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THE ROLE OF THE FINANCIAL INSTITUTIONS IN ENRON'S COLLAPSE—VOLUME 1

HEARINGS

BEFORE THE

PERMANENT SUBCOMMITTEE OF INVESTIGATIONS

OF THE

COMMITTEE ON
GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

ONE HUNDRED SEVENTH CONGRESS

SECOND SESSION

JULY 23 AND 30, 2002

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CONTENTS

Opening statements: Page

Senator Levin 1, 161
Senator Collins 5, 165
Senator Lieberman (ex officio) 9, 167
Senator Thompson (ex officio) 11
Senator Bunning 12
Senator Carper 23
Senator Fitzgerald 45, 195
Senator Cleland 49
Senator Dayton 169
Senator Durbin 199

WITNESSES

TUESDAY, JULY 23, 2002

Robert L. Roach, Counsel and Chief Investigator, Permanent Subcommittee on Investigations; accompanied by Gary M. Brown, Special Counsel, Committee on Governmental Affairs 14
Lynn E. Turner, former Chief Accountant, Securities & Exchange Commission, Broomfield, Colorado 26
Pamela M. Stumpp, Managing Director, Chief Credit Officer, Corporate Finance Group, Moody's Investors Service, New York, New York; accompanied by John C. Diaz, Managing Director, Power & Energy Group, Moody's Investors Service, New York, New York 29
Ronald M. Barone, Managing Director, Utilities, Energy & Project Finance Group, Corporate and Government Ratings, Standard & Poor's, New York, New York; accompanied by Nik Khakee, Director, Structured Finance Group, Standard & Poor's, New York, New York 31
Jeffrey W. Dellapina, Managing Director, JPMorgan Chase Bank, New York, New York; accompanied by Donald H. McCree, Managing Director, J.P. Morgan Securities, Inc., New York, New York; and Robert W. Traband, Vice President, JPMorgan Chase Bank, Houston, Texas 58
David C. Bushnell, Managing Director, Global Risk Management, Citigroup/Salomon Smith Barney, New York, New York 92
Richard Caplan, Managing Director and Co-Head, Credit Derivatives Group, Salomon Smith Barney North American Credit/Citigroup, New York, New York 94
Maureen Hendricks, Senior Advisory Director, Salomon Smith Barney/Citigroup, New York, New York 96
James F. Reilly, Jr., Managing Director, Global Power & Energy Group, Salomon Smith Barney/Citigroup 97

TUESDAY, JULY 30, 2002

Robert Furst, former Managing Director, Merrill Lynch & Co., Dallas, Texas .. 171
Schuyler Tilney, Managing Director, Global Energy & Power, Global Markets & Investment Banking, Merrill Lynch & Co., Houston, Texas 172
G. Kelly Martin, Senior Vice President and President of International Private Client Division, Merrill Lynch & Co., New York, New York 173

Page

ALPHABETICAL LIST OF WITNESSES

Barone, Ronald M.:
Testimony 31
Prepared statement with attachments 282
Brown, Gary M.:
Testimony 14
Bushnell, David C.:
Testimony 92
Prepared statement 316
Caplan, Richard:
Testimony 94
Prepared statement 323
Dellapina, Jeffrey W.:
Testimony 58
Prepared statement 312
Diaz, John C.:
Testimony 29
Prepared statement with an attachment 278
Furst, Robert:
Testimony 171
Prepared statement 337
Hendricks, Maureen:
Testimony 96
Prepared statement 330
Khakee, Nik:
Testimony 31
Prepared statement 282
Martin, G. Kelly:
Testimony 173
Prepared statement 339
McCree, Donald H.:
Testimony 58
Prepared statement 312
Reilly, James F., Jr.:
Testimony 97
Prepared statement 334
Roach, Robert L.:
Testimony 14
Prepared statement with attachments 215
Stumpp, Pamela M.:
Testimony 29
Prepared statement with an attachment 278
Tilney, Schuyler:
Testimony 172
Prepared statement 338
Traband, Robert W.:
Testimony 58
Prepared statement 312
Turner, Lynn E.:
Testimony 26
Prepared statement 265

EXHIBITS

Page

VOLUME 1

Exhibits for July 23, 2002

101. *Enron Prepays,* chart prepared by the Permanent Subcommittee on Investigations 351
102. *Financial Institution Knowledge of Enron Prepays,* chart prepared by the Permanent Subcommittee on Investigations 352
103. *Finance Related Asset Sales, Prepays and 125 Sales ($MM)* (*Source:* August 2001, Enron Corp. Finance Committee Presentation.) 353
ASF—Detail on Prepays, chart prepared by Enron Corp. 354
104. *Impact On Year 2000 Enron Credit Ratios from 1) Adding Outstanding Prepays to Debt, and 2) Deducting Prepays from "Funds Flow From Operations,"* chart prepared by the Permanent Subcommittee on Investigations 355
Impact On October 2001 Enron Valuation from Adding Outstanding Prepays to Debt, chart prepared by the Permanent Subcommittee on Investigations 356
105. *Chase/Mahonia,* chart prepared by the Permanent Subcommittee on Investigations 357
106. *Chase/Mahonia Collapsed into Loan,* chart prepared by the Permanent Subcommittee on Investigations 358
107. *Yosemite I (Citigroup),* chart prepared by the Permanent Subcommittee on Investigations 359
108. *Yosemite I (Citigroup) Collapsed into Loan,* chart prepared by the Permanent Subcommittee on Investigations 360
109. Enron Corp. Bank Presentation, November 19, 2001, Waldorf Astoria, New York, NY, *Debt Issues: Commodity Transactions with Financial Institutions,* 361
110. *Project 10, Due Diligence Findings, November 7, 2001, Prepays,* prepared by Citigroup 363
111. *What Are Prepays? Why Does Enron Enter Into Prepays?,* presentation charts prepared by Enron Corp. 365
112. *Prepaid Transactions Discussion,* presentation materials prepared by Arthur Andersen 367
113. *Prepay Transaction,* memo prepared for Enron Corp. by Arthur Andersen, June 1999 375
114. Andersen email, December 1998, re: *Cash vehicles* 379
115. *Why Enron Prepays Were Sham Transactions,* chart prepared by the Permanent Subcommittee on Investigations 380
116. *Enron Corp. Credit Conference, Credit Profile, January 29, 2000,* presentation charts prepared by Enron Corp. 381
117. *The Ownership of Mahonia Limited,* chart provided by JPMorgan Chase 393
118. Correspondence between Mourant du Feu & Jeune ("Mourant") and Jersey Financial Regulators, re: establishment of Mahonia; and Jersey incorporation documents 394
119. Mourant email, November 2001, re: *Mahonia et al—Enron trades* 410
120. Mourant—JPMorgan Chase email, March 2002, re: *mahonia pipeline imbalances* 411
121. JPMorgan Chase email, July 2002, re: *Restructuring existing prepays* 412
122. Mourant—JPMorgan Chase email, September 2001, re: *Prepay Docs* 413
123. JPMorgan Chase email, November 1998, re: *Pre-pays* 414
124. JPMorgan Chase email, June 1998, re: *Enron Forward Sale Transaction* 415
125. JPMorgan Chase call memo, June 1999, re: *RED ALERT* 416

Page

126. JPMorgan Chase email, June 1999, re: *Enron (. . . the business purpose underpinning the current $500MM prepay exercise is simply that of efficiently priced funding.)* 417
127. JPMorgan Chase email, May 2000, re: *Enron (. . . pricing of an amortizing swap.)* 418
128. JPMorgan Chase email, July 1998, attaching copy of *Prepay pitch presentation* 419
129. JPMorgan Chase email, December 2000, attaching *Description of Enron Prepay Transaction* 433
130. Enron Corp. email, September 2001, re: *Chase Prepay (We need your help to come up with a custom amortization schedule/volume schedule that looks like a "normal commodity swap.")* 435
131. Enron Corp.-JPMorgan Chase email, September 2001, re: *Prepay* with copy of *Chase $350 Million Prepay* diagram 436
132. JPMorgan Chase email, October 2001, re: *Enron ($5B in prepays!)* 438
133. JPMorgan Chase email, November 2001, re: *Enron Exposure* 439
134. Correspondence from JPMorgan Chase to the Permanent Subcommittee on Investigations, dated July 18, 2002, regarding names of J.P. Morgan Chase & Co. clients and counterparties that engaged in commodity prepaid forward transactions with a special purpose vehicle 441
135. *Security Agreement between Mahonia Limited and The Chase Manhattan Bank,* December 1997 442
136. Excerpts of Enron Corp 10K for 2000 465
137. JPMorgan Chase email, November 2000, re: *Call Report for Enron North America Corporation* 474
138. *Structuring Summary, Enron Corp.—1996 Prepay* 476
139. *Structuring Summary, Enron Corp.—1997 Prepay* 482
140. *Structuring Summary, Enron Corp.—1998 Prepay* 490
141. JPMorgan Chase, October 1997, re: *Enron Exposure $350MM Prepaid.* ... 491
142. JPMorgan Chase email, December 2000, re: *Enron Prepay Transaction (. . . need to form Mahonia III . . .)* 492
143. Correspondence from JPMorgan Chase to four Members of the U.S. House of Representatives, dated March 27, 2002, regarding Enron and Mahonia 493
144. *Global Loans Approval Memorandum,* December 21, 1998, prepared by Citicorp 513
145. Citigroup email, September 2000, re: *My take on how to explain ECLN* .. 523
146. Citibank presentation, Enron: *Yosemite funded prepaid* 524
147. Enron Interoffice Memorandum from Tax Planning Department, January 10, 2000, re: *Yosemite I Withholding* 529
148. *Walk Through of Prepay,* charts prepared by Enron Corp. 537
149. *Yosemite Funds Flow Diagram,* chart prepared by Enron Corp. 543
150. Facsimile from Maples and Calder to Citibank, dated November 2, 1999, re: *Delta Energy Corporation (the "Company")* 544
151. *New Account Information,* Delta Energy Corporation, September 1994, prepared by Citicorp 545
152. Correspondence from The Givens Hall Bank to Citibank, N.A., February 1999, re: *Delta Energy Corporation and Vega Energy Corporation fee notes* 548
153. Delta Energy Corporation Resolutions, June 26, 2001 550
154. Citibank email, May 2001, re: *prepaid script between Citibank/Enron/Delta* 552
155. *Global Loans Approval Memorandum,* September 19, 1999, prepared by Citibank (Truman) 553
156. Enron Corp. email, November 2001, re: *an investor spoke to someone at citi and received info on delta. . . . We need to shut this down.* 559
157. *Yosemite Update; Optional Use as Prepay Funding Vehicle,* Enron presentation charts 562
158. *"Credit-Linked Notices ('CLNs')," May 2001, Derivatives Capital Markets,* Citibank/Salomon Smith Barney presentation 564
159. *Yosemite, Issues/Timeline,* chart prepared by Enron Corp. 580
160. Citibank Memorandum to Project Yosemite Working Group, February 1999, re: *Initial thoughts on structures* 581
161. Citigroup, Inc. list of clients or counterparties that engaged in prepaid forward transactions with a special purpose vehicle 582
162. Citigroup, Inc. email, April 1999, re: *Enron/Project Roosevelt* 584

Page

163. Citigroup email, April 1999, re: *Enron/Consent to Amendment to Roosevelt Transaction* 586
164. *Global Loans Short Form Approval Memorandum,* April 26, 1999, prepared by Citibank (Roosevelt). 588
165. Citigroup email, April 1999, re: *Enron/Roosevelt Update* 591
166. Salomon Smith Barney Presentation to Enron on Capitalization, September 20, 1999 592
167. Salomon Smith Barney High Yield Commitment Committee Memorandum, April 2001, *Enron—$1 Billion—Credit Linked Note* 603
168. Salomon Smith Barney Investment Grade Commitment Committee—New York Memorandum, April 2001, ECLN II 604
169. Salomon Smith Barney Investment Grade Commitment Committee—Europe Memorandum, November 1999, Yosemite II 611
170. Salomon Smith Barney Investment Grade Commitment Committee—New York, October 1999, Yosemite I 619
171. Salomon Smith Barney Investment Grade Commitment Committee—New York, August 2000, Yosemite III, CLN I 629
172. Citigroup email, September 2001, re: *Enron (. . . better breakdown of where they make their money . . .)* 636
173. *Yosemite Securities Trust I,* Supplement (to Offering Memorandum dated November 4, 1999) 637
174. Enron Corp. 10-Q, June 30, 1999 644
175. Citicorp email, October 2001, re: *Enron ("relationship")* 651
176. *Yosemite Securities Trust I Financing, December 22, 1999–2000,* chart provided by Enron Corp. 653
177. Citigroup email, June 2001, re: *Prepaid Overview,* attaching chart, *Summary of Pre-Paid Accounting and Tax* 654
178. Citigroup email, April 2001, re: *Enron Credit Approval* 656
179. Citigroup email, October 2001, re: *Enron (. . . do we have incremental debt capacity . . .)* 657
180. Citigroup email, November 1999, re: *Yosemite II (Europe) (. . . I have been encouraged, from a risk point of view, to try to stay in compliance in the near term;)* 658
181. Citigroup email, November 1999, re: *Yosemite II (Europe) (. . . we still have an exposure issue . . . limits are limits . . .)* 660
182. Citigroup email, September 1999, re: *Yosemite (. . . terminate the price risk . . .)* 662
183. Citigroup email, August 2000, re: Citibank and Delta relationship *(. . . Delta is not controlled by Enron, . . . Citi had it set up several years ago.)* 664
184. Transcripts of JPMorgan Chase audio tapes:
    a. Transcripts of JPMorgan Chase audio tapes dated September 13, September 20, and October 3, 2001 665
    b. JPMorgan Chase audio tapes dated September 13, September 20, and October 3, 2001 ..... *
    c. Transcripts of selected JPMorgan Chase audio tapes 668
    d. Transcripts of selected JPMorgan Chase audio tapes ..... *
185. Additional JPMorgan Chase/Enron Corp. Documents in Support of July 23, 2002, Testimony (and Appendices) of Robert Roach, Chief Investigator, Permanent Subcommittee on Investigations:
    a. The Chase Manhattan Bank Facsimile, October 1996, re: *Enron 96—4 Term Sheets,* Draft sheets for prepaid sale options 2001 979
    b. Documents related to fees paid Mourant, Mahonia and JPMorgan Chase in relation to prepay transactions:
        1. Letter from Mourant & Co. to Chase Investment Bank Limited regarding fees due to Mahonia Limited for its participation in the "Enron V" (Prepay) transaction, December 1996 984
        2. Fee Letter from JPMorgan Chase to Enron North America Corp., September 2001 985
        3. Mourant & Co. invoice sent to The Chase Manhattan Bank for reimbursement of expenses related to Mahonia Limited, October 2001 986
    c. JPMorgan Chase email, December 1996, re: *Enron Natural Gas Marketing (Mahonia Limited)* 987
    d. JPMorgan Chase email, November 1997, re: *Heads-Up memo; Upsize to previously approved Enron Prepay* 988

Page

e. JPMorgan Chase Memorandum, September 1998, re: *Enron Prepays (1996 & 1997).* Includes detail on use of surety bonds to provide credit enhancement for prepay structures 989
f. Enron Corp.-JPMorgan Chase email, June 2000, re: *June 2000 gas prepay.* Includes detail on pricing methodology for prepay transactions 991
g. JPMorgan Chase-Mourant email, June 2000, re: *Enron-Mahonia-Chase Transaction.* Includes instructions from JPMorgan Chase attorney that documents are acceptable and may be executed by Mahonia . 992
h. Mourant-JPMorgan Chase email, September 2000, re: *Mahonia Limited.* Includes detail on fee arrangement for certain prepays 993
i. JPMorgan Chase email, November 2000, re: *Call Report for ENRON NORTH AMERICA CORPORATIO (sic)* 999
j. JPMorgan Chase email, December 2000, re: *Prepay Update #2 12/18* .. 1001
k. JPMorgan Chase email, September 2001, re: *Enron Prepay (. . . clearly they will take any money they can get now . . .)* 1002
l. Documents related to Arthur Andersen's request to Enron Corp. for representations as to the nature of the relationship between Mahonia and JPMorgan Chase:
1. Enron Corp. email, September 2001, re: *Rep Letter for Mahonia* ... 1003
2. Letter from Enron Corp. to Mahonia Limited, September 2001 1005
3. Letter from Mahonia Limited to Arthur Andersen LLP, September 2001 1006
m. Letter from Mahonia Limited to The Chase Manhattan Bank, September 2001, re: Mahonia's appointment of JPMorgan Chase as its agent 1007
n. Mourant-JPMorgan Chase email, October 2001, *Fwd: Enron Swap Transaction.* Includes attached Mourant-JPMorgan Chase emails from December 2000-September 2001 1009
o. Amended Complaint, United States District Court, Southern District of New York. JPMorgan Chase Bank, Plaintiff, against Liberty Mutual Insurance Company, et al., Defendants, June 2000, with attachments 1016
p. Letters between JPMorgan Chase and the Permanent Subcommittee on Investigations, July 2002, re: details of prepay transactions between JPMorgan Chase and Enron Corp. 1087
q. Letter from JPMorgan Chase to the Permanent Subcommittee on Investigations, July 2002, re: names of JPMorgan Chase's clients or counterparties, in addition to Enron, that engaged in prepaid forward transactions with a special purpose vehicle ("SPV") 1099
r. Letters between JPMorgan Chase and the Permanent Subcommittee on Investigations, July 2002, re: relationship and dealings of JPMorgan Chase to Mahonia Limited 1100
s. Facsimile from JPMorgan Chase to the Permanent Subcommittee on Investigations, April 2002, re: JPMorgan Chase/Enron transactions and fees 1111
186. Additional Citigroup/Enron Corp. Documents in Support of July 23, 2002, Testimony (and Appendices) of Robert Roach, Chief Investigator, Permanent Subcommittee on Investigations:
a. *Global Loans Approval Memorandum,* October 19, 1999, prepared by Citibank (Yosemite I) 1122
b. Enron Corp. Finance Committee Meeting, August 13, 2001, *Chief Financial Officer Report, Interest Rate Exposure, Finance Related Asset Sales, Outstanding Financings and Debt, ASF-Detail on Outstanding Fundings, and ASF-Detail on Prepays* 1131
c. Enron presentation charts, *Yosemite Update, Evolution, of Yosemite, Optional Use as Prepay Funding Vehicle, Yosemite Cost Analysis, Yosemite Prepay Analysis, and Conclusions & Recommendations* 1139
d. Enron Corp. documents on details of Yosemite/ECLN structures 1152
e. Enron Corp. charts, *What are Prepays, Why Does Enron Enter into Prepays, Actual Prepay Synopsis Overview, Actual Prepay Synopsis* 1166
f. Citigroup email, November 1999, re: *Yosemite II (Europe)* 1170
g. Facsimile from Maples and Calder to Schroders, September 2001, re: *Delta Energy Corporation* 1182
h. Facsimile from Maples and Calder to Milbank Tweed, Hadley & McCloy, November 1999, re: *Delta Energy Corporation (the "Company")* 1184

Page

i. Enron Corp. email, June 2001, re: *Delta Letter,* attaching . . . *sample letter with the representations that Andersen would like Delta to confirm.* 1187
j. Facsimile, re: remittance of funds to Bank of Bermuda and payment instructions for the account of Schroder Cayman Bank and Trust Company Limited, *Reference to Delta Energy Corporation* 1189
k. Correspondence from The Givens Hall Bank to Citibank, N.A., February 1999, re: *Delta Energy Corporation and Vega Energy Corporation fee notes* 1191
l. *Enron/Delta Swap Confirmation; Enron/Citibank Swap Confirmation;* and *Delta/Citibank Swap Confirmation,* all dated December 22, 1999 1194
m. *Enron/Delta Swap Confirmation and Citibank/EnronSwap Confirmation* Drafts, dated November 2, 1999 1231
n. Citigroup email, November 2001, re: *Citibank Unwind Amounts* 1251
o. Citigroup email, December 2001, re: *Ene* [Enron] *(Want to make sure swaps are terminated first thing and that delta terminates simultaneously so that we don't have any mismatch.)* 1253
p. Correspondence from Citigroup to the Permanent Subcommittee on Investigations, dated May 2, 2002, regarding Citigroup/Enron transactions and fees 1254
q. *Enron Corp. Project Yosemite, January 1999* presentation 1263
r. *Report of Independent Public Accountants, To the Trustholders of Yosemite Securities Trust I,* April 2001, draft financial statements and notes for 2000 and 1999 1276
s. *Yosemite Securities Trust Ltd., Notes to Financial Statements, December 31, 2000* 1284
t. Arthur Andersen LLP Memorandum, dated August 18, 2000, re: *$500,000,000 8% Enron Credit Linked Notes due 2005 Authorization to Sign* 1287
u. Enron Corp. letter to Arthur Andersen LLP, dated August 25, 2000, regarding Andersen's "comfort" letter issued in connection with the issue and sale of Enron Credit Linked Notes 1288

187. Additional Documents Related to JPMorgan Chase Prepays:
a. JPMorgan Chase email, August 1996, re: *Prepaid Forwards—Loans Vs Derivatives (Please arrange to report the prepaid forwards as loans effective as of August 31, 1996.)* 1290
b. JPMorgan Chase email, September 1996, re: *Loans/Borrowings Documented as Derivatives* 1294
c. JPMorgan Chase email, October 1997, re: *Loans/Borrowings Documented as Derivatives* 1299
d. JPMorgan Chase email, October 1997, re: *Sampoerna Deal (I understand the form of the transaction, rather than its economic substance, will govern in this case.)* 1300
e. JPMorgan Chase email, November 1997, re: *Loans/Borrowings Documented as Derivatives (Based on our discussions, it was concluded that such transactions which are confirmed with the counterparty as derivatives should be reported in Trading Assets/Liabilities—Risk Management Instruments and marked to market.)* 1303
f. JPMorgan Chase email, July 1999, re: *DISGUISED LOANS (We are making disguised loans, usually buried in commodities or equities derivatives (and I'm sure in other areas).)* 1304
g. JPMorgan Chase email, June 1999, re: *Prepaid Forwards (All of us have been grappling for years with the issue of determining when a structured transaction is more a kin to a loan or a derivative. There are no easy answers.)* 1306
h. JPMorgan Chase Memorandum, August 1999, re: *DBF's (Loans disguised as derivatives are now known as Derivatives Based Funding. (DBF's))* 1312
i. JPMorgan Chase email, March 2000, re: *Accounting for Compound Instruments* 1317
j. JPMorgan Chase email, March 2000, re: *Prepaid Forwards (Pat O'Brien's group has entirely dropped their proposal to change the accounting of Prepaid Forwards. This is good news.)* 1319
k. JPMorgan Chase email, March 2000, re: *Prepaid Forwards* 1321

Page

l. JPMorgan Chase email, January 1999, re: *Enron CLO Discussion (Rating agency knowledge of existing deals. Some deals that are less know (sic) to the agencies may come to light if they are placed in newly formed rated vehicles. This could well cause some heartburn for Enron)* 1323
m. JPMorgan Chase email, June 2000, re: Enron prepays 1326
n. JPMorgan Chase email, July 2000, re: *Restructuring existing prepays* 1328
o. JPMorgan Chase email, March 1998, re: *Enron Natural Gas Marketing/Mahonia/Parco* 1330
p. JPMorgan Chase Memorandum, April 2002, re: *PARCO Secured Loan to Mahonia* 1331
q. JPMorgan Chase email, November 2000, re: *Call Report for Enron North America Corporatio (sic)* 1332
r. JPMorgan Chase email, December 2000, attaching JPMorgan Chase Memorandum re: *Project Mahonia—$330 Million Forward Sale Natural Gas Contract Enron Financing Objectives* 1338
s. JPMorgan Chase email, April 1999, re: *Mahonia Ltd.* 1340
t. Mourant email, November 1997, re: *Mahoniia (sic) /New Enron Transaction* 1343
u. JPMorgan Chase-Mahonia correspondence, December 1992, attempting to identify a Jersey company to serve as SPC in prepay 1344
v. *Mahonia Limited,* Minutes of the First Meeting of Board of Directors, December 29, 1992 1347
w. *Mahonia Limited, Certificate of Incorporation (States of Jersey),* December 1992 1355
x. Mourant & Co.-Chase Investment Bank Limited correspondence, November 1993, attaching invoices for prepay transactions with Chase ... 1360
y. Mourant Memorandum, November 1995, re: Chase-Mahonia transaction 1366
z. Mourant List of *The Chase Manhattan Bank SPV Group ("Stoneville" Companies)* 1367
aa. The Chase Manhattan Bank description of ownership/purpose of *The Eastmoss Trust and Mahonia Limited* 1368
bb. The Chase Manhattan Bank-Mahonia Facsimile, December 2000, re: *Stoneville Aegean Board of Directors Minutes in connection with Enron-Mahonia transaction* 1371
cc. Mourant & Co. Limited *Annual Review* on *Mahonia Limited, ending 22/5/01* 1379
dd. JPMorgan Chase-Enron email, September 2001, re: *Rep Letter for Mahonia* 1384
ee. Mourant-Enron email, September 2001, re: *Mahonia Confirm* 1386
ff. Mahonia Limited letter to Arthur Andersen LLP, September 2001, re: representing the nature of Mahonia's operations 1388
gg. Chase Memorandum, August 1996, re: list of Chase prepays 1389
hh. Chase-Mahonia-Occidental Petroleum prepay 1391
ii. Chase email, May 1999, re: accounting for Ocean Energy, Inc. prepay 1398
jj. Chase presentation, December 22, 1999, on *Hunt Oil Company* prepay 1399
kk. JPMorgan Chase email, August 2000, re: *Columbia Prepay,* attaching copy of *Columbia Energy Group Structuring Summary* 1414
ll. Chase correspondence to Michael Kopper, Director, Enron Capital and Trade Resources, October 1994, re: *Prepaid Crude Oil Forward Sale* 1424
mm. Chase-Enron correspondence, May 1999, regarding Chase review of Enron on and off-balance sheet capital structure 1431
nn. Chase presentation, *Commodity Prepay Exposure Discussion,* January 27, 2000 1438
oo. Chase handwritten note, undated, re: *Pre-paids (Mahonia lends Enron $ in exchange for a promise that Enron will deliver . . . to Mahonia)* 1447
pp. Chase memorandum, December 2000, re: *Project Mahonia—$330 Million Forward Sale Natural Gas Contract Enron Financing Objectives* 1448
qq. Fleet-Chase email, December 2000, re: *Mahonia Forward Sale* 1453
rr. Chase email, February 2001, re: *MTM for Prepays* 1456
ss. Chase email, October 2001, re: *Enron Prepaids* 1458

Page

VOLUME 2

188. Additional Citigroup/Enron documents related to Projects "Roosevelt," "Truman," and "Nixon":
a. Enron Corp. Facsimile to Citicorp, December 1998, re: *Prepay structure* 1461
b. Citigroup email, December 1998, re: *Call Report—Project Roosevelt (Enron)* 1462
c. Citigroup Credit Memorandum (Enron), December 1998 (Roosevelt) 1466
d. Citigroup Facsimile, December 1998, *Project Roosevelt, Overview of Major Issues* 1473
e. Citigroup Facsimile, December 1998, *Project Roosevelt, Status Report* . 1475
f. Citigroup Facsimile, December 1998, *Enron—Project Roosevelt, Issues* . 1478
g. *CMAC Minutes,* June 22, 1999, *Prepaid Oil Transaction* 1482
h. Citigroup email, September 1999, re: *Enron-Roosevelt (. . . our expectation was now that the deal would not be repaid until December). Our approval to extend deliveries was done verbally.)* 1484
i. Enron Corp. email, November 1999, re: *Truman financial prepay diagram,* attaching *Crude Prepay 9/29/99 (. . . TD* [Toronto Dominion] *provides the commodity swap . . .)* 1485
j. Enron Corp. email, November 1999, re: *Y2* [Yosemite II] 1487
k. *Global Loans Approval Memorandum,* December 7, 1999, prepared by Citibank (Nixon) 1491
l. Citigroup email, December 1999, re: *Yosemite 2—Interim Solution,* attaching *Derivative Credit Form* 1496
189. Additional Documents Related to Yosemite and Enron Credit Linked Note (CLN) Transactions:
a. *Yosemite and CLN Payment Structures* 1500
b. *Project Yosemite,* Enron Corp. presentation 1501
c. Citigroup *Transaction Memorandum, Enron: Project Yosemite,* April 1999, *(This purpose of this memorandum is to obtain preliminary approval to seek a mandate to provide Enron's top tier banks with $500MM to $1,500MM of Enron default protection.)* 1506
d. Citigroup email, August 1999, re: *Rating Agency Discussions* 1511
e. Citigroup *Transaction Memorandum, Project Yosemite, $[1.0] Billion Credit Default Swap Structure Referencing Enron Corp., 10-21-99* 1513
f. Salomon Smith Barney Interoffice Memorandum, October 26, 1999, re: *Follow-up to Yosemite CMAC meeting* 1519
g. Citigroup Memorandum, October 29, 1999, *Yosemite Securities Trust I, Linked Enron Obligations (LEOs), Frequently Asked Questions* 1523
h. Moody's Investors Service letter to Yosemite Securities Trust I, November 18, 1999, re: *$750,000,000 8.25% Series 1999-A Linked Enron Obligations due 2004* 1526
i. Standard & Poor's letter to Solomon Smith Barney Inc., November 18, 1999, re: *Yosemite Securities Trust I, $750,000,000 8.25% Series 1999-A Linked Enron Obligations (LEOs) due November 15, 2004* 1527
j. Citigroup email, November 1999, re: *Project Yosemite (. . . I am afraid that if we ever had to defend this we would either (a) embarrass the client or (b) lose the accounting argument.)* 1529
k. Citigroup email, November 1999, re: *Enron—Various (Yosemite: . . . A portion of the proceeds will be used to repay our Project Roosevelt (Delta).)* 1532
l. Citigroup email, November 1999, re: *Enron Credit (. . . I am not willing to approve another incremental exposure on Enron, . . .)* 1533
m. *Enron Debt Security [Series 1999-A],* November 18, 1999 1534
n. Citigroup email, November 1999, re: *Enron-Yosemite II,* Citigroup purchase of Yosemite II certificates 1541
o. Citigroup email, December 1999, re: *Enron Failure to Pay on Prepaid* 1543
p. Citigroup Chart, *Derivative Transactions Associated With The Yosemite Structure,* January 2000 1545
q. Citibank Memorandum, March 29, 2000, re: *Project Yosemite—Yosemite Co. Structured Credit Derivative Transaction* 1546
r. Citigroup email, April 2000, re: *Project Yosemite—Revenue Recognition* 1551
s. Citigroup email, April 2000, re: *Enron* 1556
t. Citigroup Memorandum, August 13, 2000, *Enron Credit Linked Notes Trust ("Enron CLN"), Frequently Asked Questions* 1560

Page

u. Citigroup Script document, undated, detailing Enron Credit Linked Notes (CLN) Swaps 1564
v. Citigroup email, October 2000, re: *Enron Follow-up (Royal Bank of Canada as holder of $50 million Enron Credit Linked Notes)* 1566
w. Citigroup email, October 2000, re: *Enron Follow-up* 1569
x. Citigroup email, October 2000, re: *Enron Follow-up (. . . upon a credit event we can legally deliver the prepaid swap to be used to pay the noteholders.)* 1571
y. Citigroup email, October 2000, re: *Enron (. . . we ended up consolidating the trust . . . and we treated the prepaid swaps as a loan . . . for RBC purposes.)* 1574
z. Citigroup email, November 2000, re: *Enron CLN Transaction—SFAS 133 Accounting for Prepaid Swaps* 1575
aa. Citigroup Memorandum, May 2, 2001, *Enron Credit Linked Notes Trust II Senior Notes Offering ("Enron CLN II"), Frequently Asked Questions* 1579
bb. Solomon Smith Barney Memorandum, May 2, 2001, *Enron Sterling Credit Linked Notes Trust Senior Notes Offering ("Enron CLN II"), Frequently Asked Questions* 1588
cc. Citigroup email, June 2001, re: *Prepay Diagram,* attaching chart, *$250 Million Prepay* 1593
dd. Citigroup email, June 2001, re: *Enron (. . . there is an earnings impact, except that it is neutralized by offsetting trades . . .)* 1595
ee. Enron Corp. Memorandum, September 20, 2001, re: *Citibank/Delta Prepay Transactions (. . . some concerns with respect to the structure of the prepay transactions . . .)* 1596
ff. Citigroup email, November 2001, re: *ene* [Enron] *prepaid update (. . . let enron out of paying half of the libor breakage (about 250k) on the early termination of the prepaid. . . .)* 1597
gg. Enron email, December 2001, re: *AXA Enron Credit Linked Note* 1598
hh. Citigroup email, November 2002, re: *Enron II Documentation* (CLN II) 1599
ii. *Summary of Enron CLN Accounting Treatment* 1612
jj. *Enron Credit Linked Notes Trust Certificates, SFAS 133 Fair Value Hedge Documentation* (Citibank/Royal Bank of Canada Total Return Swap) 1613

190. Additional Documents Related to Citigroup/Delta Relationship:
a. Milbank Tweed email, November 1999, re: Delta 1618
b. Delta Energy Corporation letter to Enron Corp., November 18, 1999, representing the nature of Delta's operations 1622
c. Enron Corp. email, June 2001, re: *Sample Swap Co Letter* 1623
d. Enron-Citigroup email, June 2001, re: *Delta Letter* 1624
e. Delta Energy Corporation letter to Enron Corp., June 2001, re: *Delta Energy Corporation* 1626
f. Citigroup email, June 2001, re: *reps (lydia got on and stated that the reps are facts that we believe are true, and the rationale for the letter is to confirm that Delta is not a spv that needs to be consolidated on the b/s)* 1627
g. Citigroup email, August 2000, re: questions regarding Delta 1628
h. Citigroup email, undated, re: *Prepaid Transaction* 1629

191. Additional Documents Related to Transfer of Yosemite Certificates to Whitewing:
a. LJM, December 1999, *Benefits to Enron Summary (At year-end 1999, Enron sold LJM2 the equity in Yosemite structure.)* 1630
b. *SE Raptor L.P. Letter of Understanding* to LJM2 Co-Investment, L.P., Attn: Andrew S. Fastow, December 30, 1999, re: . . . *proposed acquisition by SE Raptor L.P. . . . of the Yosemite Certificates . .* 1631
c. *LJM Approval Sheet,* February 8, 2000, *Deal Name: Yosemite* 1635
d. Enron Corp. Interoffice Memorandum, February 23, 2000, re: *LJM2 Investment in Certificates of Beneficial Interest in Yosemite Securities Trust I* 1638
e. Enron Global Finance email, February 2000, re: *calculation (Yosemite Certificates)* 1639
f. Enron Corp. email, undated, re: *Yosemite Certificates* 1641
g. *Wire Transfer Requests,* February 28, 2000, re: *SE Acquisition, L.P., LJM2 Co-Investment, L.P., Enron Corp. and Whitewing* 1642

Page

h. Enron Corp. letter to LJM2 Co-Investment, L.P., Attn: Andrew S. Fastow, March 8, 2000, *(. . . Enron agrees to pay LMJ2 $100,000.)* 1645
i. General Partner, LJM2 Co-Investment, L.P. draft letter to Limited Partners, describing LJM2 purchase and sale of Yosemite Trust Certificates 1646
j. Enron Corp., *Yosemite Equity Sale Project "Yes"*, November 10, 2000 ... 1649
k. Enron Corp. *Whitewing Investment Proposal, Yosemite Securities Company Ltd,* December 12, 2000 1659
l. Dewey Ballantine LLP Memorandum, December 13, 2000, re: *Osprey Consent-Yosemite* (Consent in connection with the Whitewing's acquisition of Yosemite Trust Certificates) 1665
m. Enron Corp./Citigroup/Milbank email, February 2001, re: *Yosemite Securities Company Ltd. (Yosemite Certificate holders)* 1673
n. Enron Corp. email, November 2001, attaching *Yosemite I Transaction and Credit and Subordination Agreement between SE Acquisition and LJM2* 1677
o. Citigroup email, December 2001, re: *Ene* [Enron] *settlements* 1680
192. Additional Citigroup Documents:
a. Citibank/Solomon Smith Barney reprint of a December 6, 1999, *Investment* Dealers' Digest *regarding Enron/Yosemite* 1681
b. Citigroup/*GCIB Checkings on Michael Kopper/LJM* 1682
c. Citigroup Internal Memorandum, January 24, 2001, re: *Review of LJM2 (Enron Fund) and Recommendations for LJM3 (. . . LJM2 principals argue that Enron would make the Fund whole should it suffer losses because the vehicles that the Fund invest in are critically important to Enron's ability to manage its earnings.)* 1683
d. Citigroup, *Enron Credit Review,* August 2001 1684
e. *Presentation of Enron Corp., Direct and Indirect Liability Schedule,* October 24, 2001 1692
f. *Summary of Enron's Capital Market Exposure with Citigroup,* October 29, 2001 1704
g. Citigroup, *Project 10, Due Diligence Findings* [Enron], November 7, 2001 1706
h. Letters between Citigroup and the Permanent Subcommittee on Investigations, July 2002, regarding prepay transactions between Citigroup and Enron Corp.; names of Citigroup's clients or counterparties, in addition to Enron, that engaged in prepaid forward transactions with a special purpose vehicle ("SPV"); Citigroup's relationship with Delta Energy Corporation, etc. 1825
i. Letters between Citigroup and the Permanent Subcommittee on Investigations, July 2002, regarding Citigroup's relationship with Delta Energy Corporation 1841
j. Citigroup letter to the Permanent Subcommittee on Investigations, August 7, 2002, regarding *steps Citigroup is taking to ensure that the balance sheet effect of structured financing is transparent to investors* 1850
193. Additional Enron Corp. Documents Related to Prepay Transactions:
a. Enron Capital & Trade Resources Interoffice Memorandum, August 1997, re: *Prepaid Hydrocarbon Companies (The purpose of the Prepaid Contract is to provide cash flow to Enron Corp. in order to meet its cash flow objectives.)* 1853
b. *Enron Corp Bank Presentation, November 19, 2001, Waldorf Astoria, New York, New York,* (selected pages of presentation) 1858
c. Enron prepay guarantee coverage, *Off Balance Sheet Debt* 1930
d. *Enron Surity Bonds Summary,* March 10, 2002 1931
e. Enron Corp. Interoffice Memorandum, re: Enron Annual Reviews for Doug McDowell, 1999 and 2000 1932
f. Enron email, June 2001, re: *Citibank Prepay,* attaching presentation entitled *Enron North America, $250 Million Prepay* 1941
g. Draft Enron Letter to Milbank, Tweed, January 2001, re: *Tax Forms and Administrative Matters for Delta Energy Corp.* 1948
h. Enron Corp. Interoffice Memorandum, November 2001, re: *$750 Million Yosemite Debt—Recourse v. Nonrecourse* 1949
i. Enron Corp. Letter to the Permanent Subcommittee on Investigations, July 2002, re: accreditation records of Delta Energy and Mahonia 1953
j. *Enron Risk Assessment and Control Deal Approval Sheet, APEA Tax Exempt Prepay,* April 29, 1999 1954

Page

k. Enron Corp. Memorandum, June 30, 1999, re: *Federal Income Tax Treatment of Prepayments* 1961
l. Enron Corp. (Tax Planning Department) Interoffice Memorandum, April 2000, re: *Yosemite I Withholding for Year 2000* 1974
m. Enron Corp. (Corporate Tax Planning Department) Interoffice Memorandum, April 2001, re: *Enron Credit Linked Notes Due 2005* 1976
n. Enron Corp. (Global Finance Tax Department) Interoffice Memorandum, November 2001, re: *$750 Million Yosemite Debt—Recourse v. Nonrecourse* 1981
194. Documents Related to Additional Financial Institutions Involved in Enron Corp. Prepays:
a. Credit Suisse First Boston email, December 2000, re: *Prepaid Swap (The net effect for ENE* [Enron] *is raising $150mm . . . and not treated as debt. . . .)* 1985
b. Credit Suisse First Boston email, December 2000, re: *URGENT/decision required-status on Eneron* [sic] *oil linked loan (I have raised issues to date on reputational risk. . . .)* 1986
c. Credit Suisse First Boston email, December 2000, re: *Enron-Prepaid Oil Swap (Further, I want to clarify the reputational risk of this transaction. . . .)* 1987
d. Credit Suisse First Boston email, December 2000, re: *docs/guarantee approval (. . . DO NOT include any representations on accounting driven transactions)* 1988
e. Credit Suisse First Boston email, September 2001, re: *Enron Oil Trade (. . . special request/favor from Ben* [Glisan]*.)* 1989
f. Credit Suisse First Boston email, September 2001, re: *PLEASE CALL ME IMMEDIATELY/ENRON-RELATED CREDIT ISSUE (. . . emergency request for a $150 million prepaid facility . . . in return for the left pole position on a $1B benchmark bond deal. . . .)* 1990
g. Credit Suisse First Boston letter to the Permanent Subcommittee on Investigations, April 24, 2002, regarding Enron-related transactions and fees involving Credit Suisse First Boston or Donaldson, Lufkin & Jenrette Securities Corporation 1991
h. Fleet Bank email, December 2000, attaching copy of Project Mahonia Memorandum 2007
i. JPMorgan Chase email, December 2000, re: *Fee Letter* on December 2000 Prepay 2009
j. Enron Corp. email, July 2001, attaching copy of *Project Camelot* (Barclays) presentation 2013
k. Enron Corp., *EGM Inventory Financing, August 2001, Transaction Structure, (EGM sells inventory to SwapCo (a third party entity controlled by but NOT affiliated to Barclays . . .)* 2019
l. Sullivan & Cromwell (on behalf of Barclays Capital) letters to the Permanent Subcommittee on Investigations, May and November, 2002, attaching list of transactions involving Barclays Capital and Enron Corp. and its affiliates 2023
195. *The Wall Street Journal* Editorial, July 29, 2002, *Enron's Enablers* 2043
196. Clarifications for the record of Mr. John C. Diaz and Ms. Pamela M. Stumpps, Moody's Investors Service, dated August 15, 2002 2044

Exhibits for July 30, 2002

201. *What Merrill Knew,* chart prepared by the Permanent Subcommittee on Investigations 2046
202. *Nigerian Barge Chronology,* prepared by the Permanent Subcommittee on Investigations 2047
203. a. *Nigerian Barge Transaction,* chart prepared by the Permanent Subcommittee on Investigations 2049
b. *Nigerian Barge Transaction, Enron Guarantee/LJM2's Purchase,* chart prepared by the Permanent Subcommittee on Investigations 2050
204. a. *Factors Leading to Non-Recognition of Revenue in a Sales Transaction Under Generally Accepted Accounting Principles,* chart prepared by the Permanent Subcommittee on Investigations 2051
b. *How Nigerian Barge Deal Failed to Meet Generally Accepted Accounting Principles,* chart prepared by the Permanent Subcommittee on Investigations 2052

Page

205. *Merrill Lynch Analysts' Relationship With Enron And Impact On Fees,* chart prepared by the Permanent Subcommittee on Investigations 2053
206. a. Transcript of excepts from a videotaped presentation about LJM2 made by Andrew S. Fastow and Michael J. Kopper of Enron Corporation on or about September 16, 1999, for Merrill Lynch's Private Equity Group representatives 2054
b. Videotape of excepts from a videotaped presentation about LJM2 made by Andrew S. Fastow and Michael J. Kopper of Enron Corporation on or about September 16, 1999, for Merrill Lynch's Private Equity Group representatives. ..... *
c. Full videotaped presentation about LJM2 made by Andrew S. Fastow and Michael J. Kopper of Enron Corporation on or about September 16, 1999, for Merrill Lynch's Private Equity Group representatives ..... *
207. Merrill Lynch *Appropriation Request Cover Page for Enron Nigerian Barge Equity,* 1999 2059
208. Merrill Lynch *Interoffice Memorandum,* December 1999, re: *Enron Corp. (Jeff McMahon, EVP and Treasurer of Enron Corp. has asked ML to purchase $7MM of equity. . . .),* with attached Nigeria Barge Project Sell Down 2064
209. Merrill Lynch email, January 2002, attaching *Americas Credit Flash Report: Week ending 12/23/99* and *12/17/99* 2068
210. Draft Merrill Lynch Agreement Letter to Jeff McMahon of Enron Corp., December 23, 1999, re: *Enron Nigeria Barge Ltd.* 2071
211. Merrill Lynch Agreement Letter to Andrew S. Fastow of Enron Corp., December 29, 1999, re: *Enron Nigeria Barge Ltd.* 2074
212. *Preliminary Information Memorandum* re: *Enron Nigeria Barge Ltd.,* December 1999, with handwritten notes, *. . . reputational risks i.e. aid/abet Enron income stmt. manipulation* 2079
213. Notes of Paul J. Wood, Director of Corporate Credit, Merrill Lynch, re: Nigerian Barge Equity *(Brown hates deal)* 2105
214. *Limited Liability Company Agreement of Ebarge, LLC,* dated December 29, 1999 2107
215. *Share Transfer Forms* from *Enron Nigeria Barge Limited to Ebarge, LLC,* dated December 30, 1999 2114
216. a. *Enron Nigeria Power Holding, Ltd. and Ebarge, LLC, Loan Agreement,* dated December 29, 1999 2117
b. *Enron Nigeria Barge Holding Ltd. and Ebarge, LLC and Enron Nigeria Barge Ltd., Shareholders' Agreement,* dated December 29, 1999 2136
217. *Benefits to Enron Summary, Deal Name: Bargeco, 6/29/00 (. . . promising that Merrill would be taken out by sale to another investor by June, 2000.)* 2157
218. Merrill Lynch email, June 2000, re: *Ebarge LLC (. . . getting questions concerning Ebarge, LLC. It was our understanding that Merrill Lynch IBK positions would be repaid its equity investment as well as a return on its equity by this date. Is this on schedule to occur?)* 2158
219. Merrill Lynch email, June 2000, re: *Ebarge Letter-Enron,* attaching draft letter to Enron Corp. from Merrill *(Enron has agreed to purchase the shares from Ebarge by June 30, 2000)* 2159
220. Merrill Lynch email, January 2002, re: *eBarge (. . . the arrangement called from them to pay interest of 15% per annum on such investment.)* . 2161
221. Merrill Lynch email, May 2000, re: *Ebarge LLC (. . . calculation of the income accrual for Ebarge LLC. . . .)* 2163
222. *Share Purchase Agreement between LJM2-Ebarge, LLC and ML IBK Positions, Inc.,* dated June 29, 2000 2164
223. Merrill Lynch email, January 2002, re: *Ebarge LLC confirmation of 15% equity return rate. (. . . could not locate anything on the 15% equity return.)* 2173
224. Merrill Lynch email, January 2002, re: *Ebarge (What happened is 15% or $525,000 was the equity return. . . .)* 2174
225. Merrill Lynch email, January 2002, re: *Ebarge (the interest on the loan was to be paid by Enron. . . .)* 2175
226. Merrill Lynch email, January 2002, re: *Ebarge LLC (Poor poor Kira and Joe!!!!)* 2176
227. a. Merrill Lynch *LJM2 Investment Summary* (Ebarge LLC), June 2000 .. 2177
b. *Enron Risk Assessment And Control Deal Approval Sheet on Nigeria Power Holding, Ltd. Divestiture,* dated November 2000 2182

Page

228. Notes of Kevin Jordan, Enron Accountant, re: Nigerian Barge transaction 2191
229. Merrill Lynch email, June 2000, re: Ebarge and LJM2 *(It appears that the way we are getting out of the Enron investment on MLIBK Positions books ($7.0m + interest) is having LJM2 Co-Investment LP buy us out through LP Capital Calls, in which MLIBK is also a limited partner.)* 2192
230. *Timeline of Pertinent Information, Ebarge, LLC* 2193
231. *Summary of Merrill Lynch Enron-Related Investment Banking Compensation (By Business Segment),* chart prepared by Merrill Lynch 2194
232. Merrill Lynch email, June 2000, re: *LJM2 (The Committee* (Debt Markets Commitment Committee) *is being asked to consider $10MM share of a $65MM 364-day liquidity facility for the LJM2 Co-Investment LP. . . . Please respond with your Yes/No vote at your earliest convenience).* Follow-up Merrill Lynch email 2195
233. Merrill Lynch Interoffice Memorandum, July 2000, re: *Request for an Exception to Policy for a $10MM Loan commitment to LJM II* 2200
234. Merrill Lynch email, November 2001, re: *LJM—updated summary (They all committed to this loan, as did we, because of the Andy Fastow/Enron relationship. . . .)* 2201
235. Merrill Lynch Interoffice Memorandum, February 2001, re: *Enron (ML recently lost the mandate to underwrite $1.25 billion of zero coupon convertible debt because Enron does not believe ML is a financial partner. . . . Merrill Lynch has decided to help Enron underwrite and syndicate these types of deals.)* 2202
236. Merrill Lynch email, July 2001, re: *Enron—rawhide (I just heard back from James and he told me that Enron will definitely not tie our loss to new business.)* 2203
237. Merrill Lynch email, July 2001, re: *LJM2/Enron (. . . we took a substantial P/L hit for selling Zephyrus, not something we want to repeat. . . .)* 2204
238. Merrill Lynch email, December 2001, re: *Structured loan transactions (. . . a snapshot of the structured loans in the portfolio are as follows. . . .)* 2205
239. Merrill Lynch Interoffice Memorandum, April 1998, re: *Enron Common Stock Offering, Background,* Merrill Lynch's analyst relationship with Enron 2206
240. Merrill Lynch email, January 1999, re: *Enron Account Update (. . . regarding our difficult relationship in Research . . . two significant mandates by Enron.)* 2209
241. Merrill Lynch email, February 1999, re: *Enron Mandate/Lay Letter (. . . it might be appropriate for you to send a note to Ken Lay at Enron thanking him for a recent mandate to serve as a co-manager on a 12 million share common stock offering ($775MM).)* 2210
242. Merrill Lynch Interoffice Memorandum, December 1998, re: *Andy Fastow (SVP & CFO of Enron) visit on December 4th)* 2211
243. Merrill Lynch Calling List for the Enron Corp. common stock offering, dated April 28, 30, and May 4, 1998 2212
244. Merrill Lynch Interoffice Memorandum, March 2001, re: *$40.0 million participation request from Enron Corp. . . . in funding a five-year Senior Secured Credit Facility for Zephyrus Investments, LLC* 2225
245. *Commitment Committee Information, Zephyrus Investments, LLC/Enron Corp.,* March 2001 2233
246. Merrill Lynch Interoffice Memoranda, October 1999, re: *Skilling* (Enron) *Questions on LJM2* 2235
247. Merrill Lynch *LMJ2 Co-Investment LP, Fee Calculation* 2237
248. Merrill Lynch email, November 2001, re: LMJ2, attaching *Investor Status Summary,* as of 9/30/01 2238
249. Merrill Lynch *LJM2 Co-Investment, L.P., Private Placement Memorandum* 2240
250. *LJM2 Co-Investment, L.P., Limited Partner Groups* 2289
251. *LJM2 Co-Investment, L.P., Schedule II, Information Regarding Limited Partners, As of November 12, 2001* 2292
252. *LJM Investments, Annual Partnership Meeting, October 26, 2000,* presentation 2293
253. Merrill Lynch *LJM3 Appropriation Request* 2337

Page

254. Merrill Lynch email, November 2000, re: *ML investment in LJM III (. . . there will probably be substantial interest in re-doing the employee vehicle early next year.)* 2340
255. Merrill Lynch email, December 2001, re: *ML/LJM2 Co-Investment, L.P. Capital Call ($140K Commit) (YOU MUST BE JOKING. . . .)* 2342
256. Merrill Lynch Interoffice Memorandum, December 1998, re: *Enron Corp. Loan Commitment (The loan commitment is required by Enron's accountants to insure that the structure receives off-balance sheet treatment.)* 2344
257. Merrill Lynch email, May 2000, re: *Enron Net Works (. . . Enron not worried about debt on the balance sheet, as they can structure around it.)* 2346
258. Merrill Lynch email, May 2000, re: *Enron Net Works (Off Balance sheet debt—Not a primary driver because Enron believes they can structure anything to be off balance sheet.)* 2348
259. Merrill Lynch email, April 2001, re: *Enron meetings (. . . they do a bunch of balance sheet deals similar to your barge deal. . . .)* 2349
260. a. Merrill Lynch email, December 1999, re: *New Account Opening (Delaware LLC to Cayman Island—Tax Reasons.)* 2350
b. Merrill Lynch email, March 2000, re: *Ebarge LLC (. . . we have converted the entity to the Cayman Islands . . .* 2351
261. List of Merrill Lynch employees investing in LJM2 2352
262. Enron Corp. draft letter/edits on Enron Nigeria Barge Ltd. sale 2354
263. *Bargeco Encomics,* LJM2 document 2359
264. *Enron Risk Assessment and Control Deal Approval Sheet, Nigeria Barges Equity Sell Down,* January 13, 2000 2360
265. *Dan O Boyle, 2000 Deals and Accomplishments* 2364
266. LJM Investments, Benefit Summaries 2367
267. LJM2 Co-Investment, L.P. Facsimile, May 2001, to Price Waterhouse Coopers, re: *Enron Nigeria Barge Ltd.* 2374
268. Merrill Lynch letter to the Permanent Subcommittee on Investigations, April 2002, regarding *Merrill Lynch Transactions with Enron-Related Entities (1997 to Present)* 2379
269. Letters between Merrill Lynch and the Permanent Subcommittee on Investigations, August-November 2002, regarding follow-up questions from July 30, 2002 Subcommittee hearing 2390

* May be found in the files of the Subcommittee

THE ROLE OF THE FINANCIAL INSTITUTIONS IN ENRON'S COLLAPSE—VOLUME 1

TUESDAY, JULY 23, 2002

U.S. SENATE,
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS,
OF THE COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 9:34 a.m., in room SD–106, Dirksen Senate Office Building, Hon. Carl Levin, Chairman of the Subcommittee, presiding.

Present: Senators Levin, Cleland, Carper, Lieberman (ex officio), Collins, Bunning, Fitzgerald, and Thompson (ex officio).

Staff Present: Linda J. Gustitus, Chief of Staff, Senator Levin; Mary D. Robertson, Chief Clerk; Robert L. Roach, Counsel and Chief Investigator; Stephanie E. Segal, Professional Staff Member; Ross Kirschner, Deputy Investigator; Jamie Duckman, Professional Staff Member; Edna Falk Curtin, Detailee/General Accounting Office; Rosanne Woodroof, Detailee/Department of Commerce OIG; Lani Cossette; Alex DeMots; David Berick (Governmental Affairs Committee/Senator Lieberman); Cecily Cutbill (Senator Carper); Tara Andringa, Kathleen Long, and Clark Cohen (Senator Levin); Kim Corthell, Republican Staff Director; Alec Roger, Counsel to the Minority; Claire Barnard, Investigator to the Minority; Meghan Foley, Staff Assistant; Jessica Caron, Intern; Gary Brown and Bob Klepp (Governmental Affairs Committee/Senator Thompson); Holly Schmitt (Senator Bunning); Jennifer Bonar (Senator Fitzgerald); and Felicia Knight (Senator Collins).

OPENING STATEMENT OF SENATOR LEVIN

Senator LEVIN. The Subcommittee will come to order.

Enron was the first in the recent wave of corporate scandals, but it continues to instruct us on what has gone wrong in corporate America and what needs to be reformed. Earlier this month, the Permanent Subcommittee on Investigations released a report on the role of the Board of Directors in the collapse of Enron. It found that the Board had failed in its fiduciary duty to protect Enron shareholders and that it shares responsibility for Enron's deceptions and its bankruptcy. Today we will look at financial institutions and the role that they played in Enron's collapse.

It is now common knowledge that Enron engaged in accounting deceptions to convince investors, lenders, analysts, and the public that the company was in better financial shape than it really was. In examining the role that financial institutions played in Enron's demise, we are focusing on one type of so-called "structured fi-

nance" transactions that Enron referred to as "prepays" and that they used to obtain billions of dollars in financing for Enron without showing any additional debt on its books. I believe that most will conclude, after we hear today's testimony, that Enron's use of these prepays to disguise debt was an accounting sham, and to carry out the deceptions Enron had the help and the knowing assistance of some of the biggest financial institutions in our country, including JPMorgan Chase and Citigroup.

It should be noted that Enron was not the only company using sham prepays in the way it did. Both Chase and Citicorp have shopped the prepay structures around, and other banks and other companies have engaged in similar transactions, which is also why our investigation of this subject is so important.

Prepays, in concept, are simple and legitimate. They are arrangements in which a company is paid in advance to deliver a service or a product at a later date. But the prepays constructed by Enron and banks like Chase and Citigroup were phony prepays. There was an appearance of a product to be delivered at a later date, but the reality was different. No product was intended to be delivered; the transaction was in reality a loan; but it was disguised so no loan would appear on Enron's books.

This structured deception had that clear purpose. There is a big difference in the financial world between cash that comes from business activity versus cash that comes from a loan, and there is supposed to be a big difference in the accounting treatment. Increased business activity can boost a company's credit rating and stock value. In contrast, greater debt levels can lower a company's credit rating and stock value.

In a few minutes, we will hear from the chief investigator of the Permanent Subcommittee on Investigations Staff, Robert Roach, who will describe the intricacies of how these phony prepays worked for Enron. We will then hear from two major credit agencies, Moody's and Standard & Poor's, who will testify that despite following Enron quite closely, they were unaware of the extent and nature of Enron's prepays which, had they known of them, would have significantly affected Enron's credit ratings. We will also hear from the former chief accountant at the Securities and Exchange Commission, Lynn Turner, about the shady accounting Enron used to hide the prepay debt and deceptively increase operational cash flow.

The last two panels will be JPMorgan Chase and Citibank who were the biggest banking participants in Enron's phony prepay activities. We will show how the banks arranged for Enron to carry out these so-called prepays by using offshore shell companies which the banks controlled, like Mahonia and Delta Energy—companies which have no employees, no offices, and operate in secrecy jurisdictions, that make it tough for law enforcement to uncover or understand their relationships to the banks behind them.

The offshore entities were passthroughs, controlled by banks, and helped disguise the loans so that they wouldn't show as debt on Enron's financial statements. Those offshore entities were not the independent entities which they needed to be in order for the promises of future delivery of commodities to them to be legitimate pre-

pays. We will also hear how the banks acted to limit public disclosure of Enron's prepay obligations.

Central to the issues today is evidence indicating that Chase and Citicorp knew what Enron was doing, assisted Enron in those deceptions, and profited from their actions. Take a look at this chart which contains excerpts taken from internal documents at Enron, its auditor Arthur Andersen, and Chase and Citibank. Each discusses Enron's so-called prepays.

First is an internal presentation from Enron's own accounting department. It states: "Why Does Enron Enter into Prepays? Off balance sheet financing (i.e., generate cash without increasing debt load)." That is Enron's statement of why it enters into prepays: "i.e., generate cash without increasing debt load."

Then there is an internal email from Chase which has this to say about Enron's prepays: "Enron loves these deals as they are able to hide funded debt from their equity analysts because they (at the very least) book it as deferred rev[enue] or (better yet) bury it in their trading liabilities." That is what Chase had to say and what they knew about these prepays.

A Citigroup email makes a similar point: "E[nron] gets money that gives them c[ash]flow but does not show up on books as big D Debt."

And Andersen, of course, knew what was going on. Its internal email states: "Enron is continuing to pursue various structures to get cash in the door without accounting for it as debt."

Now, those are excerpts from just a few of the documents which our Subcommittee uncovered that show that Enron's prepay activity was well known to its participants but hidden from everybody else. Each knew that Enron's prepays were designed to manipulate its financial statements, not to achieve business objectives. Each also knew that Enron was booking prepay proceeds as trading activity instead of loans, even though no trade or sale was ever intended. Phony prepays produce misleading financial statements. And that is what happened here.

When Enron collapsed and declared bankruptcy in December 2001, it had about $5 billion in outstanding so-called prepays that were virtually unknown to the company's creditors, investors, and business associates. And this disguised debt contributed significantly to the Enron meltdown and the huge loss to Enron's shareholders, the people who depended on that stock for their pensions, people who had saved all their life and who had worked hard for these investments. The debt was disguised. It contributed to the meltdown and to the huge loss to those people.

Today we are going to shine the light in an area where complexity has been used to hide the truth. Hopefully we will cut through the darkness and place appropriate levels of responsibility on those who participated in these schemes.

[The prepared statement of Senator Levin follows:]

PREPARED STATEMENT OF SENATOR LEVIN

Enron was the first in the recent wave of corporate scandals and continues to instruct us on what has gone wrong and what needs to be reformed. Earlier this month the Permanent Subcommittee on Investigations released a Subcommittee report on the role of the Board of Directors in the collapse of Enron. It found that the Board had failed in its fiduciary duty to protect Enron shareholders and shares

responsibility for Enron's deceptions and bankruptcy. Today we are looking at financial institutions and the role they played in Enron's collapse.

It has become common knowledge that Enron engaged in accounting deceptions to convince investors, lenders, analysts, and the public that the company was in better financial shape than it really was. In examining the role that financial institutions played in Enron's demise, we are focusing on one type of so-called "structured finance" transaction Enron referred to as "prepays" and used to obtain billions of dollars in financing for Enron without showing any additional debt on its books. I think most will conclude after we hear today's testimony that Enron's use of these prepays to disguise debt was an accounting sham, and to carry out the deceptions Enron had the help and knowing assistance of some of the biggest financial institutions in our country—including JPMorgan Chase and Citigroup. By the way, Enron was not the only company using sham prepays in the way it did. Both Chase and Citicorp have shopped the prepay structures around, and other banks and other companies have engaged in similar transactions.

Prepays, in concept, are simple and legitimate. They are arrangements in which a company is paid in advance to deliver a service or product at a later date. But they didn't stay legitimate with Enron and banks like Chase and Citigroup which together began constructing complex, phony prepays that resulted in Enron obtaining billions of dollars that were in reality undisclosed loans to Enron. There was an appearance of a product to be delivered at a later date, but the reality was different. No product was intended to be delivered; the transaction was in reality a loan; and it was artfully disguised so no loan would appear on Enron's books.

Enron used these so-called prepays to obtain approximately $8 billion in financing over about 6 years. On its financial statements, Enron reported the prepays as energy trading activity instead of debt, giving the false impression that the money from the prepays was part of Enron's ordinary business activities, instead of the loans they really were.

The purpose of all the complexity was to hide a loan, so it wouldn't appear as debt on Enron's books.

This structural deception had a clear purpose. There's a big difference in the financial world between cash that comes from business activity versus cash that comes from a loan, and there is supposed to be a big difference in the accounting treatment. Increased business activity can boost a company's credit rating and stock value. In contrast, greater debt levels can lower a company's credit rating and stock value.

In a few minutes we will hear from the Chief Investigator of the PSI Staff, Robert Roach, who will describe the intricacies of how these phony prepays worked for Enron. We will then hear from two major credit agencies, Moody's and Standard and Poor's, who will testify that despite following Enron quite closely, they were unaware of the extent and nature of Enron's prepays which, had they known of them, would have significantly affected Enron's credit ratings. We will also hear from the former Chief Accountant at the SEC, Lynn Turner, about the shady accounting Enron used to hide the prepay debt and deceptively increase operational cash flow.

Then we will hear from JPMorgan Chase and Citigroup who were the biggest participants in Enron's phony prepay activities. We will hear how the banks arranged for Enron to carry out these so-called prepays by using offshore shell companies the banks controlled, like Mahonia and Delta Energy, which have no employees and no offices, and operate in secrecy jurisdictions that make it tough to uncover or understand their relationships to the banks behind them. We will also hear how the banks acted to limit public disclosure of Enron's prepay obligations.

Central to the issues today is evidence indicating that Chase and Citicorp knew what Enron was doing, assisted Enron in the deceptions, and profited from their actions. Take a look at this chart which contains excerpts taken from internal documents at Enron, its auditor, and Chase and Citibank. Each discusses Enron's so-called prepays.

First is an internal presentation from Enron's own accounting department. It states: "Why Does Enron Enter into Prepays? Off balance sheet financing (i.e., generate cash without increasing debt load)."

Next is an internal email from Chase which has this to say about Enron's prepays: "Enron loves these deals as they are able to hide funded debt from their equity analysts because they (at the very least) book it as deferred rev[enue] or (better yet) bury it in their trading liabilities."

A Citigroup email makes a similar point: "E[nron] gets money that gives them c[ash] flow but does not show up on books as big D Debt."

Andersen of course knew what was going on. Its internal email states: "Enron is continuing to pursue various structures to get cash in the door without accounting for it as debt."

These are a few of the documents my Subcommittee uncovered that show that the Enron's prepay activity was well-known to its participants, but hidden from everyone else. Each knew that Enron's prepays were designed to manipulate its financial statements, not to achieve business objectives. Each also knew that Enron was booking prepay proceeds as trading activity instead of loans, even though no trade or sale was ever intended. Phony prepays produce misleading financial statements. That's what happened here.

When Enron collapsed and declared bankruptcy on December 2, 2001, it had about $5 billion in outstanding so called prepays that were virtually unknown to the company's creditors, investors, and business associates. This disguised debt contributed significantly to the Enron meltdown and the huge loss to Enron's shareholder.

Deception piled on deception. There are many who are responsible for the massive loss to people relying on pension funds and stock investments. Today we'll shine the light in an area where complexity had been used to hide the truth. Hopefully we'll cut through the darkness and place appropriate level of responsibility on the banks who participated in these schemes.

Senator LEVIN. Senator Collins.

OPENING STATEMENT OF SENATOR COLLINS

Senator COLLINS. Thank you, Mr. Chairman.

Today is the second in a series of hearings held by the Permanent Subcommittee on Investigations into the events that contributed to the collapse of the Enron Corporation. More than 6 months ago, the Subcommittee embarked on a comprehensive investigation of Enron in an effort to gain understanding and insight into what appears to have been a colossal failure of virtually every mechanism that is supposed to provide the checks and balances on which the integrity of our capital markets depend.

I would like to take a moment to praise Senator Levin and the dedicated Subcommittee staff on both sides of the aisle who have been tireless in their efforts to unravel the complex transactions that were purposely designed to confound and confuse. This undertaking has been enormous, and I greatly appreciate the diligent work that has gone into this investigation.

The Subcommittee's first hearing examined the role of Enron's Board of Directors in the company's collapse and found that the Board failed to play its required role as the guardian of the corporation's shareholders. The Board's failures, of course, are only part of the story.

We know now, nearly 8 months after Enron filed for bankruptcy protection, that a web of conflicts of interest, accounting improprieties, high-risk transactions, and the appropriation of corporate assets by Enron executives contributed to the company's collapse. Today, we will examine the pivotal role of another set of players in the Enron story: The financial institutions.

The Subcommittee's investigation has revealed that certain financial institutions knowingly participated in, and indeed facilitated, transactions that Enron officials used to disguise debt and, thereby, make the company's financial position appear more robust than it actually was.

Through the use of structured finance vehicles that included a series of prepaid forward contracts and related swaps, Enron received billions of dollars in cash. A prepaid forward contract, or prepay, is essentially a forward sale agreement in which the buyer receives an up-front payment in exchange for a commitment to deliver goods or services in the future. As the Chairman indicated,

prepays are perfectly legitimate when used correctly, and they are common in the energy industry. When a bona fide prepay is used for a genuine business transaction, it is a perfectly legitimate means to provide needed cash to the seller and a desired commodity to the buyer.

However, as was the case with much of what went on at Enron, these transactions were neither simple nor as they seemed on the surface. Many of the so-called prepays, in fact, were not prepaid forward contracts at all. They did not transfer price risk. They did not use independent third parties. They were not entered into because the purchaser actually wanted oil or gas, nor were their terms driven by anything other than a desire to achieve an accounting end. Instead, they were elaborate circular transactions that were designed to disguise what were essentially loans totaling billions of dollars.

The facade of a prepay enabled Enron to misrepresent the cash it received as funds obtained from the company's operations rather than from financing. From an accounting standpoint, this is a critical distinction. Loans appear on the company's balance sheet as cash from financing or debt. A higher debt load raises questions about the company's borrowing power and ability to generate future profits, and it affects its credit rating. Cash flow from operations, on the other hand, enhances the appearance that the company is doing more business than it actually is and implies that such revenue, because it is from the company's core operations, is likely to continue in future periods.

Enron wanted these deals to be covered in a shroud of secrecy because they knew that they could not stand up to the scrutiny of the light of day. Furthermore, they wanted them to be limited to as few investors as possible in order to maintain the facade. In fact, an internal Enron document explains that the continued use of these transactions "is a sensitive topic for both the rating agencies and banks and institutional investors. The ability to continue minimizing disclosure will likely be compromised if transactions continue to be syndicated."

Maintaining an investment grade rating was vital to Enron. Had the rating agencies been privy to the circular nature of these transactions, they would have considered them to be financing or loans, and they would have factored that fact into the ratings. Full disclosure of Enron's source of capital might well have resulted in a downgrade of its rating.

Although many banks ultimately invested in these transactions, JPMorgan Chase and Citigroup were two of the principal banks involved. Their deals enabled Enron to keep some $8 billion of debt off its balance sheet and, as a result, misrepresent its financial status to the rating agencies and to the investing public.

JPMorgan Chase and Citigroup are two of the Nation's most prestigious financial institutions. That is why I find their involvement so shocking. It appears as though they were willing to risk their reputations to keep an important client—Enron—happy. They participated in crafting the structure of these transactions. They used special purpose, offshore vehicles of their own making as the "independent" third parties. They clearly understood Enron's motivation for wanting to use the prepay structures to hide the true

source of the company's cash flow. This charade led to Enron's never-ending need for more cash in order to pay off previous prepays, creating a merry-go-round of refinancings at the expense of investors.

While the majority of professionals in corporate America are ethical people, the public's faith in corporate integrity and professional judgment has been severely compromised by recent corporate scandals. The markets have been buffeted by both Enron and more recent revelations of corporate wrongdoing. The resulting crisis of confidence is not about the market system but, rather, the information that underpins its very validity, the information about the performance of companies whose shares are traded by investors around the world.

Some accountants, lawyers, investment bankers, analysts, and corporate executives, whose integrity and competence are critical to our system of free markets, have directly contributed to this crisis. Some have failed in their professional responsibilities and made it easier for the direct participants to get away with presenting a misleading picture to investors. The question now is how to restore trust and confidence in the markets and corporate America. Tougher laws, clearer standards, and sure and swift enforcement are part of the answer.

Fundamentally, however, restoring faith in America's capital markets requires that all the players perform their jobs—not just government regulators and prosecutors, but lawyers, accountants, investment bankers, market analysts, corporate management, and boards—in accordance with the spirit as well as the letter of the law. We all share in the responsibility for making our markets operate as efficiently, transparently, and fairly as possible. It is time to stop the practices that are beneficial to a select few and harmful to thousands.

The testimony that we will hear this morning about the role of financial institutions in the Enron debacle should yield valuable lessons for strengthening our free market enterprise system, for restoring public confidence in our capital markets, and ensuring that small investors, in particular, have access to complete and accurate information to guide their investment decisions.

[The prepared statement of Senator Collins follows:]

PREPARED OPENING STATEMENT OF SENATOR COLLINS

Today is the second in a series of hearings held by the Permanent Subcommittee on Investigations into the events that contributed to the collapse of the Enron Corporation. More than six months ago, the Subcommittee embarked on a comprehensive investigation of Enron in an effort to gain insight and understanding of what appears to be a colossal failure of virtually every mechanism that is supposed to provide the checks and balances on which the integrity of our capital markets depend.

I would like to take a moment to praise Senator Levin and the dedicated Subcommittee staff on both sides of the aisle who have been tireless in their efforts to unravel complex transactions that were purposefully designed to confound and confuse. The undertaking has been enormous, and I appreciate all the work that has gone into this investigation.

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We know now, nearly eight months after Enron filed for bankruptcy protection, that a web of conflicts of interest, accounting improprieties, high risk transactions,

and appropriation of corporate assets by Enron executives contributed to the company's collapse. Today, we will examine the pivotal role of another set of players in the Enron story: The financial institutions.

The Subcommittee's investigation has revealed that certain financial institutions knowingly participated in, and indeed facilitated, transactions that Enron officials used to disguise debt and, thereby, make the company's financial position appear more robust than it actually was.

Through the use of structured finance vehicles that included a series of prepaid forward contracts and related swaps, Enron received billions of dollars in cash. A prepaid forward contract, or prepay, is essentially a forward sale agreement in which the buyer receives an up-front payment in exchange for a commitment to deliver goods or services in the future. Prepays are commonly used in the energy industry. When bona fide prepays are used for genuine business transactions, they are a perfectly legitimate means to provide needed cash to the seller and a desired commodity to the buyer.

However, as was the case with much of what went on at Enron, these transactions were neither simple nor as they seemed on the surface. Many of the so-called prepays, in fact, were not prepaid forward contracts at all. They did not transfer price risk. They did not utilize independent third parties. They were not entered into because the purchaser actually wanted oil or gas, nor were their terms driven by anything other than a desire to achieve an accounting end. Instead, they were elaborate circular transactions that were designed to disguise what were essentially loans totaling billions of dollars.

While these transaction were incredibly complicated, they essentially boil down to the following scenario. Enron entered into a contract with an offshore entity to deliver oil or gas at a date certain in the future in exchange for an up-front cash payment. The offshore entity, created by or at the behest of the bank, made the up-front payment to Enron with funds provided by the bank. In many cases, no oil or gas ever really changed hands. The banks understood up-front what their ultimate return would be because they hedged their risk, sometimes with Enron itself. The offshore entity supposedly participating as a trading counterparty, in reality, made nothing but preset fees, and Enron received an infusion of cash without having to disclose it as a loan on its balance sheet.

The facade of a prepay enabled Enron to misrepresent the cash it received as funds obtained from the company's operations rather than from financing. From an accounting standpoint, this is a critical distinction. Loans appear on a company's balance sheet as cash from financing or debt. A higher debt load raises questions about a company's borrowing power and ability to generate future profits and affects its credit rating. Cash flow from operations, however, enhances the appearance that the company is doing more business that it actually is and implies that such revenue, because it is from the company's core operations, is likely to continue in future periods.

Enron wanted these deals to be covered in a shroud of secrecy because they knew they could not stand up to scrutiny in the light of day. Furthermore, they wanted them to be limited to as few investors as possible in order to maintain the facade. In fact, an internal Enron document explains that the continued use of these transactions "is a sensitive topic for both the rating agencies and banks/institutional investors. The ability to continue minimizing disclosure will likely be compromised if transactions continue to be syndicated."

Maintaining an investment grade rating was vital to Enron. Had the rating agencies been privy to the circular nature of the transactions, they would have considered them to be financing or loans, and they would have factored that into their ratings. Full disclosure of Enron's source of capital might well have resulted in a downgrade of its rating.

Although many banks ultimately invested in these transactions, JPMorgan Chase and Citigroup were two of the principal banks involved. Their deals, known as Mahonia and Yosemite, respectively, enabled Enron to keep eight billion dollars off its balance sheet and, as a result, misrepresent its financial status to the rating agencies and the investing public.

JPMorgan Chase and Citigroup are two of the nation's most prestigious financial institutions. Yet, it appears as though they were willing to risk their reputations to keep Enron, an important client, happy. They participated in crafting the structure of these transactions. They used special purpose, off shore vehicles of their own making as the "independent" third parties. They clearly understood Enron's motivation for wanting to use the prepay structures to hide the true source of the company's cash flow. This prepay charade led to Enron's never-ending need for more cash in order to pay off previous prepays, creating a merry-go-round of refinancings at the expense of investors.

While the majority of professionals in corporate America are ethical people, the public's faith in corporate integrity and professional judgment has been severely compromised by recent corporate scandals. The markets have been buffeted by both Enron and more recent revelations of corporate wrong doing. The resulting crisis of confidence is not about the market system but rather the information that underpins its very validity, the information about the performance of companies whose shares are traded by investors around the world.

Some accountants, lawyers, investment bankers, analysts, and corporate executives, whose integrity and competence are critical to our system of free markets, have directly contributed to this crisis. Some have failed in their professional responsibilities and made it easier for the direct participants to get away with presenting a misleading picture to investors. The question now is how to restore trust and confidence in the markets and corporate America. Tougher laws, clearer standards, and swift and sure enforcement are part of the answer.

Fundamentally, however, restoring faith in America's capital markets requires that all the players do their jobs-not just government regulators and prosecutors but lawyers, accountants, investment bankers, market analysts, corporate management and boards–in accordance with the spirit, not merely the letter, of the law. We all share in the responsibility for making our markets operate as efficiently, transparently and fairly as possible. It is time to stop practices that are beneficial to a select few and harmful to thousands.

The testimony we will hear this morning about the role of financial institutions should provide some answers, and should yield valuable lessons for strengthening our free enterprise system, restoring public confidence in our capital markets, and ensuring that small investors, in particular, have access to complete and accurate information to guide their investment decisions.

Senator LEVIN. Thank you very much, Senator Collins. Senator Lieberman.

OPENING STATEMENT OF SENATOR LIEBERMAN

Senator LIEBERMAN. Thanks, Mr. Chairman. I thank you and Senator Collins and your staffs, the staff of the Permanent Subcommittee on Investigations, for your continuing inquiry into the workings of the Enron Corporation and specifically for the meticulous work that you have done in preparing for this hearing, which I think is some of the most significant work that this Permanent Subcommittee on Investigations has ever done, and the history of this Subcommittee is already a proud one.

The work that you have done and the opening statements that you, Senator Levin, and Senator Collins have given amount to a shocking indictment of the great companies that were involved here and a profoundly unsettling picture of the way in which good people at the top of America's economy did some very bad things that have now brought our economy to a very unsettled state and greatly diminished the wealth and security of millions of people, including millions of middle-class Americans who came into the stock market over the last decade.

Today, you focus on an aspect of Enron's activities that has not received much attention, and that is the role of some of the Nation's—indeed the world's—largest financial institutions. To feed Enron's need for cash without appearing to incur debt on its balance sheet, the banks apparently created complex transactions that disguise their true nature and ultimately the true nature of Enron's financial condition.

Enron's lenders apparently even convinced a number of the Nation's largest insurance companies to provide performance bonds covering the risk of Enron's default.

As one judge put it in a case brought against Enron's insurance companies who were balking at paying off these bonds, and I quote,

"Taken together, then, these arrangements now appear to be nothing but a disguised loan," end of the quote from a judge.

In Connecticut, Enron worked out a strikingly similar deal with the Connecticut Resources Recovery Authority where a $220 million investment loan to Enron was disguised as a series of energy transactions in which no energy was actually transferred to Enron. The result, in a chain of reactions, has been extraordinary increases in fees for municipalities throughout the area served by the Connecticut Resources Recovery Authority.

Mr. Chairman, all of these transactions are deeply troubling. They are added evidence that the behavior exhibited by top Enron officials was not limited to a single company. Remember in December when Enron declared bankruptcy and collapsed, we were told that its problems were not systemic. We were told that Enron was a single bad apple in a barrel of otherwise good fruit. Now we know better. We know not only that there were other bad apples in that barrel of corporate America, but that in order for many of Enron's deceptions to occur, Enron needed partners, companies that would agree to be on the other side of questionable trades and transactions.

So the cancer of corporate greed and deceit spread. In the case of billions of dollars of disguised loans, Enron's partners were the world's largest financial institutions—institutions with proud and respected names.

Now, I don't know whether disguising loans as commodity contracts is illegal, but I do know that it allowed Enron to run roughshod over what is supposed to be the hallmark of our securities markets, and that is, individual and corporate investors' access to accurate information about the financial health of publicly traded companies. Enron and its financial partners seem to have designed these transactions, that the Subcommittee has investigated and will illuminate today, explicitly to thwart that ideal.

Sadly, millions of average investors are painfully aware of the consequences of making decisions based on untruthful or inaccurate information, and today's hearings give us one more example of how people at the top of America's economy betrayed the great American middle class which put its hope in the markets and how important it is for us to act together through government and through the private sector to restore investor confidence.

As Senator Levin and Senator Collins particularly said, we should, and I believe will, adopt tough new laws to punish and deter such corporate greed and malfeasance. Business organizations such as the stock exchanges should and are acting constructively and progressively to adopt measures of self-regulation and self-policing. But I must say, Mr. Chairman, as I prepared for this hearing today and was struck at how, again, good people were drawn into bad practices, in the end we all have to acknowledge that the law cannot be everywhere and that business self-regulation, stock exchange rules cannot be everywhere; that ultimately, particularly in a democracy, many of the most critical decisions are made in the privacy of one's own conscience.

And if I may veer from where one normally goes at these hearings, I was thinking, in reading the record for the hearing today, of something I once learned that was written in the Talmud, which

is that in the hour when our own lives are over and individuals are brought before the heavenly court, four questions will be asked, so the rabbis tell us. And the first, amazingly, is: Did you conduct your business affairs honestly? Not, did you believe in God? Did you follow all the particular rituals of your faith? But, did you conduct your business affairs honestly? Because it is in conduct that we ultimately reflect the extent to which we have embraced a set of values.

The other thing I remember having studied once is that of all the metaphorical crowns that one may earn in life, the most important is the crown of a good name. And we have here some corporations that have earned very good names that apparently by the action of individual people in them have sullied those good names.

Senator Levin, Senator Collins, I again commend you and your staff for conducting this extraordinary investigation, for bringing to light the facts that will be revealed today, and in that sense for crying out to those who hold power within America's economy to remember what the facts of your investigation show so clearly that too many forgot, which is, if I may paraphrase from the Bible; Man, people do not live by quarterly earnings reports alone.

I thank you, Mr. Chairman.

Senator LEVIN. Thank you, Senator Lieberman.

Senator Thompson, let me call on you, but first let me thank you and Senator Collins. Your staff has been part of a truly dedicated team of staffers which has brought us to this point, and I think it really represents the best in us as Senators that we and our staffs work this closely together on such a very complex kind of an investigation involving literally millions of pages that have to be reviewed. And I want to thank you both for the staff work that has been so dedicated.

OPENING STATEMENT OF SENATOR THOMPSON

Senator THOMPSON. Thank you, Mr. Chairman. I could not agree with you more about the work of the staff. I was very pleased to see Gary Brown from Nashville, whom I have known since before he became a lawyer, come up and assist in this, and he and Mr. Roach have worked very well together.

This document that these gentlemen have produced is really remarkable. I would hope that everyone would have the opportunity to see not only Mr. Roach's statement today but the document that I believe is attached to it or is an exhibit that will be a public record. It is indeed detailed and complex.

As you know, Senator Lieberman, I have been spending a little time on homeland security and a few other things, but as I got into this very recently, I was very surprised at what I saw. I usually like to wait until the evidence is in before I make too many comments. But I think the comments in this case are right on, from all you can tell from the record and actually hearing from both sides.

And I come away with the feeling that our checks and balances have let us down. We have checks and balances not only in government but in our private sector, in our free economy. And we expect auditors, lawyers, raters, and bankers to deal in certain ways; otherwise, bad things happen. And we have certainly seen a lot of bad

things happen. But, unfortunately, the lessons we learned at our mama's knees about the overwhelming power of money sometime turned out to be true. These investment bankers are making hundreds of millions of dollars in fees to set up these deals and pay themselves back in many cases. They are the ones who receive the money in many cases.

So the transactions are very complicated, but the motivations are not, unfortunately. Apparently what the average person, anyway, and I assume even the average sophisticated institutional investor would assume was debt magically turned out to appear to be cash flow from business. And instead of the debt-to-capital ratio going up, it went down, the company, therefore, appearing to be in better shape than it was.

I understand that we will hear testimony that everybody did it, that, oh, Enron fooled us again. They have to be the smartest people in the world because they fool the smartest people in the world, apparently, consistently over a period of years, while those smart people were, of course, making many millions of dollars off of being fooled. But perhaps everybody did it, perhaps the securities fraud laws tolerate it, but I venture to say we will have an opportunity to find out. It is not this body's job, but I venture to say that we will have an opportunity to find out whether or not the securities fraud laws encompass these sorts of activities and tolerate it.

Thank you, Mr. Chairman.

Senator LEVIN. Thank you, Senator Thompson. Senator Bunning.

OPENING STATEMENT OF SENATOR BUNNING

Senator BUNNING. Thank you, Mr. Chairman. I appreciate you calling this hearing today and all the work that has gone on by staff to prepare this unbelievable document that we have in front of us.

Enron's collapse earlier this year signaled the beginning of a crisis in confidence in this country that continues to have a lasting effect and is still going on. One of the largest accounting firms is in ruins. Brokerage firms are under suspicion. And Congress has spent a lot of its time this year trying to figure out what we can do to prevent another crisis like this.

Unfortunately, it is clear that Enron was not alone in the shady financial dealings. Investors have been burned more than once this year with companies, including WorldCom and Global Crossing, using questionable accounting practices in business transactions. Americans across this country are watching their savings and their pensions dwindle, and many now question the validity of financial statements, the independence of financial advisors, and the ability of boards of directors to provide proper oversight.

Personally, I believe it might take a while for average Americans to feel good about putting their money back into any part of the stock market, and I can't blame them. Company after company, over 1,000 to be exact, have restated their earnings, and all of the major markets reflect that by being in the tank. We are facing a crisis, and I hope that the accounting bill we recently passed will restore at least some of the confidence in the markets.

There is certainly enough blame to go around from Wall Street analysts to credit rating agencies to Enron executives. Too many

people dropped the ball or looked the other way when dealing with Enron, and now we are all paying for it.

As for today's hearings, I look forward to learning more about Enron's use of prepays, especially with some of the companies that helped them in this endeavor. I am particularly interested in hearing from these companies what they plan to do in the future to make sure it is not easy for companies like Citicorp and Chase, JPMorgan Chase, to use and manipulate the markets by the use of the vehicles that they did to enhance the cash flow of Enron.

Thank you, Mr. Chairman. I am looking forward to the testimony.

Senator LEVIN. Thank you.

I want to also thank and single out Senator Lieberman, who is the Chairman of the full Committee, for the strong support that he has personally given to this investigation and helping us to do what we needed to do to review the massive materials that we had to review, and also for his very powerful and eloquent opening statement.

Let me now introduce our first panel of witnesses this morning. At the witness table are Robert Roach, a Counsel and Chief Investigator of the Permanent Subcommittee on Investigations. Bob has been with the Subcommittee for the last 5 years as a valued member of my staff on the Subcommittee. He is accompanied by Gary Brown, Special Counsel for Senator Thompson on the Minority staff of the Committee. That is the full Committee on Governmental Affairs.

Gary Brown and Bob Roach represent a very dedicated team of staffers working together on this Enron investigation for many, many months. We look forward to hearing their analysis of their investigation of the role of financial institutions in Enron's collapse.

Pursuant to Rule VI, all witnesses who testify before the Subcommittee are required to be sworn, and at this time I would ask the witnesses to please stand and raise your right hand. Do you swear that the testimony that you give before the Subcommittee this morning will be the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. ROACH. I do.

Mr. BROWN. I do.

Senator LEVIN. We will be using a timing system today, and about 1 minute before the red light comes on, you will see the light change from green to yellow, which will then give you an opportunity to conclude your remarks. And your written testimony will be printed in the record in its entirety, but we ask that you limit your oral testimony to no more than 10 minutes.

Mr. Roach.

TESTIMONY OF ROBERT L. ROACH,[1] COUNSEL AND CHIEF INVESTIGATOR, PERMANENT SUBCOMMITTEE ON INVESTIGATIONS; ACCOMPANIED BY GARY M. BROWN, SPECIAL COUNSEL, COMMITTEE ON GOVERNMENTAL AFFAIRS

Mr. ROACH. Mr. Chairman, Ranking Member Collins, Members of the Subcommittee, good morning. Earlier this year, Chairman Levin directed the Subcommittee staff to investigate the role of financial institutions in Enron's collapse. The Subcommittee staff—both Democratic and Republican—have worked for the past 7 months on a bipartisan basis to conduct this investigation. We have worked together to review over a million pages of documents and interviewed dozens of witnesses from Enron, Andersen, other accounting firms, credit rating agencies, and a host of financial institutions.

Numerous major financial institutions, both here and abroad, engaged in extensive and complex financial transactions with Enron. The evidence we reviewed showed that, in some cases, the financial institutions were aware that Enron was using questionable accounting. Some financial institutions not only knew, they actively aided Enron in return for fees and favorable consideration in other business dealings. The evidence indicates that Enron would not have been able to engage in the extent of the accounting deceptions it did, involving billions of dollars, were it not for the active participation of major financial institutions willing to go along with and even expand upon Enron's activities. The evidence also indicates that at least in one case these financial institutions knowingly allowed investors to rely on Enron financial statements that they knew or should have known were misleading.

Our investigation, among other things, focused on one financing vehicle known as a "prepay." A prepay is commonly thought of as an arrangement in which one party pays in advance for a service or product to be delivered at a later date. Companies use prepays to receive money up front for services to be rendered in the future.

Enron constructed elaborate, multiparty commodity trades that they called prepays in order to book the proceeds from prepays as cash flow from operations. But when all the bells and whistles are stripped away, the basic transaction fails as a prepay, and what remains is a loan to Enron using an investment bank and an obligation on Enron's part to repay the principal plus interest. With that being true, the proceeds of the so-called prepay transaction should have been booked as debt and not as cash flow from operations.

Now let me describe in general terms why the prepays came about and how they worked. Mr. Chairman, with your permission, one of my colleagues will draw this transaction as I describe it.

Now, first of all, Enron needed more cash flow to show that it could handle its growing debt. One way to address this is for Enron to go and get a loan from a bank such as Citi or Chase. But that would add to its debt load, compounding its problem rather than solving it.

Now, Enron was a merchant energy company. It could engage in trades, and the cash from this type of activity would be accounted

[1]The prepared statement of Mr. Roach with attachments appears in the Appendix on page 215.

for as trading from business operations. However, if Enron and Chase entered into a trade of a commodity such as gas or oil, both parties would be at risk of losing money, depending on the change in value of the oil or gas. And that would be unacceptable to both Chase and Enron in this situation because the objective was to get a fixed amount of cash to Enron, and Chase wanted to be sure it would get its money back with some interest.

So to protect themselves from this uncertainty, Chase and Enron would enter into a second transaction, exactly opposite to the first, which would mitigate or eliminate that price risk. And this is a hedge.

Now, the only problem with this strategy is that these parallel transactions that you see over there cannot be accounted for as legitimate trading activity and would be obvious to auditors. So to help Enron out with its problems, Chase inserted into the trade one of its shell corporations, Mahonia, to engage in a series of trades between three supposedly independent parties.

Now, the trades between each party in the triangle were designed to perfectly offset each other so there would be no price risk. And this is the basic model of what has come to be called "the Enron prepay." Chase forwards a lump sum of money to Mahonia. Mahonia forwards the money to Enron. Enron sends regular deliveries of a commodity, generally oil or gas, back to Mahonia, and Mahonia sends it on to Chase.

Now, the advance of cash from Chase and then the advance of cash from Mahonia to Enron is booked as a trading activity by Enron rather than a loan, and the proceeds—that is the cash it receives—is booked as cash flow from operations rather than as cash flow from financing.

The transactions are worked out in advance by all the parties so that they yield a steady and predictable flow of cash from Enron to Chase, just like a loan repayment. Interest is embedded in the repayment schedule, and in the communications we have seen, the payments are referred to as amortization payments.

The net result is that on the surface this transaction appears to be a series of arm's-length trades among independent entities. However, it is really a set of integrated, prearranged trades that wash each other out, except for the movement of funds from Chase to Mahonia to Enron and eventually back to Chase with some interest payments included.

Now, this is a simplified version of what really went on. Actually, the transactions look more like the charts that we have prepared for the Citi and Chase transactions. I am not going to go into those right now. I think they will be discussed a little later, but that is what they look like. And these transactions fail as legitimate trades for a number of reasons.

Senator LEVIN. Mr. Roach, let me interrupt you just for one second. I have had a brief consultation here, and you can take longer than 10 minutes. We are going to withhold many of the questions so that you will have more time for your presentation.

Mr. ROACH. Thank you, Mr. Chairman.

In order for transactions like the ones used by Enron and the financial institutions to be legitimately booked as cash flow from operations and not debt, four elements had to be present: One, the

three parties had to be independent; two, the trades among the three parties could not be linked; three, the trades had to contain price risk; and, four, there had to be a legitimate business reason for the trades.

The Enron-type prepays we examined failed on all accounts: Two of the three parties in the Enron trades were related—the banks and their offshore special purpose entities which the banks established and controlled; the trades among the parties were linked—contracts associated with the trades were designed so that a default in one trade affected the other trades; there was no price risk—except for fees and interest payments, the final impact of the trades was a wash; neither the banks nor the banks' special purpose entities had a legitimate business reason for purchasing the commodities used in these trades.

Enron used these so-called prepay transactions to obtain more than $8 billion in financing over approximately 6 years, including $3.7 billion from 12 transactions with Chase and $4.8 billion from 14 transactions with Citigroup. This $8 billion figure is a conservative estimate for the 6-year period based on the documents we were able to review. The full amount since Enron began using prepays around 1992 may be much larger.

Now, accounting for prepay proceeds as cash flow from operations rather than cash from financing gave the impression that the money from the prepays was part of Enron's ordinary business activities and not debt. Moreover, the Subcommittee has learned that Enron was simultaneously treating the prepay transactions as loans on its tax returns in order to claim the interest expense as a business deduction.

Enron's practice of using prepay transactions to understate debt and overstate cash flow from operations made its financial statement look much stronger. That, in turn, helped Enron maintain its investment grade credit rating and support, even boost, its share price.

Now, the Subcommittee has done an analysis of what Enron's financial statements would have looked like had it accurately recorded the prepay transactions as debt. Please look at this chart which is marked as Exhibit 104 [1] in the exhibit books. The chart shows key figures from Enron's year 2000 financial statements, the last audited financial statements that the company filed with the Securities and Exchange Commission. The financial statements showed that Enron had total debt in 2000 of about $10 billion, and funds flow from operations in the range of $3.2 billion.

Now, we know from Enron board presentations that at the end of 2000, Enron had about $4 billion in outstanding financing from its so-called prepays. And as you can see from the chart, if Enron had properly accounted for these transactions, its total debt would have increased by about 40 percent to $14 billion, and its fund flows from operation would have dropped by almost 50 percent to $1.7 billion. These are dramatic changes.

Now, the impact on Enron's key credit ratios would also have been significant. These credit ratios are the ratios that financial analysts typically use to evaluate a company's financial health.

[1] Exhibit No. 104 appears in the Appendix on page 355.

Again, looking at the chart, with the inclusion of prepays as debt, Enron's debt-to-equity ratio would have risen from about 69 percent to about 96 percent. Its debt-to-total-capital ratio would have risen from 40 percent to 49 percent, and its fund flow interest coverage, a key measure of a company's ability to meet its financing obligations, would have dropped by almost half, from $4.07 to $2.37 billion. Now, the credit rating agencies testifying in the next panel will discuss the significant effect these numbers would have had on Enron's credit rating.

Any credit rating downgrade would have had serious consequences for Enron, including raising its borrowing costs, limiting the investors who could buy the company's bonds, weakening its trading status, and possibly triggering certain demand debt repayments at off-balance sheet entities affiliated with the company. Enron was acutely aware of the importance of its credit rating and its financial ratios.

Now, the Subcommittee staff has additional analysis regarding the financial impact that would have resulted if Enron had accurately reflected its prepay proceeds as debt, including drops in the company's enterprise value and a significant drop in its implied share price. In the interest of time, however, I will submit that analysis for the record and answer any questions you may have about it. I would also ask that the other appendices to my statement be included in the Subcommittee's hearing record.

Senator LEVIN. They will be made part of the record.

Mr. ROACH. Now, Enron was able to book prepay proceeds as cash flow from commodity trades rather than cash flow from loans only with the assistance of the financial institutions. The banks provided the funding for the prepays, participated in the required complex commodity trades, and allowed Enron to use their offshore entities that they controlled as sham trading partners, for the explicit purpose of allowing Enron to disguise its multi-million-dollar loans as trading activity.

Internal communications show that it was common knowledge among Enron, Chase, and Citigroup employees that the prepays were designed to achieve accounting, not business, objectives and that Enron was booking the prepay proceeds as trading activity rather than debt. The evidence indicates that Chase and Citigroup not only understood Enron's accounting goal, but designed and implemented the financial structures to help Enron achieve its objectives. Moreover, they accepted and followed Enron's desire to keep the nature of these transactions confidential.

By design and intent, the prepays as structured by Enron and the financial institutions made it impossible for investors, analysts, and other financial institutions to uncover the true level of Enron's indebtedness.

And the financial institutions marketed these structures to other potential clients. Chase developed a pitch book to sell other companies on Enron-style prepays. The pitch book describes the transactions as "balance sheet 'friendly.'" It also sets out in general terms Chase's use of Mahonia in structuring the trades and clearly explains that the trades are orchestrated to work together. This explanation of the deliberate packaging of the trades flatly contradicts claims that the trades are independent and unrelated.

Chase apparently entered into Enron-style prepays with seven companies in addition to Enron.

Citigroup also developed a presentation to sell companies on Enron-style prepays, promoting, in particular, the Yosemite structure it had developed to raise money for the prepays from third-party investors without explicitly informing them of the transactions. And you can see—well, we had a copy of the Yosemite structure up earlier. The Citi presentation boasts that the structure "[e]xpands capability to raise non-debt financing and . . . improve cash flows from operations" and "[e]liminates the need for Capital Market disclosure, keeping structure mechanics private." Citi sold its prepay structure to two other companies and shopped the Yosemite structure to 14 other companies.

This shows that Enron is not the only company obtaining loans disguised as commodity trades and recording cash flows from operations instead of from financing. Major financial institutions are knowingly assisting and even promoting such transactions, which would not be possible without their willingness to provide the funds, the paperwork, and a sham offshore trading partner.

Thank you. Mr. Brown and I would be happy to answer any questions you may have at this time.

Senator LEVIN. Thank you. I do not have any questions. Your statement is very thorough and clear analysis, and I will see if any of my colleagues have questions.

Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman. I only have a couple of questions, but I, too, want to join in complimenting the staff for its hard work and the excellent presentation as well as the invaluable assistance that we have received from Mr. Brown.

Mr. Roach, as you indicated, one requirement of a legitimate prepay is that there has to be a legitimate business purpose for the transaction. During the course of the investigation, were you ever made aware of a particular need that either of these banks had for oil or gas, or was the nature of the commodity involved essentially not relevant from the banks' perspective?

Mr. ROACH. With respect to these particular trades, it was irrelevant.

Senator COLLINS. So this was not a case where there was a legitimate need for the commodity by the bank; is that correct?

Mr. ROACH. That is correct.

Senator COLLINS. Mr. Brown, you have a great deal of experience with securities laws and I would like to ask you to comment on an issue that was not touched on in Mr. Roach's testimony. Do you believe that securities laws might be implicated in some of these prepay transactions, and specifically I would like you to comment on how the term "fraud on the market" might apply in the context of what we are hearing about.

Mr. BROWN. Well, as far as implication of securities laws, sure, they're implicated in the mere sale of the Yosemite notes, for example. The sale of the Yosemite notes implicates the securities laws since those are obviously securities. And so an issue that naturally arises there is whether or not the investors who bought those notes received truthful and accurate information, not misleading infor-

mation, in terms of the offering memorandum and any presentations that were made to them.

The term "fraud on the market" is a term that comes up in what you see in some of these securities class actions, where, quite frankly in a situation like Enron, over a period of time the company's stock price is supported in the marketplace by what is false and misleading information but the public doesn't yet know about it. When that becomes known, then the market price drops, and so people who buy stock during that time period have been defrauded. How that can be implicated in a situation like this is whether or not any persons who are actively engaged in assisting the company in misstating its public financial statements, whether or not those people can be determined to be engaged in securities fraud and either prosecuted or held civilly liable. So that's how those would operate.

Senator COLLINS. Thank you, Mr. Chairman.

Senator LEVIN. Thank you, Senator Collins. Senator Lieberman.

Senator LIEBERMAN. Thanks, Mr. Chairman.

And again, thanks to both of you for extraordinary work. Two quick questions.

Mr. Roach, this one picks up on what Senator Collins asked. The charts that you gave us showed a trail of commodity transactions, in your case, oil. Obviously, no oil actually changed hands here; is that correct?

Mr. ROACH. Well, Senator, there was at times what they would call physical transfer, but it was really simply a transferred title.

Senator LIEBERMAN. And ultimately, the paper went in a circle; am I right?

Mr. ROACH. Yes, sir, most of the time it went into a circle, went through a circle.

Senator LIEBERMAN. So that it came back to where it started, without any other immediate effect, at least regarding the commodity.

Mr. ROACH. That's right. On most occasions that's what happened.

Senator LIEBERMAN. Just to the best of your knowledge, are the financial institutions with which Enron entered into these trades, generally in the business of buying and selling commodities?

Mr. ROACH. That gets a little bit beyond my ken. But I can comment on this, that these are financial institutions which engage in all kinds of commodity transactions, and so they do have businesses which do engage in the trading of oil and gas. But this is a bit different when they sit down and prearrange it all in advance.

Senator LIEBERMAN. And prearrange it with the third party involved being a corporation that they themselves set up. In other words, Enron, financial institution, and the third party is of their own creation.

Mr. ROACH. The bank's creation, that's correct.

Senator LIEBERMAN. Mr. Roach, the financial institutions, as I have seen the press coverage of this leading up to today, argue, and I presume they will today, that these prepaid agreements are often-used financing mechanisms and that there is nothing inherently wrong with using them, either in general or in the specific case of Enron. In addition, the financial institutions argue that it is not

their responsibility to make sure that their clients such as Enron properly account for and report such transactions.

I wanted to ask you now whether it is your conclusion, based on the investigation that you and your colleagues have done, that the financial institutions involved here did in fact know how Enron intended to use these transactions, and in that sense that they aided and abetted Enron's intent to mislead investors and credit rating agencies?

Mr. ROACH. Unquestionably. The documents that we have reviewed show that the financial institutions clearly understood what Enron's objective was in engaging in these transactions.

Senator LIEBERMAN. Thank you, gentlemen.

Thank you, Mr. Chairman.

Senator LEVIN. Thank you very much. Senator Thompson.

Senator THOMPSON. Thank you very much.

Gentlemen, thank you very much for the work you have done here. It is extremely complex for most of us, but I think you have synthesized it as well as anybody could, and I recommend these exhibits for those who understand these issues and want to know more about how these things work.

As I look through here, it looks like there are two basic issues or two basic problems. One has to do with the use of these forward contracts that you have described, which basically turn liabilities into cash flow and affects the debt equity ratio. But then there is another set of issues, it seems to me, where you take issue with the fact that these investment bankers put out offering memos, prospectuses, to investors in order to sell these instruments to—I guess they are all qualified institutional investors. Let us take Yosemite, for example. There is apparently, from looking at your documents, the prospectus did not include substantial debt that should have been included in that prospectus. Was this debt based on these contracts that we have been talking about? How do those two issues interrelate?

Mr. BROWN. It is a couple of things. There is an issue whether there should have been some additional supplemental disclosure about what had been identified as off-balance sheet debt and whether or not that would have been important to the investors purchasing the notes.

The second aspect of that is whether Enron's overall financials——

Senator THOMPSON. Excuse me. Before you get off that. When you say "off-balance sheet debt," what are we talking about there?

Mr. BROWN. Well, there were—well, some things like—we've all read about and seen—Jedi, Chewco, and then there was an analysis done by one of the investment banks, and they've subsequently corrected a portion of it, but what they refer to as off-balance sheet or non-debt structures, that it would be very difficult for someone to pick up and know about, which would affect the debt-to-capital ratio and other key financial ratios relied upon by the credit rating agencies.

Senator THOMPSON. So there was an issue as to how that category of item should be reported.

Mr. BROWN. Right.

Senator THOMPSON. Go ahead.

Mr. BROWN. The second aspect of it is what has been alluded to I guess in several of the Senators' statements and also in Mr. Roach's testimony, and that is just the overall effect of these prepays on Enron's financial condition in general. I think it is interesting to note that when Enron failed last fall, the big news at that point was over a 3½-year period, approximately $2.5 billion of debt was put back on the books.

Well, here you are talking about transactions that put $2.5 billion of debt—but not classified as debt—on the books, in a year.

Senator THOMPSON. Are these the prepaid contracts?

Mr. BROWN. Right. And so there is the issue of whether or not Enron's financial statements, as a whole, which were incorporated into these offerings, were rendered false or misleading by the characterization of these transactions as trading liabilities as opposed to debt, and cash flow from operations as opposed to cash flow from financing. Now, when Mr. Turner testifies in a little while, he will be much more qualified than I to tell you about the implications of those characterizations.

But suffice to say that technically you'll hear some technical compliance with Generally Accepted Accounting Principles (GAAP) does not mean that the financial statements or the document is nevertheless not false and misleading, and there's law to that effect.

Senator THOMPSON. So breaking it down in the simplest terms, when the prospectus went out, it did not include some of these items that you were talking about that at least arguably should have been disclosed as Enron debt; is that correct?

Mr. BROWN. Right. And again, whether or not the characterization of the debt recordation, characterization of the cash flow, the known use of the proceeds of the transaction to fund or prepay other items like that, whether or not that would have been important disclosure in the offering memorandum.

Senator THOMPSON. Well, I think we know what the institutional investors say about that or are going to say about that. They clearly say that that would have been important to them. If that is important to them, it would have had some impact on their decision to invest.

Do you know whether or not these mortgage bankers actively sought to keep from disclosing, keep those items from being known?

Mr. BROWN. I believe there are some emails which indicate that when questions started to be raised about what assets are in the trust, the order comes down, I think, as to shut it down, or "Let's shut this down to keep people from asking about it."

Now, inherently, in fairness, there's nothing wrong with structured finance that includes a blind pool trust. There's nothing wrong with that. It's just when you combine it with all these other things that you raise potential questions about whether or not there would have been appropriate supplemental disclosure and whatnot.

Senator THOMPSON. Such as a three-party deal that was not at arm's length, an offshore company that had no business purpose other than to create the booking entry that was created, that sort of thing?

Mr. BROWN. Yes, sir.

Senator THOMPSON. Thank you, Mr. Chairman.

Senator LEVIN. Thank you.

Following the early bird rule, Senator Bunning.

Senator BUNNING. Thank you, Mr. Chairman.

I would like to ask Mr. Roach, how does Arthur Andersen fit into how these prepays were structured and accounted for?

Mr. ROACH. Well, Senator, we have seen documents that Arthur Andersen provided guidance documents to Enron as to what types of criteria they needed to follow in order to ensure that these transactions comply with accounting rules, and in fact the four points that I had mentioned in my statement—and I think we will see an exhibit on it later—those were actually taken from an Arthur Andersen presentation that we acquired under subpoena from Enron, and we had also seen other documents that discuss that in a similar way.

So they were clearly providing them guidance on what they should and should not be doing.

Senator BUNNING. How to set up the prepays?

Mr. ROACH. Yes, and saying this is what you need to do in order to make sure it falls within the accounting rules.

We have interviewed some Arthur Andersen accountants who worked on this, and the one thing that sort of comes across—it's not clear to us, we're still trying to work this out—it's not clear whether they really knew everything that was going on with these deals. I would say that's still an open question, but from the interviews thus far, there are certainly some issues that we've discussed with them that they profess that they didn't know about, and that could have caused further questions about the way in which these transactions were accounted for.

Senator BUNNING. In the testimony by JPMorgan Chase that we will hear later today, they say that neither Chase nor Enron has an ownership interest in Mahonia and that Mahonia's officers and directors made the decision to enter into specific transactions. Do you know who the officers and directors of Mahonia are, and were they completely separate from Chase?

Mr. ROACH. We know who they are. It is a group over in the Isle of Jersey called Mourant & Company. It's a firm that provides administrative and corporate services to corporations. And those individuals serve as the officers and directors of Mahonia. Material, which will be discussed later, indicate that while there is probably a legal separation between Chase and Mahonia, there certainly are multiple indicia of control over the entity and the way in which the relationship between Chase and Mourant and then subsequently Mahonia work.

Senator BUNNING. In other words, Chase controlled Mahonia.

Mr. ROACH. That's our belief. And it was set up specifically to affect that situation, that the entity would not——

Senator BUNNING. The transactions——

Mr. ROACH. Well, it was set up so that Chase would not own it, be able to control it.

Senator BUNNING. I understand. But they did it for that specific purpose.

Mr. ROACH. To control it, but not own it, yes. And it was involved in those other transactions other than those engaged with Enron.

Senator BUNNING. Last question. In your testimony I believe you said that Enron was treating the prepaid transactions as loans on its tax returns to get a business deduction, but was not counting the prepays as loans on its financial statements. Is that correct?

Mr. ROACH. Yes, sir.

Senator BUNNING. How does that happen if you have an accountant? If I did that on my own tax returns, I would go to jail, directly to jail, and do not pass go and not collect $200, as they say in the game of Monopoly.

Mr. ROACH. Well, Senator, I'm not a tax expert, but what we have been told in the course of our interviews is that there are sometimes situations where for purposes of accounting and financial statements, you can treat cash flow in one way and then for purposes of taxation treat it as another.

What we do know is that through interviews of the people in the tax department of Enron and memos that we have obtained, that there was a judgment made within Enron that they could, for tax purposes, treat these—the income from these transactions—as loans.

Senator BUNNING. And still show them in another manner for the public to see?

Mr. ROACH. Yes, sir.

Senator BUNNING. Thank you, Mr. Chairman.

Senator LEVIN. Thank you, Senator Bunning. Senator Carper.

OPENING STATEMENT OF SENATOR CARPER

Senator CARPER. Thank, Mr. Chairman.

To our witnesses, thank you for being here and for your testimony. I am balancing between a couple of different hearings, and I missed much of your statement.

Let me just ask a couple of related questions revolving around the issue of motivation, and I am interested in your thoughts on what was the motivation for Enron to enter into these transactions? What was the motivation for the banks who were involved in these transactions? What was the motivation for the investors to invest in these transactions? And finally, at the end of the day, who gets left holding the bag?

Mr. ROACH. I guess I do because Mr. Brown is drinking water. [Laughter.]

I mean it is hard to ascribe motives. What we have seen in documents clearly indicate that the situation with Enron was that it was showing incredible amounts of income in its financial reports due to the accounting mechanisms it employed to take advantage of these long-term contracts that it had been signing. The income, that high level of income allowed them to acquire a lot of debt. The problem is when analysts and credit-rating agencies began to look at the entire financial condition, there was a problem because the cash flow that Enron was bringing in didn't seem to be sufficient enough to support that level of debt. So the problem Enron had was that it had to bring in more cash in order to show people that it could carry the debt load that it had.

Well, it had some problems. Its assets were not very good, and in fact, as we've seen in a number of cases, probably being carried on its books at a much higher value then they really were, so selling those assets wasn't going to help them much. There were problems with trading off legitimately part of its trading book. So they didn't have many options left. If they went—and as I said earlier in the presentations, if they went out and got a loan, that wasn't going to help them because that money would be shown as additional debt. So structuring these transactions in the way they did solved the problem. They could take the cash that they received from these transactions, and count it as cash flow from business activities, and at the same time not record it as debt. So that is the motivation here with Enron.

Senator CARPER. I thought that was an excellent explanation.

Mr. ROACH. Thank you. It's a little more difficult to understand what the motives of the banks were. I mean, there are certain communications you can see that allow you to infer what's going on. I mean clearly Enron was a big player on Wall Street at that period of time. They were doling out lucrative contracts for a lot of business to a lot of people. And Enron was not shy about telling the potential suitors that if you want our business, you have to belly up to the bar. We want to see you involved in our activities helping us out. And we do see memos to the effect that not only the two financial institutions that are here today, but other financial institutions were very well aware of that, and were often very concerned about how what they were and were not doing with respect to Enron's request affected their ability to get business in the future. Whether that's the full motivation I don't know, and as I said, I'm trying to be specific here, that we've seen this in memos, that's maybe one reason, but I don't want to say that's fully it or specifically it.

A little more difficult with the investors, and I think we ought to let Mr. Brown talk about that.

Mr. BROWN. The investors, particularly in Rule 144A transactions, there are a series of institutions that are always looking to park funds and get good rates of return, which they were getting from what at the time everyone would say, Fortune 10 company, CEO or CFO, and all the other management team were being praised as the second coming. They'd look at it and people could very easily say, good return; what's the risk here? Let me sign up. And so that's certainly going to be the motivation from people who were investing in notes and investing, quite frankly, in the stock.

Who gets left holding the bag, I guess, at the end of the day will be determined in bankruptcy court and in litigation, where there's numerous claims and cross-claims among investors, investment banks, shareholders, lenders, and the rest. So I mean it will be a long process determining who ultimately does hold the bag.

Senator CARPER. Thank you both very, very much.

Thanks, Mr. Chairman.

Senator THOMPSON. Mr. Chairman, could I follow up on Senator Carper's question a little?

The documentation you have here seems to indicate that in terms of the motivation of the bankers, that substantial amounts of these transactions, the money coming in from these transactions,

were going to pay off the bankers themselves, from indebtedness that Enron owed to them; is that correct?

Mr. ROACH. Well, yes, sir. What began to happen—and I think Senator Collins mentioned this in her statement—I mean it sort of became a merry-go-round. The money brought in in prepays went to pay off the earlier prepays. This was particularly true in the Yosemite structure. The first offering for Yosemite was $800 million. And those funds were provided to the prepaid transaction, and when Enron received that money it used the $800 million to pay off two prior prepays, one named Roosevelt and the other named Truman. I don't pick the names, I just deliver them.

And in the second Yosemite a similar thing happened. I believe there was about 200 million pound sterling raised in that offering and those went to prepay transactions, and they were used to repay prepays as well.

Senator THOMPSON. So how much of that went to the bankers though is what I am getting at. Give me the extent of the——

Mr. ROACH. Well, in the end, the banks were the initial source of the funds for the prepays. So when that would happen—for example, in Yosemite structure what's really happening here is Citicorp is transferring the credit risk that it held out into the capital markets.

Senator THOMPSON. For how much? How much credit risk were they——

Mr. ROACH. Well, they were ultimately on the hook for the entire amount of the value of the prepay. So, for example, at the time of Yosemite, I think the remaining value of the Truman prepay was about $675 million, and the remaining value of the Roosevelt prepay was about $125 million.

Senator THOMPSON. So how much of that were they able to take care of in the subsequent prepays, all of it?

Mr. ROACH. Well, the entire amount because the entire $800 million raised in Yosemite was used to pay off those previous prepays.

Senator THOMPSON. Thank you, Mr. Chairman.

Senator LEVIN. Thank you very much to both of you again.

And we will now move to our second panel. Let me introduce you and you can remain standing. This will be very brief. First at the witness table, we have Lynn Turner, who is a former Chief Accountant with the Securities and Exchange Commission from 1998 to 2001.

From Moody's Investor Service we have Pamela Stumpp. She is the Managing Director and Chief Credit Officer of the Corporate Finance Group. And John Diaz, the Managing Director of Power & Energy from Moody's Investors Service.

Ronald Barone, Managing Director of Utilities, Energy & Project Finance Group, Corporate and Government Ratings; and Nik Khakee, Director of Structured Finance.

This is a very distinguished panel that we have before us. We look forward to your testimony. And pursuant to Rule 6, as I indicated, all witnesses who testify before our Subcommittee are required to be sworn. I would ask you to raise your right hands and ask you this question: Whether or not you swear that the testimony which you give before this Subcommittee will be the truth, the whole truth and nothing but the truth, so help you, God.

Mr. TURNER. I do.
Ms. STUMPP. I do.
Mr. DIAZ. I do.
Mr. BARONE. I do.
Mr. KHAKEE. I do.

Senator LEVIN. Thank you. We would note again that the written testimony will be printed in the record in its entirety. We ask the oral testimony be no more than 10 minutes, and that green light will disappear after about 9 minutes, at which point there will be a 1-minute warning before the red light comes on, which will give you the opportunity to conclude your remarks.

Let me start with Mr. Turner.

TESTIMONY OF LYNN E. TURNER,[1] FORMER CHIEF ACCOUNTANT, SECURITIES & EXCHANGE COMMISSION, BROOMFIELD, COLORADO

Mr. TURNER. Thank you, Chairman Levin, Senator Lieberman, and Senator Thompson. I testified at the first Senate hearing that was held by the full Committee with Chairman Levin, and at that point in time as I recall, both Senator Lieberman and Senator Thompson said this would be a long road and it would take a lot of determination to get us to the end of it, and I commend all of you for the fine work that you and the staff have done. To that degree, I think the staff have done a fabulous job in trying to get to the bottom of the issue.

There's no question, what we've already heard today, that the investors have lost confidence and trust in the markets is absolutely true. It's evidenced probably best by the downward spiral that we've seen in the markets that in the last few weeks have even turned into what some would say is a free fall, and as a result of that, we've seen investors lose in excess of $5 to $6 trillion of value which is phenomenal.

The impact of that on America and now on our economy is turning out to be very real and in some cases devastating. It is interesting to note that back in 1929, when we had the market crash, there were only 1.5 million Americans that were affected by that. Today there's 85 million Americans. One out of every two Americans are being impacted—voting Americans are being impacted—by that today. So it has a much broader impact, and as a result, we're seeing, I think, the concern, the frustration, certainly the disgust in some cases on the part of Americans with that, although I think we have to make sure that we understand we can't paint all market participants, all people on Wall Street with the same broad brush. But notwithstanding that, it is important that all market participants play a key and important role in making sure that the financial information that is provided to investors has a high degree of honesty and integrity, and quality and transparency behind that.

In fact, for the people to my left here to be able to do their job properly, they have to know that the CEO amendment CFO, the financial executives, have got the numbers done right, that the auditors have checked that, that the corporate boards have exer-

[1] The prepared statement of Mr. Turner appears in the Appendix on page 265.

cised, like an eagle, their oversight of that process, so that they then get good quality transparent information from which they can make judgments. Without that, the credit rating agencies would be unable to fulfill their responsibility to the public. And with that as a backdrop, I think the whole Committee and Subcommittee is to be commended for asking what role Wall Street has played in these particular transactions, and in particular these two financial questions.

There's no question that people need to ask things. What was their role in this in structuring and engineering and financing these transactions, and then executing them.

As Senator Collins said in her opening remarks, perhaps this is happening all too often. From my vantage point as the Chief Accountant at the Securities and Exchange Commission, as a CFO, and as a partner of Coopers & Lybrand, I can tell you quite frankly it is business as usual. It happens day-in, day-out, every day on Wall Street. Quite often at the SEC we would spend a significant amount of time finding these transactions and then trying to put a lid on them. As the CFO, I was actually urged by members of Wall Street to undertake accounting that was woefully inadequate and in violation of the SEC rules. I might note we didn't do it. I had a great CEO and a great board, and quite frankly, each one of the Big Five accounting firms has an on-call group that works very closely in conjunction with Wall Street in carrying out and designing and engineering these transactions to ensure that they get disguised and hid from the investors.

And with that though, let's get into the accounting for just briefly for a moment here as we try to summarize this. There are so many of these transactions because they are being done day-in and day-out that the Financial Accounting Standards Board can't write a rule for every single one of them. Not enough time, not enough resources to do that. But there are some general guidelines, general principles. And some of those clearly say, as I outlined in my written statement, that what we do is we look through to the substance of the transaction, and there are some rules in black and white that talk about that. And in my statement I note that the SEC, for example, has objected, and it's in black and white to transactions going off-balance sheet when you just came up with a nominally capitalized SPE like what we have here in Mahonia or Delta, and just insert that into the transaction, try to get off the balance sheet.

Task forces of the FASB have also come out in black and white and talked about situations where securities are issued and purchased, and I'll say, "for the sole purpose of achieving a desired accounting results, and the transaction considered individually would serve no valid business purpose or would not be entered into otherwise." In those situations we look right through the structure to find out what the substance of it is, and if it's debt, it needs to go on the balance sheet as debt.

So as you can see in this particular case, it's not an issue of being the gray. This is an issue of black and white. And leaving these liabilities up in the trading credit risk area, rather than showing them as a true loan to the bank is just absolutely wrong. Now, some would argue that who cares—and I think you will hear

some arguments as long as it was a liability on the bank, should we care at all? Or on the balance sheet, at least it's there. And I think the answer is very much so. That's why the SEC has promulgated very clear rules that say each material line time on the balance sheet needs to be separately broken out. You cannot aggregate them all and just show them one line item on the balance sheet, and I can guarantee you that as the CFO at my former employer, if I had prepared financial statements and had just one line item on my balance sheet and we're a large international semiconductor, and I had of gone to either of these institutions and asked them for financing, just said, liability, hundreds of millions of dollars, there is no way that their own banking divisions would have ever given me a loan on that basis.

There's also a question being raised here about the reporting for the cash flows. In a statement that the Financial Accounting Standards Board issued Statement No. 5 on reporting a cash flow, the FASB decided—and I think appropriately so—by rule, that you have to break out where the sources of your cash are coming from so that investors could see is it being generated by normal business operations or is it coming from the banks who are providing you financing, or is it coming from sales of assets, so that investors can currently tell what's going on with the business and how well management is doing in achieving their goals.

When you turn around and put these cash flows from these financing vehicles up in the statement of cash flow from operations, then there is no question it misleads investors and there is no question it will mislead the credit rating agencies, and the analysts into thinking that the business is doing much better, it's generating as lot more cash than it really is, which it can then turn around and use or lacks to use to pay off the bank debt. And to that degree, I think investors on this particular case were woefully misled.

It's also interesting to note that in a court case back in 1969, that the judge in that, on appeal in the U.S. Court of Appeals for the second court, noted that notwithstanding what the GAAP rules are, they kind of provide a minimum floor that if in fact there's material information out there that investors are entitled to or should know, then you need to get that information in the filing. The judge turned around and said that proof of compliance with Generally Accepted Standards was evidence which may be persuasive, but not necessarily conclusive, and in that case, that the facts were certified were not materially false or misleading, so he says you got to go beyond GAAP if there's material information.

And interesting enough, he goes on to say that when someone becomes aware of something that may be in compliance with GAAP, but more information is needed, the judge said, "Once he has reason to believe that this basis assumption is false, an entirely different situation confronts him. At least this must be true when the dishonesty he has discovered is not some minor peccadillo, but a diversion so large as to imperil, if not destroy, the very solvency of the enterprise," which is exactly what we have in the Enron situation. And so with that I think it is just a matter of black and white. These numbers should have gone on the balance sheet as debt without a question.

And let me just finish by commending the Senate, the 97 Senators that voted for the Sarbanes Bill. I think the Sarbanes Bill will help, will go a long ways to solving some of these problems. Certainly the Auditor Independence Provisions in there would cease the auditors from being involved in helping structure these transactions to keep them away from the public, and certainly I think will bring the confidence of the public back to the market. So I commend all 97 of you for having taken that serious undertaking.

Senator LEVIN. Thank you very much, Mr. Turner. Ms. Stumpp.

TESTIMONY OF PAMELA M. STUMPP,[1] MANAGING DIRECTOR, CHIEF CREDIT OFFICER, CORPORATE FINANCE GROUP, MOODY'S INVESTORS SERVICE, NEW YORK, NEW YORK, ACCOMPANIED BY JOHN C. DIAZ,[1] MANAGING DIRECTOR, POWER & ENERGY GROUP, MOODY'S INVESTORS SERVICE, NEW YORK, NEW YORK

Ms. STUMPP. Good morning, Mr. Chairman, Senator Collins, Senator Lieberman and Senator Thompson, and Members of the Subcommittee.

My name is Pam Stumpp, and I am Managing Director at Moody's Investors Service and the Chief Credit Officer for the Corporate Finance Group. I am joined by my colleague, John Diaz, who is a Managing Director in our Power & Energy Group. On behalf of Moody's, we're pleased to appear before you today at your request regarding your investigation into the role of the financial institutions in the collapse of Enron.

For over 100 years Moody's has played an important part in providing informed and independent credit analysis to investors. We are proud of our history as the world's oldest credit rating agency, and we're cognizant of the responsibility that this legacy confers upon us. It was with this responsibility in mind that we accepted your invitation to share our views on the critical issues before you. At a time when America's faith in the integrity of its corporations and the stability of its financial markets is badly shaken, we applaud the efforts of this Subcommittee, the Congress, the Securities & Exchange Commission, to investigate Enron's failure, and identify the larger lessons that can be learned from the company's collapse.

We are especially interested in these issues because our ratings depend heavily upon the integrity of the public financial statements provided by corporations. In our assessment of a company's creditworthiness, Moody's analysts begin with the premise that the issuer's SEC filings and audited financial statements are accurate. We them bring the benefit of our experience and expertise to our analysis. But as the Enron situation has demonstrated, where the principle of transparent public disclosure is abandoned, neither we nor the regulators can properly fulfill our obligations to the market and investors globally.

Before discussing Enron and related issues in more detail, it is important for me to note that Moody's did not have any knowledge, prior to Enron's bankruptcy, of the existence of Enron's prepaid for-

[1] The prepared statement of Ms. Stumpp and Mr. Diaz with an attachment appears in the Appendix on page 278.

ward and related swap transactions. Even today our understanding of the specifics of these transactions is restricted to what we have gleaned from press accounts and conversations we have had with the Subcommittee staff at their request. Based on our limited knowledge, these transactions appear to have been a form of financing. If such transactions had been accounted for as a loan, Enron's operating cash flow would have been reduced and its debt would have been greater. The disclosure of these transactions as loans would have exerted downward pressure on Enron's credit rating.

Of course, knowing all that we do know today about the true nature of Enron's corporate enterprise, it is clear that Enron had not been an investment grade company for several years. The compounded impact of these transactions alone on Enron's financial framework may have resulted in the lower rating and perhaps an earlier downgrade to below investment grade status. More fundamentally, however, Moody's would have questioned management's motivations to have implemented such a structure.

As Moody's does with all corporate entities, we expressed to Enron our views regarding its creditworthiness. Specifically Enron was rated in the Baa category, Moody's lowest investment grade level. Entities rated Baa contain speculative elements. We had communicated to Enron that its Baa rating reflected its high level of debt relative to its operating cash flow. Consistent with Moody's practice not to recommend that corporate issuers follow specific courses of action, Moody's did not instruct or suggest that Enron employee prepaid transactions or other artificial means to increase operating cash flow or to understate debt levels.

Moody's did provide ratings for the notes issued by Citibank-sponsored Yosemite Trusts I and II, as well as the several Enron Credit Linked Notes Trusts. We viewed these transactions to be a means through which Citibank reduced its level of Enron risk. We have submitted, along with this opening statement a diagram of the Yosemite structure as presented to us in the offering memorandum. Yosemite was a structure of the type that our structured finance group examines and rates frequently. The purpose of these structures is essentially to transfer the credit risks associated with a particular company to third-party note holders.

In this instance a trust was created that issued notes to investors. Citibank was obligated to make payments to the trust, which were then passed to investors. Citibank was not obligated to make these payments if Enron failed to pay on its senior note obligations or filed bankruptcy. In exchange for principle and interest due under the notes, the investors assumed the risk that Enron might go into bankruptcy or fail to pay on its obligations. Therefore, the likelihood that the note holders would receive the promised returns on these notes was linked directly to Enron's creditworthiness.

It should be stressed that structured financing is a common risk management tool available globally to corporations, financial institutions and State and local governments. It is a recognized method, for example, of enhancing liquidity and of transferring credit risk when appropriately implemented. What might seem to be a complex structure can in fact genuinely accomplish one or more of these goals. The Yosemite transaction transferred Enron risks ex-

actly as they intended to. The problem was that the actual Enron risk was different from that portrayed by Enron's incomplete and misleading financial disclosures.

The securities market can only function efficiently with transparent and credible financial information. It is critical to strengthen these elements of our financial infrastructure and bolster investor confidence. As a major consumer of publicly-available information, we support rule changes by the SEC and Congress that enforce transparency and penalize corporate deception. Furthermore, we endorse a principle-based approach to accounting, rather than a rules-based approach. Accounting that promotes adherence to the spirit and the letter of the rules would strengthen the foundations of our financial system.

At this critical juncture, we hope all market participants step forward to offer confidence-building measures. As far as Moody's is concerned, we are expanding our knowledge in key disciplines that have come to influence credit risk. We are recruiting specialist teams with particular expertise in credit-related areas such as accounting quality, corporate governance and off-balance sheet risks. These teams will supplement the work of our credit generalists in their analysis of a company's creditworthiness. We hope that our independent assessment of financial reporting and corporate governance will improve market transparency and contribute to the restoration of confidence in our capital markets.

Finally, as an institution that views its role in the capital markets with both pride and great seriousness, we welcome the opportunity to assist this Subcommittee in examining the shortcomings of the present system and in working toward effective solutions. Therefore, on behalf of our colleagues at Moody's, John Diaz and I would like to thank you for the opportunity to appear today, and we look forward to answering your questions.

Senator COLLINS [presiding]. Ms. Stumpp, thank you so much for your testimony. We only have about 2 minutes remaining in the vote that is under way, so Senator Thompson and I are going to go vote. Senator Levin will be back very shortly, and will reconvene the hearing, but I will put the hearing in recess until he returns. Thank you for your testimony.

[Recess.]

Senator LEVIN [presiding]. The Subcommittee will begin again. And I believe Ms. Stumpp has completed her testimony, and so we will move to Mr. Barone.

TESTIMONY OF RONALD M. BARONE,[1] MANAGING DIRECTOR, UTILITIES, ENERGY & PROJECT FINANCE GROUP, CORPORATE AND GOVERNMENT RATINGS, STANDARD & POOR'S, NEW YORK, NEW YORK; ACCOMPANIED BY NIK KHAKEE,[1] DIRECTOR, STRUCTURED FINANCE GROUP, STANDARD & POOR'S, NEW YORK, NEW YORK

Mr. BARONE. Good morning, Mr. Chairman, and Members of the Subcommittee. I am Ronald M. Barone. From 1994 until Enron Corporation's bankruptcy in December 2001, one of my roles at

[1] The prepared statement of Mr. Barone and Mr. Khakee with attachments appears in the Appendix on page 282.

Standard & Poor's Ratings Services was to serve first as an analyst and then as a manager with respect to Enron.

I am joined today by Nik Khakee, who was the senior analyst involved with our work on the Yosemite and Credit Linked Notes Trusts. The comments I will make a little later regarding those trusts were prepared by Mr. Khakee.

On behalf of Standard & Poor's, we welcome the opportunity to appear at this hearing. Ratings are a key component of the capital markets, which have functioned effectively for decades in the United States, and Standard & Poor's is recognized as a global leader in the field of credit ratings and risk analysis. While all parties may not agree with our ratings at all times, Standard & Poor's credit ratings have gained respect and authority throughout the investing community because they are widely understood to be based on independent, objective and credible analysis. The record bears out Standard & Poor's emphasis on objectivity and credibility. There is a longstanding and exceptionally strong correlation between the ratings initially assigned by Standard & Poor's and the eventual default record. The higher the initial rating, the lower the probability of default and vice versa.

Our ratings opinions are based on a company's audited financial information and qualitative analysis of the company and its industry sector. We also may have access to certain confidential information of the company, but only to the extent that the company's management is willing to provide such information. We use that information and rely upon it.

With regard to Enron Corporation, from 1995 until November 1, 2001, Standard & Poor's rating of Enron was BBB+, which placed Enron at the lower levels of investment grade ratings and was well below what Enron repeatedly and unsuccessfully sought from Standard & Poor's.

It now appears, based on what Mr. Roach and Mr. Brown just testified to, that in addition to the already well-documented deceptions regarding its off-balance sheet partnerships, Enron may have incurred approximately $4 billion in debt-like obligations structured as prepaid forward transactions and swap transactions. Our contemporaneous understanding of these types of transactions was that in the years leading up to its bankruptcy, Enron was employing them to actively manage its trading and marketing positions and cash flow. While Enron did not provide specific details about these particular transactions, the generalized information it did provide, which underpinned our analysis, led us to conclude that the funds from these transactions were more akin to operational cash flow than new debt-like obligations.

Despite our repeated requests for complete, timely and reliable information, Enron did not disclose any information revealing a link between the prepaid forward transactions and the swap transactions. Similarly, Enron provided no indication that these transactions were in any way related to any of the Yosemite or Credit Linked Note transactions, despite an explicit inquiry by Standard & Poor's regarding the effect, if any, of these structured finance transactions on Enron's financial situation. While our knowledge about the full nature of these transactions and/or any links between them is still limited, any lack of disclosure by Enron of their

material aspects would have been yet another flagrant violation of Enron's duty and responsibility to provide Standard & Poor's with complete, timely and reliable information.

In hindsight, and without full information, it is difficult to assess the effect full disclosure about these transactions would have had on our ratings analysis; but the sheer volume of the transactions suggests that it would likely have been significant.

It is worth noting as well that on no occasion did we advise, consult or suggest to Enron that it should employ these prepaid forward transactions or swap transactions, or any other means to increase cash flow.

The Subcommittee has also requested information regarding our understanding of the structure and operations of the Yosemite and Credit Linked Notes Trusts. Each of these trusts was structured as a standard Credit Linked Notes transaction in which the credit risk of a particular entity, which in these trusts was Enron, is transferred to the purchaser of notes issued by the trusts. In such transactions a counter-party seeks to purchase protection against the default of a particular issuer. In the first Yosemite transaction, for example, the protection buyer was Citibank. On the face of it, by entering into a credit default swap, Citibank protected itself against a default by Enron. In the event of such a default, Citibank would receive consideration from the protection seller. Here the protection seller, the Yosemite I Trust, obtained the funds needed to pay Citibank in such an event by selling notes and certificates to qualified institutional buyers.

Because our ratings analysis of the notes issued by these trusts required us only to focus on the structure of the transactions and whether the default risk of the trusts notes was a genuine pass through of the default risk of Enron, our analysis did not include review of the day-to-day operations of the trusts. As with all such transactions, it was the trustees' responsibility to ensure that the proceeds of the notes were invested in accordance with the terms of the indenture and that all of the trusts' operating requirements were met.

Enron's demise, along with other recently revealed corporate accounting problems has damaged the public's confidence in the marketplace and the economy as a whole. Because our ratings ultimately depend upon information provided by the issuer, Standard & Poor's has been a long-time champion of complete, timely and reliable disclosure of information and the highest standards of corporate governance.

To that end, while we applaud the recent proposals and recommendations made by the Securities & Exchange Commission, Standard & Poor's has already stated publicly our belief that such proposals are only a partial solution, as they still leave wide room for interpretation by companies and their accountants about whether certain items qualify for additional disclosure.

We have recently published two articles, which I have included with my testimony, which focus on the various proposals in light of Standard & Poor's ratings practices. We are also in the process of reviewing current accounting and regulatory requirements with an eye towards making specific recommendations for improvements

aimed at fostering greater corporate transparency and restoring public confidence in the markets. Thank you.

Senator LEVIN. Thank you very much, Mr. Barone.

First, Mr. Turner, if you would take a look at Exhibit 112.[1] This is an Andersen analysis on when a transaction that is being called a prepay can properly be counted as a trading contract and as cash flow from operations rather than as debt and cash from financing. Now, we've put that analysis also on a board up here to my right. We've put it on one page to make it easier to use.

In your testimony you said that you agreed with Arthur Andersen's four key points for determining when a prepay transaction can be accounted for as a trading contract, and I want to ask you about a couple of the four elements.

First of all, if a transaction fails to meet any of those criteria, am I correct that it fails the test for being treated as a trading contract?

Mr. TURNER. Yes. In this case I think that would be true.

Senator LEVIN. In other words, if you fail any of the four, it fails as a trading transaction; is that correct?

Mr. TURNER. Yes, I would agree. I think that was Andersen's analysis, and I would agree with them.

Senator LEVIN. Now, the first criteria is that none of the agreements in the structured transaction may be linked. In your judgment were the transactions involving Enron and Chase and Enron and Citibank linked?

Mr. TURNER. Yes. Your staff has shown me some exhibits. I don't recall which Bates numbers, but it certainly looked like they were linked to me.

Senator LEVIN. For instance, we understand that Mahonia entered into a contract in which it assigned to Chase all of its rights to any payment from Enron. Does that constitute linkage?

Mr. TURNER. Yes.

Senator LEVIN. And what effect does that alone have on the accounting for this transaction?

Mr. TURNER. When you link all these transactions together, in essence what you are seeing is that it's really just a collapsible transaction between Enron and the investment banker, in this particular case, which would turn it into being a bank loan on the balance sheet.

Senator LEVIN. So that it would destroy that prepay triangle and just reduce the transaction to a loan between Enron and Chase?

Mr. TURNER. That's correct.

Senator LEVIN. Now, you've seen some of the evidence the Subcommittee investigation obtained with respect to Mahonia and Delta and their relationship to Chase and Citibank. That evidence shows that the banks directed the establishment of those offshore entities; they controlled the transactions that the offshore entities entered into; they set up their bank accounts, and they effectively controlled them since the offshores were shells with no employees, offices or ongoing business facilities.

Under those circumstances, were Mahonia and Delta independent from Chase and Citigroup?

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[1] Exhibit No. 112 appears in the Appendix on page 367.

Mr. TURNER. No. As I think the written testimony points out in a number of places in the accounting literature, where you just insert a nominally capitalized SP with no real business purpose, you collapse it, and again, you get down to just a transaction between the investment banker and—the bank loan and Enron.

Senator LEVIN. Now, is it important that they be independent because if they are not independent third entities out there, this is just simply, in essence, a loan transaction between the bank and Enron?

Mr. TURNER. That is true. What the accountants are really looking for is do you have three independent parties each taking on a legitimate business purpose, legitimate business risk behind the transaction, or is it really just a sham transaction designed to try to avoid the accounting rules.

Senator LEVIN. Now, another of the Andersen criteria requires that the parties to the energy trade have an ordinary business purpose for buying or selling the prepay commodity. From what you can tell, did either Mahonia or Delta have an ordinary business reason for engaging in energy trading?

Mr. TURNER. No. I think, in fact, a number of the emails and memos specifically talk about the purpose was to try to hide this from the balance sheet of Enron and its investors.

Senator LEVIN. Now, Citigroup has said in its prepared testimony that the "overall cash flow for Enron would be exactly the same whether Enron used prepaids or entered into a bank loan. In the case of prepaids," the testimony goes on, "which are contracts transacted in Enron's trading book, Enron booked the cash it received on these contracts as cash from operations, not as cash from financing."

Let me correct my question. Citigroup's testimony said that the overall cash flow for Enron would be exactly the same whether Enron used prepaids or entered into a bank loan. My question to you is: Is it, in fact, the same?

Mr. TURNER. No. Without a doubt, both the accounting rules, GAAP, as well as the SEC regulations and SEC disclosure regulations make it very clear that you have to separate out the three different components of cash flows and report them properly. Those you generate from normal, ongoing, legitimate business operations, which is cash that you then might be using in the second category, and that is financing to pay back loans, so you have to show financing separate, distinct, those funds that came in from a bank loan separate and distinct from those that you generate from just selling normal products and goods in the normal course of business.

So they are not the same, and what is so interesting in that testimony is while people say it is the same and it really doesn't matter, people don't go to such great lengths and engage auditors, attorneys, accountants, and do all this paperwork and incur all these costs and time if it doesn't matter. If it doesn't matter, you just follow the GAAP rules. But in this case, that is not what happened. There was a reason that they did this, and that was to hide and disguise it from investors.

Senator LEVIN. What difference does it make to investors?

Mr. TURNER. Investors need to know what the liquidity of the business is going to be. Are you going to have the resources to meet

your different type of obligations? Is it an account payable that you may need to pay off in the next 30 days? Or is this going to be a big debt payment going to come due? It is like you, perhaps, Senator, going and asking a bank for a loan and putting your credit card receivables, your mortgage on your house, your loan on your car all on one line and going into the bank and saying, Don't worry about it, it's all one line liability, you don't need to know any more information about it. I don't know of a bank that would make you a loan on that basis.

Senator LEVIN. This is the way they summarize their argument in their testimony that is prepared: "Price risk management liability is a liability, plain and simple. It must be satisfied every bit as much as debt. Thus, while not recorded as debt, prepaid liabilities were clearly obligations of the company and visible as such to investors."

Do you agree with that?

Mr. TURNER. I couldn't be in more disagreement with that than you could get. It is absolutely false. It is wrong. It is counter to the SEC rules. It is counter to GAAP. And, quite frankly, again, if I was the CFO at Symbios and approaching either of these banks' lending group with a set of financial statements where you treated your liabilities all on one line like that, I can guarantee you—in fact, I think one of the banks might have even been in the consortium of banks that loaned to me at Symbios—they would have never, ever accepted those financial statements or given me a loan on that basis.

Senator LEVIN. Ms. Stumpp, do you agree with that quoted statement of their testimony?

Ms. STUMPP. I don't agree with their quoted statement. In fact, I agree with Mr. Turner.

Mr. DIAZ. I would add that from our point of view as a rating agency, that is definitely misleading because we rely very much on cash flow to debt as a key measure, on cash flow coverage of interest, and what it's doing, it's inflating the cash flow and reducing the debt. So from our point of view, it has a major impact.

Senator LEVIN. Mr. Barone, do you agree with that quoted statement from Citigroup's testimony that price risk management is a liability, plain and simple, that it must be satisfied every bit as much as debt, thus, while not recorded as debt, prepaid liabilities were clearly obligations of the company and visible as such to investors? Do you agree with that?

Mr. BARONE. No, not necessarily, Senator. While they may have appeared as liabilities on the balance sheet under price risk management liabilities, our determination of the credit protection ratios of Enron would have looked more towards true obligations and not the short-term nature of what the price risk management liability may have proved, because it is often offset by assets from price risk management. And that is how the company had always explained that their trading books were generally in balance. So, no, it's definitely concealing an obligation.

Senator LEVIN. And that is highly relevant to you?

Mr. BARONE. Absolutely.

Senator LEVIN. Because it is relevant to investors.

Mr. BARONE. I would say sure. I'm not an investor, but as someone who evaluates a company's credit and bonds that are ultimately bought by investors, it trickles downhill there.

Senator LEVIN. Mr. Khakee, did you want to add anything to that?

Mr. KHAKEE. No. I echo my colleague's comments.

Senator LEVIN. Thank you.

Now, Chase and Citibank didn't just go along with Enron and what Enron wanted to do with its prepays—these so-called prepays, these phony prepays, these fake prepays. Both banks went further. They tried to sell these Enron-style prepays to other companies. Before doing that, should each bank have done its own accounting analysis of the structure, consult with its own accountants to determine that the suggested accounting complies with generally accepted accounting principles? Could the banks reasonably rely solely on the accounting judgment of a client and say that our client's auditor said these transactions could be accounted for this way so that is good enough for us? Shouldn't they have done their own analysis, Mr. Turner?

Mr. TURNER. Yes. I actually agree with you on that, Senator, and I think that is where Judge Friendly was going in the court case that I mentioned to you before.

If you become aware of evidence, which clearly they were, as it is cited and referred to in a number of these memos, that there is something improper going on with the financial statements, then you have got to—you can't just stick your head in the sand like an ostrich. You have got to follow it through and make sure that it is okay and it is done right. In fact, at times when I was at the Commission, when we were aware of the fact that professionals outside the company who operate as gatekeepers to make sure the markets maintain their integrity, when they became aware of things and did stick their head in the sand and didn't follow through, then we did take enforcement actions and did investigate the matters, which I hope will happen here.

Senator LEVIN. Two final questions from me. Ms. Stumpp, you say in your prepared testimony—and perhaps I missed it in your oral testimony—that Moody's did not have any knowledge prior to Enron's bankruptcy of the existence of Enron's prepaid forward and related swap transactions. Is that accurate?

Ms. STUMPP. That's accurate.

Senator LEVIN. Finally, my last question to Mr. Barone. You have seen the staff analysis. If you look at Exhibit 104,[1] this is an analysis of the impact on Enron's debt of these sham prepays. I think it is in the book in front of you also. Do you agree with that analysis?

Mr. BARONE. Senator, I would agree that treated as a loan, you would add additional items to the debt line. You would reduce cash flow, as it states, and you would record a particular amount of implied interest associated with the additional debt. If you are going to add debt, you must add interest. So in that regard, yes, I agree. The mathematics of the calculation of the funds flow interest cov-

[1] Exhibit No. 104 appears in the Appendix on page 355.

erage I'm not doing here, but it does not look all that out of bounds. It looks pretty accurate.

Senator LEVIN. And so their treating this as business income rather than as a loan, has that significant effect on its credit rating?

Mr. BARONE. As presented here, yes. Going from 4 times interest coverage to 2.25 times interest coverage, all things being the same, no change in business risk, no change in strategy, and so forth, yes, that is significant.

Senator LEVIN. And should this have been treated as a loan in your judgment?

Mr. BARONE. Not having immediate firsthand knowledge of how the transaction went down, but based upon the testimony I listened to today, yes, sir, it should have been treated as an obligation, as a loan.

Senator LEVIN. And shown as debt?

Mr. BARONE. And shown as debt.

Senator LEVIN. Thank you. Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman.

Mr. Turner, I want to thank you for your usual straightforward testimony. It is very helpful to us in sifting through the conflicting messages and testimony that we are getting.

You testified that there is no question that the accounting treatment misled investors. The banks essentially are responding with two, in my view, contradictory arguments. On the one hand, they are saying that there were no red flags, an assertion that clearly is contradicted by all of the internal documents that we have. But their second argument is, "it is not our responsibility to make sure that Enron is reporting the debt correctly; it is not our job."

In your opinion, if a financial institution is involved in helping to create and finance this type of transaction and understands that they are going to be used by their client to misrepresent the company's financial position, what obligation does the financial institution have?

Mr. TURNER. Senator, in this particular case I think what concerns me, certainly what had concerned me from my role as an SEC chief accountant, was the fact that in some of these transactions they were actually going out and raising money from the public to fund these vehicles. And they had firsthand knowledge of exactly what was going on, but there was not full and fair disclosure to investors. So they, in essence, withdrew from the investors their ability to make an informed decision as they were buying these securities because they didn't see a clear and transparent picture.

At the Commission and in the markets, you have to rely upon these gatekeepers to make sure all the material information is provided to investors. When a professional gatekeeper knowingly withholds that information, I think it raises not only the question that Senator Levin raised in an earlier question about whether or not they aided and abetted in what happened here, which I certainly think they did, but I think if I was still at the SEC, we'd certainly look at whether or not they had a primary obligation under the securities laws since there appears to have been willful knowledge here of a lack of disclosure to investors that they were raising

money from to make that disclosure to them. And I would suppose that's certainly one thing that the Commission will turn around and take a look at.

Senator COLLINS. Let me follow up on that very point. Have you had the opportunity to review the prospectus that Citigroup created for the Yosemite Trust?

Mr. TURNER. Yes, I have read—I haven't read every word, but I've scanned through the Yosemite Trust offering.

Senator COLLINS. And what are your preliminary conclusions regarding the accuracy of the representations made of Enron's financial picture in that prospectus?

Mr. TURNER. One, it refers back to some of the Enron filings that clearly don't have this financial information presented as a loan to it and is telling investors go look at that, notwithstanding the fact that they clearly knew, as evidenced by their own internal memos, that it had been kept off those balance sheets as debt. And so I think there's a legitimate question here based upon what I've been provided so far to date, that raises the question about whether or not there were disclosures that the investment bankers were aware of and should have been aware of based upon their due diligence that were missing.

Senator COLLINS. It seems to me based on the review of the documents in this case that in the specific instance of structuring the prepays, that Andersen gave accurate guidance in this instance to Enron on the criteria that must be satisfied in order for this to be a legitimate prepay. Would you agree with that?

Mr. TURNER. Yes, I think Andersen did give some good guidance to the people involved with it, and it's guidance certainly I would have used myself if I was still a partner out there in evaluating whether these would be treated as prepaid trading assets and liabilities or as debt financing. So I think their conclusion, and conclusion as to how to apply it to these transactions were correct.

Senator COLLINS. But the criteria they set out clearly were not followed.

Mr. TURNER. I would agree with that. In fact, Senator I would turn around and tell you that some emails or correspondence makes it appear like people almost attempted to mislead Andersen, which is highly unfortunate. Again, one of the fine things that the Senate dealt with in the Sarbanes bill.

Senator COLLINS. Mr. Turner, some people have told us and continue to maintain—and this follows up on a question that the Chairman asked you—that the technical manner in which Enron accounted for its obligations under these transactions was really irrelevant because the trading liability or debt would be viewed similarly by the markets.

Could you explain for us further why it does, in fact, matter how Enron chose to report this cash, whether it reported it as cash from its trading operations or as a loan?

Mr. TURNER. Yes. In particular on this balance sheet, this balance sheet has a significant amount, billions of trading assets, billions of trading liabilities, and I think a normal reader of these financial settlements would understand that companies' traders try to match those assets and liabilities to where they come due at the same time and offset one another. And as a result, you're not going

to have to be generating a bunch of additional cash flow to be paying down bank debt or meet the interest and principal payments.

But, in fact, that wasn't the case here. These really weren't trading assets and liabilities that were going to be offset. They were bank loans who had debt and principal payments, interest payments that had to be met, and the company wasn't generating sufficient cash flow to meet those, as we all know now, because it ended up in bankruptcy.

By being able to pump up the cash flows to make it look like they were generating a lot of cash and then hide the bank debt so it looked like they didn't have a lot of bank debt payments coming due, it disguised the true nature of what the real liquidity of this institution looked like. We can tell, quite frankly, we all found out the day it filed for bankruptcy that it really didn't have the cash, didn't have the liquidity. The only thing it did have was a lot of bank debt that we found out for the first time was off-balance sheet.

Senator COLLINS. Ms. Stumpp, many analysts have described Enron's finances as "verging on the impenetrable," and, in fact, one stock analyst described it as a "black box." Did your rating agency have difficulty in ascertaining the true picture of Enron's finances?

Ms. STUMPP. Well, in retrospect, knowing what we all know now——

Senator COLLINS. I don't want you to answer in retrospect. I mean, when you were going through the process, did you find it difficult to analyze and rate Enron because of the complicated and unusual nature of many of its transactions?

Mr. DIAZ. Maybe I can answer that, because I was responsible for Enron. We certainly looked at Enron as being a very complex company, mainly because of its trading operations, so we spent a lot of time trying to understand the risks around the trading and, as Mr. Turner said, trying to understand the matching of the assets and liabilities.

I think we also spent a lot of time trying to understand the nature of some of the financing that was taking place off-balance sheet in terms of their investments in international projects.

But the fundamental problem was that we did not see what they were really doing in terms of the prepaids, which is part of the picture. We also were not able to see the existence of some of the other off-balance sheet vehicles like LJM and Braveheart and all those other vehicles that were kept out of the limelight.

So, what looked like a complex but understandable company really was not. There was a lot of misleading—there was a lot of deception in the way that they presented the financial statements.

Senator COLLINS. But you felt that you had adequate information on which to base a rating decision?

Mr. DIAZ. At the time we did because—if we had felt that we didn't—we would have either withdrawn—we probably would have withdrawn the rating. So at the time, based on the information we had, we did believe that we had adequate information.

Senator COLLINS. Mr. Barone, I am going to ask you the same question.

Mr. BARONE. Yes, I echo my colleagues' remarks. While Enron was certainly a little more complex than some of the other energy

credits that we evaluated—we spent a considerable amount of time trying to delve in and do the analysis, and we believed that we had—given the information that was provided to us—that it was full and adequate and enough for us to do the evaluation, certainly. What we've learned in retrospect, obviously is that that was not necessarily the case.

Senator COLLINS. Mr. Turner, I am going to put you on the spot here. Did the rating agencies do a good job?

Mr. TURNER. You're right, you are putting me on the spot. Let me say this, Senator: I remember back around the middle of October, as this whole thing was imploding on itself, one of the newspaper reporters calling me up and asking me if I would review and read the Enron financial statements.

I went through and read them in depth at that point in time, and to be quite honest with you, they raised more questions in my mind than they answered. They raised a lot of questions because there were tantalizing little bits of information, but certainly not enough to analyze the full set of financials from. And the question is: Did people who were analyzing them, not only the rating agencies but the stock analysts as well, were they able to go back into Enron—because certainly they get a mosaic of information we don't get out in the public. Were they able to go in and get the answers to those questions? Quite frankly, many of those questions, if answered, would have told you that those financial statements had been cooked. And so I think the real question was: Did they go through, did they ask those questions, did they get the answers to those questions? Because the financials themselves clearly tee up a lot of serious questions that we now have the answers to and we know they're cooked.

Senator COLLINS. Thank you, Mr. Chairman.

Senator LEVIN. Thank you very much, Senator Collins. Senator Lieberman.

Senator LIEBERMAN. Thanks, Mr. Chairman. Thank you all for your testimony.

Mr. Turner, during your oral testimony today, I believe I heard you say that the kinds of transactions that we are focusing on today occur day in and day out on Wall Street and in the economy. Could you expand on that a bit? What do you mean?

Mr. TURNER. Wall Street designs and engineers transactions, not on their own but with the help of the accounting firms as well as the law profession, quite frankly, that are intended to obfuscate or keep information from investors. Off-balance sheet types of financings, financings that will make things look like equity rather than debt on the balance sheet, not just the issue of what type of liability, but whether it's debt or equity. At the SEC, quite frankly, they're very tough to find because they design them with the notion of keeping them out of the filings, but we would find them from time to time and then basically have to go through a battle, major battles, to try to keep—or to try to get investors the information they needed disclose.

The Financial Accounting Standards Board, out from your State, Senator, actually has a list of publications that is probably about four inches thick now and about—there's thousands of answers in that on these transactions, and I would guess maybe 70 percent,

maybe more of those answers are just for these type of structured transactions coming out of Wall Street, where they've structured the transaction, tried to get around the FASB rules. We would find out about them at the SEC, and then asked the FASB to try to deal with it. I think it's probably the best indication of just how much time and effort goes into not only structuring but then trying to fix the problem and get clear disclosure for investors.

Senator LIEBERMAN. Seventy percent of what was the number you gave?

Mr. TURNER. There is what's known as the Emerging Issues Task Force of the Financial Accounting Standards Board. It's a group of people who deal with emerging accounting issues as they arise. Quite often they arise because the investment bankers have designed these transactions. People have found out about them, and so then we have to come up with an answer to try to make them transparent to investors.

Quite frankly, I would say that on a number of occasions even the accounting firms themselves were appalled by the accounting that the investment bankers were proposing or the companies were proposing to use. And to their great credit, we would have the accounting firms call us up, tell us about the transaction, and then ask us to try to shut it down.

I will tell you I do recall one situation where even the investment banker was asking everyone to sign a non-disclosure agreement as they shopped it around so that no one could come and tell the SEC about it.

Senator LIEBERMAN. And in that case, to use language that you used, the proposal had the intention to hide and disguise the true condition of the transaction from investors?

Mr. TURNER. Without a doubt.

Senator LIEBERMAN. I want to go back just real briefly. Seventy percent of what, in your first answer, were you talking about?

Mr. TURNER. It's 70 percent of these emerging accounting issues that this task force has dealt with.

Senator LIEBERMAN. Had to do with these so-called structured transactions?

Mr. TURNER. Some of them are structured transactions. Some of them are just pure off-balance sheet type transactions that are—there's more than just structured transactions that Wall Street has used to disguise the real true nature——

Senator LIEBERMAN. Again, with this 70 percent of the emerging issues, OK.

Mr. TURNER. OK.

Senator LIEBERMAN. Where the intention was to hide and disguise the true condition of the transaction—and, therefore, the company—from investors? And you are not here just talking about the kind of prepays that Enron was involved in with the financial institutions we are talking about, but other structured transactions?

Mr. TURNER. That's true. And on some of these, there's very legitimate good business reasons for them to do what they want to do because of tax reasons or to protect themselves in bankruptcy court or whatever. But that doesn't prevent you from turning

around and really reflecting the true economic substance on the balance sheet in the way it should be.

Senator LIEBERMAN. Which, by and large, they were not doing.

Mr. TURNER. Correct.

Senator LIEBERMAN. Would you say that this widespread use of these structured transactions to conceal the true nature of the transactions in the company from investors is still going on today?

Mr. TURNER. Yes.

Senator LIEBERMAN. Notwithstanding Enron, WorldCom, Tyco, ImClone, etc., still going on?

Mr. TURNER. Yes. I would guess that—and it would be speculation, but I would guess that, yes, that's still true. We're still seeing these type of issues come up at the Emerging Issues Task Force.

Senator LIEBERMAN. Let me go on to the credit rating agencies and pick up on a note, that all of you were before the full Committee earlier, as part of a series of hearings in which we asked essentially why didn't the watchdogs bark so that we had warning about what was happening at Enron in this particular case. Credit rating agencies are institutions that investors rely on because they presumably have more information than most investors do to guide where money should go, and we had very interesting testimony about the history of the agencies and they played a very important role in the development of our economy, etc.

Ms. Stumpp, you said in your testimony, "It is important for me to note that Moody's did not have any knowledge prior to Enron's bankruptcy of the existence of Enron's prepaid forward and related swap transactions." And the folks from Standard & Poor's had a similar comment, although not in as crisp a sentence as you did.

So the question that I want to ask, both looking back and looking forward, is: Why didn't the credit rating agencies know? Let me put it another way. We just heard from Mr. Turner, and we are going to hear later in the hearing from two of the largest financial institutions in the world who are going to testify that the kinds of structured transactions that they entered into with Enron were and are common practice in the world of finance.

So if these sorts of prepays are so common, I have got to ask you: Why didn't Moody's and Standard & Poor's detect them and their impact on Enron's true financial condition?

Ms. STUMPP. Well, again, it's a two-part question, looking back and looking forward.

Senator LIEBERMAN. Right.

Ms. STUMPP. Looking back, we did ask questions of these companies, but candidly, these transactions were disguised loans, and it was very difficult, and it would be very difficult from a simple examination of a company's financial statements to detect them. The financial statements were deliberately misleading, and it was intended to hide this type of transaction from specifically parties such as the rating agencies or investors.

What I would say in terms of looking forward is that we are asking more and tougher questions, specifically as it relates to companies in the energy industry. For example, we are asking them if they have engaged in these types of transactions. There was a company that did disclose as a result of certain prompting that it restated its financials as a result of prepaid transactions. We re-

viewed that situation and took a rating action and downgraded that rating in part because of the effects of this.

We're setting up specialist teams at Moody's. We are basically setting up specialist teams to review accounting and corporate governance. In fact, we're looking to factor that very closely into our ratings. And we also sent a survey to every single corporate issuer of rated debt, as well as in other areas of Moody's, to ask them about matters such as triggers and off-balance sheet obligations.

Senator LIEBERMAN. So looking back now, are you saying, by describing a commendable and encouraging series of steps you are taking now and on into the future, that Moody's was not aggressive enough in pursuing Enron and trying to obtain information about the true nature of these transactions?

Ms. STUMPP. I think we were aggressive. I think we asked direct and difficult questions of Enron, but there was——

Senator LIEBERMAN. They were not telling you the truth?

Mr. DIAZ. Yes.

Ms. STUMPP. Correct.

Mr. DIAZ. Basically, they—for example, we asked them at one point, to try to understand the scope of their off-balance sheet obligations, to tell us everything they had—whether it was on-balance sheet or off-balance sheet so that we could make a judgment as to how we would treat it. So forgetting about the accounting treatment, forgetting about the structuring of transaction, what is the economic value transaction, and they gave us what they termed to be the kitchen sink of everything they had, but there was a lot of information there that was just not given to us. So even when we were asking directly for information, they were just withholding it.

So in the case of these prepaids, Senator, I think you are alluding to the fact that they are common as long as they are real, legitimate transactions where a commodity is delivered. But in this case, it was a clear effort at hiding what was really debt from ourselves as well as other investors.

Senator LIEBERMAN. Mr. Barone, from Standard and Poor's part, I presume the answer is somewhat the same. I believe that, am I right, that you as well as Moody's did rate the Citibank sponsored Yosemite Trust, is that right?

Mr. BARONE. Yes, that is correct.

Senator LIEBERMAN. So if you did, both of you rated the Yosemite Trust, therefore, you had some firsthand knowledge of these specific transactions, why did that not lead the credit rating agencies to see what was going on and ring the bell to alert everyone?

Mr. BARONE. There was limited information provided specific to the portion of the trust that we were asked to rate. I am going to defer to my colleague, Mr. Khakee, to explain exactly why we saw page one, if you will, but never saw page two and page three.

Mr. KHAKEE. Yes. I should distinguish that from the perspective of performing the analysis, in terms of placing a rating on the notes that were issued by the Yosemite Trust the focus of the analysis is to make sure that the rating on the notes is consistent with the underlying company. That was, in this case, Enron. And so the analysis really focuses on reviewing the documentation to make sure that the rating is, in effect, a pass-through of the Enron rating.

So when you look at the eligible investments criteria, when you look at any of the dependencies from a credit perspective, our analysis showed that it was very consistent, that investors who purchased a Yosemite note were, in fact, buying the default risk of Enron. So that was completely consistent.

Senator LIEBERMAN. Yes.

Mr. KHAKEE. What we were never presented with was all of the other aspects of what Yosemite was tied to.

Mr. BARONE. The issue of the Delta entity and how the swap moved and so forth was never presented to us when we were asked to evaluate the Yosemite transaction. It was not, indeed, part of the credit evaluation of Yosemite. The bankers did not present that portion of the transaction to us.

Senator LIEBERMAN. My time is up, but that appears to me to be very focused vision. In other words, you were right in the middle in looking at Yosemite of the kinds of transactions that infuriate us today, and you are much more expert at this than I am, but it bothers me that it did not open the door for you to see what was happening.

Mr. BARONE. I know you are out of time, Senator, but there was nothing there to even elicit the second question as to what is beyond all this. There was nothing that sort of hinted at—oh, there is Delta and there is this swap with the prepay. There was nothing revealed that prompted us to ask more pointed, more direct, or specific questions regarding the transactions. These credit linked notes are very common, as I understand, in the structured finance group.

Senator LIEBERMAN. Mr. Diaz, a final question, a very brief answer I am going to ask of you. You indicated that, and I presume folks at Standard and Poor's would say the same, the people at Enron did not tell you the truth, they were not disclosing what they were doing. Who did not tell you the truth?

Mr. DIAZ. The people that we dealt with in the financial area, the CFO——

Senator LIEBERMAN. Whose name was?

Mr. DIAZ. Andy Fastow.

Senator LIEBERMAN. All right. Anyone else?

Mr. DIAZ. It would have been Ben Glisan, and Jeff McMahon at times.

Senator LIEBERMAN. Thank you. Thanks, Mr. Chairman.

Senator LEVIN. Familiar names, I am afraid. Senator Fitzgerald.

OPENING STATEMENT OF SENATOR FITZGERALD

Senator FITZGERALD. Thank you very much, Mr. Chairman, and all of you, thank you for being here.

After hearing the testimony this morning, I really think that the transactions we are describing today are along the lines of the ones that we had hearings on earlier in the year, at least in the Commerce Committee. Enron was borrowing money and booking it as revenue from operations and going to elaborate steps to keep the actual liability incurred by virtue of the borrowing off their income statements.

And whether it is all the off-the-books partnerships, which they would cause to go out and borrow money and figure out a way to have the borrowed money then paid to Enron itself, which they

would book as income or revenue. They would manage to keep the indebtedness of the partnership off the books—they did that with the Blockbuster Video transaction, where they created Braveheart. They had Braveheart go borrow $115 million from the Canadian Imperial Bank of Commerce.

Then they sold the worthless asset to the partnership. The partnership paid Enron with the borrowed money. Meanwhile, there had been some form of credit support from Enron itself over to Braveheart the partnership, but that was not disclosed to investors.

And at the end of the day, Enron, I think, incurred about $20 billion worth of obligations that they managed not to report as indebtedness on their balance sheet, and when they filed for bankruptcy last December, it was because they had $4 billion in debt coming due that they had to pay and they did not have the cash to pay it.

These prepaid transactions, as you have eloquently testified, were just another means of really borrowing money and getting the proceeds of the borrowings in a way that they could book it as cash from operations and keep the liability off their books. So they were very creative in borrowing money and booking it as income.

I do want to follow up on a few things that have been said. Mr. Turner, you said that you were very troubled by the sale of the securities to the public, and I guess in the case of Citibank, I have to say I was much chagrined to learn that Citibank had lent $1.5 billion to Enron and then they had managed to sell securities to the public to hedge their own position, and I believe when Enron went bankrupt, then they did not have to pay back the securities and they wound up, in effect, not losing any money even though they lent Enron $1.5 billion.

Morgan is in a different position because instead of selling securities to the public to hedge their risk, they got surety contracts and now the insurers will not pay them on that and they are in court over that.

But Mr. Turner, your citing your concern actually brings up the whole issue of the Glass-Steagall Act, which had been in place a long time. Congress undid it a couple of years ago, but the reason Glass-Steagall was put into effect back in the early part of the depression was because prior to the stock market crash in the 1920's, there had been a pattern of commercial banks/investment banks unloading bad loans off on the public by selling securities.

I would like you, Mr. Turner, to flush out your concerns here. When we repealed Glass-Steagall and did away with all remnants of the law between commercial banking and investment banking, do you think we made a mistake?

Mr. TURNER. You guys ask tough questions. At the time that Glass-Steagall was repealed and GLB was put in place, I do know I had a concern as to whether or not you had legitimate and real firewalls, and, in fact, I was not the only one. I recall that Chairman Greenspan on more than one occasion was up here testifying that, in fact, if you went that route, you had to make sure that you had honest-to-goodness firewalls in between and different subsidiaries set up for securities versus banks, all under his supervision as overseen from a bank holding company.

To that extent, I do agree with Chairman Greenspan that if you are going to break down the restrictions between the securities firms and the banking firms, a point I do not necessarily disagree with in light of the competitive banking and the global international market, I do agree with Greenspan that the securities firms, you have got to have functional regulation and the securities firms and banking firms cannot be working together, entering into transactions together and using the securities arm to try to get banking business. I think there does need to be some restrictions put on that and avoided or we will have some problems.

Senator FITZGERALD. Citibank sold these securities to sophisticated investors and did not have to make any disclosures except those required for sophisticated investors, right?

Mr. TURNER. Right. I think one of the things that really concern me about the Yosemite thing is you do not see disclosures in there talking about the fact that Citibank is trying to reduce its exposure to Enron, either because of its own internal lending caps or perhaps because they really felt that there was risk there. They are trying to reduce their exposure at the same time they are trying to increase exposure to outside investors through offering these notes, and I think it would have been—investors would have wanted, and I think, in fact, some—I was told some investors did drop out of later deals because they could not get adequate disclosures and had concerns about that.

And I think investors will come back and say, why did Citibank not tell us at the same time that they are placing, in essence, Enron paper with us, because that is where the debt payments and resources are going to have to come from to repay it, why was Citibank getting out of their exposure to Enron while they are turning around and selling these very same type of liabilities off to investors?

Senator FITZGERALD. We have talked a lot about how Enron took their debt off the balance sheets and we have uncovered a lot of ways in which they did it here, which they probably violated technical accounting rules. You did not really have three independent parties with this Delta-Yosemite transaction, and so forth.

But from the testimony of many of you, I guess you are very concerned about how companies in America are taking debt off their balance sheet and I am wondering, should we in Washington try to close down loopholes in the law which were in the accounting regulations which allow companies to do this?

There are some well-established and legal ways of taking debt off the balance sheet. A simple one is if you have a building, do a sale-lease back and you get rid of your mortgage. A lot of companies do that. However, you are not really fooling anybody by doing that. Airlines take debt off their balance sheet by selling aircraft and then leasing them back. I suppose you guys are not fooled by that because you look for things like that. But now, you really have to look for a lot more sophisticated ways of taking debt off the balance sheet.

Would it be helpful if Congress tried to shut down some of those means by which companies are able to take debt off the balance sheet? That is to anybody on the panel who would want to address that.

Mr. BARONE. Senator, I do not know if it is helpful to the financial markets to necessarily do away with the use of off-balance sheet financing. I think the issue is one of greater disclosure and penalties for those that do not. The airplane leasing, as you noted, often appears in footnotes and is an integral part of a company's financial reporting.

Senator FITZGERALD. Would you like to see tighter requirements in SEC disclosure laws about the use of off-balance sheet financing?

Mr. BARONE. Yes, sir. Senator, we actually have a position paper on that that is included in my testimony.

Senator FITZGERALD. Mr. Turner, what do you think about that?

Mr. TURNER. Senator, I would turn around and tell you that I believe, as a businessman, as a former businessman, that those financial statements, not only for investors but for management purposes, really need to reflect what is going on with the business. If you are structuring off-balance sheet financing because of tax purposes or others, so be it. I have got no problem with that. But at least show them in the financial statements for what they really are. Show them as debt. To the extent that we have things that are really debt that are off the balance sheet, it just does not ring true with the average investor out there and it is what has caused us a loss in the confidence.

So I do believe Congress or the financial accounting standard setters ought to turn around and do something that, in essence, says we are going to put debt on your balance sheet if you have to use your own resources or cash to pay it. Just putting it in the footnote, quite frankly, is like just putting stock options in the footnote, and that does not get the job done, either.

I think if we are going to tell the rest of the world we have got the most transparent markets in the world, which we do, clearly do have today, then we have got to uphold that leadership and make these financial statements real and real to the investors and put the debt on the balance sheet.

Senator FITZGERALD. One final question, if I could. It has been reported in the *Wall Street Journal* on February 11, 2002, that Bob Rubin of Citibank called Peter Fisher, Undersecretary of the Treasury for Domestic Financial Markets, to ask that "a Treasury official ask credit rating agencies to give Enron a break." We know that Mr. Fisher, from other reports, declined to do that. Did anybody from Citibank call any of your agencies to lobby you to give Enron a break?

Mr. BARONE. No.

Ms. STUMPP. No.

Senator FITZGERALD. No? Did you have any banks call you to lobby you to give Enron a break?

Ms. STUMPP. [Nodding affirmatively.]

Mr. BARONE. No.

Senator FITZGERALD. OK. That probably would be a warning sign to you, if a bank called you directly and asked you to give a break to somebody.

Senator LEVIN. Senator Fitzgerald, did someone shake their head no? I am sorry. You said no?

Senator FITZGERALD. Were you all saying no?

Senator LEVIN. Were the answers on the record as being no?

Mr. DIAZ. I have testified before, during the events of the week of November 5, when the Dynegy deal was in progress, we did have discussions with banks at the time, but we were not lobbied—I mean, they were looking for us to give the deal a chance to work out, and I have testified that we held off action because we thought the probability of the Dynegy deal going through was high and that the ultimate——

Senator FITZGERALD. The Dynegy deal?

Mr. DIAZ. Dynegy, when Dynegy was trying to buy Enron. I think that is what you are referring to, at that time, during that time frame.

Senator FITZGERALD. And you were having calls from banks asking you to hold off on your downgrading of Enron's debt at that time?

Ms. STUMPP. We received a call from a bank requesting a meeting following a time when we were going to downgrade Enron's rating. We had that meeting. I would not characterize the call as "give Enron a break." It was, "could we have a discussion in recognition of the fact that this is an important issue" and that there was basically new and material information that the banks wanted to convey to us.

Senator LEVIN. Thank you. I am going to call on Senator Cleland. I just want to note for the record that the Sarbanes bill does contain a provision, I think, along the lines that Senator Fitzgerald was referring to, which would significantly tighten the rules for the display and disclosure of off-balance sheet financing, so there is at least some movement in that direction. I think that is a very important area that Senator Fitzgerald got into, but I do believe that significant provision is part of the Sarbanes bill.

Senator Cleland, I think I am going to call on you. Technically, you have not had an opportunity yet. Senator Cleland.

OPENING STATEMENT OF SENATOR CLELAND

Senator CLELAND. Thank you very much, Mr. Chairman.

Mr. Turner, I would say that I am on three committees that have been investigating Enron, the Commerce Committee, the Governmental Affairs Committee, and this Permanent Subcommittee on Investigations, and each hearing increases the "Alice in Wonderland" quality of this incredible investigation. It gets curiouser and curiouser.

We started off basically by looking at Enron officers. I indicated that in combat, officers eat last, but in this combat, Enron officers ate first. Then we looked at the accountants and found out the accountants were not accounting and the auditors were not auditing.

And now we find that the lending institutions, the great financial services institutions, JPMorgan, Citigroup, Bankers Trust, Barclays, Connecticut Resource Recovery Authority, Credit Suisse, First Boston, Fleet Boston, Morgan Stanley, Royal Bank of Canada, Royal Bank of Scotland, Toronto Dominion were involved and $8 billion of loans that on any balance sheet in America, kept by any little accountant in any little hometown in Georgia would have been listed as a liability and not an asset.

What I would like to know from you is, how in the world can some of the finest minds in finance in the world with these great institutions participate in something like this? It seems like it would be more difficult to sneak sunrise by a rooster than to sneak $8 billion of liabilities and transform them into assets with these great financial institutions looking on. What happened?

Mr. TURNER. Oh, I think people are running down the yellow brick road in Oz-land.

Senator CLELAND. Well, we are not in Kansas anymore.

Mr. TURNER. Yes, we are not in Kansas anymore. [Laughter.]

When you would see these meetings occur between the investment bankers and the attorneys and the accountants as they designed these type of transactions, it became a combination of a game, a herd mentality, if you will, a very competitive, let us beat the other banker out and try to come out with another vehicle that we can sell some and raise fees off of. They really lost their compass and lost sight of the fact that, really, what makes those investment banking firms are the investing public and the markets, but instead became much more focused on making fees.

And as the industry changed from a commission-based, profit-oriented organization 30, 40 years ago to one that is driven by investment banking fees and that is where their compensation is, I think that change in profits, that change in compensation, that change in structure and what really made the investment banking firms and Wall Street changed their behavior to one of looking out for investors to one of let us make a buck and let us see what we can go around the rules——

Senator CLELAND. Would you say that was infectious greed?

Mr. TURNER. It was infectious greed——

Senator CLELAND. Mr. Greenspan was suggesting——

Mr. TURNER [continuing]. Like a bad case of cancer.

Senator CLELAND. Ms. Stumpp, what happened?

Ms. STUMPP. Well, I would say that in this regard, financial institutions do engage in structured transactions and in financial engineering as part of their history. In this case, it is perhaps not, again, the structure, although we recognize the outcome of the structure was to boost cash flow and to not show appropriate debt or the actual level of debt that was on the books, but it was the disclosure. It was the treatment of this transaction. The disclosure and the treatment were not clear so that people could not really see the true picture of the financial health of Enron. So what I would say is that perhaps it was financial engineering going a little too far, but the disclosure element was particularly problematic.

Senator CLELAND. Mr. Barone, what happened?

Mr. BARONE. I think you hit it on the head, Senator, about the greed issue. I mean, it is obviously a blatant attempt to hide and disguise various transactions to make a company look better. I believe we were defrauded. I believe we did a fine job in our attempt to try to uncover various additional debt, liabilities, and so forth, but you do not know what you do not know, and that which was concealed made it extremely difficult to paint a true picture of Enron's creditworthiness. I think it may have started out with one intent, but it clearly was a snowball rolling down the hill and it just kept building.

Senator CLELAND. I think it is the ultimate in fuzzy math and it has cost the teachers' and employees' retirement pension funds in my State almost $127 million in losses.

Thank you, Mr. Chairman.

Senator LEVIN. Thank you, Senator Cleland. Senator Carper.

Senator CARPER. Thanks, Mr. Chairman, and to our witnesses, welcome and thank you for being here today.

I would ask, Mr. Turner, I do not think anyone has asked you any questions today, so maybe I will throw one your way. How does the—I will call it the Sarbanes legislation that we have been in conference on now—how does that legislation reduce, if at all, the likelihood that other companies like Enron will try to use prepaid forward transactions or a device like that to deceive?

Mr. TURNER. I think there are actually some excellent provisions in the Sarbanes bill. I do not think it is an end-all for this problem and you should be careful about that, but there is a very important provision in there that says that the executives are going to have to sign off on the financial statements, not just based upon whether they are GAAP, but whether or not they fairly present the real true economic picture of the balance sheet and the income statement of these companies, and I think that provision is going to make the executives think twice. They can no longer hide behind GAAP as a result of that provision in that legislation. They are going to have to turn around and make sure it presents a true economic picture.

In the list of prohibited services that has been, unfortunately, severely opposed by some members of the House, it has a prohibition on some services, the nature of which the auditors would typically do in these type of situations, so it will cut off the ability of the investment bankers to go get the assistance from auditors in turning around and trying to structure these things. As long as we can hang on to that list of nine provisions, I think it will go a long ways and I really hope we do not lose those things in conference.

I think the additional legal provisions, including some strengthening of what the SEC regulations are and who they can go out and reach, give them reach that will allow them to go after these type of situations and professionals who were not at the company but nonetheless aided and abetted in this type of false and misleading financial reporting.

I think all of those components of the Sarbanes bill are just very good, very excellent, very outstanding, are going to ensure that we have some independent gatekeepers as well as some people inside who can no longer just try to get around the rules.

Senator CARPER. Let me ask our other witnesses, do you want to comment on the same question? If not, I can ask another question.

Before coming to the Senate, I was privileged to be Governor of Delaware for 8 years and well before that to be Treasurer of the State for 6 years. I remember when Delaware had the worst credit rating of all 50 States. We were tied for dead last with Puerto Rico, and they were embarrassed. That is how bad it was. We were closed out of credit markets, literally could not sell bonds, notes. It was a bad time. You folks were all over us, Moody's and Standard and Poor's, all over us in the bad old days back in the 1970's and did not let us get away with anything.

When I see what Enron got away with, the question comes to mind. I know others have probably asked this question, but how did they get away with it without you folks knowing what was going on?

Mr. BARONE. Well, Senator, I would assume that in Delaware, you did not defraud the agencies by not presenting a full, clear, and accurate picture of the financial well-being or lack thereof of the State.

No, I think they got away with it through deception, through fraudulent disclosure, lack of disclosure, insufficient disclosure, and not for a lack of asking by us. My colleague pointed to the kitchen sink document that we all were privy to. We asked what obligations do you have that were not on-balance sheet. We always had a tug of war with Enron as to what off-balance sheet obligations we should effectively put back on their balance sheet. They clearly disclosed many things that were not on-balance sheet and even came to some agreement with us that, yes, certain things probably should be added back.

What we did not know is that there was another book full of things that should have been added back to the balance sheet and considered obligations. That is how they got away with it.

Senator CARPER. Anyone from Moody's?

Mr. DIAZ. Yes. I think, fundamentally, I agree with Mr. Barone. It is a lot of use of financial engineering, lack of disclosure, lack of transparency, and basically never refusing to answer a question when we probed, but giving us misleading answers and withholding information. I spoke about the kitchen sink, where we asked them to give us a list of all their financial obligations, and they—clearly, a lot of the partnerships were not included in that information. We are not auditors, so we do not go and look at the books, but it is basically a—I think they got away with it for a while, but ultimately, that kind of situation is not sustainable, and that is what happened.

Senator CARPER. What are you doing different today at Standard and Poor's or at Moody's to ensure that companies like Enron do not get away with this sort of thing in the future?

Mr. BARONE. I think we have a degree of healthy skepticism when probing companies for information. I think history is a great teacher. You learn a lot from looking back. For many of the energy firms, we are asking about prepaid deals: If they did them, to describe them and disclose them. We are also asking about trading activity as well, not that we had not asked similar questions before, but I think we just have a greater skepticism. We are a little bit more critical. Our skills are honed even further. I mean, time is a great educator.

Senator CARPER. Thank you.

Ms. STUMPP. I would say, for Moody's, I mentioned this a few moments ago, but we are asking more and tougher questions. With respect to the energy merchants themselves, we have asked them about their engagement in prepaid forward transactions, particularly as a result of the disclosure of Project Alpha in connection with Dynegy. Some companies have told us that they have, again, been approached to do these deals. Some of them have told us they

declined to do some of these deals. At this point, few have indicated that they have done any of these deals.

We plan, as a result of the information that we understand today and from what we have read in the papers, to follow up and have written correspondence with these companies, asking them to affirm to us that they are not engaged in these prepaid forward transactions, or if they are, to disclose it to us and the level of such activity.

We are setting up at Moody's specialist teams in connection with experts who can help us with accounting and corporate governance matters. We have gone out to the entire corporate finance rated universe and asked them information on off-balance sheet obligations and on ratings triggers and we produced a report last week on our survey of ratings triggers.

Senator CARPER. Thank you very much. I might add, Mr. Chairman, just as a postscript, the State that used to have the worst credit rating of any State in the Nation ended up, I think about 2 or 3 years ago, thanks to companies here plus one that is not, Delaware ended up with a AAA credit rating. So, miracles do happen. Thank you.

Senator LEVIN. Well, one of the reasons for its dramatic improvement is one of our colleagues who is sitting right to my right. Senator Carper was then Governor of the State, and he is much too modest to take credit for it, but he deserves a great deal of that credit for his State's improvement.

Talking about credit ratings, let me ask you just one final question. You have all indicated that the prepays here should have been booked as loans. They were disguised loans. Instead they were booked as cash coming in from business operations. And my question is this. If they had been properly booked, how would that have affected your ratings? First let me ask you, Ms. Stumpp.

Ms. STUMPP. Unequivocably it would have resulted in a lower rating. And the magnitude today—it is quite dramatic, the magnitude of the reduction in cash operations and the increase in debt, and we would have had a lower rating on Enron.

Senator LEVIN. Mr. Barone.

Mr. BARONE. The same here, Senator. We would have had a lower rating on Enron for certain—significantly. How far? How much? I couldn't necessarily pass that judgment right now, but it could have easily been non-investment grade, two notches below or three notches below where it was before its demise.

Senator LEVIN. Senator Fitzgerald.

Senator FITZGERALD. If I could just ask a final question. I think we are probably going to break for lunch here.

Senator LEVIN. No, we have decided that we are going to go right through lunch, I am afraid. This is becoming a very unhappy tradition of this Subcommittee.

Senator FITZGERALD. So I don't get lunch?

Senator LEVIN. Well, I don't want to go that far. In the back room maybe we will give you a sandwich.

Senator FITZGERALD. All right. Well, let me—if I could—there has been a vast increase in the level and amount of securitizations in this country in the last maybe 20 years. A lot of financial institutions take their credit card receivables, securitize them, and

later—and then they book all the revenue after they sell the receivables, they book that as revenues.

Presumably they are setting aside some kind of reserves in case they have—they have to set aside reserves for the purchaser, I think, in most cases, but sometimes there is not really good disclosure of whether the securitizations are with recourse to the issuer. And this comes up in Enron because it appears that some of the monetization transactions that Enron did, they led the ratings agencies to believe were non-recourse to Enron and it turned out they were recourse.

I am wondering if you from the rating agencies have any general thoughts on the level and amount of securitizations out there. A lot of companies have accelerated their earnings by securitizing assets, and I wonder to what extent investors are aware of lurking liabilities out there. Quite often I read that some company had to take a charge-off because all of a sudden somebody was going after them to make good on a portfolio of securities that they securitized.

Would any of you care to comment on that? Mr. Khakee, you are a Director of Structured Finance Group at Standard & Poor's, would you care to comment on that?

Mr. KHAKEE. Yes, I would, actually, Senator. I think there is nothing fundamentally or inherently wrong with structured finance. I think that it is important to try and understand the differences between the types of transactions that you are alluding to. In a typical asset-backed structured financing, what is being securitized are receivables. The credit risk of those receivables is based on the underlying payments or cash flow streams that are coming in. You mentioned credit card transactions. You could also look at mortgages that are being securitized.

I think it is clear that securitization has benefited the vast number of consumers. It has brought down, most likely, the overall cost of financing, and mortgage financing is a very important part of the overall economy. So I think structured finance, when used properly and when explained properly, is an important tool.

When you refer to credit-linked notes, which in this case are the Yosemite transactions, that is not so much a securitization per se. The investors are investing in a different type of risk. It is directly linked to Enron, and it is quite clearly stated as such. When one is investing in a securitization, one is investing in a capital structure. The rating, if you will, when we issue a rating, reflects the risk that they are taking, given the place in the capital structure that they are investing.

So I think it is important to try and differentiate across the various products inside of structured finance. But if you want to aggregate and just make a comment on structured finance, I think it is a very important part of the overall ability of businesses——

Senator FITZGERALD. Are you seeing more companies, though, pushing the envelope on securitizing products and not fully reporting the amount of recourse that is still available to the issuer of the securities?

Mr. KHAKEE. One of the fundamental parts of our criteria when we review structured financings is non-recourse and non-consolidation. To the extent that we are able to de-link the rating on a structured finance from the origination company—the bank that

securitizes the credit card receivables or the bank that securitizes the mortgages—non-consolidation and non-recourse are a very fundamental part of that analysis.

To the extent that we can receive the appropriate opinions and comfort that is being achieved, that gives us the comfort to issue ratings that de-link from the source of the original receivables. To the extent that is not achieved, you have not achieved certain elements of structured finance, which is to de-link from the origination company.

Senator FITZGERALD. So you are very careful to look at whether all those elements have been met to justify calling it a securitization transaction and that the company is justified in taking the securitizations revenues into earnings when they do? I mean, you carefully look at that?

Mr. KHAKEE. Yes, those aspects of criteria are fundamental parts of the analysis that any analyst would execute with regard to reviewing a structured financing.

Senator FITZGERALD. But in the case of Enron, they were able to persuade the rating agencies that a lot of their monetization contracts, I won't call them securitizations, were non-recourse, were they not, when in fact they were recourse?

Mr. KHAKEE. Well, I can't comment on the——

Mr. BARONE. I can handle that. No, in many cases, we would put back certain obligations that, while legally may have been non-recourse to Enron, there was an economic incentive, a moral incentive, or some other incentive and reason to include non-recourse debt in determining its credit rating. I would say there are many cases where they just never told us these obligations existed that had recourse, real or otherwise, to Enron. And I think that should be distinct.

Mr. DIAZ. In our case, that was the reason we were trying to get a hold of all the off-balance sheet debt, so we can take a good look at what the underlying economic benefits were and what the underlying recourse was. If we can make up our own minds, even if it was legally—in some cases, we can have project financings that are legally non-recourse and you can actually have a structure that says that. But if we think that the asset is an integral part of the company's strategy, we would actually count that as part of the credit ratios.

Mr. TURNER. Senator Fitzgerald, if I could address that for just a moment. At the Commission, I think we were concerned about the point you raise, and I think it is a very—it is an excellent, valid question. There have been trillions of dollars done in securitization and the monetization of assets, and there is no question that while originally we were monetizing high-quality credit card portfolios, now we are down to monetizing much more risky assets. And I think it is exposing the markets to some additional risk, and I am very concerned about that.

And we were seeing not only monetization of assets, but we were also seeing financial instruments going out with triggers in them, that if troubles happened with the company, that if it didn't pan out, all of a sudden that trigger would turn these companies into a death spiral. In fact, you would often hear that these financial instruments did have a death spiral.

Senator FITZGERALD. We had such triggers in the case of Enron.

Mr. TURNER. And those have not been adequately disclosed. There is no question about it. And I think there does need to be greater disclosure of that. We need to get greater disclosure of any financial instruments or off-balance sheet financings that might result in the risk of those coming back to the issuer. In particular, if the issuer is going to have to use cash or other resources that it might have to pay those, then that risk needs to be disclosed. And today, it is not being disclosed.

Ms. STUMPP. Senator, if I could just add on to that. Last week, Moody's released a report, Moody's Analysis of Ratings Triggers. And what we found in looking at all ratings triggers was that less than a quarter of the rating triggers—and this is based on company-supplied information—are disclosed in companies' SEC filings. So less than half—and less than, actually, 25 percent, according to the data compiled on issuer feedback to us—is disclosed in the SEC filings. Now, this is based on all types of triggers, including some that are relatively benign.

Senator FITZGERALD. Are they supposed to disclose it, those triggers? Or is it just some of them are voluntarily doing it and they are under no obligation?

Ms. STUMPP. Well, what we found in reviewing the data was that the less-risky type triggers—those dealing with pricing grids—were the ones that were typically disclosed, whereas the ones that basically revolved around the riskier types of triggers—puts, acceleration, default—were the ones that were not always typically disclosed.

So in answer to your question, we would certainly support heightened disclosure, particularly as it relates to off-balance sheet with recourse, and what are the types triggers or factors that would cause the debt to come back on to the balance sheet. This needs to be emphasized and the disclosure needs to be improved.

Mr. TURNER. This is a point where I couldn't agree more with Ms. Stumpp. And in fact, in the rule proposals that have been put out by the Commission, this is a big hole that are in those rule proposals, because this type of disclosure would not be required even under the new rule proposals.

So I think those need to be enhanced significantly for this reason. And certainly my experience was just like Ms. Stumpp's in finding that companies weren't disclosing them notwithstanding the fact that there are some SEC rules that say if you have something that could significantly impact the liquidity of the company, unless you are certain it is never going to happen, unless you are certain it is remote, even if you don't know whether it is going to happen or not, you have to disclose it. And we are just not seeing those type of disclosures being made today.

Mr. BARONE. Senator, in a similar vein, as Ms. Stumpp noted, we had also published a white paper on ratings triggers. We even listed the companies we thought had serious exposure—which did not necessarily produce a rating change, but meant that should a rating change occur, the company's creditworthiness could spiral out of control.

And just going to your other line of questioning, I don't know if you were here before, but I pointed out that—in my testimony—we

have a white paper that was titled "Accounting Abuses and Proposed Countermeasures," where we support many of the items the SEC is proposing and information that is in the Sarbanes Bill as well.

Senator FITZGERALD. If the Chairman would indulge me, could I ask about their opinion on the accounting matter you and I discussed?

Senator LEVIN. We can, but we are going to have to move on to our third panel. So if you want to just briefly get their opinion on that.

Senator FITZGERALD. Real quick. I mean, one of my theories here is that the reason we have seen such a rash of overstatements of earnings in the last year or so is that managers have a motivation, a powerful motivation, to at all times keep their earnings per share high and their stock price high. And that is the vast increase in—exponential increase in the issuance of stock options in the last few years, which aren't accounted for on the income statement. They are treated like manna from heaven. In the case of Enron, the top 29 executives cashed in $1.1 billion worth of stock options in the last 3 years before they put the company in bankruptcy. When you have executives who can make tens or hundreds of millions of dollars by keeping their stock price high by doing whatever possible to report higher per share earnings, at a certain point you have a powerful motivating force to bend the rules.

What do the rating agencies think about my and Senator Levin's proposal to encourage companies to account for stock option compensation expense, instead of the current system where they just ignore it except in a footnote.

Mr. BARONE. We would support greater disclosure of stock options in the financial statement reporting.

Mr. DIAZ. I would support that. I would say that stock option is a form of compensation, it should be taken into account as such when you are looking at a company's net income and earnings potential.

Senator LEVIN. Mr. Turner—I am sorry. Ms Stumpp.

Ms. STUMPP. Yes, I would agree. And it should be done on a basis that is consistent so that companies can be evaluated on the same accounting-standard basis.

Senator FITZGERALD. Right now, a company that pays its managers in cash has to report an expense. But if they pay the managers in options, there is no expense there. So it has to make it hard for you to get an apples-to-apples comparison. Is that correct?

Mr. BARONE. That is correct, yes.

Mr. DIAZ. You have to make certain assumptions as to how much those are worth. And yes, you could be off. So, yes.

Senator LEVIN. Well, we are doing our best to end the misuse of accounting relative to this stealth compensation. Mr. Turner, do you have any comment on the stock option issue? Should they be treated as compensation?

Mr. TURNER. Unquestionably they should be treated as compensation. As the former Vice President, Chief Financial Officer of a major high-tech company in this country, I can tell you that I participated with many of the leading high-tech companies in surveys in which we all characterized the options as expense. I would

be more than willing to share that with the Subcommittee. We even had our standard methodology for measuring those. These executives that say they can't measure the value of an option, we all knew what the value was that we were giving employees. And if a manager, if an executive can't figure out what he is paying employees in the form of paper versus cash, then quite frankly, probably he shouldn't be sitting in that company as an executive.

Senator FITZGERALD. What about a company that pays, like, a law firm bill or some vendor's bill in stock options? High-tech companies do that all the time. They will pay a law firm in stock options.

Mr. TURNER. We would record that as expense. And I will tell you, Senator, I recorded compensation expense for options in my financial statements and it never caused me a problem. It made it much more transparent.

Senator LEVIN. The temptation is great to pursue that issue because we put a lot of time in on it, and I hope we can still obtain that reform, this Congress, but we are going to have to move on. We thank this panel for your appearance here, and we will now move to our third panel.

Donald H. McCree, the Managing Director of Morgan Chase; Robert Traband, the Vice President of Morgan Chase Bank in Houston; and Jeffrey Dellapina, who is Managing Director of Morgan Chase Bank in New York. And I would ask you to please stand and raise your right hands.

Do you swear that the testimony that you will give before this Subcommittee will be the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. MCCREE. I do.

Mr. TRABAND. I do.

Mr. DELLAPINA. I do.

Senator LEVIN. Thank you for appearing here today. And we will again use that same timing system, which we have announced. And I believe that Mr. Traband is going to begin, is that correct?

Mr. TRABAND. I hand it off to my colleague.

Senator LEVIN. Mr. Dellapina first?

Mr. DELLAPINA. Yes, sir.

Senator LEVIN. Fine. Please proceed.

TESTIMONY OF JEFFREY DELLAPINA,[1] MANAGING DIRECTOR, JPMORGAN CHASE BANK, NEW YORK, NEW YORK, ACCOMPANIED BY DONALD H. McCREE, MANAGING DIRECTOR J.P. MORGAN SECURITIES, INC., NEW YORK, NEW YORK; AND ROBERT W. TRABAND, VICE PRESIDENT, JPMORGAN CHASE BANK, HOUSTON, TEXAS

Mr. DELLAPINA. Mr. Chairman and Members of the Subcommittee, my name is Jeffrey Dellapina. I am a Managing Director in the Credit and Rates Group of JPMorgan Chase & Co. I am accompanied by my colleagues Don McCree, a Managing Director, and Robert Traband, a Vice President. I was involved in the Enron prepay transactions beginning in 1997. Mr. Traband is based in Texas, and worked on the Enron account beginning in 1999. Mr.

[1] The prepared statement of Mr. Dellapina appears in the Appendix on page 312.

McCree currently serves as senior credit officer for the JPMorgan Chase Bank. He was not involved in the transactions that are being discussed today. He is here because the Subcommittee requested a senior banker who could address broad policy issues. I am presenting this oral statement on behalf of the three of us.

JPMorgan Chase & Co. is a holding company. Through our subsidiaries and affiliated companies we offer global financial services, have operations in more than 50 countries, and serve more than 30 million consumers and the world's most prominent corporate, institutional, and government clients, including over 90 percent of the Fortune 1000 companies. JPMorgan Chase & Co. and its subsidiaries and affiliated companies employ nearly 100,000 people throughout the United States and worldwide.

Our institution has an established reputation for integrity, and we welcome the opportunity to appear today at the invitation of the Subcommittee. In accordance with the Subcommittee's request, this statement will focus on and provide background information with respect to the prepaid natural gas and oil forward contracts involving JPMorgan Chase and Enron.

At the outset, we wish to emphasize two significant points. First, prepaid forward contracts have been used for many years and are widely recognized as an entirely proper tool to enable businesses to increase their liquidity and diversify their sources of funding. Second, we do not provide accounting services to our clients. In the U.S. financial system, those are responsibilities that are properly assigned to the client's management, advised by its auditors, both internal and external, guided by generally accepted accounting principles.

Before we turn to the Enron prepaid forward transactions, we would like to talk generally about corporate finance and prepaid forward commodity contracts in order to place these specific transactions in their proper context.

Senior financial officers of major corporations are continuously working to ensure that their companies' ongoing access to capital will enable asset growth and business prosperity. The management process includes taking actions to maintain liquidity and diversify the corporation's source of funds. In support of these objectives, lawyers, accountants, commercial bankers, and investment bankers all work with clients to structure financial transactions that have favorable characteristics within the parameters of existing accounting, tax, and legal requirements.

Financing can be obtained in a multitude of ways, including, for example, common equity, preferred stock, loans, commercial paper, and other debt securities and, in the case of financial trading firms, repurchase and forward agreements. These are other forms of transactions that are designed to meet particular financing needs, commonly referred to as "structured finance" transactions. The structured finance market is very large, and is participated in by the world's major financial firms. Examples of structured finance transactions include collateralized debt obligations, such as mortgage-backed securities and credit card securitizations, debt-equity hybrid securities, leases of all varieties, convertible bonds and convertible preferred stock.

Prepaid forward commodity transactions are also a form of structured finance. In forward commodity transactions, which are common in many industries, the parties enter into a contract for sales and deliveries of the commodity at future dates. A prepaid forward provides for payment to be made at the inception of that contract.

The specifics of structured finance transactions may differ significantly from client to client as we and other financial firms participate in transactions to meet the specific needs of each client. What these transactions have in common is increased liquidity and the diversification of funding sources. Diversification of funding sources is a matter of prudence. Throughout recent history, there have been numerous events that have had an adverse impact on the ability to access one or more funding sources and on the cost of doing so. Diversifying sources of financing mitigates a corporation's exposure to such events and enables it to maintain and expand its core business.

Let me now turn to the specifics of the Enron transactions themselves. Let me first emphasize that the more than 20 transactions before you were not all identical.

In 1992, Enron approached the Chase Manhattan Bank, one of the four predecessor banks that have now all been merged into JPMorgan Chase, with a request that it enter into a prepaid forward transaction. At that time, there was some uncertainty as to whether Chase, as a national bank, was authorized to accept physical delivery of a commodity. Therefore, the 1992 transaction was accomplished by having a special purpose entity, or SPE, take delivery of the commodity. SPEs are companies that are established for a particular purpose. They are widely used in structured finance transactions. As the people working on the transaction were located in London, a Jersey SPE was used.

From 1993 through 2001, Enron entered into a total of 11 more prepaid transactions involving Chase. Ten of the transactions were with Mahonia Limited and one was with Mahonia Natural Gas Limited, both Jersey Channel Islands SPEs. All but one of these transactions were physically settled transactions, meaning that they were settled with deliveries of gas and oil. The last transaction was financially settled, meaning no commodity was delivered, although the cash payment was to be determined by the price of natural gas.

Prior to continuing with the chronology, we would like to address Mahonia. Mahonia is beneficially owned by a charitable trust. Neither Chase nor Enron has any ownership interest in Mahonia. No employee or officer of Chase or Enron served as an officer or director or held shares in Mahonia. The directors and officers of Mahonia make the ultimate determination as to whether or not to enter into a transaction. Those directors and officers are neither appointed nor controlled by Chase or Enron. The use of entities like Mahonia is standard activity in structured finance.

In the Enron prepaid forwards. the SPE entered into a prepaid forward contract with an Enron subsidiary using funds provided by Chase. The prepaid forward transaction created not only credit risks for Chase, but performance, delivery, and commodity price risks as well. As mitigants for these transactions—as mitigants for these risks, the transactions included an Enron Corp. guarantee, a

performance letter of credit or a surety bond, and either exchange-traded futures contracts or over-the-counter derivative contracts with Enron Corp. Although the last prepaid transaction was financially settled, similar risks and mitigants were present in that transaction, the sole difference being that no physical delivery was required. Originally, the commodity purchased from Enron was sold into the broader market. After Chase was capable of taking physical delivery of gas or oil, Chase purchased the commodity from Mahonia and in turn sold physical gas or oil into the market. Beginning in the late 1990's, Chase entered into contracts to sell its gas or oil positions to Enron, which was by far the largest market participant.

All of the prepaid transactions in which the Subcommittee has an interest were undertaken at the initiative of Enron. Chase understood that the transactions originally had tax benefits for Enron. Later, Chase learned, Enron no longer received tax benefits from the transactions but chose to continue to engage in prepaid forward transactions for other corporate purposes. Enron management informed Chase that the prepaid forwards served to monetize the unrealized profit in its trading book. Enron also advised Chase that the rating agencies wished to see more cash generated from its growing trading activities.

There have been allegations in the media that the prepaid forward transactions were disguised debt or a disguised loan. The prepaid forwards were undoubtedly financing, as all contracts are that involve prepayment features, but every financing is not a loan. These transactions had different features, benefits, and risks than loans.

These prepaid transactions were accounted for on the books of JPMorgan Chase consistent with GAAP. It is our understanding that Enron reported these transactions as liabilities on its balance sheet in accordance with GAAP; in other words, they were not off-balance sheet transactions. As I stated earlier, however, the manner in which Enron accounted for these transactions on its books and in its financial statements was a matter for Enron and its management and auditors.

As the Subcommittee is aware, JPMorgan Chase was one of several financial firms that provided financial services to Enron. We have been one of the parties substantially harmed by its failure, incurring hundreds of millions of dollars in losses. JPMorgan Chase welcomes this opportunity to answer the Subcommittee's questions today and will continue to cooperate with the Subcommittee's inquiry. This concludes our oral presentation, and we would be pleased to respond to your questions.

Senator LEVIN. Thank you, Mr. Dellapina. Mr. Traband.

Mr. TRABAND. He was representing all three of us.

Senator LEVIN. It is very clear that Enron saw prepays as a way to get cash without reporting it as debt. If you will look in your books at Exhibit 111,[1] exhibit books in front of you, there is a page from an Enron document on prepays. "Why does Enron enter into prepays?" "Off-balance sheet"—the first bullet. "Off-balance sheet financing." That is, it generates cash without increasing debt load.

[1] Exhibit No. 111 appears in the Appendix on page 365.

Now let us see how Chase saw the prepays. Take a look, if you would, at Exhibit 139.[2] This is one of Chase's structuring summaries, the documents which are used to gain credit approval for a financial transaction. It echoes that same thing.

In the past 3 years—if you look at—near the bottom of the front page there—in the past 3 years Enron has utilized the prepaid sale as a mechanism to address a number of needs, including refreshment of Section 29 credits and sourcing funds classified as liabilities from price risk management as opposed to long-term debt.

So Chase is clearly aware that that is one of Enron's motives, to classify that income as price risk management rather than long-term debt.

Now, I also want to refer you now to Exhibit 123.[2] This is an email from George Serice—I believe that is how he pronounces his name—who is an investment banker with Chase. And the third paragraph reads as follows:

"Enron loves these deals, as they are able to hide funded debt from their equity analysts, because they, at the very least, book at as deferred revenue or, better yet, bury it in their trading liabilities."

That is what Chase knew.

Now, does this email not provide some pretty compelling evidence as to what Chase knew? "Enron loves these deals"? This is 1998, November. "Enron loves these deals, as they are able to hide funded debt from their equity analysts . . ." better yet—even better than deferred revenue—they "bury it in their trading liabilities."

Do you have any comment on that email?

Mr. TRABAND. Yes. This email predates my involvement with Enron, but I can tell you my own understanding of the purpose of the prepays and how I viewed them.

Senator LEVIN. I am not asking you that question. You could have testified to that. My question is do you have any comment on that email? This is a Chase person here, now, acknowledging what Enron is doing—acknowledging. They love these deals. It allows them to hide funded debt. They can bury this in their trading liabilities—which is exactly what happened, and Chase knew it in 1998. Do you have any comment on this email, Mr. McCree?

Mr. CREE. I think I would view that as a casual commentary by an employee that, frankly, was not informed as to the completeness of the entirety of the transactions.

Senator LEVIN. Would you agree it is a devastating commentary?

Mr. MCCREE. Well, I don't know, devastating. I don't think he was fully informed as to Enron's intention or the full structure of the Mahonia as they were put together.

Senator LEVIN. Are you embarrassed by that?

Mr. MCCREE. I am confused by it.

Senator LEVIN. You are not embarrassed by this?

Mr. MCCREE. I think it is an unfortunate statement. I don't think it bears resemblance to how we as an institution view the transactions that were undertaken here.

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[2] Exhibit No. 139 appears in the Appendix on page 482.
[2] Exhibit No. 123 appears in the Appendix on page 414.

Senator LEVIN. OK, Mr. Dellapina. You are in this email.

Mr. DELLAPINA. I don't——

Senator LEVIN. Do you have any comment on that?

Mr. DELLAPINA. Yes, I don't recall receiving it or responding to it. But I certainly have had a chance to look at it recently, and I believe that it is inaccurate. I believe that prepaid forwards are fundamentally different than funded debt.

Senator LEVIN. When you say it is inaccurate, are you saying that Enron did not love those deals?

Mr. DELLAPINA. I am unfamiliar with why that comment was raised.

Senator LEVIN. But you are not saying that is inaccurate?

Mr. DELLAPINA. I am saying the reference to funded debt, which is throughout this document, I believe to be inaccurate.

Senator LEVIN. But I want to get back to this question. Here you got a Chase email that you received, or at least you are referred to in the email, that says Jeff Dellapina and Bob Mertensotto worked on a deal this summer where they took out a couple of older prepaid PLCs with these surety bonds. Jeff is also working on another prepay for Enron now.

That is you. It is the only "Jeff" in here.

And then it says something, and I want to ask you whether or not you deny its accuracy. "Enron loves these deals, as they are able to hide funded debt from their equity analysts"—do you deny that, first of all, that Enron loved those deals for that reason?

Mr. DELLAPINA. Mr. Chairman, I have no reason to believe why they would love them or why they would not love them, and its impact on equity analysts.

Senator LEVIN. All right. Do you deny that Enron loved these deals not just because they could hide it, but because they could bury it in their trading liabilities? You are not able to deny that either, are you?

Mr. DELLAPINA. I know that the transactions, or at least it was represented to the bank that the transactions were reflected in their trading liabilities. The references to "bury"——

Senator LEVIN. The word here in the Chase memo is "bury." Does that embarrass you?

Mr. DELLAPINA. It confuses me as well. I believe it to be inaccurate.

Senator LEVIN. Now, here is Chase's—well, let me just say this. If I were Chase, I would be embarrassed. I would be ashamed of that email. Let me just get that on the record. But I am not sure what will embarrass or shame you, so let me go on to Exhibit 128.[1]

Here is your prepay pitch. Now, you are making a pitch for prepays. And the introduction says the following about prepays. And this is—I think it is page 3 of this Exhibit, where it says "Introduction." Let me just—so that I connect both Mr. Traband and Mr. Dellapina to this particular document. There is an email, which is the front page of Exhibit 128, which shows a copy of this going to Mr. Dellapina, and it is to Mr. Traband, and it says, this is P&C. What does that mean?

Mr. DELLAPINA. I believe P&C means private and confidential.

[1] Exhibit No. 128 appears in the Appendix on page 419.

Senator LEVIN. And not for distribution? So only use this for your own education. OK?

Now, on, I think it is page 3, but in any event, it is the page which is headed by "Introduction." It says: "Prepayment received for a forward sale of inventory: Fixed quantity; specific delivery location(s)." It is an "Alternative source of finance," and its "Balance sheet 'friendly'."

And then on page 5, it says the following: "Attractive accounting impact by converting funded debt to 'deferred revenue,' or long-term trade payable."

Isn't the "balance-sheet friendly" aspect of prepays a selling point which Chase stressed when it pitched this product to other companies? Is that an accurate statement?

Mr. TRABAND. In the course of our dialog with our clients we certainly discuss the merits of transactions, and among those are accounting or tax issues. At the end of the day, we are not—we do not advise them on those issues and they go back and talk to their own accountants and attorneys.

Senator LEVIN. Part of your pitch, is it accurate to say, is that these prepays have an attractive accounting impact by converting funded debt to deferred revenue or long-term trade payable? Isn't that what you represent to people who are hearing that pitch?

Mr. TRABAND. That is certainly in the pitch. And there are different forms of liabilities that appear differently on the balance sheet. Ultimately all are liabilities. And for different types of financing transactions, one may more accurately reflect the transaction.

Senator LEVIN. At least this is part of your pitch that you made?

Mr. TRABAND. That is part of the pitch.

Senator LEVIN. So on the next page of the pitch book is the phrase "attendant tax benefits." Now, is it not the case that the funds that Enron received from these prepays could be considered by them as a loan for tax purposes?

Mr. TRABAND. I can't speak to the tax treatment of these transactions.

Senator LEVIN. What are the attendant tax benefits? Can that not be treated as a loan? Is that not one of them?

Mr. TRABAND. I don't know what the attendant tax benefits are.

Senator LEVIN. Well, who was making the pitch?

Mr. DELLAPINA. I may have——

Senator LEVIN. Dellapina made the pitch. So what did——

Mr. DELLAPINA. I may have contributed to the pitch as well. I am not a tax professional and do not understand tax. What I believe it refers to, and again, this is not an expert opinion, but that the use of a prepaid forward could be used either as current income or possibly treated as taxable income on a deferred basis. That is current taxable income. That is about the extent of the tax knowledge that I have.

Senator LEVIN. Is the interest paid deductible, do you know?

Mr. DELLAPINA. There is no interest paid on a prepaid forward.

Senator LEVIN. Are the fees or the payments deductible?

Mr. DELLAPINA. I am not familiar with the accounting.

Senator LEVIN. Are any of you familiar with the tax benefits which you pitched to companies?

Mr. MCCREE. No, I think what we would likely say in a situation like that is the tax attributions of any deal, structured finance, prepaid, will be dependent upon the tax characteristics of the individual company. And that would be a matter between their tax advisors and themselves. But in our experience, prepaids had certain tax attributes which were attractive to a variety of our clients.

Senator LEVIN. Would you agree, Mr. McCree that one of the tax attributes—one of the attributes—was the attractive accounting impact by converting funded debt to long-term trade payable? Would you agree that is something which is attractive, that you made a pitch to——

Mr. MCCREE. I don't know about——

Senator LEVIN [continuing]. Potential clients?

Mr. MCCREE. I think the ability for, certainly in Enron's case, the company to treat this as a trading liability, which is how they treated it based on advice from Andersen, was an attractive feature to the prepaids.

Senator LEVIN. And you pitched you could convert funded debt to deferred revenue or long-term trade payable?

Mr. MCCREE. I don't know the answer to that. I don't know if that was——

Senator LEVIN. You don't know if your company made——

Mr. MCCREE. That is what it says.

Senator LEVIN. Well, this is your company.

Mr. MCCREE. Yes, it is.

Senator LEVIN. Are you familiar with that document?

Mr. MCCREE. I have never seen it.

Senator LEVIN. Are you familiar with that document, Mr. Traband?

Mr. TRABAND. I recall distantly that document.

Senator LEVIN. Mr. Dellapina.

Mr. DELLAPINA. I am familiar with, yes, components of the document.

Senator LEVIN. All right. So that is one of the attractive attributes of this particular approach, is that not correct? And you made that pitch to companies, right?

Mr. DELLAPINA. Yes, I don't recall the specific details of the pitch. One of the parties that would do a transaction like a prepaid forward would be a producer of a commodity, and it—it would probably be a pretty accurate way of portraying a forward sale, and the actual forward sale of the commodity as a deferred revenue item. And actually raising finance in that manner.

Senator LEVIN. What companies did Chase sell this product to? Can you give us the list?

Mr. MCCREE. Mr. Chairman, if possible, and as a general matter, we at JPMorgan, both from an individual standpoint and a corporate standpoint, guard the confidentiality of our clients closely and believe in keeping their information private. So if it would be possible not to go into specific company names, that would be important to us as a policy matter. If you insist we do it, we are happy to do it.

Senator LEVIN. Is it accurate to say that one, two, three, four, five, six, at least seven companies bought that pitch?

Mr. MCCREE. I don't know—do you know?

Mr. DELLAPINA. I do not know whether all seven of those companies were actually pitched.

Senator LEVIN. Can you give us the number of companies which bought this approach from Chase?

Mr. DELLAPINA. Well, I can tell you there were seven companies that entered into transactions, as we supplied to the Subcommittee, with Mahonia. I cannot confirm that they were pitched. The prepaid forward transactions were fairly well known in the market, and I can't confirm that I pitched this to all seven of those.

Senator LEVIN. Can you tell us how many you did pitch it to?

Mr. DELLAPINA. I cannot tell you what number of companies I pitched it to.

Senator LEVIN. Now, Mr. Turner on the previous panel said there are a number of criteria that prepaid transactions must meet before they can be considered real trades and accounted for as such. They have to be independent trades among independent parties, there must be price risk, among other criteria.

Mr. Dellapina, were the trades that made up the Chase prepaid transactions with Enron independent trades between independent parties?

Mr. DELLAPINA. Yes, I believe they were.

Senator LEVIN. Let us look at Mahonia now, just to see how independent Mahonia was. If you look at Exhibit 118.[1] First, this is from a firm, a law firm in the Channel Islands, are these offshore folks that you work with? Mourant? It says, "our clients, Chase Bank & Trust Company Limited." So, now, Chase is the client of Mourant, this offshore Channel Island firm—so it represents Chase. And here is the letter that goes to the Registrar of New Corporations and Trusts in Jersey. And the letter says the following:

"Our clients, Chase Bank & Trust Company Limited . . . are considering promoting from time to time specific purpose vehicles for use in particular banking transactions. The possible areas in which the SPV's could be used are numerous, but at this stage it can be foreseen that the likely use for them would be:"—and then the letter lists one of the reasons as "where a company wishes to raise finances not by way of borrowing but by way of a related transaction." That is number one.

Now, the letter goes on to say, if you look at the top of page 2: "For obvious reasons, it is important that the SPV"—the special purpose vehicles—"are controlled by Chase."

". . . It is important that the SPV's are controlled by Chase." And I want you to remember those words.

But for accounting and other requirements it is not desirable that they are wholly owned by Chase. Accordingly, Chase is considering establishing a charitable trust which would own all the shares of a holding company, which in turn would wholly own the various SPVs.

Are you familiar with that letter?

Mr. DELLAPINA. I have never seen that letter from 1986, so——

Senator LEVIN. Do you have any reason to doubt its authenticity? You, Mr. McCree, are you familiar with this letter?

[1] Exhibit No. 118 appears in the Appendix on page 394.

Mr. MCCREE. No, never seen it.

Senator LEVIN. Your lawyers haven't gone over this with you, this letter?

Mr. MCCREE. No.

Senator LEVIN. This is the first time you are seeing it, all of you?

Mr. MCCREE. Yes.

Mr. TRABAND. Yes.

Mr. DELLAPINA. The first time.

Senator LEVIN. OK. So here goes. Your lawyer says it is important SPVs are controlled by Chase, but for accounting and other requirements it is not desirable that they be wholly owned by Chase: "Accordingly, Chase is considering establishing a charitable trust"—Chase is considering establishing a charitable trust—"which would own all the shares of a holding company which in turn would wholly own the various SPVs."

And there is a second letter in this packet here, April 29, from the Jersey office, telling the incorporating law firm that such an entity would not be a problem.

Next document, then, is May 13. It shows that—excuse me, the next document is May 12, received on May 13, showing that East Moss Limited has in fact been formed.

Then if you will skip to the letter after next, which is the one that Chase's attorney, James Mourant, wrote to the Jersey agency on May 29, 1986, to explain a financial transaction that involved Chase and East Moss Limited. And this is what he wrote—if you will look at the middle of page 2:

"In order that the U.S. authorities could be entirely satisfied with the arrangements it was considered preferable that my firm's trust company act as trustee of the charitable trust and administer East Moss rather than Chase Jersey."

So now we have Chase's agent, a trust company of Chase's agent, Mourant, acting as trustee of the trust. OK?

Now, the next document is Mahonia's registration form to the Jersey Commercial Relations Department. And we can see there that when Mahonia was formed in 1992, Chase's agent, Mourant, was listed as the owner. Do you see that, down—number 7, beneficial owner? It is your agent, Mourant.

So, any doubt in your mind that Chase controlled Mahonia?

Mr. MCCREE. Well, I would say that Chase did not control Mahonia and Chase did not own Mahonia. It was set up as a separate special purpose——

Senator LEVIN. Who did own Mahonia?

Mr. MCCREE. A charitable trust.

Senator LEVIN. And who owned the charitable—who established the charitable trust?

Mr. MCCREE. I don't know the answer to that.

Senator LEVIN. Well, it is in this letter. Chase established the charitable trust.

Mr. MCCREE. I am just looking at this letter—the 1986 letters referred to a bid by Dixon's for Woolworth's. It looks to me like a completely unrelated transaction. I have never seen the letters before, so I don't know the specifics as to the transactions that are referenced to in the 1986 letters and the linkages between Mahonia. I just don't know the answer to that, Senator.

Senator LEVIN. Well, take a look again at that May 19, 1986, letter.

"Further to our application to incorporate an investment holding company to be called East Moss Limited, I am writing to give you further details."

This is your agent writing the registrar, now, in Jersey. And right in the middle:

"I should begin by mentioning that although this particular transaction is part of a Chase scheme"—that is your agent's words—"for various reasons, one of my firm's trust companies will in fact be acting as trustee of the charitable trust."

Your agent's trust company—are you with me so far—is going to be the trustee and administering East Moss Limited. Any problems so far?

Mr. DELLAPINA. Mr. Chairman, may I just make a comment?

Senator LEVIN. Sure.

Mr. DELLAPINA. None of us have seen this email before—this letter before. And the suggestion that Ian James was our agent or our attorney, I do not understand that. For the period of time——

Senator LEVIN. The suggestion by whom?

Mr. DELLAPINA. That he was our attorney.

Senator LEVIN. Whose suggestion?

Mr. DELLAPINA. I think the suggestion—at this hearing.

Senator LEVIN. No, the suggestion by your attorney. "Our clients"—do you see that? Exhibit 118?[1] Our clients, Chase? It is not the suggestion here; it is your lawyer's statement that he represents you. Now, who pays his fees? Who pays Mourant's fees?

Mr. DELLAPINA. On the transactions that I have been involved with, we have—the Chase Manhattan Bank has paid the fees for Mourant.

Senator LEVIN. There you go. Mourant writes the letter, says he is your lawyer. You are paying his fees. Mourant's trustee is running the charitable trust that owns the holding company that owns Mahonia. You can put as many layers on this as you want, but it comes right back to it. Your agent has a trust which is the trustee of a charitable trust which owns a holding company which owns Mahonia.

Folks, is there any doubt about what I am saying, in your mind? This may be the first time that you are seeing it, but you are seeing it. It is right in front of you. Do you have any reason to doubt that?

Mr. MCCREE. I just—my understanding is that we do not own Mahonia, we do not control Mahonia.

Senator LEVIN. Who gave you the understanding you don't control Mahonia? Who told you that?

Mr. MCCREE. It might have been Jeff.

Senator LEVIN. Jeff, who told you you don't own Mahonia?

Mr. DELLAPINA. When I started doing the transactions, I understood this to be an independent SPE, from our attorneys. I don't recall specifically who would have conveyed that information. We have always known Ian James to be the attorney for Mahonia. And yes, Ian James with Mourant's fees have been paid by the Chase

[1] Exhibit 118 appears in the Appendix on page 394.

Manhattan Bank. We don't view this as entirely uncommon. It is not uncommon, for example, in a closing of a home mortgage that a client would pay a bank's attorney's fees. But we have always known—I have always known Ian James to be the attorney for Mahonia.

Senator LEVIN. You pay their fees.

Mr. DELLAPINA. We do pay their fees.

Senator LEVIN. And this is the first you ever heard that you folks established Mahonia? This is the first you have ever heard of that?

Mr. DELLAPINA. Mr. Chairman, when Enron approached JPMorgan Chase to do a prepaid forward transaction, as we described in the statement, Chase—we were not sure as to whether Chase could take physical commodities at that point. Chase did at the time approach Mourant and ask if there was an SPE that would be interested in entering into the transaction. That is to the best of my information. I was not in the group at the time.

Senator LEVIN. Who pays all the costs associated with the administration of Mahonia.

Mr. DELLAPINA. Those costs are paid by Chase.

Senator LEVIN. Not just the legal fee?

Mr. DELLAPINA. Not just the legal fees.

Senator LEVIN. And who pays Mahonia's annual Jersey statutory charge?

Mr. DELLAPINA. I am not sure of the answer.

Senator LEVIN. Do either of you know? Well, let me tell you: Chase does. You pay the annual charge, you pay the legal fees, you pay the administrative costs, you established Mahonia. Your lawyer is the agent for it. And you are telling me you don't have any control over Mahonia? You are under oath. You are telling me Chase has no control over Mahonia?

Mr. MCCREE. I don't believe we control the individual decisions of Mahonia.

Senator LEVIN. Do you have any control over Mahonia at all, Mr. McCree?

Mr. MCCREE. Not to my knowledge.

Senator LEVIN. Mr. Traband.

Mr. TRABAND. Not to my knowledge.

Senator LEVIN. Mr. Dellapina.

Mr. DELLAPINA. To the best of my knowledge, Mahonia and its attorneys——

Senator LEVIN. Despite all that.

Mr. DELLAPINA. I do not believe we control Mahonia.

Senator LEVIN. You have no control over it. Does your agent control it, Mr. McCree?

Mr. MCCREE. I don't believe so.

Senator LEVIN. Is Mourant——

Mr. MCCREE. I don't know who the board of directors of Mahonia is, but I believe the board of directors of Mahonia controls the decisions of that company.

Senator LEVIN. Do you know who is on that board?

Mr. MCCREE. I do not off the top of my head.

Senator LEVIN. Do you know who is on that board, Mr. Traband?

Mr. TRABAND. I don't know who is on the board.

Senator LEVIN. Mr. Dellapina.

Mr. DELLAPINA. I believe I know at least one individual who is on the board.

Senator LEVIN. Who is that?

Mr. DELLAPINA. I believe Ian James. He is a director of Mahonia. Ian James is an attorney at Mourant.

Senator LEVIN. And that is the law firm that you pay the fees to, right?

Mr. DELLAPINA. That is the law firm that represents Mahonia.

Senator LEVIN. And you pay the fees to.

Mr. DELLAPINA. And we paid their fees on these structured transactions.

Senator LEVIN. Do you know whether Mahonia has ever entered into a commercial transaction in which Chase was not involved?

Mr. DELLAPINA. I do not believe so.

Senator LEVIN. Mr. Traband.

Mr. TRABAND. I am not aware of any.

Senator LEVIN. Mr. McCree.

Mr. MCCREE. I do not know.

Senator LEVIN. Did Chase serve as Mahonia's agent in the prepays, Mr. Dellapina?

Mr. DELLAPINA. I believe that we served as an agent for commercial transactions.

Senator LEVIN. Did Chase serve as Mahonia's agent in the prepays?

Mr. DELLAPINA. I believe that is correct.

Senator LEVIN. Mr. Traband.

Mr. TRABAND. I don't know the answer.

Senator LEVIN. Mr. McCree.

Mr. MCCREE. I am sorry, I don't know.

Senator LEVIN. You don't know.

Now, Exhibit 184(a)[1] is a transcript of part of a phone conversation which was recorded apparently by Chase.

Mr. Dellapina, let me address this to you. This is a transcript of part of a phone conversation that you had with Mr. Traband here, Mr. Serice, who wrote that honest letter about what the motives here were of Enron, and Joe Deffner and Lisa Bills of Enron, and it was on September 13, 2001, and if we can play that conversation, do we have that? Do you see the transcript in front of you at the bottom of page 7—I am sorry, at the bottom—it is in Exhibit 184.

[Audio tape played.]

Senator LEVIN. Let's go back now in the transcript. Ms. Bills—this is the best that we understand. We need to have—excuse me, Mr. Garberding, I guess, is speaking here first. "We need to have a specific rep letter that a representative of Mahonia signed that reference a certain point." Ms. Bills: "Which is, yes, separate from Chase. It doesn't have Chase showing up anywhere on the fax letterhead or anything along those lines, a separate fax number, etc." Mr. Dellapina. "Oh, talk about it, yes." Mr. Deffner. "That goes to the same point you were raising"—you were raising—"earlier, Jeff, that from your side you also want to make sure that Mahonia seems independent." "Seems independent."

[1] Exhibit No. 184(a) appears in the Appendix on page 665.

Mr. Dellapina, if Mahonia is independent, you don't need to make it seem independent.

Mr. DELLAPINA. I entirely agree with that statement. To the best of my understanding——

Senator LEVIN. Why do you want to make it seem independent?

Mr. DELLAPINA. I don't believe I would have wanted it to seem independent.

Senator LEVIN. It says right here though——

Mr. DELLAPINA. I believe it is independent.

Senator LEVIN. "That goes to the same point you were raising earlier, Jeff, that from your side you also want to make sure that Mahonia seems independent." That's the point you were making, Jeff.

Mr. DELLAPINA. Mr. Chairman, that's a statement by another individual.

Senator LEVIN. Did you disagree with that?

Mr. DELLAPINA. I disagree that I——

Senator LEVIN. No. Did you disagree with it on the phone conversation, Mr. Dellapina?

Mr. DELLAPINA. I did not challenge that point on that phone conversation.

Senator LEVIN. No, you didn't challenge the fact that you had made that point earlier. The representation that was made here by Deffner that "That goes to the same point you were raising earlier, Jeff, that from your side you also want to make sure that Mahonia seems independent." Do you deny ever making that point?

Mr. DELLAPINA. I do not believe that Mahonia is not independent. I believe it is independent.

Senator LEVIN. Do you deny under oath that you stated earlier in this conversation or sometime before that you also wanted to make sure that Mahonia seems independent or words to that effect? Do you deny having said that?

Mr. DELLAPINA. Mr. Chairman, I don't recall what I said in that conversation or in an earlier conversation.

Senator LEVIN. OK. Now take a look at Exhibit 142.[1] This is an email from an attorney at Chase to Mourant. Your lawyer, your agent. You pay him.

The second line down there, it says—so this is now from an attorney at Chase to the attorney in the islands there, the Jersey Islands. "At this point, while not a certainty, it looks like we will need to form Mahonia 3."

"We will need to form Mahonia 3."

"In addition to entering into the prepay with Enron North America, this entity will be entering into a contract to sell its rights to receive gas under the prepay agreement to a group of purchasers, including Chase. In this connection, the purchasers will appoint Mahonia 3 to act as its agent in handling the sale of the natural gas delivered under the Enron contract. The purchaser of the gas in this contract will be Chase. Chase will then sell the gas pursuant to a fixed price forward contract to Stoneville Aegean, an SPV that entered into transactions introduced by Chase in the early to

[1] Exhibit No. 142 appears in the Appendix on page 492.

mid-1990's. Stoneville will then sell the gas pursuant to a fixed price forward contract to Enron."

Great specificity as to what Mahonia 3 is going to be doing during the next so-called prepay.

So Mahonia 3 was created and it did engage in so-called prepay with Chase and with Enron. Now, Mr. Dellapina, Mahonia is an independent entity. Why is a lawyer from Chase telling Mahonia's administrators that "we will need to form Mahonia 3"? If Mahonia is independent, why is Chase telling Mahonia's administrators that?

Mr. DELLAPINA. In this structured transaction, I believe as is common in other structured transactions, the bank introduces the idea of a transaction to a party, in this case the law firm that had, in fact, formed or identified Mahonia for the first transaction. So raising this as a new opportunity for this attorney seems consistent with what would be done in a structured transaction, to the best of my knowledge.

Senator LEVIN. So now your attorney—or, excuse me, Chase's is describing in great detail what contractual arrangements this supposedly independent entity you are going to decide to enter into when it hasn't even been formed yet? You are laying out all the specifics of contractual arrangements that an independent entity is supposed to apparently make decisions on, and that entity hasn't even been formed yet. In fact, you are telling someone to form that entity. You call that independence? Is that your definition of independence?

Mr. DELLAPINA. The use of SPVs in these transactions are designed to create independent legal agreements, an independent legality in the transactions. Ultimately we will explain to you later that that legal independence did, in fact, create financial—additional financial risk to us and additional financial harm.

Senator LEVIN. Exhibit 120,[1] if you will take a look at it, February 28, 2002. This is an email between two employees of your agent, Mourant & Company, administrator of Mahonia. In this email, one employee reports that Chase has just informed her that it discovered that Mahonia was inadvertently omitted from the gas delivery agreements related to one of the 1998 prepay transactions. Four years, nobody was even aware of the fact that Mahonia was omitted from the agreement, so title to the gas was never transferred to Mahonia.

Then she writes the following: "Accordingly, new pipeline agreements need to be completed, reflecting the providers delivering to Mahonia, who in turn deliver to JPMorgan."

"New pipeline agreements need to be completed. He will forward the paperwork to me by fax and would be grateful if the directors would consider execution as soon as possible."

Were those papers delivered, do you know, Mr. Dellapina?

Mr. DELLAPINA. I do not know.

Senator LEVIN. You are not familiar with this?

Mr. DELLAPINA. I'm not familiar with this email.

Senator LEVIN. No. Are you familiar with the problem?

Mr. DELLAPINA. Generally. Not specifically.

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[1] Exhibit No. 120 appears in the Appendix on page 411.

Senator LEVIN. Generally, were you familiar that Mahonia was left out of one of these transactions and you had to go back and create new papers to include it?

Mr. DELLAPINA. I don't know that Mahonia was left out of the transaction. I don't—what I generally understand is that there was an operational issue—it wasn't appropriately booked on an operational basis with the pipeline. But I don't know much more than that.

Senator LEVIN. You're not familiar with the fact that there was a discovery of an anomaly that it was left out of a transaction? This is the first time you are hearing about that?

Mr. DELLAPINA. No. I am generally aware that there was an operational issue that it was not actually booked properly.

Senator LEVIN. Not booked properly. Mahonia was left out, right?

Mr. DELLAPINA. I don't understand "left out."

Senator LEVIN. You don't understand what?

Mr. DELLAPINA. "Left out."

Senator LEVIN. Omitted. Wasn't included.

Mr. DELLAPINA. All of the legal paperwork was executed. I understand that the issue was relating to the actual communication with the pipeline company and the actual recording by the pipeline company.

Senator LEVIN. Was there a new pipeline agreement that was completed reflecting the providers delivering to Mahonia, who then in turn delivered to JPMorgan?

Mr. DELLAPINA. That I am not aware of.

Senator LEVIN. Let me read you one line from this memo. "Greg has just called to advise that JPMorgan's agents have arranged to settle the invoice and that they do not need our instruction. Have also advised that they have just discovered anomalies in the Texas Eastern Pipeline agreements in respect to certain trades, whereby the pipeline agreements are made directly between the providers and JPMorgan, effectively bypassing Mahonia."

How's that for a definition of "left out"? Is that better? Were you familiar with—are you familiar with the fact that Mahonia was bypassed inadvertently?

Mr. DELLAPINA. Inadvertently, I am familiar that on the pipeline records, the gas does not note Mahonia in the title chain.

Senator LEVIN. Are you aware of the fact that this was described as an inadvertent bypassing?

Mr. DELLAPINA. That it was described as that?

Senator LEVIN. Yes.

Mr. DELLAPINA. No. I have not seen this email before, and I'm not familiar with that.

Senator LEVIN. All right. But you are generally aware of the fact that Mahonia was inadvertently bypassed in one of these deals in the booking?

Mr. DELLAPINA. Yes.

Senator LEVIN. All right. Now, if Mahonia is an independent company and it was bypassed for 4 years, would you say that it is particularly an independent company? If someone discovers 4 years later that Mahonia was bypassed in a booking, no one discovered it for 4 years, is that your definition of independent company?

Mr. DELLAPINA. Mr. Chairman, we have transacted prepaid forward physical transactions with Enron and Mahonia since 1992, and there was a discovery made that in one transaction there was inappropriate communication to the pipeline which didn't specify exactly how the volumes were flowing.

With SPVs, we are not suggesting that this SPV had a vast operation and that it was designed to get into a vastly detailed commercial activity. The SPV was designed in the structured transaction or served the role in the structured transaction to create legal independence among contracts.

Senator LEVIN. You said "legal independence." Are you distinguished that from actual independence?

Mr. DELLAPINA. I don't know the definition of "actual independence." The history——

Senator LEVIN. Real.

Mr. DELLAPINA [continuing]. Of the transactions——

Senator LEVIN. Real-world independence.

Mr. DELLAPINA. Legal independence.

Senator LEVIN. Does that distinguish from real-world independence?

Mr. DELLAPINA. I don't know the answer to that.

Senator LEVIN. OK.

Mr. DELLAPINA. We began these transactions in 1992 for the reasons we described, that is, Chase's—the lack of clarity as to our ability to take physical oil and gas back in 1992. The purpose of Mahonia at that point was to enable that physical delivery, and throughout the period in which we've been involved with Mahonia, we've always recognized it as a legally independent entity.

Senator LEVIN. Which didn't have a vast operation, in your words, right?

Mr. DELLAPINA. No, it did not.

Senator LEVIN. As a matter of fact, it was a shell. It was created by Chase, wasn't it, solely for your transactions? That is its registration statement. Is that correct? I went through the registration statement with you. That is the purpose of Mahonia, to assist you in transactions. There is no operations, except to assist you.

Mr. DELLAPINA. That is correct. They work on structured transactions with us. That is correct.

Senator LEVIN. All right. So when you say they didn't have vast operations, don't try to sell us on the concept that they were anything other than a shell corporation created by you to assist Chase, run by your agent, Mourant—who you paid, whose fees, Mahonia's fees you paid, and you are going to try to leave it with this Subcommittee that in your judgment you honestly believe that this Mahonia was not under the effective control of Chase? Is that your testimony, Mr. Dellapina?

Mr. DELLAPINA. To the best of my knowledge, when I worked on these transactions I did not understand that we controlled this company. We did not own it, and we did not enter into documentation on their behalf.

Senator LEVIN. You were aware of the fact that it was created to assist Chase, was owned by a trust, which was in turn owned by your agent, was created for you, you paid all of its registration fees, you paid all of its administrative fees, you paid its legal fees.

And are you telling this Subcommittee that in your honest judgment Chase did not effectively control Mahonia?

Mr. DELLAPINA. Mr. Chairman, I am not sure that I have the legal knowledge to define——

Senator LEVIN. I am just asking you for your honest judgment. I am not asking you for a legal opinion. I am asking you from what you know.

Mr. DELLAPINA. I understand—I think I understand the question. And I will again say that we—I fully recognize that this is an SPV that was working on these transactions for a purpose. Originally it was to accommodate the physical transfer of oil, which the bank at that time did not do. And continuing throughout the evolution of these transactions, which occurred over 10 years and changed form over time, the transaction—the company was recognized independently as a legal entity.

Senator LEVIN. I am going to go back to my question, because you say you understand it.

Mr. DELLAPINA. I did understand the question——

Senator LEVIN. I am asking you for your honest judgment. Did Chase effectively control Mahonia?

Mr. DELLAPINA. I don't believe that we controlled Mahonia.

Senator LEVIN. Mr. McCree, do you want Chase to stand by that answer?

Mr. MCCREE. Yes.

Senator LEVIN. In your judgment, Mr. McCree, do you believe that Chase did not effectively control Mahonia, given all the facts we have laid out here—it was created for you, owned and operated by your agent, you paid all of its fees, you paid its legal fees, you don't know of any example where it did anything for any other company from Chase, and you want as a representative of Chase to tell this Subcommittee that in your honest judgment Chase did not effectively control Mahonia?

Mr. MCCREE. My understanding, Mr. Chairman, is that Mahonia was controlled by a charitable trust, which was governed by a board of directors which made independent decisions on the individual transactions that were forwarded to them for consideration.

Senator LEVIN. Are you aware of the fact that Mahonia was owned by your agent, operated by your agent, that Chase paid all of its legal fees, registration fees, and administrative fees, and that there was no—its sole purpose for coming into existence was to assist Chase? Are you aware of all those facts?

Mr. MCCREE. My understanding is it was owned by a charitable trust, not by our agent.

Senator LEVIN. Who owns the charitable trust?

Mr. MCCREE. I don't know the answer to that.

Senator LEVIN. Well, we went through the letter.

Mr. MCCREE. I'm not sure who owns the charitable trust. I believe a charitable that was established, but I'm not—I am not fluent in the entirety of the legal structure of the ownership structure of Mahonia—or the charitable trust, sorry.

Senator LEVIN. Well, do you want to read your agent's letter again? April 24, first letter in Exhibit 118,[1] page 2. You see, when

[1] Exhibit No. 118 appears in the Appendix on page 394.

you use offshore jurisdictions this way, it is kind of hard for us to subpoena them, by the way. But let's read what they say. This is 1986. Page 1 of the letter, it says, "Our clients, Chase." Here's page 2. "For obvious reasons, it is important that the SPVs are controlled by Chase." He's lying? Is your lawyer lying?

Mr. MCCREE. Well, I don't—this is a 1986 letter.

Senator LEVIN. Which created Mahonia.

Mr. MCCREE. Did it create Mahonia?

Senator LEVIN. Led to it.

Mr. MCCREE. I do not know——

Senator LEVIN. Well, let's just keep reading it. "For obvious reasons, it is important that the SPVs are controlled by Chase." Was it important that the SPVs be controlled by Chase?

Mr. MCCREE. I have no idea what SPVs——

Senator LEVIN. Is it important that the SPVs that you used, that they created, are controlled by you?

Mr. MCCREE. No, I don't believe so, but I don't know the specifics of this individual transaction. I really have no knowledge of a 1986 transaction.

Senator LEVIN. Well, we are going to have to get the answer from Chase then. If you don't know the answers to this, we are going to need to get the answer. And if we have to get your president here to do it, we are going to get it, because this is shameful. This is shameful that you are not owning up to something that your lawyer did in 1986 on your behalf, creating an entity on your behalf, saying here, "For obvious reasons, it's important the SPVs are controlled by Chase. But for accounting and other requirements, it's not desirable that they be wholly owned by Chase. Accordingly"—what does your lawyer, your agent say? "Chase is considering establishing a charitable trust which would own all the shares of the holding company, which in turn would wholly own the various SPVs."

Did Chase establish a charitable trust? Yes or no.

Mr. MCCREE. I just—Mr. Chairman, I do not know the entirety of the context of this letter, the time frame, or anything. So I feel uncomfortable describing what was being described in this letter. I don't know the answer to that.

Senator LEVIN. We thought you would be prepared to answer questions here for Chase today, and I guess you are not.

Mr. MCCREE. Not this one. I apologize.

Senator LEVIN. This goes to the heart of the matter here. This goes to the heart of a deception as to whether Mahonia was an independent entity. Because if it is not, it is a loan. Everyone acknowledges that. If Mahonia is not independent, it is a loan. It has got to meet three other criteria, too, which we haven't gotten to. But this isn't just a question.

Mr. MCCREE. I would say I would be happy—or we would be happy to provide additional information on this matter. I don't have the full context. My understanding is Mahonia is an independent entity.

Senator LEVIN. Yes. Well——

Mr. MCCREE. And I apologize for that.

Senator LEVIN. When we sent Chase a letter, we expected that they would send somebody that could answer questions about control.

All right. Keep going now. "It is not desirable that they be wholly owned by Chase. Accordingly, Chase is considering establishing a charitable trust"—you don't know if they did or not, right?

Mr. MCCREE. I have no idea.

Senator LEVIN. ". . . which would own all the shares of the holding company which in turn would wholly own the various SPVs."

It is a shell, and it is a shell game, and Chase should own up to it, be honest about it, and it is not. And this Subcommittee is going to get the answers from Chase to that question. Who do you suggest we call here as a witness who can answer the question?

Mr. MCCREE. I don't know. I will have to find out who was involved in the transactions at the time.

Senator LEVIN. Turn, if you would, to Exhibit 131.[1] Now, Exhibit 131 is a diagram that was sent to you by email by an Enron employee, and I believe it is addressed to you, Mr. Dellapina. This diagram works on the details of the prepay transactions, and it was sent to you less than 2 days before the $350 million prepay between Chase, Mahonia, and Enron was signed. The diagram shows all three legs of the transaction, the expected price, and the general terms of the arrangements between the three parties. That is on page 2. Do you follow me so far?

Mr. DELLAPINA. Yes.

Senator LEVIN. So these trades were developed as a package deal, is that true?

Mr. DELLAPINA. Yes.

Senator LEVIN. Now, in these transactions, the contract between Mahonia and Enron and the contract between Mahonia and Chase were identical in terms of volumes and delivery dates, and the financial terms were only slightly different to reflect the fees that Mahonia would receive for participating as a party in the transaction. Is that correct?

Mr. DELLAPINA. I believe that's correct.

Senator LEVIN. So Mahonia essentially received a fee for participating in these transactions. Is that correct?

Mr. DELLAPINA. That is correct.

Senator LEVIN. But one of the four criteria for a legitimate prepay was not met here by your own testimony, because there cannot be this kind of linkage. They are all part of—this was a package deal. You have just testified to us under oath.

Mr. DELLAPINA. Mr. Chairman.

Senator LEVIN. Yes.

Mr. DELLAPINA. I am not familiar with the four criteria for a prepay.

Senator LEVIN. They have been testified——

Mr. DELLAPINA. I saw this earlier, and I was—I don't believe that I was ever asked to review that. That would have been out of my scope, and I'm not familiar with——

Senator LEVIN. According to the testimony this morning, for there to be a legitimate prepay you need a number of things. One

[1] Exhibit No. 131 appears in the Appendix on page 436.

of them has got to be independent parties which are not involved in a package deal transaction which is linked together.

When you look at the diagram that was showing the last prepay, it was signed in 2001. All the transactions are financially settled. All the legs use the same amount of gas, pegged to the exact same price. All of the payments are fixed. The same amount of funds go in and out of Mahonia and into Enron. The only difference is that Chase picks up an extra $6 million, and now there is risk that one party may not pay, but that is true in any loan. That is not price risk.

Is there any price risk in this transaction, Mr. Dellapina?

Mr. DELLAPINA. The price risk in this transaction initiates with the transaction between Enron and Mahonia, and then the transaction between Mahonia and Chase. That price risk is being hedged with a swap between Enron and Chase.

Senator LEVIN. So there is no price risk at the end of the game when you put it all together; is that not correct?

Mr. DELLAPINA. Provided that all parties, in fact, perform on the contracts, there is no speculative price risk, the price risk materializes in the form of a pretty large counterparty credit exposure.

Senator LEVIN. But there is a credit risk. So there is a credit risk here, but not a price risk. Is that correct?

Mr. DELLAPINA. The price risk will only materialize if the credit—the counterpart does not perform.

Senator LEVIN. Why don't we just get a straight answer to this question? In other words, there is a credit risk here, but not a price risk; is that not correct?

Mr. DELLAPINA. There is a credit risk.

Senator LEVIN. You are not willing to say there was no price risk. Even though every party was perfectly hedged and guaranteed here, you are not willing to answer the question was there a price risk before this Subcommittee?

Mr. DELLAPINA. There was not a speculative price risk in the transaction. There was not when the transaction was concluded. We certainly look at prices, and the movement in prices will, in fact, affect our credit exposure.

Senator LEVIN. Mr. McCree, do you want to comment on that? Do you agree with that? Was there a price risk here?

Mr. MCCREE. There's certainly a credit risk. The magnitude of the credit risk moves in a scenario that we have to now based on market prices, I believe.

Senator LEVIN. Try my question. Was there a price risk here?

Mr. MCCREE. Not at the outset of the transaction. There was, but it was hedged.

Senator LEVIN. Now, in Exhibit 138—and, by the way, price risk is another criteria which has been testified to as absolutely essential for there to be a legitimate transaction here. It would not count as debt.

Let me point you to Exhibit 138.[1] This is Chase's own description of one of these transactions, and it comes right out and it clearly states the objective. It is in the middle of—let me see if I can get you the right page here. It is right under that—see the black bar?

[1] Exhibit No. 138 appears in the Appendix on page 476.

"The transaction calls for Chase to advance funds to a special purpose corporation formed by Chase in the Channel Islands, Mahonia, Limited." Does that sound familiar? Do you agree at least that you formed Mahonia? Mr. McCree, did you form Mahonia?

Mr. MCCREE. I think we asked Mourant & Co. to consider forming Mahonia.

Senator LEVIN. I see. To consider forming Mahonia, not even to form it. This is your document.

Mr. TRABAND. I think the language used in this document is loose and inaccurate.

Senator LEVIN. That is a problem with a lot of Chase documents. Let me tell you, that is exactly the problem. So your document here, which says that this special purpose corporation which was formed by Chase in the Channel Islands, Mahonia Limited, that is not true; is that what you are saying? This isn't 1986, folks.

Mr. TRABAND. I think what we would say is——

Senator LEVIN. This is 1996.

Mr. MCCREE. Mr. Chairman, I think what we would say is Chase arranged for the establishment of Mahonia.

Senator LEVIN. I see.

Mr. MCCREE. But once it was established, it was controlled by its board of directors——

Senator LEVIN. Which were controlled by your agent.

Mr. MCCREE. No, by its board of directors. And we believe it was all done in accordance with law.

Senator LEVIN. So this is not an accurate statement in this Chase document. Is that the bottom line? You didn't form it?

Mr. MCCREE. We arranged for the formation——

Senator LEVIN. You just caused it to be formed.

Mr. MCCREE. We arranged for the——

Senator LEVIN. You arranged for it to be formed, but you are not willing to say you—that this is formed by you. You just paid somebody else to form it.

Mr. MCCREE. Correct.

Senator LEVIN. So if I go and tell somebody, hey, I am building a new house, you are just saying literally that means I have got to go out and build it myself rather than paying to build it; is that correct? That is the way you use language at Chase?

Mr. MCCREE. No. I think it's—I think——

Senator LEVIN. Come on, you formed Mahonia. That is the common-sense version. You formed it. You paid for it to be formed. You caused it to be formed. You formed it. You created it. You brought it into existence.

Mr. MCCREE. We asked our attorney and Mourant & Co. to establish a special purpose entity for the——

Senator LEVIN. And they did it.

Mr. MCCREE [continuing]. Purpose of doing this—yes.

Senator LEVIN. And they did what you paid them to do, didn't they? Right?

Mr. MCCREE. Yes.

Senator LEVIN. OK. Let's keep going beyond that. "Mahonia in turn enters into a forward gas sales contract, referred to as a prepay, with an Enron subsidiary, Enron Natural Gas Marketing. An integral part of the prepay is the execution of a series of commodity

and interest rate swaps which result in a known cash flow stream." "Known cash flow stream." That is a pretty good definition of eliminating price risk, wouldn't you say, steady repayment of funds? Mr. Dellapina.

Mr. DELLAPINA. Yes, we were trying to eliminate price risk.

Senator LEVIN. Mr. Dellapina, isn't it the case when you look at these so-called prepays that they are nothing more than a big circle designed to get Chase loans to Enron and back to Chase? Just a circle, isn't that true?

Mr. DELLAPINA. Mr. Chairman, these transactions were started in 1992, the form of which changed over the ensuing 11 years or so that the transactions were being done with Enron. There were elements of the transaction that were designed to mitigate price risk. Towards the end of the transactions, there were elements of it that were designed to also mitigate the physical delivery risk. But there are structural differences which we believe make these fundamentally different than loans. And if you have a moment, I'd like to go through the differences with you.

Senator LEVIN. Well, why don't we just address my questions, if you would.

Mr. DELLAPINA. Excuse me, Mr. Chairman?

Senator LEVIN. I would rather you just respond to my questions, if you would. I want to talk to you about the way you characterized the last prepay, the $350 million prepay. Wasn't that characterized as a circular deal, Mr. Traband?

Mr. TRABAND. Characterized as a circular deal?

Senator LEVIN. One that went in a circle.

Mr. TRABAND. Well, I mean, my understanding is that——

Senator LEVIN. Like that triangle you just saw there.

Mr. TRABAND. My understanding is that there was a prepaid swap and a separate commodity swap.

Senator LEVIN. Would you call that a circular deal?

Mr. TRABAND. I don't know if I'd call that a circular deal.

Senator LEVIN. You did. Do you want to hear yourself, a telephone conversation that Chase recorded?

Mr. TRABAND. I have no doubt to question you there.

Senator LEVIN. You described it as a circular deal. What did you mean by that?

Mr. TRABAND. I don't recall.

Senator LEVIN. You don't recall what you meant, 2001, September——

Mr. TRABAND. I'm sure I was addressing the fact that we were trying to mitigate our price risk.

Senator LEVIN. Let's listen to the tape, Exhibit 184(a),[1] so you can follow it. This is Mr. Ballentine. Can we start over? Is it possible? The first voice we think is Mr. Ballentine who is saying, "Jeff, why do they want to hedge with gas where it is now?" Then Mr. Dellapina, then Mr. Traband.

[Audio tape played.]

Senator LEVIN. Did you hear that, "it's amortizing debt"? Did you hear Mr. Ballentine say that?

Mr. TRABAND. I heard him say that.

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[1] Exhibit No. 184(a) appears in the Appendix on page 665.

Senator LEVIN. Is that accurate?

Mr. TRABAND. I think he was using the term "debt" interchangeably with the term "credit"?

Senator LEVIN. He was using the term "debt" interchangeably with the term "credit."

Mr. TRABAND. There was credit risk in the transaction that would be apparent in a debt transaction as well, they have common characteristics.

Senator LEVIN. OK. What do you mean by "back-to-back swap"? That term is used, "back-to-back swap." What does that mean?

Mr. TRABAND. I think we were referring to the fact that we were entering into the prepaid swap and the subsequent commodity swap to hedge the price risk.

Senator LEVIN. What did you mean when you said this is a circular deal that goes right back to them?

Mr. TRABAND. I think we were reflecting that this is a structured financing.

Senator LEVIN. Is that a term you use a lot, "circular deal"?

Mr. TRABAND. I don't believe so.

Senator LEVIN. Let me just conclude with a couple questions here. First, Mr. Traband, Mr. Dellapina, who are the people at Enron whom you dealt with on the prepays? Let me start with you, Mr. Dellapina.

Mr. DELLAPINA. The principal individual I dealt with was Joseph Deffner.

Senator LEVIN. The one who we talked about before?

Mr. DELLAPINA. Yes.

Senator LEVIN. And who else?

Mr. DELLAPINA. The only other individuals I would have dealt with would have worked for Joseph, and their names, I believe, were Lisa Bills and Michael Garberding. Those are the two names I recall.

Senator LEVIN. Mr. Traband, who did you work with at Enron on the prepays?

Mr. TRABAND. On the actual prepay transactions, I worked with Joe Deffner and Lisa Bills and had reason to discuss the prepays with others.

Senator LEVIN. OK. One exhibit I want you to look at, we haven't looked at it yet but it has been referred to this morning is Exhibit 131.[1]

Before you look at that, have any of you ever spoken with Jeff McMahon at Enron? Mr. Dellapina.

Mr. DELLAPINA. I have not spoken directly to Jeff McMahon.

Senator LEVIN. Mr. Traband.

Mr. TRABAND. Yes, I had occasion to speak with Jeff McMahon.

Senator LEVIN. On prepays?

Mr. TRABAND. Generally, yes.

Senator LEVIN. On prepays?

Mr. TRABAND. Yes.

Senator LEVIN. Mr. McCree.

Mr. MCCREE. No.

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[1] Exhibit No. 131 appears in the Appendix on page 436.

Senator LEVIN. Now, on Exhibit 131, this is an October 2001 exchange of emails at Chase, and here is one person—when the bank is learning that, to its surprise, Enron had $5 billion in prepays outstanding, an amount which was greater than Chase even had expected. And here's the conversation: One employee of Chase says, "$5 billion in prepays!" The other one says, "Shut up and delete this email."

Any of you involved in this conversation? Mr. McCree.

Mr. MCCREE. No.

Senator LEVIN. Are you familiar with it?

Mr. MCCREE. No, not to my knowledge.

Senator LEVIN. Mr. Traband, are you familiar with it?

Mr. TRABAND. I was not part of this conversation. I've subsequently seen the email.

Senator LEVIN. You have seen the email?

Mr. TRABAND. Just in preparation for this meeting.

Senator LEVIN. It was not deleted.

Mr. TRABAND. I'm sorry?

Senator LEVIN. Was the email not deleted?

Mr. TRABAND. We are all aware that our email does not get deleted. It's archived for a period of time.

Senator LEVIN. I gave you the wrong exhibit number. It is Exhibit 132.[1]

OK. Mr. Dellapina, do you know who participated in this conversation?

Mr. DELLAPINA. I'm just turning to this now. I am not familiar with that.

Senator LEVIN. Here we have got one Chase employee telling the other to shut up and delete the email. Does that trouble you, Mr. McCree? Are you embarrassed by that?

Mr. MCCREE. Yes. But I'm not sure what it means.

Senator LEVIN. It means delete the email.

Mr. MCCREE. No, I know. But it's—I don't know the context, but yes.

Mr. TRABAND. If I could just say something?

Senator LEVIN. Yes.

Mr. TRABAND. We are all aware that our emails are archived for a period of time and that it's not possible to delete an email. So I think that was said in jest and not meant to be taken seriously.

Senator LEVIN. Mr. McCree, let me just ask you the final question. You represent one of the most important financial institutions in the country, and you have a reputation to maintain. Yet you use entities and secrecy jurisdictions, arguing that you don't control them, when I think it is obvious to any reasonable person looking at this that you created it and you control it. You maintain the fiction here that you don't control it, ignoring all of the evidence, producing none, by the way, to counter it other than the fact that your understanding is that it is independent. But I went through all of the control mechanisms, all of the indicators of control, so you maintain that you don't effectively know Mahonia even though it was created for you, run by your agent, paid for by you.

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[1] Exhibit No. 132 appears in the Appendix on page 438.

You then helped to create a situation here where you have got prepays that, according to the experts that we have had, do not meet the criteria for prepays. They are linked transactions, for one thing. The parties are not independent, at least if you can accept all of the evidence that says Mahonia is really controlled by Chase, and they are treated as loans. There are many indicators we have that they are treated as loans.

So you are now, as Chase, participating in this entire picture where billions of dollars of cash coming into Enron, which should have been treated as loans, if it had been treated as loans, would have affected their credit rating and a lot fewer people would have been stung by Enron. And they produce documents which are misleading, documents which bury it. Your own employees says Enron loves these kinds of transactions because they can hide debt and they can bury it.

Is Chase at all troubled by this? Do you find this troubling at all? I don't mean the fact that you are here. I hope you find that troubling.

Mr. MCCREE. Yes.

Senator LEVIN. But I mean the fact—are these facts at all troubling to Chase?

Mr. MCCREE. Let me answer it this way: In establishing the transactions with Mahonia, we believed that we were in compliance with all relevant laws, all accounting standards, all tax standards. We had no reason to believe then that we were not, and we have no reason to believe now that we are not.

We also believed that Enron at the time was in compliance, and particularly with its accounting regulations, and was reflecting these transactions in accordance with GAAP on their balance sheet.

I find it personally troubling and hard to understand in terms of Chase doing something wrong here how that would jibe with the financial loss that we suffered as a firm in the entirety of the Enron transactions and, frankly, in many of these prepay transactions. So as to the difference between a loan and a prepaid contract, aside from whether the accounting was appropriate at the time or not, we suffered multiple legs of loss due to the structure of these transactions, some on the commodity risk, some on delivery risk, and we are in litigation on some with the sureties.

We do find it troubling. We find what is happening in the financial system in general troubling right now. I'll echo what a few people said up here earlier. We applaud the efforts that the Congress is going about in terms of reform and transparency of the financial accounting system and financial system in general. We believe we have as high an interest as a major principal lender across corporate America in this transparency.

As it relates to JPMorgan, we have significantly increased our attention to diligence, to probing questions around our clients' financial statements, to purpose of transactions, and we are rethinking the way we conduct business on a going-forward basis in the new environment that we operate in today.

Senator LEVIN. Well, you have plenty of reason to believe that your company controls Mahonia. You were given reason to believe today. Would you agree with that, that you now have reason to believe that your company controls Mahonia?

Mr. MCCREE. I continue to repeat what I said before——
Senator LEVIN. Yes, I know that, but——
Mr. MCCREE [continuing]. Which is I——
Senator LEVIN. But you heard reasons here today that are reasons to believe that Chase controls Mahonia.
Mr. MCCREE. I believe Mahonia was controlled by its board of directors. They made the decisions.
Senator LEVIN. You didn't hear anything today which gives you any reason to believe that Chase controlled Mahonia?
Mr. MCCREE. No.
Senator LEVIN. OK. Well, let me tell you, both the board of directors of Mahonia—we think all the board of directors of Mahonia work for your agent. They are all working for that law firm. You can try to avoid it, but you can't. Responsibility comes right back to you. You can sit here repeating that you believed it was independent despite overwhelming evidence that you control it. You use an offshore jurisdiction in a secrecy jurisdiction. The evidence that we were able to obtain nonetheless dramatically demonstrates that Mahonia was created for Chase, created by Chase, paid for by Chase, controlled by Chase, run by Chase's agents, fees paid for by Chase, and yet you sit here and just repeat the mantra that you believe it was independent. That does not satisfy the responsibility of a major bank. You have got a greater responsibility than to do that. And I must tell you that I think that this is just one example of why the American people have lost confidence in Wall Street, that we have a bank that is participating in Enron's effort, known to the bank—we have those emails—to turn debt into operating income. Your people knew that. That is in those emails. They knew that this is what Enron was up to. They love to do it. They love to hide it. And to just sit here and to try to tell this Subcommittee that you believe Mahonia is independent and you believe that this transaction was not, in fact, a phony prepay, even though, by the way, your own testimony here today indicates quite clearly that these transactions were linked, those three legs were linked together, you acknowledge that here today, which by expert testimony means it was not, in fact, a transaction which could qualify as a legitimate prepay.

We are going to have to hear from folks at Citibank to answer questions that you could not answer or would not answer here today, but your testimony today here just seems to me is part of a picture which I find mighty disturbing. I would like to see that picture change. I hope we are going to do our share here in Congress in a constructive and positive way. But it is going to take some recognition on the part of our financial institutions that things have got to change. You can't have people writing emails back and forth to each other saying, hey, these kind of transactions are just what Enron loves, they can hide debt, and just ignore it as though that is not going on inside of your own bank.

So we will ask your folks to answer the questions that you could not or would not answer relative to the control of Mahonia. We will refer all of this testimony and the exhibits to this Securities and Exchange Commission and to the Department of Justice. And I will call upon Senator Fitzgerald in case he has questions of this panel.
Senator FITZGERALD. Thank you, Mr. Chairman.

I just wanted to go back and be very clear in my own mind about the extent of JPMorgan Chase's understanding of the nature of the prepay transactions.

Now, as I understand it, JPMorgan is trying to force certain insurers to pay an obligation pursuant to surety bonds that were backing Enron's performance on some of these prepays. Is that correct, Mr. Dellapina?

Mr. DELLAPINA. Yes, Senator, several of the prepay transactions that were done beginning in 1998 had a credit diversification benefit to those transactions which were surety bonds from major insurance companies in the United States. Those insurance bonds, those insurance companies worked with Enron and came to us and asked us to participate in the transactions——

Senator FITZGERALD. So Enron got those insurance companies to offer the surety bonds. It wasn't JPMorgan Chase that went out and got the insurance policies?

Mr. DELLAPINA. That is correct, Senator.

Senator FITZGERALD. OK. Now, you are suing certain insurers asking them to perform under their surety bonds. That is correct? Do you know the names of the insurers that you are suing?

Mr. DELLAPINA. I know several of the names, sir.

Senator FITZGERALD. Can you give us a few of those? It is in a public record——

Mr. DELLAPINA. The Traveler's Insurance Company, Chubb, St. Paul.

Senator FITZGERALD. Traveler's is owned by—who are they owned by?

Mr. DELLAPINA. I believe Citigroup.

Senator FITZGERALD. OK. That will be interesting. This is very—a lot of connections here. So you are suing Traveler's, Chubb, and other insurers, asking them to pay.

Now, according to published reports, the insurance companies are saying we are not going to pay because these weren't real prepay transactions, these were just loans. Is that correct that that is the defense of the—in essence, that is the defense of the insurance companies?

Mr. DELLAPINA. Senator, I am not familiar with all of the defenses raised by the insurance companies. I disagree with that characterization that they're loans, if that's, in fact, what they're making as a characterization.

Senator FITZGERALD. My understanding from published reports is that they are saying these aren't—these were just loans and that they were misled. For the record, I guess the case is styled JPMorgan Chase Bank v. Liberty Mutual Insurance Company, Traveler's, St. Paul, Continental Casualty, National Fire Insurance Company of Hartford, Firemen's Fund, Safeco, another Traveler's indemnity company, Federal Insurance Company, Hartford Fire Insurance Company, and Lumbermen's. Those are the defendants.

My understanding is that those insurance companies are maintaining that this was just a loan and that they were misled on the nature of the transaction. Your position is they weren't loans. Is that correct?

Mr. DELLAPINA. I'd prefer not to speak in context of that outstanding litigation, but if you are asking me with respect to the

prepays outside of the litigation and not taking into account what their defense might be, I do believe that the characteristics of these transactions are fundamentally different from a loan and have different risks associated with them.

Senator FITZGERALD. So your personal opinion is that these are different than loans, but earlier Senator Levin produced Exhibit 123,[1] which was an email to Karen Simon that was cc'd to you, Jeffrey W. Dellapina, on 11/25/98, and this is the email. Is it written by George Serice? George Serice I believe wrote this. That is where it was said that "Enron loves these deals." He is talking about prepays. He says, "Jeff is also working on another prepay for Enron now." That is you, I presume. He said, "Enron loves these deals as they are able to hide funded debt from their equity analyst."

Well, it would seem to me that whoever wrote this email knew that these prepays were a way of hiding what was essentially a loan, doesn't it?

Mr. DELLAPINA. Senator, as I mentioned to the Chairman, I do not believe that that email is accurate, and prepaid forwards are, in fact, a form of financing, but not all forms of financing are loans. I'm not an accountant, but I believe there are very different characteristics of the prepaid forward transaction and the loan. Some of those characteristics are as follows: This is a commercial contract between a buyer and seller that is not satisfied in dollars. It is satisfied in goods and/or services. With the prepaid forward, the final market value of this contract and the actual goods that are being delivered will only be known at the delivery, and as opposed to a loan where it is a set dollar amount that is going to be paid at maturity.

There are very—there are probably three or four additional risks in prepaid forward transactions that are not present in a loan and that, regrettably, have caused us to suffer additional losses in these transactions, losses that are incremental to any losses we would have suffered if it was just a loan.

Those risks are commodity price risks, account receivable collection risk, and these transactions, through the first 5 or 6 years of these transactions, the physical commodities were delivered into the market. Over the last several years, the physical commodities and the natural gas was actually delivered to Enron. That was not an essential part of the transaction and was not part of the transaction for the first 6 years. The decision to sell the commodity to Enron, which has been characterized as a circle, actually introduced an entirely new credit risk for us. We could have sold that gas, as we had in the past, prior to the time I was there, to other market participants, and we would have taken the risks that those participants would have paid for that commodity.

When Enron bought the natural gas in the latter transactions, we assumed an entirely new credit risk. And to summarize that, when Enron went bankrupt, they owed us an additional $32 to $35 million for natural gas that had been delivered to them, and they did not pay that.

Senator FITZGERALD. How much does Enron owe you now?

Mr. MCCREE. In total?

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[1] Exhibit No. 123 appears in the Appendix on page 414.

Senator FITZGERALD. Yes.

Mr. MCCREE. I'm not sure. Right now, as of——

Senator FITZGERALD. As of the bankruptcy——

Mr. MCCREE. December 19, which is when we announced, I think. Have to look at my notes—$2.6 billion.

Senator FITZGERALD. $2.6 billion? At about the time of their bankruptcy, and that's when you last calculated it?

Mr. MCCREE. I'm not sure. I just haven't seen the figure lately.

Senator FITZGERALD. Now, would you know, Mr. McCree, how much they owed you back in, say, May 2001?

Mr. MCCREE. No, but Mr. Traband may.

Mr. TRABAND. I don't recall specifically how much they owed us, but it, I would imagine was, something greater than $2 billion.

Senator FITZGERALD. Over $2 billion in May 2001

Mr. MCCREE. In the latter—I don't know the question, but we actually increased our credit exposure in a number of different ways through the fall of 2001, prior to the bankruptcy.

Senator FITZGERALD. Can you give me in rough terms—it started apparently in 1992, Mr. Dellapina was saying, with this structured financing. Was that when your relationship with Enron started?

Mr. DELLAPINA. I do not believe any of us were involved with Enron in 1992. I do not believe it was the only transaction or the only relationship with Enron back then.

Senator FITZGERALD. But in rough terms would you know how much was owed to JPMorgan back in 1997, 1998, 1999, 2000, or 2001?

Mr. MCCREE. No, but we can certainly provide that information. We would be happy to do that.

Senator FITZGERALD. If you could provide that later, we would appreciate that.

Now, I want to call your attention to—I don't know if this is an exhibit. This is an analyst report by Anatol Feygin, dated May 18, 2001. The headline is: "Enron Corp, Enron Weakness Not Explainable Fundamentally."

In this report, your firm, J.P. Morgan Securities, Inc.—and I guess that is your company, Mr. McCree—via its analyst, Anatol Feygin, is rating Enron as a buy and setting a 12-month price target at $120 a share, even though Enron was then trading at $52.20. I am wondering how much exposure specifically you had to Enron at the time this report was put out, and so I would ask if for the record, Mr. McCree, you could provide exactly how much indebtedness was owed your company.

One of the concerns I have is that analysts do not always have to disclose to the people that they are offering their research reports to the full gamut of potential conflicts that they have, and in the case of Enron owing large amounts of money, over $2 billion, to JPMorgan Chase, I am concerned whether that would have influenced in any way the research reports.

Now, Mr. Feygin testified before this Subcommittee in February about his coverage of the Enron Corporation and explained why he made the recommendations that he did. Do you think that this potential liability of your firm to the fortunes of Enron would have had any impact at all on the ratings that Mr. Feygin or other JPMorgan analysts would give to Enron?

Mr. MCCREE. No. I believe we have very stringent and very thorough Chinese Wall policies which would segregate any public research professional from any kind of relationship material, size of exposure whatsoever that we would have on the banking side of the firm. And we, as a general matter, lend material amounts of money to virtually all of the Fortune 1,000 companies and we hold our responsibilities around confidentiality and wall issues very, very seriously.

Senator FITZGERALD. Do you believe Mr. Feygin would have known that Enron owed your firm over $2 billion?

Mr. MCCREE. I don't know how he would know that.

Senator FITZGERALD. Because that is done over on the bank side; is that correct, the loans or the prepay transactions were done over there on the bank side and you are over at J.P. Morgan Securities? You say you have a firewall there.

Do either of the other of you want to comment on that issue as to whether Mr. Feygin could have been in any way influenced by the debt owed to your bank by Enron?

Mr. TRABAND. I'm not aware of how Anatol could have been aware of our exposure. I would—I certainly never had any conversation with him about that, and would not have had any.

Senator FITZGERALD. Do you know Anatol?

Mr. TRABAND. Only by reputation.

Senator FITZGERALD. Have you ever talked to him?

Mr. TRABAND. I requested information from him once, and the firewalls work that public information can be shared to private, but private cannot go to public.

Senator FITZGERALD. Did you ever have any conversations with him about Enron?

Mr. TRABAND. Not that I recall.

Senator FITZGERALD. Mr. Dellapina, did you ever have any——

Mr. DELLAPINA. I have never met Anatol and have never spoken with him to the best of my knowledge.

Senator FITZGERALD. You don't know him?

Mr. DELLAPINA. I don't.

Senator FITZGERALD. Mr. McCree.

Mr. MCCREE. Never met him.

Senator FITZGERALD. You have never met him, even though he works within J.P. Morgan Securities, so you never talked to him.

Well, with that, Mr. Chairman, let me ask one final question. All of the approximately $2.6 billion now owed to JPMorgan Chase, how much of that is covered by surety bonds, and they may be disputed whether the surety bonds are good, but assuming they are good, how much of that is covered by surety bonds?

Mr. DELLAPINA. I believe that the amount is slightly over $900 million.

Senator FITZGERALD. So even if you could collect on the surety bonds, you would be out approximately another $1.6 or $1.7 billion; is that correct?

Mr. TRABAND. Our total exposure at the time of the bankruptcy was $2.6 billion. Not all of that was unsecured exposure to Enron.

Senator FITZGERALD. How much of it was secured?

Mr. TRABAND. I think—and I am trying to recall the numbers. I think that unsecured exposure was roughly $600 or $700 million dollars.

Senator FITZGERALD. Now, are you terming the loans for which you had, or the prepaid transactions for which you had——

Mr. TRABAND. Yes.

Senator FITZGERALD. Now, it's interesting, these prepaid transactions show up basically as debt in Enron's bankruptcy filing, right, that you are just another creditor that they are going to blow out just like they would blow out somebody who had given them a straight-up loan?

Mr. TRABAND. Well, all of their creditors appear in their bankruptcy filing including accounts payable creditors.

Senator FITZGERALD. Right. But we have gone along with not calling these prepaid transactions loans. Mr. Dellapina was explaining why it is not necessarily a loan, but we see that at the end of the day when there is a bankruptcy filing the debtor is just treating you like a bank that had given it an extension of credit pursuant to a promissory note and they are going to blow you out in bankruptcy court in their reorganization or their liquidation. Of that $2.6 billion you said approximately $600 million was unsecured, the rest of it was secured. Are you describing the liability that is owed to you that is covered or potentially covered by surety bonds as secured?

Mr. TRABAND. Certainly prior to the bankruptcy we viewed it that way.

Senator FITZGERALD. OK.

Mr. TRABAND. We obviously have not successfully collected.

Senator FITZGERALD. But that is not really security. That is a credit enhancement. That is a credit guarantee. It is not the collateral.

Mr. TRABAND. Yes, that's correct. I used "secured" broadly. Credit enhanced or secured.

Senator FITZGERALD. So of the $2.6 billion, if you cannot recover from the surety bonds, you will lose $900 million and then another $600 million is unsecured. So you might have about $1.5 billion that is actually secured and you think you could get repaid on? What is your collateral for the $1.5 billion that you think is secured?

Mr. TRABAND. That varies. For example, $400 million would be related to the pipeline loans that were entered into in November prior to their bankruptcy.

Senator FITZGERALD. And you got good security for that?

Mr. TRABAND. We got good security for that. And there are other transactions. At the time of the bankruptcy we had credit exposure to their Florida Gas Transmission affiliate, which was subsidiary-level financing. It was not technically secured, but it was not to Enron Corp. So we were—the $2.6 billion is aggregate exposure to Enron and Enron-related entities.

Senator FITZGERALD. Now, is the bank carrying—what percentage of the $2.6 billion had the bank reserved for and what percentage are you carrying as nonaccrual?

Mr. MCCREE. I do not know the nonaccrual or reserve. I believe we have written off roughly $450 million of that exposure.

Senator FITZGERALD. You have written off $450 million——
Mr. MCCREE. In the fourth quarter of this year, last year.
Senator FITZGERALD. Presumably you have set aside reserves——
Mr. MCCREE. Yes. I just don't know what the number is.
Senator FITZGERALD. You do not know the number.
Mr. MCCREE. I think the general—just to finish, the general comment I would make on this is, we have the largest exposure we believe of any institution in the world to Enron. We feel as—I'll use the word—defrauded as anybody else in connection with the broad happenings at Enron. We believe that we acted in accordance with law, in accordance with GAAP, and from a reputational standpoint, which, Mr. Chairman, you referenced, that we upheld our general reputation and tried to do things as the rules were written. That is not saying the rules were right or the rules were wrong. I think as we go forward, as I said before, transparency is a fantastic development and we applaud that. I would—or we would caution about throwing the whole structured finance industry out based on the effects of what Enron did. We think that the fundamentals of structured finance, the legal basis on which structured finance is done, and the constructs supporting the industry need to have—need to be looked at, but once the rules are looked at and well articulated, they are a fundamental diversification of funding sources and a powerful tool for corporations around the world, specifically in the United States, if used responsibly.
Senator FITZGERALD. So even though you may have lost an awful lot of money by engaging as a banker for an entity that was heavily engaged in monetization transactions, you are not at all less enthusiastic to do more securitization transactions in the future?
Mr. MCCREE. I would say we are much more diligent in terms of how the transactions are put together, the extent of questions that are asked around the transactions and the underlying broad financial condition of the companies that we interact with.
Senator FITZGERALD. Do you know if any banks declined to do the transactions that you did for Enron before they came to you; are you aware of that?
Mr. MCCREE. I don't know the answer to that.
Mr. TRABAND. Don't know.
Senator FITZGERALD. OK. Mr. Chairman, I yield the floor back to you.
And thank you, gentlemen for being here. I think it took a lot of courage to come before this Subcommittee and answer our questions. Thank you.
Senator LEVIN. Well, I do not think they had a heck of a lot of choice, but nonetheless, we are glad that you were here, and structured transactions and arrangements clearly do have a purpose, Mr. McCree, if they are legitimate. And if they are illegitimate and if they are deception, they not only do not have a purpose that is acceptable, they have indeed a very deleterious and a very negative effect on people who have invested their savings and on the economy as a whole.
When you say in your final comment, Mr. McCree, that the move to transparency that is going on now is fantastic or words to that effect, the whole purpose of these prepays, as used by Enron, and in which you participated, was to hide the nature of the trans-

action. So we are glad that you testify that you welcome a move to transparency. I must tell you that is one of the things that was missing here, that it was an effort here to hide, in the words of that email, that Chase email, that were so devastating here, which caused losses, huge losses to so many people. Chase may have been stung by Enron. Apparently it was. You are going to take some losses too. But that in no way can justify any participation of Chase in the losses of others. The fact that you yourself may have lost isn't in any way going to excuse your participation in the deceptive practices that Enron perpetrated.

And that is going to be for others to judge. It is going to be for the SEC and the Department of Justice, and I guess in civil court where you are right now. You have got cases that are existing in court that are brought by a number of people, and you, yourself apparently are bringing suit on some surety arrangement. So some of those issues will be resolved elsewhere.

But we will close your panel here by thanking you for coming today. We will be calling upon people at Chase to give us the answers to those questions relative to Mahonia, and we will now stand adjourned because—excuse me one minute.

Do we have votes?

We will excuse you, and we will hold off calling our next panel until after we return, which will be perhaps as long as 20 minutes because we have two roll calls I believe back to back. Thank you.

We will recess for about 20 minutes.

[Recess.]

Senator LEVIN. The Subcommittee will come back to order, and I now would like to call our final panel of witnesses for today.

David Bushnell, the Managing Director of Global Risk Management at Citigroup; James Reilly, Jr., the Managing Director of Salomon Smith Barney, which is a member of Citigroup; Richard Caplan, the Managing Director and Co-Head of the Credit Derivatives Group at Salomon Smith Barney North American; and finally, Maureen Hendricks, Senior Advisory Director of Salomon Smith Barney. And I would ask you to please rise and raise your right hands.

Do you solemnly swear that the testimony that you will give to the Subcommittee today will be the truth, the whole truth and nothing but the truth, so help you, God?

Ms. HENDRICKS. I do.

Mr. BUSHNELL. I do.

Mr. REILLY. I do.

Mr. CAPLAN. I do.

Senator LEVIN. Thank you. We will use the same timing system as we did this morning for your statements, so please keep your oral testimony to no more than 10 minutes, but we will print any written testimony in the record in its entirety, and the red light will come on after 10 minutes, but the green will change to yellow after about 9 minutes to give you a chance to conclude your remarks.

And according to this, Mr. Reilly, you are to start I believe; is that correct?

Mr. BUSHNELL. Actually, Mr. Chairman, I am going to start.

Senator LEVIN. OK. Mr. Bushnell.

TESTIMONY OF DAVID C. BUSHNELL,[1] MANAGING DIRECTOR, GLOBAL RISK MANAGEMENT, CITIGROUP/SALOMON SMITH BARNEY, NEW YORK, NEW YORK

Mr. BUSHNELL. Good afternoon, and thank you for the opportunity to come to speak with you today.

My name is David Bushnell, and I'm a Managing Director at Citigroup's Global Corporate and Investment Bank. I am head of its Risk Management Division. That division functions as an independent control unit over our operating businesses.

Our institution recognizes the importance of the work that this Subcommittee is doing with respect to its examination of Enron's collapse. Enron's failure was a pivotal event in American business. In the space of a few short months, Enron went from an investment grade credit, ranked seventh in the Fortune 500, to bankruptcy. Like many others, Citigroup lost money as an Enron lender. More importantly, investors have lost money, employees have lost jobs, and the public has lost confidence in our financial markets.

The integrity of our markets and the integrity of our borrowers and their financial statements is of utmost importance to us. We therefore commend the Subcommittee's efforts to understand the factors that caused or permitted Enron's stunning collapse, and we encourage changes in our accounting or other rules that will protect against what happened here.

During our business relationship with Enron we thought we were dealing with honest managers who had legitimate business purposes for the transactions we did with them. We believe that Enron was making good faith accounting judgments that were reviewed by Arthur Andersen, which was then the world's premier auditing firm in its sector. We believe that the Audit Committee of Enron's board exercised meaningful supervision over the company's accounting policies and procedures.

The emerging facts suggest that Enron was not the company that we thought it was. If what has been reported out turns out to be the case, large-scale self dealing, inflated assets, management that was inattentive or worse, a subservient board, and a failure of accounting controls, we would not have done the business we did with Enron.

But let me be clear. While we regret our relationship with Enron, we acted in good faith at all times. Our employees, including the bankers who are here today, are honest people doing honest business. They did transactions that were common throughout the financial markets and they believe those transactions were entirely appropriate.

