTSE 100 index of leading stocks in London was dragged down in trading on December 3rd as it emerged that Barclays, one of Britain's biggest banks, was among those exposed to Enron, to the tune of \$126m in an unsecured loan. CSFB in London, an investment bank, has a \$70m unsecured loan, and UBS, a Swiss bank, in New York, one of \$74m. Fortis, a Belgian-Dutch financial group, said this week that it has a \$68m exposure. ABN Amro of the Netherlands and Britain's Abbey National have already admitted to chunky exposures. Investors were also worried about other banks that may not yet have disclosed their exposure to Enron, and this dragged down the whole sector.

But what has been bad news for investors and lenders has been good news for Enron's rivals, who see the giant's travails as an opportunity to pick up assets on the cheap. Centrica, a British gas utility, has bought Enron Direct, which sells gas and electricity to 160,000 small and medium-sized customers in Britain, for \$137m. PricewaterhouseCoopers, which are the administrators of Enron's European assets, are now trying to sell the company's metals, commodity trading and credit derivatives business. Dynegy will not rule out a bid for Enron's share of Europe's biggest gas-fired power station at Teeside in the north-east of England. Shell's Indian business is looking to buy Enron's liquefied natural-gas terminal there. Two other companies, Britain's BG Group and the Gas Authority of India are rumoured to be interested in the plant too, though Enron is seeking to sell the terminal along with a power plant. Enron's Australian administrators have received 18 expressions of interest in the company's electricity derivatives book.

Others see a chance to pick up business now that customers are nervous of trading with Enron. Duke Energy, an American utility and energy trader, is looking at picking up Enron's role as a market-maker in power. InterContinentalExchange, a young, electronic over-the-counter commodities market, is picking up business from EnronOnline, an electronic trading platform.

AP



Friends no more

But as Enron tries to hold on to the trading business, and sell other assets, it will be dealing with regulatory investigations, fighting off a raft of lawsuits, and pursuing one of its own. It is suing Dynegy for \$10 billion for backing out of the merger. It is also trying to stop Dynegy from exercising an option to take possession of the Northern Natural Gas pipeline, its most valuable asset. Stung by this move, on December 3rd, Dynegy countersued for the pipeline, and dismissed Enron's suit as "frivolous and disingenuous".

Enron's employees are suing the trustees of their pension plan, which invested in Enron shares, for mishandling their investments. The American labour department has also opened an investigation into the retirement plan. Congress has signalled that its planned investigation into Enron will be "very aggressive". More than 15 law firms are seeking class-action status from American courts for shareholder actions against Enron. They are also pursuing Andersen, Enron's auditors, for allegedly mis-stating Enron's finances.

The Securities and Exchange Commission (SEC), America's top securities watchdog, is investigating all of Enron's accounting, including Andersen's role. This is in addition to a separate investigation of Enron's off-balance-sheet dealings. Andersen's chief executive, Joe Berardino, tried to deflect attention from Andersen by arguing in a newspaper article that both the financial reporting model and regulation were to blame. The profession has swung behind Andersen in an attempt to shift attention from one of their own. The "Big Five" top accounting firms said that they were committed to "chart[ing] a course to address issues important to investors." The whole profession has come under scrutiny in recent years. Last year the SEC attempted to prevent auditors from offering non-audit services, but dropped the proposal after sustained lobbying by the industry.

The accountants are not the only ones who missed the signs at Enron. Ron Barone, an analyst at UBS Warburg, a bank which had extensive dealings with Enron, downgraded Enron's stock from a "strong buy" to a "hold" only when Dynegy withdrew its merger offer last week. And a fund manager at Alliance Capital Management, once Enron's biggest shareholder, admitted that it had bought shares all the way down from \$80: the stock trades well under \$1 now. "All the way down the stock looked cheap," Alfred Harrison said. He admitted that the departure of former chief executive Jeff Skilling in August after just six months for a change in lifestyle, ought to have raised a red flag. "Anytime you get something like that, you have to wonder if there was something more afoot," he observed ruefully.

