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THE ROLE OF THE BOARD OF DIRECTORS IN ENRON'S COLLAPSE

HEARING

BEFORE THE

PERMANENT SUBCOMMITTEE OF INVESTIGATIONS

OF THE

COMMITTEE ON
GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

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THE ROLE OF THE BOARD OF DIRECTORS IN ENRON'S COLLAPSE

TUESDAY, MAY 7, 2002

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

The Subcommittee met, pursuant to notice, at 9:37 a.m., in room SH–216, Hart Senate Office Building, Hon. Carl Levin, Chairman of the Subcommittee, presiding.

Present: Senators Levin, Lieberman, Durbin, Carper, Collins, Bunning, and Fitzgerald.

Staff Present: Elise J. Bean, Acting Staff Director and Chief Counsel; Linda J. Gustitus, Chief of Staff for Senator Levin; Mary D. Robertson, Chief Clerk; Stephanie E. Segal, Professional Staff Member; Ross Kirschner, Deputy Investigator; Jamie Duckman, Majority Accountant; Kim Corthell, Republican Staff Director; Alec Roger, Counsel to the Minority; Claire Barnard, Investigator to the Minority; Jim Pittrizzi, Detailee/General Accounting Office; Joyce Rechtschaffen, Staff Director and Counsel, Governmental Affairs Committee; Marianne Upton (Senator Durbin); Joe Bryan (Senator Levin); Bill Weber (Senator Durbin); Cindy Lesser (Senator Lieberman); Kathleen Long (Senator Levin); Holly Schmitt (Senator Bunning); Anne Fisher (Senator Cochran); Bob Klepp and Trent Kittleman (Senator Thompson).

OPENING STATEMENT OF SENATOR LEVIN

Senator LEVIN. Good morning, everybody. The Subcommittee will come to order.

On December 2, 2001, the seventh largest corporation in America collapsed. Its stock, having plummeted from $80 a share to practically nothing in less than 10 months, the reins of what was once a high-flying company of $100 billion in gross revenues and 20,000 employees were handed over to a Federal bankruptcy judge. That collapse has rolled like a tidal wave across the corporate boardrooms of America, across Wall Street, and across the entire investing community, which now includes over half of U.S. households.

With this tidal wave, we are all asking two questions: What happened at Enron, and could it happen again? Today, we hope to help answer the first question in order to ensure that the answer to the second question will become "no."

One of the key players responsible for overseeing the operations of our publicly held corporations is the Board of Directors. Directors are charged by law to be the fiduciaries, the trustees who protect the interests of the corporate shareholders. In that capacity, they are supposed to exercise their best business judgment on behalf of those shareholders. They are supposed to be independent. And while they are not expected to be detectives, they are expected to ask tough questions of management, to probe opaque answers, and to display sufficient skill and fortitude to say no to transactions that do not look right.

Along with management and the auditors, the Board shares the responsibility to provide to the company's shareholders a financial statement that is a fair representation of the financial position of the company. As the Second Circuit Court of Appeals held in a widely quoted opinion, technical compliance with Generally Accepted Accounting Principles may be evidence of acting in good faith, but it is not necessarily conclusive: The "critical test," the court said, is "whether the financial statements as a whole fairly present the financial position" of a company. Enron's financial statements did not, and the Board's role in that failure is before us.

Today, we have five key members from the Enron Board of Directors to tell us what they knew about the financial condition of Enron, when they knew it, and what they did about it. In other words, what role did the Board play in these events?

The Subcommittee issued over 50 subpoenas for documents to Enron, Arthur Andersen, members of the Enron Board, and officers of Enron. Staff has reviewed about 300 boxes of documents to date, and conducted interviews with 13 current and past Board members. Each Board member complied with the document subpoenas and willingly appeared for interviews. We appreciate their cooperation and their voluntary appearance today.

We have found that when you pare down the hundreds of incredibly complex financial transactions that were the hallmark of Enron, you realize that many were nothing more than smoke-and-mirrors bookkeeping tricks, designed to artificially inflate earnings rather than achieve economic objectives, to hide losses rather than disclose business failures to the public, to deceive more than inform.

The decisions to engage in these accounting gimmicks and deceptive transactions were fueled by the very human but unadmirable emotions of greed and arrogance. Putting a growth gloss on the balance sheet pumped up the stock price, and the rise in stock price, regardless of the underlying true value of the company, was, for many, the measure in the 1990's for judging corporate success. The Board that was supposed to be the check on the greed and the arrogance, in fact, was not. Here is how it happened.

Enron was in transition from an old-line energy company, with pipelines and power plants, to a high-tech global enterprise engaged in energy trading and international investment. It experienced large fluctuations from quarter to quarter in its earnings. Those large fluctuations affected the credit rating Enron received, and the credit rating affected Enron's ability to obtain low-cost financing, attract investment, and increase its stock price.

In order to smooth out its earnings and avoid the natural dips, Enron engaged in a variety of complicated transactions that relied on structured finance, derivatives, and other arrangements that, while legal if done right, are nonetheless designed to massage a company's financial statement to make its financial condition look better than it really is.

While it is not uncommon for a company to use these devices, they are also used somewhat sparingly. Enron, however, made them a high art form and used them aggressively, and in some cases, improperly. When used extensively and when they become dominant, when they involve billions of dollars, $27 billion in assets at Enron's peak, the real impact of these complex transactions on a financial statement is to cover up reality with a glitzy coat of paint. The financial statement becomes a fiction, and that is what happened at Enron.

Step by step, Enron shifted a larger percentage of its assets into these structured finance arrangements, not for any real business purpose, but in order to make Enron look more profitable than it really was. Funds flow and the appearance of funds flow became the Enron mantra in order to keep Enron's credit rating up and its stock price climbing, and the Board of Directors went along with it.

In many actions starting in 1997, when the Board first approved Whitewing, through the summer of 2001, just before things fell apart publicly, the Board of Directors went along with management's wishes. The Board relinquished its role of questioner and adopted the role of facilitator. It succumbed to the Enron ether of invincibility, superiority, and gamesmanship in manipulating Enron's financial statement to keep the Enron stock price soaring. This is a company, we are told, that had televisions in its elevators in order for employees to monitor Enron's stock price at all times.

The financial transactions that the Board approved were used to make debt look like equity, to make loans look like sales, to make poorly performing assets look like money makers, and to make Enron-controlled entities look like legitimate third parties. By the time of the collapse, Enron held almost 50 percent of its assets off its books, and what started as a useful tool to address specific business problems had become a way of life.

As long as Enron's stock was rising, these elaborate financial structures did what they were designed to do, make Enron's financial condition look better than it was. But once Enron stock started falling, these financial structures collapsed on themselves like a house of cards, revealing at the end that there was no "there" there. These transactions involved a number of deceptions that pushed the limit of accepted accounting practices and, at times, exceeded them. And parenthetically, if it turns out that Generally Accepted Accounting Principles allow such deceptions, then those accounting principles need to be changed.

One type of deception that Enron used was to report on the company's financial statements 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. Five of the seven assets sold this way to the LJM partnership at the end of the last two quarters of 1999 were bought back by Enron, sometimes within 6 months' time. But those guarantees did not show on Enron's books as a liability. Only the sales showed as funds flow.

Another type of deception made what was essentially a loan look like a sale, so the company's financial statement reflected the transaction as income or cash flow instead of debt.

A third type of deception inflated the value of the assets that Enron held for sale. For example, Enron would buy a power plant on day one for $30 million, and within a month or so would begin carrying it on Enron's books as an asset worth $45 million. Two weeks ago, Enron filed a statement with the SEC declaring that it is going to write down its assets by another $14 to $24 billion, a staggering sum, due to overvaluations on the books and "accounting errors or irregularities."

Another type of deception, the Raptors, used Enron stock to backstop a risk that the LJM partnership and its investors were supposed to be assuming for Enron, and the risk retained by Enron was not disclosed on the company's financial statements in a meaningful way.

As these structured financial transactions grew in number, size, and frequency, and as 50 percent of Enron's assets were moved off Enron's books, no one on the Enron Board said that their fiduciary duty required them to blow the whistle and prevent a deceptive picture of Enron's financial situation from being presented to the public.

During the 13 interviews, the Board members told us that they had not been aware of the depth of Enron's problems or the extent of these structured transactions and accounting gimmicks, and most said they had no inkling that Enron was in troubled waters until mid-October 2001. But look at this chart that the Subcommittee staff has put together,[1] identifying numerous red flags presented to the Board of Directors from February 1999 on, that signaled the risks Enron was taking, and that should have alerted the Board to probe and then to change course.

The staff has identified well over a dozen of these red flags, but I am just going to highlight a few. In February 1999, the Board's Audit Committee was told by Arthur Andersen directly that Enron's accounting practices were high risk and pushed limits.

In June 1999, the Board approved at a special meeting and without prior Finance Committee consideration the creation of the LJM partnership, and waived the conflict of interest provision of the Enron code of conduct. The Enron Chief Financial Officer, Andy Fastow, served as the managing partner of LJM, something no Board member had ever approved or heard of prior to this. The Board was to approve a code of conduct waiver for Fastow three times over the next 16 months.

In September 1999, the Board approved moving off the Enron balance sheet a $1.5 billion joint venture called Whitewing, which was established by the Board in December 1997 to get a loan that looked like equity, and then used from 1999 on to purchase assets that Enron wanted to move off its books.

In May 2000, the Board approved the first Raptor transaction, a vehicle designed to hedge Enron investments by using Enron stock to backstop the hedge, which amounted to Enron hedging with itself.

[1] See Exhibit No. 1 which appears in the Appendix on page 203.

By October 2000, the Board knew that Enron had $27 billion in assets, almost half of its assets, off its balance sheet.

In April 2001, the Enron Board knew that 64 percent of Enron's assets were troubled or not performing and that 45 million shares of Enron stock were at risk in Raptors and Whitewing.

Starting with the creation of Whitewing in 1997 and with its deconsolidation in 1999, the Board started to wade into dangerous waters. With the establishment of the LJM partnership and the waiver of the code of conduct, they were up to their necks, and with the Board's approval of the Raptors, the Board was swimming way over their heads. In the end, Enron drowned in its own debt. As the chart shows, the Board had ample knowledge of the dangerous waters in which Enron was swimming and it did not do anything about it.

The Board told the Subcommittee staff that because each of Enron's transactions was approved by Enron management, whom they saw as some of the most creative and talented people in the business, and because the transactions had been approved by Arthur Andersen, a top auditing firm, and by Enron's lawyers and private law firms like Vinson and Elkins, by the credit rating agencies, or by investment bankers who had a significant stake in a lot of these transactions, the Board assumed that the transactions were OK. Now, I can see why you might rely on a company auditor or an outside attorney, but the Board must exercise independent judgment. The Board is not supposed to be a rubber stamp for auditors or attorneys.

Also, the people that the Board relied on were conflicted in their roles involving Enron, and the Board knew it. First, the Board knew that Enron's management handed out bonuses like candy at Halloween. Employees were given huge bonuses for closing deals, and many of these deals proved damaging to Enron. For instance, two executives closed a deal on a power project in India, which is now a financial disaster, and got bonuses in the range of $50 million. The head of one Enron division who was moved out of the company walked away with more than $250 million in the year that he was shown the door. The temptation to self-enrichment at Enron was overwhelming.

Arthur Andersen was conflicted, because it served Enron as both an auditor and a consultant, and, for 2 years, it also served as Enron's internal auditor, essentially auditing its own work. Enron was Andersen's largest client, and in 2000, Andersen earned over $50 million in fees from the company. Employees of Andersen routinely crossed over to work for Enron, and an Andersen employee who actually questioned Enron practices while serving on the audit team was promptly reassigned to another client at Enron's urging.

Relying on outsiders, conflicted or not, does not relieve the Board from the ultimate responsibility to make sure that at the end of the day, Enron was operating properly and Enron's financial statement was a fair representation of Enron's financial condition. The Board failed in that responsibility.

The structured debt and guarantees overwhelmed Enron's ability to pay, and that meant bankruptcy for the corporation, huge pension losses for employees, investment losses for stockholders, and business losses for hundreds of small companies that did business with Enron, while the officers of the corporation walked away with fortunes.

Today, we are going to go over the decisions that the Board made on a number of these transactions, as well as the decisions that they made with respect to compensation. We will also look at the interlocking financial relationships that some members of the Board had with Enron.

Following the Board, we will hear in a second panel from several experts in the field of corporate governance, and I expect that we will be taking a break for lunch sometime around 12 or 12:30.

Senator Collins.

OPENING STATEMENT OF SENATOR COLLINS

Senator COLLINS. Thank you, Mr. Chairman. Today is the first in a series of hearings to be held by the Permanent Subcommittee on Investigations into the events that led to the bankruptcy of the Enron Corporation. As a result of the company's downward spiral and ultimate bankruptcy, shareholders, both large and small, individual and institutional, lost an estimated $60 billion. This includes more than 15,000 Enron employees and retirees who had a significant proportion of their pension funds invested in the company's stock. They lost an astounding $1.3 billion. The collapse of Enron caused thousands of Americans to lose their jobs, to lose savings, and to lose confidence in corporate America.

Unraveling the complexities of what happened, determining who is responsible, and prosecuting those individuals will take the Department of Justice, the Labor Department, and the Securities and Exchange Commission many months and possibly years. The Subcommittee's job is not to duplicate those efforts, but rather to examine the actions taken by all of the players who contributed to Enron's demise in order to illuminate the public policy issues. By doing so, the Subcommittee can help focus the debate in Congress, in State legislatures, and in corporate board rooms across the Nation on what measures should be taken and by whom to minimize the chances of another Enron-like debacle.

In this first hearing, the Subcommittee will examine the role played by Enron's Board of Directors in the company's bankruptcy. I want to acknowledge the Board's full cooperation with this investigation. I also want to take a moment to praise Senator Levin and the dedicated both Majority and Minority Subcommittee staff who have been tireless in their efforts to unravel a very tangled web of conflicts of interest, unusual transactions, and lax oversight.

Corporate boards play an essential role in the American economy. They are the single most important guardians of a company's shareholders, and as such, they have a fiduciary duty to promote the interests of the corporation, to act in good faith, and to exercise their best judgment.

When Korn/Ferry, a major corporate recruiter, polled corporate directors in 2001 to determine the outstanding capabilities of board members, it identified one single trait that stood significantly above all the others. That trait is a willingness to challenge management decisions when necessary.

There is no question that directors generally should be able to rely on the representation of management and independent experts. But directors have an obligation to do more than simply accept what they are told, occasionally ask whether there are any problems, and inquire whether the accountants agree on the propriety of actions presented for their approval. Prudent directors retain their objectivity and to some degree, a healthy skepticism. They must be willing to ask the tough questions of management, recognize those situations where independent expert advice should be sought, and exercise heightened diligence when a company is pursuing unfamiliar or new territory.

Enron was a company that prided itself on its innovation. CEO Jeffrey Skilling often boasted of Enron's pioneering efforts as it transformed itself from a traditional energy company to a global enterprise creating new markets and businesses. In contrast, it appears that the Board of Directors continued to perform its duties as if Enron were still an old-line, conservative energy company, at a time when it appears they should have been far more probing, given Enron's metamorphosis into an energy trading company.

Serving as a director for a corporation as complicated as Enron obviously is not an easy task. Enron was one of America's largest corporations. It had thousands of partnerships, joint ventures, and other special purpose entities, many of which were engaging in transactions that can only, and barely even then, be followed with the aid of complex diagrams. In fact, the Board members interviewed by the staff appear to have been unaware that Enron has some 3,000 related entities, including 600 using the same post office box in the Cayman Islands. I would argue that should have been another red flag.

The complexity of the responsibility is precisely why Enron's Directors were paid hundreds of thousands of dollars per year in cash, stock, and options. While the exact amount of compensation can be difficult to determine, depending on how one calculates the value of stock options, there is no question that Enron's Board members were among the most highly compensated in the world.

Today, we will ask five Enron Directors what they did to protect shareholders and why they believe that they failed in doing so. We will also hear an evaluation of their efforts from some of the leading experts on corporate governance. I am particularly interested to learn more about the Board's response to the large stock sales engaged in by Enron's management, its reaction to the departure of a CEO who left after only 6 months on the job, and its decision to approve a waiver of Enron's code of conduct to allow the Chief Financial Officer to engage in business deals with the company.

This latter decision is the Board action that I find among the most inexplicable. During the investigation, the Subcommittee spoke with many experts on corporate governance, and not a single one had ever heard of a public company ratifying a similar proposal.

I want to understand also the Board's view of what now appears to be the obvious conflicts of interest that contributed to Enron's collapse and to explore whether the Board, and its Audit Committee in particular, believed that they acted prudently in monitoring the outside auditor, Andersen. Actually, Andersen, as we know, was more than the outside auditor, which is another issue in and of itself. The Board, with Andersen's endorsement, approved many of the transactions described by Senator Levin that enabled the company to paint a false picture of its financial health and Enron employees to enrich themselves at the expense of the corporation, its shareholders, and ultimately its creditors.

We are still working to unravel the complexities of these transactions, which has proven to be a monumental task. It is troubling to me that in staff interviews, Board members have provided little insight into major transactions. For example, not one Board member could explain or recall a $2.2 billion Board resolution that approved the issuance of preferred Enron stock to an outside investor. Now, I certainly do not expect the Board members to have perfect recall of every deal that they approved, but I would hope that transactions that rise to the threshold of multiple billions of dollars would be memorable to at least someone on the Board.

In addition, we will discuss some of the alleged conflicts of interest created by some of the Board members' other relationships with Enron. Was the Board's vigilance dulled by large consulting fees, corporate contributions to their favorite charities, and other business relationships? Every corporate governance expert with whom we spoke was critical, for example, of any Board member having a consultant contract with Enron. At a minimum, such relationships do not foster the appearance of propriety and financial independence of Board members.

Mr. Chairman, the Enron case is uncannily similar to another business failure that occurred some 70 years ago. In the early 1930's, an electric holding company called Middle West Utilities collapsed under the weight of stock fraud and cooked books. Middle West was comprised of so many interlocking boards that it took the Federal Trade Commission 7 years to fully comprehend its structure, which involved 284 affiliates. Underneath its incredibly complex structure lay an immense amount of debt taken on as it expanded in the 1920's. Ironically, Middle West's auditor was a relatively new firm named Arthur Andersen.

There is, however, one significant difference between Middle West's and Enron's executives. The Middle West CEO's considerable fortune of around $150 million was tied up in Middle West holdings and disappeared with the company. In contrast, many of Enron's managers were making tens and, at least in one case, hundreds of millions of dollars by dumping their Enron stock before the corporation's collapse.

Although imperfect, it is important to remember that today, our systems of accounting and financial regulation are the best in the world. That makes the Enron case all the more troubling, because it simply should not have happened. It represents 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. And in that system, the Board of Directors is supposed to provide the first line of defense by overseeing the conduct of management.

There are already encouraging signs that many directors in the wake of Enron's collapse are taking their roles much more seriously. As we seek answers in the Enron case, we should be careful not to act precipitously without understanding the true nature and extent of the problems underlying the corporation's bankruptcy.

The testimony we will hear this morning about the role of the Board of Directors should provide some answers. It should also 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.

The Chairman of our full Committee, Senator Lieberman.

OPENING STATEMENT OF SENATOR LIEBERMAN

Senator LIEBERMAN. Thank you, Senator Levin. Thanks to you and Senator Collins and your staff of the Permanent Subcommittee on Investigations for holding this important hearing, which really does initiate the next phase of the Senate Governmental Affairs Committee's investigation of the scandalous collapse of the Enron corporation.

Over the past 6 months, we have all heard many reports about who failed Enron's shareholders and employees leading up to the company's fall. Obviously, the company's management has been cited, Arthur Andersen, government watchdogs, stock analysts, and even rating agencies. There were bad decisions, breakdowns, and some betrayals at several points and links in the oversight chain. Today, we focus on another group that must accept some of the blame for failing to uncover the crookedness in the company's behavior and books, and that is the Board of Directors.

Textbooks tell students that the board of directors is a group of people elected by the shareholders to watch over the management of a corporation on behalf of the shareholders. Board members are, in that sense, like trustees or guardians for the shareholders and, in a larger sense, for the integrity and reliability of our economic system.

In fact, because of their essential role, directors by law owe special duties to the corporation and particularly to its shareholders, duties of loyalty and care. Loyalty, meaning freedom from conflicts of interest—in other words, serving shareholders and only shareholders with independence and undivided attention. Care, meaning doing their work responsibly, thoroughly, and in good faith.

By all appearances, unfortunately, Enron's Board of Directors failed their shareholders on both counts.

First, about the Directors' loyalty to their shareholders, even though a majority of Enron's Board was made up of outside directors, meaning directors not in Enron's management, a stunning 10 of the 15 most recent outside Directors had conflicts of interest, including contracts with Enron, common ties or contributions to charities, and memberships on the board of other companies doing business with Enron.

For example, charities close to some of the Directors were supported heavily by Enron and its officers. Two Directors earned more than $6.5 million in consulting fees from Enron since 1991. One Director served on the board of a company that in 1999 signed a $1 billion energy management agreement with an Enron affiliate.

Arrangements like these can divide or even redirect a director's loyalties to the hand that feeds them, management, and away from their single-minded responsibility to the shareholders. Consulting contracts or large donations to favored charities, just as a matter of human nature, can whittle away the objectivity directors must bring to every decision they make and leave shareholders without the protectors that they need.

Second, regarding the Directors' duty to take care and be diligent in overseeing the management of the company, my colleagues have spoken to this, and the fact is, unfortunately, that the more we look, the more evidence we find of inadequate oversight. In 1999, as has been said, the Board went so far as to suspend Enron's Code of Ethics on two separate occasions to allow the company's Chief Financial Officer, Andrew Fastow, to run partnerships that would enter into deals with Enron. That, to me, was extraordinary, and extraordinarily irresponsible. Rather than raising a red flag, the Board gave a green light to Mr. Fastow to, as Sherron Watkins put it in her testimony before the Senate Commerce Committee, "put his hands in the Enron candy jar."

As the shareholders' elected representatives, it seems to me that the board of directors has an affirmative obligation to ask questions and get answers, and these Directors were and are qualified individuals, very qualified, with a professional understanding of industry. They had impressive credentials—former Chairman of the Executive Committee of Gulf and Western Industries, former Chairman of the U.S. Commodity Futures Trading Commission, former Secretary of State for Energy of the United Kingdom, professor of accounting and former Dean of the Stanford Business School.

The question is, why all that experience and so much more accomplished so little for the shareholders of Enron in the end.

To me, the Directors' lack of due diligence is even more troubling in light of the fact that some of them profited so much from their positions as Board members. In stock sales alone over the years studied by our staff, some made hundreds of thousands of dollars and a few made more than $1 million. In that sense, I am sad to say that the Board of Directors did not just fiddle while Enron burned, some of them toasted marshmallows over the flames, even as those flames shook our economy and engulfed the dreams of thousands of dedicated Enron employees who lost not only their jobs, but their retirement security.

The failures of Enron's Board of Directors are a warning that we must heed, particularly because of the more than 100 million Americans who are now, in one way or another, stock investors, owners of stock, particularly those millions of middle-class Americans who entered the market over the last 20 years. They are shaken and they are asking, if the distinguished Board of Enron failed in this case, as they did, to represent the shareholders adequately, how many other boards of how many other American corporations might be similarly negligent?

After all, investment capital is the lifeblood of our free market economy. So the belief that directors are failing their shareholders is a threat to the health of our economic system. We cannot let it grow or go untreated. We all must work together now to restore investors' confidence, and quickly.

There are many proposals of potential reforms that have been made to strengthen directors' accountability. I believe we should give the SEC new powers to remove negligent directors from their boards and prohibit them from future service on the boards of any other public companies. I am also very interested in proposals that have been made to ban or limit company stock sales by directors for the duration of their terms on the boards and to impose mandatory term limits on directors.

I strongly support the call to the stock exchanges to adopt listing requirements that would obligate companies to limit the number of insiders who can serve on boards, to restrict directors from serving on more than a given number of boards, and to prohibit behavior such as that we have all described this morning by Enron's Directors, some Enron Directors, that amounts to conflicts of interest.

As usual, self-regulation by the companies and by the stock exchanges would, in my opinion, be the most direct and effective path to reform. But if there is inadequate self-regulation, there is no question that some government action will be necessary to prevent the most egregious abuses of responsibility by boards of directors.

Mr. Chairman, about 100 years ago, the famous satirist Ambrose Bierce defined a corporation as, "an ingenious device for obtaining individual profit without individual responsibility." Let us work together now to make sure that cynical joke does not become a prophecy. Let us make sure that directors are accountable and vigilant, that they act as the shareholders' first line of defense against corporate negligence, mismanagement, or corruption, and that they give investors the confidence our economy needs to grow as robustly as we all want it to. Thank you very much.

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

OPENING STATEMENT OF SENATOR DURBIN

Senator DURBIN. Thank you, Mr. Chairman. I will be very brief and I thank you for this hearing.

I think it is fair to say that the Enron experience has shaken corporate America to the core. I think it has shaken America to the core because of the victims. Those victims are scarcely represented at these Congressional hearings, not only employees that have lost their jobs at Enron and related companies, but the investors, the pensioners, all of those victims will only have the comfort of reading these transcripts or watching C–SPAN. That is as close as it gets.

The theory behind corporate governance is that the board of directors is supposed to be defending them, too. But as we look at the report from the Powers Committee and others, it is not very encouraging in terms of the role of the Board of Directors at Enron. In fact, the Powers Report says point-blank, "The Board of Directors failed, in our judgment, in its oversight duties." That is a stunning condemnation.

Enron has called into question corporate governance and corporate honesty. It appears now when you look at the salaries being paid to some of the people who were clearly deceiving everyone in sight, they were being treated like corporate royalty in a Nation which long ago decided that royalty was not going to be part of our future.

I am going to be asking these Board members, some of whom I know and have worked with and respect very much, whether they were misled, whether or not as directors of a corporation of this size and importance they had the tools or gave the time that was necessary to do their job right.

I am always fascinated by how many people express an interest in how many boards of directors they serve on, and I just wonder if that is a real service, a real dedication, and a real commitment, or just another notch on your gun, another line on your resume, whether or not members of boards of directors of important companies really take that job as seriously as they should if this system is to work.

I think that as we look at the challenge we have before us, that this hearing of this Subcommittee will lead us to ask some hard questions, lead us to, I hope, pass some important legislation, because if all of these hearings on Capitol Hill are just about face time on the nightly news, we have failed those employees and those pensioners and the people that count on this government to enact laws to protect them. Thank you, Mr. Chairman.

Senator LEVIN. Thank you very much, Senator Durbin. Senator Bunning.

OPENING STATEMENT OF SENATOR BUNNING

Senator BUNNING. Thank you, Mr. Chairman. Enron's collapse has not only affected its shareholders and employees, but it will continue to have tremendous ramifications on the markets, specific sectors of the economy, and in the way stock analysis, credit rating agencies, and accounting firms do business. The status quo in many of these industries is no longer acceptable, and I suspect Congress and Federal agencies will be making several reforms over the next couple of months and years to prevent another company from slipping through the cracks. Congress will never be able to prevent another Enron from happening, but we can make it more difficult.

Today, we will be looking at the role Enron's Board of Directors played in the company's collapse. As has been said before, the Powers Report that was published in February is fairly critical about some actions taken by Enron's Board of Directors, while also acknowledging that critical information was withheld. I hope this Subcommittee can get answers today to some important questions about decisions the Directors made and their relationships with the company's management and outside contractors.

What is striking about the Enron collapse is that so many people, both inside and outside the company, failed to ask the questions that needed to be asked. Enron's failure did not occur because one person dropped the ball. Instead, it was an across-the-board failure of many individuals. In hindsight, I am sure that many of them wish that they had done more.

Thank you for coming today. I appreciate the time you have taken, and I am looking forward to hearing from you today on the Enron collapse. Thank you.

Senator LEVIN. Thank you, Senator Bunning.

We will now introduce our first panel of witnesses this morning who are either current or former members of the Board of Directors of Enron Corporation. These are the five men that we have at our witness table.

John Duncan, the former Executive Committee Chair for Enron Corporation; Dr. Herbert Winokur, Enron Corporation's Finance Committee Chair; Robert Jaedicke, former Audit and Compliance Committee Chair for Enron; Dr. Charles LeMaistre, former Compensation Committee Chair; and finally, Norman Blake, who is the Interim Chairman of the current Board of Directors and a former member of the Compensation and Finance Committees.

Pursuant to Rule VI of this Subcommittee, all witnesses who testify before the Subcommittee are required to be sworn. I now would ask our witnesses to please stand and raise your right hand.

Do you solemnly 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. DUNCAN. I do.

Mr. WINOKUR. I do.

Mr. JAEDICKE. I do.

Dr. LEMAISTRE. I do.

Mr. BLAKE. I do.

Senator LEVIN. We are going to use a timing system today. About a minute before the red light comes on, you will see the light change from green to yellow, which will give you an opportunity to conclude your remarks. We have your written testimony, which will be printed in the record in its entirety, and so we would ask that you limit your oral testimony to no more than 10 minutes.

Mr. Duncan, let us start with you.

TESTIMONY OF JOHN H. DUNCAN,[1] FORMER EXECUTIVE COMMITTEE CHAIR, BOARD OF DIRECTORS, ENRON CORPORATION, HOUSTON, TEXAS

Mr. DUNCAN. Chairman Levin, Senator Collins, and Members of the Subcommittee, good morning and thank you for the opportunity to address this Subcommittee. My name is John Duncan. From 1967 to 1985, I was a Director of Enron's predecessor company, Houston Natural Gas, and I was there when Enron began in 1985. I have served as the Chairman of the Executive Committee since 1986. Thus, I am the Enron Director who has served the longest period of time. Until the Fall of 2001, I considered Enron one of the great companies of this country, and I was proud to be one of its directors. I resigned from the Board in March 2002.

After receiving my bachelor's degree in business administration at the University of Texas, I set out to become a businessman, to start and run my own company. With the exception of the first job, in a family business, and a stint in the U.S. Air Force during the Korean War, I have not drawn a paycheck from a company of which I was not either the founder or the co-founder.

As co-founder and President of Gulf and Western and founder of Gulf Consolidated Services, both companies had small beginnings and wonderful success stories. During the course of my career, I have served on the board of seven New York Stock Exchange Companies, and, Senator Durbin, not all at one time. I have also served and chaired the boards of several important Texas institutions, including the Chancellor's Council of the University of Texas System,

[1] The prepared statement of Mr. Duncan appears in the Appendix on page 113.

Southwestern University in Georgetown, Texas, the Board of Visitors at M.D. Andersen Cancer Center, and all the metropolitan Houston YMCAs.

I provide that background to the Subcommittee to respectfully suggest that I have had substantial experience and exposure to the workings and to the role and to the duties of a board of directors. I also know a board's limitations. That is what I want to talk about today. In particular, I want to focus on what I believe are the elements of an effective board and why I believe the tragic events of Enron occurred.

First, I believe the directors must be individuals who possess integrity and intelligence. They also should collectively bring a broad spectrum of knowledge and experience in the areas of business and finance and in the particular fields that the company is in. People usually acquire this experience by having operated a company with a significant budget or by having obtained unique experience from other professions that are relevant to the company's mission.

The Directors of the Enron Board certainly possess, in my opinion, these qualities. My colleagues are highly ethical and of good character. As far as intelligence goes, I can simply say that if education is any measure, I believe I was one of only two directors who did not have a master's degree or a doctorate degree. Our directors are experienced, successful businessmen and women, experts in areas of finance and accounting, and have had experience in leading large institutions. Others, like our overseas directors, brought experience in certain areas of the world in which Enron saw great business potential.

Second, I believe the board must be dedicated and diligent in addressing the matters that are presented to it. The directors need to do their homework, analyze the issues, ask penetrating questions, and make decisions that are always in the best interest of the shareholders.

In my opinion, the Enron directors met this criteria. We worked hard. We prepared for meetings. We asked probing questions and imposed specific controls and procedures that management and outside advisors were required to follow. I know that my colleagues here today will address those items in more detail. We were also willing to say "no" to management when we did not agree with its recommendations.

A good example of exercising a board's responsibility and to act independently in the company's best interest occurred only last September, when all the indicators that we had were still positive and before any of the outside directors was aware that Enron was in trouble. We were presented two transactions at the Executive Committee and the Board; management requested to authorize the purchase of two pulp paper mills at a price in excess of $300 million cash. We did not approve these acquisitions because we were concerned about a prior acquisition in the same field; we did not like the purchase price; and we wanted to preserve our financial flexibility in the light of the September 11 tragedies. We postponed our decision, but we now know that subsequent events soon overtook us and the company.

I did not sit on the Audit Committee or the Finance Committee, but I did sit in as a guest at a number of their meetings. I witnessed my colleagues asking probing questions of management and independent accountants. In my opinion, these committees and these members thoroughly executed their duties.

Third, I think that a board cannot be successful unless it feels comfortable relying on the intelligence and integrity of the management, as well as other advisors who present matters to the board. With over 20,000 employees working at the company, with over 200 lawyers writing contracts every day, and with over 400 accountants posting the daily books, we, the directors, had to rely on the reports given to us by the officers of the company. Frankly, there is no other way that we could direct effectively a company of that size. We felt confident relying on the senior management of the company, as we truly believed we had hired some of the best and the brightest in the industry. National, independent publications lauded the Enron officers for their intelligence, leadership, and creativity.

Finally, I believe the management and other advisors reporting to the board must tell the truth. They must tell the complete truth, good or bad, in order for the board to make informed decisions. We now know this did not happen at Enron. The Board had implemented mechanisms and controls to ensure, at the very least, it obtained early warning signals of any impending problem. Among other procedures, we created a risk management officer position, and we staffed that department with nearly 100 employees. That officer and that department was responsible for reporting to the Board the most significant concerns and credit issues that faced the company. That did not happen.

It is now quite clear that significant information about related party transactions was withheld from us. We were not aware, for example, of the problems of Chewco. They were withheld from us for years. We were not informed about Raptor III. We were not told about the $800 million recapitalization of the Raptors in late 2000 and 2001. We were not told that employees, in addition to Andy Fastow, were participants in a number of partnerships, and we were unaware of their substantial windfall profits.

As late as the August 14, 2001 Board meeting, the Board was briefed on the financial condition of the company. Your staff has that briefing. The report was—earnings were up, balance sheet was stable, except maybe a credit rating improvement in the year 2002. Various Power Point slides given at that same meeting indicated to the Board that the company's good business was still improving as usual. The Powers Report and the reports we now have read in the press indicate that for many months, if not years, certain members of management and our outside auditors were well aware of the problems facing the company, and they did not tell us.

In sum, I do not believe that Enron's fall would have been avoided had the Board asked more questions, implemented more controls, or avoided certain financing projects, because they were too complicated or risky. Rather, I believe if management had implemented the Board's controls, as they assured us they had, if just one of the Board's officers or employees had fulfilled his or her corporate duty to reveal these problems or to any one director, or if the outside auditors had executed their obligation to convey to us concerns they privately expressed and documented amongst themselves, that I and we would not be here today.

I thank you for allowing me to make this statement.

Senator LEVIN. Thank you very much. Dr. Winokur.

TESTIMONY OF HERBERT S. WINOKUR, JR.,[1] FINANCE COMMITTEE CHAIR, BOARD OF DIRECTORS, ENRON CORPORATION, GREENWICH, CONNECTICUT

Mr. WINOKUR. Chairman Levin, Senator Collins, Members of the Subcommittee, good morning and thank you for the opportunity to address you. My name is Herbert S. Winokur, Jr. I currently am a member of the Board of Directors of Enron Corporation. I have served as Chairman of the Finance Committee of the Board of Directors and have been a member of the Board since the mid-1980's. I volunteered for and served as a member of the Board's special investigative committee, the Powers Committee, to understand what happened at Enron.

I appreciate the opportunity today to talk with the Members of this Subcommittee about the involvement of Enron's Directors in the related party transactions that have received so much attention and about our oversight of Enron more generally.

In my opinion, and it is only my opinion, one of the principal causes of Enron's failure was the loss of lender and investor confidence that resulted from the three significant restatements to Enron's financial statements presented in October and November 2001. Two related to earnings restatements for 4 and 2 years, respectively, and the third, a significant reduction in shareholder equity. While a related party was involved in each transaction, the related party aspect does not appear to have been a factor in any of the accounting errors.

In none of these three restatements did the Board or its Audit Committee have prior knowledge of the errors that were required to be corrected. In each case, Enron's management had approved the original financial statement presentations, and as appropriate, Arthur Andersen had certified or reviewed them.

With that in mind, I would like to discuss three areas. First, how Enron's Board of Directors and Finance Committee discharged its obligations; second, the specific circumstances in which we approved the LJM structures and the controls we put in place; and finally and very briefly, certain of the hedging transactions that the Board approved.

Enron's Finance Committee reviewed regularly the company's financial ratios and liquidity. At our meetings, Enron management routinely presented Enron's actual and projected financial ratios and near-term liquidity, a report on relationships and meetings with the credit rating agencies, and an analysis of Enron's borrowing costs relative to those of its competitors, which informed us of the market's contemporaneous view of Enron. Between meetings, we also received and read reports on Enron from Wall Street equity and debt analysts, including the analysts' detailed financial projections.

[1] The prepared statement of Mr. Winokur appears in the Appendix on page 116.

Let me turn to the Finance Committee's involvement in the approval and oversight of the LJM partnerships. The press and others have reported repeatedly that Enron's Board waived the code of conduct when it permitted Enron's Chief Financial Officer, Andy Fastow, to serve as general partner of LJM1 and LJM2. The Board did not.

For many years, Enron has maintained a code of conduct with which every employee must comply. It also permits the Chief Executive Officer to make a determination that an officer's investment "presents no probability of any conflict of interest."

When the Board approved LJM1 in June 1999, the Board adopted and ratified the determination by the Office of the Chairman that Andy Fastow's participation as managing partner "will not adversely affect the interests of the company." The Board was told that PricewaterhouseCoopers would be rendering a fairness opinion on the transaction between LJM and Enron with which we were presented and that Mr. Fastow would have no direct pecuniary interest in the Enron stock, which was used as part of that transaction as credit support. Enron publicly disclosed this transaction, including the related party aspect, and Arthur Andersen reviewed it as part of its 10–Q review in June.

At the October 1999 Finance Committee and Board meetings, Mr. Fastow recommended to obtain quick, flexible equity to Enron with reduced transaction costs, that he be permitted to organize and serve as managing partner of LJM2, a newly formed fund with outside investors that would be an alternative and optional source of private equity. There would be no requirement that Enron trade with LJM2. He proposed that the Chief Accounting Officer review and approve all transactions between Enron and LJM2.

The Finance Committee, after questioning, learned that Arthur Andersen was fine with the partnership structure and that LJM2's limited partners were expected to be institutional investors who would be able to remove Mr. Fastow without cause. The Finance Committee augmented these controls by requiring that the Chief Risk Officer also review and approve all transactions and that the Board's Audit Committee review all transactions annually and make any recommendations it deemed appropriate. The Board ratified the Office of the Chairman's determination that Mr. Fastow's participation would not adversely affect the interest of the company. Enron publicly disclosed LJM2 as a related party transaction.

Updates given to the Finance Committee about the LJM transactions were positive. At the May 2000 Finance Committee meeting, Mr. Fastow reported that he was personally devoting approximately 3 hours a week to the investment vehicles. We were also told that LJM2's investments had a projected rate of return of 17.95 percent. Mr. Causey, the Chief Accounting Officer, told us that Arthur Andersen was comfortable with the governance structure of LJM. We, of course, now know that the LJM2 investors received much higher returns.

The minutes of the October 2000 Finance Committee also show that the Committee continued to focus on Mr. Fastow's dual role. Mr. Fastow described to the Committee six of the mechanisms that had been put in place to mitigate any potential conflicts, one of which was that Messrs. Buy, Causey, and Skilling approve all transactions between the company and LJM funds. A second was that Mr. Fastow maintain his fiduciary duty to Enron. In addition to these controls that Mr. Fastow described, the Committee instructed management that the Board's Compensation Committee review Mr. Fastow's compensation and that the Finance Committee, in addition to the annual review by the Audit Committee, conduct a quarterly review of the transactions between the company and the LJM funds.

The Finance Committee received its first quarterly and the Audit Committee its second annual report on the related party transactions with LJM on February 12, 2001, from Mr. Causey. Mr. Causey discussed the Board-established guidelines for transacting with LJM. He then told the Board that the company had adopted certain procedures and controls in response to the Board's direction and reviewed the checklist review complemented by the adoption of additional controls. Mr. Causey informed the Finance Committee that the controls "had been discussed with the Audit and Compliance Committee and commented that the process was working effectively."

The preceding, I submit, illustrates that the Board applied Enron's code of conduct when it ratified management's recommendation regarding LJM1 and LJM2 and added substantial additional controls to ensure that all of the Enron LJM transactions would be in the best interest of the company. The record also indicates that the directors regularly monitored the LJM transactions and management's involvement. We asked for and repeatedly received reports informing us that the controls were working and that there were no concerns raised either by management or our outside auditors.

Let me turn to the financing. Enron has been criticized for its use of off-balance-sheet financing or special purpose vehicles to raise debt and equity. This practice is common and permitted by the accounting rules, if structured correctly. For example, leasing companies and reinsurance companies exist to provide off-balance-sheet financing to their customers. The Board also has been criticized for authorizing hedge transactions involving these vehicles that made use of Enron stock for credit support. Let me respond.

Enron owned certain highly volatile high-technology investments. That combination of volatile investments and required mark-to-market accounting had the potential to create instability and unpredictability in Enron's income statement. Putting in place hedges to mitigate these risks made good business sense. In fact, companies have been sued by their shareholders because they failed to put in place hedges on significant and volatile investments.

Management wanted, appropriately, to use the significant unrealized value and forward contracts on Enron stock most effectively for the benefit of Enron's stockholders. It informed the Board that the proposed hedge transactions did so. Outside auditors concurred, or in one case, provided fairness opinions.

In conclusion, what happened at Enron has been described as a systemic failure. I see it instead as a cautionary reminder of the limits of a director's role. A director's role, by its nature, is a part-time job. By force of necessity, we could not know personally all of

Enron's employees. As we now know, key managers and employees whom we thought we knew proved to disappoint us significantly, and outside advisors whom we believed to be critical components of an effective oversight role failed in their duty. Arthur Andersen's failure to disclose its concerns to the Board, as well as management's marked disregard for the required internal controls and lack of candor with respect to information owed to us deprived the Board and deprived me of the ability to deal proactively with these problems. We cannot, I submit, be criticized for failing to address or remedy problems that had been concealed from us.

Three months ago, days after the release of the Powers Committee report, I appeared before a House subcommittee. At that time, I was deeply disturbed and disappointed with what I had learned. I also squarely disagreed with certain conclusions, particularly about the directors' judgment and oversight, presented in the report, which disagreement I expressed during my testimony.

Even with the benefits of a few more months to review these issues, I remain resolute in my belief that we were diligent and dedicated to our charge. Based on the recommendations, advice, and information we received from management and our advisors, we, the directors, acted in good faith and attempted to pursue the best interests of Enron and its shareholders. However, I deeply wish that at least one person in management, an employee, or an outside advisor, someone had come forward to the Board with his or her concerns when we could have addressed them.

I am prepared to respond to any questions from the Subcommittee. Thank you.

Senator LEVIN. Thank you very much. Dr. Jaedicke.

TESTIMONY OF ROBERT K. JAEDICKE,[1] FORMER AUDIT AND COMPLIANCE COMMITTEE CHAIR, BOARD OF DIRECTORS, ENRON CORPORATION, BOZEMAN, MONTANA

Mr. JAEDICKE. Chairman Levin, Senator Collins, and Members of the Subcommittee, good morning and I also thank you for the opportunity to address the Subcommittee. My name is Robert Jaedicke. I served as the Chairman of the Audit Committee of the Board of Directors of Enron Corporation. As part of an overall restructuring of the Board, I recently resigned as a director, having served since the mid-1980's.

Let me tell you very briefly about my background. I joined the faculty of the Stanford Graduate School of Business in 1961. I served as Dean of the school from 1983 to 1990. At that time, I returned to the faculty of the Business School, and I retired from the university in 1992.

Throughout my tenure as Chairman of the Enron Board's Audit Committee, I was committed to ensuring that it was an effective and actively functioning body. Over the last few years, we undertook to review and strengthen our already vigorous control systems. In 1999, we began a number of initiatives to ensure that we remained a "best practices" audit committee. Throughout 2000 and into 2001, our committee worked with Arthur Andersen to make

[1] The prepared statement of Mr. Jaedicke with attachments appears in the Appendix on page 155.

sure that we complied with the recommendations of the Securities and Exchange Commission, the New York Stock Exchange, and the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees. That effort culminated in February 2001, when the Audit Committee drafted a new charter that was approved by the full Board.

The lifeblood of the work of any audit committee is the development and implementation of adequate controls, many of which cross-check each other. The committee's responsibility is to review reports from management and the outside auditors, to review the adequacy of internal controls, and to oversee the filing of financial statements. The committee's effective oversight also depends on the full and complete reporting of information to it. Without full and accurate information, an audit committee cannot be effective. The audit committee does not manage the company and does not do the auditing.

It is my understanding that audit committees of most corporations, like Enron, typically meet for a few hours several times a year. Warren Buffet wrote to the New York Stock Exchange Chairman and CEO Richard Grasso in 1999, and I quote, "An audit committee that meets for a few hours several times a year is simply not going to pick up anything that is missed by the outside auditors. Therefore, the task of the audit committee should be to hold the feet of the outside auditors to the fire." In that same letter, Mr. Buffet also stated, and I quote, "Simply put, audit committees cannot act as auditors. Their true job, and I would argue the only important function that they can adequately discharge, is to make sure that the auditors do their job instead of becoming subservient to management."

I agree. We held regular meetings at least four or five times a year; always four, usually five. At meetings, we received reports from a broad range of senior management and Arthur Andersen personnel. Audit Committee meetings regularly included three Arthur Andersen partners, Enron's Chief Accounting Officer, Chief Risk Officer, General Counsel, Chief Internal Auditors, Mr. Lay, Mr. Skilling, and other senior officers and outside advisors, as appropriate. We were entitled to rely on these reports. We asked questions. We provided oversight. We received several special reports on accounting policies. And we continually discussed the adequacy of our internal controls. I respectfully submit that we did our job.

At each Audit Committee, it was my invariable practice to hold—or at least offer to hold—an executive session with the Arthur Andersen representatives where they could meet with us without management present. There, Arthur Andersen could freely report to the committee any matters of concern that made the auditors uncomfortable, including whether they had any significant disagreements with management, whether they had full cooperation of management, whether reasonably effective accounting systems and controls were in place, whether there were any material systems and controls that needed strengthening, and whether they had detected instances where company policies had not been fully addressed.

Arthur Andersen did not raised concerns about the partnerships in these executive sessions. In fact, they normally reported to us that the structures and transactions were complex, they required judgment, but that they were in at an early stage to understand and review the transactions and that they were comfortable with the accounting treatment.

Last February, Alan Greenspan testified before the Congress, "I have served on too many audit committees to know that even though I would consider myself independent, I would consider myself knowledgeable, I did not know what questions to ask the Chief Financial Officer during meetings to find out what it is that conceivably is wrong in the corporation, and he was not about to tell me."

I agree with Mr. Greenspan. We did everything possible to ensure that our controls and procedures were being followed. To my knowledge, we were one of the few major corporations that required Arthur Andersen or their outside auditor to give an attest opinion on the management's assertions that our controls were adequate.

What happened at Enron, as my colleague has indicated, has been described as a systemic failure. I agree with him as it pertains to the Board. I see it as a cautionary reminder, also, of the limits of the director's role. We served as directors of what was then the seventh-largest corporation, which required us to confine our attention to the broad policy decisions. At meetings of the Board and its committee, in which all of us participated, these issues were considered and decided on the basis of summary reports, corporate records, upon which we were entitled to rely. We also relied on the honesty and integrity of management, their subordinates and advisors, and on the integrity of the information we were receiving. At the time, we had no doubt—we had no reason to doubt the integrity of either the management or the advisors.

We did all this and more. Sadly, despite all that we tried to do in the face of all the assurances that we received, we had no cause for suspicion until it was too late.

Thank you very much, and I am prepared to respond to questions from the Subcommittee.

Senator LEVIN. Thank you very much, Dr. Jaedicke. Dr. LeMaistre.

TESTIMONY OF CHARLES A. LeMAISTRE,[1] M.D., FORMER COMPENSATION AND MANAGEMENT DEVELOPMENT COMMITTEE CHAIR, BOARD OF DIRECTORS, ENRON CORPORATION, SAN ANTONIO, TEXAS

Dr. LEMAISTRE. Chairman Levin, Senator Collins, Members of the Subcommittee, we are delighted to be here to participate in your investigation. Senator Durbin, I want to assure you that we were shaken to the core, also. It is a very good description of what happened by the events that we first learned about on October 17, that our controls were not being followed. The Board thereafter took immediate action on several fronts, one of which was very val-

[1] The prepared statement of Dr. LeMaistre with an attachment appears in the Appendix on page 176.

uable to you in your investigation, the no-holds-barred Powers Report, which enlightened all of us as to where the problems were.

My name is Charles LeMaistre. I am a physician by profession. I am also President Emeritus of the University of Texas M.D. Anderson Cancer Center and former Chancellor of the University of Texas System. For 17 years, I have served on the Enron Board. For most of those years, I have held a position as Chairman of the Compensation and Management Development Committee. I resigned in March 2002 as a part of the restructuring of that Board.

I would like to directly address some of the questions that have been raised regarding compensation and the bonus process for executives. The Compensation Committee's basic responsibility is to assure that the senior executives of the company are compensated effectively in a manner consistent with the compensation strategy stated to the shareholders. The Committee considered internal equity, competitive compensation practices, and the requirements of appropriate regulatory bodies.

The philosophy behind the executive compensation is to reward executive performance that creates long-term shareholder value, in essence, a pay-for-performance philosophy that benefits the shareholder. Executives had the opportunity to earn up to the 75th percentile or higher of the compensation rates at comparable competitive companies, subject to obtaining a performance at 75th percentile or higher.

As a first step in this process, we received the recommendations from management and discussed their justifications fully. We also relied almost always on the outside executive firm, Towers Perrin, to independently review the recommendations and give us advice and a recommendation regarding the various compensation issues brought to the committee. Based on that advice, the committee arrived at proposals for presentation to the Board, and they deliberated on these very carefully and for long hours in order to arrive at a common position.

In recent years, the Compensation Committee was dealing with Enron's evolution from a pipeline company to an energy trading company that engaged in sophisticated and complex financing structures. Enron sought out different talent for its management in the energy trading business. To hire and successfully retain these highly-sought individuals, Enron needed to offer compensation packages equivalent to, and sometimes better than, those offered by the competition. Enron believed that the talented individuals leading the company were one of the most valuable assets the company had and critical to its success. Towers Perrin was often asked to craft compensation packages, stress test the executive compensation plan, and conduct surveys of competitive practices to be sure Enron was well positioned in the marketplace.

Let us go into some compensation-related issues. First, with regard to Ken Lay, the media and others have raised many questions about Mr. Lay's compensation. In particular, I would like to address the $141 million he received in total compensation for the year 2000. It has been suggested that this level of compensation was unreasonably high and over 10 times the average received by the CEOs of the top 200 companies.

First, I believe that comparing Mr. Lay's total compensation against the average salary of the CEO in a top 200 company does not necessarily yield an accurate picture. Because Mr. Lay's compensation placed him in the top 10 highest-paid CEOs, I believe that comparing his compensation to those in that category is more accurate. Within the top ten, Mr. Lay was ranked seventh that year. Enron, coincidentally, was ranked as the seventh largest company. The average compensation for the top 10 CEOs was about $169 million. The top compensation was $293 million. I have attached a chart to my statement that presents this information.

Second, I think it is important to break out what comprises Mr. Lay's total compensation package to determine the actual cost to the company for that year. A very large portion of the total compensation is at risk under the pay-for-performance philosophy. The portion at risk depends upon meeting competitive criteria for the future value from stock options exercised to be realized and from restricted stock payouts to be realized. For this portion at risk, the executive is rewarded only if the shareholder is rewarded.

If the "at risk" portion is subtracted from the total, you arrive at about $10 million, which I believe is a more accurate representation of what Mr. Lay's 2000 compensation cost the company that year. I also note that 2000 was an extraordinary year for Enron and its shareholders, which accounts for the large increase in bonus for that year. That is roughly $10 million, including his base salary of $1.3 million and a bonus of $7 million. Mr. Lay's compensation was disclosed and footnoted and detailed in the proxy statement each year.

Next, Andy Fastow's salary from the LJM partnerships. On October 19, 2001, the *Wall Street Journal* reported that Mr. Fastow and possibly some of his partnership associates received more than $7 million in compensation from the LJM partnerships. Let me comment on what I know about his LJM compensation.

On October 19, a special meeting of the full Board was called to discuss Mr. Fastow's compensation from the LJM and other related matters. We went into it in some detail, and on October 22, 2001, the Board authorized Mr. Duncan, Chairman of the Executive Committee, and myself, as Chairman of the Compensation Committee, to inquire directly of Mr. Fastow as to his compensation from the partnerships. Enron's General Counsel drafted the questions we would ask. I called Mr. Fastow on October 22 and arranged for a conference call the very next day.

On that call, Mr. Duncan and I asked Mr. Fastow about the amount of his investment in LJM1 and LJM2 and his return on those investments. Mr. Fastow responded that his commitment in LJM1 and LJM2 was $1 million and $3.9 million, respectively. He stated that his income from LJM1 was $23 million, and approximately $22 million from the LJM2. On October 24, the very next day, the Board met. Mr. Fastow was relieved of his responsibility as Chief Financial Officer.

I do not believe that the Board of Directors would ever have approved Mr. Fastow's participation in the partnerships if we had known he would be generating such compensation. Indeed, we were told just the opposite. Very conservative yields should come from the formulas that were presented to the Board. If management had instituted the controls that the Board authorized, Mr. Fastow's compensation would have been reported to Mr. Skilling, the Audit Committee, the Finance Committee, and the Compensation Committee.

On October 6, 2000, the Finance Committee meeting minutes clearly show from his own presentation that Mr. Fastow was aware of the six controls imposed by the Board on his participation in LJM, including his responsibility to review with Mr. Skilling "his economic interest in the company and the LJM funds." Following Mr. Fastow's presentation, the Finance Committee then added to the existing controls a quarterly review of the LJM transactions and a review by the Compensation Committee of Mr. Fastow's LJM compensation. That meant there would be two full reviews by the Finance Committee and the Audit Committee, one on a quarterly basis and the other on an annual basis, through which that information should have come in addition to the newly authorized review by the Compensation Committee.

Enron's Performance Unit Plan has been confusing to many. I would like to comment briefly on it. Prior to 1999, Enron granted performance units to corporate and certain operating company executives who were not in an Enron long-term incentive plan at that time. These operating company executives were, for the most part, in commercial support and in the pipeline business. Enron was a highly decentralized company at that time.

The first performance units were awarded in 1987 and the last in 1998. The units have a life of 4 years, so the payouts could still be continuing as of last year. Awards were based on Enron's total shareholder return over the 4 years. The participants were nominated by the Office of the Chairman and approved by the Compensation Committee. There was a limit of three million performance units per individual. Performance was measured against that of a performance of peer group of companies with a payout scale of one to seven. Each unit was assigned a valuation of $1. A ranking of one had a payout of $2, twice the value, and a ranking of seven did not pay out anything. In the event that the total shareholder return did not exceed the cumulative percentage for the 90-day Treasury Bill, a performance unit would have no value.

In conclusion, I believe that our Committee and the Enron Board endeavored to manage carefully and effectively Enron's executive compensation while the company was rapidly evolving, growing, and undertaking new business opportunities. The Committee sought and relied on the advice of outside executive compensation experts to ensure our recommendations and decisions were consistent with the marketplace. Although the Board was willing to award compensation that was competitive and deserved, it certainly did not approve and was not made aware by management that some individuals reaped huge profits at the company's expense or that others abused certain benefits in ways for which they were not designated.

Thank you very much for your attention. I will be pleased to answer your questions.

Senator LEVIN. Thank you very much, Dr. LeMaistre. Mr. Blake.

TESTIMONY OF NORMAN P. BLAKE,[1] INTERIM CHAIR, BOARD OF DIRECTORS, ENRON CORPORATION, ROSEMONT, ILLINOIS

Mr. BLAKE. Thank you, Mr. Chairman. It is good to be here, Senator Collins and Members of the Subcommittee. It is certainly a privilege to be here and I thank you for the opportunity.

My name is Norm Blake. I am Interim Chairman of the Board of the Enron Corporation. I have been a Director of Enron since 1993. Since the onset of bankruptcy, five members of the Board and I have been actively engaged in the development of a newly constituted Board of Directors in cooperation with Enron's Creditors Committee. It is the intention of these Board members and me to resign from the Board once an orderly and effective transition of authority has taken place. We are now serving on a pro bono basis in recognition of our responsibility to serve the interests of Enron's stakeholders and employees.

My background can essentially be characterized as having extensive management and leadership experience in a variety of industries, with significant involvement in financial services. Over the last 12 years, I have been Chairman and CEO of three different Fortune 500 companies and held board membership positions in others. Much of my earlier business career was with the General Electric Company, with my latest position in 1984 being Executive Vice President of Financing Operations for the General Electric Credit Corporation.

My colleagues in their statements today will discuss the Board's and its committees' respective roles and involvement in the related party transactions. I would like to focus on certain issues that have been raised with respect to the Board and the outside Directors as a collective unit.

I will begin by saying unequivocally that I am proud to have served as a member of the Board with such capable, hard working, intelligent, and ethical individuals. Personally, I believe while we may have initially just been a collection of individuals, we have now evolved into a very cohesive and collegial group. Moreover, in my view, this Board has remained diligent and dedicated to its responsibilities throughout the process.

Although we, at the time, had much confidence and respect in the abilities of the management of the company, we did, in fact, operate independently and did, in fact, exert our influence, and at times, contrary to the wishes of management. For example, the decision made by the majority of the Board to acquire Wessex and form Azurix was made over the dissention of two Directors and abstention of another. More recently, management's intention to acquire a pulp mill in October of last year was resisted by the Board to the extent that the decision was not made to make the acquisition.

Allow me to put Enron into perspective over the last couple of years, and as cited by many of you this morning. By 2000, Enron was one of the 10 largest companies in the United States. Enron had begun a transformation from a traditional pipeline and energy company with substantial fixed assets to an innovative energy

[1] The prepared statement of Mr. Blake appears in the Appendix on page 181.

trading company that showed tremendous potential but required liquidity and creditworthiness.

My personal focus as a member of the Board and its Finance Committee had been Enron's liquidity and financial leverage in furtherance of this strategy. As a Board, we were attentive to and working with management and outside experts to realize this mission. We believed that the company was successful in moving in that direction. In late 2000 or early 2001, no one had predicted by the end of 2001, Enron would file for bankruptcy. In fact, as late as October 2001, we were informed by management that we were ahead of plan in terms of earnings and that creditworthiness and liquidity issues were manageable.

A central issue at hand involves Enron's intentions in establishing SPEs. I would like to provide an opposing point of view to that held by many that the intention of Enron in establishing these partnerships was to manufacture earnings. To the contrary, it is my opinion that the primary purpose of these partnerships was to improve liquidity and get debt off our balance sheet. The LJM partnerships were specifically constituted for that purpose, and by the way, I would contend that many companies establish SPEs for exactly such a purpose.

Of course, now, with the benefit of hindsight, committees of Congress, the media, government officials, financial experts, and others have tried to dissect and examine what went wrong at Enron. Over the past several months, several questions have been raised with respect to the Directors as a group. In particular, people ask if the Board failed in its oversight duty, whether Enron was moving so quickly that independent directors could not keep up.

I think not. We worked hard. We worked very hard. We came prepared and we asked questions. We were sent materials in advance of meetings and it seemed that each Director reviewed them and came to the meetings prepared. Sometimes before a Board meeting, after spending many hours in preparation for these meetings, I would speak with Mr. Skilling about the balance sheet issues or with the Chief Risk Officer, Rick Buy, about liquidity, leverage, and credit issues.

I know that my fellow Director Pug Winokur, who is here today, spent time with Enron's Chief Financial Officer, Andy Fastow, before meetings, asking him a variety of questions. And Dr. LeMaistre, who is also appearing with us today, spent much of his time in advance of upcoming Compensation Committee meetings with Enron's human resource and compensation staff, as well as external consultants, to ensure himself that he understood all the technical aspects of Enron's compensation plans and to be in a position to evaluate recommendations made by management. He took his job very seriously, as we all did. In short, I believe, judged by any standard, that this Board executed its duties to the company and its shareholders.

During Board and committee meetings, we did, in fact, question management. For example, during October 1999 Finance Committee, in which we discussed the LJM2 partnership, the Board material discloses that I specifically asked whether Arthur Andersen had reviewed the partnership. We were told by the Chief Accounting Officer that Arthur Andersen was, "fine with it." If we had been told that Arthur Andersen had not reviewed the structure or that Arthur Andersen had reservations, this Board would never have approved it.

The first Raptor transaction was brought to the Finance Committee, in May 1, 2000. The minutes reflect the Chief Accounting Officer told us that, "Arthur Andersen LLP had spent considerable time analyzing the Talon structure and the governance structure of LJM2 and was comfortable with the proposed transaction." This advice was critical to our decision to authorize this transaction. Some commentators have since suggested that the structure of this transaction was inappropriate on its face. This is not the advice that we received. My fellow directors asked questions pertaining to propriety and the oversight of these transactions. We did not rubber stamp management's recommendations and requests.

Even with the benefit of hindsight, I cannot speculate as to what else we could have done to ensure that our controls and procedures were followed. We put the right controls in place and we asked the right questions. These directors were a smart and talented group of people who brought a diversity of experience and expertise to the Board. Unfortunately, I believe that we were uninformed because management and outside experts who reported to us failed in their jobs and did not give us full and complete information.

Again, I thank you for being here today. I welcome the opportunity to answer your questions. Thank you, sir.

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

Let me start with you, Dr. Jaedicke. You were Chairman of the Audit Committee. The Audit Committee got an annual briefing from Andersen about its accounting policies and its practices, as you have testified. We have a number of excerpts from those briefings in the exhibit book, and I wish you would turn to Exhibit 2.[1]

Mr. JAEDICKE. Yes, sir.

Senator LEVIN. Exhibit 2 is part of the Andersen briefing on February 7, 1999. It relates to the Enron financial reporting in 1998, which was the previous year that had just finished. Now, this was an unusual Audit Committee meeting, because instead of taking place in Houston, it took place in London. Do you remember this meeting in London?

Mr. JAEDICKE. Yes, I do.

Senator LEVIN. Thank you. The Board's minutes reflect that David Duncan, the Andersen partner who headed the Enron audit team, and that Tom Bauer, who was also on the audit team, and that Steve Goddard, who was head of the Andersen office in Houston, were in attendance. Those were the three Andersen partners who typically dealt with your Audit Committee and the Board, and the minutes show that all of the Audit Committee members were there, as well as another Andersen employee and several members of Enron management, including Mr. Lay and Mr. Skilling.

Now, this chart, or this document that you're looking at says at the top "Risk Profile," which means the risk to Enron that its accounting practices may not be found to be in compliance with sound accounting practices. And you will see there the letters "H",

[1] See Exhibit No. 2 which appears in the Appendix on page 204.

"M", and "L", and those letters stand for high, medium, and low risk. So "H" stands for high, "M" for medium, and "L" for low risk.

Andersen was telling your Audit Committee about the risks, and the first item you will see on the list is highly structured transactions. These are the elaborate transactions which I talked about in my opening statement. And the chart here shows high risk, "H", circled for emphasis, in all three categories, including accounting judgments. So the document indicates—and this is a document from your files, so we know you were shown this document—that Enron was engaging in high-risk accounting practices when it came to those structured transactions. Do you remember that presentation?

Mr. JAEDICKE. Yes, I do. Would you like me to comment on it, sir?

Senator LEVIN. Feel free to do that.

Mr. JAEDICKE. I think the way—the interpretation—this was a template given to the Audit Committee to try to help us—to help us understand the kinds of accounting policies that were important to the company.

Now, maybe "risk" is a poor term, but if you look, for example, at highly structured transactions, I think the way to read this, and I think the comments generally support this, is to say energy asset securitizations—now, this is in 1998—that the accounting judgments—read "H" as important. They are important because there is a risk that——

Senator LEVIN. I am going to read "H" for what it stands for, which is high.

Mr. JAEDICKE. The risk, the judgments, they are complex. They need to be made very carefully.

Senator LEVIN. Are you denying that "H"——

Mr. JAEDICKE. Now just let me——

Senator LEVIN. Excuse me. Are you denying that "H" means high?

Mr. JAEDICKE. OK, high. Disclosure judgment, the importance is high. The risk is high. It needs to be done carefully. The rule change—risk in the sense of rule change, I think simply means there is a high probability that the rules in this area will develop and can change, and they did.

Now, if you just allow me to contrast that with something like purchase accounting down in the middle of the page, to judge whether the purchase accounting can be used instead of, say, a pooling of interest, that is an important, in your terms, high-risk area. You need to make a very careful judgment. But then if you move over, the disclosure is "M". I would assume that is medium. And it is because that issue has been around for a long time and there is a fair amount of guidance on it. It was already in existence in 1998. And if you go to the rule change, under "L", some rule change coming along, the odds were fairly low. About the only one at that time that was under consideration was to do away with pooling.

And so I think what this is and what we used it for was a way of saying, well, where are the sensitive areas, what are their disclosure characteristics, and what are the odds that rule changes will come along and somehow change what either we have to do or the way we have to disclose or the way in which the accounting has to be done. That is my interpretation, sir.

Senator LEVIN. Well, these are not my terms. These are Arthur Andersen's terms and they are circled. The "H" is not my term. It stands for high. You can say that the "H" under rule changes means there is a high risk that the rule may change, and I fully agree with you, but by that same logic, the "H" under accounting judgments means there is a high risk involved in that judgment.

So, Dr. Jaedicke, these are not my terms. These are the documents presented to you with "H", high risk, circled by Arthur Andersen in 1999.

Next, Exhibit 3.[1] The handwriting on this document belongs to David Duncan.

Mr. JAEDICKE. Yes.

Senator LEVIN. It is his handwriting on it, and this is basically Andersen's version of the previous exhibit, with the same matrix, but now it is a document with their talking points for the presentation that was made to you at that London Audit Committee meeting.

I would like to direct your attention to the handwritten note in the lower right-hand corner. It is hard to read, so we put it up on the board here and made that Exhibit 4.[2] This is what that note says at the bottom. "Obviously, we are on board with all of these, but many push limits and have a high 'others could have a different view' risk profile." High-risk profile. This is Duncan's note on this document. Then it lists those various accounting practices which you also see on Exhibit 4.

So not only was the Audit Committee told by Andersen that although Andersen was on board, that many of Enron's accounting practices, in the words used there, his note, "push limits," and that others could view them as outside of compliance with Generally Accepted Accounting Principles. Now, do you remember David Duncan telling that to the Audit Committee on February 7, 1999?

Mr. JAEDICKE. I do not remember David Duncan telling us this particular note. David Duncan did tell us on several occasions that these were complex transactions, that they were complex structures, that Enron was a complex company. They were moving very fast, and very careful accounting judgments were required.

He also would, on occasion, try to indicate to us how much guidance was available on those. But in terms of—and I do not recall him saying, well, others could have a different view. But I think all of us understood that these were highly structured, new kinds of transactions, but please, sir, keep in mind, that was one reason that Enron paid Arthur Andersen some pretty hefty fees, to try to be in on the beginning of these transactions so that those accounting judgments, they understood the transaction and that the accounting judgments would be properly made.

Senator LEVIN. You do not remember David Duncan notifying your Committee that these were high-risk accounting approaches?

[1] See Exhibit No. 3 which appears in the Appendix on page 208.
[2] See Exhibit No. 4 which appears in the Appendix on page 209.

Mr. JAEDICKE. I remember these—this chart, sir. I cannot say that I remember this quote that is in the bottom of his—the lower right-hand corner of the——

Senator LEVIN. If he had told you that they were high-risk accounting approaches, would you remember it?

Mr. JAEDICKE. I think I would. I do not quite—we knew these were important transactions.

Senator LEVIN. I am using the words "high risk." You can try to change that from a "H" to an "I". I am saying that the "H" was circled. It was Andersen's word. It was presented to you in the document in Exhibit 2. We have Duncan's note saying specifically that these push limits. Those are his words on his copy of the document, and you are saying you do not remember him using the words "push limits," is that correct?

Mr. JAEDICKE. I do not remember the words "push limits."

Senator LEVIN. OK. Let me just keep going, then. Now, Andersen also rated the accounting risks that Enron was taking. They did their own rating, which is reflected in the documents which you have just seen. This analysis is done at accounting firms for a number of reasons, and the Andersen analysis upon which those first two documents were based are Exhibits 10a and 10b. If you could look now at Exhibits 10a and 10b——

Mr. JAEDICKE. Exhibits 10a and 10b——

Senator LEVIN. Let me go back. I missed a document that I wanted to show you, Exhibit 5,[1] so if I could just interrupt the flow here for a moment——

This is a letter that we received last week from legal counsel representing Arthur Andersen's partner, Tom Bauer, who was at that London meeting and participated in the discussion. Here is what this letter says, and this, again, is Exhibit 5 in the book. "Certain risk areas were described as pushing the limits, as reflected in Dr. Duncan's note, or as being at the edge."

So now we have Exhibit 2, which you acknowledge was before you, with that circled "H" for high-risk accounting approaches. We have Exhibit 3, which has Duncan's note as to what he was telling you. And now we have an exhibit which supports those two earlier exhibits. This is a letter which says that Mr. Bauer remembers that, "Certain risk areas were described as 'pushing the limits,' as reflected in Mr. Duncan's notes, or as being 'at the edge'."

So now we have got that memory of Bauer, which is added to Exhibits 2 and 3. So now your memory differs also with Bauer as well as with the exhibit itself.

Now I want to move you over to Exhibit 10.[2] This is a document which was Arthur Andersen's internal document, but upon which Exhibits 2 and 3 had either been based, or it is similar to a document in which those conclusions were reached.

First, if you would turn to Exhibit 10a.[3] This is for the year 2000. This is for a later year, and I am going to give you this and then go back to 1999. Take a look, if you would, at the line which is marked on the first page there in which it says, "Accounting and Financial Reporting Risk—Very Significant." "Management Pres-

[1] See Exhibit No. 5 which appears in the Appendix on page 210.
[2] See Exhibit No. 10 which appears in the Appendix on page 222.
[3] See Exhibit No. 10a which appears in the Appendix on page 222.

sures"—do you see that, on driver number five? Do you see that on the front page? "Management Pressures—Very Significant."

This document, signed by David Duncan, this risk classification offers several comments which justify their conclusion. On the front page, under "Management Pressures," "Enron has aggressive earnings targets and enters into numerous complex transactions to achieve those targets." Also on the front page, "The Company's personnel are very sophisticated and enter into numerous complex transactions and are often aggressive in structuring transactions to achieve derived financial reporting objectives."

The 1999 risk analysis is Exhibit 10b and it uses similar—let me get you to the third page of Exhibit 10a before we turn to Exhibit 10b. It's under "Risk Classification and Rationale." It says, "Risk Classification: Maximum." Do you see that there?

Mr. JAEDICKE. I see it.

Senator LEVIN. Do you see where it says "Prior Year Risk Classification," and it says "Maximum"? Now, these are risk classifications.

Mr. JAEDICKE. I see it.

Senator LEVIN. Now we will go back to 1999 and Exhibit 10b.[1] And again, these are further evidence not only that Andersen considered Enron to be engaged in high-risk accounting and had management pressure, but they also substantiate the Duncan note, the Bauer letter, and Exhibit 2 which was directly presented to you and which talked about high-risk accounting transactions.

But if you will look now on Exhibit 10b, you will see under "Complex/risky transactions," where it says, "Form over substance transactions." "Form over substance transactions"—this is 1999, now, we are talking about. The box that they check is "Very Significant." So your auditor viewed Enron accounting practices as being high risk. They said that the use of form over substance transactions was very significant and that very strongly supports the Duncan note as to what he told you in London in 1999 and Exhibit 2, which was directly handed to you and which said that your accounting practices were high-risk practices.

And despite all of that, what you are saying is you do not remember or you deny that your auditor told you in 1999 and 2000 that you were engaged in high-risk accounting practices, is that correct?

Mr. JAEDICKE. We knew that the company was engaged in high-risk and innovative transactions. But if you contrast this, if David Duncan had given this to the Audit Committee, my guess is the discussion would have been a lot different than it was.

If you go back and you look at the Audit Committee, the various meetings, Senator, you would find that on almost every agenda, there were listed—you would look at what were the audit emphases of the past quarter and what were the audit emphases of the quarter coming up, and they would almost always list related party transactions, structured transactions, securitizations, and mark-to-market and fair value. Those were almost always areas of emphasis.

[1] See Exhibit No. 10b which appears in the Appendix on page 226.

Now, when we would ask them, even in executive session, about, OK, how do you feel about these, the usual expression was one of comfort. It was not, these are the highest risk transactions on our scale of one to 10 or whatever this is. If the information in this kind of a document had been conveyed to us in the terms that it showed here, the template that you showed me, the "H"s were almost always interpreted, at least by me, as saying if you want a template of those accounting areas that are important to Enron and deserve our emphasis, that is where you would look, and the "H"s were no surprise. Those were almost always on the agenda of the Committee.

Now, this kind of information, where you say pushing the limits or whatever—form over substance, I never, ever heard that term used.

Senator LEVIN. The reason that——

Mr. JAEDICKE. That I recall.

Senator LEVIN. The reason that is so important is because what was presented to you were the "H"s, not "I"s, not "M"s, not "L"s, "H"s, high-risk accounting judgments. You acknowledge that. Now the question is, well, wait a minute. Did that mean what it said? Then you have got a note contemporaneously from Duncan, as well as from the other witness who was there, saying you, in fact, were informed that these were pushing the limits at that meeting. You deny hearing that, but there is very strong evidence that, in fact, that occurred—the evidence: Contemporaneous notes, statement of another witness, and the internal documents of Arthur Andersen—show that was, indeed, their conclusion.

You put all that together, and the evidence is pretty strong that you were informed these were high-risk accounting practices but that you did not act on those notes and that information. That is what jumps out from these exhibits and from this testimony. So weigh that against "you do not remember"—it seems to leave me with one conclusion. You may not remember——

Mr. JAEDICKE. All I said was I do not remember the particular wording of the comment that you showed me on that particular—on that slide.

Senator LEVIN. Thank you. Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman.

Dr. Jaedicke, in an interview with the Subcommittee staff, Lord Wakeham indicated that he had been concerned that Andersen's high level of involvement with the company meant that Anderson might be too close to Enron's management. As Chairman of the Audit Committee, did you ever have a similar concern?

Mr. JAEDICKE. Well, Senator, we—on the independence issue, for the last couple of years, we had a very sort of set pattern of trying to assure ourselves that, in fact, Arthur Andersen was independent. It worked like this.

There is a series of criteria and guidelines that are set forth by, for example, the Independent Standards Board. We would discuss those usually in the August meeting and we would also hear from Arthur Andersen how their internal processes on affecting the independence issue worked, and those stemmed all the way from saying, well, how do you monitor and handle the relationships of family members, all the way over to saying, what do your internal dispute resolutions look like for partner disputes? How do they work at the local level? How do they work at the Chicago level? How do they work worldwide? And they would go over in August with us all of the—sort of their internal processes for assuring independence.

And then in the February meeting, when we reviewed the financials and we had to make a recommendation to the auditors, we heard a representation from the Arthur Andersen engagement team that the firm had assessed its independence using these procedures and criteria and that they believed they were independent. So in February, we would receive their independence—or, excuse me, their representation.

Senator COLLINS. I understand that the Audit Committee accepted the representation of Andersen that it was independent, but I do not understand why the Audit Committee would accept that assertion given that Andersen had consulting, and internal and external auditing roles for Enron. Essentially, was not Andersen passing judgment on its own work? We have talked with numerous experts who are very critical of having the outside auditor also do some internal auditing as well as consulting work. Does that not set up a situation that is just ripe for conflicts of interest?

Mr. JAEDICKE. Let me speak to the so-called integrated audit, which is commonly phrased as doing the internal auditing. You have to keep in mind that Enron probably had about on the order of twice as much internal auditing as Arthur Andersen did. We had a Risk Control Group that consisted of, I do not know, 100 people or more. We had the Enron Assurances Group, which were a group of internal auditors that had internal auditors in each business unit, and we had an Information Technology Auditing Group.

Now, that alone would be a sizeable amount of internal auditing. What the integrated audit tried to do, two things. One is to say, Arthur Andersen, you have to review the adequacy of internal controls in order to make a judgment on the fairness of the financial statements. What we would like you to do is to go farther than that and do enough internal auditing on the adequacy of the internal controls, where you control the scope, not management, such that you can give us an attest opinion on management's assertion that the controls are adequate.

Now, I was in favor of that because otherwise, you get the assertion that says, we do not know of any material weaknesses. It is a very positive opinion.

But the other thing I wish to emphasize is they were not auditing their own work. For example, my colleague Dr. Winokur, and I, worked for a couple of years responding to drafts from the management who was working on a risk management policy, not only for the trading, but for liquidity and many other things. When the Board adopted that policy, it was our policy, but what we wanted Arthur Andersen to tell us is, we have done enough auditing to assure you that it is the management's contention that it is adequate and we also will be able to tell you it is being followed. That is what we were after.

Senator COLLINS. Were you aware that the fees paid to Andersen had increased dramatically, from $29.6 million in 1998 to $46.4 million in 1999?

Mr. JAEDICKE. That is total.

Senator COLLINS. That is total.

Mr. JAEDICKE. Yes. Well, we were reported the fees, but I think about half of that, Senator, would be the baseline and the integrated audit—the baseline integrated audit and the fees that they charged us to express an accounting opinion on the transactions.

Senator COLLINS. My point is that this work was pretty lucrative for Andersen and Andersen was playing more and more of a role and passing judgment on transactions that were risky, to say the least. Should it not have been a red flag to the Audit Committee, given how lucrative this business was, that Andersen might not be as forthcoming as it should have been? You have been very critical of Andersen for not sharing information. Should these not have been red flags that Andersen was playing more and more of a role, such that Lord Wakeham raised a concern about it?

Mr. JAEDICKE. Are you asking for my opinion?

Senator COLLINS. I am.

Mr. JAEDICKE. In my opinion, I did not see it as a red flag. I saw it actually as some comfort that said the management is willing to pay fees large enough to get Arthur Andersen to tell us in a positive way whether our internal controls are adequate and functioning, rather than to have an internal auditor working for the company do it, which was always, to me, a problem.

Senator COLLINS. Let me ask you this question. The SEC had a blue ribbon commission in 1999 and 2000 that made several suggestions to ensure the independence of auditors. Are you familiar with those?

Mr. JAEDICKE. Well, I am familiar with some of their rules.

Senator COLLINS. Let me ask you about a specific one, if I may. One of the recommendations that the SEC made was that the Audit Committee obtain a written statement from the auditor listing all of the relationships between the auditor and the company, and that the Audit Committee should then discuss each of those relationships and pass judgment—the Audit Committee should pass judgment, not the auditor passing judgment on itself—on whether or not any of those relationships compromised the independence of the auditor. Was that done?

Mr. JAEDICKE. The review of independence in August, I think, would have included that, because I think one of the criteria or one of the issues that you had to look at had to do with those relationships, and they reported to us on, well, what are the firm's policies when you have people go to work for Enron? They also reported to us at one point, and I would have to look at the details because I have forgotten it, that there was a small joint venture, I believe on some software, and I really have to go back and look at it and see what the details were. It was considered to be immaterial, but it was disclosed to the Audit Committee.

Senator COLLINS. Dr. Jaedicke, you have a lot of experience. Have you ever known an auditor to come in and say, "we are not independent," or "we are too close to management"?

Mr. JAEDICKE. No, I guess——

Senator COLLINS. Is it not the job to be——

Mr. JAEDICKE. They would not last very long if they did that.

Senator COLLINS. Exactly my point.

Mr. JAEDICKE. I agree.

Senator COLLINS. When the auditor is making over $40 million a year, the auditor is not likely to come to the Audit Committee and say anything other than that it is independent. Is it not the job of the Audit Committee to make sure that the auditor truly is giving full, accurate, and independent advice to the Board?

Mr. JAEDICKE. I think the way we tried to do that, Senator—I agree, we should try to do it—was to say OK and once a year, at least, lead us through all of the controls that the firm has in place to help assure their independence. Again, an Audit Committee's work is on the adequacy not only of the company's controls but also of the controls of their outside advisors, and we did that.

Senator COLLINS. As the Chairman of the Audit Committee, you were the Board member most responsible for ensuring that there was full and complete and accurate communication between Andersen and the Board. In your tenure as Chairman, how often did Andersen tell you of problems that concerned Andersen with the management of Enron?

Mr. JAEDICKE. Well, they would usually—let me define problems. They would usually—these would usually come out in the form of saying, for example, we are engaged in a review of the internal controls of the new businesses, and then we would—and so they would—there was reason to believe you needed to concentrate on the controls. There was need for, for example, some pre-measurement type of controls in Enron Energy Systems at one point. We were concerned about were there access issues in Enron On-Line. Now, things of that nature would come out in talking to the Audit Committee and then we would follow that.

And if you looked, for example, at the minutes, you would find that the next meeting, they would say, significant progress has been made in these areas. And so they did—the types of problems that they talked to us about were usually in connection with their auditing emphases or the controls that were inherent in a particular business unit or things like that, and they brought those to our attention.

Senator COLLINS. Mr. Duncan, in February 2001, *Fortune* magazine ran an article about Enron and questioned whether its stock was overpriced. According to the story, the company was described by one analyst as impenetrable, a black box to outsiders. Another said the lack of clarity was a red flag. You told the Subcommittee staff that you remembered the article, that it was not flattering, that you were concerned about it. Did you ask Andersen to take a look at the allegations in the article?

Mr. DUNCAN. I did not. You must remember, I was not on the Audit Committee. But to answer your question, I did not ask Andersen to take a look.

Senator COLLINS. Did you bring it up in your role as Chair of the Executive Committee to any of the executives of Enron?

Mr. DUNCAN. I do not remember doing so.

Senator COLLINS. Dr. Jaedicke, did you bring it up to the other members of the Audit Committee or to Andersen and ask them to look into it? *Fortune* magazine is a well-regarded publication and these were pretty serious criticisms of the business for which you were on the Board. Did you take any action in response to it?

Mr. JAEDICKE. Not in response to that particular article, ma'am, no.

Senator COLLINS. Mr. Duncan, in October 2001, and I actually want all of the panel to answer this question, the Board became aware that an Enron employee had written an anonymous letter to Ken Lay. We now know this as Ms. Watkins' memo. Mr. Lay advised you that he had met with the employee and turned the matter over to Vinson and Elkins for further review. He obviously thought the charges were serious enough to warrant a review, but then he reported to you that there was no substance to the charges.

I would like to ask each of you, and since my time is fast running out, if I could just get a quick answer, did you ask to see the Watkins memos? Mr. Duncan.

Mr. DUNCAN. I did not.

Senator COLLINS. Dr. Winokur.

Mr. WINOKUR. I did not.

Senator COLLINS. Dr. Jaedicke.

Mr. JAEDICKE. We asked for a written report after they gave us an oral report and they had characterized the essence of Ms. Watkins' comments in that oral report, and we asked for a written report afterwards, which we got, but not until fairly late.

Senator COLLINS. Did you see her memo which warned that the company could implode in a wave of accounting scandals?

Mr. JAEDICKE. The first time we asked for the report, at least the Audit Committee did not get the memo. Now, I am talking about December.

Senator COLLINS. Right. But did you ask——

Mr. JAEDICKE. Then we asked for the memo.

Senator COLLINS. When did you ask for the memo?

Mr. JAEDICKE. When we got the written report from Vinson and Elkins, which turned out to be—you have got to remember, a lot of things happened—which turned out to be at the December Board meeting in 2001. That is when I got the memo.

Senator COLLINS. Dr. LeMaistre.

Dr. LEMAISTRE. My recollection is exactly like Dr. Jaedicke's. We got the memo after we heard the report. We only had an oral report saying that there was going to be an investigation. When the investigation was reported, we asked to see the memo.

Senator COLLINS. Mr. Blake.

Mr. BLAKE. Mine is very similar, and I do specifically remember asking for a written—we did not have a copy of the letter at the time that the report was given to the Board and we specifically asked also for a copy of the letter as well as a report from Vinson and Elkins.

Senator COLLINS. Dr. Jaedicke, former SEC Chairman Rod Hills has said very strongly that he feels the Audit Committee should have engaged an outside firm to review the allegations in the memo rather than leaving it up to the CEO. Could you comment on that?

Mr. JAEDICKE. Yes, I could comment on that, Senator. The memo was—actually, memos. There were, I think, two of them, a letter and a memo that were given to Mr. Lay, in August at some point. Mr. Lay handled those as they would have been handled under the code of conduct. They would have required an investigation. And we did not hear about the results of that investigation. We did not hear there was an investigation underway until about the time of the October Audit Committee meeting. By that time, the investigation had been completed.

The investigation turned up no new information. I can come back to that if you like. But it also—some of the issues that she had brought up were not even verified by the people whom she had named, or at least who were thought to know something about them. The investigation was completed and it did not say, I do not think, that there was nothing, there were no problems. I think what it said is that no further investigation seems warranted.

Senator COLLINS. That really is not my point. My point is that the CEO chose the firm to do the investigation of the allegations against the firm, and Rod Hills says, as a former SEC Chair, and I agree with him, that it would have been better and would have allowed for a more thorough review of the allegations for the Audit Committee to control that.

But let me move just quickly to another point, if I may.

Senator LEVIN. I wonder if I could just intervene for one second——

Senator COLLINS. Please go ahead.

Senator LEVIN [continuing]. Because I want to just pursue one aspect of the point which Senator Collins just raised to make sure I understand your answer. No one on the Board saw a copy of the Watkins memo until after the Powers Committee report was completed, is that correct?

Mr. JAEDICKE. No. I do not think——

Senator LEVIN. In that case, I will let your answers stand the way they were.

Senator COLLINS. Thank you.

Dr. LeMaistre, you attended the October 6, 2000, Finance Committee meeting in which Mr. Winokur suggested that Andrew Fastow's compensation should be reviewed by the Compensation Committee, is that correct?

Dr. LEMAISTRE. That is correct.

Senator COLLINS. And I believe Dr. Winokur proposed that review as a control to mitigate Mr. Fastow's conflict of interest. Yet, it is my understanding that the Compensation Committee did not at that time follow through on that recommendation. Can you explain why?

Dr. LEMAISTRE. Yes. The Compensation Committee was aware that there had been controls put in place for Mr. Fastow to report his compensation. They were aware of the fact that his approved compensation on both LJM1 and LJM2 was to be modest.

Second, we knew there were reports coming on an annual basis and on a quarterly basis and we expected information to come through these reports and that management, as they should have done, bring that to the Compensation Committee. I inquired on two occasions of our staff, after the first quarterly report subsequent to that, whether we received any information on a 16(b) officer outside compensation. The answer was no. The second time I inquired was a few months later, in August or September, I believe, and we still had not received the information. With all of the events that transpired, the next trigger became, of course, the October 17 or 19 revelation that he was alleged to have made $7 million.

Senator COLLINS. That was the story in the *Wall Street Journal.*

Dr. LEMAISTRE. Yes Ma'am, that is correct.

Senator COLLINS. So it took a story in the *Wall Street Journal* to prompt your going back. You had asked twice, had not gotten the information. But it was only when the *Wall Street Journal* learned that there was an important issue here and actually gravely understated the amount of money that Mr. Fastow was making that you pursued this?

Dr. LEMAISTRE. That is correct.

Senator COLLINS. Thank you, Mr. Chairman.

Senator LEVIN. Senator Lieberman.

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

Yesterday, attorneys for Enron provided several documents to the Federal Energy Regulatory Commission which related to what I would consider to be highly questionable trading strategies used by Enron in the California and Western electricity markets in the year 2000 energy crisis, and apparently continuing into 2001. These documents, which, as I am sure you know, have now been made public by FERC and which I had a chance to look over this morning were prepared for Richard Sanders, a senior official of Enron, by attorneys from both inside and outside the company, apparently in anticipation of possible regulatory sanctions, investigations, and litigation arising out of the crisis, or perhaps, I suppose, just as notification to the traders.

They are very interesting documents because they describe a range of different strategies with very colorful names, such as Death Star, Get Shorty, Wheel Out, Fat Boy, Ricochet, and others by which Enron's traders maximized profits while gaming the system and taking advantage of the energy crisis in California.

One memo which I have looked at, dated December 8, 2000, specifically discusses the California market regulations against gaming and other predatory market behavior after it describes the strategies that the Enron traders were following, and in my opinion, may have been violating, although the memo is, in that sense, as I read it, you might say value neutral. It does not make a recommendation. It describes the strategies and then the sanctions that can be applied by the California—against Enron should the activities be discovered, and that is a direct quote, "should it discover such activities, a California system operator could take these actions against Enron."

So I want to ask a series of questions about that. First, was the Enron Board of Directors aware of the trading practices and strategies used by Enron's traders in the California and Western markets? Mr. Duncan or Mr. Blake?

Mr. BLAKE. No, sir. We were not aware of those specific strategies, and if I may add, the first time I was aware of those strategies was when Pug Winokur and I, who are on the Restructuring Committee of the Board, were given those documents 2 weeks ago to this day and I subsequently, as Acting Interim Chairman, set up a Board meeting for that following Thursday, at which time we discussed it with the Board. I think, in fairness, the predisposition was to make this disclosure as responsibly and as quickly as possible. We instructed our counsel to investigate further because Rob Walls, who Mr. Walls is the now-current General Counsel, but was not there before, just came upon these memos.

Subsequently, the following week, last week, there was further discussion of this report by counsel, actually last Sunday morning, by counsel and the management and we, as a Board, moved to direct specifically the release of that information yesterday.

Senator LIEBERMAN. I appreciate the speed with which you did move. What was your reaction when you saw the documents 2 weeks ago?

Mr. BLAKE. I was extremely upset and disappointed.

Senator LIEBERMAN. Did you read them as I did, that they seemed to be both descriptions of strategies that were questionable and then an indication of what the penalties were, but almost a directive about how to avoid the law instead of how to comply with it? Am I overreaching, or was that part of your reaction?

Mr. BLAKE. Well, in candor, my reaction was very much similar to yours. It certainly appeared on its face, although it was sort of a description of the practices, but from what I could discern, certainly questionable practices, seemingly gaming the system—I think those are the exact words I used at the Board meeting—very offensive to me personally and members of the Board.

Senator LIEBERMAN. I appreciate that answer.

Dr. Winokur, perhaps as Chairman of the Finance Committee it is appropriate to ask you that question, also.

Mr. WINOKUR. Sir, in terms of the recent 2 weeks, I was exactly where Mr. Blake was. There were five meetings from October 2000 to August 2001 in which there were reports to the Board of Directors by management about California, and we asked questions, including are we doing anything wrong? There is a lot of bad press. Are we doing everything that we are supposed to do to comply? We had reports from our General Counsel on litigation. We had reports from our Chief Regulatory Executive. We had reports from the senior people. And at no time ever were we given any information or hint of information that we might be out of compliance with the trading rules.

Senator LIEBERMAN. So that, again, as far as any of you know, and particularly the two of you, the Enron Board was not aware of these memos until 2 weeks ago, and, therefore, aware of any of the legal and financial liabilities that might be incurred by the trading strategies, is that correct?

Mr. WINOKUR. Yes, sir, we were not aware.

Senator LIEBERMAN. Right. Let me ask this question about this matter, and this is as we try to work our way through what is the appropriate and required role for boards of directors. I mean, ideally—well, I suppose the first question has an answer to itself, which you have already given. You actually asked questions. I mean, there was a lot of public commentary when this was going on, particularly from people in California and our colleagues who represent California here in the Senate or the House that Enron was profiteering, whatever the word was. So you asked questions, then, of the employees and really got what you now know are inadequate answers?

Mr. WINOKUR. Yes, sir. I lived in Los Angeles for 7 years and was on the board of UCLA Hospital, so I have a lot of friends there. I responded to the press statements and said, are we asked questions, are we doing anything wrong? Is there anything we should be talking about here? We had reports in these five meetings from our General Counsel, our Chief Regulatory Officer, and the senior executives, not everybody at every meeting, but in those series of meetings, all those people reported, and not once did we hear anything that suggested any impropriety in California.

Senator LIEBERMAN. Let me ask it in a different way, a different kind of question, which is, both stepping back and looking back—and here it sounds to me like you had public notice—you asked the question, you dispatched your responsibility.

More generally speaking, what can we expect of directors in terms of their oversight of activities such as trading practices of a corporation? Let us say it would not have fit the public interest because there was not that much interest in the California price spikes during that time period, so how would you set a standard for what directors should expect to know?

Mr. WINOKUR. Sir, I am not sure I was qualified, but it seems to me that if we ask the senior people responsible for that line of business and we ask separately the General Counsel to give us reports on what is going on, and we, third, set up a risk system to measure quantitatively how the trading system has worked, I am not sure I have any other suggestions. I am sorry.

Senator LIEBERMAN. Anyone else? Mr. Jaedicke.

Mr. JAEDICKE. It is a very thoughtful question. As far as the trading is concerned, we, of course, paid an awful lot of attention to the financial measures to say, do not take too much risk. Do not have too many open positions. We had an elaborate policy on that.

Now, one part of that policy was that we were in the process of developing even more, was something called operational risk, and operational risk, we did not have it fully developed in terms of what all it meant, but surely, whatever it meant, it meant that you would try to put in control systems that would assure you that you were complying with the law. Our other compliance systems involving the internal and external legal people, you would expect that to be part of the systems and to be reported if they were not followed.

Senator LIEBERMAN. Let me move on to one additional area of questioning. I thank you for that answer. As I am sure you know, there has been a lot of concern among the employees, former employees, particularly, of Enron, and, of course, that concern has been expressed over the months since early December by members of Congress about the inequity, perceived inequity of the bonuses given to various higher-level employees of Enron at the same time the 4,000 or 5,000 employees who were laid off were given severance payments that were greatly below what they expected.

In the case of some of the bonuses, I gather that to get and keep the money, they had to agree to stay for 90 days. Some of the bonuses exceeded $1 million. One was even $5 million. That is contrasted with the employees, who, by my recollection, received an average of about $4,500 each, which, as I said, was a fraction of what they had expected in the way of severance.

According to Mary Joyce, who I know you know is a VP of Compensation at Enron, the issue of severance was discussed at a meeting of the Compensation Committee of the Board just before bankruptcy, but she has said to us that she did not remember the substance of the discussion. Dr. LeMaistre, you are the Chairman of the Compensation Committee. I believe, if my records are right, that Mr. Duncan, Mr. Jaedicke, and Mr. Blake are members of the Committee.

So my question, obviously, is can you remember and describe for us what was discussed at that meeting about the severance payments, and particularly, did anyone ask if it was possible to compensate these people more fairly for the employees, that is, the lower-level employees, for their service to the company?

Dr. LEMAISTRE. Senator Lieberman, I recall that very clearly and I would ask my colleagues to comment on it, to add additional things. It is a very important question.

The severance plan presented by management to us required several different areas of interrogation by us of management, and the plan actually was moot because we went into bankruptcy before it was acted upon, if we are talking about the same severance plan, and I assume we are.

The W.A.R.N. (Workers' Adjustment and Retraining Notification Act) provisions can be exempted in bankruptcy and all that is allowed to be paid, if the bankruptcy court agrees, is the $4,500 per employee. So I think that explains the problem.

Yes, we did discuss this. The Board of Directors met on December 2, which I think is the day we went into bankruptcy. The Directors agreed to work without compensation and expressed the desire that our fees go to the employees or to an employees' fund. Later, we were told it was too complicated to work that out.

We discussed this because we were very much concerned about what was happening to the employees. I would remind you, one of the prime reasons everyone should be concerned about that is as far as I know now, a very small number of employees created a major part of the internal problems at Enron and there were more than 20,000 very honest people there——

Senator LIEBERMAN. Correct.

Dr. LEMAISTRE [continuing]. And those are the ones that suffered.

Senator LIEBERMAN. Who suffered? So am I hearing you correctly, that you would have wanted to give the 4,000 or 5,000 employees something closer to the severance payments they thought they were entitled to under their agreements, but you could not do it according to bankruptcy law?

Dr. LEMAISTRE. Well, we were—if I recall correctly, and I would ask the members of the committee to comment, the first discussion was on a Saturday, December 1, and I think the next day, Sunday, December 2, we were ready to propose this. Unfortunately, Enron had filed for bankruptcy at 2 a.m. in the morning on Sunday, and so we were governed by bankruptcy law.

But to answer the other part of your question, the high bonuses that you——

Senator LIEBERMAN. Right.

Dr. LEMAISTRE [continuing]. Alleged to be high. Those were for traders. We felt that the traders were the group that was essential to hold the company together. In the weeks approaching bankruptcy, we were trying desperately to hold on to them. We were trying to merge with Dynegy, and the traders were of primary interest to Dynegy. That was really the group they wanted.

Second, we knew that they were being sought by many other companies because of Enron's public problems, and, therefore, we were trying to give them a 90-day stay bonus——

Senator LIEBERMAN. I see.

Dr. LEMAISTRE [continuing]. Which had a draw-back on it. They had to repay if they did not.

Senator LIEBERMAN. If they——

Dr. LEMAISTRE. If they did not stay.

Senator LIEBERMAN. For the 90 days?

Dr. LEMAISTRE. Yes, that is correct.

Senator LIEBERMAN. So that explains my other concern, which was why you would give such large bonuses for people who are only staying 90 days, and you are saying you were doing it because they were traders and you wanted them for that period of time.

The light is up, so I am going to close in a minute on my time. Do I take it that bankruptcy law did not similarly prohibit the company from paying the large bonuses——

Dr. LEMAISTRE. That occurred before we were under bankruptcy.

Senator LIEBERMAN. You made the decision before?

Dr. LEMAISTRE. Timing, yes.

Senator LIEBERMAN. OK. My time is up. Thank you.

Senator LEVIN. Senator Fitzgerald.

Senator FITZGERALD. Thank you, Mr. Chairman. This is my first meeting at the Governmental Affairs Committee and this Subcommittee. I just joined the Committee, and I appreciate you having me on. I think I get assigned to all the committees investigating Enron.

Senator LEVIN. The Chairman, I think, wants the honor of welcoming you——

Senator LIEBERMAN. Yes.

Senator LEVIN [continuing]. But we welcome you to the Subcommittee today, and the Chairman can do that appropriately.

Senator LIEBERMAN. Thank you, Senator. Senator Fitzgerald, we welcome you here. This is a very interesting Subcommittee with very significant oversight responsibility and we are delighted to have you and I am sure you will contribute substantially to our work.

OPENING STATEMENT OF SENATOR FITZGERALD

Senator FITZGERALD. I am pleased to be aboard, and all of you, thank you. Some of you, I have met you in the Commerce Committee, which has also had several hearings on Enron.

Some of you may know my theory on Enron. I was the one who described Enron as a gigantic pyramid scheme or Ponzi operation, and if I could just explain why I say that. Mr. Blake made mention earlier of the SPEs being used to improve liquidity and get debt off the balance sheet. After going through several of those SPE transactions and all the 41 boxes that were delivered to the Commerce

Committee, I concluded that what Enron was doing was creating off-the-books partnerships, instructing those off-the-books partnerships to borrow money, in essence, and then Enron would transfer assets to the off-the-books partnerships. The partnerships would borrow money, while Enron had typically guaranteed their borrowings, and then the SPEs or the partnerships would pay Enron for some asset that Enron had transferred to the SPE.

But Enron had always provided a credit support in all the cases I looked at for the borrowings of the SPE, and if you really reduce this to simple terms, Enron was simply borrowing money, filtering the borrowings through the off-the-books partnerships, and then booking that borrowed money as income, and that is how you built up some $20 billion worth of off-the-books indebtedness. But Enron was contingently liable for that indebtedness, and when you filed for bankruptcy in December, it was because you had a very familiar problem. You had too much debt. You had several billion dollars worth of indebtedness coming due and Enron could not pay it.

Now, I think these specific transactions were very well disguised. I think that the management obfuscated enough, used high-falluting sounding language to describe all these transactions to make them sound legitimate. I think it would be very difficult, you would really have to be on your guard to figure out what they were up to.

But I have also felt that in the hands of management was plenty incentive to engage in this kind of pyramid scheme, to keep booking fictitious earnings, and that incentive was to keep the stock price up, and they wanted to do that because many of them had millions or tens of millions, and in some cases hundreds of millions of dollars worth of stock options in their hands.

Now, many of the senior managers cashed in their stock options and got out of the company before it all spun out of control. There are many people who got out of the company, having successfully cashed in millions of dollars worth of stock options. I think Mr. Baxter, who committed suicide, got out a long time ago. Others, the Army Secretary, got out quite some time ago.

Mr. Skilling tried to get out last summer. He succeeded in cashing in, I think, $78 million worth of his options, of 1.7 million options in 2000 and 2001. He got out. I have heard reports that Mr. Lay had lined up a job at another company and was planning to get out. He cashed in in the last 2 years $82 million worth of options. In all, the top 29 executives at Enron cashed in some $1 billion worth of options in the last 3 years, according to reports that I have read.

I have several questions for you. I notice that the compensation of the Board, total compensation in fiscal year 2000 for each Board member was roughly an average compensation of $329,000 per Board member. Some got less, some got more, depending on what committees they chaired, what committee meetings they attended. Only a small portion of that compensation was cash compensation. The average Board member got $78,000 in cash compensation, but the average Board member got $250,000 in stock options.

The question I have to ask to you is, your interests were to see that the stock price kept going up, given that your compensation was so heavily weighted towards options. Did you all not have a financial interest in seeing those options go up and always be in the money? I understand you could exercise them—they did not expire for 10 years, and so you did not have pressure to cash them in right away.

But do you care to comment on that issue? I mean, were your interests really aligned with the interests of the long-term shareholders? How many shares did each of you own outright in Enron, excluding options? How many shares? Mr. Blake.

Mr. BLAKE. I cannot quite remember, sir. I bought some initial shares of both Enron and Enron Oil and Gas and EOTT and Northern Border Partners when I first joined in 1993 as a statement of interest in the company, and——

Senator FITZGERALD. How much do you think you had——

Mr. BLAKE. I might guess——

Senator FITZGERALD. What was your cost basis?

Mr. BLAKE. Maybe about 3,000 shares, something of that nature.

Senator FITZGERALD. And would that be, like, $30,000, or——

Mr. BLAKE. Yes. Well, I also made a purchase in October 2001 that was $80,000, so I would say probably something in excess of $100,000.[1]

Senator FITZGERALD. Dr. LeMaistre.

Dr. LEMAISTRE. I had—I lost approximately $3.5 million in shares of the restricted stock, which is a gift, of course, and in the stock options, I cannot give you the exact total, but I would say something in the order of maybe 40,000, 50,000 of beneficially owned stock——

Senator FITZGERALD. Forty or 50,000 shares?

Dr. LEMAISTRE. Yes, something like that.

Senator FITZGERALD. That you had bought outright, or had——

Dr. LEMAISTRE. Had bought outright, maybe more than that. I cannot remember the exact figure——

Senator FITZGERALD. And that you owned in your own account?

Dr. LEMAISTRE. That is right, and——

Senator FITZGERALD. What would your cost basis have been in that, roughly?

Dr. LEMAISTRE. Well, they were bought all the way back to 1991, so I would have to recalculate that to tell you that. I would assume—I really could not answer it accurately without looking at notes. I would be happy to do that.

Senator FITZGERALD. A hundred-thousand dollars, maybe?

Dr. LEMAISTRE. Probably.[1]

Senator FITZGERALD. About $100,000.

Dr. LEMAISTRE. A little more than that, I think, but——

Senator FITZGERALD. A little more than that?

Dr. LEMAISTRE. Yes.

Senator FITZGERALD. Mr. Jaedicke.

Mr. JAEDICKE. I could give you the information. I would be glad to send the exact information. My recollection is it would be slightly over 20,000 shares, many of which were taken as part of Board compensation.

Senator FITZGERALD. But what would your cost basis for what you had——

[1] See Exhibit No. 80 which appears in the Appendix on page 665.

Mr. JAEDICKE. Well, the cost basis of the shares taken for Board compensation would be that I was paid ordinary income at the time I got them. So, I do not know, I suppose it would be between $20 and $30 or $40 a share. I do not know what the average would be. Again, I can supply that to you.[1]

Senator FITZGERALD. I would be very interested in that. Dr. Winokur.

Mr. WINOKUR. Yes, sir. I own approximately 80,000 shares. I have a cost base of about $1.8 million or $1.9 million. Some of those were shares I bought. Some of those were shares from options that I exercised and did not sell. I have never sold a share of stock.[1]

Senator FITZGERALD. So you had some skin in the game, as SherronWatkins would say?

Mr. WINOKUR. Yes, sir.

Senator FITZGERALD. Mr. Duncan.

Mr. DUNCAN. I now own 167,000 shares. I have owned those shares from the beginning. I cannot now recall my cost basis. I do recall that the options that I exercised only last year, and held, I did pay ordinary income tax on them, so that changes the arithmetic a little. But broad general statement, I lost over $10 million.

Senator FITZGERALD. How much money do you think you had invested, though, your total cost basis——

Mr. DUNCAN. Well, if you go back——

Senator FITZGERALD. Now, did you acquire those shares from prior companies that Enron merged with?

Mr. DUNCAN. No. When Enron sold for cash—excuse me. When Houston Natural Gas sold for cash to InterNorth, then I took my proceeds and invested the proceeds in Enron.

Senator FITZGERALD. OK.

Mr. DUNCAN. At that particular time, if my memory serves me, it was about $1.5 million.[1]

Senator FITZGERALD. So some of you did have substantial investments in the company, and I would think your personal financial interests were, for some of you, very closely aligned with those of ordinary shareholders.

Did any of you think about what kind of temptations, though, could be in the hands of senior managers when they stood to make the kind of sums Mr. Skilling and Mr. Lay did by cashing in their options, because cannot any company fictitiously goose-up its earnings per share to keep its stock price high, for a while, at least, until other people catch on? When there is so much in options outstanding in the hands of senior management, does that not begin to worry some of you as Directors that, ultimately, their interests could no longer be allied with the interests of the long-term shareholders? They could just try to goose the stock price, cash in their shares, and get out of the company? Would any of you care to comment?

Dr. LEMAISTRE. Let me make a comment, Senator Fitzgerald, that first, the policy of awarding stock was to ensure that they kept their eye on the ball and saw that the stock price increased for the shareholders' benefit, because that is really what the shareholder

[1] See Exhibit No. 80 which appears in the Appendix on page 665.

does, he invests in a company and wants that stock to increase. So that over the period of time, to have the stock increase, the employees win, but also the shareholders win. So I think that it is a two-edged sword. If one gets the incentive so high that is all that people are really working for in order to cash out——

Senator FITZGERALD. As Chairman of the Compensation Committee, did you ever worry that maybe the incentives were so high, there were so many options outstanding, that, boy, maybe we have a problem here, because some people play a game here?

Dr. LEMAISTRE. I did not worry about it, primarily because I talked to our Towers Perrin consultant every year about whether our scale of pay, our programs, including the incentive pay that we had, especially the incentive pay, was commensurate with exactly what was being done by companies our size. We had our last report as of the spring of 2001 that said we were right on target with where we were supposed to be.

Senator FITZGERALD. Can you think of any other motivation that management would have had to engage in such aggressive accounting and gimmicks to keep the earnings up, other than to keep the share price up to keep their options in the money, because they were getting very rich very quickly on this scheme while everybody else was—all your other rank-and-file employees were wiped out, pension funds were wiped out, and $60 or $70 billion in market capitalization was lost, but a lot of your inside management got very rich and came out very well on the whole thing. Can any of you think of any other motive that management would have had for deceiving the Board and deceiving the public?

Dr. LEMAISTRE. Senator, I do not want to monopolize the time, the other Subcommittee Members may want to speak to this, but I will say that we thought the integrity and honesty of our employees, especially those in key positions, was intact, and that was the most important thing. We had quarterly reviews of all of the higher-level echelon officers by Mr. Lay directly to the Compensation Committee and then a very large review annually in our management development responsibility. So we thought we knew these individuals well. I have no answer for your question except that the problem was, in my opinion, dishonesty and lack of integrity.

Senator FITZGERALD. Mr. Chairman, I appreciate the Subcommittee's time, and all of you, thank you for being here today.

Senator LEVIN. Thank you, Senator Fitzgerald, and again, it is great having you with us. Senator Carper.

OPENING STATEMENT OF SENATOR CARPER

Senator CARPER. Thanks, Mr. Chairman, and to each of you, welcome and we appreciate your time and your testimony today and your responses to our questions.

Before I was elected as Senator about 2 years ago, I served as Governor of Delaware for 8 years. One of the things I learned as Governor was that when things went well, I was wise to share the credit. When things went badly, I was wise to assume the blame. One of my frustrations in listening to the testimony here this morning, and frankly, listening to the comments of those who served in very senior positions at Enron, relatively few people seem willing to accept the blame.

I, for much of my life, served in the Navy as a Naval flight officer, about 23 years, in fact, on active and reserve duty. In the Navy, we have a tradition, and a proud tradition, that the captain of the ship assumes the responsibility when things go badly, or the commanding officer of the squadron that I served in assumed responsibility, was held accountable and responsible when things went badly.

Obviously, from your testimony today, you believe that you were deceived and misled. Who bears the responsibility? If not the Board, if not the Audit Committee, if not those with whom you served, if not the Chairman, who does deserve the blame? Who should step forward and say, this is my fault?

Mr. JAEDICKE. Are you directing that at me?

Senator CARPER. From any of you, please.

Mr. BLAKE. Well, I will speak for all the Board and say that we feel terrible, what has happened here, and we have scrutinized our own behavior and we have asked the question numerous times, what could we have done differently? I am absolutely convinced, sincerely, honestly convinced that the controls, had they worked, this would not have happened, and I feel absolutely misled in light, too, with that question.

I do not know where the fault lies. I mean, I accept the same philosophy as you do, and as the CEO of many companies, it is my ship and I am totally responsible for its conduct and the companies that I run. I absolutely philosophically totally agree with you, without exception. I do not know where the fault lies here. I do not know enough of the information. I do not want to get into personalities today, but——

Senator CARPER. If you do not, and those of you with whom you serve—excuse me for interrupting, but if you do not know where the fault lies, how are we going to figure that out?

Mr. BLAKE. We do not know the facts, sir. I do not know what Ken Lay knew or did not know. I would love to know. I would like to know what Jeff Skilling knew and what he did not know, because I look to them as leaders of the company, responsible to the Board in the exercise of their particular responsibility as the chief executives of the company and responsible for the ship. I want the answer, too. I do not have an answer. If I had the facts, I would give it to you, honest.

Mr. WINOKUR. Senator, I served on the Powers Committee, the special investigative committee, and as that report indicates, there is considerable ambiguity in exactly who knew what, when, and how, because our committee was not able, as government agencies can, to subpoena people, to force them to talk, and so on. So I think all of the interviews have been provided to you and there are numerous investigations underway by people who have the ability and the authority to find out answers to those questions.

But I concur with what Norm said. I think we reacted as best we could to the information we had. We relied on the candor of management. We relied on our advisors to do their job, which was to confirm what we were being told, and there is a lot left to be learned, unfortunately, as the Powers Committee report indicates.

Senator CARPER. Anyone else?

Mr. JAEDICKE. I agree with the two statements that have been made. I guess all I would say to elaborate on that, or to maybe bring up another point, is to say—and I guess I am speaking from the viewpoint of an Audit Committee, although I think it would be the same for a Board, as well, is that there is this classic problem that the information that the Board needs to do the oversight, not entirely, but largely comes from management. And so the people you are supposed to be overseeing do control a great deal of the information.

Now, how do you deal with that? Well, you try to put controls in place. You also hire an external auditor. We had within Enron an organization that I thought supported that, those kinds of checks and balances, because, for example, we had a separate financial officer, a separate accounting officer, and a separate risk control officer, a separate legal officer. None of those were combined and all of them reported in at the same level.

Dr. LeMaistre makes a very good point, also, with this whole thing, you hire one of the best accounting firms in the business, or at least that was their reputation. The same with legal. You try to assess management, and we had no reason to distrust management or our outside advisors. Where you feel let down is when you do not get the information that you need to act, and I do not know how you can act if you do not have that information.

Senator CARPER. What punishment is appropriate for those who have led to this debacle? And again, this is for any of you.

Mr. WINOKUR. Senator, I will just speak for myself. I am not a lawyer, and I am certainly not a criminal lawyer, I am not a civil lawyer. I do not have any idea what is appropriate. I hope the investigation pursues everything it can to find out everything it can because I think all of us, you, the Directors, the employees, deserve to know who knew what, when, how, and why. But I could not comment on the——

Senator CARPER. Anyone else?

Mr. DUNCAN. Only that we share your frustration.

Senator CARPER. I serve on three committees that have conducted parts of the hearings into Enron and we will presumably be developing a legislative package to address a number of the suggestions that we have heard throughout the course of the last several months. They include the roles of the auditing firms, the independent audit, whether they should rotate firms, whether we should rotate lead auditors, issues involving independence of the board, how many independent directors should there be, what constitutes a breach of independence, issues involving 401(k)'s, how long people should have to hold their company stock in order to vest.

Some of the people who have testified to us have said, you should legislate little. You should let the market force the corrections and punish those who make the reforms, adopt the reforms, and that is the better approach. We have heard from people who say the SEC should do certain things, that the board exchange, the New York Stock Exchange and others, should push various reforms.

In the end, what should the Congress do? What should we do in some of the areas that I have mentioned or others that I have not touched on? What should we do as legislators?

Dr. LEMAISTRE. Senator, I would like just to agree with you. I think there is much the Congress can do once the facts are known. I think the only thing the Congress can do now, though, is to await the final understanding of exactly how this happened, how Enron was brought down and by whom, and where controls need to be placed, not by the Board but by either law or by the voluntary organizations, and businesses that do this, such as the auditors.

But there is going to be a role for legislation. It may be a midpoint between those that said, leave it alone and let it happen, and those of us who are a little bit emotional about getting everything done right now. I think the best thing to do is to let the process of justice go through here where we will find out everything, and I am looking forward to that understanding, because I could answer your question better then.

I will say this to you. A Board like this one that has been through what we have been through would be willing to help you in any way we can and tell you where we think, in some more detail than we can do today, what really happened and why we were let down. I think we do not know enough today to tell you more about what is the real problem.

Mr. BLAKE. Senator, if I could add one thing, I want to go back to the point you made. It gets down to the leadership. You cannot legislate leadership. It gets down to what the role of a leader of an organization is, the culture of the organization he is responsible for, the discipline and the incentives put in place to encourage character, honesty and integrity as an offset to greed or whatever may be the other compelling factor in someone's mind.

I have been associated with some very successful companies as an employee and as a leader of that company, and stressing values above performance, values above compensation, a sense of integrity and sense of purpose about the company, is what it is all about. There has to be a higher purpose for that company ultimately to be successful. It should not be motivated by short-term windfalls of stock prices. It should be motivated by the vision of the company. It should become sort of imbibed in the person. You know what I am talking about. That is what real leadership is about.

So I have to say my honest answer to your question, it starts with leadership. Forget about anything else. It starts with leadership, and if it is not there, then the company will fail.

Senator CARPER. Well, there are certain things we can do. We are not very good at legislating integrity or character, but that is obviously what is needed to best ensure that these kinds of things do not happen again.

Anybody else in terms of—I know my time is expiring.

Mr. DUNCAN. Senator, I would agree that it would be very difficult to legislate integrity. It would be very difficult to write the law on leadership and character. But there are some issues, in my opinion, that your Subcommittee and this Congress and this Senate should consider, and one of them is that stock option problem of how it is accounted for.

And one of the problems that really is a catch-22, if the Dow had not moved from 3,000 to 10,000 while these employees had their options, their 7- and 10-year options, then they would not be so rewarded. But when the whole market moves up and they want to go to work for options and the overhang of the stock is one of the things that we kept worrying about. We worried that we wanted to compare ourselves with other companies on the overhang, i.e., the amount of options that were out in relation to the total number of shares of stock, and was that in the ballpark, and if it was in the ballpark and if we thought we were hiring and were hiring the youngest, the brightest leaders, then they wanted options and we would issue options.

But once issued, if they were 10-year options and the whole market triples, then you have a catch-22 there, which is an incentive to get out, and I do not know the answer to that. If we would have issued these options in 1970, at the end of the 10-year period, they would not have any profit because the market did not move. And so I do not know how you put that into legislation.

I will say that one of the reasons, in my opinion, that the American system has worked so well for the majority of the leaders is because they had options and they led the company with leadership and integrity and they made themselves and their families some money. So if that had to have been removed from the system entirely, I do not think the American economy would be doing as well as it is today.

Senator CARPER. Thank you for those comments, and Mr. Chairman, thank you for allowing me the time.

Senator LEVIN. Thank you, Senator Carper. Senator Durbin.

Senator DURBIN. Thank you, Mr. Chairman. Let me say at the outset that I am personally familiar with one of the members of the panel. Dr. LeMaistre and I became acquainted almost 20 years ago. Dr. LeMaistre, you are one of my heroes——

Dr. LEMAISTRE. Thank you, sir.

Senator DURBIN [continuing]. What you have done in the field of public health has saved countless lives, not just in Texas, but in our Nation and around the world——

Dr. LEMAISTRE. Thank you, Senator.

Senator DURBIN [continuing]. And I am truly sorry that you are in this predicament now and wearing a different hat, but I wanted to start off by saying my admiration for you has not been diminished in any way whatsoever by this.

But I want to raise this question. Let me concede at the outset I am a liberal arts lawyer. I am not a business major, so I struggle to understand a lot of the things that you talk about, which are common parlance for people who are involved in business. But occasionally, I rely on folks that I think really get to the core of the issue for me, and the person that I turn to once a year and make sure I never miss his views on life is a fellow by the name of Warren Buffet, who puts out the Berkshire Hathaway Annual Report. It should be "must" reading for everyone in Congress, if not everyone in business, because I think Warren Buffet has proven that you can do things differently and still be very successful.

Here is what he said in his most recent report to the shareholders of Berkshire Hathaway. He said, "Though our corporate performance last year was satisfactory, my performance was anything but. I manage most of Berkshire's equity portfolio and my results were poor, just as they have been for several years."

He goes on to say, “One of my ground rules is applicable. I cannot promise results to partners. But Charlie Munger,” who is his vice chairman, “and I can promise that your economic result from Berkshire will parallel ours during the period of your ownership. We will not take cash compensation, restricted stock, or option grants that would make our results superior to yours. Additionally, I will keep well over 99 percent of my net worth in Berkshire. My wife and I have never sold a share, nor do we intend to.”

“Charlie and I are disgusted by the situation so common in the last few years in which shareholders have suffered billions in losses while the CEOs, promoters, and other highers-up who fathered these disasters have walked away with extraordinary wealth. Indeed, many of these people were urging investors to buy shares while concurrently dumping their own, sometimes using methods that hid their actions. To their shame, these business leaders view shareholders as patsies, not partners. Though Enron has become the symbol for shareholder abuse, there is no shortage of egregious conduct elsewhere in corporate America.”

My question to you, because some of you—Mr. Duncan, you talked about your business experience and your success—and others, as well, have dedicated your lives to American business. You have taken risks. Some have succeeded and some have failed. For your successes, you have been rewarded, and that is the nature of capitalism and free enterprise, as it should be.

But reflect for a moment on what it says to America that we can step back and look at this viper’s tangle of Enron and judge that Mr. Lay was worth over $140 million a year to create this fraud on the American public, or that Mr. Fastow was discovered to be making an additional $15 million which had not quite come to light. Think about what this says to the rest of America that wants to believe this is on the square. I do not think it meets the standard and test which Warren Buffet is talking about here.

I think Enron, as I said at the outset, has shaken us to the core. I do not think any Americans are opposed to success. That is what America is all about. That is the American dream. But this is not success, this is fraudulent conduct that has resulted in unjust rewards.

I would like to ask you, Dr. LeMaistre, you deal in your hospital situations with some of the most gifted men and women in the world, skilled people who give more of their lives than any of us even in Congress and receive a tiny fraction of what some of these corporate officers were receiving. Help me put this in perspective. Help me understand why we should use as a standard who is making the most in business to decide who is worth an extra dollar.

Dr. LEMAISTRE. Senator, your quote and your question come right to the point. I think that it is difficult for someone who has come from a purely academic background to speak to this because M.D. Anderson is an academic institution and we do not use the same pay methods that we are talking about.

The real problem, it seems to me, is that we need more disclosure from the leadership of business as to what the principles are on which they are operating their companies. We had an inquiry earlier about what went on in California, for example. This Board was never told of any illicit practices that were going on in California. I think that the leadership should be required to tell a board and the shareholders what their practices are going to be. We know in medicine exactly what they are going to be and we have a high standard, and if it is not met, then there is a remedial action taken.

As a consequence, I would like to see the same stringent approach to the responsibility for leadership, including boards, and all of business, because I think we can find ways. I think it is going to require, though, as I said before you came back in, that we really understand thoroughly what happened at Enron. I think the Powers Report is a first, and a very quick look at that, and until we get testimony under oath, I do not think we are going to fully know exactly why charges like gaming are being made in this thing.

Senator DURBIN. Let me use another illustration and then ask the other panelists to comment, as well. About a month ago, the *New York Times* in the business section published the salaries of the top 100 executives in the United States and they compared what they were making to the performance of their corporations. Now, you have heard this story repeatedly, how boards of directors have repeatedly given bonuses and extra payment while the company is going into the dirt.

If you are standing on the outside looking in from the viewpoint of an average citizen or a worker or an investor or someone whose pension is on the line, you have got to say this is an upside down world. There must be such a closed culture within American corporations that they believe they are royalty, that they can treat one another with royal conduct even if they have not performed accordingly. When I look at some of these salaries that are being paid here, this goes way beyond incentive compensation.

Mr. Duncan, you started long ago. Your opening testimony talked about your distinguished career in business. You have seen some dramatic changes in executive compensation, have you not?

Mr. DUNCAN. I certainly have.

Senator DURBIN. Are they fair?

Mr. DUNCAN. What a comp committee has to do in today's world is try to determine whether that executive is the best and then determine what he can get if he walks across the street.

When I was President of Gulf and Western, there were two guys working there, Michael Eisner and Barry Diller. They made a lot more than I did. Why? Because they could walk across the street and get more money, and representing the shareholders, we did not want them to walk across the street.

So one of the catch-22s that you face is that you have to pay the going rate. Now, the second part of your question, is the going rate ludicrous? Yes. But when you have a large corporation and you have 20,000 employees and you want the corporation to succeed, then you cannot ignore what the going rate is, whether you think it is right or wrong.

And incidentally, I like Warren Buffet's approach. He is my hero, too. But he can talk with luxury because he is the second richest man in the United States. So he can enjoy saying, "I am not taking a dollar." But the young guy who is fresh out of MBA school, who has kids that are growing up and knows what he can get if he walks down the street, you cannot ignore that, either, and it is a tough problem, and it is helped by the fact that the Dow keeps moving and stock options are in the mix. It is really helped by that fact, because everybody starts reading what the other guy is making.

Senator DURBIN. I could defer to our Chairman on the stock option question. We are both cosponsors of legislation which he has introduced on this issue.

But Dr. Winokur, would you comment on this executive compensation? What is, I think, brewing in this land is a feeling of disgust about how much people are being paid and how the chasm between the average person who gives his life to Enron, puts his entire pension and future in that Enron 401(k) and sees it disappear while others are skating away with second and third multi-million-dollar homes, there is a basic injustice here. There is a feeling of privilege which is not part of the American experience. Could you comment on that, as well?

Mr. WINOKUR. Yes, sir. I manage a private investment partnership with a number of financial institutions involved and the way our partners get paid is after our limited partners have been paid all their money, and a return on their money, and all that cash has been sent out, then we split what is left if any is left. So I am the last guy in the food chain, so I am very sympathetic to both you and Warren Buffet and Charlie Munger's point.

I would just make one suggestion of an item to consider as the Chair and you consider the stock option matter. It has seemed odd to me in the companies in which we invest that if we issue stock, restricted stock, to the employees, there is a charge to earnings. If we issue stock options, there is not a charge to earnings, a point you obviously know well. But if we issue options but the options vest only on achievement of performance criteria, there is a charge.

Now, it would seem to me it would go the other way around, that is, that you would want to give people incentives not to receive compensation unless they have actually performed, as opposed to, as my colleague, Mr. Duncan, said, have a ride on the market. I do not know if that is helpful, but it is something that has occurred to me.

Senator DURBIN. Well, I stopped short of reading the next sentence in Warren Buffet's report, but I am going to read it now since it is an open invitation. He says in his annual report, "One story I have heard illustrates the all-too-common attitude of managers toward owners. A gorgeous woman slinks up to a CEO at a party and purrs, 'I will do anything, anything you want. Just tell me what you would like.' With no hesitation, he replies, 'Reprice my options.'" [Laughter.]

A lot of us believe that this option business has gotten completely out of hand, not just for tax purposes but as incentives for compensation. I thank you for your testimony today, and Mr. Chairman, thank you for this hearing.

Senator LEVIN. Thank you, Senator Durbin.

We are going to proceed for perhaps 45 minutes to an hour here and then break, perhaps completing this panel, but perhaps not.

I am absolutely amazed at your denial of any responsibility for what happened at Enron. From the outside, Enron appears as a case where insiders made fortunes, much of it based on stock options, jacking up share prices, while the shareholders were left holding an empty bag. That is from the outside. From the inside, I think there is responsibility just from what we are going to go into right now and what we have gone into. What the Board knew should have triggered on the part of the Board a heck of a lot greater vigilance than it did.

In the words of the Powers Report, which we are going to try to demonstrate here factually with documents, "The financial reporting abuses of management could and should have been prevented or detected at an earlier time had the Board been more aggressive and vigilant." That is the Powers Report. You deny even that, that you could have been more aggressive and vigilant. You just point your fingers at management, and let me tell you, they bear a lot of the responsibility, plenty of it, and their time will come.

But now, you should step up to the plate. You are the Board. You are the captain of this ship that went down, and you are denying any responsibility.

All of those red flags which we are going to go into, you say you did not see them, they were not there, you were not told. There were plenty of things you were told and that you knew which should have triggered much stronger action on your part. I want to go into some of those right now because I do not think the facts support your denial of any responsibility, and I just don't buy it.

There is responsibility in this Board and it should be accepted. Otherwise, directors are going to duck responsibility in all corporations, blame it on people who did not tell them things, even though there were warning signals and even though there were facts, much more than warning signals, facts which we are going to go into which were brought to the attention of the Board and which should have triggered action on the part of the Board.

First, I want to talk about Whitewing, one of these complex transactions. This was an early step which you took as a Board which waded into dangerous waters.

The strategy of Enron was to become asset-light. That means selling assets to or syndicating, sharing the liability or risk of assets, with a third party. The money raised from the sale of these assets was then to be used for new instruments that would offer a higher return, and the sales would improve your balance sheet.

Enron called these assets that were held for sale merchant assets. I want to talk to you about how Enron set about selling these assets and finding outside investors to invest in them, and I will be asking most of these questions of Mr. Winokur, as Chairman, and Mr. Blake. Both of you were on the Finance Committee.

First, back in 1997, according to the *CFO* magazine, Enron is having a challenging year. The debt is the result of enormous growth. It was higher than was consistent with your credit rating, and retaining a high credit rating was critical to the success of your trading business. So with that background, Mr. Blake first, what can you tell me about Whitewing and Nighthawk?

Mr. BLAKE. Well, as the chart indicates,[1] this is a means by which to substitute equity for debt, and that is the $1 billion that comes in from Whitewing is proceeds that can be used to pay down debt, and when you are transferring convertible preferred stock to Whitewing.

Senator LEVIN. Now, when you talked to our staff, did you tell them that you did not have much recollection of this?

Mr. BLAKE. That is correct. I did, Senator.

Senator LEVIN. So you have refreshed your recollection since then?

Mr. BLAKE. Yes, I have.

Senator LEVIN. Fine. Mr. Winokur, what can you tell me about Whitewing and Nighthawk?

Mr. WINOKUR. Nighthawk, which is really an entity owned by Citibank, put up $500 million. Enron put up $500 million into Whitewing, which was an LLC, and that company took the $1 billion and paid it back to Enron, so Enron had net $500 million with which it could pay down its debt or make further investments.

Senator LEVIN. All right. Now, when you met with my staff, did you also tell my staff you did not have much recollection of that transaction?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. Now that you have refreshed your recollections, Enron was borrowing a half-a-billion dollars from Citibank, but it did not show up on the balance sheet of Enron as debt but rather as preferred shares, which looked more like equity than debt. It was a loan disguised as equity in order to avoid showing debt on the books. Now, look at page 2 of Exhibit 15.[1]

Mr. WINOKUR. Sir, I believe it was accounted for as a consolidated subsidiary with a——

Senator LEVIN. Was it shown as a loan?

Mr. WINOKUR. It was shown as—the entity was consolidated and the $500 million of Citibank was a minority interest.

Senator LEVIN. But was it shown as a loan?

Mr. WINOKUR. No, sir.

Senator LEVIN. That is, in effect, what it was.

Let us go now to 1999. The Board is now getting into deeper and deeper water. This time, Jeff Skilling tells the Board about his asset-light strategy, and Andrew Fastow is talking openly about the determination to sell assets. The market goes for it. Enron's stock price continues to go up.

This Nighthawk-Whitewing deal had worked like a charm. Enron borrowed a half-a-billion dollars in funds without appearing to burden the company with more debt. Now, it needed more money to invest in broadband and other new ventures, but it did not want to directly borrow the money and put the debt on the balance sheet, so now you have to figure out a new way to bring funds into Enron.

So the second stage of Whitewing comes along. It is a trust called Osprey. Now, first, Mr. Winokur, did you tell my staff you basically did not remember much about the Osprey transaction?

[1] See Exhibit No. 15, chart entitled "Condor Transaction," which appears in the Appendix on page 253.

Mr. WINOKUR. Yes, sir.

Senator LEVIN. And, Mr. Blake, did you also tell my staff you did not remember much about that transaction?

Mr. BLAKE. Yes, sir.

Senator LEVIN. OK. Now, this was a transaction where Osprey raised $1.5 billion by selling bonds to outside investors and used it to buy a stake in Whitewing. Enron deconsolidated Whitewing, so it took Whitewing off the Enron books. This chart is the second page of that Exhibit 15.[1] It lays out this structure of Whitewing with Osprey. Basically, what the Board did here was use Enron stock as collateral for Osprey's $1.5 billion borrowing.

Mr. Duncan, I believe that you were there when you moved to approve that transaction, is that correct?

Mr. DUNCAN. That is correct.

Senator LEVIN. And, Mr. Blake, you seconded that?

Mr. BLAKE. That is correct.

Senator LEVIN. A billion-and-a-half dollars. At least when my staff talked to you, no memory of that. Osprey had come up 15 times in presentations to the Finance Committee and to the entire Board.

Now, Mr. Winokur, do you know what Whitewing did with the $1.5 billion that it got from Osprey?

Mr. WINOKUR. Well, it repaid Citibank the $500—actually, $570 million, because that was—there was an accrual, and part of the reason was that the convertible preferred stock that had been in Whitewing had appreciated significantly and that was not part of the consideration to Citibank.

Senator LEVIN. Did it also buy Enron's assets?

Mr. WINOKUR. It bought merchant assets at no gain or loss. Those were merchant assets.

Senator LEVIN. All right.

Mr. WINOKUR. And the debt——

Senator LEVIN. Did Enron have to sell these in order to go through its asset-light strategy? Was that part of the strategy, to sell these assets?

Mr. WINOKUR. Well, it was part of the strategy to sell the assets when it was time to sell them. I do not know specifically what the motivation was behind each individual sale.

Senator LEVIN. But you do remember the meeting where Mr. Fastow, the Chief Financial Officer, talked openly about the need to sell assets back in 1999, and Skilling talking about the asset-light strategy? Do you remember that?

Mr. WINOKUR. I understand that strategy, yes, sir.

Senator LEVIN. Do you remember that?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. Was this part of that strategy?

Mr. WINOKUR. Yes, sir. I would also like to say that the bonds were rated and the equity in affiliates, which is where Whitewing was then carried, showed the consolidated balance sheet for all of the equity and affiliate transactions.

[1] See Exhibit No. 15 which appears in the Appendix on page 253.

Senator LEVIN. Now, were the bondholders—did they have a guarantee that if the assets did not generate cash to pay them back on their bonds, that Enron shares would be used to pay them back?

Mr. WINOKUR. Yes, sir, and that was fully disclosed, as well.

Senator LEVIN. These were promises that were made to the bondholders that Enron shares would be used if they did not get——

Mr. WINOKUR. They were made to the bondholders and disclosed in Enron's financials, yes.

Senator LEVIN. So they could not lose. The bondholders could not lose. Enron stock was there to guarantee the return, is that the bottom line?

Mr. WINOKUR. Well, they could lose if Enron went bankrupt and could not make good on its——

Senator LEVIN. Right. Other than that, though, Enron stock, no matter how much was needed, was used to back up that bond return, is that correct?

Mr. WINOKUR. It was not an infinite quantity of stock, as I recall. It was either convertible preferred stock in a fixed amount or common shares.

Senator LEVIN. You think that there was a limit on how much stock could be converted or used to pay for those bonds?

Mr. WINOKUR. I think it was convertible preferred stock was available, as well.

Senator LEVIN. So was there, then, in effect, either through convertible preferred stock or otherwise, a guarantee as long as Enron was in business that whatever amount of stock of Enron was needed to pay those bond holders, it would be used?

Mr. WINOKUR. It was contingent support, sir.

Senator LEVIN. Contingent?

Mr. JAEDICKE. That would have been disclosed in the footnote.

Senator LEVIN. I am asking you, what was there? Was there any limit on how much Enron stock, preferred or otherwise, could be used to back up the payment of those bonds to the bondholders? That is a simple question.