The focus of this hearing is structured finance and the accounting rules that apply to the types of structured transactions that Enron used. My colleagues will talk to you about some of the specifics, but I want to emphasize that like every other institution in the financial services industry, we design financing structures for a diverse set of clients against a background of accounting, tax, and legal rules. Some of those accounting rules are complicated and subject to interpretation by accounting experts. If specific rules do

[1] The prepared statement of Mr. Bushnell appears in the Appendix on page 316.

not work the way they should, then they should be fixed. Moreover, changes are needed to increase accounting oversight and the reliability of companies' financials.

I must stress, however, that we do not dictate our clients' accounting practices. Once we are satisfied that a client's proposed tax and accounting treatment seem reasonable, the accounting judgments are left to the client and its accounting professionals who have complete access to all of the information. And this, I would submit, is as it should be. It has always been the law and accepted practice that companies are permitted to rely on the certified financial statements of the party on the other side of the transaction. The auditors are experts in understanding the accounting rules, and the auditors are in possession of detailed information about the companies' entire financial picture.

Recent regulatory initiatives appreciate that responsibility for the accuracy of financial statements, that it must rest with the companies' management and auditors as evidenced by the recent SEC rule requiring CEOs and CFOs to certify the accuracy of their financial statements, and the legislative proposal strengthening the independence and oversight of the accounting function.

At Citigroup I oversee a comprehensive process for reviewing structured finance transactions. Our Commitment Committee is responsible for reviewing equity and fixed income securities underwritings to ensure that we are comfortable with the transactions and so that we protect our reputation for high-quality financings and retain investor confidence.

Our Capital Markets Approval Committee—you'll hear us call it CMAC here—reviews structured financing products and approves only those transactions that it concludes are appropriate. For example, the Enron—the Yosemite transactions, about which this Subcommittee has expressed interest, were reviewed and approved by our CMAC. We pride ourselves on our reputation for being an institution with integrity. If a transaction raises potential accounting, tax, legal compliance, regulatory, or appropriateness issues for us or our clients, or otherwise exposes us to reputational risk, the CMAC evaluates those risks to ensure that our institution is comfortable in completing the transaction. This is not to say that we substitute our judgment for that of our clients, or their tax, accounting or legal advisers. Responsibility for those judgments remains with them.

Thus, when we agreed to structure prepaid transactions for Enron, we relied heavily on the assurances that its outside auditor, Arthur Andersen, had reviewed these transactions. Enron told us that Andersen believed the proposed accounting treatment for the prepaids was appropriate. And while I'm not an accounting expert and no one on this panel is, the accounting treatment seemed reasonable to the members of our CMAC.

I am sure that the Subcommittee understands that at the time these transactions were done, Arthur Andersen was considered the preeminent accounting firm whose word carried weight and gave comfort. Certainly now, with all of the information that's come to light, it's easy to question Andersen's review. And indeed, the information contained in your Subcommittee's recent report on Enron's board is striking for what it reveals about Andersen's own concerns

about the risk of Enron's accounting methodologies, but we learned about these reservations only after the fact.

The sobering facts about Enron set forth in this Subcommittee's recent report make clear that much stronger oversight of the accounting profession is needed. The report also suggests that a rule-based accounting system such as American GAAP may be too susceptible to abuse. It perhaps should be supplemented by more of a principle-based system. We would also support rules requiring greater management accountability, more stringent board oversight and greater board independence. These rule changes are essential if we are going to re-establish the trust that is necessary to the efficient functioning of our economy.

Thank you, and I look forward to answering your questions.

Senator LEVIN. Thank you very much, Mr. Bushnell.

Mr. Caplan, are you next?

Mr. CAPLAN. Yes.

TESTIMONY OF RICHARD CAPLAN,[1] MANAGING DIRECTOR AND CO-HEAD, CREDIT DERIVATIVES GROUP, SALOMON SMITH BARNEY NORTH AMERICAN CREDIT/CITIGROUP, NEW YORK, NEW YORK

Mr. CAPLAN. My name is Rick Caplan. I am a Managing Director of Citigroup's Corporate and Investment Bank, and Co-Head of the North American Credit Derivatives Group, one of several groups at Citi that structure financings for sophisticated corporate clients.

A prepaid swap transaction, the transaction you have invited us to talk about today, is a form of structured finance. Structured financings have been used over the past several decades by virtually all sophisticated companies as a way of raising money. While many structured financings have the same impact as a loan, they often are treated differently for accounting purposes. There are many examples of loan-like transactions that have different accounting treatments, including financing tools that support much of this Nation's trading and fixed income securities, such as repurchase agreements or repos and reverse repos, widely-used insurance products such as guaranteed investment contracts and finite insurance, equipment trust certificates widely used in the airline industry and common project finance strategies such as synthetic leases.

As this Subcommittee is aware, Enron made extensive use of structured finance. Indeed, from 1995 through 2001 Fortune Magazine selected Enron as the most innovative company in America. And in 1999, Enron's CFO, Andrew Fastow, was awarded CFO Magazine's Excellence Award for Capital Structure Management, based on the unique financing techniques he pioneered.

For all of Enron's innovation and sophistication, the prepaid swap transactions we are discussing today, were hardly a unique financing technique. Prepaid swap transactions and similarly commodity-based financings have been widely used in the power and energy industry since the 1970's. In essence a prepaid swap contract involves an up front cash payment by one party in return for an obligation by another party to deliver a commodity for the cash

[1] The prepared statement of Mr. Caplan appears in the Appendix on page 323.

value of that commodity at some point in the future. In the prepaid engaged in by Citibank with Enron, Enron received cash up front in exchange for Enron's obligation to deliver at some point in the future a specific quantity of gas or oil or its financial equivalent.

The prepaids provided Enron with an ability to raise cash against certain long-term assets, which as we understood it, helped Enron address a disconnect between the revenue and cash flow in its trading book. Enron told Citibank that because of the way auditors, including its auditors, Arthur Andersen, accounted for prepaids, Enron could use prepaids to bring its cash flow in line with its revenues. As Enron explained, because prepaids were comprised of commodity trades, executed in Enron's trading book, Enron's financial obligations on these trades, were recorded in its trading book as a trading liability, termed price risk management liability, and the cash generated by these trades would be disclosed in its cash flow statement as cash flow from operations.

Enron assured Citibank that its accounting treatment of prepaids had been fully vetted by Arthur Andersen, which at the time was one of the Nation's leading accounting firms. The accounting position we understood Enron was taking seemed reasonable based on our understanding of the then-existing accounting rules and guidelines. I should add that Citibank did not advise Enron, nor would it advise any client as to the appropriate accounting treatment of any transaction. Some have suggested that prepaids are off-balance sheet or that the liabilities that Enron incurred as a result of these financings somehow were disguised or hidden. That simply is not true. Enron's obligations on these financings were clearly reflected as liabilities on Enron's balance sheet, and denominated as I said before, as a price risk management liability.

A price risk management liability is a liability, plain and simple, that must be satisfied every bit as much as debt. Thus, while not recorded as debt, prepaid liabilities were clearly obligations of the company, and visible as such to investors.

There also has been a suggestion that Enron somehow was able to generate extra cash flow by using prepaids instead of loans. That also is not accurate. The overall cash flow for Enron would be exactly the same whether Enron used prepaids or entered into a bank loan. In the case of prepaids, Enron booked the funds it received on these contracts in its cash flow statement as cash from operations, not as cash from financing. We understood that Arthur Andersen has fully vetted this accounting treatment as well. Another point I would like to address is the confusion that has arisen between prepaids and Credit Linked Notes. There is no necessary linkage between the two. Prepaids exist without Credit Linked Notes. Credit Linked Notes exist without prepaids.

A Credit Linked Note is simply a security through which an investor takes on the credit risk of a particular company without actually purchasing a bond issued by that company. Credit Linked Notes are well recognized financial instruments. Citi structured Enron Credit Linked Notes called Yosemite and the ECLNs. These instruments were sold to the largest and most sophisticated institutional investors in several Rule 144A offerings. As with every offering that Salomon Smith Barney brings to market, the Enron Credit Linked Notes and the underlying prepaid financings that

the notes funded were fully vetted and reviewed. The firm's stringent internal control processes are designed to safeguard Citi's reputation through careful screening of potential transactions. The Credit Linked Notes and the underlying prepaid financings were approved only after undergoing this screening process. I believe that our conduct in arranging the prepaids and in selling Enron Credit Linked Notes was entirely appropriate. We arranged these financings for what appeared at the time to be one of America's best and most admired companies. We used the financing structure that had been commonly employed in the energy and power industry for many years, and we relied on the fact that Enron's accounting treatment of these transactions was blessed by one of the Nation's leading accounting firms and seemed reasonable under the then-existing accounting rules and guidelines.

Thank you, and I look forward to answering your questions.

Senator LEVIN. Thank you, Mr. Caplan. Ms. Hendricks.

TESTIMONY OF MAUREEN HENDRICKS,[1] SENIOR ADVISORY DIRECTOR, SALOMON SMITH BARNEY/CITIGROUP, NEW YORK, NEW YORK

Ms. HENDRICKS. Thank you, Mr. Chairman, and Members of the Subcommittee. My name is Maureen Hendricks, and I am currently a Senior Advisory Director at Salomon Smith Barney. From 1999 until May 2001 I was the head of Salomon Smith Barney's Global Energy & Power Group, with the responsibility for the Enron account.

As you have heard quite often Enron was a significant user of structured finance, which is simply a way of providing cash to a company through means other than traditional bank loans. And far from being faulted for it, at the time, Enron was celebrated for its innovative financing techniques.

One project that I worked on for Enron was the Yosemite structure, which was designed as a way for Enron to do structured finance in the capital markets. As it happened, the structured financing underlying the Yosemite offerings was a prepaid. Prepaid are a commodity-base structured financings that were widely used in the energy sector. Production payments, which I structured back in the 1970's, are precursors of the prepaids at issue here today. And like prepaids, they originally had certain accounting advantages over straight loans.

At the time that we structured the Yosemite deals, I had absolutely no reason to believe that there was anything wrong with prepaids or with Enron's proposed accounting treatment for them. Indeed, it appeared very familiar. Moreover, we understood from Enron that Arthur Andersen had fully vetted the accounting treatment. In shepherding the Yosemite offering, I oversaw the due diligence that we conducted of Enron in close cooperation with our outside counsel. I believe that we asked the company to answer questions. I regret to say that it appears from all that has recently been disclosed that we were not provided with the right answers by Enron management. It also appears that the audited financial statements upon which we relied were not accurate and did not

[1] The prepared statement of Ms. Hendricks appears in the Appendix on page 330.

present fairly Enron's financial condition. I believe the decision to approve these transactions was an appropriate one based on the information that had been provided to me and my team. I continue to believe that structured finance, if used by honest companies, whose books are reviewed by responsible auditors, serves a valuable function in our Nation's economy. However, with the benefit of hindsight and the raft of recent disclosures about Enron, I deeply regret that our firm ever entered into transactions with this company.

Thank you.

Senator LEVIN. Thank you very much. Mr. Reilly.

TESTIMONY OF JAMES F. REILLY, JR.,[1] MANAGING DIRECTOR, GLOBAL POWER & ENERGY GROUP, SALOMON SMITH BARNEY/CITIGROUP

Mr. REILLY. Thank you, Mr. Chairman and Members of the Subcommittee. My name is Jim Reilly. I am a Managing Director of the Global Power and Energy Group at Salomon Smith Barney. I have spent more than 25 years as a banker covering the energy industry, and I have spent virtually my entire banking career in the city of Houston.

I was a relationship manager for Enron and its predecessor companies since the 1980's, first at Bankers Trust, later at Citibank, and finally at Salomon Smith Barney. Relationship managers work closely with a particular group of clients in order to understand best their needs. We help them access the full range of resources and expertise available at the firm. Thus, if a client came to me with a particular financing objective, I would put it in touch with the appropriate group at Citibank or Salomon Smith Barney that was best positioned to help accomplish its goals. While in most cases I have a general familiarity with the transactions that my firm arranges for the clients, I do not structure these transactions and typically am not close to the details.

I am aware that questions have now been raised about my references in certain emails to what the *New York Times* reported were "secret oral agreements." There were no "secret deals." The facts are these. In December 1998 Citibank and Enron entered into a $500 million 3-year prepaid swap transaction for the delivery of oil and natural gas. Agreements were entered into with insurance companies to guarantee the delivery of the oil and natural gas. It was understood that Enron would likely settle this contract early within several months, but that informal expectation did not affect the basic 3-year agreement between the parties. In April 1999 Citibank was prepared to syndicate the deal to other banks to spread its risk. Enron preferred that Citibank not do that for reasons having to do with other unrelated credit needs of Enron. Enron paid down a $375 million portion of the contract around that time and expressed its intention to settle the rest of the contract several months later in September, an informal expression of intent not unlike its original December 1998 indication that it expected to settle the contract early.

[1] The prepared statement of Mr. Reilly appears in the Appendix on page 334.

There was no binding agreement between Enron and Citibank that Enron would in fact settle the contract at that time. There was still a 3-year derivative contract covered by 3-year insurance contracts. Indeed September 1999 came and went without Enron settling the contract. No one took action or considered taking action against Enron because there had been no binding or enforceable agreement that Enron had broken. In short my emails about the paperwork not reflecting Enron's intention to settle the contract ahead of time were meant only to alert my coworkers that Enron was intending to take Citigroup out of the transaction. No one read that language to refer to a binding or enforceable agreement, and that's not the way it was intended.

On a more personal note, I have lived in Houston for virtually all of my working life. Every day I see the tragedy that Enron's demise has wrought on my home town, and it saddens me greatly. It is for that reason that I want to thank this Subcommittee for the thorough and detailed investigation it is conducting.

I look forward to answering your question.

Senator LEVIN. Thank you very much, Mr. Reilly.

First though let me ask you a question, Mr. Caplan. Do you agree that there was an objective on the part of Enron to structure these transactions so that the cash obtained by Enron would be reported in the cash flow statement as funds flow from operations, rather than as funds flow from financing or debt?

Mr. CAPLAN. I would say, Mr. Chairman, that was the express—one of the express objectives of the company in entering the financings.

Senator LEVIN. And that you were aware of that objective?

Mr. CAPLAN. Absolutely.

Senator LEVIN. Exhibit 144,[1] if you would have a look at that. This is a loan approval memo. The exhibits are in the books in front of you there.

On page—it is under No. 7, Key Success Factors under the word "story" in the middle. It said there—and this is a Citicorp document—that the prepaid forward structure will allow Enron to raise funds without classifying the proceeds from this transaction as debt. Is that correct?

Mr. CAPLAN. That is correct.

Senator LEVIN. That was clearly known to you. Now, Exhibit 145,[2] this is a September 2000 email in which a Citicorp employee discusses how to present the Yosemite transaction to potential investors. In it he demonstrated he understood that the purpose and the benefits of prepaid transactions included allowing Enron to generate cash flow without increasing the company's reported debt, and right in the—at the beginning where it says, "First, I would go through the prepaid on a stand-alone basis, and get into why a company does it, gets cash flow, shows up as other liability not debt." And then in the middle where it says, that "Enron pays back a fixed stream over time, net net, economically like a loan." Then near the bottom, about 5 lines up, it says, "E", Enron, "gets money that gives them [cash flow] but does not show up on books as

[1] Exhibit No. 144 appears in the Appendix on page 513.
[2] Exhibit No. 145 appears in the Appendix on page 523.

Debt." So that was very clearly understood, that they were trying to have cash flow come from business transactions and not appear as debt on their books; is that correct?

Mr. CAPLAN. Yes, sir, I would say it's very correct because this transaction that's described here and we're discussing today is a form of structured financing, and there are many forms of structured financing out there that have loan-like characteristics that people don't call loans. So none of this would be unusual in this kind of—in speaking about something like this, even saying something like "net net, economically like a loan," I think that's a true statement, but that you could say about a lot of different products that companies enter into.

I think a good example is a synthetic lease, where a company wants to buy a building, and they can kind of do it one of two ways. One way they can do it is go to the bank and borrow the money to buy the building and record that borrowing as a loan on its books. Alternatively, what the company can do is go to the bank and say, "You bank, buy the building and lease the building to us for the economic life of the building, and we'll call that a lease, and we won't record that on our books as debt, we'll record it as lease payments." And I think the point of this is that there are many different ways to structure financings, and they're all based on interpretations of accounting rules by internal accountants and by outside auditors that are within the companies own purview and not the responsibility of the banks.

Senator LEVIN. Well, maybe we will look at synthetic leases next year, but we are looking at prepays at the moment.

If you look at a memo on Yosemite I, this is——

Mr. BUSHNELL. Excuse me, Senator. What number exhibit is that?

Senator LEVIN. I was just going to get to that. Exhibit 146.[1] This is a chart prepared by Citibank. Now, this chart was prepared by Citibank and completed prior to the Yosemite I offering. The numbers do not correspond to the numbers involved in the Yosemite I prepay, but it is illustrative of how various features of the transaction are calculated. Is it not true that the amount of oil or the gas used in the Enron Citi prepays was determined by the amount of money that Enron was getting? In other words, you back into the amount of oil and gas that is the basis of the transaction; is that correct?

Mr. CAPLAN. The ways the transactions were structured is that—again, like in other alternative forms of financing, the company came and said they wanted to receive funds of a certain amount, and then the transactions were structured so that you created a barrel equivalent or a gas equivalent of that amount of funds and attached a price to it. So I think that, yes.

Senator LEVIN. So they did not decide first how many barrels of oil they wanted to sell in advance; they decided first about how much money was needed, and then they translated that into the current or predicted future price of oil; is that correct?

Mr. CAPLAN. I think that is a fair way to say it.

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[1] Exhibit No. 146 appears in the Appendix on page 524.

Senator LEVIN. Now, a memo on Yosemite I which was prepared by the Enron Tax Department described the prepay transaction funded by Yosemite I as a prearranged integrated transaction. That was a memo on Yosemite I prepared by the Enron Tax Department. Would you agree with that description of the prepay transaction, a prearranged integrated transaction?

Mr. CAPLAN. I'm actually not clear what that means. That sounds like a tax term for describing the transaction, and we weren't privy to their internal tax memos or what their tax treatment of the transactions were, so I feel like I can't really comment on the use of that term.

Senator LEVIN. That term appears at the bottom of page 1 of Exhibit 147.[1] You see it down there?

Mr. CAPLAN. I'm sorry. Where is it?

Senator LEVIN. See at the last line, where it says "prearranged integrated transaction?"

Mr. CAPLAN. Yes.

Senator LEVIN. That is an Enron document, but my question to you is do you think that is an accurate description of the prepay transaction that Citibank, Delta and Enron were engaged in?

Mr. CAPLAN. I would say that the legs of the transaction were certainly arranged at the closing of transaction. I'm not sure—again, I'm not sure if that's a tax term, integrated transaction. So I don't really know how to comment on that. The legs of the transaction were all executed on the same day.

Senator LEVIN. Simultaneously?

Mr. CAPLAN. On the same day at the same time, yes.

Senator LEVIN. Now, Exhibit 148 is your chart.[2]

Mr. CAPLAN. I think this might be an Enron chart.

Senator LEVIN. Is that an Enron chart? Yes, you are right, it is an Enron chart. It is called a Prepay Walk Through. This is a prepay walk through. It reviews a Citibank, Delta and Enron prepay, and it is a little difficult here to read, but it reports one important point in a box next to the name of each entity in the transaction, and that is that each entity in that triangle is completely hedged. In other words, there is no price risk. Can you read that? Are you able to read that?

Mr. CAPLAN. Yes, I am.

Senator LEVIN. The top box, it is kind of hard to read, but it says "Delta" at the top and then it says "Debt is now completely hedged," underneath the word "through." Do you see that?

Mr. CAPLAN. Yes, I can read it.

Senator LEVIN. And then down at the right it says Citibank or "Citi is now completely hedged." See that?

Mr. CAPLAN. Yes.

Senator LEVIN. And then on the left it says "Enron" and then it is kind of hard to read because it has got black ink over it, but it says, "Enron is now completely hedged and has only limited exposure to Delta."

Mr. CAPLAN. Yes, I can read that.

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[1] Exhibit No. 147 appears in the Appendix on page 529.
[2] Exhibit No. 148 appears in the Appendix on page 537.

Senator LEVIN. So at that point there is no price risk; is that correct?

Mr. CAPLAN. I think on the beginning of the transaction, in the first leg of it, the price risk is created, and then that price risk is hedged away by entering into the next two legs. So when all the legs are executed, the price risk, the intent is to eliminate the price risk.

Senator LEVIN. And that was done all at the same time?

Mr. CAPLAN. It was done all at the same time.

Senator LEVIN. When those three legs were put together, there was no price risk?

Mr. CAPLAN. When the transaction was—when all the legs were executed, the price risk was eliminated, which I think this is an interesting piece of paper to look at because it clearly indicates that Enron, and I would think therefore their accountants, understood the nature of the transaction and the way that the legs worked together.

Senator LEVIN. And so did Citibank.

Mr. CAPLAN. And absolutely, so did Citibank.

Senator LEVIN. And the parties worked together to arrange that?

Mr. CAPLAN. We worked with Enron to structure the transaction so that our risks were hedged and that it met their requirements. Enron worked with their accountants to set the transaction up so that they could book the transaction as they saw fit, but we did not get involved in their accounting decision, nor do we get involved in any company's accounting decisions.

Senator LEVIN. Who represented Delta?

Mr. CAPLAN. Delta was represented by a firm in the Cayman Islands called Maples and Calder.

Senator LEVIN. But in that particular transaction who represented them?

Mr. CAPLAN. In this particular——

Senator LEVIN. Yes. When you were putting together that triangle, who represented Delta?

Mr. CAPLAN. Maybe we should spend a couple minutes——

Senator LEVIN. Not quite yet. Who represented Delta when you put together—you said the same day they were all——

Mr. CAPLAN. Well, the way the transactions were documented is—in these kinds of structured financings, usually the investment bank prepares the documentation, so our counsel, Milbank Tweed, prepared all of the documentation. Delta had its own counsel, but that counsel's role was somewhat limited in the transaction.

Senator LEVIN. Well, was it there at all?

Mr. CAPLAN. Yes, it was definitely there because they reviewed the documents and had to prepare board resolutions and do all the things that make Delta an independent entity for accounting purposes, which is what's relevant here.

Senator LEVIN. Who paid Milbank Tweed?

Mr. CAPLAN. Mainly in these transactions Enron paid Milbank Tweed.

Senator LEVIN. So Delta's lawyer was paid by Enron?

Mr. CAPLAN. Delta's lawyer—it depended on the transaction—honestly, I don't remember exactly, but Delta, some of the fees for Delta's lawyers were paid by us, some were paid by Enron, some

were paid by spreads in the transaction where amounts were—where when you netted out the three legs of the transaction, there was a spread left at Delta, and that paid some of the fees to their lawyers and their management and that sort of thing. It's a very typical kind of arrangement for the bank to make those payments or——

Senator LEVIN. So what did Delta pay?

Mr. CAPLAN. What did Delta make?

Senator LEVIN. Pay.

Mr. CAPLAN. Pay?

Senator LEVIN. You paid part of it, Enron paid part of the Milbank fee. What did Delta pay? What part of the fee did Delta pay?

Mr. CAPLAN. To its lawyers?

Senator LEVIN. Yes.

Mr. CAPLAN. I'm not clear that they paid any of their fees to their lawyers. Only if there was spread left in the transaction that was there to pay lawyers, but it was never intended that Delta was going to have huge sums of money to pay—to pay its lawyers or anyone else.

Senator LEVIN. How about any sums of money?

Mr. CAPLAN. It was intended to have sums of money, yes.

Senator LEVIN. Have a spread?

Mr. CAPLAN. To have—yes, there were always earnings at Delta in these transactions, because there were transaction costs associated with using Delta as the special purpose entity in the deal.

Senator LEVIN. But you do not think they paid Milbank on this one; you think it was either you or Enron?

Mr. CAPLAN. Yes. It was either us or Enron. Enron paid all of the—until they went into bankruptcy, they paid all of the Milbank bills. Some remained outstanding.

Senator LEVIN. Now, in the prepays involving, or most of the prepays involving Enron, Citibank, and Delta, did commodities ever change hands?

Mr. CAPLAN. All of the prepaid transactions that I worked on were financially settled, which means that there is no change of commodities between parties. In the commodities market you can do transactions that are either physically settled by delivery of the commodity, or you can financially settle the contract by just exchanging payments based on the price of whatever the commodity reference is.

Senator LEVIN. And can you tell in advance in this particular one whether it was intended that commodities actually be transferred?

Mr. CAPLAN. Absolutely not, because these were financially settled arrangements.

Senator LEVIN. It was never intended that the commodities——

Mr. CAPLAN. I think in some of the earlier prepaids that predate my time at Citibank, and I think a large part of the reason Delta was set up in the first place was because there was going to be a physical delivery of commodities, and Citibank, as a bank, under its regulatory regime, wasn't able to take physical deliveries of commodities, so I think the intent was there, but when I got involved, financial settlement was the way—was the method of settlement of choice.

Senator LEVIN. Looking again at that Exhibit 148, would you agree that the point here was to eliminate price risk, ensure that the funding source get its money; in other words, to perfectly hedge the transaction; would you agree with that, that was the intent?

Mr. CAPLAN. I'm sorry. Where are you reading that?

Senator LEVIN. Exhibit 148, that transaction that is described there with that triangle, the intent of that was to ensure that the funding source get its money, price risk be eliminated, and that it be a perfectly hedged transaction.

Mr. CAPLAN. Absolutely, because as a bank, we don't look to take on commodity risk. We look to take on credit risk. So any time we enter into a transaction that creates some commodity risk, the first thing we do as a prudent risk management exercise is to go and hedge that commodity risk. So that was absolutely the intent.

Senator LEVIN. All of the parties were hedged in that one?

Mr. CAPLAN. All of the parties were hedged in this one, yes.

Senator LEVIN. Now, as we learned earlier today, it is important that the third party be independent of the first two parties or the other two parties. So we are now going to talk a bit about Delta.

Delta, as we understand it, was formed in the Cayman Islands in 1993. Do you know who formed Delta?

Mr. CAPLAN. Yes, absolutely. It was formed by Citibank, much as Citibank forms special purpose entities to do lots of structure finance transactions, much as other institutions in the market form special purpose entities.

Why they're called special purpose entities is they are formed to do a specific purpose, and we formed it—we were involved in setting it up and identifying a law firm that could draft the papers, and paying that law firm in the Cayman Islands.

Senator LEVIN. You paid the law firm?

Mr. CAPLAN. Absolutely.

Senator LEVIN. To set up Delta?

Mr. CAPLAN. We paid the law firm to set up Delta. We—much as we do in many of these—whether it's a credit card receivables transaction, mortgage securitization, we set Delta up for accounting and legal purposes as an independent entity. We were trying to satisfy accounting tests then in existence which still apply today, and Delta's been—as you just noted, Delta's been around since 1993. It's been vetted through our accounting system over that period of time, and it remains for accounting purposes an independent entity.

Senator LEVIN. And who effectively controls Delta? Putting aside the accounting purpose, who effectively controls Delta?

Mr. CAPLAN. I'm not sure——

Senator LEVIN. Common sense terms.

Mr. CAPLAN. Common sense terms, when you're talking about SPVs, I don't think they're that relevant.

Senator LEVIN. Just in conversation here, I am asking you a simple question. Who has effective control of Delta?

Mr. CAPLAN. I'm not certain what—regardless of who has effective control of Delta, I'm not certain why that's a relevant aspect of any of this.

Senator LEVIN. We will decide the relevance of it. But why don't you try to answer the question. Who has effective control of Delta?

Mr. CAPLAN. I would say the directors of Delta, because it's, as a legal matter and as an accounting matter, and I know that you're saying not to look at this as an accounting matter, but I think the only way you can look at Delta is from an accounting perspective, because the only reason it's there is to satisfy the rule-based system of accounting that we have. It's very similar to—I mean "control" is a tough word for me to work with. It's very similar to the word "gain" in the tax code. There are multiple definitions of "gain" depending on the circumstance you're talking about at the moment, and "control" has that same connotation, and I think the relevance of "control" here——

Senator LEVIN. It has nothing to do with gain. It has to do with who controls the entity, that is all. But in any event, has Delta ever entered into a prepay transaction in which Citibank was not involved?

Mr. CAPLAN. No, it has not.

Senator LEVIN. Was it created to assist Citibank?

Mr. CAPLAN. It was absolutely created to assist Citibank.

Senator LEVIN. And is it owned by a charitable trust?

Mr. CAPLAN. It is.

Senator LEVIN. Called Grand Commodities Corporation?

Mr. CAPLAN. That's my understanding.

Senator LEVIN. And who has control of that trust?

Mr. CAPLAN. I'm not certain of who controls that trust.

Senator LEVIN. Do you know, Mr. Bushnell?

Mr. BUSHNELL. No, I don't, Senator.

Senator LEVIN. Do you know, Ms. Hendricks?

Ms. HENDRICKS. No, sir.

Senator LEVIN. Do you know, Mr. Reilly?

Mr. REILLY. I don't, Senator.

Senator LEVIN. Could Citibank control that trust?

Mr. CAPLAN. Not to my knowledge.

Senator LEVIN. Could it?

Mr. CAPLAN. It would be pure conjecture to answer that, but——

Senator LEVIN. As far as you know, who—when you want Delta to do something, you notify some lawyer down there in the Caymans?

Mr. CAPLAN. Yes, absolutely. Again, this——

Senator LEVIN. And you pay that lawyer's fees or Enron does, right?

Mr. CAPLAN. It depends on the transaction. It's been different in every one. But, again, I don't find any of that unusual for structured——

Senator LEVIN. I am not arguing usual or unusual. In fact, it is probably mighty discouraging that it is very usual. The fact that it is common doesn't mean that it is not deceptive. The question is whether or not a common practice was put here to a deceptive purpose. That is the issue here. You have got a lawyer down in the Cayman Islands. It is a secrecy jurisdiction. You can't pierce that veil. Some trust is created, just the way it was—we just went through that with Chase. Some trust is created. In the case of Chase, Chase's lawyers created the trust. We don't know who created this trust. You don't know who created this trust. We are going to try to find out, if you will be cooperative.

Along that line, by the way, will you agree to authorize Maples and Calder in the Cayman Islands to give the Subcommittee all documents relating to the formation, ownership, and activities of these entities? Will you give us that authority?

Mr. CAPLAN. I think we'd have to defer to counsel to answer that question.

Senator LEVIN. Will you let the Subcommittee know whether you will give us that authority?

Mr. CAPLAN. Absolutely.

Senator LEVIN. Why do you do this in the Caymans, a secrecy jurisdiction? Why aren't you just open about these kind of things? You are forming an entity. The operations of that entity are hidden. It has got to be independent or else this whole thing doesn't work. It doesn't work for other reasons, by the way, which it seems to me you have already pretty well cleared. It was all done at one time. There is linkage between the transactions. According to our experts here, this doesn't even qualify in any event, no matter who owns Delta.

But putting that aside just for a moment, why are you forming this kind of entity in the Cayman Islands, in a secrecy jurisdiction? And why do you hesitate to say that you will give us authority to try to pierce that secrecy to find out who owns that trust which holds the stock in Delta? That is troubling and I want to know your answers, either you or Mr. Bushnell.

Mr. BUSHNELL. I think I would answer in a couple of ways, Senator. I think the reason why we want to check with counsel is we don't know if we are able to enforce anything on——

Senator LEVIN. I didn't say that. I said authorize.

Mr. BUSHNELL. Authorize to ask. We certainly could ask. Whether they'll respond to that or not, I don't know what their terms and bylaws and conditions are.

Senator LEVIN. Are you then saying that you will—that Citibank will authorize us to—that you will authorize them to turn over any documents that they have to this Subcommittee?

Mr. BUSHNELL. Again, Senator, that is something that I want to discuss with counsel.

Senator LEVIN. OK. Then let's go back to the Caymans. Why do you do this in secrecy jurisdictions? Why not do it in daylight?

Mr. BUSHNELL. Do you want to answer that, Mr. Caplan?

Mr. CAPLAN. Yes, I don't think that there's anything really nefarious about doing it in the Caymans. Again, you have to step back and put this in perspective of what this business is. And the structured finance business has developed over the last 30 years, and a lot of it is around using these special purpose entities, and you often set them up in different jurisdictions. And I think the main reason you use the Caymans is there's tax neutrality in the Caymans. It's not because we are trying to hide something. All the transactions that we've done with Delta you see in these papers. We have fully disclosed what we have done with Delta. I don't think we're trying to in any way——

Senator LEVIN. We don't know who Delta is. We can't find out from the Caymans——

Mr. CAPLAN. I think the reason for that is there's not much to know about Delta. It's a special purpose entity——

Senator LEVIN. I think you are right. It is a shell.

Mr. CAPLAN. It satisfies accounting requirements to be an independent entity, and that was the sole purpose for setting it up. That was the sole purpose for its use. And I think that if you would examine other special purpose entities used by Citibank and other banks and other corporations in receivables financings or mortgage financings, you will find that they have very similar characteristics to Delta. And if the Subcommittee thinks that that's an appropriate thing to spend its time on, we would applaud anything that makes things clearer to people in the market.

Senator LEVIN. You would applaud making things clearer to the market including——

Mr. CAPLAN. Yes.

Senator LEVIN [continuing]. The nature of Delta. And yet you are reluctant to authorize us to find out everything that we can from Delta. You have to check with counsel.

OK. But, at any rate, let me go back to one of the criteria for this to be a true trading—for a prepay to be a trading contract, according to the experts before us, the purchaser of the gas must have an ordinary business reason for purchasing the gas, not in substance be a special purpose entity established just to get a secured investment in a dead instrument from a gas supplier.

Now, that is what our experts say a legitimate prepay has got to meet, and you have just told us twice this entity was created purely for accounting purposes, no intention whatsoever that that purchaser of the gas have an ordinary business reason for purchasing it. So, whether or not we pierce that veil around Delta—and we are going to keep trying—according to the experts here, this is not a legitimate prepay by your own testimony because Delta was created solely for accounting purposes, you have told us twice. It does not have an ordinary business reason, which it must have, for purchasing the gas. It cannot in substance be a special purpose entity. You just told us that is all it is, is a special purpose entity.

Do you want to respond to that? Because you have just, it seems to me, proven what we have, what our staff has, I think, very thoroughly proven in not only that way but in a lot of other ways as well. But do you want to comment on that?

Mr. CAPLAN. Well, might I ask what that document you're referring to is?

Senator LEVIN. This is the document which the experts here—which we had this morning. It is not a document. These are the criteria for a legitimate prepay.

Mr. CAPLAN. Is it in the exhibit book?

Senator LEVIN. It is not in the exhibit book. It is—what is the exhibit number? Exhibit 112?[1]

We asked the experts that we had this morning about the document which Arthur Andersen prepared for its customers saying that for prepays to be treated as trading contracts, the following attributes must exist, and then if you will look at page 4, the purchaser of the gas must have an ordinary business reason for purchasing the gas, not in substance be a special purpose entity estab-

[1] Exhibit No. 112 appears in the Appendix on page 367.

lished just to affect a secured investment in the debt instrument from the gas supplier. We asked them, our experts, whether or not those criteria, in fact, must be met in order for there to be a legitimate prepay transaction that would appear as a business expense or a business operation on the books rather than a debt. They all said yes this morning. Do you have any reason to doubt that that is accurate?

Mr. CAPLAN. Just briefly looking through this, I think this is a very interesting document because it's a document prepared by Enron's auditors. So, clearly, Enron's auditors had to——

Senator LEVIN. It is by Arthur Andersen.

Mr. CAPLAN. Right, which is——

Senator LEVIN. Arthur Andersen, at least at that moment, was known as a legitimate firm which——

Mr. CAPLAN. Absolutely.

Senator LEVIN [continuing]. Set up the caution. Here Arthur Andersen is being cautionary here. They are telling their client, if you are going to have a legitimate prepay, you have got to follow certain rules. It is certainly nice to hear Arthur Andersen laying down certain rules for Enron. They told Enron for prepays to be treated as trading contracts, in other words, not as debt, the following attributes must exist, and then they listed here—this attribute doesn't exist in the contract that you just mentioned.

Mr. CAPLAN. Well, what's interesting to me about this exhibit is that if truly that is Arthur Andersen's opinion and Arthur Andersen knew of the entire transaction as described in the Enron documents you've just shown me, I would say either one of two things happened: Arthur Andersen concluded that these criteria were met because they gave a clean audit opinion for Enron through all the periods—and I see this document has a 1997 reference in it, so it's clear that this was in existence for a while; and if our transactions didn't meet these criteria, which I'm seeing for the first time, frankly, and Arthur Andersen still gave a clean opinion, then what does that say about what Arthur Andersen was doing?

Senator LEVIN. But they didn't know who Delta was. And you do.

Mr. CAPLAN. Why, then——

Senator LEVIN. They are just telling their client Delta has got to be—they just lay it out here. Delta has to have an ordinary business reason for purchasing the gas. They are notifying their client of that.

Mr. CAPLAN. But then I——

Senator LEVIN. They don't know who Delta is. You do.

Mr. CAPLAN. Absolutely.

Senator LEVIN. You just told me that Delta must have an ordinary business purpose for purchasing the gas, not in substance be a special purpose entity. You knew they were a special purpose entity. You said twice, of course, that is all they are. So unless you disagree with that criteria for what is a legitimate prepay, you have demonstrated why this was not a legitimate prepay. And yet it appeared on the books as a legitimate prepay.

Mr. CAPLAN. Senator, could I——

Senator LEVIN. You referred investors to those books, by the way.

Mr. CAPLAN. I would actually disagree with the statement that Arthur Andersen had no knowledge of Delta.

Senator LEVIN. Forget that. If they had knowledge of Delta and knew then that it violated their own criteria, then they are culpable. I am not talking about Arthur Andersen. We have had them here. We will have them again. I am talking about you folks. You folks knew by your own testimony that Delta did not have an ordinary business purpose for purchasing the gas. It was a special purpose entity. You have told us that twice. So unless that criteria is wrong—and we had an expert here this morning that said it is not wrong, by the way—you folks knowingly participated in a transaction characterized as a prepay which, in fact, was not a prepay.

Now, do you disagree with this criteria as being accurate?

Mr. CAPLAN. I disagree with—I have no basis for—I mean, this is an accounting interpretation, so I have no—I'm not an accountant. I have no basis for determining what the right criteria are for a prepay to be treated as a prepay on a company's books. That is between the company and its auditors.

We were of the belief that Enron in connection with its accountants had done whatever disclosure to its accountants, had reached whatever conclusions, we were fully of the belief that Andersen was fully aware of every aspect of this transaction. So if these are the requirements that Andersen was setting out, which we had no knowledge of prior to this point, then clearly Andersen must have thought they were met. Why else would they give an unqualified opinion to the financials?

Senator LEVIN. Let's come back to you. You have an accountant, don't you, Citibank?

Mr. CAPLAN. Absolutely.

Mr. BUSHNELL. Yes, sir.

Senator LEVIN. Doesn't Citibank tell you the same thing, that in order for a prepay to be treated as a trading contract, that the purchaser must have an ordinary business purpose and not be a special purpose entity? Isn't that what your accountant tells you?

Mr. BUSHNELL. The accountants in this transaction for Citibank, we classified this as a trading asset, Senator.

Senator LEVIN. Did your accountant——

Mr. BUSHNELL. For purposes——

Senator LEVIN. Has your accountant notified you or ever told you that the purchaser of gas must have an ordinary business purpose for purchasing gas and not be a special purpose entity? Have you ever been told that?

Mr. BUSHNELL. I don't know what their interpretation——

Senator LEVIN. Not interpretation. Have you ever been informed of that by your accountant?

Mr. BUSHNELL. No.

Senator LEVIN. Who is your accountant?

Mr. BUSHNELL. Our accountant at this time is KPMG.

Senator LEVIN. And who was it then?

Mr. BUSHNELL. It was KPMG.

Senator LEVIN. If there is no third party here that is independent that has the characteristics of not just being created for the purpose and being a special purpose entity, then it is a loan. Now, unless you disagree with that, that is what you end up with here, is that you have a loan and that has got some huge implications because it wasn't treated as a loan on the books. Andersen—I am in-

formed that Andersen asked for a representation that Delta was independent. Enron wrote Citibank and worked on the letter saying that Delta was independent. Is that accurate?

Mr. CAPLAN. There was a representation——

Senator LEVIN. Did Citibank ever work on a letter——

Mr. CAPLAN. Yes.

Senator LEVIN [continuing]. Which represented that?

Mr. CAPLAN. I think this is the point that I'm trying to make, is that Andersen knew fully well about Delta and requested certain representations be made by Delta saying—effectively certifying its status as a special purpose entity that was separate from Citibank. So Andersen fully knew exactly what Delta was and still came to the conclusion that these transactions should not be treated as loans but should be treated as trading assets.

Senator LEVIN. You are saying Andersen knew that this was a special purpose entity established just for that purpose, not because it was interested in buying gas, you think Andersen knew that?

Mr. CAPLAN. I think they knew that.

Senator LEVIN. And did you join in the analysis of this letter that represented that—with Enron representing that Delta was independent?

Mr. CAPLAN. I was involved in the creation of that letter, yes.

Senator LEVIN. Now, we have an Exhibit 150,[1] a fax from the law firm in the Cayman Islands. This is Maples and Calder, a firm that represents Delta that is paid for by other folks like you. Maples and Calder wrote Citibank about a request for information regarding Delta. If you could take a look at Exhibit 150, the Delta attorneys asked Citibank for permission to respond to the request. At least that is what it looks like to me, Exhibit 150 in the middle: "I noted that this information could not be disclosed until we had received authorization from our client."

Maybe I best go back a little bit here. "Regarding Delta Energy Corporation (the 'Company')"—here's the email. We've "been contacted . . . Milbank Tweed in relation to this Company." That's Delta. "They've requested the information outlined in the attached email. I noted that this information could not be disclosed until we had received authorization from our client. In connection therewith, I should be grateful if you would kindly confirm whether it is acceptable to you for this information to be provided."

Are you familiar with that?

Mr. CAPLAN. Yes.

Senator LEVIN. Now, you have no control over Delta. Why would Maples and Calder be seeking permission from Citibank?

Mr. CAPLAN. Again, I think it goes to the reason you set these special purpose entities up, and it is not a question of control. We were the person that sponsored it. We were the person that used it. I don't think it's unusual that Maples and Calder, who we used to set up Delta, would contact us asking if this was OK to talk about with another law firm. The point, again, with the SPVs is that they're separate, independent for accounting and legal pur-

[1] Exhibit No. 150 appears in the Appendix on page 544.

poses, but that doesn't mean that Citibank doesn't have a continuing role in the way they operate.

Senator LEVIN. Well, it looks like you gave permission to Milbank Tweed to get information on Delta, and I am just wondering why you can't do the same for us.

Mr. CAPLAN. I just have to defer that question.

Senator LEVIN. The exhibit, if you would, take a look at Exhibit 151.[1] And this is page 2 of the exhibit, and it is part of account-opening documentation for Delta Energy at Citibank. And given the Subcommittee's attention to money-laundering issues, we checked to see what due diligence was performed by Citibank on Delta before the account was established, and the document contains the following notation: "We will not be"—this is page 2. "We will not be obtaining any documentation because of the internal nature of the account."

Why would Citibank consider the Delta account to be an internal account if you did not have some control over Delta?

Mr. CAPLAN. I think it just goes back to why we set Delta up. I mean, obviously I'm just in the past few days familiar with this document. But if you subscribe to the theory that in these kind of transactions the bank sets up special purpose entities to perform specific roles, then setting up a bank account for that entity would be part of the overall structuring of the deal and would not be unusual. And I would bet that if you were to examine our records on other SPVs or other banks' records on SPVs that you would find similar documentation in pretty much every transaction out there.

Senator LEVIN. It goes on to say, "It will be controlled"—and they are referring here to the account. "It will be controlled exclusively by the Houston office until it is transferred to Citibank, New York, at which time it"—that is, Delta's account—"will be controlled exclusively by New York." So you are controlling Delta's account?

Mr. CAPLAN. I think that's, again, a typical thing in structured financing. You don't allow funds out of accounts in the entire structure because this is one of the control mechanisms you put in place that is a prudent risk management technique so your SPV—because your SPV, Delta in this instance, could theoretically go off and do business with other parties. So one of the ways——

Senator LEVIN. One of the control mechanisms you put in place, you finally got there.

Mr. CAPLAN. I would call it more of a risk management mechanism.

Senator LEVIN. It slipped. The word "control" slipped from your lips. One of the control mechanisms which you put in place.

Mr. CAPLAN. Control of a bank account means that you don't allow disbursement of funds without a sign-off, effectively, which we would call a risk management practice that is prudent so that if the SPV—if the management of the SPV turned—decided to go off on some jaunt and enter into some transaction with another bank, for instance, our funds would not be at risk.

Senator LEVIN. Well, it slipped out there. That was just one of the control mechanisms. But you are going to help us find out all the rest of them.

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[1] Exhibit No. 151 appears in the Appendix on page 545.

Exhibit 152,[1] this is the bill sent by Citibank by Givens Hall Bank and Trust Company of the Cayman Islands, the company that provided administrative services for Delta. The bill for services related to the management and administration of Delta Energy, and you can see Givens Hall bills Citibank. Why? For supplying the board of directors, shareholders, etc., to the company and its parent company and administering the overlying trust for the year ending December 31, 1999. So Citibank is paying for the administrative costs relating to Delta. Is that correct?

Mr. CAPLAN. Again, very typical in these kind of transactions. Yes, it's correct.

Senator LEVIN. You can repeat the word "typical," but the answer comes out the same way. You were paying——

Mr. CAPLAN. Yes, absolutely.

Senator LEVIN [continuing]. For these administrative costs.

Mr. CAPLAN. Absolutely.

Senator LEVIN. It is very typical for you to control the entity that you create. That is typical. That is essential. In fact, you want to control its bank account, you say, because just on some theory that some day this creation of yours might somehow or other decide to go off in some different direction for some unexplained reason.

Mr. CAPLAN. That's correct.

Senator LEVIN. Now, Givens Hall has been replaced by Schroder Cayman Bank and Trust Company as the administrator of Delta. Who owns Schroder, do you know?

Mr. CAPLAN. It's an independent, Schroder.

Senator LEVIN. Wasn't this acquired by Salomon Smith Barney in the year 2000?

Mr. BUSHNELL. Mr. Chairman, perhaps I could answer that. In 2000, we acquired a part of the Schroder's organization.

Senator LEVIN. I am sorry. "Part" was the word?

Mr. BUSHNELL. A part of the Schroder's organization. It did not have to do with funds administration. That remains an independent company that is not under the Citibank umbrella.

Senator LEVIN. Let me yield here to Senator Fitzgerald.

Senator FITZGERALD. Thank you, Mr. Chairman. And I thank all of you for being here.

I want to shift gears just a little bit. How much money does Enron owe Citibank and its—your holding company is Citicorp, right, and all of you work for——

Mr. BUSHNELL. Mr. Fitzgerald, it's Citigroup.

Senator FITZGERALD. Citigroup, OK. That is the bank holding company. It owns Citibank, it owns Salomon Smith Barney, and it owns Traveler's.

Mr. BUSHNELL. That's correct.

Senator FITZGERALD. How much money is owed to Citigroup and its subsidiaries by Enron, say the last time you looked at that time question? I imagine you looked at it at the time of their bankruptcy filing.

Mr. BUSHNELL. Yes, we did, Mr. Fitzgerald, Senator. We could get the Subcommittee the exact number, so this is from my recollection, but at time of bankruptcy filing, the total exposure to

[1] Exhibit No. 152 appears in the Appendix on page 548.

Citigroup was about $1.2 billion. That was comprising three major components that you've discussed in the organizational structure of Citigroup. There were bonds, Enron bonds, and indeed——

Senator FITZGERALD. How much were the bonds?

Mr. BUSHNELL. To my recollection, the bonds were—had an amount of about $150 million face. That's what they were purchased for. At the Traveler's Insurance Company there was——

Senator FITZGERALD. Direct bonds of Enron Corporation.

Mr. BUSHNELL. Those were corporate bonds, that's correct. Not only Enron but Enron subsidiaries that went under different names. But that's correct.

Senator FITZGERALD. OK.

Mr. BUSHNELL. Then there was about $300 million of the indemnity company's indemnification risk in the Mahonia transactions. So when we look at overall exposure, we looked at that as a risk.

Senator FITZGERALD. Is that Traveler's?

Mr. BUSHNELL. That's a Traveler's Indemnity Company.

Senator FITZGERALD. But you are contesting that you owe anything——

Mr. BUSHNELL. We are contesting that we owe anything on that.

Senator FITZGERALD. And why are you contesting that? Aren't you saying that JPMorgan Chase knew that its prepay transactions were really loans?

Mr. BUSHNELL. No. What we're contesting is that under New York State law, indemnity companies are not allowed to guarantee financing transactions of any type.

Senator FITZGERALD. When you offered the guarantee, you didn't recognize it was a financing transaction?

Mr. BUSHNELL. We did not recognize it, and that's, in essence, what the documents that were disclosed to us at the Traveler's——

Senator FITZGERALD. And you are saying it was a financing transaction. You believe it—you are now saying it was a financing transaction.

Mr. BUSHNELL. What was issued, in essence, was—the indemnification bonds are for performance bonds. That is what the indemnity companies are authorized to do under insurance law. If this was a financially settled transaction, they're not allowed to indemnify financial settlements, only commodities and other services settlements.

Senator FITZGERALD. Do you think JPMorgan—are you contending that JPMorgan Chase knew it was a financing transaction or didn't know?

Mr. BUSHNELL. I don't know—I'm not—I don't know what JPMorgan Chase thought they——

Senator FITZGERALD. You don't know what they knew, so you don't—it's not your position at Citibank that—or at Traveler's that JPMorgan Chase knew it was a financing transaction that they were getting a surety contract for?

Mr. BUSHNELL. I am not aware of what our position is in that litigation, Senator. I know the basics of the outlined litigation between the indemnity company and JPMorgan Chase.

Senator FITZGERALD. OK. Back to this $1.2 billion in indebtedness: $150 million in Enron Corporation or corporate subsidiary bonds; $300 million in indemnity.

Mr. BUSHNELL. Exposure, as potential.

Senator FITZGERALD. Indemnity exposure?

Mr. BUSHNELL. Correct. And we had about $650 million at time of filing of secured exposure, secured by assets within the Enron group.

Senator FITZGERALD. Is that a loan, a direct——

Mr. BUSHNELL. That was a loan.

Senator FITZGERALD. A $600 million loan.

Mr. BUSHNELL. Yes.

Senator FITZGERALD. Secured by collateral of Enron. What was the collateral?

Mr. BUSHNELL. Pipelines.

Senator FITZGERALD. OK. Was that——

Mr. BUSHNELL. Two pipeline systems.

Senator FITZGERALD. Was that financing you did after the bankruptcy?

Mr. BUSHNELL. No. We did that before the bankruptcy.

Senator FITZGERALD. OK. You are secured on that.

Mr. BUSHNELL. And we——

Senator FITZGERALD. And so that is the total of your exposure, $650 million in secured lending, $300 million in indemnity exposure, and $150 million in bonds.

Mr. BUSHNELL. No, we need a little bit more to get to $1.2 billion, if my math is correct. We had about $150 million of unsecured exposure. Some of that was loan exposure, and some of that was contractual exposures in trading with them for foreign exchange, for interest rate swaps, for commodity trades. So we had those unsecured exposures added up.

Senator FITZGERALD. OK. I want to ask you about the off-the-books partnerships that Congress—at least in the Commerce Committee we were examining these heavily last winter. Enron, as you know, created apparently a couple thousand off-the-books partnerships. Many of them were borrowing money. Enron would sell assets to the partnerships and book revenue from the sale of assets. They would kind of do it in the way to encourage the perception that these were revenues from recurring operations rather than one-time sales.

It was reported on page 73 of the Powers report that Citigroup invested bank funds—I imagine Citibank funds—in at least one of these partnerships, LJM2. Is that true?

Mr. BUSHNELL. Yes, it is, Senator. A point of clarification. When I discussed the $150 million of corporate bond exposure, we would have included the $15 million—I believe the number was $15 million, but, again, we can get the Subcommittee the exact number—as investment exposure, maybe is a better way to term it, in that. And, again, I can get you the exact entity within the Citigroup family which had that. I doubt that it was Citibank NA, but instead a different structure that would have made that investment.

Senator FITZGERALD. Could be Salomon Smith Barney?

Mr. BUSHNELL. No, not Salomon Smith Barney either. Perhaps a holding company at Citigroup or a different investment vehicle.

Senator FITZGERALD. That invested the $15 million, but they invested in it in LJM2. That money isn't owed by Enron to Citibank

or whoever invested that money. In fact, that is not a loan. That was an investment, right, an equity investment?

Mr. BUSHNELL. That's correct.

Senator FITZGERALD. So they lost that.

Mr. BUSHNELL. That's correct.

Senator FITZGERALD. Do you know who at Citigroup was responsible for managing the Citigroup investments in these partnerships?

Mr. BUSHNELL. I know at the senior level. I don't know who would have—that would have been Todd Thompson who runs the investment group.

Senator FITZGERALD. Todd Thompson.

Mr. BUSHNELL. Todd Thompson.

Senator FITZGERALD. Would he have been the one to sign off on the investment in LJM2?

Mr. BUSHNELL. I'm not aware of what their sign-off procedure is, Senator, for that portion of Citigroup, how they handle——

Senator FITZGERALD. But in his office or his group?

Mr. BUSHNELL. Somewhere within his division there must have been, since we made the investment, some sort of vetting process and approval process to take that in.

Senator FITZGERALD. Now, some of the class action lawsuits that have been filed that named JPMorgan and Citigroup allege that JPMorgan Chase and Citigroup administered the financial affairs, such as profit distribution and capital calls, of LJM2. Is that correct?

Mr. BUSHNELL. Senator, I don't know what the structure was, who the administrative agent might have been from the bank for LJM2.

Senator FITZGERALD. Was the bank an administrator or——

Mr. BUSHNELL. Again, I don't know.

Senator FITZGERALD. Does anybody know? You don't know the answer to that?

Mr. BUSHNELL. No, sir.

Senator FITZGERALD. Is it possible that any of the employees, executives, or director of Citigroup personally invested in any of the Enron partnerships such as LJM2?

Mr. BUSHNELL. I don't know, Senator, the answer to that question, if any did. We have a fairly stringent policy in Citigroup regarding investments by any individuals that would have been vetted through our compliance and responsibility function, but——

Senator FITZGERALD. Does anybody know if any——

Mr. BUSHNELL. No, sir.

Senator FITZGERALD. OK. Then can you answer that question in writing and give it to us and tell us, survey the office, find out if any employees, executives, or directors of Citibank invested in any of the Enron partnerships?

Mr. BUSHNELL. Yes, we will, Senator, and put that in writing. I've been informed by our counsel behind me that no individuals did invest, no Citigroup individuals did invest in LJM2.

Senator FITZGERALD. So your testimony is that no employees, no executives, and no directors of Citigroup invested as individuals in any of the Enron partnerships, any of the 2,000 partnerships?

Mr. BUSHNELL. The only one, again, that I've just been passed a note from counsel refers to LJM2. But we could get that information for you, Senator, if that——

Senator FITZGERALD. I would appreciate a written response to that survey.

Now, it has been reported that Mr. Rubin, currently the vice chairman of Citigroup, made calls to the Undersecretary of the Treasury and to Moody's Investor Services in an attempt to assist Enron days before they filed for bankruptcy. Do you know if that is true?

Mr. BUSHNELL. I don't know if that's true, Senator.

Senator FITZGERALD. Does anybody know if that is true?

Ms. HENDRICKS. I have no knowledge.

Mr. CAPLAN. I don't know.

Senator FITZGERALD. Has any of you ever talked to Mr. Rubin about Enron?

Mr. BUSHNELL. No.

Mr. CAPLAN. No.

Senator FITZGERALD. None of you have?

Mr. BUSHNELL. I have talked to Mr. Rubin about Enron in a general discussion when it was going into bankruptcy. We had several high-level meetings, as you could attest to a situation, and he was in attendance at those, but not about anything having to do with——

Senator FITZGERALD. So the *New York Times* reported on February 21, 2002, that Mr. Rubin made those calls to the Undersecretary of Treasury and to Moody's Investor Service, and you are saying you are not sure if that *New York Times* report is accurate?

Mr. BUSHNELL. I have no knowledge of accuracy or inaccuracy.

Senator FITZGERALD. Does anybody? Can you find out an answer to that and clarify that in writing what Mr. Rubin's contacts were with the administration and provide that to the Subcommittee? I find that fairly incredible that something like that is reported in the *New York Times* and you don't know whether that is true, there is no investigation to find out whether that is true, nobody cares whether your vice chairman called the Undersecretary of the Treasury?

Did you ask Mr. Rubin to get involved, Mr. Bushnell?

Mr. BUSHNELL. No, I did not.

Senator FITZGERALD. Are you aware of anybody who may have asked Mr. Rubin to get involved?

Mr. BUSHNELL. No, I'm not.

Senator FITZGERALD. Do you think he just came into work 1 day and it popped into his head, I'm going to pick up the phone and call the Undersecretary of the Treasury and ask them to see what they can do to help Enron out?

Mr. BUSHNELL. I don't know what was going on in his head. Senator, we'd be happy to respond to the question in writing for you, if that helps.

Senator FITZGERALD. Mr. Caplan, do you have no knowledge, too?

Mr. CAPLAN. No, sir, I'm not at that level of the organization, unfortunately.

Senator FITZGERALD. Are you, Mr. Bushnell? You talk to Mr. Rubin.

Mr. BUSHNELL. I do talk with Mr. Rubin. But I did not question him about his phone calls or involvement with either Moody's or governmental officials.

Senator FITZGERALD. Either of you talk to Sandy Weill about Enron Corporation?

Mr. BUSHNELL. I did.

Senator FITZGERALD. And what was the nature of that conversation?

Mr. BUSHNELL. The nature of that conversation was many conversations about our exposures across Citigroup—how we were going to deal with them, what was likely to happen in terms of financing, debtor in possession financing after they filed for bankruptcy, and——

Senator FITZGERALD. Is it possible Mr. Weill asked Mr. Rubin to call the Undersecretary of the Treasury?

Mr. BUSHNELL. I wouldn't know, Senator.

Senator FITZGERALD. Did you ask him for help?

Mr. BUSHNELL. I did not ask Mr. Weill or Mr. Rubin for help.

Senator FITZGERALD. Ms. Hendricks.

Ms. HENDRICKS. Yes, sir?

Senator FITZGERALD. Have you talked to Mr. Rubin or Mr. Weill——

Ms. HENDRICKS. No, sir, I have not.

Senator FITZGERALD [continuing]. About Enron?

Ms. HENDRICKS. No, sir.

Senator FITZGERALD. Mr. Reilly.

Mr. REILLY. No, I have not, Senator.

Senator FITZGERALD. Salomon Smith Barney, were they going to be an advisor or were they hoping to get the business to advise Enron on their merger with Dynegy? Any of you aware?

Mr. REILLY. Yes, Senator, we were—Salomon Smith Barney was the co-advisor with JPMorgan.

Senator FITZGERALD. You were.

Mr. REILLY. Yes.

Senator FITZGERALD. And so you hoped that that merger would go through at the time? I mean, you were trying to put it together; is that correct?

Mr. REILLY. We were, again, one of the advisors.

Senator FITZGERALD. Moody's or Standard & Poor's—I can't remember which one of the credit agencies—said that they were getting calls from banks urging them to not lower Enron's credit rating, to give it some time because they wanted this merger to go through. Are you aware of anyone at Citibank calling Moody's, Standard & Poor's, or any other credit agency urging them not to lower the credit rating of Enron prior to this merger?

Mr. BUSHNELL. Senator, I'm not aware of the people involved. I know that there were conversations between the rating agencies and Enron during this time when the possibility of a merger existed and that as advisors we would have been involved in those meetings as to the possibility of the merger happening or not and what its influence on the business and ratings might have been.

Senator FITZGERALD. Any of the others care to comment on that? Mr. Reilly, do you have any knowledge of attempts by anyone with-

in the Citigroup holding company to contact the rating agencies around the time of the Dynegy transaction?

Mr. REILLY. Senator, I would echo what Mr. Bushnell said.

Senator FITZGERALD. Mr. Reilly, do you know how much money in fees Citigroup or Salomon Smith Barney would have realized had the Dynegy-Enron deal gone through?

Mr. REILLY. Not precisely, Senator.

Senator FITZGERALD. Roughly?

Mr. REILLY. It was in the tens of millions.

Senator FITZGERALD. Forty-five million sound about right?

Mr. REILLY. I don't recall the exact figure, but that number wouldn't surprise me.

Senator FITZGERALD. I would like to go to your analyst Raymond Niles at Salomon Smith Barney. I gather that he tracked Enron for you, and on October 26, 2001, he downgraded Enron from a speculative buy to a speculative neutral. This followed the October 16 restatement, I think, that caused Enron to report a $618 million third quarter loss and disclosed a $1.2 billion reduction in shareholder equity.

Now, Mr. Niles, like Mr. Fagin from JPMorgan Chase, testified before this Subcommittee earlier this year and gave his reasons for making the recommendations he did make.

Do you think that the indebtedness of Enron to Citibank in any way, shape, or form had any influence on the analyst ratings, on Mr. Niles' ratings?

Mr. BUSHNELL. No, I don't, Senator. We have stringent internal controls, even if there was a desire to retain private side information from public side information, Mr. Niles is a public side analyst. He has access to public information. Clearly, as bankers and as advisors, we had a lot of private side information, and we have a strict internal compliance process known in the industry as a Chinese wall, but a firewall that prevents information from flowing between those private side information to the public side.

Senator FITZGERALD. But Salomon Smith Barney was owed money, not just Citibank but Salomon Smith Barney——

Mr. BUSHNELL. Salomon Smith Barney, the legal entity, had trading exposures—contracts—which caused us to end up as we are—an unsecured creditor.

Senator FITZGERALD. You are an unsecured creditor in the bankruptcy, and you are telling me that Mr. Niles—there is no way that he could have known that, that the company he worked for was owed money by Enron.

Mr. BUSHNELL. That's—he did not know the amount that we would have had—or if he had——

Senator FITZGERALD. Did he know that money was owed?

Mr. BUSHNELL. Don't even know if he—he would not have had access to that information.

Senator FITZGERALD. Would anybody who did know that Enron owed Salomon Smith Barney money have been in a position to influence Mr. Niles in any way?

Mr. BUSHNELL. Again, Senator, that would definitely be against our internal compliance rules as well as lots of others. So we don't feel that that would have happened.

Senator FITZGERALD. If I could ask you a few questions about the Delta transactions, we have established that Citigroup has a subsidiary in the Cayman Islands known as Delta.

Mr. CAPLAN. I would not term them a "subsidiary."

Senator FITZGERALD. OK. What would you term it?

Mr. CAPLAN. They are an independent special purpose entity that we've used in these transactions, but it is definitely not a subsidiary of Citigroup.

Senator FITZGERALD. And it is out of your control?

Mr. CAPLAN. For accounting purposes, which I think is the relevant regime, it's out of our control.

Senator FITZGERALD. Who owns it?

Mr. CAPLAN. A charitable trust.

Senator FITZGERALD. OK. And we had some discussion about this before. And what is the name of the charitable trust?

Mr. CAPLAN. I think it's something called Grand Cayman Commodities Corp.

Senator FITZGERALD. Who established that trust?

Mr. CAPLAN. I'm not sure. Delta predates my time at Citibank.

Senator FITZGERALD. And what is the charitable business of the charitable trust?

Mr. CAPLAN. I'm not sure of that either. But, again, the purpose of Delta, it was established by us. We had the entire——

Senator FITZGERALD. I thought it was established by a charitable trust.

Mr. CAPLAN. It was established by Citibank, it was sponsored by Citibank, and a charitable trust——

Senator FITZGERALD. I thought you just said that Delta was established by a charitable trust.

Mr. CAPLAN. Delta is owned—I'm sorry for using the wrong word. Delta is owned by a charitable trust, but it was sponsored and put together by Citibank to use in these particular type of structured financing transactions, and, again, it's very similar to special purpose entities we create——

Senator FITZGERALD. Who is the trustee of the charitable trust?

Mr. CAPLAN. I'm not certain of that.

Senator FITZGERALD. Can you find that out and put that in writing to our Subcommittee, please?

Mr. CAPLAN. Certainly.

Senator FITZGERALD. Who is in control of the—does this charitable trust do whatever Citibank tells it to do?

Mr. CAPLAN. The charitable trust?

Senator FITZGERALD. Yes. You told them to establish Delta, and they just go ahead and do that?

Mr. CAPLAN. The charitable—all the charitable trust did was buy the shares of Delta.

Senator FITZGERALD. So is Delta a corporation?

Mr. CAPLAN. Delta is a corporation.

Senator FITZGERALD. And the charitable trust——

Mr. CAPLAN. Is the owner.

Senator FITZGERALD [continuing]. Bought the shares?

Mr. CAPLAN. Correct.

Senator FITZGERALD. Did you ask the trustees of the trust to buy the shares?

Mr. CAPLAN. Of the—yes.

Senator FITZGERALD. What year was this?

Mr. CAPLAN. Nineteen-ninety-three.

Senator FITZGERALD. How much did the charitable trust pay for the shares?

Mr. CAPLAN. I'm not even sure that they paid for them. They own the shares. They may have been contributed to the charitable trust. That's typically—when you set up a special purpose vehicle to act in a role in one of these structured financings, you typically take the ownership interest and contribute it to a charitable trust. So I don't think there was any payment by the—I mean, the purpose of the charitable trust is that it's supposed to hold the shares. Again, it's a very generic concept in structured finance.

Senator FITZGERALD. Well, now I think whoever the trustees of this charitable trust that are holding shares in Delta might regret that they are holding them because there could be some liability attached to that, couldn't there, with all the lawsuits that have been filed regarding ways in which Enron's debts were concealed from the public? I would like to know who the trustees of this charitable trust were, and I would appreciate it if you could provide that to the Subcommittee.

Mr. CAPLAN. Yes, Senator.

Senator FITZGERALD. Any information. Is this charitable trust directly or indirectly controlled by Citibank?

Mr. CAPLAN. Not to my knowledge.

Senator FITZGERALD. It is independent of Citibank?

Mr. CAPLAN. That's my understanding.

Senator FITZGERALD. Is it a U.S.-based charitable trust?

Mr. CAPLAN. I don't think so. I think it's a Cayman Islands-based charitable trust.

Senator FITZGERALD. OK. Delta was established in 1993. Has it had any business transactions that were not related to Enron?

Mr. CAPLAN. Yes, it has. With, I think, Arcla Energy Corporation, and I think the other one was Hess.

Senator FITZGERALD. With two other energy——

Mr. CAPLAN. Yes.

Senator FITZGERALD. Only with energy corporations.

Mr. CAPLAN. Well, I think that is because of the reason why—again, when you establish these special purpose entities, they are established for a special purpose. That's kind of where the name comes from. And in this case, Delta was established to do commodity swap transactions, and those commodity swap—and where that business—my understanding of where that business started was, again, in the oil—in the energy and power industry, these prepay transactions were fairly typical. And they started to come to banks to do them, but banks, at least at that time, weren't able to hold physical commodities such as oil. So Delta was established for the special purpose of being able to hold physical commodities of oil.

Senator FITZGERALD. Who first suggested setting up Delta? Whose idea was that?

Mr. CAPLAN. I'm not sure of the answer to that.

Senator FITZGERALD. Were you around in 1993, Mr. Caplan?

Mr. CAPLAN. No. I didn't join the bank until 1997.

Senator FITZGERALD. So it was already up and running?

Mr. CAPLAN. It was up and running, had been used multiple times for these kind of transactions.

Senator FITZGERALD. How many times do you think it has been used for these types of transactions?

Mr. CAPLAN. I think it's about—well, it's all the Enron transactions and the Hess one, and I just want to correct one thing which I think we need to straighten out. We're not sure whether it was used by Arcla. I was led to believe that, but I'm just handed a note saying it may not have been. So we'll find out the answer to that.

Senator FITZGERALD. OK.

Mr. CAPLAN. But it's been used probably ten—about ten times.

Senator FITZGERALD. Do you think it was Citigroup that came up with the idea establishing this company, Delta, or do you think it was Enron or some other energy company?

Mr. CAPLAN. I mean, again, we've done these transactions with counterparties such as other banks, so, for example, we did a transaction with Enron where Toronto Dominion was—it was either Toronto Dominion or Barclay's was in the place that Delta is in in these deals. So I'm not sure whether it was something that Citibank decided to establish or was established in connection with here's a transaction, we need a party to hedge commodity risk with, let's—is there someone in the market we can use, or is there a more efficient way to do it.

Senator FITZGERALD. If you could find out who incorporated Delta and provide that——

Mr. CAPLAN. There's a law firm in the Cayman Islands called Maples and Calder who we hired to incorporate Delta.

Senator FITZGERALD. You hired them to——

Mr. CAPLAN. Yes.

Senator FITZGERALD. OK. So Citibank really hired the law firm to incorporate Delta.

Mr. CAPLAN. Yes, which is what—again, we do this all the time. This is standard operating procedure in the structured finance industry. If you go to any other bank out there that engages in these kind of transactions or any corporation that does receivable sales or anything—or mortgage sales, any of those things, you will find that special purpose entities are created in the middle of these transactions to serve different purposes, but they're all kind of formed the same way. The bank involved pays the costs of setting it up, makes sure that it's set up in a way that for accounting purposes it is an independent entity. And then it goes on to serve whatever purpose it's been created for, but, again, it's a very standard concept in structured finance.

Senator FITZGERALD. Now, Citibank, isn't it true that Citibank attempted to lay off some of its position in Enron, Enron owed it a lot of money and Citibank attempted to lay off some of that risk by selling Enron-linked securities, including the Delta loans as notes? Is that correct?

Mr. CAPLAN. The whole purpose of the Yosemite transactions was to take credit risk that was resident in the bank market and move it to the bond market, because the bond market is able to accept longer——

Senator FITZGERALD. OK, credit risk that was a risk that Citibank was absorbing——

Mr. CAPLAN. Citibank or other banks.

Senator FITZGERALD. Citibank and other banks.

Mr. CAPLAN. Yes.

Senator FITZGERALD. You were maybe the lead lender? How many other banks were involved?

Mr. CAPLAN. The way the transactions worked is the money—Enron would refinance transactions with the proceeds it received in the transactions we entered into. So I'm not certain exactly how many other banks they used, but that was the stated purpose of the transaction.

Senator FITZGERALD. How much money did Enron owe to Citibank that Citibank was able to offset by selling bonds?

Mr. CAPLAN. In the first transaction that we did?

Senator FITZGERALD. Yes.

Mr. CAPLAN. I think it was $125 million.

Senator FITZGERALD. And how many more transactions did you do?

Mr. CAPLAN. We did, I guess, four transactions in total.

Senator FITZGERALD. Laying off a total of how much?

Mr. CAPLAN. $2.4 billion.

Senator FITZGERALD. You laid off $2.4 billion——

Mr. CAPLAN. But it's not—again, that's not all of our exposure. It was exposure——

Senator FITZGERALD. How much of it was yours?

Mr. BUSHNELL. Senator, in the first transaction, I think the transaction you were referring to was the $800 million issuance, of which $125 million was repaid to Citibank and $675 million, if my math is correct, would then have been repaid to other banks. And I don't know in each of the separate——

Senator FITZGERALD. Ms. Hendricks, you were actually in charge of the——

Ms. HENDRICKS. Yes, Senator.

Senator FITZGERALD [continuing]. Yosemite investments; is that right?

Ms. HENDRICKS. I was the senior investment banker at Salomon Smith Barney at the point at which Enron first approached us to discuss the concept of using the public capital markets in a structured finance way to enable them to raise capital which would allow them to repay bank structured financings.

Senator FITZGERALD. Money that they owed to you.

Ms. HENDRICKS. And others.

Senator FITZGERALD. So they got the proceeds from——

Ms. HENDRICKS. Absolutely.

Senator FITZGERALD. From the bonds that they issued——

Ms. HENDRICKS. Absolutely.

Senator FITZGERALD [continuing]. And used it to repay to you.

Ms. HENDRICKS. Absolutely. And the purpose for that was so that they could continue to get new capital from us, which they subsequently did in a series of transactions, which was all part of their original purpose for structuring the Yosemite deals.

Mr. CAPLAN. And if I could add something to that, when we marketed the Yosemite deals, the purpose that we used in the mar-

keting, that we told investors why we were doing the deals, was to shift credit risk from the bank market to the bond market, which is a deeper market, which—one of the main purposes of this transaction was the bank market is typically a short-term market, and Enron had a lot of long-term assets and wanted to extend its liabilities.

Senator FITZGERALD. You are saying Enron came to you and asked you to do this. It was not any concern that you had at all with Enron's ability to repay the money it owed to Citibank.

Ms. HENDRICKS. No, Senator, perhaps I could answer that. When Enron came to us, the presentation that they made was that they were at a point——

Senator FITZGERALD. When did they come to you with this?

Ms. HENDRICKS. Well, I started covering the account in 1999, early 1999, so this is really about then. And the discussions were 100 percent around that they were beginning to feel constrained in terms of the use of the bank debt markets, constrained relative to not a concern that we had about the credit quality of the company, but constrained in terms of the opportunities that they saw to grow their company.

Putting ourselves back, I mean, it's hard to do today, but going back into the psyche of 1999, Enron was a firm proponent that they had a very novel and different business model which could be applied to a variety of different industries.

Senator FITZGERALD. They sure did.

Ms. HENDRICKS. Yes, Senator, they did. But at the time, virtually everyone——

Senator FITZGERALD. OK, let me ask you this: Enron wants to switch away from borrowing from banks to borrow from the public. So why doesn't Enron—why don't you at Salomon Smith Barney help them issue corporate bonds of the Enron Corporation? What is wrong with that? Why couldn't you have just issued corporate bonds and repaid the indebtedness to you?

Ms. HENDRICKS. We absolutely could have done that. The request of the company was to help them resolve something that had been widely discussed in all of the public market information on the company, which was that as a result of mark-to-market accounting, they were required to recognize as revenue mark-to-market—they were required to recognize as revenue their price risk management book. And, unfortunately, there was no attendant cash flow associated with that.

When they came to us, their comment was that what they wanted to do—and they'd had these discussions with the rating agencies——

Senator FITZGERALD. Well, what difference does it make if there was no attendant cash flow with that?

Ms. HENDRICKS. They needed——

Senator FITZGERALD. The banks had to start doing mark-to-market. When Citibank used to just report your bonds at what you paid for them, and when they changed to mark-to-market, banks started to account for their bond portfolio every day. And, yes, there was no cash flow associated with that.

Ms. HENDRICKS. Yes, but——

Senator FITZGERALD. So what?

Mr. BUSHNELL. Maybe I could answer that, Senator, with, again, the complexities that we deal with. We have bonds in Citigroup that are mark-to-market. We have bonds in Citigroup that are historical cost basis. It depends on the——

Senator FITZGERALD. Then whether they are held for trading or for long-term investment.

Mr. BUSHNELL. Correct. But the intent of it is they're trading, they're mark-to-market. If they're held for investment, they're usually held at an accrual-based process. If I could also, Senator—I misstated some information. On the first Yosemite I transaction, the $800 million, we were repaid $350 million of the $800 million, not $125 million. That is the information that I have.

Senator FITZGERALD. Go back, Ms. Hendricks, explaining why Enron Corporation did not issue bonds, why they instead, you did this Yosemite transaction.

Ms. HENDRICKS. Their objective was to monetize their future cash flows, and the proceeds from those monetizations were going to be used——

Senator FITZGERALD. That is another way of saying borrow, is it not?

Ms. HENDRICKS. Senator, we have had a lot of discussion today with respect to the use of structured financing. There is no question is it a financing. There is no question it is the economic equivalent of a financing. It is structured in such a way so that we'll achieve certain accounting or tax or regulatory issues. In this case, it was an accounting issue, but it was an accounting issue that was represented to us that had been created as a result of the tremendous growth in their trading book and the advent of mark-to-market accounting.

The conjunction of those two, at a time when they believed there was phenomenal additional investment opportunities, resulted in, and this is frankly widely discussed in a number of the public-market documents, including reports from Moody's and Standard & Poor's, at a time when they thought that there were significant investment opportunities that would not generate cash for a 3-year period. So what they were trying to do is to monetize the cash from an existing asset base that they had, which was their trading portfolio and reinvest that in assets which were publicly disclosed——

Senator FITZGERALD. They could have done that by issuing bonds and pledging the assets that you referred to as collateral for the bonds.

Ms. HENDRICKS. Yes.

Senator FITZGERALD. What I am asking you is why do the Yosemite transaction instead of issuing bonds? You can monetize anything by issuing bonds, and what I am asking you is why did you work with Enron, not to help them issue corporate bonds, if they wanted to go to the public markets, as opposed to the bank markets to borrow from, but why did you help them do Yosemite?

Mr. CAPLAN. Maybe I could help on that answer. The purpose of Yosemite was to allow Enron to continue to do structured finance in the bank market because they thought there was a lot of value to the way they structured their balance sheet, and they felt that banks were the most capable or the best clearing house to do structured finance through. So that the idea with Yosemite was to cre-

ate a mechanism where we, as a bank, could move credit risk from the bank market to the capital markets and extend the tenor of bank-type financing.

Senator FITZGERALD. So explain to me how Yosemite worked. Explain exactly how that worked.

Mr. CAPLAN. Yosemite is actually a relatively—I know that it has been perceived as something very complex, but at the end of the day, it is a relatively simple idea. We went to the market and raised money, and the note-holders in Yosemite took the credit risk of Enron, and the way they took that credit——

Senator FITZGERALD. You sold them notes?

Mr. CAPLAN. We sold them notes of a trust.

Senator FITZGERALD. Of a trust.

Mr. CAPLAN. That they were credit-linked notes, and they were linked to the reference credit of Enron. So, if Enron went bankrupt, note-holders would take Enron risk, and they were paid a spread that was above Enron straight bond spreads for taking that risk because of the more complex nature of the transaction.

Senator FITZGERALD. They got a higher return than they would have gotten from Enron bonds.

Mr. CAPLAN. Right, because Enron bonds are publicly offered. They were very generic in a way, and these were Rule 144A offerings. You were buying——

Senator FITZGERALD. What was the return? What was the interest rate on the——

Mr. CAPLAN. To give you an example, in the first transaction, the return relative to Enron, to straight Enron debt, was about 1 percent above, the annual return was about 1 percent above straight Enron debt. So investors were getting paid that extra return for not only taking the credit risk, but understanding the structure that we devised.

Senator FITZGERALD. Was the indebtedness that Enron indirectly incurred by virtue of this Yosemite transaction, was that indebtedness reflected on their balance sheet?

Mr. CAPLAN. Well, the Yosemite transaction did not create indebtedness for Enron. All the Yosemite transaction did was create a credit transfer mechanism for Citibank, but then Citibank turned around and did the prepaid transactions with Enron, which showed up as liabilities on their balance sheet. So what we told investors when we marketed the deal is that any credit risk that Citibank is effectively hedging using this structure, that credit risk starts with Enron and is disclosed in their financial statements.

Senator FITZGERALD. Your testimony here is that there was no desire on the part of Citibank to limit their exposure to Enron that caused you to engage in this Yosemite transaction, that it was all Enron's idea. You didn't hit your lending limits with Enron. You liked Enron as a credit. You would have kept loaning to Enron. It was Enron that came to you and said let us get rid of this loan, this money we owe to Citibank, and let us change it this transaction with Yosemite and have Salomon Smith Barney basically sell this indebtedness off to public investors who will own these notes.

Mr. BUSHNELL. Maybe I can address that, Senator, to help a little bit.

We have, in terms of our own exposures to any corporation, we have internal limits that we set against individual obligors or companies that is in accord with our perceived riskiness of them. Obviously, the higher rated credit, not only by the rating agencies, but done independently by us, we would be willing to extend more money to a higher rate of credit. Those limits are well beneath our legal lending limit. We are strong believers in——

Senator FITZGERALD. What is your legal lending limit?

Mr. BUSHNELL. I believe right now our legal lending limit for Citibank N.A., the largest bank in our chain, I think it is upwards of $5.5 or $6 billion. So the limits——

Senator FITZGERALD. What is your internal lending limit?

Mr. BUSHNELL. Again, generally, you would have to refer to that via both the rating of the company and the maturity or duration of the risk that we were taking on. So the shorter the time frame you might be willing to take more risk, it was only for a 6-month or a 9-month transaction versus something that has 7 years' worth of credit risk. But to give you an indication for a BBB-rated company, our 2 to 5 year maturity side would be on the order of about $400 to $425 million that we would, in general, not want to have any more exposure. This is prudent risk diversification.

Senator FITZGERALD. Four hundred and?

Mr. BUSHNELL. Of equivalent, unsecured credit.

Senator FITZGERALD. This——

Mr. BUSHNELL. This internal guideline.

Senator FITZGERALD. That is your internal guideline.

Mr. BUSHNELL. Yes, Senator.

Senator FITZGERALD. Four hundred and fifty million dollars, but at one time, Enron owed you as much as $2.4 billion.

Mr. BUSHNELL. I am not sure it got quite that high, but we had larger exposure than that. It was over our internal guidelines, and we had an active desire, not because we were concerned about credit quality, but from a portfolio management process, we do not believe in putting too many eggs in any one basket.

Senator FITZGERALD. So you did have a desire to get rid of some of this exposure; is that not correct?

Mr. BUSHNELL. That is correct.

Senator FITZGERALD. Ms. Hendricks, you had said it was just Enron coming to you wanting to do this Yosemite transaction. Now Mr. Bushnell is saying that you had an internal desire at Citibank to get rid of some of this exposure of this one company.

Mr. BUSHNELL. Senator, I think the understanding is my bank is not unique in that, and what was happening, and what the company was expressing, and what this entire transaction was set up to do was a lot of the banks were getting to their limit. Enron was a very fast-growing company, and so there were lots of capital needs, and the banks were providing it, but even though they liked the credit, they obviously continued to extend money, etc.

They were starting to reach their internal prudency thresholds, if you will, and the purpose of the Yosemite transaction was to provide relief, if you will, on those banks so that by accessing the public capital markets so that the banks could continue in their activities in Enron.

Mr. CAPLAN. I would just add to that, one of the reasons I am personally involved in this deal, is I run the credit derivatives business at Citibank, and what we do with credit derivatives is move risk off of our books through swap contracts, which is effectively what we did here, and we do it for prudent risk-management purposes, so that we maintain a diversified lending book and that we do not have too much exposure to any one obligor. It is not necessarily the financial health of that obligor.

Senator FITZGERALD. Oftentimes you lay off that risk with other big banks, though, do you not?

Mr. CAPLAN. We lay it off all different ways. We have done other Rule 144A offerings, where we have laid off risk in a very similar manner to this transaction.

Senator FITZGERALD. Were you doing that prior to the legislation that passed a couple of years ago to repeal Glass-Steagall? Have you been doing that a long time?

Mr. BUSHNELL. Yes, Senator. We have been using various means of credit mitigation, including insurance contracts from insurance companies, including other banks, and that was prior to the passage of Gramm-Leach.

Mr. CAPLAN. The credit derivatives business has been evolving over time, been around since 1996, I would say.

Senator FITZGERALD. The credit derivatives business has only been around since 1996?

Mr. CAPLAN. In any large-scale way. I mean, I think there were small transactions done prior to that, but nothing like it is today.

Senator FITZGERALD. Is that the first time you started laying them off in Rule 144A offerings?

Mr. CAPLAN. I think the first—some of that predates me. I know of one Rule 144A offering that we did in 1998 where we laid off several million dollars of a diversified basket of names.

Senator FITZGERALD. I do not know if the Chairman has called your attention to Exhibit 181.[1] This is an email from William Fox, dated November 10, 1999, to, among others, James F. Reilly, Niels Kirk and also to William Fox—William Fox sending an email to himself, I guess. But Mr. Fox in this email said, "In spite of all of the repayments that we have or will receive from Condor and Yosemite, we still have an exposure issue as it relates to obligor limits; there is a developing view that limits are limits and not to be exceed—" he must have meant not to be exceeded. "This is something we will have to deal with. Also, we do not have room for incremental assets of $200 to $300 million over year end. I will discuss with Reilly later today for current status and review of options."

Mr. Reilly, do you remember this email?

Mr. REILLY. I do, Senator.

Senator FITZGERALD. Did you subsequently discuss with Mr. Fox this email or the issues raised therein?

Mr. REILLY. Certainly the issues raised there.

Senator FITZGERALD. Who is Mr. Fox?

Mr. REILLY. He was then, and is currently, the head of Citibank's Global Energy & Mining Group.

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[1] Exhibit No. 181 appears in the Appendix on page 660.

Senator FITZGERALD. What was Mr. Fox's message to you? It sounds to me like he was concerned that you had too much exposure to Enron, and he is referring to Yosemite, and was he encouraging you to hurry up and get the Yosemite transactions done?

Mr. REILLY. No, that is not the intent of this email. There was, by date—I do not remember the precise date in which Yosemite I actually closed, but there were discussions about looking at what became Yosemite II in Europe and what this bridge, I believe what this bridge was dealing with was whether or not, if we could not get Yosemite II closed by the end of the year, would we consider making another loan on our books.

Senator FITZGERALD. Did you have a position on that issue? Did you favor making more loans to Enron at the time?

Mr. REILLY. What was happening was going back to Mr. Fox's comment is that, and as Mr. Bushnell said earlier, there is in place a framework called the obligor limits, and we were, I think, over time—this is my characterization—over time we would try to manage all clients down and into that obligor limit range. That does not mean that there are not exceptions from time-to-time, and so we were moving in that direction, and so the question here was were we prepared to put on an additional amount of credit exposure in light of those obligor limits.

Senator FITZGERALD. Would you have favored it, taking on an additional amount?

Mr. REILLY. In fact, we did take on the additional amount, Senator.

Senator FITZGERALD. You did, and did you favor taking on the additional amounts?

Mr. REILLY. Yes, I did.

Senator FITZGERALD. You did.

Now, Ms. Hendricks, why do you not finish up with what you started. I interrupted you, and we went to others. You started to explain how the Yosemite transactions worked. You said that Enron came to you and wanted to switch from tapping bank debt to tapping public debt.

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. So who came in to ask you for help? Did Mr. Fastow come to you?

Ms. HENDRICKS. No. Actually——

Senator FITZGERALD. Mr. Glisan.

Ms. HENDRICKS. No, Mr. Glisan was not in charge of the company. I think it would have been Jeff McMahon.

Senator FITZGERALD. Jeff McMahon came to you.

Ms. HENDRICKS. Yes.

Senator FITZGERALD. And he asked you to put this together.

Ms. HENDRICKS. He or members of his team. It was a collective conversation.

Senator FITZGERALD. Did you know roughly when that was?

Ms. HENDRICKS. Well, in early 1999.

Senator FITZGERALD. Early 1999, and explain to me what you did with Yosemite. You said that you created a trust. Was Yosemite a trust?

Ms. HENDRICKS. Senator, the first thing I would have done on the investment banking side is, first, make sure that Jim Reilly,

who was my colleague on the commercial banking side, was aware, and he would have done the same with me. And then the second thing we would have done is created a team of product specialists who would have sat down with us with the company and attempted to brainstorm solutions to the problem that the company was presenting to us.

Senator FITZGERALD. Did you sit down with Mr. Reilly at that time?

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. You two collaborated on this?

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. And you came up with the idea of Yosemite?

Ms. HENDRICKS. No, sir. I am not smart enough.

Senator FITZGERALD. Who came up with that idea?

Ms. HENDRICKS. Mr. Caplan and colleagues of his in the Credit Derivatives Group.

Senator FITZGERALD. These are the credit derivatives guys.

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. They were the only ones smart enough for that. Again, go back and walk me through this transaction slowly, how this worked. You started to explain about the trust and the notes.

Mr. CAPLAN. The place to really start is the financings that Enron was doing in the bank market, and there were a variety of financings. So the real premise was Enron came to us and said we do a lot of financing in the bank market, we like doing our financing in the bank market——

Senator FITZGERALD. Not just at Citibank, but all other banks.

Mr. CAPLAN. All over the place.

Senator FITZGERALD. Did they take all of their bank borrowings from all over the world and come to you and ask you to——

Mr. CAPLAN. And they said one of the problems we have with bank financing is that it is short term, for the reasons that Mr. Bushnell just explained.

Senator FITZGERALD. Right.

Mr. CAPLAN. So we would like—but the rest of our balance sheet, we have a lot of long-term assets, so we have got long-term assets and short-term liabilities. That seems like a recipe for disaster at some point, if you do not manage those things.

So what their premise was is we are a growing company. We have to be careful thinking about our liquidity plans for the future, and one of the tenets of a carefully thought-out liquidity plan is to better match your assets and your liability maturities.

So the thought was where can you get longer term debt, effectively or where can you place your credit risk in the longer term market? The logical place is the bond market because investors will invest for longer terms there.

So, understanding that they wanted to have the flexibility to continue to finance in a sophisticated way in the bank market, but wanted to move the credit risk out into the capital markets, we developed Yosemite, which basically the idea behind Yosemite is Yosemite is just a credit default swap written from the bond market——

Senator FITZGERALD. Yosemite is a what?

Mr. CAPLAN. It is basically a credit default swap, and I will explain what that means.

Senator FITZGERALD. What is Yosemite from a legal standpoint?

Mr. CAPLAN. From a legal standpoint, the first deal was a trust; the second deal was a Channel Island Corporation; and the other deals were trusts.

Senator FITZGERALD. Yosemite I was a trust.

Mr. CAPLAN. Yes.

Senator FITZGERALD. Was a Cayman Islands trust?

Mr. CAPLAN. A Delaware business trust.

Senator FITZGERALD. A Delaware business trust.

Mr. CAPLAN. So we set up Yosemite. Yosemite issued notes and certificates and held the proceeds of those notes and certificates and invested them—it basically had the ability to invest in several different things, which were not disclosed to——

Senator FITZGERALD. How much did Yosemite I raise?

Mr. CAPLAN. It raised $750 million of notes and $75 million of equity or certificates—equity for tax purposes.

Senator FITZGERALD. Who gave the equity?

Mr. CAPLAN. It was a combination of Citibank and Enron.

Senator FITZGERALD. So Citibank invested its own bank funds?

Mr. CAPLAN. Not directly. It is a little complicated. Actually, a Fleet Boston, Fleet Bank's conduit, which is something called Long Lane Master Trust, I mean this is the essence of structured finance, right? Fleet Boston's conduit called Long Lane Master Trust actually bought the Citibank half of the equity, and then that entity, Long Lane Master Trust entered into a swap with Citibank, where we took the risk on the equity, and we effectively paid them a financing cost for buying the equity, plus a spread for their——

Senator FITZGERALD. That sounds like really you were behind all of the equity then.

Mr. CAPLAN. Well, no, that was only on half of the equity and then Enron, through some entity, bought the other half.

Senator FITZGERALD. Yes, but if you are paying somebody else to invest their half, to take half the equity, you are really putting together all of the equity.

Mr. CAPLAN. The only purpose of having the equity in the transaction was a tax reason, which was to get the notes treated as debt for tax purposes. So the equity had——

Senator FITZGERALD. Are these notes Yosemite issues, are they so-called NIPs?

Mr. CAPLAN. No.

Senator FITZGERALD. No.

Mr. CAPLAN. No, they are credit-linked notes.

Senator FITZGERALD. And they are strictly debt.

Mr. CAPLAN. For tax purposes, they are debt.

Senator FITZGERALD. For other purposes, are they equity?

Mr. CAPLAN. No, they are not equity for any purposes. They are strictly debt. They offer it under an indentured——

Senator FITZGERALD. It is not the new-fangled combination debt——

Mr. CAPLAN. There is no special——

Senator FITZGERALD. So you issued notes and certificates. Are the certificates the equity certificates?

Mr. CAPLAN. Yes, exactly.

Senator FITZGERALD. So you raised $750 million in notes and $75 million in equity. You raised that $750 million in notes, is that promissory notes?

Mr. CAPLAN. No. The trust would issue notes to the market through an indenture——

Senator FITZGERALD. What is the note, a promissory note?

Mr. CAPLAN. It is more like a bond. I guess you could call it a promissory note.

Senator FITZGERALD. Well, a bond is a note.

Mr. CAPLAN. Yes.

Senator FITZGERALD. So a bond or a note——

Mr. CAPLAN. So there was an indenture under which——

Senator FITZGERALD. But there is a promise to repay, right?

Mr. CAPLAN. Yes, by the trust.

Senator FITZGERALD. Yosemite was obligated to repay——

Mr. CAPLAN. Exactly.

Senator FITZGERALD [continuing]. The purchaser of the note. What increments were those notes in? You sold $750 million in notes. Did you sell them in $75-million chunks or $5-million chunks?

Mr. CAPLAN. I think the minimum denomination was a million dollars.

Senator FITZGERALD. Do you know how many investors you got?

Mr. CAPLAN. I think in the first deal it was less than 100.

Senator FITZGERALD. So you had 100 people invested——

Mr. CAPLAN. All in the Rule 144A market, which is qualified institutional buyers.

Senator FITZGERALD. Could you give me examples of some of the Rule 144A market buyers?

Mr. CAPLAN. It is kind of all of the major—it is other banks, it is pension funds, it is insurance companies. To be a qualified institutional buyer, you have to have at least $100 million in investable assets. So it is large institutions.

Senator FITZGERALD. So pension funds, the State pension funds and so forth could have bought those.

Mr. CAPLAN. If they met the requirements for buying the notes, they could, if they had a qualified asset manager and that sort of thing.

Senator FITZGERALD. Do you see any risk with the new breakdown of Glass-Steagall, where a bank could have, and I am not saying this is what happened, but say you have a bad loan, a bank is enabled to sell securities to the public to take that bad loan off their books, do any of you see any risk in that, in the new rules we have created by repealing Glass-Steagall in the last couple of years? Do any of you care to comment on that? Then I will turn this back to the Chairman.

Mr. BUSHNELL. Senator, I think raising funds in the capital markets, in the public markets, and where those proceeds go is something that has been quite common. When you do a bond offering in the public markets, the proceeds are fungible, and what the issuer does with those monies, they may pay down banks, they may

pay down certain banks and not other banks. They may pay down payables that they owe. They may do lots of different things with that. It generally flows into that.

So we have stringent rules that I have discussed internally that would not let the public side know what our own exposures were as a means to manage risk. So I think that, at this point in time, we are comfortable with those internal controls.

Senator FITZGERALD. Does Citibank feel, in any way, misled by Enron, Mr. Reilly?

Mr. REILLY. Certainly. Do you mean, with respect, just broadly, Senator?

Senator FITZGERALD. Yes. You were a lending officer at Citibank for them. Do you feel you were misled by them in any way?

Mr. REILLY. I think, Senator, in the 8 or 9 months since Enron declared bankruptcy, an awful lot of stuff has been in the press and has come out through committees and other reports, and I would say that if all of that turns out to be true, then, yes, we would feel very misled.

Senator FITZGERALD. Do you feel that selling the Yosemite securities to the public, that in doing so, Citibank contributed to misleading the people who bought those securities in any way?

Ms. HENDRICKS. No, sir.

Senator FITZGERALD. You do not?

Ms. HENDRICKS. No, sir.

Senator FITZGERALD. Why do you say that?

Ms. HENDRICKS. Because on the basis of the information that we had at the time and the publicly audited financial statements that we had and on which we had every reason to rely, and I would echo, and perhaps state more strongly, Mr. Reilly's conclusion. I do feel misled, and I would say that we disclosed what we knew to be correct. And in accordance with generally accepted accounting principles, the purpose of Yosemite was to deliver senior unsecured credit of Enron to the public markets, which is, in fact, as the structure worked, and it was disclosed, throughout the prospectus, that that is what we were going to be doing.

Senator FITZGERALD. Maybe the Subcommittee has it, but I would love to have a prospectus for Yosemite.

Ms. HENDRICKS. Absolutely.

Senator FITZGERALD. If you could provide that for me. I want to thank you. All of you have been very good. You have been good at explaining some of these transactions. I used to be a general counsel for a bank holding company, but we were much smaller, and we were not this fancy. We stayed away from things that got too complex. We were very simple. We liked the collateral, in the bank vault, in the basement.

This has been a real learning experience, and you have been very helpful, and I appreciate the indulgence of the Chairman of the Subcommittee. You have been very kind to this non-ranking Member to let me go on for quite some time.

So thank all of you for being here.

Senator LEVIN. Mr. Caplan, one of your colleagues apparently thought that there was a need to put a little more window dressing on some of these transactions, and I would ask you to look at Ex-

hibit 154.[1] Exhibit 154 is a May 9, 2001, memo to you from a colleague named Timothy Swanson. He added a minimal charge of one penny to the price spread between the purchase and sale price of the oil involved in this prepay to make it seem a little more like a true trade.

He reports to you that he told another Citi employee that, "The charge makes the prepaid structure a little more like a true trade." That is a pretty good example, is it not, of where Citi employees felt the transactions were not real trades? They had to do something like a penny, which is totally nominal, as he points out, just to make him look like real trades.

Do you remember this memo?

Mr. CAPLAN. I do, in fact.

Senator LEVIN. Did you call him up and say, Hey, wait a minute. These are real trades. We do not——

Mr. CAPLAN. Actually, yes.

Senator LEVIN. You called him right back and said these are real?

Mr. CAPLAN. What I would say is that the economics of the trade, what the various parties were going to receive, were negotiated into the transaction already and what all of this represents is, frankly, another group who started working on these trades late in the day, trying to put some more revenues through. In fact, the one basis point per annum on the whole transaction, this additional revenue that Mr. Swanson was attempting to——

Senator LEVIN. Which is totally nominal, you would agree? It is one penny. It is a totally——

Mr. CAPLAN. It is $315,000.

Senator LEVIN. But its purpose is to make——

Mr. CAPLAN. Its purpose was to make more money.

Senator LEVIN. No, the purpose, it says right here, is to make the prepaid structure more like a true trade. That is what it says here. Did you call back and say——

Mr. CAPLAN. I did, and I said I do not think that that is necessary to make this trade work. And, in fact, the Kelly that is referenced, the Kelly McIntyre referenced in this email, is not a Citibank employee. She is an Enron employee, and Enron came——

Senator LEVIN. Who is an Enron employee?

Mr. CAPLAN. Kelly McIntyre, who——

Senator LEVIN. Is Timothy Swanson?

Mr. CAPLAN. Timothy Swanson is a Citibank employee. Kelly McIntyre, who this email is referring to, is an Enron, was an Enron employee. What ended up happening in this transaction is we executed the transaction without this additional one-basis-point spread because Enron thought the transaction was a real transaction, had vetted it again with their auditors, and felt that this was just Citibank trying to make more money, and they were unwilling to pay the additional amount that we had asked for.

So they said that is very nice that you would like to make more money, but, sorry, we think this transaction works as is, and we are not going to pay you additional fees to do something we think already works.

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[1] Exhibit No. 154 appears in the Appendix on page 552.

Senator LEVIN. But the stated purpose in the memo was not to make more money. The stated purpose was that it would make the spread a more real transaction. That is what was stated here, twice.

Mr. CAPLAN. I think that that's—I'm sorry.

Senator LEVIN. "I told her the change makes the prepay structure more like a true trade." My question to you is: Are you testifying then you called Timothy Swanson and said you don't have to make this look like a true trade, it is a true trade?

Mr. CAPLAN. Yes.

Senator LEVIN. You called Mr. Swanson.

Mr. CAPLAN. Absolutely. I called—in fact——

Senator LEVIN. That is fine. That is good enough.

Mr. CAPLAN. Yes.

Senator LEVIN. You called him back and said——

Mr. CAPLAN. Yes.

Senator LEVIN [continuing]. No need to add a penny——

Mr. CAPLAN. In fact, what I said was Enron won't agree to this because they think it's a true trade already.

Senator LEVIN. The penny is, in fact, diminutive. You would agree to that, right?

Mr. CAPLAN. No, I would not——

Senator LEVIN. You would not agree with that?

Mr. CAPLAN. It's $315,000 additional revenue to Citibank.

Senator LEVIN. I understand, but you would agree——

Mr. CAPLAN. Present value.

Senator LEVIN. You disagree that the penny is, in fact, diminutive, then. You think that's false.

Mr. CAPLAN. It's figured to be an incremental one basis point on the whole transaction. I don't think $315,000 is a diminutive amount of money.

Senator LEVIN. You disagree with that, too.

Mr. CAPLAN. I would disagree with that as well, yes.

Senator LEVIN. And that its purpose was to make this look like a true trade.

Mr. CAPLAN. Yes.

Senator LEVIN. Was that the reason for his recommendation? Would you agree to that?

Mr. CAPLAN. No. The reason for his recommendation was to make more money on the trade, plain and simple.

Senator LEVIN. That is not what he says here, though, is it?

Mr. CAPLAN. I understand——

Senator LEVIN. So now I am asking you, he in this memo said that the purpose of the incremental penny was to make it look like a true trade. Is that not true?

Mr. CAPLAN. That is true. That is what the memo says.

Senator LEVIN. I want to get to the Yosemite structure now. Investors here were told, as I understand it, only that the trust would invest in Enron-related investments. They did not know specifically what the money was invested in.

Mr. CAPLAN. Yes, that is correct.

Senator LEVIN. So nobody was supposed to know specifically what the $800 million was going to be invested in.

By the way, Ms. Hendricks, did Mr. McMahon know that the funds from the Yosemite trusts were going to be used to finance the Enron prepays?

Ms. HENDRICKS. Senator, I believe that when we first started the conversation on this, there was discussion of a number of different assets that were considered before it was determined that it would be prepaids that were used. So I'm not sure that at the first conversation with Mr. McMahon that it was expressly stated that it would be used for prepaids, although clearly that was one of the alternatives.

Mr. CAPLAN. If I might, when the transaction was executed in November 1999, Mr. McMahon absolutely knew what the bank financing was going to be, that it was going to be a prepay transaction. I mean, it's a $750 million transaction. The treasurer of the company would want to know where the money is going and how it's coming in, and he was absolutely involved in that process.

Senator LEVIN. Did he know that the funds from the Yosemite trusts were going to be used to finance Enron prepays?

Mr. CAPLAN. Absolutely. He himself was on the road show for the first deal, so he was intimately aware of the details of the transaction and its intended uses.

Senator LEVIN. He told us something very different, by the way.

In Exhibit 156,[1] if you would take a look at that now, this is a memo from Doug McDowell, an Enron employee who was heavily involved in working with you on the Yosemite structure, I believe. Is that correct?

Mr. CAPLAN. That is correct.

Senator LEVIN. And this is what he wrote, that "Apparently an investor spoke to someone at Citi and received info on Delta. This person at Sumitomo is now calling us asking about Delta now. We need to shut this down."

Did you shut it down?

Mr. CAPLAN. This is a very interesting email.

Senator LEVIN. Did you shut it down?

Mr. CAPLAN. It turned out that the information on Delta had come not from Citibank but from Enron. And we had agreed—again, we've talked about the purpose of the transaction to maintain flexibility and that the investments in Yosemite would not be disclosed to investors. So we had agreed with Enron that we would not tell investors about Delta, and it turned out in this instance that it wasn't Citibank telling Enron about Delta. It was—sorry, the investor. It was Enron telling the investor.

Senator LEVIN. Whoever it was who told the investor, you agreed that information should not go to the investors?

Mr. CAPLAN. Our agreement with Enron was not to disclose the details of the Delta deal. It was a confidential deal from their perspective.

Senator LEVIN. Do you think it is appropriate for an investment bank to shut down the flow of information when an investor requests that information?

Mr. CAPLAN. I think it's appropriate to meet our obligations under whatever contractual arrangement we have, and it was ex-

[1] Exhibit No. 156 appears in the Appendix on page 559.

tremely clear in the disclosure document for Yosemite that investors would not learn the trust investments. So investors had no right to know what was in the trust until Enron filed bankruptcy.

Senator LEVIN. My question, though, is: Do you think it is appropriate for an investment bank not to respond to a request for information, to agree to that?

Mr. CAPLAN. I think it's appropriate—I think "appropriate" is not the right—respectfully——

Senator LEVIN. That is my word. But, no, I——

Mr. CAPLAN. I understand that's——

Senator LEVIN. That is my question. Do you think it is appropriate for an investment bank to agree to deny information to a prospective investor who seeks information?

Mr. CAPLAN. I think unless the investment bank has a legal obligation in a transaction such as this to disclose the information, the investment bank is completely within its rights not to disclose the information. And, in fact, in some of the transactions I was talking about earlier where we did similar Rule 144A offerings and used credit default swaps, we have the same blind trust concept, and investors have asked for information in those transactions as well, and we have again declined to provide the information on the same theory.

Senator LEVIN. I think then that your answer is yes.

Mr. CAPLAN. I think my answer is a little different than yes.

Senator LEVIN. It is appropriate to agree to refuse to provide information on request to a prospective investor. Is that correct?

Mr. CAPLAN. As long as we don't have a legal obligation.

Mr. BUSHNELL. If I could add to that, Senator.

Senator LEVIN. Sure.

Mr. BUSHNELL. In many instances—and we've discussed with Senator Fitzgerald that we are in possession of material, non-public information, and should an investor ask that of an investment bank, it is entirely inappropriate for us and would be indeed a violation of securities law to give that information up.

Ms. HENDRICKS. Senator, if I might?

Senator LEVIN. Sure.

Ms. HENDRICKS. It is specifically stated in the offering document for Yosemite I that we would not tell investors what was in the trust. And I think that's the point that Mr. Caplan—the distinction that Mr. Caplan is trying to draw, is that the fundamental underlying credit of the investor—that the investor was purchasing was Enron senior unsecured, and that was unrelated to the assets that were held in the trust. And because we were not going to disclose at the outset what was in the trust and were not going to disclose on an ongoing basis what was in the trust, it was inappropriate for us to be discussing that after we had specifically stated that we were not going to.

Senator LEVIN. Do you know why Enron wanted to keep the Delta prepay secret?

Mr. CAPLAN. As in many of their structured financings, they required confidentiality as part of the transaction, and that's true, again, in many structured finance transactions. You don't disclose the details of it. There are often proprietary aspects of it that you don't wish your competitors to get a hold of.

Senator LEVIN. But you know that they were also trying to avoid showing debt. You have already testified to that. Is that correct?

Mr. CAPLAN. It's not that they were trying to avoid showing debt. They were trying to classify this as a price risk management liability——

Senator LEVIN. Instead of——

Mr. CAPLAN. Which is a liability.

Senator LEVIN. Instead of debt.

Mr. CAPLAN. Instead of a loan, yes.

Senator LEVIN. Try not to show it as debt. Why do you avoid that word? You say they don't want to show it as a loan.

Mr. CAPLAN. Actually, no reason.

Senator LEVIN. I say they don't want to show it as debt.

Mr. CAPLAN. That's fine. Debt——

Senator LEVIN. Why do you——

Mr. CAPLAN. They do not—they wanted to show it as price risk management liability and not as debt.

Ms. HENDRICKS. Not as funded debt, correct.

Mr. CAPLAN. Not as funded debt.

Senator LEVIN. Now, you say in your testimony today that price risk management liability is a liability, plain and simple. It must be satisfied every bit as much as debt. And thus, while not recorded as debt, prepaid liabilities were clearly obligations of the company and visible as such to investors.

Every witness on our second panel—Moody's, Standard & Poor's, Mr. Turner—disagreed with your statement. Were you here when they disagreed with that?

Mr. CAPLAN. I was not.

Senator LEVIN. Did you hear that? Were you watching or do you——

Mr. CAPLAN. Yes, some of it.

Senator LEVIN. Mr. Turner, former chief accountant at SEC, said it was clearly wrong, your statement, that there is a huge difference between showing something as debt and showing something as price risk management liability.

Who supports your position? Has your accountant told you that there is no difference between showing something as price risk management liability and showing it as debt? Have you been informed of that by somebody?

Mr. CAPLAN. Well, again, I think this is a—it's an accounting question and——

Senator LEVIN. Has your accountant told you there is no difference?

Mr. CAPLAN. Well, I think that a liability is a—it's an obligation to repay. I think that's a legal definition, not an accounting concept. But the accounting concept here was—if the books of Enron didn't properly reflect what their true debt was, then I think that's a matter you have to take up with their accountants and not with their bankers. We don't have control——

Senator LEVIN. But you are the one who said there is no difference whether it is shown as debt or whether it is shown as price risk management. You are making that statement.

Mr. CAPLAN. Yes.

Senator LEVIN. Now you are telling me take that up with their auditors, with Enron's auditors.

Mr. CAPLAN. I'm making the statement that a liability is a legal obligation. I'm not making a qualitative statement as to where something should appear on a company's balance sheet. That is not within the purview or the role or the responsibility of a bank. That is between a company and its auditors.

Senator LEVIN. Mr. Bushnell, do you agree that it makes no difference if an obligation is shown as price risk management liability or as debt, that a liability is a liability?

Mr. BUSHNELL. I think——

Senator LEVIN. Do you agree with that statement?

Mr. BUSHNELL. I think that in the bankruptcy situation that Enron is now in, there are many people that are in the same position——

Senator LEVIN. I am not talking about a—I am not talking about that. I am talking about before the bankruptcy, before that happened. Do you agree that a liability is a liability, it doesn't make any difference, it has to be satisfied whether it is debt or price risk management? Do you agree with that? Is that Chase's position? Excuse me. Is that Citibank's position?

Mr. BUSHNELL. Citibank's position is—from a credit aspect is there are many different types of liabilities, and the correct accounting classification is important for us to understand the nature of the credit.

Senator LEVIN. So it does make a difference where it shows?

Mr. BUSHNELL. What the correct accounting aspect is, yes.

Senator LEVIN. Right. So the issue then is not—as Mr. Caplan has said, look, it was shown in their books—that is his testimony here—that it was reflected in their books, that it was disclosed in Enron's books, and a liability is a liability, plain and simple, that has to be satisfied. Price risk management liability has to be satisfied every bit as much as debt. While not recorded as debt, prepay liabilities were clearly obligations of the company and visible as such to investors. We had the former chief accountant of the SEC saying he couldn't disagree with the statement more. Mr. Caplan, representing Citibank, has made that statement.

Mr. BUSHNELL. I don't think Mr. Caplan's statement is inconsistent at all. I think what he was trying to——

Senator LEVIN. Inconsistent with what?

Mr. BUSHNELL. Inconsistent with what I just said, Senator.

Senator LEVIN. Is it Citibank's position?

Mr. BUSHNELL. Is that the correct classification of a liability is an accounting concern, and that classification differential is important.

Senator LEVIN. And it matters.

Mr. BUSHNELL. And it matters.

Senator LEVIN. And if it is buried somewhere in the financial statement under a false label, that matters?

Mr. BUSHNELL. If the accounting for it was certified by its board of directors, its chief financial officer, and its independent accounting firm, that would make a difference.

Senator LEVIN. But if it is buried somewhere under a false label, that would matter, wouldn't it?

Mr. BUSHNELL. It would matter what the classification of that is, yes.

Senator LEVIN. It would make a difference. It would be significant. It is important, then, as to whether or not it is put in the proper category, that an obligation isn't an obligation, that there are——

Mr. BUSHNELL. That all——

Senator LEVIN [continuing]. Different obligations——

Mr. BUSHNELL [continuing]. Items on the balance sheet, Senator, both the assets and liability, are put in their correct accounting structure is important for fundamental analysis, yes. We rely on accounting firms and boards of directors and the management of companies to put those assets and liabilities in the correct positions in the balance sheet, both on the asset side and the liability side. That is their responsibility.

Senator LEVIN. It is also your responsibility, it seems to me, not to participate in a deception. Would you agree that that is the bank's responsibility? I know you are not going to agree you did participate in a deception. I am sure you are not going to agree with that.

Mr. BUSHNELL. That's correct.

Senator LEVIN. But would you agree that you have a responsibility not to participate in a deception?

Mr. BUSHNELL. We have a responsibility to our clients, both investors and to the customers who need capital, to do things in accordance with the rules as they're established. And the rules that were established, whether they are tax rules, whether they are accounting rules, whether they're regulations for commodity trading or banking, yes, we have an obligation to stay within those rules. And we let the experts who determine what those rules should be as well as interpret exactly what they are do that.

Senator LEVIN. I am really surprised that you can't answer that question with a yes, that you have an obligation not to participate in a deception. It seems to me that is an easy one, that that one doesn't have to be hedged.

Mr. BUSHNELL. I thought that's what I answered, Senator. I think the answer is yes in a more English verbiage or—it depends on what the definition of a deception is.

Senator LEVIN. Any way you want to define it. You can define it any way you want. Don't you think that the bank has an obligation not to participate in a deception? You define deception.

Mr. BUSHNELL. Yes.

Ms. HENDRICKS. Senator, might I add something to that discussion?

Senator LEVIN. Sure.

Ms. HENDRICKS. I did listen this morning to the presentation on the expert panel, and I for one was a little surprised at the testimony in the context that I have in front of me—a report that was written by Moody's in 1998 that refers to under risks and weaknesses of the credit, significant off-balance sheet liabilities, including $1.3 billion in guarantees, $1.4 billion in transportation agreements, and $4.4 billion invested in projects of unconsolidated subsidiaries globally add significant leverage to Enron's capital position.

This is a direct lift from footnotes of Enron's financial statements, and had Lynn Turner read the financial statements which he said he did, he would obviously have seen this. And I would posit that $1.3 billion in guarantees, while not listed as funded debt, certainly is a liability of the company that one would take into consideration in thinking about its overall financial obligations. And I think that's the distinction that we're trying to draw, is that as specifically determined under accounting that it is not listed, in fact, unlike price risk management assets and liabilities, it's not on the balance sheet. It's in the footnotes, which arguably are an integral part of the balance sheet.

But I do think that there is perhaps—there was perhaps some overstatement with respect to the issues this morning.

Senator LEVIN. Take a look at Exhibit 157,[1] if you would please. This is an Enron document. In the middle of it, it says, "The Citibank swap combined with the Enron credit link notes provides for a unique black box feature which provides considerable flexibility for substitution." Two dots down, "Black box allows Enron the ability to provide a permanent takeout feature for highly structured transactions in the capital markets while limiting disclosure of prepay to Citibank."

And then on the next page, at the bottom, "The use of prepays as a monetization tool is a sensitive topic for both the rating agencies and bank institutional investors. The ability to continue minimizing disclosure will be compromised if transactions continue to be syndicated."

Do you believe that is a legitimate purpose—to minimize disclosure? Were you aware that that was Enron's purpose? Anyone.

Ms. HENDRICKS. I'll take that. I think I would say a couple of things. One, this is obviously not a document that we prepared and prior to the preparation for this meeting had not seen, or at least I have not seen.

This is the first that I've heard about use of prepays as a monetization tool being a sensitive topic. Quite the contrary, again, in that report that I just referenced by Moody's in December 1998, there is, if not a specific reference to prepays, a definition of prepays in there and an acknowledgment that the company was doing that.

Further, we had been told by Enron that the agencies were supportive of their monetization of their price risk trading book, provided that the book was either in balance or in a net asset long position and, therefore, were not aware of this comment about it being a sensitive topic, etc.

Senator LEVIN. Were you aware—I would like to just move on a little more quickly. Were you aware of the fact that Enron did not wish to have to explain the details of any of the assets to investors or rating agencies?

Ms. HENDRICKS. The assets of the trust?

Senator LEVIN. Yes.

Mr. CAPLAN. That was the primary purpose of the transaction.

Ms. HENDRICKS. Yes, absolutely.

Senator LEVIN. So you were aware of that.

[1] Exhibit No. 157 appears in the Appendix on page 562.

Mr. CAPLAN. Yes.

Ms. HENDRICKS. Absolutely.

Senator LEVIN. And Citi was aware that that lack of disclosure was a fundamental goal of the Yosemite structure?

Ms. HENDRICKS. Absolutely.

Mr. CAPLAN. It wasn't—let me just correct——

Senator LEVIN. I am not saying you are agreeing that it was improper. I am just saying you agree that that was a purpose of that structure.

Mr. CAPLAN. Right. The disclosure in Yosemite made clear that investors would not learn about the credit risks that were being hedged through the transaction.

Senator LEVIN. You then began to tout the black box feature, did you not, Exhibit 158?[1] Take a look at it. This is, I believe, is page 33. This is a Citibank document where you are now trying to sell the feature of this kind of structure, SPV investments purchased by the SPV are unknown to the investors and the rating agencies.

Mr. CAPLAN. We were very successful in marketing the Yosemite deal to investors, so we tried to duplicate the concept with other capital-intensive borrowers such as Enron, because we thought the concept had a lot of merit, the concept of moving credit risk, but leaving other risks in the bank market, so yes.

Senator LEVIN. All right. But also selling—that one of the benefits of the structure is to mask what was being done with the funds. You touted that as one of the benefits.

Mr. CAPLAN. It wasn't so much mask. It was provide flexibility in the bank market, effectively.

Senator LEVIN. Unknown to the investors, right?

Mr. CAPLAN. Yes, but that's consistent with the disclosure——

Senator LEVIN. I am not saying it is not consistent. That is what masking means. You keep it hidden.

Mr. CAPLAN. It's consistent with the disclosure in the Yosemite offering document that investors would not know the trust investments. We were effectively just duplicating that concept for other borrowers.

Senator LEVIN. How many companies used this same structure after you made a pitch to them? Do you know?

Mr. CAPLAN. We did one structure like this with one company, but it was primarily done in the bank market.

Senator LEVIN. So you didn't sell any structures similar to Yosemite?

Mr. CAPLAN. In the Rule 144A market we did not.

Senator LEVIN. OK. Let me check with Mr. Reilly on Project Roosevelt. You talked about this before. This consisted of two prepays, $310 million natural gas prepay and $190 million oil prepay. The purpose was to supply Enron with $500 million in cash at year end because another financing deal fell through. According to the memos that you wrote, although this transaction was written up as a 3-year deal, it was Enron's intention to repay the $500 million by May 1, 1999, Citibank held off syndicating the $500 million loan that it made to Enron with the expectation that it would be repaid

[1] Exhibit No. 158 appears in the Appendix on page 564.

by May 1, and the prepaid oil and gas deliveries were also delayed until after the expected repayment date.

Now I would like you to look at Exhibit 162.[1] It is a memo you wrote on April 19, 1999, reporting that Enron indicated it could not repay all the $500 million by May 1. It asked if it could pay off the $310 million gas prepay by May 1 and delay repayment of the $190 million oil prepay until November or December. It asked you to hold off syndicating the $190 million until after the new repayment date and characterized it as a favor.

You allowed Enron to defer repayment of $125 million until September 30, and you delayed syndication of the loan and deliveries of the oil until after the September 30 repayment date.

So now Project Roosevelt is billed as to commodity prepays. Enron promised that it would repay the money within 5 months. You held off syndicating the loan and scheduling deliveries until after the expected repayment. Enron asks to delay the repayment of some of the funds. You push back the syndication and delivery dates.

So far am I OK?

Mr. REILLY. Generally, yes, Senator.

Senator LEVIN. OK. Now, it sounds to me more like a short-term loan than a commodity deal. You keep pushing back the delivery date until after full repayment is scheduled to be made, and let's take a look here. I quoted from Exhibit 162, so we will move on to Exhibit 144.[2]

OK. We are on Exhibit 144. This is the initial loan approval memo for this transaction, and it gives us some insight as to what is really going on.

Under the subheading "Story" on page 7—or it is not page 7, but it is Item 7—it reads the following: "The prepaid forward structure will allow Enron to raise funds without classifying the proceeds from this transaction as debt (it is accounted for as 'deferred income'). This is a common method of raising non-debt financing among energy companies." So it was very clear to you that this prepay forward structure will allow Enron to raise funds without classifying the proceeds from this transaction as debt. Right?

Mr. REILLY. That is correct, Senator.

Senator LEVIN. OK. Now, Exhibit 164,[3] the loan approval memo for the extension notes,"The company has verbally agreed to repay the remaining $125 million by September 30, 1999." However, in another memo, which is Exhibit 163,[4] you write the following: "Although they have agreed to prepay by 9/30, the papers cannot stipulate that as it would require recategorizing the prepaid as simple debt." Our records cannot reflect what they've agreed to. That is very clear. Your records cannot stipulate that they have agreed to prepay by 9/30.

Mr. REILLY. Senator, I——

Senator LEVIN. That's your words, isn't it?

Mr. REILLY. Yes, those are the words, but if I might, I think as I referred to in the opening, my opening statement, that "agree-

[1] Exhibit No. 162 appears in the Appendix on page 584.
[2] Exhibit No. 144 appears in the Appendix on page 513.
[3] Exhibit No. 164 appears in the Appendix on page 588.
[4] Exhibit No. 163 appears in the Appendix on page 586.

ment" is probably—is a word that could mean different things, but in this particular case, there had been discussions with the client about the likelihood that they would repay the transaction or prepay the transaction before it ran the full term.

Having said that, the transaction was structured to go to full term, and in the intervening period between the initial closing of the Roosevelt transaction and when we were getting to the point of dealing with the syndication, potential syndication of the transaction, Enron had also begun the process that ultimately became the Yosemite transaction, which then gave other opportunities, other ways that structured transactions—may or may not have been a prepay, but structured transactions might have been funded.

So I think what we had was a statement of intention on the part of the company, but not in any way a binding agreement on the part of the company, and I think, as evidence of that, they did not prepay the transaction along those schedules.

Senator LEVIN. Twice you used the term "agreement." You are saying both times you were inaccurate.

Mr. REILLY. I would say that no one that read that—I did not intend that to mean that it was a binding agreement, and no one in my institution felt that a binding agreement had been made.

Senator LEVIN. That is not the issue. They agreed to something. But you said you cannot be much more explicit than this. This is contemporaneous. The papers cannot stipulate that. That is very explicit. This is not some casual comment. You write down here, "They've agreed to prepay by 9/30, but the papers cannot stipulate that." How much more precise can you be here, folks? You are saying those papers have got to keep that oral. It is an oral agreement. For God's sake, you cannot make a record of that. Why? It would require recategorizing the prepaid as simple debt. Now we talk about participation of the bank.

Mr. REILLY. No, I——

Senator LEVIN. Oh, yes. Now we are talking about your role because your papers—the papers here cannot reflect the reality, which was an agreement. It has got to be kept oral. It cannot show in the papers why that would be debt. That is what Enron did not want, debt reflected on their books. You cannot tell me it makes no difference how obligations are described in books. There is no way you can persuade anybody of that. They were fighting, struggling to make sure debt did not appear on their books. They went through all kinds of contortions and other companies went along with them, using offshore items, companies' entities to filter through money that were not real entities at all, controlled by, you do not know if you did or not. The record is pretty clear. But you go through all these contortions. They went through all these contortions to avoid debt being shown on their books for one very clear reason, it would hurt their credit rating, hurt their stock price, and now your bank, in a very specific clear way, in your words, the papers cannot stipulate that they have agreed to what they have agreed to orally. Why? It would require recategorizing the prepaid as simple debt.

What can be clearer than that?

Mr. REILLY. Senator, I think if you took all of the papers, emails, approval memos throughout the life of the Roosevelt transaction, which was really from December 1998 until near the end of the year in 1999, I think that there are—when that is discussed, it is discussed in some cases as an intention, in some cases as an expectation. In the two references you've made to what I've said, it does say agreement. There was no—I am telling you again, there was no agreement in any——

Senator LEVIN. No oral agreement?

Mr. REILLY. No contractual sense, no agreement, no——

Senator LEVIN. No oral agreement?

Mr. REILLY. No, there was no commitment on the part of the company to repay those loans, none.

Senator LEVIN. Was there an oral agreement?

Mr. REILLY. No, there was not.

Senator LEVIN. You said there was.

Mr. REILLY. I understand that.

Senator LEVIN. You lied in this memo.

Mr. REILLY. No, I don't believe I did. I believe that—I believe that——

Senator LEVIN. Says there was an oral agreement.

Mr. REILLY. I believe what I said in the agreement, which was understood by the individuals who are the recipients of that agreement, was telling them that they would—that it was likely that the transaction would be repaid.

Senator LEVIN. It did not say "likely." I want to read you your words. These are your words at the time. "The company has verbally agreed to repay the remaining $125 million by September 30." They verbally agreed. I said, "Did they orally agree?" You said, "No." Your memo says they did. Which is true?

Mr. REILLY. They did not.

Senator LEVIN. The memo is wrong?

Mr. REILLY. The memo was wrong.

Senator LEVIN. A contemporaneous memo that you wrote at that time was in error, and then the second memo, 4/28/99, is also in error; is that correct, that they have agreed to prepay by 9/30; that is wrong?

Mr. REILLY. It is the same situation. What they have said is that they would—their intention was to repay, prepay. Sorry.

Senator LEVIN. Who are you telling that they made this agreement? Who are you representing that to in the bank?

Mr. REILLY. That list of people that are on this.

Senator LEVIN. Why would you tell them that there was an agreement if there was not?

Mr. REILLY. Again, Senator, I believe that those individuals do not—did not believe that that was a binding contract on the part of the company to make prepayments.

Senator LEVIN. If you would take a look at Exhibit 165.[1] OK, about the fifth line down. We have—let us start at the top. It is from you. "We have agreed the following with Enron: On 5/1 Enron will prepay the $310 million natural gas portion. The $190 million oil portion will remain outstanding. Deliveries scheduled for May/

[1] Exhibit No. 165 appears in the Appendix on page 591.

June/July/August/September will be rescheduled to sometime after 10/1—there will, therefore, be no amortization until after 9–30. They have agreed to prepay that amount no later than 9/30. The paperwork cannot reflect their agreement to repay the $190 million as it would unfavorably alter the accounting."

What can be clearer? How many more times do I have to read your own words to you in different memos?

Mr. REILLY. Senator, I will say the same thing again.

Senator LEVIN. I expect you would.

Mr. REILLY. And that——

Senator LEVIN. "The paperwork cannot reflect their agreement to repay the $190 million as it would unfavorably alter the accounting." Whose accounting?

Mr. REILLY. Enron's.

Senator LEVIN. It would have to show as a debt, would it not?

Mr. REILLY. Well, Senator, this—the Roosevelt——

Senator LEVIN. If there was an agreement, it would have to show as a debt, would it not?

Mr. REILLY. Senator, if the—I think we've acknowledged here both generically structured finance and Enron specifically did in fact undertake transactions in which they could categorize capital raising as non-debt, whether it be prepaids or the like. So there's no reason to back away from that.

It's also mentioned in other emails that their intention, should they prepay, was to refinance it with other commodity-based transactions, which I think sticks with the same line of intent that they had when they closed this deal in December 1998.

Senator LEVIN. Now, let me ask my question again. If there were an agreement to repay to $190 million, it would result in their being required to list this as a debt, would it not?

Mr. REILLY. I believe that if we had redone the documents and required it to be paid on a given day, because it was a physical delivery prepay, that you simply couldn't meet that physical delivery schedule on any 1 day.

Mr. CAPLAN. Senator, I would add——

Senator LEVIN. That is not responsive.

Mr. REILLY. I'm sorry. I'll try——

Senator LEVIN. I am asking a fairly direct question. If there was an agreement to pay that money to you by that fixed date of September 30, that would have required them to account for this as a loan, would it not?

Mr. REILLY. If there had been an amendment to the document so that there was a binding contractual agreement, I understood from the company that that could recategorize the transaction.

Senator LEVIN. As a——

Mr. REILLY. As debt.

Senator LEVIN. Debt. Hard to get that word out of your testimony here, but we are going to keep getting it. You can fuzz it up. You can put words around it, but my question is so direct, and your answer tends to be so indirect. And I do not know—I think I know why, but you ought to be straightforward here. You have said it in your own words. If this is shown as a specific date to repay this, then it would change their accounting and they would have to show

it as a debt. And you knew that. Is that correct? If the documents were rechanged——

Mr. REILLY. Senator——

Senator LEVIN. I got all that.

Mr. REILLY. Can I go back and just read——

Senator LEVIN. No, I do not think so. I want to go on to the next question. I do not want to go backward. I want to go forward here. I am going to just try one more time, because it seems to me it is so clear what I am asking.

If the documents reflected an agreement on the part of Enron to pay that money back to Citibank by that specific date, Enron would have been required to show that as a debt on their books; is that not true?

Mr. REILLY. I believe that is true, although that particular accounting judgment was not mine. That was what I understood from the——

Senator LEVIN. And that is what you wrote in this memo, this email, did you not?

Mr. REILLY. Yes.

Senator LEVIN. That is something that you worked with them to avoid, did you not? You left that agreement out of those documents, did you not?

Mr. REILLY. Senator, again, there was no agreement.

Senator LEVIN. I understand.

Mr. CAPLAN. Senator, could I add something to clarify this maybe a little bit?

Senator LEVIN. Yes. Well, yes, try to clarify it. Not if it is going to "fuzzify" it.

Mr. CAPLAN. I'll try not to "fuzzify" it. September 30 comes along, there is no repayment of this transaction. So, one, if there was a real agreement to repay it, then they breached that agreement, and we did not do anything about that. And usually on multimillion dollar transactions, if companies breach their agreement, we tend to do something about it.

Also I would add that there are other discussions of other types of agreement around this transaction such as syndication strategy and what the "agreement" with the company is on that. But you won't find anything in the documents on a syndication strategy, because I think the word "agreement" is being used very loosely here, and I think why my colleague, Mr. Reilly, is struggling, is that there wasn't—if you went to the company, they would tell you they were not agreeing to do anything. They were telling—they were expressing an intention which got us comfortable in making a credit decision, but that intention was not—did not rise to the level of an obligation. And I think that is kind of the basic difference, and I think it is unfortunate that Mr. Reilly used the word "agreement," but I don't think that's supported by the facts surrounding the transaction.

Senator LEVIN. When they did not pay by that fixed date, was there a understanding that they could pay by a later date? Was there any conversation about them paying at a——

Mr. CAPLAN. I was not privy to those conversations.

Senator LEVIN. Who is? Mr. Reilly, are you privy as to what happened when they did not pay by the date they said they would pay it by?

Mr. REILLY. They did not.

Senator LEVIN. And then there was an understanding, representation, whatever word you want?

Mr. REILLY. Ultimately that—ultimately.

Senator LEVIN. But they said they would pay it by another time, right, in another way?

Mr. REILLY. Well, I think—I'm not sure exactly what you're referring to, but I believe——

Senator LEVIN. What happened on that date when they did not pay it? Was there not an understanding at that point as to how and when they would pay it?

Mr. REILLY. Well, we kept the existing transaction documents in place. We did change the amortization schedule, and it was the understanding of the parties that Roosevelt transaction would likely be retired to the proceeds from the first Yosemite transaction.

Senator LEVIN. That was the understanding, not the agreement, the understanding?

Mr. REILLY. That's correct, Senator.

Mr. CAPLAN. I think our credit approval——

Senator LEVIN. There is no difference between——

Mr. CAPLAN. Our credit approval indicates that we had approved the transaction for the full tenor of the transaction which is very typical in derivative transactions, and in many instances counterparties early terminate those kind of transactions. So our credit approval didn't indicate that this was a shorter transaction in any way based on Mr. Reilly's communications.

Senator LEVIN. Did Citibank represent to the sureties that it expected real commodity deliveries?

Mr. REILLY. I never had a conversation with the sureties.

Senator LEVIN. Who would know most about that? Who had conversation with the sureties, anybody here?

Mr. CAPLAN. I was not involved in that transaction.

Senator LEVIN. Mr. Bushnell.

Mr. BUSHNELL. I did not.

Senator LEVIN. Ms. Hendricks.

Ms. HENDRICKS. No, sir.

Senator LEVIN. Let us see. Why do I not yield to my colleague, Senator Fitzgerald? I have more questions, but let us go back and forth.

Senator FITZGERALD. All right. Thank you very much.

Ms. Hendricks, my understanding is that you were the Citibank/Salomon Smith Barney investment banker that was in charge of the Yosemite transactions; is that correct?

Ms. HENDRICKS. Yes, I was the Salomon Smith Barney investment banker, sir.

Senator FITZGERALD. And is it correct that on September 9, 1999, you had to make a presentation to the Investment Grade Commitment Committee of the bank in New York regarding some of Enron's obligations, specifically regarding Project Condor; is that correct?

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. Now, you made the presentation on September 8. Robert Rubin was present for that presentation; is that not correct, according to the minutes of the meeting?

Mr. BUSHNELL. Excuse me, Senator, if I could clarify. We have two Robert Rubins at Citigroup. The Robert Rubin that this was referring to was a Senior Managing Director in the Salomon Smith Barney entity. He had come from Shearson Lehman. He sat on our Capital Commitments Committee. That's not the Robert Rubin that was Treasury Secretary.

Senator FITZGERALD. So that is not the Mr. Rubin we were talking about before?

Ms. HENDRICKS. No, Senator.

Senator FITZGERALD. It is another Robert Rubin. You made a presentation to that Investment Grade Commitment Committee, is that correct, on September 8, 1999?

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. Did they ask you to do a follow-up report to them?

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. And why did they ask you to do a follow-up report?

Ms. HENDRICKS. As part and parcel of the discussion that we had related to this transaction, there were a number of questions from the Subcommittee, which is an extremely rigorous investigative body prior to any transaction that we do, about the amount of disclosure in Enron's public financial statements. And I was specifically asked that if one included—and I believe the question that was asked of me was off-balance sheet debt, but that was a catch-all term for basically all of the liabilities that we could think of.

Senator FITZGERALD. That were off-balance sheet, that were not in their public financials; is that——

Ms. HENDRICKS. Well, frankly, that were in footnotes, OK? So whether or not you categorize that as off-balance sheet, whether or not you categorize certain things that might be listed as non-debt, as debt items, etc., the question that was asked of me is if you included all of those items, is this still an investment grade company?

Senator FITZGERALD. And what is the debt to equity ratio?

Ms. HENDRICKS. No. I was not asked that question. I was asked the question, is this still an investment grade company?

Senator FITZGERALD. And how do you determine if it is?

Ms. HENDRICKS. My approach was to go back with my team and say, all right, we don't have a lot of time here. Let's do the most rigorous, most punitive, in terms of including everything we can think of, analysis that we possibly can of the company's overall leverage.

Senator FITZGERALD. And what did you come up with? Is that not the exhibit that is Exhibit 166?[1] Is that not the report that you prepared in response to——

Ms. HENDRICKS. That is correct, Senator.

Senator FITZGERALD [continuing]. The Investment Grade Commitment Committee's request?

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[1] Exhibit No. 166 appears in the Appendix on page 592.

Ms. HENDRICKS. That is correct, Senator.

Senator FITZGERALD. And you found that Enron, on a GAAP basis, what they totally reported was total debt of $12,056,000,000; is that correct? That would be on the second page of your report dated September 20, 1999; is that correct?

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. And then you found that Moody's was aware of additional off-balance sheet items, such as $4.4 billion in investments in unconsolidated subsidiaries, off-balance sheet guarantees of $1.3 billion, transportation commitments of $1.4 billion for a total of $5.7 billion?

Ms. HENDRICKS. Yes, and that's a mathematical mistake. That should be $7.7 billion, I believe.

Senator FITZGERALD. That should be $7.7 billion, OK. And then beneath, where you put that——

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. Seven point one billion dollars in additional off-balance sheet liabilities——

Ms. HENDRICKS. Disclosed in their footnotes, yes, sir.

Senator FITZGERALD. And that Moody's was aware of?

Ms. HENDRICKS. Correct, in the report that I mentioned earlier.

Senator FITZGERALD. And while the publicly-reported financials show a GAAP debt to capitalization ratio of 49 percent, you calculate that the GAAP debt plus Moody's off-balance sheet liabilities was 56 percent; is that correct?

Ms. HENDRICKS. Yes, and that's an error. Using the $7.1 billion, it should be 60 percent.

Senator FITZGERALD. Sixty percent, OK. Then you came up—if you have this document here, on this next page—I want to hold this up so we are carefully talking about the same document here. There is a document that says, "SSB." I suppose that is Salomon Smith Barney—"Additional Known Structures"—so these are additional structures you knew of—"other off-balance sheet items," and you come up with an additional $6 billion in off-balance sheet liabilities; is that correct?

Ms. HENDRICKS. That's what's on this page, yes, sir.

Senator FITZGERALD. Is the math on this page correct?

Ms. HENDRICKS. The math on this page is correct.

Senator FITZGERALD. And then you have a little line here of GAAP debt plus Moody's liabilities, plus the Salomon Smith Barney known structures, brings the debt to equity ratio to 65 percent; is that correct?

Ms. HENDRICKS. That is correct.

Senator FITZGERALD. So you were aware that really their debt level was higher than would appear in their publicly-available financial reports as of the date of this report, September 20; is that correct?

Ms. HENDRICKS. Well, Senator, if I might, on that sheet that you just held up, if you look further in your materials, you'll see that we provided the Subcommittee with a list of those assets that we feared at the time, but could not—were not absolutely certain, we were double counting. We threw them in because we wanted to be as punitive as possible, but we recognized that we were being negatively sloppy in our analysis. And so a number of those items—and

frankly, we were sloppy not only in the calculation that I've just admitted to, but also in our terminology, when we call that SSB additional known structures.

Senator FITZGERALD. But you were aware that there were significant substantial off-balance sheet liabilities that were out there that Moody's did not necessarily know about and that were not necessarily self-evident from the publicly available financial statements filed by Enron; is that correct?

Ms. HENDRICKS. Senator, the answer to that question is no, because I did this calculation to be as negative as I could, not to demonstrate that I knew things that weren't in the information. As a consequence of that, I knew we were double counting, and I subsequently then——

Senator FITZGERALD. Were you double counting—was everything double counted or just a few items on there double counted?

Ms. HENDRICKS. Most of the items were double counted. I think if you look in your exhibits at—if you continue on in that same exhibit, Exhibit 165.[1] If you keep turning pages, you'll get to the part—that same chart, where it lists the double-count.

Senator FITZGERALD. I, maybe, see that you are saying about $3 billion of the additional $6 billion is double counted.

Ms. HENDRICKS. It turns out that leases as well are on the balance sheet, or actually picked up in the Moody's report I believe. So there were a number of items here. I think the principal item that is on the balance sheet is the——

Senator FITZGERALD. When did you realize you had double counted?

Ms. HENDRICKS. I knew it when I was doing the calculation, but I couldn't be certain, and so after we prepared this analysis and I was able to demonstrate that this was still an investment grade company, which is the next page of this presentation, which was the whole purpose of doing the presentation, was to get to this final page, and to be able to demonstrate that even throwing in things that I knew to be double counting, even though I couldn't precisely give you the numbers, which I subsequently did. I subsequently went back and said, OK, the Marlin financing is in Note 9, and the Firefly financing is electro and that's Note 9, and the Sutton Bridge financing is a Rule 144A Euro bond and that is in the public domain.

When I was subsequently able to go back and get that specific data, we absolutely corrected the information. But at the time my objective was not to be accurate. My objective was to be as conservative as I conceivably could be, and to demonstrate first to my own satisfaction and second to the Subcommittee's satisfaction, that this was still an investment grade company. And that is what the final page of this presentation demonstrates to me and to my satisfaction at the time.

When I subsequently was able to go back——

Senator LEVIN. What page are you looking at?

Ms. HENDRICKS. I'm sorry, sir. If you go to the last page——

Senator LEVIN. Just the number at the bottom.

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[1] Exhibit No. 166 appears in the Appendix on page 592.

Ms. HENDRICKS. Down at the bottom, page 4, comparable companies, the last page of that exhibit.

Senator LEVIN. OK, thank you.

Ms. HENDRICKS. What we did was to say here are companies that are in the same industry that are subjected—financing themselves in the same way. And, Senator, the reason I derive so much comfort from this presentation was because I did not adjust these other companies's numbers of any form of off-balance sheet activity.

Senator FITZGERALD. I am looking at comparable companies. This is document CITISPSI 0031098.

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. Here you are just disclosing the GAAP indebtedness. It says, "The following is a review of the GAAP debt capital ratio of certain comparable companies." And then you have Enron listed, and it seems like here you have backed out the off-balance sheet liabilities.

Ms. HENDRICKS. No, sir. This is the——

Senator FITZGERALD. Well, how do you come up with a debt to equity ratio of 48.7 percent here?

Ms. HENDRICKS. Because all of these are debt-to-cap. When you look at AES Corp, when you look at Sonat, for this to be apples to apples on this page, I showed Enron's number. But on the prior page and on the previous page——

Senator FITZGERALD. Yes, but you are aware of substantial off-balance sheet liabilities of Enron, which you have just demonstrated in the prior pages.

Ms. HENDRICKS. They were disclosed in the footnotes to the financial statements.

Senator FITZGERALD. All of those liabilities?

Ms. HENDRICKS. No. Maybe, I'm obviously not being clear.

Senator FITZGERALD. I see what you are saying, that you know that the publicly reported GAAP debt to capital ratio of AES Corp was 78 percent.

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. And that does not make reference to any off-balance sheet liabilities that company may have.

Ms. HENDRICKS. Correct.

Senator FITZGERALD. I understand that. But are you saying the only thing that is relevant to determine whether a company is investment grade are its GAAP basis liabilities, and that all of those off-balance sheet obligations are irrelevant in deciding whether it is investment grade?

Ms. HENDRICKS. Senator, what I'm saying is the question that you asked me first was do I recall this presentation and what was I asked in the presentation, and what was the purpose of my response presentation. I was asked if including the off-balance sheet—loose language—liabilities of this company would still—if we included those, would the company still be an investment grade credit.

This is the analysis that I did and this is the analysis that I sent to the Chairman of the Subcommittee, and subsequently had either a telephone or over-lunch conversation. I mean I don't think it was an actual presentation where I went back to the committee with

the material, but it was a discussion in which I said we have done an incredible stress testing.

Senator FITZGERALD. So you persuaded the committee that this was an investment grade company, that Enron was, and you should go forward with the public offering or the Rule 144A sale of securities?

Ms. HENDRICKS. Yes, Senator.

Senator FITZGERALD. Did anybody question you on that?

Ms. HENDRICKS. No, Senator, and what I represented was that we would, from this point forward, do a thoroughly rigorous analysis, which we did in each subsequent Commitment Committee presentation.

Senator FITZGERALD. Was your compensation in any way tied to how many deals you brought in and persuaded the company to underwrite?

Ms. HENDRICKS. No. In any direct way, no. We're not paid on a commission basis. My compensation, as the global head of the group, was primarily a function of the global revenues of the firm of which Enron was less than 10 percent.

Senator FITZGERALD. So if you did not generate any business all year, it would not really affect your compensation?

Ms. HENDRICKS. No, I wouldn't say that. I would think they might question whether or not I should still be the head of the group.

Senator FITZGERALD. Can it not be said that they expect you to generate some deals?

Ms. HENDRICKS. Absolutely, sir.

Senator FITZGERALD. You try to generate deals for the bank, right?

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. But at the same time you do not want your firm to underwrite something it should not.

Ms. HENDRICKS. Senator, in my belief, there is no level of fee compensation that justifies risking the firm's reputation, and there is absolutely no way that we would have done this transaction to do this transaction if we thought there was an issue.

Senator FITZGERALD. Are bankers at Salomon Smith Barney penalized if they sell bad securities to the public that do not get repaid?

Ms. HENDRICKS. In my opinion, absolutely.

Senator FITZGERALD. In your opinion. Is that any part of a written compensation policy for the bankers there?

Ms. HENDRICKS. No, because we do not have written compensation policies, sir.

Senator FITZGERALD. There is nothing written, it is all just—who decides what your compensation is?

Ms. HENDRICKS. My boss.

Senator FITZGERALD. Who is your boss?

Ms. HENDRICKS. At the time, the Global head of the investment bank.

Senator FITZGERALD. And you do not know on what criteria he bases your compensation?

Ms. HENDRICKS. No, sir, I think I have a general idea of the criteria——

Senator FITZGERALD. What are they?

Ms. HENDRICKS. But there is no contractual arrangement.

Senator FITZGERALD. Do you think that they look favorably, when it comes to compensating you, on how many deals you generate?

Ms. HENDRICKS. Yes, and I think they would look very favorably, very unfavorably on me for doing transactions that resulted in either a loss of prestige for the firm or an economic loss.

Senator FITZGERALD. Would you not think this transaction resulted in somewhat of a loss of prestige?

Ms. HENDRICKS. Absolutely.

Senator FITZGERALD. Were you penalized at all in your compensation?

Ms. HENDRICKS. I believe I was, sir, yes.

Senator FITZGERALD. You were. OK. Now, on November 4, this is a supplement to the offering memorandum, dated November 4, 1999, for Yosemite Securities Trust I. When did you actually sell?

Ms. HENDRICKS. I am sorry, Senator. Could you say that one more time for me. I am sorry.

Senator FITZGERALD. This is the prospectus for Yosemite Securities Trust I.

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. For the notes, and I asked you for that before, and lo and behold my staff had one. What was the date that you sold the Yosemite securities, that you actually closed the sale of those notes?

Ms. HENDRICKS. I do not know.

Mr. CAPLAN. It is November 4, 1999.

Senator FITZGERALD. That is the date of this supplement. It says, initially, "Purchasers expect to deliver the securities on or about November 18."

Mr. CAPLAN. Oh, I am sorry.

Senator FITZGERALD. So somewhere around November 18.

Mr. CAPLAN. Sorry. It was November 18th.

Senator FITZGERALD. In this prospectus, you do disclose certain risk factors that you knew of. The underwriter is Salomon Smith Barney; is that correct?

Ms. HENDRICKS. Yes.

Senator FITZGERALD. That is the company you work for, right?

Ms. HENDRICKS. Yes, sir.

Senator FITZGERALD. We have established that Salomon Smith Barney knew of some of the off-balance sheet liabilities by September 1999 of Enron. Did you disclose any of those off-balance sheet liabilities in this offering prospectus?

Ms. HENDRICKS. Senator, I do not mean to quibble with terminology, but it is relevant I think to this discussion. I do not agree that these are off-balance sheet liabilities. That was a sloppy term that we used in our presentation material, but virtually all of the transactions——

Senator FITZGERALD. Was it material information—let me put it that way—what you prepared for the Investment Grade Committee? It was apparently material enough for you to tell your committee before they went forward with it. Was it material——

Ms. HENDRICKS. No, sir, I did not believe that was material nonpublic information for us to disclose to the committee—I mean, to the public.

Senator FITZGERALD. Why were you disclosing it to the committee? If it is not material, why are you wasting their time?

Ms. HENDRICKS. One, because they asked me to, but, two, most importantly, this was a flawed analysis that anyone could have done in reading the financial statements and which I think Lynn Turner referred to this morning in terms of when you read through these financial statements, there are a number of questions that are asked. At the point at which I did the analysis, it was inaccurate, and had we disclosed it, it would have been misleading. Having said that——

Senator FITZGERALD. It was overly conservative.

Ms. HENDRICKS. There was no legal requirement to disclose it, and what we disclosed is what we believe is the legal requirement. As I am sure you know, our underwriting activities are extremely carefully monitored, and we do exactly what it is appropriate for us to do, recognizing that to step outside of those boundaries is to subject both investors and ourselves to risk.

Mr. CAPLAN. And we relied upon experts in determining what the appropriate disclosure in this instance was and received legal opinions consistent with that——

Senator FITZGERALD. Who is your law firm?

Mr. CAPLAN. In this transaction, we actually received two different legal opinions on the securities law issues. One was from Millbank Tweed basically on the Yosemite structure, and then Vinson & Elkins, who is——

Senator FITZGERALD. Vinson & Elkins?

Mr. CAPLAN [continuing]. Who is Enron's legal counsel, as you know, gave a 10b-5 opinion——

Senator FITZGERALD. They opined that your disclosures were sufficient.

Mr. CAPLAN. That the disclosure, the Enron-related disclosure, in particular, was sufficient, as well as received a comfort letter from Enron's accountants that the information incorporated by reference and included in the document was proper.

Senator FITZGERALD. So let me just get this straight. You, Ms. Hendricks, that whole analysis you did for your Investment Commitment Committee, the presentation, dated September 20, where you itemized the off-balance sheet liabilities of Enron Corporation, you do not believe that was material information that someone who might want to invest directly or indirectly in Enron needed to be aware of?

Ms. HENDRICKS. I believe that all of that information was public information, that anyone could have done the analysis that I did, that the liabilities were not off-balance sheet, and that, no, I did not need to disclose it.

Mr. CAPLAN. Which was verified by our experts, effectively.

Senator FITZGERALD. All of that information was disclosed, and so you did not believe it needed to be detailed in any risk-factor statement in your offering memorandum?

Ms. HENDRICKS. No, sir. I know that in this morning's presentation, there was discussion by the staff with respect to require-

ments for supplemental disclosure, but we did not believe that that was appropriate or necessary.

Senator FITZGERALD. So is your position that if it is disclosed in publicly available documents, even if the disclosure is obtuse, you would admit that the disclosure in the footnotes is fairly obtuse with respect to these off-balance sheet liabilities, would you not? Your position is that if it is somewhere in the publicly available reports, even if it is buried in an obscure footnote, that you do not have to further disclose it or highlight it.

Ms. HENDRICKS. Senator, my position is that this was a Rule 144A transaction that was being sold to QIBs, which are the largest, most sophisticated institutional investors in the world and that our obligation here was to incorporate, by reference, which we did, the financial statements of Enron which were audited by a reputable accounting firm at the time and that that was the standard of required disclosure, which we met.

Senator FITZGERALD. Well, I appreciate that. Mr. Chairman, if you want to——

Senator LEVIN. We are going to take a 10-minute recess for the sake of our witnesses, and our staff, and I think ourselves. We will recess for 10 minutes.

[Recess.]

Senator LEVIN. We will come back to order.

I want to pick up where Senator Fitzgerald left off and refer you to Exhibit 168,[1] Page 21. Now this was prepared, as I understand, Ms. Hendricks, by the time you have gotten to Yosemite IV, through all of these transactions involving Yosemite; is that correct?

Ms. HENDRICKS. Is this Yosemite IV, Senator? I am sorry. I just turned right to——

Senator LEVIN. That is OK. If you go back to Exhibit 168.

Ms. HENDRICKS. April 16.

Senator LEVIN. All right.

Ms. HENDRICKS. Yes, sir.

Senator LEVIN. What is this document?

Ms. HENDRICKS. This is the Commitment Committee memorandum that would have been prepared for the Investment Grade Commitment Committee.

Senator LEVIN. This is after Yosemite IV?

Ms. HENDRICKS. No, this would have been——

Senator LEVIN. Just before Yosemite IV?

Ms. HENDRICKS. Prior to, yes. This would have been the approval for Yosemite IV, sir.

Senator LEVIN. So, by now, you have gone through this kind of an assessment as to what the appropriate amount of what previously had been called additional known structures, off-balance sheet items, etc. You have now got to the point where you are about to take up Yosemite IV, right? You have done it for Yosemite I, you have done it for Yosemite II, you have done it for ECLN I, haven't you?

Ms. HENDRICKS. Yes, and this is actually ECLN II. I know that the staff refers to it as Yosemite IV, but——

[1] Exhibit No. 168 appears in the Appendix on page 604.

Senator LEVIN. OK. We will call it either ECLN II or Yosemite IV interchangeably, correct?

Ms. HENDRICKS. Yes, sir.

Senator LEVIN. Now what you have testified to is that these figures appeared in the Enron financial statement; is that correct?

Ms. HENDRICKS. Yes, Senator.

Senator LEVIN. As a matter of fact, and this is the critical question, these items are financings, are they not?

Ms. HENDRICKS. Yes, Senator.

Senator LEVIN. They are.

Ms. HENDRICKS. Yes, Senator.

Senator LEVIN. They appear as financings in the financial statements of Enron?

Ms. HENDRICKS. No, Senator. It would depend on the structure as to how they are accounted for.

Senator LEVIN. My question is did they appear as financing in the financial statements of Enron?

Ms. HENDRICKS. They would have been listed on the balance sheet or in the footnotes as obligations of the company. I am not trying to be difficult, Senator. I am trying to make sure I understand what you are asking.

Senator LEVIN. I thought that they were listed in that big item called price risk management liabilities, were they not?

Ms. HENDRICKS. The prepaids are, yes, sir. Receivable financing, for example, would not have been.

Senator LEVIN. Let us just talk about the prepaids.

Ms. HENDRICKS. OK.

Senator LEVIN. Prepaids were listed in price risk management liabilities; is that correct?

Ms. HENDRICKS. They were included, yes, Senator.

Senator LEVIN. In the Enron financial statements.

Ms. HENDRICKS. In the Enron audited financial statements, yes, Senator.

Senator LEVIN. But you know that they are financings, do you not?

Ms. HENDRICKS. Senator, I know that they have monetized the future cash flows, yes, sir.

Senator LEVIN. You know they are financings, do you not?

Ms. HENDRICKS. Yes, sir.

Senator LEVIN. You use that term all of the time.

Ms. HENDRICKS. Yes, Senator.

Senator LEVIN. They do not appear as financings, do they, in the Enron financial statement?

Ms. HENDRICKS. They appear as liabilities, Senator.

Senator LEVIN. Not as financing.

Ms. HENDRICKS. Senator, I——

Senator LEVIN. Is that not correct? They do not appear as financings in the Enron financial statement; is that correct?

Ms. HENDRICKS. I believe that the generally accepted accounting principles required them to be disclosed, as their auditors told them they had to disclose them; that these are price risk management liabilities of the firm that what——

Senator LEVIN. I am talking here about the prepays.

Ms. HENDRICKS. Yes, of Enron.

Senator LEVIN. They are not financings.

Ms. HENDRICKS. They were structured financings. I mean, they were loans, they were structured financings. You have used different terms——

Senator LEVIN. No, I have not. You told your board that they are financings.

Ms. HENDRICKS. Well, we called them off-balance sheet financings, Senator, and they are not off-balance sheet either.

Senator LEVIN. But they are financings.

Ms. HENDRICKS. Well——

Senator LEVIN. You treat them as financings to your board. You tell them your financings. We have been told all day long by the folks who were trying to defend this stuff that the oil prepaids are financings. That is the argument you have all been using.

Ms. HENDRICKS. Correct.

Senator LEVIN. OK, if they are financings, they do not show up as financings on the Enron financial statement as financings. Do they?

Now that is a very precise question. Do they show up on the Enron financial statement as financings?

Ms. HENDRICKS. Nowhere on the Enron financial statement, that I am aware of, does anything show up as financings.

Senator LEVIN. They show up——

Ms. HENDRICKS. They show up as long-term debt, but not financings.

Senator LEVIN. They do not show up at all as debt or financings, do they?

Ms. HENDRICKS. I am not aware of anything that shows up as financings.

Senator LEVIN. Including oil prepaids.

Ms. HENDRICKS. Including oil prepaids.

Senator LEVIN. So now you believe the oil prepaids are financings. They do not show up on the Enron financial statement as financings; are you with me so far?

Ms. HENDRICKS. I am with you, sir.

Senator LEVIN. But you tell investors that they can rely on the financial statements of Enron which you incorporate by reference in your offering——

Ms. HENDRICKS. Yes, Senator.

Senator LEVIN [continuing]. Even though that financial statement, which you incorporate by reference, leaves off the fact that there are this many prepaids that you treat as financings when you deal with your own board; is that factually correct, what I just said?

Ms. HENDRICKS. No, this is not our board. I am sorry.

Senator LEVIN. Excuse me, to the committee.

Ms. HENDRICKS. OK.

Senator LEVIN. You are right.

Ms. HENDRICKS. There is a difference.

Senator LEVIN. You are right. I am sorry. To the committee that you presented this to, you presented this as a financing; is that correct?

Ms. HENDRICKS. Yes, sir, I presented this as off-balance sheet financings, which is incorrect, but it definitely is presented as specific things that we were aware of, yes.

Senator LEVIN. And you believe it is a financing, do you not, the prepaids?

Ms. HENDRICKS. I believe that it is a structured financing, yes, sir.

Senator LEVIN. You do, the prepaids.

Ms. HENDRICKS. Yes, sir.

Senator LEVIN. But they do not appear on the financial statement of Enron as a financing, do they?

Ms. HENDRICKS. No, sir, they do not. They appear as price risk management liabilities.

Senator LEVIN. And you incorporate that financial statement, by reference, in your offering, do you not?

Ms. HENDRICKS. Yes, sir, we do.

Senator LEVIN. Therefore, you are incorporating something which is not accurate.

Ms. HENDRICKS. I disagree with that, Senator.

Senator LEVIN. You present to your Capital Committee this is a financing. It does not show as a financing on the financial statement that you incorporate, by reference. It shows as something else, something very different, which everyone here has finally acknowledged, which is a risk management liability.

Ms. HENDRICKS. Senator, we disclose, throughout this memorandum to our Commitment Committee, that these transactions are accounted for under generally accepted accounting principles under price risk management and asset liabilities. And when we are asked by them what the business purpose is of engaging in these transactions, we gave the same response that we gave to your Subcommittee earlier this morning with respect to our belief that this was a legitimate business purpose as an attempt to monetize future cash flows.

I also further believe that this type of transaction was described in the report by Moody's in 1998. I think there are references that are made to it in other transactions, but if you are asking me if, specifically——

Senator LEVIN. That is my question, very specifically.

Ms. HENDRICKS. And I gave the answer, no, these are not listed as financings and, no, it would not have been appropriate for us to include them because, under generally accepted accounting principles, they are not financings, and it would have been inappropriate——

Senator LEVIN. Prepaids are not financings.

Ms. HENDRICKS. Under generally acceptable accounting principles——

Mr. CAPLAN. But again, I think that is not even our decision.

Senator LEVIN. I thought that you have been arguing all afternoon that they are financings.

Mr. CAPLAN. We consider them financings because we take credit risk in them.

Senator LEVIN. Good. So that is—yes.

Mr. CAPLAN. However, the accountants are the ones that are charged with disclosing them where they should be disclosed in the

financial statements. So you are asking us to indicate whether we think an accounting principle is right or wrong, and I do not think we are in a position to do that.

Senator LEVIN. No, I am not. I am asking you a simple question. You presented to your committee here these prepays as financing, which you have been arguing they are all afternoon, and they are not shown as financings on the financial statement of Enron, which you incorporate by reference in your offering. Those are factual statements.

Ms. HENDRICKS. Correct.

Senator LEVIN. Mr. Caplan, who were the people at Enron whom you dealt with on the prepays and on the Yosemite structure?

Mr. CAPLAN. Starting, I guess, from the top of the organization, I know that Andy Fastow was aware of them, but I did not have direct dealings with him—Jeff McMahon, Bill Brown, Doug McDowell, Jody Coulter, Barry Schnapper, George McKean, Dan Boyle, I would say those are kind of the primary people—I am sorry, Ben Glisan, a couple of people in Europe, Trease Kirby, and Simon Crowe and Paul Chivers, and one other person in Europe, a woman named Anne Edgley, I would say that is probably the core group of people.

Senator LEVIN. Mr. Bushnell, this is a question for you.

Chase supplied us with tapes of phone conversations related to the prepay transactions. They supplied them because all of the traders calls are taped, and they were under subpoena to produce all documents, including tapes that addressed Enron transactions.

Now Citigroup received a similar subpoena. Your traders apparently are also taped, their phone conversations. Why has Citigroup not produced any tapes to the Subcommittee?

Mr. BUSHNELL. I cannot answer that question in terms of why we might not have responded to that. I believe, Senator, that some of our traders are taped and others are not, but I am not aware of the existence of any tape recordings.

Senator LEVIN. Have you inquired?

Mr. BUSHNELL. I have not.

Senator LEVIN. How would you be aware of them if you have not inquired?

Mr. BUSHNELL. I said I am not aware of the existence of any of the tapes. I have not asked the question, Senator.

Senator LEVIN. Would you do that?

Mr. BUSHNELL. Yes, sir.

Senator LEVIN. We have asked a number of questions which we are going to need answers for, for the record, from both of our last panels. The testimony today and the documents surely paint a very disturbing picture. Enron came to the banks. It had a clear desire to get cash, but to show it not as debt, but as something else—cash flow from operations. The financial institutions provided the structure and the vehicle to create these fake prepaid trades. It attempted to turn debt into cash flow from operations.

The critical third party that was provided were off-shore shell corporations that existed in secrecy jurisdictions solely for, and as the creation of, the investment bank.

Just a little bit like the "Wizard of Oz," when Toto pulls back the curtain to show the great Oz is no more than just an old man rap-

idly manipulating pyrotechnic devices, when you pull back the curtain of off-shore shell companies, it reveals that the banks were calling the shots and pulling the strings. There is no other conclusion that any reasonable person can reach, I believe, that effective control of those two off-shore entities were in the hands of the banks.

This deception was taken a step further when investments were, in the Yosemite Trust, sold to persons relying on an Enron financial statement which did not disclose these prepays and which Citibank incorporated by reference in its offering.

Enron desperately wanted the cash to be booked as prepays, real prepays, they hoped people would believe, but in order for them to be legitimate prepays, there had to be independent parties, the third-party entities could not be controlled by the banks, the trades could not be linked, and the testimony—it is very obvious here today—shows that they were linked. There had to be price risk. Plenty of testimony was that they were all hedged, and there was no price risk. The purchaser of the commodity had to have an ordinary business reason for purchasing it. That surely did not appear with either of these off-shore entities.

So the reality was hidden from credit rating agencies, from the public, from outside investors. I do not believe that Enron could have done what it did in hiding debt and disguising it as cash flow from operations without the assistance and participation of the banks.

All of the documents in the record here are going to be referred, as I indicated, to the SEC and the Department of Justice. We hope that the Sarbanes bill will cure some of the problems here, but I think the problem ultimately has got to be addressed internally by our major institutions. It is a sad day for me, believe me, when two institutions like Citigroup and Chase, come before us and, instead of shedding light on what clearly was the intent here of Enron to turn debt into operational cash coming in, we find the continuation basically of an insistence that nothing was done wrong here, that nobody knew that this was intended to be shown as debt, even though there is no jurisdiction for it—excuse me—it was intended to be shown as operational income, even though there is no jurisdiction for it according to the criteria which we had set out to be shown as anything other than debt.

The answer has got to come not just from additional regulation and laws, although I think they are appropriate, if done sensibly, but the ultimate answer here has got to be given at least significantly by our institutions, our banks, our boards of directors, our corporations. This is a pretty sad story, in my judgment. I know we have not heard the end of it, but we have reached the end of the hearing. We thank our witnesses for coming forward. It has been a long day, I hope an illuminating day. That has been our intention.

We will stand adjourned.

[Whereupon, at 7:25 p.m., the Subcommittee was adjourned.]

THE ROLE OF THE FINANCIAL INSTITUTIONS IN ENRON'S COLLAPSE

TUESDAY, JULY 30, 2002

U.S. SENATE,
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS,
OF THE COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 9:36 a.m., in room SD–342, Dirksen Senate Office Building, Hon. Carl Levin, Chairman of the Subcommittee, presiding.

Present: Senators Levin, Durbin, Carper, Dayton, Lieberman (ex officio), Collins, and Fitzgerald.

Staff Present: Linda J. Gustitus, Chief of Staff, Senator Levin; Elise J. Bean, Acting Chief Counsel; Mary D. Robertson, Chief Clerk; Robert L. Roach, Counsel and Chief Investigator; Stephanie E. Segal, Professional Staff Member; Ross Kirschner, Deputy Investigator; Jamie Duckman, Professional Staff Member; Edna Falk Curtin, Detailee/General Accounting Office; Rosanne Woodroof, Detailee/Department of Commerce OIG; Lani Cossette, Intern; Alex DeMots, Intern; Kim Corthell, Republican Staff Director; Alec Roger, Counsel to the Minority; Claire Barnard, Investigator to the Minority; Jim Pittrizzi, Detailee/General Accounting Office; Meghan Foley, Staff Assistant; Jessica Caron, Intern; Victor Marsh, Intern; Tim Henseler (Senator Levin); David Berick (Senator Lieberman); Bill Weber (Senator Durbin); Gary Brown and Bob Klepp (Government Affairs Committee/Senator Thompson); Holly Schmitt (Senator Bunning); and Jennifer Bonar (Senator Fitzgerald).

OPENING STATEMENT OF SENATOR LEVIN

Senator LEVIN. Good morning, everybody.

Last week, the Subcommittee looked at the sham transactions that Enron used to obtain billions in loans from major financial institutions without showing any debt on Enron's books. The hearing revealed that the financial institutions not only were aware that Enron was engaged in misleading accounting but actively assisted Enron in its deceptions.

The documentation included an internal email from a Chase banker reporting how "Enron loves these transactions because it can hide debt from its equity analysts." We saw how Chase and Citigroup helped Enron construct false energy trades by providing offshore entities, effectively controlled by the banks, to participate as sham trading partners, the banks that then helped orchestrate multi-party trades with no price risk that canceled each other out

except for the equivalent of interest payments by Enron on loans Enron was trying to hide, and the phony cash flow from operations Enron was trying to magically create.

Chase and Citigroup did more than just help Enron carry out its deceptions. They also pitched Enron-style phony prepays to other companies, further spreading into the U.S. business community the poisonous practice of misleading accounting.

At the hearing, through the witnesses, and after the hearing, through statements by their CEOs, the two banks claimed this was all business as usual, reflecting industry practices, and that their companies acted properly and with integrity, to use their words. William Harrison, the CEO from Chase, even lauded Chase's witnesses because, in his words, they "stood tall" in the face of Subcommittee questioning. Neither company has admitted responsibility for helping Enron doctor its financial statements, much less admit to any misjudgment or wrongdoing.

The evidence presented at the hearing last week, however, was clear and convincing. And when the banks' witnesses were confronted with the documentary evidence that showed the banks knew that the phony prepays were being used by Enron to book loans as cash flow from operations in order to keep their credit rating and stock prices up, the witnesses worked hard to obfuscate the plain meaning of their own words.

Look at the testimony last week of Jeffrey Dellapina of Chase when confronted with a recording and transcript of a phone conversation in which he participated where an Enron employee said to Mr. Dellapina, "That goes to the same point you were raising, Jeff, that from your side you also want to make sure that Mahonia seems independent." When questioned about the use of the phrase "seems independent," Mr. Dellapina challenged the taped conversation. "I don't believe I would have wanted it to seem independent," he said.

When asked about an internal Chase document describing Mahonia as a special purpose entity used in the Enron prepays as "formed by Chase," Donald McCree, a senior Chase official, testified that the words "formed by Chase" were loose and inaccurate.

When Robert Traband of Chase was asked if he would call the Enron prepays with Chase a circular deal, Mr. Traband testified he didn't know. The Subcommittee then played a tape of a conversation involving Mr. Traband where he specifically described the prepays as "circular." When asked what he meant by that term, Mr. Traband said, "I don't recall."

Citigroup often took the same tack of saying its documents didn't mean what they said. When asked about a memo in which a Citigroup employee suggested adding a penny to the price spread in an Enron prepay to make the prepaid structure a little more like a trade, Richard Caplan of Citigroup denied that the memo actually meant what it said.

A similar response was given by James Reilly of Citigroup when he was asked about three different memos regarding the so-called Roosevelt prepay. In those memos, Mr. Reilly refers to Enron's undisclosed agreement to repay $125 million by September 30, 1999, an arrangement that, if known, would have forced recategorization of the so-called prepay as Enron debt.

At the hearing Mr. Reilly said, "'Agreement' is a word that could mean different things, and I did not intend to mean that it was a binding agreement."

In one exchange, when confronted with the discrepancy between what the memo said and what he was testifying to at the hearing, Mr. Reilly said, "The memo is wrong." He was, in effect, disputing the plain words of three contemporaneously written memos.

And, finally, when David Bushnell was asked whether he agreed that it is the responsibility of a financial institution like Citigroup not to participate in a deception, believe it or not, Mr. Bushnell said, "It depends upon what the definition of a 'deception' is."

I guess that is what is meant by "standing tall."

So last week, Chase and Citigroup denied the plain meaning of words in their own contemporaneous documents. Today, looking at the prepared statement of Merrill Lynch, it is more of that same approach: Deny the plain meaning of words in your own documents.

Merrill Lynch will say commitment doesn't mean commitment, guarantee doesn't mean guarantee. They mean something else, maybe best efforts. And loan doesn't mean loan. It means purchase.

Last week, we showed how two major financial institutions helped Enron hide debt. This week, we will see how a major financial institution, Merrill Lynch, helped Enron artificially and deceptively create revenue.

But the underlying truth is the same as last week. Enron couldn't have engaged in the deceptions it did without the help of a major financial institution. Merrill Lynch assisted Enron in cooking its books by pretending to purchase an existing Enron asset when it was really engaged in a loan.

The accounting sham involved the sale of an interest in three Nigerian barges that operated as floating power stations. Enron wanted to sell these barges before the end of calendar year 1999 so it could report the sales income as earnings in its 1999 financial statements. But Enron was unable to find a buyer willing to complete the sale before the end of the year.

In mid-December 1999, Enron asked Merrill Lynch as a favor to set up a special purpose vehicle, subsequently called Ebarge, to take an Enron asset—barges, or the income that they might particularly create—for a short period of time for a $28 million purchase price consisting of a $7 million cash payment from Merrill Lynch and a purported loan of $21 million from Enron to Ebarge. This transaction would allow Enron's African Division to book sales income of $12.5 million. Merrill Lynch agreed, but this is the key: Only after receiving Enron's commitment that it would find a buyer for Merrill Lynch's interest in the barges within 6 months.

Merrill Lynch also received assurances of a 15-percent return on its $7 million, plus an immediate payment of $250,000. This so-called sale arrangement violated elemental accounting rules which allow a seller to book sales income only for a transaction that is a real sale. Enron's guarantee to Merrill functioned as an ongoing obligation that kept Merrill from assuming the risks of company ownership. In a real sale, the risks and rewards of the asset are completely transferred from the seller.

The evidence is clear that Enron and Merrill were aware of this accounting problem, and in order to facilitate Enron booking the transaction as a sale, it had to keep Enron's oral guarantees a secret, omitting it from the documentation and leaving it as an oral understanding.

As the 6-month deadline approached on June 30, 2000, Merrill Lynch became concerned that Enron would not fulfill its promise. On the day before the deadline, LJM2, an investment vehicle run by Enron's chief financial officer Andy Fastow, stepped in and took over an interest in the barges from Merrill Lynch at the previously agreed upon terms. It paid Merrill Lynch the $7.525 million that had been assured to Merrill by Enron at the beginning of the transaction, the $7 million principal and 15-percent interest over 6 months, and it assumed the $21 million note that Enron initially loaned to Ebarge.

By the way, Ebarge never paid any interest on that note, notwithstanding loan documents that required it to do so. Three months later, in September 2000, Enron and LJM2 sold the barge interest to a third party.

When you look at the elements of this transaction, it is obvious that it is not a real sale. Through an unwritten side agreement, Enron provided a guarantee to take Merrill Lynch out of the deal within 6 months. Merrill Lynch was guaranteed and received a specified 15-percent return on its $7 million investment. Merrill Lynch never received the periodic cash flow payments from the operation of the barges as promised under the agreement and never complained about it to Enron. Ebarge, the Merrill Lynch special purpose vehicle, didn't pay any interest on the $21 million loan advanced by Enron. Enron paid all the costs associated with the formation, operation, and management of Ebarge. In other words, the risks of owning Ebarge weren't transferred to Merrill Lynch.

This wasn't the only troubling transaction that Merrill Lynch had with Enron. In an April 1998 memorandum, two high-ranking Merrill Lynch employees informed Merrill Lynch's president, Herb Allison, that Merrill had lost a chance to co-manage a large Enron stock offer solely because Enron objected to what Enron saw as a lack of support by Merrill Lynch's Enron analyst John Olson. The memorandum stated that Enron's decision to deny Merrill's participation in the offering was "based solely on the research issue and was intended to send a strong message as to how viscerally Enron's senior management team feels about our research effort."

A few months later, Mr. Olson was gone from Merrill. The new Merrill analyst assigned to Enron then upgraded the Enron stock from the equivalent of a neutral to a buy rating. A January 1999 memorandum thanked Mr. Allison for telephoning Kenneth Lay at Enron about Merrill's "difficult relationship in research," and it projected additional fees from Enron now in the range of $45 million.

Earlier this year, Merrill paid $100 million to the New York State Attorney General for compromising the independence of its financial analysts in a case not involving Enron.

Among the additional business that Merrill Lynch picked up that year and the next was handling the private placement offerings for Enron's off-balance sheet partnerships LJM2 and LJM3. Merrill

Lynch was not blind to the conflicts of interest raised by these partnerships, but Merrill Lynch decided to go ahead, and it helped raise some $390 million for LJM2. The money that Merrill raised for LJM2 helped Enron inflate its earnings and mislead investors and analysts in the way that it did.

Merrill described Enron internally as "one of its biggest clients" and "the key to its Houston office." In 5 years, from 1997 until 2001, Merrill Lynch received approximately $43 million in fees from Enron. There is nothing wrong with making money honestly. It is part of the American dream. But making money by assisting a company like Enron to engage in misleading accounting or by discouraging analysts to provide honest ratings or by touting a questionable investment is more like a nightmare than a dream. It misleads investors, rewards the wrong companies for the wrong reasons, and produces the situation we are in today with the crisis of investor confidence.

Today, we will inquire why a company like Merrill Lynch would risk its reputation to do what it did. Hopefully, when the details come to light, Merrill Lynch will take action against those who participated in deceptions with Enron and will set a firmer, straighter course for the future.

Senator Collins.

OPENING STATEMENT OF SENATOR COLLINS

Senator COLLINS. Thank you, Mr. Chairman. Today is the second hearing held by the Permanent Subcommittee on Investigations examining the role played by some of America's leading financial institutions in the collapse of Enron. Our investigation has revealed that certain financial institutions knowingly participated in and, indeed, facilitated transactions that Enron officials used to make the company's financial position appear more robust than it actually was, thereby deceiving shareholders, customers, and employees.

Last week, the Subcommittee examined one such type of transaction. Enron and its bankers, JPMorgan Chase and Citigroup, call them "prepays." The evidence, however, revealed them to be nothing more than sham transactions designed to obtain, as one of the banks continued to tout on its website, "financial statement-friendly financing."

Like so many of the other deals at Enron, the apparent motive was to portray a false image of the company's financial health. As NYU law professor and former judge William Allen noted recently in a speech, banks such as JPMorgan Chase and Citigroup are supposed to play a valuable role in our system of corporate checks and balances because they monitor debtors more closely than other providers of risk capital. "Did the lenders not understand that they were enabling deception?" Professor Allen asked. Much to my dismay, last week's hearing made clear that they did understand but chose to proceed anyway.

Our focus this morning is whether Merrill Lynch also participated in enabling Enron to deceive the public. There are four aspects of the Merrill Lynch-Enron relationship that we will examine. The first involves Merrill's purchase of Nigerian barges with electricity-generating equipment from an Enron-related entity in late

1999. This transaction allowed Enron's African Division to meet its quarterly reporting target and announce to the financial world that Enron had sold a $12 million asset.

As with much at Enron, though, the reality was a different story. Merrill's purchase of the barges was predicated on Enron's agreement that it would find another buyer for them within 6 months. Under a Securities and Exchange Commission accounting bulletin published that very month, such an arrangement clearly did not allow the seller to recognize the revenue. Handwritten notes by a Merrill employee warned that there was a "reputational risk, i.e., aiding and abetting Enron income statement manipulation," but, nevertheless, Merrill went ahead with the deal.

Second, the Subcommittee will examine actions taken by Merrill management in response to Enron's complaints that Merrill's financial analyst had rated the company less favorably than Enron would have liked. Enron informed Merrill that it would not be selected as a manager or co-manager of a large Enron stock offering solely because Enron objected to the rating of its equity research analyst. Merrill appears to have gone to extraordinary lengths to placate Enron, and subsequently Merrill was indeed added as a co-manager of the offering. After the offer went public, Merrill executives kept Enron's CFO updated on the activities of the research analyst. On at least three occasions, Merrill actually sent the CFO copies of the analyst's internal list of calls that he made to clients touting the offering. The analyst in question subsequently left Merrill, and his replacement immediately upgraded Enron. This case raises troubling questions about conflicts of interest compromising the integrity of the ratings on which investors rely.

Third, the Subcommittee will pursue Merrill's decision to participate in an Enron loan syndication. Enron sought Merrill's participation in a deal that had been arranged by JPMorgan Chase, but had failed to raise the needed $482 million for an Enron-related company. Prior to the request, Enron had made clear to Merrill that it was at "a distinct disadvantage" for obtaining future business from Enron because of its reluctance to use its balance sheet to support Enron's business activities. Subsequently, Merrill agreed to participate in the loan syndication despite indications that the investment would result in a financial loss. Ultimately, Merrill did indeed lose approximately $1.6 million in the deal.

Finally, the Subcommittee will closely look at Merrill's dealings with an off-the-books partnership headed by Enron's CFO Andrew Fastow. His investment company, LJM2, asked Merrill to provide a $10 million line of credit in connection with a $65 million revolving credit facility. An internal Merrill document advocating the credit request states, "Committing to this LJM2 facility will build Merrill Lynch's relationship with Andy Fastow and assist Merrill Lynch in securing future investment banking opportunities with Enron."

Other Merrill emails warned against it, citing the lack of a rating and the nature of the credit risk. Nevertheless, two of the witnesses scheduled to testify before the Subcommittee this morning requested an exception to bank policy for the loan for the following reasons: "Enron is an excellent client, $40 million in revenue in 1999, $20 million in revenue for 2000 year to date. Andy Fastow

is in an influential position to direct business to Merrill." In the end, the prospect of more lucrative business from Enron trumped those at Merrill who urged caution.

As we learn more about how prestigious financial institutions participated in transactions that allowed Enron to deceive investors, I am reminded of a congressional hearing almost a century ago with another banker. In 1912, J.P. Morgan appeared before a House Subcommittee to be questioned about his firm's banking practices. He was asked whether it was true that his bank had no legal responsibility for the value of bonds it sold to clients. He responded that the banks assumed something even more than legal responsibility—moral responsibility.

Yet, incredibly, last week, when asked by Senator Levin whether it was appropriate for a financial institution to act in a manner it knew was deceptive, one banker responded, "It depends on what the definition of a 'deception' is."

It is this sad and telling quote that sums up the attitude of some professionals on what their duty is in today's market. This attitude must change. The day of the deal that serves no purpose other than to exploit an accounting loophole and the day when the law serves as the ceiling rather than the floor on the conduct of Wall Street professionals and corporate executives must come to an end.

It is important to remember that the Enron debacle is more than just a tale of one company's greed. As a result of Enron's downward spiral and ultimate bankruptcy, shareholders, large and small, individual and institutional, lost an estimate $60 billion. The collapse of Enron caused thousands of Americans to lose jobs, to lose their retirement savings, and to lose confidence in corporate America. It is time to halt the practices that are beneficial to a select few and harmful to thousands.

I want to once again commend Chairman Levin for his leadership in this important and thorough investigation. It is my expectation that these hearings will yield valuable lessons for strengthening our free enterprise system, restoring public confidence in our capital markets, and ensuring that small investors in particular have access to complete and accurate information to guide their investment decisions.

Senator LEVIN. Thank you, Senator Collins, and thank you very much for your words and also for your and your staff's participation and support in this investigation.

Senator Lieberman.

OPENING STATEMENT OF SENATOR LIEBERMAN

Senator LIEBERMAN. Thank you, Mr. Chairman. I want to again commend you, Senator Levin, and you, Senator Collins, and your staffs for continuing the very important and very insightful work that this Permanent Subcommittee on Investigations is doing into the role of financial institutions in Enron's collapse. As Chairman of the full Senate Committee on Governmental Affairs, I am proud of and grateful for the work that you are doing.

Today, we will examine another set of very troubling transactions between Enron and one of the Nation's leading financial institutions, Merrill Lynch. We are going to be talking about a number of technical issues today, about highly complex agreements and

partnerships that improved the appearance of Enron's financial statements but kept investors in the dark about what was really happening at that company before it was too late for most of them to save their security. But there are, of course, beyond these details, much larger questions at stake here, and I would like to just speak for a moment or two about them.

For weeks now, our capital markets have seemed like a mountain climber sliding down a hill, drawn by the forces of gravity, trying to find a ledge to break the fall. In the last several days, it appears that the markets have grabbed onto a ledge, but it is too early to determine whether that ground will hold and the confidence that is the precondition of growth in the markets has fully returned.

Obviously, one of the main causes of the fall down the mountain of our markets has been the collapse of investor confidence, which is to say the inability of average investors to know who or what to believe.

We Americans are great risk takers. That is what gives our free enterprise system its vitality, its seemingly endless supply of new ideas and ambitious people to turn those ideas into opportunities and wealth, to grow the middle class. But Americans are also great pragmatists. We don't part carelessly with our money. We work hard to understand the difference between intelligent investing and reckless gambling. And that practicality is aided and based, in the case of investments, on the honesty and transparency of our markets.

It is that critical blend of hard-charging risk and hard-won trust that gives our unique brand of capitalism its strength and its stability. Without risk, our economy couldn't accelerate. But without trust, it couldn't stay on the road.

That delicate balance has clearly been upended since December 2 when Enron declared bankruptcy. Enron and its progeny, WorldCom, etc., have had a terrible effect on that transparency and sense of trust. It is now equally troubling, of course, to see truly venerable firms like Merrill Lynch drawn into this web of actions that have undermined trust in our markets in the long term for profit in the short term.

Today's hearing echoes, in fact, several of the concerns raised during the full Senate Governmental Affairs Committee's hearing on February 27 when we examined particularly that day the role of Wall Street analysts. Today we are going to be examining the interrelationship between investment firms and research analysts, and we are also going to hear evidence, as my colleagues have indicated, that strongly suggests a quid pro quo between Merrill and Enron regarding the analysis that was given by Merrill Lynch regarding Enron's stock.

The findings presented by the Subcommittee today regarding this distortion of the analyst ratings process are totally consistent with the findings of New York Attorney General Eliot Spitzer's first-rate investigation into Merrill's equity research practices. As a result of that investigation, Merrill Lynch agreed to a $100 million penalty and promised to reform its practices.

Hopefully, such conduct will now end, not just at Merrill but at all the other firms involved, as a result of the very strong bill spon-

sored and written by Senator Sarbanes that has passed the Senate and is on its way to becoming law, which contains tough mandates that should enhance the independence of the Wall Street analysts that millions of average investors depend on as they decide where and how to put their money into the market.

Finally, Mr. Chairman, I think it is important to remember again that today, as the result of a remarkable revolution that has occurred in our country over the last two decades in which capitalism has truly been democratized, more than half of the American people have a stake in our capital markets, or at least they did before the recent crisis in confidence among investors. My guess is they still do. That money is underpinning people's hopes for funding a secure retirement, for sending a child to college, or for buying a house or starting a new business. Just talk to your friends and neighbors and coworkers, as I have been over the last several weeks, and you will be able to measure the very personal impact on millions of Americans that has resulted from the topics that this Subcommittee is investigating today.

So while the talk may get technical today, the stakes here could not be more real for millions of American families. And that is why, Mr. Chairman and Senator Collins, I want to thank you and your staffs again for your outstanding work in these investigations which have told and will continue to tell such riveting stories of corporate fraud and negligence that I am confident that they will help bring about not just the corrective legislation, but the business self-regulation that will restore confidence in our markets and help those millions of Americans I have spoken of realize those dreams regarding their retirement, their children's education, and their hopes in general for a better life.

For that I thank you, and I think that the people of this country are and will be thankful for the work that you are doing here.

Senator LEVIN. Senator Lieberman, thank you, and thank you for the support which you have constantly given to this investigation.

Senator Dayton.

OPENING STATEMENT OF SENATOR DAYTON

Senator DAYTON. Thank you, Mr. Chairman. I certainly would echo the comments of Senator Lieberman to both you and Senator Collins and your staffs. I think you have done an extraordinary job in delving into these matters. I think you have uncovered more information that explains the full scope of Enron's nefarious schemes than any other entity in the Congress and, to my knowledge, anywhere in the country. I think you have performed, as Senator Lieberman has said, an invaluable service to our Nation. You have helped this Subcommittee and Congress attempt to come to a full understanding of what has occurred here so that we can prevent it from happening ever again in this country. You have given the victims, employees, investors, and the public confidence in our financial institutions.

I note that in the beginning many wondered how it was that this company could have gone so far and concealed so much and built such a web of financial transactions that proved to be unreliable and ultimately worthless. It was clear from your previous hearing that they did not engage in these transactions alone. In fact, they

could not have carried out this web of deceit and this scope of financial transactions and deceived so many other parties for so long without willing collaborators; collaborators who saw it in their financial interest to do so, even at the deception of their own investors, their own other clients, and certainly at the expense of their own corporate integrity.

The *Wall Street Journal* yesterday said, and they are not the type to easily bash business, but they said that with the evidence they have looked at, the banks, referring to Citigroup and Morgan, deserve the beating that they are now getting. And I would ask unanimous consent that this editorial be included in the record, Mr. Chairman. I think it is unusual and well-deserved support of the work of the Subcommittee.[1]

I think it also bears putting it into the record now so that it helps sets the context that the victims of these schemes that go beyond the corporations involved. As they said here, the investors who bought into these, the insurance companies, investors in Enron, the banks' investors and shareholders, and of course, the employees of these companies, have suffered from these transactions. Those who put their faith and trust in these institutions and suffered the consequences were a lot of real, regular Americans. They were not the ones with deep pockets, not the ones who walk up and down Wall Street, not the ones who have limousine service and show up every day with three-piece suits. These are people who work for a living. These are people whose retirements depended upon these investments. These are people in many cases whose life savings were wrapped up in these investments. They are people who had every reason to believe that they were being led not only to make good investments, but they were being given accurate and appropriate information by those who were counseling them, including their brokers.

This hearing today, Mr. Chairman and Ranking Member, gets into, I think, a very important area. Were people who were induced to invest in Enron and its subsidiaries given accurate information by those in the know, or was that information compromised by the very institution that they were relying upon to provide that information?

Both of you have noted in your opening remarks—and we will delve into it further—the scope of the financial relationship that Merrill Lynch has evidently had with Enron and its other operations. I note that in its July 26 public statement, the company seems to take a somewhat different tack in that regard. It notes that a couple of its employees have been notified that they are subject to a Department of Justice investigation. It says here that Merrill Lynch, however, has been advised that it is not a target or a subject of the Department of Justice's investigation, and is cooperating fully with this Subcommittee. It goes on to say Merrill Lynch's dealings with Enron were limited. As has been reported previously, they included a $7 million equity investment in a company established to operate energy generation barges and Merrill Lynch's role as a private placement agent for the LJM2 partnership. Merrill Lynch strongly believes its dealings with Enron and

[1] Exhibit No. 195 which appears in the Appendix on page 2043.

LJM2 were appropriate and proper based upon what it knew at the time. Merrill Lynch also believes that based on the information currently available to its employees, its employees also behaved properly in the Enron transactions.

I think it will be particularly interesting today, Mr. Chairman, to see how those statements reconcile with the evidence that this Subcommittee has uncovered.

Thank you.

Senator LEVIN. Thank you so much, Senator Dayton. As always, you have put your finger on some very, very significant points.

I now call as witnesses Robert Furst and Schuyler Tilney. Mr. Furst was a former Managing Director for Merrill Lynch at Dallas. Mr. Tilney is Managing Director of Global Energy and Power, Global Markets & Investment Banking for Merrill Lynch in Houston, Texas.

The first order of business today is to swear you both in as witnesses, and I would ask you to please stand and to raise your right hands. Do you swear that the testimony that you will give to this Subcommittee today is the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. FURST. I do.

Mr. TILNEY. I do.

Senator LEVIN. You have prepared statements for today informing the Subcommittee that you both are invoking your Fifth Amendment right against self-incrimination and that you both, therefore, will refuse to testify today. You may proceed with your written statements now, and then we will clarify that issue.

First, Mr. Furst.

TESTIMONY OF ROBERT FURST,[1] FORMER MANAGING DIRECTOR, MERRILL LYNCH & CO., DALLAS, TEXAS

Mr. FURST. Thank you, Mr. Chairman, Madam Ranking Member, and members of the Subcommittee. My name is Robert Furst, and I appear here today voluntarily. In anticipation of testifying before you today, I met voluntarily with the Subcommittee's staff 2 weeks ago for nearly the entire day. As your staff has no doubt informed you, I cooperated fully with them, answering all of their questions to the best of my ability, reviewing a number of documents and providing information that I believed—and still believe—will assist the Subcommittee in understanding the investment banking transactions at issue here today. At the time I met with the staff, I intended to appear today and testify truthfully, fully, and to the best of my ability.

Since I met with the staff, however, I have learned that the matter in which the Subcommittee is interested is also the subject of an investigation by the U.S. Department of Justice. As much as I would like to advise the Subcommittee of my view as to whether there was anything questionable concerning one of the investment banking transactions my colleagues and I worked on at Merrill Lynch, my lawyers have advised me that any such statement may constitute a waiver of my constitutional rights under the Fifth Amendment. As I am sure the Subcommittee knows, and as my

[1] The prepared statement of Mr. Furst appears in the Appendix on page 337.

lawyers have informed me, the U.S. Supreme Court last year reaffirmed the principle that because, "truthful responses of an innocent witness . . . may provide the government with incriminating evidence from the speaker's own mouth," even innocent witnesses may assert their Fifth Amendment right not to answer questions. I, therefore, respectfully advise the Subcommittee that I intend to assert my constitutional privilege under the Fifth Amendment in response to the Subcommittee's questions today.

Thank you.

Senator LEVIN. Mr. Tilney.

TESTIMONY OF SCHUYLER TILNEY,[1] MANAGING DIRECTOR, GLOBAL ENERGY AND POWER, GLOBAL MARKETS & INVESTMENT BANKING, MERRILL LYNCH & CO., HOUSTON, TEXAS

Mr. TILNEY. Mr. Chairman, Ranking Member, Members of the Subcommittee, my name is Schuyler Tilney, and I am a Managing Director at Merrill Lynch. As you may know, 2 weeks ago, I met with Robert Roach, special counsel—excuse me—the majority counsel and chief investigator of the Subcommittee; Gary Brown, special counsel, as well as other members of the Subcommittee staff. I answered all of the questions they asked me concerning the subjects of today's hearings. I believe they would agree that I was fully cooperative and forthcoming about the facts that I knew, and that I did my best to answer every one of their questions. I met with the Subcommittee staff voluntarily, and I fully anticipated that I would appear before you today to answer your questions.

Unfortunately, since that time, I have been advised that one of the transactions to be covered today is the subject of an investigation by the Department of Justice. Therefore, I have reluctantly accepted my lawyer's advice to decline to answer questions at this time based upon my constitutional right not to do so. I am profoundly saddened that I must make this decision, and I am mindful of the significant personal and professional consequences that follow from my decision not to give testimony at this time. I look forward to the day that I can satisfy all of the concerns the Subcommittee may have on these matters.

Thank you.

Senator LEVIN. Mr. Furst, is it your intention to refuse to answer any and all questions directed to you by the Subcommittee today?

Mr. FURST. Yes, it is.

Senator LEVIN. Mr. Tilney, is it your intention to refuse to answer any and all questions directed to you by the Subcommittee today?

Mr. TILNEY. On the advice of my lawyer, it is.

Senator LEVIN. With that understanding, you having invoked your right to assert your constitutional privilege, you are both now dismissed.

I will now call Kelly Martin, Senior Vice President and President of International Private Clients for Merrill Lynch in New York.

Before I administer the oath to Mr. Martin, I will just make one other comment about witnesses today. We have one other witness, Dan Bayly, who we invited to testify today who is a current Merrill

[1] The prepared statement of Mr. Tilney appears in the Appendix on page 338.

Lynch employee and who is familiar with a number of issues being discussed today. Despite our earlier efforts, his counsel did not offer to make him available to the Subcommittee staff for a prehearing interview until approximately 9 p.m. last night, and then for a very limited period of time, which was not an acceptable proposal. Consequently, the Subcommittee staff will be taking his deposition immediately following the close of today's hearing.

Mr. Martin, would you please stand and raise your right hand? Do you swear that the testimony you are about to give to this Subcommittee will be the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. MARTIN. I do.

Senator LEVIN. You may proceed now with your statement.

TESTIMONY OF G. KELLY MARTIN,[1] SENIOR VICE PRESIDENT AND PRESIDENT OF INTERNATIONAL PRIVATE CLIENT DIVISION, MERRILL LYNCH & CO., NEW YORK, NEW YORK

Mr. MARTIN. Thank you, Mr. Chairman.

Mr. Chairman and Members of the Subcommittee, thank you for the opportunity for me to speak with you today. My name's Kelly Martin. I'm a senior vice president at Merrill Lynch and president of the International Private Client Division. During most of the relevant time period, I was head of Merrill Lynch's Global Debt Markets Division.

As the Subcommittee has requested, I am here to speak about Merrill Lynch's policies and practices relating to its relationships with publicly traded companies. I was not personally involved in any of these transactions which will be reviewed today.

As the Chairman said, another Merrill Lynch executive, Dan Bayly, chairman of Investment Banking, will be available—was available to testify today and will be interviewed by the Subcommittee subsequently.

I will do my best to answer your questions accurately and from an overall Merrill Lynch perspective. However, please be advised that Mr. Tilney and Mr. Furst had primary relationship responsibility with Enron at the time of the transactions in question. We have addressed in our written statement all the transactions that the Subcommittee has asked about. For purpose of this oral statement, we will discuss our relationship with Enron, the December 1999 purchase of an equity interest in certain barges, and our overall research coverage.

By way of background, Merrill Lynch believes that our limited dealings with Enron were appropriate——

Senator LEVIN. Mr. Martin, let me interrupt you just for a minute. Could you bring that mike as close as possible to your mouth? A little more.

Mr. MARTIN. How's that?

Senator LEVIN. Better. Thanks. You are getting there.

Mr. MARTIN. By way of background, Merrill Lynch strongly believes that our limited dealings with Enron were appropriate and proper based on what we knew at the time. At no time did we en-

[1] The prepared statement of Mr. Martin appears in the Appendix on page 339.

gage in transactions that we thought were improper. We welcome the opportunity to discuss them with you.

At the outset, all of us in this room recognize the enormous harm caused by the collapse of Enron. The facts that now have come to light about Enron, however, were not known at the time of the transactions discussed below. All of us now have the significant benefit of hindsight. Our decisions, however, had to be made with the facts—based on the facts that we knew at the time.

At the time we conducted business with Enron, it was not a discredited, bankrupt company as it is today. It was instead the world's leading integrated electricity and natural gas company—a company of enormous stature and prestige.

In 1999, Enron reported revenues of $40 billion. It was ranked as the most innovative company in the world for 5 straight years by Fortune 500 company CEOs, board members, and senior management who participated in this survey. In addition, it was ranked as the top company for "Quality of Management." It was literally the textbook example of a modern American success story.

Moreover, at the time we dealt with Enron, it was known to have extensive in-house and outside expertise. Enron's CFO, Andrew Fastow, had been awarded CFO Magazine's "Excellent Award for Capital Structure Management." Its CEO, Jeffrey Skilling, had been a partner at McKinsey & Company, a leading management consulting firm in the world. Enron had one of the most widely respected boards in the country. Arthur Andersen was viewed throughout the world as a leader among independent auditing firms. Vinson & Elkins, Enron's principal outside counsel, was one of the leading law firms in Texas.

Our firm dealt with Enron at an arm's-length relationship and made business decisions based on information that was then available. We relied on Enron's accountant's opinions, its board approvals, its lawyers' opinions, its audit committee oversight, and other governance processes, and felt justified at the time in believing Enron's financial representations. In addition, the transactions were subject to a significant amount of Merrill Lynch internal approval processes and included review with business, legal, and other personnel who had no personal stake in the specific outcomes. At no time did we engage in transactions that we thought improper.

Merrill Lynch's relationship with Enron. Merrill Lynch is one of the leading, world's largest diversified financial institutions. At the time of 1999, we had revenues of approximately $22 billion. Our investment banking revenues for that year were some $3.7 billion. Enron was not a significant contributor to Merrill Lynch's revenues or earnings. It represented two-tenths of 1 percent of the total average annual investment banking fees for the firm—two-tenths of 1 percent.

Between 1997 and 2001, Enron retained advisers to assist it in 43 strategic transactions. Enron retained Merrill Lynch to act as adviser on one transaction during the 5-year period of time. At least 10 other firms performed more advisory assignments for Enron during this period, including two firms that, added together, performed a total of 23 such assignments.

Although Merrill Lynch participated in debt and equity offerings for Enron, the relationship was modest. From time to time, Merrill Lynch also participated in credit lines for Enron. Here, too, however, we had a minimal role. We did not participate in most of the credit lines, and our commitments to Enron represented less than 3 percent of those deals that we participated in with them. We were never a lead lender in any loan syndicate. We did not participate in any of the billions of dollars of prepay financing transactions that the Subcommittee examined last week. We discuss below the transactions that the Subcommittee has asked us to address.

The barge transaction. Questions have been raised whether it was appropriate for Enron to record a December 1999 transaction with Merrill Lynch as a sale. In that transaction, a Merrill Lynch entity—Ebarge, LLC bought shares of a company that entitled Ebarge to be part of the cash flows from the sale of energy to be produced by generators on three barges. Merrill Lynch's investment exposure in the transaction was $7 million. Merrill Lynch agreed to the transaction largely to build a relationship with Enron and believed that it was likely, although not certain, that a third party unaffiliated with Enron would ultimately purchase Merrill Lynch's shares in that company.

Merrill Lynch does not know, even today, whether Enron's accounting treatment for this transaction was correct. We were not advising Enron on the appropriate accounting treatment for this transaction. In general, when we act as a purchaser or a seller, we are not asked for and do not provide advice on the other party's accounting treatment; rather, we expect them and their experts to determine the appropriate accounting treatment unto themselves. This is a market practice and fully in accord with all legal standards. Furthermore, there was no understanding by Merrill Lynch that Enron or any entity related to Enron would buy back Merrill Lynch's shares. In fact, Merrill Lynch had a contrary understanding—that an independent third party was likely to buy Merrill Lynch's interest.

There was no guarantee, hidden or otherwise, that Merrill Lynch would receive a certain rate of return. The purpose of not including a reference to any questions—to any guarantee in the written agreement was not to hide it; it was because there was no guarantee and Merrill Lynch was at risk. The written purchase and sale agreement expressly provided that it was the entire agreement of the parties, and that it superseded any other understanding related to the purchase and sale. Had Enron not succeeded in finding a buyer for our interest, our only recourse would have been to try to find a buyer ourselves.

Three, we did anticipate that an independent third party—an Asian trading company, which we understood was close to agreeing to the principal terms of the purchase of the shares—would potentially buy Merrill Lynch's interest, but Merrill Lynch knew that it was at risk and knew that it had no remedy if the company failed to go forward and Enron and Merrill Lynch failed to find a purchaser.

Four, the transaction was, in fact, a purchase of equity interest rather than a loan. Merrill Lynch owned the shares and was at

risk until it was able to sell or re-sell those shares. Though it hoped and expected to be able to re-sell those shares at a profit, it had no guarantee that would happen.

Five, Merrill Lynch played no role whatsoever in determining Enron's own accounting for the transaction.

Six, nevertheless, we considered a number of issues presented by the transaction. Consistent with Merrill Lynch's internal procedures, the transaction was considered by a committee of individuals that included credit, legal, and other personnel who had no personal stake in the proposed transactions and who are expected to consider a wide range of issues and risks raised by a given transaction. Before deciding to proceed with this transaction, the committee did what it was supposed to do: It considered the issues, including whether the transaction could be used to manipulate Enron's income statements, and concluded that Merrill Lynch's participation in the transaction was appropriate.

Among the factors considered: Merrill Lynch was, in fact, at risk in the transaction; Enron's accounting for the transaction had been vetted with and approved by Enron's outside auditors; Enron and its experts were among the most knowledgeable in the world on structured finance; the transaction itself was so small relative to Enron, which had $40 billion in revenues in 1999, that it seemed inconceivable that the transaction could be used to manipulate Enron's earning statements.

Research coverage. The Subcommittee has asked about Enron's complaint in 1998 concerning Merrill Lynch's research coverage of Enron and whether as a result Merrill Lynch's research ratings were compromised.

The facts are: In 1998, an internal memorandum indicated that Enron was not going to invite Merrill Lynch to participate in an underwriting of Enron's common stock because Enron was disappointed with our research coverage. The memorandum asked senior executives to place a call to Enron executives for the purpose of reconsidering their decision, citing our longstanding relationship with the company and leadership position in the natural gas industry.

We understand that such a call was made, and ultimately Merrill Lynch participated as a co-manager in the transaction, which occurred in May 1998.

At no time was Merrill Lynch's research compromised. In fact, our analyst retained his intermediate neutral rating throughout the entire time in question. His neutral rating extended from at least July 1997 through August 1998, at which time he left the firm.

In October 1998, after this analyst joined a new firm—after he joined his new firm, this former analyst initiated Enron coverage with a rating of accumulate.

In 1998, the Merrill Lynch analyst who assumed coverage of Enron, along with continuing his coverage of other companies in the sector, also initiated his coverage of Enron with accumulate.

In 2001, our analyst was one of the first to downgrade Enron.

In conclusion, we thank the Members of the Subcommittee for this opportunity to come before you today and present information that may be helpful in your investigation into Enron's collapse. We

fully support your efforts and want to assist in restoring investor confidence in capital markets. Merrill Lynch intends to be an industry leader in helping to ensure that America's capital markets are governed by the highest ethical standards.

Had we known at the time what we know today, we would not have conducted business with Enron. Without the benefit of hindsight, however, and based on the information available to us at the time, we strongly believe that our actions were appropriate and proper.

Thank you, Mr. Chairman.

Senator LEVIN. Thank you, Mr. Martin.

Our questioning today will proceed as follows. Senator Collins and I will each take 20 minutes for questioning. We will then turn to our colleagues based on the early-bird approach for 10 minute rounds of questions.

Enron was one of the most aggressive companies asking Merrill Lynch to put its money to work on behalf of Enron. Enron's CFO, Andrew Fastow, made it very clear to Merrill Lynch that investment in Enron ventures was an important part of the relationship building process. The message from Enron was unambiguous. "We give business to people who lend us money and put their balance sheet to work for us." Merrill Lynch wanted to respond to Enron's demands.

Exhibit 208[1]—and these exhibits are all in front of you, Mr. Martin—is a December 1999 memo on the Nigerian barge deal. It stated that "Enron views the ability to participate in transactions like this as a way to differentiate Merrill Lynch from the pack and add significant value."

Exhibit 244[2] is a 2001 memo to senior Merrill officials, reporting that Merrill Lynch was going to try to put its money to work for Enron. "Merrill Lynch agreed to seek ways to commit its balance sheet to selected situations that were uniquely value added to the company." Commit its balance sheet. Now, that was simply because Enron had informed Merrill Lynch of the following. That "Merrill Lynch is at a distinct disadvantage because of Merrill's reluctance to use its balance sheet to support Enron's activities."

At the same time Merrill Lynch was fully aware of what Enron was trying to do, structure deals so that debt was hidden off-balance sheet and cash flow was manufactured. Look at what Merrill Lynch said about Enron deals in discussing a planned $3 billion public offering. An internal Merrill Lynch memo, Exhibit 258[3] said the following: "Enron believes they can structure anything to be off balance sheet."

The Nigerian barge transaction was referred to as a "balance sheet deal." That is Exhibit 259.[4]

In another transaction, Exhibit 256,[5] Enron asked Merrill Lynch to give a special purpose entity a loan that would never be used "to ensure that the structure receives off balance sheet treatment."

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[1] Exhibit No. 208 appears in the Appendix on page 2064.
[2] Exhibit No. 244 appears in the Appendix on page 2225.
[3] Exhibit No. 258 appears in the Appendix on page 2348.
[4] Exhibit No. 259 appears in the Appendix on page 2349.
[5] Exhibit No. 256 appears in the Appendix on page 2344.

So Merrill Lynch knew full well that Enron was trying to structure deals so that debt was hidden off-balance sheet and cash flow was manufactured. And yet it still participated in Enron deals.

The first question. Mr. Martin, would you agree that it is Merrill Lynch's responsibility not to participate in a financial deception?

Mr. MARTIN. Absolutely.

Senator LEVIN. Now, on the Nigerian barge deal, a subsidiary of Enron was trying to see projected future cash revenues from 3 barges that it owned in Nigeria. When the sale of that interest fell through, Enron sought Merrill Lynch's help in completing a transaction by the end of the year to meet Enron's revenue targets. If you look at Exhibit 208,[1] this is a memo describing the Enron proposal. "Jeff McMahon, Enron Vice President, Treasurer of Enron, has asked Merrill Lynch to purchase $7 million of equity in a special purpose vehicle that will allow Enron Corporation to book $10 million of earnings. The transaction must close by 12–31–99. Enron is viewing this transaction as a bridge to permanent equity, and they believe our hold will be for less than 6 months. The investment would have a 22.5 percent return."

So Merrill knew that Enron wanted to complete a transaction by the end of 1999 so it could book the $12 million in earnings or $10 million in earnings to assist Enron. A special purpose vehicle was created called Ebarge to hold the interest in the barges. It is our understanding that Enron paid all the costs of creating that special purpose vehicle. Ebarge was funded by a $7 million cash contribution from Merrill Lynch and a $21 million seller-financed loan from Enron. Ebarge then transferred $28 million to the Enron subsidiary. The issue is whether accounting rules allowed Enron to show the proceeds from this transaction as income on their financial statement.

Exhibit 204 is a chart.[2] According to the first chart which covers the relevant accounting rules, Enron was prohibited from taking credit in its books for the barge sale if any one of the following happens: If Enron had significant obligations for future performance to directly bring about the resale of the Nigerian barge interest by Merrill Lynch; or if the risks of ownership did not transfer from Enron to Merrill Lynch; or another factor that can prohibit recognition of a sale is if Merrill Lynch paid no interest on the financing provided by Enron.

Now, let us just look at the first two points, that Enron guaranteed a resale, and that Merrill Lynch was promised by Enron that it would receive back its equity investment plus a rate of return. The documents clearly show a commitment to Merrill Lynch that it would be bought out within 6 months. Exhibit 207[3] is the internal Merrill Lynch document written by Robert Furst, who was before us earlier today, requesting funds for the barge transaction.

"Enron is viewing this transaction as a bridge to permanent equity, and"—and here are the key words—"they have assured us that we will be taken out of our investment within 6 months."

Further down on that page. "Enron will facilitate our exit from the transaction with third party investors. Dan Bayly will have a

[1] Exhibit No. 208 appears in the Appendix on page 2064.
[2] Exhibit No. 204 appears in the Appendix on page 2051.
[3] Exhibit No. 207 appears in the Appendix on page 2059.

conference call with senior management of Enron confirming this commitment to guarantee the Merrill Lynch take out within 6 months," confirming this commitment to guarantee the Merrill Lynch take out within 6 months.

The conference call did take place, and according to Mr. Furst and Mr. Tilney, who participated in that call, and who were interviewed by our staff, Mr. Fastow represented during that call that Enron would get Merrill Lynch out of the deal within 6 months. That is what Mr. Furst and Mr. Tilney told our staff.

Now, Merrill Lynch continued to represent its understanding that it had a commitment from Enron. If you will look at Exhibit 209,[1] this is a December 23, 1999 weekly Merrill Lynch report memo. Now, this is a Merrill Lynch document, and here is what it says. "Most unusual transaction of the week was IBK"—and that is Merrill Lynch's investment bank division—"was IBK request to approve Enron Corporation relationship loan." That is Merrill Lynch's word, loan. Merrill Lynch asked to invest $7 million in a Nigerian power project relationship loan.

Within that same internal Merrill Lynch weekly report it said the following: "This transaction will allow Enron to move assets off balance sheet and book future cash flows currently as 1999 earnings, approximately $12 million. IBK was supportive based on Enron relationship, approximately $40 million in annual revenues and assurances from Enron management that we will be taken out of our $7 million investment within the next 3 to 6 months." In writing, contemporaneously, the word "assurances."

Mr. Furst and Mr. Tilney told our staff that the deal would not have gone forward without that assurance from Enron.

After negotiations over the arrangement, Enron agreed to repay Merrill Lynch's money plus a 15 percent rate of interest and an upfront $250,000 fee, making the effective interest rate 22½ percent. This understanding on Merrill Lynch's part continued throughout the next 6 months. And then as the 6-month deadline approached, Merrill Lynch's officials, including those at high levels, raised the issue of this guarantee.

In a June 13 email, Exhibit 218,[2] one Merrill Lynch employee, who also served as the Vice President, Assistant Secretary and Assistant Treasurer of Ebarge wrote the following: "As we approach June 30, I am getting questions concerning Ebarge, LLC. It was our understanding"—understanding—"that Merrill Lynch IBK positions would be repaid its equity investment as well as a return on its equity by this date. Is this on schedule to occur?" Note the contemporaneous word "our understanding."

On June 14, just the next day, a Merrill Lynch employee drafted a letter, reminding Enron of the agreement regarding Ebarge. This is Exhibit 219.[3] It stated, by Merrill Lynch employee contemporaneously: "Enron has agreed to purchase the shares from Ebarge by June 30 for a purchase price net of the balance on the loan from Enron Nigeria Power of $7,510,976." Note the word "agreed."

Now, before that letter was actually sent, Enron called and informed Merrill Lynch that a buyer had been identified. This was

[1] Exhibit No. 209 appears in the Appendix on page 2068.
[2] Exhibit No. 218 appears in the Appendix on page 2158.
[3] Exhibit No. 219 appears in the Appendix on page 2159.

LJM2. But the situation has repeatedly been made clear. Enron had made a commitment to get Merrill Lynch out of the barge deal, and pay Merrill the $7 million and its promised rate of return.

And as the share purchase agreement, Exhibit 222,[1] between Ebarge and LJM2 shows the price paid by LJM2 was $7,525,000, which is exactly equal to what Merrill Lynch was promised by Enron, at 7 million in equity, plus a 15 percent rate of return for the 6 months.

Now, given that, all that, contemporaneous and in writing, and these are on Merrill Lynch's own documents. I am not even going to take the time now to go to the LJM documents which make specific reference to the promise to Merrill that it would be taken out using the same words by another investor by June. But given all that, how can you possibly say that there was no understanding by Merrill Lynch that Enron or any entity related to Enron would buy back Merrill Lynch's shares. Do you have personal knowledge, by the way, of any of this, or are you just giving the statement here for Merrill Lynch?

Mr. MARTIN. Mr. Chairman, I was not involved in any of these transactions in any detail whatsoever.

Senator LEVIN. So when you gave the statement earlier, you are just giving the statement, position of Merrill Lynch, not your own personal information; is that correct?

Mr. MARTIN. Yes. I'm here—I believe the request of the Subcommittee was to have a senior Merrill Lynch person who could comment on policy. That was my original role. But I'll play that role and any other role——

Senator LEVIN. We of course expected that we would have the direct testimony, which we did not get, but we have the statements made by the two witnesses who used their Fifth Amendment privilege, the statements to our staff, which I have now reflected, but I also, in addition to that, have now gone through all kinds of contemporaneous documents which show that there was a commitment, a promise, an assurance, over and over again. Yet it is Merrill Lynch's position that those words were not true.

Mr. MARTIN. Let me try, in the position that I'm in, to frame that out from a Merrill Lynch perspective and try to shed some light on our view, first and foremost of this as an equity investment. And again, this is from an overall Merrill Lynch point of view. And the documents that you went through, I have seen some over the last few days, and in and of themselves each of these documents have sort of multiple words on them, some with, on the same page, "loan" and "equity", "equity" and "loan." So I can't comment on each and every one of the documents.

But this is what I can shed some light on, again from a Merrill Lynch perspective. The process internally that we used to make this decision on the barge was as follows.

Senator LEVIN. Could you pull the mike a little closer, please?

Mr. MARTIN. OK. And again, I think this was instructive how we looked at things. First and foremost, this transaction went to a committee internally at Merrill Lynch called the Debt Markets Commitment Committee, otherwise known as the DMCC. It went

[1] Exhibit No. 222 appears in the Appendix on page 2164.

there to be vetted, and it went there for a decision in December. That committee did talk about this transaction, but they could not make a decision on the transaction. The reason they could not make a decision on the transaction is the Merrill Lynch Debt Markets Commitment Committee has no authority to make equity decisions. So it was kicked to—up to Tom Davis, who is President of the Capital Market Group. And the reason it was kicked up to Tom Davis in the Cap Market Group is he is the only person—he was the only person in the investment banking world who can make an equity decision. So he had to get involved.

Third, where this transaction was booked internally was an area called IBK Positions, which if you've read through this multitude of documents, was in there in various places. And the only thing in IBK positions, the only things that can be put in IBK positions are equity investments. So the decisionmaking process on this transaction internally at Merrill Lynch, the vetting process internally at Merrill Lynch, the governance process internally at Merrill Lynch, and last but not least, how this transaction was booked and where it was booked was equity, equity, equity. With regard to conversations that took place between individuals at Merrill Lynch and Enron, between various documentation and Enron about guarantees, this is my understanding of the discussions. My understanding of the discussions are that we of course, Merrill Lynch, are not in the business of buying barges. We are in the business of making private equity decisions, and we do that, and we do that in a multitude of things.

The discussions with Enron were we do not want to be in this investment long term but as a relationship with you, a growing relationship with you, this is something that we will do from an accommodation point of view. From where I sit in the seat I sit in and the background I have involved with all of these transactions, I can't comment specifically on conversations that may or may not have taken place between various individuals. Thank you.

Senator LEVIN. All the expenses of this special purpose entity were paid for by Enron; is that correct?

Mr. MARTIN. That's my understanding.

Senator LEVIN. Is it common for a special purpose entity which is used by Merrill Lynch to have all of its associated costs paid for by another entity?

Mr. MARTIN. It is not unusual.

Senator LEVIN. Exhibit 216(a)[1] is the loan agreement between Enron and Ebarge related to the $21 million so-called loan from Enron Nigeria Power Holding, Limited. The loan to Ebarge had an interest rate of 12 percent per year. The first repayment of principal and interest, $773,000, was due April 30. Was that payment received?

Mr. MARTIN. I don't believe so, no.

Senator LEVIN. If this were a true equity investment and that interest were due, would not Merrill Lynch have written to the person owing it the money, saying, hey, where is the $773,000?

Mr. MARTIN. Ultimately, yes.

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[1] Exhibit No. 216(a) appears in the Appendix on page 2117.

Senator LEVIN. Not ultimately. I am talking about on April 30 when it was due.

Mr. MARTIN. Mr. Chairman, I mean ultimately. Merrill Lynch has hundreds and thousands and tens of thousands of these arrangements, so ultimately from the financial accounting department somewhere, they would be sending out a notice.

Senator LEVIN. So if this were a true equity position, that notice would have gone out, would it not have?

Mr. MARTIN. At some point in time it would have gotten out.

Senator LEVIN. Did it?

Mr. MARTIN. I do not know.

Senator LEVIN. Pardon?

Mr. MARTIN. I don't know if it went out.

Senator LEVIN. We have been informed it did not go out.

Mr. MARTIN. OK.

Senator LEVIN. Ebarge never made a single one of those payments, neither the principal nor the interest.

Merrill Lynch not only, or Ebarge not only, borrowed the money from Enron, the $21 million, but to perhaps clarify a point I was just making, Merrill Lynch did not receive the scheduled cash flow payments from the operations of the barges as you were supposed to receive under the terms of the agreement. Is that correct?

Mr. MARTIN. That's my understanding, yes.

Senator LEVIN. And you never complained about that; is that correct?

Mr. MARTIN. That's also my understanding.

Senator LEVIN. So this so-called loan to Ebarge from Enron on which interest was due, Ebarge never received a notice of that, and the amount of money owed Merrill Lynch, scheduled cash flow payment from the operation of the barges that they were supposed to receive under the terms of the agreement, they were never received and there was never a complaint about that as well.

My last question, because my time is up. Ebarge did not have a bank account, as we understand it, and in February or March 2000, Ebarge was re-domiciled from Delaware to the Cayman Islands at the request of Enron.

Now, if this was a Merrill Lynch company, why did Merrill Lynch re-domicile it at the request of Enron, and why did Enron want it domiciled in the Caymans?

Mr. MARTIN. Mr. Chairman, I'm not the—I'm not sure specifically with regard to this transaction why the special purpose vehicle may have been moved from one domicile to another.

I know overall that using the Cayman Islands as a domicile often has tax advantages for offshore entities, and that is often why things are moved to the Cayman Islands.

Senator LEVIN. Well, do you know whether or not Ebarge ever paid U.S. taxes?

Mr. MARTIN. I do not know.

Senator LEVIN. So here in summary appears to be what happened. There is an unwritten side agreement that you have no evidence did not occur, and there is a huge amount of contemporaneous written evidence that it did occur, that Enron provided a guarantee to take Merrill Lynch out of the deal within 6 months. Merrill Lynch was guaranteed and received a 15 percent return on

its $7 million payment. Merrill Lynch never received the periodic cash flow payments from the operation of the barges as promised under the agreement, never complained about it to Enron. Ebarge did not pay any interest on the $21 million loan advanced by Enron. Enron paid all the costs associated with the formation, operation and management of Ebarge, the Merrill Lynch special purpose vehicle. It is very clear, it seems to me overwhelmingly clear, that in fact the risks of owning Ebarge were not transferred to Merrill Lynch and indeed there was never a real sale by any of the accounting standards which have to be applied before the term "sale" can be applied to a transaction.

And so the December 23, 1999 weekly report of Merrill Lynch, its own internal report, had it exactly right. This was a relationship loan. The accounting rules indicate it was not a real sale. Merrill Lynch knew it, Enron knew it, and yet Enron booked $12 million in income from the proposed sale or supposed sale, and that was a deception in its financial statement, and Merrill Lynch was a participant in that deception.

Senator Collins.

Senator COLLINS. Thank you very much, Mr. Chairman.

Mr. Martin, I realize that you have no direct knowledge of these transactions, you were not personally involved, and in some ways I feel that you must have drawn the short straw to be here today.

Mr. MARTIN. I volunteered actually.

Senator COLLINS. But nevertheless the testimony that you presented on behalf of Merrill Lynch raises so many troubling questions, particularly since much of what you've presented appears to be directly contradicted by interviews conducted by the Subcommittee, and by documents from your company.

You started out by saying "at no time did we engage in transactions that we thought were improper." Are you saying that there were no red flags that made you think that something troubling or unusual or deceptive was going on?

Mr. MARTIN. No. We, as is in many of these pages, transactions all the time have issues, have questions, have risks. So our processes are designed internally to actually vet those before we do the transaction, and only if—and I want to underscore that—only if we feel comfortable with all the risks will we go ahead with the transaction from our point of view.

Senator COLLINS. But I do not see how you could possibly feel comfortable with these transactions given the information that is provided within your firm's documents. For example, Mr. Furst told the Subcommittee that Merrill was very much aware that Enron needed to try to inflate it earnings and to have a better return for its African division. There is ample evidence that Enron had significant obligations for future performance to bring about the resale of the Nigerian barges. And so that raises questions of whether the risk of ownership ever really transferred from Enron to Merrill.

There is a very persuasive question raised by one of Merrill's high-ranking employees, Jim Brown, in Exhibit 212,[1] in which he specifically raises reputational risk of aiding and abetting Enron's income statement manipulation. Is that not a huge red flag?

[1] Exhibit No. 212 appears in the Appendix on page 2079.

Mr. MARTIN. These are all—Senator, these are all red flags. Jim Brown's notes here talk about questions that he had going into this committee meeting, the DMCC which I mentioned previously. Foreign tax, environmental, operating performance, failure to complete, foreign ownership, reputational risk, these are all things that Jim Brown, in his capacity as a senior member of the Merrill Lynch committee, would have talked and raised about at that committee meeting.

Senator COLLINS. But he specifically raises the issue of financial statement manipulation.

Mr. MARTIN. Correct.

Senator COLLINS. Did that not put you on guard that Enron might be cooking its books through this transaction?

Mr. MARTIN. Again, I wasn't, "A", in this meeting, and "B" in this transaction, but the way our processes work—and we Merrill Lynchers spend a lot of time making sure that of the millions of transactions that we do on a yearly basis, that they are vetted as thoroughly as possible.

So my assumption is that this was discussed and the various people sitting around the table, which included legal and credit, relationship management, bankers, corporate finance, that they went through all of this and they got assurances, either from Enron or from Enron's advisers, that these things could be satisfied from our point of view, Merrill Lynch's point of view.

Again, we can't—we can't impose—we cannot look through our clients and know everything that they're going to do with all parts of their transactions, but we do the best we can to make sure that transaction at hand for us is vetted properly and as fully as possible.

Senator COLLINS. You seem to imply in your statement that the answer to the issue of financial statement manipulation was, "that the transaction was so small relative to Enron that it seemed inconceivable that the transaction could be used to manipulate Enron's income statements." On the one hand that sounds to me like you are saying it is OK if they cheat a little, but aside from that issue which is troubling to me, did it not occur to Merrill that Enron might be engaging in similar transactions with other partners, and therefore, there might be significant implications for the accuracy of its financial statements? If Enron was pushing so hard for Merrill to complete this transaction that one of your high-level employees raised a red flag about the risk to Merrill Lynch's reputation, why was that not pursued more? Why did it not occur to Merrill Lynch that this might be the tip of the iceberg?

Mr. MARTIN. A few things in response, Senator. One thing is the reference to the size of the transaction is—to put it in perspective, from a Merrill Lynch point of view, and from an Enron point of view, I suspect, what the singular transaction was, we, in our written and opening statement, were also trying to respond to the Subcommittee's questions about our, Merrill Lynch's knowledge and active involvement with Enron in their own manipulations, which is clearly not true.

Red flags, to your question on red flags. Enron was a very aggressive client. Enron was, as I said in the opening statement, recognized by everybody in the United States and perhaps globally,

from Wall Street to government to consulting to academia as the future way that American companies could potentially be run. It was $40 billion in revenue. It was an aggressive company. Their whole thesis, as stated publicly in multiple situations, was physical assets aren't needed; financial assets and off-balance sheet assets are the way to go. That was stated everywhere in every article about Enron and their philosophy about how to build their business.

So clearly, we were focused on working with them as a growth company, as a big company, as a seeming industry leader, certainly in their industry and corporate America. We, however, had never—never at any one point in time would we do something that we thought would be wrong, but there would be no way that we could possibly know, with a $40 billion company, all the various transactions that they were doing.

Senator COLLINS. Let me tell you of another red flag that was raised by Merrill Lynch. Mr. Furst raised the issue of how a $7 million sale of these barges could be booked as $10 million or earnings. Could you explain why that did not cause concern?

Mr. MARTIN. No. Again, I think—I do not know where that comes from but——

Senator COLLINS. It is Exhibit 208.[1]

Mr. MARTIN. We knew—Exhibit 208?

Senator COLLINS. Yes.

Mr. MARTIN. What we are most concerned about at Merrill Lynch is the $7 million of risk, which is why I went through, somewhat painstakingly, where we booked the transaction. You know, once again, I don't have a comment on what Enron would book in their financial statements on their books and records based on either this transaction or any other transaction.

Senator COLLINS. On page 7 of your testimony you state that the transaction was in fact a purchase of an equity interest rather than a loan, correct? That was your testimony today?

Mr. MARTIN. Yes, Senator.

Senator COLLINS. I would like you to look at Exhibit 209,[2] the second page. It is a Merrill Credit Flash Report, and there is a summary that clearly describes the Nigerian barge transaction as a loan. It says, "The most unusual transaction of the week"—I guess we should take some comfort that it was unusual—"the most unusual transaction of the week is the IBK request to approve Enron Corporation relationship loan." How is it that Merrill Lynch is maintaining this morning that this was the purchase of an equity interest, when the credit flash report put out by Merrill Lynch describes it as a loan?

Mr. MARTIN. Senator, if you'll look down on that page in the first sentence, the same page, it says: "Requested by Enron Corporation to make a $7 million equity investment." There are other documents that have both—as I said to Mr. Chairman, there are documents that use the words "equity" and "loan" and "commitments" quite interchangeably, which is why I, from my seat, and what I can help you with from an understanding point of view, is if you

[1] Exhibit No. 208 appears in the Appendix on page 2064.
[2] Exhibit No. 209 appears in the Appendix on page 2068.

follow how we made the decision to do this transaction, who can make a decision how the decision was made and where the decision ultimately—where the transaction was ultimately placed within Merrill Lynch, it was all equity. So the language on all of these various pages is actually somewhat contradictory almost on each and every one of these pages. So on the same page, after they talk about a relationship loan, they talk about a $7 million equity investment.

Senator COLLINS. I want to follow up on the question that Senator Levin asked you about the understanding that Merrill Lynch had that there would be a resale of the barges within 6 months time. You testified that there was no understanding by Merrill Lynch that Enron or any entity related to Enron would buy back Merrill Lynch's shares. And you go on to say that, in fact, Merrill Lynch had a contrary understanding that an independent third party would likely buy Merrill Lynch's interest.

My first question is then, regardless of whom you thought the ultimate purchaser was going to be, the clear understanding was that you were going to be stuck with these barges for only 6 months; is that correct?

Mr. MARTIN. Again, I wasn't involved specifically in this transaction, but the—it is my understanding that the discussions with Enron went along the lines of initially continued to increase the business relationship. They needed us to do something with regard to these barges. We are not in the business of buying barges. We can do equity investments. We obviously had discussions with Enron that we would like their help in getting out of this investment, and it's their business and they know the industry, and as a leading corporation in this sector, they would be most likely to help us. But we were fully prepared, again, fully prepared as a corporation to take that $7 million investment, and potentially over time, write it down if we still had to carry it.

So there was a hope, and there was an anticipation that we could get out of this investment over the course of 6 to 12 months, but again, I—from all of the things that I understand, there were not very specific timelines with regard to specific dates.

Senator COLLINS. In fact, was there not an understanding that Enron was responsible for finding a buyer?

Mr. MARTIN. Again, I believe the understanding was that Enron would go to great lengths to help us seek a potential other buyer for this asset. They had been working very closely with, as I said in the opening statement, an Asian corporation who was a potential buyer of these barges, and got very close, apparently, to being able to make the purchase. So we were relying on Enron's expertise in their own industry to help us find potential other buyers over time, which is correct.

Senator COLLINS. Mr. Furst told the Subcommittee that without the guarantee or assurances that Enron would find a buyer for the barges within that set time, Merrill would not have gone through with the deal. Do you contest the accuracy of that?

Mr. MARTIN. I don't actually know Mr. Furst, so I don't know exactly what he said or didn't say. I suspect, again, from a point of view of process, what would have been asked of the investment bankers is if we have to make an investment, a private equity in-

vestment to enhance a client relationship, how over time are we going to get out of this? So from his point of view as an investment banker trying to do a transaction, he may have had that view. I don't think necessarily that would have been the Merrill Lynch & Co. view.

Senator COLLINS. Are you aware that other Enron employees were becoming concerned as time went on that Merrill Lynch was still stuck with the barges and, in fact had drafted a letter about the possible resale of the barges back to Enron or some other party?

Mr. MARTIN. I was not aware, no. These are Enron concerns.

Senator COLLINS. These are Merrill Lynch concerns to Enron.

Mr. MARTIN. Some of the——

Senator COLLINS. Expressed to Enron, that there still had not been a buyer.

Mr. MARTIN. Some of the documentation that the Chairman walked us through were from different parts of Merrill Lynch, some accounting, some finance, some banking, and it is not unusual, particularly in finance and accounting, that they have certain things that they are supposed to track. So their concern would be—they would be doing their job based on what they were told as far as expected returns and expected exit of the investment.

Senator COLLINS. The reason this issue is so important is that if this is not a true sale, then it violates the Generally Accepted Accounting Principles for Enron to represent it as such, and it also violates the SEC bulletin on revenue recognition and financial statements. It seems to me that the deal had four characteristics that suggest that this was not a true sale. First, Enron did have significant obligations for future performance to directly bring about the resale of the barges. Second, the risks of ownership do not, in my judgment, seem to have truly been transferred from Enron to Merrill, given that agreement. Third, Merrill did not pay interest on the financing provided by Enron. And fourth, Enron appears to have paid all of Merrill's costs of the transaction. Do you disagree with any of those facts?

Mr. MARTIN. Well, I think, Senator, the question you are asking me is from Enron's point of view, and Enron and their advisers, accounting advisers, was this a true sale from their point of view, is not something that we, Merrill Lynch, spent a lot of time on. What we spent our time on was, again, we—it was our understanding that we had an equity investment, that we had to book it in the right place, that we had to have an exit strategy, that we needed help on the exit strategy. And that was our concern. Our concern was for Merrill Lynch shareholders, that $7 million, and make sure that the $7 million was booked the right way and that there was some rational strategy to get out of it.

Whether that was from an Enron point of view proper GAAP accounting, is it's an Enron and Enron adviser topic.

Senator COLLINS. I just cannot accept that answer when one of your employees raised the issue of whether Enron was using this transaction to manipulate its financial statement.

Mr. MARTIN. Correct. That was one of—in Jim Brown's statements of the questions he had, I'm sure—again, I wasn't in that meeting and I wasn't listening to all the dialogue around his con-

cerns, but there must have been conversation around that specific topic, that he got comfort that that actually couldn't happen from our standpoint.

Senator COLLINS. Thank you, Mr. Chairman.

Mr. MARTIN. Thank you.

Senator LEVIN. Thank you, Senator Collins. Senator Lieberman.

Senator LIEBERMAN. Thanks, Mr. Chairman.

Mr. Martin, thanks for your testimony. I must say that in the testimony today, which I gather is on behalf of Merrill, that people at Merrill essentially had no idea at the time that any of the interactions between your firm and Enron were questionable or that Enron might be engaged in deceptive and improper activities. After reviewing the Subcommittee's findings and listening this morning to your testimony and answers to the questions Senator Levin and Senator Collins have posed, I must tell you that it is hard to see how an experienced, respected, sophisticated company like Merrill Lynch missed what was going on here.

Let me just take this LJM2 agreement interaction, for instance, that people at Merrill knew because the firm was the private placement agent, because Merrill was itself an investor, and because almost 100 of Merrill's employees were investors in LJM2, that Mr. Fastow was on both sides of LJM's transactions with Enron. In fact, Merrill apparently advertised that fact in its private placement memorandum. And Merrill also said in the memorandum that two other gentlemen, also Enron finance insiders, Mr. Kopper and Mr. Glisan, would also be managing LJM. Later, when Merrill was trying to sell the Nigerian barges that it temporarily bought from Enron, it was LJM2 that bought the barges from Merrill, so there was awareness there as well.

So I must say it is hard for me to understand how Merrill Lynch did not understand that LJM, in its transactions, for which Merrill provided hundreds of millions of dollars in financing, represented a very risky and questionable corporate strategy for Enron, or is the point here really—and again, this is hindsight—that that did not matter to Merrill Lynch? In other words, as you said at one point, that Merrill Lynch was evaluating risk to Merrill Lynch in this series of transactions with Enron and its spinoffs, and not risk to the investors in Enron as a result?

Mr. MARTIN. Senator, thank you for the questions. Broad topic of LJM2, it's quite a broad topic. First and foremost we were the placement agent, which means we found people who were interested in this concept with these people for these type of investments in primarily the institutional market, some fairly sophisticated investors. We, again, in our own corporate due diligence, we raised the flags significantly about how Mr. Fastow, how are we to be—how was it going to be made clear, and how was Enron going to ensure that there was in fact no conflict, and how could they govern that? How could they actually govern the fact that they had a CFO who was in Enron and also was the managing partner for what in and of itself was a private equity alternative investment fund? We debated that internally, and again, in some of these records here that I've become familiar with, we even had a call with Jeffrey Skilling, the President of Enron, to say, "How are you, Mr. Skilling, going to make sure? Are you comfortable with this?

Are you comfortable that there is a Chinese wall, that decisions will not be compromised, that it will not be to Enron's detriment or benefit and vice versa for LJM2?"

His answer, again—and this is my understanding, having not been involved in all these conversations—his answers were very clear, that he knew all about how this was set up; he was extremely comfortable and had a lot of confidence with Mr. Fastow and the dual roles he was going to play; that it was vetted and approved by their own board of directors and it was vetted and approved by all their various advisers.

So I agree with your question/statement that we, Merrill Lynch, should have had red flags on the LJM2 contract. We did have them. We vetted them as far as we possibly could.

With regard to the complication within LJM2 and what exactly was going on in LJM2, the type of constructs, the type of financing, the type of assets, I would offer up that we didn't understand actually what was going on in LJM2, we, Merrill Lynch, but I would also offer up that nobody did, because there were other people who invested in LJM2 who were at least as sophisticated as Merrill Lynch. We all got the statements about their investments. We all got the updates with regard to what kinds of transactions they were doing or not doing. None of us spotted, or none of us connected the dots from activity in LJM2 and the potential consequences on both LJM2 and Enron. We just didn't—we either didn't connect the dots or we didn't necessarily know all the connections, but we didn't, and none of the other investors in LJM2 did either.

Senator LIEBERMAN. Here is my concern about that. The more I hear about this case, the more it seems to me that Enron, perhaps not uniquely, but Enron was like a poisonous spider spinning a web for its own benefit, in which it was engaging and entrapping a whole host of very reputable financial institutions, including your own, but your entrapment was not unknowing, or in some sense, unwilling, because the web that—the poisonous web that Enron was spinning, nonetheless had some attractive qualities to it for you. It had a business relationship, it had fees. And that ultimately what Merrill was doing was what at the base level one expects a business to do, which is to protect itself from undue risk.

But the question is, because it just does seem to me that you had an access to so much inside information as a result of your participation in these deals—and I do not mean improper inside information—I mean the kind of information, you know, the poor suckers as they turned out to be who were investing their 401(k) plans or institutional investors who were investing hundreds of millions of dollars in Enron did not have, and the information that the board of directors of Enron and the auditors and all we now know were not aggressively, independently trying to get out to the public, that one of the breakdowns in the system here was that great companies like Merrill Lynch did not blow the whistle, did not accept that extra measure of responsibility and say, "Hey, we are protecting our risk in this deal with Enron and LJM and LJM2, but this thing stinks, and maybe we do not see the whole picture." We could not see the whole picture of what Enron was up to; you could not see the whole picture.

But should not folks at Merrill have seen enough to have said, "Hey, we do not want to be part of this," because in the end maybe you ended up aiding and abetting the improper, perhaps illegal behavior of the executives of Enron?

Mr. MARTIN. I think, Senator, that again trying to go back, it is hard to go back in time, very hard. I take your point and that is a level and a role that Merrill Lynch frankly aspires to play which is over and above the next transaction or the next 10 transactions. What is in the long-term best interest of—at Merrill Lynch, our clients and frankly the markets themselves, and we have tried to play that role, not just in the United States, but around the world.

Speaking purely personally—and my dealings with Enron were quite limited—it was a very complicated company. We, for a living, are financial experts or parts of financial experts. Clearly in hindsight, it would have been great to put this whole puzzle together and blow the whistle. It was a very hard puzzle. It was almost a multidimensional puzzle. It is a role that we aspire to play. It is a role that we try to play, frankly. And for the snippets of information that we had—and I hear what you say about inside information, legal inside information—the balance sheets, the tax structures, the operating complexity of these type of companies are geometric, no one counterpart, be it commercial bank or investment bank, for a company like Enron was, frankly could ever see enough to actually know that whole dimensional puzzle.

Senator LIEBERMAN. Let me interrupt you because my time is up. But I want to ask you—my colleagues will come, I am sure, to the question of the relationship between Enron and the analyst at Merrill who was giving the adverse ratings on Enron, and what Merrill's executives' conduct toward them said about what you knew about what was happening there.

But my final question, and I ask for a brief answer. This is one of those knowing all we know now, and having been through the torment the market and the economy has been through as a result of Enron and its progeny, has anything changed at Merrill Lynch? In other words, if you saw what you saw, if today this deal came in, would it raise enough red flags so somebody at Merrill would have said, "We can protect our risk. Merrill's going to be all right in this deal, but this thing smells and we should not be part of it?"

Mr. MARTIN. Senator, we are continuously changing and trying to improve all of our processes. The processes that we went through on all of these transactions were as complete as we could make them at the time with the information we had at the time. Again, in perfect 20/20 hindsight, we would have the same processes and spend more time on them and have more discussion on them, and hope to get the answers that were more complete in this multidimensional puzzle called Enron.

Senator LIEBERMAN. Well, I hope that if one like this came through the door today, that the folks at the top would make sure the folks who were dealing with it would blow the whistle. Thank you.

Mr. MARTIN. Thank you.

Senator LEVIN. Senators Dayton, Fitzgerald, Durbin, and Carper, in that order.

Senator DAYTON. Thank you, Mr. Chairman.

Mr. Martin, I do not agree with the view that you drew the short straw to be here. It seems to me, based on your comments and lack of direct knowledge about these events so far, that you were selected very carefully to represent the company. They selected you because of your minimal knowledge of the events and incidents about which you were going to be asked today so that the company could issue a press statement saying it was cooperating fully with the Subcommittee, when it was in fact providing as little information and confirmation or informed a denial as possible. I just want to say for the record, I do not consider that to be cooperating with the Subcommittee at all.

Since you do not really have any of the answers based on your lack of involvement, I am not going to ask you many questions. I would like to put into the record and at the end get your overall observation on this matter regarding the analyst who did not give Enron the rating which they thought they were deserving, going back to 1998. I also note, just to set the context, you refer to how little the financial relationship was with Enron for Merrill Lynch. You, throughout your testimony on behalf of the company, minimized that relationship, but yet these memoranda and that subsequently stressed some of these deals which others have referred to and others which are questionable on their nature, questionable on their value as stand-alone transactions, refers to Enron, for example, one memorandum has one of the most critical relationships in the Houston office, also in another matter refers to Enron as providing $40 million in revenues for Merrill Lynch in 1999 and $20 million to be expected in the year 2000. These are not insignificant amounts of money. It seems clear that one of the reasons to engage in some of these transactions on Merrill Lynch's account was in the hopes of obtaining additional financial relationships with the company in subsequent years. There is nothing wrong with that unless the transactions themselves are wrong.

But this particular matter is a memo from Rick Gordon and Schuyler Tilney to Herb Allison. It is dated April 18, 1998. It is Exhibit 239.[1] It is on Merrill Lynch stationery and it is an interoffice memorandum, so I assume it is an accurate or valid document. It is asking Mr. Allison to call two senior executives of Enron, Ken Lay, the Chairman and Chief Executive Officer, and Jeff Skilling, President and Chief Operating Officer, regarding Merrill Lynch's participation in Enron's contemplated $750 million common stock offering.

It goes on to say, "Enron was notified approximately 6 weeks ago"—this is April 1998—"by Moody's Investor Service, that it is considering downgrading Enron's debt due to the increase in the company's leverage over the past few years. After several meetings with Moody's to better understand its concerns, Enron determined that it needed to undertake a large common stock offering to avoid a credit rating downgrade. The company is extremely sensitive with regard to the confidentiality concerning this transaction. Past equity offerings undertaken by the company have been leaked in advance of the offerings with negative consequences to the stock price. Therefore, Enron solicited advice from only Merrill Lynch re-

[1] Exhibit No. 239 appears in the Appendix on page 2206.

garding the size and terms of and market receptivity to the offering. We were obviously apprised of the transaction in the strictest confidence and were informed that no other investment banks would be contacted in order to lessen the likelihood of a leak."

It goes on to say that "the expectation at Merrill Lynch, which is certainly understandable, is that they would be selected by Enron to serve as the lead manager." Given that they were the only investment bank to be contacted for advice on the transaction, that would be my knowledge and experience, a very reasonable expectation.

"However," it goes on to say, "our research relationship with Enron has been strained for a long period of time. Our equity research analyst at Enron is John Olson. He has a poor relationship with Jeff, and particularly Ken for several reasons." This being Ken Lay, the Chairman and Chief Executive Officer, and Jeff Skilling, President and Chief Operating Officer. Those are pretty high-level people in this $40 billion Enron company to have a poor relationship with.

It goes on to say, "Enron's Chief Financial Officer, Andy Fastow, called last night to inform us that Merrill Lynch would not be selected as lead manager of the offering, and further, that we would not even be included as a co-manager. He stated that the decision was based solely on the research issue and was intended to send a strong message as to how 'viscerally' Enron's senior management feels about our research effort."

Now, this was pretty apparent that Enron plays hardball or played hardball. Here is the Chief Financial Officer calling to inform your associates that after all this work, after all this advice on a very confidential basis, you are not going to be the lead manager. You are not even going to be a co-manager because they are just unhappy with the rating that the analyst has been giving the company. It is a rating which would seem to be warranted by the very transaction here. You had been asked to advise and were rejected from participation, mainly to issue a large common stock offering in order to avoid a credit rating downgrade by Moody's, which would certainly have a major impact on the price and value of the stock.

So all of this seems to be, quite understandably, troubling to Merrill Lynch and to others. Mr. Olson, as you note in your testimony, then, without changing his rating, leaves in August. It may be a coincidental event, but it does raise some questions as to exactly why he departed from Merrill. Then his successor, who your testimony notes did not issue a revised rating or an upgrade until November. It is surprising that you would leave such a major company without someone following it on an active basis or issuing an immediate revision to the rating. There is a gap there from August to November, and maybe you can fill in that gap.

But the fact is that the rating was increased by your successor analyst, is an institutional rating, and is backed by Merrill Lynch. It is not Mr. Olson or his successor as an individual. It has all the backing, all of the prestige and all of the credibility of Merrill Lynch in terms of its clients and others who are aware of those recommendations.

It certainly seemed to have had a beneficial result with regard to the relationship with Enron. There is a memo from Mr. Tilney to Mr. Allison, Exhibit 240,[1] on January 15, 1999; after these various personnel shifts have taken place. It says, "On a positive note, I want to update you on recent developments in our relationship with Enron, since you spoke to their CEO, Ken Lay, last spring regarding our difficult relationship and research. It is clear that your responsive message was appreciated by the company, and any animosity seems to have dissipated in the ensuing months. To that end, we have recently been awarded two significant mandates by Enron; the first to lead-manage the $1.5-billion IPO of their water company, which is expected to file in late February, and the second to raise a $1-billion private equity fund on behalf of the parent, which is expected to kick off in early March. Total fees to Merrill Lynch for these two transactions alone should be $45 to $50 million."

These are pretty high-stakes evaluations then that your research analysts make. Does this happen on a regular basis that the chief financial officers of companies call to inform your one side that they are not going to be invited to be a lead manager because they are dissatisfied with a rating that has been given by your research analyst? Does that typically result then in the departure of the research analyst a couple months later and a subsequent upgrade in the rating? Is that a common occurrence at Merrill Lynch or is this unusual? Do you have any knowledge of that aspect of the company?

Mr. MARTIN. Senator, let me answer a few of your initial concerns, and I will get to that. First of all, Merrill Lynch cooperates——

Senator DAYTON. I would like you to answer the question I just asked. Is this a typical occurrence or not?

Mr. MARTIN. It is a typical occurrence for a CFO of a corporation to follow extremely closely what all of the analysts are saying.

Senator DAYTON. That was not my question, sir. My first question is, is it a typical occurrence for the CFO to call and inform your investment bankers that they will not be selected to be the lead manager because they are viscerally dissatisfied with the rating that the company has provided?

Second, is it typical then that the analyst involved, who did not change his rating, departs within a couple of months after that matter?

Third, is it typical that the successor analyst raises the rating?

Fourth, is it typical then that it is followed by these kinds of awards by the company? Those are the four questions.

Mr. MARTIN. It is not atypical to get investment banking business with research being part of that decisionmaking process.

Senator DAYTON. If your rating of the company is good enough, then you get the investment banking business? If your rating of the company is not good enough, then you do not get the investment banking business?

Mr. MARTIN. If your following of the company is complete, if your following of the company is consistent, if your following of the com-

[1] Exhibit No. 240 appears in the Appendix on page 2209.

pany is reflective of what the company thinks of their story, it is part of their decisionmaking process who then would get investment banking business. That is absolutely true.

Senator DAYTON. Is that practice typical in your company and in the industry, as you know it?

Mr. MARTIN. It is typical that the research topic is part of the investment banking process. That is typical both at Merrill Lynch, and I assume for the rest of the industry.

Senator DAYTON. So you and the company are typically then placed under enormous pressure, if you want these very lucrative investment banking awards, to have your rating of the companies reflect the positive regard with which the executives or the management of that company wants to be evaluated.

Mr. MARTIN. I think the investment banking clients want the research analysts to understand their company and reflect that accurately, as opposed to the ratings.

Your second question, I believe, Senator, was or one of the questions was, in research coverage, the gap August to November. What happens at Merrill Lynch—I can't speak for the rest of the Street—is when a new analyst takes over a company, they need time to analyze the company, which is what happened and is very typical.

Senator DAYTON. I accept that that is the case.

Do you know any of the circumstances concerning the departure of Mr. Olson?

Mr. MARTIN. I know some of them. I believe what occurred within the Research Department was, because of the way the energy industry itself was starting to segment, you had trading companies, you had physical companies, you had financial companies, that we reorganized our research group, and we put under one analyst four or five companies that were similar. So we had Enron, and Coastal, and Williams and several other companies that, to us and to the analyst community, looked similar, as far as activity goes.

Senator DAYTON. I have one other question regarding a transaction in April. Mr. Tilney sent copies of Mr. Olson's Enron call list to Mr. Fastow when Mr. Olson was under some scrutiny, and this transaction, the sale of the additional stock was going through. These are, I assume, clients of his or Merrill Lynch's that he is calling to pitch or at least make aware of this offering, but he is also the analyst who is providing the rating at this point, which is, unless he has changed it, really, not a neutral, not a buy.

Is this typical also that the call sheets are sent to the——

Mr. MARTIN. Yes.

Senator DAYTON. So that they are aware that he is on board sufficiently enough that he is pitching the company and the stock sale, even though he does not approve of it?

Mr. MARTIN. His rating, actually, specifically was neutral short term, and positive long term. So he had a one rating as far as a long-term investment. It is typical and accepted practice that in an offering, whether it is equity or debt, that our marketing effort and who we talk to would be shared with particularly the CFO, who is particularly interested in who is buying the stock or who isn't buying the stock, and why not.

Senator DAYTON. So he is rating the company, and that is the official Merrill Lynch rating of the company. He is also pitching the

sale of the stock. Is he aware then that the sale of this or the issuance of this stock is for the purpose of satisfying Moody's and bringing down the debt-to-equity ratio of the company? Is he aware of that when he makes these pitches?

Mr. MARTIN. I am not sure what he would or would not have been aware of, but clearly——

Senator DAYTON. The others were aware. The people in the investment banking side were aware.

Mr. MARTIN. There would be a Chinese wall between certain information that he would or would not have. He clearly would know there would be an equity issuance coming.

Senator DAYTON. There was not a Chinese wall, though, when Mr. Fastow called to basically tell you that he was dissatisfied with the rating; therefore, he was not going to give you the business. I mean, he is effectively bridging that wall.

Mr. MARTIN. The Chinese wall is an information wall.

Senator DAYTON. I find your comments, then, and I take you at your word, sir, about the commonality of this matter to be extremely disturbing. My time has, I guess, expired, so I will relinquish the microphone, but I think if this is the case, Mr. Chairman, that this is typical, then I think it raises a serious question whether the ratings that investors are depending on have any credibility whatsoever. It seems like it is a free-for-all and a very intense competition to get the very lucrative investment banking relationships and to increase the profits from them. Therefore, the analysts or the companies are evidently under severe pressure from the companies that they are rating to make those ratings conform to the company's desires or they are going to lose the business, and I think that is very alarming.

Mr. MARTIN. Senator, let me just follow on that the ratings, and who can change ratings, and when to change ratings is completely controlled by Compliance. As and when there are activities going on, the ratings get frozen. There is a black-out period where ratings cannot be changed up or down if there is an activity, if there is a capital market activity going on.

Senator DAYTON. But the fact is, your subsequent analyst raised the rating of the company, and Merrill Lynch was rewarded, as the January 1999 memo indicates, with a couple of very lucrative investment banking relationships with Enron. So there was definitely a very direct reward immediately following that change.

Thank you, Mr. Chairman.

Senator LEVIN. Thank you. These are disturbing questions, indeed, that you have raised. Senator Fitzgerald.

Senator FITZGERALD. Mr. Martin, thank you very much for testifying today.

Mr. MARTIN. Thank you.

OPENING STATEMENT OF SENATOR FITZGERALD

Senator FITZGERALD. I would like to turn your attention to Exhibit 212 in your book.[1] Exhibit 212 is a fax from Rob Furst, who was in your Dallas office, to Jim Brown at Merrill Lynch. Can you tell me who Jim Brown is? Do you know?

[1] Exhibit No. 212 appears in the Appendix on page 2079.

Mr. MARTIN. Senator, Jim Brown, I believe, has been or is the senior person in charge of Structured Finance.

Mr. FITZGERALD. Senior person in charge of Structured Finance?

Mr. MARTIN. Structured Finance.

Mr. FITZGERALD. Where is he located?

Mr. MARTIN. Physically? He is in New York. I believe he is located in the Investment Banking group.

Mr. FITZGERALD. So this fax is from Rob Furst to Jim Brown in Structured Finance in New York.

The cover page of the fax, it says, "Twenty-six pages are being faxed," and it includes some handwritten notes that appear to outline some of the risks of the Nigerian barge transaction for Merrill Lynch. It says, "foreign tax, environmental, operating performance, failure to complete." It says, "No repurchase obligation from Enron."

Do you know whether those notes were written by Mr. Brown or by Mr. Furst?

Mr. MARTIN. It is my understanding they were Mr. Brown's notes to go into a meeting.

Mr. FITZGERALD. So this is Mr. Brown in Structured Finance, and he wrote the last risk at the bottom which says, the handwritten note of Mr. Brown says, "Reputation risk; i.e., aid and abet Enron income statement manipulation."

Does that suggest to you that Mr. Brown, in charge of Structured Finance, feared that this whole Nigerian barge transaction was designed to assist Enron in manipulating their income statement?

Mr. MARTIN. Senator, what this list would indicate to me is that Mr. Brown, first of all, was doing a very thorough job. He was, to himself, writing down all of the potential risks, and again, having not been at that specific meeting, had each and every one of these vetted to his satisfaction.

Mr. FITZGERALD. So he must have discussed the reputational risk; i.e., aiding and abetting Enron income statement manipulation, he must have discussed that at a meeting with other people in the Structured Finance office in New York?

Mr. MARTIN. He would have discussed it, again, I assume he discussed it, he would have discussed it at a meeting that had people from Legal, and Credit, and Product, and Banking all together. He would have gone through a list and wanted to get comfort from his seat that these things were not a problem.

Mr. FITZGERALD. So there would have been a whole group of people at Merrill Lynch who would have been made aware of that risk that this transaction was designed to manipulate Enron's income statement, but they nonetheless went forward with this?

Mr. MARTIN. No, I think that this was a question, these are a series of questions and risks. So there would have been a group of people—again, having not been at the meeting, it is hard to be exact—but I would surmise there would have been a group of people, and each and every one of these risks would have been discussed from different points.

Mr. FITZGERALD. Let me ask you this. You are here, you have no firsthand knowledge of the Enron transactions, but you do speak for Merrill Lynch to answer questions about their policies.

Mr. MARTIN. Sure.

Mr. FITZGERALD. What is the policy, within Merrill Lynch, when it comes to assisting with transactions that are designed to manipulate your clients' income statement?

Mr. MARTIN. The policy is unequivocally not to do them.

Mr. FITZGERALD. Not to do it.

Mr. MARTIN. Absolutely.

Mr. FITZGERALD. What if a transaction comports with GAAP, and it is legal, but really it has no economic purpose, and the only reason to do it is to gin up the earnings, the reported earnings of the company? It seems to me that Enron engaged in thousands of those types of transactions, many of which do seem to have comported with GAAP.

If the sole purpose of a transaction was to manipulate the income statement, but it is legal, and it comports with GAAP, would Merrill Lynch do the deal?

Mr. MARTIN. If the transaction was legal, and if it had sign-off from Enron's advisers, our judgment, we would have a discussion, we would have a discussion about, if it was in a gray area, whether we reputationally wanted to do that or not.

Mr. FITZGERALD. And that is apparently what went on here.

From my standpoint, I think it is very apparent that Merrill Lynch, whether wittingly or unwittingly, became the investment banker to a big Ponzi scheme at Enron, along with other investment banks. You were very involved in setting up LJM2, the purpose of which, as far as I can tell, was to help Enron book fictitious earnings. You were involved in the Nigerian barge situation.

I guess, rather than beating you up by going through individual transactions, and I think the Subcommittee has many documents they are going to want to continue to ask you about today, I would want to ask you a broader question. I feel that Congress is actually ignoring the root cause of why companies are manipulating their earnings.

Just today in *The New York Times,* on the front page of the Business Section, it was disclosed that top managers at Qwest Communications cashed in $500 million worth of stock options in the last couple of years. They have all since left the company. There is a new CEO, Dick Notebaert, who happens to be from my State of Illinois, and now he is restating the earnings. But those previous managers have gotten very rich on their stock options, and the long-term investors are left holding the bag.

I actually think it is Congress's fault that we have created this situation, because back in 1993–1994, Congress put a gun to the head of the Financial Accounting Standards Board and made them back down from their Rule 123, which was going to require companies to expense stock option compensation on their income statements. I think that would have at least been some discipline on corporate America.

In the case of Enron, the top 29 managers cashed in $1.1 billion worth of stock options. Most of those managers left the company by the time it hit the wall. Unfortunately for Ken Lay, he had to come back because Jeff Skilling left. He had lined up, himself, had lined up a job with another company. My suspicion is they all knew it was a house of cards.

My guess is tons of Enrons are out there goosing their earnings, trying to keep their earnings per share high to keep the options in the money so the senior managers can cash in those options. You are seeing cases of companies actually accelerating their earnings and deferring their expenses, like WorldCom did. They just capitalized expenses.

What is Merrill's perspective, as an investment banker who sees a lot of companies on a day-to-day basis? Do you think this is a worry out there that Congress has given executives in corporate America, 90 percent of their compensations now coming from stock options, some of the executives are in a position to make tens or hundreds of millions of dollars by fictitiously posting earnings? Do you think that those stock options are a potential motivating factor in causing corporate America to fictitiously goose their earnings?

Mr. MARTIN. I think stock options, in addition to other things, would be a contributing factor to behavior, which may not be perhaps in the long-term best interests of shareholders. It may be a contributing factor. I think the short-termism and the pressure to perform, as viewed by all of the analysts, which we just previously spoke about, by shareholders, by boards is intense and seems to be getting more intense.

I think the true alignment, particularly of the officers of a company, with the long-term success and value creation of a company, would be a very worthwhile thing and something that, although I have never spoken to Merrill Lynch directly about it, I assume that Merrill Lynch would be very supportive of that.

The alignment of risk, the proper risks and rewards for the people at corporations making these decisions—we all make a lot of decisions. The big decisions take years, and years and years to unfold, whether they are right or they are wrong. So linking those together and alignment of responsibility, accountability, and rewards would be something that we would be supportive of.

Mr. FITZGERALD. Now Merrill Lynch itself uses stock options, do they not, in their employee compensation?

Mr. MARTIN. Yes, we do.

Mr. FITZGERALD. And you, yourself, have stock options; is that correct?

Mr. MARTIN. I have a few, yes.

Mr. FITZGERALD. You have a few. Now does that give your investment bankers the incentive to help drive up business however possible to keep the earnings flowing so that their individual stock options can stay in the money, and they can cash them in before they expire? Do you think that that is itself an incentive within Merrill Lynch to ignore the reputational risk to Merrill Lynch to go ahead, get those extra fees, keep Enron as a client? What do you think?

Mr. MARTIN. I think that we have a saying, at least at Merrill Lynch, that no transaction or no one person's bottom-line P&L, one person being a business unit, is more important than the reputation of Merrill Lynch. That is the way we behave and act.

Mr. FITZGERALD. Do you know whether Mr. Furst got any stock options and whether he has cashed them in? And now my guess is he's leaving the company; is that correct?

Mr. MARTIN. I believe he is no longer with us.

Mr. FITZGERALD. Can you look into that and tell us what stock options he has exercised, and maybe he has already profited from that.

Mr. MARTIN. OK.

Mr. FITZGERALD. Well, with that, I suppose we will have further opportunities to get into more specifics this afternoon.

Incidently, Senator Levin and I have a bill that would kind of undo some of the ill effects from Congress's actions in 1993–1994. I am pleased that some companies are voluntarily expensing their stock option compensation expense. I am very fearful that there are many more Enrons out there and that the root cause of it is powerful motivation in the hands of managers to book current earnings, cash in their stock options. They can leave the company before the restatements. Their fortune is assured, but the long-term investors are left holding the bag.

I wish that Congress would have the courage to address this. It seems to me that almost every executive in America who has stock options is dead set against having to record them as a compensation expense on their income statements, and the earnings of almost every company in America are grossly overstated because the compensation expense is just ignored on the income statement.

But thank you very much, Mr. Martin.

Mr. MARTIN. Thank you.

Senator LEVIN. Thank you, Senator Fitzgerald. Senator Durbin.

Senator DURBIN. Thank you, Mr. Chairman.

Mr. Martin, thank you for being here.

Mr. MARTIN. Thank you.

OPENING STATEMENT OF SENATOR DURBIN

Senator DURBIN. For the record, before joining this inquiry into the corporate culture of America, I would like to take a moment and make an observation about the notion of justice in America. If you follow the morning papers, you realize that a professional basketball player is in the news for misdemeanor charges that he engaged in threatening conduct, and because of that threatening conduct, he faces a maximum jail term of 5 years.

I want to make a point of that for the record because all that we have heard and described about the conduct of the Enron Corporation. As we sit here today, there is still not a single officer of Enron who has been charged by this government for any wrongdoing. That professional basketball player faces more jail time than any officer of Enron today as we enter into this discussion.

Second, I would like to note that there is a Hollywood actress who has been accused of shoplifting, and I would like to make a point that whatever the amount that she shoplifted, she is facing the prospect of more jail time than any of the employees of Merrill Lynch who were involved in what led to the agreement between the State of New York and Merrill Lynch, because of conflicts of interest and deception by the employees of Merrill Lynch when it came to the selection of stocks. I am going to ask Mr. Martin for some detail on that in a moment, but what I have read in press accounts suggests that analysts at Merrill Lynch were intentionally deceiving the clients of that company about their true feelings concerning the value of companies, compromising in the process the savings,

the investments, the retirements, and sometimes the lives and futures of a lot of innocent people.

The net result of that misconduct was a fine on Merrill Lynch in the amount of $100 million, a substantial amount of money for the average person. But according to the *New York Times,* that fine represented less than one-third of what Merrill Lynch paid for office supplies and postage in the previous year.

As I said, I hope that we will keep in perspective the notion of justice in America when we are talking about misdemeanor charges and jail time for shoplifting and threatening conduct that far exceed any of the penalties which we are imposing on wrongdoers in this corporate corruption scandal.

Mr. Martin, tell me, if you will, why Merrill Lynch agreed to pay the $100 million to New York and other States.

Mr. MARTIN. Senator, I am not in a position to answer that. I was not involved in those discussions, the dialogue, the decision-making process. Unfortunately, I am just not in a position to answer that question.

Senator DURBIN. Well, do you know? I mean, what is your position at Merrill Lynch?

Mr. MARTIN. I run the International Private Client business.

Senator DURBIN. Are you aware of the nature of the charges against Merrill Lynch which led to the payment of this fine?

Mr. MARTIN. Only broadly.

Senator DURBIN. Can you tell me, broadly, what they were?

Mr. MARTIN. I think there was an allegation that there was undo influence by certain parts of the firm on our research process.

Senator DURBIN. How was that manifest? Was it not manifest in emails that were brought to the attention of the attorney general of New York, where analysts at Merrill Lynch were, in fact, advising clients to buy certain stock which they had personally said in email was not valuable or not of great worth; is that not the nature of this charge?

Mr. MARTIN. Senator, I am just not prepared to have a dialogue on that.

Senator DURBIN. Mr. Martin, I am glad you are here today, but you are of very little value to us, and perhaps that is why you are here today.

Mr. MARTIN. Thank you.

Senator DURBIN. You were able to suggest that you are carrying the banner for Merrill Lynch, but just have plausible deniability on every single thing that we ask. Thanks for joining us, nevertheless.

Let me ask you about your testimony because I am curious. There are two things that come out of your testimony that do not square. One is, early in the testimony, on page 4, where you go to great lengths to suggest that the relationship between Merrill Lynch and Enron was modest and minimal. Those are your words. Do you recall that part of your testimony?

Mr. MARTIN. Yes, Senator.

Senator DURBIN. And then on page 10, when you talk about the problems dealing with research in your testimony and the lengths to which your company went, to try to win back the confidence of your buddies, your friends and colleagues at Enron, you refer to this as a longstanding relationship worthy of these extraordinary

efforts. That seems to be in contrast. At one point, this is a client of very little importance, and then by page 10, it is a client that, when it expresses misgivings about your ratings by Merrill Lynch of Enron, is worth all of this extra effort to win back their friendship. Can you explain the difference?

Mr. MARTIN. Senator, there is a difference between relationship—the importance of the Enron relationship, again, going back in time, was accurately stated; large, important relationship. Again, $40 billion in revenue, growth company, leader in the industry, leader in technology, leader in the thought processes of corporate America, so it was a critical relationship for us, no doubt.

The facts are, from a business point of view, it was a small account. Again, our investment banking revenues, which I went through on page 4, $3.5 to $3.7 billion of investment banking revenues on an annual basis, and the Enron investment banking fees to us were two-tenths of 1 percent of that number. So it was a small account as far as activity, a very important account as far as both current relationship and potential relationship.

Senator DURBIN. Mr. Martin, I could dwell on that particular comment because, in a memo on January 18, 1999, someone from the Investment Banking Division notified your president on an update on Merrill's relationship with Enron, since your president spoke to Mr. Lay concerning "our difficult relationship in Research," and went on to say, in so many words, things are back on track between Enron and Merrill Lynch now, since we have got some new ratings out. And he concluded by saying, "Total fees to Merrill Lynch for two transactions," which are referred to here, significant mandates by Enron alone would be worth[1] "$40 to $50 million."

So, when you talk about a million dollars, and $2 million and $8 million, it appears that this email raises a question as to whether it was a much larger relationship, but I do not want to dwell on the difference in dollars and how big it was to your bottom line. I guess it really comes down to a more fundamental question.

For the individual investor relying on Merrill Lynch's recommendations and analysis to make important life decisions about their savings and their pensions, whether Enron represented 1 percent or 10 percent of your bottom line is insignificant. They trusted you. They believed that you were the cop on the beat; that Merrill Lynch was giving them good, solid information. But instead of being the cop on the beat, you were the dog in the lap.

It appears that what occurred here is that once pressure was put on Merrill Lynch, because this seventh largest corporation in America disapproved of being rated neutral, that your officers, including your president, scrambled, hat in hand, to try to win back the love and affection of Enron. I mean, by every indication, that is what occurred. How does that, in any way, enhance Merrill Lynch's reputation for trustworthiness?

Mr. MARTIN. The research process that we have at Merrill Lynch is extremely rigorous. It is separate from the rest of the firm. We probably cover more stocks, and more locations, and more countries in the world than any other institution.

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[1] Exhibit No. 240 appears in the Appendix on page 2209.

If you look at the facts about our research and the performance of the stocks that the research recommends, it is, year in and year out, if not the leader amongst the top two or three leaders as far as providing accurate, concise, balanced research on companies.

Enron, in question, the various analysts that we had, the two different analysts, each came up with the conclusion that, from a long-term perspective, that Enron was a company to buy. They were not alone in that. There were 40 or 45 other analysts on Wall Street who also covered Enron, almost all of them as positive. We try very hard and work very hard, as a research provider, to give unbiased, consistent, long-term research to our individual investors and our institutional investors, and we do not get everything right as human beings, but we very much take seriously the responsibility we have.

Senator DURBIN. Mr. Martin, I think there are enough disclaimers on everything that the stock analysts do to give their recommendations and say past performance will not necessarily predict future results and so forth. I know that. I own stock. Most people do in this country. I understand those disclaimers, and I understand people can miscalculate and guess something big is going to happen or something bad is going to happen, neither of which occurs.

But what has been raised here is a question of conflict of interest and deception, and that is much different. To make an honest mistake in analyzing the future performance of a company is one thing, to be so intricately enmeshed in the business dealings of Enron that your company is not playing it straight is another thing.

The point I would like to close with is this. You have repeatedly made reference to a Chinese wall. I might just say, as far as that analogy is concerned, that a Chinese wall may have been a great challenge to breach a thousand years ago, but it is not today, and I happen to believe that without strong laws and meaningful penalties, the Chinese walls built by corporations are not enough to restore the confidence of the average person in this process. If that confidence is not restored, not only will your company suffer, but this economy will suffer.

Thank you, Mr. Chairman.

Mr. MARTIN. Thank you.

Senator LEVIN. Thank you, Senator Durbin.

You just told Senator Durbin that "Research is separate from the rest of the firm." Why was Olson then peddling the Enron stock offering?

Mr. MARTIN. Organizationally, the way it is structured in Merrill Lynch is Research reports to Research who reports to somebody who is executive vice president on the Executive Committee who reports to the president. So Research is not imbedded in the investment bank or the consumer business. It is a separate entity. It is a separate function. It obviously has dealings with the different parts of the firm, but it is run as a separate function with checks and balances.

Senator LEVIN. Which reinforces my question. Why was he peddling stock then?

Mr. MARTIN. He was not—I do not know what he was doing. I do not necessarily think he was peddling stock.

Senator LEVIN. Have you not seen the notes that you made reference to before? You said it was ordinary that notes of conversations that somebody like he would have in offering stock would be made available to the company whose stock offering it was. You said that was very common.

Mr. MARTIN. It is not unusual.

Senator LEVIN. My question is why was he peddling Enron stock if he is an analyst, when you said the Research Division is separate from the rest of the firm? It is a very fundamental question.

Mr. MARTIN. The role of the analyst, in a capital market transaction, is usually to provide content and depth of a topic. So the role he most likely played was talking to accounts with the sales people, and the accounts asking him in-depth questions that only an analyst can answer about Enron.

Senator LEVIN. Enron seemed to have so much trouble with his analysis that they wanted him removed from the scene. So it is not just making phone calls and getting responses, he was analyzing Enron; is that not correct?

Mr. MARTIN. He is the analyst for Enron.

Senator LEVIN. My question is what is he doing then peddling Enron stock if there is a Chinese wall.

Mr. MARTIN. In that process——

Senator LEVIN. There is not even a wall.

Mr. MARTIN. In that process, in the distribution process, the analyst would provide, the analyst would be the content expert for both the industry and that company, and they would provide that expertise to the account base and to the sales force to give them answers to questions that they were going to have.

Senator LEVIN. So you are saying he did not initiate calls?

Mr. MARTIN. No, he is going to be making——

Senator LEVIN. Let me ask that clearly. Are you saying he did not initiate calls; he only was responding to calls?

Mr. MARTIN. No. With regard to what he was doing specifically, I do not know. What I am trying to respond to and give you a frame of reference on is that an analyst can be involved, and will often be involved, if there is an equity issuance, to provide what an analyst has spent a lot of time doing, which is depth of coverage and content.

Senator LEVIN. Can you take a look at Exhibit 243.[1] These are calling lists from John Olson for the Enron Corporation common stock offering as of today. It says call list. He goes through all of the calls.

No. 2, likes the story; No. 5, likes the story; left voice mail, Enron story, No. 7; No. 8, Enron story; No. 9, Enron story; No. 12, Enron story. He is telling the Enron story. No. 13, will probably pass.

He is not responding to questions here. He is pitching. In fact, in your own words, I think he said he was pitching.

Will consider it. He is leaving all of these voice mails. He is not responding to inquiries here. He is leaving voice mails with the

[1] Exhibit No. 243 appears in the Appendix on page 2212.

Enron story. He is pitching. Day after day after day he is pitching. There are three different days of call sheets here. That is not a Chinese wall. There is no wall. You have got your Research people, who are supposed to be making a pitch for the stock that you are selling, and that is one of the most disturbing features of this matter.

Do you have any further comment on this?

Mr. MARTIN. Again, Mr. Chairman, it is—I see this list of clients, it is not unusual for a Research person to work with the institutional sales group, because these are all institutional sales people, about trying to provide insight into the company that they are analyzing, but I cannot speak for all of these various calls and things.

Senator LEVIN. Do you want to qualify or rethink your statement about Research being separate from the rest of the firm?

Mr. MARTIN. Well, I will qualify it. The organizational construct of Research is designed at Merrill Lynch to provide an organizational distinctiveness to that function.

Senator LEVIN. Well, it may be created for that purpose, but it sure as heck is not functioning in that way, by your own evidence. You have got a pitch man here in your Research Department.

Mr. Martin, let me ask you about another document. You told me earlier that the Debt Management Commitment Committee bumped the decision on the barge transaction upstairs. I want to go back now to the barge transaction, and you mentioned, I think, that it may have gone to Tom Davis.

Now the Subcommittee staff has been informed that the decision was sent to either Mr. Davis or Mr. Bayly. So is it possible that Mr. Bayly, instead of Mr. Davis, made the decision on this?

Mr. MARTIN. Again, I do not have the direct knowledge or involvement, but from a process point of view, the person who should have made the decision is Tom Davis.

Senator LEVIN. Will you take a look at Exhibit 207,[1] because Mr. Bayly, I take it, was one of the—can you give us his title?

Mr. MARTIN. He is chairman of Investment Banking.

Senator LEVIN. Chairman of Investment Banking?

Mr. MARTIN. The Investment Banking team.

Senator LEVIN. Now this, if you look at Exhibit 207, this is what the chairman of Investment Banking is going to do, according to the notes of Mr. Furst. If you look at the bottom now, here is the chairman of the Investment Banking Committee.

"Dan Bayly will have a conference call with senior management of Enron confirming this commitment to guaranty the ML takeout within 6 months." That is what Mr. Furst's memo says. That is what the head of this Subcommittee is going to do. He is going to confirm a commitment to guarantee the takeout.

Now do you know whether that conference call, in fact, took place?

Mr. MARTIN. I believe it did take place.

Senator LEVIN. Do you have the notes of that or a tape of that call?

Mr. MARTIN. I do not, no.

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[1] Exhibit No. 207 appears in the Appendix on page 2059.

Senator LEVIN. Have you done an investigation as to what he said in that call?

Mr. MARTIN. I have not, no.

Senator LEVIN. Has Merrill?

Mr. MARTIN. I do not know if Merrill has.

Senator LEVIN. This is the most critical issue on this matter that the Subcommittee is looking at this morning, is whether or not that guarantee was made the way all of the evidence, contemporaneous and in writing, says it was made. This is directly on point. "Dan Bayly will have a conference call with senior management of Enron confirming the commitment to guaranty the takeout," and you are coming before this Subcommittee and telling us that you do not even know if Merrill Lynch has asked Mr. Bayly whether or not that call, in fact, contained that kind of——

Mr. MARTIN. I assume they either have or are, but I do not know, in fact, whether that has occurred.

Senator LEVIN. I do not assume either. I wish I could.

Would you get us the notes of any conversations that Merrill Lynch has had with Mr. Bayly about that call?

Mr. MARTIN. Yes.

Senator LEVIN. Why did you not inquire about that before you go there today, since it is such a central matter?

Mr. MARTIN. The original role I was asked to play was to provide a Merrill Lynch perspective, a policy perspective, and a broad perspective on ML and Co, and how it, particularly from a process point of view, would have been involved in all of these, which is what I spent the last several days doing. So the role I was expected to play is the role I am trying to play. I was not going to get prepared to discuss each and every one of these transactions, having not been in them.

Senator LEVIN. Mr. Martin, you have testified here today that there was no guarantee, and you have said that under oath. Here is a document which says that Mr. Bayly will have a conference call with the management of Enron confirming this commitment to guarantee, and you are appearing in front of this Subcommittee, under oath, saying you have made no inquiry, you do not know whether or not Merrill Lynch has made any inquiry as to the content of that call, as to whether Mr. Bayly, in fact, said that.

I find that totally impossible, frankly, to accept because you are representing a firm. You made the statement today there was no guarantee, and yet, and no understanding by Merrill Lynch that Enron or any entity related to Enron would buy back Merrill Lynch's shares. How can you make that statement without having made the inquiry or knowing about whether or not Merrill Lynch has even inquired of Bayly, who is the head of your Credit Division there, about the content of that conference call? I do not even know how you could come before this Subcommittee and make the statement that there was no understanding, in the face of this document saying that the head of your whole division here was going to confirm that understanding.

Mr. MARTIN. Again, Mr. Chairman, it is, in my preparation for my role here, I knew that there was—had been made aware that there was a conference call. I am not aware of what the content of that conference call was, having not been on it. Again, I know

it is easy to assume, but my assumption is that Merrill Lynch has spoken with Mr. Bayly at some length about this topic and we would be happy to send you all of the notes and information on that.

Senator LEVIN. Mr. Martin, let me wind up this segment by just, on this particular issue, and I am going to be moving on to the other aspects, after I call upon Senator Collins, but basically the claim that the barge deal was a purchase by Merrill Lynch and that there was a real sale by Enron is just simply unbelievable, and the documents of Merrill Lynch are just so full of references to a guarantee, and a commitment, and an assurance that is contemporaneous, that it is incredible to believe that this was a real purchase.

The fact that it was booked as a purchase by Merrill Lynch is not evidence of the fact that it was a real purchase; in fact, quite the opposite. The question is why would Merrill Lynch book this as a purchase, in the face of all of the contemporaneous evidence that, in fact, it was a "relationship loan," to use the words of a Merrill Lynch employee. That is the issue. It is not evidence that it was a purchase. It raises the question very dramatically as to how could it be booked as a purchase in the face of all of that contemporaneous, documented evidence.

There is also, in addition to that contemporaneous evidence, the statements of employees of Merrill Lynch to the staff of this Subcommittee that Merrill Lynch would not have entered into the transaction, but for the pledge by Enron to take out Merrill Lynch from the barge transaction within 6 months. Enron, in fact, found a buyer on the date that it had promised, and it had to do so by using its own entity of last resort, LJM2. The agreement up front that you were going to get the $250,000, and then 15-percent interest on the $7 million was very clear. It is exactly what you got when LJM2 transferred the $7 million on the scheduled date.

So the claims of Merrill Lynch here are too thin, and we are not that naive. There was all of the motivation in the world to book this as a sale to please Enron and to make sure that Enron's own financial treatment and deception was not countered by the way in which Merrill Lynch treated it in its own books. You tried to stuff a loan into what was supposed to be the skin of a sale, but the skin is just too thin, and I think we can see right through it, and hopefully you can, too, at Merrill Lynch.

Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman.

Mr. Martin, I want to go back to the issue of John Olson's calls, because like the Chairman, I am convinced that these were calls where he is trying to sell the stock, as opposed to your explanation of answering questions from institutional investors. By my quick count, it looks like Mr. Olson made at least 110 calls. Let me give you some of the comments, just taking three of the calls, one of them Mr. Olson noted.

One records his conversation with a Rod Mitchell at the Mitchell Group. He says, "Wants to buy cheaper. He is a bargain hunter."

Another one is with Barbara Friedman from John Hancock. "Likes the idea. Will consider it. Does not own now."

A third, Barry Allan at Putnam. "Thinks the price is too high. Might buy at $44 to $45."

Would you agree that these are calls where Mr. Olson was trying to sell the stock?

Mr. MARTIN. Senator, as we went through the information before, having not been there and having not listened to phone calls, and who was there, and who was not there, it is hard for me to answer. The answer is I do not know.

Senator COLLINS. If you look at the comments that Mr. Olson recorded, and it is clear that he initiated the call because in many cases his comment is "left voice mail/Enron story," what other conclusion could one reach?

Mr. MARTIN. Again, the role of an analyst in these discussions can be multiple, but the one, I do not know what he was speaking about, I do not know if he was the only person on the phone call, I do not know if there were other sales people, I do not know if he was playing a role that was supportive. I just do not know.

Senator COLLINS. Mr. Martin, on three occasions Merrill sent Enron executives copies of these call sheets listing Mr. Olson's calls. Is it common for Merrill to provide companies like Enron with copies of analysts' internal call sheets to clients?

Mr. MARTIN. During a deal, during a capital market deal, it is not uncommon to, particularly with CFOs of corporations, to share with them feedback on specific, for specific clients. It is not uncommon.

Senator COLLINS. If Mr. Olson was making calls touting the stock, as I believe is evident from the call sheets, and he was a research analyst responsible for rating the stock, is Merrill precluded from having a research analyst make such calls as a result of its settlement with the New York State attorney general?

Mr. MARTIN. That, Senator, I do not know, specifically. I would be happy to follow up on that.

Senator COLLINS. Are you unfamiliar with the attorney general's settlement?

Mr. MARTIN. I am familiar with it in broad terms.

Senator COLLINS. Do you think Enron's complaints about how it was rated by this research analyst would have been handled differently now that Merrill Lynch has entered into a settlement with the attorney general?