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, December 07, 2001 12:47 PM
To: Bair, Shella; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamora (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark
Subject: DJ: Dynegy Files Motion To Transfer Enron Bankruptcy Case

December 7, 2001	
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Dynegy Files Motion To Transfer Enron Bankruptcy Case

By Kathy Chu
OF DOW JONES NEWSWIRES

NEW YORK -- Dynegy Inc. (DYN) filed a motion late Thursday to transfer former merger partner **Enron Corp.**'s (ENE) bankruptcy case to Houston.

The case - the largest ever in corporate history - is currently presided over by Arthur J. Gonzales in the Bankruptcy Court of the Southern District of New York.

With its court filing, Dynegy joins Enron's 401(k) plan holders and some of the energy-trading company's creditors in seeking a change of venue.

In its motion, Dynegy noted that hearing the case in the Bankruptcy Court of the Southern District of Texas would make it more convenient for creditors, the debtors and witnesses to attend the hearings.

Also, **Enron** "will not suffer any economic harm or inconvenience if this case is transferred to the district in which its headquarters and business operations are located," according to the filing. "In fact, just the opposite is true. The costs to both creditors and the debtors in terms of both time and money will be astronomical if these cases remain in the Southern District of New York."

The change-of-venue motions are scheduled to be heard by federal Judge Gonzalez in a Jan. 7 hearing.

Enron couldn't immediately be reached for comment.

The parent company, **Enron Corp.**, and almost all of its 19 units that have filed for Chapter 11 bankruptcy protection are based in Houston. But **Enron Metals & Commodity Corp.** is headquartered in New York.

Enron currently employs about 3,500 workers in Houston - after laying off 4,000 there earlier this week - and about 250 in New York.

The company's problems began two months ago when it reduced its shareholder equity by \$1.2 billion and admitted that it had moved assets and debt off its balance sheet to limited partnerships controlled by **Enron** executives. In November, the company restated more than four years' worth of financial results, cutting earnings by a total of \$586 million.

Dynegy agreed to buy the troubled company in a deal valued at more than \$9 billion, but later backed out after other financial problems were disclosed and credit-rating agencies cut Enron's notes to junk-bond status.

After filing for bankruptcy, **Enron** also filed a \$10 billion lawsuit against Dynegy. Dynegy, in return, filed a countersuit to stake its claim to a valuable **Enron** asset, the Northern Natural Gas pipeline.

The odds seem to be slightly against the transfer of Enron's bankruptcy case to Houston.

Because unit **Enron** Metals & Commodity is located in New York, the parent company has the jurisdiction to file for bankruptcy protection here, according to legal experts.

"I would give (the motions) a 30% to 40% chance of success - significant, but not a slam dunk," said Nancy Rapoport, dean of law at the University of Houston.

An alternative to moving the case to Texas would be for Judge Gonzalez to appoint an additional creditors committee to represent the interest of employees, according to Rapoport.

The U.S. Trustee Office, a division of the Department of Justice, will hold a meeting Dec. 12 to form the creditors committee - provided for under Chapter 11 law. The group will play a pivotal role in steering creditors' positions in court.

Bankruptcy experts said it's likely that one committee will be appointed at that time, and another group will be named later - in order to ensure that the interests of all parties are accounted for in what is likely to be one of the most complex bankruptcy cases ever.

Traditionally, only one official committee represents the interests of all creditors in bankruptcy proceedings.

-By Kathy Chu; Dow Jones Newswires; 201-938-5392
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Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, December 14, 2001 10:02 AM
To: Bair, Sheila; Bieger, Peter; Bitsberger, Timothy; DeMarco, Edward; Dorsey, Karen; Ellett, Martha; Ellis, Dina; Gabilondo, Jose; Gross, Jared; Huffman, Lucy; Hughes, Gerry; McGivern, Tom; McInerney, Roberta; Nickoloff, Peter; Roseboro, Brian; Salladin, Anne; Schultheiss, Heidilynne; Smith, Amy; Sutton, Gary; Tishuk, Brian; Berardi, Steve; Eichner, Matthew; Hammer, Viva; Lori Sanatamarena (E-mail); Novey, Michael; Pietrangeli, Fred; Whaley, Jean; Wiedman, Mark
Subject: Enron and Bankruptcy Bill -- ABI Website