Mr. JAEDICKE. Was there any limit?

Senator LEVIN. Yes. As long as Enron was in business, was there any limit to the amount of stock?

Mr. JAEDICKE. I think the only limit that would come into play would be that there is a transaction approval process on the sale and purchase of assets and the issuance of stock. It would have had to come to the Board.

Senator LEVIN. My question is, to repay those bondholders what they were guaranteed, was there any limit on the number of shares of Enron stock that had to be or would be sold, if necessary, to pay them back? That is my question.

Mr. JAEDICKE. The market would have imposed the limit, just like they would have imposed a limit on how much you can borrow.[1]

Senator LEVIN. I am talking about the number of shares sold, not the value of——

Mr. JAEDICKE. I do not think—no——

[1] See Exhibit No. 80 for clarification which appears in the Appendix on page 665.

Mr. WINOKUR. Sir, the minutes say that there were reserved 20 million additional shares of common stock and 100,000 preferred shares of the company for issuance under the share settlement agreement.

Senator LEVIN. Take a look at Exhibit 32,[1] if you would, the "Stock Price Risk and Financing."

Mr. WINOKUR. Yes, sir.

Senator LEVIN. Do you see that risk on Osprey?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. Ten thousand shares if it went down to $40?

Mr. WINOKUR. Ten million shares, yes.

Senator LEVIN. Ten million shares if it went down to $40?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. If it went down to $20, what would be the risk?

Mr. WINOKUR. I cannot do that calculation.

Senator LEVIN. But whatever was necessary?

Mr. WINOKUR. No. The share settlement agreement that I just read—now, again, I do not have the detailed document—said that a certain amount of common stock or preferred stock was reserved for issuance, and that is why I said to you that I believe that there was a contingent limited guarantee.

Senator LEVIN. You believe it was limited as to how many shares would be sold to pay back those bondholders, is that what you are saying?

Mr. WINOKUR. In 1999, when this was done, to the best of my knowledge.

Senator LEVIN. Let me just make sure here that we are on the same wavelength. We are talking about the number of shares, not the amount of the dollars to be repaid. But what I am asking you again is, was there any limit on the number of shares of Enron that would be sold to pay back the bondholders? That is my question. You are saying the answer is yes. Is that your answer?

Mr. WINOKUR. To the best of my recollection—this was a transaction that happened 3 years ago—I am referring to the minutes which says there will be reserved 20 million additional shares of common stock and 100,000 preferred shares of the company for issuance under the share settlement agreement. That is my only recollection, is what is here.

Senator LEVIN. You do not know, then, whether or not there was any limit?

Mr. WINOKUR. I do not know——

Senator LEVIN. You know how many were reserved, but you do not know whether there was a limit?

Mr. WINOKUR. Well——

Senator LEVIN. Under the agreement—I am just trying to get an answer.

Mr. WINOKUR. I only know what is in the minutes, sir.

Senator LEVIN. All right. You do not know, then, whether there was a limit or not.

Next, LJM. Now getting more and more dangerous and deeper, here is another off-the-books entity that Enron helped to create which bought Enron assets. With the Board's approval of the part-

[1] See Exhibit No. 32 which appears in the Appendix on page 334.

nership, here is what happened. On June 28, 1999, the Board held a special meeting in which all five of you participated either by phone or in person. You approved the creation of LJM1, and for the first time, you waived Enron's conflict of interest provision in your code of conduct to allow the Chief Financial Officer, Andrew Fastow, to take an ownership interest and act as the general partner of the LJM partnership.

Now, Mr. Winokur, under the normal order of business, this matter was not first presented to the Finance Committee, is that correct?

Mr. WINOKUR. Yes, sir. That is correct. It was not presented.

Senator LEVIN. It was not presented to the Finance Committee. The Finance Committee was skipped. Why was that?

Mr. WINOKUR. Well, this was not a regularly scheduled meeting of the Board.

Senator LEVIN. You had a lot of special meetings of the Board.

Mr. WINOKUR. Special meeting. I cannot tell you why there was not a special Finance Committee meeting.

Senator LEVIN. Did you ask?

Mr. WINOKUR. I do not recall asking why there was not a special Finance Committee meeting, no.

Senator LEVIN. Now, you testified this morning that the Board did not waive the code of conduct.

Mr. WINOKUR. Yes, sir.

Senator LEVIN. That was your testimony this morning. Take a look at Exhibit 19, if you would.[1]

Mr. WINOKUR. Sir, I know that the chart uses the term——

Senator LEVIN. That is your chart, is it not?

Mr. WINOKUR. No, this is management's chart.

Senator LEVIN. Was it presented to you?

Mr. WINOKUR. It was presented to us, and in the resolution that the Board approved, we ratified management of the Office of the Chairman's decision that permitting Mr. Fastow to participate in this would not be adverse to Enron.

Senator LEVIN. Well, that is a different issue. The question is whether or not it was considered inside Enron, as well as by the rest of us, as a waiver of your code of conduct. Your own document says, "waiver of code of conduct," yet you testified this morning that there was no waiver of a code of conduct. I am just presenting you with your own document.

Mr. WINOKUR. Sir this is——

Senator LEVIN. It says it was.

Mr. WINOKUR. This was management's presentation to the Board. We applied the code of conduct. The Chief Executive has the ability to make a determination, as I said in my statement this morning, that permitting Mr. Fastow to make this investment would not have any probability of conflict of interest, and we ratified that decision, which is applying the code of conduct.

Senator LEVIN. Applying the code of conduct. Let us take a look at Exhibit 20.[2] Now, the second time it is presented to you as a waiver. It has got the Enron logo on there. Look at the bottom, Fi-

[1] See Exhibit No. 19, entitled "Key Elements of Transaction to be Approved," which appears in the Appendix on page 261.

[2] See Exhibit No. 20 which appears in the Appendix on page 271.

nance Committee, Board of Directors action requested. “Ratify decision of Office of the Chairman to waive—not apply—waive code of conduct in order to allow A. Fastow participation.”

Now, did you tell them, hey, wait a minute, do not present that to us as a waiver. Present that to us as an application. You did not tell them that, did you?

Mr. WINOKUR. When we approved it at the Board meeting, that is what we approved, the application.

Senator LEVIN. I understand that. That was the first time.

Mr. WINOKUR. The resolution following this meeting, which was in October 1999, has the same language.

Senator LEVIN. Right. I understand. But it is presented on Enron documents the second time now as a waiver. That is the way it was viewed inside Enron by the management. That is the way it is viewed by me. But you are saying, no, we did not waive it, we applied it. I am just asking you this question. When this was presented to the Board as a waiver in the Enron document Exhibit No. 20,[1] did you object to the presentation of it to you as a waiver?

Mr. WINOKUR. I did not treat it as a waiver. I did not object to the words in this document.

Senator LEVIN. You did not tell management, hey, wait a minute. You are asking us to waive——

Mr. WINOKUR. Yes, sir.

Senator LEVIN [continuing]. For the second time. We are telling you, we are not waiving. We are applying. Did you do that?

Mr. WINOKUR. We did that in the Board approval.

Senator LEVIN. You told them, this is not a waiver? Did you ever use the words, “This is not a waiver” in the Board approval?

Mr. WINOKUR. No, sir.

Senator LEVIN. No.

Mr. JAEDICKE. Mr. Chairman, can I——

Senator LEVIN. Sure.

Mr. JAEDICKE [continuing]. Just inject that I think if you—I am not absolutely sure of this, but I think if you look at the minutes of that meeting, you will find that Fastow himself says in presentation—this slide does not say it, but that it requires the Board to ratify the decision of the Office of the Chairman——

Senator LEVIN. Right.

Mr. JAEDICKE [continuing]. That his—it requires a finding and a recommendation that it will not—that there appears to be a zero probability that it will be adverse to Enron. Now, he did not use zero probability, but——

Senator LEVIN. That is his opinion.

Mr. JAEDICKE. But he presented it, I think, properly, is what the minutes indicate.

Senator LEVIN. He presented it in this document as a waiver. Was that proper?

Mr. JAEDICKE. The document——

Senator LEVIN. Is that proper?

Mr. JAEDICKE. No.

Senator LEVIN. Thank you. Now, LJM1 is an extremely unusual arrangement. You set up a private equity fund. You waive the code of conduct, or in your words, you approve a deviation from it, and install Enron’s CFO as the managing partner of the fund. Each of you said during your interview that you had never approved a similar arrangement before and you were unaware of any company that had its CFO running a private equity fund on the side. So far, are you with me?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. None of the experts we have contacted have ever heard of such an arrangement, either. But LJM1 was made after 3 days notice of the proposal, no prior Board discussion with either Enron management or Andersen, no written legal opinion, no prior Finance Committee review. Now, some of you told us that the Board was told that speed is of the essence. Is that your understanding? Was speed of the essence?

Mr. WINOKUR. I do not recall saying that.

Senator LEVIN. You do not remember——

Mr. JAEDICKE. I think I can speak to that.

Senator LEVIN. Is that what you were told, that speed is of——

Mr. JAEDICKE. Well, the meeting took place in the middle of June. The end of June was the end of the quarter, second quarter. Shortly after that, you had to issue financial statements. They had the Rhythms stock. The Rhythms stock had gone up greatly and they wanted to get it hedged. We thought this was a valid hedge. We did not—I think the reason they wanted it done by the end of June is because they did not want to be in the position of having a fair value investment, a stock on their books, a mark-to-market, without a hedge. So there was—the hedge should have been put on by the end of June.

There were other items on the agenda of that June Committee, sir. I do not know, we had a stock split. There were two or three other items on the agenda, and I think it was not—I think we can probably find other decisions were made that necessarily did not go through a particular committee.

Senator LEVIN. This was an unusual transaction, was it not?

Mr. JAEDICKE. Well, you mean——

Senator LEVIN. No one had ever heard of an equity fund like this before.

Mr. JAEDICKE. What is the unusual transaction?

Senator LEVIN. To create an equity fund to buy your own assets.

Mr. JAEDICKE. Sir, I am sorry. We approved a specific transaction, which was a Rhythms hedge, and the company—we did it with Fastow. That was different. But the use of hedges and the use of at least what I would call less-than-perfect correlation hedges, was explained in detail in the annual report. I mean, that was part of the strategy.

Senator LEVIN. But you have said that now the only purpose of this was to acquire a hedge.

Mr. WINOKUR. Sir, LJM2, which was set up in October, was, in fact, an alternative optional source of capital.

Mr. JAEDICKE. That was different. I am sorry. I thought you were talking about LJM1.

Senator LEVIN. I am talking about LJM1. Is it not true that LJM1, in addition to the hedge, which you said was its only purpose, could negotiate with the company regarding the purchase of additional assets? Is that not true?

Mr. JAEDICKE. That is true.

Senator LEVIN. So it was not just for the hedge. It had an additional purpose, which was to buy assets.

Mr. JAEDICKE. And in the meantime, you would put in the controls that were necessary.

Senator LEVIN. I understand, but you just said a minute ago the sole purpose——

Mr. JAEDICKE. Sir, I would just like to point out to you——

Senator LEVIN. But you just said a minute ago the sole purpose was for the hedge. I am just pointing out to you that it had an additional purpose, which was to buy assets.

Mr. JAEDICKE. I told your staff this, that the ironic part of this is—I have been in a situation recently where I would have been prepared to have an inside transaction, in this case, with an equity fund that was run by a very senior—not the CFO, but a very senior person in the company. It turned out the transaction did not—because I thought in that case, as this case, that you could do it better inside than you could outside. It was cheaper. It was quicker. It was more efficient. That was the thought on LJM1. And on the related party, I just happened to be in a similar position with a very similar fund. It did not take place, but I would have supported it.

Senator LEVIN. In October 1999, more than 3 months after you approved LJM1, the Finance Committee was asked to approve LJM2. Mr. Fastow now was proposing another vehicle that would complete a large number of deals with Enron and push further the Enron strategy to move assets off the books.

Mr. Winokur, I believe you told the staff that before the Finance Committee meets, you typically meet with Enron management to set the agenda and to discuss the issues, but that did not happen with LJM2, did it?

Mr. WINOKUR. Well, we had a telephonic meeting in advance to go over the agenda. I have no reason to believe it did not happen.

Senator LEVIN. Did you not tell us the first time you heard about this was at the Finance Committee meeting on October 11?

Mr. WINOKUR. I do not recall whether there was a telephone meeting or not.

Senator LEVIN. When was the first time you heard about LJM2?

Mr. WINOKUR. At the meeting, unless we had a telephonic meeting to describe the agenda. Sir, I do not remember which.

Senator LEVIN. Is not the creation of LJM2 something that you, as Chairman of the Finance Committee, should have been consulted on before the day that you were expected to make a decision?

Mr. WINOKUR. Well, to make a recommendation, yes, sir.

Senator LEVIN. To make a recommendation. Well, it is a decision to make a recommendation. But my question is, should you not have been consulted before the day that you were expected to make a decision or a recommendation?

Mr. WINOKUR. Sir, I do not recall when I learned of the LJM2 matter, whether it would have been with the material that was provided in advance of the meeting or in a telephonic conversation or at the meeting itself.

Senator LEVIN. But my question is a little different. Should you not have been consulted about this transaction, this proposal, prior to the meeting, as Chairman of that Committee?

Mr. WINOKUR. The principal purpose of a pre-meeting was to make sure that we had the agenda laid out, not so much necessarily to go through individual items in detail.

Senator LEVIN. Was LJM2 on the agenda?

Mr. WINOKUR. I do not have the agenda here.

Senator LEVIN. Do you remember whether it was on the agenda?

Mr. WINOKUR. Well, I believe it was, yes, sir.

Senator LEVIN. This is a major transaction. We are talking billions of dollars. You are now telling us that you would not normally have discussed a transaction of that magnitude prior to it appearing on the agenda at the Finance Committee?

Mr. WINOKUR. Sir, we were talking about organizing a fund that might raise $200 million that would be alternative and optional as a source of funds for Enron. It did not require—there was no specific transaction being proposed except the organization of the fund and the ratification of the decision to permit Mr. Fastow to participate in it. There was no sale being discussed.

Senator LEVIN. It was a fund, however, which would openly now have a member of the Enron management participate in an outside company whose purpose was to purchase assets, is that correct?

Mr. WINOKUR. Yes, sir. We had a vigorous discussion at the meeting.

Senator LEVIN. And you decided to let him do it?

Mr. WINOKUR. We decided to ratify the decision of the Office of the Chairman.

Senator LEVIN. Another off-balance-sheet vehicle, buying assets. But this time and the time before, this is really interesting, this time, when we talk about LJM, now you have got a guy who is management who is on the other side of the table. He is buying assets from you, and he is wearing both hats. He is now playing a key role in the sale, setting the sale price, and he is also buying at the same time. You put certain what you call protective devices in place, but they sure did not work very well.

Mr. WINOKUR. Sir, the concept of LJM was to provide bridge financing for the business unit heads who wanted to sell assets. They were not required to sell them to LJM2. They had their own financial incentives. They had their own operational capabilities. So LJM2 was an alternative and optional source of capital for them. If they did not like the price LJM2 was offering, they did not have to use it.

Senator LEVIN. Why did you create LJM2? What was wrong with Whitewing?

Mr. WINOKUR. Whitewing was a very large vehicle. It was expensive and time consuming and complicated to create. To have an independent, smaller, private vehicle which would provide bridge financing for smaller transactions seemed like a perfectly reasonable thing to do.

Senator LEVIN. Let me show you Exhibit 21,[1] if you would. This is the way LJM was being marketed. The first page of the text, in

[1] See Exhibit No. 21 which appears in the Appendix on page 272.

the middle, says, "Under Mr. Fastow's management, the Partnership expects to have the opportunity to co-invest with Enron" and then "acquire existing Enron assets on a highly selective basis. This access to deal flow should provide the Partnership with unusually attractive investment opportunities." The memo goes on to say it is going to be managed by a "team of three investment professionals who all currently have senior level finance positions with Enron." Then if you look at the end of this document, the last line, "The Partnership should also benefit indirectly from time spent by the Principals in evaluating and structuring investments for Enron, as many of these investments may become candidates for investment by the Partnership."

They are touting their inside information in Enron as they are selling the interest in that LJM partnership. That conflict of interest is being sold as a plus to people who are investing. Now, did you ever inquire as to how they were marketing this? Did you ever ask for any marketing documents like this?

Mr. WINOKUR. We asked and were told that Enron's counsel, Vinson and Elkins, had reviewed drafts of the document. I did not actually see this document until my work on the Powers Committee, and we, of course, were never told that Mr. Kopper was a participant. Mr. Glison said in his Powers interview that his name was erroneously included here.

Senator LEVIN. Mr. Glison was not erroneously included, though.

Mr. WINOKUR. Well, as it turned out.

Senator LEVIN. Right. But what I am saying is, you never asked to see documents?

Mr. WINOKUR. This was an independent, separately organized entity. We asked our counsel to review the drafts to make sure the disclosures were proper.

Senator LEVIN. And did your counsel tell you that it is OK to tout a conflict of interest as a way to sell something?

Mr. WINOKUR. They did not.

Senator LEVIN. Have you asked them about why they did not?

Mr. WINOKUR. Well, I did not ask Vinson and Elkins, no, sir, but the Powers Committee report makes it clear that Vinson and Elkins reviewed these drafts. They would have done that and reported through the Enron legal chain and no one came forward——

Senator LEVIN. And after you heard that they approved this kind of marketing, using a conflict situation to sell an interest, saying that: Hey, I have got an inside position. We are in Enron, three of us. We are in a great position to help this partnership that is buying things from Enron get a good deal. That is being used, touted. And you are saying your lawyer saw that and approved it. Then my question to you is, after you heard that he had approved it and after you now have read this, have you ever asked your lawyer, how in heaven's name could you have approved that? That is my question.

Mr. WINOKUR. Sir, first of all, we knew that a possibility is that Enron would be selling assets to LJM2. One of the reasons for establishing LJM2 was to provide an optional alternative source of capital to buy assets from Enron, and the benefit of having Fastow, who is the only person we knew about, involved in this is that he would know the assets, and the benefit of having the other people inside Enron who ran divisions to go to Fastow, if they did not like Fastow's bid, they did not have to take it. We also had the Chief Risk Officer and the Chief Accounting Officer reviewing each transaction. So the fact of the conflict was known from the beginning.

Senator LEVIN. Exhibit 16,[1] if you will take a look at it, will show you how you could have sold these assets without that kind of a conflict. This is the result, though, of what happened. When LJM bought these Enron assets—now we are talking LJM again—Enron tacitly agreed to buy some of them back if LJM could not sell them. Are you aware of that?

Mr. WINOKUR. No, sir.

Senator LEVIN. When that happened, Enron paid more to LJM than Enron had paid to buy the asset in the first place. Are you aware of that?

Mr. WINOKUR. No, sir.

Senator LEVIN. In negotiating the sale of assets to LJM, Fastow clearly had a superior bargaining position over Enron personnel because both sides reported to him. Are you aware of that?

Mr. WINOKUR. Well, the operating divisions did not report to Mr. Fastow.

Senator LEVIN. Were there people involved on the Enron side making a decision who did report to Fastow?

Mr. WINOKUR. We later found that was the case. That was not consistent with the controls that we had put in place.

Senator LEVIN. Those controls were not working very well, were they?

Mr. WINOKUR. We were told they were and they obviously turned out not to be.

Senator LEVIN. So that, at a minimum, the controls you put in place did not function to protect Enron.

Mr. WINOKUR. Well, Mr. Fastow told us in October with Mr. Buy, Mr. Causey, and Mr. Skilling sitting right there, that the three of them were reviewing every transaction with LJM.

Senator LEVIN. My question, though, is a little different. My question is the controls that you put in place did not work very well.

Mr. WINOKUR. Well, we did not know that.

Senator LEVIN. I am just saying——

Mr. WINOKUR. We were told that they——

Senator LEVIN. They did not work very well.

Mr. WINOKUR. Well, they should have worked, but people did not do them.

Senator LEVIN. Did LJM investors get a 69 percent return on their investment?

Mr. WINOKUR. I saw a presentation through my Powers work to the LJM investors that showed a very high rate of return. I think that was the number you are quoting.

Senator LEVIN. And would you agree that when LJM was benefitted to that extent, that would be at the expense of Enron?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. And Fastow would profit from that?

[1] See Exhibit No. 16 which appears in the Appendix on page 256.

Mr. WINOKUR. Sir, in May 2000, Mr. Fastow told us he was spending approximately 3 hours a week on these vehicles and the vehicles were earning approximately an 18 percent return.

Senator LEVIN. But my question is a little different. Do you agree that Fastow, when a 69 percent return was obtained by LJM, personally benefitted from that huge return?

Mr. WINOKUR. Absolutely.

Senator LEVIN. OK. That is the outcome of that conflict of interest—one of the outcomes, because you have got a guy on the other side of the table now who is doing the negotiating who, when he is putting on the LJM hat, gets a 69 percent return at the expense of Enron. That is the outcome of the conflict of interest.

Mr. WINOKUR. But his supervisor, Mr. Skilling, and his peers, Mr. Buy and Mr. Causey, we were told that they were reviewing each and every transaction. Mr. Causey, Mr. Buy, and Mr. Skilling had no economic interest in LJM. Their interest was in Enron stock. If they had known, presumably, they would have taken steps to make sure that LJM was not making a 69 percent return. We were told they were on top of each and every transaction.

Senator LEVIN. And when you found out to the contrary, you asked them about it?

Mr. WINOKUR. I found out the contrary in the Powers investigation.

Senator LEVIN. That is the first time you knew?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. On the LJM transaction reviews, let us go on to that, Mr. Jaedicke. The Audit Committee had the primary responsibility for reviewing these transactions. It conducted two annual reviews of LJM transactions, one on February 7, 2000, and the other a year later in February 2001. First of all, is it true that the Audit Committee spent no more than 30 minutes at each meeting going through the LJM transactions?

Mr. JAEDICKE. I am sorry, who said that?

Senator LEVIN. I am asking you, is it true?

Mr. JAEDICKE. Is it true that we spent no more than 30 minutes?

Senator LEVIN. On the LJM transactions during those Audit Committee meetings.

Mr. JAEDICKE. Well, we did not necessarily review each individual transaction. We reviewed the type of transactions. We asked pointed questions about are these done at arm's length or fair to Enron. We were assured that they were. Arthur Andersen was sitting there. That footnote is in the annual report and it is an auditable footnote, and neither management nor Andersen—management cannot make that representation to us unless they have some reason, and Andersen has to audit it.

Senator LEVIN. I understand, but my——

Mr. JAEDICKE. So a half-hour? Yes, I would imagine that was probably 25 percent of the time in a typical Audit Committee, but we had the information before, and I do not know how many—I do not know how much time people spent on the exhibits and so on when they were given to us.

Senator LEVIN. OK.

Mr. JAEDICKE. All I can say is I think the—even though we did not have the information we needed, we were not told the truth, in fact, I think we spent a sufficient amount of time——

Senator LEVIN. That was not my question.

Mr. JAEDICKE [continuing]. To carry that out.

Senator LEVIN. My question was, is it true you spent no more than 30 minutes? It is just a simple, direct question.

Mr. JAEDICKE. I would suppose that would be true.

Senator LEVIN. Thank you. Now, on LJM3, on October 6, 2000, Fastow proposed LJM3 to the Finance Committee and asked for a third waiver. The Committee approved that waiver. At the same time, Dr. Winokur, I believe you proposed that the Compensation Committee review Fastow's LJM compensation. Mr. Blake, you proposed that the Finance Committee review Enron's transactions with LJM every quarter.

Mr. BLAKE. Yes, sir.

Senator LEVIN. So now I want to focus on the October 6, 2000, meeting, where Fastow proposes LJM3 to the Finance Committee, asks for the waiver, and gets it. But now, Dr. Winokur, you are proposing that there be a review of his compensation, and Mr. Blake, you are proposing that the Finance Committee review the transactions every quarter. These proposals were unanimously agreed to at the meeting. So the Committee now imposes some reviews. Now, let us talk about the follow-through on those decisions.

First, I think I asked Dr. LeMaistre about this one. You attended the Finance Committee meeting on October 6 when that proposal was adopted for the Compensation Committee to review Mr. Fastow's compensation. But that review was not completed in 2000. In fact, it was not done that year at all, was it?

Dr. LEMAISTRE. As far as I know, it was not.

Senator LEVIN. Now, why didn't you promptly do the review since you had that vote?

Dr. LEMAISTRE. Primarily because we did not have the information, and it was our understanding at the time that Fastow's compensation was to be under the control of formulas. It was to come through with the other reports on the quarterly base and the annual base and it did not.

Senator LEVIN. In other words, you are saying it was not intended that you review that compensation immediately? You were supposed to wait?

Dr. LEMAISTRE. Mr. Winokur's direct words in that meeting were, "Perhaps it would be a good idea to have the Compensation Committee take a look at information regarding his compensation." It was a remark that would indicate to me that they already had the compensation there, and that turned out not to be the case at the end of the first quarter when I checked, and, therefore, that is basically the reason I did the checking.

Senator LEVIN. When did you do the checking?

Dr. LEMAISTRE. After the first quarter of 2001.

Senator LEVIN. It was reported in the *Wall Street Journal*—we have gone into this today—that Mr. Fastow had made millions of dollars more from LJM. When was that?

Dr. LEMAISTRE. That was on October, 19, 2001.

Senator LEVIN. It was only then?

Dr. LEMAISTRE. That was the first time that any of us knew that there was something wrong going on.

Senator LEVIN. Right, but you had made inquiry about his compensation. Didn't you ask the Compensation Officer at Enron, Mary Joyce, about it?

Dr. LEMAISTRE. I asked Mary Joyce about it.

Senator LEVIN. And what did she tell you?

Dr. LEMAISTRE. She said she did not have the information.

Senator LEVIN. Did you say, well, I want it?

Dr. LEMAISTRE. She knew that I wanted it and I asked——

Senator LEVIN. Did you get it?

Dr. LEMAISTRE. I did not.

Senator LEVIN. This is the heart of the problem. You have got a Board that says, I want it. You have got a request for it. It does not come, and you do nothing. That is an approach which is unacceptable for a Board. Those folks are supposed to be reporting to you. You are the captains. You make a decision. We want to find out about this compensation. You make an inquiry of an employee and she says she does not have the information, she will get back to you. She does not, and nothing happens. There is a *Wall Street Journal* article a year later. That is not the way a Board can operate and carry out its fiduciary duties, folks.

Dr. LEMAISTRE. I did have a subsequent conversation to see if the information had been obtained. It had not, and that is immediately prior to all of the things that unfolded very rapidly in the fall. But let me make it clear——

Senator LEVIN. Should you have gotten that information?

Dr. LEMAISTRE. Yes, I should have gotten it and I should have gotten it through channels. It was Mr. Skilling's responsibility to have put that through and he did not. It did not come through any of the transactions. Mr. Fastow, in his declaration of the controls on him, said he reported that information to Mr. Skilling.

Senator LEVIN. But you had a conversation now with this employee, Mary——

Dr. LEMAISTRE. Mrs. Joyce, yes.

Senator LEVIN. Mary Joyce, and you asked her for information——

Dr. LEMAISTRE. Yes.

Senator LEVIN [continuing]. And she did not get it to you.

Dr. LEMAISTRE. She had not received it, that is correct.

Senator LEVIN. And did you ask her to get it?

Dr. LEMAISTRE. I asked—I told her I wanted all of the information on any 16(b) officer that had outside income——

Senator LEVIN. And would that include Fastow?

Dr. LEMAISTRE. Of course, yes.

Senator LEVIN. Sure. That was the reason you called, was it not?

Dr. LEMAISTRE. That is right.

Senator LEVIN. You did not mention his name?

Dr. LEMAISTRE. No, I did not mention his name.

Senator LEVIN. Even though that is why you called?

Dr. LEMAISTRE. That is exactly right, but I wanted it on all 16(b) officers.

Senator LEVIN. And you did not get it.

Dr. LEMAISTRE. I did not get it, but if I had gotten it, I would have had some other people involved in there, as you now know.

Senator LEVIN. Good. The point is, you did not get it and you did not act to get it and that is——

Dr. LEMAISTRE. I did not act to get it primarily because it was supposed to come through with the other reports and it did not.

Senator LEVIN. But did she not tell you she would get it to you?

Dr. LEMAISTRE. No, she did not.

Senator LEVIN. You did not say you wanted that information? You are doing this report for the Board. You are told, hey we would like to know more about it, and you just call up and say——

Dr. LEMAISTRE. She said she did not have the information. I said, well, let me know when it gets there.

Senator LEVIN. And did she?

Dr. LEMAISTRE. She did not let me know, so I asked again a few months later and she did not have it, and that was in August or September.

Senator LEVIN. Did you just throw your hands up? I mean, she does not have it.

Dr. LEMAISTRE. Well——

Senator LEVIN. Why does she not have it? You are a Board member. You are paid a lot of money. You are carrying out a Board direction. You want information. You do not get it. She will call you when she gets it. She does not call you. Two months later, she still does not have it.

To me, that is an approach which is totally unacceptable, I have got to tell you. I think that is what characterized the Board—is that it was deferential to management. I want to go into another document on that.

When you were told, finally, after you found out how much money—if you would take a look at Exhibit No. 24b.[1]

Dr. LEMAISTRE. All right.

Senator LEVIN. So now it appears in the *Wall Street Journal,* and the Board asks, I think, both Mr. Duncan and Dr. LeMaistre to call Fastow. I think, Dr. LeMaistre, you said in your interview that you asked the Enron General Counsel to write the questions that you would ask Mr. Fastow on the phone, and Exhibit 24b is the document that the General Counsel faxed to you with your notes from that phone conversation, is that correct? We are looking at Exhibit 24b now.

Dr. LEMAISTRE. That is correct, Mr. Chairman.

Senator LEVIN. OK. And here is the note that he typed for you. "Andy, because of the current controversy surrounding LJM1 and LJM2, we believe it would be helpful for the Board to have a general understanding of the amount of your investment and of your return on investment in the LJM entities. We understand that a detailed accounting of these matters will soon be done in connection with the response to the SEC inquiry. We very much appreciate your willingness to visit with us."

This is a guy who is supposed to be working at your direction, and you cannot get much more deferential and obsequious than that. And not only that, you then want to make sure that he under-

[1] See Exhibit No. 24b which appears in the Appendix on page 283.

stands right up at the front how much you appreciate his willingness to visit with you, and I presume you take a line, circle that, "We very much appreciate your willingness to visit with us," and make sure that goes at the top.

Why do you not call up and say, "What in God's name is going on? We just read something in the *Wall Street Journal* here that just shakes the heck out of us. Is it true? How much money did you make? What is your return?" That is not what comes out here.

You apparently, when he told you how much money he made, found it to be—I think this is your handwriting?

Dr. LeMaistre. That is correct, sir.

Senator Levin. "Incredible" is your word.

Dr. LeMaistre. Mr. Chairman——

Senator Levin. Yes, please.

Dr. LeMaistre. This is drafted by legal counsel and I followed it directly.

Senator Levin. Right. But is not that arrow that puts the, "We very much appreciate your willingness to visit with us—"

Dr. LeMaistre. Yes, that is right, because——

Senator Levin. That is your writing, is it not?

Dr. LeMaistre. Yes, and may I explain it?

Senator Levin. Sure.

Dr. LeMaistre. The day before when I talked to Mr. Fastow, he was very cautious at first about this, and finally, he said he would be glad to talk with us. But it was a decision that he could have made not to talk to us, and we would have had to go through channels to get it, but we wanted it immediately, that is the reason that we did it that way.

Senator Levin. Why do you have to go through channels? Why can you not just call up Fastow and say, I want to know right now?

Dr. LeMaistre. I could have, but I would have not used language in here had I done that. I would have used——

Senator Levin. Why did you not use language that was not in here?

Dr. LeMaistre. Primarily because——

Senator Levin. I guess that is what it comes right down to.

Dr. LeMaistre. Well, the point is that this is what our General Counsel told us to use in talking about income to a third party investment, an SPE.

Senator Levin. Were you mad?

Dr. LeMaistre. I was mad after the answer to the first question.

Senator Levin. Did you let him know?

Dr. LeMaistre. Yes.

Senator Levin. Right there on the phone?

Dr. LeMaistre. Yes.

Senator Levin. Good. That is a year late, but good.

Now, there were supposed to be quarterly reviews by the Finance Committee, I believe, because the Finance Committee was supposed to begin quarterly reviews of the LJM transactions, according to the decision of the Committee, and the Finance Committee agreed. But there is only one quarterly review that was ever conducted by the Finance Committee, which was in February 2001.

So if my recollection is correct, the decision of the Board was October 2000 that these quarterly reviews of these LJM transactions would be conducted, but there was only one, and that was February 12, 2001. Now, why is that?

Mr. WINOKUR. The first meeting after the October meeting was December, which was about 6 or 7 weeks later, so I think we assumed that a quarterly review would have meant after the year end, since the October meeting would have been around the end of the third quarter. After the February quarter, there was not activity, new investments being made, and by June, Mr. Fastow had sold his interest, so there was no more related party aspect.

Senator LEVIN. We will get to that in a moment, but there were supposed to be what are called deal approval sheets, or DASHs, for each of the LJM transactions, I believe, since they were transactions with a related party. Did you ever see those DASHs, those LJM DASHs?

Mr. WINOKUR. No, sir. There is an LJM approval sheet and a DASH which is for every transaction. They are separate.

Senator LEVIN. And did you ever see the DASH?

Mr. WINOKUR. The regular DASHs, we saw all the time——

Senator LEVIN. For LJM?

Mr. WINOKUR. No.

Senator LEVIN. Should you have?

Mr. WINOKUR. Those were internal and those, we were told, were being reviewed by Mr. Skilling, Mr. Causey, and Mr. Buy. There would have been no reason, unless the size of the investment was such that it would have normally come through our——

Senator LEVIN. So that was not normally supposed to come to you?

Mr. WINOKUR. No, sir.

Senator LEVIN. But I believe that, Mr. Jaedicke, those DASHs should have come to you, is that not correct?

Mr. JAEDICKE. No, sir. We did not—we reviewed the transactions and the type of transactions and the fairness, but we did not go—we are not auditors and so we did not go to the level of the deal approval sheets.

Senator LEVIN. So those deal approval sheets were not supposed to go to any of the committees, is that correct?

Mr. WINOKUR. Sir, transactions involving Enron's expending more than $75 million came to the Board for approval. Transactions more than $25 million but less than $75 were within the purview of Mr. Lay and Mr. Skilling. So our practice was that the transactions between $25 and $75, those DASHs were packaged up and we were sent them after the fact to look at, so we could comment on them. The deals would have been approved, but if any member of the Committee had any questions, he could bring those up.

So the only expenditure of cash that we would have seen would have been above that level of $25 million, and for divestitures, the level was much higher. So to the extent that Enron was selling assets, the transaction approval process would not have required us to see those.

Senator LEVIN. Even though there was this conflict of interest problem?

Mr. WINOKUR. The conflict of interest was being dealt with because Mr. Skilling, Mr. Buy, and Mr. Causey were reviewing, according to what Mr. Fastow told us, every transaction.

Senator LEVIN. All right, so that there was no need for a DASH?

Mr. WINOKUR. The only need we had was what we got, and that was to make sure we were told regularly that the controls we put in place were working.

Senator LEVIN. You did not need the DASH in order to achieve that?

Mr. WINOKUR. No, sir.

Senator LEVIN. That is just what I was asking. There was no need, then, for you, in your judgment, to get one of those DASHs for these transactions because you had another mechanism that you thought was doing the control?

Mr. WINOKUR. We were told the people who did review the DASHs had done so.

Senator LEVIN. Right, which is another mechanism.

Mr. WINOKUR. Yes, sir.

Senator LEVIN. Now, I believe you just testified that when you learned that Fastow was selling his LJM interest, that there was no need for a second quarterly review. But the first quarterly review, I believe, was February 12, is that correct?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. When did he sell his interest?

Mr. WINOKUR. I said two things. I said there were no transactions that we knew about that occurred with LJM after the February meeting. He sold his interest, I later learned, in June. That was disclosed to us in August, I think.

Senator LEVIN. But should there not have been a quarterly review in June? You had one in February——

Mr. WINOKUR. We have a May meeting and an August meeting, and so we——

Senator LEVIN. A quarterly——

Mr. WINOKUR [continuing]. We did not have one in the May meeting. At the August meeting, we were told that he had sold his interest in June.

Senator LEVIN. Right, but since it was supposed to be a quarterly review, and there was one that occurred in May—there is one that occurred in February, should there not have been one in June, is my question.

Mr. WINOKUR. If there were transactions to review, yes, sir.

Senator LEVIN. In other words, when you did not get a quarterly report, you assumed there were no transactions?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. And did you check?

Mr. WINOKUR. No, sir.

Senator LEVIN. Now, did you know to whom he sold it, by the way?

Mr. WINOKUR. I did not know then. I learned later.

Senator LEVIN. And who was that?

Mr. WINOKUR. Michael Kopper.

Senator LEVIN. And had you known that, would you have wanted those quarterly reviews to continue?

Mr. WINOKUR. Well, I did not know——

Senator LEVIN. Mr. Kopper was so close?

Mr. WINOKUR. I did not know Mr. Kopper was involved in Chewco. I did not know he was involved in all the things he was involved in, and had he complied with the code of conduct, we would have gotten into that much earlier.

Senator LEVIN. But did you know that he was very close to Fastow?

Mr. WINOKUR. Well, I knew Andy had a bunch of bright people working for him. I did not know that Kopper was any closer to him than anybody else.

Senator LEVIN. But if you had known, if Fastow had told you that he had sold his interest to Kopper, would you have said, "whoops, wait a minute; even though Fastow left, given our relationship with Kopper, we better continue——"

Mr. WINOKUR. Absolutely.

Senator LEVIN [continuing]. Those quarterly reviews?

Mr. WINOKUR. If I had known that the related party relationship continued informally as well as formally, I would have wanted to continue the reviews, yes, sir.

Senator LEVIN. Now, when you did find that out, then what happened?

Mr. WINOKUR. Well, I did not find it out until——

Senator LEVIN. August.

Mr. WINOKUR. No, I found out that he sold. I do not believe that I found out—I do not remember exactly when I found that Kopper bought it. I thought it was actually during the Powers work that I found out who bought it.

Senator LEVIN. That was the first time you learned that Kopper bought it?

Mr. WINOKUR. That is my recollection.

Senator LEVIN. Was it relevant as to who bought his interest? When you found that he had sold his interest, did it become relevant as to whom he sold it, since if he sold it to another related party, directly or indirectly, you would want the controls to continue? Should you have asked who he sold it to? Given that history, should you not have asked who he sold it to is my question.

Mr. WINOKUR. I would have to look back at the August minutes to see what was said by Mr. Koenig about how it was sold. If it was said it was sold to an unaffiliated party, then I would not have thought more about it.

Senator LEVIN. I asked you about whether or not there was an unwritten guarantee that LJM would not lose money in a deal with Enron. Were any of you aware of such a guarantee?

Dr. LEMAISTRE. I was not.

Mr. DUNCAN. I was not.

Mr. WINOKUR. No, sir.

Senator LEVIN. Mr. Duncan.

Mr. DUNCAN. I was not.

Senator LEVIN. I think what we are going to do here is take about a half-hour break. I just want to summarize this one LJM issue, though, before we leave to sort of tidy this thing up.

The things that really trouble me are the lack of real energy and effort by the Board in a situation where you are using accounting methods which are clearly at the margin, high risk. You were so informed early. You know that you are using a lot of off-the-balance-sheet entities, special purpose entities. You are into this whole area. You decide on a compensation review, and despite a decision in October 2000 to do it, you do not do it.

No one ever saw this LJM initial placement memo. I take that back. Your lawyer did, apparently, but your lawyer, when he saw that the conflict of interest is being touted as a reason for investors to buy LJM apparently was not troubled by that. If I understood you correctly, Dr. Winokur, you never asked your lawyer as to why.

Mr. WINOKUR. I did not learn that until my work on the Powers Committee, sir.

Senator LEVIN. Right, but after that, you did not ask your lawyer——

Mr. WINOKUR. Well, I did not have direct contact with Vinson and Elkins at that point.

Senator LEVIN. It is not the kind of active control and responsibility that I think we have to expect of Boards; that's what it comes down to. That is just on LJM, and we will go into Raptors when we come back, but let us take a half-hour break now until 2:30. Thank you.

[Recess.]

Senator LEVIN. The Subcommittee will come back to order.

We now come to the time when the Board dives into perhaps the most dangerous waters of all, and these are the Raptors, the very complex set of transactions that the Board knew about and approved, despite questionable accounting and significant financial risk to Enron.

The Raptor transactions consisted of a series of four complex transactions, each of which involved Enron, LJM2, and various special purpose entities. In each of the four complex Raptor transactions, Enron placed highly volatile shares of stock from companies in which Enron had invested. Enron did this because it had already booked as income the increase in the companies' share prices, and it wanted to protect itself from any loss if these shares dropped in price. And so Enron's goal was to hedge these stocks.

The problem was that no third party would agree to enter into a hedge to protect Enron from a loss on those shares, so Enron used LJM2, set up these special purpose entities, and secured each of the hedges by pledging its own stock as collateral. Through a series of deceptive transactions and improper accounting entries, Enron recorded earnings on its books of about $1 billion, and another $1.2 billion in increased shareholder equity.

If we could take a look at Exhibit 28b.[1] This is the "Hedging Program for Enron Assets," as it is described, that was presented to the Board on May 1, 2000. And if you will look at the last page, where it says "Project Raptor." When you look at the risks cited here, this lists the risks involved here, maybe, Mr. Winokur, you can explain this.

Mr. WINOKUR. Senator——

Senator LEVIN. First of all, did you remember this before——

Mr. WINOKUR. Yes, sir.

[1] See Exhibit No. 28b which appears in the Appendix on page 306.

Senator LEVIN [continuing]. When you were talking to our staff, did you remember this?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. Details of this? OK. Do you want to explain——

Mr. WINOKUR. To the best of my recollection, I did.

Senator LEVIN [continuing]. What you were told back on May 1 about the risks of Project Raptor, looking at those bullets?

Mr. WINOKUR. Sir, it was Enron's staff practice when they presented an item for recommendation and approval always to describe the risks of the transaction. Every transaction obviously has risks and they would set them forward, and for each risk, they would have a mitigant. In other words, the idea was, this was a risk, they had already thought about it, and here is how they dealt with the risk.

And in this case, one of the risks of a complicated structured finance transaction like this was that it would not be properly able to be accounted for, and the mitigant was, and the minutes suggest or support this, as well, that Rick Causey, the Chief Accounting Officer, and Andersen had been involved—in fact, Enron paid Arthur Andersen a fair amount of money for helping to structure this transaction so that it would conform to the accounting requirements, and so that mitigant meant that the accounting scrutiny had been dealt with.

Obviously, any time there is a hedge, there is a risk that the hedge does not work, and the mitigant there, if the hedge did not work, was to terminate the program. And, in fact, as I believe I have said here in the House, in the Powers Committee report, it says had the Raptor transactions been terminated in the first quarter of 2001 when it was clear they did not work, as opposed to their having been restructured without Board approval, I do not think, personally, Enron would be in the position it is in today.

"Counterparty credit" just means that you have to have enough credit in the structured transaction to be able to execute the hedges you propose.

Senator LEVIN. Now, first of all, what was your understanding of the words "accounting scrutiny"? Does that mean that it might not have complied with Generally Accepted Accounting Principles?

Mr. WINOKUR. No. That meant to me that it was important to make sure that the transaction was structured in a form that would pass accounting muster, and because Arthur Andersen had been paid to help work on the structuring and Rick Causey said they were comfortable and he was comfortable with it, that meant that risk was mitigated.

Senator LEVIN. Did the Board understand that this was a true hedge?

Mr. WINOKUR. Well, I did, and I believe everybody did.

Senator LEVIN. If you believed it was a true hedge, why would there be any risk to Enron?

Mr. WINOKUR. Well, Senator, we contributed unrealized gains on forward positions in the stock. In other words, we had an asset that had not previously been in Enron's income statement and we used that in contributing it in this structure as credit support for the hedge. So any time—if we contributed Exxon stock and the

Exxon stock had gone down, that would have been the same issue. We would have terminated the hedge.

Senator LEVIN. But my question, I think, is a little different, which is that if it were a true hedge, if you had gotten a third party to take that risk, your own stock would not have been at risk, would it?

Mr. WINOKUR. It depends on the structure of the hedge.

Senator LEVIN. If it is a true hedge.

Mr. WINOKUR. Well, as I said, in my example——

Senator LEVIN. Do you not transfer the risk to someone else in a true hedge?

Mr. WINOKUR. Well, you transfer risk, but if for some reason the hedge does not work, then it terminates, and that is what I said in my example. If Enron had contributed Exxon stock and Exxon stock had gone down, the credit capacity of that vehicle would have not permitted it to be viable, and so in this case, instead of Exxon stock, we used unrealized gains in forward positions on Enron stock.

Senator LEVIN. Did the Board understand that Enron stock would be at risk under some circumstances here?

Mr. WINOKUR. Yes. In fact, we——

Senator LEVIN. At the time of this deal, you realized that there was still a risk to Enron?

Mr. WINOKUR. Well, we had a large unrealized gain in these forward contracts, so we understood that realized gain would be at risk. That was part of the structure.

Senator LEVIN. If, in fact, the stock price went down and the unrealized gain disappeared, did the Board understand that then Enron would have to—that Enron stock itself would be at risk—not just the gain, but that Enron stock would be at risk, that you were not transferring the entire risk to a third party? Did the Enron Board understand that, or did the Enron Board believe that you were transferring that risk to a third party?

Mr. WINOKUR. If the assets that were being hedged went up in value, then if the forward position was in decline, it would not have mattered, or vice-versa.

Senator LEVIN. Yes. Now we are talking going down.

Mr. WINOKUR. The bad outcome was that both the assets and the forward position went down, that is, Enron stock went down and Avici or whatever stock was hedged, and in that case, which is exactly what it says here, program terminates early in negotiation of an early termination agreement. So this was contemplated as a possibility.

Senator LEVIN. The Board understood, then——

Mr. WINOKUR. That this possibility could occur.

Senator LEVIN [continuing]. That Enron stock was being pledged as collateral?

Mr. WINOKUR. No, forward positions on Enron stock. It is a derivative instrument.

Senator LEVIN. My question is, did they understand that Enron stock itself was being pledged as the collateral?

Mr. WINOKUR. Well, my recollection is, and I could look back at the previous page, was that forward positions were being pledged. That is my recollection.

Senator LEVIN. Then the answer to my question about Enron stock being pledged as collateral?

Mr. WINOKUR. We put seven million—from the previous page, we put stock in and we wrote—well, here, I think this was forward positions, even though it says that—Senator, I am looking at the diagram here. I do not have from 2 years ago the specific terms.

Senator LEVIN. Let me——

Mr. WINOKUR. I believe that it was forward positions on the stock as opposed to the actual shares.

Senator LEVIN. Forward positions on stock that Enron held in other companies?

Mr. WINOKUR. No, that Enron was contributing unrealized gains in its own stock as credit support to get this structure organized. This structure could then purchase stock in some other company——

Senator LEVIN. Let me try to ask the question, because it is an important question. Did the Board realize that Enron stock was being pledged as collateral for the hedge?

Mr. WINOKUR. I can only answer for myself.

Senator LEVIN. You cannot give me a "yes" or "no" on that?

Mr. WINOKUR. My recollection is that we were using forward—unrealized gains in forward contracts. That is my recollection.

Senator LEVIN. Therefore, the answer is you did not realize that Enron stock was being pledged as collateral for the hedge? If that is not your answer——

Mr. WINOKUR. My recollection is just as I said, which is I believed that we were using forward contracts, unrealized gains in the forward contracts. That is my recollection.

Senator LEVIN. Why is that not then a simple, "no," that you did not realize that Enron stock itself was being pledged as collateral to obtain that hedge?

Mr. WINOKUR. I do not recall that Enron stock specifically was being pledged——[1]

Senator LEVIN. OK.

Mr. WINOKUR [continuing]. Over and above the forward positions.

Senator LEVIN. That is good. Now, let me try to put this in a slightly different way. What did the Board understand to be the risk to Enron at the time it approved these transactions?

Mr. WINOKUR. The risks that were presented to us were, first, that the structured finance vehicle might not be structured in a way to meet the accounting rules, and that was mitigated, we were told, because Arthur Andersen was involved and Rick Causey approved it.

And second, we understood because of the forward positions in Enron stock that credit capacity could go away if, in fact, Enron stock went down, in which case the Raptors would have to be terminated.

Senator LEVIN. Did you understand, then, that if Enron stock fell in value, that you would have to put up large amounts of Enron stock in order to pay off the guarantee to others who were willing to——

[1] See Exhibit No. 80 for clarification which appears in the Appendix on page 665.

Mr. WINOKUR. No, sir. I understood that we would have to terminate the arrangement because the credit capacity would fall.

Senator LEVIN. OK. Now, when you were shown Exhibit 32,[1] you asked for this, as I understand it, Mr. Winokur, the "Stock Price Risk in Financings"—you asked for a chart showing what would happen if Enron's stock kept falling in price. You asked the management for this.

Mr. WINOKUR. Yes, sir.

Senator LEVIN. And by April, Enron stock had fallen from $80 to $60, and this shows what would happen if it fell to $40. It lists four deals, Osprey and three of the Raptor transactions, and shows that Enron would have had to come up with another 45 million shares of Enron stock to pay these entities. Now, were you surprised by what you saw?

Mr. WINOKUR. Well, I appreciated being provided the information I had requested.

Senator LEVIN. But were you surprised when you saw that your stock was on the hook to this extent? Did that surprise you?

Mr. WINOKUR. Actually, sir, what I read into this was Enron had about 800 million shares outstanding at this point. So what this chart said to me is if the stock price falls by another third from where it is, and at that time, I think that was not considered a probable event, Enron would have to issue approximately less than 6 percent additional shares. So the dilution to the existing shareholders to top-up these vehicles would have been around 6 percent if the stock fell by a third.

Senator LEVIN. And you were not surprised that your risk was that great in the Raptor transactions? That did not surprise you when you got that chart?

Mr. WINOKUR. Actually, I thought that a 6 percent dilution matching against a one-third decline in the stock when the stock was not considered to be overvalued at that point, or not particularly—I do not recall the specifics—was not maximal dilution.

Senator LEVIN. OK. You recognized that impact on Enron, the dilution of its stock which would result from the Raptor transactions if Enron's stock value went down, and that did not surprise you? You realized there was that great a risk in the Raptor transactions to Enron? That is all I am asking.

Mr. WINOKUR. Senator, in addition, I would like to make the point that the fully diluted shares in the EPS calculation, Enron used a model to include these kinds of results in the fully diluted share calculation, so that the additional shares already were disclosed in Enron's disclosure documents and already were included.

Senator LEVIN. When the risk was supposedly transferred, which was the purpose of those transactions, Enron maintained some significant risk, and you are telling me the Board was not surprised by that retained risk in Enron. Even though it was informed that this was a hedge transaction to transfer that risk to others, you are saying that the Board understood the extent of the risk to Enron that was left following the Raptor transactions, is that what you are telling me? They understood this?

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[1] See Exhibit No. 32 which appears in the Appendix on page 334.

Mr. WINOKUR. Sir, the handwritten note, which is a little hard to read, says, "Assumption: The value of the other assets," it looks like it says, "were zero," so I viewed this as a worst case scenario. In other words, the assets that were supposed to be hedged went to zero, and I did say earlier that the one bad outcome is the assets that were being hedged and the Enron forwards both went down. So worst case, the other assets are not worth anything—I think that says zero, the best I can read it—and even in that extreme case, Enron stock goes down a third and all the assets we put in these vehicles are worthless, there is only 6 percent dilution and it has been fully disclosed. I do not think that was a good outcome. I also did not think it was a very probable outcome.

Senator LEVIN. My question is neither whether it was good or probable. My question is, did the Enron Board understand when it was hedging a risk that it was maintaining a risk to that extent, whatever the extent is? Did it understand that?

Mr. WINOKUR. Well, we assume, because in the previous exhibit——

Senator LEVIN. Can that not be yes or no? Did it understand that it was maintaining a risk to this extent under the circumstances that you just outlined?

Mr. WINOKUR. We understood that if the credit support we provided for the vehicle was inadequate, the vehicle would have to be terminated early. That was part of the presentation when we approved Raptor.

Senator LEVIN. All right. And is not the shorthand for that, the Board understood that Enron was retaining a risk under the circumstances that you just outlined?

Mr. WINOKUR. A risk, yes, sir.

Senator LEVIN. And this shows the extent of the risk under various circumstances.

Mr. WINOKUR. Under extreme circumstances.

Senator LEVIN. It turned out not to be so extreme.

Mr. WINOKUR. Yes, sir—what were thought to be extreme circumstances at the time.

Senator LEVIN. And I just want to ask the other Board members, did they understand that this was not a hedge where the risk was transferred, but that a risk was retained to the extent that Dr. Winokur just outlined? Did you understand that, Dr. Jaedicke?

Mr. JAEDICKE. Yes, I did, sir, because that hedging strategy is explained in the annual report and had been used in Enron on many transactions. They are typically referred to as something like low-correlation hedges.

Senator LEVIN. On this chart, I think it is Exhibit 27 in your books,[1] when you look at that chart, we see that the payments by Enron to LJM2 for the Raptors were $197 million. That is up at the top. Do you see that number?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. And the loss to Enron is at the bottom, $710 million. That is the outcome of this. LJM got $197 million. Enron lost $710 million on that transaction. Would you agree with that summary, Dr. Winokur?

[1] See Exhibit No. 27 which appears in the Appendix on page 300.

Mr. WINOKUR. Well, I would like to ask Dr. Jaedicke to talk about the reduction in shareholders' equity, but as far as the losses, I do not know where these—I have not seen these numbers before, obviously. The Powers Committee had some numbers in them that were prepared by the Deloitte people. Those were not other than very rough estimates and the Powers Report specifically said that would assume that Enron had taken no other action and there is nothing else going on. In other words, it was a number that is just pro forma, add this and subtract that. It is not a number that has any, at least in the Powers Report, had any backup that was provided.

Senator LEVIN. Now, this is a number from the Powers Report.

Mr. WINOKUR. As a member of the Powers Committee, I specifically said in my testimony in front of the House that the accounting consulting help that we got was not reviewed by Deloitte and Touche and did not have any independent verification of it and did not assume that Enron would have taken any other action in the interim.

Senator LEVIN. All right. Going back to the $710 million, this is what Enron put in its SEC filing.

Mr. WINOKUR. Yes, sir.

Senator LEVIN. So can you accept that?

Mr. WINOKUR. Yes, sir.

Senator LEVIN. OK. So Enron showed a reduction in earnings due to Raptor termination of $710 million. The $197 million was made by LJM2. That is the outcome, and I am just saying, do you differ with those numbers?

Mr. WINOKUR. I do not have any disagreement with that.

Senator LEVIN. Would you acknowledge today that the Raptors were, in hindsight, a disaster for Enron?

Mr. WINOKUR. Sir, what I would say, and I said, I believe, in my statement this morning, if management had come to us in the first quarter and said the Raptors did not work, it was a great idea, but it did not work and we want to cancel them, Enron would have taken then something like a 50-cent a share charge. Mr. Skilling told the Powers Committee he did not think at that time, in the first quarter of 2001, that Enron stock would have been affected materially because lots of companies were writing off high-tech, broadband, and other kinds of investments.

So had the Raptors been terminated early, which is what we thought would have happened in May 2000 when we approved them if both the assets and Enron's forwards went down, we would have had a loss. It would have been a large loss, $400 or $500 million, but it would have been manageable by Enron. And the fact that the $800 million of additional stock was contributed and the Raptors were restructured without Board approval also gave rise to the accounting error that led to the equity write-off, and as I said this morning, I think that combination turned out to be a very bad thing.

Senator LEVIN. If a real third party had participated in the hedge, would the outcome have been different?

Mr. WINOKUR. Well, I do not know the answer to that except for one thing, and that is a real third party would not have been able, presumably, to restructure itself without Board approval in the way that this happened. We were not told of the restructure.

Senator LEVIN. OK.

Mr. WINOKUR. And LJM2 had many outside investors. It was a real third party. It had a related party as an investor, but it was a creditworthy third party when we dealt with it.

Senator LEVIN. You have seen a number of red flags now along the way, starting as early as 1999, February 1999, where it was stated that Enron's accounting was pushing limits. We have seen the various ways in which fund flows were generated to move assets off the balance sheet with Whitewing, with LJM, with Raptor, and the losses that were caused here. Then we see a steady decline, we saw in that earlier chart, of Enron's stock from which it is not going to recover.

During this time, the Board saw no red flags at all, no sense of trouble that lies ahead until mid-October 2001, and that is when you learned that Enron would take an equity write-down of $1.2 billion. That was the first time you testified that you saw any sign of trouble. We have demonstrated, I think, plenty of signs, but nonetheless, the Board did not see those signs.

But a number of people associated with Enron did see the writing on the wall well in advance of the announced write-down, even if the Board did not. One example is a senior Enron executive who left Enron in September 2001, and despite an effective separation date of November 2001, this individual sent a series of E-mails to his stockbroker about selling Enron stock. So this is September 2001.

Here is what he said on October 2, a few weeks before Enron's problems became public, and this is Exhibit 33a,[1] if you wish to follow along. This is a senior Enron executive now. "I think we may want to sell some Enron calls in the next few days before earnings are released. I don't know anything, but I know how Enron works and I am sure they will be able to show strong recurring earnings, . . . and do some housecleaning on some non-productive assets." So he says he knows how Enron works and will show some strong recurring earnings, and again, this is additional evidence suggesting that Enron management was deliberately engaged in earnings management.

Then on October 4, the same person writes, "I think we should begin thinking about shorting January calls on, say, 100,000 shares at or near the money. . . . There are a number of analyst reports out that are really trying to push up the stock and with a little help from the market, they may get a few more points out of it over the next few days." Then later the same day, he writes, "I believe [Enron] stock has limited upside in the near term and, in fact, has some downside exposure."

Now, this is a pretty strong statement given the fact that the stock had already fallen from $90 to about $30 a share at the time that he wrote these E-mails. His comments are deeply troubling. This is a senior officer at Enron, not yet separated when he begins selling calls, and a few weeks later, Enron took a $800 million earnings hit and a $1.2 billion reduction in shareholder equity. We

[1] See Exhibit No. 33a which appears in the Appendix on page 335.

cannot release the person's name at this time. We are still looking into the matter. But if the facts bear it out, we will be recommending to the SEC that they open an insider trading investigation with regard to this individual.

But in terms of what he knew, what he saw from the inside, which you did not see until later, I am wondering whether you have any comments that you want to add. Does anybody want to add any comment to that?

[No response.]

Let me ask you about Ken Lay's loans. Let me ask Senator Carper before I get to that.

Senator CARPER. Thank you, Mr. Chairman. We appreciate your patience and your sticking with us into this afternoon.

Dr. Jaedicke.

Mr. JAEDICKE. I am sorry, sir. I was not paying attention.

Senator CARPER. That is all right. I understand from the introduction today that you ran the business school at Stanford? Did you?

Mr. JAEDICKE. I was Dean of the business school.

Senator CARPER. You were the Dean of the business school. When I was in the Navy, we were stationed at Moffett Field, California, not far from where you used to hang your hat, and I lived in Palo Alto and Menlo Park. In fact, I lived on Santa Cruz Avenue, right up against the Stanford golf course, and I remember as a younger man going to—I am not Catholic, but I remember going to a lot of folk masses on Stanford at the campus on Sundays and very much enjoyed those. I have good memories. One of my best friends, my roommate for part of the time I was in the Navy out there, ended up going to the Stanford business school, I think at the time that you were running it, and from time to time, we talked about case studies in different businesses, some that did well, some that did not do so well.

I think we have got a classic here that the business schools, I do not know about Stanford, but certainly a lot of them will come back to this one time and again to figure out how they got into trouble and how a company thought to be as successful and as mighty as Enron could tumble so quickly.

How would you describe it to the next generation of business school students at Stanford who say, this is what happened and this is how they got into this mess and why they could not get out of it? How would you describe it?

Mr. JAEDICKE. I think, first of all, you would have to say—you would have to indicate that there was a lot of incomplete information floating around—well, I would not even say floating around, reported, that a lot of the reports were not accurate, that some of them were misleading in terms of how good things were or how much things had been looked at.

I think you would have to say this is a classic case of having lots of overlapping controls, which I said in my statement, involving lots of different people, trying to get very good advisors, trying to cope with the problem—the classic problem that all boards have if you are supposed to monitor management and management provides you the information. What do you do? You put in place the best controls you can think of, and these did not work.

Then I suppose you could back off and say, well, why do you think they do not work? We will describe to you the situation and then you, as students, tell us why you think they did not work. That is kind of the classic case, I guess, to get them to confront that problem. I am not sure that I would have any answers for them other than the integrity of the people and so on that were supposed to furnish information to us. It was not always what I would want it to be.

Senator CARPER. We talked earlier about whether or not we can legislate character or legislate integrity and I think we pretty much agreed that is a hard thing to do. I did not, but I might have gone on to say some folks who looked at the situation have suggested that while the Congress cannot legislate integrity or character, one of the things we can do is to pass laws that call for punishment for people who break our laws. The Congress, it is not our responsibility to prosecute and to convict those who have done so, but as you know, with our system of government, we pass the laws and then we leave it to the Executive Branch and the Judiciary to ensure that the laws we passed are enforced.

One of my hopes of what is going to come out of these hearings, and we thank you again for joining us, is that the anger, the frustration that so many Americans feel—and you have heard it and you have felt it, certainly we have—will be transformed into ensuring that justice is done in these instances.

If I could sort of segue from there, Mr. Chairman, for just a moment, we are going to have, I think, a second panel, I hope later today, with some very knowledgeable people who know a thing or two about corporate governance who are going to, I do not know that they are going to second-guess you, but they are going to come in and certainly give us their perspective.

I just want to ask you a couple of questions, and I hope to be able to ask that panel. One of those deals with the independence of board members and what we can do, given your experience on this Board and other boards that you have served on, what can we do? This is for anybody on the panel. What can we do? What ought we do to better ensure, not just we in the Congress, but we collectively, to ensure that members of boards of directors have the kind of independence that will better ensure that they make decisions that represent the interest of the shareholders? Anyone?

Mr. BLAKE. Senator, I think that I would like to respond to some of the comments that were made this morning, I, frankly, agree with. I think there has to be scrutiny relative to what extent of involvement a member or director has on a board with a company and to assess whether that could, in fact, present a conflict of interest situation, in other words, too much vested interest in the relationship with the company such that it cannot be—that person cannot be independent or dispassionate about decisions that need to be made.

I think, also, that in this case, this Board actually percentagewise has a relatively high level of independent directors on its Board and I think that is a good thing. There is probably a rationale to have some inside directors, particularly as it relates to continuity and succession of management. It is very common, for example, when one CEO was leaving and there may be a COO or something of that nature, where you want to give exposure of that potential successor to the board and to have that individual participate in the board. There is real ample justification, perhaps, of having, say, two, particularly in light of the succession situation. Otherwise, I would be more inclined to suggest that just the CEO should be a member, except for the isolated situation.

Senator CARPER. OK. Other thoughts on board independence? Other comments from any of you with respect to board independence, steps that need to be taken to better ensure board independence?

Mr. JAEDICKE. Senator, I suppose you could give the simplistic answer and say, well, you could pass legislation or come up with regulations that would say you cannot have a consulting arrangement. There is a trade-off here. It is disclosed, it is controlled, but Mr. Urquhart, for example, was an expert in the—ran the power division of GE. I am sure he gave us a lot of help overseas. It is like—I suppose you could say, well, maybe that individual should not serve on the Board. Well, the question is, can you get him?

I do not know how to—I realize that this is my personal answer, and it is just an opinion. Free enterprise is great because it is free. Now, if you want to impose constraints on it, there is always a trade-off. I am not going to tell you that you should not impose some constraints because maybe your assessment of those trade-offs is different than mine. That is what makes a system work, I guess.

Senator CARPER. Let me just interrupt. I do not mean to be rude——

Mr. JAEDICKE. I do not know how to answer this.

Senator CARPER. This is not a trick question. We have got a lot of wisdom represented at this witness table and this is an issue we are going to deal with, and we can make wise decisions or unwise decisions, and if you have some thoughts, just share them with us from your heart.

Mr. JAEDICKE. I guess I do not understand what you are asking me, sir.

Senator CARPER. Anyone else? If not, I could restate the question.

Mr. DUNCAN. Well, I will try that. I agree that every board member should be independent. Those that are not 16(b) officers should be totally independent, period. That, I agree to.

I would think that a board could do something like we did, and that is have an annual board appraisal, and in that board appraisal have items that would lead one to conclude that member is independent. Now, how you write the textbook on that would take some time.

Senator CARPER. Anyone else?

Dr. LEMAISTRE. I have wondered a great deal about the rotation of directors. It seems to me that during service on a board, it takes a good while to get acquainted with the business, especially for a physician. I can tell you that after a period of time, it would seem to me that a rotation would serve to give an indoctrination period to others coming on so that they could learn to be fully effective while over two-thirds of the board would be experienced. But it is just a thought. I do not know whether boards do that or not. We did not do it at Enron. I did discuss that with some of the 16(b) officers as a possibility.

I also feel that in the board's self-evaluation, there has to be action taken and there has been action taken in the Enron Board.

Senator CARPER. You say there has?

Dr. LEMAISTRE. There has been when a Director was not found to be effective in representing the shareholders.

Senator CARPER. Dr. Winokur.

Mr. WINOKUR. Sir, my colleagues are knowledgeable and, I think, articulate about this subject. I would just say that Enron's Board was voted one of the five best in the country 2 years ago—because I still have the plaque somewhere in my office.

Senator CARPER. Hold on to that. [Laughter.]

Dr. LEMAISTRE. But more importantly than that, we did go through a self-evaluation process and we attempted to conform with the best practices that the General Motors Pension Fund and all of the other governance entities did. So I think that independence is important, and I think a board that tries to improve itself all the time is important.

Senator CARPER. Thank you. Mr. Chairman, I do not want to go on too long. Do I have time for one more?

Senator LEVIN. Sure.

Senator CARPER. What kind of future, if any, is there for Enron coming out of bankruptcy? What do the folks who are involved in still holding shares or the people who are the employees or were the employees who have the shares in their 401(k)'s, what do they have to look forward to?

Mr. BLAKE. Senator, not very much, unfortunately. I think the jury is still out, but as represented by the recent 8(k) filing for the write-down that I believe Senator Levin mentioned in his comments this morning, there is an imbalance, obviously, in terms of claims against the estate and assets. We have already stated earlier that there is no specific value and current equity of Enron.

As it relates to employment as contrasts with perhaps an investment in Enron stock, the Board, Pug and I and the Board approved an organizational plan which we presented to the Bankruptcy Court last week called OPCO, which basically takes the traditional assets of the company, pipeline investments, power generating investments, and things of that nature, within which there is some level of synergy and relationship to the component makeup of that entity. It is hopeful that we can, essentially, try to sell these various business interests into and through a trust with something they call a 363 sale. The sale out of bankruptcy of these assets in a trust would take place whereby all the claims against the estate would be set aside, until such time that this OPCO company could then go operate as a stand alone ongoing business.

And the view, with which I personally agree, is that the ongoing value of the company is better than break up or liquidating value of assets. Enron is one of the more efficient gasline, pipeline suppliers and operators in the country. It is one of the lowest cost producers. Its reliability is one of the best in the industry. So there is real value and there are great people in that business.

So the hope is that we will be able to take this collection of assets called OPCO, have it purchased out of bankruptcy into a trust, and as such there would be employment for those employees and a livelihood to go forward, as contrasts with perhaps liquidating those assets. Otherwise, I think there are many assets that will be liquidated, and I do not want to get too far into discussion on that, but there are a lot of claims still out there and a diminishing level of assets, unfortunately.

Senator CARPER. All right. Thank you.

Mr. BLAKE. You are welcome, sir.

Senator CARPER. Mr. Chairman, do I have time for one more?

Senator LEVIN. Sure.

Senator CARPER. Just imagine for a moment that you were not sitting there and meeting the responsibilities that you now hold in your lives but you sat up here and you wore our hats for a while. Let me just ask each of you, if you were in the role of a member of the U.S. Senate, can you think of one thing that you would do, whether it is with respect to corporate governance or the role or responsibilities of the accounting firms and the way they are managed or governed, or 401(k)'s, one thing that you think needs some legislative action, needs to be addressed legislatively, not just the marketplace forcing the changes, compelling the reforms, not just the SEC, not just the Federal Accounting Standards Board, but something that we need to do, could you give me an example, each of you, just one example of something that the Congress needs to do to better ensure that this sort of thing does not happen again?

Mr. BLAKE. First of all, I think the comment was made earlier by some of my colleagues this afternoon, this morning, disclosure. Truth does not hurt, and the more disclosure the better, as far as I am concerned. That, frankly, is the governing mechanism of off-balance-sheet transactions, is the requirement of disclosure, the adequacy and completeness of disclosure. I think that is a practice that probably could be extended beyond where it is today, personally.

I do think there is an accountability that CEOs like myself have in terms of being honorable to my position and should be accepting of the consequences if I were to misbehave or I have proven to have been involved in a wrongdoing. Frankly, I think, personally, having such an act that would suggest criminal liability, if that was—it is a gray area in terms of negligence and whether there was really intent to deceive, but if, in fact, there was an intent to deceive and, in fact, it was a fraud and that the leader of that company was responsible for perpetrating that fraud, I would hope that there would be a criminal action against that individual.

Senator CARPER. All right. Thank you.

Mr. BLAKE. That has no application to Enron. It is just a philosophical statement.

Senator CARPER. I understand. Thank you.

Dr. LEMAISTRE. The company's most valuable asset is its employees. I think the 401(k) should be managed by the employees, but there should be some oversight to correlate with the top management, the CEO, and the board so that you can be sure that those employees who are managing the fund know fully what the condition of the company is, especially with regard to stock. But that does not happen. At Enron, there is no fiduciary responsibility of the Compensation Committee nor any management responsibility.

Our only responsibility is to amend the original plan when amendments are required.

Senator CARPER. Thank you, sir.

Mr. JAEDICKE. Sir, I do not know that I could answer your question. I have been so busy that I do not really think I know enough about the public policy to say what you should focus on. I have no disagreement with what my colleagues have said here, but I am just really not well enough informed on this whole process to suggest to you anything other than something off the top of my head.

Senator CARPER. If something comes to mind and you would like to share it with us later——

Mr. JAEDICKE. I certainly will.

Senator CARPER [continuing]. We would be delighted to have it.

Mr. JAEDICKE. I certainly will, and I promise you I will think about it, and if I think I can pass along anything that would be of any help to you, you will hear from me.

Senator CARPER. Thanks so much.

Mr. WINOKUR. Senator, this is not meant to relate to Enron, because I do not think it would have—I do not think it is particularly applicable, but I think, going forward, I would find it very helpful—we talked about it a little bit earlier—if the whole issue of stock versus performance options versus stock options could be simplified and clarified and made people as agents, because employees are agents for the shareholders, made their incentives more closely tied. There are many people, including the chairman, who have thought a great deal about that. I do not have the specific proposals. But the more there is disclosure and the more the incentives are aligned with the owners, the better things will be.

Senator CARPER. Thank you. Mr. Duncan.

Mr. DUNCAN. Senator, I agree with what my colleagues have said. The only thing that I would add is that the world goes on at a faster and faster speed. As the Internet comes into play in bigger and bigger portions—most of the SEC Act was, what, 1933 or something like that—as that comes into play and derivatives come bigger and bigger into the world, and a cashless society becomes a totally cashless society, the rules might have to be a little different as you move into that. I do not think that they are overdue, but I think they will be due.

Senator CARPER. All right, thanks.

Mr. JAEDICKE. Senator, can I make one comment that may sound a little facetious, but he reminds me. I do not really believe it is facetious. It seems to me that one of the things—I do not think management would like this very well because it may disclose things that really are not vital to the investment decision but would give away trade secrets or financing secrets or something like that—I have this vision in the back of my head as an accountant that the way to deal with the disclosure problem is do away, eventually, in this information age, with the annual report and just send everybody a compact disk.

And on that compact disk would be all kinds of information, and then you could maybe imbed in that—now, this sounds harebrained, but I do not think we are too far away from some of these things—the software that would say, off-balance-sheet does not mean out of the statements. What it means is you have disclosures in different places than the balance sheet and the footnotes. One of those footnotes would be—you were worrying earlier about the assets that are off the balance sheet and in the non-consolidated subsidiaries.

I am sure even I could give you a piece of software so that you could say, well, here is a statement that is according to GAAP now, but those subsidiaries are not consolidated. I would like to see them consolidated. That would be like falling off a log. And then you can see all of the assets that are in that footnote. That would be the idea.

Now, I realize that is kind of hare-brained, but my colleague has reminded me——

Senator CARPER. That is a great idea.

Mr. JAEDICKE [continuing]. That we are in a new age.

Mr. DUNCAN. And it would also save the company money.

Senator CARPER. Mr. Chairman, years from now when it is time to send out those annual reports and we open up our mailboxes and out of them fall these CDs, we will know where the idea came from, right here on this day.

Mr. JAEDICKE. Thank you.

Senator CARPER. Thank you all. Mr. Chairman, thanks.

Senator LEVIN. Let me get back to Ken Lay's loans. In May 1999, the Enron Compensation Committee told Ken Lay that—and by the way, Senator Carper, because you were inquiring, I think, in a very gentle way, I should be done in about 10 minutes, in case anyone else is trying to plan a schedule, too. [Laughter.]

I want to take just a moment, though, on Ken Lay's loans. The Compensation Committee told Mr. Lay that he could repay his company loans with stock in May 1999. At that time, he had a line of credit with Enron of about $4 million, and that was raised to $7.5 million in August 2001.

But in a 1-year period, from October 2000 to October 2001, Mr. Lay began using an "ATM approach" to his Enron credit line, as one Board member put it in his interview. If you look at Exhibit 36,[1] Mr. Lay repeatedly withdrew the entire amount available, and then repaid the loan with Enron stock. First he did this about once per month, and then about every 2 weeks, and then on some occasions several days in a row. By the end, he had obtained $77 million in cash in exchange for his Enron stock.

Now, every Board member acknowledged to us that these transactions could fairly be described as stock sales. By characterizing them as loan repayments, though, Lay was able to bypass the rules for quarterly disclosure of insider stock sales and was able to delay reporting his stock transfers until the end of the 2001 calendar year plus 45 days. All the Board members told us that they did not know that this was going on at the time, and they were shocked to learn of it later. The facts suggest, and your reactions suggested, that Ken Lay was abusing his line of credit.

First of all, do you agree that he was abusing his line of credit? Dr. LeMaistre.

Dr. LEMAISTRE. May I comment on that in two ways. First, just from what I have seen of the records, this is very unusual behavior.

[1] See Exhibit No. 36 which appears in the Appendix on page 350.

This is very clearly a different pattern from what occurred in the previous years.

Second, the loans were characterized as a line of credit and that interpretation needs always in the future to be clarified. I think it is a very important point.

The third thing is that we found out about this only this year. I believe it was February when we finally learned of this, primarily because of the point you made, Mr. Chairman, and that is the disclosure does not come periodically forward to the Board or to any other Federal agency or the SEC.

So the surprise that occurred here was one that really concerned all of us greatly without any understanding of why it was necessary. The only comment ever made to me personally by Mr. Lay was that he had found the previous loan useful and that he would like to have the loan increased to $7 million. Checking with Towers Perrin, I found that was a mid-line range, that there were loans much higher than that to executives. We had a lot of experience at Enron over many years with loans to executives. We have never seen this before. Therefore, we were very deeply concerned about this.

Senator LEVIN. In your judgment, did this constitute an abuse of his line of credit?

Dr. LEMAISTRE. I think it is subject to another concern. With the confusion over the definition of the terms, you hear terms like "revolver" and all of the other terms that would more characterize this used interchangeably. It is not a term I care to use, but I have heard that term—I think the real problem comes in what is the code of business conduct. One of the lines in the Enron code says you will do nothing to hurt the interest of Enron, and taking this much money out and repaying it with stock when the stock is declining certainly is very devious. It is very difficult for me to understand why that did not hurt Enron.

Senator LEVIN. You are stopping a little short of saying that it was an abuse. Is that intentional?

Dr. LEMAISTRE. It was intentional, yes, because I do not know the circumstances.

Senator LEVIN. Does anyone else have a comment on that?

[No response.]

OK. Dr. LeMaistre, let me just ask you this. Whose job is it to monitor and stop that from happening? Whether you call it an abuse or short of that—I think it is an obvious abuse, but you say that you were concerned, dismayed—but in any event, whose job was it, if not yours and your Committee, to monitor that particular activity of Ken Lay?

Dr. LEMAISTRE. There are three points in this. The Treasurer receives the request and disburses the money. A lawyer in the General Counsel's office receives the stock back and it is registered with the person who then must make the filing, unfortunately, 45 days after the yearend.

To correct that, some kind of quarterly reports will be needed. If the CEO has the loan, the report should come directly to the board by the people who handle the transations.

Senator LEVIN. But looking back at this now, you do not feel that you had any responsibility to monitor this?

Dr. LEMAISTRE. We had never had any responsibility to monitor this.

Senator LEVIN. Does anyone else want to add anything to that?

Mr. BLAKE. Senator, I would. I do not want to go close to the word "abuse," but I would say that as a CEO, it is not what you say, it is what you do. Sale of a stock in the nature that took place was inappropriate. And, I also personally feel as a member of the Compensation Committee that I agree with everything that Mickey said, that we did not know about this until February of this year. I was absolutely shocked by this. And I would suggest that if we had a chance to have known that occurred, we would have taken immediate and corrective action to ensure that behavior would not happen again.

Senator LEVIN. See, what I would hope for would be outrage.

Mr. BLAKE. Well, I can use that, too.

Senator LEVIN. Good. That is what we would hope for. I have not felt it.

Mr. WINOKUR. Senator, it would be impossible to feel anything other than outrage, given the amount of money that was lost by the employees, the amount of jobs that were lost——

Senator LEVIN. I did not hear that. I gave you all a chance to comment. I said, is it an abuse? Dr. LeMaistre would not go that far. I am glad to know that once I used the term "outrage," that at least that resonates, because I have got to tell you, I did not sense outrage here.

Mr. BLAKE. You have got it.

Senator LEVIN. I have got it, OK. Good.

Mr. WINOKUR. This made me very angry when I heard it.

Senator LEVIN. Good. I am glad, and I wish that was transmitted.

What stands out here, this is perhaps a harsh thing to say, but I must tell you that we have learned a lot today in terms of information, but what really stands out to me is the denial of any responsibility on your part—for what happened to Enron. A highly-paid Board not taking any responsibility for the events at Enron, with a management that was just management gone wild. That last question was just one of about 20 examples of where we had this swashbuckling management, this arrogant, greedy management that was stuffing their own pockets with the money of shareholders.

What we need in boards are people who are willing to stand up to management. You have got the backgrounds to do it. You have got the experience and knowledge. But what comes out is that you all say you did not do anything wrong, and what I am afraid of is, too often, you did not do anything, period. I mean, there were a lot of warning signs along the way.

You did not hear Andersen say that Enron used high-risk accounting. You did not remember the details of Whitewing as of 3 weeks ago. There was a $2 billion off-the-books vehicle, but no interest in reviewing LJM's private placement memo. When you learned about that memo—this is the memo that was touting a conflict of interest that cost your company that you have the fiduciary duty to protect. It cost your company, that LJM enterprise. It made a lot of money at your expense. There was a conflict of interest that was inherent right in it, because the guy who was selling, or that you were selling assets to, was on both sides of the negotiating table. He did very well at LJM, while Enron and its stockholders were getting socked.

But even after the lawyers told you about it or you read about it in the Powers Report and the lawyers were asked to look at this document, it touts conflict of interest. That is about the only thing you can say. It holds out this insider information that these folks had in Enron while selling partnership interests in LJM. You have not asked those lawyers, my God, how could you not have brought that to the attention of the Board?

You did not press to learn Fastow's LJM compensation for 1 year after you were supposed to look into it. The Board directed that you would look into this compensation. A year goes by. An employee of Enron says she does not have the information, she will get back to you. She does not get back to you. Nothing happens. You read about it in the newspaper.

You did not ask who bought Fastow's interest in LJM, even though LJM meant $2 billion in funds flow for Enron—no inquiry as to who bought that interest. You knew there was something wrong there by then, but still, no inquiry, no questions. No questions about the *Fortune* article.

I do not see any concern about the $27 billion that were represented when half of Enron's assets were off the books. Sixty-four percent of Enron's international investments were underperforming. Forty-five million shares or more of Enron's stock were at risk in the Raptor transactions. It does not set off any alarm bells. This is stuff that you knew.

You did not ask to see Watkins' letter when it was presented to the Board. You got the memo summarizing it, but you did not ask to see that letter itself.

Mr. BLAKE. Sir, I beg to differ. We did ask for the letter.

Senator LEVIN. OK. Did you get it?

Mr. BLAKE. Subsequently, but not right away, yes.

Senator LEVIN. I will stand corrected, then. You got it subsequently.

You really did not know of anything wrong, despite all of that, until the *Wall Street Journal* told everybody something was wrong on October 18 when the world found out. I think that is unacceptable, for a Board to be that out of touch with the reality of their own company. I think you were taken advantage of, too. I think your passivity was taken advantage of—I do not have any doubt of it—by the management.

That placement memo that I made reference to, which has this touting of this insider information at your expense, was issued on October 13, 1999, which was just 1 day after the Board approved LJM2. This is a pretty complicated document here that Fastow put out. It was obvious he assumed that you would approve this 1 day before he put it out. He counted on that approval.

It looks like Enron's Chief Financial Officer saw you as a rubber stamp. It is just deeply troubling to me, because I know you are good people. I have no doubt about the fact that you are individually good people. I do not know you personally, but I know your biographies and I can see that. But this responsibility is placed on the shoulders of good people, and sometimes good people do not carry out that responsibility well.

The shareholders elected you to use independent, tough judgment, to probe for facts, not to accept whatever management gives you. I do not believe you looked hard. I do not believe you asked tough questions. I do not think you considered the personal motivations that prompted related party transactions that ultimately did contribute to your downfall.

We have gone through the warning signs that you knew of. There were many of them. We have tried to go through some of them this morning and this afternoon. As I said, directors are not expected to be detectives. They are not expected to assume that misconduct pervades the highest reaches of management. But they are expected to be more than a rubber stamp for management. They are expected to dig for facts and understand complexities and to say no to transactions that do not look right.

I think the shareholders deserved better than what they got. Too often, I believe you were followers and not leaders, not the captains but followers. The management there had created this corporate culture where anything goes as long as it could produce apparent profits, and those profits that appeared on the financial statement then increased the share price. That was the culture. That was the environment. That rise in stock price, while I am sure gave great pride to members of the Board, failed to stimulate even one Director to consider that age-old truism that if something looks too good to be true, it probably is.

I hope we all learn from the Enron debacle. I hope Congress can pick up some of the points that are learned, whether here or in other committees or in the media or through just investigation, to take appropriate actions to tighten up the accounting standards, to increase independence of auditors, to give the SEC responsibility to require the directors and the auditors to be more responsible to the shareholders.

We have our responsibility. The SEC has responsibility. But the first line of defense against corporate abuse lies with the Board of Directors. There is just no substitute for it. We can pass all the laws in the world and all the regulations can be adopted by the SEC, but the corporate governance responsibility must rest with the Board of Directors. I would just hope that in all areas, whether it is the regulatory area, whether it is the legislative area, or whether it is that area of corporate culture that so badly needs to be changed into a fiduciary culture, from a culture of the share price is a god, to a fiduciary duty is a true obligation, that is the change that has to be made.

You folks have been participants in an experience which I am sure has been painful to you. It is painful to the shareholders of the company that you ran as Directors, and it took a toll on the economic system. But we are hoping that this hearing and this investigation will contribute to some corrections, that they will be common-sensical, that they will be thoughtful, that they will try to avoid unintended consequences. We will keep our focus on what we can properly do and what the SEC can properly do, and just leave to our people of integrity that will be on these corporate Boards the understanding as to that responsibility and that obligation to represent the shareholders and to stand up to management when management gives any indication that they are going in the wrong direction.

We thank you. It has been a long hearing. We thank you for coming forth. As I said, you have done so voluntarily. You have cooperated with us. You have presented what we have asked for with documents. We would greatly appreciate your continuing cooperation, and we will now move to the second panel. Thank you all.

The second panel of witnesses are experts in corporate governance and accounting. First, Charles Elson, Director of the Center for Corporate Governance at the University of Delaware, a leading expert in corporate governance issues; Michael Sutton, the former Chief Accountant at the Securities and Exchange Commission from 1995 to 1998; and Robert Campbell, former CEO, Chairman of the Board of Sunoco, and current Board member of Hershey Foods, CIGNA, and Pew Charitable Trusts.

It is a distinguished panel. We first of all must tell you how grateful we are for your staying with us. I do not know whether we warned you that it might be this long of a wait. If not, I apologize for not alerting you to it, but in any event, we are very grateful that you stayed with us.

As I indicated this morning, pursuant to Rule VI, all of the witnesses who testify before us are required to be sworn, so I would ask you to please stand and raise your right hand.

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

Mr. SUTTON. I do.

Mr. ELSON. I do.

Mr. CAMPBELL. I do.

Senator LEVIN. We will try that timing system again. If you can see these lights, 1 minute before 10 minutes is up, the green will change to yellow. It will let you then conclude your remarks. The written testimony will be part of the record in its entirety, and we will start with Mr. Elson.

TESTIMONY OF CHARLES M. ELSON,[1] DIRECTOR, CENTER FOR CORPORATE GOVERNANCE, UNIVERSITY OF DELAWARE, NEWARK, DELAWARE

Mr. ELSON. Thank you. My name is Charles Elson and I am the Director of the Center for Corporate Governance at the University of Delaware in Newark, Delaware, and the Edgar S. Woolard Professor of Corporate Governance at the University of Delaware. I serve on several commissions of the National Association of Corporate Directors, on director professionalism, director compensation, and various other commissions relating to corporate governance. Additionally, I am Vice Chair of the American Bar Association's Committee on Corporate Governance and a Director of the Investor Responsibility Research Center here in Washington, DC.

I am going to talk just a little bit about the red flags, I think, that were raised for the Enron Board, some of which were talked about today, a little bit about what corporate governance types look

[1] The prepared statement of Mr. Elson appears in the Appendix on page 185.

for in corporate Boards, what factors should be present, we believe, and finally, the problems vis-a-vis the Enron Board in meeting those requirements.

I do not have any knowledge specifically of what occurred within the Enron Boardroom other than what I have read in the press and my comments really will be more structural in nature as to the internal workings. That is something that obviously will have to be developed later on.

There were several flags that came before this Board and one wonders why they were not responded to. First and really most important was the waiver of the conflict of interest policy. That is a pretty extraordinary thing for a Board to do. A conflict of interest policy is laid out for very specific reasons. It lays out what is in the company's interest, what is not in the company's interest, and waivers from a code of ethics is not a very usual occurrence, and that is something that, in my view, at least, should have triggered lots of questions—who, why, when, and where, particularly when the policy was waived vis-a-vis the company's Chief Financial Officer. That is your chief control officer, financial control officer, and it is very unusual to have that officer on both sides of a transaction.

Additionally as a flag, there was a lot of stock selling by executives of the company, again, a flag that apparently was not responded to.

You had, additionally, a number of Directors on the Board who had financial relationships to the company itself, again, not a major flag, but something that should have raised some questions, at least amongst those who did not have those connections.

Finally, vis-a-vis the audit, an auditor, Audit Committee, you had the independent auditor of the company acting as both the internal and the external auditor. That, from a governance standpoint, is questionable. The independent auditor also was taking substantial fees from the company from both audit and consulting work, something, again, governance types should say is not such a good idea.

And finally, there apparently was a bit of a revolving door between the external auditor and the company's financial department, again, a flag, something that should have raised questions, not practices that in and of themselves were problematic, but practices that an independent Board should have been asking questions about and trying to get to the bottom, and had questions been asked, perhaps something might have been avoided.

Now, the next issue is, well, OK, these flags were there. Why were they not responded to? What kind of Board would have responded to it and was this Board somehow deficient structurally in its composition and its procedures such that these flags were not responded to?

Corporate governance types will tell you that the most important aspect of any Board, really two aspects, are that of independence and equity, independence meaning directors serving on the Board with no financial connection to the company whatsoever other than long-term equity ownership in the company, that is, no consulting arrangements, no business connections to the enterprise, no service provision to the enterprise, the only relationship being that of a director who owns equity in the company.

The second important factor is that of equity, that each director should have a personally meaningful equity position in the company itself, that a director should be compensated in stock and that the director should personally invest a meaningful amount, meaningful such that the director is aligned with the shareholder interests rather than managerial interests, the key being substantial equity ownership provides that alignment.

Independence is important for a director because it gives the director objectivity. The director's job is to monitor management for the sake of the shareholders, and independence gives you the effective objectivity to do that monitoring. Equity gives you the incentive to exercise that objectivity, very important.

The two work together. They work in tandem. An independent board without equity is not very good to the shareholders. It may be objective, but there is no incentive to exercise the objectivity. An equity holding board without independence is no good. They may have incentive, but no objectivity.

And independence is actually sort of an interesting concept. It is a two-way concept. Not only is it important vis-a-vis its monitoring aspects or its creation of objectivity, but it is also important within the organization itself, because if the board is viewed as independent of management, an employee who believes there is a problem within the organization is much more likely to contact the board if there are problems. The difficulty with a non-independent board, a board that is seen as just an arm of management, is that complaints rarely reach the level of the board. That is why independence, as I said, is important for two reasons.

Independence and equity are really the hallmarks of a good board, and that is something that corporate governance types have been calling for for a long time. The two, as I say, reinforce one another.

Additionally, vis-a-vis qualifications of directors, there is concern about directors serving on too many boards. An over-Board director is not a good director because, obviously, he o she is like a jack of all trades, a master of none. Someone who is on too many boards does not have the time or energy to focus appropriate attention on the boards on which he or she serves.

Second, there is concern about the length of directors' terms. Directors who are on a board for too long, are viewed as becoming effectively tired, not as sharp as they once were in reviewing the company and much more willing to accept management representations than not. That is why a number of folks have called for term limits for directors, either through retirement policies or through actual 10- to 15-year terms, such that, at some point, someone rotates off.

How does this apply to the Enron Board? The Enron Board was problematic, I think, in the independence issue. There were a number of directors of the company who did not meet that definition that I described to you, who were service providers or recipients of corporate largess in some way, shape, or form, and that, I think, was problematic.

Additionally, you saw a conflict, I guess, vis-a-vis this Board in the sense that they held lots of options. There was equity on this Board, but there were also substantial numbers of company options, and a number of governance folks have suggested, too, that the way to incentivize a director is not necessarily through an option, which is an expectancy, but through straight equity ownership. An option is terrific on the upside, but on the downside, you do not lose very much. As an owner of a share of stock, on the downside, you lose quite a bit. You lose your investment and, obviously, the potential for upside.

I think that was the really primary thing we saw vis-a-vis the Enron Board, the presence of a number of non-independent Directors or what folks would view as non-independents. Did that mean they did not exercise independent judgment? Not necessarily. All it means is that if one is not independent, it is a lot tougher to make that difficult call with management. You are probably more trusting of management, because, in fact, you have relations to management.

Additionally, the Board of Enron served for a long time. A number of Directors had been there for at least 10 years, and again, the problem of length of service vis-a-vis being more accepting of management representations than not, I think, came into play.

In short, there were warning signals that were present. The warning signals were apparently missed until it was, in fact, too late. Why did it occur? That will obviously be the subject of your hearings and review.

But what I can say is from a structural standpoint, there were reasons, at least in my view, that the flags may, in fact, have been missed or not responded to early enough, and I think that this is something that this Subcommittee, and, frankly, the investing public, should demand of our companies, that a substantial majority of corporate Board members should be: A) independent of management, and B) own personally meaningful equity, long-term equity stakes in the company, equity stakes that cannot be sold on the short term but must be retained for the length of the director's service on the Board. Thank you.

Senator LEVIN. Thank you very much, Mr. Elson. Mr. Sutton.

TESTIMONY OF MICHAEL H. SUTTON,[1] FORMER CHIEF ACCOUNTANT, SECURITIES AND EXCHANGE COMMISSION, WILLIAMSBURG, VIRGINIA

Mr. SUTTON. Chairman Levin, Senator Collins, Members of the Subcommittee, thank you for inviting me to share my thoughts with you today.

First, let me comment briefly on my background and experience. I was Chief Accountant of the Securities and Exchange Commission from June 1995 to January 1998. Prior to holding that office, I was a senior partner in the firm of Deloitte and Touche, responsible for developing and implementing firm policy relating to accounting and auditing and practice before the SEC. My career with Deloitte and Touche spanned from 1963 to 1995. As a retired partner, I receive a fixed retirement benefit from that firm. Presently, I undertake

[1] The prepared statement of Mr. Sutton appears in the Appendix on page 191.

from time to time independent consulting and other assignments in the field of accounting and auditing regulation and related professional issues.

Effective oversight by Boards of Directors is at the heart of the financial reporting processes that serve and protect the interest of investors and the public. Without effective oversight, important checks on the integrity, judgment, and performance of management are compromised. Without effective oversight, critical safeguards of the rigor and objectivity of the independent audit are weakened.

As we have seen in the case of Enron, failures of the corporate governance processes can be devastating and the investing public, rightly so, is asking, "Can we rely on corporate governance, oversight by Boards of Directors and audit committees, to ride herd on management and see to it that auditors do their jobs?"

We would like to believe that Enron is an anomaly, that the governance issues raised are isolated to this case, but they are not. While Enron has become a poster child for a system out of control, the underlying concerns about the diligence of Boards of Directors and audit committees reach far more broadly into our corporate and capital market culture.

As we look at the issues today, it should be abundantly clear that there is no higher goal for financial reporting than providing useful and reliable information that promotes informed investment decisions and confidence in the system. It also should be abundantly clear that without diligent, probing directors and audit committees and dispassionate, independent auditors, the quality of financial reporting can be and will be systematically undermined. Without adequate checks that must come from effective governance, conflicts of interest can, and will, go unchallenged.

One of the most practical and effective steps in reforming the financial reporting system, in my view, would be to immediately revisit and rewrite our corporate governance policies and guidelines to clearly break the bonds between management and the independent auditor and to unmistakably spell out the responsibilities of boards of directors and audit committees to shareholders and the investing public. Management should be the subject of, and not the manager of, the independent audit relationship and process.

The ultimate responsibility for full and fair disclosure to shareholders, and the direct responsibility for the independent audit relationship and the quality of the audit process, should be clearly fixed with the board of directors and its audit committee. The audit committee should be made up entirely of independent directors.

For independent auditors, I believe that a brighter future begins with full acknowledgement of the reality that seems so clear today. Failures in our financial reporting system are more than aberrations. They seriously undermine investor confidence in the institutions that are supposed to protect them. They "poison the well."

To restore and maintain confidence in the independent audit, I believe that profession will have to do three things. First, it will have to embrace a role that is fully consistent with high public expectations. In public capital markets, insiders have an advantage over public investors, and in that arena, independent auditors are expected to balance the scales by assuring investors that the financial reporting gives them a fair presentation of the economic realities of the business.

Second, the auditing profession will have to tackle fraudulent financial reporting as a distinct issue with a distinct goal, zero tolerance. We understand that in life zero defects are almost never realized. Nevertheless, the public expects that the profession will pursue that objective.

Third, it will have to accept and support necessary regulatory processes that give comfort to the public that the profession is doing all that it can do to prevent future episodes of failed financial reporting.

With respect to accounting standards, we simply cannot tolerate financial reporting that "hides the ball" and we cannot tolerate processes that are not responsive to critical financial reporting needs. Current rules for accounting for SPEs, for example, are nonsensical. They can only be explained by accountants to accountants. More broadly, outdated rules governing consolidation and off-balance-sheet financing have become recipes for masking a company's true economic risks and obligations. We have a right to insist that accounting standards clearly reflect the underlying economics of transactions and events, and it is not acceptable to sit by while market innovations outstrip the development of needed guidance.

Criticisms of U.S. standards is beginning to focus on the fact that they have become increasingly detailed, and arguments have been made that they should be broader statements of principle, applied with good judgment and respect for economic substance. I have sympathy for the desire to break the cycle of the mind-numbingly complex accounting rules that have become the norm, but to do that, I think we have to confront realistically the reasons why our standards have evolved the way they have. Here are some of the underlying pressures that are at work.

Business managers want standards that provide the greatest flexibility and room for judgment. They want to be able to manage reported results, but yet be able to point to a standard that assures the public that they are following the rules.

Deal makers and financial intermediaries want standards that permit structuring transactions to achieve desired accounting results, results that could obscure the underlying economics. In that world, creative transaction structures are valuable commodities.

Auditors are pressured to support standards that their clients will not take issue with, and they often are restrained in their expected support for reporting that is in the best interests of investors and the public. Others, including legislators, some legislators, too often lose sight of the fundamental importance of an independent and neutral standard-setting process. Without independence and neutrality, standard setters cannot effectively withstand the myriad of constituent pressures that they inevitably will face and make the tough decisions that inevitably are required.

And then standard setters too often seem to pull their punches, perhaps because of the perceived threat to the viability of private sector standards setting, perhaps because of the sometimes withering strain of managing controversial change, and perhaps because of a loss of focus on mission and concepts that should guide their actions.

As we reexamine the processes, the issue and debate should not be about whether accounting standards should be detailed or broad, but rather about what formulation of standards and standard-setting processes best accomplish the goal of providing capital markets with reliable and decision-useful information. We need to reenergize our standard-setting processes and the commitment of capital market participants to support a fully effective, independent standard setter. We should provide independent funding for the FASB, funding that does not depend on contributions from constituents that have a stake in the outcome of the process.

We also need a more independent governance process to replace the current foundation board. The leadership for these changes should come from visionaries of unquestioned objectivity and demonstrated commitment to the goals of financial reporting and the public interest.

At the outset, I suggested that the common interest in preserving and maintaining healthy capital markets far outweighs the concerns or goals of any particular group or special interest. We have to keep focusing on that fundamental tenet. Only a continuing commitment to that goal will guarantee that we continue to enjoy the best capital markets in the world.

Thank you again for inviting me. I would be pleased to respond to your questions.

Senator LEVIN. Thank you very much, Mr. Sutton. Mr. Campbell.

TESTIMONY OF ROBERT H. CAMPBELL,[1] FORMER CHAIRMAN AND CHIEF EXECUTIVE OFFICER, SUNOCO, INC., AND CURRENT BOARD MEMBER OF HERSHEY FOODS, CIGNA, AND PEW CHARITABLE TRUSTS, CORONADO, CALIFORNIA

Mr. CAMPBELL. Mr. Chairman, ladies and gentlemen, I, too, appreciate the opportunity to testify before this Subcommittee today. This Subcommittee's deliberations are extremely important, in my opinion, because it is a national imperative that we begin the process of restoring the confidence of investors in publicly-held companies.

For your information, my active business career has spanned a 40-year time period, from mid-1960 until June 2000. The entire career was spent with one company, the Sun Oil Company, or Sunoco, as it is known today, or its subsidiaries. In 1991, I was named President and CEO, and in 1992, Chairman of the Board, and I held the Chairman and CEO positions until I retired in June 2000.

Before I begin, I need to make two points clear. First of all, any remarks that I make are my own personal belief and they do not necessarily reflect the beliefs of the corporations on whose boards I have served or am currently serving.

And second, you need to understand that my knowledge of Enron and its Directors or Arthur Andersen and its partners is limited to what I have read in the print media or seen on television or heard today. I have no direct knowledge of what has taken place in those organizations.

[1] The prepared statement of Mr. Campbell with an attachment appears in the Appendix on page 195.

Now, in your letter of invitation to me, you asked that I comment on whether I thought the governance problems exposed in the Enron matter are unique or representative of most U.S. publicly-traded companies. My answer is that I certainly do not believe that the alleged behavior is representative of boards of directors in the United States today.

In addition to Sunoco, I have been or am currently a Director of CoreStates Bank, before its acquisition, Hershey Foods, CIGNA, Pew Charitable Trusts, Rocky Mountain Institute, plus numerous civic and nonprofit boards. I have chaired audit committees. I have chaired the compensation committees. I have been on governance committees, finance committees, and executive committees, and during those 15 years, I have come to know probably more than 100 directors and can state from personal experience that the allegations that I have read in the print media and seen on television are not even remotely similar to the director experiences that I have had. Unfortunately, the general public seems to believe that Enron is typical, and I think that is terrible and it is part of the reason that I am here today.

I believe the best way to explain the type of board governance that I am accustomed to is to cite some of the practices we instituted at Sunoco. The list of governance practices of that corporation spans four single-line typed pages, and you will be happy to know that I have absolutely no intention of reading them here this afternoon, but have instead submitted them as an attachment to my proposed remarks for your information.[1]

Senator LEVIN. Thank you.

Mr. CAMPBELL. In those remarks that I prepared and submitted for today's performance, I briefly outlined the company's practices in director independence, director compensation, and director election. I spoke of the company's approach to the code of ethics and to conflict of interest policies, the company's approach to CEO evaluation, director evaluation, and "board-as-a-whole evaluation. And finally, I wrote of our experience in changing the independent auditors. Now, I am not going to take the time to read through those now, but I will be glad to answer any questions that you may have on my experience with those practices.

You might be interested to know that Sunoco's approach to governance resulted in several instances of external recognition and culminated in that board of directors receiving the 1999 National Board Excellence Award from Spencer Stuart, the executive search firm, and from the Wharton School of Business at the University of Pennsylvania.

Now, also in your letter of invitation to me, you asked if I might have any recommendations for new legislation or regulatory reforms. I will confess to you up front that my business career has conditioned me to seldom seek more legislation or regulation from government. However, I do believe that the current situation calls for strong action on the part of someone, and I would suggest four areas of focus.

[1] The list of corporate governance standards appears at the end of Mr. Campbell's prepared statement in the Appendix on page 199.

First, I believe there needs to be a more complete and understandable annual disclosure of the relationship between a director and the corporation. The typical corporate proxy today issued prior to an annual meeting and the election of the directors gives a very brief description of the director standing for election.

I would like to see a much more complete description, on one page, of each director's relationship with that corporation, including not only the total compensation received in whatever form it takes, cash, stock, benefits, or perks, but also any consulting or employment contracts for them or their relatives, any business relationship between their company and the subject company. Are they a significant supplier or a customer? What are their financial holdings in the company they serve as director, stock, stock equivalents, options, bonds, other forms of debts, loans, etc.? I realize that some of this information is disclosed in other documents. However, bringing it all together annually in one place in an easily-read format and publishing it will help ensure complete disclosure of how independent your so-called independent directors really are.

My second suggestion is that an annual meeting of outside directors, and with that I mean no CEO or other members of management present, be made mandatory, not just a voluntary good practice, and it be followed with an extensive feedback session to the CEO/chairman. I have instituted that on boards that I have been on and have found it to be of tremendous value to both the CEO and the outside or independent directors in surfacing issues early while they still can be dealt with constructively.

Mr. Chairman, my experience is that you do not get in big trouble in one step. You get there in a series of small steps that progressively take you further and further away from acceptible behavior. It is the so-called slippery slope. That is why there has to be an extensive, no-holds-barred meeting of independent directors, regularly scheduled, at least annually, with no management present, because I believe in that discussion the best way to surface the issues that somehow just do not feel right in your gut as a director is to have that kind of discussion with your colleagues.

Third, I believe that consideration should be given to limiting the years an outside auditor can serve a corporation. The need for a different set of eyes is currently recognized by the existing requirement that the partner in charge be rotated every 7 years. However, bringing in a new lead partner from the same firm to work with the existing team from that firm is inadequate, in my opinion. I am certain that this requirement would be seen as unnecessarily disruptive and expensive by most corporations today, but if an outside auditing firm knew that 10 years from now, a competing auditing firm would be looking over and possibly commenting on their prior work, a whole new dynamic would be introduced in the current process.

Fourth and finally, since good corporate governance is a constantly evolving process, it would be unwise to legislate or regulate with too much specificity. What is viewed as good practice this year may not be viewed as adequate in future years. Boards instead need to institute a continuous governance review process, and I believe it would be helpful if the following were required by regulators.

One, corporations should be required to put their governance practices in writing and publish them annually in their proxy statements. In that manner, it would be clear to all shareholders how their corporation is being governed.

And two, a board committee should be identified and held responsible for reviewing and updating a corporation's governance practices, similar to the way the audit and compensation committees currently have certain regulatory duties.

One of Sunoco's current directors, Rosemarie Greco, recently published in the January 2002 edition of National Corporate Directors Monthly an excellent description of a process which a corporation can use to institutionalize the best governance practices.[1] I strongly recommend you review her offering because it is only when the governance process is institutionalized that it will continue to be effective over time.

Again, I thank you for the invitation to be here today and I will be happy to try to answer any of your questions.

Senator LEVIN. Thank you all for your testimony and again for your patience.

Enron kept about 50 percent of its assets off its balance sheet, about $27 billion out of $60 billion. It also had off-the-books guarantees that were not reported, major business ventures that were not disclosed to investors. Now, we have been told there is no way to know whether the extent of Enron's off-the-balance sheet activities is typical or unusual for U.S. companies since the activities are, by definition, off the books and not reported.

How can investors rely on financial statements if a large percentage of a company's business activities, assets, and liabilities are off the balance sheet, and what accounting rules need to be changed, with as much specificity as you are willing to give us, to acquire that disclosure which you referred to of material off-the-balance sheet activities, assets, and liabilities? Maybe, Mr. Sutton, we could start with you.

Mr. SUTTON. Let me offer several—make a few points about that.

Senator LEVIN. If I could interrupt for one second, I think you said that the current rules on these SPEs are nonsense, so that is the reason I am starting with you. You have made a very pungent point about it.

Mr. SUTTON. Let me offer a few comments to help explain why I said that and what the state of the art is. Off-balance-sheet financing is one of the most valuable commodities on Wall Street because markets tend—or companies perceive that markets tend—to value companies that have less debt on their balance sheet. Rating agencies also will do it. The markets, some segments of the markets—tend to view asset-light companies as being more attractive investment opportunities. That creates an incentive of companies to get debt off the balance sheet, to get asset-light, so that they will be looked at and perceived favorably by the market.

What has happened in the standard-setting process, and when I said we need to understand what the drivers are to understand the problem, instead of trying to develop standards that say, "what is the economic substance," "who has the risks and the benefits of

[1] See Exhibit No. 86 which appears in the Appendix on page 751.

these assets and liabilities," "who really owns them," the standard setting has lapsed into a process of "what rule do I have to comply with in order to get an asset or a liability off the balance sheet?"

So that is the state of the art, and it creates a situation, as in Enron, where you can have substantial obligations, that you or I might recognize as liabilities, off the balance sheet, substantial assets that you or I might say, "well, Enron really has the risks and benefits of that asset off the balance sheet," and it is accomplished through accounting standards that, in part, were not complied with, and in part that were complied with but that were poorly designed.

Senator LEVIN. Before I turn to either of the other two witnesses, would you have specific changes that you would propose? Because you are moving from a legalistic to an equitable or to a judgmental or, not intuitive, but something which is a little less legalistic in its description to something which is more, hey, who really has these risks and benefits. How do you put that in a rule?

Mr. SUTTON. You have to first articulate conceptually what you are trying to accomplish, and then you develop rules to the extent that you need to develop rules to accomplish that.

Senator LEVIN. Has somebody done that?

Mr. SUTTON. Well, the FASB's charge is to do that, and I mentioned their mission. That is what they are charged to do. In my personal opinion, they have not done a very good job of that, particularly in recent years.

Senator LEVIN. Has anybody outside of the FASB made an effort to design rules which would achieve that objective?

Mr. SUTTON. Well, there is a new body in place now, relatively new, and that is the International Accounting Standards Board, that has pledged, in a sense, to take a more principled approach. I would not suggest in any way that whatever approach you take is going to be easy because it is like any set of rules that you try to develop. There are always going to be those who want to game the rules. But my view is that you ought to develop your rules following the concepts that you believe are best—that give the best and fairest presentation, the most transparency, and develop those rules as best you can.

Senator LEVIN. For instance, has any academic tried to design rules which would correct for the inadequacy of the current rules relative to these transactions? Is there anyone who has done some writing in this area in academia?

Mr. SUTTON. There is lots of writing, but there is no magic bullet. The magic bullet in this is having an independent process of highly qualified people who are clearly focused on a mission that is in support of what you expect financial reporting to be in the marketplace.

Senator LEVIN. You have said you would give FASB an independent source of financing. You testified to that today. Would you also have them appointed by a different body than is currently the case? Would you, for instance, have the SEC appoint any members of that board?

Mr. SUTTON. Chairman Levin, I have not thought in detail about how the structure—my view is, we needed to get some really capable visionary thinkers who have thought about this issue a lot and try to develop a consensus view. It may be worthwhile that some part of the board would be appointed by the SEC. It may be—it would seem logical to me—that you would want a certain segment of those members who would clearly be, and clearly be recognized as, advocates of or sensitive to the needs of the investing community.

Senator LEVIN. Would you give that board additional powers, including subpoena powers? Would you give them also powers to enforce rules, in other words, separate that enforcement function?

Mr. SUTTON. What I had in mind that we were just talking about would be a body that would set accounting standards. There is a need for—the other accounting leg of this stool is the accounting profession, and I would see clearly a need to have another body, an independent body, oversee the auditing profession, and that body should have appropriate investigative powers, in my mind.

Senator LEVIN. Mr. Elson, do you have any comments on the subject that I have been talking to Mr. Sutton about?

Mr. ELSON. I am a transparency person. I have always been a big fan of transparency, and I think the more that is disclosed about those sorts of things, the better. But vis-a-vis the technical aspects of on or off-balance-sheet financing, I am a little out of my field.

Senator LEVIN. OK. Mr. Campbell, did you have any comment on that?

Mr. CAMPBELL. No. I would agree with Mr. Sutton and Mr. Elson. Prior to the Enron disclosures, I had never seen that amount, or proportion of a company's assets off-balance-sheet. Sometimes it is appropriate to have some items off-balance-sheet, where you have an investment and no control, but never to that extent. As to how you would correct that situation, I cannot offer expertise in that, sir.

Senator LEVIN. Mr. Elson, have you ever seen or know of a company that had that many off-balance-sheet entries?

Mr. ELSON. Not that I am aware of. On the other hand, again, my expertise really is not in that area. It was quite a bit to obviously have it off the balance sheet, and obviously not disclosed.

Senator LEVIN. Mr. Sutton.

Mr. SUTTON. Well, many companies have off-balance-sheet assets and liabilities, but my experience is that Enron is at the top of the scale in terms of the extent of it. Airlines, for example, would frequently have much or most of their aircraft off-balance-sheet through leasing arrangements and that would not be regarded as unusual.

Senator LEVIN. Thank you. The Enron Board approved Andersen serving not only as the outside auditor for the company, but also for a couple of years as the company's internal auditor at the same time and paid Andersen also tens of millions of dollars for consulting work. The end result was that Andersen was essentially auditing its own work.

Now, the Board members defended this practice by saying that it gave them great comfort to know that Andersen was involved in all of Enron's transactions from the very beginning. They called it an integrated audit. What is your reaction to this idea of an integrated audit, in which the same auditor is the company's consultant, internal auditor, and external auditor? Mr. Sutton.

Mr. SUTTON. Well, in my experience, the term or label "integrated audit" generally referred to a proposal to combine the internal and external auditing, and so a couple of things I would say about that. One is that it became quite fashionable in the late 1990's. The second is, I think it is a terrible idea because it does create the situation where, on the one hand, the auditor is performing a management function, i.e., internal auditing, and on the other hand is called upon to examine the financial statements.

The other aspect of it that you mentioned is consulting in the area of transaction structures. That clearly, in my mind, raises questions about auditing your own work, and it depends really on what was done and to what extent it was done. If the auditors were the creative thinkers, if you will, in terms of how do we accomplish a transaction to accomplish a certain accounting result, to me, that is over the line. On the other hand, you would expect a company that is getting ready to enter into a transaction to ask its auditor, do you have any concerns about this? So there is a line there that, in my mind, once you cross that, you have a problem.

Senator LEVIN. OK. Mr. Elson.

Mr. ELSON. I guess my answer would be in two parts. First, vis-a-vis the internal/external audit role, I have always believed that they should be separated for a very important reason. Those are—they are watchdogs, effectively. An external audit, internal audit are watchdogs of the company's financial processes in some way, shape, or form, and anytime you concentrate two watchdogs in the same watchdog, you have effectively reduced the effectiveness by half, if you have one less person there.

Second, the fashion typically today has been to outsource internal audit. Traditionally, it was always internal. That is why they called it internal audit. But there is some merit, a great deal of merit, to outsourcing the internal audit function. And when you do so, I have always felt that there is some benefit to separating the internal auditor from the external auditor because you have two different large firms in the company effectively, even if informally, checking each other's work.

The presence of a different internal auditor or the presence of a different external auditor, I think acts as a bit of a check on the work of either party and that is a pretty—I think it is healthy competition. That is the first point. I have never, frankly, felt that the two should be combined, and when it was, I think 2 or 3 years ago, the SEC effectively allowed that, I was rather critical of that at the time and I still am.

Second, vis-a-vis the consulting, the auditor consulting, when auditors do consulting, a lot of consulting, the question is, does it compromise the effectiveness of the audit itself? Can you trace the presence of heavy consulting work with a busted audit?

I have not been made aware of any empirical data to date that demonstrates emphatically the correlation between consulting, heavy consulting, and a busted audit. On the other hand, from an optical standpoint, a shareholder trust standpoint, putting it in the same party is problematic. It looks problematic. It looks as though, even though one can argue there is a Chinese wall, if you will, between the two functions, there is certainly the public perception of potential corruption of the audit process by the desire to seek consulting fees, and because of that public concern, I think it is something that I would limit.

Unless you have a really good reason to do it, I do not think I would have the external auditor doing consulting work, or if they did consulting work, it ought to be very limited in nature and in scope and only used when, frankly, you can demonstrate that there is nobody else out there who can deliver an effective service. In other words, you do not want the consulting to affect the audit function and you do not want those, certainly the members of the public who are relying on the financial statements, to be concerned that those financial statements are not reliable because someone was doing both.

Senator LEVIN. I think it is more than optics. Enron paid Andersen $5 million in the year 2000 to help structure LJM, and so it would seem to me it would be pretty hard for Andersen's auditors to say that the Andersen consultants got it wrong. I think that is the problem. I think it is a real problem, but let me ask Mr. Campbell, do you have any comment on that issue?

Mr. CAMPBELL. I think what was described today as the integrated audit is a horrible practice and I do not think it should be permitted.

As far as consulting is concerned, I think when you end up with an auditing firm which, first of all, bids a proposal on the basis of conducting the external audit and then finds over a period of time that the non-audit fees continue to grow, in my mind, that does nothing but continue to reduce, not only optically but in reality, the independence of those so-called independent auditors. There is no question, at least recently, there have been pressures to begin to bring that down because people are focusing on that issue, but it sure can reduce independence, in my opinion.

Senator LEVIN. Thank you. This is for you, Mr. Elson. You have written extensively on the importance of independence and you have testified to that this afternoon. Exhibit 43,[1] if you have a book near there, identifies some of the economic ties between Enron and some of the outside Directors. The Board members told us that none of these dollar commitments was large enough to have impaired anyone's judgment or to sway any Director from being honest and skeptical with Enron management. You can perhaps scan the amount of dollars that are involved in those items. I am just wondering what your response is to that.

Mr. ELSON. I think that if amounts for consulting services were not meaningful, then the individuals would not have taken them to begin with. Obviously, they had some meaning or they would not have accepted compensation for services rendered.

The problem with taking separate fees, other than one's directors' fees, is I think it creates a linkage between you and management. By taking those fees, you are effectively becoming part of the management team, and I think there is a real problem with exercising independent judgment vis-a-vis what the management has done if you feel part of that team, either through participating in

[1] See Exhibit No. 43 which appears in the Appendix on page 375.

the development of management plans and strategies or the fear that if one objects too strenuously, those consulting fees may disappear. That, at least, has been the generic critique of those.

I think, too, the problem with them is that by taking them and becoming, again, part of management, in a sense, you are much more reticent to be critical of management, not because you are no longer "independent," but because of the relationship you have with management, that financial management. You may take what they are telling you at face value without being more probative because of the relationship that this thing creates.

That is why the National Association of Corporate Directors in their commission report on director compensation said that if a director's role is as a consultant, hire the director as a consultant. If the director's role is to be a director, hire them as a director. You cannot blend the two. The argument that we could not retain someone's consulting services unless we made them a director, I have never felt was a very good argument.

Again, the problem here is either these fees may have affected their view of what was being presented to them—again, you have to get each of them here to testify as to whether they did or they did not, but certainly in the part of those within the organization, the presence of those relationships might have made the perception of those directors within the organization viewed as less than independent. If that were the case, it would be tougher for someone within the organization, if they objected to what was going on in management, to approach any of these directors because they were of the view that, gee, they are just part of management anyway, and that, I think, is the real issue here.

In other words, independence, as I said, is a two-way street, and I think the presence of these relationships is not a good idea, and that is why the National Association of Corporate Directors has strenuously recommended against these sorts of relationships.

Senator LEVIN. This is for Mr. Sutton. You were Chief Accountant at the SEC, and by the way, did either of you have any comment on that last answer before I go on?

Mr. CAMPBELL. Well, I would just like to point out, I think the consulting arrangements with directors is absolutely incorrect, absolutely wrong. When you accept the directorship of a corporation and join the board, you are paid a fee, obviously in the case of Enron, substantial. In my mind, your thoughts, your processes, and what have you, your support and you are there available to the management at any time they want to contact you. And if, in fact, they need you on an ongoing consulting basis, then you should not be a director of that corporation.

Senator LEVIN. Thank you. Mr. Sutton, now a question about the Raptor transactions. You were Chief Accountant, as I indicated, for the SEC and I would like you, if you would, to turn to Exhibit 28b,[1] which is the initial Raptor presentation to the Board.

Mr. SUTTON. Exhibit 28——

Senator LEVIN. Exhibit 28b. The first page states that the purpose of the Raptors is to establish a risk management program in order to hedge the profit and loss volatility of Enron investments.

[1] See Exhibit No. 28b which appears in the Appendix on page 306.

The last page of this Exhibit 28b lists the risks that are associated with the Raptors. The first one is “accounting scrutiny.” The second one is “substantial decline in the price of Enron stock,” what would happen. I am just wondering, what is your reaction to the presentation, in particular, the focus on hedging profit and loss volatility as opposed to hedging real economic risk?

Mr. SUTTON. Let me couch my response in these terms. Obviously, we do not know what was said at the meeting, and so I am going—what I give you is more of a reaction based upon my experience and insights.

The first thing that comes to mind is when I see the slide labeled “Purpose,” it says establish a risk management program in order to hedge the profit and loss volatility of Enron investments. The first thing that comes to my mind is, “what does that mean,” quite honestly. What does it mean to say, “hedge profit and loss volatility?”

I had a similar question in listening to the testimony this morning. The term “hedge,” in my mind and experience, refers to transactions that are used to transfer or alter the risk of the company, so that there is another party out there that you exchange risks with, or you transfer risk to, that has an economic impact. And this says “hedge profit and loss volatility,” and I do not know what that means. That is my first reaction.

What was the other page?

Senator LEVIN. On the last page, you have got a risk list. One is accounting scrutiny. The other one is a substantial decline in the price of Enron stock. In other words, in addition to trying to protect itself against paper losses here, not as you testified, in effect, against real economic risks, but against paper losses, Enron used the Raptors to hedge against the decline in value of certain assets, but that was backed by Enron shares rather than independent third-party equity. It was Enron shares which were put up for that hedge, so they are hedging against themselves, are they not, or am I missing something here?

Mr. SUTTON. Well, all I can interpret from the comment is that the risk is from a substantial decline in Enron stock, and then the consequences of that are identified “as the program terminates early.” I assume that would be at a loss of some kind, and it increases the credit risk, so I assume that is Enron’s credit risk, but——

Senator LEVIN. The risk here, as I understood it, is since they put up their stock as the collateral, that if, in fact, that stock declined in price and was called upon, then they would have to put up a huge amount of their own stock. So they were not transferring risk, they were using their own stock to cushion against the risk of their own assets, their own stock holdings going down in value. Is that a true hedge?

Mr. SUTTON. That is not what I would understand a hedge to be, and that would also explain, perhaps, the first slide, by what they meant by “hedge profit and loss volatility.”

Senator LEVIN. OK. So it is just not clear to you as to what——

Mr. SUTTON. It is not clear to me.

Senator LEVIN. Does anyone else have a thought on this?

[No response.]

All right. What does a board do if they are told that high-risk accounting practices are being used? What is their fiduciary duty? We will start with you, Mr. Campbell.

Mr. CAMPBELL. Well, first of all, I cannot imagine going into an audit committee room and sitting down with the auditors and being told that we are using high-risk auditing practices and just agreeing with that. I mean, my experience has been people would want to know, why are they high risk? How did we get there? Why are we using them? And what are you going to do to get us out of it?

Going forward with that kind of an environment, it is what I said before. It is a little bit like this whole thing turns into one step after another. You are going down a slippery slope on this thing, and at what point in time do you yell, enough is enough?

But having an audit committee confronted with the fact that you have high-risk auditing practices and then having the chairman take that to the board and report it to the board and have that board agree that is OK, it is unlike any board that I have ever seen or heard of.

Senator LEVIN. Mr. Elson.

Mr. ELSON. My first reaction to that would have been an extremely queasy stomach. That is a giant red flag, being told that you are—for a large publicly traded company, the seventh largest public traded company in the country—taking serious accounting risks is a pretty scary thing, just to say the very least.

As a director, under the duty of care, you are being compared to what would the reasonable director say under similar circumstances, and the reasonable person would certainly say, why are we doing this? Why is this risky? Is this very smart to be doing this? What is considered conservative treatment? Why are we not in conservative treatment? And how do we get ourselves out of risky treatment, because, obviously, risky treatment has risks. That is why they call it risky treatment. What are the risks before us and how do we restore conservative treatment?

At that point, you want to ask an awful lot of questions, and if you do not get the right answers, then you need to bring in a third party.

Senator LEVIN. OK, thank you. Mr. Sutton.

Mr. SUTTON. I would just support those comments and say that from the accountant's perspective, you would also expect some kind of dialogue to arise between the audit committee and the independent auditors.

Senator LEVIN. One of the issues which came up had to do with the compensation of the Board of Directors. Exhibit 35a[1] is the total compensation of Enron Board members for fiscal year 2000. As you can see, including stock option value which probably represented three-quarters of it, roughly, it was in the range of $320,000 to $340,000, with the cash compensation being roughly from $70,000 to $90,000 and the balance in stock option value. This is a chart from their own sources.

Mr. Elson, you particularly made reference to stock options as being an expectancy where you do not lose as much on the down-

[1] See Exhibit No. 35a which appears in the Appendix on page 348.

side, as you put it. Even though it turned out these options were not worth much in many cases when they held those options, when they were granted those options, there was a hope and an expectation that they would be worth a tremendous amount of money. This is what the estimated compensation was, a quarter-million dollars in the value of those options just in that 1 year.

Doesn't that create pressure on the Board, basically, to go along with management or with these far-out, pushing the envelope accounting practices which make the financial statement look good and then push up stock prices, because their options go up in value? Now, their answer today, frankly, was not particularly satisfactory to me because what they said is, well, they turned out not to have any value or they lost money. That is not the issue I am talking about, whether they ended up losing the value of those options.

What I am talking about is when they were granted those options, those options had real value and great potential value if the financial statement continued to look good, and one way to make that financial statement look good was with all these transactions that we have heard about.

So does that fact not create some subtle, maybe not-so-subtle, pressure on Board members to go along with the idea that it is the stock price which is the end-all and be-all, and that is so affected by the bottom line on a financial statement, then to go along with accounting standards which are pushing the envelope? That is my question, Mr. Elson.

Mr. ELSON. Sure. Let me answer in two parts. Part one, share amount. This is pretty good work here. This is a lot of compensation for being a director. You know the old joke, good work if you can get it. Three or four hundred thousand dollars a year is quite a bit for directors. That is quite a bit over the norm in companies of this size and scale. These compensation amounts would put the Directors of Enron certainly in the top quartile, or probably higher, vis-a-vis similar compensated U.S. directors.

The problem with paying a director too much is an obvious one. If management, as in many companies—I am going to speak generically—controls the proxy process and the compensation scheme for the directors becomes too high, the fear is the director, because of the income stream the director is receiving from serving as director becomes so great, that to object to a management proposal and potentially court non-renomination would not be in the director's best financial interest, and that is where compensation that is too out-of-the-ballpark, if you will, for a director is problematic.

These numbers undoubtedly placed this Board pretty far up there in the grand compensation scheme. Again, most of the value was in stock options, but their cash compensation was not small. It was pretty high, too. But clearly, the real value was in the options.

So the second part of your question, does giving director options make a director more likely to take risks, if you will, financial risks, again, that is a two-part answer. I have never been a big fan of options. I think they are useful in certain circumstances. I think they are problematic because, traditionally, you cannot charge—you do not charge them against earnings. I think there is a bill floating around that, Senator Levin, you have been involved in that would require that there be some charge for granting options. I think when you cannot charge them against earnings, people are a lot freer with them than they would ordinarily be if they had to give restricted stock and they give more of them.

The problem with an option is it has a geometric upside to it, if you work out the math, even based on mediocre performance of a company, and that, to me, is problematic. There is no real downside. The worst you can lose is the expectancy of great riches. There is no real sting on the down. They simply become worthless. Stock is a different incentive. If a stock falls, you actually have a wealth decline on the part of the holder of the stock. In this case, they got a lot of options, and again, the weakness of options, I think, of potential on the upside rather than on the down, certainly comes out here.

But your question on does it make you more risky, only if——

Senator LEVIN. Not quite.

Mr. ELSON. Yes?

Senator LEVIN. Does it make it more likely that you would go along with pushing the envelope on accounting standards which have the effect of raising that stock price and then raising your option amount? Does that make it more likely or not?

Mr. ELSON. Only if you can sell the stock underlying the option relatively quickly. I mean, I have always believed that directors should not sell their stock while they serve on the board unless there is a very unusual circumstance. In other words, as long as you are a director, you have got to hold company stock. You cannot be in the business of selling stock.

I think the ability to sell your stock or exercise an option short-term and sell it is problematic because there is the risk of the informational disadvantage, if you will. I know that bad things are going to happen. I push the stock price up. I sell, and then when the bad things happen, I am long gone and I have taken my profit. That is the risk.

That really does not have to do with the option, the grant of the option. It really has to do with the ability to sell the option or exercise the option and sell the stock quickly, or if you give a director restricted stock, the ability for the director to sell that restricted stock while that director serves on the board.

I think that is the real issue. It has got to be, and my remarks earlier had to do with long-term equity holdings. If you give someone stock and give them the ability to sell it quickly, then you have got a real problem. One, you have got that insider trading potential. And two, it is not very good to the public for a director to say, gee, I think I have found a better place for my money and it is not on the company on whose board I sit. It does not look very good. For that reason, I think the stock holdings have to be long-term.

So in the short, I do not think the fact that they gave options was problematic here vis-a-vis the question you asked, if, in fact, you required that the stock underlying the options be held long-term.

Senator LEVIN. So that would cure whatever problem there is that I have described——

Mr. ELSON. Yes. I just do not like options.

Senator LEVIN [continuing]. That prohibition. But there is no such prohibition, is there?

Mr. ELSON. No, sir.

Senator LEVIN. OK. Now, Mr. Campbell, do you have any comment on that?

Mr. CAMPBELL. I agree that these numbers are high, and, in fact, if you look at it, this is for year 2000, so if you have multiple years of compensation and multiple stock options, then they could be multiples of this. I have never felt that options for directors are appropriate for the exact reasons that Mr. Elson said.

And I would just point out to the Subcommittee that as you are thinking about where to go from here, part of problem, I am going to lay at the feet of compensation consults, which invariably come in and tell board compensation committees, if you want to compensate either your directors or your senior executives and your CEO at the 75th percentile range or level, then this is what you need to do. And then they go on to the next company and give the same talk. That becomes a one-way ratchet and it has occurred here over the past decade that is off the top of the scale, and I think we really need to get back to thinking about how do we determine what is really competitive out there.

Senator LEVIN. It is a very important issue and it is essential that dialogue occur, one way or another.

Mr. Sutton, do you have any comment on this question?

Mr. SUTTON. I do not disagree with anything that either of them has said. I would just add a thought that while I am not an expert in ethics, I have done considerable study in connection with the work at the Commission on Auditor Independence Issues. I would observe that whether it is selling, the pressures to sell non-auditing services, whether it is incentives by directors to enter into consulting arrangements, or whether it is what is perceived to be excessive compensation, those arrangements can create incentives that can interfere with otherwise expected independent behavior.

Ethicists sometimes call that "gray blindness," meaning that once you get so co-opted, you cannot tell the difference between black and white anymore, and there is that risk. Other incentives can give rise to it, but certainly financial incentives can.

Senator LEVIN. You all have added a very important dimension to this hearing and to our investigation. The Congress really has a very heavy responsibility that we are addressing, but we are playing just a partial role in implementing and taking care of the problems. But your participation—your staying power is very much appreciated, and your very thoughtful written testimony, which will be made part of the record, and your comments in response to questions are very much appreciated.

Mr. Elson, regards from Senator Carper. He had to go and preside this afternoon or else he would have been here to ask questions.

Mr. ELSON. Thank you.

Senator LEVIN. I want to thank my staff for the enormous effort they put into going through all of these documents.

We will stand adjourned. Thank you all.

[Whereupon, at 4:55 p.m., the Subcommittee was adjourned.]

APPENDIX

STATEMENT OF JOHN DUNCAN

Before the Permanent Subcommittee on Investigations
Committee on Governmental Affairs
United States Senate

May 7, 2002

Chairman Levin, Senator Collins, and Members of the Subcommittee. Good morning, and thank you for the opportunity to address the Subcommittee.

My name is John Duncan. From 1967 to 1985, I was a director of one of Enron's predecessor companies, Houston Natural Gas, and I was there when Enron began in 1985. I have served as Chairman of the Enron Board's Executive Committee since 1986. Thus, I am the Enron director who has served the longest period of time. Until the fall of 2001, I considered it one of the great companies in this country, and I was proud of Enron. I resigned from the Board in March 2002.

I received my bachelor's degree in business administration from the University of Texas. I set out to become a businessman, to start and run my own company. With the exception of my first job in a family business and a stint in the United States Air Force during the Korean War, I have not drawn a payroll check from a company of which that I was not either the founder or a co-founder.

I was a co-founder and President of Gulf + Western and founder of Gulf Consolidated Services. Both companies had small beginnings and wonderful success stories. During the course of my career, I have served on the boards of seven New York Stock Exchange companies. I have also served and chaired the boards of several important community institutions, including the Houston YMCA, the Chancellor's Council of the University of Texas, Southwestern University in Georgetown, Texas, and the Board of Visitors at the M.D. Andersen Cancer Center.

I provide that background to the Subcommittee to suggest that I have had substantial experience with and exposure to the workings, role and the duties of a company's Board of Directors, and limitations. That is what I want to talk about today. In particular, I want to focus on what I believe are the elements of an effective Board, and why I believe the tragic events at Enron occurred.

First, I believe that the directors must be individuals who possess integrity and intelligence. They also should collectively bring a broad spectrum of knowledge and experience in the areas of business, finance, and the company's particular industry. People usually acquire this experience by having operated a company with a significant budget or by having obtained a unique experience from another profession that is relevant to the company's mission.

The directors of the Enron Board certainly possessed these qualities. In my opinion, my colleagues are highly ethical, and of good character. As far as intelligence goes, I will simply say that if education is any measure, I believe I was the only one of a few directors who did not have a Masters or Doctorate degree. Our directors are experienced, successful businessmen and women, experts in the areas of finance and accounting, and had experience in leading large institutions. Others, like our overseas directors, also brought an expertise in certain areas of the world in which Enron saw tremendous business potential.

Second, I believe an effective Board must be dedicated and diligent in addressing the matters that are presented. The directors need to do their homework, analyze the issues, ask penetrating questions, and make decisions that are in the best interests of the company and its shareholders.

In my opinion, the Enron directors met these criteria. We worked hard. We prepared for meetings. We asked probing questions and imposed controls and procedures that management and outside advisors were required to follow. I know that my colleagues here today will address those in more detail. We were willing to say "No" to management when we did not agree with their recommendations.

A good example of the Board exercising these responsibility to act independently and in the Company's best interests occurred last September, when all company indicators were still positive and before any outside director was aware that Enron was in trouble. At least two transactions were presented to the Executive Committee and turned down for price and strategic reasons. The Executive Committee and Board were requested by management to authorize the purchase of two pulp mills for in excess of $300 million in October 2001. The Committee declined to approve those acquisitions because we were concerned about the performance of the previous acquisitions in that industry, the purchase price, and we wanted to preserve financial flexibility in light of the September 11 tragedies. We postponed our decision, and as we all now know, subsequent events soon overtook us.

I did not sit on the Audit and Finance Committees, but I did "sit in" as a guest at some of their meetings. My colleagues asked probing questions of the management and independent accountants. In my opinion, these Committees thoroughly executed their duties.

Third, I think that a Board cannot be successful unless it feels comfortable relying on the intelligence and integrity of the management and other advisers who are presenting matters to it. With over 20,000 employees, over 200 company lawyers writing contracts, and over 400 accountants posting the books, we needed to rely on reports given by the officers of the Company. Quite frankly, there is no other way that we could direct effectively a company of that size. We felt confident relying on Enron's senior management because we believed we had hired some of the best and brightest executives in the country. National, independent publications and organizations recognized and lauded these people for their intelligence, leadership, and creativity.

Finally, I believe the management and other advisors reporting to the Board must provide the complete truth, good or bad, to the Board so that it can make fully informed decisions. We now know this did not happen at Enron. The Board implemented mechanisms and controls to ensure that, at the very least, it obtained early warning signals of impending problems. Among many other procedures, we created a Risk Management Officer position and staffed that department with nearly 100 employees. That officer was responsible for reporting to the Board the most significant concerns and credit issues that faced the Company.