Mr. MARTIN. Again, I do not know the specifics of the agreement—agreement and agreements—that we have in the settlement with the New York attorney general. I can say with regard to Enron and its ratings, again, both Olson and the new analyst had the same exact rating as far as long term. And, in fact, when Olson moved from Merrill Lynch to another firm, even before our analyst came out, he came out with a short-term buy and a long-term buy.

So, with regard to our behavior and change specific to the New York attorney general, I just—I'm not in a position to answer that.

Senator COLLINS. Was Mr. Olson forced to leave or encouraged to leave because Enron complained to Merrill about his ratings?

Mr. MARTIN. It is my understanding it was not specifically tied just to Enron; it was tied to——

Senator COLLINS. Was that one of the factors?

Mr. MARTIN. I believe not. What we were doing in the Research group at the time was there was a whole host of these companies that seemed to look like—looked different. So, specifically, Williams Company, and Coastal and a few others, we wanted to group together under one analyst. So there was a restructuring of analyst coverage. And so a bunch of companies that heretofore been covered by different people were put under one analyst. So his job, his specific job was eliminated as the restructuring occurred.

Senator COLLINS. Is it your testimony that Mr. Olson's departure was not, in any way, connected to the criticism that Merrill executives received from Enron?

Mr. MARTIN. That is my testimony.

Senator COLLINS. Thank you, Mr. Chairman.

Mr. MARTIN. Thank you.

Senator LEVIN. Just an additional question or two relative to the Olson matter. Has Merrill Lynch made an investigation as to whether or not there were conversations with Mr. Olson about his analysis of Enron stock?

Mr. MARTIN. I am sorry, Mr. Chairman. Was there an investigation by Merrill Lynch on his analysis of Enron?

Senator LEVIN. Has Merrill Lynch asked—have they investigated whether there were discussions with Mr. Olson about his analysis of Enron stock?

Mr. MARTIN. I do not know.

Senator LEVIN. That is a very important issue before the Subcommittee, obviously, today, and would you make inquiry as to that and send us a copy of those notes of conversations relative to that subject and any investigation into that?

I would think that Merrill Lynch would want to investigate that. Since it has made the claim that there is a wall, one would think that it would want to see whether or not, in fact, there was such a wall or whether it functioned in any semblance of way during this process. It sure did not look like a wall to me, it looked like a ditch.

But if you would furnish that, for the record.

Mr. MARTIN. Yes, I will do that.

Senator LEVIN. Thank you. You do know that Mr. Allison did call Ken Lay and Jeff Skilling in an attempt to have Merrill Lynch inserted as a co-manager, those calls were made?

Mr. MARTIN. That is my understanding, yes, sir.

Senator LEVIN. Do you know what Mr. Allison told Mr. Lay and Mr. Skilling in those calls?

Mr. MARTIN. No, I do not.

Senator LEVIN. Would you make inquiry—I would think that that would be a fairly important issue to Merrill Lynch; it is to us—and let us have a copy of that inquiry when you make it?

Mr. MARTIN. Yes. We'll have that done.

Senator LEVIN. Exhibit 242 [1] has been referred to in some detail. I am not going to go over the material that Senator Dayton and others have gone over in this regard, except to point out in the middle line there called "Background" that this is to Dan Bayly from Schuyler Tilney, and it says, "As you know, Merrill Lynch was

[1] Exhibit No. 242 appears in the Appendix on page 2211.

nearly excluded from Enron's $750 million common stock offering earlier this year. So this mandate is critical to reigniting our relationship with Enron." That is how important it was to Merrill Lynch.

Do you know whether or not any supervisor or anybody above the analysts in the chain of command at Merrill Lynch ever discussed with Mr. Olson the fact that Merrill Lynch lost a lucrative deal solely because of his or, in part, because of his research activity? Do you know whether or not any supervisor or anyone above him——

Mr. MARTIN. Mr. Chairman, I do not know.

Senator LEVIN. Would you make inquiry and let us know?

Mr. MARTIN. Yes.

Senator LEVIN. And, if so, what the result of that inquiry was.

Mr. Martin, you said a moment ago that it is your testimony that Mr. Olson's departure was "not in any way related to his Enron rating." That is not our understanding, and I am wondering whether you wish to qualify your statement.

Mr. MARTIN. I thank you for the opportunity to qualify, but I am comfortable with the statement, Mr. Chairman.

Senator LEVIN. You what?

Mr. MARTIN. I am comfortable with the original statement.

Senator LEVIN. Thank you.

Let me turn now to LJM2. In September 1999, Andrew Fastow, Enron's chief financial officer, and Michael Kopper, his right-hand man, made a presentation to a Merrill Lynch investment team to pitch a proposal for LJM2, which is a private investment fund established to make its money primarily from transacting business with Enron.

Mr. Fastow was to be the general manager and then equity holder of LJM2 at the same time he continued his job as Enron CFO. Three others—Mr. Kopper, Ben Glisan, and Anne Yaeger—would also work at LJM2, while maintaining their full-time jobs at Enron.

In September, Mr. Fastow was looking for help in raising about $200 million in capital for LJM2. Without that money, LJM2 could not do anything. It was the fuel that LJM needed to act. Mr. Fastow made his pitch to Merrill Lynch on September 16, 1999, at its offices in New York.

During the course of the Subcommittee investigation, Merrill Lynch provided a 50-minute videotape that captured some of Mr. Fastow's pitch to the Merrill Lynch team, and we have edited that tape down to about 7 minutes. And I would ask that it run now, but before it starts running, there is a transcript which is available. I think this is Exhibit 206(a).[1]

I wonder if we could just play these excerpts.

[Videotape played.]

Senator LEVIN. We will come back to that chart in a minute, why LJM2 is unique.

[Videotape played.]

Senator LEVIN. Mr. Martin, were you at that briefing?

Mr. MARTIN. No, Mr. Chairman.

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[1] Exhibit No. 206(a) appears in the Appendix on page 2054.

Senator LEVIN. This Subcommittee has already looked at the LJM2 transaction in some depth at earlier hearings, and what we found after interviewing 13 Enron board members and a number of corporate governance and accounting experts is that, as far as any of them knew, it was unprecedented for a publicly traded company to allow its CFO, the person with the greatest access to the company's money flows and profit margins to set up his own investment fund to do business directly with the company.

Now Merrill was obviously aware of the conflicts of interest. If you look at Exhibit 246,[1] this is from Schuyler Tilney and Robert Furst, the two people who were before us early this morning, briefly. The subject is, "Skilling Questions on LJM2."

"We would like to have a conversation with Jeff about LJM2. Our questions are as follows:"

And then No. 3, "Are you comfortable with the internal mechanics put in place to resolve the conflict-of-interest issue? Have these internal policies been reviewed with internal and external counsel and the board?"

Now that is the question which Merrill Lynch is asking Fastow, who is involved in the conflict. Of course, his answer comes back, if you will see the next document, where it says that on October 11, which is 4 days after that first memo, Mr. Tilney first spoke with Jeff Skilling, president and COO of Enron Corporation. "We asked Jeff the questions listed on the memo. It was apparent he has spent a great deal of time on LJM2 matters, and he is comfortable," it says here, "with the conflict-of-interest issue for the following reasons," and then gives the reasons that he, the person who is involved in the conflict or who, on behalf of Enron, approved the conflict is saying why he approved it on behalf of the corporation.

But that does not, it should not satisfy Merrill Lynch. Merrill Lynch now has the problem, the dilemma, which was raised by your own people as to whether or not you want to participate in a transaction where there seems to be a conflict. Instead of asking the company that is involved, it would seem to me you would ask your own legal counsel as to whether or not it would be appropriate to participate in that transaction and to sell that LJM2 stock.

My question to you is did you get a legal opinion about the ethics issue from your own counsel?

Mr. MARTIN. Mr. Chairman, I do not know the answer to that question.

Senator LEVIN. If you would find out if you did, would you send us a copy; and if you did not, would you let us know, for the record——

Mr. MARTIN. And that is a legal opinion on the conflict topic.

Senator LEVIN. On that conflict question.

Mr. MARTIN. OK.

Senator LEVIN. As to why, since there was a question raised as to whether or not there was not a clear conflict, which there was, and it was waived by the Enron board, but nonetheless it was a clear conflict, to have their CFO deal with them from an outside investment firm with inside information that he had.

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[1] Exhibit No. 246 appears in the Appendix on page 2235.

So now if you look at Exhibit 249,[1] which is the private placement memorandum that Merrill put together to convince qualified investors, like pension funds, insurance companies and banks, to invest in LJM2, and here is what it says. It says that "Under Mr. Fastow's management, the partnership expects to have the opportunity to co-invest with Enron in many of Enron's new investment activities and the opportunity to acquire existing Enron assets on a highly selective basis, and the access to deal flow should provide the partnership with unusually attractive investment opportunities. The partnership will be managed on a day-to-day basis by a team of three investment professionals who all currently have senior-level finance positions with Enron—Fastow, Kopper and Glisan—who will continue their current responsibilities with Enron, while managing the day-to-day operations of the partnership."

So that is repeating the pitch that Mr. Fastow made to you. If you take a look at the chart on page 2 of this transcript, this is what Mr. Fastow was telling you at Merrill Lynch why LJM2 is unique. Preferred access to proprietary deal flow is No. one; four, ability for LJM2 to evaluate investments with full knowledge; five, LJM2 speed and knowledge advantage—knowledge, knowledge, knowledge. Inside, by the way, inside information because of Fastow's dual role.

Do you know whether or not anyone from Merrill contacted the Enron board about LJM2?

Mr. MARTIN. Mr. Chairman, I do not know specifically, no.

Senator LEVIN. Would you inquire of that?

Mr. MARTIN. Yes.

Senator LEVIN. Had anyone from Merrill spoken to the board, by the way, they would have learned that the board had not authorized anyone and did not waive the conflict of interest rules relative to anyone but Fastow to participate in LJM2. Glisan and Kopper, both listed in your placement memo, were violating Enron's ethics rules, because they did not get a waiver, by working at LJM2 in addition to their inside position at Enron.

Were you aware of that at Merrill?

Mr. MARTIN. No, I was not.

Senator LEVIN. The Subcommittee report on the Enron board concluded that "No company ought to set up a fund like LJM2 because the conflicts of interest overwhelm any internal controls that are set up to supposedly keep the fund fair." We also know now that LJM2 was one of the primary devices that Enron used to cook its books through phony asset sales and other transactions that produced about $2 billion in funds flow in a 6-month period and through accounting shams, such as the so-called Raptor hedges that Enron used to hide a billion dollars in stock losses at the same time that Mr. Fastow and LJM2 investors lined their pockets with millions of dollars in profits in just 2 years at the expense of Enron's shareholders.

Looking back at this, do you believe that Merrill should have gotten outside advice before agreeing to underwrite the private offer-

[1] Exhibit No. 249 appears in the Appendix on page 2240.

ing of LJM2, given the fact that Merrill was aware of a conflict-of-interest situation?

Mr. MARTIN. Mr. Chairman, I believe that, from a due-diligence point of view, that we should have done everything possible to ensure that we got comfortable with the conflict.

Senator LEVIN. Let me conclude by saying just a few words about today's hearing and last Tuesday's hearing, because we have been looking at, and we continue to look at the role of financial institutions and Enron's collapse.

Last week's hearing looked at Citibank and Chase and their role in $8 billion of financing that Enron never reported on its books as debt.

Today we looked at Merrill Lynch and its willingness to put its "balance sheet to work" for Enron in order to position itself to get Enron's business.

We have looked at a number of troubling interactions between Merrill and Enron. First, the Nigerian barges. We looked at a $28-million transaction involving Nigerian barges that Enron used to improperly inflate its 1999 earnings by $12.5 million, after claiming an end-of-the-year sale to Merrill, but the sale to Merrill was conditioned on a guarantee, a guarantee that Enron would take Merrill out of the deal within 6 months and pay Merrill not only a $250,000-up-front fee, but also a 15-percent return on Merrill's cash investment of $7 million. That guarantee meant there was no real sale at all.

Merrill has contradicted, in its testimony, the contemporaneous documents, saying that those documents do not really mean what they say. Well, that is what last week's inadequate, and may I say feeble, explanation was as well.

The facts are that the documents show that Merrill got a promise from Enron to take them out of the deal within 6 months at a specified profit and that LJM2 met that promise by buying Merrill's interest in the barges by the end of June for $7.25 million. Nothing says it more eloquently than the internal document at Merrill Lynch that says that the most unusual transaction of the week was the request to approve Enron's relationship loan.

The second transaction we looked at had to do with a $750-million Enron stock offering, from which Merrill was initially excluded by Enron due to Merrill's analyst's visceral reaction—excuse me—due to Enron's visceral reaction to Merrill's investment research on the company.

Within months of Enron's complaint, the analyst who had given Enron the equivalent of a neutral rating had left Merrill, a new analyst was assigned to the company, and by November 1998, Enron's investment rating was upgraded to the equivalent of a buy.

The third one was the LJM2 offering. We looked at Merrill's lead role in underwriting the $390-million private offering of LJM2, the off-the-books partnership which was run by Enron's CFO, who had clear conflicts of interest, and that was a major contributor to Enron's accounting deceptions and downfall. Merrill was aware of the potential conflicts involved in LJM2, but did not seek, apparently, outside legal counsel or other advice on whether it should participate in that underwriting. In the end, it helped raise the money which LJM2 used to help Enron cook its books.

Our investigation indicates that Enron could not have engaged in the extent, and to the extent, of the deceptions that it did without the knowing assistance and participation of major financial institutions.

The purpose of these hearings has been, and will continue to be, to set out what happened, to provide a record for possible legislative action. Of course, it is not our job to determine whether the facts that we have laid out constitute violations of securities laws or other laws prohibiting corporate misconduct. We will turn over the findings, and the information and the evidence, to the Securities and Exchange Commission, the Department of Justice, and other law-enforcement agencies who have the responsibility to make those determinations. But it is our job to build a legislative record to show what needs to change to help prevent financial institutions from participating in or contributing to accounting deceptions, to alter investment research or to finance questionable transactions.

Important advances were made by the Sarbanes accounting reform bill, which I strongly supported, which has now passed both Houses of Congress and which is awaiting the signature of President Bush. Additional steps are being taken by the SEC, the New York Stock Exchange and other bodies. The key to the success, however, of the changes which need to be made is whether the financial institutions themselves will address the problem that needs correction.

So far, the institutions which have appeared before us—Citibank, Chase and Merrill—have not acknowledged any problem in the way in which they handled Enron. And while the case histories presented during these hearings of the problems that indeed were in existence and did exist with the way in which financial institutions handled Enron, these three financial institutions are not the only ones that dealt improperly with Enron.

So the question that now needs to be asked and which we will leave this hearing with is whether the financial institutions in this country are going to acknowledge the problems, step up and make the changes that need to be made internally as a result of the events that have been so tragically unfolding in the fall of Enron and since.

I can only hope that the financial institutions will carry out their responsibility, and I know that each of us on this Subcommittee are determined that we will carry out our responsibility.

We thank you for coming forward today, Mr. Martin, and we will stand adjourned.

Mr. MARTIN. Thank you, Mr. Chairman.

[Whereupon, at 1:03 p.m., the Subcommittee was adjourned.]

APPENDIX

TESTIMONY OF ROBERT ROACH
CHIEF INVESTIGATOR
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS
THE ROLE OF THE FINANCIAL INSTITUTIONS IN ENRON'S COLLAPSE

July 23, 2002

Mr. Chairman, Ranking Member, Members of the Subcommittee, good morning.

Earlier this year Chairman Levin directed the Subcommittee staff to investigate the role of financial institutions in Enron's collapse. The Subcommittee staff – both Democratic and Republican – have worked for the past 7 months on a bipartisan basis to conduct this investigation. We have worked together to review over a million pages of documents and interview dozens of witnesses from Enron, Andersen, other accounting firms, credit rating agencies, and a host of financial institutions including Barclays, Citigroup, Credit Suisse First Boston, FleetBoston, JPMorgan Chase, and Merrill Lynch.

Numerous major financial institutions, both here and abroad, engaged in extensive and complex financial transactions with Enron. The evidence we reviewed showed that, in some cases, the financial institutions were aware that Enron was using questionable accounting. Some financial institutions not only knew, they actively aided Enron in return for fees and favorable consideration in other business dealings. The evidence indicates that Enron would not have been able to engage in the extent of the accounting deceptions it did, involving billions of dollars, were it not for the active participation of major financial institutions willing to go along with and even expand upon Enron's activities. The evidence also indicates that some of these financial institutions knowingly allowed investors to rely on Enron financial statements that they knew or should have known were misleading.

Our investigation, among other things, focused on one financing vehicle known as a "prepay." A prepay is commonly thought of as an arrangement in which one party pays in advance for a service or product to be delivered at a later date. Companies use prepays to receive money up front for services to be rendered in the future.

Enron constructed elaborate, multiparty commodity trades that they called prepays in order to book the proceeds from the prepays as cash flow from operations. But when all the bells and whistles are stripped away, the basic transaction fails as a prepay and what remains is a loan to Enron using a bank and an obligation on Enron's part to repay the principal plus interest. With that being true, the proceeds of the so-called prepay transaction should have been booked as debt and cash flow from financing, not as a trading liability and cash flow from operations.

In order for transactions like the ones used by Enron and the banks to be legitimately booked as a trading liability and not debt, four elements had to be present:

- The three parties had to be independent.
- The trades among the three parties could not be linked.
- The trades had to contain price risk.
- There had to be a legitimate business reason for the trades.

The Enron type prepays we examined failed on all accounts:

- Two of the three parties in the Enron trades were related, that is the banks and their offshore special purpose entities which the banks established and controlled.
- The trades among the parties were linked, that is contracts associated with the trades were designed so that a default in one trade affected the other trades.
- There was no price risk. Except for fees and interest payments, the final impact of the trades was a wash.
- Neither the banks nor the banks' special purpose entities had a legitimate business reason for purchasing the commodities used in the trades.

Let me describe the structure and operation of these sham prepays. [Appendix C and Appendix D that discuss the details of the prepays have been submitted for the record.]

Enron used these so-called "prepay" transactions to obtain more than $8 billion in financing over approximately 6 years, including $3.7 billion from 12 transactions with Chase and $4.8 billion from 14 transactions with Citgroup. This $8 billion figure is a conservative estimate for the 6 year period, based on the documents we were able to review; the full amount since Enron began using prepays in 1992 may be much larger. Barclays, Credit Suisse First Boston, FleetBoston, Royal Bank of Scotland, and Toronto Dominion participated in over $1 billion of the prepay transactions.

Accounting for "prepay" proceeds as cash flow from operations, rather than cash from financing gave the impression that the money from the prepays was part of Enron's ordinary business activities and not debt. Moreover, the Subcommittee has learned that Enron was simultaneously treating the prepay transactions as loans on its tax returns in order to claim the interest expense as a business deduction.

Enron's practice of using prepay transactions to understate debt and overstate cash flow from operations made its financial statement look much stronger. That, in turn, helped Enron maintain its investment grade credit rating and support, even boost, its share price.

The Subcommittee has done an analysis of what Enron's financial statements would have looked like had it accurately recorded the "prepay" transactions as debt. Please look at this chart, which is marked as Exhibit 104. The chart shows key figures from Enron's year 2000 financial statements, the last audited financial statements that the company filed with the Securities and

Exchange Commission. The financial statements showed that Enron had total debt in 2000 of about $10 billion, and funds flow from operations in the range of $3.2 billion. We know from an Enron Board presentation that, at the end of 2000, Enron had about $4 billion in outstanding financing from its so-called "prepays." If Enron had properly accounted for these transactions, its total debt would have increased by about 40% to about $14 billion, and its funds flow from operations would have dropped by almost 50% to about $1.7 billion. Those are dramatic changes.

The impact on Enron's key credit ratios would also have been significant. These credit ratios are the ratios that financial analysts typically use to evaluate a company's financial health. With the inclusion of the prepays as debt, Enron's debt to equity ratio would have risen from about 69% to about 96%. Its debt to total capital ratio would have risen from 40% to 49%. And its funds flow interest coverage, a key measure of a company's ability to meet its financing obligations, would have dropped by almost half, from 4.07 to 2.37. The credit rating agencies testifying in the next panel will discuss the significant effect these numbers would have had on Enron's credit rating.

Any credit rating downgrade would have had serious consequences for Enron, including raising its borrowing costs, limiting the investors who could buy the company's bonds, weakening its trading status, and possibly triggering certain demand debt repayments at off balance sheet entities affiliated with the company. Enron was acutely aware of the importance of its credit rating and its financial ratios.

The Subcommittee staff has additional analysis regarding the financial impact that would have resulted if Enron had accurately reflected its "prepay" proceeds as debt, including drops in the company's enterprise value and a significant drop in its implied share price. In the interests of time, however, I will submit that analysis for the record and answer any questions you may have about it. I also ask that the other appendices to my statement be included in the Subcommittee's hearing record.

Enron was able to book "prepay" proceeds as cash flow from energy trades rather than cash flow from loans only with the assistance of the financial institutions. The banks provided the funding for the prepays, participated in the required complex commodity trades, and allowed Enron to use their offshore entities that they controlled as sham trading partners, for the explicit purpose of allowing Enron to disguise multi-million-dollar loans as trading activity.

Internal communications show that it was common knowledge among Enron, Chase and Citigroup employees that the "prepays" were designed to achieve accounting, not business, objectives and that Enron was booking the "prepay" proceeds as trading activity rather than debt. The evidence indicates that Chase and Citigroup not only understood Enron's accounting goal - increasing operating cash flow without reporting debt - but designed and implemented the financial structures to help Enron achieve its objective. Moreover, they accepted and followed Enron's desire to keep the nature of these transactions confidential.

By design and intent, the prepays as structured by Enron and the financial institutions made it impossible for investors, analysts and other financial institutions to uncover the true level of Enron's indebtedness.

Despite its desire to keep the information confidential, Enron dealt with so many financial institutions that word of its "prepay" structures began to circulate. Chase developed a "pitch book" to sell other companies on Enron-style prepays. The presentation describes the transactions as "Balance sheet 'friendly'." It also sets out in general terms Chase's use of its special purpose entity, Mahonia, in structuring the trades and clearly explains that the trades are orchestrated to work together. This explanation of the deliberate packaging of the trades flatly contradicts claims that the trades are independent and unrelated. Chase apparently entered into Enron-style prepays with seven companies apart from Enron.

Citigroup also developed a presentation to sell companies on Enron-style prepays, promoting, in particular, the Yosemite structure it had developed to raise the money for the prepays from third party investors without explicitly informing them of the transactions. The presentation boasts that the structure "[e]xpands capability to raise non-debt financing and ... improve cash flows from operations" and "[e]liminates the need for Capital Market disclosure, keeping structure mechanics private." Citigroup shopped this Enron-style prepay to 14 companies, successfully selling it to at least three.

Enron is not the only company obtaining loans disguised as commodity trades, and recording cash flows from operations instead of from financing. Major financial institutions are knowingly assisting and even promoting such transactions, which would not be possible without their willingness to provide the funds, the paperwork, and a sham offshore trading partner.

Thank you. Mr. Brown and I would be happy to answer any questions.

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APPENDICES A, C, D & E

(Appendix B to be released July 23, 2002)

TO

STAFF STATEMENT

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

HEARING ON

THE ROLE OF THE FINANCIAL INSTITUTIONS IN ENRON'S COLLAPSE

JULY 23, 2002

APPENDIX A

ACCOUNTING TREATMENT OF PREPAYS; EFFECT OF ENRON'S FINANCIAL STATEMENT

I. Prepays -- A General Description

A prepay, in its most simple form, is paying in advance for a service or product to be delivered at a later date. Companies use prepays to receive money up-front for services to be rendered in the future. Enron used a complex form of prepays as a source of financing that, in the end, misled investors as to the financial health of the company.

To understand Enron's use of prepays, it is important to have knowledge of basic accounting and financial reporting. Publicly traded companies such as Enron are required to file audited financial reports with the Securities Exchange Commission ("SEC") on an annual basis. These filings consist of three key financial statements, which combined with the accompanying disclosures, should provide a realistic view of a company's financial health. They are the income statement, the balance sheet, and the cash flow statement.

The **income statement**, or statement of earnings, provides details on a company's profitability. It includes both the company's revenues and the costs incurred to generate those revenues. Other costs, such as interest and taxes are also included, arriving at a company's net income number. This net income number, divided by the number of a company's shares outstanding, represents the critical earnings-per-share or "EPS" number, used by equity analysts and investors to determine a company's share price.

The **balance sheet** serves as a snapshot of a company's financial condition at a point in time. Among the critical information it conveys is detail on the amount of debt (money owed by the company) and equity that comprise the company's total value. Companies with high levels of debt relative to their equity are generally considered risky companies. They typically are charged higher rates of interest and are sometimes considered less attractive business partners than companies with lower debt levels. In the case of Enron, the company was under constant pressure to lower the amount of debt on its balance sheet.

The **cash flow statement** represents a company's sources and uses of cash over the quarter or fiscal year. Sources and uses of cash are divided among 1) operating activities; 2) financing activities; and 3) investing activities. These three sections are critical to understanding how a company finances its operations and, in particular, if a company's operations are sufficient to cover its costs and plans for investment. If a company is not able to meet its cash needs through operating activities, it will probably need to borrow money.[1] Cash from borrowing will appear on a

[1] A company may choose to issue additional equity to meet its cash needs. This has the effect of increasing the company's equity but will also dilute the earnings of the company's current shareholders.

company's cash flow statement as cash flow from financing activities and will also be reflected in higher debt levels on a company's balance sheet.

Companies registered with the Securities and Exchange Commission are required to file their financial statements in conformance with Generally Accepted Accounting Principles ("GAAP"). GAAP provides the conceptual framework for financial reporting. The primary purpose of financial reporting is to provide financial statement users, such as investors and creditors, with relevant and reliable financial information on which to base decisions. GAAP is also intended to enhance the consistency, comparability, and transparency of financial statements. Financial statements prepared under GAAP should, when taken as a whole, present fairly the financial condition, results of operations and cash flows of the company.

In the United States, the SEC has responsibility for the establishment of GAAP. The SEC administers GAAP through Regulation S-X, Financial Reporting Releases and Staff Accounting Bulletins. However, the SEC has looked primarily to the private sector standard setter, the Financial Accounting Standards Board ("FASB") to provide authoritative guidance for GAAP through its Statements and Interpretations, Technical Bulletins and Implementation Guides, as well as through consensus published by its Emerging Issues Task Force. The accounting industry, represented by the American Institute of Certified Public Accountants ("AICPA") contributes to GAAP by issuing Accounting Research Bulletins, Statements of Position, Audit and Accounting Guides, ACSEC Practice Bulletins and Accounting Interpretations.

II. Motivation behind Enron's Prepay Transactions

Enron had two major reasons to reduce its balance sheet debt and increase cash flow from operations: 1) to improve Enron's credit rating and 2) to support and even boost Enron's share price.

Improve Enron's Credit Rating

Until the recent wave of accounting scandals, cash flow was seen as the most reliable measure of a company's operating performance, because it was believed that the cash flow from operations number could not be manipulated as easily as earnings and was the best representation of the company's ability to meet its obligations. As a result, financial analysts placed heavy emphasis on cash flow numbers in determining a company's credit rating. These ratings, in turn, determined a company's cost of borrowing, attractiveness as a trading partner, and ultimately had an impact on its share price.

Enron, therefore, placed a heavy emphasis on generating operating cash flow, and business units at Enron were given cash flow targets by Enron management that they were expected to meet. In order to generate cash flow, Enron had the following options:

a) It could sell its hard assets, such as power plants and pipelines.
b) It could sell the value (and risks) of specific trades in its trading book to someone else and collect cash proceeds from the sale. (Early in its corporate history, Enron actually did sell off a number of its trades in order to generate cash flow.)

c) It could go to a bank and borrow money, using the trades and their promise of delivering cash a few years down the road as collateral.

Enron used all three options, but it is Enron's use of the third option that is the subject of my testimony today. When using the third option, if Enron borrowed money against the value of its trades, it would have to record the amount borrowed as debt on its balance sheet and proceeds from the loan as cash flow from financing. Already under pressure from rating agencies to reduce its debt load, Enron was unwilling or unable to do this and instead turned to an unusual and complex alternative (some would say an accounting gimmick) -- highly structured prepays that Enron used to report loans in a way that hid its borrowing while painting a more favorable picture of Enron's financial condition. It booked the advance of cash as a trading activity rather than as a loan and proceeds from the loan as cash from operations rather than cash from financing. In this way, Enron raised funds of $8 billion or more beginning in 1995[2] and buried the loans as trading liabilities. The result was that Enron secured the operating cash flow that analysts needed to see in order to view Enron favorably and avoided the appearance of additional debt that analysts would have viewed as troubling.

Several internal Enron documents confirm Enron's view of this use of prepays. An internal memorandum dated August 1997 defines the purpose of prepay transactions as "provid(ing) cash flow to Enron Corp in order to meet its cash flow objectives. They are not intended to be income generating transactions."[3] A later Enron presentation anticipated the need for prepay financings to generate $1 billion in "FFO" (funds flow from operations) annually.[4] A document obtained from an employee in the Enron Accounting Department describes the prepays as "off balance sheet financing (i.e., generate cash without increasing debt load)."[5]

In 2000, Enron initiated $1.935 billion[6] or more in prepay transactions, the proceeds of which were included in Enron's financial statements as "Cash Flows from Operating Activities." In addition, the Subcommittee staff estimates that Enron had $4 billion of outstanding prepay debt on its balance sheet as of December 31, 2000.[7] As the following chart demonstrates, if Enron's 2000 year-end financial statements were adjusted to reflect $4 billion in outstanding prepay transactions

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[2]Enron presentation to the Finance Committee of the Enron Board, August 2001. "ASF - Detail on Prepays." Bates EC 000058019.

[3]Enron Interoffice Memorandum, "Subject: Prepaid Hydrocarbon Companies," August 22, 1997. Bates EC 001537017.

[4] Enron Yosemite presentation. Bates ECa 000196339-51.

[5] Bates EC 001594743.

[6] Subcommittee staff estimate based on the following prepay transactions: Chase X (9) / Mahonia - $650 million - June 2000; Chase XI (10) / Mahonia - $330 million - December 2000; Citibank / Delta / Yosemite II - $305 million - February 2000; Citibank / Delta / Yosemite III (CLN I) - $500 million - August 2000; Credit Suisse First Boston, Morgan Stanley - $150 million - December 2000.

[7] 2001 Enron Board presentation. Bates RCO 21428.

as debt and deducted the $1.527 billion[8] from "Funds Flow from Operations,"[9] Enron's credit profile would have changed dramatically.

	2000 Reported Financials	Adjustment[10]	2000 Adjusted Financials
Total Debt	$10.2 billion	$4.0 billion	$14.2 billion
Total Equity[11]	$14.8 billion		$14.8 billion
Total Capital	$25.0 billion		$29.0 billion
Debt / Equity	**69.2%**		**96.2%**
Debt / Total Capital	**40.9%**		**49.0%**
Funds Flow from Operations[12]	$3.2 billion	$1.5 billion	$1.7 billion
Interest and Other[13]	$1.1 billion	$200 million	$1.3 billion
Funds Flow Interest Coverage[14]	**4.07**		**2.37**

These adjustments have a significant impact on Enron's credit ratios. Enron's reported "Funds Flow Interest Coverage" (footnote 14) of 4.07 was typical of a company with an A-/A3 rating, which is a rating that is assigned to a very stable and financially healthy company. The adjusted number of 2.37 is in line with a company with a BBB-/Baa3 rating, a decline of three rating "notches," reflecting a considerably considerably weaker credit. Likewise, the revised Debt as a

[8] Subcommittee staff estimate of Fiscal Year 2000 prepay proceeds of $1.935 billion less $408 million in prepay amortizations, leaving net prepay proceeds of $1.527 billion. Bates EC000058019.

[9] Enron's calculation of "Funds Flow from Operations" is equal to "Cash Flow from Operations" adjusted for Merchant Activities, Equity Earnings, Equity Partnership Distributions and Other. Bates EC 000469193.

[10] Adjustment to "Funds Flow from Operations" deducts the value of Year Fiscal 2000 prepay transactions net of prepay amortizations. Bates EC 000058019. Adjustments to "Interest and Other" reflect a 5% rate of interest on $4.0 billion in prepay debt.

[11] Total Equity is equal to Shareholders' Equity, Company-Obligated Preferred Securities of Subsidiaries and Minority Interests, consistent with Enron's presentation of Total Capital in company presentations to rating agencies. Bates EC 000469368.

[12] Subcommittee staff estimate based on March 2001 Enron Global Markets presentation citing "Actual Funds Flow Interest Coverage" of 4.07. Calculation assumes interest expense of $838 million, dividends on preferred shares of $77 million and rent expense of $143 million as reported in Enron 2000 10-K, yielding "Funds Flow from Operations" of $3.248 billion. Bates EC 000007671.

[13] Interest and Other includes dividends on preferred shares and rent expense.

[14] "Funds Flow Interest Coverage" is calculated as "Funds Flow from Operations" + interest incurred + dividends on preferred shares + rent expense, divided by interest incurred + dividends on preferred shares + rent expense. The Subcommittee staff has included dividends on preferred shares based on the appearance of their inclusion in previous years' calculations.

Percentage of Total Capital figure of 49.0% is approximately three rating notches below Enron's reported figure of 40.9%.[15]

These declines in financial ratios are significant, because the lower financial ratios would have affected Enron's credit rating, and a lower credit rating would have had serious consequences for Enron's operations:

- Below BBB-/Baa3, Enron would no longer be considered an "investment grade" company. As a result, certain investors' internal investment requirements would have prohibited them from buying the company's bonds, thereby shrinking the pool of money that Enron could tap for its growing cash needs. More importantly, Enron would have been shut out of the commercial paper market which accounted for a significant portion of Enron's borrowing.

- At a lower credit rating, Enron would have been considered a less attractive trading partner. This means that Enron would have lost trading business, the largest source of income to the company. Parties still willing to trade with Enron probably would have reduced the trades they would have been willing to enter into with Enron and/or require Enron to post additional collateral.[16]

- Even more threatening, if Enron had fallen below investment grade (to "junk" status), a number of its trading partners would have had the contractual right to close out existing trades and demand payment from Enron, further straining Enron's cash position.

- A fall below investment grade also would have had a significant impact on Enron's financing. As a higher credit risk, Enron's cost of borrowing would have increased considerably, increasing its interest expense and lowering earnings.

- Equally as significant is the fact that Enron sponsored a number of off-balance sheet vehicles that were supported with Enron credit. Once Enron fell below investment grade, debt holders in these vehicles could demand repayment and Enron would have to make sure they received it. This would have represented a huge liquidity crisis to Enron, and in fact, that liquidity crisis eventually occurred.[17]

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[15]Average Funds Flow Interest Coverage and Debt / Total Capital per rating category based on March 2001 Enron Global Markets presentation. Bates EC2 000007671.

[16]From Enron's Form 10-Q filing, September 30, 2001: "Maintaining an investment grade credit rating is a critical element in maintaining liquidity for Enron's wholesale business which, together with the natural gas pipeline operations and the retail business, comprise Enron's core business . . . A downgrade to below investment grade could lead to a substantial increase in the level of cash required for collateral and margin deposits with Enron's wholesale trading partners . . . The recent deterioration in Enron's credit rating and decline in its stock price has caused a negative impact on Enron's projected 2001 fourth quarter profitability. This is primarily the result of a reduced level of transaction activity by Enron's trading counter-parties, particularly for longer-term transactions."

[17]From Enron's Form 10-Q filing, September 30, 2001: "Enron has various financial arrangements which require Enron to maintain specified credit ratings. The November 12, 2001 downgrade in Enron's senior unsecured debt rating to BBB- by Standard & Poor's has caused a ratings event related to a $690 million note payable that, absent Enron

Enron was acutely aware of the importance of its credit rating and reported on "progress" with the credit rating agencies at internal meetings and to the Board of Directors. It was also aware that the financial ratios just discussed determined the company's ratings. Enron's decisions on when to engage in a prepay and the size of the prepay were driven by its need to meet certain ratio targets. Consequently, funds from prepay transactions would appear on Enron's cash flow statement just days before the end of a quarter, just in time to be factored into Enron's financial statements and pump-up key ratios.

Support Enron's Share Price

In addition to a credit ratings impact, Enron's use of prepay transactions and the accounting treatment of these transactions had a profound impact on Enron's valuation, which in turn drove Enron's stock price. Dozens of equity analysts followed Enron and relied on the company's audited financial statements, as well as guidance from Enron management, to set a future target for the company's share price. The manipulation of prepay transactions had a direct impact on the value equity analysts assigned to Enron shares in two ways.

Understating Debt: A company's "enterprise value" is a measure of what the market believes a company's ongoing operations are worth. A text book definition calculates enterprise value as:

Market equity (representing shareholders' ownership in the company)
\+ Preferred stock (representing preferred shareholders' ownership in the company)
\+ Net debt (representing lenders' "investment" in the company)
= Enterprise value[18]

This definition assumes the market has knowledge of a company's indebtedness and preferred equity obligations, and takes that information into account when determining the "fair" value of a company's shares, which equate to its market equity. If, however, a company has hidden a portion of its debt either off-balance sheet or in other liabilities such as trading liabilities, or if analysts and investors fail to adjust their estimation of the company's value to reflect this higher indebtedness, the company's market equity value will be overstated.

The following graph illustrates this point. Enron had a market-determined enterprise value of $23.4 billion as of October 2001.[19] Enron's equity value can be determined by subtracting net debt and preferred securities from the enterprise value. Dividing that equity value by the number of

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posting collateral, will become a demand obligations on November 27, 2001. . . In the event Enron were to lose its investment grade credit rating and Enron's stock price was below a specified price, a note trigger event would occur. This could require Enron to repay, refinance or cash collateralize additional facilities totaling $3.9 billion, which primarily consist of $2.4 billion of debt in Osprey Trust and $915 million of debt in Marlin Water Trust."

[18]Enterprise value or "Market Value of Invested Capital ("MVIC"). Pratt, Shannon. The Market Approach to Valuation of Businesses. John Wiley, publisher, 2001.

[19]Enterprise value equals market equity value of $10.4 billion plus balance sheet debt, net of cash, of $12.0 billion plus preferred securities of $1.1 billion. Market equity value is based on Enron's share price of $14 as of October 2001 multiplied by 744 million shares outstanding.

Enron shares outstanding yields the market price per share. If investors learn that instead of $12 billion in net debt on its balance sheet, Enron has close to $17 billion in debt, they will likely react by selling Enron shares until the price falls to a level consistent with that level of indebtedness.[20]

	Balance Sheet Debt	Adjustment	Balance Sheet Debt + Prepays
Enterprise Value	$23.4 billion		$23.4 billion
Subtract Debt and Pref. Obligations	$13.1 billion	$4.8 billion	$17.9 billion
= Equity Value	$10.3 billion		$5.5 billion
Divide by Shares Outstanding	744 million		744 million
= Actual / Implied Market Price per Share	**$14**		**$7**
Decline in Share Price			- 46%

Earnings Impact: Enron's practice of using prepay transactions to understate debt and overstate cash flows from operations had an additional share price impact. As previously discussed, Enron needed prepay transactions to generate cash flow and support its credit rating. By supporting its "investment grade" credit rating, Enron was able to expand its trading business as well as borrow money at a relatively low interest rate.

The result of robust trading activities (accented by mark to market accounting) and relatively lower interest expense was a boost to Enron's net income, which in turn is the key driver of a company's share price.[21] As long as Enron could continue to show positive earnings growth, it could expect to see appreciation in its stock price. By using prepay transactions to generate cash flow from operations, Enron was able to maintain its investment grade ratings, which allowed Enron to build a trading business that was the engine behind Enron's income growth. As earnings grew, so did Enron's share price. In addition, to the extent equity analysts viewed growth in Enron's operating cash flow, fueled by net prepay transactions of over $1.5 billion in 2000 alone, as

[20]This Subcommittee staff analysis is for demonstrative purposes only and does not take into consideration a number of other complicating factors, including the billions of dollars in off-balance sheet debt that, once known to the market, resulted in the collapse of Enron's share price. The fact that Enron shares ultimately traded at pennies per share suggests that investors thought the company had exceeded its limit in loans and other financing structures.

[21]Shares of companies in the energy sector typically trade in the market at a share price based on their Price/Earnings ratio. "Price" refers to the current market price for one share of the company; "Earnings" refers to net income or earnings per share, also known as "EPS". For example, a company whose shares trade at $20 per share and has earnings per share of $2.00 is said to trade at a P/E ratio of 10 times earnings ($20 / $2.00 = 10). If 10 times earnings is the industry standard multiple for energy companies, an increase in earnings per share to $3.00 per share should result in an increase in share price to $30 per share, thereby maintaining the P/E ratio at 10 times ($30 / $3.00 = 10).

indicative of Enron's future growth, the cash flow impact of prepay transactions can also be viewed as a key driver of Enron's share price.[22]

III. Accounting and Structuring for Prepays as Cash from Operations

In order to treat the prepay transactions as trading activities instead of loans, Enron referenced accounting guidelines[23] for treating contracts as derivatives.[24] SFAS 133, which was issued by FASB in 1998 and became effective in June 2000, establishes the rules for both defining and accounting for derivatives contracts. Derivatives contracts are considered part of a trading company's operations. To meet these guidelines, Enron had to structure the prepays using three separate parties: Enron, the bank providing the money, and an independent third party. Without an independent third party, the prepay would be viewed as a loan.

An Andersen presentation obtained by the Subcommittee from Enron summarizes the key criteria needed to meet classification of a prepay as a trade rather than a loan.[25]

> "**For prepays to be treated as trading contracts, the following attributes must exist**:
>
> **None of the individual agreements . . . are linked commercially** or make references to any of the other documents; in effect, **each is a stand-alone**, normally occurring derivative instrument which continue to be in effect even if other pieces of the transaction are terminated for any reason. . . .
>
> **Price risk** related to the PGA[26] **is transferred from the gas supplier to the purchaser**, without the gas supplier further affecting the purchaser's management of this risk or the purchaser's other PGA-related economics. **This includes any future actual or contingent swaps that may be contemplated.**
>
> **The purchaser of the gas must have an ordinary business reason for purchasing the gas, not in-substance be a special purpose entity (SPE) established just to effect a secured investment in a debt instrument from a gas supplier.** The SPE issue could arise

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[22] A higher debt level has the potential impact of reducing a company's cost of capital, which in a discounted cash flow analysis would result in a higher present value of the company's future cash flows. However, the increased debt level also increases the risk profile of the company, which would increase the cost of capital, thereby reducing the present value of future cash flows.

[23] Accounting literature referenced as per Arthur Andersen memorandum on Prepay Transactions, Bates ECp000094306: EITF 96-21; EITF 90-15; Topic D-14; December 1997 SEC Speech - Armando Pimentel; EITF 88-18. Also, FASB Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities."

[24] A derivative is a financial instrument whose value is based on another instrument, such as a stock or an index, or in the case of Enron's prepays, the price of commodities including gas and crude oil.

[25] Arthur Andersen presentation to Enron Corp. "Prepaid Transactions Discussion." Bates EC 000013365 - 69.

[26] Term undefined. It may mean "Prepaid Gas Agreement."

by virtue of the purchaser's very nature and the substance (or lack thereof) of its other business operations. It could also arise based on the types of the contractual limits included in the series of structured transactions (e.g., the debt of the purchaser is recourse to the gas supplier or not recourse to any of the purchaser's other assets)."

An Arthur Andersen memorandum to the Audit Files from June 1999[27] provides a more detailed description of the criteria, summarized in the presentation, that Andersen considered important for determining the appropriate accounting treatment for Enron's prepay transactions.

The purpose of the Andersen criteria for prepays was to distinguish true trading activity from loans. The criteria warn against such indicia of phony trading activity as linked trades, prepay transactions where no party is at risk of monetary loss, and trades involving shell corporations with no ordinary business reason to buy or sell energy commodities. These criteria show that the accounting community was well aware that prepays could be manipulated to function as disguised loans and had devised criteria to disallow accounting as operational business activity those prepays which were, in reality, devices to obtain financing.

The 1999 Andersen memorandum states explicitly that the transactions between the three parties that comprise the prepay transaction must be de-linked in every way from the original transactions. The most obvious form of linkage would be any cross-default provisions in the contracts. Cross-default provisions would allow, for example, Enron to seek payment from the bank if the third party defaults on its obligation to Enron. Furthermore, these transactions should stand alone, without reference to each other. This would preclude, for example, an assignment of rights and obligations of the third party to the bank. Finally, any elements that would indicate that the third party and the bank are related might constitute linkage. If the bank were covering all of the third party's costs, or if the third party played no role in negotiating its contract with Enron and deferred all decision-making to the bank, it might raise serious questions as to the independence of the third party from the bank.[28]

The Andersen memorandum also stipulates that the fixed payments made by the parties to the prepay transaction must be based on fixed volumes of the commodity so as to isolate the price of the commodity as the only variable.[29] Andersen also concluded that the trades should be settled periodically. Periodic settlement is more indicative of normal trading activity because it subjects the parties to the price fluctuation of the market (as opposed to basing settlement solely on the price of the commodity at a fixed point in time). Andersen also concluded that the existence of a second "triangle" that mirrored the original prepay transaction (with the direction of the fixed and floating legs reversed) would preclude treatment of any of the transactions as valid trades because the mirroring eliminated price risk entirely.[30] Finally, if, for example, either the bank or the third party

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[27] Bates ECp 000094306.

[28] Arthur Andersen, Staff Interview, July 13-14, 2002.

[29] Ibid. Arthur Andersen also required that pricing of the contracts reference the market price of the commodity in question.

[30] Arthur Andersen Staff Interview, July 14, 2002.

were so perfectly hedged that neither made any profit on the trade itself, it might raise questions as to why they entered into the transaction and to whether the parties were related.[31] Elimination of price risk, therefore, could lead to a determination that the contracts were linked and should therefore be collapsed as described above. Emphasis is placed on confirming price risk in each leg of the transaction because price risk is what distinguishes a trade from a loan.

The criteria are designed to: 1) avoid linkage between the contracts and/or the parties to the contracts; and 2) eliminate the price risk between the parties to the transaction, either of which event could result in classifying a prepay transaction as debt rather than as a trade and classifying cash generated in prepay transactions as cash flow from financing activities rather than cash flow from operating activities.

The Enron prepays blatantly contradict the Andersen prepay criteria. They involve linked trades, an elimination of price risk, and shell off-shore corporations that were controlled by banks and that functioned as sham trading parties. Each prepay was orchestrated as a three-part round-robin trade whose true function was not to buy or sell an energy commodity, but to provide Enron with financing that Enron would repay with interest. The parties involved in the Enron prepays were aware of the entire structure and its accounting purpose.

Under the Enron prepay structure, a participating bank would send cash (the money destined for Enron) to the third party, in exchange for the future delivery of a fixed amount of a commodity. The third party, in turn, would enter into an identical arrangement with Enron, and effectively serve as a pass through for the bank funding to get to Enron. Enron would repay the funding in a fixed amount of commodities, which would pass through the third party en route to the bank. Up to this point, this appears to be a "real" trade because all three parties bear the risk that the price of the underlying commodity will change. This is called price risk and it is an essential element in a true trading transaction.

But, Enron's prepays also entailed a transaction known as a "swap" in order to mitigate price risk. Under a swap agreement, Enron exchanged (with the bank) the floating price of the commodity for the fixed price of the commodity. The net effect is to cancel out any price risk to all parties in the trade. The fact that were the third party was not independent and the terms of the prepay were predetermined based on Enron's decision as to how much operating cash flow it needed to report presented other problems with Enron's prepay structure.

Enron engaged in these prepays, which often involved natural gas or crude oil, at a pace of one or two per year from 1992 to September 2001 when the last prepay transaction was implemented.[32] Most of those transactions (both in number and in dollar value) were with JPMorgan

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[31]Arthur Andersen Staff Interview, July 13, 2002. This would be especially relevant if the trades were entered into simultaneously.

[32]The September 2001 prepay closed on September 28, 2001, but remained outstanding along with seven other Chase prepays when Enron filed for bankruptcy on December 2, 2001.

Chase and Citigroup. Chase and Enron engaged in at least 12 transactions with a value of $3.7 billion. Citigroup and Enron engaged in at least 14 transactions with a value of $4.8 billion.[33]

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[33]The specific details of each transaction varied slightly - some included additional financial institutions as counterparties; some used different commodities; and some involved the actual physical exchange of the commodity while others were merely paper transactions. All but one of the Chase transactions were physically settled; conversely all but one of the Citigroup transactions were paper transactions.

APPENDIX B

KNOWLEDGE AND PARTICIPATION OF FINANCIAL INSTITUTIONS IN ENRON PREPAYS

The evidence reviewed by the Subcommittee staff indicates that the financial institutions that participated in Enron "prepays" understood that Enron was seeking to obtain financing from them, but wanted to obtain the financing through orchestrated, multi-party commodity (largely energy) trades rather than straight-out loans, so that the company could characterize the funds as cash flow from operations rather than cash flow from financing. Internal communications show that the financial institutions not only understood that Enron intended to engage in this deceptive accounting, they actively aided Enron in return for fees and favorable consideration in other business dealings. The evidence also indicates that these financial institutions complied with Enron's desire not to disclose its transactions to outside parties, and knowingly allowed investors, financial analysts and others to rely on Enron financial statements that the financial institutions knew or should have known were misleading.

The evidence indicates that Enron would not have been able to engage in the extent of the prepay accounting deceptions it did, involving more than $8 billion, were it not for the active participation of major financial institutions willing to go along with and even expand upon Enron's activities.

Financial Institutions Involved in Enron Prepays

Enron used "prepay" transactions to obtain more than $8 billion in financing over approximately 6 years.[1] This $8 billion figure is a conservative estimate based upon the evidence gathered by the Subcommittee to date; it is possible that the total dollar amount involved in this financing, since Enron began using it in 1992, is much larger.

Most of Enron's "prepays," both in number and dollar value, involved either JPMorgan Chase Bank ("Chase") or Citigroup.[2] Altogether, Chase and Enron engaged in at least 12 transactions from 1992 until 2001, with a combined value of more than $3.7 billion. Citigroup and Enron engaged in at least 14 transactions from 1993 until 2001, with a combined value of more than $4.8 billion. Enron also completed "prepays" with a number of other financial institutions over the last ten years including Barclays, Credit Suisse First Boston, FleetBoston, Royal Bank of Canada, Royal Bank of Scotland, and Toronto Dominion. Although the investigation was unable to determine the total value of these transactions, the evidence indicates they had a combined value in excess of $1 billion.

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[1] "ASF – Detail on Prepays," Enron presentation, August 2001. Bates EC 000058019.

[2] "Summary of Enron Prepays with JPMorgan Chase and Citigroup," Appendix E.

Financial Institution Knowledge of Accounting Deception

Internal communications and documentation at the financial institutions, Enron and Enron's accounting firm, Arthur Andersen, indicate that it was common knowledge that Enron's "prepays" were designed to manipulate Enron's financial statement by overstating cash flow from operations and understating debt.

Among the internal communications documenting the knowledge of the financial institutions are the following.

- A Chase banker wrote in a 1998 email: "Enron loves these deals as they are able to hide funded debt from their equity analysts because they (at the very least) book it as deferred rev[enue] or (better yet) bury it in their trading liabilities."[3]

- In a telephone conversation on September 20, 2001, taped in the normal course of business, three Chase employees discussed one of the Enron prepays in the following terms:

  - " . . . [W]hy do they want to hedge with gas where it is now?"
  - "They're not hedging, they're just, they're just, they do the back-to-back swap."
  - "This is a circular deal that goes right back to them."
  - "It's basically a structured finance-"
  - "It's a financing?"
  - "Yeah, its totally a financing, which has piece of it, they're always had on as a piece of their capital structure, so-"
  - "So its amortizing. Yeah, it's amortizing debt. I get it."
  - "That's exactly what it is."[4]

- A September 2000 internal email from a Citigroup employee to colleagues made these suggestions on how to explain the Yosemite prepay to potential investors: "Get into why co[mpany] does it (gets cash flow, shows up as other liab[ilities] not debt . . .) . . . i.e., [g]ives some oomph to revenues . . . . [Enron] gets money that gives them c[ash]flow but does not show up on books as big D Debt."[5]

- A 1997 Chase summary of a proposed $250 million Enron prepay, written to gain credit approval for this transaction, included the following statement: "In the past three years, Enron has utilized the prepaid sale as a mechanism to address a number of needs,

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[3]Chase email, November 11, 1998. Bates SENATE MAH-02129.

[4]Chase audio tape, September 20, 2001.

[5]Citigroup email, "My take on how to explain ECLN," September 28, 2000. Bates CITI-SPSI 0084924.

including . . . sourcing funds (classified as 'Liabilities from Price Risk Management' as opposed to long term debt)."[6]

- A 1998 Citigroup loan approval memorandum in support of a prepay known as Roosevelt states: "The prepaid forward structure will allow Enron to raise funds without classifying the proceeds from this transaction as debt (it is accounted for as 'deferred revenue'). This is a common method of raising non-debt financing among energy companies."[7]

- A June 2001 Citigroup document summarizing the accounting and tax treatment for Enron prepays states: "As we understand the accounting, the Pre-Paid creates price risk management liability, thereby receiving non-'D' debt treatment. Operating cash flow increases . . . . From a tax perspective, the Pre-Paid can be treated much like a traditional loan[.] Swap payments are deductible on the tax books, similar to loan payments."[8] A January 2000 memorandum from Enron's tax planning department makes it clear that the prepay structures are not driven by tax requirements, but by accounting considerations: "The use of a prepaid swap was not motivated by tax considerations but instead was necessary in order to report the transaction as part of [Enron's] price risk management activities rather than debt for financial accounting purposes."[9]

- In a June 2002 court filing to require certain surety bond providers to make payment on bonds related to certain Enron prepays, Chase asserts that the sureties "knew that the deals [the prepays] were part of a structured financing transaction for Enron's general corporate benefit" and that "the surety bonds were part of financing transactions in which the funds advanced by JPMorgan Chase to Mahonia were ultimately used by Enron for general corporate purposes, not to secure future sources of the oil and gas to be delivered."[10]

- Credit Suisse First Boston ("CSFB"), which participated in two Enron prepays also understood the accounting-driven nature of the transactions. Emails exchanged among CSFB employees describe a prepay transaction as an "oil-linked loan,"[11] and state that "the net effect for [Enron] is raising $150M at L[IBOR] + 75bps [basis points] for 9

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[6]"Structuring Summary," prepared by Chase, 11/14/97. Bates JPM-1-00061.

[7]"Global Loans Approval Memorandum" for Roosevelt prepay, prepared by Citigroup, December 21, 1998.

[8]"Summary of Pre-Paid Accounting and Tax," prepared by Citigroup and attached to internal email from Citigroup employee Timothy Swanson (6/25/01). Bates CITI-SPSI 0050680.

[9]Enron Interoffice Memorandum from Tax Planning Department, January 10, 2000. Bates EC 000037274.

[10]Amended complaint, JPMorgan Chase Bank v. Liberty Mutual Insurance Co. (USDC SDNY) Case Number 01-Civ. 11523 (JSR), paragraphs 18-19.

[11]Credit Suisse First Boston email, December 18, 2000. Bates SR 00037828.

months off-balance sheet. As the swap is booked in their oil swap book and not treated as debt."[12]

- One CSFB lawyer raised concerns that the Enron "prepay" was "an accounting driven transaction,"[13] and recommended vetting it through the firm's "Reputational Risk Review" process. This review raised sufficient concerns to request Enron to make six representations about the transaction, including attesting to the fact that Enron senior management was aware of the transaction and that Enron was responsible for determining its accounting treatment.[14] Enron reportedly provided verbal assurance on these matters, but declined to provide anything in writing. CSFB approved the transaction and funded the prepay.

- In 1998, Chase developed a "pitch book" to sell other companies on Enron-style prepays. The presentation describes the transactions as an "[a]lternative source of finance" and "[b]alance sheet 'friendly' " and explains that they have an "[a]ttractive accounting impact by converting funded debt to 'deferred revenue' or long-term trade payable."[15] A similar Citigroup presentation, promoting Yosemite-style prepays, boasts that the structure "[e]xpands capability to raise non-debt financing and ... improves cash flows from operations."[16]

- Enron itself was clear about the purpose of its "prepays." A presentation prepared by Enron's accounting department for an internal educational seminar states: "Why does Enron enter into Prepays? Off balance sheet financing (i.e. generate cash without increasing debt load)."[17]

- Andersen was equally clear. "Enron is continuing to pursue various structures to get cash in the door without accounting for it as debt."[18]

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[12]Credit Suisse First Boston email, December 8, 2000. Bates SR 00038448.

[13]Credit Suisse First Boston email, "RE: URGENT / decision required - status on Eneron (sic) oil linked loan," December 14, 2000. Bates SR 00041087.

[14]Credit Suisse First Boston, Staff Interview, July 12, 2002.

[15]Chase presentation, July 16, 1998. Bates SENATE MAH - 02604.

[16]"Credit-Linked Notes," presentation by Citibank/Salomon Smith Barney (May 2001), at 37. Bates CITI-SPSI 0041206.

[17]"What are Prepays?", presentation prepared by Enron accounting department for internal educational seminar, undated. Bates EC 001594740.

[18]Internal Andersen email, December 16, 1998. Bates AASCGA 1132-1.

Financial Institution Actions to Assist Enron's Accounting Deception

The participants in Enron's "prepays" were not only aware that the transactions were driven by Enron's desire to manipulate its financial statements, the financial institutions actively aided Enron in designing and implementing financial structures that created and maintained the fiction that the transactions were trades rather than loans.

- To help Enron create an appearance of independent trades in each "prepay," both Chase and Citigroup included as one of the participants an offshore shell corporation that appeared to be an independent entity but, in reality, was established and controlled by the respective bank. The two offshore entities are Mahonia Ltd.[19] and Delta Energy Corp., which were created and controlled by Chase and Citigroup, respectively. Since these entities apparently had no employees, no office, and no independent business operations, each bank provided the legal advice, paperwork, and financial support necessary for its affiliated offshore shell to participate in the trades. Without an independent third party, the trades that canceled each other out and allowed the prepay to function as a loan would not have been possible.

- When Andersen raised questions about the independence of Mahonia and Delta and requested a letter from each representing that it was an independent operational business apart from the bank and Enron, personnel at the associated banks complied. A taped telephone conversation on September 13, 2001, among Chase and Enron employees discussing the Andersen request shows that they were well aware that they were contributing to a fiction that Mahonia was independent from Chase:

  -"You're talking about the rep letter from Mahonia . . . saying, you know, it has the right to do transactions like this. . . .Before what we've done is just really looked at the actual charter, and you've got the information, but now Andersen is pushing back and saying, hey, we need to have a specific rep letter that a representative of Mahonia signed that reps a certain point."
  -"Which is, yeah, separate from Chase. It doesn't have Chase showing up anywhere on the fax letterhead or anything along those lines, a separate fax number, et cetera. . . ."
  -"That goes to the same point you were raising earlier, Jeff, that from your side, you also want to make sure that Mahonia seems independent."[20]

- In one recent Enron prepay, a May 2001 internal Citibank memorandum suggested adding a minimal charge of one penny to the price spread to make it seem "a little more like a true trade." The memorandum states: "[The spread offers a more real transaction,

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[19] Other Chase-controlled entities such as Mahonia Natural Gas Limited and Stoneville Aegean were sometimes used in place of or in addition to Mahonia, Ltd.

[20] Chase audio tape, September 13, 2001.

the penny is in fact diminutive and figures to be an incremental 1 [basis point] on the whole transaction . . . . I highlighted the 1 penny spread to Kelly after I sent an initial script . . . . I told her that the charge makes the prepaid structure a little more like a true trade, whereas a written floor and a purchased cap cannot be executed at the same level – good for both parties from an auditing/regulatory perspective."[21]

- To help Enron characterize prepay funds as coming from energy trades, several of the financial institutions were careful not to include requirements or descriptive language in the prepay documentation that would disclose the true nature of the transaction. For example, when drafting documents for its prepay with Enron, CSFB instructed its lawyers: "very important for them [Enron] is that the docs are as standard as possible and DO NOT include any representations on accounting driven transactions."[22]

- A 1999 Citigroup memo discussing Enron's repayment of a portion of a prepay states: "The paperwork cannot reflect their [Enron's] agreement to repay the $190 mm as it would unfavorably alter the accounting . . . ."[23] Citigroup memos reveal that Enron had agreed to repay the $190 million in two payments by dates certain, prior to the delivery dates for crude oil indicated in the energy trading documentation, but putting that agreement in writing would have caused the transaction to be classified as debt. As a result, Citibank accepted an unwritten "agreement" from Enron that it would repay the $190 million by the agreed date.[24] All of these actions made it easier for Enron to execute its "prepays" and claim they were the proceeds of energy trades rather than loans.

- When due to Enron's growing debt levels, Citigroup credit analysts became reluctant to extend Enron additional financing through new "prepays," Citigroup worked with Enron to design and establish the Yosemite structures which, instead of relying on bank financing, obtained funds under Rule 144(A) offerings from qualified investors. Citigroup underwrote four Yosemite offerings which produced sufficient funds for half a dozen Enron prepays worth a total of $2.4 billion. Citigroup even participated as an equity owner in the trusts that were a key element in these structures.

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[21]Citigroup email, May 9, 2001. Bates CITI-SPSI 0053452.

[22]Credit Suisse First Boston email, December 15, 2000. Bates SR 00037769.

[23]Citigroup email, "Enron/Roosevelt Update," April 22, 1999. Bates CITI-SPSI 0068751.

[24]Citigroup email, "Enron/Consent to Amendment to Roosevelt Transaction," April 27, 1999. Bates CITI-SPSI 0046833.

Financial Institution Actions to Keep Prepays Secret

In addition to helping Enron design and execute multiple "prepay" transactions, the financial institutions complied with Enron requests to restrict disclosure of the nature and extent of its prepay activities. By design and intent, the "prepays" structured by Enron and the financial institutions made it impossible for investors, analysts, and other financial institutions to uncover the true level of Enron's indebtedness.

> Enron hid from investors and financial analysts the extent and nature of its "prepay" activities. In its financial statements, Enron included the money it received from "prepay" transactions on its balance sheet in a line item known as "Price Risk Management," burying the proceeds within a much larger figure, about $20 billion in 2000, representing the company's overall trading liabilities. This $20 billion did not separately identify funds derived from "prepay" transactions; in fact, Enron's financial statements never explicitly addressed Enron's "prepay" activity at all, despite its growing role in the company's finances. At one point Arthur Andersen auditors recommended to Enron Chief Accounting Officer Rick Causey that Enron provide more complete disclosure on its prepay transactions, but Mr. Causey declined to do so.[25] The financial institutions that participated in Enron's "prepays" also kept quiet about what they knew. Most of Enron's "prepays" were transacted with Chase and Citigroup; neither disclosed information publicly about the extent of Enron's prepay activity, even in documentation associated with the Yosemite Rule 144(A) offerings. Financial analysts that closely followed Enron, including analysts with major credit rating agencies, told the Subcommittee staff that they had been completely unaware of Enron's prepay activities prior to its bankruptcy.
>
> Citigroup provided a major boost to Enron's prepay secrecy when it worked on the design of the Yosemite structures. These structures offered investments in Enron-related matters and did not reveal to investors the specific investments into which their funds were being placed. The trusts and the lack of information on specific investments functioned as a "black box," in the words of Enron, to prevent investors and others from knowing that the Yosemite proceeds were being used to fund Enron prepays. An Enron presentation touting the advantages of using the Yosemite proceeds for prepays states that the Yosemite structure "provides for a unique 'black box' feature which provides considerable flexibility" and that the "[b]lack box allows Enron the ability to provide a permanent take-out feature for highly structure[d] transactions in the capital markets while limiting disclosure of prepay to Citibank." The presentation warns: "[T]he use of prepays as a monetization tool is a sensitive topic for both the rating agencies and

[25] Arthur Andersen, Staff Interview, July 19, 2002.

banks/institutional investors. The ability to continue minimizing disclosure will likely be compromised if transactions continue to be syndicated."[26]

- On one occasion, when a Yosemite investor learned about Delta Energy Corporation and contacted Enron for additional information, Enron personnel reacted strongly to stop further disclosure. Enron immediately sent a series of emails to Citigroup which stated: "[A]pparently an investor spoke to someone at citi and received info on delta. This person . . . is now calling us asking about delta now. We need to shut this down."[27] "By the way – not blaming you guys just trying to figure out how to shut it down."[28] Citigroup declined to provide any additional information to the investor.

- Enron's prepay secrecy was so successful that, while each financial institution involved in an Enron prepay had inside knowledge of that particular transaction, it appears that no financial institution – even Chase or Citigroup – knew the total number and dollar value of all of the "prepays" engaged in by Enron. For example, an October 2001 exchange of emails at Chase had this to say after the bank learned, to its surprise, that Enron had $5 billion in prepays outstanding, an amount that was much greater than Chase had expected:

  -"$5B in prepays!!!!!!!!!"
  -"shutup and delete this email."[29]

- In September 1999, in response to internal concerns regarding the complexity, reliability and completeness of Enron's audited financial statements, a Salomon Smith Barney ("SSB") senior banker led a review of Enron's capitalization. The report[30] was presented to Citigroup's Investment Grade Debt Commitment Committee, which is charged with approving commitments of the bank's capital to investment grade debt financings. The report included information on Enron's capitalization taken from Enron's audited financial statements, analyses conducted by Moody's and an analysis based on SSB's knowledge of the company.

  The internal SSB analysis reported a level of indebtedness which included prepays and was higher than what was reported in Enron's financial statements and in Moody's

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[26]Enron presentation on Yosemite. Bates ECa000196339, 41.

[27]Citigroup email, November 14, 2001. Bates ECp000097038.

[28]Citigroup email, November 14, 2001. Bates ECp000097037.

[29]Chase emails, October 24, 2001. Bates SENATE MAH 00645.

[30]Salomon Smith Barney presentation, "Capitalization". September 20, 1999. Bates CITI-SPSI 0031094 - 98.

analysis of Enron.[31] In Enron's financial statements, the prepay number was not shown as debt but was buried in Price Risk Management Liabilities and not disclosed separately from Enron's other trading liabilities. There would be no way for an institution other than Enron, the bank involved, or Enron's auditor to know how much in prepay transactions was outstanding.[32]

Clearly, Citigroup had better insight into Enron's true financial condition than most other actors, acknowledging that "there is no question that Enron cashflow has become more dependent on Price Risk Management (prepay) activities."[33] It is safe to conclude that analysts and investors also would have been interested in evaluating these outstanding Enron commitments; in the case of so-called prepays, that analysis was impossible for outsiders.

In advance of Enron-linked securities offerings in 2000 and 2001 (the Yosemite and ECLN offerings), Citigroup prepared additional internal Enron credit analyses, using the same methodology employed in the first analysis. In all instances, the level of indebtedness was significantly higher than what was reported in Enron's financial statements.[34] The aggregate amount of debt related to prepays increased from $750 million in the September 1999 SSB internal analysis to more than $2.2 billion in the April 2001 analysis. This $2.2 billion includes Yosemite I, Yosemite II and ECLN I proceeds, which were used to fund new prepay transactions. Only Enron and Citigroup knew the use of Yosemite I and II and ECLN I proceeds, given the "blind" nature of these trusts. Citigroup included this information in its internal analysis of Enron, increasing Enron's publicly disclosed debt levels by the amount of the Yosemite and ECLN offerings, as well as the $750 million attributed to prepays in SSB's initial internal analysis. This fact raises questions regarding Citigroup's representation of Enron's financial condition in the offerings for Yosemite and ECLN securities.

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[31]Representatives of Citigroup pointed out that some structures included in their analysis were already counted, at least in part, in the Moody's analysis, therefore indebtedness linked to these structures may have been double-counted in the initial SSB internal analysis. These items included $1.5 billion from Condor, $550 million from Marlin; $500 million from Margaux and $450 million from Firefly. Bates CITI-SPSI 0031097.

[32]Not even Citigroup knew how much Enron had outstanding in prepay transactions. Yet, the firm viewed prepays as an important component of Enron's capital commitments, as reflected by Citigroup's inclusion of prepays in the analysis. In explaining why Citigroup decided to include the prepay number in the capitalization analysis, while it did not include any other trading liabilities, the SSB banker who oversaw the first analysis told Subcommittee staff that, "We knew the number was there, and it has cash flow that has already been spoken for associated with it." Staff Interview, July 16, 2002.

[33]Citigroup email, "Enron Credit Approval," April 18, 2001. Bates CITI-SPSI 0085843.

[34]November 1999 analysis: SSB estimate of Enron debt was 38% higher than debt reported in Enron's financial statements. Bates CITI-SPSI 0005184. August 2000 analysis: SSB estimate of Enron debt was 40 - 53% higher than debt reported in Enron's financial statements. Bates CITI-SPSI 0007241. April 2001: SSB estimate of Enron debt was 57 - 92% higher than debt reported in Enron's financial statements. Bates CITI-SPSI 0008756.

Incentives for Financial Institutions to Support Enron's Accounting Deceptions

There are many possible explanations for why major financial institutions were willing to go along with and even expand upon Enron's "prepay" activities. One obvious incentive was the fees paid by Enron which provided lucrative business deals to a number of financial institutions on Wall Street and elsewhere. Citigroup earned approximately $167 million from 1997 through 2001.

In addition, in some cases, Enron explicitly pressured some financial institutions to participate in particular "prepay" transactions, as a favor and inducement for Enron to channel additional business their way. A series of Citigroup emails illustrates this issue.

- A September 2001 Citigroup email states: "Spoke with Ben Glisan, [Enron Treasurer], re our turn down of the $200mm prepaid bridge request. . . . He was calm and did not threaten loss of any specific business. . . . [T]his turndown was major disappointment and perhaps a first from Citi but we still have significant capital committed and Enron recognizes that. . . . Expect will continue to work on existing deals with us but intend to spread the business. . . . Told him that we intended to work even harder on the relationship etc. More to come; I have call with Fastow today."[35]

- An October Citigroup email a few days later states: "Spoke with Fastow . . . . CP rollover was clear financial need in a difficult time while the prepaid was an accounting need in a difficult time and we differentiated between the two. Talked about need for continuing dialog particularly our appetite for additional Enron paper during the quarter."[36]

- A Citigroup email exchange[37] a week later states:

  -"Last week, we were informed by enron that we had not been selected to arrange either project X (monetize contract values in their price risk book) or project popeye. . . . Each are potentially precedent-setting and lucrative deals. . . . Also: chase and csfb did provide prepays at the end of the last quarter - csfb replacing us when we rejected the 200mm request. . . ."

  -"With respect to Brazos I specifically visited with Glisan several weeks ago before the $200mm request was on the table saying that we had some issues with Brazos such that we would prefer not to participate but I wanted feedback from him as to how important it was to them and that we would have to look at it as a 'trust me, Enron relationship deal'. He said he would prefer not to do 'trust me' deals and he would get back to me.

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[35]Citigroup email, September 26, 2001. Bates CITI-SPSI 0085837.

[36]Citigroup email, October 1, 2001. Bates CITI-SPSI 0085836.

[37]Citigroup emails, October 8, 2001. Bates CITI-SPSI 0085833-34.

> He has not. Also at same meeting questioned him on what he had 'scheduled' for us for remainder of year. . . . . We still have the existing $250mm prepaid to deal with for which they still 'owe' us one for having provided the $250mm originally."

CSFB emails show similar concerns, as well as actions by Enron to encourage the financial institution to participate in a "prepay." A CSFB email exchange[38] in September states:

> - "Please remind me as to who at Enron originally asked for this deal and why we agreed to do it (and most importantly what did CSFB get from it besides being nice guys once again)."
> - "We agreed to do the deal [a prepay] as it was a special request/favor from Ben [Glisan]. Not sure if we got anything specific other than a relationship building chip."

In the case of Citigroup, another motivation in setting up the Yosemite and CLN structures was to lower its own exposure to Enron. A Citigroup memorandum states, "these prepays [Roosevelt and Truman] will be repaid with the proceeds from the Yosemite, ...eliminating the obligor exception." Instead, credit exposure for all the Yosemites and CLNs was transferred to the bondholders.[39]

After several years of participating in Enron "prepays," both Chase and Citigroup found another reason to go along. Both began attempting to sell the product to other companies. Chase informed the Subcommittee that it entered into Enron-style prepays with seven companies apart from Enron.[40] Citigroup indicated that it shopped the idea to 14 companies apart from Enron, successfully selling it to at least three.[41]

This evidence suggests that Enron is not the only company obtaining loans disguised as energy trades and recording cash flows from operations instead of from financing. Major financial institutions are knowingly assisting and even promoting such transactions, which would not be possible without their willingness to provide the funds, supporting paperwork, and a sham offshore trading partner.

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[38]CSFB emails, September 17, 2001. Bates SR 00037828.

[39] Global Loans Approval Memorandum, Citigroup, October 19, 1999. Bates CITI-SPSI 0002996.

[40]Chase correspondence with the Subcommittee, July 18, 2002.

[41]Citigroup correspondence with Subcommittee, July 17, 2002.

APPENDIX C

JPMORGAN CHASE CASE HISTORY

Chase Manhattan Bank, N.A. ("Chase") arranged the first prepay for Enron in 1992 apparently so that Enron could claim oil exploration tax credits that would soon expire. To prevent the credits from expiring, Enron needed to find a way to accelerate income into that year. While early prepay transactions appear to be tax-driven, starting in the mid-1990s, prepay transactions were executed in order to meet funding objectives. By 2001, Chase (or its predecessor, Chase Manhattan Bank[1]) had arranged approximately $3.7 billion in prepays for Enron. Approximately $1.6 billion of the Chase-Enron prepays remains outstanding.

How the Chase Prepays Worked

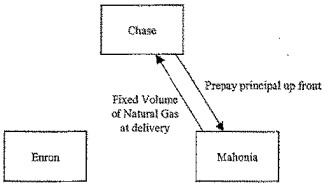
Typically, Enron would initiate the prepay transaction near the end of a financial reporting period when Enron determined it needed to report more cash flow from operations on its financial statement. Enron would contact Chase and request that Chase arrange a prepay. A Chase employee familiar with the Enron prepays said he was not aware of any instances when Chase refused Enron's request (although occasionally, the size of the prepay would be reduced from Enron's original request).[2]

Chase set up a Special Purpose Entity or SPE called Mahonia Ltd. to serve as the "independent" third party in the Enron prepays. The basic steps of the Chase prepays are as follows:

[1]Enron entered into its first prepay transactions with Chase Manhattan Bank, known currently as JPMorgan Chase Bank as the successor by merger.

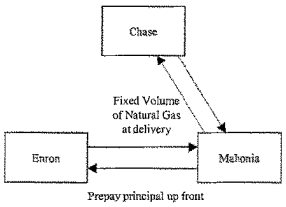
[2]Staff Interview, June 26, 2002.

- Chase and Mahonia execute a contract in which Mahonia receives funds from Chase, and in exchange, agrees to deliver to Chase a fixed amount of gas at specified dates and locations agreed to in advance. This is called a prepaid forward contract. The price paid for the gas is the estimated future price of the gas on the expected delivery date.



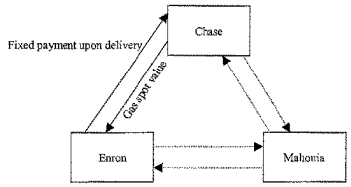
Chase-Mahonia Prepay Leg

- Mahonia and Enron (or an Enron subsidiary, such as Enron North America or Enron Natural Gas Marketing Corp.) simultaneously execute a mirror contract in which Enron receives funds (the same amount of funds that Mahonia received from Chase) from Mahonia, and in exchange, agrees to deliver to Mahonia a fixed amount of gas at specified dates and locations agreed to in advance. Thus, Chase ends up holding title to a fixed amount of gas that was transferred from Enron to Mahonia and Mahonia to Enron.



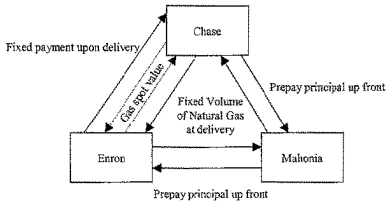
Mahonia-Enron Prepay Leg

- At the same time that the two prepaid contracts are executed, Enron and Chase execute a commodity swap agreement in which Enron pays Chase a fixed price (a predetermined amount that is equivalent to principal plus an implied interest rate) and Chase pays Enron the floating price on the same quantity of gas that passed from Enron to Mahonia and Mahonia to Chase in steps one and two above.[3] There is no transfer of title to the gas in this transaction. This transaction is called a financially settled commodity swap. Enron generally pays the fixed price in installments.



Chase-Enron Commodity Swap

- At the same time that Chase receives title to the gas from Mahonia and pays the equivalent of the floating price to Enron under the swap agreement, Chase sells the gas to the market (in some cases, back to another Enron entity) at the spot price.



Complete Structure Including Chase Gas Sale

[3] Prior to 1996, the prepay transactions included some price risk. In 1995, for example, the structure did not include a prepaid forward contract (a contract to purchase a commodity now for future delivery) between Mahonia and Chase. Instead, Mahonia and Chase entered into a financially settled swap. Mahonia then entered a prepaid forward contract with Enron. Mahonia took delivery of the oil or gas from Enron and sold it in the spot market. Mahonia hedged its price risk with a futures contract.

In sum, Enron receives cash up-front from Mahonia, which has been funded by Chase. Enron pays the cash plus interest back to Chase according to a prearranged schedule.[4] The price risk is eliminated because deliveries are made simultaneously among the parties with Chase selling the gas to the market at the spot price at the same time on the same day that it receives title to the gas. To ease the burden on Chase, which must sell the gas for cash, in most transactions Enron agreed to buy the gas.

Credit support

The basic prepay structure has two key credit support mechanisms to guarantee the parties' obligations, thus removing the performance risk in favor of Chase. First, Enron provides an unconditional guarantee for the obligations of its subsidiary to Chase (through Mahonia). Second, the Enron guarantee is supported by either a Performance Letter of Credit ("PLC") with Enron as the account and Mahonia as the beneficiary; or by surety bonds issued by insurance companies. The PLC amortizes according to the amortization schedule of the Enron subsidiary's delivery of gas to Mahonia. That is, if Enron defaults on its guarantee, drawings on the PLC will match the amount outstanding on the prepay amortization schedule. Enron pays the PLC fees, which are determined according to Enron's senior debt rating.

Sometime in May or June 1998, Enron approached Chase about replacing the existing PLCs with surety bonds. The surety bonds would guarantee Enron's delivery performance obligations. If Enron defaulted on its guarantee, the insurance companies would be obligated to pay liquidated damages.[5] Enron wanted to replace the PLCs with surety bonds issued by insurance companies to free up additional bank capacity and because it could obtain credit support from sureties at a more competitive rate.[6] The surety exposure was limited by spreading it across ten insurance companies. Chase agreed to replace the PLCs with the sureties in September 1998.[7]

Ownership and Control of Mahonia

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[4]In memoranda documenting discussions between Chase and Enron regarding prepays, fees typically are discussed in terms of the London Interbank Offered Rate (LIBOR) plus a basis point spread, terms generally used to refer to pricing on loans. Bates JPMC-H-011470; Bates JPM-6-04204; Bates Senate-MAH 02296.

[5]When Enron failed to meets its obligations, and the insurance companies failed to pay liquidated damages, Chase filed a complaint on December 11, 2001, to force the insurance companies to pay. The insurance companies claim that the prepay transactions were nothing more than a "complicated (and undisclosed) . . . loan" from Chase to Enron using Mahonia as a pass-through vehicle.

[6]Chase email, "re: request for credit approval to replace PLCs," September 22, 1998. Bates JPMC-H 011640.

[7] Staff Interview, June 25, 2002.

Although Mahonia is technically a legally separate entity from Chase, the facts surrounding its creation, operation and control raise questions as to whether it is truly independent. In 1986, Chase sought the assistance a Jersey law firm, Mourant du Feu & Jeune ("Mourant"), in establishing a charitable trust to own special purpose vehicles that would be "controlled by Chase but, for accounting and other requirements...[not be] wholly owned by Chase."[8] Chase wanted to use the trust to assist clients who wished "to raise finance not by way of borrowing but by way of a related transaction."[9] To accomplish this objective, Mourant created the Eastmoss Charitable Trust ("Eastmoss"), which would come to own a number of SPEs that served as counter-parties to prepay transactions with Chase and Chase's clients. Mourant served as trustee for Eastmoss.

Chase's ongoing involvement in Eastmoss and its related entities is undeniable. In thanking the Commercial Relations Department of the States of Jersey for assisting with incorporation of Eastmoss, Mourant adds that the Department's work "was very much appreciated . . . by Chase."[10] The purpose of the SPEs was to "issue notes and to finance transactions arranged by Chase Bank."[11] Documents indicate that over twenty-five Jersey registered companies owned by the Trustees of the Eastmoss Trust were created on Chase's behalf.[12] One of these companies was Mahonia Limited.

Mahonia Limited, created by Mourant in December 1992, is described as a "finance company" whose purpose is "to assist in transactions arranged by Chase Bank."[13] Mourant defined the purpose of these vehicles more narrowly in a letter regarding the incorporation of Mahonia II Limited: "The overall effect of these arrangements will be that Chase will be providing finance to the relevant US Oil or Gas company on the security of the inventory of Oil or Gas, but without [Mahonia II] taking any exposure to the Oil and Gas market."[14] In reality, Mahonia could not have functioned as an independent trading party because it had only £10,000 of capitalization,[15] no employees and Mourant attorneys who served as the Directors. In each prepay transaction Mahonia's financing came from Chase, and a security agreement signed by Mahonia in favor of Chase gave Chase a lien on all rights to receive gas, collateral and proceeds. In addition, for each

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[8]April 24, 1986 application letter to Commercial Relations Officer for Island of Jersey from Mourant, page 2.

[9]Ibid., page 1.

[10]May 29, 1986 letter to Assistant Commercial Relations Officer for the Island of Jersey from Mourant.

[11]States of Jersey creation documents for Stoneville Aegean Limited.

[12]"Jersey Registered Companies Owned by the Trustees of Eastmoss Trust."

[13]States of Jersey creation documents for Mahonia Limited; Chase Staff interview confirmed that Mahonia only performed transactions involving Chase.

[14]Letter to the Jersey Financial Services Commission from Mourant, November 19, 1999. February/March, 2002 Mourant email discusses "anomalies" in which Mahonia was excluded from certain trades, indicating that Mahonia's sole purpose was to overcome legal and accounting hurdles rather than to serve as a pivotal trading partner.

[15]States of Jersey creation documents for Mahonia Limited.

prepay transaction, Mahonia agreed to let Chase operate as its agent. The agency agreement allowed Chase to review transaction documents on behalf of Mahonia, and even more broadly, to "perform such other functions as are reasonably" necessary.[16] Chase controlled Mahonia so completely that such a security agreement was probably superfluous.

If Mahonia and Chase are substantively the same entity, then Enron's prepay transactions have but two legs and must be accounted for as loans. Mahonia is a non-substantive entity established for the benefit of Chase:

- Chase used Mahonia to assist clients who wished "to raise finance not by way of borrowing but by way of a related transaction."[17]
- Mahonia could not have functioned as an independent trading party because it had only £10,000 of capitalization,[18] no employees and Mourant attorneys who served as the Directors.
- In each prepay transaction Mahonia's financing came from Chase.
- Chase and Enron bypassed Mahonia in pipeline agreements for certain trades.[19]
- Mahonia attorney states that Mahonia "would be controlled by Chase but, for accounting and other requirements...[not be] wholly owned by Chase.[20]
- Chase was granted power of attorney and named as agent by Mahonia.[21]
- Chase's attorneys would review the documents on behalf of Mahonia and forward the documents to Mourant attorneys for them to sign.[22] In some cases, Enron's attorneys from

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[16]Agency agreement between Chase and Mahonia, September 28, 2001. Bates JPM-6-03145.

[17]April 24, 1986, application letter to Commercial Relations Officer for Island of Jersey from Mourant.

[18]States of Jersey creation documents for Mahonia Limited.

[19]February 2002 Mourant email discusses "anomalies" in which Mahonia was excluded from certain trades, indicating that Mahonia's sole purpose was to overcome legal and accounting hurdles rather than to serve as a pivotal trading partner.

[20]April 24, 1986 application letter to Commercial Relations Officer for Island of Jersey from Mourant.

[21] See, for example, letter from Mahonia to Chase, September 28, 2001. Bates JPM-6-03145.

[22] Chase, Staff Interview, June 25, 2002; Chase, Staff Interview, July 16, 2002; Chase email to Mourant in which a Chase attorney states that he is "in the process of reviewing the enclosed documents and will provide comments on Mahonia's behalf to Enron," September 24, 2001. Bates JPM-6-03044; email from Chase to Mourant attorneys states that "the following documentation forwarded by Vinson & Elkins is acceptable and may be executed by Mahonia," June

Vinson & Elkins would review the Enron-Mahonia documents and forward them (assumably for Mahonia's review) directly to Chase.

- Chase did not charge Mahonia a fee for its services, and, in fact, reimbursed Mahonia for any administrative fees incurred as a result of transactions with Chase.[23]

- When Enron employees needed to communicate with Mahonia, they directed all inquiries through Chase.[24]

- Chase bankers made business decisions for Mahonia, such as whether or not to close bank accounts.[25]

- When Arthur Andersen sought to confirm Mahonia's independence from Chase, employees of Chase and Enron crafted Mahonia's response.[26]

Further evidence indicates that contracts between Enron, Chase and Mahonia did not achieve the other criteria outlined by Arthur Andersen for treating prepays as trading activities: de-linkage and price risk.

28, 2000.

[23] Chase, Staff Interview, July 16, 2002; Mourant invoice sent to Chase, October 29, 2001. Bates JPM-6-03128.

[24] Enron, Staff Interview, June 28th, 2002.

[25] Chase email to Mourant. ". . . close a number of dormant demand deposit accounts . . . close all but two accounts (Mahonia Limited and Mahonia II Limited)," April 27, 2000. Bates JPMC-H 011240.

[26] Email exchange among and between Chase and Enron, September 2001. Bates SENATE MAH - 00765. Approximately two weeks before the September 2001 prepay transaction was scheduled to close, Arthur Andersen communicated to Enron that they would like Mahonia to make four representations: (1) Mahonia was not restricted from undertaking business with other entities and that it had undertaken business with entities other than Enron; (2) Mahonia had assets other than those acquired through transactions with Enron; (3) Mahonia had unencumbered assets, which were available for application toward obligations owed to its creditors; and (4) Chase and its consolidated subsidiaries do not own the ownership interests of the Company or consolidate the Company under generally accepted accounting principles. Arthur Andersen did not, however, ask Mahonia to confirm that it had participated in transactions other than with Chase.

The resulting letter from an Enron executive, dated September 26, 2001, informed Mahonia that Arthur Andersen would like to confirm information as part of "an audit of [Enron's] financial statements." The Subcommittee learned in Staff Interview with Andersen, July 13, 2001, that Andersen allowed Enron to send the letter, which was addressed to Mourant and signed by the Enron executive, directly to Mahonia and that it was returned by Mahonia directly to Enron. The normal course of action when an auditor is attempting to confirm information from a third party as part of an audit is for the auditor to maintain custody of the letter, including sealing the envelope, sending the confirmation letter, and receiving the third party's response.

The purpose for this audit approach is to ensure that terms of the confirmation letter are not changed by the third party. In this case, point number four (4) from above was changed to "The Chase Manhattan Bank and its consolidated subsidiaries do not own the ownership interests of the Company" before the letter was signed and returned by Mahonia.

- The Security Agreement between Chase and Mahonia related to the December 1997 Chase/Enron prepay gives Chase a lien on Mahonia's rights and interests in its agreement with Enron. Enron consented to that Agreement.[27]

- Mahonia was perfectly hedged in its transactions with Enron and Chase in every prepay.

- Mahonia's profit from each of the prepays was fixed and in no way dependent on the market price of the underlying commodity.[28]

- Margin calls owed by Enron to Mahonia as a result of changes in the market price of the commodities underlying the prepay transactions were, in some instances, never made, demonstrating that Mahonia neither benefitted not lost in its transactions with Chase on the basis of market fluctuations.[29]

- Enron had an elaborate methodology for backing into the monetary values in the prepay transactions irrespective of commodities prices.[30]

- Pricing of prepays with Chase were based on LIBOR, a convention for pricing bank loans.[31]

September 28, 2001, Prepay

The last Enron prepay closed on September 28, 2001, and was arguably the most obvious about its true purpose. At that time, Enron needed to identify additional operating cash flow to report in its third quarter financial statements and was making inquiries of several financial

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[27]Consent and Agreement for the December 1997 Chase/Enron Prepay, Bates JPMC-H 003030, and the corresponding Security Agreement between Mahonia and Chase, Bates JPMC-H 000045. Arthur Andersen stipulates that the contracts in the Prepay must stand alone and not reference each other in any way, especially in the event of default. Under this arrangement Chase received all rights to floating payments by Enron to Mahonia and accepted all responsibilities of Mahonia. The arrangement would cause Mahonia and Chase to collapse into a single entity in the event of a Mahonia default. The net result of that collapse would have Enron paying a fixed amount to Chase under the Enron-Chase swap agreement in exchange for the cash it was prepaid originally, a typical loan arrangement.

[28]Letter from Mourant to Chase regarding a fixed management fee and administration fee. Bates JPM-6-04141; September 5, 2000, email from Mourant describing Mahonia's fees as being "levied on a fixed basis" and not "factored into trading prices," JPMC-H 011239; Mourant memo to Chase dated December 11, 1996: "In return for participation in the transaction described in your letter Mahonia Limited would levy a fixed management and administration fee of £15,000."

[29]Chase email, July 17, 2000. Bates SENATE MAH - 02500.

[30]Enron email to Chase describes in detail Enron's methodology, June 19, 2000. Bates SENATE MAH - 00757.

[31] Bates SENATE MAH 02296 and Bates JPM-1-00061.

institutions about the possibility of executing a prepay transaction.[32] When two Enron employees called Chase about doing a $350 million prepay designed to close before the end of the third quarter, an Enron manager told Chase that Enron would "take any money (it could get) now even if it's on a one year basis."[33]

Eventually, Chase and Enron agreed on a prepay with a six month duration/maturity. Unlike previous Chase/Enron prepays, the parties agreed that the transaction would be financially settled; thus, rather than execute two prepaid forward contracts and a swap, the structure had three swaps. The transaction closed on September 28, 2001, with bullet payment scheduled for March 26, 2002. The structure included the following steps:

- Chase and Mahonia entered into a prepaid commodity swap whereby Chase transferred $350 million to Mahonia on September 28, 2001, and Mahonia agreed to pay a floating price calculated by multiplying the notional quantity of natural gas (127,923,977 MMBtus) by the market price for gas on the agreed upon payment day, March 26, 2002. The floating payment was to be derived from the price of gas on March 25, 2002, of the NYMEX Henry Hub Natural Gas Futures Contract for the April 2002 delivery month.

- Mahonia and Enron entered into a mirror contract whereby Mahonia paid $350 million to Enron on September 28, 2001, and Enron agreed to pay the same floating price on the same payment day, March 26, 2002. (Enron agreed to pay an arrangement fee of $1 million at closing to be deducted from the $350 million prepayment amount.[34])

- To hedge their exposure from the price risk created by the prepaid swaps in steps one and two, Enron and Chase entered into a financially settled commodity swap whereby on March 26, 2002, Enron was to pay a fixed price to Chase determined by multiplying $2.7826 by the notional quantity of natural gas, 127,923,977 MMBtu ($355,961,258). In return, Chase was to pay on March 26, 2002, a floating price determined as described in step one and step two.

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[32]Concurrent with its discussions with Chase, Enron was executing a $150 million prepay "refinancing" with Credit Suisse First Boston ("CSFB"). Moreover, Enron requested an additional $200 million in prepay financing from CSFB, bringing the total prepay funding sought by Enron prior to prior to the end or the third quarter 2001, to $700 million.

[33]Chase email, September 12, 2001. Bates SENATE MAH - 0721. Initially, Enron requested that the prepay be backed by surety bonds as in similar prepays. Chase's credit department refused because the bank did not want to take on additional surety exposure and would no longer accept the bonds as credit support. Enron signed a guarantee, as it did for previous prepay transactions, in favor of Chase to guarantee the performance of its subsidiary, Enron North America. To mitigate risk, Enron brought Westdeutsche Landesbank Girozentrale ("WestLB") into the transaction, and WestLB underwrote a letter of credit for $165 million that was syndicated to other banks. Chase also arranged a syndication of banks that issued a second letter of credit for $150 million in Mahonia's favor. The letters of credit were posted to secure Chase's exposure under the prepaid commodity transaction. WestLB has refused to pay, and Chase has filed a lawsuit against WestLB in a United Kingdom court.

[34]Fee letter from Chase to Enron, September 28, 2001. Bates SENATE MAH- 03273.

The result of these financially settled swaps was that Chase provided $350 million to Enron in September 2001, and Enron promised to re-pay Chase $355.9 million in March of 2002. In effect, Chase loaned Enron $350 million, and Enron agreed to re-pay the principal within 6 months at an effective annual interest rate of 3.44%.[35]

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[35]Effective interest rate does not factor in the $1 million up-front fee paid to Chase.

APPENDIX D

CITIGROUP CASE HISTORY

Citigroup, along with Chase was, was a major provider of prepays and financing to Enron. Beginning in December 1993, Citigroup led 14 separate prepay transactions totaling $4.8 billion for Enron. The total outstanding Citigroup prepay debt at the time of Enron's bankruptcy was $2.5 billion.[1]

The structure employed for Citigroup's prepays closely follows the structure of Chase/Mahonia transactions with Enron.[2] Citigroup created an offshore entity called Delta Energy Corporation in the Cayman Islands, which along with Enron and Citibank, would form the familiar triangle used to structure the prepays and remove price risk from the transaction.

The most prominent structural difference between the Enron/Chase transactions and the Enron/Citigroup transactions was the manner in which the later Enron/Citigroup transactions were financed. The first Enron/Citigroup transactions involved financing similar to the Enron/Chase transactions, in which the bank served as the source of funds that went through the special purpose entity, Delta, and on to Enron. Later Enron/Citibank transactions, representing $2.4 billion of the total $4.8 billion in prepay transactions between the two parties, were financed through bond offerings. "Yosemite" was the name of a series of six synthetic Enron bond offerings used to raise the $2.4 billion.[3] All of these bonds, with maturities ranging from five to seven years, remained outstanding at the time of the Enron bankruptcy.

For each of the offerings, a trust that was off-balance sheet to Enron offered credit linked obligations (notes that were linked to Enron's credit) to "Qualified Institutional Buyers."[4] By raising the funds for the prepays in this fashion, the institutional investors, rather than Citigroup, took on the risk that Enron would not or could not repay the funds. No additional credit support, such as surety bonds or letters of credit, was employed.

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[1]See Appendix E for a list of all the Citigroup prepays.

[2]Citigroup's prepays involved the transfer of crude oil and natural gas. Prior to 1999, the transactions appear to have been physically settled -- the title to ownership of the commodity was transferred among the parties to the transactions. Thereafter, the transactions were all financially settled -- the funds representing the net value of each of the trades and swaps between the parties to the transaction was transferred among the parties.

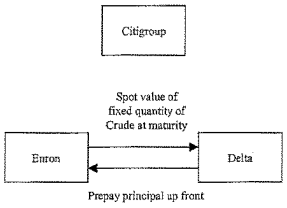
[3]They were: Yosemite I, 11/18/99, $750 mm; Yosemite II, 2/23/00, £200 mm; Yosemite III (issued as Enron CLN I--Credit Linked Note), 8/17/00, $500 mm; Yosemite IV (issued as Enron CLN II), 5/17/01, comprising 3 offerings: $500 mm; £125 mm; and 200 mm Euros.

[4]Under SEC rules, "Qualified Institutional Buyers" are entities that have sufficient resources and investment sophistication that they are deemed capable of making investment decisions without the offering material being filed with the SEC for adequate disclosure review. These are commonly called Rule 144(A) offerings.

How the Citigroup Prepays Worked

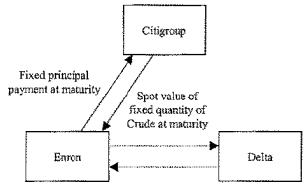
The same basic triangle employed in the Enron/Chase prepays applied to the Enron/Citigroup transactions. For illustration purposes, a simplified prepay transaction is described with the Yosemite I Trust providing the initial funding.

- The Yosemite I Trust loaned $800 million proceeds to Delta Energy, a Citigroup SPE.
- Delta immediately entered into a cash-settled prepaid forward contract with Enron. Delta paid Enron the $800 million up front. In return, Delta would receive the spot price value of a preset number of barrels of crude oil at maturity. The net difference between Delta's payment to Enron and the value of the crude oil owed to Delta by Enron would be settled through a cash payment.



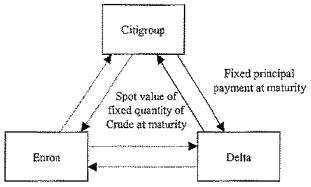
Delta-Enron Prepay Leg for Yosemite I

- At the same time, Enron and Citigroup entered into a hedging transaction.[5] In a cash-settled swap, Enron would receive the spot value of the same fixed amount of crude as in the Enron-Delta transaction at maturity, while Citigroup would receive a fixed value of $800 million at maturity.



Enron-Citigroup Commodity Swap (Hedge)

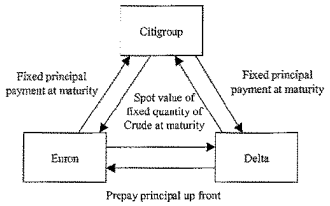
- Meanwhile, Citigroup and Delta entered into a hedging transaction. In a cash-settled swap, Citigroup would receive the spot value of the same fixed amount of crude as in the Enron-Delta and Citigroup-Enron transaction at maturity, while Delta would receive the fixed value of $800 million at maturity.



Citigroup-Delta Commodity Swap (Hedge)

[5]A hedging transaction is a transaction established to limit or eliminate the risk a party bears in another transaction. In this case, Enron has price risk in its transaction with Delta - i.e., the $800 million it receives from Delta might be less than the cost of the spot price of the oil that it owes to Delta. Similarly, Citibank has price risk from the transaction that it enters into with Delta as part of the series of transactions involved in this prepay transaction - the spot value of the oil it receives from Delta may be less than the $800 million it pays up front to Delta.

In this arrangement, the spot value of the crude oil that each party owes and receives cancel each other out. Thus, the net effect is that the only transfer of funds is the transfer of $800 million from Enron to Citigroup and back to Delta, from which it originated.[6]



Complete Citigroup Prepay

In effect, Enron receives $800 million at the beginning of the transaction and repays the principal to Delta (via Citibank) at maturity. Every six months an interest payment, the spot value of a certain fixed volume of oil, is returned to Delta by Enron. Swaps in place on the Enron/Citibank and Citibank/Delta legs ensure a fixed interest payment of $29 million being paid to Delta every six months, an effective rate of 7.25%. The risk retained by Citibank and Delta is the same as if they loaned money to Enron. The effect of the transaction is like a loan, but it is not accounted as such in Enron's financial statements.

Citigroup and Enron also introduced a series of caps and floors on the payments made in each leg of the transaction.[7] These floors and caps ensured that no party paid or received more or less than

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[6]Another way to look at the structure is to look at the net cash payments at maturity for each leg. The Enron-Delta leg pays the spot value of the fixed number of barrels back to Delta upon maturity. This value may be more or less than $800 million. If it is more than $800 million, the swaps in the other trading legs effectively "refund" the spread to Enron via Citigroup. If the Enron-Delta payment at maturity is less than $800 million, the swaps in the other trading legs effectively provide a "make-whole" payment paid by Enron to Delta via Citigroup such that Delta's payments from both legs total $800 million. Price risk is eliminated. The net result is that $800 million of principal is routed directly and indirectly from Enron to Delta upon maturity.

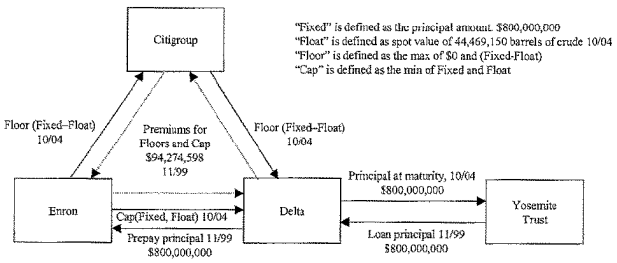
[7]The purpose of the floor/cap arrangement was to eliminate excess pre-settlement risk (PSR) on the principal. The problem addressed arises from the case where the spot value of the oil at maturity is greater than the fixed amount of $800 million. Under this circumstance, the cash in excess of $800 million that needs to be in transit during settlement represents additional risk for the parties depending on how the legs settle.

The Yosemite structures place a cap on the cash payment at maturity from Enron back to Delta. The cap is set to the fixed amount, namely $800 million in the case of Yosemite I. There is no longer any need for additional cash to refund the excess payment to Enron via Citigroup should the spot value of the crude exceed $800 million. To complete the structure, floors along the path from Enron to Delta via Citigroup block payments in the reverse direction for the high spot value case.

Therefore, if the spot value paid by Enron to Delta at maturity is less than the fixed value, just as before, the

the original $800 million paid by Delta. The floor/cap arrangement was considered proprietary "prepay technology" by Citigroup, not to be revealed to other financial institutions.[8]

To ensure that each leg of the triangle appears as a true trading contract, there is also an up-front premium payment made in each leg to cover the value of the cap or floor derivatives in each leg. Since the price of each derivative ($94 million for Yosemite I) is identical for each of the legs and flows in the same direction around the triangle, no net payment accrues to any party. The net effect, however, is that the $800 million up-front prepay from Delta to Enron is reduced to $706 million, and an additional "premium payment" flows from Delta to Enron via Citigroup. Enron still receives the same $800 million up-front.



Yosemite I Principal Payments

Upon close-out of the trading legs, Delta repays the $800 million principal to the trust, which then pays back the bondholders.

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swap/floor still effectively provides a make-whole payment from Enron to Delta via Citigroup such that Delta's payments from both legs total $800 million. If the spot value at maturity is greater than or equal to the fixed value, then a payment of the fixed value is made by Enron directly to Delta. No payments are made on the other legs. In either case, price risk is eliminated, but now the total amount of cash in transit prior to settlement is never more than the fixed value, namely $800 million in the case of Yosemite I.

[8]Citigroup email, "RE: Yosemite II (Europe)," November 16, 1999. Bates CITI-SPSI 003361.

Ownership and Control of Delta

Similar to the Enron-Chase prepays, all but one of the Citibank-Enron prepays involved an SPE, Delta Energy Corporation, which was incorporated in the Cayman Islands in 1993 at the request of Citigroup.[9] Its purpose was to be a third party to the prepay transactions. None of the individuals interviewed from Enron and Citigroup, however, indicated to the Subcommittee that Delta was anything other than an SPE established for the sole purpose of entering into contracts to effect prepays.

Although Delta appears, technically, to be a legally separate entity from Citigroup, as with Mahonia, the facts surrounding its creation, operation and control prove otherwise. Delta is a non-substantive entity established for the benefit of Citigroup.

- Delta was established by Citigroup.[10]
- There is no indication that Delta has a physical office or staff, or that it has the personnel or physical facilities to engage in oil and gas trading.
- Delta only participated in prepay transactions that also included Citigroup.[11]
- Delta was capitalized with only $1,000. It could not have participated in trading activity of the size of the Yosemite deals without receiving financing from Citigroup or Yosemite Securities Trust.[12]

Citigroup controls Delta

- For each transaction, Citigroup and Enron prepared a set of completed documents for Delta.[13]

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[9]Delta was originally administered by Givens Hall Bank and Trust, Ltd. in the Cayman Islands and is now administered by Schroder Cayman Bank and Trust Company, Ltd. Schroder was acquired by Salomon Smith Barney, a subsidiary of Citigroup, in January 2000. As of September 10, 2001, Delta's parent company was Grand Commodities Corporation, also of the Cayman Islands. It is represented by Maples and Calder, Cayman Islands Attorneys at Law. Bates CITI-SPSI 0103726.

[10]Citigroup email, "RE: A couple more questions," August 31, 2000. Bates CITI-SPSI 0046024.

[11]September 3, 1999 Citigroup email implies that Citigroup is Delta's only business partner. Bates CITI-SPSI 0036322.

[12]Bates CITI-SPSI 0046605 and CITI-SPSI 0046542.

[13]Citigroup, Staff Interview, June 24, 2002.

- When third parties needed to communicate or negotiate with Delta, they directed all inquiries through Citigroup.[14,15]
- Delta's outside attorneys seek authorizations from Citigroup instead of from Delta directly.[16]
- Delta's expenses associated with prepay transactions were reimbursed by Citigroup.[17,18]
- Delta's Citigroup bank account is controlled by Citicorp.[19]
- Further evidence indicates that contracts between Enron, Citigroup and Delta did not achieve the de-linkage requirements set forth by Arthur Andersen.[20]
- Yosemite had cross-termination provisions that were designed to collapse the entire prepay structure in the event of a party's default.[21]
- As a result of a provision associated with the Yosemite trust, Citigroup effectively had a lien on Delta's right, title, and interest in Delta's agreements with Enron.[22]

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[14]Memo from Maples and Calder to Citigroup asks Citigroup to look into fees not paid by Enron to Maples and Calder related to Delta, September 10, 2001. Bates CITI-SPSI 0103726.

[15]Enron email to Citigroup to discuss representations that Delta needs to make to Arthur Andersen, June 22, 2001. Bates CITI-SPSI 0050675.

[16]Memo from Maples and Calder. They would like to disclose information about Delta and ask Citigroup "if you would confirm whether it is acceptable to you for this information to be provided." November 2, 1999. Bates CITI-SPSI 0046604.

[17]Fax from Bank of Bermuda (Cayman) Limited to Citigroup asking to be paid fees for work done related to Delta. Bates CITI-SPSI 0103717.

[18]May 16, 1999 fax to Citicorp Securities Inc. acknowledging that Delta fees were paid. Bates CITI-SPSI 0046893.

[19]Citigroup memos, "We will not be obtaining any documentation because of the internal nature of the account," September 27, 1994. Bates CITI-SPSI 0032825 and CITI-SPSI 0032830.

[20]Bates CITI-SPSI 0103943.

[21]See, for example, December 22, 1999, Citibank/Delta Swap Confirmation, p. 8, Bates CITI-SPSI 0003606. In his interview with Subcommittee staff, a Citigroup Vice President who signed many of the swap agreements, confirmed that the goal of these clauses was to collapse all three legs of the transaction simultaneously. Note: Swap Confirmation agreements for all three parties to the prepay (including the Enron-Delta leg) were drafted by the same attorneys for Citigroup, Milbank, Tweed, Hadley & McCloy.

[22]Enron/Delta Swap Confirmation, December 22, 1999, p. 8, Bates CITI-SPSI 0003580.

- Another provision of the Citigroup-Delta leg precludes Delta from making any changes in the Enron-Delta leg without the consent of Citigroup.[23]

- Citigroup emails after Enron bankruptcy show an operational concern for terminating the agreements on the same day.[24,25]

Finally, as with Mahonia in the Chase prepays, Delta did not have sufficient price risk in its transactions to justify accounting for them as trades.

- Citigroup paid Delta a fixed fee for serving as a party to the prepay transaction.[26]

- Delta never profited from or lost on price fluctuation in the commodities traded in the prepay transactions. Commodities prices were not a factor in profitability to Delta.[27]

- Values for legs of the Yosemite prepay were calculated based on borrowing rates instead of commodities prices.[28]

- Delta contracts designed to terminate simultaneously with other contracts to avoid price risk.[29]

Yosemite

Citigroup (then Citicorp) had been working with Enron on various financial transactions since 1989. The relationship earned Citigroup a total of $167 million in fees and interest income from 1997 to 2001.[30] By the first quarter of 1999, Citigroup's total exposure to Enron increased to

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[23]Citibank/Delta Swap Confirmation, December 22, 1999, p. 8, Bates CITI-SPSI 0003606.

[24]Citigroup email addressing the need to terminate the floating legs of a prepay transaction between Delta and Enron simultaneously, November 13, 2001. Bates CITI-SPSI 0068679.

[25]Citigroup email, December 2, 2001. Bates CITI-SPSI 0091839.

[26]From transaction documents, this amount, typically $5,000, was taken from the initial proceeds of each financing. Delta Fee document, Bates CITI-SPSI 0103719.

[27]Ibid.

[28]An Enron/Citigroup presentation for Yosemite prepay shows the prepay calculated in terms of LIBOR. Bates CITI-SPSI 0103942.

[29]Citigroup email, September 3, 1999. Bates CITI-SPSI 0036322.

[30]Citigroup letter to the Subcommittee, May 2, 2002, in response to Subcommittee subpoena.

$1.668 billion, a level more than four times Citibank's internally-imposed limit for Enron.[31] At this time, internal Citibank documents indicate that it was making efforts to rein in this exposure. One company email late in 1999 states, "we still have an exposure issue as it relates to obligor limits; there is a developing view that limits are limits and not to be exceeded. This is something we will all have to deal with."[32]

Sometime in early 1999, Enron selected Salomon Smith Barney to create a security known as a Credit Linked Obligation (CLO).[33] This structure allowed for securitization of assets by issuing obligations that looked like corporate bonds and would free-up bank capacity by tapping the capital markets, selling bonds linked to Enron credit. Enron's objectives for the CLO included limited "Rating agency disclosure", "Substitution rights" and "flexibility."[34]

Yosemite was intended to be a synthetic Enron bond. Its first issuance would offer a fixed interest rate of 8.25% – roughly 200 basis points above U.S. Treasury bills of matching tenor. In the case of an Enron bankruptcy, it would emulate an Enron bond: Yosemite bondholders would receive claims to an equivalent holding of senior unsecured Enron debt.

From Citigroup's perspective this was good business to pursue. The newly merged Citigroup possessed or could develop key capabilities to carry out the structure arm that was to become Yosemite. But besides the substantial fees it would earn on the deal, it would be a way to significantly reduce Citigroup's own exposure to Enron by rolling over its Enron loans into the capital markets.

A Salomon Smith Barney official described Enron's goal of achieving flexibility typically associated with a bank facility through the CLO vehicle. The "black box" feature of the Yosemite vehicle, which hid from investors Enron's use of the proceeds turned out to be an ideal cloak for prepays. In fact, a "Yosemite Update" presentation points out that the structure "provides for a unique 'black box' feature which provides considerable flexibility for substitution...while limiting disclosure of the prepay to Citibank."[35] The presentation goes on to state, "The use of prepays as a monetization tool is a sensitive topic for both the rating agencies and banks/institutional investors. The ability to continue minimizing disclosure will likely be compromised if transactions continue to be syndicated."

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[31]This "Obligor Limit" was set to $375 million prior to mid-1999. Global Loans Approval Memorandum, "Truman" Extension Transaction. Bates CITI-SPSI 0103768.

[32]Citigroup email, "RE: Yosemite II (Europe)" November 10, 1999. Bates CITI-SPSI 0033633.

[33]Citigroup, Staff Interview, June 24, 2002.

[34]Enron Presentation, "Project Yosemite," January 1999. Bates CITI-SPSI 0035868.

[35]Bates ECa000196339.

Both Enron and Citigroup clearly knew about and understood the accounting implications of Yosemite. An internal Enron memo states, "The use of the prepaid swap was not motivated by tax considerations but instead was necessary to report the transaction as part of ENA's price risk management activities rather than debt for financial accounting purposes."[36]

A Citigroup email provides an overview of the entire core functionality of the Yosemite transaction in a single, shorthand paragraph.[37] The text describes the transaction as "net net economically like a loan . . . E [Enron] gets money that gives them cflow [cash flow] but does not show up on the books as big D Debt."

The Yosemite Investments

Yosemite brought in a total of $825 million, $750 million from debt notes, and $75 million from equity certificates.[38] Of these proceeds, *all* were invested in so-called "Enron Investments"–

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[36]Enron memo, "Yosemite I Withholding", January 10, 2000, Bates EC2 000011612, footnote 5. The Subcommittee staff verified the conclusions in this document through a Staff Interview, June 18, 2002.

[37]Citibank email, "My take on how to explain ECLN." Bates CITI-SPSI 0084924.

[38]For various tax, ERISA, accounting, and structural considerations, Citigroup and Enron settled on $75 million worth of equity "certificates" to be issued. For tax purposes, Yosemite would be structured as a debt vehicle, the certificates would be first loss, and the certificates would bear 11% interest. The certificates were to be split evenly between Enron and Citigroup such that neither company would be required to consolidate Yosemite on its books, nor report the structure in footnotes to financial statements.

Although there was no apparent business purpose for doing so, Citigroup set out to mask the identities of the certificate holders–including Citgroup's own identity. All of the four Yosemite Offering Memoranda state that the identities of the certificate holders will not be revealed. The *de facto* owners, Enron and Citigroup, each turned out to have issues with their certificates.

Citigroup set up a "front" certificate holder using BankBoston (now FleetBoston Financial) as a "conduit" or "balance sheet provider." Fleet had previously established a general-use, special-purpose, off-balance sheet entity called Long Lane Master Trust IV. On paper, Long Lane "owned" the Yosemite certificate. However, through a Total Return Swap transaction with Fleet, Citigroup would effectively retain the rights and risks (albeit remote) of ownership. During an interview with Subcommittee staff, June 19, 2002, officials from Fleet stated that it was not their habit to ask questions of Citigroup about how the conduit would be employed and that they would hold this transaction, like any other transaction, confidential. The Subcommittee staff believes that such conduit providers are commonplace and are thought to be permissible–at least in their simple building block form–under a literal interpretation of accounting rules.

Since Citigroup was providing $37.5 million of credit for its share of the trust certificates, it analyzed its own risk position in a Global Loans Approval Memorandum. As part of Citigroup's agreement with Enron, Citigroup's equity certificates would realize preferential payback in case of an Enron bankruptcy by a factor of two over the Yosemite noteholders.

After Yosemite closed, Enron determined that for accounting reasons related to the disclosure of Yosemite on Enron's financial statements, Enron actually still had too much equity in Yosemite. Therefore, Enron acted to find

specifically defined in the Offering Memorandum as "payment obligations supported, in whole or in part, directly or indirectly, by Enron." Specifically, $800 million were invested in a prepay through Delta Energy.[39] (This was the exact amount of prepay obligations due in the fourth quarter of 1999 to two Citibank-structured prepays known as "Roosevelt" and "Truman.")

Yosemite II, CLN I, CLN II

Yosemite II closed in February 2000 for £200 million. Structurally, it was identical to Yosemite I, except that it was incorporated in Jersey, Channel Islands, rather than Delaware.[40] After Yosemite I and II, two more versions, Yosemite III and IV were issued. To the outside world, these were known as the Credit Linked Note (CLN) I (issued in August 2000) and CLN II, CLN Euro, and

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another buyer–before the year 1999 was out–for what amounted to 45% of the total Yosemite equity. Enron finally found a buyer in an Enron-related party, Whitewing. Enron did not sell its Yosemite certificate directly to Whitewing. Rather, the certificates were sold to Whitewing via LJM–the partnership managed by Enron Chief Financial Officer Andy Fastow–such that the certificates passed through LJM2's possession for a single day. Enron wanted to carry out a true value sale between the related parties, Enron and Whitewing. The transfer may well have missed the end-of-year deadline for a disclosure-related sale–the sale was formally closed in late February, 2000.

[39]The remaining $25 million was invested in what Enron called the "Magic Note." The Magic Note provided a "make whole" payment. The yield from Yosemite's investments inevitably fell short of the 8.25% advertised in the Offering Memorandum. Delta's note was set up to pay 7.25% interest. Therefore, a credit subsidy was needed to make up the spread between the actual and required returns. Bates EC2 000011608.

The $25 million "principal" was invested in Enron corporate bonds. The "interest" payments came back to Yosemite to exactly make up the difference in interest payments and certificate yield from the prepays that would be required to pay the noteholders and certificate holders the return they were advertised. The interest received for Yosemite I was nearly $10 million per year–an effective interest rate of 40% per annum.

[40]To provide further protection to Citigroup for Yosemite II, Citigroup's certificates would still receive preferential payback by a factor of two. Furthermore, an amount equal to the Citigroup certificate value of £11,125,000 Sterling was retained in the trust in the form of high-yield securities. This amount was intended to serve as collateral for Citigroup in the event of an Enron bankruptcy. Bates CITI-SPSI 0035139. As in Yosemite I, Enron transferred its share of all but 5% of the outstanding ownership of Yosemite II to Whitewing at year end 2000 for accounting disclosure reasons. However, instead of transferring the certificate to Whitewing via LJM2 as it had done for Yosemite I, Enron first transferred the certificate through FleetBoston's Long Lane Master Trust IV on its way to Whitewing. Bates AASCGA(TX)005886.

CLN Sterling (issued in three currencies in May 2001). These CLN structures offered a number of minor but significant improvements over the Yosemite I and II structures. Most of these had to do with simplifying the security from the bondholder's perspective, but Citigroup also took steps to reduce its own exposure.[41]

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[41]The main difference with the CLN was that all the investments were AAA rather than a mix of high-yield and Enron investments. The broad specification of AAA investments was largely appearance, however, as the trust simply invested its proceeds into Citibank certificates. Citibank then entered into a prepay agreement with Enron with Delta Energy as the hedging counterparty.

Citibank took 100% of the certificate value, using Royal Bank of Canada as the conduit for CLN I and ING Baring for CLN II. Ultimately, Citibank (retroactively) chose to consolidate the CLNs on Citigroup's balance sheet, but at that point such consolidation was of no consequence to Citigroup since the bond proceeds would exactly cancel out the loan to Enron.

Collateral for the full amount of the certificate was retained in the trust for Citibank (i.e., not used in the prepays). In the event of an Enron bankruptcy and the Citibank swap, there would be essentially no risk for Citibank to recover its certificate investment. Internal Citibank emails appear to discuss the implications of such a position and point out that the Offering Memorandum "makes clear" that the certificate is not a first loss position for the noteholders. Bates CITI-SPSI 0081540.

APPENDIX E

Summary of Enron "Prepays" with J.P. Morgan Chase and Citigroup

Prepay Transactions with Chase

US$ millions

Transaction Name	Issuance Date	Commodity	Chase Commitment	Amount	Final Maturity Date	Amount Outstanding at Bankruptcy*	
Chase I	Dec-92	Crude	$75.0	$75.0	Dec-94	$0.0	
Chase II	Jun-93	Crude	$230.0	$230.0	Dec-94	$0.0	
Chase III	Dec-94	Crude	$207.9	$207.9	Dec-00	$0.0	
Chase IV	Sep-95	Gas	$225.0	$225.0	Jun-04	$0.0	
Chase V	Dec-96	Gas/Crude	$350.0	$350.0	Jun-05	$0.0	
Chase VI	Dec-97	Gas	$300.0	$300.0	Nov-01	$6.0	
Chase VII	Jun-98	Gas	$250.0	$250.0	Jun-02	$48.5	
Chase VIII	Dec-98	Crude	$250.0	$250.0	Dec-02	$85.4	
Chase IX	Jun-99	Gas	$500.0	$500.0	Jun-04	$298.0	
Chase X	Jun-00	Gas	$650.0	$650.0	Jun-05	$519.6	
Chase Xi	Dec-00	Gas	$165.0	$330.0	Dec-05	$255.2	
Chase XII	Sep-01	Gas	$350.0	$350.0	Mar-02	$352.0	
			$3,552.9	$3,717.9		$1,564.7	**Totals**

Prepay Transactions with Citigroup

US$ millions

Transaction Name	Issuance Date	Commodity	Citigroup Commitment	Amount	Final Maturity Date	Amount Outstanding at Bankruptcy**	
Citibank Delta Energy 1994	Sep-94	Crude	$125.0	$125.0	Apr-96	$0.0	
Roosevelt (Natural Gas)	Dec-98	Gas	$310.0	$310.0	May-99	$0.0	Planned syndication not realized
Roosevelt (Crude Oil)	Dec-98	Crude	$190.0	$190.0	May-99	$0.0	
Roosevelt Extension	May-99	Crude	$125.0	$125.0	Dec-99	$0.0	
Truman	Jun-99	Crude	$250.0	$500.0	Jun-99	$0.0	Enron name: "Jethro"
Truman Extension	Sep-00	Crude	$337.5	$675.0	Nov-99	$0.0	Enron name: "Jethro Extension"
Yosemite I	Nov-99	Crude	$37.5	$800.0	Nov-04	$800.0	
Nixon	Dec-99	Crude	$104.0	$331.4	Apr-00	$0.0	Enron name: "Yosemite II Bridge"
Yosemite II	Feb-00	Crude	$16.0	$305.0	Feb-07	$305.0	
CLN I (Yosemite III)	Aug-00	Crude	$0.0	$500.0	Aug-05	$475.0	
Yosemite IV							
CLN II	May-01	Crude	$0.0	$500.0	May-06	$475.0	
Euro CLN	May-01	Crude	$0.0	$155.0	May-06	$155.0	
Sterling CLN	May-01	Crude	$0.0	$161.0	May-06	$161.0	
Citibank Natural Gas	Jun-01	Gas	$250.0	$250.0	Dec-01	$250.0	
			$1,745.0	$4,927.4		$2,621.0	**Totals**
			$5,297.9	$8,645.3		$4,185.7	**GRAND TOTALS**

**From letter from J.P. Morgan Chase Counsel pursuant to Subcommittee request. Amount for Chase XII submitted by Chase was $176,000,000.*

***From Credit Linked Notes Offering Memoranda and Citigroup due diligence for Dynegy merger, Bates CITI-SPSI 0033029*

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

THE GOVERNMENTAL AFFAIRS
PERMANENT SUBCOMMITTEE ON
INVESTIGATIONS

UNITED STATES SENATE

"THE ROLE OF THE FINANCIAL INSTITUTIONS IN ENRON'S COLLAPSE"

Tuesday, July 23, 2002

Dirksen Senate Office Building

Written Statement

Lynn Turner

Professor of Accounting and Director

Of The Center For Quality Financial Reporting

Colorado State University

Mr. Chairman, Ranking Member, Members of the Subcommittee, my name is Lynn Turner. As I believe you are aware, I served as the Chief Accountant of the Securities and Exchange Commission (SEC) from July of 1998 through August of 2001. I also served on the staff of the SEC from June of 1989 through July of 1991. Currently I am a professor of accounting and Director of The Center For Quality Financial Reporting at Colorado State University.

From June of 1996 to June of 1998, I was Vice President and Chief Financial Officer of Symbios, Inc., an international manufacturer of semiconductors and storage solution products. Prior to joining Symbios, I served as a partner at one of the then "Big Six" international accounting firms, Coopers & Lybrand (C&L). While at C&L, I served as an auditor and partner who reviewed SEC filings.

Restoring The Trust

Mr. Chairman, the capital markets in the United States are vitally important to the health of the U.S. economy. Maintaining the confidence and trust of the investing public in the integrity of the markets is critical to the ability of the markets to continue to attract capital. Capital that is invested by 85 million Americans. Capital that fuels the expansion of plants, creation of jobs and development of new technologies that has made our great country *the* leader in innovation.

Yet as recently as this past week, polls show many Americans have lost trust in Corporate America, the accounting profession, analysts, Wall Street firms and other market participants. The recent downward spiral of market indexes is a strong indicator that confidence in the markets has ebbed. That loss of confidence, if not stemmed, may well have a profound and lasting effect on this country, its economy and its citizens.

To restore the trust, all market participants must once again fulfill their roles in a responsible fashion. Corporate executives must make full and fair disclosure of their financial information, the corporate board must oversee the financial reporting process with the keen eye of an eagle, auditors must once again become unbiased and independent so as to ensure the numbers are accurate, and Wall Street must provide real due diligence on behalf of the markets and meaningful analysis to investors.

Those market participants who fail in their respective roles, and thereby aid and abet a fraud being perpetrated on thousands, if not millions of investing and hard working Americans should be dealt justice in a swift and appropriate manner.

The foundation of the markets rests on the integrity of the numbers reported to analysts, credit rating agencies and investors. Numbers that are necessary in assessing a company's financial health and prospects for the future.

When it comes to integrity and honesty in financial reporting, the buck starts and stops with the Chief Executive Officer (CEO) and Chief Financial Officer (CFO). But others also play a key role. For example, investment bankers and auditors will often

carry out due diligence, learning much about a company and its business. They also read the filings made by public companies. It is important that the corporate executives, auditors and investment bankers ensure that the financial statements and other disclosures included in offering documents, include ***all*** the material information that those market participants would want if they were investing in the company themselves. Unfortunately, I have seen all too often where that has not occurred. Enron only confirms that concern for millions of investors.

Enron has raised many issues, questions and doubts in the minds of the public. One issue in particular those members of this committee are to be commended for addressing today, is: what role was played in Enron's demise by the various financial institutions that helped finance or raise capital for its operations? Did these institutions have knowledge of information that could have been a red flag to investors, analysts or the credit rating agencies, if properly disclosed? Was there information available that if made transparent would have warned investors an iceberg was lurking ahead that would inevitably sink the ship? Did the institutions assist or otherwise aid and participate in the structuring and execution of transactions for the purpose of reducing the transparency of disclosures to investors?

Determining the Proper Accounting

I would like to focus in particular on the accounting for a series of transactions I will call the Mahonia and Delta transactions. But before I delve deeper into these, allow me to outline some basic accounting ground rules that, I hope, will better frame the issue.

The statutory responsibility for establishment of generally accepted accounting principles, or GAAP, resides with the SEC. However, since almost from the inception of the SEC, the Commission has looked to the private sector for the establishment of GAAP. As a result, GAAP has been promulgated by or under the oversight of the Financial Accounting Standards Board (FASB) or one of its predecessors.

However, businesses enter into billions of transactions. In the past couple of decades, the number of these transactions involving complex financial contracts and off-balance sheet transactions has increased exponentially. As a result, it is virtually impossible to write accounting standards for each particular type of transaction. Unfortunately, during the bull market of recent years, some companies with the assistance of their external auditors and investment bankers, have improperly taken advantage of this.

The FASB does have a task force, comprised of representatives from accounting firms and Corporate America, which establish accounting principles for emerging accounting issues. This is an effort to accomplish "real time" accounting standard setting. This task force is known as the Emerging Issues Task Force (EITF). A significant amount of its efforts since its inception in 1983 has been devoted to determining the accounting for transactions structured by Wall Street and the accounting firms. Many of these structured or engineered transactions are done to circumvent

existing accounting rules and reduce transparency through such ingenuity as off-balance sheet financings or avoiding classifying financings as debt as we have seen done by Enron.

I can't tell you Mr. Chairman, how often as an audit partner or the Chief Accountant as the SEC I heard the common refrain – "Where does it say in the accounting literature I can't do it." In fact, I recall on more than one occasion when investment bankers suggested an accounting treatment that I believed was absolutely and without a doubt, black and white, and wrong! Sometimes they would even show partners in my firm filings with the SEC that contained what we believed was improper accounting while at the same time saying since one Big Five firm accepted it, my firm was also obligated to agree to it. This type of behavior contributes to a lack of a "level playing field" for the majority of those in business who "do the right thing." It quickly degenerates into "lowest common denominator" financial reporting and disclosures.

When there is not an accounting standard written for a specific transaction entered into by an entity, the accountant and/or auditor often will look to accounting principles for similar types of transactions or economic events. In accounting, this is sometimes referred to as determining accounting principles by analogy.[1]

Financial executives and auditors must determine that the accounting principles selected by a company "present fairly" the financial condition, results of operations and cash flows, including operating cash flows, of the company. In making this determination, one has to consider whether the accounting principles selected have (a) general acceptance, (b) are appropriate in the circumstances, (c) the financial statements, including the related notes, are informative of matters that may affect their use, understanding and interpretation by users, and (d) that the numbers in the financial statements are properly classified (e.g., presented as a trading liability versus bank financing).[2]

It is important that numbers are properly classified in the financial statements. Classification of assets and liabilities into the appropriate line items and as short or long term in nature will provide investors, analysts and credit rating agencies with a transparent picture of the assets that will provide cash that can be used to extinguish liabilities, when those assets will give rise to cash and when there will be a demand for cash to pay off the debt. For example, trading companies may "match" their asset and liability positions and use the settlements of each to offset one another. However, bank loans cannot be repaid from offsetting positions and require the use of cash generated by

[1] See Securities and Exchange Commission Staff Accounting Bulletin (SAB) No. 99, *Materiality*, August 1999. SAB 99 states: "This SAB and the authoritative accounting literature cannot specifically address all of the novel and complex business transactions and events that may occur. Accordingly, registrants may account for, and make disclosures about, these transactions and events based on analogies to similar situations or other factors....The staff, therefore, encourages registrants and auditors to discuss on a timely basis with the staff proposed accounting treatments for, or disclosure about, transactions or events that are not specifically covered by the existing accounting literature."

[2] Statement on Auditing Standard (SAS) No. 69, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles*, Paragraph 4.

ongoing business operations. Accordingly, if bank loans are disguised as trading liabilities, investors and other users of the financial statements, such as credit rating agencies, can easily be misled as to the demands on cash and other liquid assets the company will incur, the timing of those demands, and pending shortages in liquidity. I strongly agree with the testimony of John Diaz of Moody's Investor Service that "If such transactions had been accounted for as a loan, Enron's operating cash flow would have been reduced and its debt would have been greater. The disclosure of these transactions as loans would have exerted downward pressure on Enron's credit rating."

Accounting For The Substance of A Transaction

The accounting profession's guidance notes that GAAP recognizes "the importance of reporting transactions and events in accordance with their substance....Because of the developments such as...the evolution of a new type of business transaction, there sometimes are no established accounting principles for reporting a specific transaction or event. In those instances, it might be possible to report the event or transaction on the basis of its substance by selecting an accounting principle that appears appropriate when applied in a manner similar to the application of an established principle to an analogous transaction or event."[3]

Consistent with the guidance in the professional literature, Judge Friendly ruled in U.S. of America versus Simon, United States Court of Appeals for the Second Court, that it was proper for Judge Mansfield to have directed the jury that mere adherence to GAAP was not sufficient. Mansfield stated "that the 'critical test' was whether the financial statements as a whole 'fairly presented the financial position of Continental...and whether it accurately reported the operations...Proof of compliance with generally accepted standards was 'evidence which may be very persuasive but not necessarily conclusive...that he acted in good faith, and that the facts as certified were not materially false or misleading.'" Judge Friendly went on to say that "Generally accepted accounting principles instruct an accountant what to do in the usual case where he has no reason to doubt that the affairs of the corporation are being honestly conducted. Once he has reason to believe that this basic assumption is false, an entirely different situation confronts him...At least this must be true when the dishonesty he has discovered is not some minor peccadillo but a diversion so large as to imperil if not destroy the very solvency of the enterprise."

The FASB has developed general broad principles contained in Statements of Financial Accounting Concepts (SFAC) that are useful in determining the appropriate accounting principles to be applied to a particular transaction. Often the staff of the SEC has referenced these concepts when asked by a public company or its auditor as to the staff's views on the proper accounting for a particular transaction. These concepts or principles provide an accountant and auditor with a framework for determining transparent accounting. [4] One of the concepts set forth is that the accounting principles

[3] Ibid Note 2.Paragraphs 6 and 9.

[4]Statement of Financial Accounting Concepts (SFAC) No. 2, *Qualitative Characteristics of Accounting Information*, states that the FASB conceptual framework "...is expected to serve the public interest by

selected for a transaction should faithfully represent the underlying "economic resources and obligations and the transactions and events that change those resources and obligations."[5]

Andersen set forth it views on accounting for prepay transactions in a memo dated June 1999.[6] In simple terms, the transaction described in the memo involves a public company (Enron), a special purpose entity (SPE – e.g., Mahonia and Delta) and a swap counter party (such as a financial institution). Enron receives a fixed payment from the SPE and agrees to sell a fixed amount of a commodity such as gas at a specified future dates. The SPE also enters into an agreement with the financial institution and receives a fixed payment amount which is used to fund the SPE's payment to Enron. In turn, the SPE enters into a swap agreement that will result in it making the same floating payments to the financial institution that it is receiving from Enron. Finally, Enron and the financial institution enter into an agreement whereby Enron will pay a fixed amount to the financial institution through periodic settlements (payments) and in turn receives floating payments in a swap, that are the same as those it will make to the SPE. In the case of Mahonia, the SPE also becomes the beneficiary of a surety bond from an insurance company.

Andersen appropriately referred to various analogous accounting literature in trying to determine the appropriate accounting for the prepay transaction. Andersen appropriately concluded that if there is linkage between the various contracts among the three parties, such as cross default provisions, then "all three transactions must be considered one and therefore be accounted for as a financing. EITF 88-18 provides guidance on whether certain factors of the transaction indicate debt or deferred revenue. We reviewed the factors indicating debt vs. deferred revenue and believe the transaction would meet several factors that would indicate debt if the contracts contained cross default provisions." Andersen's memo also goes on to note that the terms of the contracts should have basic criteria to avoid being treated as debt including the counterparties have price risks, each contract must be de-linked, and the contracts should be standard normal swaps.

In a separate Andersen document titled "Prepaid Transactions Discussions," Andersen states that for prepays to be treated as trading contracts they must meet four criteria. Those criteria are:

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providing structure and direction to financial accounting and reporting to facilitate the provision of evenhanded financial and related information that is useful in assisting capital and other markets to function efficiently in allocating scarce resources in the economy....Careful use of the concepts may also provide guidance in resolving new or emerging problems of financial accounting or reporting in the absence of applicable authoritative pronouncements."

[5] SFAC No. 5, Para. 63.

[6] Andersen memo to the files dated June 1999. Bates No. ECp000094306. The memo references Emerging Issues Task Force (EITF) Consensus 88-18, 90-15, 96-21, EITF Topic D-14 and a December 1997 Speech made the SEC staff at the Annual SEC Conference of the American Institute of Certified Public Accountants analyzing a similar type structure involving fixed payments and a total return swap. The transaction involved a financial institution, special purpose entity and company.

- None of the individual agreements are linked commercially or make reference to any of the other documents; in effect, each is a stand-alone, normally occurring derivative instrument which continues to be in effect even if other pieces of the transaction are terminated for any reason.

- The PGA (contract agreements) and each swap are settled at current market values, and the PFA includes provisions typical of trading instruments such as replacement cost provisions with monthly settlements

- Price risk related to the PGA is transferred from the gas supplier to the purchaser without the gas supplier further affecting the purchaser's management of this risk or the purchaser's other PGA-related economics, and

- The purchaser of the gas must have an ordinary business reason for purchasing the gas, not in-substance be an SPE established just to effect a secured investment in a debt instrument from a gas supplier.

In essence, Andersen established criteria to assess and determine if the Enron prepay transactions were with independent entities with economic substance, entering into substantive business contracts, or merely "sham" transactions without any business purpose other than to hide financings from the investor. If the transactions were sham transactions and financings, Enron would have been required to report and disclose the transactions in their financial statements as bank debt. They would also need to report the cash received from the financings, as well as the repayments, in the financing section of the statement of cash flows rather than as cash flows from operations. However, when Enron reported these contracts as trading activities and liabilities, they also reported the receipts of cash as if they were generated by normal business operations and as a component of operating cash flows. When a company improperly reports cash flows generated by or used in financings as cash generated from typical business operations that investors, analysts and credit rating agencies will be misled as to the financial health of a company and its ability to meet future commitments on cash. In developing the standard for how to report cash flows, the FASB specifically decided that for cash flow information to be useful and relevant to investors, cash flows from operations, investing activities and financing activities should be separately reported. To do otherwise violates GAAP and accordingly, the rules and regulations of the SEC.

I agree with the factors Andersen has used in determining whether the prepay transactions have real economic substance or are "sham" transactions structured to avoid treating prepays as financing transactions in the financial statements. Based on my experience as an audit partner, CFO and Chief Accountant of the SEC, I would also consider the following factors, some of which are encompassed within the Andersen factors:

- Does the transaction have a legitimate business purpose other than avoiding presenting the financing as bank debt on the balance sheet?

- Does the SPE engage in normal business operations? For example, does it undertake normal trading activities for the purpose of making normal trading profits? Does it assume the typical risks and rewards associated with a trading entity?

- Does the SPE have more than nominal capitalization? Where does the SPE receive its funding from? Apart from that source of cash, could it operate on its own and engage in the transactions? Does the SPE undertake trading activities with parties other than Enron and the Wall Street Bank? If not, why not? Who determines what transactions the SPE can and does enter into? Does the SPE have full control over the transactions and contracts it enters into, or by contract, does it give up some of its control to Enron or the Wall Street Bank?

- Does the SPE have officers and directors who function as they would in any normal trading company?

- Does the sponsor of the SPE or the entity it enters into transactions with have all the risks and rewards of the transactions or does the SPE have them? Is there any economic substance to the SPE or is it placed into the transaction merely as a third party to facilitate false and misleading financial reporting?

- Do the transactions between Enron, an SPE and the Wall Street Bank actually transfer economic risk from or to Enron, the SPE or bank? Are the transactions structured as a "round trip" whereby the cash flows and risks merely move in a circle and end up with the same party as they began with?

- Are the transactions linked in such a manner that risks or the ultimate obligations to repay financings are not really transferred? Are they linked in a manner such that they show lack of independence of one of the parties or any of the "legs" of the transactions?

- Are the forward sales contracts more like debt than a forward sale of a commodity or product? Do the terms of the contracts result in the parties earning trading profits for taking on trading risks or are the returns to the contract parties limited to an interest rate of return or limited in some other fashion?

- Are the contracts linked in such a fashion that Enron ultimately has the obligation to repay the funds used in the transaction? Does the Wall Street bank, via cross default provisions or other contract terms, such as termination arrangements, have the ability to obtain payments from Enron? If Enron goes into bankruptcy, can the Wall Street bank by contract or otherwise control the SPE in such a fashion it demands payments or assets from Enron?

- Does the SPE have the ability to make the payments if Enron does not? What is the continuing involvement of Enron in ensuring the Wall Street Bank is repaid?

Analogous Accounting Literature

In EITF Topic D-14, *Transactions involving Special-Purpose* Entities, the SEC staff stated it has "objected to a proposal in which the accounting for a transaction would change only because an SPE was placed between the two parties to the transaction. The SEC staff believes that insertion of a nominally capitalized SPE does not change the accounting for the transaction." EITF Issue 90-15, *Impact of Nonsubstantive Lessors, Residual Value Guarantees, and Other Provisions in Leasing Transactions*, addresses accounting for SPE's created to keep lease financings off the balance sheet. As a result of EITF Issue 90-15, the SEC staff sent a letter to the EITF and accounting profession that stated the "...equity investment should be comparable to that expected for a substantive business involved in similar leasing transactions with similar risks and rewards." EITF 90-15 also requires that if an SPE engages in activities only for a single company, where that company has the risks and rewards of the transaction as opposed to the SPE and the SPE has only nominal capital, the SPE will not be considered substantive and will have to be consolidated by the sponsoring company. EITF Issue 96-21, *Implementation Issues in Accounting for Leasing Transactions involving Special-Purpose Entities*, which provides further guidance on accounting for lease transactions involving SPE's, notes that cross-collateralization provisions that give two parties access to the same leased assets should be collapsed and assuming all other criteria are met, the lease is treated as financing on the balance sheet.

EITF 88-18 *Sales of Future Revenues* sets forth criteria for assessing when a forward sale is to be treated as debt. Some of the criteria include:

- Whether the enterprise (Enron) has significant continuing involvement in the generation of the cash flows due the investor (Wall Street Bank),
- Whether the investor's rate of return is implicitly or explicitly limited by the terms of the transaction, and
- The investor has recourse to the enterprise relating to the payments due the investor.

Andersen notes in their June 1999 memo that when cross defaults exist in transactions, the Enron prepays would be treated as debt on the balance sheet based on the criteria in EITF 88-18. I concur with Andersen's conclusion that prepays with cross defaults should be reported and disclosed in the balance sheet as loans from the lending financial institution.

EITF Issue 98-10, *Accounting for Contracts Involved in Energy Trading and Risk Management Activities*, sets forth a number of criteria for determining if an entity is in substance involved in energy trading activities. It states that energy trading contracts that are not derivatives should be reported in the balance sheet at their fair value. The 98-10 consensus established a framework for evaluating the treatment of energy-related contracts that assesses the facts and circumstances surrounding the various activities of an

entity rather than solely on the terms of the contract. It states: "Inherent in that framework is an evaluation of the entity's intent in entering into an energy contract."[7]

EITF Issue 98-15, *Structured Notes Acquired for a Specified Investment Strategy* addresses when should two separate structured note transactions should be collapsed and considered a single transaction for accounting purposes. The consensus lists factors such as the following that would lead to the conclusion that accounting treatment as a single combined transaction is appropriate:

- The two securities are issued contemporaneously and in contemplation of one another or are issued separately but the terms for their remaining lives result in off setting changes in fair value.

- The two securities are issued by the same counterparty and/or the same issuer (or issued by different issuers but structured through an intermediary).

- The two securities were purchased by the investor for the sole purpose of achieving a desired accounting result, and the transaction considered individually would serve no valid business purpose or would not be entered into otherwise.[8]

SEC Regulation S-X, Article 3A-02 states the Commission will look to factors other than just ownership in determining if an entity is independent or really under the control of another party. For example, an entity may appear independent because of separate ownership but still be controlled through a contract that stipulates what the entity can or cannot do.

The FASB has provided guidance on accounting for prepaid interest rate swaps in implementation guidance it has published on accounting for derivatives. In its Derivative Implementation Group Issue A9, the DIG states that the prepaid interest rate swaps in the described transactions would be reported at fair value as a derivative instrument in the balance sheet. However, underlying this conclusion is that the described transactions are not "sham" transactions but rather swaps with a legitimate business purpose between independent parties who have assumed the risks and rewards of their respective transactions.

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[7] EITF Issue No. 98-10, *Accounting for Contracts Involved in Energy Trading and Risk Management Activities*. Para. 8.

[8] Ibid, Para. 4. Derivatives Implementation Group (DIG) Issue K1 also discusses a situation where two or more transactions have been entered into in an attempt to circumvent the accounting literature for derivatives. The DIG issue states that "the following indicators should be considered in the aggregate and, if present, should cause the transactions to be viewed as a unit and not separately:

a. The transactions were entered into contemporaneously and in contemplation of one another.
b. The transactions were executed with the same counterparty (or structured through an intermediary).
c. There is no apparent economic need nor substantive business purpose for structuring the transactions separately that could *not* also have been accomplished in a single transaction."

Accounting for Mahonia and Delta Transactions

I have read the testimony of the subcommittee's chief investigator and various documents the staff of the subcommittee have provided to me. These documents lead to the conclusion that the Enron prepay transactions described therein should have been accounted for as bank or credit financings, rather than as liabilities from price risk management activities in the financial statements of Enron. The cash flows from these transactions should also have been reported in the financing section of the Enron statement of cash flows. Specific considerations set forth by the chief investigator that I agree support this conclusion include:

- Mahonia and Delta are nominally capitalized and lacking economic substance apart from the Enron transactions. Their purpose was not to engage in ongoing competitive trading operations as a trader but rather to facilitate less than transparent reporting by Enron.

- Mahonia and Delta lack price exposure and earning fixed fees rather than trading profits.

- Mahonia and Delta were established for the benefit of Chase and Citibank and only engaged in transactions with those respective banks. They did not engage in ongoing competitive trading activity with other independent financial institutions.

- The level of control over Mahonia and Delta exercised by Chase and Citibank, by contract or otherwise.

- The linkage of legal agreements among the involved parties.

- All three "independent" legs of the prepay transactions were contemplated and executed simultaneously.

- Deal terms that in form referenced commodities indexes were in substance calculated using borrowing rates.

I also share the concerns of the staff of the subcommittee on the Yosemite transaction. The role of the investment bankers in creating what appears to have been planned in advance as a unitary transaction, for the purpose of reducing Enron's transparency to investors and the investment bankers risk, should be the subject of investigations by both the SEC and the Department of Justice.

Lessons To Be Learned

There are important lessons that can and should be learned from the Enron Mahonia and Delta structured financings. First, GAAP must be considered a minimum reporting benchmark for financial statements and disclosures. Ultimately, the financial

statements and disclosures must fairly present in all material respects, the financial condition, cash flows and operations of the issuer.

Second, professionals within or external to a company that mislead auditors should be held accountable for false statements. All parties, including investment bankers, who aid and abet fraudulent reporting to investors should feel the sharp blade of the sword of justice.

Third, independent accountants should not help Wall Street facilitate the structuring of transactions so as to reduce the transparency of financial reports. Twice during my term as chief accountant I requested the accounting profession to cease their participation in this process. My successor has also requested auditors reduce their involvement with Wall Street in this dubious process. Despite these requests, the profession has not acted in a timely and responsible fashion, instead choosing to continue to generate fees at the expense of investors. This behavior is simply at odds with the purpose of the public franchise Congress granted the accounting profession by government mandate in 1933.

The role Wall Street has played in structuring and executing transactions to reduce transparency to investors, in exchange for fees that may run into tens of millions, is also inconsistent with honest due diligence and integrity in the market place. If Wall Street was serious about reforms, they would stop providing this service and start serving investors. Wall Street needs to remember that the U.S. capital markets cannot, and will not, effectively function if investors believe that investment bankers have "rigged the tables." Today, too many investors are concerned they are playing with a "stacked deck."

Fourth, there needs to be greater enforcement of existing accounting rules. In Enron, the existing accounting rules were not complied with and as a result, the financial statements provided to investors were materially misleading. However, to accomplish increased enforcement by the SEC and the Justice Department, these agencies will need to be provided with significantly increased funding and resources.

Some have argued that the solution to a lack of compliance with today's accounting rules is to adopt "principled based" rules. However, the predecessor the FASB, the Accounting Principles Board developed several principles based rules during its existence from 1958 to 1973. However, this did not stem a stream of false and misleading financial statements and disclosures that emerged during the 1972-73 bear market. Then as now, the number one issue was a lack of compliance with existing accounting rules. As we saw at the SEC, the principles based approach to rules in foreign countries often did not result in transparent reporting or better compliance with the rules. In fact today, the FASB's conceptual framework provides a substantial "principal based approach" that all too often is ignored by preparers of financial statements.

Fifth, the existing accounting rules for special purpose entities and off-balance sheet transactions should be improved. While the FASB has recently issued an exposure draft of a new standard, I am concerned that it will not result in a company reflecting all

the debt on its balance sheet that will require the use of the company's assets or resources to pay off. The change in the proposed standard to a rebuttable presumption that there must be not less than 10% equity in the SPE will not result in all public companies which continue to have the risks associated with off balance sheet financings, reporting all of those financings on their balance sheets.

Closing

Let me close by pointing out that the solutions for fixing the systemic problems we have learned from the Enron experience, are included in the Sarbanes bill. Its prohibition on auditors providing certain services to companies they audit, will stop the auditors from participating in reducing the transparency of disclosures to investors. It clearly establishes a new standard consistent with Judge Friendly's decision of over thirty years ago that all financial statements and disclosures, regardless of GAAP, must fairly present the true economic health of a company. It mandates that new disclosure standards be adopted for off-balance sheet transactions and will study whether the proposed FASB rule for SPE's will get the job done. The Sarbanes bill provides long overdue and much needed resources to the SEC. Finally, for those scoundrels in corporate America who have painted the many ethical and upstanding American businessmen with a tarred image, it will put them where they belong: Behind bars.

The 97 members of the U.S. Senate who voted for the Sarbanes bill should be loudly applauded by their constituents and investors for supporting this important piece of legislation. I believe if it is passed by Congress without weakening any of its provisions, it will once again restore the trust and confidence investors have had in the U.S. capital markets. For that I say thank you all.

Testimony of John C. Diaz
Managing Director
Power & Energy Group
Moody's Investors Service

and

Pamela M. Stumpp
Managing Director
Chief Credit Officer
Corporate Finance Group
Moody's Investors Service

Before the
Permanent Subcommittee on Investigations
Committee on Governmental Affairs
United States Senate

July 23, 2002

Good morning Mr. Chairman, Senator Collins and members of the Subcommittee. My name is Pamela Stumpp, and I am a Managing Director at Moody's Investors Service and the Chief Credit Officer for the Corporate Finance Group. I am joined by my colleague John Diaz, a Managing Director in our Power & Energy Group. On behalf of Moody's, we are pleased to appear before you today at your request regarding your investigation into the role of financial institutions in the collapse of Enron.

For over one hundred years, Moody's has played an important part in providing informed and independent credit analysis to investors. We are proud of our history as the world's oldest credit rating agency and are cognizant of the responsibility that this legacy confers upon us. It was with this responsibility in mind that we accepted your invitation to share our views on the critical issues before you. At a time when America's faith in the integrity of its corporations and the stability of its financial markets is badly shaken, we applaud the efforts of this Subcommittee, the Congress and the Securities and Exchange Commission to investigate Enron's failure and identify the larger lessons that can be learned from the company's collapse.

We are especially interested in these issues because our rating decisions depend heavily on the integrity of the public financial statements provided by corporations. In our assessment of a company's creditworthiness, Moody's analysts begin with the premise that the issuer's SEC filings and audited financial statements are accurate. We then bring the benefit of our experience and expertise to our analysis. But as the Enron situation has demonstrated, where the principle

of transparent public disclosure is abandoned, neither we nor the regulators can properly fulfill our obligations to the market and investors globally.

Before discussing Enron and related issues in more detail, it is important for me to note that Moody's did not have any knowledge, prior to Enron's bankruptcy, of the existence of Enron's prepaid forward and related swap transactions. Even today, our understanding of the specifics of these transactions is restricted to what we have gleaned from press accounts and the conversations we have had with the Subcommittee staff at their request. Based on our limited knowledge, these transactions appear to have been a form of borrowing. If such transactions had been accounted for as a loan, Enron's operating cash flow would have been reduced and its debt would have been greater. The disclosure of these transactions as loans would have exerted downward pressure on Enron's credit rating.

Of course, knowing all that we know today about the true nature of Enron's corporate enterprise, it is clear that Enron had not been an investment-grade company for several years. The compounded impact of these transactions alone on Enron's financial framework may have resulted in a lower rating and perhaps an earlier downgrade to below investment-grade status. More fundamentally, however, Moody's would have questioned management's motivations to implement such a structure.

As Moody's does with all corporate entities, we expressed to Enron our views regarding its creditworthiness. Specifically, Enron was rated in the Baa category, Moody's lowest investment grade level. Entities rated Baa contain speculative elements.[1] We had communicated to Enron that its Baa rating reflected its high level of debt relative to its operating cash flow. Consistent with Moody's practice not to recommend that corporate issuers follow specific courses of action, Moody's did not instruct or suggest that Enron employ prepaid transactions or other artificial means to increase operating cash flow or to understate debt levels.

Moody's did provide ratings for the notes issued by the Citibank-sponsored Yosemite Trusts I and II, as well as the several Enron Credit Linked Notes Trusts. We viewed these transactions to be a means through which Citibank reduced its level of Enron risk. We have submitted, along with this opening statement, a diagram of the Yosemite structure as presented to us in the Offering Memorandum. Yosemite was a structure of the type that our Structured Finance Group examines and rates frequently. The purpose of these structures is essentially to transfer the credit risks associated with a particular company to third-party noteholders.

In this instance, a trust was created that issued notes to investors. Citibank was obligated to make payments to the trust, which were then passed to the investors. Citibank was not obligated to make these payments if Enron failed to pay on its senior obligations or filed

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[1] Baa obligations are considered as medium-grade obligations (i.e., they are neither highly protected nor poorly secured). Interest payments and principal security for such obligations appear adequate for the present but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such bonds lack outstanding investment characteristics and in fact have speculative characteristics as well.

bankruptcy. In exchange for principal and interest due under the notes, the investors assumed the risk that Enron might go into bankruptcy or fail to pay on its obligations. Therefore, the likelihood that the noteholders would receive the promised returns on these notes was linked directly to Enron's creditworthiness.

It should be stressed that structured financing is a common risk management tool available globally to corporations, financial institutions, and state and local governments. It is a recognized method, for example, of enhancing liquidity and of transferring credit risk when appropriately implemented. What may seem to be a complex structure can in fact genuinely accomplish one or both of these goals. The Yosemite transactions transferred Enron risk exactly as they were intended to do. The problem was that the actual Enron risk was different from that portrayed by Enron's incomplete and misleading financial disclosures.

The securities market can only function efficiently with transparent and credible financial information. It is critical to strengthen those elements of our financial infrastructure and bolster investor confidence. As a major consumer of publicly available information, we support rule changes by the SEC and Congress that enforce transparency and penalize corporate deception. Further, we endorse a principle-based approach to accounting, rather than a rules-based approach. Accounting that promotes adherence to the spirit and the letter of the rules would strengthen the foundations of our financial system.

At this critical juncture, we hope all market participants step forward to offer confidence-building measures. As far as Moody's is concerned, we are expanding our knowledge in key disciplines that have come to influence credit risk. We are recruiting specialist teams with particular expertise in credit-related areas such as accounting quality, corporate governance and off-balance sheet risks. These teams will supplement the work of our credit generalists in their analysis of a company's creditworthiness. We hope that our independent assessment of financial reporting and corporate governance will improve market transparency and contribute to the restoration of confidence in our capital markets.

Finally, as an institution that views its role in the capital markets with both pride and great seriousness, we welcome the opportunity to assist this Subcommittee in examining the shortcomings of the present system and in working toward effective solutions. Therefore, on behalf of our colleagues at Moody's, John Diaz and I would like to thank you for the opportunity to appear today, and look forward to answering your questions.

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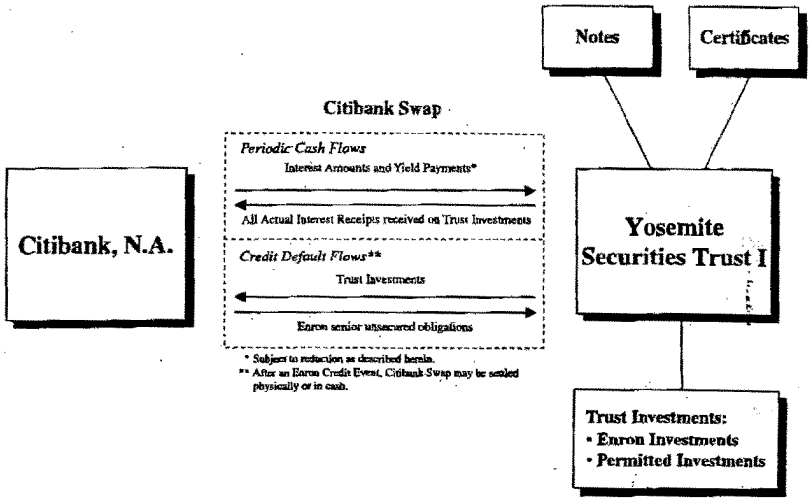
Diagram of the Transaction

The following diagram illustrates the structure of the transaction described in this Memorandum. The diagram does not purport to be complete and is qualified in its entirety by, and should be reviewed in conjunction with, the more detailed information included elsewhere in this Memorandum and the Transaction Documents described herein.



TESTIMONY OF RONALD M. BARONE

MANAGING DIRECTOR, STANDARD & POOR'S RATINGS SERVICES

BEFORE THE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

COMMITTEE ON GOVERNMENT AFFAIRS

UNITED STATES SENATE

JULY 23, 2002

Good morning, Mr. Chairman and members of the Subcommittee. I am Ronald M. Barone, a managing director in the Corporate and Government Ratings Group of Standard & Poor's Ratings Services. From 1994 until Enron Corporation's bankruptcy in December 2001, one of my roles at Standard & Poor's was to serve as a corporate analyst with respect to Enron. I was the primary Enron analyst from mid-1996 until early 2000 and then became and have remained the manager of Standard & Poor's ratings work for Enron.

I am joined today by Nik Khakee, a Director in Standard & Poor's Structured Finance Group. Mr. Khakee serves as Global Co-Head of Derivative Ratings. Mr. Khakee is Standard & Poor's senior analyst regarding credit derivatives-based Structured Finance transactions and was the senior analyst involved with our work on the Yosemite and Credit Linked Notes Trusts. The comments I will make a little later regarding those trusts were prepared by Mr. Khakee.

On behalf of Standard & Poor's, we welcome the opportunity to appear at this hearing. Standard & Poor's shares the Subcommittee's urgent sense of the need to investigate all the circumstances relating to Enron's collapse and its impact on the financial markets to prevent future harm to employees, shareholders, investors and the financial marketplace itself of the sort that has already occurred here. Before turning to the specific issues which the Chairman has asked us to address, I would like to take a moment and provide some background on Standard & Poor's and credit ratings in general.

Background on Standard & Poor's and the Nature of Credit Ratings

Standard & Poor's began its credit rating activities 85 years ago with the issuance of credit ratings on corporate and governmental debt issues and today is a global leader in the field of credit ratings and risk analysis. Standard & Poor's is — and has always been — independent of any investment banking firm, bank or similar organization. Since 1916, Standard & Poor's has rated hundreds of thousands of issues of corporate, government and structured financed securities through periods of economic growth and recession. Standard & Poor's also assesses the credit quality of, and assigns credit ratings to, managed funds and the ability of insurance companies to pay claims.

Ratings are a key component of the capital markets, which have functioned effectively for decades in the United States, and which are growing and flourishing in many

countries abroad. Investors throughout the world look to Standard & Poor's ratings to help in their understanding of credit risks. While all parties may not agree with our ratings at all times — they are, after all, *opinions* about an issuer's creditworthiness at a particular moment in time — Standard & Poor's credit ratings have gained respect and authority throughout the investment community because they are widely understood to be based on independent, objective and credible analysis. Standard & Poor's rates more than 99.2% of the debt obligations and preferred stock issues publicly traded in the United States, and our ratings are generally regarded as a global benchmark for assessing these issues.

I want to say a few words about what a rating is and what it is not. When Standard & Poor's issues a rating, we are offering our own opinion about a company's medium- to long-term credit risk. Similarly, ratings on particular instruments, such as the notes related to the structured finance transactions that I will discuss in a few moments, reflect our opinion about the likelihood of default on those instruments. In determining all of our ratings, we try to take into account whatever relevant future events may be anticipated. Because events always occur which are unforeseeable or simply unknowable, we regularly review our analysis.

Standard & Poor's does not perform an audit of the issuer, does not guaranty an issuer's payment on its debt, or provide insurance in case the issuer does not pay the debt. A Standard & Poor's rating does not constitute a recommendation to purchase, sell, or hold a

particular security. Nor does a Standard & Poor's rating speak to the suitability of an investment for particular investors. Rather, a rating reflects our opinion as of a specific date of the creditworthiness of a particular company or security based on our objective and independent analysis. Because ratings concerning creditworthiness are not investment advice or recommendations, they are fundamentally different from recommendations made by equity analysts as to whether investors should "Buy," "Sell," or "Hold" a security. Standard & Poor's also does not issue credit ratings on an issuer's common stock.

When we provide a rating of "A," "BBB" or "C," we are encapsulating our opinion into a letter or series of letters, which may be accompanied by a plus or minus. Our credit ratings also generally include more information about the rationale for the rating and our outlook as to the long-term credit quality. Long-term credit ratings are divided into several categories ranging from "AAA," reflecting the strongest credit quality, to "D," reflecting default. Ratings from "AA" to "CCC" may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories, although the categories themselves remain the prime component of the rating. Ratings in the "BBB" category or higher are considered by the market to be "investment grade," a term first used by regulators to denote obligations eligible for investment by institutions such as banks, insurance companies, and savings and loan associations. The term has gained widespread use over time in the investment community.

In addition to issuing letter ratings, Standard & Poor's also uses other well-known and understood indicators and signals to alert the marketplace to noteworthy aspects of our ratings. A rating, for example, can appear on "CreditWatch" signaling the strong possibility of a rating change. CreditWatch actions are normally taken in response to specific events or sudden changes in circumstances that have a high potential to affect creditworthiness. However, not all rating changes are necessarily preceded by a "CreditWatch" listing because circumstances may call for an immediate rating change. Additional informational tools useful to investors are Standard & Poor's "Outlooks" which offer long-term (one-to-three-year) perspective on credit quality. Outlooks are assigned to all long-term issues.

Standard & Poor's Commitment to Objectivity

Standard & Poor's objectivity is a key component to the credibility of our ratings in the marketplace. In order to ensure maximum objectivity, fairness and in-depth analysis, ratings are assigned by a committee, not by any individual. Moreover, no portion of an analyst's compensation is dependent on or connected with the performance of the companies that analyst rates or the amount of fees paid by that company to Standard & Poor's. The record bears out Standard & Poor's emphasis on objectivity and credibility. There is an exceptionally strong correlation, which has existed for decades, between the ratings initially assigned by Standard & Poor's and the eventual default record: the higher the initial rating,

the lower the probability of default and vice versa. The information below shows cumulative default history over the past fifteen years of issuers rated by Standard & Poor's based upon the rating category they were initially assigned. This clearly demonstrates the very low probability of default of an issue initially rated in the "AAA" category (only 0.52% have defaulted in the past fifteen years) contrasted with the much greater possibility of default for an issuer initially receiving our lowest rating level of "CCC" (54.38% have defaulted in the past fifteen years):

Rating Category	Percentage of Defaults Initially Rated in the Category
AAA	0.52
AA	1.31
A	2.32
BBB	6.64
BB	19.52
B	35.76
CCC	54.38

Our ratings opinions are based on public information provided by the issuer, audited financial information, and qualitative analysis of a company and its industry sector. We also may have access to certain confidential information of the issuer but only to the extent that the company's management lives up to its obligation to provide complete, timely and reliable information. We use that information and rely upon it. We tell the issuers we rate that we rely upon them to provide complete, timely and reliable information —

information that includes, but is by no means limited to, the company's financial information. As we told Enron (and, indeed, every other company Standard & Poor's rates): "Standard & Poor's relies on the issuer and its counsel, accountants, and other experts for the accuracy and completeness of the information submitted in connection with the rating process."

As mentioned earlier, we are not auditors, we do not audit the auditors of the companies that we rate or repeat the auditors' accounting work, and we have no subpoena power to obtain information that a company is unwilling to provide. We expressly rely on the companies we rate not only for current and timely information at the time of the initial rating but on an ongoing basis for the proper conduct of surveillance of the company's creditworthiness. This ongoing obligation includes providing on a timely basis all material changes to information the company has previously provided to Standard & Poor's. Indeed, our entire business as well as the United States financial system is based on the principle of full and fair disclosure.

Standard & Poor's Rating of Enron Corporation

With regard to Enron Corporation, from December 1995 until November 1, 2001, Standard & Poor's rating of Enron was BBB+, which we define as adequate ability to repay debt, but subject to worsening economic conditions. This was by no means the greatest vote of confidence a Standard & Poor's rating can bestow. It placed Enron at the lower levels

of investment grade ratings and was well below what Enron repeatedly — and unsuccessfully — sought from Standard & Poor's. It was also well below how Enron was often treated when it borrowed money from the market.[1]

Standard & Poor's rating of Enron in the BBB category was calculated and monitored on an ongoing basis through a thorough analysis of, among other materials, Enron's reported and audited financial statements including, in particular, its cash flow, debt burden, and other key financial metrics relevant to our opinion concerning Enron's creditworthiness. Standard & Poor's also employed a capital adequacy and liquidity review as Enron's businesses focused more on energy trading and marketing. Standard & Poor's also took into account Enron's emphatic and repeated representations, both publicly and to Standard & Poor's, about its strong corporate commitment to maintain its creditworthiness. Over the years, Enron made such representations during personal visits to our offices by the company's CFO's (including Mr. Andrew Fastow) and, in at least one instance, an October 2001 personal telephone call to me from its Chairman, Mr. Kenneth Lay, who explicitly stated that maintaining Enron's creditworthiness was a top corporate priority.

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1 Enron often borrowed from banks, investors, pension funds, etc. at lower interest rates than those usually charged to companies rated BBB+.

As I have said, at the heart of the process which leads to a rating being issued by Standard & Poor's is an unambiguous understanding between the company seeking the rating and Standard & Poor's itself: The company is obliged to furnish complete, timely and reliable information to Standard & Poor's on an ongoing basis and we, in turn, use that and other information to assess the creditworthiness of the company and then offer our opinion as to that creditworthiness in the form of a rating. It now appears that with respect to several material items, Enron did not keep its part of this well understood bargain.

As has been well-publicized, Enron hid from public view the true nature of many of its dealings with its off-balance sheet partnerships and thus its true financial picture. This concealment extended to Standard & Poor's as well. More particularly, on February 1, 2002, The Special Investigative Committee of the Board of Directors of Enron Corp., chaired by William C. Powers, Jr., issued its report regarding Enron's deceptive practices and concealment related to certain off-balance sheet partnerships and special purpose entities ("SPEs"). The Powers Report focused on four entities: Chewco, LJM1, LJM2, and the Raptor entities. None of these was adequately described in any of the company's publicly reported financial statements, if at all.[2] Nor did Enron provide information — complete or

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2 As the Powers Report observes, Enron's financial statements did mention the existence of some of these partnerships. "However, these disclosures were obtuse, did

Footnote continued on next page.

otherwise — about their nature to Standard & Poor's separately. In fact, in a series of presentations, Enron failed to mention these entities despite explicitly assuring us that it was providing a "kitchen sink" analysis of its affiliated off-balance sheet entities. We have previously provided the Subcommittee's staff with copies of two of these presentations.

In addition to the direct misrepresentations made to the marketplace and Standard & Poor's by Enron's management, other entities apparently played a role in misleading investors about Enron's true financial situation. Earlier this month, this Subcommittee published its report entitled, "The Role of the Board of Directors in Enron's Collapse," in which the Subcommittee concluded that there was a fiduciary failure by Enron's Board in allowing, among other things, the company to engage in "high risk accounting, inappropriate conflict of interest transactions, extensive undisclosed off the books activities, and excessive executive compensation." (July 8, 2002 Report at 3). Similarly, numerous press reports, as well as the Powers Report, have concluded that Enron's accountants, Arthur Andersen, bore significant culpability for Enron's troublesome practices and inadequate disclosures.

Footnote continued from previous page.

> not communicate the essence of the transactions completely or clearly, and failed to convey the substance of what was going on between Enron and the partnerships."

Footnote continued on next page.

Enron's Use of Prepaid Forward Transactions and Swap Transactions

It now appears, based upon press reports and other sources of information, that Enron may have also incurred approximately $4 billion in debt-like obligations structured as prepaid forward transactions and swap transactions. Our contemporaneous understanding of these types of transactions was that, in the years leading up to its bankruptcy, Enron was engaged in prepaid forward transactions to actively manage its trading and marketing positions and cash flow. Based upon discussions with Enron, we understood these transactions to be part of Enron's Price Risk Management ("PRM") account. Moreover, according to these discussions, Enron's PRM accounts were by and large in balance, lending support to our assessment that these transactions were indeed being executed in accordance with Enron's stated purpose.

In determining how to treat forward prepaid transactions for purposes of ratings analysis, Standard & Poor's looks at a variety of factors and performs both quantitative and qualitative evaluations. For example, funds from a set of prepaid transactions may be treated as operational cash flow if it appears that the issuer, as part of a stated pre-defined

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(Powers Report at 17). See also Powers Report at 200-03.

strategy, is engaging in such transactions so as to smooth out cash flow or earnings and that the transactions can and likely will occur on a regular and consistent basis. Such treatment would also require a demonstration by the issuer of the resources necessary to deliver on the forward prepaid contracts in an on-going manner. On the other hand, if our analysis reveals that these transactions are more of a singular nature aimed at raising funds for the issuer in lieu of or in addition to other financing, then we will often factor the amounts in as alternative financing and adjust our analysis accordingly. While Enron did not provide specific details about particular transactions, it did provide us with a general understanding of its use of such prepaid transactions and other monetizations. This information, coupled with our analysis, led us to conclude that Enron was utilizing such transactions on a consistent basis for strategic reasons. Accordingly, we considered the funds from these transactions to be more akin to operational cash flow.

Enron did not, despite our repeated requests for complete, timely and reliable information, disclose any information revealing a link between the prepaid forward transactions and the swap transactions. Similarly, Enron provided no indication that these transactions were in any way related to any of the Yosemite or Credit Linked Notes transactions despite an explicit inquiry by Standard & Poor's regarding the effect, if any, of these structured finance transactions on Enron's financial situation. While our knowledge about the full nature of these transactions and/or any links between them is still limited, any

lack of disclosure by Enron of their material aspects would have been yet another flagrant violation of Enron's duty and responsibility to provide Standard & Poor's with complete, timely and reliable financial information.

If such links did, in fact, exist and Enron's use of prepaid forward transactions and swap transactions were, in reality, an alternate form of financing giving rise to debt-like obligations, such information would have likely had a material impact on our ratings analysis of Enron. While in hindsight, and without full information, it is difficult to assess the degree of that impact, the effect on Enron's rating of approximately $4 billion in additional debt-like obligations would have, in all likelihood, significantly altered Standard & Poor's analysis of Enron's creditworthiness.

The revelation of the debt-like nature of these transactions would also have had a substantial effect on our qualitative analysis of Enron's creditworthiness. The very foundation of Standard & Poor's opinion on Enron's credit quality over the years leading up to its bankruptcy rested on the previously high regard that our analysts had for the company's risk management oversight and controls. The revelation that Enron may have been significantly more leveraged than previously represented to us and was possibly far more lax about its risk management controls than it led us to believe would have directly undermined this fundamental predicate of our ratings analysis.

Moreover, had they been revealed, any clandestine dealings and obfuscatory disclosure practices conducted by Enron's management would necessarily have cast long shadows on the validity of Enron's credibility in general and its financial reporting in particular. While it is difficult to say with certainty all the steps we would have taken had we known this potentially material information, Standard & Poor's does have a policy of not issuing ratings at all or withdrawing ratings when we conclude that we do not have enough information to form a clear and accurate opinion of the issuer's creditworthiness. The recent revelations about Enron certainly indicate that Enron materially failed to provide Standard & Poor's with the information necessary to form a true and accurate rating opinion.

It is worth noting as well that on no occasion did we advise, consult or suggest to Enron that it should employ these prepaid forward transactions and/or swap transactions, or any other means, to increase cash flow. As discussed above, the credibility of Standard & Poor's ratings in the marketplace is dependent on our ability to maintain objectivity. Therefore, Standard & Poor's does not advise or consult with any issuer as to how the issuer should conduct its business or present its financial information, and we certainly did not do so with Enron.

The Yosemite and Credit Linked Notes Trusts

The Subcommittee's Chairman, Senator Levin, has also requested information regarding our understanding of the structure and operations of the Yosemite and Credit Linked Notes trusts. Between November 1999 and May 2001, Standard & Poor's rated notes issued by the following Enron-related trusts: Yosemite Securities Trust I (November 1999), Yosemite Securities Co. Ltd. (February 2000), Enron Credit Linked Notes Trust (August 2000), Enron Credit Linked Notes Trust II (May 2001), Enron Euro Credit Linked Notes Trust (May 2001), and Enron Sterling Credit Linked Notes Trust (May 2001).

Each of these trusts possessed a standard credit linked notes structure in which the credit risk of a particular entity (the "Reference Entity"), which in these trusts was Enron, is transferred to the purchasers of notes issued by the trusts. In such transactions, a counterparty seeks to purchase protection against the default of a particular issuer. This protection can be most simply thought of as default insurance. This type of credit derivative is also most commonly thought of as a default or credit put option in which the holder of the put option holds the right to transfer obligations of the Reference Entity to the credit derivative protection seller in exchange for either money or other value. These transactions, like many other structured finance transactions, have been employed with frequency and with demonstrable utility over recent years. They provide sophisticated solutions to frequently

complex financial challenges and they have often provided significant benefit to the marketplace.

More specifically, in the first Yosemite transaction, for example, the protection buyer was Citibank. The protection bought was insurance against the possibility of a default by Enron and certain losses that might arise from such a default to Citibank. By entering into a credit default swap and thus purchasing a default put option, Citibank was able to hedge itself because the protection seller (the trust) was obligated to pay monies or transfer value to Citibank upon Enron's default.

The protection seller, which in the first Yosemite transaction was named Yosemite Securities Trust I, collects a fixed periodic payment, akin to an insurance premium from Citibank, as compensation for the possibility that it will have to perform, i.e., send money to Citibank, if the named Reference Entity, in this instance Enron, defaults. The protection seller obtains the funds needed to perform on such an obligation by selling notes and certificates to qualified institutional buyers. Thus, for example, when Yosemite Securities Trust I issued $750 million of rated notes, it received, as cash, that same amount of money to invest in eligible investments and to satisfy its obligations to Citibank in the event of an Enron default. In order to meet Standard & Poor's criteria, the investments made by the trust must qualify as eligible investments, which in the case of Yosemite I meant they had various maturity and credit restrictions. The most material of these credit restrictions limited eligible

investments to one of the following: securities rated AA- or higher or "Enron Investments." Enron Investments are obligations or participations supported, in whole or in part, directly or indirectly by Enron itself.

Our ratings analysis on the notes issued by these trusts requires us only to focus on the structure of the transactions and whether the default risk of the trusts' notes was a genuine pass through of the default risk of Enron. That analysis did not and does not include review of the day-to-day operations of the trusts after the closing of the transactions. As with all such transactions, it was and is the trustees' responsibility to ensure that the proceeds of the notes were invested in accordance with the terms of the indentures and that all of the trusts' operating requirements were met. Standard & Poor's is not a party to the transactions and, as such, does not interact with the trustees beyond being notified of credit events or material action being taken by the trustees that could affect our ratings. We also may interact with the trustees when we take ratings actions on the trusts.

I have included with this testimony a published research report from October 9, 2000 entitled, "New Issue: Enron Credit Linked Notes Trust." This report further explains our understanding and ratings analysis of these trusts.

Current Accounting Trends and Possible Changes Towards Greater Corporate Transparency

Clearly the collapse of Enron has been a terrible tragedy for its employees, shareholders, investors and business partners. Enron's demise, along with other recently revealed corporate accounting problems, has also damaged the public's confidence in the marketplace and economy as a whole. It has caused many to question the effectiveness of several long-standing and effective components of America's capital markets, most of which have functioned effectively for decades. At Standard & Poor's, we feel it is vital that these events be viewed as an opportunity to consider improvements that can be made to the system, weighing such improvements against the enormous benefits witnessed as the capital markets have grown in size and scope.

Because our ratings ultimately depend upon information provided by the issuer, Standard & Poor's has been a long-time champion of complete, timely and reliable disclosure of financial information and the best means of corporate governance. Standard & Poor's has supported, and will continue to support, any regulatory efforts aimed at enhancing these goals. The lessons from recent events, including the collapse of Enron, only underscore the need for such increased corporate transparency.

To that end, while we applaud the recent proposals and recommendations made by the Securities and Exchange Commission, Standard & Poor's has already stated publicly our belief that such proposals are only a partial solution as they still leave wide room for interpretation by companies and their accountants about whether certain items qualify for additional disclosure. Included with this statement are two articles published earlier this month on our website (www.standardandpoors.com) which address these topics. These articles, respectively, are entitled " Accounting Abuses and Proposed Countermeasures" (dated July 2, 2002) and "Enhancing Financial Transparency: The View from Standard & Poor's" (dated July 2, 2002). These articles focus on the various proposals and practices in light of Standard & Poor's ratings practices. We are also currently in the process of reviewing current accounting and regulatory requirements with an eye towards making specific recommendations for improvements aimed at fostering greater corporate transparency and restoring public confidence in the markets.

Thank you.

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Return to Regular Format

Research:

New Issue: Enron Credit Linked Notes Trust

$500 million Enron credit linked notes

Publication date: 09-Oct-2000

Analyst: Terry McCarthy, New York (1) 212-438-2680; Nadine E Gunter, New York (1) 212-438-2475; Marc Daly, New York

Ratings Detail

Profile

New Rating

BBB+

Closing date:Aug. 25, 2000

Transaction Summary

Collateral: Trust investments, a swap agreement between Enron Credit Linked Notes Trust and Citibank N.A., and all swap payments received, including obligations of Enron Corp.

Interest payments: Feb. 15 and Aug. 15 each year, beginning Feb. 15, 2001.

Principal payment: On the maturity date of the notes, Aug. 15, 2005.

Swap counterparty: Citibank N.A. New York, NY.

Arranger: Salomon Smith Barney Inc.

Depositor: Citibank N.A. New York, NY.

Collateral agent: U.S. Trust Co. of New York.

Securities intermediary: U.S. Trust Co. of New York.

Indenture trustee: U.S. Trust Co. of New York.

Trustee: Wilmington Trust Co.

Rationale

The rating assigned to the 8.00% Enron credit linked notes issued by Enron Credit Linked Notes Trust reflects a weak link approach based on the ratings of the trust investments ('AA-'), Enron Corp. (Enron) ('BBB+'), and the swap counterparty, Citibank N.A. ('AA-').

Transaction Overview

Enron Credit Linked Notes Trust, a Delaware statutory business trust, has issued notes and certificates. The initial principal amount of the notes and certificates are $500 million and $50 million, respectively. The certificates represent the beneficial ownership interests of the trust, and the certificate holders are subordinate in payment rights to the noteholders. The trust will use the proceeds from the sale of the notes and certificates to purchase trust investments that mature no later than the maturity date of the notes.

The assets of the trust primarily consist of trust investments (rated at least 'AA-' by Standard & Poor's), rights under a swap agreement with Citibank N.A., and obligations of Enron delivered by the swap

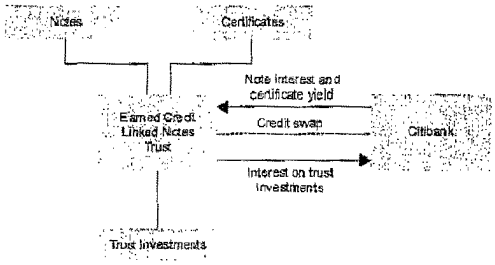
counterparty to the trust as a result of certain Enron credit events. A swap will be relied on to provide interest payments on the notes that are due semiannually each Feb. 15 and Aug. 15. Principal on the notes will be repaid at maturity from principal proceeds received from the trust investments.

Description of the Swap Agreement

A swap agreement documented by an International Swaps and Derivatives Association master agreement and related schedule and confirmation has been entered into between the trust and Citibank N.A., as swap counterparty (see chart). The swap is also linked to the credit performance of Enron.

In the absence of any event leading to an early termination of the swap, the swap counterparty will make payments to the trust on each Feb. 15 and Aug. 15 in an amount sufficient to pay interest payments due to the noteholders, and the trust will transfer to the swap counterparty all proceeds from the trust investments on the business day after receipt.

Enron Credit Linked Notes Trust Structure



Early Termination of the Swap

Certain events may cause either a full or partial termination of the swap. The swap may be terminated by the trust or by the swap counterparty upon the occurrence of events of default or termination events specified in the swap agreement. The swap counterparty may terminate the swap if Enron voluntarily files for bankruptcy under the U.S. Bankruptcy Code or is involuntarily filed into bankruptcy (an Enron

bankruptcy).

The swap counterparty may also terminate the swap in whole or in part after Enron fails to make payments on senior obligations of at least $25 million, which rank at least equal to claims against Enron for senior unsecured indebtedness for borrowed money in terms of priority of payment, coupled with publicly available information (an Enron failure to pay).

In addition, the swap counterparty has the option of terminating the swap in whole or in part at any time and for any reason by delivering a swap early termination notice to the trust specifying the notional amount by which the swap will be reduced, the specific trust investments to be sold, and the settlement date.

Payments Upon an Enron Bankruptcy

Upon an Enron bankruptcy, the outstanding principal and unpaid interest on the notes will be due and payable immediately. Despite the automatic acceleration of the notes, the trust may not take any action with respect to the trust collateral until the day after the right of the swap counterparty to settle the swap has expired. Payments on the notes will be made from the trust assets, which consist of Enron obligations as well as any remaining trust investments.

If a bankruptcy of Enron occurs, the swap counterparty or the trust may notify each other of the bankruptcy, and the swap counterparty has 60 days to inform the trust of its intention to terminate the swap. On the settlement date, the swap counterparty will deliver to the trust senior obligations of Enron that rank at least equal to claims against Enron for senior unsecured indebtedness for borrowed money in terms of priority of payment (Enron obligations) with a principal balance equal to the notional amount of the swap. The trust will deliver to the swap counterparty trust investments with a principal amount equal to the amount of Enron obligations delivered by the swap counterparty, plus, on the initial settlement date, the base amount of the certificates (initially $50 million).

Payments Upon an Enron Failure to Pay

After an Enron failure to pay, noteholders will be paid, to the extent of available funds, from trust assets consisting of Enron obligations, any remaining trust investments, as well as any swap payments from the swap counterparty. If the trust has insufficient funds to make full and timely payments to the noteholders, then at the written direction of holders of at least 25% of the outstanding principal amount of the notes, the indenture trustee will declare the outstanding principal and accrued interest on the outstanding notes to be due and payable immediately.

If an Enron failure to pay determined by means of publicly available information has occurred, the swap counterparty may notify the trust of its intention to terminate the swap in whole or in part. In the case of a partial termination of the swap, the swap counterparty will deliver to the trust a principal amount of Enron obligations (corresponding to the reduction of the notional amount of the swap) that mature no later than the business day before the maturity date of the notes, in exchange for trust investments plus, on the initial settlement date, the base amount of the certificates. The swap counterparty will continue to make interest payments to the trust based on the principal amount of trust investments remaining and the trust will pay the swap counterparty all receipts from the remaining trust investments. In addition, on each interest payment date, based on the principal amount of Enron obligations delivered to the trust, if interest payments due on the notes exceed actual interest received from such Enron obligations, the swap counterparty will pay the amount of any interest shortfall to the trust. Alternately, if on an interest payment date, interest payments received by the trust on the Enron obligations exceed the amount needed to pay noteholder interest, the trust will pay any excess interest to the swap counterparty.

Payments Upon a Swap Early Termination Notice

The aggregate amount of the outstanding notes will be redeemed on the redemption date, which is the same date as the settlement date. The redemption price will be an amount equal to the greater of principal plus accrued interest on the notes and the present value of the remaining scheduled payments of principal and interest on the principal amount of the notes discounted to the redemption date semiannually at the applicable treasury yield, plus 0.30%.

If the swap counterparty delivers a swap early termination notice to the trust, the trustee acting on behalf of the trust will calculate and notify both the indenture trustee and the swap counterparty of the principal amount of notes to be redeemed and the redemption price due to the noteholders. On the settlement date, the swap counterparty will pay the trust the redemption price of the notes and the trust will pay the proceeds received from the sale of trust investments to the swap counterparty.

Legal Review

Enron Credit Linked Notes Trust is a trust that conforms to Standard & Poor's criteria for special-purpose, bankruptcy-remote entities. Standard & Poor's has received various legal opinions from counsel of the parties to this transaction. These opinions, based on reasoned analysis and assumptions, provide comfort that, among other things, each party is authorized to enter into the contracts and agreements being executed, and the transaction documents are legal, valid, and binding obligations of the signatories enforceable according to their terms.

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Research:

Accounting Abuses and Proposed Countermeasures

Publication date: 02-Jul-2002
Analyst: Scott Sprinzen, New York (1) 212-438-7812

The epidemic of accounting abuses by U.S. corporations has severely undermined analysts' and investors' confidence in the veracity of financial reports. Numerous companies have been found to have significantly overstated their revenues, earnings, cash flow, or assets, or to have understated their liabilities. Lax corporate boards and outside auditors have evidently helped give rise to this phenomenon. Certain out-of-date accounting standards, gaps in the standards, or even the complexity of standards have also played a role, as has the intense pressure on managements to "make the numbers" and meet Wall Street's growth and earnings expectations.

Responding to the current crisis, the U.S. Securities and Exchange Commission (SEC) and the Financial Accounting Standards Board (FASB) are now pursuing various initiatives to restore confidence in financial reporting and disclosure. Standard & Poor's expects that much of the resulting information will benefit its analytic process and surveillance. The current initiatives, however, are likely to provide only a partial solution, and heightened attention to accounting-related matters--and skepticism by analysts--will continue to be appropriate.

Accounting Abuses

The greatest concentration of abuses has been in revenue reporting. Such improprieties have accounted for the dominant share of the restatements mandated by the SEC in the past few years. Notable recent examples include the following:

- Some energy marketers have admitted to engaging in phantom, or "round trip," trades in electricity contracts. These are essentially back-to-back swaps with no business purpose except to artificially bolster apparent trading volume and revenue.
- Similarly, in the telecom sector, Global Crossing Ltd. and Qwest Communications International Inc. are reportedly being investigated by the SEC for back-to-back swaps of fiber-optic capacity.
- In the pharmaceuticals sector, Allergan Inc. and Elan Corp. PLC have entered into transactions in which they formed joint ventures (JV) with third parties, made cash investments into the JV entity, but then got back some or all of the cash in the form of fees for performing R&D, these fees having been reported as revenue.
- Manufacturers of telecom equipment such as Lucent Technologies Inc. have made highly aggressive use of vendor financing in which, on sales to financially shaky buyers, profits are reported up front, with the financing being provided by the seller. Lucent's vendor notes receivables reached $8.4 billion at year-end 1999. Among its biggest vendor-financing deals was a $2 billion, five-year pact signed in 1998 with Winstar Communications Inc.: Winstar filed for bankruptcy in 2001.

Also, companies have increasingly made use of large, one-time, "big bath" restructuring charges or have regularly booked smaller restructuring charges--hoping these would be disregarded by analysts and investors--to accelerate the recognition of operating expenses with the objective of bolstering subsequent reported earnings. Among the many companies that Forbes magazine has termed "serial chargers" are Allied Waste Industries Inc., Cisco Systems Inc., Compaq Computer Corp., E.I. DuPont de Nemours & Co., Fortune Brands Inc., Tenet Healthcare Corp., and Waste Management Inc.

Moreover, notwithstanding the generally poor pension investment portfolio returns of the past two years, most companies have clung to seemingly aggressive long-range--return assumptions (i.e., 9.5% to 10.0% per year), enabling some of them to continue reporting material non-cash pension credits. For certain companies, including Ethyl Corp., United States Steel Corp., Weirton Steel Corp., Verizon

Communications Inc., GenCorp Inc., Northrop Grumman Corp., and Allegheny Technologies Inc., pension credits represent a substantial portion of their total reported earnings.

Although the statement of cash flows is much less susceptible to accounting manipulations than the income statement, recent developments have shown that it is far from sacrosanct. Thus, WorldCom Inc. has just admitted that it improperly reported $3.8 billion of expenses as capital expenditures within the past five quarters, thereby bolstering reported net cash flow from operating activities.

Along with the trend of overstating their financial performance, some companies have seemingly put renewed emphasis on innovative means of concealing debt:

- Companies--including Enron Corp.--have employed share trusts in which assets are "sold" to off-balance-sheet, special-purpose entities (SPEs), but in which the transaction's funding is supported by the seller in some manner such that the seller effectively retains the economic risks associated with the assets.
- Companies reportedly have entered into prepaid transactions under which they receive payment up front from a financial counterparty for future delivery of some commodity and reporting the transaction as deferred revenue rather than debt, even though interest expense is imputed in the terms of the transaction. There is no intent to make physical deliveries to satisfy the commitment; rather, the goods are ultimately sold back to the seller.
- Companies have entered into synthetic leases, which are structured to qualify as operating leases for financial reporting purposes, and finance leases for taxation purposes. Analytically, they are viewed by Standard & Poor's as a debt equivalent, just as are conventional operating leases. The insidious aspect is that they are not just off-balance-sheet, but are largely "off-footnote": Because the initial term of the lease is kept artificially short (for tax purposes), and in some cases the lease is nominally cancelable, the disclosed minimum future lease commitments understate the extent of the true economic liability.
- Finally, companies have entered into borrowing, derivatives, and operating agreements that include credit triggers--such as rating triggers, financial covenants, or material-adverse-change clauses--which can greatly magnify the consequences of erosion in credit quality, but which have often been poorly disclosed (see "Identifying Ratings Triggers and Other Contingent Calls on Liquicity, Part 2," published on May 15, 2002).

Countermeasures by the Rule Setters

In recent months, the SEC has greatly increased the number of investigations (formal and informal) it is pursuing regarding accounting-related matters. This has led to a large number of restatements by companies and, in several high-profile cases, the levying of fines.

The SEC has taken some steps that could lead to enhanced disclosures. Of these, Standard & Poor's views the following SEC proposals as particularly promising from an analytic perspective:

- A rule that would require companies to make disclosures about critical accounting policies and the effect on reported financial performance if the company were to assume that certain key estimates were changed;
- Accelerated and more comprehensive disclosure of insider company equity transactions, plus "loans of money to a director or executive officer made or guaranteed by the company or an affiliate of the company." Presumably, such a requirement would have revealed the abuses at Adelphia Communications Corp., where the founder and controlling owner, and members of his family, borrowed under a credit facility shared with--and guaranteed by--the company, using the proceeds in part to acquire shares of the company.
- Companies accelerate filing their quarterly and annual reports: 10K's would have to be filed within 60 days of the end of the fiscal year, rather than the current 90 days, and 10Q's would have to be filed within 30 days of the end of the quarter, rather than the current 45 days. The only downside could be the increased potential for errors as companies rush to meet the tighter deadlines; and
- Expansion of the list of events that require a company to file an 8K, and an acceleration of the deadline--to two business days from five to 15 days--for filing such a report.

Separately, the SEC has offered as guidance, in "Management's Discussion and Analysis of Financial Condition and Results of Operation" section of the financial statement, that companies consider including:

- Provisions in financial guarantees or commitments, debt or lease agreements, or other arrangements that could trigger a requirement for an early payment, additional collateral support, changes in terms, acceleration of maturity, or the creation of or an additional financial obligation. Such provisions could include adverse changes in the registrant's credit rating, financial ratios, earnings, cash flows, or stock price, or changes in the value of underlying, linked, or indexed assets;
- Circumstances that could affect the registrant's ability to continue to engage in transactions that have been integral to historical operations or are financially or operationally essential, or that could render that activity commercially impracticable, such as the inability to maintain a specified investment-grade credit rating, level of earnings or earnings per share, financial ratios, or collateral.

The SEC also stated that companies should consider the need to "provide disclosures concerning transactions, arrangements, and other relationships with unconsolidated, structured-finance or special-purpose entities or with other persons that are reasonably likely to materially affect liquidity or the availability requirements for capital resources."

Such disclosure could significantly enhance Standard & Poor's ability to maintain surveillance of credit triggers, but the SEC has instructed companies to consider disclosing only circumstances "that could materially affect liquidity if such circumstances are reasonably likely to occur." This, of course, is subject to interpretation.

The FASB, too, has launched a number of initiatives to address shortcomings in financial reporting. Broadly, these initiatives are also welcomed by Standard & Poor's. Most notably, the FASB is developing an "Exposure Draft" that would provide rules for determining when an entity (termed the "primary beneficiary") should consolidate an SPE that functions to support the activities of the primary beneficiary. With this initiative, the FASB's aim is to require the consolidation of SPEs that "lack sufficient independent economic substance." The FASB is clearly targeting the type of abusive schemes employed by Enron.

Nevertheless, preliminary indications are that the FASB is seeking to require consolidation of a number of types of "plain vanilla" securitizations, including collateralized debt obligations and multiseller commercial-paper conduits. On one hand, this could be seen as a non-event from a ratings perspective: Analytically, most securitized assets and related debt are added back to the balance sheet anyway because the corporate sponsor typically remains in a first-loss position and given the concerns regarding moral recourse, i.e., the reality that companies feel they must bail out a troubled securitization although there is no legal requirement for them to do so. (See "Substance, Not Form, of Securitizations Drives Standard & Poor's Leverage Analysis," published on April 18, 2002.)

On the other hand, Standard & Poor's would need to be alert to the potential practical ramifications of such accounting changes. For example, some companies might be in violation of financial covenants upon the consolidation of securitizations. Moreover, there is the risk of a chill being sent through segments of the asset-backed securities market on which certain companies are highly dependent.

In addition, the FASB has issued an exposure draft of a proposed interpretation of guarantees ("Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others," May 2002). This exposure draft essentially reiterates existing rules, compliance with which has been lax, requiring the guarantor to make the following disclosures, "...even if it is probable that the guarantor will not need to make any payments under the guarantee":

- The nature of the guarantee, including how the guarantee arose and the events or circumstances that would, under the guarantee, require the guarantor to perform;
- The maximum potential amount of loss under the guarantee; and
- The nature of any recourse provisions or collateral that would enable the guarantor to recover

amounts paid under the guarantee.

The FASB is also undertaking an ambitious project that would consist of a comprehensive review of standards governing revenue recognition. Given its sweeping nature, such a project could take several years to complete.

Standard & Poor's Responds

In the wake of recent developments, Standard & Poor's, in its credit review process, is placing significantly heightened emphasis on the assessment of accounting quality and information risk. Standard & Poor's also plans to incorporate expanded commentary on accounting-related factors into its industry- and company-specific research reports.

In addition, Standard & Poor's intends to take a more active role in commenting on proposed changes in accounting standards and financial disclosure regulations. Last month, Standard & Poor's called for more discipline and standardization in the reporting of core earnings (see "Standard & Poor's to Change System for Evaluating Corporate Earnings," published on May 14, 2002, and "Core Earnings and Ratings Analysis," published on June 4, 2002).

Moreover, to be fully responsive to market needs, Standard & Poor's intends to hold regular discussions with key constituents to consider ways in which its debt-rating policies and research could enhance investor recognition and understanding of accounting quality. To this end, Standard & Poor's sponsored an accounting forum on June 17 and plans to sponsor other such programs.

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Research:

Enhancing Financial Transparency: The View from Standard & Poor's

Publication date: 02-Jul-2002
Analyst: Vickie A Tillman, New York (1) 212-438-2625

(Editor's note: The following remarks were made by Vickie A. Tillman, executive vice president, Standard & Poor's, at the FDIC's Enhancing Financial Transparency Symposium on June 4, 2002, in Washington, D.C. They are being published on RatingsDirect as part of a series of articles on transparency.)

Thank you, and good morning. I am honored to be here.

This is a welcome opportunity to discuss with some of the best and brightest in the financial and regulatory worlds what needs to be done to enhance financial transparency. The capital markets depend on the confidence of investors, which in turn depends on truthful, timely and thorough public disclosure of a company's finances. Financial transparency is indeed the linchpin of our whole system, and I applaud the FDIC for convening this gathering.

Standard & Poor's has always championed transparency. Indeed, our credit and equity opinions depend upon it. I'd therefore like to give you a sense of how Standard & Poor 's broadly serves transparency, and how through more specific initiatives, we are taking action to enhance it.

We've all witnessed the growing complexity and globalization of the financial markets over the past decade. New financing techniques have also grown in complexity. We've seen more aggressive debt leveraging, more off-balance-sheet financing, more international transactions. Given the difficulty of understanding a corporation 's true underlying financial picture, investors and in some cases, security analysts, have been increasingly drawn to shorter-term performance—and companies have come under pressure to manage these expectations.

Few would dispute that there have been numerous benefits—and beneficiaries—from these structural changes. But few also doubt that this very complexity has had its dark side. It has become difficult for all but the most sophisticated to understand how some businesses actually operate. At the same time, it has made it easier for some businesses to appear transparent while actually hiding, or at least shading, their financial reality. Aggressive accounting techniques have become almost standard in some parts of corporate America. Many—perhaps most—of these techniques may be within the letter of the law, but it seems that too many of them probably skirt if not violate the spirit of full disclosure.

While creditworthiness is not generally driven by accounting, creditworthiness is obviously affected by accounting abuse, as—at the very least—it erodes confidence in management.

Everyone agrees our system needs fixing. And right now, corporate America's commitment to high ethical standards is under intense scrutiny.

At Standard & Poor's, we believe that fundamental analysis and the role that rating agencies play has grown even more critical in the current environment.

The SEC, Congress, FASB and others have proposed steps to enhance and accelerate disclosure. Standard & Poor's is clearly in favor of encouraging stricter accounting standards, more disclosure, and more compliance.

Mandating public disclosure is of course the realm of regulation and law. We rely on the regulators as the primary source of market discipline and we rely on them to ensure its adequacy. We also acknowledge the vital role that industry groups such as the FASB, SIA and others can play in ensuring the integrity of the

marketplace.

The system works when you have disclosure and when you have independent analysis of it. Standard & Poor's is an integral part of that process. We have a long history of providing value to investors through our analysis that allows them to make better financial decisions. We also see ourselves as part of the solution.

First, our credit and equity opinions rely on the completeness and accuracy of public disclosure.

- Rating agencies are not auditors, nor are we forensic accountants. However, we do have critical analytic skills honed over years of experience that allow us to make informed decisions. We scrutinize public documents and meet with management to understand a company's financial health before we assign a rating, and we use public documents in our surveillance activities.
- We will continue to regard skeptically the inability or unwillingness of managements to provide requested information, where that information can be reasonably expected to be a necessary part of the risk management or operations of an organization. This "information risk" is factored into our ratings.
- The SEC initiatives will enhance our surveillance activities. As more information becomes public more quickly, we will be able to utilize that information in our ratings and take appropriate actions as indicated on a timely basis.
- As I said earlier, we are not forensic accountants, but we are reviewing ways to provide more readily comparative assessments of accounting quality. These include expanded dialog with the internal audit function of the companies we rate, and access to the external audit's board.

Second, Standard & Poor's makes public our ratings process, and the information we need to arrive at our analysis.

- Evolving analytical and disclosure requirements generally reflect structural changes in the market. Some of the financing techniques I mentioned earlier—securitizations, off-balance-sheet financings, to name just two—have added to the information requirements needed for fundamental analysis. Credit risk has become more liquid, and there has been rapid growth and evolution of risk transfer markets spurred by securitizations and derivatives.
- Standard & Poor's has most recently focused on making public contingent commitments, particularly with respect to triggers in borrowing, counterparty or off-balance-sheet financing arrangements. Earlier this year, we urged that these contingent commitments be disclosed, and at the same time, we conducted a survey of some 1,000 investment grade corporate issuers, both here and abroad, asking for information on their use of contingent commitments.
- On May 15th, we released a survey of rating triggers and contingent calls on liquidity that was extremely well received, and we will continue to request this information as a matter of routine.
- We are also working in other areas that include liquidity and funding risk, risk transfer, and risk retention in securitizations. Later in June, we will be bringing together analysts, attorneys, and accountants to discuss certain credit market concerns with respect to these and other corporate accounting and disclosure issues.
- Perhaps the most important point to make here is that as markets change, the rating process has to change as well. Often, because of our work with both the issuers and the marketplace, we are in the position to identify areas that need to be captured through public disclosure. We welcome any initiatives, such as today's symposium, that allows us to discuss our observations and concerns with respect to public disclosure requirements.

Third, we adopt and promote analytical methodologies that bring clarity and consistency to financial reporting, and potentially contribute to the standardization of financial disclosure.

- Jointly with our equity analytic team, on May 14th, we took a bold step and introduced Core Earnings, a new definition of how we believe earnings should be calculated—one that reflects fundamental earnings performance. We hope it will bring much needed consistency and transparency to corporate reporting.
- We will utilize Core Earnings in our equity and credit analysis, in our U.S. equity indices, including the S&P 500, as well as adapt our databases to provide this information for our customers. To date

the public reaction has been overwhelmingly positive.

- Standard & Poor's would like to see the convergence of international accounting standards. We recognize the difficulties and long-term nature of achieving this goal, but would encourage continued discussions among the various entities. We maintain a globally consistent rating scale that requires significant adjustments across a range of accounting systems to enable comparisons. While we strive to make these adjustments as transparent as possible, a uniform, globally accepted set of standards would be to everyone's benefit.

Fourth, we can develop additional services to facilitate investors' ability to differentiate either the relative quality of disclosure or of corporate governance.

- Later this year Standard & Poor's Risk Solutions unit will release a survey rating the transparency, disclosure, and corporate governance practices of the companies in the S&P 500. This comparative survey is intended to draw attention to those with—and those without—strong practices.
- We have launched from our Risk Solutions unit a corporate governance assessment service. While originally intended for emerging markets where governance practices are more variable, it clearly has applicability to developed markets. Interest in and demand for the service has been accelerating. This is a separate enterprise from our rating services, and maintains its own staff of analysts.
- Finally, we are mulling the potential role of an expanded corporate governance assessment in the rating process and are currently surveying companies and investors to get their feedback.

We are all peers on this journey to help restore investor trust and confidence in the information used to make investment decisions. To make the system work for all of us in our various capacities, we need public disclosure. Henry Varnum Poor founded Standard & Poor's 142 years ago on the principle, "The investor's right to know." That is still our purpose today.

Thank you.

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STATEMENT OF

JP MORGAN CHASE & CO.

SUBMITTED TO

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

COMMITTEE ON GOVERNMENT AFFAIRS

UNITED STATES SENATE

JULY 23, 2002

Mr. Chairman and Members of the Subcommittee, my name is Jeffrey Dellapina. I am a Managing Director in the Credit and Rates Group of JP Morgan Chase & Co. I am accompanied by my colleagues Don McCree, a Managing Director and Robert Traband, a Vice President. I was involved in the later Enron prepay transactions. Mr. Traband is based in Texas and worked on the Enron account beginning in 1999. Mr. McCree currently serves as senior credit officer for the JP Morgan Chase Bank. He was not involved in the transactions that are being discussed today. He is here because the Subcommittee requested a senior banker who could address broad policy issues.

Overview

JP Morgan Chase & Co. is a holding company. Through our subsidiaries and affiliated companies we offer global financial services, have operations in more than 50 countries and serve more than 30 million consumers and the world's most prominent corporate, institutional and government clients, including over 90 percent of the *Fortune 1000* companies. JP Morgan Chase & Co. and its subsidiaries and affiliated companies employ nearly 100,000 people throughout the United States and worldwide.

Our institution has an established reputation for integrity and we welcome the opportunity to appear today at the invitation of this Subcommittee. In accordance with the Subcommittee's request, this statement will focus on, and provide background information with respect to the prepaid natural gas and oil forward contracts involving JP Morgan Chase and Enron.

At the outset, we wish to emphasize two significant points. *First*, prepaid forward contracts have been used for many years and are widely recognized as an entirely proper tool to enable businesses to increase their liquidity and diversify their sources of funding. *Second*, we do not provide accounting services to our clients. In the U.S. financial system, those are responsibilities that are properly assigned to the client's management, advised by its auditors (both internal and external), guided by generally accepted accounting principles (GAAP).

The Enron Prepaid Forwards

Before we turn to the Enron prepaid forward transactions, we would like to talk generally about corporate finance and prepaid forward commodity contracts in order to place these specific transactions in their proper context.

Importance of Corporate Finance Transactions

Senior financial officers of major corporations are continuously working to ensure that their companies' ongoing access to capital will enable asset growth and business prosperity. This management process includes taking actions to maintain liquidity and diversify the corporations' sources of funds. In support of these important objectives, lawyers, accountants, commercial bankers and investment bankers all work with clients to structure financial transactions that have favorable characteristics, within the parameters of existing accounting, tax and legal requirements.

Financing can be obtained in a multitude of ways, including, for example, common equity, preferred stocks, loans, commercial paper and other debt securities and, in the case of financial trading firms, repurchase and forward agreements. There are other forms of transactions that are designed to meet particular financing needs, commonly referred to as "structured finance" transactions. The structured finance market is very large and is participated in by the world's major financial firms. Examples of structured finance transactions include collateralized debt obligations (such as mortgage-backed securities and credit card securitizations), debt-equity hybrid securities, leases of all varieties, convertible bonds and convertible preferred stock.

Prepaid forward commodity transactions are also a form of structured finance. In "forward" commodity transactions, which are common in many industries, the parties enter into a contract for future performance tied to a commodity. A "prepaid forward" provides for payment to be made at the inception of the contract.

The specifics of structured finance transactions may differ significantly from client to client as we and other financial firms participate in transactions to meet the specific needs of each client. What these transactions have in common is increased liquidity and the diversification of funding sources. Diversification of funding sources is a matter of prudence. Throughout recent history, there have been numerous events that have had an adverse impact on the ability to access one or more funding sources and on the cost of doing so. Diversifying sources of financing mitigates a corporation's exposure to such events and enables it to maintain and expand its core business.

Description of the Enron Transactions

In 1992, Enron approached The Chase Manhattan Bank ("Chase"), one of the four predecessor banks that have now all been merged into JP Morgan Chase, with a request that it enter into a prepaid forward transaction. At that time, there was some uncertainty as to whether Chase, as a national bank, was authorized to accept physical delivery of a

commodity. Therefore, the 1992 transaction was accomplished by having a special purpose entity, or SPE, take delivery of the commodity. SPEs are companies that are established for a particular purpose. They are widely used in structured finance transactions.

From 1994 through 2001, Enron entered into a total of 10 more prepaid transactions involving Chase. Nine of these transactions were with Mahonia Limited and one was with Mahonia Natural Gas Limited, both Jersey Channel Islands SPEs (together, "Mahonia"). All but one of these transactions were "physically settled" transactions, meaning that they were settled with deliveries of gas or oil. The last transaction was "financially settled," meaning no commodity was delivered, although the cash payment was to be determined by the price of natural gas.

Prior to continuing with the chronology, we would like to address Mahonia. Mahonia is beneficially owned by a charitable trust. Neither Chase nor Enron has any ownership interest in Mahonia. No employee or officer of Chase or Enron served as an officer or director or held shares in Mahonia. The directors and officers of Mahonia make the ultimate determination as to whether or not to enter into a transaction. Those directors and officers are neither appointed, nor controlled, by Chase or Enron. The use of entities like Mahonia is standard activity in structured finance.

In the Enron prepaid forwards, the SPE entered into a prepaid forward contract with an Enron subsidiary using funds provided by Chase. The prepaid forward transaction created not only credit risks for Chase, but performance, delivery and commodity risks as well. As mitigants for these risks, the transactions included an Enron Corp. guarantee, a performance letter of credit or a surety bond, and either exchange-traded futures contracts or over-the-counter derivatives contracts with Enron Corp. Although the last prepaid transaction was financially settled, similar risks and mitigants were present in that transaction, the sole difference being that no physical delivery was required. Originally, the commodity purchased from Enron was sold into the broader market. After Chase was capable of taking physical delivery of gas or oil, Chase purchased the commodity from Mahonia, and in turn sold physical gas or oil into the market. Beginning in the late 1990s, Chase entered into contracts to sell its gas or oil positions to Enron, which was by far the largest market participant.

All of the transactions were undertaken at the initiative of Enron. Chase understood that the transactions originally had tax benefits for Enron. Later, Chase learned, Enron no longer received tax benefits from the transactions but chose to continue to engage in prepaid forward transactions for other corporate purposes. Enron management informed Chase that the prepaid forwards served to monetize the unrealized profit in its trading book. Enron also advised Chase that the rating agencies wished to see more cash generated from its growing trading activities.

There have been allegations in the media that the prepaid forward transactions were "disguised debt" or a "disguised loan." The prepaid forwards were undoubtedly

financing, as all contracts are that involve prepayment features, but every financing is not a loan. These transactions had different features, benefits and risks than loans.

These prepaid transactions were accounted for on the books of JP Morgan Chase consistent with GAAP. It is our understanding that Enron recorded these transactions on its balance sheet; in other words, they were not "off balance sheet" transactions. As stated earlier, however, the manner in which Enron accounted for these transactions on *its* books of account and in *its* financial statements was a matter for Enron and *its* management and auditors.

Conclusion

As the Subcommittee is aware, JP Morgan Chase was one of several financial firms that provided financial services to Enron. We have been one of the parties substantially harmed by its failure, incurring hundreds of millions of dollars in losses. JP Morgan Chase welcomes this opportunity to answer the Subcommittee's questions today and will continue to cooperate with the Subcommittee's inquiry.

Opening Statement of David Bushnell

Before the Senate Permanent Subcommittee on Investigations

July 23, 2002

Mr. Chairman and members of the Committee, thank you for the opportunity to speak to you today.

My name is David Bushnell. I am a Managing Director at Citigroup's Global Corporate & Investment Bank and its head of Global Risk Management, which functions as an independent control over our business units and is responsible for monitoring market and credit risk. In that capacity, my department ensures that risks – including market risk, credit risk, and risks to reputation – are identified, measured, and evaluated by our institution before we commit capital or become a party to any transaction or new type of business. My division establishes and monitors trading and credit limits, and, where appropriate, approves exceptions. In addition, the firm's risk management committees report to me.

Our institution recognizes the importance of the work that this Committee is doing with respect to its examination of Enron's collapse. Enron's failure was a pivotal event for American business. In the space of a few short months, Enron went from an investment grade credit ranked 7th in the Fortune 500 to bankruptcy. Like many other market participants, Citigroup lost money as an Enron lender. More importantly, investors have lost money, employees have lost jobs and the public has lost confidence in our financial markets. The integrity of our markets,

and the integrity of our borrowers and their financial statements, is of the utmost importance to us. We therefore commend the Committee's efforts to understand the factors that caused or permitted Enron's stunning collapse, and we encourage changes in accounting or other rules that will protect against what happened here.

During our business relationship with Enron, we thought we were dealing with honest managers who had a legitimate business purpose for the transactions we did with them. We believed that Enron was making good-faith accounting judgments that were reviewed by Arthur Andersen, which was then the world's premier auditing firm in this sector. We believed that the Audit Committee of Enron's Board exercised meaningful supervision over the company's accounting policies and procedures. The facts that are emerging about Enron's business and accounting practices, including the facts that have come to light through the work of this Committee, are very disturbing to us. They no doubt are disturbing to other financial institutions as well, because Enron had similar relationships with most of the large firms on Wall Street.

The emerging facts suggest that Enron was not the company we thought it was. If what has been reported turns out to be the case – large-scale self-dealing, inflated assets, management that was inattentive or worse, a subservient Board, and a failure of auditing controls – we would not have done the business we did with Enron. To the extent that Enron was able to manipulate and abuse good-faith financing efforts, our industry must understand how this happened – and do

everything possible to prevent it from ever happening again – so that investor confidence can be restored.

But let me be clear. While we regret our relationship with Enron, we acted in good faith at all times. Our employees, including the bankers who are here today, are honest people doing honest business. They did transactions that were common throughout Wall Street, and they believed those transactions were entirely appropriate.

The focus of this hearing is structured finance, and the accounting rules that apply to the types of structured transactions that Enron used. My colleagues will talk to you about some of the specific financing structures at issue, but I want to emphasize that, like every other institution in this business, we design financing structures for diverse businesses with unique needs against a background of accounting, tax, and legal rules. Some of those accounting rules are complicated and subject to interpretation by accounting experts. If specific rules do not work the way they should, then they should be fixed. Moreover, changes are needed to increase accounting oversight and the reliability of a company's financials. Clear accounting rules rigorously applied by businesses and their auditors are necessary predicates for investor trust. I must stress, however, that we do not dictate our clients' accounting practices. Once we are satisfied that a client's proposed tax and accounting treatment seem reasonable, the accounting judgments are left to the client and its accounting professionals who have access to complete information.

This, I would submit, is as it should be. It has always been the law and accepted practice that companies are permitted to rely on the certified financial statements of the party on the other side of a transaction. Our financial system assumes that all market participants must be able to rely on a company's financial statements and the representations of its outside auditors. The auditors are the experts in understanding the accounting rules – for example the 800 pages of rules that govern accounting for derivative transactions. And the auditors are in possession of detailed information about the company's entire financial picture, not just specific transactions. Recent regulatory initiatives appreciate that responsibility for the accuracy of financial statements must rest with company management and auditors, as evidenced by the recent SEC Rule requiring CEOs and CFOs to certify the accuracy of financial statements, and legislative proposals strengthening the independence and oversight of the auditing function.

At Citigroup, I oversee a sophisticated and comprehensive process for reviewing structured finance transactions. Two of our key approval committees are the Global Commitment Committee and the Capital Markets Approvals Committee (CMAC). The Commitment Committee is responsible for reviewing equity and fixed income securities underwritings. The overall mission of the Commitment Committee is to ensure that we are comfortable selling newly issued securities so that we protect our reputation for high-quality financings and retain investor confidence. To that end, the Commitment Committee meets with the

bankers who worked on the transactions, and reviews the issuer's accounting and disclosure statements, among many other factors.

The CMAC reviews structured financing products, among other things. Senior representatives from our market risk, credit risk, legal, accounting, and tax departments (as well as other departments) sit on the CMAC to evaluate proposed transactions from each of these perspectives. The CMAC approves only those transactions that it concludes are appropriate. For example, the Yosemite transactions, about which this Committee has expressed interest, were reviewed and approved by the CMAC.

We pride ourselves on our reputation for being an institution with integrity. If a transaction raises potential accounting, tax, legal, compliance, regulatory, or appropriateness issues for us or our clients – or otherwise exposes us to reputational risk – the CMAC evaluates the risks to ensure that our institution is comfortable in completing the transaction. This is not to say we substitute our judgment for that of our clients, or their tax, accounting, and legal advisors; responsibility for those judgments remains with them.

Thus, when we agreed to structure prepaid transactions for Enron, we relied heavily on its assurances that its outside auditor, Arthur Andersen – which at the time was a market leader – had reviewed these transactions. Enron told us that Andersen believed the proposed accounting treatment for the prepaids – that is, accounting for the cash the transactions generated as cash from operations rather than as cash from financing, and accounting for the resulting obligations as price

risk management liabilities rather than as debt -- was appropriate. And while I am not an accounting expert (no one on this panel is), this accounting treatment seemed reasonable to the members of the CMAC.

I am sure that the Committee understands that at the time these transactions were done, Arthur Andersen was one of the "Big Five" – a preeminent auditing firm whose word carried weight and gave comfort. Certainly now, with all of the information that has come to light about Arthur Andersen, it is easy to question Andersen's review. And, indeed, the information contained in this Committee's recent report and the related exhibits on Enron's Board is striking for what it reveals about Andersen's own concerns about the overall risk of Enron's accounting methodologies. The report indicates that Arthur Andersen shared its concerns with the Audit Committee of Enron's Board. But we learned about Arthur Andersen's reservations only after the fact. Legitimate questions can and should be asked about whether the three institutions charged with ensuring that Enron's financials were properly stated – Enron's management, auditors, and Board -- failed to live up to their obligations to the investing public.

The sobering facts about Enron set forth in this Committee's recent report make clear that much stronger oversight of the accounting profession is needed, and that controls must be put in place to ensure that auditors are truly independent of their clients. The report also suggests that a rule-based accounting system such as American GAAP, which creates narrow pigeonholes for classification, may be too susceptible to abuse. It perhaps should be supplemented by more of a

principle-based system. And we would certainly support rules requiring greater management accountability, more stringent Board oversight, and greater Board independence. We welcome debate on these issues. It is essential that we reestablish the trust that is necessary to the efficient functioning of our economy.

Thank you. I look forward to answering your questions.

Opening Statement of Rick Caplan

Before the Senate Permanent Subcommittee on Investigations

July 23, 2002

Thank you Mr. Chairman and Members of the Committee.

My name is Rick Caplan. I am a Managing Director of Citigroup's Corporate and Investment Bank and co-head of the North American Credit Derivatives Group, one of several business groups at Citi that structures transactions for sophisticated corporate clients. I began working in the derivatives business at Citibank in 1997, and I first became involved in structuring certain transactions for Enron in 1999.

A prepaid swap transaction – the transaction you have invited us to talk about today – is a form of structured finance. Structured financings have been used over the past several decades by virtually all sophisticated companies as a way of raising money. Just as companies always consider the tax, legal, and accounting consequences of every transaction they enter into and attempt to structure those transactions so as to achieve the most favorable results, the same is true when companies seek to finance themselves. Often times, the most efficient and effective form of financing for a company is not a straight loan, but a structured finance transaction that, in addition to generating liquidity, can address these other business considerations.

Most large public companies use many different forms of structured financing. In each instance, they choose the form of financing that best addresses their unique business and capital needs. While many structured financings have the same economic impact as a loan, they often are treated differently for accounting purposes. Such transactions are commonplace in corporate America and play an integral role in our capital markets.

There are many examples of loan-like transactions that have different accounting treatments. These include, among many others, financing tools that support much of this nation's trading in fixed income securities (such as repurchase agreements – "repos" – and reverse repos), widely-used insurance products (such as guaranteed investment contracts and finite insurance), equipment trust certificates widely used in the airline industry, and common project finance strategies (such as synthetic leases). Like many clients, Enron retained Citibank to arrange various types of financings – ranging from simple revolving credit facilities to more sophisticated structured financings, such as asset securitizations, synthetic leases, and prepaid transactions.

As this Committee is aware, Enron was the 7th ranked company in the Fortune 500 and was a company of great prestige and high standing, which made extensive use of structured finance. Indeed, from 1995 through 2001, Fortune Magazine selected Enron as the "Most Innovative Company in America."

And in 1999, Enron's CFO, Andrew Fastow, was awarded CFO Magazine's "Excellence Award for Capital Structure Management," based on the "unique financing techniques" he pioneered.

For all of Enron's innovation and sophistication, the prepaid swap transactions we are discussing today were hardly a unique financing technique. Prepaid swap transactions – and similar commodity-based financings – had been widely used in the power and energy industry since the 1970s. Prepaids have been an efficient way for energy traders to extract some of the embedded cash value of their long-term trading contracts, particularly since those contracts cannot be readily sold or assigned.

In essence, a prepaid swap contract involves an up-front cash payment by one party in return for an obligation by another party to deliver a commodity (or the cash value of that commodity) at some point in the future. In the prepaids engaged in by Citibank with Enron, Enron received cash up-front, in exchange for Enron's obligation to deliver, at some point in the future, a specific quantity of gas or oil or its financial equivalent.

The prepaids provided Enron with an ability to raise cash against certain long-term assets which, as we understood it, helped Enron address a "disconnect" between the revenue and cash flow in its trading book.

Enron, like all other trading companies, applied "mark-to-market" accounting to its trading activities. Under mark-to-market accounting, Enron was required immediately to record as revenue the present value of all its long-term commodity contracts, even though it would not receive the actual cash flow related to such revenue until a later time. Enron's financial statements therefore showed substantial revenue, without corresponding cash flow.

Enron told Citibank that, because of the way auditors – including its auditors, Arthur Andersen – accounted for prepaids, Enron could use prepaids to bring its cash flow in line with its revenues. As Enron explained, because prepaids were comprised of commodity trades executed in Enron's trading book, Enron's financial obligations on these trades would be recorded in its trading book as a trading liability – called "price risk management liability" – and the cash generated by these trades would be recorded in its trading book as "cash flow from operations."

Enron assured Citibank that its accounting treatment of prepaids had been fully vetted by Arthur Andersen, which, at the time, was one of this nation's leading accounting firms. The accounting position we understood Enron was taking, on the advice of Arthur Andersen, seemed reasonable based on our understanding of the then-existing accounting rules and guidelines. I should add that Citibank did not advise Enron – nor would it advise any client – as to the

appropriate accounting treatment of any transaction. Indeed, it is the firm's policy to inform clients that Citibank is not giving accounting advice and to direct clients to consult with their independent auditors on the appropriate accounting treatment for any transaction.

Some have suggested that prepaids are "off balance sheet" or that the liabilities that Enron incurred as a result of these financings somehow were "disguised" or "hidden." That simply is not true. Enron's obligations on these financings were clearly reflected as liabilities on Enron's balance sheet and denominated as "price risk management liability." A "price risk management liability" is a liability, plain and simple, that must be satisfied every bit as much as "debt." Thus, while not recorded as debt, prepaid liabilities were clearly obligations of the company and visible as such to investors.

There also has been a suggestion that Enron somehow was able to generate extra cash flow by using prepaids instead of loans. That also is not accurate. The overall cash flow for Enron would be exactly the same whether Enron used prepaids or entered into a bank loan. In the case of prepaids, which are contracts transacted in Enron's trading book, Enron booked the cash it received on these contracts as "cash from operations" – not as "cash from financing." We understood that Arthur Andersen had fully vetted, and blessed, this accounting treatment as well.

Another point I would like to address is the confusion that has arisen between prepaids and credit-linked notes. There is no necessary linkage between the two. Prepaids exist without credit-linked notes; credit-linked notes exist without prepaids.

A credit-linked note is simply a security through which an investor takes on the credit risk of a particular company without actually purchasing a bond issued by that company. Credit-linked notes are well-recognized financial instruments, widely issued and traded each year.

Citi structured Enron credit-linked notes – called Yosemite and the ECLNs. These instruments were sold to the largest, and most sophisticated, institutional investors in several Rule 144A offerings. Citi promised investors that the credit-linked notes would perform similarly to straight Enron bonds – and they have. In the case of the Yosemite transactions, the proceeds of these credit-linked notes offerings happened to be used – on day-one – to fund prepaid transactions, but could have been used to fund alternative obligations over time. There is no inherent connection between credit-linked notes and prepaids.

As with every offering that Salomon Smith Barney brings to market, the Enron credit-linked notes (and the underlying prepaid financings) were fully vetted and reviewed. The firm's stringent internal control processes are designed to safeguard Citi's reputation for integrity through careful screening of potential

transactions. The credit-linked notes and the underlying prepaid financings were approved only after undergoing this screening process.

I believe that our conduct in arranging the prepaids (and in selling Enron credit-linked notes) was entirely appropriate. We arranged these financings for what appeared at the time to be one of America's best and most admired companies. We used a financing structure that had been commonly employed in the energy and power industry for many years. And we relied on the fact that Enron's accounting treatment of these transactions was blessed by one of the nation's leading accounting firms and seemed reasonable under the then-existing accounting rules and guidelines.

Thank you Mr. Chairman and members of the Committee, and I look forward to answering whatever questions you may have.

Opening Statement of Maureen Hendricks

Before the Senate Permanent Subcommittee on Investigations

July 23, 2002

Thank you Mr. Chairman and Members of the Committee.

My name is Maureen Hendricks. I am currently a Senior Advisory Director at Salomon Smith Barney. I have spent almost three decades as an investment banker covering companies in the energy sector. I began my career in 1973 at Morgan Guaranty Trust – which later became JP Morgan – and then joined Salomon Brothers in 1997 – which then became Salomon Smith Barney. From 1999 until May 2001, I was the head of Salomon Smith Barney's Energy and Power Group, with responsibility for the Enron account.

As head of that group, I managed Salomon Smith Barney's investment banking relationship with Enron. As SSB's lead investment banker on the Enron account, I worked with Enron representatives and SSB product specialists to determine how we could best address Enron's investment banking needs. In that capacity, I worked with the client on such investment banking projects as raising money in the capital markets or merger and acquisition activity.

As you have no doubt heard quite often, Enron was a significant user of structured finance – which is simply a way of providing cash to a company through means other than traditional bank loans. And far from being faulted for it, at the time Enron was celebrated for its innovative financing techniques. The

structured financings for which Enron was applauded were done exclusively with banks since they have requisite expertise. The general capital markets – such as bond purchasers – prefer simplicity and generally will not purchase highly structured products.

One project that I worked on for Enron, along with others at SSB, was the Yosemite structure, which, in overly simplified terms, was designed as a way for Enron to do structured finance in the capital markets. The Yosemite notes were offered under SEC Rule 144A, which permits them to be sold only to the largest, most sophisticated institutional investors.

As it happened, the structured financing underlying the Yosemite offerings were prepaids. Prepaids are commodity-based structured financings that were widely-used in the energy sector. In fact, they have a very long history.

Production payments, which I structured in the 1970s when I worked in the petroleum group at Morgan, are precursors of the prepaid at issue here today. Production payments were financings that enabled an energy company to "monetize" – that is, extract the expected future cash flow – its future revenues from oil or gas production. The companies received cash upfront from a financing counterparty, in exchange for a promise to repay that amount with future revenues from production. In order to protect themselves from the movement of commodity prices, banks that entered into such financings would secure collateral that exceeded the value of the repayment obligation. As with the prepaids at issue

here, production payments originally had certain accounting advantages over straight loans.

Over the following three decades, structured finance has evolved considerably and is used in many forms by many industries. One evolution was that the market developed more sophisticated ways of limiting, or hedging, the commodity price risk associated with the company's obligation. By using derivatives, a bank could hedge out commodity price much more efficiently, without requiring posting of collateral.

We understood from Enron that Arthur Andersen had fully vetted the accounting treatment for prepaids and that, under the governing accounting rules, prepaids would have advantageous treatment similar to the earlier production payments. Specifically, Enron's obligation on the prepaids would not be recorded as debt (but as a "price risk management liability") and the upfront cash received would not be treated as cash flow from financing, but as cash from operations.

At the time that we structured the Yosemite deals for Enron, I had absolutely no reason to believe that there was anything wrong with prepaids or with Enron's proposed accounting treatment for them. Indeed, it appeared very familiar.

I was among the people responsible for shepherding the Yosemite offering to market. In that connection, I oversaw the due diligence that we conducted of Enron, in close cooperation with our outside counsel. We received

an opinion from Enron's outside counsel and a comfort letter from Enron's auditor. I believe that we asked the company the right questions. I regret to say that it appears from all that has recently been disclosed that we were not provided with the right answers by Enron management. It also appears that the audited financial statements, upon which we relied, were not accurate and did not fairly present Enron's financial condition.

Beyond supervising due diligence, I also was involved in the presentation of the Yosemite offering to the SSB Investment Grade Debt Commitment Committee. This Committee is charged with responsibility for reviewing, evaluating and, if appropriate, approving any transaction in which SSB acts as an underwriter or agent in connection with the sale of newly issued securities. It is the guardian of our reputation and our franchise. In this particular instance, the Commitment Committee conducted a searching evaluation of the Yosemite offering and approved those offerings.

I believe the decision to approve these transaction was an appropriate one, based on the information that had been provided to me and my team. I continue to believe that structured finance – if used by honest companies whose books are reviewed by responsible auditors – serves a valuable function in our nation's economy. However, with the benefit of hindsight and the raft of recent disclosures about Enron and its financial misdeeds, I deeply regret that our firm ever entered into transactions with this company.

Thank you.

Opening Statement of James Reilly

Before the Senate Permanent Subcommittee on Investigations

July 23, 2002

Thank you Mr. Chairman and members of the Committee.

My name is Jim Reilly. I am a Managing Director at Salomon Smith Barney in the Global Power and Energy Group. I have spent more than twenty-five years as a banker covering the energy industry. I began my career at Bankers Trust, where I spent nearly fifteen years. I then spent nearly ten years at Citibank and, after a brief stint at Donaldson Lufkin & Jenrette, re-joined the Company. I have spent virtually my entire banking career in Houston.

My responsibilities at Bankers Trust, Citibank, DLJ, and Salomon Smith Barney have largely remained the same. At each firm, I served as the "relationship manager" for a number of companies in the energy sector. In fact, many of the clients I serviced remained my clients even as I switched firms. Enron is one such example. I was the "relationship manager" for Enron (and its predecessor companies) since the 1980s, first at Bankers Trust, then at Citibank, and finally at Salomon Smith Barney.

Relationship managers work closely with a particular group of clients in order to understand their needs and to help them access the full range of resources and expertise available at the firm. Thus, if a client came to me with a particular financing objective, I would put it in touch with the appropriate group at

Citibank or SSB that was best positioned to help accomplish its goal. While in most cases I have a general familiarity with the transactions that my firm arranges for my clients, I do not structure these transactions and typically am not close to the details.

Clients approach me in very different ways about addressing their financial needs. In some cases, a client will come to us with a particular need or problem, but without a concrete idea about how to structure a solution. In those circumstances, I will introduce the client to the appropriate group within Citi, which will then work with the client to devise a solution. In other cases, a client will come to us with a financial need and a very specific idea about how it wants to meet that need. In those cases, I will involve the appropriate groups within Citi to review and, if appropriate, to implement the client's preferred solution.

My dealings with Enron were of both types, but generally followed this latter course. Enron was unique among my clients in terms of both the size and the sophistication of its in-house finance group. Enron's finance department in many ways resembled a small investment bank. While comparable companies employed a handful of finance professionals, Enron reportedly employed approximately one hundred professionals – many of whom were experienced bankers and graduates of the nation's top business schools. Beyond its size, Enron's finance department also was structured like an investment bank, with a number of subgroups that focused on different types of financial structures and products.

Mr. Chairman and members of the Committee, I would like to end my opening remarks on a more personal note. I have lived and worked in Houston for most of my life. Every day, I see the tragedy that Enron's demise has wrought on my hometown, and it saddens me greatly: the thousands of honest workers without jobs, their retirement savings wiped out, our city's economy in a tailspin. I want to thank this Committee for the thorough and detailed investigation it is conducting, in the hopes that we will see our way through this difficult period and emerge to find a stronger economy fueled by honest and hardworking companies.

Thank you, and I look forward to answering your questions.

Statement of Robert Furst
Before the
Senate Permanent Subcommittee on Investigations
July 30, 2002

Mr. Chairman, Madam Ranking Member, Members of the Subcommittee:

My name is Robert Furst and I appear here today voluntarily. In anticipation of testifying before you today, I met voluntarily with the Subcommittee's staff two weeks ago for nearly the entire day. As your staff has no doubt informed you, I cooperated fully with them, answering all of their questions to the best of my ability, reviewing a number of documents and providing information that I believed - and still believe - would assist the Subcommittee in understanding the investment banking transaction at issue here today. At the time I met with the staff, I intended to appear today and testify truthfully, fully and to the best of my ability.

Since I met with the staff, however, I have learned that the matter in which the Subcommittee is interested is also the subject of an investigation by the United States Department of Justice. As much as I would like to advise the Subcommittee of my view as to whether there was anything questionable concerning the investment banking transactions my colleagues and I worked on at Merrill Lynch, my lawyers have advised me that any such statement might constitute a waiver of my Constitutional rights under the Fifth Amendment. As I am sure the Subcommittee knows, and as my lawyers have informed me, the United States Supreme Court last year reaffirmed the principle that because, and I quote, "truthful responses of an innocent witness . . . may provide the government with incriminating evidence from the speaker's own mouth," even innocent witnesses may assert their Fifth Amendment right not to answer questions. I therefore respectfully advise the Subcommittee that I intend to assert my Constitutional privilege under the Fifth Amendment in response to the Subcommittee's questions today.

Thank you.

Statement of Schuyler Tilney

Mr. Chairman, Ranking Member, Members of the Subcommittee:

My name is Schuyler Tilney and I am a Managing Director at Merrill, Lynch. As you may know, two weeks ago, I met with Robert Roach, the Majority Counsel and Chief Investigator of this Subcommittee, Gary Brown, Special Counsel, as well as other members of the Subcommittee staff. I answered all of the questions they asked me concerning the subjects of today's hearing. I believe they would agree that I was fully cooperative and forthcoming about the facts that I knew, and that I did my best to answer every one of their questions. I met with the Subcommittee staff voluntarily, and I fully anticipated that I would appear voluntarily again this morning to answer your questions.

Unfortunately, since that time, I have been advised that one of the transactions to be covered today is the subject of an investigation by the Department of Justice. Therefore, I have reluctantly accepted my lawyer's advice to decline to answer questions at this time based upon my constitutional right not to do so. I am profoundly saddened that I must make this decision, and I am mindful of the significant personal and professional consequences that follow from my decision not to give testimony at this time. I look forward to the day when I can satisfy all of the concerns the Subcommittee may have about these matters. Thank you.

PREPARED STATEMENT OF G. KELLY MARTIN,
SENIOR VICE PRESIDENT AND PRESIDENT,
INTERNATIONAL PRIVATE CLIENT DIVISION,
MERRILL LYNCH & CO., NEW YORK, NEW YORK

BACKGROUND

Merrill Lynch strongly believes that our limited dealings with Enron were appropriate and proper based on what we knew at the time. At no time did we engage in transactions that we thought were improper. We welcome the opportunity to discuss them with you.

At the outset, all of us in this room recognize the enormous harm caused by the collapse of Enron. As Chairman Levin has stated:

- When Enron filed for bankruptcy on December 2, 2001, it was ranked the seventh largest corporation in America.

- In ten months, its stock had plummeted from $80 a share to practically nothing.

- Almost overnight, 20,000 employees lost their jobs and many of them lost their life's savings.

The facts that have now come to light about Enron, however, were not known at the time of the transactions discussed below. All of us now have the benefit of hindsight. Our decisions, however, had to be made based on the facts that we knew at the time.

At the time we conducted business with Enron, it was not the discredited, bankrupt company that it is today. It was, instead, the world's leading integrated electricity and natural gas company — a company of enormous stature and prestige.

In 1999, Enron reported revenues of $40 billion. It was ranked as the most innovative company in the country for ***five straight years*** by the Fortune 500 company CEOs, board members, and senior management who participate in the annual Fortune survey. In addition, it was ranked the top company for "Quality of Management" and the second best company for "Employee Talent." It was the highest rated global energy firm on the list of the "100 Best Companies to Work for in America." It was, literally, the textbook example of a modern American success story.

Moreover, at the time we dealt with Enron it was known to have extensive in-house and outside expertise. Enron's CFO, Andrew Fastow, had been awarded CFO Magazine's "Excellence Award for Capital Structure Management." Its CEO, Jeffrey Skilling, had been a partner at McKinsey & Co., the leading management consulting firm in the world. Enron had one of the most widely respected Boards in the country. Arthur Andersen, with its 85,000 employees and partners worldwide, was viewed throughout the world as a leader among independent auditing firms. Vinson & Elkins, Enron's principal outside counsel, was one of the leading law firms in Texas, where Enron was headquartered. It was well understood that Enron's financing activities were developed and vetted with these experts.

Importantly, Enron and its advisers were considered to be among the most knowledgeable in the world in structured finance transactions, particularly in the asset heavy energy business. All major corporations and their officers continuously work to ensure that they have diversified access to capital. An important component of this process is to maintain liquidity and seek a wide array of funding alternatives.

Funding can be obtained through equity or debt financing, private equity investments, preferred equity, loans or structured finance transactions. The types of structured finance transactions will vary by type of client, industry or asset classes, but their common objective is increased liquidity and diversification of funding sources. All would agree that, used appropriately, structured finance transactions are perfectly acceptable.

Our firm dealt with Enron at arms-length, and made business decisions based on the information that was then available. We relied on Enron's accountant's opinions, its Board approvals, its lawyers' opinions, its audit committee oversight, and other governance processes, and felt justified at the time in believing Enron's financial representations. In addition, the transactions were subject to Merrill Lynch's internal approval process, and included review with business, legal, and other personnel who had no personal stake in the outcome. At no time did we engage in transactions that we thought were improper.

MERRILL LYNCH'S RELATIONSHIP WITH ENRON

In terms of fees, Enron was not a large client relationship for Merrill Lynch.

Merrill Lynch is one of the world's largest global diversified financial institutions. We participate in every aspect of investment banking for corporate, institutional, and government clients throughout the world. In 1999 – the time of the transactions at issue – we had net revenues of $22.3 billion and net earnings of $2.7 billion. Our investment

banking revenues alone that year were $3.7 billion. Enron was not a significant contributor to Merrill Lynch's revenues or earnings.

Between 1997 and 2001, Enron retained advisors to assist it on 43 completed strategic transactions. These transactions often involved mergers and acquisitions and are among the most profitable transactions for investment banks. Merrill Lynch is one of the leading advisers in the world on such transactions. Yet Enron retained Merrill Lynch to act as an adviser on only one such transaction during the entire five-year period. The total fee on that assignment was $1 million. At least ten other firms performed more advisory assignments for Enron during this period, including two firms that, added together, performed a total of 23 such assignments.

Although Merrill Lynch participated in debt and equity offerings for Enron, the relationship was modest. During these five years, Merrill Lynch's average annual investment banking fees were $3.5 billion while its Enron-related investment banking fees were $8.2 million – only two-tenths of one percent of the total average annual fees.

From time to time, Merrill Lynch also participated in credit lines for Enron. Here too, however, we had a minimal role. We did not participate in most of the credit lines and our commitments represented less than 3% of the few credit lines in which we participated. We were never the lead lender in any loan syndicate. We did not participate in any of the billions of dollars of pre-pay transactions that the Subcommittee has examined.

We discuss below the transactions that the Subcommittee has asked us to address.

BARGE TRANSACTION

At his May 7 testimony, Chairman Levin stated:

> One type of deception Enron used was to report on the company's financial statement the sale of an asset, despite an understanding that Enron would buy it back after the financial statement was filed or despite a hidden guarantee that the entity buying the asset would receive a certain rate of return.

In this regard, questions have been raised whether it was appropriate for Enron to record a December 1999 transaction with Merrill Lynch as a sale. In that transaction, a Merrill Lynch entity – Ebarge, LLC – bought shares of a company that entitled Ebarge to part of the cash flows from the sale of energy to be produced by generators on three barges. Merrill Lynch's investment exposure in the transaction was $7 million. Merrill Lynch agreed to the transaction largely to build our relationship with Enron, and believed that it was likely, though not certain, that a third party unaffiliated with Enron would soon purchase Merrill Lynch's shares in the company.

Merrill Lynch does not know — even today — whether Enron's accounting treatment for this transaction was correct. We were not advising Enron on the appropriate accounting treatment for this transaction. In general, when we act as a purchaser or seller, we are not asked for and do not provide advice on the other party's accounting treatment; rather, we expect them and their experts to

determine the appropriate accounting treatment. This is market practice and fully in accord with legal standards. Furthermore,

1. There was no understanding by Merrill Lynch that Enron or any entity related to Enron would buy back Merrill Lynch's shares. In fact, Merrill Lynch had a contrary understanding – that an independent third party was likely to buy Merrill Lynch's interest.

2. There was no guarantee, hidden or otherwise, that Merrill Lynch would receive a certain rate of return. The purpose of not including a reference to any guarantee in the written agreement was not to hide it; it was because there was no guarantee and Merrill Lynch was at risk. The written purchase and sale agreement expressly provided that it was the entire agreement of the parties, and that it superseded any other understanding related to the purchase and sale. Had Enron not succeeded in finding a buyer for our interest, our only recourse would have been to try to find a buyer ourselves.

3. We did anticipate that an independent third party (an Asian trading company, which we understood was close to agreeing to the principal terms of a purchase of the shares) would buy Merrill Lynch's interest, but Merrill Lynch knew that it was at risk and knew that it had no remedy if the company failed to go forward and Enron and Merrill Lynch failed to find another purchaser.

4. The transaction was, in fact, a purchase of an equity interest rather than a loan. Merrill Lynch owned the shares, was at risk until it was able to re-sell those shares, and, though it hoped and expected to be able to re-sell those shares at a profit, had no guarantee that would happen.

5. Merrill Lynch played no role whatsoever in determining Enron's accounting for the transaction.

6. Nevertheless, we considered a number of issues presented by the transaction. Consistent with Merrill Lynch's internal procedures, the transaction was considered by a committee of individuals that included credit, legal and other personnel. Merrill Lynch uses these types of committees as a significant internal control. They include people from different areas of the firm who have no personal stake in the proposed transaction and who are expected to consider a wide range of issues potentially raised by a transaction. Before deciding to proceed with this transaction, the committee did what it was supposed to do: it considered the issues (including whether the transaction could be used to manipulate Enron's income statements) and concluded that Merrill Lynch's participation in the transaction was appropriate.

Among the factors considered:

i. Merrill Lynch was, in fact, at risk in the transaction,

ii. Enron's accounting for the transaction had been vetted with and approved by Enron's outside auditors,

iii. Enron and its experts were among the most sophisticated in the world on structured finance, and

iv. The transaction was so small relative to Enron ($40 billion in revenues reported in 1999) that it seemed inconceivable that the transaction could be used to manipulate Enron's income statements.

The Subcommittee may ask why the Asian trading company never purchased Merrill Lynch's interest and why LJM2 eventually did purchase Merrill Lynch's interest at the price it paid. We do not know the answer. Enron told Merrill Lynch in December 1999 that 1) it expected the Asian trading company to buy Merrill Lynch's shares within a relatively short time, 2) Enron was close to an agreement with that company on the terms of the purchase, 3) Enron could not guarantee this result (obviously, with good reason, since the Asian trading company ultimately decided not to buy the shares), and 4) if the company elected not to purchase Merrill Lynch's interest then Enron would use its resources to try to find another purchaser. The only people who can explain why the Asian trading company elected not to go forward and why LJM2 ultimately purchased those shares at the price it paid are the people at those entities who made the decisions.

LJM2

The Subcommittee has asked Merrill Lynch to discuss its role in LJM2.

LJM2 was organized by Mr. Fastow with the approval of Enron and its Board of Directors. Its express purpose was to make privately negotiated investments in energy and communications related businesses or assets – principally those owned or identified by Enron. It followed the structure of LJM1, which was developed by Enron and its experts, not Merrill Lynch.

Merrill Lynch acted as private placement agent for LJM2 between September 1999 and April 2000 and, in that capacity, helped introduce sophisticated investors to LJM2. These investors contributed approximately $265 million of the $390 million that was raised for LJM2. For these efforts, Merrill Lynch received just over $3 million in fees. Merrill Lynch itself invested $5 million in and committed to lend up to $10 million — out of a total commitment by all lenders of $120 million — to LJM2. It is not unusual for placement agents to invest in private partnerships for which they are acting and in this partnership other major investment banking houses made similar or larger investments. Ninety-six Merrill Lynch employees invested approximately $16.6 million in LJM2 through an investment fund. All such transactions were conducted only after appropriate review in accordance with Merrill Lynch's applicable policies and procedures. To date, the investors in LJM2 (including Merrill Lynch and its employees) have not received and may not ever receive the full amount of their investment, much less a significant return on their investment.

Following Enron's collapse questions have arisen about the role played by Mr. Fastow as the managing member of LJM2's general partner. Of course, Merrill Lynch did not choose that role for Mr. Fastow. We did, however, receive assurances that Enron's Board and senior management had considered Mr. Fastow's role and had implemented a number of significant internal controls designed to protect Enron's interests (for example, requiring Enron's Chief Accounting Officer to review each transaction). We also knew that Enron's Board had vetted the issue internally with its own lawyers. The conflicts were disclosed not only to LJM2 investors but to Enron investors as well.

RESEARCH COVERAGE

The Subcommittee has asked about an Enron complaint in April 1998 concerning Merrill Lynch's research coverage of Enron and whether, as a result, Merrill Lynch's research rating was compromised.

The facts are:

- In April 1998, an internal memorandum to Merrill Lynch's then-president, Herb Allison, indicated that Enron was not going to invite Merrill Lynch to participate in an underwriting of Enron's common stock because Enron was disappointed with our research coverage. The memorandum asked Mr. Allison to place a call to Enron executives for the purpose of reconsidering their decision, citing our longstanding relationship with the company and leadership position in the natural gas industry.

- We understand that such a call was made and ultimately Merrill Lynch participated as a co-manager in the transaction, which occurred in May 1998.

- At no time was Merrill Lynch's research compromised. In fact, our analyst retained his intermediate Neutral rating throughout the time in question. His Neutral rating extended from at least July 1997 through August 1998, when he left the Firm.

- In October 1998, after he joined his new firm, our former analyst initiated his Enron coverage with a rating of Accumulate.

- In November 1998, the Merrill Lynch analyst who assumed coverage of Enron, along with continuing his coverage of a related sector, also initiated coverage with a rating of Accumulate.

- In 2001, our analyst was one of the first to downgrade Enron.

PARTICIPATION IN LOAN FACILITY FOR ZEPHYRUS

Finally, the Subcommittee has also asked about Merrill Lynch's participation in a loan syndication for Zephyrus, an Enron-related entity. The facts with regard to Zephyrus are:

- On November 28, 2000, J.P. Morgan Chase, Bank of America, N.A., BNP Paribas and Fleet National Bank provided Zephyrus with a $482 million five-year senior secured loan.

- In April 2001, Merrill Lynch agreed to commit up to $40 million of the $482 million facility; we are currently owed $22.5 million.

- This commitment was approved in the ordinary course pursuant to the firm's applicable policies and procedures for such commitments.

CONCLUSION

We thank the members of the Subcommittee for this opportunity to come before you today and present information that may be helpful in your investigation into Enron's collapse. We fully support your efforts and want to assist in restoring investor confidence in our capital markets. Merrill Lynch intends to be an industry leader in helping to ensure that America's capital markets are governed by the highest ethical standards.

Had we known at the time what we know today, we would not have conducted business with Enron. Without the benefit of hindsight, however, and based on the information available to us at the time, we strongly believe that our actions were appropriate and proper.

ENRON PREPAYS

Total Prepays: more than $8 Billion (9/95 - 9/01)
($5 billion outstanding at bankruptcy)

- **JPMorgan Chase:** more than $3.7 Billion
  12 prepays, 1992-2001

- **Citigroup:** more than $4.8 Billion
  14 prepays, 1993-2001

- **Others:** more than $1 Billion
  Multiple prepays, 1992-2001

  - **Bankers Trust**
  - **Barclays**
  - **Connecticut Resource Recovery Authority**
  - **Credit Suisse First Boston**
  - **FleetBoston**
  - **Morgan Stanley**
  - **Royal Bank of Canada**
  - **Royal Bank of Scotland**
  - **Toronto Dominion**

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Permanent Subcommittee on Investigations
EXHIBIT #101

FINANCIAL INSTITUTION KNOWLEDGE OF ENRON PREPAYS

Enron: "Why Does Enron Enter into Prepays? Off balance sheet financing (i.e., generate cash without increasing debt load)."

–Internal Enron presentation, accounting dept., Bates EC1594741

JP Morgan Chase: "Enron loves these deals as they are able to hide funded debt from their equity analysts because they (at the very least) book it as deferred rev[enue] or (better yet) bury it in their trading liabilities."

– Internal Chase email (11/25/98), Bates MAH 2129

Citigroup: "E[nron] gets money that gives them c[ash]flow but does not show up on books as big D Debt."

– Internal Citigroup email (9/28/00), Bates CITI-SPSI 84924

Andersen: "Enron is continuing to pursue various structures to get cash in the door without accounting for it as debt."

– Internal Andersen email from Enron auditor (12/16/98), Bates AASCGA 1132-1

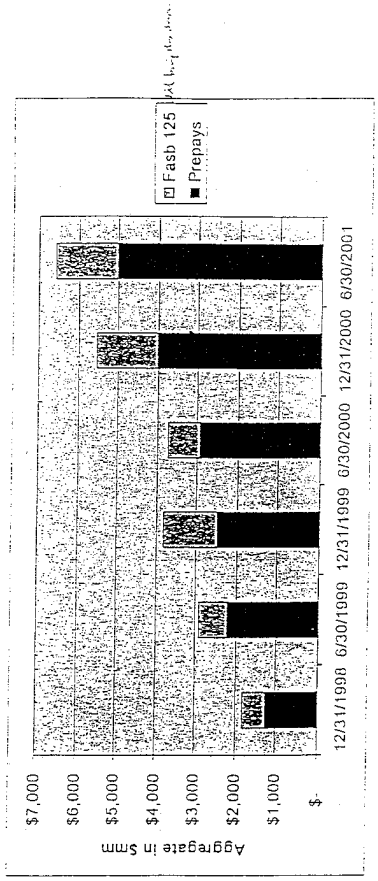
Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Permanent Subcommittee on Investigations
EXHIBIT #102

Finance Related Asset Sales

Prepays and 125 Sales ($MM)

	12/31/1998	6/30/1999	12/31/1999	6/30/2000	12/31/2000	6/30/2001
Prepays	$ 1,258	$ 2,239	$ 2,489	$ 2,962	$ 4,016	$ 5,031
Fasb 125	$ 573	$ 683	$ 1,316	$ 772	$ 1,521	$ 1,533
	$ 1,831	$ 2,922	$ 3,805	$ 3,734	$ 5,537	$ 6,564



Permanent Subcommittee on Investigations
EXHIBIT #103

SOC 21423

ASF – Detail on Prepays

Prepay	Term	Inflows	Dec-98	Jun-99	Dec-99	Jun-00	Dec-00	Jun-01
Gas: Chase II	Sep 95 - Oct 00	224,440	3,706	2,647	413	-	-	-
Gas: Chase III	Dec 96 - Jan 00	225,021	(184,851)	(107,536)	(40,984)	(19,872)	9	(9)
Gas: Chase IV	Dec 97 - Dec 01	299,992	(252,755)	(210,151)	(171,146)	(129,995)	(88,390)	(45,605)
Gas: Chase V	Jun 98 - Jul 02	250,000	(240,721)	(205,192)	(173,603)	(140,448)	(107,499)	(74,027)
Gas: Energy America	Jun 98 - May 08	36,443	(40,482)	(37,577)	(35,359)	(34,291)	(35,046)	(34,439)
Gas: Chase VII (APEA)	Apr 99 - Apr 11	287,611	-	(271,687)	(263,745)	(256,654)	(263,192)	(256,729)
Gas: Chase VIII	Jun 99 - Jun 04	500,000	-	(507,324)	(486,471)	(435,179)	(393,457)	(350,083)
Gas: Cage	Sep 99 - Sep 00	(250)	-	-	418	529	-	-
Gas: Chase IX	Jun 00 - Jun 05	648,374	-	-	-	(661,938)	(656,136)	(604,936)
Gas: Chase X	Dec 00 - Nov 05	328,258	-	-	-	-	(340,279)	(332,242)
Gas:Citibank I	Jun 01 - Dec 01	250,000						(250,592)
Power: CRRA	Mar 01 - May 12	220,180		-	-	-	-	(227,421)
Crude: Chase IV	Dec 98 - Dec 02	249,994	(254,387)	(242,756)	(193,753)	(172,332)	(139,846)	(133,051)
Crude: Delta	Dec 98 - Nov 99	190,000	(189,917)	(121,407)				
Crude: Truman	Jun 99 - Sep 99	500,000	0	(488,809)				
Crude: Jethro	Sep 99 - Nov 99	675,000	0					
Crude: Yosemite I	Dec 99 - Dec 04	800,000	0	-	(797,744)	(795,157)	(832,326)	(760,194)
Crude: Yosemite II	Feb 00 - Jan 07	324,000	0	-	-	(322,982)	(332,814)	(319,751)
Crude: Yosemite III	Aug 00 - July 05	472,000	0	-	-	-	($506,056)	(523,597)
Crude: Chase II	Dec 00 - Dec 01	315,000		-	-	-	($319,286)	(304,546)
Crude: Yosemite II Bridge		315,000			(327,298)			
Crude: Citibank-Mahil	Ended 12/99		(46,973)	(23,111)		-	$0	-
Crude: Chase III	Ended 11/99		(51,999)	(26,116)	-	-	$0	-
Crude: Citibank FX Hedge	May 01 - Apr 06							(12,075)
Crude: Citibank USD	May 01 - Apr 06	474,781						(489,973)
Crude: Citibank GBP	May 01 - Apr 06	156,732						(158,434)
Crude: Citibank EUR	May 01 - Apr 06	149,956						(151,103)
Total		$7,894,532	$(1,258,379)	$(2,239,019)	$(2,489,272)	$(2,962,319)	$(4,016,320)	$(5,030,807)

EC 000088019

Impact on Year 2000 Enron Credit Ratios from 1) Adding Outstanding Prepays to Debt, and 2) Deducting Prepays from "Funds Flow from Operations"

	2000 Reported Financials	Adjustment[1]	2000 Adjusted Financials
Total Debt	$10.2 billion	+ $4.0 billion	$14.2 billion
Total Equity[2]	$14.8 billion		$14.8 billion
Total Capital	$25.0 billion		$29.0 billion
Debt / Equity	**69.2%**		**96.2%**
Debt / Total Capital	**40.9%**		**49.0%**
Funds Flow from Operations[3]	$3.2 billion	- $1.5 billion	$1.7 billion
Int. + Pref. Dividends + Rent Exp.	$1.1 billion	+ $200 million	$1.3 billion
Funds Flow Interest Coverage [4]	**4.07**		**2.37**

[1]$4.0 billion in prepay debt taken from 2001 Enron Board presentation, Bates RCO 21428; $1.5 billion deduction to "Funds Flow from Operations," taken from 2001 Enron Board presentation, Bates EC 000058019; $200 million addition to interest expense based on interest at 5% on additional $4.0 billion in prepay debt.

[2]Total Equity is equal to Shareholders' Equity, Company-Obligated Preferred Securities of Subsidiaries and Minority Interests, consistent with Enron's presentation of Total Capital in company presentations to rating agencies. Bates EC 000469368.

[3]Subcommittee staff estimate based on March 2001 Enron Global Markets presentation citing "Actual Funds Flow Interest Coverage" of 4.07. Calculation assumes interest expense of $838 million, dividends on preferred shares of $77 million and rent expense of $143 million as reported in Enron 2000 10-K, yielding "Funds Flow from Operations" of $3.248 billion. Bates EC 000007671.

[4]"Funds Flow Interest Coverage" calculated as "Funds Flow from Operations" + interest incurred + dividends on preferred shares + rent expense, divided by interest incurred + dividends on preferred shares + rent expense. The Subcommittee staff has included dividends on preferred shares based on the appearance of their inclusion in Enron's previous years' calculations.

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Permanent Subcommittee on Investigations
EXHIBIT #104

Impact on October 2001 Enron Valuation from Adding Outstanding Prepays to Debt[5]

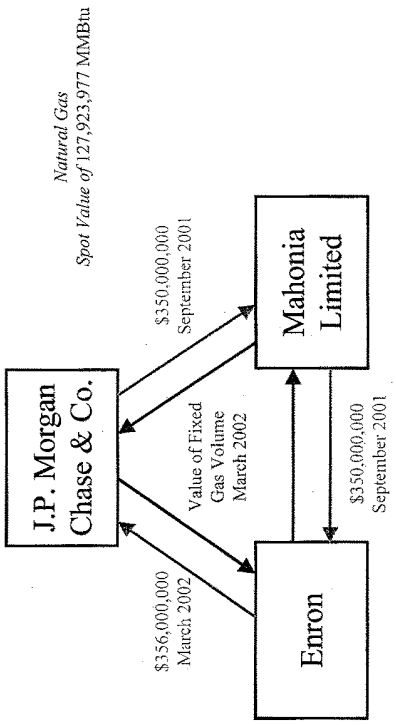
	Balance Sheet Debt	Adjustment	Balance Sheet Debt + Prepays
Enterprise Value[6]	$23.4 billion		$23.4 billion
Subtract Debt and Pref. Obligations	$13.1 billion	+ $4.8 billion	$17.9 billion
= Equity Value	$10.3 billion		$5.5 billion
Divide by Shares Outstanding	744 million		744 million
= Actual / Implied Market Price per Share	$14		$7
% Change in Share Price			46%

[5]This Subcommittee analysis is for demonstrative purposes only and does not take into consideration a number of other complicating factors, including the billions of dollars in off-balance sheet debt that, once known to the market, resulted in a collapse of Enron's share price. The fact that Enron shares ultimately traded at pennies per share suggests that investors thought the company had exceeded its limit in loans and other financing structures.

[6]Enterprise value equals market equity value of $10.4 billion plus balance sheet debt, net of cash, of $12.0 billion plus preferred securities of $1.1 billion. Market equity value is based on Enron's share price of $14 as of October 2001 multiplied by 744 million shares outstanding.

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Chase/Mahonia



Permanent Subcommittee on Investigations
EXHIBIT #105

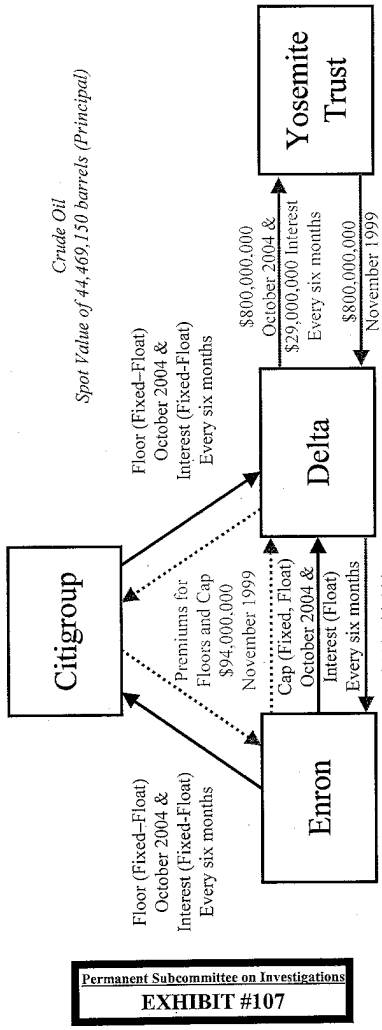
Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Chase/Mahonia Collapsed into Loan

Permanent Subcommittee on Investigations
EXHIBIT #106

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Yosemite I (Citigroup)



Permanent Subcommittee on Investigations
EXHIBIT #107

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Yosemite I (Citigroup) Collapsed into Loan

Permanent Subcommittee on Investigations
EXHIBIT #108

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Here is a copy of today's bank presentation.
Please keep any confidential as we have
discussed before.
Thanks,
Mark

ENRON

Enron Corp Bank Presentation

November 19, 2001

Waldorf Astoria

New York, NY

PRIVILEGED AND CONFIDENTIAL

Permanent Subcommittee on Investigations
EXHIBIT #109

EC 001006346

Debt Issues

Commodity Transactions with Financial Institutions

		Term	Current Amount ($MM)	Funding Source
Gas				
	Gas 1	Dec-01	19	Bank - amortizing
	Gas 2	Mar-02	350	Bank - non-amortizing
	Gas 3	Jun-02	46	Bank - amortizing
	Gas 4	Jun-04	308	Bank - amortizing
	Gas 5	Jun-05	533	Bank - amortizing
	Gas 6	Nov-05	299	Bank - amortizing
	Gas 7	May-08	33	Bank - amortizing
	Gas 8	Apr-11	258	Bank - amortizing
		Total Gas:	1,846	
Power				
	Power 1	May-12	211	Bank - amortizing
		Total Power:	211	
Crude				
	Crude 1	Dec-01	168	Bank - N/A
	Crude 2	Oct-02	150	Bank - non-amortizing
	Crude 3	Nov-02	75	Bank - amortizing
	Crude 4	Oct-04	800	US Dollar Yosemite I - non-amortizing
	Crude 5	Jul-05	475	US Dollar CLN I - non-amortizing
	Crude 6	Apr-06	475	US Dollar CLN II - non-amortizing
	Crude 7	Apr-06	162	Sterling CLN II* - non-amortizing
	Crude 8	Apr-06	155	Euro CLN II* - non-amortizing
	Crude 9	Feb-07	305	Sterling Yosemite II* - non-amortizing
		Total Crude:	2,765	
		Total:	4,822	*Amounts stated in USD

Note: GBP 1.00 = USD 1.4761 and EUR 1.00 = USD 0.9113

EC 00100407

FINAL

Project 10

Due Diligence Findings

November 7, 2001

CONFIDENTIAL

Permanent Subcommittee on Investigations
EXHIBIT #110

CONFIDENTIAL

CITI-SPSI 003302

Prepays

Deals	Type	Arranger	Commodity	O/S Amount as of 9/30/2001
Financial - Capital Markets				
Yosemite I	Financial - CLN	SSB	Crude	$800.0
Yosemite II (GBP)	Financial - CLN	SSB	Crude	305.0
ECLN I	Financial - CLN	SSB	Crude	475.0
ECLN II	Financial - CLN	SSB	Crude	475.0
ECLN II (Euro)	Financial - CLN	SSB	Crude	155.0
ECLN II (GBP)	Financial - CLN	SSB	Crude	161.0
				$2,371.0
Financial - Bank				
Gas Pre-Pay	Financial - Bank	Citibank	Gas	$250.0
Crude Pre-Pay	Financial - Bank	CSFB	Crude	165.0
				$415.0
Physical - Bank				
Chase III/TD	Physical - Bank	Chase	Crude	$150.0
Chase IV	Physical - Bank	Chase	Crude	52.0
Chase 3Q	Physical - Bank	Chase	Crude	150.0
Chase IV	Physical - Bank	Chase	Gas	$15.2
Chase V	Physical - Bank	Chase	Gas	49.2
Chase VIII	Physical - Bank	Chase	Gas	305.7
Chase X	Physical - Bank	Chase	Gas	299.4
Chase IX	Physical - Bank	Chase	Gas	532.8
Chase 4C's	Physical - Bank	Chase	Gas	350.0
				$1,904.3
Industrial				
Chase VII (APEA)//Municipality	Industrial	APEA/Chase	Gas	$178.5
North America/Municipality	Industrial	Municipality	Gas	33.5
Energy America/CRA	Industrial		Power	212.3
				$424.3
Total Pre-Pays				$5,114.6

What are Prepays?

- Series of normal individual trading transactions (i.e. swaps, options, physical forwards, etc.) structured to generate cash in return for some obligation, either product or cash settlement through financial instructions.
- Example: Enron contracts with XYZ Corp. where XYZ delivers Enron $25MM cash in return for 1,000,000 BBLS of crude valued at $27/BBL in 12 months. Enron and XYZ will normally enter into a separate, offsetting swap agreement to eliminate any open positions and price risk.
- Common industry practice.

Permanent Subcommittee on Investigations
EXHIBIT #111
EC 001594740

Why Does Enron Enter into Prepays?
• Off balance sheet financing (i.e., generate cash without increasing debt load).
• Allows for balance sheet management specifically price risk management assets and liabilities.
• Allows for purchasing product at discount.
EC 001594741

EC 00001336S

ARTHUR ANDERSEN

Prepaid Transactions Discussion

Permanent Subcommittee on Investigations
EXHIBIT #112

Prepaid Transactions

EC 000013366

- Include upfront payments of cash in exchange for future deliveries of gas over some time period (Usually 10-20 years).
- Typically counterparties are municipalities who can raise cash through the issuance of tax free municipal bonds.
- Municipalities, when raising cash through tax free municipal bonds, must comply with certain "no arbitrage" rules.
- Due to this, there are many instances where the gas marketer signs certain statements that prohibit them from treating these transactions as debt.

368

For prepays to be treated as trading contracts, the following attributes must exist:

- None of the individual agreements in this structured transaction are linked commercially or make reference to any of the other documents; in effect, each is a stand-alone, normally occurring derivative instrument which continue to be in effect even if other pieces of the transaction are terminated for any reason.
- The PGA and each swap are settled at current market values, and the PFA includes replacement cost provisions with monthly settlement (which is typical of MTM trading instruments).
- Price risk related to the PGA is transferred from the gas supplier to the purchaser, without the gas supplier further affecting the purchaser's management of this risk or the purchaser's other PGA-related economics. This includes any future actual or contingent swaps that may be contemplated.

EC 000013367

EC 000013368

- The purchaser of the gas must have an ordinary business reason for purchasing the gas, not in-substance be a special purpose entity (SPE) established just to effect a secured investment in a debt instrument from a gas supplier. The SPE issue could arise by virtue of the purchaser's very nature and the substance (or lack thereof) of its other business operations. It could also arise based on the types of contractual limits included in the series of structured transactions(e.g., the debt of the purchaser is recourse to the gas supplier or not recourse to any of the purchaser's other assets). EITF 97-__ also addresses the establishment of a "virtual SPE" when the recourse provisions of specific contracts substantively create an SPE within an otherwise "normal" commercial entity.

Prepaid Transactions

EC 000013369

Other Issues:

Recent IRS interest

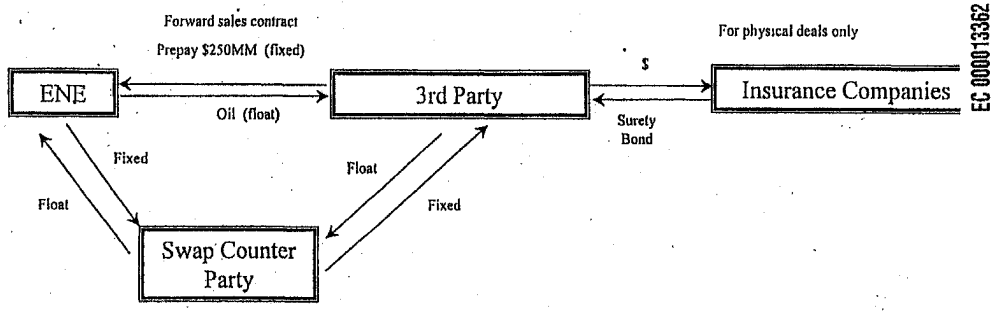
- The IRS is currently investigating certain gas prepay structures to determine whether or not these would be debt/taxable transactions which would violate the no arbitrage rules discussed previously.

Index based prepays

- These are considered to be debt because no price risk management activity is being performed as no price risk is transferred in a floating/index transaction.

ARTHUR ANDERSEN

PREPAY STRUCTURE



- ENE receives a lump sum cash payment of $250MM in return for the delivery of oil over the term of the contract (forward sales contract).
- Volumes are fixed upfront (on a monthly or quarterly basis) therefore ENE is providing price risk management services.
- Third party hedges its price risk related to the forward sales contract by entering into a de-linked swap with Swap Counterparty. Where third party receives fixed for float.
- Swap Counterparty hedges their price risk by entering into a de-linked swap with ENE where Swap Counterparty receives fixed for float.
- Settlement between ENE and Third Party can be physical or financial.
- For physical deals ENE purchases a surety bond for Third Party guaranteeing ENE's performance under the forward sales contract. If the insurance company's credit rating decreases, ENE is required to replace the insurance company or pay a higher float.

EC 000013362

Prepay Swap

Issues

(1) **What is the accounting by ENE for the forward sales contract?**

Since ENE is a MTM company they are not within the scope of SFAS 133 therefore, bifurcation is not required. ENE is providing price risk management services and would record the following:

CASH

MTM Liability

(2) **How would ENE account for the swap with Swap Counter Party?**

The swap would be MTM.

(3) **What is the accounting for the surety bond?**

Under Statement 133, the surety bond is considered a financial guarantee that provides for payments to be made in response to changes in an underlying (insurance company's credit rating). Therefore, the derivative would be measured at fair value.

(4) What would the accounting be if there were cross defaults between all three transactions? (i.e. if ENE defaults on forward sales contract the swap is terminated)

If the contracts include cross defaults, then all three transactions must be considered one and therefore be accounted for as a financing. EITF 88-18 provides guidance on whether certain factors of the transaction indicate debt or deferred revenue. We reviewed the factors indicating debt vs. deferred revenue and we believe we would meet several factors that would indicate debt.

EC 000013363

Important Factors In Prepay Transactions

1. Lump sum payment = Present Value (Fixed volumes x price curve (term deal))
2. Counter party has price risks
3. Settlement should be periodic (ie monthly/quarterly)
4. Each contract must be de-linked
5. Contracts should be standard (normal swap)

Current Issues

1. Master ISDA's – creates cross default provisions and contracts are no longer de-linked
2. SPE – If ENE is sponsor of SPE only hedge 97% in swap due to ENE's continuing involvement.
3. 133 – Forward sales contract is scoped out of 133 because Enron is a MTM company (otherwise it would be accounted for as debt)
4. Cost of Funds – Prepays are discounted at Enron's cost of funds and Enron is changing the discount rate used on the other liabilities from LIBOR to Enron's cost of funds. (So there will be no deferred items on Schedule C related to prepays).

EC 000013364

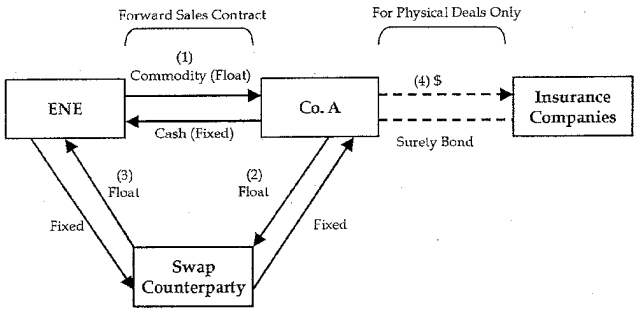
ARTHUR ANDERSEN

To: The Files

From: Deb Cash
Patty Grutzmacher

Date: June, 1999

Subject: Prepay Transaction



Transaction Description

1. ENE receives a fixed amount of cash in return for a floating payment in cash or a commodity, the amount determined as the product of future commodity index prices and fixed commodity volumes.
   a) This transaction represents a forward sales contract as opposed to the monetization of an existing contract.
   b) Volumes to be repaid are fixed therefore Enron is providing price risk management services
   c) The forward sales contract must settle periodically (i.e. monthly or quarterly) to maintain the integrity of the price risk.

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Permanent Subcommittee on Investigations
EXHIBIT #113

Date: June, 1999

Subject: Prepay Transactions

d) The forward sales contract must be at market day one:
fixed payment = present value (fixed volumes * price curve)

2. Co. A may choose to hedge its price risk related to the forward sales contract by entering into a swap with Swap Counterparty where Co. A receives fixed for float.
   a) This swap must be de-linked in every manner (i.e. termination provisions) from the forward sales contract. Note that Master ISDA's may create cross default provisions in these prepay transactions and therefore contracts are no longer de-linked.
   b) If Co. A is an SPE, and Enron is considered the sponsor of the SPE, Co. A can only hedge 97% of their price risk in order for Enron to avoid consolidation of Co. A due to Enron's continuing involvement. Per EITF 90-15 and Topic D-14, the 3% residual equity must stay at risk for the entire term of the transaction.

3. Swap Counterparty may choose to hedge their price risk related to the swap in (2) above by entering into a swap with Enron where Swap Counterparty receives fixed for float.
   a) This swap must be de-linked in every manner from the forward sales contract in (1) and the swap in (2).

4. For physical deals, Enron may purchase a surety bond for Co. A guaranteeing Enron's performance under the forward sales contract. If the insurance company's credit rating decreases, Enron is required to replace the insurance company or pay a higher rate.
   a) If Co. A is an SPE and Enron is considered the sponsor of the SPE, then the surety bond can only guarantee 97% of Enron's performance in order for Enron to avoid consolidation of Co. A due to Enron's continuing involvement.

Based on our discussions and lengthy consultation with John Stewart of the PSC, the following is a summary of the accounting, basic criteria and considerations related to prepay transactions:

Accounting

(1) **What is the accounting by ENE for the forward sales contract?**
Since ENE is a MTM company providing price risk management services they would record the following:

MTM Liability

Date: June, 1999

Subject: Prepay Transactions

(2) **How would ENE account for the swap with Swap Counterparty?**
The swap would be MTM.

(3) **What is the accounting for the surety bond?**
Under Statement 133, the surety bond is considered a financial guarantee that provides for payments to be made in response to changes in an underlying (insurance company's credit rating). Therefore, the derivative would be measured at fair value.

(4) **What would the accounting be if there were cross defaults between all three transactions? (i.e. if ENE defaults on forward sales contract the swap is terminated)**
If the contracts include cross defaults, then all three transactions must be considered one and therefore be accounted for as a financing. EITF 88-18 provides guidance on whether certain factors of the transaction indicate debt or deferred revenue. We reviewed the factors indicating debt vs. deferred revenue and believe the transaction would meet several factors that would indicate debt if the contracts contained cross-defaults.

Basic Criteria

(1) Fixed payment = present value (fixed volumes x price curve (term deal))

(2) Counterparty has price risks

(3) Settlement should be periodic (i.e. monthly/quarterly)

(4) Each contract must be de-linked

(5) Contracts should be standard (normal swap)

(6) Term of prepays done during the fourth quarter should cross-over at least two reporting periods (i.e. if the prepay is done in November, the term must be greater than four months to cross-over year-end and first quarter), otherwise a term that crosses over one reporting period is acceptable

Date: June, 1999

Subject: Prepay Transactions

Considerations

(1) Master ISDA's create cross default provisions and therefore contracts are no longer de-linked

(2) SPE – If ENE is the sponsor of SPE, the SPE can only hedge 97% in swap in order for Enron to avoid consolidation of SPE due to ENE's continuing involvement

(3) Cost of Funds – Prepays are discounted at Enron's cost of funds and Enron is changing the discount rate used on the other liabilities from LIBOR to Enron's cost of funds and Enron is changing the discount rate used on the other liabilities from LIBOR to Enron's cost of funds. (So there will be no deferred items on Schedule C related to prepays)

Accounting Literature
- EITF 96-21
- EITF 90-15
- Topic D-14
- December 1997 SEC Speech – Armando Pimentel
- EITF 88-18

To: John E. Stewart@ANDERSEN WO
CC: Thomas H. Bauer@ANDERSEN WO; Carl E. Bass@ANDERSEN WO; Patricia S. Grutzmacher@ANDERSEN WO
BCC:
Date: 12/16/1998 09:52 AM
From: Debra A. Cash
Subject: Cash vehicles
Attachments:

John,

Enron is continuing to pursue various structures to get cash in the door without accounting for it as debt. Rawhide is closing this week along with several of the prepay structures. A question has come up with respect to monetizing the value (MTM asset) associated with some long-term power contracts in their portfolio.

We have all concluded that Enron could transfer price and credit risk in the cash structures and account for them as price risk management activities as long as price risk was not passed directly back to ECT by the party that took the price risk from ECT (no cross defaults in swaps, etc). They want to take this one step further and transfer only the credit risk associated with the contracts. In the proposed structure, ECT assigns its rights to certain in the money power contracts to an spe in exchange for a price swap at the money and $. The cash would represent the MTM value of the contract. The price swap would pay fixed to spe and float to ENE.

I believe, since ENE receives $ and pays a fixed amount back to the spe, that this would be debt. Do you agree?

Unlike most deals, I don't need an answer right away!

Deb

Permanent Subcommittee on Investigations
EXHIBIT #114

WHY ENRON PREPAYS WERE SHAM TRANSACTIONS

- The trading parties, Mahonia and Delta, were not independent from the banks, JPMorgan Chase and Citigroup.

- The trades in each prepay transaction were linked.

- There was no price risk for any party.

- There was no ordinary business reason for purchase of gas or oil by the banks or the special purpose entities.

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002

Permanent Subcommittee on Investigations
EXHIBIT #115

FITCH 18244
CONFIDENTIAL

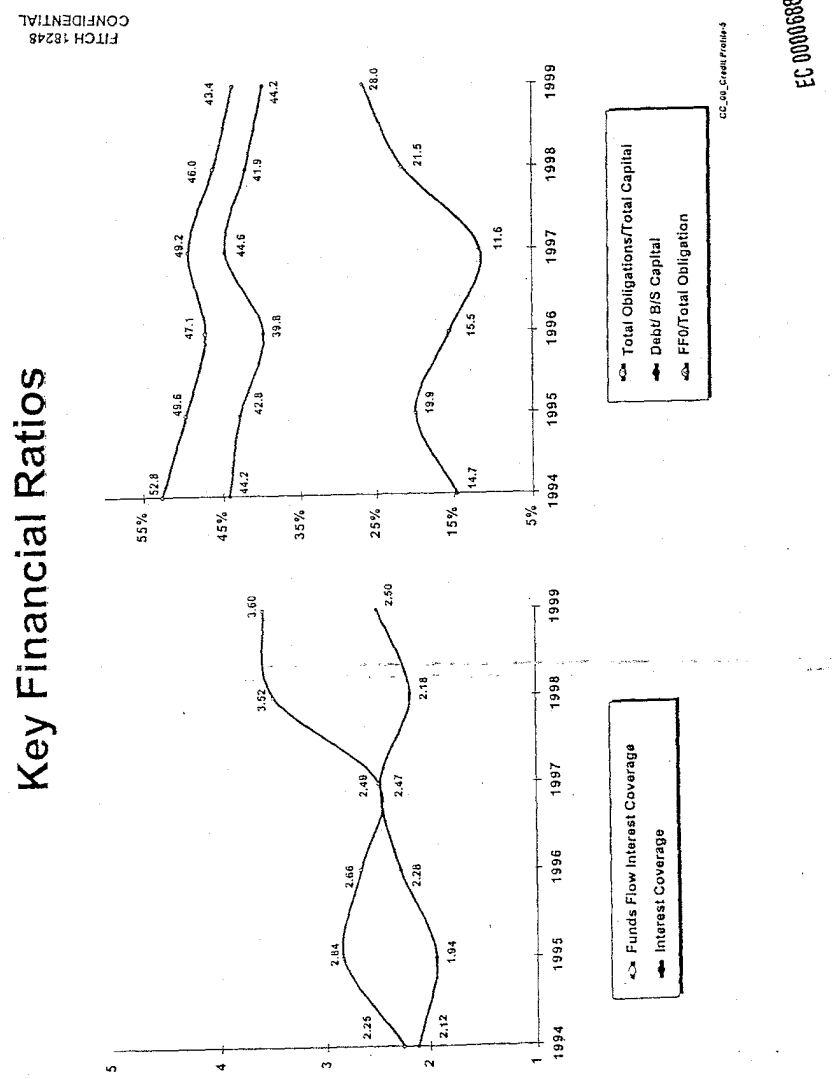
Enron Corp. Credit Conference
Credit Profile
January 29, 2000

Jeffrey McMahon
Executive Vice President, Finance
and Treasurer

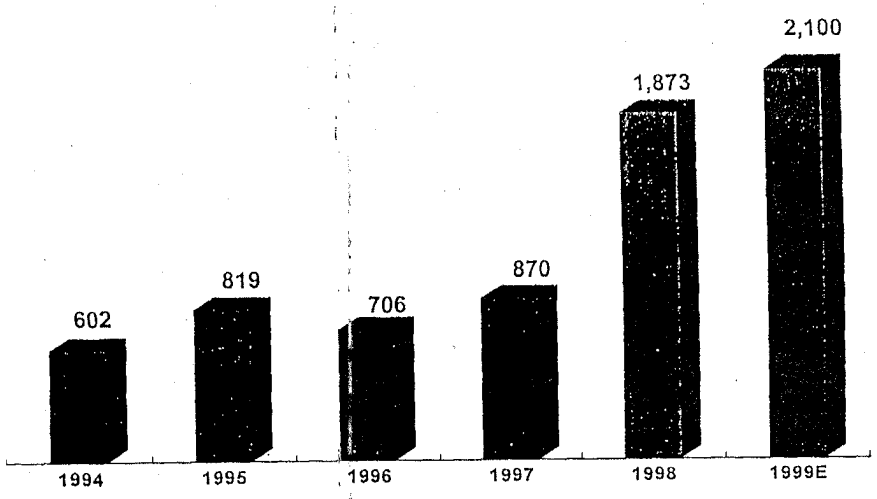
Permanent Subcommittee on Investigations
EXHIBIT #116

GC_00_Credit Profile-1

EC 000068842


CONFIDENTIAL
FITCH 18248
Key Financial Ratios
55%
45%
35%
25%
15%
5%
52.8
49.6
47.1
49.2
46.0
43.4
44.2
42.8
39.8
44.6
41.9
44.2
14.7
15.5
11.6
21.5
28.0
1994
1995
1996
1997
1998
1999
Total Obligations/Total Capital
Debt/ B/S Capital
FFO/Total Obligation
5
4
3
2
1
2.25
2.84
2.66
2.48
2.47
2.28
2.12
1.94
3.52
3.60
2.18
2.50
Funds Flow Interest Coverage
Interest Coverage
EC 000068846

Total Funds Flow from Operations
(in millions of USD)



FITCH 18249
CONFIDENTIAL

EC 000068847

FITCH 18253
CONFIDENTIAL
Is it Everything?
Hmmm....
Off Balance Sheet
Debt, Structured
Finance, Non-Recourse
Debt, Guaranties
Can they
make
a more
confusing
Annual
Report?
CC_20_Credit Pitfalls-19

Is Non-Recourse Debt Non-Recourse?