ENRON UPDATE

Greenspan, Oxley Meet; Netting Bill Gains Support Following Enron Debacle

Federal Reserve Chairman Alan Greenspan met yesterday with key House lawmakers to discuss this year's prospects for passing legislation that clarifies corporate bankruptcy laws by allowing companies to quickly settle outstanding derivatives contracts in the event of an insolvency, Dow Jones reported. The once-obscure financial issue has gained new prominence and urgency on Capitol Hill as federal investigators sift through the mess left behind by Enron's chapter 11 bankruptcy filing. The measure allows institutions to quickly close outstanding derivatives contracts with bankrupt trading partners by netting all the losses and gains of individual contracts into one deal.

House Financial Services Chairman Michael Oxley (R-Ohio) invited Greenspan to meet with House Judiciary Chairman James Sensenbrenner (R-Wis.) after Oxley held a bruising hearing on Wednesday on financial improprieties leading to Enron's demise. Complicated, off-balance sheet transactions were the company's undoing. Its stock collapsed after a Nov. 8 announcement that the firm had overstated its net income over four years by \$569 million. Creditors are now lining up to collect on about \$40 billion in debt owed by Enron.

"Congress should not fail to enact netting legislation this year," Greenspan and Treasury Secretary Paul O'Neill wrote House lawmakers a few weeks after the attacks. "Further delays would unnecessarily place the financial system at greater risk." Lawmakers are now questioning whether the legislation, which is also attached to a broader bankruptcy bill in both chambers, could be applied to Enron's bankruptcy case if the bill passes this year. Federal securities officials said it was unclear whether they could apply new contract netting laws retroactively. Oxley hopes to get the bill passed by next week, before Congress finishes its work for 2001.

House Probe Seeks Andersen's Records On Enron Audits

The House Energy and Commerce Committee yesterday asked Arthur Andersen to provide records relating to its audits of Enron Corp., Dow Jones reported. At the same time, the committee sent a letter to former Enron Chief Executive Jeffrey Skilling, requesting an interview with committee investigators within the next two weeks. The committee also formally sought interviews with David Duncan, Andersen's partner in charge of the company's Enron account, and Andersen employees involved in the company's audits. The requests came after Joseph Berardino, Andersen's chief executive, told the House Financial Services Committee on Wednesday that the auditing and consulting firm didn't receive critical information from its client concerning the special-purpose entities that brought about Enron's

financial downfall.

Enron Seeks Supplier to Take Over California University System Powers Contract

Enron Corp is looking for another electricity supplier to complete its contract with California's two public university systems, a spokeswoman for California State University said yesterday, reported Dow Jones. Enron Energy Services Inc.'s current contract with California State and the University of California Systems expires on March 31, 2004, said spokeswoman Clara Potes-Fellow. The Enron subsidiary filed for chapter 11 bankruptcy protection Dec. 2.

Enron Contract Hearing Moved To Dec. 18

A bankruptcy court hearing regarding embattled Enron Corp.'s motion to negotiate, end or sell certain contracts has been postponed to next Tuesday, Dec. 18, Dow Jones reported. The meeting was originally scheduled for today. Earlier this week, Enron filed a motion with the court asking to be allowed to terminate with other parties certain contracts with safe-harbor provisions. The company doesn't want to ask for court approval every time it seeks to end an agreement.

In its filing, Enron had asked for authority to end some of these safe-harbor contracts and negotiate payments for each termination. Creditors, including Cinergy Corp.'s Cinergy Services Inc. and Wiser Oil Co., have filed objections. The motions and objections will be addressed at Tuesday's bankruptcy court hearing.