It is now quite clear that significant information about the related party transactions was withheld from us. We were not aware, for example, of the problems with Chewco, were not informed of Raptor III, were not told of the $800 million recapitalization of the Raptors in late 2000 and early 2001, were not told that employees in addition to Andrew Fastow were participants in these and other partnerships, and were unaware that they had reaped substantial windfalls from their participation.

As late as the August 14, 2001 Board meeting, the Board was briefed on the financial condition of the company. The report was "earnings up," balance sheet "stable," "possible credit rating improvement in year 2002." Various Power Point slides indicated to the Board that the Company's good business was improving. The Powers Report and the reports we have all now read in the press indicate that for many months prior to August 2001, members of management and our outside auditors were well aware of the problems facing the company—but they did not tell us.

In sum, I do not believe that Enron's fall would have been avoided had the Board asked more questions, implementing more controls, or avoiding certain financing projects because they were too complicated or risky. Rather, if management had implemented the controls as they assured us they had, if just one of the company's officers or employees had fulfilled his or her corporate duty to reveal these problems to just one director, or if the outside auditors had executed their obligation to convey to us the concerns they expressed privately and documented among themselves, I do not believe that we would be here today.

I am prepared to respond to questions from the Subcommittee.

Thank you.

STATEMENT OF HERBERT S. WINOKUR, JR.

Before the Permanent Subcommittee on Investigations
Committee on Governmental Affairs
United States Senate
May 7, 2002

Chairman Levin, Senator Collins, and Members of the Subcommittee. Good morning, and thank you for the opportunity to address the Subcommittee.

My name is Herbert S. Winokur, Jr. I currently am a member of the Board of Directors of Enron Corporation. I have served as the Chairman of the Finance Committee of the Board of Directors of Enron. I have been a member of the Board since the mid-1980s. I volunteered for and served as a member of the Board's Special Investigations Committee (the "Powers Committee") to attempt to understand what happened at Enron.

I. INTRODUCTION

I appreciate the opportunity today to talk with the members of this Subcommittee about the involvement of Enron's directors in the related party transactions that have received so much attention, and about our oversight of Enron more generally. My colleagues will address issues related to accounting of and internal controls regarding these transactions, management compensation, and other matters concerning the directors. Attached as an appendix to this statement are excerpts from Enron's Board of Directors' meeting minutes that document some of my comments in the following paragraphs.

I will discuss shortly the basis on which the Board approved and sought to control the LJM transactions. But, in my opinion, one of the principal causes of Enron's failure was the loss of lender and investor confidence that resulted from the three significant restatements to Enron's financial statements presented in October and November 2001. Two related to earnings restatements for four and two years, respectively, and the third a significant reduction in shareholder equity. The first two derived from inadequate outside equity capitalization (to permit deconsolidation) in two special purpose entities of $6 million and $25 million respectively. The third derived from a presentation change from grossing up equity and liabilities to netting them. While a related party was involved in each transaction, the related party aspect does not appear to have been a factor in any of the accounting errors.

In none of these three restatements did the Board – or its Audit Committee – have any prior knowledge (except immediately prior to their disclosures) of the errors which were required to be corrected. In each case, Enron's management had approved the financial statement presentations and, as appropriate, Arthur Andersen had certified or reviewed the presentations. How and why these errors occurred are the subjects of several government investigations. As I said above, I believe that the loss of investor confidence in Enron and its management that resulted from these accounting restatements was a significant contributing factor to Enron's downfall.

With that in mind, I would like to turn to a general discussion of three areas.

- The first is to describe how the Enron Board of Directors and the Finance Committee went about discharging its obligations.
- The second summarizes the specific circumstances in which we approved the LJM structures and the controls we put in place to ensure that these transactions remained in the best interests of the Company.
- Finally, I will address certain of the hedging transactions that the Board approved and that have come under so much criticism.

II. DISCUSSION

A. The Board of Directors and the Finance Committee of Enron

Enron's Board of Directors was composed of 12 independent directors and two inside directors, Kenneth Lay and Jeffrey Skilling. As a Board, we worked to help move Enron into a new business environment characterized by increased globalization of investment, increased sophistication in the capital markets, and rapid regulatory and technological change. This new business environment required us to make certain business decisions that, at the time, made sound economic sense: undertaking initiatives in power and water deregulation, entering into developing markets abroad, and building an extensive broadband network. Enron's expansions were hailed in the media as innovative and brilliant. Over the decade of the 1990's, Enron became the dominant company in providing electricity and gas to customers around the world.

To some extent, as now has been learned, by early 2001 Enron's reach had exceeded its grasp. Business decisions that made sense at the time, such as the building of an extensive broadband network, or Enron's entry into developing energy markets abroad, did not work out. Other broadband companies, such as Level 3 and Qwest, have experienced severe declines in the price of their stock as the demand for bandwidth dried up. Global Crossing, another broadband company, is—like Enron—in bankruptcy. Our initiatives in power and water deregulation abroad were also less productive than we believed they would be. Other similar companies such as AES and Dynegy also have seen significant declines in their stock prices.

I raise this to make an important point. Enron, as a company, took a number of business and financial risks. These risks were disclosed by Enron. They were also recognized by the analysts and rating agencies who followed the company. To suggest otherwise is to ignore the disclosed and well-publicized facts about Enron and its business strategy.

One of the responsibilities of Enron's Finance Committee was to review regularly the Company's financial ratios and liquidity. At the Finance Committee meetings, Enron management routinely presented us with Enron's actual and projected financial ratios and near-term liquidity, a report on meetings and discussions with the credit rating agencies, and an analysis of Enron's borrowing costs relative to those of its competitors, which informed us of the market's contemporaneous view of Enron. Between meetings, we also received reports on Enron from Wall Street equity and debt analysts, including their detailed financial projections.

For example, during the February 12, 2001 Finance Committee meeting, we were told that "the Company's total liquidity was over $8.3 billion." We were also told that "there had not been any change in the Company's ratings by the rating agencies but noted that the Company was working on being upgraded to 'positive outlook' by Standard & Poors." We regarded this as a good report on the financial health of the Company. Based on the Powers Report, we have since learned, however, that during this time period, management (without Board knowledge or approval) was working to restructure the Raptor vehicles by inserting $800 million in additional equity capital. Neither the Finance Committee nor the Board was told of those efforts. The Raptor structures, in fact, never appeared on a list of the top 25 credit exposures that was presented regularly to the Finance Committee. I do not know why we were not told of the credit concerns about the Raptors. The procedures we had put in place to receive reports on significant credit exposures should have revealed this issue to us, but the required report was never made. The improper accounting related to the Raptor restructuring was one of the matters that were addressed in the October/November 2001 restatement.

The picture presented by management at the August 13, 2001 Board meeting was no different. Recurring net income for the second quarter and the six-month period was reported to be higher than plan and the prior year's levels. Debt to equity capital ratio was 46% at the end of June, about the same as the prior year, and was expected to be 42.7% by year-end.

B. Special Controls for the LJM Partnerships

I will now focus on the Finance Committee's involvement in the approval and oversight of the LJM partnerships.

The press and others have reported repeatedly that Enron's Board "waived the Code of Conduct" when it permitted Enron's Chief Financial Officer, Andrew Fastow, to serve as general partner of LJM1 and LJM2. The Board did not.

For many years before the LJM matters were brought to the Board, Enron maintained a Code of Conduct for its employees, which required each employee to certify in writing annually as to his or her compliance.

Enron's Code of Conduct permits the Chief Executive Officer to make a determination that an officer's investment does not present a conflict of interest. The Code of Conduct provides as follows:

> "The Chairman of the Board and Chief Executive Officer of Enron Corp. shall consider carefully the summary of relevant facts, and if he concludes that there appears to be *no probability of any conflict of interest* arising out of the proposed investment the officer or employee shall be so notified and may then make the proposed investment in full reliance upon the findings of the Chairman of the Board and Chief Executive Officer of Enron Corp." (emphasis added)

As the Board minutes of June 28, 1999 state, when LJM1 was approved, the Board adopted and ratified the determination by the Office of the Chairman "that participation of

Andrew S. Fastow as managing partner/manager of the [LJM] partnership will not adversely affect the interests of the Company." This Board action followed a presentation describing the business purpose of LJM1 and the significant financial benefits therefrom to Enron. The Board was told that PricewaterhouseCoopers "would be rendering a fairness opinion" and that Mr. Fastow would have "no direct pecuniary interest in the Company's stock" which provided credit support to the partnership. This transaction was disclosed in Enron's June 30, 1999 and in succeeding Form 10-Qs and 10-Ks, including the related party aspect. Arthur Andersen reviewed the transaction as part of its review of the June 30, 1999 10-Q.

At the October 10, 1999 Finance Committee meeting and the Board meeting on October 11, Mr. Fastow presented an update on the financial benefits from LJM1, and recommended, to obtain quick, flexible equity to Enron with reduced transaction costs, that he be permitted to organize LJM2, a new fund with outside investors (and him as managing partner) to be an "additional, optional source of private equity." He proposed that the Chief Accounting Officer review and approve all transactions with LJM2. The Committee, upon questioning, learned that Arthur Andersen was "fine with" the partnership structure, and that LJM2's limited partners -- expected to be institutional investors -- would be able to remove Mr. Fastow without cause. The Finance Committee augmented these controls by requiring that the Chief Risk Officer also review and approve all transactions and that the Board's Audit and Compliance Committee review all transactions annually and make any recommendations it deemed appropriate. Thereafter, upon management's recommendation, and after mandating additional controls, the Board ratified the Office of the Chairman's determination that Mr. Fastow's participation "will not adversely affect the interest of the Company." LJM2 was disclosed as a related party transaction in Enron's 1999 and 2000 Forms 10-K and the 2000 Proxy Statement.

Updates given to the Finance Committee about the LJM transactions were positive. At the May 1, 2000 Finance Committee meeting, prior to a discussion of the proposed "Raptor" hedging transaction, Mr. Fastow reported that "he had hired individuals to manage the investment vehicles [LJM1 and LJM2] and that he personally was devoting approximately three hours a week to the investment vehicles." We were also told that LJM2's investments had a "projected rate of return of 17.95%." Mr. Causey, the Chief Accounting Officer, told the Finance Committee that "Arthur Andersen, LLP had spent considerable time analyzing . . . the governance structure of LJM2 and was comfortable . . . ." We now know from the Powers Committee report that the LJM2 investors were receiving much higher returns.

The minutes of the October 6, 2000 Finance Committee show that the Finance Committee continued to focus on Mr. Fastow's dual role. Mr. Fastow described to the Committee six of the mechanisms that "*had been put in place* to mitigate any potential conflicts," (emphasis added) one of which was that "Messrs. Buy, Causey and Skilling approve all transactions between the Company and the LJM funds." A second was that Mr. Fastow maintained his fiduciary duty to Enron. In addition to the controls that Mr. Fastow described, the Committee instructed management that Mr. Fastow's compensation be reviewed by the Board's Compensation and Management Development Committee and that transactions between the Company and the LJM funds be reviewed quarterly by the Finance Committee in addition to the annual review by the Audit Committee.

The Finance Committee received its first quarterly, and the Audit and Compliance Committee received its second annual, report on the related party transactions with LJM on February 12, 2001 from the Chief Accounting Officer. Arthur Andersen was present at the Audit Committee meeting when these matters were discussed. Mr. Causey discussed the "Board-established guidelines for transacting with LJM." He then reviewed compliance with the Board guidelines, informing them that "The Company has adopted the following procedures and controls in response to the Board's direction," and listed them. Finally, he reviewed with the Committees the "Checklist review complemented by the adoption of additional controls." Mr. Causey informed the Finance Committee that the controls "had been discussed with the Audit and Compliance Committee, and commented that the process was working effectively."

The preceding, I submit, illustrates that the Board applied Enron's Code of Conduct when it ratified management's recommendation regarding LJM1 and LJM2, and added substantial additional controls to ensure that all of the Enron/LJM transactions would be in the best interests of the company. The record also indicates that the directors regularly monitored the LJM transactions and management's involvement. We asked for and repeatedly received reports which informed us that the controls were working and that there were no concerns raised either by management or our outside auditors.

C. Enron's Use of Off Balance Sheet Financing, Hedges and Forward Contracts

Enron has been criticized for its use of what are widely accepted and well-established off balance sheet financing or special purpose vehicles to raise debt and equity. This practice is common and permitted by the accounting rules (if structured correctly). Many large and well-known companies use off-balance sheet financing routinely. Leasing companies and reinsurance companies exist to provide off balance sheet financing to their customers. Enron's extensive use of off-balance sheet financing was widely known and well publicized.

The Board has also been criticized for authorizing hedge transactions that made use of Enron stock for credit support. Let me address that criticism.

Enron had within its portfolio certain highly volatile investments, such as restricted stock of Rhythms NetConnection, a high technology company. Enron was required to use mark to market accounting on its "merchant" investments. That combination of volatile investments and mark to market accounting had the potential to create instability and unpredictability in the Company's income statement. Putting in place hedges to mitigate and stabilize those risks made good business sense. In fact, companies have been sued by their shareholders because they failed to put in place hedges on significant and volatile investments.

The Board was presented by management with a plan to hedge these investments with an under-utilized asset. We were told that Enron had significant unrealized value in forward contracts previously issued on its own stock. These forward contracts were written by Enron in order to hedge the expense of Enron's stock-based incentive compensation plan. In simple terms, Enron wrote forward contracts to purchase its stock in the future at present prices to protect itself against the risk that its stock would appreciate in value and thus make its incentive compensation plan more expensive. I understand this to be a common business practice.

Management wanted, appropriately, to use that unrealized value most effectively for the benefit of the shareholders. It informed the Board that the proposed transaction was the best way to do so. We were informed at the same time that the transaction would be the subject of a fairness opinion by PriceWaterhouse Coopers. We were also aware that Arthur Andersen would be reviewing the transaction in connection with its review of the June 30, 1999 10Q and had no reason to believe, either at the time we approved the transaction or at any subsequent time, that Arthur Andersen was troubled by the transaction or its accounting treatment.

We believed that the Raptor I transaction, which was presented to the Finance Committee on May 1, 2000, was quite similar structurally to the original LJM hedge transaction. By that time, Arthur Andersen had certified the 1999 10K, and our inside and outside attorneys had, we believed, approved the disclosure. The minutes disclose that during that meeting, Mr. Causey "stated that Arthur Andersen LLP; had spent considerable time analyzing the [Raptor] structure and the governance structure of LJM2 and was comfortable with the proposed transaction."

The use of forwards on Enron stock in Rhythms Net and the Raptor transactions was disclosed in Enron's public filings, in disclosures that we believed had been reviewed and approved by both Arthur Andersen and Vinson & Elkins, our regular outside securities counsel.

The transactions that were presented to us—and many were not—were presented as valid economic hedges of Enron's risks, using the gains in the Enron stock forward positions. I want to make clear that I never understood, and was not told, that the business purpose of entering into the LJM transactions was to create fictitious earnings. Quite the contrary, I was told that the LJM transactions were being undertaken to hedge the risks and volatility of our assets, and to assist Enron in obtaining additional third-party debt and equity capital on favorable terms to Enron shareholders to support the company's growth.

III. CONCLUSION

What happened at Enron has been described as a systemic failure. I see it instead as a cautionary reminder of the limits of a director's role. We served as directors of what was a large and complex corporation. A director's role, by its nature, is a part-time job. It also was necessarily defined by the nature of Enron's enterprise—which was worldwide in scope, employed more than 20,000 people, and engaged in a vast array of trading and global development activities.

By force of necessity, we could not know personally all of the employees. As we now know, key managers and employees whom we thought we knew proved to disappoint us significantly. And outside advisors, whom we believed to be critical components of an effective oversight role, failed in their duties.

Take, for example, the Raptor restructure. As has been disclosed in the press, on February 5, 2001, Arthur Andersen held an internal meeting in which it expressed significant concern about the credit capacity of the Raptor vehicles and the quality of the earnings being attributed to them. Just one week later, however, with full knowledge of the Raptor credit problems, Arthur Andersen assured the Audit Committee that Enron would receive a clean audit opinion on its financials. Andersen also told the Audit Committee that there were no material weaknesses in Enron's internal controls—even though one week earlier its auditors had discussed, but not shared with the Board, the fact that the controls imposed by the Board for these related party transactions were not being followed.

Had the Raptor restructure been presented to the Board, I believe the Board might well have chosen the alternative - to shut down the Raptors - which also would have by definition avoided the accounting error related to issuance of new equity which accounted for the bulk of the $1.2 billion reduction in shareholders' equity we took in October. I find the failure of management to come forward in this mater to be particularly tragic.

Arthur Andersen's failure to disclose its concerns to the Board, as well as management's marked disregard for the required internal controls and lack of candor with respect to information owed to us, deprived the Board—and deprived me—of the ability to deal proactively with this problem. We cannot, I submit, be criticized for failing to address or remedy problems that were concealed from us.

Three months ago, days after release of the Powers' Report, I appeared before a House Subcommittee. At that time, I was deeply disturbed and disappointed with what I had read. I also squarely disagreed with certain conclusions in the Report, especially about the directors' judgment and oversight, which disagreement I expressed during my testimony. Even with the benefit of a few more months to review these issues, I remain resolute in my belief that we directors were diligent and dedicated to our charge. Based upon the recommendations, advice, and information we received from management and our advisors, we acted in good faith and attempted to pursue the best interests of Enron and its shareholders. I deeply wish, however, that at least one person—management, employee, or outside advisory - had come forward to the Board with his or her concerns when we could have addressed them.

I am prepared to respond to any questions from the Subcommittee.
Thank you.

EXCERPTS FROM THE MINUTES OF THE
JUNE 28, 1999
SPECIAL MEETING OF THE BOARD OF DIRECTORS
ENRON CORPORATION

MINUTES
SPECIAL MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
June 28, 1999

Minutes of a special meeting of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 10:00 a.m., C.D.T., on June 28, 1999, at the Enron Building in Houston, Texas.

The following Directors were present, either in person or by telephone conference connection, where each participant could hear the comments of the others and join in the discussion, constituting a quorum:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Dr. John Mendelsohn
Mr. Jerome J. Meyer
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

Director Ronnie C. Chan was absent from the meeting. Messrs. James V. Derrick, Jr. and Andrew S. Fastow, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, were also in attendance. Messrs. Richard B. Buy, Daniel R. Castagnola, James A. Hughes, and Joseph W. Sutton joined the meeting in progress as noted below.

Mr. Lay called upon Mr. Skilling to discuss a proposed investment partnership. Mr. Skilling noted that due to changes in the accounting treatment of off-balance sheet transactions the Company had been analyzing new types of financing vehicles. He called upon Mr. Fastow to discuss the proposal.

Mr. Fastow discussed certain challenges the Company is facing regarding hedging its investment in Rhythms NetConnections ("Rhythms"), a high-speed data communication services company in which the Company holds an equity position, and increasing the liquidity in its Merchant Portfolio. He noted that the Company has certain special purpose vehicles ("SPV") that have significantly appreciated in value due to holdings of forward contracts on the Company's stock. He proposed establishing a non-Enron investment partnership ("LJM") with outside investors. The Company would transfer the in-the-money value of a forward contract currently held in a SPV into LJM. LJM would pay the Company $50 million and enter into a swap with the Company to hedge the investment in Rhythms. In addition, LJM may negotiate with the Company regarding the purchase of additional assets in the Merchant Portfolio. Mr. Fastow stated that he would serve as the General Partner of LJM but have no direct pecuniary interest in the Company's stock. A copy of Mr. Fastow's presentation is filed with the records of the meeting.

A discussion ensued with Messrs. Derrick, Fastow, Lay, and Skilling answering questions from the Directors regarding Mr. Fastow's involvement in the partnership and the economics of the transaction. Mr. Fastow noted that PricewaterhouseCoopers LLP would be rendering a fairness opinion that, in their

RESOLVED FURTHER, that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Conduct of Business Affairs/Investments and Outside Business Interests of Officers and Employees that participation of Andrew S. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company;

EXCERPTS FROM THE MINUTES OF THE
OCTOBER 11, 1999
MEETING OF THE FINANCE COMMITTEE OF
THE BOARD OF DIRECTORS
ENRON CORPORATION

MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
October 11, 1999

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 4:30 p.m., C.D.T., on October 11, 1999 at the Enron Building in Houston, Texas.

The following Committee members were present constituting a quorum:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Jerome J. Meyer
Mr. John A. Urquhart

Committee member Ronnie C. Chan was absent from the meeting. Directors Ken L. Harrison, Kenneth L. Lay, Charles A. LeMaistre, and Jeffrey K. Skilling, Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, David B. Gorte, Mark E. Koenig, Jeffrey McMahon, Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, also attended the meeting.

Mr. Fastow then updated the Committee on a financing structure approved earlier in the year. LJM 1, and discussed the benefits that the Company had incurred since the transaction closed on June 30, 1999. He recommended that the Company continue to syndicate capital investments to address the funds flow issue. He presented information concerning an unaffiliated investment partnership, LJM 2, and discussed the rationale and benefits of the proposed partnership. He stated that the partnership could possibly provide the Company with an alternative, optional source of private equity to manage its investment portfolio risk, funds flow, and financial flexibility. He noted that he would be acting as managing partner of LJM 2 and discussed his role in the LJM 2 partnership and how it would benefit the Company. He commented on the differences between LJM 1 and LJM 2, the controls that would be put in place to manage any transactions between the Company and LJM 2, the fund fees and promote, and any required disclosure. He noted that the controls include review and approval of all transactions by the Chief Accounting Officer and the Chief Risk Officer of the Company. He stated that the Audit and Compliance Committee would, on an annual basis, review all transactions completed within the past year and make any recommendations they deemed appropriate. He noted that the Company's Conduct of Business Affairs Policies (relating to investments and outside business interests of officers and employees) would prohibit him from participating in LJM 2 as managing partner due to his position as Executive Vice President and Chief Financial Officer of the Company, absent appropriate reviews and waivers from the Board and a finding that such participation does not adversely affect the best interests of the Company. He asked that the Committee recommend to the Board that such review and findings be made in this instance to allow his participation. Messrs. Causey, Fastow, and Skilling answered questions from the Committee concerning the role of other partners, the review by Arthur Andersen LLP, and the benefits to the Company, which included having another potential buyer of assets and provider of capital, of having Mr. Fastow act as managing partner. Following a discussion, upon motion duly made by Mr. Meyer, seconded by Mr. Blake, and carried, the proposed waiver of the aforementioned policy, including findings of no adverse effects to the best interests of the Company related to Mr. Fastow's involvement in LJM 2, was approved for recommendation to the Board. A copy of Mr. Fastow's report is filed with the records of the meeting.

LJM 2 Summary

LP will be traditional pension funds

- Follow-on private equity fund to LJM1 bring quick flexible equity

- Purpose: Alternative, optional source of private equity for Enron to manage its investment portfolio risk, funds flow, and financial flexibility

- Major differences from LJM1:
  - No forward contracts / value from Enron contributed
  - No business relationships between Enron and LJM2 at close
  - Size: target $200+ million institutional private equity
  - GP investment: 1% of committed capital

- Controls
  - R. Causey to approve all transactions between Enron and LJM1/LJM2

- Compensation / Disclosure
  - No compensation from Enron to A. Fastow
  - LJM2 has typical private equity fund fees and promote
  - No related party disclosure expected at close. Related party disclosures specific to asset sales probably required.

- Finance Committee / Board of Directors action requested
  - Ratify decision of Office of the Chairman to waive Code of Conduct in order to allow A. Fastow participation in LJM2 as General Partner

Blake - Has AA reviewed Causey. yes, they're fine w/ it.
Blake - Still concerned about conflict of interest Causey - Gave LP enough authority to keep Andy from having too much power. LP can remove GP w/out cause.

ENRON
Finance Committee Meeting
1999/JM-10/99

**EXCERPTS FROM THE MINUTES OF THE
OCTOBER 11, 1999
MEETING OF THE BOARD OF DIRECTORS
ENRON CORPORATION**

MINUTES
MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
October 11-12, 1999

Minutes of a meeting of the Board of Directors of Enron Corp. ("Company") noticed to begin at 7:00 p.m., C.D.T., but actually begun at 7:20 p.m., C.D.T., on October 11, 1999 at the Four Seasons Hotel, Whitney Room, in Houston, Texas.

The following Directors were present, constituting a quorum:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Ms. Rebecca P. Mark
Dr. John Mendelsohn
Mr. Jerome J. Meyer
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

Director Ronnie C. Chan was absent from the meeting. The meeting was begun in executive session, during which Messrs. Richard A. Causey, Andrew S. Fastow, Mark E. Koenig, Jeffrey McMahon, and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, and Messrs. Paulo V. Ferraz Pereira and Frank Savage, candidates for election to the Company's Board of Directors, were also in attendance.

Mr. Winokur then discussed information concerning an unaffiliated investment partnership, LJM 2, and stated that the partnership could possibly provide the Company with an alternative, optional source of private equity to manage its investment portfolio risk, funds flow, and financial flexibility. He noted that Mr. Andrew S. Fastow would be acting as the managing partner of LJM 2 and discussed Mr. Fastow's role in the LJM 2 partnership. He commented on the controls that would be put in place to manage any transactions between the Company and LJM 2 and noted that the Company and LJM 2 were not obligated to one another in any way. He noted that the controls include review and approval of all transactions by the Chief Accounting Officer and the Chief Risk Officer of the Company. He stated that the Audit and Compliance Committee would, on an annual basis, review all transactions completed within the past year and make any recommendations they deemed appropriate. He stated that the Company's Conduct of Business Affairs Policies (relating to investments and outside business interests of officers and employees) would prohibit Mr. Fastow from participating in LJM 2 as managing partner due to his position as Executive Vice President and Chief Financial Officer of the Company, absent appropriate reviews and waivers from the Board and a finding that such participation does not adversely affect the best interests of the Company. He recommended that such review and findings be made in this instance. his motion was duly seconded by Mr. Urquhart. and carried. and the following resolutions were approved:

WHEREAS. Andrew S. Fastow serves as the Executive Vice President and Chief Financial Officer of the Company:

WHEREAS. Mr. Fastow has the opportunity to participate in the formation of an investment partnership (the "Partnership") that would not be affiliated with the Company:

WHEREAS. it is anticipated that Mr. Fastow will serve as the managing partner/manager of the Partnership:

WHEREAS. it is anticipated that the Partnership will invest in energy and communications-related businesses and assets. including businesses and assets of the Company:

WHEREAS. the Partnership. as a potential ready purchaser of the Company's businesses and assets or as a potential contract counterparty. could provide liquidity. risk management. and other financial benefits to the Company:

WHEREAS. the Office of the Chairman of the Company has determined. for the foregoing reasons. that Mr. Fastow's participation as the managing partner/manager of the Partnership will not adversely affect the interests of the Company:

NOW. THEREFORE IT IS RESOLVED. that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Conduct of Business Affairs/Investments and Outside Business Interests of Officers and Employees that participation of Mr. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company: and

**EXCERPTS FROM THE MINUTES OF THE
MAY 1, 2000
MEETING OF THE FINANCE COMMITTEE OF
THE BOARD OF DIRECTORS
ENRON CORPORATION**

MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP
MAY 1, 2000

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 4:00 p.m., C.D.T., but actually begun at 4:10 p.m., C.D.T., on May 1, 2000 at the Enron Building in Houston, Texas.

The following Committee members were present:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Frank Savage

Committee members Ronnie C. Chan, Jerome J. Meyer, Paulo V. Ferraz Pereira, and John A. Urquhart were absent from the meeting. Directors John H. Duncan, Ken L. Harrison, Kenneth L. Lay, and Jeffrey K. Skilling, Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, Ben F. Glisan, Jr., David B. Gorte, Mark E. Koenig, Jeffrey McMahon, Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, also attended the meeting.

Mr. Fastow then gave the Committee an update on LJM2 transactions with the Company including the level of capital commitments, number of investors, number and dollar value of investments already completed, and the Company's business units that had transacted with LJM2. He commented on the direct and indirect impact of LJM1 and LJM2 ('the investment vehicles") on the Company's earnings and funds flow. He stated that he had hired individuals to manage the investment vehicles and that he personally was devoting approximately three hours a week to the investment vehicles. He then called upon Mr. Glisan to discuss Project Raptor.

Mr. Glisan stated that Project Raptor involved establishing a risk management program to enable the Company to hedge the profit and loss volatility of the Company's investments. He discussed the highlights of Project Raptor including the establishment of a non-affiliated vehicle ("Talon") as a hedge counterparty to selected investments, the mechanism for funding Talon, and the level of hedging protection Talon could initially provide the Company. He reviewed the structure of Talon and the amount of capital that would be contributed by LJM2. Mr. Causey joined the discussion and stated that Arthur Andersen LLP had spent considerable time analyzing the Talon structure and the governance structure of LJM2 and was comfortable with the proposed transaction. Mr. Glisan then discussed Project Raptor's risk and potential mitigants to those risks. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Savage, and carried, Project Raptor was approved for recommendation to the Board.

LJM2 Update

- $386 million of capital commitments
- 33 investors including pension funds, insurance companies, banks, private funds, individuals
- 7 investments to date 5 different business units
  - $139 million
  - All purchased from Enron
  - Projected IRR of investments = 17.95% - not leveraged
  - 5 different business units

Provide capital very quickly b/c of prior knowledge of the transactions

Direct and indirect LJM impact (including LJM1)

- Earnings = $229.5 million
- Funds flow = $2,077.4 million
- Fee savings = $2.3 million
- LJM2 provided marketing "backstop" on 3 occasions
- Q4 1999: 8 days/6 deals/$125 million

Andy discussed his time commitment Approx. 3 hrs. a week spent

ENRON®

Finance Committee Meeting 04/00

**EXCERPTS FROM THE MINUTES OF THE
OCTOBER 6, 2000
MEETING OF THE FINANCE COMMITTEE OF
THE BOARD OF DIRECTORS
ENRON CORPORATION**

MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
OCTOBER 6, 2000

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 10:00 a.m., E.D.T, but actually begun at 10:35 a.m., E.D.T., at The Breakers, Ponce de Leon III Ballroom, Palm Beach, Florida.

All of the Committee members were present, either in person or by telephone conference connection, where each member could hear the comments of the other participants and join in the discussion, as follows:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. Jerome J. Meyer
Mr. Paulo V. Ferraz Pereira
Mr. Frank Savage
Mr. John A. Urquhart

Directors Duncan, Gramm, Lay, LeMaistre, Mendelsohn, and Skilling, Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, Ben F. Glisan, Jr., David B. Gorte, Mark E. Koenig, Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, and Mr. Richard N. Foster, of McKinsey & Company, Inc., also attended the meeting.

Mr. Fastow then discussed the Company's private equity strategy and noted that there would be continued significant capital investments by the Company, some of which would not generate cash flow or earnings for a number of years. He stated that this would necessitate syndication of capital investments if the Company were to continue to grow. He discussed the Company's current total assets and the total assets when unconsolidated affiliates were included. He then noted that management was proposing transacting with a new private equity fund, LJM3, and discussed the Company's rationale for transacting with the fund. He reviewed LJM1 and LJM2, equity funds previously approved by the Board that the Company was already transacting with, and noted the dates of formation, the amount of equity in the funds, and the projects that the funds had invested in. He then discussed how his role in the LJM funds could potentially create a conflict of interest in that he negotiates for the LJM funds when they are making investments in the Company's transactions/business, he receives value from the LJM funds if they perform well, and he must allocate a certain amount of his time to the funds. He then discussed the mechanisms that had been put in place to mitigate any potential conflicts including: 1) his fiduciary responsibilities to the Company, 2) the Office of the Chairman or the Board could ask him to resign from the LJM funds at any time, 3) Messrs. Buy, Causey, and Skilling approve all transactions between the Company and the LJM funds, 4) there is an annual Audit and Compliance Committee review of the Company's transactions with the LJM funds, 5) a review of his economic interest in the Company and the LJM funds is presented to Mr. Skilling, and 6) there is no obligation for the Company to transact with the LJM funds.

Messrs. Causey and Skilling then discussed the benefits to the Company of having the ability to transact with the LJM funds and Mr. Fastow discussed the other investors in the LJM funds. Mr. Blake proposed that the Finance Committee also review transactions between the Company and the LJM funds on a quarterly basis and Mr. Winokur proposed that the Compensation and Management Development Committee review the compensation received by Mr. Fastow from the LJM funds and the Company. The Committee unanimously agreed to the two proposals.

Mr. Fastow noted that in order to allow him to participate as the General Partner of the LJM funds it would be appropriate for the Committee to recommend to the Board the ratification of a decision by the Office of the Chairman that Mr. Fastow's participation in the LJM funds, with the noted conflict mitigation mechanisms in place, would not adversely affect the best interests of the Company. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Meyer, and carried the proposal was approved for recommendation to the Board.

EXCERPTS FROM THE MINUTES OF THE
FEBRUARY 12, 2001
MEETING OF THE FINANCE COMMITTEE OF
THE BOARD OF DIRECTORS
ENRON CORPORATION

MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
FEBRUARY 12, 2001

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 4:00 p.m. C.S.T., but actually begun at 4:05 p.m., C.S.T., at the Enron Building, Houston, Texas.

The following Committee members were present constituting a quorum:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Ronnie C. Chan
Mr. Jerome J. Meyer
Mr. Paulo V. Ferraz Pereira
Mr. Frank Savage
Mr. John A. Urquhart

Committee member Norman P. Blake, Jr. was absent from the meeting. Directors Wendy L. Gramm, Ken L. Harrison, Kenneth L. Lay, John Mendelsohn, and Jeffrey K. Skilling, Messrs. William S. Bradford, Richard B. Buy, Richard A. Causey, Timothy A. DeSpain, Andrew S. Fastow, Ben F. Glisan, Jr., David G. Gorte, Mark E. Koenig, and Jordan H. Mintz, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, and Mr. Richard N. Foster, of McKinsey & Company, Inc., also attended the meeting.

Mr. Glisan reviewed the liquidity report as of January 29, 2001 and noted that the Company's total liquidity was currently over $8.3 billion. He then reviewed the Company's outstanding letters of credit and discussed the changes since year end. He presented the Company's guarantee portfolio as of year end and noted that required guarantees continued to be higher than normal due to the significant increase in the volumes transacted by the Company. He then stated that there had not been any change in the Company's ratings by the rating agencies but noted that the Company was working on being upgraded to "positive outlook" by Standard & Poors.

Mr. Winokur called upon Messrs. Causey and Fastow to review the Company's procedures regarding transactions with LJM and the transactions completed in 2000. Mr. Fastow began with a discussion of the Company's utilization of the LJM vehicles. Mr. Causey reviewed each of LJM's investments with the Company that were made during 2000. He categorized the investments into four areas, balance sheet, hedges, income statement, and other, and presented a brief description of each transaction and the notional dollar amount. He then reviewed the Company's internal policies and procedures that were in place to monitor transactions between the Company and LJM, stated that the items had also been discussed with the Audit and Compliance Committee, and commented that the process was working effectively. He also noted that the Company had implemented supplemental efforts to complement the Board-established guidelines regarding transactions between the Company and LJM.

There being no further business to come before the Committee, the meeting was adjourned at 5:45 p.m., C.S.T.

Rebecca C. Carter
Secretary

APPROVED:

Chairman

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EXCERPTS FROM THE MINUTES OF THE
FEBRUARY 12, 2001
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE OF
THE BOARD OF DIRECTORS
ENRON CORPORATION

DRAFT

MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
FEBRUARY 12, 2001

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 1:30 p.m., C.S.T., but actually begun at 1:40 p.m., C.S.T., on February 12, 2001 at the Enron Building, Houston, Texas.

All of the Committee members were present as follows:

Dr. Robert K. Jaedicke, Chairman
Mr. Ronnie C. Chan
Dr. Wendy L. Gramm
Dr. John Mendelsohn
Mr. Paulo V. Ferraz Pereira
Lord John Wakeham

Directors Kenneth L. Lay and Jeffrey K. Skilling, Messrs. Robert H. Butts, Richard B. Buy, Richard A. Causey, James V. Derrick, Jr., Shawn Kilchrist, Mark E. Koenig, Tod A. Lindholm, and Jordan H. Mintz and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, Messrs. Thomas H. Bauer and David B. Duncan, of Arthur Andersen LLP ("AA"), and Mr. Richard N. Foster of McKinsey & Company, Inc. also attended the meeting.

Dr. Jaedicke called upon Mr. Duncan to begin AA's presentation, a copy of which is filed with the records of the meeting. Mr. Duncan began by providing an update of the status of AA's audit and the communications required by AA under

the Statement on Auditing Standards 61, "Communication with Audit Committees". He noted that AA's financial statement opinion was expected to be unqualified and that there were no significant audit adjustments, new accounting policies, changes not previously communicated to the Committee, modifications to interim financial information, disagreements with management, significant difficulties encountered during the audit, major issues discussed with management affecting retention, or consultation with other accountants on the application of Generally Accepted Accounting Principles ("GAAP").

Mr. Duncan then discussed AA's opinion on the Company's internal controls and stated that the opinion would be unqualified, the audit was complete, and no material weaknesses had been identified. He stated that Mr. Kilchrist would discuss certain areas where improvement opportunities had been identified. He noted that AA had made its annual determination that, in its professional judgement, it remained independent. He then discussed the status of any adjustments proposed by AA that were not made and noted that management had determined that the items were not material to the Company's financial statements taken as a whole and that AA had concurred.

Mr. Duncan then provided selected observations regarding the Company's accounting procedures and financial reporting. He stated that the Company continued to utilize highly structured transactions, such as securitizations and syndications, in which there was significant judgement required in the application of GAAP. He commented on the use of mark-to-market and fair value model accounting in the areas of trading and derivative contracts and stated that these also required significant judgement regarding the applicability of certain models to specific products or transactions. He then reviewed related party transactions, classification issues that had arisen during the year, and certain other areas requiring material judgments to be made.

Mr. Causey then began a discussion of transactions with LJM during 2000. He stated that the Company had established internal policies and procedures to deal with related party transactions such as LJM. He reviewed the Board established guidelines for transacting with LJM and then began a discussion of the

Company's compliance with the guidelines. He stated that, in response to the Board's direction, the Company had adopted the following procedures and controls: 1) an LJM Deal Approval Sheet ("DASH") was prepared for every transaction between the Company and LJM with approval required by a variety of senior-level Company professionals in the commercial, technical, and commercial support areas and 2) the DASH was supplemented by an LJM Approval Process Checklist that tested for compliance with the Board's directive for transacting with LJM. He then stated that the Company had implemented supplemental efforts regarding transactions with LJM including the following: 1) LJM senior professionals do not ever negotiate on behalf of the Company, 2) Company professionals negotiating with LJM report to senior Company professionals separate from Mr. Andrew S. Fastow, 3) numerous groups monitor compliance with procedures and controls and regularly update him and Mr. Buy, and 4) the Company regularly consults with internal and outside counsel regarding disclosure obligations. He then presented all of the transactions between the Company and LJM during 2000, gave a brief description of each transaction, and noted the notional amount. He noted that the majority of the transactions were non-earnings related and were primarily related to deconsolidations, securitizations, or monetizations.

EXCERPTS FROM THE MINUTES OF THE AUGUST 13, 2001 MEETING OF THE BOARD OF DIRECTORS ENRON CORPORATION

Balance Sheet Debt

($ in millions)

	June YTD 2000	2001 June YTD	2001 Full Year	Estimate
Opening Debt Balance	$ (8,152)	$ (10,229)	$ (10,229)	
Funds Flow from Operations	(23)	1,883	3,000	
Change in Working Capital *	(174)	(500)	712	
Changes in Deposit / Margin Activity	(350)	(2,642)	(2,642)	
Proceeds from Sales of Assets	105	1,345	1,385	
Capital Expenditures	(1,009)	(1,200)	(1,910)	
Equity Investments	(1,350)	(1,384)	(1,551)	
Dividends	(265)	(256)	(544)	
(Increase)/Decrease in Cash on Hand	(430)	527	527	
Other	(49)	(356)	(352)	
Period Activity	(3,545)	(2,583)	(1,375)	
Period Ending Debt Balance	$(11,697)	$ (12,812)	$ (11,604)	
Key Credit Ratios				
Funds Flow / Interest	0.95	4.91	4.08	
Debt / Balance Sheet Capital	46.3%	46.0%	42.7%	

* Excluding Deposit/Margin Activity

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Net Income

($ in millions)

	Second Quarter		Six Months	
	Plan	Actual	Plan	Actual
Transportation & Distribution				
Transportation & Storage	$ 37	$ 37	$ 95	$ 97
Portland General Group	-	27	48	59
Wholesale				
Americas	174	756	351	1,289
Europe	47	34	82	86
Global Markets	33	9	52	27
Industrial Markets	4	8	10	14
Global Assets	45	(4)	80	(1)
Other Wholesale	20	(397)	96	(575)
Enron Energy Services	25	33	52	52
Enron Broadband Services	(10)	(69)	(35)	(90)
Corporate and Other	(6)	1	(45)	(85)
Azurix	(20)	(31)	(37)	(63)
Recurring Net Income	$349	$ 404	$ 749	$ 810

STATEMENT OF DR. ROBERT K. JAEDICKE

Before the Permanent Subcommittee on Investigations
The Committee on Government Affairs
U.S. Senate
May 7, 2002

Chairman Levin, Senator Collins, and Members of the Subcommittee. Good morning, and thank you for the opportunity to address the Subcommittee.

My name is Robert Jaedicke. I served as the Chairman of the Audit Committee of the Board of Directors of Enron Corporation. As part of an overall restructuring of the Board, I recently resigned as a director, having served since the mid-1980s.

Let me briefly tell you about my background. I joined the faculty of the Stanford Graduate School of Business in 1961. I served as Dean of the Business School from 1983 until 1990. At that time, I returned to the faculty of the Business School, and retired in 1992.

I. THE AUDIT COMMITTEE OF THE BOARD OF DIRECTORS

Throughout my tenure as Chairman of the Enron Board's Audit Committee, I was committed to ensuring that it was an effective and actively functioning body. Over the last few years, we undertook to review and strengthen our already vigorous control systems. In 1999, we began a number of initiatives to ensure that we remained a "best practices" Audit Committee. Throughout 2000 and into 2001, our Committee worked with Arthur Andersen to make certain we complied with the recommendations of the Securities and Exchange Commission, the New York Stock Exchange, and the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees. That effort culminated in February 2001, when the Audit Committee drafted a new charter that was approved by the full Board. Throughout that lengthy process, involving both Enron management and Arthur Andersen, we implemented a series of further refinements to our corporate policies and controls.

The lifeblood of the work of any Audit Committee is the development and implementation of adequate controls, many of which cross check each other. The Committee's responsibility is to receive reports from management and the outside auditors, to review the adequacy of internal controls, and to oversee the filing of financial statements. The Committee's effective oversight also depends on the full and complete reporting of information to it. Without full and accurate information, an Audit Committee cannot be effective. The Committee does not manage the Company and does not do the auditing. It is my understanding that the audit committees of most corporations like Enron typically meet for a few hours several times a year. As Warren Buffet wrote to New York Stock Exchange Chairman and CEO Richard Grasso in 1999, "An audit committee that meets for a few hours several times a year is simply not going to pick up anything that is missed by the outside auditors. . . . Therefore, the task of the audit committee should be to hold the feet of the outside auditors to the fire." In that same letter, Mr. Buffett also stated, "Simply put, audit committees cannot act as auditors. Their true job—and I would argue the only important function that they can adequately discharge—is to make sure that the auditors do their job instead of becoming subservient to management."

I agree. As Chairman of the Audit Committee, I believe that our duty was to ensure that the outside auditors were in a position to perform their independent auditing function with full cooperation from management and with no management-imposed constraints on the audit scope. We regularly reviewed Arthur Andersen's independence, whether they had disagreements with management, and whether they had the appropriate control over access issues and accounting treatment.

We held regular meetings at least four—and usually five—times a year at which we received reports from a broad range of senior management and Arthur Andersen personnel. Audit Committee meetings regularly included three Arthur Andersen partners, the chief accounting officer, the chief risk officer, the general counsel, the chief internal auditors, Mr. Lay, Mr. Skilling, and other senior Enron officers and outside advisors as appropriate. We were entitled to rely on the representations made to us by management, our outside auditors and advisers about the appropriateness of the accounting for the partnerships, and the adequacy of our disclosures. We asked questions, provided oversight, received several special reports on accounting policies, and continually discussed the adequacy of our internal controls. I respectfully submit that we did our job.

Three Arthur Andersen partners regularly attended each Audit Committee meeting and reported on issues of interest or concern. It was my invariable practice to hold—or at least offer to hold--an executive session with the Arthur Andersen representatives where they could meet with us without management present. There, Arthur Andersen could freely report to the Committee any matters of concern that made the auditors uncomfortable, including; whether they had had any significant disagreement with management; whether they had full cooperation of management; whether reasonably effective accounting systems and controls were in place; whether there were any material systems and controls that need strengthening; and whether they had detected instances where company policies had not been fully addressed.

Arthur Andersen did not raise concerns about the partnerships in these executive sessions. In fact, they normally reported to us that the structures and transactions were complex and required judgment, but that they were in at an early stage to understand and review the transactions and that they were comfortable with the accounting treatment.

Over the last several months, however, through the media and other public disclosures, I have learned that within the management of Enron and within Arthur Andersen, there was substantial turmoil about the related party partnerships. For example, until recently, I was unaware that:

- In February 2001, Arthur Andersen officials met among themselves and raised concerns about the accounting for the partnerships and whether the related party transactions were fair to Enron;

- In the summer of 2001, an Enron in-house attorney was sufficiently concerned about the partnerships that he consulted with a separate law firm;

- In early October 2001, Arthur Andersen retained outside counsel in anticipation of possible litigation arising from Enron's financial statements;

Contrast what Arthur Andersen knew and was doing during that time with what it was telling the Audit Committee. In a February 12, 2001 Audit Committee meeting, Arthur Andersen reported:

- Arthur Andersen's financial statement opinion for the 2000 financial statements would be unqualified. The 2000 statements would cover the first full year of existence of the LJM partnerships.

- Arthur Andersen's opinion on the company's internal controls (which should have included an assessment of the internal controls in place for related party transactions) would be unqualified and they noted no material weaknesses.

- The use of structured transactions and mark to market accounting required significant judgment, but Arthur Andersen did not suggest that anything about the judgments being made was inappropriate.

- Arthur Andersen was present when we reviewed the related party transactions, and did not indicate any impropriety or major concerns with the accounting or the fairness of the transactions.

II. THE RELATED PARTY TRANSACTIONS

I want to highlight two critical pieces of information about these related party transactions that management did not reveal to the Board. First, as the Powers Report indicates, it was never disclosed to the Board that Enron employees other than Andrew Fastow had acquired interests in, or become parties to, related party transactions with Enron.

It is also apparent that management's lack of candor was not limited simply to the non-disclosure of related party interests. We now know that certain Enron employees believed that particular transactions with the LJM entities were unfair to Enron, were an improper effort to manipulate the company's financials, or were not properly being disclosed in Enron's proxy statements and financial disclosures. These are serious issues that the employees, management, or both should have brought to the Board's attention. The one time the Board was informed that a concern had been voiced about the related party transactions, we were informed that the matter had been investigated and resolved by outside counsel.

LJM1 and LJM2 were presented to the Board as having significant benefits to Enron. The Office of the Chairman determined that the LJM structure – with Mr. Fastow as the general partner of the LJMs– would not adversely affect the interests of the company. Senior management discussed with the Board the very real and substantial benefits to Enron of such a structure. The Board thought, based upon these presentations, that the LJM partnerships offered real business benefits to Enron. Many special controls were put in place to manage the related party aspect of the partnerships. Significant and legitimate economic benefits were presented to justify why Mr. Fastow should be permitted to assume the role that we ultimately permitted him to assume.

Enron's Code of Conduct allows a senior officer to participate in a transaction in which he has a potential conflict of interest with Enron if the Office of the Chairman determines that this participation will not adversely affect the interests of the Company. Mr. Fastow was allowed to participate in LJM because the Office of the Chairman made such a determination, and the Board ratified it. This action had no affect whatsoever on Mr. Fastow's obligation to comply with all other requirements of Enron's Code of Business Conduct and its Code of Ethics as a senior officer and fiduciary of Enron.

The Audit Committee executed its responsibility of overseeing management's proper implementation of the controls and was repeatedly assured that they were being followed. The Board was told, and had every reason to believe, that the several parties with the obligation to monitor the transactions were ensuring that the procedures that the Board and the Company had put in place were followed and that transactions with LJM were fair to Enron and were accounted for properly.

The Audit Committee reviewed the LJM transactions with Enron's Chief Accounting Officer each year, in the presence of Arthur Andersen partners, Mr. Lay, Mr. Skilling, the Chief Risk Officer, and in-house counsel, and was assured that all of the transactions were done at arms length and were fair to Enron. The Board and the Audit Committee had no reason not to trust the assurances they received. Despite the existence of these controls, it is now apparent that numerous critical and troubling facts about LJM1 and LJM2 were not brought to the attention of the Board or the Audit Committee. There was ample opportunity to express concerns because the related party partnerships were discussed at meetings of the Finance and Audit Committees.

We had the following understandings about Arthur Andersen's assurances concerning these transaction:

- In the October 1999 Audit Committee meeting before the Board meeting where LJM2 was approved, Arthur Andersen assured the Audit Committee that it "had spent considerable time during the third quarter reviewing a joint venture [Enron] was forming to assist in monetizing investments."

- In presenting LJM2 to the Finance Committee in October 1999, senior management also discussed the fact that Arthur Andersen had reviewed LJM2 and were fine with it.

- In May 2000, Arthur Andersen reported to the Audit Committee that Enron's related party transactions were a "high priority" area, that Arthur Andersen "would be spending additional time" specifically on Enron's "structured transactions related to securitization and syndication and hedging vehicles." Notes that apparently were taken at the meeting reflect that Andersen reported that it "gets involved in the structure on the front end to discuss applicable accounting issues," and that Arthur Andersen typically consults with its Chicago and New York offices.

- In February 2001, Arthur Andersen reported to the Audit Committee that its "financial statement opinion was expected to be unqualified, and that there were no significant audit adjustments, . . . disagreements with management, [or] significant difficulties encountered during the audit." Arthur Andersen also discussed its "opinion on the [Enron's] internal controls and stated that the opinion would be unqualified, the audit was complete, and no material weaknesses had been identified."

Arthur Andersen often mentioned that Enron was utilizing highly complex structured transactions that required significant judgment in the application of the accounting rules. As the Audit Committee minutes reflect, Enron paid Arthur Andersen specifically to address the accounting issues related to these transactions. Arthur Andersen assured us that they were working with their experts in Chicago to make sure that Enron properly accounted for those transactions.

III. CONCLUSION

Last February, Alan Greenspan testified before Congress, "I've served on too many audit committees to know that, even though I would consider myself independent, I would consider myself knowledgeable, I did not know what questions to ask the chief financial officer during meetings to find out what is it that conceivably is going wrong in the corporation, and he wasn't about to tell me. So that there was a very difficult problem that one confronts." I agree with Mr. Greenspan. We did everything possible to ensure that our controls and procedures were being followed. To my knowledge, we were one of the few major corporations that required Arthur Andersen to give us an attest opinion on management's assertion that our internal controls were adequate.

What happened at Enron has been described as a systemic failure. As it pertains to the Board, I see it instead as a cautionary reminder of the limits of a director's role. We served as directors of what was then the seventh largest corporation in America, which required us to confine our attention to the broad policy decisions. At the meetings of the Board and its committees, in which all of us participated, these issues were considered and decided on the basis of summaries, reports and corporate records, upon which we were entitled to rely. We also reasonably relied upon the honesty and integrity of management, their subordinates and advisers, and on the integrity of the information we were receiving. At the time, we had no reason to doubt the integrity of either the management or our advisors.

We did all of this, and more. Sadly, despite all that we tried to do, in the face of all the assurances we received, we had no cause for suspicion until it was too late.

I am prepared to respond to questions from the Subcommittee.

Thank you.

EXCERPTS FROM THE MINUTES OF THE OCTOBER 11, 1999 MEETING OF THE FINANCE COMMITTEE OF THE BOARD OF DIRECTORS ENRON CORPORATION

MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
October 11, 1999

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 4:30 p.m., C.D.T., on October 11, 1999 at the Enron Building in Houston, Texas.

The following Committee members were present constituting a quorum:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Jerome J. Meyer
Mr. John A. Urquhart

Committee member Ronnie C. Chan was absent from the meeting. Directors Ken L. Harrison, Kenneth L. Lay, Charles A. LeMaistre, and Jeffrey K. Skilling, Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, David B. Gorte, Mark E. Koenig, Jeffrey McMahon, Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, also attended the meeting.

Mr. Fastow then updated the Committee on a financing structure approved earlier in the year. LJM 1. and discussed the benefits that the Company had incurred since the transaction closed on June 30. 1999. He recommended that the Company continue to syndicate capital investments to address the funds flow issue. He presented information concerning an unaffiliated investment partnership. LJM 2. and discussed the rationale and benefits of the proposed partnership. He stated that the partnership could possibly provide the Company with an alternative. optional source of private equity to manage its investment portfolio risk. funds flow. and financial flexibility. He noted that he would be acting as managing partner of LJM 2 and discussed his role in the LJM 2 partnership and how it would benefit the Company. He commented on the differences between LJM 1 and LJM 2. the controls that would be put in place to manage any transactions between the Company and LJM 2. the fund fees and promote. and any required disclosure. He noted that the controls include review and approval of all transactions by the Chief Accounting Officer and the Chief Risk Officer of the Company. He stated that the Audit and Compliance Committee would. on an annual basis. review all transactions completed within the past year and make any recommendations they deemed appropriate. He noted that the Company's Conduct of Business Affairs Policies (relating to investments and outside business interests of officers and employees) would prohibit him from participating in LJM 2 as managing partner due to his position as Executive Vice President and Chief Financial Officer of the Company. absent appropriate reviews and waivers from the Board and a finding that such participation does not adversely affect the best interests of the Company. He asked that the Committee recommend to the Board that such review and findings be made in this instance to allow his participation. Messrs. Causey. Fastow. and Skilling answered questions from the Committee concerning the role of other partners. the review by Arthur Andersen LLP. and the benefits to the Company. which included having another potential buyer of assets and provider of capital. of having Mr. Fastow act as managing partner. Following a discussion. upon motion duly made by Mr. Meyer. seconded by Mr. Blake. and carried. the proposed waiver of the aforementioned policy. including findings of no adverse effects to the best interests of the Company related to Mr. Fastow's involvement in LJM 2. was approved for recommendation to the Board. A copy of Mr. Fastow's report is filed with the records of the meeting.

LJM 2 Summary

LP will be traditional pension funds

- Follow-on private equity fund to LJM1 bring quick flexible equity

- Purpose: Alternative, optional source of private equity for Enron to manage its investment portfolio risk, funds flow, and financial flexibility

- Major differences from LJM1:
  - No forward contracts / value from Enron contributed
  - No business relationships between Enron and LJM2 at close
  - Size: target $200+ million institutional private equity
  - GP investment: 1% of committed capital

- Controls
  - R. Causey to approve all transactions between Enron and LJM1/LJM2

- Compensation / Disclosure
  - No compensation from Enron to A. Fastow
  - LJM2 has typical private equity fund fees and promote
  - No related party disclosure expected at close. Related party disclosures specific to asset sales probably required.

- Finance Committee / Board of Directors action requested
  - Ratify decision of Office of the Chairman to waive Code of Conduct in order to allow A. Fastow participation in LJM2 as General Partner

Blake - Has AA reviewed Causey. yes, they're fine w/ it.
Blake - Still concerned about conflict of interest Causey - Gave LP enough authority to keep Andy from having too much power. LP can remove GP w/out cause.

ENRON

Finance Committee Meeting
1999/JM-10/99

X.

EXCERPTS FROM THE MINUTES OF THE
OCTOBER 11, 1999
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE OF
THE BOARD OF DIRECTORS
ENRON CORPORATION

MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
October 11, 1999

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"). held pursuant to due notice at 3:00 p.m.. C.D.T.. on October 11. 1999 at the Enron Building in Houston. Texas.

The following Committee members were present constituting a quorum:

Dr. Robert K. Jaedicke, Chairman
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Dr. John Mendelsohn
Lord John Wakeham

Director Ronnie C. Chan was absent from the meeting. Directors Kenneth L. Lay and Jeffrey K. Skilling. Messrs. Robert H. Butts. Richard B. Buy. Richard A. Causey. and Theodore R. Murphy. and Mesdames Sharon A. Butcher and Rebecca C. Carter, all of the Company or affiliates thereof. and Messrs. Thomas H. Bauer. David B. Duncan. and D. Stephen Goddard. all of Arthur Andersen LLP ("AA"). also attended the meeting. Mr. Joseph W. Sutton joined the meeting in progress as noted below.

Mr. Duncan noted that in addition to the EOG and MTBE transactions, AA had spent considerable time during the third quarter reviewing a joint venture the Company was forming to assist in monetizing investments.

EXCERPTS FROM THE MINUTES OF THE
MAY 1, 2000
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE OF
THE BOARD OF DIRECTORS
ENRON CORPORATION

MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
MAY 1, 2000

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 2:00 p.m. C.D.T., on May 1, 2000, but actually begun at 2:05 p.m., C.D.T., on May 1, 2000 at the Enron Building in Houston, Texas.

The following Committee members were present constituting a quorum:

Dr. Robert K. Jaedicke, Chairman
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Dr. John Mendelsohn
Lord John Wakeham

Committee members Ronnie C. Chan and Paulo Ferraz Pereira were absent from the meeting. Directors John H. Duncan, Kenneth L. Lay, Charles A. LeMaistre, and Jeffrey K. Skilling, Messrs. Robert H. Butts, Richard B. Buy, Richard A. Causey, James V. Derrick, Jr., Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, and Messrs. Thomas H. Bauer, David B. Duncan, and D. Stephen Goddard, all of Arthur Andersen LLP ("AA"), also attended the meeting.

The Chairman, Dr. Jaedicke, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Duncan discussed the financial reporting areas that AA had determined to be high priorities due to inherent risks that were present. He stated that the ongoing high priority areas included structured transactions, the merchant portfolio, commodity trading activities, project development activities, and intercompany and related party transactions. He also commented on specific areas where AA would be spending additional time including the following: 1) the formalization of accounting models, policies, and procedures relating to Enron Energy Services, LLC ("EES"), Enron Broadband Services, Inc. ("EBS"), Enron NetWorks, and the Company's activities in Japan, 2) structured transactions related to securitizations and syndication and hedging vehicles, and 3) analyzing the impact of rulemaking activity specifically as it relates to the Company.

Summary Of Fees - Activity Overview

(millions)

Topical View

	1998	1999	1999 Comments
Recurring Baseline Audit	$ 10.0	$ 11.1	– Increase Related to Activity Growth at All Units, Most Notably ENA, Europe and EES
Expanded Accounting, Auditing and Risk Management Services			
Structured and/or Significant Transactions	7.8	12.2	– Significant Syndication and Structured Finance Activity (Condor, Marguax, LJM, Yosemite, Other) – Real-Time Deal Related Activities for Significant Transactions – EOG Disposition worked on structure w/ the company – Various M&A Projects – Registration Statements and Other Required Regulatory Reporting Activities
General Rule Application and Monitoring	2.1	3.9	– Significant Rulemaking Surrounding Trading Activities, Weather Derivatives, General Derivatives, and Other Areas – Implementation Issues Related to SFAS No. 133 (Derivatives) – EES Accounting Model Development
Risk Management Related Projects - General	1.1	3.1	– Various Special Projects (Valuation Models, IT Standards, F/X Management, etc.)
- SAP Related	2.1	2.6	– Reviews of Controls
- Y2K Related	0.3	1.6	
	$ 13.4	$ 23.4	
Other Services			
Tax - Transactions & Compliance	3.0	4.9	– 8 New Locations, 52 Locations Total
- System Implementation	1.1	1.5	– SAP Related Activities
Strategy or Profit Improvement Related	1.7	3.7	– Primarily Strategic Sourcing (Procurement) brings anticipated sav... to company. and Various EES Projects
Loaned Staff and Other	0.4	1.8	– Primarily Information Gathering Projects at EES
	$ 6.2	$ 11.9	
Totals	$ 29.6	$ 46.4	

AA gets involved in the structure on the front-end to discuss applicable accounting issues. AA typically consults w/ its Chicago & N.Y. offices

more classic consultation

ENRON

ARTHUR ANDERSEN

EXCERPTS FROM THE MINUTES OF THE
FEBRUARY 12, 2001
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE OF
THE BOARD OF DIRECTORS
ENRON CORPORATION

DRAFT

MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
FEBRUARY 12, 2001

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 1:30 p.m., C.S.T., but actually begun at 1:40 p.m., C.S.T., on February 12, 2001 at the Enron Building, Houston, Texas.

All of the Committee members were present as follows:

Dr. Robert K. Jaedicke, Chairman
Mr. Ronnie C. Chan
Dr. Wendy L. Gramm
Dr. John Mendelsohn
Mr. Paulo V. Ferraz Pereira
Lord John Wakeham

Directors Kenneth L. Lay and Jeffrey K. Skilling, Messrs. Robert H. Butts, Richard B. Buy, Richard A. Causey, James V. Derrick, Jr., Shawn Kilchrist, Mark E. Koenig, Tod A. Lindholm, and Jordan H. Mintz and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, Messrs. Thomas H. Bauer and David B. Duncan, of Arthur Andersen LLP ("AA"), and Mr. Richard N. Foster of McKinsey & Company, Inc. also attended the meeting.

Dr. Jaedicke called upon Mr. Duncan to begin AA's presentation, a copy of which is filed with the records of the meeting. Mr. Duncan began by providing an update of the status of AA's audit and the communications required by AA under

the Statement on Auditing Standards 61, "Communication with Audit Committees". He noted that AA's financial statement opinion was expected to be unqualified and that there were no significant audit adjustments, new accounting policies, changes not previously communicated to the Committee, modifications to interim financial information, disagreements with management, significant difficulties encountered during the audit, major issues discussed with management affecting retention, or consultation with other accountants on the application of Generally Accepted Accounting Principles ("GAAP").

Mr. Duncan then discussed AA's opinion on the Company's internal controls and stated that the opinion would be unqualified, the audit was complete, and no material weaknesses had been identified. He stated that Mr. Kilchrist would discuss certain areas where improvement opportunities had been identified. He noted that AA had made its annual determination that, in its professional judgement, it remained independent. He then discussed the status of any adjustments proposed by AA that were not made and noted that management had determined that the items were not material to the Company's financial statements taken as a whole and that AA had concurred.

Mr. Duncan then provided selected observations regarding the Company's accounting procedures and financial reporting. He stated that the Company continued to utilize highly structured transactions, such as securitizations and syndications, in which there was significant judgement required in the application of GAAP. He commented on the use of mark-to-market and fair value model accounting in the areas of trading and derivative contracts and stated that these also required significant judgement regarding the applicability of certain models to specific products or transactions. He then reviewed related party transactions, classification issues that had arisen during the year, and certain other areas requiring material judgments to be made.

Mr. Causey then began a discussion of transactions with LJM during 2000. He stated that the Company had established internal policies and procedures to deal with related party transactions such as LJM. He reviewed the Board established guidelines for transacting with LJM and then began a discussion of the

Company's compliance with the guidelines. He stated that, in response to the Board's direction, the Company had adopted the following procedures and controls: 1) an LJM Deal Approval Sheet ("DASH") was prepared for every transaction between the Company and LJM with approval required by a variety of senior-level Company professionals in the commercial, technical, and commercial support areas and 2) the DASH was supplemented by an LJM Approval Process Checklist that tested for compliance with the Board's directive for transacting with LJM. He then stated that the Company had implemented supplemental efforts regarding transactions with LJM including the following: 1) LJM senior professionals do not ever negotiate on behalf of the Company, 2) Company professionals negotiating with LJM report to senior Company professionals separate from Mr. Andrew S. Fastow, 3) numerous groups monitor compliance with procedures and controls and regularly update him and Mr. Buy, and 4) the Company regularly consults with internal and outside counsel regarding disclosure obligations. He then presented all of the transactions between the Company and LJM during 2000, gave a brief description of each transaction, and noted the notional amount. He noted that the majority of the transactions were non-earnings related and were primarily related to deconsolidations, securitizations, or monetizations.

STATEMENT OF DR. CHARLES A. LeMAISTRE

Before the Permanent Subcommittee on Investigations
Committee on Governmental Affairs
United States Senate
May 7, 2002

Chairman Levin, Senator Collins, and Members of the Subcommittee. Good afternoon, and thank you for the opportunity to address the Subcommittee.

My name is Charles LeMaistre. I am a physician by profession. I am also the President Emeritus of the University of Texas M.D. Anderson Cancer Center, and former Chancellor of the University of Texas System. For 17 years, I served on Enron's Board. For most of those years, I held the position of Chairman of the Compensation and Management Development Committee. I resigned in March 2002 as part of the restructuring of the Board.

I would like to address some of the questions that have been raised regarding the compensation and bonus process for Enron executives.

I. THE COMPENSATION COMMITTEE

The Compensation Committee's basic responsibility was to assure that the senior executives of the Company were compensated effectively in a manner consistent with the compensation strategy stated to the shareholders. The committee considered internal equity, competitive compensation practices, and the requirements of appropriate regulatory bodies. The philosophy behind executive compensation is to reward executive performance that creates long-term shareholder value; in essence a "pay-for-performance" philosophy. Enron executives had the opportunity to earn at the 75th percentile or higher of the compensation rates at comparable competitive companies, subject to obtaining performance at the 75th percentile or higher at Enron.

As a first step, we received detailed recommendations from management and discussed the justifications fully. We also relied, frequently, on an outside executive compensation firm, Towers Perrin, to provide advice and recommendations regarding the various compensation issues that were brought to the Committee. Based on that advice, the Committee arrived at its proposals for presentation to the Board.

In recent years, the Compensation Committee was dealing with Enron's evolution from a pipeline company to an energy trading company that engaged in sophisticated and complex financing structures. Enron sought out different talent for its senior management in the energy trading business. To hire and successfully retain these highly sought individuals, Enron needed to offer compensation packages equivalent to, or better than, those offered by the competition. Enron believed that the talented individuals leading the Company were one of its most valuable assets, and critical to its success. Towers Perrin was often asked to craft compensation packages, stress test the executive compensation plan, and conduct surveys of competitive practices to be sure Enron was well-positioned in the marketplace.

II. COMPENSATION RELATED ISSUES

A. Ken Lay

The media and others have raised many questions about Mr. Lay's compensation. In particular, I would like to address the $141 million he received in total compensation for the year 2000. It has been suggested that this level of compensation was unreasonably high and over 10 times the average received by the CEOs of top two hundred companies.

First, I believe that comparing Mr. Lay's total compensation against the average salary for a CEO in a top 200 company does not necessarily yield an accurate picture. Because Mr. Lay's compensation placed him in the top 10 highest paid CEOs, I believe that comparing his compensation to those in that category is more accurate. Within the top 10, Mr. Lay was ranked seventh. That year, Enron coincidentally was ranked as the seventh largest company. The average compensation for the top 10 CEOs was about $169 million. The top compensation was $293 million. I have attached a chart to my statement that presents this information.

Second, I think it is important to break out what comprises Mr. Lay's total compensation package to determine the actual cost to the Company for that year. A very large portion of the total compensation is at risk under the pay-for-performance philosophy. The portion at risk depends upon meeting competitive criteria for the future value realized from stock options exercised and from restricted stock payouts to be realized. For this portion, the executive is rewarded only if the shareholder is rewarded. If the "at risk" portion is subtracted from the total, you arrive at about $10 million, which I believe is a more accurate representation of Mr. Lay's 2000 compensation cost the company that year. That roughly $10 million includes a base salary of about $1.3 million and a bonus of $7 million. I also note that 2000 was an extraordinary year for Enron and its shareholders, which accounts for the large increase in his bonus from the previous year. Mr. Lay's compensation was disclosed and footnoted in detail in the Proxy Statement each year.

B. Andy Fastow's Salary from the LJM Partnerships

On October 19, 2001 the Wall Street Journal reported that Mr. Fastow, and possibly some of his partnership associates, received more than $7 million in compensation from the LJM partnerships. Let me comment on what I know about his LJM compensation.

On October 19, 2001, a special meeting of the full Board was called to discuss Mr. Fastow's compensation from the LJM and other related matters. On October 22, 2001, the Board authorized Mr. Duncan and me to inquire directly of Mr. Fastow as to his compensation from the

LJM partnerships. Enron's General Counsel drafted the questions that we would ask. I called Mr. Fastow on October 22 and arranged for a conference call the next day. On that call, Mr. Duncan and I asked Mr. Fastow about the amount of his investments in LJM1 and LJM2 and the return on those investments. Mr. Fastow responded that his commitments in LJM1 and LJM2 were $1 million and $3.9 million respectively. He stated that his income from LJM1 was $23 million, and approximately $22 million from LJM2. On October 24, 2001, Mr. Fastow was relieved of his responsibility as Chief Financial Officer.

I do not believe that the Board of Directors would ever have approved Mr. Fastow's participation in the partnerships if we had known he would be generating such compensation. If management had instituted the controls the Board installed, Mr. Fastow's compensation would have been reported to Mr. Skilling, the Audit Committee, Finance Committee, and the Compensation Committee. The October 6, 2000 Finance Committee meeting minutes clearly show, from his own presentation, that Mr. Fastow was aware of the six controls imposed by the Board on his participation in LJM, including his responsibility to review with Mr. Skilling "his economic interests in the Company and the LJM funds." Following Mr. Fastow's presentation, the Finance Committee added to the existing six controls a quarterly review of the LJM transactions and a review by the Compensation Committee of Mr. Fastow's LJM compensation.

C. Enron's Performance Unit Plan

Prior to 1999, Enron granted performance units to corporate and certain operating company executives who were not in an Enron long-term incentive plan. These operating company executives were, for the most part, in commercial support and pipeline businesses. The first performance units were awarded in 1987 and the last in 1998. Awards were based on Enron's total shareholder return over four years. The participants were nominated by the Office of the Chairman and approved by the Compensation Committee. There was a limit of 3 million performance units per individual. Performance was measured against that of a performance peer group of companies with a payout scale of 1 to 7. Each unit was assigned a valuation of $1.00. A ranking of 1 gained a payout of $2 per performance unit ("p.u."). A ranking of 7 gained a payout of $ 0.00/p.u..

In the event that the total shareholder return did not exceed the cumulative percentage for the 90-day Treasury Bill, a performance unit would have no value.

III. CONCLUSION

I believe that our Committee and the Enron Board endeavored to manage carefully and effectively Enron's executive compensation while this company was rapidly evolving, growing, and undertaking new business opportunities. The Compensation Committee sought and relied on the advice of outside executive compensation experts to ensure that our recommendations and decisions were consistent with the marketplace. Although the Board was willing to award compensation that was competitive and deserved, it certainly did not approve and was not made aware by management that some individuals reaped huge profits at the Company's expense, or that others abused certain benefits in ways for which they were not designed.

Thank you for your attention.

I will be pleased to answer questions from the Subcommittee.

Kenneth L. Lay
Compensation History

Item	2000	1999	1998	1997	1996
Salary	$1,300,000	$1,300,000	$1,266,667	$1,200,000	$990,000
Bonus	$7,000,000	$3,900,000	$3,150,000	$475,000	$1,620,864
Restricted Stock	$7,500,025		$3,883,503		
LTIP Payouts	$1,218,750				
Other Compensation	$381,551	$206,716	$160,292	$228,847	$275,155
All Other Compensation	$857,316	$560,048	$554,904	$545,264	$281,368
Total Compensation	$18,257,642	$5,966,764	$9,015,366	$2,449,111	$3,167,387
Value Realized for Options Exercised	$123,399,478	$43,845,331	$13,094,776	$1,437,500	$4,409,375
Potential Value of FYE Options	$15,275,826	$30,403,125	$8,158,912	$16,387,212	$15,791,080
Total Compensation + Realized Option Value	$141,657,120	$49,812,095	$22,110,142	$3,886,611	$7,576,762
Cash Impact Per Financial Statements	**$18,257,642**	**$5,966,764**	**$9,015,366**	**$2,449,111**	**$3,167,387**

Source: Enron DEF14a, 1996-2001.

STATEMENT OF NORMAN P. BLAKE

Before the Permanent Subcommittee on Investigations
Committee on Governmental Affairs
United States Senate
May 7, 2002

Chairman Levin, Senator Collins, and Members of the Subcommittee. Good morning, and thank you for the opportunity to address the Subcommittee.

My name is Norman Blake. I am Interim Chairman of the Board of Enron Corporation. I have been a director of Enron since 1993. Since the outset of bankruptcy, five members of the Board and I have been actively engaged in the development of a newly constituted Board of Directors in cooperation with Enron's Creditors Committee. It is the intention of these Board members and me to resign from the Board once an orderly and effective transition of authority has taken place. We are serving now on a pro bono basis and in recognition of our responsibility to serve the interests of Enron's stakeholders and employees.

My background can essentially be characterized as having had extensive management and leadership experience in a variety of different industries with significant involvement in financial services. Over the last twelve years, I have been the Chairman and CEO of three different Fortune 500 companies and held Board membership positions in others. Much of my earlier business career was with the General Electric Company, with my latest position in 1984 being Executive Vice President of Financing Operations for the General Electric Credit Corporation.

My colleagues in their statements today will discuss the Board's and its Committees' respective roles and involvement in the related party transactions. I would like to focus on certain issues that have been raised with respect to the Board and the outside directors as a collective unit.

I begin by saying unequivocally that I am proud to have served on a Board with such capable, hardworking, intelligent, and ethical individuals. Personally, I believe that while we may have begun initially as a collection of individuals, we evolved into a cohesive and collegial group. Moreover, in my view, this Board has remained diligent and dedicated to its responsibilities throughout the process. Although we, at the time, had much confidence and respect for the abilities of the management of the Company, we did operate independently and did exert our influence and, at times, contrary to the wishes of management. For example, the decision made by the majority of the Board to acquire Wessex and form Azurix was made over the dissenting votes of two directors and the abstention of another. More recently, management's intention to acquire a pulp mill in October of last year was resisted by the Board to the extent that decision was not made to make the acquisition.

Allow me to put Enron into perspective over the last couple of years. By 2000, Enron was one of the ten largest companies in the United States. Enron had begun to transform itself from a pipeline company with substantial fixed assets to an innovative energy trading company that showed tremendous potential, but required liquidity and creditworthiness. My personal focus, as a member of the Board and its Finance Committee, had been Enron's liquidity and financial leverage in furtherance of this strategy. As a Board, we were attentive on working with management and our outside experts to realize this mission. We believed that the Company was successfully moving in that direction. In late 2000 or early 2001, no one would have predicted that by the end of 2001, Enron would file for bankruptcy. In fact, as late as October of 2001, we were informed by management that we were ahead of plan in terms of earnings and that creditworthiness and liquidity issues were manageable.

A central issue at hand involves Enron's intentions in establishing SPEs. Before I make any comments regarding the financial structures that are of concern, I would like to provide an opposing point of view to that held by many that the intention of Enron in establishing these partnerships was to manufacture earnings. To the contrary, it is my opinion that the primary purpose of these partnerships was to improve liquidity and get debt off the balance sheet. The LJM partnerships were specifically constituted for that purpose. And, by the way, I would contend that many companies establish SPEs for exactly such a purpose.

Of course, now, with the benefit of hindsight, Committees of Congress, the media, government officials, financial experts, and others have tried to dissect and examine what went wrong at Enron. Over the past several months, several questions have been raised with respect to the directors as a group. In particular, people ask if the Board failed in its oversight duty, whether Enron was moving so quickly that the independent directors could not keep up.

I think not. We worked hard as a Board. We came prepared, and we asked questions. We were sent materials in advance of meetings, and it seemed that each director reviewed them and came to the meetings prepared. Sometimes before a Board meeting, and after spending many hours in preparation for the meeting, I would speak with Mr. Skilling about balance sheet issues or with the Chief Risk Officer, Rick Buy, about liquidity and leverage issues. I know that my fellow director, Mr. Winokur, who is here today, spent time with Enron's Chief Financial Officer Andrew Fastow before meetings asking him questions about various issues. And Dr. LeMaistre, who is also appearing with us today, spent much of his time in advance of upcoming Compensation Committee meetings with Enron's human resources and compensation staff, as well as external consultants, to ensure himself that he understood all of the technical aspects of Enron's compensation plans and to be in a position to evaluate recommendations made by management. He took his job very seriously. In short, I believe that, judged by any standard, this Board executed its duties to the Company and its shareholders.

During Board and Committee meetings, we questioned management. For example, during the October 1999 Finance Committee meeting where the LJM2 partnership was discussed, the Board material discloses that I specifically asked whether Arthur Anderson had reviewed the partnership. We were told by the Chief Accounting Officer that Arthur Andersen was "fine with it." If we had been told that Arthur Andersen had not reviewed the structure, or that Arthur Andersen had reservations, the Board would never have approved it.

The first Raptor was brought to the Finance Committee on May 1, 2000. The minutes reflect that the Chief Accounting Officer told us that "Arthur Andersen LLP had spent considerable time analyzing the Talon structure and the governance structure of LJM2 and was comfortable with the proposed transaction." This advice was critical to our decision to authorize this transaction. Some commentators have since suggested that the structure of this transaction was inappropriate on its face. That is not the advice we received at the time. My fellow directors asked questions pertaining to the propriety and oversight of these transactions. We did not rubber stamp their recommendations and requests.

Finally, media reports have cited particular transactions as evidence of earnings improprieties. These transactions were either not disclosed to the Board or, in fact, affirmatively misrepresented to us. I list a few of them here to illustrate the point.

1. The Raptors

a. The Raptors Vehicles

The media reports that the Raptor vehicles were set up so that LJM2 would recoup its investment before any hedging took place. The directors were unaware of any such arrangement.

b. Raptor I

Throughout the Board minutes and in the presentation materials, the Board was assured that the projected return for this transaction was 30%. In fact, at least one and possibly other members of management knew that LJM2's projected return was, in fact, a minimum of 76%. Yet no one told us the true rate of return they had projected.

c. Raptor III/New Power

The New Power hedge transaction was never disclosed to the Board. This particular transaction would and should have been avoided by simple adherence to the controls we put into effect.

d. Raptor Recapitalization

The credit problems with the Raptor entities, which began in late 2000, were not disclosed to the Board. The decision in early 2001 to recapitalize the Raptor structure with $800 million in equity was, likewise, concealed from us.

2. Chewco

No director knew that Chewco was, in fact, an affiliated transaction. The directors were not aware that an Enron employee, Michael Kopper, had an ownership interest in Chewco. The Board was not told that Mr. Kopper received a payment when Chewco was closed out. We were similarly unaware, until the fall of 2001, that Chewco was in violation of the 3% equity rule.

3. Braveheart

This was the project with Blockbuster that would allow customers to choose from thousands of movies sent via telephone lines to their homes. Media reports state that Enron inexplicably claimed over $110 million in profits in the fourth quarter of 2000 and first quarter of 2001. If Enron was falsely claiming these profits, the directors were unaware of it.

4. Southampton Place

The Board was not informed that Southampton was formed with Enron employees, or that it was able to sell Enron shares back to Enron at a huge windfall to Southampton. From the media reports I have read about this, it seems that Southampton never would have reaped such big profits if this deal had been negotiated at arms' length.

5. Churned Transactions

We are now aware from the Powers Report of a pattern of assets being sold to LJM in one quarter, only to be repurchased by Enron in the following quarter. This, too, was concealed from the Board.

Even with the benefit of hindsight, I cannot speculate as to what else we could have done to ensure that our controls and procedures were followed. We put the right controls in place, and asked the right questions. These directors were a smart and talented group of people who brought a diversity of experience and expertise to the Board. Unfortunately, I believe that we were uninformed because management and outside experts who reported to us failed to do their jobs and give us full, complete information.

I am prepared to respond to any questions from the Subcommittee.

Thank you.

SUBMISSION
OF
CHARLES M. ELSON
Director, Center for Corporate Governance
University of Delaware

(In Lieu Of Prepared Statement)

Vol XXVI No 7 July / August 2000

Directorship

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by Charles M. Elson
Professor of Law
Stetson University College of Law

In recent months a significant debate has engulfed the investment community over the role traditional governance principles and practices should play in the emerging-growth, newly public technology companies. In an engaging article entitled "Governance in emerging companies: Is this the new model?" (*Directorship*, April 2000), David Berger persuasively argues that the governance model seemingly favored by many of these young businesses is both appropriate to their circumstances and may offer a sound "path to success." While some of the structural characteristics of these boards have appeal, on the whole I believe that this approach to governance suffers from a fundamental flaw that makes the model highly problematic for these businesses and their shareholders. While traditional "good governance" practices may not presently find welcome acceptance at the emerging growth companies, these standards are not only appropriate but critical to the long-term success of these businesses.

Berger identifies three structural characteristics common to the new technology boards: "First, the boards seek directors based more on expertise and a belief that such directors will act in an independent manner in the best interests of shareholders rather than ensuring directors meet some technical definition of independence. Second, these boards are smaller than boards of companies of comparable size in more traditional industries. Finally, directors on such boards often collectively own a greater percentage of their company's stock than is typically seen in older companies."

I have no argument with Berger's second and third characteristics—those involving board size and equity ownership. I have always believed that a smaller board is preferable to the old-style "come one, come all" approach. Berger is correct in suggesting that a smaller group can communicate more easily with management and among themselves, providing much more effective and responsive oversight. As to heavy board equity ownership, I am in complete agreement. The cornerstone of my personal model for strong corporate governance has been director stock ownership. A director with a substantial equity position is much more proprietary in his or her approach to oversight than one with little or no stake in the enterprise. Equity ownership aligns the director's interest with those of the organization and its shareholders, rather than management, and creates the kind of management monitoring vital to continued corporate success.

"It is always tough to examine objectively one's own conduct."

Serious disagreement

However, I have a serious disagreement with Berger's initial and most significant point. Berger argues that the board members' lack of classical independence from management should be no cause for concern in the emerging growth company. Service providers, consultants and venture capital investors, because of their industry knowledge and expertise and despite their economic affiliation with management, "provide important guidance and skills to a company that must move in Internet time." Because these directors are also substantial equity holders, Berger suggests that they have the proper incentive to exercise effective oversight and act in the shareholders' interest. I disagree. Under traditional governance theory, the board acts as an active management monitor for shareholder benefit. It must decide when to engage and when to terminate a management team and acts to provide supportive management oversight in between these two points. Central to this active monitoring are the concepts of independence and equity. To fulfill their oversight responsibilities effectively, directors must be independent of management and holders of a personally meaningful equity stake in the enterprise. Independence is a critical element in meaningful monitoring. Independence, which involves the absence of any economic ties to management or the company itself other than equity ownership, provides a director with the distance and objectivity necessary to examine management action in the most effective manner. Economic relationships with management, including consulting, service provision or other arrangements, may cloud judgment and make it more difficult to review management conduct objectively. A good distance from everyday operations allows the kind of reflective review of management conduct that public shareholders expect and is necessary to long-term corporate success.

Involvement in day-to-day operations by non-independent directors has two problems. First, as previously discussed, linkage with management makes oversight problematic. And second, the directors become, in effect, managers and may find it more difficult to challenge and reverse a nonproductive course of conduct that they had a role in creating and implementing. It is always tough to examine objectively one's own conduct. This is no less true in corporate affairs than in everyday human activity. That is one reason for the very existence of a board—to provide objective review of management conduct to ensure the most productive course of action. Such review is crucial, not only for protecting shareholder wealth, but also for stimulating effective management.

Accountability and responsibility

The watchwords are accountability and responsibility. All of us must need to feel accountable to someone. The idea of responsibility to a watchful intermediary spurs thoughtful decision-making and reflection on management's part. This cannot occur unless the intermediary is in fact independent of the examined party. This is why the concept of the independent board is so critical to modern governance theory. No matter whether a company is decades old and rooted in the "old economy," or newly formed and growing exponentially in "new economy" ventures, intelligent and inspired leadership is a common need. A watchful, independent board promotes that kind of management. Despite the benefits some non-independent service providers may bring to the emerging growth enterprise board, their lack of independence imposes a cost in terms of compromised oversight that no shareholdership can afford.

But what about the heavy equity investment that we see represented on numerous "new-style" boards? Can this alone act, as Berger argues, to create spirited oversight? Unfortunately not. Equity ownership provides the incentive to monitor, but standing alone does not provide the proper objectivity to create effective oversight. It is independence that creates objectivity. That is why a modern governance theory demands both equity ownership *and* independence. Independent directors without equity ownership may be objective but have little incentive to engage in active oversight. It is the equity ownership that provides the incentive to exercise that objectivity. Equity-holding directors who are not independent may have the incentive but lack the necessary objectivity. Independence and equity ownership, acting in tandem to reinforce one another, are the watchwords of effective corporate governance.

Despite the impassioned cry that "new economy" companies deserve "new-style" governance—this new style, with its unfortunate reliance on non-independent boards, looks and feels a lot like the old-style corporate governance of years past that brought investors multiple performance-related problems. Independent, equity-holding directors provide both old and new style corporations the kind of management oversight that inspires the good corporate results management, directors and shareholders desire and deserve. ■

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*Charles M. Elson holds the Edgar S. Woolard, Jr., Chair of Corporate Governance and is Director of the new Corporate Governance Center at the University of Delaware (*Directorship, *June 2000). He is on leave from his professorship at the Stetson University College of Law in St. Petersburg, Florida. He is a director of Sunbeam Corporation and Nuevo Energy Company. He is a Salvatori Fellow at the Heritage Foundation and of counsel to the Tampa law firm of Holland & Knight LLP. Mr. Elson has been a member of a number of National Association of Corporate Directors commissions, is a frequent contributor to* Directorship *and other publications and a speaker on governance issues.*

CORPORATE counsel

March 2001

The Bad Board Booby Trap

Before your company invests in a dot-com or other high-tech venture, be warned: Too often, New Economy corporate boards are stacked with self-dealing members—and that can spell management disaster.

By Charles M. Elson

WE ARE WITNESSING a dramatic turnaround in the financial fortunes of numerous emerging-growth, newly public technology companies. Spectacular market capitalizations and individual fortunes have evaporated as blindingly fast as they were created.

Varying explanations for this startling turn of events have been offered, including poor business planning, strategy, and execution. But there is also a less obvious culprit: New Economy companies' unique corporate governance structures. They can be so deadly that, before a brick and mortar company buys or invests in a New Economy company, legal counsel should vet the board.

The chief criteria for board membership should be independence and equity. Unfortunately, many New Economy companies fail on both counts. First, they are loaded with industry experts who do business with the company; second, their directors often are compensated with options rather than stock.

It is a big problem when directors have direct business dealings with the company. Traditional companies tend to people their boards with officers of other companies, financiers, or academics.

New Economy boards, in contrast, make board members out of the company's own service providers, consultants, and venture capitalists. The argument is that industry-specific expertise makes such insiders indispensable as board members, and that their economic affiliation with management is offset by their substantial equity holdings, which inspire them to exercise effective oversight and act in the shareholders' interest.

I disagree. Modern governance theory dictates that directors should not have financial relationships with the company beyond their equity ownership. The board must act as an active management monitor for the benefit of shareholders. It must decide when to engage and terminate a management team. To do this, it must be completely independent of management.

Instead, in New Economy companies, directors are intimately and self-interestedly involved in day-to-day operations, making them more managers than the overseers of managers. Their big equity investments are not enough of a counterbalance.

Heavy director equity ownership can be a good thing. The cornerstone of my model for strong corporate governance has been director stock ownership. Directors with substantial equity positions are more proprietary in their approach to oversight than those with little or no stake in an enterprise. Equity ownership aligns the directors' interests with those of the organization and its shareholders, rather than with management. It therefore creates the kind of management monitoring vital to continued corporate success.

In fact, independent directors without equity ownership tend to be weak watchdogs: They may be objective, but they have little incentive to actively oversee management.

But New Economy directors tend to be compensated in the company's stock options. And this is a big mistake. They should receive the stock itself. The reason is simple: When a stock you own declines in price, you feel a real loss; with an option, the loss is just the loss of an expectancy. The key is compensating directors with something that gives them a real sense of equity in the business.

Before a traditional company decides to invest in a dot-com or other New Economy venture, it is well advised to look at who sits on the board and how board members are compensated. If you don't like what you see—and you might not—there are choices, depending on the level of investment. If you're taking a minority stake, condition it on a new board. If you're buying the company outright, clean house yourself.

While objective governance boards may not have ensured the success of the now-failing dot-coms, they might have helped avert some of the more extreme examples of New Economy meltdowns.

Whether a company is decades old and rooted in the Old Economy, or newly formed and growing exponentially in New Economy ventures, intelligent and inspired leadership is needed. Of course, good governance is not the cure-all for a poorly run or ill-conceived enterprise. But independent, equity-holding directors will provide both old- and new-style corporations the kind of oversight that management, directors, and shareholders deserve.

Charles M. Elson is the Edward S. Woolard, Jr., professor of corporate governance at the University of Delaware.

▸ CONTRIBUTORS

KEVIN EVANICH ("Grab Those Bargains," page 64) is a partner in the Kirkland & Ellis corporate group specializing in leveraged acquisitions and buyouts, and in venture capital fund formations. He is a member of the Chicago firm's management committee. His clients include buyout and venture capital firms as well as equity investment advisers.

CHARLES M. ELSON ("The Bad Board Booby Trap," page 68) is a professor at the University of Delaware. He also directs the university's Center for Corporate Governance. A fellow at the Heritage Foundation in Washington, D.C., Elson is of counsel to Tampa's Holland & Knight. He also serves on several boards, including Circon Corporation in Santa Barbara, California, and Sunbeam Corporation in Boca Raton, Florida.

HOLLY ENGLISH ("Sweating Out The Review," page 52) is a principal with Values at Work, a consulting firm based in Montclair, New Jersey. A former litigator, she is a frequent contributor to *Corporate Counsel* affiliates, including the *New York Law Journal*.

CORRECTION

Due to an editor's error, the name of McDonald's Corporation's chief executive officer was misstated in "Don't Manage, Lead!" [February]. It is Jack Greenberg.

How To Reach *Corporate Counsel*

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Permanent Subcommittee on Investigations
Committee on Governmental Affairs
United States Senate

Statement by Michael H. Sutton
May 7, 2002

Chairman Levin. Senator Collins. Members of the Subcommittee.

Thank you for inviting me to share my thoughts on the corporate governance and accounting issues raised by the failure of Enron.

First, let me comment briefly on my background and experience. I was Chief Accountant of the Securities and Exchange Commission from June 1995 to January 1998. Prior to holding that office, I was a senior partner in the firm of Deloitte & Touche, responsible for developing and implementing firm policy relating to accounting and auditing, and practice before the SEC. My career with Deloitte & Touche spanned from 1963 to 1995. As a retired partner, I receive a fixed retirement benefit from that firm. Presently, I undertake from time to time independent consulting and other assignments in the field of accounting and auditing regulation and related professional issues.

Effective oversight by boards of directors is at the heart of the financial reporting processes that serve and protect the interests of investors and the public. Without effective oversight, important checks on the integrity, judgment, and performance of management are compromised. Without effective oversight, critical safeguards of the rigor and objectivity of the independent audit are weakened. As we have seen in the case of Enron, failures of the corporate governance processes can be devastating, and the investing public, rightly so, is asking, "Can we rely on corporate governance processes - oversight by boards of directors and audit committees - to ride herd on management and see to it that auditors do their jobs?"

Today, you are examining the questions raised by Enron in a search for meaningful remedies. We would like to believe that Enron is an anomaly - that the governance issues raised are isolated to this case, but they are not. While Enron has become a "poster child" for a system out of control, the underlying concerns about the diligence of boards of directors and audit committees reach far more broadly into our corporate and capital market culture.

To help put the search for reform in perspective, I offer some essential views that I think all can agree on.

- First, I think all will agree that our capital market system is a national treasure. It is vital to the success of the economy. Indeed, our exceptional standard of living depends on its vitality.

- Accordingly, we all share a compelling common interest in assuring the strength and liquidity of our capital markets.

- This compelling common interest must shape our policy goals and guide our thinking as we search for solutions.

- Finally, the most critical, yet intangible, ingredient of a successful capital market system is the confidence of investors that the markets are fair – confidence that the information they depend on is trustworthy – confidence that they can make informed decisions and will not be misled.

As we look at the issues today, it should be abundantly clear that there is no higher goal for financial reporting than providing useful and reliable information that promotes informed investment decisions and confidence in the system. It also should be abundantly clear that, without diligent, probing directors and audit committees and dispassionate independent auditors, the quality of financial reporting can be, and will be, systematically undermined. Without adequate checks that must come from effective governance, conflicts of interest can, and will, go unchallenged.

One of the most practical and effective steps in reforming the financial reporting system would be to immediately revisit and rewrite our corporate governance policies and guidelines to clearly break the bonds between management and the independent auditor, and to unmistakably spell out the responsibilities of boards of directors and audit committees to shareholders and the investing public. Management should be the subject of, not the manager of, the independent audit relationship and process. The ultimate responsibility for full and fair disclosure to shareholders, and the direct responsibility for the independent audit relationship and the quality of the audit process, should be clearly fixed with the board of directors and its audit committee. The audit committee should be made up entirely of independent directors.

As we consider reforms, it is important to keep in mind that investor confidence is influenced by both the fact and the appearance of the independence of the auditor. At the end of the day, governance of the financial reporting process should provide comfort to the investing public that the financial statements they receive have been subjected to an effective and truly independent audit.

For independent auditors, I believe that a brighter future begins with full acknowledgement of the reality that seems so clear today. Failures in our financial reporting system are more than aberrations. They seriously undermine investor confidence in the institutions that are supposed to protect them. They "poison the well."

Pleas that the vast majority of financial reports are sound, that most audits are effective, and that failures are few miss the point. In capital markets, a single financial reporting failure can be a disaster in which losses can wipe out decades of hard work, planning, and saving. In that context, debates about how many failures can be tolerated are not only not productive, they are nonsense.

To restore and maintain confidence in the independent audit, I believe that the auditing profession will need to do three things:

- First, it will have to embrace a role that is fully consistent with high public expectations. In public capital markets, insiders have an advantage over public investors, and in that arena independent auditors are expected to balance the scales by assuring investors that financial reporting gives them a fair presentation of the economic realities of the business.

- Second, the auditing profession will have to tackle fraudulent financial reporting as a distinct issue, with a distinct goal – zero tolerance. We understand that, in life, "zero defects" are almost never realized. Nevertheless, the public expects that the profession will pursue that end.

- Third, it will have to accept and support necessary regulatory processes that give comfort to the public that the profession is doing all that it can do to prevent future episodes of failed financial reporting.

Regulatory processes that will build confidence in the auditing profession will be truly independent; they will be open; they will actively engage, inform, and involve the public; they will be adequately resourced and empowered to accomplish their mission; and they will be adaptable to changing conditions.

With respect to accounting standards, we simply can't tolerate financial reporting that "hides the ball." And, we can't tolerate processes that are not responsive to critical financial reporting needs. Current rules for accounting for SPEs, for example, are nonsensical – they can only be explained by accountants to accountants. More broadly, outdated rules governing consolidation and off-balance-sheet financing have become recipes for masking a company's true economic risks and obligations. We have a right to insist that accounting standards clearly reflect the underlying economics of transactions and events. And, it is not acceptable to sit by while market innovations outstrip the development of needed guidance.

Criticism of US standards is beginning to focus on the fact that they have become increasingly detailed, and arguments have been made that they should be broader statements of principle, applied with good judgment and respect for economic substance. I have sympathy for the desire to break the cycle of the mind-numbingly complex accounting rules that have become the norm, but to do that I think we have to confront realistically the reasons why our standards have evolved the way they have.

Here are some of the underlying pressures at work:

- Business managers want standards that provide the greatest flexibility and room for judgment. They want to be able to manage reported results, but yet be able to point to a standard that assures the public that they are following the rules.

- Dealmakers and financial intermediaries want standards that permit structuring transactions to achieve desired accounting results – results that could obscure the underlying economics. In that world, creative transaction structures are valuable commodities.

- Auditors are pressured to support standards that their clients will not take issue with, and they often are restrained in their expected support for reporting that is in the best interests of investors and the public.

- Others, including some legislators, too often lose sight of the fundamental importance of an independent and neutral standards-setting process. Without independence and neutrality, standards setters cannot effectively withstand the myriad of constituent pressures that it inevitably will face and make the tough decisions that inevitably are required.

- And then, standards setters too often seem to pull their punches – perhaps because of a perceived threat to the viability of private sector standards setting – perhaps because of the sometimes withering strain of managing controversial change – perhaps because of a loss of focus on mission and concepts that should guide their actions.

As we re-examine our processes, the issue and debate should not be about whether accounting standards should be detailed or broad, but rather about what formulation of standards and standards-setting approaches best accomplish the goal of providing capital markets with reliable and decision-useful financial information.

We need to re-energize our standards-setting processes and the commitment of capital market participants to support a fully effective, independent standards setter. We should provide independent funding for the FASB – funding that does not depend on contributions from constituents that have a stake in the process. We also need a more independent governance process to replace the current foundation board. The leadership for these changes should come from visionaries of unquestioned objectivity and demonstrated commitment to the goals of financial reporting and the public interest.

At the outset, I suggested that the common interest in preserving and maintaining healthy capital markets far outweighs the concerns or goals of any particular group or special interest. We have to keep focusing on that fundamental tenet and on the goal of assuring that confidence in our capital markets is preserved and that confidence in our financial reporting and disclosure system is restored. Only a continuing commitment to that goal will guarantee that we continue to enjoy the best capital markets in the world.

Thank you again for inviting me. I would be pleased to respond to your questions.

REMARKS ON CORPORATE GOVERNANCE TO THE U.S. SENATE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS
MAY 7, 2002
ROBERT H. CAMPBELL RETIRED CHAIRMAN / CEO SUNOCO INC.

Good morning ladies and gentlemen. My name is Robert Campbell. I am the retired Chairman and Chief Executive Officer of Sunoco Inc. and I would like to thank you for the opportunity to testify before this committee today. The primary role of the outside director in protecting the interest of the shareholders has always been important in the past, but it is a national imperative today if we are to restore the confidence of investors in publicly held companies.

I would like to begin this morning by making two points clear. First of all, any remarks I make are my personal beliefs and do not necessarily reflect the beliefs of the corporations on whose boards I have served or am currently serving. And secondly, you need to understand that my knowledge of Enron and its directors and Arthur Anderson and its partners is limited to what I have read in the print media or seen on television. I have no direct knowledge of what has taken place within those organizations.

For your information my active business career spanned a 40 year time period from mid 1960 until June 2000. The entire career was spent with one company (Sun Oil Company – Sunoco) or its subsidiaries. In 1991, I was named President and CEO, and in 1992, I was named Chairman of the Board of Directors. I held the Chairman / CEO positions until I retired in June of 2000.

In your letter of invitation to me, you asked that I comment on whether I thought the governance problems exposed in the Enron matter are unique, or representative of most U.S. publicly traded companies. My answer is that I certainly do not believe that the alleged behavior is representative of boards of directors in the U.S. today. In addition to Sunoco, I have been or am currently a director of CoreStates Bank (before its acquisition), Hershey Foods, CIGNA Inc., Pew Charitable Trusts, and Rocky Mountain Institute, plus numerous civic and non profit boards. During those 15 years I have come to know probably more than a hundred directors, and can state from personal experience that the allegations I have read in the print media and seen on television are not even remotely similar to the director experiences I have had.

Possibly the best way to explain the type of board governance I am accustomed to is to cite some of the practices instituted at Sunoco. The list of governance practices of that corporation spans four typed pages, and you'll be happy to know that I have no intention of reading them this morning – but have instead submitted them as an attachment to my remarks for your information.

However, let me highlight some of the practices that we may want to discuss further in today's meeting:

At Sunoco, the Board consists entirely of independent outside directors except for the CEO / President. The directors have no consulting contracts, have a mandatory retirement age, but no company retirement plan. In addition, more than half of a directors compensation is in the form of company stock or stock equivalents, and a set of Directors Stock Ownership Guidelines has been instituted.

Each director is elected annually for a one year term, and the company has a confidential voting process in place for shareholders. The directors are also expected so sign off annually on Code of Ethics and Conflict Of Interest statements.

An extended meeting of all "outside directors" is held annually without the Chairman / CEO present. The purpose of this meeting is a thorough examination of the CEO's performance and the surfacing of any issues or concerns that outside directors may have about corporate performance or direction. The results of this meeting are then fed back to the CEO by the entire Board in a follow-up meeting.

A meaningful and in depth review of the performance of each Director is held annually by a governance committee of the board, and one-on-one feedback is given to the Director on the results of the review. In addition there is a tabulated periodic evaluation by all directors of the "board as a whole", with suggestions for improvement given to the CEO / Chairman.

There is the recognition that the external auditors work WITH management, but work FOR the Audit Committee. Approximately 7 years ago at Sunoco we decided to ask the "big 5" auditing firms (including our current firm) to submit a proposal for our external auditing work. After reviewing the proposals we decided to change our external auditors. The firm we replaced had been with the company more than 80 years – almost since its formation. Incidentally we found that the change process was not overly disruptive or expensive, and we were very happy with the effect on the corporation of bringing in the new outside auditors.

I could go on and list more of the many practices in place, but I expect by now you understand the seriousness with which this subject has been approached at Sunoco. And I might add that virtually all of these practices have been in place for almost a decade -- long before board governance became the popular subject it is today. Sunoco's approach to governance resulted in several instances of external recognition, and culminated in the Board of Directors receiving the 1999 national "Board Excellence" award from Spencer Stuart (an international executive search firm) and from the Wharton School of Business of the University of Pennsylvania.

Also in your letter of invitation to me you asked if I might have any recommendations for new legislative or regulatory reforms. I will confess up front that my business career has conditioned me to seldom seek more legislation or regulation from government. However I do believe that the current situation calls for strong action on the part of someone, and I would suggest four areas of focus.

First I believe there needs to be more complete and understandable annual disclosure of the relationship between a director and the corporation. The typical corporate proxy today, issued prior to the annual meeting and the election of directors, gives a very brief description of the director standing for election. I would like to see a much more complete description, on one page, of each directors relationship with that corporation including not only the total compensation received (in whatever form it may take – cash, stock, benefits or perqs) but also any consulting or employment contracts for them or their relatives ... any business relationship between their company and the subject company (are they a significant supplier or customer)? ... what are their financial holdings in the company they serve as director (stock, stock equivalents, options, bonds, other forms of debt, loans, etc.?). I realize that some of this information is disclosed in other documents, however bringing all of it together annually in one place, in an easily read format will help insure complete disclosure.

My second suggestion is that an annual meeting of outside directors (no CEO or other member of management present) be made mandatory – not just a good practice. And that it be followed with an extensive feed-back session with the CEO / Chairman. I have found it to be of tremendous value to both the CEO and the outside directors in surfacing issues early while they can still be dealt with constructively.

Next, I believe that consideration should be given to limiting the number of years an outside auditor can serve a corporation. The need for "a different set of eyes" is currently recognized by the existing requirement that the partner in charge be rotated every seven years. However, bringing in a new lead partner from the same firm to work with the existing team from that firm is inadequate in my opinion. I'm certain this requirement would be seen as unnecessarily disruptive and expensive by most corporations today. But if an outside auditing firm knew that ten years from now a competing auditing firm would be looking over and commenting on their work, a whole new dynamic would be introduced in the current process.

Finally, since good corporate governance is a constantly evolving process, it would be difficult to legislate or regulate with too much specificity. What is viewed as "good" this year may not be viewed as "adequate" in future years. Boards need to institute a continuous governance review process, and I believe it would be helpful if the following were required by regulators:

1. Corporations should be required to put their current governance practices in writing, and publish them annually in their proxy statements. In that manner it would be clear to all shareholders how their corporation is governed.

2. A board committee should be identified and held responsible for reviewing and updating a corporation's governance practices, similar to the way th audit and compensation committees currently have certain regulatory duties.

One of Sunoco's current directors (Rosemarie Greco) recently published in the January 2002 edition of National Corporate Directors Monthly an excellent description of a process which a corporation can use to institutionalize "best" governance practices. I strongly recommend you review her offering. For it is only when the governance process is institutionalized that it will continue over time.

Again, thank you for your invitation to be here today, and I will be happy to try to answer your questions.

Robert H. Campbell

STATEMENT ON CORPORATE GOVERNANCE

The corporate governance standards established by the Board provide a structure within which directors and management can effectively pursue Sunoco's objectives for the benefit of its shareholders. Sunoco's business is managed under the direction of the Board of Directors. The Board delegates the conduct of business to Sunoco's senior management team. The principal functions of the Board are to:

Evaluate the Chief Executive Officer: The ongoing evaluation of the CEO is accomplished through the following process:

- The Chief Executive Officer meets with the Compensation Committee to develop appropriate goals and objectives for the next year, which are then discussed with the entire Board.
- At year end, the Compensation Committee, with input from the Board, evaluates the performance of the Chief Executive Officer in meeting those goals and objectives.
- This evaluation is communicated to the Chief Executive Officer at an executive session of the Board.
- The Compensation Committee uses this evaluation in determining the Chief Executive Officer's compensation.

Review and Approve Sunoco's Strategic Direction and Annual Operating Plan, and Monitor Sunoco's Performance:

- Annually, the outside directors meet with the Chief Executive Officer to discuss the overall performance and direction of the Company.
- Following that discussion, the outside directors meet independently, at a meeting which is chaired by the Chairperson of the Governance Committee, to evaluate Sunoco's performance and direction.
- This evaluation is communicated to the Chief Executive Officer at an executive session of the Board.
- The Board stays abreast of political, regulatory and economic trends and developments that may impact Sunoco's strategic direction.
- Each year, the Board and management participate in a two-day off-site meeting at which major long-term strategies and financial and other objectives and plans are discussed and approved.

- Annually, the Board reviews and approves a three-year strategic plan, yearly goals and an operating plan for the Company.

- On an ongoing basis during the year, the Board monitors Sunoco's performance against its annual operating plan and against the performance of its peers.

Review Management Performance and Compensation:

- The Compensation Committee reviews and approves the Chief Executive Officer's evaluation of the top management team on an annual basis.

- The Board (largely through the Compensation Committee) evaluates the compensation plans for senior management and other employees to ensure they are appropriate, competitive and properly reflect Sunoco's objectives and performance.

Review Management Succession Planning:

- The Board plans for succession to the position of Chairman of the Board and CEO as well as certain other senior management positions.

- To assist the Board, the Chairman and CEO annually provides the Governance Committee with an assessment of senior managers and their potential to succeed him.

- He also provides the Governance Committee with an assessment of persons considered potential successors to certain senior management positions.

- The results of these reviews are reported to and discussed with the Board.

Advise and Counsel Management:

- Advice and counsel to management occurs both through formal Board and Committee meetings and through informal, individual director's contacts with the Chief Executive Officer and other members of management.

- The Board is composed of individuals whose knowledge, background, experience and judgment are valuable to the Company.

- The information needed for the Board's decision-making generally will be found within Sunoco, and Board members have full access to management.

- On occasion, the Board may seek legal or other expert advice from a source independent of management, and generally this is done with the knowledge and concurrence of the Chief Executive Officer.

Review Structure and Operations of the Board: The Governance Committee periodically reviews the Board's structure, operations, and need for new members and reports the result of this review to the Board for its approval. The Board observes the following general practices:

- ***Selection and Evaluation of Board Candidates:*** When searching for new nominees, the Board selects candidates based on their character, judgment, and business experience, as well as their ability to add to the Board's existing strengths. The Governance Committee evaluates the performance of individual directors on an annual basis and this evaluation provides the basis for the Board's recommendation of a slate of directors to the shareholders.

- ***Board Structure:***

  - Each director is elected annually by shareholders for a one-year term.

  - The Board consists entirely of independent outside directors except for the Chief Executive Officer. None of the directors has a consulting contract with Sunoco.

  - As a general rule, director-nominees are required to own at least $2,000 worth of Sunoco common stock prior to standing for election as a director.

  - Periodically, the full Board conducts an assessment of how it is functioning as a whole so that it may continuously improve its performance.

  - The mandatory retirement age for directors is 72.

  - An outside director must tender his or her resignation for consideration by the Governance Committee if the position he or she held at the time of election changes.

  - As a general rule, it is the Board's expectation that when officer directors leave their Company positions, they will no longer serve on the Board.

  - New directors must participate in an orientation process that includes reviewing extensive materials regarding Sunoco's business and operations, visits to Sunoco facilities and meetings with key personnel. As part of this process, new directors attend meetings of all the Board's committees to acquaint them with the work and operations of each. After this orientation, new Board members are given regular committee assignments.

- ***Board Operations and Meetings:***

  - Sunoco's Board usually meets seven times per year in regularly scheduled meetings but meets more often if necessary.

- While the Board believes that a carefully planned agenda is important for effective Board meetings, the agenda is flexible enough to accommodate unexpected developments. The items on the agenda are typically determined by the Chairperson in consultation with the Board. Any director may request that an item be included on the agenda.

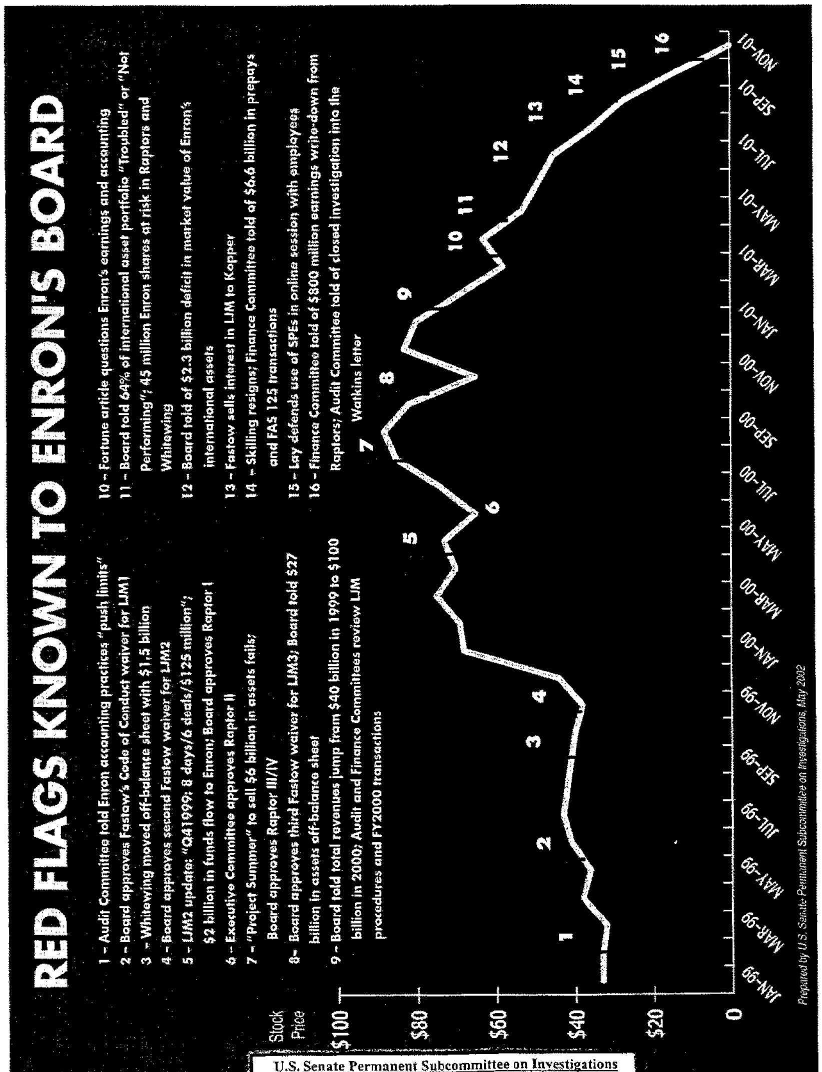
- Generally, Board members receive information well in advance of Board meetings so they will have an opportunity to prepare for discussion of the items at the meeting. Information is provided from a variety of sources, including management reports, a comparison of performance to operating and financial plans, reports on Sunoco's stock performance and operations prepared by third parties, and articles in various business publications. In many cases, significant items requiring Board approval may be reviewed in one or more meetings and voted upon in subsequent meetings, with the intervening time being used for clarification and discussion of relevant issues.

- At Board meetings, ample time is scheduled to assure full discussion of important matters. Management presentations are scheduled to permit a substantial proportion of Board meeting time to be available for discussion and comments.

Committee Structure: The full Board considers all major decisions of the Company. However, the Board has established the following five standing committees, each of which is composed entirely of outside directors, except for the Executive Committee, so that certain important areas can be addressed in more depth than may be possible in a full Board meeting:

- *The Audit Committee* oversees Sunoco's accounting processes and reporting systems and the adequacy of internal controls, reviews and approves Sunoco's financial disclosures, and evaluates the performance and recommends the appointment of independent auditors. This Committee is responsible for preparing and issuing the Audit Committee Report published in this proxy statement. This Committee, along with the Board, is responsible for reviewing and updating the Audit Committee Charter.

- *The Governance Committee* reviews the role, composition, and structure of the Board and its committees as well as directors' compensation. It also reviews and evaluates Board members in determining the annual directors' slate and identifies new director nominees. This Committee reviews the CEO's recommendations of potential successors, as well as potential successors to other senior management positions. This Committee, along with the Board, is responsible for reviewing and updating Sunoco's Statement on Corporate Governance published in this proxy statement.



U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #1

Selected Observations
1998 Financial Reporting

Category	Risk Profile: Accounting Judgements	Risk Profile: Disclosure Judgements	Risk Profile: Rule Changes	Comment
Highly Structured Transactions				
Energy Asset Securitizations	H	H	H	• Judgement Relates To General Applicability of Model And Any Retained Control Features • Significance of Earnings Heightens Need for Disclosure • Ongoing Rulemaking Activity Could Drastically Limit Model
Other Income Related	H	M	M	• Judgement Usually Relates To Extent of Any Continued Involvement And/Or Contingency Exposures
Commodity and Equity Portfolio				
Commodities (MTM) and Merchant Investments (Fair Value)	H	H	M	• Inherent Judgement Around Methodologies • Significance of Merchant Earnings Heightens Need For Disclosure
Prudency	H	H	L	• Assessment and Documentation Procedures Recently Enhanced • Relationship to SEC Hot Areas
Purchase Accounting	H	M	L	• Judgement Relates To Original Valuations and Accounting for Subsequent Activity
Balance Sheet Issues				
Equity Investments	H	H	M	• Judgement Relates To Control And Retained Economic Parameters • Continue Appropriate Commitment/Guarantee/Contingency Disclosures
Portfolio Monetizations	H	M	H	• Judgement Relates To Extent of Any Continued Involvement • Ongoing Rulemaking Activity (Could Be Positive)
Other				

ARTHUR ANDERSEN

U.S. Senate Permanent Subcommittee on Investigations
(Source: February 7, 1999, Andersen Presentation to Audit Committee.)
EXHIBIT #2a

AAHEC(2)02762.9

DRAFT

MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
FEBRUARY 7, 1999

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 3:30 p.m., but actually begun at 3:50 p.m., G.M.T., on February 7, 1999, at the Four Seasons Hotel in London, England.

All of the Committee members were present, as follows:

Dr. Robert K. Jaedicke, Chairman
Mr. Ronnie C. Chan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Lord John Wakeham

Directors Kenneth L. Lay and Jeffrey K. Skilling, Messrs. Richard B. Buy, Robert H. Butts, Richard A. Causey, and James V. Derrick, Jr., and Mesdames Rebecca C. Carter and Peggy B. Menchaca, all of the Company or affiliates thereof, and Messrs. Thomas H. Bauer, David Duncan, D. Stephen Goddard, and Douglas King, all of Arthur Andersen LLP ("Arthur Andersen"), also attended the meeting.

The Chairman, Dr. Jaedicke, presided at the meeting, and the Secretary, Ms. Menchaca, recorded the proceedings.

Dr. Jaedicke called the meeting to order and noted that minutes of the meeting of the Committee held on December 7, 1998, had been distributed to members of the Committee, and he called for comments, additions, or corrections. There being none, it was the consensus of the Committee that the minutes of the meeting of the Committee held on December 7, 1998, be approved as distributed.

Mr. Duncan introduced Mr. King, the partner in charge of Arthur Andersen's London office, and then began the 1998 financial and internal controls audit update. He discussed the timing of work performed in 1998, and he stated that Arthur Andersen would submit an unqualified financial statement opinion as a result of its 1998 audit and that there would be no significant audit adjustments or new accounting policies or changes. He added that no modification was required, in Arthur Andersen's opinion, in either management's judgments on accounting

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #2b

estimates or results of reviews of interim financial information. He then presented an update of the 1998 internal audit and the status of the Company's internal controls.

Mr. Duncan reviewed selected observations by Arthur Andersen including a risk profile analysis of accounting judgments, disclosure judgments, and rule changes. He was joined in the discussion by Mr. Bauer.

Mr. Causey began the report on the 1999 Internal Control Audit Plan and discussed key business trends in business risk assessment. Mr. Duncan presented an assessment of the likelihood and significance of high risk in the Company's operations and strategies and pointed out key risk changes from prior years. Mr. Causey discussed areas of emphasis for management and for Arthur Andersen in 1999. Mr. Duncan reviewed the planned work effort on controls by business risk area. A copy of Arthur Andersen's 1999 Internal Control Audit Plan is filed with the records of the meeting. Following a brief discussion, upon motion duly made by Dr. Gramm, seconded by Mr. Foy, and carried, the 1999 Internal Control Audit Plan was approved by the Committee.

Mr. Butts distributed a copy of the 1998 Financial Statements, marked "Draft, 2/4/99," a copy of which is filed with the records of the meeting. He pointed out differences from the previous year in the financials, including the Year 2000 disclosure and accounting for derivatives. He stated that accounting pronouncements that had not been enacted were not acted upon by management. A thorough discussion ensued and management answered questions from the Committee members. Representatives from Arthur Andersen noted that it was comfortable with the 1998 Financial Statements. Following the discussion, it was the consensus of the Committee that the 1998 Financial Statements be approved substantially in the form presented to and discussed at the meeting for inclusion in the 1998 Annual Report to Shareholders and the 1998 Annual Report on Form 10-K to be filed with the Securities and Exchange Commission ("SEC").

Mr. Causey distributed and led a discussion concerning the significant reserves included in the 1998 financial statements, a copy of which is filed with the records of the meeting.

Mr. Derrick reported in detail on and answered questions related to legal matters included in the 1998 financial statements to be disclosed in the 1998 Annual Report on Form 10-K to be filed with the SEC.

Dr. Jaedicke directed the attention of the Committee to the annual report on the taxable value of corporate aircraft use by officers and directors during 1998.

He noted that the information was presented to the Committee each year as an informational item, and a copy is filed with the records of the meeting.

Mr. Buy presented a credit and market risk update. He discussed the top 25 trade credit exposures, the Company's risk profile, and limit violations. He distributed and discussed a stress test analysis on trading portfolios.

Mr. Causey reported to the Committee on a power outage at the Enron Building due to a power surge on the system.

All non-Committee members were excused from the meeting, with the exception of Ms. Menchaca. During the executive session, Mr. Duncan indicated there were no areas of significant concern.

Following the executive session, all representatives of Arthur Andersen left the meeting.

Dr. Jaedicke noted that it would be in order to approve Arthur Andersen as the Company's independent accountants for 1999. Following discussion, upon motion duly made by Lord Wakeham, seconded by Dr. Gramm, and carried, the appointment of Arthur Andersen as the Company's independent public accountants for 1999 was approved by the Committee for recommendation to the Board of Directors.

There being no further business to come before the Committee, the meeting was adjourned at 5:25 p.m., G.M.T.

Secretary

APPROVED:

Chairman

pbm\minutes\2799a.doc

U.S. Senate Permanent Subcommittee on Investigations
Source: 2/7/99, Andersen internal document related to presentation to Enron Audit Committee.
EXHIBIT #3

New, and Things: — startup/Def. Costs — MTM

To Jeff, Ken: A/C → Talked Broadly about # Judgement Areas
→ Talked About How Well We Work Together (Early Involvement)
Feel One Layer Lower

Selected Observations
1998 Financial Reporting

Category	Risk Profile: Scrutiny of Judgement	Risk Profile: Scrutiny of Disclosure	Risk Profile: Rule Changes	Comment
"SFAS 125" Securitizations (Financial Assets; ~$660 Million)	H	H	H	• Judgement Relates To General Applicability of Model And Any Retained Control Features • Significance of Earnings Heightens Need for Disclosure • Ongoing Rulemaking Activity Could Drastically Limit Model Ask about A/C comm.
Fair Value Merchant Investments (~$700 Million)	H	H	M	• Inherent Judgement Around Methodologies • Significance of Earnings Heightens Need For Disclosure
Purchase Accounting (PGE, Elektro, Wessex)	H	M	L	• Judgement Relates To Original Valuations and Accounting for Subsequent Activity
BS Off-Balance Sheet Equity Investments (- EOTT, - JEDI, - Wessex)	H	H	M	• Judgement Relates To Control And Retained Economic Parameters Continue Appropriate Commitment/Guarantee Disclosures
EPS Contingent Equity Funding Vehicles	M	H	L	Continue Appropriate Disclosures Describing Features and Contingencies
BS Other Portfolio Monetizations (B/S)	H	M	H	• Judgement Relates To Extent of Any Continued Involvement • Ongoing Rulemaking Activity (Could Be Positive)
Other Structured Transactions (- Sale/Executory K's, - Tax Motivated)	H	M	M	• Judgement Usually Relates To Extent of Any Continued Involvement And/Or Contingency Exposures
Prudency\Other Reserves (MTM Cond)	H	H	L	• Assessment and Documentation Procedures Recently Enhanced • Hot Area For SEC (MD&A Disclosure)
Other (Potential Impairments - CATS - EOS Pd. - MTBE)	H			

- Obviously, we are on board with all of these, but many push limits and have a high risk profile. "Others could have a different view"

AASCGA(TX)014630

David Duncan of Andersen
to Enron Audit Committee
(Feb. 7, 1999)

"Obviously, we are on board with all of these, but many push limits and have a high 'others could have a different view' risk profile."

–SFAS 125 Securitizations

–Fair Value Merchant Investments

–Purchase Accounting

–Off-Balance Sheet Equity Investments

–Contingent Equity Funding Vehicles

–Other Portfolio Monetizations

–Other Structured Transactions

–Prudency/Other Reserves

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #4

ARNOLD & PORTER

Scott B. Schreiber
Scott_Schreiber@aporter.com
202.942.5672
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555 Twelfth Street, NW
Washington, DC 20004-1206

May 2, 2002

VIA FACSIMILE

Ms. Elise Bean
United States Senate
Permanent Subcommittee on Investigations
Committee on Governmental Affairs
199 Russell Senate Office Building
Washington, D.C. 20510

Dear Ms. Bean:

As you requested, on behalf of Tom Bauer, a partner in Arthur Andersen, I am responding to your inquiries as set forth in your attached request.

To the best of Mr. Bauer's knowledge, the handwriting on the document bearing production #014630 is the handwriting of David Duncan. It reflects what Mr. Duncan and others discussed at an Enron Audit Committee meeting held on February 7, 1999 at the Four Seasons Hotel in London, England. The handwritten notes, Mr. Bauer believes, were Mr. Duncan's talking points. The risk profile of Enron as reflected in the document was discussed at that meeting with and among the members of the Audit Committee and the representatives of the Company who attended. The Andersen representatives expressed their views with respect to a risk profile analysis of the Company's accounting judgments, disclosure judgments and rule changes as reflected on document no. 014630. Company management also participated in this discussion. Certain risk areas were described as "pushing the limits", as reflected in Mr. Duncan's notes, or as being "at the edge."

Sincerely,

Scott B. Schreiber

SBS/jab
Attachment

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #5

High Priority Financial Reporting Risk Areas

Ongoing

- Complex Accounting for Structured Transactions
- Commodity Trading Activities
  - New Products
  - Remote Activity
  - Valuation
- Project Development Related Activities
  - Development Costs
  - Revenue Recognition
  - Consolidation
- Debt and Equity Transactions
- Intercompany and Related Party Transactions

1999 Specific

- Growth of Merchant Asset and Investment Portfolio
  - Applicability of Fair Value Accounting Model
  - Portfolio Management and Valuation
- Accounting Issues Related to Newer Businesses
  - Enron Energy Services
  - Enron Communications
- Regulatory Activity
  - Northern Natural
  - Portland General
  - Wessex
  - Elektro
- Potential Acquisition/Divestiture Activity
- Impact of Significant New Pronouncements
  - FAS 133 (Derivatives)
  - Technical Amendments to FAS 125 (Securitizations)
  - FASB Exposure Draft (Consolidation)
  - Anticipated FASB Exposure Draft (Business Combinations)

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U.S. Senate Permanent Subcommittee on Investigations

(Source: May 3, 1999, Andersen Presentation to Enron Audit Committee.)

EXHIBIT #6

High Priority Financial Reporting Risk Areas

Ongoing

- Complex Accounting for Structured Transactions
- Merchant Asset and Investment Portfolio
  - Portfolio Management and Valuation
  - Applicability of Fair Value Accounting Model
- Commodity Trading Activities
- Project Development Activities
  - Cost Deferral
  - Revenue Recognition
  - Consolidation
- Sophisticated Debt and Equity Transactions
- Intercompany and Related Party Transactions

2000 Specific

- Formalization of Accounting Models, Policies and Procedures Related to Newer Businesses Monitoring business [illegible]
  - EES - Bundled Service/Commodity Contracts
  - EBS - Bandwidth Trading, Content Delivery Services
  - Other (Net Works, Japan) on MTM issues
- Structured Transaction Activity
  - Securitizations and Syndication Vehicles & Managing risk
  - Hedging and Other Vehicles
- Impact of Rulemaking Activity especially on company reports.
  - Anticipated FASB Pronouncements (Consolidations, Business Combinations, Liabilities and Equity, Measuring Financial Instruments at Fair Value)
  - Anticipated Accounting and Audit Guide Regarding Investment Companies Good example. Company worked w/ Committee to help educate.
  - Interpretations of Previously Issued FASB Pronouncements (Primarily SFAS No. 133 Related to Derivatives) Causey discussed the impact on the Company & its customers. Still determining the impact on the Company.
  - Other
- Other Significant Transaction Activity

Expect additional attention this year

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ENRON

EC 000051656

U.S. Senate Permanent Subcommittee on Investigations

(Source: May 1, 2000, Andersen Presentation to Enron Audit Committee.)

EXHIBIT #7a

Summary Of Fees - Activity Overview
(millions)

	1998	1999	1999 Comments
Recurring Baseline Audit	$ 10.0	$ 11.1	– Increase Related to Activity Growth at All Units, Most Notably ENA, Europe and EES
Expanded Accounting, Auditing and Risk Management Services			
Structured and/or Significant Transactions	7.8	12.2	– Significant Syndication and Structured Finance Activity (Condor, Margaux, LJM, Yosemite, Other) – Real-Time Deal Related Activities for Significant Transactions – EOG Disposition worked on structure w/ the company – Various M&A Projects – Registration Statements and Other Required Regulatory Reporting Activities
AA gets involved in the structure on the front end to discuss applicable accounting issues, AA typically consults w/ its Chicago & N.Y. offices			
General Rule Application and Monitoring	2.1	3.9	– Significant Rulemaking Surrounding Trading Activities, Weather Derivatives, General Derivatives, and Other Areas – Implementation Issues Related to SFAS No. 133 (Derivatives) – EES Accounting Model Development
Risk Management Related Projects - General	1.1	3.1	– Various Special Projects (Valuation Models, IT Standards, F/X Management, etc.)
- SAP Related	2.1	2.6	– Reviews of Controls
- Y2K Related	0.3	1.6	
	$ 13.4	$ 23.4	
Other Services			
Tax — Transactions & Compliance	3.0	4.9	– 8 New Locations, 52 Locations Total
- System Implementation	1.1	1.5	– SAP Related Activities
Strategy or Profit Improvement Related	1.7	3.7	– Primarily Strategic Sourcing (Procurement) and Various EES Projects
Loaned Staff and Other	0.4	1.8	– Primarily Information Gathering Projects at EES
	$ 6.2	$ 11.9	
Totals	$ 29.6	$ 46.4	

more classic consultation

bring to

ENRON

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EC 000051661

U.S. Senate Permanent Subcommittee on Investigations
(Source: May 1, 2000, Andersen Presentation to Enron Audit Committee.)
EXHIBIT #7b

DRAFT

MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
MAY 1, 2000

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 2:00 p.m. C.D.T., on May 1, 2000, but actually begun at 2:05 p.m., C.D.T., on May 1, 2000 at the Enron Building in Houston, Texas.

The following Committee members were present constituting a quorum:

Dr. Robert K. Jaedicke, Chairman
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Dr. John Mendelsohn
Lord John Wakeham

Committee members Ronnie C. Chan and Paulo Ferraz Pereira were absent from the meeting. Directors John H. Duncan, Kenneth L. Lay, Charles A. LeMaistre, and Jeffrey K. Skilling, Messrs. Robert H. Butts, Richard B. Buy, Richard A. Causey, James V. Derrick, Jr., Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, and Messrs. Thomas H. Bauer, David B. Duncan, and D. Stephen Goddard, all of Arthur Andersen LLP ("AA"), also attended the meeting.

The Chairman, Dr. Jaedicke, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Dr. Jaedicke called the meeting to order, noted that a draft of the minutes of the meeting of the Committee held on February 7, 2000 had been distributed to members of the Committee, and called for comments, additions, or corrections. There being none, upon motion duly made by Mr. Foy, seconded by Dr. Gramm, and carried, the minutes of the meeting of the Committee held February 7, 2000 were approved as distributed. Dr. Jaedicke called upon Messrs. Causey and Duncan to begin their presentation, a copy of which is filed with the records of the meeting.

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #7c

Mr. Duncan discussed the financial reporting areas that AA had determined to be high priorities due to inherent risks that were present. He stated that the ongoing high priority areas included structured transactions, the merchant portfolio, commodity trading activities, project development activities, and intercompany and related party transactions. He also commented on specific areas where AA would be spending additional time including the following: 1) the formalization of accounting models, policies, and procedures relating to Enron Energy Services, LLC ("EES"), Enron Broadband Services, Inc. ("EBS"), Enron NetWorks, and the Company's activities in Japan, 2) structured transactions related to securitizations and syndication and hedging vehicles, and 3) analyzing the impact of rulemaking activity specifically as it relates to the Company. Mr. Causey joined him in a discussion of the interpretation of previously issued Financial Accounting Standards Board pronouncements, especially as they related to the Company and its customers.

Mr. Duncan then distributed a handout entitled Financial Reporting & Accounting Principles, a copy of which is filed with the records of the minutes. He noted that the handout addressed the American Institute of Certified Public Accountants' suggested topics for expanded qualitative discussions between outside auditors and companies' Audit Committees. He stated that, in AA's opinion, they were already addressing all of the topics with the Committee and AA would address any specific items on an ongoing basis as necessary. He then discussed AA's selected observations for the first quarter including the impact of EnronOnline on the Company's trading activities, the narrowing of valuation parameters for U.S. gas and power positions due to increased liquidity in the markets, certain structured investment vehicles set up by the Company, and the instigation of separate reporting for EBS. He noted that AA had determined that there were two potential immaterial audit adjustments in the first quarter that were still being considered.

Mr. Causey discussed significant current activities relating to the Company's business risk management analysis. He noted that AA and the Company had substantially completed a joint review of the trading controls in remote locations and that no significant issues had been discovered. He commented on two projects undertaken by the Risk Assessment and Control Group ("RAC"): a review of the EES portfolio and a foreign currency risk management project. He noted that the Information Technology Group was performing a compliance review of EnronOnline and he discussed the implementation date for SAP software in the international regions, EBS, Enron North America Corp., EES, and the Gas Pipeline Group.

Mr. Duncan then began a report on AA's fees for audit and other services provided to the Company. He detailed the expenses related to the baseline audit, expanded accounting, auditing, and risk management services, and other services provided by AA.. He noted that AA had five full-time partners and 80-100 professionals in Houston who were focused on providing services to the Company.

Dr. Jaedicke then called upon Mr. Buy for an update on credit and market risk. Mr. Buy began the presentation by discussing the impact on the Company's credit and market risks of the increase in trading related to EnronOnline and noted that the Company was better able to monitor transactions conducted online. He then called upon Mr. Murphy to discuss the Company's market risk. A copy of Mr. Murphy's presentation is filed with the records of the meeting. Mr. Murphy reviewed the first quarter profit and loss and value-at-risk ("VAR") by commodity group and discussed the impact of a significant decline in United Kingdom ("U.K.") electricity prices during the quarter. He discussed the returns each commodity group had earned compared to the VAR it had taken, gave an overview of the VAR backtesting, and noted that the increases in VAR during the quarter were primarily related to increases in the U.S. gas VAR and the U.K. gas and power VAR. He discussed exposures under a "worst case" scenario of 5%-25% shifts in commodity prices and noted that the sale of the Sutton Bridge assets earlier in the year had significantly increased the Company's exposure to the U.K. power markets. Mr. Lay noted that the U.K. government had recently announced its intention to lift the ban later in the year on new gas-fired generation and that this would have a positive impact on the Company's ability to develop new power projects in the U.K.

Mr. Murphy then reviewed loss notifications for the first quarter and noted that the notifications in the financial trading portfolio were due to a disconnect in the equity markets earlier in the year and that it took the Company some time to unwind its positions. He then discussed the Company's VAR as a percentage of market capitalization and of net income and compared the Company's percentages to those of certain other companies in the industry. He noted that the Company's percentages were high because it marked-to-market a significantly larger number of its contracts than most of the other companies presented and the Company was the largest gas and power marketer in the U.S.

Mr. Murphy then presented proposed changes to the Enron Corp. Risk Management Policy ("the Policy"). He discussed certain proposed limit increases to existing commodity groups within the Policy, including Equity Trading, Australian Electricity, and Pulp & Paper, and certain permanent limit structures and limit increases for commodity groups currently covered under the Interim Policy, including Southern Cone Electricity and Gas. He stated that the Company was also recommending that the Policy be amended to include Japanese Electricity as a new commodity group. He stated that the proposed changes to the Policy would be brought before the Finance Committee. He then discussed actions taken by the Executive Committee of the Board since the February 7, 2000 Board meeting that necessitated revisions to the Policy, most notably the sale of the Sutton Bridge assets in the U.K.