FITCH 18254
CONFIDENTIAL

YES!

EC 000068852

Kitchen Sink Disclaimer

FITCH 18255
CONFIDENTIAL

Enron does not recommend using this analysis for anything other than illustrative purposes and for the purpose of concluding that the off-balance sheet obligations are not material to Enron's consolidated credit analysis. Cigarette smoking may be harmful to your health.

EC 000068853

Kitchen Sink Analysis
Proforma 1999

		Off Balance Sheet Ventures	Guaranties	Pro Forma
Funds Flow	[illegible]	560.9		2,660.9
Interest	[illegible]	449.6		1,257.2
	[illegible]			3.12
Pre-Tax Income	2,019.0	943.2		2,962.2
Interest	807.6	449.6		1,257.2
	2.50			2.36
Total Obligation	8,000.0	7,394.0	17.5	15,411.5
Total Equity	10,433.2	4,275.8		14,709.0
	43.4%			51.2%
Funds Flow	2,100.0	560.9		2,660.9
Total Obligation	8,000.0	7,394.0		15,394.0
	26.3%			17.3%
B/S Debt *	7,845.3	7,394.0	17.5	15,256.8
Debt/Capital	39.6%			47.7%

* *Excludes ACES*

FITCH 18256
CONFIDENTIAL

387

CC_00_Credit Profile-13

EC 000068854

Common Misperceptions

Myth vs Fact

Myth	Fact
○ Enron operates in a non-rate base trading business which is inherently risky	○ Enron's cash flows from its non-regulated businesses are stable and predictable
○ There are massive amounts of debt that is not included in Enron's credit profile	○ The inclusion of all obligations (without adjustment for non-recourse) does not materially change the financial profile of Enron
○ The deregulated energy market is so new it is too early to determine who will survive	○ Enron has been in this segment for over a decade and is the dominant market participant

FITCH 18263
CONFIDENTIAL

EC 000068861

Common Misperceptions

Myth vs Fact

FITCH 18264
CONFIDENTIAL

Myth	Fact
○ Enron is reluctant to issue equity	○ Enron has issued over $7 billion of equity since 1994
○ Management does not communicate its true financial position to the investor community or the rating agencies	○ Management is extremely accessible to anyone willing to take the time to understand its credit - Banks - Institutional Investors - Rating Agencies
○ Enron dealmakers worldwide aggressively pursuing new business lines bind the company without centralized approval and control	○ Risk and Assessment Controls policy requires the approval of Enron Corp Senior Management and the Board of Directors to bind the company
○ Enron characterized by competitors as being overly aggressive and engaged in "Risky Business" lines	○ Enron enjoys First Mover status in Network Business creating substantial barriers to entry for competitors

EC 000068862

Top Ten Reasons Enron is Under-Rated

FITCH 18265
CONFIDENTIAL

10. It's been years since the last rating agency upgrade and EVERY financial metric has improved
    - Ratios
    - Scale and Scope
    - Management Depth
    - Market Share
    - Diversity
    - Book Equity and Market Cap

9. Management has delivered on all credit profile promises and proactively manages its balance sheet to achieve target rating.

8. Enron boasts the premier Risk Management Control System in the industry (over $130 million spent annually).

7. Management has issued over $7 billion of equity over the past several years.

6. Enron's major initiatives are only in those markets in which it can become the number one participant, thereby significantly adding stability to its earnings by having a structural cost advantage over its competitors .

EC 000068863

Top Ten Reasons Enron is Under-Rated

FITCH 19266
CONFIDENTIAL

5. Over the past 10 years, Enron's performance has demonstrated a low risk business strategy in a highly volatile commodity/energy market.

4. Enron's financial ratios vs peer companies are favorable, especially considering Enron's competitive advantage with respect to market shares and control systems.

3. Bond spreads/bank spreads indicate A- risk weighting.

2. Communication with analysts investors and credit officers is direct and candid - No Secrets Policy

1. Enron's credit rating is critical to the maintenance and growth of its existing dominant market share position.

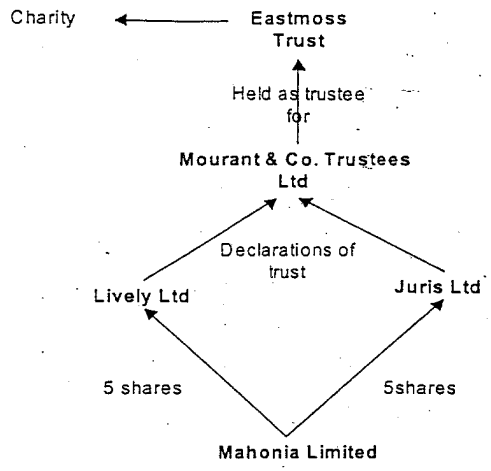
EC 000068864

Conclusion

AA Credit Company with Above Market Yields

FITCH 18267
CONFIDENTIAL

The Ownership of Mahonia Limited



Permanent Subcommittee on Investigations
EXHIBIT #117

D. O. Moon
P. de C. Mourant
K. S. Baker
R. F. V. Jeune
C. E. Coutanche
I. C. James
A. R. Binnington
J. D. F. Crill
T. J. Herbert

Consultants
H. de. C. Mourant
C. A. R. du Feu
R. R. Jeune, O.B.E.

Mourant du Feu & Jeune
Advocates, Solicitors and Notaries Public
P.O. Box 87, 18 Grenville Street, St Helier,
Jersey, Channel Islands

Telephone (0534) 74343
Telex 4192064
Telecopier (0534) 79064

Mislaid! Any news? Richard S. 25/7

Our Ref: ICJ/50/275/6

COMMERCIAL RELATIONS
25.APR.1986
RECEIVED

R.A.C. Syvret, Esq.,
Commercial Relations Officer,
Commercial Relations Department,
Cyril Le Marquand House,
The Parade,
St. Helier,
Jersey, C.I.

24th April, 1986

Dear Richard,

Our Clients, Chase Bank & Trust Company (C.I.) Limited, Trust Division are considering promoting, from time to time, special purpose vehicles for use in particular banking transactions. The possible areas in which the SPV's could be used are numerous, but at this stage it can be foreseen that the likely use for them would be:

1. where a company wishes to raise finance not by way of borrowing but by way of a related transaction. For example, a company may prefer not to borrow money on the security of a freehold property but rather to sell it to an SPV with the right of first refusal to repurchase the property at the same price. The SPV would borrow the money from Chase and the loan would be financed by the rental income generated by the property. By this means the company is able to retain an interest in any increase in value of the property whilst releasing the value of the property for investment in higher yield investments and at the same time retaining its existing debt/equity ratios. The SPV can be protected by insurance the value of the property falling below the cost price and so can avoid any risk to it.

2. where a company has a long-term borrowing at a fixed rate of interest below market values the liability can be assumed by an SPV in return for a payment by the company which would be financed by a borrowing this amount from Chase at market rates. By this means the principal amount borrowed by the company could be reduced whilst the cost of servicing the debt is also effectively reduced.

Permanent Subcommittee on Investigations
EXHIBIT #118

R.A.C. Syvret, Esq.
24th April, 1986

For obvious reasons it is important that the SPVs are controlled by Chase but, for accounting and other requirements, it is not desirable that they are wholly owned by Chase. Accordingly, Chase is considering establishing a charitable trust which would own all the shares of a holding company which in turn would wholly own the various SPVs. As you are aware this type of structure has been used for some of the "put-through" companies which have been used to "re-package" bonds and other monetary instruments over the recent months.

In this case however, unless the structure is used for a public issue of securities which although is possible, is not contemplated at this stage, there do not appear to be any particular consents which will be required from your Department other than those normally required in connection with the incorporation of a company. Accordingly, I felt that it would be proper to write to you to inform you of this proposal as Chase would welcome your comments on the principles involved in these types of arrangements.

Yours sincerely,

I.C. James

I. C. James, Esq.,
Mourant du Feu & Jeune,
18, Grenville Street,
St. Helier,
Jersey.

ICJ/50/275/6

RCAS/smb/G.24

29th April, 1986

Dear Ian,

Thank you for your letter of 24th April, 1986 regarding the fact that Chase Bank & Trust Company (C.I.) Limited are considering promoting special purpose vehicles for use in particular banking transactions. We have read this with interest and cannot foresee any special difficulties in the structure envisaged.

I would imagine that the companies would only be incorporated for specific transactions and I think it would be useful if the Control of Borrowing application form identified these vehicles at the time of incorporation and gave a brief summary of the anticipated transaction and a note of the person or company for whose benefit the entity will operate.

If you or your client would wish to discuss any particular cases with us in advance of incorporation, we shall be only to happy to assist.

Yours sincerely,

R. C. A. Syvret
Commercial Relations Officer

34768

THE COMPANIES (JERSEY) LAWS 1861–1968
APPLICATION FOR COMPANY NAME

12. MAY 1986
RECEIVED

Proposed Name of Company (and alternatives in order of preference).

EASTMOSS LIMITED

still on index

If change of name, indicate present name of company and reason for change.

Significance of name (if any). If name is similar to existing company, give details, i.e. name and place of registration, and connection with that company.

None
(To replace 00004)

Principal activities of Company.

Investment / Trading

OFFICE APPLYING Mourant du Feu & Jeune Tel. No. 74363

OFFICE REFERENCE JEY Date 12-5-86

Commercial Relations Department

Office use only

Index checked by:

03101

replaces 004

Reserved

Refused

C.R.O. (any special conditions)

COMMERCIAL RELATIONS
13 MAY 1986
RESERVED

O. Moon
de C. Mourant
S. Baker
F. V. Jeune
E. Coutanche
C. James
R. Binnington
D. P. Crill
J. Herbert

Consultants
J. de. C. Mourant
A. R. du Feu
J. R. Jeune, O.B.E.

Mourant du Feu & Jeune
Advocates, Solicitors and Notaries Public
P.O. Box 87, 18 Grenville Street, St Helier,
Jersey, Channel Islands

Telephone (0534) 74343
Telex 4192064
Telecopier (0534) 79064

Our Ref: ICJ/nf

M.D. Fox, Esq.,
Assistant Commercial Relations Officer
Commercial Relations Department,
Cyril Le Marquand House,
The Parade,
St. Helier,
Jersey, C.I.

COMMERCIAL RELATIONS
19 MAY 1986
RECEIVED

19th May, 1986

Dear Michael,

Eastmoss Limited

Further to our application to incorporate an investment holding company to be called Eastmoss Limited I am writing to give you some further details of the reasons for its incorporation and the activities in which it will participate. By way of background I should mention that I wrote to Richard Syvret on 24th April, 1986 regarding this general type of transaction for Chase and in his letter of 29th April under reference RCAS/smb/G24 he confirmed that he saw no special difficulties with the proposed structure but requested that at the time of incorporation:-

(1) we indentify any vehicle which is being incorporated for such a transaction;
(2) we give a brief summary of the anticipated transaction; and
(3) we give details of the person or company for whose benefit the entity will operate.

I should begin by mentioning that although this particular transaction is a part of a Chase scheme, for various reasons, one of my firm's trust companies will in fact be acting as trustee of the charitable trust and will be administering Eastmoss Limited.

The transaction is as follows:-

1. A Bidder wishes to make a bid for a U.K. Company during this week but faces a problem with the bid as the Bidder and a subsidiary ("Canco") of the Target company would control a significant percentage of the U.K. market in a particular sector.

Feu & Jeune

COMMERCIAL RELATIONS
19 MAY 1986
RECEIVED

M.D. Fox, Esq.
19th May, 1986

2. The Bidder therefore must be able to confirm to the U.K. Office of Fair Trading that it has entered into an agreement with an independent third party to sell Canco subject to the bid succeeding.

3. There are two alternatives open to the Bidder namely:

   (a) sell Canco at an undervalue now; or

   (b) agree to sell Canco to a U.K. Company ("Xco") for a consideration which will largely be a deferred price based on the eventual sale proceeds of Canco to a third party over the next 3 to 6 months. The proposal is that Xco would be owned 19.9% by a Chase nominee company and 80.1% by Eastmoss Limited.

   In other words by this second route in the event of the bid succeeding the Bidder would be able immediately to divorce itself from Canco whilst retaining the benefit of its ultimate sale proceeds.

4. The Bidder wishes to keep its options open to the last moment and so Eastmoss is to be incorporated although it may not actually participate in this transaction, if the Bidder decides to sell Canco at an undervalue.

For obvious reasons this is the extent of the information that I can give you at this stage. Once the bid is public I will of course write to you again to confirm whether or not Eastmoss has participated and, if it has, to give you details of the Bidder, the Target, Canco and XCo.

This matter is very urgent as the structure must be in place by this Tuesday evening so that the formal offer may be made on Wednesday morning.

Please let me know if you require any further information.

Yours sincerely,

I.C. James

Mourant du Feu & Jeune
Advocates, Solicitors and Notaries Public
P.O. Box 87, 18 Grenville Street, St Helier,
Jersey, Channel Islands

Telephone (0534) 74343
Telex 4192064
Telecopier (0534) 79064

Consultants
H. de. C. Mourant
C. A. R. du Feu
R. R. Jeune, O.B.E.

Our Ref: ICJ/8320/2/7

M.D. Fox, Esq.,
Assistant Commercial Relations Officer,
Commercial Relations Department,
Cyril Le Marquand House,
The Parade,
St. Helier,
Jersey, C.I.

29th May, 1986

Dear Michael,

Eastmoss Limited

I should begin by thanking you and your department for the speed with which Eastmoss was incorporated. This was very much appreciated not only by this firm, but also by Chase and the other participants in the transaction which for reasons which I shall explain later in this letter, was abortive, but nevertheless was highly successful from the point of view of Chase and its ultimate client. The role of the Island in achieving this was crucial and the fact that we were able to incorporate the company in this very short time scale has, in my view, enhanced Jersey's reputation with the various professionals involved in this transaction.

I undertook in my letter to you of 19th May that as soon as the matter became public I would write to you to give you full details of the various participants.

The participants were as follows:-

Bidder	Dixons
Target	Woolworths
Canco	Comet
XCo	Teak Investments Limited (a Coward Chance U.K. shelf Company)

The position was that Chase were aware that Dixons had been negotiating with a third party, who has now been identified as Granada, regarding the sale of Comet should Dixons' acquisition of Woolworths prove successful. In view of the complexities of the situation it is not surprising that Granada's initial offers were significantly below the actual market value of Comet and both from the commercial point of view and from the fact that this could give rise to unfavourable publicity which would not assist Dixons in the midst of a contested takeover, it was felt by Dixons and their advisers, S.G. Warburg & Co., that Dixons could not accept this initial offer. Accordingly Chase were approached with the suggestion that they should fund Xco which would thereupon agree to purchase Comet at a price determined by the actual sale proceeds of Comet to a third party in the months following a successful takeover of Woolworths by Dixons.

For U.S. regulatory reasons Chase were then advised that they could not have either the ownership or the control of Xco and so the Jersey structure outlined in my letter to you was proposed. In order that the U.S. authorities could be entirely satisfied with the arrangements it was considered preferable that my firm's trust company should act as trustee of the charitable trust and administer Eastmoss rather than Chase Jersey.

In the event, at 4 a.m. on Thursday 19th May Xco was able to make a formal offer for the purchase of Comet. Apparently, in the light of this 'market-value' offer, the discussions between Dixons and Granada intensified. At 9 a.m. on that morning it was announced that Granada had agreed to acquire Comet, provided that Dixons' bid for Woolworths was successful, on terms which were acceptable to Dixons and significantly higher than the original offer. The result was therefore highly satisfactory both for Chase and its client, Dixons, even though the Xco offer was not accepted.

I think that I should also mention that Eastmoss Limited was only entering into this transaction on the basis that it would have made a profit pro rata to the amount of the Comet sale price. Thus if Comet had ultimately been sold to a third party for the same price as that paid by Granada, Eastmoss would have made a net profit of approximately £40,000 which would have been available to be distributed to the Trustees of the Charitable Trust for them to apply for charitable purposes.

I am raising with Chase the question of whether Eastmoss Limited should now be dissolved but I understand that there is a possibility that it will be used in an alternative transaction provided that your

department is agreeable. I am obtaining details of this transaction and I will write to you with these if it appears that Eastmoss Limited is to be involved.

Please let me know if you require any further information.

Yours sincerely,

I.C. James

STATES OF JERSEY

Application for consent to issue shares in a proposed Jersey Company (made pursuant to the provisions of the Control of Borrowing (Jersey) Order, 1958, as amended).

Notes: Refer to page 3 for instructions on the completion of this form.
Information contained in Parts I and II will be supplied to the Comptroller of Income Tax.

FOR OFFICIAL USE ONL

PART I – DETAILS OF PROPOSED COMPANY.

A

1. Name of proposed company and reference Number of the provisional Name: CP 7606
MAHONIA LIMITED — 54172

B

2. Principal objects of the company:–
FINANCE COMPANY

C

3. Details of share capital: (State amount of authorised capital and no. and par value of shares).
10,000 shares of £1 each — 27

D

4. Full names of Founder members:
JURIS LIMITED
LIVELY LIMITED

E

F

5. Is the company to be "exempt" for Jersey Income Tax purposes? YES/~~NO~~*

6. (a) Will any additional owners be introduced within six months of incorporation? ~~YES~~/NO*

(b) Will any shares or other securities in this Company be offered to the public at any time? (See Note 6.) ~~YES~~/NO*

If the answer to either question is "YES", please give relevant details in Parts II and/or III, or by separate letter. *Delete as appropriate.

G

Note: Before completing Parts II and/or III, please read Notes 2 and 10 on Page 3 of this form.

16/12/92

PART II – DETAILS OF BENEFICIAL OWNERS RESIDENT IN JERSEY.

7. State the full name(s) and full residential address(es) of the ultimate beneficial owners of the shares in the proposed company (Refer to Notes 3 and 10).
Mourant & Co. Trustees Limited as Trustees of
The Eastmoss Trust, a wholly charitable trust
established by declaration of trust.

J

K

8. If any of the applicants are or have been a beneficial owner of any other Jersey companies, give names and registered numbers of all such companies. See Note 3(c).
Kindly refer to attached schedule

...lication for consent to issue shares. 54172 Page two

...fer to page 3 for instructions on the completion of this form | FOR OFFICIAL USE ONL

PART III – DETAILS OF BENEFICIAL OWNERS RESIDENT ELSEWHERE

9. State the full name(s), occupation, and address(es) of the ultimate beneficial owners of the shares in the proposed company (Refer to Note 3).

.....

.....

.....

.....

10. If any of the applicants are or have been a beneficial owner of any other Jersey company, give names and registered numbers of all such companies. See note 3(d).

.....

.....

.....

PART IV – GENERAL

11. Explain fully why the company is being incorporated in Jersey, giving details of its proposed activities. See note 4.

To assist in transactions arranged by Chase Bank

.....

.....

.....

.....

12. Has a licence been granted under Part II of the Regulation of Undertakings and Development Law? (See note 7). ~~YES~~ / No* Licence No.: .....

13. If the share capital is to be issued at a premium on incorporation or in the future, please give full details, or if Control of Borrowing consent is required in respect of the issue of any other securities, please give full details.

.....

.....

.....

14. Confirm that none of the beneficial owners, the Settlor or named beneficiaries has in any part of the world been declared bankrupt or 'en desastre' or been a Director of, or otherwise concerned in the management of, a company which has been subject to an insolvent liquidation or been the subject of a Judicial enquiry. (If such confirmation cannot be given, give full details by covering letter) Confirmed

.....

I DECLARE THAT THE ABOVE PARTICULARS, AND INFORMATION GIVEN IN ANY ATTACHED LETTER, ARE TRUE TO THE BEST OF MY KNOWLEDGE AND BELIEF, AND THAT I AM AWARE OF THE PENALTIES CONTAINED IN THE BORROWING (CONTROL) (JERSEY) LAW, 1947, AS AMENDED, FOR PROVIDING FALSE INFORMATION.

Date 15th December 1992 Signed .....
(See Note 9)

Mouvant du Fau & Jeune

L

M

N

O

P

Q

R

S

STATES OF JERSEY

Application for consent to issue shares in a proposed Jersey Company (made pursuant to the provisions of the Control of Borrowing (Jersey) Order, 1958, as amended).

Notes: Refer to page 3 for instructions on the completion of this form.
Information contained in Parts I and II will be supplied to the Comptroller of Income Tax.

FOR OFFICIAL USE ONLY

PART I – DETAILS OF PROPOSED COMPANY.

1. Name of proposed company and reference Number of the provisional Name: CP .....
STONEVILLE AEGEAN ..... LIMITED.

2. Principal objects of the company:– .....
TO ISSUE NOTES .....

3. Details of share capital: (State amount of authorised capital and no. and par value of shares).
10,000 of £1 each .....

4. Full names of Founder members: .....
MOURANT & CO. SECRETARIES LIMITED .....
JURIS LIMITED .....
LIVELY LIMITED .....
.....

5. Is the company to be "exempt" for Jersey Income Tax purposes? YES/~~NO*~~

6. (a) Will any additional owners be introduced within six months of incorporation? ~~YES~~/NO*

(b) Will any shares or other securities in this Company be offered to the public at any time? (See Note 5.) ~~YES~~/NO*

If the answer to either question is "YES", please give relevant details in Parts II and/or III, or by separate letter. *Delete as appropriate.

Note: Before completing Parts II and/or III, please read Notes 2 and 9 on Page 3 of this form.

PART II – DETAILS OF BENEFICIAL OWNERS RESIDENT IN THE BRITISH ISLES.
(For definition – See note 2)

7. State the full name(s) and full residential address(es) of the ultimate beneficial owners of the shares in the proposed company (Refer to Notes 3 and 9).

Mourant & Co. Trustees Limited as Trustees of the Eastmoss Trust
a wholly charitable trust created by declaration of trust.
RC 43164/4827P
Senior Chase Bank RC 48819/4890
RC 44563/4
RC 44443/44

8. If any of the beneficial owners named in this application have, or have had 25% or more beneficial interest in the shares of any other Jersey companies, give names and registered numbers of all such companies. See Note 3(d).

Kindly refer to attached schedule.

Application for consent to issue shares. 44747 Page two

Refer to page 3 for instructions on the completion of this form | FOR OFFICIAL USE ONLY

PART III – DETAILS OF BENEFICIAL OWNERS RESIDENT ELSEWHERE

9. State the full name(s), and town and country of residence of the ultimate beneficial owners of the shares in the proposed company (Refer to Note 3)

.....

.....

.....

.....

L

M

N

10. If any of the beneficial owners named in this application have, or have had 25% or more beneficial interest in the shares of any other Jersey companies, give names and registered numbers of all such companies. See note 3(d).

.....

.....

PART IV – GENERAL

11. Explain fully why the company is being incorporated in Jersey, giving details of its proposed activities. Separate more comprehensive information is required if the company, or an associated company thereof, is to provide any services connected with or relating to banking, deposit taking, insurance, investment or finance for persons other than those disclosed in replies to questions 7 and 9 above.

...TO ISSUE NOTES AND TO FINANCE TRANSACTIONS ARRANGED BY.....

...CHASE BANK.....

.....

.....

O

12. Has an application been made for a licence under Part II of the Regulation of Undertakings and Development Law? ~~YES~~/NO* Licence No .....

P

13. If the share capital is to be issued at a premium on incorporation or in the future, please give full details, or if Control of Borrowing consent is required in respect of the issue of any other securities, please give full details. (See also Note 6).

.....

.....

.....

Q

R

S

14. Confirm that none of the beneficial owners, the Settlor or named beneficiaries has in any part of the world been declared bankrupt or 'en desastre' or been a Director of, or otherwise concerned in the management of, a company which has been subject to an insolvent liquidation or been the subject of a Judicial enquiry. (If such confirmation cannot be given, give full details by covering letter).

.....CONFIRMED.....

I DECLARE THAT THE ABOVE PARTICULARS, AND INFORMATION GIVEN IN ANY ATTACHED LETTER, ARE TRUE TO THE BEST OF MY KNOWLEDGE AND BELIEF, AND THAT I AM AWARE OF THE PENALTIES CONTAINED IN THE BORROWING (CONTROL) (JERSEY) LAW, 1947, AS AMENDED, FOR PROVIDING FALSE INFORMATION.

Date 14th July 1989 Signed T.J. Herbert

(See Note 8)

CHASE BANK

JERSEY REGISTERED COMPANIES OWNED BY THE TRUSTEES OF THE EASTMOSS TRUST

EASTMOSS LIMITED	34768
DALEBURY LIMITED	38317
RUBYDOWN FINANCE LIMITED	41044
STONEVILLE ONTARIO FINANCE LIMITED	41010
STONEVILLE MICHIGAN FINANCE LIMITED	41009
STONEVILLE TOPAZ LIMITED	41300
STONEVILLE HURON LIMITED	41301
STONEVILLE ATLANTIC LIMITED	41648
STONEVILLE CASPIAN LIMITED	43164
STONEVILLE SUPERIOR LIMITED	43278
STONEVILLE BALTIC LIMITED	43819
STONEVILLE JAVA LIMITED	43890
STONEVILLE MARMARA LIMITED	44443
STONEVILLE ADRIATIC LIMITED	44444
STONEVILLE TIMOR LIMITED	44563
STONEVILLE CORAL LIMITED	44564
STONEVILLE AEGEAN LIMITED	44747
STONEVILLE KARA LIMITED	45573
GOTHIA FINANCE LIMITED	47355
GRAPHICS FINANCING (JERSEY) LIMITED	47987
TAVON LIMITED	48067
GOLDVALE FINANCE LIMITED	48068
SHONDUS LIMITED	48529
SPARTAN LIMITED	49220
WELLSGATE LIMITED	49735
TUNWELL LIMITED	51426
CIDERFORD LIMITED	51769

Mourant du Feu & Jeune
ADVOCATES, SOLICITORS AND NOTARIES PUBLIC

PO Box 87
22 Grenville Street
St Helier
Jersey JE4 8PX
Channel Islands

Tel: 01534 609000
Fax: 01534 609333
International
Tel: +44 1534 609000
Fax: +44 1534 609333
www.mourant.com

Direct Dial 01534 609335

COBO

Jersey Financial Services Commission
Nelson House
David Place
St Helier
Jersey JE4 8TP

19 November 1999

Our ref: ICJ/8276/1/1395490

Dear Sirs

Mahonia II Limited (the *Company*)

We attach the incorporation papers for the Company that will be wholly owned by Mourant & Co. Trustees Limited as trustees of the Eastmoss Trust.

This Company will be invited from time to time to enter into arrangements that will assist The Chase Manhattan Bank in providing finance for major US Oil and Gas companies. The arrangements in each case will involve the Company entering into a Forward Purchase Contract with a US Oil or Gas company to purchase its forward inventory of Oil or Gas, as the case may be. The Company will also at the same time enter into a Forward Sale Contract with Chase to sell the inventory of Oil or Gas that it will be acquiring from the US Oil or Gas Company. The arrangements with Chase will be such that the Company's obligations to Chase will be limited in recourse to the benefits which it receives from the relevant US Oil or Gas company under the respective Forward Purchase Agreement. The overall effect of these arrangements will be that Chase will be providing finance to the relevant US Oil or Gas company on the security of the inventory of Oil or Gas but without the Company taking any exposure to the Oil and Gas market. Chase will act as the Company's agent in monitoring the making and receipt of all payments to and from the US Oil or Gas Company and the delivery and receipt of Oil and Gas by the Company.

The first transaction proposed for this Company will be with Columbia Natural Resources Inc, a subsidiary of the Columbia Energy Group, and will involve the Company agreeing to purchase Natural Gas from it.

The directors of the Company will be provided by this firm.

P de C Mourant, R F V Jeune, C E Coutanche, I C James, A R Binnington, J D P Crill, T J Herbert, J A Richomme, E A Breen, C L i Davies, N C Davies, A J R Syvret, E C Devenport, J P Speck, B H Lacey, M R Scott, J A J Chapman, J C Walker

Associates: N M Hamel, G A Pollano, S M Gould, W Malorey, D R Wilson, N J D Chapman, R A Hickling
Consultants: R R Jeune C B E, K S Baker

Please do not hesitate to contact me if I can provide any further information in order to complete the incorporation of the proposed Company.

Yours faithfully

Ian James

M

From: Ian James
To: Gareth EssexCater
Date: 26/11/01 13:46:09
Subject: Re: Mahonia et al - Enron trades

Thanks for the information. I have no comments.

>>> Gareth EssexCater 26/11/2001 12:26:11 >>>
Ian - regarding the e-mails sent to you overnight from JPM New York requesting that each of the Mahonia vehicles execute POA in favour of JPM I have spoken to Jeff Dellapina this morning.

JPM believe Enron are close to defaulting on their forward sale contract obligations. A credit rating downgrade is expected which will trigger all sorts of margin calls and, Jeff believes, the default. They are, in Jeff's words, in the grip of a 'pretty good meltdown'.

The purpose of the POA is to empower JPM to act on behalf of the various SPV's and take the various action that will need to be taken in relation to the contracts (and in particular of course the collateral) if the default becomse a reality.

Jeff stressed the urgency of this as you can imagine. I am arranging board meetings today - please can you let me know if you have any immediate comments. I am looking at the contracts to see what the practical effect of a default will be for the SPV's.

Gareth

Permanent Subcommittee on Investigations
EXHIBIT #119

Julie Carter

From: Ian James
Sent: 04 March 2002 13:45
To: Julie Carter
Subject: RE: mahonia pipeline imbalances

Ok

-----Original Message-----
From: Julie Carter
Sent: 28 February 2002 16:17
To: Ian James
Cc: Gareth EssexCater
Subject: FW: mahonia pipeline imbalances

Ian

Further to the request below Greg has just called to advise that JPMorgan as Agents have arranged to settle the invoice and that they do not need our instruction.

He has also advised that they have just discovered anomalies in the Texas Eastern Pipeline agreements in respect to certain trades (Occidental and also Enron 98) whereby the pipeline agreements are made directly between the providers and JP Morgan, effectively bypassing Mahonia. Accordingly new pipeline agreements need to be completed reflecting the providers delivering to Mahonia who then in turn deliver to JP Morgan. He will forward the paperwork to me by fax and would be grateful if the directors would consider execution as soon as possible.

If you require further information in this respect he is happy for you to call either himself (00 1 212 834 4286) and\or Phil Levy for more background.

In addition he advised that Mahonia II is due to start receiving and delivering gas shortly and accordingly new pipeline agreements will need to be put in place for that company.

In addition, should I inform Jonathan Cotton of Slaughter & May of these conversations and copy him in on all paperwork in this respect as he has requested?

Kind regards

Julie

-----Original Message-----
From: Julie Carter
Sent: 19 February 2002 14:18
To: 'GREGORY.CROWLEY@jpmorgan.com'
Cc: Ian James; jonathan. cotton@slaughterandmay. com (E-mail)
Subject: RE: mahonia pipeline imbalances

Dear Gregory

The Directors are in the process of preparing the request for JPMorganChase as Agent to settle the invoice in question.

To enable them to finalise that request would you, as Agents, kindly confirm to which trade the invoice relates.

Kind regards

Yours sincerely
For and on behalf of Mourant & Co. Secretaries Limited

Julie Carter

Permanent Subcommittee on Investigations
EXHIBIT #120

Richard S Walker
07/17/2000 09 23 AM

To Robert Traband/CHASE@CHASE
cc
Subject Re Restructuring existing prepays

Rob -

FYI - you'll see that Jeff D. is working on this situation
----- Forwarded by Richard S Walker/CHASE on 07/17/2000 09 19 AM -----

Jeffrey W Dellapina
07/17/2000 07 24 AM

To Davis_Thames@enron net, Joseph_Deffner@ECT enron net, Brian_Kerrigan@ECT enron net
cc Gregory Crowley/CHASE@CHASE, Richard S Walker/CHASE@CHASE
Subject Re Restructuring existing prepays

Look forward to discussing this morning. (**Brian.** Rick called me over the weekend - I'll be available to assist.)

Some background and addit'l thoughts.

- several months ago we realised that the Mahonia margin calls had not been made and when these commenced, I began discussions with several individuals at Enron. I'm well aware that Enron was working on a proposal; howeve, I thought that the margin was being posted in the meantime.
- given the nature of these transactions, which involve a notionally equal swap where Enron pays fixed and Chase pays floating, Chase is currently posting huge margin with Enron NA. This collateral is likely in the form of Treasuries
- Is it also worth considering the following solution: Grant Enron the right to re-hypothecate these Treasuries (I have not yet cleared this with legal nor have I checked our Master with you.)

Let's discuss

Davis_Thames@enron net on 07/14/2000 07:20:11 PM

Davis Thames@enron.net on 07/14/2000 07:20:11 PM

To Jeffrey W Dellapina/CHASE@CHASE, Gregory Crowley/CHASE@CHASE

Permanent Subcommittee on Investigations
EXHIBIT #121

SENATE
MAH - 02500

FOIA Confidential Treatment
Requested by JPMC

Julie Carter

From: Julie Carter
Sent: 24 September 2001 15:24
To: Levy@Philip
Subject: RE: Prepay Docs

Phil

Thanks for forwarding these documents.

Just to let you know, we will not have any partners in the office on Friday afternoon as they will all be attending the partners six-monthly meeting.

Kind regards

Yours sincerely
For and on behalf of
Mourant & Co. Secretaries Limited

Julie Carter

>>> <Philip.Levy@chase.com> 24 September 2001 >>>
"Julie-

Following is a communication from Enron with respect to a new transaction that they would like to close this week. Unlike the prior prepay transactions which resulted in physical delivery of natural gas, this transaction will be documented as a cash-settled prepaid swap under ISDA documentation. Under this scenario, Mahonia will make an upfront payment (much like in the standard prepay) but, instead of receiving specified quantities of natural gas over time, Enron will pay cash to Mahonia (which will, in turn, make payment to Chase under a swap transaction with Chase, which transaction will also put Mahonia in funds to make its payment to Enron.)

I am in the process of reviewing the enclosed documents and will provide comments on Mahonia's behalf to Enron. I believe that all the ancillary documentation between Mahonia and Enron typically provided in the physical prepay transactions will be necessary here as well (Board resolutions, minutes, legal opinions, etc.).

I also want to apologize for the delay in resolving the account issues you have raised. It is my understanding that Jeff and Mike are following up on the matter and will respond to you shortly. It is my further understanding that the back office is retrieving the Crystal confirms you requested and will forward them shortly.

Please feel free to contact me should you have any questions. Thank you for your patience and cooperation.

Phil.

---------- Forwarded by Philip Levy/CHASE on 09/24/2001 10:07 AM ----------

"Koehler, Anne C." <Anne.C.Koehler@ENRON.com> on 09/23/2001 07:20:08 PM

To: Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, Philip Levy/CHASE@CHASE
cc: "Garberding, Michael" <Michael.Garberding@ENRON.com>, "Bills, Lisa" <Lisa.Bills@ENRON.com>, "Moon, Eric" <Eric.Moon@ENRON.com>, "Boyt, Eric" <Eric.Boyt@ENRON.com>, "Quaintance Jr., Alan" <Alan.Quaintance_Jr@ENRON.com>, "Clark, Catherine" <Catherine.Clark@ENRON.com>, "Blumenthal, Jeff" <Jeff.Blumenthal@ENRON.com>
Subject: RE: Prepay Docs

Attached hereto are first drafts of the form of swap documents we propose to use in connection with the prepay transaction with Chase and Mahonia. Since we do not have a Master ISDA in place with Mahonia, I have drafted the ENA/Mahonia confirmation in the form of a "deemed ISDA".

FOIA Confidential

Permanent Subcommittee on Investigations
EXHIBIT #122

SENATE
MAH - 00912

George Serice 11/25/1998 10:01 AM

Global Syndicated Finance 713-216-8079 Fax Number: 713-216-2339

To: Karen Simon/CHASE@CHASE
cc: Jeffrey W. Dellapina/CHASE
Subject: Re: Pre-pays

Karen,

The latest developments on the famed Enron prepays is that we are no longer utilizing the bank markets to lay off the Chase risk through Performance Letters of Credit. Rather, Chase is laying-off its concentration risk through **Surety Bonds** provided by Enron's insurance companies. They get a great rate (as the insurance risk pricing is better than the PLC pricing we can get) and an ancillary benefit for Enron is to free-up precious bank capacity.

Jeff Dellapina and Bob Mertensotto worked on a deal this summer where they took out a couple of the older Prepay PLC's with these surety bonds. Jeff is also working on another prepay for Enron now. So, the last time we were actually in the market with a PLC-backed deal was quite a while back (1 year?) ... bottom line, **Jeff doesn't need me anymore.**

Enron loves these deals as they are able to **hide funded debt from their equity analysts** because they (at the very least) book it as deferred rev or (better yet) bury it in their trading liabilities. There are, however, tax attributes to the structure that can **"freshen" NOL's.** This attribute was key in a transaction which was done for Crystal Oil. Short story is that sale can accelerate gains to the year in which the prepay is consumated, which gains can be offset by (expiring) NOL's. Following years yield larger than otherwise losses, which build back "freshened" NOL's.

I am attaching the latest Prepay bank universe that I have.

bkuniv98.xls

I am also attaching the struc summ for the 98 prepay which was ultimately done with the surety bonds. I think it has some historical pricing info. Of course, all of that pricing is ancient history. I always started with a PLC fee at 75% of company's funded cost and adusted from there for size, time of year, bank capacity issues, etc.

98ssum3.doc

Take care, we're heading out to do the Thanksgiving thing this PM, so I am working from the satellite office (i.e. home) this AM.
Karen Simon

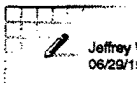
Karen Simon 11/25/98 03:10 AM

Global Syndicated Finance 44-171-777-3830 Fax Number 44-171-777-3841

To: George Serice/CHASE@CHASE
cc: David 'GSF-London' Stewart/CHASE@CHASE
Subject: Pre-pays

FOIA Confidential Treatment Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #123



Jeffrey W. Dellapina
06/29/1998 02:30 PM

To: Mark Malloy/CHASE@CHASE, Heather Lindstrom/CHASE@CHASE
cc: James M. Biello/CHASE@CHASE, Richard S. Walker/CHASE@CHASE, Philip Levy/CHASE@CHASE, Dexter Charles/CHASE@CHASE
Subject: Enron Forward Sale Transaction

This morning we closed the $250,000,000, natural gas forward sale transaction. Thanks to your assistance, we have "advanced the technology" on the prepaid commodity transactions by structuring credit enhancement in the form of surety bonds rather than bank LCs (the traditional credit support in this structure).

Is this a trend?

REDACTED

Regards and thanks again!

FOIA Confidential Treatment Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #124

Client Attendees:	Chase Attendees:	CC: List:
Joe Deffner	Richard S. Walker	Jeffrey W. Dellapina Bob Mertensotto Robert Traband Christopher Wardell Gary K. Wright Todd Maclin Dod Fraser
Level of Attendees: Asst. Treasurer, Other	Filing Officer(s): Richard S. Walker	OTC/Sr Mgmt Attendees:

Call Date: 06/11/99 Call Type: In Person

Meeting Details:
RED ALERT

Joe called to indicate that Enron would like to do a $500 MM natural gas prepay and that they would like to do it prior to June 30 !!! This is the prepay that Jeff McMahon refered to in our recent meeting and it would (a) likely be the only prepay executed for 1999 and (b) would represent the monetization of most but not all of the expect excess of assets over liabilities for price risk management.

I told Joe we would determine any capacity constraints ASAP. In this regard the prefered structrure is as follows

- Amount: $500 million
- Commodity: Natural Gas
- Tenor: 5 years (we've done one five year prepay although the last two have been 3 and 4 years)
- Average Life: 2.8 year (Deffner's estimate)
- Preferred Sureties: Liberty Mutual, St Paul, Travellers, SAFECO (ie., 4 x $125 MM each)

Jeff give me a call ASAP

Relationship Information:

Follow-Up:

Product(s) Discussed: Derivatives

Permanent Subcommittee on Investigations
EXHIBIT #125

JPMC-H 011269

Richard S. Walker
06/24/99 11:16 AM

To: Dinsa Mehta/CHASE
cc: Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, Bob Mertensotto/CHASE@CHASE
Subject: Re: Enron

Dinsa -

As discussed, the business purpose underpinning the current $500 MM prepay exercise is simply that of efficiently priced funding. From a financial statement perspective, the prepay structure serves to "monetize" the positive excess of assets for price risk management over liabilities for price risk management.

I have had this "business purpose" discussion a couple times recently - in late May we had a high level meeting with Enron's Treasurer, Jeff McMahon in which he articulated the business purpose outlined above. Chase participants in that May meeting included myself along with, Jim Biello, Chris Wardell and several others. In addition I have had a similar business purpose discussion with Joe Deffner who is the Enron finance person who is in charge of their end of the prepay execution.

Let me know if you need anything further.

Rick
Dinsa Mehta

Dinsa Mehta
06/11/99 04:10 PM

To: Richard S. Walker/CHASE@CHASE, Jeffrey W. Dellapina/CHASE@CHASE
cc:
Subject: Enron

Ric, Jeff

If Enron are contemplating a jumbo prepay I think it would be good to have a use-of-proceeds / corporate objectives type of discussion at an appropriate level. I would like to be part of this discussion. You can get hold of me in London.

Regards

Dinsa

Permanent Subcommittee on Investigations
EXHIBIT #126

Robert Traband 05/31/2000 01:38 PM

To: Jeffrey W. Dellapina/CHASE@CHASE
cc: Richard S. Walker/CHASE@CHASE
Subject: Enron

---------- Forwarded by Robert Traband/CHASE on 05/31/2000 01:40 PM ----------

Dennis Oakley 05/31/2000 12:53 PM

Global Credit Capital Management/Credit Derivatives (212) 270-9015 Fax Number (212) 270-2370

To: Robert Traband/CHASE@CHASE
cc:
Subject: Enron

Rob,

Below is the pricing of an amortizing swap As I mentioned to you on the phone its about 10-15bps above the current market for enron due to the size of the trade. The average cost is 85 bps.

		Size	Price
Year	1	750	70
	2	600	80
	3	450	90
	4	300	100
	5	150	110

Since this is a prepaid forward contract the economics work just like a loan and will attract hog share capital The risk mitgation will eliminate the that capital. The capital freed up will be over $16MM If you can give me credit spreads on the forward I can calculate a break-even for you.

regards

Dennis

Permanent Subcommittee on Investigations
EXHIBIT #127

FOIA Confidential Treatment Requested by JPMC

SENATE
MAH - 00713

William Manias
07/17/98 09:56 AM

Global Oil & Gas (713) 216-6386 Fax Number (713) 216-4227

To: Robert Traband/CHASE@CHASE
cc:
Subject: Prepay

..... Forwarded by William Manias/CHASE on 07/17/98 09:52 AM .....

07/16/98 12

Commodity Derivatives (212) 834-4284 Fax Number: (212) 834-6084

To: William Manias/CHASE@CHASE
cc: Jeffrey W. Dellapina/CHASE@CHASE
Subject: Prepay

Bill,

prepaygeneric_0798.ppt Here is a copy of the new prepay pitch. I have saved it as a 4.0 powerpoint file as I think this is the version you guys use in Texas.

Obviuosly this is p&c and not for distribution so only use for your own education.

Jeff will be back in on Friday, and you can speak with him directly regarding Coastal States.

regards,

HSC

OIA Confidential Treatment
Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #128

SENATE
MAH - 02604

FOIA Confidential Treatment
Requested by JPMC

XYZ Corporation

Presentation of:

Prepaid, Forward Sale of Inventory

16 July 1998

SENATE
MAH - 02605

FOIA Confidential Treatment
Requested by JPMC

Contents

		Page
I.	Introduction	3
II.	Transaction Attributes	4
III.	Indicative Terms & Conditions	7
IV.	Summary Diagram	12
V.	Documentation	13

SENATE
MAH - 02606

FOIA Confidential Treatment Requested by JPMC

Introduction

- Prepayment received for a forward sale of inventory: fixed quantity; specific delivery location(s)
- Alternative source of finance
- Balance sheet "friendly"
- Chase has arranged transactions totaling in excess of $2 Billion

SENATE
MAH - 02607

Transaction Attributes

- Alternative Source of Medium Term Finance
  - Transactions generally 3-5 years
  - Performance risk rather than payment risk
  - Syndication of xyx risk using non-traditional means
    - amortizing, syndicated performance LC
    - surety bonds

FOIA Confidential Treatment
Requested by JPMC

SENATE
MAH - 02608

Transaction Attributes (cont'd)

- Attractive accounting impact by converting funded debt to "deferred revenue", or long-term trade payable
- Competitive economics
  - Performance LCs draw 50% capital weighting (loans, stand-by LCs, payment guarantees are 100% weighted)
  - Insurance companies have been aggressive in other deals

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SENATE
MAH - 02609

Transaction Attributes (cont'd)

- Attendant tax benefits
- "Off-the-shelf" documents for US crude oil- and natural gas-based transactions
- Chase's working relationship with Mahonia Limited, a Jersey company active in commodity prepayments

FOIA Confidential Treatment Requested by JPMC

SENATE
MAH - 02610

FOIA Confidential Treatment Requested by JPMC

Terms and Conditions

Seller:	xyx Corporation (or designated subsidiary)
Purchaser:	Mahonia Limited (or The Chase Manhattan Bank)
Prepayment Amount:	[approximately $250,000,000]
Delivery Volume:	pre-determined volume of hydrocarbons
Delivery Period:	[5] years with a [ ] month grace period from closing
Delivery Sched:	Either (i) ratable monthly over the period, (ii) tailored to specific requirements

SENATE
MAH - 02611

FOIA Confidential Treatment
Requested by JPMC

Terms and Conditions (cont'd)

Delivery Locations:

- For WTI, Cushing Oklahoma
- For Natural Gas, various pipeline pooling locations in U.S., including:

Pipeline	Points
Transco	**Pooling points**
TX Gas	**Pooling points**
Texas Eastern	**Pooling points**
Columbia Gulf	Pooling points
El Paso	Permian pool
Henry Hub	All pipes

other arrangements, including oil cargo settlements, as agreed between Mahonia and xyx

SENATE
MAH - 02612

Terms and Conditions (cont'd)

Performance Risk Diversification:

	Alternative (1)	***Alternative (2)***
Performance L/C:	Amortizing L/C, syndicated by Chase, with an initial drawing amount equal to the natural gas delivery at closing	
L/C Drawing:	By Mahonia upon failure to deliver and make replacement payment	
Surety Bond:		Amortising surety bond issued by a number of acceptable insurance companies
Bond Drawing:		By Mahonia upon failure to deliver and make replacement payment

FOIA Confidential Treatment
Requested by JPMC

SENATE
MAH - 02613

Terms and Conditions (cont'd)

Economics:

	Alternative (1)
Discount rate:	Libor + [20] basis points
PL/C Fees:	[25] basis points per annum on outstanding
Up front fees:	[15] basis points
	Alternative (2)
Discount rate:	Libor + [20] basis points
Premium on Surety Bond:	To be agreed with insurers
Up-front fees:	[15] basis points

FOIA Confidential Treatment
Requested by JPMC

SENATE
MAH - 02614

Terms and Conditions (cont'd)

Enhancements:

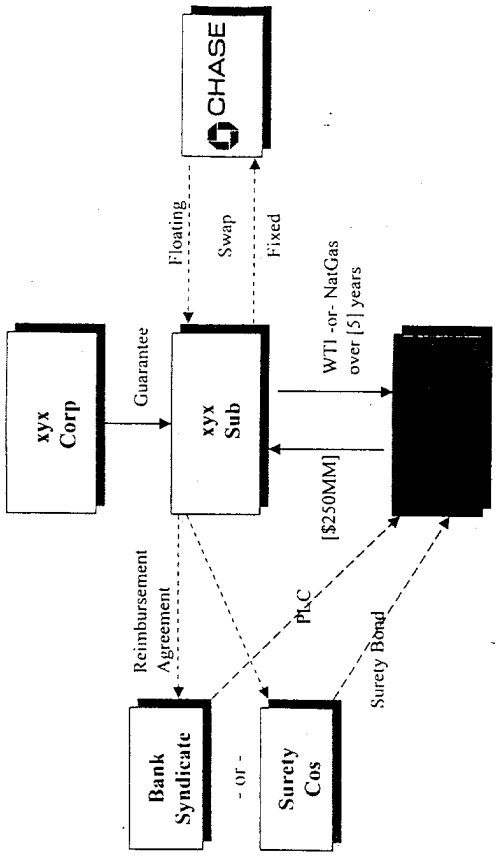
Chase can improve the economics for xyx as follows:

- Neutralize xyx's fixed price position (resulting from the forward sale) with a swap contract between Chase and xyx
- Reduce discount rates through embedded options
  - provide Mahonia option to call natural gas or crude oil
  - provide Mahonia a call on additional gas at a fixed price

FOIA Confidential Treatment
Requested by JPMC

SENATE
MAH - 02615

Summary Diagram



12

FOIA Confidential Treatment Requested by JPMC

Documentation

- Commercial forward sale agreement
- Guarantee, if necessary
- Reimbursement agreement with banks or sureties
- [Financial swap confirmation]
- Standard enforceability opinions
- Estimated legal cost (excl xyx counsel) $25,000 *
  - * Having executed US oil & gas prepays totaling $2 billion, Chase can produce "shelf" documents.

FOIA Confidential Treatment
Requested by JPMC

SENATE
MAH - 02617

Pam Collins 12/04/2000 03:57 PM

SECURITIES & SYNDICATION (713) 216-2963 Fax Number: (713 216-4583

To: Doron_sabag@sumitomobank.com
cc: (bcc: George Serice/CHASE)
Subject: FROM GEORGE SERICE

Struc Summ.doc

Permanent Subcommittee on Investigations
EXHIBIT #129

FOIA Confidential Treatment Requested

Description of Enron Prepay Transaction:

Executive Summary:

Chase is in discussions with Enron to arrange a 5-year $500MM Prepaid Gas Sale ("Prepay") for either Enron North America or Enron Natural Gas Marketing Corporation to be backed 100% by sureties. As a result of Chase's exposure to sureties and our aggregate exposure to Enron, the Prepay would be structured as a 3-way club transaction, with each bank funding $167MM. This structure calls for Enron to delivery monthly gas volumes over the 5-year term, with an initial 6 month holiday. The gas volumes are sold at a swapped price, resulting in a fixed loan amortization. The average life of the loan is approximately 3 years.

Enron Corporation will guarantee the performance under the Prepaid Transaction. The buyer of the gas will be Mahonia Limited. The primary credit exposure is to Enron given that the primary gas delivery obligation is with Enron; back-up credit protection to ensure deliveries/ performance is provided through surety bonds. Chase will also provide credit support to the structure in our position as hydrocarbon and interest rate swap counterparty to Mahonia.

In an effort to manage year-end liquidity, Enron has labeled this transaction a high priority year-end item. Further, the company has expressed that due to several large sources of cash in the 1st quarter of 2001 (Portland General, South America, large CTC (stranded cost monitization) bond offering). In the past four years, Enron has utilized the prepaid sale as a mechanism to balance Enron's book of Assets from Price Risk Management Activities versus Liabilities from Price Risk Management Activities.

This transaction is similar to the other Prepays recently put in place and will have substantially the same transaction papers. In addition, the credit enhancement via the sureties will work similar to an L/C and will provide credit support should Enron not perform the contemplated deliveries.

The proposed pricing of 25 bps upfront, 75 bps spread.

Sureties:

Thoughts are:

Travelers Indemnity Company $100-125 million
Chubb (Federal Insurance Company) $100-125 million
St. Paul Fire and Marine Insurance Company $60-90 million
Lumbermens Mutual Casualty Company (Kemper) $100 million
Safeco Insurance Company of America $50-75 million

He has also discussed with American Home Assurance Company (AIG). They have not done a private transaction of this nature. If they can underwrite this, we would expect capacity of $50-100 million.

We have also placed these types of obligations with Continental Casualty Company (CNA) on past Mahonia transactions. They only have about $75 million exposure left to runoff, and would take at least $75 million.

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Requested by JPMC

From: Bills, Lisa
Sent: Friday, September 21, 2001 8:10 PM
To: Moon, Eric; Boyt, Eric; Little, Kelli
Cc: Garberding, Michael; Kolle, Brian; Edmonds, Marcus; Clark, Catherine
Subject: RE: Chase Prepay

Upfront fee of 28.5 bps. Please be advised also that the transaction may be "early terminated" and reformulated as a physical transaction in October or November to assist with the syndication of the deal. As such, we may need to chat about the calculation methodology. My understanding is that 18 months is as long as the screens go. The documents (you should receive them Sunday afternoon) will say that Loss Value if Early Termination is prior to [2] years from "Expiry". Let me know your comments.

Finally, I have told Chase I want the docs done by Tues pm with a walk thru on Wed to allow for any changes to calculations, etc and closing and funding on Thursday. Therefore, we really need to get the calculations done (into docs) by Monday pm so they can go to Chase for review. I will be speaking with Chase on Monday am and will ask Eric B to participate to insure both parties are on same page.

Thanks, Lisa

-----Original Message-----
From: Clark, Catherine
Sent: Friday, September 21, 2001 7:10 PM
To: Moon, Eric; Boyt, Eric; Little, Kelli
Cc: Garberding, Michael; Kolle, Brian; Bills, Lisa; Edmonds, Marcus
Subject: Chase Prepay

Eric, Eric and Kelli,
I'm attaching the prepay model with the updated pricing information from Chase (87.5 basis points over LIBOR). Per my conversation with the Erics and discussions with Chase, here is our timeline:

1) Monday - finalize model

-- We need your input on the amortization schedule. Arthur Andersen does not want a bullet payment at the end, and we prefer to weight the payments toward the end of the term rather than have straight-line amortization (less cash out the door in the early months). We need your help to come up with a custom amortization schedule/volume schedule that looks like a "normal commodity swap".
-- Lets try and meet Monday to go over the model (maybe early afternoon?)

2) Tuesday - finalize documents

-- Eric M., when you mentioned the "margining issue", I'm assuming you meant the provision in the documents that allows Chase to not post margin unless they receive margin. This language won't be in the latest draft of the documents, since it is a negotiating point we will give them in return for something else. We'll make sure you get a copy of the docs on Monday.
-- The Erics mentioned they planned to book the swaps on Tuesday to make sure there were no issues.

3) Thursday - closing and funding

Please let me know if there are any issues I'm missing. Thank you all for your help,
-Catherine
x3-9943

<< File: Chase Model 9-18v2.xls >>

Permanent Subcommittee on Investigations
EXHIBIT #130

Jeffrey W. Dellapina
09/26/2001 02:36 PM

To: Michael Sabloff/CHASE@Chase
cc:
Subject: Prepay

---------- Forwarded by Jeffrey W Dellapina/CHASE on 09/26/2001 02:38 PM ----------

"Garberding, Michael" <Michael.Garberding@ENRON.com> on 09/26/2001 02:24:41 PM

To: Jeffrey W. Dellapina/CHASE@CHASE
cc:
Subject: Prepay

Jeff --

Revised structure based on our tax issue (i.e., cash flows of trade have to be within a 180-day time period so settlement is on March 25 and payment on March 26). This only affected the Fixed Price 2 within the transaction structure. With regard to the embedded libor issue in the structure, it might make sense to have our interest rate desks just agree on a six-month forward price rather than entering into a trade (as will be unwound in the future). Let me know your thoughts. Thanks again.

<<Chase $350 9-26-01.ppt>>

Michael Garberding
Enron Americas Global Finance
Work: (713) 853-1864
Fax: (713) 646-3602
E-mail: michael.garberding@enron.com

****
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****

- Chase $350 9-26-01.ppt

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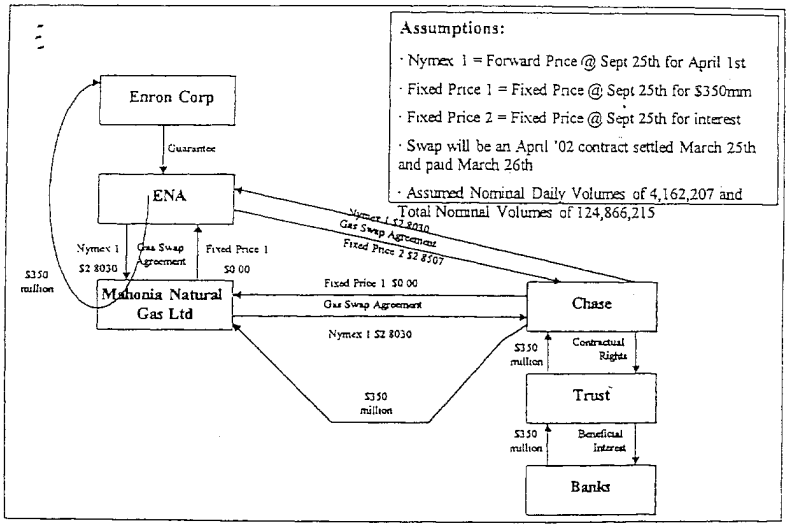
Permanent Subcommittee on Investigations
EXHIBIT #131

SENATE

Chase $350 Million Prepay



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Richard S. Walker
10/24/2001 08:32 PM

To: George Serice/CHASE@CHASE
cc:
Subject: Re: Enron

shutup and delete this email
George Serice

George Serice
10/24/2001 07:26 PM

JP Morgan Global Syndicated Finance, George.Serice@JPMChase.com 713-216-8079 Fax Number: 713-216-4583
To: Richard S. Walker/CHASE
cc:
Subject: Enron

$58 in prepays!!!!!!!!!!!!!!

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Permanent Subcommittee on Investigations
EXHIBIT #132

0329

SENATE
MAH - 00645

Andrew Threadgold@JPMORGAN
11/27/2001 10:14 AM

ARCHIVED

To: Marc Shapiro/CHASE@CHASE
cc: Lesley Danielswebster/Chase@Chase, Suzanne Hammett/Chase@Chase, James M. Biello/Chase@Chase, James Ballentine/CHASE@CHASE
Subject: Re: Enron Exposure

Marc,

The $500mm we owe Enron was a previous day's number ... subsequently updated to the $353mm mentioned below.

After adjustment for excess collateral posted by us and inclusion of "indirect deals", they owe us approximately $206mm.

Total net exposure (after securities collateral, surety bonds and letters of credit) .... is $1070mm ... per the third attachment
Surety bonds now $936mm; L/Cs now $313mm so Gross (after securities collateral) is $2339

Jim Ballentine is reviewing all numbers for accuracy.

Andrew

Marc Shapiro@CHASE

Marc Shapiro@CHASE 11/27/2001 08:25

To: Andrew Threadgold@JPMORGAN, Lesley DanielsWebster/CHASE@CHASE, Suzanne Hammett/CHASE@CHASE, James M. Biello/CHASE@CHASE
cc:
Subject: Re: Enron Exposure

Still hard for me to get a fix on this. At yesterday's meeting, Lesley said that we owed Enron $500mm in trading books. If we had to answer the question today of what is our exposure, in total both from trading and loans, and what is our loss potential, how would we answer it?
Andrew Threadgold@JPMORGAN

Andrew Threadgold@JPMORGAN
11/26/2001 07:25 PM

ARCHIVED

To: (see below)
Subject: Enron Exposure

During today's Large Exposures Meeting I indicated that the mark-to-market on derivatives with Enron was such that they owed money to us ($353mm). While this particular figure is accurate, it represents only part of the the story and is therefore misleading:

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EXHIBIT #133

SENATE
MAH - 00004

1. It does not include risks associated with the so called "Prepaid Forward" trades which while technically between Enron
and SPVs sponsored by JPMC are economically JPMC risk.

2. It ignores the collateral we have posted against the mtm
A more accurate (conservative?) number is that we are owed around $206mm .. the attached spreadsheet shows the details: Enron Derivatives Detail.

(Deals diagrams Enron Diagram.p NB some of the SPV deals may be with ENAC .. double checking)

This number is then incorporated into the overall Enron exposure Enron Exposure.xl

Notes:

1. All figures as at Monday open -- before any collateral calls settled or moneys received (could reduce risk by $150mm)
2. Possible double count in some derivative figures + some exposures may have amortized.
3. Contingent exposure to surety and l/c providers of up to $1278mm needs follow up.
4. Repos and securities settlement exposures not shown (former reportedly well collateralized).
5. FX settlement lines of $465mm not shown ... large settlements ($500mm?) due on November 30th
6. Collateral agreements assumed to require daily calls ... to be confirmed

Andrew

Ps. Thanks to the cc's for help in piecing together all this information.

To: Don Layton/Chase @Chase
Marc Shapiro/Chase @Chase
Suzanne Hammett/Chase @Chase
Lesley Danielswebster/Chase @Chase
David Pflug/Chase @Chase
James M. Biello/Chase @Chase

cc: Gary Smeal/Chase @Chase
Piers Murray @Jpmorgan
Vivian Shelton/Chase @Chase
John Duddy/Chase @Chase
Edward R Kastl @Jpmorgan
Karl Obey/Chase @Chase

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by JPMC

Ahuva Genack
Vice President and
Assistant General Counsel
Legal Department

July 18, 2002

By Facsimile Transmission

Robert L. Roach, Esq.
Counsel & Chief Investigator
Permanent Subcommittee on Investigations
United States Senate
199 Russell Building
Washington, DC 20510

Dear Mr. Roach:

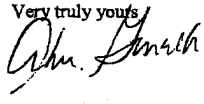
I am writing in response to the Subcommittee's subpoena dated July 2, 2002.

The names of J.P. Morgan Chase & Co. ("JPMC") clients or counterparties that engaged in commodity prepaid forward transactions with a special purpose vehicle ("SPV"), the identity of the SPV, the number of transaction that each entity entered into with the SPV, and whether the entity entered into a swap with JPMC are as follows:

Client	Number of Responsive Transactions	SPV	Swap w/JPMC For Equal or Partial Volumes
Columbia Natural Resources Inc.	2	Mahonia II, Ltd.	No
Crystal Oil Company	1	Mahonia Ltd.	No
Metallgesellschaft Corp.	1	Mahonia Ltd.	Yes
Occidental Petroleum Company	1	Mahonia Ltd.	Yes
Ocean Energy Inc.	1	Mahonia Ltd.	No
Santa Fe Snyder Corp.	2	Mahonia Ltd.	No
Tom Brown Inc.	1	Mahonia Ltd.	No

This response is based on information currently available. Should we determine that there are any additional clients or counterparties that entered into transactions described in the subpoena we will so notify you.

Very truly yours,



AG:mh

J.P. Morgan Chase & Co. - One Chase Manhattan Plaza, Floor 26, New York, NY 10081
Telephone: 212 552 0918 - Facsimile: 212 552 1295
ahuva.genack@chase.com

103288:v01

Permanent Subcommittee on Investigations
EXHIBIT #134

SECURITY AGREEMENT

between

MAHONIA LIMITED

and

THE CHASE MANHATTAN BANK

176024:v01

Permanent Subcommittee on Investigations
EXHIBIT #135

THIS SECURITY AGREEMENT is dated as of the 18th day of December 1997

BETWEEN:

(1) MAHONIA LIMITED a company incorporated under the laws of Jersey whose registered office is at 22 Grenville Street, St. Helier, Jersey (the "Company"); and

(2) THE CHASE MANHATTAN BANK (the "Bank").

WHEREAS

(A) The Bank has entered into a Natural Gas Forward Sale Agreement dated as of the date hereof with the Company pursuant to which the Bank has agreed to purchase certain volumes of natural gas from the Company for forward delivery in exchange for the payment therefor, on a discounted price basis, on December 19, 1997 in a principal amount not exceeding $300,000,000 (as amended, supplemented and modified and in effect from time to time, the "Chase Gas Agreement"); and

(B) To induce the Bank to enter into the Chase Gas Agreement and for good and other valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Company has agreed to pledge and grant a security interest in the Collateral (as hereinafter defined) as security for the Secured Obligations (as hereinafter defined).

IT IS HEREBY AGREED as follows:

1. Interpretation

1.1 In this Security Agreement, unless the context otherwise requires, the following terms shall have the following meanings:

"Collateral" has the meaning ascribed to it in Clause 4(c) hereof;

"Dollars" and "$" means lawful money of the United States of America;

"ENGMC" means Enron Natural Gas Marketing Corp., a Delaware corporation and a wholly-owned subsidiary of Enron;

"Enron" means Enron Corp., an Oregon corporation;

"Event of Default" means any of the events of default set out in Section 5.01 of the Chase Gas Agreement;

"Forward Sale Contract" means the Natural Gas Inventory Forward Sale Contract dated as of the date hereof between the Company and ENGMC, as the same shall be amended, modified and supplemented and in effect from time to time;

"Guaranty Agreement" means the Guaranty Agreement dated as of the date hereof between Enron and the Company, pursuant to which Enron guarantees the performance and other obligations of ENGMC under the Forward Sale Contract, as the same shall be amended, modified and supplemented and in effect from time to time;

"Letter of Credit" means the Irrevocable Performance Letter of Credit for the account of Enron, in favor of the Company and issued on or after the date hereof by the Lenders named therein and The Chase Manhattan Bank, as Agent;

"Margin Agreement" means the Margin Agreement dated as of the date hereof between the Company and ENGMC, pursuant to which ENGMC provides security to the Company for its obligations under the Forward Sale Contract, as the same shall be amended, modified and supplemented and in effect from time to time;

"NYMEX" means the New York Mercantile Exchange Inc. and any successor thereto;

"Receiver" has the meaning ascribed to it in Clause 10; and

"Secured Obligations" means all sums and liabilities referred to in Clause 2.

1.2 Any references in this Security Agreement to this Security Agreement or another agreement or instrument shall be construed as a reference to this Security Agreement, that other agreement or instrument as the same may have been, or may from time to time be amended, supplemented, otherwise modified or novated.

1.3 Clause and Schedule headings are for ease of reference only.

2. Covenant to Pay

2.1 The Company hereby covenants with the Bank to perform, pay and discharge in full to the Bank:

(i) all delivery obligations, sums and liabilities whatsoever, present or future, actual or contingent, which are now or may at any time hereafter become due, owing or incurred by the Company to the Bank under or in connection with the Chase Gas Agreement; and

(ii) all sums and liabilities whatsoever, present or future, actual or contingent, which are now or may at any time hereafter become due, owing or incurred by the Company to the Bank under or

arising in connection with this Security Agreement,

Provided that every performance or payment in respect of the delivery obligation, sums and liabilities hereby covenanted to be paid or discharged which is made in the manner provided in the Chase Gas Agreement shall be in satisfaction pro tanto of the covenant of the Company contained in this Clause.

2.2 The Company shall pay interest (after as well as before any judgment) from the date payment is due hereunder until the date of payment calculated on a daily basis on such sums at the rate of 1-1/2% per annum over the rate announced by the Bank from time to time at its head office in New York as its prime commercial lending rate.

3. No Obligation to Make Advances

The Bank shall have no obligation to make advances to the Company (except pursuant to the Chase Gas Agreement in accordance with the terms thereof).

4. Lien and Security Interest

As a continuing security for the Secured Obligations, the Company as beneficial owner hereby:-

(a) assigns in equity to the Bank all right, title and interest which it may now and from time to time hereafter have in, to or under, and grants the Bank a lien and security interest in:-

(i) the Forward Sale Contract;

(ii) the Margin Agreement;

(iii) all sums, instruments and other property constituting margin provided by ENGMC to the Company pursuant to the terms of the Margin Agreement;

(iv) the Guaranty Agreement and Letter of Credit (and all proceeds of the Guaranty Agreement and Letter of Credit);

(v) the natural gas delivered to the Company or to its order pursuant to the Forward Sale Contract;

(vi) all proceeds, income, benefits and substitutions of and for any of the foregoing and its other incidental property relating to the transactions anticipated by, or

acknowledged in, the above-mentioned documents, rights, titles and interests (including but not limited to proceeds, income, benefits and substitutions of and for any of the foregoing);

(b) grants the Bank a lien and security interest in, the whole of the Company's undertaking and assets, present and future (including but not limited to the Collateral identified in Clause 4 of the Security Agreement dated as of September 26, 1995 between the Company and the Bank and identified in Clause 4 of the Security Agreement dated as of December 16, 1996 between the Company and the Bank).

(c) The interests, assets and property of the Company described in Clauses 4(a) and 4(b) above shall be the "Collateral" hereunder.

Execution of this Security Agreement by the Company shall constitute notice to the Bank of the lien and security interest created by or pursuant to Clauses 4(a) and 4(b).

5. Further Assurance

5.1 The Company shall, from time to time, at the request of the Bank, do any act or execute in favor of the Bank or as it may direct such further or other legal or other assignments (including, without limitation, converting the equitable assignments referred to at Clause 4(a) into legal assignments), transfers, mortgages, charges, securities or other documents as in each case the Bank shall stipulate, in such form as the Bank may require, for the improvement or perfection of the security intended to be conferred on the Bank by or pursuant to this Security Agreement including any act or document which may be required or desirable under the laws of any jurisdiction in which any property and assets equivalent or similar to the security intended to be conferred by or pursuant to this Security Agreement or to perfect or improve any security held thereover or to facilitate the realization thereof or the exercise of any and all powers, authorities and discretions intended to be vested in the Bank or any Receiver by or pursuant to this Security Agreement.

5.2 The Company shall take all such action as is available to it:

(a) to perfect, protect and maintain the security intended to be conferred on the Bank by or pursuant to this Security Agreement; and

(b) to make all such filings and registrations and to take all such other steps as may be necessary in connection with the creation, perfection, protection or

maintenance of any security which it may, or may be required to, create in connection herewith.

5.3 The Company shall, as continuing security for the Secured Obligations, assign in equity to the Bank all right, title and interest which it may from time to time have after the date hereof in, to or under, and grant the Bank a lien and security interest in, any natural gas or futures contracts which may be entered into by the Company on NYMEX.

6. Redemption of Security

Upon and subject to the Secured Obligations having been performed, paid or discharged in full to the satisfaction of the Bank and the Company having no liability (whether actual or contingent) to the Bank hereunder, the Bank shall at the request and cost of the Company reassign the property referred to in Clause 4 above and release or otherwise discharge the security hereby constituted in such form as is satisfactory to the Bank (and without recourse to, or representation or warranty by, the Bank).

7. Representations and Warranties

The Company hereby represents and warrants to the Bank that:

(a) it is and will, at all times during the subsistence of this Security Agreement, be the sole, lawful and beneficial owner of all the Collateral;

(b) it has not assigned, charged, pledged or otherwise encumbered (other than in favor of the Bank pursuant to the terms of this Security Agreement, the Security Agreement dated as of September 26, 1995 and the Security Agreement dated as of December 16, 1996, as amended) any of its rights, title and interest in the Collateral;

(c) it has and will at all times have the necessary power, authority and standing to enable it to enter into and perform the obligations expressed to be assumed by it under this Security Agreement;

(d) it has taken all corporate action and any other action necessary in connection with the execution and performance of this Security Agreement and such execution and performance will not cause the Company to be in breach of any agreement to which it is a party, its Memorandum and Articles of Association or any applicable law or regulations;

(e) this Security Agreement constitutes, and will continue to constitute, during the subsistence of the security herein provided for, legal, valid, binding and enforceable obligations of the Company in accordance with its terms except that the enforceability thereof may be affected by applicable bankruptcy, insolvency, reorganization or other similar laws affecting the rights of creditors generally and by general principles of equity;

(f) it does not have a place of business in the United States of America, in any territory or possession of the United States of America or in the Commonwealth of Puerto Rico; and

(g) it has not taken any corporate action nor have any other steps been taken or legal proceedings been started or, to the best of its knowledge and belief, threatened against it for its winding-up, liquidation, administration, dissolution or reorganization or for the appointment of a receiver, administrative receiver, trustee or similar officer of any or all of its assets or revenues.

8. Covenants

8.1 The Company hereby covenants with the Bank that it will:

(a) do or permit to be done each and every act or thing which the Bank may from time to time require to be done for the purpose of enforcing or perfecting or assuming or improving the Bank's rights under this Security Agreement and in relation to any of the Collateral;

(b) exercise its rights, authorities and discretions under or in respect of the Collateral in such manner as the Bank may from time to time require;

(c) indemnify and hold harmless the Bank on demand by the Bank from and against all actions, losses, claims, proceedings, costs, demands and liabilities which may be suffered by the Bank by reason of the failure of the Company to perform any of its obligations pursuant to this Security Agreement;

(d) perform its obligations under the Forward Sale Contracts and the Physical Sale Contracts and use its best endeavors to procure that the other parties thereto shall perform their obligations thereunder and the Bank shall be under no obligation of any kind whatsoever thereunder or be under any liability whatsoever in the event of any failure of the Company to perform its obligations thereunder;

(e) notify the Bank upon receiving or becoming aware of any matter which may have an adverse effect on the obligations of ENGMC under the Forward Sale Contract;

(f) forthwith on execution hereof give notice of the assignment effected by this Security Agreement to Enron and ENGMC in the form set out in the Schedule and request that the person on whom notice is served executes and delivers to the Bank an acknowledgment in the form set out in the Schedule or in such other form as may be acceptable to the Bank;

(g) forthwith on execution hereof give notice of the assignment effected by this Security Agreement to the Letter of Credit banks in form satisfactory to the Bank.

8.2 The Company hereby covenants with the Bank that it will not, save with the prior written consent of the Bank:

(a) permit any variation of any Forward Sale Contract, the Guaranty Agreement, the Margin Agreement or any release of any party from any of its obligations thereunder, any waiver of any breach of any party's obligations nor will it give any consent to any act or omission by any such party which would otherwise constitute a breach;

(b) assign, charge, pledge, dispose of or otherwise encumber any or all of the Company's rights, title and interest in the Collateral;

(c) otherwise deal with the Collateral (other than by way of the performance thereof or the exercise of the Company's rights thereunder or deal with such property in a manner approved or required by the Bank).

9. The Bank's Powers

The powers conferred on the Bank hereunder are solely to protect the Bank's interest in the Collateral and shall not impose any duty upon it to exercise any such powers.

10. Entry into Possession, Bank's Powers and Appointment, Removal and Status of Receiver

10.1 On or at any time after the occurrence of an Event of Default, the Bank may, without notice to the Company, take possession of and hold all or any part of the Collateral and the Bank may, without first appointing a Receiver, exercise all or any of the powers conferred on secured parties by the Uniform Commercial Code in effect in the State of New York (the "UCC") as varied or extended by this

Security Agreement and all of the powers, authorities and discretions conferred by this Security Agreement expressly or by implication on any Receiver or otherwise conferred by statute or common law on secured parties, mortgagees or receivers.

10.2 On or at any time after the occurrence of an Event of Default or after having been requested to do so by the Company, the Bank may, without notice to the Company, appoint one or more persons to be a receiver or receiver and manager of administrative receiver of the whole or any part of the Collateral (individually or together with any other or additional persons appointed or substituted as a receiver, receiver and manager or administrative receiver (and where more than one jointly or severally or jointly and severally), a "Receiver" or the "Receivers", as the case may be). The Bank may:

(a) (so far as it is lawfully able) remove any Receiver; and

(b) appoint another person or persons as Receiver or Receivers either in the place of a Receiver who has been so removed or who has ceased to act or to act jointly with any other Receiver.

11. Enforcement

11.1 At any time after the occurrence of an Event of Default the power of sale and other powers conferred on secured parties by the UCC shall be immediately exercisable (without any restrictions as to the giving of notice or otherwise) and the Bank may at its absolute discretion sell or otherwise dispose of, for any consideration the whole or any part of the Collateral. The Bank shall be entitled to apply the proceeds of such sale or other disposal in or towards discharge of the Secured Obligations in whatever manner or order as it thinks fit.

11.2 The Secured Obligations shall be deemed to have become due and payable and the power of sale and other powers conferred on secured parties by the UCC shall arise immediately on an Event of Default.

11.3 The Bank shall not be liable to account as mortgagee in possession in respect of the whole or any part of the Collateral or be liable (in each case in the absence of gross negligence or willful misconduct) for any loss upon realization in connection with all or any of the Collateral for which a mortgagee in possession might as such be liable.

12. Powers of Receiver

Every Receiver shall (subject to any limitations or restrictions expressed in the instrument appointing him but notwithstanding any winding-up or dissolution of the Company) have, in relation to the Collateral or, as the case may be, that part of the Collateral in respect of which he was appointed, and as varied and extended by the provisions of this Security Agreement:

(a) all the powers conferred by applicable law on mortgagors and on mortgagees in possession and on receivers appointed under such law;

(b) power in the name of, or on behalf of, and at the cost of the Company, to manage the assets and business of the Company (whether or not part of the Collateral) and for such purpose to use the services of any employee or consultant of the Company; and

(c) power in the name or on behalf and at the cost of the Company to exercise all the powers and rights of an absolute owner and to do or omit to do anything which the Company itself could do or omit to do (including but not limited to drawing under the Letter of Credit and obtaining payment directly thereunder).

13. Remuneration

Every Receiver shall be entitled to remuneration for his services at a rate to be fixed by agreement between him and the Bank (or, failing such agreement, to be fixed by the Bank) appropriate to the work and responsibilities involved upon the basis of charging from time to time adopted in accordance with his current practice or the current practice of his firm.

14. Application of Payments

14.1 Monies received by a Receiver

All monies received by any Receiver shall (subject to the rights and claims of any person having prior rights thereto) be applied in the following order:

(a) in the payment of the costs, charges and expenses of and incidental to the Receiver's appointment and the payment of his remuneration;

(b) in the payment and discharge of any liabilities incurred by the Receiver in the exercise of any of the powers of the Receiver including the costs of realization of that part of the Collateral in respect of which he was appointed;

(c) in payment to the Bank for application in accordance with Clause 14.2.

14.2 All Monies

All monies from time to time received or recovered by the Bank from the Company or from any person or persons liable to pay the same from any Receiver or otherwise pursuant to this Security Agreement (including the proceeds of any conversion of currency) may be applied by the Bank (and notwithstanding any purported appropriation by the Company) either as a whole or in such order and in such proportions and otherwise in such manner as the Bank shall think fit in or towards the discharge of the Secured Obligations or in payment to the credit of any suspense or nonpersonal account and be so held in such account for so long as the Bank shall think fit pending further application in accordance with this Clause 14.2 or in payment to the credit of any nominated account (including an account opened by the Bank for the purpose) as security for any of the Secured Obligations which are at such time contingent or future.

15. Protection of Purchasers

No purchaser or other person dealing with the Bank or any Receiver shall be bound to see or inquire whether the right of the Bank or such Receiver to exercise any of its or his powers has arisen or become exercisable or be concerned with any propriety or regularity on the part of the Bank or such Receiver in such dealings.

16. Power of Attorney

16.1 The Company hereby by way of security for the performance of the Company's obligations under this Security Agreement irrevocably appoints the Bank and any Receiver jointly and severally to be the attorney or attorneys of the Company and in its name and otherwise on its behalf and as its act and deed to sign, seal, execute, deliver, perfect and do all deeds, instruments, acts and things which may be required (or which the attorney shall consider desirable):

(a) for carrying out any obligation imposed on the Company by or pursuant to this Security Agreement or by or pursuant to or in connection with the Forward Sale Contract and everything in connection therewith;

(b) for carrying any sale, lease or other dealing whatsoever by the Bank or any Receiver into effect;

JPMC-H 000055

(c) for conveying or transferring any legal estate or other interest in land or any other property whatsoever;

(d) for getting in all or any part of the Collateral;

(e) generally for enabling the Bank and any Receiver to exercise the respective powers, authorities and discretions conferred on them by or pursuant to this Security Agreement or by law.

The power granted to the Bank and any Receiver under this Clause 16.1 shall include the power to exercise all rights and remedies of the Company under the Forward Sale Contract, the Margin Agreement, the Guaranty Agreement and the Letter of Credit (collectively, the "Assigned Agreements"), including without limitation, (i) the right to receive all payments of all amounts owing under or in respect of any Assigned Agreement (including, without limitation, Termination Payments and Unpaid Amounts (as defined of the Forward Sale Contract)), (ii) the right to receive and send all specifications and notices to or by the Company under any Assigned Agreement, (iii) the right to make demands and to declare amounts owing under any Assigned Agreement to be due and payable and (iv) the right to modify or supplement, or waive any of the provisions of, any Assigned Agreement.

Each of the Bank and any Receiver shall have full power to delegate the power conferred on it or him by this Clause 16.1 but no such delegation shall preclude the subsequent exercise of such power by the Bank or the Receiver itself or himself or preclude the Bank or the Receiver from making a subsequent delegation thereof to some other person; any such delegation may be revoked by the Bank or the Receiver at any time.

16.2 Where the Bank is appointed as attorney such appointment may be carried out by any officer of the Bank.

16.3 The Company shall ratify and confirm all things done by the attorney in the exercise or purported exercise of his powers.

17. Set-Off and Combination of Accounts

Without prejudice to any rights the Bank may have at law or in equity or otherwise, the Company authorizes the Bank to apply any credit balance to which the Company is entitled on any account with the Bank (at any of its branches) in satisfaction of the Secured Obligations (and on or at any time after the occurrence of an Event of Default the Bank may make such application notwithstanding any specified maturity of any deposits standing to the credit of any

JPMC-H 000056

account of the Company with the Bank) and for this purpose the Bank is authorized to purchase with the monies standing to the credit of any such account such other currencies as may be necessary to effect such application. The Bank shall not be obliged to exercise any right given to it by this Clause 17.

18. Effectiveness of Security

18.1 The Security shall be:

(a) a continuing security for the Secured Obligations and shall not be considered as satisfied or discharged by any intermediate payment or settlement of the whole or any part of the Secured Obligations or any other matter or thing whatsoever; and

(b) in addition to and independent of and shall not operate so as to prejudice or affect or merge in any other security which the Bank may hold at any time for the Secured Obligations or any other obligations whatsoever and shall not be affected by any release, reassignment or discharge of such other security.

18.2 Neither the security constituted by this Security Agreement nor any remedy of the Bank in respect thereof shall be prejudiced by:

(a) any unenforceability or invalidity of any other agreement or document; or

(b) any time or indulgence granted to the Company or any other person or any other act or thing whatsoever which, but for this Clause 18.2, would or might prejudice the security furnished by this Security Agreement or the right of the Bank to any such remedy.

18.3 No failure on the part of the Bank to exercise, or the delay on its part in exercising, any of the rights, powers and remedies provided by this Security Agreement or by law (collectively, the "Bank's Rights") shall operate as a waiver thereof, nor shall any single or partial exercise of any of the Bank's Rights preclude any other or further exercise thereof or the exercise of any other right, power or privilege. The rights and remedies provided in this Security Agreement are cumulative and not exclusive of any rights or remedies provided by law.

19. Accounts

19.1 If the Bank shall at any time receive notice of any subsequent mortgage, assignment, charge or other interest affecting the whole or any part of the Collateral, the Bank may open a new account or accounts for the Company in its books. If the Bank does not do so, then (unless the Bank gives express written notice to the contrary to the Company) as from the time of receipt of such notice by the Bank, all subsequent payments made by the Company to the Bank shall in the absence of any express appropriation by the Bank to the contrary be treated as having been credited to a new account of the Company and not as having been applied in reduction of the Secured Obligations at the time when the Bank received the notice.

19.2 All monies received, recovered or realized by the Bank under this Security Agreement (including the proceeds of any conversion of currency) may in the Bank's discretion be credited to any suspense or impersonal account and may be held in such account for so long as the Bank shall think fit (with interest accruing thereon at such rate, if any, as the Bank may deem fit) pending their application from time to time (as the Bank shall be entitled to do in the Bank's discretion) in or towards the discharge of any of the Secured Obligations.

19.3 In case the Bank shall have more than one account for the Company in its books, the Bank may at any time after the Bank shall have received notice of any subsequent charge or other interest affecting all or any part of the Collateral, and without prior notice, forthwith combine any such account with, or transfer all or any part of any balance standing to the credit of any such account to, any other such account which may be in debit.

20. Currency

For the purpose of satisfying or discharging any or all of the Secured Obligations, the Bank shall be entitled to convert from the currency (the "First Currency") in which any monies are received, recovered or realized under this Security Agreement into another currency (the "Second Currency") which is the currency of denomination of the Secured Obligations at the rate of exchange at which the Bank may in the ordinary course of business purchase a second currency with the first currency. Accordingly, the Secured Obligations shall be discharged to the extent of the proceeds of such conversion actually received by the Bank (net of any premia, commissions or other charges paid or incurred in connection therewith).

JPMC-H 000058

21. Notices

All notices, requests, demands, consents or other communications to or upon either party hereto shall be in writing addressed to either party at the address specified below (or at such other address as either party may hereafter specify to the other):

if to the Company:

Mahonia Limited
22 Grenville Street
St. Helier, Jersey

Attention: Ian James
Facsimile No.: 44-1534 609333
Telephone No.: 44-1534 609000

if to the Bank:

The Chase Manhattan Bank
270 Park Avenue, 8th Floor
New York, New York 10017

Attention: Alex Mintcheff
Facsimile No.: 212-834-6084
Telephone No.: 212-834-5364

22. Severability

Every provision contained in this Security Agreement shall be severable and distinct from every other such provision and if at any time any one or more of such provisions is or becomes invalid, illegal or unenforceable, the validity, legality or enforceability of the remaining such provisions shall not in any way be affected thereby.

23. Counterparts

This Security Agreement may be executed by the parties hereto in separate counterparts, each of which when so executed and delivered shall be an original, and such counterparts shall together constitute one and the same instrument.

24. Expenses

All the costs and expenses (including tax liabilities, legal costs and VAT in respect thereof) incurred by the Bank in the exercise of any of the rights, remedies and powers conferred on the Bank by this Security Agreement or in the perfection or enforcement of any of the security herein provided for in respect of the Secured Obligations shall be reimbursed by the Company to the Bank on demand for a full indemnity basis and shall carry interest from the date of such demand until so reimbursed at the rate and otherwise as mentioned in Clause 2.2.

25. Governing Law

This Security Agreement shall be governed by and construed in accordance with the law of the State of New York.

IN WITNESS WHEREOF, this Security Agreement has been executed by the parties hereto and is intended to be and is hereby delivered on the date first above written.

MAHONIA LIMITED

By_____
Title:

THE CHASE MANHATTAN BANK

By_____
Title: Managing Director

THE SCHEDULE

Notice of Assignment

To: [ ]

We refer to [ ] dated [ ] (the [Agreement]") and made between yourselves and ourselves.

We hereby give you notice that by a Security Agreement dated December 18, 1997 we have assigned in equity to The Chase Manhattan Bank (the "Bank") all of our rights, title and interest in and to the [Agreement], including, without limitation, the full amount of all payments [and/or deliveries of natural gas] due or to become due from you to us thereunder. Such Security Agreement entitles the Bank to require us to convert such assignment into an absolute assignment.

Accordingly, we hereby instruct you that upon receipt by you of instructions from the Bank all deliveries of natural gas [and/or payments] due from you to us as from the date of such instructions under the [Agreement] should be paid or made direct to the Bank in accordance with its instructions. Please note that these instructions may not be altered without the written consent of the Bank.

We should be grateful if you would kindly acknowledge receipt of this notice of assignment by signing and returning a copy of this letter to the Bank in the form attached.

DATED this __ day of _____, 199_

For and on behalf of
MAHONIA LIMITED

176024:v01

CONSENT AND AGREEMENT

CONSENT AND AGREEMENT dated as of December 18, 1997 between ENRON NATURAL GAS MARKETING CORP., a Delaware corporation ("ENGMC") and THE CHASE MANHATTAN BANK, a New York State banking corporation (the ("Bank").

ENGMC and Mahonia Limited, a company incorporated under the laws of Jersey (the "Company") are party to (i) a Natural Gas Inventory Forward Sale Contract dated as of the date hereof (as amended from time to time, the "Forward Sale Contract") pursuant to which ENGMC has agreed to sell to the Company, and the Company has agreed to purchase from ENGMC, certain natural gas, and (ii) a Margin Agreement dated as of the date hereof (as amended from time to time, the "Margin Agreement" and, together with the Forward Sale Contract, the "Assigned Agreements") pursuant to which ENGMC has agreed to provide security to the Company pursuant to the Forward Sale Contract.

The Company and the Bank are parties to a Natural Gas Forward Sale Contract dated as of the date hereof (as amended from time to time, the "Gas Agreement") pursuant to which the Bank has agreed to purchase certain volumes of natural gas from the Company for forward delivery in exchange for payment therefor, on a discounted basis, in a principal amount not to exceed $300,000,000, which payment will be used by the Company to make the purchase from ENGMC of certain natural gas pursuant to the Forward Sale Contract.

In order to induce the Bank to enter into the Gas Agreement, the Company and the Bank have entered into a Security Agreement dated as of the date hereof (as amended from time to time, the "Security Agreement") pursuant to which Security Agreement the Company has, as continuing security for the Company's obligations under the Gas Agreement (as well as certain other "Secured Obligations" defined in the Security Agreement), assigned to the Bank all right, title and interest of the Company in, to and under the Assigned Agreements.

ENGMC expects to derive substantial benefit from the transactions contemplated by the Gas Agreement and the Security Agreement and, accordingly, hereby consents to the assignment by the Company to the Bank of all of its right, title and interest in, to and under the Assigned Agreements and agrees that (as contemplated by the Security Agreement), the Bank and any Receiver (as defined in the Security Agreement) under the Security Agreement may exercise all rights and remedies of the Company under the Assigned Agreements, including without limitation, (i) the right to receive all payments of all amounts owing under or in respect of the Assigned Agreements (including, without limitation, Termination Payments and Unpaid Amounts (as defined in the Forward Sale Contract)) (ii) the right to receive and send all specifications and notices to or by the Company under the Assigned Agreements, (iii) the right to make demands and to declare

amounts owing under the Assigned Agreements to be due and payable and (iv) the right to modify or supplement, or waive any of the provisions of, the Assigned Agreements.

This Consent and Agreement may be executed in any number of counterparts, all of which taken together shall constitute one and the same instrument and any of the parties hereto may execute this Agreement by signing any such counterpart. This Consent and Agreement shall be governed by, and construed in accordance with, the laws of the State of New York.

IN WITNESS WHEREOF, the parties hereto have caused this Consent and Agreement to be duly executed as of the day and year first written above.

ENRON NATURAL GAS
MARKETING CORP.

By: _____
Title: William D. Gathmann
Vice President, Finance and Treasurer

THE CHASE MANHATTAN BANK

By: _____
Title: Managing Director

176668-v01

DEC 18'97 20:05 FR UE LLP HOU 23 X2346 713 758 2346 TO 96463491 P.04

[illegible] P.4

CONSENT AND AGREEMENT

CONSENT AND AGREEMENT dated as of December 18, 1997 between ENRON CORP., an Oregon corporation ("Enron") and THE CHASE MANHATTAN BANK, a New York State banking corporation (the "Bank").

Enron and Mahonia Limited, a company incorporated under the laws of Jersey (the "Company") are party to a Guaranty Agreement dated as of the date hereof (as amended from time to time, the "Guaranty Agreement") pursuant to which Enron guarantees certain obligations owing to the Company by Enron Natural Gas Marketing Corp. ("ENGMC") under a Forward Sale Contract (as defined in the Gas Agreement defined below).

The Company and the Bank are parties to a Natural Gas Forward Sale Contract dated as of the date hereof (as amended from time to time, the "Gas Agreement") pursuant to which the Bank has agreed to purchase certain volumes of natural gas from the Company for forward delivery in exchange for payment therefor, on a discounted basis, in a principal amount not to exceed $300,000,000, which payment will be used by the Company to make the purchase from ENGMC of certain natural gas pursuant to the Forward Sale Contract.

In order to induce the Bank to enter into the Gas Agreement, the Company and the Bank have entered into a Security Agreement dated as of the date hereof (as amended from time to time, the "Security Agreement") pursuant to which Security Agreement the Company has, as continuing security for the Company's obligations under the Gas Agreement (as well as certain other "Secured Obligations" defined in the Security Agreement), assigned to the Bank all right, title and interest of the Company in, to and under the Guaranty Agreement.

Enron expects to derive substantial benefit from the transactions contemplated by the Gas Agreement and the Security Agreement and, accordingly, hereby consents to the assignment by the Company to the Bank of all of its right, title and interest in, to and under the Guaranty Agreement and agrees that (as contemplated by the Security Agreement), the Bank and any Receiver (as defined in the Security Agreement) under the Security Agreement may exercise all rights and remedies of the Company under the Guaranty Agreement, including without limitation, (i) the right to receive all payments of all amounts owing under or in respect of the Guaranty Agreement, (ii) the right to receive and send all specifications and notices to or by the Company under the Guaranty Agreement, (iii) the right to make demands and to declare amounts owing under the Guaranty Agreement to be due and payable and (iv) the right to modify or supplement, or waive any of the provisions of, the Guaranty Agreement.

This Consent and Agreement may be executed in any number of counterparts, all of which taken together shall constitute one and the same instrument and any of the parties hereto may execute this Agreement by signing any such counterpart.

176668-v01

DEC 18'97 20:05 FR UE LLP HOU 23 X2346 713 758 2346 TO 96463491 P.05

This Consent and Agreement shall be governed by, and construed in accordance with, the laws of the State of New York.

IN WITNESS WHEREOF, the parties hereto have caused this Consent and Agreement to be duly executed as of the day and year first written above.

ENRON CORP.

By: _____
Title: William D. Gathmann
Vice President, Finance and Treasurer

THE CHASE MANHATTAN BANK

By: _____
Title: Managing Director

[illegible]

EXHIBIT NOTE: THESE ARE EXCERPTS OF ENRON CORP 10K FOR 2000

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

Form 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2000
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 1-13159

ENRON CORP.

(Exact name of registrant as specified in its charter)

Oregon	47-0255140
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

ENRON BUILDING

1400 Smith Street, Houston, Texas 77002-7369
(Address of principal executive offices) (zip code)

Registrant's telephone number, including area code:
713-853-6161

Permanent Subcommittee on Investigations
EXHIBIT #136

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED INCOME STATEMENT

(In millions, except per share amounts)	Year ended December 31, 2000	1999	1998
Revenues			
Natural gas and other products	$ 50,500	$19,536	$13,276
Electricity	33,823	15,238	13,939
Metals	9,234	-	-
Other	7,232	5,338	4,045
Total revenues	100,789	40,112	31,260
Costs and Expenses			
Cost of gas, electricity, metals and other products	94,517	34,761	26,381
Operating expenses	3,184	3,045	2,473
Depreciation, depletion and amortization	855	870	827
Taxes, other than income taxes	280	193	201
Impairment of long-lived assets	-	441	-
Total costs and expenses	98,836	39,310	29,882
Operating Income	1,953	802	1,378
Other Income and Deductions			
Equity in earnings of unconsolidated equity affiliates	87	309	97
Gains on sales of non-merchant assets	146	541	56
Gain on the issuance of stock by TNPC, Inc.	121	-	-
Interest income	212	162	88
Other income, net	(37)	181	(37)
Income Before Interest, Minority Interests and Income Taxes	2,482	1,995	1,582
Interest and related charges, net	838	656	550
Dividends on company-obligated preferred securities of subsidiaries	77	76	77
Minority interests	154	135	77
Income tax expense	434	104	175
Net income before cumulative effect of accounting changes	979	1,024	703
Cumulative effect of accounting changes, net of tax	-	(131)	-
Net Income	979	893	703
Preferred stock dividends	83	66	17
Earnings on Common Stock	$ 896	$ 827	$ 686
Earnings Per Share of Common Stock			
Basic			
Before cumulative effect of accounting changes	$ 1.22	$ 1.36	$ 1.07
Cumulative effect of accounting changes	-	(0.19)	-
Basic earnings per share	$ 1.22	$ 1.17	$ 1.07
Diluted			
Before cumulative effect of accounting changes	$ 1.12	$ 1.27	$ 1.01
Cumulative effect of accounting changes	-	(0.17)	-
Diluted earnings per share	$ 1.12	$ 1.10	$ 1.01
Average Number of Common Shares Used in Computation			
Basic	736	705	642
Diluted	814	769	695

The accompanying notes are an integral part of these consolidated financial statements.

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

(In millions)	December 31, 2000	1999
ASSETS		
Current Assets		
Cash and cash equivalents	$ 1,374	$ 288
Trade receivables (net of allowance for doubtful accounts of $133 and $40, respectively)	10,396	3,030
Other receivables	1,874	518
Assets from price risk management activities	12,018	2,205
Inventories	953	598
Deposits	2,433	81
Other	1,333	535
Total current assets	30,381	7,255
Investments and Other Assets		
Investments in and advances to unconsolidated equity affiliates	5,294	5,036
Assets from price risk management activities	8,988	2,929
Goodwill	3,638	2,799
Other	5,459	4,681
Total investments and other assets	23,379	15,445
Property, Plant and Equipment, at cost		
Natural gas transmission	6,916	6,948
Electric generation and distribution	4,766	3,552
Fiber optic network and equipment	839	379
Construction in progress	682	1,120
Other	2,256	1,913
	15,459	13,912
Less accumulated depreciation, depletion and amortization	3,716	3,231
Property, plant and equipment, net	11,743	10,681
Total Assets	$65,503	$33,381

LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	$ 9,777	$ 2,154
Liabilities from price risk management activities	10,495	1,836
Short-term debt	1,679	1,001
Customers' deposits	4,277	44
Other	2,178	1,724
Total current liabilities	28,406	6,759
Long-Term Debt	8,550	7,151
Deferred Credits and Other Liabilities		
Deferred income taxes	1,644	1,894
Liabilities from price risk management activities	9,423	2,990
Other	2,692	1,587
Total deferred credits and other liabilities	13,759	6,471
Commitments and Contingencies (Notes 13, 14 and 15)		
Minority Interests	2,414	2,430
Company-Obligated Preferred Securities of Subsidiaries	904	1,000
Shareholders' Equity		
Second preferred stock, cumulative, no par value, 1,370,000 shares authorized, 1,240,933 shares and 1,296,184 shares issued, respectively	124	130
Mandatorily Convertible Junior Preferred Stock, Series B, no par value, 250,000 shares issued	1,000	1,000
Common stock, no par value, 1,200,000,000 shares authorized, 752,205,112 shares and 716,865,081 shares issued, respectively	8,348	6,637
Retained earnings	3,226	2,698
Accumulated other comprehensive income	(1,048)	(741)
Common stock held in treasury, 577,066 shares and 1,337,714 shares, respectively	(32)	(49)
Restricted stock and other	(148)	(105)
Total shareholders' equity	11,470	9,570
Total Liabilities and Shareholders' Equity	$65,503	$33,381

The accompanying notes are an integral part of these consolidated financial statements.

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS

(In millions)	Year ended December 31, 2000	1999	1998
Cash Flows From Operating Activities			
Reconciliation of net income to net cash provided by operating activities			
Net income	$ 979	$ 893	$ 703
Cumulative effect of accounting changes	-	131	-
Depreciation, depletion and amortization	855	870	827
Impairment of long-lived assets (including equity investments)	326	441	-
Deferred income taxes	207	21	87
Gains on sales of non-merchant assets	(146)	(541)	(82)
Changes in components of working capital	1,769	(1,000)	(233)
Net assets from price risk management activities	(763)	(395)	350
Merchant assets and investments:			
Realized gains on sales	(104)	(756)	(628)
Proceeds from sales	1,838	2,217	1,434
Additions and unrealized gains	(1,295)	(827)	(721)
Other operating activities	1,113	174	(97)
Net Cash Provided by Operating Activities	4,779	1,228	1,640
Cash Flows From Investing Activities			
Capital expenditures	(2,381)	(2,363)	(1,905)
Equity investments	(933)	(722)	(1,659)
Proceeds from sales of non-merchant assets	494	294	239
Acquisition of subsidiary stock	(485)	-	(180)
Business acquisitions, net of cash acquired (see Note 2)	(777)	(311)	(104)
Other investing activities	(182)	(405)	(356)
Net Cash Used in Investing Activities	(4,264)	(3,507)	(3,965)
Cash Flows From Financing Activities			
Issuance of long-term debt	3,994	1,776	1,903
Repayment of long-term debt	(2,337)	(1,837)	(870)
Net increase (decrease) in short-term borrowings	(1,595)	1,565	(158)
Net issuance (redemption) of company-obligated preferred securities of subsidiaries	(96)	-	8
Issuance of common stock	307	852	867
Issuance of subsidiary equity	500	568	828
Dividends paid	(523)	(467)	(414)
Net disposition of treasury stock	327	139	13
Other financing activities	(6)	(140)	89
Net Cash Provided by Financing Activities	571	2,456	2,266
Increase (Decrease) in Cash and Cash Equivalents	1,086	177	(59)
Cash and Cash Equivalents, Beginning of Year	288	111	170
Cash and Cash Equivalents, End of Year	$ 1,374	$ 288	$ 111
Changes in Components of Working Capital			
Receivables	$(8,203)	$ (662)	$(1,055)
Inventories	1,336	(133)	(372)
Payables	7,167	(246)	433
Other	1,469	41	761
Total	$ 1,769	$(1,000)	$ (233)

The accompanying notes are an integral part of these consolidated financial statements.

3 PRICE RISK MANAGEMENT ACTIVITIES AND FINANCIAL INSTRUMENTS

Trading Activities. Enron offers price risk management services to wholesale, commercial and industrial customers through a variety of financial and other instruments including forward contracts involving physical delivery, swap agreements, which require payments to (or receipt of payments from) counterparties based on the differential between a fixed and variable price for the commodity, options and other contractual arrangements. Interest rate risks and foreign currency risks associated with the fair value of the commodity portfolio are managed using a variety of financial instruments, including financial futures.

Notional Amounts and Terms. The notional amounts and terms of these instruments at December 31, 2000 are shown below (dollars in millions):

	Fixed Price Payor	Fixed Price Receiver	Maximum Terms in Years
Commodities(a)			
Natural gas	7,331	6,910	23
Crude oil and liquids	3,513	1,990	6
Electricity	2,424	2,388	24
Metals, coal and pulp and paper	368	413	9
Bandwidth	167	325	11
Financial products			
Interest rate(b)	$4,732	$3,977	29
Foreign currency	$ 79	$ 465	22
Equity investments(c)	$2,998	$3,768	13

(a) Natural gas, crude oil and liquids and electricity volumes are in TBtue; metals, coal and pulp and paper volumes are in millions of metric tonnes; and bandwidth volumes are in thousands of terabytes.
(b) The interest rate fixed price receiver includes the net notional dollar value of the interest rate sensitive component of the combined commodity portfolio. The remaining interest rate fixed price receiver and the entire interest rate fixed price payor represent the notional contract amount of a portfolio of various financial instruments used to hedge the net present value of the commodity portfolio. For a given unit of price protection, different financial instruments require different notional amounts.
(c) Excludes derivatives on Enron common stock. See Notes 10 and 11.

Enron also has sales and purchase commitments associated with commodity contracts based on market prices totaling 8,169 TBtue, with terms extending up to 16 years, and 7.2 million metric tonnes, with terms extending up to 5 years.

Notional amounts reflect the volume of transactions but do not represent the amounts exchanged by the parties to the financial instruments. Accordingly, notional amounts do not accurately measure Enron's exposure to market or credit risks. The maximum terms in years detailed above are not indicative of likely future cash flows as these positions may be offset in the markets at any time in response to the company's price risk management needs to the extent available in the market.

The volumetric weighted average maturity of Enron's fixed price portfolio as of December 31, 2000 was approximately 1.5 years.

Fair Value. The fair value as of December 31, 2000 and the average fair value of instruments related to price risk management activities held during the year are set forth below:

(In millions)	Fair Value as of 12/31/00 Assets	Fair Value as of 12/31/00 Liabilities	Average Fair Value for the Year Ended 12/31/00(a) Assets	Average Fair Value for the Year Ended 12/31/00(a) Liabilities
Natural gas	$10,270	$ 9,342	$ 5,525	$ 5,114
Crude oil and liquids	1,549	3,574	1,402	2,745
Electricity	7,335	5,396	3,453	1,613
Other commodities	1,509	1,311	988	757
Equity investments	795	295	492	280
Total	$21,458	$19,918	$11,860	$10,509

(a) Computed using the ending balance at each month-end.

The income before interest, taxes and certain unallocated expenses arising from price risk management activities for 2000 was $1,899 million.

Securitizations. From time to time, Enron sells interests in certain of its financial assets. Some of these sales are completed in securitizations, in which Enron concurrently enters into swaps associated with the underlying assets which limits the risks assumed by the purchaser. Such swaps are adjusted to fair value using quoted market prices, if available, or estimated fair value based on management's best estimate of the present value of future cash flow. These swaps are included in Price Risk Management activities above as equity investments. During 2000, gains from sales representing securitizations were $381 million and proceeds were $2,379 million ($545 million of the proceeds related to sales to Whitewing Associates, L.P. (Whitewing)). See Notes 4 and 9. Purchases of securitized merchant financial assets totaled $1,184 million during 2000. Amounts primarily related to equity interests.

Credit Risk. In conjunction with the valuation of its financial instruments, Enron provides reserves for credit risks associated with such activity. Credit risk relates to the risk of loss that Enron would incur as a result of nonperformance by counterparties pursuant to the terms of their contractual obligations. Enron maintains credit policies with regard to its counterparties that management believes significantly minimize overall credit risk. These policies include an evaluation of potential counterparties' financial condition (including credit rating), collateral requirements under certain circumstances and the use of standardized agreements which allow for the netting of positive and negative exposures associated with a single counterparty. Enron also minimizes this credit exposure using monetization of its contract portfolio or third-party insurance contracts. The counterparties associated with assets from price risk management activities as of December 31, 2000 and 1999 are summarized as follows:

(In millions)	2000 Investment Grade(a)	2000 Total	1999 Investment Grade(a)	1999 Total
Gas and electric utilities	$ 5,050	$ 5,327	$1,461	$1,510
Energy marketers	4,677	6,124	544	768
Financial institutions	4,145	4,917	1,016	1,273
Independent power producers	672	791	471	641
Oil and gas producers	1,308	2,804	379	688
Industrials	607	1,138	336	524
Other	256	357	59	67
Total	$16,715	21,458	$4,266	5,471
Credit and other reserves		(452)		(337)
Assets from price risk management activities(b)		$21,006(c)		$5,134

(a) "Investment Grade" is primarily determined using publicly available credit ratings along with consideration of cash, standby letters of credit, parent company guarantees and property interests, including oil and gas reserves. Included in "Investment Grade" are counterparties with a minimum Standard & Poor's or Moody's rating of BBB- or Baa3, respectively.
(b) One and two customers' exposures, respectively, at December 31, 2000 and 1999 comprise greater than 5% of Assets

From Price Risk Management Activities and are included above as Investment Grade.

(c) At December 31, 2000, Enron held collateral of approximately $5.5 billion, which consists substantially of cash deposits shown as "Customers' Deposits" on the balance sheet.

This concentration of counterparties may impact Enron's overall exposure to credit risk, either positively or negatively, in that the counterparties may be similarly affected by changes in economic, regulatory or other conditions. Based on Enron's policies, its exposures and its credit reserves, Enron does not anticipate a materially adverse effect on financial position or results of operations as a result of counterparty nonperformance.

During 2000, the California power market was significantly impacted by the increase in wholesale power prices. California customer rates are currently frozen, requiring the utilities to finance the majority of their power purchases. If wholesale prices remain at the current levels and no regulatory relief or legislative assistance is obtained, certain California utilities may need to seek bankruptcy protection. During 2000, Enron entered into wholesale power transactions with California utilities, including their nonregulated power marketing affiliates. Enron has provided credit reserves related to such activities based on Enron's net position with each California utility. Due to the uncertainties surrounding the California power situation, management cannot predict the ultimate outcome but believes these matters will not have a material adverse impact on Enron's financial condition.

Non-Trading Activities. Enron also enters into financial instruments such as swaps and other contracts primarily for the purpose of hedging the impact of market fluctuations on assets, liabilities, production or other contractual commitments.

Energy Commodity Price Swaps. At December 31, 2000, Enron was a party to energy commodity price swaps covering 18.6 TBtu, 29.9 TBtu and 0.5 TBtu of natural gas for the years 2001, 2002 and 2003, respectively, and 0.3 million barrels of crude oil for the year 2001.

Interest Rate Swaps. At December 31, 2000, Enron had entered into interest rate swap agreements with an aggregate notional principal amount of $1.0 billion to manage interest rate exposure. These swap agreements are scheduled to terminate $0.4 billion in 2001 and $0.6 billion in the period 2002 through 2010.

Foreign Currency Contracts. At December 31, 2000, foreign currency contracts with a notional principal amount of $1.4 billion were outstanding. These contracts will expire $1.0 billion in 2001 and $0.4 billion in the period 2002 through 2006.

Equity Contracts. At December 31, 2000, Enron had entered into Enron common stock swaps, with an aggregate notional amount of $121 million, to hedge certain incentive-based compensation plans. Such contracts will expire in 2001.

Credit Risk. While notional amounts are used to express the volume of various financial instruments, the amounts potentially subject to credit risk, in the event of nonperformance by the third parties, are substantially smaller. Forwards, futures and other contracts are entered into with counterparties who are equivalent to investment grade. Accordingly, Enron does not anticipate any material impact to its financial position or results of operations as a result of nonperformance by the third parties on financial instruments related to non-trading activities.

Financial Instruments. The carrying amounts and estimated fair values of Enron's financial instruments, excluding trading activities, at December 31, 2000 and 1999 were as follows:

	2000		1999	
(In millions)	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Short- and long-term debt (Note 7)	$10,229	$10,217	$8,152	$8,108
Company-obligated preferred securities of subsidiaries (Note 10)	904	920	1,000	937
Energy commodity price swaps	-	68	-	(3)

Interest rate swaps	-	1	-	(55)
Foreign currency contracts	-	94	-	-
Equity contracts	15	15	4	4

Enron uses the following methods and assumptions in estimating fair values: (a) short- and long-term debt - the carrying amount of variable-rate debt approximates fair value, the fair value of marketable debt is based on quoted market prices and the fair value of other debt is based on the discounted present value of cash flows using Enron's current borrowing rates; (b) company- obligated preferred securities of subsidiaries - the fair value is based on quoted market prices, where available, or based on the discounted present value of cash flows using Enron's current borrowing rates if not publicly traded; and (c) energy commodity price swaps, interest rate swaps, foreign currency contracts and equity contracts - estimated fair values have been determined using available market data and valuation methodologies. Judgment is necessarily required in interpreting market data and the use of different market assumptions or estimation methodologies may affect the estimated fair value amounts.

The fair market value of cash and cash equivalents, trade and other receivables, accounts payable and investments accounted for at fair value are not materially different from their carrying amounts.

Guarantees of liabilities of unconsolidated entities and residual value guarantees have no carrying value and fair values which are not readily determinable (see Note 15).

George Serice
11/13/2000 05:30 PM

GSF: George.Serice@Chase.com 713-216-8079 Fax Number 713-216-4583

To: Richard S. Walker/CHASE
cc: Robert Traband/CHASE@CHASE
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

That's a knife, man.

I suppose the insurance company surety option is out.

Richard S. Walker

Richard S. Walker
11/13/2000 04:12 PM

To: Richard S. Walker/CHASE@CHASE, Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, George Serice/CHASE@CHASE, Christopher Lowe/CHASE@CHASE, Christopher Teague/CHASE@CHASE
cc:
Subject: Call Report for ENRON NORTH AMERICA CORPORATIO

---------- Forwarded by Richard S. Walker/CHASE on 11/13/2000 04:13 PM ----------

CHASE

Call Report

ENRON CORPORATION

ENRON NORTH AMERICA CORPORATIO

Client Attendees:	Chase Attendees:	CC: List:
Joe Dettner	Richard S. Walker Jeffrey W. Dellapina	Robert Traband George Serice Christopher Lowe Christopher Teague
Level of Attendees:	Filing Officer(s):	Exec. Committee/ Sr. Mgmt. Attendees:
CFO	Richard S. Walker	H&Q & Flemings Attendee/Referral:

Call Date: [illegible] Call Type: In Person

FOIA Confidential Treatment Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #137

SENATE
MAH - 02504

Meeting Details:
Talked to Joe about his interest in a 4th quarter prepay. Joe is looking for $500 MM essential to fill the liquidity gap resulting from the delay in closing the big asset sales of Portland General and the Southern Cone assets.

The challenge is that Deffner wants a structure that gets non-debt treatment on his balance sheet. Chase on the other hand needs to use the form of a physical swap (vs financial swap) in order to get favorable MTM accounting treatment. Currently the default swap market is not an attractive alternative to selling down our risk position.

We concluded that there were probably three funding alternatives beyond our usual execution -

- A CP conduit - the challenge here is disclosure in the public domain
- Bank syndication - timing is the issue unless we are willing to hold even more Enron risk over year end.
- Private placement - this would be a welcomed alternative

Joe is willing to go to a shorter tenor if necessary - say two years versus the last several deals which have been five years

Relationship Information:

Follow-Up:

Product(s) Discussed: Derivatives

Confidential? N

Y = Yes = Call Report viewable by Chase Attendees and CC : Only

N = No = Call Report viewable by all Authorized Users

Client Type: B
Client Unit(s): Oil & Gas
Industry Client Exec: RICHARD S WALKER
Geography Client Exec:
Country of Domicile: UNITED STATES
Country of Transaction: UNITED STATES

Created By:
Richard S Walker

Edit History:
[illegible] PM Richard S Walker - Mailed -

SENATE
MAH - 0250[illegible]

[illegible]A Confidential Treatment
[illegible] Requested by JPMC

Enron Corporation - Structuring Summary
GIB Deal Team: T. Benton, MD; G. Serice, VP; J. Bieser, Assoc.
Client Manager: R. Walker, VP; S. Aultman, Assoc.
Credit Deputy: Ron Potter, MD
Timing: Closing: December 1996

Industry:	Diversified Energy	**Primary SIC Code(s):**	1321
Company Headquarters:	Houston, TX	**Major Plant Locations:**	NA
Major Overseas Ops:	N/A		
Ratings (LT & ST):	Sr. Unsec. BBB+/Baa2 Sub. Debt BBB/Baa3 Commercial Paper A2/P2	**Ratings Outlook/Trend?**	Currently on watch for possible upgrade
Date Ratings Last Changed:	12/08/95	**Date Last Reaffirmation:**	NA
Stock Price (as of 11/1/96)	$46 1/8	**52 Wk High/Low**	$46 1/8 / $32 1/2
Market Capitalization:	$10,528MM	**Market Cap/Book Cap**	2.9x
Bond Spreads:	NA	**Bond Description**	

Product Description / Nature of Deal

Enron Corporation ("Enron") has requested that Chase underwrite a $300,000,000 Performance Letter of Credit ("PLC") to backstop its natural gas delivery performance obligation resulting from its guaranty of a subsidiary as a counterparty to a Prepaid Natural Gas Sale. The Facility calls for the delivery of a certain dollar amount of gas in quarterly amortizing payments over 3 years with an average life of 1.5 years. PLC fees will be based on an applicable Eurodollar margin determined by Enron's senior debt rating as follows:

≥ BBB+/Baa1	BBB/Baa2	BBB-/Baa3	≤ BB+/Ba1
20.0 bps	22.5 bps	40.0 bps	52.5 bps

The transaction calls for Chase to advance funds to a Special Purpose Corporation formed by Chase in the Channel Islands (Mahonia Limited). Mahonia in turn enters into a Forward Gas Sales Contract (referred to as a "prepay") with an Enron Subsidiary, Enron Natural Gas Marketing Corp. An integral part of the prepay is the execution of a series of commodity and interest rate swaps which result in a known cash flow stream. As in prior prepay transactions, Chase will retain the natural gas delivery risk associated with these swaps. Through a guaranty, Enron unconditionally guarantees the obligation of its subsidiary to deliver natural gas. Enron's obligations under the guaranty are in turn supported by the syndicated PLC. Any drawings under the PLC in the event of Enron's failure to cause its subsidiary to perform under the prepay will be paid to Chase in satisfaction of its original funding to Mahonia.

The PLC fee reflects the diminished capital required for a performance letter of credit in the syndication of Enron performance risk. Because such an instrument is less capital attractive than a funded asset, syndicate banks will accept reduced letter of credit fees.

Enron has the option, 15 days in advance of deliveries, to select up to two of nine of the most liquid physical delivery points for gas, these nine points being defined in advance. This added flexibility will help minimize transaction costs associated with delivery at a NYMEX location such as Henry Hub.

Given that price and interest rate risk will be mitigated in the swap market, the principal risk associated with this transaction is natural gas delivery risk. We are comfortable that, as the largest vertically integrated natural gas concern in the US, Enron is fully capable of managing its performance obligations. Note that during 1995, Enron Capital and Trade Resources was the largest buyer and seller of natural gas in North America with physical volumes of 7.2 BCF/day and financial settlements of 32.9 BCF/day. Assuming straight line delivery, the gas associated with this transaction represents less than 1/2 of 1% of Enron's merchant activities.

DIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

Permanent Subcommittee on Investigations
EXHIBIT #138

JPM-1-00001

Chase Relationship and Competition

Relationship

Chase has significantly improved its relationship with Enron over the past five years, beginning with Chase's 1991 $25 million participation in Enron's flagship $600 million R/C facility. In June 1993, Chase earned the Administrative Agency on the $1 billion facility, and currently holds $20 million in the facility and is in the process of amending the facility. Chase also agents the $470 million JEDI R/C facility with a hold position of $35 million and is in the process of amending the facility.

Competition

Chase Client Management suspects that Enron may have approached Citibank and Nations for proposals for the current prepay transaction. However, as a result of our PLC structure and continued innovation, we have underwritten and syndicated four of Enron's seven prepays and are confident of our ability to secure the mandate with a committed underwriting.

Company Overview

Enron Corp. ("Enron"), with approximately $15 billion in assets, is one of the world's largest integrated natural gas and electricity companies. Enron transports and markets natural gas throughout the U.S. via 44,000 miles of pipelines. The Company explores for and produces natural gas throughout the world and markets natural gas liquids, crude oil and refined petroleum products internationally. The Company also sells and produces cogenerated steam and electricity. Enron is North America's #1 buyer and seller of natural gas.

Enron is publically owned and its stock trades on the NYSE as ENE. Enron employs approximately 6,700 persons and employees own approximately 14% of the Company. Enron's revenues for the first nine months of 1996 were $9.2 billion compared to $6.6 billion in 1995. Net income for the same period increased 15% from $389.6 million in 1995 to $452.4 million in 1996. The Company is organized into 5 major subsidiaries outlined as follows:

Enron Operations (EOC) handles about 15% of the natural gas and 4% of the natural gas liquids consumed in the U.S. It also builds and manages worldwide natural gas transportation, power generation, liquids, and clean fuels facilities. EOC reported EBIT of $442MM in 1995, prior to $83MM of fourth quarter charges primarily related to reserves established for litigation and regulatory matters, compared to $403MM in 1994. These results include earnings from the interstate pipelines and the construction, management and operation of assets worldwide.

Enron Capital and Trade Resources (ECT) manages the world's largest portfolio of natural gas-related risk management contracts (futures and swaps) and is the leading supplier of natural gas to the U.S. electric generation industry. Through its affiliates, Enron Capital and Trade Resources owns or has access to two intrastate pipelines and several storage facilities. ECT's businesses include cash/physical transactions, risk management products and finance activities in natural gas, natural gas liquids, crude oil and electricity.

During 1995, ECT continued to increase market share in its core natural gas business, established its position as the largest non-regulated electricity wholesaler, commenced commercial activities in Europe, and demonstrated continued effectiveness of its risk management processes and controls. ECT's EBIT increased from $202MM in 1994 to $232MM in 1995 prior to a $75MM non-recurring charge related to its clean fuels plant operations. Earnings from physical contracts of one year or less involving marketing and transportation of natural gas, liquids, electricity and other commodities declined to $146MM in 1995 from $170MM in 1994. ECT's earnings from its risk management operations, which consist of market activity on long-term contracts improved to $193MM in 1995 compared to $151MM in 1994. ECT's finance operations, which provide capital to customers through various product offerings including volumetric production payments contributed $31MM to ECT's earnings in 1995, compared to $13MM in 1994.

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Company Overview *(continued)*

Enron Development and Enron Global Power & Pipelines (Enron holds a 52% interest) builds and operates power plants and pipelines in such emerging-market economies as China, Guatemala, and the Philippines. The Company also operates a natural gas pipeline in Argentina and has signed a deal with Russia's Gazprom to help the state-owned company market gas in Europe. The segment reported EBIT of $142MM in 1995 compared to $148MM in 1994.

Enron Oil & Gas Company (EOG) (rated A- by S&P), is one of the leading low-cost, fast-track, independent E&P companies in the U.S. with an increasing presence in international markets. Enron Oil & Gas is 61% owned by Enron. The Company's proved reserves are 88% North American and 92% natural gas. In December, 1995, Enron reduced its ownership in EOG to 61% from 80% with the sale of approximately 31 million shares of EOG stock. As a result of the reduced ownership, EOG is no longer included in Enron's consolidated federal income tax return. Exploration and Production's EBIT rose to $241MM in 1995, compared to $198MM in 1994. The results include $45MM and $35MM, respectively, related to hedges placed on open commodity positions by Enron independent of EOG. Exploration and development expenditures were $519MM in 1995, compared to $501MM in 1994.

Key Issues and Challenges

- Enron has executed seven prepaid sale transactions, so the banks are generally familiar with the proposed prepay structure. Four of the seven have been underwritten and syndicated by Chase.
- The facility is for back up purposes and is not expected to be drawn.
- Banks will be paid an upfront fee of 6.0 bps on allocated commitments.
- Capacity - Individual banks' total Enron family exposure may be an issue.

	Current Deal (if any)	First Cut at Proposed Deal	Final Deal
Amount		$300MM	
Tenor		3 year	
Commitment Amount		$300MM	
Hold Amount		$25MM	
Undrawn Cost		NA	
Drawn Cost		20.0 bps	
Utilization Fee		No	
Grid ?		Yes	
Upfront Fees to Market		6 bps on average	
Underwriting Fee (if U/W)		[30 bps]	
Funded ?		No	
Secured ?		No	
Agent		Chase	

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Credit Statistic & Synopsis

Credit Statistics- Fair Value Accounting Method *Dollars in Millions*	FYE 12/31/93	FYE 12/31/94	FYE 12/31/95	Six Months 6/30/96
Revenues	7,986	8,984	9,189	6,015
EBITDA	1,089	1,157	1,050	676
EBIT	631	716	618	447
EBIT/Interest	2.10	2.62	2.18	3.31
Total Debt/EBITDA	2.44	2.42	2.92	4.92
Current Ratio	0.75	0.83	1.12	1.25
Fixed Charge Coverage	3.91	1.73	1.98	4.78
Total Debt / Total Capital	50.4%	49.3%	49.2%	45.8%

Six Months Ending June 30, 1996:

Enron Corp. said second quarter net income rose 24% as it benefited from higher natural gas prices as well as improvements in its pipeline, trading and electricity businesses. The results exceeded Wall Street expectations.

Revenues increased 35% to $6B for the first half of 1996 compared to $4.4B for the first half of 1995. Earnings increased 7.5% as a result of an increase in earnings in its transportation segment and its domestic and international gas and power services. This increase was partially offset by a decrease in earnings in the Company's exploration and production segment and in its corporate and other segment.

Earnings in the Company's Transportation and Operation segment increased 34% to $334MM in the first half of 1996 compared to $250MM in the first half of 1995. The increase in earnings is primarily due to a 72% decline in expenses for the first 6 months of 1996, primarily as a result of decreased purchases by Northern Natural, as that pipeline is now exclusively a transporter of natural gas. In addition, operating expenses declined 21% in the first 6 months of 1996 as a result of lower operating expenses on the interstate pipelines and reduced expenses related to gathering facilities sold during 1995 and the first quarter of 1996.

In the Company's Domestic Gas and Power segment, earnings increased $52MM to $150MM for the first 6 months of 1996 as a result of an increase in the Company's cash and physical operations' earnings to $130MM for the first 6 months of 1996 compared to $49MM for the first 6 months of 1995. The earnings from this unit increased primarily due to earnings from higher margins for natural gas and increased earnings from electricity marketing. Earnings from the management of ECT's portfolio of contracts also increased in 1996. These increases were partially offset by a decrease in earnings from gas processing. Earnings before overhead expenses for the risk management business were $60MM in the first 6 months of 1996 and $84MM in the same period in 1995. Earnings from this unit decreased primarily due to lower originations from long-term contracts with utilities and independent power plants, which were partially offset by increased originations for electricity and originations in the European market.

Earnings in the Company's International Gas and Power Services segment increased $4MM to $79MM in the first 6 months of 1996 primarily because of a $9MM decline in operating expenses due to the transfer of marketing operations to the domestic gas and power services segment beginning in January, 1996.

In the Company's Exploration and Production segment, earnings declined to $107MM for the first 6 months of 1996 compared to $107MM for the first 6 months of 1995. Although wellhead natural gas prices and production volumes increased in the first half of 1996, this increase was more than offset by lower results from commodity price swap transactions and a decrease in gains on sales of oil and gas reserves and related assets.

In the Company's Corporate & Other Segment, earnings decreased $26MM to $10MM in the first half of 1996. The $10MM includes gains of $45MM related to the sale of 2.6MM shares of EOG stock held by Enron Corp., partially offset by a $25MM reserve established for litigation contingencies.

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Supply/Demand Dynamics
Adequate capacity to syndicate the proposed facility, although the proposed transaction will come on the heels of a $470 million JEDI facility amendment and an amendment to the $1,000 million Enron Corp Revolver.

Brief Discussion of Most Comparable Recent Transactions (ie: why comparable)
Comparable transactions include natural gas and crude oil prepays with Enron. Summary terms of the deals were as follows:

- 1994 Crude Oil Prepay: $208MM 5 year PLC with pricing of 30.0 bps and upfront fees of 5.0 and 10.0 bps for commitments of $15,000,000 and $30,000,000, respectively.
- 1995 Natural Gas Prepay: $225MM 5 year PLC with pricing of 30 bps and upfront fees of 2.5, 5.0, and 10.0 for commitments of $10,000,000, $20,000,000 and $30,000,000, respectively.

Syndication Strategy
We are confident in the ability to execute this transaction targeting prior prepay transaction banks and Enron Corp. banks. We plan to payout 6.0 bps on average to participants with the following tiers:

Commitment Amount	Upfront Fee
$10,000,000	[2.5] bps
$20,000,000	[5.0] bps
$30,000,000	[10.0] bps

We plan to approach the current Prepay transaction bank groups listed below:

	1994 Prepay $208 MM	1995 Prepay $225 MM
ANZ Bank	$15	
Banca di Roma	$15	$10
Bayerische Vereinsbank		$18
BCI	$15	
Chase	$28	$22
Credit Lyonnais		$18
Dai-ichi Kangyo	$15	$10
DG Bank Deutsche		$20
Fuji	$15	
Gulf International	$15	$10
IBJ	$15	
LTCB	$30	$20
Mitsubishi		$20
Mitsui Trust		$10
Sakura		$10
Standard Chartered	$15	
Sumitomo	$30	
Sumitomo Bank		$20
West LB		$20
Yasuda		$18
Total	$208	$225

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Syndication Strategy *(continued)*
And, additionally, we plan to approach the following Enron Corp. banks:

Scotia Bank	Credit Lyonnais
Citicorp	Bank of America
Barclay's	Toronto Dominion
Bank of New York	First Chicago

Cross-Sell Opportunities and Strategy
Commodity derivatives and interest rate swaps.

Approval Signatures

	Name (Print)	Signature
GIB Lead Transactor:	Tod Benton	
	George Serice	
Senior Banker:	Richard Walker	
Credit Deputy:	Ron Potter	
Credit Deputy:	Edward Nelson	
Additional Approvals (as required):	Howard Schramm	

FOIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

STRUCTURING SUMMARY

Enron Corp. - 1997 Prepay

GIB Deal Team: G. Serice Client Executive/Lender: R. Walker/S. Aultman

Credit Executive: R. Potter, J. Biello

Maximum Exposure for Approval (SMM):	$1,767MM	Industry Description:	Diversified Energy
Transaction for Approval ($MM):	[$250MM]	Primary SIC Code:	1321
Customer Name:	Enron Corp.		
Obligor/Facility Risk Grade:	3/3	Major Plant Locations:	
Parent Name: Parent Risk Grade:	Enron Corp. 3	Major Overseas Ops: TREND: Improving/Stable/Declining	
Public Ratings (LT & ST): *Enron Corp.* (ENE)	Senior Unsecured: BBB+/Baa2 Subordinated Debt: BBB/Baa3 Commercial Paper: A2/P2	Ratings Outlook/Trend:	Ratings reaffirmed by S&P and Moody's on 6/2/97 and 6/4/97, respectively.
Date Ratings Last Changed:	S&P upgrade on December 8, 1995	Date Last Reaffirmation:	6/2/97 (S&P) 6/4/97 (Moody's)
Enron Stock Price (as of 9/18/97):	$39 3/16	52 Wk High/Low:	$47.50/$35.00
Market Capitalization:	$11,924MM	Market Cap/Book Cap:	2.25x
Bond Spreads:		Bond Description:	

Executive Summary

We are requesting approval to arrange and underwrite up to a [$250MM] Performance Letter of Credit ("PLC") to backstop Enron's gas delivery performance obligation as a result of its guarantee of the performance of a subsidiary, as the seller counterparty to a Prepaid Natural Gas Sale. The subsidiary will be Enron Natural Gas Marketing Corp. ("ENGMC"), a wholly owned subsidiary of Enron Corp. Timing for executing the prepay transaction is by December 15 with the closing of the PLC Facility to immediately follow. In addition to attractive pricing, Enron is inclined to use Chase because of our past execution of three Enron Prepays and the availability of "template" documentation. Chase will receive 40 basis points upfront for the underwrite and the PLC fee to the lenders will be 22.5 bps (capital-adjusted yield of 45 bps) for this Enron Corp. (BBB+) PLC.

In the past three years, Enron has utilized the prepaid sale as a mechanism to address a number of needs, including refreshment of Section 29 credits and sourcing funds (classified as "Liabilities from Price Risk Management" as opposed to long term debt). To date, the company has executed eight such transactions, four utilizing 18 month tenors, our last transaction utilizing a three year tenor and the previous three making use of a five year tenor. Five of the eight, totaling $1,089MM, have been underwritten and syndicated by Chase, one by BT, and at least one by Citibank. As a result of our proprietary PLC structure and our continued demonstrated innovation, we have become the first stop for Enron for this type of transaction. All prior prepay transactions have performed as agreed.

Below is a listing of the three transactions (all Chase-led deals) which remain outstanding:

Transaction ($ MM's)	1994 Prepay	1995 Prepay	1996 Prepay
Original Amount	*$207.8*	*$224.5*	*$350.0*
Amount as of 10/97	*$94.8*	*$133.2*	*$286.9*
Amount Repaid/Amortized	*$113.0*	*$91.3*	*$63.1*

CHASE CONFIDENTIAL TREATMENT REQUESTED

Permanent Subcommittee on Investigations
EXHIBIT #139

Transaction Overview

The basic transaction calls for Chase to enter into a Forward Gas Sale Agreement with an Enron subsidiary, Enron Natural Gas Marketing Corp. An integral part of the Forward Gas Sale Contract (referred to as a "Prepay") is the execution of a series of commodity and interest rate swaps which result in a known cash flow stream. As in prior Prepay transactions, Chase will retain the delivery risk associated with these swaps. Through a guaranty, Enron Corp. unconditionally guarantees the obligation of its subsidiary to provide the gas. Enron Corp.'s payment obligations to Chase under the guaranty are in turn supported by a syndicated performance letter of credit ("PLC"). Any drawings under the PLC in the event of Enron's failure to cause its subsidiary to perform under the prepay will be paid to Chase.

Similar to the December 1994 and September 1995 transactions executed with Chase, this structure presents a quarterly amortizing prepayment obligation, over four years, which calls for delivery of a certain dollar amount of gas on each delivery date. With this structure, the gas price for any delivery - and therefore the MMBtu obligation - can be fixed by Enron with the Chase at any time before that delivery date. This feature gives Enron the flexibility to match its delivery obligations, on a delivery date by delivery date basis, with either fixed or floating price sales. As a matter of past practice, Enron has chosen to fix prices on a rolling 13 month horizon. In this structure, deliveries are initially scheduled on a straight line basis subject to volumetric adjustment as Enron fixes the gas price. We have had no problems with the past execution of such balancing adjustments.

Additionally, Enron will have delivery flexibility as in the past structure. Enron will have the option, 15 days in advance of deliveries, to select up to two of nine of the most liquid physical delivery points for gas. These nine points will be defined in advance. This flexibility is present in order for Enron to minimize the transaction costs ($0.03/MMBtu) associated with a delivery at a NYMEX location such as Henry Hub.]

Company's Business

Enron Corporation, one of the world's largest integrated natural gas and electricity companies with approximately $19 billion in assets and operates one of the largest natural gas transmission systems in the world. Enron is the largest purchaser and marketer of natural gas and the largest non-regulated marketer of electricity in North America; is a leading participant in liberalized energy markets in the United Kingdom and the Nordic Countries; markets natural gas liquids worldwide; manages the largest portfolio of fixed-price natural gas risk management contracts in the world; is among the leading entities arranging new capital to the energy industry; and is a major supplier of solar and wind renewable energy worldwide. The Company owns 53 percent of Enron Oil & Gas Company (one of the largest independent, non-integrated exploration and production companies in the United States) and 59 percent of Enron Global Power and Pipelines L.L.C. (an owner and manager of operating power plants and natural gas pipelines around the world).

Chase Relationship

Flagship Revolver - Chase has significantly improved its position with Enron over the past five years, beginning with Chase's 1991 $25MM participation in Enron's flagship $500MM R/C facility. Originally, the flagship was agented by Bankers Trust, however, in June 1993, Chase earned the Administrative Agency on the $1,000MM R/C facility. As compensation for arranging this facility and successfully syndicating it to 53 banks, Chase received a $250,000 arrangement fee, upfront fees of $10,000, $50,000/year in agency fees, and a 20bps flat facility fee paid semiannually. Chase currently holds $36.5MM of the facility. The flagship was recently repriced as follows:

Senior Rating		Pricing
≥A-	=	9.0/25.0
≥BBB+	=	*10.0/30.0*
≥BBB	=	11.0/32.5
≥BBB-	=	15.0/50.0
<BBB-	=	25.0/62.5

FOIA CONFIDENTIAL TREATMENT REQUESTED

Credit Statistics ($millions)	1993	1994	1995	1996	Six Months Ending 6/30/97
Sales	$7,986	$8,984	$9,189	$13,289	$8,595
EBITDA	1,089	1,157	1,050	1,164	(50)
EBIT	631	716	618	690	(299)
Interest	300	273	284	274	149
Senior Debt	2,661	2,805	3,065	3,349	4,537
Total Debt	2,661	2,805	3,065	3,349	4,537
Total Equity	2,619	2,880	3,165	3,723	3,431
EBIT / Cash Interest	2.09x	2.62x	2.18x	2.52x	NA
Total Debt / Book Capitalization	50.4%	49.3%	49.2%	47.4%	56.9%
Total Debt / EBITDA	2.44x	2.42x	2.92x	2.88x	NA

Credit Synopsis

- Enron's long-term debt ratings were affirmed in June by both S&P and Moody's. There had been speculation about a possible upgrade, but due to the J-Block settlement the ratings were left unchanged.

- Enron Corp. reported revenues of $13.3 billion and net income of $584 million during 1996 compared to $9.2 billion and $504 million, respectively, for 1995. For the nine months ending September 30, 1997, Enron reported revenues of $14.4 billion and a net loss of $(64) million compared to $9.24 billion and $453 million, respectively for the same time period in 1996. The net loss was as a result of the $675 million pre-tax settlement charge from Enron's J-Block contract in the North Sea and $100 million pre-tax to reflect depressed MTBE margins on committed production. There were reduced earnings in the transportation and operations and exploration and production segments, losses realized by the newly formed retail energy services group and increased interest charges and dividends on company-obligated preferred securities of subsidiaries. An income tax benefit of $251 million partially offset the effect of the non-recurring charges.

Proposed Prepay Deal Terms	
Obligor	Enron Corp.
Beneficiary	"Buyer" in Prepay transaction
Amount	up to $250MM
Tenor	4 Years (with an average life of 2.5 to 3 years)
Commitment Amount	$250MM
Hold Amount	$35MM
Participation Fee	4-10 basis points with an avg of 7.5 bps (same as Dec 1996 Prepay)
Arrangement Fee	40 basis points (vs. 35 bps for 1996 Prepay)
Funded ?	No
Secured ?	No
Guaranteed?	No
Administrative/Syndication Agent	Chase
PLC Fee	22.5 bps (PLC carries 50% capital weighting, adjusted yield of 45 bps)
Facility Fees	N/A

Exposure

The transaction incorporates a performance letter of credit (as in prior transactions) to syndicate Enron's gas delivery performance obligation. We will participate the PLC to a broad syndicate so that our net Enron performance exposure will approximate $35MM. This PLC is similar to a syndicated R/C in that Chase will not front the LC, avoiding incurrence of various bank credit exposures. Instead Chase, as in the past, will syndicate the LC on a several obligation basis.

The mark to market exposure on this transaction is approximately 20% of the principal amount, assuming prices are locked in by Enron on day one for the entire contract horizon. However, with the addition of required collateral for

adverse price movements, the current maximum actual mark to market exposure is $10MM, growing to $50MM if Enron were to achieve an AA- rating. Chase GRM will evaluate the actual mark to market exposure on a daily basis and require LCs, cash, or treasuries for exposure in excess of the thresholds stated as follows:

Rating	Threshold
AA- or better	$50MM
A- or better	$15MM
BBB or better	$10MM
BBB-	$ 0

We have set the LIBOR margin used to discount the value of the deliveries at an initial level of 27.5 bps. Our ability to offer this competitive margin is facilitated by the use of the performance letter of credit in the syndication of Enron performance risk. Because such an instrument is less capital attractive than a funded asset, syndicate banks will accept reduced letter of credit fees (which are paid from the implicit interest component in the discounted prepay). The second component of Chase compensation is the proposed arrangement fee. The proposed arrangement fee of 40 bps produces a favorable loan pricing model result, as shown in the attached model.

Key Syndication Issues

Highlights:

- **Strong Credit** - BBB+/Baa2 investment grade ratings.
- **Marquee Name** - one of the world's largest integrated natural gas and electricity companies.
- **Financial Strength** - $19 Billion in Assets. Market capitalization of $11.924 Billion.
- **Strong bank following** - 70 banks currently have commitments to Enron.

Challenges:

- **Capacity** - Individual bank's total Enron family exposure is always a consideration, although pre-screening of most all of the co-agents and upper tier players in the December 1996 Prepay reveals capacity and interest in the transaction, with the one caveat being competing Enron paper in the market in the 4Q. In December 1995, we raised $650MM for a $350MM PLC. In addition, GSF-London recently syndicated a [$215] million 364-day multi-currency facility which was over 2x oversubscribed (pricing was 3 undrawn and 30 drawn) and brought new banks to the relationship. The yield on the Prepay transactions are higher than many of Enron's "corporate obligation" paper. Please see Supply and Demand Chart.
- **Enron's debt to capitalization** has increased from 47% to 57% due to the J-Block settlement in June. However, this ratio should lower in the third quarter due to the equity issuance from the PGC merger.

Cross-Sell Opportunities and Strategy

Chase continues to be a first tier bank to Enron and is one of its top two agents (Citi being our principal competition). During 1996 and 1995 respectively, Chase earned $4.6MM and $2.9MM from the Enron relationship.

CIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

Prepaid Hydrocarbon Forward Sale
Floating Price Facility

This outline is for discussion purposes only. Any commitment to lend is subject to completion of The Chase Manhattan Bank's due diligence review and is further contingent upon credit approval by The Chase Manhattan Bank and the execution and delivery of mutually acceptable legal documentation. No commitment should be construed or implied herein. The following terms are indicative only and additional terms may be incorporated into final documentation.

TERM: [4] Years.

AMOUNT: Up to [$250] million payment for future deliveries of natural gas.

CONTRACT PARTIES:
Purchaser: The Chase Manhattan Bank.
Seller: A wholly owned subsidiary of Enron Corporation.

NATURAL GAS DELIVERIES: Equal [quarterly] installments from [January 1998] to maturity.

FLOATING PRICE FACILITY: [Each hydrocarbon delivery obligation will equal, in MMBtu of gas a set dollar amount*. The hydrocarbon price for any delivery - and therefore the MMBtu/crude oil obligation - can be fixed by Enron with the SPC at any time before that delivery date. Enron also has the facility to initially position its gas/oil sales to [Chase] to any date(s) before the final delivery dates (with the intention to roll out to each final delivery date). The roll adjustment is expressed in terms of incremental MMBtus of gas/oil.]

*[The choice of hydrocarbon for each delivery is at Enron's election.]

REVENUE PREPAYMENT COST: Hydrocarbon revenues prepaid at a rate of LIBOR plus a margin determined by senior debt rating as follows:

≥ BBB+/Baa1	BBB/Baa2	BBB-/Baa3	≤ BB+/Ba1
27.5 Bps	30.0 Bps	47.5 Bps	60.0 Bps

Adjustments in LIBOR margin during contract term shall be made through adjustments in volumes delivered to be determined at the end of the term.

ARRANGEMENT FEE: 0.40%

COSTS: Legal fees, including those associated with syndication, and customary transaction costs.

DOCUMENTATION: Standard documentation with the addition of the Security Agreement attached to the Enron Risk Management Services-Chase ISDA trading agreement, to cover collateral for mark-to-market exposures.

SYNDICATION: Enron performance obligation, pursuant to guarantee of Seller delivery obligation, to be syndicated through a performance letter of credit ("PLC"). PLC upfront and usage costs to be paid by Chase.

FOIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

NATURAL GAS PHYSICAL DELIVERY TERMS

PHYSICAL DELIVERY:

1. Seller's obligation to deliver Natural Gas under the terms of the Prepaid Forward Sale contract can be satisfied by delivery to Purchaser at any of the following locations or such other delivery point(s) as shall be mutually agreed among Purchaser and Seller:

   Columbia Gulf Transmission
   Louisiana Onshore

   Tennessee Pipeline (mainline points)
   Louisiana - 800 Leg
   Louisiana - 500 Leg

   Texas Eastern Transmission
   East Louisiana
   West Louisiana

   Texas Gas Transmission
   Zone SL

   Transcontinental Gas Pipeline
   Zone 3 (Station 65)

   Katy

   Permian
   El Paso pool

   Seller will arrange appropriate transportation to delivery point. Title transfer occurs at delivery location.

2. For any delivery month Seller may deliver gas at up to any three of the locations set out above. Seller may make its election of location(s) at any time not later than 10 business days preceding the delivery month.

3. The process of establishing the final physical price is as follows:

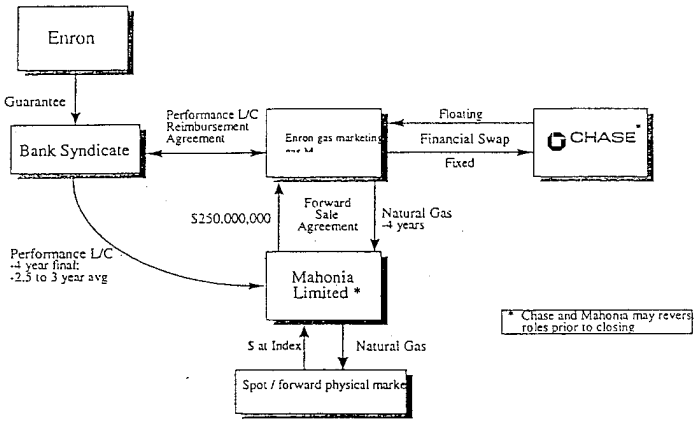
   Seller will sell physical gas to Purchaser at NYMEX *less* a benchmark discount of 5 cents/MMBtu for delivery as above.

   When Seller makes its election of delivery point(s), Purchaser will establish in consultation with Seller the *exchange for physical* ("EFP") discount attaching to the delivery point(s). The benchmark discount will be adjusted by the EFP cost to determine the final physical price.

4. To the extent that the establishment of the final physical price as provided above results in an over or under delivery of gas, the excess or deficit shall be carried over to the next month's obligation.

IA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

Transaction Schematic



DIA CONFIDENTIAL TREATMENT
REQUESTED BY JPMC

Existing Prepay Bank Groups

Transaction ($ MM's)	1994 Prepay		1995 Prepay		1996 Prepay	
Original Amount	*$207.8*		*$224.5*		*$350.0*	
Amount as of 10/97	*$94.8*		*$133.2*		*$286.9*	
Amount Repaid/Amortized	*$113.0*		*$91.3*		*$63.1*	
Bank Group	Original Commitment	%	Original Commitment	%	Original Commitment	%
ANZ	15.0	*7.22*			7.50	*2.14*
Banca di Roma	15.0	*7.22*	10.0	*4.45*		
Bank Brussels Lambert					15.0	*4.29*
Bank Hapoalim					12.5	*3.57*
Bank of America					20.0	*5.71*
Bank of Montreal					20.0	*5.71*
Bank of New York					15.0	*4.29*
Bank of Tokyo-Mitsubishi					12.5	*3.57*
Bank of Yokohama					7.5	*2.14*
Bayerishe Vereinsbank			17.54	*7.81*	12.5	*3.57*
BCI	15.0	*7.22*			20.0	*5.71*
Chase	27.8	*13.38*	22.0	*9.79*	22.5	*6.43*
Commerzbank					20.0	*5.71*
Credit Lyonnais			17.54	*7.81*		
Credit Suisse					12.5	*3.57*
Dai-Ichi Kangyo Bank	15.0	*7.22*	10.0	*4.45*		
DG Bank Deutsche			20.0	*8.90*	15.0	*4.29*
Fuji Bank	15.0	*7.22*			7.5	*2.14*
Gulf International Bank B.S.C.	15.0	*7.22*	10.0	*4.45*	7.5	*2.14*
IBJ	15.0	*7.22*			20.0	*5.71*
Long-Term Credit Bank	30.0	*14.44*	20.0	*8.90*	20.0	*5.71*
Mellon					7.5	*2.14*
Mitsui Trust & Banking			10.0	*4.45*	7.5	*2.14*
Royal Bank of Canada					15.0	*4.29*
Sakura Bank			10.0	*4.45*		
Sanwa					20.0	*5.71*
Standard Chartered	15.0	*7.22*				
The Mitsuibishi Bank			20.0	*8.90*		
The Sumitomo Bank, Limited	30.0	*14.44*	20.0	*8.90*	20.0	*5.71*
Westdeutsche Landesbank			20.0	*8.90*		
Yasuda Trust and Banking			17.57	*7.81*		
TOTAL	207.8	*100.0%*	224.62	*100.0%*	350.0	*100.0%*

FOIA CONFIDENTIAL TREATMENT
REQUESTED BY JPMC

STRUCTURING SUMMARY

Enron Corp. - 1998 Prepay

GIB Deal Team: G. Serice Client Executive/Lender: R. Walker/R. Mertensotto

Credit Executive: G. Wright, J. Biello

Maximum Exposure for Approval ($MM):	$MM	Industry Description:	Diversified Energy
Transaction for Approval ($MM):	$250MM	Primary SIC Code:	1321
Customer Name:	Enron Corp.		
Obligor/Facility Risk Grade:	3/3	Major Plant Locations:	
Parent Name: Parent Risk Grade:	Enron Corp. 3	Major Overseas Ops: TREND: Improving/Stable/Declining	
Public Ratings (LT & ST): *Enron Corp.* (ENE)	Senior Unsecured: BBB+/Baa2 Subordinated Debt: BBB/Baa3 Commercial Paper: A2/P2	Ratings Outlook/Trend:	Ratings reaffirmed by S&P and Moody's on 6/2/97 and 6/4/97, respectively.
Date Ratings Last Changed:	S&P upgrade on December 8, 1995	Date Last Reaffirmation:	6/2/97 (S&P) 6/4/97 (Moody's)
Enron Stock Price (as of 5/22/98):	$50 1/16	52 Wk High/Low:	$53 5/16 / $35.00
Market Capitalization:	$16,351MM	Market Cap/Book Cap:	
Bond Spreads:	65-100 bps	Bond Description:	BBB/BBB3

Executive Summary

We are requesting approval to arrange and underwrite up to a $250MM Performance Letter of Credit ("PLC") to backstop Enron's gas delivery performance obligation as a result of its guarantee of the performance of a subsidiary, as the seller counterparty to a Prepaid Natural Gas Sale. The subsidiary will be Enron Natural Gas Marketing Corp. ("ENGMC"), a wholly owned subsidiary of Enron Corp. Timing for executing the prepay transaction is by June 30 with the closing of the PLC Facility to immediately follow. In addition to attractive pricing, Enron is inclined to use Chase because of our past execution and the availability of "template" documentation. Chase will receive 50 basis points upfront for the underwrite and the PLC fee to the lenders will be 30.0 bps (capital-adjusted yield of at least 60.0 bps) with upfronts to average 10 to 12.5 bps for this Enron Corp. (BBB+/Baa2) PLC. Pricing for the 12/97 prepay was 40 for the underwrite, 22.5 PLC fee with 7.5 upfront to lenders. This transaction would replace $135MM of run-off since 10/97 (see chart below) and get Enron off the year-end execution timetable. This runoff plus the pre-screening results give us confidence that sufficient bank capacity exists for this transaction.

In the past three years, Enron has utilized the prepaid sale as a mechanism to address a number of needs, including refreshment of Section 29 credits and sourcing funds (classified as "Liabilities from Price Risk Management" as opposed to long term debt). To date, the company has executed eight such transactions, four utilizing 18 month tenors, our last transaction utilizing a four year tenor (average life of two years) with previous tenors being either three, four or five. Six of the nine, have been underwritten and syndicated by Chase, one by BT, and at least one by Citibank. As a result of our proprietary PLC structure and our continued demonstrated innovation, we have become the first stop for Enron for this type of transaction. All prior prepay transactions have performed as agreed.

Permanent Subcommittee on Investigations
EXHIBIT #140

10/01/97 02:24 PM

To: Stephen Rochford/CHASE@CHASE
cc: Sandra Aultman/CHASE@CHASE
Subject: Enron Exposure $350MM Prepaid

Steve,

As a follow up to my voice mail, at the end of last year, Chase structured a $350 million loan to Enron Corp in connection with a Prepaid Forward Gas Sale. The loan amortizes with the delivery of the gas over the next 3-1/2 years.
The liability was structured as a direct loan with Chase receiving Performance Letters of Credit (PLC) from the various participating banks as support for the loan.
Although GES is showing the full exposure of $350MM which represents the Chase loan, Mr.Biello has asked if the Enron exposure may be misrepresented since in effect we have received 22 PLC's from the various participating banks and perhaps the differential exposure should be transferred to the various Bank's liability and thus not reflected under Enron?

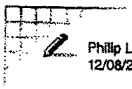
Any thoughts on how this may systematically be adjusted on GES

Thanks & Regards

Peter 713-216-8569

FOIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

Permanent Subcommittee on Investigations
EXHIBIT #141



Phillip Levy
12/08/2000 07:45 AM

Legal (212) 270-5951 Fax Number: (212) 270-7368

To: Julie.Carter@mourant.com
cc: Gareth.EssexCater@mourant.com, Ian.James@mourant.com, Jeffrey W. Dellapina/CHASE@CHASE
Subject: Enron Prepay Transaction

This is to update you on the proposed Enron prepay transaction. At this point, while not a certainty, it looks like we will need to form Mahonia III (it is currently contemplated that the name will be Mahonia Natural Gas Limited; if this presents a problem, let me know). In addition to entering into the prepay with Enron North America, this entity will be entering into a contract to sell its rights to receive gas under the prepay agreement to a group of purchasers, including Chase. In this connection the purchasers will appoint Mahonia III to act as its agent in handling the sale of the natural gas delivered under the Enron contract. The purchaser of the gas in this contract will be Chase. Chase will then sell the gas pursuant to a fixed price forward contract to Stoneville Aegean (an SPV that entered into transactions introduced by Chase in the early to mid 1990's); Stoneville will then sell the gas pursuant to a fixed price forward contract to Enron.

Please advise at your earliest convenience whether Stoneville is still a viable company and has the power to enter into the types of contract contemplated. I am in the process of finalizing a term sheet and diagram that describes the entire transaction and will forward that as soon as it is done. I just wanted to alert you to the Mahonia III formation and the "resurrection" of Stoneville so that you could start the process.

Please feel free to contact me with any questions.

Many thanks and best regards,

Phil

FOIA Confidential Treatment
Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #142

JPMorganChase

Ahuva Genack
Vice President and
Assistant General Counsel
Legal Department

March 27, 2002

The Honorable Billy Tauzin, M.C.
Chairman, Committee on Energy and Commerce

The Honorable John D. Dingell, M.C.
Ranking Member, House Committee on Energy and Commerce

The Honorable James C. Greenwood, M.C.
Chairman, Subcommittee on Oversight and Investigations

The Honorable Peter Deutsch, M.C.
Ranking Member, Subcommittee on Oversight and Investigations

U.S. House of Representatives
House Committee on Energy and Commerce
Washington, D.C. 20515-5115

Dear Congressmen:

I am writing in response to your letter to Mr. William B. Harrison, Jr., dated March 6, 2002, requesting information regarding J.P. Morgan Chase & Co.'s relationship with Enron and its related partnerships, trusts, and special purpose entities (hereinafter collectively "Enron") for the period 1997 to the present.

As you know, J.P. Morgan Chase & Co. is the successor to The Chase Manhattan Corporation ("Chase") and J.P. Morgan & Co., Inc. ("JPM") which merged on December 31, 2000. Prior to the merger, The Chase Manhattan Bank ("CMB") was one of Enron's tier one, or lead, banks. JPM, on the other hand, had relatively limited involvement with Enron.

In preparing a timely response to the Committee, we were unable to identify and retrieve relevant documents from heritage JPM's files, with the exception of materials related to LJM2 Co-Investment, L.P. ("LJM2 Co-Investment"). We believe, though, that, other than with respect to LJM2 Co-Investment, JPM was not involved in matters which are the subject of the Committee's inquiry.

J.P. Morgan Chase & Co. • One Chase Manhattan Plaza, Floor 26, New York, NY 10081
Telephone: 212 552 0918 • Facsimile 212 552 1295
ahuva.genack@chase.com

Permanent Subcommittee on Investigations
EXHIBIT #143

We are also still in the process of identifying and retrieving documents, including archived electronic data and documents. Accordingly, this response and an accompanying production represent our best effort based on the information and materials presently available. We would be pleased to make a supplementary production once our data collection process is completed should the Committee so request.

Request 1:

Please list all securities underwriting, advisory services, including, but not limited to, mergers and acquisitions advisory services, and credit facilities services provided by J.P. Morgan Chase & Co., Mahonia Ltd., Mahonia Natural Gas Ltd., and/or Stoneville Aegean Ltd. for Enron or its SPEs or related partnerships from 1997 to present. Please list the date of each contract or other commitment for such services, the fee or compensation earned by J.P. Morgan Chase & Co. with respect to each such contract, and the date and amount of the underlying transactions.

Response to Request 1:

A summary of the securities underwriting, advisory services and credit facilities services provided by affiliates of J.P. Morgan Chase & Co. (hereinafter, with its affiliates and subsidiaries, "JPMC") is set forth in the enclosed Schedule.

The remaining entities, including Mahonia Limited ("Mahonia"), Mahonia Natural Gas Limited ("Mahonia NG"), and Stoneville Aegean Limited ("Stoneville"), are not owned or controlled by JPMC. JPMC, however, has had a longstanding association with these companies. These entities were incorporated for use in transactions that were to be introduced to them by CMB. To that end, since 1992, the companies have entered into natural gas and oil forward commodity contracts with CMB and its customers, including Enron.

Additional information concerning these companies and Enron-related transactions in which they were involved is provided below in our responses to Requests 6 – 9.

Request 2:

Did J.P. Morgan Chase & Co. invest in, or otherwise provide financing for, any Enron SPEs or related partnerships, including, but not limited to the Raptor and Whitewing entities, the Marlin Water trust, the Osprey Trust and related SPEs, the Nighthawk SPE, the Firefly SPE, the Sequoia SPE, the Choctaw SPE, the Cherokee SPE, the Cheyenne SPE, Chewco Investments, LP., JEDI I and II, LJM 1 and LJM2? If so, please provide the dates and amounts of the investments or financing who authorized them, and the fees or compensation earned by J.P. Morgan Chase & Co.

Response to Request 2:

JPMC provided financing in accordance with the enclosed Schedule. JPMC did not invest in any Enron SPE's or related partnerships other than LJM2 Co-Investment. (See Response to Requests 4 and 5).

Request 3:

Did any J.P. Morgan Chase & Co. employee, officer, or director invest in any Enron SPEs or related partnerships, including, but not limited to, the Raptor and Whitewing entities, the Marlin Water Trust, the Osprey Trust and related SPEs, the Nighthawk SPE, the Sequoia SPE, the Choctaw SPE, the Cherokee SPE, the Cheyenne SPE, Chewco Investments, LP, JEDI I and II, LJM 1 and LJM2? If so, please identify the individuals making the investments, and the date and amount of each investment, and state J.P. Morgan Chase & Co.'s policy regarding investments by its employees, officers, or directors in entities for which J.P. Morgan Chase & Co. provided investment services or advice. Please provide a copy of this policy to the Committee.

Response to Request 3:

No JPMC employee, officer or director made a direct investment in any Enron SPE's or related partnerships. However, as set forth below, Sixty Wall Street Fund, L.P. ("Sixty Wall") made a capital commitment of $3,000,000 to LJM2 Co-Investment in 1999. Sixty Wall is a highly diversified investment partnership formed by heritage JPM in 1995 to provide certain officers of JPM, pursuant to an annual co-investment program, with the opportunity to co-invest lock-step with the firm's then existing principal private equity investment entity, J.P. Morgan Capital Corporation and its subsidiaries ("Morgan Capital").

The investors in Sixty Wall have no investment discretion and are not aware of particular investments by Sixty Wall at the time that they are made. For all practical purposes, from the investors' point of view, Sixty Wall operates as a mutual fund.

Request 4:

Committee interviews with, and testimony from, Jeffrey McMahon and Sherron Watkins, as well as other information learned by the Committee, indicate that several financial institutions and their employees claimed to have received promises, inferences, or suggestions from Enron and/or LJM employees that the financial institutions would receive future Enron business if they invested in the LJM partnerships. Please state whether any officer or employee of Enron or the LJM partnerships made any guarantee, promise, suggestion, innuendo or other communication that suggests or otherwise indicated that J.P. Morgan Chase & Co. would receive future business from Enron, or that the likelihood of receiving such business would increase, if J.P. Morgan Chase & Co.

or its employees, officers, or directors invested in, or provided financing to, any Enron SPE or related partnership. If so:

a. Identify and provide any records relating to such communications described above:
b. Identify each transaction associated with any business received from Enron as a result of investments made by J.P. Morgan Chase & Co. or its employees, offices, or directors; and
c. Provide all records relating to these transactions.

Request 5:

Committee interview with, and testimony from, Jeffrey McMahon and Sherron Watkins, as well as other information learned by the Committee, indicate that several financial institutions and their employees claimed to have received threats, suggestions, or innuendo that a failure to invest in the LJM partnerships would have a negative impact on the likelihood that they would receive future Enron business. Please state whether any officer or employee of Enron or the LJM partnerships made any threat, suggestion, or innuendo that suggests or otherwise indicates that J.P. Morgan Chase & Co. would not receive future Enron business if it or its employees, officers, or directors did not invest in any Enron SPE or related partnership. If so, please identify and provide any records relating to such communications described above. If so:

a. Identify and provide any records relating to such communications described above:
b. Identify any Enron-related transaction J.P. Morgan Chase & Co. believes it was denied as a result of a failure to invest in the LJM partnerships or other Enron-related partnerships; and
c. Provide all records relating to these lost transactions.

Responses to Requests 4 and 5:

Neither JPM nor Chase invested in any of the entities listed in Request 2 other than LJM2 Co-Investment. As noted above, in December 1999, at the time LJM2 Co-Investment was formed, JPM and Chase were separate entities. Chase, through an affiliate, Chemical Investments, Inc., made a capital commitment of $10,000,000, as a limited partner, in LJM2 Co-Investment. JPM, through an affiliate, together with Sixty Wall, made a capital commitment of $15,000,000. LJM2 Co-Investment ultimately received commitments totalling $394,000,000, which gave Chase a 2.5% interest in the partnership and JPM, together with Sixty Wall, a 3.8% interest.

The reasons that each institution invested in LJM2 Co-Investment were different. JPM's two principal reasons for investing in LJM2 Co-Investment were (1) to gain access to the co-investment opportunities that might be available, including, for example, joint

ventures with LJM2 Co-Investment in non-Enron, third-party energy related assets; and (2) to earn what it believed would be a good rate of return on its investment based on the experience of people with extensive familiarity and knowledge of the energy industry.

On the Chase side, Chase was aware that, since at least 1993, Andrew Fastow ("Fastow") had managed two private equity partnerships on behalf of Enron and CalPERS, JEDI 1 and JEDI 2, as part of Enron's financing and investment strategy. Fastow also had formed and managed a third equity fund, LJM1, for the same purposes. Chase was advised that LJM2 Co-Investment likewise was highly strategic for Enron's financing and investment strategy.

In line with Chase's practice of supporting its clients' strategic needs, and to maintain and further its position as one of Enron's tier one, or lead, banks, Chase made the decision to invest in LJM2 Co-Investment through an affiliate, Chemical Investments, Inc. Further, LJM2 Co-Investment appeared to be a solid investment, with projected rates of return consistent with those realized by Chemical Investments, Inc.'s passive investments in other private equity funds (which, today, number in excess of 325 separate funds).

Chase was advised that Fastow's proprietary interest in LJM2 Co-Investment was a positive factor. Chase understood that the partnership would be properly managed and that LJM2 Co-Investment would not simply be a repository for underperforming assets that Enron had no interest in retaining. While Chase recognized that Fastow had loyalties to both Enron and LJM2 Co-Investment, Chase was assured that the Board of Directors of Enron had thoroughly discussed and considered the conflict issues and that they were comfortable that sufficient safeguards would be put in place to protect Enron's interests. Chase was further informed that Enron's Board of Directors had waived Enron's Code of Conduct in order to allow the partnership to proceed.

No officer or employee of Enron or the LJM partnerships promised that either Chase or JPM would receive further business from Enron if it invested in LJM2 Co-Investment. Nor were there any threats, suggestions or innuendoes that either Chase or JPM would not receive future business if it did not invest in LJM2 Co-Investment. However, Fastow indicated that an investment by Chase in LJM2 Co-Investment would be viewed positively by Enron.

Documents responsive to these Requests are included in our submission in response to Request 10.

Request 6:

Reportedly, J.P. Morgan Chase & Co. earned over $100 million in revenue from its relationship with Mahonia, Ltd. and Mahonia Natural Gas, Ltd. Please describe what interest, economic or otherwise, J.P. Morgan Chase & Co. has in Mahonia Ltd., Mahonia

Natural Gas Ltd., Stoneville Aegean Ltd., Lively Ltd., and/or Justice Ltd., and the dates those interest were obtained.

Response to Request 6:

JPMC has no ownership interest in Mahonia, Mahonia NG, Stoneville, Lively Ltd. or Juris Ltd. (which we believe to be the Company to which you refer as Justice Ltd.) These entities were, however, incorporated for transactions that were to be introduced to them by CMB.

Mahonia itself became involved in these transactions in 1993 as at that time The Chase Manhattan Bank, N.A., a predecessor by merger to JPMC, determined that it could not buy and sell physical commodities, whereas Mahonia would be able to take delivery of oil or gas. The Mahonia structure continued to be used for various customers of JPMC, including Enron, after JPMC was authorized to enter into these transactions for its own account.

CMB received fees from its customers in respect of transactions involving the customers, Mahonia, Mahonia NG and/or Stoneville.

Request 7:

Reportedly, from 1997 to 2000, J.P. Morgan Chase & Co. used Mahonia Ltd. and its related companies provided for or arranged more than $2.2 billion of "back-to-back" transactions where Mahonia-related companies signed forward contracts for delivery of oil and gas from Enron, and contemporaneously, J.P. Morgan would sign identical contracts with Mahonia-related companies. Please provide all records relating to such transactions.

Response to Request 7:

For many years, prepaid transactions have been a common source of financing for many corporations.[1] These financings have been arranged by CMB as well as other financial institutions.

From June 1993 through December 2000, Enron, Mahonia, and CMB entered into several prepaid forward transactions involving the sale and delivery of crude oil and/or natural gas.[2] In the case of Enron, it is our understanding that institutions other than

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1 In addition, these structures may also enable parties to satisfy other financial, tax, regulatory, and accounting objectives, all within the relevant rules and standards.

2 Heritage JPM never had any association with Mahonia, Stoneville, or any other related entity.

CMB have also provided Enron-related entities with significant amounts of financing through prepaid structures.

During the time frame that is the subject of the Committee's inquiry, Enron entered into six prepaid forward transactions with Mahonia or Mahonia NG and, in connection with such transactions, Mahonia/Mahonia NG entered into similar prepaid forward transactions with CMB.[3] Pursuant to these transactions, Enron was obligated to, and, prior to its bankruptcy, did, deliver natural gas and crude oil to Mahonia. Likewise, Mahonia was obligated to, and did, deliver natural gas and crude oil to CMB.

In response to Request 7, JPMC is providing (1) transaction documents for the prepaid forward transactions between Enron and Mahonia/Mahonia NG, and Mahonia/Mahonia NG and CMB; (2) correspondence relating to such transactions; and (3) pipeline records that show deliveries of natural gas or crude oil from Enron to Mahonia/Mahonia NG and/or Mahonia/Mahonia NG to CMB, to the extent that JPMC possesses such documents. JPMC notes that it is engaged in an ongoing process of document identification and retrieval, including the identification and retrieval of archived materials and electronic data, and will supplement its production to the extent requested.

CMB has also entered into transactions with Enron and other third parties for the sale and delivery of the natural gas and crude oil that it received pursuant to the Enron and non-Enron prepaid forward transactions. To the extent that the Committee wishes to review the transaction documents or correspondence relating to such transactions, CMB will provide access to such documents as soon as they are available, subject to resolving any confidentiality concerns that the non-Enron entities may have.

Request 8:

Please describe any ownership or economic interest that persons, charitable trusts, or entities/shareholders other than J.P. Morgan Chase & Co. may have in Mahonia Ltd., Mahonia Natural Gas Ltd., Stoneville Aegean Ltd., Justice Ltd., and/or Lively Ltd. Please provide names of these persons, charitable trusts, or other entities/shareholders of Mahonia Ltd., Mahonia Natural Gas Ltd., Stoneville Aegean Ltd., Justice Ltd., and/or Lively Ltd.

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[3] These transactions occurred on or about (1) December 18, 1997, (2) June 26, 1998, (3) December 1, 1998, (4) June 29, 1999, (5) June 28, 2000, and (6) December 28, 2000. Additional transactions occurred both before 1997 and in 2001.

Response to Request 8:

Our response is based on information that the named entities provided. A diagram setting out the ownership structure of Mahonia is annexed hereto as Exhibit A.

Mahonia is an SPE which was incorporated in December 1992. The beneficial owner of Mahonia is the trustee of the Eastmoss Trust, Mourant & Co. Trustees Limited (hereinafter the "Eastmoss Trustee").

The Eastmoss Trust was established in 1986 under Jersey law for charitable purposes. Under this mandate, the Eastmoss Trustee has made distributions to charities in Jersey, the United Kingdom, Ireland and North America of approximately £74,000, which represents dividends paid to it by SPEs, such as Mahonia, beneficially owned by the Eastmoss Trustee.

JPMC has no ownership interest in the Eastmoss Trustee or in the Eastmoss Trust. Nor is JPMC a beneficiary of the Eastmoss Trust.

JPMC does not have any ownership interest in Juris Limited, Lively Limited, Mourant & Co. Trustees Limited, Mourant & Co. Secretaries Limited and Mourant & Co. Limited (together the "Mourant Companies"). The Mourant Companies are all controlled by the partners of Mourant Group, a Jersey partnership providing specialist professional services. Many of the partners of Mourant Group are partners in Mourant du Feu & Jeune, a leading Jersey law firm.

Mahonia NG was incorporated in December 2000 and is a wholly owned subsidiary of Mahonia.

Stoneville was incorporated in 1989 with the Eastmoss Trustee as beneficial owner. In May 1994, the beneficial interest in Stoneville was transferred to Mourant & Co. Trustees Limited in its capacity as trustee of the Axmouth Trust. The Axmouth Trust is a Jersey trust established under Jersey law for charitable purposes.

Request 9:

Reportedly, Mahonia Ltd. and Mahonia Natural Gas Ltd. are owned or controlled by two entities, Mourant & Co. and Mourant & Co. Secretaries. Please describe J.P. Morgan Chase & Co.'s relationship with Mourant & Co. and Mourant & Co. Secretaries.

Response to Request 9:

As described above, the Eastmoss Trustee is the beneficial owner of Mahonia and Mahonia NG. Mourant & Co. Limited and Mourant & Co. Secretaries Limited do not have any beneficial interest in the shares of Mahonia and Mahonia NG.

Mourant & Co. Limited and Mourant & Co. Secretaries Limited are part of the Mourant Group. Mourant du Feu & Jeune supplies legal services and Mourant Co. Limited supplies administrative and corporate services to many global companies, including JPMC.

Request 10:

Please provide all records relating to communications from 1997 to the present between Vice Chairman Mark Shapiro, Vice Chairman James Lee, Jr., Associate General Counsel Phillip Levy, David Pflug, or any other J.P. Morgan Chase & Co. employee, officer, or director, and Ken Lay, Jeff Skilling, Jeffrey McMahon, Andrew Fastow, Richard Causey, Richard Buy, or Joseph Deffner, relating to any Enron SPEs, trusts, or related partnerships.

Response to Request 10:

Documents responsive to Request 10 are produced herewith. JPMC notes that it is engaged in an ongoing process of document identification and retrieval, including the identification and retrieval of archived materials and electronic data, and will supplement its production to the extent requested.

Request 11:

Please provide copies of all communications from 1997 to the present between Vice Chairman Mark Shapiro, Vice Chairman James Lee, Jr., Dinsa Mehta, Associate General Counsel Phillip Levy, David Pflug, or any other J.P. Morgan Chase & Co. employee, officer, or director, and Ken Lay, Jeff Skilling, Cliff Baxter, Jeffrey McMahon, Andrew Fastow, Richard Causey, Richard Buy, or Joseph Deffner, relating to any investment, loan, or derivative contract that J.P. Morgan Chase & Co. and/or Mahonia Ltd., Mahonia natural Gas Ltd., or Stoneville Aegean Ltd. made with or to Enron or its related SPEs, trusts, or partnerships.

Response to Request 11:

Documents responsive to Request 11 are produced herewith. JPMC notes that it is engaged in an ongoing process of document identification and retrieval, including the identification and retrieval of archived materials and electronic data, and will supplement its production to the extent requested.

Request 12:

Please provide all records relating to communications from 1997 to present between Vice Chairman Mark Shapiro, Vice Chairman James Lee, Jr., Dinsa Mehta, Associate General

Counsel Phillip Levy, David Pflug, or any other J.P. Morgan Chase & Co. employee, officer, or director, and Ian James, reportedly a director of Mahonia Ltd.

Response to Request 12:

In response to Request 12, JPMC is providing records relating to communications from 1997 to the present between its officers and employees and Ian James, a director of Mahonia, that concern Enron. Over the past five years, however, JPMC also entered into several prepaid forward transactions involving Mahonia that provided financing to ***non***-Enron entities. To the extent that the Committee wishes to review the transaction documents or correspondence relating to such non-Enron transactions, JPMC will provide access to such documents, subject to resolving any confidentiality concerns that the non-Enron entities may have. JPMC notes that it is engaged in an ongoing process of document identification and retrieval, including the identification and retrieval of archived materials and electronic data, and will supplement its production to the extent requested.

Request 13:

Please identify all senior J.P. Morgan Chase & Co. employees or officers who worked on or were responsible for its Enron-related transactions, and make them available for interviews with committee staff.

Response to Request 13:

Senior JPMC officers most familiar with the Enron-related transactions include the following:

Name	Position
James M. Biello	Managing Director, Senior Credit Officer for Enron
Jeffrey W. Dellapina	Managing Director, Energy Derivatives
Samuel T. Maclin	President, Southwest Region of JPMC
Robert W. Traband	Vice President, Corporate Banker for Enron
Richard S. Walker	Managing Director, Client Executive for Enron

Our responses are to the best of our knowledge and the information available to us as of the date of this letter. If we should subsequently learn that any of the information set forth herein is inaccurate, we will notify the Committee.

Respectfully submitted,

Abuva Genack

AG/dch

Encl.

Exhibit A

April 9, 2002

VIA FACSIMILE TRANSMISSION
AND FEDERAL EXPRESS

Kevin M. Loftus, Esq.
Senior Counsel
U.S. Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549-0703

Re: *In the Matter of Enron Corporation,*
File No. HO-09350

Dear Mr. Loftus:

I am writing in response to your letter to Mr. Kent Stauffer, dated March 1, 2002, and the accompanying subpoena (the "Subpoena") issued to J.P. Morgan Chase & Co. (as defined in the Subpoena, hereinafter, "JPMC") by the United States Securities and Exchange Commission ("the Commission"), Division of Enforcement, in connection with the formal investigation of Enron Corporation ("Enron").

In accordance with our agreement, on April 8, 2002, JPMC produced to the Commission numerous documents responsive to the Subpoena. JPMC also provided to the Commission on April 2, 2002 courtesy copies of documents it produced to the House Committee on Energy and Commerce (the "House"), many of which are also responsive to the Subpoena issued by the Commission.

We are still in the process of identifying and retrieving documents, including archived electronic data and documents. Accordingly, this response and the documents produced thus far, represent our best efforts based on the information and materials presently available. We will make additional documents available on a rolling basis.

Request 1:

Documents sufficient to identify all relationships, dealings, or transactions between J.P. Morgan and Enron including, but not limited to, all partnerships, joint ventures, special purpose entities, investments, forward contracts, prepay transactions, hedging transactions, derivatives, swaps, loans or lines of credit, consulting services, insurance services, securities account services, or banking services.

Response to Request 1:

Documents responsive to Request 1 bearing bates numbers JPM-1-00001 through JPM-1-00597 were produced to the Commission on April 8, 2002. Further, a schedule listing securities underwriting, advisory services and credit facilities provided by The Chase Manhattan Bank and

affiliates ("Chase") from January 1, 1997 through December 31, 2001, and by the combined entity formed by the merger of J.P. Morgan & Co. and Chase ("JPMC"), from that date until the present, and the fees earned on those transactions (the "Schedule"), a copy of which was provided to you in connection with the House submission, is enclosed herewith.

In addition to the relationships, dealings or transactions described in the Schedule, we identify the following relationships and dealings with Enron:

JPMC provided corporate trust services for Enron for which it earned a total of approximately $1.2 million for the entire period 1997 through 2001. By way of example, JPMC served as indenture trustee for three issues of Enron senior debt securities and two issues of senior notes for Enron affiliates; fiscal agent for an Enron affiliate; escrow agent for Enron related escrow accounts; and issuing and paying agent for certain issues of Euro and Japanese debt and U.S. commercial paper.

JPMC periodically entered into routine risk management transactions with Enron. These transactions consisted of cash-settled swaps and options relating to commodity price risk, interest rate risk and currency price risk in nine currencies. These transactions were governed by the terms of an ISDA Master Agreement between Enron North America Corporation and JPMC.

JPMC's Private Bank provides high net worth clients customized and integrated delivery of financial products, including investment management, estate and trust services and credit and banking. These clients included, among others, senior executives and directors of Enron.

JPMC provided corporate banking services for Enron related partnerships such as LJM2 and Southampton.

Prior to Enron's bankruptcy, JPMC performed cash management services for Enron.

JPMC is investing debtor-in-possession funds for Enron Corp.

Request 2:

Documents sufficient to identify and quantify, by fiscal quarter, the number and dollar value of any transactions between (a) J.P. Morgan and Enron; (b) Mahonia and Enron; (c) J.P. Morgan and Mahonia; (d) J.P. Morgan and LJM1; (e) J.P. Morgan and LJM2; and (f) J.P. Morgan and JEDI.

Response to Request 2:

See Response to Request 1.

Request 3:

All documents concerning communications by, to, with or among J.P. Morgan's Board of Directors or any committee thereof concerning Enron, Mahonia, LJM1, LJM2 and JEDI, including, but not limited to, all documents concerning authorizations by the Board or any committee thereof to engage in any transaction or agreements with such entity.

Response to Request 3:

Documents reflecting communications by, to, with or among J.P. Morgan's Board of Directors or any committee thereof concerning the named entities through December 31, 2001 bearing bates numbers JPM-3-00001 through JPM-3-00041 were provided to the Commission on April 8, 2002.

Request 4:

All documents concerning the formation and ownership of Mahonia, LJM1, LJM2 and JEDI including, but not limited to, all sales or marketing materials, private placement memoranda, internal communications or analyses, incorporation documents, shareholder or transfer agent records, organization charts, wire transfers, bank statements and journal entries that relate to their capitalization.

Response to Request 4:

Documents responsive to Request 4 bearing bates numbers JPM-4-00001 through JPM-4-00584 were provided to the Commission on April 8, 2002.

Request 5:

All documents concerning board of director, partnership, or other executive management meetings for Mahonia, LJM1, LJM2 and JEDI since their inception, including, but not limited to, all minutes or other summaries, transcripts, or notes, and any agendas, schedules, hand-outs, presentations, or other supporting documents provided to directors, partners, or management concerning such meetings.

Response to Request 5:

Documents responsive to Request 5 bearing bates numbers JPM-5-00001 through JPM-5-00096 were provided to the Commission on April 8, 2002.

Request 6:

All documents concerning any agreements between or among Mahonia, J.P. Morgan and Enron, including, but not limited to, contracts, wire transfers, communications, and the settlement of any contracts in commodities.

Response to Request 6:

Documents responsive to Request 6 bearing bates numbers JPM-6-00001 through JPM-6-03662 were provided to the Commission on April 8, 2002. Numerous documents responsive to Request 1 which were provided to the Commission are also responsive to Request 6. Additional documents responsive to Request 6 were delivered to the Commission on April 2, 2002 in connection with JPMC's submission to the House.

Request 7:

Documents sufficient to show the accounting treatment of J.P. Morgan's transactions, dealings or relationships with Enron, Mahonia, LJM1, LJM2, and JEDI in J.P. Morgan's financial statements.

Response to Request 7:

We will respond to this Request as soon as responsive materials are available.

Request 8:

All documents concerning audited or unaudited financial statements of Mahonia.

Response to Request 8:

We will attempt to obtain responsive documents, if any.

Request 9:

All documents concerning tax returns or other statutorily-required returns concerning Mahonia, LJM1, LJM2 and JEDI whether filed in the United States or any foreign jurisdiction.

Response to Request 9:

We will attempt to obtain responsive documents.

Request 10:

All general ledgers of Mahonia.

Response to Request 10:

We will attempt to obtain responsive documents.

Request 11:

All documents concerning any direct investment by J.P. Morgan or any J.P. Morgan employees in Mahonia, LJM1, LJM2, and JEDI.

Response to Request 11:

See JPMC's submission to the House provided to the Commission on April 2, 2002.

Request 12:

All documents concerning J.P. Morgan's research analyst recommendations and ratings concerning the purchase or sale of Enron stock, including, but not limited to, documents identifying the analysts responsible for such recommendations, financial analyses, and internal communications concerning the recommendations and ratings.

Response to Request 12:

Documents responsive to Request 12 were provided to the Commission by letter to Camille Thornton, Esq. dated March 7, 2002. We are in the process of identifying and retrieving additional documents responsive to this Request and will produce them to the Commission as soon as they are available.

Request 13:

Documents sufficient to identify all of J.P. Morgan's positions in and trading of any Enron common stock, option, warrant, or other publicly traded security, including, but not limited to, the account(s) utilized for such trades or holding such positions, the date(s) of any such trades, and the individuals responsible for making such trades.

Response to Request 13:

We are in the process of identifying and retrieving documents responsive to this Request and will produce them to the Commission as soon as they are available.

Request 14:

All communications concerning any actual or contemplated syndication of Enron debt.

Response to Request 14:

Documents concerning actual syndication of Enron debt bearing bates numbers JPM-14-00001 through JPM-14-2439 were produced on April 8, 2002. Numerous documents responsive to Request 1 are also responsive to Request 14. We are in the process of identifying and retrieving additional documents responsive to this Request and will produce them to the Commission as soon as they are available.

Request 15:

All documents concerning the sale of Enron credit derivatives or other Enron-related financial instruments to the Employee Retirement System of Texas or other retirement funds managed by J.P. Morgan.

Response to Request 15:

Based on JPMC's review to date, it appears that there are no documents responsive to Request 15.

Request 16:

All communications with PWC or any other independent accountants concerning Enron, Mahonia, LJM1, LJM2, and JEDI.

Response to Request 16:

We are in the process of identifying and retrieving documents responsive to this Request, if any, and will produce them to the Commission as soon as they are available.

Request 17:

All documents obtained, reviewed or created by J.P. Morgan's executive management to monitor, manage or control J.P. Morgan's credit risk, value at risk, interest rate risk, market risk, currency risk, country risk, or any other risk concerning its relationship and transactions with Enron, Mahonia, LJM1, LJM2, and JEDI, including, but not limited to, exception reports or summaries.

Response to Request 17:

Documents responsive to Request 1 provided to the Commission on April 8, 2002 are also responsive to Request 17. We are in the process of identifying and retrieving additional documents responsive to this Request and will produce them to the Commission as soon as they are available.

Request 18:

All documents concerning press releases or other public statements made by J. P. Morgan concerning Enron, Mahonia, LJM1, LJM2 and JEDI, including, but not limited to, internal communications concerning such press releases and public statements.

Response to Request 18:

We are in the process of identifying and retrieving documents responsive to this Request and will produce them to the Commission as soon as they are available.

Request 19:

All documents concerning "Chinese wall" or other policies that segregated availability of information concerning Enron, Mahonia, LJM1, LJM2 and JEDI within J.P. Morgan.

Response to Request 19:

Documents responsive to Request 19 bearing bates numbers JPM-19-00001 through JPM-19-00547 were produced to the Commission on April 8, 2002.

We ask that you treat as confidential all documents produced herein and designated with the legend "FOIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC", and any notes, extracts, summaries, or memoranda that the Commission creates regarding, incorporating, or based on the enclosed information, or referring to any conference, meeting, or telephone conversation with JPMC's current or former employees, agents, auditors, or counsel relating to your inquiry.

Please advise me if you intend to provide copies of this information or documents produced by JPMC to any other agency.

This production is not intended to be, and shall not be construed as, a waiver of any applicable privilege or legal basis under which information may not be subject to production.

If you have any questions, please do not hesitate to contact me at (212) 552-0918.

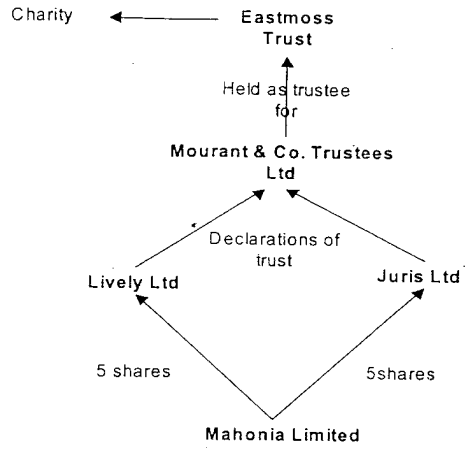
Very truly yours,

Ahuva Genack

AG/dch
Encl.

cc: Freedom of Information Officer

The Ownership of Mahonia Limited



CITICORP

GLOBAL LOANS APPROVAL MEMORANDUM

Memo Date: December 21, 1998 — Approval Due Date: December 24, 1998

[ ] Renewal, Repricing or Restructuring	[X] League Table Eligible		Yes	No
[ ] Amendment (Number ____)	[X] Agent-only	Media Disclosure	[ ]	[X]
	[ ] Co-Agent	Contact:		

A. KEY STATISTICS

Borrower:	A Special Purpose Entity	Citibank Commitment ($MM):	$500.0MM
Sponsor:	Enron Corp.	Citibank Hold ($MM):	$125.0MM
GFCID#:	0000446084	U/W Amount ($MM):	$375.0MM
Deal Size ($MM):	$500.0MM	B/E Amount ($MM):	Not Applicable
Facilities ($MM)/Tenor:	$500.0MM /3-Years	Accom. Amount ($MM):	Not Applicable
Pre-approved (Y/N):	No	Scheduled Launch Date:	March 17, 1999
Date Pre-Approved:	Not Applicable	Scheduled Closing Date:	April 22,1999
Origination Unit:	GEM-Houston	Sell Down Date(s):	June 15, 1999
GRB Industry:	Integrated Oil and Gas	Secured (Y/N):	Yes
GRB Market:	US South	Obligor Exception (Y/N):	Yes
Account Segment:	Priority	(Exception Amt.):	[$---]MM
Syndicated Y/N:	Yes	Liquidity Exception (Y/N):	No
Agent(s)/Amount($MM):	Citibank	Pricing Exception (Y/N):	No Market / No Hurdle
Co-Agent(s)/Amount($MM):	To Be Determined		

Team Leader:	Tel:	Back-up:	Tel:
David Gorte	713-654-2862	Jim Reilly	713-654-2828

Approvals:

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CONFIDENTIAL

CITI-SPSI 0025979

Permanent Subcommittee on Investigations
EXHIBIT #144

CITICORP

Syndication Strategy

1. Overview

As noted previously, the debt associated with this three-year prepaid forward gas sale transaction is $500.0 million. This debt will be funded through CXC, a Citigroup-sponsored securitization vehicle, backstopped by $500.0 million of bank commitments pursuant to an Asset Purchase Agreement ("APA"). Salomon Smith Barney is seeking approval to underwrite $375.0 million of these APA commitments, with Citibank's GEM Group holding $125.0 million. It should be noted that we are seeking a five and one-half month syndication period here, rather than the typical 90 days, due to a requirement by Enron that we delay the syndication of this transaction to mid-March 1999. Salomon Smith Barney will be paid $1.0 million net for syndicating this transaction; this equates to 25 bps on the underwriting position and 75 bps on Citibank's hold position. (In the event that this transaction is prepaid prior to the end of the syndication period, Salomon Smith Barney will be paid a $625,000 fee for structuring this transaction). Enron will pay all up-front fees to the syndicate banks. Because of market conditions and the delayed commencement of syndication, Enron has agreed to full market flex language in order to reduce Salomon Smith Barney's $375 million (or less as reduced through amortization) underwriting position to zero by June 15, 1999. Salomon Smith Barney will manage the syndication process with Enron and will have a limited, soft clear market period with respect to an agreed-upon list of banks in which to syndicate this transaction. Enron has pledged to use its significant relationship leverage to effect the selldown.

Our syndication strategy is to syndicate this transaction in a single step to five to eight relationship banks. The unusual aspect of this syndication is that we are being requested to delay the launch of this syndication until several other Enron bank-funded transactions have been syndicated during the first two and one-half months of 1999. As a result, the general syndication of this transaction will not commence until March 1999. As noted above, Salomon Smith Barney will benefit from full market flex language permitting us to modify the coupon, up-front fee, and structure as necessary to syndicate this transaction. At that time, we plan to approach eight to twelve banks in order to have five to eight banks commit $50 million - $75 million to this transaction. The large commitment size requested is a function of two factors: (1) the vast majority of the credit risk associated with this transaction is that of a group of five A-rated or better insurance companies through the surety bond they issue supporting Enron's delivery obligations and of the commodity swap counterparty(ies), expected to be Barclay's and/or National Westminster and (2) this is an amortizing three-year transaction, where principal exposure will reduce via mortgage-style amortization. We plan to offer 30 bps upfront on a $50 million commitment and 45 bps upfront on a $75 million commitment.

Because the funding structure is a securitization, the bank facility will take the form of a 364-day unfunded backstop commitment (zero risk – based capital) through an Asset Purchase Agreement ("APA") with a two-year term out that will support commercial paper issued by CXC. At Enron's and the insurance company's current ratings, the proposed grid-based pricing on the liquidity backstop is 22.5 bps and, if drawn, the LIBOR margin will be 125 bps. As noted above, with the market flex language, the undrawn and drawn pricing, as well as the up-front fees, are subject to change as necessary to bring Citibank to its approved $125 million hold position.

While this is an Enron credit, from a syndication perspective our objective will be to focus potential investors on the "look-through" from Enron to the credit of: (1) the insurance companies providing the surety bonds and (2) the swap counterparty(ies). The Enron delivery risk is fully supported by the surety bonds provided by the five insurance companies. While Enron risk exists with respect to the marketing agreement to ensure that the natural gas is sold at the index price and that the proceeds of these sales are delivered to the Special Purpose Entity ("SPE"), assuming this occurs, the payments from the commodity swap counterparty(ies), will provide 100% of the cash flow required to make the principal payments on this amortizing credit. The SPE will then make the fixed interest payments to the interest rate swap counterparty (an Enron-guaranteed subsidiary) in order that the floating interest rate payments can be made to CXC or, if the funding is put to the APA banks, to the APA banks.

In an effort to minimize the due diligence process, each potential investor will be provided with detailed due diligence information on (i) the insurance companies providing the surety bond and (ii) the commodity swap counterparty(ies), as well as on the securitized prepaid forward transaction itself. Prepaid forward transactions have been done by various energy companies (including a large number by Enron) over the past seven or eight years and all Enron banks are very familiar with the structure of prepaid forward transactions. The two innovative aspects of this transaction are the surety bond support from the five insurance companies and the securitized funding. Each of these innovative aspects is expected to be viewed as a significant plus by the banks by reducing the Enron credit exposure content of this transaction and by making each bank's commitment a zero risk – based capital exposure.

2. Comparables – Structure and Pricing

The underlying credit structure – advancing against Enron's obligations to deliver crude oil and natural gas to specified delivery points where they will be sold for index prices to be swapped to predetermined fixed prices – is a familiar structure in the energy bank market. The only differences between this structure and traditional prepaid forward crude oil and natural gas financings are: (1) the introduction of the insurance companies' surety bonds to support Enron's delivery obligation and (2) the securitization aspect. As a result, perhaps the best comparables for this transaction are the A-Note portions of securitized Asset Defeasance Product (synthetic lease) financings, since these are securitized corporate debt obligations, and this prepaid forward is effectively a commodity denominated corporate obligation, albeit one supported by five highly rated insurance companies' surety bond. This additional, highly rated credit support and the relatively short average life—the average life of this transaction is less than two years, compared to the five to seven and one-half year non-amortizing tenors of the securitized ADPs. Attached is an exhibit that outlines the pricing of the A-Notes on several recent "BBB"-sponsored securitized ADPs. It is important to note that the proposed pricing exceeds that of these comparable transactions, even without giving benefit to the surety bond support for Enron's delivery obligations.

In part, the rationale for pricing this transaction above the comparables is the significant volume of Enron bank exposure in the market. The surety support reduces this concern by minimizing the amount of Enron credit risk embedded in this transaction. Even so, the proposed pricing appears attractive relative to the 85 bps drawn, 25 average up-front fee pricing of the somewhat comparable, but non-credit-supported Enron Pilgrim transaction described below.

Given that Enron has agreed to full market flex, the proposed pricing is the starting point for conversations with the prospective lender candidates. Feedback from that group will provide a good read on where the appropriate pricing levels should be and whether any adjustment in our proposed pricing is necessary.

3. Enron Forward Calendar

Because of our concern regarding the volume of transactions that Enron had planned to have in the market simultaneously with the Rawhide transaction, the company has agreed to delay the general syndication of two transactions and to cancel altogether the general syndication of a third transaction. Consequently, about $1 billion of Enron paper which would have been in the market at the same time as the Enron's Citibank/SSB Rawhide transaction will now be syndicated in February 1999. This transaction is therefore slotted to be syndicated after Enron's Rawhide, Electro, Firefly, Pilgrim, and Dabhol 2 transactions. Enron transactions other than Roosevelt that are scheduled to close by year end are as follows:

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CITICORP

Deal	Amount/Term	Remarks/Pricing
Rawhide	$727.5MM/2 years	Monetization of Enron's merchant asset portfolio. 364-day facility. 100 bps commitment fee/drawn margin of 262.5 bps in year 1 and 287,.5 bps in year 2/upfront fees of 100 bps on average.
JEDI 1	$325MM/5 years	Refinancing of JEDI 1. Co-underwriters are BZW and CSFB. General syndication will close by 12/31. Pricing: 25bps undrawn 112.5-200 bps drawn (determined by asset coverage)/ 37.5 bps upfront
Elektro	$500MM/3 years	Acquisition financing for Enron's purchase of Brazilian electric utility. Enron is self syndicating and 9 Arrangers have committed $100MM each. General syndication will not be necessary since each arranger is already near its $50MM hold. 100 bps upfront with average drawn pricing of 270 bps.
Firefly	$400MM/2 years	Synthetic equity for Elektro. Arranged by DLJ, Chase and BT. Also in the deal are Bayerische Landesbank, Commerzbank, National Australia, TD and DG. Close scheduled for 12/15 to be followed by general syndication in February.
Pilgrim	$300MM/3 years	Contract monetizaton arranged by CIBC, First Union, ABN and National Australia Bank. General syndication in February. Funded transaction with drawn rate of 85 bps and average upfront of 25 bps.
Dabhol 2	$380MM/12 years	Second phase of project financing in India arranged by ABN and CSFB. 12-year final, no completion guarantee. 100 bps undrawn/375 bps drawn/262.5 upfront. No Enron recourse.
Cogen	$900MM/17 years	Bridge to capital markets takeout for purchase by Enron of three power plants in New Jersey. Arranged by 8 of A. CSFB, TD and UBS. Deal will not be syndicated.
Watershed	L170MM/Tenor Unknown.	Acquisition financing for ICI unit. Non-recourse financing led by NatWest. If syndicated, expected to occur at end of first quarter.

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Firefly and Pilgrim had been scheduled for general syndication in January but will now be delayed until February. In addition, Elektro was assumed to require about $250 million of commitments in the general syndication in order to reduce Arranger final hold levels to $50 million. In light of the success of the Elektro syndication, each of the Arrangers has already been allocated down to $62.5 million. Consequently, the general syndication will be required only to raise approximately $100 million.

To help with bank capacity issues, Enron is canceling approximately $2.6 billion in existing syndicated facilities by year-end. Those facilities are as follows:

- Elektro acquisition bridge facility — $1.1 billion
- Wessex acquisition facility — $1.0 billion
- JEDI 1 revolver — $265 million
- JEDI 1 term loan — $240 million

Because the sheer volume of Enron transactions and attendant capacity issues create syndication concerns, we want to be certain the Roosevelt transaction has a competitive advantage when stacked up against the other deals. Consequently, Roosevelt, through the insurance company surety bonds and the commodity swap counterparty(ies) has the highest credit quality, the shortest average life, and, along with our Rawhide transaction, is the most capital friendly of all of Enron's year end deals. Importantly, while 90%+ (barring an astronomical increase in the SPE's floating rating borrowing cost) of the credit risk associated with this transaction is of A-rated or better insurance companies and banks, the transaction is priced using a grid using the lowest of the ratings of Enron, each of the insurance companies, and each of the commodity swap counterparties. As a result, at the outset, the banks will be receiving attractive "BBB" pricing for what is largely an "A" credit risk.

4. Syndication Story

The story to the banks is that the credit exposures of the Roosevelt transaction are: (1) Enron natural gas and crude oil delivery obligations 100% backstopped by five "A"-rated insurance companies through a surety bond, (2) commodity swaps with Barclay's and/or NatWest, both AA/Aa2-rated issuers, and (3) if floating interest rates for the SPE increase over the fixed interest cost, Enron risk for the interest rate swap. As such, little of the exposure here should be allocated to Enron, an important issue given the large volume of Enron transactions in the syndicated bank market.

The bulk of this transaction's credit exposure is that of the five "A"-rated insurance companies and the one or two "AA"-rated commodity swap counterparties. Nevertheless, the transaction is priced from a grid providing the banks with the pricing applicable to the weakest of the ratings of Enron, the commodity swap providers, and each of the five insurance companies. As such, we believe this transaction should be very attractive to the banks, assuming that the Enron relationship managers can persuade their financial institution and insurance groups to accept their shares of this exposure.

We believe this is a compelling story and is saleable in the bank market.

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5. **Potential Investors**

Because of the securitization structure, the investor universe is limited to A_1P_1 institutions. Based on conversations with Enron as well as Securitization, we have developed a preliminary investor universe as follows:

Bank of Montreal	CCB	Deutsche
Bank of New York	ING/BBL	Dresdner
Banque Paribas	PNC	UBS
BNP	Rabobank	JP Morgan
Credit Agricole-Indosuez	Royal Bank of Scotland	Bankers Trust
Hong Kong Shanghai	Bank of Nova Scotia	Societe Generale
Den Danske	Wachovia	

The criteria used to select the potential lenders included familiarity with our securitization structures and available Enron capacity. While these banks overlap the prospective Rawhide managing agents, this transaction will appeal to those institutions that have more limited Enron exposure availability or less willingness to take non-OECD project risk than in the Rawhide transaction in exchange for lower pricing. Assuming that the lenders are prepared to hold the full amount of their commitments, given the small Enron-content of this amortizing three-year exposure, we need five banks at the $75 million senior managing agent level or eight banks at the $50 million co-agent level to eliminate our underwriting position (assuming no amortization).

Because of the limited A_1P_1 investor universe, we have worked out a backup plan with West LB that could be implemented if it becomes apparent that we can't fully syndicate the deal to only A_1P_1 investors. This would involve the "wrapping" by West LB of certain A_2P_2 investor commitments that could support CXC commercial paper issuance. West LB has approved a $150 million basket for A_2P_2 investors which includes 4 Japanese banks – Fuji, Sumitomo, Sanwa and Bank of Tokyo-Mitsubishi ($25MM each). Other A_2P_2 investors will be identified. AMBAC has approved the additional West LB concentration risk.

Finally, through the market flex language, we still the option to go to A_2P_2 investors on a funded basis for a portion of the commitments for this transaction. We believe that the drawn LIBOR margin of 125 bps would be appealing to certain investors.

6. **Syndication Calendar**

December 29	Close and fund transaction
March 1 - 8	Conduct market read with potential Managing Agents/Co-Agents
March 17	Distribute offering memorandum
March 18	Managing Agent/ Co-Agent bank meeting
April 8	Managing Agent/Co-Agent commitments due
April 19	Comments due on documentation
April 22	Closing

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7. Key Success Factors

KEY SUCCESS FACTORS GRID

KEY SUCCESS FACTORS	POOR	AVERAGE	VERY GOOD	EXCELLENT
Company/Borrower			X	
Sponsor			X	
Story			X	
Industry		X		
Deal Size		X		
Market Conditions		X		
Credit Statistics			X	
Pricing			X	
Tenor			X	

COMPANY/BORROWER

The Borrower is rated "very good" because it is a special purpose entity with contractual cash flows to cover 100% of debt service from three sources: a crude oil and natural gas delivery obligation from a BBB+/Baa2 guaranteed entity supported by a surety bond from five A-rated insurance companies, a commodity swap agreement from one or two AA/Aa2 counterparties, and an interest rate swap agreement from a BBB+/Baa2 guaranteed entity. Importantly, the interest rate swap contributes less than 5% of the Borrower's cash flow unless the Borrower's floating CXC or LIBOR borrowing costs exceed 10% per annum.

SPONSOR

Enron is a financially strong, well-known corporation that has multiple strong bank relationships and a large number of transactions financed in the bank market. These factors, and the addition of the surety bond to ameliorate capacity issues, support the "very good" sponsor rating.

STORY

The prepaid forward structure will allow Enron to raise funds without classifying the proceeds from this transaction as debt (it is accounted for as "deferred revenue"). This is a common method of raising non-debt financing among energy companies.

INDUSTRY

Enron's operations in pipelines have produced strong and steady cash flows, while its trading and capital-raising activities and oil and gas exploration and production segment have provided it with realized and potential growth. Because of its extensive hedging operations, as well as the nature of certain of its businesses, Enron does not have the commodity price exposure of many other firms in the energy industry.

DEAL SIZE

This is a relatively large structured transaction with good credit parameters and good absolute dollar revenue and earnings associated with it for the syndicate banks. As such, it will be syndicated to a relatively small group of relationship banks familiar with this structure or similar structures.

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MARKET CONDITIONS

Average, with increased resistance to thinly priced transactions has emerged. Overall market conditions are average, but we believe this transaction will be considered "very good," due to the 22.5 basis point undrawn cost, 125 basis point drawn cost, and the 30.0-45.0 basis point up front fees.

CREDIT STATISTICS

Since this credit relies principally on Enron's A-rated surety-supported delivery obligations and payments from one or two AA/Aa2-rated banks for 90%-100% of the cash flow required for debt service unless LIBOR rates triple during the next three years, and on BB8+/Baa2-rated Enron for the balance, our designation of "very good" is considered to be conservative.

PRICING/TENOR

Pricing is considered "very good." Both up-front fees, undrawn fees, and drawn margins are better than for the recent Citibank-led Coastal and Williams SADPs. These transactions had up front fees of 10 to 30 bps, undrawn fees of 20 bps for BBB/Baa3 Williams and 22.5 bps for BB8-/Baa3 Coastal and drawn spreads of 55.0 bps for the Williams and 57.5 bps for the Coastal A-Note portions of these transactions. By comparison, for this transaction we are offering higher up-front fees of 30-45 bps (albeit for larger commitments), the same 22.5 bps undrawn cost as Coastal despite one to two notch better ratings ignoring the benefits of the surety support for Enron, and more than double the drawn LIBOR margin than either the Williams or Coastal transaction.

The tenor is also very favorable here, with a three-year maturity and a less than two-year average life. By comparison, the Williams and Coastal SADPs had non-amortizing tenors of 5 and 7 ½ years, respectively.

8. Conclusion

Enron has represented to us that it will provide whatever is necessary for this transaction to be successful. The company has supported that representation with concrete actions that materially improve the syndication outlook for Roosevelt. Those actions include the following:

(i) Agreed to structure the transaction so that the bulk of the exposure is to "A"-rated and better insurance companies and commodity swap counterparties and not to Enron, materially reducing the Enron capacity issue associated with the syndication.

(ii) Agreed to full market flex language

Given these actions plus the company's commitment to do whatever it takes to get the transaction syndicated, approval is recommended.

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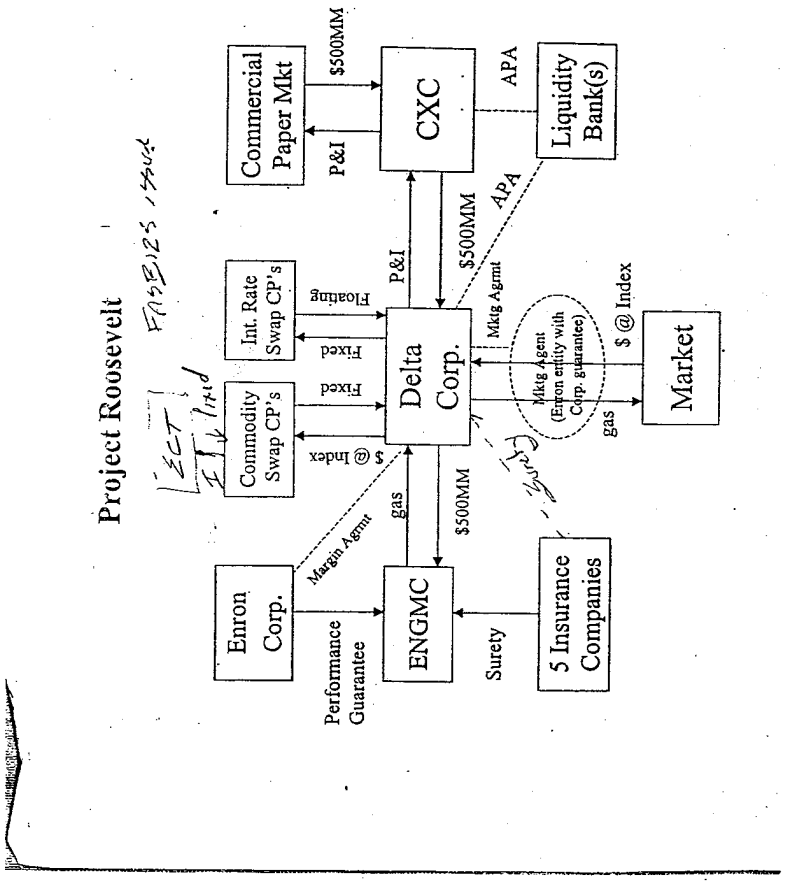
EXHIBIT "A"
Page 1 of 2

ADVANCE PAYMENT SUPPLY SURETY BOND
REDUCTION SCHEDULE

Monthly Period	Monthly Maximum Penal Sum
December 30, 1998 - February 28, 1999	$ 300,000,000
March 1, 1999 - March 31, 1999	$ 504,037,500
April 1, 1999 - April 30, 1999	$ 506,036,849
May 1, 1999 - May 31, 1999	$ 508,259,194
June 1, 1999 - June 30, 1999	$ 498,158,736
July 1, 1999 - July 31, 1999	$ 487,677,238
August 1, 1999 - August 31, 1999	$ 477,489,307
September 1, 1999 - September 30, 1999	$ 466,917,036
October 1, 1999 - October 31, 1999	$ 456,298,335
November 1, 1999 - November 30, 1999	$ 445,977,043
December 1, 1999 - December 31, 1999	$ 435,266,381
January 1, 2000 - January 31, 2000	$ 424,855,704
February 1, 2000 - February 29, 2000	$ 414,052,284
March 1, 2000 - March 31, 2000	$ 403,201,418
April 1, 2000 - April 30, 2000	$ 393,006,030
May 1, 2000 - May 31, 2000	$ 382,062,737
June 1, 2000 - June 30, 2000	$ 371,425,944
July 1, 2000 - July 31, 2000	$ 360,387,878
August 1, 2000 - August 31, 2000	$ 349,658,967
September 1, 2000 - September 30, 2000	$ 338,525,307
October 1, 2000 - October 31, 2000	$ 327,342,753
November 1, 2000 - November 30, 2000	$ 316,473,400
December 1, 2000 - December 31, 2000	$ 305,194,001
January 1, 2001 - January 31, 2001	$ 294,230,516
February 1, 2001 - February 28, 2001	$ 282,853,433
March 1, 2001 - March 31, 2001	$ 271,426,387
April 1, 2001 - April 30, 2001	$ 261,059,856
May 1, 2001 - May 31, 2001	$ 249,537,099
June 1, 2001 - June 30, 2001	$ 238,337,072
July 1, 2001 - July 31, 2001	$ 226,714,524
August 1, 2001 - August 31, 2001	$ 215,417,501
September 1, 2001 - September 30, 2001	$ 203,694,298
October 1, 2001 - October 31, 2001	$ 191,919,611
November 1, 2001 - November 30, 2001	$ 180,474,710
December 1, 2001 - December 31, 2001	$ 168,598,049
January 1, 2002 - January 31, 2002	$ 157,054,032
February 1, 2002 - February 28, 2002	$ 145,074,516
March 1, 2002 - March 31, 2002	$ 133,042,390
April 1, 2002 - April 30, 2002	$ 122,126,936
May 1, 2002 - May 31, 2002	$ 109,994,032
June 1, 2002 - June 30, 2002	$ 98,200,947
July 1, 2002 - July 31, 2002	$ 85,962,968
August 1, 2002 - August 31, 2002	$ 74,067,751
September 1, 2002 - September 30, 2002	$ 61,723,787
October 1, 2002 - October 31, 2002	$ 49,325,612
November 1, 2002 - November 30, 2002	$ 37,274,687
December 1, 2002 - December 31, 2002	$ 24,769,140
January 1, 2003 - January 31, 2003	$ 12,613,849



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Unknown

From: Wagman, Steve [FI]
Sent: Thursday, September 28, 2000 5:09 PM
To: Hashmi, Azfar [FI]
Subject: Mytake on how to explain ECLN

First I would go through the prepaid on a stand alone basis. Get into why co does it (gets cash flow, shows up as other liab not debt, cflow helps to avoid large revenues (due to MTM gains going through I/S) with no cash flow...i.e. Gives some oomph to revenues. Also more efficient on a CRF basisn instead of having loan plus swap CRFn I think you just have the loan amount. Show all the boxes and arrows (crdt derivs rec fixed from delta pays delta fltg oil...delta pays fltg oil to E and rec fltg oil from E...E pays fltg oil to credt derivs and should rec fixed from credit derivs but receives ppmt upfront of this fixed leg, prepmt amt equals ppmt amt less optio prem...so far E has recd pfront money from crdt derivs less premium, all fltg oil goes in acircle so they all cancel, and E pays fixed to delta which ends up at credit derivs (net net E has money today and pays back a fized stream over time--net net economically like a loan. Now the premiums...crdt derivs buys option from delta...delta buys option from E...one option is a put, one is a call, same strike. Now that you are finished with the prepaid stand alone, you can get into the fact that the bnks are tapped out on credit for E, so they don't want to lend more and the capital markets who are willing to lend only want to lend and take vanilla sr secured risk...so, we effectively use the ECLN to take the investors money, give them vanilla sr unsercured E risk, and we use that money to fund a prepaid for E...we effectively wear the basis risk of structured credit ridk and vanilla sr unsecured, E gets money that gives them cflow but does not show up on books as big D Debt.
I'm going to send this to derek as well, so he has an idea of how it works and may be better able to follow it. I think yosemite is quite similar except I'm not sure whether the funds raised paid off the bnks who had funded previous strctured deals or whether it funnelled back to E. I will find the answer to that . Thr is minor detail missing, but not matl to following major impt concepts

Permanent Subcommittee on Investigations
EXHIBIT #145

Remite funded prepaid

Assumptions:

Notional:	$500MM
5 year oil forward rate:	$18.18
5 year oil swap price:	$18.00
Interest cost:	L + 100bps
5 year interest rate swap rate:	6.50%
Cap/Floor cost:	$1.80/bbl

Flow Calculations:

Principal in bbls - $500MM/$18.18 - 27.5MM bbls

Quarterly interest cost - $500MM * 7.50% - $9.375MM

Quarterly interest cost in bbls - $9.375MM/$18 - 520,833 bbls

Cap/Floor gross payment - $49.5MM

Citibank, N.A. is pleased to present to you the proposed transaction or transactions described herein. Although the information contained herein is believed to be reliable, Citibank makes no representation as to the accuracy or completeness of any information contained herein or otherwise provided by Citibank. The ultimate decision to proceed with any transaction rests solely with the Company. Citibank, N.A. is not acting as the Company's advisor. Therefore, prior to entering into any proposed transaction, the Company should determine, without reliance upon Citibank or its affiliates, the economic risks and merits, as well as the legal, tax and accounting characterizations and consequences, of the transaction and that it is able to assume these risks. The terms set forth herein are intended for discussion purposes only and subject to the final negotiation of the terms of a transaction as set forth in a definitive agreement and/or confirmation. This proposal is neither an offer to sell nor the solicitation of an offer to enter into a transaction. Citibank and its affiliates may act as principal or agent in similar transactions or in transactions with respect to instruments underlying a proposed transaction. This document and its contents are proprietary information and products of Citibank and may not be reproduced or otherwise disseminated in whole or in part without Citibank's written consent.

Permanent Subcommittee on Investigations
EXHIBIT #146

- Upon any early termination, obligations under the cap, both floors and Enron's 27.5MM barrel payment obligation will be valued based on the spot WTI price on the date of early termination. This term will be explicitly stated in the relevant confirmations.
- Upon any early termination, Enron's quarterly barrel obligation on the SPV swap will be limited to barrels accrued to such date - no claim will be made for remaining barrels to be delivered. The commodity swap between Citibank and Enron, and Citibank and the SPV will be structured to mirror this mechanic.
- Upon an Enron Bankruptcy Filing, termination of all trades will be automatic.
- Citibank will have the right to control the the SPV's exercise of any termination right vis-a-vis Enron.

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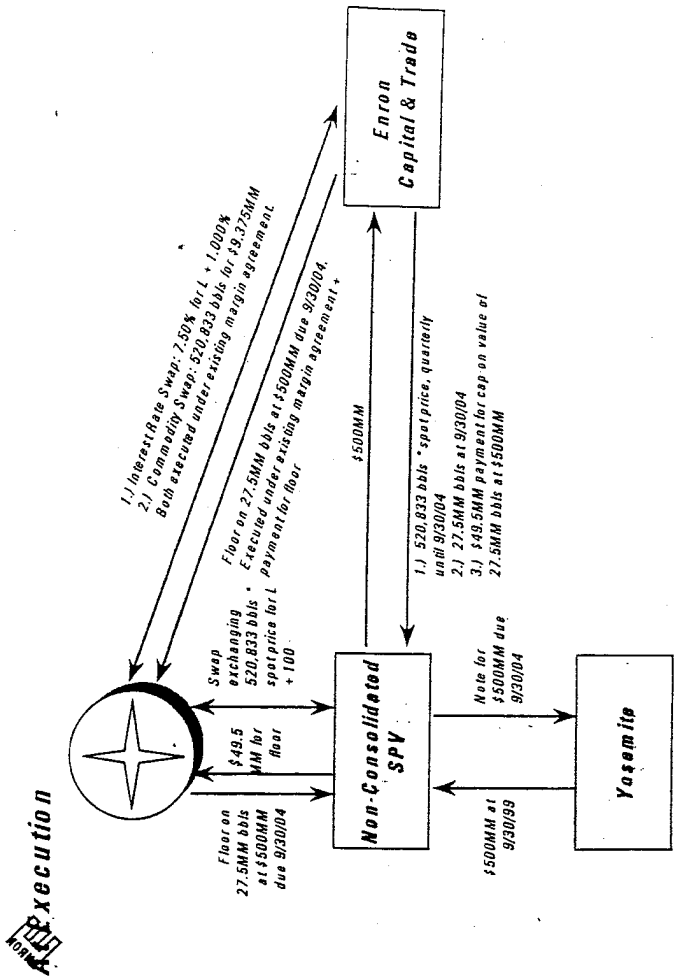
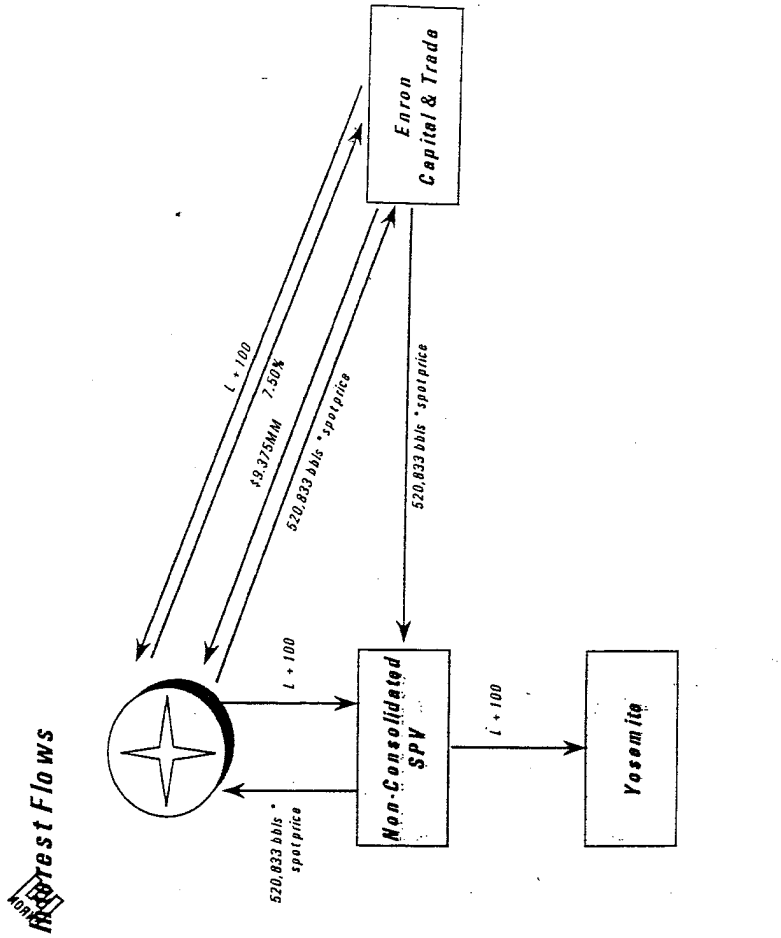
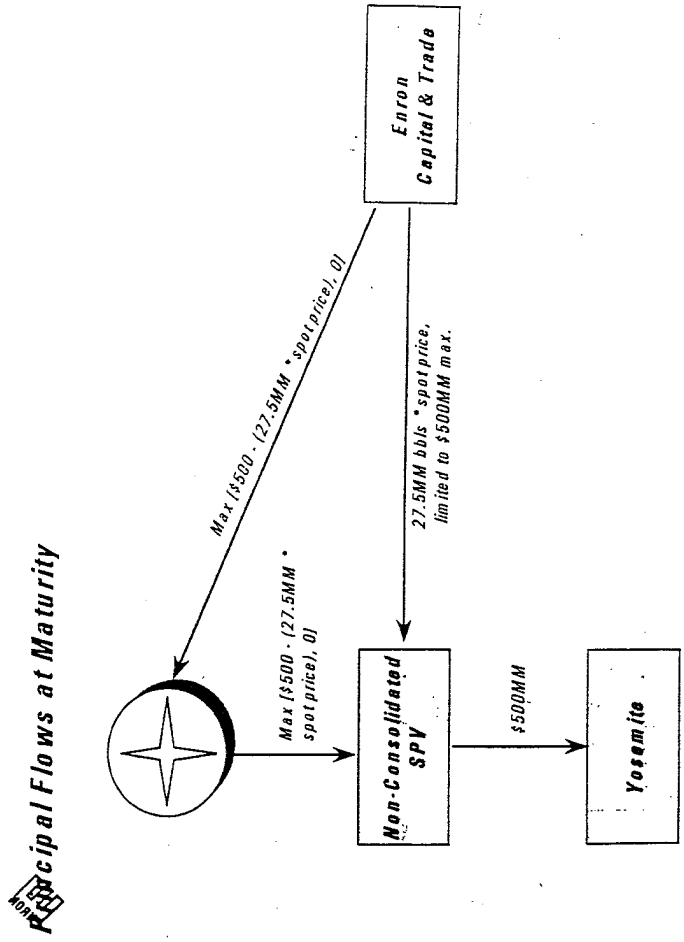

Enron Capital & Trade
1.) Interest Rate Swap: 7.50% for L + 1.000%
2.) Commodity Swap: 520,833 bbls for $9.375MM
Both executed under existing margin agreement
Floor on 27.5MM bbls at $500MM due 9/30/04.
Executed under existing margin agreement +
payment for floor
$500MM
1.) 520,833 bbls * spot price, quarterly
until 9/30/04
2.) 27.5MM bbls at 9/30/04
3.) $49.5MM payment for cap on value of
27.5MM bbls at $500MM
Swap exchanging 520,833 bbls * spot price for L + 100
$49.5 MM for floor
Floor on 27.5MM bbls at $500MM due 9/30/04
Non-Consolidated SPV
Note for $500MM due 9/30/04
$500MM at 9/30/99
Yosemite
Execution

3


Enron Capital & Trade
L + 100
7.50%
$9,375MM
520,833 bbls * spotprice
520,833 bbls * spotprice
L + 100
Non-Consolidated SPV
L + 100
Yosemite
520,833 bbls * spotprice
Interest Flows



Principal Flows at Maturity

Interoffice
Memorandum

To: Ann Marie Tiller

From: Brent Vasconcellos Department: Tax Planning

Subject: Yosemite I Withholding Date: January 10, 2000

Confidential: Attorney-Client Privilege

Pursuant to your request, I have prepared the following analysis of U.S. federal withholding tax considerations related to payments made by Enron North America ("ENA") to Delta Energy Corp. ("Delta"), a Cayman Islands exempt LLC, as part of the Yosemite structured finance transaction.

Background

On November 18, 1999, Yosemite Securities Trust I ("Yosemite"), a Delaware statutory business trust, issued $750 million in senior unsecured notes (the "Notes"). The beneficial ownership interests of Yosemite are evidenced by $75 million of certificates held by Enron Corp. ("Enron") and Long Lane Master Trust IV ("Long Lane"), a Delaware statutory business trust.[1] Yosemite is treated as a partnership for tax purposes, and the trust certificates held by Enron and Long Lane are treated as partnership interests for tax purposes. Currently, Yosemite's sole asset is an $800 million debt obligation of Delta (the "Delta Note").[2] The Delta Note originally bore interest at a rate of 6.3% payable semi-annually, although it was amended on December 22, 1999 (as discussed below) to, among other things, increase the rate to 7.25%.

Delta is checked open as a partnership and is capitalized with nominal equity held by a Cayman Islands charitable trust (the "Trust") and $800 million in proceeds, nominally in the form of a loan, from the issuance of the Delta Note to Yosemite.[3] Delta plans to take certain precautionary measures in order to assure itself of favorable tax treatment for withholding purposes by filing a Form 926 (Form 8865 which is not yet in final form) and has also included tax characterization language in the Delta Note.[4]

The $800 million proceeds received by Delta were used as a prepayment of Delta's obligation under a cash-settled swap with ENA on the price of crude oil (the "Prepay").[5] As part of a pre-arranged integrated transaction, ENA entered into a cash-settled commodity swap with

[1] Enron and Long Lane each own $37.5 million of the certificates. Long Lane is an accommodation party for Citibank through the total return swap in place between Long Lane and Salomon Smith Barney, a Citibank affiliate.

[2] Yosemite is also a swap counterparty to a credit default swap with Citibank, N.A. and has entered into a guarantee arrangement, nominally characterized as a loan, with Enron in which Enron effectively guarantees the interest payable on the Notes (although Enron's obligation is not in the nature of a traditional guarantee because it is not dependent on a payment default by Delta). Neither transaction is relevant for purposes of this discussion.

[3] The use of Delta came at the insistence of Enron Global Finance due to accounting concerns over the Yosemite investing entity's status as a special purpose vehicle (SPV). Characterization of an alternative Delta-like entity as an SPV for financial accounting purposes would have jeopardized the accounting treatment of the debt issuance by Yosemite as an off-balance sheet financing. The decision to use Delta apparently reduced such concerns based, at least in part, on ENA's prior dealings with Delta in similar swap transactions.

[4] These precautionary measures relate to withholding in calendar years 2001-2004. *See* discussion *infra*.

[5] The use of a prepaid swap was not motivated by tax considerations but instead was necessary in order to report the transaction as part of ENA's price risk management activities rather than debt for financial accounting purposes.

Permanent Subcommittee on Investigations
EXHIBIT #147

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Citibank and Citibank entered to into a cash-settled commodity swap with Delta. Citibank and Delta hold floors and ENA holds a cap on the price of crude oil at the swap's maturity. All three swaps are based on an identical notional amount. Further, the caps and floors are identically priced and have the effect of creating a hedge to all three parties. After canceling all of the redundant terms to the three swaps, ENA receives $800 million and Delta receives 6.3% interest payable semi-annually. Delta uses the interest received from the Swaps to make identical semi-annual interest payments to Yosemite on the Delta Note. Yosemite uses the interest earned on the Delta Note to satisfy the semi-annual interest payments due on the Notes and the semi-annual yield payments due on the Certificates.[6]

Due to commercial uncertainty caused by a last-minute change to a provision in the Swaps, Enron decided to shorten the tenor of the Swaps to two and a half months with a maturity date of January 31, 2000. The tenor of the Delta Note was also shortened to reflect an identical maturity date. Enron terminated the original Swaps and executed new Swaps on December 22, 1999 that reflect the originally contemplated maturity date of October 26, 2004. The Delta Note was also amended to reflect a similar maturity date. The terms under the new Swaps and the Delta Note remained substantially unchanged with the exception of the maturity date and a new interest rate of 7.25%. In connection with the termination of the original Swaps and execution of the new Swaps, Yosemite will execute a consent to these changes in order avoid a mandatory repayment of the Delta Note as required under its terms.[7]

Issues

1. In calendar year 2000, what basis does ENA have for making payments to Delta under the Prepay without reduction for U.S. federal income tax withholding under I.R.C. § 1441 and the regulations thereunder?

2. In calendar years 2001 through 2004, what basis does ENA have for making payments to Delta under the Prepay without reduction for U.S. federal income tax withholding under I.R.C. § 1441 and the regulations thereunder?

Executive Summary

1. For calendar year 2000, ENA can forego withholding on payments made to Delta under the original Prepay by relying on the short-term OID exception contained in I.R.C. § 871. ENA can also forego withholding on payments made to Delta under the new Prepay in calendar year 2000 by relying on the "portfolio interest" exemption.

2. The regulations promulgated under I.R.C. § 1441, effective January 1, 2001, would not require ENA to withhold on any payments made to Delta under the new Prepay for calendar years 2001 through 2004 on the basis that the beneficial owner of the income received by Delta is a U.S. person.

[6] These cash flows only partially satisfy the Notes and certificates. The "Magic Note" was put in place to make up the shortfall amount.
[7] For purposes of this discussion, the term "original Swaps" refers to the two-and-a-half-month Swaps that mature on January 31, 1999 and the "new" Swaps refers to the Swaps executed on December 22, 1999 that mature on October 26, 2004. Any reference to the "Prepay" or the "Swaps" also refers to the new Prepay/Swaps.

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Discussion

§ 1441 Withholding in Calendar Year 2000

Tax Characterization of the Prepay

The tax characterization of the Prepay is an integral part of the withholding analysis for calendar year 2000 because it allows ENA to identify alternative reporting positions based on the availability of withholding exemptions. Once the tax characterization of the underlying transaction is determined, the most advantageous reporting position for withholding purposes can be determined.

As noted above, the net result of the Swaps was that ENA received $800 million in exchange for interest payable semi-annually at 7.25%. Based on the economic substance of the Swaps, the Service could potentially view the Prepay as a 7.25%, $800 million loan by Delta to ENA and view the ENA/Citibank swap and the Citibank/Delta swap as swaps for tax purposes. Therefore, under this characterization, any payments made by ENA to Delta under the Prepay would be characterized as interest.[8]

Current § 1441 Regulations

The current version of the regulations promulgated under I.R.C. § 1441 are effective until December 31, 2000.[9] Those regulations generally provide that payments made by U.S. persons to foreign persons that constitute gross income from sources within the U.S. are subject to withholding tax at a rate of 30% unless an exemption applies.[10] Here, ENA is expected to make semi-annual payments to Delta under the Prepay that are likely characterized as interest. Therefore, in order for ENA to avoid the withholding obligation under § 1441, it must show either that:

- The payments constitute non-U.S. source income as:
  - Interest paid to by an 80/20 company[11]; or
  - Income from a notional principal contract

- OR -

- The payments are U.S. source income, but an exemption from withholding applies:

[8] ENA intends to report the payments under the Swaps according to their form but acknowledges that the economic substance of the Swaps for withholding purposes is a loan by Delta to ENA. ENA will obtain the appropriate withholding certificates from Delta in accordance with its acknowledgement that the Prepay is a loan for tax purposes. *See* § 1441 Documentation discussion *infra*.

[9] *See* I.R.S. Notice 99-25, 1999-20 I.R.B. 75. This notice was the second postponement of the effective date for the new withholding regulations. *See* I.R.S. Notice 98-16, 1998-15 I.R.B. 12 (moving the effective date from 1/1/99 to 1/1/2000).

[10] *See* Treas. Reg. § 1.1441-1.

[11] Under Treas. Reg. § 1441-3(a), payments that represent income from sources without the U.S. are not subject to tax and withholding. I.R.C. § 861(a)(1)(A) excludes from the definition of income from sources within the U.S., interest received by a foreign taxpayer from an "80/20 company." Thus, if the provision applies, any interest paid to a foreign taxpayer would be deemed non-U.S. source income and thus not subject to withholding. An "80/20 company" is a domestic corporation that, for the three-year period ending on the close of the taxable year preceding the interest payment, derived at least 80% of its income from all sources as "active foreign business income." "Active foreign business income" is income derived from outside of the U.S. and is attributable to the active conduct of a trade of business in a foreign country. Here, ENA does not derive 80% of its income from all sources as "active foreign business income" and thus would not qualify as an "80/20 company" under § 861.

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- Income tax treaty[12]; or
- Short-term OID exception; or
- The portfolio interest exemption

Non-U.S. Source Income

Income from a Notional Principal Contract

Under § 1441, a payer is only required to withhold on payments to foreign persons that constitute income from sources within the U.S.[13] Payments that constitute income from sources outside of the U.S. are not subject to § 1441 withholding. Under Treas. Reg. § 1.863-7(b)(1), the source of notional principal contract income is determined by reference to the residence of the taxpayer. Here, Delta is a Cayman Islands resident and thus under § 1.863-7, any income earned by it from a notional principal contract would be foreign source income. Therefore, if the payments made by ENA to Delta under the Prepay are characterized as payments made under a notional principal contract pursuant to § 1.446-3, no withholding would be required under § 1441 because the payments would not constitute U.S. source income to Delta.

Here, however the Service would likely take the position that the economic substance of the Prepay supports a loan characterization rather than a notional principal contract characterization. The $800 million prepayment by Delta would be treated as the advanced principal and the semi-annual barrel payments by ENA would be treated as interest payable to Delta on that principal. However, the payments under ENA/Citibank swap and the Citibank/Delta swap would be treated as payments under a notional principal contract. Another position the Service could take is that § 1.446-3(g)(4) applies to the Prepay. This provision generally provides that a swap that contains significant non-periodic payments is treated as two separate transactions consisting of a loan and a swap.[14] As such, all of the payments made by ENA to Delta under the Prepay would be characterized as interest rather than periodic swap payments under § 1.446-3, thus requiring ENA to identify another withholding exemption.

Exemptions from Withholding[15]

(i) Short-term OID Exception

The § 1441 regulations generally impose a withholding obligation on payments representing original issue discount under I.R.C. § 871(a)(1)(C). However, an amount representing original issue discount that is payable less than 183 days from an obligation's date of issuance is not subject to the tax imposed under § 871(a)(1)(C) and thus is not subject to withholding under § 1441.[16] Here, the original Swaps executed on November 18, 1999 provided for a maturity of January 31, 2000 and did not provide for any payments to be made during this

[12] Under Treas. Reg. § 1.1441-6(a), a foreign taxpayer may claim a reduced rate of withholding or complete exemption from withholding pursuant to an income tax treaty between the U.S. and the taxpayer's home country. The U.S. and Cayman Islands do not currently have a negotiated tax treaty in place and therefore this withholding exemption would not be available to Delta for the payments it receives from ENA.

[13] *See* Treas. Reg. § 1.1441-1. For purposes of this discussion, the term "payer" is synonymous with the term "withholding agent" under § 1441 and the regulations thereunder.

[14] *See also* Treas. Reg. § 1.446-3(g)(6) example 3. It is not entirely clear how this provision would apply to the Prepay. However, the potential does exist that the Service could apply this provision in an attempt to recharacterize the transaction.

[15] The exemptions discussed below are dependent on a characterization of the Swaps as a loan for § 1441 withholding purposes.

[16] *See* I.R.C. § 871(g)(1)(B)(i).

period.[17] Therefore, any interest component of the termination payment made by ENA to Delta is not subject to withholding since the payment contains OID payable less than 183 days from the Swaps' execution date.

(ii) The Portfolio Interest Exemption

Payments to foreign persons that constitute "portfolio interest" are generally not subject to withholding.[18] "Portfolio interest" includes interest paid on certain registered debt issued to unrelated non-bank persons. In order to be unrelated for purposes of the "portfolio interest" exemption, the foreign person may not own, either directly or indirectly, through application of the § 318 stock attribution rules, 10 percent or more of a corporate debt issuer's total combined voting power of all classes of stock entitled to vote. I.R.C. § 871(h)(3)(C) modifies the § 318 stock attribution rules by eliminating the 50-percent limitation.[19]

It is not entirely clear whether a withholding agent is required to look beyond the form of a transaction to reasonably rely on a foreign payee's claim of exemption from withholding. Here, the Service could potentially argue that ENA is required to acknowledge the economic substance of the transactions in the Yosemite structure for purposes of determining its withholding obligations under § 1441. This argument would effectively require that ENA, as a "withholding agent" under § 1441, determine the tax characterization of any transaction that ultimately determines whether it has an obligation to withhold on payments to foreign persons. In the context of payments made by ENA to Delta that constitute "portfolio interest", the Service's argument would require that ENA determine the tax character of the Delta Note held by Yosemite in order to determine whether Delta is a 10% or more shareholder in ENA under § 871(h)(3). Thus, the potential exists that the Service would disallow use of the "portfolio interest" exemption by asserting that Delta is a 10% or more shareholder in ENA.

If the Service were to attack ENA's reliance on the "portfolio interest" exemption, ENA should argue that Delta is merely an accommodation party used solely for accounting purposes and that the ultimate recipient and beneficiary of all payments made by ENA is Yosemite, who is a U.S. person. This argument should be at least somewhat persuasive because it serves as the foundation for the new but not yet effective § 1441 regulations. The new § 1441 regulations recognize that the status of the ultimate beneficiary of income should determine (as discussed further below) whether withholding is appropriate.

---

[17] The Swaps, as drafted, retained provisions that provided for interest payments beyond the maturity date of the Swaps, effectively creating OID. This was done in anticipation of the early termination and issuance of new Swaps with similar terms and a maturity of October 26, 2004.

[18] *See* I.R.C. § 1441(c)(9).

[19] The § 318 stock attribution rules, as modified by § 871(h)(3)(C), could potentially apply to Delta as follows:

1. Yosemite's constructive ownership of the ENA stock owned by Enron
   - § 318(a)(3)(A), as modified by § 871(h)(3)(C), provides that stock (the ENA stock) owned by a partner (Enron) shall be considered as owned by the partnership (Yosemite).
   - Thus, through application of this provision, Yosemite is deemed to constructively own the ENA stock.
2. Reattribution of the constructively owned ENA stock by Yosemite to Delta
   - § 318(a)(5)(A) provides that the entity (Yosemite) deemed to "constructively" own stock (the ENA stock) from the first application of § 318 is deemed to "actually" own the stock (ENA stock) for purposes of applying the attribution rules a second time (i.e., continuing ENA stock attribution down the chain of ownership to Delta).
3. Delta's constructive ownership of the ENA stock "actually" owned by Yosemite for the purposes of § 318
   § 318(a)(3)(A), as modified by § 871(h)(3)(C), provides that stock (the ENA stock) owned by a partner (Yosemite) shall be considered as owned by the partnership (Delta).

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Reporting Position for Year 2000 Payments to Delta

Loan Characterization

Given the economic substance underlying the Swaps, the most advantageous position for ENA to take is that the Prepay is a loan for tax purposes but that § 1441 withholding should not apply based on the following arguments:

1. The Swaps possess a five-year tenor that straddles the effective date of the new § 1441 regulations. The transaction should be treated consistently over its outstanding life and since four of five years' payments under the Prepay will not be subject to withholding under the new § 1441 regulations, the first year payments under the Prepay should be treated similarly.

2. By promulgating the new § 1441 regulations, Treasury recognized that the aggregate theory of partnerships was appropriate for § 1441 withholding purposes in contrast to the entity theory utilized by the current § 1441 regulations. Since Yosemite is a U.S. partner in Delta for tax purposes and is allocated all of the income of Delta, payments made by ENA to Delta should not be subject to withholding by virtue of Yosemite's status as a U.S. person under the approach embodied by the new § 1441 regulations.

3. By giving effect to the new withholding certificates, the Service implicitly authorized the use of the new regulations since the new withholding certificates were created for use under the new withholding regulations.

4. The new regulations were originally expected to take effect on January 1, 1999, but were delayed for two years and therefore ENA should be allowed to informally adopt the new § 1441 regulations.

Even if the Service were to ignore all of the preceding arguments regarding the inapplicability of § 1441 withholding to payments made by ENA to Delta in calendar year 2000, ENA should argue that once the tax is paid it is abated and therefore ENA is only potentially liable for interest and penalties.[20]

§ 1441 Withholding in Calendar Years 2001-2004

New § 1441 Regulations

As discussed above, effective January 1, 2001, the withholding rules promulgated under § 1441 will change.[21] One of the major changes under the new regulations is the addition of the partnership look-through rules which recognize that payments made to partnerships generally flow through the partnership to its partners whom are the beneficial owners of income.[22] Thus, if a payment is made to a foreign partnership in which only U.S. persons are partners, the payment would not be subject to withholding because it would be considered a payment by a U.S. person to a U.S. person under the new regulations.

[20] *See* I.R.C. § 1463.
[21] *See* note 5, *supra*.
[22] *See generally* Treas. Reg. § 1.1441-5.

The new § 1441 regulations also contemplate payments to partnerships where another partnership is a partner.[23] In such a case, the regulations require that the payer look through only the partnerships that are foreign until it can identify a U.S. person, if any.[24] For purposes of the new § 1441 regulations, language was included in the Delta Note that acknowledges its treatment as a partnership for tax purposes. Therefore, Yosemite and the Trust would be treated as partners in Delta. Yosemite is a U.S. person and the Trust is a foreign person for tax purposes. Since Yosemite is allocated all of the income of Delta under the terms of the Delta Note, any payments made by ENA to Delta after the year 2000 would not be subject to withholding under the new § 1441 regulations since they would be considered made between ENA and Yosemite rather than between ENA and Delta.

§ 1441 Documentation

In 1998, the Service announced that it would be implementing the use of new withholding certificates in connection with the new § 1441 regulations that were finalized in 1997.[25] However, the Service announced that the new certificates would be valid under the current withholding regime.[26] Generally, a U.S. taxpayer must request the appropriate withholding certificate from a foreign payee in order to meet the reliance standard under § 1441 and the regulations thereunder. (*See* Attachment A for a summary of the required withholding certificates and other tax forms discussed below).

Portfolio Interest Exemption

A foreign payee claiming the "portfolio interest" exemption from withholding under § 1441 should provide the payer with Form W-8BEN. The purpose of the form is to establish that the payee is a foreign person and that it is the beneficial owner of the income. The payer reports the payment to a foreign person on Form 1042-S and claims an exemption from withholding as portfolio interest. If ENA relies upon the "portfolio interest" exemption Delta should provide ENA with Form W-8BEN to claim its status as a foreign person and beneficial owner of the income it receives.

The Look-through Rules under the New § 1441 Regulations

Under the look-through rules of the new § 1441 regulations, a foreign partnership that claims it is not subject to withholding must provide the payer with Form W-8IMY that indicates its status as a foreign partnership. In order for the payer to rely on the foreign partnership's claim of exemption from withholding, the partnership must also provide the payer with the withholding certificates of its beneficial owners evidencing each owner's distributive share and the owner's status for withholding purposes (e.g., U.S. person, foreign person, income effectively connected with a U.S. trade or business). For purposes of the new § 1441 withholding regulations, Delta is a foreign partnership and Delta's partners are Yosemite, a Delaware statutory business trust, and the Trust, a Cayman Islands exempt LLC. Yosemite should provide Delta with Form W-9 to

[23] *See* Treas. Reg. § 1.1441-5(c).

[24] *See* parenthetical in Treas. Reg. § 1.1441-5(c)(1)(i). The documentation requirements for a withholding agent's reliance on a partner's U.S. or foreign status is discussed *infra*.

[25] *See* Announcement 98-15, 1998-10 I.R.B. 36; T.D. 8734, 1997-44 I.R.B. 5.

[26] *See* Notice 98-16, 1998-15 I.R.B. 12. The withholding certificates discussed herein refer to the new certificates.

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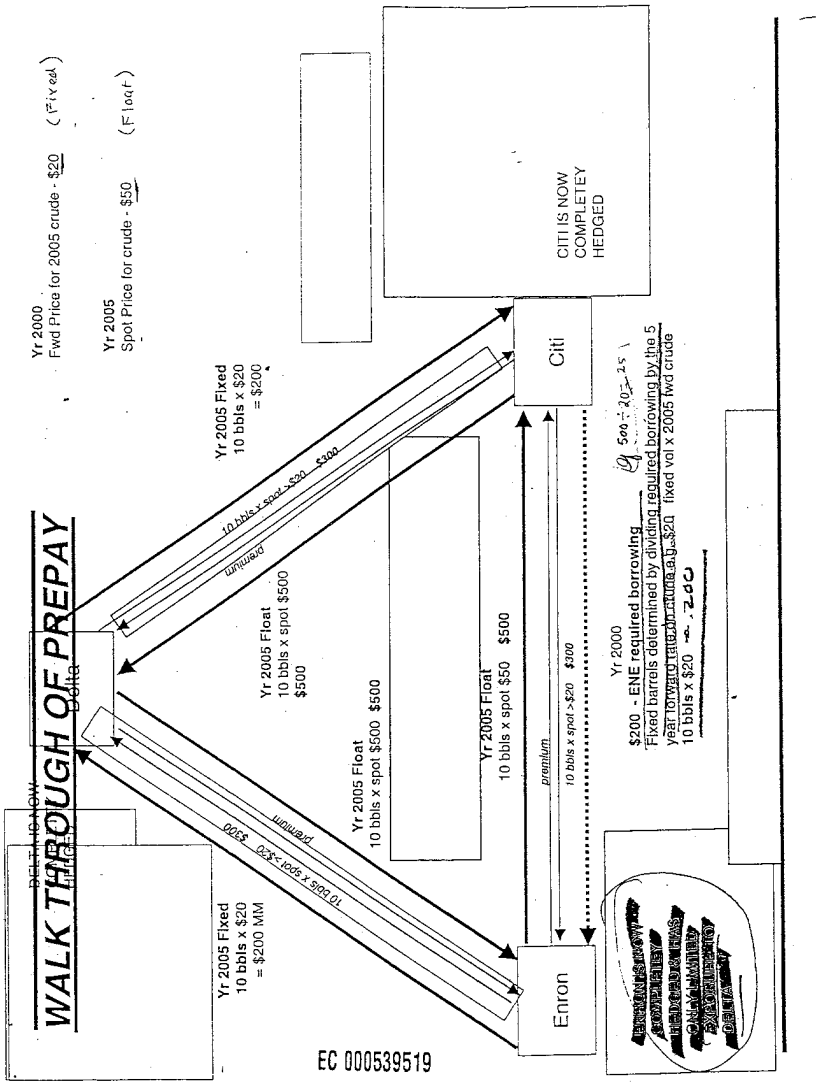
claim its status as a U.S. person. Delta should provide ENA with its Form W-8IMY and attach Yosemite's Form W-9 in order to satisfy the requirements under Treas. Reg. § 1.1441-5(c).[27]

CC: Jim Ginty
Dave Maxey
Morris Clark
Janine Juggins
Mathew Landy
Ed Osterberg

[27] As a precautionary measure, ENA should obtain these forms during calendar year 2000 based on the discussion, *supra*, regarding year 2000 reporting. The Trust need not provide a withholding certificate since none of the money paid by ENA under the Swaps will be allocated to the Trust. The Trust's "accommodation fee" will be deducted from the initial prepayment made by Delta to ENA under the Prepay.



Permanent Subcommittee on Investigations
EXHIBIT #148

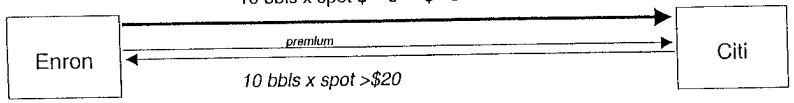
ENRON CITI LEG

Following the payment of the principal in 2000, the effect of the Enron/Citi leg is as follows:

2005 Spot Price: $100 **Net Result $200** →
2005 Spot Price: $50 **Net Result $200** →
2005 Spot Price: $0 **Net Result $ 0** →

Net result: Enron has a cap = to the original amount of principal.

Yr 2005 Float
10 bbls x spot **$100 $1000**
10 bbls x spot **$ 50 $500**
10 bbls x spot **$ 0 $ 0**

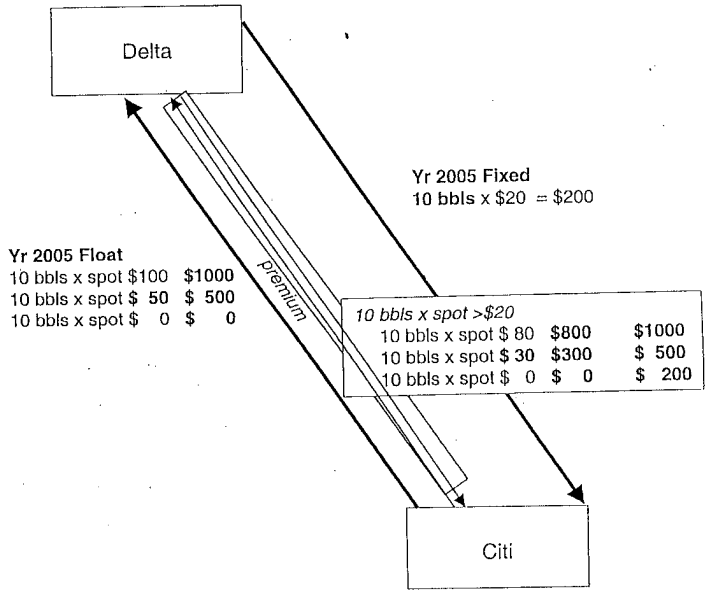


10 bbls x spot >$20

10 bbls x **$80 $800**
10 bbls x **$30 $300**
10 bbls x **$ 0 $ 0**

2

CITI DELTA LEG



2005 Spot Price: $100 Net Result $ 0

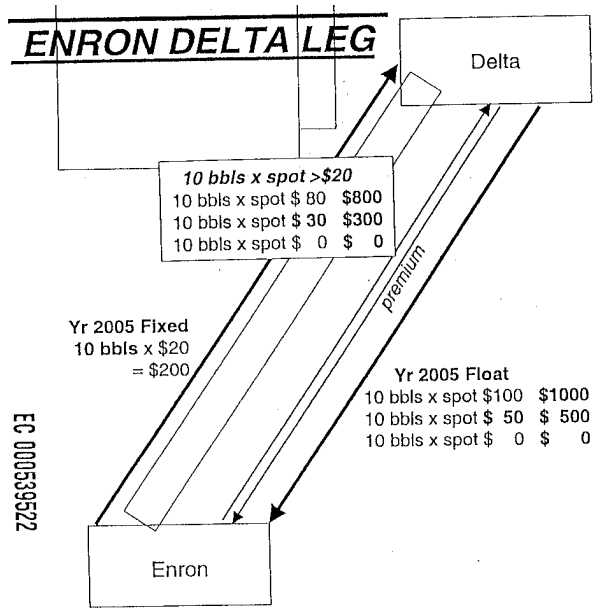
2005 Spot Price: $50 Net Result $ 0

2005 Spot Price: $0 Net Result $200

Net result: If prices tank, Citi has a floor = to the original amount of principal.

EC 000539521

3



2005 Spot Price: **$100** Net Result $ 0

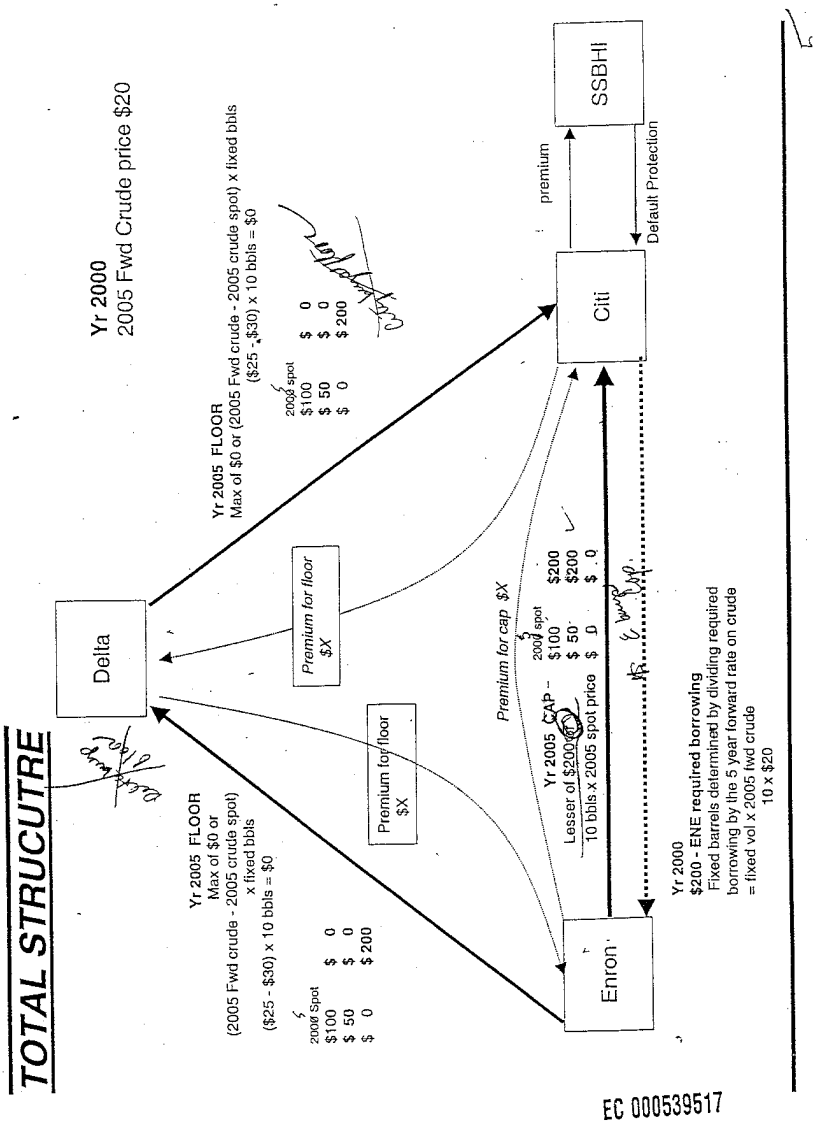
2005 Spot Price: **$50** Net Result $ 0

2005 Spot Price: **$0** Net Result $200

Net result: If prices tank, Delta has a floor = to the original amount of principal.

EC 00039522

4



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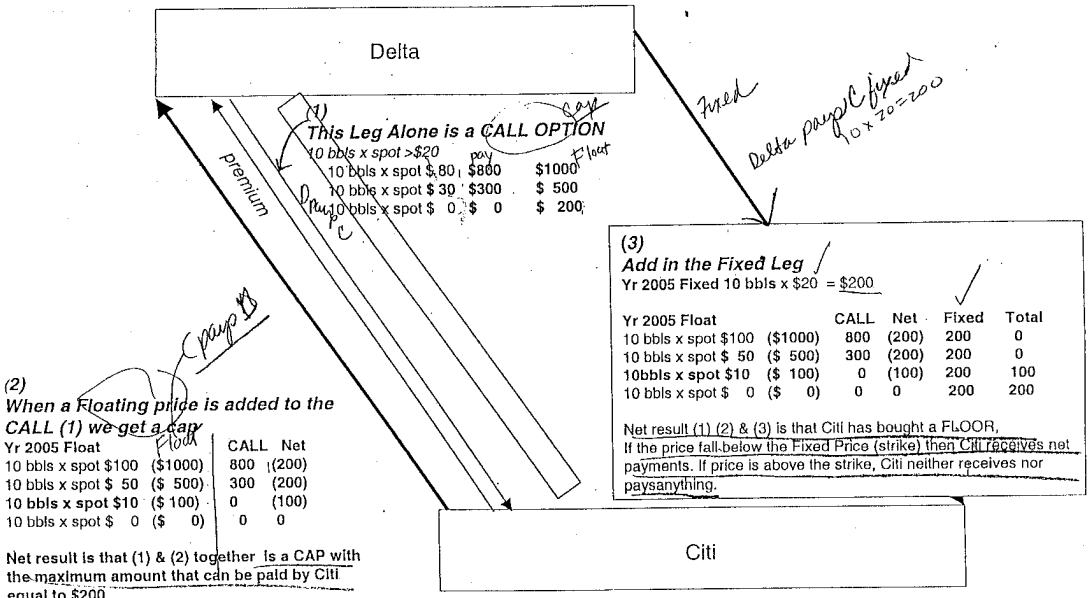
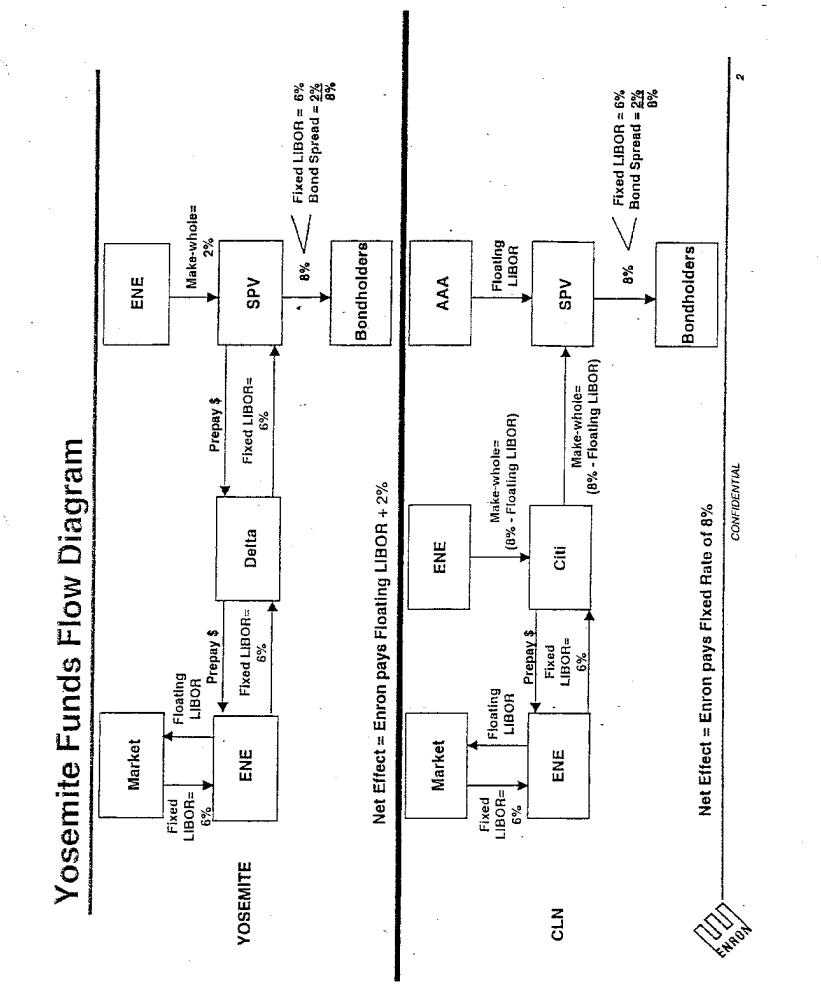


EC 000599518



Permanent Subcommittee on Investigations
EXHIBIT #149

E 23488

MAPLES and CALDER
Attorneys-at-Law

TO:	Bill Sullivan	DATE:	2 November, 1999
COMPANY:	Citibank	REF:	197468-01
COUNTRY:	USA	FAX NO.:	1-212-816-4223
FROM:	Joannah Bodden	NO. OF PAGES: (including this page)	
SENDER'S E-MAIL ADDRESS:	jlb@maples.candw.ky		

PLEASE NOTIFY US IMMEDIATELY
IF YOU DO NOT RECEIVE ALL PAGES
OUR FAX NUMBER IS 345-949-8080
OUR TELEPHONE NUMBER IS 345-949-8066 Ext. 149 (fax room)

This fax is confidential and may also be privileged. If you are not the intended recipient, please notify us immediately. You should not copy nor disclose its contents to any other person.

cc: Eric Moser, Milbank Tweed, New York Cover only 1-212-530-5219
Andrew Walker, Milbank Tweed, D.C. Cover only 1-202-835-7586

Re: Delta Energy Corporation (the "Company")

We have been contacted by Eric Moser and Andrew Walker of Milbank Tweed in relation to this Company. They have requested the information outlined in the attached email.

I noted that this information could not be disclosed until we had received authorisation from our client. In connection therewith I should be grateful if you would kindly confirm whether it is acceptable to you for this information to be provided.

Relevant contact details should you wish to liaise with them directly are as follows:

1. Eric Moser - phone: 212-530-5388, email: emoser@milbank.com

2. Andrew Walker - phone: 202-835-7500, email: awalker@milbank.com

I look forward to hearing from you.

With kind regards.

Joannah Bodden

Maples and Calder Europe, 7 Pilgrim Street, London EC4V 6AQ Tel: 44(207) 466 1600 Fax: 44(207) 466 1700
Maples and Calder Asia, Suite 1001, One Exchange Square, 8 Connaught Place, Hong Kong Tel. (852) 2521 9333 Fax. (852) 2537 2933

JNT\MS\401974681\4\0015\0\SD\P01
02 November, 1999

Permanent Subcommittee on Investigations
EXHIBIT #150

SENT BY: 9-27-91 ; 1:12PM ; CITICORP HOUSTON- 91-3023235800:# 5/ 6

CORPORATE ACCOUNTS ONLY

MUST BE TYPED OR CLEARLY PRINTED ONLY

ALL FIELDS MUST BE ENTERED OR PUT (N/A)

DDA ACCOUNT OPENING FORM PAGE 1

NEW ACCOUNT INFORMATION

1. Account Number 4065-4228 (Please list pre-assigned Account Number if applicable)
2. Account Title DELTA ENERGY CORPORATION
3. Primary Account Address C/O CITICORP NORTH AMERICA INC.
   1200 SMITH STREET - 20TH FLOOR
   HOUSTON, TX 77002
4. Attention Party CAROL ROONEY
5. Customer Contact CAROL ROONEY Telephone # 713-654-3570
6. Taxpayer ID N/A
   (required for all U.S. based companies)
7. TAFT Information (specify one): TAFT Customer number Account is to be tied to 993794 Open new TAFT Customer ☐
8. Industrial Code 4922 SIC Code _____ 9. General Ledger Code: 261
   (required field N/A will not be accepted) (required field N/A will not be accepted)
10. Credit Risk Rating 4 11. Status Code: 00
    (required field N/A will not be accepted) (required field N/A will not be accepted)
12. Credit Limit: ADR Credit -0- ACH Debit -0-
13. Daylight OD limit: -0-
14. MIP yes ☐ no ☒ Main Rate: Prime ☐ LIBOR ☐ Fed Funds ☐ Spread point _____ / MIN _____
15. Balance Type: Ledger ☐ Avail ☐ Days Calculation: 365 ☐ 360 ☐ Wire Options: Charge ☐ Waive ☒
16. Offsettable Account? yes ☐ no ☒ If yes, description _____
17. Overdraft Code ? yes ☐ no ☒
18. Statement Frequency: DAILY ☒ Plus ☐ (attach schedule) Other (specify) ☐ _____
19. Send Statements via: Regular Mail ☒ Foreign Mail ☐ Other (specify) ☐ _____
20. Number of statement sets 1
21. Duplicate Statement: yes ☐ no ☒
    Duplicate Statement Address _____
22. Max. Checks _____ Balance Plus 999,999,999.99
23. CCMS yes ☐ no ☒
    Existing CCMS Customer: yes ☐ no ☐ CCMS Customer # _____ CCMS Parent Account # _____
    New CCMS Customer ☐ (Documentation enclosed)
24. ACH Account? yes ☐ no ☒ If Yes, specify which options: (choose one (1) option only)
    What is the Parent Account Number? _____
    ____ (1) Transfer entire credit ledger balance.
    ____ (2) Transfer entire debit ledger balance.
    ____ (3) Increase ledger balance to amount to target $ _____
    ____ (4) If ledger balance falls below $ _____ Increase to target $ _____
    ____ (5) Transfer ledger balance in excess of target $ _____ in even multiples of $ _____
    ____ (6) Transfer to get $ _____
    ____ (7) If the ledger balance is between required target $ _____ Transfer amount over target in even multiples of $ _____
    ____ (8) If the ledger balance reaches target $ _____ Transfer entire credit balance.
    Sweep Accounts ? yes ☐ no ☒
    ____ (9) Known Sweep
    ____ (10) Prevue Sweep
25. Billing Type Compensating Balance ☒ Direct Debit ☐ 26. Communication Analysis - Yes ☐ No ☒ #: _____

RECEIVED BY AODU
91 SEP 27 PM 2:10

Permanent Subcommittee on Investigations
EXHIBIT #151

CITI-SPSI 0032827

MEMORANDUM TO: Beverly McPherson

FROM: Carol Rooney

DATE: September 27, 1994

RE: Delta Energy Corporation
A/C #4065-4228

The above mentioned account needs to be opened as soon as possible to facilitate a deal closing on September 30, 1994. This account is considered an internal account. It will be controlled exclusively by the Houston office until it is transferred to Citibank New York at which time it will be controlled exclusively by New York.

The account is being opened to facilitate swaps and commodities transactions. We will not be obtaining any documentation because of the internal nature of the account.

Should you require any additional information, please don't hesitate to contact me at 713-654-3590.

Approved: RAYMOND W. LOWER, JR., V.P.

Post-it® Fax Note 7671	Date 9/27/94	# of pages ▸ 6	
To BEVERLY HEPHERSON	From CAROL ROONEY		
Co./Dept.	Co.		
Phone # 4152	Phone # 713-654-3590		
Fax # 302-323-5800	Fax #		

CONFIDENTIAL

0 3 4 3 2 5 0 1 8 7

MEMORANDUM TO: Beverly McPherson

FROM: Carol Rooney

DATE: September 27, 1994

RE: Delta Energy Corporation
A/C #4065-4228

The above mentioned account will be controlled by the Houston office.

Below is a list of authorized signers on this account.

Approved:

Carol Rooney

Hilda Munoz

HILDA G. MUNOZ, AVP
Citicorp North America, Inc.
713 654-2827

J.P. Garcia

J. P. GARCIA
Senior Service Officer
Citicorp North America, Inc.
(713) 654-2827

The Givens Hall Bank

February 5, 1999

Mr. Arni Greenstein
Citibank N.A.
New York

Fax: 1 212 291 3684

Dear Mr. Greenstein,

FAXED 2/5/99

Delta Energy Corporation
Vera Energy Corporation

Following on from our earlier telephone conversation I am forwarding to you fee notes relating to the above companies.

Yours sincerely,

J.B. Benbow

Givens Hall Bank & Trust, Ltd.
Cannis Building
P.O. Box 2097 GT
Grand Cayman
Cayman Islands
Telephone 345 949 8141
Facsimile 345 949 8295
Email

Received Time May. 14. 11:35AM Print Time May. 14. 11:35AM

Permanent Subcommittee on Investigations
EXHIBIT #152

The
Givens
Hall
Bank

February 5, 1999

Delta Energy Corporation

STATEMENT FOR SERVICES

To:	Supplying the board of directors, shareholders etc. to the company and its parent company, and administering the overlying Trust for the year ending December 31, 1999.		
	Fee as agreed		5,000.00
	Reviewing and signing of documents with regard to the formal purchase and sale of oil and gas from Enron and related parties. Documents executed December 30, 1998.		
	Fee on a time spent basis		2,920.00
	Disbursements Sundry items		25.00
		US$	7,945.00

Fee Note GH 29/99

Givens Hall Bank & Trust, Ltd. | Genesis Building P.O. Box 2097 GT | Grand Cayman Cayman Islands | Telephone 345 949 8141 Facsimile 345 949 8295 Email ghbt@candw.ky

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DELTA ENERGY CORPORATION

WRITTEN RESOLUTIONS OF THE SOLE DIRECTOR
PASSED ON THIS 26th DAY OF JUNE, 2001

WHEREAS:

(A) it is proposed that the Company enter into a commodity swap transaction with Enron North America Corp. ("Enron") to be matched with a commodity swap transaction with Citibank, N.A. ("Citibank");

(B) the Company will receive a fee of US$5,000 for participating in the transaction; and

(C) it is in the Company's best commercial interests and for a proper purpose that the Company enter into the documents set forth in these resolutions.

The sole Director has reviewed and considered carefully the following documents:

(i) the Confirmation (the "Enron/Delta Swap Confirmation") between the Company and Enron to be entered into pursuant to the ISDA Master Agreement and related Schedule dated as of November 18, 1999 (the "Enron Master Agreement");

(ii) the Confirmation (the "Citibank/Delta Confirmation") between the Company and Citibank to be entered into pursuant to the ISDA Master Agreement and related schedule dated as of 27th September, 1994 (the "Citibank Master Agreement");

Documents listed at (i) to (ii) inclusive, above, are hereinafter called the "Documents".

IT IS HEREBY RESOLVED:-

1. THAT the Company should approve and, as the case may be, enter into the Documents as being in its best commercial interests.

2. THAT drafts of the Documents having been reviewed by the sole Director, the form thereof be approved on behalf of the Company subject to such amendments and additions thereto as the sole Director of the Company should in his absolute discretion and opinion deem appropriate, the signature of any such person on any of the documents being due evidence for all purposes of his approval of any such amendment or addition and the final terms thereof on behalf of the Company.

Permanent Subcommittee on Investigations
EXHIBIT #153

3. THAT the Company do give, make, sign, execute and deliver all such notes, deeds, agreements, letters, notices, certificates, acknowledgments, instructions and other documents (whether of a like nature or not) ("Ancillary Documents") as may in the sole opinion and absolute discretion of the sole Director of the Company be considered necessary or desirable for the purpose of compliance with any condition precedent or the coming into effect of or otherwise giving effect to, consummating or completing or procuring the performance and completion of all or any of the transactions contemplated by or referred to in all or any of the Documents and the Company do all other such acts and things (including, without limitation, opening all necessary bank accounts, the standard resolutions required concerning opening bank accounts with the relevant banks being hereby adopted as if set out here in full, and the sole Director of the Company or any other person authorised by resolution of the Company, all acting singly (unless otherwise resolved) being appointed as authorised signatory with respect to any such accounts) and agree all fees, as might in the sole opinion and absolute discretion of the sole Director or Attorney be necessary or desirable for the purposes aforesaid.

4. THAT the Ancillary Documents be in such form as the sole Director of the Company should in his absolute discretion and sole opinion approve, the signature of the sole Director on any of the Ancillary Documents being due evidence for all purposes of his approval of the terms thereof on behalf of the Company.

5. THAT the Documents and Ancillary Documents (where required to be executed by the Company) be executed by the signature thereof of the sole Director of the Company or where required to be sealed, by the affixing thereto of the common seal of the Company, witnessed as required by the Articles of Association of the Company.

6. THAT all the Documents and Ancillary Documents be valid, conclusive, binding on and enforceable against the Company when executed and delivered in the manner aforesaid.

7. THAT the Enron Master Agreement and Citibank Master Agreement be and hereby is reaffirmed in all respects.

8. THAT the execution and delivery of the Representation Letter be and hereby is approved and that the sole Director be and hereby is authorised to execute and deliver the same on behalf of the Company.

a duly authorised representative
of Corporate Services Ltd.

CORPORATE SERVICES LTD.

JLP\SPW\047532\04961\Jg28w05!
14 June, 2001

JUN.27.2001 17:46 212 723 9810 #012 P.003/004

Unknown

From: Swanson, Timothy [FI]
Sent: Wednesday, May 09, 2001 5:59 PM
To: Caplan, Rick [FI]; Angelini, Amanda [FI]; Incontro, Steve [FI]
Cc: Wagman, Steve [FI]
Subject: CLN PrePaids update...dry-run soon

Below is a copy of the prepaid script between Citibank/Enron/Delta as sent to Kelley McIntyre yesterday. (thanks to Steve I. for his thorough review)
The script has incorporated in the calculations a bid-offer spread in the WTI option on principal repayment at maturity ($0.01 between the written floor and purchased cap by Enron).

With respect to booking and the fact that the spread offers a more real transaction, the penny is in fact diminutive and figures to be an incremental 1 bp p.a. on the whole transaction (pv of USD315k).

I highlighted the 1 penny spread to Kelley after I sent an initial script, and in going through the spreadsheet she had noted it. I told her that the change makes the prepaid structure more like a true trade, whereas a written floor and purchased cap can not be executed at the same level - good for both parties from an auditing/regulatory perspective. She understood and did not voice any protest.

With the opportunity to capture additional revenues with the goal of enhancing any future prepaid transactions, hopefully the incremental penny will be supported by everyone.

Currently, we have prepared for the dry-run scheduled for next week.
We also should round up with them on a straight Rate Lock on the USD CLN portion (Dan Boyle attempted to set up a discussion last week to talk to the actual decision maker, but such a discussion did not occur).

Tim

Revised CLN Script

Permanent Subcommittee on Investigations
EXHIBIT #154

TRUMAN

CITIBANK

GLOBAL LOANS APPROVAL MEMORANDUM

This deal is properly recorded on Syndicator. Verified by _____ (Deal Team Leader initials required).

Memo Date: September 19, 1999 — Approval Due Date: September 24,1999

				Yes	No
X	Renewal, Repricing or Restructuring		League Table Eligible		
	Amendment (Number ____)		Agent-only	Media Disclosure	X
N	Multi-Currency (Y or N)		Co-Agent	Contact: Not Applicable	

A. KEY STATISTICS

Borrower:	Enron Corp.	Citibank Commitment ($MM):	$400 million
GFCID#:	446084	Citibank Hold ($MM):	$400 million
Deal Size ($MM):	$400 million	U/W Amount ($MM):	Not Applicable
Facilities ($MM)/Tenor:	$400 million PSR line / 67 Days	B/E Amount ($MM):	Not Applicable
Pre-approved (Y/N):	No	Accom. Amount ($MM):	Not Applicable
Date Pre-approved:	Not Applicable	Scheduled Launch Date:	Not Applicable
Origination Unit:	GEM-Houston	Scheduled Closing Date:	September 30, 1999
GRB Industry:	Global Energy & Mining	Sell Down Date(s): (if applicable)	Not Applicable
GRB Market:	US South		
Account Segment:	House	Secured (Y/N):	No
Syndicated (Y/N):	No	Obligor Exception (Y/N): (Exception Amt.):	Yes $378 million (1)
Agent(s)/Amount($MM):	Not Applicable	Liquidity, Pricing Exception (Y/N):	No

(1) Following the scheduled 9/24 repayment of Nighthawk and 9/20 repayment of Elektro

Team Leader: James F. Reilly	Tel: 713-654-2828	Back-up Contact: Steve Baillie	Tel: 713-654-2887

Pricing (bps)**:	Undrawn	Drawn	Utilization Fee
	N/A	55 bps	N/A

LT UNSECURED RATINGS:	RR for Facility (DRM)	LTM Sales	LTM EBITDA	LTM Gross Int. Coverage
BBB+/Baa2	4+	$36.3B	$2.3B	3.0x

*Stable watch at both S&P and Moody's

APPROVALS:

James F. Reilly, III
Managing Director
Citicorp Securities, Inc.
(713) 654-2828

STEVEN M. BAILLIE
Vice President
Citicorp North America, Inc.
(713) 654-2887

THOMAS E. BOLAN
Managing Director
399 Park/11/15
212/559-1544

Approval Level Required: Level 1/CPC/CE

9/22/99

H. ONNO RUDING
Vice Chairman
399 Park Avenue/2nd Floor
(212)559-2185

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Permanent Subcommittee on Investigations
EXHIBIT #155

CITI-SPSI 0021561

CITIBANK

DEAL TEAM:

Global Loans:	Origination:	Research:	Loan Investor Services:	Credit Admin:
	James F. Reilly 713-654-2820 Steve Baillie 713-654-2887	J. Trevor Randolph 713-654-2911 Sumit Mathai 713-654-2868		Carol Rooney 713-654-3590

PURPOSE:

Recommend approval for an increase and extension of the PSR line available to Global Derivatives for the "Truman" crude oil prepaid. The line will be increased to $400 million, from $320 million. Final maturity will be extended to approximately 12/6/99 from 9/30/99. Truman is an oil-prepaid transaction that closed in June 1999. The intent was to retire Truman with Yosemite, a Citi/SSB structured transaction designed to refinance Enron bank paper in the long-term capital markets, prior to the end of third quarter 1999. Due to current market conditions, however, it is now anticipated that Yosemite will not close until October/November1999.

With this approval, Enron Total Facilities will equal $1,150 million. Outstanding and unused commitments total $843 million, resulting in an Obligor Exception of $378 million. These levels reflect the retirement of the Citibank Nighthawk facility and Elektro term loan, representing reduction of $544.9 million and $52.5 million, respectively (Nighthawk is in the process of being unwound with payoff scheduled for 9/24; Elektro will be repaid on 9/20). As outlined later in the "Enron Exposure" section, we expect a significant additional reduction in Enron exposure before year-end 1999.

At the original June 30, 1999 closing, we received an upfront fee on Truman of $1.0 million. There is no additional upfront fee for the extension. The facility yields a 55 basis points drawn cost. Through not directly connected with Yosemite, the extension of Truman does facilitate its execution. Yosemite is expected to yield Citi/SSB revenues of approximately $9 million upfront and $2 plus million per annum throughout its term.

B. SUMMARY

Transaction Description:

At June 30, 1999, Citibank closed Truman, advancing $250 million in a crude oil prepaid forward sale transaction. The transaction was originally intended to have a tenor of 90 days, with repayment scheduled at September 30, 1999. Including calculated exposure on the associated derivatives, we carry our Truman exposure at an aggregate of $320 million. Truman is, in principal, similar to Roosevelt, a $500 million Citigroup arranged oil/gas prepaid that closed in December 1998, with the exception that Truman is cash settled rather than commodity settled.

In the expanded cash deal, at execution, Citibank will pay Enron $337.5 million, derived as the product of a nominal number of barrels of oil and the 9/30 crude oil index price. At maturity, Enron will deliver cash equal to the nominal number of barrels at the then current index price to settle outstandings under Truman. Commodity price risk and consequently any shortfall required to make up the balance of the loan is covered via a commodity swap with Toronto Dominion. Under the terms of the swap agreement, Toronto Dominion will pay Citibank the fixed price on the nominal barrels, in exchange for the value of the nominal barrels at the future index price. The aggregate of the exposures under this transaction will be covered by the $400 million PSR, for which we are seeking approval in this memo.

At June 30, 1999, Toronto Dominion executed an identical $250 million oil-prepaid transaction with Enron, which closed simultaneously with Truman. Citibank executed a commodity swap with Toronto Dominion, under which Citibank will pay Toronto Dominion a fixed price on the nominal product volume, in exchange for the index price. Citi then hedged this exposure with Enron. At September 30, 1999, Toronto Dominion will again execute an identical prepaid transaction, this time at the expanded $337.5 million amount. Again, we will provide a swap to Toronto Dominion and hedge our portion with Enron – exposure under the swap is included in the $400 million PSR.

Refinancing Plan:

Yosemite

Citibank expects to eliminate the Enron exposure from both Truman and Roosevelt via the $1.5 billion capital markets transaction, "Yosemite", arranged by Citibank/SSB. In Yosemite, a special purpose trust will purchase $1.5 billion of Enron loans

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from the bank market. The majority of the purchased paper will be crude oil/natural gas prepaids totaling $800-$1,000 million – including Truman ($337.5 million), Toronto Dominion ($337.5 million), and Roosevelt ($125.0 million). Yosemite is particularly valuable to Enron as a source of prepaids, because they can achieve tenors in excess of those available in the bank market. Prepaids assist in balancing the company commodity position.