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, December 14, 2001 10:10 AM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark; Bieger, Peter; DeMarco, Edward; Dorsey, Karen; Ellett, Martha; Ellis, Dina; Huffman, Lucy; Hughes, Gerry; McGivern, Tom; McInerney, Roberta; Salladin, Anne; Smith, Amy; Sutton, Gary; Tishuk, Brian
Subject: DEC 13 ABI Website -- More on Enron and Bankruptcy

Enron Update

House Panel Vows Comprehensive Enron Investigation

House Financial Services Committee members yesterday plunged into what they pledged would be a comprehensive investigation into the collapse of Enron Corp., a task made more difficult by Enron Corp. CEO Kenneth Lay's failure to appear before the panel as a witness, *CongressDaily* reported. Lay sent the committee a letter on Tuesday, explaining that he would be unable to attend the hearing because he was scheduled to participate in bankruptcy proceedings. Financial Services Capital Markets Subcommittee Chairman Richard Baker (R-La.) said the committee would continue its investigation in "late January, possibly early February." And, he added, "Our task is to establish the facts, change the rules where needed and assist the SEC in pursuit of those who have violated the law."

Several lawmakers on both sides of the aisle also used Enron's demise as an opportunity to renew their calls for the passage of a financial "netting" bill, provisions of which are included in the bankruptcy reform bill. Financial Services Committee Chairman Michael Oxley (R-Ohio) and ranking member John LaFalce (D-N.Y.) agreed that Enron's collapse underscores the urgent need for passage of provisions designed to strengthen and update current statutory protections for netting financial market contracts if a party defaults. Netting refers to the practice where the amounts due between financial institutions in the event of a default are quickly calculated as one net amount, helping reduce risk. The netting language is one of the few consensus items included in comprehensive bankruptcy reform legislation that "is destined to go down to defeat," LaFalce asserted. "[Netting] is not a new issue," he fumed. "We need to extract [those] provisions and simply pass them independently."

Auditor Hints of 'Illegal Acts' at Enron

Enron Corp.'s outside auditor said yesterday "illegal acts" may have been committed at the energy-trading company before it sought bankruptcy protection last week, *The Washington Post* reported. The chief executive of Arthur Andersen, the accounting firm that approved years of financial statements that overstated Enron's profits and understated its debts, also said Andersen made "an error in judgment" that accounted for \$103 million in overstated profits.

While Joseph F. Berardino testified yesterday on Capitol Hill, giving Andersen's first substantive explanation of why it certified Enron's reports, top Enron officers detailed a reorganization strategy for creditors at a meeting in New York. And former Enron chief financial officer Andrew Fastow, after failing to honor a Securities and Exchange Commission subpoena, surfaced at a news conference to dispel speculation that he had fled the country. In addition to Congress and the SEC, the Justice and Labor departments are investigating Enron's collapse. More congressional hearings are expected next month. To read the entire story, point your browser to <http://www.washingtonpost.com/wp-dyn/articles/A34904-2001Dec12.html>.

Enron Seeks \$6 Billion From Asset Sales

Bankrupt Enron Corp. yesterday announced that it may sell its key energy trading unit and plans to raise up to \$6 billion by selling other assets, Reuters reported. Chief Financial Officer Jeff McMahon said that Enron plans to sell its troubled Azurix Corp. water unit, businesses in emerging markets and wind energy assets. It plans to retain its exploration and production unit, wholesale and retail services and regulated businesses. McMahon said Enron has about \$13 billion in unsecured bank debt and an additional \$2 billion in secured bank debt. Enron plans to raise between \$4 billion to \$6 billion with the noncore asset sale.

Dynegy Suit to Gain Enron Pipeline Moved to Federal Court

Dynegy Inc.'s lawsuit to secure ownership of an Enron Corp. pipeline company has been transferred to the Federal District Court in Houston, Dow Jones reported. The state District Court of Harris County, Texas, where Dynegy originally filed the suit, transferred the case on Tuesday. Enron asked that the suit be moved to federal court to determine whether it should be heard by the federal bankruptcy court in New York, as Enron's lawyers have argued, or in state court, as Dynegy prefers. Dynegy plans to seek to move the case back to state court.