Dr. Jaedicke then called upon Mr. Causey to review the proposed amended charter for the Audit and Compliance Committee, a copy of which is filed with the records of the meeting. Mr. Causey discussed the revisions to the charter that were necessary to reflect guidelines proposed by the Securities and Exchange Commission and the New York Stock Exchange. Following a discussion, upon motion duly made by Mr. Foy, seconded by Dr. Gramm, and carried, the proposed amended Audit and Compliance Committee Charter was approved for recommendation to the Board.

There being no further business to come before the Committee, the meeting was adjourned at 3:00 p.m., C.D.T.

Secretary

APPROVED:

Chairman

K:\a Minutes\2000 Minutes\050100a.doc

2000 Audit Update

Selected Observations - Financial Reporting

AA comments on the Company's accounting practices

Category	Examples	Comment
Highly structured transactions	• Securitizations • Syndication and off-balance sheet vehicles • Other complex sales structures • Complex contract structures	• High dependency on transactions to meet objectives • Application of GAAP often requires significant judgement • Continued interpretive guidance likely • Extent of necessary disclosures can be judgemental

Use of mark-to-market and fair value model	• Trading contracts
	• Derivative contracts
	• Investment company holdings of public and non-public securities
		• Significant inherent judgemental issues regarding:
		  • Applicability of model to specific products or transactions;
		  • Valuation (curves, reserves)
		  • Multi-element arrangements
		• Consistency of application among business units continues to be refined
		• Incorporating new products continues to present challenges
		• Continued interpretive guidance likely
		• Extent of necessary disclosures can be judgemental

There are a number of areas where accounting rules have not kept up w/ the Company's practices & some interpretation is necessary.

II-4

RCO 20680

U.S. Senate Permanent Subcommittee on Investigations
(Source: February 12, 2001, Andersen Presentation to Enron Audit Committee.)
EXHIBIT #8a

ENRON

2000 Audit Update
Selected Observations - Financial Reporting

Category	***Examples***	***Comment***

Related party transactions	• LJM related activity
	• Syndication vehicles where company has an ownership interest
		• Relationship issues add scrutiny risk to:
		  • Judgemental structuring and valuation issues
		  • Understanding of transaction completeness
		• Required disclosures reviewed for adequacy

Other Material Judgemental Areas	• Azurix impairment • Impact of high volatility on mark-to-market valuations • Credit (California) • India Contingencies	• Company positions reviewed for reasonableness • Certain disclosures made as warranted
Classification issues	• Financial statements classification • Other public disclosures	• Categorization of activities between certain segments, operating vs. non-operating or recurring vs. non-recurring can be highly judgemental • Certain intersegment allocation practices need refinement

2000 Audit Update
Status and Required Communications

• Financial statement opinion	• Expected to be unqualified.
• Significant audit adjustments	• None significant; see "Status of Proposed Adjustments " (pg. II-3) for further detail and discussion.
• Significant new accounting policies or changes	• None not previously communicated in prior reports. Adoption of new standard related to derivatives (SFAS No. 133) is required in first quarter 2001. As will be disclosed in the 2000 financial statements, impact not expected to be significant (pending final evaluation of PGE).
• Management's judgements and accounting estimates	• No modifications required; see "Selected Observations - 2000 Financial Reporting" (at pages II-4 and II-5).
• Results of reviews of interim financial information	• No modifications required.
• Disagreements with management	• None
• Significant difficulties encountered during the audit	• None
• Major issues discussed with management affecting retention	• None
• Consultation with other accountants on the application of GAAP	• None of which we are aware.
• Review of other financial information (e.g. , Supplemental Disclosures and Management's Discussion and Analysis)	• Currently performing limited review procedures including consistency with basic financial statements.

U.S. Senate Permanent Subcommittee on Investigations
(Source: February 12, 2001, Andersen Presentation to Enron Audit Committee.)
EXHIBIT #8b

AAHEC(2)02743.2

High Priority Financial Reporting Risk Areas

Ongoing

- Complex Accounting for Structured Transactions
- Commodity Trading Activities
  - Core Products
  - Emerging Products
- Merchant Asset and Investment Portfolio
- Related Party Transactions
- Impact of Rulemaking Activity

2001 Specific

- Continued Refinement of Policies Related To:
  - Securitizations and Syndication Vehicles
  - MTM Applications
    - Emerging Products
    - Multi-element Contracts
    - Lease vs. Executory Contract
- Credit and Other Trading Related Exposures
- Structured Transaction Activity
- Rationalization of Business Segments and Related Reporting
- Rationalization of Assets (Sales or Otherwise)

ENRON

ARTHUR ANDERSEN

U.S. Senate Permanent Subcommittee on Investigations
(Source: April 20, 2001, Andersen Presentation to Enron Audit Committee.)
EXHIBIT #9

AAHEC(2)02745.13

SMART Tool
Enron Corp.

Approval Report

Risk Drivers

Drivers		Assessments
1.	Financial Health	Good
2.	Industry/Operations Risk	Significant
3.	Management Ability	Excellent
4.	Management Opportunities Risk	Moderate
5.	Management Pressures	Very Significant
6.	Management Integrity and Behavior	Good
7.	Accounting and Financial Reporting Risk	Very Significant

Critical Issues

Industry/Operations Risk

Your overall assessment of this entity's Industry/Operations Risk is Significant or Very Significant. Please document below any critical issues in this entity's Industry/Operations.

Enron operates in many different industries, the most material of which creates "significant" risk. These are their trading operations and structured transactions which are addressed throughout this SMART.

Management Pressures

Your overall assessment of this entity's Management Pressures is Significant or Very Significant. Please document below any critical issues in this area.

Enron has aggressive earnings targets and enters into numerous complex transactions to achieve those targets.

Accounting and Financial Reporting Risk

Your overall assessment of this entity's Accounting and Financial Reporting Risk is Significant or Very Significant. Please document below any critical issues in this area.

The Company's personnel are very sophisticated and enter into numerous complex transactions and are often aggressive in structuring transactions to achieve derived financial reporting objectives.

Risk Profile

Risk Profile Elements		Impact
1.	Low Risk Country	N/A
2.	Private Ownership w/ Legal Protections Obtained	N/A
3.	IPO Within Next Year	Increased Risk
4.	Sale/Merger w/o Legal Protection Clauses	N/A
5.	Privity Expected to be Established	N/A

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #10a

SCGA(TX)012368

6.	Low Capital at Risk	N/A
7.	High Market Risk	Increased Risk
8.	First or Second Year Engagement	N/A
9.	Management Changes w/ Possible Challenges	N/A

Independence Consideration

Will acceptance of this engagement create an independence violation under the guidelines of the Firm's Ethical Standards? — No

Conflict of Interest

Will acceptance of this engagement create a conflict of interest, including adversarial positions with existing clients of either AA or AC? — No

Professional Competence Risk

Does the engagement team, including appropriate industry and specialty experts who will be a direct part of the team, have the relevant experience and competence and sufficient available time to: a) address the primary and other industries noted above, b) address each of the certain issues and risks noted above and c) reduce the engagement risk to an acceptable level? — Yes

You have indicated that the engagement team, including any industry and specialty experts assigned to the team, has the relevant experience, competence and availability to a) address the primary and other industries noted above, b) address each of the issues noted above and c) reduce the engagement risk to an acceptable level. Please state the relevant experience and competence of the engagement team including the names and descriptions of the industry and specialty experts assigned.

The Enron engagement is made up of various audit teams, each reponsible for various geographical regions and/or business units. The engagement team includes eight partners (two exclusively control work oriented) and twenty-eight managers. Each audit team is comprised of a partner/manager group with relevant experience in their particular industry segment.

Is the engagement partner licensed to sign this report in the jurisdiction where the engagement is performed or the client is located? — Yes

Engagement Economics

Estimated Net Audit Fees in Local Currency:	9576500
Currency:	USD
Estimated Net Audit Fees in US Dollars (in thousands):	$500 +
Estimated Net Audit Fees Per Hour in US Dollars:	$101 to $125
Estimated Planned Fee Adjustment %:	51% +
Estimated Contribution as a-% of Net Audit Fees:	51% to 60%

The audit fee targets established by North America ABA leadership have not been met. You are required to complete the Client Attribute Tool (located in Research Manager) and obtain the approval of the ABA Head to accept or retain this engagement. Please document below your resolution of this matter.

These job economics are embellished by other work performed for Enron. Enron is the largest client of the Firm with a 74% recovery and a $158 net rate on a total engagement and worldwide basis.

Risk Classification & Rationale

SMART Risk Classification: **Maximum***

Final Current Year Risk Classification: **Maximum***

Prior Year Risk Classification: **Maximum**

Rationale for Acceptance / Retention Decision: (required if risk is High, Max, or Max* and/or if the engagement profitability is low based on local targets)

We recommend that this engagement be accepted/retained and believe (1) the risks identified can be managed to an acceptable level, (2) the engagement team is well qualified to manage the risks of this engagement and (3) although Enron enters into complex transactions, they regularly consult with us and other experts. Enron's management is very sophisticated and understands their risks. Further, if subsequent facts or situations raise significant concerns about this accept/retain decision or the ability to manage the engagement risks, we will immediately consult with the signees below.

Approvals

Required Approver	Name	Approval Obtained

Engagement Team

I, the partner on this engagement, have reviewed this report for completeness and accuracy and based on my review, recommend that the engagement be accepted/retained based on acceptable client risk and engagement economics.

Engagement Partner: David B. Duncan [signature]

AASCGA(TX)012370

Other Approvers

Office/Division ABA Head	William E. Swanson	✓
ABA Practice Director	Michael C. Odom	✓
Other Approver (if required)	Michael M. Lowther	✓
Other Approver (if required)	D. Stephen Goddard	✓

Accounting and Financial Reporting Risk

Overall Assessment	Very Significant ✓

Critical Issues Your overall assessment of this entity's Accounting and Financial Reporting Risk is Significant or Very Significant. Please document below any critical issues in this area.

The Company's personnel are very sophisticated and enter into numerous complex transactions and are often aggressive in structuring transactions to achieve derived financial reporting objectives.

Detail Assessment

1. Selection of accounting policies and methods of applying them (Although not all inclusive, consider the following in making this assessment):

a) Objectivity in the client's methodologies, assumptions and estimations	Significant	✓
b) Revenue recognition policies	Significant	✓
c) Deferral costs and amortization periods	Very Significant	✓
d) Asset reserves (e.g., bad debt / loan loss, inventory obsolescence, etc.) and impairment of long-lived assets	Significant	✓
e) Accrued liabilities (e.g., self insurance, environmental, other loss contingencies, etc.)	Significant	✓
f) Unusual / nonrecurring charges to income (e.g., restructuring charges, etc.)	Significant	✓
g) Change in accounting policies or year-end adjustments that increase income	Moderate	✓
h) Accounting for business combination purchase price allocations	Significant	✓
i) Other	Significant	✓

2. Complex/risky transactions:

a) Highly risky or speculative transactions	Significant	✓
b) Form over substance transactions	Very Significant	✓
c) Transactions with related parties	Significant	✓

3. Complex/risky accounts:

a) Revenue recognition	Significant	✓
b) Collectibility of receivables	Minimal	✓
c) Inventory risks (e.g., valuation, obsolescence, existence)	Minimal	✓

d) Realizability of intangibles/"soft" assets	Moderate			✓						
e) Valuation of income tax or other tax liabilities	Significant-						✓			
f) Investments audited by others or unaudited (i.e., custody and responsibility assigned to third parties)	Minimal-	✓								
g) Asset portfolio valuations (e.g., investments, real estate, loans)	Very Significant							✓		

4. Contingencies and uncertainty exposures:

a) Self-insurance exposure	Moderate		✓							
b) Off balance sheet exposures (e.g., derivatives)	Significant				✓					
c) Year 2000 compliance exposure (e.g., financial/operating systems, suppliers/customers, third parties, regulators)	Significant				✓					
d) Other (e.g., litigation, environmental exposure, product liability, taxes, warranties)	Moderate		✓							

5. Other complex/risky transactions and accounts	Very Significant-								✓	
6. Industry specific risk factors for banks, savings and loans, finance companies, insurance companies, mutual funds, real estate/construction companies and hospitality/gaming companies (see guidance)	Moderate-			✓						

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EXHIBIT #11

Specific References to Whitewing/Nighthawk/Osprey in Enron's Board/Committee Presentations[1]

Date	Document	Description
12/09/97	Board of Director Minutes	Project Nighthawk: Board authorizes the creation of a structured finance vehicle funded $500 million by Enron (later increased to $560 million) and $500 million by Citibank; these funds are used to buy $1 billion in Enron convertible preferred stock. Result is $500 million in net funding for general corporate purposes that does not have to be shown on the balance sheet as debt. Dr. Winokur presented Nighthawk to the full board; motion to approve the transaction made by Dr. Winokur, seconded by Mr. Blake.
02/01/99	Special Board of Director Minutes	Project Daybreak: Plan to restructure Whitewing to "expand balance sheet capacity" and "create an additional syndication vehicle for the merchant (asset) portfolio." Mr. McMahon presented to Board; motion to approve the transaction made by Mr. Foy, seconded by Dr. Winokur.
09/17/99	Special Board of Director Minutes	Project Condor: Formation of Osprey Trust which will issue $1.4 billion in debt securities. Proceeds to be used to purchase a limited partner interest in Whitewing (which will then use the proceeds to buy Enron assets.) Mr. McMahon presented; motion to approve the transaction made by Mr. Duncan, seconded by Mr. Blake. (Includes presentation pages faxed to Directors.)
10/11/99	Arthur Andersen report to the Audit Committee	"3rd Quarter Observations: Sizeable Joint Venture Formed with Potential to Facilitate Future Monetizations." Andersen highlights Whitewing/Osprey as one of three significant events in quarterly presentation to the Audit Committee.

[1] *Prepared by U.S. Senate Permanent Subcommittee on Investigations, May 2000*

08/07/00	Finance Committee presentation	"EGF (Enron Global Finance) Execution Schedule - 2000 Balance Sheet Management" lists Enron asset sales to Whitewing of $561 million and notes expanded Whitewing capacity.
08/07/00	Finance Committee meeting packet	Enron Deal Approval Sheet ("DASH") sent to all Finance Committee members for their review; provides detail on Project Margaux: "This transaction allows Enron to keep the interests it holds in the assets (power plants in Italy, Poland and Turkey) through Whitewing off-balance sheet, while restoring Whitewing's liquidity and thereby enabling it to make further asset purchases if so desired." At the time of this transaction (June 2000) Whitewing had $471.9 million invested in the three power plants that were once owned outright by Enron.
12/11/00	Finance Commitee presentation	Major Transactions, June 30-December 31, 2000 includes "Osprey Trust Add-on" of $1 billion. It is described as "Off-Balance Sheet Acquisition vehicle, allows for positive funds flow."
12/13/00(?)	Board presentation: "2000 Enron Strategic Goals Status"	"Goal: Provide platforms for increased capital velocity to achieve return on equity target" "Status: Complete - Established numerous vehicles to stimulate capital markets and *reduce use* of Enron equity - • Raptor • Hawaii 125 • Osprey
02/12/01	Finance and Audit Committee presentation	"LJM Investment 2000 Activity with Enron" Includes the "Osprey Add-On: Purchases of additional Trust Certificates in Osprey - an unaffiliated equity and debt holder of Whitewing, an Enron non-consolidated affiliate, which invests in both domestic and foreign merchant and other assets." Presentation page also mentions Margaux, a project that relied on Whitewing financing.

02/12/01	LJM Approval Sheet	Included in briefing packets sent to Audit and Finance Committees in February 2001. Transaction reviewed is "Osprey Certificate Follow-On" which closed in July 2000. "LJM and three other equity investors are purchasing additional (debt) certificates from Osprey Trust. Osprey Trust has an ownership interest in a structured vehicle that has acquired certain assets from Enron."
04/30/01	Finance Committee presentation	"Stock Price Risk in Financings - Potential Required Future Equity Issuance" - lists Osprey as one of the vehicles that would require additional Enron shares (10.7 million) if Enron's stock dropped to $40/share. At the time, Enron stock had dropped from a high of $90/share to $60/share and would never recover.
10/08/01	Board of Director Minutes	Dr. Winokur "reviewed the maturities and refinancings planned for the structures referred to as Marlin and Whitewing."
10/22/01	Statement prepared by Enron public relations for Board members regarding SEC inquiry	Includes description of Whitewing/Osprey and the disclosure that Osprey's $2.4 billion in debt is supported by the assets of Whitewing which include a contingent obligation of Enron.
12/20/01	Finance Report to Board	Shows two Whitewing entities - Whitewing SE (Screaming Eagle) Acquisition LP and Whitewing Condor Share Trust as the 14th and 16th largest creditor to Enron among all filing entities. Enron obligations to these Whitewing entities total $400 million.
12/20/01	Audit Committee presentation	Special Purpose Entities (SPEs) data sheet: Shows the 1999 Osprey deal which raised $100 million in equity from three institutional investors and LJM and $1.4 billion in debt from John Hancock and others.

MINUTES
MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
December 9, 1997

Minutes of a meeting of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 8:00 a.m., C.S.T., on December 9, 1997, at the Enron Building in Houston, Texas.

All of the Directors were present, as follows:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Mr. Jerome J. Meyer
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Dr. Charls E. Walker
Mr. Bruce G. Willison
Mr. Herbert S. Winokur, Jr.

The meeting was begun in executive session, during which the only non-directors in attendance were Messrs. James V. Derrick, Jr., Tod A. Lindholm, and Edmund P. Segner, III and Mesdames Rosalee T. Fleming and Peggy B. Menchaca.

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Menchaca, recorded the proceedings.

Mr. Lay stated that minutes of meetings of the Board held on October 5 and October 14, 1997, had been distributed to the Directors and were included in the meeting material. He called for additions, corrections, or comments. There being none, upon motion duly made by Mr. Foy, seconded by Mr. Belfer, and carried,

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EXHIBIT #12

AASCGA0071.163

Mr. Winokur stated that the Finance Committee had approved four items for recommendation to the Board: (i) a $500 million equity hybrid financing with Citicorp, N.A., and others; (ii) a new shelf registration in the amount of $1 billion; (iii) the JEDI II Development Fund, including a $500 million capital contribution and a guarantee of $75 million advance facility related to JEDI II revolving line of credit; and (iv) the sale of a minority interest in EES to a private consortium. He moved adoption of each. Mr. Winokur's motion was duly seconded by Mr. Blake and carried, and the following resolutions were approved and adopted:

$500 Million Equity Hybrid Financing

WHEREAS, Enron Corp. (the "Company") desires to consummate a structured finance transaction, with the assistance of Citicorp, N.A. ("Citibank") and its affiliates, by issuing for approximately $1 billion a newly established series of junior convertible preferred stock of the Company (the "Preferred Shares") to a newly organized limited liability company to raise up to approximately $500 million of net funding for general corporate purposes, after taking into account the Company's acquisition of a majority interest in such limited liability company (the "Transaction");

NOW, THEREFORE, IT IS RESOLVED, that the issuance and sale of the Preferred Shares are hereby authorized and approved, and that the Company shall proceed with the consummation of the Transaction in accordance with the resolutions hereby adopted;

RESOLVED FURTHER, that the issuance and sale of the Preferred Shares shall be subject to the following terms and conditions (the "Board Conditions"):

(i) the maximum number of Preferred Shares to be issued shall not exceed 300,000;

(ii) the Preferred Shares shall initially be convertible into no more than 30,000,000 shares of common stock of the Company ("Common Stock"), such number of shares to be subject to antidilution adjustments to be provided in the terms of the Preferred Shares; and

(iii) the aggregate liquidation preference of the Preferred Shares, exclusive of accrued dividends, shall not exceed $1.1 billion;

RESOLVED FURTHER, that Kenneth L. Lay, Jeffrey K. Skilling, and Herbert S. Winokur, Jr. are hereby appointed as a committee of this Board of Directors (the "Committee"), with the power and authority of the full Board of Directors to the fullest extent permitted by law, to authorize and approve all agreements, instruments, and documents, and the taking of all actions, as the Committee may deem necessary or desirable to consummate the Transaction (subject, however, in all respects, to the Board Conditions), including, without limitation:

(i) the determination of all or any part of the terms of the issuance and sale of the Preferred Shares; including, but not limited to, the determination that the consideration received or to be received by the Company for the Preferred Shares is adequate;

(ii) the determination of all or any part of the designation and relative rights, preferences, and limitations of the Preferred Shares (the "Designation");

(iii) the approval of a form of certificate representing the Preferred Shares;

(iv) the authorization, execution, and delivery of a limited liability company agreement, with such terms and conditions as the Committee shall approve, relating to a limited liability company (the "LLC") in which the Company will be a member with, at least initially, a majority economic interest (it being understood and approved that the Company may, in the future, make additional capital contributions to the LLC), and which LLC will acquire the Preferred Shares and which will enter into one or more loans to the Company in an aggregate amount outstanding at any one time not currently expected to exceed $100 million;

(v) the authorization, execution, and delivery of a Preferred Stock Purchase and Registration Agreement, with such terms and conditions as the Committee shall approve, between the Company and the LLC;

(vi) the authorization, execution, and delivery of a Purchase Option Agreement, with such terms and conditions as the Committee shall approve, among the Company and various other parties (the "Purchase Option Agreement");

(vii) the authorization, execution, and delivery of an Enron Agreement, with such terms and conditions as the Committee shall approve, executed by the Company in favor of the indemnified parties referred to therein;

(viii) the authorization, execution, and delivery of a supplement to the ISDA Master Agreement, with such terms and conditions as the Committee shall approve, between the Company and Citibank providing for a payment to Citibank in the form of cash or securities of the Company in the event of, among other things, a decline in the price of the Common Stock, with a maximum settlement amount payable by the Company of $500 million; and

(ix) the authorization, execution, and delivery of such other agreements, instruments, and documents relating to the Transaction, including, but not limited to, agreements, instruments, and documents that provide, among other things, for the indemnification of third parties, the granting of registration rights, and the payment of fees and expenses of third parties;

RESOLVED FURTHER, that the direct or indirect repurchase at any time or from time to time by the Company of all or a part of the Preferred Shares for an amount not exceeding $600 million in the aggregate pursuant to the terms of the Purchase Option Agreement or otherwise pursuant to the terms of any other agreement executed by the Company in connection with the Transaction are hereby authorized and approved;

RESOLVED FURTHER, that pursuant to the authority expressly granted and vested in this Board of Directors by the Company's Amended and Restated Articles of Incorporation (as amended, the "Articles"), and pursuant to the appointment and authorization by this Board of Directors of the Committee, this Board of Directors hereby authorizes the amendment of the Articles for the purpose of the creation of the Preferred Shares, and hereby authorizes the Committee and the officers of the Company to authorize, execute, and deliver for filing the Articles of Amendment, setting forth the Designation of the terms of the Preferred Shares, with the Office of the Secretary of State of the State of Oregon and such other offices as the Committee and/or the officers of the Company shall deem necessary or advisable;

RESOLVED FURTHER, that upon issuance of certificates for the Preferred Shares in accordance with the foregoing resolutions, such Preferred Shares shall be validly issued, fully paid, and nonassessable;

RESOLVED FURTHER, that, subject to the Board Conditions, effective immediately upon issuance of such shares of the Preferred Shares, there will be reserved a number of shares of Common Stock of the Company for issuance to the holders of the Preferred Shares upon the conversion of such Preferred Shares pursuant to the conversion rate for the Preferred Shares authorized and approved by the Committee in accordance with the Board Conditions;

RESOLVED FURTHER, that upon any adjustment to the conversion rate for the Preferred Shares, sufficient additional shares of Common Stock (and such other shares of capital stock of the Company, if applicable, as a result of the antidilution provisions of the Preferred Shares) shall be reserved and kept available so that the maximum number of shares of Common Stock (and such other capital stock) issuable upon conversion of the Preferred Shares shall at all times be reserved and kept available;

RESOLVED FURTHER, that the Company is authorized to issue such shares of Common Stock of the Company (and such other capital stock) upon conversion of the Preferred Shares, and that upon any such issuance, such shares of Common Stock (and such other capital stock) shall be validly issued, fully paid, and non-assessable;

RESOLVED FURTHER, that if it is deemed necessary or advisable by the Committee or the officers of the Company that the Preferred Shares and/or the Common Stock issuable upon conversion of the Preferred Shares be qualified or registered for sale under the applicable Blue Sky Laws or securities acts of any jurisdiction, or that a filing be made in any jurisdiction to secure or obtain an exemption from qualification or registration. the Committee and the officers of the Company are each authorized to perform on behalf of the Company any and all such acts as any one or more of them may deem necessary or advisable in order to comply with such laws of such jurisdiction. and in connection therewith. to execute and file all requisite papers and instruments and to make any and all payments of filing. registration. or other fees. costs. and expenses, and to take any and all further action in connection with the foregoing which any one or more of them shall deem necessary or advisable;

RESOLVED FURTHER. that the execution by any officer of the Company of any papers and instruments or the performance by any one or more of them of any act in connection with the foregoing resolutions shall conclusively establish their authority therefor from the Company and the approval and ratification by the Company of the papers and instruments so executed and the actions so taken; and

RESOLVED FURTHER. that the proper officers of the Company and its counsel be. and each of them hereby is. authorized. empowered. and directed (any one of them acting alone) to take any and all such further action. to amend. execute. and deliver all such further instruments and documents. for and in the name and on behalf of the Company. under its corporate seal or otherwise. and to pay all such expenses as in their discretion appear to be necessary. proper. or advisable to effectuate the lawful issuance and sale of the Preferred Shares. and to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

$1 Billion Shelf Registration

WHEREAS. the Company desires to file with the Securities and Exchange Commission (the "Commission") a registration statement and post effective amendments (collectively. the "universal shelf registration statement") which will include the registration of. among other securities. Debt Securities. Preferred Stock. Depository Shares. Common Stock. and Common Stock Warrants; and

WHEREAS. this Board desires to provide for the issuance and sale of Debt Securities. Preferred Stock. Depository Shares. Common Stock. and Common Stock Warrants by the Company:

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

JEDI II $500 Million Commitment and Guaranty

RESOLVED, that the formation of Joint Energy Development Investments II Limited Partnership ("JEDI II" or the "Partnership"), a Delaware limited partnership in which certain affiliates of the Company will own a 1% general partnership interest and a 49% limited partnership interest and commit to make capital contributions of up to $500,000,000, of which up to 50% can be made in the Company's common stock, is hereby approved and that the business purpose of JEDI II will be to make energy related investments that are developed by certain affiliates of the Company;

RESOLVED FURTHER, that each of the Chairman of the Board, the Vice Chairman of the Board, the President of the Company, or any Vice President of the Company (any one of them acting alone) is hereby authorized and empowered to negotiate, execute, deliver, perform, and consummate, for and in the name and on behalf of the Company, the following agreements in connection with the formation of JEDI II, each such agreement to be in substantially the form that was agreed to in connection with the transactions related to the formation of Joint Energy Development Investments Limited Partnership ("JEDI"), with such changes, additions, and modifications to the form of each such agreement as any such officer of the Company executing the same may approve (including, without limitation, any future amendments, changes, additions, or modifications from time to time to each such agreement), such execution to be conclusive evidence of such approval on behalf of the Company:

1. A Shares Issuance and Registration Rights Agreement (the "Purchase Agreement") to be executed by the Company, the Partnership, Enron Capital Management II Limited Partnership, the general partner of JEDI II,

Enron Capital Management III Limited Partnership, a limited partner of JEDI II, and The California Public Employees' Retirement System, a limited partner of JEDI II, which will facilitate the making of capital contributions by the Enron partners of JEDI II with the Company's common stock; and

2. All other agreements necessary, advisable, or desirable for the consummation of the transactions relating to the formation of the Partnership or any of the foregoing agreements:

(all such agreements collectively called the "Principal Agreements"):

RESOLVED FURTHER, that all Principal Agreements authorized under these resolutions may be expected to benefit, directly or indirectly, the Company, and it is in the best interest of the Company to enter into the Principal Agreements, and the Principal Agreements are necessary or convenient to the conduct, promotion, or attainment of the business of directly or indirectly wholly-owned subsidiaries of the Company;

RESOLVED FURTHER, that the Company is authorized and directed to observe and perform in full all of the obligations, conditions, covenants, and other terms set forth in or contemplated by the Principal Agreements as the same may be amended from time to time as hereby provided:

RESOLVED FURTHER, that the Chairman of the Board, the Vice Chairman of the Board, the President of the Company, or any Vice President of the Company be, and each of them hereby is, authorized in the name and on behalf of the Company, under its corporate seal or otherwise, to negotiate, execute, deliver, amend, perform, and consummate such other agreements, instruments, or documents as such officer may deem necessary or desirable to carry out the purpose and intent of the resolutions herein, in such forms as shall be approved by the officer executing the same, such approval to be conclusively evidenced by the execution thereof by such officer:

RESOLVED FURTHER, that each such officer be, and each such officer hereby is, authorized in the name and on behalf of the Company to take or cause to be taken such action as such officer may deem necessary or desirable in connection with the performance by the Company of its obligations under any agreement, document, or instrument related to these transactions to which the Company is a party;

RESOLVED FURTHER, that all actions heretofore taken by any officer of the Company, in the name and on behalf of the Company, related to or in connection with the transactions contemplated by these resolutions, including without limitation the execution and delivery of any instruments or other documents as any officer shall have deemed necessary, proper, or advisable, are hereby adopted, ratified, confirmed, and approved in all respects; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Monetization of EES

RESOLVED, that the formation by Enron Corp., an Oregon corporation (the "*Company*"), of a Delaware limited liability company to be known as "Enron Energy Services, L.L.C." ("*EES*") is hereby ratified and approved and that the execution and delivery by an officer of the Company of a Limited Liability Company Agreement for EES (the "EES LLC Agreement") is hereby ratified and approved;

RESOLVED FURTHER, that the business purpose of EES and its subsidiary companies shall be to conduct the retail energy business of the Company and its wholly-owned subsidiaries in the United States, and the officers of the Company are authorized to refine, elaborate upon, and modify such description of the business purpose of EES and its subsidiaries in such manner as they deem appropriate and in the best interests of the Company;

RESOLVED FURTHER, that in connection with the formation of EES, the officers of the Company are hereby authorized

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5/11/99

MINUTES
SPECIAL MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
February 1, 1999

Minutes of a special meeting of the Board of Directors of Enron Corp. ("Company"), held pursuant to waiver of notice at 2:00 p.m., C.S.T., on February 1, 1999, at the Enron Building in Houston, Texas.

The following Directors were present, constituting a quorum, by telephone conference connection whereby each of the participants could hear the comments and discussions by the other participants and join in the discussions:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Mr. Herbert S. Winokur, Jr.
Dr. Charls E. Walker

Directors Ronnie C. Chan, John H. Duncan, Jerome J. Meyer, and John Wakeham were absent from the meeting. Messrs. Richard A. Causey, Michael K. Kopper, and Jeffrey McMahon and Ms. Peggy B. Menchaca, all of the Company, also attended the meeting.

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Menchaca, recorded the proceedings.

Mr. Lay stated that the primary purpose of the meeting was to consider a public offering of the Company's common stock. He stated that in addition, an item would be presented for the Board's consideration called "Project Daybreak" which was similar in structure to a project previously approved by the Board known as "Project Nighthawk." He called upon Mr. Skilling to present the first item.

Mr. Skilling stated that with current market conditions, management recommended a sale of 12 million shares of common stock pursuant to an underwritten

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EXHIBIT #13

AASCGA0073.6

necessary to effect the aforesaid listing; and that the officers of the Company be, and they hereby are, authorized and directed to execute and deliver any applications, documents, or agreements, to take any and all actions, to appear before such exchanges if necessary, to appoint any banking or other institution as an agent of the Company for any purpose, and to do or cause to be done any and all things as may appear to them to be necessary or desirable in order to effect such listing; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Mr. McMahon reminded the Board of the details of a transaction that the Company consummated with the assistance of Citicorp, N.A. and its affiliates in December, 1997, known internally as Project Nighthawk. He said that the current proposal would result in a restructuring of the transaction that would expand balance sheet capacity and would create an additional syndication vehicle for the merchant portfolio. He noted that the transaction would increase the number of shares of common stock outstanding, on a fully diluted basis, but would be non-dilutive. He stated that Board approval was required to (i) approve the redemption of all or a portion of the shares from the initial transaction approved in December, 1997, and (ii) permit the distribution of the Company's demand note back to the Company. Following discussion, upon motion duly made by Mr. Foy, seconded by Mr. Winokur, and carried, the following resolutions were approved:

WHEREAS, Enron Corp. (the "Company") consummated a transaction with the assistance of Citicorp, N.A. and its affiliates in December 1997, which involved, among other things, the issuance of 250,000 shares of Series A Junior Voting Convertible Preferred Stock, no par value, of the Company (the "Preferred Shares") to Whitewing Associates, L.L.C. ("Whitewing"), a newly organized limited liability company of which the Company is the Class A managing member; and

WHEREAS, the Company desires to amend the Amended and Restated Company Agreement of Whitewing Associates L.L.C., as amended (the "JV Company Agreement"), and the other transaction documents associated with the transaction in order to, among other things, deconsolidate financially Whitewing from the Company;

NOW, THEREFORE, IT IS RESOLVED, that each of the Chairman of the Board, the Vice Chairman of the Board, the President, any Senior Vice President, and any Vice President of the Company (collectively, the "Officers") is hereby authorized and empowered, for and in the name and on behalf of the Company, to negotiate, execute, and deliver an amendment to, or to otherwise cause the amendment of, the JV Company Agreement and such other documents related to the transaction as may be appropriate or desirable to effectuate such deconsolidation of Whitewing;

RESOLVED FURTHER, that in connection with the foregoing, and without in any way limiting the authority granted in the immediately preceding resolution, the Officers are hereby authorized and empowered to cause (i) Whitewing to (x) distribute to the Company the Demand Promissory Note dated December 29, 1997, in the amount of $78,762,249 and (y) sell or otherwise transfer the Preferred Shares to one or more persons, on such terms and conditions as may be determined by any of the Officers, and (ii) the Company to (x) repurchase or otherwise acquire up to all of the Preferred Shares and (y) effect a partial or full purchase of the interest of Nighthawk Investors L.L.C. ("Nighthawk") in Whitewing pursuant to the Purchase Option Agreement dated as of December 29, 1997, among Enron, Nighthawk, and the other parties thereto;

RESOLVED FURTHER, that in connection with any repurchase or other acquisition of any of the Preferred Shares, the Officers are hereby authorized and empowered to sell, exchange, transfer, or otherwise contribute (or cause the sale, exchange, transfer, or contribution of) assets or instruments of the Company or of its affiliates to Whitewing in exchange for, or as a replacement of, such Preferred Shares, on such terms and for such price as may be determined by any of the Officers (the current expectation being that the value of such assets or instruments would be approximately equivalent to the value of the acquired Preferred Shares);

RESOLVED FURTHER, that the Executive Committee of the Board of Directors is hereby authorized, to the fullest extent permitted by law, to authorize and approve all agreements, instruments, and documents, and the taking of all actions, as such Executive Committee may deem necessary or desirable to consummate the transactions contemplated hereby;

RESOLVED FURTHER, that each of the Officers is hereby authorized, in the name and on behalf of the Company, to take or cause to be taken such action as such Officer may deem necessary or desirable in connection with the performance by the Company of its obligations under any agreement, document, instrument, or amendment related to the transactions contemplated hereby to which the Company is a party;

RESOLVED FURTHER, that the execution by any officer of the Company of any papers and instruments or the performance by any one or more of them of any act in connection with the foregoing resolutions shall conclusively establish their authority therefor from the Company and the approval and ratification by the Company of the papers and instruments so executed and the actions so taken; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action (including filings pursuant to the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended), to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

There being no further business to come before the Board, the meeting was adjourned at 2:20 p.m., C.S.T.

Peggy B. Menchaca
Secretary

APPROVED:

Kenneth L. Lay
Chairman

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12/27/46

MINUTES
SPECIAL MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
September 17, 1999

Minutes of a special meeting of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 4:30 p.m., C.D.T., on September 17, 1999 at the Enron Building in Houston, Texas.

The following Directors were present, constituting a quorum, in person or by telephone conference connection whereby each of the participants could hear the comments and discussions by the other participants and join in the discussions:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Dr. John Mendelsohn
Mr. Jerome J. Meyer
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

Director Rebecca P. Mark was absent from the meeting. Messrs. Jeffrey McMahon and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company, also attended the meeting.

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Lay called the meeting to order and inquired if the Committee members had received the material for the meeting, and each responded that he or she had received the material. He stated that the meeting had been called for the Board to consider a financing transaction and called upon Mr. McMahon to present the matter.

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EXHIBIT #14

AASCGA0073.149

Mr. McMahon stated that in December of 1997 the Company, with the Board's approval, had put in place a financing structure referred to as "Condor". He reviewed the original Condor transaction and stated that the Company and an outside third-party ("Nighthawk") had each contributed $500 million cash to a financing vehicle ("Whitewing"). Whitewing then paid the Company $1 billion cash for the Company's mandatory convertible preferred stock. He stated that the primary purpose of the transaction had been to convert debt to equity. He stated that the value of the preferred stock in Whitewing, in which the Company has a 50% ownership interest, had increased significantly since the original transaction. He stated that the Company was proposing a redemption of the original preferred stock and the issuance of a similar preferred stock. He stated that this would allow the Company to take advantage of the increase in value of the preferred stock. He discussed how Condor would be structured after the redemption of the preferred stock, noting that Whitewing would be funded by a private placement sale of bonds to institutional investors and outside equity. The Company would then contribute assets from its "Merchant Portfolio" and receive cash from Whitewing. Following a discussion in which Mr. McMahon answered questions from the Committee, upon motion duly made by Mr. Duncan, seconded by Mr. Blake, and carried, the following resolutions were approved:

> WHEREAS, Enron Corp. (the "Company") desires to consummate a structured finance transaction using a newly established series of Mandatorily Convertible Junior Preferred Stock, Series B of the Company (the "Preferred Shares") which are to be exchanged for the outstanding Series A Junior Voting Convertible Preferred Stock of the Company ("Exchanged Shares") presently held by Whitewing Associates L.L.C. ("Whitewing") to raise up to approximately $1.5 billion of funding for general corporate purposes (approximately $930 million) and to restructure the outstanding equity of Whitewing and provide funds for the repayment of a previous structured financing (approximately $570 million) which transaction involves the sale by Donaldson, Lufkin & Jenrette Securities Corporation, Deutsche Bank Securities Inc., Bear, Stearns & Co. Inc., and Salomon Smith Barney Inc. (together the "Initial Purchasers") of up to $1,400,000,000 of senior secured notes (the "Osprey Notes") of a newly formed entity, Osprey Trust, and the issuance and sale by Osprey Trust of approximately $100 million of trust certificates (the "Osprey Trust Certificates") and the purchase by Osprey Trust using the proceeds of such offerings of a limited partner interest in Whitewing (which will be converted into a limited partnership in connection with such transactions) (all transactions necessary to recapitalize Whitewing and to consummate the sale of the Osprey Notes and the Osprey Trust Certificates are herein referred to as the "Osprey Transactions");

NOW, THEREFORE, IT IS RESOLVED, that the Osprey Transactions and the issuance of the Preferred Shares are hereby authorized and approved, and that the Company shall proceed with the consummation of such transactions in accordance with the resolutions hereby adopted;

RESOLVED FURTHER, that the issuance of the Preferred Shares and the Osprey Transactions shall be subject to the following terms and conditions (the "Board Conditions"):

(i) the Preferred Shares shall have the terms and conditions and powers, preferences, and relative, participating, optional, or other special rights, and the qualifications, limitations, and restrictions set forth in the Statement of Resolutions attached hereto as Exhibit A and which is incorporated herein by this reference as if fully set forth herein (together with any changes thereto consistent with the Board Conditions negotiated by and among the Initial Purchasers, the purchasers of the Osprey Trust Certificates, and the Company and approved by an officer of the Company or other person authorized and empowered to act pursuant to these resolutions, the execution and filing of which by any such officer or person, in the name and on behalf of the Company, with the appropriate agencies of the State of Oregon to be conclusive evidence of the approval by such officers or person of the contents thereof;

(ii) the maximum number of Preferred Shares to be issued shall be an indefinite number of shares up to the number of shares necessary to fulfill the Company's obligations pursuant to the Share Settlement Agreement (as defined in Exhibit A), but in no event more than the number of authorized but unissued shares of Preferred Stock, with 250,000 shares to be initially issued;

(iii) the Preferred Shares shall initially be convertible into no more than 50,000,000 shares of common stock of the Company ("Common Stock") (the same number of shares of Common Stock into which the Exchanged Shares are presently convertible), and the number of shares of Common Stock which the Company may ultimately be obligated to issue at the maturity of the Osprey Transactions shall also be increased by (a) antidilution adjustments to be provided in the terms of the Preferred Shares and (b) the requirements of the Share Settlement Agreement upon a resale by the share trust pursuant to Remarketing (as defined in the remarketing and registration rights agreement associated with the Preferred

Shares) based on the closing price per share of Common Stock on or about the date of such resale or such Remarketing, but in no event more than the number of authorized but unissued shares of Common Stock that have not been reserved by the Board of Directors for other purposes as of the date of such resale or such Remarketing (or as of such other date determined by any officer of the Company authorized to act in accordance with these resolutions);

(iv) the liquidation preference per share of the Preferred Shares, exclusive of accrued dividends, shall not exceed $4,000 (an aggregate of $1.0 billion) in respect of initially issued Preferred Shares; and

(v) the number of shares of Common Stock that may be issued after the Preferred Shares have been issued pursuant to the remarketing and registration rights agreement referred to above shall not exceed the number of authorized but unissued shares of Common Stock that have not been reserved by the Board of Directors for other purposes as of the date of such issuance;

RESOLVED FURTHER, that each of the Chairman and Chief Executive Officer, the President and Chief Operating Officer, any Vice Chairman or any Vice President is hereby authorized, empowered, and directed, with the power and authority of the full Board of Directors to the fullest extent permitted by law, to authorize and approve (or ratify if already executed or taken) all agreements, instruments, and documents, and the taking of all actions, as any such officer may deem necessary, advisable, convenient, or proper to consummate the Osprey Transactions and the issuance of the Preferred Shares (subject, however, in all respects, to the Board Conditions), including, without limitation:

(i) the determination of all or any part of the terms of the issuance of the Preferred Shares;

(ii) the determination of all or any part of the designation and relative rights, preferences, and limitations of the Preferred Shares;

(iii) the approval of a form certificate representing the Preferred Shares;

(iv) all matters insofar as they affect the Company or any of its subsidiaries or affiliates associated with the issuance of the Osprey Notes and the Osprey Trust Certificates and the authorization, execution, and delivery by the purchasers of the Osprey Certificates of a trust agreement for Osprey Trust with such terms and conditions relative to the Company and any of its subsidiaries or affiliates as such officer shall approve;

(v) the authorization, execution, and delivery of a purchase agreement among the Company, Osprey Trust, and the purchasers of the Osprey Trust Certificates for the sale of the Osprey Trust Certificates with such terms and conditions (including pricing terms) as such officer shall approve;

(vi) the authorization, execution, and delivery of a purchase agreement among the Company, Osprey Trust, and the Initial Purchasers for the sale of the Osprey Notes with such terms and conditions (including pricing terms) as such officer shall approve;

(vii) the authorization, execution, and delivery of an indenture among Osprey Trust, Osprey I, Inc. and a trustee to be selected with such terms and conditions as such officer shall approve;

(viii) the approval insofar as they affect the Company or any of its subsidiaries or affiliates of a form of note representing the Osprey Notes and a certificate representing the Osprey Certificates;

(ix) the authorization, execution, and delivery of a participation agreement (the Osprey Participation Agreement") among the Company, Osprey Trust, Whitewing, Whitewing Management LLC, Egret I LLC, Peregrine I LLC, Condor Share Trust, and the Indenture Trustee providing for the parties' participation in the Osprey Transactions and certain undertakings made by each of the parties, with such terms and conditions as such officer shall approve;

(x) the authorization, execution, and delivery of (a) a remarketing and registration rights agreement among the Company, Condor Share Trust, Osprey Trust, Whitewing Associates L.P., Whitewing Management LLC, the Indenture Trustee, and the Initial Purchasers providing for, among other things, the registration of the Preferred Shares or Common Stock into which it is convertible, and (b) the related Share Settlement Agreement providing for the potential issuance of additional Preferred Shares or Common Stock to the extent required by the remarketing and registration rights agreement and such Share Settlement Agreement with such terms and conditions as such officer shall approve;

(xi) all matters insofar as they affect the Company or any of its subsidiaries or affiliates associated with the formation of Whitewing Associates L.P. (by the conversion of Whitewing into a limited partnership) and its subsidiary, Condor Share Trust, including the authorization, execution, and delivery of a trust agreement for the formation of Condor Share Trust with such terms and conditions as such officer shall approve; and

(xii) the negotiation, authorization, execution, and delivery of such other agreements, instruments, and documents relating to the Osprey Transactions and the Preferred Shares, including, but not limited to, agreements, instruments, and documents that provide, among other things, for the indemnification of third parties, and the payment of fees and expenses of third parties as such officer may deem necessary, advisable, convenient, or proper in connection with the Osprey transactions or any other matters addressed by these resolutions;

RESOLVED FURTHER, that Ben Glisan is hereby appointed as agent and attorney-in-fact of the Company and is authorized, empowered, and directed, with the power of the full Board of Directors, subject to control and direction by the Company, to the fullest extent permitted by law, to authorize and approve all agreements, instruments, and documents and the taking of all actions as such agent and attorney-in-fact may deem necessary or desirable and shall have all the powers of an officer of the Company with respect to these resolutions (subject, however, in all respects, to the Board Conditions) solely for the purpose of consummating the Osprey Transactions (excluding, however, the issuance of the Preferred Shares and the matters set forth in or contemplated by (ii) and (iii) in the immediately preceding resolution); it is the intent of the Board of Directors that Mr. Glisan, in his capacity as agent and attorney-in-fact of the Company, shall have all the duties, obligations, and responsibilities of an officer of the Company for purposes of the Osprey Transactions, as if he were an officer of the Company;

RESOLVED FURTHER, that pursuant to the authority expressly granted and vested in this Board of Directors by the Company's Amended and Restated Articles of Incorporation (the "Articles"), and pursuant to the appointment and authorization by this Board of Directors to the officers of the Company set forth above, this Board of Directors hereby authorizes the amendment of the Articles for the purpose of the creation of the Preferred Shares, and hereby authorizes the officers of the Company to authorize, execute, and deliver for filing the Articles of Amendment, setting forth the Statement of Resolutions of the terms of the Preferred Shares, with the Office of the Secretary of State of the State of Oregon and such other offices as the officers of the Company shall deem necessary or advisable;

RESOLVED FURTHER, upon issuance of certificates for the 250,000 initially issued Preferred Shares in exchange for the Exchanged Shares in accordance with the foregoing resolutions, such Preferred Shares shall be validly issued, fully paid, and nonassessable;

RESOLVED FURTHER, upon issuance of certificates for any Preferred Shares required to be issued pursuant to the terms of the Share Settlement Agreement in accordance with the terms of the Share Settlement Agreement and in accordance with the foregoing resolutions, such Preferred Shares shall be validly issued, fully paid, and nonassessable;

RESOLVED FURTHER, that the 50 million common shares currently reserved for Whitewing (in connection with the Exchanged Shares) shall remain reserved under the remarketing and registration rights agreement referred to above in for use in upon the conversion of the Preferred Shares;

RESOLVED FURTHER, that, subject to the Board Conditions, effective immediately upon issuance of the Preferred Shares, there will be reserved 20 million additional shares of Common Stock of the Company and 100,000 Preferred Shares of the Company for issuance under the Share Settlement Agreement;

RESOLVED FURTHER, that upon any adjustment to the conversion price of the Preferred Shares, sufficient additional shares of Common Stock shall be reserved and kept available so that the maximum number of shares of Common Stock issuable upon conversion of the Preferred Shares shall at all times be reserved and kept available;

RESOLVED FURTHER, that the Company is authorized to issue such shares of Common Stock of the Company upon conversion of the Preferred Shares, and that upon any such issuance in accordance with the terms of the Preferred Shares, such shares of

Common Stock shall be validly issued, fully paid, and non-assessable;

RESOLVED FURTHER, that upon issuance of certificates for any shares of Common Stock required to be issued pursuant to the terms of the Share Settlement Agreement in accordance with the terms of the Share Settlement Agreement and in accordance with the foregoing resolutions, such shares of Common Stock shall be validly issued, fully paid, and nonassessable;

RESOLVED FURTHER, that if it is deemed necessary or advisable by the officers of the Company that the Preferred Shares and/or the Common Stock issuable upon conversion of the Preferred Shares be qualified or registered for sale under the applicable Blue Sky Laws or securities acts of any jurisdiction, or that a filing be made in any jurisdiction to secure or obtain an exemption from qualification or registration, or that a listing application be filed with any national securities exchange, the officers of the Company are each authorized to perform on behalf of the Company any and all such acts as any one or more of them may deem necessary or advisable in order to comply with such laws of such jurisdiction or the rules of such exchanges, and in connection therewith, to execute and file all requisite papers and instruments and to make any and all payments of filing, registration, or other fees, costs, and expenses, and to take any and all further action in connection with the foregoing which any one or more of them shall deem necessary or advisable;

RESOLVED FURTHER, that the execution by any officer of the Company of any papers and instruments or the performance by any one or more of them of any act in connection with the foregoing resolutions shall conclusively establish their authority therefor from the Company and the approval and ratification by the Company of the papers and instruments so executed and the actions so taken;

RESOLVED FURTHER, that the actions of the officers of the Company heretofore taken on behalf of the Company in connection with the above resolutions and the actions contemplated thereby are, in all respects, confirmed and ratified, and the officers of the Company, together or individually, may take any and all action and do any and all things as may be deemed by any of them to be necessary or advisable to effectuate the lawful issuance and sale of the Preferred Shares, and the taking of any and all such actions and the performance of any and all such things in connection with the foregoing shall conclusively establish their authority from the Company and the approval and ratification by the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Messrs. Lay and Skilling then gave the Board a brief update on activities throughout the Company.

There being no further business to come before the Board, the meeting was adjourned at 4:50 p.m., C.D.T.

Rebecca C Carter

Secretary

APPROVED:

Kenneth L Lay

Chairman

H:\a Minutes\1999 Minutes\91799sp.doc

SEP.17.1999 11:19AM ENRON CORP. NO.609 P.1/3

Facsimile Cover Sheet

To: Members of the Board of Directors
Company:
Phone:
Fax:

From: Rebecca C. Carter
Company: Enron Corp.
Phone: (713) 853-7241
Fax: (713) 853-2534

Date: 9/17/99
Pages including this cover page:

Comments: We are enclosing two flowcharts to help clarify the transaction to be considered at today's board meeting.

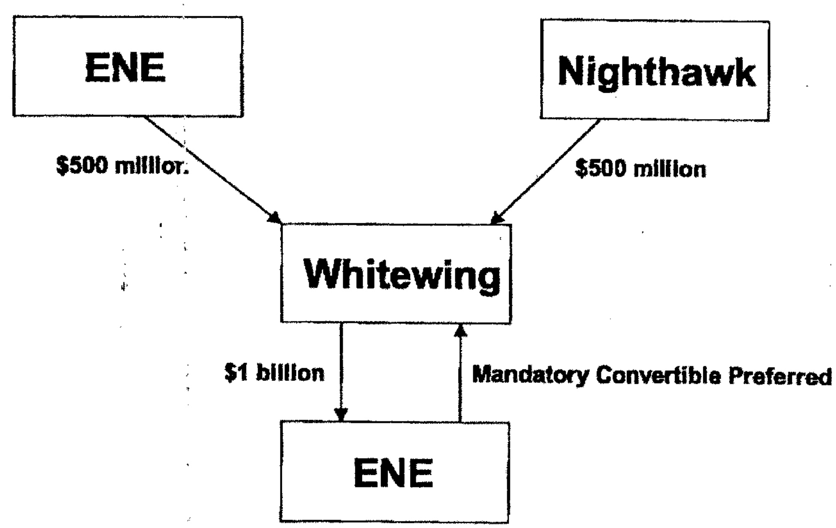
U.S. Senate Permanent Subcommittee on Investigations
(Source: September 1999, Presentation to the Board of Directors.)
EXHIBIT #15

DJM 04874

Condor Transaction

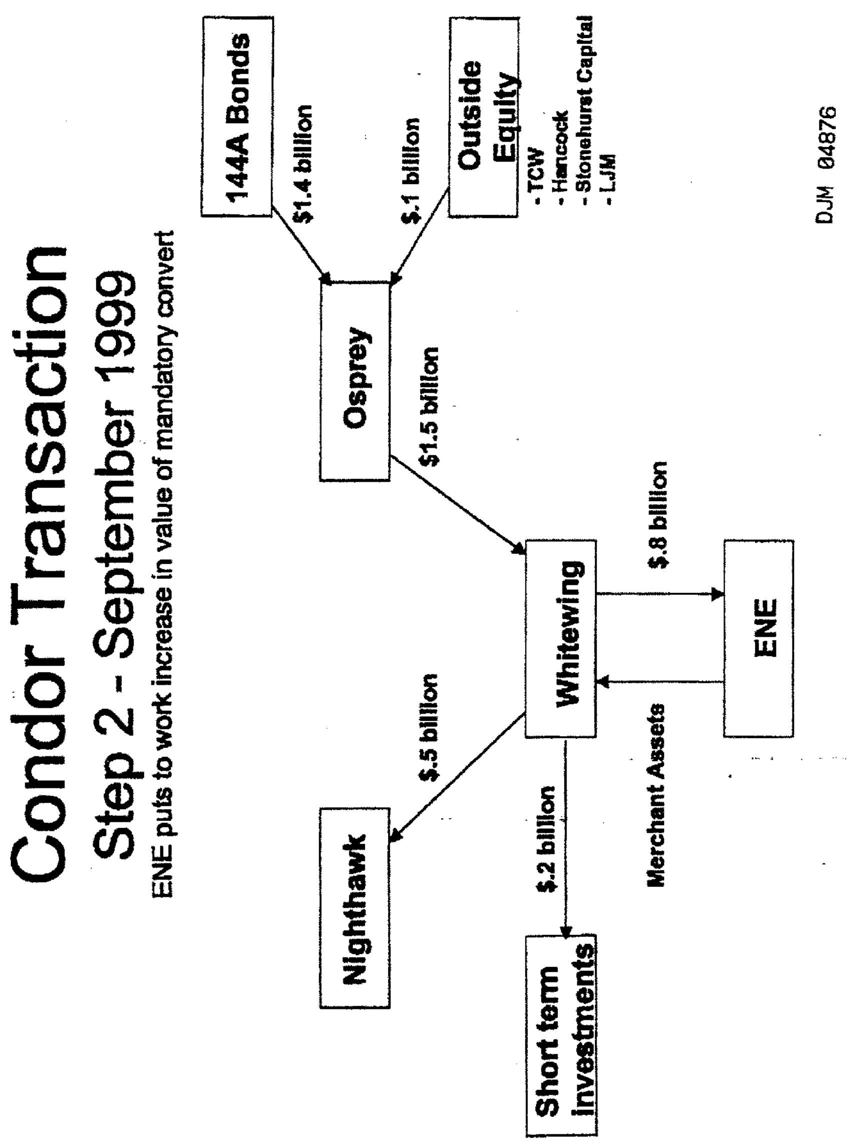
Step 1 - December 1997

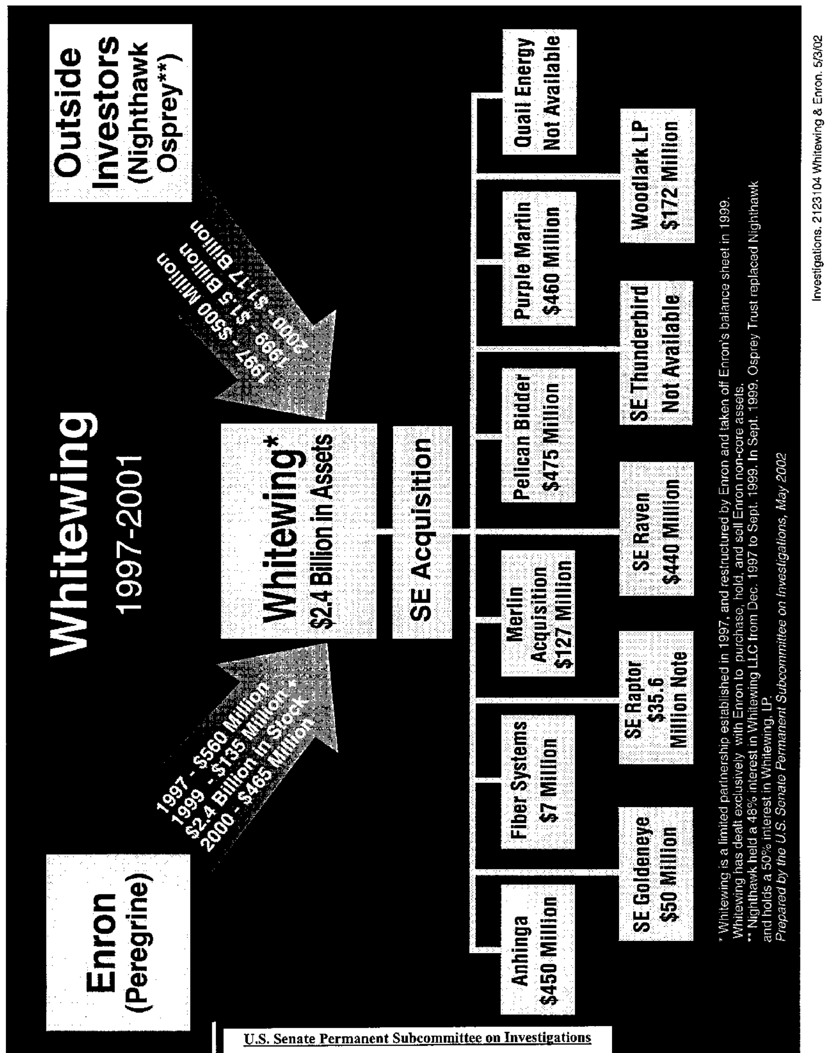
ENE issues mandatory convertible preferred stock to convert debt to equity



DJM 04875

SEP.17.1999 11:20AM ENRON CORP. NO.609 P.3/3





U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #16

EGF Execution Schedule

2000 Balance Sheet Management

Transaction	Description	Size
A. Asset Sales:		
–Whitewing Purchases	Off balance sheet vehicle to purchase assets from Enron	$ 561MM
–FAS 125's Extended	Asset sales to third parties supported by Enron total return swaps	$ 468MM
B. Vehicle Capacity Expansion:		
–Whitewing	✓Add-on to existing capacity of $250MM in Osprey Trust 144A in the amount of $700MM less $561MM of acquisitions above	$ 389MM
–Hawaii	✓Add-on to existing $400MM FAS 125 line in the amount of $150MM less assumption of $308MM of the $468MM extensions above	$ 242MM
–LJM2	✓Additional $300MM to be available for third-party asset sales	$ 300MM
		$1,960MM

Glisan · Raptor I up & running almost full, Raptor II available late in the year
Whitewing still has 1B of value, will probably want to put another
vehicle in place before 2001. New vehicle - resolution
Approval to recommend to Board. Blake, Meyer

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ENRON

Finance Committee Meeting

EC 000025209

U.S. Senate Permanent Subcommittee on Investigations
(Source: August 2000, Finance Committee Presentation.)
EXHIBIT #17

References to LJM Controls and Waivers in Enron Board/Committee Presentations[1]

Date	Document	Description
06/28/99	Special Meeting of the Board of Directors minutes and presentation	Mr. Fastow presents LJM1 as a vehicle to hedge Rhythms. Mr. Fastow will serve as General Partner of LJM, and the partnership may purchase additional Enron assets from merchant portfolio. Accompanying presentation includes description of Fastow compensation (fee of $500,000 + 2% of LP invested capital). Board approves transaction and ratifies decision by the Office of the Chairman for Fastow Code of Conduct waiver.
10/11/99	Finance Committee meeting minutes and presentation	Mr. Fastow gives presentation on LJM1. Recommends company "continue to syndicate investments to address the funds flow issue." Proposes establishment of LJM 2. Discusses his role as Managing Partner. Describes controls, including Chief Accounting and Chief Risk Officers to approve transactions and annual Audit Committee review of transactions. Cites need for Code of Conduct waiver. Finance Committee approves Fastow Code of Conduct waiver for recommendation to the full Board.
10/12/99	Board of Directors meeting minutes	Dr. Winokur discusses LJM2, describes benefits, Fastow role, controls and need for Code of Conduct waiver. Dr. Winokur recommends Board adopt waiver. Board ratifies Fastow Code of Conduct waiver for LJM2.
02/07/00	Audit Committee meeting minutes and presentation	Mr. Causey outlines the Company's transactions with LJM1 and LJM2. Mr. Causey stated that in his opinion all of the transactions had been negotiated on an arms-length basis.

[1] *Prepared by U.S. Senate Permanent Subcommittee on Investigations, May 2002*

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #18

10/06/00	Finance Committee meeting minutes and presentation	Mr. Fastow proposes establishment of LJM3. Cites need for continued asset syndication. Reviews LJM1 & 2. Discusses additional controls: (1) Fastow has continued fiduciary duty to Enron; (2) Office of Chairman or Board can ask Fastow to resign at any time; (3) Causey/Buy/Skilling approve all Enron-LJM transactions; (4) annual Audit Committee review of transactions; (5) a review of Fastow economic interest in Enron and LJM presented to Skilling; and (6) no obligation for Enron to transact with LJM. Mr. Fastow cites need for Code of Conduct waiver. Finance Committee approves Fastow Code of Conduct waiver for recommendation to the full Board. Mr. Blake proposes that Finance Committee review LJM transactions quarterly and Committee adopts. Dr. Winokur proposes that Compensation Committee review Dr. Fastow compensation and Committee adopts.
10/07/00	Board of Directors meeting minutes	Dr. Winokur discusses LJM3. Recommends Board ratification of Code of Conduct waiver for Mr. Fastow. Board ratifies Fastow Code of Conduct waiver for LJM3.

02/12/01	Audit Committee meeting minutes and presentation	Mr. Causey makes presentation on 2000 LJM transactions. Reviewed Board controls and discussed company established procedures including: (1) LJM deal approval sheet (DASH) for every LJM transaction; and (2) LJM approval process checklist. Mr. Causey also presented supplemental efforts established by the company including: (1) LJM senior professionals do not ever negotiate on behalf of Enron; (2) Enron employees negotiating for Enron do not report to Fastow; (3) Global Finance, Commercial, Legal, and Accounting monitor compliance with controls and update Messrs. Causey and Buy; and (4) internal and outside counsel consulted regarding disclosure obligations. Mr. Causey gave brief presentation of each LJM transaction. Presentation states that as part of the DASH, there is to be a "review of transaction by Enron's OTC, Chief Accounting and Risk Officers."
02/12/01	Finance Committee meeting minutes and presentation	Mr. Fastow discusses company's use of LJM vehicles. Mr. Causey characterizes specific transactions by purpose: balance sheet, hedges, income statement, and other. Mr. Causey reviews company policies and procedures as they relate to LJM transactions. Mr. Causey says company implemented supplemental efforts (described above in 2/7/01 Audit Committee presentation) to compliment Board established guidelines. Mr. Causey says process was working effectively.

Project LJM
Board Presentation

June 28, 1999

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #19

Economics of ENE Stock Positions*

- UBS forwards: 7.8 million shares @ $45 = $234 million
- Nighthawk: 25 million shares @ $40 = $875 million
- JEDI: 6 million shares @ $67 = $48 million

* *Assuming an Enron Corp. stock price of $75/share.*

Current ENE Stock Positions of Little Value to Enron

- Equity transaction below the line.
- Book up of equity does not increase debt capacity; Enron is funds flow constrained.
- Debt to buy back shares would hurt Enron's credit profile / rating.
- Sale of shares would depress stock price.
- Best scenario: Net settle option increases EPS approximately $0.015.

Transaction Summary

- Establish non-Enron investment partnership ("LJM") with outside equity.

- Transfer in-the-money value of forward contract into LJM.

- LJM:

  (1) Pays Enron $50 million (cash);
  (2) Enters into a swap (or put) with Enron valued at $90 million to hedge Rhythms NetConnections position at no cost to Enron;
  (3) Negotiates with Enron for purchase of additional merchant assets.

- A. Fastow involvement:

  (1) Serves as G.P. of LJM;
  (2) Has no direct pecuniary interest, either current or future, in the Enron stock.

Direct Value to Enron

Value	Amount	Comments
Cash Payment	$ 50 million	Cash; counts as funds flow
Rhythms NetConnections put	$ 90 million	
	$140 million	
Excess value to protect swap	$ 25 million	Additional credit protection to ENE in downside Rhythms scenario
	$165 million	

Benefits to Enron

- Enron receives a $50 million cash payment and a Rhythms NetConnections put valued at $90 million
- Immediately shifts MTM risk in merchant equity portfolio
- Credit ratings positive
  - Liquidity of merchant portfolio
- Keeps large block of stock closely held and restricted
- Insures against new consolidation rules
- Future Investment Management Company?
- Capture Cuiaba / Elektro value?

A. Fastow Involvement

General Partner Interest

- General Partner commits $1 million.
- **General Partner will not receive any current or future (appreciated) value of ENE stock.**
- Distribution formula:

  (1) 100% of proceeds from the Enron stock to the LP's;
  (2) 100% of proceeds from all other assets to GP until return of and a 25% IRR on Invested Capital*;
  (3) 50% to the Partners (including the GP) in proportion to their capital commitments and 50% to the GP.

Fees to Management Company

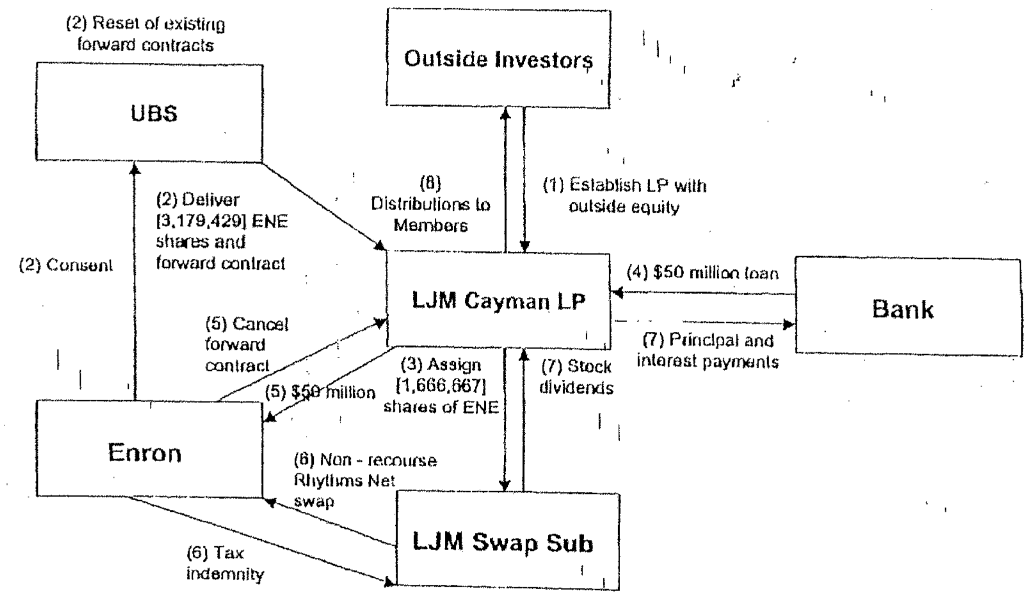
- Fee of $500,000 + 2.0% of Limited Partners' Invested Capital*

*For any Partner, "Invested Capital" represents the sum of such Partner's capital commitment plus such Partner's percentage interest (based on capital commitments) of the fair value of the Partnership's investment portfolio (other than the ENE stock).

Key Elements of Transaction to be Approved

	Approval Required
1. Waiver of Code of Conduct.	Chairman & CEO, President & COO
2. Enter into Rhythms NetConnections swap or put with LJM Swap Sub.	President & COO or CAO
3. Approve transaction: (a) Reset strike price on UBS forward contract. (b) Consent to assignment of forward contract. (c) Cancellation of LJM Cayman, L.P. forward contract. (d) Tax indemnification. (e) Section 16 indemnification.	Full Board

Transaction Structure



June 28, 1999

Steps 5 and 6 occur simultaneously.

Appendix p. 1

Steps to Complete the Transaction

- Step (1) : Establish LJM Cayman, L.P. with outside equity.
- Step (2) : Reset of current forward contracts with UBS. Assign ENE shares and forward contract from UBS to LJM Cayman, L.P. with Enron's consent.
- Step (3) : Assignment of [1,666,667] shares of ENE stock to LJM Swap Sub.
- Step (4) : LJM Cayman, L.P. enters into a loan agreement with a bank for $50 million.
- Step (5) : Cancellation of forward contract between Enron and LJM Cayman, L.P. Enron receives a $50 million payment.

  Steps 5 and 6 occur simultaneously.
- Step (6) : LJM Swap Sub enters into a non-recourse put agreement on the Rythms Netconnections stock with Enron. In return, LJM Cayman, L.P. receives a tax indemnity.
- Step (7) : ENE dividends will flow from LJM Swap Sub to LJM Cayman, L.P. LJM Cayman, L.P. makes principal and interest payments on loan to bank.
- Step (8) : Distributions to Members.

LJM 2 Summary

LP will be traditional pension funds

- Follow-on private equity fund to LJM1 Bring quick flexible equity

- Purpose: Alternative, optional source of private equity for Enron to manage its investment portfolio risk, funds flow, and financial flexibility

- Major differences from LJM1:
  - No forward contracts / value from Enron contributed
  - No business relationships between Enron and LJM2 at close
  - Size: target $200+ million institutional private equity
  - GP investment: 1% of committed capital

- Controls
  - R. Causey to approve all transactions between Enron and LJM1/LJM2

- Compensation / Disclosure
  - No compensation from Enron to A. Fastow
  - LJM2 has typical private equity fund fees and promote
  - No related party disclosure expected at close. Related party disclosures specific to asset sales probably required.

- Finance Committee / Board of Directors action requested
  - Ratify decision of Office of the Chairman to waive Code of Conduct in order to allow A. Fastow participation in LJM2 as General Partner

Blake - Has AA reviewed Causey. yes, they're fine w/ it.
Blake - Still concerned about conflict of interest. Causey - Gave LP enough authority to keep Andy from having too much power. LP can remove GP w/out cause.

ENRON

Finance Committee Meeting

RCO 17455

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U.S. Senate Permanent Subcommittee on Investigations
(Source: October 11-12, 1999, Finance Committee Presentation.)
EXHIBIT #20

CONFIDENTIAL

PRIVATE PLACEMENT MEMORANDUM

LJM2 CO-INVESTMENT, L.P.

CONFIDENTIAL TREATMENT REQUESTED
By Dechert on behalf of its client

U.S. Senate Permanent Subcommittee on Investigations
(Source: October 1999, LJM2 Co-Investment, LP Private Placement Memo.)
EXHIBIT #21

Merrill Lynch & Co.

DP 162281

I. EXECUTIVE SUMMARY

Introduction

LJM2 Co-Investment, L.P., a Delaware limited partnership ("LJM2" or the "Partnership"), is being organized by Andrew S. Fastow, Executive Vice President and Chief Financial Officer of Enron Corp., an Oregon corporation ("Enron"), to make privately negotiated equity and equity-related investments in energy- and communications-related businesses and assets. The Partnership expects that Enron will be the Partnership's primary source of investment opportunities and that the Partnership will (i) co-invest with Enron or its subsidiaries in new investments in, or acquisitions of, businesses and assets, and (ii) make investments in, or acquire an investment interest from Enron or its subsidiaries relating to, existing assets or businesses owned by Enron or its subsidiaries. It is expected that in connection with the foregoing investments, Enron will retain a significant economic or operating interest in the businesses or assets in which the Partnership invests. The Partnership may also from time to time make investments in businesses or assets where Enron has no involvement. This is the second such fund formed by Mr. Fastow targeted at investing primarily in companies owned or controlled by Enron. The Partnership's objective is to generate an annualized internal rate of return ("IRR") in excess of 30% to investors in the Partnership after payment of all Partnership fees and expenses and payment of the carried interest to the General Partner.

Enron, headquartered in Houston, Texas, is one of the largest sellers of natural gas and electricity in deregulated and privatized markets on three continents. Additionally, Enron is the largest provider of energy risk management services in the world and owns the largest natural gas pipeline system in the U.S. Enron is also constructing a 10,000 mile nationwide fiber-optic telecommunications network. Enron is frequently characterized as the agent of change in the rapidly deregulating and privatizing energy markets and has been named the "Most Innovative Company in the World" for four consecutive years by *Fortune*. Enron currently ranks among the Fortune 100 companies with annual revenues of over $30 billion. Importantly, Enron has made investments of over $7 billion in each of the last two years in a variety of energy-related businesses and currently owns merchant investments of over $10 billion. *See* "Overview of Enron." 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. This access to deal flow should provide the Partnership with unusually attractive investment opportunities.

The target size of the Partnership is $200 million. The General Partner reserves the right to accept additional commitments in excess of $200 million. The Partnership is expected to generate significant co-investment opportunities for investors in the Partnership because the Partnership will be limited to investing no more than 10% of its committed capital in any one company, and the General Partner expects many of the opportunities the Partnership pursues to require capital in excess of the amount the Partnership is able to provide under this diversification limitation. Co-investment amounts will not be subject to a carried interest.

The General Partner of the Partnership will be LJM2 Capital Partners, LLC, a Delaware limited liability company (the "General Partner"), an entity owned and controlled by one or more of the Principals (as defined below). 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: Andrew S. Fastow, Michael J. Kopper, and Ben Glisan, Jr. (collectively, the "Principals"). The Principals will continue their current responsibilities with Enron while managing the day-to-day operations of the Partnership. *See* – "Risk Factors – Dependence on Key Personnel" and "Conflicts of Interest – Dual Role of Principals."

Investment Opportunity

The Principals believe that LJM2 provides investors with an unusually attractive investment opportunity for the following reasons:

Access to Significant Proprietary Deal Flow. Enron has extensive deal origination capability that is derived from approximately 2,000 fully dedicated Enron-employed origination and monitoring professionals located around the world. The deal flow emanating from this origination infrastructure has resulted in Enron making over $7 billion of energy-related investments in each of the last two years and holding merchant investments of over $10 billion. As a result of Enron's in-house deal sourcing capability as well as its leading market position in most businesses in which it operates, Enron frequently has access to investment opportunities that are not available to other investors. The Partnership expects to benefit from having the opportunity to invest in Enron-generated investment opportunities that would not be available otherwise to outside investors.

Enron's Investment Record. Enron's record as a successful investor is reflected in returns it has generated for its shareholders as measured by the appreciation in its common stock, which, from January 1, 1990, through September 30, 1999, has increased 641% (price increase plus assumed re-investment of dividends), as compared to returns of 363% for the S&P 500 and 141% for the S&P Energy Index for the same period. Furthermore, Enron has successfully managed two institutionally funded private equity partnerships, Joint Energy Development Investments Limited Partnership ("JEDI I") and Joint Energy Development Investments II Limited Partnership ("JEDI II"), which have generated (or are estimated to generate, as the case may be) an IRR after payment of fees and expenses of the partnership and payment of a carried interest, if any, to the partnerships' general partners (each, a "Net IRR") of 23% and 194%, respectively, compared to targeted IRRs for the partnerships on invested capital before fees, expenses, and carried interest (a "Gross IRR") of 15% and 20%, respectively. The General Partner believes that a significant portion of this superior performance can be attributed to the quality of investment opportunities sourced by Enron. *See* – "Summary of Investment Experience."

Enron's Capabilities to Analyze and Structure Investments and Operate Assets. Over the years, Enron has developed a rigorous process of investment analysis, which employs approximately 130 professionals in varying disciplines such as engineering, research, credit, tax, legal, accounting, insurance, and risk analysis. As LJM2 expects that it primarily will be investing in assets in which Enron has an interest, it should benefit from Enron's expertise in all areas relating to the investment in and management of energy and communications assets, including the physical and financial risk management of energy assets and extensive operating capabilities in all aspects of the energy industry and certain aspects of the communications industry.

The Ability to Evaluate Investments with Full Knowledge of the Assets. Due to their active involvement in the investment activities of Enron, the Principals will be in an advantageous position to analyze potential investments for LJM2. The Principals, as senior financial officers of Enron, will typically be familiar with the investment opportunities LJM2 considers. The Principals believe that their access to Enron's information pertaining to potential investments will contribute to superior returns.

Speed and Knowledge Advantage of LJM2. LJM2 will be positioned to capitalize on Enron's need to rapidly access outside capital due to the Principals' familiarity with Enron's assets and their understanding of Enron's objectives, which should facilitate LJM2's ability to quickly execute transactions. This ability to act quickly is invaluable to Enron and should enhance the flow of opportunities for LJM2.

Investment and Financial Expertise of Principals. The Principals are a group of highly talented financial professionals with extensive experience originating and structuring complex transactions. This experience has given the Principals the ability to create innovative financial structures around investments, which should enhance returns to investors in LJM2. The Principals have been involved in managing JEDI I and JEDI II.

The Principals

The day-to-day activities of the Partnership will be managed by Messrs. Fastow, Kopper, and Glisan. Each of the Principals has spent a significant portion of his professional career in energy and communications investing, structured finance, and risk management (including substantial involvement in the organization, operation, and investment management of each of JEDI I and JEDI II), and, as a team, the Principals possess specific expertise necessary to maximize the Partnership's performance.

Andrew S. Fastow, Executive Vice President and Chief Financial Officer of Enron, has been the Chief Financial Officer of Enron since 1997; prior to that, he was a Managing Director and principal financial officer for Enron Capital & Trade Resources Corp. ("ECT"), Enron's principal merchant and investing subsidiary. In these capacities, he has been involved in structuring and managing many of Enron's investments. Mr. Fastow has been with Enron for nine years. Michael J. Kopper, Managing Director in Enron's Global Equity Markets Group, is responsible for Enron's Global Equity and Structured Finance businesses. He has been with Enron for five years. Ben Glisan, Jr., Vice President in Enron's Global Equity Markets Group, is primarily responsible for Enron's structured finance activity. Mr. Glisan has been with Enron for three years. Summary biographies of the Principals are included elsewhere in this Memorandum. *See* – "Management of the Partnership – Biographies of the Principals."

The Principals will remain employees of Enron and will devote such of their business time and attention as they deem reasonably necessary to manage the affairs of the Partnership, subject to their obligation to devote their business time and attention primarily to the discharge of their responsibilities as senior financial officers of Enron. The Partnership should also benefit indirectly from time spent by the Principals in evaluating and structuring investments for Enron, as many of these investments may become candidates for investment by the Partnership.

Jaedicke - Audit Committee will review & determine that transactions ... arms length transactions

LJM Investment Activity
1999

Vehicle	Investment	Description	Amount (millions)
LJM	RhythmsNet Stock Options	Hedge of RhythmsNet investment for ENE	$104
LJMII	Nowa Saryzna (Poland)	Sale of interest in power plant	$ 30
LJMII	ENA CLO-Equity	Sale of equity in securitization vehicle for ENA merchant assets	$ 20
LJMII	ENA CLO-BB Notes	Structured notes related to assets included in equity above	$ 13
LJMII	Bob West Treasure, L.C.C. (EEX)	Natural gas prepay	$ 3
LJMII	MEGS, L.L.C. (Pluto)	Sale of equity in offshore gathering system	$ 26
LJMII	Yosemite	Equity in vehicle used to finance ENE natural gas prepays	$ 34
LJMII	Resco	Sale of equity in EES residential business	$ 1

Causey - All transactions negotiated

U.S. Senate Permanent Subcommittee on Investigations
(Source: February 7, 2000, Audit Committee Presentation.)
EXHIBIT #22

EC 000051643

LJM2 Update

- $386 million of capital commitments
- 33 investors including pension funds, insurance companies, banks, private funds, individuals
- 7 investments to date 5 different business units
  - $139 million
  - All purchased from Enron
  - Projected IRR of investments = 17.95% - not leveraged
  - 5 different business units

Provide capital very quickly b/c of prior knowledge of the transactions

Direct and indirect LJM impact (including LJM1)

- Earnings = $229.5 million
- Funds flow = $2,077.4 million
- Fee savings = $2.3 million
- LJM2 provided marketing "backstop" on 3 occasions
- Q4 1999: 8 days/6 deals/$125 million

Andy discussed his time commitment Approx. 3 hrs a week spent

20

ENRON®
Finance Committee Meeting
04/00

Andy discussed the LJM vehicles and utilized benefits to Enron

Enron Corp

Review of LJM procedures and transactions completed in 2000

February 12, 2001

2D-1

U.S. Senate Permanent Subcommittee on Investigations
(Source: February 12, 2001, Audit and Finance Committee Presentation.)
EXHIBIT #24a

EC 000024694

LJM INVESTMENT 2000 ACTIVITY WITH ENRON

Investment	Description	Notional Amount ($Millions)
A. Balance Sheet		
Resco The New Power Company	Purchase of equity investment in EES' residential energy services.	.67 (private) 38 (public)'
Yosemite	Purchase of an interest in certain Trust Investments supported by Enron credit; such interest subsequently sold to Whitewing, an Enron nonconsolidated affiliate.	33.75
EE&CC Turbines	Acquired rights from Enron to purchase two turbines from GE with option to sell such turbines to EE&CC.	38
Margaux	Purchase of equity certificates in a monetization structure for three European power plants.	10
Rawhide	Purchase of equity certificates in a monetization structure for certain domestic and international assets.	12.5
Avici	Purchase of equity certificates in a monetization structure for Enron's interest in Avici shares.	1
Catalytica	Purchase of equity certificates in a monetization structure for Enron's interest in Catalytica shares.	1.8
Pulp and Paper	Serves as general partner in a limited partnership interest that purchased an interest in Enron's Pulp and Paper trading business.	8

Similar transactions

EC 000024695

Investment	Description	Notional Amount Millions)
B. Hedges		
RhythmsNet Stock options	Termination of hedge of RhythmsNet investment.	~~26.8~~ 15
Raptors I, II, III, IV	Purchase of equity interests in four structured-finance hedging vehicles.	127.1
C. Income Statement		
Dark Fiber	Purchase of Dark Fiber.	30
D. Other		
Osprey Add-On	Purchase of additional Trust Certificates in Osprey – an unaffiliated equity and debtholder of Whitewing, an Enron nonconsolidated affiliate, which invests in both domestic and foreign merchant and other assets.	32.5

RELATED PARTY TRANSACTIONS – LJM 2000
INTERNAL POLICIES AND PROCEDURES
(February 2001)

Causey noted [illegible] it was discussed at Audit Committee

1. Background: Board-established guidelines for transacting with LJM.

- No obligations vis-à-vis one another;
- Chief Accounting and Risk Officers review and, where appropriate, approval;
- Annual review by Board's Audit and Compliance Committee of completed transactions; recommendations, as appropriate; and
- Annual Board review as to application of Company's Code of Ethics, i.e. such transactions "do not adversely affect the best interests of the Company".

Process working effectively

2. Compliance: The Company has adopted the following procedures and controls in response to the Board's direction.

- LJM Deal Approval Sheet ("DASH") prepared for every Enron/LJM transaction generally describing the nature of the Commercial transaction and relevant economics; approval required by a variety of senior-level Commercial, Technical, and Commercial Support professionals.
- DASH is supplemented by an "LJM Approval Process Checklist" testing for compliance with Board's directive for transacting with LJM, including questions addressing the following:
  - -- Alternative sales options and counterparties;
  - -- Determination that transaction was conducted at arm's-length; any evidence that it was not;
  - -- Disclosure obligations; and
  - -- Review of transaction by Enron's OTC, Chief Accounting and Risk Officers.

3. Supplemental Efforts: Checklist review complemented by the adoption of additional controls.

- LJM senior professionals do not ever negotiate on behalf of Enron;
- Enron professionals negotiating with LJM report to senior Enron professionals apart from Andrew Fastow;
- Global Finance Commercial, Legal, and Accounting monitor compliance with procedures and controls; regularly update Chief Accounting and Risk Officers; and
- Internal and outside counsel regularly consulted regarding disclosure obligations and review any such disclosures.

EC 000024697

OCT 21 2001 2:26 PM FR ENRON CORP. 713 853 3920 TO 917183953198 P.03

(A) Board Requested John Duncan and [illegible] to inquire of Fastow Re outside income –
(B) Questions prepared by Jim Derrick for questioning Andy Fastow

Andy, because of the current controversy surrounding LJM I and LJM II, we believe it would be helpful for the Board to have a general understanding of the amount of your investment and of your return on investment in the LJM entities. We understand that a detailed accounting of these matters will soon be done in connection with the response to the SEC inquiry. We very much appreciate your willingness to visit with us.

In responding to our questions with respect to your interest in the LJM entities, we would appreciate your including any interest, direct or indirect, that the members of your family may have had in the entities.

Reaborn – Fastow income "about" LJM I = 23m LJM II = 22m

[redacted]

1. What was your aggregate income attributable to LJM I and LJM II, inclusive of salary, consulting fees, management fees, partnership distributions, and gain on the sale of your partnership interests?

Mickey To ask

\# Fastow commit'd: LJM I 1.0m LJM II 3.9m

2. What was your aggregate investment in LJM I and LJM II? What was the aggregate amount invested in LJM I and LJM II by the other participants? What was your return on investment? Did you have a promote? If you did, what was it? How does your rate of return on investment compare to that of the other participants in LJM I and LJM II? no answer

others: LJM I 15… LJM II 39… m

Total (Both) 58.9m

incredible! note to myself: J. Duncan does anyone know what Fastow's contract c LJM provided; Mickey never brought to ENE Board or To The Comp. Com. –

3. Other than you and Michael Kopper, did any current former employees, officers, or directors of any Enron entity or any of their family members have any economic interest in or derive any benefit from LJM I or LJM II? "No"

4. We assume that in the course of the SEC inquiry and the litigation that has been filed, LJM and its relationship with Enron will be fully scrutinized. Do you know of any

J Duncan

OCT 21 2001 2:27 PM FR ENRON CORP. 713 853 3920 TO 917183953198 P.04

potentially troublesome matter of which we should now be apprised in connection with the LJM relationship? "No"

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #24b

LJM
INVESTMENTS

Annual Partnership Meeting

October 26, 2000

U.S. Senate Permanent Subcommittee on Investigations
(Source: October 26, 2000, LJM Investments Partnership Meeting Presentation.)
EXHIBIT #25

LJM Investments

Introduction: Meeting Agenda

- Introduction
- LJM Rationale
- LJM Strategy
- Activity Summary
- Valuation
- Sample Investments
- Other Issues
- Summary
- Guest Speakers: Jeff Skilling, Enron
  Gene Lockhart, The New Power Company
  Bill Jacobs, The New Power Company
  Will Byers, The New Power Company

LJM Investments

Introduction: Meeting Attendees

1.) LJM Investments
- Andrew Fastow
- Michael Kopper
- Kathy Lynn
- Michael Hinds
- Anne Yaeger
- Joyce Tang
- Chris Loehr
- Ace Roman

2.) LJM Consultants

<u>Kirkland & Ellis</u>
- Michael Edsall
- Martha Stuart

<u>Price Waterhouse Coopers</u>
- Ian Schachter

3.) LJM2 Limited Partners
- Chase Capital
- World Air Lease
- GE Capital
- J.P. Morgan Capital
- Merrill Lynch
- C&I Partners
- Dresdner
- AON
- Rho Management
- CSFB
- Ulysses Partners
- Fort Wash. Private Equity
- Morgan Stanley
- First Union Investors

4.) Guests

<u>Enron</u>
- Jeff Skilling

<u>TNPC</u>
- Gene Lockhart
- Bill Jacobs
- Will Byers

LJM Investments

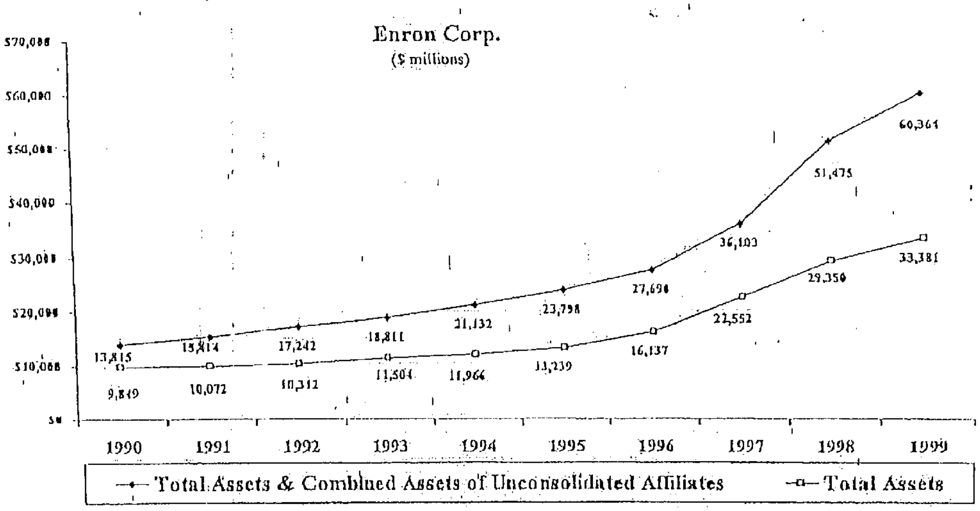
LJM Rationale: Why does Enron need private equity?

- Energy and communications assets typically do not generate earnings or cash flow within the first 1-3 years
  - Investments are dilutive to Enron's current EPS
  - Investments are dilutive to credit rating ratios
- Solutions
  - Enron must deconsolidate assets
  - Enron must create structures which accelerate projected earnings and cash flows

➢ This leads to opportunities for LJM

LJM Investments

LJM Rationale: Why does Enron need private equity?



LJM2 Co-Investment, L.P.

Activity Summary: Overview

- 23 investments have been made
- $511 million committed to investments / $438 million invested
- 6 investments liquidated on schedule at target returns ($108 million)
- 5 investments partially realized ($123 million)
- $245 million of Partners' capital has been funded
- $135 million of debt used for investments
- Projected Net Limited Partner IRR* – 69% Cash multiple – 2.3X

*See Valuation: Key model assumptions slide

LJM2 Co-Investment, L.P.

Activity Summary: Investments

Asset	Investment Date	Amount Invested	Asset Outlook (+/B/-)	Cash Received to Date	Current IRR	Projected Cash Multiple	Current Projected IRR
Unrealized Investments							
Subordinated Debt							
ENA CLO Trust I - Debt	22-Dec-99	19,600,000	0		-100%	1.85	14%
Total Debt		19,600,000					
Equity							
Backbone	30-Jun-00	29,990,763	0		-100%	1.18	18%
ENA CLO Trust I - Equity	22-Dec-99	12,900,000	0		-100%	3.10	32%
First Union CLO	29-Sep-00	25,200,000	0		-100%	2.42	24%
Margaux	12-Jul-00	10,000,000	0		-100%	1.84	16%
Osprey	12-Jul-00	26,000,000	0		-100%	1.53	20%
Osprey 2	11-Sep-00	6,500,000	0		-100%	3.10	75%
Raptor I-A	19-Sep-00	6,000,000	0		-100%	1.42	12.5%
Raptor II-A	13-Oct-00	1,100,000	0		-100%	1.41	12.5%
Raptor IV	21-Sep-00	30,000,000	0		-100%	2.37	125%
Resco	6-Jan-00	673,200	0		-100%	1.32	25%
TNPC	12-Jul-00	38,000,000	0		-100%	1.89	133%
Zenith	8-Aug-00	21,000,000	0		-100%	1.85	21%
Total Equity		207,363,963					
Total Unrealized Investments		226,963,963					
Partially Realized Investments							
GE 7EA Turbines	12-May-00	8,226,975	0	846,378	-100%	1.09	40%
Raptor	4-May-00	29,500,000	0	40,366,667	156%	2.37	193%
Raptor II	6-Jul-00	30,000,000	0	41,050,000	248%	2.37	278%
Raptor III	28-Sep-00	30,000,000	0	39,550,000	2500%	2.32	2500%
Rawhide	28-Mar-00	12,500,000	0	830,730	-100%	1.52	18%
Total Partially Realized Investments		110,226,975		122,643,775			
Realized Investments							
Bargeco	29-Jun-00	7,525,000		8,235,000	30%	1.09	
Bob West Treasure	29-Dec-99	2,953,125	n/a	3,246,649	21%	1.10	
Coyote Springs	7-Jul-00	-	n/a	3,557,000	-	-	
Pluto	29-Dec-99	26,313,610	n/a	26,794,115	8%	1.02	
Poland	22-Dec-99	30,000,000	n/a	32,641,500	41%	1.09	
Yosemite****	28-Feb-00	33,750,000	n/a	33,850,000	194%	1.003	
Total Realized		100,541,735		108,324,264			
Total Invested		437,732,673					
Total Portfolio IRR		51%					

LJM INVESTMENTS

Confidential

Code of Ethics

July, 2000

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #26

INTEROFFICE MEMORANDUM

To: All Employees

From: Ken KL

Subject: Code of Ethics

Department: Office of the Chairman

Date: July 1, 2000

As officers and employees of Enron Corp., its subsidiaries, and its affiliated companies ("Enron" or collectively the "Company"), we are responsible for conducting the business affairs of the Company in accordance with all applicable laws and in a moral and honest manner.

To make certain that we understand what is expected of us, Enron has adopted certain policies, with the approval of the Board of Directors, all of which are set forth in the enclosed booklet revised July 2000. *Please note that Enron has added the Principles of Human Rights; provided further description of our Business Ethics policy with respect to our legal contracts, the selection of outside counsel, and the making of disparaging remarks, oral or written, about Enron by employees; provided further clarification of Enron's policy with respect to Confidential Information and Trade Secrets; decreased the number of days passwords are valid under Enron's Communication Services and Equipment Policy, provided additional information with respect to the criminal penalties and civil fines assessed by the US government under the Foreign Corrupt Practices Act; and clarified Enron's policy with respect to Conflicts of Interests, Investments, and Outside Business Interests of Employees.*

The Code of Ethics contains commonsense rules of conduct with which the great majority of Enron employees routinely conform. However, I ask that you read them carefully and completely and that, as you do, you reflect on your past actions to make certain that you have complied with the policies. It is absolutely essential that you fully comply with these policies in the future. If you have any questions, talk them over with your supervisor, manager, or Enron legal counsel.

Enclosed with this memorandum and booklet is a Certificate of Compliance (revised 7/00) to be signed by you as a statement of your personal agreement, since you last so certified, to comply with the policies stated herein during the term of your employment with the Company. **Please carefully review this booklet. Then select the Code of Ethics option from *eHRonline.enron.com* to certify your compliance or you may sign and send this form to Elaine V. Overturf, Deputy Corporate Secretary, Enron Corp., 1400 Smith Street, Suite 4836, Houston, Texas 77002-7369.**

This memorandum, the Code of Ethics booklet, and Certificate of Compliance are also available to all employees on the Enron Home Page at *http://home.enron.com/*. **You may access them by clicking on Code of Ethics.**

For your convenience, I have briefly stated below each of the Policies in the booklet. Please retain this booklet for future reference.

Principles of Human Rights

As a partner in the communities in which we operate, Enron believes it has a responsibility to conduct itself according to certain basic tenets of human behavior that transcend industries, cultures, economics, and local, regional and national boundaries.

And because we take this responsibility as an international employer and global corporate citizen seriously, we have developed the following principles on human rights.

Enron's Vision and Values are the platform upon which our human rights principles are built.

Vision
Enron's vision is to become the world's leading energy company - creating innovative and efficient energy solutions for growing economies and a better environment worldwide.

Values
Respect
We treat others as we would like to be treated ourselves. We do not tolerate abusive or disrespectful treatment. Ruthlessness, callousness and arrogance don't belong here.

Integrity
We work with customers and prospects openly, honestly and sincerely. When we say we will do something, we will do it; when we say we cannot or will not do something, then we won't do it.

Communication
We have an obligation to communicate. Here, we take the time to talk with one another ... and to listen. We believe that information is meant to move and that information moves people.

Excellence
We are satisfied with nothing less than the very best in everything we do. We will continue to raise the bar for everyone. The great fun here will be for all of us to discover just how good we can really be.

Principles of Human Rights

- Enron stands on the foundation of its Vision and Values. Every employee is educated about the Company's Vision and Values and is expected to conduct business with other employees, partners, contractors, suppliers, vendors and customers keeping in mind respect, integrity, communication and excellence. Everything we do evolves from Enron's Vision and Values statements.
- At Enron, we treat others as we expect to be treated ourselves. We believe in respect for the rights of all individuals and are committed to promoting an environment characterized by dignity and mutual respect for employees, customers, contractors, suppliers, partners, community members and representatives of all levels of Government.
- We do not and will not tolerate human rights abuses of any kind by our employees or contractors.
- We believe in treating all employees fairly, regardless of gender, race, color, language, religion, age, ethnic background, political or other opinion, national origin, or physical limitation.
- We are dedicated to conducting business according to all applicable local and international laws and regulations, including, but not limited to, the U.S. Foreign Corrupt Practices Act, and with the highest professional and ethical standards.
- We are committed to operating safely and conducting business worldwide in compliance with all applicable environmental, health, and safety laws and regulations and strive to improve the lives of the people in the regions in which we operate. These laws, regulations, and standards are designed to safeguard the environment, human health, wildlife, and natural resources. Our commitment to observe them faithfully is an integral part of our business and of our values.
- We believe that playing an active role in every community in which we operate fosters a long-term partnership with the people with whom we come into daily contact. Strengthening the communities

Business Ethics

Employees of Enron Corp., its subsidiaries, and its affiliated companies (collectively the "Company") are charged with conducting their business affairs in accordance with the highest ethical standards. An employee shall not conduct himself or herself in a manner which directly or indirectly would be detrimental to the best interests of the Company or in a manner which would bring to the employee financial gain separately derived as a direct consequence of his or her employment with the Company. Moral as well as legal obligations will be fulfilled openly, promptly, and in a manner which will reflect pride on the Company's name.

Products and services of the Company will be of the highest quality and as represented. Advertising and promotion will be truthful, not exaggerated or misleading.

Agreements, whether contractual or verbal, will be honored. No bribes, bonuses, kickbacks, lavish entertainment, or gifts will be given or received in exchange for special position, price, or privilege.

Employees will maintain the confidentiality of the Company's sensitive or proprietary information and will not use such information for their personal benefit.

Employees shall refrain, both during and after their employment, from publishing any oral or written statements about the Company or any of its' officers, employees, agents, or representatives that are slanderous, libelous, or defamatory; or that disclose private or confidential information about their business affairs; or that constitute an intrusion into their seclusion or private lives; or that give rise to unreasonable publicity about their private lives; or that place them in a false light before the public; or that constitute a misappropriation of their name or likeness.

Relations with the Company's many publics – customers, stockholders, governments, employees, suppliers, press, and bankers – will be conducted in honesty, candor, and fairness.

It is Enron's policy that each "contract" must be reviewed by one of our attorneys prior to its being submitted to the other parties to such "contract" and that it must be initialed by one of our attorneys prior to being signed. By "contract" we mean each contract, agreement, bid, term sheet, letter of intent, memorandum of understanding, amendment, modification, supplement, fax telex, and other document or arrangement that could reasonably be expected to impose an obligation on any Enron entity. (Certain Enron entities utilize standard forms that have been pre-approved by the legal department to conduct routine activities; so long as no material changes are made to these pre-approved forms, it is not necessary to seek legal review or initialing prior to their being signed.) Please Bear in mind that your conduct and/or your conversations may have, under certain circumstances, the unintended effect of creating an enforceable obligation; Consult with the legal department with respect to any questions you may have in this regard.

Additionally, it is Enron's policy that the selection and retention of outside legal counsel be conducted exclusively by the legal department. (Within the legal department, the selection and retention of counsel is coordinated and approved by James V. Derrick Jr., Enron's Executive Vice President and General Counsel.) In the absence of this policy, it would not be possible for our legal department to discharge its obligation to manage properly our relationships with outside counsel.

Employees will comply with the executive stock ownership requirements set forth by the Board of Directors of Enron Corp., if applicable.

Laws and regulations affecting the Company will be obeyed. Even though the laws and business practices of foreign nations may differ from those in effect in the United States, the applicability of both foreign and U.S. laws to the Company's operations will be strictly observed. Illegal behavior on the part of any employee in the performance of Company duties will neither be condoned nor tolerated.

Conflicts of Interests, Investments, and Outside Business Interests of Officers and Employees

Employees of the Company have inquired from time to time as to the propriety of their association with, or the investment of their personal funds in, business enterprises similar in character to certain activities of the Company. In response, the Company has established certain principles for the guidance of officers and employees with respect to personal business and investment interests.

The primary consideration of each full-time (regular as well as temporary) officer and employee should be the fact that the employer is entitled to expect of such person complete loyalty to the best interests of the Company and the maximum application of skill, talent, education, etc., to the discharge of his or her job responsibilities, without any reservations. Therefore, it follows that no full-time officer or employee should:

(a) Engage in any outside activity or enterprise which could interfere in any way with job performance;

(b) Make investments or perform services for his or her own or related interest in any enterprise under any circumstances where, by reason of the nature of the business conducted by such enterprise, there is, or could be, a disparity or conflict of interest between the officer or employee and the Company; or

(c) Own an interest in or participate, directly or indirectly, in the profits of any other entity which does business with or is a competitor of the Company, unless such ownership or participation has been previously disclosed in writing to the Chairman of the Board and Chief Executive Officer of Enron Corp. and such officer has determined that such interest or participation does not adversely affect the best interests of the Company.

Notwithstanding any provision to the contrary in this Policy on Investments, securities of publicly owned corporations which are regularly traded on the open market may be owned without disclosure if they are not purchased as a result of confidential knowledge about the Company's operations, relations, business, or negotiations with such corporations.

If an investment of personal funds by an officer or employee in a venture or enterprise will not entail personal services or managerial attention, and if there appears to be no conflict or disparity of interest involved, the following procedure nevertheless shall be followed if all or any part of the business of the venture or enterprise is identical with, or similar or directly related to, that conducted by the Company, or if such business consists of the furnishing of goods or services of a type utilized to a material extent by the Company:

(a) The officer or employee desiring to make such investment shall submit in writing to the Chairman of the Board and Chief Executive Officer of Enron Corp. a brief summary of relevant facts; and

(b) The Chairman of the Board and Chief Executive Officer of Enron Corp. shall consider carefully the summary of relevant facts, and if he concludes that there appears to be no probability of any conflict of interest arising out of the proposed investment, the officer or employee shall be so notified and may then make the proposed investment in full reliance upon the findings of the Chairman of the Board and Chief Executive Officer of Enron Corp.

In the event the Chairman of the Board and Chief Executive Officer of Enron Corp. should desire to make such an investment, he may do so only upon approval of the majority of a quorum of the Executive Committee of the Board of Directors of Enron Corp., other than himself, at any regular or special meeting of such Committee.

Every officer and employee shall be under a continuing duty to report, in the manner set forth above, any situation where by reason of economic or other interest in an enterprise there is then present the possibility of a conflict or disparity of interest between the officer or employee and the Company. This obligation includes but is not limited to (1) any existing personal investment at the date of promulgation of this policy, (2) any existing personal investment at the time of employment of any officer or employee by the Company, and (3) any existing personal investment, whether or not previously approved, which may become in conflict with the provisions of this policy because of changes in the business of the Company or changes in the business of the outside enterprise in which investment has been made.

In the event of a finding by the Chairman of the Board and Chief Executive Officer of Enron Corp. (or by the Executive Committee of the Board of Directors of Enron Corp., if applicable) that a material conflict or disparity of interest does exist with respect to any existing personal investment of an officer or employee, then, upon being so notified, the officer or employee involved shall immediately divest himself or herself of such interest and shall notify the Chairman and Chief Executive Officer of Enron Corp. (or the Executive Committee, if applicable) in writing that he or she has done so.

THE RAPTORS

2000 – 2001

COST OF RAPTORS TO ENRON SHAREHOLDERS

Enron Payments to LJM2 for Raptors		
Guaranteed payments to LJM2		$ 162 million
Raptors Termination Fee		$ 35 million
		$ 197 million
Initial Enron Shares At Risk		
Enron Shares	4 million	$ 264 million
Enron Stock Contracts (contingent on certain Enron stock price)	18 million	$1.350 billion
Enron Warrants for TNPC Shares	24 million	$ 259 million
	46 million shares	**$1.870 billion**[1]
March 2001 Restructuring (Additional Enron Shares at Risk)		
Enron Shares	12 million	$ 738 million
Enron Shares if Original Stock Contracts Failed	18 million	$1.110 billion
	30 million shares	**$1.850 billion**

WHAT ENRON SHAREHOLDERS WERE TOLD

Raptors' Inflation of Enron Earnings[2]	
Enron's Earnings with Raptors	$1.500 billion
Enron's Earnings without Raptors	$ 429 million
	$1.070 billion
Loss on Enron Financial Statements	
Reduction in Shareholders' Equity due to Accounting Restatement	**($1.200 billion)**
Reduction in Earnings due to Raptor Termination	**($ 710 million)**[3]

[1] Value of shares at time of each transaction.
[2] Source: Powers Report at 132-3.
[3] The Powers Report indicates at 128 that, in addition to the $710 million earnings reduction, another $367 million earnings reduction from the Raptors transactions may be required but has not been included in any Enron restatement.

Prepared by the U.S. Senate Permanent Subcommittee on Investigations, May 2002

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #27

MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
MAY 1, 2000

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 4:00 p.m., C.D.T., but actually begun at 4:10 p.m., C.D.T., on May 1, 2000 at the Enron Building in Houston, Texas.

The following Committee members were present:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Frank Savage

Committee members Ronnie C. Chan, Jerome J. Meyer, Paulo V. Ferraz Pereira, and John A. Urquhart were absent from the meeting. Directors John H. Duncan, Ken L. Harrison, Kenneth L. Lay, and Jeffrey K. Skilling, Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, Ben F. Glisan, Jr., David B. Gorte, Mark E. Koenig, Jeffrey McMahon, Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, also attended the meeting.

The Chairman, Mr. Winokur, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Winokur called the meeting to order and called for a revised agenda to begin with the Treasurer's report. He called upon Mr. McMahon to begin the presentation, a copy of which is filed with the records of the meeting. Mr. McMahon reviewed the liquidity report as of March 31, 2000 and noted that the Company's total liquidity was over $8 billion. He reviewed year-to-date investments and proceeds on sales of assets and stated that the Company still planned to monetize over $1 billion in investments before the end of the year. He discussed the status of capital commitments by business unit and active letters of credit. He reviewed the guarantee portfolio and commented that the portfolio was expected to increase with the growth in certain businesses. He reviewed the Company's rating by each rating agency and noted that Moody's Investor Services had recently upgraded the Company to Baa1 and, therefore, the Company no

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EXHIBIT #28a

longer had a split rating between the two largest rating agencies. He also noted that Standard & Poors Corporation was currently performing its annual analysis of the Company and that Duff & Phelps Credit Rating Co. had recently acquired Fitch IBCA.

Mr. McMahon then discussed the Company's need for additional borrowing flexibility and a proposed authorization for additional debt securities to include the issuance and sale of incremental, unsecured senior debt securities in an amount not to exceed $1 billion. Upon motion duly made by Mr. Blake, seconded by Mr. Savage, and carried, the proposed issuance and sale of incremental, unsecured senior debt securities in an amount not to exceed $1 billion was approved for recommendation to the Board.

Mr. Winokur then noted that a draft of minutes of the meeting of the Committee held on February 7, 2000 had been distributed to the Committee members and called for any corrections or additions. There being none, upon motion duly made by Mr. Blake, seconded by Mr. Belfer, and carried, the minutes of the meeting of the Committee held on February 7, 2000 were approved as distributed.

Mr. Winokur called upon Mr. Fastow to present the Chief Financial Officer's report, a copy of which is filed with the records of the meeting. Mr. Fastow began his presentation by introducing Mr. Glisan and stating that the Company was proposing that Mr. Glisan replace Mr. McMahon as the Company's Treasurer. He discussed Mr. Glisan's background along with backgrounds of Barry J. Schnapper and Timothy A. DeSpain, two individuals that the Company was proposing be elected Deputy Treasurers of the Company. Upon motion duly made by Mr. Blake, seconded by Mr. Belfer, and carried, the proposed officer elections were approved for recommendation to the Board.

Mr. Fastow then discussed the Company's current and projected key financial ratios and stated the ratios were based on the assumption that the proceeds from the sale of Portland General Electric Company were reinvested in the Company's other businesses. He reviewed the stock trading portfolio and the Company's cost of capital, stating that all of the transactions in the portfolio were accomplished utilizing swaps and that the increase in the cost of capital was due to the increase in the Company's stock price. He commented on the Company's increased borrowing spreads, noted that other companies have also experienced increased borrowing spreads, and stated that the offsetting decline in the yield curve has led to borrowing costs comparable to year end costs. He compared the Company's five-year borrowing spread to the BBB and A indices and stated that the Company's borrowing spread was more favorable than its rating would suggest.

Mr. Fastow then gave the Committee an update on LJM2 transactions with the Company including the level of capital commitments, number of investors, number and dollar value of investments already completed, and the Company's business units that had transacted with LJM2. He commented on the direct and indirect impact of LJM1 and LJM2 ("the investment vehicles") on the Company's earnings and funds flow. He stated that he had hired individuals to manage the investment vehicles and that he personally was devoting approximately three hours a week to the investment vehicles. He then called upon Mr. Glisan to discuss Project Raptor.

Mr. Glisan stated that Project Raptor involved establishing a risk management program to enable the Company to hedge the profit and loss volatility of the Company's investments. He discussed the highlights of Project Raptor including the establishment of a non-affiliated vehicle ("Talon") as a hedge counterparty to selected investments, the mechanism for funding Talon, and the level of hedging protection Talon could initially provide the Company. He reviewed the structure of Talon and the amount of capital that would be contributed by LJM2. Mr. Causey joined the discussion and stated that Arthur Andersen LLP had spent considerable time analyzing the Talon structure and the governance structure of LJM2 and was comfortable with the proposed transaction. Mr. Glisan then discussed Project Raptor's risk and potential mitigants to those risks. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Savage, and carried, Project Raptor was approved for recommendation to the Board.

Mr. Winokur called upon Mr. Buy to present the Chief Risk Officer's report, a copy of which is filed with the records of the meeting. Mr. Buy reviewed the current Transaction Approval Process ("TAP") and noted that certain revisions were proposed to reflect recent organizational changes at the Company. The Committee then discussed the TAP for divestitures, currently requiring Board approval for divestitures exceeding $500 million. Following a discussion, the Committee recommended that the TAP be modified such that divestitures be classified as either strategic assets or merchant assets and that the threshold for requiring Board approval would be $200 million for strategic assets and would remain at $500 million for merchant assets. Mr. Buy then answered questions from the Committee regarding the Risk Assessment and Control Group's ("RAC's") analysis of proposed transactions that require additional investments in the future and that involve obtaining toehold positions in publicly traded companies. Following a discussion, the Committee agreed that toehold positions in publicly traded companies should be considered non-conforming transactions per the TAP. Upon motion duly made by Mr. Blake, seconded by Mr. Belfer, and carried, the proposed revisions to the Enron Corp. Transaction Approval Process presented and discussed at the meeting were approved for recommendation to the Board.

Mr. Buy then discussed proposed changes to the Enron Corp. Risk Management Policy ("the Policy"). He stated that the Company was recommending that the Policy be amended to include Japanese Electricity as a new commodity group and noted that the individuals currently analyzing the business opportunities in Japan were the same individuals that had set up the Company's operations in Australia. He then discussed certain proposed limit increases to existing commodity groups within the Policy, including Australian Electricity, Pulp & Paper, and Equity Trading, and certain permanent limit structures and limit increases for commodity groups currently covered under the Interim Policy, including Southern Cone Electricity and Gas. He also noted that there was a proposal to change the wording of the Policy to clarify the difference between position limit violations and loss notification requirements. Upon motion duly made by Mr. Blake, seconded by Mr. Belfer, and carried, the proposed revisions to the Policy were approved for recommendation to the Board.

Mr. Buy then discussed the composition of the Company's merchant portfolio as of December 31, 1999 and any significant changes since the December Board meeting. He commented on the Company's credit exposure to TXU Europe Energy Trading Ltd. ("TXU"), formerly known as Eastern Energy & Power Trading Ltd., noted that the exposure was associated with long term transactions with TXU, and stated that the Company was actively pursuing credit risk mitigation opportunities. He reviewed a detail of non-performing assets, the overall credit reserve, and the Company's equity investments.

Mr. Buy then presented RAC's review of certain Enron Energy Services, LLC ("EES") transactions to ascertain the reasons why RAC and EES have calculated different expected values for proposed transactions. He noted that RAC models the EES base case and does not incorporate certain potential upsides, such as the potential for additional services, into its valuation. He stated that RAC would be incorporating methodologies to enable it to perform a consistent appraisal of the potential upside in EES transactions. He then presented a summary of EES's total commodity portfolio and discussed the two components, wholesale and regulated. He noted that the wholesale portion was incorporated into the North American limits of the Policy and that the regulated portion related to expectations regarding the timing of deregulation and the extent of declines in tariff prices. He then discussed the credit quality of EES's counterparties and noted that 80% were investment grade and that the overall credit quality was very strong. Messrs. Skilling and Sutton joined Mr. Buy in answering questions from the Committee on the EES portfolio and RAC's review of EES.

Mr. Buy then updated the Committee on RAC's Foreign Exchange Project ("the FX Project) that was previously discussed with the Board at the February Committee meeting. He stated that the objective of the project was to identify, measure, and report on foreign currency economic exposure for the Company's worldwide merchant and strategic asset activities. He discussed the FX Project timeline for the Company's overseas regions and the targeted completion dates. He presented an overview of the methodology used in the FX Project including how the exposure would be identified, the data collection tool and the foreign exchange reporting model that RAC had developed, and the overall reporting. He stated that RAC had completed the analysis of Enron South America and he discussed the net notional position by asset and by position type, noting that the majority of the Company's exposure was related to Elektro and was considered a currency translation adjustment exposure. He reviewed the market data on the Brazilian currency, the reais, and noted when the Company had made its major investments in the country and its sensitivity to devaluation of the currency.

Mr. Buy then presented the Market Risk Update and discussed the returns each commodity group had earned compared to the Value-at-Risk ("VAR") it had taken. He gave an overview of the VAR backtesting, stress testing, and the Company's exposure under a "worst case" scenario of 5%-25% shifts in commodity prices. He reviewed limit violations during the first quarter of 2000, noted that the majority of the violations had occurred in the equity portfolio, and discussed the reasons for the violations. He presented two charts displaying VAR as a percentage of market capitalization and of net income for the Company, financial institutions, and other energy companies and commented on how the Company's risk profile impacted the comparisons.

There being no further business to come before the Committee, the meeting was adjourned at 5:40 p.m., C.D.T.

Rebecca C. Carter
Secretary

APPROVED:

Chairman

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EC 000024409

ENRON

Finance Committee Meeting

Project Raptor

Hedging Program for Enron Assets

21

U.S. Senate Permanent Subcommittee on Investigations
(Source: May 1, 2000, Project Raptor Finance Committee Presentation.)
EXHIBIT #28b

EC 000025081

Purpose

Establish a risk management program in order to hedge the Profit & Loss volatility of Enron investments

Original transaction last year LJM to hedge an investment the company [illegible]

looking for a new transaction [illegible] pre-paying

Finance Committee Meeting 04/00

Enron owns a member interest in Talon

- Talon also owns approx. $400 million of ENE stock which is subject to a 3 year stock restriction agreement - Talon cannot sell or hedge the stock.

Finance Committee Meeting
04/00

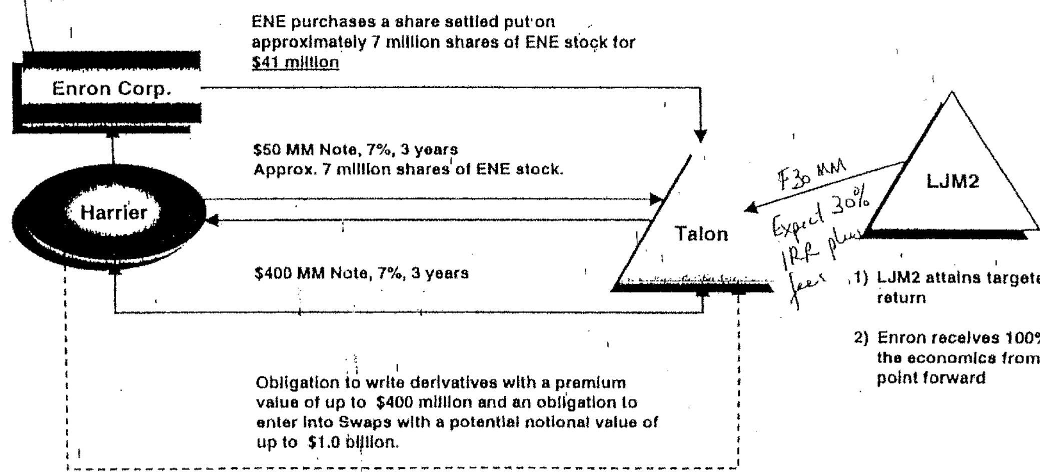
- ENE will help establish a non-affiliated vehicle ("Talon") as a hedge counterparty to selected investments.
- Excess stock from existing structured finance vehicles will be utilized to seed approximately $400 million of capital to Talon. (ie UBS forward positions) (currently held in SPV)
- Initially, vehicle can provide approximately $200 million of P & L protection to ENE. As ENE stock price increases, the vehicle's P & L protection capacity increases as well.
- LJM2 will provide non-ENE equity and will be entitled to a 30% annualized return plus fees.
- ENE will be entitled to 100% of the upside beyond LJM2's return hurdle.

Does not transfer economic risk but transfers P&L volatility

000025084

EC 000025083

Vehicle Structure



1) LJM2 attains targeted return
2) Enron receives 100% of the economics from this point forward

Enron owns a member interest in Talon

- Talon also owns approx. $400 million of ENE stock which is subject to a 3 year stock restriction agreement - Talon cannot sell or hedge the stock.

Finance Committee Meeting 04/00

EC 000025084

Project Raptor

Risks

- Accounting scrutiny
- Substantial decline in the price of ENE stock
  - Program terminates early
  - Increases credit risk
- Counterparty credit

Mitigants

- Transaction reviewed by CAO and Arthur Anderson
- Negotiation of early termination with LJM2
- Assets of vehicle subject to a master netting agreement

ENRON
Finance Committee Meeting
04/00

MINUTES
MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
MAY 2, 2000

Minutes of a meeting of the Board of Directors of Enron Corp. ("Company") held pursuant to due notice at 8:00 a.m., C.D.T., on May 2, 2000 at the Enron Building in Houston, Texas.

The following Directors were present, constituting a quorum, either in person or by telephone conference connection, where each of the participants could hear the comments by the other participants and join in the discussions:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Ms. Rebecca Mark-Jusbasche
Dr. John Mendelsohn
Mr. Paulo Ferraz Pereira
Mr. Frank Savage
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

Director Jerome J. Meyer was absent from the meeting. The meeting began in executive session, during which Messrs. James V. Derrick, Jr. and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company, were also in attendance. Messrs. Robert B. Butts, Richard A. Causey, and Mark E. Koenig, and Ms. Rosalee T. Fleming, all of the Company, joined the executive session in progress as noted.

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #29

C.H

formalization of accounting models, policies, and procedures relating to Enron Energy Services, LLC ("EES"), Enron Broadband Services, Inc. ("EBS"), and Enron NetWorks. He stated that the Committee had received a report on AA's fees for audit and other services provided to the Company. He noted that AA had five full-time partners and over 80 professionals in Houston who were focused on providing services to the Company. He then discussed an amended Audit and Compliance Committee Charter ("the Charter") and he commented on the changes that had been incorporated. Dr. Jaedicke moved approval of the amended Charter, his motion was duly seconded by Mr. Foy, and carried, and the following resolution was approved:

> RESOLVED, that the Charter for the Audit and Compliance Committee of the Board of Directors be, and hereby is, approved and that a copy of the document be attached to the minutes as Exhibit A.

Mr. Lay called upon Mr. Winokur to begin his report. Mr. Winokur stated that one of his acquaintances had told him of a situation at the Company in which an employee's wife had been fatally injured and his children seriously injured while on vacation in Africa. He discussed the extraordinary efforts the Company had undertaken on behalf of the employee and his family to provide for medical assistance and evacuation from Africa. He commented that he was very proud of the Company for its response and the compassion it had shown in the situation.

Mr. Winokur then reported on the Finance Committee meeting held on May 1, 2000. He stated that at the meeting the Committee had received the standard financial reports and that the outlook for the year appeared very positive. He stated that the Committee had also approved the following items for recommendation to the Board: 1) Project Raptor, a transaction to establish a risk management program to enable the Company to hedge the profit and loss volatility of investments, 2) the election of a new Treasurer and two Deputy Treasurers of the Company, 3) the authorization for Incremental Debt, 4) a revision to the Transaction Approval Process to change the limits relating to divestitures, and 5) a revision to the Enron Corp Risk Management Policy to add additional commodities. Following a discussion, Mr. Winokur moved approval of the items, his motion was duly seconded by Mr. Blake, and carried, and the revision to the Enron Corp. Risk Management Policy, as filed with the records of the meeting, and the following resolutions were approved:

Project Raptor

> WHEREAS, Enron Corp. (the "Company") desires to consummate a series of risk management transactions involving (1) the issuance by a newly organized subsidiary entity of the Company

to be named Harrier or a similar name ("Harrier") of a debt security (the "Harrier Note") in consideration of (a) the execution and delivery of the Master Agreement described below and the Security Agreement described below, and (b) the contemporaneous issuance to Harrier by a newly formed entity ("Talon") to be owned indirectly by LJM2 Co-Investment, L. P. (together with its subsidiaries and affiliates, "LJM2") and Harrier of (i) an equity interest in Talon, and (ii) a debt security having a like tenor to the Harrier Note (the "Talon Note") to Talon, (2) the guarantee by the Company of the indebtedness of Harrier under the Harrier Note and the performance of the obligations of Harrier under the Talon Derivatives described below and of any affiliate of the Company under the Securities Agreement described below, (3) the entry by the Company or such subsidiary of a series of agreements with Talon providing for the risk management by the Company against (a) fluctuations in value of, or returns receivable in respect of, equity securities (and derivatives with respect thereto) designated by the Company or its subsidiaries and affiliates, including, without limitation, equity securities acquired or to be acquired by the Company in connection with its broadband activities and merchant assets generated in the Company's wholesale business, and (b) fluctuations in value of a number of shares of Common Stock of the Company to be agreed between the Company and LJM2 from a price to be established by agreement between the Company and LJM2 (the "ENE Derivative"), through the execution of a master agreement and related derivative securities and risk management transactions under the terms agreed in the documents to be executed in connection with the transaction, (4) as partial consideration for the issuance of the Talon Note and equity interest in Talon, the entry by an affiliate of the Company and Talon of an agreement (the "Securities Agreement") granting Talon the right to acquire an agreed number of shares of Common Stock of the Company in which such subsidiary presently owns an indirect beneficial interest, and (5) as partial consideration for the issuance of the Talon Note and equity interest in Talon, the assignment by the Company or an affiliate to Talon of rights to acquire shares of Common Stock of the Company (or equivalent value) (the "UBS Transaction") arising from amendment of certain existing agreements between the Company and an international banking institution (collectively referred to herein as the "Transactions");

NOW, THEREFORE, IT IS RESOLVED, that the Transactions, including, without limitation, the execution and delivery by Harrier to Talon of the ENE Derivative and the acquisition by Talon of shares of Company Common Stock, if any, issued in settlement of the ENE Derivative and the Securities Agreement, are hereby authorized and approved, that any actions taken by officers and officials of the Company prior to the date hereof with respect to the Transactions are hereby ratified, and that the Company shall proceed with the consummation of the Transactions in accordance with the resolutions hereby adopted;

RESOLVED FURTHER, that the Transactions shall be subject to the following terms and conditions (the "Board Conditions"):

(i) the definitive contracts and agreements relating to the Transactions shall have such terms and conditions as are negotiated and approved by an officer of the Company or other person authorized and empowered to act pursuant to these resolutions, the execution of which by any such officer or person, in the name and on behalf of the Company, to be conclusive evidence of the approval by such officers or person of the contents thereof;

(ii) the maximum aggregate principal amount of the Harrier Note to be issued by Harrier to Talon in connection with the Transactions shall not exceed $50 million and the interest rate payable thereon shall not exceed 7%; and

(iii) the maximum number of shares of Company Common Stock (i) subject to the ENE Derivative shall not exceed 7.5 million shares, and the ENE Derivative shall provide that any payment required to be made by Harrier or the Company thereunder may be made in either cash or shares of the Company's Common Stock, at the Company's sole option, and (ii) issuable under the Securities Agreement shall not exceed 4.2 million shares;

RESOLVED FURTHER, that each of the Chairman and Chief Executive Officer, the President and Chief Operating Officer, any Vice Chairman, any Executive or Senior Vice President, any Managing Director, or any Vice President is hereby authorized, empowered, and directed, with the power and authority of the full Board of Directors to the fullest extent permitted by law, to authorize and approve (or ratify if already executed or taken) all agreements, instruments, and documents, and the taking of all actions, as any such officer may deem necessary, advisable, convenient, or proper to consummate the Transactions (subject, however, in all respects, to the Board Conditions), including, without limitation:

(i) all matters insofar as they affect the Company or any of its subsidiaries or affiliates associated with the formation of Talon and the acquisition by Harrier of an equity interest therein, including, without limitation, the execution and delivery of constituent agreements establishing Talon and the terms thereof and the establishment of the amount and form of any capital contribution to be made to Talon in respect of Harrier's equity interest therein;

(ii) the authorization, execution, and delivery of a guarantee agreement whereby the Company guarantees the indebtedness under the Harrier Note and the performance of the obligations of Harrier under the Talon Derivatives and of any affiliate of the Company under the Securities Agreement;

(iii) the authorization, execution, and delivery of a master agreement (the "Master Agreement") providing for the general terms and conditions upon which the risk management activities contemplated by the Transactions will take place, the related form of the 1992 ISDA Master Agreement (Multicurrency-Cross Border), as modified by agreements of the parties and individual confirmations relating to particular transactions (collectively, the "Talon Derivatives"), and the security agreement granting the Company a security agreement in amounts received by Talon in order to secure Talon's obligations under the Talon Note, the Talon Derivatives, and the ENE Swap (the "Security Agreement"), in each case having such terms and conditions (including pricing terms) as such officer shall approve;

(iv) the authorization, execution, and delivery of the Harrier Note with such terms and conditions (including pricing terms) as such officer shall approve;

(v) the approval insofar as they affect the Company or any of its subsidiaries or affiliates of a form of note representing the Talon Note and the issuance by Talon of such Talon Note;

(vi) the authorization, execution, and delivery of a registration rights agreement among the Company and Talon providing for, among other things, the registration of any shares of Common Stock of the Company that may be delivered by the Company or its affiliates in performance of the ENE Derivative and the Securities Agreement, with such terms and conditions as such officer shall approve; and

(vii) the negotiation, authorization, execution, and delivery of such other agreements, instruments, and documents relating to the Transactions, including, but not limited to, agreements affecting the UBS Transaction and agreements, instruments, and documents that provide, among other things, for the indemnification of third parties, and the payment of fees and expenses of third parties as such officer may deem necessary, advisable, convenient, or proper in connection with the Transactions or any other matters addressed by these resolutions;

RESOLVED FURTHER, that in addition to the officers appointed above, Ben F. Glisan, Jr. is hereby appointed as agent and attorney-in-fact of the Company and is authorized, empowered, and directed, with the power of the full Board of Directors, subject to control and direction by the Company, to the fullest extent permitted by law, to authorize and approve (or ratify if already executed or taken) all agreements, instruments, and documents, and the taking of all actions as such agent and attorney-in-fact may deem necessary or desirable and shall have all the powers of an officer of the Company with respect to these resolutions (subject, however, in all respects, to the Board Conditions) solely for the purpose of consummating the Transactions; it is the intent of the Board of Directors that Mr. Glisan, in his capacity as agent and attorney-in-fact of the Company, shall have all the duties, obligations, and responsibilities of an officer of the Company for purposes of the Transactions, as if he were an officer of the Company;

RESOLVED FURTHER, that an aggregate of 7.5 million shares of Common Stock are hereby reserved for issuance in settlement of the ENE Derivative referred to above in the event the Company elects to make settlement thereunder in shares of Company Common Stock;

RESOLVED FURTHER, that the Company is authorized to issue such shares of Common Stock of the Company in settlement of the ENE Derivative and to offer and sell any such shares delivered in settlement of the Securities Agreement, and that upon any such issuance in accordance with the terms of the ENE Derivative and

Securities Agreement, such shares of Common Stock shall be validly issued, fully paid, and non-assessable;

RESOLVED FURTHER, that if it is deemed necessary or advisable by the officers of the Company that the Common Stock issuable upon settlement of the ENE Derivative or the Securities Agreement be qualified or registered for sale under the applicable Blue Sky Laws or securities acts of any jurisdiction, or that a filing be made in any jurisdiction to secure or obtain an exemption from qualification or registration, the officers of the Company are each authorized to perform on behalf of the Company any and all such acts as any one or more of them may deem necessary or advisable in order to comply with such laws of such jurisdiction, and in connection therewith, to execute and file all requisite papers and instruments and to make any and all payments of filing, registration or other fees, costs, and expenses, and to take any and all further action in connection with the foregoing which any one or more of them shall deem necessary or advisable;

RESOLVED FURTHER, that if the officers of the Company determine that it is desirable for the Company to do so, the Company may make application to the New York Stock Exchange, Inc. and one or more other national securities exchanges for listing of the Enron Common Stock to be issued in the Transactions; that the Chairman of the Board, any Vice Chairman of the Board, the President, any Executive or Senior Vice President, any Managing Director, or any Vice President of the Company be, and they hereby are, authorized and directed to execute and deliver any applications, documents, or agreements, to take any and all actions, to appear before such exchanges if necessary, to appoint any banking or other institution as an agent of the Company for any purpose, and to do so or cause to be done any and all things as may appear to them to be necessary or desirable in order to effect such listing;

RESOLVED FURTHER, that the execution by any officer of the Company of any papers and instruments or the performance by any one or more of them of any act in connection with the foregoing resolutions shall conclusively establish their authority therefor from the Company and the approval and ratification by the Company of the papers and instruments so executed and the actions so taken;

RESOLVED FURTHER, that the actions of the officers and employees of the Company acting under the supervision of the officers heretofore taken on behalf of the Company in connection with the above resolutions and the actions contemplated thereby, are, in all respects, confirmed and ratified, and the officers of the Company, together or individually, may take any and all action and do any and all things, or direct the taking of such action or the doing of such things by employees of the Company acting under the supervision of the officer(s) as may be deemed by any of them to be necessary or advisable to effectuate the Transactions, and the taking of any and all such actions and the performance of any and all such things in connection with the foregoing shall conclusively establish their authority from the Company and the approval and ratification by the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Officer Elections

RESOLVED, that the following persons be, and each hereby is, elected to the position set forth opposite their names, to serve for the ensuing year and until their successors are duly elected and qualified:

Ben F. Glisan, Jr.	Vice President, Finance and Treasurer
Timothy A. DeSpain	Deputy Treasurer
Barry J. Schnapper	Deputy Treasurer

Incremental Debt Authority

WHEREAS, the Company desires to effect the issuance and sale from time to time of incremental, unsecured senior debt in an aggregate amount not to exceed $1,000,000,000 (at exchange rates current at the date of issuance, if and to the extent all or any portion of such senior debt is denominated in a currency other than United States Dollars), for general corporate purposes, at interest rates, durations, and such other terms (including whether the debt will be

TO 1/28 1/4/01

MINUTES
MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
AUGUST 7-8, 2000

Minutes of a meeting of the Board of Directors of Enron Corp. ("Company") noticed to begin at 7:00 p.m., C.D.T., but actually begun at 7:25 p.m., C.D.T., on August 7, 2000 at the Four Seasons Hotel, Whitney Room, in Houston, Texas.

The following Directors were present, constituting a quorum:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Ms. Rebecca P. Mark
Mr. Jerome J. Meyer
Dr. John Mendelsohn
Mr. Paulo Ferraz Pereira
Mr. Frank Savage
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham

Director Herbert S. Winokur was absent from the meeting. Messrs. Richard A. Causey, Andrew S. Fastow, Mark E. Koenig, and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company, also attended the meeting.

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Lay called the meeting to order and called for a revised agenda to begin the meeting with the Financial and Earnings and Stock Performance reports. He called upon Mr. Causey to begin his presentation, a copy of which is filed with the records of the meeting.