The trust will fund itself via the sale 5 and 7 year Enron-Credit-Linked notes. We expect execution in October/November.

By refinancing our prepaids, Yosemite will reduce our exposure by $525 million (from the Total Facilities number on this CA). Global Derivatives and Global Energy will have credit exposure in the Yosemite transaction, currently estimated up to $75 million.

Enron Syndicated Bank Facility

Should Yosemite be unable to proceed before year-end 1999, Enron will mandate Citibank to arrange an $800 million, 1-year crude oil/natural gas prepaid. We have agreed that syndication will commence around 11/1 unless it is certain that Yosemite will sell before 12/6. Additionally;

- Enron will identify 5/7 other banks to participate, resulting in a hold position for Citi of no greater than $125/$150 million. Selection and contact will begin in early October.
- Enron has agreed that, if feasible, we will securitize the syndicated deal to eliminate GAAP/RAP positions. Preliminary review by Syndication suggests this is possible. However, further work is necessary.

Enron Exposure:

Recent/expected activity affecting our Enron exposure is outlined below. With this increase to Truman, Total Facilities are $1,150 million, commitments and outstandings are $843 million, and our Obligor Exception is $378 million. Following Yosemite, these will total $700 million, $477 million, and $26 million, respectively. Discussions continue on a range of additional incremental transactions.

($ in Millions)	Total Facilities	Obligor Exception[1]
@ 9-13-99	$1,668	$979
(Nighthawk)	(545)	(545)
(Elektro)	(53)	(53)
Truman Increase	80	95
Net @ 9-30-99	$1,150	$476
(Truman)	(400)	(400)
(Roosevelt)	(125)	(125)
Yosemite	75	75
Net @ Yosemite Close	$700	$26
New Revolving Credit	50	50
Net @ 12-31-99	$750	$76

[1]Obligor Limit increased to $450 million from $375 million in 08/99 for 4+ rated borrowers. In addition, we have purchased default swap protection that now totals roughly $80 million.

By its terms, Roosevelt has an additional 4+ years until final maturity. However, we had an agreement with Enron to prepay it on 9/30/99 (Enron prepaid $375 million on 5/1/99). As part of the Truman extension, they have asked instead to repay Roosevelt at 12/6/99.

EXPOSURE SUMMARY

(in $ millions)

Facility Description	Current	Proposed	Change
Truman Crude Oil Prepaid	$320	$400	$80
Total	$320	$400	$80

Borrower: Enron Corp.

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CITIBANK

GFCID #:	446084
LT Unsecured Ratings (S&P and Moody's):	BBB+/Baa2
Purpose:	PSR line for Prepaid Oil Inventory Financing
Deal Size ($MM):	$400 Million
Facilities ($MM)/Tenor:	$400 Million / 67 Days
Upfront Fee (bps) to Investors:	Not Applicable
Undrawn Cost (bps), FF or CF, (at current/expected ratings):	Not Applicable
Drawn Cost (LIBOR spread in bps) plus FF (at current/expected ratings):	55 bps
Utilization Fee (at current/expected ratings):	Not Applicable
Ratings Pricing Grid (Y/N):	Yes
Financial Covenants (List):	Max. senior debt-to-capital of 65% MTNW of $1.5B
Admin. Agent:	Citibank N. A.
Documentation Agent:	Not Applicable
Syndication Agent:	Not Applicable
Arrangement Fee (5 or bps):	Not Applicable
Admin. Agency Fee ($):	Not Applicable

C. RETURNS TO CITICORP

Return on transaction:

No upfront fee is payable with this extension. At original closing the upfront fee on Truman was $1.0 million. Truman is positioned to roll into the Yosemite transaction. Yosemite is positioned to generate $9.0 million upfront and $2.0 million per annum thereafter.

Return of the Relationship:

Revenue YTD July:	$18.6 million
12 Month 1998 Revenue:	$16.2 million
RORAP YTD July:	319 bps
1998 RORAP:	148 bps

D. MANAGEMENT AND RELATIONSHIP BACKGROUND

We continue to maintain an attractive, strong relationship with Enron; one that has provided over $16 million in revenues each of the last two years at well-above hurdle RORAP levels (140 bps in 1998). Our success to-date has been measured by management's comfort in our expertise and ability to structure, arrange and syndicate the company's "more-difficult", time-constrained financings.

As "Citigroup", we are now presented with additional opportunities with the company. Specifically, Citi/SSB was awarded roles in the company's common equity issuance in February, exchangeable notes issuance (related to the EOG share exchange agreement and related EOG equity offering in July), the recent Condor structured bond transaction, and forthcoming Yosemite transaction. Enron believes that with our expanded role in the bank, bond and equity markets, and specifically as its advisor in Yosemite, should come the willingness to commit capital resources as necessary.

E. **Credit Update**

June 30, 1999 Financial Update:

Enron operates as one of the largest integrated natural gas and electricity distribution companies in the world, with over $34 billion in both assets and revenues. It continues to generate consistent cash flow growth from its key operating divisions, which on a consolidated basis can now be relied upon to produce EBITDA of nearly $2.4 billion per annum. The company generated more than $2.2 billion of EBITDA during 1998, covering gross interest expense of $698 million 3.2x. Cash flow should continue to accrete even further as existing investments mature and go cash flow positive. Specifically, as of the end of 1Q99, the company reported 10 investments at a cost of roughly $6.7 billion, which it anticipated would begin to source cash flow over the course of the next twelve months. This excluded cash flow from Enron Energy Service ("EES"), Enron's retail electricity subsidiary, which the company believes will show positive cash flow (for the first time) in 4Q99.

S&P and Moody's rate Enron's senior unsecured debt BBB+/Baa2 (Citibank Obligor risk rating of 4+). Importantly, these ratings take into consideration the company's aggressive growth strategy during last few years, which aims to enhance market share in

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the deregulated, international, and clean energy markets. Concurrent with this strategy, the company remains committed to keeping its stable, investment grade credit ratings via active management of the its balance sheet. For example, during 1998, Enron financed approximately 75 transactions at a principal amount of $75.0 billion through the public, private, debt and equity markets. The company raised a significant amount of this capital through structured transactions that were (i) not EPS dilutive; (ii) segregated risk from Enron Corp.; (iii) expanded the company's lender/investor base; and (iv) overcame inherent balance sheet constraints. Most importantly, the high level of capital investments in 1998 reflects the capturing of opportunities available to Enron and an enhancement of its current franchise position. Thus far during 1999, this strategy has progressed, with Citibank and Salomon Smith Barney ("SSB") playing important lead roles via capital structuring and derivative products and investment banking expertise. In February 1999, Enron issued 13.8 million shares of common stock (stock price of $62.2875/share) and applied the proceeds towards the funding of investment activities. SSB was a co-underwriter in the transaction. Also during 1Q99, the company acquired via an unconsolidated affiliate an interest in three CoGen plants in New Jersey for 3.8 million shares of common stock. Further, in April 1998, Enron issued 17 million shares of common stock. These issuances were all met favorably by the market, as demonstrated by the company's stock price, which has appreciated more than 100% since the beginning of 1998. On a broader basis, Enron's equity market capitalization has more than doubled in the last three years and currently exceeds $30.0 billion (stock price of $42/share on September 13, 1999. The company announced a 2-for-1 common stock split that took effect in mid-August).

Outlined below is select consolidated financial data through the last twelve months ("LTM") ended June 30, 1999:

Enron Corp. Financial Summary ($ in millions)	June 30, LTM	Year Ended December 31, 1998	1997	1996
Total Revenues	$36,325	$31,260	$20,212	$13,289
Operating EBITDA	$2,388	$2,266	$1,431	$1,253
Gross Interest Expense	$791	$698	$419	$285
Net Income (unadjusted)	$688	$703	$105	$584
Capital Expenditures	$2,289	$1,905	$1,392	$864
Cash & Equivalents	$286	$111	$170	$256
Total Debt*	$9,980	$8,358	$7,247	$3,941
Total Shareholder's Equity	$11,681	$9,191	$6,765	$4,478
Debt-to-Capitalization	46.1%	47.6%	51.7%	46.8%
Debt-to-EBITDA	4.3x	3.7x	5.1x	3.1x
EBITDA-to-Gross Interest	3.0x	3.2x	3.4x	4.4x

*Including Company Obligated Preferred Securities and excluding "Off Balance Sheet Debt," which is currently estimated at roughly $2.0 billion.

In the first quarter 1999, Enron recorded an after-tax charge of $131 million related to the adoption of two new accounting pronouncements. Enron also increased its ownership percentage in Jacare Electrical Distribution Company from 47% to 53%. Jacare is the entity that previously held Enron's interest in Elektro. As a result, Jacare's balance sheet, which consisted of net assets of approximately $1,160 million, including goodwill of $1,080 million, net PP&E of approximately $820 million and debt of $900 million, was consolidated on Enron's balance sheet.

Although Enron's debt level increased dramatically over the past two years (total book debt of $10.0 billion at 6/30/99 as compared to $4.0 billion at 12/31/96), its debt to capitalization ratio of 46.1% marks an improvement from 46.8% at year-end 1996 (and 47.6% at YE98). The improvement can be traced to equity issued, partially offset by increased debt. Total debt-to-EBITDA coverage and interest coverage are not as strong as previous levels, but should see improvement in the not-to-distant future as investments mature and incremental cash flow comes on-line. Generally, though, EBITDA continues to appreciate and totaled $2,338 million for the last twelve months ended June 30, 1999. Comparatively, EBITDA was $2,266 million and $1,431 million for 1998 and 1997, respectively. Given the growth in cash flow and strength of the company's existing asset base, future debt obligations are acceptable and are estimated at: $541 million, $413 million, $666 million, $182 million and $656 million between 1999-2003, respectively.

Through July 1999, the Enron relationship had resulted in $18.6 million in revenues and a RORAP of 319 bps. Comparatively, in 1998, the Enron relationship contributed revenues of $18.2 million and RORAP of 148 bps.

Off Balance Sheet Debt:
Enron's off balance sheet debt is estimated at approximately $2.0 billion.

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Prepaids	Leases	Receivables
$700-1,000MM	$1,000MM	$0-$250MM

The above does not include equipment leases. Also, project debt, debt at JVs, and contract monetizations (as the only Enron obligation here is to deliver gas and power) are not given consideration in the above calculation.

In addition, Enron uses a myriad of structured financings, including:

Transaction	Size	Purpose	Take-Out
Condor	$1,500	Nighthawk Refinancing/Asset Monetizations	Equity
Rawhide	750	Minority Interest Equity/ Asset Monetizations	Cash Flow/Asset Sales/Refinancings
Marlin	550	Wessex acquisition finance	Equity
Firefly	415	Elektro acquisition finance	Equity
Total	$3,215		

EOG:
Enron announced and completed a share exchange agreement with Enron Oil and Gas early in the third quarter of 1999, which established EOG as a company independent of Enron. Under the agreement, Enron exchanged roughly 80% of its 82 million shares of EOG common stock for EOG's China and India operations. In connection with the exchange, EOG contributed $700 million in cash to one of EOG's India subsidiaries. Concurrent with the share exchange, Enron sold exchangeable notes, which are mandatorily exchangeable into 11.5 million EOG common stock currently owned by Enron. As a result, upon closing of the transaction in late August, Enron's ownership of EOG was eliminated entirely, and the EOG board of directors was renamed, with all Enron officers and directors resigning their positions on the EOG board.

Although EOG has long been regarded as one of the lowest cost E&P companies in North America, management believed that the capital commitments required of an exploration and production operation had become too substantial for the risk inherent in the business (i.e. the risk of dry holes and commodity prices). Enron management would rather re-deploy this capital along other business lines in an effort to facilitate a midstream/downstream integrated energy approach. The ultimate divestiture of EOG had been anticipated since 4Q98.

Enron Corp. ($ in Millions)	EBITDA	Total Debt	Total Equity	Debt/Cap.	Debt/EBITDA	EBITDA/Int.
December 31, 1998	2,266	8,358	9,191	47.5%	3.7x	3.2x
LTM June 30, 1999	2,338	9,980	11,681	46.1%	4.3x	3.0x
LTM Pro Forma for Share Exchange	1,888	7,940	11,681	40.5%	4.2x	2.9x

Given that EOG was consolidated on Enron's balance sheet; (i) all assets and liabilities, including debt of $1.2 billion were de-consolidated; (ii) the incremental cash flow provided by EOG (roughly $450MM for 1998) is gone; and (iii) interest expense at Enron will be reduce going forward by approximately $140 million (based upon a 7% interest rate, and assuming the $700 million cash from the share exchange and $200 million cash, net of transaction costs, from the exchangeable notes are applied towards outstanding debt).

Conclusion:
In summary, despite financial market uncertainty and commodity price volatility (over the last two years), Enron continues to demonstrate an ability to generate solid cash flow and predictable earnings, all-the-while significantly growing its asset base and market presence. At the root of this success is a stable, yet diversified, operating system which affords management the opportunity to grow and seek out new market share. Among integrated energy companies, Enron appears well-positioned in two areas regarded as critical to global energy: (i) the deregulation of wholesale and retail energy markets in developed economies; and (ii) the privatization of energy and utility infrastructure in emerging economies. The company is also aggressively pursuing market share in other "new" energy markets, including wind and solar power, and in communications, business that many believe will blossom in near future.

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From: McDowell, Doug
Sent: Wednesday, November 14, 2001 3:23 PM
To: 'rick.caplan@ssmb.com'

Spoke to tim despain and greg caudell apparently an investor spoke to someone at citi and received info on delta. This person at sumitomo is now calling us asking about delta now. We need to shut this down.

Permanent Subcommittee on Investigations
EXHIBIT #156

From: McDowell, Doug
Sent: Wednesday, November 14, 2001 3:34 PM
To: 'rick.caplan@ssmb.com'
Subject: Re:

Not sure just received a call from some guy at sumitomo trust who indicated that they had received this info from citi. Give greg caudell a call--left you a voicemail--and he can give you the name and details on the call.

From: McDowell, Doug
Sent: Wednesday, November 14, 2001 3:34 PM
To: 'rick.caplan@ssmb.com'

By the way--not blaming you guys just trying to figure out how to shut it down.

Yosemite Update

Original Objectives	Current Comments
Reduce bank exposure/ increase bank liquidity	• Bank exposure to Enron can be reduced on a "transaction" basis via 100% buyout or on a "target bank" basis via credit default swaps
Maintain existing balance sheet treatment of transactions	• The Yosemite SPV will not be consolidated. When loans are purchased, the underlying accounting treatment will remain unchanged as Yosemite will simply replace the banks as the lender under the original documentation
Warehousing capability	• The Citibank Swap combined with the Enron credit-linked notes provides for a unique "black box" feature which provides considerable flexibility for substitution
Expand investor base beyond commercial banks/top tier institutional investors	• Investors in capital markets have ability to purchase a synthetic ENE Bond through black box feature • Black box allows Enron the ability to provide a permanent take-out feature for highly structure transactions in the capital markets while limiting disclosure of prepay to Citibank. Limitations are ability of Citi to wear the basis risk and a restriction on the maturity date to match the Yosemite maturity
Cost-efficient source of funding	• In certain cases, Yosemite can underwrite • Demonstration of vehicle for permanent take-out of bank financings provides benefits of increased competition to banks

Permanent Subcommittee on Investigations
EXHIBIT #157

ECa000196339

Optional Use as Prepay Funding Vehicle

- Need for prepay financings to generate FFO are anticipated to be ~$1Bn/yr
- Continued use of bank financings for prepay transactions are limited by the following:
  - Banks are reluctant to provide longer-term funded prepays; either a premium is paid for the longer tenor or continued refinancing risk is assumed if a shorter tenor is chosen
  - Finite capacity exists in the surety market and bank market; each incremental deal will likely be more expensive
  - Traditional bank prepays include exposure through the commodity swaps as well as the loan exposure
  - The use of prepays as a monetization tool is a sensitive topic for both the rating agencies and banks/institutional investors. The ability to continue minimizing disclosure will likely be compromised if transactions continue to be syndicated.

ECa000196341

"Credit-Linked Notes ("CLNs")"

May 2001

Derivatives Capital Markets

CITIBANK | SALOMON SMITH BARNEY

Permanent Subcommittee on Investigations
EXHIBIT #158

Transaction Summary

- Many companies use structured debt for funding, and these transactions offer significant accounting and rating agency benefits when compared to straight corporate debt financings.
- Citigroup has developed and executed a Credit Linked Notes (CLNs) structure that separates and places each of these risks in the most cost-effective markets.
  - The Bank Markets have traditionally been where structured debt has been placed. Banks analyze and understand complex structures, while keeping the structures confidential.
  - The Capital Markets have traditionally understood credit risk and can accommodate larger concentrations of corporate credit with longer tenors.

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Transaction Summary (cont.)

- With industry consolidation, many banks are approaching their capacity for structured credit, and are increasingly struggling to take concentrated corporate credit and/or longer-dated exposures
- CLNs can be used for accessing Capital Markets with minority interest structures, synthetic leases, commodity prepays, and other structured transactions
- Benefits of CLNs include:
  - Preserves bank liquidity / refreshes existing capacity
  - Accesses Capital Markets while maintaining accounting and rating agency treatment of the structured financing
  - Eliminates the need for Capital Market disclosure, keeping structure mechanics private
  - Allows for larger, longer-tenor transactions

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Recent Credit Linked Notes

Over $3 billion total size

Citigroup has executed Five major transactions employing derivatives technology to transfer credit risk to the capital markets via a synthetic bond.

Capital Markets Deals Completed	Yosemite I November 14, 1999	Yosemite II February 23, 2000	Enron Credit Linked Notes August 25, 2000	Energy Co. Credit Linked Notes March, 2001	Enron Global Credit Linked Notes May, 2001
Size:	$ 750 million	£ 200 million	$500 million	$335 million	$200 million, £200 million, EUR300 million
Issuer:	Yosemite Securities Trust I	Yosemite Securities Company Ltd.	Enron Credit Linked Notes Trust	Energy Co. Credit Linked Notes Trust	Enron Credit Linked Notes Trust
Final Maturity:	5 Years (November, 2004)	7 Years (February, 2007)	5 Years (August, 2005)	5 Years (April, 2006)	5 Years (May, 2006)
Coupon:	8.25%	8.75%	8.00%	- - -	8.00%
Ratings:	Baa1 / BBB+	Baa1 / BBB+	Baa1 / BBB+	- - -	Baa1 / BBB+
Highlights:	Largest single name credit linked note offering to date	A groundbreaking offering that introduced Sterling investors to Enron and synthetic bonds	Simplified structure Two times oversubscribed priced at 52bps spread to Enron's new issue price	Raised funds in an accounting friendly manner Enhanced time to funding with a syndication of banks Preserved structure details of transaction	Global Appeal of credit linked note offerings Access to non-USD markets

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Recent Credit Linked Notes (cont.)

- As a leader in innovative structures, Citigroup has applied new derivatives technology to the basic corporate finance needs of its clients, as evidenced by the recent marketing of over $3 billion in synthetic financings that repackage the credit risk of structured bank loans
- Salomon Smith Barney Debt Capital Markets has established a track record for excellent execution of "first time" deals
- Currently over $1 Billion in the execution process

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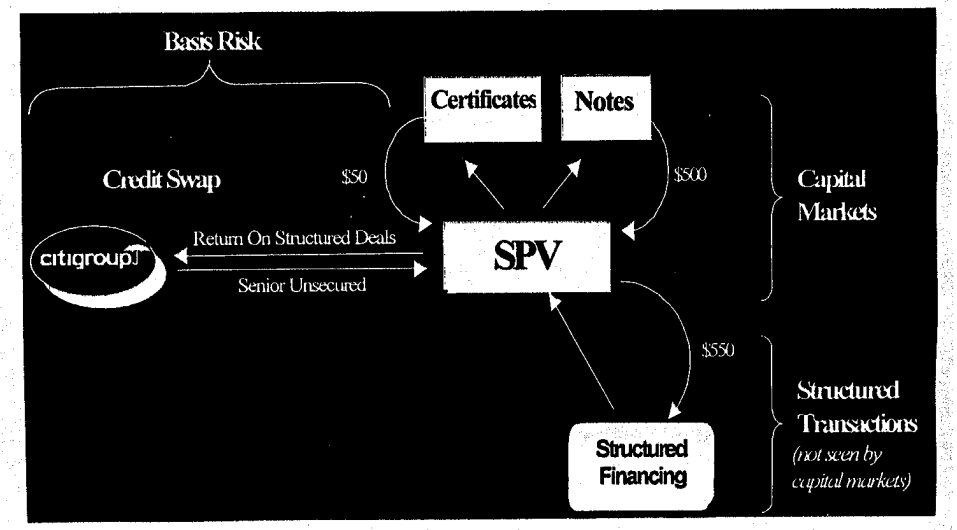
Structure Overview



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Structure Overview (cont.)

- Citibank creates an SPV that will issue "Company" Credit Linked Notes to the capital markets
- The proceeds of the notes will be used to purchase structured financings
- SPV enters into the Citibank Swap that provides, in the absence of a Credit Event, that Citibank receives any periodic distributions on the structured financings and makes interest payments on the Notes and the yield on the Certificates
- If "Company" defaults or enters bankruptcy, Citibank will have the right to settle the Citibank swap by delivering senior, unsecured obligations of "Company"
- The "Basis Risk" Citibank assumes in the Credit Swap is the difference between the structured deal's credit risk and that of "Company" senior, unsecured debt

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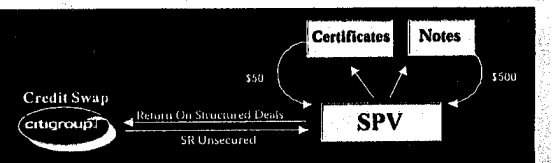
Credit Swap

Scenario 1: All Goes Well

SPV purchases Structured Transactions from Citibank

Citibank pays coupon of the notes to the SPV

SPV pays coupon of the notes to the investors



Scenario 2: A Credit Event Occurs

- "Company" Credit Events in a credit swap will be limited to:
- Payment default by "Company" on senior, unsecured obligations in an aggregate outstanding amount in excess of $25 million
- "Company" bankruptcy

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Credit Swap (cont.)

Scenario 2: A Credit Event Occurs (cont.)

- Upon a "Company" Credit Event, Citibank will settle the credit default swap by delivering Deliverable Obligations to the SPV
  - Deliverable Obligations may include
    - "Company" senior unsecured notes
- After a "Company" Credit Event, the SPV will pay principal plus accrued and unpaid interest to the Noteholders from proceeds received from the sale or workout of the Deliverable Obligations

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Rating Agencies

Treatment of the trust notes

- A credit linked note transaction will be rated by Moody's and S&P
- Three prior transactions have received the same rating as the company's senior unsecured credit rating, based upon the support of the Citigroup credit swap

Effect on overall credit rating

- Each rating agency will perform a review of the credit linked note transaction
  - Citigroup will be the primary contact with the rating agencies

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Rating Agencies (cont.)

- Effectively, the money raised is reverting to Citibank and *not* "Company". As such, "Company" is not raising funds by issuing the notes
- Rating agencies will *not* view the proceeds raised from the offering of the credit linked notes as "Company" debt
- SPV Investments purchased by the SPV are unknown to the investors and the rating agencies
  - In past transactions, the rating agencies have been told that these obligations were already included in the financials of the relevant company
- No negative impact to rating agencies view of the company
- Accounting treatment for any structured transactions should not be impacted

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Advantages of Credit Linked Notes

- Allows structured transaction access to the Capital Markets
  - However, structure remains private – no Capital Markets disclosure
  - Easily understood and accepted by fixed income investors and rating agencies
- Avoids syndicating and explaining new underlying transactions to its banks, potentially speeding up the closing and funding of assets
- Allows the Company to amend the terms of the underlying structure *(sell assets, etc.)* by dealing with one party *(Citibank)* instead of a syndicate or bond investors

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Advantages of Credit Linked Notes (cont.)

- Avoids impacting Tax / Accounting / Rating Agency Treatment of the original structure
- Preserves valuable bank liquidity *(New Deals)*
  - Refreshes existing capacity *(replace banks in existing deals)*, extends term of existing deals
- Ability to package many smaller individual structured deals together for efficient capital markets execution
  - Can add various additional structure types to increase size and term
- Executable in the Capital Markets or Bank Markets, in order to optimize "Company"'s use of the credit markets

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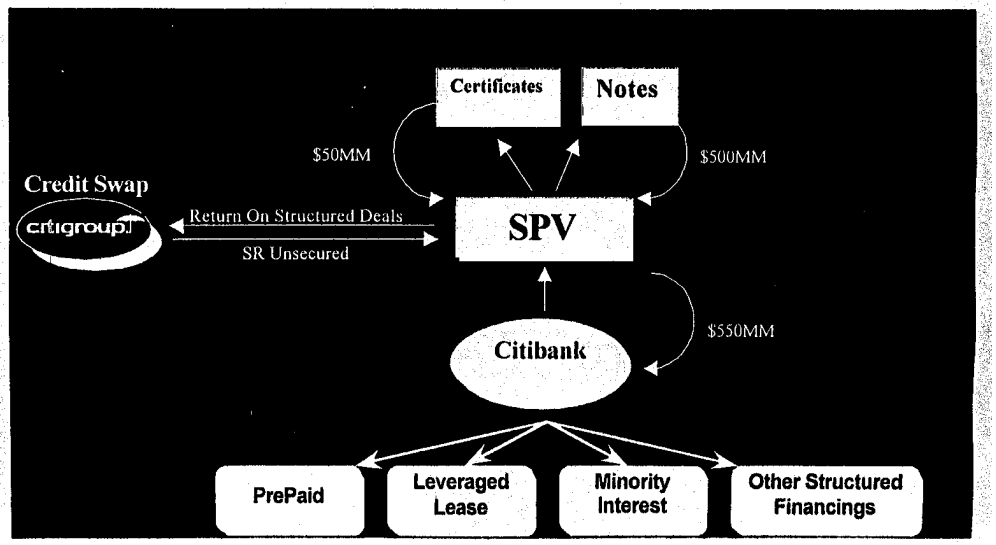
Transaction Summary - *Many Applications*



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Transaction Summary - *Many Applications* (cont.)

- Transaction considers replacing banks on existing structured debt [prepays/minority interest/leverage leases, etc.] thereby refreshing bank capacity
- Expands capability to raise non-debt financing and incorporate structures to improve cash flows from operations (i.e. pre-paids)
- Citibank takes "basis" risk between structures and senior unsecured debt
- Capital markets look to the credit swap and do not see the structures
- Possibly revisits structures that were earlier considered, but tabled because there was a concern about using bank capacity

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Selected Secondary Levels

Issuer	Rating	Coupon	Maturity	Amt ($mm)	Bid Spread (bp)	5year Equivalent (bp)
Structured Offerings						
Osprey Trust	Baa2/BBB	7.797%	01/15/03	$750	+220	+240
Yosemite Sec Trust I	Baa1/BBB+	8.250%	11/15/04	$750	+230	+238
ECLN	Baa1/BBB+	8.000%	08/15/05	$500	+220	+225
Enron Corp.	Baa1/BBB+	6.750%	09/01/04	$100	+185	+190

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Yosemite
Issues/Timeline

Original Yosemite	vs	CLN
Blackbox		Blackbox
144 A no reg rights only		Public registration option
Faster execution:	Same documentation	Slower execution: Primarily same documentation
	No structural changes	Some structural changes
	Sold as same deal	Sell as different, improved structure
No use of Citibank balance sheet		Use of Citibank balance sheet (no mark against credit)
Marketing: Enron story only		Marketing: Potential for Citibank story--less of Enron story

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EXHIBIT #159

CLN Structure

Very similar to the original Yosemite structure with a few basic improvements. Open issues are as follows:

Issues:		Action	Timeline
SPV Permitted Investments:	Use of GIC or Salomon floating rate note would allow for Grantor Trust treatment which could minimize the equity requirement to 3%	Discuss with Tax, confirm no need for any equity, 3% is only to satisfy	Complete by Friday (July 7)
Categories of Deliverable Obligations:	Critical difference in the structure which would allow for registration and provide the investors with greater understanding of specific types of senior unsecured Enron paper representing their ultimate collateral. Limitations on deliverable obligations may limit our ability to substitute with Citibank--they may be less inclined to wrap a transaction which they do not feel would fit the deliverable definition.	Finance review with legal review.	Obtain V&E assessment and Milbank will obtain preliminary view from SEC as to the basic concept by next week
$ 25 MM Magic Note	In order to avoid Citibank absorbing any credit risk associated with the magic note, the prepay or transactions within the SPV would need to be cross-defaulted to the magic note in order for Citibank to be able to settle the entire default swap.	Discuss with internal acct.	Answer by Friday (July 7)
Upfront Fees:	Amortize or expense immediately. Would obviously like to capitalize and amortize over the life of the CLN term.	Discuss with internal acct/crude desk	Answer by Friday (July 7)
Placement of Equity:	We utilized a wrinkle in the swap which allowed for Citibank to over-collateralize its equity position in the prior transaction. If we use the same concept, it will add some complexity to the swap document but it was not questioned at all by the rating agencies or investors. Citibank may need outside equity of 3% however which means they may not be the optimal party to hold the equity.	Open	Open

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Citibank

Global Markets

Structured Risk Management

Citibank
399 Park Avenue
7th Floor
New York, NY
10043

Adam Kulick
Vice President
Tel: (212) 291-0742
Fax: (212) 291-1261

CITICORP

Memo to: Project Yosemite Working Group

From: Adam Kulick, Gary Davis

Date: February 4, 1999

Subject: Initial thoughts on structures

The purpose of this memo is to outline the structure we discussed at the meeting on 1/19/99.

Client Objectives

The goal is to increase the capacity of top tier banks to take more exposure to the client. Successful strategies will effectively defease the top tier banks' risk and will take into account the following considerations:

Maintain the client's accounting and rating agency treatment of the existing deals;
Achieve ability for client to change or prepay the deals covered by the credit protection;
Close quickly;
Diversify investor base;
Create substantial amount of protection – approximately $1 billion.

The ideal solution will take into account the folding:

Mitigation of loss recognition: Many of the banks's assets are below market due to widening credit spreads. Sale of these assets would trigger mark to market losses for the institutions.
Minimization of complexity: The client does not wish to have to explain the details of many of the assets to investors or rating agencies.
Maintenance of bank group in existing deals: Ideally, non-tier 1 participant banks in the deals will be unaware of the "sale" of the existing positions of the tier 1 banks.

Solution

Permanent Subcommittee on Investigations
EXHIBIT #160

Citigroup Response to July 2 Subpoena
Senate Permanent Subcommittee on Investigations

Summary in Lieu of Production of Document

The following are the names of Citigroup, Inc. clients or counterparties that engaged in pre-paid forward transactions with a special purpose vehicle and a description of (1) the number of transactions; (2) identities of any special purpose vehicles used by the client or counterparty; and (3) whether or not price risk was hedged with Citigroup:

Arkla Exploration Company (1992):
(1) One transaction
(2) International Commodity Merchants
(3) Undetermined (documents have not yet been located)

Amerada Hess Corporation (1993):
(1) One transaction
(2) Delta Energy Corporation
(3) Price risk hedged on the NYMEX, not with Citibank.

Enron Corporation: (1) Transactions identified below, as follows:

- December 1993
  (2) Vega Energy Corporation
  (3) Price risk hedged on NYMEX

- September 1994
  (2) Delta Energy Corporation
  (3) Some price risk hedged with Citibank

- December 1998
  (2) Delta Energy Corporation
  (3) Price risk not hedged with Citibank

- June 1999
  (2) No SPV was used; Toronto Dominion was a counterparty
  (3) Citibank was counterparty to hedges with Toronto Dominion

- November 1999
  (2) No SPV was used; Toronto Dominion and Royal Bank of Scotland served as counterparties
  (3) All three bank counterparties engaged in price risk hedges

Permanent Subcommittee on Investigations
EXHIBIT #161

- December 1999
  (2) Delta Energy Corporation
  (3) Price risk hedged with Citibank

- February 2000
  (2) Delta Energy Corporation
  (3) Price risk hedged with Citibank

- August 2000
  (2) Delta Energy Corporation
  (3) Price risk hedged with Citibank

- May 2001
  (2) Delta Energy Corporation
  (3) Price risk hedged with Citibank

- June 2001
  (2) Delta Energy Corporation
  (3) Price risk hedged with Citibank

With respect to request 1(c), for which we have interpreted "a financing structure similar to Yosemite" to mean a credit linked note with a prepaid placed in the trust structure, Citigroup did not execute a financing structure similar to Yosemite for any client other than Enron. Citigroup made presentations regarding financing structures similar to Yosemite (referred to generically as "credit linked notes") to the following companies:

Williams Cos.	Kerr-McGee
El Paso	NiSource
Mirant	PG&E Corporation
Dynegy	Devon Energy
AEP	Dominion
Reliant	Duke Energy
Equitable Resources	Phillips 66

Jane C. Sherburne
Deputy General Counsel

Unknown

From: James F. Reilly
Sent: Tuesday, April 20, 1999 3:42 PM
Subject: Re: Enron/Project Roosevelt

Distribution:

To: William Fox

Bill: Feedback from Loan (Victorin thru Gorte) is very negative. They suggest:

- Accept the $310MM paydown and immediately commence syndication of the remaining $190MM; or
- Accept the $310MM paydown as a reduction in the underwriting position and immediately commence syndication of the remaining $65MM underwriting position; or
- Energy increases our hold to accomodate the remaining $190MM as our hold position (up from $125MM).

Not very constructive from my perspective. Enron recognozes that this is a change from their previous statements that the full $500MM would be retired by 5/1. They know that we could syndicate under terms of our closing agreements. They are asking a "favor". Again, I would be comfortable with their undertaking to repay the remainder by a date certain. The $310MM repayment is not a small move in the direction of early repayment.

Can you call either at home tonight or in the AM. I have a conference call with SSB at 830AM - I should be in around 800AM.

_____ Forward Header _____

Subject: Re: Enron/Project Roosevelt
Author: Thomas Stott at 01USNYC/o=AF1/c=US/a=MCI/p=CITICORP
Date: 4/20/1999 9:32 AM

The $190MM is supported by what ....straight Enron risk . Would not like to see tenor past 9/30 due to year end back up.

_____ Reply Separator _____

Subject: Enron/Project Roosevelt
Author: James F. Reilly at 10USHOU/o=AF1/c=US/a=MCI/p=CITICORP
Date: 4/19/1999 5:59 PM

Roosevelt is the $500MM natural gas and crude oil prepaid closed for Enron last December. Citi provides 100% of this deal, with a hold of $125MM and an underwriting of $375MM. Syndication was scheduled for the second quarter if Enron had not repaid the deal, as was their stated intention. Enron delivery obligations under the prepaid are backstopped by surety bonds from insurance companies approved by Global Insurance until 6/30. Hydrocarbon deliveries are scheduled to commence in the near future. In recent conversations, Enron indicated that Roosevelt would be repaid in its entirety before 5/1.

Today, Enron requested that we consider the following:

- Before 5/1, Enron will repay approximately $310MM, reducing the

Permanent Subcommittee on Investigations
EXHIBIT #162

outstanding to roughly $130MM.
- The $310MM repayment corresponds to the natural gas portion of Roosevelt - Enron is closing another gas prepaid soon and will use the procedds of that to reduce Roosevelt.
- The remaining $130MM would stay outstanding without amortization until no later than November/December 1999. Within that time frame, Roosevelt would be fully repaid.

Enron characterizes this as a "favor" - they do not wish to repay Roosevelt without full corresponding refinancing and they were unable, with all else that has been going on, to arrange the crude oil refinancing piece in time (the prepaids go into their commodity "book" so repaying requires a offsetting deal to keep the "book" in balance). The Nov/Dec time frame provides cushion.

Joe Mackiewicz has spoken with Global Insurance and thinks they will extend their approval of the sureties to some later date (atleast September). Even without their support, I think we should approve the changes given the short time frame and the firm promise to fully repay before YE99.

2.txt (495 B)

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CITI-SPSI 0068750

Author: Tom Boland at 20USNYC/o=AF1/c=US/a=MCI/p=CITICORP
Date 4/28/1999 9:17 AM
Priority: Normal
TO: John J. Kennedy at 14USNYC/o=AF1/c=US/a=MCI/p=CITICORP,
James F. Reilly at 10USHOU/o=AF1/c=US/a=MCI/p=CITICORP,
H-Onno Ruding at 20USNYC/o=AF1/c=US/a=MCI/p=CITICORP
CC: Steve Baillie at 22EXTNL/o=af1/c=us/a=mci/p=citicorp,
William Fox at 20USNYC/o=AF1/c=US/a=MCI/p=CITICORP,
David B. Gorte at 10USHOU/o=AF1/c=US/a=MCI/p=CITICORP,
Chris Lyons at 10USHOU/o=AF1/c=US/a=MCI/p=CITICORP,
Sumit Mathai at 22EXTNL/o=af1/c=us/a=mci/p=citicorp,
Trevor Randolph at 11USHOU/o=af1/c=us/a=mci/p=citicorp, Thomas Stott at 01USNYC
Subject: RE: Re: Enron/Consent to Amendment to Roosevelt Transactio

---------- Message Contents ----------

Providing the subsequent transaction which will generate the $175MM to pay down our facility in no way compromises the structure of the original transaction
I am o.k.

-----Original Message-----
From: Reilly, James F.
Sent: Tuesday, April 27, 1999 1:09 PM
To: Ruding, H-Onno; Kennedy, John J.; Boland, Tom
Cc: Fox, William; Stott, Thomas; Gorte, David B.; Baillie, Steve; Lyons, Chris; Mathai, Sumit; Randolph, Trevor
Subject: Re: Enron/Consent to Amendment to Roosevelt Transaction

Last December, Citi arranged and underwrote the Roosevelt transaction for Enron. Roosevelt is a $500MM prepaid forward sale of natural gas and crude oil. In return for the upfront amount, Enron delivers the commodities over a three year period. The commodity delivery schedule is hedged to ensure that the price realized on the ultimate sale of the commodities is sufficient to retire the loan. Enron arranged for five insurance companies to guaranty their delivery obligations. Citi underwrote the entire deal and agreed with Enron to delay syndication until after several other Enron deals (including our Rawhide transaction) cleared the bank market - estimated by 4/30. Altho a syndication approach was agreed, it was understood that Roosevelt would likely never make it to syndication as the intent was to repay it with the proceeds of more "permanent" bank/securitization deals (generally the refinancings must also be commodity-based to ensure that the Enron risk book remains balanced). Roosevelt was securitized - all outstandings reside today in CXC.

On May 3, Enron will prepay $375MM of the Roosevelt transaction, using the proceeds of a $300MM natural gas prepaid (longer tenor and less-restrictive structure than our deal) done with another bank supplemented with available general corporate funds. This will eliminate our underwriting position by paying us down to our approved $125MM hold amount. Enron has agreed to repay the remaining $125MM by 9/30. In return, they have asked for the following amendments:

- amend the syndications agreement to read that syndication will commence on 10/1 if the deal is still outstanding (altho they have agreed to prepay by 9/30, the papers cannot stipulate that as it would require recategorizing the prepaid as simple debt);
- deliveries under the remaining deal will begin post-10/1 if the deal

CITI-SPSI 0046833

Permanent Subcommittee on Investigations
EXHIBIT #163

during the June/September stretch will be rescheduled.

Global Insurance has agreed to extend their approval of the insurance guarantor risk thru 9/10 (the actual insurance company guaranties run thru the final maturity of the deal). The nearly-completed syndication of Rawhide, the currently-underway refinancing of Nighthawk, and these developments on Roosevelt mean:

- Our Enron underwriting overhang will be gone by end-May (we have an underwriting position on Rawhide of roughly $130MM and of $375MM on Roosevelt);
- Our Enron Obligor Exception will be eliminated by 9/30 (the current OE is roughly $608MM).
- Total Facilities to Enron will reduce to approximately $600MM by 9/30(from $1.3B today).

We see significant benefit in these changes to Roosevelt and therefore recommend consent to the amendments. We will circulate a CA tomorrow requesting your formal consent. Given the timing of the prepayment, we will request your signoff by Friday, 4/30. Your consent by CitiMail, again given the time frame, would be appreciated, especially if you are travelling.

Roosevelt

CITIBANK

GLOBAL LOANS SHORT FORM APPROVAL MEMORANDUM

This deal is properly recorded on Syndicator. Verified by _____ (Deal Team Leader initials required).

Memo Date: April 26, 1999 — Approval Due Date: April 29, 1999

[X]	Renewal, Repricing or Restructuring	[X]	League Table Eligible		Yes / No
[ ]	Amendment (Number ____)	[X]	Agent-only	Media Disclosure	[ ] / [X]
[ ]	Multi-Currency (Y or N)	[ ]	Co-Agent	Contact: _____	

A. KEY STATISTICS

Borrower:	A Special Purpose Entity	Citibank Commitment ($MM):	$125 million
GFCID#:	446084	Citibank Hold ($MM):	$125 million
Deal Size ($MM):	$125 million	U/W Amount ($MM):	$125 million
Facilities ($MM)/Tenor:	$125 million/3-year	B/E Amount ($MM):	Not Applicable
Pre-approved (Y/N):	No	Accom. Amount ($MM):	Not Applicable
Date Pre-Approved:	Not Applicable	Scheduled Launch Date:	Not Applicable
Origination Unit:	GEM-Houston	Scheduled Closing Date:	April 30, 1999
GRB Industry:	Integrated Oil & Gas	Sell Down Date(s): (If applicable)	Not Applicable
GRB Market:	US South		
Account Segment:	Priority	Secured (Y/N):	Yes
Syndicated (Y/N):	Yes	Obligor Exception (Y/N): (Exception Amt.):	No
Agent(s)/Amount($MM):	Citibank	Liquidity Exception (Y/N):	No
Co-Agent(s)/Amount($MM):	Not Applicable	Pricing Exception (Y/N):	No Market / No Hurdle

Team Leader: Jim Railly	Tel: 713-654-2820	Back-up Contact: Steve Baillie	Tel: 713-654-2887

PURPOSE:

This memo seeks approval to: (i) delay amortization of Citibank's $125 million hold in the Roosevelt transaction by 5 months, and (ii) reduce Enron's obligor exception by $125 million. This approval is necessary to accommodate a modest change to Roosevelt's refinancing plan as requested by Enron.

ROOSEVELT TRANSACTION BACKGROUND

The Roosevelt transaction was approved in December 1998. As noted previously, the $500 million transaction is a three-year prepaid forward natural gas and crude oil sale transaction funded through CXC, a Citigroup-sponsored securitization vehicle, and backstopped by a $500 million bank commitment pursuant to an Asset Purchase Agreement ("APA"). The mechanics of the Roosevelt transaction require Enron to physically deliver crude oil and natural gas to a Special Purpose Entity ("Delta") at specified delivery points to be sold for index prices swapped to predetermined fixed prices with commodity swap counterparties. Enron is to act as Delta's agent in selling the commodities. In exchange Delta prepays Enron $500MM, which is repaid over 3 years through proceeds realized from the sale of the commodities. Delta in turn has borrowed $500MM from CXC. Both commodity price risk and interest rate risk are eliminated through swaps with highly rated counterparties.

Permanent Subcommittee on Investigations
EXHIBIT #164

CITIBANK

To improve the credit of the transaction, the performance risk associated with the Enron natural gas and crude oil delivery obligations is 100% backstopped by five $100 million dollar surety bonds issued by A rated insurance companies for the full three year tenor of the transaction.

Citibank currently provides the entire $500MM liquidity backstop. The bank commitment is a $500 million 364-day credit facility, with a two-year term out option, backstopping commercial paper issued by CXC. Salomon Smith Barney ("SSB") has underwritten $375.0 million of this "APA" commitment, and Citibank's Global Energy & Mining ("GEM") group holds the remaining $125 million. It was agreed at closing that if the facility was not repaid by April 30, 1999, syndication of the $375MM would then commence May 1999, with the goal to reduce SSB's underwriting position to zero by June 15, 1999.

PROPOSED CHANGES

In April 1999, Enron requested Citibank to change certain aspects of the Roosevelt transaction. Specifically, Enron agreed to repay the entire $375 million underwritten by SSB on May 3, 1999. This will be accomplished by repaying the entire gas tranche of the facility, which represents $310 million, and repaying $65 million of the $190 million oil tranche. As a result, SSB's underwriting role will be eliminated, and the facility size will be reduced to Citibank's original approved $125 million hold amount. The company has verbally agreed to repay the remaining $125 million by September 30, 1999.

In addition, the initial delivery of oil, which was originally scheduled to begin in May 1999, will now begin in October 1999. Hence the amortization of the facility will be deferred by 5 months. The amount of principal which would have been repaid on the $125 million over that 5 month period is $16.3 million.

Citibank's insurance group is extending its approvals of the five surety bond providers from June 30, 1999 to September 30, 1999. Unlike the initial deal where the surety bond approvals expired prior to deal maturity, Enron's agreement to repay the entire obligation by September 30, 1999 for the amended deal coincides with Citibank's new surety bond approvals. In effect, Citibank's exposure in this transaction is now limited to five A-rated insurance companies, issuing surety bonds with a face value of $25 million each. The removal of Enron exposure from this transaction should enable Enron's obligor exception to be reduced by $125 million, or the size of the amended Roosevelt transaction.

Based on the positive aspects of this transaction including the repayment of $375 million and the promise to repay in 5 months time, we recommend approval of the amended Roosevelt transaction.

APPROVALS:

STEVEN M. GILLIS
Vice President
Citicorp North America, Inc.
(713) 654-2587

JAMES F. GILLIS JR.
Managing Director
Citicorp North America, Inc.
(713) 654-2129

THOMAS G. STOTT
Vice Chairman

HOWARD B. BALLARD
Managing Director
Head I Marketing

Approval Level Required: Level 1 CPC CE

W. Fortunato

4/30/99

ROBIN FIELDING
Vice Chairman
399 Park Ave, 2nd Floor
(212) 559-2785

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CITIBANK

Deal Team:

Loan Structuring:	Origination:	Research:	Loan Investor Services:	Credit Admin:
Dave Gorte 713-654-2912	James F. Reilly 713-654-2820 Steve Baillie 713-654-2887	Sumit P. Mathai 713-654-2868 Trevor J. Randolph 713-654-2911		Carol Rooney 713-654-3590

ATTACHMENTS:
CA

Unknown

From: James F. Reilly
Sent: Thursday, April 22, 1999 7:53 AM
Subject: Enron/Roosevelt Update

Distribution:

To: Thomas Stott
To: Steve Baillie
To: Trevor Randolph
To: David B. Gorte
To: Chris Lyons
To: Joseph J. Mackiewicz
To: Jean M. Diaz
To: William Fox

We have agreed the following with Enron:

- On 5/1, Enron will prepay the $310MM natural gas portion;
- The $190MM oil portion will remain outstanding; deliveries scheduled for May/June/July/August/September will be rescheduled to some time after 10/1 - there will, therefore, be no amortization until after 9/30; they have agreed to prepay that amount no later than 9/30;
- The paperwork cannot reflect their agreement to repay the $190MM as it would unfavorably alter the accounting; to compensate for that, we will amend the syndications letter to read that syndication will commence on 10/1; in addition, deliveries will begin in October.

At $190MM, Loan has taken the view that they want the full $310MM prepayment to reduce their underwriting positon and that we must either i) immediately syndicate the remaining $65MM (the remaining underwriting position) or ii) Energy must increase its hold to $190MM (from $125MM). I have spoken with Bill and he is OK with increasing our hold if necessary. Enron, understanding our desire to get to our hold, is considering paying the deal down to $125MM instead of $190MM.

Jean/Steve/Dave: I have spoken with Alan Rafte to get Bracewell working on the docs.

Tom: If we increase our hold, I know that we need approvals. If we are paid down to our originally approved $125MM - what approvals/paperwork do we need to prepare? (the only change will be the lack of several months amortization). In any event, as Global Insurance has agreed to extend their approvals until 9/30 and Enron has committed to prepay by 9/30, can we treat Roosevelt as if it were fully hedged (no reduction in Total Facilities, but a reduction in the Obligor exception).

Permanent Subcommittee on Investigations
EXHIBIT #165

SALOMON SMITH BARNEY

Interoffice Memo

Date of Meeting: *Wednesday, September 8, 1999*

Committee: Investment Grade - New York

Jessica Palmer	*7WTC-32nd*	*Robert Case*	*388-34th*
Carol Healy	*7WTC-32nd*	*Robert Rubin*	*388-39th*
Steve Bowman	*390-4th*	*George Saks*	*388-16th*
Patrick Ryan	*390-5th*	*Myrna Cruz*	*388-34th*
Janice Warne	*390-4th*	*John Binnie*	*388-35th*
Geoff Coley	*390-4th*	*Brad Gans*	*388-32nd*
Marwan Marshi	*390-4th*		
Melissa Motherway	*390-4th*		
James Kelly	*390-8th*		

PLEASE DELIVER MESSENGER

Dick Trask	*Citibank 5th Floor*
559-6665	*399 Park Avenue*
Jolie Eisner	*Citibank 11th Floor*
559-3498	*399 Park Avenue*

DELIVER BY INTEROFFICE MAIL

Control Group Attn: John Benesch	*388-20th*
Tom Doyle	*CitiCorp*
559-5204	*909 Third Avenue*
	NYC 10043

Name of Transaction: Enron – Yosemite
Enron - Condor

Enron

Permanent Subcommittee on Investigations
EXHIBIT #166

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Presentation to:

Enron

CAPITALIZATION

September 20, 1999

SALOMON SMITH BARNEY

Enron Capitalization Table

ENRON CAPITALIZATION (In Millions of $)		
Current Portion of Long Term Debt	$	1,457
Long Term Debt		8,979
Other		1,620
Total Debt	$	12,056
Minority Interests	$	2,475
Company Obligated Preferred		1,001
Junior Voting Preferred		1,000
Shareholders Equity		8,206
Total Capitalization	$	24,738

SCENARIOS	DEBT/CAP RATIO
1. GAAP Debt/Capitalization	49%
2. GAAP Debt with the addition of "Moody's" allocated debt	56%
3. GAAP Debt plus "Moody's" debt plus SSB know "financings"	65%

The following represents the GAAP accounting for Enron's Balance Sheet. Scenarios including additional "debt" follow.

SALOMON SMITH BARNEY
A member of citigroup

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CITI-SPSI 0031095

Moody's Off-Balance Sheet Items

According to Moody's, in December 1998 Enron had "significant off-balance sheet liabilities" including $1.3 billion of guarantees, $1.4 billion in transportation agreements and approximately $4.4 billion in investments in unconsolidated subsidiaries at end of 1998 which "add significant leverage to the balance sheet".

At least one mitigant, however, is the higher credit quality of Florida Gas which is included in Investments in unconsolidated subsidiaries.

OFF-BALANCE SHEET LIABILITIES

(In Millions of $)	
Investments in unconsolidated subsidiaries	$ 4,400
Off-balance sheet guarantees	$ 1,300
Transportation commitments	$ 1,400
Total	$ 5,700

	Debt/Cap
GAAP Debt plus Moody's off-balance sheet liabilities Total Debt/Total Capitalization (1)	56%

The addition of the off-balance sheet liabilities identified by Moody's suggests a slightly higher debt/cap ratio.

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CITI-SBSI 003222

SSB Additional Known Structures

OTHER OFF-BALANCE SHEET ITEMS (In Millions of $)	
Condor	$ 1,500
Oil Prepaids	$ 750
Leases	$ 1,000
Receivable financing	$ 250
Rawhide	$ 750
Marlin	$ 550
Margaeux	$ 500
Firefly	$ 450
Sutton Bridge	$ 250
Total	$ 6,000

GAAP Debt plus "Moody's" Liabilities plus SSB known structures	65%

Mitigants:

- Stock take-outs for certain financings (Marlin, Condor)
- Some double counting between Moody's analysis and the information on this table

With the addition of certain financings identified by SSB that are generally "off-balance sheet," the debt/cap ratio increases accordingly.

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SEC 0031097

Comparable Companies

Company	Debt/Cap	Rating
AES Corp.	78.0 %	Ba1/BB
Sonat Inc.	65.0	Baa2/BBB-
Williams Companies	66.0	Baa2/BBB-
El Paso Energy	60.0	Baa3/BBB-
Coastal Corp	53.0	Baa2/BBB-
Enron	48.7%	Baa2/BBB+

The following is a review of the GAAP debt/cap ratio of certain comparable companies.

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CITI-SPSI 0031098

EXHIBIT NOTE:
CITIGROUP PROVIDED TO THE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS THE FOLLOWING CORRECTED DOCUMENTS: CITI-SPSI0031094 through CITI-SPSI0031098, July 2002)

SALOMON SMITH BARNEY

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Presentation to:

Enron

CAPITALIZATION

September 20, 1999

Enron Capitalization Table

ENRON CAPITALIZATION (in Millions of $)	
Current Portion of Long Term Debt	$ 1,457
Long Term Debt	8,979
Other	1,620
Total Debt	$ 12,056
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Total Capitalization	$ 24,738

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Error: Should read 60%

The following represents the GAAP accounting for Enron's Balance Sheet. Scenarios including additional "debt" follow.

1

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CITI-SPSI 0031095

Moody's Off-Balance Sheet Items

According to Moody's, in December 1998 Enron had "significant off-balance sheet liabilities" including $1.3 billion of guarantees, $1.4 billion in transportation agreements and approximately $4.4 billion in investments in unconsolidated subsidiaries at end of 1998 which "add significant leverage to the balance sheet".

At least one mitigant, however, is the higher credit quality of Florida Gas which is included in investments in unconsolidated subsidiaries.

The addition of the off-balance sheet liabilities identified by Moody's suggests a slightly higher debt/cap ratio.

OFF-BALANCE SHEET LIABILITIES

(In Millions of $)	
Investments in unconsolidated subsidiaries	$ 4,400
Off-balance sheet guarantees	$ 1,300
Transportation commitments	$ 1,400
Total	$ 5,700

Error: Should read 7,100

	Debt/Cap
GAAP Debt plus Moody's off-balance sheet liabilities Total Debt/Total Capitalization (1)	56%

Error: Should read 60%

1

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CITI-SPSI 0031096

SSB Additional Known Structures

OTHER OFF-BALANCE SHEET ITEMS (In Millions of $)		
Condor	$ 1,500	**Double counted**
Oil Prepaids	$ 750	
Leases	$ 1,000	
Receivable financing	$ 250	
Rawhide	$ 750	
Marlin	$ 550	**Double counted**
Margaeux	$ 500	**Double counted**
Firefly	$ 450	**Double counted**
Sutton Bridge	$ 250	
Total	$ 6,000	

GAAP Debt plus "Moody's" Liabilities plus SSB known structures	65%

Mitigants:

- Stock take-outs for certain financings (Marlin, Condor)
- Some double counting between Moody's analysis and the information on this table

With the addition of certain financings identified by SSB that are generally "off-balance sheet," the debt/cap ratio increases accordingly.

SALOMON SMITH BARNEY

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CITI-SPSI 0031097

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Comparable Companies

Company	Debt/Cap	Rating
AES Corp.	76.0 %	Ba1/BB
Sonat Inc.	65.0	Baa2/BBB-
Williams Companies	66.0	Baa2/BBB-
El Paso Energy	60.0	Baa3/BBB-
Coastal Corp	53.0	Baa2/BBB-
Enron	46.7%	Baa2/BBB+

The following is a review of the GAAP debt/cap ratio of certain comparable companies.

SALOMON SMITH BARNEY

Monday, April 16, 2001

High Yield Commitment Committee

Attending: Jessica Palmer, Dick Trask

Chair: Jessica Palmer

Issue: Enron - $1 Billion –Credit Linked Note

Salomon Role: Others:
Books

Presenting: Bankers: D. Keller Research: J. Melesius Capital Markets: R. Kaplan, A. Angelini

Issues Discussed:

- Structure-on face of it is closed loop where note proceeds used to buy AA "Investment" Enron puts in unsecured paper only in case of credit event. But no proceeds to Enron.
- However, key is that "investments" will be a Citi CD, proceeds of which we turn around and "lend" to Enron as prepaid oil swap contract. If credit event happens swap and CD unwind and Enron puts unsec. note into trust.
- Exposure to PG&E-potentially $500 area very complex due to regulatory system in Cal, potentially really a windfall for Enron
- Dhabol (own 65%) will take long time to sort. Don't currently consolidate due to LOI to sell below 50%. Risk accountants will make them put $1.7 billion debt on balance sheet.
- Retained Milbank to dig down on due diligence. Particularly focussed on details of all structured deals, triggers, liquidity.
- Diversification into other industries for their B2B exchange, paper, metals (made small acquisitions) steel?
- Portland General Sale – unlikely to happen

Defer

Due diligence re: earnings
Recent California/Dhabol developments

Permanent Subcommittee on Investigations
EXHIBIT #167

CITI-SPSI 0008735

SALOMON SMITH BARNEY

Interoffice Memo

Date of Meeting: Monday, April 16, 2001

Committee: Investment Grade - New York

DELIVER BY HAND

Jessica Palmer	388-24th	James Kelly	390-8th
Krys Gaboff	388-24th	Janice Warne	390-4th
Richard TB Trask	388-24th	Geoff Coley	390-4th
Robert Rubin	388-39th	Melissa Motherway	390-4th
John Binnie	388-35th	Marwan Marshi	390-4th
Scott Van Bergh	388-34th	c/o Nancy Davis	Large Trading Floor
Jolie Eisner	388-20th	Richard Stuckey	390-4th
Robert Case	388-18th	Patrick Ryan	390-1st
George Saks	388-16th	Steven Ekert	390-1st
Marcy Engel	250W-10th		
Chris Teano	250W-10th		

DELIVER BY INTEROFFICE MAIL

Control Group c/o John Benesch 7 WTC – 32nd Floor

Rona Pocker Citigroup
Audit Risk & Credit Review - CF
111 Wall Street/Floor 7
New York, NY 10016

Name of Transaction: **Enron Corp.**

Enron

Permanent Subcommittee on Investigations
EXHIBIT #168

CITI-SPSI 0008736

SALOMON SMITH BARNEY

Investment Banking Commitment Committee Memorandum

CLIENT:	Enron Corp. ("Enron")
ISSUERS:	Enron Credit Linked Notes Trust II ("ECLN II") Enron Euro Credit Linked Notes Trust Enron Sterling Credit Linked Notes Trust
TRANSACTION:	Up to $1.0 billion Enron credit linked notes due ___ (Approx $700-800 US dollar equivalent in Euro and Sterling, the remainder in USD)
COMMITTEE:	Investment Grade

TRANSACTION TEAM:

Investment Banking		Fixed Income Derivatives	
Maureen Hendricks	(212) 816-0967	Steve Wagman	(212) 723-6449
Jim Reilly	(713) 694-2912	Credit Derivatives	
Dean Keller	(212) 816-0994	Rick Caplan	(212) 723-6453
Damien Mitchell	(212) 816-0879	Amanda Angelini	(212) 723-6484
Amy Richards	(212) 816-5671	Tim LeRoux	(212) 723-6436
Sebastian Arango	(212) 816-7309	Steve Incontro	(212) 723-6012
Fixed Income Research		Doug Warren	(212) 723-6118
John Melesius	(212) 816-8657	Fixed Income Capital Markets	
Deborah Grosser	(212) 723-6201	Steve Becton	(212) 723-6093
Brian Schmidt	(212) 816-2699	Dan Botoff	(212) 723-6138
		Jerry Lee	(212) 723-6103

TRANSACTION OVERVIEW – DEBT	
Transaction:	Enron Credit Linked Note Trust Senior Notes Offering (3 separate transactions marketed as one, USD, Euro, and Sterling)
Transaction Size:	Up to a $1 billion (and approx $100 million of Certificates)
Debt Ranking:	Senior Unsecured
Maturity:	5 to 10 years
Underwriting Format:	Rule 144A/Reg S without Registration Rights
Managers:	**Salomon Smith Barney (Sole Books)** Jt. Lead UBS
Co-Managers:	Credit Lyonnais, Royal Bank of Scotland
Anticipated Ratings:	Baa1 / BBB+ (Moody's / S&P)
Enron Market Capitalization:	Approx. $42 billion
Roadshow Launch:	April 23
Offering Date:	April 27
Latest Financials in Off. Circular:	December 31, 2000
Latest Audit in Off. Circular:	December 31, 2000 10-K

(Transaction Overview continued on following page)

Use of Proceeds:	To purchase "Trust Investments" **USD** Trust Investments may include: time deposits or promissory notes of North America money center banks rated AA-/Aa3 with a short term rating of A1/P1, obligations for borrowed money, GICs from insurance companies rated Aaa by Moody's and AAA/ by S&P (less than one year), and AAA US Government securities. **EURO** Trust Investments may include: Euro- denominated time deposits or promissory notes or CP of U.S. money center banks rated AA-/Aa3 with a short term rating of A1/P1, promissory notes or GICs from insurance companies rated Aaa by Moody's and AAA by S&P (less than one year), and AAA Government securities issued by an EU Member State. **Sterling** Trust Investments my include: pounds sterling-denominated time deposits or promissory notes or CP of U.S. money center banks or [E-11] commercial banks rated AA-/Aa3 with a short term rating of A1/P1, promissory notes or GICs from insurance companies rated Aaa by Moody's and AAA by S&P (less than one year), and debt securities of the United Kingdom known as Gilts.
Issuer's Counsel:	Vinson & Elkins L.L.P.
Underwriters' Counsel:	Milbank, Tweed, Hadley & McCloy LLP
Company Auditors:	Arthur Anderson LLP

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CITI-SPSI 0008738

Portland General. Enron entered into an agreement with Sierra Pacific on November 8, 1999 to sell its wholly owed subsidiary, Portland General, to Sierra Pacific for $2.1 billion in equity and the assumption of approximately $1.0 billion in debt. In connection with the recent utility developments in California, this sale process has been complicated due to regulatory developments in both California and Nevada. Sierra Pacific intended to fund part of the purchase of Portland General through the sale of certain generation assets (which are currently under contract to sell). However, because Sierra owns a small service territory in California, it is effected by a newly enacted California law restricting the sale of generation assets until 2006. Similarly, Nevada, in reaction to the developing situation in California, has considered placing restrictions on the ability of Sierra to sell generation assets. There is a drop-dead date under the merger agreement between Portland General and Sierra Pacific of May 5, 2001. In a conference call with analysts and investors on March 23, 2001, Jeff Skilling, CEO of Enron, expressed a belief that the merger had only a 5% chance of being consummated. There is no financing out, but it should be noted that Citibank is the lead arranger on an approximately $2.2 billion un-syndicated acquisition financing facility for Sierra and SSB, i.e. Sierra's financial advisor. Financing conditions include the maintenance of investment grade ratings and that no material adverse change exists in the syndicated loan market. Finally, it should be noted that any change in the financing plan relating to the acquisition would require further filing with the SEC for approval, which could further delay the process. The Company is considering financing alternatives to try to affect the de-consolidation of this business.

International Assets. Internationally, the Company has been pursuing and continues to pursue the sale of certain assets in Latin America and Asia. SSB is currently advising Joe Sutton, the ex vice chairman of Enron, on raising private equity which would be used to acquire certain of these assets.

India – Dabhol. Enron has a 65% stake in the Dabhol Power Company. The approximately US $2.9 billion combined-cycle facility, located south of Mumbai, is being constructed in two phases. The 740-megawatt Phase I began commercial operation in May 1999. Phase II is scheduled to come on-line fourth quarter 2001: Phase II of the operation includes the construction of a liquefied natural gas (LNG) terminal, expected to be completed in mid-2002, which will be the world's largest. LNG is a relatively new technology in energy, and according to Enron, is the cleanest and most economical fuel choice. Enron, as majority owner of the Dabhol project, operates the plant and serves as fuel manager.

Prices for electricity at Dabhol have more than doubled in the past two years due to rising world fuel prices and a depreciating Rupee. As a result, the Maharashtra State Electricity Board (MSEB) has been unable to make its payments. The defaults have caused Enron to invoke a payment guarantee by India's federal government. The NY Times reported that the project could be owed as much as a $1 billion dollars by next year if no payments are made. The Indian Government stated it will honor its commitments.

SUMMARY OF ENRON CREDIT

A review of the Enron credit profile focuses on cash flow, capital structure and risk management. Enron's cash flow has been steadily increasing, with 2000 FFO of $3,010 million, rising from $2,228 million in 1999, and $1,873 million in 1998 (a compound annual growth rate of 27%). The Company has a healthy funds flow interest coverage of 4.1x, up from 3.7x in 1999 and 3.5x in 1998. This compares favorably to Enron's peer group of energy merchants and generators (see pg. 15) who have reported an average of 3.9 times funds flow interest coverage. It also is in line with Enron's Integrated Energy peer group which has reported an average FFO coverage ratio of 3.7 times. We have also performed an overall review of Enron's capital structure. Using our most conservative approach, adjusting Enron's total obligations to include significant off-balance-sheet financing, we find Enron's adjusted debt/capital [1] ratio to be approximately 62.6% (see pg 20 for analysis).

[1] Includes as debt a conservative estimate of off-balance sheet financing, including structured products, contingent equity transactions, a present value estimate of operating lease commitments, prepaid contract and receivable financing. Total capital includes total debt, preferred securities, minority interest, and shareholders equity.

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CITI-SPSI 0008741

Salomon Smith Barney has been mandated to act as lead-manager and sole book runner of an expected $1.0 billion Notes offering (the "Offering"). Due to the accelerated timing the Company has requested, this transaction will include three separate bond deals, one for each currency. This should not be an issue for investors as the offerings will be done simultaneously and will be marketed as one. In the remainder of this document we will refer to the combined offerings as the ECLN II transaction.

This transaction is very similar to the Enron Credit Linked Notes ("ECLN I") screened by the Committee on August 14, 2000. The Trust Investments purchased by the Trust as collateral for the Notes will be AAA governments, AAA insurance companies (less than one year) and AA-/Aa3 North America money center banks with a short term rating of A1/P1. (There are slight differences in Euro and Sterling Trust Investments as described in the Transaction Overview section at the beginning of this document, and further in the "Detailed Discussion of Structural Mechanics" section). Unlike the original Yosemite transactions the Trust will not hold Enron assets.

The ECLN II Notes are structured such that payments from sources of funds available to the Trust are expected to be sufficient to pay the amount that would have been paid on the Notes if the Notes were senior unsecured obligations of Enron having the same principal amount.

The Notes will represent debt obligations of the Trust secured by the assets of the Trust. The Trust will also issue approximately $100 million of Certificates that will represent interests in the assets of the Trust subordinate in right of payment to the Notes, with payments on the Certificates to be made only after the payment in full of any amounts then due and payable under the Notes.

In the absence of an Enron Credit Event, Citibank will pay to the Trust an amount sufficient to pay interest on the Notes and yield on the Certificates (Citibank Fixed Payment). Hence, the investors look to Citibank for the interest component of the investment throughout the life of the transaction unless an Enron Credit Event occurs. The Trust will pay to Citibank the actual interest payments received on the Trust Investments (Trust Payments) and will use the principal received on the Trust Investments to repay the principal amount of the Notes and the Certificates on the Maturity Date. If an Enron Credit Event occurs, the Credit Swap will permit Citibank to physically settle all or a portion of the Credit Swap by delivering senior unsecured obligations of Enron (Enron Deliverable Obligations) in exchange for a like principal amount of the Trust Investments. The Citibank Fixed Payment will be reduced if a Failure to Pay has occurred, and cease if an Enron Bankruptcy has occurred.

Rationale for the Transaction

The primary purpose of this transaction is to permit Enron to refinance certain borrowings, with proceeds from the Offering, while allowing Enron to maintain the advantageous accounting and rating agency treatment of these financings. The Trust Investments contributed to the trust structure will in part serve as the collateral for the Notes.

In addition, Enron is looking to take advantage of the opportunity available in using bank debt to finance structured products and the bond market to find longer-term borrowings. Through this offering Enron is essentially taking bank debt which was used most efficiently to fund structured financing and converting that liability into public debt which provides a more efficient source for funding long-term liabilities.

Yosemite I & II and ECLN I Transactions

SSB was also sole lead manager of the $750 million Yosemite I offering on November 4, 1999 and sole book running manager of the £200 million Yosemite II structured finance bond offering on February 15, 2000.

SSB was the book-running leading manager on the $500 million ECLN I bond offering on August 17, 2000.

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CAPITAL STRUCTURE PRESENTATION

To attain a better understanding of Enron's capital structure we have examined it in the following ways:

GAAP. This includes as debt only those liabilities defined as debt under Generally Accepted Accounting Principles. This is the least conservative scenario, but also a relatively standard analysis.

Enron Analysis. This analysis adds 100% of Enron's unconsolidated sub debt. Also, it adds the equity invested by its partners to its total capitalization.

SSB Base Case. This case adds certain significant "off-balance-sheet" financing to the total debt number, excluding contingent equity secured transactions.

SSB Alternative. This is the most conservative scenario, also including contingent equity secured transactions as debt. All of the off-balance-sheet financing included in both SSB cases is detailed on the following page.

($ in millions)	GAAP	Enron Analysis	SSB Base Case Analysis	SSB Alternative Analysis
GAAP Items				
Current Portion	$1,679	$1,679	$1,679	$1,679
Long Term Debt	8,550	8,550	8,550	8,550
Minority Interest	2,414	2,414	2,414	2,414
Minority Interest adjustment [1]			(750)	(750)
Company Obligated Preferred	904	904	904	904
Shareholders' Equity	11,470	11,470	11,470	11,470
ENE Analysis Items				
Unconsolidated Subsidiary Debt (100% of Project Debt)		9,717		
Unconsolidated Subsidiary Partner Equity [2]		8,257		
SSB Analysis Items				
Off Balance Sheet Financings			5,880	
Minority Interest Reclassification as Debt [1]				
All off balance sheet financings [3]				9,430
Total "Debt"	$10,229	$19,946	$16,109	$19,659
Total Capitalization	$25,017	$42,991	$30,147	$33,697
Debt/Cap with Obligated Preferred as Equity	40.9%	46.4%	53.4%	58.3%
Debt/Cap Excluding Obligated Preferred	42.4%	47.4%	55.1%	59.9%
Debt/Cap with Obligated Preferred as Debt	44.5%	48.5%	56.4%	61.0%
Allocable share of Unconsolidated Project Debt [4]			3,796	3,796
(Total Debt + Allocable share of Unconsol. Proj. Debt.)/Cap. [5]			58.6%	62.6%

[1] Adjustment represents the Rawhide transaction which is reflected on the balance sheet in minority interest and included in off balance sheet financings.
[2] Unconsolidated subsidiary partner equity equals total equity in Enron unconsolidated subsidiaries less Enron investment in those subsidiaries.
[3] See detail following page, significant "other financings"
[4] Allocable share of Unconsolidated Project Debt represents an estimate of Enron's share of total unconsolidated affiliate debt. We have estimated this as Enron's overall share of unconsolidated affiliated equity (total investment / total affiliate equity) applied to the total debt of the affiliates.
[5] Obligated Preferred treated as Equity

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Significant "Other Financings" of Enron

($'s in Millions)

Transaction	Amount
Off Balance Sheet financings	
ECLN I	$500
Rawhide	750
Yosemite II	700
Yosemite I	280
Oil Prepaids [1]	750
Leases [2]	1,000
Receivable Financing	250
Merlin	500
Margaux	150
Miscellaneous [3]	1,000
Subtotal	$5,880
Contingent Equity Transactions	
Osprey I and II	2,400
Firefly	450
Marlin	700
Subtotal	$3,550
Total	$9,430

[1] Oil Prepaids are classified as a "financing" because they represent a contract which has been prepaid to Enron. Amount represents an estimate and does not include prepaids relating to Yosemite I, Yosemite II, or the ELCN I transactions.

[2] Leases represent operating leases that Enron has entered which are essentially off-balance-sheet financing. The amount represented here is an estimate of the debt outstanding.

[3] Represents possible other financings that may exist of which we are not aware.

Integrated Energy Peer Group - Selected Financial Statistics 12/31/00

Enron compares favorably with its integrated pipeline peer group companies on most financial benchmarks. Enron is the largest of its peers as measured by assets, revenues, and market capitalization. Enron is also the least leveraged of its peers when calculated by Debt to Capital and Debt to FFO. Enron's cash flow coverage is also among the strongest in the group but its earnings coverages, EBIT / Interest of 2.30x and EBITDA / Interest of 3.40x are slightly weaker than the peer group averages of 2.88x and 4.38x respectively. The weaker earnings coverage ratios can be explained, in part, by Enron's relatively modest use of short-term debt financing. At 12/31/00, only 16% of Enron's debt was short-term. Although a greater use of short-term debt can lower interest expense and improve coverage measures, it also increases refinancing and interest rate risk.

Company	Moody's	S&P	Assets	Market Cap[1]	ROE	EBIT[2] / Int	EBITDA[2] / Int	FFO Cov[3]	Debt / FFO	Debt/ Cap[4]	Net Debt / Net Cap[5]
Enron Corp.	Baa1/Stable	BBB+/Stable	52,996	44,134	9.1 %	2.30 x	3.40 x	4.10 x	3.61 x	40.9 %	41.7 %
El Paso Energy	Baa2/Stable	BBB/Stable	45,994	32,228	NA %	3.00 x	4.30 x	4.10 x	5.01 x	60.7 %	59.4 %
Dynegy Inc.	Baa2/Stable	BBB+/Stable	21,406	16,985	16.9 %	3.00 x	4.50 x	2.60 x	7.21 x	42.7 %	42.0 %
Williams	Baa2/Stable	BBB-/Positive	32,228	18,947	11.3 %	3.50 x	5.60 x	4.50 x	9.88 x	66.0 %	62.4 %
Average			*38,156*	*26,776*	*8.2 %*	*2.88 x*	*4.38 x*	*3.35 x*	*6.43 x*	*55.6 %*	*53.9 %*

(1) Market capitalization as of April 11, 2001, (2) Includes earnings from unconsolidated equity affiliates, (3) (FFO + Cash Interest) / Cash Interest, (4) Total Debt / (Total Debt + Equity), (5) (Total Debt + Preferred Securities) / (Total Debt + Preferred Securities + Minority Interest + Equity)

Source: Company financial statements and Salomon Smith Barney

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CITI-SPSI 0008757

Friday, November 19, 1999

Investment Grade Commitment Committee - Europe

Attending: B. Case, G. Saks, J. Kaplan, C. Teano, P. Mason

Chair: Bob Case

Issue: Enron-Project Yosemite II - £175MM Linked Enron Obligations (LEOs) – Final Commitment

Salomon Role:	Others:
Lead	Barclays, RBS

Presenting: D. Keller, D. Grosser (Res.), A. Angelini, P. Deards, A. Kulick, J. Riley (Citi), P. Charles (CMS), S. Becton (CMS)

Issues Discussed:

- Closed Yosemite-I yesterday.
- This is almost identical transaction except denominated in Sterling and sold to UK investors.
- Recent developments:
  - -Announced sale of Portland General.
  - -Rating agencies reacted positively. Did not hurt the Yosemite-I deal.
- London CMS views on marketability of Sterling-denominated structured obligations:
  - -Have started pre marketing with UK investors.
  - -Buyer base is thin now-25-30 accounts max.
  - -Expect a quick read-by next week.
  - -5-6 investors could drive transaction. Prudential UK could emerge as the lead buyer.
  - -We have reflected to Enron the possibility that this is not a "slam dunk", and might not be marketable in the UK at this time.
  - -Will continue premarketing rest of this week.
  - -If premarketing is positive, launch week of Dec. 7 & price around Dec. 14.
  - -Minimum deal size is £100MM. Less than that is uneconomic.
  - -This is in effect a best efforts transaction. We do not plan to go long this security in any meaningful amount.
  - -Experience from Yosemite I:
    - -Lost a few investors over some structure issues.
    - -Lack of disclosure about underlying assets was the major point.
    - -Complexity of structure.
- Discussed CMAC approval process
  - -Written document being circulated this afternoon to CMAC to confirm approval for initial asset (prepaid oil swap) and future substitutions.

APPROVED

Permanent Subcommittee on Investigations
EXHIBIT #169

SALOMON SMITH BARNEY

Interoffice Memo

Date of Meeting: Friday, November 19, 1999

Committee: Investment Grade - European

Jessica Palmer	388-24th	Janice Warne	390-4th
[redacted]		Geoff Coley	390-4th
Robert Case	388-24th	Melissa Motherway	390-4th
Myrna Cruz	388-24th	James Kelly	390-8th
Brad Gans	388-34th	Phil Bennett	London
Michael Klein	388-33rd	Edward Miller	London
Robert Rubin	388-39th	Tim Horlick	London
John Birnie	388-35th	Jeannette Gelbhardt	London
George Saks	388-16th	Kamran Hashemi	London
Steve Bowman	390-4th	Peter Maskrey	London
Patrick Ryan	390-1st	Samantha Long	London
Marwan Marshi c/o Nancy Davis	390-4th Large Trading Floor	Laurie Adams Citibank 3rd Floor	Hudson House 2010 Tavistock St. London WC2E 7 PP

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Dick Trask (559-6665) Citibank 5th Floor Zone 20	399 Park Avenue New York, NY 10022	Jolie Eisner (559-3498) Citibank 11th Floor Zone 5	399 Park Avenue New York, NY 10022
Chris Teano (559-2502 Citibank 11th Floor Zone 14	399 Park Avenue New York, NY 10022		

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Control Group Attn: John Benesch Tom Doyle 212-559-5204 Audit & Risk Review - CF	388-20th Citigroup 909 Third Avenue NYC 10043

Name of Transaction: Yosemite II

Yosemite-III

INDEX

INDEX 1
SECTION I – YOSEMITE II TRANSACTION 2
YOSEMITE II TRANSACTION 4
RATING AGENCY REVIEW 4
ECONOMICS OF PROPOSED OFFERING 5
SYNDICATION STRATEGY 5
TRANSACTION STRUCTURE 5
SECTION II – ENRON CORP. UPDATE 6
RECENT DEVELOPMENTS 7
ENRON CORP – CAPITAL STRUCTURE DISCUSSION 8
REVIEW OF FINANCIAL AND STOCK MARKET PERFORMANCE 10
ENRON CORP. HISTORICAL FINANCIAL INFORMATION 11
ENRON CORP. HISTORICAL SEGMENT DATA 11
SECTION III – LIST OF EXHIBITS 12
LIST OF EXHIBITS 13

A. Yosemite I Screening Memorandum
B. Yosemite I Roadshow Slides
C. Yosemite I Final Offering Memorandum
D. Yosemite II Draft Offering Memorandum (marked to show changes from Yosemite I)
E. List of Yosemite I Investors
F. Enron "Kitchen Sink" Analysis
G. Enron 10-Q, 9/30/99
H. Enron 10-K, 12/31/98
I. Rating Agency Releases on November 8

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SECTION I – YOSEMITE II TRANSACTION

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Investment Banking Commitment Committee Memorandum

CLIENT:	Enron Corp. ("Enron") Project Yosemite II
TRANSACTION:	£175 million Senior Notes
COMMITTEE:	Investment Grade

TRANSACTION TEAM:

Investment Banking		Fixed Income Derivatives	
Maureen Hendricks	(212) 816-0967	Lynn Feintech	(415) 627-6165
Dean Keller	(212) 816-0994		(212) 723-6445
Amanda Angelini	(212) 816-0997	Paul Deards	(212) 723-6335
Kim Champlin	(212) 816-0877	Adam Kulick	(212) 723-6449
		Rick Caplan	(212) 723-6453
Structured Finance			
Janice Warne	(212) 723-6152	Fixed Income Capital Markets	
Brooke Schooley	(212) 723-6222	Anne Clarke Wolff	(212) 723-6089
Roland DaCosta	(212) 723-6227	Steven Becton	(212) 723-6093
James Mitchell	(212) 723-6235	Storm Nickerson	(212) 723-6097
Fixed Income Research		London	
John Melesius	(212) 816-8657	Peter Charles	44-171-721-3625
Debbie Grosser	(212) 723-6201	Pippa Mason	44-171-721-3610
		Myles McBride	44-171-721-4323
		Daisuke Takekawa	44-171-721-6469

TRANSACTION OVERVIEW – DEBT	
Transaction:	Linked Enron Obligations (LEOs) Senior Notes Offering
Transaction Size:	£196 million (£175 million of Notes, £21 million of Certificates)
Debt Ranking:	Senior Unsecured
Maturity:	20 years (shorter tranche possible)
Underwriting Format:	Reg S / Registered on Luxembourg Exchange (possible Rule 144A)
Managers:	**Salomon Smith Barney (Lead, Books)** Possible Co-Manager(s)
Anticipated Ratings:	Moody's: Baa2 Standard & Poor's: BBB+
Enron Market Capitalization:	$30.146 billion
Mail Preliminary Offering Circular:	Wednesday, November 24, 1999
Roadshow Launch:	November 22-23, 1999
Offering Date:	Week of November 28, 1999
Latest Financials in Off. Circular:	September 30, 1999 10-Q (unaudited)
Latest Audit in Off. Circular:	December 31, 1998 10-K
Use of Proceeds:	• To purchase "Enron Investments" (Enron structured debt supported in whole or in part, directly or indirectly by Enron) to free up bank capacity • To purchase "AAA Investments" (debt securities rated Aaa/P-1 by Moody's and AAA/A-1+ by S&P and direct registered obligations of the USA) and "Eligible Investments"
Issuer's Counsel:	Vinson & Elkins L.L.P.
Underwriters' Counsel:	Milbank, Tweed, Hadley & McCloy LLP
Company Auditors:	Arthur Anderson LLP

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CITI-SPSI 0005179

ENRON CORP – CAPITAL STRUCTURE DISCUSSION

The following is a discussion of four different analyses of the Company's capital structure.

1. GAAP Debt/Capitalization
2. Enron's Analysis for Rating Agencies
3. Citibank/SSB Analysis including certain off-balance sheet obligations
4. Moody's analysis with certain "allocated" debt

Enron, Citibank/SSB and Moody's have each approached this analysis in different ways. In particular, Enron has responded to Moody's concerns about off balance sheet financing with an analysis of the effect of including certain unconsolidated financings and related equity on the capital structure. This Enron-provided analysis is attached as Appendix F. In part, as a result of this openness, Moody's recently changed its outlook on Enron from "stable" to "positive" (Baa2).

The following analysis attempts to summarize these approaches under a common set of capital structure assumptions. Consequently, The results differ slightly from the exact numbers arrived at by Enron.

Capitalization Analysis

($ in millions)	GAAP	Enron Analysis	SSB Analysis	Moody's 1999 Analysis
GAAP Items				
Long Term Debt	8,592	8,592	8,592	8,592
"Other" Liabilities	1,718	1,718	1,718	1,718
Minority Interest	1,822	1,822	1,822	1,822
Minority Interest adjustment			(1,165)	
Company Obligated Preferred	1,001	1,001	1,001	1,001
Junior Voting Preferred	1,000	1,000	1,000	1,000
Shareholders' Equity	8,345	8,345	8,345	8,345
ENE Analysis Items				
Unconsolidated Subsidiary Debt (100% of Project Debt)		7,415		
Unconsolidated Subsidiary Partner Equity		4,275		
SSB Analysis Items				
Off Balance Sheet Financings			1,350	
Guarantees			755	
Minority Interest Reclassification as Debt			1,165	
Moody's Analysis Items				
Investments in Projects/Unconsolidated Subsidiaries				4,779
Off Balance Sheet Guarantees				1,300
Transportation Commitments				1,400
Total "Debt"	10,310	17,725	14,180	17,788
Total Capitalization	$ 22,478	$ 34,168	$ 25,183	$ 29,957
Debt/Cap with Obligated Preferred as Equity	45.9%	51.9%	56.3%	59.4%
Debt/Cap Excluding Obligated Preferred	48.0%	53.4%	58.8%	61.4%
Debt+Cap with Company Preferred as Debt	50.3%	54.8%	60.3%	62.7%

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ENRON'S ANALYSIS OF OFF-BALANCE SHEET LIABILITIES FOR RATING AGENCIES

The Enron analysis takes into consideration the inclusion onto the balance sheet of approximately $7,415 million of non-recourse indebtedness/guarantees incurred at unconsolidated subsidiaries. This represents 100% of the project debt associated with those projects even though Enron owns 50% or less of the equity interests in these projects. Accordingly, for the purposes of this analysis, Enron also includes in capitalization the book equity of its partners in these projects ($4,275 million).

CITIBANK/SSB ANALYSIS INCLUDING CERTAIN OFF BALANCE SHEET OBLIGATIONS

With the addition of certain transactions entered into by Enron which create non-debt obligations for GAAP reporting purposes, the debt/cap ration increases. The types of transactions include the following:

- *Off Balance Sheet Financing*: Consists of approximately $1.95 billion prepaid oil and gas, leases, and receivables securitizations. The Company has an estimated $1.0 billion of prepaids, which are used to monetize profits embedded in the company's trading book. Enron also has approximately $700 million of operating (synthetic) leases. The Company also has available a receivables securitization program of up to $250 million, which is largely unutilized. Enron also is involved in a number of transactions via supply and offtake agreements.

- *Guarantees of Unconsolidated Subsidiaries*: Enron provides guarantees totaling $755 million to support trading, trade and certain debt of unconsolidated subsidiaries. Of these guarantees 43% are backed with crude oil as collateral; 37% are related to power projects, half of which involve flexible tariff structures.

- *Structured Financings*: Enron actively employs structured finance transactions. These include $2.95 billion that are classified as either, minority interest ($1.2 billion), common equity ($1.0 billion), or Linked Enron Obligations ($750 million). These transactions should not be regarded as debt, since Enron's contractual obligation is limited to either equity $1.415 billion) or the liquidation of a stipulated pool of non-core assets ($750 million).

Examples of Structured Financings
(In Millions of $)

Condor	$ 1,500
Rawhide	750
Marlin	550
Firefly	450
Sutton Bridge	250
Total	$ 3,500

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MOODY'S ANALYSIS

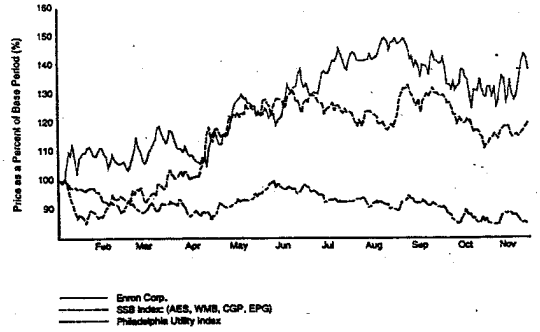
According to Moody's, in December 1998 Enron had "significant off-balance sheet liabilities" including $1.3 billion of guarantees, $1.4 billion in transportation agreements and approximately $4.4 billion in investments in unconsolidated subsidiaries at the end of 1998 which "add significant leverage to the balance sheet". Moody's adds that "most of Enron's $4.4 billion investments in unconsolidated subsidiaries is already fully leveraged. While the debt is non-recourse to Enron, cash flows of the unconsolidated subsidiaries are subject to the prior debt claim. Some of these assets are strategic to certain Enron sheet assets, making it unlikely that Enron would not support the dent in a stressed situation.

COMPARABLE COMPANIES

	GAAP Debt/Cap	Rating
AES	78.0 %	Ba1/BB
Williams Companies	66.0	Baa2/BBB-
El Paso Energy	60.0	Baa2/BBB
Coastal Corp	53.0	Baa2/BBB

REVIEW OF FINANCIAL AND STOCK MARKET PERFORMANCE

DAILY DATA: JAN/01/1999 THROUGH NOV/16/1999



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CITI-SPSI 0005186

Monday, October 25, 1999

Investment Grade Commitment Committee - New York

Attending: B. Case, G. Saks, R. Rubin, R. Trask, J. Palmer, B. Gans, J. Warne, M. Marshi, T. Boland, E. Wagner, L. Feintech

Chair: Jessica Palmer

Issue: Enron Project Yosemite - $725MM Linked Enron Obligations (LEOs)

Salomon Role: Lead

Others:

Presenting: M. Hendricks, D. Keller, Derivatives: A. Kulick, Res.: D. Grosser, CMS: J. Purcell

Issues Discussed:

- Ratings Baa2 } estimated BBB+}
- Condor was too large for comfortable absorption.
- This 144(a)-no reg rights.
- $725MM LEOs.
- $75MM in equity 1st loss on AAA risk. Enron taking 50% Citibank taking "synthetically"-will borrow balance sheet from Hypobank with total return swap. Annual renewal, can replace Hypo-regularly borrow balance sheet.
- Initial assets will be $800 pre paid oil derivative plus an Enron Adjustable Rate Notes to cover negative carry.
- Noteholders will have securities designed to look like Enron sr. secured obligation.
- If Enron fails to pay/bankrupt, Citi can settle by delivering obligations.
- If at end recovery of sr. unsecured is 50¢ and trust settles at 40¢, Citi will be obligated to make up the 10¢.
- If excess cash in trust after all settles then goes to Citi.
- If permitted investment (AAA securities) payment event certificate holders take the loss (after "equity").
- Will price cheap to public Enron sr. unsecured.
- CMAC issues-resolved. Final resolution is in memo being circulated to Bushnell, Engel and other CMAC members.
- Wagner OK, Boland OK.
- Rating agencies-off balance sheet debt/assets leverage.

APPROVED

Permanent Subcommittee on Investigations
EXHIBIT #170

CITI-SPSI 0003047

SALOMON SMITH BARNEY

Interoffice Memo

Date of Meeting: **Monday, October 25, 1999**

Committee: **Investment Grade - New York**

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~~Jessica Palmer~~	~~7WTC-32nd~~	Robert Case	388-34th
Carol Healy	7WTC-32nd	Robert Rubin	388-39th
Steve Bowman	390-4th	George Saks	388-16th
Patrick Ryan	390-1st	Myrna Cruz	388-34th
Janice Warne	390-4th	John Binnie	388-35th
Geoff Coley	390-4th	Brad Gans	388-34th
Marwan Marshi	390-4th		
Melissa Motherway	390-4th	Eleanor Wagner	390-8th
James Kelly	390-8th		

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Dick Trask (559-8685) Citibank 5th Floor Zone 20	399 Park Avenue New York, NY 10022	Jolie Eisner (559-3498) Citibank 11th Floor Zone 5	399 Park Avenue New York, NY 10022
Chris Teano (559-2502 Citibank 11th Floor Zone 14	399 Park Avenue New York, NY 10022		

DELIVER BY INTEROFFICE MAIL

Control Group Attn: John Benesch	388-20th
Tom Doyle 559-5204	CitiCorp 909 Third Avenue NYC 10043

Name of Transaction: **Enron Corp – "Project Yosemite" TIERS-Credit Linked Securities Trust**

TIERS1

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ENRON CORP - Yosemite
CREDIT PROFILE

Executive Summary

- Enron is one of the largest integrated natural gas and electricity companies in the world, with over $29 billion in assets and $31 billion in revenue for 1998. Enron is rated BBB+/ Baa2 by S&P and Moody's. The company had market capitalization of $27 billion at October 21, 1999.
- Enron has consistently grown earnings and cash flow. The pipeline/electric utility businesses are "hard assets" that provide a stable earnings base, while the trading business and merchant activities investments have become increasingly important. These businesses are also shown to be significant cash generators. Near term growth will come from merchant activities, electricity sales, water ("Azurix), telecommunications, and retail.
- An analysis of book debt, including minority interest, off balance sheet obligations, and guarantees as debt, shows that Enron maintains an acceptable credit profile under the most conservative assumption.

Consolidated Earnings Analysis

- Trend of strong growth of revenue and cash flow. Recent growth is driven by (1) electricity sales, and (2) "Other" revenues, which includes price risk management activities and merchant activities (see "Wholesale" below).

($MM)	Q2/99 – LTM	1998	1997	1996	1995
Natural Gas	NA	$13,276	$13,211	$11,157	$7,529
Electricity	*NA*	*13,939*	*5,101*	*980*	*179*
Transportation	NA	627	652	707	692
Other	*NA*	*3,418*	*1,309*	*445*	*789*
Total Revenues	36,325	31,260	20,273	13,289	9,189
EBITDA	2,337	2,249	1,327	1,142	851
Net Income	$688	$703	$105	$584	$520

Segment Analysis

($MM)	Q2/99 – LTM	1998	1997	1996	1995
Transportation	812	515	558	403	361
Exploration & Prod.	434	448	463	456	456
Retail Energy Services	(71)	(88)	(100)	-	-
Corporate & Other	(87)	(1)	(103)	(142)	(389)
Wholesale Energy	1,249	1,075	509	425	423
Enron EBITDA	**2,337**	**2,249**	**1,327**	**1,142**	**851**

- *Transportation & Distribution*: Regulated industries. Comprised of interstate natural gas pipelines and electric utility operations (Portland General acquired July/97). Segment is regulated, and produces very stable earnings and cash flow. Enron may sell Portland General in the future, reducing the "core" earnings from this segment.
- *Retail Energy Services*: Sale of gas and electricity directly to commercial and industrial end users, and outsourcing of energy-related activities. Began in 1997 and seen as a growth vehicle, but has been a modest cash drain to date.
- *Exploration & Production*: Historically a provider of significant cash flow, with sale of EOG in August/99, Enron have largely exited this business. This has reduced Enron's exposure to gas/oil price volatility, and has increased reliance on other business segments.
- *Corporate and Other*: Includes growth businesses water, telecommunications, renewable energy businesses. New businesses are spun into own core segment as they attain critical mass.
- *Wholesale Energy Operations and Services*: Marketing energy commodities (largest in U.S. for gas and electricity), price risk management and financial services to wholesale clients. Development, acquisition, and operation of power plants, gas pipelines and other energy assets, for which long term ownership is not seen as strategic. Enron's largest segment, and the historic driver of growth. Recent growth has come from (1) electricity sales, which is driven by expanding electricity market and the activity created by the purchase of Portland General, and (2) *Price risk management* and *merchant* activities.

($MM)	Q2/99 – LTM	1998	1997	1996	1995
Cmdty Sales/Svcs	564	411	249	348	243
Engy Assts/Invtmts.	969	904	698	401	428
Unallocated Expense	(284)	(240)	(438)	(324)	(248)
Wholesale EBITDA	1,249	1,075	509	425	423

Price risk management:

- Primarily activities associated with trading. Enron has demonstrated an ability to grow this business, and consistently generate significant cash.
- Employs mark-to-market ("MTM") accounting, by which unrealized gains imbedded in the trading book (net of all costs) are taken into income. MTM accounting is now industry standard.
- In recent years rating agencies have focussed on "managing to cash" the profits earned under MTM accounting: that is ensuring earnings were a reflection of cash received. They have also focused on the tenor mismatch within the trading book between short term trading liabilities, and longer term trading assets. Enron has addressed these concerns by entering into contract monetizations, prepaids, and transactions like "Yosemite", which has helped to create a more timely match between cash received and earnings recognized. These transactions have also lengthened the tenor of the trading liabilities to create a better match with trading assets.

Merchant activities:

- The business of providing capital, primarily to energy related businesses, seeking debt or equity financing. Also includes certain energy assets. Those investments and assets which are deemed not strategic but rather are available for sale, are classified as "merchant".
- Beginning in 1998, merchant investments/assets have been marked-to-market, with consequent gains/losses brought into income. In 1998, Enron sold merchant assets for gross proceeds of $1,422 million, realizing a gain of $628 million. Year end balance of merchant assets was $2,045 million. After factoring in the purchase of merchant assets, the business was still a positive cash generator in 1998, giving some comfort that these activities produce "real" cash flow.
- During the Rawhide transaction, we evaluated in detail Enron's methodology in valuing its merchant assets. We concluded (as do Enron's auditors Arthur Anderson) that the company's methodology is prudent.

($MM)	1998	1997
Realized gain on sale	$628	$136
Cash proceeds	1,434	339
Addition to merchant portfolio	(721)	(309)
Net Cash Proceeds	$713	$30

Capital Structure

- Growth has driven debt levels higher over the past two years, but leverage has remained stable because of equity issuances and earnings. Coverages have declined somewhat but are still acceptable for a BBB+ /Baa2 company.

($MM)	Q2/99 – LTM	1998	1997	1996
Total Debt	$9,980	$8,358	$7,247	$3,941
Total Equity	11,681	9,191	6,765	4,478
Total Debt/Book Cap	46.1%	47.6%	51.7%	46.8%
Total Debt/EBITDA	4.3x	3.7x	5.1x	3.1x
EBITDA/Interest	3.0x	3.2x	3.4x	4.4x

- Off Balance Sheet Obligations:

Enron has entered into certain transactions, which create non-debt obligations for GAAP reporting purposes. If we adopt a conservative viewpoint and bring all of these obligations on balance sheet, the impact on Enron's ratios is negative, but still results in a company with an acceptable credit profile. These obligations are:

- *Off Balance Sheet Financing*: Consists of $1.95 billion prepaid oil and gas, leases, and receivables securitizations. We estimate the company has about $1.0 billion of prepaids, which are used to monetize profits embedded in the company's trading book (see PRM above). We also estimate Enron has approximately $700 million of operating (synthetic) leases. The company also has available a receivables securitization program of up to $250 million, which is largely unutilized. Enron also is involved in a number of transactions via supply and offtake agreements.
- *Guarantees of Unconsolidated Subsidiaries*: Enron provides guarantees totaling $755 million to support trading, trade and certain debt of unconsolidated subsidiaries. Of these guarantees 43% are backed with crude oil as collateral; 37% are related to power projects, half of which involve flexible tariff structures.
- *Structured Financings*: Enron actively employs structured finance transactions. These include $2.2 billion that are classified as either, minority interest ($1.2 billion) or common equity ($1.0 billion). We believe that these transactions should not be regarded as debt, since Enron's contractual obligation is limited to either equity ($1.415 billion) or the liquidation of a stipulated pool of non-core assets ($750 million).

CITI-SPSI 0003050

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We have adjusted reported financials to include off-balance sheet obligations and guarantees as debt, and reclassified $1.2 billion of minority interest and $1.0 billion of common equity as debt. Under these highly conservative adjustments, Enron maintains an acceptable credit profile.

($MM)	Q2/99 – LTM	Off Balance Sheet	Guarantees	Structured Finance	Pro-Forma Adjusted
BkDebt (BD)	$9,980	+ $1,950	+ $755	+ $2,165	$14,850
Min Int. (MI)	2,475			- 1,165	1,310
BkEquity (BE)	9,206			- 1,000	8,206
Interest	636	+156	+60	+173	1,025
EBITDA	2,337	+156			2,493
FFO	1,853				1,853
TD/Bk Cap	46%				61%
TD/EBITDA	4.3x				6.0x
EBITDA/Int.	3.7x				2.4x
(FFO+Int.)/Int.	3.9x				2.8x

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INDEX

SECTION I – YOSEMITE TRANSACTION 2
INTRODUCTION 4
RATING AGENCY REVIEW 5
ECONOMICS OF PROPOSED OFFERING 5
ACCOUNTING IMPLICATIONS 6
SYNDICATION STRATEGY 6
TRANSACTION STRUCTURE 6
SUMMARY OF PROJECT MECHANICS 6
DETAILED SUMMARY OF THE CITIBANK SWAP 10
PRELIMINARY TRANSACTION NOTE CREDIT CONSIDERATIONS 11
DESCRIPTION OF INITIAL PERMITTED INVESTMENT 14
CITIBANK CREDIT AND OTHER EXPOSURE UNDER YOSEMITE AND RELATED APPROVALS 15
SECTION II– ENRON CORP. 16
MARKET STATISTICS 17
OVERVIEW OF ENRON CORP. 17
ENRON CORP. HISTORICAL FINANCIAL INFORMATION 20
ENRON CORP. HISTORICAL SEGMENT DATA 20
ENRON CORP – SENSITIVITY ANALYSIS 20
RECENT DEVELOPMENTS 22
REVIEW OF FINANCIAL AND STOCK MARKET PERFORMANCE 24
COMPARABLE COMPANIES ANALYSIS 24
STRATEGY 25
SUMMARY ENRON STRENGTHS 25
SUMMARY RISK FACTORS 25
DETAILED INVESTMENT CONSIDERATIONS 26
RISK FACTORS 27
ENRON STRUCTURED TRANSACTION DESCRIPTIONS 29
MANAGEMENT AND BOARD OF DIRECTORS 32
SECTION III 35
SALOMON SMITH BARNEY / CITIBANK RELATIONSHIP 36
FUTURE BUSINESS POTENTIAL 37
RECOMMENDATION 37
DUE DILIGENCE 37
SALOMON SMITH BARNEY CONFLICTS 37
SECTION IV – LIST OF EXHIBITS 38
LIST OF EXHIBITS 39

A. Yosemite – Preliminary Offering Memorandum
B. Yosemite Summary of Terms and Conditions
C. Enron Marketing Slides
D. Summary of Events Impacting Payments from Yosemite Assets
E. Enron Top 20 Investors
F. Enron Third Quarter Announcement
G. Enron 10-Q, 6/30/99
H. Enron 10-K, 12/31/98
I. Enron Research Notes and Reports

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SECTION I – YOSEMITE TRANSACTION

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Investment Banking Commitment Committee Memorandum

CLIENT:	Enron Corp. ("Enron") Project Yosemite
TRANSACTION:	$800 million - $1 billion Senior Notes due ___
COMMITTEE:	Investment Grade

TRANSACTION TEAM:

Investment Banking		Fixed Income Derivatives	
Maureen Hendricks	(212) 816-0967	Lynn Feintech	(415) 627-6165
Dean Keller	(212) 816-0994		(212) 723-6445
Amanda Angelini	(212) 816-0997	Paul Deards	(212) 723-6335
Kim Champlin	(212) 816-0877	Adam Kulick	(212) 723-6449
Structured Products		Rick Caplan	(212) 723-6453
Tim Beaulac	(212) 723-6173	Fixed Income Capital Markets	
Matt Mayers	(212) 723-6173	Anne Clarke Wolff	(212) 723-6089
Jim Keller	(212) 723-6173	Storm Nickerson	(212) 723-6097
Structured Finance		Fixed Income Research	
Janice Warne	(212) 723-6152	John Melesius	(212) 816-8657
Brooke Schooley	(212) 723-6222	Debbie Grosser	(212) 723-6201
Roland DaCosta	(212) 723-6227		
James Mitchell	(212) 723-6235		

TRANSACTION OVERVIEW - DEBT

Transaction:	Linked Enron Obligations (LEOs) Senior Notes Offering
Transaction Size:	$800 – 1000 million ($725 million – $925 million of Notes, $75 million of Certificates)
Debt Ranking:	Senior Unsecured
Maturity:	5 and 7 year tranches
Underwriting Format:	Rule 144A/Reg S without Registration Rights
Managers:	**Salomon Smith Barney (Joint Lead, Books)** DLJ (Joint Lead) Deutsche Banc Alex. Brown (Joint Lead) NatWest (Co-Manager)
Anticipated Ratings:	Moody's: Baa2 Standard & Poor's: BBB+
Enron Market Capitalization:	$28 billion
Mail Preliminary Offering Circular:	Tuesday October 26, 1999
Roadshow Launch:	Expected week of November 1, 1999
Offering Date:	Expected late week of Nov 1 or early Nov 8
Latest Financials in Off. Circular:	June 30, 1999 10-Q (unaudited)
Latest Audit in Off. Circular:	December 31, 1998 10-K
Use of Proceeds:	• To purchase "Enron Investments" (Enron structured debt supported in whole or in part, directly or indirectly by Enron) to free up bank capacity • To purchase "AAA Investments" (debt securities rated Aaa/P-1 by Moody's and AAA/A-1+ by S&P and direct registered obligations of the USA) and "Eligible Investments"
Issuer's Counsel:	Vinson & Elkins L.L.P.
Underwriters' Counsel:	Milbank, Tweed, Hadley & McCloy LLP
Company Auditors:	Arthur Anderson LLP

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ENRON CORP – CAPITAL STRUCTURE DISCUSSION

The following is an analysis of Enron's capitalization giving effect to GAAP debt, a review by Moody's of Enron's debt profile and additional details of Enron off-balance sheet financings that SSB has knowledge of.

SCENARIOS	GAAP DEBT/CAP RATIO
1. GAAP Debt/Capitalization	49%
2. GAAP Debt with the addition of "Moody's" allocated debt	56%
3. GAAP Debt plus "Moody's" debt plus SSB known "financings"	65%

1. GAAP DEBT/CAPITALIZATION ANALYSIS
(In Millions of $)

Current Portion of Long Term Debt	$ 1,457
Long Term Debt	8,979
Other (1)	1,620
Total Debt	$ 12,056
Minority Interests	2,475
Company Obligated Preferred	1,001
Junior Voting Preferred	1,000
Shareholders Equity	8,206
Total Capitalization	$ 24,738

Under GAAP accounting, Enron's total debt/total capitalization ratio is 49%.

2. GAAP DEBT WITH THE ADDITION OF "MOODY'S" ALLOCATED DEBT

According to Moody's, in December 1998 Enron has "significant off-balance sheet liabilities" including $1.3 billion of guarantee $1.4 billion in transportation agreements and approximately $4.4 billion in investments in unconsolidated subsidiaries at the end of 1998 which "add significant leverage to the balance sheet".

(In Millions of $)

Investments in unconsolidated subsidiaries	$ 4,400
Off-balance sheet guarantees	1,300
Transportation commitments	1,400
Total	$ 5,700

The addition of these liabilities suggests a slightly higher debt/cap ratio: 56%.

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3. GAAP DEBT PLUS "MOODY'S" DEBT PLUS SSB KNOWN FINANCINGS

With the addition of certain financings identified by Salomon Smith Barney that are generally "off-balance sheet," the debt/cap ratio increases accordingly.

(In Millions of $)	
Condor	$ 1,500
Oil Prepaids	750
Leases	1,000
Receivable financing	250
Rawhide	750
Marlin	550
Margaux	500
Firefly	450
Sutton Bridge	$ 250
Total	$ 6,000

The debt/cap ratio suggested by the addition of these financings is 65%.

Mitigants:
- Stock take-outs for certain financings (Marlin, Condor)
- Certain double counting between Moody's analysis and the information on this table

COMPARABLE COMPANIES

	GAAP Debt/Cap	Rating
AES	78.0 %	Ba1/BB
Williams Companies	66.0	Baa2/BBB-
El Paso Energy	60.0	Baa2/BBB
Coastal Corp	53.0	Baa2/BBB

RECENT DEVELOPMENTS

October 14, 1999	Enron announced it entered a 10-year alliance valued at $1.5 billion to provide energy-management services to Simon Property Group, the largest U.S. mall developer.
October 6, 1999	Enron announced that it will offer free online electricity prices for regional utilities in Germany through Enron Energie GmbH, the German unit of Enron Corp.
October 4, 1999	Enron wins a five-year contract to sell natural gas to Chicago-based Peoples Energy Corp.'s two utilities.
September 27, 1999	Azurix Corp. announced today that it has entered into an agreement to acquire Lurgi Bamag GmbH, a process engineering company specializing in the water sector. Azurix will pay US$30 million for Lurgi Bamag GmbH and its subsidiaries, which have offices in Germany, Brazil and the United Kingdom.
September 22, 1999	Enron announced a more than $1 billion ten-year outsource agreement for total energy management services at 20 of Owen Corning's major manufacturing

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Monday, August 14, 2000

Investment Grade Commitment Committee - New York

Attending: Robert Case, Brad Gans, J. Binnie, Janice Warne, Steve Eckert, Marwan Marshi, James Kelly, Chris Teano, P. Ahearne

Chair: Bob Case

Issue: Enron Corp. – Final Commitment - $500MM-Credit Linked Notes

SSB Role:	Others:
Jt. Lead/Books	LEH (Jt. Lead); DBAB

Presenting: Bankers: M. Hendricks; Capital Markets: A. Angelini, R. Caplan, T. LeRoux

Issues Discussed:

- 3D time to market with the "Yosemite" structure.
- Discussed changes in structure
  - Citibank is intermediating the structure now, so the assets in the trust are A-1/P-1 short-term paper or Citibank deposits.
  - Negative is that it balloons Citibank's GAAP assets by $500MM.
- Cleaner structure for investors. No sense of a "blind pool", as we now have short-term paper in the trust.
- Pricing expected to be 75-80bps over Enron unsecured.
- Use of proceeds: oil prepaid swap.
  - We hedge the oil risk back to Enron.
  - Allows Enron to net-down its swap obligations.
- Discussed Enron business and credit profile.
  - Expanding business model to new areas which can be "commoditized".
  - Credit upgraded by Moody's to Baa1.
  - Enron Online is the company's online order book for electricity and natural gas. Have taken nearly 50% market share now by taking the lead here.
  - Off balance sheet debt about $6bn – would increase proforma debt/capital to 58% from 48%.
- Desire of Enron to divest Latin American assets.
  - Company is exploring sale through MS.
  - Discussed likely credit impact. Equity writeoff, if any, likely immaterial.
  - Discussed current disclosure posture. Not at a point of disclosure yet. We need to continuously monitor.
  - Melesius is over the wall on due diligence.

[APPROVED]

Follow up: Final due diligence, especially on any divestiture plans.

Permanent Subcommittee on Investigations
EXHIBIT #171

SALOMON SMITH BARNEY

Interoffice Memo

Date of Meeting: Friday, August 11, 2000

Committee: Investment Grade - New York (Special Meeting)

DELIVER BY HAND

Jessica Palmer	388-24th	Robert Rubin	388-39th
Robert Case	388-24th	James Kelly	390-8th
Myrna Cruz	388-24th	Patrick Ryan	390-1st
Krys Gaboff	388-24th	Janice Warne	390-4th
Brad Gans	388-34th	Geoff Coley	390-4th
John Binnie	388-35th	Melissa Motherway	390-4th
George Saks	388-34th	Marwan Marshi	390-4th
		c/o Nancy Davis	Large Trading Floor
Scott Van Bergh	388-34th		

DELIVER BY MESSENGER

Dick Trask (559-6665)	399 Park Avenue	Jolie Eisner (559-3498)	399 Park Avenue
Citibank 11th Floor	New York, NY	Citibank 11th Floor	New York, NY
Zone 17	10022	Zone 17	10022

Chris Teano
Citibank
250 West Street
10th Floor
New York, NY 10013

DELIVER BY INTEROFFICE MAIL

Control Group c/o John Benesch — 7 WTC – 32nd Floor

Tom Doyle (559-5204)
Citigroup
Audit Risk & Credit Review - CF
850 Third Avenue
NYC 10043

Name of Transaction: **Enron Credit Linked Note Trust**

Com Cover

SALOMON SMITH BARNEY
A member of citigroup

Investment Banking Commitment Committee Memorandum

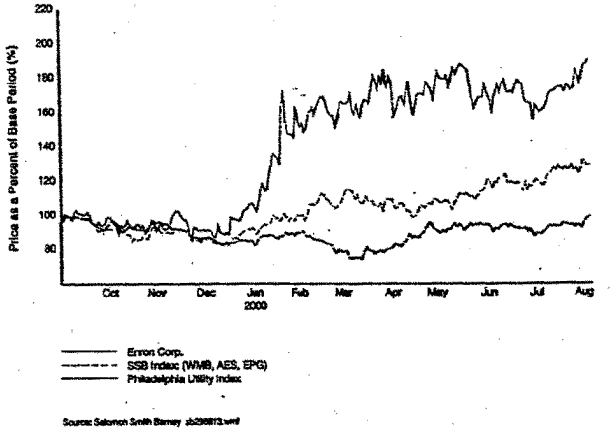
CLIENT:	Enron Corp. ("Enron") Enron Credit Linked Note Trust
TRANSACTION:	$500 million Senior Notes due ___
COMMITTEE:	Investment Grade

TRANSACTION TEAM:

Investment Banking		Fixed Income Derivatives	
Maureen Hendricks	(212) 816-0967	Lynn Feintech	(415) 627-6165
Dean Keller	(212) 816-0994		(212) 723-6445
Paul Burton	(212) 816-0309	Rick Caplan	(212) 723-6453
Structured Finance		Amanda Angelini	(212) 723-6484
Janice Warne	(212) 723-6152	Tim LaRoux	(212) 723-6436
Fixed Income Research		Doug Warren	(212) 723-6118
John Melesius	(212) 816-8657	Fixed Income Capital Markets	
Deborah Grosser	(212) 723-6201	Anne Clarke Wolff	(212) 723-6089
Brian Schmidt	(212) 816-2699	Steve Becton	(212) 723-6093
Citibank Team			
Steven Bailey	(713) 654-2887		

TRANSACTION OVERVIEW – DEBT	
Transaction:	Enron Credit Linked Note Trust Senior Notes Offering
Transaction Size:	$500 million (and $50 million of Certificates)
Debt Ranking:	Senior Unsecured
Maturity:	5 to 10 years
Underwriting Format:	Rule 144A/Reg S without Registration Rights
Managers:	**Salomon Smith Barney (Books)** Lehman Brothers (Joint Lead) Deutsche Banc Alex. Brown (Co-Manager)
Anticipated Ratings:	Moody's: Baa1 Standard & Poor's: BBB+
Enron Market Capitalization:	$58 billion
Roadshow Launch:	Week of Aug 14, 2000
Offering Date:	August 23, 2000
Latest Financials in Off. Circular:	March 31, 2000 10-Q (unaudited)
Latest Audit in Off. Circular:	December 31, 2000 10-K
Use of Proceeds:	To purchase "Trust Investments" (time deposits or promissory notes of North America money center banks rated AA-/Aa3 with a short term rating of A1/P1), obligations for borrowed money, gics from insurance companies rated Aaa by Moody's and AAA/ by S&P (less than one year), and AAA US Government securities.
Issuer's Counsel:	Vinson & Elkins L.L.P.
Underwriters' Counsel:	Milbank, Tweed, Hadley & McCloy LLP
Company Auditors:	Arthur Anderson LLP

DAILY DATA: SEPTEMBER 01, 1999 THROUGH AUGUST 08, 2000



Source: Salomon Smith Barney zb250813.wmf

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RATING AGENCY REVIEW

On March 23, 2000, Enron got its wish with a coveted upgrade by Moody's to Baa1 from Baa2. The outlook is now stable. With the rating action, Enron is now firmly ensconced as a High BBB credit by the four major rating agencies. Moody's more positive stance on the credit began in November 1999, with Enron's announcement that it would sell Portland General for $3.1 billion in cash and assumed debt to Sierra Pacific Resources. At that time, Moody's cited the added financial flexibility Enron derives from the transaction as well as the prospects for improvements in the company's capital structure resulting from debt paydown. In leading up to rating action, Moody's also appears to have gained greater comfort with Enron's marketing and trading operations, which are becoming an increasingly important source of earnings and cash flow for the company. According to Moody's, Enron's, "stress testing and VAR calculations in the Wholesale business are consistent on a relative scale with other commodities trading firms."

Moody's Investors Service (Baa1/Stable)

Enron's rating was raised to Baa1 reflecting increased earnings from its position as North America's leading energy wholesaler and the expectation of an improved capital structure subsequent to the sale of Portland General Electric. The outlook for Enron's Baa1 rating is stable. The challenge to management will be to continue growth in the wholesale business, which requires ever-increasing volumes, without further levering its financial position.

Standard & Poor's (BBB+/Stable)

Enron's ratings recognize the stable regulated gas transmission and electric utility businesses, and the accelerating growth in riskier, non-regulated units. With its sizable energy asset base, Enron has created a powerhouse wholesale energy marketing operation, which it is duplicating in Europe and Latin America. Ratings stability anticipates continued financial stability, reflecting Enron's healthy business profile and its growth opportunities. As non-regulated businesses grow, Enron is constantly challenged to achieve financial performance commensurate with its shifting asset mix and business risk.

Duff & Phelps (BBB+)

The approximately $1.7 billion in after-tax cash proceeds from the sale of Portland General, coupled with the assumption of $1.1 billion in debt by Sierra Pacific, will allow Enron to reduce its consolidated debt by $2.8 billion. The loss of $250 million of PGE-related cash flow would be offset by a like reduction in PGE's fixed obligations. The net effect of these considerations helps offset the loss of a stable, regulated cash flow source for Enron.

Fitch IBCA (BBB+)

Enron's core operations demonstrate strong competitive market positions and continue to provide stable earnings and cash flow contributions. Enron is the clear industry leader in energy marketing, trading, and risk management. On balance, Enron's domestic and international growth opportunities remain favorable. Credit risk is minimized by a disciplined investment strategy and prudent risk management practices.

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CAPITAL STRUCTURE DISCUSSION

($ in millions)	GAAP	Enron Analysis	SSB Base Case Analysis *	SSB Alternative Analysis	Moody's 1998 Analysis
GAAP Items					
Current Portion	$ 1,884	$ 1,884	$ 1,884	$ 1,884	$ 1,884
Long Term Debt	8,288	8,288	8,288	8,288	8,288
Other	1,695	1,695	1,695	1,695	1,695
Minority Interest	1,872	1,872	1,872	1,872	1,872
Minority Interest adjustment			(1,165)		
Company Obligated Preferred	1,099	1,099	1,099	1,099	1,099
Junior Voting Preferred	1,000	1,000	1,000	1,000	1,000
Shareholders' Equity	9,140	9,140	9,140	9,140	9,140
ENE Analysis Items					
Unconsolidated Subsidiary Debt (100% of Project Debt)		8,486	--		
Unconsolidated Subsidiary Partner Equity		4,667			
SSB Analysis Items					
Off Balance Sheet Financings			2,630		
Leases			1,000		
Minority Interest Reclassification as Debt			1,165		
All off balance sheet financings				6,330	
Moody's Analysis Items					
Investments in Projects/Unconsolidated Subsidiaries					5,038
Off Balance Sheet Guarantees					1,300
Transportation Commitments					1,400
Total "Debt"	11,867	20,353	16,662	18,197	19,603
Total Capitalization	$ 24,978	$ 38,131	$ 28,608	$ 31,306	$ 32,714
Debt/Cap with Obligated Preferred as Equity	47.5%	53.4%	58.2%	58.1%	59.9%
Debt/Cap Excluding Obligated Preferred	43.7%	55.0%	60.6%	60.2%	62.0%
Debt+Cap with Company Preferred as Debt	51.9%	58.3%	62.1%	61.6%	63.3%
Allocable share of Unconsolidated Project Debt			3,819	3,819	
(Total Debt + Allocable share of Unconsol. Proj. Debt)/Cap.			63.2%	62.7%	

* Excludes contingent equity secured transactions

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CITI-SPSI 0007241

Significant "Other Financings" of Enron

(In Millions of $)

Transaction	Amount
Off Balance Sheet financings	
Yosemite II	$700
Yosemite I	280
Oil Prepaids	750
Leases	1000
Receivable Financing	250
Merlin	500
Margaux	150
Continent Equity Transactions	
Condor	1500
Firefly	450
Marlin	750
Total	$6,330

Integrated Energy Peer Group - Selected Financial Statistics for LTM 3/31/00

Enron compares favorably with its integrated pipeline peer group companies on most financial benchmarks. Enron is the largest of its peers as measured by assets, revenues, and market capitalization. Enron is also the least leveraged of its peers when calculated by Debt to Capital and Debt to FFO. Enron's cash flow coverage is also among the strongest in the group but its earnings coverages, EBIT / Interest of 2.55x and EBITDA / Interest of 3.83x are slightly weaker than the peer group averages of 2.58x and 3.96x respectively. The weaker earnings coverage ratios can be explained, in part, by Enron's relatively modest use of short-term debt financing. At 12/31/99, only 16% of Enron's debt was short-term compared with approximately 47% for Dynegy. Although a greater use of short-term debt can lower interest expense and improve coverage measures, it also increases refinancing and interest rate risk.

Company	Moody's	S&P	Assets	Market Cap[1]	ROE	EBIT[2] / Int	EBITDA[2] / Int	FFO Cov[3]	Debt / FFO	Debt Cap[4]	Debt / Tot Cap[5]
Enron Corp	Baa1/Stable	BBB+/Stable	37,484	56,322	9.9 %	2.55 x	3.83 x	4.33 X	4.65 x	53.0 %	53.3 %
El Paso Energy	Baa2/Stable	BBB/Stable	16,654	11,578	4.8 %	2.33 x	3.61 x	3.14 X	6.78 x	65.8 %	58.6 %
Dynegy Inc.	Baa2/Stable	BBB+/Stable	13,042	10,869	8.6 %	3.26 x	4.84 x	3.15 X	22.46 x	63.7 %	66.2 %
Williams	Baa2/Stable	BBB-/Positive	25,800	17,698	4.7 %	1.36 x	2.53 x	3.93 X	7.39 x	65.6 %	64.7 %
Coastal Corp.	Baa2/Stable	BBB/Stable	15,366	12,996	13.1 %	3.39 x	4.87 x	5.93 X	4.85 x	56.8 %	59.9 %
Average			*21,669*	*21,893*	*8.2 %*	*2.58 x*	*3.94 x*	*4.10 x*	*9.23 x*	*61.0 %*	*60.5 %*

[1] Market capitalization as of May 16, 2000, [2] Includes earnings from unconsolidated equity affiliates, [3] (FFO + Cash Interest) / Cash Interest, [4] Total Debt / (Total Debt + Equity),
[5] (Total Debt + Preferred Securities) / (Total Debt + Preferred Securities + Minority Interest + Equity)
Source: Company financial statements and Salomon Smith Barney

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CITI-SPSI 0007242

Unknown

From: Fox III, William T
Sent: Wednesday, September 26, 2001 7:06 AM
To: Verme, Alberto J [IBD]; Reilly, James F [IBD]; Nepveux, Michael W; Clarke Wolff, Anne [FI]; Hendricks, Maureen A [IBD]
Cc: Macdonald, Alan S; Morse, Robert [IBD]
Subject: Enron

Spoke with Ben Glisan, Tres, re our turndown of the $200mm prepaid bridge request. Tim Dispain listened in.

Upon his questioning gave following reasons: 1) We currently had high exposure and we have established limits based on risk rating and term; 2) we already had the $250mm prepaid bridge on the books from June; and 3) given today's capital markets and the uncertain outlook we were not confident as to when the bridge could be taken out.

He was calm and did not threaten loss of any specific business. He did want to understand if we had any specific problems with the Enron credit. We talked about need for updated review with the company and suggested address the following: 1) Skilling departure and if any smoking guns; 2) liquidity needs of the trading business if in todays enviornment we have wide sudden swings in commodity prices; 3) better breakdown of where they make their money in the trading business; 4) better disclosure on their off balance sheet obligations particularly to what extent they stand on their own credit or if Enron was effectively on the hook; and 5) an update from Rick Buy on risk management process, procedures, measurement etc. It is in the works and will be arranging mutually convenient date. Also agreed to send him list of issues/questions prior to the meeting.

For clarrity he posed to two questions: 1) If Enron had provided letter of credit from say Bank of America for the prepaid would we have done the deal; said yes as this would not be counted as Enron exposure and that market take out risk would have been eliminated; 2) Do we still have capital available for Enron in the 4th quarter; said yes subject to the existing $250mm prepaid being paid off and outlook for the capital markets.

Finally, he acknowledged that we had long historical relationship that he fully expected to continue; this turndown was major disappointment and perhaps a first from Citi but we still have significant capital committed and Enron recognizes that. However, he expects to expand the core banks he relys on from 1-2 to 3-5. They currently have 10 tier one relationship banks. Expect will continue to work on existing deals with us but intend to spread the business. His real concern is that if his key bank cannot deliver for him his oher banks could well have the same issues This is probably valid concern. No specifics on the bond deal. The real franchise issue is the CLN business as well as continued penetration of M&A business. Told him that we intended to work even harder on the relationship etc.

More to come; I have call with Fastow today.

Permanent Subcommittee on Investigations
EXHIBIT #172

SUPPLEMENT
(To Offering Memorandum
dated November 4, 1999)

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$750,000,000

Yosemite Securities Trust I

(a Delaware statutory business trust)

8.25% Series 1999-A Linked Enron Obligations (LEOs℠) due 2004

The 8.25% Series 1999-A Linked Enron Obligations (LEOs℠), due 2004, offered pursuant to the accompanying Offering Memorandum, dated November 4, 1999 (the "Memorandum") as supplemented hereby (the "Series 1999-A LEOs"), evidence the debt obligations of the Yosemite Securities Trust I (the "Trust") secured by all of the assets related to the Series 1999-A LEOs. This Supplement may not be used to effect sales of the Series 1999-A LEOs unless accompanied or preceded by the Memorandum. Capitalized terms used herein and not defined shall have the meaning ascribed to such terms in the accompanying Memorandum.

Application has been made to list the Series 1999-A LEOs on the Luxembourg Stock Exchange.

Information about the LEOs is contained in: (i) this Supplement which specifically describes the Series 1999-A LEOs being offered and (ii) the accompanying Memorandum which describes the Notes.

Investing in the Series 1999-A LEOs involves certain risks. See "Risk Factors" in the Memorandum beginning on page 10.

The Series 1999-A LEOs have not been and will not be registered under the Securities Act of 1933, as amended (the "Securities Act"), or any state securities laws and may not be offered or sold except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and applicable state securities laws. Accordingly, the Series 1999-A LEOs are being offered and sold in the United States only to "Qualified Institutional Buyers" (as defined under Rule 144A under the Securities Act) and outside the United States in accordance with Regulation S under the Securities Act. For a description of certain restrictions on transfers of the Series 1999-A LEOs, see *"Plan of Distribution"* and *"Notice to Investors"* in the accompanying Memorandum.

	Per LEO	Total
Price to Investors	99.973%	$749,797,500

The Trust will receive all of the proceeds of the sale of the Series 1999-A LEOs. The price to investors set forth above does not include accrued and unpaid interest, if any. Interest on the Series 1999-A LEOs will accrue from November 18, 1999 and must be paid by the investors if the Series 1999-A LEOs are delivered after November 18, 1999.

The Initial Purchasers, as named below, are offering the Series 1999-A LEOs subject to various conditions. The Initial Purchasers expect to deliver the Series 1999-A LEOs to investors on or about November 18, 1999.

LEOs is a service mark of Enron.

Book-Running Lead Manager

Salomon Smith Barney

Joint Lead Manager

Deutsche Banc Alex. Brown

Joint Lead Manager

Donaldson, Lufkin & Jenrette

Manager

Greenwich NatWest

November 4, 1999

Permanent Subcommittee on Investigations
EXHIBIT #173

You should rely only on the information contained in or incorporated by reference in this Supplement and the accompanying Memorandum. The Trust and the Initial Purchasers have not authorized anyone to provide you with different information. The Trust is not, and the Initial Purchasers are not, making an offer of the Series 1999-A LEOs in any state where the offer is not permitted. You should not assume that the information contained in or incorporated by reference in this Supplement and the accompanying Memorandum is accurate as of any date other than the date of this Supplement.

TABLE OF CONTENTS

	Page
Supplement	
Description of Series 1999-A LEOs	S-3
Supplemental Plan of Distribution	S-3
Offering Memorandum	
Available Information	iv
Forward Looking Statements	vi
Summary of Offering	1
The Offering	3
Risk Factors	10
Use of Proceeds	15
Trust Capitalization	15
Unaudited Pro Forma Balance Sheet of the Trust	15
Ratings	15
Description of Enron	16
Enron Historical Consolidated Financial Information	17
Selected Historical Consolidated Financial Information of Enron	18
Capitalization of Enron	19
Description of Citibank, N.A.	20
The Depositor	21
The Trust	21
Description of the Notes	22
Description of the Certificates	40
Description of the Citibank Swap	42
Tax Considerations	57
Certain ERISA Considerations	59
Plan of Distribution	60
Notice to Investors	61
Legal Matters	64
Glossary	A-1
Index of Defined Terms	B-1

The information contained and incorporated by reference in this Memorandum has been furnished by the Trust, the Depositor, Citibank, N.A., Enron Corp. ("Enron"), the other parties to the transactions described herein and other sources believed by the Trust, the Depositor, Citibank, N.A., Enron and the other parties to the transactions described herein to be reliable. The Initial Purchasers make no representation or warranty as to the accuracy or completeness of any such information. The Initial Purchasers do not assume responsibility for the verification of the information furnished by, or referred to herein concerning, Citibank, N.A. This Memorandum contains or incorporates by reference summaries, believed to be accurate, of certain terms of certain documents, but reference is made to the actual documents, copies of which (except for Underlying Instruments and individual Confirmations under the Citibank Swap) will be made available upon reasonable request (subject to appropriate confidentiality restrictions), for the complete information contained therein. All such summaries are qualified in their entirety by this reference and such complete information.

No person is authorized in connection with any Offering made hereby to give any information or to make any representation not contained or incorporated by reference in this Memorandum, and, if given or made, such other information or representation must not be relied upon as having been authorized by the Trust, the Depositor, Citibank, N.A., Enron, any of the other parties to the transactions described herein or the Initial Purchasers. The information contained herein is provided as of the date hereof and is subject to change or amendment without notice. Neither the delivery of this Memorandum at any time nor any subsequent sale of the Notes offered hereby shall, under any circumstances, create any implication that there has been no change in the information set forth or incorporated by reference herein or in the affairs of the Trust, the Depositor, Citibank, N.A., Enron or any of the other parties to the transactions described herein since the date hereof.

Prospective investors are not to construe the contents of this Memorandum as investment, legal or tax advice. Each investor should consult its own counsel, accountants and other advisors as to legal, tax, business, financial and related aspects of a purchase of the Notes offered hereby. None of the Trust, the Depositor, Citibank, N.A., Enron, the other parties to the transactions described herein nor the Initial Purchasers are making any representation to any offeree or purchaser of the Notes regarding the legality of an investment therein by such offeree or purchaser under applicable laws.

The distribution of this Memorandum and the offer and sale of the Notes may be restricted by law in certain jurisdictions. Persons into whose possession this Memorandum or any of the Notes come must inform themselves about, and observe, any such restrictions.

This Memorandum does not constitute an offer to sell or a solicitation of an offer to buy any of the Notes to any person in any jurisdiction where it is unlawful to make such an offer or solicitation.

The Notes described herein have not been registered with, recommended by or approved by the U.S. Securities and Exchange Commission (the "SEC") or any other U.S. federal or state securities commission or regulatory authority, nor has the SEC or any such commission or regulatory authority passed upon the accuracy or adequacy of this Memorandum. Any representation to the contrary is a criminal offense.

This Memorandum has been prepared by the Trust solely for use in connection with the offering of the Notes and the listing of the Notes on the Luxembourg Stock Exchange. The Trust (and the Depositor, with respect to the information appearing under *"Depositor,"* the Initial Purchasers, with respect to certain information appearing under *"Plan of Distribution,"* Enron, with respect to the information appearing under *"Description of Enron,"* and Citibank, N.A., with respect to the information appearing under *"Description of Citibank"*) has taken reasonable care to ensure that facts stated in this Memorandum (in the case of the Depositor, the Initial Purchasers, Enron and Citibank, N.A., solely with respect to the information provided by such party under the applicable heading) are true and accurate in all material respects and that there have not been omitted material facts the omission of which would make misleading any statements of fact or opinion herein (in the case of the Depositor, the Initial Purchasers, Enron and Citibank, N.A., solely with respect to the information provided by such party under the applicable heading). The Trust (and the Depositor, with respect to the information appearing under *"Depositor,"* the Initial Purchasers, with respect to certain information appearing under *"Plan of Distribution,"* Enron, with respect to the information

Limitation as to Placement in the United Kingdom

This Memorandum may only be issued or passed on to any person in the United Kingdom if that person is of a kind described in Article 11(3) of the Financial Services Act 1986 (Investment Advertisements) (Exceptions) Order 1996 (as amended) or is a person to whom this Memorandum may otherwise be lawfully issued or passed on. No offer to sell or sale of the Notes offered hereby may be made in the United Kingdom by means of this Memorandum other than to a person whose ordinary business is to buy or sell shares or debentures (whether as principal or agent) or in circumstances which do not constitute an offer to the public within the meaning of the Public Offers of Securities Regulation 1995. *See "Plan of Distribution."*

AVAILABLE INFORMATION

The Trust

The Trust is not currently subject to the informational requirements of the United States Securities Exchange Act of 1934, as amended (the "Exchange Act"). Consequently, the Trust has not been and will not be required to file reports, proxy statements or other information with the SEC. The Trust has agreed that it will furnish to the Noteholders and to prospective transferees of Notes, upon their request, the information required to be delivered pursuant to Rule 144A(d)(4) under the Securities Act. The Trust will provide to the Indenture Trustee, who will then furnish to Citibank and, upon request by any Noteholder, to such Noteholder, within 60 days after the end of the first, second and third fiscal quarters of each fiscal year (beginning with the first fiscal quarter in the year 2000), unaudited consolidated balance sheets and statements of income and cash flows for such fiscal quarter and the portion of the fiscal year ending with such fiscal quarter, and will provide to the Indenture Trustee, who will then furnish to Citibank and, upon request by any Noteholder, to such Noteholder, within 120 days after the end of each fiscal year, audited consolidated financial statements (beginning with fiscal year 2000). *See "Description of the Notes — Covenants — Reports."*

Enron

Enron is subject to the informational requirements of the Exchange Act, and in accordance therewith files reports, proxy statements and other information with the SEC. Such reports, proxy statements and other information can be inspected and copied at the public reference facilities maintained by the SEC at 450 Fifth Street, N.W., Room 1024, Washington, D.C. 20549; and at the following Regional Offices of the SEC: Midwest Regional Office, Citicorp Center, Suite 1400, 500 West Madison Street, Chicago, Illinois 60661-2511; and Northeast Regional Office, 7 World Trade Center, New York, New York 10048, at prescribed rates or from the site maintained by the SEC on the World Wide Web at http://www.sec.gov. Enron's common stock is listed on the New York, Chicago and Pacific Stock Exchanges. Reports, proxy statements and other information concerning Enron can be inspected and copied at the respective offices of these exchanges at 20 Broad Street, New York, New York 10005; 120 South LaSalle Street, Chicago, Illinois 60603; and 301 Pine Street, San Francisco, California 94014.

The following documents filed by Enron (File No. 1-13159) with the SEC pursuant to the Exchange Act are incorporated herein by reference:

(a) Annual Report on Form 10-K for the year ended December 31, 1998;

(b) Quarterly Report on Form 10-Q for the quarter ended March 31, 1999;

(c) Quarterly Report on Form 10-Q for the quarter ended June 30, 1999;

(d) Current Reports on Form 8-K dated January 26, 1999 and March 18, 1999; and

(e) The description of Enron's capital stock set forth in Enron's Registration Statement on Form 8-B filed on July 2, 1997.

RISK FACTORS

The purchase of the Notes involves certain risks. Prospective purchasers of the Notes should carefully review the information included elsewhere and incorporated by reference in this Memorandum and should particularly consider, among others, the following factors prior to investing in the Notes:

Investment Decisions

Noteholders will have credit exposure to Enron, Citibank and obligors on Permitted Investments. However, in the absence of a foreclosure on Collateral under the Indenture, Noteholders will not have a direct contractual claim against Enron in respect of Enron Investments or otherwise and will not have a direct contractual claim against Citibank in respect of the Citibank Swap or otherwise. These risks are discussed more fully below.

Dependence on Enron

Sources of funds available to the Trust are designed to be sufficient to provide for payments on the Notes that would have been made if the Notes were Enron senior unsecured obligations having the same principal amount and interest rate as the Notes. Therefore, the Notes are subject to the same credit risks to which such Enron obligations are subject, as well as certain other risks. Accordingly, the Trust's ability to make timely and full payment of the amounts payable on the Notes will be dependent in part upon the creditworthiness of Enron. Amounts payable to the Trust under the Citibank Swap will, in turn, depend in part upon certain credit related events with respect to Enron. Thus, although the Notes are not a direct obligation of Enron, amounts paid with respect to the Notes depend in part upon (i) in the event of an Enron Failure to Pay or an Enron Bankruptcy, amounts paid by or recovered from Enron either in respect of Deliverable Obligations or Enron Investments held by the Trust and (ii) in the event of an Enron Bankruptcy, the value of Enron Reference Obligations.

Enron Bankruptcy

Payments under the Citibank Swap. If an Enron Bankruptcy occurs, all Trust Fixed Payments and Citibank Fixed Payments under the Citibank Swap will immediately cease. As a result, the Trust may not have sufficient funds to pay interest on the Notes during the pendency of such proceedings, which may be a substantial period. The Citibank Swap is designed to provide that, after settlement thereunder, the Trust will be holding assets with a value equivalent to Enron senior unsecured obligations with the same outstanding amount as the Notes; thus, after all payments on the Citibank Swap, the value of such assets at the completion of the Enron Bankruptcy proceedings may be insufficient to permit the Trust to pay in full the amount due to the Noteholders on the Notes. Further, there can be no assurance as to when a final distribution with respect to the Notes will be made in the Enron Bankruptcy proceedings. Citibank is not obligated to make payments prior to the completion of the Enron Bankruptcy proceedings. A final distribution with respect to the Notes in connection with the completion of the Enron Bankruptcy proceedings may not occur until after the Maturity Date of the Notes. *See "Description of the Citibank Swap — Settlement of the Citibank Swap following an Enron Bankruptcy."*

Substitution of Non-Performing Enron Investments. If Citibank exercises its option during an Enron Bankruptcy to substitute Enron Investments (which need not be Deliverable Obligations) for Trust Investments, such Enron Investments need not be performing. The outstanding amount of Enron Investments delivered to the Trust will equal the outstanding amount of Trust Investments so exchanged less, in the case of Deliverable Obligations, a *pro rata* share of the related Certificates. Citibank is likely to exercise such option. If Citibank substitutes Deliverable Obligations then, in such circumstances, all of Citibank's obligations under the Citibank Swap with respect to such Deliverable Obligations will cease. As a result, in the event of an Enron Bankruptcy, sources available to the Trust may not be sufficient to permit the Trust to repay the related Series of Notes in full when due.

Distributions In-Kind. If distributions on account of an Enron Investment following an Enron Bankruptcy are made in securities or property other than cash, there can be no assurance that the proceeds of the sale or other disposition of such securities or property will equal the value of such securities or property as determined by an Appraiser in connection with calculation of the Recovery Percentage of such Enron Investment for purposes of settlement under the Citibank Swap. Accordingly, the proceeds received by the

USE OF PROCEEDS

The net proceeds from the offering and sale of the Notes of a Series (and the related Certificates) will be used by the Trust on the Closing Date to acquire Series Trust Investments that will mature prior to the Maturity Date of such Series, in an aggregate outstanding amount equal to the sum of (i) the principal amount of the Notes of such Series and, (ii) the Designated Certificate Base Amount. Such Series Trust Investments will be available to pay amounts due and payable under the related Series and, until such related Series is paid in full, such Series Trust Investments will not be available to pay amounts due and payable under any other Series.

TRUST CAPITALIZATION

The initial capitalization of the Trust on the Closing Date will be as follows:

Notes	$750,000,000
Total Debt	$750,000,000
Certificates	$ 75,000,000
Total Equity	$ 75,000,000
Total Capitalization	$825,000,000

UNAUDITED PRO FORMA BALANCE SHEET OF THE TRUST

The unaudited pro forma balance sheet of the Trust on the Closing Date will be as follows:

Assets		Capital	
Trust Investments	$825,000,000	Notes	$750,000,000
		Certificates	$ 75,000,000
Total Assets	$825,000,000	Total Capital	$825,000,000

RATINGS

Moody's and S&P will assign each Series of Notes the ratings set forth in the related Supplement. Ratings are not a recommendation to purchase, hold or sell any Series of Notes, inasmuch as the ratings do not comment as to the market price or suitability for a particular investor. The ratings assigned to each Series of Notes reflect only the views of the Rating Agencies, and are based upon current information furnished to Moody's and S&P by the Trust, Citibank, N.A., the Depositor, Enron and the Initial Purchasers and obtained from other sources and upon their own investigations, studies and assumptions. The ratings may be changed, suspended or withdrawn as a result of changes in, or unavailability of, such information, and none of the Trust, Citibank, the Depositor, Enron or the Initial Purchasers has undertaken any responsibility to the Noteholders after issuance of each Series of Notes to assure the maintenance of the ratings, to oppose any revision or withdrawal thereof, or to notify purchasers of such Series of Notes in any such event. Any downward change in or withdrawal of the ratings may have an adverse effect on the market price or marketability of each Series of Notes.

An explanation of the significance of the ratings may be obtained from the rating agency furnishing the same at the following addresses: Moody's Investors Service, Inc., 99 Church Street, New York, New York 10007 and Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, 55 Water Street, New York, New York 10041.

CAPITALIZATION OF ENRON
(In millions)

The following table sets forth the consolidated capitalization of Enron as of June 30, 1999.

Short-Term Debt	$ —
Notes payable	—
Current maturities of long term debt	—
	—
Long-Term Debt	8,979
Minority Interests	2,475
Company-Obligated Preferred Securities of Subsidiaries	1,001
Shareholders' Equity	
Second preferred stock, cumulative, no par value	131
Series A Junior Voting Convertible Preferred Stock, no par value	1,000
Common stock, no par value	6,588
Retained earnings	2,369
Accumulated other comprehensive income	(760)
Common stock held in treasury	(1)
Other	(121)
Total Shareholders' Equity	9,206
Total Capitalization	$21,661

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ACCESSION NUMBER: 0001024401-99-000020
CONFORMED SUBMISSION TYPE: 10-Q
PUBLIC DOCUMENT COUNT: 3
CONFORMED PERIOD OF REPORT: 19990630
FILED AS OF DATE: 19990816

FILER:

COMPANY DATA:
COMPANY CONFORMED NAME: ENRON CORP/OR/
CENTRAL INDEX KEY: 0001024401
STANDARD INDUSTRIAL CLASSIFICATION: WHOLESALE-PETROLEUM & PETROL
IRS NUMBER: 470255140
STATE OF INCORPORATION: OR
FISCAL YEAR END: 1231

FILING VALUES:
FORM TYPE: 10-Q
SEC ACT:
SEC FILE NUMBER: 001-13159
FILM NUMBER: 99690211

BUSINESS ADDRESS:
STREET 1: 1400 SMITH ST
CITY: HOUSTON
STATE: TX
ZIP: 77002-7369
BUSINESS PHONE: 7138536161

MAIL ADDRESS:
STREET 1: 1400 SMITH ST
CITY: HOUSTON
STATE: TX
ZIP: 75002-7369

FORMER COMPANY:
FORMER CONFORMED NAME: ENRON OREGON CORP
DATE OF NAME CHANGE: 19961008
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 1999

Commission File Number 1-13159

Permanent Subcommittee on Investigations
EXHIBIT #174

ENRON CORP.
(Exact name of registrant as specified in its charter)

Oregon	47-0255140
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
Enron Building 1400 Smith Street Houston, Texas	77002
(Address of principal executive offices)	(Zip Code)

(713) 853-6161
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes [X] No [ ]

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at July 31, 1999
Common Stock, No Par Value	356,916,343 shares

<PAGE>

ENRON CORP. AND SUBSIDIARIES

TABLE OF CONTENTS

Page No.

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

http://www.sec.gov/Archives/edgar/data/1024401/0001024401-99... 07/17/2002

Consolidated Income Statement - Three Months Ended June 30, 1999 and 1998 and Six Months Ended June 30, 1999 and 1998 3
Consolidated Balance Sheet - June 30, 1999 and December 31, 1998 4
Consolidated Statement of Cash Flows - Six Months Ended June 30, 1999 and 1998 6
Notes to Consolidated Financial Statements 7

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 16

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings 41

ITEM 4. Submission of Matters to a Vote of Security Holders 41

ITEM 6. Exhibits and Reports on Form 8-K 42

<PAGE>
<TABLE>

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS
ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED INCOME STATEMENT
(In Millions, Except Per Share Amounts)
(Unaudited)

<CAPTION>

	Three Months Ended June 30,		Six Months Ended June 30,	
	1999	1998	1999	1998
<S>	<C>	<C>	<C>	<C>
Revenues	$9,672	$6,557	$17,304	$12,239
Costs and Expenses				
Cost of gas, electricity and other products	8,347	5,528	14,647	10,087
Operating expenses	780	570	1,425	1,007
Oil and gas exploration expenses	20	26	45	60
Depreciation, depletion and amortization	236	190	451	372
Taxes, other than income taxes	56	45	118	103
	9,439	6,359	16,686	11,629
Operating Income	233	198	618	610
Other Income and Deductions				
Equity in earnings of unconsolidated affiliates	163	109	231	153
Gains on sales of assets and investments	-	4	12	4
Other income, net	73	34	141	49
Income Before Interest, Minority Interests and Income Taxes	469	345	1,002	816
Interest and Related Charges, net	175	131	350	264
Dividends on Company-Obligated Preferred Securities of Subsidiaries	19	20	38	39

Minority Interests	23	19	56	44
Income Tax	30	30	83	110
Net Income Before Cumulative Effect of Accounting Changes	222	145	475	359
Cumulative Effect of Accounting Changes, net of tax	-	-	(131)	-
Net Income	222	145	344	359
Preferred Stock Dividends	19	5	23	9
Earnings on Common Stock	$ 203	$ 140	$ 321	$ 350
Earnings Per Share of Common Stock				
Basic				
Before Cumulative Effect of Accounting Changes	$ 0.57	$ 0.44	$ 1.30	$ 1.12
Cumulative Effect of Accounting Changes	-	-	(0.38)	-
Basic Earnings per Share	$ 0.57	$ 0.44	$ 0.92	$ 1.12
Diluted				
Before Cumulative Effect of Accounting Changes	$ 0.54	$ 0.42	$ 1.22	$ 1.06
Cumulative Effect of Accounting Changes	-	-	(0.35)	-
Diluted Earnings per Share	$ 0.54	$ 0.42	$ 0.87	$ 1.06
Average Number of Common Shares Used in Computation				
Basic	354	319	348	312
Diluted	386	346	379	338

<FN>
The accompanying notes are an integral part of these consolidated financial statements.
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<PAGE>
<TABLE>

PART I. FINANCIAL INFORMATION - (Continued)
ITEM 1. FINANCIAL STATEMENTS - (Continued)
ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET
(In Millions)
(Unaudited)

<CAPTION>

	June 30, 1999	December 31, 1998
ASSETS		
<S>	<C>	<C>
Current Assets		
Cash and cash equivalents	$ 286	$ 111
Trade receivables	2,730	2,060
Other receivables	792	833
Assets from price risk management activities	1,756	1,904
Inventories	557	514
Other	772	511
Total Current Assets	6,893	5,933
Investments and Other Assets		
Investments in and advances to unconsolidated affiliates	4,779	4,433

Assets from price risk management activities	2,364	1,941
Goodwill	2,696	1,949
Other	5,599	4,437
Total Investments and Other Assets	15,438	12,760
Property, Plant and Equipment, at cost	17,507	15,792
Less accumulated depreciation, depletion and amortization	5,691	5,135
Net Property, Plant and Equipment	11,816	10,657
Total Assets	$34,147	$29,350

<FN>
The accompanying notes are an integral part of these consolidated financial statements.
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<PAGE>
<TABLE>

PART I. FINANCIAL INFORMATION - (Continued)
ITEM 1. FINANCIAL STATEMENTS - (Continued)
ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET
(In Millions)
(Unaudited)

<CAPTION>

	June 30, 1999	December 31, 1998
LIABILITIES AND SHAREHOLDERS' EQUITY		
<S>	<C>	<C>
Current Liabilities		
Accounts payable	$ 2,603	$ 2,380
Liabilities from price risk management activities	2,386	2,511
Other	1,457	1,216
Total Current Liabilities	6,446	6,107
Long-Term Debt	8,979	7,357
Deferred Credits and Other Liabilities		
Deferred income taxes	2,352	2,357
Liabilities from price risk management activities	2,068	1,421
Other	1,620	1,916
Total	6,040	5,694
Minority Interests	2,475	2,143
Company-Obligated Preferred Securities of Subsidiaries	1,001	1,001
Shareholders' Equity		
Second preferred stock, cumulative, no par value	131	132
Series A Junior Voting Convertible Preferred		

Stock, no par value	1,000	-
Common stock, no par value	6,588	5,117
Retained earnings	2,369	2,226
Accumulated other comprehensive income	(760)	(162)
Common stock held in treasury	(1)	(195)
Other	(121)	(70)
Total	9,206	7,048
Total Liabilities and Shareholders' Equity	$34,147	$29,350

<FN>
The accompanying notes are an integral part of these consolidated financial statements.
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PART I. FINANCIAL INFORMATION - (Continued)
ITEM 1. FINANCIAL STATEMENTS - (Continued)
ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS
(In Millions)
(Unaudited)

<CAPTION>

	Six Months Ended June 30, 1999	1998
<S>	<C>	<C>
Cash Flows From Operating Activities		
Reconciliation of net income to net cash provided by (used in) operating activities		
Net income	$ 344	$ 359
Cumulative effect of accounting changes	131	-
Depreciation, depletion and amortization	451	372
Oil and gas exploration expenses	45	60
Deferred income taxes	(11)	60
Gains on sales of assets and investments	(65)	(32)
Changes in components of working capital	(909)	(660)
Net assets from price risk management activities	247	(253)
Merchant assets and investments:		
Realized gains on sales	(161)	(252)
Proceeds from sales	561	629
Additions	(490)	(282)
Other operating activities	(181)	(252)
Net Cash Used in Operating Activities	(38)	(251)
Cash Flows From Investing Activities		
Capital expenditures	(969)	(585)
Equity investments	(648)	(151)
Proceeds from sales of investments and other assets	138	58
Acquisition of subsidiary stock	-	(180)
Business acquisitions, net of cash acquired	(40)	(25)
Other investing activities	(340)	(254)
Net Cash Used in Investing Activities	(1,859)	(1,137)

Cash Flows From Financing Activities		
Issuance of long-term debt	1,301	305
Repayment of long-term debt	(645)	(341)
Net increase in short-term borrowings	128	769
Issuance of common stock	889	844
Issuance of subsidiary equity	513	-
Dividends paid	(227)	(204)
Net disposition of treasury stock	181	7
Other, net	(68)	13
Net Cash Provided by Financing Activities	2,072	1,393
Increase in Cash and Cash Equivalents	175	5
Cash and Cash Equivalents, Beginning of Period	111	170
Cash and Cash Equivalents, End of Period	$ 286	$ 175
Changes in Components of Working Capital		
Receivables	$ (644)	$(1,345)
Inventories	(37)	(155)
Payables	120	691
Other	(348)	149
Total	$ (909)	$ (660)

<FN>
The accompanying notes are an integral part of these consolidated financial statements.
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PART I. FINANCIAL INFORMATION - (Continued)

ITEM 1. FINANCIAL STATEMENTS - (Continued)
ENRON CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The consolidated financial statements included herein have been prepared by Enron Corp. (Enron) without audit pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, these statements reflect all adjustments (consisting only of normal recurring entries) which are, in the opinion of management, necessary for a fair statement of the financial results for the interim periods. Certain information and notes normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although Enron believes that the disclosures are adequate to make the information presented not misleading. These consolidated financial statements should be read in conjunction with the financial statements and the notes thereto included in Enron's Annual Report on Form 10-K for the year ended December 31, 1998 (Form 10-K).

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of

Unknown

From: Reilly, James F [IBD]
Sent: Monday, October 08, 2001 10:23 AM
To: Fox III, William T; 'michael.nepveux@citicorp.com'
Cc: Junek, Lydia G
Subject: RE: Enron

Bill: I am not sure that it is conflicting or inconsistent. they are distinct answers to different questions. i assume that your question was asked and answered in a "relationship" context - turning it down is not a relationship event. it is of greater gravity to the enron deal team handling any given transaction. in the enron system, the deal guys are able to horse-trade, particularly among their own deals. again, the game may be over but: would you do brazos now for 15mm if it would return us to the ABS competition?

also: in this same vein, i hear that glisan told you there was no need for us to do the Azurix Europe RC. the deal team again has a different perspective - if the RC is accelerated, we could face the yes/no decision while enron still holds back the azurix restructure mandate. even if the RC is pushed back, it is likely that the deal team will make us testify to participation before awarding AZX.

-----Original Message-----
From: Fox III, William T
Sent: Monday, October 08, 2001 7:54 AM
To: Reilly, James F [IBD]; 'william.fox@citicorp.com'; 'michael.nepveux@citicorp.com'
Cc: Verme, Alberto J [IBD]; Hendricks, Maureen A [IBD]; Keller, Dean [IBD]; Junek, Lydia G
Subject: RE: Enron

Seems we might be getting some conflicting feedback from Enron.

With respect to Brazos I specifically visited with Glisan several weeks ago before the $200mm request was on the table saying that we had some issues with Brazos such that we would prefer not to participate but I wanted feedback from him as to how important it was to them and that we would have to look at it as a " trust me, Enron relationship deal ". He said he would prefer not to do "trust me " deals and he would get back to me. He has not.

Also at same meeting questioned him on what he had " scheduled" for us for remainder of year. Never mentioned the recent prepaid. Said he had us "earmarked" for $400mm conduit funding for Project X with Deutche doing $1B placed either publicly and/or privately not yet fully determined. Also said had CIBC earmarked to do $500mm ABS deal - not sure whether this was/is Popeye.

In any event some conflicting feedback that we need to get resolved. We still have the existing $250mm prepaid to deal with for which they still "owe" us one for having provided the $250mm originally. Joint call on Glisan/Fastow appropriate.

-----Original Message-----
From: Reilly, James F [IBD]
Sent: Monday, October 08, 2001 7:47 AM
To: 'william.fox@citicorp.com'; 'michael.nepveux@citicorp.com'
Cc: Verme, Alberto J [IBD]; Hendricks, Maureen A [IBD]; Keller, Dean [IBD]; Reilly, James F [IBD]
Subject: Enron

Last week, we were informed by enron that we had not been selected to arrange either project X (monetize contract values in their price risk book) or project popeye (public ABS based on trade receivables). Each are potentially precedent-setting and lucrative deals.

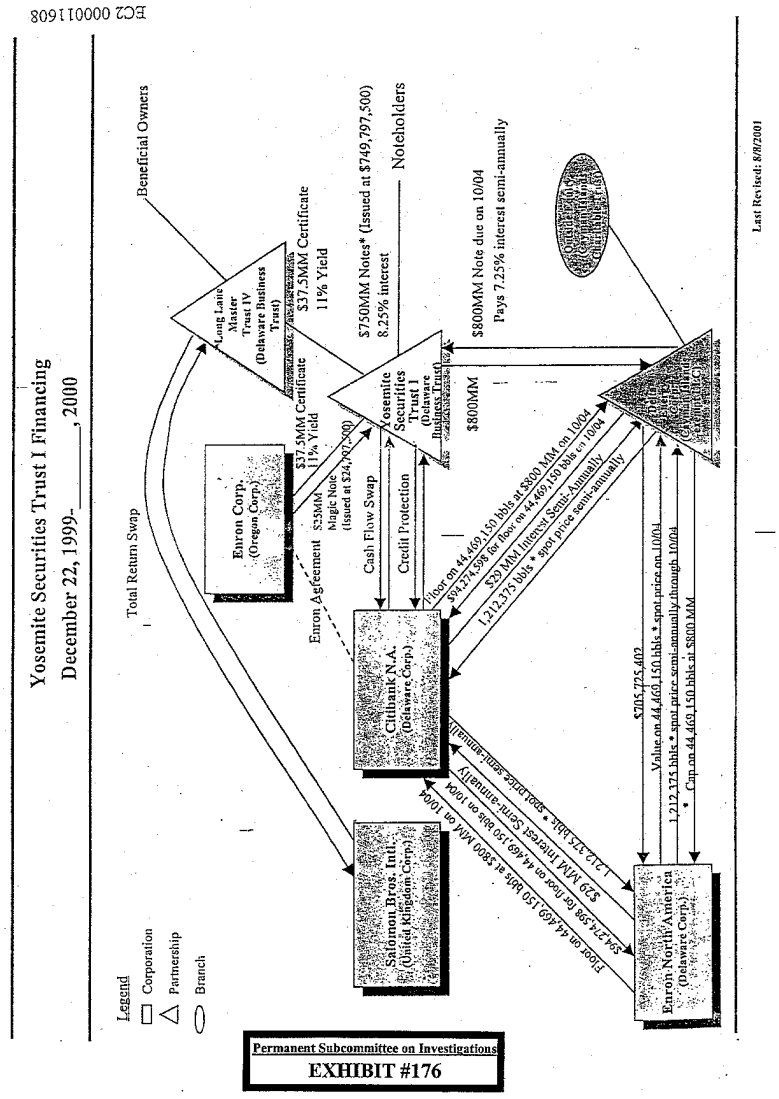
1

Permanent Subcommittee on Investigations
EXHIBIT #175

In the case of X, it appears that we were beaten by a aggresive bid from a competitor. However, with popeye, we were told that it was a result of our rejection of a 15mm participation in the brazos production-payment financing. Brazos was a difficult BofA syndication which enron asked us to aid late in the transaction. It was handled by the same enron person in charge of popeye. He was surprised by our decision and our vocal criticism of the deal. Chase, and others, did participate based on the enron call to help.

I believe it is too late to save popeye, but could we reconsider brazos in an attempt to get back into the ABS hunt?

Also: chase and csfb did provide prepaids at the end of the last quarter - csfb replacing us when we rejected the 200mm request. While csfb MAY have slightly less exposed to enron, the chase position is comparable to ours.



Permanent Subcommittee on Investigations
EXHIBIT #176

Unknown

From: Swanson, Timothy [FI]
Sent: Monday, June 25, 2001 6:02 PM
To: Forese, James A [FI]
Cc: Wagman, Steve [FI]; Deards, Paul B [FI]
Subject: Prepaid Overview

Attached is a page that depicts a summary of the enron prepaid and the accounting treatment

prepaidsummary.doc (40 KB)

Tim Swanson
Derivatives Capital Markets

SALOMON SMITH BARNEY
A member of citigroup

390 Greenwich Street
New York, NY 10013
ph. (212)-723-6504
fax (212)-723-8610

Permanent Subcommittee on Investigations
EXHIBIT #177

Summary of Pre-Paid Accounting and Tax

Bullet

Cash Flows	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
CF from Ops	500	0	0	0	0	-500
CF from Financing	-500	0	0	0	0	500
	0	0	0	0	0	0
Balance Sheet						
Debt	-500	0	0	0	0	500
Price Risk Management Liability	500	0	0	0	0	-500

Cash Flow from Ops increase on Day 1, and reverse at maturity.

Debt decreases on Day 1, and returns at maturity. Price Risk Management Liability increases on Day 1, and reduces in full at maturity.

Amortizing

Cash Flows	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
CF from Ops	500	-100	-100	-100	-100	-100
CF from Financing	-500	100	100	100	100	100
	0	0	0	0	0	0
Balance Sheet						
Debt	-500	100	100	100	100	100
Price Risk Management Liability	500	-100	-100	-100	-100	-100

Cash Flow from Ops increase on Day 1, and reverse over time.

Debt decreases on Day 1, and returns over time. Price Risk Management Liability increases on Day 1, and is undone over time.

* We have assumed that benefits mature in Year 5 for the bullet, and over time in the amortizing example.

- As we understand the accounting, the Pre-Paid creates price risk management liability, thereby receiving non-"D" debt treatment
- Operating cash flow increases, helping to offset the current "disconnect" between book and cash earnings
- While we have assumed that benefits undo by Year 5, the benefits may be continued by refinancing with another Pre-Paid

TAX ISSUES

- From a tax perspective, the Pre-Paid can be treated much like a traditional loan
  - Swap payments are deductible on the tax books, similar to loan payments

Error! AutoText entry not defined.

citigroup Corporate & Investment Bank

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CITI-SPSI 0050681

Unknown

From: Fox, William
Sent: Wednesday, April 18, 2001 4:29 PM
To: Stott, Thomas
Subject: Enron Credit Approval

As you know Enron is pressing us to go to market with the renewal and increase of their flagship RC as well as the increase in the Rawhide transaction. The existing deal expires May 16 and Rawhide needs to be resolved by April 30. There is no question that Enron cashflow has become more dependent on Price Management Activities. For 2000 EBIT from PRM was $1.9B up $1B from 1999. Nevertheless, they still have substantial fixed assets, non PRM cashflow and substantial capital: $22B; $1.7B; and $12.5B respectively. As you know we are committed to undertake an indepth review of all the energy marketing companies including the use of outside accounting and technical advisors to deal with transparancy and PRM accounting.. This should be completed by mid/end of May. At that time we can make an informed judgement as to how much exposure we want with these clients, on what basis, and how we should mange any transition/change going forward. As part of this review Enron as in the past will be more than willing to review with all interested Citi parties their PRM strategies and risk management process. Enron generates substantial GCIB revenue ($50mm in 2000); any decision to limit/reduce credit availability will significantly reduce revenues going forward both at Citi and SSB and permanently impair the relationship. Let's discuss.

Further to the Enron approval memo total OSUC to Enron is $795mm broken down as follows:

$200mm - Bacchus: SPV where we have a total return swap from Enron for $180mm and verbal support for the balance
100mm - Enron 364 day RC
100mm - Rawhide: SPV consisting of both 100% Enron notes and merchant assets
75mm - Turbo Park: synthetic lease (ADP) on series of gas power plant turbines; 85% Enron guaranteed
54mm - Yosemite 1,2: CLN structure with 100% Enron risk through prepaids
42mm - Enron Funding: SPV with Enron guaranty and AAA insurance company credit wrap
41mm - Dabhol: power plant project financing in India
30mm - JT Holdings: ADP on gas liquids assets with 85% Enron guarantee
25mm - Garden State: loan against paper assets with verbal support of Enron
24mm - Nahanni: SPV 100% supported by US Tres. bills
10mm - JEDI II: SPV consisting of Enron oil & gas properties
6mm - Coal Monetization: coal contract monetization from Houston Lighting & Power (Reliant)
68mm - misc PSR
20mm - misc facilities

Recommend that we approve the two requests at hand. They are 100% Enron risk with the RC being a 364 day facility.

CITI-SPSI 0085843

Permanent Subcommittee on Investigations
EXHIBIT #178

Unknown

From: Fox III, William T
Sent: Monday, October 01, 2001 8:47 AM
To: Verme, Alberto J [IBD]; Hendricks, Maureen A [IBD]; Keller, Dean [IBD]; Reilly, James F [IBD]; Nepveux, Michael W; Clarke Woiff, Anne [FI]
Cc: Stott, Thomas D [CRRM]; Junek, Lydia G
Subject: Enron

Spoke with Fastow; he had two questions: 1) do we have incremental debt capacity available for Enron in the 4th quarter; 2) confused by conflicting messages: turndown of the prepaid request and willingness to fund a significant overdraft to meet CP maturities following September 11.

With respect to #1 reiterated what I told Glisan: if existing $250mm prepaid was paid off and capital markets outlook was positive for a refinancing we would have debt capacity; with respect to #2: CP rollover was clear financial need in a difficult time while the prepaid was an accounting need in a difficult time and we differentiated between the two.

Talked about need for continuing dialog particularly our appetite for additional Enron paper during the quarter; will arrange meeting after release of financials for detailed review. No comment on bond issue but now thinking November; if market is receptive prior we should provide input; we should assume we continue to have sole books.

Jim, Michael need to find out if and how they did the prepaid.

Permanent Subcommittee on Investigations
EXHIBIT #179

Unknown

From: Kirk, Niels C. [Niels C Kirk /70EULON] on behalf of Kirk, Niels C.
Sent: Wednesday, November 10, 1999 11:33 AM
To: Beldam, Rufus
Subject: FW: Yosemite II (Europe)

I spoke to Jim. Its quite clear that we do not have the capacity to do an extra $250 $200 MM over year-end.

Chivers left me another e-mail today hinting at a push towards the bridge. I intend to counter with arranging the bridge through Japanese Canadians. Chivers also hinted at a complicated fee discussion which I'm not in the mood for either.

Niels

-----Original Message-----
From: Reilly, James F
Sent: Tuesday, November 09, 1999 10:51 PM
To: Kirk, Niels C
Subject: Re: Yosemite II (Europe)

Niels: Same as my voicemail (if you have had the chance to listen to it): We are in no position to take on a $250MM underwriting across 12/31/99. Several points: 1) With the paydowns from Yosemite, we are going to be under our Obligor Limit for the first time in years - I have been encouraged, from a risk point of view, to try to stay in compliance in the near term; 2) Even with #1 as a caution, we are working a $500MM Capital Structuring deal that must be closed and will require an underwriting - we are still determining the extent of our exposure; 3) To even consider any bridge, we would need some feedback from Capital Markets - likelihood and timing of ultimate deal, compensation, etc - I do not have that certainty as yet - I am told that we will not have that feedback until next week following preliminary talks with investors in London; 4) Ultimately, we could be seen as "bailing out" the banks in the European RC - why would they allow that deal to lapse?

We have not been approached by Enron HQ regarding any bridge - that makes expectations hard to manage unless we want to stir things up. It is equally critical, maybe moreso at this point, to manage the expectations of Enron Europe.

_____ Reply Separator _____
Subject: Yosemite II (Europe)
Author: Niels C. Kirk at 70EULON/o=AF1/c=US/a=MCI/p=CITICORP
Date: 11/05/1999 1:19 PM

Bill/Jim,

Just a quick heads-up.

Enron Europe are proposing that Yosemite II be arranged for GBP 175/200 MM. They need this by year-end as the deal generates count as operational funds flow which will evidently fill a gap left by certain European projects/contracts.

Coincidentally, their $250 MM corporate 364 day R/C (which is fully drawn) matures next week. Enron to repay from corporate

Permanent Subcommittee on Investigations
EXHIBIT #180

CITI-SPSI 0073053

funds, but it appears that the proceeds from Yosemite II are earmarked for reimbursement of the corporate funds.

Chivers has begun to make noises about Citi stepping up and bridging the deal in the event that the capital markets fail us. My response to date has been non-committal, especially as Yosemite is still in prototype mode and typical of Enron they are already in replication mode. I'm concerned that the capital markets may close before we can get the structure away, then we could be left holding the bag.

SSB London have approached certain investors and we are waiting for their feedback. I understand that other "roadshows" are contemplated for London and Scotland in the near future. Also there is a structuring session slated for next week in New York.

So the question is, where do we stand on Enron credit capacity? Is there any room for $250/$300 MM over year-end? If not, would it be feasible (from a practical and structuring point of view) to arrange a we arrange a bridge for say Japanese or Canadian only banks (their year-end is different)?

Please advise. If we have no more capacity, please begin to manage Enron HQ expectations.

Niels

>
> I called Chivers and reiterated our concern over the manner
> in which he's pushing Yosemite II and the "bridge" on us
> (especially given the fact that we (and Houston for that
> matter) still don't know if there's a deal). He understood
> and knows, that we know, he's trying to jam us (such
> is life...).
>
> Anyway I covered our four points:
>
> 1. Next week is very important. We can't even say whether
> this is a bridge or a prepaid pier until we know the market.
>
> 2. What's Enron's threshold on the spread?
>
> 3. If we were to do a club deal on a bridge, how many banks
> does Enron think they could deliver? Why is Enron against
> clubbing the bridge?
>
> 4. There could be a chance of ST booking the deal in one of
> our European conduit vehicles (as done previously in the US)
> but this still needs to be explored and it could be pricey
> given that Enron's goal is to go LT (25+ years).
>
> Chivers was unable to answer the questions above but stated that
> my (our) reaction/response was valid and productive.
>
> Niels
>
>
> -----Original Message-----
> From: Fox, William
> Sent: Wednesday, November 10, 1999 5:56 PM
> To: Fox, William; Kirk, Niels C.; Reilly, James F.
> Subject: RE: Yosemite II (Europe)
>
> Just to make it clear: no room to bridge.
>
> -----Original Message-----
> From: Fox, William
> Sent: Wednesday, November 10, 1999 12:50 PM
> To: Fox, William; Kirk, Niels C.; Reilly, James F.
> Subject: RE: Yosemite II (Europe)
>
> In spite of all the repayments we have/will receive from Condor and
> Yosemite we
> still have an exposure issue as it relates to obligor limits; there is a
> developing view that limits are limits and not to be exceed. This is
> something
> we will all have to deal with. Also we do not have room for incremental
> assets
> of $200-300mm over year end. Iwill discuss with Reilly later today for
> current
> status and review of options.
>
> -----Original Message-----
> From: Kirk, Niels C.
> Sent: Friday, November 05, 1999 1:20 PM
> To: Fox, William; Reilly, James F.
> Subject: Yosemite II (Europe)
> Importance: High
>
> Bill/Jim,
>
> Just a quick heads-up.
>
> Enron Europe are proposing that Yosemite II be arranged for
> GBP 175/200 MM. They need this by year-end as the deal

Permanent Subcommittee on Investigations
EXHIBIT #181

> generates count as operational funds flow which will evidently
> fill a gap left by certain European projects/contracts.
>
> Coincidentally, their $250 MM corporate 364 day R/C (which is
> fully drawn) matures next week. Enron to repay from corporate
> funds, but it appears that the proceeds from Yosemite II are
> earmarked for reimbursement of the corporate funds.
>
> Chivers has begun to make noises about Citi stepping up and
> bridging the deal in the event that the capital markets fail us.
> My response to date has been non-committal, especially as
> Yosemite is still in prototype mode and typical of Enron they
> are already in replication mode. I'm concerned that the capital
> markets may close before we can get the structure away, then
> we could be left holding the bag.
>
> SSB London have approached certain investors and we are waiting
> for their feedback. I understand that other "roadshows" are
> contemplated for London and Scotland in the near future. Also
> there is a structuring session slated for next week in New York.
>
> So the question is, where do we stand on Enron credit capacity?
> Is there any room for $250/$300 MM over year-end? If not, would
> it be feasible (from a practical and structuring point of view) to
> arrange a we arrange a bridge for say Japanese or Canadian only
> banks (their year-end is different)?
>
> Please advise. If we have no more capacity, please begin to
> manage Enron HQ expectations.
>
> Niels
>
> << File: MAPI-1 Distribution List.TXT >>
>

RE_ Yosemite II (Europe).TXT

Kirk, Niels

From: Riggall, Simon [Simon Riggall /61EULON/o=AF1/c=US/a=MCI/p=CITICORP]
Sent: 16 November 1999 16:26
To: Gibson, Suzanne; Riggall, Simon; Kirk, Niels C.; Reilly, James F.; Zaman, Sikander; Elliston, Simon
Cc: Streamer, Sarah
Subject: RE: Enron in West Africa

Thanks. Jeff called me today and we are trying to arrange a time to meet. Rgds

-----Original Message-----
From: Gibson, Suzanne
Sent: 15 November 1999 16:49
To: Riggall, Simon; Kirk, Niels C.; Reilly, James F.; Zaman, Sikander; Elliston, Simon
Cc: Streamer, Sarah
Subject: Enron in West Africa

Had a call from Jeff Forbis at Enron in Houston. He had got my name from a colleague with whom we looked at several Central European opportunities some time ago. As he described it, he is trying to get a handle on financing alternatives for West African projects (as I understood his focus -- on the power side). He said he didn't have a particular deal in mind at the moment, but wanted to hae a discussion on what is possible/financeable.

He would like to speak to someone both from a project finance and a

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Francois, Tom

From: Lofaso, Betty Ann on behalf of Sullivan, William A
Sent: Friday, September 03, 1999 2:43 PM
To: Kulick, Adam; Warren, Doug; Caplan, Rick
Cc: Francois, Tom
Subject: RE: Yosemite

Sent on behalf of William Sullivan

Adam - to respond to your August 30, 1999 questions:

1) My only concern is non-bankruptcy events of default, e.g. Enron stops paying on the Enron-SPV swap, but is not bankrupt. We would still want to terminate the price risk at the same time, etc. There should be a way to do this within Enron's accounting concerns. Maybe we can set up a call to discuss.

2) If we are the only lender to the SPV, these concerns go away, I assume.

3) The Roosevelt deal was funded in Charta; I will see what we did there, and it can probably work the same way when funded directly by the Bank.

Regards,

Bill Sullivan
Tel. 212-816-8591
Fax 212-816-7772
email: william.a.sullivan@ssmb.com

From: Sullivan, William A
Sent: Friday, September 03, 1999 12:27 PM
To: Lofaso, Betty Ann
Subject: FW: Yosemite

From: Kulick, Adam
Sent: Monday, August 30, 1999 2:59 PM
To: Caplan, Rick; Warren, Doug; Sullivan, William A
Cc: Francois, Tom
Subject: RE: Yosemite

Bill,

Some questions and comments:

1) Cross-termination between the Enron-SPV deals and the Citi/Enron floor would cause Enron accounting problems. Can we take comfort on termination timing from automatic termination of the trades on the petition date?

2) How can we give the SPV and its lenders comfort on trigger events for our early termination? How about we link the early termination date to a bankruptcy of Enron?

3) I imagine the banks would want a pledge of the assets of the trust including the rights under the Citi floor and the Enron obligation - what do you suggest here?

Permanent Subcommittee on Investigations
EXHIBIT #182

Regards,

AK

From: Lofaso, Betty Ann on behalf of Sullivan, William A
Sent: Monday, August 30, 1999 12:10 PM
To: Kulick, Adam; Caplan, Rick; Warren, Doug
Cc: Francois, Tom
Subject: Yosemite

Sent on behalf of William Sullivan

On the revised funded prepaid structure (now USD 750MM):

- in the Citi-SPV floor: an additional Termination Event if either the Citi-Enron floor or the Enron-SPV swap terminates for any reason, as of the date of such termination.

- in the SPV-Enron swap: Citi shall have the ability to designate an Early Termination Date. We would need this to be a term of the swap.

- I agree that on the bankruptcy event of default should be "automatic" even though not our standard approach.

- in the Citi-SPV deals, we should specifically allow for set-off between the floor and the Note.

- will the Banks, including us, who fund the SPV need a pledge from the SPV of its rights to receive under the swap and the floor? Or is it enough that the SPV is bankruptcy remote and can't do anything else?

Regards,

Bill Sullivan
Tel. (212) 816-8591
Fax (212) 816-7772
email: william.a.sullivan@ssmb.com

CONFIDENTIAL

Lee, Andrew P [FIN]

From: Caplan, Rick [FI]
Sent: Thursday, August 31, 2000 9:07 AM
To: Lee, Andrew P [FIN]
Subject: RE: A couple of more questions

We still would have to consolidate as all of the assets of the trust are citibank assets. Delta is not controlled by Enron, it is independently operated, set up with its own management - Citi had set it up several years ago. It was used for the same reason it was used in the first deal.

-----Original Message-----
From: Lee, Andrew P [FIN]
Sent: Wednesday, August 30, 2000 5:03 PM
To: Caplan, Rick [FI]
Subject: A couple of more questions

Hi Rick,

This will seem like a dumb question but was it not possible to have Enron (or some other party) buy 50% of the certificates as in the earlier Yosemite trades in order to avoid having to consolidate the trust? (I guess it doesn't have that much of an affect on the overall Citibank balance sheet but it does appear to affect the one for credit derivatives).

Also, is Delta Energy a Cayman-based SPV controlled by Enron? Why was it used in this deal? (We tried looking for information in Eric Pipa's old files but weren't able to come up with much.)

Thanks,
Andy

Permanent Subcommittee on Investigations
EXHIBIT #183

TRANSCRIPT OF TAPED TELEPHONE CALL

Telephone call among JPMorgan Chase employees Mr. Jeffrey Dellapina, investment banker; Mr. Robert Traband, corporate banker; and Mr. James Ballentine, credit department.

September 20, 2001
Conversation began at 1:40 pm

Identification of the speakers with the text is based on the Subcommittee staff's best judgment.

MR. BALLENTINE: Jeff, why do they want to hedge with gas where it is now?

MR. DELLAPINA: They're not hedging, they're just, they're just, they do the back-to-back swap. This is--

MR. TRABAND: This is a circular deal that goes right back to them.

MR. DELLAPINA: It's basically a structured finance--

MR. BALLENTINE: It's a financing?

MR. DELLAPINA: Yeah, it's totally a financing, which has piece of it, they've always had on as a piece of their capital structure, so--

MR. BALLENTINE: Yeah.

MR. DELLAPINA: So, if it reduces 500 a year--

MR. BALLENTINE: Yeah.

MR. DELLAPINA: --they have to do something with it, which is swap back.

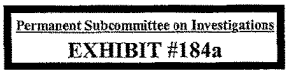
MR. BALLENTINE: So it's amortizing. Yeah, it's amortizing debt. I get it.

MR. DELLAPINA: That's exactly what it is.

MR. BALLENTINE: Rob, do we include this debt in our credit stats?

MR. TRABAND: No, we don't. It fits into their trading book and so, you know, effectively they've got, you know, it's monetizing assets from price risk management.

Prepared by U.S. Senate Permanent Subcommittee on Investigations, July 2002



TRANSCRIPT OF TAPED TELEPHONE CALL

Telephone call among JPMorgan Chase employees Mr. Jeffrey Dellapina, investment banker; Rob (believed to be Mr. Robert Traband, corporate banker); George (believed to be Mr. George Serice, investment banker); and Enron North America employees Mr. Joseph Deffner, Chief Financial Officer; Ms. Lisa Bills, finance department; and Mr. Michael Garberding, finance department.

September 13, 2001
Conversation began at 10:08 am

Identification of the speakers with the text is based on the Subcommittee staff's best judgment.

MR. DEFFNER: Okay. And, Jeff, one additional thing Andersen is throwing back is, when we confirm the deal this go-around--

MR. DELLAPINA: Yeah?

MR. DEFFNER: --I think they want us confirming it, if I'm not mistaken, with Mahonia, the Mahonia letter; is that right? Lisa, you're more familiar with the--or Mike?

MR. GARBERDING: You're talking about the rep letter from Mahonia, basically, I think we talked about this before, saying, you know, it has the right to do transactions like this. Before what we've done is just really looked at the actual charter, and you've got the information, but now Andersen is pushing back and saying, hey, we need to have a specific rep letter that a representative of Mahonia signed that reps a certain point.

MS. BILLS: Which is, yeah, separate from Chase. It doesn't have Chase showing up anywhere on the fax letterhead or anything along those lines, a separate fax number, et cetera.

MR. DELLAPINA: Oh, Okay, lets talk about it, yeah.

MR. DEFFNER: That goes to the same point you were raising earlier, Jeff, that from your side, you also want to make sure that Mahonia seems independent.

MS. BILLS: If it helps, Jeff, we can get you a copy of what they're asking.

MR. DELLAPINA: Yeah. I mean, of course, we're going to have to get that, sure, eventually.

MS. BILLS: Okay.

TRANSCRIPT OF TAPED TELEPHONE CALL

Telephone call among Mr. Jeffrey Dellapina, investment banker, JPMorgan Chase; and Enron North America employees including Michael (believed to be Mr. Michael Garberding, finance department); Mr. Brian Kolle, finance department; Mr. Eric Boyt, gas structuring; and Kelli Little, gas structuring.

October 3, 2001
Conversation began at 2:12 pm

Identification of the speakers with the text is based on the Subcommittee staff's best judgment.

MR. GARBERDING: . . . I've talked to our logistical people on several occasions, and we've talked to the Transco rep, for example, saying, you know, what if we did want to do it at one location and try to move three-and-a-half bcf to a point where there really only is capacity physically for two.

MR. DELLAPINA: Yeah.

MR. GARBERDING: Well, you know, it may raise a red flag, but technically you've got to be able to do it because it's a circle that comes--

MR. DELLAPINA: True.

MR. GARBERDING: --you're the first purchaser or first provider, and it comes right back to you, so the pipes should just be able to confirm it either way, but it probably would be a little bit cleaner, as long as we can all agree upon the points and locations, and if we're all comfortable with no fees.

MR. DELLAPINA.: Yep. Yep. We've done it before. I'm pretty confident we'll get there.

MR. GARBERDING: Okay.

United States Senate
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS
Committee on Governmental Affairs

Carl Levin, Chairman
Susan M. Collins, Ranking Republican

TRANSCRIPTS OF SELECTED JPMORGAN CHASE AUDIO TAPES

Permanent Subcommittee on Investigations
EXHIBIT #184c

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T2243

1

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collpase of Enron

Dellapina, (AT) 015

September 5, 2001

9:07:34

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

nr 2

P R O C E E D I N G S

MR. : This is Jeff.

MR. BALLENTINE: Jeff. Ken Ballentine.

[Audio break.]

MR. : The other day I called him for an approval. He was just yelling at me. I'm like, "Jim, I'm not even asking you about this."

MR. : Well, I know that Enron is. So --

MR. : Yeah. You heard about that. Yeah.

MR. : Yeah. Traband called me yesterday.

[Audio break.]

MR. : Are you around on Friday?

MR. : Yeah.

MR. : Maybe make a pencil mark on Friday afternoon.

MR. : Yeah.

MR. : Because I think we should, at long last, sit and go through the work that Peter did--

nr

MR. : Yep.

MR. : --on the sureties and get educated.

MR. : Yep.

MR. : Get me educated, anyway.

MR. : Good.

MR. : All right. So I'm going to mark that down and hopefully we can do that on Friday, and I don't know. Is Enron like looking to do something like this week or?

MR. : I think this month. You know, basically, what they're doing is they're trying to roll over what's run off this year.

The runoff is enormous. It's 550 million a year.

MR. : Yeah.

MR. : Because you've probably got about one-point--actually, you want me to show you--I'll show you the chart that shows what their runoff is.

MR. : Yeah.

MR. : I can e-mail that up to

nr

you, but.

MR. : Okay.

MR. : And that's what they're trying to do is replace that. I don't think there's any chance in hell that we're going to go for that, because it will reduce--

MR. : I agree.

MR. : I mean, I'm not--I don't have any--

MR. : I agree.

MR. : But is there another way to do it? I don't know.

MR. : Yeah.

MR. : I mean, but I think--but the credit default swap market for them is off the chart.

MR. : I know. [Audio break] then Enron, just because I think Enron's number is gaudy.

MR. : Yeah.

MR. : And, you know, subject to criticism.

nr

5

MR. : Yeah, yeah, yeah, yeah.

MR. : If we put more exposure on there.

MR. : Yep.

MR. : But--

MR. : We'll talk about it.

MR. : Yeah. We need to.

MR. : All right. Good.

MR. : All right. Good.

MR. : I'll pencil in Friday and I'll get Lea to send you the stuff right away.

MR. : Great. Thanks, Jeff. See you.

MR. : Bye.

[END OF TAPE RECORDING.]

- - -

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T2243

1

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 017

September 12, 2001

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

nr 2

P R O C E E D I N G S

MR. : You know, we never got back and I was talking to Traband yesterday morning, like 8:30, the day before, about, you know, getting back to Enron.

So I'm fairly pessimistic in our ability to do much with them right now.

MR. : Yeah. I know. That's why I called. I'm just pulling into the garage. Let me call you back in about five or ten, if that's okay.

MR. : No. Take your time.

MR. : Because that's exactly what I wanted to talk about, number one. Well, I've got a couple minutes [?].

MR. : Because I'll tell you what. I think if I'm Enron now, unfortunately, right, wrong, or indifferent, if your view is these guys, they could quietly access capital, they'll just pay whatever the hell it takes, because the last thing they want to do is have to go start doing bond deals now, right?

MR. : Yeah.

MR. : And, you know, maybe there are things we could do that are even outside of the default market.

Like one idea I had is why can't we structure a deal where we're effectively shorting their bonds.

We're covering the borrowing cost of the bonds and then we're shorting them. So it doesn't really get into the default swap market, but that might--the costs may be about the same.

I don't know. I mean, if they don't see it and, you know, maybe they do a deal that's a one or two-year [?].

MR. : I'm not sure I quite understand that, but one of the things that I'm mentioning to Rob that makes some sense to me is, you know--you know, honestly, I don't mean to sound opportunistic because of, you know, everything yesterday, but, you know, liquidity is going to become that much more of a premium commodity here.

MR. : Yeah.

nr 4

MR. : Pretty soon and, you know, I think that, you know, we want to--I mean, A, we want to do the right thing as corporate citizens, and, B, do the right thing by the right clients.

MR. : Yeah.

MR. : And maybe the answer is, you know, we can't do a five-year, 350--350 million dollar deal. We can do you a one-year deal for 250, so you got to blow it down really quick.

MR. : Yeah.

MR. : And we'll just do it.

MR. : And we'll charge [audio break] out of it.

MR. : Right.

MR. : Now, quite frankly, I don't think we can get there unless we get protection.

MR. : Yeah.

MR. : I don't even think--even if we could talk about the insurance issue right now in terms of they hate--you know, they're stubborn about this issue [audio break] him and

nr 5

Chris, but the bottom line is the insurance company [audio break] right now. So they're going to--

MR. : Right. That's exactly right.

MR. : I mean, we're talking already ten to fifteen billion dollars of insurance paying through workman's comp, through, you know, deaths, [audio break], property. It's going to be brutal.

So I think it's how do we, as efficiently as possible for the client, get protection on this, you know.

MR. : Right.

MR. : Some of it might be participation, paying a premium to participate, and some of it, maybe we can do some other stuff, you know. Let's [audio break] about it.

But I think you're right. I think you're absolutely right, Rick. I mean, forget about the cheap money, but if you want to quietly get a deal done, where you don't have to go to public markets, this is what we always said we would do.

Pay--pay--you got to pay us large, but we'll do it.

MR. : Right.

MR. : And for 250 million bucks for these guys right now, do they really want to--you guys are struggling syndicating normal stuff, aren't you?

MR. : Yeah. That's right.

MR. : So I would--I would tell them like they should tell us like this week go do whatever you have to do, it'll cost me 25 basis [audio break.]

MR. : [?] low now. I mean, you're still talking about--

MR. : Two [?], what, 360 basis--you know, 3.6 percent.

MR. : Yeah. The other thing, just on our group call this morning, you know, we were talking about, well, what are some--what are some revenue opportunities, you know, that we really ought to pick up the stick on between now and the end of the year.

nr 7

MR. : Yeah.

MR. : And yeah. So there were some--you know, some derivative kind of stuff, you know, bond call monetizations and a couple other things.

And I threw out, you know, the pre-paid product as one, you know, that, you know, certainly, this--certainly, the atmosphere has changed, but, you know, Eric was kind of like, "Yeah, we definitely ought to think about that."

I said, "Yeah. I think the challenge is going to be, you know, Enron's, you know, the most--the most exacerbated challenge, you know, because of our exposure and their exposure on the market," yada, yada, yada, but, you know, we ought to sort of think about, you know, who are--who are five people that we can go out and really push this on, you know, somebody like Dominion right now, with all the Louis Dreyfus natural gas reserves.

MR. : Well, right after that announcement came out, I sent a note to--I sent a note to Fornal [ph] and copied like Cerese [ph],

nr

8

because both our Geronimo VTP products and prepays for them are [audio break] genius for them.

I mean, they're totally leveraged. They're getting leveraged, right?

MR. : Right.

MR. : You're absolutely right. No. Thanks for sponsoring that. How should we follow up? Should we--

MR. : Well, let me get up the elevator and, you know, within half an hour, I'll call you back and--

MR. : All right. Bye. Bye.

MR. : And we'll make--

[END OF TAPE RECORDING.]

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 51 [1 of 2]

September 13, 2001

10:08:34

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : --really, really smart.

MR. : Hey, what's up?

MR. : Hey, man.

MR. : What's up?

MR. : I was just practicing my best [inaudible].

MR. : Exactly.

MR. : What's going on?

MR. : Not much. I thought we'd try to call Joe.

MR. : Who's on the phone--Rob?

MR. : Rob is here, and actually George is here as well.

MR. : Hey, George.

MR. : Hey.

MR. : Okay. Now is this still mostly listening? Because I don't think I'm, you know, we're, any of us, prepared to offer any solutions. Are we just--

MR. : I think it's brainstorming, and I think it's brainstorming about, you know, what--what can we possibly think of. You know, so for instance, you know, for George and Rob's benefit, something that Jeff has mentioned to me a couple of times that I'm not, well, I honestly hadn't sat down to think of it, but even if I did, I think it's kind of one of those things that just reflects

how much smarter Jeff is than I am.

But he was, you know, just, okay, let's do a pre-pay and to cover this what if we then go out and short the bond, short some Enron bond? Now, we've got to go borrow the bond somewhere and, you know, what would we ask for, from Enron, to kind of cover us on that securities borrowing situation, something like that.

MR. : It's not clear to me, in that situation, if we're even specifically telling Enron what we're doing. We may or may not, if we were doing that. I think what we're trying to gauge is how, how aggressive they are to pay for this stuff now, which is discreetly get, you know, several hundred million dollars and have no market knowledge of what's going on and not necessarily reveal that could be a route we'll propose, but it might be something we do without even telling them.

MR. : Yeah.

MR. : Say, look, 200 basis points, you're done for a year.

MR. : And I think, you know, the trick for us is going to be, if we can think of something--

MR. : Yep.

MR. : --you know, it's going to take, you know, maybe particularly now just because of all of the market disruption, you know, we're going to have to get credit to sort of--

MR. : Yeah.

MR. : --you know, sign up for kind of an underwriting period, not unlike the one of these things that we did a couple of years ago where we then took like 60 days to layer[?] in a couple hundred million dollars of default[?] swaps.

MR. : That was last June.

MR. : Yeah, no, I hear you.

MR. : I think that one of the things we ought to--we ought to recommend to Joe, and I'm thinking I still have an e-mail you sent out a while back, Jeff--Enron pre-pay, no. You sent something out to somebody with like a graph--

MR. : Yeah.

MR. : There it is. And so, in '01, how much have we really run off since sort of the first of the year? It's kind of hard to read this graph.

[Telephone ringing.]

MR. : That's Joe. Hold on a second, okay?

MR. : Yeah.

[Pause.]

MR. : So how much did we run off this year?

MR. : I'm guessing 400 to date.

MR. : Yeah, because I think that--I

think one of the things that we just honestly have to say to Joe is, you know, politically, et cetera, you know, just kind of given that I guess you can sort of think of it, yeah, on the one hand, we've got a bunch of these things on our books that, you know, have got pieces of surety bond paper attached to them, you know, in kind of the crudest fashion. I think you just have to accept that we've sort of come to deem ourselves a little bit less secure than we used to be.

MR. : Yeah, exactly. That's going to come more onto the Enron book--

MR. : Okay. So, in other words, sort of, without anybody really trying, our Enron book is just, it "creeped" up to gigantic proportions, you know, as the value of those sureties, you know, just--

MR. : Sure.

MR. : --just faded away. All of which is to say, you know, we've kind of paid off 400 or even if you want to kind of be sneaky and say for all of '01 maybe the pay-down is 500--

MR. : Right.

MR. : I don't know, politically, we can't go back to reflect[?] 500.

MR. : You're right.

MR. : We'll try for something. I don't know if it'll be 250 or 300 or less than 250, but, to me,

that just sounds like the battle that at least could be fought, and you know we're going to have to come up with a risk-mitigation strategy that we can speak to with confidence to right that battle.

MR. : And then I think that's--I think you have--then that message is that whatever we replace, we're going to be pressured to mitigate. And what, Joe, what we can try to do is come up with a proposal that gives you some economic view of what that's going to cost, and you know--

MR. : You know what default[?] swaps cost, so that's the one thing you always have in the back of your mind as a possibility, Joe, to pay that, plus some asset carrying cost.

MR. : Yeah.

MR. : But, you know, for a short-term deal just to get something done and roll some money, now--but we'll try to come up with other ideas. But there is a, you know, if he always[?] wants to pay the offer on the default[?] swaps, we could do that.

MR. : Right.

MR. : Okay. Well, hold on. Let's go ahead and tie him in. And I suspect this woman, Lisa Beals [ph] is likely to be with him.

MR. : Okay.

[Pause.]

MR. : Go ahead.

MR. : So Rob and George are actually with, we're all together in one room, and then I think we have Jeff--

MR. : Hey, Joe B.[?].

MR. : Hey, how ya doing, man?

MR. : All right, bro.

MR. : How are you hanging in up there?

MR. : Eh, you know. Actually, probably better than my wife, man. She seems to be seeing more of the families at school and suffering more through this. It's, for us, you know, you just sort of plug through it.

MR. : Yeah. Aye, yi, yi.

We've got myself, Lisa, and Mike Garberding over here.

MR. : Okay.

MR. : Well, I'm trying--I'm trying to figure out what the best way is to kind of, kind of start this off, Joe. I mean, you know, I think the basic setting is, you know, clearly, we've, you know, number one, I think, you know, we've--one of the last couple ones of these pre-pays that we did, maybe it was the last one, I think, you know, which was a pretty big jumbo one, and, you know, there's a little bit of rhetoric that we, you know, that we used internally because it was something that we talked about, which was that we were going to take a considerable

amount of time off from this market

MR. : Right.

MR. : And so, you know, just so you'll know, we're going to--we're faced with the risk that somebody has a reasonably good memory, and they call us on the carpet on that.

MR. : Yep.

MR. : And so we have to plead guilty to that, just for having the conversation.

Number two, you know, maybe--I don't have the exact figure, but I think we were all kind of thinking that year-to-date, '01, we've had in our Enron pre-pay portfolio, approximately, 350 to 400 million roll-off.

MR. : I think for the year we think it's probably somewhere just north of 500 million for the whole calendar year.

MR. : And we kind of thought about the same number.

MR. : Right.

MR. : I think one of the other kind of facts of the matter is, although we certainly have the mitigation of the surety bond paper that we have attached to a bunch of these pre-pays, and some of them are also mitigated with other kinds of instruments, at least with respect to the sureties, you know, we've been I think pretty frank with you guys that we've, you know, had a battle with

our credit chain, where they basically just deemed those instruments to be, you know, of far less value than when we booked these deals, and so through no fault of ours, yours or whatever, our balance sheet, our Enron balance sheet exposure has just sort of, you know, migrated, you know, geometrically upward as we kind of reassessed the value of that risk mitigation. It's there, and we wouldn't want it to go away, it's just not a basis upon which we sort of automatically feel like we can book new exposure and kind of deem ourselves to be mitigated.

MR. : Right.

MR. : So--

MR. : Joe, do you even think they're in the market? I mean, I'd be shocked if they're in the market.

MR. : Providing bonds like that?

MR. : Yeah.

MR. : Yeah, actually, we've gotten some pretty good indications. I mean, there are a number of them that are gone. I mean, Travelers is sitting out, Chubb is sitting out, Zurich is sitting out, Camper[?] is out, but there are a couple of other names. I think we were originally putting out interest for a 5-year--

MR. : Yeah.

MR. : We had about 125 million of interest come in, but there was a lot more interest if we

shorten it to 3 years. At this point, though, I know you guys have struggled internally with them. I've got Bear[?] still talking to people, but I've also given the heads-up that the sureties may not be the risk mitigant we're going to go for this year--this go-around.

MR. : Yeah. Some are also talking about this event, too, right? Which they're trying to assess what their damages are, right?

MR. : Right. I mean, that's why a lot of these guys are just out of the market right now. So the feedback we've got is a number of them, Chubb, Travelers, and others just won't accept the exposure they have right now.

MR. : Right.

MR. : Hopefully, they'll come back, but there are still guys that are out there open for business. We're not finding any problems still on, you know, construction bonding and things like that.

MR. : Yeah.

MR. : But stuff like this, which is more of a specialty product, there is a lot of hesitation to get out there and do anything big until, you know, some time passes.

MR. : Yep.

MR. : I mean, I suppose, you know, even if, even if that market kind of stays open, I think one of

the other risks that's out there is just the potential quality of documentation. I just have to assume that those guys that are sort of in a market crisis like this, to the extent that, you know, we all invested a bunch of time, you know, about 3 years ago, in rewriting these sureties to a different instrument than what came off the shelf. You know, they may, they may basically say we're not writing it like that any more.

MR. : That's fair. I don't think that's necessarily going to be a risk we'll actually ultimately have to live with, but I think, I mean, [inaudible] there will be some more questions on the bonds.

MR. : Yep.

MR. : Yeah, the reinsurance community. Well, just the reinsurance community is going to get crushed there, so we'll see.

MR. : That's right. That's where the problem is right now is--

MR. : Yep.

MR. : --the guys like Travelers and Chubb, they're open for business only if they get reinsurance, but they don't have any reinsurance to play with.

MR. : Exactly. We've heard the same from [inaudible] and, you know, a bunch of others.

MR. : Right.

MR. : You know, they'll take--they'll take it for their book, but it's a very small size.

MR. : Right.

MR. : Well, I think what I'd like to do, you know, I think, Joe, I think it would be helpful, you know, we should, we should brainstorm a little bit about what some risk mitigation alternatives are. I think, really, preceding that, though, I think that the--I think the right kind of request for us to consider, you know, to continue to work on is something that's going to be, you know, less than what you're seeing as our run-off amount, okay?

MR. : Okay.

MR. : I just don't think that we're--that's probably not going to be a very successful battle for us.

MR. : What number do you think, do you have in mind?

MR. : I don't know. You know, I'm sort of thinking 250 to 3-, you know. I know you came with 350. I'm happy for that to kind of be the number that we start with--

MR. : Right.

MR. : I just, I think I'd be kind of stupid to give you a high degree of confidence on that number right now just taking everything into totality.

MR. : Okay.

MR. : So, but I just want to make sure that we're all sensitized to that.

MR. : I think it's fair, you know, it's fair to say, Joe, that there's also a high likelihood that we are going to have to propose internally some form of risk mitigation.

MR. : Right.

MR. : And, you know, the most obvious one is extremely expensive and is there any other way we can come up with a creative risk mitigation strategy.

MR. : Ballantine.

MR. : Are you suggesting just credit derivatives is the most expensive alternative?

MR. : Yeah. I mean, I think, you know, that stays on the table as, yeah, as for short term, you know, want to roll over discreet financing, do it reasonably short term at a pretty high cost, that is there, and probably will be.

MR. : Okay.

MR. : But can we come up with something else creative to propose internally.

MR. : Right.

MR. : You know, that's the question.

MR. : I was going to throw out--I'm glad George is on the phone--going back to the old performance LC

option, is that--does a performance LC really hold any value any more?

MR. : Well, I think you still run into the capacity situations that we have been running into [inaudible].

MR. : Well, [inaudible], you know, his question is, you know, does that work for us.

MR. : Oh, yeah, yeah, yeah. No, that works.

MR. : Yeah, I think that--

MR. : That works.

MR. : If we could get them, that works.

MR. : Well, the question is, I mean, is there a difference between performance LCs and financial LCs any longer?

MR. : Oh, oh, that Arbitrage. I don't think so, right, George?

MR. : Well, I mean, we haven't, we haven't tried that in a while, but I mean there still is, you know, as far as capital allocation, [inaudible].

MR. : Okay.

MR. : And there's a 50-percent capital weighting, and we had always kind of priced it, in the old days, kind of 75 percent of what we thought your drawing[?] cost was to be able to [inaudible]. So I don't think that there's a reason why, you know, theoretically, that would

not work.

MR. : The options that strike me clearly are the performance LC against a physical pre-pay, a financial LC against perhaps a financially settled pre-pay or a true syndication of the funded deal on a risk basis to everyone except Jim McBride.

I mean, any of those options don't sound workable as such or--

MR. : Well, now we start I think talking about, you know, just anecdotally, what the potential costs are.

MR. : Right.

MR. : That's why I was asking George's view on all of that.

MR. : On one of these?

MR. : Yeah. I mean, the sense we've been getting all year is, you know, funded assets are what the market is looking for, as opposed to just unfunded commitments. And so if that is still the case, there is really a performance base or a financial LC, is that going to syndicate it any better or worse than a funded participation in the deal?

MR. : In general, if you're talking a funded versus an unfunded asset, you're actually correct. A funded deal is going to go, you know, many, many times better. And, you know, if we kind of want to shift a little

bit to get more of the reality of capacity, yeah, I think you're on the right track, as far a that goes, if we're talking about going to the bank market here.

MR. : I think two, I mean, two alternatives, as far as, you know, getting a quick deal done, the old ways, as I recall, you know going back a few years, we would have you guys underwrite, we would syndicate the following quarter as quickly as possible, and I think at times you would mitigate the risk, in the short term, as Jeff indicated, through a credit derivative hedge until we could syndicate, and then you'd lift the hedge. I think that's clearly one option to cover off on the exposure.

I think there's other options. We could just corral a bunch of the LCs we are using against our own collateral postings right now and pledge a bunch of LCs against the exposure and then drop all of those LCs and put them back to our regular course of business once we have syndicated the position.

Those are two short-term fixes.

MR. : How much risk are you willing to take on the re--

[audio break]

MR. : I'd say I'm all ears at this point.

MR. : Okay.

MR. : Where we are, if--

MR. : What is the shortest possible scenario for you--like 6 months, [inaudible] months?

MR. : I'd prefer to do like a year.

MR. : Okay.

MR. : And if we do a year, clearly, I think we just want to do it as a financially settled pre-pay rather than delivering, you know, the volumes we'd be talking about.

MR. : Okay. Okay.

MR. : But even if it's a year, I think we'd be willing to look at that, and if we ultimately get into syndication of this thing, we'd determine that we can take it out to 3 years perhaps, perhaps we can amend it and put it away for a while, but as far as getting it closed, you know, whatever you guys--I guess I'll listen to hear what you guys think can work internally to get this deal executed.

MR. : Right, right, right, right, right.

MR. : Do you think we'd want to do the funded kind of executions?

MR. : Well, again, if we're talking about going to the bank market, I think, in general, a funded deal is received much more favorably than an unfunded. I mean, I guess, knowing the other things that are potentially in the pipeline for you guys, I would love to see a solution other than bank market here, which I think

we're kind of new [inaudible] things, but, yeah, in general, a funded asset is going to go a whole lot better.

MR. : George, do you see a lot of bank stuff that Kelly is talking about [inaudible]? Because the sheets I have don't really have us doing a lot in the bank market.

Are you saying that? Or there might be some stuff I'm not aware of yet.

MR. : I think there are a couple of deals that are still out there that are trying to wrap up that have been out there for a while. There's, obviously, you know, Verizon's[?] BPP[?], which we're coming into at the next month, and I know that a couple of other banks are looking at.

MR. : Yeah, I think that one is pretty much--I mean, that one is really out of the market. There's just a couple of names looking at it.

MR. : Yeah, but in terms of kind of carryover, and then you've got, you know, our own, you know, Flagstaff transaction that is still getting wrapped up, and then I know we're working on another transaction that may or may not get there, and I would assume there are some others out there.

MR. : Which one is that that you're still working on?

MR. : The Cosmo.

MR. : Cosmo.

MR. : Oh, okay. I'll talk about that one at Ben's meeting this morning.

MR. : Are you up to speed on that one?

MR. : Yeah. Yeah. I'd prefer not to comment on it just yet, though.

MR. : We'd appreciate your comment.

[Laughter.]

MR. : How did you put it yesterday, Rick? To be honest with you this time--

[Laughter.]

MR. : But I'd say, you know, and certainly George is, you know, on the same page as us. A funded deal will syndicate a lot better than the unfunded, particularly if we have to start packing the pricing on the unfunded or the funded for you guys, unfunded for other people. If you guys take a look at the options we just laid out, and I know, Rick, you know, Brandon[?] and you were talking about just, you know, what size, just short-term Enron risk you guys may be able to hold if--clearly, unless we cannibalize some of that, I think then we'll be more open to that option. Whether or not we need to cover it off with derivatives for a short term or perhaps we could set a window that says, you know, from closing for the next, you know, whatever, 30, 60, 90 days, you guys might be able to wear it while we syndicate the exposure down, and if at

that point we haven't, we'll have to kind of wrap with either derivatives or LCs or such until they'll get syndicated.

Is there a window you guys could hold the exposure or do you need to put it away immediately?

MR. : Okay. Well, obviously, we've got to come back to you on that. That's certainly what we're thinking about and probably can't comment on that right now.

MR. : And then whatever you think expected pricing would be on--

MR. : Yep.

MR. : I mean, I'm not confident the arb[?] on the performance LC really makes sense, given the appetite for funded paper at this point, but if that does make economic sense, we'd be interested to hear that.

MR. : Okay.

MR. : What do you think the process or response time is going to be on this one?

MR. : Well, you know, obviously, I think we should just accept that this week is kind of shot. It gives us a couple of days to get our script together, you know, to start attacking the mountain, and I think it's going to have an awful lot to do, you know, I guess if we can come up with some, you know, alternative--alternative risk mitigation stuff, you know, establishing some confidence, you know, that that can get executed and then I

think that, to the extent that it's more of a bank syndication type execution, you know, to a certain extent, that's just going to kind of come down to pricing.

MR. : The other thing we're trying to--

MR. : And I think, you know, understanding what the holding period is going to be, you know, how long that's going to be, I think, you know, clearly, our desire is going to be to get it, you know, off the books, you know, ASAP, before the end of our year end--

MR. : Right.

MR. : And that's going to be a bit of a function of what the rest of your calendar looks like.

MR. : But now when you say get it off--are you talking about the exposure or the funded asset?

MR. : Well, preferably, well, the exposure for sure, right? So I think, at a minimum, we're closing year end with a bunch of credit default swaps--

[Audio break.]

MR. : Hey, John, can I call you back?

MR. : Sure.

MR. : Bye.

[Audio break.]

MR. : We'd come back, and we're able to do something, and, you know, and ultimately we're going to take this out to some sort of bank market [inaudible]--

MR. : Right.

MR. : --all of this kind of stuff, and you guys--

[Audio break.]

MR. : Hey, John. Hello?

MS. : Hi.

MR. : Hey, what's up?

MS. : Jeff?

MR. : Yes.

MS. : Hi. Well, I spoke internally with the different persons involved and with my boss, and it's difficult for the bank to close the transaction today.

MR. : Okay.

MS. : Because we have a lot of persons involved in the problems with gas[?] futures[?].

MR. : Okay.

MS. : And my boss prefers to wait some days--the markets stabilize.

MR. : Okay.

MS. : And so if it's possible to wait until Tuesday to see how the things go. Of course, we are all committed in this transaction, there is no problem, but it's just that we have a lot of people involved in the power[?] future problems.

MR. : Okay. Would you kindly just have your colleagues in Buenos Aires convey that to--

MS. : Yes, I already spoke with them

just a few minutes ago.

MR. : Okay.

MS. : So they are going to call there very soon.

MR. : Okay. So, if that's going to happen, we should definitely wire the money back to you.

MS. : Yes.

MR. : Do you--does our back office have instructions on where to send it?

MS. : I'm going to call them now to call your back office.

MR. : Thank you.

MS. : Okay?

MR. : Good.

MS. : Thank you.

MR. : Bye.

MS. : Bye.

[Audio break.]

MR. : --we have certainty lowest risk of execution.

MR. : How does that--okay, I just want to make sure I've got my head around that in terms of the question that I would expect to get asked, which is kind of like, well, wait a second, you know, if we give them cash--I guess this becomes a function of the short-term versus the longer-term use of the cash, which is, you know, if there's

a cash funding and the short-term Band-Aid is to divert, you know, those trade credit LCs to our direction, you know, you're not up any net cash, correct?

MR. : The's right. It's just pure geography that we've got a short-term working capital use of cash.

MR. : And so then the risk is on that, in fact, we get the thing syndicated, and then you redeploy the LCs back to where you had them before, and you've got "X" millions of dollars, you know, back in the system.

MR. : That's right. That's right. All of the cash flow is just working capital items, deposits, and, while it is still important to us, it's not as important as the other stuff. But the intent would be it would just be a short-term working capital item until we syndicated it, and then we got the LCs back and brought the cash back to them.

MR. : Sounds good. We will--we'll get to work on this.

Is there any more to cover on the pre-pay before we get started?

MR. : I don't think--tell me if I've got it right. The sense to me is, I mean, if, if the underlying deal is still going to be a pre-pay transaction, regardless of where we take the credit exposure, and term and all cf that, I mean, that's, you know, off-the-shelf documents,

with the exception of maybe doing this as a financially settled, rather than physical.

MR. : Right.

MR. : And that's the kind of deal kind of between Enron and Chase. We could do that in, you know, in a week maximum time frame, but it's the kind of thing I wouldn't press, but I'll just start, at least on our side, just document that up and have that ready to go, and then determining just wherever we place it or hold--you know, we'll have a couple of weeks to figure that whole thing out. But the mechanics of the actual closing between the two institutions should be relatively simple and easy.

MR. : Yep.

MR. : Yeah, I think that's right.

MR. : I think I'm okay now. You know, we've had problems with this in the past, Joe, but I think I'm okay to do a cash settle deal now.

MR. : Yeah. Yeah, okay. Good.

MR. : We got some CFTC changes recently that may make that okay.

MR. : Okay.

MR. : But I'll just, I'll go through that.

MR. : Joe, before we drop off, I was hoping you might be able to help me. I just got a call from one of our credit guys that Enron had shown up on some

report as having missed a margin call last night for 120 million bucks.

MR. : To you guys?

MR. : Yeah.

MR. : I'd say give Gleason[?] a call on that. He's making all of the decisions right now on that side.

MR. : Okay. Okay.

MR. : In fact, I thought he had mentioned that he was going to call you guys and say, you know, we need a day timeout, just everybody is taking a day timeout. The same thing happened I think with CP yesterday and all, but--

MR. : We'll follow with up with him on that.

MR. : And on my side, you know, my goal--I know there has been some question as to coordinating curves and all of this stuff, but if you haven't done it already, we need to get the core dollars into that account on the APEA deal.

MR. : Is that--Mike's here--where's that stand?

MR. : Right now where it stands is that there's a question between what the margin is on how we look at it versus them, but at the end of the day, it [inaudible] circle.

MR. : It should be the same, right? It doesn't matter what it is.

MR. : It doesn't matter what is.

MR. : Whatever you think it is, I just need you to do it.

MR. : Yeah, we are.

MR. : When is that going to be done?

MR. : That is going to be run today. We couldn't run it yesterday, so we are following up on it, and we should have it solved today. So--

MR. : Okay, because that's been going on for a bit. Okay.

MR. : Beat on Mike if you don't see an answer on it.

MR. : Yeah. I know everybody is trying to get this right, but now it's better to do it and get it not so right.

MR. : Yeah.

MR. : Because it's only margin money, it's not--

MR. : Okay.

MR. : Exactness is not the most critical thing right now. If there's some dispute on the forward[?], it doesn't matter. It just can't wait--

[End of Recorded Segment.]

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, . (AT) 52 [2 of 2]

September 13, 2001

10:08:34

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : Right.

MR. : Okay. And, Jeff, one additional thing Andersen is throwing back is, when we confirm the deal this go-around--

MR. : Yeah?

MR. : --I think they want us confirming it, if I'm not mistaken, with Mahonia [ph], the Mahonia letter; is that right? Lisa, you're more familiar with the--or Mike?

MR. : You're talking about the rep letter from Mahonia, basically, I think we talked about this before, saying, you know, it has the right to do transactions like this. Before what we've done is just really looked at the actual charter, and you've got the information, but now Andersen is pushing back and saying, hey, we need to have a specific rep letter that a representative of Mahonia signed that refs[?] a certain point.

MS. : Which is, yeah, separate from Chase. It doesn't have Chase showing up anywhere on the fax letterhead or anything along those lines, a separate fax number, et cetera.

MR. : Oh, [inaudible] talk about it, yeah.

MR. : That goes to the same point you

were raising earlier, Jeff, that from your side, you also want to make sure that Mahonia seems independent.

MS. : If it helps, Jeff, we can get you a copy of what they're asking.

MR. : Yeah. I mean, of course, we're going to have to get that, sure, eventually.

MS. : Okay.

MR. : So--

MR. : So I guess we'll hear from you guys you think on Monday?

MR. : No.

MR. : Nice try, though.

MR. : Yeah, that's kind of our starting point.

MR. : Okay.

MR. : One thing we're doing through the rest of the week is just trying to figure out which banks are open for business and, you know, which banks are physically open, but closed from a credit or commitment standpoint. There's a lot of work going on in New York, you know, calling different folks, because obviously there are a lot of financial institutions, a lot of foreign banks in the World Trade Center. So we're doing a lot of that work this week to just kind of figure out what kind of market there will be next week and the following week.

MR. : Okay. All right. Well, we'll

wait to hear back from you guys. We'll get the process started on our side.

MR. : Sounds good.

MR. : Thanks, Jeff.

MR. : Thanks.

[End of Recorded Segment.]

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON GOVERNMENTAL AFFAIRS

In the Matter of the Collapse of Enron

J. Dellapina, (AT) 046

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10:40:19

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MILLER REPORTING CO., INC.
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WASHINGTON, D.C. 20003-2802
(202) 546-6666

pab

P R O C E E D I N G S

MR. : Hey, do you have a minute--George and Rob are still in here--do you have a minute to try to fire a call in with us right now to Eric Fornell?

MR. : Yeah, the value of which is?

MR. : [Tone.] And, number two, to get him fired up about helping us fight the battle on, you know, whatever kind of holding period we end up--

MR. : All right. Give me, give me your real guts here. Do you think we're going to having any holding period on this [inaudible]?

MR. : Well, no, I think that we have to have--

MR. : I don't think--

MR. : I think we're going to have to have the credit swaps like from the beginning or something like--

MR. : Yeah. I mean, the holding period I think is maybe a de minimis number--maybe,

you know, 50, I just, [audio break]--I can't believe anything is uncovered.

MR. : Yeah, I hear what you're saying. I'm just wondering if we don't just put together before even you talk to Eric just like what our three alternatives here are, what our, you know, what we think it could cost the company and what the--

MR. : Yeah.

MR. : --and just put it on a quick, little chart or put the boxes.

MR. : [Inaudible.]

MR. : And I think there are extremes, right? The one extreme is we go out and buy swaps on everything, and we buy them for a two- to three-year period, whatever the market will give us, and then if, and when, we can syndicate this thing, we'll sell the swaps, and, you know, they'll suffer bid all for consequence. So if we buy them at 200 and we sell them for 180, that costs the company 20 bits.

MR. : And we'll just [inaudible]

in the documents that we have an adjustment for that?

MR. : Yeah, exactly. And, you know, that kind of--well, basically, you don't even need them in the documents. It's more like a handshake because we own the swaps, and we, you know, we're the only ones who can change it. So they'd have to come back to us and make a price on it. So it's all we control everything at that point. It's more them trusting that we will help them switch it to a syndicated deal and get the cost down.

But I think that's one extreme that we lay out to Joe. It's we're going to [tone], and it's basically going to cost you 250. We'll do a two-year deal at 250, if that's what we can [inaudible] spot and the default swap market is, and, hey, you know what, you know, under Rob, and George, and Rick, they're going to try their best to syndicate this thing and get you all of the economic return back on that thing. If they get it down to 150, great; if not, you're stuck with it,

and you can always refinance it. We'll be happy to refinance it at that time.

But that's your starting point. This is your worst case in getting credit to sign on that we can do that, and then start sort of clawing back what would be better to bring the costs down for him.

So can we reconvene later? In the meantime, I will find out from the desk what is accessible, in terms of default swaps, what we would need to carry that asset and just say this is our starting point of a deal that we can show credit we can do, which they can't object to really.

MR. : Right.

MR. : But then we--because if we don't show them that you could do this thing, then they're going to be very nervous.

MR. : Oh, absolutely.

MR. : So at least we say, look, this is what we can do, but obviously the company has got their backs up against the wall. If we jam

pab

them at Libor[?] for 300 and show no credit flexibility, they're going to be pretty bummed, but I could do it, guys. So now they at least know the market is there.

MR. : Right.

MR. : And then we start backing up and say, we go[?] about 4- or 500. Can we at least hold 150 through year-end because we've got another 150 rolling off concurrently? That's one argument.

Today, if the clock stops today, and you gave them a three-month window to syndicate, we put a new 150 on, but every day we're losing another 150, right? Between now and year-end.

MR. : Right.

MR. : So, you know, just giving them--I'm just wondering if we, sure, we can call Eric, but we don't really have anything yet that we--I don't know. It's your call, Rick. I'm happy to be on it.

MR. : Well, I'll tell you what, I'll just give him a call and just tell him that

we're looking at this; you know, we're going to, you know, that you're putting something together; that, you know, we're trying to get our script together for Ballantine; that the real trick is, you know, to kind of give the best deal for the client, you know, what can we do that--

MR. : Yeah.

MR. : You know, we need to, you know, I think it would be a great goodwill gesture for us to, you know, hold a little bit of this. I think, you know, I don't know. I mean, this is sort of mixing apples and oranges totally, but based on Joe's comment, this other deal we're working on, he's probably thinking--

MR. : It ain't going to happen.

MR. : It ain't going to happen.

MR. : So do you guys want to come up with your scenario of how you could fund this thing?

MR. : I'm assuming that the uncovered amount we're talking about, the 150 or whatever the number is, would still have, would

still look like [inaudible] what it's replacing and how it's the surety support.

MR. : No, I don't think so. There's no way the sureties are right in this stuff.

MR. : I've got to agree with that. I've got to figure they're just in such disarray.

MR. : I can't even imagine. The reassures[?] could be getting--there's no way.

MR. : But, Rob, we would definitely ask for it because I think it's a good add-on, but not only would the bank put no value in it, I don't think they'll possibly write a deal.

MR. : I don't think they're putting no value on it. I think it's just, I mean, there are numbers that have gotten done in these prepaids that wouldn't get done without it, but they're not putting a lot of value in it.

MR. : Right. Right.

MR. : And so I think the argument for holding 150, which is a big number, is

pab 9

a little more sound when you say we're replacing that 150 with something that looks like we've already got, we've got the support from the sureties. Our overall exposure to Enron when the surety goes down, what we're replacing looks like what we're losing. I just thought--and I hear you, but--

MR. : Well, I think your thought process is totally logical, and--

MR. : I hear you.

[Simultaneous conversation.]

MR. : I believe in it.

MR. : --sureties, you know, your choice [tone.]

MR. : I hear you. It's something we would definitely ask Joe do, which is get cover on the 150, why not?

MR. : I'm just assuming it's better than nothing.

MR. : It is. It is better than nothing.

Okay. Well, do you guys, should we--I'll

call you in a bit, and I'll try to probe from this side, and then you can possibly probe what you think is practical that you could argue is doable in, you know, 30 days or in 90 days, in terms of costs from the bank side.

MR. : It's going to be expensive.

MR. : I mean, George, what are you thinking off the top of your head, like 180?

MR. : [Inaudible.]

MR. : 175?

MR. : Yeah, I mean, I think it's going to be between 150 and 200.

MR. : And what kind of fees?

MR. : Well, what tenor are we talking about now?

MR. : Just say three-year.

MR. : Three-year? I mean, I think you could [inaudible] yield to between 150 and 200 between margin and up front. That's your, that's your range.

MR. : So maybe 150, with a

pab 11

75-basis point up front.

MR. : Something like that. I mean, it also depends upon how big a chunk we're at [inaudible], obviously. That'll push it more towards the 200.

MR. : Right.

MR. : I mean, if our strategy is to go to just the two folks and have them each take a 50 to 75 chunk or even 75 to 100 chunk if we really make it a [inaudible], which is I would guess the way that maybe they'd want to go with this thing. See, they are just going to be super sensitive because this will be a new marker out there for Enron-funded paper.

MR. : Exactly.

MR. : I would think they'd want to keep it down to a handful of banks, like three.

MR. : Exactly. That's why I'm sort of suggesting, if you're thinking 200 all in, and we think we could do a deal at like 250 to 275 ourselves--

MR. : Yeah.

pab

MR. : You know.

MR. : [Audio break.]

MR. : What's that?

MR. : That's a premium that they might want to pay.

MR. : Yeah, and they could always refinance it in six months if, because we can just sell the bonds, the surety--the default swaps, right? I mean, we could sell the default swaps. So that's something that they may [tone] I'll take the refinance, I'll pay it now, and I'm betting on my company the credit spreads are going to calm down, but I'll take the bet rather than risk, risk a total blowout of spreads across every deal.

MR. : Because I know going back to '98, when they just had it inch up just a bit to kind of 125 to 150 range, they've commented many times that's come back to haunt them because in following deals everyone went back to that price point. So if we put a price point out there that's 200, that could potentially hurt them.

MR. : Okay.

MR. : Yeah, I'm actually supposed to see--I don't know if Ben is going to hold this lunch today or not. I don't really want to--I may get into this a little bit with him, but probably not terribly specific on price [inaudible], maybe not. I don't know.

I'd be interested--and, Jeff, if there's any chance that you can get any kind of readout of the desk, out of the default swap desk--

MR. : Yeah, I will. I'll call you right back.

MR. : That would be good.

MR. : I will.

MR. : Okay. Thanks, guys. Talk to you in a bit.

MR. : Bye.

[END OF TAPE RECORDING.]

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nr 1

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collpase of Enron

Dellapina, (AT) 018

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15:10:25

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MILLER REPORTING CO., INC.
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nr 2

P R O C E E D I N G S

MR. : Richard.

MR. : Jeffy.

MR. : What's up?

MR. : I'm sitting here with Cerese [ph] and Traband.

[Audio break.]

MR. : Anyway, we're reaching the point of soon it will be just physically impossible to do. So I guess it's a good idea we have this conversation.

MR. : Well, Rob was just saying that he--

MR. : [?].

MR. : He had to have a quick phone call with Ballentine [audio break] that he had a quick phone call with Ballentine and they were going to have to get a package put together [audio break.]

MR. : [?] your job.

MR. : Yeah. Bottom line, I think we're going to need to take a--you know, to

nr 3

answer what the obvious question is going to be, which is, well, why would we want anymore Enron exposure.

MR. : Mm-hmm.

MR. : It's got to be a profitability question. So I think we need to get an idea of what we think we're going to be able to book.

So--

MR. : Well--

MR. : I haven't dug out my files and I'm hoping yours are handier in terms of kind of where have our price points been the last couple of times and, you know, every--you know, the last five or six of these we've managed to eke out. We have a couple more basis points.

MR. : Yeah. I mean, here's the--here's the trick with this. Basically, what I would--Enron, what are they rated now?

MR. : Triple B plus. Well, they're a three-plus on--

MR. : They're a three-plus.

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MR. : They're a three-plus. So, basically, what I can tell you is what does the three-plus show in our system, that when we book this asset, what is it going to show, and it's probably going to say that we have to reserve and, you know, basically pay away something like 80 or 80 basis points or 90 basis points, right?

In theory, you could pay the rest, right?

MR. : Okay.

MR. : But I will say that the question becomes a little bit fuzzier, because you don't really usually have a three-plus trading at 250 basis points in the default swap market.

So I don't know who's going to throw--you know, cast the sort of inquiring eyes on this and say, "Well, you know, this is probably inappropriate to mark this thing, you know, to whatever--whatever the--I don't know--the model is saying is an SVA neutral loan for a three-plus."

I mean, what does the model say?

MR. : I'd have to go back and look at, but it's--

nr

5

MR. : It's probably going to say like a 100 basis points or something, I bet.

MR. : Yeah. Maybe a little less.

MR. : Okay.

MR. : That's about right.

MR. : So the question is, you know, would people have a problem with us, you know, TV'ing anything on something like this when everything is so in question.

Now, if you think it's okay, I can give you what that number is. Conservatively, we could just start with the fees and then work our way from there.

MR. : Well, I mean, have we talked about the fees?

MR. : Well, I mean, George--I guess George opened up with some fee discussion and then we should talk about what arrangement fee we would want.

MR. : Exactly.

MR. : Right. And what I had

nr 6

thrown out was if you're looking at kind of a three-year deal and 1.75 year average, I think what I had talked about is a--for a big ticket LIBOR plus one and three-eights and then 50 to 75 up front, if you wanted to buy down the rate, I thought it was 75 to a 100 up front and one and a quarter.

MR. : Okay. Seventy-five to a 100, right, right, of fees, and then one and a quarter basis points. Right.

MR. : Right.

MR. : Which I thought was--I don't know. It seemed kind of low, but basically just your preview on that, what do you think?

MR. : Well, I mean, we kind of wrote this with Enron and we're met with shock and indignation. I think some of that was a little veil, but--

MR. : Yeah. I do, too.

MR. : I mean, I think--I think this is aggressive, but I think you could probably get a bite. Yeah.

nr 7

MR. : Okay. A bite. All right. So if we go that route.

MR. : I'm sure we could get McBride interested for this.

MR. : Well, remember, we don't have the insurance companies at the time, right?

MR. : Right.

MR. : Although I talked to a broker and he still thinks he can get them. I don't know. Which complicates it a little bit because we might want different [audio break] might want to buy the insurance, even though we're not valuing it a whole lot.

All right. Well, I don't know. What do you think we should get? At least--at least 50 basis points, right? At least, right?

MR. : Do you recall what we got the last time?

MR. : Three hundred and fifty grand--350 million. Somehow I thought it was--

MR. : I think the last one--was the last one 350 or 500? I can't--

nr 8

MR. : Three-fifty we did, right, George? Three thirty-five or something like that.

MR. : I think it was 335.

MR. : Yeah. It was less than 350, but it was close.

MR. : And do you remember what your fees were, George? Well, actually, you know what? I'll pull out the fee letter right now.

MR. : Yeah.

MR. : How about I do that?

[Audio break.]

MR. : Okay. Enron--ready? The answer is. Hold your ears, George. [?].

[Audio break.]

MR. : Three-thirty. It was 330 million and they paid an arrangement fee of 2.145 between Chase and Fleet. It was split equally between us and Fleet. So that is--

MR. : [?].

MR. : No. Well, somebody do that math. Anybody have a calculator handy?

MR. : It's about--

nr 9

MR. : Sixty-five.

MR. : Sixty-five?

MR. : Sixty-five, 2.145 over 330. Right. Then, George, then you prepared a separate letter to him, correct?

MR. : I don't remember.

MR. : Which was, I think, something like another--

MR. : [?] something on top like that.

MR. : Yeah. I think so.

MR. : And for some reason, I'm almost thinking it was--it was about anywhere between 800,000 to a million, because you remember, George, when we sent that money over?

MR. : I ended up getting like 375 out of that. I don't remember--I don't know remember what you got.

MR. : I remember you made me send a letter to you. So let me see if I can find that.

MR. : Signed by the guys in

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Jersey. That is, the Isle of Man.

MR. : We can pull that up, but I think it was in the order of magnitude of around 750. I think that's what it was. So that wouldn't have been a whole lot of money, then. What was 750?

MR. : Isn't it on the arrangement fee?

MR. : Yeah. Sounds about right.

MR. : Yeah, it does. But [?] 23 bits.

MR. : Yeah. So pretty much--I don't know if it was a flat fee or if it was 25 bits. I don't remember. That's probably what it was, though.

MR. : And then we had--we had the insurance wrap and then we had, of course, our margin.

MR. : The margin, which was seven-eights, is that right? I think it was.

MR. : I think we start--didn't we start off at like five-eights and in courtesy of

McBride, I think we ended up--

MR. : Yeah.

MR. : At least seven-eights. Yeah.

MR. : Yeah.

MR. : Yeah.

MR. : Yeah. So I think that's what it was. It wound up being about 25 basis points on the whole thing that we got as an arrangement fee.

Basically, you know, obviously, there is work to do. I just--I don't know. How badly do they want this, Rick, Rob?

MR. : Sounds like they want it pretty badly.

MR. : [?] badly.

MR. : I think they do. And I think this is a steal if they get that thing funded at three--at 125 and you spread the fees. That's about what they would pay anyway, George, right, in fees, 75?

MR. : Yeah. I mean, the fees

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that I threw out were kind of market, what I think market is.

MR. : Okay.

MR. : And, you know, so, of course, we get that, also, and then I think for arrangement fees, I think we've kind of been around that 750 to a million sort of number.

MR. : Okay. Okay. But that's the--you know, again, spreading that over three years is really not a big deal. I mean, I would--I would think one--yeah. I guess one percent.

No. I mean, I--we charged more than 25 basis points on this.

MR. : For arrangement.

MR. : Absolutely. The bottom line is we've got the biggest exposure and we're topping up again. So we should be paid the most money. I think we have the biggest exposure.

MR. : I think--

MR. : Well, we haven't exactly set that yet, so.

MR. : Not in the deal, but just

overall for the company.

MR. : Oh.

MR. : You know.

MR. : One of several. I think we might be able to top it off.

MR. : Yeah. Two, they can't really--probably can't--

MR. : [?].

MR. : I mean, just given how spooked out the market is right now, they probably can't do this without us, I mean, without us stepping up. Is that probably true?

MR. : Especially in the time frame.

MR. : Yeah. Especially in the time frame, yeah. Actually, that's a huge point, because, you know, really, the only other firm that they do these things with very much is City, I think, and they just vastly prefer to do them with--with the redheaded stranger.

MR. : Yeah. So I don't know.

MR. : I don't disagree with you,

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that it would seem like we could get more of an arrangement fee this time given the circumstances, given the markets, given the timing.

MR. : I'll go back to [?] and find my notes on--

MR. : I'll go look in my office, too.

MR. : The last prepay ever, that we would ever do.

MR. : Yeah, right.

MR. : So if we're--the last time was seven-eights, 65, and we got 25.

MR. : Yep.

MR. : So now we're sort of saying 125, 75 to one percent, and 50.

Personally, what I would like to say is I would like to say I would almost give them two different interest rate exposures, depending on whether they bring the sureties on board.

Now, I know we don't really value that, but I would say like, you know, we do it at either one and an eighth with or 150 without.

nr

15

[Audio break.]

MR. : I don't know. I mean, I see this--I see these--I don't know. One--basically, you got a little over a week to get these guys in.

MR. : What we need to have happen--

MR. : Whatever happened to the funded concept? I mean, how are they going to--how are we going to get a funded trade done in the next week?

MR. : Well, I think the idea was that we were going to do it ourselves.

MR. : [?].

MR. : Yeah.

MR. : Over quarter end and then October 2nd, they were going to--whatever portion we were going to remain--that we weren't going to hold, they were going to throw an LC at it, and then we would like, you know, presumably, by year end, to get it off our asset upper bound sheet, we'd get the other two institutions in.

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MR. : So we were going to hold--do this over year end?

MR. : No.

MR. : No.

MR. : I mean, over quarter end.

MR. : Yes.

MR. : Yes.

MR. : Really.

MR. : Well, that's their ask.

MR. : That's the ask, I mean.

MR. : What's the difference between--why October 2nd for the LCs and not September 30th?

MR. : Because that's going to--they have to report their usage and availability under their LC lines in their financial statement.

MR. : I see. So they'd have to have in availability to use.

MR. : Well--

MR. : Well, more importantly, the evidence they have availability to everybody

nr 17

else in their financial statements.

MR. : No. I just meant for credit approval purposes. You don't [?].

MR. : Oh, right. Right. Right.

MR. : [?] you said October 2nd they were--

MR. : And they actually know they've got it, because we [?] big LC [?] for them.

MR. : Okay.

MR. : And we can just look on the system and see that they haven't drawn it or issued on it.

MR. : Cool.

MR. : Do you expect--do you expect that they will expect--

MR. : Actually--you know, actually--sorry. You know what the issue is? They've got the LCs out there. They're currently posted with the likes of Duke and Williams and people like that.

So they pull those LCs away from those trading counter parties and give them to us. Then

they're going to have--then they'll have to turn around to Duke, et cetera, and post cash flow.

So what they want is to have--is show the high level of cash at quarter end.

MR. : Okay.

MR. : Which then they're happy to swap out these transactions on October 2nd.

MR. : Do you think, during the period that we're covered with letters of credit, they will be expecting a lower--a lower margin?

MR. : Haven't talked about it. Haven't talked about it.

MR. : Hold on a second.

MR. : Not an unreasonable expectation.

MR. : It's kind of a funny thing, because you're closing this one deal and then just talking about when it flips in the future, but, you know, we haven't talked about--I don't think you can build a mechanism in--

MR. : I think the way you should do that is you say, "Fine. We're real serious

nr 19

about when we get this off and diversified, and so we'll give you a break for 60 days and then it's going to explode again."

MR. : Uh-huh.

MR. : Yeah. That's right.

MR. : Which they want it to be off in 60 days--well, less than 60 days anyway.

[Audio break.]

MR. : I just wonder if they're looking for a lower rate during that time.

MR. : I think we need to talk about what it should be, though. You know, they--they haven't brought it up, but it makes sense.

MR. : And, you know, in fact, for the rate at the end of the 60 days, whenever we roll it, it's going to be a market at that time. We can tell them what we think it's going to be and maybe what we're going to push for, but we don't know what another bank will do it for in 60 days.

MR. : Full of flex.

[END OF TAPE RECORDING.]

pab 1

T2243

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON GOVERNMENTAL AFFAIRS

In the Matter of the Collapse of Enron

J. Dellapina, (AT) 022
SENATE AT-022

September 14, 2001

10:03:01

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

P R O C E E D I N G S

[Telephone ringing.]

MR. : G.

MR. : Hey.

MR. : [Inaudible.]

MR. : Hey, well, I think you called yesterday.

MR. : Oh, yeah, just real quick. [Tone] [inaudible] [Tone] default swap market right now.

MR. : Yeah.

MR. : Enron could be as wide as 250 right now.

MR. : Uh-huh.

MR. : Easily, and not for any [inaudible].

MR. : Right.

MR. : So Rick has been calling me. I haven't hooked up with him this morning.

MR. : Yeah.

MR. : We got to, you know, regroup on this. I mean, you know [audio break] order to just say go do what you can, you know--

MR. : I don't know.

MR. : They're not going to do that, but--do we have a view as to what their, you know, what their liquidity situation is?

MR. : Well, I mean, it is extremely tight right now. I mean, kind of the way that I see this happening, and Rob and I talked a little bit about it, for this type of transaction execution, I see them pulling together three or four banks and just having them take big chunks of this and just paying up for it.

MR. : Give me the price. What is it?

MR. : Well, I think, I think other banks could probably shake lose some exposure for a big number for, you know, between 150 and 200 on a Libor margin and, you know, like I said, a pretty nice up-front fee like, you know, 75 basis points or something like that.

MR. : Okay. Why don't you do this? Why don't you just sort of, can you firm up a view as to who the three would be or four?

MR. : Well, I mean, I have an idea of at least one or two. The way we would normally do that would be to talk with their bank relations people is who I talk with every day.

MR. : Okay.

MR. : But, I mean, I don't know that we need to necessarily come up with the names. I think the strategy, and I could say like, you know, Royal Bank of Canada, who's told me they have Enron capacity, but they're not going to give it away cheap.

MR. : Okay.

MR. : And Royal Bank has done this sort of thing. So, from this perspective, they need to do this for accounting reasons. They don't want to just keep rolling this into debt.

MR. : Right. Right.

MR. : So, now, Royal Bank, they have done some of these just pure prepayments of financial swaps.

MR. : Uh-huh.

MR. : So they could go to them

direct. I wouldn't [audio break] surprised if they did. Literally, they do like a [inaudible] swap and just prepay it--

MR. : Uh-huh.

MR. : --which I don't know how the [tone] they've ever gotten the accounting [inaudible], but I think the accountants are getting tougher. I think they need this. I think you should. I think you [inaudible], we can do it together.

MR. : Uh-huh.

MR. : [Inaudible] Joe, I'll give him the view on the default swap market [audio break], you can do that and just say this is where we think it is.

To tell you the truth, I would tell him, if he thought people were there, and you think your people are there, I would say, this is what you do, Joe. You get standby LCs right now [audio break] [tone]. Why would people not want stand--see, he doesn't want, people would do the standby LC for the exact same price as a funding. Of course, they

would, right?

MR. : Right.

MR. : [Audio break] they would, right?

MR. : Yeah.

MR. : Now the problem is then he's got to pay me to carry the asset.

MR. : Right

MR. : Say an extra 50, but we leave a little carrot out for those people to say, all right, when we roll this in, you get another 25 or basis point 50 into a funded piece. So, Joe, then saves the money [audio break]. Get the LC, link it to this trade, we can get him the documentation instantly on this trade and say, are you backing us up for any default on [audio break], so they know their LC links to this?

MR. : Right.

MR. : And then they have some sort of a give-back, you know, basically, you know, the intention is in three months to fund this out. That's what you're being paid for now, and we're

going to leave another carrot out there. So we're not, we're not going to die if we have to hold it because we're still getting paid a spread, maybe 50 bits--

MR. : Uh-huh.

MR. : Or whatever it is, and, you know, he's got an incentive to, and the banks have incentive to roll because they get more fees. I think that work-- [audio break]. And who knows, a week from now, we [tone] and there is no market. Nobody will fund anything.

MR. : Uh-huh.

MR. : So Joe would be nuts not to do this like over the weekend and try to [audio break] right now.

MR. : Yeah, I just wonder how quickly we could get these banks to approve, you know, an LC for these guys. I mean, like RBC, I've heard, is in pretty much disarray right now, you know, just to mention one, and I just don't know, from a timing perspective, if we're better off trying to jam that through quickly. You know, I

pab 8

don't know.

MR. : Why would that be easier? That's got to be harder. They've got to review documentation. What are they getting into? What are their risks? Remember the whole thing with [audio break] the default link-up. I just think about the lawyers that got involved the last time--

MR. : Oh, no--

MR. : [Inaudible] Mahonia, all of this mess.

MR. : Yeah, I don't disagree that--I think the complexity of the documentation is going to make it a lot tougher, but I'm just, even a vanilla credit approval on a standby LC, I'm wondering how realistic that would be for Enron to get it through in a week or so.

MR. : Right. But if they're going to pursue a path, I would just, if we've got to give them the best [inaudible] if there's no default swap market, and we--

MR. : Right.

MR. : We have, basically,

pab 9

a--there is no way we're going to [inaudible] holding this thing, Joe, for three months--

MR. : Uh-huh.

MR. : --all ourselves. I'm sorry.

Would we do it if we can access the default market, and you pay that cost? Yes. Can we access it? Not today.

MR. : Right.

MR. : So here's your best shot, 100 each, maybe get three [audio break], and if you can gather up whatever piddly LCs you can, and if we can go to two of these other guys for big shares or pay them a lot of money, this is what you [audio break] counted on, and forget about the concentration about the documentation because they're going to look and spend an inordinate amount of time trying to see how they're getting screwed on the documents.

MR. : Right.

MR. : And try to make it very clear for them

MR. : Uh-huh. Uh-huh

MR. : Because we can put that in front of people Monday. We can't [audio break] people Monday.

MR. : Right.

MR. : It'll be impossible.

MR. : Right. And I mean Joe's distinction that, you know, people like a funded asset better than an unfunded. That's true, but if you basically get the yield up on the standby to where they're indifferent, they shouldn't care.

MR. : Why the [tone] would they care?

MR. : And then--

MR. : And, actually, by the way, why not do the LCs very short term, and then we have [audio break], right?

MR. : Uh-huh.

MR. : Short-term, with a fund-out, right? So, basically, they know that if this isn't restructured in six months or a year, you know, we're all going to roll into a funded

part of this deal, and we would draw on them--

MR. : And then they could immediately go back to Enron.

MR. : Well, they can immediately go or they'd just be, yeah, but they immediately become partners with us in any of the cash flows coming out of the prepay, under the normal schedule.

MR. : Right, or worst case, I mean, they've been drawing upon their LC--

MR. : To make a [inaudible].

MR. : And then they have [inaudible].

MR. : And that's very simple.

MR. : Yeah.

MR. : And so it makes it a very short-term--want to get Rick on the phone, and let's run it by he and Rob or--

MR. : Yeah. Yeah, why don't we do it? Hang on.

[Pause.]

MR. : George?

[Pause.]

MR. : They're not in. I'll try to get them and call you back, but I think, I think you're on it. I mean, I think if they want to, you know, it kind of escaped me for a moment. They actually want to get this done at the end of the month, right?

MR. : Exactly.

MR. : Yeah. Yeah. That's something I've forgotten in the flurry here. So I think your plan is probably the way to go.

MR. : Okay.

MR. : And we haven't missed any possible investor, right? There's no way there's a money market investor that will take a one-year piece of paper, and maybe there is, but we could do that later, too.

MR. : Yeah.

MR. : There's nobody--he's so concerned, and rightly so, about putting a new price point out on the market.

MR. : Yes.

MR. : Which is why he's got to do this close to the vest.

MR. : Right. Right. And I think you do it, we were thinking you'd do it with two or three banks, and you know get them to take big chunks and pay them a bunch of money.

MR. : Right.

MR. : And just keep it out of the mainstream.

MR. : Right.

MR. : And basically say, Joe, the alternative would be that we were probing was instead of paying 200 to three banks and get any info out on the market, it could be as much as paying 300 to us to go to the default market. So--and we'd give them those two ideas.

MR. : Yeah.

MR. : So is 100 basis points at least for a one-year deal worth it to you, 3 mil--you know, to keep that price point out of the market? It might be, because--it could be, I don't know, but at least we'd say that's what we think

right now, because there's no liquidity, it might have to be.

MR. : And I think there's, there's a little bit of an arbitrage because I think that some banks, like RBC, and some other ones that I've mentioned, I think they'll do this for less than, you know, 300.

MR. : Yeah.

MR. : So I think he comes out ahead that way, and you still keep it relatively quiet--

MR. : Yep.

MR. : --between those guys.

MR. : And I think you're right, and to try to hit the time frame, you've got to do it with LC backup, so that they don't get, you know, mired in all of the minutia.

Now the interesting thing would be, you know, in the past, whenever we've done the standby LCs, we've participated in that, you know, which, in essence, means that, you know, we've taken on the Enron risk.

pab 15

MR. : Yeah, here we would just, we would just deal, and just not get an LC big enough for the deal. So if we did a 350 deal, and we got 250 worth of LC or something like that.

MR. : Yeah, which I guess the next question is, well, how much exposure would we take?

MR. : Exactly.

MR. : And then how are we going to cover up on it?

MR. : You know what my argument would be there? I would use the, I would equate it to how much runoff--

MR. : Runoff, yeah.

MR. : --[inaudible] between now and--forget about what's runoff because [tone] there's no way Jim and Chris are going to take that argument. We'd say what are they going to runoff in the next, say, [audio break] months, which, by the way, it's going to be like $150-200 million, but some number there to say pretty much it's 50 million bucks every 25th of the month. So, you

know, if we commit this, we're getting it back pretty quickly in total exposure.

MR. : Right. Right. And do you think we'd just go naked on that or do you think--I mean, obviously, we're not going to have enough treasury I think to buy--

MR. : Well, that's exactly right. I mean, what do we do?

MR. : Yeah.

MR. : You know, we could force the company to pay us a higher spread or we could use our fees.

MR. : Uh-huh.

MR. : We could use our fees.

MR. : Right, but I don't think that's--I don't know. I don't know.

MR. : It just doesn't--

MR. : I think we're naked.

MR. : And then we'd just buy off into the runoff, try to get them to buy off into the coming runoff over the next six months or so.

MR. : Yeah. [Inaudible] a lot

in six months.

MR. : Yeah. Well, let me try to catch Rob and Rick, but I think, I think that's the plan.

MR. : Okay. bye.

MR. : All right, man.

MR. : Bye.

[END OF TAPE RECORDING.]

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T2243

1

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON GOVERNMENTAL AFFAIRS

In the Matter of the Collapse of Enron

J. Dellapina, (AT) 021

September 14, 2001

15:11:53 (1 of 2)

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

P R O C E E D I N G S

MR. : Rick Walker.

MR. : Hey, it's Jeff.

MR. : Hi.

MR. : How are you doing?

MR. : Okay.

MR. : Did [inaudible] get you guys? He's trying to reach you and Rob.

MR. : We talked a little earlier, but it was kind of in another context, but I know he's given thoughts, and he basically said, you know, kind of the syndicated club LC was kind of where he was coming out.

MR. : Yeah. I mean, my thought is this is the only thing we could practically do very quickly.

MR. : Yeah.

MR. : We fund, we get the LC, and there is an incentive for those guys to convert to a [audio break].

MR. : I don't know if he's going to, yeah, I guess I didn't catch the nuance about

the--

MR. : Well, what I'm saying there--

MR. : --incentive to [inaudible]. Yeah, I just didn't hear it. That's all.

MR. : Yeah, and I think the juice with that--this is my idea--Joe, if he just gets the LC versus a funded loan, you know, and there's no juice for, you know, there's no reason why somebody would charge less on an LC than they would on a loan spread--

MR. : Uh-huh.

MR. : --which we don't think there's really a big arb, but we're going to charge them 50 bits just to carry the assets anyway.

MR. : Uh-huh.

MR. : So what we'll then say--Joe will feel like he's paying an extra 50 bits, and he's right. So what we'll say is, okay, then what we'll do is we'll place that LC which has, the LC they can do so fast, right? If we just

share the existing documents, we could show it to him, you know, Tuesday, and tell those banks they just have to write an LC that can be drawn only if there's a termination event on this contract, right?

MR. : Uh-huh.

MR. : And they would do that very quickly. But then we price it just to have incremental fees that they collect if they convert. It goes from a one-year LC to a three-year funding.

MR. : Uh-huh.

MR. : And the reason why is you hold back some of those fees, that if they go to the funding, then Joe effectively gets 50 basis points back from the loan spread because we're going to carry that asset at that, and we'll have a provision where it's like a one-year deal goes to a three, but we would basically change the structure.

MR. : Okay.

MR. : So I think that probably works best for him, but the spreads we're talking about enormous, right? The default swap market for

these guys are off the charts.

MR. : Two-fifty.

MR. : Yeah, at 250, if you can get any--

MR. : Two-fifty no liquidity.

MR. : Exactly.

MR. : It's probably 200 base, 250 offer, shift[?] to[?] liquidity, but who knows when that'll open up. It could be soon, right?

MR. : Yeah.

MR. : But my view is to these guys it's either you pay us an obscene amount of money, way beyond that 200/250 basis points, to take the field down, right? You either do that, and I mean an insane amount of money, which we think at least gives us a chance to get out in the next couple weeks, and default swaps the next couple months or what you do, and what's the benefit to that, even if it costs you an extra 200 basis points? Well, you know what? Nobody will see the price point. And what does that mean to you on the next billion dollars of debt? Probably

pab 6

a lot.

The other alternative is you open it up to maybe three other banks, and you pay them the ransom price, but it's not quite that high.

MR. : Uh-huh.

MR. : Now those guys have that ransom price. So I think the best route for him is going to be, you know, pay whatever it takes to get those LCs done, try to get like 150 bucks [audio break]. Believe me, Bank of Boston struggled with it, and they sort of did it because they sort of trusted that we had done it, but there are a lot of complicated provisions. We'd have to ensure them that they are covered on both sides for the gas risk and all of that good stuff.

MR. : Uh-huh.

MR. : It's not that easy. I had to go up to Boston, go through like ten of them in a room [audio break]. If you could do this deal next week, you do anything as soon as you can. There's no point to waiting, unless they're that liquid.

MR. : As usual, I'm doing too many things at once, and so therefore I'm--

MR. : I know. You didn't pay any attention--

MR. : --therefore, I'm confused. [Inaudible] do it as a club.

MR. : I'd say we do it as a club.

MR. : That's what I thought, because it felt like you kind of came around to the other end.

MR. : But the thing I want--I think you want to also pitch it that we're sensitive to your issue of putting a price point out there. With even as many as three or four banks, that's 200 basis points.

But the only way we're willing to even think about it Joe is going to be at an insane price that will give us a very good chance of getting out of that thing with default swaps in the next couple weeks.

What's the benefit of that? It's probably

going to cost you 150/200 basis points more than doing the club deal, but having said that, nobody else sees the price, and that incremental cost could be worth it.

I don't think you'd want to do that deal, and quite frankly, I don't think we'd recommend it.

MR. : I'm not sure we'd want to do it.

MR. : We don't really want to do it. Even if it's 400 basis points a day, we probably don't want to do it.

MR. : No.

MR. : No. So you cobble together what LC exposure we have today. We put together one or two other banks, and you just do the deal, and you just do it "rapido."

Now, from our perspective, we're probably rolling off another 150 in the next three months.

MR. : Uh-huh.

MR. : So, you know, for Christian, blah, blah, you know, I don't think they should have a big problem with the 150, but they

will. But, I mean--

MR. : Yeah.

MR. : --keep in mind, if this company goes bankrupt in the next three months, it's because the whole "fricken" system is wiped out.

MR. : Right.

MR. : It has nothing to do with Enron. That ain't happening in three months. So you're going to be getting down significant exposures. So I think, and, plus, you know, we're helping, you know, helping them work through a problem, getting paid for it

MR. : Yep.

MR. : Nothing slows down. Those reductions just keep happening. Anyway.

MR. : And they do keep happening.

MR. : They do keep happening. [Inaudible] bucks a month.

MR. : So--

MR. : We will have net gotten

down like 450 this year.

MR. : Yeah.

[Tone.]

MR. : And we will do that, while also maintaining a helpful posture with the client.

MR. : Yeah.

MR. : So should we get Rob and Joe on the line? Because I think we should talk to Joe and say this is what we're thinking about. Why don't you think about it over the weekend because we don't want to waste time here.

MR. : Yeah, we haven't gone, you know, to get slapped around on this yet.

[Tone.]

MR. : We can see if Rob's around. Hold on. I guess I probably ought to get George, too, huh?

MR. : I'll get George; you get Ron.

MR. : Okay.

[Telephone ringing.]

MS. : George Sarice's office.

MR. : Hi. Is he there?

MS. : He is on the phone.

MR. : Okay, it's Jeff Dellapina and Rick Walker. Is there any way he could pick up?

MS. : Hold on.

MR. : Rick?

MR. : Yeah. I couldn't find--

MR. : We've got to find [inaudible], man, [inaudible]. You know, we're going to go in and say, and we'll get blasted about all of the existing stuff. [Tone.] that insurance paper is worthless. This company [inaudible].

MR. : Hey guys.

MR. : Hey, G-man.

MR. : Hey.

MR. : I was just trying to give Rick a little flavor of what our best proposal was. He was, of course, you know, playing with his [tone] Palm Pilot, and he was ignoring everything I said. So maybe you--

MR. : It's a club LC. I told

you, I told you exactly what it was going to be up front, and then you kind of--you tried to fool me into thinking we were back to the heads-up deal.

MR. : Yes. So just, in summary, again, I think, George, our best guess is maybe we can, maybe we can pull the old tap dance, and explain to credit that they've got 150 rolling off in the next three months, and that's the kind of number we'd like to hold, but we fund the whole thing, crank documents out by Tuesday, show them to Enron and the banks that we identify and say we want an LC that basically pays out only on a termination drawing under this deal, so they get to see the deal, and they get to see that it is a performance risk.

MR. : Right.

MR. : And only if they don't perform and Enron Corp doesn't pay us out, do we draw, right?

MR. : Right. Let me put you on hold for one second. I'll be right with you.

MR. : Okay.

MR. : See, he doesn't understand either.

[Tone.]

MR. : Hey, Rob just walked in.

MR. : Hey, Rob.

MR. : What's going on?

MR. : We were just sort of thinking, well, should we tell, maybe the thing we ought to do is sort of tell Joe what we're kind of thinking about on the prepay--I just, that's you can trash that--and let him think about it before, you know, he sends us to go get our head lopped off.

[Laughter.]

MR. : Actually, that probably makes some sense.

MR. : The [inaudible] part about that is if you guys can't travel, I'm going to have to step in the room, when you guys are on a conference call.

MR. : You know, as I think about it, the kind of route we're thinking about--

MR. : LCs, it's all about the exposure we hold on our end.

MR. : Yes.

MR. : That's what it's all about.

MR. : That's exactly right.

MR. : Yeah, and that was the question we had discussed a little bit earlier.

MR. : And that's, [inaudible], that's when we get our head lopped off.

MR. : Rob, I'll have to separately go through with you what's on the books now, what the runoff is, what insurance companies are backing us now because they're all going to, I mean [tone] [inaudible] [tone], anyway--

MR. : [Inaudible] know that for all of the existing prepays, and then obviously I've got to [inaudible] and talk about everything else we've got.

MR. : Okay. I can get that info. So let's assume we roll off 50 a month for the next three months. So we propose, and we're

trying to help the client here, right, so? We're trying to make these payments.

MR. : Yeah, and we're telling ourselves that.

MR. : Yeah, we're still trying to tell ourselves that.

So they, they keep 150 of ours, which we basically roll down by month's end, by year end, and we try to find another, you know, 300.

And the idea we were thinking about, George and I, was that given that it really is not that easy, as we experienced the last time, to get other banks to get into this documentation--

MR. : Right, I remember.

MR. : There's just a lot of, they don't understand it. They have to do their due diligence to make sure they're not getting screwed in some sort of a settlement. It gets sort of complicated.

What we're thinking of is, if we do it in two steps where we crank the documents out, we can pretty much get out by Tuesday or Wednesday, and we

gave them to the company and the banks, and the LCs that would have to be written in favor of us would basically go to, you know, backing up a termination notice.

So they want[?] the document that shows that it's a performance-related deal, and they might get some comfort because that's not subject to an automatic stay in bankruptcy, blah, blah, blah, but whatever. [Inaudible], see how it works in a meltdown, and we'd say only if we made the drawing statement on Enron Corp and they didn't pay would we come to you.

[END OF TAPE RECORDING.]

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1

UNITED STATES SENATE

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PERMANENT SUBCOMMITTEE ON GOVERNMENTAL AFFAIRS

In the Matter of the Collapse of Enron

J. Dellapina, (AT) 020

September 14, 2001

15:11:53 (2 of 2)

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P R O C E E D I N G S

MR. : --the LC they'd write, but we structured a deal such that it's sort of like a one-year LC that, you know, they'd have, they'd have an economic incentive post-closing to turn that into a funded deal, and the reason why we want to turn that into a funded deal is, from the company's perspective, we're going to charge--probably charge them 50 basis points to carry the assets, at least, and he doesn't want to double pay for the risk; pay the, you know, the LC spread, which George is conservatively saying, and appropriately, it's going to be the same as a loan spread.

So maybe we hold back some of the fees, and we tell the banks, you know, you get X fees now and then once we, once we do a funded, convert this to a funded deal, you get the balance of the fees. And from the company's perspective, if we charge them 50-60 basis points to hold the assets, you can get that back at some point.

MR. : Yeah, I don't know how

those, I haven't really thought through those staged fees, but I still think the concept is where we need to go. I mean, we obviously haven't kind of worked out the whole fee arrangement.

MR. : Right.

MR. : You know, we probably want to noodle on that a little bit, but I think the bigger thing is, to get this done by the end of the month, we think the standby thing is the way to go.

MR. : And you think you can get banks to do this, to do the standby LCs by the end of the month?

MR. : Well, I mean, from a credit-approval standpoint, you know, at least, you know, complexity of the transaction, it's pretty simple.

MR. : Right.

MR. : It's just do you want another $100 million of Enron risk if we pay you X? You know, as far as a documentary exercise, it's not going to be that big of a deal.

MR. : Right.

MR. : The question is can we find the capacity, and I think there probably is some capacity out there. I'd want to sit down with, with Kelly and talk to her a little bit about it, but I think when you start talking the fees and the spread that we're talking about, we should be able to loosen things up.

MR. : But, I mean, are we still talking about a 350 prepay here?

MR. : Apparently, I guess more or less.

MR. : Yeah.

MR. : I mean, actually, I think the answer is, I think you kind of have to start talking about banks--

MR. : Yeah.

MR. : And you've got kind of a standard, the standard objections that we deal with. You know, there's, there's, first, there's the whole education process over the documents, then you're going to have the, I can't remember who it was last year besides--didn't we have somebody

besides Fleet last year?

MR. : We had B&P looking at it for a little while.

MR. : Well, somebody else who's going to say, well, we want part of the trade--

MR. : Right.

MR. : And I guess the question is there's what universe of banks out there, of Enron banks, you know, kind of have no capacity to do the trade kind of like Fleet did.

MR. : No, but there is no trade here. That's the thing.

MR. : That's true.

MR. : There is no trade. We--this one has no trade in it, so--

MR. : Yeah

MR. : It took us about two weeks to get Jim to really believe that, but he did eventually believe we weren't lying to him.

[Laughter.]

MR. : You're right. I mean, they--

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pab 6

MR. : I bet we're going to have to deal with that again.

MR. : No, they'll ask about it.

MR. : And I think it's a matter of, you know, who, I mean, like, for instance, is anybody out there good for a $100-million LC?

MR. : Well--

MR. : Is anybody out there good for a $50-million LC?

MR. : Yeah.

MR. : So it's got to become what do you think we can realistically cobble together, and maybe that adds up to $200, and then we say, okay, well, we'll do 100.

MR. : Yeah, I don't disagree with that analysis.

MR. : And I would imagine if we could cobble together a little more, they'd take it.

MR. : Oh, sure. Sure.

MR. : Yeah.

MR. : But I think that the point

here is, yes, it's an LC, but we're going to price it attractively enough to where it would make them whole or near whole what the yield, what the yield on a funded loan would be, and I'm thinking people ought to be indifferent for that. I mean, if anything, there still is a real capital boost on a performance letter of credit.

MR. : Yeah.

MR. : That's just reality.

MR. : And that we think--what do we think the number is, 250?

MR. : Oh, as far as the yield?

MR. : Yeah.

MR. : Well, I was thinking it would have to have some type of an LC [inaudible], okay, somewhere between 150 and 200 basis points.

MR. : Okay.

MR. : And then we'll have to put an up-front fee on there, which is going to be a function of the size of the commitment. But, you know, I would imagine, for $100-million commitment, you know, you'd have to be talking 75 basis points

or so, and I guess the question is, and this is where we have the kind of staging of the fees, and the tenor, and all of this kind of stuff. If they're going to pay those types of fees, are they not better just going ahead and making this like a three-year letter of credit, and then, you know, if they, if they want to negotiate a funded deal later, they can.

I don't know that Enron would necessarily care.

MR. : Wait. So a three-year LC--

MR. : I guess my question is would Enron care--

MR. : So I guess my question is why are we trying to push this into a funded deal, given the prices we're, the spreads we're talking about on the LC?

MR. : No, because Enron--because we're going to charge Enron like incre--they're going to pay double for the risk, sort of. So they're going to pay, the LC is going to be paying

[inaudible] Enron risk, then they're going to pay us to carry this asset.

MR. : But we're only going to charge them like, what, 50 basis points or something usually?

MR. : I don't know. I mean, it depends what kind of schlocko banks you bring into the deal, you know?

MR. : Okay.

MR. : All right.

[Tone.]

MR. : Hey, Dellapina, how much are you go--are you going to charge George to do this deal?

MR. : I don't know. [Tone.] He's got to know the default swap market is bad at the moment.

MR. : Yeah. I'm up for it. Ready to go, team?

MR. : Right.

MR. : Hold on.

[Tone.]

pab 10

MR. : Hi. How are you guys doing?

MR. : Fine. What's up with you?

MR. : Oh, you know, we're hanging in here. Lisa is standing by. What's going on?

MR. : Well, we've been, we've been thinking about, you know, what we want to kind of what we can do for you, and I think we want to just kind of give you a "heads up" as to what we're thinking about and maybe ask you to just think about it over the weekend before we go kind of into internal battle.

MR. : Okay.

MR. : I'll start and then kind of defer to Jeff and George, but I think what we're thinking is kind of a club performance LC that we would have in place at the "get-go."

We'll come back and discuss the specific pricing range, but something that would then be sort of structured as I think we were thinking like a one, one-year LC that, to try to figure out

conceptually an incentive pricing mechanism where the banks would want to conver that into a funded asset.

Because just--I think the thought is, you know, to get something together pretty quick, the performance LC is probably the quickest way to go, but obviously we'd be carrying the funding, and if we incent people to, to take that pro rata onto their own balance sheet, that is going to bring your overall costs down ultimately--

MR. : Right.

MR. : --because of what we'll have to charge you just to carry the asset.

MR. : Right.

MR. : We just don't think it's conceivable, Joe, that even if we do a deal by month end, given the experience we've had, given the way the lawyers will look in the documents to try to find ways that their banks are being screwed or potentially going to have to suffer in a meltdown. We have to give them something simple to evaluate.

MR. : [Inaudible.]

MR. : It took Bank of Boston way too long, and I think the other banks would take longer. So I'm just trying to say, you know, what you issue is a letter of credit. We show you the documents, we show you what the termination event is and what the drawing statement is to Enron Corp, but that is the drawing statement that goes back to you if, in fact, we melt down.

So, really, at this initial phase or this circling phase, you give them something simple to approve, which is not a structure, it's just a credit [inaudible].

MR. : I'm sorry. So they have a performance LC at the end of this month, and then you want to incentivize them to basically participate or, or what [inaudible] to Mahonia wrote [inaudible]?

MR. : Basically, it would be to migrate it to the Bank of Boston structure that we have the papers on, but that's going to take longer for them to absorb and understand.

MR. : Okay. Now does it matter, from the bank perspective, if this is a physical versus a financially settled deal?

MR. : You know, the only thing I could think of, Joe, is that--no, I can't comment on that. I don't know the answer to that right now.

MR. : Yeah, it wouldn't matter from the performance LC perspective.

MR. : Well, wouldn't it? I mean--

MR. : It might.

MR. : The performance LC, do you run the same issues we run with all of the sureties [inaudible]; physical performance, as opposed to financial performance.

MR. : Right.

MR. : If it really is a performance LC, we're all going to need a commercial deal.

MR. : Right. But if, but if we're going to, you know, rapidly convert this into

a funded deal, rather than a performance LC, you're talking about taking advantage of the capital log, then, you know, the ultimate deal, we really should be indifferent whether it's physical or financial, right?

MR. : Yeah. I mean--

MR. : I think we should be, I guess, from a, you know, if you had some guy, since we haven't done these, these LCs kind of the market [inaudible] like this, and if somebody is trying to get themselves, you know, talked into whether or not it's really a performance versus a standby, I suspect physical element probably, that helps that argument.

MR. : How long do you want to keep the performance LC in place before you convert this to a funded deal? It sounds like you want to do that pretty rapidly.

MR. : Well, actually, I think you want to do it rapidly.

MR. : Okay. They've got--

MR. : We're going to charge you

to carry this asset.

MR. : Right.

MR. : And that's why we're trying to, we're just contemplating that we'd like to set up some sort of incentive mechanism maybe by part of the fees are held back until we, you know, until we can convert this to a funded deal because we're going to have to charge you to carry that asset, and I know you were--you were, you know, you pointed that out early on that you think you could double charge that way.

MR. : Right.

MR. : So, from us, yeah, we'd like to get it off our books, too, but, you know, we're going to charge for it, so--

MR. : Okay.

MR. : Yeah, we--hopefully, not too long, and I don't know. Three months, I guess, would be a goal. Obviously, the LC couldn't be struck at three months because that would be--

MR. : Yeah, Joe, again. I think that, you know, with Enron, that always kind of

becomes the function of, you know, having the bigger picture view of your forward calendar, you know--

MR. : Right.

MR. : You know, your--well, you've just got, you've got air-traffic-control problems that only you guys know about.

[Tone.]

MS. : [Inaudible] told you Jeff called from our conversation this morning that we do have some reconciliation between ourselves to do, but that we are sending you $57 million today. APA gave us a margin call for 57.

MR. : Jeffie?

MR. : Yes. I literally just jumped back on. I'm sorry.

MS. : I'm not repeating myself.

MR. : So the answer is, I think a lot of those discrepancies are in the back offices, and the collateral for APA is being resolved, and we are wiring out $57 million of collateral calls today I think is what we were

called for.

MR. : Okay. No, no, I heard, Lisa. Yeah, that's great. And thank you very much for helping us resolve that. Unfortunately, the passage of time makes things more complicated to resolve things.

Thanks.

MR. : All right. So that'll all be taken care of.

MR. : Okay.

MR. : All right, guys.

MR. : Joe and George Sarice, I wonder, does it make any sense for us to have some kind of conversation with Kelly before we, you know, kind of before we really start seeing exactly which direction we're going to take this?

MR. : Do you want to do that this afternoon?

MR. : George, is that okay?

MR. : Yeah, that's okay with me.

MR. : Hang on a real quick second. I've got a 3 o'clock meeting with Bill

pab 18

Brown. Maybe we can do it maybe like in an hour, guys?

MR. : Yeah, around 4 o'clock?

MR. : Yeah.

MR. : Yeah, that sounds fine.

MR. : Let me call Kelly and see if I can get her freed up, and let's try doing that in Kelly's office.

MR. : Okay.

MR. : All right.

MR. : Are you guys going to go down there or do you just want to call in, call into George's line?

MR. : Yeah, I'll just call to George.

MR. : Okay.

[END OF TAPE RECORDING.]

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UNITED STATES SENATE

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In the Matter of the Collapse of Enron

Dellapina, (AT) 12 [1 of 2]

September 18, 2001

15:10:25

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : Richard?

MR. : Yes, Steve.

MR. : What's up?

MR. : I'm sitting here with Cerise [ph] and Traband [ph] or, as we just heard, it's actually, it's kind of like Joni Dorsett [emphasis on first syllable] became Joni Dorsett [emphasis on last syllable]. Somebody just recently pronounced Rob's name as Rob Traband.

MR. : Traband.

MR. : Kind of like Alex Trebek.

MR. : Traband. Yeah.

MR. TRABAND: There you go. I have a future as a game show host.

MR. : I thought that's what you did.

MR. : You already are one.

MR. : Exactly.

MR. TRABAND: I'm sure feeling like it.

MR. : So Rob has, to your highly justified inquiries about, "Hey, what's going on here, the--"

MR. : What the hell's going on?

MR. : You know how these guys, they're sending me e-mails with diagrams, and I'm like what the fuck?

MR. : You know--

[Simultaneous conversation.]

MR. : As if that took any work on their part.

MR. : Yeah, exactly.

MR. : Yes, I think they have on their server they have like--

MR. : Yeah, one of their folders is probably like diagrams for use in initial bank discussions.

MR. : Yeah, exactly.

MR. : But this will get the ball rolling.

MR. : That's right, and Joe never actually puts his name on any of those things.

Anyway, we're reaching the point of soon it will be just physically impossible to do, so I guess it's a good idea we have this conversation.

MR. : Well, Rob was just saying that he had a quick phone call with Ballantine--

MR. : Could we get a number, and we'll call him right back?

MR. : Who is that?

MR. : Chris [inaudible].

MR. : [Inaudible], okay.

MR. : But he had a quick phone call with Ballantine, and you know we're going to have to get a package put together. Rob, and the guys that work for Rob

are I think, they've got a bunch of portfolio review--

MR. : Yeah, constraints on their time right now, but--

MR. : That's an important part of your job.

MR. : Bottom line, I think we're going to need to take a, you know, to answer what the obvious question is going to be, which is, well, why would we want any more Enron exposure?

MR. : Uh-huh.

MR. : It's got to be a profitability question, so I think we need to get an idea of what we think we're going to be able to book.

MR. : Well--

MR. : So I haven't dug out my files, and I'm hoping yours are handier in terms of where our price point has been the last couple of times, and you know every, you know, the last five or six of these, we've managed to eke out, you know, a couple more basis points.

MR. : Yeah, I mean, here's the, here's the trick with this. Basically, what I would--Enron is, what are they rated now?

MR. : Triple B-plus, they are three-plus--

MR. : They're three-plus.

MR. : They're three-plus. So,

basically, I can tell you is what does a three-plus show in our system that, when we book this asset, what is it going to show, and it's probably going to say that we have to reserve and, you know, basically pay away something like 80 or 80 basis points or 90 basis points, right? But, in theory, you could PV [ph] the rest, right?

MR. : Right.

MR. : But I will say that the question becomes a little bit fuzzier because you don't really usually have a three-plus trading at 250 basis points in a default[?] for[?] that[?] market. So I don't know who's going to throw, you know, cast a sort of inquiring eyes on this and say, "Well, you know, this is probably inappropriate to mark this thing, you know, to whatever, whatever the, I don't know, the model is saying is an SBA[?]-neutral loan for a three-plus. I mean what does the model say?

MR. : I'd have to go back and look at it.

MR. : It's probably going to say like 100 basis points or something, I bet.

MR. : Yeah, maybe a little less.

MR. : Okay.

MR. : That's about right.

MR. : So the question is, you know, would people have a problem with us, you know, PV-ing

anything on something like this, when everything is still in question.

Now, if you think it's okay, I can give you what that number is. Conservatively, we could just start with the fees and then work our way from that.

MR. : Well, I mean, have we talked about the fees?

MR. : Well, I mean, George, I guess George opened up with some fee discussion, and then we should talk about what arrangement fee we would want.

MR. : Exactly.

MR. : Right.

MR. : And what I had thrown out was, if you are looking at kind of a 3-year deal and 1.75-year average, I think what I had talked about is a, for a big-ticket Libor, plus one-and-three-eighths and then 50 to 75 up front. If you wanted to buy down the rate, I thought it was 75 to 100 up front and one-and-a-quarter.

MR. : Okay. Seventy-five to one hundred of--oh, right, right, of fees, and then one-and-a-quarter basis points, right.

MR. : Right.

MR. : Which I thought was, I don't know. It seemed kind of low, but based on your previews on that, what do you think?

MR. : Well, I mean, we kind of

road-tested it with Enron, and we were met with shock and indignation. I think some of that was a little veiled, but--

MR. : Yeah, I do too.

MR. : I mean, I think, I think this is aggressive. I think you could probably get a bite.

MR. : Yeah.

MR. : Okay. A bite, all right. So, if we go that route--

MR. : I'm sure we could get McBride interested for this.

MR. : Well, remember, we don't have the insurance company this time, right?

MR. : Right.

MR. : Although I talked to a broker, and he still thinks he can get him--I don't know--which complicates it a little bit because we might want, you know, different--

[Audio break.]

MR. : We might want Joe to buy the insurance, even though we're not valuing it a whole lot.

All right. Well, I don't know. What do you think we should get? At least 50 basis point arrangement fee, at least, right?

MR. : Do you recall what we got the last time?

MR. : Three hundred fifty grand--or 350 million.

MR. : Somehow I thought it was--

MR. : I think the last one was, was the last one 350 or 500? I can't--

MR. : No, 350 we did, right, George?

MR. : Three-thirty-five or something like that.

MR. : Something like--I think it was 335 or 330.

MR. : Yeah, it was less than 350, but it was close.

MR. : And do you remember what your fees were, George?

MR. : Oh, actually, you know what? I'll pull out the fee letter right now.

MR. : Yeah.

MR. : How about I do that?

MR. : You know, I always get kind of the sanitized fee. I'm not sure what the gross is.

[Laughter.]

MR. : I have it in writing, brother. I have it in writing. I shared the letter with you. I mean, total transparency, man.

MR. : Yeah, I got a letter that looked--

MR. : You know, if I wasn't Italian, I

would get so insulted by that.

[Laughter.]

MR. : Instead I'm honored by it.

[Laughter.]

MR. : You're really, really good at this, you know that?

MR. : By the way, as I'm pulling up my Word documents here, and here's the mafia approach to getting bin Laden, right?

You get all of these, all of the, all of the bankers in the room from all of these tax havens, all of these numbered account zones, Luxembourg, Switzerland, you put all of the bankers in the room, and you say here's the deal, you put a picture of all of their families on the wall and say, okay, you guys are either going to stop making the money moves and make people come and pick up their money, and forget about the numbered accounts or we're just going to send out a note to tell bin Laden that the bankers gave him up and told us where the money was, and then one of you is going to die, so you might as well tell us where it is.

MR. : Sounds persuasive.

MR. : It's the mafia. I guess. That's what I've heard.

MR. : So we're going to subcontract a hit out to the Cosa Nostra?

MR. : Exactly. That was--

MR. : The "Wise Guys."

MR. : You know, a Catholic and a Jew put that idea together yesterday--me and someone else.

MR. : It's got to be good.

MR. : How ecumenical of you.

MR. : Okay. Enron, ready, the answer is--hold your ears, George--damnit. It was 330 million, and they paid an arrangement fee of 2.145 between Chase and Fleet. It was split equally between us and Fleet, so that is--

[Simultaneous conversation.]

MR. : Now what was--would somebody do that math? Does somebody have a calculator handy?

MR. : Sixty-five.

MR. : Sixty-five?

MR. : Sixty-five. 2.145 over 330, right.

Then, George, then you prepared a separate letter to him, correct?

MR. : I don't remember.

MR. : Which was I think something like another--

MR. : Did he just say something on top of what [inaudible]?

MR. : Yeah, I think so.

MR. : And for some reason, I'm almost

thinking it was, it was about anywhere between 800,000 to a million because, you remember, George, when we sent that money over?

MR. : I ended up getting like 375 out of that. I don't remember, I don't remember what you got.

MR. : All right. I remember you made me send a letter to you, so let me see if I can find that.

MR. : [Inaudible] guys in Jersey, that is the hour of the [inaudible] of man.

MR. : We can pull that up, but I think it was on the order of magnitude of around 750. I think that's what it was. So that wouldn't have been a whole lot of money then. What was 750?

MR. : You mean on the arrangement fee?

MR. : Yeah.

MR. : That sounds about right.

MR. : Yeah, it does.

MR. : That's another 23 bits.

MR. : Yeah, so pretty much, I don't know if it was a flat fee or if it was 25 bits, I don't remember. That's probably what it was, though.

MR. : And then we had, we had the insurance rap[?], and then we had, of course, our margin.

MR. : You had the margin which was seven-eighths; is that right?

MR. : I think it was--

MR. : Yeah, I think we started--didn't we start off at like five-eighths and then, courtesy of McBride, I think we ended up--

MR. : Yeah, at least seven-eighths.

MR. : Yeah.

MR. : Yeah.

MR. : Yeah.

MR. : Yes, I think that's what it was. It wound up being about 25 basis points on the whole thing that we got as an arrangement fee.

MR. : Basically, you know, obviously, there's work to do. I just, I don't know, how badly do they want this, Rick?

MR. : Rob?

MR. : It sounds like they want it pretty badly.

MR. : I think they do.

MR. : Pretty badly.

MR. : And if I think, this is a steal if they get that thing funded at, funded at 3--at 125, and you spread the fees. That's about what they would pay anyway, George, right, in fees--75?

MR. : Yeah, I mean, the fees that I threw out were kind of market, what I think market is.

MR. : Okay.

MR. : And, you know, so, of course, we

get that, also, and then I think for arrangement fees, I think we've kind of been around that 750 to a million sort of number.

MR. : Okay. Okay. But that's, again, spreading that over three years is really not a big, big deal. I mean, I would--I would think 1 percent--yeah, I guess, 1 percent. No, I mean, I would charge more than 25 basis on this.

MR. : For arrangement?

MR. : Absolutely. The bottom line is we've got the biggest exposure, and we're topping up again, so we should be paid the most money. I think we have the biggest exposure.

MR. : Well, we haven't exactly set[?] that yet, so--

MR. : Not in the deal, but just overall for the company.

MR. : Oh, you know, one of several. I think we may be at the top, though.

MR. : Two, they can't really, probably can't--

[Simultaneous conversation.]

MR. : I mean, just given how "spooked out" the market is right now, they probably can't do this without us, I mean, without us stepping up; is that probably true?

MR. : Well, especially in the time frame.

MR. : Yes, especially in the time frame. Yeah, I mean, actually, that's a huge point because, yeah, really the only other firm that they do these things with very much is Citi, I think, and maybe [inaudible] would prefer to do them with the red-headed stranger.

MR. : Yeah, so--hmm. I don't know.

MR. : I don't disagree with you that it would seem like we would get more of an arrangement fee this time, given the circumstances, given the market, given the timing.

MR. : I'll go back and see if I can find my notes on--

MR. : I'll go look in my office too.

MR. : --the last three that we would ever do.

MR. : Yeah, right. So, if the last time was seven-eighths, sixty-five, and we got twenty-five.

MR. : Yep.

MR. : So now we're sort of saying 125, 75 to 1 percent and 50.

Personally, what I would like to say is I would like to say I would almost give them two different interest rate exposures, depending upon whether they bring the sureties on board. Now I know we don't really value that,

but I would say like, you know, we do it at either one-and-an-eighth with or 150 without.

I don't know. I see these, I don't know. One, basically, you've got a little over a week to get these guys in.

MR. : What we need to have happen--

MR. : Whatever happened to the funded concept? I mean, how are they going to--how are we going to get a funded trade done in the next week?

MR. : Well, I think the idea was that we were going to do it ourselves over quarter end, and then October 2nd they were going to, for whatever portion we were going to remain, that we weren't going to hold, they were going to throw another[?] fee at it, and then we would by, presumably by year end, to get it off our, the asset off our balance sheet, we'd get the other two institutions in.

MR. : So we were going to hold--do this over year end?

MR. : No.

MR. : I mean, over quarter end?

MR. : Yes.

MR. : Yes.

MR. : Really?

MR. : Well, that's their ask, that's the ask.

MR. : What's the difference between--why

October 2nd for the LCs and not September 30th?

MR. : Because that's going to, you know, they have to report their usage and availability under their LC line in their financial statements.

MR. : I see. So they'd have to have evidence availability to--

MR. : Well, more importantly, they'd be evidencing availability to everybody else in their financial statements when they're--

MR. : No, I just meant for credit-approval purposes.

MR. : Oh, right, right, right.

MR. : [Inaudible] October 2nd, they were all--

MR. : And we actually know they've got it because we [inaudible] a big LC facility[?] form[?].

MR. : Okay.

MR. : And we can just look on the system and see they haven't drawn it or issued on it.

MR. : Cool.

MR. : Do you expect they'll be--do you expect that they will expect--

MR. : Well, actually, George, you know what the issue is? They've got the LCs out there. They're currently posted with the likes[?] of Duke and Williams and people like that. So they're going to pull those LCs away

from those trading counterparties and give them to us, and [inaudible], and then they'll have to turn around to Duke, et cetera, and post cash flow. So what they want is show the high level of cash at quarter end--

MR. : Okay.