Dynegy filed suit against two Enron subsidiaries on Dec. 3 in the state court seeking control of the Enron Northern Natural Gas Co. Dynegy based its claim to Northern Natural on an option it secured from Enron in exchange for a \$1.5 billion cash infusion. The option allowed Dynegy to acquire complete control of Northern Natural in the event Dynegy's offer to acquire Enron fell through. Dynegy terminated its acquisition offer last month and told Enron it was exercising its option to buy Northern Natural. Enron is contesting Dynegy's claim and has sued its one-time suitor for \$10 billion for wrongfully terminating its acquisition offer.

Enron Objection Deadline Extended to Dec. 18

Enron announced that it has moved the date of its next bankruptcy hearing, originally scheduled for tomorrow, to Dec. 20. Enron representatives weren't immediately available to provide the reason for the rescheduling. Enron said the hearing is designed to give adequate assurance to utility companies providing services to Enron and its debtor subsidiaries. In connection with the rescheduled hearing, Enron has extended the objection deadline to Dec. 18.

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, December 14, 2001 10:13 AM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark; Bieger, Peter; DeMarco, Edward; Dorsey, Karen; Ellett, Martha; Ellis, Dina; Huffman, Lucy; Hughes, Gerry; McGivern, Tom; McInerney, Roberta; Salladin, Anne; Smith, Amy; Sutton, Gary; Tishuk, Brian
Subject: Enron -- ABI Website Dec. 12

Enron Update

U.S. Congress to Hold First Hearing on Enron Bankruptcy Today

The first congressional hearing into the collapse of Enron Corp. gets underway today with testimony from auditors of the former energy trading giant but not the top executive of the embattled Houston-based company, Reuters reported. Enron chief executive Kenneth Lay declined an invitation to testify before the House Financial Services Committee. "We're disappointed," panel chairman and Rep. Michael Oxley (R-Ohio) said. "But this is [just] the first in a series of hearings and investigations that the committee will be conducting."

Arthur Andersen CEO Joseph Berardino will face questions about when Enron's auditors first realized there were problems with Enron's accounts. SEC Chairman Harvey Pitt, who has promised a thorough but quick probe of Enron, also declined an invitation to appear at today's hearing. Instead, SEC Chief Accountant Robert Herdman will testify. Also set to testify at the hearing is Richard Trumka, secretary-treasurer of the AFL-CIO. Oxley has said any further Financial Services committee hearings on Enron after Wednesday will not occur until 2002.

Congress Demands Records, Briefing From Enron

A congressional committee yesterday demanded that Enron Corp. hand over financial records and meet with committee staff within 10 days, according to Reuters. The House Energy and Commerce Committee called on Enron to turn over documents relevant to the committee's investigation into the company's collapse, said committee Chairman Rep. Billy Tauzin (R-La.) and Rep. James Greenwood (R-Pa). In letters sent this week to Enron Chairman Kenneth Lay, and Andrew Fastow, the company's former chief financial officer, Tauzin and Greenwood also requested staff interviews with both current and former senior Enron employees as well as members of Enron's audit and compliance committee by Dec. 21.

In their letters, Tauzin and Greenwood requested that a mountain of documents be turned over to the committee by Dec. 17. The request listed 43 separate aspects of the Enron case in which the committee has interest, including: earnings restatement decisions, financial ties among Enron officers and outside partnerships they were involved with, minutes from board and audit committee meetings from 1997 to present and correspondence between Enron auditor Arthur Andersen and the company.

J.P. Morgan Sues Enron for \$2.1 Billion

J.P. Morgan Chase & Co., one of Enron Corp.'s biggest creditors, yesterday sued the troubled energy trader for more than \$2.1 billion, Reuters reported. The New York-based bank claimed in a suit filed in the U.S. Bankruptcy Court in New York on behalf of itself and related parties that it has rights to Enron assets such as accounts receivable, commercial paper, cash, and other property, which allegedly are not protected in Enron's bankruptcy proceedings.