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #30a

CA

AASCGA0073.350

empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Mr. Skilling then distributed a suggested form of resolutions relating to a proposed risk management program, Raptor III. He stated that management was proposing Raptor III to provide for the creation of up to two additional structures and related risk management transactions. He stated that Raptor III would be similar in structure to Raptor I and Raptor II, approved by the Board at the May 2, 2000 meeting and by the Executive Committee at the June 22, 2000 meeting, respectively. He noted that Raptor III would provide additional mechanisms to hedge the profit and loss volatility of the Company's investments. Following a discussion, upon motion duly made by Mr. Meyer, seconded by Mr. Ferraz, and carried, the following resolutions were approved:

WHEREAS, Enron Corp. (the "Company") desires to authorize the creation of up to two additional structures and related risk management transactions similar to those approved by the Company's Board of Directors on May 2, 2000 involving Harrier I LLC and Talon I LLC and by the Executive Committee of the Company's Board of Directors on June 22, 2000 involving Harrier II LLC and Talon II LLC, including, without limitation, (1) the issuance by each of one or more existing or newly organized subsidiaries of the Company (each a "Subsidiary") of a debt security (each a "Subsidiary Note") in consideration of (a) the execution and delivery of a Master Agreement described below and a Security Agreement described below, and (b) the contemporaneous issuance to Subsidiary by one or more entities (each an "Entity") owned or to be owned directly or indirectly by LJM2 Co-Investment, L. P. (together with its subsidiaries and affiliates, "LJM2") or another third-party entity and Subsidiary of (i) an equity interest in Entity, and (ii) a debt security having a like tenor to the subject Subsidiary Note (each an "Entity Note"), (2) the guarantee by the Company of the indebtedness of each Subsidiary under its Subsidiary Note and the performance of the obligations of Subsidiary under the subject Entity Derivatives and the Securities Agreement described below, (3) the guarantee by the Company of the performance of a Subsidiary's obligation to purchase LJM2's (or other third-party entity's) interest in an Entity upon the occurrence of certain events set forth in the subject Entity constitutional documents, (4) the entry by the Company or Subsidiary into a series of agreements with

Entity providing for the risk management by the Company against (a) fluctuations in value of, or returns receivable in respect of, equity securities (and derivatives with respect thereto) designated by the Company or its subsidiaries and affiliates, including, without limitation, equity securities acquired or to be acquired by the Company in connection with its broadband activities and merchant assets generated in the Company's wholesale business, and (b) fluctuations in value of a number of shares of Common Stock of the Company to be agreed between the Company and LJM2 (or other third-party entity, if applicable) from a price to be established by agreement between the Company and LJM2 (or other third-party entity, if applicable) (each an "ENE Derivative"), through the execution of a master agreement and related derivative securities and risk management transactions under the terms agreed in the documents to be executed in connection with the transaction, and (5) as partial consideration for the issuance of a Subsidiary Note and equity interest in an Entity to a Subsidiary, the entry by such Subsidiary and Entity into an agreement (each a "Securities Agreement") granting Entity the right to acquire an agreed number of shares of Common Stock of the Company in which Subsidiary will own (after giving effect to the transactions contemplated by these resolutions) an indirect beneficial interest, and (6) any types or combinations of transactions or series of transactions similar to those outlined in (1) through (5) of this paragraph (transactions (1) through (6) collectively referred to herein as the "Transactions").

NOW, THEREFORE, IT IS RESOLVED, that the Transactions, including without limitation, the execution and delivery by each Subsidiary of a Subsidiary Note, an Entity Derivatives described below, and a Securities Agreement, the execution and delivery by the Company of each ENE Derivative and the guarantee agreements referred to above and the acquisition by any Entity of shares of Company Common Stock, if any, issued in settlement of an ENE Derivative and a Securities Agreement, are hereby authorized and approved subject to the following terms and conditions (the "Board Conditions"):

(i) specific Transactions must be approved and authorized by either the Company's Chairman and Chief Executive Officer or President and Chief Operating Officer;

(ii) subject to the immediately preceding clause (i), the definitive contracts and agreements relating to the Transactions shall have such terms and conditions as are negotiated and approved by an officer of the Company or other person authorized and empowered to act pursuant to these resolutions, the execution of which by any such officer or person, in the name and on behalf of the Company, shall be conclusive evidence of the approval by such officers or person of the contents thereof;

(iii) the maximum aggregate principal amount of each Subsidiary Note or other debt instrument to be issued by a Subsidiary in connection with the Transactions shall not exceed $50 Million and the stated interest rate payable thereon shall not exceed 7%;

(iv) the maximum aggregate principal amount of all Subsidiary Notes or other debt instruments contemplated by the immediately preceding clause (iii) shall not exceed $100 Million;

(v) the maximum number of shares of Company Common Stock (a) subject to each ENE Derivative shall not exceed 8.0 million shares, and (b) issuable under each Securities Agreement shall not exceed 8.0 million shares; and

(vi) the maximum number of shares of Company Common Stock (a) subject to all ENE Derivatives contemplated by the immediately preceding clause (v) shall not exceed 16 million shares, and (b) issuable under all Securities Agreements contemplated by the immediately preceding clause (v) shall not exceed 16 million shares;

RESOLVED FURTHER, that each of the Chairman and Chief Executive Officer, the President and Chief Operating Officer, any Vice Chairman, any Managing Director, any Vice President, and the Treasurer or any Deputy Treasurer is hereby authorized, empowered, and directed, with the power and authority of the Board of Directors to the fullest extent permitted by law, to authorize and approve (or ratify if already executed or taken) all agreements, instruments, and documents, and the taking of all actions, as any such officer may deem necessary, advisable, convenient, or proper to consummate the Transactions (subject, however, in all respects, to the Board Conditions), including, without limitation:

(i) all matters insofar as they affect the Company or any of its subsidiaries or affiliates associated with the formation of each Entity and the acquisition by a Subsidiary of an equity interest therein, including, without limitation, the execution and delivery of constituent agreements establishing an Entity and the terms thereof and the establishment of the amount and form of any capital contribution to be made to an Entity in respect of a Subsidiary's equity interest therein;

(ii) the authorization, execution, and delivery of each guarantee agreement whereby the Company guarantees the indebtedness under a Subsidiary Note and the performance of a Subsidiary's obligations under an Entity Derivatives and a Securities Agreement;

(iii) the authorization, execution, and delivery of each guarantee agreement whereby the Company guarantees the performance of a Subsidiary's obligation to purchase LJM2's (or other third-party's) interest in an Entity upon the occurrence of certain events set forth in the Entity constitutional documents;

(iv) the authorization, execution, and delivery of one or more master agreements (each a "Master Agreement") providing for the general terms and conditions upon which the risk management activities contemplated by the Transactions will take place, the related form of the 1992 ISDA Master Agreement (Multicurrency-Cross Border), as modified by agreements of the parties and individual confirmations relating to particular transactions (collectively, the "Entity Derivatives"), and the security agreement granting the Company and a Subsidiary a security interest in amounts received by Entity in order to secure Entity's obligations under an Entity Note, Entity Derivatives, and ENE Derivative (each a "Security Agreement"), in each case having such terms and conditions (including, without limitation, pricing terms) as such officer shall approve;

(v) the authorization, execution, and delivery of each Subsidiary Note and Securities Agreement, in each case, with such terms and conditions (including, without limitation, pricing terms) as such officer shall approve;

(vi) the approval insofar as they affect the Company or any of its subsidiaries or affiliates of each form of note representing an Entity Note and the issuance by an Entity of such Entity Note;

(vii) the authorization, execution, and delivery of each registration rights agreement between the Company and an Entity providing for, among other things, the registration of any shares of Common Stock of the Company that may be delivered by the Company or its affiliates in performance of an ENE Derivative and a Securities Agreement, with such terms and conditions as such officer shall approve; and

(viii) the negotiation, authorization, execution, and delivery of such other agreements, instruments, and documents relating to the Transactions, including, but not limited to, documents relating to each ENE Derivative and agreements, instruments, and documents that provide, among other things, for the indemnification of third parties, and the payment of fees and expenses of third parties as such officer may deem necessary, advisable, convenient, or proper in connection with the Transactions, or any other matters addressed by these resolutions;

RESOLVED FURTHER, that an aggregate of 16.0 million shares of Company Common Stock are hereby reserved for issuance in settlement of the ENE Derivatives referred to above in the event the Company elects to make settlement thereunder in shares of Company Common Stock;

RESOLVED FURTHER, that the Company is authorized to issue such shares of Common Stock of the Company in settlement of ENE Derivatives, and to offer and sell any such shares delivered in settlement of any Securities Agreement and that upon any such issuance in accordance with the terms of the subject ENE Derivative and Securities Agreement, such shares of Common Stock shall be validly issued, fully paid, and non-assessable;

RESOLVED FURTHER, that if it is deemed necessary or advisable by the officers of the Company that the Common Stock issuable upon settlement of an ENE Derivative or Securities Agreement be qualified or registered for sale under the applicable Blue Sky Laws or securities acts of any jurisdiction, or that a filing be made in any jurisdiction to secure or obtain an exemption from qualification or registration, the officers of the Company are each authorized to perform on behalf of the Company any and all such acts as any one or more of them may deem necessary or advisable in order to comply with such laws of such jurisdiction, and in connection therewith, to execute and file all requisite papers and instruments and to make any and all payments of filing, registration or other fees. costs. and expenses, and to take any and all further action in connection with the foregoing which any one or more of them shall deem necessary or advisable;

RESOLVED FURTHER, that if the officers of the Company determine that it is desirable for the Company to do so, the Company may make application to the New York Stock Exchange, Inc. and one or more other national securities exchanges for listing of the Company Common Stock to be issued in the Transactions; that the Chairman of the Board, any Vice Chairman of the Board, the President, any Executive or Senior Vice President, any Managing Director. any Vice President. the Treasurer. or any Deputy Treasurer of the Company be. and they hereby are, authorized and directed to execute and deliver any applications, documents, or agreements, to take any and all actions, to appear before such exchanges if necessary, to appoint any banking or other institution as an agent of the Company for any purpose, and to do or cause to be done any and all things as may appear to them to be necessary or desirable in order to effect such listing;

RESOLVED FURTHER, that the execution by any officer of the Company of any papers and instruments or the performance by any one or more of them of any act in connection with the foregoing resolutions shall conclusively establish their authority therefore from the Company and the approval and ratification by the Company of the papers and instruments so executed and the actions so taken;

RESOLVED FURTHER, that the actions of the officers and employees of the Company acting under the supervision of the officers heretofore taken on behalf of the Company in connection with the above resolutions and the actions contemplated thereby are, in all respects, confirmed and ratified, and the officers of the Company, together or individually, may take any and all action and do any and all things, or direct the taking of such action or the doing of such things by employees of the Company acting under the supervision of the officer(s) as may be deemed by any of them to be necessary or advisable to effectuate the Transactions, and the taking of any and all such actions and the performance of any and all such things in connection with the foregoing shall conclusively establish their authority from the Company and the approval and ratification by the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

There being no further business to come before the Board, the meeting was adjourned at 11:20 a.m., C.D.T.

Rebecca C. Carter
Secretary

APPROVED:
Kenneth L. Lay
Chairman

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AGENDA ITEM 3

Project Raptor II

- ENE will establish a second risk management program to hedge the Profit & Loss volatility of Enron investments.
- Raptor II is exactly the same structure as Raptor I.
- Raptor II is being implemented due to overwhelming business unit demand.
- The structure requires 6 months from the closing of the transaction before hedges can be executed. Closing the transaction now will allow ENE to utilize Raptor II at year-end.

Structural Highlights:

Excess stock from existing structured finance vehicles will be utilized to seed approximately $400 million of capital to Raptor II.

Initially, the vehicle can provide approximately $200 million of P&L protection to ENE. As ENE stock price increases, the vehicle's P&L protection capacity increases as well.

For additional information on the Raptor structure please refer to the board presentation dated May 2, 2000

ENRON

RB 00231

U.S. Senate Permanent Subcommittee on Investigations
(Source: June 22, 2000, Executive Committee Meeting, Project Presentation.)
EXHIBIT #30b

ENRON DEAL SUMMARY

DEAL NAME: Raptor
Originated: Enron Corp.
Expected Closing Date: 4/18/00
Expected Funding Date: 5/04/00

Date Completed: April 18, 2000
Investment Analyst: Chris Loehr
Investment Type: Equity

INVESTMENT

LJM2 Capital Commitment	$ 30,000,000

DEAL DESCRIPTION

Talon I LLC ("Talon") is a special purpose entity organized for the purpose of entering into certain derivative transactions. LJM2, through its 100% voting control of Talon, has the unilateral ability to make the investment decisions for Talon and is not contractually obligated to execute any derivative transactions with Enron. LJM2 will execute derivative transactions with Harrier I LLC ("Harrier"), a wholly-owned subsidiary of Enron, to the extent those investment decisions are aligned with LJM2's investment objectives. Enron, through Harrier, will offer LJM2 the opportunity to execute derivative instruments relating to both public and private energy and telecommunication investments made by Enron.

TRANSACTION SUMMARY

- On April 21, 2000, LJM2 will purchase 100% of the voting interest in Talon for $30,000,000
- Talon is a bankruptcy remote, special purpose vehicle that will be capitalized with:
  - LJM2's capital investment
  - A series of forward sales on Enron shares ($500 million of gross value but $350 million of net value after a 30% liquidity discount has been ascribed given the restrictions imposed on the underlying shares) resulting in ultimate ownership by Talon of Enron common stock
  - The sale of puts on [7 million] Enron shares with a strike of [$57.50], a maturity in [six months] from close and a premium due of [$6] per share.
- In exchange for the above capitalization, Talon will provide Harrier: (i) a $400 million note whose principal is convertible into derivatives, and (ii) a special limited partnership interest in Talon initially valued at $1,000.
- To limit Talon's exposure to the mark-to-market movements of the underlying derivative transactions, Talon and Harrier agree to limit the notional amount of swaps and premiums paid as follows: (i) up to $1.5 billion notional value of at-the-money swaps, (ii) up to $400 million of net premiums on other derivative transactions, and (iii) up to $1 billion of loss on premium paid derivatives.
- LJM2 will have a fair market value put for its membership interest in Talon that allows LJM2 to put its interest back to Harrier in the event that LJM2 has not received the greater of $41 million or a 30% IRR by October 31, 2000. Enron has provided support for Harrier's financial obligation under such an event in the form of a guaranty.
- At the maturity of the structure, Talon will liquidate the excess value, if any, of the Enron shares under the forward sales over the derivative losses, if any, at Talon and any principal outstanding on the Talon note. The excess proceeds, if any, will be distributed to LJM2 and Harrier in accordance with their capital accounts and the distribution waterfall.

INVESTMENT RETURN SUMMARY

Base Case Return

It is expected that Talon will have earnings and cash sufficient to distribute $41 million to LJM2 within six months, yielding an annualized return on investment to LJM2 of 76.8%

Distributions

Talon's distributions to equity holders will be limited by earnings at Talon. To the extent there are earnings and sufficient cash to distribute, distributions will be made according to the following waterfall:

- First, $41 million to LJM2
- Second, distributions as necessary until LJM2 receives a 30% IRR over the term of the structure (unless the IRR was achieved through the $41 million distribution above)
- Third, 100% to the special limited partnership interest, Harrier I LLC, a wholly-owned subsidiary of Enron

VEL 00132

U.S. Senate Permanent Subcommittee on Investigations
(Source: April 18, 2000, Enron and LJM2 Deal Approval Sheets: Raptor.)
EXHIBIT #31

Fair Market Value Put
In the event that LJM2 has not received the greater of $41 million or a 30% IRR on its investment by October 31, 2000, LJM2 will have a fair market value put whereby LJM2 can put its interest in Talon back to Harrier. The fair market value of the membership interest is determined largely by Enron's stock price and is summarized below:

Enron Stock Price	Fair Market Put Value	LJM2 IRR
[$57.50]	$41.0 million	76.8%
[$48.95]	$34.5 million	30.0%
[$48.35]	$30.0 million	0.0%

Expenses
Enron has agreed to cover all of LJM2's accounting and legal expenses related to this transaction. Enron will cover expenses related to formation of the structure as well as ongoing expenses.

VEL 00133

APPROVALS	Name	Signature	Date
Business Unit Originator	Ben Glisan	Ben Glisan	6-12-00
Business Unit Legal	Scott Sefton	S. Sefton	5-23-00

VEL 00134

LJM2 APPROVAL SHEET

This Approval Sheet should be used to approve Enron's participation in any transactions involving LJM Cayman, L.P. ("LJM1") o LJM2 Co-Investment, L.P. ("LJM2"). LJM1 and LJM2 will collectively be referred to as "LJM". This Approval Sheet is in additior to (not in lieu of) any other Enron approvals that may be required.

GENERAL

Deal name: Raptor

Date Approval Sheet completed: April 18, 2000

Enron person completing this form: Trushar Patel

Expected closing date: May 4, 2000

Business Unit: Enron Corp.

Business Unit Originator: Ben Glisan

This transaction relates to ☐LJM1 and/or ☑LJM2.

This transaction is ☐ a sale by Enron ☐a purchase by Enron ☐a co-sale with Enron ☐a co-purchase with Enron and/or ☑other: creation of hedging structure.

Person(s) negotiating for Enron: Ben Glisan

Person(s) negotiating for LJM: Michael Kopper

Legal counsel for Enron: Vinson & Elkins

Legal counsel for LJM: Kirkland & Ellis

DEAL DESCRIPTION

Talon I LLC ("Talon") is a special purpose entity organized for the purpose of entering into certain derivative transactions. LJM2, through its 100% voting control of Talon, has the unilateral ability to make the investment decisions for Talon and is not contractually obligated to execute any derivative transactions with Enron. LJM2 will execute derivative transactions with Harrier I LLC ("Harrier"), a wholly-owned subsidiary of Enron, to the extent those investment decisions are aligned with LJM2's investment objectives. Enron, through Harrier, will offer LJM2 the opportunity to execute derivative instruments relating to both public and private energy and telecommunication investments made by Enron.

ECONOMICS

Talon's distributions to equity holders will be limited by earnings at Talon. To the extent there are earnings and sufficient cash to distribute, distributions will be made according to the following waterfall:

- First, $41 million to LJM2
- Second, distributions as necessary until LJM2 receives a 30% IRR over the term of the structure (unless the IRR was achieved through the $41 million distribution above)
- Third, 100% to the special limited partnership interest, Harrier I LLC, a wholly-owned subsidiary of Enron

DASH

See attached.

VEL 00129

LJM APPROVAL SHEET
Page 2

ISSUES CHECKLIST

1. Sale Options

   a. If this transaction is a sale of an asset by Enron, which of the following options were considered and rejected:

      ☐Condor ☐JEDI II ☐Third Party ☐Direct Sale. Please explain: Not a sale of an asset by Enron

   b. Will this transaction be the most beneficial alternative to Enron? ☑Yes ☐No. If no, please explain:__________.

   c. Were any other bids/offers received in connection with this transaction? ☐Yes ☑No. Please explain: Private structured finance transaction

2. Prior Obligations

   a. Does this transaction involve a Qualified Investment (as defined in the JEDI II partnership agreement)? ☐Yes ☑No. If yes, please explain how this issue was resolved: __________.

   b. Was this transaction required to be offered to any other Enron affiliate or other party pursuant to a contractual or other obligation? ☐Yes ☑No. If yes, please explain: __________.

3. Terms of Transaction

   a. What are the benefits (financial and otherwise) to Enron in this transaction? ☐Cash flow ☐Earnings

      ☑Other: Ability to hedge mark-to-market exposure on investments in publicly and privately held companies

   b. Was this transaction done strictly on an arm's-length basis? ☑Yes ☐No. If no, please explain:__________.

   c. Was Enron advised by any third party that this transaction was not fair, from a financial perspective, to Enron? ☐Yes ☑No. If yes, please explain:__________.

   d. Are all LJM expenses and out-of-pocket costs (including legal fees) being paid by LJM? ☐Yes ☑No. If no, is this market standard or has the economic impact of paying any expenses and out-of-pocket costs been considered when responding to items 1.b. and 3.b. above? ☑Yes ☐No.

4. Compliance

   a. Will this transaction require disclosure as a Certain Transaction in Enron's proxy statement? ☑Yes ☐No.

   b. Will this transaction result in any compensation (as defined by the proxy rules) being paid to any Enron employee? ☐Yes ☑No.

   c. Have all Enron employees' involvement in this transaction on behalf of LJM been waived by Enron's Office of the Chairman in accordance with Enron's Conduct of Business Affairs Policy? ☑Yes ☐No. If no, please explain: __________.

   d. Was this transaction reviewed and approved by Enron's Chief Accounting Officer? ☑Yes ☐No.

   e. Was this transaction reviewed and approved by Enron's Chief Risk Officer? ☑Yes ☐No.

   f. Has the Audit Committee of the Enron Corp. Board of Directors reviewed all Enron/LJM transactions within the past twelve months? ☐Yes ☑No. (The Audit Committee has not held a meeting since LJM2's formation.) Have all recommendations of the Audit Committee relating to Enron/LJM transactions been taken into account in this transaction? ☐Yes ☐No.

VEL 00130

I:\Raptor_LJMApproval.doc

LJM APPROVAL SHEET
Page 3

APPROVALS	Name	Signature	Date
Business Unit	Ben Glisan	Ben Glisan	6-12-00
Business Unit Legal			
Enron Corp. Legal	Rex Rogers	[illegible]	5-24-00
Global Finance Legal	Scott Sefton	Scott Sefton	5-22-00
RAC	Rick Buy [illegible]	[illegible]	5-22-00
Accounting	Rick Causey	Richard A Causey	5-22-00
Executive	Jeff Skilling		

VEL 00131

Stock Price Risk in Financings

Potential Required Future Equity issuance

4 transactions w/ Enron stock price [illegible]

Equivalent Shares (000's)

	$40	$50	$60	$70	$80
Osprey	10,688	-	-	-	-
Raptor 1	11,683	7,149	2,666	1,197	95
Raptor 2	11,733	5,219	-	-	-
Raptor 4	11,237	7,358	4,771	-	-
	45,341	19,726	7,437	1,197	95

Assumption: the value of the other assets were [illegible] Enron stock would need to be [illegible]

- -Osprey matures in 2003
- -Raptor vehicle share issuances are triggered by date
  - -Osprey shares trigger in 2003
  - -Q101 Restructuring shares trigger in 2005

2A - 8

U.S. Senate Permanent Subcommittee on Investigations
(Source: April 2001, Finance Committee Presentation.)
EXHIBIT #32

EC 000024474

[redacted]

REDACTED

From: [redacted]
Sent: Friday, October 05, 2001 12:49 PM
To: [redacted]
Subject: Reply Message: Reply from [redacted] is RE: option trades

[redacted]

I will clear things with ENE legal before we do anything. If you can get me wiring instructions I will get Paine Webber to wire funds.

Thanks

[redacted] to Text message

Original Message:
[redacted]

one more thought before we talk (actually [redacted] thought):

would it make sense for you to run your contemplated trades by [redacted]

issue may involve your comfort in directing us to make enron transactions so soon after departure (given effective date of separation agreement).

from a hedge, market, and volatility perspective, i think your decision and timing is right on. your equity position remains entirely concentrated in enron stock. your mark-to-market wealth is down signficantly this year. markets have had a nice rebound from terrorist attacks, and you are taking advantage of the turbulent market conditions through selling volatility (call options) as a partial hedge against a portion of your economic shares owned through in the money options.

assuming that you are able to get your paine webber broker to wire funds to us today (he has had instructions for over a week and has not been responsive), we should be ready to act on your instructions tuesday.

[redacted] and i will call you this morning to follow up.

[redacted]

p.s. are you going to [redacted]

-----Original Message-----
From: [redacted]
Sent: Thursday, October 04, 2001 6:49 AM
To: [redacted]
Subject: RE: option trades

[redacted]

My thought process is that I believe that the stock has limited upside

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #33a

in
the near term and, in fact, has some downside exposure. I would rather
short calls at this point than to buy puts and my thinking is to do
something relatively short term and probably close to the money, so your
nov
30's and jan 30's would probably provide the best opportunity. I am not
too
worried about liquidity right now and I have paid quarterly tax payments
so
the end of year or april 15 tax payment is managable. My biggest
question
right now is liquidity in the options themselves. It has been a long
time
since I really looked at trading volume, what kind of volume do they
trade?

I will call you later today.

[redacted]

-----Original Message-----
From: [redacted]
Sent: Wednesday, October 03, 2001 5:35 PM
To: [redacted]
Cc: [redacted]
Subject: option trades

[redacted]

a few thoughts and questions (more questions than thoughts):

1) probably talking conventional, exchange-traded short-call options
secured
(initially) by cash. as unrestricted shares transfer into [redacted] we
can
substitute shares for cash.

2) i assuming that the option trade is based on a thought that the stock
has
limited upside (and you wish to reduce exposure to concentrated
position) as
opposed to huge near-term price risk. thus, recommend shorting a call,
as
opposed to buying a put.

3) how far out in time were you thinking on the option expiration? from
a
time-skew volatility perspective, at-the-money call volatility declines
from
59 november to 57 january to 53 april to 46 jan 03. 100 day historic
volatility in stock a 56 (although near-term higher).

4) how far in/out of the money were you thinking? looking at the price
strike skew, from 10% out of money to 10% in: november 65 vs 59; jan 58
vs
55; april 53 vs 53; jan 03 47 vs 45.

5) i was thinking of selling either jan 02 35 calls for $3.40 or april
35
calls for $4.60 (if that gives sufficient downside protection).
alternatively, you have upside from existing out of money option, what

[redacted]

rom: [redacted]
ent: Thursday, October 04, 2001 6:16 PM
o: [redacted]
c:
ubject: RE: option trades

[redacted]

) tuesday late morning would work well; normally happy to meet monday we are officially closed), but entertaining out of town brother.

) i am in all week, so mid-week execution works fine. you are welcome o sit in with me should you desire.

) still need to set later date for us to present investment plan to you we will not be ready by tuesday).

alk to you soon,

[redacted]

----Original Message-----
'rom: [redacted]
ent: Thursday, October 04, 2001 5:47 PM
'o: [redacted]
ubject: RE: option trades

[redacted]

: think we should begin thinking about shorting January calls on say .00,000 hares at or near the money. We should shoot for midweek or so of next eek. There are a number of analyst reports out that are really trying o ush up the stock and with a little help from the market, they may get a ew ore points out of it over the next few days. I can beam some cash into n ccount at [redacted] tomorrow or monday. I would also like to get ogether n Monday or Tuesday. I can come over probably late morning on one of hose ays.

[redacted]

-----Original Message-----
From: [redacted]
Sent: Thursday, October 04, 2001 8:48 AM
To:
Cc: [redacted]
Subject: RE: option trades

1) open interest in many strikes around 1000 contracts.

2) don't worry too much, as the more interesting number relates to liquidity

[redacted]

From: [redacted]
Sent: Tuesday, October 02, 2001 7:47 PM
To: [redacted]
Subject: RE: [redacted]

[redacted]

Sorry, I didn't get this until tonight. You can either deliver it or send it, whatever is easiest for you. I'll get with you probably on thursday to check dates. Also, please let [redacted] know that I think we may want to sell some ENE calls in the next few days before earnings are released. I don't know anything, but I know how ENE works and I'm sure they will be able to show strong recurring earnings, but with the market where it is and the stock where it is I expect them to take that opportunity and do some housecleaning on some non=productive assets. If I'm wrong about that, I can't imagine anything coming out that would move ENE (or just about any other company) up much, but there is downside in everything. I would be interested in yours and [redacted] perspective.

Thanks

[redacted]

-----Original Message-----
From: [redacted]
Sent: Tuesday, October 02, 2001 8:49 AM
To: [redacted]
Subject: RE: [redacted]

[redacted] We will prepare a check from you [redacted] for $1,533 (you don't need to sign it). I will be at the Houston Chapter office today and could deliver the check or alternately drop it by your home if you would like to deliver. Let me know.

Please check you calendar for the weeks of October 8 and 15 and give us some dates that work for you for a meeting. Thanks.

[redacted]

-----Original Message-----
From: [redacted]
Sent: Monday, October 01, 2001 11:13 PM
To: [redacted]
Subject: [redacted]

[redacted]

You have probably already seen the email I sent pledging [redacted] a [redacted] Would you please have a check written and I will stop by and sign it later this week. Also, should we get together with [redacted] in the next

THE

LUNTZ RESEARCH COMPANIES

Luntz Research & Strategic Services ■ The Public Opinion Company ■ Luntz Corporate ■ Luntz Worldwide

MEMORANDUM

To: Ken Lay, Grey Whalley, and Mark Frevert
From: Frank Luntz
Re: Initial Focus Group Observations & Recommendations
Date: October 19, 2001

OVERVIEW

The words I am about to write are direct, strong and may startle you but I am convinced of their accuracy.

I realize that at the end of the day, most of what I say here will be boiled down in terms of your bottom line: profitability and productivity. But that is ***exactly*** why you will hear me use words like ***crisis*** and ***emergency***. From associates to VPs, your employees are telling us that these issues take up serious amounts of time during their workday. The negative environment they are working in has become more than just a distraction. It is now a barrier to the "excellence" and "performance" that Enron values so highly.

Having helped a number of large companies through similar problems, I can tell you firsthand that employees who are basically content with their jobs perform more efficiently and more effectively on a day-to-day basis. Employees who are frustrated at the levels we saw this week, tend to be less focused and less willing to give 110% when it matters most. So as I said before, this all comes down to your bottom line.

Your employees at the associate, manager, director and VP level made it very clear to us that they see a morale crisis among their colleagues at Enron. Sure, we live in unstable times, Enron prides itself on innovation and competition, and the precipitous drop in the stock price undoubtedly contributes to their expressions of insecurity and unease. But in listening to the four employee focus groups (stratified by level in the company), they are all waiting with growing impatience for senior management to provide a more clearly defined and less chaotic path toward the future.

The intensity and uniformity of responses cannot be dismissed. From systemic problems with HR to the lack of a corporate vision, there is a consensus at all four employee levels that Enron is at a crossroads and that the path you take in the coming months will determine whether you succeed in retaining and building a satisfied workforce or cause a mass exodus of employees.

1000 Wilson Boulevard ■ Suite 950 ■ Arlington, Virginia 22209 ■ Phone (703) 358-0080 ■ Fax (703) 358-0089

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #34

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I must admit some surprise at how candid your employees were with me. I think one reason was that several people recognized me from my television work and that helped them realize that this was a serious effort to understand what employees really felt. But I must still emphasize that these are only "qualitative" results – a scientific quantitative survey will come later. We were looking for the kind of intensity and depth-of-response that only a focus group can deliver. And we certainly found it.

If you take only one thing away from this document, it should be this: ***your greatest asset and most powerful tool for communicating to employees is your CEO.*** Employees want to see Ken Lay's face. They want to hear from him and be led by him. Across the board, from associates to VPs, employees agree than ***in the midst of the employee crisis, any major initiative must be led by Ken if it is to have any chance of succeeding.***

You also know too well the impact that the stock price holds on employee morale. The problem is that there is still the nagging belief that the message delivered to "the street" is still different than the message delivered to employees. Yes, as the stock price rises, some employee dissatisfaction will dissipate. But there are also a number of other employee issues that ***are*** definitely under your control. And that is what I want to address here.

OBSERVATIONS

(1) **Instability & Chaos:** We began each focus group by asking for a single word to describe Enron as a place to work. One theme stood out clearly above everything else: chaos, instability and uncertainty. In their own words, *"this can sometimes be a good thing, but most of the time it's dysfunctional and disorganized. The left hand doesn't seem to know what the right hand is doing."* In each group, it was very clear that this sense of instability is not a new phenomenon. Rather, for better and now for worse, it has become a part of the Enron culture.

No observation can illustrate the point more clearly than this: **of the 30 associate and manager-level employees we spoke to, 26 were actively planning or discussing their exit strategies from Enron.** Why? Most felt they had to. But this doesn't mean they *want* to. Of all the various options we offered employees that would better define the "excellence" of Enron, nothing scored better than the following statement: "working to make a place where employees stay for the long-run and build lasting relationships." Your employees simply feel that the possibility of a bad PRC review, having their business unit dissolve underneath them, or just plain bad (or lack of) corporate planning from the top down gives them little choice.

Not surprisingly, your VPs echoed the very same words we heard coming from your associates. They feel that *"there is a sense of chaos in our everyday work. It's a symptom of the lack of an overriding strategy at the top and it's starting to define practically everything."* They see this instability in their day-to-day work and they know that tensions are only getting worse.

(2) **Reorganization:** Each of the four employee groups reacted to the number of *"re-orgs"* in much the same manner – with frustration and rolled eyes. Employees unanimously felt that the never-ending reorganization efforts not only makes communication difficult in the company, but it gives them little or no time to adjust or feel comfortable in their jobs. **Employees do understand the need to restructure the company and adjust to a changing market. But five or six reorganizations in an 18-month period are too many** – to the point that they are a major impediment to job performance.

This sentiment was echoed in all the groups. But it came up most loudly with the directors. *"When you have five or six re-orgs in a year, it just leads to chaos. The managers need at least keep the re-orgs long enough to see results."* In this manner, reorganization and instability are intricately linked.

(3) **Waiting for the Roadmap:** At all levels of the company, employees are looking for a clear vision for the future of Enron and an understanding of their place in it. One of the VPs expressed the view that *"as a company, we're still suffering from small-business syndrome. We're a major corporation still acting like a dot.com startup."* But there is a positive side to this perception. Unanimously, employees want to hear that vision articulated. And they want to hear it from Ken Lay.

None of the employees seemed intimidated by new business opportunities. Most take great pride in the innovation and ingenuity of Enron. But they want to know that there is a "game-plan." Your VPs are particularly concerned that there appears to be no long term thinking, strategy or game plan from the corporate leadership. They want to know that their leaders have a path to follow. And they want their CEO to explain it to them.

(4) **The Corporate Divide:** As a company, Enron recruits a special caliber of employee. People join Enron feeling they are truly the "best of the best." And most of them are. But it took only a matter of minutes to uncover the split between traders and everyone else. It took even less time to elicit the frustration that many employees have from seeing those same deal-makers put into managerial positions without any managerial experience whatsoever.

"*Deal-makers do not necessarily make great leaders.*" This cliché was mentioned verbatim by each level of employee. Across the board, people felt that the deal-maker moved up the corporate ladder regardless of other abilities (or lack of) while implementers were too often forgotten. With a premium being placed on closing deals, most people feel that no one in the corporate leadership truly cares about those charged with executing the deals and making them actually produce profit.

This attitude came up most forcefully with your vice-presidents. It appeared to affect them most personally. They feel that *"there is no apparent reward for trying to be a team leader."* And this only makes their jobs more frustrating. With responsibility for improving morale largely on their shoulders, most feel it is *"utterly unrealistic"* to expect any real progress in the current environment.

(5) **The PRC:** None of this is new to you but the intensity of this reaction cannot be overstated. I could very easily write an entire analysis on just the PRC and its effect on morale. It would start by saying that ***you must be able to understand the PRC as your employees understand it.*** At its heart, the PRC is seen as a ***punitive*** process, not an incentive policy. It is ***not*** viewed as a reward system. It is ***not*** viewed as a meritocracy. It ***is*** viewed as a punishment.

In addition to being seen as a penalty, the PRC is regarded as a highly politicized process that too often depends on the ability of a supervisor to defend his employees against the other members of the committee. As one employee put it: *"it all comes down to how good your manager is at defending you. I was told I had a pretty good score going in, but then the committee bumped me down and there was nothing he could do about it."* The extent of this frustration is best illustrated by our written exercises. **Among associates and managers, the number one step for improving morale is a PRC appeals process for employees who feel their assessments are unfair or biased.**

The PRC process also illustrates the level of disconnect between lower and upper-level employees. Among Associates, most in our groups did not know how the PRC actually worked. And even fewer had heard about the "Laying It On the Line" memo. Almost none of the associates understood the changes to the PRC that were taking place. In associates and managers alike, most wished their supervisors would explain the system better for them. But among directors and vice-presidents, there was a slightly clearer understanding of the process. Still, few were aware of the specific changes underway.

(6) **Trust and the HR Department:** This is an important point because it highlights an interesting disconnect between middle-management and the rest of the staff. Among managers and directors, "an improved HR department where employees can have concerns acted upon without any fear of reprisal" was consistently ranked as a top step for improving morale. Among associates and vice-presidents, it was consistently at the bottom of the list.

Managers expressed repeated annoyance that their conversations with HR representatives were disclosed to others in the company. They were even more frustrated with the HR's inability to respond to problems and return phone calls in a timely manner. But these concerns are generally limited to middle management, perhaps because these are the people who deal most closely with HR on a day-to-day basis.

RECOMMENDATIONS

I offer these initial recommendations without the benefit of a scientific survey. Please accept them as such:

(1) **Take advantage of your most valuable asset – Ken Lay:** When it comes to all the key attributes in delivering a corporate message that your employees will believe and accept -- credibility, confidence and trust -- Ken is your most powerful weapon. A personal commitment from Ken Lay will go further than the entire executive team combined. The VPs told us quite directly that *"any initiative, unless it is headed up and presented to the employees by Ken, will fail...absolutely."*

This is not a warning. It is an opportunity.

Talk about positive change. Talk about employee morale in terms of where you will be five to ten years down the road. Talk about changes in terms of the innovation that has helped Enron in the past. When these words come from Ken, employees will listen.

But whatever you do, be very careful with where and how he focuses his message. The PRC is a classic example of the type of policy he should be staying away from. Employees associate the PRC with Jeff Skilling and the last thing you want is for that negative association to shift to Ken. So pick your messages very carefully.

(2) **At every occasion, do not just write in a way that you will understand. Write so that your employees will understand you:** At first, this may seem like a vague recommendation. But I am putting it up front for a specific reason. It is integral to every other recommendation I can make. And the PRC is a good example of this point. Most of the employees who read the "Laying It On the Line" letter did not understand the changes discussed in it. Unfortunately, it was probably not home run that you were looking for.

Employees need to see side-by-side exactly how the system used to be and what specifically will be different from now on. Simply stated, they need a side-by-side explanation of the old and the new. And they needed to know how those changes will impact their everyday lives. That's what I mean when I say ***communicate in their terms, not yours.***

(3) **Memos must be backed up and reinforced by group discussions with immediate supervisors:** The disconnect between employees and their supervisors is striking up and down the corporate ladder. Focusing again on the PRC, any policy changes need to be followed-up with supervisors holding small staff meetings and explaining the changes that are happening. This is specifically what associates and managers asked for in the focus groups. They are less concerned with town-hall style meetings and Q & A sessions with their vice-presidents. But they do want an in-person explanation whenever major policies are being revised.

(4) **Compensate management for mandatory training sessions:** Associates criticize the lack of training in their supervisors and it is a source of daily frustration. As I have mentioned before, your employees are keenly aware that good deal-makers to not necessarily make good managers. Supervisors admit that what little training is offered is rarely taken seriously. If you want your managers to have the leadership skills necessary for doing their job, then training needs to be made a priority. And executives need to recognize and reward those who treat it as such.

(5) **Bring back employee mentoring and one-on-one "coaching" from senior employees:** Both associates and managers ranked this among their top choices for improving morale. They want greater access to their superiors. And the want the *cut-to-the-chase, no-nonsense* advice that only this sort of training can provide.

Make no mistake, most associates will be happy to get whatever positive "face-time" they can get with their executives. But this is an opportunity to improve both training and communication in the same effort. Directors responded favorably to this idea and ranked it among their higher choices. And many of the VPs remembered similar policies from Enron's past. They expressed little adversity to getting involved and seemed willing to help their lower-level employees.

(6) **Consider a PRC appeals process to ensure fairness and accountability during reviews:** When it comes right down to it, nearly all your employees feel the same about the PRC process. They regard it as a biased system that is too often used for posturing rather than rewarding. If you intend to keep these reviews in place, something needs to be done to make them seem more systematic and less politicized.

This particular recommendation may not be the answer you go with in the end. But it is one that is regarded very favorably among all the employees we spoke to. Changing the criteria for review is seen as the best way to bring better accountability into the actual review process. When your employees regard the PRC system as an unfair tool used for penalizing, then a change needs to be made. And among associates and managers, this was their number one choice for doing so.

(7) **PRC restructuring must integrate the concept of teamwork:** This is a theme that came up several times in each focus group. Finally, the directors we were talking to insisted that we add the concept to one of our written exercises. When we did that, it was consistently ranked as the number one choice for improving employee morale. VPs voted unanimously that they want to see **"a significantly greater recognition of teamwork in the compensation process."**

I realize that this is easier said than done. But employees at all levels feel that their team efforts are not being recognized in the PRC process. Non-traders feel that their abilities to implement and execute deals hold no weight during their performance reviews. Employees want these efforts recognized. They want credit for the teamwork that they believe is integral to Enron's success.

(8) **Devote less time to online forums and e-solutions:** I do not know how much effort currently goes into maintaining these tools. But of the 56 employees we talked to, only 2 picked these efforts as something that demonstrates communication at Enron. My intention is not to attack these solutions. Employees showed no signs of being dissatisfied with their services. But there was little indication that online discussions were making a significant impression in either direction.

Quite frankly, they rarely came up at all. Only when we asked direct questions did employees mention them at all. None of them were ever mentioned by name. So what do they want instead? They want a personal statement from Ken Lay. They are not looking for chat-rooms and message boards. They what to actually see Ken and hear his voice. So some of that effort is probably better spent elsewhere.

(9) **Create a significant PUBLIC effort to revitalize Enron's core values:** I am putting this recommendation last for a specific reason. We touched briefly on this idea during the wrap-up session following the focus groups. Frankly, this is a topic better discussed in person. Employees need something big to show them that things are truly different now at Enron. Too many feel they have been through this routine before. A major action/effort can go very far in showing employees that *real* changes are in effect and that things are really going to be different from now on.

One focus group participant commented that *"I've been in four employee morale discussions and nothing ever seems to change. Why should now be any different?"* You have an opportunity to show employees that their concerns are being taken seriously and acted upon. That sentiment has never existed before. It's a powerful message that will only come from taking an equally powerful stance.

CONCLUSION

After talking to and listening to employees at all levels of the company, I can safely say that I have never seen an employee disconnect so apparent that it actively turns the workplace into a negative environment. I realize that this is a harsh statement to make, but it is exactly what I'm hearing from your employees. And without a solution in place, that negativity tends only to feed on itself and get worse.

Our focus groups showed us quite clearly that your employees are looking for leadership and a message from Ken Lay. They are waiting for that message and a clear plan of action. But they don't want just words. **They want actions to back up those words.** That is why some of my recommendations have been message oriented and others are tough policy solutions.

My goal here is not to make Enron employees love their jobs. But it is important that negativity and frustration be eliminated enough to turn the workplace back into the positive environment it should be. When you achieve that – and you certainly can – you will see performance levels increase across the board. That is why these issues are so important.

As I said in the beginning, these are based solely on what we are hearing in the focus groups. They are based on qualitative results…not polling numbers. The next step is to back up each recommendation with empirical data from the company as a whole. That will allow us to prioritize each step and produce a more concrete course of action.

I look forward to that next step.

A FEW WORDS FROM YOUR VPs
(apologies for the language but these are the exact words)

"Change is good. You can't have too much change. But there needs to be stability in what people do."

"What people are defining as chaos now we would probably have defined as creativity and entrepreneurship a year ago. But the bloom is off the lily right now."

"The chaos is symptom of the lack of an operating strategy. Most people don't think the top leadership have their shit together."

"There is chaos in the company that starts at the top and filters down. There's the feeling that we don't follow our own bullshit."

"It's utterly unrealistic to maintain morale when the people above us don't play the game properly."

"If you look at people who made it to senior levels, they reflect the old Enron. You did it individually and you did it by making deals. We have a legacy of promoting people who were good individually but not necessarily as a team."

"The Enron line, the verbiage that has nothing to do with how it is run. People are rewarded for all the wrong things."

"I tell my guys how great things are. I say all the right things to them but in the back of my mind I know the truth."

"Information travels around here so quickly. When our executive management says one thing and others know the truth, you get a problem. Look at today. People don't feel like they're getting the straight story right now, and the Street is sending back the same message."

* * * * * * * * * * * *

Note: All nine VP participants defined the current employee situation as a crisis.

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #35a

Enron Board Members

Total Compensation - Fiscal Year 2000

Source: Enron Schedule 14A filing - "Definitive Proxy Statement" filed March 27, 2001

Non-employee Board Member	Annual Service Fee	Committee Chair Fee	Est. Meeting Compensation (1)	Other (2)	Total Cash Compensation (3)	Total Stock / Option Value	Total Compensation
1 Robert Belfer	$50,000		$26,250		$76,250	$250,626	$326,876
2 Norman P. Blake, Jr.	50,000		30,000		$80,000	$250,626	$330,626
3 Ronnie C. Chan	50,000		20,000		$70,000	$250,626	$320,626
4 John H. Duncan	50,000	$10,000	32,500		$92,500	$250,626	$343,126
5 Wendy L. Gramm	50,000		21,250		$71,250	$250,626	$321,876
6 Robert K. Jaedicke	50,000	10,000	30,000		$90,000	$250,626	$340,626
7 Charles A. LeMaistre	50,000	10,000	32,500		$92,500	$250,626	$343,126
8 John Mendelsohn	50,000		21,250		$71,250	$250,626	$321,876
9 Jerome Meyer (5)	50,000		21,250		$71,250	$250,626	$321,876
10 Paulo V. Ferraz Pereira	50,000		23,750		$73,750	$250,626	$324,376
11 Frank Savage	50,000		30,000		$80,000	$250,626	$330,626
12 John Urquhart (5)	50,000		17,500	$493,914	$67,500	$250,626	$318,126
13 John Wakeham	50,000	10,000	21,250	$70,000	$81,250	$250,626	$331,876
14 Herbert S. Winokur, Jr.	50,000	10,000	26,250		$86,250	$250,626	$336,876
AVERAGE BOARD MEMBER COMPENSATION (6)					**$78,839**	**$250,626**	**$329,465**

(1) Directors earned $1,250 per meeting attended; Assumes Directors (exc. Chen) attended all scheduled Board and Committee meetings to which they were assigned
(2) "Other" compensation consists of consulting on International Business and Operations (Urquhart) and European Business and Operations (Wakeham)
(3) Exc. "Other" compensation; Directors required to defer 50% of annual service fee to Phantom Stock Plan; remaining fees paid in cash and/or Phantom Stock Units
(4) Stock option grant valuation was based on a Black-Scholes pricing model which was presented by Enron to the Board's Compensation Committee in April 2001
(5) Left Board in 2001; replaced by election of William Powers and Raymond Troubh
(6) Cash calculation compares with $79,107 average as reported in 14A filing; Cash/Stock calculation compares with $330,626 as reported by Compensation Committee

Note: Compensation does not take into account business between Enron and National Tank Company (NATCO), an affiliate of Mr. Winokur, which led to revenues of $370,294 for NATCO. Compensation does not take into account business between Enron and Belco Oil & Gas Corp. (BOGC), an affiliate of Mr. Belfer, which led to a net payment to Enron of $33 million in option and settlement payments

Prepared by the U.S. Senate Permanent Subcommittee on Investigations, May 2002

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #35b

Enron Board of Directors

Estimated Equity Compensation, 1991-2000

Source: Enron Corporation, Executive Compensation Department

Director	Total Value (1) of Options/PSUs (2)	Options Exercised	Deferral Plan Account Balance	TOTAL: Deferral Plan + Options
Belfer	$2,641,458	0	$5,900,657	$8,542,115
Jaedicke	3,273,208	0	1,669,995	4,943,203
LeMaistre	3,273,208	0	262,542	3,535,750
Blake	3,074,433	0	448,768	3,523,201
Duncan	3,273,208	0	170,063	3,443,271
Winokur	2,641,458	0	170,063	2,811,521
Chan	1,508,631	0	356,614	1,865,245
Wakeham	1,679,592	0	149,330	1,828,922
Mendelsohn	585,533	0	112,947	698,480
Ferraz Pereira	192,858	0	38,851	231,709
Savage	170,498	0	46,373	216,871
Gramm (3)	N/A	N/A	N/A	N/A

(1) As of August 21, 2000 - based on Enron share price of $86/share. Value of Enron shares at the current stock price less the cost to exercise options

(2) PSU = Phantom Stock Units; payable in Enron stock upon lapse of vesting restrictions

(3) 2000 Options/Deferred Compensation data not provided

Options and PSUs vest 20% at date of grant and 20% each annual anniversary of the initial grant for five years

Automatic vesting of PSUs upon death or retirement from the Board of Directors; option exercise dates remain firm

Options expire after the tenth anniversary of the Date of Grant

Prepared by the U.S. Senate Permanent Subcommittee on Investigations, May 2002

Ken Lay's Repayment of Cash Loans By Transferring Enron Stock Back to Enron

Date	Action
11/20/00	Repayment of $4 Million loan with stock.
12/28/00	Repayment of $4 Million loan with stock.
02/01/01	Repayment of $4 Million loan with stock.
04/30/01	Repayment of $4 Million loan with stock.
05/14/01	Repayment of $4 Million loan with stock.
05/30/1	Repayment of $4 Million loan with stock.
06/12/01	Repayment of $4 Million loan with stock.
06/19/01	Repayment of $4 Million loan with stock.
06/22/01	Repayment of $4 Million loan with stock.
06/26/01	Repayment of $4 Million loan with stock.
06/27/01	Repayment of $4 Million loan with stock.
06/29/01	Repayment of $4 Million loan with stock.
07/26/01	Repayment of $4 Million loan with stock.
08/20/01	Repayment of $4 Million loan with stock.
08/23/01	Repayment of $4 Million loan with stock.
08/24/01	Repayment of $4 Million loan with stock.
08/30/01	Repayment of $4 Million loan with stock.
09/04/01	Repayment of $4 Million loan with stock.
10/23/01	Repayment of $1.5 Million of $4 Million loan with stock.
10/24/01	Repayment of $1.7 Million of $6 Million loan with stock. (Handwritten note – $3.5 Million advance on same day)
10/25/01	Repayment of $550,000 of $5.8 Million loan with stock.
10/26/01	Repayment of $2.275 Million of $7.25 Million loan with stock.

Prepared by the U.S. Senate Permanent Subcommittee on Investigations, May 2002

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #36a

NOV 19 2000 3:20 PM FR CHAIRMAN'S OFFICE13 853 5313 TO 586 P.02/02

Interoffice
Memorandum

To: To Whom It May Concern

From: Kenneth L. Lay

Department: Executive

Subject: Enron Line of Credit

Date: November 20, 2000

This serves as notice of my intent to repay my outstanding loan balance of $4,000,000 plus interest in full with shares of Enron stock as of this day, November 20, 2000.

Kenneth L.

CC: Elaine Overturf

Mary Joyce

Bob Butts

Rocky Emery

KLL-01111

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #36b

CONFIDENTIAL TREATMENT
REQUESTED BY KENNETH LAY

... CHAIRMAN'S OFFICE 853 5313 TO 558 P.01/01

** JOB STATUS REPORT ** AS OF NOV 20 200 8:02 PM PAGE.01

CHAIRMAN'S OFFICE

JOB #328

	DATE	TIME	TO/FROM	MODE	MIN/SEC	PGS	STATUS
001	11/20	8:01P	713 654 4755	EC--S	00'18"	001	OK

ENRON

Kenneth L. Lay
Chairman and
Chief Executive Officer

Enron Corp.
P.O. Box 1188
Houston, TX 77251-1188
713-853-6773
Fax 713-853-5313
kenneth.lay@enron.com

November 20, 2000

Rocky Emery
Paine Webber, Inc.
Private Client Group
109 N. Post Oak Lane, Suite 150
Houston, TX 77024

RE: Sale of 49,950 shares of Enron Corp. to Company for Repayment of $4,000,000 LOC plus accrued interest through November 20, 2000

Dear Rocky:

This letter is your authority to transfer 49,950 shares of Enron Corp. stock from the stock option award, Grant #5108, with an exercise date of 3/27/00 in Paine Webber Acct. [redacted] to the Enron Corp. Omnibus Paine Webber Acct. [redacted] by Monday, November 27th.

Please call Sherrie Gibson at 713/630-0103 should you have any questions.

Sincerely,

Kenneth Lay

49,950 shares
x $80.25
4,008,487.50
→ + 74.69 Cash
(Loan + Accrued Int.) $4,008,562.19

CC: Elaine Overturf
Pam Butler
Joanne Cortez
Sherrie Gibson

KLL-01115

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #36c

CONFIDENTIAL TREATMENT
REQUESTED BY KENNETH LAY

** TOTAL PAGE.01 **

LexisNexis

The New York Times

March 1, 2002, Friday, Late Edition - Final

SECTION: Section A; Page 1; Column 5; Business/Financial Desk

LENGTH: 1569 words

HEADLINE: ENRON'S MANY STRANDS: EXECUTIVE COMPENSATION;
Enron Paid Huge Bonuses in '01; Experts See a Motive for Cheating

BYLINE: By KURT EICHENWALD

BODY:
The **Enron** Corporation paid its executives huge one-time bonuses last year as a reward for hitting a series of stock-price targets ending in 2000 -- the very time, investigators now say, when corporate officials were improperly inflating the company's profits by as much as a billion dollars.

The bonus payments and other special cash distributions include some $320 million paid just 10 months before **Enron's** collapse into bankruptcy, according to company records. Legal experts said that the payments could provide strong evidence of a motive for the financial machinations that investigators think distorted the company's reported performance and ultimately led to its demise. Without those efforts, the profit and stock price levels required to obtain the money almost certainly would not have been reached. Details of the bonuses -- as well as other payments totaling more than $432 million made to almost 2,000 corporate executives during the two years before **Enron's** collapse -- are described in spreadsheets and data maintained on the corporate computers, information that has been obtained by federal prosecutors. Copies of the spreadsheets were also obtained by The New York Times.

An **Enron** spokesman said that bonus payments at the company were linked to a variety of factors, and did not differ significantly from similar programs offered by other companies. "They were all performance-based programs, which is pretty standard for most corporations," the spokesman, Eric Thode, said.

However, former prosecutors said that given the size of the payments and their direct tie to stock price and earnings performance, the program used by **Enron** was almost certain to find its way into any criminal case that prosecutors might ultimately decide to pursue.

"A strong financial motive is probably the best evidence a prosecutor can get to

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #37

promote or to establish criminal intent," said Stephen Meagher, a former federal prosecutor who handled white-collar cases and who now represents whistle-blowers. "The levels of compensation that we are talking about here would certainly seem to be a powerful incentive for anyone to do anything."

Current and former **Enron** executives said that the one-time payments -- under a program known as the Performance Unit Plan -- had been awaited for several years, and that their distribution ultimately contributed to an exodus of executives throughout the ranks of the company beginning last March and continuing through the early fall.

"Everybody knew that money was coming, and was hanging on for it," one former executive said. "Once it was paid, a lot of people who wanted to move on decided that the time had come."

In addition, executives received large bonuses at almost the same time, with the amount based in large part on the earnings of the company -- figures that investigators for a special committee of the **Enron** board have concluded were inappropriately inflated by company executives.

"This is powerful new evidence of potential fraud," said Eli Gottesdiener, one of several lawyers representing **Enron** workers in suits arising out of losses to their retirement savings as a result of the stock's price collapse. "It shows yet another way -- beyond just the already unusually high volume of insider stock sales -- that top **Enron** insiders concretely and personally benefited from what appears to have been an intentional manipulation of the company's books."

The payments to individuals, according to the data, were huge. For example, Andrew S. Fastow, the former chief financial officer whose complex series of partnerships were used to hide debt and bolster profits, was issued a $350,000 check on Jan. 11, 2001. A few weeks later, on Feb. 5, Mr. Fastow received a check for $1.3 million. That was followed two days later by another payment, of just under $1.4 million.

The records show the final payment to Mr. Fastow was issued twice on the same day, and **Enron** executives said such double listings mean that two checks were issued; that could not be independently verified.

Michael J. Kopper, another executive who worked closely with Mr. Fastow on the partnerships, also received multiple payments early last year. On Feb. 5, a check was issued to him for $800,000, the records show; the next day, a check was cut for just under $603,000. Another check was written to Mr. Kopper on Aug. 10, for $905,000, but that amount was part of a severance agreement, records show.

A third executive whose role is being examined by prosecutors, Ben F. Glisan Jr., received smaller sums. The records show that a check was issued in his name for

$600,000 on Feb. 5, followed by a second check the next day, for $69,223.

Two **Enron** executives who were primarily responsible for reviewing the partnership dealings to protect against conflicts of interest also profited from the reports of strong financial performance made possible by those transactions. Richard A. Causey, the recently dismissed chief accounting officer, was paid $350,000 on Jan. 11, followed by $1 million on Feb. 5; that same day, a second check was issued in his name for $200,000. Richard B. Buy, the chief risk officer, was paid $75,000 on Jan. 11; $900,000 on Feb. 5; and $695,000 on Feb. 7. The records show another $695,000 payment that same day, although again it is not clear if this is a repeat from a data error or the record of an actual check.

Some of the largest payments went to the top officers. Kenneth L. Lay, then the chairman and chief executive, received a check for $3.6 million on Jan. 11, and then one for $7 million on Feb. 5. Jeffrey K. Skilling, then the president and chief operating officer, received $1.9 million on Jan. 11, and $5.6 million on Feb. 5. As required by law, those payments were disclosed in the company's filings with the Securities and Exchange Commission.

The records also describe in detail the $55 million in bonus payments that were handed out to an array of top executives immediately before the company's collapse, to ensure their continued employment at the company. For example, Jeffrey McMahon, the former treasurer and current president and chief operating officer, received a $1.5 million bonus on Nov. 29. At the beginning of 2001, on Feb. 5, he received a check for $1.1 million; the next day, another check was issued to him for just under $700,000.

The long-term payments were made under the Performance Unit Plan, a four-year program that compensated executives with cash if **Enron's** total shareholder return -- a combination of dividends and the increase in the stock price -- ranked sixth or greater compared with a number of alternative investments. Those comparisons included the performance from 1997 through 2000 for 11 industry peers, the Standard & Poor's 500-stock index and 90-day Treasury bills.

Almost every decision that ultimately led to the company's collapse -- including the establishment of a series of partnerships known as LJM2, Chewco and Raptor, which an investigating committee of the board concluded were used to bolster earnings improperly -- was made during the time frame of the Performance Unit Plan.

Before that period, company filings with the S.E.C. show, **Enron's** stock performance was comparatively lackluster. A $100 investment in **Enron** stock in 1995 would have been worth $159.58 by 1998, compared with $210.85 for a $100 investment in the same time period in the S.& P. 500.

But, with many of **Enron's** poor-performing assets being shifted into the partnerships, earnings -- and the stock performance -- became supercharged in the next two years. By 1999, that $100 invested four years before would have been worth $251.60 -- just under the $253.61 value of the investment in the stock index. The following year, as the shakeout in technology stocks began, **Enron** stock vanquished the competition. It would have been worth $474.61, compared with $227.89 for the S.& P. investment.

The differences in performance appear to be reflected in the data on the spreadsheets. With no multiyear bonuses coming due, and with the company's performance in 1999 below that of 2000, the payments that went out for the earlier year are dramatically lower.

The data -- which purport to be all checks issued of more than $50,000 over the last two years -- show only $23 million in such checks issued in 2000. There is the possibility that the data are incomplete, however: the first such check to appear on the spreadsheet was issued on Feb. 3 of that year, meaning either that earlier data are missing or that the payment is indeed the first one of 2000.

The annual bonuses were financed out of a pool established as a percentage of after-tax net income, according to S.E.C. filings. In other words, the smaller the company's reported profits, the less money there was to be distributed in the bonus pool.

A report from the board special committee concluded earlier this month that company executives intentionally manipulated the company's profits, inflating them by almost $1 billion in the year before **Enron's** collapse through byzantine dealings with the partnerships.

According to the report, **Enron** entered into a series of transactions with the partnerships controlled by Mr. Fastow that served no economic purpose other than to manipulate reported profits. An independent third party would never have entered into such dealings, the committee concluded.
http://www.nytimes.com

GRAPHIC: Photo: Jeffery K. Skilling and other top **Enron** executives got big bonuses for bolstering the stock in 2000. (Associated Press)(pg. C6)

Graph: "Big Payments"
The following is a list of **Enron** executives and the bonuses and other payments they received in 2001. Many were for hitting profit and stock price targets during a period when, investigators say, the company inflated profits. Only amounts over $50,000 are shown.

NAME: Kenneth L. Lay
CHECK AMOUNT: $3,600,000
DATE (2001): Jan. 11

day. **Enron** executives said that such multiple appearances indicated separate checks were issued, but because that could not be confirmed, only one check is listed here.

(pg. C6)

LOAD-DATE: March 1, 2002

Big Payments

The following is a list of Enron executives and the bonuses and other payments they received in 2001. Many were for hitting profit and stock price targets during a period when, investigators say, the company inflated profits. Only amounts over $50,000 are shown.

NAME	CHECK AMOUNT	DATE (2001)
Kenneth L. Lay	$3,600,000	Jan. 11
	7,000,000	Feb. 5
Jeffrey K. Skilling	1,920,000	Jan. 11
	5,600,000	Feb. 5
Kenneth Rice	1,750,000	Feb. 5
	1,487,500	Feb. 5
	262,500	Feb. 5
	1,617,011	Feb. 7*
Jeffrey McMahon	1,100,000	Feb. 5
	694,862	Feb. 6
	1,500,000	Nov. 29
John Clifford Baxter	200,000	Jan. 11
	1,200,000	Feb. 5
	1,386,055	Feb. 7
Andrew S. Fastow	350,000	Jan. 11
	1,300,000	Feb. 5
	1,386,055	Feb. 7*
Richard A. Causey	350,000	Jan. 11
	1,000,000	Feb. 5
	200,000	Feb. 5
Michael J. Kopper	800,000	Feb. 5
	602,671	Feb. 6
	905,000	Aug. 10
Richard B. Buy	75,000	Jan. 11
	900,000	Feb. 5
	694,862	Feb. 7*
Mark Haedicke	175,000	Jan. 11
	400,000	Feb. 5*
	808,346	Feb. 6
	141,461	Feb. 6*
	750,000	Nov. 29
James V. Derrick Jr.	484,000	Jan. 11*
	800,000	Feb. 5*
Ben F. Glisan Jr.	600,000	Feb. 5
	69,223	Feb. 6

*Documents show that another check was issued in the same amount on the same day. Enron executives said that such multiple appearances indicated separate checks were issued, but because that could not be confirmed, only one check is listed here.

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

Form 10-K

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1999

16 RELATED PARTY TRANSACTIONS

In June 1999, Enron entered into a series of transactions involving a third party and LJM Cayman, L.P. (LJM). LJM is a private investment company which engages in acquiring or investing in primarily energy-related investments. A senior officer of Enron is the managing member of LJM's general partner. The effect of the transactions was (i) Enron and the third-party amended certain forward contracts to purchase shares of Enron common stock, resulting in Enron having forward contracts to purchase Enron common shares at the market price on that day, (ii) LJM received 6.8 million shares of Enron common stock subject to certain restrictions and (iii) Enron received a note receivable and certain financial instruments hedging an investment held by Enron. Enron recorded the assets received and equity issued at estimated fair value. In connection with the transactions, LJM agreed that the Enron officer would have no pecuniary interest in such Enron common shares and would be restricted from voting on matters related to such shares. LJM repaid the note receivable in December 1999.

LJM2 Co-Investment, L.P. (LJM2) was formed in December 1999 as a private investment company which engages in acquiring or investing in primarily energy-related or communications-related businesses. In the fourth quarter of 1999, LJM2, which has the same general partner as LJM, acquired, directly or indirectly, approximately $360 million of merchant assets and investments from Enron, on which Enron recognized pre-tax gains of approximately $16 million. In December 1999, LJM2 entered into an agreement to acquire Enron's interests in an unconsolidated equity affiliate for approximately $34 million. Additionally, LJM acquired other assets from Enron for $11 million.

At December 31, 1999, JEDI held approximately 12 million shares of Enron Corp. common stock. The value of the Enron Corp. common stock has been hedged. In addition, an officer of Enron has invested in the limited partner of JEDI and from time to time acts as agent on behalf of the limited partner's management.

In 1999, Whitewing acquired approximately $192 million of merchant assets from Enron. Enron recognized no gains or losses in connection with these transactions.

Management believes that the terms of the transactions with related parties are representative of terms that would be negotiated with unrelated third parties.

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #38a

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

Form 10-K

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2000

ENRON CORP.

16 RELATED PARTY TRANSACTIONS

In 2000 and 1999, Enron entered into transactions with limited partnerships (the Related Party) whose general partner's managing member is a senior officer of Enron. The limited partners of the Related Party are unrelated to Enron. Management believes that the terms of the transactions with the Related Party were reasonable compared to those which could have been negotiated with unrelated third parties.

In 2000, Enron entered into transactions with the Related Party to hedge certain merchant investments and other assets. As part of the transactions, Enron (i) contributed to newly-formed entities (the Entities) assets valued at approximately $1.2 billion, including $150 million in Enron notes payable, 3.7 million restricted shares of outstanding Enron common stock and the right to receive up to 18.0 million shares of outstanding Enron common stock in March 2003 (subject to certain conditions) and (ii) transferred to the Entities assets valued at approximately $309 million, including a $50 million note payable and an investment in an entity that indirectly holds warrants convertible into common stock of an Enron equity method investee. In return, Enron received economic interests in the Entities, $309 million in notes receivable, of which $259 million is recorded at Enron's carryover basis of zero, and a special distribution from the Entities in the form of $1.2 billion in notes receivable, subject to changes in the principal for amounts payable by Enron in connection with the execution of additional derivative instruments. Cash in these Entities of $172.6 million is invested in Enron demand notes. In addition, Enron paid $123 million to purchase share-settled options from the Entities on 21.7 million shares of Enron common stock. The Entities paid Enron $10.7 million to terminate the share-settled options on 14.6 million shares of Enron common stock outstanding. In late 2000, Enron entered into share-settled collar arrangements with the Entities on 15.4 million shares of Enron common stock. Such arrangements will be accounted for as equity transactions when settled.

In 2000, Enron entered into derivative transactions with the Entities with a combined notional amount of approximately $2.1 billion to hedge certain merchant investments and other assets. Enron's notes receivable balance was reduced by $36 million as a result of premiums owed on derivative transactions. Enron recognized revenues of approximately $500 million related to the subsequent change in the market value of these derivatives, which offset market value changes of certain merchant investments and price risk management activities. In addition, Enron recognized $44.5 million and $14.1 million of interest income and interest expense, respectively, on the notes receivable from and payable to the Entities.

In 1999, Enron entered into a series of transactions involving a third party and the Related Party. The effect of the transactions was (i) Enron and the third party amended certain forward contracts to purchase shares of Enron common stock, resulting in Enron having forward contracts to purchase Enron common shares at the market price on that day, (ii) the Related Party received 6.8 million shares of Enron common stock subject to certain restrictions and (iii) Enron received a note receivable, which was repaid in December 1999, and certain financial instruments hedging an investment held by Enron. Enron recorded the assets received and equity issued at estimated fair value. In connection with the transactions, the Related Party agreed that the senior officer of Enron would have no pecuniary interest in such Enron common shares and would be restricted from voting on matters related to such shares. In 2000, Enron and the Related Party entered into an agreement to terminate certain financial instruments that had been entered into during 1999. In connection with this agreement, Enron received approximately 3.1 million shares of Enron common stock held by the Related Party. A put option, which was originally entered into in the first quarter of 2000 and gave the Related Party the right to sell shares of Enron common stock to Enron at a strike price of $71.31 per share, was terminated under this agreement. In return, Enron paid approximately $26.8 million to the Related Party.

In 2000, Enron sold a portion of its dark fiber inventory to the Related Party in exchange for $30 million cash and a $70 million note receivable that was subsequently repaid. Enron recognized gross margin of $67 million on the sale.

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #38b

In 2000, the Related Party acquired, through securitizations, approximately $35 million of merchant investments from Enron. In addition, Enron and the Related Party formed partnerships in which Enron contributed cash and assets and the Related Party contributed $17.5 million in cash. Subsequently, Enron sold a portion of its interests in the partnerships through securitizations. See Note 3. Also, Enron contributed a put option to a trust in which the Related Party and Whitewing hold equity and debt interests. At December 31, 2000, the fair value of the put option was a $36 million loss to Enron.

In 1999, the Related Party acquired approximately $371 million, merchant assets and investments and other assets from Enron. Enron recognized pre-tax gains of approximately $16 million related to these transactions. The Related Party also entered into an agreement to acquire Enron's interests in an unconsolidated equity affiliate for approximately $34 million.

UNITED STATES SECURITIES AND EXCHANGE

COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

For the quarterly period ended SEPTEMBER 30, 2001

ENRON CORP.

DESCRIPTION OF RESTATEMENT ITEMS (continued)

On November 8, 2001, Enron released information in a Form 8-K regarding the two LJM limited partnerships formed by Enron's former chief financial officer, his role in the partnerships, the business relationships and transactions between Enron and the partnerships, and the economic results of those transactions as known thus far, and transactions between Enron and certain other Enron employees. Following is the information that was provided.

THE LJM LIMITED PARTNERSHIPS AND TRANSACTIONS WITH ENRON. LJM1 and LJM2 (collectively, LJM) are private investment limited partnerships that were formed in 1999. Andrew S. Fastow was (from inception through July 2001) the managing member of the general partners of LJM1 and LJM2. Enron believes that the LJM partnerships have as limited partners a significant number of institutions and other investors that are not related parties to Enron. These partnerships are a subject of the Special Committee's investigation and it is possible that this investigation will identify additional or different information concerning matters described herein.

Enron, like many other companies, utilizes a variety of structured financings in the ordinary course of its business to access capital or hedge risk. Many of these transactions involve "special purpose entities," or "SPEs." Accounting guidelines allow for the non-consolidation of SPEs with the sponsoring company's financial statements in certain circumstances. Accordingly, certain transactions between the sponsoring company and the SPE may result in gain or loss and/or cash flow being recognized by the sponsor, commonly referred to by financial institutions as "monetizations."

The LJM Partnerships. Enron believes that, under the LJM1 and LJM2 limited partnership agreements (as with many similar agreements in private equity investing), the general partners are entitled to receive a percentage of the profits in excess of their portions of total capital contributed to the partnerships depending upon the performance of the partnerships' investments. Enron also believes that the general partners are entitled to receive annual management fees based in part on formulas that take into account the total amount of capital committed and/or invested by the limited partners. Enron now believes that Mr. Fastow earned in excess of $30 million relating to his LJM management and investment activities. Enron believes that the initial capital commitments of all partners to LJM1 were $16 million, and aggregate capital commitments of all partners to LJM2 were $394 million.

LJM1 and LJM2 were described to the Enron Board of Directors as potential sources of capital to buy assets from Enron, potential equity partners for Enron investments and counterparties to help mitigate risks associated with Enron investments. The Board also was informed that LJM1 and LJM2 intended to transact business with third parties. Prior to approving Mr. Fastow's affiliation with LJM1 and LJM2, the Board determined that Mr. Fastow's participation in the partnerships would not adversely affect the interests of Enron. The Board approved the initial transaction with LJM1 and recognized that Enron could (but was not required to) engage in additional transactions with LJM.

The Board directed that certain controls be put into place relating to Mr. Fastow's involvement with the partnerships and transactions between Enron and the partnerships. The Board required review and approval of each transaction by the Office of the Chairman, the Chief Accounting Officer and the Chief Risk Officer. The Board also recognized the ability of the Chairman of the Board to require Mr. Fastow to resign from the partnerships at any time and directed that the Audit and Compliance Committee conduct annual reviews of transactions between Enron and LJM1 and LJM2 completed during the prior year to ensure the Board's requirements as to controls were met. Whether these controls and procedures were properly implemented is a subject of the Special Committee's investigation.

Enron believes that, as of July 31, 2001, Mr. Fastow sold his interests in LJM1 and LJM2 to Michael J. Kopper, and that Mr. Fastow ceased to be the managing member of LJM's general partners. Prior to that time, Mr. Kopper reported to Mr. Fastow as a non-executive officer of an Enron division. Mr. Kopper resigned from Enron immediately before Enron believes he purchased Mr. Fastow's interests in LJM. Mr. Fastow is no longer working for Enron.

<u>U.S. Senate Permanent Subcommittee on Investigations</u>

EXHIBIT #38c

General Summary of LJM Transactions. From June 1999 through September 2001, Enron and Enron-related entities entered into 24 business relationships in which LJM1 or LJM2 participated. These relationships were of several general types, including: (1) sales of assets by Enron to LJM2 and by LJM2 to Enron; (2) purchases of debt or equity interests by LJM1 or LJM2 in Enron-sponsored SPEs;

(3) purchases of debt or equity interests by LJM1 or LJM2 in Enron affiliates or other entities in which Enron was an investor; (4) purchases of equity investments by LJM1 or LJM2 in SPEs designed to mitigate market risk in Enron's investments; (5) the sale of a call option and a put option by LJM2 on physical assets; and (6) a subordinated loan to LJM2 from an Enron affiliate. The financial results of these transactions are summarized below.

(In Millions)	LJM Investment	Cash and Other Value Received by LJM	LJM Net Cash Flow	Impact of LJM Transaction s on Enron's Restated Pre-Tax Earnings
Nine Months Ended September 30, 2001				
Sales of Assets	$ -	$ -	$ -	$ 0.7
Purchases of Equity/Debt in Enron-Sponsored Special Purpose Entities	-	52.5	52.5	-
Investments in Enron Affiliates	3.4	17.8	14.4	-
Portfolio Special Purpose Entities	-	75.5	75.5	(166.2)(a)
Call Option	-	-	-	-
Transactions with LJM and Other Entities	-	-	-	-
Transaction with LJM and Whitewing	-	-	-	-
Total	$ 3.4	$145.8	$142.4	$(165.5)
Nine Months Ended September 30, 2000				
Sales of Assets	$ 30.0(b)	$ -	$(30.0)	$ 67.0
Purchases of Equity/Debt in Enron-Sponsored Special Purpose Entities	83.3	63.0	(20.3)	-
Investments in Enron Affiliates	64.3	48.9	(15.4)	-

Portfolio Special Purpose Entities	127.1	109.0	(18.1)	48.6(a)
Call Option	8.2	0.9	(7.3)	-
Transactions with LJM and Other Entities	7.5	11.7	4.2	-
Transaction with LJM and Whitewing	-	-	-	-
Total	$320.4	$233.5	$(86.9)	$ 115.6

(a) Enron's pre-tax earnings impact of transactions with LJM2 through the Raptor SPEs was approximately $545 million and $49 million for the nine months ended September 30, 2001 and 2000, respectively, excluding the pre-tax charge described below. During the nine months ended September 30, 2001 and 2000, the Raptor SPEs hedged losses related to Enron investments of $453 million and $35 million, respectively. The 2001 pre-tax earnings amount includes a $710 million pre-tax charge in the quarter ended September 30, 2001 related to the termination of the Raptor SPEs.

(b) This amount excludes a seller financed note from Enron to LJM of approximately $70 million.

(In Millions)	LJM Investment	Cash and Other Value Received by LJM	LJM Net Cash Flow	Impact of LJM Transactions on Enron's Restated Pre-Tax Earnings
2000				
Sales of Assets	$ 30.0(b)	$ 32.4	$ 2.4	$ 86.6
Purchases of Equity/Debt in Enron-Sponsored Special Purpose Entities	100.7	64.4	(36.3)	
Investments in Enron Affiliates	66.5	51.2	(15.3)	

Portfolio Special Purpose Entities	127.1	148.5	21.4	532.0(a)
Call Option	11.3	12.5	1.2	-
Transactions with LJM and Other Entities	7.5	11.7	4.2	-
Transaction with LJM and Whitewing	40.3	-	(40.3)	-
Total	$383.4	$320.7	$(62.7)	$ 618.6
1999				
Sales of Assets	$ -	$ -	$ -	$ -
Purchases of Equity/Debt in Enron-Sponsored Special Purpose Entities	73.8	15.4	(58.4)	2.4
Investments in Enron Affiliates	44.5	1.0	(43.5)	16.9
Portfolio Special Purpose Entities	64.0	95.2(c)	31.2	-
Call Option	-	-	-	-
Transactions with LJM and Other Entities	-	-	-	-
Transaction with LJM and Whitewing	-	38.5	38.5	-
Total	$182.3	$150.1	$(32.2)	$ 19.3
Estimated Fair Value of Existing LJM Investments			$ 43.6(d)	

The estimate was based on a 36% discount off the market price on the date of issuance for shares that were restricted and estimated proceeds received by LJM from the sale of the unrestricted shares.

(d) This amount represents Enron's estimated fair value of the six investments made by LJM that remained outstanding as of September 30, 2001.

Sales of Assets. In June 2000, LJM2 purchased dark fiber optic cable from Enron for a purchase price of $100 million. LJM2 paid Enron $30 million in cash and the balance in an interest-bearing note for $70 million. Enron recognized $67 million in pre-tax earnings in 2000 related to the asset sale. Pursuant to a marketing agreement with LJM2, Enron was compensated $20 million for marketing the fiber to others and other fees for providing operation and maintenance services to LJM2 with respect to the fiber. This arrangement gave Enron profit potential in proceeds received after LJM2 achieved a specified return level. LJM2 sold a portion of the fiber to industry participants for $40 million. LJM2 sold the remaining dark fiber assets for $113 million in December 2000 to an SPE that was formed to acquire the fiber. In December 2000, LJM2 used a portion of the proceeds to pay in full the note and accrued interest owed to Enron. At the time of LJM2's sale of the fiber to the SPE, Enron entered into a derivative contract which served as credit support for the benefit of some of the debt holders of a third-party investor in the SPE. This credit support provided the lender with a specified rate of return. As a result, Enron's credit exposure under the $70 million note was replaced with $61 million in remaining exposure under the derivative contract. LJM2 earned $2.4 million on its resale of the fiber.

Purchases of Equity/Debt in Enron-Sponsored SPEs. Between September 1999 and December 2000, LJM1 or LJM2 purchased equity or debt interests in nine Enron-sponsored SPEs. LJM1 and LJM2 invested $175 million in the nine SPEs. These transactions enabled Enron to monetize assets and generated pre-tax earnings to Enron of $2 million in 1999.

Enron believes that LJM received cash of $15 million, $64 million and $53 million in 1999, 2000 and 2001, respectively, relating to its investments in these entities. In three instances, third-party financial institutions also invested in the entities. LJM invested on the same terms as the third-party investors. In one of these nine transactions, Enron entered into a marketing agreement with LJM2 that provided Enron with the right to market the underlying equity. This arrangement gave Enron profit potential in proceeds received after LJM2 achieved a specified return level. In six of these nine transactions, Enron repurchased all or a portion of the equity and debt initially purchased by LJM.

The SPEs owned, directly or indirectly, a variety of operating and financial assets. For example, Yosemite Securities Trust was a finance entity which facilitated Enron's ability to raise funds in the capital markets through the use of credit-linked notes, a standard financing arrangement offered by investment banks. Osprey Trust is beneficially-owned by a number of financial institutions and is a limited partner in Whitewing Associates, L.P., an Enron unconsolidated affiliate (Whitewing) (see Note 8). Enron is the other partner. Whitewing purchased certain Enron investments for future sale.

In addition, as a result of these transactions, Enron was able to monetize equity interests with investment banks. These monetizations resulted in Enron's recognizing $146 million and $5 million in pre-tax earnings in 2000 and the nine months ended 2001, respectively, and $252 million in cash inflows, all in 2000.

Investment in Enron Affiliates. In two transactions, LJM2 made direct and indirect investments in stock (and warrants convertible into stock) of NPW. NPW initially was a wholly-owned subsidiary of Enron, subsequently included other strategic and financial investors, and in October 2000 became a

public company. NPW is engaged in the retail marketing and sale of natural gas, electricity and other commodities, products and services to residential and small commercial customers in the United States. In January 2000, LJM2 invested $673,000 in Cortez Energy Services LLC (Cortez), a limited liability company formed by Enron and LJM2, and Enron contributed five million shares of NPW stock to Cortez. In July 2000, in a private placement, LJM2 purchased warrants exercisable for NPW stock for $50 million on the same terms as third-party investors. Enron believes that LJM2 still owns these investments.

In September 1999, LJM1 acquired from Enron a 13% equity interest in a company owning a power project in Brazil for $10.8 million, and acquired redeemable preference shares in a related company for $500,000. Enron recognized a $1.7 million loss on the sale of these interests to LJM1. Enron recognized revenues of $65 million, $14 million and $5 million from a commodity contract with the company owning the power project in 1999, 2000 and 2001, respectively. As part of an exclusive marketing arrangement to sell LJM1's equity in the project to third parties and to limit LJM1's return, Enron paid LJM1 a $240,000 fee in May 2000. In 2001, Enron repurchased LJM1's 13% equity interest and the redeemable preference shares for $14.4 million. Enron currently owns this equity interest and consolidates the Brazilian company.

In December 1999, LJM2 paid Enron $30 million for a 75% equity interest in a power project in Poland. Enron recognized a $16 million gain in 1999 on the sale. Enron paid $750,000 to LJM2 as an equity placement fee. In March 2000, Enron repurchased 25% of the equity in the Polish power project from LJM2 for $10.6 million, and Whitewing acquired the remaining 50% from LJM2 for $21.3 million. Enron and Whitewing still own their respective equity interests.

In December 1999, LJM2 acquired a 90% equity interest in an Enron entity with ownership rights to certain natural gas reserves for $3 million. As a result, Enron recognized $3 million in revenue from an existing commodity contract. Subsequently, LJM2 assigned a portion of its ownership interest in the entity to Enron and Whitewing at no cost (to achieve certain after-tax benefits). Enron believes LJM2 continues to own its remaining interest.

Portfolio SPEs. Enron and LJM established a series of SPEs to mitigate market exposures on Enron investments, including investments in NPW, Rhythms NetConnections, Inc., and other technology, energy, and energy-related companies. LJM made $191 million in equity investments in five separate SPEs ($127 million in the four Raptor SPEs and $64 million related to the Rhythms SPE), three of which (Raptor I, II and IV) were also capitalized with Enron stock and derivatives which could have required the future delivery of Enron stock. Raptor III was capitalized with an economic interest in warrants convertible into stock of NPW. The Rhythms SPE is discussed in Note 3 in the "LJM1 Subsidiary Consolidation" section. Enron subsequently engaged in hedging transactions with these SPEs, which included price swap derivatives, call options and put options. The derivatives and options generally were intended to hedge Enron's risk in certain investments having an aggregate notional amount of approximately $1.9 billion.

In the first quarter of 2001, Enron entered into a series of transactions with the Raptor SPEs that could have obligated Enron to issue Enron common stock in the future in exchange for notes receivable. These transactions, along with a transaction entered into in 2000, obligated Enron to deliver up to 30 million shares of Enron common stock to the Raptor SPEs in March 2005.

Such transactions were to have been accounted for as equity transactions when settled.

In the third quarter of 2001, as a result of deterioration in the credit quality of the Raptor SPEs caused by the decline in Enron and NPW's stock price, the increase in Raptor's exposure under derivative contracts with Enron and the increasing dilutive effect on Enron's earnings per share calculation, Enron acquired LJM2's equity in the SPEs for $35 million and terminated the entities.

Enron recognized pre-tax earnings (losses) (as restated) relating to risk management activities of none, $532 million and ($166) million in 1999, 2000 and 2001, respectively, including the effect of a $710 million pre-tax charge recognized in 2001, related to the decline in credit quality and ultimate termination of the Raptor SPEs. During 2000 and the nine months ended September 30, 2001, the Raptor SPEs hedged losses of $501 million and $453 million, respectively. The Rhythms SPE was used to hedge Enron's exposure arising from an investment in the stock of Rhythms NetConnections, Inc. However, it was subsequently determined that it did not meet the criteria to qualify as an adequately capitalized unconsolidated SPE. See Note 3 for a discussion of the restatements related to the Rhythms SPE.

In total, LJM1 and LJM2 invested $191 million and received $319 million (an estimated $95 million of which is non-cash value from the receipt of 3.6 million shares of Enron restricted stock) related to their investments in these five SPEs.

Call Option. In May 2000, Enron purchased a call option from LJM2 on two gas turbines at the same time that LJM2 contracted to purchase the gas turbines from the manufacturer. Enron paid LJM2 $1.2 million for this right during a seven-month period in 2000. The call option gave Enron the right to acquire these turbines from LJM2 at negotiated fair market value, which was $11.3 million. The call option was subsequently assigned from Enron to an Enron-sponsored SPE capitalized by a third-party financial institution. In December 2000, the call option was exercised by the SPE, which acquired the turbines from LJM2 at cost.

Transactions with LJM and Other Entities. Enron sold its contractual right to acquire a gas turbine to a utility for $15.8 million in July 2000. Enron recognized a pre-tax gain of $3.5 million on the transaction. At the same time, the utility entered into a put option agreement with LJM2 relating to the turbine under which the utility paid LJM2 $3.5 million. Subsequently, upon the execution of an engineering, procurement and construction contract with a wholly-owned subsidiary of Enron, the utility assigned the contractual right to acquire the gas turbine to that subsidiary.

In December 1999, Enron sold an equity investment in Enron Nigeria Barge Ltd. to an investment bank and provided seller financing. In June 2000, LJM2 purchased this equity investment directly from the investment bank for $7.5 million and the assumption of the seller-financed note from Enron. In September 2000, LJM2 sold the equity investment to an industry participant for $31.2 million. The proceeds from LJM2's sale were used by LJM2 to repay the principal and interest on the note from Enron in the amount of $23.0 million. The remaining $8.2 million repaid LJM2's $7.5 million purchase price and provided a profit of $700,000 to LJM2.

Transaction between LJM and Whitewing. In December 1999, a wholly-owned subsidiary of Whitewing entered into a $38.5 million credit agreement with

LJM2, the borrower. The loan had a term of one year and carried an interest rate of LIBOR+2.5%. The loan amount (including interest) of $40.3 million was repaid by LJM2 in 2000.

Currently Outstanding LJM2 Transactions. Enron believes that LJM2 currently has interests in six of the investments described above in which LJM2 originally invested $124 million, and that LJM2 has received cash inflows of $27 million from these investments. These investments include $23 million in equity in two Enron-sponsored SPEs, $32.5 million in equity in Osprey Trust, $3 million in equity in an Enron affiliate and $50.7 million in direct equity investments in NPW (representing two transactions).

Enron and LJM2 also entered into various agreements relating to cash management services, employee services and office space provided by Enron to LJM2. In addition, Enron paid LJM2 a management fee for certain transactions, and other transaction fees described above. Enron also reimbursed LJM2 for transaction-related expenses (such as legal and tax fees and other costs) associated with some of the transactions described above.

OTHER EMPLOYEE TRANSACTIONS. From June 1993 through November 1997, an Enron subsidiary was the general partner of JEDI and a third-party, the California Public Employees' Retirement System (CalPERS), was the limited partner. In November 1997, JEDI made a liquidating distribution to CalPERS of $383 million. Concurrently, Chewco purchased a limited partnership interest in JEDI for $383 million, $132 million of which was financed by an interest-bearing loan from JEDI to Chewco, and $240 million of which was borrowed from a third-party financial institution (supported by a guarantee from Enron). The balance of the transaction (approximately $12 million) was principally funded by a contribution from a third party. Enron has subsequently determined that a portion of this contribution was cash collateralized. Based on current information, Enron believes that a non-executive officer of an Enron division, Michael J. Kopper, was an investor in the general partner of Chewco and, at the time of the purchase, also was the manager of the Chewco general partner. These events resulted in inadequate capitalization of Chewco to meet the SPE accounting guidelines. The restatement resulting from the Chewco transaction is discussed in Note 3.

From December 1997 to December 2000, Chewco received distributions of $433 million from JEDI. Among other things, Chewco used a portion of these distributions to make repayments on its JEDI loan and to repay an additional borrowing from the third-party financial institution.

In December 1999, Chewco purchased a $15 million equity interest in Osprey Trust, an Enron-sponsored SPE, from LJM1.

In March 2001, Enron purchased Chewco's limited partnership interest in JEDI for $35 million. In September 2001, Enron paid an additional $2.6 million to Chewco in connection with a tax indemnification agreement between JEDI, Chewco and Enron. Of the total purchase consideration, $26 million was used by Chewco to make a payment on the JEDI loan. Chewco currently has an outstanding balance due on the JEDI loan of $15 million. JEDI is currently a wholly-owned subsidiary of Enron.

Enron now believes that Mr. Kopper also was the controlling partner of a limited partnership that (through another limited partnership) purchased interests in affiliated subsidiaries of LJM1 in March 2000. Enron also now believes that four of the six limited partners of the purchaser were, at the time of the investment, non-executive officers or employees of Enron, and a

fifth limited partner was an entity associated with Mr. Fastow. These officers and employees, and their most recent job titles with Enron, were Ben Glisan, Managing Director and Treasurer of Enron Corp.; Kristina Mordaunt, Managing Director and General Counsel of an Enron division; Kathy Lynn, Vice President of an Enron division; and Anne Yaeger, a non-officer employee. Enron has terminated the employment of Mr. Glisan and Ms. Mordaunt. Ms. Lynn and Ms. Yaeger are no longer associated with Enron and Enron believes they are now associated with LJM2. At the time these individuals invested in the limited partnership, LJM1 had ceased entering into new transactions with Enron. However, some pre-existing investments involving LJM1 and Enron were still in effect, and Enron believes that these investments resulted in distributions or payments to LJM1 and to the limited partnership in which these individuals invested.

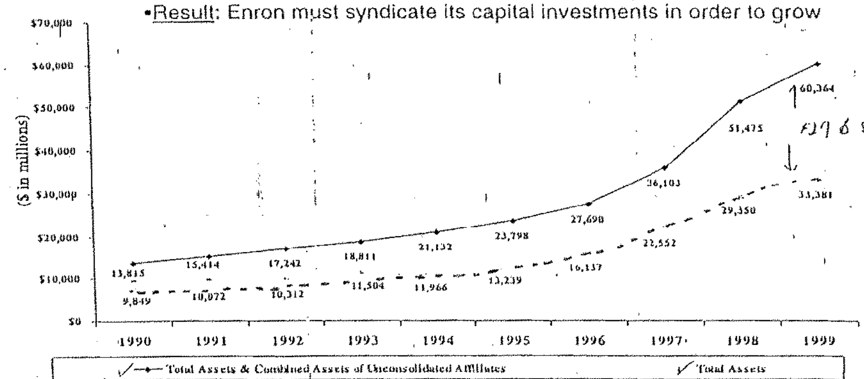
Pursuant to a services agreement among Enron, LJM1 and LJM2, Enron made available to LJM1 and LJM2 a portion of the time of certain of its employees to provide administrative assistance to the general partners of LJM1 and LJM2. Mr. Kopper, Ms. Lynn and Ms. Yaeger, among other Enron employees, were made available to LJM1 or LJM2 from time to time during their employment by Enron.

OTHER TRANSACTIONS. In the first nine months of 2001, Enron received approximately $241.8 million from Whitewing, an unconsolidated equity affiliate, related to monetizations. During the first nine months of 2001, Enron acquired investments from Whitewing for approximately $28.8 million. No gains were recorded by Enron in connection with these transactions. Management believes that the terms of these transactions are reasonable compared to those which could have been negotiated with third parties.

LJM structured to Not be an Enron affiliate

Private Equity Strategy

- Continued significant capital investment by Enron
- Energy and communications investments typically do not generate significant cashflow and earnings for 1-3 years
- Limited cash flow to service additional debt
- Limited earnings to cover dilution of additional equity
- Result: Enron must syndicate its capital investments in order to grow



syndicate or structured transaction

22

Finance Committee Meeting

U.S. Senate Permanent Subcommittee on Investigations
(Source: October 2000, Finance Committee Presentation.)
EXHIBIT #39

EC 000025374

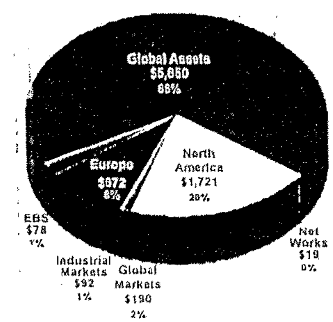
Summary of Investment Portfolio

as of March 31, 2001

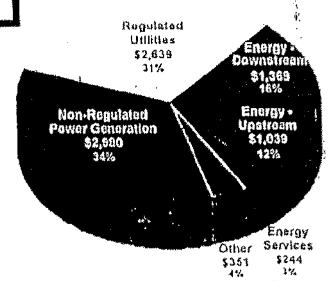
In $MM's

Net Portfolio Carry Value $8,622

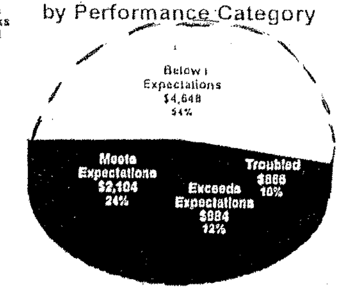
by Business Unit



by Industry



by Performance Category



4-13

U.S. Senate Permanent Subcommittee on Investigations
(Source: April 2001, Finance Committee Presentation.)
EXHIBIT #40

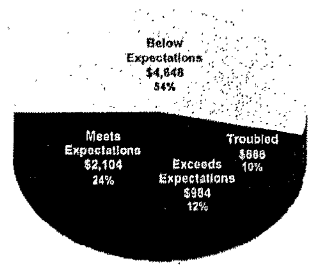
Portfolio Summary

as of March 31, 2001

In $MM's

Net Portfolio Carry Value $8,622

by Performance Category



Exceeds Expectations	
El Paso (East Coast Power proceeds)	261
EcoElectrica, L.P. Equity	203
Vengas	172
Hanover Compressor	138
Meets Expectations	
Mariner	487
TGS – Transportadora De Gas Del Sur	429
Gaspart	193
KCS	171
Below Expectations	
Elektro	1,995
Dabhol Power Company	851
Sarlux S.R.L.	350
SK-Enron	265
Companhia Estaudal De Gas (CEG)	198
Promigas	155
COPEL	120
Bahia Las Minas	102
Troubled	
Cuiaba	432
Trakya	214
Transredes	138

4-14

U.S. Senate Permanent Subcommittee on Investigations

(Source: April 2001, Finance Committee Presentation.)

EXHIBIT #41a

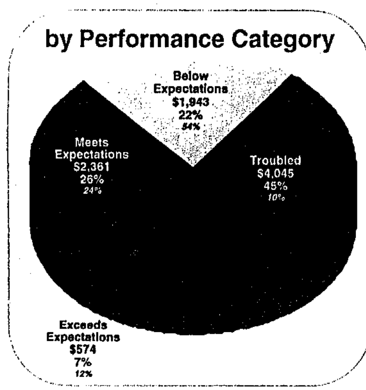
RCO 20884

Portfolio Summary

as of June 30, 2001

In $MM's

Net Portfolio Carry Value $8,923



Exceeds Expectations	
EcoElectrica, L.P. Equity	197
Vengas	142
Meets Expectations	
Mariner	517
Transportadora De Gas Del Sur	451
Dalshowa Forest Products	357
El Paso (East Coast Power Proceeds)	266
Below Expectations	
Sarlux	350
SK – Enron	298
Trakya	216
Gaspart	192
Promigas	159
COPEL	97
Troubled	
Elektro	2,031
Dabhol	849
Cuiaba	537
CEG	199
Transredes	144
Bahia Las Minas	109

Numbers in italics represent comparable amounts at March 31, 2001. *4-16*

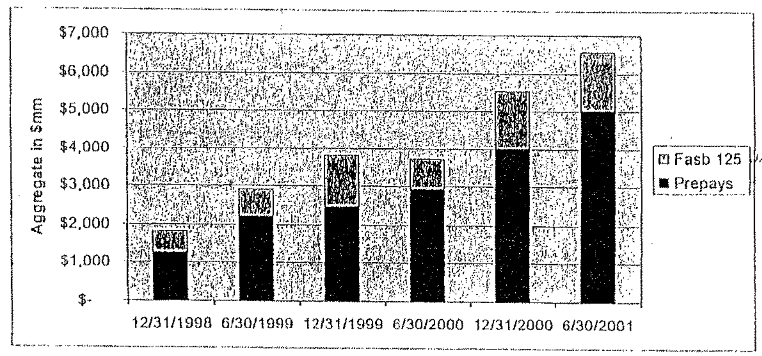
RCO 21467

U.S. Senate Permanent Subcommittee on Investigations
(Source: August 13, 2001, Finance Committee Presentation.)
EXHIBIT #41b

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



2-5

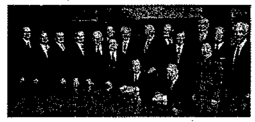
U.S. Senate Permanent Subcommittee on Investigations

(Source: August 2001, Finance Committee Presentation.)

EXHIBIT #42

RCO 21428

Enron Board of Directors – Financial Ties to Enron



Lord John Wakeham	Since 1996, Enron paid a monthly retainer of $6,000 to Lord Wakeham for consulting services, in addition to his Board compensation. In 2000, Enron paid him $72,000. (Enron 2001 Proxy)
John Urquhart John A. Urquhart Associates	Since 1991, Mr. Urquhart provided consulting services to Enron while a Board member. In 2000, Enron paid Mr. Urquhart $493,914 in addition to his Board compensation. (Enron 2001 Proxy)
Herbert Winokur, Director, National Tank Company:	In 1997, 1998, 1999, and 2000, NATCO recorded revenues of $1,035,000, $643,793, $535,682 and $370,294 from sales to Enron subsidiaries of oilfield equipment and services. (Enron 2000, 2001 Proxy)
Dr. Charles LeMaistre, Former President, M.D. Anderson Cancer Center **John Mendelsohn, President, M.D. Anderson Cancer Center**	In the past five years, Enron and Ken Lay donated nearly $600,000 to the M.D. Anderson Cancer Center. In 1993 Enron Foundation pledged $1.5 million to the Cancer Center. (M.D. Anderson)
Dr. Wendy Gramm, Director Regulatory Studies Program of the Mercatus Center at George Mason University	Since 1996, Enron and the Lay Foundation contributed to GMU and the Mercatus Center more than $50,000. (New York Times, 11/30/01)
Robert Belfer, Former Chair and CEO Belco Oil and Gas	Since 1996, Belco and Enron engaged in hedging arrangements worth tens of millions of dollars. (Enron 2001 Proxy) In 1997, Belco bought Enron affiliate Coda Energy. (Enron 1998 Proxy)
Frank Savage, Former Chairman, Alliance Capital Management	Alliance was Enron's largest institutional shareholder with about 43 million shares. (New York Times 1/19/02)
Charls Walker, Principal, Walker/Free Associates, Walker/Potter Associates, American Council for Capital Formation	In 1993-1994, Enron paid Walker/Free and Walker/Potter more than $70,000 for governmental relations and tax consulting in addition to Mr. Walker's Board compensation. (Enron 1994, 1995 Proxy) Enron was also, for more than ten years ending in 2001, a major contributor of up to $50,000 annually to ACCF, a non-profit corporation that lobbies on tax issues and is chaired by Mr. Walker. (Walker interview)

Prepared by U.S. Senate, Permanent Subcommittee on Investigations, May 2002

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #43

THE WALL STREET JOURNAL.

10/18/01 WSJ C1
10/18/01 Wall St. J. C1
2001 WL-WSJ 2879036

The Wall Street Journal

Thursday, October 18, 2001

Partnership Spurs Enron Equity Cut

Vehicle Is Connected To Financial Officer

By Rebecca Smith and John R. Emshwiller
Staff Reporters of The Wall Street Journal

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

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

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

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

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

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

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

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

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

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #44a

10/18/01 WSJ C1

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

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

THE WALL STREET JOURNAL.

10/19/01 WSJ C1
10/19/01 Wall St. J. C1
2001 WL-WSJ 2879138

The Wall Street Journal

Friday, October 19, 2001

Enron CFO's Partnership Had Millions in Profit
By Rebecca Smith and John R. Emshwiller
Staff Reporters of The Wall Street Journal

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

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

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

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

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

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

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

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

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

Mr. Fastow has declined several requests for an interview about LJM2. In late July, he formally severed his ties with LJM2, as a result of what Enron officials said was growing unease by Wall Street analysts and major shareholders. Mr. Fastow has been finance chief of Enron since 1997 and has been

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #44b

10/19/01 WSJ C1

with the firm 11 years, which included extensive work setting up and managing company investments.

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

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

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

TC
AA
2/22/01

INUTES
MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
OCTOBER 7, 2000

Minutes of a meeting of the Board of Directors of Enron Corp. ("Company") held pursuant to due notice at 8:00 a.m., E.D.T., on October 7, 2000 at the Four Seasons Resort, Poinciana III Ballroom, Palm Beach, Florida.

All of the Directors were present, either in person or by telephone conference connection, where each of the participants could hear the comments by the other participants and join in the discussions, as follows:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. John H. Duncan
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Dr. John Mendelsohn
Mr. Jerome J. Meyer
Mr. Paulo Ferraz Pereira
Mr. Frank Savage
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

The meeting began in executive session, during which Messrs. Richard A. Causey, James V. Derrick, Jr., Andrew S. Fastow, Mark E. Koenig, and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company, and Mr. Richard N. Foster of McKinsey & Company, Inc., were also in attendance, either in person or by telephone conference connection, where each of the participants could hear the comments by the other participants and join in the discussions. Messrs. Jeremy M. Blachman, Harold G. Buchanan, Daniel P. Leff, Mark S. Muller, Lou L. Pai, Matthew Scrimshaw, Martin Sunde, Greg L. Whalley and Thomas E. White and Ms. Rosalee T. Fleming, all of the Company or affiliates thereof, joined the meeting in progress as noted.

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WHEREAS, Andrew S. Fastow serves as the Executive Vice President and Chief Financial Officer of the Company;

WHEREAS, Mr. Fastow has the opportunity to participate in the formation of an investment partnership (the "Partnership") that would not be affiliated with the Company;

WHEREAS, it is anticipated that Mr. Fastow will serve as the managing partner/manager of the Partnership;

WHEREAS, it is anticipated that the Partnership will invest in, among other things, energy and communications-related businesses and assets, including businesses and assets of the Company;

WHEREAS, the Partnership, as a potential purchaser of the Company's businesses and assets or as a potential contract counterparty, could provide liquidity, risk management, and other financial benefits to the Company;

WHEREAS, the Board has evaluated two similar previous investment partnerships in which Mr. Fastow has served as the managing partner/manager and has concluded that the existence of such investment partnerships, and Mr. Fastow's involvement therein, have not been adverse to the best interests of the Company; and

WHEREAS, the Office of the Chairman of the Company has determined, for the foregoing reasons, that Mr. Fastow's participation as the managing partner/manager of the Partnership will not adversely affect the interests of the Company;

NOW, THEREFORE, IT IS RESOLVED, that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Code of Ethics (Conflicts of Interests, Investments, and Outside Business Interests of Officers and Employees) that participation of Mr. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and the foregoing resolution.

Revision to the Transaction Approval Process

WHEREAS, the Board of Directors of the Company approved resolutions on October 12, 1998 adopting the Enron Corp. Transaction Approval Process (the "Transaction Approval Process") which provides for (i) a process for review and approval of Capital Expenditures (as defined in the revised policy attached to these minutes) and (ii) a process for prior transactions involving Capital Expenditures to be reviewed for performance and results;

WHEREAS, the Board of Directors of the Company approved amendments to the Transaction Approval Process at meetings held on February 8, 1999, August 10, 1999, February 7th and 8th, 2000, and May 2, 2000; and

WHEREAS, it would be in the best interests of the Company to amend the definitional provisions of the Transaction Approval Process in order to reflect the recent changes in assignments and reorganization of the Company into regional business units and global functions and to reflect amendments to both Approving Units and approval limits with respect to Deal Size;

NOW THEREFORE, IT IS RESOLVED, that the Company revise the Transaction Approval Process to that attached to these minutes and as set forth in these resolutions;

RESOLVED FURTHER, that the revised Transaction Approval Process is adopted and approved, that a copy of the revised policy be attached to the minutes as Exhibit A, and that the persons, officers, and Approving Units identified therein shall perform the responsibilities as specified; for the purposes of this policy a certification by the President, the Chief Financial Officer, the Treasurer, the Chief Risk Officer (or his or her designee), any

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

2001 PROXY STATEMENT

ENRON CORP.

ROBERT A. BELFER, 65
Director since 1983
Mr. Belfer's principal occupation is Chairman and Chief Executive Officer of Belco Oil & Gas Corp., a company formed in 1992. Prior to his resignation in April 1986 from Belco Petroleum Corporation ("BPC"), a wholly owned subsidiary of Enron, Mr. Belfer served as President and then Chairman of BPC.

NORMAN P. BLAKE, JR., 59
Director since 1993
Mr. Blake is the former Chief Executive Officer and Secretary General of the United States Olympic Committee from December 1998 until November 1999. Mr. Blake served as Chairman, President and Chief Executive Officer of the Promus Hotel Corporation when it merged with the Hilton Hotels Corporation. From November 1990 until May 1998, he served as Chairman, President and Chief Executive Officer of Companies. Mr. Blake is also a director of Owens-Corning Corporation.

RONNIE C. CHAN, 51
Director since 1996
For the past ten years, Mr. Chan has been Chairman of Hang Lung Group, comprising three publicly traded Hong Kong-based companies involved in property development, property investment and hotels. Mr. Chan also co-founded and is a director of various companies within Morningside/Springfield Group, which invests in and manages private companies in the manufacturing and service businesses, and engages in financial investments. Mr. Chan is also a director of Standard Chartered Bank plc and Motorola, Inc.

JOHN H. DUNCAN, 73
Director since 1985
Mr. Duncan's principal occupation has been investments since 1990. Mr. Duncan is also a director of EOTT Energy Corp. (the general partner of EOTT Energy Partners, L.P.), Azurix Corp. and Group I Automotive Inc.

WENDY L. GRAMM, 56
Director since 1993
Dr. Gramm is an economist and Director of the Regulatory Studies Program of the Mercatus Center at George Mason University. From February 1988 until January 1993, Dr. Gramm served as Chairman of the Commodity Futures Trading Commission in Washington, D.C. Dr. Gramm is also a director of IBP, inc., State Farm Insurance Co. and Invesco Funds. Dr. Gramm was also a director of the Chicago Mercantile Exchange until December 31, 1999.

KEN L. HARRISON, 58
Director since 1997
Mr. Harrison served as Chairman of the Board and Chief Executive Officer of Portland General Electric Company from 1988 to March 2000, at which time he retired from Portland General Electric Company. Additionally, Mr. Harrison served as Chairman of Enron Communications, Inc. from its inception in 1996 through November 1999 and as a Vice Chairman of Enron from July 1997 to July 1999.

ROBERT K. JAEDICKE, 72
Director since 1985
Dr. Jaedicke is Professor (Emeritus) of Accounting at the Stanford University Graduate School of Business in Stanford, California. He has been on the Stanford University faculty since 1961 and served as Dean from 1983 until 1990. Dr. Jaedicke is also a director of California Water Service Company. Dr. Jaedicke was also a director of GenCorp, Inc. until July 2000 and Boise Cascade Corporation until April 2001.

KENNETH L. LAY, 58
Director since 1985

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Mr. Lay has been Chairman of the Board of Enron since 1986. From 1986 until February 12, 2001, Mr. Lay was also the Chief Executive Officer of Enron. Mr. Lay is also a director of Eli Lilly and Company, Compaq Computer Corporation, EOTT Energy Corp. (the general partner of EOTT Energy Partners, L.P.), i2 Technologies, Inc., NewPower Holdings, Inc. and Azurix Corp.

CHARLES A. LEMAISTRE, 77
Director since 1985
Cancer Center in Houston, Texas and now holds the position of President Emeritus.

JOHN MENDELSOHN, 64
Director since 1999
Since July 1996, Dr. Mendelsohn has served as President of the University of Texas M.D. Anderson Cancer Center. Prior to 1996, Dr. Mendelsohn was Chairman of the Department of Medicine at Memorial Sloan-Kettering Cancer Center in New York. Dr. Mendelsohn is also a director of ImClone Systems, Inc.

JEROME J. MEYER, 63
Director since 1997
For over eight years, Mr. Meyer served as Chairman and Chief Executive Officer of Tektronix, Inc., an electronics manufacturer located in Wilsonville, Oregon. Currently, Mr. Meyer serves as Chairman and as a director of Tektronix, Inc. He is also a director of Standard Insurance Corp. and Centerspan Communications, Inc.

PAULO V. FERRAZ PEREIRA, 46
Director since 1999
Mr. Pereira is Executive Vice President of Group Bozano. Mr. Pereira served for over five years as President and Chief Operating Officer of Meridional Financial Group and Managing Director of Group Bozano. Mr. Pereira is also the former President and Chief Executive Officer of the State Bank of Rio de Janeiro.

FRANK SAVAGE, 62
Director since 1999
Since 1995, Mr. Savage has served as Chairman of Alliance Capital Management International (a Martin Corporation, Alliance Capital Management L. P. and Qualcomm Corp.

JEFFREY K. SKILLING, 47
Director since 1997
Since February 2001, Mr. Skilling has served as President and Chief Executive Officer of Enron. Mr. Skilling served as President and Chief Operating Officer of Enron from January 1997 through February 2001. From August 1990 until December 1996, he served as Chairman and Chief Executive Officer of Enron North America Corp. and its predecessor companies. Mr. Skilling is also a director of Azurix Corp. and the Houston Branch of the Federal Reserve Bank of Dallas.

JOHN A. URQUHART, 72
Director since 1990
Mr. Urquhart serves as Senior Advisor to the Chairman of the Board of Enron. From 1991 to 1998, Mr. Urquhart was a Vice Chairman of Enron. Since August 1991, Mr. Urquhart has also been President of John A. Urquhart Associates, a management consulting firm in Fairfield, Connecticut. He also serves as a director of TECO Energy, Inc., Hubbell, Inc. and The Weir Group, plc and as a board member of and consultant to Catalytica Energy Systems, Inc.

JOHN WAKEHAM, 68
Director since 1994
Lord Wakeham is a retired former U.K. Secretary of State for Energy and Leader of the Houses of Commons and Lords. He served as a Member of Parliament from 1974 until his retirement from the House of Commons in April 1992. Prior to his government service, Lord Wakeham managed a large private practice as a chartered accountant. He is currently Chairman of the Press Complaints Commission in the U.K. and chairman or director of a number of publicly traded U.K. companies. Lord Wakeham is also a director of Azurix Corp.

HERBERT S. WINOKUR, JR., 57
Director since 1985
Mr. Winokur is Chairman and Chief Executive Officer of Capricorn Holdings, Inc. (a private investment company) and Managing General Partner of Capricorn Investors, L.P., Capricorn Investors II, L.P. and Capricorn Investors III, L.P., partnerships concentrating on investments in restructure situations, organized by Mr. Winokur in 1987, 1994 and 1999, respectively. Since 2000, Mr. Winokur has also served as Nonexecutive Chairman of Azurix Corp. Prior to his current appointment, Mr. Winokur was Senior Executive Vice President and a director of Penn Central Corporation, The WMF Group, Ltd., Mrs. Fields' Holding Company, Inc., CCC Information Services Group, Inc. and DynCorp.

Corporate Governance Guidelines
of
The Board of Directors
of
Enron Corp.

The business and affairs of Enron Corp. ("Enron"), an Oregon corporation, are managed under the direction of its Board of Directors (the "Board") in accordance with the provisions of the Oregon Business Corporation Act and Enron's Articles of Incorporation and Bylaws.

In discharging its responsibilities to Enron and to Enron's shareholders, the Board performs the following principal functions:

a) ensuring legal and ethical conduct by Enron and its officers and employees;

(b) selecting, compensating, and evaluating Directors and evaluating Board processes and performance;

(c) selecting, compensating, evaluating, and, when appropriate, replacing senior executives of Enron and ensuring that a succession plan is in place with respect to such senior executives;

(d) approving Enron corporate strategy;

(e) approving major management initiatives; and

(f) providing general oversight of Enron's business.

These activities are performed in cooperation with Enron's Chief Executive Officer and Enron's Chief Operating Officer. The Board also has complete access to other senior management of Enron to ensure that it is supplied with sufficient and adequate information to keep it informed with respect to Enron's business affairs.

Ensuring Legal and Ethical Conduct

The Board approves the Enron Conduct of Business Affairs policy, which imposes on each officer and employee of Enron the duty of conducting the business affairs of Enron in accordance with all applicable laws and in a moral and honest manner. The Audit and Compliance Committee provides reasonable assurance that the provisions of the Enron Conduct of Business Affairs policy are observed.

Criteria to Qualify as an Independent Director

For the purposes of these guidelines, a Director or potential Director is considered to be independent if he or she has been determined by the Nominating and Corporate Governance Committee to be independent after taking into consideration such individual's activities and relationships with

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Enron and any and all other factors that such Committee deems relevant to make such determination.

Number of Directors

The Board believes that its appropriate size is approximately 14 -17 but recognizes that, upon the recommendation of the Nominating and Corporate Governance Committee, it may be appropriate from time to time to modify its size in light of then current circumstances.

Criteria for Selection of Director Candidates

The Board selects Director candidates that it believes will enhance the quality of its deliberations and decisions. The Nominating and Corporate Governance Committee is responsible for establishing criteria for Board membership. It includes among the factors it considers in evaluating potential Director candidates the qualities of strength of character, an inquiring and independent mind, practical wisdom, and mature judgment, and it periodically reviews membership criteria with the Board.

Mix of Independent and Non-Independent Directors

The Board believes that Enron's Chief Executive Officer and Enron's Chief Operating Officer should usually be members of the Board but that a majority of the Board should be comprised of independent Directors. Accordingly, although the Board believes it may be appropriate from time to time for one or more additional officers of Enron to be elected to the Board, no such officer should expect to be elected to the Board simply by virtue of his or her position with Enron.

Selection of Board Members

The Nominating and Corporate Governance Committee, in consultation with Enron's Chief Executive Officer, is responsible for identifying and screening potential Director candidates, for determining their independence, and for recommending them to the Board for its approval. Following the Board's approval of a candidate, the invitation to join the Board is extended to the candidate by Enron's Chief Executive Officer or by such other Director as the Board may specify.

Orientation of New Directors

Each new Director is oriented in respect of Enron and his or her duties as a Director through a program administered by Enron's Corporate Secretary. The program includes background briefings by Enron's Chief Executive Officer, Enron's Chief Operating Officer, and other senior Enron executives.

Director Compensation

Enron management reports periodically to the Compensation and Management Development Committee on the status of the existing Board compensation program relative to the board of directors compensation programs of those companies that are believed to be comparable to Enron. The Compensation and Management Development Committee is responsible for approving for recommendation to the Board annual retainer fees for Directors and meeting fees for Board and Board committee meetings and for approving the terms and awards of stock compensation for Directors.

Lead Director

The Board, upon recommendation of the Nominating and Corporate Governance Committee, designates one of its independent Directors as the Lead Director. The Lead Director is responsible for chairing all executive sessions of the independent Directors and has such other responsibilities as may be assigned to such Director from time to time by the Board.

Assessment of Director Performance and Board Procedures

The Nominating and Corporate Governance Committee is responsible for conducting, on an annual basis, an assessment of the performance of each Director. Such Committee is also responsible for assessing the effectiveness of the processes used by the Board and for recommending to the Board for its consideration any changes to the responsibilities, organization, and membership of existing standing Board committees and the creation of any new standing Board committees.

Director Attendance at Meetings

Each Director is expected to attend all Board meetings and all Board committee meetings of which the Director is a member. The Board recognizes that from time to time conflicts may arise that prevent one or more Directors from attending a regularly scheduled meeting of the Board or one of its committees and that occasionally Board or Board committee meetings may need to be scheduled on short notice when the participation of every member is not possible. The Board expects, however, that each Director will make a concerted effort to keep his or her absences from Board and Board committee meetings to a minimum.

Director Term and Tenure

Each Director is elected annually and holds office until his or her successor has been elected and qualified or until such Director's earlier death, resignation, or removal. There is no limit on the number of terms for which a Director may be elected.

Each Director is expected to volunteer to retire from the Board effective at the Enron Annual Meeting of Shareholders that follows such Director's seventy-second birthday. The Board believes that such Director should not necessarily be required to retire from the Board, but, rather, that the Nominating and Corporate Governance Committee should have the opportunity to assess each individual situation and to make a recommendation to the Board with respect to whether such tendered retirement should be accepted. If the tendered retirement is not accepted, the Director in question is expected to re-tender his or her retirement annually effective as of each succeeding Enron Annual Meeting of Shareholders, and the Nominating and Corporate Governance Committee is expected to recommend to the Board annually whether to accept such tendered retirement.

Each Director who retires from or changes the principal position such individual held when he or she was last elected to the Board is expected to volunteer to resign from the Board as of the date of such retirement or change. The Board believes that such Director should not necessarily be required to resign from the Board, but, rather, that the Nominating and Corporate Governance Committee should have the opportunity to assess each individual situation and to make a recommendation to the Board with respect to whether such tendered resignation should be accepted.

Succession Planning

Enron's Chief Executive Officer is responsible for developing and maintaining a process for advising the Compensation and Management Development Committee and the Board with respect to planning for potential successor Chief Executive Officers and for potential successors to other key senior leadership positions in Enron. Enron's Chief Executive Officer is expected to review this plan with the Compensation and Management Development Committee and the Board at least annually.

Selection of the Chief Executive Officer

The chair of the Compensation and Management Development Committee recommends to the Board an appropriate process pursuant to which a new Chief Executive Officer will be selected. The Board has no required procedure for executing this responsibility because it believes this decision must be made in the way the Board determines to be in the best interest of Enron relative to the circumstances surrounding each such decision.

The Board customarily combines the role of Chairman of the Board with the role of Chief Executive Officer because it believes this practice generally provides the most efficient and effective leadership model for Enron. The Board recognizes, however, that this decision must be examined in the light of the circumstances surrounding each new selection of a Chief Executive Officer.

Evaluation of the Chief Executive Officer

The chair of the Compensation and Management Development Committee is responsible for leading the independent Directors ...ducting periodically (but at least annually) a review of such Committee's assessment of the performance of Enron's Chief Executive Officer.

Equity Ownership by Directors and By Officers

The Board believes that each Director and each officer of Enron should hold a meaningful equity ownership position in Enron. The Compensation and Management Development Committee is responsible for determining and approving from time to time the appropriate requirements of such equity ownership and any exceptions to such requirements.

Executive Sessions of Independent Directors

Meetings of the independent Directors, chaired by the Lead Director, are held following regularly scheduled Board meetings at least annually and more often if any Director requests such a meeting. In addition, the independent Directors meet in executive session when they review the Compensation and Management Development Committee's evaluation of the performance of Enron's Chief Executive Officer.

Frequency of Board Meetings

The Board regularly meets five times annually, in the months of February, May, August, October, and December. In addition, the Board may hold such other meetings as may be required to enable it to discharge its duties.

Selection of Agenda Items for Board Meetings

The Chairman of the Board establishes the agenda for each Board meeting. Each Director may suggest the inclusion of additional items on the agenda. Each Director may raise for discussion at any regular meeting subjects that are not on the meeting's formal agenda.

Director Materials Distributed in Advance

The Board expects that information that is important to a Director's understanding of the business to be discussed at a Board meeting or at a Board committee meeting will be distributed to such Director sufficiently in advance of such meeting to enable such Director to be properly prepared for such meeting.

Corporate Strategy

Periodically (but at least annually) the Board devotes an extended meeting to reviewing with Enron senior executives the strategic issues and opportunities facing Enron.

The Board expects significant corporate strategy decisions to be brought to it in a timely manner for its consideration, discussion, and approval.

Standing Committees of the Board

The Board has established the standing committees described below. The responsibilities of each committee are set forth below in summary form and are more fully described in the charter of each such committee.

Audit and Compliance Committee

The Audit and Compliance Committee serves as the overseer of Enron's financial reporting process, system of internal controls, and corporate compliance process, and it provides reasonable assurance that Enron conducts its business in conformance with appropriate legal and regulatory standards and requirements. Such Committee annually recommends independent auditors for appointment by the Board, reviews the services to be performed by the independent auditors, and exercises oversight of their duties. The Audit and Compliance Committee is comprised solely of independent Directors.

Compensation and Management Development Committee

The Compensation and Management Development Committee establishes and evaluates the compensation of Enron's senior executives to assure that such individuals are compensated in a manner consistent with the stated compensation strategy of Enron, internal equity considerations, competitive practice, and the requirements of applicable regulatory bodies. Such Committee also oversees Enron's employee benefit programs, its Director compensation program, and its management development and succession planning. The Compensation and Management Development Committee is comprised solely of independent Directors.

Executive Committee

The Executive Committee, during the intervals between the meetings of the Board, possesses and exercises all the powers of the Board, subject to the limitations imposed on such Committee by Enron's Bylaws and by the Oregon Business Corporation Act.

Finance Committee

The Finance Committee reviews and makes recommendations to the Board and management on matters concerning both current and long-range financial strategy and planning, including, without limitation, budgets, dividends, equity offerings, debt and other financings, foreign exchange policy, investment policy, and trading limits policy. A majority of the members of the Finance Committee is comprised of Directors who have expertise and experience in economic and financial matters and/or capital markets.

Nominating and Corporate Governance Committee

The Nominating and Corporate Governance Committee reviews criteria for membership on the Board, recommends to the Board candidates for election as Directors, approves for recommendation to the Board the Directors to be selected for membership on Board committees, approves for recommendation to the Board the independent Director to be selected as the

Lead Director, reviews annual Director performance, reviews and makes recommendations to the Board with respect to proposed revisions to the Board's Corporate Governance Guidelines, and monitors compliance with such Guidelines. The Nominating and Corporate Governance Committee is comprised solely of independent Directors.

Review of Board Committee Charters; Changes to Board Committees

Each standing Board committee reviews its charter annually and submits to the Board for its approval any changes in the charter that such committee deems appropriate.

The Board, acting upon the recommendation of the Nominating and Corporate Governance Committee, has the discretion to form a new standing Board committee or to disband a current standing Board committee as it deems appropriate.

Board Committee Chairs

Only an independent Director may serve as a chair of a Board committee. The chair of each Board committee reports to the full Board, whenever appropriate, with respect to those matters considered and acted upon by his or her committee.

Selection of Agenda Items for Board Committee Meetings

The chair of each Board committee, in consultation with the appropriate members of Enron management, develops the committee's agenda.

Each member of a Board committee may suggest the inclusion of additional items on such committee's agenda. In addition, each member of a Board committee may raise for discussion at any regular meeting of such committee subjects that are not on the meeting's formal agenda.

Frequency of Board Committee Meetings; Staff Support

Each Board committee chair, in consultation with the members of his or her committee, determines the frequency of the meetings of such committee. Each committee prepares minutes of its meetings.

Enron management assigns one or more officers to provide and coordinate staff support for each committee.

Attendance of Non-Committee Members at Board Committee Meetings

Each Director has the right to attend all Board committee meetings (except executive sessions of the independent Directors, which can be attended only by the independent Directors), irrespective of whether such Director is a member of such committee, but only those Directors who are members of the committee are entitled to vote on matters considered by the committee.

Should a meeting of the Executive Committee be called to consider issues that, in the opinion of Enron's Chief Executive Officer or Enron's Chief

Operating Officer, would also merit the time and attention of the Directors who are not members of the Executive Committee, every Director will be notified of such meeting and will be entitled to attend it as a non-voting participant.

Meeting fees in respect of a Board committee meeting are paid only to those attending Directors who are members of such committee.

Each Board committee chair may invite members of Enron management to attend such sessions of the committee meetings as the chair deems appropriate.

Assignment and Rotation of Board Committee Members

The Nominating and Corporate Governance Committee, after consultation with the Chairman of the Board and after giving due consideration to the desires of the individual Directors and to the membership criteria of each Board committee, is responsible for recommending to the Board the assignment of Directors to various Board committees and the selection of Board committee chairs.

The Board has no set policy for the regular rotation of committee members or chairs.

Board Interaction with the Media

The Board expects any Director who receives from the media a request for comment with respect to an Enron matter to refer such request to Enron's designated media spokesperson, it being the Board's view that only Enron management or the individual so designated by Enron management should express Enron's positions to the media.

Crisis Management Plan

Enron management has implemented a crisis management plan to facilitate efficient management of a security related incident (such as a kidnapping, extortion, death threat, hijacking, or hostage taking) affecting a Director, officer or employee of Enron. The Audit and Compliance Committee is responsible for periodically reviewing such plan.

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EXHIBIT A

ENRON CORP.

AUDIT AND COMPLIANCE COMMITTEE CHARTER
(As Amended February 12, 2001)

The Board of Directors of Enron Corp. (the "Company") has heretofore constituted and established an Audit and Compliance Committee (the "Committee") with authority, responsibility and specific duties as described in this Audit and Compliance Committee Charter. This document replaces and supersedes in its entirety that certain document adopted by the Board of Directors of the Company on August 9, 1988, entitled "Authority and Responsibility of the Audit and Compliance Committee of the Board of Directors."

Composition

The Committee shall be comprised of three or more directors who, in the opinion of the Board of Directors, as evidenced by its election of such Committee members, have no relationship to the company that may interfere with the exercise of independent judgement as a Committee member. All members of the Committee shall be financially literate or become financially literate within a reasonable period of time after appointment to the Committee, and at least one member of the Committee shall have accounting or related financial management expertise, in each case as interpreted by the Board of Directors.

Mission Statement and Principal Functions

The Committee shall serve as the overseer of the Company's financial reporting process and internal controls. As such, the Committee will have direct access to financial, legal, and other staff and consultants of the Company. Such consultants may assist the Committee in defining its role and responsibilities, consult with Committee members regarding a specific audit or other issues that may arise in the course of the Committee's duties, and conduct independent investigations, studies, or tests. The Committee has the authority to employ such other accountants, attorneys, or consultants to assist the Committee as it deems advisable. The Committee's principal functions shall include:

Ensure Audit Function Independence

- Recommend to the Board of Directors, for subsequent submission to the shareholders of the Company, the firm to engage as the Company's independent auditor, and, if warranted in the discretion of the Committee, recommend to the Board of Directors the termination of that engagement. Furthermore, ensure that the independent auditor is ultimately responsible and accountable to the Committee and the Board of Directors as representatives of the Company's shareholders.
- Review the independent auditor's compensation, the terms of its engagement, and its independence. On a periodic basis, the Committee should obtain a formal written statement from the independent auditors delineating all relationships between the auditor and the Company and hold active discussions with the auditor with respect to any disclosed relationships or services that may impact the objectivity or independence of the auditor. In response to the report and if necessary, the Committee should take action or recommend that the Board take appropriate action, to satisfy itself of the outside accountant's independence. In addition, review the planning of the independent audit, the performance of the independent auditors, and review any special audit procedures required.

- Serve as a channel of communication between the independent auditor and the Board of Directors and between the executive responsible for the audit functions provided internally or by contract and the Board of Directors of the Company.
- Review the Company's annual financial statements and any significant disputes between management and the independent auditor that arose in connection with the preparation of those financial statements, including any restrictions on the scope of work or access to required information.

Assess Internal Controls and Quality of Financial Reporting

- Discuss with the independent auditor information relating to the auditor's judgments about the quality of the Company's accounting principles, including such matters as the consistency of application of the Company's accounting policies, as well as the clarity and completeness of the Company's accounting information contained in the financial statements and related disclosures filed with the Securities and Exchange Commission and distributed to the Company's shareholders.
- Review, in consultation with the independent auditor and the executive having responsibility for the internal and contract audit functions, the adequacy of the Company's internal financial controls. Among other things, determine whether these controls provide reasonable assurance that the Company's publicly reported financial statements are presented fairly in conformity with generally accepted accounting principles.
- Review the Company's electronic data processing procedures and controls on a periodic basis. Also review any deficiencies noted by the independent auditor in such electronic data processing procedures and control.
- Approve major changes and other major questions of choice regarding the appropriate accounting principles and practices to be followed when preparing the Company's financial statements for the purpose of making recommendations to the Board of Directors as necessary.

Review Financial Statements

- Review financial statements included in the Annual Report to Shareholders, footnotes, and management commentaries, Form 10-K filings made with the Securities and Exchange Commission prior to release of such statements and filings. In addition, review findings of any examinations by regulatory agencies, such as the Securities and Exchange Commission.
- Publish a written report in the annual proxy statement indicating that (a) the Committee has reviewed and discussed the financial statements with management, (b) the Committee has discussed the quality of the Company's accounting principles as applied in its financial reporting, (c) the Committee has received the written report from the independent auditors delineating all relationships between the auditor and the Company, (d) the Committee has discussed with the independent auditors their independence and taken or recommended action, if necessary, related to independence concerns and (e) nothing has come to the Committee's attention that would cause them to believe that the financial statements included in the Annual Report on Form 10-K contain an untrue statement or omit a material fact, and thus recommend to the Board that the audited financial statements be included in the Company's Annual Report on Form 10-K. Furthermore, the Committee will take action where necessary to be in compliance with all applicable rules and regulations.

- Review with management and the independent auditor each quarterly Form 10-Q prior to its filing. The Chair of the Committee may represent the entire Committee for purposes of this review.

- Review with management the Company's policies and practices for communications with analysts.

Other

- Approve for recommendation to the Board of Directors the Company's policies and procedures regarding compliance with the law and with significant Company policies, including but not limited to, codes of conduct expressing principles of business ethics, legal compliance, the Foreign Corrupt Practices Act, and other matters relating to business conduct, and programs of legal compliance designed to prevent and detect violations of law.

- Review with the general counsel any legal and regulatory matters that may have a material effect on the Company's financial statements, compliance policies, and programs.

- If necessary, institute special investigations and, if appropriate, hire special counsel or experts to assist.

- Perform other oversight duties and responsibilities as may be assigned to the Committee, from time to time, by the Board of Directors of the Company and/or the Chairman of the Board of Directors.

- Review and, to the extent that the Committee determines is appropriate, update this Charter periodically, at least annually, as conditions dictate.

Meetings

The Committee shall meet at least four times annually, or more frequently as circumstances dictate. Meetings may be called by the Chairman of the Committee and/or management of the Company. In addition, the Committee will make itself available to the independent auditors of the Company as requested by such independent auditors. All meetings of the Committee shall be held pursuant to the Bylaws of the Company with regard to notice and waiver thereof, and written minutes of each meeting shall be duly filed in the Company records. Reports of meetings for the Committee shall be made to the Board of Directors approved by the Committee. On a regular basis the Committee will meet with the independent auditor independent of management, and it will meet with Company management independent of the independent auditor on a regular basis.

While the Audit and Compliance Committee has the responsibility and power set forth in this charter, it is not the duty of the Audit and Compliance Committee to plan or conduct audits or to determine that the Company's financial statements are complete and accurate and are in accordance with generally accepted accounting principles. This is the responsibility of management and/or the independent auditors.

ENRON CORP.

FINANCE COMMITTEE CHARTER

The Board of Directors of Enron Corp. (the "Company") has heretofore constituted and established a Finance Committee (the "Committee") with authority, responsibility, and specific duties as described in this Finance Committee Charter.

COMPOSITION

The Committee shall be composed of Directors who have expertise and experience in economic and financial matters and/or capital markets.

MISSION STATEMENT AND PRINCIPAL FUNCTIONS

The Committee shall serve as a monitor of the Company's financial activities. The Committee's principal functions shall include:

- Review and approve for recommendation to the Board of Directors, if appropriate, equity offerings to be undertaken by the Company and its subsidiaries and affiliates.

- Review and approve for recommendation to the Board, if appropriate, specific debt and other financings to be undertaken by the Company and its subsidiaries and affiliates.

- Review the Company's activities with credit rating agencies.

- Monitor on an ongoing basis the Company's key financial ratios, including the debt to total capitalization ratio, for both consolidated and unconsolitated obligations.

- Review on a periodic basis the Company's policy governing approval levels for capital expenditures and the Company's financial plan to fund approved capital expenditures.

- Review and approve for recommendation to the Board the Company's Foreign Exchange Policy and amendments thereto.

U.S. Senate Permanent Subcommittee on Investigations
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FS-00650

- Review and approve for recommendation to the Board the Company's Investment Policy and amendments thereto.

- Review and approve for recommendation to the Board changes in the rate of the dividend.

- Monitor the Company's exposure under outstanding letters of indemnity, letters of credit, and corporate guaranties, and review and approve for recommendation to the Board of Directors, if appropriate, the Company's policies with regard thereto.

- Review, no less than annually, fees paid to and relationships with banks, investment banks, and other financial advisors.

- Review no less than annually, the assets and performance of the Company's retirement plan.

- Perform such other oversight duties and responsibilities as may be assigned to the Committee, from time to time, by the Board of Directors and/or the Chairman of the Board of Directors.

MEETINGS

The Committee will meet as often as necessary to carry out its responsibilities, but no less than twice annually. Meetings may be called by the Chairman of the Committee and/or management of the Company. All meetings of the Committee shall be held pursuant to the Bylaws of the Company with regard to notice and waiver thereof, and written minutes of each meeting shall be duly filed in the Company records. Reports of meetings of the Committee shall be made to the Board of Directors at its next regularly scheduled meeting following the Committee meeting accompanied by any recommendations to the Board of Directors approved by the Committee.

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ENRON CORP.

COMPENSATION COMMITTEE CHARTER

The Board of Directors of Enron Corp. (the "Company") has constituted and established a Compensation Committee (the "Committee") with authority, responsibility, and specific duties as described in this Compensation Committee Charter.

COMPOSITION

The Committee shall consist of directors who are independent of management and free from any relationship that, in the opinion of the Board of Directors, as evidenced by its election of such Committee members, would interfere with the exercise of independent judgment as a Committee member.

MISSION STATEMENT AND PRINCIPAL FUNCTIONS

The Committee's basic responsibility is to assure that the senior executives of the Company and its wholly-owned affiliates are compensated effectively in a manner consistent with the stated compensation strategy of the Company, internal equity considerations, competitive practice, and the requirements of the appropriate regulatory bodies. The Committee shall also communicate to shareholders the Company's compensation policies and the reasoning behind such policies as required by the Securities and Exchange Commission. More specifically, the Committee shall be responsible for the following:

- Review from time to time and approve the Company's stated compensation strategy to ensure that management is rewarded appropriately for its contributions to Company growth and profitability and that the executive compensation strategy supports organization objectives and shareholder interests.

- Review annually and determine the individual elements of total compensation for the Chief Executive Officer and communicate in the annual Board Compensation Committee Report to shareholders the factors and criteria on which the Chief Executive Officer's compensation for the last year was based, including the relationship of the Company's performance to the Chief Executive Officer's compensation.

- Review and approve the individual elements of total compensation for the senior management of the Company other than the Chief Executive Officer and communicate in the annual Board Compensation Committee Report to shareholders the specific relationship of corporate performance to executive compensation.

- Assure that the Company's Executive Incentive Compensation Program, including the annual and long-term incentive plans, is administered in a manner consistent with the Company's compensation strategy as to participation, target annual incentive awards, corporate financial goals, actual awards paid to senior management, and total funds reserved for payment under the compensation plans.

- Approve, subject, where appropriate, to submission to shareholders, all new equity-related incentive plans for senior management.

- Approve annual retainer and meeting fees for Board of Directors and committees of the Board and fix the terms and awards of stock compensation for members of the Board.