MR. : --which then they're happy to swap out these transactions on October 2nd.

MR. : Do you think during the period that we're covered with letters of credit they will be expecting a lower, a lower margin?

MR. : Haven't talked about it. Haven't talked about it.

MR. : Hold on a second.

MR. : Not an unreasonable expectation.

MR. : It's kind of a funny thing because you're posing this one deal and then just talking about when it flips in the future, but you know we haven't talked about I don't think you can build a mechanism in--

MR. : Well, I think the way that you do that is you say, fine, but we're real serious about wanting to get this off and diversified, and so we'll give you breaks for 60 days, and then it's going to explode again.

MR. : Uh-huh.

MR. : That's right.

MR. : Which they want it to be off in 60 days--well, less than 60 days anyway.

MR. : I just wonder if they're looking for a lower rate during that time.

MR. : I think we need to talk about what it should be. You know, they haven't brought it up, but it makes sense.

MR. : In fact, before[?] they're raised at the end of the 60 days, whenever we roll it, it's going to be a market at that time. We can tell them what we think it's going to be, and maybe what we're going to push for, but we don't know what another bank will do it for in 60 days.

MR. : It can still flex[?].

[End of Recorded Segment.]

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 50 [2 of 2]

September 18, 2001

15:10:25

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : I like it. So what are you doing this piece for?

MR. : We haven't settled on that.

MR. : You're going to be back to it, letters of credit.

MR. : You know, Tunan[?] paper was a letter of credit, so--

MR. : I guess actually you have a blended risk, right? Because they want us to go naked on a portion of this.

MR. : Right. So that portion is going to have to be at--now, but you also have the question of, you know--

MR. : But, I guess, on the other hand, arguing against myself, it's for such a short term, it's blended risk. Do you not just say, you know, go along Jeff's lines, you know, this is where we're going to price it, and this is where we would think we'd price it once we term it out, if you will.

MR. : So the portion that--the 150 we're not going to be covered on is going to be priced at what you think the ultimate pricing is going to be?

MR. : Well, what I'm saying is it's for such a short term, arguing against myself, do you not just price it where you ultimately think--

MR. : [Inaudible] the whole thing.

MR. : Yes.

MR. : Well, they haven't asked for a discounted price.

MR. : Yeah.

MR. : [Inaudible.]

MR. : No.

MR. : Well, you know, not off the bat.

MR. : And then I did like the idea of kind of the stratified pricing between the surety and the nonsurety, whether or not they--

MR. : Yeah.

MR. : I mean, do we have a feel how other banks feel about the value of the sureties?

MR. : I mean, I think, in some ways didn't we have to kind of hold Fleet's hand through that surety discussion?

MR. : Well, essentially, since that article in the Journal came out, you know, a few months before all of us met last year, I think, about the movies[?]--

MR. : Well, I assume any bank that's been involved in any of those deals is going to have kind of our view on the sureties.

MR. : Well, not to mention the tragedy.

MR. : Not to mention the tragedy that's

affecting all of the P&C [ph] companies.

MR. : It's still worth something, and it still helps certain banks justify a hold[?] position.

MR. : Yes.

MR. : But I'm not, you know--but he could do that after the fact.

MR. : [Inaudible.]

MR. : If and when things calm down. How would we do this, by the way? Do you think we would just--I wonder how we would do this, just like if and when we are bringing new people in, will we just redo the whole deal on the second phase? Because, remember, we set all of those fixed-rate interests, fixed interests. I'm just trying to think how we would do that.

MR. : The quick[?] price on it, while you're thinking about that--

MR. : Yeah.

MR. : I gather that you're able to do a financial transaction now, as opposed to a physical?

MR. : Levy is out for the holiday, but he'll be back Thursday. I think we can. I think the CFTC rules changed a little bit.

MR. : Super, because, I mean, I think--

MR. : The reason why I don't like doing that is because it sort of takes it, you know, potentially sometime it could take it off of our desk. So maybe we will

have an either/or, physical or--

MR. : Yeah. I mean, Jeff certainly felt more comfortable that it would be easier, easy to restructure this deal when we bring the other banks in, if it were financial.

MR. : Yeah.

MR. : So it's going to be before--I won't be able to give you the final on that before Thursday, but I guess we could do that. I just--I don't want to lose the control of this or it'll start flowing out of our desk.

MR. : Right. The--I guess the other question, and I don't know that I feel strongly about it one way or the other, but at one point we had talked about, during this initial period until we brought the other banks in, setting this at a 1-year term and then restructuring it as a 3-year deal when we brought the other banks in?

MR. : Right.

MR. : I think that, certainly, the bridge component of this is easier if we do that.

MR. : Well, but to the extent, I mean, we're talking about this thing coming due within 60 days, is that what we're saying, if the LCs--

MR. : Well, I mean, it doesn't come due. We just have the LCs.

MR. : Well, we have the LCs for the first 60 days.

MR. : We were talking about whether or not they'd press us for a cheaper price because we had the LC, and so I think the suggestion was, you know, we could do that, but we might want that price to explode a little bit, notwithstanding--

MR. : Oh, it was a pricing [inaudible].

MR. : Right. And I think--I think if we're not discounting the LC, I mean, the pressure on them, I mean, they're not getting any benefit, other than a fund[?] slow[?] reporting benefit out of this transaction if they don't get the LCs removed.

MR. : Right. That's correct.

MR. : I mean, I think they're going to be under a lot of pressure to get that thing sold to a couple other firms.

MR. : You know what we need to do, as with one of our other transactions that are out there, not an Enron transaction, like, I don't know, don't we have one with like Ocean or somebody like that?

MR. : What about it?

MR. : We need to orchestrate something where, where our client screws up and that we actually have to, you know, make the, make the surety pay.

MR. : Yeah, exactly.

MR. : And then hope it does.

[Laughter.]

MR. : We've got to game the system.

MR. : I like them. I like them. Much too much time for things doing them right.

So what's the next step from here? Are we just going to sort of throw it out there?

MR. : I think the next step is we need to get our package together enough to, you know, Biello [ph], Wardel and Ballantine, and we need to have an all-hands conversation, and I know that they have been very hard to, you know, schedule because of what's going on up in New York MR. : Because of bailing out the airline industry.

MR. : Yeah.

MR. : [Inaudible] do you have very many swaps or less exposure on your desk with the airlines?

MR. : No, actually, mostly we're owing them money these days because oil prices have risen, and most of the stuff they've done was lower prices.

MR. : That's good.

MR. : But, you know, just hopefully someone will tell us when they want to pull the trigger.

MR. : So, I mean, I think the answer is we need to try to get in front of, you know, Biello and crew tomorrow or Wednesday and come to resolution, whether we're going to be able to do this or not.

MR. : Right.

MR. : Which means we've got to have the package out tomorrow morning. And if, you know, assuming if you can give us the, I mean, I know what the fees we're talking about, but if you could get us the MPV value, assuming that you don't have to reserve extra over a three-plus, we can tie that into the transaction, and I guess, in terms of, you know, kind of our normal issues of what are the volumes and stuff like that, not even relevant because it's a financial deal.

MR. : Correct. Why--all right. Why is that number relevant for this, what we're going to PV and stuff? They really don't care, do they?

MR. : Yeah, they do.

MR. : Yeah, they want to know--

MR. : No, I don't think they--you just tell them what the loan spread is, and you tell them what fees we're charging, and you could tell them the loan spread is, you know, if we just keep creeping it up, they're going to view that--I think we're just going to antagonize them if we start saying, well, we're going to take a portion of that loan spread. I think people are, you're going to antagonize them and say, oh, you're just trying to PV, you know--

MR. : Well, they know how this deal is booked.

MR. : Yeah.

MR. : And they know the economics on it.

MR. : Does SVA not give you the same kind of number?

MR. : We can--we'll come up with an SVA number.

MR. : Yeah, if you come up with the SVA basis points, just come up with the basis, yeah, come up with the SVA and use that as your PV number, before fees.

MR. : Well, I think what we'll actually do is just do, as though this were a loan, what the SVA is, the model--the model doesn't allow us to come up with a--

MR. : [Inaudible.]

MR. : Yeah, a up-front--

MR. : Well, if you tell me what basis points this loan has to be SVA neutral, then I can come up with a PV for you.

MR. : Yeah, okay. Okay.

MR. : Yeah. I mean, you can always do it on $100 million and then just flex it up--

MR. : Yeah.

MR. : You got it.

MR. : --when you get your final 250 approved.

MR. : Now do you have runoff numbers and things like that? I think Monty sent you a pretty good schedule on that.

MR. : I think so. I'll have to double

check it, but I think he did.

MR. : So you should be able to tell in the next three months how much is running off.

MR. : Exactly, which obviously is important. Now, as Rick was saying, I had kind of a high-level overview conversation with Ballantine on what we wanted to do here. I don't think that there is a whole lot of point in having a lot more conversations there. I think we just need to have a full conversation among everybody, and I told Ballantine the same thing, so he won't be surprised by that, just because, you know, his marching orders have been our [inaudible] Enron is too high, and so that's the refraining thing.

So we need to get to Biello and Wardel and convince them that this is a good deal to do.

MR. : I think one of the things we've done, though, is certainly, at least in the last couple of deals, we've evidenced that we'll manage our roll-off by spreading the risk to other banks, right?

MR. : Yeah. No--

MR. : So it's slowing down the roll-off a little bit, but, you know, it's always a difficult relationship[?] decision to just tell them you're never going to replace anything.

MR. : No, absolutely. I hear you, and I think that if we all give, you know, or participate in that

conversation, we'll get there, but I just, you know, as our view of what a surety is worth has evolved, we've gone from being comfortable with our pre-pay exposure, and I say "we" being Biello, Wardel and Ballantine, to suddenly saying we have way too much Enron exposure because we're no longer comfortable with the sureties.

MR. : Yeah.

MR. : So, you know, that's the issue as, okay, fine, we're--we may be--we're still allowing roll-off to occur and we're just slowing it down, that's all well and good, but if our exposure is already way too high, how do, you know, why are we even slowing down the roll-off.

MR. : Right.

MR. : And I agree with you, in addition to profit reasons, there's good relationship reasons. You can't just cut them off cold turkey, but that, that is the conversation.

MR. : If everybody, if every bank behaves like that, the company has got a serious liquidity problem; i.e., no new money till we get down to 400 million or the 200 million, then everything just sort of stops for the company.

MR. : Well, I hear you. I hear you. So I think we'll get there, but that's the--those are the issues we've got to deal with.

MR. : Jeff, do you remember the tenor of

the last deal we did for them?

MR. : It was 5-year, 3-year average for them.

MR. : Okay. So this--

MR. : Two-and-a-half-year average, something like that.

MR. : They're going to push a little bit on this one because it's a shorter tenor and shorter average life.

MR. : You mean in terms of pricing?

MR. : In terms of pricing.

MR. : Well, no, but I think you were trying to make it a bullet, close to a bullet, right?

MR. : On this one?

MR. : Yeah.

MR. : I didn't realize that. I think--

MR. : No, I hope not, but I thought that's what I heard.

MR. : I assume this is the same type of amortization we've always had.

MR. : Yeah.

MR. : Well, on a 3-year basis--

MR. : Let me tell you, let me tell you, if we go the physical route, the financial route, then we can never bring the sureties in.

MR. : Oh, right.

MR. : But, you know what, we could just wipe this deal clean, we could just close it in two months and just do a whole new one. We could always do that.

MR. : Right. It would just be replaced by an identical transaction that was physical that had sureties.

MR. : Yeah, exactly. Exactly. [Inaudible] be easier for [inaudible], yeah.

MR. : You end up in the same place.

MR. : Well, maybe one of the things we need to get straight with Joe on is just, you know, what's the tenor, what's the average life here before we can sort of start pricing some things out or before you can even really go for credit approval.

MR. : Well, I mean, I thought we knew that it was a 3-year deal that would have the normal amortization schedule.

MR. : So it's like 1.75-year average life or something like that?

MR. : Yeah.

MR. : Okay. All right. Well, then we're straight.

MR. : That's a good idea, yeah.

MR. : [Inaudible] the question because--

MR. : I think that's what we should do.

MR. : Okay. Fine.

MR. : What does that do to--George, what does that do to his price points out there if you do a bank deal at 100-and-whatever, 150 basis points/140 basis points? I know on a--

[Audio break.]

MR. : Again, I think--

MR. : They're stuck at one and a quarter right now, and they can't get a deal done, right?

MR. : Well, we've got one at one and an eighth that we're stuck on, but, again, that's a 5-year final 2.75 average and, you know, as you draw the tenor in, they're going to push you hard on the rate, but I still kind of stand by the numbers that I threw out originally as sort of market, you know, especially for a 1.75-year-average life. I think the fees, in combination with the margin, will probably be attractive to somebody.

So, I mean, maybe we try to push for that and get more of an arrangement fee for us is the exercise because, you know, they're actually fairly amenable to that. They'd rather pay us to arrange than to--

MR. : Yeah. All right.

MR. : And we can always have the McBride premium if you want to do that.

MR. : I think we're going to go way beyond the McBride premium here. It's just hard when there's no defaults for that market out there.

MR. : Has that market come back at all?

MR. : I don't know. I doubt it's anywhere under two and a quarter right now.

MR. : Yeah.

MR. : All right, guys.

MR. : All right. Well, I'll get--we'll get a package put together for the morning and try to get on the calendar.

MR. : Yeah. Obviously, I'm out of pocket all after--you know, late afternoon--

MR. : Right.

MR. : --on Cosmo [ph], so why don't we try to get a package out first thing in the morning and maybe try to get on their schedule. Are you around tomorrow?

MR. : Yes.

MR. : I was thinking like early afternoon.

MR. : You can break your Cosmo?

MR. : What's that? No, Cosmo doesn't really kick off till 3:00.

MR. : Okay. Good.

MR. : So, if we did something early afternoon. Now I don't know if that works for them. I think that's the other big hurdle is just scheduling these guys.

MR. : I do need to know the, kind of the PV number because--which I think we said we can figure out, just because I need to get [inaudible] kind of fired up for this.

MR. : Okay.

[End of Recorded Segment.]

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 004

September 19, 2001

10:43:17

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

P R O C E E D I N G S

MR. : Rob.

MR. : Yes. Hi.

MR. : How you doing?

MR. : All right. How are you?

MR. : Good. Are you all set? Are you writing up a proposal or something?

MR. : We're almost done putting it together. We're trying to get it as--the one thing I--I had actually sent Monte an e-mail on--

MR. : He's out. He's out.

MR. : Okay.

MR. : In Houston.

MR. : That--I--in fact, I was about to call you or to see if he was around.

The--the pre-pay runoff that he had sent me--

MR. : Yep.

MR. : --was just an aggregate number and it was starting in like July, and I was wondering if you guys had it by prepay starting at the beginning of the year.

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MR. : Give me one second. Let me open it up.

MR. : Sure. All right. So basically [audio break.] Do we have it by [?] is your question here. I think we do.

MR. : Well, and do we have it from the start of the year?

MR. : Yeah. We should have that, too. Do you remember what the file name was? Did we--

MR. : Let me see here. I got it.

MR. : See if he shoved this in.

MR. : Enron prepay.xls is the file he sent me.

MR. : All right.

[Audio break.]

MR. : [?]

MR. : Yep.

MR. : It doesn't have any of the runoff like that?

MR. : No. It's got one

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aggregate number starting in July.

MR. : All right. So why do we--oh, you just need to go backwards. Okay. Okay.

MR. : Yep. And even if I didn't have it by prepay, even if I had it in this format--the format going back to the first of the year, that would help.

MR. : Yeah. That's what I think I might just try to--

MR. : What do you have for July on your sheet?

MR. : For July, balance of 1.189 and runoff of 42.3.

MR. : Hmm.

MR. : Is that not what you asked?

MR. : I see that. The numbers look a little bit lower than this other sheet. I don't know why. [Audio break] numbers here today.

MR. : That would be great.

MR. : For the--for the

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year-to-date runoff down to June. Down to June, I saw runoff at around 237.

MR. : Two thirty-seven.

MR. : Down to [?] I see at 469.

MR. : I can make that work.

MR. : Okay. We'll just use that.

MR. : You got it. And I'm trying to get a--get something set up for early this afternoon, also.

MR. : Okay.

MR. : So I'll keep you posted.

MR. : Bye.

MR. : Bye.

[END OF TAPE RECORDING.]

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T2243

1

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 006

September 20, 2001

8:31:51

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

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P R O C E E D I N G S

MR. : Hello.

MR. : Hey. How you doing?

MR. : Good.

MR. : Good.

MR. : You returning mine?

MR. : I was returning yours and just kind of giving you an update.

MR. : Yeah. Because I had Ballentine on the phone yesterday about a couple things and then I said, "Hey, you know, what's up, we getting together," and he's like, "Yeah. I'm really struggling with this," blah, blah, blah.

MR. : Yeah. I know. What I've been--what I've been trying to do, and he's been dragging his feet on, you know, he likes to be fully bought off on something before it goes on.

MR. : Yep.

MR. : And we don't have time for that.

MR. : Yeah. We're sort of running out of time.

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MR. : So what I've been trying to tell him the past two days, and I think I've told him, you know, pretty directly last night and this morning, is, "Jim, we've got to have an answer today. We don't have time to get this done if we don't have this resolved."

MR. : Right.

MR. : And so we need to--we can't have everything buttoned up. We need to--we all know Enron. We all know the prepay. We all know the issues with both. Let's all get together and talk about it.

MR. : Right.

MR. : And so, you know, hopefully, you know, we can get collected today, because I got Lisa Billis [ph] calling me every five minutes.

MR. : Yeah. He told me now--I said, "Yeah, well, you know, it's about equal to the runoff for the rest of the year. So we just sort of delay on the runoff."

He goes, "Yeah, I know, but we've been

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counting on that runoff."

MR. : But we still have all the runoff year-to-date.

MR. : No. Exactly. Exactly. And I just--this is not the kind of thing you sort of publicly talk about, but--especially in the presence of a meeting, but, hopefully, everybody's got this thinking this way.

You know, again, it's in the issue of responsibility. You know, if we're really petrified of the client, that's one thing, but, you know, I mean, you can't--

MR. : I know where you're going here. I know where you're going here. If we just yank--

MR. : Yeah. You're pulling [?].

MR. : --credit support.

MR. : Yeah. You're pulling 500 off and you're just not helping them. You're fixing your problem, but slower than you'd like, but you are fixing it by getting other people in, so.

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MR. : Yeah, yeah.

MR. : So hopefully they're thinking like that, because, you know, it's just going to run out of [audio break] let them go to the bond market. But yeah, well, that's pretty--that gets pretty spooky, right? That helps--hurts us, too.

MR. : Yeah. Yeah. That's right. So anyway. I mean--

MR. : Okay.

MR. : I think the answer is is that, you know, Jim is afraid of Enron because of all the exposure and all the crap. He's gotten some [?] on Enron. Well, you know, we get that crap from him every time.

MR. : Yeah. That's why I say.

MR. : You know what I'm saying?

MR. : No. I know what you're saying.

MR. : And so we just need to get in front of him and talk, and I just got to get Jim there. You know, with Gary, it was real easy. You

just--he just said, "Hey, you know, this is getting elevated."

MR. : It's out of my hands. Exactly.

MR. : This is getting elevated anyway. Let's go talk.

MR. : Yeah.

MR. : So I just got to get Jim there. Anyway. I've got to run. I've got to head over to Enron for another meeting.

MR. : Okay.

MR. : But I did want to get back with you and give you that update.

MR. : You're thinking today?

MR. : It's got to be.

MR. : It's got to be.

MR. : I mean, don't you think?

MR. : I know it has to be.

MR. : I mean, we're out of time here.

MR. : We have to discuss with them--you know, you've got to really be convinced

that that liquidity is there to take us out.

MR. : And I think--

MR. : [?] the documents. It's not -- you know, it's not the easiest thing in the world to do.

MR. : That's exactly right. And so I just think we've got to talk to them.

MR. : Well, you're just going to have to do some sort of screening to say it's conceivable that they will be taken out.

MR. : Although I think that while that's important, I think to the extent we're getting covered by LCs, you know--

MR. : Those LCs will be short term.

MR. : The L--what's that?

MR. : Short term?

MR. : Well, I mean, it doesn't really matter. If the LC is about to mature, we're going to draw it, if it's not renewed.

MR. : Okay. [?].

MR. : So, you know, if we're

nr 8

covered by LCs, you know, effectively, it's syndicated anyway. That's how we syndicated the original ones.

MR. : Okay.

MR. : We did the--I mean, isn't that right? We did the prepay, but we syndicated an LC.

MR. : No. Of course. Of course. It's just, you know, that was a long time ago, a lot different market, and--

MR. : Yeah. I guess my point, though, is that they have access to the LC capacity, and so they don't need this--you know, so on a temporary basis--

MR. : I would agree with you [audio break] for us, but then the broader question, which we're going to have to at least have a view on, is, yeah, but--

MR. : Yeah.

MR. : --will this be syndicatable, because once you start drawing on those LCs, it's going to spook everybody.

MR. : Absolutely. So--

MR. : So if they say forget it, no interest in cooperating, and then you say, "Fine, we'll draw on your LC, you have to cooperate," that's going to spook the market.

So George is going to have to have a view that--

MR. : No question. And I think he's been pretty--I think he's ready to say that, you know, you--with the pricing we're talking about, you can go out and load up.

MR. : Okay.

MR. : You know, a couple of banks that will take a big piece.

MR. : Okay. Good.

MR. : All righty.

MR. : Thanks. Bye.

MR. : Bye.

[END OF TAPE RECORDING.]

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 20

September 20, 2001

13:40:50

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : --exposure.

MR. : This is Jeff.

MR. : Hey, Jeff. Rob.

MR. : Hey.

MR. : I've got Jim Ballantine on the line as well.

MR. : Hi, Jeff.

MR. : Have you got a couple minutes?

MR. : Yes.

MR. : I wanted to talk about the pre-pay, and your impression--I think Jim has spent some time really going through the maturities that we've relied on.

MR. : Yes.

MR. : And I think he may be starting, and this is Jim speaking, not Jim and [inaudible]--

MR. : There's a light coming over the horizon maybe.

MR. : But Jim I think is getting--

MR. : Lights [inaudible] on marble head.

MR. : I think, and I don't mean to speak for you, Jim, but I think you're starting to get comfortable that maybe the maturities do provide us more support than what the new[?] maturities[?] provided?

MR. : Yes, I'm leaning that way. We're

going to have a call at 4 o'clock with Chapnick at Morgan Lewis.

MR. : And then, so I think his bias, on the Enron pre-pay that we're talking about, is to actually use sureties, and I don't know if we can indicate also to a couple of other banks, but to use sureties, rather than to go naked. And wanted to visit with you--I know you had talked a little bit to one of the insurance brokers--and just wanted to get a sense if you had any idea whether they're even writing policies right now.

MR. : Well, you know, the words we're getting from the primaries is, yes, they're writing. The problem is that as the sizes get bigger, they have to access the reinsurance market. So I don't think they've tested, I guess, for a big, big $3-400 million deal because it--

[Audio break.]

MR. : It's going to the reinsurers. It's going to be painful.

MR. : Now I would assume that it's a matter of time before the reinsurers are back?

MR. : Yes, I think--

MR. : So, I mean, and I'm just trying to think real-time here, Jim, one alternative might be, you know, we start the surety process, and, you know, we commit to having it done within a certain time frame so that maybe, day one, the sureties aren't in place, but they will be in

place within 60 days or something like that?

MR. : Yeah. Maybe we use the LC and give them the option of either sureties or syndication.

MR. : Yeah. Yeah, something like that might work. My--

MR. : You're suggesting we don't syndi--okay. Because what I thought we were talking about is actually syndicating the surety deal.

MR. : [Inaudible.]

MR. : Yeah.

MR. : Yeah, well--

MR. : Well, I think that's nirvana.

MR. : Here's my notion. My notion is if there's a way to trade this exposure for other direct exposure to Enron, I think that's a good trade.

MR. : I see.

MR. : If it's surety wrapped. So--

MR. : And I guess my--

MR. : So the amount would sort of have to do with what we think we could do on the other side, whether it's, you know, whether it's through the company saying, all right, we'll ease you up over here or maybe it's, maybe it's some [inaudible] swaps, I don't know.

MR. : I guess my concern, Jim, and maybe the reason that we still tried to syndicate some of this is that most of what we, if you really get down to it, most of

our exposure is either trading exposure or the pre-pay, and we do have other exposure, and we talked about the effects[?] on getting rolled[?] under the [inaudible], which would help.

MR. : Right. We've got 560 of exposure outside of the pre-pays that's primary, right?

MR. : Yeah. I guess where I was going is I'm not sure that there's 350 or even necessarily 150 that we can point to and say this is what we're going to get rid of.

MR. : Well, my point is I think, I think I potentially could argue that anything we could achieve to reduce the 560, with the company's assistance, might be worthwhile if the quid pro quo is putting on surety-backed exposure. So maybe it doesn't have to be dollar-for-dollar. I don't know yet.

I'm saying that if we get comfortable with sureties, then, you know, maybe we put on some, you know, disproportionately large number of pre-pay exposure if the company says, all right, you know, for that we will knock off, you know, we'll do something about this $46-million [inaudible] or something. I don't know what it is, but some, some number, you know, gets taken care of that's direct Enron exposure, and I don't even know--

MR. : Well, you know, one thing that--yeah, one thing that might--I mean, I think we touched

on two of them. One of them is the FX exposure, but another thing we could do is talk to them about putting the mutual margining language in the ISDA with Enron Credit.Com. That's 100 million right there.

MR. : Uh-huh.

MR. : So, if you did that on the FX and on the Credit.Com, there's 160 million right there.

MR. : You know, I think now would be a great time to do something dramatic on the exposure, and if the quid pro quo is putting on insurance company exposure, then that could be a great trade for us. Well, that's a notion I want to play with.

MR. : Okay. Can I suggest that--

MR. : Yep.

MR. : --in parallel to that, under the assumption that they can[?] access the insurance market now, and we have to go down the path potentially of a syndication, you know, is there--

MR. : Probably syndication and credit derivatives.

MR. : I'm sorry?

MR. : Then I think the back-up plan is syndication and credit derivatives.

MR. : Okay. And when you say "and credit derivatives" for the full share?

MR. : Yeah--

MR. : Or for our uncovered--

MR. : Yeah.

MR. : Rob, this is where the rubber meets the road.

MR. : Yeah, absolutely.

MR. : You know, George is saying you could syndicate a bank deal at, whatever, 150, plus big fees, whatever his number is, but there is, one, there is really no cheap[?] defaultor[?] market at the moment and, two, the width of it is 250 basis points. So, if that's the case, then we're talking Enron, as we discussed early on, of an entirely different price deal.

MR. : Yeah, then I'm not sure we can do a deal. I don't think incremental, unhedged, exposure gets put on right now for Enron, unless it's a, you know, relationship-breaking event.

MR. : Well, I think it's a pretty critical financing for them right now. You know, maybe, maybe what makes sense is, one, for us to explore the surety discussion a bit more, and then--I'm just taking a look here--and then, yeah, at the same time we talk about what exposure we can get off here, and kind of--

MR. : Then, you know, I suppose the fall-back is, if this is a big relationship issue, the fall-back is a syndicated deal with some, you know, exposure trading, right?

MR. : Yep. Yep.

MR. : Now, on exposure trading, I'm assuming that replacement exposure counts for you. That's what's primary.

MR. : Replacement exposure counts, but the problem--the thing is, Rob, I don't want to trade for exposure that they otherwise would be willing to roll under a margin agreement. So, you know, I want to do both. If they're okay rolling this stuff under a margin agreement that we have now with Credit.Com and with--

MR. : On credit.com, I don't know. We're working on the FX line.

MR. : The FX, you know, I think we should--I don't see why they wouldn't do it otherwise.

MR. : Well, I mean, except that it uses up, you know, LC or cash that they wouldn't otherwise use up. I mean, we do a lot of FX business with them.

MR. : Right. I just want to negotiate carefully here. I don't--I don't want to trade, you know, 70 million of new pre-pay exposure unhedged for rolling the 70 million FX contract under a margin agreement. I don't think that's a good trade. I don't think that's a good negotiation because it sounds to me like you know, with a little, with a little work we can get it under there anyway.

I mean, Enron, Enron is under some pressure here. Every--everybody that has credit to Enron is probably, you

know, doing what we're doing, so I don't think it's, it's--I don't imagine it's going to be a huge relationship event for us to be, you know, talking to them about rolling some of these exposures under margin agreements.

So, if this pre-pay wasn't here, we would hopefully be doing this anyway, right? I mean--

MR. : Well, we are doing it anyway, but I mean I guess, you know, I've been trying to actively work on some of these items so that we can work our exposure down, partially because we've got high exposure, but also so that we have capacity to do this deal.

MR. : So we can do this deal.

MR. : And not necessarily this one, but to do new ones, and a little bit feels like I would have been better off not trying to work this ahead of time and offer it up now.

MR. : I know.

MR. : You know what I mean?

MR. : Yeah, but--and what I'm saying is I think, you know, you can manage that any way you want, but there is going to come a day, and I'm trying to manage this, as you are, that, you know, I feel like we're dangerously close to the day when this relationship could blow up. They are like one ask away from, from the deal we can't do. I mean, this is from Diello's [ph] mouth and, you know, we've got to be really careful here. So I'm trying to manage to

have sort of, you know, do this deal and still have some dry powder.

MR. : No, and I really do understand.

MR. : I know.

MR. : You and I both have a vested interest in this.

MR. : And I think one of the things I would point to is if you look at kind of the total MEA, it's, since the end of the year, it's come down, you know, very dramatically.

MR. : And everybody is, you know, getting pats on the back, but--

MR. : But it's not where they want it to be.

MR. : It's 560 million, if you look at it the best possible way, and I'm getting myself, I think, convinced that that is the right number. So now what do you do? Okay, it's not a billion-seven any more, it's 560. That's good news, but it's still 560, and you know how do we feel about that? I feel like that's a huge number.

MR. : You know, one other thing we could think about in the mix, Rob, is maybe the possibility of reducing tenor[?] on an existing deal.

MR. : Right.

MR. : I mean, I don't know. You know, would they be willing to trade up by bringing in tenor[?] on

existing deals? Pre-paids I'm talking about.

MR. : Yeah. No--

MR. : You know, obviously, we're most concerned about the next 12 months, given our view of the economy, but that might be an angle.

MR. : Right.

MR. : Something we could trade.

MR. : Yeah, I mean, you know, I think, Jim, the one thing, and I don't necessarily agree that that 1.7 doesn't exist because you always have the risk that--I love these bonds, and they're good, but you always run the risk that one of these insurance companies goes bankrupt and then you--

MR. : Right.

MR. : --you're naked on that piece. But having said that, I think the message that Rob, and Rick, and me, to some extent, communicated pretty hard, they've sort of honored in that they're not coming back and saying, "Come on, guys, you've had all of this runoff, could you replace this."

They're saying, we've told them you've got to come down, and they're sort of saying, "Could you help us sort of maintain this, but doing it in a way where for $4 you come off, can you sort of put one-half back on and help me with the rest of it, and then we'll bring new banks into it and we'll work it down."

MR. : Jeff, why do they want to hedge with gas where it is now?

MR. : They're not hedging, they're just, they're just, they do the back-to-back swap. This is--

MR. : This is a circular[?] deal that goes right back to them.

MR. : It's basically a structured finance--

MR. : It's a financing.

MR. : Yeah, it's totally a financing, which has piece of it, they've always had on as a piece of their capital structure, so--

MR. : Yeah.

MR. : So, if it reduces 500 a year--

MR. : Yeah.

MR. : --they have to do something with it, which is swap back.

MR. : So it's amortizing. Yeah, it's amortizing debt. I've got you.

MR. : That's exactly what it is.

MR. : Rob, do we include this debt in our credit stats?

MR. : No, we don't. It fits into their trading book and so, you know, effectively they've got, you know, it's monetizing assets from price risk management.

MR. : Yeah, it is a liability, though.

I want to--I want to--I'd like to understand that. It's something we do with a [inaudible], just, you know, as sort of a notation, you know, what the leverage is, including pre-pays. It's a little tricky, but that's one of the questions I had for you on this [inaudible].

MR. : Okay.

MR. : You know, I understand the, I think I, you know, I understand the request here. So I think, Rob, again, we've sort of done this before, let's itemize and maybe prioritize the exposures here, in terms of what has any chance potentially of getting, you know, dealt with, you know, from sort of easiest to more difficult and get a sense of what buttons we have to push here.

MR. : Okay. And, Jeff, I had a question in to Ann Marie, and maybe it's something that you've got some insight into, also. On our Enron North America limit for physical transactions, the 75, as the pre-pays are rolling down and off and gas prices come down, is that still the right number?

MR. : It may be slightly high--

MR. : But not--

MR. : The only issue--not egregiously high.

MR. : Yes.

MR. : And the issue is, if prices move up, we're going to be over the number again.

MR. : Well, and if we do this transaction as a physical transaction, which it sounds like we're moving back towards, we'd need it in place anyway.

MR. : Yes.

MR. : Is there any impact from the price changes on any of these replacement exposures that you're aware of, Jeff?

MR. : It shouldn't be from my side because everything squares up in margins in our books. So everything is margins.

I don't know, Rob? I mean--

MR. : No, not really. Most of these are lines that are in place. What we really need to do, I think that the two big things we need to do, in terms of priority, are get the foreign exchange under the margin agreement, which we're doing, and get Credit.Com under our margin agreement, which I'll get started on right away, and those are the two big opportunities to ratchet back exposure.

MR. : Right.

MR. : And that's right there 160.

MR. : What is their LC facility we have for them, Rob?

MR. : We have--

MR. : Is that a syndicated or a bilateral or--

MR. : No--

MR. : Almost 100 million.

MR. : The 100 million is bilateral, and it's pretty heavily used most of the time. It was originally 150, and we cut them back to 100, and that was pretty painful for them.

MR. : When is the syndicated LC facility due?

MR. : I want to say that that was a one-year facility, and it just renews.

MR. : So the hypothesis, with respect to that exposure, would be, you know, okay, guys, you know, we can take on some more exposure, but we'd like you to syndicate this LC line for us.

MR. : Well, I mean--

MR. : We'll roll it into the syndicated deal, and we'll take a share [inaudible] 100.

MR. : The problem there is that they will put this, the syndicated LC facility, the $500 million facility in place in order to get incremental LC capacity, and they rely pretty heavily on us, and others, to provide these bilateral lines to support their LC needs as well.

So, I mean, it wasn't a case of 500 replacing 500 somewhere, and we just didn't get--

MR. : No, I guess I'm saying that, you know, up-size it to 600, and we'll take some share of it, but not all 100, you know. Up-size the syndicated facility,

rather than bilats. Now I'm sure we're not the only bilat.

MR. : That's right.

MR. : So it's probably a bigger roll-up than that, but--

MR. : And then I guess the question really, and I'll talk to George, but I know that syndicated LC facilities aren't really everyone's favorite in terms of getting them syndicated, and we really got this one done on the back of the corporate CP facility and saying, if you play in one, you've got to play in both, and if you aren't playing in them, you don't get any other business.

MR. : Do you know how many bilat facilities they have?

MR. : I don't know the number, but I know kind of the amount. They've got like a billion dollars in LC bilats.

MR. : Yeah, okay. So we're like 10 percent already.

MR. : Yeah.

MR. : So that may not help.

MR. : What's outstanding, Rob, on that 100?

MR. : On our 100?

MR. : Yeah.

MR. : Well, it varies from time-to-time, but at times, and I don't know what's outstanding today, but

it goes anywhere from like 50 up to 100 over the course of a year.

MR. : Whatever that is right now, given that they have some huge amorts coming due, maybe they'd be willing to contribute that conceptually to our whatever ask we have; i.e., it's 100 now, if you've got 60 utilized, can we pull, you know, you're asking us for, what, 150 in the pre-pay? Can you give us, you know, can we hold back the 40 and revisit in 6 months? And we'll have a lot more amorts[?] at that point. We'll know what other asks they have in the first quarter.

MR. : Yeah, I mean--

MR. : It's easy for me to say this. I don't have a--

MR. : I mean--

MR. : I mean, whatever is not drawn on that now, that could be a term, you know, something we could say, guys, we're going to need that.

MR. : Yeah, I mean, we can certainly talk to them about that. It was not too long ago that we cut 50 million out of it already, and that, I know, caused them, you know, some pain along the way.

MR. : Jeff, what's happening today in the market?

MR. : Choppy. Gas is up slightly, oil is down a little bit, and oil followed the Dow down today.

Dow is getting 250--

MR. : Did you hear anything more on Calpine or--

MR. : No, I have not. I have not. Rob, I think Calpine is having trouble, the rumor is, posting margins to their over-the-counter counterparts.

MR. : Really?

MR. : Yeah, not a big surprise. I mean, you know, it's exactly what we talked about, that they could be perfectly hedged.

MR. : Yeah. I mean, not dissimilar to what happened to Reliant in December. They had the right hedges in place, but the margins--

MR. : Exactly.

MR. : Except that Reliant is a little bit bigger company. But, yeah, that's exactly--

MR. : Yeah.

MR. : So, no; no new market news there.

MR. : Let me ask you a quick question, Jim, because, you know, the timing on this is getting really tight, what--I want to make sure I understand exactly what the next steps are here. I need to talk to you, go through our exposure and kind of prioritize, you know, what we think we can do something with--

MR. : Right.

MR. : --and then how do we want to

handle this after that?

MR. : Well, then you have basically parallel paths. If it's--if we think we can get some exposure off here as a quid pro quo, then we proceed, in talking with them, theoretically, a minor matter of getting Jim and Chris on board--

MR. : Right.

MR. : --and work towards getting it surety backed. If it ends up being surety backed, then that's one path, and if we can't, then we have to have some other mechanic in place to limit the amount of incremental exposure we're putting on.

MR. : Right.

MR. : Okay. So, Rob, concurrently, why don't I, either with you or without you, start probing whether there is a market.

MR. : That would be great. In the meantime, I'll start working on kind of the quid pro quo.

MR. : Okay.

MR. : And, also, Rob, let's look at the credit stats with all of their pre-pay complications.

MR. : You've got it.

MR. : Okay.

MR. : Jim, are you doing that call in your office at 4:00?

MR. : Yeah, you want to join?

MR. : Yeah, I might jump up.

MR. : That would be great.

MR. : Bye.

MR. : Okay, bye.

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 23

September 21, 2001

15:06:01

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : This is Jeff.

MR. : Hey, Jeff.

MR. : Hey.

MR. : I've got Rick on, also. If you guys can hold on a second, I'm going to try to get George.

MR. : I thought George was out today.

MR. : Mm-hmm.

MR. : In some sort of meetings all day or training or some--either that or he's just avoiding my call, one or the other. That'd be the natural thing to do. Did you get through your meeting, Rick?

MR. : Uhh, I didn't get much. I talked to Biello [?]. I couldn't sweet talk him out of anything more than 35 million bucks, net.

MR. : God.

MR. : How do you [inaudible] get any new approvals for them? How do you do any new deals?

MR. : I don't know.

MR. : I mean, like, what have you gotten approved recently?

MR. : Reliant Resources.

MR. : No, I meant on Enron.

MR. : I guess the--well, [indiscernible]'s idea was no new exposure.

MR. : Was no new exposure?

MR. : I guess it was at something on--with the syndicated LC deals earlier in the year and that was, like [inaudible].

MR. : So they did a reset. Thirty-five is the only stuff he could replace.

MR. : Mm-hmm.

MR. : And that's obviously on a 350 deal, so, I mean, it's not like we can kind of be cute and say all of a sudden, all right, we'll do like a 150 deal and we'll take 35.

MR. : So, I mean, you know, who knows. Jim may want to close the deal with a quarter in and then decide to take it out elsewhere, I don't know.

MR. : Oh, you've got an underwriting approval?

MR. : Yeah. Well, you know, we've got a--we're going to get LCs right after the quarter ends. We're basically just going to tote it over the quarter ends.

MR. : And they said that's okay?

MR. : Yes. And, basically, that was actually pretty [inaudible] easy because Biello was used, you know, the quarter end's going to be so screwed up this time anyway that it's kind of throw another log on the fire.

MR. : Yeah.

MR. : Hey, guys. I'm sending him an e-mail right now. I can't get through to him right now.

MR. : Okay.

MR. : I mean, do we need--you know, we had a negotiated price and everything with Joe, but I guess we need to just call him and say, here's what we're going to be able to live with, you think?

MR. : Yeah, I think so.

MR. : Well, I think pricing is, like, so important in the equation, though.

MR. : Yes.

MR. : Well--

MR. : Maybe we can do--

MR. : Well, I may have to call him and say, you know, here's where we know we're going to come out exposure-wise.

MR. : Yeah.

MR. : We really haven't thought about pricing. You know, the point is is we can help you get through the quarter and, you know, we need to get George in the loop and [inaudible] and so, you know, the principal value is is we're here for some--some new exposure, not as much as I would like or that you asked for, but we're actually--he never really asked us for anything specific, I don't think, did he?

MR. : Umm, no, not really.

MR. : I mean, it's kind of like, you know--

MR. : He carries the club, you know. I don't want to get pricing out there, three or four banks, blah, blah, blah.

MR. : Yeah. Whatever.

MR. : Well, you know, they can bring [and sell fees?] [inaudible] to 35 and, you know, I guess we'll keep it.

MR. : Yeah.

MR. : [Inaudible] so you go, you know, you're there at 350, right, is that the number?

MR. : Yep.

MR. : Three-fifty, they get the, whatever, 315 out of those LCs a couple of days later, right?

MR. : Yes.

MR. : Then they have how long to syndicate?

MR. : Well, if they've got the LCs, then in theory, they have as long as they need, because--isn't that right, Rick? You were saying that--

MR. : Yes.

MR. : --we can either have the LCs or it can be syndicated.

MR. : Yeah. I mean, as far as, you know, what I--what I--what Biello and Wardell [ph.] said is that--first of all, they wanted LCs for everything. I said,

you know, that doesn't communicate them. You've got to--you've got to buck up, you know, [inaudible]. It's kind of like [inaudible]. Well, we don't do the L--you can't--he said, you can't compare all this runoff, you know, to new exposure, because we did have this here--

MR. : I'm going to--actually, George is calling and I'm going to tie him in.

MR. : They actually said that?

MR. : Yeah. You can't compare the runoff to--

MR. : George?

MR. : --that's bullshit, this--they're killing me on one side, saying they can go over--

MR. : We've got Jeff and Rick on the phone, obviously.

MR. : We can get the [inaudible]--

MR. : --fucking ridiculous.

MR. : Well, good afternoon, everyone.

MR. : Good thing I was right when I thought that was your number.

MR. : Yes.

[Laughter.]

MR. : New job at Lafayette?

MR. : No, this charity golf thing this morning.

MR. : Oh--

MR. : We're finishing up.

MR. : Well, we have update on the pre-pay. Well, I called Wardell and he tied in Biello and now they didn't want to do anything and, basically, you know--then they said, okay, we'll do it but we want to have fees for everything, you know. I said, well, what about our part? Oh, no new Enron exposure. We can't do that. I said, we've got to have something, you know. They said, okay, you know, I finally got them to, you know, say ten percent of the deal, so 35.

That's, I mean, that's the best I could do, and I said, well, then let me be very clear about what the--their specific act is and then there's, you know, they're asking our help on a quarter end liquidity situation, you know, to do a deal, close it, carry it over the quarter end, and then their promise is to deliver us LCs, umm, you know, basically on the first business day in October, or whatever that is, and Wardell says, no, no, no. They deliver the LCs, they get the money. I said, that's not the deal, you know, that's--you know, we're being asked and I would like for us to help out with the quarter end.

Biello kind of said, he goes, well, yeah, okay, do a deal that, you know, if they don't deliver the LCs in, like, two days or whatever the number needs to be, you know, that--that [inaudible] on the table. I said, I don't have a problem with that. I mean, we know the LCs are there. He

goes, well, that's fine. He goes, our quarter end's going to be sucked up anyway.

[Laughter.]

MR. : Okay. So--

MR. : That ain't what we'd like to deliver, but, yeah, there's--we still haven't really, you know, negotiated with Joe on price and we're all a little bit spread out here on--I don't know--my suggestion as to the best thing to do is, you know, [inaudible] can let you go and finish your afternoon, but, you know--

MR. : Well, I'm done, actually--

MR. : Okay.

MR. : --so--

MR. : We--yeah. I think we ought to call Joe and say, you know, here's what we can do. First and foremost, we can see you through the quarter end. You know, unfortunately [inaudible] we can take on some new net exposure for our book, but it's not a big number. It's 35 million bucks. I thought about, just for a second, asking for 50, which Wardell kind of said he would have done, but I could tell in Biello's voice I would have been making a gigantic mistake.

MR. : [Laughter.] Might have lost it all.

MR. : Right. You know, come on 50--and here's what we're talking about, you know. We're going to

underwrite it, you know, so we're going to--you know, we're going to get paid there. We're going to have to sell it, and we are--we do have the flexibility, you know, from our point of view of selling it off as a funded deal, or we can, you know, keep LCs so we can, you know, we can obviously go out and procure LCs, or you can procure the LCs. You know, we've got to have the ones that you have--that you said that you would deliver right after the first of the new quarter, but if you would sort of replace those with something that's more dedicated, you know, some sort of amortizing of fee for this specific deal, then, you know, we'll work with you to do that. Or we can--or we can syndicate a funded deal and, you know, that's basically going to become--be a function of price.

MR. : Of course, with--if we're down to 35 million of exposure, that means that we've really moved more to a retail-type execution here rather than a club.

MR. : Yep.

MR. : That's right.

MR. : Which on a funded basis is going to be highly [inaudible].

MR. : I agree.

MR. : That almost says--well, that says you should stick with the LC, but the problem with the LC is that you'd, umm, you'd have to pay us to carry the asset.

MR. : I mean, can they arb this by

basically paying for one year rolling LCs and just keep trying to keep the spread down a little bit?

MR. : Umm, I mean, that'll--that'll help a little bit.

MR. : I don't know how we fucking club--I don't know how we do a retail deal with this fucking structure on a funded basis.

MR. : I don't think we can do a funded deal--

MR. : I don't know how it can be a funded deal, either.

MR. : No.

MR. : So you're really back to the LC option, and then the question is, how does that affect the total cost.

MR. : Well, the LCs are default swaps, so, Joe, if the default swap market came in--

MR. : You can buy--

MR. : [Inaudible.]

MR. : Right?

MR. : Yeah.

MR. : All right. Well, we've got--you know, we've got to get--there's a couple of segments of pricing here that get kind of complicated, right? What will we carry this asset at?

MR. : Well, let me ask you this question

before we get to that. Do we think we can characterize this as a performance LC?

MR. : Not on--

MR. : No, but I think we could make it physical if we have to.

MR. : Yeah, I think--yeah.

MR. : Yeah, I think you could, George, sure.

MR. : Well, I think that would help--

MR. : Now, just as a quick aside, and I don't know if, Rick, you've talked with Chris and Jim about this, but, you know, one of Chris's comments is if we do it as a physical, it needs to sit under the existing 75 million dollar physical line or the increased physical exposure has to have an LC.

MR. : Oh, gee.

MR. : I know, and, you know, that's what Chris told me.

MR. : Well, I guess we could just tell Enron that--basically, it's going to be within the 75, definitely at these prices. If--if the market keeps going up, they'll have to maybe then give us, you know, one month LC if they're buying the physical or something. So we'll just have to tell them that's going to be measured against 75. Man. These guys are getting way too smart about all this shit.

[Laughter.]

MR. : It's the 75--you know what I'm saying, like today, man, I don't even know. I don't fucking know. I assume it's at much less than 75 today. It's probably like 45 or 50. But if prices go up again--

MR. : Yeah.

MR. : --then they're going--they're going to have to collateralize this, I guess?

MR. : Something like that.

MR. : Right.

MR. : Well, if we can somehow characterize the LC as performance, I still think there's a price pick-up there--

MR. : [Inaudible.]

MR. : No, no, I think--I think it's probably more than that. I mean, if you wanted to put an LC that was--if you wanted to price an LC, it would basically, you know, they're funded cost shares, you know, a financial LC. Let's just call it 150 over. And if you could maybe sell a performance LC, I would think for maybe one-and-an-eighth, you know, with 50 percent capital weighting--

MR. : Okay.

MR. : --and, you know, logic would say, well, you ought to be able to chop that 150 in half, but we know we never do that, so could you sell a performance LC

for one-and-an-eighth? I think--I think there's a shot at that. I mean, if you truly carry it at 50 percent, that means you've got an asset that gives you two-and-a-quarter. I would think that would be appealing to some folks.

MR. : Yeah.

MR. : Umm.

MR. : Well, we didn't talk about the notion of kind of one-year LCs that would be replacing--I think you can guarantee that that would be something that Biello and Wardell wouldn't want to entertain.

MR. : Well, I mean, I'm assuming that we--

MR. : [Inaudible.]

MR. : Yeah. I mean, if we had a one-year evergreen [inaudible]--

MR. : Yeah.

MR. : --if it weren't renewed, we'd fund it.

MR. : Exactly.

MR. : Okay.

MR. : So we should be indifferent to having a one-year evergreen as long as we all stay on top of it and make sure that the LCs are rolled and if they're not, we fund them.

MR. : Right.

MR. : [Inaudible] more easily for George

instead of having it an evergreen, you might just make it a one-year LC--

MR. : Yeah--

MR. : --with the notion that--or whatever.

MR. : But it's definitely going to be drawn if they're not rolled or not replaced.

MR. : Exactly.

MR. : Enron doesn't take it out, so--

MR. : Exactly.

MR. : So it doesn't have, like, a, you know, six-year date on it.

MR. : Right.

MR. : So then you'd have the pressure on Enron every 364 days, they could pressure Enron and say, take me out. That'd probably make them feel a lot better than having a six-year LC or a five-year LC which keeps rolling.

MR. : So should we call Joe and defer the price discussion or [inaudible] pricing out there that we--

MR. : I think we should defer.

MR. : I think we ought to defer the pricing.

MR. : I think we ought to defer it, because we've got to think this through in steps and, you

know, what is the return I'm going to need on a facet even if it's LC-ed back. Who the fuck knows who these banks are going to be? What are they--you know, are these banks, like, risk rated three, some of them, or--

MR. : Well, I mean, if it's under their syndicated facility, they're mostly pretty high-quality banks, but, I mean, there's, you know, what, 60 of them.

MR. : Who sets the price? Doesn't the pricing group kind of have a performance LC [inaudible]?

MR. : Yeah, I believe so. Let me--I'd have to pull it up--

MR. : --364 [inaudible]. I've got it here. It expires next May.

MR. : If it moves down to our prices [?], maybe they don't need as much margin anymore [inaudible] a new deal.

MR. : I'm taking a look here.

MR. : [Inaudible.]

[Pause.]

MR. : I'm going to have to look up that pricing.

MR. : Yeah.

MR. : [Inaudible] in front of me.

MR. : Yeah. [Inaudible.]

MR. : --trivial pursuit.

MR. : It's probably about 67-and-a-half or something like that, or 68-and-a-half, I bet.

MR. : Do you think we had a performance option in that facility, Rob?

MR. : I don't recall.

MR. : I don't remember that it did.

MR. : Again--

MR. : --but we can--

MR. : Yeah. Actually, let's see--we had--we did have a performance option of 30 bits [?], and up to 50--and looks like it's 52-and-a-half for financial.

MR. : For how long?

MR. : One-year facility.

MR. : So if you wrote the LC today, how long would it be good for?

MR. : Until next May.

MR. : Or is it a one-year starting in May?

MR. : I'd have to go back and look at the agreement.

MR. : All right.

MR. : I don't think it could--I think it could extend for up to one year beyond the maturity.

MR. : And how much availability do they have in that thing?

MR. : It's a 500-million-dollar line.

MR. : And what's drawn?

MR. : I don't know.

MR. : That's pretty cheap.

MR. : Yeah, it's very cheap.

MR. : We should draw on that thing.

MR. : Yeah. I mean, [inaudible] got to be getting.

MR. : And then we go incrementally or whatever the hell else they need.

MR. : So it would even cover our physical exposure under that.

MR. : I mean, the physical exposure may not be such a big issue for gas prices to stay down--

MR. : Right.

MR. : I think that's the least of our worries, Jim--

MR. : Yeah. It seems to me that--I think you should tell Joe, yeah, you've got a ready-made source. You've got 35 of new capital from us. We're going to underwrite this over a quarter end, which seems to be very important to him. I mean, that's why he's so nervous about the passage of time, is he's--he's got to get this thing closed, I think. Does anybody see it different?

MR. : No, I think you're right.

MR. : I think the underwriting is kind of worth a lot of value here, or am I reading it wrong?

MR. : No. I mean, I think that's very important. I'm--

MR. : Yeah, we're going to give you--what we're taking, you know, what we're hearing, one of the things you need the most is the underwriting. We've got the underwriting done so we can carry over those couple of days at the end of the quarter--

MR. : And make a deal back.

MR. : You can imagine our balance sheet's looking pretty bad, so 350 of underwriting on the quarter end, pretty big--

MR. : That's a pretty big commitment.

MR. : Pretty big commitment. We're not in a position to give you a big, you know, term hold on this deal, but we're going to, you know, treat it like we would something else we would syndicate and we'll take ten percent, so that's 35 million. We obviously want, you know, the LCs that you're thinking about, you know, when you said you'd give them, you know, right the first business day of October or whatever, and we had the flexibility from a quote-unquote "permanent" syndication option for, you know, the 315 that we need to sell.

We can either take bank LCs or we can--we can syndicate it on a funded basis. You know, our view is that [inaudible] LCs may be the better way to go. Clearly, the biggest [inaudible] for you is just use you all's committed

LC line and then maybe--maybe you'll become opportunistic and watch in the credit default swap market and we'll take those in lieu of LCs and, you know, if you want to bring some [inaudible] we'll allow you to get [inaudible] LC.

And that way, you know, then we have to--we have to kind of complete our pricing here because we need, you know, we need an underwriting fee and if you ultimately want us to syndicate this deal, we'll have to have an arrangement fee for that.

MR. : [Inaudible.]

MR. : --surprised to see you'd made money?

MR. : George, you're going to push him towards leaving--keeping this as a physical deal just so we have the possibility of this performance benefit?

MR. : Well, it's, I mean, it's up to him, but--but I think, you know, in the long term, there's possibly some price savings if we keep this as a performance LC rather than a financial.

MR. : Right.

MR. : I mean, you know, it's not inconceivable that to syndicate the thing, he may come back to us and say, I can get insurance bonds in--maybe instead of syndicating it for, you know, 150 or whatever, I can get insurance bonds for, you know, whatever, 30. Can you get these other banks in for, you know, a much lower price?

MR. : Exactly. So that leaves that option open. So I think we should stay physical.

MR. : Yeah.

MR. : Because there's a couple of alternatives, okay?

MR. : Yeah.

MR. : Let's talk--we should probably just have an idea of what pricing is. So, again, we have to take this action on which we think we're going to get some sort of a blended risk rating, two, something like that, Rob? I mean, one of your analysts maybe can run that real quick.

MR. : Yeah. I mean, I would assume with an LC, that's always been viewed as better than a surety, so, you know, we've got, let's call it a one-minus, and what kind of return are we looking here, looking for?

MR. : Well, what kind of--what kind of--you know--

MR. : The question is, what are those LCs going to cost, then we back into how much we can charge for this. I know it's kind of a round-about way of doing it, but, you know, we're saying existing LCs are about 50, maybe even under that, under that line, if we've got room. Other ones are going to cost them, you think, about 100?

MR. : I would think that's probably a good estimate. George?

MR. : George, is that about right?

MR. : I'm sorry, one more time?

MR. : I said, existing--we're just trying to back into what we would charge for this asset and how much the all-in costs would be for him.

MR. : Right.

MR. : So you're saying the performance LCs, we know there's this existing line where we can get them real cheap for the May.

MR. : Right. Right.

MR. : But then separately, they're going to cost him, you know, for whatever incremental needs he has or to extend them, it's going to cost a lot more than that, right?

MR. : Right.

MR. : So you're going to assume, what, 100?

MR. : Today, that may be.

MR. : George--

MR. : I'm fading in and out, but I think you said if we would do the other performance LCs just out [inaudible] right now, about 100 basis points, is that what you said?

MR. : Yeah.

MR. : Yeah, that sounds good.

MR. : Okay. So, you know, I mean, for

this asset, I mean--I don't know. What do we charge, 50, 60 basis points? Sixty basis points?

MR. : Whatever you're thinking, Jeff, make it the top end.

MR. : I think you've got to charge at least 60 basis points for this asset.

MR. : Tell him 75.

MR. : Seventy-five. So let's say 75 bits--

MR. : Seventy-five as the run, run rate?

MR. : Yeah, that's your carrying cost.

MR. : Yeah. And then--

MR. : --carrying cost, but that assumes, you know, delivery of all the LCs.

MR. : Right. So his cost for the LC could be anywhere from 250 to 100, so--

MR. : If there are, so assume in the middle--

MR. : So, you know, hey, Joe, you know, you've got--that's yours to kind of choose from. You've got a ready-made, you know, [inaudible], you know, that Mary Perkins, who's this other treasury person there, she, you know--if I were Mary Perkins, I'd be charging Jim more than 50.

MR. : Yeah, exactly. She just fought to get this capacity. The 75--hold on. Yeah, that gives us

about a 25 percent return with no up-front fees--

MR. : On a risk rating.

MR. : --on a risk rating one-minus, but with the capital charges that Enron gets. If you run that at a two, just to be--two-plus to be conservative, you're still at a 20 percent--

MR. : Twenty percent. That's not very attractive.

MR. : That's just the loan spread. That's not any underwriting fee.

MR. : Okay.

MR. : Or that's the asset carrying charge.

MR. : Okay.

MR. : Now, we had been throwing around, you know, getting kind of up-front fee of 75 at one point.

MR. : Yeah, the problem with that--

MR. : That was a different kind of execution, I think.

MR. : No, I know. I'm just teeing up that as a--

MR. : Can I call you back?

MR. : Yeah, sure.

MR. : Is everything okay?

MR. : Yeah. Listen, I wanted to give you a quick information. They're going to bury Mr.

Kreopolous [ph.] Monday--

MR. : Okay.

MR. : --and they're only going to have a one-day.

MR. : I've got to call you, because I'm supposed to go to London Sunday night.

MR. : Oh, yeah?

MR. : So let me call you back and see if I can do it.

MR. : Well--

MR. : They're doing it Sunday, right?

MR. : Yeah, it'd be Sunday. Yeah. Yeah. Did you hear about it?

MR. : I just heard from George about an hour ago.

MR. : Oh, okay. All right.

MR. : Actually, I was going to call you tonight--

MR. : Yeah. The old man just across the street just told me about it, so I thought I'd call you. All right. Okay. Are you home?

MR. : Yeah. I've got to call you back. Sorry.

MR. : This is--

MR. : What are you talking about?

MR. : That's 28-and-a-half--

MR. : --for a second.

MR. : Hey, John.

MR. : How are you doing?

MR. : Hey, Jeff, that's not a very cordial hello.

MR. : How are you?

MR. : I'm doing fine?

MR. : Somebody pounded this market big-time [inaudible].

MR. : Dan, probably overdone a little bit, huh?

MR. : Yeah. I think it might be in the--just today's--the end-of-day activity was absolute just panic selling, put buying, like usually paying up for 20 and 19--

[End of recorded tape.]

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

J. Dellapina, (AT) 030

September 26, 2001

10:25:10

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

P R O C E E D I N G S

MR. : Hey, buddy.

MR. : Hi. Enron called back. Do you want to try to patch in Robert Traband?

MR. : Yeah, patch him in.

MR. : Okay. [Inaudible].

MR. : [Tone.]

MR. : Yeah, hopefully I could do that. Hold on.

MR. : I'll do it. I'll do it. Hold on. Hold on. Is anybody on the line there?

MR. : Not yet.

MR. : Okay, hold on.

[Phone dialed, ringing.]

MS. : Bob Traband's office. This is Melanie.

MR. : [Inaudible] she might be looking after that.

MS. : Hello?

MR. : Hi. This is Jeff. Is Robert there?

MS. : He's on his phone. Would

you like to [inaudible]?

MR. : Could you tell him that Phil and I need to speak with him?

MS. : Hold on.

MR. : Thanks. They're trying to interrupt [Tone].

MS. : He'll be right with you.

MR. : Thanks.

MR. : I'm going to try to conference Enron back in.

MR. : Okay. Hello?

MS. : Uh-huh.

MR. : Ann?

MS. : Yes.

MR. : Hi. I have Jeff Dellapina on the line.

MS. : Hi, Jeff.

MR. : Hi, Ann.

MR. : And I think Rob Traband is going to try to--

MS. : Okay. I have Morris Spark on line.

MR. : Right.

MS. : From our tax department.

MR. : Right.

MR. : How are you all doing?

MR. : Hi.

MS. : Okay. I guess what we need to do is get some information about Mahonia. First and foremost, not tax-related, is the correct name Mahonia Limited?

MR. : Yes.

MR. : Yep.

MS. : Not Mahonia [inaudible] Limited?

MR. : This is Rob Traband.

MR. : Mahonia Limited, spelled out Limited.

MS. : Okay. I think the big question for us is are they a U.S. taxpayer?

MR. : I guess the big--can we ask a question first?

MS. : Uh-huh.

MR. : What is the difference

now?

MS. : Well, I'll let Morris--

MR. : Yeah. There's a big difference in that, that the U.S. withholding regime, under a physical deal we're okay because it doesn't, it doesn't--the payments don't become withholdable payments. But when you switch it to a--a financial deal, then interest comes into play and that interest is subject to withholding.

MR. : Okay.

MS. : So is that to the extent that any of a--that a part of the payments are deemed to be interest?

MR. : Exactly.

MS. : Okay. So it's not all of the payment.

MR. : No, exactly. It's just the interest components.

MS. : It would be a portion of--

MR. : Well, why in a physical deal, when there's a prepayment component--so we all, we all know that any prepayment has a discount

in it.

MR. : You're absolutely--the economics are absolutely identical. It's just one of those, one of those regimes that are different in the tax code.

MR. : Yeah.

MR. : Yeah, I think you're right. The economic result is the same.

MS. : Exactly the same.

MR. : Yeah.

MR. : So, you know, Phil, stop me if I'm going in the wrong direction. But, you know, we're trying to reach Mahonia, right? I don't know if they're filing U.S. tax returns.

MS. : Okay.

MR. : Yeah, we don't know that either.

MS. : Is--

MR. : I have a suspicion that they don't really make a whole lot of money on these trades after their financing costs.

MR. : Yeah.

MS. : Well, if the answer to that is yes, then our, our fix is easy.

MR. : Exactly.

MS. : If it's not, then it's not easy.

MR. : Yeah, exactly. And the issue is complicated because of the fact that we don't have an income tax treaty with Jersey. So there's no--not only do you have withholding, but there's no reduced rate subject to a treaty, so you have a 30 percent rate [?].

MR. : I don't think they're filing a U.S. tax return.

MR. : I think that's accurate.

MR. : I would--my gut would say that's probably the case, but since they are engaged in doing these physical deals with other counterparties in addition to Enron, I just thought there was a chance.

MR. : Well, no. I mean they definitely file, you know, get their tax exemption on all their sales, and you know, file for, you

know, exemption on excise taxes and those sorts of things, but in terms of U.S. income tax, I do not believe they are a U.S. filer.

MR. : Okay.

MR. : Having said that, I don't--I also don't believe--I know that magnitude is not really the issue, but I do not believe that they're incurring an enormous amount of U.S.--what could be potentially deemed as U.S. taxable income on a net basis. So I don't know if that is part of their decision on whether--you know, if their interpretation is they don't have to--

MR. : I don't really think it's--I don't think, I don't think the issue is probably, is driven by the volume of the income. I think it's just a determination of whether or not they're engaged in U.S. trade or business, and that's just subject to, you know, their interpretation.

MR. : So where do we go from here?

MR. : We just need to get

confirmation on that. Again that's--I don't know--

MR. : Well, why don't you assume that? We'll try to get confirmation, but assume that they don't file a U.S. tax return.

MR. : Okay. Then we've got--we've got this--we're looking at the Satolian [?] issue square on.

MS. : The deal is it's under a normal ISDA [?], as I understand it--Morris, correct me if I'm wrong. You know, if you can't make these reps to--reps to us, then, you know, we're subject to withholding part of the payments that would go to Mahonia. And then we have to gross them up.

MR. : That's--

MS. : And, you know, our guys, that's just not--that's not a--

MR. : It's not going to work.

MS. : That's not part of the answer.

MR. : No.

MS. : That's not the answer for

us. So--

MR. : But you're right, and under the normal ISDA [?] that's right. We would be required to gross up, and that's where the disconnect is.

MR. : Okay. So I guess the--I mean I guess we leave this to you to say you either, I guess, you know, you either can get comfortable with it on a financial basis, or I don't know, or we revert back to physical. I--

MS. : Well, I mean I think there are some, some alternatives, and I don't remember all of them. I mean, one of them is if this were a shortened deal, and--

MR. : Yeah, you could--

MS. : --only a six months deal--

MR. : Exactly.

MS. : --then we wouldn't have this problem.

I think there are some other structural things. There are some things that we can get from you guys in terms of indemnification. I don't have

all the details. I don't know if you do, Morris, or not.

MR. : Yeah. Yeah, there are a couple--I mean I don't know how--how much detail you want to go into here, but there are a couple alternatives, one of which Ann--we can make the payments and not withhold, but we'll need either one of two things. We'll need the certification that you are engaged in a U.S. trade or business. If you can't make that, then we'll need indemnification from you. If--

MR. : When you say "you", "you" meaning--

MR. : Mahonia. I assume Mahonia, but I assume [inaudible] because Mahonia, I don't know what the substance is of Mahonia, and I assume we'd want more substance--

MR. : Yeah. Well, see, I--again, don't spend a lot of time going that direction because you're probably not getting any indemnities from us.

MS. : Okay.

MR. : On that. I mean, just practically speaking, I can't imagine we'd indemnify you for that issue.

MR. : Okay. The other alternative is a structural change. And you can use a subsidiary of Mahonia that's resident in a treaty jurisdiction and it's limited to certain treaty jurisdictions that have either a reduced rate or a zero withholding rate on--

MR. : They have subs, but they're all in Jersey.

MR. : So [inaudible] create one?

MR. : Yeah.

MR. : I don't know if we--

MR. : It's not going to happen by tomorrow.

MR. : See, that's the issue there is just the timing.

MR. : Yeah. So, so far, other than it--so far what I'm hearing to do a financial deal, but the only thing on the table right now might be a shorter day to deal.

MR. : For taxes [inaudible], that's exactly right, yeah.

MR. : Now, one of the ways to think about that is if that's the only alternative that you're comfortable with, is that--you know, I was certainly clearly under the impression--we had pushed for a physical deal from the get-go, but Lisa, I guess, is of the opinion this was going to be restructured within the next 3 to 4 months anyway, so she just wanted to do something quickly.

MS. : Um-hm.

MR. : So it's not inconceivable--

MS. : I don't know if that's the only restriction. It may just be the size of the transaction. I don't know.

MR. : Because if we could do a physical, obviously, that doesn't cause these same concerns.

MR. : Well, I mean, we were always comfortable running a physical from our end.

MR. : Is it too late to convert

this to physical?

MS. : Yeah. I mean we need to get Lisa on the phone.

MR. : Yeah.

MS. : We're going to--

MR. : I mean, obviously--yeah, we can't make that decision. I'm just--is that even something that's still an option?

MS. : I don't know. I don't know. I mean I'm just the, you know, finance [inaudible].

MR. : No, I understand.

[Simultaneous discussion.]

MR. : Both Ann and I are in advisory roles. We'll have to get this--

MR. : I was thinking more from the standpoint of physically, mechanically, can it--can we convert this to a physical--

MR. : Physically and mechanically, Rob, from our perspective--obviously it's not a tomorrow [inaudible]. Is it conceivable we could do a deal by Friday? Anything's

conceivable.

MR. : Okay. I'm just saying whether--I'm trying to figure out whether that's something we should even explore with Lisa if we've got time to get it done.

MR. : My only issue there is I would--if it--

MR. : Well, Jeff, Jeff, I don't know--I mean we were told that the Mahonia directors are not going to be around on Friday to sign documents.

MR. : So Mahonia, we're running out of time with--all right. Well, why don't we--why don't we--you guys track down Lisa if you could, or Joe, and find out what--which direction you want to go.

MS. : Okay. Where--how should we get in touch with you, if we just get them to call you? Do they know how to get in touch with you wherever you are?

MR. : Absolutely.

MS. : Okay.

MR. : Absolutely.

MS. : All right.

MR. : All right.

MS. : We'll have them call you.

MR. : Just another--just another challenge here.

MR. : Okay. And we--Jeff, we'll call Mahonia just to double check, but I think you're right. I think we've got a high degree of confidence that they are not U.S. taxpayers, but we'll ask the question.

MR. : If we can just confirm that.

MR. : We'll ask the question.

MS. : I'd hate to miss that if that--

MR. : No. Agreed, agreed. Like I said, I have a high degree of confidence that they're not, but in the off chance that we're wrong, we'll make a call anyway.

MS. : Okay.

MR. : Okay, great.

MR. : All right.

MS. : Thank you.

MR. : Thanks.

MR. : Bye.

[END OF TAPE RECORDING.]

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 30

September 27, 2001

10:48:41

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : Hey, you guys. How are you doing?

MS. : Okay. So my understanding now that I've hooked up with Garp [ph.] is it's this tax rep that we're asking Jeff that's the concern?

MR. : Yeah. I think there were some other business things that, umm, his [inaudible] two lawyers and he could just clean up, but, yeah, I think that's right. I mean, basically, I thought any sort of tax reps are going to require some discussion and analysis of Mohonian [ph.]. We sort of thought the whole point of yesterday, not going physical but going to a six-month transaction, was so we wouldn't have to deal with the tax rep.

MS. : Or so that we didn't have to make a--

MR. : Withholding.

MS. : --have a U.S. withholding tax.

MR. : Right.

MR. : Right, but--

MS. : And as a result, to ensure that, that's why this rep's needed, which goes--because we have to be able to file the W--you have to be able to file a W-8-BN to indicate that you aren't a U.S. taxpayer, therefore, there is no U.S. withholding tax and fit into this exemption of--

MR. : Okay. Well, they've not spot

filled out that form, and I guess the issue here is, you know, reaching the partners and trying to get them to, you know, analyze this and determine whether, you know, they should be making that rec, and, you know, I think that's the issue we're having just time-wise.

MS. : Yeah. Well, I guess--

MR. : I don't know--I haven't talked to the partners at the law firm that represent Mohonian. We sort of knew they were going to be swamped today and they were out of the office, but they got me other documents and now, you know, I think we're having difficulty sort of getting in touch with them and trying to get them to analyze this.

MS. : Right, and the way our tax side says it is, this should be--if you--they get with someone who truly knows the tax code here in the U.S., this should be a slam-dunk, that if they don't pay U.S. taxes, and that's clear, then by default, they should be able to say that's because that means they have no trade or business in the U.S.

MR. : And what are you doing with that form? What does that do? I'm really not familiar with this, but--an extent of--in getting that form, what do you do with it? Is that something you file?

MS. : That we file that provides that we are not subject to withholding tax on payments that we make

in Mohonian, yes, and that form, you know, we need--

MR. : Since you're making those payments to Mohonian in the U.S., you still need to--

MS. : Right, because--exactly, because otherwise we should be paying withholding tax on it.

MR. : Hmm.

MR. : And he said the actual tax form. Morris told LaFitz [ph.], basically, it's their name and address.

MS. : Well, and the same rep.

MR. : And the same rep again, so--and that's it.

MR. : Okay. Well, basically, you know, I'm--I think that--I don't know the answer, guys. I mean, I'm trying--we'll try to reach the partners over there and see if they can do this, but it's a last-minute request. It's they're just not around right now. As perfunctory as, you know, you think it is, we still have to find these guys and they have to think about it.

MR. : Right, and--

MR. : It's not something they've done before, right?

MR. : Right, but it--

MR. : They have not--

MS. : I understand. That's why I guess I thought--there's the U.S. tax partner that, you know, if

you find them, that you can talk--you know, can get on the phone with them and explain what it is so that they don't have to spend a lot of their own time trying to do due diligence. It's already--

MR. : Right. Unfortunately, a couple of the guys we wanted today are out on holiday internally and the guys--you know, so this involves outside counsel. You know, we have to figure out how the hell we're going to get them up to speed or just--you know, we're working on it, but I--

MS. : What are the other business points?

MR. : Umm--

MS. : Mike, are you familiar with them? Garb?

MR. : I think there was--

MR. : No, I--

MR. : --there was a couple of things. One was confidentiality, that Mohonian wouldn't share anything, any information on that swap, and what that--what that raised is that we have not gotten--well, first of all, you know, obviously, they have to be able to share with us. They have to.

MS. : Yeah--

MR. : And secondly, on every other deal, we have a side letter which I spoke to Ann about and she's

going to look it up, that you guys acknowledge that they pledge their interest in this to us. They do that on every deal we--

MS. : Mm-hmm.

MR. : Okay. So that--that has to go. The issue of assignability, Ann thought it was asked and answered with Phil Levy [ph.], but I think when this other lawyer was looking at it, he was saying, okay, well, you can assign it, if it says, as long as the Enron Corp. guarantee is in place. I just asked him to look at the issue of, well, does that affect in any way the LC, if you start assigning this trade [?].

Again, I'm not--I think the lawyers just need to, you know, get over that on both sides and figure out an agreeable solution because I really don't think he has [inaudible] to assign this thing.

MR. : It's a six-month--I mean, it's a six-month deal, so--

MR. : I know, but--

MS. : Yeah, but I--yeah, I mean, I--

MR. : No, I understand your--

MR. : But there are some things in there, you know, that--that's our whole credit protection and we have to keep an eye on it. I think those are the only things I had that she raised to me, and I think Ann and he will hopefully just, just get those away from us and

leave us--

MS. : Well, yeah, the confidentially, that's fine. We can go to her and say, confidentiality, you know, other than to--

MR. : Yeah. Yeah.

MS. : --Chase or other parties involved.

MR. : And I think that both sides overlooked that letter that said--

MS. : Yeah.

MR. : --you're pledging. I'd probably be prepared to do that on a post-closing basis, that letter.

MS. : Yeah, and the letter's not a problem.

MR. : Okay. I hope not, because from your accounting, I don't know why, but you've always given us that letter, but I hope there's no problem with that, right, acknowledging that we're the secured party, the Mohonian lender to--

MR. : We did that in the past, though, because of--

MR. : --deal.

MR. : Yeah, and all the physical deals we did.

MR. : Okay, so that's critical. All right. So I think, then, I'll--let me call my attorney and see if they've been able to reach anyone about this

tax--this tax rep.

MS. : Okay. Jeff, let me ask, do you think--

MR. : I know it sounds easy to you guys, right, but think about what happens. What happens is these guys start coming, you know, for advice to us and we don't want to take any responsibility. They say, well, we're not, you know, filing U.S. taxes, whatever, but we don't want to make--you know, that's our business, and then they come and say, well, you know, what do you think? Should we send this, give them this rep, or ultimately, you know--you know, it's not--you've decided not to file U.S. taxes. You've taken that view.

And then, well, what does this form mean? What happens if I fill this form and fill it out and they submit it? Is this going to trigger all kinds of other discussions with the IRS? And I don't know the answer to that. But they also will not be prepared to know the answer to that right away, so then they started looking to us.

MS. : And I guess [inaudible] have you talked to anyone internally, though, that would think that this would be an issue, or is it more just a matter of hooking up with them so that someone can explain it to them so that they understand that it's not--

MR. : Well, I don't think any of us really--I mean, only a tax attorney would know if it's an

issue--

MS. : Well, right. That's what we're saying--

MR. : Where do we find--

MS. : Okay. You just haven't hooked up with the tax lawyers to get that--

MR. : Exactly, and unfortunately, the guys we use internally are not in today, so that's what--that was the initial problem that our attorneys had.

Are you going to be on your cell phone for a little bit, or should I just call through Michael?

MR. : I'll be here and I can get a hold of Lisa, if need be.

MS. : Yeah, because the pager's working better than my phone. Unfortunately, the phone didn't charge last night.

MR. : Okay. Well, why don't you, if you wouldn't mind, call Ann and find out where she is, if she thinks there's any--any other stumbling blocks--

MS. : Yep.

MR. : --and I'll keep chasing down the tax side of this.

MS. : Okay.

MR. : Okay.

MR. : All right, guys.

MS. : Thanks, Jeff.

MR. : Bye.

[End of recorded tape.]

T2243

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON GOVERNMENTAL AFFAIRS

In the Matter of the of the Collapse of Enron

J. Dellapina, (AT) 033

September 27, 2001

12:37:35

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

P R O C E E D I N G S

MR. : This is Jeff.

MR. : Hey, Jeff. Garberding.

MR. : Hi, buddy. What's up?

MR. : Issues to walk back through real quick.

Tax issue. I guess, Lisa talked to Terry Benn [ph].

MR. : Well, we sent--our lawyer is sending to Ann the response from Mahonia.

MR. : Let me get, let me get Lisa. She's on the cell phone. Let me get her on real quick. One sec.

[Music playing.]

MR. : Sorry about that. She should be getting on.

MR. : Okay. It looks like a tomorrow deal.

MR. : We've already said tomorrow is fine with us because with the 180 days, that's fine. That works. That should be no problem.

MS. : Hello.

MR. : Hey, Lisa.

MR. : Hey, Lisa.

MS. : How are you doing, Jeff?

MR. : All right. Where are you guys?

MS. : We're at this recruiting event down in Florida.

MR. : Florida, no kidding?

MS. : Yeah.

MR. : I said that--

MS. : Yes?

MR. : --the deal toy for this deal should be those Mickey Mouse hats for everyone.

MS. : That's what it's turning into.

MR. : Yeah.

MS. : Rob called Jeff and said that everything is okay now with the rep--tax rep and the form, that Jersey counsel gave him the okay because we're not looking for an opinion.

MR. : Well, yes.

MS. : Is that your understanding?

MR. : Let me just--what your lawyers are going to see is an e-mail back from Ian James, who is the attorney and board member of Mahonia, saying I'm happy to make the rep, but he's just trying to be totally forthcoming, and he's saying, just to let you know, I'm making the rep based on Jersey analysis, that we don't believe we subject ourselves to any sort of U.S. taxes, but he's saying I have not gotten New York or U.S. counsel opinion for you on the rep.

MS. : Yeah, we're not looking for an opinion.

MR. : So when they see that e-mail, they should be fine that he's signing it.

MS. : Right.

MR. : Because [inaudible].

MS. : Exactly. That's why I just wanted to make sure we were all on the same page is all.

MR. : Okay.

MS. : And then we have the pledging interest, that we sent some language over to your counsel. Did he share that with you?

MR. : He didn't as yet, but I'll get all over him.

MR. : Yep, that should be done.

MS. : Mike--yeah, Mike, why don't you lay out what it says, since you helped craft it.

MR. : Basically, what it's saying is there was already some language in the Mahonia guarantee, and basically what we did was give the right to Mahonia, assigned its rights under the transaction as the security interest for a hedge that Mahonia enters into.

MR. : Okay.

MR. : And we're just going to put that in assignment [inaudible] within that actual confirm.

MR. : Okay.

MR. : And it should, since

Amir[?] is the guarantee, it should fit nicely.

MR. : Okay. And the acknowledgement that they are assigning and pledging to us--

MR. : No, we can't.

MR. : --like we usually have?

MR. : We can't. We can't specifically say Chase. We can just say they can assign it, and it gives them the right to assign it to whoever they want to.

MR. : And they're saying because it's not a physical deal?

MR. : Yeah, because it's a financial deal. If we say, if we put in a transaction where they can assign it to Chase--

MR. : Okay.

MR. : --we are at zero. We consolidate debt.

MS. : Exactly, you're combining the legs[?], which is what the whole point of using Mahonia.

MR. : Okay.

MS. : So, again, because of the [audio break] financial [inaudible] through the [inaudible], which is why we're at this point on that. So you still have the--they still have the assignability rights, it's just you'll have to make sure it gets assigned to you, not to anybody else.

MR. : No, no, no. That's fine. Just, okay. You know, the global sort of securitizations work that I've done always speaks to you're supposed to notify the party specifically of how you're, how you're assigning that. I'm sure our lawyer is not going to have a problem with it, but I've done securitizations in the past, and it's always been pretty key that there's a notification.

MR. : Yeah, they'd notify us, and we have a reasonable right or whatever to say something is what I've seen in the past on monetizations.

MR. : Okay. So they can assign it and notify you, right?

MR. : That's exactly right.

MR. : Okay. Okay.

pab 8

MS. : We took a look at it, and we think it should work, and it passes our accounting, but that's why we wanted to make sure you knew that it was [audio break], you know, that business people can talk, too, and not just have the lawyers get all caught up in legal stuff, too.

MR. : I'll check with them right now. Okay.

MS. : And as far as we knew, those were the only things, other than some pricing, Mike?

MR. : Yeah, I'm going to, I'm going to give Mike Sabloff [ph] a call and get that done. We'll price it as of assuming cash flow is tomorrow.

MR. : Yes.

MS. : Yes, and that's what Rob said.

MR. : Yeah.

MS. : The money is going to flow tomorrow morning.

MR. : Right, and that's how the

confirm is going to change, and then we'll just agree on basically an interest rate. That's the last thing we have to do.

MR. : Okay. So from your attorney's perspective, obviously, it's got to--and mine as well--we have to have, obviously, super clean execution copies, nice and simple for Mahonia over--by e-mail tonight because they're only in, in the morning tomorrow. So he said he's done all of his opinions, constituent documents. He's all ready to send those over with his signatures, provided we get all of that stuff to him overnight, because he's basically in for a half-day tomorrow.

MS. : Yes, that's the plan.

MR. : We'll have, we'll have everything out for signature pages. My goal is to have everything out this afternoon.

MR. : Super, yeah.

MR. : And then everyone will have it in their place. So really tomorrow is more of just fax around, get it done, you know, confirm the trade, and flow the money.

[Tone.]

MS. : Yes. Is there anything else on your side, though, Jeff, that you think is out there?

MR. : Nothing that I'm aware of. I'm just going to go check that assignment language with my attorney and make sure we're in good shape.

MS. : Okay.

MR. : And, please, Michael, just give Diane a call and make sure she's fine with that, that comment on the rep.

Now do they have the rep letter from, from or the request from Andersen?

MR. : Yes, they've not received it yet. I talked to Julie this morning or send an e-mail to her. We're changing a little bit, and they fully agreed to what it looks like. We changed four up a little bit to make them happy.

MR. : Good.

MR. : And once they get it there, we'll just make that one change, which we agreed to, and send it back.

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11

MR. : Tremendous. All right. Well, I'll expect to talk to you in another hour or so, Michael.

MR. : Sounds good.

MR. : I'll call you if there's an issue.

MS. : That would be great.

MR. : Okay. Thanks.

MS. : Thank you.

MR. : Bye.

MS. : Bye.

[END OF TAPE RECORDING.]

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 38

September 28, 2001

12:22:07

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : This is Jeff.

MR. : Hey, Jeff, it's Joe.

MR. : Joe Day [ph].

MR. : Yeah, I got a page that says that you're not calling about the deal, so I figured I could call you back, then.

MR. : Yeah, one of your guys was calling--I was kind of distracted this morning. We're going to send the money out now. I just needs to know where--we just hadn't seen any of the signatures and nobody from V&E called and that, you know, you guys are [inaudible] so--we just need to see those.

MR. : You don't need the signature pages, do you?

MR. : Yes. Hey, on this fee letter? Where should I send it to? Just send it to your office and you'll sign it Monday?

MR. : Okay, great. We can take the fees out of the [inaudible] payments.

MR. : [inaudible]

MR. : Yeah, sure. Sure.

MR. : And it was a buck, right? Hello?

MR. : Yeah, I'm here.

MR. : It was a--it was a million.

MR. : I don't know what the--I think it was

three and a half bits, wasn't it? Is that what the deal was?

MR. : It was, what, 28 and a half, or something?

MR. : Yeah.

MR. : It was [inaudible] for a million--

MR. : Okay.

MR. : --is what--yeah. So, um, all right, I will--yeah, I will get to that.

Did you hear the--hear--I need to tell you something. Back--there was a--and I just want to let you know--back a gazillion years ago, there was an issue with JP Morgan, Chase, and probably a host of other banks dealing with a company called Sumikomo [ph]. I don't know if you remember. And there was all kinds of lawsuits, right.

MR. : Yeah.

MR. : So one of the things they asked for was transactions that the bank was involved with from, you know, a certain period, whether it was 1993 to 1996 or something, which involved the funding off the commodity desk. And it involved any [inaudible] issues down there, like, you know, three or four gold companies, a couple--one or two oil companies, and, you know, one non-gold metals company or something. It was, like, five deals as far as different [inaudible] performed.

Anyway, so they asked to discover the documents,

and the bank said drop dead. They then asked to see the documents that the court forced them to release the documents with no names, and now the court's requiring them to actually show the names of who the deals were done with. And we really don't have a choice. Hello?

MR. : Yeah. Yeah, I'm still--

MR. : All I'm saying is the court, or the Sumikomo attorneys will see documents that have Enron and about five other, you know, non-energy companies.

MR. : Okay.

MR. : And so all I'm doing is letting you know that.

MR. : Yeah.

MR. : I can't really tell you much more. You know, it's typical, if they ever wanted a--who knows, if you got a call in the next six months--

MR. : Yeah.

MR. : --somebody wanted to talk to somebody at Enron, and somebody said to you, some one of your lawyers say, hey, somebody wants to ask us a couple of questions from Sumikomo, this would be why, because they have now demanded and the court is--the judge is going to make us show the names of those deals.

MR. : Okay. Is there--I'll--

MR. : Yeah?

MR. : No, I was going to say, let me lob a

call to our legal guide as well. This is in confidentiality. I know that, you know, you guys are obliged to show that; I just want to know that something is going on here.

MR. : Absolutely. And then, you know, I'll put them in touch with Phil Levy and to say to what extent the court has said show us this, which means, you know, for your eyes only, can never be revealed, blah, blah, blah, and they can explain all the nature of that. Which is what I'm sure the judge is saying--that sure, you can look at this, [inaudible] you can possibly disclose, share--

MR. : Right.

MR. : But it's--you know. So anyway--

MR. : Anyway, [inaudible] provided those performance LCs, didn't they--in those deals?

MR. : Um, you know--

MR. : That's the involvement, right?

MR. : Joe, I don't think that has anything to do with it.

MR. : So why--

MR. : It has to do with it because they were somebody else borrowing money. That's what their lawsuit is.

MR. : That Sumikomo was borrowing money--

MR. : Their metals people.

MR. : Right. Borrowing through the books.

And so explain to me, then, the discovery--

MR. : Well, I don't want to--I don't want to surmise that I know exactly the--but there's a lawsuit outstanding, which is, I think in the public record, that they're claiming, I think, that a lot of banks incorrectly lent them money through their metals desks. And they basically--they lost a ton of money. And again, I'm guessing, because I'm not that familiar. The metals desk lost a frigging fortune, I think.

MR. : Right.

MR. : On just bullshit trading and stuff. So I think they're going back to the banks saying why did you lend money to our metals desk.

MR. : Okay. But then, how did all these other deals get dragged into it?

MR. : Well, I think they're--again, I think the lawyers should know about this, but I surmise it--well, all right, well, what were your practices on lending money to the commodity desk?

MR. : Okay.

MR. : So how did you do it, and who did you do it with?

MR. : Right.

MR. : That has nothing to do with-- the bank side.

MR. : All right, I got--

MR. : So we--they were actually--

MR. : The bank faxed those issues.

MR. : I think so. And they were like an Enron rather than a bank.

MR. : Right. Okay.

MR. : But anyway. [inaudible] and who knows if they'll ever call, but I just wanted to let you know. And if they want to talk to Phil, you talk to Phil.

MR. : All right.

MR. : Thanks. Bye.

MR. : Thanks. Bye.

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1

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 011

September 28, 2001

12:39:28

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

MILLER REPORTING CO., INC.
735 8th STREET, S.E.
WASHINGTON, D.C. 20003-2802
(202) 546-6666

P R O C E E D I N G S

MS. : Phil Levy's office.

MR. : Hey. It's Jeff.

MS. : Hey.

MR. : I need--can you look at that fax for me? I need you to read something for me.

MS. : Sure. Let me just get it. Hold on.

MR. : Okay. I need--I need the one that's the confirmation between Mahcney and Enron.

MS. : Okay. Mahoney EMA confirm with collateral support on it.

MR. : Yeah. Could you just fax to me the confirm? Forget about the collateral support. How many pages is that? It can't be many, right?

MS. : You don't want the guarantee. So it's probably about six or seven pages.

MR. : Could you stick it on

right now, please?

MS. : Yep.

MR. : To 6205.

MS. : Six-two-oh-five.

MR. : Yep. Thanks.

MS. : All right. Bye.

[END OF TAPE RECORDING.]

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UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 40

September 28, 2001

12:34:26

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : Hello. Chase.

MR. : Phil, Jeff.

MR. : Jeffrey.

MR. : Hi.

MR. : What's up?

MR. : We're closing an Enron deal today.

MR. : Yeah, I was kind of wondering when you were going to call me.

MR. : Okay.

MR. : I'm the stepchild left in the closet.

MR. : It's not a physical deal. Sort of like--I'm sorry, I'm letting Mike [inaudible] handle this, and--all right. So, um--
it's not a physical deal; it's a financial deal. Everything's just been signed.

MR. : Mm-hm.

MR. : So the steps are going to be two instructions: one wire from Chase to Mahonia--it's just ChaseMan Bank New York.

MR. : Mm-hm.

MR. : And then one wire from Mahonia to Enron.

MR. : Okay.

MR. : Okay, and I'll give you those amounts shortly.

MR. : Okay.

MR. : If you could just get ready and tee up whatever you have to do.

MR. : Yeah.

MR. : It's going to be 350 million. Mike's already covered the funding that's coming in for this.

MR. : Okay. So Bullion should know that?

MR. : Yeah, hold on a second.

Hey, Donny? That 350? Is that coming from you or somebody else--

Yeah, it's coming from Don.

MR. : Okay, so Bullion will know this. I'll give them a call.

MR. : They will. And I'll call you shortly with those numbers. And I'll have--they're basically confirmations. They're actually--these are confirms which govern the prepayment.

MR. : Uh-huh.

MR. : So we will fax them to you shortly.

MR. : Okay.

MR. : But if you could just tee it up, I'll call you with the amounts shortly.

MR. : Okay.

MR. : Thanks. You going to be around?

MR. : Yeah. I need Enron's instructions.

MR. : You got them.

MR. : Yeah, I have them, but I just want to make sure we have the right ones.

MR. : Yeah, it's ENA. It's the same ones.

MR. : Same ones?

MR. : No, I think the instruction's probably part of the whole deal.

MR. : Do they give wire instructions in there?

MR. : It's whatever the ENA--yeah, it's whatever the ENA wire instructions are. So whatever we did the last time.

MR. : Okay. Is there someone I should--I can verbally confirm those--

MR. : Yeah, sure. Sure. Uh, hold on. The name's Michael Garberding. And--this fucking system of mine just sucks. Hold on. [Pause]

713--

MR. : Mm-hm.

MR. : --853--

MR. : Mm-hm.

MR. : One second. {Pause] 1864.

MR. : Okay.

MR. : And if he's not there, ask for Marcus.

MR. : Marcus.

MR. : [inaudible]

MR. : Huh?

MR. : [phone problem]

MR. : Huh?

MR. : [inaudible] 4243, and this guy Marcus.

MR. : 4243.

MR. : Call one of them, and then they're going to say what's the exact number you're pressing the button on. Say you'll call back in a second, let me just--Jeff's just got to give me that final sign-off, so I'll do it momentarily.

MR. : Okay. I just want to get the wire instructions. Okay.

MR. : Okay, bud.

MR. : Thanks. Bye.

MR. : Bye.

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942

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 42

September 28, 2001

13:30:00

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : Hi, buddy.

MR. : Hey.

MR. : All right, we can send that money out.

MR. : All right, give me--

MR. : Here's the deal. The money-- and all documentation will be faxed to you, but what we are sending to Enron from Mahonia--

MR. : Go ahead.

MR. : Is 349 million.

MR. : Even?

MR. : Yeah. That's Enron--Mahonia to Enron.

MR. : Okay.

MR. : And what it really is, is 350 less a million-dollar fee. I'll fax you the fee letter right now.

MR. : Okay.

MR. : What's your fax number?

MR. : 622-1836.

MR. : 1836, okay. So I'm going to send you that. So it's 349 even going from Mahonia to Enron.

MR. : And--

MR. : From--now, from Chase to Mahonia--

MR. : Mm-hm.

MR. : It's going to be three-fifty--350

million and five [sound glitch]. So 350,005,000.00--that's Chase to Mahonia.

MR. : Okay.

MR. : Now, let me make sure I got this right. Okay, right. So then Maho--

MR. : So now Maho--

MR. : Well, no, was it--I got--yeah three-point--right. Then what Mahonia does is Mahonia pays the 349 to Enron but keeps--but puts a million to us for P&L. That's our fee. You'll see that with the fee letter.

MR. : Yeah, but Mahonia's bal--Mahonia's account can't have a balance in it.

MR. : No, they're going to get three-fifty from--three-fifty--yeah, it can. Five thousand dollars. Sure it can. They're going to--then they'll dividend that out.

MR. : Yeah, but I'm telling you that whatever goes in that account must go out. It has to. You can't have--it has to be flat zero.

MR. : It can't be positive?

MR. : No.

MR. : Five thousand dollars?

MR. : No. No, I'll get a call from somebody in Funds Transfer [inaudible] saying that this account can't have balances.

MR. : Okay, well, we'll wire it out, then.

We'll get you some wire instructions. But it's gotten that--yeah, I mean, this is the way we used to do it.

MR. : Yeah, so if you can get me wire instructions to wire it out, then it will be flat. Because right now, if I'm looking at 349 going out the door, right, to Enron; and then I got 350,005 coming in from Chase--

MR. : And then a million bucks going out to--I guess you--you really don't have to--how do you have to do this? The million dollars from--how do you want to--how do we recognize the fee all the time? How do we do that?

MR. : Well, who's this fee--who's getting this fee? A million--

MR. : Basically, there's going to be three-fifty going from the Gold desk to the Energy desk, right?

MR. : Okay.

MR. : And then the fee comes to the bank. So do you just want to fund Mahonia with the 349?

MR. : Okay, yeah.

MR. : Do it that way?

MR. : Okay. And then the fee stays in Chase's account, but then how do we take that in? That's a straight P&L event?

MR. : Yup. Okay, now, you'll get the fee letter momentarily.

MR. : Okay. That's P&L, then.

MR. : Okay.

MR. : So then Mahonia's account's going to see 349 going--

MR. : --in, and 349 going out.

MR. : Yeah, but, my God, I want to get the $5,000 in there.

MR. : Well, if we can do that, Jeff--but I have to wire it out.

MR. : --instructions. I don't know where to wire the money for Mahonia.

MR. : Is that somewhere in the Channel Islands?

MR. : Yeah, it is, but I've got to--I can't--I've got to find out what that bank account is.

MR. : Can--can we contact them?

MR. : I could try. All right, could you tee up, then, and let that Mahonia and Enron go, because it's driving me bananans. Three-forty-nine even.

MR. : Three-forty-nine even going to Enron.

MR. : Going to Enron.

MR. : Yeah, and then we'll sort out those other details later.

MR. : I'll call you back in a minute. Yeah, so if you call me back, just tell me when you press the button.

MR. : Okay.

MR. : Can I just tell them you're sending it in a minute?

MR. : Yeah, you can tell them that, but it takes a couple of minutes to go through the Fed and all that other stuff.

MR. : All right, give me a Fed number. So it's 349 even, Mahonia to Enron. Great.

MR. : Right.

MR. : Bye.

MR. : Bye.

[End of recorded segment]

948

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 58

October 3, 2001

14:12:44

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

P R O C E E D I N G S

MR. : I'm going to get Kelly Little on. Hold on one second.

MR. : Who is this--Michael?

MR. : Yeah.

MR. : It's Jeff.

MR. : Hi, Jeff. How are you doing, man?

MR. : Yeah, Jeff just got on. You might repeat who was on the line again.

MR. : Okay. It's, on the gas-structuring side, it's going to be Eric Boyt [ph] and Kelly Little, and then on my side, it's myself and Brian Cully [ph].

MR. : Okay. I've got Kelly Little on the phone as well.

MR. : I guess really the purpose of this is, you know, with the conversions we're looking at doing to a physical--

MR. : Yeah.

MR. : One of the issues we had, since where prices are at, is, you know, volumes and where those volumes are going to go through, and we just wanted to make sure that it made sense for both parties, what kind of structure we're going to use. I know, in the past, I mean, in the past when I did, we ended up just using the Transco vitri [ph] point for all of the volumes, but I think prices

were a little bit higher at the point in time, and typically in the past I think we've used up to four points.

MR. : Yep.

MR. : Is there a preference from your side, when they put the structure together, of points to use?

MR. : There really isn't. I mean, you know, given the way we structure it, we do sell the physical back, I'm not really that stressed by any specific point. I think it's probably a good idea to spread it out only to your point. It's just we will pro--we've had more issues in the last, you know, year than we've ever had in terms of, you know, temporary disruptions or things that would require us to get on the phone and reschedule. So we might as well spread it out so we don't have it all at one point.

MR. : And then another question I think Eric had was, you know, is we've used these points in the past, but he mentioned just, I think, [inaudible] hub[?] or[?] something[?] like that?

MR. : Well, that was just something I didn't know where these guys may have contracts to do something like this. We're just going to match it up.

MR. : Right.

MR. : Yeah. Well, the hub is a problem because we're incurring more costs if we go through the hub, so we've always stayed away from that.

MR. : Okay.

MR. : You know, because, you know, at that point you're paying some transfer fees to schedule volumes at the hub, which we really don't want to do.

MR. : Sure, and I would agree with the--

MR. : So that's why we're picking these other locations.

MR. : Okay.

MR. : What else would you do besides, say, a Transco Zone 3?

MR. : We did TGT--

MR. : Yeah, we've done Texas Gas, Columbia Gulf, [?]sco, you know, even. We do sort of--where else could we do? I'm sure there's a couple of other Gulf points we can deal on.

MR. : Okay.

MR. : Tennessee. We can do a couple of Tennessee legs[?].

MR. : Tennessee legs[?]. Yeah, Mike, I think we just need to--I agree with the concept of spreading it out. I think we could probably do it at one point, but it may make more sense to spread it out, and then the big discussion is, you know, make sure Chase Mahoning[?], they all have similar type of contracts, such that this nomination[?] can go through without incurring any other fees.

MR. : That's right, and that's pretty much how they are designed on a back-to-back basis. They have all of the sort of requisite incentives from both parties that if, in fact, there were ever any fees, we would move pipes, we would, you know, just we're going to work to keep all of that pretty much zero, where it is--

MR. : Yeah. On these other--on these other deals that are physical, did we actually get confirmation from a pipeline, like a third-party [inaudible]--

MR. : You did.

MR. : Yes.

MR. : Okay.

MR. : So we actually do nom[?] at those locations.

MR. : All right.

MR. : Which is kind of awkward, right? Because then when they start cutting people radically[?], we actually sometimes have gotten cut, so then what we'll do is we'll always ask you to say, hey, you know, could you make sure we're a priority delivery because you're going to get it back from us.

MR. : Right.

MR. : So--

MR. : Okay. That was a question I didn't have. I've talked to our logistical people on

several occasions, and we've talked to the Transco rep, for example, saying, you know, what if we did want to do it at one location and try to move three-and-a-half bcf to a point where there really only is capacity physically for two.

MR. : Yeah.

MR. : Well, you know, it may raise a red flag, but technically you've got to be able to do it because it's a circle that comes--

MR. : True.

MR. : --you're the first purchaser or first provider, and it comes right back to you, so the pipes should just be able to confirm it either way, but it probably would be a little bit cleaner, as long as we can all agree upon the points and locations, and if we're all comfortable with no fees.

MR. : Yep. Yep. We've done it before. I'm pretty confident we'll get there.

MR. : Okay.

MR. : Michael, do you have any news on timing for this whole thing?

MR. : No, I think really what we're going to go through now, I think the LCs are moving forward. I think the discussions have been made, and they're going to be done on I think Tuesday, as had been agreed upon.

MR. : Okay.

MR. : And then that's why we're going to

go forward and start modeling up what a physical would look like, maybe start with the four points we did on the last physical deal we used.

MR. : Fine.

MR. : And start working toward that.

MR. : Okay. And give us a heads-up on the amounts and the actual banks associated with those LCs, if you could.

MR. : Will do.

MR. : Because I think we do have the right to look, you know, tell you whether or not they're acceptable or not, as long as we're not unreasonable.

MR. : Okay. No problem.

MR. : All right.

MR. : Anything else?

MR. : That's it, guys.

MR. : Anything else, Eric?

MR. : No, I think I'm fine.

MR. : Okay.

MR. : Sounds good.

MR. : Thanks. Be talking to you.

MR. : Okay.

MR. : Bye.

[End of Recorded Segment.]

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1

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

In the Matter of the Collapse of Enron

Dellapina, (AT) 098

October 10, 2001

14:11:04

[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

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elw 2

P R O C E E D I N G S

MR. : [Inaudible] and Calvert.

MR. : Hey, Winston, it's Jeff Dellapina.

MR. : Mr. Dellapina, how are you?

MR. : What's going on?

MR. : You know, just the usual.

MR. : Yeah? Which is what?

MR. : You know, just kind of hanging out watching the Astros lose again.

MR. : Oh, yeah. What's the score now?

MR. : It's 1 to nothing, Braves.

MR. : What inning?

MR. : Third.

MR. : Oh, that's a little early to be throwing in the towel.

MR. : Well, okay. I'll wait 10 more minutes and then throw in the towel.

MR. : Then you're going to chuck it in, huh? That would be pretty depressing if

elw 3

they went three and out here. That ain't going to happen.

MR. : Well, what's up?

MR. : Not much, man. Wanted a follow-up to our conversation on Friday.

MR. : Oh, yeah. Why don't we--why don't I talk to Steve this afternoon, and let's go back over it, because I want to make sure we get to, all the way to the back where you were talking, also about slopping in the oil and all that good stuff.

MR. : Okay. Were there any structural pieces that we sort of didn't--either you weren't, you know, thinking about the same way as we were, or--because I thought one thing that was interesting, how do you account for this thing as a forward sale? And how do you--do you put it on the books at 75, and then do you recognize some accrued interest on it, or how does that--

MR. : No, we just put it on the books at $75 million.

MR. : Okay, so you don't incur

elw

4

any--

MR. : No, and then we start amortizing it as we--as we start delivering barrels.

MR. : Okay, so let me just think about that. Okay, but when you actually sell them, when you sell the--how does that--

MR. : We actually [inaudible]--

MR. : Do you change the price of the gas, that you're actually selling it at? Do you acknowledge you're selling it at--well, you don't even know what you're selling it at.

MR. : Right.

MR. : So you don't even have to --okay, so this is kind of cool because you don't actually show any interest expense.

MR. : Right, until we start delivering barrels, and then we--

MR. : Which is a pretty damn good reason to think about rolling it off the--

MR. : [Laughter.] Yeah.

MR. : --any reason you want to

elw

shell like $5 million more--

MR. : [Laughter.]

MR. : Okay, I see, yeah. Okay, so that's good to know.

MR. : It's really as--it's really deferred--I mean, we do it as deferred revenue.

MR. : When you get the last, the crude to you--

MR. : And really, I'm not even sure we show interest from it, I mean at all, even when we start delivering the barrels. It's really just more that was our--it just goes into our calculation of realized price.

MR. : Well, that's right, so if you get--if you wind up getting $140 million for that gas, well, yes, then you just--how do you, let's see, how do you do--you just--it all goes to revenue, but the--let's think about that. So when this thing--let's say you deliver the gas, and let's say gas is twice as much the day you deliver it. It's $5. So you give me the January gas.

elw 6

You're going to book revenue of $5, right?

MR. : Uh-huh.

MR. : You're going to then incur--what are you going to--are you going to then take, you know, part of the deferred revenue down--

MR. : No. Okay, let's say I deliver--when I start delivering to you, and let's say we're at the price of $2.65.

MR. : Yeah.

MR. : Okay, and let's say that regular prices are like $4.

MR. : Yeah.

MR. : We're going to recognize that we delivered to you at $2.65, and it's just going to lower our overall realized price. You see what I'm saying? And embedded in your $2.65 number is interest. Okay? How we got to the $2.65 is that you, you know, you had--you sort of calculate interest in there. But all we do is, we say, "Well, we delivered, we sold your gas, we sold gas to you at $2.65 even though the market was $4."

MR. : All right, but this case

is a little different, right? So if the market here is $3--

MR. : Uh-huh.

MR. : --when you deliver me that gas, I'm going to give you another 50 cents.

MR. : Yeah.

MR. : So I guess you're basing it--

MR. : I'll just say my realized price is $3, or whatever the net is.

MR. : Your realized price is $3.

MR. : Right.

MR. : So then basically the entries would be, deferred revenue goes down by $2.50 times the volume, cash goes up by 50 cents--

MR. : Uh-huh.

MR. : --and then your equity account shows a revenue of $3--

MR. : Uh-huh.

MR. : --and then you have whatever costs and expenses are associated with taking that gas out of the ground and delivering

elw 8

it.

MR. : Right.

MR. : Okay. That's kind of a neat way to do it.

MR. : Yeah.

MR. : All right.

MR. : I mean, that's one of the reasons why, you know, we liked it.

MR. : Oh, it's tremendous, yeah.

MR. : Right, but I mean we can't have too much of it, because everybody starts getting a little sort of--

MR. : Yeah, like everything else, right? Keep it under the radar screen.

MR. : That's right.

MR. : Basically the whole of structured finance.

MR. : That's right.

MR. : All right. Well, then--

MR. : Okay, let me talk to Steve, because he wanted to get back with you. I think the only thing he was concerned about is,

elw 9

he's afraid that we're missing something.

MR. : Yeah.

MR. : He's afraid that--he's just--I think he's a little afraid that there's more juice in it for you guys than we know.

[Laughter.]

MR. : Yeah, but--

MR. : Because it comes too easy. But I'll--

MR. : No, basically what it is, is when we bought the gas from you, we paid $2.50, right?

MR. : Uh-huh.

MR. : Less the value of the premium.

MR. : Uh-huh.

MR. : Because you now were buying a put from me, effectively.

MR. : Right.

MR. : And you can look at it--I think you've got to look at it as a put at the moment, right? So you sold me the gas at $2.50,

elw 10

but at the same time you bought from me the put at $2.50--

MR. : Uh-huh.

MR. : --right? Which means you can basically--you can't go lower than $2.50. And I know we got hung up on that because he was looking at it more like a call.

MR. : Right.

MR. : Right? So can you see how that works, more that the fact that the economic or derivative elements of it are as if you bought a put from me at $2.50? You could have bought that put at any strike, and I could have agreed to pay you any other price for the commodity.

MR. : Yeah.

MR. : Like basically you could have bought a put at $3, struck, but I still could have paid you $2.50.

MR. : Yeah.

MR. : We just happened to coincide the two.

MR. : No. I think, I mean, I

elw

think he agrees. I think it's just that's really more of a sort of semantic.

MR. : Yeah. Yeah, it is.

MR. : It's just that it's a difference without really--I mean, I just don't think it's that big a difference.

MR. : Okay.

MR. : I think he does understand that there's two different elements to it and, you know, you can value them separately. And he just wants, I think he really kind of wants to understand what the value of those two are in separate--

MR. : Okay.

MR. : --and then how do we translate that value into doing a new structure that would make sense?

MR. : Okay. Now, do you understand that? While I have you on the phone, I just want to make sure you understand it. Because what we do is, we just say let's take the value of what we have today, and we're going to sum

elw

everything back to a present value and just discount it all. So we look at everything on the books today--

MR. : What do you discount it at?

MR. : Well, we have--in both cases we were using liable plus 100.

MR. : Okay.

MR. : Which is basically saying that's to your benefit when you buy back the 02 and 03, because you're getting it back cheaper. But if we use a higher discount rate, the cost of you having to replace the 02-3 piece is better for you. But then we use liable plus 100 on the back piece, too, so it's consistent. It's exactly the way it should be. But I'm losing you there already.

MR. : Well, if, you know, you start--no, I think I understand.

MR. : I mean, what I'm saying, what would work great for me but you're not going to let me get away with, say if we roll this thing forward, I give you all of that gas of 02 and 03,

you buy it back, at liable or flat--

MR. : Right.

MR. : --but then you'd be punished. You want it at a higher interest rate because you want to buy it back cheaper.

MR. : Right.

MR. : Then when you sell it to me in the back, because all you've done is rolled this financing out two years--

MR. : Right.

MR. : --and then you're going to basically sell that to me back there at the same discount rate, at the same spread. That's the principle. So I'm trying to equate everything back to its present value today. So what we do is, we take that 02 and 03 piece right now--

MR. : Uh-huh.

MR. : --and we say that gas on the basis of $2.50 is valued at X, fully discounted.

MR. : Uh-huh.

MR. : And let's say the number

is $88 million or something like that.

MR. : Uh-huh.

MR. : But at the same time, if you also are giving me back the put, I'll pay you the current value of the put.

MR. : Right.

MR. : Because I've got to give you that benefit.

MR. : Because you own this put in there. So then we take that off the $88, because if you don't own that put any more, that protection, basically I'll buy it back from you, so then we solve to a net number, whatever that number is. Say it was $83 million or something.

MR. : Uh-huh.

MR. : And then we say, okay, if that costs you $83 million to take the whole structure out today, which means buy back the $2.50 gas but then give me the put back on a net basis, say that's $83 million, then what we say is, any structure we can come up with will solve for $83 million. Anything you want. You can sell me

bananas, you can sell me gas, you can sell me crude.

But if you're not going to exchange cash, you've just got to give me forward value stuff worth $83 million, and that's all we do. We just trade the first thing, whatever the current thing was, and then we try to solve for anything in 04 and 05 that's worth and gives you the best characteristics but has a present value of $83 million, and then it's a totally even exchange.

MR. : Yeah. No, and I think I understood what you're doing. I guess the real issue that Steve's struggling with is, you know, he looks at it--you know, I go back to this call/put sort of thing.

MR. : Yeah.

MR. : He looks at it as if we have a call, we have swapped out at a certain price and we have a call at another price.

MR. : Right.

MR. : Okay? And so he's saying, you know, that call is worth a lot. He thinks

that--he feels like the call at $2.50 or whatever it is is worth a certain amount of money. He's not sure he understands how you're--

MR. : Okay, so let me tell you how that would work, then.

MR. : Yeah.

MR. : So then you could do, which will get you through the same number--

MR. : And that's what I need you to do, sort of demonstrate--

MR. : Yeah, what we call parity, right. What you could do is say, "Okay, Steve, I'll sell you back the call, the $2.50 call. I'll buy back the $2.50 call from you." And let's say that thing is worth $1.50. An enormous amount, right? "But at the same time that you get that positive $2.50, you have to buy back the gas from me, and you're going to pay current market."

MR. : Right.

MR. : And that current market may be, you know, $3.30. Right?

MR. : Uh-huh.

MR. : And that's where, that's where--and let's just say in that example, so you've got to buy back the gas from me and it's basically today's pump, because you sold me the gas, so whatever the price is for that gas today. It's $3.20. But then you own this call, so you give that back to me--I'll give that back to you at the--

MR. : You ship that out for the same number.

MR. : Yeah. That's like--exactly.

MR. : And what you need to do is show how that nets out.

MR. : Perfect. All right. Thanks.

MR. : If you do that, I think he'd go along with it.

MR. : All right, so we'll just--that's exactly what we'll show him.

MR. : Okay.

MR. : All right? And then we'll

hopefully sort of take this off, because it's really not as critical a price risk management tool as it is a--it's probably a little bit more of a financing tool than a price tool right now.

MR. : Yeah.

MR. : I mean, but having said that, I think you definitely should be opportunistic where you think there's value in crude, as we talked about last year. God knows it's probably $30 million that thing has moved, so you can be opportunitistic about it. Switch it to crude, switch it further out in gas.

MR. : Yeah. I just look at, and maybe I'm really simplistic, but I look at it as the BTU value of gas has come down a lot quicker than the BTU value of oil over the last six months, so--

MR. : And carrying that out, you think that long--you know, over time the BTU value of gas is going to improve relative to the BTU value--

MR. : That's right.

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19

MR. : So on that thesis, if you had the ability, you would still be inclined to move it to crude.

MR. : Right, and that's what I--that's where I think maybe there's some juice in the trades, because I think that always--there are always going to be differences in BTU values. They are all going to kind of move in different--but they're always going to come back to each other at some point in time, because it is just heating value, and there is a certain amount of fuel switching from crude to natural gas.

MR. : Right.

MR. : It always kind of moves those lines back together. And when they diverge so much, that's when you need to do something on one side or the other, because natural gas moves on its own because of the way, the nature of the BTU--

MR. : Right.

MR. : But at the end of the day, if natural gas gets too high, then the BTU value in the crude becomes more valuable and people start

buying crude.

MR. : Okay.

MR. : And people start buying crude. Do you see what I'm saying?

MR. : Perfectly understand what you're saying, and let me just make one comment to that. That is perfectly spot-on and a pretty linear decision if you had sold the gas just like a swap, if you had just sold us fixed-price gas--

MR. : Yeah.

MR. : --and you didn't have this sort of, as you call it, the call structure.

MR. : Right.

MR. : So, for example, the deal you did with us in crude was exactly that concept. You know, we're trying to--you know, because you sold at fixed price.

MR. : Yeah.

MR. : So at some point if crude crapped out so much and gas was high, you should do that. You should switch it to gas.

MR. : Yeah.

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MR. : But now with the way you have this particular gas trade on, the way you're realizing the benefit of gas having come way down versus crude is (a) when the put, or the call, if you will, I call it the put, has increased in value, and you would switch it to crude. One, you wouldn't get as much of a benefit, but you get some of that BTU benefit because of the put structure. The real benefit in that trade, the massive benefit, too, would be when if gas exploded, you would just switch it back to gas and you would make a ton of money on that trade because you would need almost no gas to deliver.

MR. : Right, right.

MR. : That's what you would be prepared for, because in the first step move from gas to crude, it's good but it's not a great transfer right at that day. It sets up the great trade later on, which is moving it back to gas in a year. Then you can make a fortune--

MR. : Yeah.

MR. : --because if oil migrated

to 20 and gas migrated back over 4, you could switch it back to gas, and instead of doing like 50 a day, you're delivering, you know--

MR. : 25 a day?

MR. : Yes, exactly.

MR. : Right.

MR. : That's the trade.

MR. : Yeah.

MR. : Okay.

MR. : Well, gas is up today a little bit.

MR. : Yeah, we're rocking here on a higher AGA number--a lower AGA number but--

MR. : Well, you know, my guess is, people laying down those rigs, I think production's going down.

MR. : Yeah, I think it's down. The only thing we've got to remember is--

MR. : I mean, we're struggling onshore--

MR. : Yep.

MR. : --and I think a lot of

people are struggling onshore.

MR. : Yep.

MR. : So--

MR. : So if we have a winter like last year, we'll fix the problem quickly. The question is, as this market is, is the weather is so important. If we have a normal winter, you know, like the last 10 years, and we're 7 percent warmer, then the supply reductions aren't going to offset the demand.

MR. : Yeah.

MR. : So really I think you're right. If the weather is good, I think we can run through a lot of this storage overhang.

MR. : Yeah.

MR. : So, yeah, pretty good stuff.

MR. : All right.

MR. : So I'll put that little, you know, thing together, and then you want to schedule something and come back to me?

MR. : Yeah. Once you finish

that, we'll just set something up for like tomorrow or something.

MR. : That's cool. Thanks.

MR. : Okay?

MR. : Bye.

[END OF TAPE RECORDING.]

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Greater than BBB+ or Baa1	Greater than BBB- and Baa3	Less than BBB- or Baa1
30.0 Bps	37.5 Bps	62.5 Bps

Adjustments in LIBOR margin during contract term shall be made through adjustments in volumes delivered to be determined at the end of the term.

ARRANGEMENT FEE: 0.20%

COSTS: Legal fees, including those associated with syndication, and customary transaction costs.

DOCUMENTATION: Standard Enron-Mahonia documentation with the addition of the Security Agreement attached to the Enron Risk Management Services-Chase ISDA trading agreement, to cover collateral for mark-to-market exposures.

SYNDICATION: Enron performance obligation, pursuant to guarantee of Seller delivery obligation, to be syndicated through a performance letter of credit ("PLC"). PLC upfront and usage costs to be paid by Chase.

FOIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

Prepaid Hydrocarbon Forward Sale - Option 2

Floating Price Facility

TERM:	5 Years.
AMOUNT:	Up to $300 million payment for future deliveries of natural gas or crude oil.
CONTRACT PARTIES:	Purchaser: Mahonia Limited, an SPC established by Chase / or The Chase Manhattan Bank. Seller: A wholly owned subsidiary of Enron Corporation.
GAS DELIVERIES:	Equal quarterly installments from January 1997 to June 2001.
FLOATING PRICE FACILITY:	Each hydrocarbon delivery obligation will equal, in MMBtu of gas or barrels of WTI crude oil, a set dollar amount*. The hydrocarbon price for any delivery - and therefore the MMBtu/crude oil obligation - can be fixed by Enron with the SPC at any time before that delivery date. Enron also has the facility to initially position its gas/oil sales to Mahonia to any date(s) before the final delivery dates (with the intention to roll out to each final delivery date). The roll adjustment is expressed in terms of incremental MMBtus of gas/oil. *The choice of hydrocarbon for each delivery is at Enron's election.
REVENUE PREPAYMENT COST:	Hydrocarbon revenues prepaid at a rate of LIBOR plus a margin as determined in Option 1.
ARRANGEMENT FEE:	0.35%
COSTS:	Legal fees, including those associated with syndication, and customary transaction costs.
DOCUMENTATION:	Standard Enron-Mahonia documentation with the addition of the Security Agreement attached to the Enron Risk Management Services-Chase ISDA trading agreement, to cover collateral for mark-to-market exposures.
SYNDICATION:	Enron performance obligation, pursuant to guarantee of Seller delivery obligation, to be syndicated through a performance letter of credit ("PLC"). PLC upfront and usage costs to be paid by Chase.

FOIA CONFIDENTIAL TREATMENT
REQUESTED BY JPMC

Prepaid Gas Forward Sale - Option 3

Flexible Delivery Facility

TERM:	5 Years.	
AMOUNT:	Up to $300 million payment for future gas deliveries.	
CONTRACT PARTIES:	Purchaser:	Mahonia Limited, an SPC established by Chase / or The Chase Manhattan Bank.
	Seller:	A wholly owned subsidiary of Enron Corporation.
GAS DELIVERIES:	Seller may deliver gas on any date(s) before December 2001.	
FLOATING PRICE FACILITY:	The initial delivery obligation is set to December 2001 and will equal, in MMBtu of gas, a set dollar amount. The gas price - and therefore the MMBtu obligation - can be fixed by the Seller with the SPC at any time before delivery date. Roll adjustments to ultimate delivery dates will be expressed in terms of incremental MMBtu of gas.	
REVENUE PREPAYMENT COST:	Gas revenues prepaid at a rate of LIBOR plus a margin as determined in Option 1.	
ARRANGEMENT FEE:	0.55%	
COSTS:	Legal fees, including those associated with syndication, and customary transaction costs.	
DOCUMENTATION:	Standard Enron-Mahonia documentation with the addition of the Security Agreement attached to the Enron Risk Management Services-Chase ISDA trading agreement, to cover collateral for mark-to-market exposures.	
SYNDICATION:	Enron performance obligation pursuant to guarantee of Seller delivery obligation, to be syndicated through a performance letter of credit ("PLC"). PLC upfront and usage costs to be paid by Chase.	

OCT-15-1998 10:16 P.24

FOIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

Prepaid Natural Gas Forward Sale - Option 4

Securitized Natural Gas Revenue Floor Facility

TERM:	5 Years.	
AMOUNT:	Up to $300 million for future natural gas deliveries.	
CONTRACT PARTIES:	Purchaser:	Mahonia Limited, an SPC established by Chase / or The Chase Manhattan Bank.
	Seller:	A wholly owned subsidiary of Enron Corporation.
REVENUE FLOOR:	$2.00 / MMBtu	
GAS DELIVERIES:	Equal quarterly installments from January 1997 to December 2001.	
SECURITIZED FLOOR FACILITY:	The Gas Seller establishes, through Mahonia, a revenue floor at, for example, $2.00/MMBtu. Mahonia funds the floor immediately in the form of a prepayment. The value of the prepayment is the present value of the floor less it cost. With this facility, Enron has the ability to resell the floor to recoup the cost of the floor, concurrent with the prepayment, or in segments through the term of the transaction. Enron can also fund the cost of the floor by selling offsetting caps. On each quarter date, the Gas Seller delivers natural gas to the excess multiplied by the scheduled by the Revenue Floor.	
EXCESS REVENUE PAYMENTS:	On any quarter date during which the price of natural gas exceeds $2/MMBtu, Mahonia will pay Enron an amount equal to the excess multiplied by the scheduled MMBtu. The transaction therefore houses two cash flows: An immediate prepayment of the Revenue Floor and a potential incremental payment to reflect any appreciation in the natural gas price over the floor.	
REVENUE PREPAYMENT COST:	Natural gas revenues prepaid at a rate of LIBOR plus a margin as determined in Option 1.	

FOIA CONFIDENTIAL TREATMENT
REQUESTED BY JPMC

Mourant & Co.
TRUSTEES LIMITED

P.O. Box 87.
22 Grenville Street.
St. Helier.
Jersey JE4 8PX.
Channel Islands

Tel: 01534 609000
Fax: 01534 609333
Telex: 4192064
International
Tel: +44 1534 609000
Fax: +44 1534 609333

Direct Dial: 01534 609290
via secretary

D.L. Dubin, Esq.,
Chase Investment Bank Limited,
125, London Wall,
London, EC2Y 5AJ

11 December 1996

Our ref: GEC/SG/8322-1/22268-3.72/G12

Dear Drake,

Re: The Eastmoss Trust / Mahonia Limited

I refer to your letter dated 9th December, 1996 addressed to Ian James. On behalf of the Eastmoss Trust I am pleased to confirm the Trustees willingness, in principle, to permit the participation of its wholly owned subsidiary Company known as Mahonia Limited in the "Enron V" transaction proposed to be structured by Chase Securities Inc. in the manner and upon the terms set out in your letter of 9th December, 1996 and the term sheet appended thereto.

In return for participating in the transaction described in your letter Mahonia Limited would levy a fixed management and administration fee of £15,000 exclusive of any legal costs incurred by the Company as a result of its participation in the transaction. In addition, the Trustees would expect a profit of approximately £1,000 to accrue to the Company as a result of its participation in the transaction.

Should the structure of the transaction change significantly or be amended during its life time or extended beyond its expected life time, Mahonia Limited would reserve the right to negotiate an appropriate additional fee.

Yours sincerely,
For and on behalf of
Mourant & Co. Trustees Limited

Authorised Signatory

COPY

OIA CONFIDENTIAL TREATMENT
REQUESTED BY JPMC

A Company owned by Moura

Permanent Subcommittee on Investigations
EXHIBIT #185b-1

The Chase Manhattan Bank
JPMorgan
270 Park Avenue 6th Floor
New York, N.Y. 10017

September 28, 2001

Mr. Joseph M. Deffner
Chief Financial Officer
Enron North America Corp.
1400 Smith Street
Houston, TX 77002-7361

FEE LETTER

Subj: Fees associated with the prepaid natural gas swap between Enron North America Corporation ("ENAC) and Mahonia Limited ("Mahonia")

ENAC and its ultimate parent, Enron Corp., (collectively "Enron") have requested The Chase Manhattan Bank ("Chase") to arrange a prepaid, natural gas swap in the amount of approximately $350,000,000.00 (the "Transaction") between ENAC and Mahonia. In connection with the Transaction, Enron has agreed to pay an arrangement fee of $1,000,000 at closing. In this connection, Enron acknowledges that Chase shall be forwarding the prepayment amount for and on behalf of Mahonia and agrees that Chase may deduct the fees from the prepayment amount of approximately $350,000,000.00 resulting in a net payment to Enron of approximately $349,000,000.00.

Please acknowledge your agreement with the above by signing below.

Regards,

Jeffrey W. Dellapina
Managing Director
The Chase Manhattan Bank

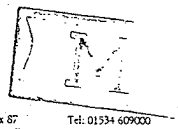
Acknowledged and Agreed by:

Mr. Joseph M. Deffner
Chief Financial Officer
Enron North America Corp.

Permanent Subcommittee on Investigations
EXHIBIT #185b-2

SENATE
MAH - 03273

FOIA



Mourant & Co.
LIMITED

PO Box 87
22 Grenville Street
St Helier
Jersey JE4 8PX
Channel Islands

Tel: 01534 609000
Fax: 01534 609333
Telex: 4192064
International
Tel: +44 1534 609000
Fax: +44 1534 609333

The Chase Manhattan Bank
270 Park Avenue
40th Floor
New York
NY10017
USA

Your Ref:
Our Ref: 22268/41218/12/JUC
Bill No: S42864
29 October 2001

Mahonia Limited		
Administration Fees		8,645.69
Sundry Disbursements and Service Charges		124.31
		£8,770.00

For terms and details of payment see overleaf

Please detach and remit with payment

We enclose a cheque for £.....

Amount £8,770.00.....

Our Reference 22268/41218/12/JUC.....Bill No S42864 .....29 October 2001 .....

FOIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

Permanent Subcommittee on Investigations
EXHIBIT #185b-3

To: Ronald Potter @ Chase
cc:
From: Peter M. Lipsitz NAS CorpFin: Energy 713-751-8661 Fax Number: 713-751-8122
Date: Thursday December 18, 1998 03:20 PM
Subject: Enron Natural Gas Marketing (Mahonia Limited)

Ron,

As I understand the transaction now, Chase will be putting on a direct loan to Mahonia Ltd. guaranteed by Enron Corp for the $350,000M (previously approved for $352,000M)
Chase will be receiving $327,500M in Performance Letters of Credit which represents the participating Banks pro-rata share of the facility.
Also, Chase will be issuing a PLC for their share as well in favor of Mahonia Ltd. which from a GES systems standpoint constitutes additional Enron Corp exposure of our share of the PLC which will be $22,500M.
Thus, I will need the approval from yourself and Mr. Nelson to set up this PLC for $22,500M.

Thanks & Regards

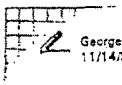
Approved: Potter Edward L. Nelson Jr.

Ronald Potter Edward L. Nelson, Jr.

JPM-6-04212

FOIA CONFIDENTIAL TREATMENT
REQUESTED BY JPMC

Permanent Subcommittee on Investigations
EXHIBIT #185c



George Serice
11/14/97 10:59 AM

To: Greg Nelson@CHASE, Peter Gleysteen/CHASE@CHASE, SusanF Stevens@CHASE
cc: Tad Benton/CHASE@CHASE, Karen Simon/CHASE@CHASE, Christian Gates/CHASE@CHASE
Subject: Heads-Up memo; Upsize to previously approved Enron Prepay;

Last week I took the $250MM Enron 97 Prepay Performance Letter of Credit through deals (underwritten deal). The account party on this PLC is Enron Corp. and the paper backs up the performance of an Enron subsidiary, which entered into a natural gas prepay. Upfront pricing for Chase is 40 bps (vs 35 bps for '96 prepay) and PLC fee is 22.5 bps (same as 96 prepay). Please note that the PLC is capital advantaged, so yield is 45 bps, a 50% premium over flagship drawn cost.

Enron seems OK with pricing, but asked if we can increase the underwrite from $250 to $300MM. Credit is OK, and our target hold is $30MM.

I have adjusted my supply/demand to incorporate a few new banks (in addition to the '96 Prepay banks) which have approached Enron in the past couple of weeks anxious to do a deal before year-end. Enron doesn't want the market-out language in the commitment letter, as we can launch the deal next week. We have discussed choppy markets with them and will have another discussion with them before we seal the deal. Enron has been very active in the bank selection process and they will exert pressure on banks if we need them.

Permanent Subcommittee on Investigations
EXHIBIT #185d

Memorandum

September 22, 1998

To: Jim Biello

From: Bob Mertensotto

CC: Jeff Dellapina
Rick Walker

RECEIVED
BY
CREDIT DIVISION
OCT 8 1998
Time
By
Texas Commerce Bank N.A. Houston

Re: Enron Prepays (1996 & 1997)

ACTION REQUESTED:
Approval to replace existing SBLC which provide credit enhancements to the 1996 Enron Prepay ($163.617 million exposure balance) and the 1997 Enron Prepay ($255.759 million exposure balance) with five to six surety bonds from issuers outlined below:

Company	S&P Rating	Capital Surplus ($Billion)	
1) Continental Casualty	A+	5.4	
2) Fireman's Fund	A	2.8	
3) Liberty Mutual Ins	AA	6.1	
4) SAFECO Ins	AA+	1.0	
5) St Paul	AA	2.7	
6) Travelers Casualty	A+	2.8	(Travelers Casualty & Travelers Indemnity
Travelers Indemnity	A+	2.7	viewed as one entity)

(These surety bond providers have been approved by Mark Malloy as acceptable credit enhancement entities.)

The syndication allocations are currently being determined and Enron is seeking to minimize concentration levels (i.e. less than $90 million per insurer). Further, the papers will track the June 1998 Enron Prepay surety bond structure where as Enron would agree to replace a surety if that surety were downgraded below A-. The remedy is increased pricing (35 bps p.a. on the relevant portion) if no replacement within 30 days. From a drawing perspective, the surety bond included the same "no questions asked" drawing provisions as the LCs.

It should be noted that each of the four outstanding deals (the 1994, 1995, 1996 & 1997 Enron Prepays) involved LC credit enhancement, though no mechanism existed to require the replacement of LC banks in the event of a bank downgrade/default. The logic being that Enron may be perfectly healthy and performing its monthly obligations while, as a result of an event beyond its control, it may experience the "snowball" effect of a technical default should one of the banks downgrade.

Enron will be paying a fee of $100,000 for accommodating them on this request.

Background:
As you are aware, CMB currently has four Enron Prepay structures in place which are supported by Performance Letters of Credit ("PLCs") and one Enron Prepay, which was recently put in place, supported by insurance company surety bonds. As Enron looks for ways to free up additional bank capacity in the market, they have asked CMB to work with them by allowing them to replace all of the existing PLCs supporting the '96 &'97 Prepays with insurance company surety bonds. The total remaining PLCs balance on the "96 & '97 Enron Prepay PLCs Facilities is approximately $419.376 million with CMB's portion being $33.11 million. (Attached is a schedule delineating the bank group, debt rating of bank, exposure levels by bank, PLCs balances for each of the '96 & '97 Enron Prepay structures contemplated by this request.)

Permanent Subcommittee on Investigations
EXHIBIT #185e

Enron would like to replace all of the PLCs with insurance company surety bonds, acceptable to CMB, which would have an "A" rating or better. Enron proposes to bring an additional five to six insurance companies to work along with Liberty Mutual Insurance Company ("AA" rated) and Travelers Casualty and Surety Company ("A" rated) to supply the credit support on the remaining Enron Prepay PLCs Facilities (thereby working with a total of up to six insurance companies). The structure/documentation would be similar to the existing Enron 1998 Prepay credit enhanced by surety bonds.

Approved by:

Jim Fiello Date 7/9/98

(Return via Fax to 713-216-4295)

Davis_Thames@enron.net on 06/19/2000 09:59:32 AM

To: Gregory Crowley/CHASE@CHASE
cc: Joseph_Deffner@ECT.enron.net, Lisa_Bills@ENRON.enron.net
Subject: June 2000 gas prepay

Gregory;

Wanted to take you through the methodology that I used to arrive at these prices:

For each delivery point, calculate a fixed 5-year price using Libor+0 as the discounting function. Assume a fixed 5 year volume to start. I used 32,900 MMBtu/d for Sta65, 40,000/d for ColGulf, 40,000/d for TGTSL, and 30,000/d for ELa.
Set up two discounting tables for the $250mm tranche and the $400mm tranche for each delivery point using L+72.5 bps for the discount function on the $250mm tranche and L+57.5 bps for the $400mm tranche.
Figure out how you will allocate dollars to each delivery point by taking the product of the fixed price at a point with its volume, then dividing that by the sum of the fixed price * volume for all four points. Daily volumes are fine. Multiply this fraction by the two tranche amounts ($250mm and $400mm). That tells you how much of the total each delivery point will contribute. I had 23.3% for Sta65, 28.0% for ColGulf, 28.0% for TGTSL, and 20.7% for ELa.
Knowing your target for the L+72.5 piece, let 100% of the volumes pay off that part until the sum of the fixed price * PV volume reaches your target. In the final delivery month, less that 100% of that month's volumes will go to pay the 72.5 bps piece.
Allocate the rest of that month's volumes to the L+57.5 bps part along with the remaining deliveries. The sum of the PV revenues of both tranches should be equal to the allocation for that delivery point.
To calculate the 1 year strip prices, sum the calculated PV volumes from each tranche (this gives you the blended discounted volumes). Multiply that month's price by the curve price to get PV revenue for that month. Calculate a fixed price for the year that gives you zero MTM for that strip. Repeat for every year, with the terminal year being the short strip.
Undiscount the PV volume in your blended strip by dividing by the appropriate discount factors to get your absolute volume. Divide by the 1 year strip fixed price to get your 1 year strip volume.

Don't hesistate to call if you have any questions or if you think there's an error - 713-853-1492.

Best -
Davis

FOIA Confidential
Treatment Requested
by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #185f

SENATE
MAH - 00757

From: <Philip.Levy@chase.com>
To: <gareth.essexcater@mourant.com>, <julie.carter@mourant.com>
Date: 28 June 2000 03:49:52
Subject: Enron-Mahonia-Chase Transaction

The following documentation forwarded by Vinson & Elkins is acceptable and may be executed by Mahonia:

Natural Gas Inventory Forward Sale Agreement
Margin Agreement
Enron Guaranty
Duplicate Information Letter Agreement
Hedging Strategies Letter

As indicated in Cliff's email, please have Ian execute six (6) originals, fax one of each and overnight all 6 originals directly to Vinson & Elkins, along with the originals of Mahonia's documentation (including legal opinion).

Also attached please find execution copies of the following Chase-Mahonia documents:

Natural Gas Forward Sale Agreement
Security Agreement

An executed Limited Recourse Letter will be faxed along with the signature pages of these documents signed on behalf of Chase tomorrow. Please have Ian execute two (2) originals, fax one of each and overnight all originals to me, along with the originals of Mahonia's documentation (including legal opinion).

Obviously, all confirmation letters (Margin Price and Gas Sale) will be finalized on Thursday morning upon funding.

Thanks once again for your prompt attention and assistance on this transaction. Please feel free to contact me should there be any questions or problems.

Regards,

Phil

(See attached file: Chase-Mahonia Gas Forward Agmt 6 00 (Enron).doc)(See attached file: Chase-Mahonia Security Agmt 6 00 (Enron).doc)

CC: <Jeffrey.W.Dellapina@chase.com>

Permanent Subcommittee on Investigations
EXHIBIT #185g

From: Gareth EssexCater
To: michael.sabloff@chase.com
Date: 09/05/00 15:21:47
Subject: Re: Mahonia Limited

REDACTED

22268

re our telephone conversation concerning trading profits on the various oil and gas deals participated in by Mahonia Limited, and Stoneville Aegean Limited I have reviewed our archived records to see if I could find any useful information on the earlier trades and in particular anything relating to anticipated trading profits for the SPV's. As we discussed, all the profits achieved on the post November 1998 deals are agreed.
Unfortunately, Im not sure the information on our early files will be of great use. Nevertheless I list below the various pre November 1998 trades and such information as I have about the agreement on profits / fees.

Specifically relating to the Stoneville Aegean retained earnings you hold my understanding of the trades participated in by this Company (the first two Enron trades and the first MG trade particularly) is that the oil acquired was sold on an EFP basis to meet the Company's obligations under oil swap agreements with Chase. Also Chase funded all initial and ongoing margin payments in relation to the NYMEX positions and any net gains arising as a result of the futures positions were accordingly payable to Chase under the oil swaps. Our fees were levied on a fixed basis and did not seem to be factored into trading prices as obviously as in later trades. Our costs in respect of all these trades were of course settled including an element that represented in our books a net profit for the SPV (around £1000 per deal).
Given that it seems to me the amount held must be an amount payable to Chase under the oil swaps - do you agree?

DETAILS OF TRADES:

1. December 1992. Enron I. S. Aegean participant. All costs inc SPV profit paid.
2. June 1993. Enron II. S. Aegean / Mahonia participants. All costs paid.
3. REDACTED
4. December 1994. Enron III. Mahonia participant. All costs paid.
5. REDACTED
6. September 1995. Enron IV. Mahonia participant. All costs paid. Deal runs to June 2000.
7. REDACTED
8. December 1996. Enron V. Mahonia participant. Oil and gas acquisition - credit agreement and commodity swap with Chase. No trading profit anticipated. All costs paid.
9. REDACTED
10. REDACTED REDACTED

11. December 1997. Enron VI. Mahonia participant. Gas trade. Gas cost - $299,991,678.74. Sale receivables - $300,004,178.74. $12,500 paid to SPV.
12. June 1998. Enron VII. Mahonia participant. Gas trade. Gas cost - $250,000,000. Sale receivables - $250,012,500. $12,500 paid to SPV.

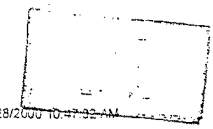
I hope this is of some use. Please call / e-mail if I can clarify anything or provide additional information.
Regards
Gareth Essex-Cater
For Mourant & Co Limited

Mahonia RBC Exic 2006468
S. Aegean RBC Exic 2002616

>>> <Jeffrey.W.Dellapina@chase.com> 28/04/00 15:54:39 >>>

Excellent. While you earlier asked for a $20,000 distribution, we would recommend a full distribution.

Permanent Subcommittee on Investigations
EXHIBIT #185h



"Gareth EssexCater" <Gareth.EssexCater@mourant.com> on 04/28/2000 10:47:32 AM

To: Jeffrey W. Dellapina/CHASE@CHASE
cc:
Subject: Re: Mahonia Limited

Jeff - if OK with you I was just going to check back through our records and intended to give you a call early next week (Monday is a bank holiday here) - all these amounts seem right to me but I wanted to reacquaint with some of the older trades. Let me know if you need to discuss this before then, however.
Thanks
Gareth E-C

>>> <Jeffrey.W.Dellapina@chase.com> 28/04/00 15:22:13 >>>

Additionally we recognize that Stoneville Agean has retained earnings of $59,185.50 related to the Enron '96 transaction.

---------- Forwarded by Jeffrey W. Dellapina/CHASE on 04/28/2000 10:23 AM ----------

Jeffrey W. Dellapina
04/27/2000 12:29 PM

To: gareth.essexcater@mourant.com, ian.james@mourant.com
cc: Michael Sabloff/CHASE@Chase
Subject: Mahonia Limited

We propose to close a number of dormant demand deposit accounts that we had opened in the names of Stoneville Aegean, Mahonia and to support transactions that have subsequently matured. Our recommendation is to close all but two accounts (Mahonia Limited and Mahonia II Limited). To that end, we would like to reconcile with yourselves the profits achieved on the various transactions. Shortly thereafter we recommend that these amounts be disbursed to Mahonia. Below is a schedule of the amounts we recognize.

Let's discuss by phone at your earliest convenience.

Transaction	Date Closed	Profit / Fee

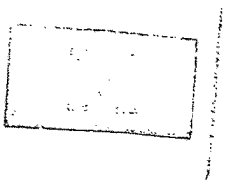
REDACTED

Enron Dec. '96 $12,499.93

REDACTED

Enron Jun. '99 $ 7,013.76

REDACTED



Website: http://www.mourant.com

The information in this email is confidential. The contents may not be disclosed or used by anyone other than the addressee. If you are not the intended recipient, please notify us immediately at the above E-mail address or telephone +44 1534 609000

We cannot accept any responsibility for the accuracy or completeness of this message as it has been transmitted over a public network. If you suspect that the message may have been intercepted or amended, please call the sender.

From: Gareth EssexCater
To: michael.sabloff@chase.com
Date: 09/05/00 15:21:47
Subject: Re: Mahonia Limited

re our telephone conversation concerning trading profits on the various oil and gas deals participated in by Mahonia Limited, Percolin Limited and Stoneville Aegean Limited I have reviewed our archived records to see if I could find any useful information on the earlier trades and in particular anything relating to anticipated trading profits for the SPV's. As we discussed, all the profits achieved on the post November 1998 deals are agreed.
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Given that it seems to me the amount held must be an amount payable to Chase under the oil swaps - do you agree?

DETAILS OF TRADES:

1. December 1992. Enron I. S. Aegean participant. All costs inc SPV profit paid.
2. June 1993. Enron II. S. Aegean / Mahonia participants. All costs paid.
3. September 1993. MG I. S. Aegean and Percolin participants. All costs paid.
4. December 1994. Enron III. Mahonia participant. All costs paid.
5. March 1995. Petrogal. S. Aegean participant. All costs paid. Matching sale and purchase prices.
6. September 1995. Enron IV. Mahonia participant. All costs paid. Deal runs to June 2000.
7. March 1996. MG II deal. Mahonia partipant. All costs paid.
8. December 1996. Enron V. Mahonia participant. Oil and gas acquisition - credit agreement and commodity swap with Chase. No trading profit anticipated. All costs paid.
9. June 1997. Crystal Gas. Mahonia participant. Gas swaps - no price or volume risk for SPV. All costs paid.
10. September 1997. Crystal Properties. Mahonia participant. Oil and gas acquisition - credit agreement and commodity swap with Chase. No anticipated trading profit. All costs paid.
11. December 1997. Enron VI. Mahonia participant. Gas trade. Gas cost - $299,991,678.74. Sale receivables - $300,004,178.74. $12,500 paid to SPV.
12. June 1998. Enron VII. Mahonia participant. Gas trade. Gas cost - $250,000,000. Sale receivables - $250,012,500. $12,500 paid to SPV.

I hope this is of some use. Please call / e-mail if I can clarify anything or provide additional information.
Regards
Gareth Essex-Cater
For Mourant & Co Limited

>>> <Jeffrey.W.Dellapina@chase.com> 28/04/00 15:54:39 >>>

Excellent. While you earlier asked for a $20,000 distribution, we would recommend a full distribution.

"Gareth EssexCater" <Gareth.EssexCater@mourant.com> on 04/28/2000 10:47:32 AM

To: Jeffrey W. Dellapina/CHASE@CHASE
cc:
Subject: Re: Mahonia Limited

Jeff - if OK with you I was just going to check back through our records and intended to give you a call early next week (Monday is a bank holiday here) - all these amounts seem right to me but I wanted to reacquaint with some of the older trades. Let me know if you need to discuss this before then, however.
Thanks
Gareth E-C

>>> <Jeffrey.W.Dellapina@chase.com> 28/04/00 15:22:18 >>>

Additionally we recognize that Stoneville Agean has retained earnings of $59,185.50 related to the Enron '96 transaction.

---------- Forwarded by Jeffrey W. Dellapina/CHASE on 04/28/2000 10:23 AM ----------

Jeffrey W. Dellapina
04/27/2000 12:29 PM

To: gareth.essexcater@mourant.com, ian.james@mourant.com
cc: Michael Sabloff/CHASE@Chase
Subject: Mahonia Limited

We propose to close a number of dormant demand deposit accounts that we had opened in the names of Stoneville Aegean, Mahonia and Percolin to support transactions that have subsequently matured. Our recommendation is to close all but two accounts (Mahonia Limited and Mahonia II Limited). To that end, we would like to reconcile with yourselves the profits achieved on the various transactions. Shortly thereafter we recommend that these amounts be disbursed to Mahonia. Below is a schedule of the amounts we recognize.

Let's discuss by phone at your earliest convenience.

Transaction	Date Closed	Profit / Fee

Occidental	Nov. '98	$20,000.00
Enron	Dec. '98	$12,499.93
Tom Brown	Dec. '98	$ 2,333.33
Enron	Jun. '99	$ 7,013.76
Santa Fe	Aug. '99	$ 5,426.17
Columbia	Dec. '99	$ 5,000.00

Website: http://www.mourant.com

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To: Richard S. Walker/CHASE@CHASE
cc: Robert Traband/CHASE@CHASE, George Sence/CHASE@CHASE
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

Cool - he called yesterday afternoon and I didn't have a chance to engage with him yet.

One note - I had face-to-face with Nick Argirou yesterday and he retested Enron - default swap prices may actually be 10 bps wider than he reported earlier. There appears to be one bank out there which is driving the market higher.

My thoughts:

- Cover entire amount with default swaps for year 1.
- Obtain termination rights (i.e., acceleration of deliveries) if we can't get comfortable with our exposures. Credit will not likely approve today the additonal insurance coverage.
- Pricing remains a huge issue: we'll need substantial compensation for the asset, and more with the future surety coverage. Perhaps we link pricing to the bond spreac in the future.

Let's discuss at your earliest convenience.

Richard S. Walker

Richard S. Walker
11/15/2000 06:44 PM

To: Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, George Sence/CHASE@CHASE
cc:
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

Don't know if you guys have had a chance to do any more brain storming on Joe's $500 MM prepay need. He called this afternoon and clearly he needs this deal.

He suggested the following:

He recognizes the balance sheet pressure we have -- and he has communicated that to Ben Glisan
Given the amount of money that should be coming in off of PGE, Southern Cone, etc in 2001 he thinks that they can give us a pledge that they won't ask for a prepay next.
Recognizing the cost of default swaps right now he propsed the following:

Execute a three year prepay with year one covered by default swaps at today's prices and a covenant by Enron Corp to deliver surety coverage for the balance in one year's time. The thought being that this time next year, we will have had a bunch of run-off that is currently covered by sureties.

Permanent Subcommittee on Investigations
EXHIBIT #185i

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SENATE

I had to cut Joe off because of another call but I think this is a creative way to think -- although if Enron will give us sureties might as well take them now.

A twist on Joe's thought might be

(1) Take the first year's coverage in default swaps
(2) Go ahead and take the sureties now for years two and three
(3) Structure some sort of economic option that would obligate Enron or give Chase the right to replace the sureties for years 2 and three at some later date.

We need to think through #3 to see if it makes any sense.
Jeffrey W. Dellapina

Jeffrey W. Dellapina
11/15/2000 11:39 AM

To: Richard S. Walker/CHASE@CHASE
cc:
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

I'm trying to reach Rob to follow-up.

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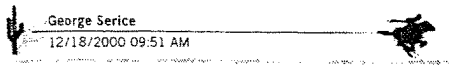

GSF George Serice@Chase.com 713-216-3079 Fax Number 713-216-4583

To Robert Traband/CHASE@CHASE, Jeffrey W. Dellapina/CHASE, Richard S. Walker/CHASE, 9936302@skytel.com
cc Tod Benton/CHASE
Subject Prepay Update #2 12/18

Deffner has agreed to pricing (65 bps upfront and L+87.5 bps). Likely close ~ Dec 27. Chase and Fleet at 2 x 165 = 330. Fleet will seek final approval. FYI, Deffner remarked to McBride that the extra upfront would come out of Chase's arrangement fee.

Treatment
JPMC

Permanent Subcommittee on Investigations
EXHIBIT #185j

SENATE
MAH - 02296

George Serice
09/12/2001 05 40 PM

JP Morgan Global Syndicated Finance, George Serice@JPMChase com 713-216-8079 Fax Number 713-216-4583

To Richard S Walker/CHASE
cc Jeffrey W Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE
Subject Re Enron Prepay

Sure

Richard S. Walker

Richard S Walker
09/12/2001 04 13 PM

To Jeffrey W Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, George Serice/CHASE@CHASE
cc
Subject Enron Prepay

Got a call from Joe Deffner / Lisa Bills inquiring on the status of their prepay request.

I told them that I had my doubts (a) about winning the argument to reconsider our view on the value of sureties and (b) whether or not a surety market even exsits

Joe countered with the first signs of desperation in his voice that he would like us to consider doing something direct with him and then working together to get the risk sold down in a timely fashion We also discussed tenor and clearly they will take any money they can get now even if its on a one year basis

As already discussed with Jeff and Rob, we will call Joe on Thursday at 9am to discuss alternatives. George can you join ? I think your market perspective on Slapshot will be helpful?

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Permanent Subcommittee on Investigations
EXHIBIT #185k

"Bills, Lisa" <Lisa.Bills@ENRON.com> on 09/20/2001 05:03:02 PM

To Jeffrey W Dellapina/CHASE@CHASE
cc "Garberding, Michael" <Michael Garberding@ENRON com>, Robert Traband/CHASE@CHASE
Subject RE Rep Letter for Mahonia

Jeff,

Regarding the Rep Letter Michael sent you below, we have been requested by our auditors to include another representation. It will state (in words not yet crafted, so any you want to propose are welcome) that Mahonia and Chase are unrelated entities which are not consolidated on a legal or accounting basis with each other.

I would appreciate hearing from you while we continue to draft documents that there will be no issues with Mahonia delivering the required Rep Letter. Also, we would appreciate receiving Mahonia's Charter and Articles of Incorporation as we don't have them in our files. We only have Stoneville information from the December 2000 deal.

Thanks, Lisa

> -----Original Message-----
> From: Garberding, Michael
> Sent: Friday, September 14, 2001 8:09 AM
> To: Jeff Dellapina (E-mail)
> Cc: Bills, Lisa; Quaintance Jr., Alan
> Subject: Rep Letter for Mahonia
>
> Jeff --
>
> As discussed yesterday in our call, Arthur Andersen (AA) now requires
> us to have certain reps from the Swap Co.that is utilized within the
> prepay structure. The following attachment is an example of what the
> letter will look like. With regard to the process (as the transaction
> reaches completion), AA will send directly to the Swap Co. a letter
> from Enron that describes the rep confirm process along with an
> example of the rep letter. The Swap Co. will need to return a signed
> rep letter to AA on their own letterhead signed by an authorized
> member of the Swap Co. (that is similar to the example). Please let
> us know if you have any questions with regard to either the letter or
> the process. Thanks for your help.
>
> << File: Rep Letter 9-13-01.doc >>
>
>
> Michael Garberding
> Enron Americas Global Finance
> Work: (713) 853-1864
> Fax: (713) 646-3602
> E-mail: michael.garberding@enron.com
>

****
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****

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M

Wes Colwell
Managing Director

Enron Wholesale Services
1400 Smith Street
Houston, TX 77002-7361

P.O. Box 1188
Houston, TX 77251-1188
713-853-7249
Fax 713-646-8029
wes.colwell@enron.com

September 26, 2001

Mahonia Limited
Attention: Ian James
22 Granville Street
Jersey, Channel Islands JE4 8PX
Fax Number 44-1534-609333

Dear Ian:

Our auditors, Arthur Andersen LLP, are now engaged in an audit of our financial statements. In connection therewith, they desire to confirm the following information about Mahonia Limited (the "Company"):

1. There is no restriction in the corporate documentation of the Company limiting the number of entities with which the Company may conduct business. The Company has undertaken transactions with entities other than Enron Corp and its subsidiaries and affiliates ("Enron");

2. The Company has assets other than those that will be acquired through transactions with Enron; and

3. The Company has unencumbered assets, which are available for application towards obligations owed to its present and future creditors (including Enron).

4. The Chase Manhattan Bank and its consolidated subsidiaries do not own the ownership interests of the Company or consolidate the Company under generally accepted accounting principles.

Please confirm the above statements on your letterhead if you agree with the statements. If not, please furnish any information you may have that explains to the auditors why you don't agree with the above statements. See sample return confirmation attached.

After signing and dating your confirmation, please mail it directly to Arthur Andersen LLP, 711 Louisiana, Suite 1300, Houston, Texas 77002. A stamped, addressed envelope is enclosed for your convenience.

Very truly yours,

Wes Colwell

Wes Colwell
Managing Director

Permanent Subcommittee on Investigations
EXHIBIT #185l-2

Enclosure

Mahonia Limited

PO Box 87
22 Grenville Street
St Helier
Jersey JE4 8PX
Channel Islands

Tel: 01534 609000
Fax: 01534 609333
Telex: 4192064
International
Tel: +44 1534 609000
Fax: +44 1534 609333

Direct Dial 01534 609637
via secretary

Arthur Andersen LLP

28 September 2001

Our ref: 0809/g12/InFin/109264/41218/22268

Dear Sirs

We confirm the following information about Mahonia Limited (the "**Company**"), with the following exceptions (if any):

1. There is no restriction in the corporate documentation of the Company limiting the number of entities with which the Company may conduct business. The Company has undertaken transactions with entities other than Enron Corp and its subsidiaries and affiliates ("**Enron**");

2. The Company has assets other than those that will be acquired through transactions with Enron; and

3. The Company has unencumbered assets, which are available for application towards obligations owed to its present and future creditors (including Enron).

4. The Chase Manhattan Bank and its consolidated subsidiaries do not own the ownership interests of the Company.

Yours faithfully,
For and on behalf of
Mahonia Limited

Ian James
Director

Permanent Subcommittee on Investigations
EXHIBIT #185l-3

1007

Mahonia Limited

PO Box 87
22 Grenville Street
St Helier
Jersey JE4 8PX
Channel Islands

Tel: 01534 609000
Fax: 01534 609333
Telex: 4192064
International
Tel: +44 1534 609000
Fax: +44 1534 609333

Direct Dial 01534 609637
via secretary

The Chase Manhattan Bank
270 Park Avenue
New York
NY 1007
USA

28 September 2001

Our ref: 0809/g12/InFin/108907/41218/22268

Dear Sirs

We have entered into or propose to enter into a prepaid commodity price swap transaction (the "**Swap Transaction**") with Enron North America Corp. ("**ENAC**") pursuant to which we will have a Irrevocable, Transferable Standby Letter of Credit issued in our favour (the "**Letter of Credit**"). Under the Swap Transaction we are required to receive payments and receive or transfer cash and securities pursuant to the terms of a Credit Support Annex.

We hereby appoint you as our agent to:

(a) monitor and arrange for the receipt of such payments and the receipt and transfer of such cash and securities;

(b) act for and on our behalf in connection with any instrument furnished by or on behalf of ENAC in connection with the Swap Transaction and the Letter of Credit, including, without limitation, drawing under the Letter of Credit on our behalf; and

(c) generally to perform such other functions as are reasonably incidental to the above.

We confirm that for these purposes you shall be entitled to appoint an agent or agents in order to enable you to perform your role as our agent in accordance with the terms of this letter.

Your duties shall be performed subject to the overall direction of the Directors of this Company and in accordance with their instructions.

We confirm that, in the absence of gross negligence or willful default on your part, we shall have no claim against you in respect of any failure by you to perform or properly to perform any of the duties set out above.

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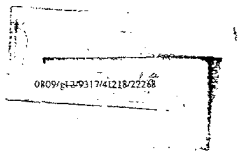
Permanent Subcommittee on Investigations
EXHIBIT #185m



We may terminate your appointment at any time upon serving written notice upon you, such notice to become effective only when received by you, but such a termination shall be without prejudice to any rights or claims which you may have against us as of the date such notice becomes effective.

You may resign from your position as our agent any time upon serving written notice upon us.

This letter shall be governed by English law.

Yours faithfully,
For an on behalf of
Mabonia Limited

Director

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"Julie Carter" <Julie.Carter@mourant.com> on 10/26/2001 07:34:17 AM

To: Philip Levy/CHASE@CHASE
cc: Jeffrey W. Dellapina/CHASE@CHASE, "Gareth EssexCater" <Gareth.EssexCater@mourant.com>
Subject: Fwd: Enron Swap Transaction

Phil

I refer you to my e-mail dated 12 October 2001 which is attached and should be grateful if you would revert with your comments as soon as possible.

I also refer you to my e-mail dated 20 September 2001, a copy of which is also attached, and advise that I am still waiting to hear from you in respect of the draft accounts prepared to 31 March 2000 (the level of commission having now been decided).

Kind regards

Yours sincerely
For and one behalf of
Mourant & Co. Secretaries Limited

Julie Carter

Website: http://www.mourant.com

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If this message includes attachments, please ensure they are opened within the relevant application to ensure full receipt.
If you experience difficulties, please refer back to the sender.
Content-Transfer-Encoding: quoted-printable
Date: Fri, 12 Oct 2001 11:30:23 +0100
From: "Julie Carter" <Julie.Carter@mourant.com>
To: <Philip.Levy@chase.com>
Cc: <Jeffrey.W.Dellapina@chase.com>,<Michael.Sabloff@chase.com>, "Gareth EssexCater" <Gareth.EssexCater@mourant.com>
Subject: Enron Swap Transaction
Mime-Version: 1.0
Content-Type: text/plain; charset="us-ascii"
Content-Disposition: inline

Phil

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Permanent Subcommittee on Investigations
EXHIBIT #185n

Further to the execution of documentation relating to the Enron Swap transaction on 28 September 2001 we have the following comments:

1) We have not as yet received completed versions of any of the documentation that was signed ie signature pages and versions of the documents such as the Security Agreement with the 'blanks' filled in. Can you please forward these for our files as soon as possible.

2) We have assumed that the Chase - Mahonia side of the swap is effected under the pre-existing Master Agreement - the security agreement refers (under the definition of 'Transaction') to a 'prepaid commodity price transaction' between the company and Chase. Has this or will this be reflected in a confirmation or similar advice?

3) Will we need to 'sign over' the Letters of Credit to Chase under the provisions of the Security Agreement?

4) We are slightly confused by the credit annex as it seems to suggest that Letter of Credit cover will be at '100% '. The fixed swap payment to Enron from the company is $350 million and the two Letters of Credit received by us have a maximum value of $315 million. Can we please have your comments.
I
look forward to hearing from you in respect of the above as soon as possible.

Kind regards

Yours sincerely
For and on behalf of
Mourant & Co. Secretaries Limited

Julie Carter

>>> <Philip.Levy@chase.com> 24 September 2001 >>>
Julie-

Following is a communication from Enron with respect to a new transaction that they would like to close this week. Unlike the prior prepay transactions which resulted in physical delivery of natural gas, this transaction will be documented as a cash-settled prepaid swap under ISDA documentation. Under this scenario, Mahonia will make an upfront payment (much like in the standard prepay) but, instead of receiving specified quantities of natural gas over time, Enron will pay cash to Mahonia (which will, in turn, make payment to Chase under a swap transaction with Chase, which transaction will also put Mahonia in funds to make its payment to Enron.)

I am in the process of reviewing the enclosed documents and will provide comments on Mahonia's behalf to Enron. I believe that all the ancillary documentation between Mahonia and Enron typically provided in the physical prepay transactions will be necessary here as well (Board resolutions, minutes, legal opinions, etc.).

I also want to apologize for the delay in resolving the account issues you have raised. It is my understanding that Jeff and Mike are following up on the matter and will respond to you shortly. It is my further understanding that the back office is retrieving the Crystal confirms you requested and

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REQUESTED BY JPMC

will forward them shortly.

Please feel free to contact me should you have any questions. Thank you for your patience and cooperation.

Phil

---------- Forwarded by Philip Levy/CHASE on 09/24/2001 10:07 AM ----------

"Koehler, Anne C." <Anne.C.Koehler@ENRON.com> on 09/23/2001 07:20:08 PM

To: Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, Philip Levy/CHASE@CHASE
cc: "Garberding, Michael" <Michael.Garberding@ENRON.com>, "Bills, Lisa" <Lisa.Bills@ENRON.com>, "Moon, Eric" <Eric.Moon@ENRON.com>, "Boyt, Eric" <Eric.Boyt@ENRON.com>, "Quaintance Jr., Alan" <Alan.Quaintance.Jr@ENRON.com>, "Clark, Catherine" <Catherine.Clark@ENRON.com>, "Blumenthal, Jeff" <Jeff.Blumenthal@ENRON.com>
Subject: RE: Prepay Docs

Attached hereto are first drafts of the form of swap documents we propose to use in connection with the prepay transaction with Chase and Mahonia. Since we do not have a Master ISDA in place with Mahonia, I have drafted the ENA/Mahonia confirmation in the form of a "deemed ISDA".

You will note that the business terms of the swaps as well as the calculation of collateral posting amounts have been left blank. These will be filled in as soon as the parties have agreed to them.

Please be advised that none of the members of the business team at Enron have had a chance to review the form of documents attached hereto. Therefore the documents remain subject to further change based on their input.

If you have any questions or comments, please contact me at your earliest convenience.

<<ChaseENAswapv2.doc>> <<MahoniaENAswapv2.doc>>

-----Original Message-----
From: Bills, Lisa
Sent: Friday, September 21, 2001 7:57 PM
To: 'jeffrey.w.dellapina@chase.com'; 'robert.traband@chase.com'; 'philip.levy@chase.com'
Cc: Koehler, Anne C.; Garberding, Michael
Subject: Prepay Docs

Gentlemen,

As my voicemail to Rob this evening indicated, we will

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be sending the documents for your review on Sunday afternoon. They will not have the transaction specifics (pricing etc) as our model is being finalized now that we received your approval. I also want to speak with Jeff on Monday about it. However, there is enough boilerplate to review and comment on as necessary in the interim.

The plan is to have documents at least 90% finalized by end of day on Tuesday; have a dry run on Wed so we have time to adjust calculations, etc.; close and fund on Thursday.

We look forward to successfully executing another transaction with Chase.

If you need to reach me this weekend you may leave me a message at work - 713 853 1703; or at home - 713 426 5705.

Regards, Lisa

PS. It would be very helpful to receive the requested Mahonia information and signoff on Monday or at least let us know that it is all ok and will be delivered on time.

****
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****

(See attached file: ChaseENAswapv2.doc)
(See attached file: MahoniaENAswapv2.doc)
Date: Thu, 20 Sep 2001 12:12:11 +0100
From: "Julie Carter" <Julie.Carter@mourant.com>
To: <Philip.Levy@chase.com>
Cc: "Jeffrey Dellapina (E-mail)" <Jeffrey.W.Dellapina@chase.com>, <Michael.Sabloff@chase.com>
Subject: Fwd: Mahonia Limited - Accounts & Mahonia Natural Gas Limited
Mime-Version: 1.0
Content-Type: multipart/mixed; boundary="=_94CE7B54.8EEF99CB"

Dear Phil

I refer to recent e-mails (attached) and should be grateful to receive your comments on the draft accounts for the period to 31 March 2000 for Mahonia Limited. I should also be grateful to receive the necessary accounting information ie the total value of receipts\payments in respect of the Crystal 9/97 deal together with confirmation that the deal terminated in December 1998.

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In addition I should be grateful if you would advise what level of commission Mahonia Natural Gas Limited earned in connection with the natural gas deal with Enron and when we can expect to receive those funds.

Kind regards

Yours sincerely
For and on behalf of
Mourant & Co. Secretaries Limited

Julie Carter
Date: Tue, 04 Sep 2001 14:43:22 +0100
From: "Julie Carter" <Julie.Carter@mourant.com>
To: "Jeffrey Dellapina (E-mail)" <Jeffrey.W.Dellapina@chase.com>,
<Philip.Levy@chase.com>
Cc: <Michael.Sabloff@chase.com>
Subject: Mahonia Limited - Accounts
Mime-Version: 1.0
Content-Type: multipart/mixed; boundary="=_94CE7B54.89E89ECC"

Dear Jeff & Phil

I refer to you to the attached e-mail which was sent some time ago to Mike Sabloff which attaches draft accounts for the period to 31 March 2000 for Mahonia Limited.

Since then I have been chasing you on a regular basis to obtain your comments on the draft accounts and also the necessary accounting information ie the total value of receipts\payments in respect of the Crystal 9/97 deal together with confirmation that the deal terminated in December 1998.

As yet I have not heard anything from you.

By not finalising these accounts we are effectively contravening the Companies (Jersey) Law 1991 which states that accounts for private companies should be laid before the shareholders within 10 months of the year end.

Accordingly I should be grateful to receive your comments by return. As soon as your comments are received I will finalise the accounts to 31 March 2000 for Mahonia Limited and will then be in a position to prepare accounts to 31.12.2000 for both Mahonia Limited and Mahonia II Limited.

Kind regards

Yours sincerely
For and on behalf of
Mourant & Co. Secretaries Limited

Julie Carter
Date: Fri, 18 May 2001 17:14:21 +0100
From: "Julie Carter" <Julie.Carter@mourant.com>
To: <Michael.Sabloff@chase.com>
Cc: <Jeffrey.W.Dellapina@chase.com>,<Philip.Levy@chase.com>, "Gareth EssexCater" <Gareth.EssexCater@mourant.com>
Subject: Re: Mahonia Limited
Mime-Version: 1.0
Content-Type: multipart/mixed; boundary="=_94CE7B54.88E99FCD"

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Mike

Thank you for your e-mail of 11 December 2000. Please accept my apologies for the delay in getting back to you.

I have noted your comments and have adjusted the draft accounts as follows and attach a revised draft copy for your comments. I have

1. removed reference to futures transactions in the accounts
2. included the second Sante Fe transaction figures
3. ensured that no Coastal transaction figures are included
4. noted safe receipt of the $500 commission due regarding the Enron 6/99 transaction and have ensured that it is included this in the transaction fees receivable
5. removed reference to any costs payable in connection with Surety Bond maintenance

These accounts do not however included any figures in respect the Crystal 9/97 deal which terminated in December 1998 according to our records. I should be grateful to receive Jeff's confirmation in this respect and the necessary accounting information (total value of receipts\payments) as mentioned in your e-mail.

As soon as I receive the comments from Jeff and your approval of these drafts I will arrange for them to be finalised.

Going forward I would appreciate receiving the Prepay Masters for both Mahonia Limited and Mahonia II Limited as at 31 December 2000 in order that I may prepare management accounts to that date thereby bringing both companies back in line with their year end.

Kind regards

Yours sincerely
For and on behalf of
Mourant & Co. Secretaries Limited

Julie Carter

>>> <Michael.Sabloff@chase.com> 11 December 2000 >>>

Re: your e mail of 12/6/00, I will try to answer what I can and will have to defer to Jeff for the remainder. (He is out of the office today.)

Yes, the Enron '95 transaction was the last one hedged with futures. The last of the futures positions was closed in May '99. Since then, Mahonia has not had any futures positions.

The Santa Fe transaction in January '00 was an amendment to the original transaction done in August '99, not a completely new transaction. On my schedule you would need to add the two amounts together to come up with the total outstanding.

The Coastal transaction of June '99 was not done through Mahonia and should not have been included on the schedule I sent (my mistake).

Our records for the Enron 6/99 Natural Gas forward sale show that the

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profit margin due to Mahonia was $7,513.76.
I will contact our Operations to transfer $500 to Mahonia. The 1998 date was a typo on the Enron Confirmation

Regarding the Surety Bonds, there should be no charges attributable to Mahonia.

I will have Jeff get back to you concerning the details on the Crystal transaction as I don't have a copy of the termination.

I hope this clears up most of the questions.

Regards,

Mike Sabloff

- Accounts-31.3.2000.xls

FOIA CONFIDENTIAL TREATMENT
REQUESTED BY JPMC

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

JPMORGAN CHASE BANK, for itself and for and on behalf of Mahonia Limited and Mahonia Natural Gas Limited,

Plaintiff,

-against-

LIBERTY MUTUAL INSURANCE COMPANY, TRAVELERS CASUALTY & SURETY COMPANY, ST. PAUL FIRE AND MARINE INSURANCE COMPANY, CONTINENTAL CASUALTY COMPANY, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, FIREMAN'S FUND INSURANCE COMPANY, SAFECO INSURANCE COMPANY OF AMERICA, THE TRAVELERS INDEMNITY COMPANY, FEDERAL INSURANCE COMPANY, HARTFORD FIRE INSURANCE COMPANY, and LUMBERMENS MUTUAL CASUALTY COMPANY,

Defendants.

01 Civ. 11523 (JSR)

AMENDED COMPLAINT

John M. Callagy, Esq.
William A. Escobar, Esq.
Steven P. Caley, Esq.
Neil N. Merkl, Esq.
KELLEY DRYE & WARREN LLP
101 Park Avenue
New York, New York 10178
(212) 808-7800
Attorneys for Plaintiff JPMorgan Chase Bank, for itself, and for and on behalf of Mahonia Limited and Mahonia Natural Gas Limited

Permanent Subcommittee on Investigations
EXHIBIT #185o

TABLE OF CONTENTS

INTRODUCTION 1

THE PARTIES 14

SIGNIFICANT OTHER ENTITIES 16

JURISDICTION AND VENUE 18

FIRST CLAIM - FRAUD AGAINST LIBERTY AND TRAVELERS 18

The Initial Enron Prepaid Forward Transactions Secured by Performance Letters of Credit 19

In the Midst of A Slump In Business, Surety Companies Seek To Expand Their Business By Competing With Banks 21

SECOND CLAIM – FRAUD AGAINST LIBERTY, TRAVELERS, ST. PAUL, CNA AND FIREMAN'S FUND 28

THIRD CLAIM – FRAUD AGAINST TRAVELERS, SAFECO, ST. PAUL, CNA, AND FIREMAN'S FUND 33

FOURTH CLAIM – FRAUD AGAINST FEDERAL, TRAVELERS, ST. PAUL, CNA AND FIREMAN'S FUND 38

FIFTH CLAIM – FRAUD AGAINST FEDERAL, TRAVELERS, LUMBERMENS, AND FIREMAN's FUND 43

SIXTH CLAIM – FRAUD AGAINST TRAVELERS, ST. PAUL, LUMBERMENS, HARTFORD AND SAFECO 47

SEVENTH CLAIM FOR RELIEF BY JPMORGAN CHASE, FOR AND ON BEHALF OF MAHONIA, AGAINST ALL DEFENDANTS FOR BREACH OF CONTRACT 52

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

JPMORGAN CHASE BANK, for itself and for and on behalf of Mahonia Limited and Mahonia Natural Gas Limited,

Plaintiff,

-against-

LIBERTY MUTUAL INSURANCE COMPANY, TRAVELERS CASUALTY & SURETY COMPANY, ST. PAUL FIRE AND MARINE INSURANCE COMPANY, CONTINENTAL CASUALTY COMPANY, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, FIREMAN'S FUND INSURANCE COMPANY, SAFECO INSURANCE COMPANY OF AMERICA, THE TRAVELERS INDEMNITY COMPANY, FEDERAL INSURANCE COMPANY, HARTFORD FIRE INSURANCE COMPANY, and LUMBERMENS MUTUAL CASUALTY COMPANY,

Defendants.

01 Civ. 11523 (JSR)

AMENDED COMPLAINT

Plaintiff JPMorgan Chase Bank ("JPMorgan Chase") for itself, and for and on behalf of Mahonia Limited and Mahonia Natural Gas Limited, by its attorneys Kelley Drye & Warren LLP, for its Amended Complaint alleges as follows:

INTRODUCTION

1. JPMorgan Chase commenced this action for and on behalf of Mahonia Limited and Mahonia Natural Gas Limited ("Mahonia") on December 11, 2001. The original complaint sought declaratory relief because the defendants stated that they would not comply with their obligations to Mahonia, the contractual obligee of the disputed surety bonds.

2. In this Amended Complaint, Mahonia asserts a breach of contract claim because defendants failed to make payment as required by the surety bonds. In addition to Mahonia's breach of contract claim, JPMorgan Chase asserts independent claims against the defendants

based on their failure to disclose certain facts known to defendants at the time they issued the surety bonds, which facts defendants knew JPMorgan Chase did not know and which they knew, if disclosed, would have caused JPMorgan Chase to refuse to accept the defendants' surety bonds as security for transactions with Enron Corp. and its subsidiaries ("Enron").

3. JPMorgan Chase's fraud claims arise from a scheme by the defendant insurance companies to generate premium revenue by inducing JPMorgan Chase to accept surety bonds issued by the defendants in the place of letters of credit to secure more than $1 billion in funding advanced by JPMorgan Chase for the purchase of natural gas and crude oil from subsidiaries of Enron.

4. Confronted with a protracted soft market for traditional surety bonds, and anxious to generate premiums, each of the defendants decided in the mid- to late- 1990s to aggressively market commercial surety bonds as an alternative to bank-issued letters of credit for use in structured financing transactions.

5. Upon information and belief, they viewed the opportunity as lucrative, given the creditworthiness of potential customers such as Enron.

6. Upon information and belief, defendants calculated that their existing customer base, many of whom engaged in structured financing transactions utilizing letters of credit issued by banks, would be receptive to what defendants represented were the alternative benefits of surety bonds. As an example, the Surety Association of America, a non-profit association which provides ratings of its member surety companies, advises them and collects statistical information, described some of these purported benefits in marketing materials designed to publicly promote the benefits of surety bonds over letters of credit. For example, the marketing material states:

Letters of Credit ("LOC")	Surety Bonds
Use of LOC diminishes borrowing capacity of entity	No such impact. Unused borrowing capacity can be viewed as an off-balance sheet strength.
LOC's are usually reflected on borrowers financial statements as a contingent liability	No such impact. Surety bonds are not recognized as a contingent liability.

7. The defendants were interested in selling surety bonds as credit support for transactions involving energy companies, which engaged in prepaid forward sale transactions including oil and gas deliveries as a source of corporate finance.

8. Since the early 1990s, JPMorgan Chase had been providing financing to clients in the energy industry in the form of prepaid forward transactions. Generally, under the terms of a prepaid forward transaction, JPMorgan Chase would make advance payment to a special purpose entity for the benefit of its customer, and the customer would promise to deliver oil or gas in the future.

9. Under the terms of the transactions, JPMorgan Chase's customers would be required to pay a termination payment (akin to an acceleration clause) if an event of a default occurred under the commodity sale contract. To secure the termination payment, JPMorgan Chase required the customer, in the instant case Enron, to post a letter of credit which could be drawn upon in the event the customer failed to pay the termination payment.

10. Beginning in 1998, JPMorgan Chase was asked to accept surety bonds written by the defendants in place of letters of credit.

11. In marketing the bonds in this case, the defendants were required to demonstrate and give assurance to JPMorgan Chase that the bonds they would issue would be the functional equivalent of letters of credit and, like letters of credit, would constitute absolute and

unconditional pay-on-demand financial guarantees, and that the bonds would be valid, binding and enforceable obligations of the insurance companies.

12. But it is now clear that, while the defendants were successful in persuading JPMorgan Chase to relinquish the use of letters of credit in their transactions, the defendants failed to disclose to JPMorgan Chase information which, if disclosed, they knew would have caused JPMorgan Chase not to accept the surety bonds in the first place.

13. Defendants' submission in opposition to plaintiff's Motion for Summary Judgment on the original Complaint, in which they claim that they never knew that their bonds were components of structured financing transactions, is a starting point for understanding the defendants' concealments.

14. In response to JPMorgan Chase's motion for summary judgment, defendants raised a series of alleged defenses premised on the claim that "In the wake of Enron's collapse, the defendants learned that the [Advance Payment Supply Surety Bonds] are apparently one leg of a complicated (and undisclosed) loan from [JPMorgan] Chase to Enron via Mahonia, a Jersey Island corporation which [JPMorgan] Chase controls." (See Defendants' Memorandum of Law in Opposition to Plaintiff Motion for Summary Judgment, dated February 11, 2002, (hereinafter "Defendants' Opposition Memo") at 1).

15. The defendants claim that only after the collapse of Enron, "the Sureties have been able to gather evidence indicating that the [Advance Payment Supply Surety Bonds] were designed to camouflage loans by [JPMorgan] Chase to Enron, and that [JPMorgan] Chase defrauded the Sureties into guaranteeing obligations which they otherwise would not, and statutorily could not, have bonded." (Id. at 2).

16. More specifically, the defendants maintained that only after Enron's collapse did they learn that the gas and oil purchased by Mahonia was to be sold to JPMorgan Chase in return for JPMorgan Chase advancing the funds necessary for Mahonia to make the prepayment to Enron. They argued that "such an arrangement is highly unusual in connection with a bona fide forward sale contract. It is more readily understood in the context of a commercial loan transaction." (Id. at 12).

17. Accordingly, defendants would not pay because of information that JPMorgan Chase allegedly concealed from them.

18. In fact, nothing about the transactions was disguised. It is demonstrable that long before Enron failed, and indeed before one or more of the surety bonds at issue were written, the defendants, and their agent Wortham, knew that the deals were part of a structured financing transaction for Enron's general corporate benefit.

19. The documentary record to date reflects that at various times before Enron collapsed and the bonds were called, and before one or more of the surety bonds were written, one or more of the defendants, and/or their agent through whom each of them acted, formed a belief that:

- The surety bonds were part of financing transactions in which the funds advanced by JPMorgan Chase to Mahonia were ultimately used by Enron for general corporate purposes, not to secure future sources of the oil and gas to be delivered. (See Exhibits A and B attached).
- The surety bonds were being used by Enron as a central piece of overall financial deal structures, in which surety bonds bear the risk of Enron's credit. (See Exhibits A and B attached).

FROM CHASE LEGAL (WED) 7. 3'02 17:06/ST. 17:04/NO. 4800925589 P 7

- Advance Payment Supply Bonds could be regarded as bank loan guarantees. (See Exhibit C attached).
- Mahonia was a special purpose entity used by JPMorgan Chase in financing transactions; that the use of Mahonia, *inter alia*, provided favorable tax treatment for Enron; and that Mahonia was to sell the underlying product to JPMorgan Chase which would trade it off through JPMorgan Chase's trading department. (See Exhibit D attached).
- JPMorgan Chase provided the cash for Mahonia to use in the transactions. (See Exhibits E and F attached).

20. Thus, the record to date strips away the alleged factual underpinning of defendants' claim that the defendants learned about the nature of what they bonded after Enron collapsed.

21. In June 1998, in the first transaction to substitute a surety bond for a letter of credit, Liberty Mutual Insurance Company ("Liberty") represented that it was authorized to write pay-on-demand instruments just as a bank was authorized to issue letters of credit. Moreover, JPMorgan Chase required Liberty to provide, *inter alia*, a corporate legal opinion on which the bank could rely that the bonds were valid, enforceable and binding.

22. Liberty provided an unequivocal legal opinion in order to obtain the first transaction, and the promise of more transactions to come.

23. JPMorgan Chase relied on this legal opinion.

24. Liberty gave the opinion to JPMorgan Chase but did not disclose the fact that its outside counsel (now a member of the law firm representing Federal in this action), confidentially had opined to Liberty as follows:

FROM CHASE LEGAL (WED) 7. 3'02 17:06/ST. 17:04/NO. 4860925589 P 8

> The bond issued by Liberty Mutual appears to be a surety bond and not financial guaranty insurance. The Surety Bond 'guarantees' both the performance and payment obligation under the underlying Agreement, however it is possible that the New York Insurance Department may determine that the Surety Bond is [prohibited] financial guaranty insurance.

Liberty transmitted that opinion to John L. Wortham & Son L.L.P. ("Wortham"), the agent for all the defendants in all of the transactions, and, upon information and belief, to one or more of the other defendants.

25. Liberty did not disclose its belief that its authority to write the bonds was in doubt.

26. Thus, from time to time Liberty had been advised that the proposed bonds would or could be viewed from a regulatory standpoint as a type of prohibited insurance under New York Insurance Law subjecting Liberty to fines and licensing issues.

27. JPMorgan Chase had previously consummated prior to June 1998 several transactions with Enron relying on the absolute and unconditional payment obligation of letters of credit and could have continued to rely on letters of credit in future transactions for its security.

28. If Liberty had failed to furnish an unequivocal legal opinion to JPMorgan Chase, or had disclosed that the bond would or could be viewed as "crossing the line" toward a form of prohibited insurance that Liberty was not authorized to write, Liberty knew that JPMorgan Chase would not have accepted the bond.

29. In each of the subsequent transactions from September 1998 through December 2000, the other defendants were also required to provide an opinion of counsel which also was specifically extended to, and provided for the benefit of, JPMorgan Chase. Those legal opinions

FROM CHASE LEGAL (WED) 7. 3'02 17:06/ST. 17:04/NO. 4800925589 P 9

asserted that the surety bonds were, and at all times continued to be, valid, binding and enforceable against the respective defendants, according to their terms.

30. Each of the defendants was well aware that these legal opinions were an integral part of the respective transactions. Again, each of the defendants knew that if the defendants gave anything but unequivocal opinion letters reflecting the validity, legality or enforceability of the surety bonds and the terms thereof, JPMorgan Chase would not have accepted the surety bonds in lieu of letters of credit.

31. After JPMorgan Chase made a demand for payment on December 7, 2001, the defendants resisted paying on their obligation on the grounds that, *inter alia*, the bonds constituted a form of prohibited insurance, and argued that the bonds therefore were not valid, not binding and not enforceable. Thus, the very issue that was hidden from JPMorgan Chase at the outset became the purported basis for the defendants' refusal to pay.

32. The record now reflects that, at all times defendants had been advised that, and/or believed that, there were issues of illegality concerning their authorization to issue the bonds, which advice and belief they failed to disclose to JPMorgan Chase.

33. The record also reflects that the fraud continues. Despite defendants' present assertion that issues of illegality have impaired the enforceability of the bonds, at all times defendants have also known that any failure on their part to satisfy insurance regulations did not prejudice in any way the enforceability of the bonds or the plaintiff's ability to enforce the bonds.

34. The defendants have also asserted, by way of defense, that after the December 7, 2001 demand to pay, JPMorgan Chase "stonewalled" them by not cooperating with defendants in their alleged investigation of the claim. They justified their inquiry as an effort " ... to consider

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FROM CHASE LEGAL

whether they should attempt to fulfill Enron's delivery obligations under the Contracts." (See Defendants' Opposition Memo at 7). They asserted a purported right to perform contractual obligations under the gas delivery contracts as if they were dealing with contract performance bonds which purported to guarantee performance of the underlying contracts, rather than make a cash payment.

35. Beyond the clear import of the language agreed to, the documentary record makes it clear that the defendants understood from the outset that, if called upon to satisfy the bonds, their only option was to pay, and to pay within 10 days.

36. Thus, one or more of the defendants, and/or their agent through whom they acted:

- Acknowledged that the bonds replaced letters of credit with a pay on demand bond form allowing no defenses. (See Exhibit G attached).
- Knew that the bonds were substitutes for bank letters of credit to secure bank lines and to enhance credit. (See Exhibit H attached).
- Knew that payment was the only remedy under the bond. (See Exhibit I attached).
- In short, the defendants knew that they had no way out. (See Exhibit J attached).

37. It was clear that the common practice of the insurance industry of accepting premiums and then vigorously litigating with the insured over coverage was not to be available.

38. However, it is now clear that if the bonds were called upon, defendants did not intend to pay on demand. Rather, defendants intended to pursue a "claims adjustment" process as if the bonds were contract performance bonds - but never disclosed that intent to JPMorgan Chase and misrepresented to JPMorgan Chase that the bonds would be paid on demand.

39. In fact, when Enron collapsed and JPMorgan Chase delivered the demands for payment, the defendants refused to pay, and proceeded to pursue "claims adjustment." For example, counsel for Travelers Casualty & Surety Company wrote to JPMorgan Chase counsel:

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> It is imperative that we understand fully and as quickly as possible the status and circumstances surrounding the Forward Sales Contracts, and certainly require the necessary information no later than December 11, 2001. To the extent that we do not receive the requested information from you on an immediate and timely basis, Travelers may be required to take legal action. Travelers reserves all of its rights in this matter. Nothing in this letter should be construed as an admission of liability, and any such construction is expressly disclaimed.

(See Defendants' Affidavits in Opposition to Plaintiff's Motion for Summary Judgment and in Support of Defendants' Request for Discovery Pursuant to Rule 56(f), Volume I, Exhibit 5, A, dated February 3, 2002, at 3).

40. In response to JPMorgan Chase's motion for summary judgment, the defendants admitted that they never intended to pay on demand.

41. The defendants insisted that they could choose to perform Enron's delivery obligations.

42. For example, Liberty's Norleen Davies swears to her intention at the time she underwrote the bonds:

> ...it was very important to me that, in the event of a default by [Enron], Liberty be in a position to offer to Mahonia performance of the underlying delivery obligations as a means to limit Liberty's potential losses.
>
> * * *
>
> ...I specifically negotiated into the June 28, 1998 Bond an increase from three (3) to ten (10) days the period after receipt by Liberty of a default notice that triggered Liberty's obligation to pay under the bond. As I explained to representatives of Enron during the negotiations, Liberty wanted the additional time to allow it to perform the underlying obligations, if it were able to do so.

Id., Volume I, Exhibit 6, dated February 7, 2002, at ¶¶ 11-12).

43. Travelers' Paul Wicks also reflected his intent:

FROM CHASE LEGAL (WED) 7. 3'02 17:07/ST. 17:04/NO. 4800925259 P 12

> Among other things, I wanted information relating to the contracts Enron had signed with producers to supply the gas and oil it was supposed to deliver to Mahonia (the "Producer Agreements") and the contracts Mahonia had signed with end-users (the "End-User Agreements") to resell the gas and oil it was buying from Enron. I wanted to communicate with the producers, Mahonia and the end-users in order for Travelers to work out an arrangement whereby, if an Enron entity was about to default (or defaulted), Travelers would step into Enron's shoes, pay the producers or possibly finance Enron and keep the gas and oil flowing to Mahonia and on the end-users. As I explained above, this would allow Travelers to spread its payment over the life of the underlying agreements, instead of having to make one lump-sum payment to Mahonia; it would also allow Travelers to take advantage of any lower price of the commodity in Enron's contracts with its suppliers.

(Id., Volume II, Exhibit 6, dated February 8, 2002, at ¶ 20). Indeed, Mr. Wicks ignored the clear language of the bonds, and his own internal records which reflect a thorough understanding of Travelers' obligation to pay on demand.

44. Fireman's Fund's Carolyn Abbott swore to her state of mind:

> If Enron defaulted, and Mahonia still needed the natural gas it had already paid for, Fireman's Fund might have been able to mitigate the claim by attempting to step into the shoes of Enron and arranging for the continued supply of natural gas to Mahonia. Fireman's Fund might have considered making payments under the contract with some other producer in order to deliver natural gas to Mahonia. Such an arrangement in mitigation would be preferable to making one lump sum payment under the bond.

(Id., Volume I, Exhibit 1, dated January 30, 2002, at ¶ 18).

45. St. Paul's Karen M. Eichten swore to her intent:

> If Enron defaulted, and Mahonia still needed the gas it had already paid for, St. Paul might have been able to engage in "claim mitigation," by stepping into Enron's shoes and arranging the continued supply of gas to Mahonia. For example, if Enron had a long term supply contract with a producer to obtain the gas it needed to satisfy its obligations to Mahonia, and had prepaid the producer for that gas, St. Paul could attempt to assume Enron's end of that contract. If Enron's contract with its producer did not involve a pre-payment, but the price of the gas under the contract was lower than the market price of gas at the time of Enron's

FROM CHASE LEGAL (WED) 7. 3'02 17:07/ST. 17:04/NO. 4860925589 P 13

> default, St. Paul might consider making payments under the contract with the producer in order to deliver gas to Mahonia. This arrangement would be preferable to making one lump-sum payment under the bond.

(Id., Volume I, Exhibit 9, dated February 7, 2002, at ¶ 8).

46. Safeco's Ronald F. Goetsch swore to Safeco's internal views of the bonds:

> During my conversation with Mr. Deffner [of Enron], I asked about any transactions that might relate to the forward sales contracts that the Bonds secured. My purpose in asking these questions was to determine whether, in the event Safeco was required to pay claims against its Bonds, there existed any contract rights held by Mahonia Limited and Mahonia Natural Gas Limited (collectively "Mahonia"), the obligees, or held by Enron, the principal, that Safeco as the surety could "step into" or assert to salvage or mitigate any future loss. A surety is subrogated to the rights of its obligee and of its principal upon payment of a loss. Moreover, a surety CNA discharge its obligations under a bond by arranging performance of the underlying obligations. In investigating surety claims, therefore, it is typical for a surety to inquire about the prospects for salvage and mitigation before the surety has reached a decision about the validity or merits of the claim or claims.

(Id., Volume I, Exhibit 11, dated January 18, 2002, at ¶ 7).

47. Thus, at the time the defendants issued the surety bonds and made the representations to JPMorgan Chase to induce it to accept the surety bonds in lieu of letters of credit, they intended that: (i) if a claim was made under the surety bonds by Mahonia, they would treat the surety bonds as if they permitted claim adjustments, rather than a payment on demand; (ii) they would not accept JPMorgan Chase's notice to pay Mahonia as they represented they would; and (iii) notwithstanding the explicit terms of the surety bonds, they would proceed as if the surety bonds were not the functional equivalent of letters of credit.

48. Within 60 days of participating in the first two bond transactions totaling approximately $500 million, Liberty quietly exited the business, declining to participate in

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another advance payment supply surety bond. Liberty shared with Wortham, the agent for all of the other sureties, the reason for Liberty's skittishness:

> My explanation [to Wortham] for our inability to go forward with the particular bond [a new deal that became the December 1999 transaction] request included the following:
>
> LBS' increasing awareness and scrutiny of ALL large financial guarantee type transactions born of "irregular" underwriting issues, including but not limited to:
>
> * * * *
>
> objectionably worded attorney opinion letters, and possible Appleton law violations. [1]

(See Exhibit K attached).

49. Indeed, Liberty recognized that it had taken a risk in writing these bonds and in issuing opinion letters that the bonds were valid, binding and enforceable instruments. (See Exhibits L and M attached).

50. So, while Liberty slipped away, the trap was set. The deal structure had been put in place, documentation had been agreed to – including the pay-on-demand feature and the legal opinions – and JPMorgan Chase had been successfully induced to believe that it had the security in place it negotiated to call upon if necessary. In fact, as the clock ticked, and as its exposure to Enron mounted in the case of prepaid forward transactions, the defendants at all times believed there were regulatory issues with the pay-on-demand bonds which they could assert as a defense to payment. Defendants never intended to pay on demand, never intended to treat the surety bonds as the equivalent of letters of credit, and, if called on, always intended to find another way out – which is exactly what they did following JPMorgan Chase's demand in December 2001.

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[1] The Appleton Rule, which was the subject of Liberty's concern under New York law, caused Liberty to seek a legal opinion from outside counsel as reflected in ¶ 24 herein.

FROM CHASE LEGAL (WED) 7. 3'02 17:08/ST. 17:04/NO. 4800925509 P 13

51. In all, JPMorgan Chase advanced approximately $1.9 billion to fund the purchase of crude oil and natural gas from subsidiaries of Enron Corp., relying on the defendants' representations that:

- the surety bonds that they issued were pay-on-demand instruments that were the functional equivalent of letters of credit;
- the surety bonds they issued were valid, binding and enforceable according to their terms;
- the defendants' obligations to pay on demand was absolute and unconditional;
- the defendants would pay within ten (10) days of a written notice by JPMorgan Chase which notice defendants agreed constituted conclusive evidence of all conditions for payment; and
- the defendants would even disregard any instructions by any person not to pay on demand as required by the surety bonds.

52. Inasmuch as each of the defendants participated, along with their agent Wortham in one or more misrepresentations, provided one or more false legal opinions, or participated in a systematic failure to disclose information as to which they had a duty to disclose, with the goal of inducing JPMorgan Chase to accept the bonds in lieu of letters of credit, each of the defendants are jointly and severally liable for the entire amount of one or more of the bonds as further alleged herein.

53. Defendants' wrongful conduct caused direct damages of $1.1 billion, additional damages in an amount to be determined at trial, plus punitive damages.

THE PARTIES

54. JPMorgan Chase Bank is a banking corporation duly organized and existing under the laws of New York.

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55. Upon information and belief, defendant Liberty is a corporation organized and existing under the laws of the Commonwealth of Massachusetts with its principle place of business in Boston, Massachusetts.

56. Upon information and belief, defendant Travelers Casualty & Surety Company ("Travelers") is a corporation organized and existing under the laws of the State of Connecticut with its principle place of business in Hartford, Connecticut.

57. Upon information and belief, defendant St. Paul Fire & Marine Insurance Company ("St. Paul") is a corporation organized and existing under the laws of the State of Minnesota with its principle place of business in St. Paul, Minnesota.

58. Upon information and belief, defendant Continental Casualty Company ("CNA") is a corporation organized and existing under the laws of the State of Illinois with its principle place of business in Chicago, Illinois.

59. Upon information and belief, defendant National Fire Insurance Company of Hartford ("CNA") is a corporation organized and existing under the laws of the State of Connecticut with its principle place of business in Hartford, Connecticut.

60. Upon information and belief, defendant Fireman's Fund Insurance Company ("Fireman's Fund") is a corporation organized and existing under the laws of the State of California with its principle place of business in Novato, California.

61. Upon information and belief, defendant Safeco Insurance Company of America ("Safeco") is a corporation organized and existing under the laws of the State of Washington with its principle place of business in Seattle, Washington.

FROM CHASE LEGAL

62. Upon information and belief, defendant Travelers Indemnity Company ("Travelers") is a corporation organized and existing under the laws of the State of Connecticut with its principle place of business in Hartford, Connecticut.[2]

63. Upon information and belief, defendant Federal Insurance Company ("Federal") is a corporation organized and existing under the laws of the State of Indiana with its principle place of business in New Jersey.

64. Upon information and belief, defendant Hartford Fire Insurance Company ("Hartford") is a corporation organized and existing under the laws of the State of Connecticut with its principle place of business in Hartford, Connecticut.

65. Upon information and belief, defendant Lumbermens Mutual Casualty Company ("Lumbermens") is a corporation organized and existing under the laws of the State of Illinois with its principle place of business in Long Grove, Illinois.

66. Upon information and belief, the defendants collectively are some of the leading insurance companies in the world, and dominate the domestic surety market.

SIGNIFICANT OTHER ENTITIES

67. Prior to its recent bankruptcy, Enron Corp. and its subsidiaries (collectively "Enron") was one of the world's largest integrated natural gas and electricity companies. Enron operated one of the largest natural gas transmission systems in the world. Enron, *inter alia*, was the largest purchaser and marketer of natural gas and the largest non-regulated marketer of electricity in North America. Enron at various points managed the largest portfolio of natural gas risk management contracts in the world.

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[2] Travelers Casualty & Surety Company and Travelers Indemnity Company each issued surety bonds at issue in this litigation. Plaintiff has referenced both companies collectively as "Travelers" unless otherwise specified in the Amended Complaint.

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FROM CHASE LEGAL

68. Enron Natural Gas Marketing Corp. and Enron North America Corp. were wholly owned subsidiaries of Enron Corp. and they engaged in, *inter alia*, the business of producing, transporting and marketing natural gas.

69. On December 2, 2001, Enron Corp. and certain of its subsidiaries filed for protection under Chapter 11 of the United States Bankruptcy Code.

70. Wortham is a limited liability partnership organized under the laws of Texas with its principal place of business in Houston, Texas. At all relevant times Wortham was an insurance agent and producer of insurance premiums for each of the defendants. Upon information and belief, at various times, Enron was one of Wortham's principal insurance clients. Through an arrangement that included various agreements and powers of attorney, the defendant insurance companies directly and indirectly worked with Wortham in order to generate insurance business for themselves including the business related to the surety bonds. Wortham acted as an agent for the defendants, and shared in the premiums paid to the defendants.

71. Philip N. Bair, a Wortham partner in charge of Wortham's Surety Bond Department, was an attorney-in-fact for each of the defendants and the principal person at Wortham producing the surety bonds. Indeed, Philip Bair signed the surety bonds on behalf of the defendants.

72. Mahonia Limited is a company organized in 1992 under the laws of Jersey, Channel Islands. Mahonia Limited is owned by Juris Limited and Lively Limited, two companies organized under the laws of Jersey.

73. Mahonia Limited has bought and sold natural gas and oil.

(WED) 7. 3'02 17:09/ST. 17:04/NO. 4860925509 P 19 FROM CHASE LEGAL

74. Mahonia Natural Gas Limited is a company organized under the laws of Jersey, Channel Islands. Mahonia Natural Gas Limited is also owned by Juris Limited and Lively Limited.

75. Mahonia Natural Gas Limited has bought and sold natural gas.

76. Mahonia Limited and Mahonia Natural Gas Limited are independent companies and are not owned or controlled by JPMorgan Chase. Both Mahonia entities have appointed JPMorgan Chase as their agent to, *inter alia*, prosecute Mahonia's claims against the defendants.

JURISDICTION AND VENUE

77. This Court has subject matter jurisdiction of this action pursuant to 28 U.S.C. § 1332. The amount in controversy exceeds $75,000 exclusive of interests and costs. This Court has personal jurisdiction over each defendant. Venue is proper in this District pursuant to 28 U.S.C. § 1391(a).

FIRST CLAIM – FRAUD AGAINST LIBERTY AND TRAVELERS

78. Enron – like other producers and marketers of natural gas – entered into prepaid forward transactions. Prepaid forward transactions enable companies engaged in commodities businesses to, *inter alia*, access financing.

79. In a prepaid forward transaction, the seller of the commodity typically enters into a contract with a purchaser who pays an amount of money up-front for the future delivery of the commodity on agreed terms.

80. Parties to prepaid forward transactions commonly engage in swap transactions to hedge against the future market price risk of the commodity involved.

81. Major financial institutions such as JPMorgan Chase, Citigroup, Inc. affiliates and others work with clients such as Enron to effectuate prepaid forward transactions. Defendant Travelers has been a subsidiary of Citigroup, Inc. Upon information and belief, Citigroup, Inc.,

FROM CHASE LEGAL (WED) 7. 3'02 17:09/ST. 17:04/NO. 4860925589 P 20

through its member banking affiliates, has engaged in $2.5 billion worth of prepaid oil and gas transactions with Enron – and a substantial but unknown number of such transactions with other energy producers and marketers.

82. JPMorgan Chase participated in similar prepaid forward transactions for other leading producers and marketers of natural gas.

The Initial Enron Prepaid Forward Transactions Secured by Performance Letters of Credit

83. Beginning in approximately 1992, JPMorgan Chase was asked by Enron to participate in prepaid forward sales of natural gas and oil.

84. The transaction contemplated that, *inter alia*, an Enron subsidiary would enter into a forward sale contract with a special purpose entity organized in Jersey, Channel Islands, pursuant to which the special purpose entity would pay up front, or prepay, for Enron's future monthly delivery of oil over the course of a specific term.

85. Mahonia Limited was one of these special purpose entities.

86. Using funds received from JPMorgan Chase, Mahonia Limited paid to an Enron subsidiary a lump sum up-front payment for the future delivery of the agreed upon amount of commodity for delivery to Mahonia Limited at agreed upon pipeline delivery points on an agreed upon future schedule. After receiving the commodity, Mahonia Limited would satisfy its obligation to JPMorgan Chase from the proceeds of its sale of the commodity.

87. Originally, JPMorgan Chase had not been authorized regulatorily to take physical delivery of gas and oil. JPMorgan Chase arranged for the ultimate sale of the commodity by Mahonia.

88. Because Mahonia Limited paid the Enron subsidiary one hundred percent of the purchase price for the commodity on day one, but was not going to receive delivery until

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sometime in the future, the contract contained provisions governing what happened in the event Enron became insolvent or defaulted in its future delivery. In the case of such events the Enron subsidiary was required to pay Mahonia Limited a cash payment (the "Termination Payment"). If the Enron subsidiary failed to make the payment, Enron Corp. was required to make that payment.

89. The Termination Payment was designed to be equal to the value, at the time of breach, of any still undelivered commodity.

90. JPMorgan Chase received permission from the New York State Banking Department to take physical delivery of oil and natural gas in connection with prepaid forward transactions in 1996.

91. Thereafter, the structure of the transactions was altered such that JPMorgan Chase entered into its own forward sale contract under the terms of which JPMorgan Chase became a buyer and Mahonia a seller of the commodity to be received from Enron. In effect, this mirrored the purchase and sale transaction between Mahonia and the Enron subsidiary. JPMorgan Chase then disposed of the commodity as a principal.

92. The parties to a prepaid forward transaction face several economic risks. Among them is the risk that the party in the position of the Enron subsidiary, having received an up-front payment, will not deliver the commodity.

93. To address the risk that Enron Corp. might not perform its obligation to guarantee the transaction, the forward sale contract was to be secured by a letter of credit.

94. Indeed, by the end of 1997, Enron had conducted several prepaid forward transactions involving JPMorgan Chase and, as of December 31, 1997 JPMorgan Chase had in place transactions with a total original amount of $1,802,300,000, guaranteed by Enron Corp.

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and supported by syndicated letters of credit totaling the same amount and involving 35 banks with committed participations to the respective letters of credit ranging from a low of $4.9 million to a high of $58.7 million.

95. In each of these prepaid forward transactions, JPMorgan Chase funded Mahonia's prepayment to Enron.

96. In each instance, JPMorgan Chase advanced the funds to Mahonia on the condition that a letter of credit had been established that could be drawn upon if Enron became insolvent, or the commodity was not delivered, and Enron did not pay.

97. Without the letters of credit, JPMorgan Chase would not have advanced the funds to Mahonia.

98. The letters of credit in the foregoing transactions provided that each bank would pay its commitment amount upon a demand by JPMorgan Chase stating that an event of default had occurred under the gas contract, a Termination Payment was due and Enron Corp. had defaulted on its guarantee of the Termination Payment. This was the only prerequisite to payment on demand.

99. As alleged in greater detail below, it was defendants' inducement of JPMorgan Chase to accept surety bonds in lieu of such letters of credit that gives rise to the fraud claims asserted herein.

In the Midst of A Soft Market, Surety Companies Sought To Expand Their Business By Competing With Banks

100. Traditionally, the surety company's business involved the writing of contract performance bonds where the surety guaranteed the performance of an uncompleted contract.

FROM CHASE LEGAL (WED) 7. 3 07 11:10/ST. 11:04/NO. 4800427069 1 23

The most common form of these is the construction performance bond where a surety guarantees the contractor's performance to the owner of the project.

101. Generally, the issuance, or underwriting, of contract performance bonds is labor intensive in that the surety company needs to evaluate the underlying project, follow the progress of construction and generally be involved with the project in case it needs to step in and perform if the contractor defaults.

102. In the mid-1990s surety companies, including the defendants, were in the midst of a protracted soft market.

103. In order to increase their flow of cash, each of the defendants decided to increase their surety bond business by issuing, *inter alia*, bonds that could be utilized as financial guarantees as a component of a financial transaction.

104. According to the Surety Association of America, a financial guarantee bond is a bond which guarantees payment of a sum of money, whether or not the exact amount is known or stated.

105. Upon information and belief, in the late 1980s, the insurance commissioners of several states, including New York, became concerned that multi-line insurance companies were increasingly exposed to significant risk without proper underwriting or reserves by issuing surety bonds covering certain debt or investment instruments, thereby prejudicing the financial viability of insurance companies to the possible detriment of the policy-holding public.

106. Upon information and belief, in 1989 New York enacted legislation that prohibited multi-line insurance companies, such as the defendants here, from issuing financial guaranty insurance.

FROM CHASE LEGAL

107. Upon information and belief, this New York insurance law applied not only to New York domiciled insurance companies, but to all insurance companies licensed to conduct insurance business in New York whether or not domiciled in New York.

108. Notwithstanding these regulatory developments within the insurance industry, insurance companies with surety bond operations, including the defendants, apparently viewed prepaid forward transactions as a potential market for surety bonds. Indeed, not only could the defendants write millions of dollars in premiums on new prepaid forward transactions, but could replace expiring letters of credit with new surety bonds on pre-existing prepaid transactions.

109. In addition, one or more of the defendants already had significant commercial relationships with Enron.

110. For example, Enron was already one of Liberty's largest customers for surety business.

111. One obstacle to generating this business, however, was convincing financial institutions, such as JPMorgan Chase, that were funding these transactions, that a surety bond would provide the same security as a letter of credit.

112. Liberty, *inter alia*, worked through Wortham, its agent in Houston, Texas.

113. Enron was also one of Wortham's most significant clients, and Wortham pursued Enron business for Liberty, as well as the other defendants.

114. Enron requested JPMorgan Chase to arrange a prepaid forward sale contract for $250 million to close on or about June 30, 1998 (the "First Transaction").

115. At the same time, Philip Bair of Wortham was in discussions with Enron concerning the use of a surety bond to be used in place of a letter of credit for the proposed deal.

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FROM CHASE LEGAL

116. Upon information and belief, Liberty advised Enron that it wanted to work with Wortham and Enron to write a surety bond acceptable to JPMorgan Chase that would serve the function previously filled by letters of credit.

117. On or about June 4, 1998, Liberty attended a meeting with Enron arranged by Wortham for Enron to describe for Liberty the proposed transaction. Upon information and belief, at that meeting Enron provided a detailed description of the prepaid forward transaction and, among other things, informed Liberty that the proceeds of the transaction would be used by Enron to pay down its debt.

118. Upon information and belief, Enron explained to Liberty all of the material aspects of the transaction – that the prepaid forward transaction was a form of financing through which Enron received approximately $250 million.

119. Upon information and belief, Enron explained to Liberty its price risk management activities related to the prepaid forward transaction and discussed the instruments used for these purposes, including forwards, swaps, and options.

120. Liberty and Wortham initially wanted to issue one bond for the proposed $250 million transaction without any other sureties involved. As Philip Bair put it in an e-mail message, dated June 5, 1998, to Liberty:

> If we had enough capacity established, we may want to see if we could replace some existing [letters of credit], particularly ones with a remaining life of 1 – 2 years. The most important thing is getting the first one done smoothly. If a co-surety approach would complicate things, and we can get the bank [i.e., JPMorgan Chase] to accept Liberty Mutual on their own, let's proceed on that basis.

121. Underwriters and legal counsel at Liberty began working with Philip Bair of Wortham and representatives of Enron to discuss with legal representatives of JPMorgan Chase the terms and documents required by JPMorgan Chase.

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122. JPMorgan Chase advised that it would not accept a bond issued only by Liberty and it would require at least one co-surety because JPMorgan Chase did not want the risk for payment on such a large bond to be borne by one insurance company.

123. On or about June 5, 1998, Wortham and Liberty requested Travelers to join the transaction as co-surety. Travelers agreed to do so.

124. On or about June 15, 1998, Traveler's representatives met with Enron which, upon information and belief, described the transaction for Travelers as it had done for Liberty.

125. The representatives of JPMorgan Chase told Liberty and Travelers that the surety bond had to be the functional equivalent of a letter of credit – i.e., a pay-on-demand instrument.

126. In addition to the language of the bond, JPMorgan Chase required that Liberty and Travelers provide legal opinions that the surety bonds were valid, binding and enforceable, according to their terms, and that JPMorgan Chase could rely upon them.

127. On or about June 29, 1998, Norleen Davies, counsel for Liberty, and its chief negotiator on the June 1998 bond, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the June 1998 surety bond was valid, binding and enforceable against Liberty, according to its terms.

128. On or about June 29, 1998, Nicholas Seminara, Counsel to the Bond Division of Travelers, issued an opinion to Mahonia, and authorized that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the June 1998 surety bond was valid, binding and enforceable against Travelers, according to its terms.

129. On or about June 29, 1998, Liberty and Travelers approved and issued Surety Bond Nos. 22 003071 and 61S101175023BCM, respectively, for the $250 million prepaid forward transaction. The June 1998 surety bond is incorporated herein by reference.

FROM CHASE LEGAL

130. Relying on, *inter alia*, the June 1988 surety bond and legal opinions given by Liberty and Travelers to JPMorgan Chase, JPMorgan Chase wire-transferred to Mahonia approximately $250 million to fund the prepaid forward transaction.

131. Liberty and Travelers, like the other defendants, concealed information from JPMorgan Chase as to which they had superior knowledge and a duty to disclose, and which they knew was material to JPMorgan Chase's decision to participate in these transactions, and made representations to and gave opinions to JPMorgan Chase which were misleading, false and fraudulent in light of the concealment, which concealments included, *inter alia*, the following:

- That Liberty and Travelers, and the other defendants, intended to ignore the pay on demand feature of the surety bonds, and at the time of a claim would proceed as follows:
  - Instead of making the Termination Payment to Mahonia which they knew to be the only option available, they would explore the remedies normally available to a surety on a performance bond;
  - They would seek to limit their potential losses; and
  - They would negotiate for performance to limit their exposure.
- That the surety bonds were, or could be viewed by insurance regulators, reinsurers, and officers, employees and agents of Liberty and Travelers and the other defendants as a prohibited form of insurance.

132. After JPMorgan Chase made the demand for payment in December 2001, Liberty and Travelers resisted payment on the grounds that, *inter alia*, had they known the truth about the nature of the prepaid forward transactions, they would have determined that they were not authorized to write the bonds. In fact, they were at all times aware that they were not authorized, or that there was a material issue as to whether they were authorized under applicable insurance regulations to write the bonds – but did not disclose this to JPMorgan Chase, and affirmatively represented that they were authorized to do so.

133. From time to time, but in all cases before Enron's collapse, Liberty and Travelers also knew that their reinsurers had advised them that the surety bonds written for the benefit of Mahonia may not be covered by their reinsurance treaties – but never disclosed this to JPMorgan Chase.

134. Liberty and Travelers knew that JPMorgan Chase was relying on the legal opinions of Liberty and Travelers, and knew that JPMorgan Chase was not aware of the communications on these subjects between Liberty and Travelers, their attorneys and their reinsurers, which undermined the truthfulness of their legal opinions and representations.

135. Liberty and Travelers knowingly agreed to issue bonds which would serve in the place of letters of credit, and would by the terms of the contract with Mahonia, be paid on demand.

136. Liberty's and Travelers' underwriters knew however, that they would not pay on demand, but would rather seek to mitigate their losses by negotiating performance of the underlying obligations.

137. Liberty and Travelers did not disclose this information to JPMorgan Chase.

138. Liberty and Travelers knew that JPMorgan Chase would not have participated in this First Transaction if JPMorgan Chase had been advised that the defendants did not intend to pay on demand.

139. Liberty and Travelers knew that JPMorgan Chase had no way of knowing what their intent was in this regard.

140. But for the fraudulent concealments of Liberty and Travelers, JPMorgan Chase would not have made the payment to Mahonia for the purposes of the First Transaction, or any of the subsequent transactions.

FROM CHASE LEGAL

141. Accordingly, both Liberty and Travelers are each jointly and severally liable for the amount of the loss sustained by JPMorgan Chase as a result of (a) the First Transaction; (b) the Second Transaction through the Sixth Transaction; (c) other damages resulting from the defendants' refusal to pay, in a combined amount in excess of $1.1 billion; and (d) punitive damages.

SECOND CLAIM – FRAUD
AGAINST LIBERTY, TRAVELERS,
ST. PAUL, CNA AND FIREMAN'S FUND

142. Plaintiff repeats and realleges paragraphs 1 through 141 of the Amended Complaint.

143. In August 1998, Liberty, Travelers, St. Paul, CNA, and Fireman's Fund, sought to replace other letters of credit with surety bonds guaranteeing prepaid forward transactions that JPMorgan Chase previously had entered into with Enron in 1996 and 1997 (the "Second Transaction").

144. For example, on numerous occasions in August 1998, Liberty, Travelers, St. Paul, CNA, and Fireman's Fund communicated with Wortham indicating their interest in working with it to replace previously issued letters of credit with surety bonds issued by defendants.

145. To that end, Wortham, acting as agent for the defendants, met with Enron to discuss the replacement of letters of credit with surety bonds on the already existing prepaid forward transactions from 1996 and 1997.

146. In September 1998, Wortham advised representatives of Liberty, Travelers, St. Paul, CNA, and Fireman's Fund that Enron and JPMorgan Chase were willing to accept the surety bonds using the same bond forms utilized in the First Transaction to replace the letters of credit that had secured the previously consummated prepaid forward transactions.

FROM CHASE LEGAL

147. Upon information and belief, in September 1998, Liberty, Travelers, CNA, St. Paul and Fireman's Fund representatives either knew and/or were informed at this time, either by Enron or Wortham, of Enron's price risk management activities, including the use of forwards, swaps, options, and structured financing for corporate purposes.

148. Thus, upon information and belief, Liberty, Travelers, CNA, St. Paul, and Fireman's Fund knew that the proposed transaction was a form of financing through which Enron would receive $250 million from Mahonia advanced by JPMorgan Chase.

149. Upon information and belief, Liberty, Travelers, St. Paul, CNA and Fireman's Fund had a complete understanding of the material aspects of the Second Transaction.

150. Liberty, Travelers, St. Paul, CNA and Fireman's Fund were aware that each was required to provide a pay-on-demand guarantee functionally equivalent to a letter of credit, and a legal opinion for the benefit of JPMorgan Chase that the surety bonds were valid, binding and enforceable, according to their terms.

151. Each of these defendants was provided with, on or about September 24 or 25, 1998, copies of the forward sale contracts, and draft bond forms for the Second Transaction.

152. Further, CNA, St. Paul and Fireman's Fund knew that JPMorgan Chase required that a bond issued by Liberty and Travelers be the functional equivalent of a letter of credit – i.e., a pay-on-demand instrument.

153. CNA, St. Paul and Fireman's Fund each also knew that JPMorgan Chase was entitled to rely on Liberty's, Travelers', CNA's, St. Paul's and Fireman's Fund's legal opinions that the surety bonds were valid, binding and enforceable, according to their terms.

154. On or about September 29, 1998, Norleen Davies, counsel for Liberty, and its chief negotiator on the June 1998 and September 1998 surety bonds, issued an opinion to

FROM CHASE LEGAL (MON) F. 3 '02 11:12/ST. 11:09/NO. 4800726209 P 31

Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the September 1998 surety bonds were valid, binding and enforceable against Liberty according to their terms.

155. On or about September 28, 1998, Nicholas Seminara, the Counsel to the Bond Division of Travelers, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the September 1998 surety bonds were valid, binding and enforceable against Travelers according to their terms.

156. On or about September 28, 1998, John F. Simanski, Jr., counsel to St. Paul issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the September 1998 surety bonds were valid, binding and enforceable against St. Paul according to their terms.

157. On or about September 28, 1998, Sandra D. Wagman, counsel to CNA issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the September 1998 surety bonds were valid, binding and enforceable against CNA according to their terms.

158. On or about September 28, 1998, Keith E. Langan, counsel to Fireman's Fund issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the September 1998 surety bonds were valid, binding and enforceable against Fireman's Fund according to their terms.

159. On or about September 28, 1998 Liberty, Travelers, St. Paul, CNA and Fireman's Fund approved and issued three (3) surety bonds, with the following Surety Bond Nos.: 22-003-142, 61SI011789965BCM, 400JX8826, 190475173, and 11141592649, respectively, for $255,760,000 of the remaining unpaid amount from previously consummated prepaid forward

transaction, dated December 18, 1997; Surety Bond Nos.: 22-003-140, 61S1011789963BCM, 400JX8824, 190475142, and 11141592623 for $105,183,000 of the unpaid amount from the previously consummated prepaid forward transaction, dated December 16, 1996; and Surety Bond No.: 22-003-141; 61S1011789964BCM, 400JX8825, 190475156, and 11151592631 for $58,434,000.00 of the unpaid amount for the previously consummated prepaid forward transaction, dated December 16, 1996. The three (3) bonds are incorporated herein by reference.

160. Relying on, *inter alia*, the surety bonds and the opinions given by Liberty, Travelers, CNA, St. Paul and Fireman's Fund to JPMorgan Chase, JPMorgan Chase agreed to continue funding the previously consummated prepaid forward transactions.

161. Liberty, Travelers, St. Paul, CNA and Fireman's Fund concealed information from JPMorgan Chase as to which they had superior knowledge and a duty to disclose, and which they knew was material to JPMorgan Chase's decision to participate in these transactions, and made representations to, and gave opinions to JPMorgan Chase which were misleading, false and fraudulent in light of the concealment, which concealment included, *inter alia*, the following:

- That Liberty, Travelers, CNA, St. Paul, and Fireman's Fund, intended to ignore the pay-on-demand feature of the surety bonds, and at the time of a claim would proceed as follows:
  - Instead of making the Termination Payment to Mahonia which they knew to be the only option available, they would explore the remedies normally available to a surety on a contract performance bond;
  - They would seek to limit their potential losses; and
  - They would negotiate for performance to limit its exposure.
- That the surety bonds were, or could be viewed by insurance regulators, reinsurers, and officers, employees and agents of the defendants as a prohibited form of insurance.

(WED) 7. 3'02 17:13/St. 17:04/No. 4800925569 P 33
FROM CHASE LEGAL

162. After JPMorgan Chase made a demand for payment, Liberty, Travelers, CNA, St. Paul, and Fireman's Fund resisted payment on the grounds that, *inter alia*, had they known the truth about the nature of the prepaid forward transactions, they would have determined that they were not authorized to write the bonds. In fact, they were at all times aware that they were not authorized or that there was a material issue as to whether they were authorized under applicable insurance regulations to write the bonds – but none of the defendants disclosed this to JPMorgan Chase, and affirmatively represented that they were authorized to do so.

163. From time to time, but in all cases before Enron's collapse, Liberty, Travelers, CNA, St. Paul, and Fireman's Fund also knew that their reinsurers had advised them that the surety bonds written for the benefit of Mahonia may not be covered by their reinsurance treaties – but never disclosed this to JPMorgan Chase.

164. Liberty, Travelers, CNA, St. Paul and Fireman's Fund knew that JPMorgan Chase was relying on the legal opinions of each, and knew that JPMorgan Chase was not aware of the communications on these subjects between Liberty, Travelers, CNA, St. Paul or Fireman's Fund, their respective attorneys and their reinsurers, which undermined the truthfulness of their legal opinions and representations.

165. Liberty, Travelers, CNA, St. Paul and Fireman's Fund knowingly agreed to issue bonds which would serve in the place of letters of credit, and would by the terms of the contract with Mahonia, be paid on demand.

166. Liberty's, Travelers', CNA's, St. Paul's and Fireman's Fund's underwriters or representatives knew that they would not pay on demand, but rather seek to mitigate their losses by negotiating performance of the underlying obligations.

FROM CHASE LEGAL (WED) 7. 5 02 11:13/RI. 11:04/NO. 4800926989 : 39

167. Liberty, Travelers, CNA, St. Paul and Fireman's Fund did not disclose this information to JPMorgan Chase.

168. Liberty, Travelers, CNA, St. Paul, and Fireman's Fund knew that JPMorgan Chase would not have participated in this transaction if JPMorgan Chase had been advised that the defendants did not intend to pay on demand.

169. Liberty, Travelers, CNA, St. Paul, and Fireman's Fund knew that JPMorgan Chase had no way of knowing what their intent was in this regard.

170. But for the fraudulent concealments of Liberty, Travelers, CNA, St. Paul, and Fireman's Fund, JPMorgan Chase would not have made the payment to Mahonia for the purposes of this Second Transaction, or any of the subsequent transactions.

171. Accordingly, Liberty, Travelers, CNA, St. Paul, and Fireman's Fund are each jointly and severally liable for the losses sustained by JPMorgan Chase as a result of (a) the Second Transaction; (b) the Third Transaction through the Sixth Transaction; (c) other damages resulting from the defendants' refusal to pay; and (d) punitive damages.

THIRD CLAIM – FRAUD
AGAINST TRAVELERS, SAFECO,
ST. PAUL, CNA, AND FIREMAN'S FUND

172. Plaintiff repeats and realleges paragraphs 1 through 171 hereof.

173. Starting in early to mid-November 1998, Travelers, St. Paul, CNA, Safeco and Fireman's Fund communicated with Wortham regarding participating in another transaction with Enron to issue a surety bond in lieu of a letter of credit, to secure a proposed December 1998 forward sale contract (the "Third Transaction").

174. Travelers, St. Paul, CNA and Fireman's Fund, based on their previous involvement in the First and Second Transactions, and based on Safeco's discussions with Wortham, were each aware of all material aspects of the proposed Third Transaction, as well as

FROM CHASE LEGAL (MON) N. 5 '02 11:13/ST. 11:09/NO. 4000927209 P 33

what would be necessary to induce JPMorgan Chase to agree to accept surety bonds in lieu of letters of credit for this forward sale contract.

175. Upon information and belief, in November 1998, Travelers, St. Paul, Safeco, CNA, and Fireman's Fund each knew of, or were informed of, Enron's price risk management activities related to the prepaid forward transaction including the use of swaps, hedging, options, and structured financing for its corporate purposes.

176. Thus, by November 1998, Travelers, St. Paul, CNA, Safeco, and Fireman's Fund knew and/or were informed that the proposed transaction was a form of financing through which Enron would receive approximately $250 million from Mahonia advanced by JPMorgan Chase.

177. Upon information and belief, Travelers, St. Paul, CNA, Safeco, and Fireman's Fund had a complete understanding of the material aspects of the Third Transaction.

178. In the latter half of November 1998, Travelers, St. Paul, CNA, Fireman's Fund, and Safeco, each received the proposed bond form which was the same form used in the First and Second Transactions, and agreed to act as co-sureties on the Advance Payment Supply Surety Bond for this Third Transaction.

179. Travelers, St. Paul, CNA, Safeco and Fireman's Fund were aware that each was required to provide a surety bond that was the functional equivalent of a letter of credit – i.e., a pay-on-demand instrument.

180. In addition, Travelers, St. Paul, CNA, Safeco and Fireman's Fund were aware that each was required to provide a legal opinion and JPMorgan Chase could rely upon it that the surety bonds were valid, binding and enforceable according to their terms.

181. On or about November 25, 1998, Rosemary Quinn, counsel to St. Paul, issued an opinion to Mahonia and consented that a copy be sent to JPMorgan Chase for its benefit, that,

(WED) 7. 3'02 17:13/ST. 17:04/NO. 4800925589 P 30
FROM CHASE LEGAL

inter alia, the December 1998 surety bond was valid, binding and enforceable against St. Paul, according to its terms.

182. On or about November 30, 1998, Nicholas Seminara, the Counsel to the Bond Division of Travelers, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the December 1998 surety bond was valid, binding and enforceable against Travelers, according to its terms.

183. On or about November 30, 1998, Laura M. Murphy, counsel to Safeco, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the December 1998 surety bond was valid, binding and enforceable against Safeco, according to its terms.

184. On or about December 2, 1998, Sandra Wagman, counsel to CNA Surety, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the December 1998 surety bond was valid, binding and enforceable against Safeco, according to its terms.

185. On or about December 2, 1998, Keith E. Langan, counsel to Fireman's Fund, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the December 1998 surety bond was valid, binding and enforceable against Fireman's Fund, according to its terms.

186. On or about December 2, 1998, Travelers, Fireman's Fund, Safeco, St. Paul and CNA approved and issued Surety Bond Nos. 61S01181219BCM, 11141592664, 5925110, 400JZ7535, and 159129510, respectively, for the $250 million prepaid forward transaction. The December 1998 surety bond is incorporated herein be reference.

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FROM CHASE LEGAL

187. Relying on, *inter alia*, the December 1998 surety bond and the legal opinions given by Travelers, St. Paul, CNA, Fireman's Fund, and Safeco to JPMorgan Chase, JPMorgan Chase wire-transferred to Mahonia approximately $250 million to fund the prepaid forward transaction.

188. Travelers, Fireman's Fund, Safeco, St. Paul and CNA concealed information from JPMorgan Chase as to which they had superior knowledge and a duty to disclose, and which they knew was material to JPMorgan Chase's decision to participate in these transactions, and made representations to and gave opinions to JPMorgan Chase which were misleading, false, and fraudulent in light of the concealment, which concealments, included, *inter alia*, the following:

- That Travelers, Safeco, St. Paul, CNA, and Fireman's Fund and the other defendants, intended to ignore the pay-on-demand feature of the surety bonds, and at the time of a claim would proceed as follows:
  - Instead of making the Termination Payment to Mahonia which they knew to be the only option available, they would explore the remedies normally available to a surety on a contract performance bond;
  - They would seek to limit their potential losses; and
  - They would negotiate for performance to limit their exposure.
- That the surety bonds were, or could be viewed by insurance regulators, reinsurers, and officers, employees and agents of Travelers, St. Paul, Safeco, CNA, and Fireman's Fund as a prohibited form of insurance.

189. After JPMorgan Chase made a demand for payment in December 2001 on the December 1998 surety bond, Travelers, Safeco, St. Paul, CNA and Fireman's Fund resisted payment on the grounds that, *inter alia*, had they known the truth about the nature of the prepaid forward transactions, they would have determined they were not authorized to write the bonds. In fact, however, they were at all times aware that they were not authorized, or that there was a material issue as to whether they were authorized under applicable insurance regulations to write

FROM CHASE LEGAL (WED) 7. 3'02 17:14/ST. 17:04/NO. 4800972589 P 36

the bonds – but none of them disclosed this to JPMorgan Chase, and affirmatively represented that they were authorized to do so.

190. From time to time, but in all cases before Enron's collapse, Travelers, Safeco, St. Paul, CNA and Fireman's Fund also knew that their reinsurers had advised them that the surety bonds written for the benefit of Mahonia may not be covered by their reinsurance treaties – but never disclosed this to JPMorgan Chase.

191. Travelers, Safeco, St. Paul, CNA and Fireman's Fund knew that JPMorgan Chase was relying on the legal opinions of each, and knew that JPMorgan Chase was not aware of the communications on these subjects between Travelers, Safeco, St. Paul, CNA, and Fireman's Fund, their attorneys and their reinsurers, which undermined the truthfulness of their legal opinions and representations.

192. Travelers, Safeco, St. Paul, CNA and Fireman's Fund knowingly agreed to issue bonds which would serve in the place of letters of credit, and would by the terms of the contract with Mahonia, be paid on demand.

193. Travelers', Safeco's, St. Paul's, CNA's and Fireman's Fund's underwriters knew, however, that they would not pay on demand, but rather seek to mitigate their losses by negotiating for performance of the underlying obligations.

194. Travelers, Safeco, St. Paul, CNA and Fireman's Fund did not disclose this information to JPMorgan Chase.

195. Travelers, Safeco, St. Paul, CNA and Fireman's Fund knew that JPMorgan Chase would not have participated in this transaction if JPMorgan Chase had been advised that the defendants did not intend to pay on demand.

(WED) 7. 3'02 18:02/ST. 18:00/NO. 4860027551 P 5

FROM CHASE LEGAL

196. Travelers, Safeco, St. Paul, CNA and Fireman's Fund knew that JPMorgan Chase had no way of knowing what their intent was in this regard.

197. But for the fraudulent concealments of Travelers, Safeco, St. Paul, CNA and Fireman's Fund, JPMorgan Chase would not have made the payment to Mahonia for the purpose of funding the Third Transaction, or any of the subsequent transactions.

198. Accordingly, Travelers, Safeco, St. Paul, CNA, and Fireman's Fund are each jointly and severally liable for the losses sustained by JPMorgan Chase as a result of (a) the Third Transaction; (b) the Fourth Transaction through the Sixth Transaction; (c) other damages resulting from the defendants' refusal to pay; and (d) punitive damages.

FOURTH CLAIM – FRAUD
AGAINST FEDERAL, TRAVELERS,
ST. PAUL, CNA, AND FIREMAN'S FUND

199. Plaintiff repeats and realleges paragraphs 1 through 198 hereof.

200. In mid-June 1999, Federal, Travelers, St. Paul, CNA, and Fireman's Fund representatives discussed with Wortham another opportunity to issue a surety bond (the "Fourth Transaction") in lieu of a letter of credit similar to the surety bonds issued in June, September and December 1998.

201. By this time, Federal, Travelers, St. Paul, CNA, and Fireman's Fund were each aware of all material aspects of the Fourth Transaction, as well as the purposes for which the transaction was entered into, based on their previous involvement in the First, Second and Third Transactions and/or based on information received from Enron and Wortham in or around June 1999.

202. Indeed, upon information and belief, Federal, Travelers, St. Paul, CNA, and Fireman's Fund representatives had all met with Enron representatives during which time they had been informed of Enron's price risk management activities related to the prepaid forward

(WED) 7. 3'02 18:02/ST. 18:00/NO. 4860922591 P 6
FROM CHASE LEGAL

transaction, including the use of forwards, swaps, options and structured financing for corporate purposes.

203. Thus, Federal, Travelers, St. Paul, CNA and Fireman's Fund knew that the proposed transaction was a form of financing to Enron, through which Enron would receive approximately $500 million from Mahonia advanced by JPMorgan Chase.

204. At this point, the surety bonds had been formulated by Liberty and Travelers, utilized in three prior transactions, and now, without question, Federal, St. Paul, Travelers, CNA, and Fireman's Fund agreed to the obligations in the surety bond.

205. Further, Federal, Travelers, St. Paul, CNA and Fireman's Fund representatives were aware, upon information and belief, that the surety bond had to be the functional equivalent of a letter of credit – i.e., a pay on demand instrument.

206. Federal, Travelers, St. Paul, CNA and Fireman's Fund each knew that JPMorgan Chase required that Federal, Travelers, St. Paul, CNA and Fireman's Fund provide legal opinions that the surety bonds were valid, binding and enforceable according to their terms, and that JPMorgan Chase could rely upon them.

207. On or about June 28, 1999, Susan J. Murr, Associate Counsel of Chubb & Son, a division of Federal Insurance Company, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the June 1999 surety bond was valid, binding and enforceable against Federal, according to its terms.

208. On or about June 28, 1999, Nicholas Seminara, the Counsel to the Bond Division of Traveler's, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the June 1999 surety bond was valid, binding and enforceable against Traveler's, according to its terms.

(WED) 7. 3'02 18:02/ST. 18:00/NO. 4880925591 P 7
FROM CHASE LEGAL

209. On or about June 28, 1999, Rosemary Quinn, the Senior Corporate Counsel to St. Paul, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the June 1999 surety bond was valid, binding and enforceable against St. Paul, according to its terms.

210. On or about June 29, 1999, Marvin J. Cashion, Deputy General Counsel for CNA, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the June 1999 surety bond was valid, binding and enforceable against CNA, according to its terms.

211. On or about June 30, 1999, Robert C. Buckley, Chief Counsel for Fireman's Fund, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase for its benefit, that, *inter alia*, the June 1999 surety bond was valid, binding and enforceable against Fireman's Fund, according to its terms.

212. On or about June 28, 1999, Federal, Travelers, St. Paul, CNA, and Fireman's Fund approved and issued Surety Bond Nos. 8153-80-20, 61S103171488BCM, JZ8081, 190772038, and 11141665189, respectively, for the $500 million prepaid forward transaction. The June 1999 surety bond is incorporated herein by reference.

213. Relying on, *inter alia*, the June 1999 surety bond and legal opinions given by Federal, Travelers, St. Paul, CNA, and Fireman's Fund to JPMorgan Chase, JPMorgan Chase wire-transferred to Mahonia approximately $500 million to fund the prepaid forward transaction.

214. Federal, Travelers, St. Paul, CNA, and Fireman's Fund concealed information from JPMorgan Chase as to which they had superior knowledge and a duty to disclose, and which they knew was material to JPMorgan Chase's decision to participate in these transactions, and made representations to and gave opinions to JPMorgan Chase which were misleading, false,

FROM CHASE LEGAL (WED) W. 3'02 18:03/ST. 18:00/NO. 4800927991 P 8

and fraudulent in light of the concealment, which concealments, included, *inter alia*, the following:

- That Federal, Travelers, St. Paul, CNA, and Fireman's Fund, and the other defendants, intended to ignore the pay-on-demand feature of the surety bonds, and at the time of a claim would proceed as follows:
  - Instead of making the Termination Payment to Mahonia which they knew to be the only option available, they would explore the remedies normally available to a surety on a performance bond;
  - They would seek to limit their potential losses; and
  - They would negotiate for performance to limit its exposure.
- That the surety bonds were, or could be viewed by insurance regulators, reinsurers, and officers, employees and agents of Travelers, Federal, St. Paul, CNA, and Fireman's Fund and the other defendants as a prohibited form of insurance.

215. After JPMorgan Chase made the demand for payment in December 2001, Federal, Travelers, St. Paul, CNA and Fireman's Fund resisted payment on the grounds that, *inter alia*, had they known the truth about the nature of the prepaid forward transactions, they would have determined that they were not authorized to write the bonds. In fact, however, they were at all times aware that they were not authorized or that there was a material issue as to whether they were authorized under applicable insurance regulations to write the bonds – but none of them disclosed this to JPMorgan Chase, and affirmatively represented that they were authorized to do so.

216. From time to time, but in all cases before Enron's collapse, Federal, Travelers, St. Paul, CNA and Fireman's Fund also knew that their reinsurers had advised them that the surety bonds written for the benefit of Mahonia may not be covered by their reinsurance treaties – but never disclosed this to JPMorgan Chase.

(WED) 7. 3'02 18:03/ST. 18:00/NO. 4860925591 P 9
FROM CHASE LEGAL

217. Federal, Travelers, St. Paul, CNA and Fireman's Fund knew that JPMorgan Chase was relying on the legal opinions of Federal, Travelers, St. Paul, CNA and Fireman's Fund, and knew that JPMorgan Chase was not aware of the communications on these subjects between Travelers, Federal, St. Paul, CNA and Fireman's Fund, their attorneys and their reinsurers, which undermined the truthfulness of their legal opinions and representations.

218. Federal, Travelers, St. Paul, CNA and Fireman's Fund knowingly agreed to issue the June 1999 surety bond which would serve in the place of letters of credit, and would by the terms of the contract with Mahonia, be paid on demand.

219. Federal's, Travelers', St. Paul's, CNA's and Fireman's Fund's underwriters knew that they would not pay on demand, but rather seek to mitigate their losses by negotiating performance of the underlying obligations.

220. Federal, Travelers, St. Paul, CNA and Fireman's Fund did not disclose this information to JPMorgan Chase.

221. Federal, Travelers, St. Paul, CNA and Fireman's Fund knew that JPMorgan Chase would not have participated in this Fourth Transaction if JPMorgan Chase had been advised that the defendants did not intend to pay on demand.

222. Federal, Travelers, St. Paul, CNA and Fireman's Fund knew that JPMorgan Chase had no way of knowing what their intent was in this regard.

223. But for the fraudulent concealments of Federal, Travelers, St. Paul, CNA and Fireman's Fund, JPMorgan Chase would not have made the payment to Mahonia for the purposes of the Fourth Transaction, or any of the subsequent transactions.

224. Accordingly, Federal, Travelers, St. Paul, CNA, and Fireman's Fund are each jointly and severally liable for the losses sustained by JPMorgan Chase as a result of (a) the

(WED) 7. 3'02 18:03/ST. 18:00/NO. 4860925591 P 10
FROM CHASE LEGAL

Fourth Transaction; (b) the Fifth and the Sixth Transactions; (c) other damages resulting from the defendants' refusal to pay; and (d) punitive damages.

FIFTH CLAIM – FRAUD AGAINST FEDERAL, TRAVELERS, LUMBERMENS, AND FIREMAN'S FUND

225. Plaintiff repeats and realleges paragraphs 1 through 224 hereof.

226. Starting in mid-May 2000, discussions again started among Federal, Travelers, Lumbermens, Fireman's Fund and Wortham, defendants' agent, concerning a new surety bond opportunity with Enron (the "Fifth Transaction").

227. The discussions among representatives from Wortham, Enron, Federal, Travelers, Lumbermens and Fireman's Fund continued through the end of June 2000 concerning this new proposal. Initially, the proposal from Enron and Wortham was for a $750 million surety bond, in the same form as in the First through Fourth Transactions.

228. However, prior to the consummation of the June 2000 Surety Bond, the transaction amount was modified to $400 million, still with the same bond form as in the First through Fourth Transactions.

229. By this time, Federal, Travelers, Lumbermens and Fireman's Fund were each aware of all material aspects of the Fifth Transaction, as well as the purpose for which the transaction was entered into, based on their previous involvement in the First, Second, Third and Fourth Transactions, and/or based on information received from Enron and Wortham in or around June 2000.

230. Upon information and belief, by June 2000, Federal's, Travelers', Fireman's Fund's and Lumbermens' representatives had all met with Enron representatives during which time they had been informed of Enron's price risk management activities related to the prepaid

(WED) 7. 3'02 18:03/ST. 18:00/NO. 4860925591 P 11
FROM CHASE LEGAL

forward transaction, including the use of forwards, swaps, options and structured financing for corporate purposes.

231. Thus, by June 2000, Federal, Travelers, Fireman's Fund and Lumbermens knew of and/or were informed that the proposed transaction was a form of financing through which Enron would receive approximately $400 million from Mahonia advanced by JPMorgan Chase.

232. Again, in mid-June 2000, Wortham communicated with Federal, Travelers, Lumbermens and Fireman's Fund regarding this Surety Bond, and the fact that all aspects of the transaction would be the same as in the First through Fourth Transactions.

233. Indeed, Federal, Travelers, Lumbermens and Fireman's Fund were each aware that the surety bond had to be the functional equivalent of a letter of credit – i.e., a pay-on-demand instrument.

234. In addition to the language of the bond, JPMorgan Chase required that Federal, Travelers, Lumbermens and Fireman's Fund provide legal opinions for the benefit of JPMorgan Chase that the surety bond was valid, binding and enforceable, according to its terms and that JPMorgan Chase could rely upon them.

235. On or about June 23, 2000, Julie A. Garrison, counsel for Fireman's Fund, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the June 2000 surety bond was valid, binding and enforceable against Fireman's Fund, according to its terms.

236. On or about June 28, 2000, William J. Murray, counsel to Chubb & Son, a division of Federal Insurance Company, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the June 2000 surety bond was valid, binding and enforceable against Federal, according to its terms.

(WED) 7. 3'02 18:04/ST. 18:00/NO. 4860525591 P 12
FROM CHASE LEGAL

237. On or about June 28, 2000, Julie Alleyne, counsel to the Bond Division of Travelers, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the June 2000 surety bond was valid, binding and enforceable against Travelers, according to its terms.

238. On or about June 28, 2000, Allan R. Sye, an assistant general counsel of Lumbermens Mutual Casualty Company, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the June 2000 surety bond was valid, binding and enforceable against Lumbermens, according to its terms.

239. On or about June 28, 2000, Federal, Travelers Indemnity, Lumbermens and Fireman's Fund each proposed a Surety Bond with Bond Nos. 81538343, 61S103299951BCV, 001825, and 11133420775, respectively, for the $500 million prepaid forward transaction. The June 2000 surety bond is incorporated herein by reference.

240. Relying on, *inter alia*, the June 2000 surety bond and legal opinions given by Federal, Travelers, Lumbermens and Fireman's Fund to JPMorgan Chase as described herein, JPMorgan Chase wire-transferred to Mahonia approximately $400 million to fund the prepaid forward transaction in this Fifth Transaction.

241. Federal, Travelers, Lumbermens and Fireman's Fund, like the other defendants, concealed information from JPMorgan Chase as to which they had superior knowledge and a duty to disclose and which they knew was material to JPMorgan Chase's decision to participate in these transactions, and made representations to and gave opinions to JPMorgan Chase which were misleading, false and fraudulent in light of the concealment, which concealments included, *inter alia*, the following:

(WED) 7. 3'02 18:04/ST. 18:00/NO. 4860925591 P 13
FROM CHASE LEGAL

- That Federal, Travelers, Lumbermens and Fireman's Fund, and the other defendants, intended to ignore the pay-on-demand feature of the surety bonds, and at the time of a claim would proceed as follows:
  - Instead of making the Termination Payment to Mahonia which they knew to be the only option available, they would explore the remedies normally available to a surety on a performance bond;
  - They would seek to limit their potential losses; and
  - They would negotiate for performance to limit its exposure.
- That the surety bonds could be viewed by insurance regulators, reinsurers, and officers, employees and agents of Federal, Travelers, Lumbermens and Fireman's Fund and the other defendants as a prohibited form of insurance.

242. After JPMorgan Chase made a demand for payment, Federal, Travelers, Lumbermens and Fireman's Fund resisted payment on the grounds that, *inter alia*, had they known the truth about the nature of the prepaid forward transactions, they would have determined that they were not authorized to write the bonds. In fact, they were at all times aware that they were not authorized or that there was a material issue as to whether they were authorized under applicable insurance regulations to write the bonds – but none of them disclosed this to JPMorgan Chase, and affirmatively represented that they were authorized to do so.

243. From time to time, but in all cases before Enron's collapse, Federal, Travelers, Lumbermens and Fireman's Fund also knew that their reinsurers had advised them that the surety bonds written for the benefit of Mahonia may not be covered by their reinsurance treaties – but never disclosed this to JPMorgan Chase.

244. Federal, Travelers, Lumbermens and Fireman's Fund knew that JPMorgan Chase was relying on the legal opinions of Federal, Travelers, Lumbermens and Fireman's Fund, and knew that JPMorgan Chase was not aware of the communications on these subjects between

(WED) 7. 3'02 18:04/ST. 18:00/NO. 4860925591 P 14
FROM CHASE LEGAL

Federal, Travelers, Lumbermens and Fireman's Fund, their attorneys, and their reinsurers, which undermined the truthfulness of their legal opinions and representation.

245. Federal, Travelers, Lumbermens and Fireman's Fund knowingly agreed to issue bonds which would serve in the place of letters of credit, and would by the terms of the contract with Mahonia, be paid on demand.

246. Federal's, Travelers', Lumbermens' and Fireman's Fund's underwriters knew however that they would not pay on demand, but rather seek to mitigate their losses by negotiating performance of the underlying obligations.

247. Federal, Travelers, Lumbermens and Fireman's Fund did not disclose this information to JPMorgan Chase.

248. Federal, Travelers, Lumbermens and Fireman's Fund knew that JPMorgan Chase would not have participated in this Fifth Transaction if JPMorgan Chase had been advised that the defendants did not intend to pay on demand.

249. Federal, Travelers, Lumbermens and Fireman's Fund knew that JPMorgan Chase had no way of knowing what their intent was in this regard.

250. But for the fraudulent concealments of Federal, Travelers, Lumbermens and Fireman's Fund, JPMorgan Chase would not have made the payment to Mahonia for the purposes of the Fifth Transaction, or any of the subsequent transactions.

251. Accordingly, Federal, Travelers, Lumbermens, and Fireman's Fund are each jointly and severally liable for the losses sustained by JPMorgan Chase as a result of (a) the Fifth Transaction; (b) the Sixth Transaction; (c) other damages; and (d) punitive damages.

SIXTH CLAIM – FRAUD
AGAINST TRAVELERS, ST. PAUL, LUMBERMENS, HARTFORD AND SAFECO

252. Plaintiff repeats and realleges paragraphs 1 through 251 hereof.

(WED) 7. 3'02 18:05/ST. 18:00/NO. 4860925591 P 15
FROM CHASE LEGAL

253. In mid-November 2000, Enron discussed with Wortham another surety bond opportunity ("the Sixth Transaction") similar to those previously transacted in June, September and December 1998, June 1999, and June 2000. This Sixth Transaction was for a surety bond for approximately $365 million, and would be based on the same bond form used in the First through Fifth Transactions.

254. By mid to late November 2000, Travelers, St. Paul, Lumbermens, Hartford, and Safeco representatives had agreed that they wanted to be involved in the Sixth Transaction on the same terms as in the First through Fifth Transactions.

255. Upon information and belief, Travelers, St. Paul, Lumbermens, Safeco, and Hartford had a complete understanding of the material aspects of the Sixth Transaction.

256. Upon information and belief, by November 2000, Travelers, St. Paul, Lumbermens, Safeco, and Hartford each knew of, or were informed of, Enron's price risk management activities related to the prepaid forward transaction, including the use of forwards, swaps, options, and structured financing for corporate purposes.

257. Thus, by November 2000, Travelers, St. Paul, Lumbermens, Safeco, and Hartford knew and/or were informed that the proposed transaction was a form of financing through which Enron would receive $365 million from Mahonia advanced by JPMorgan Chase.

258. Travelers, St. Paul, Lumbermens, Hartford and Safeco were all aware that each was required to provide a surety bond which had to be the functional equivalent of a letter of credit – i.e., a pay-on-demand instrument.

259. In addition to the language of the bond, JPMorgan Chase required that Travelers, St. Paul, Lumbermens, Hartford and Safeco provide a legal opinion for the benefit of JPMorgan

(WED) 7. 3'02 18:05/ST. 18:00/NO. 4860925591 P 16
FROM CHASE LEGAL

Chase stating that the surety bonds were valid, binding and enforceable, according to their terms, and that JPMorgan Chase could rely upon them.

260. On or about December 22, 2000, Julie Alleyne, the Counsel to the Bond Division of Travelers, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the December 2000 Surety Bond was valid, binding and enforceable against Travelers according to its terms.

261. On or about December 22, 2000, Allan R. Syc, an Assistant General Counsel of Lumbermens, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the December 2000 Surety Bond was valid, binding and enforceable against Lumbermens, according to its terms.

262. On or about December 27, 2000, Rosemary Quinn, counsel for St. Paul, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the December 2000 Surety Bond was valid, binding and enforceable against St. Paul, according to its terms.

263. On or about December 27, 2000, Robert S. Brooks, an Assistant General Counsel of Hartford, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the December 2000 Surety Bond was valid, binding and enforceable against Hartford, according to its terms.

264. On or about December 27, 2000, Edward H. Southon, Assistant General Counsel of Safeco, issued an opinion to Mahonia, and consented that a copy be sent to JPMorgan Chase, that, *inter alia*, the December 2000 Surety Bond was valid, binding and enforceable against Safeco, according to its terms.

(WED) 7. 3'02 18:05/ST. 18:00/NO. 4860925591 P 17
FROM CHASE LEGAL

265. On or about December 28, 2000, Travelers, St. Paul, Lumbermens, Hartford and Safeco approved and issued the Surety Bond with Nos. 061S103500004BCM, SD 4611, 970483, 61BSBAP3909, and 609 88 70, respectively, for the prepaid forward transaction, which is incorporated herein by reference.

266. Relying on, *inter alia*, the language of the December 2000 Surety Bond and legal opinions given by Travelers, St. Paul, Lumbermens, Hartford and Safeco to JPMorgan Chase as described herein, JPMorgan Chase wire-transferred to Mahonia approximately $365,000,000 to fund the prepaid forward transaction.

267. Travelers, St. Paul, Lumbermens, Hartford, and Safeco, like the other defendants, concealed information from JPMorgan Chase as to which they had superior knowledge and a duty to disclose and which they knew was material to JPMorgan Chase's decision to participate in these transactions, and made representations to and gave opinions to JPMorgan Chase which were misleading, false and fraudulent in light of the concealment, which concealments included, *inter alia*, the following:

- That Travelers, St. Paul, Lumbermens, Hartford, and Safeco, and the other defendants, intended to ignore the pay-on-demand feature of the surety bonds, and at the time of a claim would proceed as follows:
  - Instead of making the Termination Payment to Mahonia which they knew to be the only option available, they would explore the remedies normally available to a surety on a performance bond;
  - They would seek to limit their potential losses; and
  - They would negotiate for performance to limit its exposure.
- That the surety bonds could be viewed by insurance regulators, reinsurers, and officers, employees and agents of Travelers, St. Paul, Lumbermens, Hartford, and Safeco and the other defendants as a prohibited form of insurance.

(WED) 7. 3'02 18:05/ST. 18:00/NO. 4860925591 P 18

FROM CHASE LEGAL

268. After JPMorgan Chase made the demand for payment in December 2001, Travelers, St. Paul, Lumbermens, Hartford, and Safeco resisted payment on the grounds that, *inter alia*, had they known the truth about the financial nature of the prepaid forward transactions, they would have determined that they were not authorized to write the bonds. In fact, they were at all times aware that they were not authorized or that there was a material issue as to whether they were authorized under applicable insurance regulations to write the bonds -- but none of them disclosed this to JPMorgan Chase, and affirmatively represented that they were authorized to do so.

269. From time to time, but in all cases before Enron's collapse, Travelers, St. Paul, Lumbermens, Hartford, and Safeco knew that their reinsurers had advised them that the bonds they had written for the benefit of Mahonia could be potentially prohibited financial guarantees, and may not be covered by their reinsurance treaties -- but never disclosed this to JPMorgan Chase.

270. Travelers, St. Paul, Lumbermens, Hartford, and Safeco knew that JPMorgan Chase was relying on the legal opinions of Liberty and Travelers, and knew that JPMorgan Chase was not aware of the communications on these subjects between Travelers, St. Paul, Lumbermens, Hartford, and Safeco, their attorneys, and their reinsurers, which undermined the truthfulness of their legal opinions and representation.

271. Travelers, St. Paul, Lumbermens, Hartford, and Safeco knowingly agreed to issue bonds which would serve in the place of letters of credit, and would by the terms of the contract with Mahonia, be paid on demand.

(WED) 7. 3'02 18:06/ST. 18:00/NO. 4860925591 P 19
FROM CHASE LEGAL

272. Travelers', St. Paul's, Lumbermens', Hartford's, and Safeco's underwriters knew that they would not pay on demand, but rather seek to mitigate their losses by negotiating performance of the underlying obligations.

273. Travelers, St. Paul, Lumbermens, Hartford, and Safeco did not disclose this information to JPMorgan Chase.

274. Travelers, St. Paul, Lumbermens, Hartford, and Safeco knew that JPMorgan Chase would not have participated in this transaction if JPMorgan Chase had been advised that the defendants did not intend to pay on demand as specified in the forward sale contracts with Mahonia.

275. Travelers, St. Paul, Lumbermens, Hartford, and Safeco knew that JPMorgan Chase had no way of knowing what their intent was in this regard.

276. But for the fraudulent concealments of Travelers, St. Paul, Lumbermens, Hartford, and Safeco, JPMorgan Chase would not have made the payment to Mahonia for the purposes of this Sixth Transaction.

277. Accordingly, Travelers, St. Paul, Lumbermens, Hartford and Safeco are each jointly and severally liable for the losses sustained by JPMorgan Chase as a result of (a) Sixth Transaction; (b) other damages resulting from the defendants' refusal to pay; and (c) punitive damages.

SEVENTH CLAIM FOR RELIEF BY JPMORGAN CHASE, FOR AND ON BEHALF OF MAHONIA, AGAINST ALL DEFENDANTS FOR BREACH OF CONTRACT

278. Plaintiff repeats and realleges paragraphs 1 through 277 as if fully set forth herein.

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FROM CHASE LEGAL

279. Each surety bond written by the defendants in connection with the First through the Sixth Transactions constitutes a valid and binding contract between each defendant, Enron as the principal, and Mahonia as obligee.

280. Each defendant received consideration in the form of premium payments from Enron for undertaking the contractual obligations of the respective surety bonds.

281. Under each surety bond, the respective defendant insurance company, in the event of default by the principal, had an absolute and unconditional obligation to perform by paying the obligee, Mahonia, a Termination Payment as set forth in each surety bond.

282. On December 2, 2001, Enron Natural Gas Marketing Corp. defaulted on its obligations under the prepaid forward contracts guaranteed by each surety bond.

283. On December 2, 2001, Enron Corp. failed to make the Termination Payments under its guarantee agreements.

284. On December 7, 2001, plaintiff JPMorgan Chase, for and on behalf of Mahonia Limited and Mahonia Natural Gas Limited, gave written notice to the defendant insurance companies of amounts which are presently due and owing pursuant to the terms of the surety bonds.

285. On December 6, 2001, counsel for defendant Travelers sent a letter to counsel for plaintiff, demanding various items of information that were not called for under the surety bonds. The letter demanded the information not later than December 11, 2001, and stated that "[t]o the extent that we do not receive the requested information from you on an immediate and timely basis, Travelers may be required to take legal action."

(WED) 7. 3'02 18:06/ST. 18:00/NO. 4860925591 P 21
FROM CHASE LEGAL

286. By letters dated December 6 and 7, 2001, counsel for defendants CNA, Fireman's Fund, Hartford, Liberty, Lumbermens, and Safeco joined in the letter sent by counsel for defendant Travelers.

287. By a letter dated December 7, 2001, counsel for defendant St. Paul demanded various items of information that were not called for under the surety bonds. The letter demanded the information not later than December 12, 2001, and stated that "[t]o the extent that you fail to provide St. Paul with the requested information on a timely basis, St. Paul will be forced to take legal action."

288. By a letter dated December 10, 2001, counsel for defendant Federal demanded various items of information that were not called for under the surety bonds.

289. Mahonia fully satisfied the conditions precedent under the surety bonds by forwarding the respective amounts of prepayments for each prepaid forward transaction, and notifying defendants that the Enron subsidiary had defaulted under the gas contract, that a Termination Payment was due, and that Enron Corp. had defaulted on its guarantee of the Termination Payment, thus triggering defendants' obligations under the bonds.

290. Each defendant insurance company has breached its obligations under the respective surety bonds.

291. As a result of these breaches by the defendant insurance companies, Mahonia was damaged by each defendant in the approximate amounts set forth as follows:

(a)	Liberty Mutual Insurance Company	$25,476,327
(b)	Travelers Casualty & Surety Company	$25,476,327
(c)	St. Paul Fire and Marine Insurance Company	$134,030,366
(d)	Continental Casualty Company/ National Fire Insurance Company of Hartford	$77,880,135

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FROM CHASE LEGAL

(e)	Fireman's Fund Insurance Company	$153,880,135
(f)	Safeco Insurance Company of America	$55,356,350
(g)	The Travelers Indemnity Company	$240,481,616
(h)	Federal Insurance Company	$183,602,433
(i)	Hartford Fire Insurance Company	$40,836,532
(j)	Lumbermens Mutual Casualty	$156,150,231

WHEREFORE, Plaintiff JPMorgan Chase Bank, for itself, and for and on behalf of Mahonia Limited and Mahonia Natural Gas Limited, seeks judgment against the defendants as follows:

(1) That defendants have breached their contracts with Mahonia Limited and Mahonia Natural Gas Limited in the First through the Sixth Transactions, and are liable to Mahonia Limited and Mahonia Natural Gas Ltd. in the amounts stated herein, plus interest;

(2) That each of the defendants are jointly and severally liable to JPMorgan Chase on account of their fraudulent concealment in the amount, plus interest, as described in the claims herein;

(WED) 7. 3'02 18:07/ST. 18:00/NO. 4860925591 P 23
FROM CHASE LEGAL

(3) Granting plaintiff its attorney's fees, and the costs and disbursements of this action; and

(4) Awarding punitive damages, and such other and further relief as the Court may find just and proper.

Dated: New York, New York
June 28, 2002

KELLEY DRYE & WARREN LLP

By: _____

John M. Callagy (JC 8166)
William A. Escobar (WE 8146)
Steven P. Caley (SC 4236)
Neil M. Merkl (NM 6704)

101 Park Avenue
New York, NY 10178

Attorneys for Plaintiff JPMorgan Chase Bank for itself, and for and on behalf of Mahonia Limited and Mahonia Natural Gas Limited

Of Counsel

William H. McDavid
Mark E. Segall
Lawrence N. Chanen
JPMorgan Chase Bank Legal Department
One Chase Manhattan Plaza
26th Floor
New York, New York 10081

(WED) 7. 3'02 18:07/ST. 18:00/NO. 4860925591 P 24
FROM CHASE LEGAL

James D. McMahon
Vice President

GeneralCologne Re.

To: Jack Ruby
Charles Lucky
FYI - Gen Re's letter to Gerry
on "Credit Enhancement"
Rana
11/20/00

November 20, 2000

Mr. Gerardo G. Maurtz
Senior Vice President
Chubb & Son Inc.
15 Mountain View Road
Warren, NJ 07060

Re: Credit Enhancement

Dear Gerry:

Thank you for taking the time to see Rich Patronik and me last week. Rana and you asked that we reconsider our position on Advance Payment Bonds as part of Future Flow Securitizations. We discussed this business again with the appropriate people here at General Re and would like to articulate the basis of our position. We are open to continued dialog, but at this time we recommend against putting this business in the surety treaty.

We are all aware of the convergence of financial and insurance markets. We believe that traditional insurers are moving into the financial guarantee arena in a substantial way. The financial markets and certain hybrid insurance/financial product brokers have been very creative in packaging "insurance products" that have many of the characteristics of credit enhancement or financial guarantee obligations. A number of the larger surety operations are involved in these deals.

Example Future Flow Securitizations:

For example, "Future Flow Securitizations" take many forms outside the United States, but within the US we generally see the "Advance Payment Surety Bond" format as part of a financing vehicle in which the surety bond is the key risk bearing component of the debt issuing entity. These structures allow debt issuers to leverage the value of future receivables through complex securitization transactions where the supply of some commodity (natural gas, oil, etc.) is guaranteed by a surety bond. It seems the predominant purpose for future flow transactions is to raise low cost capital that does not show up as a loan on the borrower's balance sheet. In the event of default the surety must pay on demand the value of the outstanding debt balance.

General Reinsurance Corporation
Financial Centre, 695 East Main Street, Stamford, CT 06901
Tel. 203 328 5531, Fax 203 328 5880
jdmcmahon@gcre.com, www.gcre.com

FROM CHASE LEGAL (WED) 7. 3'02 18:07/ST. 18:00/NO. 4860925591 P 25

Traditional Advance Payment Bonds:

Future flow securitization surety bonds should not be confused with traditional advance payment bonds which are covered by most surety treaties. Our perception is that traditional advance payment bonds cover a low percentage (10% to 25%) of the contract price for relatively short term delivery of goods or services (turbine for power plant, steel for an oil rig, etc). Certainly there are some pay on demand advance payment bonds, but there also seem to be other remedies available to the surety to mitigate the cost of a claim in the event of default.

Acceleration Risk:

Hybrid advance payment bonds when issued as part of a future flow securitization have characteristics that are closer to financial guarantee than traditional advance payment bonds. One of the key differences is that they seem to have only one remedy, which is to pay the outstanding balance of the debt instrument on demand in the event of default; i.e: The obligee is instantly made "whole" and the surety is left to accept payments over time, assuming the principal remains viable. We view these hybrid deals as falling somewhere between traditional pay on demand surety business and monoline financial guarantee. These deals appear to break a cardinal rule in the monoline financial guarantee world, which is to write the business in such a way that they avoid acceleration payments of the underlying debt. Monolines almost always structure deals to provide the option of making scheduled payments of interest and/or principal instead of acceleration of the underlying debt (typical PML estimates are 24 to 36 month interest payments). This key strategy is employed to 1) avoid a call on full principal on short notice that could strain liquidity resources; 2) allow the insurer flexibility to manage the work-out of a trouble situation; 3) reflect the common knowledge that the ultimate loss will be reduced (or eliminated) if the potential work-out period is extended. Sureties can still get the advantage of longer work-outs if they have good rights of subrogation under the indemnity agreement, but the potential call on resources involved with pay on demand for the full outstanding balance would still be high and on short notice.

FROM CHASE LEGAL (WED) 7. 9'02 18:07/ST. 18:00/NO. 4860925591 P 26

Example Structure:

Attached is an example future flow structure and your current future flow portfolio and pricing comparison to illustrate our perception. The diagram shows a typical structure, which to us seems complex. The basic idea is that credit enhanced debt is sold to investors and the debt is retired with proceeds from the sale of some commodity. The cash is used by the borrower, in this case a utility, for general corporate purposes. The surety is a senior unsecured creditor in most cases.

Pricing:

Monoline wrapped obligations do not trade like real Aaa's, which is reflected in prices charged by financial guarantee insurers. The attached spreadsheet shows the Chubb future flow portfolio and gives a pricing example on REDACTED As an example of the value of credit enhancement, we looked at REDACTED spreads on enhanced and unenhanced debt issues with similar duration REDACTED and REDACTED The market fluctuates, but at this time the credit enhancement is worth REDACTED BPPS per annum to the market. Theoretically the maximum price a financial guarantor can charge is the difference between market value of identical credit enhanced debt and the market value of unenhanced debt. This quite reasonably could highlight the question of whether the debt insurers are getting arbitraged by financial markets. We believe bond insurer pricing is at least twice the surety pricing in the attached spreadsheet. Beyond apparent below market pricing by the surety, sureties appear to take additional volatility risk through the acceleration payment of the outstanding debt. We conclude that the surety is taking on risk at well below market price and has substantial additional exposure when compared to financial guarantee insurers, a combination that we feel will eventually cause severe loss.

Reinsurance Limits:

We believe you have approximately REDACTED treaty reinsurance capacity per principal. These treaties attach on a per principal basis, therefore, the notional exposure for each bond per principal must be added together; it appears your exposures are well in excess of treaty limits (over REDACTED for REDACTED. We believe the initial PML will be REDACTED of the outstanding debt balance. The surety

FROM CHASE LEGAL (WED) 7. 3'02 18:08/ST. 18:00/NO. 4860925591 P 27

will have a claim against the REDACTED REDACTED REDACTED Even if recovery is available down the road, the surety will take an immediate hit from the pay on demand instruments. Quarterly EPS can be gravely impacted.

Credit Enhancement Strategy:

Beyond the pure pricing issue, we feel that a rational approach to this business requires more than traditional surety underwriting. At this point we are not saying that we will not support this class of business, but rather we feel it will be to our mutual benefit to discuss these opportunities on a case by case basis. Underwriting, pricing, portfolio management and limits management are among the areas that we should be working on together to assure a rational use of our capacity and capital. We certainly feel that any credit enhancement obligation such as the above described advance payment bonds, certain lease guarantees or other credit enhancement of debt in an insurance wrapper should be subject to further discussion on a case by case.

Obviously as a reinsurer we are not on the front lines of this type product development and we have much to learn. We are very much interested in your observations on this subject.

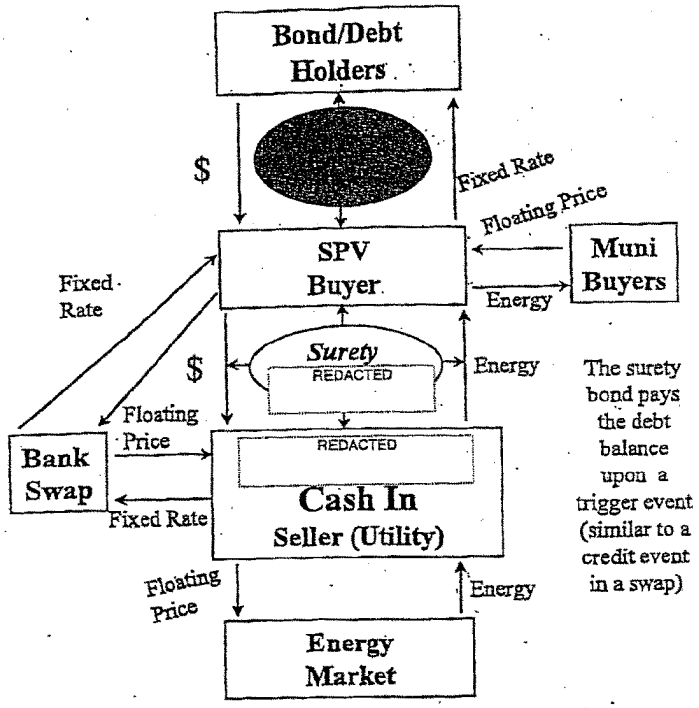
Kind regards,

James D. McMahon

cc: Rana Nikpour

FROM CHASE LEGAL (WED) 7. 3'02 18:08/ST. 18:00/NO. 4860925591 P 28

11/20/00 18:17 FAX 203 328 5880 PORTFOLIO/TREATY 005



Advance Payment Surety Bond

$ Motivation - Seller (Utility) gets cheap working capital - credit enhanced by the surety

HIGHLY CONFIDENTIAL
FED0040
FROM CHASE LEGAL
(WED) 7. 3'02 18:08/ST. 18:00/NO. 4860923591 P 29

Chubb Advance Payment Bond Exposure
REDACTED
REDACTED
REDACTED

Kemper.
Insurance Companies

To: Brian Schmalz

From: James Crinnion

Date: April 26, 2001

Subject: Financial Guarantee Audit for the Commercial book of Kemper Surety

Account

Enron Corporation is an account written out of our Dallas office. Enron is one of the world's largest integrated natural gas and electricity companies. Enron is broken up into 4 main groups. They groups are, Exploration and Production, the Gas Pipeline Group, Wholesale Energy Operations and Retail Energy Services.

Enron is written out of our Dallas office. Mike Davis is the lead underwriter for this account.

Bonded Obligation

Kemper has a total of 3 bonds outstanding for Enron Corporation. Two advance payment bonds, one of them is for $100MM and the other is $72.6MM. The obligee for both advance payment bonds is Mahonia Ltd. The first Natural Gas Inventory Forward Sale Contract between Enron and Mahonia Ltd. was signed on June 28, 2000. It was a $400MM contract and Kemper took 25% of the liability. The $100MM in liability is on bond #001825. The second contract was signed 6 months later in December 2000. It was worth $330MM. On this deal Kemper took 22% or $72.6MM. (Bond #970483) In both cases Mahonia Ltd. paid a fixed amount of money up front in return for a set supply of natural gas over a period of time. In consideration of receiving all of the money up front, Enron, as principal has put up a bond to Mahonia guaranteeing the supply of natural gas per the contract. Both of these bonds are identical in terms of language, and both are on-demand type instruments. The sureties on both of the bonds have 10 days after receipt of a written notice of claim to make a payment to the obligee. The language surrounding this term on the bond is very onerous and waives some of the standard defenses sureties normally employ during a claims process.

On both of these bonds, the aggregate liability of each surety declines each month as the gas is delivered. Both bonds have their respective reduction schedule attached to the back of them. As of today (4/30/01) both bonds are still at their maximum liability. Bond #970483 will begin decreasing in June with full runoff to be complete on 1/1/06. Bond #001825 will not begin to decrease in liability until January 2003, with full runoff to be

LMB-000146

FROM CHASE LEGAL (WED) 7. 3'02 18:09/ST. 18:00/NO. 4860925591 P 31

JPMorgan Chase Bank v. Liberty Mutual Insurance Co., et. al.

01 Civ. 11523 (JSR)

PAGE 2 TO EXHIBIT "G" ANNEXED TO THE AMENDED COMPLAINT, DATED JUNE 28, 2002, HAS BEEN FILED WITH THE COURT UNDER SEAL, PURSUANT TO THE PROTECTIVE ORDER ENTERED ON MAY 6, 2002

FROM CHASE LEGAL (WED) 7. 3'02 18:09/ST. 18:00/NO. 4860925591 P 32

out completely with all of the pertinent information. The 12/31/00 annual review needs to be completed on this account.

Summary
From all accounts Enron is a large enough account with a strong balance sheet, cash flow and available credit facilities to warrant Kemper to issue such onerous bonds. The two advance payment bonds are financial guarantees despite their performance obligation to supply natural gas. The sole obligation of the last bond is to guarantee a premium payment if Enron fails to do so. All three bonds have a very long tail of liability with very short turn around times to pay a claim. The bond's language implies that they are very hard, if not impossible to cancel. Based on Enron's financial strength I would recommend these long tail financial guarantees as an acceptable risk on a going forward basis. The bonds themselves are very onerous in nature and I would not recommend that we write these types of obligations in the future unless they are for one of the financially strongest companies in their respective industry.

Financial Guarantee
Based upon my understanding of what Kemper's reinsurer's current views on financial guarantee obligations, these bonds would fall into their category of a financial guarantee. All three bond's language reads more like an LOC with an 8 or 10-day demand clause. It is my understanding of the reinsurer's position, that despite Enron's size and stature within its industry, we should avoid writing these types of obligations in the future.

Follow up Questions
None at this time...

Additional Comments: Overall Enron is a good credit risk and qualifies financially for the o/s exposure. Also, once delivery of natural gas under the contracts begin, the liability decreases consistently from month to month.

The two issues are price relative to risk and capacity, and reinsurance acceptance. In general, rates for a well heeled principal on this class are too cheap. We simply cannot charge enough to support our u/w risk, particularly given the size and term of the obligations Kemper's future appetite on this class will be limited to qualified accounts for which we can charge appropriate rates.

Based on notes in the file, Kemper discussed the risk with reinsurers prior to writing any bonds. An early underwriting memo indicates reinsurers had no objections. It is my understanding that Swiss Re participates in similar transactions on a direct basis in its special

FROM CHASE LEGAL (WED) 7. 3'02 18:09/ST. 18:00/NO. 4860925591 P 33

risk division. A valid concern from the reinsurance perspective is the aggregate market capacity. If each transaction is several $100mm, requiring participation of several sureties, and Enron enters into many transactions, any reinsurer can find it has much more exposure than it desires. We share the responsibility to help insurers manage their exposure when entering into shared accounts. MKWeissbaum, 5/2/01

FROM CHASE LEGAL (WED) 7. 3'02 18:10/ST. 18:00/NO. 4860925591 P 34

LIBERTY BOND SERVICES

INTEROFFICE MEMO

Date: November 19, 1998

To: Chehab Chehab & John Duffy, LBS New York

From: Randy Calhoun, LBS-Dallas

Phone: (972) 233-6078

Subject: Enron Corp. ("Enron")

I have declined LBS' participation in the estimated $250MM "Mahonia" bond that we have been discussing over the past several days. As you know, we have been told that the bond is required by 11/30/98 although additional detail has not yet been forthcoming. Nevertheless, Phil Bair confirmed that the bond is a "go". He reports that the other four sureties participating on the previous Mahonia bond have all indicated their willingness to provide Enron with credit on the upcoming bond as well. He has also indicated that each of these sureties would be willing to accept the entire $250MM risk without other co-surety participation.

I have explained to Phil that all concerned hope that our declination on this single transaction will be followed by continuing involvement on similar future Enron and subsidiary credit needs of this type. My explanation for our inability to go forward with this particular bond request included the following:

- LBS' increasing awareness and scrutiny of ALL large financial guarantee type transactions born of "irregular" underwriting issues, including, but not limited to: cross default and negative pledge provisions (either directly in the bond or in the account's debt instruments and/or credit agreements); objectionable bond requirements (i.e. bond default caused by a decline in Liberty Mutual's credit rating); objectionably worded attorney "opinion" letters and possible "Appleton" law violations.

- Our need to explore the possibility of obtaining a "pari passu" position equal to Enron's most restrictive, unsecured creditor (Phil and I have previously discussed this underwriting philosophy and he agrees with our approach. He does however, rightfully question the commercial viability of our actions relative to other LBS (domestic) accounts of Enron's creditworthiness and in the context of what other sureties appear to be willing to do without similar indemnity protections).

LIB-004544

M CHASE LEGAL (WED) 7. 3'02 18:10/ST. 18:00/NO. 4860925591 P 35

- The unfortunate timing of this bond request in relation to LBS' changed/changing underwriting approach on these transactions together with our continuing inability to provide him with alternative dates following our request for an imminent meeting with Enron (we were all aware of another Mahonia transaction in the fourth quarter of this year at the time of the 9/29 execution of the most recent Mahonia bond).

- The need to introduce LBS' Chief Underwriter to the account in conjunction with his as well as all of our need to gain greater confidence in our understanding of certain underwriting considerations, generally. This point is emphasized in association with Enron's rapidly escalating surety needs and our understanding of the account's intention to take further advantage of surety products in lieu of its own banking facilities.

Phil has requested that we provide him with a written response outlining the indemnity issues that we believe we must have to support future Mahonia-like transactions. Reiterating, he supports the thought process behind our needs in this area. He would like to present our request to Enron for their review prior to our actual visit with the account. For this purpose, I must rely upon you and/or SLD. Once we have furnished these indemnity needs to Phil, he will attempt to "sell" our position to Enron, at least for purposes of continuing dialog with LBS. At the time of delivery, Phil will also encourage Enron to seriously consider the merits of our needs and the importance of retaining relations with LBS.

Like us, Phil understands the risk to both his and our future as a result of his recommending that Enron provide LBS with a more secure indemnity arrangement. Clearly, the competitive marketplace will work aggressively against us on this. In this regard, I feel fortunate that we have him representing our collective interests.

Please help me to keep our chances of account retention alive by expediting the requested indemnity wording. I am sure you agree with me that it is vitally important we move quickly on this given the unfortunate events of the past few days and weeks.

[redacted]

JPM CHASE LEGAL (WED) 7. 3'02 18:10/ST. 18:00/NO. 4860925591 P 36

ADVANCE PAYMENT SUPPLY SURETY BOND

Principal: Enron Natural Gas Marketing Corp.

Sureties: Liberty Mutual and Travelers

Penal Sum $250MM - shall not be cumulative and shall be reduced automatically and permanently from time to time in accordance with the attached exhibit A. In no event shall the sureties aggregate liability exceed the Monthly Maximum Penal Sum in effect at the time the surety bond written notice attached hereto as exhibit B is received pursuant to this bond.

Covers Natural Gas Inventory Forward Sale Contract and the prepaid price paid by Mahonia to Enron

Sureties have agreed to be severally and not jointly liable under this bond and the maximum liability of each surety is limited to 50% of the total bond exposure.

Condition precedent to any right of recovery that obligee or Chase Manhattan Bank on behalf of the obligee provide written notice that represents

a) Termination Payment is due under the terms of the agreement and state the unpaid amount of such termination payment

b) Enron Marketing has not made termination payment in full

c) Enron has not made such payment in accordance with the terms of the guarantee agreement

d) payment from the surety is due within 10 days after receipt of written notice from each surety up to their % interest of the lesser 1) the unpaid amount of such termination payment or 2) the monthly Maximum penal sum in effect at the time the written notice is received. Demand Instrument

Paragraph 7 basically states that surety has to perform under the bond irrespective of the value, validity or enforceability of the obligations of the Principal under the agreement or Enron under the Guaranty Agreement - Basically sureties waive all defenses Clear we have no outs

Paragraph 8 (i)time for performance of or compliance with any provision of the agreement shall be waived, extended or renewed. Concern we could get extended out past original completion date. (ii) any of the provisions of the agreement or the guarantee agreement or any other agreement can be modified. Creates some concern over contractual risk

Paragraph 10: Subject to the laws of the State of New York

paragraph 12 Each sureties liability under this bond shall cease on such surety payment pursuant to the written notice on or before 5PM NYC time, 7-31-2002, or if the written notice has not been received on or Expiration Date on the Expiration Date

FROM CHASE LEGAL TRV-003120
(WED) 7. 3'02 18:10/ST. 18:00/NO. 4860925591 P 3/

JOSEPH I. LIEBERMAN, CONNECTICUT, CHAIRMAN

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JOYCE A. RECHTSCHAFFEN, STAFF DIRECTOR AND COUNSEL
RICHARD A. HERTLING, MINORITY STAFF DIRECTOR

United States Senate

COMMITTEE ON
GOVERNMENTAL AFFAIRS
WASHINGTON, DC 20510–6250

July 9, 2002

Ms. Ahuva Genack, Esquire
Vice President and Assistant General Counsel
Legal Department
J.P. Morgan Chase & Co.
Floor 26
One Chase Manhattan Plaza
New York, NY 10081

Via Fax at 212-552-1295

Dear Ahuva:

There are a number of additional facts that the Subcommittee needs to obtain before our hearing on July 23. Please provide the following:

A list of all prepay transactions J.P. Morgan Chase entered into with Enron. Provide the name of the transaction, date, commodity, and amount of each transaction. Furthermore, provide the total amount of fees that J.P. Morgan Chase earned in connection with each transaction, including, but not limited to, up-front structuring and arrangement fees and the implied interest rate earned on each transaction.

Does J.P. Morgan Chase pay all fees associated with Mahonia Ltd. and Mahonia Natural Gas Ltd. (Mahonia)? Does J.P. Morgan Chase pay any fees or costs for the administration or management of Mahonia to Mourant du Feu & Jeune, separate from fees related to specific transactions Mahonia enters into with J. P. Morgan Chase?

The official position, title, and department (group, division, etc.) of J.P. Morgan Chase that the following individuals work for currently (as of July 2002) and worked for during the period(s) indicated next to the individual's name:

A. Richard S. Walker (November 1998 and June 1999)
B. Jeffery W. Dellapina (November 1998 and June 1999)
C. Bob Mertensotto (June 1999)
D. Robert Traband (June 1999)
E. Christopher Wardell (June 1999)
F. Dinsa Mehta (June 1999)
G. George Serice (November 1998)
H. Karen Simon (November 1998)

Permanent Subcommittee on Investigations
EXHIBIT #185p

Please contact me if you have any questions and to schedule the call with Mr. Levy (202-224-9505). Thank you for your assistance.

Sincerely,

Bob Roach

Bob Roach

CHASE LEGAL

JPMorganChase

One Chase Manhattan Plaza, 26th Floor
New York, New York 10081
Tel 212-552-0918
Fax 212-552-1295
Ahuva.Genack@chase.com

Ahuva Genack
Assistant General Counsel

TELECOPIER TRANSMITTAL SHEET

DELIVER TO: Ross K. Kirschner
Permanent Subcommittee on Investigations

FAX NO(S).: 202-224-1972

DATE: July 18, 2002

RE: **Please see attached**

MESSAGE:

Attached is a copy of the J.P. Morgan Chase officers' names and their titles, as well as the transaction information you inquired about.

PAGES INCLUDING THIS COVER SHEET: 3

IF YOU DO NOT RECEIVE ALL THE PAGES, PLEASE CALL BACK AS SOON AS POSSIBLE AT (212) 552-0512.