Enron holds the assets in dispute only as a servicer for the alleged owners, under two accounts

receivables deals, the suit claims. The assets are not property of Enron because they were sold before Enron's Dec. 2 bankruptcy filing. J.P. Morgan acted as an agent in two credit facilities whose proceeds helped fund two accounts receivables transactions between Enron and Sequoia Financial Assets, a special purpose, bankruptcy-related entity, the suit said. Sequoia allegedly bought the receivables from Enron and reinvested the money collected on the bills in short-term paper issued by Enron and its Enron North America unit.

Dynegy Files Motion to Dismiss Or Transfer Enron Case

Dynegy Inc. filed a motion on Monday asking the federal bankruptcy court in the Southern District of New York to dismiss Enron's \$10 billion breach-of-contract lawsuit against Dynegy, or, to transfer the case to Houston, Dow Jones reported. Enron's claims against its former merger partner "in no way relate to federal bankruptcy law or the administration of these chapter 11 cases," according to the filing.

Dynegy asked the New York bankruptcy court to abstain from hearing Enron's suit against Dynegy, which allegedly involves state rather than federal breach-of-contract claims. Alternatively, the case should take place in Texas - where Enron and most of its units are based - instead of New York, where the "only link to the dispute is ... hung upon the gossamer thread of the location of (Enron's) subsidiary Enron Metals and Commodity Inc."

Nickoloff, Peter

From: Carleton, Norman
Sent: Friday, December 14, 2001 10:15 AM
To: Bair, Sheila; Berardi, Steve; Bitsberger, Timothy; Eichner, Matthew; Gabilondo, Jose; Gross, Jared; Hammer, Viva; Lori Sanatamarena (E-mail); Nickoloff, Peter; Novey, Michael; Pietrangeli, Fred; Roseboro, Brian; Schultheiss, Heidilynne; Whaley, Jean; Wiedman, Mark; Bieger, Peter; DeMarco, Edward; Dorsey, Karen; Ellett, Martha; Ellis, Dina; Huffman, Lucy; Hughes, Gerry; McGivern, Tom; McInerney, Roberta; Salladin, Anne; Smith, Amy; Sutton, Gary; Tishuk, Brian
Subject: Enron -- Dec. 11 ABI Website

Enron Bankruptcy Update

Enron Japan, Affiliates Seek Bankruptcy Protection

Enron Japan Corp., a wholly-owned subsidiary of failed U.S. energy giant Enron Corp. announced that it and its three Japanese affiliates filed for bankruptcy yesterday, Dow Jones reported. The move follows Enron's Dec. 2 chapter 11 bankruptcy filing in New York. "Enron Japan Corp., Enron Japan Marketing Corp., Enron Japan Funding Corp. and E Power Corp. filed for bankruptcy...in accordance with the Japanese bankruptcy law," Enron Japan said.

Enron Court Hearing Pushed Back to Dec. 20

An Enron Corp. hearing has been rescheduled for Dec. 20 from Dec. 14, Doe Jones reported. The hearing, the second since the energy-trading company filed for chapter 11 bankruptcy protection on Dec. 2, will pertain to Enron's request to continue paying utility companies for electric bills. **Judge Arthur Gonzalez**, who is presiding over Enron's case will also hear an interim request at this time to retain Blackstone Group as financial adviser in Enron's restructuring.

600 Enron Employees Got Bonuses

Nearly 600 Enron Corp. employees deemed critical to running its prized energy trading business received more than \$100 million in bonuses last month as the company faced a merger and then bankruptcy, according to the Associated Press. About half of those bonuses, given to 75 traders in early November when Enron was planning to merge with smaller rival Dynegy Inc., may have to be repaid because the merger collapsed, said **Todd Zywicki**, a law professor at **George Mason University**.

Enron spokesman Mark Palmer said the \$50 million given to traders before the merger crumbled "was done in discussions with Dynegy to protect and preserve the value of the trading organization through what we thought was going to be a fairly long merger process." Dynegy spokeswoman Debbie Fiorito said that Dynegy didn't approve or endorse those bonuses. Enron distributed an additional \$55 million to 500 employees two days before filing for bankruptcy as an incentive for them to remain with the company while Enron works to emerge from chapter 11.