- Approve revisions to the Company's executive salary range structure, annual salary increase guidelines, and review compensation arrangements among members of the Company's Management Committee.

- Review with the Chief Executive Officer matters relating to management succession, including, but not limited to, compensation.

- Review the Company's employee benefit programs and approve changes subject, where appropriate, to shareholder or Board of Director approval.

- If appropriate, hire experts in the field of executive compensation to assist the Committee with its reviews.

- Such other duties and responsibilities as may be assigned to the Committee, from time to time, by the Board of Directors of the Company and/or the Chairman of the Board of Directors, or as designated in plan documents.

MEETINGS

The Committee will meet as often as necessary to carry out its responsibilities. Meetings may be called by the Chairman of the Committee and/or management of the Company. All meetings of the Committee shall be held pursuant to the Bylaws of the Company with regard to notice and waiver thereof, and written minutes of each meeting shall be duly filed in the Company records. Reports of meetings of the Committee shall be made to the Board of Directors at its next regularly scheduled meeting following the Committee meeting accompanied by any recommendations to the Board of Directors approved by the Committee.

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ENRON CORP.

NOMINATING COMMITTEE CHARTER
(Revised October 10, 1995)

The Board of Directors of Enron Corp. (the "Company") has constituted and established a Nominating Committee (the "Committee") with authority, responsibility, and specific duties as described in this Nominating Committee Charter. This document replaces and supersedes in its entirety that certain document adopted by the Board of Directors of the Company in December, 1988, entitled "Rules of Governance."

COMPOSITION

The Committee shall be comprised of directors who are independent of management and free from any relationship that, in the opinion of the Board of Directors, as evidenced by its election of such Committee members, would interfere with the exercise of independent judgment as a Committee member.

MISSION STATEMENT AND PRINCIPAL FUNCTIONS

The Committee shall have oversight for recruiting and recommending candidates for election to the Board of Directors, with advice and consent of the Company's Chairman and Chief Executive Officer; review of criteria for board membership against current needs of the Board to ensure timeliness of the criteria; and review of annual director performance evaluations and formulation of recommendations to the Board of Directors with regard thereto. Specific duties expressly included under the foregoing mission statement follow:

- Approve for recommendation to the Board of Directors the slate of nominees for directors to be elected by the shareholders (and any directors to be elected by the Board to fill vacancies). Recognizing that election to the Board of Directors does not ensure tenure to mandatory retirement age, the Committee will thoughtfully review the performance and contribution of each director coming to the end of his or her term before deciding whether to recommend reelection. In addition, the Committee will carefully review the qualifications of any proposed new directors.

- Approve for recommendation to the Board of Directors the directors to be selected for membership on the various Board committees.

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- Recommend responsibilities, organization, and membership of existing and creation of new Board committees; excluding, however, special purpose committees established by the Board of Directors.

- Review and recommend from time to time to the Board of Directors amendments in Board actions relating to number of Directors and mandatory retirement age.

- Such other duties and responsibilities as may be assigned to the Committee from time to time by the Board of Directors.

CRITERIA FOR BOARD MEMBERSHIP

The principal qualities of an effective corporate director include strength of character, an inquiring and independent mind, practical wisdom, and mature judgment. In addition to these basic attributes, the Committee will establish particular criteria for board membership. These may include individual qualifications such as technical skills, career specialization, geographical representation, or specific backgrounds. Under the Committee's guidance, such criteria may change from time to time. The Committee will determine the independence of current and prospective Board members prior to recommending a candidate to the Board of Directors. Each director or director-candidate must have a holding in Enron Corp. stock.

MEETINGS

The Committee will meet as often as necessary to carry out its responsibilities. Meetings may be called by the Chairman of the Committee and/or management of the Company. All meetings of the Committee shall be held pursuant to the Bylaws of the company with regard to notice and waiver thereof, and written minutes of each meeting shall be duly filed in the Company records. Reports of meetings of the Committee shall be made to the Board of Directors at its next regularly scheduled meeting following the Committee meeting accompanied by any recommendations to the Board of Directors approved by the Committee.

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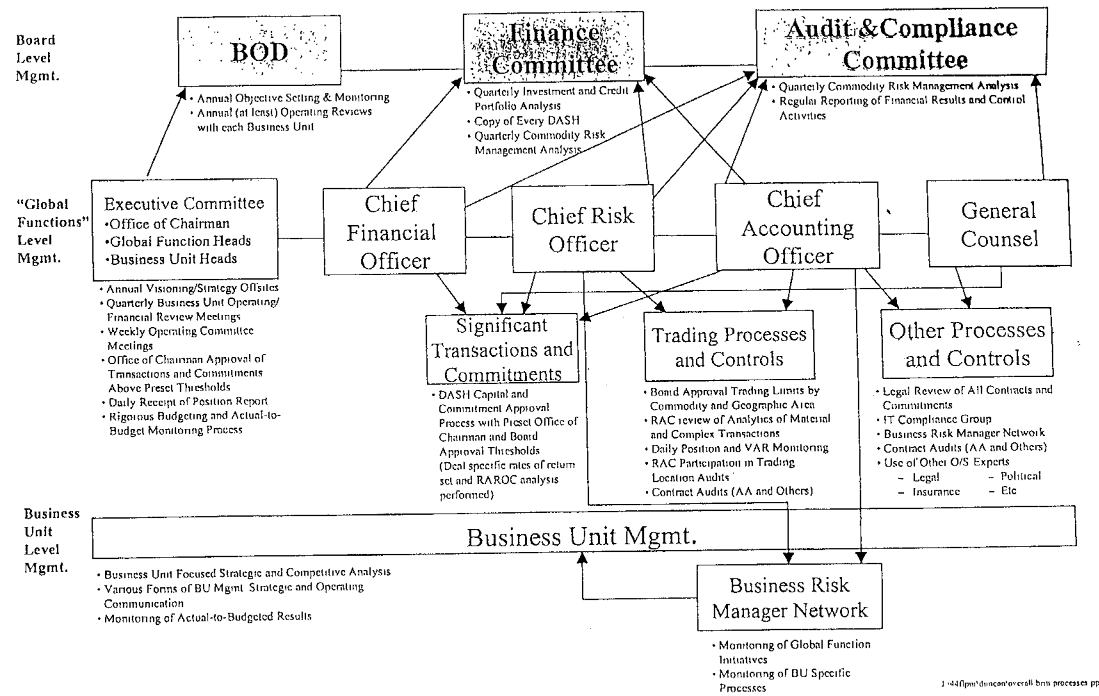
Enron Corp.
Business Risk Management
Process Overview



AAHEC(2)02114.11

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #48

Audit and Compliance Committee
Calendar of 2001 Activities

	Scheduled Meetings				
	February	**May**	**August**	**October**	**December**
I. Audit Committee Composition and Meetings					
• Assess independence and financial literacy of audit committee, submit written affirmation to NYSE		X			
• Review charter (publish in proxy every 3 years)	X				
• Audit Committee Chair to approve meeting agenda	X	X	X	X	X
• Executive session with auditors, internal audit, management, committee	X	*	*	*	*
• Maintain minutes and report to Board	X	X	X	X	X
II. Audit Committee Responsibilities and Duties					
• Recommend appointment of auditors	X				
• Approve audit fees		X			
• Discuss auditor independence, obtain written statement of all relationships	X		X		
• Review plans for financial statement audit		X			
• Review annual financial statements prior to release– discuss with mgmt, auditors	X				
• Discuss quality of accounting principles-approve major changes	X	*	*	*	*
• Review adequacy of financial and EDP internal controls					X
• Review internal control plan	X				
• Discuss results of year-end audit and other matters required by SAS 61	X				
• Prepare report to shareholders to be included in the annual proxy	X				
• Review quarterly results and findings prior to filing	X	X	X	X	
• Review policies and practices for management's communications with analysts	X				
• Review/Approve for recommendation to the Board policies and procedures regarding compliance with laws and significant policy				X	
• Review credit and market risk with RAC	X	X	X	X	X
• Review legal matters with general counsel	X	*	*	*	*
• Conduct special investigations, studies or tests	*	*	*	*	*
• Review director and officer use of aircraft	X				

X = Recommended Timing
* = As Needed

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U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #49

ARTHUR ANDERSEN

ENRON

Report to the Audit Committee Of the Board of Directors

August 2000

AASCGA(TX)000324

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #50

Blue Ribbon Committee

Review of Key Recommendation Points

Key Points	Enron Status (all will require ongoing activities or monitoring)
Committee Independence:	
• Require minimum of three directors, all independent, and at least one financial expert	• Complies
• Monitor director independence	• Complies
Committee Accountability:	
• Reassess adequacy of written charter on annual basis	• Complies
• Continue required disclosures in the proxy statement regarding the charter and the committee's satisfaction of its responsibilities as stated in the charter	• Effective for proxy related to year ended December 31, 2000
Auditor Independence:	
• Perpetuate understanding that external auditor is ultimately accountable to committee and Board of Directors	• Complies
• Continue obtaining written statement from the auditor listing all relationships between the auditor and the company, discuss such relationships with auditor and ensure the auditor's independence	• Complies; expanded discussion related to 2000 included herein
Committee Effectiveness:	
• Require auditor to discuss quality, not just acceptability, of financial reporting with committee	• Complies
• Require formal audit committee report in proxy of: (a) discussions with management and auditors regarding the quality of the financial statements; and (b) that financial statements comply with GAAP and are fairly presented	• Effective for proxy related to year ended December 31, 2000
• Require timely interim (SAS 71) financial review by auditors	• Complies
• Require auditor to discuss interim reporting with committee prior to release of financial information	• Complies

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Application of Mark-to-Market and Fair Value Accounting

October 11, 1999

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Comparison with traditional model

Accrual

- Carried on the balance sheet at historical cost (zero for most commodity contracts)
- Earnings realized over the life of the asset or upon ultimate sale
- Changes in value only recorded in certain scenarios (e.g. loss contracts, impairments etc.)

Mark-to-market/ Fair Value

- Carried on the balance sheet at fair value
- Fair value recorded at origination - changes in fair value recorded through income statement
- Requires continuous revaluation of asset and liabilities

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JW-00780

Authority for Application

- Correspondence with the SEC during 1991 and 1992 regarding application of mark-to-market accounting for Enron's natural gas trading activities (Broker-Dealer rules)

- In 1995, Enron affiliate JEDI adopts fair value accounting under the investment company rules. Later expanded to Enron subsidiaries which are investments companies

- Enron registers as a Power Marketer with the FERC and applies mark-to-market accounting to power trading operations consistent with natural gas trading operations

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Authority for Application (cont.)

- In November 1998, EITF issue No. 98-10 "Accounting for Energy Trading and Risk Management Activities" requires energy trading companies (as defined) to carry contracts at fair value

- In June 1998, the FASB issued Statement 133 which defines a derivative broadly and requires that instrument to be carried at fair value (application pending)

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Current State - Trading and Investing

Trading Operations	Investing Operations
Natural Gas	Public Equities
Power	Private Equities
Liquids	Structured Debt
Securities Trading	Convertible Securities
Interest Rate	
Foreign Exchange	
Emerging Products	
Weather Derivatives	
Pulp and Paper	
Coal	

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Operations not using Value Based Accounting

- Portland General Electric
- Pipeline Operations
- Enron Communications
- Wholesale Power Plant Construction and Operations (US & International)
- Corporate Activities

(all may be affected by Statement 133)

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Key Valuation Drivers -Trading

Drivers

- Forward price of the underlying (i.e. power, natural gas, etc.)
- Volatility of the underlying (options)
- Basis differentials due to location and quality
- Interest rates
- Counterparty credit
- Liquidity of the market
- Other deal specific valuation reserves

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Key Valuation Drivers - Investing

Drivers

- Quoted market prices when available

  or

- Discounted cash flow models considering
  - Risk adjusted discount rate for the investment
  - Expected future growth rate
  - Assumed timing of disposition
  - Comparable market multiples

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Continuing Evolution

Scope

- Illiquid markets
- Long-dated positions in mature markets
- EES bundled contracts
- Deregulation of retail power
- Bandwith trading

Application Issues

- FASB focus on financial instruments
- Development of authoritative literature

ENRON

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Comp Committee

Mary K. Joyce
Vice President
Executive Compensation

Enron Corp.
1400 Smith Street
Houston, TX 77002
713-853-3993
Fax 713-646-2210

April 13, 2001

Dr. Charles A. LeMaistre, Chairman,
Compensation & Management Development Committee

Mr. Norman P. Blake, Jr.
Mr. John H. Duncan
Dr. Robert K. Jaedicke
Mr. Frank Savage

Subject: Potential Proxy Q & As

Dear Sirs:

Attached are answers for potential questions that could arise relating to the Enron 2001 Proxy. Dr. LeMaistre thought these would be of interest to each of you. As additional Q&As are drafted, they will be distributed.

As always, if you have any questions, please call Pam Butler (713) 853-5816 or me (713) 853-3993.

Very truly yours,

Mary K Joyce

Attachment

cc: Ken Lay
Jeff Skilling
Steve Kean
Pam Butler

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #52

2000
TSR ↑ 88%
Recurring net income ↑ 28%
E.P.S. ↑ 25%

Performance Based Compensation

91 - 2000
Shareholder Return = 1415%
S + P 383%

CONFIDENTIAL
FOR ENRON BOARD OF DIRECTORS,
PUBLIC RELATIONS, INVESTOR RELATIONS & HR USE ONLY
POTENTIAL QUESTIONS - ENRON PROXY 2001

1. *The proxy tables do not show a total value for the executives' 2000 compensation. Please indicate the total compensation for each of these executives and which items are included in the total.*

The following charts show the total compensation in 2000, 1999 and 1998 for each executive:

Performance sets size of pool (funded as a % of Recurring after-tax Recurring net income
ind. performance vis à vis pre-established earnings targets

2000 Total Compensation

Short-Term

Median of Marketplace

Executive	~~Salary~~	Bonus	Other Annual Compensation	All Other Compensation	Total Annual Compensation
Mr. Lay	$1,300,000	$7,000,000	$381,551	$857,316	$9,538,867
Mr. Skilling	$850,000	$5,600,000	$47,403	$120,825	$6,618,228
Mr. Frevert	$520,000	$2,000,000	$2,603,541	$447,584	$5,571,125
Mr. Rice	$420,000	$1,750,000	$81,333	$16,482	$2,267,815
Mr. Horton	$520,000	$1,200,000	$15,600	$11,934	$1,747,534

Long-Term

Before payout: S.O. increase in stock price
R.S. re. market competitiveness @ 75%

Executive	Restricted Stock Awards	LTIP ~~Payouts~~	Value of Options Exercised	Total Long-Term Compensation	Total Compensation	Percent At Risk*
Mr. Lay	$7,500,025	$1,218,750	$123,399,478	$132,118,253	$141,657,120	98.2%
Mr. Skilling	$3,500,037	$0	$62,484,460	$65,984,497	$72,602,725	98.6%
Mr. Frevert	$1,500,043	$0	$28,732,712	$30,232,755	$35,803,880	90.0%
Mr. Rice	$0	$3,953,820	$16,226,027	$20,179,847	$22,447,662	97.7%
Mr. Horton	$1,000,044	$300,000	$20,601,248	$21,901,292	$23,648,826	97.7%

1999 Total Compensation

Short-Term

Executive	Salary	Bonus	Other Annual Compensation	All Other Compensation	Total Annual Compensation
Mr. Lay	$1,300,000	$3,900,000	$206,716	$560,046	$5,966,762
Mr. Skilling	$850,000	$3,000,000	$51,701	$116,342	$4,018,043
Mr. Frevert	$513,333	$1,300,000	$1,670,356	$198,203	$3,681,892
Mr. Rice	$413,333	$1,100,000	$63,681	$8,937	$1,585,951
Mr. Horton	$513,333	$1,000,000	$15,000	$7,078	$1,535,411

Long-Term

Executive	Restricted Stock Awards	LTIP Payouts	Value of Options Exercised	Total Long-Term Compensation	Total Compensation	Percent At Risk*
Mr. Lay	$0	$0	$43,845,331	$43,845,331	$49,812,093	95.9%
Mr. Skilling	$0	$0	$46,359,937	$46,359,937	$50,377,980	98.0%
Mr. Frevert	$0	$0	$5,517,450	$5,517,450	$9,199,342	74.1%
Mr. Rice	$0	$0	$1,726,803	$1,726,803	$3,312,754	85.3%
Mr. Horton	$0	$0	$5,578,104	$5,578,104	$7,113,515	92.5%

04/16/01

CL 00410

1998 Total Compensation

Short-Term

Executive	Salary	Bonus	Other Annual Compensation	All Other Compensation	Total Annual Compensation
Mr. Lay	$1,266,667	$3,150,000	$160,292	$554,904	$5,131,863
Mr. Skilling	$816,667	$2,250,000	$23,949	$114,055	$3,204,671
Mr. Frevert	$458,337	$1,000,000	$612,258	$390,917	$2,461,512
Mr. Rice	$362,500	$1,100,000	$9,000	$4,342	$1,475,842
Mr. Horton	$491,667	$700,000	$14,300	$13,362	$1,219,329

Long-Term

Executive	Restricted Stock Awards	LTIP Payouts	Value of Options Exercised	Total Long-Term Compensation	Total Compensation	Percent At Risk*
Mr. Lay	$3,883,503	$0	$13,094,776	$16,978,279	$22,110,142	91.0%
Mr. Skilling	$1,764,544	$0	$2,886,044	$4,650,588	$7,855,259	87.8%
Mr. Frevert	$2,390,004	$0	$1,255,662	$3,645,666	$6,107,178	76.1%
Mr. Rice	$2,503,766	$0	$341,086	$2,844,852	$4,320,694	91.3%
Mr. Horton	$1,002,548	$0	$2,048,953	$3,051,501	$4,270,830	87.8%

*Percent at Risk - Includes bonus, restricted stock awards, LTIP payouts and value of options exercised as a percentage of Total Compensation.

Another potential item which outside consultants might add for total compensation is the difference between Enron's 2000 year-end stock price of $83.125 and various grant prices (shown in the chart "Stock Option Grants During 2000" on p. 23) times the number of options granted in 2000. If this item were added, it would increase the total for each executive by the following amounts:

Executive	2000 Stock Option Grant Value
Mr. Lay	$27,549,260
Mr. Skilling	$21,356,823
Mr. Frevert	$18,732,159
Mr. Rice	$27,445,748
Mr. Horton	$3,674,140

CL 00411

2. *How is executive compensation linked to Company performance?*

All decisions regarding executive compensation are based upon performance as measured against pre-established objectives, and market competitiveness. To ensure market competitiveness, Enron utilizes the services of Towers Perrin to conduct an annual total compensation study covering top positions.

Base salary Targeted at the median for the marketplace

Although executive's base salary is targeted at the median of the marketplace, all other compensation is "at risk" based on Enron's performance. Annual bonus funding (the "bonus pool") is determined considering Enron's performance against pre-established earnings targets. Performance sets the size of the pool that is distributed to employees across Enron based on business unit performance, and individual performance. Long-term incentive awards are delivered to eligible executives 50% in stock options and 50% in restricted shares. An increase in stock price, which benefits all shareholders, is required for executives to receive any gain on stock options. Restricted shares, a key retention mechanism, vests four years following the grant date, but may be accelerated based on Enron's annual cumulative shareholder return relative to the S&P 500. Size of grants is set considering market competitiveness (at the 75th percentile) and management's discretion. The Compensation and

Short term
Annual bonus Related to performance against pre established earning Targets
(size of pool - performance

04/16/01

Long Term (50% SO 50% RS) an increase in Stock price Required before executives Receive any gain on SO
Rest. Stock - size of grant considers market competitiveness (@75% level)

Management Development Committee of the Board of Directors approves base salaries, bonuses, and long-term incentive awards for executives.

3. *Why should Enron stockholders be supportive of employment agreements for the Named Officers?*

   The Board of Directors believes that employment agreements are an essential mechanism for retaining who we believe to be the top executives in the industry. The agreements generally provide for stock option grants, which align the interests of these executives with stockholder interests. The agreements also contain strong non-compete language should any of these individuals leave Enron. Consequently, we believe these employment agreements serve both parties equally.

4. *Why is the title in Ken Rice's employment agreement "Chief Commercial Officer, but his title in the Summary Compensation Table "Chairman and Chief Executive Officer, EBS"?*

   Mr. Rice's employment agreement was executed prior to July 21, 2000 when he was appointed to Chairman and Chief Executive Officer, Enron Broadband Services, Inc.

5. *The "Other Annual Compensation" in 1999 and 2000 for Mr. Frevert appears to be significantly higher than the other executives.*

   offset tax + costs

   Mr. Frevert was on an expatriate assignment, which terminated during 2000. In conjunction with his assignment, he had received payments to cover premiums, allowances, and tax gross-ups for additional tax liabilities.

6. *What plan generated the large LTIP payment to Mr. Rice in the "Summary Compensation Table"?*

   Mr. Rice received a grant of 101,380 phantom units in 1997 under the ECT Long Term Compensation Plan, in lieu of participating in the Enron Corp Long Term Program for that year. That grant vested based upon ECT actual performance relative to target performance, with an accelerated vesting schedule where ECT exceeded its operating plan. As per the Plan, for 1997 performance, 43-1/3% became vest- [illegible] additional 33-1/3% vested in 1998; the last traunche vested December 31, 1999. As per the Plan and after 100% vesting, 60% of the grant was redeemed in cash based upon Enron's closing stock price on January 24, 2000. An additional 20% was redeemed on January 24, 2001. The remaining 20% will be redeemed in 2002 based on Enron's stock price performance.

7. *The "Aggregated Stock Option/SAR Exercises" Table show that Ken Lay realized $123,399,478 in 2000. What grants generated this value?*

   Mr. Lay's employment agreement was amended in 1994 and he was awarded a grant of 1,200,000 (pre-split) options on February 8, 1994 (previously disclosed in Enron's 1995 Proxy.) The grant became 20% vested in 1994 with the remainder to vest on December 8, 2000. However, vesting was to be accelerated based on Enron's attainment of annual growth targets in earnings per share. The grant became fully vested in January 1999. The grant was made with a 7-year term; as such, the options were scheduled to expire on February 13, 2001. The options were granted at $17.00/share (post-split) and were exercised throughout the year 2000 at an average exercise price of $76.0588/share.

8. *The total shares/options reported in several tables (Summary Compensation Table-Securities Underlying Options, Aggregate Stock Option) for 1998 are different from what was reported in the 1999 Proxy. Why?*

   Stock split

   On August 13, 1999, Enron stock underwent a 2-for-1 split. For every one option or share in an employee's account, another option or share was credited to that account. The pure number of options/shares doubled. At the same time, the price per share was reduced by ½. The net value for every account after this transaction remained the same as the value immediately prior to the split. Thus, the tables have been adjusted to reflect the split.

04/16/01

9. *How did you determine the amount to contribute to Dr. Gramm's Deferral account?*

The amount is calculated as per the 1991 Stock Plan and represents the aggregate fee paid to other directors in stock options and phantom stock units. The aggregate fee is the annual retainer plus meeting fees for six regular Board meetings.

10. *Why did Lord Wakeham receive Phantom Stock Units in lieu of the mandatory deferral into the Phantom Stock Account?*

Deferral plan schemes do not work in the UK. However, a grant of phantom stock units in lieu of mandatory deferral into the Phantom Stock Account (under the 1994 Deferral Plan) provides Lord Wakeham with the opportunity to defer income taxes for up to 60 months.

11. *Why did executives exercise stock options in 2000? (See chart titled "Aggregated Stock Option/SAR Exercises During 2000 and Stock Option/SAR Values as of 12/31/00").*

Decisions by executives to exercise their stock options are completely personal, and usually result from personal financial or tax advice, and cash flow objectives.

12. *Why does Enron provide split-dollar life insurance to Messrs. Lay and Skilling?*

Split-dollar life insurance is often provided as part of the total compensation package for the most senior executives. Enron will recover the cost of life insurance premiums upon each of their deaths.

13. *What percent of Enron Corp. stock is owned or controlled by Enron employees?* 3.8% (9.0% if officers/directors added)

Enron employees own approximately 12.6 million shares of stock under the ESOP and approximately 16.3 million shares of stock under the Savings Plan for a total of 28.9 million shares. There are approximately 751.6 million Enron shares outstanding and, therefore, employees own approximately 3.8%. If we include Enron shares of stock held by Enron officers and directors outside the above two plans, the percentage increases to approximately 9.0%.

14. *How did Enron rank relative to the eleven industry peer companies for the 4-year performance unit period of 1997-2000?*

Based on Enron's 4-year Total Shareholder Return, Enron ranked 1st out of 11 other comparable companies. During the measurement period of 1/1/97-12/31/00 Enron's return to its stockholders was 294.45% compared with 128.05% for industry peers, 87.02% for the S&P 500, and 21.63% for 90-day U.S. Treasury Bills. Therefore, performance units granted in 1997 were valued at $2.00 for payout purposes.

15. *How are costs associated with each executive's personal use of Enron aircraft calculated?*

The actual incremental costs of using the company's airplane is based on a per mile and per plane formula, called the "Standard Industry Fare Level," which is set by the IRS and is approximately equivalent to the cost of first class travel on commercial airlines. These costs are imputed income to each executive. They pay taxes on this amount.

16. *Does Enron use an independent consultant for advice on executive and director's compensation?*

Yes, Enron utilizes the consulting services of Towers Perrin as it relates to executive and director's compensation. We rely on the consultants' expertise when we are presenting compensation recommendations to the Compensation Committee of the Board. At Compensation Committee meetings, the employee directors, Messrs. Lay and Skilling, leave the boardroom so that their own compensation packages and the company's performance may be discussed without influence.

04/16/01

CL 00413

17. *What is Enron's philosophy in entering into consulting agreements with non-employee Directors such as Messrs. Urquhart and Wakeham?*

Non-employee directors are generally chosen because of the specific expertise they can offer to the company. They are familiar with the company and can provide valuable assistance in the areas of their expertise. Enron believes we can obtain a competitive edge by using the specific talents of our Board members. Some may call

18. *Why is Enron no longer granting performance units under the Enron Corp. Performance Unit Plan?*

Enron has become such a diversified company that utilizing the S&P 500 to determine vesting of executive long-term grants was determined to better align executive pay to total shareholder return.

19. *Why does Enron use restricted stock with time-based vesting and a performance accelerator?*

There is no mark-to-market liability associated with restricted stock grants that vest on a time basis with a feature to accelerate vesting if performance hurdles are achieved. Additionally, this long-term incentive design provides an incentive for executives to provide returns that meet or exceed the S&P 500, which is great for shareholders.

Interoffice Memorandum

To: Enron Corp. Board of Directors

From: Mary K. Joyce Mary

Department: Executive Compensation

Subject: Management Committee Compensation Summary

Date: November 2, 2001

Dr. LeMaistre has requested that we send you the attached schedule, which has been used by the Compensation Committee for many years. October 30, 2001 values are reflected in this report. Please treat this information as highly sensitive and confidential.

Mr. Lay and Mr. Frevert each have a Loan Commitment Agreement which allows for advances up to $7,500,000 and $3,000,000 respectfully. Under SEC rules, Enron stock can be used to reduce an outstanding balance. Since May 1999, Mr. Lay's Loan Agreement authorizes the use of Enron stock to repay the loan and some payments have been made.

Also attached is a memo from Chuck Essick of Towers Perrin outlining and opining on a recent insurance contract swap for Mr. Lay.

If you have any questions, please contact Charles (Mickey) LeMaistre at (210) , Mary Joyce at (713) or Pam Butler at (713) .

Enron Corp. Board of Directors:

Robert A. Belfer
Norman P. Blake
Ronnie C. Chan
John H. Duncan
Wendy L. Gramm
Robert K. Jaedicke
Charles A. LeMaistre
John Mendelsohn
Paulo V. Ferraz Pereira
William C. Powers
Frank Savage
John Wakeham
Herbert S. Winokur, Jr.

cc: Kenneth L. Lay
Greg Whalley
Mark Frevert
Pam Butler

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #53

Charles E. Essick
Principal

1 Houston Center
1221 McKinney, Suite 2600
Houston, TX 77010-1006
713 754-5416
Fax: 713 754-5462

Towers Perrin

PRIVATE & CONFIDENTIAL

November 2, 2001

Dr. Charles A. LeMaistre
Chairman, Enron Compensation Committee
Enron Corp.
7 Bristol Green
San Antonio, TX 78209

Dear Dr. LeMaistre:

As you requested, Towers Perrin has prepared this letter based on our previous discussions with Mary Joyce prior to September 14, 2001, providing our observations regarding the Ken Lay insurance swap approved by Enron's Compensation Committee earlier this year.

Background

Towers Perrin understands that Ken Lay purchased annuities with a tax basis of $5 million for his wife Linda and himself (for a total tax basis value of $10 million). At the time when Enron's Board asked Ken to resume his duties as CEO following Jeff Skilling's departure, the Company began exploring ways to provide a reasonable retention incentive for Mr. Lay to encourage him to continue serving as CEO for the next 4.25 years.

Traditionally in the market, this type of retention handcuff is handled by issuing restricted stock to the executive. However, we understand that Mr. Lay has a very large current position in Enron stock and that he expressed an interest in having more liquidity in his personal portfolio. Consequently, as part of an attempt to give Mr. Lay the liquidity he desired and a simultaneous retention incentive, Enron's Compensation Committee agreed to the following:

- Enron purchased the two annuities from Mr. Lay for $10 million in cash.
- The Board agreed to allow Mr. Lay to earn the annuities back over 4 years for continued service.
- The $10 million present value of the annuities is to be netted out against Mr. Lay's long-term incentive awards over the next 4 years ($2.5 million per year).

As we understand this transaction, the initial $10 million cash payout to Mr. Lay for the annuities is equal in value (on net present value basis) to his cost for the annuities and is less than the current NPV floor value of the annuities ($11.2 million). Therefore, while there are cash flow consequences to the transaction (since Mr. Lay receives the cash now), the Company will receive greater value for this swap in the future than the $10 million payout made to Mr. Lay.

The feature of the swap which allows Mr. Lay to earn back the annuities over 4 years is similar to the way a restricted stock award would be structured. Thus, it should serve as an effective retention device, similar to restricted stock. However, since this portion of the insurance swap was done in lieu of restricted stock (which would be the more common vehicle used in the market), Towers Perrin recommends that this value be subtracted from future restricted stock/option awards that would otherwise be granted to Mr. Lay over then next 4 years (at a rate of $2.5 million per year).

Finally, Towers Perrin understands that one alternative to the structure described above was to simply provide a $5 million signing bonus to Mr. Lay and to allow him to also sell his annuity, but not his wife's annuity to the Company. Towers Perrin believes the structure of the original agreement is preferable to this alternative, since it provides a meaningful retention incentive.

* * * * *

I hope this letter meets Enron's needs. Please call me with any questions.

Sincerely,

Chuck Ericks

CEE:mhm

cc: Ms. Mary Joyce
Mr. John Duncan

AGENDA ITEM NO. 6
OTHER BUSINESS

6(a) Employment Agreements for Stan Horton and Rebecca Carter

6(b) Ken Lay's Employment Agreement

6(c) Administrative Committee Approval Process

6(d) Potential Acceleration of LTIP /KEYSOP January 2002 Grants

6(e) Potential Miscellaneous Broad Based Employee Grant

6(f) Stock Utilization Report

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #54

CL 00576

AGENDA ITEM NO. 6(a)
EMPLOYMENT AGREEMENT SUMMARIES approved

Stan Horton – Chairman & CEO, Enron Transportation Services Company

DOB 2/7/50

- Standard Contract   unvested equity $2.1 mm
- Expires March 1, 2005
- Mutual consent if requested to relocate from Houston, Texas
- Signing equity grant of $3,000,000:
  - $1,500,000 stock options = 107,145 options
  - $1,500,000 restricted stock = up to 37,500 shares
- Standard vesting and 5-year term options
- Date of grant will be date approved by the Compensation Committee or date employment agreement is executed, whichever is later.

520
1200
2000
$3720

Rebecca Carter – Sr. Vice President, Board Communications & Secretary

deferred to full Board

- Standard Contract
- Expires August 31, 2004
- Signing equity grant of $500,000:
  - $250,000 stock options = 17,860 options
  - $250,000 restricted stock = up to 6,250 shares
- Standard vesting and 5-year term options
- Date of grant will be date approved by the Administrative Committee or date employment agreement is executed, whichever is later.

Exec Sess

AGENDA ITEM NO. 6(b)
KENNETH L. LAY
CHANGES TO CURRENT EMPLOYMENT AGREEMENT PROVISIONS

	CURRENT	PROPOSED
Term:	12/31/03 Term Date	12/31/05 Term Date
Title(s):	Chairman of the Board, Enron Corp.	Chairman of the Board, Enron Corp. Chief Executive Officer, Enron Corp. add President
Base Salary:	$975,000	$1,000,000
Pension Benefits:	Years of service through termination are used to calculate pension benefits. Would lose final average pay "backstop" benefit, present value of $2.5mm, if remains active after 12/31/01.	Include provision in the employment agreement which specifies that "backstop" benefits will be provided to Mr. Lay through the term of the agreement.
Loan Agreement:	$4 million through 12/31/2001	Extend ~~$4~~ $7.5 million through 12/31/2005
HTD **Contract Equity at signing:**	$13.6mm for 2 year extension (12/31/01 to 12/31/03)	Supplemental contract to extend 10 yrs beyond Retirement Combination • Equity grant $10 million ([illegible]% options/[illegible]% restricted stock – standard vesting). • Potential upward adjustment in the next 4 to 6 weeks when new market data is available.

Personal Admin Asst 80000+ Bonus

+ Business duties

? OK

Special Asst to Chm CFO

not employee @ ENE

CL 00578

Arthur Andersen
Professional Standards Group

To: Benjamin S. Neuhausen@ANDERSEN WO
cc: John E. Stewart@ANDERSEN WO
Date: 05/28/99 05:15 PM
From: Benjamin S. Neuhausen, Chicago 33 W. Monroe, 50 / 72307
Subject: Enron

Comments from Dave Duncan marked below

——————— Forwarded by Benjamin S. Neuhausen on 05/28/99 04:35 PM ———————

To: David B. Duncan@ANDERSEN WO
cc: John E. Stewart@ANDERSEN WO
Date: 05/28/99 03:50 PM
From: Benjamin S. Neuhausen, Chicago 33 W. Monroe, 50 / 72307
Subject: Enron

In case we don't hook up this afternoon, here are the results of discussion with John and further thinking on my part.

1. Setting aside the accounting, idea of a venture entity managed by CFO is terrible from a business point of view. Conflicts of interest galore. Why would any director in his or her right mind ever approve such a scheme? Plus, even if all the accounting obstacles below are overcome, it's a related party, which means FAS 57 disclosures of all transactions. Would Enron want these transactions disclosed every year as related party transactions in their financial statements? **Agree**

2. Enron should view the new entity as a SPE for accounting purposes, and apply EITF Topic D-14 and Issue 90-15. This raises several issues: **OK**

a. CFO's capital is not capital from an independent party as that term is used in EITF 90-15. Therefore, CFO's capital is ignored in determining whether the entity has enough independent capital at risk to avoid consolidation by Enron. **OK**

b. If Enron makes a gift to the entity after formation, the value of the gift should be subtracted from the investors' equity at risk, including the independent investors. So, if CALPERS invests $10 million and their pro rata share of the gift from Enron is $50 million, CALPERS has no equity at risk. The result is that Enron will need to consolidate the SPE because the SPE has no outside equity at risk. **Awfully tough. CALPERS doesn't actually receive a cash reimbursement of its equity contribution (different from fees discussed in 90-15). Duncan suggests viewing the gift as an Enron capital contribution, and then considering whether the outside capital passes the Crooch 80/20 test.**

c. The outside investors need to own the residual class of equity. That is, the CFO can't be subordinated to the outside investors. **Agree**

3. We would be very uncomfortable with Enron recording gains on sales of assets to the entity or immediate gains on any transactions. Subsequent mark to market gains are not troublesome, but

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Exhibit 763
H-02-0121
JURY TRIAL

AA(H)-J 000817

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EXHIBIT #55

immediate gains are. Dave understands concern, but if as proposed every transaction with Enron is approved by the outside investors, what is the basis to preclude gain?

4. If part of the gift goes to the CFO, that is compensation expense to Enron. Agree.

5. If Enron insulates the CFO from risk, then the CFO's capital and vote should be viewed as Enron's capital and vote. Same result if Enron has the upside on the CFO's investment. A new twist is to have either the value of the gift or at least some of the upside go to a charitable remainder trust. Enron would recommend charities to the trustee, but the trustee would have variance power. Would that constitute an Enron residual interest?

Printed By: John E. Stewart

AA(H)-J 000818

To: Benjamin S. Neuhausen@ANDERSEN WO
cc: John E. Stewart@ANDERSEN WO
Date: 06/01/99 11:07 AM
From: David B. Duncan
Subject: Re: Enron

Ben- I agree with all the points you and John raise except for two, where I need some more help.

But first, on your point 1(i.e., the whole thing is a bad idea), I really couldn't agree more. Rest assured that I have already communicated and it has been agreed to by Andy that CEO, General Council, and Board discussion and approval will be a requirement, on our part, for acceptance of a venture similar to what we have been discussing. Rick is insistent of such communication also. You should also know that none of this communication has yet to occur and this thing could get killed when it does. This thing is still very much in the brainstorming stage, but Andy wants to move through it very quickly to get all this done, if possible, this quarter. Andy is convinced that this is such a win-win that everyone will buy in. We'll see.

I have also discussed with Andy and Rick the formation and ongoing related party disclosures that will be necessary in the proxy and financials. This will also be a component of any discussion with those mentioned above.

Also, as usual, I am and will keep our local office mgmt. in the loop on this unusual potential transaction as it proceeds to ensure I'm getting appropriate practice advice.

On the accounting, I'd like to discuss further your points 2b (gift reduces equity at risk) and 3 (uncomfortable with transaction gains).

2b- The purpose of the "gift"(obviously, Enron and Andy would dispute that characterization for the reasons I've mentioned to you previously) is to,no doubt, provide over- collateralization to the venture equity players. It will no longer enrich the equity holders as was a consequence of the original discusions(the deemed compensation issue took care of that). The current plan is to have any residual that may remain after some predetermined time go to this charity trust idea that Andy had last Thursday(more about that later). It seems to me that the important consideration is whether the equity holders maintain original capital at risk sufficient to meet the SPE requirements throghout the life of the venture. If they were to receive a distribution of any "gift" capital or otherwise get a return of capital, I would agree with your conclusion. But if they do not and outside capital sufficient to meet the test remains in the venture,I don't understand why any other excess capital would make a difference. Please clarify.

In other ventures where Enron has employed an over-collateralization technique, we have looked to the 80/20 rule as a guide for excess. I have been thinking about how that may apply here, it would not seem to take much borrowed capital for the venture to pass the test if we wanted to apply it (assuming the "gift" as Enron capital for purposese of the test). Obviously, this structure is unusual in that Enron has no vote and no real ownership interest in the venture. It's like this gift equity is parked here for awhile to provide the over-collateralization, then will go away(to charity I'm told). Does it make sense to apply this test here? It does not seem that this will preclude the outside holders from truly controlling there important rights in the venture(i.e., to approve all investments). Your thoughts on this would be appreciated.

3- If we can clear the hurdle of Enron not consolidating this venture, help me to defeat gain accounting on Enron transactions where approval of the transaction is controlled by the nonrelated owners and fairness

Def. ANDERSEN
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opinions will be obtained for all. I'm not saying I'm in love with this either,but I'll need all the ammo I can get to take that issue on.

Finally, the charitable trust idea. As I mentioned to you, Andy's latest idea to avoid the compensation issue and ,in my view , make this all more saleable to top mgmt. and the BOD,is to have any residual benefits from the forward transaction(the "gift") go to a charitable trust as opposed to the other venture parties. The notion is that this does not create a residual interest to Enron as Enron would not control the trust,(although Enron could suggest to the trustees where to direct gifts and the trust would probably be called the Enron Charity Trust). He says these are done all the time for tax purposes.

I'm still working with him to figure out how exactly this will work and accomplish his objectives. It seems if the gift is in the venture in general(as opposed to the trust only) it will attach to all the venture owners. It must be that the trust will hold a real but specfically defined residual interest in the venture but have no vote. If Enron will truly have no control over this trust and the funds could never return , how would you view this? Still no accounting by Enron(consolidation of trust and/or charitable donation expense)?

Thanks for your advice and patience as this thing unfolds. Let's please talk as soon as possible.

Printed By: John E. Stewart

LJM1

Excerpt from
MINUTES
SPECIAL MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
June 28, 1999

Minutes of a special meeting of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 10:00 a.m., C.D.T., on June 28, 1999, at the Enron Building in Houston, Texas.

The following Directors were present, either in person or by telephone conference connection, where each participant could hear the comments of the others and join in the discussion, constituting a quorum:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Dr. John Mendelsohn
Mr. Jerome J. Meyer
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

Director Ronnie C. Chan was absent from the meeting. Messrs. James V. Derrick, Jr. and Andrew S. Fastow, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, were also in attendance. Messrs. Richard B. Buy, Daniel R. Castagnola, James A. Hughes, and Joseph W. Sutton joined the meeting in progress as noted below.

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Lay called upon Mr. Skilling to discuss a proposed investment partnership. Mr. Skilling noted that due to changes in the accounting treatment of off-balance sheet transactions the Company had been analyzing new types of financing vehicles. He called upon Mr. Fastow to discuss the proposal.

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EXHIBIT #56a

Mr. Fastow discussed certain challenges the Company is facing regarding hedging its investment in Rhythms NetConnections ("Rhythms"), a high-speed data communication services company in which the Company holds an equity position, and increasing the liquidity in its Merchant Portfolio. He noted that the Company has certain special purpose vehicles ("SPV") that have significantly appreciated in value due to holdings of forward contracts on the Company's stock. He proposed establishing a non-Enron investment partnership ("LJM") with outside investors. The Company would transfer the in-the-money value of a forward contract currently held in a SPV into LJM. LJM would pay the Company $50 million and enter into a swap with the Company to hedge the investment in Rhythms. In addition, LJM may negotiate with the Company regarding the purchase of additional assets in the Merchant Portfolio. Mr. Fastow stated that he would serve as the General Partner of LJM but have no direct pecuniary interest in the Company's stock. A copy of Mr. Fastow's presentation is filed with the records of the meeting.

A discussion ensued with Messrs. Derrick, Fastow, Lay, and Skilling answering questions from the Directors regarding Mr. Fastow's involvement in the partnership and the economics of the transaction. Mr. Fastow noted that PricewaterhouseCoopers LLP would be rendering a fairness opinion that, in their opinion, the value the Company was receiving in the transaction was in excess of the value of the forward contract the Company was giving up. Following the discussion, upon motion duly made by Mr. Meyer, seconded by Dr. Jaedicke, and carried, the following resolutions were approved:

RESOLVED, that amendments to the confirmations dated February 13, 1997 and March 23, 1998, respectively (the "Confirmations"), to the master agreements dated January 16, 1996 and December 9, 1997, respectively, between UBS AG ("UBS") and Enron Corp. (the "Company") resulting in an increase in the strike price for a portion of the Confirmations and a decrease in the strike price for the balance is hereby authorized;

RESOLVED FURTHER, that the assignment by UBS to, and assumption or purchase by LJM Cayman, L.P. (the "Partnership") of, a portion of the Confirmations and underlying shares of Enron Corp. common stock held for the Company by UBS (the "Enron Shares") together with the Company's execution of a master stock purchase agreement (the "LJM Master Stock Purchase Agreement") with the Partnership is authorized;

RESOLVED FURTHER, that cancellation of the LJM Master Stock Purchase Agreement prior to the expiration of such agreement in connection with the transactions, and for the consideration to the Company, presented to the Board for its approval is authorized;

RESOLVED FURTHER, that Kenneth Lay and Jeffrey Skilling are hereby appointed as a committee of this Board with full power and authority to determine if the consideration received by the Company in such transaction is sufficient in the event of a change in the terms of such transaction from those presented to the Board for its consideration;

RESOLVED FURTHER, that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Conduct of Business Affairs/Investments and Outside Business Interests of Officers and Employees that participation of Andrew S. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company;

RESOLVED FURTHER, that each of the Chairman of the Board, the Vice Chairman of the Board, the President, or any Vice President of the Company (any one of them acting alone) is hereby authorized and empowered to negotiate, execute, deliver, perform, and consummate, for and in the name and on behalf of the Company, such agreements as are necessary to effectuate the Amendments and transfer of Enron Shares, such execution to be conclusive evidence of such approval on behalf of the Company;

RESOLVED FURTHER, that the Chairman of the Board, the Vice Chairman of the Board, the President, or any Vice President of the Company be, and each of them hereby is, authorized in the name and on behalf of the Company, under its corporate seal or otherwise, to negotiate, execute, deliver, amend, perform, and consummate such indemnification agreements or other agreements, instruments, or documents as such officer may deem necessary or desirable to carry out the purpose and intent of the resolutions herein, in such forms as shall be approved by the officer executing the same, such approval to be conclusively evidenced by the execution thereof by such officer;

RESOLVED FURTHER, that each such officer be, and each such officer hereby is, authorized in the name and on behalf of the Company to take or cause to be taken such action as such officer may deem necessary or desirable in connection with the performance by the Company of its obligations under any agreement, document, or instrument related to these transactions to which the Company is a party;

RESOLVED FURTHER, that all actions heretofore taken by any officer of the Company, in the name and on behalf of the Company, related to or in connection with the transactions contemplated by these resolutions, including without limitation the execution and delivery of any instruments or other documents as any officer shall have deemed necessary, proper, or advisable, are hereby adopted, ratified, confirmed, and approved in all respects; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
October 11, 1999

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 4:30 p.m., C.D.T., on October 11, 1999 at the Enron Building in Houston, Texas.

The following Committee members were present constituting a quorum:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Jerome J. Meyer
Mr. John A. Urquhart

Committee member Ronnie C. Chan was absent from the meeting. Directors Ken L. Harrison, Kenneth L. Lay, Charles A. LeMaistre, and Jeffrey K. Skilling, Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, David B. Gorte, Mark E. Koenig, Jeffrey McMahon, Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, also attended the meeting.

The Chairman, Mr. Winokur, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Winokur called the meeting to order and noted that a draft of minutes of the meeting of the Committee held on August 9, 1999 had been distributed to the Committee members. He called for any corrections or additions. There being none, upon motion duly made by Mr. Meyer, seconded by Mr. Urquhart, and carried, the minutes of the meeting of the Committee held on August 9, 1999 were approved as distributed.

Mr. Winokur called upon Mr. Fastow to present the Chief Financial Officer's report. Mr. Fastow reviewed the Company's key financial ratios and long-term liability analysis, noting the mix between fixed and floating rate liabilities and on-balance and off-balance sheet debt. He discussed the Company's stock trading portfolio and noted changes since the beginning of the year. He reviewed the investments made year-to-date by each business unit and compared them to the plan amount. He discussed the status of capital commitments year-to-date and commented on the transactions the Company had taken or would be taking to fund the cash outflows and noted the importance of funds flow to the Credit Rating Agencies. He distributed a handout on funds flow, a copy of which is filed with the records of the meeting. He discussed issues impacting funds flow and how the Company was managing funds flow, including vehicles currently in place

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U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #56b

and the strategy for the future. A copy of Mr. Fastow's report is filed with the records of the meeting.

Mr. Fastow then updated the Committee on a financing structure approved earlier in the year, LJM 1, and discussed the benefits that the Company had incurred since the transaction closed on June 30, 1999. He recommended that the Company continue to syndicate capital investments to address the funds flow issue. He presented information concerning an unaffiliated investment partnership, LJM 2, and discussed the rationale and benefits of the proposed partnership. He stated that the partnership could possibly provide the Company with an alternative, optional source of private equity to manage its investment portfolio risk, funds flow, and financial flexibility. He noted that he would be acting as managing partner of LJM 2 and discussed his role in the LJM 2 partnership and how it would benefit the Company. He commented on the differences between LJM 1 and LJM 2, the controls that would be put in place to manage any transactions between the Company and LJM 2, the fund fees and promote, and any required disclosure. He noted that the controls include review and approval of all transactions by the Chief Accounting Officer and the Chief Risk Officer of the Company. He stated that the Audit and Compliance Committee would, on an annual basis, review all transactions completed within the past year and make any recommendations they deemed appropriate. He noted that the Company's Conduct of Business Affairs Policies (relating to investments and outside business interests of officers and employees) would prohibit him from participating in LJM 2 as managing partner due to his position as Executive Vice President and Chief Financial Officer of the Company, absent appropriate reviews and waivers from the Board and a finding that such participation does not adversely affect the best interests of the Company. He asked that the Committee recommend to the Board that such review and findings be made in this instance to allow his participation. Messrs. Causey, Fastow, and Skilling answered questions from the Committee concerning the role of other partners, the review by Arthur Andersen LLP, and the benefits to the Company, which included having another potential buyer of assets and provider of capital, of having Mr. Fastow act as managing partner. Following a discussion, upon motion duly made by Mr. Meyer, seconded by Mr. Blake, and carried, the proposed waiver of the aforementioned policy, including findings of no adverse effects to the best interests of the Company related to Mr. Fastow's involvement in LJM 2, was approved for recommendation to the Board. A copy of Mr. Fastow's report is filed with the records of the meeting.

Mr. Winokur called upon Mr. McMahon to present the Treasurer's report. Mr. McMahon reviewed the liquidity report and discussed financings that had occurred since the August Committee meeting. He commented on the current market liquidity and the potential for disruption related to year-end. He reviewed the active letters of credit and noted that the Company had significantly increased its available capacity and lowered its cost by utilizing surety bonds, issued by insurance companies, in lieu of letters of credit. He discussed the guaranty portfolio and commented that Enron Energy Service, LLC was currently the largest user of trade guarantees issued by the Company. He noted that there was no change in the Company's debt ratings, as determined by the Credit Rating

Agencies, and added that he and Messrs. Fastow and Skilling had met with Moody's Investor Services recently and formally requested an upgrade. He updated the Committee on the level and type of financial support that the Company had provided to Azurix Corp. A copy of Mr. McMahon's report is filed with the records of the meeting.

Mr. McMahon then discussed the proposed "shelf" registration statement to be filed with the Securities and Exchange Commission ("SEC"). He noted that, per the SEC regulations, the number of shares of common stock registered for sale from time to time pursuant to the current effective shelf registration statement did not automatically double when the Company's two-for-one stock split was effected during the third quarter. He stated that the proposed resolution was necessary to increase the number of shares that could be offered and sold from time to time pursuant to the registration statements. Following a discussion, upon motion duly made by Mr. Belfer, seconded by Mr. Urquhart, and carried, the resolution was approved for recommendation to the Board.

Mr. McMahon then discussed a proposed resolution to allow a Special Committee of the Board, consisting of Messrs. Lay and Skilling, to approve the issuance and sale of up to 500,000 shares of the Company's common stock in connection with acquisitions. He noted that Oregon law allows the full Board of Directors to authorize a committee to approve the issuance or sale of shares if the full Board (1) approves a specific maximum number of shares to be issued and (2) designates the specific purpose for which such shares would be issued. He stated that this would enable the Company to use small amounts of stock to make relatively small acquisitions without having to bring the matter before the full Board. Following a discussion, upon motion duly made by Mr. Belfer, seconded by Mr. Urquhart, and carried, the resolution was approved for recommendation to the Board.

Mr. Sutton left the meeting following Mr. McMahon's report.

Mr. Winokur called upon Mr. Buy to present the Chief Risk Officer's report, a copy of which is filed with the records of the meeting. Mr. Buy discussed the Company's top 25 credit exposures, with specific emphasis on companies that did not appear on the list at the August 9, 1999 Committee meeting. He reviewed the Company's current credit reserve and compared it to the historical and required reserve, as calculated. He gave an overview of the Company's Restructuring Group and discussed the deals currently in the group's portfolio, the criteria for transferring assets into the group, and completed restructurings. He reviewed the top and bottom ten performing investments and discussed investments new to the lists since the last Committee meeting. He ended his presentation with an overview of the initiatives currently being undertaken by the Company's Risk Assessment & Control Group ("RAC Group"). He called upon Mr. Murphy to give a market risk update.

Mr. Murphy presented the Committee with an update on market risk, a copy of which is filed with the records of the meeting. He reviewed the third quarter and year-to-date profit and loss and value-at-risk ("VAR") of the Company by commodity group. He discussed the returns each commodity group had earned compared to the VAR it had taken. He gave an overview of the VAR backtesting performed by the RAC Group to test the accuracy of the VAR calculation. He discussed exposures under a "worst case" scenario of 5%-25% shifts in commodity prices. He reviewed limit violations during the third quarter of 1999 and noted that violations had significantly decreased from earlier in the year. Mr. Winokur called upon Mr. Koenig to discuss the common stock dividend.

Mr. Koenig gave the Board an overview of the Company's current dividend yield and level and the historical annual increase. He commented on the impact an increase in the dividend had on cash flow and discussed the Company's increasing capital needs and investment opportunities. He compared the dividend yield to the Company's energy peer group and investment peer group. Following a discussion, the Committee agreed by consensus that it would recommend to the Board that the dividend level be held constant.

There being no further business to come before the Committee, the meeting was adjourned at 6:00 p.m., C.D.T.

Rebecca C. Carter
Secretary

APPROVED:

Chairman

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LJM1 Update

- Closed June 30
- $16 million outside equity raised
- Forward contract "restructuring" completed
- Benefits to Enron
  - $50 million cash payment to Enron increased to $64 million
  - Rhythm Netconnections swap in the money $164 million for Enron*
  - Purchased $15 million equity in Condor
    - Bridged Project Margaux
    - Purchased Promigas
    - Purchased Sarlux
  - Purchased stake in Cuiaba
  - Services Agreement
- Positioned as an alternative, optional source of private equity for Enron to manage its investment portfolio risk, funds flow, and financial flexibility

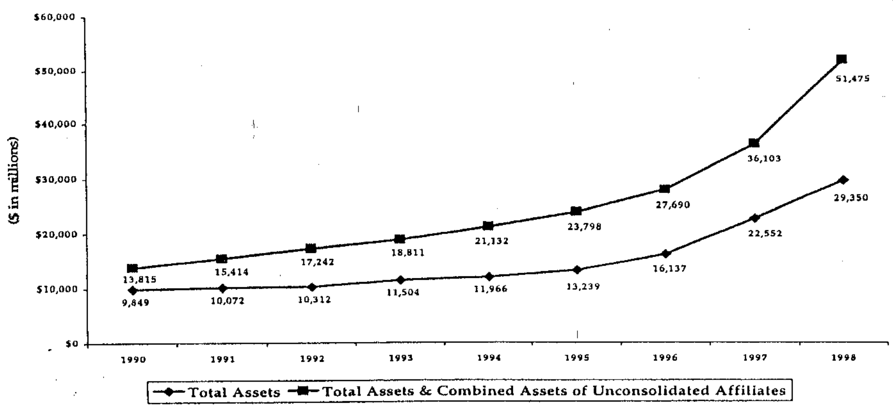
*As of September 30, 1999

VEL 00325

ENRON
Finance Committee Meeting
1999/JM-10/99

Private Equity Strategy

- Continued significant capital investment by Enron
- Energy and communications investments typically do not generate significant cash flow and earnings for 1-3 years
- Limited cash flow to service additional debt
- Limited earnings to cover dilution of additional equity
- Result: Enron must syndicate its capital investments in order to grow



Finance Committee Meeting
1999/JM-10/99

VEL 00326

Rationale for LJM 2 Structure

- New FASB consolidation rules
- Better ability to manage risk positions (non-affiliate status)
- Better ability to manage financial flexibility

Finance Committee Meeting
1999/JM-10/99

VEL 00327

Agenda Item ____
RATIFICATION OF DETERMINATION
(Suggested Form of Resolutions)

WHEREAS, Andrew S. Fastow serves as the Executive Vice President and Chief Financial Officer of the Company;

WHEREAS, Mr. Fastow has the opportunity to participate in the formation of an investment partnership (the "Partnership") that would not otherwise be affiliated with the Company;

WHEREAS, it is anticipated that Mr. Fastow will serve as the managing partner/manager of the Partnership;

WHEREAS, it is anticipated that the Partnership will invest in energy and communications-related businesses and assets, including businesses and assets of the Company;

WHEREAS, the Partnership, as a potential ready purchaser of the Company's businesses and assets or as a potential contract counterparty, could provide liquidity, risk management and other financial benefits to the Company;

WHEREAS, the Office of the Chairman of the Company has determined, for the foregoing reasons, that Mr. Fastow's participation as the managing partner/manager of the Partnership will not adversely affect the interests of the Company;

NOW THEREFORE BE IT RESOLVED, that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Conduct of Business Affairs/Investments and Outside Business Interests of Officers and Employees that participation of Mr. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

VEL 00329

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12/22/99

MINUTES
MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
October 11-12, 1999

Minutes of a meeting of the Board of Directors of Enron Corp. ("Company") noticed to begin at 7:00 p.m., C.D.T., but actually begun at 7:20 p.m., C.D.T., on October 11, 1999 at the Four Seasons Hotel, Whitney Room, in Houston, Texas.

The following Directors were present, constituting a quorum:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Ms. Rebecca P. Mark
Dr. John Mendelsohn
Mr. Jerome J. Meyer
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

Director Ronnie C. Chan was absent from the meeting. The meeting was begun in executive session, during which Messrs. Richard A. Causey, Andrew S. Fastow, Mark E. Koenig, Jeffrey McMahon, and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, and Messrs. Paulo V. Ferraz Pereira and Frank Savage, candidates for election to the Company's Board of Directors, were also in attendance.

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Lay called the meeting to order and called for a revised agenda to discuss the election of two new directors to the Company's Board of Directors. He called upon Lord Wakeham to present the candidates. Lord Wakeham noted that the Nominating Committee of the Board was recommending that Messrs. Paulo Ferraz Pereira and Frank Savage be elected to the Company's Board. He

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EXHIBIT #56c

Distributed 12/14

Common Stock in the number of shares issued or reserved for issuance; that the Chairman of the Board, any Vice Chairman of the Board, the President, any Executive or Senior Vice President, or any Vice President of the Company be, and each of them hereby is, authorized and directed to execute and deliver on behalf of the Company to the New York Stock Exchange, Inc. or other such securities exchanges such indemnity agreements in such form as may be necessary to effect the aforesaid listing; and that the officers of the Company be, and they hereby are, authorized and directed to execute and deliver any applications, documents, or agreements, to take any and all actions, to appear before such exchanges if necessary, to appoint any banking or other institution as an agent of the Company for any purpose, and to do or cause to be done any and all things as may appear to them to be necessary or desirable in order to effect such listing; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Mr. Winokur then discussed information concerning an unaffiliated investment partnership, LJM 2, and stated that the partnership could possibly provide the Company with an alternative, optional source of private equity to manage its investment portfolio risk, funds flow, and financial flexibility. He noted that Mr. Andrew S. Fastow would be acting as the managing partner of LJM 2 and discussed Mr. Fastow's role in the LJM 2 partnership. He commented on the controls that would be put in place to manage any transactions between the Company and LJM 2 and noted that the Company and LJM 2 were not obligated to one another in any way. He noted that the controls include review and approval of all transactions by the Chief Accounting Officer and the Chief Risk Officer of the Company. He stated that the Audit and Compliance Committee would, on an annual basis, review all transactions completed within the past year and make any recommendations they deemed appropriate. He stated that the Company's Conduct of Business Affairs Policies (relating to investments and outside business interests of officers and employees) would prohibit Mr. Fastow from participating in LJM 2 as managing partner due to his position as Executive Vice President and Chief Financial Officer of the Company, absent appropriate reviews and waivers from the Board and a finding that such participation does not adversely affect the best interests of the Company. He recommended that such review and findings be made in this instance, his motion was duly seconded by Mr. Urquhart, and carried, and the following resolutions were approved:

WHEREAS, Andrew S. Fastow serves as the Executive Vice President and Chief Financial Officer of the Company;

WHEREAS, Mr. Fastow has the opportunity to participate in the formation of an investment partnership (the "Partnership") that would not be affiliated with the Company;

WHEREAS, it is anticipated that Mr. Fastow will serve as the managing partner/manager of the Partnership;

WHEREAS, it is anticipated that the Partnership will invest in energy and communications-related businesses and assets, including businesses and assets of the Company;

WHEREAS, the Partnership, as a potential ready purchaser of the Company's businesses and assets or as a potential contract counterparty, could provide liquidity, risk management, and other financial benefits to the Company;

WHEREAS, the Office of the Chairman of the Company has determined, for the foregoing reasons, that Mr. Fastow's participation as the managing partner/manager of the Partnership will not adversely affect the interests of the Company;

NOW, THEREFORE IT IS RESOLVED, that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Conduct of Business Affairs/Investments and Outside Business Interests of Officers and Employees that participation of Mr. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Mr. Winokur stated that the Finance Committee had discussed the Company's dividend level taking into consideration the Company's increasing capital needs and investment opportunities. He recommended that the Board keep the dividend level constant and approve the declaration of dividends payable in the fourth quarter of 1999 for the common and preferred issues of stock; his motion was duly seconded by Mr. Blake, and carried, and the following resolutions were adopted:

RESOLVED, that a dividend of $3.413 per share on the Cumulative Second Preferred Convertible Stock of the Company, covering the quarter ending December 31, 1999, be, and it hereby is, declared payable on January 3, 2000, to shareholders of record of said stock at the close of business on December 10, 1999; and

RESOLVED FURTHER, that a dividend of $0.125 per share on the Common Stock of the Company be, and it hereby is, declared payable on December 20, 1999, to shareholders of record of said stock at the close of business on December 1, 1999, out of the net profits or surplus of the Company available for the payment of dividends.

Mr. Winokur stated that the Committee had also discussed the Company's liquidity and noted that the Company had significantly increased its available capacity and lowered its cost by utilizing surety bonds, issued by insurance companies, in lieu of letters of credit. He stated that Messrs. Fastow, McMahon, and Skilling had met recently with Moody's Investor Services and formally requested an upgrade to the Company's credit rating.

Mr. Lay called upon Dr. Jaedicke to report on the Audit and Compliance Committee's meeting held on October 11, 1999. Dr. Jaedicke stated that Mr. Causey and Mr. David B. Duncan, of Arthur Andersen, LLP ("AA"), had given a status report on the Company's internal controls. He noted that Mr. Richard B. Buy had given credit and market risk reports and Mr. Causey had discussed the progress made on the SAP implementation. He stated that the Committee also heard a report from Ms. Sharon A. Butcher, of the Company, regarding the Company's compliance with its Conduct of Business Affairs Policies. He stated that the Committee held an executive session with AA to discuss the adequacy of the Company's financial disclosure and he noted that AA was very comfortable with the Company's level of disclosure.

MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
December 13, 1999

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 4:00 p.m., C.S.T., but actually begun at 4:30 p.m. C.S.T., on December 13, 1999 at the Enron Building in Houston, Texas.

All of the Committee members were present, as follows:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. Jerome J. Meyer
Mr. Paulo Ferraz Pereira
Mr. Frank Savage
Mr. John A. Urquhart

Directors Ken L. Harrison, Kenneth L. ~~Lay,~~ Charles A. LeMaistre, and Jeffrey K. Skilling and Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, David B. Gorte, Mark E. Koenig, Jeffrey McMahon, Theodore R. Murphy, and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, also attended the meeting.

The Chairman, Mr. Winokur, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Winokur called the meeting to order, noted that a draft of minutes of the meeting of the Committee held on October 11, 1999 had been distributed to the Committee members, and called for any corrections or additions. There being none, upon motion duly made by Mr. Pereira, seconded by Mr. Blake, and carried, the minutes of the meeting of the Committee held on October 11, 1999 were approved as distributed.

Mr. Winokur called upon Mr. Fastow to present the Chief Financial Officer's report. Mr. Fastow presented three scenarios outlining the potential utilization of the proceeds to be received from the Company's sale of Portland General Electric Company and discussed the impact each scenario would have on the Company's key financial ratios. He noted that the Company would continue to analyze the potential uses of the proceeds and the effect on the Company prior to any proposal of a recommendation to the Committee. He reviewed recent Company stock repurchase activity, the Company's

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EXHIBIT #56d

stock repurchase program previously authorized by the Board, and the Company's cost of capital over the last three years. He distributed a handout, a copy of which is filed with the records of the meeting, and discussed the value created by Enron Global Finance during 1999 and how the group had performed against its goals. He also discussed the major financial issues the Company would be facing in 2000 including changes in public market liquidity, the accounting treatment for structured finance transactions, the impact of the decline in Azurix Corp.'s stock price on the Company's ability to transact in the financial markets, and how capital invested in Enron Communications, Inc. would be regarded by the financial markets. A copy of Mr. Fastow's presentation is filed with the records of the meeting.

Mr. Winokur called upon Mr. McMahon to present the Treasurer's report. Mr. McMahon reviewed the liquidity report and stated that the Company aimed to maintain between $750 million and $1 billion in overnight liquidity. He discussed the five largest merchant asset investments in each of three categories, public equity, debt instruments, and private equity, and the liquidity assumptions related to each investment. He reviewed the year-to-date investments and status of capital commitments by business unit and commented on the year end transactions the Company would be undertaking to fund the cash outflows. He reviewed the active letters of credit and the guaranty portfolio and commented on changes since the end of the third quarter. He noted that Moody's Investor Services had recently put the Company on "positive outlook" and stated that this was typically a transition rating that companies were given before an upgrade would be considered. He discussed two ~~new~~ products that the Company was introducing into the insurance markets and the benefits the products would offer. He discussed a recommended revision to the Company's Cash Management Policy and following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Urquhart, and carried, the proposed revision to the Cash Management Policy was approved for recommendation to the Board. A copy of Mr. McMahon's report is filed with the records of the meeting.

Mr. Winokur revised the agenda to postpone the discussion of the operating plan financing until after the discussion of the operating plan at the Board meeting.

Mr. Winokur called upon Mr. Sutton to discuss certain proposed projects and amendments. Mr. Sutton stated that the Company had executed a nonbinding letter of intent with the government of United Arab Emirates ("UAE") to develop an interconnected three bcf/day gas pipeline system from Qatar through UAE to Oman in partnership with the UAE government and Elf Aquitaine. He discussed the pipeline route, the cost, and the key motives for undertaking the project. He noted the commercial terms of the project and stated that the Company was only seeking approval of $30 million in the form of an initial investment at this time. He discussed the benefits of the project to the Company and the additional steps that would be taken over the next few months. He requested that the Committee recommend to the Board that the Board delegate to the Office of the Chairman the authority to approve the initial investment of $30 million and following a discussion, upon motion duly made by Mr. Meyer, seconded by Mr. Urquhart, and carried, the delegation of authority to the Office of the Chairman to approve the initial investment of $ 30 million was approved for recommendation to the Board.

Mr. Sutton then discussed a proposal for three business units of the Company to purchase a combined total of 38 turbines. He stated that the global availability of turbines was constrained through the end of the year 2002 and that turbines were required across the Company. He discussed the turbines currently in the Company's inventory, the most likely uses for the additional turbines, and the capital requirement timeline. He stated that the purchase was initially low risk because the initial investment was fairly small, there was considerable time until significant expenditures for the turbines needed to be made, and the Company had termination rights in the contracts. Following a discussion, upon motion duly made by Mr. Belfer, seconded by Mr. Blake, and carried, the proposed turbine purchases were approved for recommendation to the Board.

Mr. Sutton called upon Mr. Gorte to discuss a project proposed by Enron North America ("ENA"). Mr. Gorte stated that ENA had an opportunity to acquire up to 60 Bcfe of gas, over a five-year period, for up to $117 million, by entering into a prepaid agreement with a special purpose entity of EEX Corp., a Houston-based independent oil and gas company. He noted that gas reserves would secure the prepay agreement and that the transaction was similar to a volumetric production payment. He stated that it was ENA's intention to fully syndicate the prepay exposure and that, therefore, the fundamental risk remaining would be bank syndication risk. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Belfer, and carried, the proposed project was approved for recommendation to the Board.

Mr. Winokur revised the agenda and noted that the discussion of the revision to the Enron Corp. Risk Management Policy had already occurred in the joint Finance and Audit and Compliance Committee meeting.

He then called upon Mr. Causey to discuss a proposed subsidiary preferred stock financing. Mr. Causey stated that, as part of the Company's overall financing plan, the Company was proposing the sale of up to $2.2 billion of securities to an investor group not affiliated with the Company. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Belfer, and carried, the proposed sale of securities was approved for recommendation to the Board.

Mr. Causey then discussed a proposed sale of a portion of the Company's interest in Empresa de Generacion Electrica Bahia Las Minas, S.A. in Panama (the "Panama project"). He noted that when the Board approved the Panama project in November of 1998 it did not give specific authorization allowing a sell-down of the Company's ownership interest even though that was the Company's intent. Following a discussion, upon motion duly made by Mr. Urquhart, seconded by Mr. Blake, and carried, the authorization to sell-down an interest in the Panama project was approved for recommendation to the Board.

Mr. Winokur then called upon Mr. Buy to present any additional business. Mr Buy distributed a deal approval sheet relating to a contract extension with Eastern Power & Energy Trading Ltd. ("Eastern"), a copy of which is filed with the records of the meeting. He noted that the Company's current contract with Eastern expired on June 1, 2018 and that the contract extension would lengthen the expiration date until June 1, 2022. He also stated that the Company was currently working on a transaction, expected to be completed in 2000, to reduce its financial and credit exposure to Eastern. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr Chan, and carried, the extension of the Eastern contract was approved for recommendation to the Board.

There being no further business to come before the Committee, the meeting was adjourned at 5:45 p.m., C.S.T.

Rebecca C. Carter
Secretary

APPROVED:

Chairman

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MINUTES
MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
December 14, 1999

Minutes of a meeting of the Board of Directors of Enron Corp. ("Company") held pursuant to due notice at 8:00 a.m., C.S.T., on December 14, 1999 at the Enron Building in Houston, Texas.

All of the Directors were present, as follows:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. John H. Duncan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Ms. Rebecca Mark-Jusbasche
Dr. John Mendelsohn
Mr. Jerome J. Meyer
Mr. Paulo Ferraz Pereira
Mr. Frank Savage
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

The meeting began in executive session, during which Messrs. James V. Derrick, Jr. and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, were also in attendance. Messrs. Robert B. Butts, Richard A. Causey, and Mark E. Koenig, all of the Company, joined the executive session in progress as noted.

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Lay stated that minutes of meetings of the Board held on September 17, 1999 and October 11-12, 1999 had been distributed to the Directors and were

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EXHIBIT #56e

Distributed 3/13

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RESOLVED FURTHER, that upon execution of such amendment prepared according to the above provisions, such amendment shall be deemed adopted by this Board and is hereby ratified and approved; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel are hereby authorized, empowered, and directed to take all such further action, to amend, execute, and deliver all such instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses, as in their judgment may be necessary, appropriate. or advisable in order fully to carry into effect the purposes and intentions of this and each of the foregoing resolutions, including the execution of any further amendments, forms, or documents recommended by counsel or required by any governmental agency, and to do anything necessary to effect compliance with applicable law or regulation.

Mr. Lay called upon Dr. Jaedicke to report on the Audit and Compliance Committee's meeting held on December 13, 1999. Dr. Jaedicke stated that Mr. David B. Duncan, of Arthur Andersen, LLP, had given a status report on the Company's internal controls and commented that all controls were adequate or better and had shown improvement from the prior year. He stated that Mr. Causey had given a very favorable report on the Company's Year 2000 ("Y2K") readiness. He noted that the Committee also heard a report from Ms. Sharon A. Butcher, of the Company, and representatives of Vinson and Elkins, L.L.P. regarding the Company's compliance during 1998 with its Conduct of Business Affairs Policies.

Mr. Winokur reported on the Joint Audit and Compliance and Finance Committee meeting that was held on December 13, 1999. He stated that Mr. Richard B. Buy presented a detailed analysis of the Company's strategic and merchant assets including an overview of the percentage of performing versus non-performing assets by category. He noted that Mr. Buy also gave a presentation on the Company's risk perspective regarding EnronOnline and Enron Energy Services, LLC ("EES").

Mr. Winokur then reported on the Finance Committee meeting that was held on December 13, 1999. He stated that the Committee discussed different scenarios regarding the potential utilization of the proceeds to be received from the Company's sale of Portland General Electric Company and the impact each scenario would have on the Company's key financial ratios. He noted that the Company would complete approximately $21 billion in financings in 1999 and commented on two new products that the Company was introducing into the insurance markets. He stated that the Finance Committee had approved the following items for recommendation to the Board: 1) a revision to the Company's Cash Management Policy, 2) an Enron Caribbean/Middle East project that would require an initial investment of $30 million to develop a three Bcf/day gas pipeline system from Qatar through UAE to Oman in partnership with the UAE government and Elf Acquitaine, 3) a proposal for three business units of the Company to purchase a combined total of 38 turbines for a total cost of $919 million, 4) a project proposed by ENA to acquire up to 60 Bcfe of gas, over a five-year period, for up to $117 million, by entering into a prepaid agreement with a special purpose entity of EEX Corp., a Houston-based independent oil and gas company, 5) proposed revisions to the Enron Corp. Risk Management Policy, primarily relating to changes in the position limits in Europe, that had been discussed in the Joint Audit and Compliance and Finance Committee meeting, 6) a proposed subsidiary preferred stock financing, 7) a proposed sale of a portion of the Company's interest in Empresa de Generacion Electrica Bahia Las Minas, S.A. in Panama, and 8) a proposed contract extension with Eastern Power & Energy Trading Ltd. He moved approval of the revisions to the Enron Corp. Risk Management Policy and the other proposals discussed, his motion was duly seconded by Mr. Urquhart, and carried, and the following resolutions were approved:

Revision to Cash Management Policy

RESOLVED, that the Cash Management Policy (the "Cash Management Policy") be, and the same hereby is, approved and adopted, in the form presented to and discussed at this meeting, a copy of which is attached to the minutes of the meeting as Exhibit I;

RESOLVED FURTHER, that the Cash Management Policy shall supersede and replace all prior policies or guidelines relating to the cash management process; and

RESOLVED FURTHER, that the Chairman of the Board, the Vice Chairman of the Board, the President, the Chief Financial Officer, the Treasurer, any Deputy Treasurer, and any Assistant Treasurer of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Subsidiary preferred stock financing

WHEREAS, it is in the Company's best interest to provide financing and liquidity for affiliates of the Company; and

WHEREAS, it is anticipated that the Company and/or its affiliates may engage in a financing transaction through the sale of up to $2,200,000,000 of securities to an investor or investor group not affiliated with the Company (the "Investor") (such action, together with all other actions to be taken in connection therewith, the "Transaction");

NOW, THEREFORE, IT IS RESOLVED, that the Company hereby authorizes the implementation of all actions deemed necessary and appropriate to the Transaction and approved and executed by officers or representatives of the Company acting on the advice of counsel, which shall be conclusively evidenced by their signatures on such contracts and agreements;

RESOLVED FURTHER, that the Transaction and all arrangements relating to them in a form acceptable to the officers and representatives of the Company acting on the advice of counsel be, and hereby are, approved;

RESOLVED FURTHER, that the Chairman of the Board, the President, any Senior Vice President, any Managing Director, any Vice President, the Treasurer, and any Deputy Treasurer of the Company be, and each of them hereby is, authorized and empowered on behalf of the Company to take such actions as are necessary or appropriate to effectuate the intent of these resolutions;

RESOLVED FURTHER, that all actions heretofore taken by any officer or representative of the Company related to or in connection with the Transaction and the matters described in these resolutions, including without limitation the execution and delivery of any related documents or instruments, are hereby adopted, ratified, confirmed, and approved in all respects; and

RESOLVED FURTHER, that the officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action to amend, execute, and deliver all such further instruments and documents for and in the name and on behalf of the Company, and to cause the Company to pay all such costs and expenses as are in the judgment of such officer or counsel necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Empresa de Generacion Electrica Bahia Las Minas, S.A. in Panama

WHEREAS, on November 17, 1998, the Board of Directors of the Company approved the acquisition by Enron Internacional Panama S.A. ("EIPSA") of a 51% equity interest in Empresa de Generacion Electrica Bahia Las Minas, S.A. ("Bahia Las Minas") and such acquisition has occurred; and

WHEREAS, as a central element of making this acquisition, the Company planned to sell a portion of its interest in Bahia Las Minas;

NOW, THEREFORE, IT IS RESOLVED, that the Board of Directors of the Company hereby confirms that the delegations of authority to the Office of the Chairman stated in the resolutions of the Board of Directors of the Company dated November 17, 1998 include the authority to authorize and approve the sale of a portion of the Company's ownership interest in Bahia Las Minas; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and the foregoing resolution.

Name	Position
Kenneth L. Lay	Chairman and Chief Executive Officer
Jeffrey K. Skilling	President and Chief Operating Officer
Joseph W. Sutton	Vice Chairman
J. Clifford Baxter	Chief Executive Officer, Enron North America
Mark A. Frevert	Chief Executive Officer, Enron Europe
Joseph M. Hirko	Co-Chief Executive Officer, Enron Communications, Inc.
Stanley C. Horton	Chairman and Chief Executive Officer, Enron Gas Pipeline Group
Kenneth D. Rice	Co-Chief Executive Officer, Enron Communications, Inc.
Lou L. Pai	Chairman, President and Chief Executive Officer, Enron Energy Services, Inc.
Richard B. Buy	Executive Vice President and Chief Risk Officer
Richard A. Causey	Executive Vice President and Chief Accounting Officer
James V. Derrick, Jr.	Executive Vice President and General Counsel
Andrew S. Fastow	Executive Vice President and Chief Financial Officer
Steven J. Kean	Executive Vice President and Chief of Staff
Mark E. Koenig	Executive Vice President, Investor Relations
Michael S. McConnell	Executive Vice President, Technology
Jeffrey McMahon	Executive Vice President, Finance and Treasurer
J. Mark Metts	Executive Vice President, Corporate Development
Cindy K. Olson	Executive Vice President, Human Resources and Community Relations

There being no further business to come before the Board, the meeting was adjourned at 12:10 p.m., C.S.T.

Rebecca C. Carter
Secretary

APPROVED: Kenneth L. Lay
Chairman

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DRAFT

MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
February 7, 2000

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 3:30 p.m. C.S.T., on February 7, 2000, but actually begun at 3:40 p.m., C.S.T., on February 7, 2000 at the Enron Building in Houston, Texas.

All of the Committee members were present, as follows:

Dr. Robert K. Jaedicke, Chairman
Mr. Ronnie C. Chan
Mr. Joe H. Foy
Dr. Wendy L. Gramm
Dr. John Mendelsohn
Mr. Paulo Ferraz Pereira
Lord John Wakeham

Directors Kenneth L. Lay and Jeffrey K. Skilling, Messrs. Robert H. Butts, Richard B. Buy, Richard A. Causey, James V. Derrick, Jr., Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, Messrs. Thomas H. Bauer, David B. Duncan, and D. Stephen Goddard, all of Arthur Andersen LLP ("AA"), and Mr. Ronald T. Astin, of Vinson and Elkins, L.L.P. ("V&E"), also attended the meeting.

The Chairman, Dr. Jaedicke, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Dr. Jaedicke called the meeting to order, noted that a draft of the minutes of the meeting of the Committee held on December 13, 1999 had been distributed to members of the Committee, and called for comments, additions, or corrections. There being none, upon motion duly made by Dr. Gramm, seconded by Dr. Mendelsohn, and carried, the minutes of the meeting of the Committee held December 13, 1999 were approved as distributed. Dr. Jaedicke called upon Messrs. Causey and Duncan to discuss regulatory initiatives.

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Mr. Causey updated the Committee on the final New York Stock Exchange and Securities and Exchange Commission ("SEC") rules regarding audit committees. He highlighted the key changes in the rules since the discussion at the December 13, 1999 Committee meeting including: 1) that the *full* board adopt a formal written charter for the audit committee, 2) a recommendation that the board take appropriate action in response to the outside auditors' report to satisfy itself of the auditors' independence, 3) requiring the proxy statement to include a report from the audit committee stating whether, based upon a review and discussion of the audited financial statements with management, the audit committee recommended to the board that the audited financial statements be included in the company's Form 10-K, and 4) providing a limited "safe harbor" for the new proxy statement disclosures to protect companies and their directors from certain liabilities under the federal securities laws. Mr. Causey then discussed other SEC and AICPA activities and the potential impact on the Company. Representatives from AA and V&E joined him in a discussion of the Staff Accounting Bulletin that formalized the SEC's views regarding a company's evaluation of materiality. Mr. Causey then discussed a Statement on Auditing Standards, issued in December of 1999, that formalized requirements regarding auditors' responsibilities for evaluating and communicating audit adjustments. He outlined the specific items that the Company would need to implement to comply with the new rules and noted the effective date with respect to the Company's filings with the SEC.

Dr. Jaedicke then called upon Mr. Duncan for an audit update. Mr. Duncan stated that AA's financial statement opinion for 1999 would be unqualified and that there were no significant audit adjustments, disagreements with management, or significant difficulties encountered during the audit. He stated that the internal controls opinion would also be unqualified, the 1999 audit was complete, and in AA's professional judgement they remained independent. He discussed the status of proposed audit adjustments and noted that no items were considered significant or indicative of material weaknesses. He commented on selected observations from the Company's 1999 financial reporting and stated that the Company's sophisticated business practices introduced a high number of accounting models and applications requiring complex interpretations and judgement and that the broadness of the SEC business-related disclosure requirements added to the complexity of the Company's financial reporting. A copy of Mr. Duncan's report is filed with the records of the meeting.

Mr. Duncan then discussed the 2000 Internal Control Audit Plan ("the Audit Plan"). He reviewed the Company's key business trends that could impact AA's business risk assessment, the areas of the Company that had high inherent risks, and the Company's key business risks, highlighting the major targeted activities for the audit and key changes from the prior year's audit. Mr. Causey joined him in a discussion of the areas of emphasis in the Audit Plan including portfolio risk management, trading, systems, and certain other basic controls.

Dr. Jaedicke then called upon Mr. Causey for a discussion of the 1999 financial statements ("the Statements"). Mr. Causey noted that all Committee members had received a preliminary copy of the Statements and he discussed some of the changes from the prior year, including the elimination of the Year 2000 and oil and gas reserve disclosures. He commented on the Statement footnotes regarding related party transactions and asset impairments and stated that there was no change from the prior year relating to segment disclosure. Mr. Derrick joined him in a discussion of the legal matters disclosed in the Statements. Mr. Derrick commented on the litigation and other contingencies footnote and stated that it was not significantly different from the prior year's disclosure and that no new items were addressed. Dr. Jaedicke called for any comments or questions and there being none, upon motion duly made by Lord Wakeham, seconded by Mr. Chan, and carried, the Statements were approved for inclusion in the Company's annual report and Form 10-K.

Mr. Causey then distributed a handout addressing the significant reserves included in the Statements, a copy of which is filed with the records of the meeting. He stated that certain reserves related to Portland General Electric Company ("PGE") would be eliminated when the sale of PGE was completed and that prudency and credit reserves throughout the Company are reevaluated monthly.

Mr. Causey then gave an annual report on the personal use by executives and directors of the Company's aircraft. He discussed the direct cost to the Company and the taxable value that was attributed to the individuals.

Dr. Jaedicke then called upon Mr. Murphy for an update on market risk. Mr. Murphy reviewed the 1999 profit and loss and value-at-risk ("VAR") by commodity group. He discussed the returns each commodity group had earned compared to the VAR it had taken and gave an overview of the VAR backtesting performed by the RAC Group to test the accuracy of the VAR calculation. He discussed exposures under a "worst case" scenario of 5%-25% shifts in commodity prices and answered questions from the Committee regarding the United Kingdom power position. He reviewed limit violations for the year, noting that the majority related to profit and loss violations which are less controllable than position or VAR limit violations. He then discussed the Company's VAR as a percentage of market capitalization and of net income and compared the Company's percentages to those of certain other companies in the industry.

Dr. Jaedicke then noted that it was the Committee's responsibility to review the Company's transactions with the LJM1 and LJM2 investment vehicles to ensure that the transactions were done on an arms-length basis. He called upon Mr. Causey for the report. Mr. Causey outlined the transactions that had been completed during the year including a description and the total amount of each transaction. He stated that in his opinion all of the transactions had been negotiated on an arms-length basis.

Dr. Jaedicke called for an executive session and Messrs. Astin, Bauer, Buy, Duncan, Goddard, and Murphy left the meeting.

During the executive session Dr. Jaedicke called upon Mr. Causey to discuss the Company's recommendation to the Committee regarding the appointment of independent public accountants for 2000. Mr. Causey stated that the Company was currently in its third year of a five-year agreement with AA regarding the audit. He discussed AA's qualifications and expertise regarding the Company's operations and stated that it was management's recommendation that AA be appointed the Company's independent public accountants for 2000. Following a discussion, upon motion duly made by Mr. Foy, seconded by Dr. Gramm, and carried, the appointment of AA as the Company's independent public accountants for 2000 was approved for recommendation to the Board.

Directors Lay and Skilling, Messrs. Butts, Causey, Derrick, and Sutton, and Ms. Carter left the meeting and Messrs. Bauer, Duncan, and Goddard rejoined the meeting for an executive session with AA and the Committee. Minutes of this executive session were not recorded for the record.

There being no further business to come before the Committee, the meeting was adjourned at 4:50 p.m., C.S.T.

Secretary

APPROVED:

Chairman

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MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
AUGUST 7, 2000

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 3:00 p.m., C.D.T., on August 7, 2000 at the Enron Building in Houston, Texas.

All of the Committee members were present, either in person or by telephone conference connection, where each member could hear the comments of the other participants and join in the discussion, as follows:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. Jerome J. Meyer
Mr. Paulo V. Ferraz Pereira
Mr. Frank Savage
Mr. John A. Urquhart

Directors Wendy L. Gramm, Ken L. Harrison, Kenneth L. Lay, John Mendelsohn, and Jeffrey K. Skilling, Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, Ben F. Glisan, Jr., David B. Gorte, Mark E. Koenig, Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, also attended the meeting. Directors Robert K. Jaedicke, Charles A. LeMaistre, and John Wakeham and Messrs. James M. Bannantine, Richard A. Lammers, and Brent R. Wiggs joined the meeting in progress as noted below.

The Chairman, Mr. Winokur, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Winokur called the meeting to order, noted that a draft of the minutes of the meeting of the Committee held on May 1, 2000 had been distributed to the Committee members, and called for any corrections or additions. There being none, upon motion duly made by Mr. Meyer, seconded by Mr. Belfer, and carried, the minutes of the meeting of the Committee held on May 1, 2000 were approved as distributed.

Mr. Winokur called upon Mr. Fastow to present the Chief Financial Officer's report, a copy of which is filed with the records of the meeting. Mr. Fastow discussed the Company's current and projected key financial ratios and stated that the ratios were based on the current plan. He noted that certain projected ratios deviated from commitments made to the rating agencies earlier in the year and he discussed the reasons for the deviations. He reviewed the stock trading portfolio and he stated that the all of the positions had been closed by the end of the previous week. He discussed the Company's exposure to changes in interest rates, presented a chart depicting the Company's interest rate sensitive items, and noted the dollar amounts at fixed and at floating interest rates. He commented on the Company's cost of capital and he stated that the Company was still reviewing the equity component of the cost of capital calculation.

Directors Jaedicke and LeMaistre joined the meeting following Mr. Fastow's presentation.

Mr. Fastow called upon Mr. Glisan for the Treasurer's report, a copy of which is filed with the records of the meeting. Mr. Glisan reviewed the liquidity report as of July 25, 2000 and noted that the Company's total liquidity was over $7 billion. He reviewed year-to-date investments and proceeds on sales of assets and he stated that without additional action by the Company the year-end debt balances would be over the target levels. Messrs. Fastow and Skilling joined him in a discussion of the Company's capacity in the bank markets, the constraints facing the Company, and the projected cash flows from new businesses. Mr. Glisan then presented a schedule describing the vehicles the Company was utilizing to manage its balance sheet debt. He discussed Raptor I and Raptor II, previously approved by the Board, and noted that Raptor I was almost completely utilized and that Raptor II would be not be available for utilization until later in the year. He noted that Project Whitewing still had available capacity but that the Company was proposing an additional Raptor structure, Raptor III, to increase available capacity. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Meyer, and carried, the Raptor III transaction was approved for recommendation to the Board.

Mr. Winokur called upon Mr. Buy to present the Chief Risk Officer's report, a copy of which is filed with the records of the meeting. Mr. Buy discussed the composition of the Company's merchant portfolio as of June 30, 2000 and any significant changes since the May Board meeting. He commented on the significant increase in the Company's credit exposure and he noted that it was primarily driven by increases in gas and power prices in North America and a decrease in power prices in Europe. He reviewed a detail of non-performing debt instruments and the Company's top 25 credit exposures. He stated that the Company was still working to reduce its over $1 billion exposure to TXU Europe Energy Trading Ltd., a BBB+ rated company. He reviewed the top 10 countries where the Company had the largest trade credit exposure and he noted that the U.S., Canada, and the U.K. combined contributed over 96% of the Company's total trade credit exposure. He commented on the significant increase in the Company's credit reserve and he noted that it was caused by the considerable increase in prices and volumes marketed. He presented the Company's equity investment portfolio detailed by industry, geographic region, and performance measurements. He discussed the Company's equity investments that were performing below expectations and he stated that the assessments were made on a qualitative basis by comparing current expectations to original expectations and did not imply that the assets needed to be written-down. He noted that any write-downs taken on investments were shown on the troubled asset detail. Messrs. Skilling and Sutton joined him for a discussion of the international investments included in the troubled assets detail and a general discussion of Project Summer.

Mr. Buy then discussed the Company's ten top and bottom performing investments and commented on investments new to the list since the first quarter. He postponed the foreign exchange project update, included in the meeting materials, until a later meeting. He briefly discussed Project Doorstep, a review by the Company, with assistance from Arthur Andersen LLP, of the Company's remote offices to ensure the establishment and maintenance of the Company's global standards.

Mr. Buy then presented the Market Risk Update and discussed the returns each commodity group had earned compared to the Value-at-Risk ("VAR") it had taken. He noted that the Company's overall return on VAR was greater than any of the individual commodity groups' returns due to the benefits of diversification. He gave an overview of the VAR backtesting, stress testing, and the Company's exposure under "worst case" scenarios of 5% and 25% shifts in commodity prices. He reviewed limit violations during the second quarter of 2000, noted that the majority of the violations had occurred in the gas portfolio, and discussed the reasons for the violations.

Director Wakeham and Messrs. Bannantine, Lammers, and Wiggs joined the meeting.

Mr. Buy then discussed proposed changes to the Enron Corp. Risk Management Policy ("the Policy"). He stated that the Company was recommending that the Policy be amended to increase the aggregate VAR limit by $15 million. He noted that the Executive Committee of the Board had approved a temporary increase in the aggregate VAR limit at a meeting on June 1, 2000 with the recommendation that the increased VAR be submitted to the Board. He discussed how the additional VAR limits would be allocated to the commodity groups and he noted that there was not a corresponding increase in the volumetric limits. He then discussed certain proposed limit increases to existing commodity groups within the Policy, including Metals and Minerals, Continental Electricity, and Nordic Electricity, and certain revisions to the Policy recommended to better reflect current practice and to add clarity to roles and responsibilities. He stated that there was a proposal to increase the North American Electricity position and VAR limits if the Company was successful in its bidding for certain power purchase arrangements in Canada, as approved by the Executive Committee of the Board at the July 31, 2000 meeting. He then mentioned actions taken by the Company's management, under the Interim Trading Policy, since the May 2, 2000 Board meeting. Following a discussion, upon motion duly made by Mr. Urquhart, seconded by Mr. Belfer, and carried, the proposed revisions to the Policy were approved for recommendation to the Board.

Mr. Winokur left the meeting and with the Committee's permission Mr. Blake acted as Chairman and presided for the remainder of the meeting. Mr. Blake changed the order of the agenda to discuss Project Tammy during the executive session of the meeting.

Mr. Blake called upon Mr. Bannantine to present the proposed Enron South America ("ESA") transactions. Mr. Bannantine began his presentation, a copy of which is filed with the records of the meeting, by discussing how the proposed transactions would be impacted if Project Summer was completed. He then stated that ESA was proposing three transactions, including: 1) the RioGen Merchant Plant, 2) financing related to the Cuiabá Integrated Energy Project ("Cuiabá"), and 3) a buyout of Transredes' interest in Cuiabá. He began with the RioGen project and stated that ESA had the opportunity to build capacity in a power market that was short power. He stated that the RioGen project was to build, own, and operate a 355-megawatt skid mounted merchant power plant near Rio de Janeiro, Brazil. He noted that the transaction would be structured to minimize the downside risk while retaining significant upside potential. He noted that Petrobras, the national oil and gas company of Brazil, was willing to provide a minimum investment return guarantee in order to increase its sales of natural gas and to obtain a minimal participation in the upside of the power plant. He reviewed the Brazilian market fundamentals and he noted that ESA was projecting that an energy shortage would occur during the next three to five years thereby driving up the price of power. He presented an overview of the transaction structure and he stated that the project was structured to give the Company the maximum flexibility and upside potential while providing a guaranteed return on its investment. He noted that the plant would provide a full payback in five years even if it were not utilized. He discussed the assumptions that were used in the project analysis and the economics of the project. He stated that ESA was seeking approval for the remaining $119 million of project costs, with final review and approval delegated to Messrs. Lay or Skilling after the completion of definitive documents, and the approval to utilize eight of the Company's LM6000 turbines. Following a discussion, upon motion duly made by Mr. Belfer, seconded by Mr. Savage, and carried, the proposals were approved for recommendation to the Board.

Mr. Bannantine then discussed the transaction related to the financing of the Cuiabá project. He stated that ESA was seeking approval for commitments required to support a $365 million funding of limited recourse project financing provided by the Overseas Private Investment Corporation and Kreditanstalt für Wiederaufbau and to obtain approval for the Company to also provide Transredes' (a partner in the project) share of the support until Transredes' Cuiabá interest was sold to Shell Cuiabá Holdings Ltd. and Shell Gas (Latin America) B.V. (together with their affiliates, "Shell") or a combination of the Company and Shell. He updated the Committee on the status of the Cuiabá project and reviewed the details of the $365 million in guarantees. He requested that the Committee approve the Company's share of the loan guarantee commitments and authorize the Company to provide up to $46 million of loan guarantee commitments on behalf of Transredes. Following a discussion, upon motion duly made by Mr. Savage, seconded by Mr. Chan, and carried, the proposals were approved for recommendation to the Board.

Mr. Bannantine then discussed a proposal for the Company to participate on an equal basis with Shell in the purchase of Transredes' interest in Cuiabá. He stated that the Company desired to maintain a 50% or greater voting control of Cuiabá to protect the upside value associated with additional Cuiabá projects and he noted that purchasing the additional interest would allow the underlying investment to eventually be sold with a control premium in place. He reviewed the proposed deal structure and detailed the Company's current and proposed ownership in the individual Cuiabá assets. He presented an investment analysis, noted that the Company would be paying a control premium when compared to the analysis performed by the Company's Risk Assessment and Control group, and stated that if Project Summer were completed the additional Cuiabá investment would be treated as a purchase price adjustment. He requested that the Committee recommend to the Board that the authority to approve a capital expenditure of $59.7 million to purchase 50% of Transredes' interest in the Cuiabá project be delegated to Messrs. Lay and Skilling. Following a discussion, upon motion duly made by Mr. Meyer, seconded by Mr. Ferraz, and carried, the proposal was approved for recommendation to the Board.

Mr. Blake called for an executive session at 4:50 p.m., C.D.T., to discuss Project Tammy and Messrs. Bannantine, Buy, Glisan, Gorte, Koenig, Lammers, Murphy, and Wiggs left the meeting.

Mr. Blake called upon Mr. Causey to present Project Tammy. Mr. Causey stated that the Company was proposing the formation of a new company to serve as an intermediate financing vehicle for the Company. He noted that the new company, Enron Finance Partners, LLC ("EFP"), would be created to own certain of the Company's assets. He discussed how transactions would be conducted between the Company and EFP, EFP's plans to raise capital through third parties, and how the capital would be utilized. He stated that the proposal included the formation of EFP, the contribution of certain operating assets into EFP, the assumption by EFP of $1.047 billion of the Company's intermediate and long-term debt, and the sale of $500 million of preferred securities in EFP to outside investors. Following a discussion, upon motion duly made by Mr. Meyer, seconded by Mr. Belfer, and carried, the proposal was approved for recommendation to the Board.

There being no further business to come before the Committee, the meeting was adjourned at 5:00 p.m., C.D.T.

Secretary

APPROVED:

Chairman

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MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
OCTOBER 6, 2000

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 10:00 a.m., E.D.T, but actually begun at 10:35 a.m., E.D.T., at The Breakers, Ponce de Leon III Ballroom, Palm Beach, Florida.

All of the Committee members were present, either in person or by telephone conference connection, where each member could hear the comments of the other participants and join in the discussion, as follows:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. Jerome J. Meyer
Mr. Paulo V. Ferraz Pereira
Mr. Frank Savage
Mr. John A. Urquhart

Directors Duncan, Gramm, Lay, LeMaistre, Mendelsohn, and Skilling, Messrs. Richard B. Buy, Richard A. Causey, Andrew S. Fastow, Ben F. Glisan, Jr., David B. Gorte, Mark E. Koenig, Theodore R. Murphy, and Joseph W. Sutton, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, and Mr. Richard N. Foster, of McKinsey & Company, Inc., also attended the meeting.

The Chairman, Mr. Winokur, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Winokur called the meeting to order, noted that a draft of the minutes of the meeting of the Committee held on August 7, 2000 had been distributed to the Committee members, and called for any corrections or additions. There being none, upon motion duly made by Mr. Meyer, seconded by Mr. Ferraz, and carried, the minutes of the meeting of the Committee held on August 7, 2000 were approved as distributed.

Mr. Winokur called upon Mr. Fastow to present the Chief Financial Officer's report, a copy of which is filed with the records of the meeting.

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #56h

EC 000024420

Mr. Fastow discussed the Company's current and projected key financial ratios and stated that the ratios were based on the current plan. He reviewed the stock trading portfolio and noted that there were currently no open positions. He presented a chart depicting the Company's interest rate sensitive items and noted the dollar amounts at fixed and at floating interest rates. He stated that the Company had recently recalculated its cost of capital utilizing the current estimate of the equity cost component rather than the previous method, which utilized a historical calculation for the equity component. He noted that the new cost of capital calculation would impact the pricing used by the Risk Assessment and Control ("RAC") group when determining the required rate of return on potential projects. He stated that if a project's expected returns where lower than the Company's weighted average cost of capital of 17.17%, then additional syndication or leverage would be necessary.

Mr. Fastow then discussed the Company's private equity strategy and noted that there would be continued significant capital investments by the Company, some of which would not generate cash flow or earnings for a number of years. He stated that this would necessitate syndication of capital investments if the Company were to continue to grow. He discussed the Company's current total assets and the total assets when unconsolidated affiliates were included. He then noted that management was proposing transacting with a new private equity fund, LJM3, and discussed the Company's rationale for transacting with the fund. He reviewed LJM1 and LJM2, equity funds previously approved by the Board that the Company was already transacting with, and noted the dates of formation, the amount of equity in the funds, and the projects that the funds had invested in. He then discussed how his role in the LJM funds could potentially create a conflict of interest in that he negotiates for the LJM funds when they are making investments in the Company's transactions/business, he receives value from the LJM funds if they perform well, and he must allocate a certain amount of his time to the funds. He then discussed the mechanisms that had been put in place to mitigate any potential conflicts including: 1) his fiduciary responsibilities to the Company, 2) the Office of the Chairman or the Board could ask him to resign from the LJM funds at any time, 3) Messrs. Buy, Causey, and Skilling approve all transactions between the Company and the LJM funds, 4) there is an annual Audit and Compliance Committee review of the Company's transactions with the LJM funds, 5) a review of his economic interest in the Company and the LJM funds is presented to Mr. Skilling, and 6) there is no obligation for the Company to transact with the LJM funds.

Messrs. Causey and Skilling then discussed the benefits to the Company of having the ability to transact with the LJM funds and Mr. Fastow discussed the other investors in the LJM funds. Mr. Blake proposed that the Finance Committee also review transactions between the Company and the LJM funds on a quarterly basis and Mr. Winokur proposed that the Compensation and Management Development Committee review the compensation received by Mr. Fastow from the LJM funds and the Company. The Committee unanimously agreed to the two proposals.

Mr. Fastow noted that in order to allow him to participate as the General Partner of the LJM funds it would be appropriate for the Committee to recommend to the Board the ratification of a decision by the Office of the Chairman that Mr. Fastow's participation in the LJM funds, with the noted conflict mitigation mechanisms in place, would not adversely affect the best interests of the Company. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Meyer, and carried the proposal was approved for recommendation to the Board.

Mr. Fastow then called upon Mr. Glisan for the Treasurer's report, a copy of which is filed with the records of the meeting.

Mr. Glisan reviewed the liquidity report as of September 20, 2000, noted that the Company's total liquidity was currently over $7 billion, and stated that a transaction recently completed would bring the total to approximately $8 billion. He reviewed year-to-date investments and proceeds on sales of assets and noted that during the year there had been fewer assets sales and more capital invested than originally planned. He commented on the financing activity that had occurred since June of 2000 and the financings still to be completed before year end. He noted that certain turbine purchases, previously approved by the Board, were requiring a significant amount of capital investment during the year. He then reviewed the Company's outstanding letters of credit and noted that there was no significant change since the last Committee meeting. He discussed the Company's guarantee portfolio and stated that the significant increase in the volumes transacted by the Company had led to related increases in required guarantees. He then stated that there had not been any change in the Company's ratings by the rating agencies.

Mr. Lay left the meeting following Mr. Glisan's presentation and Mr. Winokur called upon Mr. Buy to present the Chief Risk Officer's report, a copy of which is filed with the records of the meeting.

Mr. Buy discussed the Company's Top 25 credit exposures and commented on the exposure to Owens Corning, which had recently declared Chapter 11 bankruptcy. He also discussed a transaction that was underway to reduce the Company's credit exposure to TXU Europe Energy Trading Ltd. He reviewed the current credit reserve and compared it to the required reserve. He then gave the

Committee a brief update on the RAC group's foreign exchange project currently underway and noted that it was scheduled to be completed in December.

Mr. Buy then gave a status report on the RAC group's review of Enron Energy Services, LLC ("EES"). He discussed EES's business and the different ways it earned money and he presented a summary of EES's net open commodity positions, the associated Value-at-Risk ("VAR"), and the mark-to-market credit exposure. He then reviewed EES's outsourcing transactions and noted that there were two components, demand side management and commodity price risk, associated with the transactions. He presented a chart depicting the capital expenditures made or projected to be made by EES and stated that improvements have been made in developing projects but that actual project implementation was lagging behind the original projections. Mr. Skilling joined him in answering questions from the Committee regarding EES's capital expenditures and the potential implication of the slowdown in project implementation on future earnings.

Mr. Buy then presented the Market Risk Update and discussed the returns each commodity group had earned compared to the VAR it had taken. He then presented the same information by business unit and specific commodity. He gave an overview of the VAR backtesting and stress testing of the Company's exposure under "worst case" scenarios of 5% and 25% shifts in commodity prices. He reviewed limit violations during July and August of 2000, noted that the RAC group was working with the business units to reduce the number of violations, and discussed the reasons for the violations. He discussed the loss notifications during July and August of 2000 and noted that there was a daily loss in the portfolio that had required that Mr. Winokur be notified. Mr. Skilling joined him in a discussion of the reason for the loss and commented that the loss was preceded by a number of days of significant earnings.

Ms. Carter then distributed a supplement to the Chief Risk Officer's report, a copy of which is filed with the records of the meeting. Mr. Buy presented a summary of the Transaction Approval Process ("TAP") including the number of transactions that had been approved by the various levels of management and the Board. He then reviewed the Company's annualized VAR versus trading profits over the last six years and discussed the annualized VAR as a percent of trading profits. He commented on the average daily VAR and the VAR limit as a percent of market capitalization over the last six years and noted that during 2000 the average daily VAR had more than doubled. He stated that management was proposing an increase in the overall VAR and also recommending that a certain amount of the overall VAR limit be deemed discretionary, to be allocated by himself and Mr. Skilling to the business units/commodity groups.

Mr. Savage left the meeting and Mr. Lay returned to the meeting following the presentation.

Mr. Buy then discussed proposed changes to the Enron Corp. Risk Management Policy to incorporate the increased VAR. Following a discussion, upon motion duly made by Mr. Ferraz, seconded by Mr. Chan, and carried, the proposed changes to the Enron Corp. Risk Management Policy presented at the meeting were approved for recommendation to the Board.

Mr. Buy then discussed the proposed changes to the TAP, including the addition of a category of approval for the Office of the Chairman of the Wholesale Energy Operations business unit, the ability of Messrs. Lay and Skilling to give Mr. Buy verbal authority to sign on their behalf on transactions up to $25 million, and an updated region/business unit head listing to reflect recent reorganizations or promotions. Following a discussion, upon motion duly made by Mr. Urquhart, seconded by Mr. Belfer, and carried, the proposed changes to the TAP, as filed with the records of the meeting, were approved for recommendation to the Board.

Mr. Winokur then called upon Mr. Glisan to discuss a proposed equity derivatives authorization. Mr. Glisan noted that the Company periodically enters into equity derivative transactions, including swap transactions, forward sales and purchases, and options. He stated that to clarify the equity derivative resolution currently in place management was proposing some minor modifications. He reviewed the modifications and, following a discussion, upon motion duly made by Mr. Meyer, seconded by Mr. Belfer, and carried, the proposed equity derivatives authorization was approved for recommendation to the Board.

There being no further business to come before the Committee, the meeting was adjourned at 12:20 p.m., E.D.T.

Rebecca C. Carter
Secretary

APPROVED:

Chairman

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EC 000024424

LJM 3

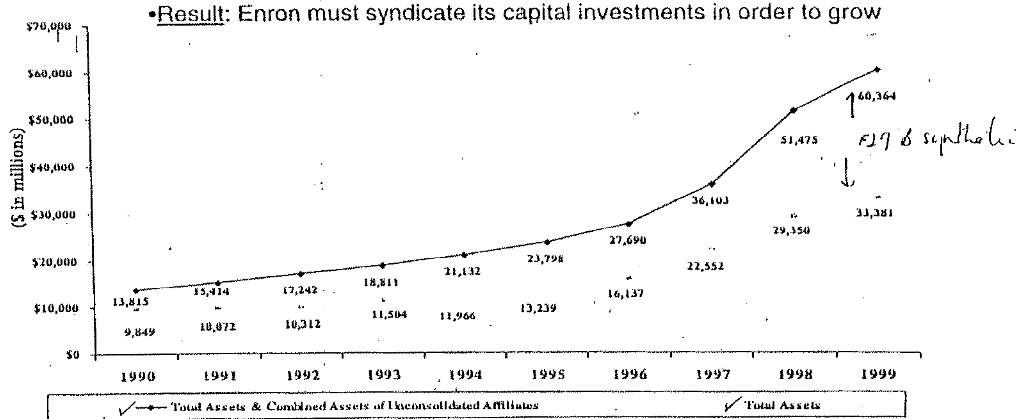
Finance Committee Meeting

EC 000025373

LJM structured to Not be an Enron affiliate

Private Equity Strategy

- Continued significant capital investment by Enron
- Energy and communications investments typically do not generate significant cashflow and earnings for 1-3 years
- Limited cash flow to service additional debt
- Limited earnings to cover dilution of additional equity
- Result: Enron must syndicate its capital investments in order to grow



syndicate or structured transaction

ENRON
Finance Committee Meeting

EC 000025374

Rationale for LJM Structure

- New FASB consolidation rules
- Better ability to manage risk positions (non-affiliate status)
- Better ability to manage financial flexibility

Agenda Item 3

LJM1 and LJM2 Summary

- **LJM1**
  - Formed in June, 1999, with $16 million of equity.
  - Hedged Enron investment in Rhythms NetConnections resulting in a gain of approximately $175 million for Enron.
  - Purchased minority interest in Cuiaba so that Enron could deconsolidate the project.
- **LJM2**
  - Formed in December, 1999, with $394 million of equity.
  - Invested $403 million in 21 transactions.

  500 now

Finance Committee Meeting

7

Conflicts of Interest

- **LJM creates a conflict of interest for EVP/CFO of Enron**
  - Negotiates investments in Enron transactions/business for LJM.
  - Receives value from LJM if fund performs well.
  - Allocates time to LJM matters.
- **Conflict largely mitigated**
  - Board resolution does not relieve A. Fastow of fiduciary responsibility to Enron.
  - OOC or Board can ask A. Fastow to resign from LJM at any time.
  - R. Causey/R. Buy/J. Skilling approve all Enron-LJM transactions.
  - Annual audit committee review of LJM (February).
  - Legal department responsible for maintaining audit trails/files on all transactions.
  - Review of A. Fastow economic interest in Enron and LJM presented to J. Skilling.
  - No obligation for Enron to transact with LJM.

(3) Causey discussed accounting rules (consolidation & special purpose vehicle.) Related party disclosures

(2) Fastow discussed other investors in LJM

LJM has an Advisory Committee

(4) Blake would like finance comm (in addition to Audit) to review the transactions quarterly. Also Comp. Committee look @ Fastow's compensation from LJM & Enron.

(1) JKS - Need non Enron GP to get accounting treatment. Third party transactions would take much longer to do

EC 000025378

Finance Committee Meeting

LJM3

- Follow-on private equity fund to LJM1 and LJM2.
- Purpose: Alternative, optional source of private equity for Enron to manage its investment portfolio risk and financial flexibility.
- Structure to be substantially similar to LJM2.
- Finance Committee/Board of Directors action requested:
  - Ratify decision of Office of Chairman to waive Code of Conduct in order to allow A. Fastow involvement as General Partner of LJM.

Agenda Item 2
RATIFICATION OF DETERMINATION
(Suggested Form of Resolutions)

WHEREAS, Andrew S. Fastow serves as the Executive Vice President and Chief Financial Officer of the Company;

WHEREAS, Mr. Fastow has the opportunity to participate in the formation of an investment partnership (the "Partnership") that would not be affiliated with the Company;

WHEREAS, it is anticipated that Mr. Fastow will serve as the managing partner/manager of the Partnership;

WHEREAS, it is anticipated that the Partnership will invest in, among other things, energy and communications-related businesses and assets, including businesses and assets of the Company;

WHEREAS, the Partnership, as a potential ready purchaser of the Company's businesses and assets or as a potential contract counterparty, could provide liquidity, risk management, and other financial benefits to the Company;

WHEREAS, the Board has evaluated two similar previous investment partnerships in which Mr. Fastow has served as the managing partner/manager and has concluded that the existence of such investment partnerships, and Mr. Fastow's involvement therein, has been beneficial to and in the best interests of the Company;

WHEREAS, the Office of the Chairman of the Company has determined, for the foregoing reasons, that Mr. Fastow's participation as the managing partner/manager of the Partnership will not adversely affect the interests of the Company;

NOW, THEREFORE IT IS RESOLVED, that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Code of Ethics (Conflicts of Interests, Investments, and Outside Business Interests of Officers and Employees) that participation of Mr. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Blake, Meyer

ENRON

Finance Committee Meeting

EC 000025380

TO: AP
2/22/01

INUTES
MEETING OF THE BOARD OF DIRECTORS
ENRON CORP.
OCTOBER 7, 2000

Minutes of a meeting of the Board of Directors of Enron Corp. ("Company") held pursuant to due notice at 8:00 a.m., E.D.T., on October 7, 2000 at the Four Seasons Resort, Poinciana III Ballroom, Palm Beach, Florida.

All of the Directors were present, either in person or by telephone conference connection, where each of the participants could hear the comments by the other participants and join in the discussions, as follows:

Mr. Kenneth L. Lay, Chairman
Mr. Robert A. Belfer
Mr. Norman P. Blake, Jr.
Mr. Ronnie C. Chan
Mr. John H. Duncan
Dr. Wendy L. Gramm
Mr. Ken L. Harrison
Dr. Robert K. Jaedicke
Dr. Charles A. LeMaistre
Dr. John Mendelsohn
Mr. Jerome J. Meyer
Mr. Paulo Ferraz Pereira
Mr. Frank Savage
Mr. Jeffrey K. Skilling
Mr. John A. Urquhart
Lord John Wakeham
Mr. Herbert S. Winokur, Jr.

The meeting began in executive session, during which Messrs. Richard A. Causey, James V. Derrick, Jr., Andrew S. Fastow, Mark E. Koenig, and Joseph W. Sutton and Ms. Rebecca C. Carter, all of the Company, and Mr. Richard N. Foster of McKinsey & Company, Inc., were also in attendance, either in person or by telephone conference connection, where each of the participants could hear the comments by the other participants and join in the discussions. Messrs. Jeremy M. Blachman, Harold G. Buchanan, Daniel P. Leff, Mark S. Muller, Lou L. Pai, Matthew Scrimshaw, Martin Sunde, Greg L. Whalley and Thomas E. White and Ms. Rosalee T. Fleming, all of the Company or affiliates thereof, joined the meeting in progress as noted.

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #56i

CA

The Chairman, Mr. Lay, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Lay called the meeting to order and called upon Mr. Causey to present the Financial and Earnings Report, a copy of which is filed with the records of the meeting. Mr. Causey discussed the third quarter and nine months ended September 30, 2000 diluted earnings per share ("EPS") and compared them to the comparable periods in 1998 and 1999 and to the 2000 Operating Plan. He noted that in both the third quarter and the nine-month period of 2000 the Company's recurring EPS had increased by 23% over the same periods in 1999. He reviewed the earnings by business segment and net income for the third quarter and nine-month periods and compared them to the 2000 Operating Plan. He commented that the increased net income in 2000 was primarily due to stronger performances by the Wholesale Energy Operations and Retail Energy Services business units partially offset by increased corporate expenses. He discussed the Company's balance sheet debt and provided a roll-forward from year-end 1999 balances. He discussed the higher than planned equity investments made during the year, noted that two major items were the purchase of MG plc and the repurchase of the minority interest in Enron Energy Services, LLC ("EES"), and stated that the Company was on-target to meet its year-end credit ratio targets.

Mr. Lay then called upon Mr. Koenig for an Investor Relations update, a copy of which is filed with the records of the meeting. Mr. Koenig reviewed the Company's year-to-date total return to shareholders, of 98.1%, and noted that it continued to substantially exceed the total return achieved by the Company's energy and broadband peer groups, the S&P 500, the Dow Jones Industrial Average, and the NASDAQ. He noted that the Company's energy peer group return had benefited from a very strong performance by Dynegy, Inc. during the year. He presented the year-to-date stock price performance for the Company, the S&P 500, and the NASDAQ and noted that the Company's stock price improvement during the summer was attributable to strong second quarter earnings, the results from the Wholesale Energy Operations group, and the transaction with Blockbuster Video. He reported on the Company's price-to-earnings valuation as of December 1999 and September 2000 and compared them to that of the S&P 500 and the Company's peer group. He reviewed the year-to-date stock price performance of companies in different segments of the energy and utility industries and noted that the diversified natural gas and power companies had the strongest performance. He discussed the expected EPS growth rates for the next two years for the Company, its peer group, and the S&P 500.

Mr. Koenig then reviewed the Company's shareholder composition and the investor style of its institutional investors, noting that 60% were growth-oriented investors while only 17% were value-oriented investors. He commented on the

Company's largest shareholders and discussed changes in ownership since June 30, 2000, particularly by Janus Capital Corporation. He discussed Motley Fool's "Now 50" Index and stated that as of August 31, 2000 the Company's year-to-date total return to shareholders was the highest of any company in the Now 50 Index.

Mr. Lay ended the executive session at 8:30 a.m., E.D.T. and Messrs. Blachman, Buchanan, Leff, Muller, Pai, Scrimshaw, Sunde, and White and Ms. Fleming joined the meeting. Mr. Lay then revised the agenda to begin with the Special Reports/Updates and called upon Mr. Pai to begin the EES presentation, a copy of which is filed with the records of the meeting.

Mr. Pai began his presentation by displaying a chart depicting some of the larger companies that EES had transacted with during the year. He discussed EES's organizational structure, introduced Messrs. Buchanan, Blachman, Leff, Muller, Scrimshaw, and Sunde, and commented on each of the individual's responsibilities. He then discussed contract signings in 1999 and 2000 and noted that EES had achieved eleven quarters of consecutive growth in contract signings. He reviewed revenues, operating expenses, and earnings before interest and taxes for the last two years and commented that the growth in operating expenses typically lagged the growth in revenues. He noted that EES's sources of gross margin included outsourcing, commodity, Enron Facility Services, upselling, EES Europe, and risk management and stated that all sources had shown an increase from 1999 to 2000. He displayed charts showing EES's return on invested capital, noted that the business was not very capital intensive, and discussed EES's intellectual capital base. He then called upon Mr. Sunde to discuss EES North America ("EES-NA").

Mr. Sunde presented an EES-NA organization chart and discussed his team of employees. He stated that his group was migrating to utilizing tools and processes that were new to the EES-NA client base. He then discussed the deals that EES-NA had in the pipeline and the various stages of deal development including: 1) qualification, 2) conceptualization, 3) initial development, 4) detailed development, and 5) signed contracts. He reviewed each of the deal stages and stated that it typically took a transaction 12 to 15 months to go from the initial development stage to a signed contract. He then presented a year-in-review summary of the transactions EES-NA had completed, or would be completing in the fourth quarter, related to the manufacturing/consumer goods, high technology, real estate/financial/healthcare, and education business sectors. He reviewed the structure of EES-NA's risk management books and discussed each of the components, the net open positions, and the number of people involved with each of the books. He commented on the risk management tools employed and noted that the tools and discipline were similar to those used by the Company's Wholesale Energy Operations group. He discussed current market trends, including increasing commodity prices, the deregulation momentum, the increase in companies seeking outsourcing, and a continuation of the evolution of the competitive landscape. He stated that all of the factors would create opportunities for the Company in the coming years. He commented on how the Company was able to quickly respond to changes in the marketplace and discussed the situation in San Diego, California as an example of how the Company could rapidly respond. He commented on the Company's competitors and the potential areas for growth in 2001. He then called upon Mr. Scrimshaw to begin the EES Europe presentation.

Mr. Scrimshaw began by presenting an overview of the European end-use market and noted that the Company had specific products for each market segment including: 1) middle market products for the domestic and small commercial market segment, 2) total energy outsourcing ("TEO") for the commercial and light industrial market segment, and 3) heavy industrial services for large energy-intensive businesses. He presented a schematic of his organization and noted that the team had significant wholesale and retail experience. He began a detailed review of each of the market segments and the products offered by stating that Enron Direct-UK would be providing the middle market products including five-year fixed price discounts to the electricity tariffs and one-to-five year fixed price gas contracts at a single unit rate. He discussed the growth in Enron Direct UK's customer base and market share and noted that the electricity markets were continuing to open throughout Europe. He then stated that Enron Directo-Spain would offer one-to-two year fixed price discounts off the tariff electricity price in Spain, one of EES Europe's primary target countries. He then moved to the market for TEO and discussed the market segment, products to be offered, the business model that would be utilized, and the anticipated competitor response. He commented on the advantages and disadvantages the Company would be facing when promoting TEO in Europe, the estimated total contract value ("TCV") by country and by business segment, and the projects currently under development. He then discussed the heavy industrial services market segment and stated that the Company anticipated providing power, steam, and other key services to petrochemical clients. He noted that the Company would add value through new origination, contract and asset restructuring, and improving fixed costs and stated that no other company was offering a similar comprehensive package to customers. He gave an overview of the targeted customers and discussed the growth prospects for 2001. He then called upon Mr. Leff to begin the Global Energy Services ("GES") presentation.

Mr. Leff noted that GES's goal was to deliver world-class execution services to maximize the value in the Company's network businesses. He described his organizational structure and noted that he worked closely with Messrs. Scrimshaw and Sunde and their respective groups. He stated that GES had three primary objectives: 1) to profitably deliver on all of the Company's contractual commitments, 2) to create incremental value in the existing contract portfolio, and 3) to increase the throughput of products and services to customers. He stated that the first objective involved preparing deals for implementation, performing development engineering management, project and construction management, energy asset management, and operations and labor management. He discussed the Company's delivery platform in North America and stated that the Company was the largest manager of private utility assets utilizing a common global platform. He noted that there had been acceleration throughout the year of the project approval process and that the total net savings related to projects approved in 2000 were estimated to be over $250 million. He discussed savings that were achieved at one customer's facilities when EES invested funds to consolidate the company's chillers leading to increased operating efficiency, reliability, and capacity. He stated that EES also provided labor and maintenance services so that customers did not have to employ a labor force to maintain and operate its assets infrastructure and EES could leverage its experience and scale to drive efficiencies. He stated that GES's second objective related to improving the margins in EES's existing contract base by exercising contract option value, adding additional sites to existing contracts, upselling additional products and services, building scalable tools and processes to enhance value, and providing information back to the organization. He gave an overview of the value enhancement progress made during 2000, the specific details of how it was utilized, and the results at one client. He noted the importance of customer satisfaction ratings, stated that the Company believed a rating of "very good" was necessary in order to receive customer referrals, and noted that GES had exceeded its targeted customer satisfaction goals in 2000. He then reviewed five of GES's transactions and noted the original TCV of the transaction and the enhanced value that had been added since the original signing. He ended his presentation with a discussion of the expectations for 2001 which included expanding and continuing the success of the global execution platform, continuing the web-enhancement of the entire platform, enhancing the scale value, and exceeding customer satisfaction targets. He then called upon Mr. Pai to discuss The New Power Company ("TNPC").

Mr. Blake disconnected from the call following Mr. Leff's presentation.

Mr. Pai discussed the initial public offering ("IPO") of shares of common stock of TNPC and stated that the IPO had been over-subscribed, priced above the anticipated range, and produced net proceeds of $473 million. He stated that TNPC had the opportunity to be the "first mover" in the national energy market and that 50% of the market would be open for competition by the year 2002. He noted that TNPC had unique scale advantages through its strategic partnership with IBM and America Online ("AOL") and would benefit from a cost structure fundamentally lower than that of any competitor. He then stated that the role of each of the partners would be as follows: 1) the Company would provide a commodity cost advantage to TNPC through the use of non-exclusive wholesale buying arrangements and also provide the Company's risk management expertise and software, 2) IBM would provide assistance with the back office operations since IBM was considered the "best in class" regarding unit cost for back office functions and its solutions were scalable to large customer volumes, and 3) AOL would provide exclusive access to over 23 million subscribers that match TNPC's target market. He discussed TNPC's management team and noted that its business plan through the year 2002 was expected to be fully funded through private placements, the IPO proceeds, and profits from operations. He then presented the fully-diluted ownership summary post-IPO. He stated that the Company would have a 45% equity ownership in TNPC, IBM would also have an equity ownership, and AOL would receive equity and cash incentives based on the customers acquired.

Mr. Lay called for a break at 10:30 a.m. E.D.T. and the meeting resumed at 10:40 a.m. E.D.T. with all of the attendees noted above in attendance. Mr. Lay then called upon Mr. Whalley to begin the Enron Net Works ("Net Works") presentation, a copy of which is filed with the records of the meeting.

Mr. Whalley stated that Net Work's mission was to provide the framework for applying the Company's successful wholesale business model to other markets, develop the electronic platforms necessary to increase market share in both current and future markets, and design tools for streamlining support processes valuable to both the Company and other potential users/customers. He then gave the Board an update on the Company's metals business and noted that the utilization of EnronOnline ("EOL") had significantly increased the number of metals transactions completed. He stated that Enron Industrial Markets ("EIM") had been formed to expand the Company's business model into new markets including pulp and paper, lumber, and steel. Mr. Skilling joined him in a discussion of the manner in which the Company's marketing efforts in Japan and Australia were being led by metals marketing with the expectation that gas and power marketing would soon follow. Mr. Whalley then reviewed the EIM organizational structure and stated that funding for EIM would be provided by Enron Net Works Partners LP ("ENWP"), a proposed partnership with outside equity investors that was expected to close by the end of October. He stated that the Company would own approximately 60-70% of ENWP.

Mr. Whalley then discussed the second phase of EOL, noted that there was a highly successful launch on September 18, 2000, and stated that phase II included new trading functionality and market specific content. He stated that there had been a significant increase in the level of business conducted via EOL, the system architecture had proven scalable and reliable, the metals group had been rapidly integrated into EOL, there were commercial agreements in place with competing platforms, and the Company was establishing a private network with 25 of its largest customers in conjunction with Enron Broadband Services. He then provided an update on the status of the Company's DealBench project and noted that it was a secure, collaborative web platform that enabled the Company's clients to conduct business on the web. He commented on the Company's Commodity Logic platform and noted that it provided a web-based solution for companies' commodity mid-office and back-office operations. He stated that in the future Net Works would be analyzing opportunities to expand into other markets including transportation/logistics, agriculture, and the Nymex.

Mr. Lay called for an executive session at 11:25 a.m. and Messrs. Blachman, Buchanan, Leff, Muller, Scrimshaw, Sunde, and White and Ms. Fleming left the meeting.

Mr. Lay called upon Mr. Winokur to report on the Finance Committee meeting held on October 6, 2000. Mr. Winokur stated that at the meeting the Committee had received the standard financial reports and had discussed LJM3, a new private equity fund similar in structure to LJM I and LJM II. He noted that in order to allow Mr. Fastow to participate as the General Partner of the LJM funds it would be appropriate for the Board to ratify a decision by the Office of the Chairman, and recommended by the Committee, that Mr. Fastow's participation in the LJM funds, with noted conflict mitigation mechanisms in place, would not adversely affect the best interests of the Company. He then stated that the Committee also approved the following items for recommendation to the Board: 1) a revision to the Risk Management Policy to allow for an increase in the overall VAR and also to allow a certain amount of the overall VAR limit to be deemed discretionary and to be allocated by Messrs. Buy and Skilling to the business units/commodity groups, 2) a revision to the Transaction Approval Process to address the approval process for projects that do not achieve the Company's required rate of return, and 3) some minor modifications to the equity derivative resolution currently in place. Following a discussion, Mr. Winokur moved approval of the items, his motion was duly seconded by Mr. Meyer, and carried, and the changes to the Enron Corp. Risk Management Policy discussed at the meeting and the following items were approved:

LJM3

WHEREAS, Andrew S. Fastow serves as the Executive Vice President and Chief Financial Officer of the Company;

WHEREAS, Mr. Fastow has the opportunity to participate in the formation of an investment partnership (the "Partnership") that would not be affiliated with the Company;

WHEREAS, it is anticipated that Mr. Fastow will serve as the managing partner/manager of the Partnership;

WHEREAS, it is anticipated that the Partnership will invest in, among other things, energy and communications-related businesses and assets, including businesses and assets of the Company;

WHEREAS, the Partnership, as a potential purchaser of the Company's businesses and assets or as a potential contract counterparty, could provide liquidity, risk management, and other financial benefits to the Company;

WHEREAS, the Board has evaluated two similar previous investment partnerships in which Mr. Fastow has served as the managing partner/manager and has concluded that the existence of such investment partnerships, and Mr. Fastow's involvement therein, have not been adverse to the best interests of the Company; and

WHEREAS, the Office of the Chairman of the Company has determined, for the foregoing reasons, that Mr. Fastow's participation as the managing partner/manager of the Partnership will not adversely affect the interests of the Company;

NOW, THEREFORE, IT IS RESOLVED, that the Board hereby adopts and ratifies the determination by the Office of the Chairman pursuant to the Company's Code of Ethics (Conflicts of Interests, Investments, and Outside Business Interests of Officers and Employees) that participation of Mr. Fastow as the managing partner/manager of the Partnership will not adversely affect the interests of the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and the foregoing resolution.

Revision to the Transaction Approval Process

WHEREAS, the Board of Directors of the Company approved resolutions on October 12, 1998 adopting the Enron Corp. Transaction Approval Process (the "Transaction Approval Process") which provides for (i) a process for review and approval of Capital Expenditures (as defined in the revised policy attached to these minutes) and (ii) a process for prior transactions involving Capital Expenditures to be reviewed for performance and results;

WHEREAS, the Board of Directors of the Company approved amendments to the Transaction Approval Process at meetings held on February 8, 1999, August 10, 1999, February 7th and 8th, 2000, and May 2, 2000; and

WHEREAS, it would be in the best interests of the Company to amend the definitional provisions of the Transaction Approval Process in order to reflect the recent changes in assignments and reorganization of the Company into regional business units and global functions and to reflect amendments to both Approving Units and approval limits with respect to Deal Size;

NOW THEREFORE, IT IS RESOLVED, that the Company revise the Transaction Approval Process to that attached to these minutes and as set forth in these resolutions;

RESOLVED FURTHER, that the revised Transaction Approval Process is adopted and approved, that a copy of the revised policy be attached to the minutes as Exhibit A, and that the persons, officers, and Approving Units identified therein shall perform the responsibilities as specified; for the purposes of this policy a certification by the President, the Chief Financial Officer, the Treasurer, the Chief Risk Officer (or his or her designee), any

Executive Vice President, or any Senior Vice President to the effect that this policy has been complied with in connection with any transaction involving Capital Expenditures shall be conclusive evidence of compliance and may be relied upon by all persons interested in or participating in such transaction, including (without limitation) the officers signing transactional documents on behalf of the Company and attorneys issuing legal opinions with respect to the transaction;

RESOLVED FURTHER, that the revised Transaction Approval Process shall not apply to the approval process for guarantees *except* as to those guaranteeing the obligations of unaffiliated third parties. The approval process for all other guarantees shall continue as described in the Company's existing "Policy for Approval of Guarantees, Letters of Credit, Letters of Indemnity, and Other Support Arrangements" and shall be reviewed by the Finance Group and the Risk Assessment and Control Group;

RESOLVED FURTHER, that the Chairman of the Board and Chief Executive Officer, the President and Chief Operating Officer, the Vice Chairman, the Executive Vice President and Chief Risk Officer, the Executive Vice President and Chief Financial Officer, the Treasurer, any Executive Vice President, Senior Vice President, Managing Director, or Vice President of the Company, or any other person authorized by the Board to act on behalf of the Company be, and each of them hereby is, authorized and empowered to negotiate, enter into, execute, and deliver on behalf of the Company any agreements and documentation in connection with any transaction involving Capital Expenditures which has been approved in accordance with the revised Transaction Approval Process and as the officers executing such agreements shall approve, such approval to be conclusively evidenced by such execution;

RESOLVED FURTHER, that all actions heretofore taken by the Chairman of the Board and Chief Executive Officer, the President and Chief Operating Officer, the Vice Chairman, the Executive Vice President and Chief Risk Officer, the Executive Vice President and Chief Financial Officer, the Treasurer, any Executive Vice President, Senior Vice President, Managing Director, or Vice President, in the name and on behalf of the Company, related to or in connection with transactions of the type contemplated by the new review process attached to these minutes but which originated prior to these resolutions, including, without limitation, the execution and delivery of any instruments or other documents as any such officer shall have deemed necessary, proper, or advisable, are hereby adopted, ratified, confirmed, and approved in all respects; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Equity Derivatives Authorization

WHEREAS, the Company desires to enter into and has entered into equity derivative transactions from time to time relating to the Common Stock of the Company, including, but not limited to swap transactions, forward sales and/or purchases, and options (the "ENE Equity Derivatives Transactions"), which are or may be in addition to obligations or contingent obligations to issue shares of Common Stock of the Company relating to project financings;

NOW, THEREFORE, IT IS RESOLVED, that the Company be, and it hereby is, authorized to enter into ENE Equity Derivative Transactions from time to time, subject to the limitations contained in these resolutions, and on such terms as are approved by the Chairman of the Board, the President, the Vice Chairman, any Executive Vice President, Senior Vice President, Managing Director, or Vice President, the Chief Financial Officer, the Treasurer, or any Deputy Treasurer of the Company (each an "Authorized Officer") and that such transactions heretofore entered into on behalf of the Company are ratified and approved;

RESOLVED FURTHER, that the Company is authorized and directed to execute and deliver any agreements evidencing or relating to ENE Equity Derivative Transaction(s) and to observe and perform in full all of the obligations, conditions, covenants, and other terms set forth in or contemplated by any agreements relating thereto as the same may be amended from time to time;

RESOLVED FURTHER, that each Authorized Officer be, each such officer hereby is, authorized in the name and on behalf of the Company to take or cause to be taken such action as such officer may deem necessary or desirable in connection with the performance by the Company of its obligations under any agreement, document, or instrument contemplated by these resolutions to which the Company is or will become a party;

RESOLVED FURTHER, that each Authorized Officer be, and each of them hereby is, authorized in the name and on behalf of the Company, under its corporate seal or otherwise, to negotiate, execute, deliver, amend, perform, and consummate such agreements, instruments, or documents, however designated, as such officer may deem necessary or desirable to carry out the purpose and intent of the resolutions herein, in such form(s) as shall be approved by the officer executing the same, such approval to be conclusively evidenced by the execution thereof by such officer;

RESOLVED FURTHER, that the maximum number of shares of Company Common Stock for which ENE Equity Derivatives Transactions are written and outstanding at any time ll not exceed 50 million shares;

RESOLVED FURTHER, that up to an aggregate of 20 million shares of Company Common Stock are hereby authorized to be issued pursuant to ENE Equity Derivatives Transactions and up to an aggregate of 20 million shares of Company Common Stock are hereby authorized to be reacquired pursuant to ENE Equity Derivatives Transactions;

RESOLVED FURTHER, that an aggregate of 20 million shares of Company Common Stock are hereby reserved for issuance in settlement of any or all of the ENE Equity Derivatives Transactions referred to above in the event the Company elects to make settlement in shares of Company Common Stock;

RESOLVED FURTHER, that the Company is authorized to issue such shares of Common Stock of the Company in settlement of ENE Equity Derivatives Transactions as deemed appropriate by the officers of the Company and to offer and sell any such shares delivered in settlement of any ENE Equity Derivatives Transaction d that upon any such issuance in accordance with the terms of the bject ENE Equity Derivatives Transaction, such shares of

Common Stock shall be validly issued, fully paid, and non-assessable;

RESOLVED FURTHER, that if registration of shares of the Company's Common Stock is appropriate in connection with any ENE Equity Derivative Transaction, the officers of the Company be, and they hereby are, authorized and directed, for and in the name and on behalf of the Company, to cause to be prepared, executed, and filed with the Securities and Exchange Commission (the "Commission") one or more Registration Statements and/or post-effective amendments to previously filed Registration Statements, including exhibits thereto (collectively, the "Registration Statement"), and such amendments and post-effective amendments to any Registration Statement or supplements to the Prospectuses constituting a part thereof, relating to the registration under the Securities Act of 1933 of the Common Stock of the Company relating to the ENE Equity Derivative Transaction(s) whenever same are appropriate; and the proper officers of the Company are hereby authorized and directed to cause such Registration Statement to be executed and filed in such form as the officers executing such Registration Statement shall approve, such approval to be conclusively evidenced by such execution;

RESOLVED FURTHER, that the officers of the Company be, and they hereby are, authorized and directed to file such amendments or supplements to the Registration Statement(s) referred to above, and to take any or all other action or to do or cause to be done any or all other things as may appear to them to be necessary or advisable in order to cause such Registration Statement(s), as amended, to become effective and otherwise to effect the registration under the Securities Act of 1933 of the appropriate amount of Common Stock of the Company relating to an ENE Equity Derivative Transaction which are covered by such Registration Statement;

RESOLVED FURTHER, that if it is deemed necessary or advisable by the officers of the Company that the Common Stock issuable upon settlement of an ENE Equity Derivative Transaction be qualified or registered for sale under the applicable Blue Sky Laws or securities acts of any jurisdiction, or that a filing be made in any jurisdiction to secure or obtain an exemption from qualification or registration, the officers of the Company are each authorized to perform on behalf of the Company any and all such acts as any one or more of them may deem necessary or advisable in order to comply with such laws of such jurisdiction, and in connection therewith, to execute and file all requisite papers and instruments and to make any and all payments of filing, registration, or other fees, costs, and expenses, and to take any and all further action in connection with the foregoing which any one or more of them shall deem necessary or advisable;

RESOLVED FURTHER, that if required, the Company may make application to the New York Stock Exchange, Inc. and one or more other national securities exchanges for listing of the Company Common Stock to be issued in connection with the ENE Equity Derivatives Transactions; that the Chairman of the Board, the President, any Executive or Senior Vice President, any Managing Director, any Vice President, the Treasurer or any Deputy Treasurer of the Company be, and they hereby are, authorized and directed to execute and deliver any applications, documents, or agreements, to take any and all actions, to appear before such exchanges if necessary, to appoint any banking or other institution as an agent of the Company for any purpose, and to do so or cause to be done any and all things as may appear to them to be necessary or desirable in order to effect such listing;

RESOLVED FURTHER, that the execution by any officer of the Company of any papers and instruments or the performance by any one or more of them of any act in connection with the foregoing resolutions shall conclusively establish their authority therefore from the Company and the approval and ratification by the Company of the papers and instruments so executed and the actions so taken;

RESOLVED FURTHER, that the actions of the officers and employees of the Company acting under the supervision of the officers heretofore taken on behalf of the Company in connection with the above resolutions and the actions contemplated thereby are, in all respects, confirmed and ratified, and the officers of the Company, together or individually, may take any and all action and do any and all things, or direct the taking of such action or the doing of such things by employees of the Company acting under the supervision of the officer(s), as may be deemed by any of them to be necessary or advisable to effectuate the ENE Equity Derivatives Transactions, and the taking of any and all such actions and the performance of any and all such things in connection with the foregoing shall conclusively establish their authority from the Company and the approval and ratification by the Company; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel be, and each of them hereby is, authorized, empowered, and directed (any one of them acting alone) to take any and all such further action, to amend, execute, and deliver all such further instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses as in their discretion appear to be necessary, proper, or advisable to carry into effect the purposes and intentions of this and each of the foregoing resolutions.