Confidentiality Note

The information contained in this facsimile message is legally privileged and confidential information intended only for the use of the individual or entity named above. If the reader of this message is not the intended recipient, you are hereby notified that any dissemination, distribution or copy of this telecopy is strictly prohibited. If you have received this telecopy in error, please immediately notify us by telephone and return the original message to us at the address above via the United States Postal Service. Thank you.

J.P.Morgan Chase Employees

The current (as of July 2002) and past positions, titles and departments of certain individuals working for J.P.Morgan Chase are as follows:

A. Richard S. Walker currently serves as Managing Director, Investment Banking, Client Management group. this is the same position he held in November of 1998 and June of 1999.

B. Jeffrey W. Dellapina currently serves as Managing Director, Investment Banking, Credit & Rate Markets, NY Energy Derivatives Marketing group. He served as Vice President of this group in November of 1998 and June of 1999.

C. Bob Mertensotto currently serves as Managing Director, Corporate Banking, Global Credit Management, Oil and Gas group, the same position he held in June 1999.

D. Robert Traband currently serves as Vice President, Corporate Banking, Oil & Gas group. He held the same position in June of 1999.

E. Christopher Wardell currently serves as Managing Director, Deputy General Credit Officer, North America Corporate Credit and Middle Market Corporate Credit groups. In June of 1999, he served as Managing Director, Group Credit Executive, North America Corporate Credit group.

F. Dinsa Mehta currently serves as Managing Director, Credit & Rates Market, Global Commodities and FX Options group. He held the same position in June of 1999.

G. George Serice currently serves as Vice President, Investment Banking, Corporate Solutions group. In June of 1999, he served as Vice President, Investment Banking, Global Syndication Finance group.

H. Karen Simon currently serves as Managing Director, Investment Banking, Credit & Rate Markets, Global Syndication Finance group.

FROM CHASE LEGAL

Date	Amount
Dec. 1997	$ 6,028,000
June 1998	48,541,454
Dec. 1998	85,360,508
June 1999	298,012,165
June 2000	519,603,740
Dec. 2000	255,228,323
Sept. 2001	176,000,000

Ahuva Genack
Vice President and
Assistant General Counsel
Legal Department

July 22, 2002

Via Facsimile (202-224-1972)

Robert L. Roach, Esq.
Counsel & Chief Investigator
Permanent Subcommittee on Investigations
United States Senate
199 Russell Building
Washington, DC 20510

Dear Mr. Roach:

In response to your inquiry, dated July 9, 2002, we are providing information pertaining to J.P.Morgan Chase's ("JPMC") relationship with Enron, Mahonia Limited and Mahonia Natural Gas Ltd. in connection with certain natural gas and crude oil transactions. While we believe this information is substantially accurate, given the time frame you designed for a response, we did not have an opportunity fully to review our files.

Prepay Transaction Details

While J.P.Morgan Chase did not enter into any prepaid transactions with any Enron entity, I assume that you are requesting information involving prepaid transactions involving Mahonia Limited and Mahonia Natural Gas Ltd. (collectively, Mahonia), JPMC and an Enron entity. Attached herewith is a chart addressing available information for prepaid transactions involving JPMC, Mahonia and Enron. Please note that the fees indicated do not include an "implied interest rate" earned on each transaction. We are in the process of determining the number of basis points JPMC earned on each financing and will provide you with such information as soon as it is available. Further, the 1992 prepaid transaction involved Stoneville Aegean Limited rather than a Mahonia entity and we have included the information for your convenience.

JPMC's Payment of Fees Associated with Mahonia Entities

Based on the information currently available, we believe that JPMC made payments to Mourant du Feu & Jeune for the administration of Mahonia. In addition, JPMC paid the following:

- Mahonia's annual Jersey statutory charges,
- Mourant & Co.'s fee for administrative services related to each transaction, and
- Mourant du Feu & Jeune's legal fee for providing the legal opinion for each transaction.

J.P. Morgan Chase & Co. • One Chase Manhattan Plaza, Floor 26, New York, NY 10081
Telephone: 212 552 0918 • Facsimile: 212 552 1295
ahuva.genack@chase.com

JPMC Employees

The current (as of July 2002) and past positions, titles and departments of certain individuals working for JPMC are as follows:

A. Richard S. Walker currently serves as Managing Director, Investment Banking, Client Management group. This is the same position he held in November of 1998 and June of 1999.

B. Jeffrey W. Dellapina currently serves as Managing Director, Investment Banking, Credit & Rate Markets, NY Energy Derivatives Marketing group. He served as Vice President of this group in November of 1998 and June of 1999.

C. Bob Mertensotto currently serves as Managing Director, Corporate Banking, Global Credit Management, Oil and Gas group, the same position he held in June 1999.

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H. Karen Simon currently serves as Managing Director, Investment Banking, Credit & Rate Markets, Global Syndication Finance group.

Please call me if you have any questions regarding any of the information provided.

Sincerely,

Ahuva Genack/dch

Ahuva Genack, Esq.

AG/dch
Enclosure

103290:v01

Details of Prepaid Transactions Involving Enron

12/21/92	Swap Transaction between Stoneville Aegean Limited and Chase Manhattan Bank	Crude Oil	Transaction value = $76,126,754[3]	$1,000,000
	Forward Sale Contract between Enron Reserve Acquisition Corp. and Stoneville Aegean Limited	Crude Oil	Transaction value = $75,090,054 Quantity = 3,870,000 barrels	
06/24/93	Commodity Swap Transaction between Mahonia Limited and Chase Manhattan Bank	Crude Oil	Transaction Value = $230,006,022	Not available
	Inventory Forward Sale Contract between Enron Hydrocarbons Marketing Corp. and Mahonia Limited	Crude Oil	Transaction value = $230,006,022 Quantity = 12,100,000 barrels	
12/13/94	Inventory Forward Sale Contract between Enron Hydrocarbons Marketing Corp. and Mahonia Limited	Crude Oil	Transaction value = $213,[8]56,050[4] Quantity = Not available	Not available

1 Includes transaction value and amount of commodity to be delivered. Derived from confirmations of the forward sale contracts unless otherwise indicated.

2 Referring to fees paid to J.P.Morgan Chase.

3 Value determined by Notice of Execution pursuant to Master Forward and Protection Agreement.

4 Bracketed number is not clear on confirmation.

09/26/95	Commodity Swap Transaction between Mahonia Limited and Chase Manhattan Bank	Natural Gas	Transaction value = $224,440,450	$729,431[5]
	Inventory Forward Sale Contract between Enron Natural Gas Marketing Corp. and Mahonia Limited	Natural Gas	Transaction value = $224,440,450 Quantity = Not available	
12/16/96	Credit Agreement between Mahonia Limited and Chase Manhattan Bank		Transaction value = $350,000,000	Not available[6]
	Inventory Forward Sale Contract between Enron Natural Gas Marketing Corp. and Mahonia Limited	Natural Gas	Transaction value = $225,021,380 Quantity = 111,900,000 mmbtus	
	Inventory Forward Sale Contract between Enron Natural Gas Marketing Corp. and Mahonia Limited	Crude Oil	Transaction value = $124,986,595 Quantity = 6,963,000 barrels	

1095

[5] No fee letter for this transaction is available. However, this arrangement fee was referenced in Mahonia Limited's account debit authorization letter, dated 09/29/95.

[6] A fee letter is not available for this transaction. However, there is an arrangement fee for a Performance Letter of Credit (PLC) issued by Chase Securities Inc. in connection with transaction in an amount equal to 35 basis points on the PLC amount of $350,000,000.

12/18/97	Forward Sale Contract between Mahonia Limited and Chase Manhattan Bank	Natural Gas	Transaction value = $300,004,179 Quantity = 157,665,000 mmbtus	$750,000
	Inventory Forward Sale Contract between Enron Natural Gas Marketing Corp. and Mahonia Limited	Natural Gas	Transaction value = $299,991,679 Quantity = 157,665,000 mmbtus	
06/26/98	Forward Sale Contract between Mahonia Limited and Chase Manhattan Bank	Natural Gas	Transaction value = $250,012,500 Quantity = 123,210,000 mmbtus	$625,000
	Inventory Forward Sale Contract between Enron Natural Gas Marketing Corp. and Mahonia Limited	Natural Gas	Transaction value = $250,000,000 Quantity = 123,210,000 mmbtus	
12/01/98	Forward Sale Contract between Mahonia Limited and Chase Manhattan Bank	Crude Oil	Transaction value = $250,006,852 Quantity = 17,595,000 barrels	$625,000
	Inventory Forward Sale Contract between Enron Natural Gas Marketing Corp. and Mahonia Limited	Crude Oil	Transaction value = $249,994,352 Quantity = 17,595,000 barrels	

06/28/99	Forward Sale Contract between Mahonia Limited and Chase Manhattan Bank	Natural Gas	Transaction value = $500,007,500 Quantity = 242,900,000 mmbtus	$1,250,000
	Inventory Forward Sale Contract between Enron Natural Gas Marketing Corp. and Mahonia Limited	Natural Gas	Transaction value = $499,999,986 Quantity = 242,900,000 mmbtus	
06/28/00	Forward Sale Contract between Mahonia Limited and Chase Manhattan Bank	Natural Gas	Transaction value = $650,004,352 Quantity = 264,211,000 mmbtus	$1,625,000
	Inventory Forward Sale Contract between Enron North America Corp. and Mahonia Limited	Natural Gas	Transaction value = $649,999,352 Quantity = 264,211,000 mmbtus	
12/28/00	Assignment Agreement between Mahonia Natural Gas Limited and Chase Manhattan Bank and Fleet National Bank	Natural Gas	Transaction value = $330,403,325[7] Quantity = 95,146,900 mmbtus	$1,072,500
	Inventory Forward Sale Contract between Enron North America Corp. and Mahonia Natural Gas Limited	Natural Gas	Transaction value = $330,403,325 Quantity = 95,146,900 mmbtus	

[7] Chase Manhattan Bank's portion of the Assignment Agreement purchase price was 50%, totaling $165,201,663. Chase Manhattan Bank entered into a Natural Gas Offtake Agreement and Assignment Agreement with Fleet National Bank for Fleet's remaining 50% of the assigned commodity.

1097

09/28/01[8]	Commodity Swap Transaction between Mahonia Limited and Chase Manhattan Bank	None	Transaction value = $350,000,000	$1,000,000
	Swap Transaction between Enron North America Corp. and Mahonia Limited	None	Transaction value = $350,000,000	

[8] This was a financially settled swap transaction and, therefore, no physical settlement.

1098

JPMorganChase

Ahuva Genack
Vice President and
Assistant General Counsel
Legal Department

July 18, 2002

By Facsimile Transmission

Robert L. Roach, Esq.
Counsel & Chief Investigator
Permanent Subcommittee on Investigations
United States Senate
199 Russell Building
Washington, DC 20510

Dear Mr. Roach:

I am writing in response to the Subcommittee's subpoena dated July 2, 2002.

The names of J.P. Morgan Chase & Co. ("JPMC") clients or counterparties that engaged in commodity prepaid forward transactions with a special purpose vehicle ("SPV"), the identity of the SPV, the number of transaction that each entity entered into with the SPV, and whether the entity entered into a swap with JPMC are as follows:

Client	Number of Responsive Transactions	SPV	Swap w/JPMC For Equal or Partial Volumes
Columbia Natural Resources Inc.	2	Mahonia II. Ltd.	No
Crystal Oil Company	1	Mahonia Ltd.	No
Metallgesellschaft Corp.	1	Mahonia Ltd.	Yes
Occidental Petroleum Company	1	Mahonia Ltd.	Yes
Ocean Energy Inc.	1	Mahonia Ltd.	No
Santa Fe Snyder Corp.	2	Mahonia Ltd.	No
Tom Brown Inc.	1	Mahonia Ltd.	No

This response is based on information currently available. Should we determine that there are any additional clients or counterparties that entered into transactions described in the subpoena we will so notify you.

Very truly yours,

AG:mh

J.P. Morgan Chase & Co. - One Chase Manhattan Plaza, Floor 26, New York, NY 10081
Telephone: 212 552 0918 - Facsimile: 212 552 1295
ahuva.genack@chase.com

103288:v01

Permanent Subcommittee on Investigations
EXHIBIT #185q

JOSEPH I. LIEBERMAN, CONNECTICUT, CHAIRMAN

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SUSAN M. COLLINS, MAINE
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JIM BUNNING, KENTUCKY

JOYCE A. RECHTSCHAFFEN, STAFF DIRECTOR AND COUNSEL
HANNAH S. SISTARE, MINORITY STAFF DIRECTOR AND COUNSEL

United States Senate
COMMITTEE ON
GOVERNMENTAL AFFAIRS
WASHINGTON, DC 20510-6250

July 25, 2002

Mr. William B. Harrison, Jr.
President and Chief Executive Officer
J.P. Morgan Chase & Co.
270 Park Avenue
New York, N.Y. 10017

Dear Mr. Harrison:

Earlier this week the Permanent Subcommittee on Investigations held a hearing on the role of financial institutions like yours in the collapse of the Enron Corporation. One of the very troubling factual issues that emerged was Chase's use of a Special Purpose Vehicle (SPV), Mahonia, Ltd. (and its successors), as a pass-through entity established in Jersey for Enron's "prepays" in which Chase participated. Documents the Subcommittee obtained show that Chase directed its agent, the law firm of Mourant du Feu & Jeune, to establish an SPV in Jersey that would be "controlled by Chase" but not "wholly owned" by Chase and that to accomplish this, Chase wanted to establish a charitable trust that would own a holding company that would own the SPV. Chase witnesses told us that Chase neither owns or controls Mahonia despite the documents presented at the hearing and the statements of the witnesses that Chase pays Mahonia's attorney fees and all costs associated with the administration of Mahonia, that Mahonia has not entered into a commercial transaction that did not involve Chase, and that Chase served as Mahonia's agent on all of the prepays in which Chase and Mahonia were involved.

We ask that you, personally, no later than 12 P.M. Monday afternoon, July 29th: 1) answer the following questions on behalf of Chase under oath and return them to the Subcommittee office, SR-199; and 2) instruct/direct your agents, attorneys and all other parties responsible for the formation, operation, administration or management of Mahonia Limited, Mahonia II Limited, and Mahonia Natural Gas Limited (collectively called "Mahonia") (including but not limited to Mourant du Feu & Jeune, Mourant & Co. Trustees Limited, Mourant & Co., Eastmoss Limited, The Eastmoss Trust, Juris Limited, Lively Limited, and all entities that have a beneficial or controlling interest in, or agency relationship with, Delta) to make available to the Subcommittee all documents related to the ownership, formation, operation, administration or management of Mahonia, and all documents that address or indicate Chase's relationship to Mahonia.

QUESTIONS: (Please note that any reference to Chase is intended to include any entity related to Chase or Chase's agent.)

1) Did Chase establish Mahonia and, if so, when, for what purpose and why in Jersey?

Permanent Subcommittee on Investigations
EXHIBIT #185r

2) Does Chase own Mahonia, and if it doesn't, who does?

3) If the owner of Mahonia is a charitable trust, does Chase own the charitable trust, and if it doesn't, who does?

4) Who serves on the Board of Directors of Mahonia and the entity that owns Mahonia?

5) Who is the agent for Mahonia and who is the agent for the entity that owns Mahonia?

6) Does Chase pay for: Mahonia's administrative fees? Registration fees? Attorney fees? Transactions fees?

7) When a non-Chase entity does business with Mahonia, with whom does the entity conduct the negotiations -- a Chase employee or a Mahonia employee?

8) What obligations do any of the attorneys, trustees, administrators, directors, or beneficial owners of Mahonia have to Chase with respect to Mahonia and separate and apart from Mahonia?

9) Does Chase effectively control Mahonia?

If you have any questions about this request, please contact either or us or have your staff contact Robert Roach, Counsel and Chief Investigator of the Subcommittee at 202-224-9505.

Sincerely,

Susan Collins
Ranking Member

Carl Levin
Chairman

Permanent Subcommittee on Investigations

CL:ljg

William B. Harrison, Jr.
Chairman and Chief Executive Officer

July 29, 2002

VIA FEDERAL EXPRESS & FACSIMILE

The Honorable Carl Levin
The Honorable Susan M. Collins
United States Senate
Permanent Subcommittee On Investigations
199 Russell Senate Office Building
Washington, D.C. 20510

Dear Chairman Levin and Senator Collins:

As Chairman and Chief Executive Officer of J.P. Morgan Chase & Co., I submit this letter in response to the Permanent Subcommittee on Investigations' July 25, 2002 request for certain information regarding the relationship and dealings of J.P. Morgan Chase & Co., and its affiliates and their predecessors ("JPMorgan Chase") with Mahonia Limited ("Mahonia"). I do not have personal knowledge of, and, therefore, cannot attest on the basis of my personal knowledge to, the facts necessary to answer the Subcommittee's questions. Instead, those with knowledge of the facts and familiarity with the relevant documents have been consulted, and I submit the following responses on behalf of JPMorgan Chase. I note that (i) you have imposed a very short deadline for answering your questions, (ii) many of the events in question took place ten or more years ago, and (iii) there may be relevant facts not known to JPMorgan Chase. JP Morgan Chase has, however, sought to obtain the best information available, and it has prepared this response on the basis of that information.

At the outset, I should point out a few basic facts relating to Mahonia. Mahonia is a special purpose entity incorporated in 1992 at JPMorgan Chase's request. As is typical with special purpose entities, whether they are organized in the United States or elsewhere, Mahonia was formed to participate in transactions arranged by the sponsor, in this case JPMorgan Chase. Mahonia is a legally independent entity that has its own shareholders and directors and makes its own decisions about whether to enter into transactions. JPMorgan Chase has no power to compel Mahonia to enter into a transaction Mahonia does not wish to enter into. Once Mahonia accepts a particular transaction and transaction documents are executed, Mahonia appoints JPMorgan Chase as its agent for that transaction. That appointment gives JPMorgan Chase the power and authority to carry out the steps necessary to perform the transaction on Mahonia's behalf.

1. Did Chase establish Mahonia and, if so, for what purpose and why in Jersey?

Mahonia was established at JPMorgan Chase's request in December 1992 by Mourant du Feu & Jeune, acting on behalf of The Eastmoss Trust.

J.P. Morgan Chase & Co. • 270 Park Avenue, New York, NY 10017-2070
Telephone: 212 270 4019
william.harrison@chase.com

Mahonia was established to participate in transactions arranged by JPMorgan Chase (as was explained by Mourant du Feu & Jeune to the Jersey authorities at the time Mahonia was incorporated). It was not incorporated in contemplation of a transaction with Enron but in contemplation of a transaction with one or more other clients of JPMorgan Chase that did not proceed. Having been incorporated but not used, Mahonia was then identified as available for use in a June 1993 prepay transaction with Enron.

At the time, The Chase Manhattan Bank, N.A. (predecessor to The Chase Manhattan Bank and, later, JPMorgan Chase Bank) believed that it did not have regulatory authority to take physical delivery of commodities such as oil or gas. To satisfy regulatory requirements, Mahonia served as the entity that received physical delivery of gas or oil from Enron under the gas and oil forward contracts referred to as prepays. The reason that JPMorgan Chase utilized a Jersey special purpose entity, as opposed to an entity in another jurisdiction, is that some JPMorgan Chase employees who worked on the early Enron prepay transactions worked in JPMorgan Chase's London office and had often arranged transactions involving Jersey special purpose entities. I further note that Jersey is also regarded as having high quality legal and regulatory systems and as not having significant tax impact on transactions.

2. Does Chase own Mahonia, and if it doesn't, who does?

JPMorgan Chase does not own Mahonia. Mahonia is directly owned by Lively Limited and Juris Limited and is beneficially owned by Mourant & Co. Trustees Limited as trustee of The Eastmoss Trust.

JP Morgan Chase also does not own Mahonia II Limited, Mahonia Natural Gas Limited, Mourant du Feu & Jeune, Mourant & Co., Juris Limited, Lively Limited, The Eastmoss Trust or Eastmoss Limited. The shareholders of Mahonia, Juris Limited and Lively Limited, are two Jersey companies that act as subscribers for shares in companies incorporated by the Mourant Group, the Jersey professional services firm whose partners include partners in the law firm of Mourant de Feu & Jeune. Lively Limited and Juris Limited are ultimately owned by the partners of the Mourant Group. Juris Limited and Lively Limited made Declarations of Trust in respect of their shareholdings in Mahonia in favor of the Trustee of The Eastmoss Trust, Mourant & Co. Trustees Limited.

We understand that this is a standard arrangement for special purpose entities established in Jersey by the leading law firms and corporate services providers, including the Mourant Group.

3. If the owner of Mahonia is a charitable trust, does Chase own the charitable trust, and if it doesn't, who does?

The Eastmoss Trust was formed in 1986 at the request of JPMorgan Chase. The Eastmoss Trust, as formed, is not the structure that was contemplated at the time of Ian James' April 24, 1986 letter that you referred to during the hearing on July 23, 2002. At the time that letter was written, it was contemplated that the structure of the trust would involve JPMorgan Chase having a controlling interest, and Chase Bank & Trust Company (C.I.) Limited ("Chase

Jersey") was intended to be the Trustee and would have provided all of the directors of the special purpose entity. It was in this context that Mr. James made the comments on the second page of his letter relating to JPMorgan Chase's control of the special purpose entities. However, as indicated in Mr. James' May 29, 1986 letter, which was included as part of Subcommittee Exhibit 118 distributed at the hearing, this is not the structure that was thereafter actually adopted for The Eastmoss Trust. In that subsequent letter, Mr. James stated:

> "For U.S. regulatory reasons Chase were then advised they could not have either the ownership or control of Xco and so the Jersey structure outlined in my letter to you was proposed. In order that the U.S. authorities could be entirely satisfied with the arrangements it was considered preferable that my firm's trust company should act as trustee of the charitable trust and administer Eastmoss rather than Chase Jersey."

See May 29, 1986 Letter, attached hereto as Exhibit A. Neither Chase Jersey, nor any other JPMorgan Chase entity, now has or ever has had any control over The Eastmoss Trust, whether as trustee or otherwise. As explained below, the Trustee of The Eastmoss Trust was and is Furze Trustees Limited, which subsequently changed its name to Mourant & Co. Trustees Limited.

As noted, JPMorgan Chase does not own or have any ownership interest in The Eastmoss Trust. The Eastmoss Trust is a charitable trust formed in accordance with the laws of Jersey. As a trust, The Eastmoss Trust has no owners, but does have a trustee. The Trustee of The Eastmoss Trust is Mourant & Co. Trustees Limited. JPMorgan Chase does not own Mourant & Co. Trustees Limited and is not a trustee of The Eastmoss Trust.

4. Who serves on the Board of Directors of Mahonia and the entity that owns Mahonia?

Richard Jeune and Ian James are the directors of Mahonia. There are 26 directors of Lively Limited and Juris Limited, including Mr. Jeune and Mr. James, of whom 23 are also directors of Mourant & Co. Trustees Limited, again including Mr. Jeune and Mr. James. All of the directors are partners of the Mourant Group (and none is an employee of JPMorgan Chase).

5. Who is the agent for Mahonia and who is the agent for the entity that owns Mahonia?

JPMorgan Chase is not and has never been the general agent for Mahonia or Mourant & Co. Trustees Limited/The Eastmoss Trust. To JPMorgan Chase's knowledge, neither Mahonia nor The Eastmoss Trust has a general agent. Once Mahonia accepts a particular transaction and transaction documents are executed, Mahonia appoints JPMorgan Chase as its agent for that transaction. That appointment gives JPMorgan Chase the power and authority to carry out the steps necessary to perform the transaction on Mahonia's behalf. In addition, following Enron's collapse, Mahonia appointed JPMorgan Chase as its attorney-in-fact in connection with protecting and enforcing the parties' rights under the prepay transactions.

6. Does Chase pay for: Mahonia's administrative fees? Registration fees? Attorney fees? Transaction Fees?

As is typical with special purpose entities, whether they are organized in the United States or elsewhere, Mahonia's fees and expenses, including administrative, transactional, attorneys' and annual registration fees, are paid or reimbursed by the party that asked that the special purpose entity be established, in this case, JPMorgan Chase. It is not uncommon in various kinds of commercial transactions between independent parties for one party to pay another party's fees and expenses.

7. When a non-Chase entity does business with Mahonia, with whom does the entity conduct the negotiations – a Chase employee or a Mahonia employee?

In developing a transaction, the non-JPMorgan Chase entity (in this case, Enron) typically would negotiate a potential transaction with JPMorgan Chase. If the transaction required a special purpose entity, then JPMorgan Chase might propose the transaction to a suitable special purpose entity, in this case Mahonia. This process is commonplace for transactions involving special purpose entities. (I note that on at least one occasion, Mahonia declined to engage in an activity proposed to it by JPMorgan Chase that did not meet Mahonia's risk criteria.)

It was understood by all parties that Mahonia generally required that the contract on one side (*e.g.*, Mahonia-Chase) follow closely the terms of the contract on the other side (*e.g.*, Mahonia-Enron). Also, JPMorgan Chase had a significant economic interest in the Mahonia-Enron contracts, which were collateral for Mahonia's obligations under the Mahonia-Chase contracts. Thus, for most issues a third party like Enron negotiated with JPMorgan Chase, which was negotiating on its own behalf the terms of collateral acceptable to it and the terms of the Mahonia-Enron contract that it would be willing to have reflected in the Mahonia-Chase contract. As would invariably be the case with special purpose entities, it was unusual for a third party to raise an issue that affected Mahonia separately in a way that would not be reflected in Mahonia's contract with Chase. Mahonia would, however, take its own advice and make its own comments as part of the negotiations.

8. What obligations do any of the attorneys, trustees, administrators, directors, or beneficial owners of Mahonia have to Chase with respect to Mahonia and separate and apart from Mahonia?

The attorneys, trustees, administrators, directors and beneficial owners of Mahonia do not, in their capacity as such, owe any obligations or duties to JPMorgan Chase with respect to Mahonia. To the contrary, these individuals' obligations and duties are owed to Mahonia and to its shareholders. Separately and unconnected with Mahonia, from time to time the Mourant Group and Mourant de Feu & Jeune provide other company formation and administration services and legal advice to JPMorgan Chase as well as to many other large financial services institutions.

9. Does Chase effectively control Mahonia?

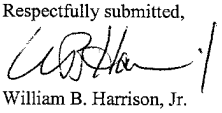
As you know, "control" is a term that is defined in different ways by various statutes and regulations. For example, Regulation Y issued pursuant to the Bank Holding Company Act defines "control" in relation to the ownership or power to vote shares, the control over the election of the Board of Directors and the power to exercise a controlling influence over the management or policies of a company. Likewise, regulations issued pursuant to the Securities Act of 1933 define control in terms of the power to direct the management and policies of another person. The International Swaps and Dealers Association ("ISDA") Master Agreement, which applies to trading in gas and oil swap contracts (including those that were agreed in relation to certain of the Enron prepays), employs a similar concept in determining whether parties are "affiliates." ISDA deems entities to be "affiliates" only if (i) one party owns (directly or indirectly) a majority of the voting power of the other party, or (ii) some third party owns a majority of the voting power of both parties. The common theme is the power to direct the activities of the controlled entity.

Thus understood, JPMorgan Chase does not control (or "effectively" control) Mahonia. While Mahonia is a special purpose entity incorporated at JPMorgan Chase's request, it is nonetheless legally independent from JPMorgan Chase. Mahonia is owned by Mourant & Co. Trustees Limited as trustee of The Eastmoss Trust and controlled by its directors, not JPMorgan Chase. Mahonia's directors' obligations and duties are owed to Mahonia, not to JPMorgan Chase. The type of transactions proposed by JPMorgan Chase are generally of a kind that JPMorgan Chase is aware Mahonia will be willing to enter, so there is an expectation that Mahonia will accept transactions proposed by JPMorgan Chase, provided that they are considered appropriate by the Mahonia directors. However, Mahonia's directors have the exclusive authority to decide whether to enter into any proposed transaction. JPMorgan Chase has no power to compel Mahonia to enter into a transaction Mahonia does not wish to enter into. In fact, as indicated above, on at least one occasion, Mahonia declined to engage in an activity proposed by JPMorgan Chase.

* * * * * *

With respect to the Subcommittee's request for documents, JPMorgan Chase does not have the power to direct Mahonia or the other entities listed in your letter to produce the documents requested. I understand that Mahonia has cooperated with a number of investigations that are occurring in the United States and has produced a number of documents. We will forward your request to Mahonia, second it with our own request to the same effect, and will advise the Subcommittee of Mahonia's response.

Respectfully submitted,



William B. Harrison, Jr.

State of New York)
: ss.:
County of New York)

William B. Harrison, Jr., being duly sworn, deposes and says:

1. I am the Chairman and Chief Executive Officer of J.P. Morgan Chase & Co. (together with its subsidiaries and affiliates, "JPMorgan Chase").

2. I submit this verification in connection with my July 29, 2002 letter in response to the July 25, 2002 request of the United States Senate Permanent Subcommittee on Investigations (the "Subcommittee").

3. As stated in my July 29, 2002 letter, I do not have the personal knowledge needed to respond to the Subcommittee's questions. However, in an effort to be responsive to the Subcommittee's request, I directed that inquiry be made to the extent appropriate and feasible in the time allowed by the request to provide the Committee with answers to its questions based on the best information available to JPMorgan Chase. I have reviewed the July 29, 2002 letter and certain of the documentary evidence on which it is based, and I have discussed the letter and its contents with persons involved in its preparation.

4. On the basis of the foregoing, I believe the answers contained in my July 29, 2002 letter to be true and accurate.

William B. Harrison, Jr.

Sworn to before me this 29th
day of July, 2002

Notary Public

ANGELINA F. LONGO
Notary Public, State of New York
No. 4736577
Qualified in Westchester County
Certificate Filed in New York County
Commission Expires April 30, 2003

Mourant du Feu & Jeune
Advocates, Solicitors and Notaries Public
P.O. Box 87, 18 Grenville Street, St Helier,
Jersey, Channel Islands

Telephone (0534) 74343
Telex 4192064
Telecopier (0534) 79064

J. D. F. Crill
F. J. Herbert
Consultants
H. de. C. Mourant
C. A. R. du Feu
R. A. Jeune, O.B.E.

Our Ref: ICJ/8320/2/7

M.D. Fox, Esq.,
Assistant Commercial Relations Officer,
Commercial Relations Department,
Cyril Le Marquand House,
The Parade,
St. Helier,
Jersey, C.I.

29th May, 1986

Dear Michael,

Eastmoss Limited

I should begin by thanking you and your department for the speed with which Eastmoss was incorporated. This was very much appreciated not only by this firm, but also by Chase and the other participants in the transaction which for reasons which I shall explain later in this letter, was abortive, but nevertheless was highly successful from the point of view of Chase and its ultimate client. The role of the Island in achieving this was crucial and the fact that we were able to incorporate the company in this very short time scale has, in my view, enhanced Jersey's reputation with the various professionals involved in this transaction.

I undertook in my letter to you of 19th May that as soon as the matter became public I would write to you to give you full details of the various participants.

The participants were as follows:-

Bidder	Dixons
Target	Woolworths
Canco	Comet
XCo	Teak Investments Limited (a Coward Chance U.K. shelf Company)

EXHIBIT A

...2/

The position was that Chase were aware that Dixons had been negotiating with a third party, who has now been identified as Granada, regarding the sale of Comet should Dixons' acquisition of Woolworths prove successful. In view of the complexities of the situation it is not surprising that Granada's initial offers were significantly below the actual market value of Comet and both from the commercial point of view and from the fact that this could give rise to unfavourable publicity which would not assist Dixons in the midst of a contested takeover, it was felt by Dixons and their advisers, S.G. Warburg & Co., that Dixons could not accept this initial offer. Accordingly Chase were approached with the suggestion that they should fund Xco which would thereupon agree to purchase Comet at a price determined by the actual sale proceeds of Comet to a third party in the months following a successful takeover of Woolworths by Dixons.

For U.S. regulatory reasons Chase were then advised that they could not have either the ownership or the control of Xco and so the Jersey structure outlined in my letter to you was proposed. In order that the U.S. authorities could be entirely satisfied with the arrangements it was considered preferable that my firm's trust company should act as trustee of the charitable trust and administer Eastmoss rather than Chase Jersey.

In the event, at 4 a.m. on Thursday 19th May Xco was able to make a formal offer for the purchase of Comet. Apparently, in the light of this 'market-value' offer, the discussions between Dixons and Granada intensified. At 9 a.m. on that morning it was announced that Granada had agreed to acquire Comet, provided that Dixons' bid for Woolworths was successful, on terms which were acceptable to Dixons and significantly higher than the original offer. The result was therefore highly satisfactory both for Chase and its client, Dixons, even though the Xco offer was not accepted.

I think that I should also mention that Eastmoss Limited was only entering into this transaction on the basis that it would have made a profit pro rata to the amount of the Comet sale price. Thus if Comet had ultimately been sold to a third party for the same price as that paid by Granada, Eastmoss would have made a net profit of approximately £40,000 which would have been available to be distributed to the Trustees of the Charitable Trust for them to apply for charitable purposes.

I am raising with Chase the question of whether Eastmoss Limited should now be dissolved but I understand that there is a possibility that it will be used in an alternative transaction provided that your

St Jeune

department is agreeable. I am obtaining details of this transaction and I will write to you with these if it appears that Eastmoss Limited is to be involved.

Please let me know if you require any further information.

Yours sincerely,

I.C. James

JPMorganChase

One Chase Manhattan Plaza, 26th Floor
New York, New York 10081
Tel 212-552-0918
Fax 212-552-1295
Ahuva.Genack@chase.com

Ahuva Genack
Assistant General Counsel

TELECOPIER TRANSMITTAL SHEET

DELIVER TO:	**Mr. Bob Roach**
FAX:	**202-224-1972**
FROM:	**Diane Haywood (Assistant to Ahuva Genack)**
DATE:	**April 12, 2002**
RE:	**In the Matter of Enron Corporation** **File No. HO-09350**

Remarks:

Ahuva asked me to forward to you this schedule, which was previously produced to the House Committee on Energy and Commerce. She asked that this document be accorded confidential treatment. Thank you.

PAGES INCLUDING THIS COVER SHEET: 11

IF YOU DO NOT RECEIVE ALL THE PAGES, PLEASE CALL BACK AS SOON AS POSSIBLE AT (212) 552-0512.

Confidentiality Note

The information contained in this facsimile message is legally privileged and confidential information intended only for the use of the individual or entity named above. If the reader of this message is not the intended recipient, you are hereby notified that any dissemination, distribution or copy of this telecopy is strictly prohibited. If you have received this telecopy in error, please immediately notify us by telephone and return the original message to us at the address above via the United States Postal Service. Thank you.

Permanent Subcommittee on Investigations
EXHIBIT #185s

SCHEDULE

Summary of JPMorgan Chase - Securities Underwriting, Advisory and Credit Facilities Services for Enron Corp. 1997-2002

Project Name	Year	Type	Total Size (CMB Participation)	Fees (000's)	Comments
1997					
364-day Revolver	1997	Corp. Revolver	$1 billion ($46mm CMB)	N/A	Citibank as arranger / administrative and paying agent, The Chase Manhattan Bank ("CMB") as a participant.
Brazos Office Holdings	1997	Syndicated Loan	$285 million ($28mm CMB)	$255	Chase Securities Inc. ("CSI") as arranger and CMB as agent for bank market syndication. Synthetic lease structure supported by the value of Enron's headquarters building. Approximately, 75% of the credit supported by an Enron Corp. guarantee (100% in a post default scenario)
Multi-currency Facility	1997	Syndicated Loan	$250 million ($16mm CMB)	$163	CSI as arranger and CMB as agent for bank market syndication
Enron Oil & Gas Short Term Revolver	1997	Syndicated Loan	$300 million ($25mm CMB)	$60	CSI as arranger and CMB as agent for bank market syndication
Enron Oil & Gas Long Term Revolver	1997	Syndicated Loan	$100 million ($8mm CMB)	See prior transaction	CSI as arranger and CMB as agent for bank market syndication.
Project Balboa	1997	Advisory services	N/A	$500	CSI provided advice relating to Enron's plan filed with the Pennsylvania public utility commission to act as "default provider" of power in the service territory of PECO. In addition to the advisory fee, Enron retained

[CONFIDENTIAL]

					CSI as sole manager on a $100 MM bond to be executed at a later date.
Enron Corp. Bond	1997	Capital Markets	$100 million	($160)	This mandate intended to produce $500 M in additional compensation related to Project Balboa. Executed as a "bought deal" on which CSI lost money.
Chewco Bridge Loan	1997	Six Week Bridge Loan	$188 million (All CMB)	$100	Short term loan to purchaser of CalPERS interest in JEDI. Credit risk secured by Enron Corp. guarantee. Loans to Chewco and subsidiaries totaled $193.5 MM (see below). These loans were outstanding approximately six weeks.
Big River Bridge Loan	1997	Six Week Bridge Loan	$5.5 million (All CMB)		Related to Chewco Bridge. Guaranteed by Enron.
Little River Bridge Loan	1997	Six Week Bridge Loan	$166 thousand (All CMB)		Related to Chewco Bridge
SONR #1 Bridge Loan	1997	Six Week Bridge Loan	$57 thousand (All CMB)		Related to Chewco Bridge
SONR #2 Bridge Loan	1997	Six Week Bridge Loan	$5 thousand (All CMB)		Related to Chewco Bridge
JEDI Amendments	1997	Syndicated Loan	N/A	$500	Various amendments executed by CSI as arranger. Amendments dealt with use of proceeds.
JEDI II Short Term Bridge Loan	1997	Bridge Loan	$200 million ($100mm CMB)	$100	CMB and Barclays Bank as lenders to JEDI II partnership between Enron and CalPERS.
Forward Commodity Contract	1997	Commodity Contract	$300 million	$750	CMB entered into a commodity prepaid forward sale contract with Mahonia, which in turn entered into a forward sale and margin agreement with an Enron subsidiary. Enron Corp. guaranteed performance of Enron

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					subsidiary. Enron Corp. performance risk syndicated to bank letter of credit market.
Mexican Gas LDC	1997	Advisory Services	N/A (Deal never closed)	$150	CSI provided M&A advisory services related to Enron's proposed bid on the privatization of a gas LDC in Monterrey. No bid was submitted.
1998					
EICPO	1998	Advisory Services and Capital Markets	$5 billion target (Deal never closed)	$1,000	CSI and Lehman retained as joint advisor and placement agent for an international project finance concept. EICPO filed a registration statement with the SEC but the transaction was ultimately pulled due to conditions in the emerging markets.
Enron Oil & Gas Bonds	1998	Capital Markets	$150 million	$300	CSI acted as a co-manager
Enron Europe Ltd.	1998	Revolver	$250 million ($20mm CMB)	$163	CSI as arranger and CMB as agent for bank market syndication. Enron Corp. provided a guarantee to its principal operating subsidiary in Europe.
JEDI II	1998	Syndicated Loan	$500 million ($26mm CMB)	$750	CSI and Barclays as joint arrangers and CMB as agent for bank market syndication. Credit supported by undrawn partners capital of $1 billion from CalPERS and Enron as well as by asset coverage from partnership investments.
Forward Commodity Contract	1998	Commodity Contract	$250 million	$625	CMB entered into a commodity prepaid forward sale contract with Mahonia, which in turn entered into a forward sale and margin agreement with an Enron subsidiary. Enron Corp. guaranteed performance of Enron subsidiary. Enron Corp. procured surety bonds from a group of insurers to secure its

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					performance risk.
Enron Bonds	1998	Capital Mkts	$500 million	$1,500	CSI acted as sole manager
Azurix Private Equity	1998	Private Placement	$500 million target (Deal never closed)	$250	CSI retained to advise on potential private equity alternatives to IPO. Deal pulled based on available price and terms.
Elektro Opco Loan	1998	Syndicated Loan	$500 million ($52mm CMB)	$3,200	CSI as arranger and CMB as agent for bank market syndication. Credit supported by the operations of one of the largest electric distributors in Brazil together with a total return swap with Enron Corp. to provide credit support with respect to non-operating risks such as Brazilian political risk and devaluation risk above a preset limit.
Project Firefly	1998	Syndicated Loan	$400 million ($30mm CMB)	$3,500	CSI and DLJ as arrangers and CMB as agent for bank market syndication. Credit was supported by equity value of Enron's investment in Elektro, one of the largest electric distributors in Brazil. Credit further supported by Enron's issuance of mandatory convertible preferred stock into a Trust. To the extent that these shares were required to be sold by the Trust and that re-marketing effort failed, the credit also benefited from a put to Enron Corp.
Forward Commodity Contract	1998	Commodity Contract	$250 million	$625	CMB entered into a commodity prepaid forward sale contract with Mahonia, which in turn entered into a forward sale and margin agreement with an Enron subsidiary. Enron Corp. guaranteed performance of Enron subsidiary. Enron Corp. procured surety bonds from a group of insurers to secure its

					performance risk.
1999					
Forward Commodity Contract	1999	Commodity Contract	$500 million	$1,250	CMB entered into a commodity prepaid forward sale contract with Mahonia which in turn entered into a forward sale and margin agreement with an Enron subsidiary. Enron Corp. guaranteed performance of Enron subsidiary. Enron Corp. procured surety bonds from a group of insurers to secure its performance risk.
Rawhide	1999	Syndicated Loan	$720 million ($17mm CMB)	$87	CMB as a participant in this transaction arranged by Citibank. Credit based on the value of a diversified pool of merchant energy assets contributed by Enron to the Rawhide vehicle. Additional credit support provided by undertakings by Enron Corp.
AGOSBA Advisory	1999	Advisory Services	$438 million	$2,600	CSI acted as buy side M&A advisor to Azurix, Enron's water segment investment, in its purchase of a water and waste water service concession that was privatized by the State of Buenos Aires in Argentina.
Choctaw BV	1999	Syndicated Loan and Private Placement	$500 million ($45mm CMB)	$9,735	CSI as arranger and CMB as agent for this syndicated loan to a special purpose entity ("SPE") that invested in qualified trade receivables generated by Enron's gas and power trading business as well as other qualified investments including debt of Enron. CSI also placed $15 MM in preferred shares to an unrelated third party investor.
Azurix Europe Ltd. Revolver ("AEL")	1999	Syndicated Loan	$595 million ($14mm CMB)	$1,750	CSI and WestLB acted as joint arrangers. AEL credit supported by its ownership of Wessex

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					Water, a regulated water utility in the UK. Note the figures are dollar equivalent of a Pound Sterling denominated transaction
Enron Corp.	1999	Eurobond	$500 million	$100	CSI acted as a junior co-manager
Citrus Corp.	1999	Syndicated Loan	$240 million ($16mm CMB)	$350	CSI as arranger and CMB as agent. Citrus is 50% owned by Enron. Citrus credit is based on its ownership of Florida Gas Transmission, a regulated pipeline.
EICPO	1999	Debt Fund	$5 billion target (Deal never closed)	$800	Final installment on fees for this terminated transaction.
JEDI SPV	1999	Syndicated Loan	$513 million ($128mm CMB)	$500	CSI as arranger and CMB as agent. This credit was structured on the basis of the value of Enron shares held by the JEDI SPV partnership. The value of the shares was supported by a swap agreement with Enron Corp.
LJM2	1999	Syndicated Loan	$65 million ($25mm CMB)	$650	CSI as arranger and CMB as agent. Credit based on a percentage of the unfunded equity capital committed to LJM2 by a diversified group of creditworthy investors. Lenders had certain rights to compel the call on investor capital.
2000					
364-Day Revolver	2000	CP Back-up Revolver	$1.75 billion ($46mm CMB)	$250	Citibank as paying agent, CSI and Citibank acted as co-arrangers
5-Yr Revolver	2000	CP Back-up Revolver	$1.25 billion ($33mm CMB)	See Above	Citibank as paying agent, CSI and Citibank acted as co-arrangers.
Forward Commodity	2000	Commodity	$650 million	$1,625	CMB entered into a commodity prepaid

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Contract		Contract			forward sale contract with Mahonia which in turn entered into a forward sale and margin agreement with an Enron subsidiary. Enron Corp. guaranteed performance of Enron subsidiary. Enron Corp. procured surety bonds from a group of insurers to secure $400mm of its performance risk. CMB purchased credit default swaps to mitigate the remaining $250mm of Enron performance risk.
San Juan Gas	2000	Bank Line	$40 million	$8	CMB bi-lateral facility guaranteed by Enron Corp.
Hawaii	2000	Syndicated Loan	$550 million ($20mm CMB)	$16	CMB as a participant in this transaction arranged by CIBC supported by a combination of a pool of assets and supplemented by Enron Corp. credit in the form of a total return swap
Enron NetWorks	2000	Private Equity Placement	$500 million to $1 billion target (Deal never closed)	$500	CSI retained to advise on potential private equity to share risk with Enron on the development of new. Deal pulled based on available price and terms.
TNPC	2000	New Power IPO	$500 million (Co-manager)	$2,500	CSI acted as a co-manager for the IPO of The New Power Company
Zephyrus	2000	Syndicated Loan	$500 million ($50mm CMB)	$1,500	CSI as arranger and CMB as agent for this syndicated loan to an SPE that invested in qualified trade receivables generated by Enron's gas and power trading business as well as other qualified investments including debt of Enron.
Garden State Paper	2000	Syndicated Loan Project Financing	$49 million ($24.5mm CMB)	$250	CSI and Citibank as joint arrangers. Credit based on the operating cash flows of a newsprint mill. Additional support provided by Enron in the form of a partial guarantee and

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					certain commodity swaps benefiting the project.
Annapurna	2000	Unfunded Bank Commitment	$41.875 million	$500	CMB provided an unfunded commitment to the purchaser of Enron's pulp and paper trading book. The credit was secured by the value of the trading book that was approximately four times the commitment.
Forward Commodity Contract	2000	Commodity Contract	$330 million ($165mm CMB)	$1,000	CMB as assignee of Mahonia's rights under a forward sale contract entered into with an Enron subsidiary. Enron Corp. guaranteed performance of Enron subsidiary. Enron Corp. procured surety bonds from a group of insurers to secure its performance risk.
Florida Gas Transmission	2000	144A Bonds	$325 million	$1.2 million	CSI acted as lead manager. FGT is 50% owned by Enron. Florida Gas Transmission, is a regulated pipeline.
Citrus Corp.	2000	Money Market Loans	$40 million (repeating)	5 bps	CSI originated short term (overnight – 30 days) loans sold to money market funds. Citrus is 50% owned by Enron. Citrus credit is based on its ownership of Florida Gas Transmission, a regulated pipeline.
Enron Corp.	2000	Money Market Loans	$100 million (repeating)	5 bps	CSI originated short term (overnight – 30 days) loans sold to money market funds
JEDI SPV	2000	Bank Loan Amendment	$513 million	$50	Change to certain terms of this syndicated loan secured by Enron stock.
2001					
Enron Corp.	2001	Convertible Preferred	$1.9 billion (Co-manager)	$2,100	JPMorgan Securities Inc. ("JPMSI) acted as a co-manager
Flagstaff	2001	Syndicated Loan	$375 million ($73 million	$5,250	Structured bank financing for Enron Canadian subsidiary. JPMSI as arranger and CMB as

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			CMB)		agent. Credit support provided by a total return swap with Enron for the value of the entire loan. Structure included a $1.039 Bn intraday loan to Flagstaff.
364-Day Revolver	2001	CP Back-up Revolver	$1.75 billion ($66 mm CMB)	$150	Citibank as paying agent, JPMSI and Citibank acted as co-arrangers
364-Day L/C Facility	2001	Syndicated L/C Facility	$500 million ($19 mm CMB)	See Above	JPMSI and Citibank acted as co-arrangers
Letters of Credit	2001	Bi-lateral L/C's	$101 million	Est. $250 - $500 per year	CMB extended standby and performance letters of credit on a bi-lateral basis for a variety of transactions (bid bonds, workman's comp. etc). The $101 MM figure represents LC's at the time of bankruptcy. This amount varied from time to time in the 1997-2001 period.
Azurix Corp.	2001	Advisory Services	$300 million Asset Sale	$1,590	JPMSI retained to sell a series of North American and Latin American water businesses. Azurix North America sale completed in 2001. Latin America engagement in ongoing.
Brazos VPP	2001	Syndicated Loan (participant)	$200 million ($15mm CMB)	$4	B of A arranged this non recourse facility backed by a portfolio of volumetric production payment.
Enron Corp.	2001	CP Dealership	$3 billion (one of five dealers)	5 bps	JPMSI appointed as a dealer post-September 11, 2001
JEDI II	2001	Bank Loan Extension	$200 million ($20mm CMB)	$250	JPMSI acted as arranger and CMB as agent
Forward Commodity Contract	2001	Commodity Contract	$350 million ($35mm CMB)	$1,000	CMB as swap counterparty with Mahonia; Mahonia as swap counterparty with Enron

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					subsidiary. Enron Corp. guaranteed performance of Enron subsidiary. Enron Corp. procured letters of credit from existing committed credit facilities to secure its performance risk.
Transwestern	2001	Syndicated Loan	$550 million ($220mm CMB)	$12,000	JPMSI and Citigroup jointly structured this secured facility after the announcement of Enron's 3Q '01 earnings. Security is a pledge of shares and filed security interests.
Northern Natural Gas	2001	Syndicated Loan	$450 million ($180mm CMB)	$12,000	JPMSI and Citigroup jointly structured this secured facility after the announcement of Enron's 3Q '01 earnings. Security is a pledge of shares and filed security interests.
Project Notre Dame	2001	Advisory Services	$22 billion	$13,629	JPM and Citigroup acted as joint advisors in merger negotiations with Dynegy Inc. A definitive merger was announced on 11/09/01 and subsequently terminated on 11/28/01.
2002					
Enron Corp.	2002	Debtor in Possession Financing	$250 million ($125mm JPM)	$3,125	JPMSI and Citigroup jointly arranged the debtor-in-possession facility to provide finance to Enron's bankruptcy estate on an "all assets" security basis.
Azurix Corp.	2002	Advisory Services	$300 million Asset Sale	$188	Continuation of JPMSI mandate in 2001. 2002 fee reflects the sale of an Azurix business in Brazil. Still pending is the sale of a business in Mexico.

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CITIBANK

GLOBAL LOANS APPROVAL MEMORANDUM

This deal is properly recorded on Syndicator. Verified by _____ (Deal Team Leader initials required).

Memo Date: October 19, 1999 — Approval Due Date: October 22, 1999

					Yes	No
	Renewal, Repricing or Restructuring		League Table Eligible			
	Amendment (Number ____)		Agent-only	Media Disclosure		X
N	Multi-Currency (Y or N)		Co-Agent	Contact:		

A. KEY STATISTICS

Borrower:	Yosemite Trust (1)	Citibank Commitment ($MM):	$37.5 million
GFCID#:	446084	Citibank Hold ($MM):	$37.5 million
Deal Size ($MM):	$37.5 million	U/W Amount ($MM):	Not Applicable
Facilities ($MM)/Tenor:	$37.5 million/7-year "Equity Certificates"	B/E Amount ($MM):	Not Applicable
Pre-approved (Y/N):	No	Accom. Amount ($MM):	Not Applicable
Date Pre-approved:	Not Applicable	Scheduled Launch Date:	October 25, 1999
Origination Unit:	GEM-Houston	Scheduled Closing Date:	October 31, 1999
GRB Industry:	Global Energy & Mining	Sell Down Date(s): (if applicable)	Not Applicable
GRB Market:	US South		
Account Segment:	House	Secured (Y/N):	No
Syndicated (Y/N):	No	Obligor Exception (Y/N): (Exception Amt.):	Yes $385.3 million
Agent(s)/Amount($MM):	Not Applicable	Liquidity Exception (Y/N):	Not Applicable
Co- Agents/Amount($MM):	Not Applicable	Pricing Exception (Y/N):	No Market; No Hurdle

(1) $37.5 million PSR fine for "Total Return Swap" between Citibank and "Balance Sheet Provider" purchasing Equity Certificates issued by the Yosemite Trust. Structural elements enhance transaction recovery characteristics to equate Equity Certificates exposure with Enron Senior Unsecured Credit Risk.

Team Leader: Jim Reilly	Tel: 713-654-2820	Back-up Contact: Steve Baillie	Tel: 713-654-2887

Pricing (bps):	Undrawn	Drawn	Fees (bps):
	N/A	LIBOR + 500 bps	None

LT UNSECURED RATINGS:	RR for Facility (DRM)	LTM Sales	LTM EBITDA	LTM Int. Coverage
BBB+/Baa2	4+	36.3 billion	$2.3 billion	3.0x

PURPOSE:

Request approval for a $37.5mm synthetic investment in Equity Certificates to be issued by Yosemite Securities Trust I ("Yosemite Trust"). Yosemite Trust will (i) refinance $800mm in existing crude oil prepaid transactions for Enron, and (ii) potentially purchase AAA-rated securities and provide Enron default protection to Citibank, thus allowing Citibank to enter into Default Swaps providing protection to Enron relationship banks. Yosemite Trust will be capitalized with $725mm-$925mm of 5-7 year Linked Enron Obligations (the "Notes"), to be placed by SSB in the capital markets via a 144A offering, and $75mm of Equity Certificates with a 7 year maturity. Each of Enron and a "Balance Sheet Provider" will purchase $37.5mm of the Equity Certificates. The Balance Sheet Provider will then enter into a total return swap with an SSB entity under which it will pay the total return on the Equity Certificates (an expected coupon of Libor plus 500bps) and receive a yet-to-be determined fixed

Permanent Subcommittee on Investigations
EXHIBIT #186a

financing charge from the SSB entity. The total return swap would obligate the SSB entity to also pay the Balance Sheet Provider any amount of the initial Certificate investment that is ultimately not recovered. Certain swaps, which Citibank will enter into with Yosemite Trust as part of the overall structure, will give the synthetic investment in the Equity Certificates return characteristics that generally should be superior to those associated with a direct $37.5mm investment in Enron senior, unsecured debt.

With this approval, Enron Total Facilities are $1.1 billion. Outstanding and unused commitments total $850.3 million, resulting in an Obligor Exception of $385.3 million. These facilities DO NOT reflect the reduction in exposure related to the retirement of Roosevelt ($125 million) and Truman ($400 million) prepaids. These prepaids will be repaid with the proceeds from the Yosemite, as there may be a short time lag between the execution of Yosemite and the repayment of Roosevelt and Truman. We estimate that this time lag will be less than three weeks. With the repayment of Roosevelt and Truman, Total Facilities will be $583.4 million and the Outstanding and Unused Commitments will be $366.6 million, eliminating the Obligor Exception. However, we could take hold positions in two transactions currently under discussion, a $375 million Revolver and a $350 million Capital Structuring transaction.

Through July 1999, the Enron relationship had resulted in $18.6 million in revenues and a RORAP of 319 bps. Comparatively, in 1998, the Enron relationship contributed revenues of $18.2 million and RORAP of 148 bps. Based on an Equity Certificate yield of 500 bps over LIBOR, we expect the proposed transaction to generate $1.875 million of revenue per annum. Derivatives is approving the Facilities and Swaps for the remainder of the transaction, and will also generate revenue of at least $4.7 million from a 65 bps Underwriting Fee and $800,000 per annum from a 10 bps Swap Fee.

APPROVALS:

STEVEN M. BAILLIE
[illegible] America, Inc.
(713) 654-2887

JAMES F. REILLY JR.
Managing Director
Citicorp North America, Inc.
(713) 654-2820

THOMAS R. STOTT
Vice President

WILLIAM T. FOX III
Managing Director
399 Park Ave / 16th Fl./Zn. 3
(212) 559-1011

Approval Level Required: Level 1/CPC/CE

DEAL TEAM:

Derivatives:	Origination:	Research:	Loan Investor Services:	Credit Admin
Adam Kulick	James F. Reilly	Sumit Mathai		Carol Rooney
212-723-6449	713-654-2820	713-654-2858		713-654-3590
Rick Caplan	Steve Baillie			
212-723-6453	713-654-2887			

11/12/99

R. CARRO RUBIO
Vice Chairman
399 Park Ave / 20th Floor
(212) 559-2785

THOMAS F. BOLAND
MD - LEVEL ONE ADVISORS
399 PARK AVE. 24TH FL.
212-559-1424

B. SUMMARY

Transaction Description

Enron engages in highly structured financings ("Enron Structured Debt") with a select group of banks on a regular basis. These transactions provide significant value to Enron in that it can finance capital needs while maintaining favorable accounting and rating agency treatment. In planning its capital needs, Enron has become increasingly sensitive that its ability to continue executing these transactions is constrained by limited bank credit capacity. Year-end 1998 volume into the bank market was particularly heavy. As a result, and as an explicit objective of the Enron Finance group, the company is working to free up bank capacity, primarily through the refinancing of bank transactions in the capital markets.

The "Yosemite" transaction is a $800-1,000 million transaction funded with Notes sold under Rule 144A that is designed to: (i) refinance existing Enron borrowings while maintaining advantageous accounting and rating agency treatment, (ii) create a hedge vehicle to act as a swap counterparty in credit default swaps of Enron credit, and (iii) free up Enron bank capacity with top tier financial institutions. Net proceeds from the offering will be used to purchase an $800 million Oil Prepaid transaction ("Prepaid") from Enron (the proceeds being used to retire existing prepaids with lenders, including Citibank), and purchase t up to $200 million of AAA rated investments (together the "Permitted Investments").

SSB has been mandated to act as Lead-Manager for the expected Notes offering (the "Offering") for Yosemite Trust, which is expected to close in October/November 1999. The notes will be issued in 5-year and 7-year tranches. The Notes of each tranche will represent senior debt obligations of the Trust secured by the assets of the Trust relating to the tranche. These assets may be changed over time, provided that Enron and Citibank agree to any substitution. The Trust will also issue Equity

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Certificates that will represent equity interests in the Trust. It is contemplated that an SSB entity (synthetically via a total return swap) and Enron (directly) will each purchase one half of the $75 million of Equity Certificates issued by the Trust.

Citibank Exposure/Risk

- *Yosemite Equity:* Yosemite Trust will issue $75 million of Equity Certificates. Enron will purchase $37.5 million of Equity Certificates directly, and Citigroup, via an SSB entity, will "synthetically purchase" the remaining Equity Certificates via a Total Return Swap with an Investor (i.e. Balance Sheet Provider) who will actually fund the equity investment. Consequently, the Balance Sheet Provider is exposed to SSB risk only, and SSBi assumes the equity exposure. Under the terms of the Citibank Swap, as explained more fully below, Citi receives the benefit of the overcollaterization in the Trust (the excess of the trust assets over the amount of Notes issued). This excess makes it highly likely that we will recover on the proposed $37.5mm synthetic equity investment, in an Enron bankruptcy, an amount in excess of that which would be recovered had we invested in an Enron Senior Unsecured loan. In fact, there would be the possibility of recovering more than the $37.5mm investment depending on recovery rate assumptions regarding Enron obligations.. Please seethe attachement Yosemite Equity Investment for greater detail.

Other Exposure/Risk

- *Citibank Swap:* there are other risks associated with the Yosemite transaction, which have been reviewed by CMAC, the Capital Markets Approval Committee (the Citibank Derivatives Approval Committee has been integrated into this group) These risks are outlined below.

  - Basis Risk: Citibank will "wrap" the Enron Investments purchased by Yosemite Trust (initially the Prepaid) with a swap ("Citibank Swap"), which is designed to assure that the Note Holders have effectively purchased Enron senior unsecured credit risk. The "wrap" will avoid the need of both investors and ratings agencies to perform due diligence on individual Enron investments purchased by the Trust. The Citibank Swap assures that the Note Holders , in an Enron bankruptcy, will receive a recovery rate equal to that of a senior, unsecured Enron obligation. Citi has, therefore, accepted the basis risk of a potential recovery rate differential between a direct Enron senior unsecured obligations and the structured financings. In the event of a bankruptcy of Enron, Citibank will settle the Citibank Swap by either delivering to the Trust senior, unsecured obligations of Enron (and receiving from the Trust the Enron Investments) or paying/receiving the difference between amounts recovered on the Enron Investments held by the Trust and corresponding actual recoveries on Enron "reference obligations" or any combination of the two. The Citibank Swap provides that payments/deliveries made by Citibank will only relate to an amount of notional principal corresponding to the Noteholder's percentage interest in the Yosemite Trust Assets (i.e. 92.75% on a structure involving $925mm in Notes and $75mm in Equity Certificates in the Yosemite Trust Capital Structure). However, payments/deliveries made by the Trust will be based on 100% of the underlying Yosemite Trust Assets. Hence, the effective overcollateralization noted above. Legal due diligence by Milbank, counsel to Citibank/SSB has determined that the Prepaid meets the standard of senior unsecured claims.
  - Cash Flow: . The interest payments on the Citibank Swap will be structured so: (i) the Trust will pay Citibank all interest payments on the Permitted Investments received by the Trust and (ii) Citibank will pay the Trust an amount equal to the interest payments on the Notes and the yield payments on the Equity Certificates due and payable on the related payment date (the "Citibank Fixed Payments") subject to certain adjustments. The Notes will be repaid on their stated maturity from the payments received by the Trust upon the maturity of the Permitted Investments. The principal on the Equity Certificates will only be repaid after the Notes are repaid. The payment obligations of Citibank under the Citibank Swap may vary upon the occurrence of events affecting the creditworthiness of Enron or affecting payments made upon the investments held by the Trust. Most importantly, Citibank is obliged to pay to the Trust only amounts received from Enron and our obligation to pay will cease upon an Enron bankruptcy.

- *Default Swaps:* Proceeds not invested in the Crude Oil Prepaid, will be used to purchase AAA investments that will hedge long-dated default swaps that Citibank will enter into with other Enron relationship banks (effectively this portion of the structure will be a traditional credit-linked note). AAA investments will include securities with long term ratings of AAA/Aaa or short term ratings of A1/P1, registered obligations of the United States of America or any agency or instrumentality whose obligations are guaranteed by the United States of America. Global Derivatives will select any AAA investments to be purchased by the Trust..

Enron Exposure:

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Recent/expected activity affecting our Enron exposure is outlined below. With the Yosemite transaction, Total Facilities are $1.1 billion, Total Outstanding and Unused Commitments are $850.3 million, and our Obligor Exception is $385.3 million. The Truman and Roosevelt transactions will be repaid with proceeds from Yosemite, however there may be a brief time lag between assumption of additional exposure on Yosemite and repayment of Truman and Roosevelt.

($ in Millions)	Total Facilities	Obligor Exception[1]
Net @ 9-30-99	$1,150	$476
(Truman)	(400)	(400)
(Roosevelt)	(125)	(125)
Yosemite	38	38
Net @ Yosemite Close	$663	$0

[1]Obligor Limit increased to $450 million from $375 million in 08/99 for 4+ rated borrowers. In addition, we have purchased default swap protection that now totals roughly $80 million.

By its terms, Roosevelt has an additional 4+ years until final maturity. However, the company has informally agreed to repay Roosevelt at 12/6/99.

EXPOSURE SUMMARY

(in $ millions)

Facility Description	Current	Proposed	Change
Yosemite Trust Equity Certificates	$0	$37.5	$37.5
Total	$0	$37.5	$37.5

Borrower:	Yosemite Trust
GPCID #:	446084
LT Unsecured Ratings:	BBB+/Baa2
Purpose:	PSR line for Total Return Swap
Type:	PSR line
Deal Size ($MM):	$37.5 million
Facilities ($MM)/Tenor:	$37.5 million/7-year
Upfront Fee (bps) to Investors:	None
Undrawn Cost (bps), FF or CF, (at current/expected ratings):	Not Applicable
Drawn Cost (LIBOR spread in bps) plus FF (at current/expected ratings):	500 bps
Utilization Fee (at current/expected ratings):	None
Ratings Pricing Grid (Y/N):	None
Financial Covenants (List):	None
Admin. Agent:	Not Applicable
Documentation Agent:	Not Applicable
Syndication Agent:	Not Applicable
Arrangement Fee ($ or bps):	Not Applicable
Admin. Agency Fee ($):	Not Applicable
Law Firm:	Not Applicable

GCCP 540-543 Exceptions:
Final Documentation is currently under negotiation, and will be reviewed by legal counsel for any GCCP 540-543 Exceptions once completed.

Year 2000 Issues:
Enron's Board of Directors adopted a Year 2000 plan (the "Plan") covering all of Enron's business units. The aim of the Plan is to prevent Enron's mission-critical functions from being impaired due to the Year 2000 problem and develop contingency plans. Enron also has engaged outside consultants, technicians and other external resources to aid in formulating and implementing the Plan. Enron's Year 2000 Plan calls for most business units to have completed initial rounds of inventory, assessment,

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remediation and validation testing of its mission critical internal items by June 30, 1999. At Enron, that deadline has been met in all material respects. Remaining mission critical items are expected to be completed for purposes of initial remediation and validation testing prior to September 30, 1999. Under the Plan and otherwise, Enron has not incurred material historical costs for Year 2000 awareness, inventory, assessment, analysis, conversion, testing, or contingency planning. Further, Enron anticipates that its future costs for these purposes, including those for implementing its Year 2000 contingency plans, will not be material.

C. SYNDICATION STRATEGY

The proposed transaction will not be syndicated. The Yosemite Trust will refinance existing Enron Structured Debt in the capital markets market and may also be used to issue Default Swaps to Enron relationship banks.

D. RISKS AND MITIGANTS

There are Deal Risks and an Enron Credit Risk related to the proposed Total Return Swap. The Deal Risks are outlined in Exhibit 6 – Derivative Transactions Description, which is included in this approval memo as an attachment.

Risk
Enron Default Risk: the Balance Sheet Provider will rely on Enron to repay $37.5 million of Equity Certificates, and Citibank is exposed to a pre-settlement risk under the Total Return Swap, as a result. The equity in Yosemite absorbs any losses in the Trust before the Notes, and the recovery on the Equity is zero if recovery on the Yosemite bonds is below 92.5 cents on the dollar.

Mitigant
Citibank receives the benefit of the overcollateralization in the Trust under the terms of the Citibank Swap. Specifically, the Citibank Swap provides that payments/deliveries made by Citibank will only relate to an amount of notional principal corresponding to the Noteholder's percentage interest in the Yosemite Trust Assets (i.e. 92.75% on a structure involving $925mm in Notes and $75mm in Equity Certificates in the Yosemite Trust Capital Structure). However, payments/delivenes made by the Trust will be based on 100% of the underlying Yosemite Trust Assets. Hence, this effective overcollateralization will ensure that exposure under the proposed transaction is no worse than an Enron Senior Unsecured credit facility. Please refer to the Yosemite Equity Investment memo for a more detailed discussion. Enron maintains investment grade senior unsecured credit ratings of BBB+/Baa2, and we expect the company to perform its obligations under the Yosemite structure.

E. RETURNS TO CITICORP

Return on transaction:
No upfront fee is payable with the proposed transaction. The Equity Certificates will yield a margin of 500 bps over LIBOR, and we expect the proposed transaction to generate $1.875 million of revenue per annum (The PV-6% of the transaction over the life of the deal is $10.5 million). In addition, we expect SSB to generate revenue of at least $4.7 million from the Underwriting Fee (65 bps on $725 million of Notes) and $800,000 per annum (PV of $4.5 million) from the Swap Fee (10 bps on an $800 million Transaction Amount). The PV of the transaction to Citigroup is approximately $19.7 million.

Return of the Relationship:

Revenue YTD July:	$18.6 million
12 Month 1998 Revenue:	$16.2 million
RORAP YTD July:	319 bps
1998 RORAP:	148 bps

F. MANAGEMENT AND RELATIONSHIP BACKGROUND

We continue to maintain an attractive, strong relationship with Enron; one that has provided over $16 million in revenues each of the last two years at well-above hurdle RORAP levels (140 bps in 1998). Our success to-date has been measured by management's comfort in our expertise and ability to structure, arrange and syndicate the company's "more-difficult", time-constrained financings.

As "Citigroup", we are now presented with additional opportunities with the company. Specifically, Citi/SSB was awarded roles in the company's common equity issuance in February, exchangeable notes issuance (related to the EOG share exchange

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agreement and related EOG equity offering in July), the recent Condor structured bond transaction, and forthcoming Yosemite transaction. Enron believes that with our expanded role in the bank, bond and equity markets, and specifically as its advisor in Yosemite, should come the willingness to commit capital resources as necessary.

G. Approval Profile

Third Quarter of 1999 Earnings:
Enron released its third quarter 1999 earnings on October 12, 1999. In the third quarter 1999, Revenue increased to $11.8 billion from $11.3 billion the same period the prior year, largely due to an increase in the Wholesale Energy and Operations and Transportation and Distribution ("Core Operations") revenue. In the third quarter 1999, the increase in revenue from Core Operations was largely due to a 19% increase in total natural gas volumes an increase in international revenue as projects went cash flow positive in India, Turkey, and South America. During the third quarter, IBIT (includes $67 million of net post-tax extraordinary items, as described below) from Core Operations was $515 million, which represented an increase of 27% from $407 million in the third quarter 1998. Net Income increased by 33% to $223 million, compared to $168 million in the third quarter 1998. These amounts include a $345 million post-tax gain related to the sale of EOG Resources ("EOG") common shares and a $278 million charge related to a fair value adjustment of Enron's MTBE asset.

First Half of 1999 Financial Update:
Enron operates as one of the largest integrated natural gas and electricity distribution companies in the world, with over $34 billion in both assets and revenues. It continues to generate consistent cash flow growth from its key operating divisions, which on a consolidated basis can now be relied upon to produce EBITDA of nearly $2.4 billion per annum. The company generated more than $2.2 billion of EBITDA during 1998, covering gross interest expense of $698 million 3.2x. Cash flow should continue to accrete even further as existing investments mature and go cash flow positive. Specifically, as of the end of 1Q99, the company reported 10 investments at a cost of roughly $6.7 billion, which it anticipated would begin to source cash flow over the course of the next twelve months. This excluded cash flow from Enron Energy Service ("EES"), Enron's retail electricity subsidiary, which the company believes will show positive cash flow (for the first time) in 4Q99.

S&P and Moody's rate Enron's senior unsecured debt BBB+/Baa2 (Citibank Obligor risk rating of 4+). Importantly, these ratings take into consideration the company's aggressive growth strategy during last few years, which aims to enhance market share in the deregulated, international, and clean energy markets. Concurrent with this strategy, the company remains committed to keeping its stable, investment grade credit ratings via active management of the its balance sheet. For example, during 1998, Enron financed approximately 75 transactions at a principal amount of $75.0 billion through the public, private, debt and equity markets. The company raised a significant amount of this capital through structured transactions that were (i) not EPS dilutive; (ii) segregated risk from Enron Corp.; (iii) expanded the company's lender/investor base; and (iv) overcame inherent balance sheet constraints. Most importantly, the high level of capital investments in 1998 reflects the capturing of opportunities available to Enron and an enhancement of its current franchise position.

Thus far during 1999, this strategy has progressed, with Citibank and Salomon Smith Barney ("SSB") playing important lead roles via capital structuring and derivative products and investment banking expertise. In February 1999, Enron issued 13.8 million shares of common stock (stock price of $62.2875/share) and applied the proceeds towards the funding of investment activities. SSB was a co-underwriter in the transaction. Also during 1Q99, the company acquired via an unconsolidated affiliate an interest in three CoGen plants in New Jersey for 3.8 million shares of common stock. Further, in April 1998, Enron issued 17 million shares of common stock. These issuances were all met favorably by the market, as demonstrated by the company's stock price, which has appreciated more than 100% since the beginning of 1998. On a broader basis, Enron's equity market capitalization has more than doubled in the last three years and currently exceeds $30.0 billion (stock price of $42/share on September 13, 1999. The company announced a 2-for-1 common stock split that took effect in mid-August).

Outlined below is select consolidated financial data through the last twelve months ("LTM") ended June 30, 1999:

Enron Corp. Financial Summary ($ in Millions)	June 30, LTM	Year Ended December 31, 1998	1997	1996
Total Revenues	$36,325	$31,260	$20,212	$13,289
Operating EBITDA	$2,388	$2,266	$1,431	$1,253
Gross Interest Expense	$791	$698	$419	$286
Net Income (unadjusted)	$688	$703	$105	$584
Capital Expenditures	$2,289	$1,905	$1,392	$864

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Cash & Equivalents	$286	$111	$170	$256
Total Debt*	$9,980	$8,358	$7,247	$3,941
Total Shareholder's Equity	$11,681	$9,191	$6,765	$4,478
Debt-to-Capitalization	46.1%	47.6%	51.7%	46.8%
Debt-to-EBITDA	4.3x	3.7x	5.1x	3.1x
EBITDA-to-Gross Interest	3.0x	3.2x	3.4x	4.4x

*Including Company Obligated Preferred Securities and excluding "Off Balance Sheet Debt," which is currently estimated at roughly $2.0 billion

In the first quarter 1999, Enron recorded an after-tax charge of $131 million related to the adoption of two new accounting pronouncements. Enron also increased its ownership percentage in Jacare Electrical Distribution Company from 47% to 53%. Jacare is the entity that previously held Enron's interest in Elektro. As a result, Jacare's balance sheet, which consisted of net assets of approximately $1,160 million, including goodwill of $1,080 million, net PP&E of approximately $820 million and debt of $900 million, was consolidated on Enron's balance sheet.

Although Enron's debt level increased dramatically over the past two years (total book debt of $10.0 billion at 6/30/99 as compared to $4.0 billion at 12/31/96), its debt to capitalization ratio of 46.1% marks an improvement from 46.8% at year-end 1998 (and 47.6% at YE98). The improvement can be traced to equity issued, partially offset by increased debt. Total debt-to-EBITDA coverage and interest coverage are not as strong as previous levels, but should see improvement in the not-to-distant future as investments mature and incremental cash flow comes on-line. Generally, though, EBITDA continues to appreciate and totaled $2,338 million for the last twelve months ended June 30, 1999. Comparatively, EBITDA was $2,266 million and $1,431 million for 1998 and 1997, respectively. Given the growth in cash flow and strength of the company's existing asset base, future debt obligations are acceptable and are estimated at: $541 million, $413 million, $666 million, $182 million and $656 million between 1999-2003, respectively.

Off Balance Sheet Debt:
Enron's off balance sheet debt is estimated at approximately $2.0 billion.

Prepaids	Leases	Receivables
$1,000-$1,500 MM	$700MM	$0-$250MM

The above does not include equipment leases. Also, project debt, debt at JVs, and contract monetizations (as the only Enron obligation here is to deliver gas and power) are not given consideration in the above calculation.

In addition, Enron uses a myriad of structured financings, including:

Transaction	Size	Purpose	Take-Out
Condor	$1,500	Nighthawk Refinancing/Asset Monetizations	Equity
Rawhide	750	Minority Interest Equity/ Asset Monetizations	Cash Flow/Asset Sales/Refinancings
Marlin	550	Wessex acquisition finance	Equity
Firefly	415	Elektro acquisition finance	Equity
Total	**$3,215**		

EOG:
Enron announced and completed a share exchange agreement with Enron Oil and Gas early in the third quarter of 1999, which established EOG as a company independent of Enron. Under the agreement, Enron exchanged roughly 80% of its 82 million shares of EOG common stock for EOG's China and India operations. In connection with the exchange, EOG contributed $700 million in cash to one of EOG's India subsidiaries. Concurrent with the share exchange, Enron sold exchangeable notes, which are mandatorily exchangeable into 11.5 million EOG common stock currently owned by Enron. As a result, upon closing of the transaction in late August, Enron's ownership of EOG was eliminated entirely, and the EOG board of directors was renamed, with all Enron officers and directors resigning their positions on the EOG board.

Although EOG has long been regarded as one of the lowest cost E&P companies in North America, management believed that the capital commitments required of an exploration and production operation had become too substantial for the risk inherent in

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the business (i.e. the risk of dry holes and commodity prices). Enron management would rather re-deploy this capital along other business lines in an effort to facilitate a midstream/downstream integrated energy approach. The ultimate divestiture of EOG had been anticipated since 4Q98.

Enron Corp. ($ in Millions)	EBITDA	Total Debt	Total Equity	Debt/Cap.	Debt/EBITDA	EBITDA/Int.
December 31, 1998	2,266	8,358	9,191	47.6%	3.7x	3.2x
LTM June 30, 1999	2,338	9,980	11,681	46.1%	4.3x	3.0x
LTM Pro Forma for Share Exchange	1,888	7,940	11,681	40.5%	4.2x	2.9x

Given that EOG was consolidated on Enron's balance sheet: (i) all assets and liabilities, including debt of $1.2 billion were de-consolidated; (ii) the incremental cash flow provided by EOG (roughly $450MM for 1998) is gone; and (iii) interest expense at Enron will be reduce going forward by approximately $140 million (based upon a 7% interest rate, and assuming the $700 million cash from the share exchange and $200 million cash, net of transaction costs, from the exchangeable notes are applied towards outstanding debt).

Enron also had approximately $7.4 billion of debt at unconsolidated subsidiaries at December 31, 1998. With the consolidation of Elektro, deconsolidation of EOG, and the inclusion of debt at unconsolidated subsidiaries, the company is expected to have pro-forma total debt/book capitalization of 48% at year-end 1999.

Conclusion:
In summary, despite financial market uncertainty and commodity price volatility (over the last two years), Enron continues to demonstrate an ability to generate solid cash flow and predictable earnings, all-the-while significantly growing its asset base and market presence. At the root of this success is a stable, yet diversified, operating system which affords management the opportunity to grow and seek out new market share. Among integrated energy companies, Enron appears well-positioned in two areas regarded as critical to global energy: (i) the deregulation of wholesale and retail energy markets in developed economies; and (ii) the privatization of energy and utility infrastructure in emerging economies. The company is also aggressively pursuing market share in other "new" energy markets, including wind and solar power, and in communications, business that many believe will blossom in near future.

H. SUMMARY OF PROJECTIONS

Citibank will assume Enron credit risk as part of the proposed transaction. The company is currently rated BBB+/Baa2, and we expect Enron to maintain investment grade ratings going forward. In keeping with other transactions approved for investment grade companies, Enron projections have not been provided.

I. SECURITY/COLLATERAL

There is no security or collateral related to the proposed transaction. However, the returns from the Total Return Swap are backed by a Recovery Rate Swap with SSB that equates Citibank exposure on the proposed transaction to exposure under a Senior Unsecured credit facility. If actual recovery is greater than 50%, Citibank will receive a windfall from the Yosemite Trust. Please see Exhibit 4 – Yosemite Equity Investment for a more detailed description.

J. KEY COVENANTS

There are no covenants related to the proposed transaction.

K. WAYS OUT

Cash Flow
Enron generated $2.4 billion of EBITDA in the last twelve months ended June 30, 1999, and maintained EBITDA/Interest coverage of 3.0x. The company's EBITDA was $2.3 billion in 1998, and EBITDA/Interest coverage was 3.2x. We expect the company to maintain an EBITDA/Interest cover of at least 3.0x over the tenor of the transaction.

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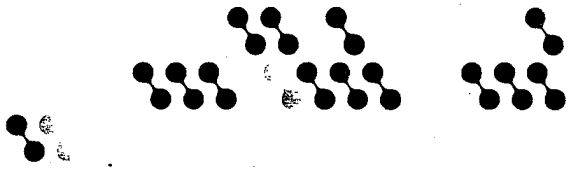
Refinancing

Enron maintains access to the bank and capital markets by virtue of investment grade ratings of BBB+/Baa2 at Standard and Poor's and Moody's, respectively. The proposed transaction is being used to refinance existing Enron debt, which reflects the company's ability to restructure its balance sheet. We expect the company to maintain financial flexibility over the tenor of the transaction.

L. EXHIBITS

1. CA
2. CITICORP INDUSTRY REVIEW
3. YOSEMITE TRANSACTION MEMO
4. YOSEMITE EQUITY INVESTMENT
5. YOSEMITE FUNDED PREPAID DESCRIPTION
6. DERIVATIVE TRANSACTIONS DESCRIPTION

CONFIDENTIAL CITI-SPSI 0003004



Finance Committee Meeting

August 13, 2001

| Committee Members |

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. Paulo V. Ferraz Pereira
Mr. Frank Savage

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Permanent Subcommittee on Investigations
EXHIBIT #186b

ENRON
Endless possibilities.™

FC 000057994

rt S. Winokur, Jr., Chairman
t A. Belfer
an P. Blake, Jr.
e C. Chan
V. Ferraz Pereira
Savage

AGENDA
Meeting of the Finance Committee of the Board of Directors of Enron Corp.

5:00 p.m. (CDT), August 13, 2001
50th Floor Boardroom, Enron Building
Houston, Texas

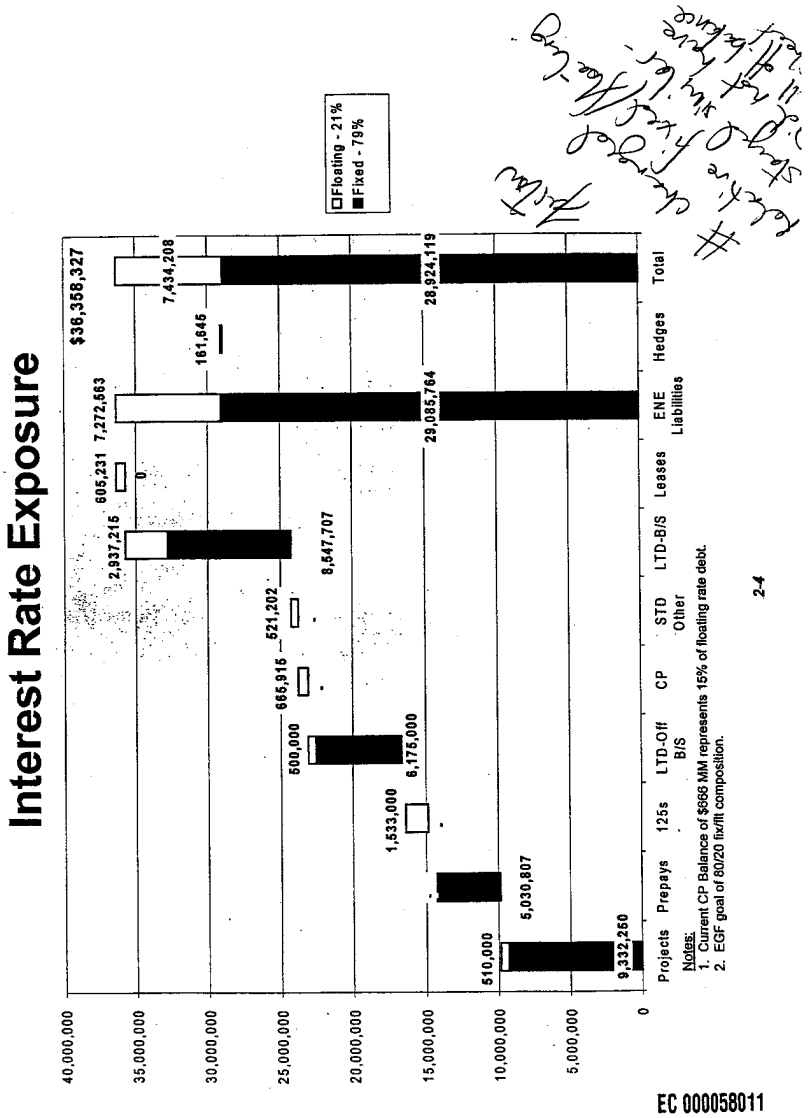
		Page
roval of April 30, 2001 Finance Committee Minutes	**Mr. Winokur**	1-1
ef Financial Officer Report	**Mr. Fastow**	2-1
asurer Report	**Mr. Glisan**	3-1
ef Risk Officer Report	**Mr. Buy**	4-1
Quarterly Risk Update		
- Enron's Assets		4-2
- Trade Credit Update		4-3
- Investment Portfolio		4-13
- Enron Energy Services		4-17
- Market Risk Update		4-21
ects and Amendments		5-1
A) **Brokerage Account Authorization**	**Mr. Glisan**	5A-1
- Approve for Recommendation to the Board		
er Business		6-1
ourn		7-1

See Addendum for Deal Approval Sheets approved between Board meetings

Enron Corp

Chief Financial Officer Report
August 13, 2001

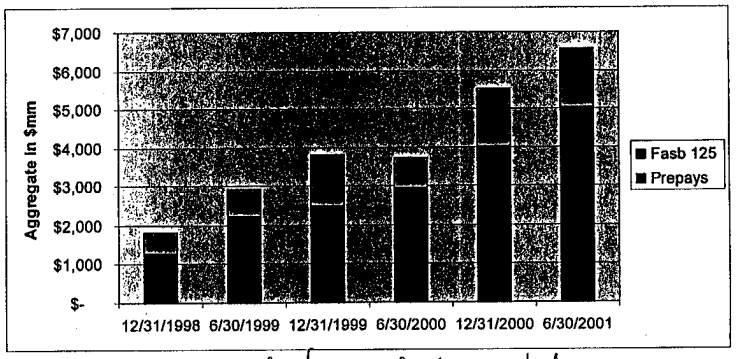
2-1


Interest Rate Exposure
Floating - 21%
Fixed - 79%
$36,358,327
7,434,208
161,646
28,924,119
7,272,563
605,231
0
29,085,764
2,937,215
8,647,707
521,202
665,915
500,000
6,176,000
1,533,000
5,030,807
510,000
9,332,260
40,000,000
35,000,000
30,000,000
25,000,000
20,000,000
15,000,000
10,000,000
5,000,000
0
Projects
Prepays
125s
LTD-Off B/S
CP
STD Other
LTD-B/S
Leases
ENE Liabilities
Hedges
Total
Notes:
1. Current CP Balance of $666 MM represents 15% of floating rate debt.
2. EGF goal of 80/20 fix/flt composition.
2-4
EC 000058011

Finance Related Asset Sales

Prepays and 125 Sales ($MM)

	12/31/1998	6/30/1999	12/31/1999	6/30/2000	12/31/2000	6/30/2001
Prepays	$ 1,258	$ 2,239	$ 2,489	$ 2,962	$ 4,016	$ 5,031
Fasb 125	$ 573	$ 683	$ 1,316	$ 772	$ 1,521	$ 1,533
	$ 1,831	$ 2,922	$ 3,805	$ 3,734	$ 5,537	$ 6,564



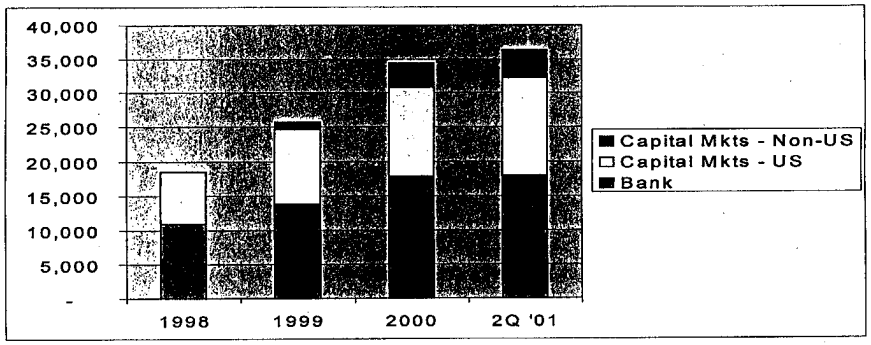
EC 000058012

1135

epays - financing to bring cash forward to match earnings
FAS 125 monetize portion of generate cash flow & earnings

Outstanding Financings and Debt

($MM)



	1998		1999		2000		2Q '01	
	Year End Outstanding	% of Total	Year End Outstanding	% of Total	Year End Outstanding	% of Total	Quarter End Outstanding	% of Total
Bank	10,885	59%	13,807	54%	17,933	52%	17,954	50%
Cap Mkt - US	7,674	41%	10,870	42%	12,897	38%	14,302	39%
Cap Mkt - Non US	-	0%	1,037	4%	3,549	10%	4,102	11%
Total	$ 18,559	100%	$ 25,714	100%	$ 34,379	100%	$ 36,358	100%

Access to capital markets. Moving out of bank markets

EC 000058013

ASF - Detail on Outstanding Fundings

	1998	1999	2000	2Q '01
Bank	**10,885**	**13,807**	**17,933**	**17,954**
Corp	760	1,334	1,393	895
Unconsolidated Equity Affil - 100%	7,176	7,841	9,717	8,622
Prepay	1,163	2,490	4,016	5,031
125/Monetization	573	1,415	1,539	1,533
Nighthawk	485	-	-	-
Rawhide	728	728	718	718
Zephyrus	-	-	500	500
Valhalla	-	-	50	50
Leases	-	-	-	605
Capital Mkts - US	**7,674**	**10,870**	**12,897**	**14,302**
On Balance Sheet	5,790	6,294	7,881	9,801
NBPL & FPL	446	646	1,221	1,221
Osprey	-	1,400	2,150	2,150
Marlin	1,024	830	830	315
Firefly	415	415	-	-
Yosemite 1		800	800	800
Nahanni	-	485	15	15
Capital Mkts - Non-US	**-**	**1,037**	**3,549**	**4,102**
On Balance Sheet	-	530	955	1,193
Osprey Euros = 315 Euros	-	-	297	297
Margaux	-	-	95	95
Wessex Water Bond	-	507	507	507
Marlin				315
Azurix Bond	-	-	590	590
Yosemite II	-	-	359	359
Yosemite III - GBP	-	-	747	747
Total	**18,559**	**25,714**	**34,379**	**36,358**

EC 000058017

ASF – Detail on Prepays

Prepay	Term	Inflows	Dec-98	Jun-99	Dec-99	Jun-00	Dec-00	Jun-01
Gas: Chase II	Sep 95 - Oct 00	224,440	3,706	2,647	413	-	-	-
Gas: Chase II	Dec 96 - Jan 00	225,021	(184,851)	(107,536)	(40,984)	(13,872)	9	(9)
Gas: Chase IV	Dec 97 - Dec 01	299,992	(252,755)	(210,151)	(171,146)	(129,995)	(88,390)	(45,605)
Gas: Chase V	Jun 98 - Jul 02	250,000	(240,721)	(205,192)	(173,603)	(140,448)	(107,499)	(74,027)
Gas: Energy America	Jun 98 - May 08	38,443	(40,482)	(37,577)	(35,359)	(34,291)	(35,046)	(34,439)
Gas: Chase VII (APEA)	Apr 99 - Apr 11	287,611	-	(271,687)	(263,745)	(256,654)	(263,192)	(258,729)
Gas: Chase VIII	Jun 99 - Jun 04	500,000	-	(507,324)	(486,471)	(435,179)	(393,457)	(350,083)
Gas: Cage	Sep 99 - Sep 00	(250)	-	-	418	529	-	-
Gas: Chase IX	Jun 00 - Jun 05	648,374	-	-	-	(661,938)	(658,136)	(604,936)
Gas: Chase X	Dec 00 - Nov 05	328,258	-	-	-	-	(340,279)	(332,242)
Gas:Citibank I	Jun 01 - Dec 01	250,000						(250,592)
Power: CRRA	Mar 01 - May 12	220,180		-	-	-	-	(227,421)
Crude: Chase IV	Dec 98 - Dec 02	249,994	(254,387)	(242,756)	(193,753)	(172,332)	(139,846)	(133,051)
Crude: Delta	Dec 98 - Nov 99	190,000	(189,917)	(121,407)				
Crude: Truman	Jun 99 - Sep 99	500,000	0	(488,809)				
Crude: Jethro	Sep 99 - Nov 99	675,000	0					
Crude: Yosemite I	Dec 99 - Dec 04	800,000	0	-	(797,744)	(795,157)	(832,326)	(760,194)
Crude: Yosemite II	Feb 00 - Jan 07	324,000	0	-	-	(322,982)	(332,814)	(319,751)
Crude: Yosemite III	Aug 00 - July 05	472,000	0	-	-	-	($506,056)	(523,597)
Crude: Chase II	Dec 00 - Dec 01	315,000		-	-	-	($319,288)	(304,546)
Crude: Yosemite II Bridge		315,000			(327,298)			
Crude: Citibank-Mahil	Ended 12/99		(46,973)	(23,111)		-	$0	-
Crude: Chase III	Ended 11/99		(51,999)	(26,116)	-	-	$0	-
Crude: Citibank FX Hedge	May 01 - Apr 06							(12,075)
Crude: Citibank USD	May 01 - Apr 06	474,781						(489,973)
Crude: Citibank GBP	May 01 - Apr 06	156,732						(158,434)
Crude: Citibank EUR	May 01 - Apr 06	149,956						(151,103)
Total		$7,894,532	$(1,258,379)	$(2,239,019)	$(2,489,272)	$(2,962,319)	$(4,016,320)	$(5,030,807)

EC 000058019

1138

No

Yosemite Update

Original Objectives	Current Comments
Reduce bank exposure/ increase bank liquidity	• Bank exposure to Enron can be reduced on a "transaction" basis via 100% buyout or on a "target bank" basis via credit default swaps
Maintain existing balance sheet treatment of transactions	• The Yosemite SPV will not be consolidated. When loans are purchased, the underlying accounting treatment will remain unchanged as Yosemite will simply replace the banks as the lender under the original documentation
Warehousing capability	• The Citibank Swap combined with the Enron credit-linked notes provides for a unique "black box" feature which provides considerable flexibility for substitution
Expand investor base beyond commercial banks/top tier institutional investors	• Investors in capital markets have ability to purchase a synthetic ENE Bond through black box feature • Black box allows Enron the ability to provide a permanent take-out feature for highly structure transactions in the capital markets while limiting disclosure of prepay to Citibank. Limitations are ability of Citi to wear the basis risk and a restriction on the maturity date to match the Yosemite maturity
Cost-efficient source of funding	• In certain cases, Yosemite can underwrite • Demonstration of vehicle for permanent take-out of bank financings provides benefits of increased competition to banks

Permanent Subcommittee on Investigations
EXHIBIT #186c

Evolution of Yosemite

- Basis Pricing
  - Assumed zero cost initially
  - Pricing inefficient from Citi; Erring on the expensive side
- Bond Pricing
  - Assumed cost of ____ bps
  - Bonds have gapped 50 bps

Yosemite is still a capital market black box for structure bank deals
  - Immediate use is for prepay funding

ECa00196340

Optional Use as Prepay Funding Vehicle

- Need for prepay financings to generate FFO are anticipated to be ~$1Bn/yr
- Continued use of bank financings for prepay transactions are limited by the following:
  - Banks are reluctant to provide longer-term funded prepays; either a premium is paid for the longer tenor or continued refinancing risk is assumed if a shorter tenor is chosen
  - Finite capacity exists in the surety market and bank market; each incremental deal will likely be more expensive
  - Traditional bank prepays include exposure through the commodity swaps as well as the loan exposure
  - The use of prepays as a monetization tool is a sensitive topic for both the rating agencies and banks/institutional investors. The ability to continue minimizing disclosure will likely be compromised if transactions continue to be syndicated.

ECa00196341

Yosemite Cost Analysis

Yosemite - CLNs	
	5 yr
Note Amount	$ 750,000,000
Equity Amount	50,000,000
ENE Bond (bps)	60
New Issue (bps)	10-20
144A Premium (bps)	10-15
Liquidity (bps)	10-15
Structuring (bps)	50
	140-160
Misc (admin, swap, basis)	22.5-27.5
Annualized upfront	12.4
Equity cost	7.5-15
All-in Cost over LIBOR (bps)	**182.4-214.9**
$ impact after-tax on EPS over comparable	**$(0.0059 - 0.0076)**
7 yr Incremental All-in Cost	7.5

Chase Mohonia Alternative 1	
	5 yr
Note Amount	$800,000,000
Enron Funded Spread (bps)	60
Surety Bond Premium	16.2
	76.2
Misc (handling fees, etc.)	5
Annualized upfront	5
All-in Cost over LIBOR (bps)	**86.2**
$ after-tax impact on EPS	**$(.0057)**
7 yr Incremental All-in Cost	5

ECa00019634 2

Yosemite Cost Analysis

Yosemite - CLNs	
	5 yr
Note Amount	$ 750,000,000
Equity Amount	50,000,000
ENE Bond (bps)	60
New Issue (bps)	10-20
144A Premium (bps)	10-15
Liquidity (bps)	10-15
Structuring (bps)	50
	140-160
Misc (admin, swap, basis)	22.5-27.5
Annualized upfront	12.4
Equity cost	7.5-15
All-in Cost over LIBOR (bps)	**182.4-214.9**
$ after-tax impact on EPS over comparable	**$0.0008-(.0009)**
7 yr Incremental All-in Cost	7.5

Chase Mohonia Alternative 2	
	5 - 7 yr
Note Amount	$ 800,000,000
Enron Funded Spread (bps)*	60
Tenor Spread	25
LC Backstop	87.5
	172.5
Misc (handling fees, etc.)	5
Annualized upfront	10
All-in Cost over LIBOR (bps)	**187.5**
$ after-tax impact on EPS	**$(.0125)**
7 yr Incremental All-in Cost	5

ECa00196343

Yosemite Cost Analysis

Yosemite - CLNs	
	5 yr
Note Amount	$ 750,000,000
Equity Amount	50,000,000
ENE Bond (bps)	60
New Issue (bps)	10-20
144A Premium (bps)	10-15
Liquidity (bps)	10-15
Structuring (bps)	50
	140-160
Misc (admin, swap, basis)	22.5-27.5
Annualized upfront	12.4
Equity cost	7.5-15
All-in Cost over LIBOR (bps)	**182.4-214.9**
$ after-tax impact on EPS over comparable	**$(.0038-.0055)**
7 yr Incremental All-in Cost	7.5

Chase Mohonia Alternative 3	
	5 - 7 yr
Note Amount	$ 800,000,000
Enron Funded Spread (bps)	60
Tenor Spread	25
Surety Bond Premium	16.2
	101
Misc (handling fees, etc.)	5
Annualized upfront	10
All-in Cost over LIBOR (bps)	**116.2**
$ after-tax impact on EPS	**$(.0078)**
7 yr Incremental All-in Cost	5

ECa00019634

Yosemite Cost Analysis

Yosemite - CLNs	
	5 yr
Note Amount	$ 750,000,000
Equity Amount	50,000,000
ENE Bond (bps)	60
New Issue (bps)	10-20
144A Premium (bps)	10-15
Liquidity (bps)	10-15
Structuring (bps)	50
	140-160
Misc (admin, swap, basis)	22.5-27.5
Annualized upfront	12.4
Equity cost	7.5-15
All-in Cost over LIBOR (bps)	**182.4-214.9**
$ after-tax impact on EPS over comparable	**$.0000-.0007**
7 yr Incremental All-in Cost	7.5

Citi Alternative - Bank Funded with Margin	
	5 yr
Note Amount	$ 800,000,000
Enron Funded Spread (bps)	60
Structuring	40-65
	100-125
Misc (arrangement, derivative fee.)	65-77
Annualized upfront	10
All-in Cost over LIBOR (bps)	**175-212**
$ impact after-tax on EPS	**$(.0116-0141)**
7 yr Incremental All-in Cost	5

ECa00019634S

Yosemite Cost Analysis

Yosemite - CLNs	5 yr
Note Amount	$ 750,000,000
Equity Amount	50,000,000
ENE Bond (bps)	60
New Issue (bps)	10-20
144A Premium (bps)	10-15
Liquidity (bps)	10-15
Structuring (bps)	50
	140-160
Misc (admin, swap, basis)	22.5-27.5
Annualized upfront	12.4
Equity cost	7.5-15
All-in Cost over LIBOR (bps)	**182.4-214.9**
$ after-tax impact on EPS over comparable	**$.0035-.0051**
7 yr Incremental All-in Cost	7.5

Citi Alternative - Bank Funded w/o Margin	5 yr
Note Amount	$ 800,000,000
Enron Funded Spread (bps)	60
Structuring	40-65
	100-125
Misc (arrangement, derivative fee.)	118-142
Annualized upfront	10
All-in Cost over LIBOR (bps)	**228-277**
$ impact after-tax on EPS	**$(.0151-.0184)**
7 yr Incremental All-in Cost	5

ECa000196346

Yosemite Cost Analysis

Yosemite - CLNs	
	5 yr
Note Amount	$ 750,000,000
Equity Amount	50,000,000
ENE Bond (bps)	60
New Issue (bps)	10-20
144A Premium (bps)	10-15
Liquidity (bps)	10-15
Structuring (bps)	50
	140-160
Misc (admin, swap, basis)	22.5-27.5
Annualized upfront	12.4
Equity cost	7.5-15
All-in Cost over LIBOR (bps)	**182.4-214.9**
$ after-tax impact on EPS over comparable	**$.0010-.0019**
7 yr Incremental All-in Cost	7.5

Citi Alternative- CXC w/o Margin	
	5 yr
Note Amount	$ 800,000,000
Program Fee	25-30
Liquidity Backstop (bps)	25-30
	50-60
Surety Bond	10-15
Credit Enhancement	2
	62-77
Misc. (arrangement, derivative)	118-142
Annualized upfront	10
All-in Cost over LIBOR (bps)	**190-229**
$ impact after-tax on EPS	**$(.0126-.0152)**
7 yr Incremental All-in Cost	5

ECa00019634?

Yosemite Cost Analysis

Yosemite - CLNs	
	5 yr
Note Amount	$ 750,000,000
Equity Amount	50,000,000
ENE Bond (bps)	60
New Issue (bps)	10-20
144A Premium (bps)	10-15
Liquidity (bps)	10-15
Structuring (bps)	50
	140-160
Misc (admin, swap, basis)	22.5-27.5
Annualized upfront	12.4
Equity cost	7.5-15
All-in Cost over LIBOR (bps)	**182.4-214.9**
$ after-tax impact on EPS over comparable	**$(.0026-.0024)**
7 yr Incremental All-in Cost	7.5

Citi Alternative- CXC with Margin	
	5 yr
Note Amount	$ 800,000,000
Program Fee	25-30
Liquidity Backstop (bps)	25-30
	50-60
Surety Bond	10-15
Credit Enhancement	2
	62-77
Misc. (arrangement, derivative)	65-77
Annualized upfront	10
All-in Cost over LIBOR (bps)	**137-164**
$ impact after-tax on EPS	**$(.0091-.0109)**
7 yr Incremental All-in Cost	5

ECa00196348

Yosemite Cost Analysis

Condor	
	5 yr
Note Amount	$ 1,400,000,000
Equity Amount	100,000,000
Marlin Notes	165
New Issue (bps)	25
Curve for 3 Year	10
Structuring	25-50
	225-250
Annualized upfront	29
Equity Cost	29-31
All-in Cost over LIBOR (bps)	**283-310**
$ after-tax impact on EPS	**$(.0319-.0351)**
(over 3yr treasuries 5.85%)	

Yosemite - Firefly	
	5 yr
Note Amount	$ 415,000,000
Equity Amount	25,937,500
ENE Bond (bps)	60
New Issue (bps)	10-20
144A Premium (bps)	10-15
Liquidity (bps)	10-15
Structuring	50
	140-160
Misc (admin, swap, basis)	90-95
Annualized upfront	12.4
Equity Cost	7.5-15
All-in Cost over LIBOR (bps)	**249.9-282.4**
$ after-tax impact on EPS	**$(.0089 - .0098)**
7 yr Incremental All-in Cost	7.5

ECa000196349

Yosemite/Prepay Analysis

Yosemite provides distinct advantages in conjunction with a prepay:

- A longer-dated prepay (10+ years) can be accommodated within Yosemite to eliminate refinancing risk without any incremental costs other than the normal bond tenor costs
- A new prepay model has been developed to fit within the Yosemite structure which eliminates the need for any commodity swap exposure
- Disclosure of the prepay transaction would be limited to Citibank
- Yosemite can underwrite the transaction
- Modifications can be achieved through Citibank as opposed to a syndicate bank group

ECa00196350

Conclusions & Recommendations

- Benefits of proceeding with Yosemite vehicle are as follows:
  - Minimal effect on EPS
  - Permanent housing for highly structured deals
  - Relieves banks of Enron capacity; increases investor base
  - Flexibility in deals used as asset base
  - New product in the market with the Enron name

ECa00196351

Yosemite

How do they fall out into I, II and III?

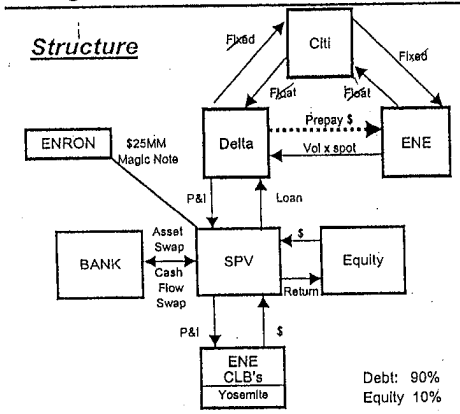
—

Permanent Subcommittee on Investigations
EXHIBIT #186d

EC2 000011598

Original Yosemite

Structure



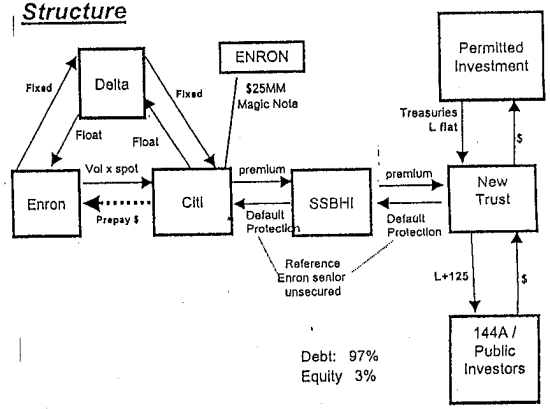
CLB = Credit Linked Bonds

Highlights

- Blackbox / flexibility to substitute
- 144 A no reg rights only
- Faster execution: Same documentation
  No structural changes
  Sold as same deal
- No use of Citibank balance sheet
- Marketing: Enron story only
- Timing - 4 weeks

CLN

Structure



Highlights

- Blackbox / flexibility to substitute
- Public registration option
- Slower execution: Primarily same documentation
  Some structural changes
  Sell as different, improved structure
- Use of Citibank balance sheet (no mark against credit)
- Marketing: Potential for Citibank story--less of Enron story depending on the size of the transaction.
- Timing 6-8 weks with out reg rights

Very similar to the original Yosemite structure with a few basic improvements. Open issues are as follows:

EC2 000011599

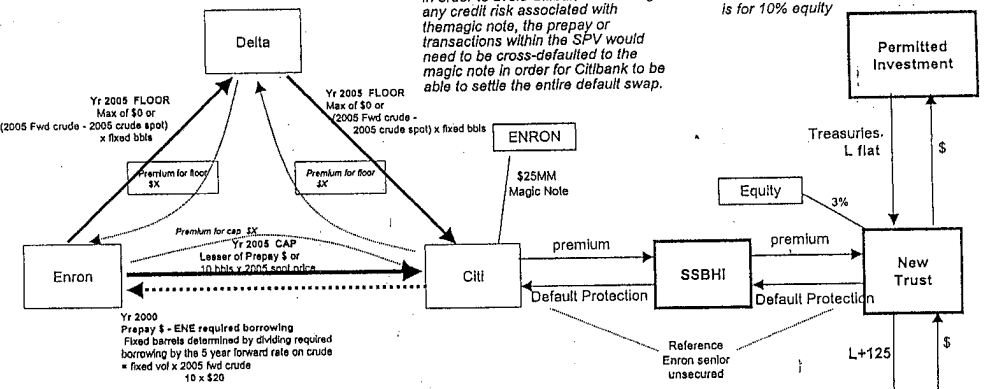
EO 000037712

Open issues on CLN Structure

Upfront Fees:
Amortize or expense immediately.
Would obviously like to capitalize and amortize over the life of the CLN term.

$ 25 MM Magic Note
In order to avoid Citibank absorbing any credit risk associated with themagic note, the prepay or transactions within the SPV would need to be cross-defaulted to the magic note in order for Citibank to be able to settle the entire default swap.

SPV Permitted Investments:
Use of GIC or Salomon floating rate note would allow for Grantor Trust treatment which could minimize the equity requirement to 3%. Without a Grantor Trust tax pressure is for 10% equity



Placement of Equity:
We structured the swap such that Citibank would be over-collateralizd in its equity position in the prior transaction. If we use the same concept, it will add some complexity to the swap document but it was not questioned at all by the rating agencies or investors. Citibank may need outside equity of 3% however which means they may not be the optimal party to hold the equity.

Categories of Deliverable Obligations:
Critical difference in the structure which would allow for registration and provide the investors with greater understanding of specific types ofsenior unsecured Enron paper representing their ultimate collateral. Limitations on deliverable obligations may limit our ability to substitute with Citibank-- (i.e. they may be less inclined to wrap a transaction which they do not feel would fit the deliverable obligation definition.

EC 000037713

EC2 000011600

11154

Timeline for Open issues

CLN Structure
Very similar to the original Yosemite structure with a few basic improvements. Open issues are as follows:

Issues:		Action	Timeline
SPV Permitted Investments:	Use of GIC or Salomon floating rate note would allow for Grantor Trust treatment which could minimize the equity requirement to 3%	Discuss with Tax & confirm no need for any equity, 3% is only to satisfy accounting	Complete by Friday (July 7)
Categories of Deliverable Obligations:	Critical difference in the structure which would allow for registration and provide the investors with greater understanding of specific types of senior unsecured Enron paper representing their ultimate collateral. Limitations on deliverable obligations may limit our ability to substitute with Citibank--they may be less inclined to wrap a transaction which they do not feel would fit the deliverable definition.	Finance review along with with legal review.	Obtain V&E assessment and Milbank will obtain preliminary view from SEC as to the basic concept by next week
$ 25 MM Magic Note	In order to avoid Citibank absorbing any credit risk associated with the magic note, the prepay or transactions within the SPV would need to be cross-defaulted to the magic note in order for Citibank to be able to settle the entire default swap.	Discuss with internal acct.	Answer by Friday (July 7)
Upfront Fees:	Amortize or expense immediately. Would obviously like to capitalize and amortize over the life of the CLN term.	Discuss with internal acct/crude desk	Answer by Friday (July 7)
Placement of Equity:	We structured the swap so that Citibank would be over-collateralized in its equity position in the prior transaction. If we use the same concept, it will add some complexity to the swap document but it was not questioned at all by the rating agencies or investors. Citibank may need outside equity of 3% however which means they may not be the optimal party to hold the equity.	Open	Open

EC2 000011601

EC 000037714

1155

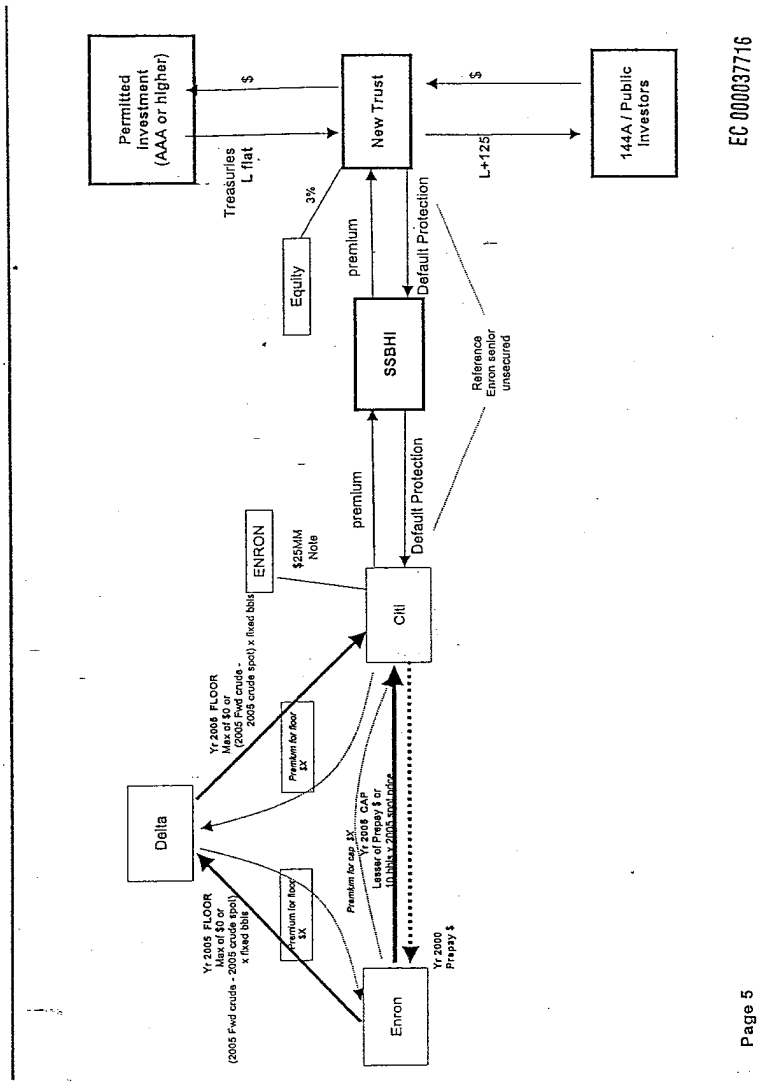
Yosemite Pricing Breakdown

Pricing Comparison (5 year transaction--Fixed Libor basis)	Yosemite	CLN--Public	CLN--144A
ENE Corporate	60.00	60.00	60.00
New Issue Premium	10.00-20.00	10.00-20.00	10.00-20.00
144A Premium	15.00	na	15.00
Illiquidity Premium	15.00	10.00	15.00
Structural Premium	50.00	40.00-50.00	40.00-50.00
Subtotal Premium	90.00-100.00	60.00-80.00	80.00-100.00
Bond Pricing	150.00-160.00	120.00-140.00	140.00-160.00
Certificates--(9% of capitalization)	25.00	na	na
Citibank:			
Prepay Basis Risk	12.50	12.50	12.50
Regulatory Capital Charge	15.00	na	na
AAA Asset Risk	na	10.00	10.00
Balance Sheet Charge	na	12.50	12.50
Subtotal Citibank	27.50	35.00	35.00
All-in Spread Charge	202.50-212.50	155.00-175.00	175.00-195.00
Delta		37.50-47.50	17.50-27.50

1156

EC2 000011602

EC 000037715



EC2 000011603

Sherman, Cris

From: Walden, Clint
Sent: Tuesday, November 13, 2001 9:56 AM
To: Sherman, Cris

I do not have individual structure charts. I have attaced a chart that we did when we were putting together ECLN 1. It compares the structures side by side. Page 1 shows the two structures. The one on the left is YO 1 & 2 , while the one on the right is ECLN 1 & 2 (YO 3& 4). One difference to note is that in the diagram, it indicates that there is a 97/3 structure. However, each YO 1&2 and ECLN 1&2 are capitalized 90/10. Call me if you have any questions.

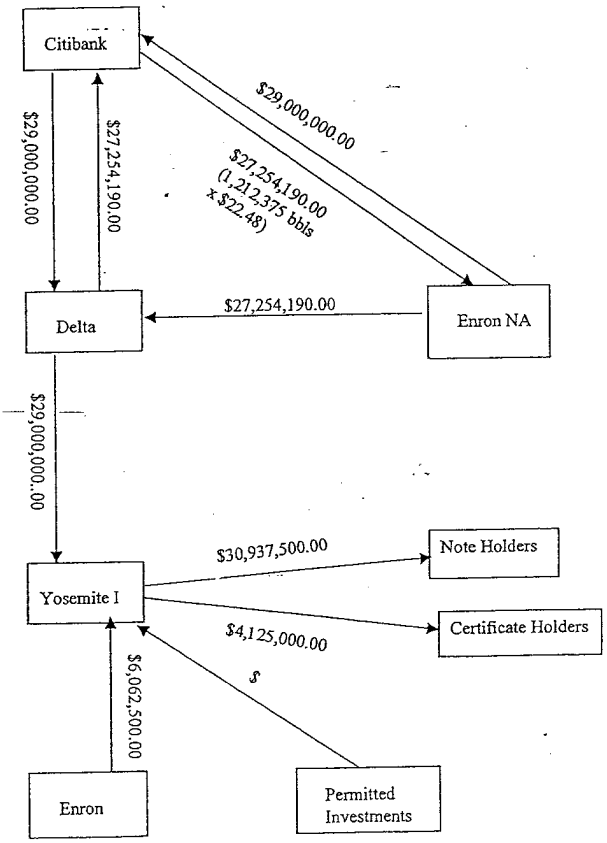
Yosemite #3.ppt

EC 000037717

EC2 000011604

10/01

Yosemite Securities Trust I



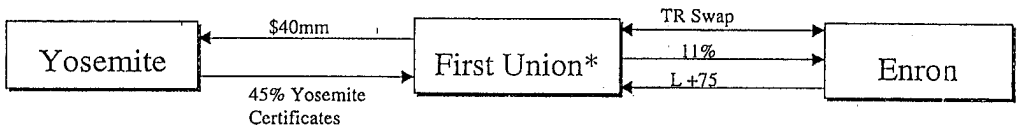
EC 000037718

EC2 000011605

Yosemite Certificates

EC2 000011606

Option 1

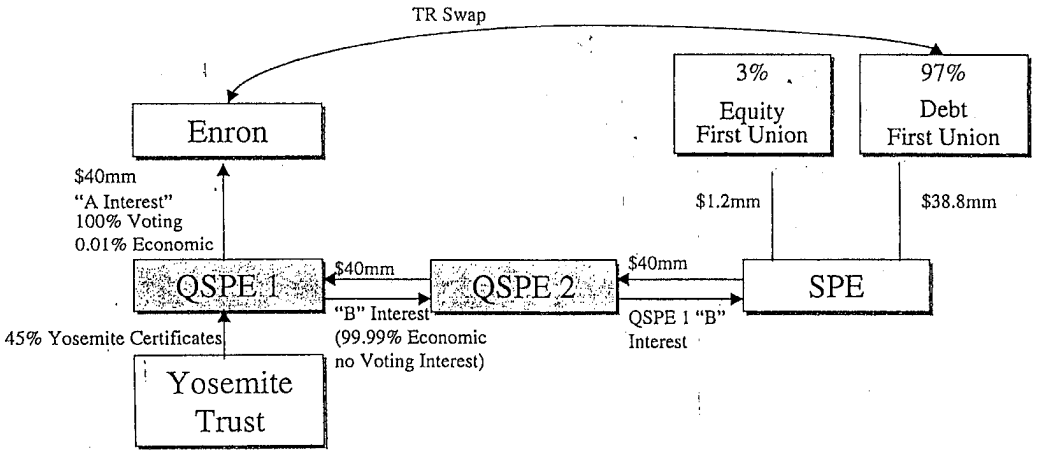


* First Union Bank, N.A. or non-SPV subsidiary

12/14/99

Yosemite Certificates

Option 2*

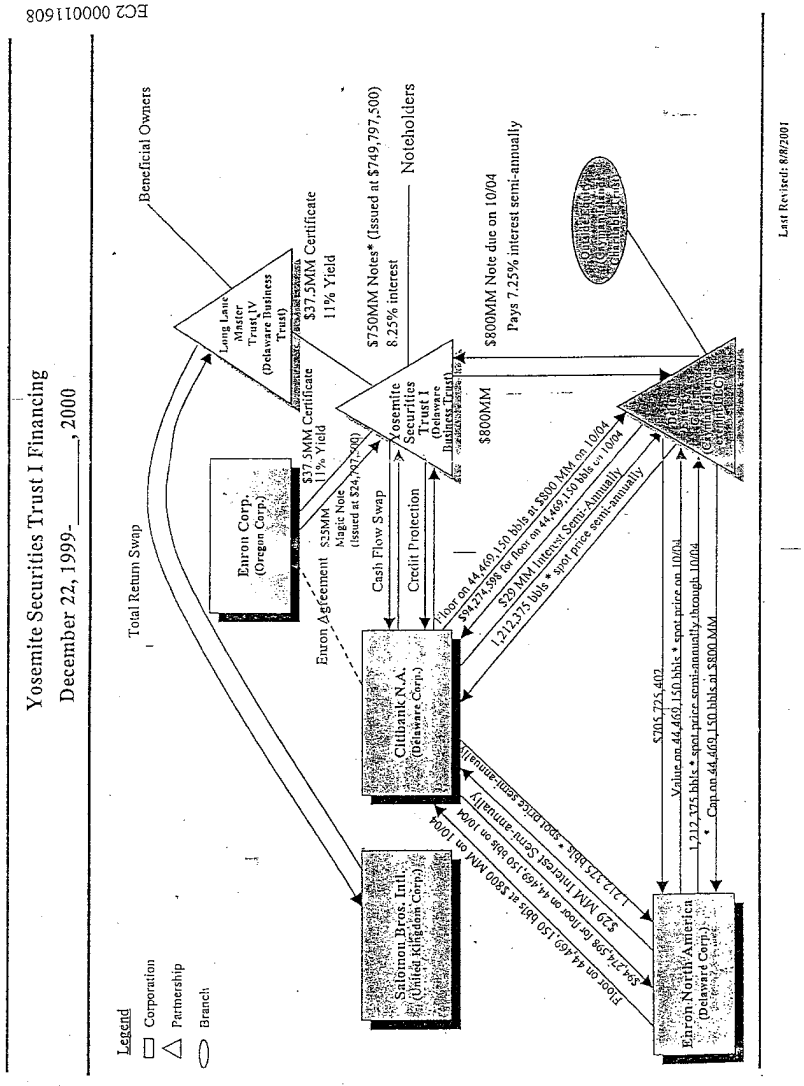


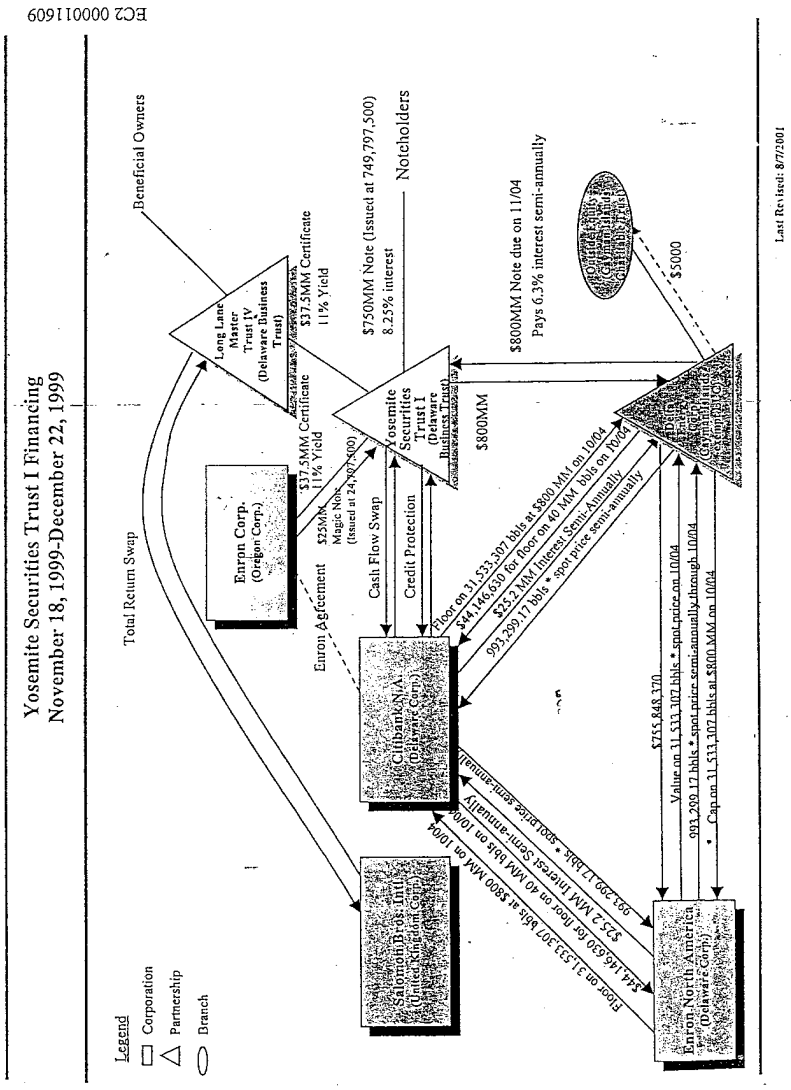
* Structure as "true sale" or "true issuance"

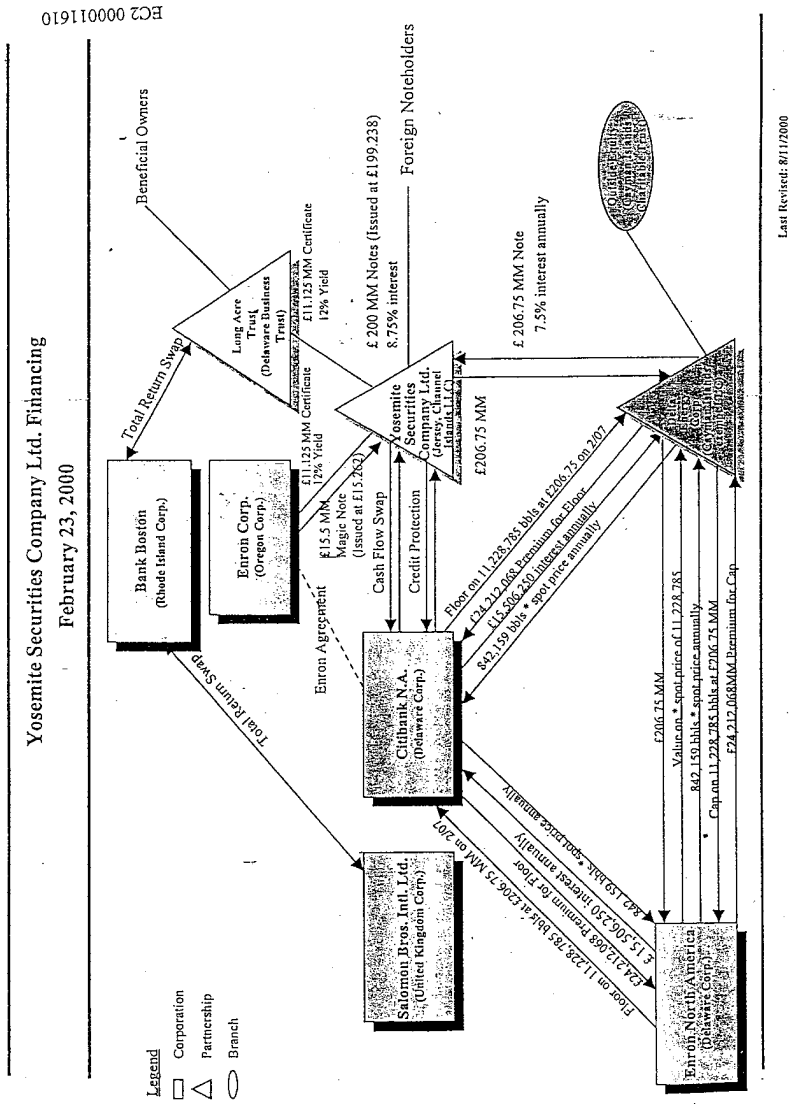
12/14/99

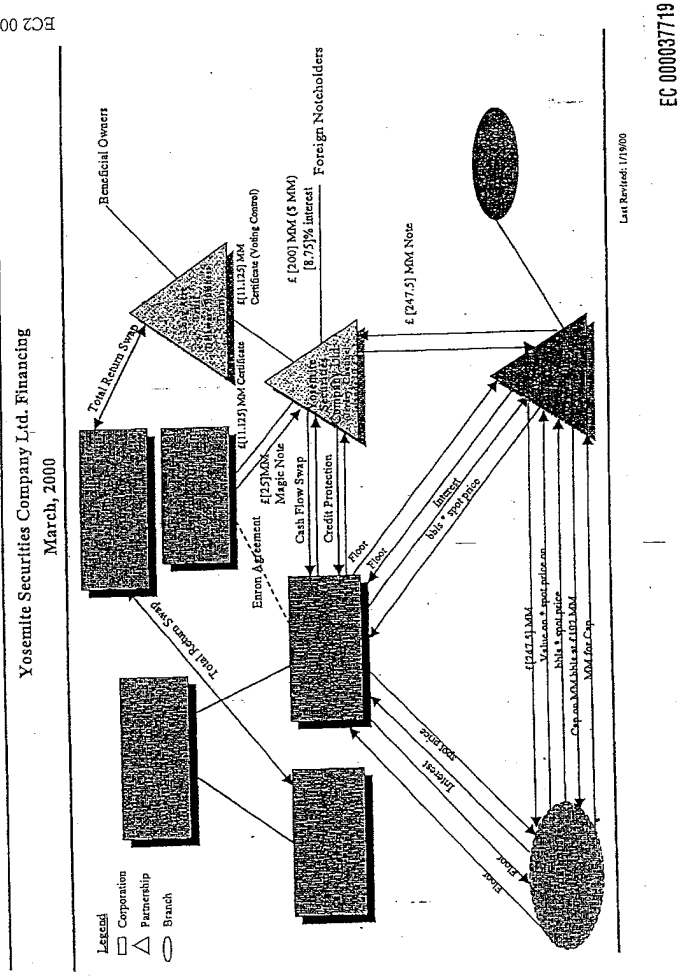
EC2 000011607

EC2 000011608




EC2 000011609
Yosemite Securities Trust I Financing
November 18, 1999-December 22, 1999
Legend
Corporation
Partnership
Branch
Beneficial Owners
Total Return Swap
Long Lane Master Trust IV (Delaware Business Trust)
$37.5MM Certificate
11% Yield
$750MM Note (Issued at 749,797,500)
8.25% interest
Noteholders
$800MM Note due on 11/04
Pays 6.3% interest semi-annually
$5000
Enron Corp. (Oregon Corp.)
$37.5MM Certificate
11% Yield
Enron Agreement
$25MM Magic Note (Issued at 24,797,500)
Yosemite Securities Trust I (Delaware Business Trust)
$800MM
Cash Flow Swap
Credit Protection
Floor on 31,533,307 bbls at $800 MM on 10/04
$44,146,630 for floor on 40 MM bbls on 10/04
$25.2 MM Interest Semi-Annually
993,299.17 bbls * spot price semi-annually
Citibank, N.A. (New York Corp.)
Salomon Brothers Holding Co. Inc. (Delaware Corp.)
Floor on 31,533,307 bbls at $800 MM on 10/04
$44,146,630 for floor on 40 MM bbls on 10/04
$25.2 MM Interest Semi-annually
993,299.17 bbls * spot price semi-annually
$755,848,370
Value on 31,533,307 bbls * spot price on 10/04
993,299.17 bbls * spot price semi-annually through 10/04
Cap on 31,533,307 bbls at $800 MM on 10/04
Enron North America (Delaware Corp.)
Last Revised: 8/7/2001


EC2 000001610
Yosemite Securities Company Ltd. Financing
February 23, 2000
Legend
Corporation
Partnership
Branch
Beneficial Owners
Long Acre Trust (Delaware Business Trust)
£11.125 MM Certificate
12% Yield
Total Return Swap
Bank Boston (Rhode Island Corp.)
Enron Corp. (Oregon Corp.)
£11.125 MM Certificate
12% Yield
£15.5 MM Magic Note (Issued at £15.2362)
£ 200 MM Notes (Issued at £199.238)
8.75% interest
Foreign Noteholders
Yosemite Securities Company Ltd. (Jersey, Channel Islands) Ltd.
£206.75 MM
£ 206.75 MM Note
7.5% interest annually
Cash Flow Swap
Credit Protection
Enron Agreement
Citibank, N.A. (Delaware Corp.)
Floor on 11,228,785 bbls at £206.75 on 2/07
£24,212,068 Premium for Floor
£15,506,250 interest annually
842,159 bbls * spot price annually
Total Return Swap
Salomon Bros. Intl. Ltd. (United Kingdom Corp.)
£206.75 MM
Value on * spot price of 11,228,785
842,159 bbls * spot price annually
Cap on 11,228,785 bbls at £206.75 MM
£24,212,068MM Premium for Cap
£15,506,250 Interest for Floor at £206.75 MM on 2/07
842,159 bbls * spot price annually
Floor on 11,228,785 bbls at £206.75 MM on 2/07
£24,212,068 Premium for Floor
£15,506,250 interest annually
842,159 bbls * spot price annually
Enron North America (Delaware Corp.)
Last Revised: 8/11/2000


EC 000037719
Yosemite Securities Company Ltd. Financing
March, 2000
Last Revised: 1/19/00
Beneficial Owners
Foreign Noteholders
Total Return Swap
£ [200] MM ($ MM)
[8.75]% interest
£ [247.5] MM Note
Enron Agreement
Cash Flow Swap
Credit Protection
Floor
Interest
bbls * spot price
Legend
Corporation
Partnership
Branch

What are Prepays?

- Series of normal individual trading transactions (i.e. swaps, options, physical forwards, etc.) structured to generate cash in return for some obligation, either product or cash settlement through financial instructions.
- Example: Enron contracts with XYZ Corp. where XYZ delivers Enron $25MM cash in return for 1,000,000 BBLS of crude valued at $27/BBL in 12 months. Enron and XYZ will normally enter into a separate, offsetting swap agreement to eliminate any open positions and price risk.
- Common industry practice.

Permanent Subcommittee on Investigations
EXHIBIT #186e

Why Does Enron Enter into Prepays?

- Off balance sheet financing (i.e., generate cash without increasing debt load).
- Allows for balance sheet management specifically price risk management assets and liabilities.
- Allows for purchasing product at discount.

EC 001594741

Actual Prepay Synopsis Overview

- Background

  In June 1999 Enron entered into a prepay agreement with Citibank and Toronto Dominion, under the agreement.

- Contract Details

  With Citibank

  - Enron received $250,000,000 on June 29, 1999
  - Sold physical forward = 14,198,809 Bbls in September 1999
    - Settle price = April 2000 Nymex Contract as of September 25, 1999
  - Bought financial swap = 14, 143, 407 Bbls in September 1999
    - Settle price = May 2000 Nymex Contract as of September 25, 1999
    - Fixed price = $17.94

  With Toronto Dominion

  - Enron received $250,000,000 on June 29, 1999
  - Sold physical forward = 14,143,407 Bbls in September 1999
    - Settle price = May 2000 Nymex Contract as of September 1999
  - Bought financial swap = 14, 198,809 Bbls in September 1999
    - Settle price = April 2000 Nymex Contract as of September 25, 1999
    - Fixed price = $17.87

EC 001594742

Actual Prepay Synopsis

Risk Management/Open Positions

	April 00	May 00
• Citibank (forward)	<14,198,809>	
• Citibank swap		14,143,407
• Toronto (forward)		<14,143,407>
• Toronto swap	14,198,809	
• Total	- 0 -	- 0 -

EC 00194743

Kirk, Niels

From: Reilly, James F. [James F. Reilly /10USHOU/o=AF1/c=US/a=MCI/p=CITICORP]
Sent: 16 November 1999 18:03
To: Fox, William; Kirk, Niels C.
Subject: RE: Yosemite II (Europe)

_____ Forward Header _____
Subject: RE: Yosemite II (Europe)
Author: adam.kulick (adam.kulick@ssmb.com) at INTERNET
Date: 11/16/1999 4:37 AM

Jim, thanks for the e-mail. i have a couple of comments that you may see fit to forward to bill/niels...

if we do a traditional bridge, i would prefer to keep it in the truman structure rather than running it through delta as i do not want to share our new prepaid technology with other banks. to address bill's appropriateness point, the equity is only in the structure to satisfy tax and accounting issues, not as a first loss position for the benefit of investors. consequently, the prospectuis and marketing materials make clear that investors do not get the benefit of the equity in an enron default. in addtion, the materials make very clear that investors shoud not expect to get the benefit of any AAAs in the vehicle either, as they will susbtituted out to citi in the event of an enron default. therefore i do not believe that there is an appropriateness issue here.

regards from the sunny uk, adam

> ----------
> From:
> James.F.Reilly@x400prod2.cgin.us-md.citicorp.com[SMTP:James.F.Reilly@x400p
> rod2.cgin.us-md.citicorp.com]
> Sent: Monday, November 15, 1999 8:55 PM
> To: Kulick, Adam;
> Lynn.Feintech/OU=14USSFO@jupiteralias.email.citicorp.com
> Subject: RE: Yosemite II (Europe)
>
> <<File: ATT292958.ATT>>
> Self-explanatory.
>
>
> _____ Forward Header
> _____
> Subject: RE: Yosemite II (Europe)
> Author: William Fox at 20USNYC/o=AF1/c=US/a=MCI/p=CITICORP
> Date: 11/14/1999 7:06 PM
>
>
> I agree we need to find mutually acceptable solution but need to first
> have the
> market feedback and at same time press an interim securitization solution
> that
> can be structured around the 25 years. Also there is the issue on the
> equity.
> Two points: one can we technically strcuture a default swap from the trust
> that
> elirninates our exposure and two there is a question of appropriateness:
> presumably we will be respresenting to investors that we are putting up
> half the
> equity and then with or without disclsoure(?) we are doing a default swap
> with

Permanent Subcommittee on Investigations
EXHIBIT #186f

> the trust; sound questionable.
>
> -----Original Message-----
> From: Reilly, James F.
> Sent: Friday, November 12, 1999 4:42 PM
> To: Fox, William; Baillie, Steve
> Cc: Kirk, Niels C.
> Subject: RE: Yosemite II (Europe)
>
>
> Bill: The possible Yosemite 2 "bridge" will not die. Enron is ramping up
> the
> pressure with a story that goes like this:
>
> - Mandates on capital markets deals carry with them the obligation of
> bridging
> if the bridge is required due to timing or market conditions - not new, we
>
> discussed this when we rolled Truman at 9/30;
> - Enron has paid (can you guess what comes next) Citigroup over $20/25MM
> in
> revenues (fees?) in 1999 - including actively working to expand the
> relationship
> to SSB (EOG equity, Enron equity and ACES);
> - Citi exposure has dropped dramatically as a result of Condor and
> Yosemite.
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> Our position:
> - Exposure, altho down, is still in running at $600+/-MM;
> - We cannot build YE assets by $250MM; and
> - SSB has not yet given us a clear view of the viability of Yosemite 2 -
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> feasible structurally and can it be ready on time; will the European
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> it; can it be succesfully launched before YE; at a price acceptable to
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> and not impact our balance sheet (Nahanni will be in the conduits) or add
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> "club" bridge where Citi might speak to only 33%.
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> sessions with
> SSB/Enron/investors in London will provide critical input to an assessment
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> the situation. We will also continue talking about the "club" and
> securitization
> options (see below). SSB (derivatives and Energy/Power) is aware of the
> "bridge"
> issue.
>
>
> _____ Forward Header
> _____
> Subject: RE: Yosemite II (Europe)
> Author: Niels C. Kirk at 70EULON/c=AF1/c=US/a=MCI/p=CITICORP
> Date: 11/12/1999 1:30 PM
>
>
> Jim,

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> I called Chivers and reiterated our concern over the manner
> in which he's pushing Yosemite II and the "bridge" on us
> (especially given the fact that we (and Houston for that
> matter) still don't know if there's a deal). He understood
> and knows, that we know, he's trying to jam us (such
> is life...).
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> 1. Next week is very important. We can't even say whether
> this is a bridge or a prepaid pier until we know the market.
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> 2. What's Enron's threshold on the spread?
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> 3. If we were to do a club deal on a bridge, how many banks
> does Enron think they could deliver? Why is Enron against
> clubbing the bridge?
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> 4. There could be a chance of ST booking the deal in one of
> our European conduit vehicles (as done previously in the US)
> but this still needs to be explored and it could be pricey
> given that Enron's goal is to go LT (25+ years).
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> Chivers was unable to answer the questions above but stated that
> my (our) reaction/response was valid and productive.
>
> Niels
>
>
> -----Original Message-----
> From: Fox, William
> Sent: Wednesday, November 10, 1999 5:56 PM
> To: Fox, William; Kirk, Niels C.; Reilly, James F.
> Subject: RE: Yosemite II (Europe)
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> Just to make it clear: no room to bridge.
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> -----Original Message-----
> From: Fox, William
> Sent: Wednesday, November 10, 1999 12:50 PM
> To: Fox, William; Kirk, Niels C.; Reilly, James F.
> Subject: RE: Yosemite II (Europe)
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> In spite of all the repayments we have/will receive from Condor and
> Yosemite we
> still have an exposure issue as it relates to obligor limits; there is a
> developing view that limits are limits and not to be exceed. This is
> something
> we will all have to deal with. Also we do not have room for incremental
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> of $200-300mm over year end. Iwill discuss with Reilly later today for
> current
> status and review of options.
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> -----Original Message-----
> From: Kirk, Niels C.
> Sent: Friday, November 05, 1999 1:20 PM
> To: Fox, William; Reilly, James F.
> Subject: Yosemite II (Europe)
> Importance: High
>
> Bill/Jim,
>
> Just a quick heads-up.
>
> Enron Europe are proposing that Yosemite II be arranged for
> GBP 175/200 MM. They need this by year-end as the deal

CITI-SPSI 0033633

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> generates count as operational funds flow which will evidently
> fill a gap left by certain European projects/contracts.
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> Coincidentally, their $250 MM corporate 364 day R/C (which is
> fully drawn) matures next week. Enron to repay from corporate
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> bridging the deal in the event that the capital markets fail us.
> My response to date has been non-committal, especially as
> Yosemite is still in prototype mode and typical of Enron they
> are already in replication mode. I'm concerned that the capital
> markets may close before we can get the structure away, then
> we could be left holding the bag.
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> SSB London have approached certain investors and we are waiting
> for their feedback. I understand that other "roadshows" are
> contemplated for London and Scotland in the near future. Also
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> So the question is, where do we stand on Enron credit capacity?
> Is there any room for $250/$300 MM over year-end? If not, would
> it be feasible (from a practical and structuring point of view) to
> arrange a we arrange a bridge for say Japanese or Canadian only
> banks (their year-end is different)?
>
> Please advise. If we have no more capacity, please begin to
> manage Enron HQ expectations.
>
> Niels
>
> << File: MAPI-1 Distribution List.TXT >>
>

RE_ Yosemite II (Europe).TXT

Kirk, Niels

From: Riggall, Simon [Simon Riggall /61EULON/o=AF1/c=US/a=MCI/p=CITICORP]
Sent: 16 November 1999 16:26
To: Gibson, Suzanne; Riggall, Simon; Kirk, Niels C.; Reilly, James F.; Zaman, Sikander; Elliston, Simon
Cc: Streamer, Sarah
Subject: RE: Enron in West Africa

Thanks. Jeff called me today and we are trying to arrange a time to meet. Rgds

-----Original Message-----
From: Gibson, Suzanne
Sent: 15 November 1999 16:49
To: Riggall, Simon; Kirk, Niels C.; Reilly, James F.; Zaman, Sikander; Elliston, Simon
Cc: Streamer, Sarah
Subject: Enron in West Africa

Had a call from Jeff Forbis at Enron in Houston. He had got my name from a colleague with whom we looked at several Central European opportunities some time ago. As he described it, he is trying to get a handle on financing alternatives for West African projects (as I understood his focus -- on the power side). He said he didn't have a particular deal in mind at the moment, but wanted to hae a discussion on what is possible/financeable.

He would like to speak to someone both from a project finance and a

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geographical focus on Africa. He will follow up with Sarah in the morning if he doesn't hear anything and would like to speak with someone as soon as practicable. His number is 0799 089 8329 -- dialed as a UK mobile.

Thanks and regards
Suzanne

Kirk, Niels

From: Gibson, Suzanne [Suzanne Gibson /71EULON/o=AF1/c=US/a=MCI/p=CITICORP]
Sent: 15 November 1999 16:49
To: Riggall, Simon; Kirk, Niels C.; Reilly, James F.; Zaman, Sikander; Elliston, Simon
Cc: Streamer, Sarah
Subject: Enron in West Africa

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He would like to speak to someone both from a project finance and a geographical focus on Africa. He will follow up with Sarah in the morning if he doesn't hear anything and would like to speak with someone as soon as practicable. His number is 0799 089 8329 -- dialed as a UK mobile.

Thanks and regards
Suzanne

Kirk, Niels

From: Fox, William [William Fox /20USNYC/o=AF1/c=US/a=MCI/p=CITICORP]
Sent: 15 November 1999 00:07
To: Baillie, Steve; Fox, William; Reilly, James F.
Cc: Kirk, Niels C.
Subject: RE: Yosemite II (Europe)

I agree we need to find mutually acceptable solution but need to first have the market feedback and at same time press an interim securitization solution that can be structured around the 25 years. Also there is the issue on the equity. Two points: one can we technically strcuture a default swap from the trust that eliminates our exposure and two there is a question of appropriateness: presumably we will be respresenting to investors that we are putting up half the equity and then with or without disclsoure(?) we are doing a default swap with the trust; sound questionable.

-----Original Message-----
From: Reilly, James F.
Sent: Friday, November 12, 1999 4:42 PM
To: Fox, William; Baillie, Steve
Cc: Kirk, Niels C.
Subject: RE: Yosemite II (Europe)

Bill: The possible Yosemite 2 "bridge" will not die. Enron is ramping up the pressure with a story that goes like this:

- Mandates on capital markets deals carry with them the obligation of bridging if the bridge is required due to timing or market conditions - not new, we discussed this when we rolled Truman at 9/30;
- Enron has paid (can you guess what comes next) Citigroup over $20/25MM in revenues (fees?) in 1999 - including actively working to expand the relationship to SSB (EOG equity, Enron equity and ACES);

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- Citi exposure has dropped dramatically as a result of Condor and Yosemite.

Our position:
- Exposure, altho down, is still in running at $600+/-MM;
- We cannot build YE assets by $250MM; and
- SSB has not yet given us a clear view of the viability of Yosemite 2 - is it feasible structurally and can it be ready on time; will the European market buy it; can it be succesfully launched before YE; at a price acceptable to Enron (what is the threshold price above which the Company will not sell?).

We have suggested that Nahanni could provide the capital shortfall if Y2 cannot be launched - this would use capacity designed for just this sort of shortfall and not impact our balance sheet (Nahanni will be in the conduits) or add incremental exposure (beyond Nahanni, that is) - this may not work as Y2 is a prepaid which provides benefits not part of Nahanni. They have suggested a "club" bridge where Citi might speak to only 33%.

It has been left (for the weekend) that the outcome of next week's sessions with SSB/Enron/investors in London will provide critical input to an assessment of the situation. We will also continue talking about the "club" and securitization options (see below). SSB (derivatives and Energy/Power) is aware of the "bridge" issue.

_____ Forward Header _____
Subject: RE: Yosemite II (Europe)
Author: Niels C. Kirk at 70EULON/o=AF1/c=US/a=MCI/p=CITICORP
Date: 11/12/1999 1:30 PM

Jim,

I called Chivers and reiterated our concern over the manner in which he's pushing Yosemite II and the "bridge" on us (especially given the fact that we (and Houston for that matter) still don't know if there's a deal). He understood and knows, that we know, he's trying to jam us (such is life...).

Anyway I covered our four points:

1. Next week is very important. We can't even say whether this is a bridge or a prepaid pier until we know the market.

2. What's Enron's threshold on the spread?

3. If we were to do a club deal on a bridge, how many banks does Enron think they could deliver? Why is Enron against clubbing the bridge?

4. There could be a chance of ST booking the deal in one of our European conduit vehicles (as done previously in the US) but this still needs to be explored and it could be pricey given that Enron's goal is to go LT (25+ years).

Chivers was unable to answer the questions above but stated that my (our) reaction/response was valid and productive.

Niels

-----Original Message-----
From: Fox, William
Sent: Wednesday, November 10, 1999 5:56 PM
To: Fox, William; Kirk, Niels C.; Reilly, James F.
Subject: RE: Yosemite II (Europe)

Just to make it clear: no room to bridge.

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CITI-SPSI 0033636

-----Original Message-----
From: Fox, William
Sent: Wednesday, November 10, 1999 12:50 PM
To: Fox, William; Kirk, Niels C.; Reilly, James F.
Subject: RE: Yosemite II (Europe)

In spite of all the repayments we have/will receive from Condor and Yosemite we still have an exposure issue as it relates to obligor limits; there is a developing view that limits are limits and not to be exceed. This is something we will all have to deal with. Also we do not have room for incremental assets of $200-300mm over year end. Iwill discuss with Reilly later today for current status and review of options.

-----Original Message-----
From: Kirk, Niels C.
Sent: Friday, November 05, 1999 1:20 PM
To: Fox, William; Reilly, James F.
Subject: Yosemite II (Europe)
Importance: High

Bill/Jim,

Just a quick heads-up.

Enron Europe are proposing that Yosemite II be arranged for GBP 175/200 MM. They need this by year-end as the deal generates count as operational funds flow which will evidently fill a gap left by certain European projects/contracts.

Coincidentally, their $250 MM corporate 364 day R/C (which is fully drawn) matures next week. Enron to repay from corporate funds, but it appears that the proceeds from Yosemite II are earmarked for reimbursement of the corporate funds.

Chivers has begun to make noises about Citi stepping up and bridging the deal in the event that the capital markets fail us. My response to date has been non-committal, especially as Yosemite is still in prototype mode and typical of Enron they are already in replication mode. I'm concerned that the capital markets may close before we can get the structure away, then we could be left holding the bag.

SSB London have approached certain investors and we are waiting for their feedback. I understand that other "roadshows" are contemplated for London and Scotland in the near future. Also there is a structuring session slated for next week in New York.

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Please advise. If we have no more capacity, please begin to manage Enron HQ expectations.

Niels

<< File: MAPI-1 Distribution List.TXT >>

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CITI-SPSI 003363

Kirk, Niels

From: adam.kulick [adam.kulick@ssmb.com]
Sent: 13 November 1999 00:14
To: p.chivers; tkirby
Cc: Kulick, Adam; Reilly, James F [CITI]; Mcbride, Myles; Kirk, Niels C [CITI]; Charles, Peter
Subject: Fees for Yosemite II

Dear Paul and Treasa,

Please find the fee schedule for Yosemite II outlined below.

Underwriting Fee: 75 bps upfront

Per annum return on:

AAA Investments: 10 bps
Enron Investments: 15 bps
Basis Risk of Prepaid: 12.5bps
Equity Investment hedge) 175 bps (assumes that Enron pays for default swap to

We look forward to discussing these with you in more detail on Monday.

Best regards,

Adam Kulick

PS. The most recent version of the roadshow is attached for your review.

<<Roadshow1.ppt>>

Roadshow1.ppt

Kirk, Niels

From: Reilly, James F. [James F. Reilly /10USHOU/o=AF1/c=US/a=MCI/p=CITICORP]
Sent: 12 November 1999 21:42
To: Fox, William; Baillie, Steve
Cc: Kirk, Niels C.
Subject: RE: Yosemite II (Europe)

Bill: The possible Yosemite 2 "bridge" will not die. Enron is ramping up the pressure with a story that goes like this:

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Forward Header

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Author: Niels C. Kirk at 70EULON/o=AF1/c=US/a=MCI/p=CITICORP
Date: 11/12/1999 1:30 PM

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Niels

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Sent: Wednesday, November 10, 1999 5:56 PM
To: Fox, William; Kirk, Niels C.; Reilly, James F.
Subject: RE: Yosemite II (Europe)

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From: Fox, William
Sent: Wednesday, November 10, 1999 12:50 PM
To: Fox, William; Kirk, Niels C.; Reilly, James F.
Subject: RE: Yosemite II (Europe)

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CITI-SPSI 0033639

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To: Fox, William; Reilly, James F.
Subject: Yosemite II (Europe)
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Niels

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CITI-SPSI 003364n

Kirk, Niels

From: Kirk, Niels C. [Niels C. Kirk /70EULON] on behalf of Kirk, Niels C.
Sent: 12 November 1999 18:30
To: Reilly, James F.
Subject: RE: Yosemite II (Europe)

Importance: High

Jim,

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To: Fox, William; Kirk, Niels C.; Reilly, James F.
Subject: RE: Yosemite II (Europe)

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Please advise. If we have no more capacity, please begin to manage Enron HQ expectations.

Niels

CITI-SPSI 0033642

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SEP-10 01 MON 12:39 PM FAX NO. P. 01/03

MAPLES and CALDER

Cayman Islands Attorneys-at-Law

PO Box 309, Ugland House
South Church Street, George Town
Grand Cayman, Cayman Islands

Telephone: 1(345) 949 8066
Facsimile: 1(345) 949 8080
Email: info@maplesandcalder.com

To:	Sharon Lamb	Date:	10 September, 2001
Company:	Schroders	Ref:	047582-01
Country:	Grand Cayman	Fax No.:	345-949-5409
Sender:	Owen Jones	No. of pages: (Including this page)	3
Sender's e-mail address:	Owen.jones@maplesandcalder.com		

Please notify us immediately if you do not receive all pages
Our fax number is 1(345) 949 8080
Our telephone number is 1(345) 949 8066 Ext. 149 (fax room)

This fax is confidential and may also be privileged. If you are not the intended recipient, please notify us immediately. You should not copy or disclose its contents to any other person.

cc:

Melba Trevino	Enron Corp.	1-713-853-9252
Jordan Mintz	Enron Corp.	1-713-853-9252
Doug Warren	Salomon Smith Barney, Inc.	1-212-723-8578
Steve Wagman	Salomon Smith Barney, Inc.	1-212-723-8610
Steve Incontro	Salomon Smith Barney, Inc.	1-212-723-6012
Steve Bailey	Citicorp	1-713-654-2849

Re: Delta Energy Corporation

I acknowledge receipt from Enron Corp. of their cheque in the amount of US$13,168.87 in partial settlement of our invoice number 205630 dated 31st May, 2001 for US$21,775.12 addressed to our client Delta Energy Corporation (copy attached).

This leaves a total of US$8,606.25 outstanding which Enron Corp. have indicated that they are not willing to pay.

We currently hold a total of US$9,766.59 on retainer for Delta Energy Corporation and its parent Grand Commodities Corporation to meet miscellaneous fees and expenses and propose to settle the outstanding balance from this retainer.

DOL1\[illegible]\582\507712\1\[illegible]
10 September, 2001

Permanent Subcommittee on Investigations
EXHIBIT #186g

CITI-SPSI 0103726

MAPLES and CALDER

To: Sharon Lamb
Re: Delta Energy Corporation

10 September, 2001
Page 2

If Citibank/Salomon Smith Barney think that the entire account should be settled by Enron Corp. then I would be grateful if they would liaise directly with Enron Corp.

Kind regards

Owen Jones

Encs

DOMFSW 83575.62 4077 17/09/01 08:01
10 September, 2001

MAPLES and CALDER

Cayman Islands Attorneys-at-Law

PO Box 309, Ugland House,
South Church Street, George Town
Grand Cayman, Cayman Islands

Telephone: 1(345) 949 8066
Facsimile: 1(345) 949 8080
Email: info@maples.candw.ky

3 November, 1999

By Courier: 212-530-5000

Mr. Eric Moser
Milbank Tweed, Hadley & McCloy
1, Chase Manhattan Plaza
New York, NY- 1005
U.S.A.

Dear Eric,

Re: Delta Energy Corporation (the "Company")

Thank you for your email of November 2nd.

The current and past transactions of the Company are best outlined in the board resolutions authorising the same. In connection therewith I enclose the Company's board minutes (and miscellaneous documents which may be relevant) which date from its incorporation. They give a detailed overview of all business conducted, thus dealing with many of your queries.

I confirm that the authorised share capital of the Company is US$900,000 - divided into 900,000 Ordinary Shares of US$1.00 - of which 1,000 have been issued to Grand Commodities Corporation. I also enclose a copy of the Company's Register of Members which reflects this.

We are currently trying to locate the Company's first Correspondence File which was initially handled by another member of this firm. Once located I will revert with any information contained therein on Grand Commodities Corporation, in addition to any other information relevant to your queries.

I hope that this proves useful. Please do not hesitate to contact me should you have any questions. Please note that I will be out of office between the 8th and 12th of November and in my absence your principal contact should once again be Julian Reddyhough.

Permanent Subcommittee on Investigations
EXHIBIT #186h

MAPLES and CALDER

With kind regards,

Yours sincerely,

Joannah Bodden

cc: Andrew Walker, Milbank Tweed (cover page by fax)
William Sullivan, Citibank (cover page by fax)

JLB\HKT\197468\552092\BTZW01!
03 November, 1999

CONFIDENTIAL

Ref: GC 1

REGISTER OF MEMBERS
OF
DELTA ENERGY CORPORATION

NAME OF MEMBER	ADDRESS	DATE OF ENTRY AS MEMBER	CERTIFICATES ISSUED		FROM WHOM SHARES WERE TRANSFERRED (IF ORIGINAL ISSUE ENTER AS SUCH)	AMOUNT PAID THEREON	DATE OF TRANSFER OF SHARES	TO WHOM SHARES ARE TRANSFERRED	CERTIFICATES SURRENDERED		NUMBER OF SHARES HELD (BALANCE)
			CERTIF NOS	NO SHARES					CERTIF NOS	NO SHARES	
A.B. Travers	PO Box 309, Grand Cayman	3.12.93	-	-1-	Original Issue	US$1.00	3.12.93	Grand Commodities Corporation	-	-1-	-
Megan Stone	PO Box 309 Grand Cayman	3.12.93	-	-1-	Original Issue	US$1.00	3.12.93	Grand Commodities Corporation	-	-1-	-
Grand Commodities Corporation	PO Box 309, Grand Cayman	3.12.93		1,000	Two from Subscribers, 998 New Issue						

CONFIDENTIAL

CITI-SPSI 0046542

1186

M:\DMS\1971681\47730.
3 November 1999

Unknown

From: Quaintance Jr., Alan [Alan.Quaintance.Jr@enron.com]
Sent: Friday, June 22, 2001 4:51 PM
To: Wagman, Steve [FI]; Swanson, Timothy [FI]; Bills, Lisa
Cc: Garberding, Michael
Subject: Delta Letter

Delta.doc (19 KB)

All:

<<Delta.doc>>

As discussed with Tim, attached is a sample letter with the representations that Andersen would like Delta to confirm. I am the accountant working on the deal with Michael and Lisa. I am happy to discuss any of these representations with you or your advisors at your convenience.

I have already questioned Andersen about why these representations were not required on recent deals with Delta. Their response was that the reps will be required on this transaction if we are to achieve our accounting objectives. So that route is not available.

I can be reached at the following numbers.

(713)345-7731 (Office)
(713)503-3709 (Cell)
(713)621-1763 (Home)

Please feel free to call me at anytime over the weekend. I have voicemail on all numbers.

Thanks,

Alan Quaintance

Permanent Subcommittee on Investigations
EXHIBIT #186i

June , 2001

Enron Corp.
1400 Smith Street
Houston, Texas 77002

To Whom It May Concern:

Re: Delta Energy Corporation (the "Company")

We confirm:

1. There is no restriction in the corporate documentation of the Company limiting the number of entities with which the Company may conduct business. The Company has undertaken business with a number of entities.

2. The Company has assets other than those acquired through transactions with Enron Corp and its subsidiaries and its affiliates (collectively "Enron").

3. The Company has unencumbered assets, which are available for application towards obligations owed to its creditors.

Yours truly,

Signed by:_____
Title:_____

345 949 5413

BANK OF BERMUDA (CAYMAN) LIMITED

Herewith are details for the remittance of funds to Bank of Bermuda (Cayman) Limited.

Remit U.S. Dollars

TO: Citibank N.A., 399 Park Avenue, New York, New York
SWIFT Code – CITI US33
ABA Routing # - 021-0000-89

For account of: Bank of Bermuda (Cayman) Limited
SWIFT Code: BBDAKYKX
* For further credit to: Givens Hall Bank & Trust Ltd.
* Account No.: 7500-3009
* For REFERENCE to : Delta Energy Corporation

MUST BE IN BY 11.30 AM TO GO OUT SAME DAY.

TO: TIM SWANSON - CITIBANK - 212 723 8610.

FROM: SHARON LEA LAING "IN THE VACATION ISLAND"!

TIM,

ABOVE PLEASE FIND THE BANKING DETAILS. I WOULD DRAW YOUR ATTENTION TO THE NAME OF THE A/C & FURTHER CREDIT TO & THE REF. PLEASE LET ME KNOW EXACTLY WHAT IS COMING IN - OUR FEE IS $8000.00. WILL TALK TO YOU TOMORROW. REGARDS, SHARON.

Permanent Subcommittee on Investigations
EXHIBIT #186j

CITI-SPSI 0103717

Tim SWANSON

1212 723 8610 .

URGENT - URGENT

Schroders

PAYMENT INSTRUCTIONS

US$ WIRE TRANSFER DETAILS – IBJ Whitehall

IBJ Whitehall Bank & Trust Company
One State Street,
New York, New York 10004
U.S.A.

ABA No.:	026007825
For the account of:	Schroder Cayman Bank and Trust Company Limited
Account No.:	81354204
Reference:	DELTA ENERGY

Deposits may be made by wire transfer, cheque or bankers draft. **Please quote reference with any remittance.**

Telephone: (345) 949-2849
Facsimile: (345) 949-5409
E-mail: schroder@candw.ky

Schroder Cayman Bank and Trust Company Limited
P.O. Box 1040 GT, Harbour Centre
Grand Cayman, British West Indies

CONFIDENTIAL

MAY-14-1999 FRI 10:38 AM GIVENS HALL BANK & TRUST FAX NO. 345 949 8295 P. 01

The Givens Hall Bank

FAX COVER SHEET

DATE: MAY 14, 1999

FAX NO: 1 212 758 6372

TO: WADE SPEARS

COMPANY: CITICORP SECURITIES INC.

FROM: DAN BENSON

RE: DELTA & UTAH ENERGY CORPORATION

NO. OF PAGES INCLUDING COVER SHEET: 3

COMMENTS:

DELTA FEES PAID - MANY THANKS FOR YOUR HELP. HOWEVER SISTER COMPANY UTAH ENERGY CORPORATION SHOULD HAVE BEEN PAID AT SAME TIME, CAN YOU PLEASE CHASE UP.

Regards

Dan Benson

Givens Hall Bank & Trust, Ltd. Genesis Building P.O. Box 2097 GT Grand Cayman Cayman Islands Telephone 345 949 8141 Facsimile 345 949 8295

Received Time May. 14. 11:35AM Print Time May. 14. 11:36AM

CITI-SPSI 0046893

Permanent Subcommittee on Investigations
EXHIBIT #186k

The Givens Hall Bank

February 5, 1999

Mr. Ami Greenstein
Citibank N.A.
New York

Fax: 1 212 291 3684

Dear Mr. Greenstein,

FAXED 2/5/99

Delta Energy Corporation
Vega Energy Corporation

Following on from our earlier telephone conversation I am forwarding to you fee notes relating to the above companies.

Yours sincerely,

J.B. Benbow

Givens Hall Bank & Trust, Ltd. Genesis Building P.O. Box 2097 GT Grand Cayman Cayman Islands Telephone 345 949 8141 Facsimile 345 949 8295 Email

Received Time May. 14. 11:35AM Print Time May. 14. 11:36AM

The
Givens
Hall
Bank

February 5, 1999

Delta Energy Corporation

STATEMENT FOR SERVICES

To:	Supplying the board of directors, shareholders etc. to the company and its parent company, and administering the overlying Trust for the year ending December 31, 1999.		
	Fee as agreed		5,000.00
	Reviewing and signing of documents with regard to the formal purchase and sale of oil and gas from Enron and related parties. Documents executed December 30, 1998.		
	Fee on a time spent basis		2,920.00
	Disbursements		
	Sundry items		25.00
		US$	7,945.00

Fee Note GH 29/99

Givens Hall Bank & Trust, Ltd. Genesis Building P.O. Box 2097 GT Grand Cayman Cayman Islands Telephone 345 949 8141 Facsimile 345 949 8295 Email ghbt@candw.ky

CONFIDENTIAL

CITI-SPSI 0046895

Enron/Delta Swap Confirmation

December 22, 1999

To: Delta Energy Corporation
P.O. Box 309
George Town, Grand Cayman
Cayman Islands, British West Indies
Attention: John Benbow
Facsimile No.: (345) 949-8080
Telephone No.: (345) 949-8066

From: Enron North America Corp.
1400 Smith Street
Houston, Texas 77002
Attention: Joe Hunter
Facsimile No.: (713) 646-2495
Telephone No.: (713) 853-3316

Ladies and Gentlemen:

The purpose of this letter agreement (this "*Confirmation*") is to set forth the terms and conditions of the Transaction entered into between Enron North America Corp. ("*Party A*" or "*ENA*") and Delta Energy Corporation ("*Party B*" or "*Delta*") on the Trade Date specified below (the "*Transaction*"). This Confirmation constitutes a "Confirmation" as referred to in the Master Agreement specified below. Certain capitalized terms used herein are defined in Section 6 below.

This Confirmation supplements, forms a part of, and is subject to, the ISDA Master Agreement, dated as of November 18, 1999 (the "*Master Agreement*"), between Party A and Party B. All provisions contained in the Master Agreement govern this Confirmation except as expressly modified below.

Each party will make each payment specified in this Confirmation as being payable by it, not later than the due date for value on that date in the place of the account specified below, in freely transferable U.S. Dollars and in the manner customary for payments in U.S. Dollars.

The terms of the Transaction to which this Confirmation relates are as follows:

1. *General Terms*:

Trade Date:	December 22, 1999
Effective Date:	December 22, 1999
Scheduled Termination Date:	October 26, 2004
Floating Amount Payer:	Party A
Fixed Amount Payer:	Party B
Calculation Agent:	Citibank

Permanent Subcommittee on Investigations
EXHIBIT #1861

Business Day Convention:	Preceding.
Commodity Business Day Convention:	Preceding.
Periodic Payment Dates:	Each April 14 and October 14 of each year.
Payment Dates:	For payments to be made under Section 3: (a) each Periodic Payment Date during the period from the Effective Date to but excluding the Cancellation Date; and (b) the Cancellation Date (but only if (x) the Cancellation Date is on or prior to the Periodic Payment Date in October 2004 and (y) no Event of Default or Termination Event shall have occurred and be continuing on the Cancellation Date).
Market Disruption Events:	Price Source Disruption Trading Suspension Disappearance of Commodity Reference Price Tax Disruption
Disruption Fallback:	If a Market Disruption Event with respect to the Specified Price for the relevant Pricing Date occurs, then the Specified Price shall be determined by using the first preceding Commodity Business Day on which no Market Disruption Event existed with respect to the Specified Price (all as determined by the Calculation Agent).

2. ***Fixed Payment***

Fixed Payment Date:	The Effective Date
Fixed Payment Amount:	U.S.$705,725,402.00
Settlement:	On the Fixed Payment Date, the Fixed Amount Payer shall pay the Fixed Payment Amount to Party A.

3. ***Periodic Floating Payments***

Periodic Floating Payment Dates:	Each Payment Date.
Periodic Floating Amount:	For any Payment Date, the Periodic Notional Quantity for such Payment Date *multiplied by* the Periodic Floating Price for such Payment Date.
Periodic Notional Quantity:	(a) For the First Periodic Payment Date, 1,212,375 barrels *multiplied* by the First Periodic Payment Fraction; (b) for each Payment Date (other than the Payment Date referred to in clause (a) above) prior to the Cancellation Date, 1,212,375 barrels; and (c) for the Cancellation Date (if it is a Payment Date but is not the First Periodic Payment Date), 1,212,375 barrels *multiplied by* the Cancellation Fraction.

Periodic Floating Price:	For any Payment Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" for such Payment Date is the First Nearby Month with respect to such Payment Date; and (d) the "Pricing Date" is the Commodity Business Day that is three Commodity Business Days prior to such Payment Date (or, for determinations under Section 7 below, the Windup Date).
Settlement:	On each Payment Date, the Floating Amount Payer shall pay the Periodic Floating Amount for such Payment Date to Party B.

4. *Final Floating Payment*

Final Floating Payment Date:	The Cancellation Date
Final Floating Amount:	The lesser of: (a) the Final Notional Quantity *multiplied by* the Final Floating Price; and (b) U.S.$800,000,000.00
Final Notional Quantity:	44,469,150 barrels
Final Floating Price:	For the Final Floating Payment Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" is the First Nearby Month with respect to the Final Payment Date; and (d) the "Pricing Date" is the Commodity Business Day that is three Commodity Business Days prior to the Final Floating Payment Date (or, for determinations under Section 7 below, the Windup Date).
Settlement:	On the Final Floating Payment Date, the Floating Amount Payer shall pay the Final Floating Amount to Party B.

5. *Notice and Account Details*

Telephone, Telex and/or Facsimile Numbers and Contact Details for Notices:	
Party A:	As specified in the Master Agreement

Party B:	As specified in the Master Agreement
Account Details:	
	Wire transfers to:
	NationsBank of Texas, N.A.
	Account No. 3750494727
Account Details of Party A:	ABA No. 111000012
Account Details of Party B:	Wire transfers to the Enron/Delta Account

6. *Certain Definitions*:

As used in this Confirmation, the following terms shall have the following respective meanings:

"*Bankruptcy Code*" means the United States Bankruptcy Code, Title 11 of the United States Code, as amended.

"*Cancellation Date*" means the earliest to occur of:

(1) the Early Termination Date (if any) under the Master Agreement;

(2) such date as Party A and Party B may agree in writing to be the Cancellation Date; and

(3) the Scheduled Termination Date,

all as determined by the Calculation Agent in good faith in accordance with the terms of this Confirmation (and such determination shall be binding absent manifest error).

"*Cancellation Fraction*" means, for any Periodic Floating Payment to be made under Section 3 above on the Cancellation Date (if it is a Payment Date), a fraction, the numerator of which is equal to the actual number of days elapsed during the period from and including the immediately preceding Payment Date (or, if the Cancellation Date is the first Payment Date, from and including the Effective Date) to but excluding the Cancellation Date, and the denominator of which is equal to 180.

"*Citibank*" means Citibank, N.A., a national banking association, and its successors.

"*Collateral Agent*" means United States Trust Company of New York, in its capacity as "Collateral Agent" under the Collateral Security Agreement and the other Financing Documents referred to therein, and its successors in such capacity.

"*Collateral Security Agreement*" means the Collateral Security Agreement dated as of November 18, 1999 by and among (*inter alia*) Yosemite, Citibank and United States Trust Company of New York, in its capacity as indenture trustee, as amended.

The "*Discounted Present Value*" of any payment (the "*Future Payment*") scheduled to be made on any date (the "*Future Payment Date*") and determined as at any date (the "*Determination Date*") is equal to the present value of such Future Payment, determined by discounting such Future Payment semi-annually on each Periodic Payment Date falling during the period from and including the Determination Date to and including such Future Payment Date at a rate *per annum* (determined on a 30/360 basis) equal to the Discount Rate, all as determined by the Calculation Agent in accordance with

standard industry practice (*provided* that if the Future Payment Date is prior to the Determination Date, then the Discounted Present Value of the related Future Payment will be equal to such Future Payment).

"*Discount Rate*" means a rate per annum equal to 7.25%.

"*Enron*" means Enron Corp., a corporation organized under the laws of the State of Oregon, and its successors.

"*Enron/Delta Account*" means the "Enron/Delta Account" referred to in the Fiscal Agency Agreement.

"*Enron Guaranty*" means the Guaranty dated as of December 22, 1999 made and entered into by Enron in favor of Party B and its successors and assigns, substantially in the form of Exhibit I hereto.

"*First Periodic Payment Date*" means the Payment Date in April 2000.

"*First Periodic Payment Fraction*" means, for any Floating Payment to be made under Section 3 above on the First Periodic Payment Date, a fraction, the numerator of which is equal to the actual number of days elapsed during the period from and including the Effective Date to but excluding the First Periodic Payment Date, and the denominator of which is equal to 180.

"*Fiscal Agency Agreement*" means the Fiscal Agency Agreement dated as of November 18, 1999 among ENA, Enron, Delta and the Fiscal Agent, as from time to time amended.

"*Fiscal Agent*" means United States Trust Company of New York, in its capacity as fiscal agent under the Fiscal Agency Agreement, together with its successors in such capacity.

"*Net Termination Amount*" means an amount equal to the Termination Payment owing by the Defaulting Party *minus* the Termination Payment owing by the Non-defaulting Party.

"*Termination Claims*" means, as to a Defaulting Party, amounts owing (or deemed owing) by such party under Section 7 of this Confirmation and under Section 6(e) of the Master Agreement (to the extent relating to this Transaction), together with all other amounts (including, without limitation, amounts owing under Section 11 of the Master Agreement and interest accruing on overdue amounts at the Default Rate) owing by such party with respect to this Transaction.

"*Termination Payment*" means, as to any party ("*X*"), an amount equal to:

(1) the sum of the Discounted Present Values of each Periodic Floating Amount (if any) scheduled to be made by X under Section 3 above during the period from and including the Windup Date to and including the Scheduled Termination Date; *plus*

(2) the Discounted Present Value of the Final Floating Amount (if any) scheduled to be made by X under Section 4 above on the Scheduled Termination Date,

in each case determined as at the Windup Date. As used above, payments "scheduled to be made" on any date or during any period shall be determined as if all payments are to be made through and including the Scheduled Termination Date without regard to whether the Windup Date occurs prior thereto.

"*Transfer*" means a transfer, assignment or other disposition, and "*Transferred*" and "*Transferee*" have correlative meanings.

"*Yosemite*" means Yosemite Securities Trust I, a Delaware statutory business trust, and its successors.

"*Yosemite Notes*" means the Notes issued under the Indenture dated as of November 18, 1999 between Yosemite and United States Trust Company of New York, as indenture trustee, as from time to time amended.

7. *Payments on Early Termination.*

Party A and Party B agree that, if an Early Termination Date occurs under the Master Agreement (such Early Termination Date being referred to herein as the "*Windup Date*"), then the Calculation Agent shall determine the Net Termination Amount, and:

(1) if the Net Termination Amount is positive, then the Defaulting Party will pay such amount to the Non-defaulting Party (together with interest on an amount equal to the Net Termination Amount at a stated rate of interest equal to the Discount Rate applicable to this Transaction for the period from and including the immediately preceding Periodic Payment Date (or, if the Windup Date occurs prior to the first Periodic Payment Date, from and including the Effective Date) to but excluding the Windup Date); and

(2) if the Net Termination Amount is negative, then the Non-defaulting Party will pay the absolute value of the Net Termination Amount to the Defaulting Party.

Such payments shall be in lieu of payments that otherwise would be made on the Windup Date under Sections 3 and 4 above (and in lieu of liquidation payments or payments on early termination that otherwise would be determined and payable in accordance with Section 6(e) of the Master Agreement), and shall constitute the final payments payable under or in respect of or in connection with this Confirmation and this Transaction (other than interest at the Default Rate payable on overdue amounts and amounts payable under Section 11 of the Master Agreement in connection with this Transaction). Notwithstanding the foregoing, payments made in accordance with this Section 7 shall be deemed to be payments under Section 6(e) of the Master Agreement for all purposes thereof.

8. *Other Terms.*

(a) *Concerning the Calculation Agent.*

(1) Party A and Party B hereby irrevocably appoint Citibank as the Calculation Agent hereunder and by its signature below Citibank accepts such appointment, *provided* that if Citibank (or any successor Calculation Agent) shall fail to perform any of its duties as Calculation Agent, Party A and Party B may appoint a successor Calculation Agent. Citibank (and any successor Calculation Agent) may, by not less than 30 days' prior written notice to Party A and Party B, resign as Calculation Agent (*provided* that such resignation shall not become effective until a successor Calculation Agent shall have been appointed by Party A and Party B).

(2) Each party agrees that the Calculation Agent is not acting as a fiduciary for or as an advisor to either party in respect of its duties as Calculation Agent in connection with the Transaction to which this Confirmation relates.

(3) The Calculation Agent's calculations and determinations shall be made in good faith, in a commercially reasonable manner and be binding in the absence of manifest error.

(4) At least one Business Day prior to each date on which any payment is required to be made by Party A hereunder (and otherwise from time to time upon the reasonable request of the Fiscal Agent), the Calculation Agent shall provide to the Fiscal Agent a statement of amounts owing by Party A hereunder.

(b) *Swap Agreements.*

Each party hereby acknowledges and agrees that it intends, for all purposes relevant to such determination, that this Confirmation be treated as a "swap agreement" under the Bankruptcy Code.

(c) *Interpretation.*

Each reference to the singular shall include the plural and vice versa.

(d) *Headings.*

The headings used in this Confirmation are for convenience of reference only and are not to affect the construction of or to be taken into consideration in interpreting this Confirmation.

(e) *Additional Credit Support Documents, Etc.*

For purposes of this Transaction, "Credit Support Document" includes, in relation to Party A, the Enron Guaranty.

For purposes of this Transaction, "Credit Support Provider" includes, in relation to Party A, Enron.

(f) *Assignments by Party A.*

Notwithstanding anything to the contrary in Section 7 of the Master Agreement, Party A reserves the right to transfer all (but not less than all) of its rights and obligations in respect of this Transaction to any of its Domestic Affiliates (such a transfer, an "*Affiliate Transfer*"), subject to the following conditions:

(1) Party A shall have given not less than 30 days' prior written notice of such Affiliate Transfer to Party B, specifying in such notice, *inter alia*, the name of such Domestic Affiliate.

(2) The Enron Guaranty (and all other Credit Support Documents applicable to this Transaction) shall continue in full force and effect in favor of Party B notwithstanding such Affiliate Transfer.

(3) No Event of Default or Termination Event with respect to Party A shall have occurred and be continuing (either on the date on which notice is given to Party B under clause (1) above or on the date of such Affiliate Transfer).

(4) Such Domestic Affiliate shall expressly assume, by an amendment hereto, executed and delivered to Party B, the due and punctual payment of all obligations of Party A

hereunder and the performance of every covenant and obligation on the part of Party A to be performed or observed under or in respect of this Transaction.

(5) Party B and such Domestic Affiliate shall have entered into an agreement in substantially the form of the Master Agreement (including any Credit Support Documents requested by Party B), and such Domestic Affiliate shall have delivered to Party B all of the documents, instruments and other items required to be delivered under Part 3 of the Schedule to the Master Agreement.

(6) Such Domestic Affiliate shall have delivered to Party B an officer's certificate stating that such Affiliate Transfer (and all of the documents delivered in connection therewith) comply with this Section 8(f) and that all conditions precedent in this Section 8(f) relating to such Affiliate Transaction have been complied with.

(7) Such Domestic Affiliate shall have agreed to be bound by the Fiscal Agency Agreement to the same extent as Party A.

(8) Party B shall have received such other documents, instruments, opinions, information and other items in connection with such Affiliate Transfer as it may reasonably request.

For purposes of this Section 8(f), "*Domestic Affiliate*" means any Affiliate of Party A organized under the laws of the United States or any state thereof.

(g) *Assignments by Party B, Etc.*

(1) Notwithstanding anything in the Master Agreement (including, without limitation, in Section 7 thereof) to the contrary, Party A hereby acknowledges and agrees that all Termination Claims owing by Party A may from time to time, without notice to or consent of Party A, be Transferred in whole or in part to one or more Transferees and in one or more separate transactions, and may be so Transferred successively, *provided* that irrespective of any such Transfer Party A shall continue to make all payments owing by it under this Transaction to the Enron/Delta Account to the extent required under the Fiscal Agency Agreement.

(2) Party A and Party B acknowledge and agree that Transfers of Termination Claims owing by Party A shall be effected in accordance with the terms of the Fiscal Agency Agreement.

(3) Notwithstanding anything in Section 7 of the Master Agreement to the contrary, Party A hereby acknowledges that:

(A) all of Party B's right, title and interest in and to this Transaction, including rights in and to the Master Agreement (to the extent relating to this Transaction) and rights under the Enron Guaranty (collectively, the "*Relevant Assets*"), have been pledged to Yosemite to secure indebtedness or other obligations from time to time owing by Party B to Yosemite; and

(B) all of Yosemite's rights with respect to the Relevant Assets are to be pledged to the Collateral Agent for the benefit of the holders of the Yosemite Notes and the other secured obligations referred to in the Collateral Security Agreement,

and Party A hereby consents to such pledges.

(4) Subject to paragraphs (1), (2) and (3) above, Party B agrees that, so long as Party A is a Non-defaulting Party, it will Transfer its rights under this Confirmation only by surrender of this Confirmation to Party A and the issuance by Party A of a new Confirmation to the Transferee.

(5) At any time when the Fiscal Agency Agreement is not in effect, Party A shall be authorized to pay each person in whose name the ENA Claims are registered in the Claims Register maintained under the Fiscal Agency Agreement as of the time it ceased to be in effect (to the extent of the ENA Claims held by such person) until Party A receives notification that the ENA Claims held by such person have been assigned and that payment is to be made to the assignee, *provided* that (1) a notification that does not reasonably identify the rights assigned shall be ineffective and (2) if requested by Party A, the assignee of ENA Claims must seasonably furnish reasonable proof that the assignment has been made, and unless such assignee does so Party A may pay the assignor. As used in this paragraph (5), the terms "*ENA Claims*" and "*Claims Register*" have the meanings assigned to them in the Fiscal Agency Agreement.

(h) *Payments.*

Except as otherwise provided in the Fiscal Agency Agreement, Party A and Party B acknowledge that all payments to be made by Party A under this Confirmation (including, without limitation, all payments made in respect of Termination Claims owing by Party A that have been assigned by Party B to third parties) shall be made to the Enron/Delta Account for application as provided in the Fiscal Agency Agreement.

(i) *Additional Termination Events.*

Solely for purposes of this Transaction, the following Additional Termination Events shall apply:

An Early Termination Date occurs under any Material Commodity Transaction, in which event:

(A) Party A shall be the Affected Party; and

(B) an Early Termination Date under this Transaction shall occur automatically on and as of the Early Termination Date under such Material Commodity Transaction.

As used in this Section 8(i), "*Material Commodity Transaction*" means a Commodity Transaction that (a) is a Transaction to which Party A is or has ever been a party and (b) is a Transaction having an initial notional amount or strike price in excess of U.S.$250,000,000 (or its equivalent in other currencies, determined as of the trade date applicable to such Transaction).

(j) *Netting Provisions.*

Notwithstanding anything in the Master Agreement to the contrary:

(1) Section 2(c)(ii) of the Master Agreement will apply to this Transaction.

(2) For purposes of the Netting Provisions set forth in Paragraph 13 of Part 1 of the Schedule to the Master Agreement, if this Transaction is a Terminated Transaction, it shall not be

aggregated with or netted against other Terminated Transactions in performing the calculations contemplated by Section 6(e) of the Master Agreement unless the Non-defaulting Party (or Non-Affected Party) so elects.

(k) *Default Rate.*

Notwithstanding anything in the Master Agreement to the contrary, the "Default Rate" for purposes of this Transaction shall be a stated rate of 8.25% per annum (calculated on a 30/360 basis), and interest accruing hereunder at the Default Rate shall be payable on demand of the Non-defaulting Party and in any event on each Periodic Payment Date (or, if any such date is not a Business Day, the next preceding Business Day).

(l) *Confidentiality.* For purposes of Part 5, Section 11, of the Schedule to the Master Agreement, Party A hereby agrees that Party B may disclose Confidential Information to Yosemite, the Collateral Agent, the holders from time to time of the Secured Obligations (other than the Yosemite Notes) referred to in the Collateral Security Agreement and, at any time following the occurrence of an Event of Default or Termination Event, the holders from time to time of the Yosemite Notes.

(m) *Waiver of Jury Trial.*

EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES TO THE FULLEST EXTENT PERMITTED BY LAW ALL RIGHT TO TRIAL BY JURY IN ANY PROCEEDING ARISING OUT OF OR RELATING DIRECTLY OR INDIRECTLY TO THIS CONFIRMATION OR THE TRANSACTIONS CONTEMPLATED HEREBY (WHETHER BASED ON CONTRACT, TORT OR ANY OTHER THEORY). EACH PARTY HERETO (A) CERTIFIES THAT NO REPRESENTATIVE, AGENT OR ATTORNEY OF ANY OTHER PARTY HAS REPRESENTED EXPRESSLY OR OTHERWISE, THAT SUCH PARTY WOULD NOT, IN THE EVENT OF LITIGATION, SEEK TO ENFORCE THE FOREGOING WAIVER AND (B) ACKNOWLEDGES THAT IT AND THE OTHER PARTIES HERETO HAVE BEEN INDUCED TO ENTER INTO THIS CONFIRMATION BY, AMONG OTHER THINGS, THE MUTUAL WAIVERS AND CERTIFICATIONS IN THIS PARAGRAPH.

[remainder of page intentionally blank]

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

ENRON NORTH AMERICA CORP.

By: _____
Authorized Signatory
Name: Joe Hunter
Agent and Attorney-In-Fact
Enron North America Corp.

Accepted and confirmed as
of the Trade Date:

DELTA ENERGY CORPORATION

By: _____
Authorized Signatory
Name:

By its signature below, Citibank, N.A. hereby agrees to act as initial Calculation Agent for purposes of the Transaction to which this Confirmation relates on the terms set forth in Section 8(a) above:

CITIBANK, N.A., as initial Calculation Agent

By: _____
Authorized Signatory
Name:

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

ENRON NORTH AMERICA CORP.

By: _____
Authorized Signatory
Name:

Accepted and confirmed as
of the Trade Date:

DELTA ENERGY CORPORATION

By: _____
Authorized Signatory
Name:

By its signature below, Citibank, N.A. hereby agrees to act as initial Calculation Agent for purposes of the Transaction to which this Confirmation relates on the terms set forth in Section 8(a) above:

CITIBANK, N.A., as initial Calculation Agent

By: _____
Authorized Signatory
Name:

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

ENRON NORTH AMERICA CORP.

By: _____
Authorized Signatory
Name:

Accepted and confirmed as
of the Trade Date:

DELTA ENERGY CORPORATION

By: _____
Authorized Signatory
Name:

By its signature below, Citibank, N.A. hereby agrees to act as initial Calculation Agent for purposes of the Transaction to which this Confirmation relates on the terms set forth in Section 8(a) above:

CITIBANK, N.A., as initial Calculation Agent

By: _____
Authorized Signatory
Name:

Enron/Citibank Swap Confirmation

December 22, 1999

To: Enron North America Corp.
1400 Smith Street
Houston, Texas 77002
Attention: Joe Hunter
Facsimile No.: (713) 646-2495
Telephone No.: (713) 853-3316

From: Citibank, N.A.
399 Park Avenue
New York, New York 10043
Attention:
Facsimile No.:
Telephone No.:

Counterparty Ref:

Ladies and Gentlemen:

The purpose of this letter agreement (this "*Confirmation*") is to set forth the terms and conditions of the Transaction entered into between Citibank, N.A. ("*Party A*" or "*Citibank*") and Enron North America Corp. (formerly known as Enron Capital & Trade Resources Corp.) ("*Party B*" or "*ENA*") on the Trade Date specified below (the "*Transaction*"). This Confirmation constitutes a "Confirmation" as referred to in the Master Agreement specified below. Certain capitalized terms used herein are defined in Section 7 below.

This Confirmation supplements, forms a part of, and is subject to, the ISDA Master Agreement, dated as of November 17, 1992 (the "*Master Agreement*"), between Party A and Party B. All provisions contained in the Master Agreement govern this Confirmation except as expressly modified below.

Each party will make each payment specified in this Confirmation as being payable by it, not later than the due date for value on that date in the place of the account specified below, in freely transferable U.S. Dollars and in the manner customary for payments in U.S. Dollars.

The terms of the Transaction to which this Confirmation relates are as follows:

1. *General Terms:*

Trade Date:	December 22, 1999
Effective Date:	December 22, 1999
Scheduled Termination Date:	October 26, 2004
Floating Amount Payer:	Party A
Fixed Amount Payer:	Party B

Calculation Agent:	Citibank
Business Day Convention:	Preceding.
Commodity Business Day Convention:	Preceding.
Periodic Payment Dates:	Each April 14 and October 14 of each year.
Payment Dates:	For payments to be made under Sections 3 and 4: (a) each Periodic Payment Date during the period from the Effective Date to but excluding the Cancellation Date; and (b) the Cancellation Date (but only if (x) the Cancellation Date is on or prior to the Periodic Payment Date in October 2004 and (y) no Event of Default or Termination Event shall have occurred and be continuing on the Cancellation Date). For payments to be made under Section 5: the Cancellation Date.
Market Disruption Events:	Price Source Disruption Trading Suspension Disappearance of Commodity Reference Price Tax Disruption
Disruption Fallback:	If a Market Disruption Event with respect to the Specified Price for the relevant Pricing Date occurs, then the Specified Price shall be determined by using the first preceding Commodity Business Day on which no Market Disruption Event existed with respect to the Specified Price (all as determined by the Calculation Agent).

2. *Initial Payment*

Initial Payment Date:	The Effective Date
Initial Payment Amount:	U.S.$94,274,598.00
Settlement:	On the Initial Payment Date, the Floating Amount Payer shall pay the Initial Payment Amount to Party B.

3. *Floating Payments*

Floating Payment Dates:	Each Payment Date.
Floating Amount:	For any Payment Date, the Periodic Notional Quantity for such Payment Date *multiplied by* the Periodic Floating Price for such Payment Date.

Periodic Notional Quantity:	(a) For the First Periodic Payment Date, 1,212,375 barrels *multiplied* by the First Periodic Payment Fraction; (b) for each Payment Date (other than the Payment Date referred to in clause (a) above) prior to the Cancellation Date, 1,212,375 barrels; and (c) for the Cancellation Date (if it is a Payment Date but is not the First Periodic Payment Date), 1,212,375 barrels *multiplied by* the Cancellation Fraction.
Periodic Floating Price:	For any Payment Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" for such Payment Date is the First Nearby Month with respect to such Payment Date; and (d) the "Pricing Date" is the Commodity Business Day that is three Commodity Business Days prior to such Payment Date (or, for determinations under Section 8 below, the Windup Date).
Settlement:	On each Payment Date, the Floating Amount Payer shall pay the Floating Amount for such Payment Date to Party B.

4. *Fixed Payments*

Fixed Payment Dates:	Each Payment Date.
Fixed Amount:	(a) For the First Periodic Payment Date, U.S.$29,000,000.00 *multiplied* by the First Periodic Payment Fraction; (b) for each Payment Date (other than the Payment Date referred to in clause (a) above) prior to the Cancellation Date, U.S.$29,000,000.00 and (c) for the Cancellation Date (if it is a Payment Date but is not the First Periodic Payment Date), U.S.$29,000,000.00 *multiplied by* the Cancellation Fraction.
Settlement:	On each Payment Date, the Fixed Amount Payer shall pay the Fixed Amount for such Payment Date to Party A.

5. *Final Payment*

Final Payment Date:	The Cancellation Date
Final Payment Amount:	The greater of: (a) U.S.$0.00; and (b) the Strike Price *minus* the product of (x) the Final Payment Notional Quantity and (y) the Final Payment Floating Price.
Strike Price:	U.S.$800,000,000
Final Payment Notional Quantity:	44,469,150 barrels
Final Payment Floating Price:	For the Final Payment Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" is the First Nearby Month with respect to the Final Payment Date; and (d) the "Pricing Date" is the Commodity Business Day that is three Commodity Business Days prior to the Final Payment Date (or, for determinations under Section 8 below, the Windup Date).
Settlement:	On the Final Payment Date, the Fixed Amount Payer shall pay the Final Payment Amount to Party A.

6. *Notice and Account Details*

Telephone, Telex and/or Facsimile Numbers and Contact Details for Notices:

Party A:	As specified in the Master Agreement
Party B:	As specified in the Master Agreement

Account Details:

Account Details of Party A:	Wire transfers to the Enron/Citibank Account
Account Details of Party B:	Wire transfers to: NationsBank of Texas, N.A. Account No. 3750494727 ABA No. 111000012

7. *Certain Definitions*:

As used in this Confirmation, the following terms shall have the following respective meanings:

"*Bankruptcy Code*" means the United States Bankruptcy Code, Title 11 of the United States Code, as amended.

"*Cancellation Date*" means the earliest to occur of:

(1) the Early Termination Date (if any) under the Master Agreement;

(2) such date as Party A and Party B may agree in writing to be the Cancellation Date; and

(3) the Scheduled Termination Date,

all as determined by the Calculation Agent in good faith in accordance with the terms of this Confirmation (and such determination shall be binding absent manifest error).

"*Cancellation Fraction*" means, for any Floating Payment and Fixed Payment to be made under Sections 3 and 4 above, respectively, on the Cancellation Date (if it is a Payment Date), a fraction, the numerator of which is equal to the actual number of days elapsed during the period from and including the immediately preceding Payment Date (or, if the Cancellation Date is the first Payment Date, from and including the Effective Date) to but excluding the Cancellation Date, and the denominator of which is equal to 180.

The "*Discounted Present Value*" of any payment (the "*Future Payment*") scheduled to be made on any date (the "*Future Payment Date*") and determined as at any date (the "*Determination Date*") is equal to the present value of such Future Payment, determined by discounting such Future Payment semi-annually on each Periodic Payment Date falling during the period from and including the Determination Date to and including such Future Payment Date at a rate *per annum* (determined on a 30/360 basis) equal to the Discount Rate, all as determined by the Calculation Agent in accordance with standard industry practice (*provided* that if the Future Payment Date is prior to the Determination Date, then the Discounted Present Value of the related Future Payment will be equal to such Future Payment).

"*Discount Rate*" means a rate per annum equal to 7.25%.

"*Enron*" means Enron Corp., a corporation organized under the laws of the State of Oregon, and its successors.

"*Enron/Citibank Account*" means the "Enron/Citibank Account" referred to in the Fiscal Agency Agreement.

"*Enron Guaranty*" means the Guaranty dated as of December 22, 1999 made and entered into by Enron in favor of Party A and its successors and assigns, substantially in the form of Exhibit I hereto.

"*First Periodic Payment Date*" means the Payment Date in April 2000.

"*First Periodic Payment Fraction*" means, for any Floating Payment and Fixed Payment to be made under Sections 3 and 4 above, respectively, on the First Periodic Payment Date, a fraction, the numerator of which is equal to the actual number of days elapsed during the period from and including the Effective Date to but excluding the First Periodic Payment Date, and the denominator of which is equal to 180.

"*Fiscal Agency Agreement*" means the Fiscal Agency Agreement dated as of November 18, 1999 among ENA, Enron, Citibank and the Fiscal Agent, as from time to time amended.

"*Fiscal Agent*" means United States Trust Company of New York, in its capacity as fiscal agent under the Fiscal Agency Agreement, together with its successors in such capacity.

"*Net Termination Amount*" means an amount equal to the Termination Payment owing by the Defaulting Party *minus* the Termination Payment owing by the Non-defaulting Party.

"*Termination Claims*" means, as to a Defaulting Party, amounts owing (or deemed owing) by such party under Section 8 of this Confirmation and under Section 6(e) of the Master Agreement (to the extent relating to this Transaction), together with all other amounts (including, without limitation, amounts owing under Section 11 of the Master Agreement and interest accruing on overdue amounts at the Default Rate) owing by such party with respect to this Transaction.

"*Termination Payment*" means, as to any party ("*X*"), an amount equal to:

(1) the sum of the Discounted Present Values of each Floating Amount (if any) scheduled to be made by X under Section 3 above during the period from and including the Windup Date to and including the Scheduled Termination Date;

(2) the sum of the Discounted Present Values of each Fixed Amount (if any) scheduled to be made by X under Section 4 above during the period from and including the Windup Date to and including the Scheduled Termination Date; *plus*

(3) the Discounted Present Value of the Final Payment Amount (if any) scheduled to be made by X under Section 5 above on the Scheduled Termination Date,

in each case determined as at the Windup Date. As used above, payments "scheduled to be made" on any date or during any period shall be determined as if all payments are to be made through and including the Scheduled Termination Date without regard to whether the Windup Date occurs prior thereto.

"*Transfer*" means a transfer, assignment or other disposition, and "*Transferred*" and "*Transferee*" have correlative meanings.

8. *Payments on Early Termination, Etc.*

Party A and Party B agree that, if an Early Termination Date occurs under the Master Agreement (such Early Termination Date being referred to herein as the "*Windup Date*"), then the Calculation Agent shall determine the Net Termination Amount, and:

(1) if the Net Termination Amount is positive, then the Defaulting Party will pay such amount to the Non-defaulting Party (together with interest on an amount equal to the Net Termination Amount at a stated rate of interest equal to the Discount Rate for the period from and including the immediately preceding Periodic Payment Date (or, if the Windup Date occurs prior to the first Periodic Payment Date, from and including the Effective Date) to but excluding the Windup Date); and

(2) if the Net Termination Amount is negative, then the Non-defaulting Party will pay the absolute value of the Net Termination Amount to the Defaulting Party.

Such payments shall be in lieu of payments that otherwise would be made on the Windup Date under Sections 3, 4 and 5 above (and in lieu of liquidation payments or payments on early termination that otherwise would be determined and payable in accordance with Section 6(e) of the Master Agreement), and shall constitute the final payments payable under or in respect of or in connection with this Confirmation and this Transaction (other than interest at the Default Rate payable on overdue amounts

and amounts payable under Section 11 of the Master Agreement in connection with this Transaction). Notwithstanding the foregoing, payments made in accordance with this Section 8 shall be deemed to be payments under Section 6(e) of the Master Agreement for all purposes thereof.

9. *Credit Support Documents, Margining, Etc.*

(a) *Credit Support Documents.*

Notwithstanding Part 4, Section 8(a), of the Schedule to the Master Agreement, the Enron Guaranty shall be the Credit Support Document of Party B as if referenced as such in said Part 4, Section 8.

(b) *Margining.*

Notwithstanding the provisions of Annex A (Collateral and Exposure Provisions) of the Master Agreement (the "*Annex*"), this Transaction shall not be considered a Transaction for the purpose of any determination made pursuant to the terms of the Annex. This Transaction shall, however, be considered as a Transaction for all other purposes related to the Master Agreement.

10. *Other Terms.*

(a) *Concerning the Calculation Agent.*

(1) Each party agrees that the Calculation Agent is not acting as a fiduciary for or as an advisor to either party in respect of its duties as Calculation Agent in connection with the Transaction to which this Confirmation relates.

(2) The Calculation Agent's calculations and determinations shall be made in good faith, in a commercially reasonable manner and be binding in the absence of manifest error.

(3) At least one Business Day prior to each date on which any payment is required to be made by Party B hereunder (and otherwise from time to time upon the reasonable request of the Fiscal Agent), the Calculation Agent shall provide to the Fiscal Agent a statement of amounts owing by Party B hereunder.

(b) *Swap Agreements.*

Each party hereby acknowledges and agrees that it intends, for all purposes relevant to such determination, that this Confirmation be treated as a "swap agreement" under the Bankruptcy Code.

(c) *Interpretation.*

Each reference to the singular shall include the plural and vice versa.

(d) *Headings.*

The headings used in this Confirmation are for convenience of reference only and are not to affect the construction of or to be taken into consideration in interpreting this Confirmation.

(e) *Additional Termination Events, Etc.*

For purposes of this Transaction, Section 5(b)(vi) of the Master Agreement (added pursuant to Part 1, Section 12 of the Schedule to the Master Agreement) shall not apply.

(f) *Assignments by Party B.*

Notwithstanding anything to the contrary in Section 7 of the Master Agreement, Party B reserves the right to transfer all (but not less than all) of its rights and obligations in respect of this Transaction to any of its Domestic Affiliates (such a transfer, an "*Affiliate Transfer*"), subject to the following conditions:

(1) Party B shall have given not less than 30 days' prior written notice of such Affiliate Transfer to Party A, specifying in such notice, *inter alia*, the name of such Domestic Affiliate.

(2) The Enron Guaranty (and all other Credit Support Documents applicable to this Transaction) shall continue in full force and effect in favor of Party A notwithstanding such Affiliate Transfer.

(3) No Event of Default or Termination Event with respect to Party B shall have occurred and be continuing (either on the date on which notice is given to Party A under clause (1) above or on the date of such Affiliate Transfer).

(4) Such Domestic Affiliate shall expressly assume, by an amendment hereto, executed and delivered to Party A, the due and punctual payment of all obligations of Party B hereunder and the performance of every covenant and obligation on the part of Party B to be performed or observed under or in respect of this Transaction.

(5) Party A and such Domestic Affiliate shall have entered into an agreement in substantially the form of the Master Agreement (including any Credit Support Documents requested by Party A), and such Domestic Affiliate shall have delivered to Party A all of the documents, instruments and other items required to be delivered under Part 3 of the Schedule to the Master Agreement.

(6) Such Domestic Affiliate shall have delivered to Party A an officer's certificate stating that such Affiliate Transfer (and all of the documents delivered in connection therewith) comply with this Section 10(f) and that all conditions precedent in this Section 10(f) relating to such Affiliate Transaction have been complied with.

(7) Such Domestic Affiliate shall have agreed to be bound by the Fiscal Agency Agreement to the same extent as Party B.

(8) Party A shall have received such other documents, instruments, opinions, information and other items in connection with such Affiliate Transfer as it may reasonably request.

For purposes of this Section 10(f), "*Domestic Affiliate*" means any Affiliate of Party B organized under the laws of the United States or any state thereof.

(g) *Assignments by Party A.*

(1) Notwithstanding anything in the Master Agreement (including, without limitation, in Section 7 thereof) to the contrary, Party B hereby acknowledges and agrees that all

Termination Claims owing by Party B may from time to time, without notice to or consent of Party B, be Transferred in whole or in part to one or more Transferees and in one or more separate transactions, and may be so Transferred successively, *provided* that irrespective of any such Transfer Party B shall continue to make all payments owing by it under this Transaction to the Enron/Citibank Account to the extent required under the Fiscal Agency Agreement.

(2) Party A and Party B acknowledge and agree that Transfers of Termination Claims owing by Party B shall be effected in accordance with the terms of the Fiscal Agency Agreement.

(3) Subject to paragraphs (1) and (2) above, Party A agrees that, so long as Party B is a Non-defaulting Party, it will Transfer its rights under this Confirmation only by surrender of this Confirmation to Party B and the issuance by Party B of a new Confirmation to the Transferee.

(4) At any time when the Fiscal Agency Agreement is not in effect, Party B shall be authorized to pay each person in whose name the ENA Claims are registered in the Claims Register maintained under the Fiscal Agency Agreement as of the time it ceased to be in effect (to the extent of the ENA Claims held by such person) until Party B receives notification that the ENA Claims held by such person have been assigned and that payment is to be made to the assignee, *provided* that (1) a notification that does not reasonably identify the rights assigned shall be ineffective and (2) if requested by Party B, the assignee of ENA Claims must seasonably furnish reasonable proof that the assignment has been made, and unless such assignee does so Party B may pay the assignor. As used in this paragraph (4), the terms "*ENA Claims*" and "*Claims Register*" have the meanings assigned to them in the Fiscal Agency Agreement.

(h) *Payments.*

Except as otherwise provided in the Fiscal Agency Agreement, Party A and Party B acknowledge that all payments to be made by Party B under this Confirmation (including, without limitation, all payments made in respect of Termination Claims owing by Party B that have been assigned by Party A to third parties) shall be made to the Enron/Citibank Account for application as provided in the Fiscal Agency Agreement.

(i) *Additional Termination Events.*

Solely for purposes of this Transaction, the following Additional Termination Event shall apply:

An Early Termination Date occurs under any Material Commodity Transaction, in which event:

(x) Party B shall be the Affected Party; and

(y) an Early Termination Date under this Transaction shall occur automatically on and as of the Early Termination Date under such Material Commodity Transaction.

As used in this Section 10(i), "*Material Commodity Transaction*" means a Commodity Transaction that (a) is a Transaction to which Party B is or has ever been a party and (b) is a Transaction having an initial notional amount or strike price in excess of

U.S.$250,000,000 (or its equivalent in other currencies, determined as of the trade date applicable to such Transaction).

(j) *Netting Provisions.*

Notwithstanding anything in the Master Agreement to the contrary:

(1) Section 2(c)(ii) of the Master Agreement will apply to this Transaction.

(2) For purposes of the Netting Provisions set forth in Paragraph 11 of Part 1 of the Schedule to the Master Agreement, if this Transaction is a Terminated Transaction, it shall not be aggregated with or netted against other Terminated Transactions in performing the calculations contemplated by Section 6(e) of the Master Agreement unless the Non-defaulting Party (or Non-Affected Party) so elects.

(k) *Default Rate.*

Notwithstanding anything in the Master Agreement to the contrary, the "Default Rate" for purposes of this Transaction shall be a stated rate of 8.25% per annum (calculated on a 30/360 basis), and interest accruing hereunder at the Default Rate shall be payable on demand of the Non-defaulting Party and in any event on each Periodic Payment Date (or, if any such date is not a Business Day, the next preceding Business Day).

(l) *Address for Notices.*

Solely with respect to this Transaction, Section 12(a) of the Master Agreement is hereby amended to delete the following phrase from the second and third line thereof: "(except that a notice or other communication under Section 5 or 6 may not be given by facsimile transmission or electronic messaging system)".

(m) *Definitions.*

Definitions. This Confirmation is subject to the 1991 ISDA Definitions as in effect on the date hereof without regard to any amendments, supplements, updates, or restatements thereto after the date hereof but including the Commodity Definitions as in effect on the date hereof to the extent this Transaction involves a "Commodity" as defined therein (the "*Definitions*"), each as published by ISDA, and will be governed in all respects by the Definitions (except that references to "Swap Transactions" in the Definitions will be deemed to be references to "Transactions"). The Definitions are incorporated by reference in, and made part of, this Confirmation as if set forth in full in this Confirmation. In the event of any inconsistency between the provisions of this Confirmation, the Master Agreement and the Definitions, this Confirmation will prevail for the purpose of this Transaction.

(n) *Confidentiality.*

Notwithstanding anything in Part 5, Section 14, of the Schedule to the Master Agreement to the contrary, Party B hereby agrees that Party A may disclose information otherwise restricted by said Part 5, Section 14 to Yosemite, the Collateral Agent, the holders from time to time of the Secured Obligations (other than the Yosemite Notes) referred to in the Collateral Security Agreement and, at any time following the occurrence of an Event of Default or Termination Event, the holders from time to time of the Yosemite Notes. As used herein, the following terms have the following meanings:

"*Collateral Agent*" means United States Trust Company of New York, in its capacity as "Collateral Agent" under the Collateral Security Agreement and the other Financing Documents referred to therein, and its successors in such capacity.

"*Collateral Security Agreement*" means the Collateral Security Agreement dated as of November 18, 1999 by and among (*inter alia*) Yosemite, Citibank and United States Trust Company of New York, in its capacity as indenture trustee, as amended.

"*Yosemite*" means Yosemite Securities Trust I, a Delaware statutory business trust, and its successors.

"*Yosemite Notes*" means the Notes issued under the Indenture dated as of November 18, 1999 between Yosemite and United States Trust Company of New York, as indenture trustee, as from time to time amended.

(o) *Waiver of Jury Trial.*

EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES TO THE FULLEST EXTENT PERMITTED BY LAW ALL RIGHT TO TRIAL BY JURY IN ANY PROCEEDING ARISING OUT OF OR RELATING DIRECTLY OR INDIRECTLY TO THIS CONFIRMATION OR THE TRANSACTIONS CONTEMPLATED HEREBY (WHETHER BASED ON CONTRACT, TORT OR ANY OTHER THEORY). EACH PARTY HERETO (A) CERTIFIES THAT NO REPRESENTATIVE, AGENT OR ATTORNEY OF ANY OTHER PARTY HAS REPRESENTED EXPRESSLY OR OTHERWISE, THAT SUCH PARTY WOULD NOT, IN THE EVENT OF LITIGATION, SEEK TO ENFORCE THE FOREGOING WAIVER AND (B) ACKNOWLEDGES THAT IT AND THE OTHER PARTIES HERETO HAVE BEEN INDUCED TO ENTER INTO THIS CONFIRMATION BY, AMONG OTHER THINGS, THE MUTUAL WAIVERS AND CERTIFICATIONS IN THIS PARAGRAPH.

[remainder of page intentionally blank]

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

CITIBANK, N.A.

By: _____
Authorized Signatory
Name:

Accepted and confirmed as
of the Trade Date:

ENRON NORTH AMERICA CORP.

By: _____
Authorized Signatory
Name:

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

CITIBANK, N.A.

By: _____
Authorized Signatory
Name:

Accepted and confirmed as
of the Trade Date:

ENRON NORTH AMERICA CORP.

By: _____
Authorized Signatory
Name: Joe Hunter
Agent and Attorney-In-Fact
Enron North America Corp.

Delta/Citibank Swap Confirmation

December 22, 1999

To: Delta Energy Corporation
P.O. Box 309
George Town, Grand Cayman
Cayman Islands, British West Indies
Attention: John Benbow
Facsimile No.: (345) 949-8080
Telephone No.: (345) 949-8066

From: Citibank, N.A.
399 Park Avenue
New York, New York 10043
Attention:
Facsimile No.:
Telephone No.:

Counterparty Ref:

Ladies and Gentlemen:

The purpose of this letter agreement (this "***Confirmation***") is to set forth the terms and conditions of the Transaction entered into between Citibank, N.A. ("***Party A***" or "***Citibank***") and Delta Energy Corporation ("***Party B***" or "***Delta***") on the Trade Date specified below (the "***Transaction***"). This Confirmation constitutes a "Confirmation" as referred to in the Master Agreement specified below. Certain capitalized terms used herein are defined in Section 7 below.

The definitions and provisions contained in the 1991 ISDA Definitions as in effect on the date hereof (as published by the International Swaps and Derivatives Association, Inc.) (the "***1991 Definitions***") are incorporated into this Confirmation. In addition, for purposes of the Floating Payments and Final Payment referred to below (the "***Commodity Transactions***"), the definitions and provisions contained in the 1993 ISDA Commodity Derivative Definitions as in effect on the date hereof (as published by the International Swaps and Derivatives Association, Inc.) (the "***Commodity Definitions***") are incorporated into this Confirmation. In the event of any inconsistency between the 1991 Definitions and this Confirmation, this Confirmation will govern; in the event of any inconsistency between the Commodity Definitions and this Confirmation, this Confirmation will govern; and in the event of any inconsistency between the Commodity Definitions and the 1991 Definitions in connection with the Commodity Transactions, the Commodity Definitions will govern.

This Confirmation supplements, forms a part of, and is subject to, the ISDA Master Agreement, dated as of September 27, 1994 (the "***Master Agreement***"), between Party A and Party B. All provisions contained in the Master Agreement govern this Confirmation except as expressly modified below.

Except as otherwise expressly provided herein, each party will make each payment specified in this Confirmation as being payable by it, not later than the due date for value on that date in the place of the account specified below, in freely transferable U.S. Dollars and in the manner customary for payments in U.S. Dollars.

The terms of the Transaction to which this Confirmation relates are as follows:

1. *General Terms*:

Trade Date:	December 22, 1999
Effective Date:	December 22, 1999
Scheduled Termination Date:	October 26, 2004
Fixed Amount Payer:	Party A
Floating Amount Payer:	Party B
Calculation Agent:	Citibank
Business Day Convention:	Preceding.
Commodity Business Day Convention:	Preceding.
Periodic Payment Dates:	Each April 14 and October 14 of each year.
Payment Dates:	For payments to be made under Sections 3 and 4: (a) each Periodic Payment Date during the period from the Effective Date to but excluding the Cancellation Date; and (b) the Cancellation Date (but only if (x) the Cancellation Date is on or prior to the Periodic Payment Date in October 2004 and (y) no Event of Default or Termination Event shall have occurred and be continuing on the Cancellation Date). For payments to be made under Section 5: the Cancellation Date.
Market Disruption Events:	Price Source Disruption Trading Suspension Disappearance of Commodity Reference Price Tax Disruption
Disruption Fallback:	If a Market Disruption Event with respect to the Specified Price for the relevant Pricing Date occurs, then the Specified Price shall be determined by using the first preceding Commodity Business Day on which no Market Disruption Event existed with respect to the Specified Price (all as determined by the Calculation Agent).

2. *Initial Payment*

Initial Payment Date:	The Effective Date
Initial Payment Amount:	U.S.$94,274,598.00
Settlement:	On the Initial Payment Date, Party B shall pay the Initial Payment Amount to Party A.

3. *Floating Payments*

Floating Payment Dates:	Each Payment Date
Floating Amount:	For any Payment Date, the Periodic Notional Quantity for such Payment Date *multiplied by* the Periodic Floating Price for such Payment Date.
Periodic Notional Quantity:	(a) For the First Periodic Payment Date, 1,212,375 barrels *multiplied* by the First Periodic Payment Fraction; (b) for each Payment Date (other than the Payment Date referred to in clause (a) above) prior to the Cancellation Date, 1,212,375 barrels; and (c) for the Cancellation Date (if it is a Payment Date but is not the First Periodic Payment Date), 1,212,375 barrels *multiplied by* the Cancellation Fraction.
Periodic Floating Price:	For any Payment Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" for such Payment Date is the First Nearby Month with respect to such Payment Date; and (d) the "Pricing Date" is the Commodity Business Day that is three Commodity Business Days prior to such Payment Date (or, for determinations under Section 8(a) below, the Windup Date).
Settlement:	On each Payment Date, the Floating Amount Payer shall pay the Floating Amount for such Payment Date to Party A.

4. *Fixed Payments*

Fixed Payment Dates:	Each Payment Date
Fixed Amount:	(a) For the First Periodic Payment Date, U.S.$29,000,000.00 *multiplied* by the First Periodic Payment Fraction; (b) For each Payment Date (other than the Payment Date referred to in clause (a) above) prior to the Cancellation Date, U.S.$29,000,000.00 and (c) for the Cancellation Date (if it is a Payment Date but is not the First Periodic Payment Date), U.S.$29,000,000.00 *multiplied by* the Cancellation Fraction.
Settlement:	On each Payment Date, the Fixed Amount Payer shall pay the Fixed Amount for such Payment Date to Party B.

5. *Final Payment*

Final Payment Date:	The Cancellation Date
Final Payment Amount:	The greater of: (a) U.S.$0.00; and (b) U.S.$800,000,000 *minus* the product of (x) the Final Notional Quantity and (y) the Final Floating Price.
Final Notional Quantity:	44,469,150 barrels
Final Floating Price:	For the Final Payment Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" is the First Nearby Month with respect to the Final Payment Date; and (d) the "Pricing Date" is the Commodity Business Day that is three Commodity Business Days prior to the Final Payment Date (or, for determinations under Section 8(a) below, the Windup Date).
Settlement:	On the Final Payment Date, Party A shall pay the Final Payment Amount to Party B.

6. *Notice and Account Details*

Telephone, Telex and/or Facsimile Numbers and Contact Details for Notices:

Party A:	As specified in the Master Agreement
Party B:	As specified in the Master Agreement

Account Details:

Account Details of Party A:	Citibank, N.A., New York ABA No. 021000089 Account No. 00167679 Financial Futures Reference Commodities Department 46
Account Details of Party B:	Wire transfers to the Collection and Payment Account

7. *Certain Definitions*:

As used in this Confirmation, the following terms shall have the following respective meanings:

"*Bankruptcy Code*" means the United States Bankruptcy Code, Title 11 of the United States Code, as amended.

"*Cancellation Date*" means the earliest to occur of:

(1) the Early Termination Date (if any) under the Agreement;

(2) such date as Party A and Party B may agree in writing to be the Cancellation Date; and

(3) the Scheduled Termination Date,

all as determined by the Calculation Agent.

"*Cancellation Fraction*" means, for any Floating Payment and Fixed Payment to be made under Sections 3 and 4 above, respectively, on the Cancellation Date, a fraction, the numerator of which is equal to the actual number of days elapsed during the period from and including the immediately preceding Payment Date (or, if the Cancellation Date is the first Payment Date, from the Effective Date) to but excluding the Cancellation Date, and the denominator of which is equal to 180.

"*Collection and Payment Account*" means the "Collection and Payment Account" referred to in the Paying Agency Agreement.

"*Delta Note*" means the Note dated November 18, 1999 payable by Delta to Yosemite and its registered assigns in the original principal amount of U.S.$800,000,000, as amended by Amendment No. 1 dated as of December 22, 1999 thereto.

The "*Discounted Present Value*" of any payment (the "*Future Payment*") scheduled to be made on any date (the "*Future Payment Date*") and determined as at any date (the "*Determination Date*") is equal to the present value of such Future Payment, determined by discounting such Future Payment semi-annually on each Periodic Payment Date falling during the period from and including the Determination Date to and including such Future Payment Date at a rate *per annum* (determined on a 30/360 basis) equal to the Discount Rate, all as determined by the Calculation Agent in accordance with standard industry practice (*provided* that if the Future Payment Date is prior to the Determination Date, then the Discounted Present Value of the related Future Payment will be equal to such Future Payment).

"*Discount Rate*" means a rate per annum equal to 7.25%.

"*Enron*" means Enron Corp., a corporation organized under the laws of the State of Oregon, and its successors.

"*Enron/Citibank Swap*" means the ISDA Master Agreement (and the Schedule thereto) dated as of November 17, 1992 between Enron North America and Citibank and the Confirmation dated as of December 22, 1999 thereunder. Reference in this Confirmation to the Enron/Citibank Swap shall include reference to any guarantee thereof by Enron or any of its affiliates.

"*Enron/Delta Swap*" means the ISDA Master Agreement (and the Schedule thereto) dated as of November 18, 1999 between Enron North America and Delta and the Confirmation dated as of December 22, 1999 thereunder. Reference in this Confirmation to the Enron/Delta Swap shall include reference to any guarantee thereof by Enron or any of its affiliates.

"*Enron North America*" means Enron North America Corp., a Delaware corporation (formerly known as Enron Capital & Trade Resources Corp.), and its successors and assigns under either or both of the Enron Swaps.

"*Enron Swap Obligations*" means obligations of Enron North America then owing to Citibank under the Enron/Citibank Swap (and related guaranty obligations of Enron), whether or not performing.

"*Enron Swaps*" means (a) the Enron/Citibank Swap and (b) the Enron/Delta Swap.

"*First Periodic Payment Date*" means the Payment Date in April 2000.

"*First Periodic Payment Fraction*" means, for any Floating Payment and Fixed Payment to be made under Sections 3 and 4 above, respectively, on the First Periodic Payment Date, a fraction, the numerator of which is equal to the actual number of days elapsed during the period from and including the Effective Date to but excluding the First Periodic Payment Date, and the denominator of which is equal to 180.

"*Net Termination Amount*" means an amount equal to the Termination Payment owing by the Defaulting Party *minus* the Termination Payment owing by the Non-defaulting Party.

"*Paying Agency Agreement*" means the Paying Agency Agreement dated as of November 18, 1999 among Delta and the Paying Agent, as from time to time amended.

"*Paying Agent*" means United States Trust Company of New York, as paying agent under the Paying Agency Agreement, and its successors in such capacity.

"*Termination Payment*" means, as to any party ("*X*"), an amount equal to:

(1) the sum of the Discounted Present Values of each Floating Amount (if any) scheduled to be made by X under Section 3 above during the period from and including the Windup Date to and including the Scheduled Termination Date;

(2) the sum of the Discounted Present Values of each Fixed Amount (if any) scheduled to be made by X under Section 4 above during the period from and including the Windup Date to and including the Scheduled Termination Date; *plus*

(3) the Discounted Present Value of the Final Payment Amount (if any) scheduled to be made by X under Section 5 above on the Scheduled Termination Date,

in each case determined as at the Windup Date. As used above, payments "scheduled to be made" on any date or during any period shall be determined as if all payments are to be made through and including the Scheduled Termination Date without regard to whether the Windup Date occurs prior thereto.

8. ***Payments on Early Termination, Etc.***

(a) Party A and Party B agree that, if an Early Termination Date occurs under the Master Agreement above (such Early Termination Date being referred to herein as the "*Windup Date*"), then the Calculation Agent shall determine the Net Termination Amount, and:

(x) if the Net Termination Amount is positive, then the Defaulting Party will pay such amount to the Non-defaulting Party (together with interest on an amount equal to the Net Termination Amount at a stated rate of interest equal to the Default Rate applicable to this Transaction for the period from and including the immediately preceding Periodic Payment Date (or, if the Windup Date occurs prior to the first Periodic Payment Date, from and including the Effective Date) to but excluding the Windup Date); and

(y) if the Net Termination Amount is negative, then the Non-defaulting Party will pay the absolute value of the Net Termination Amount to the Defaulting Party.

Such payments shall be in lieu of payments that otherwise would be made on the Windup Date under Sections 3, 4 and 5 above (and in lieu of liquidation payments or payments on early termination that otherwise would be determined and payable in accordance with Section 6(e) of the Master Agreement), and shall constitute the final payments payable under or in respect of or in connection with this Confirmation and this Transaction (other than interest at the Default Rate payable on overdue amounts and amounts payable under Section 11 of the Master Agreement in connection with this Transaction). Notwithstanding the foregoing, payments made in accordance with this Section 8(a) shall be deemed to be payments under Section 6(e) of the Master Agreement for all purposes thereof.

(b) Notwithstanding anything in this Confirmation or the Master Agreement to the contrary, Party B hereby acknowledges and agrees that, at any time following the occurrence and during the continuance of an Event of Default or Termination Event, Party A may elect to satisfy all or any portion of its obligations under Sections 4, 5 and 8(a) above by transferring (on one or more occasions) to Party B Enron Swap Obligations (and, in such connection, Party A's obligations under Sections 4, 5 and 8(a) above will be so satisfied in an aggregate amount equal to the aggregate outstanding amount of Enron Swap Obligations so transferred to Party B).

9. *Other Terms.*

(a) *Concerning the Calculation Agent.*

(1) Each party agrees that the Calculation Agent is not acting as a fiduciary for or as an advisor to either party in respect of its duties as Calculation Agent in connection with Transaction to which this Confirmation relates.

(2) The Calculation Agent's calculations and determinations shall be made in good faith, in a commercially reasonable manner and be binding in the absence of manifest error.

(3) At least one Business Day prior to each date on which any payment is required to be made by Party A hereunder (and otherwise from time to time upon the reasonable request of the Paying Agent), the Calculation Agent shall provide to the Paying Agent a statement of amounts owing by Party A hereunder.

(b) *Swap Agreements.*

Each party hereby acknowledges and agrees that it intends, for all purposes relevant to such determination, that this Confirmation be treated as a "swap agreement" under the Bankruptcy Code.

(c) *Interpretation.*

Each reference to the singular shall include the plural and vice versa.

(d) *Headings.*

The headings used in this Confirmation are for convenience of reference only and are not to affect the construction of or to be taken into consideration in interpreting this Confirmation.

(e) *Undertakings of Party B Relating to the Delta Note, Etc.*

Without the prior written consent of Party A, Party B hereby agrees that it shall not (1) amend, modify or otherwise supplement the Delta Note or the Enron/Delta Swap or (2) amend, modify, otherwise supplement or terminate the Paying Agency Agreement or the Enron/Delta Fiscal Agency Agreement (as defined in the Delta Note). By its signature below, Party A hereby consents to (x) Amendment No. 1 dated as of December 22, 1999 to the Delta Note, (y) the termination of the "Enron/Delta Swap" referred to in the Delta Note (as in effect prior to Amendment No. 1 thereto) and, in substitution therefor, the execution, delivery and performance by Party B of the Enron/Delta Swap referred to herein and (z) Amendment No. 1 dated as of December 22, 1999 to the Enron/Delta Fiscal Agency Agreement.

(f) *Payments.*

Party A and Party B acknowledge that all payments to be made by Party A under this Confirmation shall be made to the Collection and Payment Account for application as provided in the Paying Agency Agreement.

(g) *Netting Provisions.*

Notwithstanding anything in the Master Agreement to the contrary, Section 2(c)(ii) of the Master Agreement will apply to this Transaction.

(h) *Additional Termination Events.*

Solely for purposes of this Transaction, the following Additional Termination Events shall apply.

An Early Termination Date occurs under any Material Commodity Transaction, in which event:

(A) Party B shall be the Affected Party; and

(B) an Early Termination Date under this Transaction shall occur automatically on and as of the Early Termination Date under such Material Commodity Transaction.

As used in this Section 8(i), "*Material Commodity Transaction*" means a Commodity Transaction that (a) is a Transaction to which Party B is a party and (b) is a Transaction having an initial notional amount or strike price in excess of U.S.$250,000,000 (or its equivalent in other currencies, determined as of the trade date applicable to such Transaction).

(i) *Cross Default.*

Solely for purposes of this Transaction, "*Specified Indebtedness*" includes, with respect to Party B, the Delta Note (and in such connection the "*Threshold Amount*" related thereto shall be deemed to be equal to zero).

(j) *Delivery of Enron Obligations.*

In consideration of the Final Payment to be made by Party A to Party B hereunder on the Cancellation Date, Party B hereby agrees that, upon request by Party A at any time and from time to time following the occurrence of an "Event of Default" under and as defined in the Delta Note,

Party B shall exercise its rights (to the extent requested by Party A) under the second paragraph of Paragraph 2(c) of the Delta Note to deliver "Enron Swap Obligations" (as defined in the Delta Note) in satisfaction of its obligations thereunder.

(k) *Address for Notices.*

Solely with respect to this Transaction, Section 12(a) of the Master Agreement is hereby amended to delete the following phrase from the second and third line thereof: "(except that a notice or other communication under Section 5 or 6 may not be given by facsimile transmission or electronic messaging system)".

(l) *Default Rate.*

Notwithstanding anything in the Master Agreement to the contrary, the "Default Rate" for purposes of this Transaction shall be a stated rate of 8.25% per annum (calculated on a 30/360 basis), and interest accruing hereunder at the Default Rate shall be payable on demand of the Non-defaulting Party and in any event on each Periodic Payment Date (or, if any such date is not a Business Day, the next preceding Business Day).

(m) *Waiver of Jury Trial.*

EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES TO THE FULLEST EXTENT PERMITTED BY LAW ALL RIGHT TO TRIAL BY JURY IN ANY PROCEEDING ARISING OUT OF OR RELATING DIRECTLY OR INDIRECTLY TO THIS AGREEMENT OR THE TRANSACTIONS CONTEMPLATED HEREBY (WHETHER BASED ON CONTRACT, TORT OR ANY OTHER THEORY). EACH PARTY HERETO (A) CERTIFIES THAT NO REPRESENTATIVE, AGENT OR ATTORNEY OF ANY OTHER PARTY HAS REPRESENTED EXPRESSLY OR OTHERWISE, THAT SUCH PARTY WOULD NOT, IN THE EVENT OF LITIGATION, SEEK TO ENFORCE THE FOREGOING WAIVER AND (B) ACKNOWLEDGES THAT IT AND THE OTHER PARTIES HERETO HAVE BEEN INDUCED TO ENTER INTO THIS AGREEMENT BY, AMONG OTHER THINGS, THE MUTUAL WAIVERS AND CERTIFICATIONS IN THIS PARAGRAPH.

[remainder of page intentionally blank]

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

CITIBANK, N.A.

By: _____
Authorized Signatory
Name:

Accepted and confirmed as
of the Trade Date:

DELTA ENERGY CORPORATION

By: _____
Authorized Signatory
Name:

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

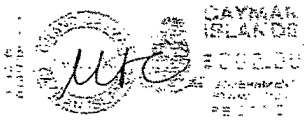
CITIBANK, N.A.

By: _____
Authorized Signatory
Name:

Accepted and confirmed as
of the Trade Date:

DELTA ENERGY CORPORATION

By: _____
Authorized Signatory
Name: V. A. BENSON



MTH&M DRAFT
~~10/20/99~~ 11/02/99

Enron/Delta Swap Confirmation

~~October~~ November [__], 1999

To: Delta Energy Corporation
~~[~~P.O. Box 309
George Town, Grand Cayman
Cayman Islands, British West Indies~~]~~
Attention:
Facsimile No.: (___) ___-____
Telephone No.: (___) ___-____

From: ~~[~~Enron North America Corp.~~]~~
~~[address]~~ 1400 Smith Street
Houston, Texas 77002
Attention:
Facsimile No.: (___) ___-____
Telephone No.: (___) ___-____

Counterparty Ref:

Ladies and Gentlemen:

The purpose of this letter agreement (this "***Confirmation***") is to set forth the terms and conditions of the Transaction entered into between ~~[~~Enron North America ~~]~~ Corp. ("***Party A***" or "***ENA***") and Delta Energy Corporation ("***Party B***" or "***Delta***") on the Trade Date specified below (the "***Transaction***"). This Confirmation constitutes a "Confirmation" as referred to in the Master Agreement specified below. Certain capitalized terms used herein are defined in Section 6 below. ~~7 below.~~

~~The definitions and provisions contained in the 1991 ISDA Definitions (as published by the International Swaps and Derivatives Association, Inc.) (the "1991 Definitions") are incorporated into this Confirmation. In addition, for purposes of the Periodic Floating Payments and Maturity Floating Payment referred to below (the "Commodity Transactions"), the definitions and provisions contained in the 1993 ISDA Commodity Derivative Definitions (as published by the International Swaps and Derivatives Association, Inc.) (the "Commodity Definitions") are incorporated into this Confirmation. In the event of any inconsistency between the 1991 Definitions and this Confirmation, this Confirmation will govern; in the event of any inconsistency between the Commodity Definitions and this Confirmation, this Confirmation will govern; and in the event of any inconsistency between the Commodity Definitions and the 1991 Definitions in connection with the Commodity Transactions, the Commodity Definitions will govern.~~

This Confirmation supplements, forms a part of, and is subject to, the ISDA Master Agreement, dated as of ~~October~~ November [__], 1999 (the "***Master Agreement***"), between Party A and Party B. All provisions contained in the Master Agreement govern this Confirmation except as expressly modified below.

~~Each party is hereby advised, and each such party acknowledges, that the other party has engaged in (or refrained from engaging in) substantial financial transactions and has taken other material actions in reliance upon the parties' entry into the Transaction to which this Confirmation relates on the terms and conditions set forth below.~~

Permanent Subcommittee on Investigations
EXHIBIT #186m

Each party will make each payment specified in this Confirmation as being payable by it, not later than the due date for value on that date in the place of the account specified below, in freely transferable U.S. Dollars and in the manner customary for payments in U.S. Dollars.

The terms of the Transaction to which this Confirmation relates are as follows:

1. *General Terms*:

Trade Date:	~~October~~ November [__], 1999
Effective Date:	~~October~~ November [__], 1999
Scheduled Termination Date:	Payment Date in ~~October~~ November 2006
~~Fixed~~ Periodic Floating Amount Payer:	Party ~~B Maturity Cap Buyer: Party A Maturity Cap Seller: Party B Periodic Floating~~ A
Fixed Amount Payer:	Party ~~A Maturity Floating Amount Payer: Party A~~ B
Calculation Agent:	Citibank ~~Calculation Agent City: New York, New York~~
Business Day Convention:	Following
Commodity Business Day Convention:	Following
Payment Dates:	(a) Each ~~January [__], April [__], July~~ May [__] and ~~October~~ November [__] falling during the period from the Effective Date to but excluding the Cancellation Date; and (b) the Cancellation Date.
Market Disruption Events:	Price Source Disruption Trading Suspension Disappearance of Commodity Reference Price Tax Disruption ~~Disruption~~ ~~Trading Suspension~~ ~~[others]~~
Disruption Fallback:	Calculation Agent Determination

2. *Fixed Payment*

Fixed Payment Date:	The Effective Date
Fixed Payment Amount:	~~U.S.$800,000,000.00~~[U.S.$728,000,000.00]
Settlement:	On the Fixed Payment Date, the Fixed Amount Payer shall pay the Fixed Payment Amount to Party A.

3. ~~*Maturity Cap Purchase. Maturity Cap Purchase Date: The Effective Date Maturity Cap Purchase Price: U.S.$72,000,000.00 Settlement: On the Maturity Cap Purchase Date, the Maturity Cap Buyer shall pay the Maturity Cap Purchase Price to the Maturity Cap Seller.*~~

~~*4. Periodic Floating Payments*~~

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Periodic Floating Payment Dates:	Each Payment Date
Periodic Floating Amount:	For any Payment Date, the Periodic Notional Quantity for such Payment Date *multiplied by* the Periodic Floating Price for such Payment Date.
Periodic Notional Quantity:	(a) For each Payment Date prior to the Cancellation Date, [842,105] barrels; and (b) for the Cancellation Date, [842,105] barrels *multiplied by* the Cancellation Fraction.
Periodic Floating Price:	For any Payment Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" for such Payment Date is **the month and year falling two months after** such Payment Date; and (d) the "Pricing Date" for such Payment Date is the Commodity Business Day ~~immediately preceding~~ **that is three Commodity Business Days prior to** such Payment Date.
Settlement:	On each Payment Date, the ~~Periodic~~ Floating Amount Payer shall pay the Periodic Floating Amount for such Payment Date to Party B.

~~5. Maturity~~ **4. *Final* Floating Payment**

~~Maturity~~ **Final** Floating Payment Date:	The Cancellation Date
~~Maturity~~ **Final** Floating Amount:	The lesser of: (a) the ~~Maturity~~ **Final** Notional Quantity *multiplied by* the ~~Maturity~~ **Final** Floating Price; and (b) ~~the Maturity Cap Amount. Maturity~~[U.S.$800,000,000.00].
Final Notional Quantity:	[40,000,000] barrels
~~Maturity~~ **Final** Floating Price:	For the Cancellation Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" is ~~December 2006~~ **the month and year falling two months after the Cancellation Date**; and

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(d) the "Pricing Date" is the Commodity Business Day ~~immediately preceding~~ **that is three Commodity Business Days prior to** the Cancellation Date.

~~Maturity Cap Amount: U.S.$800,000,000.00~~ Settlement: On the ~~Maturity~~ **Final** Floating Payment Date, the ~~Maturity~~ Floating **Amount** Payer shall pay the ~~Maturity~~ **Final** Floating ~~Payment~~ **Amount** to Party B.

6 **5**. *Notice and Account Details*

Telephone, Telex and/or Facsimile Numbers and Contact Details for Notices:

Party A: [to be advised]

Party B: [to be advised]

Account Details:

Account Details of Party A: [to be advised]

Account Details of Party B: [to be advised]

7. *Certain Definitions*:

As used in this Confirmation, the following terms shall have the following respective meanings:

"*Bankruptcy Code*" means the United States Bankruptcy Code, Title 11 of the United States Code, as amended.

"*Cancellation Date*" means the earliest to occur of:

(1) the Early Termination Date (if any) under the ~~Agreement;~~ **Master Agreement;**

~~**(2) the date (if any) on which an Enron Bankruptcy occurs;**~~

~~**(3) the date (if any) on which an Enron Failure to Pay occurs;**~~

~~(4)~~**[**(2) 10 days after the date (if any) on which [Enron has elected to redeem the Yosemite Notes in accordance with the Enron/Citibank Agreement]**]**; and

~~(5)~~**(3)** the Scheduled Termination Date~~.~~**,**

all as determined by the Calculation Agent.

"*Cancellation Fraction*" means, for any Periodic Floating Payment to be made under Section 4 **3** above on the Cancellation Date, a fraction, the numerator of which is equal to the actual number of days elapsed during the period from and including the immediately preceding Payment Date (or, if the Cancellation Date is the first Payment Date, from the Effective Date) to but excluding the Cancellation Date, and the denominator of which is equal to 90.

"*Citibank*" means Citibank, N.A., a national banking association, and its successors.

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"*Collateral Agent*" means United States Trust Company of New York, in its capacity as "Collateral Agent" under the Collateral Security Agreement and the other Financing Documents referred to therein, and its successors in such capacity.

"*Collateral Security Agreement*" means the Collateral Security Agreement dated as of November [ ], 1999 by and among *(inter alia)* the Yosemite Securities Trust I, Citibank and United States Trust Company of New York, in its capacity as indenture trustee, as amended.

"*Delta Note*" means the Note dated November [ ], 1999 payable by Party B to Yosemite and its assigns in the original principal amount of [U.S.$800,000,000], as amended.

"*Enron*" means Enron Corp., a corporation organized under the laws of the State of Oregon, and its successors.

~~"Enron Bankruptcy" means that any of the following shall occur:~~

~~(i) without petition, approval or consent of Enron, a period of 60 days shall have elapsed after:~~

~~(a) the entry of an order for relief under the Bankruptcy Code by a court of competent jurisdiction; or~~

~~(b) the entry by a court of competent jurisdiction of an order granting relief under any applicable bankruptcy, insolvency or other similar law or statute of the United States of America or any State thereof; or~~

~~(c) the appointment by such a court of a trustee, custodian or receiver of Enron or of all or any substantial part of its property upon the application of any creditor in any insolvency or bankruptcy proceeding or other creditor's suit,~~

~~but such period of 60 days shall not include any period during which any such decree or order shall be stayed upon appeal or otherwise; or~~

~~(ii) the filing, consenting or acquiescing by Enron of a petition seeking an order for relief under the Bankruptcy Code or the making by it of an assignment for the benefit of creditors or the consenting by it to, or failure by it to contest, the appointment of a custodian or receiver of all or any substantial part of the property of Enron or the filing by Enron of a petition or answer seeking, consenting to or acquiescing in the granting of relief under any other applicable bankruptcy, insolvency or other similar law or statute of the United States of America or any State thereof.~~

"*Enron/Citibank Agreement*" means the Agreement dated as of ~~October~~ November [ ], 1999 between Citibank and Enron relating to, *inter alia*, Yosemite, as amended.~~"Enron/Citibank Swap" means the Confirmation (Reference No. [ ]) dated as of October [ ], 1999 between ENA and Citibank, as amended. Reference in this Confirmation to the Enron/Citibank Swap shall include reference to any guarantee thereof by Enron or any of its affiliates.~~

~~"Enron Failure to Pay" means (a) a Failure to Pay by Enron on an Obligation with respect to which there is Publicly Available Information confirming the occurrence of such Failure to Pay; or (b) ENA or Enron shall fail to pay any amount owing by it under the~~

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~~Agreement (including any failure to pay any amount owing by it under this Confirmation); or (c) ENA or Enron shall fail to pay any amount owing by it under the Enron/Citibank Swap.~~

~~"Enron North America" means [Enron North America], a [_____] corporation (formerly known as [_____]), and its successors.~~

~~"Failure to Pay" means the failure by an obligor with respect to a specified Obligation to make, when due, any payments due thereunder, after giving effect to any applicable grace period.~~

~~"Obligation" means any senior obligation of an obligor in the amount of U.S.$25,000,000 or more incurred in the capacity of principal, surety or otherwise, for the payment or repayment of money, which would rank at least equal in priority of payment to the senior unsecured indebtedness for borrowed money in a bankruptcy of such obligor under Chapter 11 of the Bankruptcy Code.~~

~~"Public Source" means each of Bloomberg Service, Dow Jones Telerate Service, Reuter Monitor Money Rates Services, Dow Jones News Wire, the Wall Street Journal, the New York Times, Nihon Keizai Shinbun and the Financial Times and their respective successor publications.~~

~~"Publicly Available Information" means information that reasonably confirms any of the facts relevant to the determination that an Enron Failure to Pay has occurred and that:~~

~~(a) has been published in any internationally recognized published or electronically displayed news source (it being understood that each Public Source shall be deemed to be an internationally recognized published or electronically displayed news source), regardless of whether the reader or user thereof pays a fee to obtain such information; provided that, if either Party A or Party B or any of their respective affiliates is cited as the sole source of such information, then such information shall not be deemed to be "Publicly Available Information" unless such party or its affiliate is acting in its capacity as fiscal agent, administrative agent or paying agent for an Obligation; or~~

~~(b) is information received from (i) Enron or any of its affiliates or (ii) a trustee, a fiscal agent, administrative agent or paying agent for an Obligation of Enron or any of its affiliates; or~~

~~(c) is information contained in any order, decree or notice, however described, of a court, tribunal, regulatory authority or similar administrative or judicial body.~~

"*Yosemite*" means Yosemite Securities Trust I, a Delaware business trust, and its successors.

"*Yosemite Notes*" means the Notes issued under the Indenture dated as of ~~October~~ November [__], 1999 between Yosemite and ~~Bankers~~ United States Trust Company, as Indenture Trustee, in the original aggregate principal amount of [U.S.$_____], as amended.

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~~6~~ 7. *Payments on Early Termination.*

Party A and Party B agree that, if an Early Termination Date occurs under the **Master** Agreement, the Periodic Floating Amount and ~~Maturity~~ **Final** Floating Amount to be paid on the Cancellation Date in accordance with Sections 4 **3** and ~~5~~ **4** above, respectively, shall be so paid, such payments shall constitute the final payments payable under or in respect of or in connection with this Confirmation and the Transaction to which this Confirmation relates, and shall be in lieu of liquidation payments or payments on early termination that otherwise would be determined and payable in accordance with Section 6(e) of the ~~Agreement.~~ **Master Agreement (it being understood that payments made in accordance with this Section 7 shall be deemed to be payments under Section 6(e) of the Master Agreement for all purposes thereof).**

~~7~~ 8. *Other Terms.*

(a) *Concerning the Calculation Agent.*

(1) Party A and Party B hereby **irrevocably** appoint Citibank as the Calculation Agent hereunder, and by its signature below Citibank accepts such appointment. Citibank (and any successor Calculation Agent) may, by not less than 30 days' prior written notice to Party A and Party B, resign as Calculation Agent (*provided* that such resignation shall not become effective until a successor Calculation Agent shall have been appointed by Party A and Party B).

(2) Each party agrees that the Calculation Agent is not acting as a fiduciary for or as an advisor to either party in respect of its duties as Calculation Agent in connection with Transaction to which this Confirmation relates.

(3) The Calculation Agent's calculations and determinations shall be made in good faith, in a commercially reasonable manner and be binding in the absence of manifest error.

(b) *Swap Agreements.*

Each ~~party~~ hereby acknowledges and agrees that it intends, **for all purposes relevant to such determination,** that this Confirmation be treated as a "swap agreement" under the Bankruptcy Code.

(c) *Interpretation.*

Each reference to the singular shall include the plural and vice versa.

(d) *Headings.*

The headings used in this Confirmation are for convenience of reference only and are not to affect the construction of or to be taken into consideration in interpreting this Confirmation.

(e) ***Additional Credit Support Documents, Etc.***

For purposes of this Transaction, "Credit Support Document" includes, in relation to Party A, the Enron Guaranty.

For purposes of this Transaction, "Credit Support Provider" includes, in relation to Party A, Enron.

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(f) *Assignments by Party A.*

Notwithstanding anything to the contrary in Section 7 of the Master Agreement, Party A reserves the right to transfer all (but not less than all) of its rights and obligations in respect of this Transaction to any of its Domestic Affiliates (such a transfer, an "*Affiliate Transfer*"), subject to the following conditions:

(1) Party A shall have given not less than 30 days' prior written notice of such Affiliate Transfer to Party B, specifying in such notice, *inter alia*, the name of such Domestic Affiliate.

(2) The Enron Guaranty (and all other Credit Support Documents applicable to this Transaction) shall continue in full force and effect in favor of Party B notwithstanding such Affiliate Transfer.

(3) No Event of Default or Termination Event shall have occurred and be continuing (either on the date on which notice is given to Party B under clause (1) above or on the date of such Affiliate Transfer).

[(4) All (but not less than all) of Party A's rights and obligations in respect of the [Enron/Citibank Swap] are contemporaneously transferred to such Domestic Affiliate.]

(5) Such Domestic Affiliate shall expressly assume, by an amendment hereto, executed and delivered to Party B, the due and punctual payment of all obligations of Party A hereunder and the performance of every covenant and obligation on the part of Party A to be performed or observed under or in respect of this Transaction.

(6) Party B and such Domestic Affiliate shall have entered into an agreement in substantially the form of the Master Agreement (including any Credit Support Documents requested by Party B), and such Domestic Affiliate shall have delivered to Party B all of the documents, instruments and other items required to be delivered under Part 3 of the Schedule to the Master Agreement.

(7) Such Domestic Affiliate shall have delivered to Party B an officer's certificate and an opinion of counsel each stating that such Affiliate Transfer (and all of the documents delivered in connection therewith) comply with this Section 9(f), that all conditions precedent in this Section 9(f) relating to such Affiliate Transaction have been complied with and that no adverse tax consequences will result therefrom to Party B.

(8) Party B shall have received such other documents, instruments, opinions, information and other items in connection with such Affiliate Transfer as it may reasonably request.

For purposes of this Section 9(f), "*Domestic Affiliate*" means [any affiliate of Party A organized under the laws of the United States or any state thereof.]

(g) *Assignments by Party B.*

Notwithstanding anything in Section 7 of the Master Agreement to the contrary, Party A hereby acknowledges that:

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(1) all of Party B's rights under or in respect of this Transaction, including rights under the Enron Guaranty (collectively, the "*Relevant Assets*"), are to be pledged to Yosemite to secure Party B's obligations under the Delta Note; and

(2) all of Yosemite's rights with respect to the Relevant Assets are to be pledged to the Collateral Agent for the benefit of the holders of the Yosemite Notes and the other secured obligations referred to in the Collateral Security Agreement,

and Party A hereby consents to such pledges.

[remainder of page intentionally blank]

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Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

[ENRON NORTH AMERICA CORP.]

By: _____
Authorized Signatory
Name:

Accepted and confirmed as
of the Trade Date:

DELTA ENERGY CORPORATION

By: _____
Authorized Signatory
Name:

By its signature below, Citibank, N.A. hereby agrees to act as initial Calculation Agent for purposes of the Transaction to which this Confirmation relates on the terms set forth in Section 9(a) above:

CITIBANK, N.A., as initial Calculation Agent

By: _____
Authorized Signatory
Name:

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MTH&M DRAFT
~~10/20/99~~ 11/02/99

Citibank/Enron Swap Confirmation

~~October~~ November [__], 1999

To: ~~[~~Enron North America Corp.~~]~~
~~[address]~~ 1400 Smith Street
Houston, Texas 77002
Attention:
Facsimile No.: (___) ___-____
Telephone No.: (___) ___-____

From: Citibank, N.A.
~~[~~399 Park Avenue
New York, New York 10043~~]~~
Attention:
Facsimile No.: (___) ___-____
Telephone No.: (___) ___-____

Counterparty Ref:

Ladies and Gentlemen:

The purpose of this letter agreement (this "***Confirmation***") is to set forth the terms and conditions of the Transaction entered into between ~~[Enron North America] (formerly known as [ECT]) ("Party A" or "ENA")~~ and Citibank, N.A. ~~("Party B" or "Citibank")~~ A" or "*Citibank*") and Enron North America Corp. (formerly known as Enron Capital & Trade Resources Corp.) ("*Party B*" or "*ENA*") on the Trade Date specified below (the "***Transaction***"). This Confirmation constitutes a "Confirmation" as referred to in the Master Agreement specified below. Certain capitalized terms used herein are defined in Section 7 below.

~~The definitions and provisions contained in the 1991 ISDA Definitions (as published by the International Swaps and Derivatives Association, Inc.) (the "1991 Definitions") are incorporated into this Confirmation. In addition, for purposes of the Floating Payments and Maturity Floor Payment referred to below (the "Commodity Transactions"), the definitions and provisions contained in the 1993 ISDA Commodity Derivative Definitions (as published by the International Swaps and Derivatives Association, Inc.) (the "Commodity Definitions") are incorporated into this Confirmation. In the event of any inconsistency between the 1991 Definitions and this Confirmation, this Confirmation will govern; in the event of any inconsistency between the Commodity Definitions and this Confirmation, this Confirmation will govern; and in the event of any inconsistency between the Commodity Definitions and the 1991 Definitions in connection with the Commodity Transactions, the Commodity Definitions will govern.~~

This Confirmation supplements, forms a part of, and is subject to, the ISDA Master Agreement, dated as of ~~[_____, 19__]~~ November 17, 1992 (the "*Master Agreement*"), between Party A and Party B. All provisions contained in the Master Agreement govern this Confirmation except as expressly modified below.

~~Each party is hereby advised, and each such party acknowledges, that the other party has engaged in (or refrained from engaging in) substantial financial transactions and has taken other material actions in reliance upon the parties' entry into the Transaction to which this Confirmation relates on the terms and conditions set forth below.~~

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Each party will make each payment specified in this Confirmation as being payable by it, not later than the due date for value on that date in the place of the account specified below, in freely transferable U.S. Dollars and in the manner customary for payments in U.S. Dollars.

The terms of the Transaction to which this Confirmation relates are as follows:

1. *General Terms*:

Trade Date:	~~October~~ November [__], 1999
Effective Date:	~~October~~ November [__], 1999
Scheduled Termination Date:	Payment Date in ~~October 2006 Maturity Floor Seller: Party A Maturity Floor Buyer: Party B~~ November 2006
Floating Amount Payer:	Party A
Fixed Amount Payer: ~~Party A Floating Amount Payer:~~	Party B
Calculation Agent:	Citibank ~~Calculation Agent City: New York, New York~~
Business Day Convention:	Following
Commodity Business Day Convention:	Following
Payment Dates:	(a) Each ~~January [__], April [__], July~~ May [__] and ~~October~~ November [__] falling during the period from the Effective Date to but excluding the Cancellation Date; and (b) the Cancellation Date.
Market Disruption Events:	Price Source Disruption Trading Suspension Disappearance of Commodity Reference Price Tax Disruption ~~Disruption~~ ~~Trading Suspension~~ ~~[others]~~
Disruption Fallback:	Calculation Agent Determination

2. ~~*Maturity Floor Purchase Maturity Floor Purchase*~~ *Initial Payment*

Initial Payment Date:	The Effective Date

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Initial Payment Amount:	[U.S.$72,000,000.00] ~~Maturity Floor Purchase Price: U.S.$72,000,000.00 Settlement: On the Maturity Floor Purchase Date, the Maturity Floor Buyer shall pay the Maturity Floor Purchase Price to the Maturity Floor Seller. 3. Maturity Floor Payment Maturity Floor Payment Date: The Cancellation Date Maturity Floor Payment Amount: The greater of:~~ ~~(a) U.S.$0.00; and~~ ~~(b) U.S.$800,000,000 minus (x) the Maturity Floor Notional Quantity multiplied by (y) the Maturity Floor Floating Price. Maturity Floor Notional Quantity: 40,000,000 barrels Maturity Floor Floating Price: For the Cancellation Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" is December 2006; and (d) the "Pricing Date" is the Commodity Business Day immediately preceding the Cancellation Date.~~
Settlement:	On the ~~Maturity Floor~~ **Initial** Payment Date, the ~~Maturity Floor Seller~~ **Floating Amount Payer** shall pay the ~~Maturity Floor~~ **Initial** Payment Amount to ~~the Maturity Floor Buyer. 4~~ **Party B.**

3. ***Floating Payments***

Floating Payment Dates:	Each Payment Date
Floating Amount:	For any Payment Date, the Periodic Notional Quantity for such Payment Date *multiplied by* the Periodic Floating Price for such Payment Date.
Periodic Notional Quantity:	(a) For each Payment Date prior to the Cancellation Date, [842,105] barrels; and (b) for the Cancellation Date, [842,105] barrels *multiplied by* the Cancellation Fraction.
Periodic Floating Price:	For any Payment Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" for such Payment Date is **the month and year falling two months after** such Payment Date; and (d) the "Pricing Date" for such Payment Date is the Commodity Business Day ~~immediately preceding~~ **that is three Commodity Business Days prior to** such Payment Date.
Settlement:	On each Payment Date, the Floating Amount Payer shall pay the Floating Amount for such Payment Date to ~~Party A. 5~~ **Party B.**

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4. *Fixed Payments*

Fixed Payment Dates:	Each Payment Date
Fixed Amount:	(a) For each Payment Date prior to the Cancellation Date, [U.S.$16,000,000.00]; and (b) for the Cancellation Date, [U.S.$16,000,000.00] *multiplied by* the Cancellation Fraction.
Settlement:	On each Payment Date, the Fixed Amount Payer shall pay the Fixed Amount for such Payment Date to Party ~~B~~ A.

5. *Final Payment*

Final Payment Date:	The Cancellation Date
Final Payment Amount:	The greater of: (a) U.S.$0.00; and (b) [U.S.$800,000,000] *minus* the product of (x) the Final Payment Notional Quantity and (y) the Final Payment Floating Price.
Final Payment Notional Quantity:	[40,000,000] barrels
Final Payment Floating Price:	For the Cancellation Date, a "Floating Price" determined in accordance with the Commodity Definitions, where: (a) the "Commodity Reference Price" is OIL-WTI-NYMEX; (b) the "Specified Price" is the closing price; (c) the "Delivery Date" is the month and year falling two months after the Cancellation Date; and (d) the "Pricing Date" is the Commodity Business Day that is three Commodity Business Days prior to the Cancellation Date.
Settlement:	On the Final Payment Date, the Fixed Amount Payer shall pay the Final Payment Amount to Party A.

6. *Notice and Account Details*

Telephone, Telex and/or Facsimile Numbers and Contact Details for Notices:

Party A:	~~[to be advised] Party B: [to be advised]~~ As specified in the Master Agreement
Party B:	As specified in the Master Agreement

Account Details:

Account Details of Party A:	~~[to be advised]~~ Citibank, N.A., New York ABA No. 021000089 Account No. 00167679 Financial Futures Reference Commodities Department 46
Account Details of Party B:	[to be advised]

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7. *Certain Definitions*:

As used in this Confirmation, the following terms shall have the following respective meanings:

"*Bankruptcy Code*" means the United States Bankruptcy Code, Title 11 of the United States Code, as amended.

"*Cancellation Date*" means the earliest to occur of:

(1) the Early Termination Date (if any) under the ~~Agreement;~~ **Master Agreement;**

~~(2) the date (if any) on which an Enron Bankruptcy occurs;~~

~~(3) the date (if any) on which an Enron Failure to Pay occurs;~~

~~(4)~~**(2)** 10 days after the date (if any) on which [Enron has elected to redeem the Yosemite Notes in accordance with the Enron/Citibank Agreement]**1**; and

~~(5)~~**(3)** the Scheduled Termination Date~~,~~**.**

all as determined by the Calculation Agent.

"*Cancellation Fraction*" means, for any Floating Payment and Fixed Payment to be made under Sections ~~4~~ **3** and ~~5~~ **4** above, respectively, on the Cancellation Date, a fraction, the numerator of which is equal to the actual number of days elapsed during the period from and including the immediately preceding Payment Date (or, if the Cancellation Date is the first Payment Date, from the Effective Date) to but excluding the Cancellation Date, and the denominator of which is equal to 90.

"*Enron*" means Enron Corp., a corporation organized under the laws of the State of Oregon, and its successors.

~~"Enron Bankruptcy" means that any of the following shall occur:~~

~~(i) without petition, approval or consent of Enron, a period of 60 days shall have elapsed after:~~

~~(a) the entry of an order for relief under the Bankruptcy Code by a court of competent jurisdiction; or~~

~~(b) the entry by a court of competent jurisdiction of an order granting relief under any applicable bankruptcy, insolvency or other similar law or statute of the United States of America or any State thereof; or~~

~~(c) the appointment by such a court of a trustee, custodian or receiver of Enron or of all or any substantial part of its property upon the application of any creditor in any insolvency or bankruptcy proceeding or other creditor's suit,~~

~~but such period of 60 days shall not include any period during which any such decree or order shall be stayed upon appeal or otherwise; or~~

~~(ii) the filing, consenting or acquiescing by Enron of a petition seeking an order for relief under the Bankruptcy Code or the making by it of an assignment for the benefit of creditors or the consenting by it to, or failure by it to contest, the appointment of a custodian or receiver of all or any substantial part of the property of Enron or the filing by Enron of a~~

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~~petition or answer seeking, consenting to or acquiescing in the granting of relief under any other applicable bankruptcy, insolvency or other similar law or statute of the United States of America or any State thereof.~~

[~~"~~*Enron/Citibank Agreement*" means the Agreement dated as of ~~October~~ November [__], 1999 between Citibank and Enron relating to, *inter alia*, Yosemite, as amended.~~"Enron Failure to Pay" means (a) a Failure to Pay by Enron on an Obligation with respect to which there is Publicly Available Information confirming the occurrence of such Failure to Pay; or (b) ENA or Enron shall fail to pay any amount owing by it under the Agreement (including any failure to pay any amount owing by it under this Confirmation).~~]

~~"Failure to Pay" means the failure by an obligor with respect to a specified Obligation to make, when due, any payments due thereunder, after giving effect to any applicable grace period.~~**"*Enron Guaranty*" means the Guaranty dated as of November [__], 1999 made and entered into by Enron in favor of Party A and its successors and assigns, substantially in the form of Exhibit I hereto, as amended.**

~~"Obligation" means any senior obligation of an obligor in the amount of U.S.$25,000,000 or more incurred in the capacity of principal, surety or otherwise, for the payment or repayment of money, which would rank at least equal in priority of payment to the senior unsecured indebtedness for borrowed money in a bankruptcy of such obligor under Chapter 11 of the Bankruptcy Code.~~

~~"Public Source" means each of Bloomberg Service, Dow Jones Telerate Service, Reuter Moniter Money Rates Services, Dow Jones News Wire, the Wall Street Journal, the New York Times, Nihon Keizai Shinbun and the Financial Times and their respective successor publications.~~

~~"Publicly Available Information" means information that reasonably confirms any of the facts relevant to the determination that an Enron Failure to Pay has occurred and that:~~

~~(a) has been published in any internationally recognized published or electronically displayed news source (it being understood that each Public Source shall be deemed to be an internationally recognized published or electronically displayed news source), regardless of whether the reader or user thereof pays a fee to obtain such information; provided that, if Party A or any of its affiliates is cited as the sole source of such information, then such information shall not be deemed to be "Publicly Available Information" unless such Party A or its affiliate is acting in its capacity as fiscal agent, administrative agent or paying agent for an Obligation; or~~

~~(b) is information received from (i) Enron or any of its affiliates or (ii) a trustee, a fiscal agent, administrative agent or paying agent for an Obligation of Enron or any of its affiliates; or~~

~~(c) is information contained in any order, decree or notice, however described, of a court, tribunal, regulatory authority or similar administrative or judicial body.~~

[~~"~~*Yosemite*" means Yosemite Securities Trust I, a Delaware business trust, and its successors.]

[~~"~~*Yosemite Notes*" means the Notes issued under the Indenture dated as of ~~October~~ November [__], 1999 between Yosemite and Bankers Trust Company, as Indenture Trustee, in the original aggregate principal amount of [U.S.$_____], as amended.]

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8. *Payments on Early Termination.*

Party A and Party B agree that, if an Early Termination Date occurs under the **Master** Agreement, the ~~Maturity Floor Payment~~ **Floating** Amount, ~~Floating~~ **Fixed** Amount and ~~Fixed~~ **Final Payment** Amount to be paid on the Cancellation Date in accordance with Sections 3, 4 and 5 above, respectively, shall be so paid, such payments shall constitute the final payments payable under or in respect of or in connection with this Confirmation and the Transaction to which this Confirmation relates, and shall be in lieu of liquidation payments or payments on early termination that otherwise would be determined and payable in accordance with Section 6(e) of the ~~Agreement.~~ **Master Agreement (it being understood that payments made in accordance with this Section 8 shall be deemed to be payments under Section 6(e) of the Master Agreement for all purposes thereof).**

~~9. Margining.~~

~~Solely for purposes of the~~ **9.** *Credit Support Documents ~~referred to in the Agreement, Citibank agrees that Citibank's "Exposure" under the Transaction to which this Confirmation relates shall at all times be deemed to be equal to zero.~~ Margining, Etc.*

(a) ***Credit Support Documents.***

Notwithstanding Part 4, Section 8(n), of the Schedule to the Master Agreement, the Enron Guaranty shall be the Credit Support Document of Party B as if referenced as such in said Part 4, Section 8.

(b) ***Margining.***

Notwithstanding the provisions of Annex A (Collateral and Exposure Provisions) of the Master Agreement (the "*Annex*"), this Transaction shall not be considered a Transaction for the purpose of any determination made pursuant to the terms of the Annex. This Transaction shall, however, be considered as a Transaction for all other purposes related to the Master Agreement.

Notwithstanding the provisions of the Annex, for purposes of determining the Exposure Threshold with respect to Party A on any date during the term of this Transaction, the Exposure Threshold of Party A shall be [ ].

10. *Other Terms.*

(a) *Concerning the Calculation Agent.*

(1) Each party agrees that the Calculation Agent is not acting as a fiduciary for or as an advisor to either party in respect of its duties as Calculation Agent in connection with the Transaction to which this Confirmation relates.

(2) The Calculation Agent's calculations and determinations shall be made in good faith, in a commercially reasonable manner and be binding in the absence of manifest error.

(b) *Swap Agreements.*

Each party hereby acknowledges and agrees that it intends, **for all purposes relevant to such determination,** that this Confirmation be treated as a "swap agreement" under the Bankruptcy Code.

(c) *Interpretation.*

Each reference to the singular shall include the plural and vice versa.

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(d) *Headings.*

The headings used in this Confirmation are for convenience of reference only and are not to affect the construction of or to be taken into consideration in interpreting this Confirmation.

(e) *Additional Termination Events, Etc.*

For purposes of this Transaction, Section 5(b)(vi) of the Master Agreement (added pursuant to Part 1, Section 12 of the Schedule to the Master Agreement) shall not apply.

(f) *Assignments by Party B.*

Notwithstanding anything to the contrary in Section 7 of the Master Agreement, Party B reserves the right to transfer all (but not less than all) of its rights and obligations in respect of this Transaction to any of its Domestic Affiliates (such a transfer, an "*Affiliate Transfer*"), subject to the following conditions:

(1) Party B shall have given not less than 30 days' prior written notice of such Affiliate Transfer to Party A, specifying in such notice, *inter alia*, the name of such Domestic Affiliate.

(2) The Enron Guaranty (and all other Credit Support Documents applicable to this Transaction) shall continue in full force and effect in favor of Party A notwithstanding such Affiliate Transfer.

(3) No Event of Default or Termination Event shall have occurred and be continuing (either on the date on which notice is given to Party A under clause (1) above or on the date of such Affiliate Transfer).

[(4) All (but not less than all) of Party B's rights and obligations in respect of the [Enron/Delta Swap] are contemporaneously transferred to such Domestic Affiliate.]

(5) Such Domestic Affiliate shall expressly assume, by an amendment hereto, executed and delivered to Party A, the due and punctual payment of all obligations of Party B hereunder and the performance of every covenant and obligation on the part of Party B to be performed or observed under or in respect of this Transaction.

(6) Party A and such Domestic Affiliate shall have entered into an agreement in substantially the form of the Master Agreement (including any Credit Support Documents requested by Party A), and such Domestic Affiliate shall have delivered to Party A all of the documents, instruments and other items required to be delivered under Part 3 of the Schedule to the Master Agreement.

(7) Such Domestic Affiliate shall have delivered to Party A an officer's certificate and an opinion of counsel each stating that such Affiliate Transfer (and all of the documents delivered in connection therewith) comply with this Section 10(f), that all conditions precedent in this Section 10(f) relating to such Affiliate Transaction have been complied with and that no adverse tax consequences will result therefrom to Party A.

(8) Party A shall have received such other documents, instruments, opinions, information and other items in connection with such Affiliate Transfer as it may reasonably request.

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For purposes of this Section 10(f), "*Domestic Affiliate*" means [any affiliate of Party B organized under the laws of the United States or any state thereof.]

[remainder of page intentionally blank]

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Please confirm that the foregoing correctly sets forth the terms of our agreement by executing the copy of this Confirmation enclosed for that purpose and returning it to us.

Very truly yours,

CITIBANK, N.A.

By: _____
Authorized Signatory
Name:

Accepted and confirmed as
of the Trade Date:

[ENRON NORTH AMERICA CORP.]

By: _____
Authorized Signatory
Name:

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Unknown

From: Wagman, Steve [FI]
Sent: Tuesday, November 13, 2001 7:12 PM
To: Swanson, Timothy [FI]
Subject: FW: Citibank Unwind Amounts

Importance: High

tim, we will need to terminate the floating legs with delta tomorrow. Below are the amounts and payment dates. I will go over with hybrid desk in the morning (and you). Please confirm you understand this as the deal is done and we will need to ticke and follow the cash flows

-----Original Message-----
From: Wagman, Steve [FI]
Sent: Tuesday, November 13, 2001 7:11 PM
To: Junek, Lydia G; Alan Rafte (E-mail)
Cc: Lyons, Chris [FI]
Subject: FW: Citibank Unwind Amounts
Importance: High

below looks fine by me--I have sent same message to ene.
In addition
Global loans to cover the hybrid desk for 267.5 in additional breakage.

Please confirm receipt (and understanding)...I'll be around for a bit more 2night.

I

-----Original Message-----
From: Wagman, Steve [FI]
Sent: Tuesday, November 13, 2001 7:07 PM
To: 'Garberding, Michael'; Bills, Lisa; Cook, Mary; Boyle, Dan
Subject: RE: Citibank Unwind Amounts
Importance: High

looks good to me.
lets go with it.

-----Original Message-----
From: Garberding, Michael [mailto:Michael.Garberding@enron.com]
Sent: Tuesday, November 13, 2001 7:01 PM
To: Wagman, Steve [FI]; Bills, Lisa; Cook, Mary; Boyle, Dan
Subject: Citibank Unwind Amounts

Steve --

Included is the amounts as discussed:

Interest under existing prepay
$4,245,417
=(250,000,000*(4.43%*(138/360)))

Transwestern (payable upon funding Nov. 14):

Permanent Subcommittee on Investigations
EXHIBIT #186n

CITI-SPSI 0068679

Share of Interest under existing prepay
$2,334,979
=(55%*4,245,417)
Break Funding Costs
$330,000

Total Transwestern Payable upon Funding.
$2,664,979

Northern (payable upon funding Nov. 16):
Share of Interest under existing prepay
$1,910,438
=(45%*4,245,417)
Interest on O/S Balance through Nov. 16
$42,237
=((112,500,000+1,910,438)*(4.43%*(3/360))

Total Northern Payable upon Funding
$1,952,675

Let me know when you get the chance. Thanks

Michael Garberding
Enron Americas Global Finance
Work: (713) 853-1864
Fax: (713) 646-3602
E-mail: michael.garberding@enron.com

****
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****

Unknown

From: Angelini, Amanda [FI]
Sent: Sunday, December 02, 2001 12:23 PM
To: Caplan, Rick [FI]
Subject: Re: Ene

Can I tell him why or just be criptic? Frank wld probably tell him anyway

-----Original Message-----
From: Caplan, Rick [FI] <rc52842@imcnam.ssmb.com>
To: Angelini, Amanda [FI] <aa19374@imcnam.ssmb.com>
Sent: Sun Dec 02 12:21:26 2001
Subject: Re: Ene

I resent to frank. Yes call ray.

-----Original Message-----
From: Angelini, Amanda [FI] <aa19374@imcnam.ssmb.com>
To: Caplan, Rick [FI] <rc52842@imcnam.ssmb.com>
Sent: Sun Dec 02 12:18:02 2001
Subject: Re: Ene

Shd I make sure ray has all notices ready for mon morning? Is the aol address frank?

-----Original Message-----
From: Caplan, Rick [FI] <rc52842@imcnam.ssmb.com>
To: Bendernagel, Donald [GCG] <db52626@imcnam.ssmb.com>; Angelini, Amanda [FI] <aa19374@imcnam.ssmb.com>; 'aol.com' <fpuleo@milbank.com;afpuleo>
CC: Wagner, Eleanor [CRRM] <ew15838@imcnam.ssmb.com>
Sent: Sun Dec 02 12:01:24 2001
Subject: Ene

Not for public consumption, they filed today - in ny believe it or not. Tomorrow should be real fun. Want to make sure swaps are terminated first thing and that delta terminates simultaneously so that we don't have any mismatch. Also, the one place we will get push back is the "actively traded" piece of the definition of DO in the ecln trades. We should have bruce prepared to speak to how the bank market fits the definition as that is what we relied upon. He should remember the issue, we spent considerable time on it - I assume, frank, you remember too?

Permanent Subcommittee on Investigations
EXHIBIT #186o

citigroup

Jane C. Sherburne
Deputy General Counsel
Litigation and Compliance

Citigroup Inc.
1101 Pennsylvania Avenue NW
Suite 530
Washington, DC 20004

Tel 202 220 3690
Fax 202 220 3699
New York 212 793 4942
sherburnej@citi.com

May 2, 2002

BY TELECOPY AND FIRST CLASS MAIL

The Honorable Carl Levin
Chairman
The Honorable Susan Collins
Ranking Minority Member
United States Senate
Committee on Governmental Affairs
Permanent Subcommittee on Investigations
Washington, D.C. 20515-6115

In the Matter of Enron Corporation

Dear Senator Levin and Senator Collins:

This letter responds to Senator Levin's April 11, 2002 request that Citigroup provide the Subcommittee with a list of its transactions with Enron. We understand this request to cover the time period from 1997 to the present. Citigroup[1] summarizes its transactions with Enron,[2] during this period as follows:

A. Securities Underwriting

1. Equity Underwriting

- February 1999: Enron Corp. 12MM shares Common Stock Offering (Credit Suisse First Boston ("CSFB") and Donaldson Lufkin & Jenrette ("DLJ") were co-lead underwriters; SSB participated as a syndicate member).

---

[1] Citigroup was formed in October 1998 and includes Salomon Smith Barney (formed by the merger of Smith Barney and Salomon Brothers in November 1997), Travelers Group, Citibank, N.A. and Citicorp. Unless otherwise expressly stated, any references to Citigroup in this letter should be read to include any or all of these entities.

[2] For ease of reference, Enron refers to Enron Corporation and its affiliates and subsidiaries with which Citigroup had a business relationship.

Permanent Subcommittee on Investigations
EXHIBIT #186p

- August 1999: Enron Oil & Gas ("EOG") 31MM shares Common Stock Offering (Goldman Sachs and Bank of America were co-lead underwriters; SSB participated as a syndicate member).

- August 1999: Enron Corp. $10MM 7% Exchangeable Notes Offering (Goldman Sachs was lead underwriter; SSB participated as a co-manager).

- October 2000: The New Power Company 24MM shares Initial Public Offering (CSFB and DLJ were co-lead underwriters; SSB participated as a syndicate member).

- November 2000: Northern Borders Partners, L.P., 1.875MM Primary Common Units Offering (SSB was co-lead underwriter with Paine Webber).

- February 2001: Enron Corp. $1.9B Zero Coupon Convertible Senior Notes due February 7, 2021 (SSB was lead manager and underwriter).

- May 2001: Northern Borders Partners, L.P. 4.5MM Common Units Offering (SSB was co-lead underwriter with UBS Warburg).

- August 2001: Northern Borders Partners, L.P. 3.8MM Common Units Offering (SSB was co-lead underwriter with UBS Warburg).

2. Debt Underwriting

- January 1997: Enron Capital Trust II $6MM 8.13% Trust-Originated Securities (Merrill Lynch was lead underwriter; Smith Barney participated as a syndicate member).

- September 1997: EOG $100MM 6.5% Notes due September 15, 2004 (Salomon Bros. was lead underwriter).

- November 1997: Enron Corp. $300MM 6.45% Notes due November 15, 2001 (Salomon Bros. was lead underwriter).

- November 1997: Enron Corp. $150MM Floating Rate Notes due November 18, 1999 (Smith Barney was sole underwriter).

- September 1998: Enron Corp. $250MM Floating Rate Notes due March 30, 2000 (SSB was co-lead underwriter with Merrill Lynch).

- December 1998: EOG $175MM 6% Notes due December 15, 2008 (SSB was co-lead underwriter with NationsBank Montgomery).

- August 1999: Northern Borders Pipeline Co. $200MM 7.75% Senior Notes due September 1, 2009 (Banc of America Securities and Lehman Bros. were joint lead managers; SSB was among the initial purchasers).

- March 2000: Portland General Electric Co. $150MM 7.875% Notes due March 15, 2010 (ABN Amro was lead underwriter; SSB participated as a syndicate member).

3. Other Debt Offerings

- September 1999: Osprey Trust, Osprey I, Inc. $1.4B 8.31% Senior Structured Notes due January 14, 2003 (DLJ was lead manager; SSB was among the initial purchasers).

- November 1999: Yosemite Securities Trust I $750MM 8.25% Linked Enron Obligations due November 15, 2004 (SSB was lead manager and Citibank, or an affiliate thereof, made a $37.5MM investment relating to certificates issued by Yosemite Securities Trust I).

- February 2000: Yosemite Securities Company Ltd. £200MM 8.75% Linked Enron Obligations due February 23, 2007 (SSB was sole manager and Citibank, or an affiliate thereof, made a £11.125MM investment relating to certificates issued by Yosemite Securities Company Ltd.).

- August 2000: Enron Credit Linked Notes ("ECLN") Trust $500MM 8% Enron Credit Linked Notes due August 15, 2005 (SSB was lead manager and Citibank, or an affiliate thereof, made a $50MM investment relating to certificates issued by ECLN Trust).

- May 2001: ECLN Trust II $500MM 7.375% Enron Credit Linked Notes Offering due May 15, 2006 (SSB was lead manager and Citibank, or an affiliate thereof, made a $50MM investment relating to certificates issued by ECLN Trust II).

- May 2001: Enron Sterling Credit Linked Notes Trust £125MMN 7.25% Enron Sterling Credit Linked Notes due May 24, 2006 (Schroder Salomon Smith Barney ("SSSB") was lead manager and Citibank, or an affiliate thereof, made a £14MM investment relating to certificates issued by Enron Sterling Credit Linked Notes Trust).

- May 2001: Enron Euro Credit Linked Notes Trust €200MM 6.5% Enron Euro Credit Linked Notes due May 24, 2006 (SSSB was lead manager and Citibank, or an affiliate thereof, made a £22.5MM investment relating to certificates issued by Enron Euro Credit Linked Notes Trust).

B. Advisory Services

- SSB acted as a financial advisor to Enron on its acquisition of Portland General Corp. (July 1997).

- SSB acted as a financial advisor to Enron on its acquisition of Cogen Technologies (November 1998).

- SSB acted as a financial advisor to a special committee of the Enron board on re-acquisition of Azurix, a water company previously divested by Enron (Fall 1999).

- SSB acted as a financial advisor to Enron on its acquisition of Daishowa Paper Products (December 2000).

- SSB, with JPMorgan Chase, acted as a financial advisor to Enron on to its attempted merger with Dynegy (October/November 2001).

- SSB is currently acting as a financial advisor to a special committee of the Enron board that is overseeing the re-integration of Azurix.

C. Credit Facilities and Other Financings

1. Credit Facilities

- In May 1997, Citibank arranged a $600MM, 364-day revolving credit facility for Enron Corp., and held $75MM of the total commitment.

- In May 1998, the 1997 facility was replaced with a $1B, 364-day revolving facility arranged by Citibank; Citibank held $36MM. The May 1998 364-day revolving facility was renewed in May 1999.

- In August 1999, the $1B facility was replaced with a $1.5B, 364-day revolving facility arranged by Citibank; Citibank held $41MM.

- In May 2000, the $1.5B facility was replaced with a $1.75B, 364-day facility and a $1.25B, 5-year facility; Citibank held $46.7MM and $33.3MM, respectively.

- In May 2001, the $1.75B, 364-day revolving credit facility was renewed; Citibank held $65.9MM.

- Also in May 2001, Citibank syndicated for Enron Corp. a $500MM letter of credit facility and held $18.8MM.

- In December 2001, following Enron's Chapter 11 bankruptcy filing, Citibank and JPMorgan Chase arranged up to $1.5B in debtor-in-possession financing.

- In December 1999, together with Barclays, Citibank arranged a $375MM, 364-day revolving credit facility for Enron Funding Corp. Citibank held $50MM. In March 2000, the facility was decreased to $355MM, extended for another 364 days, and Citibank decreased its commitment to $38MM. In March 2001, the facility was extended for another 364 days and Citibank increased its commitment to $50MM.

- In August 1994, Citibank participated (as a member of a bank syndicate led by Chase Manhattan Bank and Barclays) in a 4½-year, $490MM revolving credit facility for Joint Energy Development Investments ("JEDI"). Citibank's original share of the facility was $10MM, which amount remained constant upon the facility's increase to $750MM in December 1996, but was reduced to $5.5MM in May 1998.

- In May 1998, Citibank participated (as a member of a bank syndicate led by Chase Manhattan Bank and Barclays) in a 3-year, $500MM revolving credit facility for JEDI II; Citibank held $10MM. On June 29, 2001, the facility was reduced to $250MM, and Citibank's commitment was reduced to $5MM. On June 28, 2001, Citibank's $5MM commitment was renewed, and the $250MM credit facility was extended for an additional 364 days.

- In November 2001, Citibank extended $600MM in secured financing to Transwestern Pipeline Company and Northern Natural Gas, two pipeline subsidiaries of Enron.

2. Project Finance Transactions

- In December 1998, Citibank participated in the $500MM financing of a Brazilian electricity distributor ("Elektro"). Citibank committed $100MM of which it held $50MM. Citibank's hold position increased to $52.5MM in July 1999.

- In May 1999, Citibank participated as a co-arranger and lender in the $880MM financing of a power plant project in India ("Dabhol II"). Citibank held $65.47MM.

- In December 2000, Citibank participated in the $600MM financing of gas-fired projects ("Turbopark"). Citibank committed $200MM of which it held $75MM.

- In December 2000, Citibank participated in the $49MM financing of pulp and paper assets ("Garden State Paper"). Citibank held $24.5MM.

- In December 2000, Citibank participated in the $250MM financing of Enron's pulp and paper trading business ("Caymus"). Citibank held $242.5MM.

3. Structured Transactions

- December 1997: Citibank structured, and was a lender in connection with, a $500MM minority interest financing transaction ("Nighthawk").

- December 1998: Citibank structured and was a lender in connection with a $750MM minority interest financing transaction ("Rawhide").