Mr. Fastow left the meeting following Mr. Winokur's report.

Mr. Lay called upon Lord Wakeham to report on the Nominating and Corporate Governance Committee meeting held on October 6, 2000. Lord Wakeham noted that the Nominating and Corporate Governance Committee meeting scheduled for October 6, 2000 had not been held and he called upon Ms. Carter to discuss the proposed Directors' Assessment. Ms. Carter stated that she was in the process of developing a Directors' Assessment for the coming year and was looking for input from the Board regarding its format and content and the Board's position regarding individual Director evaluations. The Board then discussed the pros and cons of individual Director evaluations and their experience with them at other companies. Following the discussion the Board unanimously approved Ms. Carter's recommendations on the form and content of the overall Directors' assessment and rejected the proposal regarding individual Director assessments.

Mr. Lay then stated that minutes of a meeting of the Board held on August 1, 2000 had been distributed to the Directors and were included in the meeting material. He called for any additions, corrections, or comments. There being none, upon motion duly made by Mr. Blake, seconded by Mr. Chan, and carried, the minutes of the meetings held August 1, 2000 were approved as distributed.

Mr. Lay then called upon Mr. Duncan to discuss Executive Committee minutes. Mr. Duncan noted that minutes of an Executive Committee meeting held on June 22, 2000 were included in the meeting materials and moved the approval of the minutes. Mr. Duncan's motion was duly seconded by Mr. Savage, and carried, and the minutes of the Executive Committee meeting of June 22, 2000 were approved as distributed.

Mr. Lay called upon Dr. LeMaistre to report on the Compensation and Management Development Committee meeting held on October 6, 2000. Dr. LeMaistre stated that at the meeting the Compensation and Management Development Committee had approved the following items for recommendation to the Board: 1) that the Enron Corp. Flexible Compensation Plan be amended and restated to change the definition of affiliated employers to coincide with the language in the Company's medical plan, 2) that the Enron Corp. 1994 Deferral Plan be restated to include amendments to clarify provisions relative to the deferral of gains realized upon the exercise of stock options, provide consistency with respect to references to the Company's other plans, and clarify current administrative processes and certain other administrative matters, and 3) that the Enron Corp. 1991 and 1994 Stock Plans be amended to expand the guidelines for option transferability to include family charitable foundations. Dr. LeMaistre moved approval of the items, his motion was duly seconded by Dr. Jaedicke, and carried, and the following resolutions were approved:

Enron Flexible Compensation Plan

RESOLVED, that the First Amendment to the Enron Flexible Compensation Plan, a copy of which amendment is directed to be marked for identification and filed with the records of the Company, shall be and is hereby approved and adopted; and

RESOLVED, that the appropriate officers of the Company shall be and they are hereby authorized and directed to execute said amendment on behalf of the Company and to take such other actions and execute such other instruments as they deem appropriate or necessary to carry out the intent of the foregoing resolutions.

Enron Corp. 1994 Deferral Plan

WHEREAS, the Company has heretofore established the Enron Corp. 1994 Deferral Plan (As Restated Effective August 11, 1997) (the "Deferral Plan"); and

WHEREAS, the Company desires to amend and restate the Deferral Plan effective as of October 6, 2000;

NOW, THEREFORE, IT IS RESOLVED, that the proper officers of the Company be, and they are authorized and directed to prepare and execute such amended and restated Deferral Plan on behalf of the Company substantially in the form of the document presented at this meeting;

RESOLVED FURTHER, that upon execution of such restated and amended Deferral Plan, it shall be deemed adopted by this Board and is hereby ratified and approved; and

RESOLVED FURTHER, that the proper officers of the Company and its counsel are hereby authorized, empowered, and directed to take all such further action, to amend, execute, and deliver all such instruments and documents, for and in the name and on behalf of the Company, under its corporate seal or otherwise, and to pay all such expenses, as in their judgment may be necessary, appropriate, or advisable in order fully to carry into effect the purposes and intentions of this and the foregoing resolution, including the execution of any further amendments, forms, or documents recommended by counsel or required by any governmental agency, and to do anything necessary to effect compliance with applicable law or regulation.

Enron Corp. 1991 and 1994 Stock Plans

RESOLVED, that the Sixth Amendment to the Enron Corp. 1991 Stock Plan (As Amended and Restated Effective May 4, 1999), a copy of which amendment is attached hereto and directed to be marked for identification and filed with the records of the Company, shall be and is hereby approved and adopted;

RESOLVED, that the Fourth Amendment to the Enron Corp. 1994 Stock Plan (As Amended and Restated Effective October 12, 1999), a copy of which amendment is attached hereto and directed to be marked for identification and filed with the records of the Company, shall be and is hereby approved and adopted; and

RESOLVED, that the appropriate officers of the Company shall be and are hereby authorized and directed to execute the amendments adopted pursuant to the foregoing resolutions on behalf of the Company and to take such other actions and execute such other instruments as they deem appropriate or necessary to carry out the intent of the foregoing resolutions.

Dr. LeMaistre then stated that the Committee had also spent considerable time during the executive session discussing succession planning at the Company.

Mr. Lay then called upon Dr. Jaedicke to report on the Audit and Compliance Committee meeting held on October 6, 2000. Dr. Jaedicke stated that the Audit and Compliance Committee had received reports from Arthur Andersen LLP regarding current activities at the Company from Mr. Causey relating to control related projects currently underway and from Mr. Derrick relating to the Enron Compliance Report for 1999. The Committee also received a market risk update and an analysis of proposed changes to the Enron Corp. Risk Management Policy.

Mr. Lay then called upon Mr. Skilling for an update on Enron South America ("ESA"). Mr. Skilling distributed a handout relating to a return analysis on ESA's assets, a copy of which is filed with the records of the meeting, and began by discussing the ESA asset monetization strategy. He stated that the Company would be conducting auctions to sell ESA's retail assets, noted the assets to be sold and the current book value, and commented that the closings on the sales would likely occur during the first quarter of 2001. He then compared the electricity demand in the Company's key markets to the demand in Brazil and the Southern Cone. He discussed ESA's lines of business and presented the capital employed, earnings, and anticipated net income for each business. He presented ESA's projected consolidated net income by business unit for the years 2001 through 2003 and discussed the expected net income for 2000 versus the amount of capital employed in the business. He then reviewed the Company's Brazilian wholesale power market strategy and stated that the Company believed that the market fundamentals would continue to lead to an energy shortage and the opening of the markets. He also discussed the RioGen project and stated that it would provide ESA the ability to supply power into a market the Company anticipated being significantly short for the next four to five years.

Mr. Lay called upon Mr. Derrick for a legal update. Mr. Derrick informed the Board of the status of litigation related to a subsidiary of the Company's operations in India and the status of the class action suit related to whether a subsidiary of the Company had taken gas ratably from gas fields within Texas.

Mr. Lay stated that the agenda item related to the approval of the declaration of dividends payable in the fourth quarter of 2000 would be postponed until a later date.

Mr. Lay then noted that due to recent reorganizations within the Company there were certain officer elections that were recommended by management. Upon motion duly made by Mr. Skilling, seconded by Dr. Gramm, and carried, the following resolution was approved:

RESOLVED, that the following persons be, and each hereby is, elected to the position set forth opposite their names, to serve for the ensuing year and until their successors are duly elected and qualified:

David L. Haug	Executive Vice President, Asset Monetization
Tod A. Lindholm	Managing Director, Assurance Service and IT Compliance

Messrs. Derrick and Sutton and Ms. Carter left the meeting, at which time the Board discussed succession planning.

There being no further business to come before the Board, the meeting was adjourned at 12:50 p.m., E.D.T.

Rebecca C. Carter
Secretary

APPROVED: Kenneth L.
Chairman

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MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
FEBRUARY 12, 2001

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 1:30 p.m., C.S.T., but actually begun at 1:40 p.m., C.S.T., on February 12, 2001 at the Enron Building, Houston, Texas.

All of the Committee members were present as follows:

Dr. Robert K. Jaedicke, Chairman
Mr. Ronnie C. Chan
Dr. Wendy L. Gramm
Dr. John Mendelsohn
Mr. Paulo V. Ferraz Pereira
Lord John Wakeham

Directors Kenneth L. Lay and Jeffrey K. Skilling, Messrs. Robert H. Butts, Richard B. Buy, Richard A. Causey, James V. Derrick, Jr., Shawn Kilchrist, Mark E. Koenig, Tod A. Lindholm, and Jordan H. Mintz and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, Messrs. Thomas H. Bauer and David B. Duncan, of Arthur Andersen LLP ("AA"), and Mr. Richard N. Foster of McKinsey & Company, Inc. also attended the meeting.

The Chairman, Dr. Jaedicke, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Dr. Jaedicke called the meeting to order, noted that a draft of the minutes of the meeting of the Committee held on December 11, 2000 had been distributed to members of the Committee, and called for comments, additions, or corrections. There being none, upon motion duly made by Lord Wakeham, seconded by Dr. Mendelsohn, and carried, the minutes of the meeting of the Committee held on December 11, 2000 were approved as distributed.

Dr. Jaedicke called upon Mr. Duncan to begin AA's presentation, a copy of which is filed with the records of the meeting. Mr. Duncan began by providing an update of the status of AA's audit and the communications required by AA under

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the Statement on Auditing Standards 61, "Communication with Audit Committees". He noted that AA's financial statement opinion was expected to be unqualified and that there were no significant audit adjustments, new accounting policies, changes not previously communicated to the Committee, modifications to interim financial information, disagreements with management, significant difficulties encountered during the audit, major issues discussed with management affecting retention, or consultation with other accountants on the application of Generally Accepted Accounting Principles ("GAAP").

Mr. Duncan then discussed AA's opinion on the Company's internal controls and stated that the opinion would be unqualified, the audit was complete, and no material weaknesses had been identified. He stated that Mr. Kilchrist would discuss certain areas where improvement opportunities had been identified. He noted that AA had made its annual determination that, in its professional judgement, it remained independent. He then discussed the status of any adjustments proposed by AA that were not made and noted that management had determined that the items were not material to the Company's financial statements taken as a whole and that AA had concurred.

Mr. Duncan then provided selected observations regarding the Company's accounting procedures and financial reporting. He stated that the Company continued to utilize highly structured transactions, such as securitizations and syndications, in which there was significant judgement required in the application of GAAP. He commented on the use of mark-to-market and fair value model accounting in the areas of trading and derivative contracts and stated that these also required significant judgement regarding the applicability of certain models to specific products or transactions. He then reviewed related party transactions, classification issues that had arisen during the year, and certain other areas requiring material judgments to be made.

Dr. Jaedicke then called upon Mr. Causey to review the significant reserves included in Enron's 2000 financial statements. Mr. Causey distributed a handout, a copy of which is filed with the records of the meeting, listing the reserves in the 1998, 1999, and 2000 financial statements. He commented on reserves relating to Portland General Electric's Trojan facility and Sullivan plant. He then discussed an Enron North America reserve relating to a potential contract settlement, prudency and credit reserves, and certain tax reserves related to years under audit.

Mr. Causey then began a discussion of transactions with LJM during 2000. He stated that the Company had established internal policies and procedures to deal with related party transactions such as LJM. He reviewed the Board established guidelines for transacting with LJM and then began a discussion of the

Company's compliance with the guidelines. He stated that, in response to the Board's direction, the Company had adopted the following procedures and controls: 1) an LJM Deal Approval Sheet ("DASH") was prepared for every transaction between the Company and LJM with approval required by a variety of senior-level Company professionals in the commercial, technical, and commercial support areas and 2) the DASH was supplemented by an LJM Approval Process Checklist that tested for compliance with the Board's directive for transacting with LJM. He then stated that the Company had implemented supplemental efforts regarding transactions with LJM including the following: 1) LJM senior professionals do not ever negotiate on behalf of the Company, 2) Company professionals negotiating with LJM report to senior Company professionals separate from Mr. Andrew S. Fastow, 3) numerous groups monitor compliance with procedures and controls and regularly update him and Mr. Buy, and 4) the Company regularly consults with internal and outside counsel regarding disclosure obligations. He then presented all of the transactions between the Company and LJM during 2000, gave a brief description of each transaction, and noted the notional amount. He noted that the majority of the transactions were non-earnings related and were primarily related to deconsolidations, securitizations, or monetizations.

Dr. Jaedicke then called upon Mr. Derrick to begin the report of legal matters disclosed in Enron's financial statements. Mr. Derrick reviewed the footnote in the Company's financial statements regarding litigation and other contingencies and answered questions from the Committee relating to the disclosure items.

Dr. Jaedicke called upon Mr. Causey to discuss the Company's 2000 financial statements. Mr. Causey stated that the 2000 financial statements would include a new segment, Broadband Services, reflecting the Company's increased activities in this area. He then reviewed certain areas of disclosure relating to the Wholesale Services business segment and discussed the segment's dependence on the origination and completion of transactions, some of which are individually significant and impacted by market conditions, the regulatory environment, and customer relationships. He then distributed updated pages to the financial statements on credit risk and recently issued accounting pronouncements, copies of which are filed with the records of the meeting, and commented on changes in the Company's credit risk from the prior year. He then reviewed the disclosure regarding the impact of changes in accounting principles. Following a discussion, upon motion duly made by Dr. Gramm, seconded by Mr. Chan, and carried, the Committee approved for recommendation to the Board the proposed 2000 financial statements to be included in Enron's annual report and Form 10-K.

Dr. Jaedicke called upon Mr. Causey to discuss the Audit and Compliance Committee Report. Mr. Causey stated that the Securities and Exchange Commission ("SEC") was now requiring a report from the Committee to be included in the Company's proxy statement. He reviewed the report and, following a discussion, upon motion duly made by Mr. Ferraz Pereira, seconded by Dr. Mendelsohn, and carried, the proposed Audit and Compliance Committee Report was approved

Dr. Jaedicke then called upon Mr. Causey to discuss the revised Audit and Compliance Committee Charter ("Charter"). Mr. Causey stated that the Charter was required to be put in the proxy every three years. He stated that the only change to the Charter related to the area concerning the Committee's review of the Company's financial statements and included the addition of the following responsibility: "review with management the Company's policies and practices for communications with analysts". Following a discussion, upon motion duly made by Mr. Ferraz Pereira, seconded by Dr. Gramm, and carried, the proposed Charter was approved for recommendation to the Board.

Dr. Jaedicke called upon Mr. Causey to begin the annual report on executive and director use of corporate aircraft. Mr. Causey reviewed the taxable value, flight hours, and direct cost for each officer who had utilized the Company's aircraft during the year.

Dr. Jaedicke then called upon Mr. Causey to discuss the 2001 Internal Control Audit Plan. Mr. Causey began with a review of the key business trends impacting the Company, including the significant growth in volumes and transactions, a rapid extension of the network model to new markets and locations, an aggressive movement to e-commerce platforms, a growth in Enron Energy Services and Enron Broadband Services, increasing investment in information systems development, the continued use of sophisticated portfolio and capital management practices, and the planned divestiture of various capital intensive assets. He then presented an overview of the Company's business risk assessment and commented that there were no significant changes from the prior year. He displayed a chart of the key business risks, which included the major target activities, and noted that the Company and AA continued to expand their activities into the growth areas at the Company. He commented on the key changes from the prior year in all of the key business risk areas.

He then reviewed the planned control work effort by business area and business unit for the year 2001, compared them to the years 1998 through 2000, and stated that the current year's plan was fairly consistent with that of 2000. He then called upon Mr. Kilchrist to discuss certain areas that would be emphasized in

2001. Mr. Kilchrist stated that one of the primary areas of emphasis in 2001 would be the Company's systems. He noted that the core gas and power trading systems were being redesigned and there were new or expanded systems being developed for some of the Company's newer businesses. He then commented on other basic controls that would be emphasized during 2001 and began a discussion of the shared assurance services. He noted that the Company would be working with AA on shared assurance services, stated that his group would be overseeing the internal audit process, and outlined the work that would be performed by AA and the Company. He noted that the Company had formed internal control committees in each of the business units to assist in the implementation of control and process assessment and improvement.

Dr. Jaedicke then called upon Mr. Koenig to review the Company's policies and practices for management's communications with analysts. Mr. Koenig distributed a handout, a copy of which is filed with the records of the meeting, and began with a discussion of the Company's Investor Relations group ("IR group"). He stated that the IR group had a high level of interaction and coordination with the Company's business units, corporate accounting, public relations, finance, and legal to ensure that a consistent message was being delivered. He then reviewed the Company's primary means of communicating with investors and stated that the SEC had recently implemented Regulation FD, which dealt with fair disclosure issues. He noted that this was the first attempt by the SEC to directly regulate communications between public companies and investors and that the regulation required that material developments or expectations must be communicated to all investors simultaneously and transparently. He stated that the SEC's single biggest area of concern regarded selective earnings guidance, and he reviewed the individuals that were and were not subject to Regulation FD. He noted that Regulation FD does not define materiality in regards to what is non-public material information, and he stated that common guidelines under case law precedents would likely apply. He then discussed items that would likely be considered material information, such as events including earnings information, merger and acquisition activity, new products or discoveries, changes in management, and changes in financial condition. He stated that there were no specific Regulation FD mandates but that the Regulation would be satisfied if "the method of public disclosure is reasonably designed to provide broad non-exclusionary distribution of the information to the public". He then reviewed the potential impact of the Regulation on the IR group and their meetings and discussions with analysts and investors.

Dr. Jaedicke then stated that the Credit and Market Risk Update, included on the agenda, would be discussed in the Finance Committee meeting.

Dr. Jaedicke recessed the meeting at 3:15 p.m., C.S.T., on February 12, 2001 and reconvened the meeting, in executive session, at 7:50 a.m., C.S.T., February 13, 2001 at the Enron Building in Houston, Texas.

During the executive session the Committee unanimously approved recommending to the Board that AA be appointed the Company's independent public accountants for 2001.

There being no further business to come before the Committee, the meeting was adjourned at 8:00 a.m., C.S.T.

Secretary

APPROVED:

Chairman

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MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
FEBRUARY 12, 2001

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), noticed to begin at 4:00 p.m. C.S.T., but actually begun at 4:05 p.m., C.S.T., at the Enron Building, Houston, Texas.

The following Committee members were present constituting a quorum:

Mr. Herbert S. Winokur, Jr., Chairman
Mr. Robert A. Belfer
Mr. Ronnie C. Chan
Mr. Jerome J. Meyer
Mr. Paulo V. Ferraz Pereira
Mr. Frank Savage
Mr. John A. Urquhart

Committee member Norman P. Blake, Jr. was absent from the meeting. Directors Wendy L. Gramm, Ken L. Harrison, Kenneth L. Lay, John Mendelsohn, and Jeffrey K. Skilling, Messrs. William S. Bradford, Richard B. Buy, Richard A. Causey, Timothy A. DeSpain, Andrew S. Fastow, Ben F. Glisan, Jr., David G. Gorte, Mark E. Koenig, and Jordan H. Mintz, and Ms. Rebecca C. Carter, all of the Company or affiliates thereof, and Mr. Richard N. Foster, of McKinsey & Company, Inc., also attended the meeting.

The Chairman, Mr. Winokur, presided at the meeting, and the Secretary, Ms. Carter, recorded the proceedings.

Mr. Winokur called the meeting to order, noted that a draft of the minutes of the meeting of the Committee held on December 11, 2000 had been distributed to the Committee members, and called for any corrections or additions. There being none, upon motion duly made by Mr. Winokur, seconded by Mr. Meyer, and carried, the minutes of the meeting of the Committee held on December 11, 2000 were approved as distributed.

Mr. Winokur called upon Mr. Fastow to present the Chief Financial Officer's report, a copy of which is filed with the records of the meeting. Mr. Fastow discussed the Company's current and projected key financial ratios,

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including coverage and leverage ratios, and stated that the ratios were based on the current plan. He noted that during January the Company had purchased approximately one million shares of the Company's stock now held in treasury. He presented a chart depicting the Company's interest rate exposure and noted the dollar amounts at fixed and at floating interest rates. He then reviewed the Company's cost of capital, utilizing the CAPM Black Scholes valuation method, and discussed changes from the last report to the Committee.

Mr. Winokur changed the agenda to discuss the Company's transactions with LJM later in the meeting and called upon Mr. Glisan for the Treasurer's report, a copy of which is filed with the records of the meeting. Mr. Glisan reviewed the liquidity report as of January 29, 2001 and noted that the Company's total liquidity was currently over $8.3 billion. He then reviewed the Company's outstanding letters of credit and discussed the changes since year end. He presented the Company's guarantee portfolio as of year end and noted that required guarantees continued to be higher than normal due to the significant increase in the volumes transacted by the Company. He then stated that there had not been any change in the Company's ratings by the rating agencies but noted that the Company was working on being upgraded to "positive outlook" by Standard & Poors. Mr. DeSpain joined him for a discussion of the zero coupon convertible debt security recently issued by the Company.

Mr. Winokur called upon Mr. Buy to present the Chief Risk Officer's report, a copy of which is filed with the records of the meeting. Mr. Buy distributed a handout titled "Supplemental Schedules", a copy of which is filed with the records of the meeting. He reviewed the Company's major relationship credit exposures and all of the Company's trade credit exposures that were in excess of $50 million. He then discussed the Company's internal rating of each company, the Company's total exposure, and any collateral held by the Company. He noted that only three of the major relationship credit exposures had a below investment grade rating. He then reviewed the cash and other collateral that the Company had received from or paid to its counterparties as of February 8, 2001. Mr. Skilling joined him for a lengthy discussion of the situation in the California energy markets and the efforts by the Company to mitigate its credit exposure.

Mr. Buy then began a discussion of the Company's merchant portfolio and noted that there had been a significant increase in the Company's gross and net credit exposure since the end of the third quarter 2000. He then moved to a discussion of the Risk Assessment and Control ("RAC") group's analysis of Enron Energy Services LLC ("EES"). He noted that EES had made significant progress in continuing to develop projects and obtaining customer approvals and that EES's project installation phase was now ahead of the plan. He stated that the RAC group had completed an energy asset management verification project to evaluate

EES's actual performance relative to its initial engineering estimates. He stated that the total net present value of all projects was close to the original projected value but that the standard deviation was quite high. He noted that the RAC group had determined that the issues facing EES included a wide range of distribution of the energy efficiency of the outcomes and an increased need for a premeasurement process to validate actual energy savings on individual projects. He reviewed the additional steps that were being undertaken by the RAC group to complete the analysis of EES's business and commented on the impact of the California energy crisis on the business efforts. He updated the Committee on the efforts of the EES and RAC task force and Mr. Skilling joined him for a discussion of certain recent management changes at EES.

Mr. Buy then began the market risk update by discussing the profit or loss that each commodity group had earned during 2000 compared to the average Value at Risk ("VAR") it had taken. He then presented the same information by business unit and specific commodity. He reviewed the VAR limit utilization by commodity for each quarter of 2000 and gave an overview of the VAR backtesting. He then presented four stress scenarios that had been analyzed by the RAC group and commented on the potential impact of each scenario on the Company's earnings. He noted that the potential impact of one of the scenarios had already been somewhat mitigated since the analysis was done. He then presented stress testing of the Company's exposure under "worst case" scenarios of 5% and 25% shifts in commodity prices.

Mr. Buy then discussed the Company's foreign exchange exposure by business unit and commented on the amounts that would be recorded in the Company's currency translation account and income statement. He reviewed a sensitivity analysis comparing the Company's foreign currency exposure in South America to that of all the other business units and provided an update on the status of the RAC group's overall foreign exchange project. He then began a discussion of the proposed changes to the Enron Corp. Risk Management Policy ("Policy"). He noted that the first change was to increase the aggregate VAR limit by $25 million and Mr. Skilling joined him for a discussion of the reason for the purposed increase. Mr. Buy then stated that the remaining changes to the Policy related to the following areas: 1) increases to the net open position limit, maturity /gap limit, and/or VAR for certain existing commodity groups, 2) establishing permanent net open position limits, maturity/gap limits, and/or VAR limits for certain commodities currently under the interim limit section of the Policy, 3) providing for notification of limit violations and loss notifications to the President and CEO ("CEO") at the discretion of the Chief Risk Officer ("CRO"), rather than the existing structured reporting, 4) delegation to the CRO of the authority to allocate the discretionary VAR to facilitate a new market-driven allocation framework, rather than requiring both the CRO and the CEO to approve, 5) clarifying certain aspects related to the cross-commodity trading section of the Policy, and 6) specifying the operational control requirement that all trades executed over the telephone must be recorded electronically. Following a lengthy discussion, upon motion duly made by Mr. Ferraz Pereira, seconded by Mr. Chan, and carried, all of the proposed changes to the Policy with the exception of items 3 and 4 above were approved for recommendation to the Board.

Mr. Winokur then called upon Mr. Buy to discuss the proposed changes to the Transaction Approval Process ("TAP"). Mr. Buy stated that the proposed changes to the TAP were recommended to take into account certain reorganizations at the Company and to add capital expenditures to the risk adjusted capital definition to determine the aggregate exposure in transactions. Following a discussion, upon motion duly made by Mr. Ferraz Pereira, seconded by Mr. Urquhart, and carried, the proposed changes to the TAP as presented at the meeting were approved for recommendation to the Board.

Mr. Winokur then called upon Mr. Gorte to begin the Eli Lilly presentation. Mr. Gorte noted that the Board had approved a transaction with Eli Lilly in December of 2000 and stated that the Company was recommending adjustments to the deal structure to: 1) decrease the approved energy asset project capital, 2) add LLC capital and mobilization costs, and 3) add a lease component to finance capital replacement expenditures. He reviewed each of the recommended adjustments and noted that it would not cause a significant increase in the risks of the project. Following a discussion, upon motion duly made by Urquhart, seconded by Mr. Savage, and carried, the proposed adjustments to the Eli Lilly project presented at the meeting were approved for recommendation to the Board.

Mr. Winokur then called upon Mr. Glisan to begin the Project Crane presentation. Mr. Glisan stated that when the Board initially approved Project Crane the resolution did not provide the Company the flexibility to close the transaction on balance sheet and that management was recommending an additional resolution to provide this flexibility. Following a discussion, upon motion duly made by Mr. Meyer, seconded by Mr. Urquhart, and carried, the modification to Project Crane as presented at the meeting was approved for recommendation to the Board.

Messrs. Bradford, DeSpain, Glisan, Gorte, and Koenig and Directors Gramm and Skilling left the meeting.

Mr. Winokur called upon Messrs. Causey and Fastow to review the Company's procedures regarding transactions with LJM and the transactions completed in 2000. Mr. Fastow began with a discussion of the Company's utilization of the LJM vehicles. Mr. Causey reviewed each of LJM's investments with the Company that were made during 2000. He categorized the investments into four areas, balance sheet, hedges, income statement, and other, and presented a brief description of each transaction and the notional dollar amount. He then reviewed the Company's internal policies and procedures that were in place to monitor transactions between the Company and LJM, stated that the items had also been discussed with the Audit and Compliance Committee, and commented that the process was working effectively. He also noted that the Company had implemented supplemental efforts to complement the Board-established guidelines regarding transactions between the Company and LJM.

There being no further business to come before the Committee, the meeting was adjourned at 5:45 p.m., C.S.T.

Rebecca C. Carter

Secretary

APPROVED:

Chairman

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MINUTES
MEETING OF THE FINANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
OCTOBER 8, 2001

Minutes of a meeting of the Finance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 4:30 p.m., C.D.T., at the Enron Building in Houston, Texas.

All of the Committee members were present as follows:

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

Directors John H. Duncan, Kenneth L. Lay, and Charles A. LeMaistre, Messrs. William S. Bradford, Richard B. Buy, Richard A. Causey, Timothy A. DeSpain, Andrew S. Fastow, Mark A. Frevert, Ben L. Glisan, David B. Gorte, Mark E. Koenig, David R. Port, and L. Greg Whalley, and Ms. Paula H. Rieker, all of the Company or affiliates thereof, also attended the meeting. Mr. Richard N. Foster, of McKinsey & Company, Inc., joined the meeting in progress as noted below.

The Chairman, Mr. Winokur, presided at the meeting, and the Secretary, Ms. Rieker, recorded the proceedings.

Mr. Winokur called the meeting to order, noted that a draft of the minutes of the meeting of the Committee held on August 13, 2001 had been distributed to the Committee members, and called for any corrections or additions. There being none, upon motion duly made by Mr. Blake, seconded by Mr. Chan, and carried, the minutes of the meeting of the Committee held on August 13, 2001 were approved as distributed.

Mr. Foster joined the meeting.

Mr. Winokur called upon Mr. Fastow to present the Chief Financial Officer's report, a copy of which is filed with the records of the meeting. Mr. Fastow summarized recent activity for total return swaps and stock repurchases–

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ınd reviewed the Company's total interest rate exposure, including the mix ›etween fixed and floating interest rates. He then reviewed the financial liquidity ›f the Company, noting that the liquidity risk ratio of the Company as of September 26, 2001, was significantly above the minimum ratio required by the Board and that the ratio had decreased since that date but still remained well above Board limits. He indicated that the ratio still resulted in adequate liquidity coverage when tested for very negative market events. Mr. Winokur emphasized the importance of adequate liquidity and suggested continued analysis and scenario testing. Mr. Fastow then discussed other asset monetizations, including certain transactions with similar characteristics to debt financing, and noted the importance of maintaining valuations for the assets at least equal to the monetization values. He also summarized the asset divestiture plan of the Company, which, upon completion at the end of 2002, was expected to yield $4.7 billion of debt reduction and to have a minimal impact on the earnings of the Company.

- Mr. Winokur called upon Mr. Glisan to report on certain restructuring initiatives. Mr. Glisan provided an update on the Dabhol power plant in India. A discussion ensued regarding the status of the resolution of disputes related to the plant. He also described the economics of a structure named Raptor and reported on the recent termination of Raptor and associated financial impacts to the C any, including a $1,000,000,000 reduction to shareholder equity and an approximate $800,000,000 reduction to expected third quarter 2001 earnings. He attributed the earnings reduction to a lack of credit capacity of Raptor to absorb losses associated with the Company's investment in The New Power Company. He also provided an update on the Whitewing structure, indicating that the structure included $2.4 billion of assets and that bonds related to the structure would require funding in September of 2002. He then commented on the structure related to the Company's ownership of Azurix Corp.

Mr. Winokur called upon Mr. Glisan to present the Treasurer Report, a copy of which is filed with the records of the meeting. Mr. Glisan reviewed the Company's active letters of credit and discussed the increased levels since year-end. He presented the Company's guarantee portfolio as of August 31, 2001 and noted an increase in the total guarantees since year-end. He then presented the liquidity forecast, commenting on the sources and uses of funds expected by year-end, the Company's funding activity following the terrorist events on September 11, 2001, financings expected during the remainder of the year, and the generally difficult environment in the capital markets. He presented the Company's key financial ratios, noting that the Company was on target to meet the year-end goals. He then discussed the Company's ratings by the rating agencies, commenting on the stable outlook for the Company at each of the agencies. He further commented that a negative watch was the likely worst ratings outcome for the

Company if general economic funds deteriorated further. He provided an update on the cash impact of the Company's working capital, investing activities, and asset sales initiatives. He reviewed the overall cost of capital to the Company and provided an update on current costs of new financings for Enron and other peer energy companies. Mr. Winokur emphasized the importance of diligently executing straightforward financings in the marketplace.

Messrs. Frevert, LeMaistre, Savage, and Whalley left the meeting.

Mr. Winokur called upon Mr. Buy to present the Chief Risk Officer's report, a copy of which is filed with the records of the meeting. Mr. Buy reviewed the respective roles of the Audit and Compliance Committee and the Finance Committee in monitoring the Risk Management Policy ("Policy") of the Company and in reviewing transactions previously approved. He reported on the implementation of the new Policy and related reporting. He also provided an update on the trade credit portfolio of the Company, noting that there were no significant changes from the prior report dated June 30, 2001. He indicated that the level of credit exposure related to the Company's largest counterparty continued as an area of concern. He then reported on the collateral activity of the Company, indicating that the level of collateral provided to counterparties had reduced from prior levels due to lower commodity prices and that collateral activity in the third quarter had resulted in net cash inflows to the Company.

Mr. Savage joined the meeting.

Mr. Koenig indicated that the deposits had recently become the single largest item in the Company's cash flow statement and that investors expected the Company to achieve strong cash flow from operations, excluding the deposit activity. Mr. Buy then commented on receivables owed to the Company by Pacific Gas & Electric and on the expected impact to the Company's retail credit portfolio of recent economic trends.

Mr. Winokur called upon Mr. Buy to review the Market Risk Update for the Company, a copy of which is filed with the records of the meeting. He reported on the Company's potential capital expenditures relating to transactions currently under review, indicating total potential outflows of cash of approximately $2.5 billion and a probability adjusted level of $877 million of outflows. He reported that these potential outflows should be significantly offset by cash inflows, resulting in $1.5 billion of net outflows and $350 million of outflows on a probability adjusted basis. Mr. Winokur requested a routine update to the information, sorted by the level of risk associated with the proposed expenditures. Mr. Buy then reviewed a risk profile report, indicating that the report format followed the Policy framework and reflected the Company's risk management approach. He reviewed summaries of profit and loss and average Value-at-Risk ("VAR") of the Company's wholesale businesses by both market concentration and major business units. He discussed returns on average VAR by commodity group by both market concentration and major business units. A discussion ensued on the returns experienced by different units, reasonable return expectations in the current environment, and management's assessment of certain business units. Mr. Buy also reviewed the backtesting performed on the aggregate VAR of the Company, a quarterly comparison of the utilization of the VAR limits, and analyses of various scenarios and related potential losses, which fell within acceptable ranges.

A discussion ensued regarding certain new markets entered by the Company and the respective competitive advantages of the Company and acceptable risk management approaches in the new markets.

Mr. Buy then reviewed a liquidity risk ratio analysis, indicating it represented the amount of cash available or committed to the Company relative to the future cash requirements of the Company's trading portfolio. He also discussed the Company's foreign exchange exposure related to Brazilian currency, citing an increase in the cumulative translation adjustment balances of the Company. He then reviewed implementation of procedures to perform on-going reviews of transactions. He also recommended amendments to the Policy, noting that no changes to the aggregate VAR limits were being requested. Following a discussion, upon motion duly made by Mr. Blake, seconded by Mr. Ferraz Pereira, and carried, the proposed amendments to the Policy were approved for recommendation to the Board.

Following a discussion, upon motion duly made by Mr. Belfer, seconded by Mr. Duncan, and carried, the Committee approved to defer the discussion of Project Southwood to the Board meeting.

There being no further business to come before the Committee, the meeting was adjourned at 6:20 p.m. C.D.T.

Secretary

APPROVED:

Chairman

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EXCERPT FROM OCTOBER 8, 2001
AUDIT AND COMPLIANCE COMMITTEE MEETING

Dr. Jaedicke called the meeting to order, noted that a draft of the minutes of the meeting of the Committee held on August 13, 2001 had been distributed to members of the Committee, and called for comments, additions, or corrections. There being none, upon motion duly made by Mr. Ferraz Pereira, seconded by Dr. Mendelsohn, and carried, the minutes of the meeting of the Committee held on August 13, 2001 were approved as distributed.

Dr. Jaedicke called upon Mr. Causey to discuss the Company's earnings results for the third quarter of 2001. Mr. Causey provided a report on the expected earnings results, a copy of which is included in the records of the meeting. He reviewed potential non-recurring earnings items, including items related to impairments of assets planned for sale by Azurix Corp., to the restructuring of the Company's broadband business, and to losses associated with certain investments by the Company. He described the investments contributing to the potential losses and the economics and accounting of certain financial arrangements used primarily to hedge certain investments. Mr. Duncan reported that recent reviews confirmed the prior confidence of AA in the accounting for the investments and the financial arrangements. Mr. Causey then reviewed the expected recurring earnings for the third quarter for each of the new proposed business segments. He also reviewed the quarterly balances of the financial reserves of the Company, including comparative quarterly balances since the end of the last fiscal year. A discussion ensued regarding the components of the reserve balances.

Dr. Jaedicke called upon Mr. Duncan to provide AA's presentation. Mr. Duncan indicated that AA had performed a substantial review of the potential non-recurring items in the quarter previously discussed by Mr. Causey. He indicated that he and Mr. Causey would schedule a conference call with Dr. Jaedicke if additional issues surfaced as a result of the completion of the audit work during the following week, and he reported he was not currently aware of additional issues.

Mr. Causey provided a report on the expected impact on the Company of the Statement of Financial Accounting Standards No. 142 on Goodwill and Other Intangible Assets ("Standards"), a copy of which is included in the records of the meeting. He reported that the Company expected to adopt the Standards in the first quarter of 2002 and to disclose the expected impact by the time of the filing of the Company's third quarter financial statements with the Securities and Exchange Commission. He detailed components of the Company's total $5.8 billion of goodwill, including consolidated and unconsolidated goodwill. He also

EXCERPT FROM OCTOBER 8, 2001
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MINUTES
MEETING OF THE AUDIT AND COMPLIANCE COMMITTEE
OF THE BOARD OF DIRECTORS
ENRON CORP.
NOVEMBER 2, 2001

Minutes of a meeting of the Audit and Compliance Committee ("Committee") of the Board of Directors of Enron Corp. ("Company"), held pursuant to due notice at 9:00 p.m., C.S.T., on November 2, 2001 at the Enron Building, in Houston, Texas.

The following Directors were present, constituting a quorum, either in person or by telephone conference connection whereby each of the participants could hear the comments and discussions by the other participants and join in the discussions, as follows::

Dr. Robert K. Jaedicke, Chairman
Mr. Ronnie C. Chan
Dr. Wendy L. Gramm
Dr. John Mendelsohn
Mr. Paulo V. Ferraz Pereira
Lord John Wakeham

Directors Robert A. Belfer, Kenneth L. Lay, and Charles A. LeMaistre also attended the meeting. Messrs. Richard A. Causey and James V. Derrick, Jr. and Ms. Paula H. Rieker, all of the Company, and Messrs. David B. Duncan, John M. Riley, and D. Stephen Goddard, both of Arthur Andersen LLP ("AA"), also attended the meeting. Director John H. Duncan joined the meeting in progress as noted below.

The Chairman, Dr. Jaedicke, presided at the meeting, and the Secretary, Ms. Rieker, recorded the proceedings.

Dr. Jaedicke called upon Mr. Causey to provide a report on certain matters summarized in an outline provided by AA, a copy of which is included in the records of the meeting. Mr. Causey provided an update on preparation by the Company of responses to the informal inquiry by the Securities and Exchange Commission ("SEC"). Mr. Causey reported that the Company was working with the law firm retained by the Special Committee to the Board, Wilmer, Cutler & Pickering ("WC&P"), to gather detailed financial information and to draft summaries of transactions referenced in the SEC inquiry. He stated that introductory discussions had taken place with Delloite & Touche, the independent accounting firm retained by WC&P.

Mr. Causey also provided an update on financial reporting matters of the Company. He stated that, although previously reviewed and deemed to be immaterial to the financial condition of the Company, AA had recently advised that the Company should restate the $1.2 billion increase in equity previously recognized related to certain of the Company's contingent equity obligations by netting the increase with an associated note receivable, resulting in significant reductions to shareholder equity for each of the quarterly periods subsequent to and including year-end 2000. Mr. Lay stated that the adjustment would likely have had a significantly less impact on the market value of the Company if originally taken in the periods now required to be restated.

Mr. Duncan joined the meeting.

Mr. Causey reported on new facts recently learned pertaining to a special purpose entity ("SPE") named Chewco. He indicated that, due to the sources of Chewco's equity contribution, Chewco was likely to be deemed to have insufficient equity to qualify for deconsolidation to the financial statements of the Company. He further indicated that Chewco had purchased a portion of the equity in Whitewing, another SPE reported as a deconsolidated entity of the Company, and that Whitewing may have invested in other deconsolidated structures, which may also be adversely impacted if Chewco was not deemed to be an entity qualifying for deconsolidation. A discussion ensued on the respective responsibilities of the Company and AA in validating the initial equity contributions of Chewco, the impact to the Company of potentially consolidating the structures, and the process and resources currently deployed by the Company and AA to develop and review the facts to resolve the outstanding issues.

Mr. Causey then advised the Committee that AA had made an error in accounting judgment previously provided to the Company related to a transaction executed in 1999 with LJM1, a partnership managed by a party related to the Company. He indicated that AA had recently determined that a subsidiary of LJM did not have adequate equity to support the obligations of the transaction and now strongly believed that the transactions should be reviewed for restatement. A discussion ensued on reliance by the Company on the prior judgment of AA regarding the transaction, the significant time lapse since the initial judgment, and the potential impact of the changed judgment on the schedule for filing the third quarter Form 10Q with the SEC.

Mr. Duncan then reviewed AA's work plan related to reviews of the

Company's financial statements, including preparation of responses to the SEC inquiry, completion of opinions required for the Company to close new revolving credit facilities for Northern Natural Gas Company and Transwestern Pipeline Company, additional reviews of SPE's planned for the third quarter audit, continuance of work on the annual audit, and review of the Company's financial liquidity and capitalization. Mr. Goddard commented on an article expected in the next day's edition of The Wall Street Journal regarding AA.

A discussion ensued regarding the importance of regular communications between management, AA, and the Committee, in providing adequate time to properly review the Form 10Q for the third quarter, and in responding fully to the SEC inquiry.

There being no further business to come before the Committee, the meeting was adjourned at 9:40 p.m., C.S.T.

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Secretary

APPROVED:

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Chairman

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Attachment I

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
1177 Avenue of the Americas
New York NY 10036
Telephone (212) 596 8000
Facsimile (212) 596 8910

August 17, 1999

Mr. Ben F. Glisan, Jr.
Vice President
Enron Capital Management
1400 Smith Street
Houston, Texas 75002-7369

Dear Mr. Glisan:

You have requested our opinion (the "Opinion") as to the fairness from a financial point of view of the consideration received by Enron Corp. ("Enron" or "the Company") in the transaction effective as of June 30, 1999 between the Company and LJM Cayman, L.P. ("LJM" or "Counterparty") and LJM's subsidiary, LJM Swap Sub, L.P. ("Swap Sub"). The transaction described above is referred to herein as the "Transaction." The Transaction Documents (as detailed herein) between the Company, LJM, and Swap Sub, set forth the principal terms of the Transaction. The Transaction Documents provide, among other things, that the Company received:

1. A $64 million Limited Recourse Promissory Note, which is due on September 30, 1999;
2. A five year Bermudan put option on approximately 5.4 million shares of Rhythms NetConnections Inc. stock; and
3. A restricted stock agreement which fully restricts LJM and its subsidiary, Swap Sub, from selling 3.378 million of the Company's shares for a period of four years, with two exceptions:
   a) $3.7 million of these shares are not restricted and will be liquidated by LJM on or soon after the Transaction date, and the proceeds will be transferred to Swap Sub.
   b) $50 million of the shares may be liquidated by LJM to satisfy the loan covenants of a third party debt obligation or to pay cash taxes.

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Mr Ben F. Glisan, Jr.
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Enron received the preceding three items as consideration for 3.378 million shares of Enron common stock, which is publicly traded with a value of $80.50 per share as of the Transaction Date opening of the NYSE on June 30, 1999.

In connection with our opinion, we have:

(a) considered the following Documents provided by the Company:

1. Amendments to Transaction Documents (Draft dated July 19, 1999);
2. Amended and Restated Agreement of Limited Partnership (Draft dated June 30, 1999);
3. Transfer restriction agreement (Draft dated June 30, 1999);
4. Limited Recourse Promissory Note agreement (Draft dated June 30, 1999);
5. Amendment to Forward Contracts (Four Draft agreements dated June 30, 1999);
6. Security Agreement among LJM Swap Sub, L.P., Enron Corporation, and Chase Bank of Texas (Draft dated June 29, 1999);
7. Presentation to Enron's Board of Directors (Dated June 28, 1999);
8. Memo from Vinson & Elkins LLP (Draft dated June 23, 1999);
9. Put Option Agreement (Signed and dated June 21, 1999),
10. Summary of Principal Terms (Draft dated June 15, 1999);
11. Description of Transaction (Draft dated June 15, 1999);
12. Confirmations of Original Forward Contracts (Signed and dated March 23, 1998 and April 25, 1996); and
13. Description of Soft value created by transaction (Draft with no date).

(b) considered certain financial and other information relating to the Company and the Counterparty that was publicly available or furnished to us by the Company and the Counterparty;

(c) met with members of the Company's Management to discuss the structure and details of the transaction;

(d) considered certain financial data of the Company and the Counterparty and compared that data with similar data for other publicly-held companies in businesses similar to those of the Company;

(e) considered such other information, financial studies, analyses and investigations and financial, economic and market criteria as we deemed relevant and appropriate for purposes of this opinion;

(f) determined a volatility range for Rhythms NetConnections Inc. stock by examining:

- the implied volatility based on the price of newly issued publicly available nine month put options on Rhythms NetConnections Inc. stock
- the observed volatility of comparable companies
- the historical volatility of Rhythms NetConnections Inc. stock

(g) determined a range of appropriate discounts to apply to the put option on Rhythms NetConnections Inc. stock due to the credit risk of Swap Sub.

(h) determined a range of appropriate restricted stock discounts to apply to the 3.378 million Enron shares transferred from Enron to LJM based on:

- Market transactions involving restricted stock
- statements made by investment banks regarding the discount they would require to purchase the restricted stock
- quantitative analysis of both the appropriate discount and the theoretical maximum discount
- discussions with the Securities and Exchange Commission ("SEC") regarding the ability to hedge a restricted stock position

(i) reviewed the indications of valid business reasons for the transaction

- reviewed equity reports to understand Enron's history, business strategy and financial structure
- reviewed credit agency reports to understand how the agencies assign a credit rating to Enron's long term debt
- reviewed the ramifications of this transaction in terms of:

  1) liquidity of merchant assets
  2) funds flow
  3) debt capacity

The results of the analysis are summarized as follows:

Value of Enron shares transferred to LJM	$170 - $223 million
Value of consideration received from LJM	$164 - $204 million

It should be noted that our opinion is based on prevailing interest rates, dividend rates, share price ~~information and market~~ conditions, and other circumstances and conditions existing on June 30, 1999, and our opinion does not represent our view as to the value of the consideration following consummation of the Transaction. Such subsequent actual value of the consideration could be higher or lower than indicated above depending upon

Mr. Ben F. Glisan, Jr.
August 17, 1999
Page 4 of 5

changes in factors such as interest rates, dividend rates, market conditions, general economic conditions and other factors which generally influence the price of securities. Any valuation of securities is only an approximation, subject to uncertainties and contingencies, all of which are difficult to predict and beyond the control of our Firm.

The opinions expressed herein are subject to the following additional qualifications and limitations:

(i) In arriving at our opinion, we have relied upon and assumed, without independent verification, the accuracy and completeness of all financial and other information that was publicly available or furnished to us by the Company.

(ii). We have not made an independent evaluation or appraisal of the assets of the Company, nor have we been furnished with any such appraisals. We have not been requested to, and did not, solicit third party indications of interest in acquiring all or any part of the Company.

(iii) Our services with respect to the Transaction do not constitute, nor should they be construed to constitute in any way, a review or audit of or any other procedures with respect to any financial information nor should such services be relied upon by any person to disclose weaknesses in internal controls or financial statement errors or irregularities.

(iv) Our opinion does not address, and should not be construed to address, either the underlying business decision to effect the Transaction or whether the consideration to be received by the stockholders in the Transaction represents the highest price obtainable. We express no view as to the federal, state or local tax consequences of the Transaction.

(v) Our opinion is based on business, economic, market and other conditions as they exist as of the date hereof or as of the date of the information provided to us.

(vi) This opinion is effective as of the date hereof. We have no obligation to update the opinion unless requested by you in writing to do so and expressly disclaim any responsibility to do so in the absence of any such request.

(vii) We relied on various facts represented to us by Company management which are outlined in the Representation letter dated August 16, 1999.

Based upon and subject to the foregoing, it is our opinion that, as of the date hereof, the consideration received by the Company is fair from a financial point of view.

Mr. Ben F. Glisan, Jr.
August 17, 1999
Page 5 of 5

We will receive a fee as compensation for our services in rendering this opinion. This letter is for the information of Enron's Board of Directors and Management in connection with the Transaction described herein. This opinion may not be quoted or referred to, in whole or in part, filed with, or furnished or disclosed to any other party, or used for any other purpose, without our prior written consent.

Very truly yours,

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
By: Steven J. Stampf

LJM2 CO-INVESTMENT, L.P.

SUPPLEMENT NUMBER ONE TO PRIVATE PLACEMENT MEMORANDUM

December 15, 1999

This Supplement Number One (this "*Supplement*") supplements the Private Placement Memorandum dated as of October 13, 1999 (the "*Private Placement Memorandum*") which described an investment in LJM2 Co-Investment, L.P. (the "*Partnership*"). This Supplement describes certain changes in the terms and conditions related to the Partnership from those described in the Private Placement Memorandum.

This Supplement is intended to summarize certain provisions of the Partnership's Agreement of Limited Partnership (the "*Partnership Agreement*") and the related agreements referred to herein, does not purport to be complete, and is qualified in its entirety by reference to such Partnership Agreement and related agreements.

Please refer to the Private Placement Memorandum for the definition of any capitalized terms not defined herein.

I. Update to Executive Summary

Mr. Ben Glisan, Jr. no longer serves as a Principal on the management team of the Partnership. Mr. Glisan will retain his position of Vice President at Enron's Global Markets Equity Group and will continue to provide investment advice for the Partnership in that capacity.

II. Initial Investments

Commencing at or about the time of the initial closing of the Partnership, the Partnership expects to make investments totaling approximately $93 million in the following Persons (collectively, the "*Initial Investments*"):

Nowa Sarzyna: The Partnership will invest approximately $30 million to acquire an indirect 75% equity interest in the Nowa Sarzyna facility, a gas-fired heat and power station located within a state-owned chemical complex in Poland, from Enron Europe. Electric power will be sold to the state-owned Polish Grid Company under a 20-year contract with prices indexed to the U.S. Dollar every six months. Approximately 90% of the facility's steam capacity will be sold to the on-site chemical company under a 20-year contract. The state-owned Polish Oil and Gas Company will supply fuel

ARTHUR ANDERSEN

To: The Files

From: Dave Duncan
Deb Cash
Patty Grutzmacher
Jennifer Stevenson

Date: December 31, 1999

Subject: LJMII Partnership Structure

Background

We were informed by a senior officer of Enron (CFO) that he saw a unique opportunity to match various capital providers wanting to diversify into sectors in which he had experience with needs Enron and other companies like Enron had for high degrees of third party equity capital. In effect, he wanted to form his own private equity fund similar to others he had observed in the market place which made sizable private investments and whose participants included sophisticated investors. He had explored this notion with other members of Enron's upper management who indicated a willingness for him to develop this idea. He further indicated that both he and they hoped that he could accomplish this and remain with the Company. While he and the Company planned to consider and address the obvious Corporate Governance and Fiduciary responsibility issues, we were asked by he and other members of Enron management to review the entity as it was developed to determine whether necessary features existed which would enable Enron to do transactions with the entity that would result in third party accounting recognition. Our deliberations with respect to such entity are described below.

Structure

On December 20, 1999, a private investment company, LJMII Co-Investment L.P. ("LJMII") was created for the purpose of acquiring or investing in primarily energy-related or communications-related businesses or activities.

LJMII was capitalized at formation with $55 million of equity and $63 million of debt capital. As indicated in the attached diagram (Diagram 1), the equity holders are comprised of a senior officer of Enron (2% ownership and General Partner) and various third party investors (98% ownership). The composition of the 98% third party investor ownership, which were 51 entities in total, are as follows: Financial Institutions (37%), Pension Funds (22%), Independents (19%), Insurance Co. (10%), Other funds (8%) and Foundations (4%). A portion of the debt was provided by an entity that is wholly owned by a joint venture in which Enron is a co-owner, and the remaining debt was provided by a third party bank.

Since LJMII planned to transact at least initially with Enron, we determined that we should view LJMII as an Enron sponsored SPE. We informed Enron that, at some point, we might reconsider our view of LJMII as an SPE and that such reconsideration would be based on the number of third party transactions and the size of those transactions to the operations of the entity as a whole. Since we considered LJMII to be an SPE, we informed Enron and LJMII that we would subject LJMII to the capital and control tests set forth in EITF 90-15 and Topic D-14 before any transactions between the two entities could be given accounting recognition for Enron. Additionally, because of the significant senior officer involvement we needed to determine that 1) the senior officer did not control the partnership and 2) certain criteria existed to provide assurance that all transactions executed between Enron and LJMII involved the input of the outside investors to preclude the appearance of self dealing.

Issues

Date: December 31, 1999

Subject: LJMII Partnership Structure

certain disclosures will be required. We informed the client that the existence of LJMII will need to be disclosed, including the related party that serves as the GP of the partnership, as well as the purpose of the entity. The nature of transactions executed with Enron and Enron affiliates must also be disclosed as well as any associated gains or losses. We will review the filings and other issuances of financial statements to ensure all appropriate disclosure requirements are met.

Conclusion

We concurred with Enron that the necessary capitalization and control features had been met for nonconsolidation of LJMII and that recognition could be given to transactions with LJMII as a third party.

We informed management that this conclusion would need to be reviewed as transactions occurred and that we would need to address the audit evidence we would require (particularly with respect to the valuation of transactions between the two entities) on a case-by-case basis as they occurred.

We discussed these issues with Carl Bass and John Stewart of the Professional Standards Group, who concurred with our conclusions. We also reviewed the formation of this entity and our conclusions with Mike Odom, Practice Director, Bill Swanson, ABA Head, and Mike Lowther, concurring partner.

Additional Note

In addition to the technical accounting issues, we also considered Enron corporate governance issues related to these transactions. We discussed with Enron management (other than the senior officer involved) their planned activities to ensure such issues had been considered. We determined that Enron was receiving advice from internal and external counsel regarding the acceptability of the transactions and planned to disclose the formation of the entity and any contemplated transactions between the entity and Enron with the Finance Committee of the Board of Directors of Enron prior to their completion. In connection with our procedures, we confirmed that all of the above occurred. We also ensured that the Audit Committee was made aware of the entity and related transactions.

Date: December 31, 1999

Subject: LJMII Partnership Structure

1. Is the minimum SPE capitalization requirement met to support nonconsolidation?
2. Does the control structure support nonconsolidation of the entity for Enron Corp. as a result of the related party relationship?
3. What are the necessary disclosures?

Issue 1
EITF 90-15 requires SPE structures to be capitalized with at least 3% third party residual equity. As a result of the senior officer equity ownership (which we determined should not be given any credit when determining whether sufficient capital existed when evaluating potential transactions with Enron), we determined that the required amount of equity would need to be 3.02% as opposed to the normal 3% (to effectively discount for the proportionate share of the officer's ownership). The balance sheet of LJMII consists of $55 million of funded equity capital and $63 million of debt. Total funded third party equity of LJMII is $54 million, as indicated on the attached diagram. As this represented approximately 45% of the total capitalization, we determined that the SPE capital threshold was met with respect to any transaction LJMII may undertake directly with Enron.

Issue 2
Topic D-14 states that the SEC staff believes that for nonconsolidation by the sponsor to be appropriate, the majority owner of the SPE must be an independent third party who has made a substantive capital investment in the SPE, has control of the SPE and has substantive risks and rewards of ownership of the assets of the SPE. The $54 million of LJMII equity that was contributed by third party investors represents a substantive capital investment. As indicated, a senior officer of Enron serves as the GP of LJMII and is therefore in control of day-to-day operations of the partnership. To overcome the presumption of control by the GP (and by association Enron) for purposes of consolidation, we noted that the Partnership Agreement included the provision that the GP can be removed without cause with the recommendation of two-thirds of the AC and a vote of Limited Partners (LP) that represents 75% of the total LP interests. With respect to the inclusion of criteria to ensure LP involvement in transactions with Enron, we noted that an Advisory Committee ("AC") existed with specific duties outlined in the partnership agreement. These duties included, among other things, reviewing and approving all transactions between LJMII and Enron or any of its subsidiaries above certain thresholds. We determined that transactions below the thresholds would probably not be material to Enron, but we informed management we would have to review such situations on a case-by-case basis. We noted that, the AC consists of representatives of the limited partners, all of whom we noted were independent from Enron (2 pension fund representatives, 4 financial institution members, 1 independent and 1 insurance company). Although we noted that the AC members are appointed by the GP, we noted that all other LP had the right to remove any AC member without cause with the consent of 75% of the LP's. We concluded that these provisions were sufficient to overcome the presumption that the GP (and by association Enron) controls and that nonconsolidation of LJMII is therefore appropriate. We informed the client that, while the removal of the GP without cause feature generally was sufficient to overcome a presumption of control by the GP, an important consideration was the reasonableness of the ability of the LP's to do so. We noted that the existing feature (two-thirds of AC and 75% of the LP's) was at the very upper limit of what may be acceptable. We encouraged them to request LJMII to lower these thresholds before any material transactions were consummated.

Issue 3
Since the GP of LJMII is a related party, as transactions are entered into with Enron or its affiliates,

ARTHUR
ANDERSEN

To: The Files

From: Dave Duncan
Deb Cash
Patty Grutzmacher
Jennifer Stevenson

Date: December 31, 1999, as amended, October 12, 2001

Subject: LJMII Partnership Structure

Background
We were informed by a senior officer of Enron (CFO) that he saw a unique opportunity to match various capital providers wanting to diversify into sectors in which he had experience with needs Enron and other companies like Enron had for high degrees of third party equity capital. In effect, he wanted to form his own private equity fund similar to others he had observed in the market place which made sizable private investments and whose participants included sophisticated investors. He had explored this notion with other members of Enron's upper management who indicated a willingness for him to develop this idea. He further indicated that both he and they hoped that he could accomplish this and remain with the Company. While he and the Company planned to consider and address the obvious Corporate Governance and Fiduciary responsibility issues, we were asked by he and other members of Enron management to review the entity as it was developed to determine whether necessary features existed which would enable Enron to do transactions with the entity that would result in third party accounting recognition. Our deliberations with respect to such entity are described below.

Structure
On December 20, 1999, a private investment company, LJMII Co-Investment L.P. ("LJMII") was created for the purpose of acquiring or investing in primarily energy-related or communications-related businesses or activities.

LJMII was capitalized at formation with $55 million of equity and $63 million of debt capital. As indicated in the attached diagram (Diagram I), the equity holders are comprised of a senior officer of Enron (2% ownership and General Partner) and various third party investors (98% ownership). The composition of the 98% third party investor ownership, which were 51 entities in total, are as follows: Financial Institutions (37%), Pension Funds (22%), Independents (19%), Insurance Co. (10%), Other funds (8%) and Foundations (4%). A portion of the debt was provided by an entity that is wholly owned by a joint venture in which Enron is a co-owner, and the remaining debt was provided by a third party bank.

Since LJMII planned to transact at least initially with Enron, we determined that we should view LJMII as an Enron sponsored SPE. We informed Enron that, at some point, we might reconsider our view of LJMII as an SPE and that such reconsideration would be based on the number of third party transactions and the size of those transactions to the operations of the entity as a whole. Since we considered LJMII to be an SPE, we informed Enron and LJMII that we would subject LJMII to the capital and control tests set forth in EITF 90-15 and Topic D-14 before any transactions between the two entities could be given accounting recognition for Enron. Additionally, because of the significant senior officer involvement we needed to determine that 1) the senior officer did not control the partnership and 2) certain criteria existed to provide assurance that all transactions executed between Enron and LJMII involved the input of the outside investors to preclude the appearance of self dealing.

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U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #59b

AAHEC(2)03384.1

Date: December 31, 1999

Subject: LJMII Partnership Structure

__Issues__
1. Is the minimum SPE capitalization requirement met to support nonconsolidation?
2. Does the control structure support nonconsolidation of the entity for Enron Corp. as a result of the related party relationship?
3. What are the necessary disclosures?

__Issue 1__
EITF 90-15 requires SPE structures to be capitalized with at least 3% third party residual equity. As a result of the senior officer equity ownership (which we determined should not be given any credit when determining whether sufficient capital existed when evaluating potential transactions with Enron), we determined that the required amount of equity would need to be 3.02% as opposed to the normal 3% (to effectively discount for the proportionate share of the officer's ownership). The balance sheet of LJMII consists of $55 million of funded equity capital and $63 million of debt. Total funded third party equity of LJMII is $54 million, as indicated on the attached diagram. As this represented approximately 45% of the total capitalization, we determined that the SPE capital threshold was met with respect to any transaction LJMII may undertake directly with Enron.

We discussed this issue with Carl Bass and John Stewart of the Professional Standards Group, who concurred with our conclusions.

__Issue 2__
Topic D-14 states that the SEC staff believes that for nonconsolidation by the sponsor to be appropriate, the majority owner of the SPE must be an independent third party who has made a substantive capital investment in the SPE, has control of the SPE and has substantive risks and rewards of ownership of the assets of the SPE. The $54 million of LJMII equity that was contributed by third party investors represents a substantive capital investment. As indicated, a senior officer of Enron serves as the GP of LJMII and is therefore in control of day-to-day operations of the partnership. To overcome the presumption of control by the GP (and by association, Enron) for purposes of consolidation, we noted that the Partnership Agreement included the provision that the GP can be removed without cause with the recommendation of two-thirds of the AC and a vote of Limited Partners (LP) that represents 75% of the total LP interests. With respect to the inclusion of criteria to ensure LP involvement in transactions with Enron, we noted that an Advisory Committee ("AC") existed with specific duties outlined in the partnership agreement. These duties included, among other things, reviewing and approving all transactions between LJMII and Enron or any of its subsidiaries above certain thresholds. We determined that transactions below the thresholds would probably not be material to Enron, but we informed management we would have to review such situations on a case-by-case basis. We noted that, the AC consists of representatives of the limited partners, all of whom we noted were independent from Enron (2 pension fund representatives, 4 financial institution members, 1 independent and 1 insurance company). Although we noted that the AC members are appointed by the GP, we noted that all other LP had the right to remove any AC member without cause with the consent of 75% of the LP's. We concluded that these provisions were sufficient to overcome the presumption that the GP (and by association Enron) controls and that nonconsolidation of LJMII is therefore appropriate. We informed the client that, while the removal of the GP without cause feature generally was sufficient to overcome a presumption of control by the GP, an important consideration was the reasonableness of the ability of the LP's to do so. We noted that the existing feature (two-thirds of AC and 75% of the LP's) was at the very upper limit of what may be acceptable. We

Date: December 31, 1999

Subject: LJMII Partnership Structure

encouraged them to request LJMII to lower these thresholds before any material transactions were consummated.

Issue 3
Since the GP of LJMII is a related party, as transactions are entered into with Enron or its affiliates, certain disclosures will be required. We informed the client that the existence of LJMII will need to be disclosed, including the related party that serves as the GP of the partnership, as well as the purpose of the entity. The nature of transactions executed with Enron and Enron affiliates must also be disclosed as well as any associated gains or losses. We will review the filings and other issuances of financial statements to ensure all appropriate disclosure requirements are met.

Conclusion
We concurred with Enron that the necessary capitalization and control features had been met for nonconsolidation of LJMII and that recognition could be given to transactions with LJMII as a third party.

We informed management that this conclusion would need to be reviewed as transactions occurred and that we would need to address the audit evidence we would require (particularly with respect to the valuation of transactions between the two entities) on a case-by-case basis as they occurred.

We discussed the formation of this entity and our conclusions with Mike Odom, Practice Director, Bill Swanson, ABA Head, and Mike Lowther, concurring partner, concurred with our conclusions.

Additional Note
In addition to the technical accounting issues, we also considered Enron corporate governance issues related to these transactions. We discussed with Enron management (other than the senior officer involved) their planned activities to ensure such issues had been considered. We determined that Enron was receiving advice from internal and external counsel regarding the acceptability of the transactions and planned to disclose the formation of the entity and any contemplated transactions between the entity and Enron with the Finance Committee of the Board of Directors of Enron prior to their completion. In connection with our procedures, we confirmed that all of the above occurred. We also ensured that the Audit Committee was made aware of the entity and related transactions.

Major Transactions

Largest 10 Transactions

(June 30-December 31)

	Size	Impact	Status
CORP			
Osprey Trust Add-on	$ 1,000 MM	Off-Balance Sheet Acquisition vehicle, allows for positive funds flow	Closed
EOG Stock Monetizaton	$ 500 MM	Positive Funds Flow	Closed
Enron CLN	$ 500 MM	Positive Funds Flow	Closed
Tammy Tax Advantaged Transaction	$ 500 MM	Debt reduction	Closed
SA Turbines	$ 500 MM	Balance Sheet protection	Closed
ENA			
Turbopark	$ 600 MM	Balance Sheet protection	12-15
Chase Prepay	$ 500 MM	Funds Flow	12-15
EEL			
MG Inventory (LME)	$ 750 MM	Balance Sheet protection	Closed
MG Inventory (Non-LME)	$ 1,250 MM	Balance Sheet protection	Closed
TD Prepay	$ 200 MM	Funds Flow	12-01

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ENRON®

Finance Committee Meeting

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #60

Interoffice Memorandum

Confidential Attorney-Client Communications

ENRON

To: Rick Buy
Rick Causey

From: Jordan Mintz

Department: Enron Global Finance--Legal

Subject: **LJM Approval Process -- Transaction Substantiation**

Date: March 8, 2001

With the year-end and recent Board meetings behind us, and our now being in the midst of proxy season, I thought it might be timely to memorialize my observations and summarize my recommendations for refining our compliance with the procedures approved by Enron's Board of Directors (the "Board") with respect to the Company's transacting with LJM. Briefly stated, it is my view that the Company needs to improve both the *process* it follows in executing such transactions and implement improved procedures regarding *written substantiation* supporting and memorializing the Enron/LJM transactions; at the same time, it is also my view worthwhile improvements can be accomplished without significant disruption to commercial efforts.

More specifically, my recommendations focus on two areas: the first is the need for the Company to implement a more active and systematic effort in pursuing non-LJM sales alternatives before approaching LJM, and then to create more extensive written documentation substantiating such efforts; the second is to modify the LJM Approval Checklist so as to impose a more rigorous testing of the fairness and benefits realized by Enron in transacting with LJM -- and balancing such benefits against perception and shareholder relations issues such transactions may present.

To that end, what follows below is: relevant background regarding the Board's approval for transacting with LJM; my "due diligence" findings relating to the Company's compliance with such approval; and recommendations for improvement to be effective for the 2001 year.

Overview

As you know, the sensitivities surrounding Enron's transacting with LJM primarily stem from three areas: whether such transactions are being conducted at arms-length in such a clear and convincing fashion that they will be respected from a GAAP earnings perspective; whether the benefits realized by Enron from such transactions are sufficiently "compelling" from an investor's perspective to negate perceptions, however unwarranted, of an "interested" dealing; and whether such transactions are in the best interests of the Company and, thus far, consistent with the Board's carrying out its fiduciary duties and in compliance with the Company's Code of Ethics. In order to address these three critical and often-overlapping concerns, the Board has previously approved the following procedures and controls:

(1) Enron and LJM are not obligated to one another to transact;

(2) Enron's Chief Accounting and Risk Officers are to review and approve the terms all transactions Enron or an affiliate enters into with LJM;

VEL 00524

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #61

(3) The Board's Audit and Compliance Committee shall annually review all transactions completed that year and make any recommendations they deemed appropriate; and

(4) The Board is to determine, also annually, that Andrew Fastow's controlling position at LJM and his involvement as a counterparty to Enron does not adversely effect the best interests of the Company.

Additionally, although not explicitly provided for by the Board, the Finance Committee also annually reviews all Enron/LJM transactions, but may review on an *ad hoc* basis, as needed.

To supplement the Board's mandated procedures, Enron and LJM also agreed to an additional control precluding Mr. Fastow (and Michael Kopper, also a senior level professional at both Enron and LJM) from negotiating on behalf of Enron in transactions with LJM.

The Company subsequently adopted a written "LJM Approval Sheet" to generally describe the business nature of any Enron/LJM transaction, including the deal terms and anticipated economics to Enron. This Approval Sheet is supplemented with an "Issues Checklist", which captures the procedures to be followed in executing transactions with LJM; in this manner, Enron can test whether it is complying with the Board's directions. (Such Approvals are to be reviewed and executed by certain members of Enron's Senior Management, including Jeff Skilling.) For example, the Checklist provides for the following determinations to be made:

(1) In addition to LJM, identifying other sales options that were considered and rejected, including sales to Condor, JEDI II, and third parties; identifying other banks/offers that were received with respect to the transaction;

(2) Whether the transaction with LJM will be the most beneficial alternative to Enron; identifying the related benefits – cash flow, earnings;

(3) Determining whether the transaction involves a "Qualified Investment" so that it was required to be offered to JEDI II;

(4) Whether the transaction was negotiated at arm's-length; did any advisors conclude that the transaction was *not* fair to Enron;

(5) Whether the transaction had to be disclosed in the Proxy and whether it yielded any monetary benefit to an Enron employee; and

(6) Whether LJM's participation in the transaction has been reviewed by Enron Office of the Chairman ("OTC")? Has it been reviewed and approved by Enron's Chief Accounting and Risk Officers?

And finally, the Checklist asks whether Enron's Board's Audit Committee reviewed all Enron/LJM transactions within the past 12 months.

Findings

The procedures followed by Enron in transacting with LJM, including the manner in which they have been substantiated, should be improved and can be, I believe, with minimum disruption to commercial efforts. I also believe that the adoption of certain of these recommendations will yield material benefits with respect to accounting substantiation and further documentation of the Board's carrying out of its fiduciary duties and business judgment.

The more significant areas for improvement are as follows:

(1) Enron does not consistently seek to negotiate with third parties before it transacts with LJM. No policy exists specifically requiring evaluation and pursuit of third party alternatives before transacting with LJM. Because no existing policy requires the prior evaluation of third party alternatives and, given the fluid nature of the Company's commercial activities, too often Enron finds itself facing a time deadline that makes it difficult (*in fact* often impossible, as a practical matter) to transact with a third party, thus potentially: (a) reducing the benefits Enron realizes from the LJM transaction by eroding Enron's bargaining position; (b) clouding the objective evidence of such benefits (due to a lack of comparable alternatives) and, perhaps; (c) undermining the arm's-length nature of the transaction (due to a lack of both comparable and practical alternatives);

(2) Enron does not always adequately substantiate in writing the procedures it follows with respect to transacting with LJM. For example, some of the questions in the Checklist do not capture the "full picture" of information that would be instructive in demonstrating compliance with Enron's Board. For example:

(a) The Checklist does not require an explanation as to *why* the particular transaction would be the most beneficial alternative for Enron -- only that it is. Requiring an answer to the question of *why* the transaction is beneficial would have the added advantage of requiring that the question be directly addressed by the commercial personnel charged with its execution;

(b) The Checklist does not provide for a detailed explanation/substantiation of sales efforts prior to transacting with LJM (thereby negating a contemporaneous record that could be useful in fashioning appropriate disclosures regarding those transactions required to be disclosed);

(c) The Checklist does not require an explanation as to *how* Enron determined that the transaction was conducted at arm's-length -- only if it was not (which presents the same difficulties as (b));

(d) The Checklist provides for pre-determined, rather than a more "realtime" OTC determination that transacting with LJM does not adversely affect Enron; and

(e) The Checklist does not provide any level of detail regarding the Chief Accounting and Risk's Officer's review and approval; I believe, for the Board's Audit and Finance Committee's benefit, this additional information -- when coupled with formal Board presentations -- would provide additional enhancement to the Board's decision-making as to having all relevant facts before it.

(3) Inherent employee conflicts exist that can contribute to a perception that Enron and LJM *cannot* transact at arm's-length; and

(4) Enron's transactions with LJM create potential conflicts with CalPERS, and perhaps other future "investment parties" with whom Enron may have a relationship.

Particular suggestions for improvements follow. These recommendations for a more "formal" approach for transacting with LJM, however, should not replace or supercede any "commonsense" alternatives that may better allow for flexibility in any commercial/financial transaction and, perhaps, a better balancing of competing interests.

VEL 00526

Recommendations

Adoption of the suggestions that follow should enhance those procedures already in place and being followed for purposes of substantiating Enron's compliance with the Board's directives and, in particular, "completing the Company's files" with respect to responding to audit reviews and preparation of proxy and footnote disclosures. In particular:

(1) Additional education of business units regarding the role to be played by LJM as an alternative counterparty after efforts with "traditional", third party counterparties are exhausted and the Company's expectation that such third parties will be explored before resort to LJM. Further written *substantiation* of such efforts;

(2) Amendments to the Checklist to ensure further written substantiation of *why* this particular transaction with LJM was the *most beneficial* vis-à-vis alternatives, *how* such determination is *substantiated*, and substantiation that the transaction was conducted at arm's-length;

(3) Better contemporaneous involvement by the OTC regarding review and approval of Enron's transacting with LJM, *i.e.* sign-off by Jeff Skilling on a more regular basis;

(4) Mitigation of personnel conflicts by physical separation of all fulltime LJM employees from Global Finance representatives; and

(5) Coordination of LJM Approvals, review, and substantiation documents through an internal group made up of representatives of EGF Commercial, Legal (custodian of the documents), Accounting, and Commercial Support.

Items (2) (4) and (5) above are already being addressed. We can work through the individual business unit CFOs to progress item (1) and, with your concurrence, I can discuss item (3) with Jeff.

Please let me know your thoughts about these recommendations and whether you take exception to my working towards their implementation. Of course, feel free to contact me with any questions you may have.

Thank you for your time.

Cc: Jim Derrick
Rex Rogers
Rob Walls
Ron Astin (Vinson & Elkins)

VEL 00527

Bcc: Ron Baker
Rodney Faldyn
Ben Glisan
George McKean
Gordon McKillop
Ryan Siurek

VEL 00528

Interoffice Memorandum

DRAFT
Confidential Communications
Attorney-Client Privilege

ENRON

> Gene K
> Adv 4/2/01

To: Andy Fastow

From: Jordan Mintz

Department: Enron Global Finance-Legal

Subject: **Related-Party Proxy Disclosures**

Date: March 28, 2001

You will recall that in preparing the LJM related-party disclosure for this year's (2000) Proxy, we did not explicitly provide financial information relating to your serving (ultimately) as the general partner/managing member in either LJM1 or LJM 2. The purpose of this memorandum is to explain our basis for not doing so and why such rationale(s) <u>may not</u> be applicable in future filings.

VEL 00204

Discussion

The Proxy Disclosures Rules require – among other things – a description of the related party's (<u>i.e.</u> LJM's) <u>interest</u> in transactions entered into with the registrant (<u>i.e.</u> Enron), the <u>nature</u> of such interest, and – "where practicable" – the <u>amount</u> of such person's interest in the transaction(s). It is this last piece of information relating to your financial stake that we have not explicitly disclosed; rather, in both the 1999 and 2000 Proxies we have generally provided as follows: "The general partner is entitled to receive a percentage of the profits of the partnership in excess of the general partner's proportion of the total capital contributed to LJM1/LJM2, depending upon the performance of the investments made by LJM1/LJM2." Thus, it is clear that, at a minimum, there is an understanding that you, as the general partner in these two investment vehicles, are entitled to receive some level of carried interest.

Our rational for not disclosing any additional financial information related to your general partner interests varies as between 1999 and 2000 and, in particular, with respect to the RhythmsNet transaction, as follows:

(1) <u>1999</u>: The "where practicable" language in the Proxy Disclosure Rules gave us the basis for not providing additional financial information in 1999. More specifically, the majority of the transactions entered into in 1999 between Enron and LJM1/LJM2 – and specifically the RhythmsNet hedge – were "open" transactions during the 1999 fiscal year and had not yet settled or liquidated in a fashion that it would be "practicable" to determine what you earned in your general partner capacity. The "open transaction" basis applied to both the RhythmsNet transaction and the newly-entered into LJM2-related acquisitions and hedges for 1999.

(2) <u>2000</u>: We chose not to make any additional disclosures related to LJM2 in the most recent Proxy, again, based on the existence of multiple open transactions still in place thereby not making it practicable to provide. The rationale for not making any additional disclosures relating to the settlement of the RhythmsNet transaction, however, is somewhat different. In

particular, the RhythmsNet transaction settled in 2000 pursuant to terms allowed for under the original agreement. At that time it may have been more practicable to determine your financial interest. However, no further disclosure was otherwise required of the RhythmsNet transaction in 2000 due to the earlier (1999) disclosure; accordingly, we have concluded that there was no requirement to disclose any financial information related to what you may have earned in that transaction – notwithstanding that it was now more practicable to do so.

The decision not to disclose in this instance was a close call; arguably, the more conservative approach would have been to disclose. Given other pertinent (and competing) issues that you and I have discussed at great length, we decided against doing so. It was, perhaps, fortuitous that the RhythmsNet transaction extended over two proxy filing years and our knowledge of certain facts was delinked by two separate filings; thus, we have relied on two different arguments for avoiding financial disclosure for you as the LJM1 general partner in both 1999 and then 2000. If, however, the RhythmsNet transaction began and concluded in the same year, it would have been more difficult to avoid making some additional level of financial disclosure.

Going Forward

This disclosure issue will continue to be a challenge as transactions entered into between Enron and LJM2 settle and, as such, it becomes "more practicable" to disclose your financial interest. To that end, we need to continue to be cognizant of this issue as the year progresses and continue to consider some of the safe-harbors provided under the SEC rules from having to disclose related party transactions – including the (1) competitive bid and (2) reduction of general partner control alternatives we have previously discussed. I, of course, will continue to examine other alternatives, as well.

After you have had a chance to review this summary, I am available to discuss any questions or comments you may have.

Cc: Jim Derrick
Rex Rogers
Rob Walls
Ron Astin (Vinson & Elkins)
Mike Edsall (Kirkland & Ellis)

VEL 00205

LJM MEMO

Memo

To Files

From David B. Duncan
Debra A. Cash
Patricia S. Grutzmacher

Date February 9, 2001

Re: LJM Related Party Transactions

Background

LJMI and LJMII are investment companies that were formed by Andy Fastow, Enron's CFO, in 1999. Andy is the general Partner/Manager of the investment companies. Enron entered into three transactions with LJMI prior to the creation of LJMII. All other transactions between Enron and LJM were done through LJMII. See memos related to LJMI Partnership Structure, LJMII Partnership Structure and LJMII Governance as Attachments I, II and III; respectively.

Enron routinely enters into transactions with LJMII when outside equity is needed to achieve sale or off balance sheet accounting. During 1999 and 2000, LJMII has invested approximately $126 million and $300 million, respectively, in such Enron related transactions.

Audit Concerns

Due to the significant impact to Enron as a result of transactions with the LJM entities and the related party nature of such transactions, we performed the following audit procedures.

We held discussions with Jordan Mintz, (Vice President and General Counsel), Ryan Siurek (Senior Director Transaction Accounting), Rick Causey, (Chief Accounting Officer), and Andy Fastow (Chief Financial Officer) regarding Enron's internal policies and procedures. See Attachment IV.

We reviewed minutes of the Finance, Audit, and Compliance Committees of the Board of Directors, noting discussion and approval of the LJM transactions. See Attachment V.

We tested compliance with Enron's internal policies and procedures by reviewing the deal approval sheets and LJM approval sheets for each transaction. See exceptions noted at **LJM-5**. See Attachment VI for an example of a deal approval sheet and LJMII approval sheet.

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Date February 9, 2001
Subject LJM Related Party Transactions
Page 2 of 2

On a sample basis, we also traced the contributions into LJMII to wire transfers per the Citibank and Chase Statements noting that such contributions were from third parties and agreed the amounts and dates. See testwork at **LJM-3**.

We also traced the contributions out of LJMI and LJMII to wire transfers per the Citibank and Chase Statements noting agreement of amounts and dates. See testwork at **LJM-4**.

We determined that there was sufficient funded third party equity at each reporting date as required for a special purpose entity. See testwork at **LJM-1**.

Conclusions

Based on our own review of the Company's policies and procedures, documentation of communications with the Finance, Audit, and Compliance Committees of the Board of Directors and through discussions with members of Enron management, we believe that Enron policies and procedures for related party transactions are adequate to ensure the timely identification review, approval, and disclosure of such transactions to the appropriate levels of management and the board and shareholders.

To: The Files

DRAFT

From: Ryan H. Siurek, Houston
Ron Baker, Houston

Department: Transaction Support

Subject: Project Raptor – Addendum

Date: September 2001

Objective

The purpose of this memorandum is to provide information regarding Project Raptor for events subsequent to the release of the "Project Raptor" memo dated April 2000.

History of the Project Raptor

Enron Global Finance structured a thinly capitalized special purpose entity ("SPE") to serve as a hedging vehicle of certain non-strategic investments. The original Raptor SPE, Talon I LLC ("Talon"), was a vehicle in which Enron could hedge the underlying exposure of equity investments by entering into derivatives including swaps, puts, and collars. The details of the formation of Talon are documented in the "Project Raptor" memo dated April 2000.

Subsequent to the formation of Talon, the Raptor structure was repeated three times during 2000. Two of the SPEs created, Timberwolf I LLC and Bobcat I LLC, were created with structures virtually identical to the structure of the original SPE, Talon. Porcupine I LLC (Porcupine), another SPE, was very similar in concept; however, Porcupine was capitalized by Enron's contribution of TNPC warrants rather than ENE stock. See the "Project Raptor 3" memo dated September 2000 for a full discussion of the formation of Porcupine.

Despite the creation of four Raptor vehicles in 2000, only two were fully utilized to enter into derivative instruments to hedge certain Enron investments. This was primarily due to a decline in Enron and New Power Company stock prices, as well as, the decline in value of the hedged investments. Due to the declines, Enron utilized most of the remaining notional capacity of two of the vehicles to enter into more ENE share settled derivative instruments that created additional credit capacity to provide support for the other two vehicles. Another component of this transaction was an agreement by which Enron's residual interest in any Raptor vehicle with a positive credit capacity position was assigned to cover the liabilities of any Raptor vehicle in a deficit position, as all of the vehicles' liabilities were to Enron. See the "Raptor Restructuring" memo dated April 12, 2001 for a full discussion of this transaction.

Buyout Transaction

Due to continued market declines in the third quarter of 2001, the Raptor vehicles became unable to provide continued hedge protection to Enron. Therefore, Enron management decided that the best course of action would be to pursue a buy out of the third party equity holder in each of the Raptor vehicles.

A purchase price of $35,034,579 was negotiated by Enron and the third party. Enron has no further commitments to LJM in relation to the Raptor vehicles. The acquisition resulted in a non-recurring after-tax loss of approximately $462 million directly impacting current earnings, and a non-earnings direct decrease in equity of approximately $1.3 billion.

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U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #64

Changes in Prior Accounting Consultation Guidance Provided by Andersen LLP

During the third quarter of 2001, Andersen LLP (Andersen) made several key changes to the guidance that they originally provided to Enron relative to the formation of the Raptor vehicles and to the transaction involving the Raptor vehicles in March 2001. See the applicable memos described above for a discussion of the original guidance provided relative to those transactions. The key changes made to Andersen's guidance are as follows:

Original Formation Entries:

When Enron contributed the 3.7 million shares of restricted Enron common stock to the formation of Talon I in exchange for a $171 million note, the transaction was accounted for as a debit to Notes Receivable and a credit to Equity, based on the guidance provided to Enron by Andersen. Similarly, in March 2001, Enron exchanged forward contracts on Enron common stock for notes totalling $828 million. This transaction was also accounted for as a debit to notes receivable and a credit to equity, based on Andersen's guidance.

In the third quarter of 2001, Andersen changed their opinion of the proper accounting for these entries. Andersen now believes that the correct accounting for the transactions would be a credit to equity with a debit to a contra-equity account. This entry would result in no net impact to the equity balance. As a result of their altered technical advice, Andersen now believes that Enron's equity was overstated by $171 million in the third and fourth quarters of 2000, and by $999 million in the first and second quarters of 2001. Based on analogy to subscription receivable guidance in Regulation S-X section 210.5-02 paragraph 30, Enron concurs with Andersen's revised guidance. However, Management believes, and Andersen concurred, that the overstatement of equity in the applicable periods is not material (1.51%, 1.49%, 8.52% and 8.51% of total shareholders' equity, respectively) to require a restatement of Form 10K for the year ended December 31, 2000, or the Form 10Qs for the quarterly periods ended September 31, 2000, March 31, 2001 or June 30, 2001.

Assignment of Residual Interest in the Vehicles:

Andersen has also reversed their original opinions regarding the assignment of residual value in Raptor vehicles with a positive credit capacity position to cover the liabilities of any Raptor vehicles in a deficit position. Also impacted by this reversal of opinion was a short term (45 day) cross-guarantee between each of the Raptor vehicles entered into in December 2000. Based on Andersen's new opinion, neither of the above transactions would have had any impact on the calculation of credit capacity (which was originally thought to have benefitted the credit capacity of each vehicle). This would effectively negate the entire purpose of these transactions, which were based on the original opinions expressed by Andersen. In order to ensure that Enron would not have been required to book a reserve against our receivables from Raptor under this revised view, we have performed a credit analysis (relative to derivative receivables) and a credit capacity test on the Raptor vehicles as of December 31, 2000, March 31, 2001 and June 30, 2001 (see attachments).

The credit analysis tests on derivative receivables uses the same methodology that Enron's Risk Assessment and Control group applies to similar Price Risk Management receivables. While this test indicated that Enron's reserves were less than would be required to fully cover the receivables, Management believes that the reserve deficit at any of the three dates was not material to Enron's financial statements.

The credit capacity test on each of the vehicles was performed using a probablistic Monte Carlo simulation methodology. This approach also represents a change in Andersen guidance. Previously, Andersen had insisted that Enron use a hypothetical liquidation methodology using current screen prices for public securities in assessing the credit capacity of the vehicles. Andersen has changed that view and now believes that the probablistic Monte Carlo simulation methodolgy, which Enron has consistently endorsed, to be an appropriate methodology to use in assessing the need for a reserve due to deficit credit capacity of the vehicles. The credit capacity tests performed indicate that no reserves were necessary at any of the three dates.

Interoffice
Memorandum

ENRON

To: Rick Causey, Bob Butts, Rodney Faldyn

From: Ryan Siurek, Kevin Jordan

Subject: EITF Issue Update

Department: Transaction Support

Date: August 16, 2000

Share Settlement Agreements

EITF 96-13, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock

- The 96-13 model is based on the company's ability to control the settlement method of contracts indexed to its own stock.
  - Generally, if net share settlement or physical settlement is outside the control of the company, it is marked-to-market through earnings.
  - Specifically, only contracts that require physical or net share settlement or that give the company a choice of settlement in its own shares (physical or net share settlement) receive equity accounting.
  - A contract accounted for as an equity instrument is initially measured at fair value, and subsequent fair value fluctuations are not recognized until the contract is settled.
  - Physical settlement requires initial gross up of the balance sheet for the entire cash settlement amount.

EITF 00-7, Application of EITF Issue No. 96-13 to Equity Derivative Transactions That Contain Certain Provisions That Require Cash Settlement If Certain Events Occur

- EITF 00-7 clarified the meaning in EITF 96-13 of share settlement being under the company's control.
  - If an equity derivative includes any provision that could require net cash settlement, it cannot be accounted for as equity of the issuer.
  - An equity derivative that requires physical settlement in which the company pays cash and receives shares must be classified as temporary equity.
  - Evaluation of the likelihood that an event would trigger cash settlement is irrelevant (i.e. merger events, nationalization, etc.)
  - Net cash settlement only at the liquidation of the issuer does not preclude equity accounting.
  - Effective for new contracts after March 16, 2000 and for all existing contracts as of December 31, 2000.

EITF 00-19, Determination of Whether Share Settlement Is within the Control of the Issuer for Purposes of Applying EITF Issue No. 96-13, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock"

- EITF 00-19 (final consensus expected September 2000) will likely supercede EITF 00-7.

  - An equity derivative with share settlement (net share or physical) in the company's control must be accounted for as an equity instrument only if:

    a) Issuer may settle in registered or unregistered shares at its discretion.
    b) The company has sufficient authorized but unissued shares available to settle the contract after considering all other commitments (including outstanding convertible debt, outstanding stock options, etc.)
    c) The number of shares to be delivered is explicitly limited.
    d) There is no contractual requirement for the issuer to post collateral for any reason.
    e) There is no (cash settled) top off or make whole provisions for remarketing the shares by the issuer.
    f) The counterparty must be pari passu to the existing shareholders of the stock to be issued.

  - 00-19 reiterates the temporary equity guidance in 00-7.
  - Net cash settlement in bankruptcy and nationalization is acceptable if f) above is met.
  - 00-19 will be effective for new contracts after a consensus is reached and will be effective for all existing contracts as of June 30, 2001. EITF 00-19's transition provisions are expected to supercede the transition provisions of EITF 00-7.

ENE Potential Impact

- Global Corporate Finance ENE Equity Positions
- Structured Transactions
  - Marlin
  - Whitewing
  - Firefly
  - Raptor
  - JEDI

Ryan Slurek
12/12/2000 08:22 AM

To: Bob Butts/GPGFIN/Enron@ENRON, Jill Erwin/HOU/ECT@ECT
cc: Rodney Faldyn/Corp/Enron@Enron, Clint Walden/NA/Enron@ENRON, Kevin D Jordan/Corp/Enron@ENRON
Subject: EITF 00-19 Year End Implications

Please take a look at the SEC's views (bold lettering) regarding transition on EITF 00-19. This will probably have an impact on our financial reporting for year end for any derivative instruments treated as permanent equity intstruments. We probably need to get together to discuss this issue to determine any impact. I don't know the specific provisions of our share settlement contracts but I'm sure that they don't completely comply with 00-19 since they do not have explicit caps on the number of shares potentially deliverable.

Regards,

Ryan

Derivatives on a Company's Own Shares -- Immediate Reporting Implications

December 7, 2000

As a result of the November 2000 meeting ⩯of the Emerging Issues Task Force (EITF), the staff of the U.S. Securities and Exchange Commission (SEC) has provided important guidance on treatment of derivatives in a company's own stock that include gross physical settlement as a settlement alternative. Specifically, the SEC Observer at the meeting indicated that if a public company has not yet modified such outstanding equity derivatives to qualify them for permanent equity treatment under EITF Issue No. 00-19, *Determination of Whether Share Settlement is Within the Control of the Company for Purposes of Applying EITF Issue No. 96-13, 'Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, A Company's Own Stock'* ⩯ the company **must reclassify to temporary equity** the maximum amount of the potential cash obligation (for example, the forward price in a forward purchase contract or the strike price in a written put option). This treatment is required even though Issue 00-19's transition provisions give a company until June 30, 2001, to amend a contract as necessary to avoid asset or liability treatment. (Asset or liability treatment would require the derivative to be marked to fair value through earnings each period.) Contracts that provide only for net share or net cash settlement will have to be reflected by a calendar year public company issuer at their fair value in temporary equity at December 31, 2000. (Further details are outlined in item a herein.)

At the November 2000, meeting the Task Force also reached final consensuses on the various issues in Issue 00-19 (Issue 00-19 will incorporate EITF Issue No. 00-7, "*Application of Issue No. 96-13 to Equity Derivative Instruments That Contain Certain Provisions That Require Net Cash Settlement if Certain Events outside the Control of the Issuer Occur* ⩯.")

U.S. Senate Permanent Subcommittee on Investigations
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E 28420

The thrust of Issue 00-19 is that, to classify a freestanding derivative contract in an issuer's stock as an equity instrument of the issuer, the contract cannot provide the counterparty with rights that are greater than those of a common shareholder. In addition, if settlement involves the delivery of shares, the issuer must have the right to deliver unregistered shares if the delivery of registered shares is outside of the issuer's control (for example, if the issuer must maintain an effective registration statement). Other provisions in a contract that requires the delivery of cash (other than gross physical settlement which would require temporary equity treatment) outside of the issuer's control would cause the contract to be classified as an asset or liability.

As well as confirming most of the tentative conclusions reached at the July 2000 and September 2000 EITF meetings (see the Arthur Andersen Hot Topics "EITF Action on Derivatives on a Company's Own Shares," and "EITF Clarifies Guidance on Derivatives on a Company's Own Shares," respectively, and the Arthur Andersen Hot Topic, "Derivatives on a Company's Own Shares -- Calculating a Share Cap"), the Task Force dealt with the following issues:

a) SEC Observer Views on Classification of Equity Derivatives That Have Not Yet Been Brought into Compliance with Issue 00-19 by December 31, 2000. The SEC Observer clarified its views on the classification of equity derivatives contracts that are not in compliance with Issue 00-19 at year end. The SEC Observer indicated that equity derivatives that were issued prior to September 20, 2000, and that were classified as permanent equity under the consensuses in Issue 96-13, but would be classified as asset, liability or temporary equity contracts under the consensuses of Issues 00-7 and 00-19 had these consensuses been applied as of December 31, 2000, should be classified as temporary equity as of December 31, 2000. We do not believe that this would require a company to restate prior balance sheets. We believe this means that any equity derivative contract that includes net share settlement features that were relied upon to keep the contract in permanent equity under Issue 96-13 must be reclassified to temporary equity if the net share settlement provisions do not meet the requirements of Issues 00-7 and 00-19 as of the end of this calendar year as if the contract only provided for gross physical settlement. Where a reclassification to temporary equity is required, the SEC Observer also indicated that the amount recorded in temporary equity must reflect the maximum possible cash obligation. Where the maximum amount is not known because it is contingent on the market value of the underlying security, then the amount to be classified outside of permanent equity (to the extent it represents an obligation) should be calculated based on the market price of the underlying security as of the balance sheet date. This situation would apply when the settlement method, for example, is only net share settlement. In contracts where the issuer had the choice of net share, gross physical and net cash, since only gross physical and net cash are considered effective if net share settlement is not in compliance with Issue 00-19, the model in Issue 00-19 would assume gross physical settlement (temporary equity).

b) Permanent Grandfathering of Multi-Party Transactions Entered into Before September 20, 2000: The Task Force reached a consensus that a derivative instruments entered into with more than one counterparty in a single offering (public or private) before September 20, 2000, and not modified on or after September 20, 2000, are not subject to the consensuses in Issue 00-19 or Issue 00-7 (although those contracts are subject to the requirements of Issue 96-13). For those contracts, a deemed share cap would apply to the contract until its maturity or modification in assessing whether the company controls the delivery of shares for other contracts.

c) Certain Transactions that Require the Delivery of Registered Shares Can Meet the Requirements of Issue 00-19 to be Classified as Equity Instruments of the Issuer: The Task Force reached a consensus that if a derivative involves the delivery of registered shares that are registered at the inception of the transaction and there are no further timely filing or registration requirements, the requirement of Issue 00-19 that share delivery be within the control of the company is met, notwithstanding the Task Force's previous consensus that the company must have the option to delivery unregistered shares to conclude that delivery of shares is within the company's control. (This provides some relief for public transactions where there is solely a physical delivery requirement as the initial registration remains in effect without further action by the company.)

d) Contracts that Require Physical or Net-Share Settlement: The Task Force indicated that if a derivative contract requires physical or net-share settlement by delivering registered shares and does not specify any circumstances under which net-cash settlement would be permitted or required, but the contract does not specify how the contract would be settled in the event that the company is unable to deliver registered shares, net-cash settlement is assumed if the company is unable to deliver registered shares and the contract should be classified as an asset or liability (and marked to fair value through earnings) because share settlement is not within the company's control.

e) Application of Issue 00-19 to Debt Instruments with Embedded Equity Derivatives: The Task Force reached a consensus that for derivatives indexed to a company's own stock that are embedded in a debt instrument, the incremental requirements of Issue 00-19 (including those of Issue 00-7) do not apply although the previous requirements of Issue 96-13 would continue to apply. If the embedded derivative would not qualify as an equity instrument (or temporary equity) under the provisions of Issue 96-13 (without consideration of the additional requirements of Issue 00-19), the embedded derivative would be subject to the requirements of FASB Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities*. Statement 133 excludes embedded derivatives that meet the definition of an equity instrument of the issuer from its scope (in this case, a derivative that should be treated as an equity instrument according to the original model in Issue 96-13). However, if the embedded derivative does not qualify for this scope exception, it may meet the requirements to be treated as a derivative under Statement 133 and thus may have to be carried at fair value with the change in fair value reported in current earnings.

This means that typical convertible debt instruments where the conversion feature is embedded in the debt and only payable in shares would not be included in the scope of Issue 00-19 and if the embedded derivative could only be share settled upon conversion, would qualify to be excluded from the scope of Statement 133 and thus not bifurcated by the issuer nor carried at fair value. However, equity derivatives that are detachable, such as warrants, would continue to be within the scope of Issue 00-19 and if they do not meet the requirements of Issue 00-19, would fall within the scope of Statement 133 and may have to be carried at fair value with changes in fair value recorded in the income statement. Each instrument must be individually analyzed for factors that would or would not cause it to be in the scope of Statement 133.

f) **"Best Efforts" Requirements:** The Task Force indicated that if a net share settlement is undertaken, but there are not enough authorized but unissued shares available at contract termination/maturity to make the counterparty whole (given the share cap), the derivatives contract can include provisions that the company will use its best efforts to try to obtain shareholder approval for additional shares to fully liquidate the contract. If the provision fixes the number of shares subject to this "best efforts" provision on the date that the net-share settlement occurs, the provision could not cause the contract to be classified as an asset or liability. However, if the dollar amount of the obligation is fixed (with or without accrual of interest), so that the number of shares that could be delivered if the company is able to obtain additional authorization is variable, the excess obligation represents a stock-settled debt and would preclude equity classification of the contract (or if partial net-share settlement is permitted under the contract, preclude equity classification of the portion represented by the excess obligation.)

To: David B. Duncan@ANDERSEN WO; Debra A. Cash@ANDERSEN WO
CC:
BCC:
Date: 08/23/2001 02:50 PM
From: James A. Hecker
Subject: Documentation of Client Call
Attachments:

Here is my draft memo. for your review for "smoking guns" that you can't extinguish. I tried to include only the perspectives obtained from Sherron. not other facts later discussed by us. Thanks..

Date Receiver s Name
Subject
Page 2 of 3

Date August 21, 2001
Subject Client Accounting Inquiry
Page 3 of 3

To The Files

From James A. Hecker
Date August 21, 2001
Subject Client Accounting Inquiry

Yesterday I received an ostensibly social call from Sherron Smith Watkins, a Houston office alum who works in the CFO s group at our large audit client, Enron. After some small talk about current events such as the job market and last week s CEO resignation at Enron, she asked me if I knew much about some of Enron s recent structured transactions. I told her I did not, having never worked on the Enron job, but that I had general knowledge about many of the related issues from my work on other marketing and trading clients. Although she seemed initially reluctant to get into the details with me, an Arthur Andersen audit partner, she obviously wanted a sounding board with whom she could discuss certain of her concerns related to a set of Enron transactions, and I told her I d be happy to listen.

Sherron then told me she was concerned about the propriety of accounting for certain related-party transactions. The transactions in question were, based on

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*AAHEC(2)000192.1

our discussions, with an entity with a name something like LJM , which was at the time of the transactions at least partly owned by Andy Fastow, Enron s CFO (and her current boss). She later told me that Fastow s interest in LJM has since been sold to Michael Copper, an Enron alum. I also understood by her tone that the potentially sensitive transactions were done within the last couple of years. Sherron seemed even more agitated about the transactions accounting because she perceived the related footnote disclosures in the company s consolidated financial statements were difficult to understand and did not tell the whole story .

After some investigative work since her return to Fastow s group, she reportedly had discussed some of her concerns with Enron s general counsel office (she did not name the individual). That individual had assured her that AA and Enron s external counsel (Vinson &Elkins) had reviewed the transactions accounting and financial statement disclosures and that they were sure there was no impropriety. At that point, I mentioned to Sherron that many people inside and outside the company assume we have seen every small transaction and OK d the accounting, which for many reasons, potentially including immateriality, is often not true. Sherron understood this, but assured me the dollars involved (approximately $500 million) were material, even to (a company as large as) Enron. Based both on the type and size of the transactions. Sherron told me she was concerned enough about these issues that she was going to discuss them with Ken Lay, Enron s Chairman, on Wednesday, August 22, 2001

Based on our following discussions, her perceptions and concerns were:

- In summary, Sherron couldn t understand how Enron could, with its own capital stock, repeatedly add to the collateral underlying an obligation owed to Enron from a related party without recognizing in its financial statements either a) the related Enron stock distributions or contributions to that related party or b) the high-tech investment losses such related-party obligation was supposedly protecting against.
- LJM, an investment company formerly owned at least partially by Andy Fastow (CFO of Enron), was formed to enter into various structured transactions with Enron. I understood from Sherron that one such transaction involved the hedging of certain of Enron s investments in high-tech companies. Since these high-tech investment values have declined, Enron s hedge from LJM has increased in value, thus putting LJM on the hook for a potentially large liability to Enron. Supporting this hedging arrangement, Sherron described to me that LJM was initially capitalized in large part with Enron stock, which has also significantly declined in value since yearend 2000. Well after LJM s formation, and in response to this resulting reduction in total LJM asset value, her investigative inquiries had pieced together a very troublesome scenario. She perceived that Enron was putting additional Enron stock into LJM (the exact mechanism – sales, contributions, exchanges or otherwise --wasn t clear from our conversation), primarily to bolster LJM s perceived ability to repay obligations that will be owed to Enron at some future date. However, according to Sherron, these additional Enron stock contributions/issuances to LJM did not appear to be recorded on Enron s books. I informed Sherron I could not comment because I was obviously unfamiliar with the facts behind both the formation and ongoing operations of LJM.
- She asserted that the Enron financial-statement disclosures related to the Fastow investment-company relationships and transactions were (putting it kindly) hard to understand and incomplete. A $500 million gain from the LJM contract(s) was purportedly identified in interim financial disclosures. However, according to Sherron, it was not clear in the disclosures that the

$500 million gain on Enron s books from the Fastow agreement (through LJM) actually offset other losses on Enron s investments in various high-tech investments. The potential collateralization/collectibility issues behind the LJM obligation that Sherron perceived are a problem were also not spelled out. I did not attempt to confirm these disclosure assertions by pulling Enron s Form 10-K or 10-Q s (but see documentation of engagement team discussions below).

· She also asserted that, at the time of the recent sale to Mr. Copper, she had mentioned to others that LJM must have had very limited stockholders equity and must have been an unsuccessful investment for its owner(s). I inferred that she thought Mr. Copper s purchase price must have been relatively small, for one or more of the following reasons: a) LJM owed so much to Enron, or b) the company had so few other assets or c) it only had assets such as Enron stock that had declined so much in value since LJM s inception. However, she also asserted that she had been told that most, if not all, of LJM s equity had been distributed to its shareholder(s) [including Fastow and CIBC, an independent banking organization unrelated to Enron] concurrently, or shortly after, its original formation.

Based on our discussion, I told her she appeared to have some good questions. I emphasized that I was uninvolved in the issues or client and therefore unable to give her any definitive advice or conclusions on these matters, especially without knowing all the facts, which she understood. However, I encouraged her to discuss these issues with anyone in the company who could satisfy her about the accounting and disclosures related to these transactions. I told her that I admired her stand-up attitude and that corporate introspection about these sorts of accounting and reporting issues often was very healthy and should not be surpressed. She neither committed to update me about her discussions with Ken Lay nor requested anything further from me.

Immediately after my discussion with Sherron on August 20, I relayed the essence of her asserted concerns to Bill Swanson (ABA practice director), Dave Duncan (Enron engagement partner) and Deb Cash (another partner on Enron). On August 21, we all added Mike Odom, practice director, to the discussions, and agreed to consult with our firm s legal advisor about what actions to take in response to Sherron s discussion of potential accounting and disclosure issues with me.

Copies To:

Debra A. Cash
David B. Duncan
Michael C. Odom
William E. Swanson

DRAFT – FOR DISCUSSION PURPOSES ONLY

CONFIDENTIAL

DO NOT DUPLICATE

Distribution:

Ken Lay
Rick Causey
Beth Tilney
Ray Bowen
Mark Koenig
Rodney Faldyn
Mary Cilia
Ryan Siurek
Dave Duncan, Andersen
Tom Bauer, Andersen
Deb Cash, Andersen
Joe Brenner – Wilmer, Cutler, & Pickering

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Please find enclosed the draft of the SEC Response to the LJM transactions.

DO NOT DUPLICATE

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EXHIBIT #68

DRAFT- FOR DISCUSSION PURPOSES ONLY

The following table provides a listing of distributions made to Hoss LLC subsequent to LJM2's acquisition. This information was furnished by Wilmington Trust as Enron is not responsible for payments made to equity holders of Rawhide.

Date	Amount
April 7, 2000	$410,803.39
July 10, 2000	419,927.08
October 6, 2000	436,370.23
January 8, 2001	441,312.50
April 6, 2001	418,769.06
July 9, 2001	375,256.51
October 5, 2001	340,934.03

Summary

Transaction:

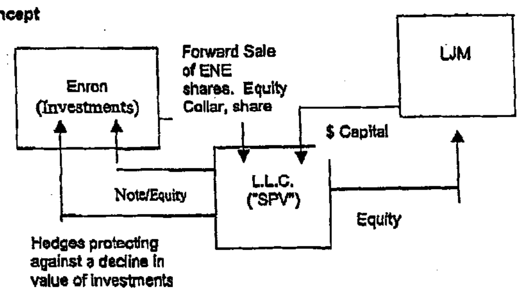
Outcome:

Project Raptor

Purpose
The Purpose of this memo is to provide a summary of the formation and subsequent transactions comprising Project Raptor, including the formation and ultimate purchase of Talon I L.L.C., Timberwolf I L.L.C., Bobcat I L.L.C. and Porcupine I L.L.C. (collectively, the Entities)

General Overview of Project Raptor:

Basic Concept



DRAFT- FOR DISCUSSION PURPOSES ONLY

- Enron made a number of public and private equity investments (principally in The New Power Company and various broadband and technology companies).
- Enron wanted to protect its shareholders against the risk of declines in the value of these investments.
- These risks were not easily hedged, in part because some of these investments were not actively traded.
- Enron and LJM formed Special Purpose Vehicles (SPV).
    - Enron contributed a promise to deliver shares and an obligation to provide more shares if the value of the Enron shares declined. This resulted in an increase in shareholders' equity of $1 billion.
    - SPV provided a note back to Enron and equity in the SPV.
    - LJM Contributed Capital to the SPV in exchange for equity in the SPV.
- SPV provided Enron with hedges against declines in Enron investments, thus transferring the risk of declines on these investments away from Enron shareholders.
- Value of Enron shares <u>and</u> the investments unexpectedly declined simultaneously. The SPV therefore became insolvent.
- Enron continued to have the obligation to provide additional contingent shares. Rather than further dilute shareholders' equity, Enron concluded it was in the best interest of shareholders to terminate the SPV. This resulted in:
    - A Reduction of shareholders' equity by $1.2 billion, reversing the previous increase of $1 Bn
    - A Cancellation of Enron's obligation to issue additional equity to the SPV
    - LJM lost the majority of its remaining investment in the SPV.

<u>Economic Benefit</u>
Enron was able to quickly transfer some of the market price risk of the investments away from its shareholders through the hedging program.

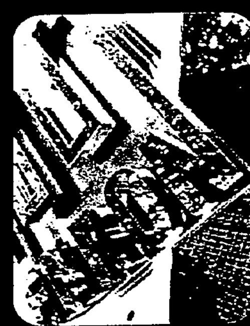
<u>Control Processes and Reviews</u>
The formation of the SPV, LJM's participation in it, the SPV's purpose and the types of transactions to be done with the SPV were reviewed by

- Inside and outside counsel
- Inside and outside accounting and audit staff
- Enron Corp.'s Board of Directors.

Disclosure
The formation of the SPV and the participation of LJM were disclosed in Enron's public filings.

Detailed Discussion of Project Raptor:

Raptor
Hedging Strategy Analysis



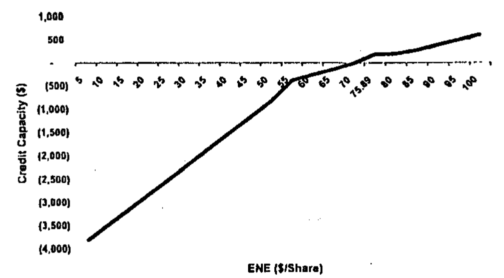
risk assessment & control

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #69

Raptor Credit Capacity Before & After Restructuring

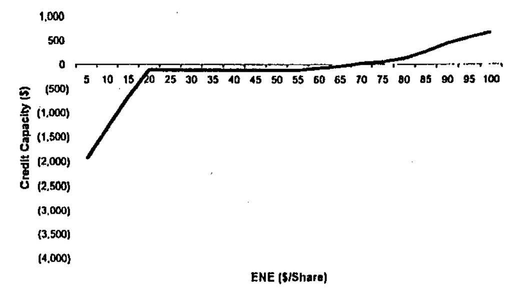
Original Raptor Structure:

- ***Shortfall of restricted shares*** Breakeven point is at $75.89/share.
- ***Significant drop in value of NPW warrants*** NPW price changed from $21/share at Raptor inception to current $6/share.
- ***Significant drop in value of Raptor hedge***
- ***Collars on ENE shares structured with Enron Corp***



New Raptor Structure:

- ***Added ENE shares from JEDI to Raptor II & IV at 23% discount***
- ***Placed Collar on Raptor II & IV***
- ***Monetized Tahiti Note***



Lessons Learned

- Recognize the effect of accounting hedge vs. economic hedge

- Corp. should consider hedging assets in Raptor to minimize credit capacity volatility

- The new Raptor structure transferred risk in the form of stock dilution

But Corp

Appendix I

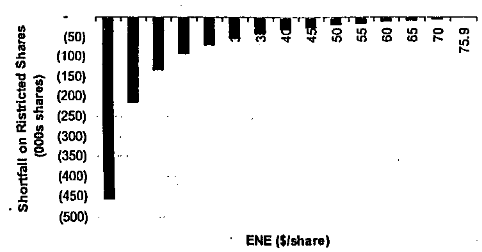
At #36 What's the issue?

Raptor Credit Capacity: (ENE: $60/share, NPW: $6/share)*

	Initial Credit Capacity	LJM Distribution	Credit Capacity Aft. LJM Distribution	Raptor Hedge Net Gain/(Loss)	Change in Contributed Stock	Other Income/(Loss)	Current Credit Capacity
Raptor I	$ 222,923,065	$ (41,000,000)	$ 181,923,065	$ (421,872,987)	$ 79,967,265	$ 24,127,011	$(135,855,646)
Raptor II	218,023,063	(41,000,000)	177,023,063	(23,229,378)	18,717,086	19,209,840	191,720,611
Raptor IV	216,923,069	(40,469,684)	176,453,385	-	(391,455,665)	24,622,723	(190,379,557)
Raptor III	536,473,800	(39,500,000)	496,973,800	(247,363,899)	(361,767,000)	(1,407,100)	(113,564,199)
Total	1,194,342,997	(161,969,684)	1,032,373,313	(692,466,264)	(654,538,313)	66,552,473	(248,078,791)

Shortfall on ENE Common stock Forwards:

	ENE Shares Forward Sales from Whitewing	Forward Sales Shares Shortfalls	TNPC Shares
Raptor I	3,876,755	-	
Raptor II	7,809,790	(2,144,878)	
Raptor IV	6,326,045	(6,326,045)	
Raptor III	-	-	24,117,800
Total	18,012,590	(8,470,923)	24,117,800

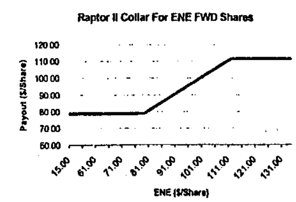


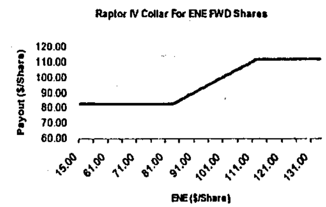
* Note: Used the hedging asset value on 3/7/01.

Appendix II: Collars in Raptor Structures

Collars in Original Raptor Structures

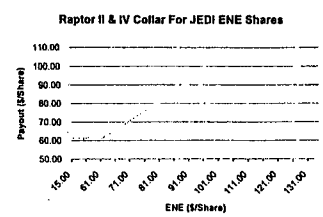
- Raptor I: Long put @81.00, short call @116.00, 3,876,755 shares
- Raptor II: Long put @78.88, short call @111.86, 7,809,790 shares
- Raptor IV: Long put @83.00, short call @112.42, 6,326,045 shares





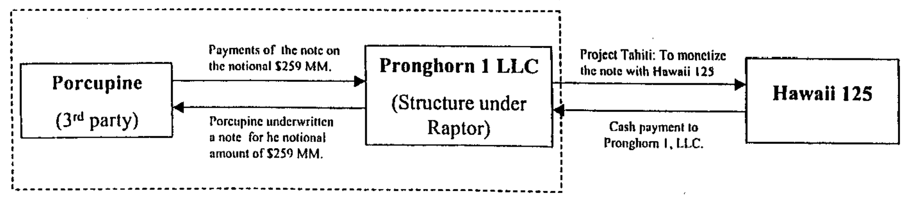
Collars in New Raptor Structure

- Both Raptor II and IV have same collar structure.
- Raptor II: Long put @$61.48, short call @$91.04, 7,919,393 shares
- Raptor IV: Long put @$61.48, short call @$91.04, 4,080,607 shares



Appendix III: Project Tahiti

- Porcupine, a third party, is making payments to Pronghorn 1 LLC, on a $259MM notional note.
- The note is due on April, 2005.
- Pronghorn 1 – LLC, is a sub-structure of Raptor.
- Pronghorn monetized the note with Hawaii 125, another ENE off-balance sheet structure.
- Currently, $30 MM of the note has been monetized with no discount
- By 2001 end of year, another $50 MM with be monitized with no discount.
- The remaining $179 MM note will be monetized in the next few years.



Enron Global Markets

Crude & Products

March 2001

EC2 000007662

Enron's Funds Flow Targets

Enron Corp. funds flow and balance sheet ratio targets set by the Board of Directors versus actual results

		Actual		S&P				
	Board Targets	2000	1999	A	A-	BBB+	BBB	BBB-
Funds flow interest coverage*	4.03	4.07	3.68	4.65	4.05	3.45	2.88	2.34
Pretax interest coverage**	2.26	2.43	2.63	4.15	3.55	2.95	2.53	2.28
Funds flow from operations/total obligations	26.1%	28.5%	25.3%	33.5%	30.1%	26.7%	23.5%	20.5%
Debt/total capital***	39.7%	40.7%	38.5%	45.1%	47.9%	50.8%	53.6%	56.4%

* Calculated as funds flow from operations plus interest incurred and estimated lease interest expense, divided by interest incurred and estimated lease interest expense

** Calculated as total adjusted earnings divided by interest incurred and estimated lease interest expense

*** Total capital includes debt, minority interests, company-obligated preferred securities of subsidiaries and shareholders' equity

ENRON GLOBAL ASSETS AND SERVICES
Equity Value Schedule
$(Millions)
As of June 2001

10/31/01

Update 1

	Corp. Dev. Est. Market Value	Enron's Carry Value	Difference
South America			
Elektro	1,016	2,026	(1,010)
Cuiaba	374	535	(161)
TGS	388	451	(63)
CEG and CEG - Rio	247	269	(22)
Gaspart	204	194	10
Transredes	115	145	(30)
TBG/GTB (BBPL)	29	41	(12)
Total South America	2,373	3,661	(1,288)
Caribbean			
Promigas	119	158	(38)
Vengas	105	142	(36)
BLM	31	110	(79)
SECLP	-	102	(102)
Accroven	37	49	(12)
PQPLLC	42	41	1
Calife	-	37	(37)
San Juan Gas	-	36	(36)
IGL	15	30	(15)
Haina note	-	18	(18)
Procaribe	-	6	(6)
Caribbean Basin Fund	-	6	(6)
Corinto	2	5	(3)
Bachequero		3	(3)
Centragas	19	(2)	21
Ecoelectrica	248	130	118
Total Caribbean	618	869	(251)
Asia			
SK-Enron	220	297	(77)
Eclipse	74	67	7
Batangas	54	51	3
Subic	26	30	(4)
Bond portfolio	23	23	(1)
Piti Guam	15	20	(5)
Total Asia	411	488	(77)
India			
Dabhol	342	870	(528)
GAIL	53	70	(17)
EGEP	385	400	(15)
Total India	780	1,340	(560)
Other			
Poland	42	34	8
Trakya	198	232	(34)
Sarlux	200	349	(149)
Total Other	440	615	(175)
Total Project Related Activities	4,621	6,973	(2,352)
Other Basis Not Related to Projects Above (See Detail)		560	
SA Merchant Activities Currently In Wholesale		177	
Total Enron Global Assets with SJG, SA Merchant and EI HQ		7,710	

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #71

E 103411

11/27/01 BoD
- Elected Ray Troubh
- Established SLC and elected Ray as chair

11/28/01 am BoD 9:30 AM
- Authorized mgmt. To allocate cash to pay bills that would maximize value of the estate

amendments to Deferral + Savings Plan effective 11/29/01 11/28/01

11/28/01 pm BoD 6PM
- Ken reported that DYN deal was cancelled
- Approved non-standard bank resolution
- Approved housing funds at PBOG
- Approved modified investment policy
- Approved suspension of contributions to Deferral Plan
- Approved suspension of co. match in stock in the Savings Plan
- Approved bonus plan
- Approved reconstitution of SIC ?

8:30 pm 12/01/01 BoD 12/01/01 Comp Commite 8:00 PM 12/01/01 Bd. Meeting Sev. Pl. poor pay 2 wks base pay/yr service max 12 wks
- Reported on Enron Europe in administration
- Approved filing of Ch. 11
- * Approved Severance Pay Plan – 2 wks. base pay for each year of service, with 3 mo. minimum and 52 week maximum
- Approved DIP loan to be secured by all unencumbered assets
- Discussed DYN litigation

Postponed to clarify costs, plans and whether pre or post bankruptcy filing would be most prudent business judgment

Bus. Reorg. Sev. – 2 wks base pay/yr service/min 12 wks Max 12 wks.

12/02/01 Comp
- * Mary Joyce reviewed current Severance Pay Plan ; question
- * Approved recommended to the BoD that company ask for an exemption from complying with WARN as the business is faltering based on our circumstances and request Court to allow $4,500 per employee

Question moot as the filing has occurred.

12/0201 BoD
- * Approved to modify the Severance Pay Plan to include a WARN offset
- * Approved netting $4,500 payment from Severance Pay Plan benefits

To: Shannon D. Adlong@ANDERSEN WO
CC:
BCC:
Date: 01/31/2001 08:32 PM
From: Shannon D. Adlong
Subject:
Attachments: beradino prep mtgs.ppt

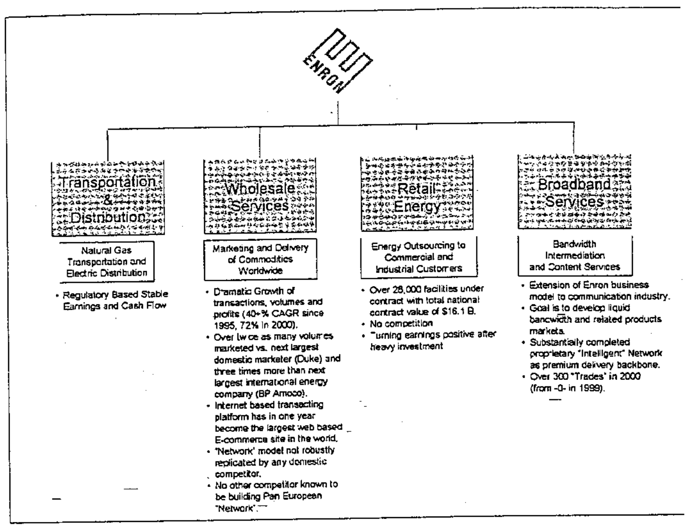
U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #73

*AASCGA005249.1

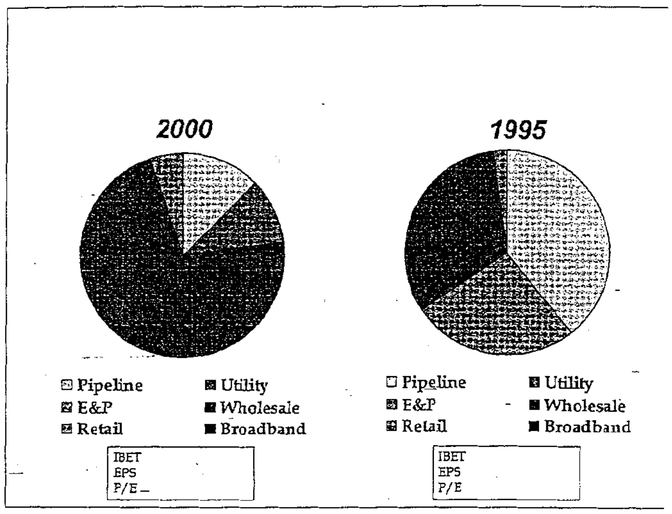
Key Objectives

- Keep Firm Leadership Informed About Enron and our Relationship
- Confirm Desire to Retain
- Generate Understanding of Need to Examine Internal Process Issues to Meet Critical Client Needs and Expectations
- Discuss Certain Matters Related to Independence

Company Overview



*AASCGA005250.3



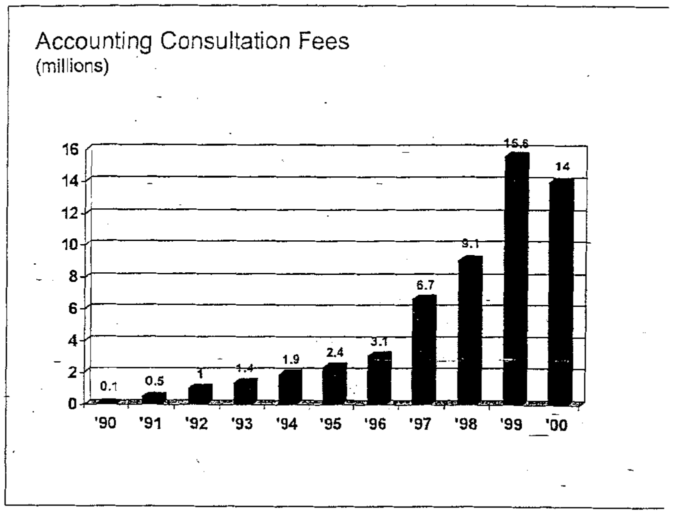
*AASCGA005250.4

External Reputation

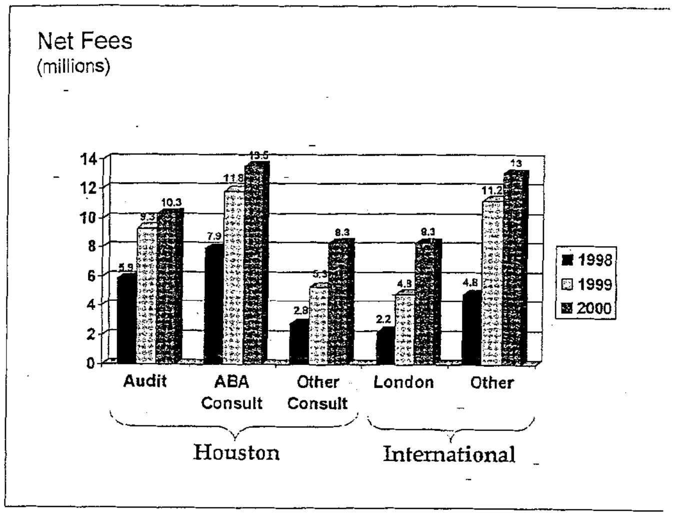
- Fortune Magazine:
  - Most Innovative Company (5 years in a row)
  - #1 Quality of Management
  - #2 Employee Talent
  - #18 America's Most Admired Company
  - #25 World's Most Admired Company
  - #22 Best Place to Work
  - #29 Top 100 Fastest Growing Companies
  - #62 Global 100 list
- Included in
  - Motley's Fool's "Now 50" Index
  - Wired 40 Index
  - Fortune's "10 Stocks to own for the decade"
- #1 Energy Company
  - Fortune
  - Forbes Global Business
  - Global Finance
- #1 Energy Risk Management Company
  - Risk Magazine
- Among Most Active Houston Corporate Civic Leaders
- Highly Politically Active and Connected

Relationship Overview

- Highly Approachable and Receptive Management
  - Frontiered Integrated Audit Arrangement
  - Extremely Open Communication
  - Challenges Us For Mutually Productive Endeavors
  - Participates Whenever Asked
- Good Board Relationship and Communication
- Aggressively Hires Our People
- Substantial Fee Growth Over Recent Years



*AASCGA005250.7



*AASCGA005250.8

Risk Overview
Company Specific Environmental Factors

- Heavy Reliance on Completing Transactions at a High Pace
  - "Bring Value Created to Bottom Line"
  - Demonstrate Liquidity of Portfolio
  - Achieve Necessary Capital Velocity to Sustain Business Growth
- Culture of Assertiveness, Informed Risk Taking and Sophisticated Structuring
- Frustration with Lack of Consistency of GAAP Models and Rulemaking Processes
- Institutional History of Success Whenever Challenged
- High Degree of Board Confidence in Management
- Transaction Structuring Activity Spread Among a Broad Group of Individuals With Varying Degrees of Sophistication and Maturity

Risk Overview
Company Efforts To Mitigate Risk

- High Quality Transaction Support Staff
- Culture of Front-End Expert (AA) Involvement
- Increased Participation In Rule-making Processes

Risk Overview
Engagement Team Efforts To Mitigate Risk

- On-Site High Quality Team
- Extensive Efforts To Understand Business
- Monitoring of External Information
- Extensive Intra-Team Consultation
- Extensive Consultation With PSG
  - Individual Transactions and Issues
  - Periodic Meetings and Conference Calls
- Use of Other Firm Experts
- Periodic Meetings With Local Office Management

To: Shannon D. Adlong@ANDERSEN WO
CC:
BCC:
Date: 01/24/2001 05:46 PM
From: Shannon D. Adlong
Subject: Enron meeting
Attachments:

---------------------- Forwarded by Shannon D. Adlong on 01/24/2001 05:38 PM ---------------------------

To: D. Stephen Goddard Jr.@ANDERSEN WO
cc:
Date: 01/24/2001 05:46 PM
From: David B. Duncan (Mailed by: Shannon D. Adlong)
Subject: Enron meeting

Steve, Dave said this is his first pass at this and to feel free to edit.
Thanks, Shannon

As many of you know, the pace and transaction orientation of Enron's business places a great deal of stress on our advisory and risk management processes. While Enron acknowledges and highly values these processes, certain recent occurrences have raised certain isues which need to be explored and addressed, both internally and with Enron management.

Toward that end, Joe Berardino has committed to visit with Enron upper management in late February. Certain of you may also be asked to attend.

To ensure we are thoroughly communicating and exploring the issues, the local team believes we need at least two meetings:

Meeting 1 - Firm Views Surrounding Risk Tolerance and Enron Client Retention

It has been some time since we have had a broad group of leadership discuss our relationship with Enron from a risk and retention perspective. We would ask the following people to participate:

Line	Service Category	Technical and Risk Management
Duncan	Bennett	Kutsenda
Bauer	Reiger	Goolsby
Samek	Odom	
Niemann	Blanchet	
Goddard	Stewart	
Swanson	Dreyfus	
Lowther		

This meeting is scheduled for ______. Although we encourage all that can physically participate to do so, the following call in number is also available ______.

Meeting 2 - Consultation Process Issues

Enron highly values our consultation process and its participants. Although they would state that we have been highly effective, they have areas where they believe we could, and where they expect us, to improve. The engagement team believes this is a good opportunity to comprehensively evaluate ways we might enhance our ability to deliver on Enron's high expectations. We believe the following should participate:

Line	Service Category	Technical and Risk Management
Duncan	Bennett	Odom
Bauer	Reiger	Blanchet
Goddard		Stewart
Swanson		Bass (?)
Lowther		

This meeting is scheduled for ______. The call in numbers is ________.

Thanks in advance for everyone's help in managing this important relationship.

Arthur Andersen
E&P and IPP's

To: David B. Duncan@ANDERSEN WO, Thomas H. Bauer@ANDERSEN WO
cc:
Date: 02/06/2001 08:24 AM
From: Michael D. Jones, Houston , 2541
Subject: Enron retention meeting

Dave, I was not sure whether you were planning on documenting the meeting yesterday. My significant notes were as follows (these were not very detailed, but I was not sure how detailed you wanted to get, assuming that you were going to document the meeting). Let me know if you want me to take a stab at it first (if so we should probably get together for a few minutes to discuss your documentation ideas.:

Attendees:
By Phone: Samek, Swanson, Jeneaux, Jonas, Kutsenda, Stewart
In Houston: Bennett, Goddard, Goolsby, Odom, Lowther, Duncan, Bauer, Jones

Significant discussion was held regarding the related party transactions with LJM including the materiality of such amounts to Enron's income statement and the amount retained "off balance sheet". The discussion focused on Fastow's conflicts of interest in his capacity as CFO and the LJM fund manager, the amount of earnings that Fastow receives for his services and participation in LJM, the disclosures of the transactions in the financial footnotes, Enron's BOD's views regarding the transactions and our and management's communication of such transactions to the BOD and our testing of such transactions to ensure that we fully understand the economics and substance of the transactions.

The question was raised as whether the BOD gets any competing bids when the company executes transactions with LJM. DBD replied that he did not believe so, but explained thier transaction approval process generally and specifically related to LJM transactions.

A significant discussion was also held regarding Enron's MTM earnings and the fact that it was "intelligent gambling". We discussed Enron's risk management activities including authority limits, valuation and position monitoring.

We discussed Enron's reliance on its current credit rating to maintain itself as a high credit rated transaction party.

We discussed Enron's dependence on transaction execution to meet financial objectives, the fact that Enron often is creating industries and markets and transactions for which there are no specific rules which requires significant judgement and that Enron is aggressive in its tranaction structuring. We discussed consultation among the engagement team, with Houston management, practice management and the PSG to ensure that we are not making decisions in isolation.

Ultimately the conclusion was reached to retain Enron as a client citing that it appeared that we had the appropriate people and processes in place to serve Enron and manage our engagement risks. We discussed whether there would be a perceived independence issue solely considering our level of fees. We discussed that the concerns should not be on the magnitude of fees but on the nature of fees. We arbitrarily discussed that it would not be unforseeable that fees could reach a $100 million per year amount considering the multi-disciplinary services being provided. Such amount did not trouble the participants as long as the nature of the services was not an issue.

In addition to the above discussions were held to varying degrees on each page of the presentation materials.