- December 1999: Citibank structured and was a lender in connection with a $500MM minority interest financing transaction ("Nahanni").

4. Asset Securitizations

- In September 1997, Citibank and Credit Lyonnais, together, underwrote and syndicated $150MM to fund the purchase of royalty payments received by Destec Properties Limited Partnership, an Enron subsidiary, from Houston Lighting and Power relating to certain coal reserves. Citibank held $25MM.

5. Foreign Exchange, Interest Rate and Other Derivative Transactions

- In December 1998, Citibank entered into a $500MM, three-year prepaid forward natural gas and crude oil sale involving Enron.

- In June 1999, Citibank entered into a 90-day, cash-settled $250MM crude oil prepaid forward sale involving Enron. In September 1999, the prepaid was increased to $337.5MM and its maturity was extended to December 1999.

- In November 1999, Citibank entered into a five-year, cash-settled $800MM crude oil prepaid forward sale involving Enron in connection with the Yosemite I transaction.

- In December 1999, Citibank entered into a 180-day, cash-settled $100MM crude oil prepaid forward sale involving Enron.

- In February 2000, Citibank entered into a seven-year, cash-settled £206MM crude oil prepaid forward sale involving Enron in connection with the Yosemite II transaction.

- In August 2000, Citibank entered into a five-year, cash-settled $475MM crude oil prepaid forward sale involving Enron in connection with the ECLN I transaction.

- In May 2001, Citibank entered into five-year, cash-settled crude oil prepaid forward sales of $475MM, £109.5MM and €170MM involving Enron in connection with the ECLN II, ECLN Sterling and ECLN Euro transactions.

- In June 2001, Citibank entered into a 180-day, cash-settled $250MM, gas prepaid forward sale involving Enron.

- In addition, Citibank and Enron engaged in foreign exchange, interest rate and commodity and credit swaps in the ordinary course of business during the relevant time period.

D. Investments

- **Sundance Industrial:** In June 2001, Citibank structured and made a $28MM equity investment and a $160MM contingent capital commitment to a partnership holding pulp and paper assets.

- **LJM2:** In October 1999, Enron approached Citibank to invest in LJM2 Co-Investment, L.P., a fund that would serve as a source of capital for various Enron investments. The decision whether to make this investment was made by Citigroup Investments (currently known as Citigroup Global Investments), the unit of Citigroup that exclusively manages Citigroup's proprietary investing. Citigroup Investments independently reviewed the investment opportunity and, in accordance with its normal investment processes, approved a $10MM investment on behalf of Citicorp and $5MM on behalf of Travelers Insurance.

- **Osprey & Marlin:** Citigroup Investments invested in two Section 144A offerings relating to Enron. Specifically, Travelers invested $129MM in 8.31% Senior Secured Notes issued by Osprey Trust in 1999. Travelers

also invested $15MM in Marlin Water Trust Certificates in 1998. These investments were approved by Citigroup Investments in accordance with its normal investment approval processes.

E. Other Dealings

- **Surety Bond:** Between 1998 and 2000, Travelers Casualty and Surety Company and the Travelers Indemnity Company (collectively, "Travelers"), entered into agreements with Enron subsidiaries to post surety bonds for, among other things, a series of deliveries of oil and gas that Enron was obligated to make pursuant to forward contracts. Currently, Travelers' obligation to pay pursuant to the surety bonds entered into with an entity called Mahonia Ltd. is the subject of litigation pending in federal court.

- **OPIC Notes:** In 1998, SSB and Merrill Lynch were co-placement agents on an Enron OPIC (Overseas Private Investment Corporation) Note offering of approximately $200MM of Certificates of Participation guaranteed by OPIC.

* * *

Specific information on fees, commissions, interest, profits and losses is not available on a transaction by transaction basis. However, in an effort to be responsive to the Subcommittee's request, we set forth a rough estimate of approximate net revenue to Citigroup in connection with its Enron-related activities for the years 1997 through 2001 as follows:

	1997	1998	1999	2000	2001
Net Revenues	$17.1MM	$18.2MM	$44.3MM	$50.2MM	$37.2MM

* * *

Much of the information set forth in this response is client sensitive or proprietary and maintained confidentially by Citigroup. Citigroup requests that the Committee treat its response confidentially. Please call me if you have any questions about any of the matters discussed above.

Sincerely yours,

Jane C. Sherburne
Deputy General Counsel

cc: Bob Roach, Chief Investigator
Kim Corthell, Staff Director to the Minority

ENRON
Enron Corp.
Project Yosemite
January 1999
ENRON
Slide 1
Confidential
Permanent Subcommittee on Investigations
EXHIBIT #186q
CITI-SPSI 0035868

The primary objective of the CLO is to free up bank liquidity

Objectives

- **Increase bank liquidity**
- Maintenance of existing balance sheet treatment of transactions
- Expand investor base beyond commercial banks / top tier institutional investors
- Warehousing capability
- Cost-efficient funding source
- Target size of facility $1 Billion
- Targeted financial close - March 1999

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CITI-SPSI 0035869

Challenges to be addressed include:

- Potential lack of credit diversity in the portfolio
- Varying maturities
- Governance - Top Tier Banks vs. Participant Banks
- Rating agency disclosure
- Credit spread gap – mtm if we take on exposure off b/s
- Substitution rights – wish to have ability to substitute transactions

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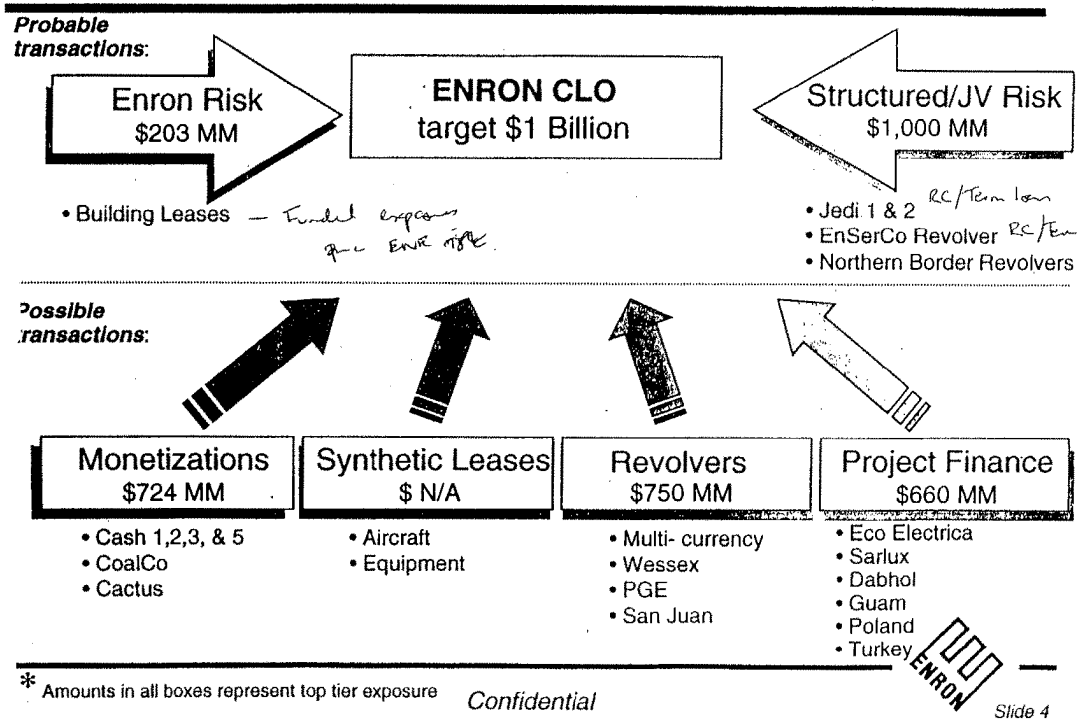
CITI-SPSI 0035870

The deals have been categorized as follows: *



* Amounts in all boxes represent top tier exposure

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Slide 4

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CITI-SPSI 0035871

1266

Deal attractiveness to Project Yosemite

FULL RECOURSE — **NON-RECOURSE**

Revolvers	Synthetic Leases	Synthetic Equity	Monetizations	JV's	Non-Recourse Project Finance
Multi- currency Wessex PGE San Juan	Building Leases Aircraft Equipment Software	Firefly Pilgrim	Cash 1,2,3 & 5 CoalCo Cactus	Jedi 1 & 2 EnSerCo Revolver Northern Border Revolvers	Eco Electrica Sarlux Dabhol Guam Poland Turkey
Top Tier Exposure					
$750 MM	**$203 MM**	**$590 MM**	**$724 MM**	**$1,000 MM**	**$660 MM**

Target $1 Billion ***of Top Tier Capacity***

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CITI-SPSI 0035872

Probable transactions to be included:

Transaction Description	Current Commitment	Top Tier Exposure	Maturity
Enron risk			
ENRON Building *Synthetic Lease, Enron credit, underlying building as collateral*	$ 284 MM	$ 179 MM	*4/2002*
Omaha Building *Synthetic Lease, Enron credit, underlying building as collateral*	$ 24 MM	$ 24 MM	*6/2002*
Structured / JV risk			
JEDI 1 *Revolver: 50/50 joint venture with CALPERS. Investment related to E&P sector*	$ 325 MM	$ 300 MM	*11/2003*
JEDI 2 *Revolver: 50/50 joint venture with CALPERS. Investment related to E&P sector*	$ 478 MM	$ 335 MM	*6/2001*
EnSerCo *Revolver: 50/50 joint venture with SCF Partners. Investments (debt & equity) in oilfield services sector*	$ 125 MM	$ 105 MM	*3/2000*
Northern Border Pipeline *Revolver*	$ 750 MM	$ 188 MM	*6/2002*
Northern Border Pipeline *Revolver*	$ 175 MM	$ 90 MM	*6/2002*

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CITI-SPSI 0035873

Synthetic equity transactions

Transaction Description	Current Commitment	Top Tier Exposure	Maturity
Pilgrim *Synthetic Equity*	$ 380 MM	$ 380 MM	*6/1999*
Firefly *Synthetic Equity*	$ 415 MM	$ 210 MM	*12/2000*

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Contract monetizations

Transaction Description	Current Commitment	Top Tier Exposure	Maturity
Cash 1	$ 52 MM	$ 36 MM	11/2018
Cash 2	$ 77 MM	$ 41 MM	12/2000
Cash 3	$ 84 MM	$ 39 MM	2/2000
Cash 5	$ 76 MM	$ 69 MM	7/2002
Coal Co	$150 MM	$150 MM	2/2013
Cactus	$ 33 MM	$ 22 MM	12/2002

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CITI-SPSI 0035875

Enron and related revolvers

Transaction Description	Current Commitment	Top Tier Exposure	Maturity
Multi Currency Revolver *Revolver*	$ 250 MM	$ 140 MM	*11/1999*
Wessex Water *Revolver*	$ 878 MM	$ 417 MM	*10/2003*
PGE Revolver *Revolver*	$ 200 MM	$ 100 MM	*7/2000*
San Juan *Revolver*	$ 9 MM	$ 9 MM	*4/2002*
Unfunded exposures			
$1 B Revolver *5 year revolver*	$1,000 MM	$ 440 MM	*11/2001*
$1 B Revolver *364 day facility*	$1,000 MM	$ 421 MM	*5/1999*

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Project finance transactions

Transaction Description	Current Commitment	Top Tier Exposure	Maturity
Eco Electrica *Puerto Rico power plant*	$ 770 MM	$ 377 MM	*9/2009*
Sarlux *Italian power plant*	$ 295 MM	$ 245 MM	*12/2011*
Dabhol *Indian power plant*	$ 150 MM	$ 96 MM	*1/2005*
Guam *Guam power plant*	$ 135 MM	$ 114 MM	*12/2014*
Poland *Poland power plant*	$ 119 MM	$ 56 MM	*12/2014*
Turkey *Turkey power plant*	$ 467 MM	$ 187 MM	*8/2008*

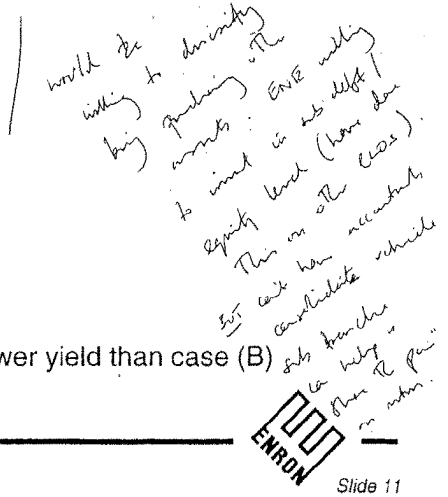
CITI-SPSI 003587

Three possible CLO structures are being considered:

(A) Enron related assets only
- No credit enhancement
- Sub debt and Equity tranches
- BBB+ rated senior tranche

(B) Enron related assets only
- Some form of credit enhancement
- Sub debt and Equity tranches
- A ~ AAA rated senior tranche

(C) Combination of Enron and third-party assets
- Some form of credit enhancement
- Sub debt and Equity tranches
- A ~ AAA rated senior tranche with lower yield than case (B)



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CITI-SPSI 0035878

Economic impact *(hypothetical example)*

	Loan	Spread Earnings	Regulatory Capital (8.25%)	Implied ROE
1 Year ago: *Spread LIBOR + 30 bps*	$100 MM	$300,000	$ 8.25 MM	3.6% + fees
Today: *Spread LIBOR + 50 bps*	$100 MM	$500,000	$ 8.25 MM	6% + fees
Incremental Earnings:		+ $200,000		

Existing Business
Market price for an existing loan with 5 year remaining life given current yields is below par if sold at market price.

New Business
Increased incremental earnings plus Fees

ECONOMIC IMPACT IS, AT WORST, NEUTRAL

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ENRON_EPSI 0035879

Timetable

Deadline	Responsible Party	Action
28 January	Enron	Delivery of transaction cashflows
8-10 February	Financial Institution	Delivery of proposals to Enron
14-15 February	Enron	Shortlist Proposal
22-26 February	Enron	Award Mandate
March '99	Enron / Arranger	Documentation / **Financial Close**

ENRON:	**Tel**	**Fax**	**Email**
Bill Brown	(713) 853 6398	(713) 646 4990	
Doug McDowell	(713) 853 7710	(713) 646 3422	dmcdowe@ect.enron.com
Jung Suh	(713) 853 7666	(713) 853 9252	jsuh@ect.enron.com
Craig Clark	(713) 345 7076	(713) 853 9252	cclark4@ect.enron.com

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CITI-SPSI 0035880

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Trustholders of Yosemite Securities Trust I

We have audited the accompanying balance sheet of Yosemite Securities Trust I ("Yosemite") as of December 31, 2000 and 1999, and the related statements of income, changes in trustholders' equity, and cash flows for the year ended December 31, 2000 and the period from inception (October 26, 1999) through December 31, 1999. These financial statements are the responsibility of Yosemite's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Yosemite at December 31, 2000 and 1999, and the results of its operations and its cash flows for the year ended December 31, 2000 and the period from inception (October 26, 1999) through December 31, 1999, in conformity with accounting principles generally accepted in the United States.

Houston, Texas
April 27, 2001

AASCGA(TX)002690

Permanent Subcommittee on Investigations
EXHIBIT #186r

F-1, 2

Yosemite Securities Trust I
Balance Sheet
(in thousands)

	December 31, 2000	December 31, 1999
ASSETS		
Current assets:		
Interest receivable from third party	$ 12,406	$ 6,532
Interest receivable from related party	-	1,821
Total current assets	12,406	8,353
Long-term assets:		
Notes receivable from third party	800,000	800,000
Notes receivable from related party	25,000	25,000
Deferred issuance cost on note payable	1,799	2,268
Total long-term assets	826,799	827,268
TOTAL ASSETS	$ 839,205	$ 835,621
LIABILITIES AND TRUSTHOLDERS' EQUITY		
Current liabilities:		
Accrued interest	$ 7,735	$ 7,391
Deferred interest income from related party	3,640	-
Total current liabilities	11,375	7,391
Long-term liabilities:		
Note payable	750,000	750,000
Total long-term liabilities	750,000	750,000
Total liabilities	$ 761,375	$ 757,391
TRUSTHOLDERS' EQUITY		
Trust certificates	75,000	75,000
Retained earnings	2,830	3,230
Total trustholders' equity	77,830	78,230
TOTAL LIABILITIES AND TRUSTHOLDERS' EQUITY	$ 839,205	$ 835,621

12/31/00 INT. Payable SO = 11,375

The accompanying notes are an integral part of these financial statements

F-2

Yosemite Securities Trust I
Statement of Income
(in thousands)

	For the year ended December 31, 2000	October 26, 1999 throug December 31, 1999
REVENUES		
Interest from third party	$ 58,415	$ 6,532
Interest from related party	11,882	1,821
TOTAL REVENUES	70,297	8,353
EXPENSES		
Interest expense to third party	(62,047)	(7,391)
Amortization of issuance cost of note payable	(469)	(78)
NET INCOME	$ 7,781	$ 884

Recap: Total Interest from 3rd Party

Interest on Note	58,000,000
+Interest on Temp. Inv.	415,015
Total	58,415,015

+ PLAN TO FOLLOW, INT. ON AMOUNT RELATED TO TEMP. INVESTMENTS ON EXCESS CASH. AA VOUCHED AMOUNTS TO BANK STATEMENTS TO WITH AN IMMATERIAL AMOUNT. AMOUNTS RECALCULATED, NO EXCEPTIONS NOTED.

The accompanying notes are an integral part of these financial statements.

F-6

Yosemite Securities Trust I
Statement of Changes in Trustholders' Equity
(in thousands)

	Trust Certificates	Retained Earnings	Total
Balance at October 26, 1999 (Date of Inception)	$ -	$ -	$ -
Issuance of trust certificates	75,000	-	75,000
Contribution of fees and services	-	2,346	2,346
Net loss	-	(884)	(884)
Balance at December 31, 1999	75,000	3,230	78,230
Net income	-	7,781	7,781
Dividends	-	(8,181)	(8,181)
Balance at December 31, 2000	$ 75,000	$ 2,830	$ 77,830

The accompanying notes are an integral part of these financial statements.

F-9

Yosemite Securities Trust I
Statement of Cash Flows
(in thousands)

	For the year ended December 31, 2000	October 26, 1999 thru December 31, 1999
CASH FLOWS FROM OPERATING ACTIVITIES		
Reconciliation of net income to net cash provided by operating activities:		
Net income (loss)	$ F-3 7,781 ✓	$ F-3 884 ✓
Changes in working capital:		
Increase in accrued interest receivable	(4,053)	F-1,2 (8,353) ✓
Increase in accrued interest payable	3,984	7,391
Amortization of issuance cost of note payable	D 469 ✓	D 78 ✓
Net cash provided by operating activities	8,181	0
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment in notes receivable - third party	-	F-1,2 (800,000) ✓
Investment in notes receivable - related party	-	(24,798)
Net cash provided by financing activities	-	(824,798)
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of note payable	-	749,798
issuance of trust certificates	-	F-1,2 75,000 ✓
Dividends paid to trustholders	B' (8,181) ✓	-
Net cash provided by financing activities	(8,181)	824,798
NET CHANGE IN CASH AND CASH EQUIVALENTS	-	-
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	-	-
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ -	$ -

RECAP INCREASE IN INT REC
12/31/00 BALANCE F-1,2 4,406 ✓
12/31/99 BALANCE 8,353
4,053 @

RECAP INCREASE IN INT PAYABLE
12/31/00 BALANCE F-1,2 11,695 ✓
12/31/99 BALANCE F-1,2 7,391 ✓
3,984 B

RECAP DISCOUNT ON NIP
PRINCIPAL AMOUNT @ 750,000,000
99.973
© 749,797,500

@ 750,000,000 - © 749,797,500 = 202,500
FN. 2 MM ✓

✓ TYING AMTS COVERING YOSEMITE TRUST I FINANCIAL HIGHLIGHTS. TIE MEMO WAS COMPILED PER REVIEW OF THE YOSEMITE CLOSING DOCUMENTS.

The accompanying notes are an integral part of these financial statements.

FN

YOSEMITE SECURITIES TRUST I
NOTES TO FINANCIAL STATEMENTS
December 31, 2000 and 1999

1. ORGANIZATION

Yosemite Securities Trust I ("Yosemite"), a Delaware Business Trust, was created October 26, 1999, primarily to issue 8.25percent Series 1999-A Linked Enron Obligations ("LEO's"). Yosemite's trust agreement requires it to invest the proceeds received from such issuance and the issuance of trust certificates in certain designated investments ("Trust Investments") as defined by the offering memorandum, including notes receivable. Yosemite has not conducted any operations, other than those activities incidental to its formation, including issuance of debt and equity securities and applying the proceeds to invest in trust investments. Yosemite was originally owned 50% by Long Lane Master Trust IV ("Long Lane") and 50% by Enron Corp. ("Enron"), an Oregon corporation. Subsequently, Enron sold 90% of its interest to SE Raptor, L.P. ("Raptor"), a related party.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

Yosemite invests in debt securities, which it accounts for in accordance with Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities". SFAS No. 115 is the authoritative pronouncement on accounting and reporting for investments in equity securities that have a readily determinable fair value and for all investments in debt securities. Except for debt securities classified as held-to-maturity securities, which are classified at amortized cost, SFAS No. 115 requires that investments in debt and equity securities be reported at fair value. SFAS No. 115 requires that the fair value of held-to-maturity securities be disclosed. Yosemite classifies its debt securities as held-to-maturity securities (See Notes 3 and 6).

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that effect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 requires companies to record derivatives on the balance sheet as assets or liabilities, measured at fair value. Gains or losses resulting from changes in the values of those derivatives will be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. The key criterion for hedge accounting is that the hedging relationship must be highly effective in achieving offsetting changes in fair value or cash flows. SFAS No. 133 is effective for all fiscal years beginning after June 15, 2000. Yosemite's management does not anticipate that the adoption of SFAS No. 133 will have a material impact on its financial position or the results of its operations.

AASCGA(TX)002695

Income Taxes

Yosemite does not pay federal or state income taxes. The taxable income or loss of Yosemite, which may vary substantially from income or loss reported for financial reporting purposes, is included in the federal and state tax returns of the individual partners. The tax return of Yosemite is subject to examination by federal and state taxing authorities. If examination of Yosemite results in changes to taxable income or loss, the taxable income of the partners will be changed accordingly.

RECAP ENRON SALE TO LONG LANE
SHARES SOLD TO LONG LANE 10,013
TOTAL ENRON SHARES ÷ 11,125
90.02%

TT/AW MEMO, COVERING YOSEMITE FINANCIAL HIGHLIGHTS. TREATMENT WAS COMPILED PER REVIEW OF THE YOSEMITE CLOSING DOCUMENTS.

YOSEMITE SECURITIES TRUST I
NOTES TO FINANCIAL STATEMENTS
December 31, 2000 and 1999

3. NOTE RECEIVABLE

On November 18, 1999, Yosemite invested in an $800 million Promissory Note ("Note") with Delta Energy Corporation ("Delta"), which terminates November 8, 2004. Principle is due upon termination. The Note is classified as a held-to-maturity security, in accordance with SFAS 115 with a balance of $800 million at December 31, 2000 and 1999. The fair values of this security were $835 million and $800 million as of December 31, 2000 and 1999, respectively. Interest on the Note accumulates interest at 7.25%. Interest is payable semi-annually on April 20 and October 20. Without the written consent of Yosemite, Delta does not have the right to prepay all or any portion of the principal amount owing under this Note. Interest income on this Note was approximately $58.0 million and $6.5 million for 2000 and 1999, respectively.

4. NOTE PAYABLE

On October 26, 1999, Yosemite issued 8.25% Series 1999-A Linked Enron Obligations ("LEO's") with a principal amount of $750 million, at a $0.2 million discount. The issuance is recorded as unamortized discount on the balance sheet and the balance is accreted to the face value over the term of the LEO's on a straight-line basis. The LEO's mature November 15, 2004. The LEO's have a balance of $750 million at December 31, 2000 and 1999. The fair values of this security were $806 million and $781 million as of December 31, 2000 and 1999, respectively. Payments of interest on the LEO's are made semi-annually in arrears on May 15 and November 15. The LEO's may be redeemed at the option of Yosemite, in whole or in part, upon not less than 30 days notice, at a redemption price equal to the sum of the accrued and unpaid interest to the date of redemption plus the greater of (i) 100% of the outstanding principal amount of the LEO's or (ii) the sum of the present values of the remaining scheduled payments of principal and interest thereon discounted to the redemption date on a semi-annual basis at a comparable U.S. Treasury issuance plus 50 point basis points. Interest expense was approximately $62 million and $7 million for 2000 and 1999, respectively.

5. EQUITY

Yosemite issued trust certificates in the amount of $75 million, which represents all of the ownership interest of Yosemite ("Trust Certificates"). Yield on the Trust Certificates will accumulate at 11.0% per annum. The dividends are payable semi-annually in arrears on each May 15 and November 15, beginning May 15, 2000. Dividends paid in 2000 were $8.2 million. There were no dividends paid in 1999.

6. RELATED PARTY TRANSACTIONS

On November 18,1999, Yosemite invested in a $25 million debt security with Enron ("Enron Note"), at a $0.2 million discount to its face value. Enron will pay interest to Yosemite equal to the amount by which the aggregate Citibank Fixed Payments exceed the aggregate scheduled interest receipts from the Delta Note semi-annually, on April 20 and October 20 until maturity. The Enron Note terminates November 8, 2004 and total interest over the five-year period equates approximately to a 8% effective rate of return. Interest income on this note was approximately $11.9 million and $1.8 million for 2000 and 1999, respectively. The Enron Note is classified as a held-to-maturity security, which had a fair value of $62 million and $68 million as of December 31, 2000 and 1999, respectively.

During 1999, Enron paid all costs incurred related to the issuance of the LEO's and Trust Certificates, which amounted to approximately $2.3 million.

AASCGA(TX)002696

TRIAL MEMO T, COVERING YOSEMITE FINANCIAL HIGHLIGHTS, THE MEMO WAS COMPILED FROM REVIEW OF THE YOSEMITE CLOSING DOCUMENTS.

3/

YOSEMITE SECURITIES TRUST I
NOTES TO FINANCIAL STATEMENTS
December 31, 2000 and 1999

Enron provides various accounting and other administrative services to the Trust. The fair value of these services are not material and are not reflected in these financial statements.

7. OTHER FINANCIAL INSTRUMENTS

On November 18, 1999, the Trust entered into two swap agreements with Citibank related to the Note and the Enron Note (collectively, the Investments). Pursuant to the swap agreements, the Trust is obligated to pay Citibank the actual interest it collects related to the Investments. In return, Citibank is obligated to pay the Trust the aggregate amount owed by the Trust related to the LEO's and the Trust Certificates. In addition, in the case of an Enron Credit Event, the swap agreements provided for the Trust to provide Citibank with its Investments in return for Citibank providing the Trust with Enron Obligations.

FV OF SWAP 11/18/99 12/31/00
DELTA F 12,685,857 F 10,710,857
ENRON ↓ 396,433 ↓ 334,714

8. CONCENTRATION OF CREDIT RISK

A significant portion of Yosemite's assets is held in instruments with realization directly or indirectly affected by the creditworthiness of Enron, Delta and Citibank. Yosemite's management does not believe this concentration of assets and credit risk will have a material risk of loss with respect to its financial position or results of operations.

9. COMPREHENSIVE INCOME

Yosemite adopted SFAS No. 130, "Reporting Comprehensive Income," effective January 1, 1998. This statement establishes standards for the reporting and display of comprehensive income (net income plus all other changes in net assets from non-owner sources) and its components in consolidated financial statements. For the years ended December 31, 2000 and 1999 comprehensive income equaled net income

✓ TTLAW MEMO, COVERING YOSEMITE FINANCIAL HIGHLIGHTS-THEMEMO.
WAS COMPILED PER REVIEW OF THE YOSEMITE CLOSING DOCUMENTS.

FN

YOSEMITE SECURITIES TRUST LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2000

1. ORGANIZATION

Yosemite Securities Trust Ltd. ("Yosemite"), a Jersey, Channel Islands limited liability company, was created February 23, 2000 to issue 8.75 percent Series 2000-A Linked Enron Obligations ("LEO's"). Yosemite's trust agreement requires it to invest the proceeds received from such issuance and the issuance of trust certificates in certain designated investments ("Trust Investments") as defined by the offering memorandum, including notes receivable. Yosemite was originally owned 50% by Long Lane Master Trust IV ("Long Lane") and 50% by Enron Corp. ("Enron"), an Oregon corporation. Enron sold 90% of its interest to Long Lane in December 2000. Long Lane subsequently sold the interest it purchased from Enron to SE Raptor, L.P. ("Raptor"), an Enron related party..

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

Yosemite invests in debt securities which it accounts for, in accordance with *Statement of Financial Accounting Standards* (SFAS) No. 115. SFAS No. 115 is the authoritative pronouncement on accounting and reporting for investments in equity securities that have a readily determinable fair value and for all investments in debt securities. Except for debt securities classified as held-to-maturity securities which are classified at amortized cost, SFAS No. 115 requires that investments in debt and equity securities be reported at fair value. SFAS No. 115 requires that the fair value of held-to-maturity securities be disclosed. Yosemite classifies its debt securities as held-to-maturity securities (See Note 3).

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 requires companies to record derivatives on the balance sheet as assets or liabilities, measured at fair value. Gains or losses resulting from changes in the values of those derivatives will be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. The key criterion for hedge accounting is that the hedging relationship must be highly effective in achieving offsetting changes in fair value or cash flows. SFAS No. 133 is effective for all fiscal years beginning after June 15, 2000. Yosemite's management does not anticipate that the adoption of SFAS No. 133 will have a material impact on its financial position or the results of its operations.

Income Taxes

Yosemite does not pay federal or state income taxes. The taxable income or loss of Yosemite, which may vary substantially from income or loss reported for financial reporting purposes, is included in the federal and state tax returns of the individual partners. The tax return of Yosemite is subject to examination by federal and state taxing authorities. If examination of Yosemite results in changes to taxable income or loss, the taxable income of the partners will be changed accordingly.

+ TTAN CERTIFICATE PURCHASE & SALE AGREEMENT EFFECTIVE AS OF 12/20/00.
TTAN MEMO COVERING ASSIGNED TRUST II FINANCIAL HIGHLIGHTS. THE MEMO WAS COMPILED FROM REVIEW OF THE YOSEMITE CLOSING DOCUMENTS

DELAP ENRON SALE TO LONG LANE
SHARES SOLD TO LONG LANE 10,01
TOTAL ENRON SHARES 11,12
90%

Permanent Subcommittee on Investigations
EXHIBIT #186s

FN 3

YOSEMITE SECURITIES TRUST LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2000

Commitments and Contingencies

Yosemite is not currently involved in any disputes.

3. NOTE RECEIVABLE

On February 23, 2000, Yosemite invested in a £207 million promissory note ("Note") with Delta Energy Corporation ("Delta"), ~~at a £0.2 million discount~~. The Note matures February 23, 2007 and earns a 7.5 percent annual interest rate. Interest is payable annually on January 23. Interest income on this Note was approximately £13 million for 2000. Without the written consent of Yosemite, Delta does not have the right to prepay all or any portion of the principal amount owing under this Note. The fair value of the Note was £228 million as of December 31, 2000.

4. NOTE PAYABLE

On February 23, 2000, Yosemite issued 8.75% Series 2000-A Linked Enron Obligations ("LEO's") in the principal amount of £200 million. The LEO's mature February 23, 2007. The Note is classified as a held-to-maturity security, in accordance with SFAS 115 with a balance of £200 million at December 31, 2000. The fair value of this security was £220 million as of December 31, 2000, respectively. Payments of interest on the LEO's are made annually in arrears on February 23. The LEO's may be redeemed at the option of Yosemite, after receiving a notice of early termination from Citibank under the Citibank Swap, in whole or in part, at a redemption price equal to the sum of the accrued and unpaid interest to the date of redemption plus the greater of (i) par and accrued interest of the LEO's and (ii) the price on the third dealing day prior to the date of publication of the notice of redemption or alternate price as determined by a third party. Interest expense was approximately £15 million for 2000.

Yosemite issued the LEO's at a £238 thousand discount to its face value. The issuance is recorded as unamortized discount on the balance sheet and the balance is accreted to the face value over the term of the LEO's on a straight-line basis.

The LEO's have not been and will not be registered under the United States Securities Act of 1933, as amended (the "Securities Act"), or any state securities laws and are being offered and sold in the United States only to "Qualified Institutional Buyers" (as defined under Rule 144A under the Securities Act) (each, a "QIB") and outside the United States in accordance with Regulation S under the Securities Act. The LEO's are being offered and sold outside the United States in accordance with Regulation S under the Securities Act and may not be offered or sold in the United States or to U.S. persons (as defined in Regulation S under the Securities Act) except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. The notes are not being offered or sold to persons in the United Kingdom except in circumstances which do not constitute an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995 (as amended).

5. EQUITY

Yosemite issued trust certificates in the amount of approximately £22 million, which represents all of the ownership interest of Yosemite ("Trust Certificates"). Yield on the Trust Certificates will accumulate at 12.0% per annum. The dividends are payable annually in arrears on each February 23, beginning February 23, 2001. Dividends accrued in 2000 were approximately £2.3 million.

P - TT/AW MEMO, COVERING YOSEMITE TRUST II FINANCIAL HIGHLIGHTS. THIS MEMO WAS COMPILED FOR REVIEW OF THE YOSEMITE CLOSING DOCUMENTS.

FN 37

YOSEMITE SECURITIES TRUST LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2000

6. RELATED PARTY TRANSACTION

On February 23, 2000, Yosemite invested in a £15.5 million Enron debt security ("Enron Note") with Enron, at a £0.2 million discount. The Enron Note matures February 23, 2007 and pays interest to Yosemite, on January 23 of each year during this period, at an amount equal to the amount by which the aggregate Citibank Fixed Payments exceed the aggregate scheduled interest receipts. This equates to approximately 7.00% effective rate. Interest income on the Enron Note was approximately $14 million for 2000. The fair value of this security was $37 million as of December 31, 2000.

During 2000, Enron paid all costs incurred related to the issuance of the LEO's and Trust Certificates, which amounted to approximately $2 million. These costs have been accounted for by Yosemite as contributions from trustholders and capitalized as deferred issuance cost on note payable, to be amortized over the life of the securities.

Enron also provides various accounting and other administrative services to the Trust. The fair value of these services are not material and are not reflected in these financial statements.

7. SUMMARIES OF SIGNIFICANT AGREEMENTS

Effective February 23, 2000, Yosemite entered into a swap agreement with Citibank, N.A., that provides for Citibank to pay to Yosemite the sum of the periodic payments consisting of the interest on the Notes plus the yield payment on the Certificates. Yosemite will pay to Citibank the Trust's fixed payment consisting of all periodic payments for interest, periodic fees and any other periodic amounts, other than principle receipts.

8. CONCENTRATION OF CREDIT RISK

The Trust's primary asset consists of a note receivable from Delta. As a result, the collectibility of the Trust's note is highly dependent on the credit worthiness of Delta. The Trust's management does not believe this will have a material impact on its financial position or the results of its operations.

9. COMPREHENSIVE INCOME

The Trust adopted SFAS No. 130, "Reporting Comprehensive Income," effective January 1, 1998. This statement establishes standards for the reporting and display of comprehensive income (net income plus all other changes in net assets from non-owner sources) and its components in consolidated financial statements. For the year ended December 31, 2000 comprehensive income equaled net income.

TYLAW MEMO 1, COVERING YOSEMITE TRUST II FINANCIAL HIGHLIGHTS. THE MEMO WAS COMPILED DUE REVIEW OF THE YOSEMITE CLOSING DOCUMENTS

ARTHUR ANDERSEN LLP

To: The Files, Houston

From: David B. Duncan, Houston

Date: August 18, 2000

Subject: $500,000,000 8% Enron Credit Linked Notes due 2005 Authorization to Sign

This hereby authorizes Kimberly R. Scardino to sign the Firm's name to the comfort letter dated August 17, 2000 issued on behalf of Enron Corp. in connection with the offering and sale of $500,000,000 8% Enron Credit Linked Notes due 2005 by Enron Credit Linked Notes Trust.

AASCGA(TX)001716

Permanent Subcommittee on Investigations
EXHIBIT #186t

Enron Corp.
P.O. Box 1188
Houston, TX 77251-1188
(713) 853-6161

August 25, 2000

Arthur Andersen LLP
711 Louisiana, Suite 1300
Houston, TX 77002

Gentlemen:

The following representations, made to the best of our knowledge and belief, apply to Enron Corp. and consolidated subsidiaries ("Enron") and are submitted in connection with your "comfort" letter to be issued in connection with the Offering Memorandum dated August 17, 2000 covering the issue and sale of $500,000,000, 8% Enron Credit Linked Notes due 2005 by Enron Credit Linked Notes Trust.

The unaudited consolidated condensed balance sheet as of June 30, 2000 included in the June 30, 2000 Form 10-Q, and the unaudited consolidated condensed statements of income for the three-month and six-month periods ended June 30, 2000 and 1999, as prepared by Enron in conformity with accounting principles generally accepted in the United States and supplied to you, are stated on a basis substantially consistent with that of the audited consolidated financial statements incorporated by reference in the Offering Memorandum and are the latest available financial statements.

For the period from July 1, 2000 to August 22, 2000, there were no decreases, as compared to the corresponding period in the preceding year, in consolidated operating revenues, net income or basic or diluted earnings per share of common stock, except in all instances for changes, increases or decreases that the Offering Memorandum discloses have occurred or may occur.

At August 22, 2000, there was no change in capital stock, increase in combined short-term debt and long-term debt or decrease in consolidated net assets or shareholders' equity of Enron as compared with amounts shown in the June 30, 2000 unaudited consolidated condensed balance sheet included in Enron's June 30, 2000 Form 10-Q, incorporated by reference in the Offering Memorandum, except in all instances for changes, increases or decreases that the Offering Memorandum discloses have occurred or may occur, except for a $167 million increase in capital stock and a $631 million increase in combined short-term and long-term debt.

Permanent Subcommittee on Investigations
EXHIBIT #186u

In connection with the preparation of this letter, we have reviewed our representations made to you in our letters dated March 13, 2000 and August 17, 2000. Except for changes disclosed in the Offering Memorandum and in reports filed by Enron with the Securities and Exchange Commission, in all respects, the representations made at that date are correct and remain applicable as of the date of this letter.

Very truly yours,

Jeffrey K. Skilling
President and Chief Operating Officer

Richard A. Causey
Executive Vice President and Chief Accounting Officer

dwg

Author: Bill Macomber at GB-NEWYORK-45
Date: 8/27/96 9:51 AM
Priority: Normal
TO: Henry Cheever at GB-NEWYORK-04
TO: Richard J Poworoznek at CCMAIL_HUBPO
TO: John Cotter at CCMAIL_HUBPO
CC: Jeffrey Satenstein@Chase at CCMAIL_HUBPO
CC: Edwin Jenkins
TO: Maggie Serravalli at GB-NEWYORK-13
TO: Martin Mussman
TO: Peter Biesszard at GB-NEWYORK-05
TO: PatrickT O'Brien at GB-NEWYORK-43
TO: John Costello at GB-NEWYORK-05
Subject: Prepaid Forwards -- Loans Vs Derivatives
---------- Forwarded w/Changes ----------
Author: Diane Butterfield at ccmail_hubpo 8/23/96 5:55 PM
TO: Bill Macomber at GB-NEWYORK-45
CC: Edwin Jenkins at GB-NEWYORK-45
CC: Ana Barrio Lopez @ CBC_NOTES at ccmail_hubpo
CC: Jody A. Blumenfeld @ CBC_NOTES at ccmail_hubpo
CC: Jeffrey Satenstein @ CHASE at ccmail_hubpo
Subject: Prepaid Forwards -- Loans Vs Derivatives
---------- Message Contents ----------

John,

Please arrange to report the prepaid forwards as loans effective as of August 31, 1996. Also, please coordinate the reporting of these balances as loans in GES. Thank.,

Bill

---------- Forward Header ----------
Subject: Prepaid Forwards -- Loans Vs Derivatives
Author: Diane Butterfield at ccmail_hubpo
Date: 8/23/96 5:55 PM

At our meeting with Joe and Mark on Monday, 8/19, it was decided that some interim guidance should be issued to Controllers relative indicators that they should look for in determining whether transactions should be recorded as loans or derivatives. Joe wanted to have this guidance go out as soon as possible so that people could focus on this issue. In addition to the list of indicators to be included in the guidance, the guidance should include examples of what we have seen to date and the reason we believe it is either a loan or a derivative. Another item to be included is that these items are not to be booked in Other Assets.

In our phone conversation subsequent to the meeting, you agreed to do an initial draft by 8/30 when you leave on vacation. You agreed to pass the initial draft onto us so that we can make changes to it while you are on vacation and then issue it upon your return.

Regards,
Diane
DisplaySSWType: All other attachments - No conversion needed
SSWType: PCDATA

Permanent Subcommittee on Investigations
EXHIBIT #187a

Author: Bill Macomber at GB-NEWYORK-45
Date: 8/28/96 12:14 PM
Priority: Normal
TO: Diane Butterfield at CCMAIL_HUBPO
TO: Ana Barrio Lopez at CCMAIL_HUBPO
TO: Jeffrey Satenstein@Chase at CCMAIL_HUBPO
TO: John Cotter at CCMAIL_HUBPO
TO: Edwin Jenkins
CC: Mark Staines at GB-NEWYORK-20
CC: PatrickT O'Brien at GB-NEWYORK-43
Subject: Loans/Deposits Documented as Derivatives
---------- Message Contents ----------

Please review the attached draft of an interim accounting policy guidance on Loans/Borrowings Documented as Derivatives. I want to discuss this draft with you before I leave for a long vacation. Can we meet Thursday afternoon or Friday morning?

Bill

Derivatives are not only the most complex instruments that controllers monitor, they are also the most variable in economic substance. While the ability to tailor the terms of a derivative transactions to satisfy a customer's request can enhance the Bank's revenues, sometimes a proposed derivative transaction causes significant accounting issues as well as "suitability" issues. In this context, Global Bank and Corporate Controllers recently became aware that timing of cash flows has occasionally been crafted in a way that a transaction is economically equivalent to lending by the Bank. Those transactions are in the process of being reclassified to loans. Upon reviewing a few other transactions, the outstanding balances are being reclassified as borrowings because that is their economic substance.

This memo provides you with interim accounting policy guidance to be applied to new transactions. Until we have an adequate sample of the transactions that are possibly at issue, the guidelines can only be fairly general and provide a few examples. You must exercise cautionary judgment whenever you apply this guidance. If you have doubt or concerns regarding the financial reporting for a transaction, you must consult with Global Bank Controller's Financial Advisory unit and your senior Business Unit Controller who will coordinate a response with Corporate Accounting Policy. Concerns regarding a possible "suitability" issue should be referred to the Legal Department (which is in the process of issuing guidelines???) and your senior Business Unit Controller.

INTERIM ACCOUNTING POLICY GUIDANCE

A transaction that is economically equivalent primarily to a loan should be reported as a loan, and one that is economically equivalent primarily to a borrowing should be reported as a borrowing. The principle factor determining whether a transaction is a loan (or a deposit) is a "time lag" between cash flows, excluding those that are inherently a market practice (such as semiannual or quarterly floating rate payment on an interest rate swap against an annual fixed rate payment.) Additional factors indicative of a lending transaction are (a) absence of market risk to the Bank, although interest rate sensitivity to the Bank's NII is incurred; (b) a strike price for a purchased option that makes it almost inevitable that the option will be exercised and produces a large premium payment by the Bank; or (c) an interest rate swap that has a very far off market rate and produces a large upfront payment by the Bank.

EXAMPLES OF LOANS DOCUMENTED AS DERIVATIVES

Transaction One, which is documented as a prepaid commodity swap with no market risk: A clear example of a loan that could be documented as a derivative is a transactions that requires the Bank to make a $10 million cash payment today and requires the customer to deliver in 30 days a quantity of a commodity to be determined based on the commodity price at the delivery date. When the quantity is determined, the related market value of the commodity to be delivered will be equal to a $10 million loan plus interest for 30 days. (Need to address whether the Bank has a commitment to purchase the commodity at a future date which should be included in schedule RCL of the Call Report.

Transaction Two, which is documented as a prepaid commodity swap with market risk: Even if Transaction One is modified so that at the inception of the transaction a known quantity of the commodity is to be delivered, the transaction is primarily a loan due to the time lag between the Bank's payment and the subsequent receipt of the commodity. (Need to address reporting the impact of market risk on SOC, I&E and RAC/Call Report.)

Transaction Three, which is documented as an off current market rate FX option having market risk: If the Bank purchases an FX option to buy Sterling 10 million for US Dollars 10 million, exercise of the option would be almost inevitable. Because the option is deep in the money (strike price of 1 Pound to 1 USD compared to a market price of say 1 Pound to USD 1.54), the Bank would be required to make a

large upfront payment. Although this transaction has market risk, it is primarily a loan. (Need to address reporting the impact of market risk on SOC, I&E and RAC/ Call Report.)

Transaction Four, which is documented as an interest rate swap having no market risk: The cash flows of a swap can be structured to be a set of fixed cash inflows and outflows occurring at different dates. This transaction is similar to Transaction One because it has no market risk, albeit having funding/reinvestment risk that would impact NII. The "notional" amounts of this transaction, if any, should not be included in any Risk Adjusted Capital or Call Report disclosure.

Transaction Five, which is documented as an interest rate swap having market risk: If under a USD interest rate swap the Bank is to receive a fixed rate of say 1000 basis points over current market, a related upfront payment by the Bank is primarily a loan. (Need to address the impact of market risk on SOC, I&E and RAC/Call Report

OFF CURRENT MARKET RATE DERIVATIVES TO BE REPORTED AS TRADING

An off current market rate derivative should be reported as a trading position when the customer's purpose is to exactly offset an existing risk position and the cash paid or received by the Bank is not significant to the transaction. To ensure that cautionary judgment is applied to the reporting of such transactions, you need to refer to Global Bank Controller's Advisory unit and your senior Business Unit Controller each such transaction that results in a cash flow exceeding $5 million having a "time lag" as the term is used under the Interim Accounting policy Guidance above.

For this purpose, the absolute sum of cash flow for (a) any series of similar transactions and/or (b) payments or receipts from one transaction. For an off current market rate option, the cash flow is limited to the amount of the premium attributable to a strike price over or under the current market rate.

Author: Ana Barrio Lopez at ccmail_hubpo
Date: 9/26/96 9:21 AM
Priority: Normal
TO: PatrickT O'Brien at GB-NEWYORK-43
Subject: Loans/Borrowings Documented as Derivatives
---------- Message Contents ----------

As requested.

To: Ana Barrio Lopez, Jody A. Blumenfeld, Fai-Hong B. Chiu
cc:
From: Diane Butterfield
Date: 09/20/96 09:22:01 AM
Subject: Loans/Borrowings Documented as Derivatives

To: Jack Alexander, Janet Caruso @ Chase, John Cotter, Miriam Haimes @ Chase, Edwin Jenkins, Douglas Kurowski, Bill Macomber, Alan Magleby, Timothy Plesko @ Chase, Jeffrey Satenstein @ Chase
cc: Marjorie H Gross, Joseph Sclafani, Mark Staines
From: Diane Butterfield
Date: 09/20/96 09:10:43 AM
Subject: Loans/Borrowings Documented as Derivatives

Attached is a memorandum that addresses the issue of certain loans/borrowings documented and accounted for as derivatives. The guidance contained herein must be followed until further notice from Global Bank and Corporate Controllers.

Regards,
Diane
(See attached file: LOANS.DOC)

Permanent Subcommittee on Investigations
EXHIBIT #187b

CHASE

Memorandum

To: Distribution

Date: September 26, 1996

From: Diane M. Butterfield
Corporate Accounting Policies, 30/GCT

Telephone: 622-9256

Subject: **Loans/Borrowings Documented as Derivatives**

While the ability to tailor the terms of derivative transactions to satisfy a customer's request can enhance the Bank's revenues, sometimes a proposed derivative transaction causes significant accounting issues as well as potential issues under the Appropriateness Policy. In this context, Global Bank and Corporate Controllers recently became aware of certain transactions in which the timing of cash flows had been crafted in a way that the transactions were economically equivalent to lending by the Bank. Those transactions are in the process of being reclassified to loans.

The purpose of this memorandum is to alert you to this issue. Global Bank and Corporate Controllers are in the process of determining how these types of transactions should be accounted for and reported going forward, including off-balance sheet reporting. This memo presents the preliminary position on when a transaction is a loan/borrowing versus a derivative, yet there are accounting/reporting/operational issues that need to be addressed in order to establish a formal Corporate Accounting Policy such as:

- Should the transaction be marked to market and if so, what income statement caption is the mark-to-market reported on?
- If a derivative is reported as a loan, should the commitment to purchase/sell in the future be reported as an off-balance sheet commitment on schedule RC-L of the Call Report? What regulatory loan disclosure must be made?
- If the transaction is booked on a derivatives system, how do we track the deals that must be reclassified to loans/borrowings?
- If the transaction is booked on a derivatives system, how do we compute and record interest on the loan/borrowing?
- If the transaction is recorded as a loan/borrowing, what are the implications for the tax return?

- If the transaction is in substance a loan/borrowing and there is a netting agreement with the customer, would the transactions qualify for netting under FIN 39?

These transactions will also be discussed with Market Risk Management and Credit to ensure they are properly reported for market and credit risk monitoring purposes. Additionally, Legal will be consulted regarding the Appropriateness Policy.

If you have doubt or concerns regarding the financial reporting for a transaction, you must consult with Global Bank Controller's Financial Advisory unit and your senior Business Unit Controller who jointly will coordinate a response with Corporate Accounting Policy. Until the open issues are addressed, new transactions less than $5 million may continue to be accounted for as derivatives. New transactions that result in a cash flow of $5 million or more having one or more of the characteristics illustrated below must be referred to Global Bank Controller's Advisory unit (Bill Macomber) and your senior Business Unit Controller. Please copy Corporate Accounting Policies (Diane Butterfield and Ana Barrio Lopez). Concerns regarding a possible Appropriateness Policy issue should be referred to Marjorie Gross in the Legal Department, and you should advise your senior Business Unit Controller.

For purposes of the $5 million threshold, the cash flow should be an aggregate sum for any series of similar transactions (i.e., six similar transactions of $1 million each, must be viewed as one $6 million transaction). Additionally the cash flows must be aggregated for transactions where the cash payments are made over time, such as "Transaction Four" below.

CHARACTERISTICS OF LOANS/BORROWINGS VS DERIVATIVES

A transaction that is a derivative in form but economically equivalent primarily to a loan should be reported as a loan, and one that is economically equivalent primarily to a borrowing should be reported as a borrowing. The principal factor determining whether a transaction is a loan (or a borrowing) is a "time lag" between cash flows, excluding those that are inherently a market practice (such as semiannual or quarterly floating rate payment on an interest rate swap against an annual fixed rate payment). Additional factors indicative of a lending transaction are (a) an absence of any market risk to the Bank, although interest rate sensitivity to the Bank's NII may be incurred; (b) an off-market strike price for a purchased option that makes it almost inevitable that the option will be exercised and results in a large premium payment by the Bank; or (c) an interest rate swap that has a rate that is significantly off-market and results in a large upfront payment by the Bank. Off-market rate derivatives that do not have the above characteristics should be reported as trading positions.

EXAMPLES OF LOANS DOCUMENTED AS DERIVATIVES

Transaction One: Documented as a prepaid commodity swap with no market risk. A clear example of a transaction that is the economic equivalent of a loan is a derivative transaction that requires the Bank to make a $10 million cash payment today and requires the customer to deliver in 30 days a quantity of a commodity to be determined based on the commodity price at the delivery date. When the quantity is determined, the related market value of the commodity to be delivered will be equal to a $10 million loan plus interest for 30 days.

Transaction Two: Documented as a prepaid commodity swap with market risk. Even if Transaction One is modified so that at the inception of the transaction a known quantity of the commodity is to be delivered, the transaction is primarily a loan due to the time lag between the Bank's payment and the subsequent receipt of the commodity.

Transaction Three: Documented as an off-market rate FX option with market risk. If the Bank purchases an FX option to buy Sterling 10 million for US Dollars 10 million, exercise of the option would be almost inevitable. Since the option is deep in the money (strike price of 1 Pound to 1 USD compared to a market price of say 1 Pound to USD 1.54), the Bank would be required to make a large upfront payment. The amount of the upfront payment in excess of a normal market rate is in essence a loan. Although this transaction has market risk, it is primarily a loan.

Transaction Four: Documented as an interest rate swap with no market risk. The cash flows of a swap can be structured to be a set of fixed cash inflows and outflows occurring at different dates. For example, in the earlier years the Bank makes above-market fixed rate payments and the swap counterparty makes below-market fixed rate payments which is equivalent to the Bank lending funds. In later years of the transaction, the Bank makes below-market fixed rate payments and the swap counterparty makes above-market fixed rate payments which is equivalent to the counterparty repaying the loan.

Transaction Five: Documented as an off-market interest rate swap with market risk. If the Bank enters into an interest rate swap in which it makes an upfront payment and receives a fixed rate of say 1000 basis points over a current market rate, the upfront payment made by the Bank is primarily a loan.

As indicated above, if you have any questions please contact Bill Macomber in Global Bank Controllers and notify your Business Unit Controller. We will notify you once the open issues addressed in this memorandum are resolved. In the interim please follow the guidance herein. In this connection, we also request that you forward a copy of this memo to other interested personnel throughout your respective areas.

Distribution:

Jack Alexander, 10 TCB-N57
Janet Caruso, 14/1CMP
John Cotter, 7/270
Miriam Haimes, 16/1CMP
Edwin Jenkins, 23/GCT
Douglas Kurowski, 4/London St.
William Macomber, 24/GCT
Alan Magleby, Shatin, Hong Kong
Timothy Plesko, London WH
Jeffrey Satenstein, 23/GCT

cc:

Marjorie Gross, 40/270
Joseph Sclafani, 28/270
Mark Staines, 16/270

E-Mail to be documented as Derivative for your review. Sharon

To: John Cotter, Bill Macomber/CHASE
cc: Diane Butterfield/CHASE, Patrick O'Brien/CHASE, Fai-Hong B. Chiu, Irene Morfit/CHASE, Bruce Ellard/CHASE
From: Sharon Fiolek/CHASE
Date: 10/03/97 04:23:14 PM
Subject: Loans/Borrowings Documented as Derivatives

John and Bill,

We are planning on sending the attached E-Mail to the business unit controllers documenting the conclusion reached at our meeting on loans/borrowings documented as derivatives. Please review and forward any comments you may have to me by Friday, October 17th .

As discussed at our meeting, there is one open issue related to the internal capital allocation, which John had agreed to further consider and address accordingly.

Regards,
Sharon

To: Jack Alexander, Janet Caruso, John Cotter, Doug Kurowski, Alan F. Magleby, Aditya Mohan, Russell Neumann, Robert T. O'Neill, Timothy Plesko/CHASE, Jim Ruppert
cc: Fai-Hong B. Chiu, Bruce Ellard/CHASE, Sharon Fiolek/CHASE, Marjorie E. Gross, Edwin M. Jenkins, Bill Macomber/CHASE, Irene Morfit/CHASE, Patrick O'Brien/CHASE, Jeffrey Satenstein, Joseph Sclafani, Mark Staines
From: Diane Butterfield/CHASE
Date: 10/03/97 03:47:44 PM
Subject: Loans/Borrowings Documented as Derivatives

A memorandum was distributed on September 20, 1996 addressing the issue of certain loans/borrowings documented and accounted for as derivatives. The memo set forth interim guidance under which loans/borrowings documented as derivatives were to be reported as loans/borrowings.

Corporate Accounting Policies recently met with John Cotter, Bruce Ellard and Bill Macomber to revisit this issue. Based on our discussions, it was concluded that the form of the loan/borrowing dictates the accounting. Accordingly, if the loan/borrowing is documented and confirmed with the counterparty as a derivative, the loan/borrowing should be reported in Trading Assets/Liabilities - Risk Management Instruments and marked to market. To the extent that there are any variations or any issues related to appropriateness, the business units are advised to contact Marjorie Gross in the Legal Department. This conclusion supercedes the interim guidance set forth in the above mentioned memorandum.

For risk-based capital purposes, loans documented as derivatives will continue to be risk weighted as loans. In order to properly reflect this in the risk-based capital calculation, the business units should continue to manually adjust the risk weighting applied to the derivative as if it were a loan.

Regards,
Diane

Permanent Subcommittee on Investigations
EXHIBIT #187c

To: Jonathan Porter
cc: John Cotter, Jeffrey Satenstein/CHASE, Patrick O'Brien/CHASE, Diane Butterfield/CHASE, Bill Macomber/CHASE, Zandra Sherrington/CHASE, Michaell. Gordon/CHASE, Doug Kurowski/CHASE
From: Edwin M. Jenkins/CHASE
Date: 10/22/97 09:43:12 AM
Subject: Re: Sampoerna Deal

I spoke to Pat last night, and I understand that Joe Sciafani has approved MTM accounting. I understand the form of the transaction, rather than its economic substance, will govern in this case. An accounting memo is to be issued by Pat(?), which will provide additional guidance on these types of transactions. I do not know anymore at this time.

I hope this will suffice for now.

Diane: Do you have an idea when the accounting memo will be issued?

---------- *Previous Memo History* ----------

To: CN=Edwin M. Jenkins/O=CHASE
cc:
From: Jonathan Porter
Date: 10/21/97 09:47:06 PM

Edwin how did this end up? Is mtm accounting confirmed? Thanks, Jonathan
To: Edwin M. Jenkins/Chase @ Chase
cc: See Below
From: Andrew Best/CHASE
Date: Wednesday October 15, 1997 10:42 AM
Subject: Re: Sampoerna Deal

As you can see Jonathan passed me your memo.

The transaction was documented as a swap, as that is how it was hedged. There is no avoidance of wht. There is a prospect that the counterparty may be able to claim the coupon expenses under the deal with 2 way final exchange as hedging expenses which may be tax deductible.

From the counterparty's point of view there is 3 purposes for the transaction.

1. Forced USD savings by company to cover future repayment of USD loans.
2. Possible future use of sinking fund to collateralise loans from Chase and therefore reduce margin.
3. Semi-annual USD payment of 1.62 mio under Transaction 1 may be considered as hedging expense and possibly tax deductible.

It was therefore considered appropriate from the customer's point of view.

In response to your earlier e-mail please find below my reply

First of all let me correct a slight misinterpretation of the transaction from your previous memo. The final exchange under swap contract HK704049/44749576
where Sampoerna will pay Chase IDR 245,000,000,000 and where Chase will pay Sampoerna USD

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vSubcommittee on Investigations
EXHIBIT #187d

100,000,000 will occur on October 1, 2012.

The final exchange under swap HK704048/44749573 where Chase will pay Sampoerna IDR 245,000,000,000 will also occur on October 1, 2012.

The transaction under swap contract HK704049/44749576 is what we call a net basis swap or a principal only swap whereby customer pays Chase a coupon to lock in an off market exchnage rate for its future purchase of USD.

We have done many of these transactions in Asia (Thailand and Indonesia) all of which have been treated on a MTM basis.

Even if you look at the two transactions together and therbey net off the IDR payments at the end (which we are not permitted to do for credit or capital purposes because the bank is not comfortable that netting will be permissible in Indonesia) the transaction has been hedged as a swap by the traders (not as a deposit through treasury) and is therefore an off-balance sheet transaction with mark to market implications.

Please let me know if you need anything else.

Regards

---- Previous E-Mail ----
To: Andrew Best/Chase
cc:
From: Jonathan Porter Asia-Pacific 2843-1238 Fax Number: 2522-8848
Date: Wednesday October 15, 1997 08:55 AM
Subject: Sampoerna Deal

FYI,

To: Jonathan Porter @ Chase
cc: See Below
From: Edwin M. Jenkins/CHASE
Date: Tuesday October 14, 1997 06:06 AM
Subject: Sampoerna Deal

I have spoken to Pat O'Brien and Bill Chiu about this deal since Cotter has threatened me with first degree murder. I will talk again in the morning with Pat and Bill. The bank MAY have a "new position" that transactions documented as swaps generally should be accounted for as swaps and not loans. If you put this deal on the accounting spectrum, it is as close to a borrowing transaction as you can get, and as we discussed the other night the true economic substance of this deal is an "investment" from the counterparty's perspective.

One question is why is the transaction documented as a swap. Is it to avoid withholding taxes? Has appropriateness been assessed?

cc: John Cotter @ Chase
Michaell Gordon/Chase @ Chase
Jeffrey Satenstein/Chase @ Chase
Patrick O'brien/Chase @ Chase
Bill Macomber/Chase @ Chase
Fai-Hong B. Chiu @ Chase
Michael Perine @ Chase

cc: John Cotter @ Chase Bill Macomber/Chase @ Chase Patrick O'brien/Chase @ Chase
Michaell Gordon/Chase @ Chase Fai-Hong B. Chiu @ Chase Jonathan Porter @ Chase
Jeffrey Satenstein/Chase @ Chase Michael Perine @ Chase

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To: Jack Alexander, Janet Caruso/CHASE, John Cotter, Doug Kurowski/CHASE, Alan F. Magleby/CHASE, Aditya Mohan/CHASE, Russell Neumann/CHASE, Robert T. O'Neill/CHASE, Timothy Plesko/CHASE, Jim Ruppert/CHASE, Jeffrey Satenstein/CHASE

cc: Fai-Hong B. Chiu, Bruce Ellard/CHASE, Sharon Fiolek/CHASE, Marjorie E. Gross/CHASE, Peter 'London' Hughes/CHASE, Edwin M. Jenkins/CHASE, Anand Krishnan/CHASE, Bill Macomber/CHASE, Irene Morfit/CHASE, David M. Morris/CHASE, Patrick O'Brien/CHASE, Joseph Sciafani/CHASE, Mark Staines/CHASE

From: Diane Butterfield/CHASE

Date: 11/13/97 12:05:26 PM

Subject: Loans/Borrowings Documented as Derivatives

Corporate Accounting Policies recently met with various individuals to revisit the issue of accounting for transactions that are in derivative form, but economically resemble loans or borrowings. Based on our discussions, it was concluded that such transactions which are confirmed with the counterparty as derivatives should be reported in Trading Assets/Liabilities - Risk Management Instruments and marked to market. Under no circumstances should such transactions be reported in Other Assets or Other Liabilities. This conclusion supercedes the interim guidance set forth in a September 20, 1996 memorandum previously distributed.

Reminder: As such transactions are typically highly structured, they are subject to the Appropriateness Policy. To the extent that there are any issues related to appropriateness, the business units are advised to contact Marjorie Gross in the Legal Department.

Regards,
Diane

Permanent Subcommittee on Investigations
EXHIBIT #187e

Janet Caruso
07/07/1999 03:52 PM

To: Lesley DanielsWebster/CHASE
cc:
Subject: Prepaid Forwards

Don Layton 05/21/99 05:27 PM

Global Markets & International 212-270-2249 Fax Number: 212-270-2296

To: Don M. Wilson/CHASE@CHASE, Fraser Partridge/CHASE@CHASE
cc: David Pflug/CHASE@CHASE, George Brash/CHASE@CHASE
Subject: DISGUISED LOANS

DON AND FRASER:

I HAVE ASKED DAVID PFLUG TO COORDINATE A TOP LEVEL REVIEW OF OUR DISGUISED LOANS, AND TO WORK ON DEVELOPING A POLICY THAT MEETS ALL OUR NEEDS, BOTH TECHNICAL AND STRATEGIC.

THIS WOULD INCLUDE THINGS LIKE:

O MIS ON HOW MUCH WE HAVE

O SOMEHOW ENSURING CONSISTENT ACCOUNTING TREATMENT

O SOMEHOW ENSURING MAXIMUM EFFORT AT OUR TRADITIONAL "LOANS ARE MADE FOR DISTRIBUTION" STRATEGY, DESPITE THE ODD FORM OF THESE LOANS.

O ENSURING THAT WE UNDERSTAND THE SUBTLE RISKS ASSOCIATED WITH SOME TRANSACTIONS, INCLUDING "DOCUMENT RISK".

I WOULD EXPECT DAVID TO INVOLVE A FAIRLY LARGE NUMBER OF PEOPLE ON THIS, YOURSELVES INCLUDED.

THANK YOU IN ADVANCE FOR SUPPORTING THIS EFFORT.

DON

Don Layton 13/05/99 01:51

To: David Pflug/CHASE@CHASE
cc: Suzanne Hammett/CHASE@CHASE, Brian O'Neill@CHASE, Robert Fallon, Herb Aspbury/CHASE@CHASE, Don M. Wilson/CHASE, Fraser Partridge/CHASE
Subject: DISGUISED LOANS

DAVID

THIS TOPIC HAS COME UP IN A VARIETY OF WAYS RECENTLY, AND WAS A DISCUSSION ITEM AT BRIAN O'NEILL'S OFFSITE TODAY.

I THINK WE NEED TO MAKE AN OFFICIAL PROJECT OUT OF THIS. HERE IS HOW I SEE THE ISSUE:

WE ARE MAKING DISGUISED LOANS, USUALLY BURIED IN COMMODITIES OR EQUITIES DERIVATIVES (AND I'M SURE IN OTHER AREAS). WITH AFEW EXCEPTIONS, THEY ARE UNDERSTOOD TO BE DISGUISED LOANS AND APPROVED AS SUCH. BUT I AM QUEASY ABOUT THE PROCESS:

Permanent Subcommittee on Investigations
EXHIBIT #187f

O IS THE PRICING RIGHT VS. THE LOAN MARKET, OR DOES IT UNDERPRICE VS. THE LOAN MARKET EVEN IF IT PRODUCES A GOOD SVA?

O IS THERE INTERNAL CAPITAL ARBITRAGE GOING ON?

O IS THE DOCUMENTATION UP TO LOAN STANDARDS, AS OPPOSED TO ISDA MASTER.

O AS A STRATEGY MATTER, IT CAN INDICATE PEOPLE FALLING BACK INTO THE HABIT OF MAKING LOANS TO MAKE LOANS (EVEN IF WELL-PRICED DUE TO STRUCTURING), AND WE DEFINITELY WANT TO END THAT BAD HABIT.

O IT ESCAPES ROUTINE TRASNPARENCY, AS THE LOAN IS BURIED IN THE TRADING BOOKS AND WHEN WE SAY "WE HAVE XXX LOANS TO COUNTRY YYY" IT IS NOT INCLUDED. WE NEED TO KEEP IT TRANSPARENT AND INCLUDE THEM.

O IT ESCAPES THE DISTRIBUTION DISCIPLINES AND PROCESS, I.E. IT JUST SITS ON THE BOOKS.

AS A POLICY MATTER, I THINK WE NEED A SMALL TASK FORCE TO NOT ELIMINATE DISGUISED LOANS BUT TO MAKE SURE THEY ARE DONE RIGHT, THAT THEY ARE TRANSPARENT AND DON'T DISAPPEAR FROM OUR RADAR SCREEN, AND THAT WE INCLUDE THEM IN THE DISTRIBUTION PROCESS OVER TIME.

PLEASE THINK ABOUT THIS AND LET'S TALK. I HAVE COPIED OTHER RELEVANT PARTIES SO THEY KNOW THIS IS GOING ON, AS SEVERAL WILL UNDOUBTEDLY GET INVOLVED, AND THEY CAN WEIGH IN WITH ANY THOUGHTS THEY HAVE AS WELL.

DON

Go to\Inbox | Go to\Next | Go to\Previous

Patrick O'Brien

06/04/1999 03:05 PM EDT

To:Dermot Drysdale/CHASE@CHASE
cc:Joseph Sclafani/CHASE@CHASE, David M. Morris/CHASE@CHASE, Dinsa Mehta/CHASE@Chase, Janet Caruso/CHASE@Chase, Maggie Serravalli/CHASE@CHASE, Erik Gerken/CHASE@CHASE, Bruce Ellard/CHASE@Chase, Ronald Antonelli/CHASE@CHASE, George Brash/CHASE@CHASE, Vivian Shelton/CHASE@CHASE, Nick Quintana/CHASE@CHASE, Anthony Carpentieri/CHASE@CHASE, Sharon Fiolek/CHASE@CHASE, Lorry Ripley/CHASE@CHASE, Aditya Mohan/CHASE@CHASE
bcc:
Subject:Re: Prepaid Forwards

Subsequent to sending my e-mail, we received a call from Joe Sclafani. There has been recent concerns expressed by senior management regarding these types of transactions. All of us have been grappling for years with the issue of determining when a structured transaction is more a kin to a loan or a derivative. There are no easy answers.

From our discussion with Joe, we still do not object to the classification of this transaction as trading. However, we need to get more information regarding the up-front income recognition. It had been my understanding that through the reserve/holdback process, a sufficient amount of income would be deferred to match all of the risks to which Chase is exposed over the life of the deal, including maintaining a sizable trading asset on the balance sheet for an extended period of time.

At this stage, it is important that we all get on the same page. It would be very helpful to move from the conceptual discussion of MTM vs accrual and to look at the actual results. I would greatly appreciate it if you could put together a rough summary of the income to be recognized up-front and over the life of the deal including the impact of any holdbacks/reserves. I do not want to create a major project for this one deal, but we need to make sure everyone understands the economics of the transaction to ensure that we are recognizing income appropriately and not just arbitraging Chase's accounting policies.

I realize this request is somewhat vague, so please call me to discuss the approach to this analysis.

Thanks and regards,

Pat

▼Dermot Drysdale

International Capital Markets - Middle Office 3393 Fax Number: 4719 / 4937

To: (see below)
Subject: Re: Prepaid Forwards

Pat,
Reading your note I am assuming that everything should be 100% marked to market with no mixture of accruals and mark to market as is done at the present time.Is this a correct interpretation?

Rgs

Permanent Subcommittee on Investigations
EXHIBIT #187g

Dermot
Patrick O'Brien on 03/06/99 15:42:10

Corporate Accounting Policies 701-7013 Fax Number: 701-7047

To: (see below)
Subject: Prepaid Forwards

We have reviewed the attached accounting for prepaid forward contracts to purchase commodities. From an accounting policy perspective, we agree that mark-to-market accounting is supportable; however, Corporate Accounting Policies is not in a position to opine on the MTM methodology. In summary, the accounting is as follows:

- The full amount of the prepaid forward is classified as Trading Assets - Risk Management Instruments and with all related income classified as Trading Revenue. The oil swap hedge is reported in a similar manner.
- The funding of the prepaid forward is obtained via an intercompany deposit from the Gold Bullion Desk. Both the Energy Desk and the Gold Bullion Desk accounts for the deposit on a MTM basis. All amounts related the deposit are eliminated in consolidation.

The MTM must represent the appropriate fair value of the transaction including amounts that should be deferred for respective risks in accordance with established policy. In order to ensure that each of these components have been reviewed and approved, I suggest that you obtain approvals from the following individuals:

Janet Caruso: General valuation approach
Vivian Shelton: Market Risk reserves, if any
George Brash: Credit risk holdback
Nick Quintana: Credit capital holdback

One minor modification to the entries that I would suggest is the balance sheet classification of the MTM on the prepaid forward be included in the balance for the forward as opposed to the MTM account for the intercompany deposits.

If you have any questions, please let me know.

Regards,

Pat

---------- Forwarded by Patrick O'Brien/CHASE on 06/02/99 02:23 PM ----------

To: Dermot Drysdale/CHASE@CHASE
cc: Patrick O'Brien/CHASE@CHASE, Janet Caruso/CHASE@Chase, Maggie Serravalli/CHASE@CHASE, Erik Gerken/CHASE@CHASE, Bruce Ellard/CHASE@Chase, Ronald Antonelli/CHASE@CHASE
Subject: Prepaid Forwards

Dermot,

Attached is a document that walks through our current processes for prepaid forwards. It is based on a

deal done with Enron in 1998 which closely resembles the proposed deal with Pan America. I have put together the accounting entries that Chase books for this transaction as well as the accounting entries that Mahonia would book.

Please let me know if you have any comments or questions.

Regards,

Lorry

prepaid forwards.xls

To: Dermot Drysdale/Chase @Chase

cc: David M. Morris/Chase @Chase George Brash/Chase @Chase
Dinsa Mehta/Chase @Chase Vivian Shelton/Chase @Chase
Janet Caruso/Chase @Chase Nick Quintana/Chase @Chase
Maggie Serravalli/Chase @Chase Anthony Carpentieri/Chase @Chase
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Bruce Ellard/Chase @Chase Lorry Ripley/Chase @Chase
Ronald Antonelli/Chase @Chase Aditya Mohan/Chase @Chase

To: Patrick O'brien/Chase @Chase

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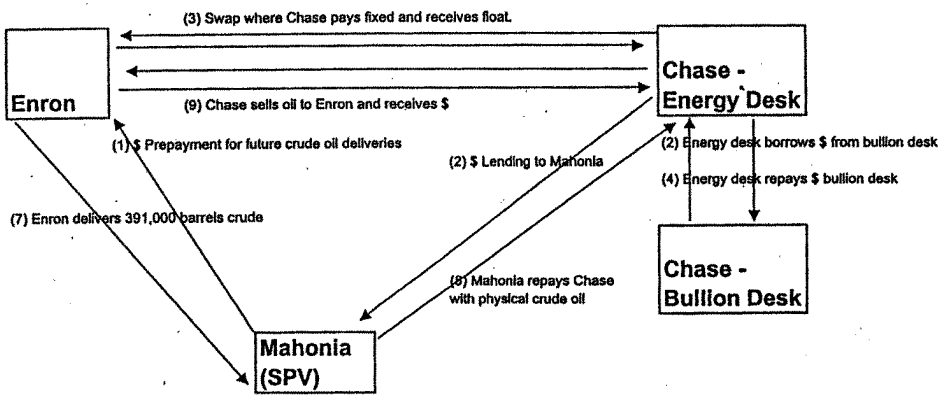
Bruce Ellard/Chase @Chase Lorry Ripley/Chase @Chase
Ronald Antonelli/Chase @Chase Aditya Mohan/Chase @Chase

ENRON '98



Sureties

(5) Guarantees payments of oil. Enron pays for guarantee - included in prepayment amount from Enron. Mahonia is beneficiary.

AT DEAL INCEPTION:

(1) Mahonia enters into a prepaid forward with Enron.

(1a) Mahonia pays Enron $249,994,351.87 up front on 12/2/98. Enron will repay Mahonia with 391,000 barrels of crude oil (at a fixed price) every month beginning May 1999 and ending December 2002. Prepayment amount based on delivery quantity, delivery schedule, forward price curve, discount factor plus a spread covering any prepayment for the surety bond, the credit risk associated with the insurance carriers and Enron and pipeline fees.

(1b) For putting this transaction together, Chase receives a fee from Enron of $375,000.

(1c) Chase pays Mahonia a fee of $12,500 for their involvement.

(2) Mahonia funds their payment to Enron by borrowing funds from the Chase Energy Desk.

(2a) Chase energy desk lends $ to Mahonia for the prepaid forward. Mahonia will repay the loan by delivering to Chase 391,000 barrels (at a fixed price) of crude oil monthly. The dollars lent to Mahonia by the energy desk are booked as a prepaid forward - trading asset.

(2b) Chase energy desk borrows the money to lend Mahonia from the Chase bullion desk.
A series of dollar placements with "londonoil" are booked in OMR and vbopts. P + I on maturing deposits is set to equal the future value of the oil to be received
The first settlement on 5/20/99 is for $6,126,167.02 in principle and $162,066.73 in interest for a total of 6,266,233.75.
An offsetting dollar deposit (and accrued interest expense) is manually posted to the general ledger to eliminate the intradesk balance sheet positions.

(3) To hedge the oil it will receive at a fixed price, Chase energy desk enters into a swap with Enron. Chase pays fixed and receives float.
No entry to ledger at inception of swap. Because this swap is booked in CORMS and the physical oil transaction is not, a short oil position has been created. This creates a problem in terms of risk limit reporting and mtm calculations. To represent the physical receipt of oil, a swap is booked in CORMS between Chase and Mahonia where Chase receives fixed and pays float. This ensures that the risk limits and MTM are correct and that the position is flat. No entry to ledger at inception of swap.
We are looking into the possibility of booking a physical trade in CORMS to replace this swap.

(5) Surety agreement where Enron pays to guarantee delivery of oil to Mahonia. The payment for the surety bond is captured in the prepayment amount (see 1a).

BETWEEN INCEPTION AND FIRST DELIVERY DATE

(6) Interest is accrued and prepaid forward and swap are mtm.
- (6a) The AIR on the bullion loan is accrued by the system and posted to the ledger. A manual adjustment is made to the ledger to capture the intracompany AIP with the energy desk. The interest income on the $ placement is reclassified to Realized Trading p/l as it represents income on the prepaid forward to Mahonia.
- (6b) The prepaid forward is MTM through vbopts based on LIBID for o/n to 9 mos and swap bid/asked from 1yr +.
  On Mahonia's books, the prepaid forward and the borrowing from Chase are both MTM. P/L offsets.
- (6c) The swaps booked in CORMS are MTM (through CORMS) on a monthly basis. P/L offsets.

FIRST DELIVERY DATE

(7) Enron delivers to Mahonia 391,000 barrels of crude oil.

(8) Mahonia delivers the 391,000 barrels of crude oil to the Chase energy desk as repayment for the $ (oil is nominated - no entries to the ledger for the physical).
Mahonia reduces their prepaid forward and borrowing from Chase.

(9) Chase Energy desk sells the oil to Enron (at market) and receives $5,967,324.70.
- (9a) Chase Energy desk receives dollars for the sale of the oil and repays bullion desk. Remainder is booked to A/P to pay pipeline fees.
  (5,967,324.70 + 325,703.00 = 6,293,027.70)
- (9b) Intradesk liability and prepaid forward amounts are reduced by the proceeds (less pipeline fees).

(10) Chase and Enron settle on the swap. The net proceeds of $325,703.00 that Chase receives makes up the difference between the value of the oil at market and the $ amount needed to repay the loan.
- (10a) Chase Energy desk receives dollar proceeds from swap and uses to repay the bullion desk. Remainder is booked to A/P to pay pipeline fees.
  (5,967,324.70 + 325.703.00 = 6,293,027.70)
- (10b) Intradesk liability and prepaid forward amounts are reduced by the proceeds (less pipeline fees).

There is no settlement on the swap between Chase and Mahonia.

(11) Chase pays Enron a pipeline fee.
There is $1,071.05 p/l fall out on the settlement.

(12) At May month end, mtm on settled portion of prepaid forward and swap will be removed from the ledger and remaining amount of prepaid fwd and swap will be re-mtm.
On Mahonia's books, mtm on settled portion of prepaid forward and borrowing from Chase offset.

MEMORANDUM

TO: Joseph Scalfani,
David Morris
Patrick O'Brien

FROM: Janet Caruso

DATE: August 17, 1999

RE: DBF's

Just to fill you in, a few things have occurred since we booked the recent Prepaid Forward deals, which you may or may not be aware of:

1. Loans disguised as derivatives are now known as "Derivatives Based Funding, ("DBF's")

2. In addition to the Prepaid Forward Trades, Upfront FPA's have been added to the list of DFB's, thus far, along with Monetarized Equity Collars

3. In addition to the requirement of capital and credit reserves for the DFB component of the aforementioned transactions, Market Risk Management has brought up the issue of marking DFB's independently to market to also reflect changes in the market credit spread of the counterparty/ industry. This represents another dimension in independently marking the trade to market that I agree with Market Risk should take place for all DFB-related valuations; for that matter, I think we should include this credit spread element in all the independent marks to markets done for GTD's FX and Derivatives in order to achieve the most accurate mark to market on a regular basis. This is a much bigger issue, though, that requires much more discussion with all concerned; so, for the time being, this additional valuation technique is solely being addressed as a requirement for the DFB portfolio of trades.

Permanent Subcommittee on Investigations
EXHIBIT #187h

4. I have been continuing to work closely with Credit re the required DFB reserves scenarios. An issue came up with, first, with the Prepaid Forwards, and then with Upfront FPA's reserve amortization. I was using a straight line amortization approach once the relevant trigger occurred (i.e. the first Commodity or security delivery was made). For 98% of the prepaid deals, this approach worked fine, whereas for the Upfront FPA's, the applicable percentage was smaller. In order to achieve full transparency, I originally agreed with Credit to review every confirmation for every DFB deal, and emulate the exact amortization schedule contained therein. The first deal I looked at was a $84,000.00 Upfront FPA deal that ran 14 years; based on the credit facility grade the required credit provision came to a total of $195.00, which would be straight-lined amortized on a monthly basis over the 14 years (which equated to $1.00 @ month). The corresponding amortization schedule in the confirmation for this deal ran to 40 pages of resets. At this stage, Credit then agreed that a straight line amortization of reserves was transparent enough.

I have already worked through the required reserve scenarios for the Upfront FPA deals, and, at this stage, addressed an accounting issue re correct balance sheet classification with Pat O'Brien for the Upfront FPA's, that becomes an even larger classification issue once the Monetarized Equity Collars are brought into the equation. The issue I have is primarily one of consistency, which I would like to discuss with yourselves at greater length to verify, going forward, that we are all in agreement as to the correct classification of these DBFs'. I have already discussed conceptually with Addy Mohan, since there is a collar booked in London, but would also like to include him on an ongoing basis in any further discussion on this topic.

Accounting Issue

In the case of the Prepaid Forwards, the DFB component is booked to Risk Management Instruments, which, I think, was fully vetted with all concerned. In the case of the Upfront FPA's, the DFB component is currently booked to Trading Assets. Conversely, in the case of the Monetarized Equity Collars, depending on origin of booking location, the DFB component is booked to either Other Assets or Trading Assets.

Regarding income recognition, Prepaid Forwards and Upfront FPA's are fully marked to market on a daily basis, whereas the DFB component of

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the Monetarized Equity Collars are accrued over the life of the deal, regardless of whether the corresponding asset is booked to Trading Securities or Other Assets.

In addition to the aforementioned accounting classification description, the following is a brief synopsis of the additional DFB's that are now on the table:

Upfront FPA's

Generally speaking, a forward purchase agreement ("FPA") is a fixed rate investment vehicle for funds deposited or received on a regular basis, such as bond fund proceeds or tax receipts. Historically, municipal issuers have invested funds deposited in the bond fund in securities with maturities of less than one year, and, more commonly, in overnight repurchase agreements or demand accounts. As a result, investment returns are reflective of the levels associated with the front end of the yield curve, which can be significantly lower than longer term investments. Since the corresponding tax-exempt debt requires the investment to be short-term in order to meet liquidity requirements, an issuer is unable to access higher returns by investing in intermediate or longer-term maturities.

An FPA allows the municipality the following benefits:

- An increase in the rate of return over conventional alternatives;
- A fixed rate of return for a pre-determined period, resulting in known future investment earnings' flow, enabling better financial planning;
- A simplified tracking of future investment earnings, if needed, for arbitrage rebate purposes; and
- The ability to tailor the investment earnings payment schedule to meet desired budget requirements or cashflow needs.

FPA's fall into three (3) categories:

1. Constant Rate

   An issuer may elect to lock-in a fixed rate today and receive the proceeds on a periodic basis (i.e. semi-annually) for the term of the contract. The mechanics of this structure require the issuer to make

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deposits in the bond fund on pre-specified dates, however, the market value of the securities purchased with the deposited funds will also include the interest earnings thereon at the pre-specified earnings rate. Currently, the FPA portfolio contains forty-eight (48) constant rate deals.

2. Escrow

An FPA in a defeasance escrow is a supplement to an existing portfolio of Treasury securities. Issuers have purchased the most efficient portfolio of securities available, and then entered into an FPA to extract the value remaining in the inefficiencies of the portfolio. Under this structure, a municipal issuer does not purchase the initial portfolio of Treasuries; but, rather, gross funds the defeasance requirements while simultaneously entering into an FPA that monetarizes all of the future investment earnings. In return, we will pay an upfront payment or an amount that maximizes the investment value for the term that the escrow proceeds are avalable for investment. The escrow trades require us to send money out at settlement but we then turn around and sell the issuer securities on the same day. This is because tax counsel requires a full defeasance at closing and we can then substitute securities for cash after closing, subject to verification by the accountants on the deal. Currently, the FPA portfolio contains one hundred and eighty five (185) escrow deals.

3. Upfront

The single, upfront payment structure provides the municipal issuer all of the contract' future investment earnings upfront (hence, the DFB component). In return, on each scheduled deposit date (i.e. monthly debt service deposits), the issuer purchases, on a delivery versus payment basis, a treasury security maturing on or prior to the bond payment date in an amount equivalent to the deposit amount specified upon the contracts closing. Currently, the FPA portfolio contains twenty-nine (29) upfront deals, and is not anticipated to expand beyond this number. The DFB required capital provision reserves amount to $522,347 currently, whereas the required capital reserves are $2,875,983. The current asset level is $36,199,000 on a straight line amortization basis. The significant amount of required reserves, relevant to the outstanding asset level, is very much a factor of the extended tenor of these deals.

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Monetarized Equity Collars

There are for (4) monetarized equity collars; one booked in London, with the remaining three (3) booked in New York. The average tenor of these deals is between two to three years, and all have a 1-G credit rating, so required reserves will not be significant. As previously mentioned, accounting treatment is inconsistent between locations from a balance sheet perspective, which needs to be rectified. In addition the DFB component is accrual accounting, whereas the derivative component is valued on a marked to market basis. In addition to seeking consistent balance sheet treatment for these transactions, I would also like to pursue full marked to market treatment for the DFB component.

Please let me know if you require any additional information.

Regards,

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Gordon Neald

NY Equity Ops 212-622-8743 Fax Number: 212-622-8323

To: Vernon Sterling/CHASE@CHASE
cc: Dermot Dryedale/CHASE@CHASE, Janet Caruso/CHASE@Chase
Subject: Accounting for Compound Instruments

Vernon,

The attached indicates that you should book all P&L on MEC's to trading income and record the entire asset as a derivative. It won't change the method of revenue recognition, just the accounting classification, ie whatever accrual you are booking to interest income should be booked to trading income and the monetization should be booked to derivatives instead of debt instruments. Let me know if you have any questions.

Regards, Gordon

---------- Forwarded by Gordon Neald/CHASE on 03/13/2000 09:39 AM ----------
Patrick O'Brien on 03/13/2000 09:01:19 AM

Corporate Accounting Policies 701-7013 Fax Number: 701-7047

To: (see below)
Subject: Accounting for Compound Instruments

As you are aware, Corporate Accounting Policies had been attempting to resolve some apparent inconsistencies regarding the classification of trading derivatives that involve an up-front payment. We had proposed classifying some of these instruments as cash instruments instead of derivatives to reflect the funding component of such instruments. While this proposal may have had conceptual merit, it was clear from the input we received that there are significant, valid operational and business issues.

As a result, we have decided to drop this proposal and will not recommend a change to the classification of such trading instruments. Specifically, prepaid forwards should continue to be classified as derivatives with all resulting income reported in Trading Revenue.

We appreciate you feedback to this proposal that helped us reach this conclusion.

Thanks and regards,

Pat

To: Janet Caruso/Chase @Chase
Bob Feeney/Chase @Chase
John Cotter/Chase @Chase
Steven Hocevar/Chase @Chase
Aditya Mohan/Chase @Chase
Alan F. Magleby/Chase @Chase
Neil Addington/Chase @Chase
Robert T. O'neill/Chase @Chase
Susan Sperling/Chase @Chase
John Locher/Chase @Chase
Marianne Lake/Chase @Chase

cc: Joseph Sclafani/Chase @Chase
David M. Morris/Chase @Chase
Fai-Hong S. Chiu/Chase @Chase
Sharon Fiolek/Chase @Chase
Edwin M. Jenkins/Chase @Chase
Tanveer Bhatti/Chase @Chase
Dermot Dryedale/Chase @Chase
Zandra Sherrington/Chase @Chase
Michaell Gordon/Chase @Chase
Jeremy Hood/Chase @Chase
Daniel Mcdonagh/Chase @Chase
Alex Castle/Chase @Chase
James Hutter/Chase @Chase
Leonard Zuckerman/Chase @Chase
Poh Keng Cheong/Chase @Chase
Gordon Neald/Chase @Chase

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Permanent Subcommittee on Investigations
EXHIBIT #187i

Don M. Wilson

02/18/2000 09:34:55 AM

To: Janet Caruso/CHASE@Chase
cc:
Subject: Re: Prepaid Forwards

Thanks.

Regards,

DMwilson

Janet Caruso

Janet Caruso
02/17/2000 05:43 PM

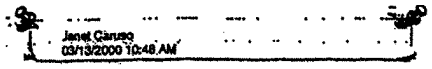
Global Trading Division 212-834-5011 Fax Number 212-834-8544

To: Don M. Wilson/CHASE@CHASE, Fraser Partridge/CHASE@CHASE
cc: William J. Staples/CHASE@Chase
Subject: Prepaid Forwards

Today's meeting on the proposed change in accounting for Prepaid Forwards ended successfully, from a bottom line perspective. After much discussion, a compromise of sorts was finally reached that the proposed policy would be fully complied with simply by recognizing a component of the p/l as interest income. The current timing of p/l recognition will not be changing in any way. Hence, all this proposal now translates to is an accounting classification/ operations, not a business, issue. The revelation that a significant amount of money was at stake may or may not have been a contributing factor to the revised compliance terms.

Please let me know if you have any questions.

Regards,



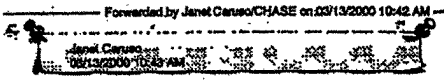
Global Trading Division 212-834-5011 Fax Number 212-834-5844

To: Dexter Charles/CHASE@CHASE, Jeffrey W. Dellapina/CHASE@CHASE, Dinea Mehta/CHASE@Chase, Mark Babunovic/CHASE@CHASE
cc:
Subject: Prepaid Forwards

Pat O' Brien's group has entirely dropped their proposal to change the accounting of Prepaid Forwards. This is good news.

Bye,

Forwarded by Janet Caruso/CHASE on 03/13/2000 10:42 AM



Global Trading Division 212-834-5011 Fax Number 212-834-5844

To: Don M. Wilson/CHASE@CHASE, Fraser Partridge/CHASE@CHASE
cc: William J. Staples/CHASE@Chase
Subject: Prepaid Forwards

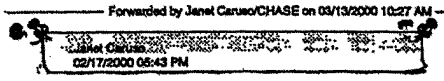
The sole remaining open issue from Corporate's recent proposed change in accounting for Prepaid Forwards was one of accounting classification. Corporate had proposed that the upfront payment component consolidate to Trading Assets (component of GTD's target asset levels). Currently, the upfront payment (approximately $2.6 billion) consolidates to Risk Management Instruments (not a component of GTD's target asset levels).

It was revealed this morning that Corporate is entirely dropping their proposal because it did not have Joe Sclafani's support. Hence, the Prepaid Forward's upfront payments will continue to consolidate to Risk Management Instruments with Corporate's blessing, and said balances will not be assessed against the division's target asset levels.

Please let em know if you have any questions.

Regards,

Forwarded by Janet Caruso/CHASE on 03/13/2000 10:27 AM



Global Trading Division 212-834-5011 Fax Number 212-834-5844

To: Don M. Wilson/CHASE@CHASE, Fraser Partridge/CHASE@CHASE
cc: William J. Staples/CHASE@Chase
Subject: Prepaid Forwards

Today's meeting on the proposed change in accounting for Prepaid Forwards ended successfully, from a

Permanent Subcommittee on Investigations
EXHIBIT #187j

bottom line perspective. After much discussion, a compromise of sorts was finally reached that the proposed policy would be fully complied with simply by recognizing a component of the p/i as interest income. The current timing of p/i recognition will not be changing in any way. Hence, all this proposal now translates to is an accounting classification/ operations, not a business, issue. The revelation that a significant amount of money was at stake may or may not have been a contributing factor to the revised compliance terms.

Please let me know if you have any questions.

Regards,

Fraser Partridge
03/20/2000 09:55 AM

To: Janet Caruso/CHASE@Chase
cc: Don M. Wilson/CHASE@CHASE, William J. Staples/CHASE@Chase
Subject: Re: Prepaid Forwards

Unbelievable . By the time we are finished the deals will have matured .
br Fraser

Janet Caruso

Janet Caruso
20/03/2000 14:51

Global Trading Division 212-834-5011 Fax Number:212-834-6644

To: Don M. Wilson/CHASE@CHASE, Fraser Partridge/CHASE@CHASE
cc: William J. Staples/CHASE@Chase
Subject: Re: Prepaid Forwards

The attached refers to Prepaid Forward spread information requested by Don Layton last week (see attached email to Jeff Satenstein). Despite the fact that we have recently received Joe Sciafani's re-approval of full mark-to-market accounting treatment for Prepaid Forwards, it appears from the attached memo that Don Layton favors accrual accounting for the loan component of the Prepaid Forward transactions (see bolded text). There is a meeting this afternoon to discuss. Will keep you informed of all progress.

Regards,

---------- Forwarded by Janet Caruso/CHASE on 03/20/2000 09:39 AM ----------
[redacted] 03/17/2000 07:28

Global Markets & International 212-270-2249 Fax Number: 212-270-7511

To: Jeffrey Satenstein/CHASE@CHASE
cc: Janet Caruso@CHASE, Jeffrey W. Dellapina/CHASE@CHASE, Robin A. Ayres/CHASE@CHASE
Subject: Re: Prepaid Forwards

Everyone

In looking over the numbers, it "seems" okay as much as I can tell. But in the future, don't confuse apples and oranges - the loan spreads you have should be compared not tot he "all in spread" which includes the up-front trading revenue we take in. My issue is that I do not want us PV-ing loan-equivalent spread. I want the loan-type spread to come in on an accrual basis over time. I think that is the "prepay commodity spread" column in your charts, but I'm not sure. And that is a lot smaller than the all-in prepay spread.

If I understand right, then, the "banking spread on existing RC" should be compared only to the "prepa commodity sprad", not the all-in spread.

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Permanent Subcommittee on Investigations
EXHIBIT #187k

Don

Janet Caruso
03/16/2000 06:28 PM

Global Trading Division 212-834-5011 Fax Number 212-834-5644

To: Jeffrey Satenstein/CHASE@CHASE, Jeffrey W. Dellapina/CHASE@CHASE
cc:
Subject: Prepaid Forwards

Overview.xls

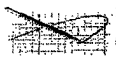
---------- Forwarded by Janet Caruso/CHASE on 03/16/2000 06:20 PM ----------

Jeffrey W. Dellapina
03/16/2000 05:06 PM

To: Jeffrey Satenstein/CHASE@CHASE
cc: Janet Caruso/CHASE@Chase
Subject:

Attached is return analysis on the commodity prepay deals.

Overview.xls



Richard S. Walker
04/15/1999 02:53 PM

To: Carrie Cerda/CHASE@CHASE
cc:
Subject: Enron CLO Discussion

---------- Forwarded by Richard S. Walker/CHASE on 04/15/99 01:56 PM ----------

Richard S. Walker
01/15/99 04:24 PM

To: Philip Orenstein/CHASE@CHASE, William Magid/CHASE@CHASE, Dan Rouse/CHASE@CHASE, Eric Gelb/CHASE@CHASE, Sandra Aultman/CHASE@CHASE, Fred Engel/CHASE@CHASE, Christopher Teague/CHASE@CHASE
cc: Juli Bieser/CHASE@CHASE
Subject: Enron CLO Discussion

Thanks to each of you for your agreement to be at next Tuesday's meeting with Enron regarding various CLO type concepts which are being considered for the purpose redeploying certain Enron exposure held by Chase and other top tier Enron banks into other markets.

I expect Enron to show up at the meeting with a flip book outlining their objectives for this exercise and hopefully including some additional data regarding their various bank exposures.

Included with this e-mail is the following:

- A repeat of Dec 18, 1998 call report outlining our current uderstanding of Enron's objectives and exposures.
- Attachments providing some detail regarding Chase's Enron exposure as well as our data on a number (but certainly not all) of Enron's various deals and othe banks' exposures.

To repeat Fred Engel's earlier logistical information, the meeting on Tuesday will be at 3:30pm in Room A 21st Flr. at 270 Park. The Enron attendees are expected to be Bill Brown (VP Enron Capital Mgmt.) and Doug McDowell (Director of ECM)

See you Tuesday

Rick Walker

CHASE

Call Report

ENRON CORP

Client Attendees:	**Chase Attendees:**	**CC: List:**
Jeff McMahon - Treasurer Enron Corp Bill Brown - VP Enron Capt. Mgmt. Doug McDowell - ECM Larry Derrett - Enron Energy	Richard S. Walker Juli Bieser Christopher Lowe Philip Orenstein Eric Gelb Fred Engel	John Youngblood William Crusoe

Permanent Subcommittee on Investigations
EXHIBIT #187l

Services	**Filing Officer:** Richard S. Walker	

Meeting Details:
Met with Enron to pursue preliminary discussions regarding a CLO concept the goal of which would be to reload underwriting capacity among Enron's top tier banks (Chase, Citi, Barclays, etc). These banks have had their balance sheets clogged with accumulating exposures over the last five years and all to one degree or another are full of "Enron-esque" expossures which is dragging down underwriting capacity A larger issue in the longer term might be to repackage the exposures of lower tiered banks for redistribution to the capital market.

Enron sponsors about $15 BN in debt capital of which on about half is on balance sheet:

Type of Enron Exposure	Approximate Amounts	Comments
Enron Corp. Balance Sheet	$ 8 BN	*$2 BN in CP and $6 BN in Bonds*
Project Financng	$ 3 BN	*Limited corp. footnote exposure*
Prepays	$ 1 BN	*Actually on B/S in "assets and liabilities for price risk mgmt." category. Much of the bank LC exposure has been redeployed to insurance company bid bonds*
JEDI I & II	$ 1BN	*Primarily bank market but about $200 MM is now privately placed*
Synthetic leases	$ 1 BN	*Footnote exposure*
Structured finance (Firefly, Marlin, FAS125, etc)	$ 1 BN	*Footnote exposure (contingencies)*
	$15 BN	

The first step in pursuing a potential repackaging of some of this exposure is to compile a more detailed analysis (deal size, tenor, interest rates, security etc). Although there are a myriad of issues, an initial list would include:

- Mark-to-market valuation of out of the money loans --Who pays ? Enron ? Banks ? Both ?
- Rating agency knowledge of existing deals. Some deals that are less know to the agancies may come to light if they are placed in newly formed rated vehicles. This could well cause some heartburn for Enron
- A variety of concentration issues --types of exposures, counterparties, country risks, etc.. These are just issues, it is likely that the total portfolio has a very interesting set of diversity characteristic.
- Redistribution of of bank loan voting rights and the implication of this for future amendments, etc.
- Swaps associated with individual deals, particularly projects.

A couple of very broad structural alternatives were discussed:

- Dynamic funding vehicle (like EICPO) vs. closed end trust.

- Bank sponsored CP conduit.
- Bank sponsored CLO in which Enron would consider being a major investor in the equity tranche
- Should Enron consider a more highly rated (AA) corporate capital structure in order to address its capacity issues.

Relationship Information:

Follow-Up:

The information gathering is in Enron's court. We will followup in mid January.

One specific input is our view on increased credit capacity if Enron were to uptier its capital structure. Juli please check Chase's own credit exposure grids.

Product(s) Discussed: Invest. Grade Sec./Pub. & Priv.

Confidential? N

Y (Yes) = Call Report viewable by Chase Attendees and CC's Only

N (No) = Call Report viewable by all Authorized Users

Client Type: B
Client Unit(s): Oil & Gas

Created By:
Richard S. Walker

Edit History:
1/1/1999 - Richard S. Walker/CHASE (Mailed)
1/1/1999 - Richard S. Walker/CHASE

---------- Forwarded by Richard S. Walker/CHASE on 01/15/99 03:55 PM ----------

01/15/99 11:47 AM

Structured Finance - Global Oil & Gas (713) 216-1303 Fax Number: (713) 218-8870

To: Richard S. Walker/CHASE@CHASE
cc:
Subject: Enron Exposure/Bank Universe

Bkuniv_1_8_99.xls EXPO_1_11_99.xls

Anne Marie Sullivan
06/15/2000 08:52 AM

Global Markets Credit (212) 270-5618 Fax Number (212) 270-3841

To: Jeffrey W. Dellapina/CHASE@CHASE
cc: Robert Traband/CHASE@CHASE, John J. Hogan/CHASE@CHASE
Subject: Re: Enron

Thanks for update. Is there a balance after the $650MM ?

ROB: The increase in the Commodity Physical Limit for Enron Nat Gas Mktg (UCN 830163069000) is not yet in GES. When do you think?

Thanks much and rgds.
AMS
Jeffrey W. Dellapina

Jeffrey W Dellapina
06/15/2000 08:06 AM

To: Anne Marie Sullivan/CHASE@CHASE
cc:
Subject: Re: Enron

$650MM before month end.

Mahonia prepays to Enron for future physical.

Chase enters into a financial swap with Enron North America for same notional and price levels

Chase will likely sell physical to Enron Nat Gas Mktg on a floating basis under the Physical Master. (I believe that Rob Traband obtained an increase of the Physical Line from $30MM to $50MM.

Anne Marie Sullivan

Anne Marie Sullivan
06/14/2000 02:56 PM

Global Markets Credit (212) 270-5618 Fax Number (212) 270-3841

To: Jeffrey W. Dellapina/CHASE@CHASE, Craig Shapiro/CHASE@CHASE

FOIA Confidential Treatment Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #187m

cc
Subject: Enron

Would someone give me an update on the Enron Prepaid that we are close to doing?
Thanks

FOIA Confidential Treatment
Requested by JPMC

Robert Traband 07/18/2000 06:17 PM

To "Sarah Heineman" <Sarah.Heineman@enron.com>
cc:
Subject: Re: Restructuring existing prepays

FYI: I will follow up with Molly.
---------- Forwarded by Robert Traband/CHASE on 07/18/2000 06:18 PM ----------

Richard S. Walker
07/17/2000 09:23 AM

Global Oil & Gas 713-216-8850 Fax Number 713-216-8882
To: Robert Traband/CHASE@CHASE
cc:
Subject: Re: Restructuring existing prepays

Rob -

FYI - you'll see that Jeff D. is working on this situation
---------- Forwarded by Richard S. Walker/CHASE on 07/17/2000 09:19 AM ----------

Jeffrey W. Dellapina
07/17/2000 07:24 AM

834-2032
To Davis_Thames@enron.net, Joseph_Deffner@ECT.enron.net, Brian_Kerrigan@ECT.enron.net
cc: Gregory Crowley/CHASE@CHASE, Richard S. Walker/CHASE@CHASE
Subject: Re: Restructuring existing prepays

Look forward to discussing this morning. (Brian, Rick called me over the weekend - I'll be available to assist.)

Some background and addit'l thoughts.

- several months ago we realised that the Mahonia margin calls had not been made and when these commenced, I began discussions with several individuals at Enron. I'm well aware that Enron was working on a proposal; howeve, I thought that the margin was being posted in the meantime.
- given the nature of these transactions, which involve a notionally equal swap where Enron pays fixed and Chase pays flaoting, Chase is currently posting huge margin with Enron NA. This collateral is likely in the form of Treasuries.
- Is it also worth considering the following solution: Grant Enron the right to re-hypothecate these Treasuries. (I have not yet cleared this with legal nor have I checked our Master with you.)

Let's discuss

Davis_Thames@enron.net on 07/14/2000 07:20:11 PM

Davis_Thames@enron.net on 07/14/2000 07:20:11 PM

FOIA Confidential Treatment
Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #187n

To: Jeffrey W. Dellapina/CHASE@CHASE, Gregory Crowley/CHASE@CHASE
cc: Joseph_Deffner@ECT.enron.net, Brian_Kerrigan@ECT.enron.net
Subject: Restructuring existing prepays

Jeff, Greg:

Today a person named Kit Kwan from Chase's Global Collateral department called Molly Harris, our credit dept. rep, asking for $420MM in collateral for five of the outstanding prepays. Needless to say, I think we'd all prefer to restructure the deals to avoid this posting.

I'm going to work this weekend with our structuring guys to get a proposal for all five deals to you by Monday a.m. If either of you makes it in to the office this weekend, please give me a call on my cell phone at 713-303-1297. We have already left messages for Rick Walker to let him know what we're going to do.

The affected prepays are:
Sep '95 $225MM (Nat gas)
Dec '97 $300MM (Nat gas)
Jun '98 $250MM (Nat gas)
Dec '98 $250MM (Crude)
Jun '99 $500MM (Nat gas)

The plan that we'd like to pursue is as follows:
- Terminate a given prepay by paying out the PV of the contract
- Create a new prepay struck at-the-money to eliminate the collateral requirement
- Goal is that money exchanged to terminate the existing deals will be paid back when the new deals are struck, such that there is no ending cash effect after the one-day wire transfers.
- For prepays with surety bonds, Phil Bair has indicated that we can restructure these deals without cancelling the bonds.

Please give me a call at your earliest convenience so that we can work on the timing.

Best regards,
Davis

FOIA Confidential Treatment
Requested by JPMC

Sandra Aultman 03/13/1998 12:13 PM

To Richard Garbarino/CHASE@CHASE
cc. Richard S Walker/CHASE@CHASE, Peter M Licalzi/CHASE@CHASE, Jim Nicholas/CHASE@CHASE, Bob Mertensotto/CHASE@CHASE
Subject: Enron Natural Gas Marketing/Mahonia/Parco

Rich-

As detailed in the attached file, two weeks ago we received approval from Ron Potter for Chase to "front" a few banks' Prepay **loan** off our balance sheet and place it in "Parco". In addition, we received approval from Richard Cumberland the individual L/C exposure to the said banks.

After speaking with Anthony Coniglio today, I understand that the Asset-Backed group which runs Parco now believes t not be economical for them. They don't believe they will earn sufficient fees for transferring this asset to Parco and that I explained to Anthony the importance for us to transfer assets off of the balance sheet prior to quarter end and that we' this on the balance sheet. He said that we can discuss this with Michael Malter.

Rich, I think we need someone at a higher level to discuss this with Michael Malter. If you need me to help, let me kno

Sandra

Parco96.doc

FOIA Confidential Treatment Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #187o

SENATE
MAH - 02401

Date: Apnl 14, 2002

To: Ron Potter, Portfolio Management

From: Anthony Coniglio, Asset Backed Securities
Jeffrey Dellapina, Commodity Derivatives

Re: PARCO Secured Loan to Mahonia

We have been working on a transaction wherein Mahonia would "refinance" debt raised to purchase a forward sale contract of Oil and Gas. The existing debt would be taken out by the proceeds of a secured loan from PARCO (Chase's asset backed commercial paper conduit). This memo is to request your approval for Chase to front for certain banks currently included in a syndicated letter-of-credit underlying the forward sale contract.

In December, 1996 Mahonia entered into a forward sale contract with **Enron** wherein Mahonia would purchase Oil and Gas over a period of 4 years. Mahonia currently funds this contract with borrowings from Chase. We believe that the secured loan from PARCO would (i) provide Mahonia with a more cost efficient means of funding, and (ii) **remove the funding from Chase's balance sheet.**

The forward sale transaction is structured such that a letter-of-credit is in place to provide 100% credit protection for Mahonia and the lender (currently Chase). The letter-of-credit is syndicated to 24 banks, a number of which are rated below A-1/P-1 by Standard & Poors and Moody's, respectively. PARCO structures its transactions to an "A" equivalent, therefore credit enhancement provided by institutions rated below A-1/P-1 creates a roadblock for a PARCO execution.

We are proposing that Chase front for those institutions rated below A-1/P-1. This would elevate the "credit quality" of the enhancement to a level acceptable to the rating agencies for a PARCO transaction. Listed below are the institutions and their respective commitments:

LTCB of Japan (A-3/P-2)	5.71%	Sanwa Bank (A-2/P-1)	5.71%
IBJ (A-2/P-1)	5.71%	Bank Hapoliam (A-2/P-2)	3.57%
Yasuda Trust (P-3)	3.57%	Gulf International (A-2/P-3)	2.14%
Mitsui Trust (A-2/P-2)	2.14%	Fuji Bank (A-2/P-1)	2.14%
Bank of Yokohama (P-2)	2.14%		

Chase's current position as Arranger is 6.43%. Current face amount outstanding under the forward sale contract is $274,583,044. **We believe that Chase, in its capacity as lender to Mahonia, already has credit exposure to these institutions in their capacity as L/C banks. Furthermore, fronting for these institutions would not result in any incremental credit exposure and would only cause a shift in the form of such exposure (Fronting Bank vs. Lender).**

We addressed, with the Controllers Group, whether or not the structure would raise any potential regulatory issues. They have indicated that they don't believe any such issues would arise and have given us their approval to move forward. Additionally, George Brash has given his approval for PARCO to provide the secured loan.

Please notify us at your earliest convenience, if Chase would front. If you have any questions please do not hesitate to call either Anthony at 834-5130 or Jeff at 834-2033.

FOIA Confidential Treatment Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #187p

SENATE
MAH - 02402

To: Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, George Serice/CHASE@CHASE
From: Richard S. Walker/CHASE
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO
Date: Wed, 15 Nov 2000 23:44:12 GMT

Don't know if you guys have had a chance to do any more brain storming on Joe's $500 MM prepay need. He called this afternoon and clearly he needs this deal.

He suggested the following:

He recognizes the balance sheet pressure we have -- and he has communicated that to Ben Glisan
Given the amount of money that should be coming in off of PGE, Southern Cone, etc in 2001 he thinks that they can give us a pledge that they won't ask for a prepay next.
Recognizing the cost of default swaps right now he propsed the following:

Execute a three year prepay with year one covered by default swaps at today's prices and a covenant by Enron Corp to deliver surety coverage for the balance in one year's time. The thought being that this time next year, we will have had a bunch of run-off that is currently covered by sureties.

I had to cut Joe off because of another call but I think this is a creative way to think -- although if Enron will give us sureties might as well take them now.

A twist on Joe's thought might be

(1) Take the first year's coverage in default swaps
(2) Go ahead and take the sureties now for years two and three
(3) Structure some sort of economic option that would obligate Enron or give Chase the right to replace the sureties for years 2 and three at some later date.

We need to think through #3 to see if it makes any sense.

Jeffrey W. Dellapina
11/15/2000 11:39 AM

To: Richard S. Walker/CHASE@CHASE
cc:
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

I'm trying to reach Rob to follow-up.

Permanent Subcommittee on Investigations
EXHIBIT #187q

FOIA Confidential
Treatment Requested by JPMC

To: Richard S. Walker/CHASE@CHASE
From: Jeffrey W. Dellapina/CHASE
cc: Robert Traband/CHASE@CHASE, George Serice/CHASE@CHASE
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO
Date: Thu, 16 Nov 2000 13:23:20 GMT

Cool - he called yesterday afternoon and I didn't have a chance to engage with him yet.

One note - I had face-to-face with Nick Argirou yesterday and he retested Enron - default swap prices may actually be 10 bps wider than he reported earlier. There appears to be one bank out there which is driving the market higher.

My thoughts:

Cover entire amount with default swaps for year 1.
Obtain termination rights (i.e., acceleration of deliveries) if we can't get comfortable with our exposures. Credit will not likely approve today the additonal insurance coverage.
Pricing remains a huge issue: we'll need substantial compensation for the asset, and more with the future surety coverage. Perhaps we link pricing to the bond spread in the future.

Let's discuss at your earliest convenience.

Richard S. Walker
11/15/2000 06:44 PM

To: Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, George Serice/CHASE@CHASE
cc:
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

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IA Confidential
eatment Requested by JPMC

SENATE
MAH - 06976

had a bunch of run-off that is currently covered by sureties.

I had to cut Joe off because of another call but I think this is a creative way to think -- although if Enron will give us sureties might as well take them now.

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11/15/2000 11:39 AM

To: Richard S. Walker/CHASE@CHASE
cc:
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

I'm trying to reach Rob to follow-up.

FOIA Confidential
Treatment Requested by JPMC

SENATE
MAH - 06977

To: George Serice/CHASE@CHASE
From: Robert Traband/CHASE
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO
Date: Fri, 17 Nov 2000 21:59:55 GMT

George,

As I mentioned in my vms, it looks like the L/c route is really the only viable alternative for a prepay right now. Additionally, I think it would be hugely beneficial if we had one other bank willing to actually fund the prepay with us. Any thoughts? Could you also take a look at the numbers below and verify whether you think they are the right order of magnatude.

Finally, Jeff and I were talking about one other thought. Joe Deffner at Enron had suggested that we get credit coverage from a credit default swap or an l/c for one year and that after one year they would purchase sureties to cover our risk at our option. I see two ways for this to work in the event we don't want the additional surety coverage 1-yr out:

1) we accelerate the prepay if we don't want the surety coverage

2) the l/c is extended for another year. Jeff thought there might be a break on either the l/c fee or up-front fee to the l/c banks under this scenario as they would have a one year deal extendible at Enron's option. If Enron opted to extend, the banks would receive another "extension fee". I told him I didn't think this would change the fees or spread much but would get your thoughts.

Obviously a couple of key outstanding issues would be the impact on bank market capacity as well as the already crowded 1st quarter Enron syndication calendar.

---------- Forwarded by Robert Traband/CHASE on 11/17/2000 03:48 PM ----------
Robert Traband 11/16/2000 10:21 AM

To: Jeffrey W. Dellapina/CHASE@CHASE
cc: Richard S. Walker/CHASE@CHASE, George Serice/CHASE@CHASE
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

The bank syndication alternative would probably look as follows:

Tenor: 3 Years
L/C fee of 50 bps p.a.
Upfront fee to L/C banks 20 bps
Arrangement Fee to GSF: $500,000
Bridge to L/C: 40 bps ($2 million)

Obviously, in addition there would be the imbedded spread and upfront on the prepay.

Jeffrey W. Dellapina
11/16/2000 07:23 AM

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ment Requested by JPMC

To: Richard S. Walker/CHASE@CHASE
cc: Robert Traband/CHASE@CHASE, George Serice/CHASE@CHASE
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

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One note - I had face-to-face with Nick Argirou yesterday and he retested Enron - default swap prices may actually be 10 bps wider than he reported earlier. There appears to be one bank out there which is driving the market higher.

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Pricing remains a huge issue: we'll need substantial compensation for the asset, and more with the future surety coverage. Perhaps we link pricing to the bond spread in the future.

Let's discuss at your earliest convenience.

Richard S. Walker
11/15/2000 06:44 PM

To: Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, George Serice/CHASE@CHASE
cc:
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

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Jeffrey W. Dellapina
11/15/2000 11:39 AM

To: Richard S. Walker/CHASE@CHASE
cc:
Subject: Re: Call Report for ENRON NORTH AMERICA CORPORATIO

I'm trying to reach Rob to follow-up.

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SENATE
MAH - 06980

"MCBRIDE, JAMES R" <JAMES_R_MCBRIDE@fleet.com> on 12/22/2000 03:11:44 PM

To: "GEORGE SERICE (E-mail)" <GEORGE.SERICE@chase.com>
cc:
Subject:

I hope this description is some what close to reality!!

Merry Christmas,
Jim

<<Approval ForumMemo.doc>>

James R. McBride
Managing Director
Fleet Corporate and Investment Banking
713.315.4210 (Direct)
713.315.4222 (Fax)
James_R_McBride@Fleet.com

Approval ForumMemo.doc

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Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #187r

SENATE
MAH - 02302

To: Loan Forum

From: James R. McBride and Jill A. Calabrese

Date: December 20, 2000

Re: Project Mahonia - $330 Million Forward Sale Natural Gas Contract
Enron Financing Objectives

On December 18, 2000, Debt Capital Markets received approval to purchase up to a $167 million interest in a natural gas contract. That contract requires Enron North American to make future deliveries of natural gas. Today, Financial Institutions is seeking to establish or increase certain credit limits for Travelers, St. Paul, Lumbermen's, Hartford, and Safeco to support this transaction. These clients will issue surety bonds to guarantee Enron's performance under the natural gas contract. This memo is written in support of Financial Institutions' request and is intended to provide a brief overview of Enron's financing objectives. While we expect Enron to make the required deliveries, it is important to note that the Enron performance risk is specifically assumed by the surety bond providers. If Enron North America fails to deliver gas and Enron Corp fails to pay, the insurance companies are obligated to pay liquidated damages.

Transaction Overview from Enron's perspective:
Enron North America ("ENA") plans to enter into a $330 million forward sale gas contract with an off-balance sheet, special purpose vehicle created by Chase, Mahonia Natural Gas Limited. Under the terms of the agreement Enron North America will receive an up front payment of $330 million, which will be funded by Fleet and Chase. Enron will be obligated to deliver to Mahonia specified volumes of natural gas (84 Bcf) at specified times and at specified locations. (Please note Fleet will not be taking any mark to market gas risk or physical delivery risk. See the Debt Capital Markets Approval Memo for a more complete description of the Mahonia transaction). Separate and apart from the Mahonia transaction, Enron will enter into a commodity price swap that will fix Enron's future cost of purchasing and delivering the scheduled gas volumes.

Enron's financing objective in completing this transaction is as follows:
Enron is attempting to match its "book income" and "cash flow." As a derivatives and commodity trader, Enron uses "mark to market" accounting practices to account for its price risk management contracts. Consequently, when Enron closes a derivative transaction, whether physical or financial, it is required by accounting practice to mark to market (on a daily basis) the expected income or loss it will incur over the life of the transaction. However, from a cash flow standpoint, it will actually receive or make payments of cash over the life of the contract. On September 30, 2000, Enron had a positive net asset position of over $1.2 billion in its price risk management books.

Enron has historically managed to monetize its "in the money" position by completing either physical or financial forward sales. The Mahonia transaction will allow Enron to receive cash upfront. Subsequently, Enron will use the future cash flows it expects to receive under its existing price risk management contracts to pay for the gas it will be required to deliver under the Mahonia contract. The scheduled deliveries under the Mahonia contract are designed to approximately match Enron's expected receipts of cash (or volumes) under its existing contracts.

The accounting impact on Enron's financial statement is as follows:
Enron is not taking this transaction into earnings. Enron will account for their $330 million liability under the Mahonia Forward Sale Contract as an increase to its "Liability from Price Risk Management Activities." As September 30, 2000 Enron had total assets from price risk management activities of $14.7 billion and total liabilities from price risk management activities of $13.5 billion, for a net asset position of $1.2 billion

SENATE
MAH - 02303

FOIA Confidential Treatment
Requested by JPMC

Peter M. Licalzi 04/21/99 11:00 AM

Oil & Gas Structured Transaction Management (713) 216-8869 Fax Number: (713) 216-4117

To: Richard S. Walker/CHASE@CHASE
cc: Bruce Ellard/CHASE@Chase, Michael P. Golden/CHASE@CHASE, Robert Traband/CHASE@CHASE, Bob Mertensotto/CHASE@CHASE
Subject: Mahonia Ltd.

Rick:

Chase global derivatives desk in NY is attempting to reissue a letter of credit in favor of Texas Gas Transmission for the benefit of Mahonia Ltd.
As I understand the transaction, this LC is to support a Gas Delivery in connection with the Enron Prepaid.

The beneficiary on this transaction is pressuring Chase through Mahonia to have the LC issued or they will call in the LC.

Previously the exposure was booked against Enron liability without any outright support or knowledge from Enron.

From a legal standpoint I am not sure whether we can utilize Enron exposure or legally the Bank needs to extend a line to Mahonia Ltd to support these underlying transactions to the various pipeline beneficiaries.

Theis particular LC is approximatley $100M and I believe there are about a half dozen similar transactions to be reissued.

Please let me know if you recollect these transactions and how to proceed with this particular one?

Thanks&Regards
Peter

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Permanent Subcommittee on Investigations
EXHIBIT #187s

SENATE
MAH - 02618

Jeffrey W. Dellapina
04/23/99 11:27 AM

To: Gary K. Wright/CHASE@CHASE
cc: Peter M. Licalzi/CHASE@CHASE, Robert Traband/CHASE@CHASE, Bruce Ellard/CHASE@Chase
Subject: Mahonia Limited

Per our discussion, I am requesting approval to issue an LC for the account of Mahonia in favor of Texas Gas Transmission Co. Mahonia, a special purpose company which works exclusively on Chase arranged transactions, is required to post a small SBLC in favor of the pipeline to cover obligations that may arise, i.e., pipeline fees, costs associated with imbalances, etc. Chase had issued an LC under the exact same terms several years ago; however, this was inadvertantly allowed to expire last fall.

The tenor will be 1 yr with an evergreen provision (i.e., extensions are at Chase discretion). The amount requested by Texas Gas is $100,000.

As I discussed, Global Commodities accepts economic responsibility for any unforeseen drawings.

Please request Peter to issue this LC by Monday at the latest.

FOIA Confidential Treatment
Requested by JPMC

[redacted]
Gary K. Wright
[redacted]

Credit 713 216 4328 Fax Number 713 216 5570

To: Peter M. Licalzi/CHASE@CHASE
cc: Jeffrey W. Dellapina/CHASE@CHASE, Robert Traband/CHASE@CHASE, Bruce Ellard/CHASE@Chase
Subject: Mahonia Limited

The request to issue a $100,000 LC for the account of Mahonia favor of Texas Gas Transmission is approved.

---------- Forwarded by Gary K Wright/CHASE on 04/23/99 11 36 AM ----------

Jeffrey W. Dellapina
04/23/99 11:27 AM

To: Gary K. Wright/CHASE@CHASE
cc: Peter M. Licalzi/CHASE@CHASE, Robert Traband/CHASE@CHASE, Bruce Ellard/CHASE@Chase
Subject: Mahonia Limited

Per our discussion, I am requesting approval to issue an LC for the account of Mahonia in favor of Texas Gas Transmission Co. Mahonia, a special purpose company which works exclusively on Chase arranged transactions, is required to post a small SBLC in favor of the pipeline to cover obligations that may arise, i.e., pipeline fees, costs associated with imbalances, etc. Chase had issued an LC under the exact same terms several years ago; however, this was inadvertantly allowed to expire last fall.

The tenor will be 1 yr with an evergreen provision (i.e., extensions are at Chase discretion).
The amount requested by Texas Gas is $100,000.

As I discussed, Global Commodities accepts economic responsibility for any unforeseen drawings.

Please request Peter to issue this LC by Monday at the latest.

FOIA Confidential Treatment
Requested by JPMC

From: Ian James
To: esseg
Date: 3 November 1997 3:24pm
Subject: Mahoniia/New Enron Transaction

Just to let you know that I have been speaking to Jeff Delapina regarding an arrangement whereby the Mahonia funding would come from a commercial paper issuer (like the M&M transaction) rather than being on balance sheet for Chase. It will have to be completed by Christmas (again)! This would involve Mahonia giving security over its receivables from Enron to the CP issuer.

M

vSubcommittee on Investigations
EXHIBIT #187t

Chase Investment Bank Limited
P.O. Box 16, Woolgate House
Coleman Street, London EC2P 2HD

Telephone:

CHASE

Ian James esq
Mourant du Feu & Jeune
18 Grenville Street
St Helier
Jersey

14th December 1992

Dear Ian,

I enclose a brief description of a structure we are proposing to discuss with a potential client. In many ways the structure resembles the transactions we have undertaken with Westash Limited but in order to be certain that we have not created any new pitfalls for the Jersey SPC, I would be grateful if you could review the transaction and give me your preliminary views.

At this stage we have not identified a specific Jersey company which could undertake the role of the SPC as described. Once we have resolved the structuring issues, of which there are many at this stage, I will be writing again to ask you to nominate such a company.

Kind regards

Yours sincerely

Mark Webster

Registered in England no. 248609 at Woolgate House, Coleman Street, London EC2P 2HD Member of SFA
Member of The London Stock Exchange

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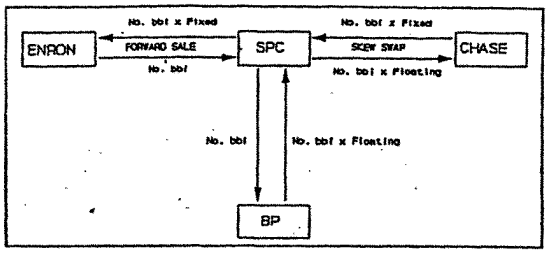
Permanent Subcommittee on Investigations
EXHIBIT #187u

ENRON STRUCTURE



Settlement Period	No. Barrels	Floating Price	Fixed Price
1	2,500,000	WTI	$40/barrel
2 - 13	385,000	WTI	$10.5/barrel

Assume that WTI = $20/barrel for life of transaction. This means that the first settlement amount will be 2.5MM x (40-20) = US$ 50MM (Chase pays SPC, SPC pays Enron).

Description of Structure

1. SPC enters into a skewed swap with Chase such that Chase pays fixed and receives floating. The fixed rate for the first settlement will be $20 higher than the floating price such that the first settlement will be for $50MM payable by Chase to the SPC. There will be 13 subsequent monthly settlements and the fixed price for these will be $10.5 which will almost certainly result in settlement by the SPC to Chase. The number of barrels and settlement prices are shown in the table above. The floating price will be based on WTI.

2. SPC enters into a physical forward oil sale agreement with Enron pursuant to which Enron sells oil to the SPC. The numbers of barrels, payment basis and due dates exactly match the skew swap between Chase and the SPC.

3. The SPC enters into a physical forward oil sale agreement with an oil producer, shown as BP in this example. Pursuant to this agreement BP agrees to buy oil from the SPC in amounts and dates matching the purchase by the SPC from Enron. The price paid will be based on WTI.

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4. On each settlement, transfer of title in the oil from the SPC to BP will only become effective once BP has paid the purchase price in cash to the SPC's bank account at Chase. Should this payment not take place, the title will remain with the SPC and the SPC will either sell it in the market or, preferably, have the right to sell it back to Enron at the floating price.

Other Issues

The following is a list of the other main issues for consideration:

- Security Structure - Protect Chase from SPC risk
  Protect BP from SPC risk
- Environmental Issues - can we avoid the risks associated with the SPC's momentary ownership of oil, or can we live with these risks.
- Tax issues - opinions
  US withholding tax on oil payment by Enron if transaction is reclassified into loan.
- Timing
- Costs - Opinions
  BP
  Jersey
- Documentation - Oil title documents
  Security documentation
  Swap documentation
  Physical forward oil sale by Enron to SPC
  Physical forward oil sale by SPC to BP
- Delivery - Where is the physical oil located
- Jersey SPC - Owned by Jersey charitable trust
  Trust administered by Jersey law firm
  Contact with Jersey law firm to be coordinated by Mark Webster.

GEC1/222648-1.AA M

MAHONIA LIMITED

MINUTES OF THE FIRST MEETING OF DIRECTORS OF THE COMPANY HELD AT 18 GRENVILLE STREET, ST. HELIER, JERSEY, CHANNEL ISLANDS ON THE 29TH DAY OF DECEMBER 1992.

PRESENT:

Mr. R.F.V. Jeune
Mr. I.C. James

CHAIRMAN OF THE MEETING:

1. Mr. R.F.V. Jeune was appointed Chairman of the meeting.

REGISTRATION OF MEMORANDUM AND ARTICLES OF ASSOCIATION:

2. IT WAS NOTED that the Memorandum and Articles of Association of the Company were registered on the 16th day of December 1992 under company number 54172.

DIRECTORS:

3. IT WAS PLACED ON RECORD that, in accordance with Article 99 of the Company's Articles of Association, the Subscribers to the Memorandum had appointed the following as the first Directors of the Company:

Richard Francis Valpy Jeune
Ian Colin James

and acceptances of the appointments were presented to the Meeting.

CHAIRMAN OF THE COMPANY:

4. IT WAS RESOLVED that Mr. I.C. James be and is hereby appointed Chairman of the Company.

SECRETARY OF THE COMPANY:

5. IT WAS RESOLVED that Mourant & Co. Secretaries Limited be and is hereby appointed Secretary of the Company.

SEAL OF THE COMPANY:

6. THE SEAL of the Company was produced (an impression of which appears in the margin hereof) and IT WAS RESOLVED that the same be deemed to have been duly affixed if affixed in accordance with Article 121 of the Company's Articles of Association.

CS

REGISTERED OFFICE:

7. IT WAS RESOLVED that the Registered Office of the Company be moved to 5 Little Green Street, St. Helier, Jersey, Channel Islands and that the Secretary be authorised to sign the Notice of change of Registered Office to be given to the Registrar of Companies as required by Law.

Permanent Subcommittee on Investigations
EXHIBIT #187v

M

GEC1/22268-1.AA

ISSUE OF SHARES:

8. IT WAS RESOLVED that the following shares of £1 each be issued to the Subscribers to the Memorandum of Association of the Company and the shares be credited for all purposes as fully paid up:

Name of Subscriber	Number of Shares	Share Numbers
Juris Limited	5	1-5 inclusive
Lively Limited	5	6-10 inclusive

SHARE CERTIFICATES:

9. IT WAS RESOLVED that Certificates in respect of the above minuted shares should be duly executed and sealed.

REPRESENTATIVES:

10. IT WAS NOTED that pursuant to the Articles of Association of the Company, Juris Limited and Lively Limited had by resolution of their respective directors authorised any signatory on the list of signatories known as the "Mourant & Co. Standard Signatory List" as shall be varied from time to time to act as their representative at any Meeting of the Company.

ANNUAL GENERAL MEETING:

11. IT WAS NOTED that all the Shareholders had agreed to dispense with the requirement to hold Annual General Meetings of the Company and the agreement duly signed by them was presented to the Meeting.

BANKING ARRANGEMENTS:

12. An account form to enable the Company to open a bank account with The Chase Manhattan Bank N.A. (the "Bank") of P.O. Box 16, Woolgate House, Coleman Street, London EC2 was presented to the Meeting and IT WAS RESOLVED that the Bank be appointed as bankers to the Company and that an account be opened with the Bank styled "Mahonia Limited" and IT WAS FURTHER RESOLVED AS FOLLOWS:-

(a) to pass the resolutions set out in the account opening form and that they be deemed to form a part of these Minutes; and

(b) powers to sign on the Company's Bank Mandates and operate the Company's bank accounts on behalf of the Company are as follows:-

(i) for routine and internal transactions such as fixing deposits, and transfers between accounts in the same name or designation and not involving payment away to third parties - any one signature on the Company's signatory list.

(ii) for all payments away to third parties, deliveries of scrip and any commitments - two signatures on the Company's signatory list, provided at least one is an "A" signatory

SIGNATORY LIST:

13. For the purposes of administering the affairs of the Company the signatory list referred to in the preceding paragraphs shall be the list of signatories known and referred to as the "Mourant & Co. Standard Signatory List", as shall be varied from time to time.

AUDITORS:

14. IT WAS RESOLVED that appointment of Auditors to the Company be deferred.

ACCOUNTING DATE:

15. IT WAS RESOLVED that the Accounts of the Company shall be prepared as at 31st December in each year

EXEMPT COMPANY STATUS:

16. IT WAS RESOLVED that the Company should make application to the Comptroller of Income Tax to be granted the status of an Exempt Company for the purposes of Jersey income tax.

IT WAS FURTHER RESOLVED that subject to the appropriate confirmations having been given to them, any officer of Mourant & Co. Secretaries Limited be and is hereby authorised to sign on behalf of the Company the exempt company application form each year.

TERMINATION:

17. There being no further business to discuss the Meeting was terminated.

.....
Chairman

GEC1/22268-1 M

MAHONIA LIMITED

ANNUAL GENERAL MEETINGS

Pursuant to the provisions of Article 87 of the Companies (Jersey) Law 1991 we, being all the shareholders of the Company being a private company hereby agree to dispense with the requirement to hold future Annual General Meetings.

.....
For and on behalf of
JURIS LIMITED

.....
For and on behalf of
LIVELY LIMITED

Dated: 29th December 1992

M

GEC1/22268-1.AC

MAHONIA LIMITED

We, the Subscribers to the Memorandum of Association of the Company in accordance with Article 99 of the Company's Articles of Association, hereby appoint the following as the First Directors of the Company:

Richard Francis Valpy Jeune
Ian Colin James

.....
For and on behalf of
JURIS LIMITED

.....
For and on behalf of
LIVELY LIMITED

29-11-92

GEC1/22268-1.AB M

MAHONIA LIMITED

I, RICHARD FRANCIS VALPY JEUNE, hereby accept office as a director of the Company.

Signed this 29th day of December 1992

.....
RICHARD FRANCIS VALPY JEUNE

M

Mourant & Co. Trustees Limited
as trustees of the Eastmoss Trust,
18 Grenville Street,
St. Helier,
Jersey.

29 December, 1992

Our ref: GEC1/22268-1.AF

Dear Sirs,

Re: Mahonia Limited

We hereby declare that subject to our terms and conditions:-

1. The shares (the "Shares") of the above named Company are registered in our names as follows:

Juris Limited	5 Shares numbered 1 to 5 of £1 each.
Lively Limited	5 Shares numbered 6 to 10 of £1 each.

2. The Shares are held for you absolutely.

3. The Shares will not be voted, transferred, dealt with or disposed of except in accordance with your written directions.

4. We will account to you for all dividends and profits which may be paid to us in respect of the Shares.

Yours faithfully,

.....
For and on behalf of
JURIS LIMITED

.....
For and on behalf of
LIVELY LIMITED

GEC1/22268-1.AE M

To: Juris Limited, and
Lively Limited
18 Grenville Street
St Helier
Jersey
Channel Islands

Dear Sirs

Mahonia Limited

We, the undersigned, hereby instruct you to take the necessary action to dispense with the requirement to hold Annual General Meetings of the Company as from the date of incorporation until further notice.

Yours faithfully

.....
Authorised Signatory
MOURANT & CO. TRUSTEES LIMITED
as trustees of the Eastmoss Trust

Dated day of December 1992

M

States of Jersey

COMPANIES (JERSEY) LAW 1991

Certificate of Incorporation of a Limited Company

Registered Number 54172

I HEREBY CERTIFY THAT

MANCHIA LIMITED

is this day incorporated as a private company under the Companies (Jersey) Law 1991

Dated this 16th day of December 199 2

Deputy Registrar of Companies

Cert 1.

Permanent Subcommittee on Investigations
EXHIBIT #187w

M

States of Jersey

Financial Services Department

Cyril Le Marquand House, P.O. Box No. 267, The Parade, St. Helier, Jersey JE4 8TZ. Tel: (0534) 603000 Fax: (0534) 89155.

- 54172

16th December 1992

On the basis of the information supplied to the Financial Services Department, CONSENT IS HEREBY GRANTED, pursuant to the Control of Borrowing (Jersey) Order, 1958, as amended to

MABONIA LIMITED

to issue up to 10,000 shares of nominal value

of £1.00 each.

For and on behalf of the
Finance and Economics Committee

Deputy Director

Director: Richard C.A. Syvret, F.C.I.S., F.C.C.A.

MARCNIA

LIMITED ✓ ~~LTD~~

CHECK M✓

MEMORANDUM Ss.	✓
SHARE CAPITAL £10,000	✓
ARTICLES Ss.	✓
SUBSCRIBERS CORP — MEMO. ✓ ARTS. ✓	✓
REGISTERED OFFICE 18 Grenville Street — Statement of Particulars	✓
APPLICATION ✓ (Jens) + Schedule of Eastmoss Cos.	✓ ✓
CHEQUE FORM ✓ RECEIVED	FILE FORM ✓ RECEIVED 22268/1 — 16/6 15/7

M

Makonia LIMITED

Authorised Share Capital		£
£10,000	Judicial Fee	110
	Treasury Duty (½%)	50
	Total Cheque	160

INFORMATION FROM CORPORATE DEPARTMENT

Co. for Eastmon Trust
& Chase Bank
— JSV

JV1/22268/1 M

COMPANIES (JERSEY) LAW 1991

STATEMENT OF PARTICULARS ON INCORPORATION

NAME OF COMPANY: PROVISIONAL NO.: CP 7606

MAHONIA LIMITED

INTENDED REGISTERED OFFICE ADDRESS:

18 Grenville Street,
St. Helier,
Jersey JE4 8PX.

STATUS OF COMPANY	Public	☐
	or Private	☑
STANDARD TABLE ADOPTED	Yes	☐
	Part Only	☐
	No	☑

SIGNATURES
of Subscribers
or their agent .....

Agent's Name Mourant du Feu & Jeune

Mourant & Co.
TRUSTEES LIMITED

P.O. Box 87, 18 Grenville Street, St. Helier, Jersey JE4 8PX, Channel Islands
Tel: 0534 609000
Fax: 0534 609333
Telex: 4192064
International
Tel: +44 534 609000
Fax: +44 534 609333

M. Webster, Esq.
Chase Investment Bank Limited,
P.O. Box 16,
Woolgate House,
Coleman Street,
London EC2P 2HD

26 November, 1993

Our ref: GEC1/22268-2.02, 22218.4, 16759-4

FILED UNDER SEAL

Dear Mark,

Re: Percolin Limited / Stoneville Aegean Limited - MG Transaction
Mahonia Limited / Stoneville Aegean Limited - Enron II Transaction

I have (finally) got around to raising invoices in respect of the Enron II and MG transactions which are attached for your review.

Regarding the Enron II Transaction I have raised a single invoice for Mahonia Limited in the amount of £10,150.00 which equates to the agreed budget of US$15,000 for both Companies. This includes the amount of our incorporation bill raised against Mahonia Limited (£1,006.33) and a paid disbursement amount of £1,000.00 which breaks down as £500 in respect of the 1993 Exempt Tax Liability of Mahonia Limited which was paid on behalf of the Company by the Eastmoss Trust and a charitable profit of £500. The legal cost figure of £1,000 when added to the legal cost figures reflected on the invoice raised against Percolin Limited in respect of the MG Transaction (see below) and the separate invoice for additional legal costs addressed to Robert Miller adds up to the total of £7,000 outstanding in respect of Mourant du Feu & Jeune's legal costs incurred and outstanding for both transactions.

The invoice raised against Percolin Limited in respect of the MG Transaction in the amount of £12,150.00 again equates to the approximate budget we had discussed of US$18,000 for both Companies. Again the legal costs arising in respect of the incorporation of the Company are included, representing £415.65 of the paid disbursements amount of £915.65. The balance of this amount (£500) represents a charitable profit element. I have also included a provision on the bill for the 1993 Exempt Tax Liability which is now payable.

HIGHLY CONFIDENTIAL

Permanent Subcommittee on Investigations
EXHIBIT #187x

After including all items shown on the Mahonia Limited and Percolin Limited invoices I was left with an excess of costs over the US Dollar budgets we had discussed of £2,821.64 which represents the balance of Ian's legal time spent in respect of both transactions. As we discussed I have raised this in the form of a separate bill marked for the attention of Robert Miller.

When you have had a chance to review the enclosures please could we discuss any comments you may have so that I could arrange for a final invoicing in respect of both transactions.

Kind regards,

Yours sincerely,
For and on behalf of
Mourant & Co. Trustees Limited

Authorised Signatory

FILE COPY

HIGHLY CONFIDENTIAL

16759/4

: Accounting
wide (Timer2(v 10.0))

Client : 16759L Stoneville Aegean Limited
Stoneville Aegean Limited

User : GEC
Date : 24/11/93
Time : 12:02 PM
PAGE : 2

DI2 Group 12
GEC Gareth Essex-Cater

Bill No \ Date

Interim
Final

Name	Latest time	Units	Rate	Value	Future £	Cfwd £	Total	Bill	Profit
M Record Units only									
FEES T & M Fees	1/10/92	1,000	NIL	NIL					
t from 0/ 0/ 0 to 23/11/93 inclusive.		1,000		NIL					
counts Preparation									
GEC Gareth Essex-Cater	25/ 6/93	44	10.5	440.00					
t from 3/ 1/92 to 23/11/93 inclusive.		44		£ 440.00					
mpany & Trust Administration									
CDE Carmel Davitt Egan	13/ 8/93	3	4.2	11.25					
GEC Gareth Essex-Cater	22/10/93	338	10.5	3,418.50					
ICJ Ian Colin James	8/10/93	5	23	114.50					
JHL Jean Mary Lee	14/ 7/93	66	10.5	528.00					
PAS Paul Skittrall	15/10/93	7	7.7	53.90					
SAFE Safe Custody (Time Recordin	1/ 7/93	1	3.5	3.50					
t from 31/12/92 to 23/11/93 inclusive.		420		£ 4,129.65					
otocopying Charges									
PCOPY Photocopy (Disbursemen	1/ 8/93	NIL	(1)	3.20					
t from 31/12/92 to 23/11/93 inclusive.		NIL		£ 3.20					
tstanding Disbursements									
OUTDSB Outstanding Disbursements	13/ 7/93	NIL	(1)	63.50					
t from 3/ 1/92 to 23/11/93 inclusive.		NIL		£ 63.50					
stmile Charges									
FAX Fax (Disbursements)	1/ 8/93	NIL	(1)	63.00					
. from 31/12/92 to 23/11/93 inclusive.		NIL		£ 63.00					
ephone Charges									
PHONE Telephone (Disbursements	2/ 7/93	NIL	(1)	6.83					
from 31/12/92 to 23/11/93 inclusive.		NIL		£ 6.83					

DATE: 26/11/93
INITIALS: (4706:18)

type to be billed CODE = NBIC

CODE = _____

1362

HIGHLY CONFIDENTIAL

ccounting
de [Tinter2(v 10.03]

012 Group 12
GEC Gareth Essex-Cater

Client : 1675906 · Stoneville Aegean Limited
Stoneville Aegean Limited

User : GEC
Date : 24/11/93
Time : 12:02 PM
PAGE : 3

Bill No | Date | Interim | Final

Name	Latest time	Units	Rate	Value	Future £	Clwd £	Total	Bill	Profit
		1,464		£ 4,706.18					

nd Debtors entry for Client

Summary of Bill 4282 Dated 31/12/92

Units	Billed	P/(L)	Carried Fwd	Job
NIL	1,004.14	1,000.00	NIL	ZTEL
NIL	4.25	NIL	NIL	ZFAX
NIL	2.55	NIL	NIL	ZCOP
205	1,865.10	NIL	NIL	ADMN
NIL	NIL	NIL	NIL	
205	2,876.04	1,000.00	NIL	TOTALS

Analysis of historical profitability.

Year	Units	Billed	%Recovery
93	NIL	NIL	Inf
92	397	7,569.74	212.05
91	2	4,258.70	116.65

Please transfer all wip and disbursements to Mahonia Ltd (4706·18) (22268/2) : one bill to raised in respect of deal 'ENRON II' participated in by both Companies.

Next Bill Date
31-12-94
Perhaps 31/12/94?
31/12/93 Annual

Annual

TTD.

Approved by

25/11

Gareth Essex Cater

HIGHLY CONFIDENTIAL

ccbunting
da CTinter2(v 10.03

012 Group 12
GEC Gareth Essex-Cater

Client : [redacted] Ironsville Aegean Limited-M2 transaction

P O Box [redacted]
18 Grenville Street
St Helier
Jersey JE4 8PX

16759 | + ©

User : JEM
Date : 5/10/93
Time : 9:56 AM
PAGE : 209

Bill No	Date	Interim	
		Final	

Name	Latest time	Units	Rate	Value	Future £	Cfwd £	Total	Bill	Profit
serv & Trust Administration									
GEC Gareth Essex-Cater	3/ 9/93	20	10	200.00					
from 0/ 0/ 0 to 30/ 9/93 inclusive.		20		£ 200.00		200			
type to be billed CODE =									
CODE =									
s		20		£ 200.00		200			

ad Debtors entry for Client

Units	Billed	P/(L)	Carried Fwd	Job
NIL	NIL	NIL	NIL TOTALS	

Analysis of historical profitability.

Year	Units	Billed	%Recovery

Next Bill Date: 30/12/93 Monthly

Approved by

Carry Forward - but to be raised in November

Gareth Essex Cater

DATE 26/11/93

1364

HIGHLY CONFIDENTIAL

Accounting
wide CTintar2(v 10.01)

012 Group 12
GEC Gareth Essex-Cater

Client : 16759 Stoneville Aegean Limited-MG transaction

P O Box 87
18 Grenville Street
St Helier
Jersey JE4 8PX

User : JEM
Date : 4/11/93
Time : 10:13 AM
PAGE : 242

16759/6

Bill No | Date | Interim | Final

Name	Latest time	Units	Rate	Value	future £	Clvd £	Total	Bill	Profit
Agency & Trust Administration									
GEC Gareth Essex-Cater	3/ 9/93	20	10.5	200.00					
il from 0/ 0/ 0 to 31/10/93 inclusive.		20		£ 200.00					
* type to be billed CODE = TT1									
CODE =									
. 8		20		£ 200.00					
lled Debtors entry for Client									

Units	Billed	P/I/Li	Carried fwd	Job
NIL	NIL	NIL	NIL TOTALS	

Analysis of historical profitability

Year	Units	Billed	%Recovery

Please transfer all WIP (£200) to Percolin Limited (22210/4) : one bill to be raised in respect of the 'MG' transaction participated in by both Companies. This matter will be terminated when invoice paid.

Gareth Essex-Cater

Next Bill Date
31.12.93
Perhaps 9/10/93?
9/ 9/93 Monthly
Quarterly

Approved by

25/11

DATE: 25/11/93
INITIALS: ...

File Note

CLIENT NAME: Mahonia Limited - Enron IV Transaction

CLIENT MATTER: 22268-2.93

REF: GEC

DATE: 23rd November, 1995

Telephone conversation with Mark Webster of CIB.

Mark referred to the large pile of gas transmission contracts we would have received for signature by Mahonia in the last day or two. He said that he hoped this would be the last significant pile of papers requiring our attention: all future administration matters should be dealt with by Chase as our agents. I mentioned the concerns that the Directors of Mahonia had expressed about the contents of the various agreements they had been asked to sign and their concern that it had not been clearly stated by the agents that these documents had been reviewed, vetted and approved by them. Mark confirmed that this was the case and asked that I pass that confirmation on to the directors.

By way of background MW spoke about why this transaction had been chosen to use natural gas as the underlying commodity rather than, as in the past, crude oil. The rationale of these transactions is to produce an income flow for Enron and for their relevant tax purposes it is important that this flow of income be deemed as resulting from the sale of inventory rather than from trading. The present structure permits the funds flowing to Enron to be treated in this manner. Apparently it was deemed that the large transactions previously completed ment that it was more difficult to justify a flow of income from further transactions representing a sale of inventory and for that reason, (and because Enron are a major natural gas producer) it was decided to connect the current transaction to natural gas as a commodity rather than oil.

Permanent Subcommittee on Investigations
EXHIBIT #187y

ADMINISTRATION NOTES

25/26 AUGUST 1999

For Registry and Matter Numbers Consult the GEC Client List

The Chase Manhattan Bank SPV Group ("Stoneville" Companies):

The Eastmoss Trust
The Lion Trust

- Stoneville Huron Limited
- Stoneville Topaz Limited
- Stoneville Caspian Limited
- Stoneville Adriatic Limited
- Stoneville Timor Limited
- Stoneville Aegean Limited
- Grand Status Limited
- Gothia Finance Limited
- Goldvale Finance Limited
- Wellsgate Limited
- Tunwell Limited
- Mahonia Limited
- Comatus Limited
- Axmouth Limited
- Kilwood Limited
- Ahona
- Thornaby Limited
- Raylex Limited
- Percolin Limited
- Westash II Limited

and administered by other individuals on Group 12:

- CRV Finance Limited
- CABCO Limited
- Molland Leasing (CI) Limited
- Vista Distributors Limited
- Thetford Limited
- Youngstar Limited
- Baobab Limited
- Whiterift Limited
- Melworth Limited
- Pitminster Limited
- Borders Limited
- Lockwell Limited
- Linkton Limited
- London Diversified Limited
- Celltone Limited

Permanent Subcommittee on Investigations
EXHIBIT #187z

The Chase Manhattan Bank One Chase Manhattan Plaza, New York, NY 10081

Chase Securities, Inc.

Date:

Number of pages including cover sheet:

To Rick Walker
713-751-9122

Phone:

Fax phone:

CC:

From: John Serice

Phone: (212) 552-6620

Fax phone: (212) 552-7625

REMARKS: ☐ Urgent ☐ For your review ☐ Reply ASAP ☐ Please comment

Permanent Subcommittee on Investigations
EXHIBIT #187aa

The Eastmoss Trust

Mourant & Co Trustees Limited, the Jersey resident trustees to the Eastmoss Trust ("Eastmoss") have verbally confirmed the following details with respect to the Eastmoss. (Mourant & Co Trustees Limited is wholly owned by the Jersey law firm, Mourant du Feu & Jeune).

Eastmoss was set up in 1986 for charitable purposes. Its trustee, Mourant & Co Trustees Limited, is located at 18 Grenville Street, St Helier, Jersey. Eastmoss currently owns approximately 30 special purpose Jersey resident companies all of which are involved in transactions offered to Eastmoss by Chase. Eastmoss agrees a fee for allowing its companies to participate in transactions brought to it by Chase. Participation in such transactions is done on arm's length terms. Profits generated by the companies are paid as dividends to Eastmoss and dispersed to various charities from time to time as determined by the trustees.

Mahonia Limited

Mahonia Limited ("Mahonia") is a Jersey registered company with nominal equity capital. Its stock is wholly owned by a Jersey charible trust called Eastmoss. The trust is administered by Mourant & Co Trustees, the trust arm of Jersey's largest law firm, Mourant du Feu & Jeune. Directors of Mahonia are also provided by Mourant du Feu & Jeune. (Mourant is also Chase's Jersey legal counsel.)

Mahonia's only business activity is the transacting of physical oil transactions and related hedging, financing and security agreements. It has only entered into transactions brought to it by Chase. It has appointed Chase as its agent for the puposes of managing all matters related to the physical oil contracts entered into with Enron Corp and its subsidiaries.

M

CHASE
THE CHASE MANHATTAN BANK
LEGAL DEPARTMENT
270 Park Avenue, 40th Floor
New York, New York 10017
Telecopier No. (212) 270-7368

M. du F. & J.
20 DEC 2000
SIGN BY
PASSED TO

CONFIDENTIALITY NOTICE

This facsimile message is intended only for the use of the individual or entity named below and contains information which is confidential, non-public or legally privileged. Any dissemination or distribution of this message other than to its intended recipient is strictly prohibited. If you have received this message in error, please notify us by telephone immediately and return the original message and all copies to us at the above address by mail.

FACSIMILE MESSAGE COVER SHEET

TO: Julie Carter
Mahonia

FROM: Philip Levy

PHONE: (212) 270-5951

DATE: December 20, 2000

Number of Pages Transmitting (including Cover Sheet): 07

Telecopy Destination - Phone Number: 011-44-1534-609333

RE: Stoneville Aegean Board of Directors Minutes in connection with Enron-Mahonia transaction

Following please find a copy of the above-referenced documents marked to indicate my comments. I have reviewed the draft minutes of Mahonia Natural Gas Limited and while the ultimate documentation is still being worked out, I would note that the minutes regarding the purchase of gas from ENA did not identify and approve the Margin Agreement and the Enron Guarantee. These minutes should be substantially similar to the minutes from the last Enron-Mahonia transaction. (I would further note that the total amount of the transaction has been reduced to $330,000,000). Finally, there will only be two Purchasers of the natural gas from Mahonia, Chase and another financial institution.

271951:v01

DEC.20'2000 05:13 212 270 7268 CHASE LEGAL 805/005

Permanent Subcommittee on Investigations
EXHIBIT #187bb

M.

The board minutes reflecting this transaction anticipates three purchasers (which was the thought when the term sheet was prepared.)

First draft of the Enron-Mahonia Natural Gas documents have been emailed to you. We will forward the other documents as soon as they have been completed.

Please call me should you have any questions.

As always, your assistance is greatly appreciated.

ZTTHSLW08

DEC.20'2006 09:14 212 270 7298 CRAVE LEGAL 8059E P.002/002

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STONEVILLE AEGEAN LIMITED

MINUTES OF A MEETING OF DIRECTORS OF STONEVILLE AEGEAN LIMITED HELD AT 22 GRENVILLE STREET, ST HELIER, JERSEY, C.I. ON THE [] DAY OF DECEMBER, 2000.

Present: Ian James
Richard F.V. Jeune

Chairman:

1. Mr I James was appointed Chairman for the purpose of the Meeting.

Minutes:

2. The Minutes of the previous Meeting of Directors were read and approved having been signed by the Chairman of that Meeting.

Financing Transactions:

3. The Chairman noted that the Company has been invited to enter into financing transactions involving, inter alia, the purchase by the Company of quantities of natural gas from The Chase Manhattan Bank ("Chase") on a prepaid basis. (pursuant to a fixed price forward transaction)

The Chairman noted that in order to give effect to the transactions referred to above the Company proposed to enter into, issue or accept as the case may be:

(a) A Fixed Price Forward Contract (the "~~Second Offtake~~ (Chase Fixed Price Forward) Agreement") to be made between the Company and Chase whereby Chase will agree to sell to the Company and the Company will agree to purchase from Chase quantities of natural gas at the times, in the quantities, with the specifications and upon the terms and conditions therein specified.

(b) A Margin Agreement (the "Stoneville Margin Agreement") to be made between the Company and Chase whereby the Company will agree to post collateral with Chase in an amount equal to the excess (if any) of the purchase price of the gas to be delivered under the ~~Second Offtake~~ Agreement over the marked to market value of the remaining natural gas to be delivered under the ~~Second Offtake~~ (Chase Fixed Price Forward) Agreement.

IT WAS UNANIMOUSLY RESOLVED that:-

(a) the Company:-

DEC.20'2000 09:44 212 270 7288 CHASE LEGAL P.003/007

M

(i) enter into the Second Offtake Agreement (Chase Fixed Price Forward) and purchase natural gas from Chase upon the terms thereof;

(ii) enter into the Stoneville Margin Agreement and post collateral with Chase upon the terms thereof;

(iii) enter into all such other deeds, agreements, notices, invoices or other documents requested now or in the future under or in connection with the above mentioned agreements or the transactions thereby contemplated.

(b) It was in the interests of the Company to purchase quantities of natural gas on a prepaid basis as contemplated by the above mentioned agreements and to enter into each of the documents and the transactions referred to by the Chairman as specified in resolution 4(a) above.

(c) A draft of each of the Second Offtake (Chase Fixed Price Forward) Agreement and the Stoneville Margin Agreement is hereby approved and any Director of the Company is hereby duly authorised and empowered to execute the same for and on behalf of the Company in the form of the said drafts with such modifications thereto as he shall approve, his execution thereof to be conclusive evidence of his approval.

(d) Any director of the Company is hereby authorised for and on behalf of the Company to take such action, to do such things and to execute and accept or deliver such other deeds and documents as may be required under or as such Director deems necessary or advisable in connection with the transactions hereby authorised including any such other deed or document to be in such form and contain such terms as such Director shall approve his execution thereof to be conclusive evidence that the form of such other deed or document as executed is approved by the Company.

Termination:

4. There being no further business the Meeting was duly closed.

_____
Chairman

DEC.29'2006 09:14 212 276 7288 CHASE LEGAL 80386 P.011/001

M

STONEVILLE AEGEAN LIMITED

MINUTES OF A MEETING OF DIRECTORS OF STONEVILLE AEGEAN LIMITED HELD AT 22 GRENVILLE STREET, ST HELIER, JERSEY, C.I. ON THE [] DAY OF DECEMBER, 2000.

Present: Ian James
Richard F.V. Jeune

Chairman:

1. Mr I James was appointed Chairman for the purpose of the Meeting.

Minutes:

2. The Minutes of the previous Meeting of Directors were read and approved having been signed by the Chairman of that Meeting.

Financing Transactions:

3. The Chairman noted that the Company has been invited to enter into financing transactions involving, inter alia, the sale by the Company of quantities of natural gas on a forward basis to [Enron Entity] ("[Enron Entity]").

The Chairman noted that in order to give effect to the transactions referred to above the Company proposed to enter into, issue or accept as the case may be:

(a) A Fixed Price Forward Contract (the "~~Third Offtake~~ Agreement") to be made between [Enron Entity] and the Company whereby the Company will agree to sell to [Enron Entity] and [Enron Entity] will agree to purchase from the Company quantities of natural gas at the times, in the quantities, with the specifications and upon the terms and conditions therein specified.

(b) A Margin Agreement (the "[Enron Entity] Margin Agreement") to be made between [Enron Entity] and the Company whereby the [Enron Entity] will agree to post collateral with the Company in an amount equal to the excess (if any) of the purchase price of the gas to be delivered under the ~~Third Offtake~~ Agreement over the marked to market value of the remaining natural gas to be delivered under the ~~Third Offtake~~ Agreement.

(c) A Guaranty (the "[Enron Entity] Guarantee") to be issued by Enron Corp. in favour of the Company whereby Enron Corp. will guarantee the obligations of [Enron Entity] under the ~~Third Offtake~~ Agreement.

DEC.20'2000 09:16 212 276 7298 CHASE LEGAL 90596 P.003/007

M

IT WAS UNANIMOUSLY RESOLVED that:-

(a) the Company:- [Enron Entity] Fixed Price Forward

(i) enter into the ~~Third Offtake~~ Agreement and sell natural gas to [Enron Entity] upon the terms thereof;

(ii) enter into the [Enron Entity] Margin Agreement whereby [Enron Entity] posts collateral with the Company upon the terms thereof;

(iii) accept the [Enron Entity] Guarantee from Enron, Corp. in respect of the obligations of [Enron Entity] arising under or in connection with the ~~Third Offtake~~ Agreement;

(iv) enter into all such other deeds, agreements, notices, invoices or other documents requested now or in the future under or in connection with the above mentioned agreements or the transactions thereby contemplated.

(b) It was in the interests of the Company to sell quantities of natural gas on a prepaid basis as contemplated by the above mentioned agreements and to enter into each of the documents and the transactions referred to by the Chairman as specified in resolution 4(a) above.

(c) A draft of each of the ~~Third Offtake~~ Agreement, [Enron Entity] Margin Agreement and [Enron Entity] Guarantee is hereby approved and any Director of the Company is hereby duly authorised and empowered to execute the same for and on behalf of the Company in the form of the said drafts with such modifications thereto as he shall approve, his execution thereof to be conclusive evidence of his approval.

(d) Any director of the Company is hereby authorised for and on behalf of the Company to take such action, to do such things and to execute and accept or deliver such other deeds and documents as may be required under or as such Director deems necessary or advisable in connection with the transactions hereby authorised and any such other deed or document to be in such form and contain such terms as such Director shall approve his execution thereof to be conclusive evidence that the form of such other deed or document as executed is approved by the Company.

DEC.26'2000 09:46 212 270 7289 CHASE LEGAL #0396 P.006/007

M

Termination:

4. There being no further business the Meeting was duly closed.

Chairman

DEC.20'2000 09:19 212 319 7288 CHASE LEGAL #0596 P.037/067

From: <Philip.Levy@chase.com>
To: <Julie.carter@mourant.com>
Date: 22/12/00 21:53:58
Subject: Mahonia/Stoneville Minutes; Agency Letter

As I indicated in an earlier email, attached are clean and blacklined versions of the Mahonia and Stoneville minutes you forwarded as well as a draft of the agency letter. Please note that although the Mahonia minutes would suggest that two agency letters would be prepared, we determined that only one was necessary. Please have this letter prepared for execution on behalf of Mahonia Natural Gas Limited and forwarded to my colleague, Melissa Vogel, in my absence.

Thanks

(See attached file: Mahonia-ENA Clean.DOC)(See attached file: Mahonia-ENA Marked.DOC)

(See attached file: Mahonia-Purchasers Clean.DOC)(See attached file: Mahonia-Purchasers Marked.DOC)

(See attached file: Stoneville-Chase Clean.DOC)(See attached file: Stoneville-Chase Marked.DOC)

(See attached file: Stoneville-ENA Clean.DOC)(See attached file: Stoneville-ENA Marked.DOC)

(See attached file: Infoagency.DOC)

CC: <gareth.essexcarter@mourant.com>, <ian.james@mourant.com>, <Melissa.C.Vogel@chase.com>, <Jeffrey.W.Dellapina@chase.com>

Mourant & Co. Limited

Annual Review - Company

BOD No. 22268	Matter No. 41218	Client Name HANOJA LIMITED	
Client Type COMPANY	Jurisdiction JERSEY	Tax status EXEMPT	
Icorp. date 16/12/98	Period of this review ..16.12.98..... to ..22.5.01.....		
Groups GROUP 12	ACTIVE	COMPANY	
MFE JAC	CS IC3	Work Group C.12	
Company Limitation BY SHARES	Public Co NO		

Has the client been verified? If NO carry out the verification procedure now and attach a copy of the verification form to this review. VERIFIED

Comments by Group Manager/Compliance

NB - ACCOUNTS PREPARED BY C12 IN DRAFT FORM - BT PROCEDURES AND 'SIGN OFF' TO BE COORDINATED WITH ACCOUNTS PREP

I certify that the details for this client have been fully reviewed, are correct and have been updated on Jobstream and Sims

Administrator	Date 22/5/01	Signature
Group Manager	Date 23-5-01	Signature
Seen by Compliance Pen Peebles.	Date 31/5/01	Signature

ATTACHMENTS TO THIS REVIEW

Register of Directors ✓

Verification Form (if appropriate) N/A

Permanent Subcommittee on Investigations

EXHIBIT #187cc

ate of Transfer from Previous Administrator	—
Date of Last Directors Meeting	28/12/00
AGMS/EGMS	
Date AGM due	—
AGM Waiver	29/12/92
If AGM held was it correctly convened (notice, quorum etc)	~~Yes/No~~
Has an EGM been held since the last review?	~~Yes/No~~
If YES was it correctly convened (notice, quorum etc)	~~Yes/No~~
Have special resolutions been filed with the Registrar of Companies	~~Yes/No~~
Have minutes been entered and signed?	~~Yes/No/NA~~

SYNOPSIS

See attached

OFFICERS

Role	Name	Appointed	Resigned
Director	ICJ	29/12/92	
Director	RFVJ	29/12/92	
Secretary	M+G Secs.	29/12/92	

If there have been changes in Directors or Officers since the last review:-	NONE
Have changes been entered in the minute book?	~~Yes/No~~
Have letters of acceptance/resignation been filed?	~~Yes/No~~
Have changes been notified to overseas Agents?	~~Yes/No~~
Have details been entered in the Register of directors?	~~Yes/No~~

Registered Office

22 GRENVILLE STREET

nnual Return Details

A/R Signatories	Director or Secretary		
Capital Currency	£	Nominal Capital	£10,000
Does Authorised Share Capital agree with statutory records?			Yes/No
Does Issued Share Capital agree with records and issued Share Certificates?			Yes/No

Class of Share	Par Value	Shares	Issued
ORDINARY	£1 -	10,000	10

Shareholders	Total Shares	Joint Holders
AVEIS LIMITED	5	—
LIVEN LIMITED	5	—

If there have been changes to Shareholders since the last review:-

Have allotments/transfers been entered in the minute book?	~~Yes~~/No
Have new share certificates been issued?	~~Yes/No~~
Have declarations of trust been issued?	~~Yes/No~~
If yes have the DOTs been placed in safe custody?	~~Yes/No~~

Beneficial owner	Immediate	Ultimate
[illegible]	—	100%

Has there been a change in beneficial ownership?	Yes/No
If Yes:	
Have details been sent to the FSC? (Exempt Companies only)	~~Yes/No~~
Have new owners signed an Administration Agreement	~~Yes~~/No
If No – reasons why not	
Have new members signed an agreement to waive AGMs?	~~Yes/No/NA~~

TAX Treatment	EXEMPT.	
Date Applied For	8/2/01	Date Approval Received 21/2/01
Date Tax paid	21/3/01	
If Exempt Company has the exemption fee been paid and a receipt obtained?		Yes/No/NA
If Company tax resident in some other jurisdiction – have overseas tax advisers been appointed?		~~Yes/No~~/NA
If 'foreign' investment company – has Exempt Tax concession been applied for and granted?		~~Yes/No~~/NA

Powers of Attorney NONE

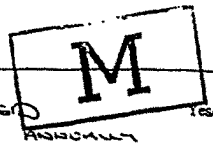
BANK ACCOUNTS

Have new bankers been appointed since the last review?		Yes/No
If yes:	Have mandates been sent to the bank?	Yes/No
	Has it been minuted	Yes/No

Year End 30/12/00	Date of Last Accounts 30/6/96

MANAGEMENT ACCOUNTS TO 30/12/2000 NEXT TO

Auditors	M
LOAN ACCOUNTS	
Have loans been advanced/received since the last review?	Yes/No
Have the terms of the loan(s) been reviewed? WRITTEN OFF INTEREST FREE	Yes/No
If yes:	
Have the terms been minuted NO - SHAREHOLDERS LOAN	Yes/No
Is the master copy of the loan agreement in safe custody? N/A	~~Yes/No~~
Is a photocopy of the agreement in the minute book? N/A	~~Yes/No~~
Are the repayment and interest dates diarised on Jobstream? N/A	~~Yes/No~~
INVESTMENTS	
If the Company is holding any investments complete the Investment Supplement	4
PROPERTY	
If the Company is holding any properties, complete the Property Supplement	N
CLIENT CONTACT	
Do we have good contact with the client? CHASE NEW YORK	Yes/No
If NO with whom do we correspond? ———	
(contact address to be entered on Jobstream)	
Frequency of contact REGULAR Is this adequate	Yes/No
CLIENT SERVICE & ADMINISTRATION	
Has all outstanding correspondence been dealt with?	Yes/No
Are you aware of any complaints by this client?	Yes/No
If YES has Compliance been advised?	~~Yes/No~~
Has the client altered the type or style of business since the last review	Yes/No
If YES should a suspicious transaction be reported to Compliance for investigation?	~~Yes/No~~
Are there any special reporting/correspondence requirements?	Yes/No
If Yes have these been noted on the file and on Jobstream?	~~Yes/No~~
Have these been adhered to since the last review?	~~Yes/No~~
BILLING	
To whom are bills to be sent? PHIL LEVY / JEFFREY DELLARNA	
Are the invoices raised in line with the latest 'fees letter' sent to the client 22/9/00	Yes/No
Have fees been reviewed with the client? 22/9/00	Yes/No
If NO please advise when fees were last discussed with the client.	
Has the latest invoice been settled?	Yes/No
If NO please advise reason if known.	———



ACCOUNTS

Does the client receive accounts NOW BEING PREPARED Yes/No

Please state the frequency of the accounts ie annual, every two years ANNUALLY

What was the period of the last set of accounts? ~~From~~.....to...30/6/96

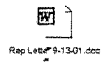
MANUAL RECORD

Have you gone through the minute book and reviewed the correspondence file to ensure that all details concerning this entity are accurate and up to date? Yes/No

From:	Garberding, Michael
Sent:	Friday, September 14, 2001 9:09 AM
To:	Jeff Dellapina (E-mail)
Cc:	Bills, Lisa; Quaintance Jr., Alan
Subject:	Rep Letter for Mahonia

Jeff --

As discussed yesterday in our call, Arthur Andersen (AA) now requires us to have certain reps from the Swap Co.that is utilized within the prepay structure. The following attachment is an example of what the letter will look like. With regard to the process (as the transaction reaches completion), AA will send directly to the Swap Co. a letter from Enron that describes the rep confirm process along with an example of the rep letter. The Swap Co. will need to return a signed rep letter to AA on their own letterhead signed by an authorized member of the Swap Co. (that is similar to the example). Please let us know if you have any questions with regard to either the letter or the process. Thanks for your help.



Michael Garberding
Enron Americas Global Finance
Work: (713) 853-1864
Fax: (713) 646-3602
E-mail: michael.garberding@enron.com

Permanent Subcommittee on Investigations
EXHIBIT #187dd

[Date , 2001]

Enron Corp.
1400 Smith Street
Houston, Texas 77002

To Whom It May Concern:

Re: [Mahonia] (the "Company")

We confirm:

1. There is no restriction in the corporate documentation of the Company limiting the number of entities with which the Company may conduct business. The Company has undertaken business with a number of entities.

2. The Company has assets other than those acquired through transactions with Enron Corp and its subsidiaries and its affiliates (collectively "Enron").

3. The Company has unencumbered assets, which are available for application towards obligations owed to its creditors.

Yours truly,

Signed by:_____
Title:_____

From: Garberding, Michael
Sent: Thursday, September 27, 2001 11:47 AM
To: 'Julie Carter'
Cc: Quaintance Jr., Alan; Edmonds, Marcus; Kolle, Brian
Subject: RE: Mahonia Confirm

Julie --

Thanks for your message. You should have already received the confirmation from Arthur Andersen. With regard to your comments below on representation #4, can you please make the representation up to the point of "or consolidate .. principles." Instead of that statement, can you please add a sentence saying the following, "We don't comment on Chase's accounting, but Chase does not own our ownership interests."

Please give me a call with any questions and thanks for all your help. Take care.

Michael Garberding
Enron Americas Global Finance
Work: (713) 853-1864
Fax: (713) 646-3602
E-mail: michael.garberding@enron.com

-----Original Message-----
From: Julie Carter [mailto:Julie.Carter@mourant.com]
Sent: Thursday, September 27, 2001 4:43 AM
To: phillip.levy@chase.com; Quaintance Jr., Alan
Cc: Garberding, Michael
Subject: Re: Mahonia Confirm

Dear Alan and Phil

Ian has the following comments:

Everything is OK except for the words "or consolidate..principles." in 4 as this is a matter for Chase not the board of Mahonia.

Kind regards

Yours sincerely
For and on behalf of
Mourant & Co. Secretaries Limited

Julie Carter

>>> "Quaintance Jr., Alan" <Alan.Quaintance.Jr@ENRON.com> 26 September 2001 >>>

Julie:

I am forwarding a draft of a confirmation to you for Ian James to review. <<Mahonia Limited Confirm.doc>>

Our auditors, Arthur Andersen, will fax a signed copy of this request to you at 44-1534-609333. When you receive the request from Arthur Andersen, please fax Andersen a confirmation in response. The confirmation, faxed back to Andersen, should be the second page of the above document on Mahonia Limited letterhead. Please have it signed and

Permanent Subcommittee on Investigations
EXHIBIT #187ee

dated. Arthur Andersen's fax number is 713-646-3555. Please also fax Enron a copy of your confirmation at 713-646-3602 (attn: Alan Quaintance).

I can be reached at 713-345-7731 if you have any questions.

Thank you,

Alan Quaintance

****
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****

Website: http://www.mourant.com

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If this message includes attachments, please ensure they are opened within the relevant application to ensure full receipt.
If you experience difficulties, please refer back to the sender.

Mahonia Limited

PO Box 87
22 Grenville Street
St Helier
Jersey JE4 8PX
Channel Islands

Tel: 01534 609000
Fax: 01534 609333
Telex: 4192064
International
Tel: +44 1534 609000
Fax: +44 1534 609333

Direct Dial 01534 609637
via secretary

Arthur Andersen LLP

28 September 2001

Our ref: 0809/g12/InFin/109264/41218/22268

Dear Sirs

We confirm the following information about Mahonia Limited (the "**Company**"), with the following exceptions (if any):

1. There is no restriction in the corporate documentation of the Company limiting the number of entities with which the Company may conduct business. The Company has undertaken transactions with entities other than Enron Corp and its subsidiaries and affiliates ("**Enron**");

2. The Company has assets other than those that will be acquired through transactions with Enron; and

3. The Company has unencumbered assets, which are available for application towards obligations owed to its present and future creditors (including Enron).

4. The Chase Manhattan Bank and its consolidated subsidiaries do not own the ownership interests of the Company.

Yours faithfully,
For and on behalf of
Mahonia Limited

Ian James
Director

FOIA CONFIDENTIAL TREATMENT REQUESTED BY JPMC

Permanent Subcommittee on Investigations
EXHIBIT #187ff

Bill
FYI
Pat

CHASE

To: Joseph L. Sclafani
Mark Staines

Date: August 6, 1996

cc: Diane Butterfield
Edwin Jenkins
John Cotter

From: William Macomber

Phone: 622-8803

Re: Prepaid Forwards

I have received a listing of "prepaid forwards" that I believe was prepared by a business manager a few months ago. I have review such listing for the purposes of determining whether any balances should be reclassified to loans or risk management assets/liabilities. In this context, a possible accounting policy would be that a transaction not causing meaningful market risk as of a reporting date should be classified as a loan , while one causing meaningful market risk should be reported as a risk management asset/liability. Because some transactions have provisions that periodically convert a fixed dollar exposure into a fixed commodity exposure, the policy would require monthly monitoring of such transactions to appropriately classify the related balances.

Based on my understanding of the terms of the listed "prepaid forwards" the following transactions should be reclassified as loans.

COUNTERPARTY	BALANCE IN MM	COMMENTS
Enron Hydrocarbons	$137	The initial balance of $207 MM amortizes monthly over a five year period. Each month, the fixed dollar balance due in 12 monthly is converted into a fixed crude oil amount based on the price of a related futures contract that hedges the Bank's exposure. The commodity balances due over this 12 month period should be reclassified as commodity derivatives, while the remaining balance should be classified as a loan. Note that an SPV was established as the Bank's counterparty to avoid a potential Regulatory issue regarding delivery of crude to a Bank. This proposed accounting effectively consolidates the SPV.
Enron Natural Gas	$183	The deal structure and proposed accounting are similar to the Enron Hydrocarbons but the commodity is natural gas and the initial balance was $225MM.
China Natural Nonferrous Metals	$30	The fixed dollar exposure will convert into an aluminum exposure during November 1996 and settles on November 27, 1996. Until conversion, the balance should be reported as a loan.

HIGHLY CONFIDENTIAL

Permanent Subcommittee on Investigations
EXHIBIT #187gg

MG Gas Services Inc.	$225	According to line management, the counter party deposited the proceeds with the Bank and the commodity risk from this transaction was immediately offset by a different commodity transaction with the same counterparty. They also said that the counterparty derived tax benefits from these transactions. The asset should be reported as a loan. I have requested documentation as to the deposit and offsetting transaction to determine the appropriate risk based capital reporting.

Two other transactions (El Indio for $51 MM and Industrias Luismin for $9 MM) were listed as prepaid commodity transactions, but these deals do cause market risk and are included in the traders' bullion arbitrage book. Under Old Chase's reporting practice, however, the net market value for all transaction in a given commodity is reported in other assets or liabilities. This seems to be contrary to FAS Interpretation No 39.

Note that under the terms of a binding commitment to El Indio, this company has the right to extent the maturity of any related transaction continuously until the expiry date of November 10, 2002. The existence of this commitment is probably the basis for an Old Chase's GRM Risk Management policy stating that these deals are not considered to be historic rate rollovers. Despite this commitment, the current maturity of a transaction has been used for risk based capital reporting purposes. At a minimum, this seems to require a change.

Recently, several proposed transactions have been referred to me that also cause concern about Old Chase's balance sheet reporting. ICM Controllers has suggested that they prepare an issue paper that would be the basis for extensive discussion among ourselves and subsequently with you.

MEMO

OCCIDENTAL PETROLEUM CORPORATION
LOS ANGELES, CALIFORNIA

To: J. R. Havert and S. Kumar
Date: November 16, 1998

From: Brian A. Levan
cc: S. P. Dominick
A. R. Leach
R. Pineci (AALLP)

Subject: Proposed Pre Sale of Gas

This memo will summarize the accounting implications of the proposed pre sale of gas that is currently contemplated. In short, Oxy would receive an up front cash payment from Mahonia for the commitment for Oxy to deliver certain volumes of natural gas over a 4-year period beginning one year after receipt of the cash. Simultaneously, Occidental intends to enter into a swap with Chase based on the same notional volumes of natural gas that corresponds to the delivery obligation to Mahonia. Under the swap Oxy will receive the floating price for natural gas which will correspond to the then current market price. Oxy will pay a fixed price for natural gas. During the first year of the five-year contract no deliveries of natural gas will be made and no payments will be made or received under the swap arrangements.

Current accounting pronouncements do not specifically address the type transaction you are contemplating, however, I have discussed the transaction with Roy Pineci of AA LLP and can provide the following guidance.

Balance Sheet and Income Statement Impact

The receipt of the cash will not be booked as long term debt, however disclosures that are similar to debt disclosure will be made in the footnotes. It will be recorded as a separate line on the balance sheet under deferred credits and other liabilities. An example of the caption could be "obligations under gas sale agreement".

An imputed interest rate should be calculated at the inception of the transaction. Interest expense will be accrued and added to the liability on the balance sheet.

As deliveries are made under the agreement, Oxy will record revenues based on the imputed market-related price curve of natural gas inherent in the transaction which would reflect imputed interest in the transaction. The effect of the swap will either be added to or subtracted from revenues based on the net position at the monthly settlement date, which in effect will be to report revenue at market prices at the time of delivery.

Footnote Disclosures

A full description of the transaction must be made in a footnote to the financial statements, similar to the disclosures made for long-term debt, including the imputed interest rate. The initial transaction must also be disclosed in management's discussion and analysis. The footnote disclosure must include the delivery commitment by year for each of the next five years with a total for all years after the fifth. The commitment must be expressed in dollars and in volume. The details of the swap must also be disclosed.

Permanent Subcommittee on Investigations
EXHIBIT #187hh

Oil and Gas Reserve Disclosures

The natural gas delivery commitment will not be deducted from Occidental's oil and gas reserves. This transaction will have no impact on Occidental's year-end oil and gas reserve disclosures.

Natural Gas Swap

The natural gas swap will be subject to current hedge accounting rules. primarily FASB Statement No. 80 Accounting for Futures Contracts. Under current accounting rules, as long as the characteristics of the swap correspond to the price risk exposure the swap will qualify for hedge accounting and no mark-to-market adjustments will be necessary.

However, on January 1, 2000 this transaction will be subject to the new derivative disclosure rules contained in FASB Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities'. Under this statement Oxy will be required to mark-to-market changes in the value of the swap AND the delivery commitment liability. Both mark-to-market adjustments will be recorded as a charge or credit on the income statement. To the extent the characteristics of the swap correspond to the price risk exposure, as is expected, the change in the value of the swap and delivery commitment should offset each other resulting in no effect on the income statement compared to the accounting that will be followed until January 1, 2000.

Margin Account

Regarding the margin account whereby if the swap with Chase results in a negative position to Oxy of more than $75 million, Oxy could be obligated to make a payment to Chase to bring the exposure down to the $75 million level. As I understand the current transaction, Oxy would not make a payment, but may either issue a letter of credit or other guarantee to Chase or place cash or other assets into a restricted account. If cash is placed in a restricted account under Occidental's name it would be shown as an other asset. However, if a payment is made, it will be recorded on the balance sheet as either an asset or as a contra liability in the same balance sheet line as the delivery commitment.

Dominick, Sam

From: Havert, Jim
Sent: Wednesday, November 11, 1998 7:54 AM
To: Leach, Tony
Cc: Levan, Brian A.; Dominick, Sam; Kumar, Sanjeev
Subject: Chase Presale Accounting

Tony,

The latest info from Brian, who has Roy's input, is that we can treat not as debt but as a deferred credit on a separate line and keep the reserves.

Jim

MEMO

OCCIDENTAL PETROLEUM CORPORATION
LOS ANGELES, CALIFORNIA 90024

TO Distribution

DATE November 4, 1998

FROM S. Kumar

cc: J. R. Havert
M. Preston

SUBJECT **Gas Forward Sale**

In order to facilitate the understanding of the proposed transaction and the review of the related documents, attached is a diagrammatic representation of the structure accompanied by a summary outline.

I hope the attached is helpful. Please note that the quantities and the prices indicated are for illustration purposes only and may change depending on the interest rates and gas prices at the time of closing. Also, the structure may need further modification to accommodate any additional concerns raised by Chase or the Sureties.

Please call Mike Preston or me if you have any questions or need further clarification.

SK:ljm
Attachments

Distribution:

D. Amato
K. Kilourie
B. Levan
H. Mukadam
M. Pate
M. Shelton
M. Soland

GAS FORWARD SALE
TRANSACTION SUMMARY

I. Form new subsidiary of Occidental Energy Services, Inc. (tentatively named Occidental Specialty Marketing, Inc., a Delaware corporation ("OSMI")).

II. OSMI enters into Forward Sale Agreement with Mahonia Limited:
   a. $500 million prepay.
   b. Gas delivery over years two through five (one year grace) at specified delivery points – daily delivery.
   c. Cash settlement for failure to deliver (including force majeure).
   d. Obligations guaranteed by OPC.

III. OSMI enters into Swap with Chase Manhattan Bank:
   a. OSMI pays fixed/receives floating (Inside FERC).
   b. Monthly cash settlement.
   c. OSMI to put up credit enhancement (collateral, LC) if mark to market exposure of amounts due to Chase exceeds $75 million, which may decline under certain circumstances.
   d. Obligations guaranteed by OPC.

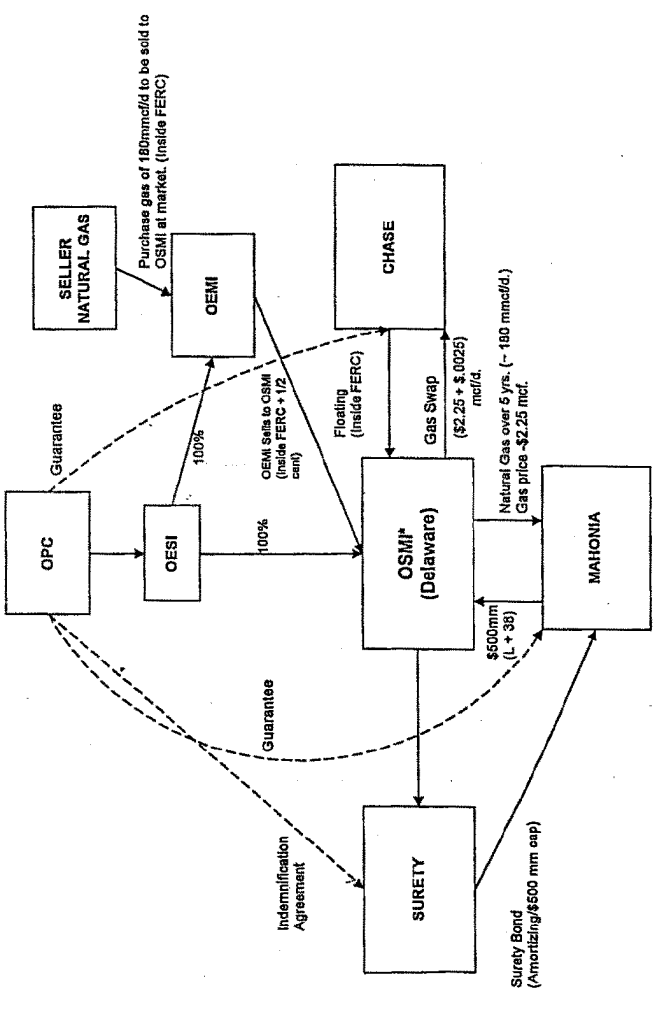
IV. Surety bond issued by syndicate of sureties in favor of Mahonia to back up obligations of OSMI under Forward Sale Agreement:
   a. Capped at $500 million and amortized over five years according to fixed schedule.
   b. Pay replacement value only not to exceed amount in IV. a. above.
   c. OPC INDEMNIFIES SURETIES

V. OSMI enters into Margin Agreement with Mahonia Limited:
   a. Pledge proceeds under Chase swap to the extent mark to market exposure of remaining amounts due OSMI exceeds $75 million.

VI. OSMI enters into Purchase and Sale Agreement with OEMI for purchase of gas to be delivered under Forward Sale Agreement:
   a. Initial term of one year, at election of parties.
   b. Purchase price equivalent to Inside FERC to be received under swap plus 1/2¢.

VII. OEMI will source gas from third parties or internal sources.

CHASE ADVANCE SALE



LEGAL DEPARTMENT MEMO

OCCIDENTAL PETROLEUM CORPORATION
10889 Wilshire Boulevard Los Angeles, California 90024 Direct: Tel. (310) 443-6187 Fax. (310) 443-6314

To: Distribution Date: May 22, 2000

From: Kathleen Kilourie cc:

Subject: Arthur Andersen Memo: Oxy Presale

Attached are my comments on Greg Geyer's memo dated May 17, 2000 regarding accounting treatment of the proposed Oxy presale. I have the following further thoughts:

I object to Greg's classification of the transaction throughout the memo as a production payment. While that may be AA's preferred accounting treatment, AA's memo should not assume its conclusion. I would like to read AA's analysis of why this deal, which contains no transfer of interest and no dedicated reserves, is a production payment. There is no such analysis in the memo.

Also troubling is AA's summary of the wrong term sheet and failure to understand basic concepts of the proposed transaction. Contrary to the memo, there are no dedicated or burdened properties in this deal. Further, the AA memo states that any change in law triggers an early termination payment; however, according to the documents, only a change in law making performance of the obligations unlawful actually triggers such a payment. This distinction alters the risk-sharing profile greatly. Oxy's receiving appropriate accounting treatment is dependent upon AA's ability to correctly and completely summarize the proposed transaction for its Houston group.

Distribution:
Sam Dominick
Jim Havert
Sanjeev Kumar

Mtg 10.15 Wed 5.24

Later meeting
Deal had changed back
to a presale to close and
neither AA nor SPD were aware of
this. Clearly communicated this
report to SK + KK.

Andrew Cozby	To:Bob Mertensotto/CHASE@CHASE
	cc:
05/27/1999 03:00 PM	bcc:
	Subject:Ocean Energy, Inc.

Bob: Shareron Gill prepared the following at my direction regarding the issues you highlighted:

Issue: Does prepay count as debt?

Yes, prepay does count as debt. As it states in section 1.1 page 10 clause (i), "**indebtedness of such person for** borrowed money (whether by loan or the issuance and sale of debt securities) or for the **deferred purchase** or acquisition price of property or services, including, without limitation, **obligations payable out of hydrocarbon production.**"

Issue: As OEI sells assets, how does it reduce the commitments?

It states in section 10.4 page 58, that the company will not sell more than 10% in the aggregate of the company's and its restricted subsidiaries consolidated total assets. However, it does not state whether it would use this small portion to reduce its commitments.

Take a look and see if this information helps any, and if it doesn't let me know and I will try again tomorrow.

Thanks for including me in this project,
Shareron

Permanent Subcommittee on Investigations
EXHIBIT #187ii

Hunt Oil Company

Reserve Financing Alternatives:
Volumetric Production Payment / Forward Sale (Prepay)
Discussion
December 22, 1999

CHASE

vSubcommittee on Investigations
EXHIBIT #187jj

Table of Contents

A. Executive Summary
- Monetization Objectives of Hunt Oil Company
- Hunt Objectives versus Strategic Alternatives

B. Volumetric Production Payment
- Transaction Diagram
- VPP Structure Highlights
- Production Payment Summary
- Production Payment Structure
- Balance Sheet and Income Statement Impact Analysis
- Financing Issues

C. Forward Sale (Prepay)
- Forward Sale (Prepay) Structure Highlights
- Transaction Diagram
- Sample Term Sheet
- Balance Sheet and Income Statement Impact Analysis
- Financing Issues

1400

A. Executive Summary

1401

Executive Summary

Monetization Objectives of Hunt Oil Company ("Hunt")

- Manage balance sheet leverage.
- Maintain / improve already strong leverage ratios.
- Reserve retention (assets) on balance sheet for accounting and SEC purposes.
- Minimize tax effects.
- Control/operation of assets.
- Retain upside in reserves (assets).
- Minimize negative impact on cash flow and net income.
- Secure competitively priced financing and minimize transaction costs.
- Maintain structural flexibility to take into account internal issues and/or advantage of favorable market movements.

Strategic Alternatives

- Production Payment -- a non-recourse sale of designated proved, developed, producing reserves (PDPs) to an existing special-purpose entity. Financing is provided via the bank market.
- Forward Sale (Prepay) -- a sale of undesignated future natural gas or crude oil production. The sale represents a general corporate obligation to deliver designated hydrocarbons volumes.

1402

Hunt Objectives versus Strategic Alternatives

	Production Payment	Forward Sale (Prepay)
Remove debt from balance sheet:	Yes, from application of cash proceeds to repay debt. [Deferred Revenue item, a long-term liability, is created on balance sheet]	Possibly, depends on the treatment of debt by rating agencies Deferred Revenue item, a long-term liability, is created on balance sheet.
Current impact to leverage ratios for rating agency purposes:	Improve from application of cash proceeds to debt. Conduit financing is viewed as off balance sheet by the rating agencies.	Potential improvement. Funded debt ratios will likely improve as deferred revenue is not included in debt / capital ratios.
Retain control of operations:	Yes	Yes
Allow Hunt to retain upside of reserves (assets):	Yes	Yes

1403

Hunt Objectives versus Strategic Alternatives (continued)

	Production Payment	Forward Sale (Prepay)
Retain reserves on balance sheet for accounting and SEC purposes:	No	Yes
Minimize tax exposure:	No cash tax effect. Proceeds considered debt for tax purposes, however transaction would qualify as a sale under GAAP.	Deferred Seller may elect to defer recognition of prepaid income.
Impact to cash flow:	Current period cash flow is improved by transaction proceeds. Future cash flows are reduced by securitized amount.	Current period cash flow is improved by transaction proceeds. Cash flow is reduced in subsequent periods by removal of production from revenue stream.

1404

Hunt Objectives versus Strategic Alternatives *(continued)*

	Production Payment	Forward Sale (Prepay)
Impact to earnings:	Reduces over the defined period due to lower revenue stream from securitized reserves.	Amortized discount on forward gas will approximate interest expense on funded debt, which will have been repaid.

1405

C. Forward Sale (Prepay)

1406

Forward Sale (Prepay) Structure Highlights

Attractive Accounting Treatment:

- Obligation to deliver hydrocarbons in the future is classified as deferred revenue vs. funded debt. Most users of the prepay structure believe the transaction to be "rating agency friendly".
- Reserves are not eliminated from SEC 10 valuation, as is the case with a Volumetric Production Payment.
- Importantly, most accounting firms believe the prepay structure avoids the potential for future mark-to-market accounting of the hedge position.

Alternative Source of Capital:

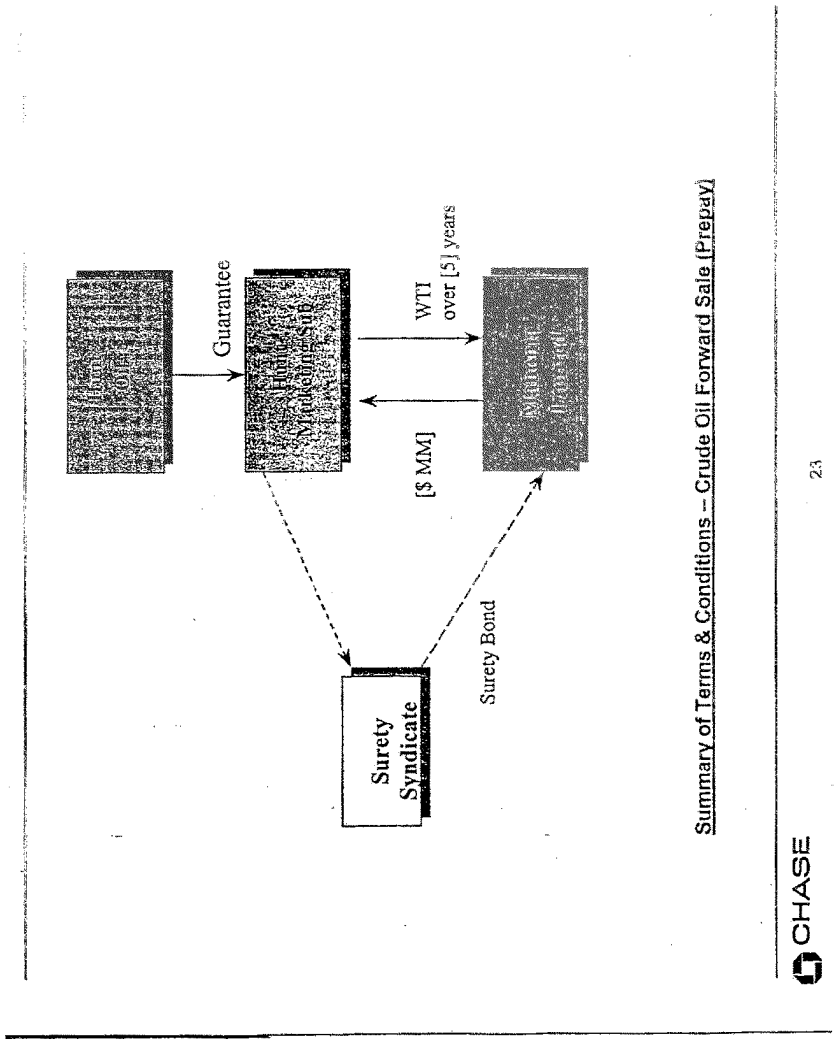
- Offers a competitively priced medium term (generally 3-5 year source of capital) without tapping traditional bank and public capital markets.
- The transaction can be completed quietly and discretely if you chose to do so.
- Performance risk associated with the transaction can be syndicated through the surety bond market via a proprietary structure developed by Chase.

Clean Execution:

- Chase has arranged over $3.0 billion of prepay transactions for the oil and gas sector during the past 24 months.
- Execution requires typically less than 30 days from mandate to execution. Legal costs are minimal and can be capped by utilizing "off-the-shelf" documentation.

Forward Sale (Prepay) –Transaction Diagram

1407


Guarantee
WTI
over [5] years
[$ MM]
Surety
Syndicate
Surety Bond
Summary of Terms & Conditions – Crude Oil Forward Sale (Prepay)
CHASE
23

SELLER:	Subsidiary of Hunt Oil Company
GUARANTOR:	Hunt Oil Company,
PURCHASER:	Mahonia Limited, a Jersey Channel Islands company ("Mahonia")
ARRANGER:	The Chase Manhattan Bank ("Chase" or "Arranger")
DESCRIPTION:	A [$], prepaid, forward sale of U.S. delivered WTI crude oil ("WTI")
DELIVERY SCHEDULE:	Continuous monthly deliveries commencing [March 2000] and ending [August 2004].
WTI DELIVERY LOCATION:	To Be Determined
WTI DELIVERY QUANTITY:	Approximately [ ] barrels per day ; Approximately [ ] barrels in total
CLOSING DATE:	[30 days from mandate]
DETERMINATION OF PREPAYMENT AMOUNT:	An amount determined simultaneous with closing. In addition to Delivery Quantity and Delivery Schedule, factors contributing to determination of the prepayment amount include: i) the forward price curve for WTI; and (ii) the Discount Factor (defined below).

VOLUNTARY TERMINATION: This commercial transaction does not contemplate voluntary termination.

DISCOUNT FACTOR:	At closing, the USD interest rate reflecting the sum of (a) an interpolated discount rate from the forward LIBOR curve related to the Delivery Schedule, plus (b) [ ] basis points.

1409

CRUDE OIL FORWARD SALE CONTRACT:	Agreement between Purchase and Seller covering all commercial aspects of the WTI forward sale.
SURETY BOND:	An irrevocable obligation by a syndicate of insurance companies (each a "Surety", collectively the "Sureties") with an initial maximum available amount equal to the prepayment amount. The maximum available amount will reduce monthly in accordance with the Delivery Schedule. Each Surety is severally but not jointly liable. The Purchaser is the Obligee (beneficiary) of the Surety Bond. Drawings may be made only following an Event of Termination and the failure of Seller to make the Termination Payment.
SURETY BOND PREMIUM:	An amount agreed between Seller and Sureties. [Target: bps]
INDEMNITY AGREEMENT:	To be negotiated between Seller and Sureties
MARGIN AGREEMENT:	Between Purchaser and Seller whereby Seller agrees to provide margin when the future value of the Deliveries ("Replacement Value") exceeds the original value by an amount in excess of the threshold [ ]. The margin may be in the form of (i) cash or (ii) letter of credit.
CONDITIONS PRECEDENT:	The usual and customary for a transaction of this nature including, but not limited to: •Delivery of corporate authorizations •Delivery of legal opinions
REPRESENTATIONS AND WARRANTIES:	The usual and customary for a transaction of this nature
AFFIRMATIVE COVENANTS:	The usual and customary for a transaction of this nature
FINANCIAL COVENANTS:	Not applicable

1410

INCREASED COSTS:	In the event that a Surety is downgraded below A -, Seller will pay Purchaser a cash premium of 35 bps per annum for that notional portion of the Surety Bond attributable to the downgraded Surety until such time as such Surety is substituted with an acceptable replacement surety
EVENTS OF DEFAULT:	Including, but not limited to: • Failure by Seller to deliver the WTI Delivery Quantity and/or Delivery Quantity to the respective Delivery Location(s) and failure to pay the Replacement Value of the undelivered quantity • Default on other Seller indebtedness • Insolvency, bankruptcy, or general reorganization of creditors
GOVERNING LAW:	State of New York.
LEGAL COUNSEL:	To be determined
LEGAL EXPENSES:	• Deal Counsel expenses for the account of Seller • Other legal expenses of Seller for account of Seller • Other legal expenses of Purchaser for account of Purchaser
OUT-OF-POCKET EXPENSES:	The Borrower will reimburse the Arranger for all reasonable out-of-pocket expenses.
ARRANGEMENT FEE:	[ ] basis points flat on prepayment amount, payable to Arranger at closing

1411

Balance Sheet and Income Statement Implications

At Closing

Balance Sheet:

- *Assets increased by [$ MM] in cash received.*
- *Liabilities increased by [$ MM] as a net discounted value of the Deferred Revenue.*

Income Statement

- *No Impact*

At each Delivery Date

Balance Sheet

- *Assets reduced due to reduction in inventory equal to the gas delivery obligation.*
- *Liabilities reduced for the reduction in the amount of the Deferred Revenue equal to the amount of gas delivered during the period*

Income Statement

- *Revenues increased by the amount of the Forward Delivery Obligation for the period.*
- *Expenses increased by the amount of Interest Expense for the period.*

Financing Issues

- Timing Issues
  - *Six to eight weeks needed to complete transaction*

Steven G Wood 08/16/2000 09:42

Global Oil & Gas 212-270-7056 Fax Number: 212-270-2519

To David S McSweeney/CHASE@CHASE
cc Douglas B Petno/CHASE@CHASE, George Serice/CHASE@CHASE
Subject Columbia Prepay

Attached is our struc sum which breaks down our exposure in the exec summary (copied below). We haven't had any further discussion on the rollover/redo of Columbia's credit facilities because of these other issues but now that the decks are cleared we will talk with them. Thanks.

Exposure – Our current primary exposure to Columbia is $390MM, consisting of the following:

- $150MM of principal exposure, broken into $50MM in Columbia's 364-day facility and $100MM in its 5-year facility
- $10MM of principal exposure for commodity physical transactions.
- $80MM of replacement exposure for derivatives.
- $150MM in counterparty trades for the previous prepay.

This prepay will result in $310MM of additional exposure consisting of $250MM principal amount and $50MM of fractional exposure.

---------- Forwarded by Steven G Wood/CHASE on 08/16/2000 09:33 AM ----------

Steven G Wood 08/16/2000 09:15

Global Oil & Gas 212-270-7056 Fax Number: 212-270-2519

To James Ballentine/CHASE@CHASE
cc Jeffrey W Dellapina/CHASE@CHASE, Sara Pirzada/CHASE@CHASE
Subject Columbia Prepay

Attached is a modified structuring summary for the Columbia prepay. Some specific answers to your questions:

- Mahonia is a SPV owned by a trust that only does Chase transactions. Chase lends to Mahonia, which does a back-to-back with Columbia.
- If CNR does not deliver, we can move against CNR, which owns gas reserves. We also exercise the Columbia Energy guarantee, which is a payment guarantee. If CG does not perform we have a debt claim against CG. We also reference the credit agreement in the prepay docs. Finally, if CG does not perform we exercise the surety bond from the insurance companies for the full amount owing. So we have recourse against CNR (operating company), Columbia Energy and the surety.
- Gas is nominated each month by CNR to Mahonia for delivery at the Teco Appalachia hub. Mahonia nominates it to Chase and we sell it to a variety of parties (Enron, El Paso, etc.).
- In the prepay we are paying fixed up front and receiving floating and this exposure is matched in our trading book.
- The loan shows up in GES indirectly as part of Columbia exposure.
- At the end of 1999, Columbia had 966 Bcfe (74% PDP) of proved reserves. This transaction will require about 93 Bcfe or less than 10% of proved reserves.

Thanks.

Columbia Energy Struct Sum 8-15-00

Permanent Subcommittee on Investigations
EXHIBIT #187kk

SENATE
MAH - 02224

FOIA Confidential Treatment
Requested by JPMC

Prepared By: Sara Pirzada

STRUCTURING SUMMARY

Columbia Energy Group
Client Executive, Lender: Petno, Wood
Credit Executive: Ballentine Timing: August 2000

Maximum Exposure for Approval ($MM):	$700MM	**Industry Description:**	Pipelines
Transaction for Approval ($MM):	$250MM Prepay	**Primary SIC Code:**	4921
Customer Name:	Columbia Energy Group	**Headquarter Location:**	Herndon, VA
Obligor/Facility Risk Grade:	3+	**Major Plant Locations:**	Ohio, NY, Pennsylvania
Parent Name:	Columbia Energy Group	**Major Overseas Ops:**	N/A
Parent Risk Grade:	3+	**TREND: Improving/Stable/Declining**	Stable
Public Ratings (LT & ST):	A3/BBB+, P2/A2	**Outlook/Trend?**	Moodys: On watch for possible downgrade S&P: Negative Credit watch
Date Ratings Last Changed:	(M) 7/30/98,(S&P) 1997	**Last Senior Contact**	
Stock Price (as of 8/9/00):	$68.94	**52 Wk High/Low:**	$69.06 / $54.19
Market Capitalization:	$5,482MM	**Market Cap/Book Cap:**	2.54x

Executive Summary:

Columbia Energy Group (Columbia), formerly The Columbia Gas System, Inc., and its subsidiaries comprise one of the nation's largest integrated natural gas systems engaged in natural gas transmission, natural gas distribution, and exploration for and production of natural gas and oil. Columbia is also engaged in related energy businesses including the distribution of propane and petroleum products, marketing of natural gas and electricity and the generation of electricity, primarily fueled by natural gas. Columbia, organized under the laws of the State of Delaware on September 30, 1926, is a registered holding company under the Public Utility Holding Company Act of 1935, as amended, (1935 Act) and derives substantially all its revenues and earnings from the operating results of its 19 direct subsidiaries. Columbia owns all of the securities of these direct subsidiaries except for approximately 8% of the stock in Columbia LNG Corporation. Columbia and its subsidiaries are sometimes collectively referred to herein as the Columbia Group.

On February 28, 2000, Columbia announced that it had entered into an Agreement and Plan of Merger between Columbia and NiSource, Inc. The Board of Directors of Columbia determined to enter into the Merger Agreement after a comprehensive evaluation of strategic alternatives that might generate value greater than that which Columbia's business plan could create. The terms of the Merger Agreement provide that NiSource will organize a new company, which shall serve as the holding company for both Columbia and NiSource after the completion of the transaction. Pursuant to the terms of the Merger Agreement, each of Columbia and NiSource will be merged into newly formed special purpose subsidiaries of the new holding company, and each will become a wholly owned subsidiary of the new holding company.

Columbia's shareholders will receive, for each share of Columbia common stock, $70 in cash and a $2.60 face value SAILS(SM) (a unit consisting of a zero coupon debt security with a forward equity contract). Columbia's shareholders also have the option to elect to receive (in lieu of cash and SAILS(SM) shares in the new holding company in a tax-free exchange, for up to 30% of the outstanding shares of Columbia common stock. Pursuant to the stock election option, each Columbia share will be exchanged for up to $74 in new holding company stock, subject to a collar such that, if the average closing price of NiSource shares during the 30 days prior to the closing of the transaction is greater than $16.50, Columbia shareholders will receive shares of the new holding company valued at $74 for each share of Columbia stock, and if the average closing price of NiSource shares during the 30 days prior to closing of the transaction is $16.50 or below, Columbia shareholders will receive 4.4848 shares of new holding company stock for each Columbia share. Upon completion of the transaction, NiSource shareholders will receive one share of holding company stock for each share of NiSource common stock that they own.

Relationship Summary – Columbia is a Green name. Chase is a Documentation Agent in Columbia's Citibank-led credit facilities and is a close second behind Citi. We closed a $150MM natural gas prepay transaction in November 1999, which included $1.5MM in fees.

Exposure – Our current primary exposure to Columbia is $390MM, consisting of the following:

- $150MM of principal exposure, broken into $50MM in Columbia's 364-day facility and $100MM in its 5-year facility
- $100MM of principal exposure for commodity physical transactions
- $80MM of replacement exposure for derivatives
- $150MM in counterparty trades for the previous prepay

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Revised 5/99

FOIA Confidential Treatment
Requested by JPMC

SENATE
MAH - 02225

This prepay will result in $310MM of additional exposure consisting of $250MM principal amount and $60MM of fractional exposure.

SVA – Total 1999 SVA for Columbia was $512 9M and LTM SVA is $623 8M Initiatives to improve our SVA this past year include:

- Repriced the company's 364-day facility in March
- Closed a $150MM natural gas prepay transaction in November 1999
- Closed on a Project Financing advisory and financing for Liberty Power

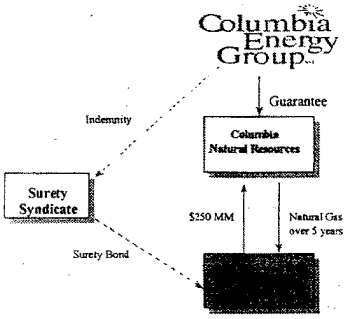
Approval Request

- We are requesting approval to do a prepay for $250MM (see below for transaction overview), which requires an additional $60MM fractional exposure

TransactionOverview:

The basic transaction calls for Chase to enter into a Forward Gas Sale Agreement with Mahonia (Buyer), which executes a back to back prepay with Columbia Natural Resources (CNR, see Chart). An integral part of the Forward Gas Sale Contract (referred to as a "Prepay") is the execution of a series of commodity and interest rate swaps, which result in a known cash flow stream. As in other Prepay transactions, Chase will retain the delivery risk associated with these swaps. This risk is supported by a payment guarantee from Columbia Energy and further supported by surety bonds from several insurance companies.

Columbia will provide a guarantee for the base prepay amount and an additional guarantee for the fractional exposure. The guarantee will remain flat through 2001 then reduce with the repayment of the prepay.



Principal Exposure Discussion:

The advance, both principal and interest, will be amortized with natural gas deliveries. The Buyer prepays Columbia for a fixed quantity of gas to be delivered over a specified schedule of time and volume. Columbia will purchase surety bonds from a group of US insurers as credit enhancement for the long-term performance obligation. (The surety bonds are structured such that drawing can occur similar to a performance LC drawing. The available amount under the surety bond will reduce as gas deliveries are met.) The deliveries will be satisfied by Columbia's produced hydrocarbons or gas purchased in the market. If CNR is unable to deliver the gas to the Buyer, the Buyer can exercise its Columbia guarantee for the full amount remaining. If Columbia fails to perform under its guarantee, the Buyer can draw on the surety bonds in an amount equal to the replacement value of the future gas deliveries, however, the drawing cannot exceed the remaining face amount of the bond. Chase, as creditor to the Buyer, is assigned a secured interest in the bond proceeds. The Prepay will be fully supported by Surety Bonds issued by a group of Insurance Companies rated "A+" or better.

Fractional Exposure Discussion

Upon executing the prepaid forward sale with the Buyer, Columbia assumes a significant fixed price short position at the current strip prices, which results in fractional exposure to Columbia. This exposure is laid off through offsetting transactions. Total FE is about 24% of the prepay amount or $60 MM.

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Requested by JPMC

Company's Business:

Columbia Transmission and Columbia Gulf provide an array of natural gas transportation and storage services for local distribution companies and industrial and commercial customers who contract directly with producers or marketers for their gas supplies.

In 1999, Columbia Transmission completed construction of the largest ever expansion of its storage and transportation system. The expansion adds approximately 500,000 Mcf (thousand cubic feet) per day of firm storage to 23 customers. Columbia Transmission is also participating in the proposed 442-mile Millennium Pipeline Project that has been submitted to the FERC for approval. As proposed, the project will transport approximately 700,000 Mcf of natural gas per day from the Lake Erie region to eastern markets.

Distribution Operations
Columbia's five distribution subsidiaries provide natural gas service to nearly 2.1 million residential, commercial and industrial customers in Ohio, Pennsylvania, Virginia, Kentucky and Maryland. Approximately 32,400 miles of distribution pipelines serve these major markets. The distribution subsidiaries have initiated transportation programs that allow residential and small commercial customers the opportunity to choose their natural gas suppliers and to use the distribution subsidiaries for transportation service. This ability to choose a supplier was previously limited to larger commercial and industrial customers.

Exploration and Production Operations
Columbia's exploration and production subsidiary, Columbia Natural Resources, Inc. (Columbia Resources), explores for, develops, gathers and produces natural gas and oil in Appalachia and Canada. As of December 31, 1999, Columbia Resources held interests in approximately 3.9 million net acres of gas and oil leases and had proved reserves of 985.8 billion cubic feet of natural gas equivalent. Columbia Resources owns and operates 8,188 wells and 6,069 miles of gathering facilities and has expanded its reserve base and production through an aggressive drilling and acquisition program. During 1999, Columbia Resources purchased 800 wells, gathering assets and approximately 800,000 undeveloped acres in the U.S. and Canada. In August 1997, Columbia Resources acquired Alamco, Inc. (Alamco), an Appalachian gas and oil exploration and development company. Through Columbia Resources' operations in north-central West Virginia, southern Kentucky, northern Tennessee and New York, it is one of the largest-volume independent natural gas and oil producers in the Appalachian Basin.

Energy Marketing Operations
The energy marketing segment includes Columbia Energy Services that consists of a retail mass marketing business, an internet based service and a wholly-owned subsidiary that provides energy related services and products. Also included in the energy marketing segment are the operations of Columbia Propane Corporation (Columbia Propane).

As a result of an ongoing strategic assessment in 1999, Columbia Energy Services decided to focus its efforts on the Mass Markets business, which provides energy products to smaller volume retail customers, and to exit the Wholesale and Trading and Major Accounts businesses. The Wholesale and Trading business was sold at the end of 1999 and the Major Accounts business is being offered for sale. These businesses are recorded as discontinued operations, in accordance with generally accepted accounting principles.

Columbia Propane sells propane at wholesale and retail and has been aggressively expanding its operations through acquisitions and internal growth. At the end of 1999, Columbia Propane served more than 350,600 customers in 31 states and the District of Columbia, which is more than triple the number of customers served at the end of 1998. Columbia Petroleum Corporation, a subsidiary of Columbia Propane, owns and operates petroleum assets and had sales of 202.4 million gallons in 1999 with approximately 42,600 customers in five states.

Power Generation, LNG and Other Operations
Columbia Electric Corporation (Columbia Electric) is an unregulated electric generation company whose primary focus is the development, ownership and operation of clean, natural gas fueled power projects. Columbia currently has three operating facilities totaling 248 megawatts, one 550-megawatt (equivalent) plant under construction in Gregory, Texas and approximately 3,000 megawatts of gas-fired generation under development. Publicly announced projects in Columbia Electric's development portfolio include the Kelson Ridge Project in Charles County, Maryland, the Liberty Electric Project in Eddystone, Pennsylvania, the Grassy Point Energy Project in Haverstraw, New York, the Ceredo Electric Generating Station in Ceredo, West Virginia and the Henderson Generating Station in Henderson, Kentucky. As part of the NiSource merger, Columbia will sell Columbia Electric.

In December 1999, a limited partnership company established between Columbia Electric and Atlantic Generation, Inc. completed a transaction terminating a long-term power purchase contract. Columbia Electric's portion was approximately $71 million pre-tax under the terms of the buyout. The partners will continue to operate the facility as a merchant power plant.

Columbia LNG Corporation and an affiliate company own an LNG facility, located in Cove Point, Maryland, which is one of the largest natural gas peaking and storage facilities in the United States. The facility has the capacity to liquify natural gas at a rate of 15,000 Mcf of natural gas per day. The facility enables LNG to be stored until needed for the winter peak-day requirements of utilities and other

large gas users

Columbia Network Services Corporation (Columbia Network), a wholly-owned subsidiary of Columbia, and its subsidiaries provide telecommunications and information services and assist personal communications service providers and other microwave radio service licensees in locating and constructing antenna facilities.

Industry Analysis:

The oil and gas business is highly competitive in searching and acquiring additional reserves and in marketing oil and natural gas. Columbia's competitors include the major and intermediate size oil companies, independent oil and gas concerns, and individual producers or operators.

The natural gas transmission industry, although regulated, is very competitive. Since the mid 1980s, customers have switched their volumes from a bundled merchant service to transportation service by acquiring gas supply under unregulated arrangements such as those provided by marketing and Citrus Trading Corp. Columbia competes with several pipelines for the transportation business of its customers and at times discounts its transportation rates in order to maintain market share. Natural gas is sold in competition with fuel oil, coal, liquefied petroleum gases, electricity and heavy crude oil. It must also compete with alternative fuel such as residual fuel oil which has been priced below the comparable price of natural gas in industrial and electric generation markets.

Competition in the gas marketing and power marketing businesses is intense and is expected to remain so due to the large number of industry participants despite growing consolidation in the gas marketing industry.

The oil and gas environment can be characterized as follows: volatile gas prices, improving exploration and production technology incremental gas supplies and growth in the gas markets. Along with volatile gas prices, there is a faster supply response time, and a more aggressive use of storage and availability of derivatives. Improvements in technology can be seen from 3-dimensional seismic analysis and completion techniques that will enhance productivity and improve economics.

The industry is heading towards deregulation and restructuring in the electric industry, consolidation/alliances in all industry segments and international power development. Consolidation and alliances are occurring to achieve cost reduction and geographic expansion In developing countries there is a growing demand for these industries. However, due to the perceived risk of operating in those territories, there is a risk/reward trade-off which companies must consider.

Discussion of Risks and Mitigating Factors:

Seasonal Risks: Seasonality plays an important role in the pipeline segment due to its affect on demand. Demand for fuel in agricultural areas and urban areas have sensitivity to seasonal and weather conditions.
Mitigants: Columbia's management team has extensive experience dealing with the seasonal pressures of the industry Liquidity needs in the nonpeak season are met via internally generated cash flows as well as committed revolving credit facilities.

Volatility of Oil & Gas Market Prices: Columbia's operational revenues are sensitive to prices of and demand for natural gas As such, Columbia is particularly exposed to the volatility of natural gas prices.
Mitigants: Historically the company has been able to mitigate the risk of adverse price fluctuations by entering into hedging contracts Furthermore, their business is sufficiently diversified by non-price sensitive businesses.

Environmental Risks: Columbia, as all other pipeline companies, face environmental regulations set by federal, state and local governments regarding water, air and land pollution.
Mitigants: Columbia's transmission subsidiaries have implemented programs to continually review compliance with existing environmental standards Columbia Transmission is currently conducting assessment, characterization and remediation activities at specific sites under a 1995 Environmental Protection Agency ("EPA") Administrative Order by Consent.

Competitive Risks: There is always a risk that new pipelines will be constructed in a given market. Also, other common carriers and pipelines owned and operated by large integrated oil companies pose as potential competition to Columbia.
Mitigants: High capital costs, governmental tariff regulation, environmental and legal considerations, and problems in acquiring rights-of-way make new pipelines difficult to develop

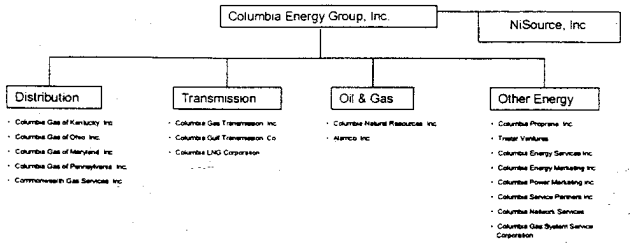
Management/ Sponsor

Columbia's management team is led by Chief Executive Officer and President Oliver G. Richard III (48). Mr. Richard has considerable industry expertise, having served in his current role since April 1995, with prior work experience most recently as Chairman, President and Chief Executive Officer, New Jersey Resources Corporation, 1992 to 1995, and formerly President and Chief Executive Officer of Northern Natural Gas Company, 1989 to 1991. Columbia's senior management team also includes Michael W. O'Donnell, Senior Vice

President and Chief Financial Officer, who has been with the Company since 1971, and in his current capacity since 1993 Each of the business units is run individually by a seasoned industry executive

In July 1999, a newly appointed president and chief executive officer of Columbia Energy Services reduced the level of trading activity at Columbia Energy Services while an ongoing evaluation is conducted to restructure the trading operations. During this period, trading activity will focus on managing physical assets and better aligning these operations with the needs in gas and power sales. As a result, Columbia Energy Services no longer engages in open position trading in power and further trading in weather derivatives has been curtailed. Positions in natural gas, electric power and weather derivatives continue to be controlled within predetermined limits as provided by Columbia's senior management. Columbia's policy prohibits any Columbia subsidiary from entering into trading positions that are not effectively connected with its business. The risks associated with these trading activities are managed consistent with policies approved by Columbia's Board of Directors. Market risks are monitored by an independent risk control group operating separately from the area that creates or actively manages these risk exposures in compliance with Columbia's stated risk management policies.

Corporate Structure



Capital Structure and Credit Statistics:

($millions)	1997	1998	1999	LTM 3/31/00
Sales	5,041.0	2,628.0	3,189.2	3,152.9
EBITDA	730.7	775.2	845.7	869.0
Total Debt	2,331.6	2,147.9	2,416.5	2,129.9
Book Equity	1,790.7	2,005.3	2,064.0	2,157.9
Interest Expense	157.6	152.4	164.4	172.6
Depreciation & Amortization	221.3	235.2	229.0	222.8
Capex	519.9	462.9	462.3	456.7
Dividends	49.9	63.9	71.8	73.5
EBITDA/Interest	4.6x	5.1x	5.1x	5.0x
EBITDA-Capex/Interest	1.3x	2.1x	2.3x	2.4x
Total Debt/Book Cap	56.6%	51.7%	53.9%	49.7%
Total Debt/EBITDA	3.2x	2.8x	2.9x	2.5x

Financial Analysis:

LTM 3/31/00 Financial Performance

Total consolidated net revenue (operating revenues less associated products purchased costs) for the three months ended March 31, 2000, was $681.6 million, a $31.3 million increase over the same period last year. The increase was primarily attributable to higher gas prices along with a 33% increase in gas production. In addition, several propane and petroleum acquisitions in 1999 increased net revenues. Tempering this improvement were lower revenues from the sale of base gas volumes for the transmission and storage segment and reduced gas sales by the distribution segment due to warmer weather.

Operating expenses for the first quarter of 2000 were $398 2 million, an increase of $31 6 million over the same period last year due to the $29 8 million reduction in the first quarter of 1999 operating expenses for the producer settlement. This was partially offset by lower gross receipts and property taxes and the beneficial effect of Columbia Transmission's Voluntary Incentive Retirement Program. Also decreasing operating expense during the first quarter of 2000 was a reduction in depreciation expense, consistent with the terms of Columbia of Ohio's 1999 regulatory settlement. These reductions were tempered by higher operation and maintenance expense in the current period associated with Columbia Propane's 1999 acquisitions.

A significant portion of Columbia's operations are subject to seasonal fluctuations in cash flow. During the heating season, which is primarily from November through March, cash receipts from sales and transportation services typically exceed cash requirements. Conversely, during the remainder of the year, cash on hand, together with external short-term and long-term financing, as needed, is used to purchase gas to place in storage for heating season deliveries, perform necessary maintenance of facilities, make capital improvements in plant and expand service.

Net cash from continuing operations for the first quarter of 2000 was $431 5 million, essentially unchanged from the same period last year

Coverage, measured by EBITDA to interest, has remained improved slightly to 5.0x in the LTM period from 5.1x at the end of 1999 Leverage decreased as Columbia continues to decrease its debt position Debt to book capitalization has declined from 53.9% at the end of 1999 to 49 7% in the LTM period.

Three Months Ended March 31, 2000 – Segment Analysis

Transmission and Storage Operations

$MM	Three Months Ended 3/31/00	Three Months Ended 3/31/99
Operating Revenues		
Transportation	$185.6	$182.4
Storage	44.6	50.3
Other	14.9	20.6
Total Operating Revenues	$245.1	$253.3
EBITDA	$151.2	$170.9
Operating Income	$123.9	$144.2
Throughput (Bcf)		
Columbia Transmission	378.1	394.0
Columbia Gulf		
Mainline	145.7	147.4
Short-haul	57.5	50.6
Intrasegment Elim	(140.4)	(138.7)
Total Throughput	440.9	453.3

Distribution

$MM	Three Months Ended 3/31/00	Three Months Ended 3/31/99
Net Revenues		
Sales revenues	$627.8	$911.1
Less: Cost of gas sold	425.2	666.6
Net Sales Revenues	$202.6	$244.5
Transportation Revenues	130.7	107.0
Less: Associated Gas Costs	12.7	9.9
Net Transportation Revenues	$118.0	$97.1
Net Revenues	$320.6	$341.6
EBITDA	$152.8	$166.2
Operating Income	$131.2	$130.2
Throughput (Bcf)		
Total Sales	79.3	93.0
Transportation	123.3	107.9
Total Throughput	202.6	200.9
Off-System Sales	7.1	156.3
Total Sold or Transported	209.7	357.2

Exploration and Production

$MM	Three Months Ended 3/31/00	Three Months Ended 3/31/99
Operating Revenues	$52.5	$30.5
EBITDA	$33.2	$15.1
Operating Income	$20.8	$5.6
Gas Production (Bcf)		
US	14.1	10.6
Canada	0.0	0.0
Total	14.1	10.6
Oil Production (Mbbl)		
US	43.0	36.0
Canada	3.0	3.0
Total	46.0	39.0

Energy Marketing

$MM	Three Months Ended 3/31/00	Three Months Ended 3/31/99
Net Revenues		
Gas Revenues	$116.1	$32.7
Propane Revenues	65.6	40.3
Petroleum Revenues	85.1	0.0
Total Operating Revenues	$266.8	$73.0
Less: Products Purchased	214.1	52.7
Gross Margin	$52.7	$20.3
EBITDA	$15.6	$1.3
Operating Income	$9.7	($0.7)
Marketing Sales		
Gas (Bcf)	13.6	11.2
Propane (Millions of Gallons)	109.4	39.0
Petroleum (Millions of Gallons)	90.6	0.0

Power Generation, LNG and other

$MM	Three Months Ended 3/31/00	Three Months Ended 3/31/99
Operating Revenues		
Power Generation	$0.5	$2.0
LNG	2.0	2.3
Other	1.1	0.2
Total Operating Revenues	$3.6	$4.5
EBITDA	$0.2	($0.6)
Operating Income	$0.2	($0.6)

1999 Financial Performance

Total net revenues (revenues less associated product purchased costs) of $1,994.8 million for 1999 reflected an increase of $132.9 million over 1998 primarily due to a gain recorded for the settlement of a co-generation power purchase contract, the impact of 1999's colder weather, increased transportation services and higher production for the exploration and production operations. Also providing higher net revenues was the effect of recent acquisitions for the propane and petroleum operations. Reduced prices for natural gas production and a reduction to revenues resulting from a Columbia of Ohio regulatory settlement partially offset these improvements.

Total operating expenses for 1999 were $1,346.4 million, an increase of $65.8 million over 1998. Operation and maintenance expense increased $108.3 million, due to higher expenses for the energy marketing and exploration and production segments, due in part to recent acquisitions for Columbia Energy Resources Corporation (Columbia Resources) and Columbia Propane Corporation (Columbia Propane) and increased costs for Columbia Energy Services, and a $25.4 million favorable adjustment in 1998 for a settlement gain related to postretirement benefit costs. Also increasing 1999 operation and maintenance expense were costs related to Columbia's response to an unsolicited tender offer.

Interest expense and related charges of $164.4 million increased $19.9 million due largely to higher short-term borrowings to finance recent acquisitions and to fund Columbia's stock repurchase program.

Net cash from continuing operations in 1999 of $825.8 million reflected a decrease of $19.9 million from 1998 due primarily to normal working capital changes.

Coverage, measured by EBITDA to interest, has remained steady at 5.1x from 1998 to 1999. Leverage increased slightly as the

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Company continues to grow by increasing its debt burden. Debt to book capitalization increased slightly from 51.7% in 1998 to 53.9% in 1999, again due to the slight increase in debt.

1999 Operating Income by Segment:

Transmission and Storage:

In 1999, operating income for the transmission and storage segment of $350.1 million increased $24 million over 1998. This increase primarily reflected the pre-tax effect of a producer settlement and additional revenues primarily resulting from Columbia Transmission's market expansion project. The 1998 results benefited from reduced post-retirement benefit costs and Columbia Gulf's regulatory settlement. Both periods included base gas sales, $14.7 million in 1999 and $13.9 million in 1998.

Distribution Segment:

Operating income for 1999 of $254.6 million increased $28.8 million over 1998, primarily due to the increase in net revenues, reduced operating expenses attributable to lower gross receipts and property taxes and, as noted above, the terms of the 1999 Columbia of Ohio regulatory settlement resulted in reduced depreciation expense. In 1998, operating expenses were reduced due to a $16.5 million settlement gain related to post-retirement benefits costs that reflected the purchase of insurance for a portion of those liabilities.

Exploration and Production Segment:

Operating income of $44.2 million for 1999 increased $7 million over 1998 as the increase in operating revenues discussed above was partially offset by $10.3 million higher operating expenses associated with an expanded operation due in part to recent acquisitions, additional gathering facilities and drilling activity.

Energy Marketing

In 1999, an operating loss of $54.5 million was recorded compared to an operating loss of $13.6 million in 1998. The improvement in net revenues was more than offset by higher operating costs for Columbia Energy Services' retail operations that included additional investment in its infrastructure. The operating loss for Columbia Energy Services for 1999 was $50.6 million compared to $17.7 million in 1998. Included in the higher costs for Columbia Energy Services was $14.3 million recorded in 1999 to reflect the write-down of certain computer software no longer necessary for its operations and an adjustment for uncollectible accounts. In addition, higher costs were incurred by Columbia Propane due to its expanded operations and the ongoing process of integrating recent propane and petroleum acquisitions.

Power Generation, LNG and other operations

Operating income for 1999 of $71.5 million increased $64.9 million over 1998 primarily reflecting the increase in operating revenues, which was partially offset by a $4.5 million increase in operation and maintenance expense due to increased staffing levels and development activity for the cogeneration business.

1998 Financial Performance

Total net revenues of $1,897.1 MM for 1998 reflected a decrease of $18.4 MM from 1997, due primarily to the adverse effect of warmer weather in 1998 on gas sales for the distribution segment. The impact of warmer weather was partially offset by a $22.1 MM increase in the marketing segment's gross margin due to higher gas sales and the addition of electric power sales in 1998, as well as higher revenues from transportation services and gas management activities in the transmission and distribution segments. Also improving revenues in 1998 was a $13.4 MM increase resulting from the gain on the sale of storage base gas volumes and higher revenues from increased gas production and prices. Natural gas sales for Columbia's marketing segment in 1998 totaled 1,561 Bcf, nearly twice the level for the same period last year, while its 1998 electric power sales were 14,364 Gigawatt hours.

Total operating expenses of $1,357.1 MM for 1998 decreased $49 MM compared to 1997, largely reflecting a reduction of $60.7 MM in operation and maintenance expense. The lower operation and maintenance expense was primarily the result of a $25.4 MM reduction in the cost of certain postretirement benefits. The transmission and storage segment's and the distribution segment's operation and maintenance expense also decreased in 1998 as a result of cost conservation measures and efficiencies gained through recently implemented restructuring activities. Overall depreciation and depletion expense increased $13.9 MM due primarily to an increase in depletion expense for the exploration and production segment resulting from a higher depletion rate, together with the effect of increased production from both the acquisition of Alamco, Inc. and the success of Columbia Energy Resources Inc.'s drilling program.

Interest expense of $152.4 MM in 1998 decreased $5.2 MM from 1997, primarily reflecting a reduction to interest expense for a 1998 tax settlement, involving tax issues from 1991-1994, partially offset by additional interest expense on prepayments received from third

parties for gas to be delivered in future periods

Net cash from operations for 1998 was $761.7 MM, an increase of $293.5 MM over 1997. The increase primarily reflects higher prepayments received for the future delivery of natural gas by Columbia, offset by a decrease in the overrecovery of gas costs by the distribution segment as well as the effect of warm weather in 1998. The decrease in the overrecovery position reflects higher gas prices in the current period compared to the same period in 1997.

Improved financial performance has helped the Company's credit profile. Coverage, measured by EBITDA to interest, has steadily improved from 4.2x in 1996 to 5.1x in 1998. Leverage is continuing to fall as the Company continues to grow without increasing its debt burden. Debt to book capitalization has declined from 59.2% in 1996 to 51.7% in 1998.

1998 Operating Income by Segment:

Transmission and Storage:

Operating income for 1998 of $225.8 MM increased by 0.7% from 1997, as the 5.7% decline in net revenue was more than offset by a 7.8% decrease in operating expenses. Operation and maintenance expense for 1998 decreased 12.3% to $386.7 MM, primarily reflecting a reduction in post-retirement benefit costs and the ongoing beneficial impact of the restructuring initiatives implemented in 1997. Other taxes decreased 1.6% from 1997, primarily due to lower payroll taxes and depreciation expense increased by 5.1% due in part to plant additions.

Distribution Segment:

Operating income for 1998 of $225.8 MM increased by 0.7% from 1997, as the 5.7% decline in net revenue was more than offset by a 7.8% decrease in operating expenses. Operation and maintenance expense for 1998 decreased 12.3% to $386.7 MM, primarily reflecting a reduction in post-retirement benefit costs and the ongoing beneficial impact of the restructuring initiatives implemented in 1997. Other taxes decreased 1.6% from 1997, primarily due to lower payroll taxes and depreciation expense increased by 5.1% due in part to plant additions.

Exploration and Production Segment:

In 1998, operating income improved by 20.4% to $37.2 MM, primarily due to higher operating revenues, which were partially offset by an increase of 32.3% in depreciation and depletion expense due to additional investments in acquisitions and drilling. Revenues for 1998 were $127.5 MM, an increase of 12.5% over 1997, primarily reflecting higher revenues generated from hedging activities and the gas production increase. Columbia's average gas sales price for 1998 was $2.91 per Mcf, an increase of 11% from 1997. The strong natural gas prices reflect the benefit of hedging a portion of 1998 production in late 1997 when prices were significantly higher.

Marketing, Propane and Power Generation Segment:

Marketing's 1998 operating loss of $59 MM was $45.8 MM greater than the $13.2 MM loss in 1997, due to 1998 operating expenses that were 200% higher than the year earlier. The higher expenses related to the implementation of Columbia Energy Services' strategy to build its systems and infrastructure, including adding and retaining qualified staff. Included in these higher expenses was the $16.3 MM reserve, discussed above, and higher current period expenses for costs associated with the development of new products and services and customer acquisition costs related to adding new Mass Market retail customers.

Propane and power generation's operating income of $10.7 MM for 1998 decreased 34.4% from 1997, primarily reflecting the 3.7% decline in net revenues and 8.6% increase in operating expenses due to the recent propane acquisitions and additional start-up costs for new services

Steven G. Wood, Lender | Jim Ballentine, Credit | Chris Wardell, Credit

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Requested by JPMC

Chase Manhattan Southwest
1221 McKinney #3000
Houston, Texas 77010

CHASE

October 27, 1994

Confidential and Proprietary

Mr. Michael Kopper
Director
Enron Capital and Trade Resources
1400 Smith
Houston, Texas 77251

Re: Prepaid Crude Oil Forward Sale

Dear Michael,

In response to your request, we are pleased to deliver three alternative proposals for a new prepaid crude oil forward sale to be underwritten by Chase. Although these proposals are subject to final documentation and final credit approval, we are confident we can execute and fund each of the presented options well within the previously discussed timetable. As you will notice in each of the attached term sheets, the proposals can be executed and funded in an amount up to $300 Million. Each proposal incorporates a five year tenor, thus allowing for a more extended delivery schedule than that currently in place under the Mahonia transaction. We have also provided a menu of delivery and commodity price options. A diagram of the transaction parties is also attached.

- Option 1 - The first term sheet represents an extension of the Mahonia prepay structure to a five year quarterly delivery schedule. In this option (as well as in Options 2 and 3) we have incorporated the principles of our previously negotiated collateral arrangements to minimize the risk of adverse price movement over the term of the contract.

- Option 2 - The second term sheet presents a quarterly amortizing prepayment obligation, over five years, which calls for delivery of a certain dollar amount of oil on each delivery date. With this structure, the oil price for any delivery - and therefore the barrel obligation - can be fixed by Enron with the SPC at any time before that delivery date. This feature gives Enron the flexibility to match its delivery obligations, on a delivery date by delivery date basis, with either fixed or floating price sales.

- Option 3 - The third term sheet presents the same variable price option as utilized in the second structure, but also grants an additional delivery option to Enron. This structure allows Enron to deliver oil on any date or dates throughout the entire contract term (again, five years), thus allowing Enron great flexibility. This delivery flexibility can be utilized to most accurately match Enron's future tax, accounting, operating and funding requirements.

Permanent Subcommittee on Investigations
EXHIBIT #187ll

Each of these proposals would incorporate a performance letter of credit, as in the Mahonia transaction, to syndicate Enron's oil delivery performance obligation.

With respect to transaction costs, we have set the LIBOR margin for Enron's current senior debt rating at an initial level of 0.375% for each of the three options. Our ability to offer this competitive margin is facilitated by the use of the performance letter of credit in the syndication of Enron performance risk. Because such an instrument is less capital attractive than a funded asset, syndicate banks will accept reduced letter of credit fees. This reduced cost is passed through to ECTR in the form of the reduced LIBOR margin. The second component of Chase compensation is the proposed arrangement fee. The Option 1 arrangement fee of 0.175% represents a substantial reduction relative to the previously executed Mahonia transaction, based on our view that this structure has become relatively common in the market. The higher arrangement fees for Option 2 (0.35%) and Option 3 (0.55%) reflect the proprietary nature and flexibility encompassed in these options. While the structures and pricing discussed above are based upon a collateralized transaction, Chase is also prepared to price a non-collateralized structure.

Please call Rick Walker at 751-5602, Dinsa Mehta at 212-552-1255, or Todd Dittmann at 751-5607 with any questions you may have. We look forward to meeting with you tomorrow.

Sincerely,

The Chase Manhattan Bank, N.A.

Rick Walker
Vice-President

Todd Dittmann
Associate

Attachments

PREPAID CRUDE OIL FORWARD SALE - OPTION 1

TERM: 5 Years.

AMOUNT: *up to* $300 Million payment for future oil deliveries.

CONTRACT PARTIES:

Purchaser Mahonia Limited or an SPC established by Chase.
Seller A wholly owned subsidiary of Enron Corp.

OIL DELIVERIES: Equal quarterly installments from March 1995 to December 1999.

REVENUE PREPAYMENT COST: Oil revenues prepaid at a rate of LIBOR plus a margin determined by senior debt rating as follows:

Greater than BBB+ or Baa1	Greater than BBB- and Baa3	Less than BBB- or Baa1
30.0 Bps	37.5 Bps	62.5 Bps

Adjustments in LIBOR margin during contract term shall be made through adjustments in barrels delivered to be determined at the end of the term.

ARRANGEMENT FEE: 0.175%.

COSTS: Legal fees and customary transaction costs.

DOCUMENTATION: Standard Enron-Mahonia documentation with the addition of the Security Agreement attached to the Enron Risk Management Services-Chase ISDA trading agreement, to cover collateral for mark-to-market exposures.

SYNDICATION: Enron performance obligation, pursuant to guarantee of Seller delivery obligation, to be syndicated through a performance letter of credit ("PLC"). PLC upfront and usage costs to be paid by Chase.

CHASE

PREPAID CRUDE OIL FORWARD SALE
FLOATING PRICE FACILITY - OPTION 2

TERM:	5 Years.
AMOUNT:	*up to* $300 Million payment for future oil deliveries.
CONTRACT PARTIES:	
Purchaser	Mahonia Limited or an SPC established by Chase.
Seller	A wholly owned subsidiary of Enron Corp.
OIL DELIVERIES:	Equal quarterly installments from March 1995 to December 1999.
FLOATING PRICE FACILITY:	Each oil delivery obligation will equal, in barrels of oil, a set dollar amount. The oil price for any delivery - and therefore the barrel obligation - can be fixed by Enron with the SPC at any time before that delivery date. Enron also has the facility to initially position its oil sales to Mahonia to any date(s) before the final delivery dates (with the intention to roll out to each final delivery date). The roll adjustment is expressed in terms of incremental barrels of oil.
REVENUE PREPAYMENT COST:	Oil revenues prepaid at a rate of LIBOR plus a margin as determined in Option 1.
ARRANGEMENT FEE:	0.30%. 0.30% Rec 11-9-94
COSTS:	Legal fees and customary transaction costs.
DOCUMENTATION:	Standard Enron-Mahonia documentation with the addition of the Security Agreement attached to the Enron Risk Management Services-Chase ISDA trading agreement, to cover collateral for mark-to-market exposures.
SYNDICATION:	Enron performance obligation, pursuant to guarantee of Seller delivery obligation, to be syndicated through a performance letter of credit ("PLC"). PLC upfront and usage costs to be paid by Chase.

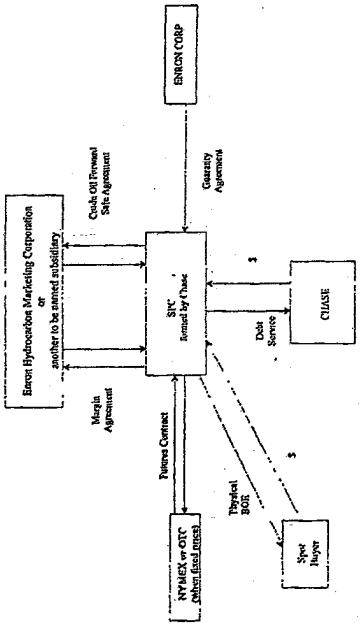
CHASE

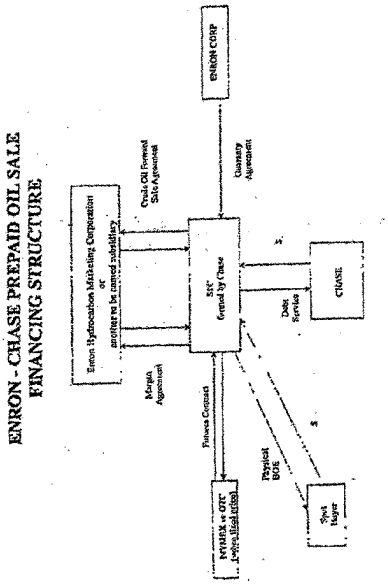
PREPAID CRUDE OIL FORWARD SALE
FLEXIBLE DELIVERY STRUCTURE - OPTION 3

TERM:	5 Years.
AMOUNT:	*up to* $300 Million payment for future oil deliveries.
CONTRACT PARTIES:	
Purchaser	Mahonia Limited or an SPC established by Chase.
Seller	A wholly owned subsidiary of Enron Corp.
OIL DELIVERIES:	Seller may deliver oil on any date(s) before March 2000.
FLOATING PRICE FACILITY:	The initial delivery obligation is set to March 2000 and will equal, in barrels of oil, a set dollar amount. The oil price - and therefore the barrel obligation - can be fixed by the Seller with the SPC at any time before delivery date. Roll adjustments to ultimate delivery dates will be expressed in terms of incremental oil barrels.
REVENUE PREPAYMENT COST:	Oil revenues prepaid at a rate of LIBOR plus a margin as determined in Option 1.
ARRANGEMENT FEE:	0.55%.
COSTS:	Legal fees and transaction costs.
DOCUMENTATION:	Standard Enron-Mahonia documentation with the addition of the Security Agreement attached to the Enron Risk Management Services-Chase ISDA trading agreement, to cover collateral for mark-to-market exposures.
SYNDICATION:	Enron performance obligation, pursuant to guarantee of Seller delivery obligation, to be syndicated through a performance letter of credit ("PLC"). PLC upfront and usage costs to be paid by Chase.

CHASE

ENRON - CHASE PREPAID OIL SALE
FINANCING STRUCTURE




ENRON - CHASE PREPAID OIL SALE
FINANCING STRUCTURE
ENRON CORP
Guaranty Agreement
Enron Hydrocarbon Marketing Corporation
or
another ex be named subsidiary
Crude Oil Forward Sale Agreement
SPE
Owned by Chase
CHASE
Debt Service
Margin Agreement
Futures Contract
Physical EOS
Spot Market

May 11, 1999

Mr. Bill Brown
Vice President

Mr. Phil Sisneros
Director

Enron Capital Management
1400 Smith Street
Houston, TX 77002-7361

By Facsimile: (713) 646-3422

Dear Bill & Phil:

We appreciate your consideration in taking time to review the Enron capital structure, both on and off-balance sheet, with us. While we believe Chase understands the Enron corporate financing structure as well as anyone outside of your firm, we are equally sure that our understanding is incomplete. Your willingness to walk us through these issues will only help us in the process of adding value to your financing process and decisions. Below are some of the key issues we hope to address:

- Level of affiliate EBITDA supporting affiliate debt
- Identification of line items where different debt structures impact ENE financials
- Use of off-balance sheet preferreds and the dividend impact on ENE's financials
- Use of off-balance sheet debt not reflected on-balance sheet or in affiliate debt totals
- Use of FASB 125 off-balance sheet structures
- Timing and structure of CLN's including current targeted facilities.

As you can see from the above areas of focus, an underlying theme is both the level and structure of consolidated and non-consolidated cash flows used to support the varying on and off-balance sheet debt structures. Attached is our understanding of how ENE's financial statements might be impacted by various project structures. We have also included a list of Chase attendees. Once again we appreciate your availability on Friday, May 14 at 9:00 am. Please do not hesitate to call if you have any questions or concerns before hand.

Very truly yours,

Richard Walker Robert Traband

Permanent Subcommittee on Investigations
EXHIBIT #187mm

Chase Attendees

Global Oil & Gas
Richard Walker – Managing Director
Robert Traband – Vice President
Carrie Cerda – Associate

Global Bank Credit
Jim Biello – Co-head of Credit, Global Investment Bank
Chris Wardell – Senior Credit Deputy, Global Investment Bank
Gary Wright – Credit Deputy

Global Syndications
Chris Teague – Managing Director
George Serice – Vice President

Enron Meeting 5/14/99

Overview (12/31/98):

Consolidated Debt:		$7,357 million
(EOG: $780 million)		
Unconsolidated Affiliate Debt:		7,621 million
On-Balance Sheet Preferreds:		1,001 million
Off-Balance Sheet Preferreds:		
Preferred & Put (Condor)		1,500 million
Preferred (Marlin)		1,000 million
Preferred (Firefly)		1,000 million
Lease Commitment Guarantees		1,039 million
Prepaids (Chase Prepaids: $849.7 million)		
Liab. from Price Risk Mgmt	3,932 million	
Assets from Price Risk Mgmt	3,845 million	
Net Liab. from Price Mgmt		$87 million

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED INCOME STATEMENT

(In Millions, except Per Share Amounts)	Year Ended December 31, 1998	1997	1996
Revenues			
Natural gas and other products	$13,276	$13,211	$11,157
Electricity	13,939	5,101	980
Transportation	627	652	707
Other	3,418	1,309	445
Total Revenues	31,260	20,273	13,289
Costs and Expenses			
Cost of gas, electricity and other products	26,361	17,313	10,478
Operating expenses	2,352	1,496	1,421
Oil and gas exploration expenses	121	102	89
Depreciation, depletion and amortization	827	600	474
Taxes, other than income taxes	201	164	137
Contract restructuring charge	-	675	-
Total Costs and Expenses	29,862	20,258	12,599
Operating Income	1,378	15	690
Other Income and Deductions			
Equity in earnings of unconsolidated affiliates	97	216	225
Gains on sales of assets and investments	56	216	274
Other income, net	51	148	59
Income Before Interest, Minority Interests and Income Taxes	1,582	595	1,238
Interest and Related Charges, net	550	401	274
Dividends on Company-Obligated Preferred Securities of Subsidiaries	77	69	34
Minority Interests	77	80	75
Income Tax Expense (Benefit)	175	(90)	271
Net Income	703	105	584
Preferred Stock Dividends	17	17	16
Earnings on Common Stock	$ 686	$ 88	$ 568
Earnings Per Share of Common Stock			
Basic	$ 2.14	$ 0.32	$ 2.31
Diluted	$ 2.02	$ 0.32	$ 2.14
Average Number of Common Shares Used in Computation			
Basic	321	272	246
Diluted	348	277	270

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(In Millions)	Year Ended December 31, 1998	1997	1996
Earnings on Common Stock	$ 686	$ 88	$ 568
Other comprehensive income:			
Foreign currency translation adjustment	(14)	(21)	26
Total Comprehensive Income	$ 672	$ 67	$ 594

The accompanying notes are an integral part of these consolidated financial statements.

Prepays

Building/Other Leases

Marlin, Firefly, JEDI, JEDI II, Florida Gas, Azurix, Elektro

Consolidated Debt (w/ EOG)

Rawhide, Nighthawk, & EOG

Preferred Stock

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

(In Millions)	December 31, 1998	1997
ASSETS		
Current Assets		
Cash and cash equivalents	$ 111	$ 170
Trade receivables (net of allowance for doubtful accounts of $14 and $11, respectively)	2,060	1,372
Other receivables	833	454
Assets from price risk management activities	1,904	1,346
Inventories	514	336
Other	511	635
Total Current Assets	5,933	4,313
Investments and Other Assets		
Investments in and advances to unconsolidated affiliates	4,433	2,656
Assets from price risk management activities	1,941	1,038
Goodwill	1,949	1,910
Other	4,437	3,665
Total Investments and Other Assets	12,760	9,269
Property, Plant and Equipment, at cost		
Exploration and Production, successful efforts method	4,814	4,291
Transportation and Distribution	5,483	5,279
Wholesale Energy Operations and Services	4,858	3,879
Retail Energy Services	141	44
Corporate and Other	498	249
	15,792	13,742
Less accumulated depreciation, depletion and amortization	5,135	4,572
Property, Plant and Equipment, net	10,657	9,170
Total Assets	$29,350	$22,552

Marlin, Firefly, JEDI, JEDI II, Florida Gas, Azurix, Elektro

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

(In Millions, except Shares)	December 31, 1998	1997
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	$ 2,380	$ 1,754
Liabilities from price risk management activities	2,511	1,245
Other	1,216	817
Total Current Liabilities	6,107	3,816
Long-Term Debt	7,357	6,254
Deferred Credits and Other Liabilities		
Deferred income taxes	2,357	2,039
Liabilities from price risk management activities	1,421	876
Other	1,916	1,769
Total Deferred Credits and Other Liabilities	5,694	4,684
Commitments and Contingencies (Notes 3, 13, 14 and 15)		
Minority Interests	2,143	1,147
Company-Obligated Preferred Securities of Subsidiaries	1,001	993
Shareholders' Equity		
Second preferred stock, cumulative, no par value, 1,370,000 shares authorized, 1,319,848 shares and 1,337,645 shares of Cumulative Second Preferred Convertible Stock issued, respectively	132	134
Common stock, no par value, 600,000,000 shares authorized, 335,547,276 shares and 318,297,276 shares issued, respectively	5,117	4,224
Retained earnings	2,226	1,852
Accumulated other comprehensive income	(162)	(148)
Common stock held in treasury, 4,666,661 shares and 7,050,965 shares, respectively	(195)	(269)
Other	(70)	(175)
Total Shareholders' Equity	7,048	5,618
Total Liabilities and Shareholders' Equity	$29,350	$22,552

Prepays

Consolidated Debt (w/ EOG)

Rawhide & Nighthawk

Preferred Stock

Building/Other Leases

Footnotes

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS

(In Millions)	Year Ended December 31, 1998	1997	1996
Cash Flows From Operating Activities			
Reconciliation of net income to net cash provided by operating activities			
Net income	$ 703	$ 105	$ 584
Depreciation, depletion and amortization	827	600	474
Oil and gas exploration expenses	121	102	89
Deferred income taxes	87	(174)	207
Gains on sales of assets and investments	(62)	(195)	(274)
Changes in components of working capital	(233)	(65)	142
Net assets from price risk management activities	350	201	15
Merchant assets and investments:			
Realized gains on sales	(628)	(136)	-
Proceeds from sales	1,434	339	-
Additions	(721)	(308)	(192)
Other operating activities	(218)	(158)	(161)
Net Cash Provided by Operating Activities	1,640	211	884
Cash Flows From Investing Activities			
Capital expenditures	(1,905)	(1,192)	(864)
Equity investments	(1,659)	(700)	(619)
Proceeds from sales of investments and other assets	239	473	477
Acquisition of subsidiary stock	(180)	-	-
Business acquisitions, net of cash acquired (see Note 2)	(106)	(82)	-
Other investing activities	(354)	(445)	(68)
Net Cash Used in Investing Activities	(3,965)	(2,146)	(1,074)
Cash Flows From Financing Activities			
Issuance of long-term debt	1,903	1,417	359
Repayment of long-term debt	(870)	(607)	(294)
Net increase (decrease) in short-term borrowings	(158)	464	227
Issuance of company-obligated preferred securities of subsidiaries	8	372	215
Issuance of common stock	867	-	102
Issuance of subsidiary equity	828	555	-
Dividends paid	(414)	(356)	(281)
Net (acquisition) disposition of treasury stock	13	(422)	5
Other financing activities	69	24	8
Net Cash Provided by Financing Activities	2,246	1,849	331
Increase (Decrease) in Cash and Cash Equivalents	(59)	(86)	141
Cash and Cash Equivalents, Beginning of Year	170	256	115
Cash and Cash Equivalents, End of Year	$ 111	$ 170	$ 256
Changes in Components of Working Capital			
Receivables	$(1,055)	$ 351	$ (678)
Inventories	(372)	63	(53)
Payables	433	(366)	870
Other	761	(113)	3
Total	$ (233)	$ (65)	$ 142

The accompanying notes are an integral part of these consolidated financial statements.

Prepays →

Rawhide & Nighthawk, Preferred →

Commodity Prepay Exposure Discussion

January 27, 2000

CHASE

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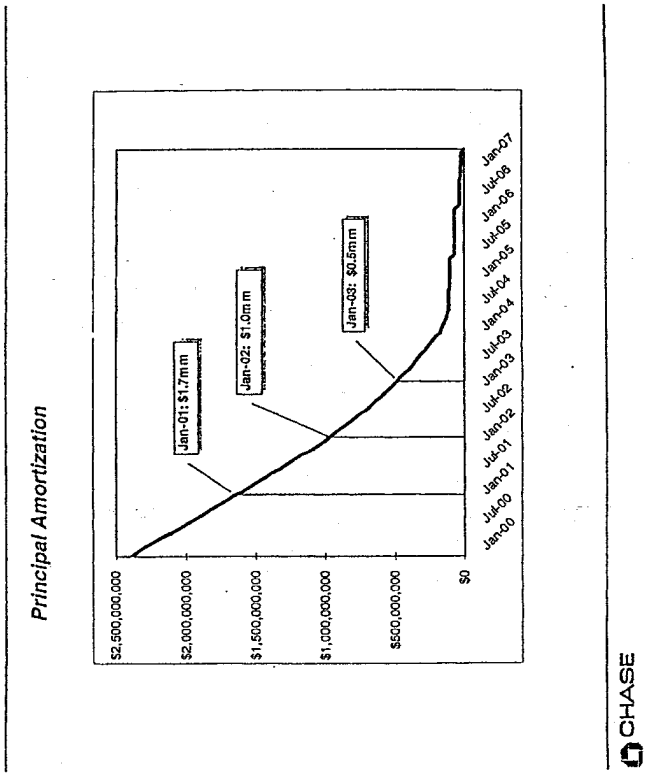
Permanent Subcommittee on Investigations
EXHIBIT #187nn



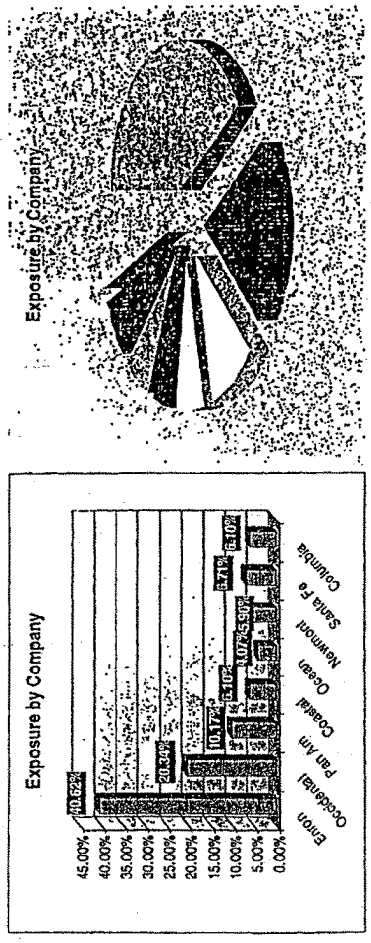
HIGHLY CONFIDENTIAL

Exposure by Client Rating

CHASE

HIGHLY CONFIDENTIAL

Exposure by Client



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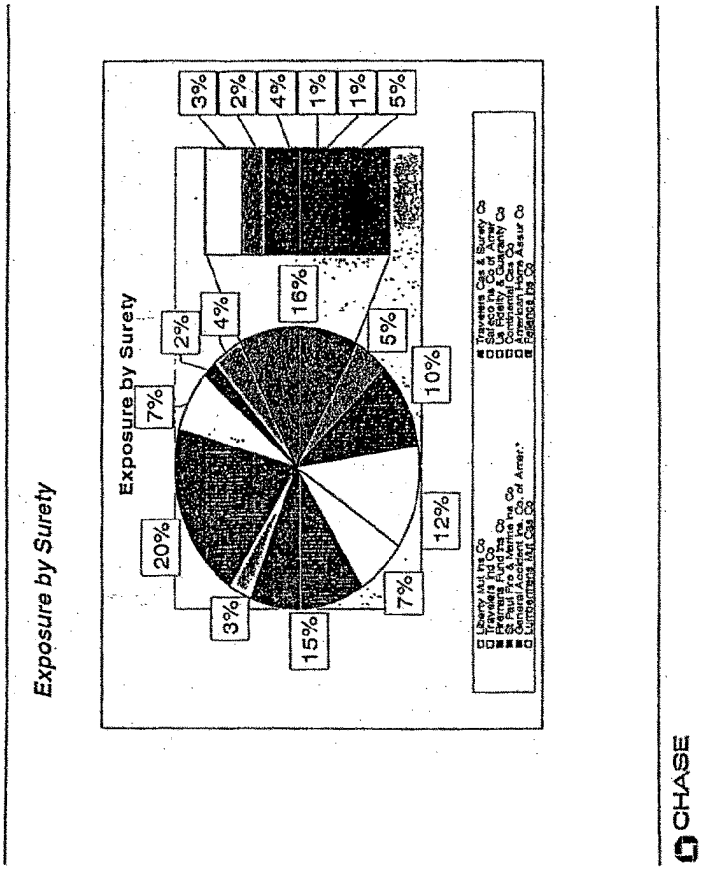

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Potential Deals

Client	Size	Probability	Adjusted Size
CMS Energy	$100,000,000	0.2	$20,000,000
El Paso/Coastal	$150,000,000	0.3	$45,000,000
Enron	$400,000,000	0.5	$200,000,000
Ocean Energy	$75,000,000	0.3	$22,500,000
Noble Affiliates	$150,000,000	0.3	$45,000,000
Barrett Resources	$100,000,000	0.4	$40,000,000
Husky Oil	$150,000,000	0.3	$45,000,000
Lat Am (PDVSA/Pemex)	$200,000,000	0.25	$50,000,000
Australia (Woodside/BHP)	$200,000,000	0.3	$60,000,000
Occidental Petroleum	$125,000,000	0.25	$31,250,000
Total			$558,750,000

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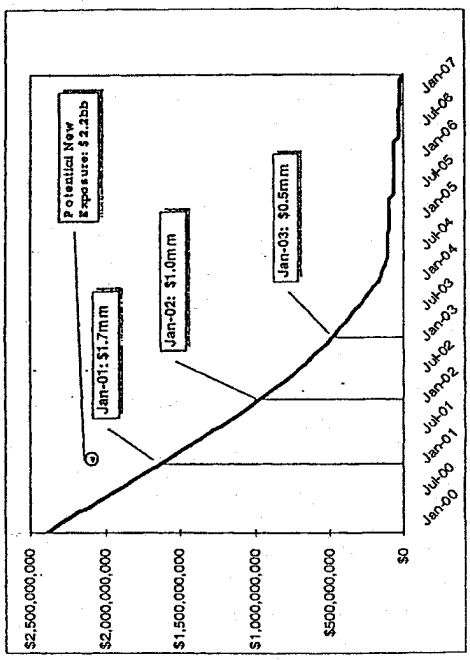
Principal Amortization



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Client Earnings

Client	Q4 Income (millions)	6/30/00 Share Price	1/27/00 Share Price	
Enron	$251	$40.875	$61.44	
Occidental	$383	$21.125	$20.50	
Coastal Corp	$499	$40.25	$37.00	
Ocean Energy	$3 (Est)	$9.625	$8.94	
Newmont Mining	$47	$19.875	$20.50	
Santa Fe Snyder	$16.6 (Est)	$7.1875	$8.00	
Columbia Energy	$95	$62.6875	$62.88	
Pan American	N/A	N/A	N/A	

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Looking Ahead

Dynamics / Challenges for 2000

I. Oil & Gas:

- $28 spot oil is a "double-edged sword"
  1. likely improvement in credit statistics and rating
  2. continued tightening oil sector credit spreads
- In addition to independent E&P's, the candidates for new deals will include utilities and pipelines (especially those with E&P activity)

II. Metals:

- Large Gold producers tend to be long cash
- Base metal candidates in North America are limited

III. General:

- Probing the "export" of the structure to selected natural resource clients in Europe / Asia
- Capacity/pricing in the re-insurance market; recently renewed treaties
- Funding syndication

CHASE — From the Desk of: Anne Marie Sullivan

Pre-paids

2 deals

Commods Desk funds Mahonia

Mahonia lends Enron $ in exchange for a promise that Enron will deliver...

① oil (Enron Hydro)

② NG (Enron Nat'l Gas Mktg)

... to Mahonia →

Permanent Subcommittee on Investigations
EXHIBIT #18700

To: Loan Forum

From: James R. McBride and Jill A. Calabrese

Date: December 20, 2000

Re: Project Mahonia - $330 Million Forward Sale Natural Gas Contract
Enron Financing Objectives

On December 18, 2000, Debt Capital Markets received approval to purchase up to a $167 million interest in a natural gas contract. That contract requires Enron North American to make future deliveries of natural gas. Today, Financial Institutions is seeking to establish or increase certain credit limits for Travelers, St. Paul, Lumbermen's, Hartford, and Safeco to support this transaction. These clients will issue surety bonds to guarantee Enron's performance under the natural gas contract. This memo is written in support of Financial Institutions' request and is intended to provide a brief overview of Enron's financing objectives. While we expect Enron to make the required deliveries, it is important to note that the Enron performance risk is specifically assumed by the surety bond providers. If Enron North America fails to deliver gas and Enron Corp fails to pay, the insurance companies are obligated to pay liquidated damages.

Transaction Overview from Enron's perspective:
Enron North America ("ENA") plans to enter into a $330 million forward sale gas contract with an off-balance sheet, special purpose vehicle created by Chase, Mahonia Natural Gas Limited. Under the terms of the agreement Enron North America will receive an up front payment of $330 million, which will be funded by Fleet and Chase. Enron will be obligated to deliver to Mahonia specified volumes of natural gas (84 Bcf) at specified times and at specified locations. (Please note Fleet will not be taking any mark to market gas risk or physical delivery risk. See the Debt Capital Markets Approval Memo for a more complete description of the Mahonia transaction). Separate and apart from the Mahonia transaction, Enron will enter into a commodity price swap that will fix Enron's future cost of purchasing and delivering the scheduled gas volumes.

Enron's financing objective in completing this transaction is as follows:
Enron is attempting to match its "book income" and "cash flow." As a derivatives and commodity trader, Enron uses "mark to market" accounting practices to account for its price risk management contracts. Consequently, when Enron closes a derivative transaction, whether physical or financial, it is required by accounting practice to mark to market (on a daily basis) the expected income or loss it will incur over the life of the transaction. However, from a cash flow standpoint, it will actually receive or make payments of cash over the life of the contract. On September 30, 2000, Enron had a positive net asset position of over $1.2 billion in its price risk management books.

Enron has historically managed to monetize its "in the money" position by completing either physical or financial forward sales. The Mahonia transaction will allow Enron to receive cash upfront. Subsequently, Enron will use the future cash flows it expects to receive under its existing price risk management contracts to pay for the gas it will be required to deliver under the Mahonia contract. The scheduled deliveries under the Mahonia contract are designed to approximately match Enron's expected receipts of cash (or volumes) under its existing contracts.

The accounting impact on Enron's financial statement is as follows:
Enron is not taking this transaction into earnings. Enron will account for their $330 million liability under the Mahonia Forward Sale Contract as an increase to its "Liability from Price Risk Management Activities." As September 30, 2000 Enron had total assets from price risk management activities of $14.7 billion and total liabilities from price risk management activities of $13.5 billion, for a net asset position of $1.2 billion.

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Permanent Subcommittee on Investigations
EXHIBIT #187pp

Legal Entity Descriptions

Chase:	Chase Manhattan Bank
FBF:	Fleet National Bank
LongLane:	LongLane Master Trust IV (SPV setup and administered by Fleet Credit Derivatives)
ENA:	Enron North America Inc.
Enron	Enron Corporation
Mahonia:	Mahonia Natural Gas limited (A Jersey Channel Island SPV set up by Chase)
Surety Providers:	Insurance companies providing Enron performance guarantee

Transaction Description

1. ENA and Mahonia will enter into a prepaid natural gas inventory forward sale contract to which Mahonia will pay $325MM to ENA in exchange for an agreement by ENA to deliver a scheduled amount of natural gas to Mahonia for 60 months.

2. Mahonia will sell to the Purchasers (LongLane. Chase and one other party) all of its rights to receive deliveries of natural gas from ENA under the forward sale contract. Mahonia will acknowledge that when gas is delivered under the contract it will take title to the gas as record owner, with all beneficial ownership interest remaining with the Purchasers.

3. The Purchasers and the Chase Natural Gas Trading Desk (Chase credit risk) enter into a fixed-price forward contract which the Purchasers agree to sell to Chase an amount of natural gas corresponding to the monthly scheduled deliveries to be made by ENA pursuant to the Forward Sale Agreement. This takes any market risk out of the transaction for Fleet.

4. Credit Derivatives enters into a interest rate swap with the Interest Rate Swap Desk which turns the fixed rate obligation into an obligation paying 1 month Libor + 87.5bps.

5. LongLane funds the proceeds ($167MM) and wires the money to the Agent (Chase).

6. Chase will act as Assignee Agent with LongLane being the participant in terms of Surety Bonds and Guarantee Agreement (described below).

7. ENA enters into a margin agreement were ENA agrees to post collateral with Chase in an amount equal to the excess of the mark-to-market value of the remaining natural gas to be delivered of the initial value of gas.

8. Enron Corp will issue a guarantee in favor of the Assignee Agent guaranteeing the obligations of ENA under the forward sale contract. In addition, Enron has purchased surety insurance for the transaction. The surety bond providers are Travelers, Hartford, St. Paul, Kemper, and Safeco. Credit approval from Fleet's Financial Institution's Group for each of these names will be required prior to executing the transaction. If the insurance companies get downgraded below A- Enron will replace the counterparty.

9. LongLane and Mahonia will enter into an agency agreement were Mahonia will agree to act as agent for the Purchasers in handling the sale and delivery of any natural gas delivered by ENA under the forward sale contract. In addition, Chase has stated that they will stay in the transaction to ensure additional operational integrity.

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RISK DESCRIPTION

Credit Risk: We have pre-settlement credit exposure under the following scenarios. It is our understanding that under credit policy it is counted as level "A" contingent risk. The following 2 scenarios describe our risk if prices vary.

Price of natural gas goes up:

If the price of natural gas goes up we have mark-to-market (MTM) exposure to Enron and the surety providers. To mitigate this risk Enron will enter into a margining agreement with a threshold amount of 10,000,000 in which Enron has to post cash collateral to an account at Chase. Chase will take all risk to Enron under this margining agreement. We never

Price of natural gas goes down:

If the price of natural gas down up we have a positive mark-to-market (MTM) gain if Enron was to default under the contracts. In this case we have exposure to the Surety Providers. Chase would unwind the contracts and liquidate the structure in approximately 7 days. The surety providers would pay the difference between the original funded amount and the unwind value.

Legal Risk:

As previously described Chase has been involved with these transactions for 5 years. Millbank is the bank attorney for this deal (representing Chase and us). In addition, we are having Weil Gotschall review the documentation because they are our derivative attorney and have been involved with the deals previously.

Execution/Operational Risk:

Credit Derivatives and Interest Rate Derivstives will work closely to ensure proper execution of the deal at inception (we have worked well together in the pass). After the transaction is closed Credit Derivative operations will monitor valuation and margin calls. Funding is similar to all of our TROR swaps.

Revenue

Pricing on the deal is 65bps upfront and Libor + 87.5 which equates to a 51MM upfront and a total revenue on the deal of approximately $4.5MM.

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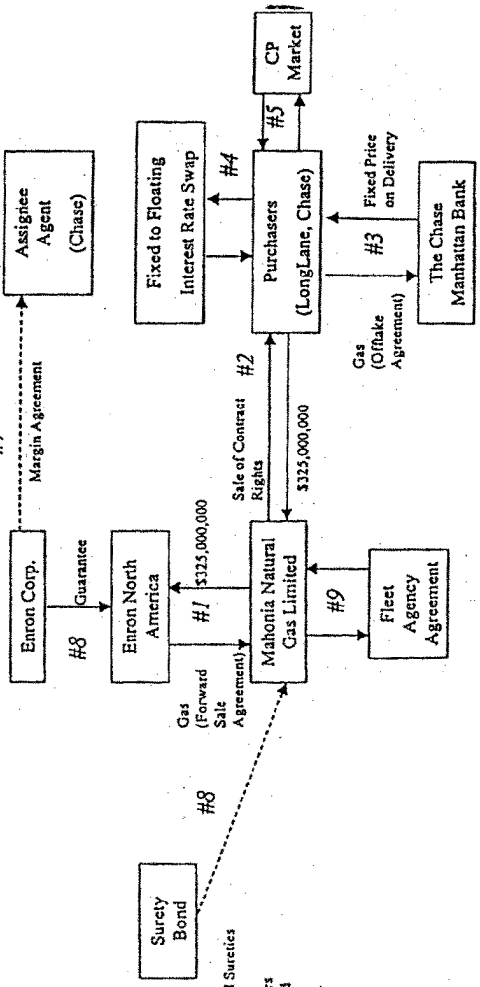
Enron Prepaid Natural Gas
Forward Sale Transaction



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Annex 1 to Summary of Terms and Conditions

Surety Bond Allocation	165,000,000.00
Travelers	41,250,000.00
St Paul	36,300,000.00
Lumbermens	36,300,000.00
Hartford	26,400,000.00
Safeco	24,750,000.00

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From: KEARNS, KEVIN P [KEVIN_P_KEARNS@fleet.com]
Sent: Friday, December 22, 2000 9:54 AM
To: Jeff Dellapina (E-mail); ~Wilson, Melanie J.
Subject: FW: Mahonia Forward Sale

Hi Jeff and Melaine

From our attorney's standpoint it was difficult to review the package until
all the documentation was received (which was this morning). I did want you
to see her comments to date so that we can discuss them (alot of them are
probably misunderstandings on our part and can be easily resolved).

Additional items to discuss include:

Fleet entity
Swap Mechanics
Timing and expectations over the next few days.

Regards, Kevin

-----Original Message-----
From: sylvie.durham@weil.com [mailto:sylvie.durham@weil.com]
Sent: Thursday, December 21, 2000 6:26 PM
To: KEARNS, KEVIN P
Subject: Mahonia Forward Sale

Kevin,

Please note that these are only my initial comments. This document works in conjunction with so many others that depending on who those documents are drafted, the language may or may not work. I was also only
looking for big picture items.

My first concern is that the Surety Bond does not cover a failure by Mahonia to perform. This document contemplates that Mahonia may refuse delivery. In such a case, Enron is entitled to sell the gas that is not purchased to sell the gas in the open market and pay the funds received to
the Purchaser. However, if Mahonia fails to accept delivery for 30 consecutive days, Enron can terminate and determine the Replacement Value
which is broadly defined as the price at which Enron can sell the gas. Accordingly, if Mahonia fails to perform, there is no assurance that you will receive your principal amount back. The Surety Bond does not cover this event.

This first concern also leads to my second concern which we discussed before. I had been assuming that Mahonia is a Chase sponsored bankruptcy
remote entity. However, bankruptcy remote entities are brain dead and accordingly there should be no scenario in which Mahonia fails to perform
(the only thing it has to do is accept delivery of the gas). Since that

Permanent Subcommittee on Investigations
EXHIBIT #187qq

scenario exists, I question whether Mahonia is a bankruptcy remote vehicle.
I also did not see the type of language in the document that one typically
sees when one is dealing with a bankruptcy remote vehicle. I strongly recommend that you request all the constitutional documents by which Mahonia has been established. These constitutional documents (which are not in the package that you sent me) will tell me whether it is bankruptcy
remote and whether my first concern is purely theoretical or actually possible. Remember that I first noted this issue to you because of my concern that the Surety Bond would be in Mahonia's name. If Mahonia is not
bankruptcy remote, then payments under the Surety Bond would be subject to
the automatic stay in a Mahonia bankruptcy. (This is usually why surety bonds are in the name of a trustee for the benefit of the securityholders.)

I'm also concerned about the timing of payments from Enron, the Enron Parent and the Surety Provider. Under Section 5.04(c), Mahonia has the right to make a demand under the Surety Bond if payment is not received from Enron or its Parent Guarantor. This language should not be optional.
The language should read that Mahonia MUST make demand on the Surety Bond
is payments are not received from Enron or its parent. Also please note the timing issue. Enron has THIRTY DAYS AFTER WRITTEN NOTICE IS DELIVERED
THAT IT HAS FAILED TO PAY before it becomes an Event of Default (see 5.01(a)). I have not looked at the Enron Guaranty but this document suggests that it also has a grace period. I think that 30 days is far too
long a grace period and that furthermore it should be automatic and not subject to receiving written notice from Mahonia. Since Mahonia is not absolutely obligated to deliver such a written notice, the time lag may be
far greater. The Surety Provider will only pay after the Enron grace period and the Enron Gurantor grace periods have been used up. You could
be looking at a very long delay. I leave to you as to what an acceptable
grace period is for Enron and its Parent. However, Mahonia should either
be forced to give notice or the requirement for a notice should be removed.
I prefer the latter approach.

Finally, as far as big picture items, I would like to see Fleet and the other purchasers to be third party beneficiaries under this Agreement. Such a designation would allow Fleet to enforce the document directly against Enron without having to go through Mahonia. Indeed, there is no provision in this document for Fleet or the other banks to force Mahonia to
do anything and since you are not a third party beneficiary, you have no direct rights to proceed against Enron.

I'll be travelling in my car tomorrow morning. My cell # is 917-821-8412.

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Zandra Sherrington
02/05/2001 08:10 AM EST

To:Douglas McLaughlin/CHASE@CHASE
cc:Cecille Taylor-Simpson/CHASE@CHASE, Taimoor Abbasi/CHASE@CHASE, Lorry Ripley/CHASE@CHASE, Catherine Ngui-Dy/CHASE@CHASE, William Spota/CHASE@CHASE
bcc:
Subject:Re: MTM for Prepays

Doug- BEfore you make any changes to the below, I would like the managers on the cc list to give any input as to how this might impact them.

BO Mgr - PLease respond accidngly
Douglas McLaughlin

To: Anne Marie Sullivan/CHASE@CHASE
cc: Jeffrey W. Dellapina/CHASE Leo Lai/CHASE@CHASE, Zandra Sherrington/CHASE@CHASE
Subject: Re: MTM for Prepays

There is no way to show both the Mahonia exposure and Mahonia's exposure to Columbia or Equitable, Would it be preferable to show the exposure to the underlying as Mahonia is a SPV of Chase's. Anne Marie would this be acceptable to you? We could change the Counterparty name to read Mahonia ref Columbia and use Columbia's UCN?

Any suggestions would be appreciated?

Tks
Doug
Anne Marie Sullivan

To: Douglas McLaughlin/CHASE@CHASE
cc: Jeffrey W. Dellapina/CHASE Leo Lai/CHASE@CHASE
Subject: Re: MTM for Prepays

Doug, is this something your group wil do? If I can assist, pls let me know.
Thanks

Permanent Subcommittee on Investigations
EXHIBIT #187rr

Jeffrey W. Dellapina

To: Douglas McLaughlin/CHASE@CHASE, Anne Marie Sullivan/CHASE@CHASE
cc: Leo Lai/CHASE@CHASE
Subject:

Through Globalnet, we need to capture the MTM exposure associated with the prepays. Given the Mahonia role, I know that the exposure doesn't flow smoothly to the "real" counterparts. The credit chain is requiring me to address this immediately.

Most pressing are (i) Columbia, and (ii) Equitable. Even if we have to manually contribute a number to Globalnet every Friday, this would be helpful

New Memo Forward Reply Edit Delete Go to Copy Into

Anne Marie Sullivan
10/29/2001 03:46 PM EST

To:Gary Smeal/CHASE@Chase
cc:
bcc:
Subject:Enron Prepaids

One other thing I thought of after you left my office in relation to our wondering what would make an Insurance Company take on the Enron risk yet we, as a Bank, would not make an outright loan for the $350MM. The difference is that we syndicate out this risk in pieces. There are usually 5 or 6 different Insurance companies taking a piece of the total. So Fireman's Fund may take risk on $75MM, AIG takes $50MM, Lumberman's Mutual Casualty takes $100MM, etc

I saw your call come in but could not get off the conference call I was on and you did not leave message. Pls call me again if you need me.
Thanks

---------- Forwarded by Anne Marie Sullivan/CHASE on 10/29/2001 04:51 PM

Global Markets Credit (212) 270-5618 Fax Number: (212) 270 -3841

To: Gary Smeal/CHASE@Chase, Judah Kaplan/CHASE@CHASE
cc:
Subject: Enron Prepaids

Description :
As an example, Enron North America (ENAC) enters into a prepaid Nat Gas forward sale in which Mahonia will pay $350MM to ENAC (which is a fixed price) for the right to receive a fixed amount of NatGas with monthly deliveries. In order to fund itself, Mahonia sells this Nat Gas to Chase under similar terms. Chase then sells the physical gas floating to the market in amounts equal to the scheduled monthly deliveries. So now Chase has paid fixed (via the $350MM) and receives gas.

To hedge both our and Enron's fixed price risk under the prepaid, Chase enters into a financial swap with Enron whereby Chase pays floating and receives fixed. (The prepaid is between Enron and Mahonia. The financial swap is between Enron and Chase. Enron cannot enter into both a prepaid and the financial hedge with the same legal entity).

We have Insurance Surety Wraps for the $350MM.
There is also a CSA under the ISDA with a $10MM threshold.

If prices fall, the surety wraps will cover only the $350MM so we needed the collateral agreement, as well because we will be selling the gas floating to the market at a loss, i.e. it is no longer worth the $350MM.

If you look through Mahonia to Enron, the mtms offset. (There are also other transactions under Enron, of course, which are separet from these Prepaids and their hedges.

The notional principal exposure created by the Prepaids are covered under separate facilities in GES called, Counterparty Limit - Open Trades , each having been set up as we close each Prepaid.
The exposure from the fixed for floating swap is captured under the FEL in GlobalNet.

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EXHIBIT #187ss

PLEASE ALSO SEE THE BELOW WHICH I SENT TO GEORGE BRASH AND JIM BALLENTINE AT BEGINNING OF LAST WEEK. IF YOU NEED ADDITIONAL INFO, PLS LET ME KNOW.
RGDS,
ANNE MARIE

---------- Forwarded by Anne Marie Sullivan/CHASE on 10/29/2001 11:07 AM ----------

Global Markets Credit (212) 270-5618 Fax Number: (212) 270 -3841

To: James Ballentine/CHASE@CHASE
cc:
Subject: Enron

FE

The following is an Excel spreadsheet containing the transaction and FE details (Replacement Value) of all of the Enron trades broken out by Enron entity. If you want to see in maturity date order just sort that way. You will likely need to widen some of the columns.
I think I have captured everything you'd want to see but if you require additional details or need assistance shifting around the data, let me know and I will be happy to help.

EnronOct01.xls

PREPAIDS
This file contains details of all Energy Prepaids , including non-Enron.

EnronPrepdBallentine.xls

PHYSICAL
Additionally, there is the following Physical exposure:

Enron North America Corp $44.7MM