Take away To Do's:
Inquire as to whether Andy Fastow and / or LJM would be viewed as an "affiliate" from an SEC perspective which would require looking through the transactions and treating them as within the consolidated group.
Suggest that a special committee of the BOD be established to review the fairness of LJM transactions (or alternative comfort that the transactions are fair to Enron, e.g., competitive bidding)
Why did Andy not select AA as auditors, including when PWC was replaced with KPMG. Discussions concluded that we would likely not want to be LJM's financial advisors given potential conflicts of interest with Enron.
Focus on Enron preparing thier own documentation and conclusions to issues and transactions.
AA to focus on timely documentation of final transaction structures to ensure consensus is reached on the final structure.

Arthur Andersen
PROFESSIONAL STANDARDS GROUP

To: John E. Stewart@ANDERSEN WO
cc:
Date: 03/04/2001 06:46 PM
From: Carl E. Bass, Houston, 237 / 2314
Subject: Enron

I know you did not ask for this but I believe you should be at least have a version of what I know about this Enron "thing" from me. You may share this with anyone you deem appropriate -- we are after all partners in this Firm and should be able to have an open dialogue about issues, especially those that affect partners. In addition, it appears that I have been the subject of some conversation and no one has discussed this with me directly. So treat this as my own New York Times OpEd piece, expect we are not discussing Presidential pardons.

The Enron "thing" with me
With regard to this "thing," I believe that several points need to be made. There appears to be some sort of assertion that I have a "problem" with Rick Causey or someone at Enron that results in me having some caustic and inappropriate slant in dealing with their questions. You may recall that when I joined the PSG on December 1, 1999, Dave Duncan had requested 500-750 hours of my time on Enron specific consultation. At the time, I/we was/were told that this was cleared with the client. If in fact I had some sort of "problem," one would have though that would have surfaced at that time. The client would have vetoed such an arrangement. In fact, I was told this was sold to them. Logic would also seem to dictate that if there was some sort of "problem," I would have been removed as one of the engagement partners, much less been placed on it to begin with. Believe me, if I had some "problem," I would have never requested to have been put on the engagement given the complexity and challenges that that engagement entails. So any notion that there is some sort of long, deep seeded animosity needs to be dispelled as it simply is not true -- nor do the facts warrant it. I should also note that I have gone to great lengths to get Causey in front of standard setters. For example, I was able to get Causey to be a guest at the EITF meeting when tolling agreements were discussed because they had a vested interest in the accounting for those transactions. If I had some sort of ax to grind, I would not have even orchestrated that.

With regard to the yearend issues that apparently triggered this "thing with me," lets go through them one by one. Again, there was dialogue on process here that I was not party to but apparently I have some sort of "problem" here.

1. Blockbuster transaction -- Roger Willard and Clint Carlin approached me for about 15 minutes one afternoon to discuss two things. One, whether an interest in joint venture could be securitized and two, what are the requirements to be a joint venture. With respect to the first question, I said yes as long as it is accounted for on the equity method. We then discussed the requirements of a joint venture, including the fact that it had to be a business. The original Blockbuster transaction was simply where Enron was going to contribute this contract and the other party was going to contribute systems and expertise to deliver this product to households. I received one other question from Clint Carlin, dealing with some puts and calls. About two months later Roger Willard asked whether the equity needed to be 3% of fair value or book value. At that time I was told that they were going to have some $50 million gain on the sale of this venture interest immediately after the contract was signed and the venture was entered into. Furthermore, the other venture partner was not contributing anything. At that time, both you and I had expressed some concern about this deal. It should be noted that despite all of the turmoil over this, we (PSG) did not object to this transaction as it appeared to meet the technical requirements of Statement 125. We relied on the engagement team to address both the definition of a business and the valuation issues of immediate gain. The client's proposed accounting nonetheless was sustained. At that time, I

was aware of another securitization in which the client had provided a side agreement to guarantee the 3% residual equity at risk with the same counterparty in this transaction. Although it is not my job (which I acknowledged to the engagement team), I did suggest confirmation as an audit procedure. I believe knowledge of this did prompt us over a weekend to have the engagement team involve various levels of practice directors in this decision. In effect, this was a very risky transaction and we did not believe that the PSG should solely be in on this without others.

With respect to the infamous 4:1 test, they did not follow our advice on this. I did acknowledge several times with the engagement team that although our test is grounded in GAAP, we did make it up and it is no where to be found in the accounting literature.

2. Networks transaction – Tom Bauer involved me on this transaction. It was similar to the one above but did involve the sale of an existing Enron business through a securitization transaction. This was probably the nth step of a series of permutations of this transaction that I had been involved in since November. The only late issue on this came after the deal had been signed. This was one of those deals where Enron contributed a business worth $100. A bank contributed cash totaling $100. The bank did this through an SPE whereby the residual equity holder contributed $3 and the debt holder contributed $97. I was asked after the deal had been signed whether that was OK. We had discussed this issue a lot within the PSG and had in fact had a client issue with the SEC along these lines. In addition, we had discussed this issue with the Enron engagement team last summer in which they documented the conclusion that the equity person would have had to contribute $6. I understand now that the gain on that transaction was $100 million. In addition, other Enron transactions had been capitalized as we have suggested.

The engagement team went back and had the equity holder contribute additional equity. The equity holder in this case was the LJM entity, a related party because the CFO is the managing equity member.

3. "Raptor" derivative transactions – Enron has entered into a series of complicated derivatives with a related party (the CFO) in which this related party CFO writes options to Enron to protect Enron's investments in various internet businesses. The capital for the SPE is derived from Enron cash settled derivatives that are European in that they cash settle at the end of the derivative life. I will honestly admit that I have a jaded view of these transactions and "dragged my feet" initially. This was in part due to an impairment test that Deb Cash had devised to keep these transactions honest. The yearend issues dealt with the impairment test. The engagement team had asked whether these various SPEs could be cross collateralized so that losses in one entity could offset losses in another. I told them that as long as they were truly cross collateralized that seemed OK. The problem I was told was that the CFO had no reason to inject a loss on one vehicle. The client's proposal was that the vehicles be cross collateralized but if the there was a loss in one vehicle, the CFO had the option to remove the cross collateralization any time he chose to. Based on how the impairment test was devised, I did not see any way that this worked. In effect, it was heads I win, tails you lose. The engagement team appeared to be split on this – two partners had a problem with the client's proposed accounting and one did not. In the end, however, the engagement team agreed with me as did the Practice Director. It was decided by them to "fix" this feature before the release of the financial statements. One thing to note was I was told that the client never agreed to the impairment test to begin with. So the real issue that I thought had been addressed and resolved had never been resolved with the client.

One problem I had with Raptor was that the original structure was one in which the PSG was not consulted on. In that transaction, the SPE had at risk only a nominal amount of equity (less than the 3% residual at risk of the notional value of an internet investment). Furthermore the SPE was in a bankrupt entity so any loss on the derivative could not be funded by the SPE. I understood that there was a $100 million loss on an internet investment that otherwise should have been reported absent the derivative. At no time was PSG consulted on the original structure – we did attempt to make sure the subsequent structures were adequately capitalized.

Those are the yearend issues. In total they represent about $150 million plus of income or avoided losses at yearend – and all involved the Practice Director. At no time did I ever have communication with the client on these issues. All of my communications were solely with the engagement team. You can understand then as to how I am perplexed as to how the client even knows I was consulted on with respect to these issues and how they believe I am too caustic and cynical with respect to their transactions (see below).

The only other issue that came up post yearend but affected 2000 was the Azurix impairment. I was consulted on an impairment issue at the Azurix level. I told the engagement team that their facts were a little shaky but if they could prove them then they had a position. It was not, however, without risk. At the time, Azurix was going through a "going private" transaction. The client wanted to record an impairment in the fourth quarter. I was also consulted on the impairment issue at the Enron level of its investment in Azurix. You had told them about 6-9 moths ago that 6-9 months was a good indicator of whether an impairment was permanent with respect to that investment. I had repeated that advice post yearend but by then the investment was under water for about 18 months. I told the engagement partner that it was judgment – not really PSG's call. I was told by him that "he had never communicated the original advice to the client and therefore he could not go in and do so now." I was led to believe that he went to his Practice Director. Again, not really our call.

Process

Apparently, part of the process issue stems from the client knowing all that goes on within our walls on our discussions with respect to their issues. I believe that when we are either having discussions or have reached a decision, the FIRM has done so. The PSG only gives advice. The engagement partners and practice directors then reach a decision based on that advice as well as other considerations, but it is the FIRM that does so. We should not be communicating with the client that so and so said this and I could not get this past so and so in the PSG. I learned that lesson the hard way when I was senior working for Gary Goolsby about 17 years ago. I have first hand experience on this because at a recent EITF meeting some lower level Enron employee who was with some else from Enron introduced herself to me by saying she had heard my name alot – "so you are the one that will not let us do something." I have been on calls where the EA has interrupted the call saying that so and so was waiting for an answer from me on this that or the other. In fact, the client called during a meeting on the Raptor derivative transactions between me, the Practice Director, and the engagement team. One of the partners told the EA that interrupted us that "they were still meeting with Carl."

I have also noted a trend on this engagement that the question is usually couched along the lines "will the PSG support this?" When a call starts out that way, it is my experience that the partner is struggling with the question and what the client wants to do. But lately managers have been posing their questions that way.

Let me propose an alternative. The engagement team should prepare a memo documenting all aspects of the transaction as well as the research that supports a conclusion or the conflicting research that leads to the grayness. All too often (in fact, without exception), it has lately been a call from a manager with a flowchart and we then have to slug through it to find the real issues. For example, within the past week the client proposed placing a contract into a "joint venture." An interest in the joint venture would then be sold for a $20-40 million gain. The parties to the joint venture were the same parties to the contract. There were no customers (the customer was the other "venturer"), no process, no business. In fact the press release was clear that a contract was entered into. There is no mention of a joint venture. In effect, nothing was accomplished in this transaction except a sale of future revenues. The engagement partner agreed with my view and in fact had the same view. She was seeking concurrence. I was told they booked the transaction any way and that we will propose a PAJE.

Once we conclude on something, or render some advice, the engagement team should deliver that advice or conclusion as if it was their own. It is after all the engagement team's responsibility to sign the opinion – not ours.

DUNCAN 3/12/01

CARL

— NOT DUNCAN DRIVEN

some PUSH CARL OUT of engagement team
by client to set

— CAUSEY
— ECHOLS — STRONG FEELINGS

NEGATIVE view of CARL
— CONSISTENCY of ADVICE
— THE FURTHER AWAY, more conservative

WIN/WIN TO GO TO PSG

CARL NOT MUCH INTERACTION directly WITH CLIENT
DISAPPOINTMENT (MATTERS IN THEORY VS. TRANSACTION

Y-E issues/LAST 6 MONTHS ⇒ CAME TO HEAD

CAUSEY = LOST political capital internally

LONDON problem

need more [illegible] in Houston
on engagement team

TOM BAUER — 8 million [illegible] fee

JFS — [illegible], DG

CLIENT SEES need to replace Carl /

CARL — move to CHICAGO
good solution,
but doesn't want to
come

PULL / PUSH

TIM JR too young

Documentation – weakest point

proof
prove
personal

I WHY

II P, P, P — CONCESSIONS

III WAY FORWARD

CHICAGO / HOUSTON

✓ 1. FILTER — CARL IN TRANSIT

✓ 2. Writing — NOT THEN LATER — AWAY

✓ 3. ~~TALKING~~

— DESIGN

— ANIMATIONS

— NO MEETINGS

— BRAIN STORMING

✓ 4. NO GRAD ⇒ NEW MODEL

— community 1st

— new important 1st

Exhibit I

Enron
Summary Comments

- Continued Heavy Emphasis On Structured Transactions To Accelerate "Value" Creation And Realize Targets (Income, Balance Sheet, Cash Flow & Disclosure)
    - Numerous Open Issues On YE Transaction Execution
    - Some Less Substantive Transactions Need Further Work (by client)
    - No Currently Known Significant Conceptual Disagreements
    - Transaction Working Environment Improved From 1998

- Heavy Use Of Structured Syndication Vehicles For 3rd And 4th Qtr. Transactions
    - Condor
    - Yosemite
    - LJM
    - Others

  Significant Consultation On Structures And Related Transactions

- FAS 125 Transactions Less Significant Than 1998 But Still Prevalent – Activity Evaluation In Order And In Process

- Credit Posture Appears To Be Improving
    - Moody's Positive Credit Outlook
    - Counterparty Insurance Activity

- Overall Internal Control Report To Audit Committee – Slight Improvement
    - Improvements Made And Continue To Be Made On Previously Identified Issues
    - Unique Past Year Issues (i.e. Y2K) And Pace Of Commercial Activity Making It Difficult To Gain Ground On An Overall Basis
    - EES And Systems Issues Emphasized

- Risk Management Issues
    - Finish Year End Transactions
    - Manage Potential PAJE's With Client (see accompanying "point-in-time" summary of known potential issues)
    - Put Together Financial Position Picture
        - Evaluate Financial Position Risks
        - Balance Against Anticipated Disclosures
    - Put Together Qualitative F/S Summary For Top Management And Audit Committee
    - Keep Continued Pressure On Known Reporting And Disclosure Issues
        - Wholesale Segment Information
        - Related Party (Particularly LJM) Information
        - Other (Prepaids, Etc.)

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AASCGA(TX)007864

Exhibit II

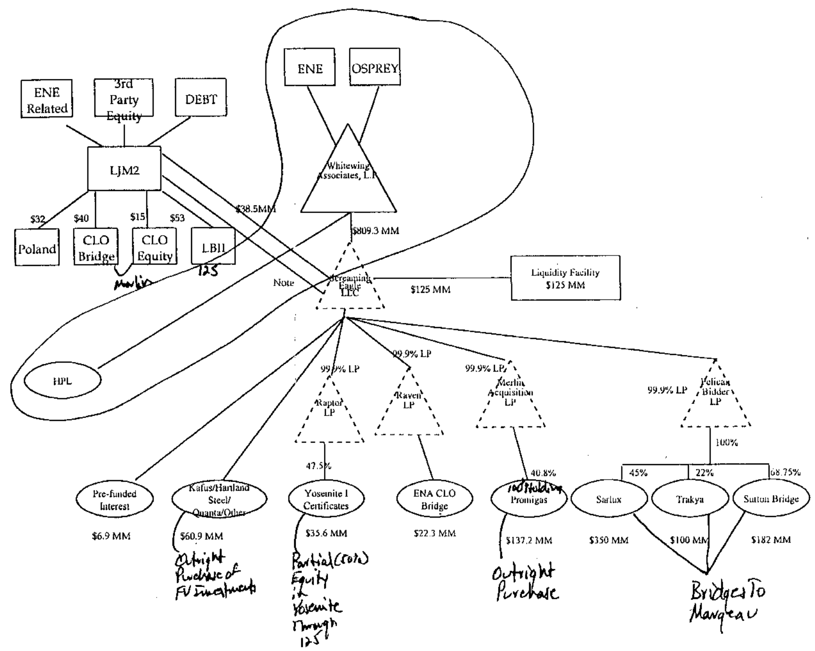
Enron Communications Inc.
December 16, 1999
Enron Partner Meeting

- Wholly owned subsidiary – Core Business
- Focus Areas of Business Operations
  1. eCommerce Services – CO/CEO Joe Hirko (Portland)
  2. Bandwidth and Network Services – CO/CEO Ken Rice (Houston)
  3. Technology and Operations - Rex Shelby (EIN. R & D)
  4. Global Network Development – Steve Elliot
- Financial Information (000's)

	12/31/97	12/31/98	9 mos. ended 9/30/99
Assets	$12	$153	$638*
Liabilities	10	138	477
Equity	2	15	161
Revenues	3	8	399*
Gross Profit	2	4	380
Net Income (Loss)	(2)	7	146

*Includes MTM on Rhythms stock of $342

- Business Model
  1. Monthly Recurring Revenue (MRR) business using epowered applications
  2. Bandwidth Trading
- ECI Activities
  1. Building physical fiber and backbone development (Global)
  2. Pushing development of Bandwidth trading model
  3. Sale of IRU's (short-term)
  4. Investment in technology companies (merchant investments)
- AA Activities
  1. Development of MTM Accounting Model for Bandwidth trading
  2. IRU sales accounting white paper/CFO Roundtable



ENE Related
3rd Party Equity
DEBT
LJM2
$32
$40
$15
$53
Poland
CLO Bridge
CLO Equity
LBI1
125
$38.5MM
ENE
OSPREY
Whitewing Associates, L.P.
$809.3 MM
Note
Yosemite Eagle LLC
$125 MM
Liquidity Facility $125 MM
HPL
99.9% LP
Raptor LP
Raven LP
Merlin Acquisition LP
Pelican Bidder LP
100%
47.5%
40.8%
45%
22%
68.75%
Pre-funded Interest
Kafus/Hartland Steel/ Quanta/Other
Yosemite I Certificates
ENA CLO Bridge
Promigas
Sarlux
Trakya
Sutton Bridge
$6.9 MM
$60.9 MM
$35.6 MM
$22.3 MM
$137.2 MM
$350 MM
$100 MM
$182 MM
Outright Purchase of FV Investments
Partial (cross) Equity in Yosemite Through 125
Outright Purchase
Bridges To Marquee

STOEL RIVES LLP

MEMORANDUM

December 8, 2000

TO: RICHARD SANDERS

FROM: CHRISTIAN YODER AND STEPHEN HALL

RE: Traders' Strategies in the California Wholesale Power Markets/ ISO Sanctions

CONFIDENTIAL: ATTORNEY/CLIENT PRIVILEGE/ATTORNEY WORK PRODUCT

This memorandum analyzes certain trading strategies that Enron's traders are using in the California wholesale energy markets. Section A explains two popular strategies used by the traders, "inc-ing" load and relieving congestion. Section B describes and analyzes other strategies used by Enron's traders, some of which are variations on "inc-ing" load or relieving congestion. Section C discusses the sanction provisions of the California Independent System Operator ("ISO") tariff.

A. The Big Picture

1. "Inc-ing" Load Into The Real Time Market

One of the most fundamental strategies used by the traders is referred to as "'inc-ing' load into the real time market." According to one trader, this is the 'oldest trick in the book' and, according to several of the traders, it is now being used by other market participants.

To understand this strategy, it is important to understand a little about the ISO's real-time market.[1] One responsibility of the ISO is to balance generation (supply) and loads (demand) on the California transmission system. During its real-time energy balancing function the ISO pays/charges market participants for increasing/decreasing their generation. The ISO pays/charges market participants under two schemes: "instructed deviations" and "uninstructed deviations." Instructed deviations occur when the ISO selects supplemental energy bids from generators offering to supply energy to the market in real time in response to ISO instructions. Market participants that increase their generation in response to instructions ("instructed deviation") from the ISO are paid the "inc" price. Market participants that increase their

[1] The "real-time" energy market is also known as the imbalance energy market. The imbalance energy market can be further subdivided into the (1) supplemental energy or instructed deviation market and (2) the ex post market or uninstructed deviation market.

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EXHIBIT #75

generation without an instruction from the ISO (an "uninstructed deviation") are paid the ex post "dec" price. In real-time, the ISO issues instructions and publishes ex post prices at ten-minute intervals.

"'Inc-ing load' into the real-time market" is a strategy that enables Enron to send excess generation to the imbalance energy market as an uninstructed deviation. To participate in the imbalance energy market it is necessary to have at least 1 MW of load. The reason for this is that a generator cannot schedule energy onto the grid without having a corresponding load. The ISO requires scheduling coordinators to submit balanced schedules; i.e., generation must equal load. So, if load must equal generation, how can Enron end up with excess generation in the real-time market?

The answer is to artificially increase ("inc") the load on the schedule submitted to the ISO. Then, in real-time, Enron sends the generation it scheduled, but does not take as much load as scheduled. The ISO's meters record that Enron did not draw as much load, leaving it with an excess amount of generation. The ISO gives Enron credit for the excess generation and pays Enron the dec price multiplied by the number of excess megawatts. An example will demonstrate this. Enron will submit a day-ahead schedule showing 1000 MW of generation scheduled for delivery to Enron Energy Services ("EES"). The ISO receives the schedule, which says "1000 MW of generation" and "1000 MW of load." The ISO sees that the schedule balances and, assuming there is no congestion, schedules transmission for this transaction. In real-time, Enron sends 1000 MW of generation, but Enron Energy Services only draws 500 MW. The ISO's meters show that Enron made a net contribution to the grid of 500 MW, and so the ISO pays Enron 500 times the dec price.

The traders are able to anticipate when the dec price will be favorable by comparing the ISO's forecasts with their own. When the traders believe that the ISO's forecast underestimates the expected load, they will inc load into the real time market because they know that the market will be short, causing a favorable movement in real-time ex post prices. Of course, the much-criticized strategy of California's investor-owned utilities ("IOUs") of underscheduling load in the day-ahead market has contributed to the real-time market being short. The traders have learned to build such underscheduling into their models, as well.

Two other points bear mentioning. Although Enron may have been the first to use this strategy, others have picked up on it, too. I am told this can be shown by looking at the ISO's real-time metering, which shows that an excess amount of generation, over and above Enron's contribution, is making it to the imbalance market as an uninstructed deviation. Second, Enron has performed this service for certain other customers for which it acts as scheduling coordinator. The customers using this service are companies such as Powerex and Puget Sound Energy ("PSE"), that have generation to sell, but no native California load. Because Enron has native California load through EES, it is able to submit a schedule incorporating the generation of a generator like Powerex or PSE and balance the schedule with "dummied-up" load from EES.

Interestingly, this strategy appears to benefit the reliability of the ISO's grid. It is well known the California IOUs have systematically underscheduled their load in the PX's Day-

Ahead market. By underscheduling their load into the Day-Ahead market, the IOUs have caused the ISO to have to call on energy in real time in order to keep the transmission system in balance. In other words, the transmission grid is short energy. By deliberately overscheduling load, Enron has been offsetting the ISO's real time energy deficit by supplying extra energy that the ISO needs. Also, it should be noted that in the ex post market Enron is a "price taker," meaning that they are not submitting bids or offers, but are just being paid the value of the energy that the ISO needs. If the ISO did not need the energy, the dec price would quickly drop to $0. So, the fact that Enron was getting paid for this energy shows that the ISO needed the energy to balance the transmission system and offset the IOU's underscheduling (if those parties own Firm Transmission Rights ("FTR") over the path).

2. **Relieving Congestion**

The second strategy used by Enron's traders is to relieve system-wide congestion in the real-time market, which congestion was created by Enron's traders in the PX's Day Ahead Market. In order to relieve transmission congestion (i.e., the energy scheduled for delivery exceeds the capacity of the transmission path), the ISO makes payments to parties that either schedule transmission in the opposite direction ("counterflow payments") or that simply reduce their generation/load schedule.

Many of the strategies used by the traders involve structuring trades so that Enron gets paid the congestion charge. Because the congestion charges have been as high as $750/MW, it can often be profitable to sell power at a loss simply to be able to collect the congestion payment.

B. Representative Trading Strategies

The strategies listed below are examples of actual strategies used by the traders, many of which utilize the two basic principles described above. In some cases, the strategies are identified by the nicknames that the traders have assigned to them. In some cases, i.e., "Fat Boy," Enron's traders have used these nicknames with traders from other companies to identify these strategies.

1. Export of California Power NO! 250?

   a. As a result of the price caps in the PX and ISO (currently $250), Enron has been able to take advantage of arbitrage opportunities by buying energy at the PX for export outside California. For example, yesterday (December 5, 2000), prices at Mid-C peaked at $1200, while California was capped at $250. Thus, traders could buy power at $250 and sell it for $1200.

   b. This strategy appears not to present any problems, other than a public relations risk arising from the fact that such exports may have contributed to California's declaration of a Stage 2 Emergency yesterday.

2. "Non-firm Export"

a. The goal is to get paid for sending energy in the opposite direction as the constrained path (counterflow congestion payment). Under the ISO's tariff, scheduling coordinators that schedule energy in the opposite direction of the congestion on a constrained path get paid the congestion charges, which are charged to scheduling coordinators scheduling energy in the direction of the constraint. At times, the value of the congestion payments can be greater than the value of the energy itself.

b. This strategy is accomplished by scheduling non-firm energy for delivery from SP-15 or NP-15 to a control area outside California. This energy must be scheduled three hours before delivery. After two hours, Enron gets paid the counterflow charges. A trader then cuts the non-firm power. Once the non-firm power is cut, the congestion resumes.

c. The ISO posted notice in early August prohibiting this practice. Enron's traders stopped this practice immediately following the ISO's posting.

d. The ISO objected to the fact that the generators were cutting the non-firm energy. The ISO would not object to this transaction if the energy was eventually exported.

Apparently, the ISO has heavily documented Enron's use of this strategy. Therefore, this strategy is the more likely than most to receive attention from the ISO.

2. "Death Star"

a. This strategy earns money by scheduling transmission in the opposite direction of congestion; i.e., schedule transmission north in the summertime and south in the winter, and then collecting the congestion payments. No energy, however, is actually put onto the grid or taken off.

b. For example, Enron would first import non-firm energy at Lake Mead for export to the California-Oregon border ("COB"). Because the energy is traveling in the opposite direction of a constrained line, Enron gets paid for the counterflow. Enron also avoids paying ancillary service charges for this export because the energy is non-firm, and the ISO tariff does not require the purchase of ancillary services for non-firm energy.

c. Second, Enron buys transmission from COB to Lake Mead at tariff rates to serve the import. The transmission line from COB to Lake Mead is outside of the ISO's control area, so the ISO is unaware that the same energy being exported from Lake Mead is simultaneously being imported into Lake Mead. Similarly, because the COB to Lake Mead line is outside the ISO's control area, Enron is not subject to payment of congestion charges because transmission charges for the COB to Lake Mead line are assessed based on imbedded costs.

d. The ISO probably cannot readily detect this practice because the ISO only sees what is happening inside its control area, so it only sees half of the picture.

e. The net effect of these transactions is that Enron gets paid for moving energy to relieve congestion without actually moving any energy or relieving any congestion.

3. "Load Shift"

a. This strategy is applied to the Day-Ahead and the real-time markets.

b. Enron shifts load from a congested zone to a less congested zone, thereby earning payments for reducing congestion, i.e., not using our FTRs on a constrained path.

c. This strategy requires that Enron have FTRs connecting the two zones.

d. A trader will overschedule load in one zone, i.e., SP-15, and underschedule load in another zone, i.e., NP-15.

Such scheduling will often raise the congestion price in the zone where load was overscheduled.

The trader will then "shift" the overscheduled "load" to the other zone, and get paid for the unused FTRs. The ISO pays the congestion charge (if there is one) to market participants that do not use their FTRs. The effect of this action is to create the appearance of congestion through the deliberate overstatement of loads, which causes the ISO to charge congestion charges to supply scheduled for delivery in the congested zone. Then, by reverting back to its true load in the respective zones, Enron is deemed to have relieved congestion, and gets paid by the ISO for so doing.

e. One concern here is that by knowingly increasing the congestion costs, Enron is effectively increasing the costs to all market participants in the real time market.

f. Following this strategy has produced profits of approximately $30 million for FY 2000.

4. "Get Shorty"

a. Under this strategy, Enron sells ancillary services in the Day-ahead market.

b. Then, the next day, in the real-time market, a trader "zeroes out" the ancillary services, i.e., cancels the commitment and buys ancillary services in the real-time market to cover its position.

c. The profit is made by shorting the ancillary services, i.e., sell high and buy back at a lower price.

d. One concern here is that the traders are applying this strategy without having the ancillary services on standby. The traders are careful, however, to be sure to buy services right at 9:00 a.m. so that Enron is not actually called upon to provide ancillary services. However, once, by accident, a trader inadvertently failed to cover, and the ISO called on those ancillary services.

e. This strategy might be characterized as "paper trading," because the seller does not actually have the ancillary services to sell. FERC recently denied Morgan Stanley's request to paper trade on the New York ISO.

The ISO tariff does provide for situations where a scheduling coordinator sells ancillary services in the day ahead market, and then reduces them in the day-of market. Under these circumstances, the tariff simply requires that the scheduling coordinator replace the capacity in the hour-ahead market. ISO Tariff, SBP 5.3, *Buy Back of Ancillary Services.*

f. The ISO tariff requires that schedules and bids for ancillary services identify the specific generating unit or system unit, or in the case of external imports, the selling entity. As a consequence, in order to short the ancillary services it is necessary to submit false information that purports to identify the source of the ancillary services.

5. "Wheel Out"

a. This strategy is used when the interties are set to zero, i.e., completely constrained.

b. First, knowing that the intertie is completely constrained, Enron schedules a transmission flow through the system. By so doing, Enron earns the congestion charge. Second, because the line's capacity is set to "0," the traders know that any power scheduled to go through the inter-tie will, in fact be cut. Therefore, Enron earns the congestion counterflow payment without having to actually send energy through the intertie.

c. As a rule, the traders have learned that money can be made through congestion charges when a transmission line is out of service because the ISO will never schedule an energy delivery because the intertie is constrained.

6. "Fat Boy"

a. This strategy is described above in section A (1).

7. "Ricochet"

a. Enron buys energy from the PX in the Day Of market, and schedules it for export. The energy is sent out of California to another party, which charges a small fee per MW, and then Enron buys it back to sell the energy to the ISO real-time market.

b. The effect of this strategy on market prices and supply is complex. First, it is clear that Enron's intent under this strategy is solely to arbitrage the spread between the PX and the ISO, and not to serve load or meet contractual obligations. Second, Ricochet may increase the Market Clearing Price by increasing the demand for energy. (Increasing the MCP does not directly benefit Enron because it is *buying* energy from the PX, but it certainly affects other buyers, who must pay the same, higher price.) Third, Ricochet appears to have a neutral effect on supply, because it is returning the exported energy as an import. Fourth, the parties that pay Enron for supplying energy to the real time ex post market are the parties that underscheduled, or underestimated their load, i.e., the IOUs.

8. Selling Non-firm Energy as Firm Energy

a. The traders commonly sell non-firm energy to the PX as "firm." "Firm energy," in this context, means that the energy includes ancillary services. The result is that the ISO pays EPMI for ancillary services that Enron claims it is providing, but does not in fact provide.

b. The traders claim that "everybody does this," especially for imports from the Pacific Northwest into California.

c. At least one complaint was filed with the ISO regarding Enron's practice of doing this. Apparently, Arizona Public Service sold non-firm energy to Enron, which turned around and sold the energy to the ISO as firm. APS cut the energy flow, and then called the ISO and told the ISO what Enron had done.

9. Scheduling Energy To Collect the Congestion Charge II

a. In order to collect the congestion charges, the traders may schedule a counterflow even if they do not have any excess generation. In real time, the ISO will see that Enron did deliver the energy it promised, so it will charge Enron the inc price for each MW Enron was short. The ISO, however, still pays Enron the congestion charge. Obviously a loophole, which the ISO could close by simply failing to pay congestion charges to entities that failed to deliver the energy.

b. This strategy is profitable whenever the congestion charge is sufficiently greater than the price cap. In other words, since the ex post is capped at $250, whenever the congestion charge is greater than $250 it is profitable to schedule counterflows, collect the congestion charge, pay the ex post, and keep the difference.

C. **ISO Tariff**

The ISO tariff prohibits "gaming," which it defines as follows:

> "Gaming," or taking unfair advantage of the rules and procedures set forth in the PX or ISO Tariffs, Protocols or Activity Rules, or of transmission constraints in period in which exist substantial Congestion, to the detriment of the efficiency of, and of consumers in, the ISO Markets. "Gaming" may also include taking undue advantage of other conditions that may affect the availability of transmission and generation capacity, such as loop flow, facility outages, level of hydropower output or seasonal limits on energy imports from out-of-state, or actions or behaviors that may otherwise render the system and the ISO Markets vulnerable to price manipulation to the detriment of their efficiency." ISO Market Monitoring and Information Protocol ("MMIP"), Section 2.1.3.

The ISO tariff also prohibits "anomalous market behavior," which includes "unusual trades or transactions"; "pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions"; and "unusual activity or circumstances relating to imports from or exports to other markets or exchanges." MMIP, Section 2.1.1 et seq.

Should it discover such activities, the ISO tariff provides that the ISO may take the following action:

1. Publicize such activities or behavior and its recommendations thereof, *"in whatever medium it believes most appropriate."* MMIP, Section 2.3.2 (emphasis added).

2. The Market Surveillance Unit may recommend actions, including fines and suspensions, against specific entities in order to deter such activities or behavior. MMIP, Section 2.3.2.

3. With respect to allegations of gaming, the ISO may order ADR procedures to determine if a particular practice is better characterized as improper gaming or "legitimate aggressive competition." MMIP, Section 2.3.3.

4. In cases of "serious abuse requiring expeditious investigation or action" the Market Surveillance Unit shall refer a matter to the appropriate regulatory or antitrust enforcement agency. MMIP, Section 3.3.4.

5. Any Market Participant or interested entity may file a complaint with the Market Surveillance Unit. Following such complaint, the Market Surveillance Unit may "carry out any investigation that it considers appropriate as to the concern raised." MMIP, Section 3.3.5.

6. The ISO Governing Board may impose "such sanctions or penalties as it believes necessary and as are permitted under the ISO Tariff and related protocols approved by FERC; or it may refer the matter to such regulatory or antitrust agency as it sees fit to recommend the imposition of sanctions and penalties." MMIP, Section 7.3.

From: Vance, Seth [FI] [seth.vance@ssmb.com]
Sent: Thursday, October 25, 2001 3:46 AM
To: Fastow, Andrew

hang in there--the news will subside and I'm sure when the facts are out, it will be clear that everything you did was approved by the board. Shareholders will sue over anything when they loose as much as they have---looks like they are grabbing for anything and everything. I guess Jeff S. and Cliff B. timing of leaving Enron could not have been better--?

How can I get ahold of you? I have a home number of do you have a home e-mail address?

Seth

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EXHIBIT #76

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DRAFT

MEMORANDUM

TO: Enron Files

FROM: Steven Rosen

DATE: January 8, 2002

RE: Interview of Herbert S. Winokur, Jr.

On January 8, 2002, William McLucas, Chuck Davidow, Joseph Brenner, Stuart Delery, and Steven Rosen of Wilmer, Cutler & Pickering ("WCP") and John Sullivan of Deloitte & Touche (an accounting firm retained by WCP), spoke with Herbert (Pug) Winokur, a director of Enron Corp., at WCP's offices in New York to gather information from him in order to allow WCP to provide legal advice to the Special Committee of Enron's Board of Directors. Winokur was represented at the interview by W. Neil Eggleston of Howry, Simon Arnold & White and Kathy Patrick of Gibbs & Brun. Williams Powers and Raymond Troubh of the Special Committee were also present.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Winokur's statements. The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Winokur has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

At the outset, Davidow explained that WCP represented the Special Committee appointed by the Board to investigate certain transactions between Enron and related parties, and we were speaking to him as part of that investigation. Davidow stated that we did not represent Enron's officers or employees, including him, that, in our view, the conversation was privileged but it was the Special Committee's (or Enron's) privilege, and that the Special Committee or Enron could decide what to do with the privilege, not him. Davidow stated that Winokur should anticipate that anything he told us could be communicated to others, such as the Board, others associated with Enron, and the Government.

Davidow emphasized that Winokur should indicate when he was giving his recollection and when he was speculating or surmising. Davidow asked Winokur to differentiate between information he learned through his contemporaneous work on the Board and information he learned through his work on the Special Committee. Davidow also stated that Winokur should feel free to refer to any documents needed to refresh his recollection.

EC2 000000812

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #77a

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ATTORNEY WORK PRODUCT

Background

Winokur graduated from Harvard University in 1964. He also received his PhD from Harvard. From 1966 until 1969, he worked at the Pentagon in the Office of Systems Controller and one other office. After working at the Pentagon, he co-founded and did consulting work for the Intercity Fund (which became ICF), until 1973. Winokur then worked at Penn Central and its affiliates until 1977. From 1977 until 1979 or 1980, he worked for Palmay Co. and then managed David Murdock's investments until 1983. He then returned to Penn Central as Senior Executive Vice-President and Director until 1987. From 1987 until the present, he has worked at Capricorn. Winokur has no accounting background.

Winokur worked with Ken Lay at the Pentagon in 1969 and 1970. When Lay became Chief Executive Officer of Houston Natural Gas, he reorganized its Board. Winokur joined the Board in 1984 or 1985 as part of that reorganization. Winokur has not held any other position with Enron. However, a small portion (.16%) of the sales of Natco, a company in which Capricorn invested, was to an Enron subsidiary. Natco went public in January 2000 and the Enron subsidiary has been partially spun-off.

Winokur has been the head of the Finance Committee for approximately eight to ten years. When there were large trading losses, the Office of the Chairman or the Chief Risk Officer would give him an early warning., which happened on a small number of occasions. To prepare for Finance Committee meetings, Winokur would speak with Andrew Fastow and Rick Buy (on occasion he would speak with their subordinates) to go over the meeting agenda.

Winokur would typically review draft minutes carefully. The Finance Committee would be given minutes from their previous meeting and would discuss them. Winokur would suggest changes if he noticed any inaccuracies.

The members of the Finance Committee with financial experience are Winokur, Norman Blake, Robert Belfer, and Frank Savage. Paulo Ferraz is a banker and Jerome Meyer is in operations. John Urquhart has less finance experience then some of the other committee members.

Board consideration of significant transactions

The Board must review and approve transactions that exceed certain thresholds. These thresholds have changed over time. At present, any transaction equal to or greater than $75 million must be presented to the Board. Typically, such transactions are first brought to the Finance Committee for discussion and possible recommendation to the full Board. The Office of the Chairman has authority to approve transactions between $25 million and $75 million, as long as the transactions are continuations of a current business. Deals that are not continuations of a current business and that are over $25 million must be presented to the Board. Authority to approve transactions under $25 million has been delegated to the business units.

Fastow

EC2 000000813

Winokur considers Fastow to be a smart individual. Based upon his personal experience and the experiences of people that he knows, Winokur had no reason to doubt Fastow's integrity or trustworthiness. He has never heard that Fastow pressured banks or other financial institutions to invest in his partnerships.

Familiarity with SPE's

Winokur only became familiar with SPEs through his work at Enron. He does not recall when he first became aware of the use of SPEs, but he does recall JEDI, which at the time he knew as an "off-balance-sheet entity." He saw SPEs as being the same as off-balance-sheet entities. He was somewhat familiar with off-balance-sheet entities through his previous business experience.

Chewco and JEDI

Winokur's first recollection of Chewco is reading about it in the October 2001 Wall Street Journal article. He has no recollection of hearing about Chewco in 1997. Davidow showed Winokur the minutes of the December 9, 1997 meeting of the Enron Board, stating "the Executive Committee approved . . . the buyout of [CalPERS] interest in [JEDI]." Winokur recalls the buyout of the JEDI partnership but he does not recall that specific discussion at the December 1997 Board meeting.

Winokur does not recall any conversation regarding Fastow's or Kopper's involvement with the buyout of CalPERS interest. He would have expected that their involvement would be brought to the Board's attention because conflict of interests should not occur without full disclosure to and discussion by the Board. After Brenner noted that the Enron Code of Conduct provides that conflict of interest transactions must be approved by the Office of the Chairman, Winokur reiterated that he expected that any material involvement by an employee in a conflict of interest transaction would be raised and aired with the Board. Winokur first heard of Kopper's Chewco conflict in the Wall Street Journal article.

Brenner stated that an individual recalls that there was a glitch in the bridge loan and that Winokur was told of the problem because he was head of the Finance Committee. Winokur knows of this contention through his work on the Special Committee, but has no recollection of meeting or speaking with Kopper about a glitch in the bridge loan. If this issue were to be raised with Winokur, Kopper's supervisor, and not Kopper, would speak with him. Winokur has no recollection of Kopper's supervisor addressing this issue with him.

Winokur has no recollection of Enron's buyout of Chewco's interest in JEDI. Given what he has learned through his work on the Special Committee, he would have expected management to inform the Board of this transaction. Like any significant transaction involving an employee with a conflict of interest, the Chewco buyout should have been brought to the attention of the Board, or at least a committee of the Board.

LJM1

Winokur first learned of LJM1 in the middle of 1999. Although Winokur does not recall the timing of events, Fastow and Jeffrey Skilling presented to the Board, either together or separately, the possibility of Enron using shared forwards for hedging and bridge transaction by setting up a vehicle and using the forwards as credit support. They stated that, while it would be possible to get outside capital, it would be faster and cheaper if the counter-party was related because it would understand the transaction. Winokur does not recall any discussion that LJM1 would be a vehicle for multiple transactions and he believed that it was only for one transaction. Winokur does not recall speaking about LJM1 with Fastow or Skilling outside of Board and Finance Committee meetings.

Winokur does not recall Lay being involved with LJM1 at this time. Winokur did not discuss LJM1 with Lay outside of Board and Finance Committee meetings. Winokur believes that Lay understood the transaction when LJM1 was discussed with him. Skilling was much more involved than Lay with day-to-day matters.

Winokur's impression was that Arthur Anderson ("AA") was deeply involved with all accounting and audit aspects of setting up LJM. Enron paid AA a lot of money to do an integrated audit and they were very involved when Enron structured transactions that involved complex consolidation issues. Winokur had no discussions with AA about LJM1 or LJM2. Prior to working on the Special Committee, he was not involved in any meetings attended by AA where LJM1 or LJM2 were discussed. He had direct contact with AA during one or two meetings on other matters.

Davidow showed Winokur the minutes of the June 28, 1999 Special Meeting of the Board. Winokur generally recalls a discussion of LJM1 at the June 1999 meeting, but does not recall the specifics of that discussion. He recalls that they discussed that the purpose of LJM1 was to use the appreciation in Enron stock to hedge the volatility in Rhythms. The Board was told that employees with a conflict of interest would have no stake in value associated with a change in the price of Enron stock. The transaction was presented so as to portray the conflict and the approval process as mechanical.

The Board was also given the impression that these would not be lucrative transactions for Fastow. Winokur understood that Fastow would get a return, but, because Fastow stated that he would not be spending much time on LJM, Winokur believed that Fastow's return would be small relative to his Enron compensation. Winokur does not recall any discussion of the amount of Fastow's compensation. He focused on the need to avoid a link between Fastow's return and any change in Enron's stock price. There was no discussion at the June 1999 meeting of safeguards or procedures that would be put in place for LJM transactions.

Winokur does not recall any discussion at the meeting concerning who would negotiate with Fastow on behalf of Enron. Davidow pointed out the resolutions authorizing Lay and Skilling to negotiate on behalf of Enron. Winokur stated that the resolutions would be the type of action the Board would take. Winokur does not recall negotiations concerning setting up LJM1 actually occurring and he received no report about the resulting transaction beyond notification that it had closed. There were discussions about the disclosures that would be required, but Winokur is not sure if those deliberations occurred during the June 1999 Special Meeting.

In general, Winokur believed that LJM1 would be used for a single transaction with a specific purpose and, although the transaction would have an unusual quirk (the conflict), Enron had a good reason for using LJM, they had a fairness opinion, and Lay and Skilling would negotiate if necessary. Winokur understands the advantages of deconsolation as being a way to move debt off Enron's balance sheet and a way to hedge. Enron's goal was to maximize earning per share and return-on-equity while remaining within certain guidelines and, to the extent that debt is off-balance-sheet, this goal would be furthered.

Davidow pointed out a reference to Cuiaba in the materials attached to the minutes of the June 1999 Special Meeting. At the WCP interview, Winokur was not sure what the reference meant, but he is familiar with the asset. After the Special Meeting, he learned that Enron sold its interest in Cuiaba to LJM. Winokur does not recall what he was told about the purpose of selling Cuiaba to LJM.

LJM2

Winokur first learned of LJM2 during a presentation made by Fastow. Fastow stated that Enron had a need for continued access to third-party capital. Enron had limited ability to engage in transactions that would be on the balance sheet. Therefore, there was a benefit to keeping them off of the balance sheet. The Board's discussion centered not on whether Enron should engage in such transactions, but instead on whether Enron should engage in the transactions with a conflicted entity. Winokur did not expect Fastow to come to him, as Chairman of the Finance Committee, prior to making this type of presentation to the Board.

All of the Board members had some unease about LJM2. The issue was not hotly contested but all the members had concerns and asked questions. Winokur can not recall exactly which members voiced dissent. However, they were all persuaded that the potential benefits outweighed the risks and agreed that Enron should proceed. Winokur does not recall any Board member dissenting when the final decision was made.

LJM1/LJM2

Looking at the references to discussion regarding LJM1 and LJM2 in the minutes of the October 11, 1999 Finance Committee meeting, Winokur stated that he believes that most or all of the Committee members would have expressed their views on LJM1 and LJM2. Blake, Duncan, and Winokur did so. Others may have done so also. The benefit of using LJM was that the transactions could be done quicker and cheaper than if they were executed with third parties that were not familiar with the assets. The downside was that they would have to impose procedures to mitigate the conflict.

Winokur does not recall being told at the time that LJM would receive $41 million shortly after it had invested $30 million in the Raptor vehicles. Winokur believes that if he had been told this fact, he would have said something. If LJM's return were greater than the return on a typical bridge fund, Winokur would have spoken up.

Prior to working on the Special Committee, Winokur's understanding was that the Service Agreement was for rent, telephone service, and other ministerial services. He did not believe that the Service Agreement entailed the use of Enron employees except in an "overhead" sense. In fact, Winokur believed that no Enron employees would work for LJM except Fastow. Winokur never heard that people had left Enron to work for LJM and he never heard that Fastow was approaching Buy or others at Enron.

The Board was never asked to approve an employee's conflict of interest other than Fastow's conflict. Winokur has seen instances at other companies where employees had an interest in transactions with their companies. However, these were one-off type transactions. Winokur has never seen transactions with off-balance-sheet entities involving the type of conflict that was present at Enron.

Fastow stated that he would work on LJM matters only a few days a month and Winokur believed that transactions would only occur occasionally. Winokur had no idea that there would be so many transactions. Winokur also was never informed that assets sold to LJM were repurchased by Enron. Winokur does not recall any Board or Finance Committee discussion about a large number of deals occurring at the end of 1999. Davidow showed Winokur an attachment to the minutes of the December 13, 1999 Finance Committee Meeting showing a listing of "Year End Transactions." There was no cut-off for what deals appeared on this document except for a dollar amount threshold. The deals on the list were financings. Winokur is not sure what the threshold was for a divestment to be included on this list. It was probably around $200 million.

Davidow showed Winokur the "LJM2 Update." Winokur stated that he did not recall, in the context of this document, a discussion of a flurry of transactions occurring at the end of 1999. However, he did recall a number of financings occurring during a tight bank market at the end of 1999. Winokur also stated that it would not be surprising to find a flurry of deals in the fourth quarter because the fourth quarter is always a busy time for the finance team. Business units would over-spend during the year and then try to meet their funds flows targets with fourth quarter asset sales. In August and November, the Board had discussions regarding the number of transaction that they would need to do. The "Year End Transaction" list is probably a list of the deals that had to get done.

Winokur had no knowledge of the buy-back of assets that were sold during the fourth quarter of 1999. The Finance Committee's job was to focus on the capital structure of the company and not on earnings. They would consider earnings in the context of determining what capital plan made sense.

Controls to mitigate the conflict

Winokur considered Vinson & Elkins ("V&E") and AA to be among the best in the business. In analyzing LJM, Winokur started with the premise that Enron's attorneys and accountants would review and approve the LJM structure. Lawyers from V&E came to either a Board or Committee meeting and stated that the disclosure and conflict of interest issues were being handled properly. Winokur did not recall who from V&E attended the meeting. Winokur knew that Enron did not skimp on costs for lawyers and accountants and proceeded on the assumption that everyone would do their job correctly.

LJM2 was supposed to be a plain vanilla bridge fund. If a business unit wanted to hedge or bridge, they would approach Fastow, who would get someone from LJM to negotiate with Enron. The business unit would be responsible for negotiating and making the decision on whether to transact with LJM. For example, in connection with Cuiaba, the assumption was that the South American unit would negotiate with LJM. From the beginning, the assumption was that, because Fastow was conflicted, LJM would negotiate with Enron employees who did not report to Fastow. Winokur recalls the presentation on Raptor, but does not recall being told that Glisan would negotiate on behalf of Enron.

In addition, Causey would review every transaction. As they thought about and discussed LJM, the procedures were broadened to require that Causey, Buy, and Skilling would review the transactions. At some point, Winokur suggested that the Compensation Committee receive a report on the extent of Fastow's compensation from LJM.

Davidow showed Winokur the minutes of the May 2, 2000 meeting of the Enron Board and highlighted the resolution appointing Glisan as agent and attorney-in-fact of Enron. Based upon his reading of the resolution during the WCP interview, Winokur does not believe the resolution appointed Glisan to negotiate with LJM. Instead, it makes him responsible for the mechanical closing of the transaction.

The Board approved the overall LJM structure as a vehicle for future transactions. This structure was presented to the Board as a "done deal" with no negotiation left to be done. When Enron wanted to sell particular assets, the safe-guarding procedures, such as the deal approval process and restrictions on who could be involved in negotiations, would be employed. Winokur was not looking to make sure that the pieces of the deal were properly priced. He was told that they were already analyzed and Winokur assumed that the price, documentation, and accounting were done correctly.

Davidow pointed out to Winokur that the Board materials sometimes state that Causey would review/approve the transactions with LJM and sometimes said that Causey and Buy would do so. For example, the presentation materials for the October 11, 1999 Finance Committee meeting state that "R. Causey to approve all transactions Enron between LJM1/LJM2," whereas the minutes state that both Causey and Buy would review and approve all transactions. Winokur stated that the presentation was made by management and the Board, in its discussions, must have concluded that they needed a broader check and that both Causey and Buy should review the transactions. Around this time, the process was evolving to include the involvement of Buy's group in the merchant portfolio. Winokur was not present when Buy was told about this responsibility.

Causey's review of the transactions was meant to ensure that the accounting was proper and to start the review of whether the transactions were arms-length. Buy would also be responsible for making sure that they transactions had a market basis and were arms-length. Although Buy's people were better situated to analyze the economics, Causey's assertion that he was only tasked to review the accounting is not consistent with Winokur's understanding of Causey's responsibilities. Winokur did not have any communications with Causey or Buy regarding how they should carry out their responsibilities. However, Winokur believes that it was clear how to look at whether the transactions were arms-length.

The presentation at the February 12, 2001 Board meeting also included a reference to a review of the transactions by Causey. If Causey said that he was following-up, the Finance Committee would assume that he was doing so. Causey never qualified his presentation by saying that he was only looking at the accounting. In addition, AA did an integrated audit and he assumed that they would alert the Board if procedures were not being followed.

Winokur pointed out the minutes of the October 6, 2000 meeting of the Finance Committee. During his presentation concerning the procedures used to mitigate the conflict of interest, Fastow stated that Causey, Buy, and Skilling would approve all transaction with LJM. Winokur does not specifically remember that Skilling attended this meeting, but he can not recall any Finance Committee meetings at which Skilling was not present. Winokur never spoke with Skilling about whether he was reviewing the transactions, but at no point did Skilling state that he was not doing so.

At the October 2000 Finance Committee meeting, Fastow listed six procedures to mitigate the conflict. The Board added two additional procedures. Winokur assumed that these procedures were being followed.

Although Causey and Buy did not say exactly what they were doing, Causey stated that the procedures were being followed and the process was working. When Causey stated that he was making sure that procedures were followed, the Finance Committee assumed that he was doing so. In addition, he assumed that AA would say something if procedures were not being followed.

Raptor

The only discussion about the Raptors that Winokur recalls was a discussion about setting up Raptor 1. He does not recall separate discussions regarding Raptor 2, Raptor 3, or Raptor 4. He does not recall any discussions regarding the hedging transactions undertaken with the Raptors, regarding the Raptors' progress once they were set up, or regarding Talon and Harrier. Winokur was not told about problems with the Raptor vehicles, including that the credit capacity was gone or substantially negative, or that the Raptors needed to be restructured. He does recall a discussion about the effect of the decline in Enron's stock on off-balance-sheet vehicles. Winokur asked Fastow to prepare a report on the implications of the decline at different Enron stock prices. Events overcame that request. Winokur would have expected that the shortfall would be brought to the attention of the Board or the Finance Committee.

Winokur assumes that Lay was at the meeting at which setting up Raptor 1 was discussed, which is the only discussion of Raptor that Winokur recalls. He is confident that Lay understood the basic concept behind Raptor but is not sure what else he knew. However, Winokur believes that Lay was not involved with the details of the hedging or financing transactions. He assumes that Skilling was intimately familiar with the details about Raptor, including the pricing of derivatives, etc. Winokur would guess that, during 1999 and 2000, Skilling was the one who knew the day-to-day details. During 1999 and 2000, Lay focused on broader issues, such as international activity, and left the building and architecture of the company to Skilling. Skilling let others make the presentations before the Finance Committee. However, Skilling would lead the discussion when the directors asked questions.

Winokur was shown the presentation on Raptor that is attached to the minutes of the May 1, 2000 Finance Committee meeting. Winokur does not know the meaning of the handwritten notes stating "Does not transfer economic risk but transfers P&L volatility." He does not recall discussion about the failure to transfer risk and that statement is contrary to Winokur's understanding.

Winokur was shown the minutes of the June 22, 2000 meeting of the Executive Committee including handwritten notes on an attachment to the minutes stating "Need 6 months lead time before facility can be utilized." Winokur does not recall the discussions at this meeting. He does not recall any discussions, either at this meeting or at previous discussions about Raptor 1, about having to wait six months. In fact, he has no recollection of this issue at all. He believes that they spent more time at the June 2000 meeting on Nigerian Power Barges than on Raptor.

Merchant Portfolio

The merchant portfolio had its origins in two areas. First, a team was developing Enron's international business. They saw some of the international assets as long-term investments but would buy, build, and then sell assets like a developer. Second, on the domestic side, Enron would make loans to small oil and gas companies and companies in other industries. Enron used structured finance as a way to invest in assets it did not want to hold long-term.

In approximately 1998, as the number of assets got large, Rick Buy was given the task of analyzing and presenting these assets as a portfolio. The investments were seen as a pool that management was responsible for managing. There were limits on the size of any one transaction and on the percentage of the total portfolio any one asset could represent. However, management could recycle money within the pool at its discretion. The Board did watch the portfolio. In 2000, the Finance Committee received a report on the ten best and ten worst performing assets as well as other reports. Winokur does not recall significant deterioration in the portfolio except that the international assets had problems. The portfolio was well diversified and, although individual assets may have been volatile, the pool as a whole was not volatile. There was never discussions of the volatility of individual assets.

Proposal re LJM3

In October 2000, Fastow stated that LJM1 and LJM2 were going well and that they should consider a bigger fund. The same reasons previously were repeated. The idea was presented as something to think about and discuss more in the future if the need arose. There was not much discussion on the topic and they did not go into much detail. It was presented and then taken off the table because it was not clear that they would need a new LJM.

Fastow's compensation

At some point, Fastow described LJM as a "bridge fund." Fastow stated that he would only be working on LJM matters for a couple of days every month. Based on these statements, Winokur believed that Fastow's return would be in the "high teens." Winokur knew, and Fastow stated, that Fastow's contribution to LJM would have to be at least one percent.

Skilling did not make a written report to the Board about Fastow's LJM compensation. Winokur does not recall if Skilling gave an oral report. However, there was enough uncertainty surrounding Fastow's compensation that Winokur wanted the Compensation Committee to look into it. Winokur believed that a review of Fastow's compensation should become part of the Compensation Committee's normal review. He did not necessarily believe that it had to undertake that review at its next meeting. LJM2 had only been active for nine months, so it is not clear if a review of the issue would be meaningful at that time. Winokur does not know if the Compensation Committee ever reviewed Fastow's compensation. However, there were a number of members of the Compensation Committee at the October Finance Committee Meeting at which Winokur stated that the Compensation Committee should look at the issue.

Board and Finance Committee review of the LJM transactions

The only time that the Finance Committee reviewed the actual transactions with LJM was at its February 12, 2001 meeting. Causey listed the notional amounts of the investments. There was no discussion of the initial leverage at LJM and no detailed discussion of the individual transactions. Causey reviewed the control procedures and stated that the process was working and that additional steps had been taken to make sure the guidelines were followed. Causey did not describe the substance of the transactions beyond the details found in the written materials attached to the minutes. Instead, he focused on the facts that Buy and Causey reviewed the transactions, that they were arms-length, that Skilling was looking at the transactions and at Fastow's compensation, and that not much time was spent by Fastow on LJM matters. Winokur was not expecting to see problems. However, he wanted to hear that procedures were followed.

Davidow directed Winokur to the "Related Party Transaction - LJM 2000 Internal Policies and Procedures" attachment to the minutes of the February 2001 meeting, which states "Chief Accounting and Risk Officer reviewed and, where appropriate, approve." He does not know the meaning of "where appropriate" or why it was included in the presentation. He does not remember discussion of this qualification.

Mintz and Glisan attended the February 2001 Finance Committee meeting. Jim Derrick was not routinely at meetings and Winokur does not believe that anyone else from the Legal Department attended. The meeting lasted one hour and forty minutes. Causey's presentation lasted approximately fifteen to thirty minutes. Winokur does not recall if the Committee members questioned Causey. Prior to the meeting, only the Audit Committee had reviewed the transactions.

Winokur has no recollection of anyone asking Causey or Buy what they were doing to look at specific transactions. Causey never explicitly said that he was doing anything other than analyzing the accounting behind these transactions. However, the Board made it clear that they wanted serious procedures to mitigate the conflict of interest. Causey said that he was looking at the transactions and no one, including Causey, ever said that Causey was only analyzing the transactions from an accounting perspective. Winokur had more contact with Buy than Causey. Buy never said that he was only looking at the transactions from a risk perspective. In every discussion with Buy, Causey, and Skilling, they implied that they were taking total ownership of the entirety of the transactions.

Skilling's statement that as long as Buy and Causey signed off, he would approve the transactions is inconsistent with Winokur's understanding of Skilling's role. Given the importance of the SPVs and the Board's concern regarding conflicts, Winokur expected Skilling to be much more involved with the process. He did not expect Skilling to know every detail. However, he thought that Skilling was asking enough questions of Causey and Buy so as to understand how they knew that the appropriate procedures were followed. Skilling did not say he was doing these things. Winokur assumed he was doing so based on Skilling's role at the company and the manner in which he ordinarily fulfilled his responsibilities.

Disclosure

Winokur did not know about any advice received by Enron about how to avoid disclosure. He also did not know about any discussions regarding structuring the deals so as to avoid disclosure of the related party transactions. At one of the Board or Committee meetings, Fastow stated that disclosure of specific transactions would be required, but that disclosure concerning setting up LJM was not required.

Winokur's closing remarks

At the end of the interview, Winokur was invited to make additional remarks. He stated that Enron was a fast growing company that changed business models every two years, that had smart people, and that was decentralized. The company used equity to compensate employees and its core value was "be the best." Around the decentralized entrepreneurial system, there were supposed to be tight controls, such as risk management. Over ten years, there were no significant trading busts.

When he voted to approve the related-party vehicles, he knew the transaction involved people that he knew, and had every reason to trust. Both Skilling and Fastow were well-regarded both inside and outside the company. However, Winokur proceeded with his eyes open. He tried to improve the controls. He knew that AA did an integrated audit of the company and he knew that V&E was involved with the disclosure issue. He believe that in both the legal and accounting areas, Enron had strong people both inside and outside the company.

There were several presentations during which the company's top officials stated that the procedures were being followed. There was no push-back regarding what they were asked to do and Winokur had no sense that they were not doing a complete job.

Winokur recently discovered that there was an extraordinary disconnect between what he was told was happening and what actually occurred. Without his knowledge, Enron employees other than Fastow had a conflict. There were no arms-length negotiations. What was intended to be a bridge fund was actually a finance and accounting vehicle that was very complex. Winokur does not know what caused this disconnect or why no one said anything even though many, inside and outside the company, were in a position to do so.

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MEMORANDUM

TO: Enron Files

FROM: Reed M. Brodsky

DATE: January 11, 2002

RE: Interview of Dr. Robert Jaedicke

On January 9, 2002, Chuck Davidow and Reed Brodsky of Wilmer, Cutler & Pickering ("WCP") and Ron Forster of Deloitte & Touche (an accounting firm retained by WCP), spoke with Dr. Robert Jaedicke, the Chairman of the Audit and Compliance Committee of Enron's Board of Directors, at the offices of Gibbs & Bruns in Houston to gather information from him in order to allow WCP to provide legal advice to the Special Committee of Enron's Board of Directors. Robin Gibbs, Kathy Patrick, Jean Frizzell, and Jeremy Doyle of Gibbs & Bruns and Neil Eggleston of Howrey Simon Arnold & White, LLP, were present and represented Dr. Jaedicke.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Dr. Jaedicke's statements. The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Dr. Jaedicke has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

Davidow explained that we represented the Special Committee of Enron's Board of Directors, that the conversation was privileged and confidential, but that the Special Committee could waive the privilege, and that it was very likely that the Special Committee would pass along what information we learned to the SEC and others looking at the issues. Dr. Jaedicke indicated that he understood.

Background

Dr. Jaedicke taught for twenty years at the University of Minnesota where he had obtained his PhD. Subsequently, he taught at the Harvard and Stanford business schools. At Stanford, he spent more time in the Dean's Office than teaching. He taught mainly accounting and some financial courses. In 1993, Dr. Jaedicke retired from Stanford and served on Boards of Directors for public companies and consulted for companies in the California area. At one time or another, Dr. Jaedicke served on the Boards of State Farm Insurance, GenCorp, Inc., Wells Fargo Bank, Homestake Mining Company, California Water Services Company, and Enron. Although he passed the CPA exam in 1952, Dr. Jaedicke is not a licensed CPA.

Dr. Jaedicke has been a director on Enron's Board since 1985. He has served on the Nominating and Corporate Governance Committee, the Compensation Committee, and the Audit and Compliance Committee. He is currently Chairman of the Audit Committee and serves on the Compensation Committee. He has never been on the Finance Committee, although he has attended some of its meetings.

SPEs

Dr. Jaedicke is familiar in general with the rules governing special purpose entities or vehicles ("SPEs"). He knows that there are equity and control requirements, that SPEs are widely used, and that the Emerging Issues Task Force has issued guidance on SPEs for some time. He could not recall when he first learned the term "SPE," but off-balance sheet financing has been used by Enron for a very long time. He read summaries of EITF bulletins relating to SPEs and heard about SPEs in general while serving on the Audit Committee from people like Rick Causey, Arthur Andersen representatives, and some members of the Audit Committee. His familiarity with SPEs stemmed solely from his work at Enron.

Chewco / JEDI

Dr. Jaedicke heard the word "Chewco" for the first time in October 2001 from an article in the Wall Street Journal. He heard the word "JEDI" from Board discussions. JEDI was a partnership between Enron and CalPERS in the early 1990's. CalPERS wanted to sell its interest in JEDI before forming a second partnership with Enron called JEDI II. Dr. Jaedicke knew that a buyer wanted to purchase CalPERS' interest in JEDI, but he did not recall the details. He did not remember a lot of discussion about the buyout of CalPERS' interest during Audit Committee or Board meetings.

LJM1

In June 1999, during a telephone meeting, LJM1 came to the Board's attention. The presentation came directly to the Board; it did not come through the Audit or Finance Committees. LJM1 was discussed by Lay, Jeffrey Skilling, Andrew Fastow, and Jim Derrick (with respect to legal issues). Fastow was the principal of LJM1. The structure was reviewed by inside counsel, outside counsel, and Andersen. Andersen and legal personnel analyzed whether the structure met the requirements for an SPE. Andersen signed off on the structure and stated that the conflict of interest had been managed. Internal and external legal counsel stated that they were comfortable with the arrangement. There were many questions and a lot of discussion about why Fastow wanted to form LJM1, the kinds of transactions and financings that could be done through LJM1 to take advantage of the value of Enron's stock, how the use of LJM1 would reduce Enron's costs, and how Fastow could bring together parties interested in making investments.

In August 1999, there was a discussion, although not a detailed one, about LJM1. By then, the Audit Committee knew that it would be reviewing all LJM transactions between June 1999 and the end of December 1999. The Board resolution approving LJM1 would have included the Audit Committee's review of any transactions. By February 2000, both LJM1 and LJM2 existed, and the required review continued with LJM2.

LJM2

The Finance Committee discussed LJM2 prior to the presentation of LJM2 to the Board. The Finance Committee discussed Fastow's conflict of interest. Norm Blake, a former Audit Committee member, asked Causey twice whether Andersen and legal personnel had reviewed the potential conflict of interest. Causey told Blake and the Committee both times that Andersen, the accounting people, and legal were comfortable with the transaction. So long as the Board's procedures were met, no one expressed any disagreement with Fastow serving as head of LJM1 and LJM2.

Conflict of Interest. Certain procedures were put in place to address the conflict of interest. Enron's ethics-policy continued to apply, both the LJM2 limited partners and Enron could ask Fastow to remove himself as general partner of LJM2, the Audit Committee would review the transactions to make sure that the transactions were negotiated at arm's-length, fair to both parties, and not biased one way or the other, and Enron was not obligated to carry out any transactions with LJM2. LJM2 was also a vehicle for investments by Enron's business units that would negotiate hard against LJM2. LJM2 was a little different than LJM1, which was aimed more at hedging Enron's investment in a stock. Dr. Jaedicke took comfort in the fact that there was a disclosure in the footnotes of public filings that the transactions were done at arms-length. He could not recall the exact wording, but Andersen had a continuing responsibility to audit and make sure that the statement in the disclosures was substantiated.

Review of Transactions. The Audit Committee always looked to Causey to sign off that the Board's requirements had been followed on each LJM1 and LJM2 transaction. It was important that Causey inform the Audit Committee that the transactions were done at arm's-length. Causey was supposed to look at the transactions to make sure that the terms appeared fair. By the time the Audit Committee reviewed the transactions in February 2001, there was an elaborate procedure in place to make sure that the transactions were done at arm's-length. Specific people had to sign off on the transactions. Also, by this time, the deal approval sheet had been developed, and the Committee expected Causey, Rick Buy, and Skilling to sign off on the deal sheet in accordance with the Board's procedures and the appropriate review by Andersen, inside counsel, and outside counsel.

LJM1 was intended to be an SPE. In almost every Audit Committee meeting, Andersen and legal were present, along with Causey, Buy, and other members of management. The Committee expected Andersen and legal to conduct a real-time review of any transactions with LJM1 and LJM2. The Committee heavily relied on the advice of Andersen and legal, and the Committee would ask Andersen and legal for their views of the transactions at almost every meeting. Andersen would present the structure of the vehicles and frequently told the Board that LJM1 and LJM2 met the structure requirements. The Committee also expected Andersen to pay attention that Causey and others followed the Board's procedures. The Company paid Andersen a lot of money to make sure that the structures were proper and Enron's disclosures complied with the rules.

SPE Rules. Enron could not control the SPE or it would not meet the requirements for deconsolidation. Fastow was the manager of LJM1's general partner of LJM1. Dr. Jaedicke did not recall any specific discussion of how LJM1 and LJM2 met the control requirements for deconsolidation, but he relied on Andersen's assurances that the requirements were met. The Audit Committee was told that Andersen was involved when LJM1 and LJM2 were structured in the beginning, and the Committee took comfort in the fact that Andersen would make sure that they would be accounted for in the proper way and meet the requirements for an SPE. LJM1 and LJM2 were reviewed by Andersen's engagement partners, its Houston office, and Andersen's experts in the use and application of SPEs from its Chicago and New York offices. The Committee assumed that Andersen would review the process to make sure that it met all the proper requirements. Dr. Jaedicke did not recall any detailed discussions with Andersen with respect to whether LJM1 and LJM2 met the control requirements.

Fairness Opinions. Fairness opinions for LJM1 and LJM2 transactions were not generally obtained. Fairness opinions from PricewaterhouseCoopers relating to some transactions were mentioned in Board meetings.

Lay. Lay was the CEO when LJM1 and LJM2 were formed, and Lay attended all the Board and Audit Committee meetings when LJM1 and LJM2 were approved. Dr. Jaedicke did not recall how active Lay was in discussions about LJM1 and LJM2. Fastow and Skilling lead the presentations of LJM1 and LJM2 before the Board. Skilling was heavily involved in the presentations.

LJM2 Buybacks

Dr. Jaedicke did not hear that Enron bought back assets sold previously by Enron to LJM2. The buybacks should have been raised during the Audit Committee's annual review of LJM1 and LJM2 transactions.

June 28, 1999 Board Meeting

Dr. Jaedicke's attention was directed to the first two full paragraphs on page six of the minutes of the June 28, 1999 Board meeting. The reference to Skilling's statement that the Company had been analyzing new types of financing vehicles for off-balance sheet transactions refers to changes in accounting treatment for off-balance sheet transactions. The Company expected new guidance aimed at consolidation and SPEs, but Dr. Jaedicke did not think that any guidance emerged. A discussion about hedging the Company's investment in RhythmsNet followed. The volatility of the Company's investment in RhythmsNet posed some accounting problems, as the Company had to mark-to-market its investment. The volatility was an issue in the second quarter 1999. One option was to hedge the Company's investment in RhythmsNet so that the Company would have confidence in marking its value to market and reporting it that way.

Enron transferred to LJM1 in-the-money forwards on Enron stock to LJM1 and, in return, received a payment from LJM1. Dr. Jaedicke did not recall the restriction imposed on the stock transferred to LJM1. Enron hoped the value of its stock would increase, and the Company financed the transaction without selling and further diluting Enron stock. LJM1 then entered into a hedge on RhythmsNet. Dr. Jaedicke did not recall having knowledge of or a detailed discussion about whether LJM1 had the credit capacity to enter into this hedge.

Dr. Jaedicke's attention was directed to page four of the Project LJM Board Presentation, entitled "Transaction Summary." Dr. Jaedicke did not recall a lengthy discussion about item number three, which states that LJM "negotiates with Enron for purchase of additional merchant assets." Dr. Jaedicke's impression was that LJM1 was discussed as a one-off transaction. The main discussion about LJM1 focused on RhythmsNet. There was little discussion of the transactions LJM1 and Enron would enter into in the future. Dr. Jaedicke did not recall any discussion of controls that should be implemented with respect to transactions with LJM1.

Dr. Jaedicke's attention was directed to page six of the Project LJM Board Presentation, entitled "Benefits to Enron." With respect to the first bullet point on that page, stating "Enron receives a $50 million cash payment and a Rhythms NetConnections put valued at $90 million," Dr. Jaedicke stated that he did not recall how much money was invested in LJM1. He did not remember any detailed discussions of whether LJM1 could pay $50 million in cash and enter into a put valued at $90 million when there was only $20 million invested in LJM1. With respect to the last bullet point, stating "Capture Cuiaba / Elektro value," Dr. Jaedicke stated that he did not recall any discussion about transacting with LJM1 in connection with Cuiaba or Elektro.

Dr. Jaedicke's attention was directed to the first page of the Appendix to the Project LJM Board Presentation. Dr. Jaedicke did not recall any specific discussion of whether LJM1 had sufficient credit capacity to support the swap shown in the diagram between Enron and LJM Swap Sub, a subsidiary of LJM1.

10-Q for the Second Quarter 1999

Dr. Jaedicke's attention was directed to Note 8 to the Financial Statements in the 10-Q for the second quarter 1999 discussing Enron's related party transactions. The Audit Committee reviewed draft 10-Q's. The second quarter 10-Q in 1999 disclosed the related-party transaction. It put the reader on notice that transactions between LJM1 and Enron did not have to take place, that future transactions may take place, that there was a transfer of shares to LJM1, that a senior officer of Enron was the managing member of LJM1's general partner, and that management believed the terms were reasonable. The statement that management believed the terms were reasonable and no less favorable than the terms of similar arrangements with unrelated parties was an auditable statement. Dr. Jaedicke assumed that Andersen analyzed the transactions before giving an unqualified opinion to management. Dr. Jaedicke did not recall being presented with an LJM1-related transaction that could not be done with a third party. LJM1 was presented as the opportunity to take advantage of a senior Enron officer's contacts with investors, and it would have been more expensive to carry out the transactions with a third party. Dr. Jaedicke did not recall whether there was any discussion of what Andersen or Causey did to make sure that the transactions were arm's-length. He had no recollection of whether Andersen or Causey or anyone else was asked whether third parties were contacted before entering into these transactions with LJM1.

The Board relied on Andersen and the Company's management to make sure that the related-party transactions were reviewed and disclosed in the 10-Q. The Audit Committee had many discussions with Andersen about the Company's accounting policies and principles, SEC requirements, and Andersen's role in making sure that the Company complied with those policies, principles, and requirements. Andersen's Thomas Bauer, David Duncan, and Stephen Goddard were always present at every Audit Committee meeting.

October 11-12, 1999 Board Meeting

Dr. Jaedicke's attention was directed to page seventeen of the minutes of the October 11-12, 1999 Board meeting. Herbert Winokur introduced LJM2. Dr. Jaedicke did not recall any discussion of whether or how LJM2 met SPE requirements, including the control requirement. Although page four of the presentation states that Causey would review the transactions, both Causey and Buy were required to review and approve all transactions, as stated in the minutes. Causey and Buy always attended the Audit Committee meetings.

Dr. Jaedicke's attention was directed to the first page of the presentation on LJM2, entitled "LJM1 Update." The update refers to LJM1 raising $16 million outside equity, a $64 million cash payment to Enron, and a RhythmsNet swap that was in the money $164 million for Enron. Dr. Jaedicke did not recall any discussion of whether LJM1 could pay $64 million and $164 million given its $16 million equity capitalization. The update also refers to Enron benefiting from LJM1's purchase of a stake in Cuiaba. Dr. Jaedicke did not recall any discussion about Cuiaba at the time. He also did not recall any discussion of subsequent problems with Cuiaba, or Enron's repurchase of LJM1's stake in Cuiaba.

February 7, 2000 Audit Committee Meeting

Dr. Jaedicke's attention was directed to the last paragraph on the third page of the minutes of the February 7, 2000 Audit Committee meeting, which refers to Causey's report outlining the transactions that had been completed with LJM1 and LJM2. Dr. Jaedicke did not recall how much time Causey spent making the presentation. There was a handout that accompanied Causey's presentation listing the transactions. Causey did not review each transaction in detail, but rather commented about each one briefly. This was the first time that the Audit Committee reviewed the LJM1 and LJM2 transactions. The discussion and questions centered around whether the transactions met the Board's requirements and controls. Buy also attended the meeting, but Dr. Jaedicke did not recall whether Buy was also asked whether the transactions met the Board's requirements and controls. The Committee asked whether Andersen was comfortable with the transactions, and Andersen said that it was. Dr. Jaedicke did not recall Causey mentioning Cuiaba or any other transaction that was not listed on the handout. The transactions with LJM1 and LJM2 seemed to be the type of transactions that were expected between Enron and LJM.

10-K for 1999

Dr. Jaedicke's attention was directed to note 16 to the financial statements in the 10-K for 1999 discussing Enron's related party transactions. Management did not review note 16 with the Audit Committee or Dr. Jaedicke. Causey presented the 10-K to the Committee and was asked about any changes that were made. Causey directed the Committee's attention to particular parts of the 10-K. The Committee asked Andersen and Derrick for their comments. The discussion centered around whether the disclosures in general were adequate and proper. Dr. Jaedicke did not recall any discussion of the related party disclosures, including the bundling together of transactions in the related-party footnote. He did not recall anyone comparing the 10-K to Causey's list of LJM1 and LJM2 investment activity in the February 7, 2000 Audit Committee meeting.

May 2, 2000 Board Meeting

Dr. Jaedicke's attention was directed to the statement "Q4 1999: 8 days/6 deals/$125 million" in Fastow's May 1, 2000 presentation entitled LJM2 Update. Dr. Jaedicke did not recall any discussion of this statement. There was a discussion of the level of return that LJM2 was expected to receive from Enron. LJM2 was compared to a bridge fund, and it was discussed that LJM2 would receive less than or equal to a twenty percent return. Dr. Jaedicke assumed that LJM2 would be leveraging its investments, but he did not recall whether LJM2's twenty percent return would take place before or after LJM2's leveraging.

Dr. Jaedicke's attention was directed to page four of the minutes of the May 2, 2000 Board meeting, which referred to the approval of Project Raptor, and the five-page handout on Project Raptor. Dr. Jaedicke did not recall the discussion of Raptor in detail. He learned about Raptor reading through the May 1, 2000 Finance Committee material. He did not know the substance of the transactions in detail. Raptor was intended to use the increased value of Enron's stock as a hedge against volatility in Enron's earnings. He did not recall exactly why Raptor was done or set up with a preferred return for a limited investment. He did not recall any discussion of whether Raptor met the requirements for an SPE. He relied on the people who told the Board that Raptor was appropriate. The Board was told repeatedly that Enron was on the front-end of these types of investments, and the Board relied on outside experts for this service. Dr. Jaedicke did not recall whether the statement on page 23 of the Project Raptor handout – "does not transfer economic risk but transfers P&L volatility" – was made.

Dr. Jaedicke's attention was directed to page 24 of the Project Raptor handout discussing Raptor's structure. Andersen told the Audit Committee that Andersen looked at the structure. The minutes to the Audit Committee meetings should have specific references to an Andersen presentation reflecting Andersen's work on structured transactions and financing vehicles. Andersen's presentation named LJM2 by name. Dr. Jaedicke did not recall any discussion of the statement on page 24 that Enron "purchases a share settled put on approximately 7 million shares of ENE stock for $41 million," or how Enron's purchase of a put on its own stock would appear to the public. The risk of "accounting scrutiny" on page 25 of the Project Raptor handout referred to the fact that disclosure issues had to be dealt with and the Raptor structure was complex. Enron mitigated the risk by paying its experts, such as Andersen, to make sure that the transactions were disclosed properly. No one told the Board that the accounting for Raptor was close to the line of permissible accounting. The Board was told that the Company had to continue to work on the Raptor transactions. If the Board had heard that the accounting for Raptor was close to the line, they would have investigated why.

10-Q for the First Quarter 2000

Dr. Jaedicke's attention was directed to note 7 to the Financial Statements in the 10-Q for the first quarter 1999 discussing Enron's related party transactions. He did not recall any changes to the language describing that "[m]anagement believes that the terms of the transactions with related partiers were reasonable and are representative of terms that would be negotiated with unrelated third parties." He did not recall noting or discussing that the language had changed from the 10-Q for the third quarter in 1999, which stated that management believed the terms were "no less favorable than the terms of similar arrangements with unrelated third parties."

10-Q for the Second Quarter 2000

Dr.Jaedicke's attention was directed to note 7 to the Financial Statements in the 10-Q for the second quarter 1999 discussing Enron's related-party transactions. He did not recall the unwinding of Enron's RhythmsNet transaction with LJM1. He did not remember any discussion of the disclosure that "Enron paid approximately $26.8 million to the Related Party." With respect to Raptor, based on the disclosure in note 7, the reader would understand clearly that transactions were done with a related party, that Enron contributed assets to "newly-formed entities," that the transferred assets were worth approximately $800 million, that Enron's stock was transferred, that the transfers were subject to certain conditions, which would imply that restrictions were imposed, and that the entities in turn transferred specific assets back to Enron.

10-K for 2000

Dr. Jaedicke's attention was directed to note 16 to the Financial Statements in the 10-K for 2000 discussing related party transactions. He did not recall any discussion of the statement in the third paragraph that "Enron recognized revenues of approximately $500 million related to the subsequent change in the market value of these derivatives, which offset market value changes of certain merchant investments and price risk management activities." He did not recall any discussion of the $500 million revenue, the level of revenues Enron recognized, or the capitalization of the Raptor entities.

February 12, 2001 Audit Committee Meeting

The annual review of LJM1 and LJM2 transactions in the February 12, 2001 Audit Committee meeting did not differ from the February 7, 2000 Audit Committee review. Data about the transactions were presented in the same form.

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10-Q for the First Quarter 2001

Dr. Jaedicke did not know at the time in 2001 that the Raptor vehicles were so undercapitalized that they owed Enron $350 million more than they could pay.

Dr. Jaedicke's attention was directed to note 8 to the Financial Statements in the 10-Q for the first quarter 2001 discussing related party transactions, and the statements in the second paragraph that Enron delivered 12 million shares of restricted stock into entities and also entered into share settled costless collar arrangements on the 12 million shares. He was not familiar with the costless collar arrangements. He did not know and did not recall any discussion about how Enron could have entered into these costless collars when the shares of stock were restricted and thus were precluded from being hedged.

Enron's Controls

Enron had many unique processes and structures in place to review related-party transactions. Enron had integrated Audit and Finance Committees that were paying attention to the structure of these transactions. The Audit Committee adopted unique procedures to watch and make sure that the Company had complied with the Board's controls and requirements. Causey, Buy, and the financial officers at Enron reviewing and approving the transactions held equal positions at the executive vice president level. Many controls were put in place. Andersen audited the Company's work, and Andersen's auditing function was very important. Enron was always willing to pay the bill for outside expert advice on the related-party transactions.

For years, capital markets have developed accounting techniques and related disclosures. Special purpose entities involving leases have been around for years. Enron made a real attempt to get ahead of that curve, involve Andersen from the very beginning of these transactions, implement the necessary arrangements to review the transactions, and use every resource available to make sure that they were done right. Enron did not just do what was necessary to meet the bare minimum, but tried to be a positive force that would meet and satisfy the requirements.

Stock Sales

Dr. Jaedicke reported two sales of stock in 2000 and 2001. The sales were connected with his expiring options. They both involved cashless exercises of options. One sale occurred after the Board meeting relating to the 10-K for 2000; had he not sold them, the options would have expired.

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MEMORANDUM

TO: Enron Files

FROM: Steven Rosen

DATE: January 14, 2002

RE: Interview of John Mendelsohn.

On January 11, 2002, Charles Davidow and Steven Rosen of Wilmer, Cutler & Pickering ("WCP") and Jason Richards of Deloitte & Touche (an accounting firm retained by WCP), spoke with John Mendelsohn, a director of Enron Corp., at Enron's Houston headquarters to gather information from him in order to allow WCP to provide legal advice to the Special Committee of Enron's Board of Directors. W. Neil Eggleston of Howry, Simon Arnold & White and Kathy Patrick, Robin Gibbs, Jean Frizzell, and Jeremy Doyle of Gibbs & Brun represented Duncan at the interview.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Mendelsohn's statements. The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Mendelsohn has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

At the outset, Davidow explained that WCP represented the Special Committee appointed by the Board to investigate certain transactions between Enron and related parties, and we were speaking to him as part of that investigation. Davidow stated that we did not represent Enron's officers or employees, including him, that, in our view, the conversation was privileged but it was the Special Committee's (or Enron's) privilege, and that the Special Committee or Enron could decide what to do with the privilege, not him. Davidow stated that Mendelsohn should anticipate that anything he told us could be communicated to others, such as the Board, others associated with Enron, and the Government.

Background

Mendelsohn is a graduate of Harvard College and Harvard Medical School. Mendelsohn practiced medicine at the National Institute of Health and at Brigham and Women's Hospital. He has served on the faculty of the University of California, San Diego Medical School and was Chairman of the Department of Medicine at Memorial Sloan-Kettering Cancer Center in New

York. For the last 5 ½ years, he has been the President of the University of Texas M.D. Anderson Cancer Center.

In June 1999, Ken Lay asked Mendelsohn to join Enron's Board of Directors. He is on the Audit Committee and the Membership Committee. He considers himself to be financially literate, but not expert. Mendelsohn has not sold Enron stock recently.

LJM

The Board discussed LJM at Mendelsohn's first Board meeting. There was a discussion about Enron's need for an entity to monetize assets and raise funds and about LJM's ability to fill that role effectively and appropriately. The Board had a long discussion about Andrew Fastow's involvement as principle of LJM1. A similar Board discussion occurred at a later time concerning Fastow's role at LJM2. The deals were complex and needed to be undertaken quickly. Fastow's knowledge would make this possible. Mendelsohn assumed that there would be a firewall between Fastow and the LJM transactions so that neither Fastow nor his subordinates would be involved in negotiations. Mendelsohn does not recall any differences in the controls put in place for LJM1 and LJM2.

In connection to LJM1, Mendelsohn does not recall discussion concerning the nature of the Rhythms hedging transaction. He believed that Enron was engaging in hedging transactions with LJM1 or LJM2 (he does not recall which one) in order to protect the value of certain assets. In addition, the transaction would allow the assets to be managed better. LJM also provide a way for Enron to raise additional money.

Mendelsohn does not recall being told that Enron repurchased the assets sold in the LJM transactions. He does not recall being told that Enron employees other than Fastow were working at LJM or that, under a services agreement, Enron employees were providing services to LJM.

Audit Committee Oversight

At each meeting of the Audit Committee, Rick Causey and David Duncan reported that they were monitoring the transactions and that everything was going according to plan. At the February 2000 and February 2001 Audit Committee meetings, Causey and Duncan, using flip charts he believes were on AA paper, described the individual LJM transactions. Each presentation lasted approximately fifteen to twenty minutes. Causey did not give a detailed description of the transactions. Instead, they put each of the deals into categories. The Committee members asked question, although Mendelsohn cannot recall the specific questions. With a relaxed demeanor, Duncan assured the Committee that control procedures, the Code of Ethics, and SEC rules were being followed. Duncan stated that, in addition to audit tasks, he was spending a lot of time making sure procedures were followed. Mendelsohn believed that the role of the Committee was to make sure the control procedures were followed and not to review the transactions.

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MEMORANDUM

TO: Enron Files

FROM: Lisa Henriques

DATE: January 30, 2002

RE: Interview of Norman Blake

On January 29, 2002, Charles Davidow and Lisa Henriques of Wilmer, Cutler & Pickering ("WCP") spoke with Norman Blake, Member of the Board of Directors, via telephone to gather information from him in order to allow WCP to provide legal advice to the Special Committee of Enron's Board of Directors. Kathy Patrick and Jeremy Doyle of Gibbs & Brun and W. Neil Eggleston and another lawyer of Howrey Simon Arnold & White participated by phone and represented Mr. Blake.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Blake's statements. The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Blake has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

At the outset, Davidow explained that WCP represented the Special Committee appointed by the Board to investigate certain transactions between Enron and related parties, and we were speaking to him as part of that investigation. Davidow stated that we did not represent Enron's officers or employees, including him, that, in our view, the conversation was privileged, but it was the Special Committee's (or Enron's) privilege, and that the Special Committee or Enron could decide what to do with the privilege, not him. Davidow stated that Blake should anticipate that anything he told us would be conveyed to the Special Committee, and that the information could be communicated to others, such as the Board, others associated with Enron, and the Government.

Davidow thanked Blake for taking time out of his schedule to meet with us. Patrick mentioned Blake was unable to thoroughly review the Board minutes WCP provided him due to time constraints on his schedule.

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #77d

EC2 000000181

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Special Meeting of the Board on June 28, 1999:

During this meeting there was a presentation to the Board regarding the creation of a partnership, LJM1, and the Rhythms transaction. Blake believed that LJM was a one-off transaction and thought that if other assets were going to be bought by LJM, it would go to the Board for approval. Blake does not recall any other transactions with LJM1. LJM1 was created to accommodate the need to hedge Enron's position in Rhythms stock. Andy Fastow would serve as the general partner of LJM1. Blake was not aware of any other third parties involved in LJM. Enron wanted to be able to hedge the position quickly and in order to do this they needed the third party to be able to transact and understand the structure quickly. Having Fastow serve as the general partner enabled Enron to have a third party that it could transact with quickly. In addition, transactions with LJM had lower transaction costs.

Blake believed that Fastow would receive the standard industry compensation for his involvement in LJM. Blake recalls that the model for his compensation was disclosed and that Skilling was going to review Fastow's compensation. It was implied that Skilling would oversee the process. Blake realized that Fastow's compensation could change according to the success of the Rhythms hedge because he made an investment and that there were risks. Blake believed that Skilling understood LJM and his responsibility to oversee Fastow's involvement.

Blake believed that Ken Lay understood the structure and he would oversee that the deal was fair and would not compromise Enron's interest. Lay would inform the Board if the terms of the structure or relationship changed.

There was skepticism and concern that Fastow, serving as Enron's CFO, would also be involved in a partnership that would transact with Enron. There was a waiver of the Code of Conduct, but Blake believed that it was more in form than in substance. Fastow still had a fiduciary duty to the company. There were a number of controls put in place to ensure that no problems would arise. For example, the Chief Risk Officer reviewed each deal. There were conversations about the consolidation rules and whether the deals were done at arm's length. Causey told the Board about the consolidation rules and said that the more control Fastow had over the LJM partnership the more the consolidation rules would be an issue.

Blake felt comfortable with the partnership because Causey said that Andersen was involved and approved the structure. Also, Vinson & Elkins ("V&E") oversaw Enron's Code of Conduct rules and these transactions. V&E had no problems with the structure.

Blake believed that the economic risk of the Rhythms hedge was transferred because if the economic risk was not transferred, it would cause consolidation of the LJM onto Enron's books. When asked by WCP how this was possible because Enron stock was used to hedge against itself, Blake replied he believed that the Enron stock was funded by a UBS forward and Andersen would not have approved the transaction if there was not adequate equity in the structure. Both Causey and Andersen said that the transaction was fine, so Blake assumed that there was enough equity at risk to comply with the SPE rules.

Blake could not recall whether Andersen, itself, made representations to the Board that they were involved in approving the structure.

Finance Committee Meeting, October 11, 1999:

When LJM2 was presented to the Board it was not in association with a specific transaction. Enron was looking for a structure that it could sell assets to in order to take them off the balance sheet. There was a lot of internal competition between the Enron subsidiaries and they were all driven to maximize the value of the their assets. Because it was in the best interest of the divisions to get the best price for the assets, the Board felt that it would ensure arm's-length negotiations with Fastow and LJM2. Blake was not aware of any other Enron employees that would be involved in LJM. He did not know about Michael Kopper's involvement and never heard of a service agreement between Enron and LJM2 to share the cost of Enron employees.

The advantages of LJM2 were transactions could be executed quickly, they could capture market value, LJM was flexible, LJM served as an optional equity investor and it reduced transaction costs. Fastow's involvement was beneficial because the transactions were complex and Fastow was already familiar with them.

Blake was under the impression that Enron employees in Global Finance who reported to Fastow would not negotiate with LJM or Fastow. Only the business unit heads would negotiate with the LJM because it was in their interest and it was their responsibility to obtain the best price for the assets they were selling. It was possible that the heads of the business units would go to Fastow's group for financial advice, but in the end, it was their responsibility to get the best deal.

Oversight Roles:

There were a number of procedures put in place to oversee the transactions. Causey, Buy and Skilling were responsible for reviewing the transactions.

Causey: Causey was the Chief Accounting Officer and he was responsible for reviewing each transaction to ensure the terms of the transactions were fair and make sure the accounting was proper. Causey had a fiduciary responsibility to act in Enron's best interest. He oversaw the entire relationship. He saw the economics of the deals and was responsible for ensuring that the process was followed.

Buy: Buy had similar responsibilities to Causey. He was the most competent analyst at Enron. Buy was responsible for looking at the transactions as a whole and at the underlying credit risk of the transactions. Blake thought Buy was responsible for looking at the transactions volatility and the adequacy of the equity.

Skilling: Skilling was responsible for overseeing the entire process, and in particular to ensure that the Code of Conduct was not being violated. Everyone knew that these were special transactions and Skilling was aware of the problems with the conflict of interest. Fastow reported to Skilling and Skilling was responsible for supervising him.

Lay: Lay had an oversight role, but it was different than Causey, Buy or Skilling's role. When Skilling was about to take over as CEO, Lay began to turn responsibilities over to him. Lay still had oversight responsibilities because he was Chairman and CEO.

Audit Committee Review:

Blake is familiar with the role of an audit committee in a company from his experience as a member of another company's audit committee. Blake believes that much of the control process of a company occurs in the audit and the audit committee's review. The other company's audit committee's routine is to be sensitive to noncompliance issues with procedures, create remedies for noncompliance and follow up at the next meeting about the implementation. He believed that this was the same procedure for Enron's Audit Committee.

Blake believed that if there was a problem with any of the transactions that Andersen or V&E would bring the issue to the attention of the Committee.

Finance Committee Review:

Blake suggested on October 6, 2000, that the Finance Committee conduct quarterly reviews of the LJM transactions. Blake made the suggestion because he was concerned that an annual review of the transactions would not be sufficient due to the number of transactions Enron was engaging in with LJM.

After the suggestion in October, the reviews were not done quarterly. Blake said that the follow-up on the reviews was terrible. The Finance Committee only conducted one quarterly review in February 2001. Skilling wanted to reduce the Board's involvement in the day-to-day aspects of Enron. He did not oppose the Finance Committee reviewing the transactions, but he was not happy about it. Pug Winokur and Blake had some conversations about the reviews outside of the Board and Committee meetings, but he does not know why they never continued the reviews. Blake did not attend the Finance Committee meeting in February 2001, so he did not participate in the only quarterly review of LJM transactions. Winokur told Blake that the Finance Committee had done a review the of the LJM transactions at the February 2001 meeting. Winokur did not believe the quarterly reviews were necessary after February 2001 because a few months later Fastow sold his interest in LJM and there was no longer a conflict.

Finance Committee Meeting, May 1, 2000:

In one of the presentations to the Committee there was a slide entitled "LJM2 Update." One of the items listed was "direct and indirect earnings was $229.5 million." Blake did not recall a discussion about Enron making this much money from transactions with LJM. Blake recalls that there was a discussion about the $2 billion funds flow. The rational for these structures were to create funds-flow and provide liquidity relief. The amount of earnings may have been significant for the quarter, but he did not believe they were significant for the yearly earnings. Blake focused on the balance sheet, funds flow, coverage and liquidity. He focused on the reference to the funds flow on the slide, not the earnings. He does not recall a discussion about the earnings at the meeting.

Another statement on the slide was that in the Fourth Quarter 1999, Enron did six deals in eight days with LJM for a total of $125 million. Blake said that LJM2's purpose was to do deals quickly.

The slide also stated that LJM2 had a projected internal rate of return of 17.75%. Blake recalls hearing about the rate of return and was not told that LJM would not receive a higher internal rate of return.

Board of Director Meeting: May 2, 2000:

Blake recalls the Raptor structure was presented at the May 2, 2000 Board of Director meeting. Raptor was a hedging vehicle. LJM2 would receive a 30% return and anything above 30% Enron would receive. The oversight and governance was similar to the procedures put in place for the LJM transactions. The Board had concerns about consolidation because Fastow would be in the same situation as he was with the LJM transactions. Blake understood that there were other partners in the Raptor structure to avoid consolidation.

One of the slides shown to the Board meeting discussed the "risks and mitigants" of Raptor. One of the risks was if Enron's stock declined in value. At the time the stock was on a roll and the Board was confident, and in hindsight, probably overly confident, that it would continue.

There was a discussion about the credit in the Raptor structure and the fact that it was funded with Enron stock. Blake said the Board was concerned about the issue, but was comforted that there was an early termination agreement with LJM2.

Glisan, who reported to Fastow, made the presentation about Raptor and had signature authority on the deal. Blake thought that Glisan was in the position for administrative ease and coordinate the dialog between the business unit heads and LJM. The business units with the assets to be placed in Raptor negotiated with LJM, not Glisan.

Blake presumed that the economic risk to the hedges were transferred and Andersen would review the transactions to make sure they were proper.

On a slide entitled "Structural Highlights" there is a handwritten note, presumably by the Corporate Secretary, that the economic risk of the hedge was not transferred. He remembers a discussion about the transfer of the economic risk, but he thought that the risk had been transferred. Blake does not know how to transfer P&L volatility without transferring economic risk.

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Blake cannot recall any discussion about Enron purchasing a share settled put on its own stock for Raptor. Blake could also not recall any discussion that LJM would receive 30% or $41 million before the Raptor structure could transact.

Blake cannot recall any discussion about accounting scrutiny, Audit Committee or Finance Committee involvement in Raptor.

On page three of the Finance Committee Minutes from May 1, 2000, Blake was surprised when he reread the minutes that Fastow mentions that he "hired individuals to manage the investment vehicles" for LJM1 and LJM2. He did not say whom he hired and Blake did not know that they were Enron employees.

Blake does not recall any discussions about Raptor III or The New Power Company. He was not aware that the Raptors had a credit capacity problem in late 2000 and the First Quarter 2001. He believed that Rick Buy would bring credit capacity problems to the attention of the Board. Blake was not aware that there was a restructuring of Raptor III at the end of the First Quarter 2001, nor that the restructuring involved $800 million of Enron stock.

Blake did not know that the reference to $500 million of revenue in the Related Party Discussion in the 10-K 2000 was revenue from Raptor. He thought he heard something about the revenue at the time, but could not remember.

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MEMORANDUM

TO: File

FROM: Lisa Henriques

DATE: January 21, 2002

RE: Ronnie Chan Interview

On January 11, 2002, Chuck Davidow and Lisa Henriques of Wilmer, Cutler & Pickering ("WCP") and Jason Richards of Deloitte & Touche (an accounting firm retained by WCP), spoke with Ronnie Chan, member of the Board of Directors, via telephone at Gibbs & Bruns LLP offices in Houston, Texas to gather information from him in order to allow WCP to provide legal advice to the Special Committee of Enron's Board of Directors. Kathy Patrick, Robin Gibbs, Jean Frizzell, and Jeremy Doyle all of Gibbs & Bruns, and Neil Eggleston of Howrey Simon Arnold & White, LLP were present and represented Chan. Jeffrey Rudman and another lawyer of Hale and Dorr, LLP were present by phone and also represented Chan.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Chan statements. The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Chan has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

At the outset, Davidow explained that WCP represented the Special Committee appointed by the Board to investigate certain transactions between Enron and related parties, and we were speaking to him as part of that investigation. Davidow stated that, in our view, the conversation was privileged but it was the Special Committee's (or Enron's) privilege, and that the Special Committee or Enron could decide what to do with the privilege, not him. Davidow stated that Chan should anticipate that anything he told us would be conveyed to the Special Committee, and that the information could be communicated to others, such as the Board, others associated with Enron, and the Government.

Chan did not have copies of the Board or Committee minutes and presentations. He responded to questions purely from memory.

EC2 000000298

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #77e

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Education and Experience:

Chan received his MBA from The University of Southern California. After he received his degree, he was in the real estate business for a couple of years. He then worked for his family's business in Hong Kong, Hang Lung. Hang Lung is a publicly listed company that focuses on property development, property investment and hotels. Chan is also involved in investment activity for his family.

Chan has a working knowledge of accounting issues. He has taken accounting courses in business school and has become familiar with accounting issues through his work in a publicly listed company. Chan had a general understanding of what a special purpose vehicle (SPE) is from meetings at Enron. Chan said it was his understanding that the basic rules for SPEs are they must have 3% cash equity and independent management.

Chan became affiliated with Enron in February 1996 when Ken Lay asked him to become a member of the Board of Directors. Lay and Chan had been friends for some time and at the end of 1996, Chan accepted a position on the Board. He is also a member of the Finance and Audit and Compliance Committees.

Chewco:

Chan vaguely recalls the buyout of CalPERS interest in JEDI. JEDI was an entity that was created before he was a member of the Board. He does not recall any discussion of Chewco until recently. He does not recall Enron providing a loan to enable the buyout of CalPERS. If a presentation were given it would have been done by Causey, Fastow, Buy or Skilling. He does not recall if other Enron personnel were involved. He does not recall the details of JEDI II.

LJM:

LJM1 was presented to the Board in June of 1999. Chan was not present at the meeting. He heard that Enron had set up LJM as an off-balance sheet entity. Chan was aware that LJM's General Partner was Andy Fastow and it was interesting to him that Fastow could be the GP of an entity transacting with Enron. Chan believed that LJM had a number of outside investors such as pension funds and institutional investors. Chan knew that LJM1 pre-dated LJM2, but did not have a clear memory of the length of time between the two entities. Chan's understanding of the purpose of LJM1 and LJM2 was that Enron could monetize assets by putting them in LJM. Chan defined monetizing as selling an asset to an entity. Chan believed that LJM1 was created in order to hedge a particular asset, possibly Rhythms. Chan was aware that LJM was an SPE and does not recall discussions concerning whether Fastow could be the GP of LJM and Enron having control of Fastow and therefore LJM, which would lead to Enron consolidating LJM onto its balance sheets.

Chan believed that Fastow represented LJM and would only be able to negotiate for LJM. The division heads of the group that was selling the asset would be the person to negotiate on behalf of Enron with Fastow for LJM. Chan assumed that no one who reported to Fastow would negotiate on behalf of Enron. This policy would ensure that Enron was getting the best deal and all negotiations would be done on the executive level, so there would be no conflict of interest. After the deal was negotiated, Buy, Skilling and Causey would review the documents to make sure Enron received a fair deal. Chan expected the people reviewing the transactions and the people negotiating on behalf of Enron would ensure that the deal was fair and that it was proper.

Chan wanted to make sure that Fastow's compensation was not "out of whack" due to his involvement in LJM. Chan did not think it would be proper or look good to other employees if Fastow make a lot of money from LJM, especially since LJM was transacting with Enron. Chan asked a question in one of the meetings whether the assets sold to LJM would result in a reasonable return on the asset. Chan asked what Fastow's return would be and someone on the Board answered that it would not be different from what he already received. Chan expected that someone at Enron, either Skilling or Causey, would monitor Fastow's compensation.

Chan calculated in his head an estimation of Fastow's return from LJM. When LJM1 was first introduced it was a small entity with only about $16 million dollars in equity. Chan assumed that LJM would receive a fair rate of return of approximately 15-20%. Therefore, LJM would receive about $3-4 million return and a management fee. Chan believed the management fee was negligible because it is not the attractive part of the investment. Chan thought that Fastow would receive approximately 15-20% of the LJM return as a "carry," which would mean that Fastow would receive about $800,000 to $1 million dollars. Chan did not think this was an unreasonable rate of return because Fastow did make an investment that had risk. When LJM2 was created, which was much larger than LJM1, Chan did a similar calculation to the one he did for LJM1. He did not question the arrangement because he assumed that top management or the Compensation Committee would monitor Fastow's compensation.

Chan did not recall the Board discussing Fastow's compensation until October of 2001. During that meeting, someone, possibly Duncan, asked Fastow how much he made from his involvement with LJM and Fastow would not answer the question. Management then looked into his compensation and told the Board that he made $20 million. The Board was shocked and enraged because it thought that management was supervising Fastow's relationship with LJM.

Committee Oversight of LJM Transactions:

At every Audit Committee meeting Chan said that there was a discussion with Andersen about the transactions and it signs off that the procedures were followed. At the end of each year there was a more in depth review of all the transactions. Chan also said that Andersen always reviewed and monitored the related party transactions. Chan does not remember the specifics of the LJM transactions.

Usually, Causey would present a list of transactions to the Committee. The transactions were not discussed individually in detail. Chan relied on Causey to ensure that the deals were fair and that the legal and accounting aspects of the transactions were done properly according to the deal approval process, GAAP and other rules.

The Audit Committee reviewed the quarterly and annual report disclosures. The members of the Audit Committee would receive drafts of the reports in advance of the meeting.

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If someone had a question about the statement they could ask it at the meeting. During the meeting, the committee did not review the reports page by page. Andersen would report on the statement and direct the members' attention to areas Andersen thought were note worthy. The committee members always asked a lot of questions about the related party transaction section of the reports. The committee members asked Andersen whether anyone was breaking the rules and the members relied on Andersen to review and monitor the transactions. Usually David Duncan, Tom Bauer and Steve Goddard were the Andersen people who attended the meetings and answered the questions.

Chan was not aware of any other Enron employees, besides Fastow, who were investors in entities transacting with Enron. Chan was shocked when he learned in October 2001 that Ben Glisan invested in the entities because Glisan was the Treasurer and was making presentations to the Board.

Rhythms:

The Board discussed a hedge of Rhythms stock. Chan believes that at the time of the hedge, the structure was discussed with the Board, but Chan did not remember the details of the transaction. Chan could not remember what the value of the Rhythms hedge was nor did he recall any discussion of whether LJM1 had the credit capacity to pay the hedge. He also could not remember if there was a discussion about the Rhythms unwind.

When Enron restated the financial statements in November 2001 there was a detailed discussion of the Rhythms transaction. The Rhythms stock, which was restricted, was dropped into a subsidiary of LJM1. It was explained to the Board that when the stock was dropped into the subsidiary it should have been done at a discount from an accounting perspective because the stock was restricted and you could not monetize it. Enron needed to fix the accounting because the stock was not dropped in at a discount.

Chan did not have copies of the Board minutes and presentations, but was asked about the October 11, 1999, Board meeting. In the presentation there was a mention of the Rhythms Hedge being "in the money" $64 million. Chan could not recall hearing that Rhythms was "in the money." Chan never wondered or realized that LJM may have obligations greater than it could handle.

Cuiaba:

Chan remembers that Enron owned the power plant, but cannot recall what, if any, interest LJM had in the asset.

Raptor:

Chan had a difficult time separating what he learned about the Raptor structures in the last two months versus what he knew at the time of the transactions. There were discussions about Raptor in May 2000. Chan did not attend the Finance Committee meeting because he had a scheduling conflict with another Board that he is a member of. Chan attended the May 2000

Board meeting in person. He cannot recall the structuring details of the transactions, but had a general understanding that the purpose of the Raptor structure was to hedge transactions. He relied on management to handle the details of creating and maintaining the structures.

Chan recalls that The New Power Company ("TNPC") was discussed at the Board meetings, but cannot recall if it was in relation to Raptor. Chan could not remember how profitable TNPC was in 2001. He does not recall any discussion in early 2001 about potential problems in Raptor. The first time he heard there was a problem with Raptor was in the summer of 2001. Chan was not sure if he had heard about the unwind of the Raptors.

Andersen:

Chan was impressed with Andersen's relationship with Enron. Chan has worked for a public company and is familiar with the relationship between auditors and companies. Andersen had a uniquely close relationship with Enron because it had a permanent group of accountants working at Enron offices who had constant contact with Enron and a good working relationship. Andersen constantly was working with Enron to structure transactions and oversee the transactions. Andersen was involved and consulted with from the beginning of the transactions through the end. Andersen also would report to the Board and the Finance and Audit Committees about guidance Andersen sought from the Securities and Exchange Commission when it proposed certain transactions. Chan asked about the fees Enron paid Andersen. The fees were high, but Chan thought they were reasonable since Andersen had a constant presence at Enron and was involved in the business.

Chan's Sale of Enron Stock:

Chan sold 8,000 shares of Enron stock in July 1999. Chan sold the stock because he heard that other members of Enron management were selling shares and thought that he should too. At the time he sold the stock he did not think there were problems with Enron's business.

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MEMORANDUM

TO:	Enron File
FROM:	Lisa Henriques
DATE:	January 10, 2002
RE:	Paulo Ferraz Pereira

On January 10, 2002, Chuck Davidow and Lisa Henriques of Wilmer, Cutler & Pickering ("WCP") spoke with Paulo Ferraz Pereira, member of the Board of Directors of Enron Corp., via telephone from Gibbs & Bruns LLP office in Houston, Texas to gather information from him in order to allow WCP to provide legal advice to the Special Committee of Enron's Board of Directors. Kathy Patrick, Robin Gibbs, Jean Frizzell all of Gibbs & Bruns and Neil Eggleston of Howrey Simon Arnold & White, LLP were present and represented Ferraz.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Ferraz's statements. The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Ferraz has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

Education and Experience:

Ferraz was trained as an engineer and received a MBA from Harvard University. He spent one and a half years with a government entity venture capital group. He then started his own software management consulting firm. After a year and a half with the consulting group, he went to Group Bozano Bank. He was on the finance side and was in charge of personnel, accounting and finance. He then became Treasurer, and was responsible for international products and accounting. He later was appointed CEO. In January or March of 2000, the bank was sold. He currently advises a holding company, owned by a Brazilian billionaire, on investments and divestures.

In 1999, Enron was making substantial investments in South America and wanted someone from the region to sit on the Board of Directors. Enron hired the headhunting firm of Spencer Stuart to locate a potential member of the Board from South America. The firm found Ferraz and he met with Jeff Skilling, Ken Lay and others from Enron. In October 1999, he was elected to the board and attended his first meeting. Ferraz has served on both the Finance and Audit and Compliance Committees of Enron's board.

Ferraz is familiar with accounting because he has a business degree and he was in charge of accounting groups in prior positions. He has no special accounting training, but feels that he has an understanding of accounting sufficient to discuss accounting issues with auditors. He is familiar with American accounting practices, such as GAAP, because other firms he has been involved with in Brazil have done ADRs in the US and private equities that have required an understanding of GAAP.

Ferraz is familiar with the requirements for Special Purpose Entities ("SPE") because they are common in Brazil. Ferraz believes SPE's are used in Brazil for the same reasons that they are used in the United States, to conduct off-balance sheet transactions and create leverage. He was aware of the 3% equity rule and the divestiture of control requirements in order to create an SPE.

LJM Deals:

When Ferraz joined the Board in 1999, LJM1 was already in existence. In the first Board meeting that Ferraz attended in October of 1999, he became aware of LJM2. There was a discussion at the board meeting that LJM1 was a successful structure and that there was a need for LJM2. There was a lot of discussion about a possible conflict of interest involving Andy Fastow. There was a discussion at the Board meeting about the policies and procedures in place to protect Enron from the possible conflict. The policies included that Rick Buy and Rick Causey would verify the transactions and ensure that the deals were negotiated at arms-length. For larger deals, the Office of the Chairman would approve the deals. In addition, Arthur Andersen ("Andersen") would verify the deals and conduct the external audit. Vinson & Elkins would serve as outside counsel. Ferraz believed that these procedures and verifications from internal Enron employees and external firms would provide Enron protection from possible conflict problems. The Board members trusted the parties involved to ensure that Enron received the best deal. Once the deal was approved, no one ever reported back to the Board that the deal was executed according to the board resolutions. The Board assumed that Andersen and the other individuals and entities were involved in all stages of the transaction.

Ferraz remembers that presentations were given either at the October or December 1999 meeting about the differences between LJM1 and LJM2, but he was too junior on the Board to realize the differences and he can not recall the details. No one on the Board disagreed with the creation of LJM2. Ferraz does not remember a discussion about Fastow's compensation from his involvement in LJM. There was no discussion about other Enron employees working for LJM or any service agreements to pay employees compensation between Enron and LJM. Ferraz did not know Michael Kopper.

Usually, Skilling would give presentations about the transactions with LJM. Lay would not participate in the presentation, but seemed knowledgeable about the transactions because he could answer questions about LJM. Ferraz did not know if Lay actively participated in the oversight of the LJM, but did not think so, because it was not part of his job description. It was the Chief Operating Officer's responsibility to oversee the LJM transactions.

The Board, Audit Committee, and Finance Committee did not know how much Fastow received from his involvement in LJM. There was a discussion in a meeting that Ken Lay, Jeff Skilling and the Compensation Committee should look at Fastow's compensation from LJM. There was no other discussion until October 2001. Ferraz does not believe that anyone ever looked into Fastow's compensation from LJM because in October 2001, when they were told how much Fastow made, everyone was surprised.

DASHs and Committee Review:

Since Ferraz was a member of both the Finance and Audit committees it was difficult for him to identify what information was presented at each meeting. He also did not have the opportunity to review the minutes or presentations prior to our interview.

Prior to each meeting, the members of the Finance Committee are provided a packet of Deal Approval Sheets (DASHs) for their review. Ferraz could not recall if there were specific LJM DASHs. At the Finance Committee meeting Buy, Causey and others would discuss the deals. The deals were not individually discussed, but instead discussed in groups. Occasionally, a committee member would ask questions about a specific deal. Generally, the committee relied on management to ensure that all policies and procedures were done and all the proper signatures were obtained.

Causey also met with the Audit and Finance committees at the end of the calendar year or the beginning of the year. Causey was responsible for ensuring that the deals with LJM were accounted for properly. Andersen attended meetings that Causey would give his report and Andersen ensured the Board that Enron was accounting for its deals properly. Ferraz assumed that SPE's were included in Andersen's review. There were no discussions about the buybacks of the projects. He could not quantify how long Causey spoke at each committee.

The Committees reviewed the 10K and 10Q. Andersen would make comments about the statements and the Board would rely on Andersen. The Committees also reviewed the proxy material.

Cuiaba:

The Cuiaba deal was highly covered in the Brazilian press and Ferraz was familiar with Cuiaba prior to joining Enron. He recalls that there was a large thermal plant in Bolivia that had a pipeline built to Brazil where electricity was generated. This project was a joint venture with Shell. There were a number of problems with the project and it frequently requested money from the Board because the project was going over its budget. He does not recall any connection between the Cuiaba deal and LJM, nor does he recall discussions about LJM2 satisfying SPE rules to deconsolidate Cuiaba from the balance sheet.

Raptor:

Ferraz recalled that Raptor was created at the beginning of 2000. Ferraz participated by phone for the May 2000 meeting when Raptor was introduced. Ferraz originally planned to attend the Board meeting in person, but at last minute he was unable to attend. He did not have the presentations or agenda at the time of the meeting because there was not enough time to forward the materials to Brazil. He recalled that Raptor was a hedging vehicle but could not recall the vehicle in detail. Raptor II and the following Raptors were presented to the Board as follow-on hedging vehicles, but he does not recall the details. There were no reports of the individual transactions that were accomplished through the Raptor vehicles. Instead, all of the transactions were reviewed, at once, at the end of the year. Causey would usually make a presentation at the end of the year about the transactions, but he would not discuss the individual transactions. Andersen was present when the presentation was made and they would confirm that the transactions were done properly.

Ferraz recalled that The New Power Company ("TNPC") was a project that involved selling power to retail customers through the internet. He could not recall if this transaction was linked to Raptor. There was an IPO of TNPC in October 2000 and Enron was going to hedge the position. He would not be surprised if this was part of the Raptor deals.

Causey made a presentation in February 2001 about LJM and Raptor. Ferraz could not recall the discussion, but said that it is possible that the LJM transactions and the Raptor transactions were on the list of transactions to review. If they were, he would have relied on Causey's presentation and the fact that Andersen was present and confirmed the fact that they oversaw the transactions.

During the Finance Committee meetings there were general discussions about Raptor. During the presentation about the merchant transactions, a list of the best and worst performing entities was provided to the committee, but he did not recall a discussion about Raptor specifically. He does not recall Raptor experiencing any financial problems or Enron issuing shares to assist the Raptor structure.

The Restatement in Third Quarter 2001:

At the beginning of 2001, Andersen said that in August or September 2000, Enron booked part of a transaction improperly, even though at the time Andersen said that the booking of the asset was proper. Due to the mistake, they needed to make the restatement. Ferraz thought that the transaction involved the Raptor unwind, but was not positive.

Ferraz first heard of the restatement when Andersen called the Audit Committee a few days before the restatement. He thought that Causey, David Duncan of Andersen and Duncan's supervisor were in Houston and called all the members of the Audit Committee. Andersen told them that there was a mistake and there was going to be a restatement. The members of the committee were very angry and kept asking why the mistake was made and Andersen would not answer the question. The members of the Committee could not figure out how Andersen could have made a mistake of this magnitude.

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MEMORANDUM

TO: Enron Files

FROM: Reed M. Brodsky

DATE: January 14, 2002

RE: Interview of Dr. Wendy Gramm

On January 10, 2002, Bill McLucas, Chuck Davidow and Reed Brodsky of Wilmer, Cutler & Pickering ("WCP") and Ron Forster of Deloitte & Touche (an accounting firm retained by WCP), spoke with Dr. Wendy Gramm, a Director on the Audit and Compliance Committee of Enron's Board of Directors, at the offices of Gibbs & Bruns in Houston to gather information from her in order to allow WCP to provide legal advice to the Special Committee of Enron's Board of Directors. Robin Gibbs, Kathy Patrick, Jean Frizzell and Jeremy Doyle of Gibbs & Bruns and Neil Eggleston of Howrey Simon Arnold & White, LLP, were present and represented Dr. Jaedicke.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Dr. Gramm's statements.
The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Dr. Gramm has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

Davidow explained that we represented the Special Committee of Enron's Board of Directors, that the conversation was privileged and confidential, but that the Special Committee could waive the privilege, and that it was very likely that the Special Committee would pass along what information we learned to the SEC and others looking at the issues. Dr. Gramm indicated that she understood.

Background

Dr. Gramm grew up in Hawaii. She attended Wellesley College and obtained a Ph.D. degree in economics from Northwestern University. She started her career as a professor at Texas A&M University and then joined the research staff of the Institute for Defense Analyses. She became the Executive Director of the Presidential Task Force on Regulatory Relief, and then Director of the Federal Trade Commission's Bureau of Economics. Subsequently, she served as an Administrator for Information and Regulatory Affairs at the Office of Management and Budget, and later as Chairman of the U.S. Commodity Futures Trading Commission from 1988-1993. Today, she works for a non-profit organization affiliated with George Mason University and is the head of George Mason's regulatory studies program.

When Dr. Gramm left the CFTC, she spoke to Ken Lay at an international conference, and Lay invited her to sit on Enron's Board of Directors. In February 1993, Dr. Gramm joined Enron's Board. She has served on the Audit and Compliance Committee since she joined the Board and the Nominating and Corporate Governance Committee.

SPEs

Dr. Gramm learned about SPEs mostly from sitting on Enron's Board. She has a general understanding of the rules governing deconsolidation. Basically, in order to deconsolidate and keep assets off-balance sheet, a company must satisfy the control and 3% equity interest requirements. Dr. Gramm understood that LJM1 and LJM2 satisfied the control requirement to be deconsolidated.

Reliance on Accountants, Counsel, and Management

Enron's Board relied on a number of good professionals and the Company's management to make sure that the SPE rules were followed. The Board asked the professionals, such as Arthur Andersen and outside counsel, whether they analyzed these partnerships carefully.

When the related-party issue in LJM1 and LJM2 was raised, the Board asked Andersen and the lawyers whether the structures were legitimate. The Board believed that Andersen, the lawyers, and Enron management had looked closely at the issues. The Board relied on the Chief Accounting Officer (Rick Causey), the Chief Risk Officer (Rick Buy), Jeffrey Skilling, Andrew Fastow, Andersen's team, including David Duncan, and Vinson & Elkins' compliance review. At every Board and Audit Committee meeting, there were discussions with and presentations by Andersen and Vinson & Elkins regarding their respective reviews of the related-party transactions.

At the end of 1999, Vinson & Elkins completed an independent review of the Company's compliance program. At or around this time, LJM2 was being discussed. Dr. Gramm asked Vinson & Elkins what its compliance priorities were, and Vinson & Elkins responded that related party and special purpose entities were among its priorities.

Andersen informed the Audit Committee in 1999 that LJM transactions were among the issues that the accounting firm was spending a lot of time reviewing. Andersen presented a series of charts outlining the areas that required particular attention, and one of those areas involved structured vehicles.

June 28, 1999 Board Meeting

LJM1 was proposed at a Board meeting during which the accountants, lawyers, and management represented that the structure was analyzed carefully. Dr. Gramm did not recall the length of the presentation. LJM1 was used to hedge Enron's investment in RhythmsNet, because it was a volatile asset. Volatile assets are difficult to value. Dr. Gramm did not think that Fastow's compensation from LJM1 was discussed at the June 1999 Board meeting, and she would not have expected it to be discussed. Skilling, management, and Andersen were expected to monitor the transaction.

Dr. Gramm thought that the Board was informed about the structure of the RhythmsNet transaction after-the-fact through presentations. LJM1 had been capitalized with $16 million. Details, such as the amount of money Enron paid for the put on RhythmsNet stock, would not have been reviewed at that point by the Audit Committee. A detailed discussion of the structure of the transaction would have taken place at the Finance Committee meetings. In February 2000, the Audit Committee would review the year-end transactions.

The Board discussed the potential conflict of interest. Norm Blake was always talking about implementing "belts and suspenders" to ensure that the conflict was mitigated. Enron's Board works well together. This is not the kind of Board that talks just to put matters on the record. Board members do not give speeches for the sake of being on the record. When Board members speak, they put thought into what they say. The Board was concerned about the conflict of interest. Management, Andersen, and Vinson & Elkins gave the Board comfort that the potential conflict was analyzed and proper controls would be implemented. The transactions were not done with an outside party, because they could be done more efficiently and at less cost than the related party transactions. Dr. Gramm was impressed by the efficiency and reduction in costs. Outside parties would be willing to hedge large equity positions in non-public companies, such as RhythmsNet at the same price, but it would be more expensive for Enron. Enron's management had done a similar transaction with an outside party; Dr. Gramm could not recall the transaction or the outside party's name.

August 9, 1999 Audit Committee Meeting

In August 1999, the Audit Committee held a meeting during which Andersen said that it was looking at the formation of an SPE and working with Enron's management on accounting issues.

October 10-11, 1999 Board Meeting

In October 1999, LJM2 was proposed to the Board. At this point, there was a lot more discussion about implementing layers of controls. The Board decided that the Audit Committee would conduct an annual review of related party transactions. The Office of the Chairman, Andersen, and Vinson & Elkins would also review all transactions. The formula for LJM2's income was discussed at the October 1999 meeting or later.

February 7, 2000 Audit Committee Meeting

At the February 7, 2000 Audit Committee meeting, Causey presented the LJM1 and LJM2 transactions that took place in 1999. Causey said that the transactions were done on an arm's-length basis and that he was comfortable with them. Causey was supposed to be reviewing everything to make sure that the Board's instructions regarding the potential conflict of interest were followed, that the transactions were monitored, and that the accounting for the transactions was done properly. Enron wanted to move merchant assets to SPEs so that they could be off Enron's balance sheet and eventually sold to a third party. Causey did not report, and she did not know, that Enron bought back assets in the first quarter 2000 that Enron had previously sold to LJM2 in 1999.

Enron obtained a fairness opinion regarding LJM2 at the start. Although the Board did not expect fairness opinions for each transaction, it did expect all procedures to be in place and the accounting done correctly. Andersen told the Committee that these transactions were done appropriately, and Andersen was comfortable with the partnership structure. The Finance Committee was more concerned about the amounts involved, the capital structures, and the deal structures.

Enron's management and Andersen were fundamentally responsible for analyzing the economic substance of the transactions. The Board expected Causey with respect to the accounting issues and Buy with respect to the finance issues to make sure that Enron was not at a disadvantage in the transactions. The Board also expected Lay to be sufficiently familiar with the economic substance of these transactions. While the Board did not expect Lay to know all the details, the Board did not believe the issues involving these transactions were over Lay's head. The Board expected Skilling to know the details, and Skilling would often make the presentations about the related party transactions. Finally, the Board expected Andersen to analyze the transactions for economic substance.

May 2, 2000 Board Meeting

In May 2000, the Board looked at Project Raptor. This project would have come to the Board through the Finance Committee. At the Audit Committee in May 2000 and throughout the year, the related party and structured transactions were a high priority. Andersen made the point of getting out on the front-end of these transactions and issues.

Dr. Gramm's attention was directed to page 23 of the Project Raptor presentation. Dr. Gramm did not recall the comment "does not transfer economic risk but transfers P&L volatility" or any discussion about economic risk. Raptor was going to be part of LJM2. LJM1 and LJM2 were different, and LJM2's involvement in Raptor would not surprise her because it involved hedging transactions. Dr. Gramm speculated that "economic risk" could refer to management risk, but there could still be a risk of losing money. She did not recall any information about total return swaps involving Raptor or what assets were transferred into Raptor. She did not recall knowing at the time about LJM2's investment of $30 million in Raptor II and that Enron could not begin entering into transactions with Raptor II until LJM2 received $41 million. She also did not recall knowing or discussing at the time Enron's payment of $41 million to LJM2 to purchase a put on its own stock. Dr. Gramm speculated that Enron might purchase a put on its own stock if it were hedging some of its assets or capitalizing something.

February 12, 2001

Dr. Gramm's attention was directed to Causey's presentation before the February 12, 2001 Audit Committee and Causey's list of LJM1 and LJM2 transactions in 2000. Causey informed the Board that the proper procedures and controls were followed. Dr. Gramm did not recall Causey's discussion of the four Raptor vehicles. Causey never discussed how the vehicles were doing or whether they were underwater. She did not recall any discussion about Enron having to report an impairment amount of millions of dollars that would have an impact on earnings or how Enron could avoid taking a hit to earnings. She also did not remember any discussion of cross-collateralization at any Board meetings.

Third Quarter 2001

Dr. Gramm did not recall any discussion of unwinding the Raptors in the third quarter 2001.

Disclosure in Public Filings

The Audit Committee reviewed drafts of the 10-Q's with Andersen before they were filed. The Committee did not review the related-party transactions in detail. The Committee expected Andersen and legal counsel to be satisfied with disclosures in the public filings.

Dr. Gramm's attention was directed to note 8 to the Financial Statements of the 10-Q for the first quarter 2001 discussing related party transactions. She did not recall any discussion by the Audit Committee of the disclosure in the second paragraph of note 8. Dr. Gramm did not remember that the disclosure stated Enron delivered 12 million shares of restricted Enron stock and then entered into share settled costless collar arrangements on these same shares. She did not know why restricted stock was hedged.

Fastow's Compensation From LJM1 and LJM2

It was always represented that LJM2 would earn normal returns for a private equity fund in the private sector. LJM2 was not Fastow's job. Fastow's job was working for Enron as the Chief Financial Officer.

In October 1999, although transactions with LJM2 had not yet begun, there was a discussion of Fastow's compensation. Skilling was to oversee that LJM1 and LJM2 earned normal rates of return for private equity funds in the marketplace. LJM1 and LJM2 were considered separate entities, and some people questioned Enron's right to know what Fastow was making. In May 2000, Project Raptor was proposed. During the Board's discussions, Andersen represented that it was looking at Raptor and Enron's governance structure. In October 2000, one year after LJM2 was formed, there were discussions at the Board level about Fastow's compensation from LJM1 and LJM2. The Board discussed with Skilling how Skilling was going to review Fastow's economic interest in the LJM funds, and the Board expected Skilling to follow through and undertake this review. In addition, the Board decided that the Compensation Committee should look at Fastow's compensation from these partnerships. The Board decided to have Fastow's compensation reviewed only one year after LJM2 was formed.

Fastow's salary at Enron and the related party transactions would have been disclosed in the Proxy Statements. Dr. Gramm did not recall focusing on the disclosure of Fastow's compensation from LJM1 and LJM2. The Board relied on Andersen and Vinson & Elkins regarding what should and should not have been disclosed in the Company's public filings.

When Dr. Gramm eventually heard how much Fastow was making in late 2001 after Fastow had left the Company, she was surprised by the large amount of money he made. She was one of the people that pushed to find out what Fastow had earned.

Stock Sales

Dr. Gramm did not sell any Enron stock in 1999 or 2000. She sold some stock in 1998, because her husband, Senator Phil Gramm, was going to get involved in energy-related issues, and they wanted to avoid any appearance of a conflict of interest. Dr. Gramm received a variance from the Board requirement that a Director must own stock, and she liquidated her holdings of Enron stock.

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ATTORNEY WORK PRODUCT
Draft

MEMORANDUM

TO: Enron File

FROM: Lisa Henriques

DATE: January 10, 2002

RE: Lord John Wakeham

On January 10, 2002, Chuck Davidow and Lisa Henriques of Wilmer, Cutler & Pickering ("WCP") spoke with Jeremy Doyle of Gibbs & Bruns LLP in regards to a conversation he had with Lord John Wakeham. Kathy Patrick, Robin Gibbs, Jean Frizzell, all of Gibbs & Bruns and Neil Eggleston of Howrey Simon Arnold & White, LLP were all present.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Doyle's statements. The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Doyle has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

Doyle stated that his client, Wakeham, did not have the opportunity to review the minutes and presentations to the Board or any Committees of the Board. Wakeham remembers that when he first joined the Board of Directors he had a conversation with an individual who lead the audit. Wakeham was fascinated that Arthur Andersen ("Andersen") was able to finish the audits in a short period of time, especially since the transactions were so complex and there a number of transactions. The response to his comment was that Andersen had a good working relationship with Enron and Enron cooperated fully with Andersen.

EC2 000000793

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #77h

AA - Arthur Andersen
SEC Practice\08. SEC Staff Views
SEC Staff Speeches, Various
The Numbers Game, Arthur Levitt, Chairman

SPCH.T.1998.Levitt.

REMARKS BY CHAIRMAN ARTHUR LEVITT
SECURITIES AND EXCHANGE COMMISSION
THE "NUMBERS GAME"
NYU CENTER FOR LAW AND BUSINESS,
NEW YORK, N.Y.
SEPTEMBER 28, 1998

Thank you very much. Dean Daly, Dean Sexton and to everyone gathered this evening, thank you for welcoming me tonight. I am honored to be here on such an auspicious evening for both NYU and Bill Allen.

The creation of the Center for Law and Business recognizes an important truth: we cannot continue to view the worlds of business and law as parallel but separate universes. And NYU could not have selected a more qualified or thoughtful individual than Bill as its first director. His leadership of the Delaware Court of Chancery -- acknowledged as the nation's most influential arbiter of corporate law -- confirmed his reputation as a great thinker who effortlessly bridges the worlds of law and business. I've heard from friends on Wall Street that it's a far less stressful experience to hear Bill lecture in front of a classroom than from his former seat on the bench.

Seven months ago, I expressed concerns about selective disclosure. Through conference calls or embargoed press releases, analysts and institutional investors often hear about material news before it is made public. In the interval, there is a great deal of unusual trading. The practice had been going on for a long time. And, while everyone was aware of it, and most were extremely uncomfortable with it, few spoke out. As the investor's advocate, the SEC did and we will continue to do so.

Well, today, I'd like to talk to you about another widespread, but too little-challenged custom: earnings management. This process has evolved over the years into what can best be characterized as a game among market participants. A game that, if not addressed soon, will have adverse consequences for America's financial reporting system. A game that runs counter to the very principles behind our market's strength and success.

Increasingly, I have become concerned that the motivation to meet Wall Street earnings expectations may be overriding common sense business practices. Too many corporate managers, auditors, and analysts are participants in a game of nods and winks. In the zeal to satisfy consensus earnings estimates and project a smooth earnings path, wishful thinking may be winning the day over faithful representation.

As a result, I fear that we are witnessing an erosion in the quality of earnings, and therefore, the quality of financial reporting. Managing may be giving way to manipulation; Integrity may be losing out to illusion.

Many in corporate America are just as frustrated and concerned about this trend as we, at the SEC, are. They know how difficult it is to hold the line on good practices when their competitors operate in the gray area between legitimacy and outright fraud.

EC 000050988

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #78

A gray area where the accounting is being perverted; where managers are cutting corners; and, where earnings reports reflect the desires of management rather than the underlying financial performance of the company.

Tonight, I want to talk about why integrity in financial reporting is under stress and explore five of the more common accounting gimmicks we've been seeing. Finally, I will outline a framework for a financial community response to this situation.

This necessary response involves improving both our accounting and disclosure rules, as well as the oversight and function of outside auditors and board audit committees. I am also calling upon a broad spectrum of capital market participants, from corporate management to Wall Street analysts to investors, to stand together and re-energize the touchstone of our financial reporting system: transparency and comparability.

This is a financial community problem. It can't be solved by a government mandate: it demands a financial community response.

THE ROLE OF FINANCIAL REPORTING IN OUR ECONOMY

Today, America's capital markets are the envy of the world. Our efficiency, liquidity and resiliency stand second to none. Our position, no doubt, has benefited from the opportunity and potential of the global economy. At the same time, however, this increasing interconnectedness has made us more susceptible to economic and financial weakness half a world away.

The significance of transparent, timely and reliable financial statements and its importance to investor protection has never been more apparent. The current financial situations in Asia and Russia are stark examples of this new reality. These markets are learning a painful lesson taught many times before: investors panic as a result of unexpected or unquantifiable bad news.

If a company fails to provide meaningful disclosure to investors about where it has been, where it is and where it is going, a damaging pattern ensues. The bond between shareholders and the company is shaken; investors grow anxious; prices fluctuate for no discernible reasons; and the trust that is the bedrock of our capital markets is severely tested.

THE PRESSURE TO "MAKE YOUR NUMBERS"

While the problem of earnings management is not new, it has swelled in a market that is unforgiving of companies that miss their estimates. I recently read of one major U.S. company, that failed to meet its so-called "numbers" by one penny, and lost more than six percent of its stock value in one day.

I believe that almost everyone in the financial community shares responsibility for fostering a climate in which earnings management is on the rise and the quality of financial reporting is on the decline. Corporate management isn't operating in a vacuum. In fact, the different pressures and expectations placed by, and on, various participants in the financial community appear to be almost self-perpetuating.

This is the pattern earnings management creates: companies try to meet or beat Wall Street earnings projections in order to grow market capitalization and increase the value of stock options. Their ability to do this depends on achieving the earnings expectations of analysts. And analysts seek constant guidance from companies to frame those expectations. Auditors, who want to retain their clients, are under pressure not to stand in the way.

ACCOUNTING HOCUS-POCUS

Our accounting principles weren't meant to be a straitjacket. Accountants are wise enough to know they cannot anticipate every business structure, or every new and innovative transaction, so they develop principles that allow for flexibility to adapt to changing circumstances. That's why the highest standards of objectivity, integrity and judgment can't be the exception. They must be the rule.

Flexibility in accounting allows it to keep pace with business innovations. Abuses such as earnings management occur when people exploit this pliancy. Trickery is employed to obscure actual financial volatility. This, in turn, masks the true consequences of management's decisions. These practices aren't limited to smaller companies struggling to gain investor interest. It's also happening in companies whose products we know and admire.

So what are these illusions? Five of the more popular ones I want to discuss today are "big bath" restructuring charges, creative acquisition accounting, "cookie jar reserves," "immaterial" misapplications of accounting principles, and the premature recognition of revenue.

"Big Bath" Charges

Let me first deal with "Big Bath" restructuring charges.

Companies remain competitive by regularly assessing the efficiency and profitability of their operations. Problems arise, however, when we see large charges associated with companies restructuring. These charges help companies "clean up" their balance sheet – giving them a so-called "big bath."

Why are companies tempted to overstate these charges? When earnings take a major hit, the theory goes Wall Street will look beyond a one-time loss and focus only on future earnings.

And if these charges are conservatively estimated with a little extra cushioning, that so-called conservative estimate is miraculously reborn as income when estimates change or future earnings fall short.

When a company decides to restructure, management and employees, investors and creditors, customers and suppliers all want to understand the expected effects. We need, of course, to ensure that financial reporting provides this information. But this should not lead to flushing all the associated costs – and maybe a little extra – through the financial statements.

Creative Acquisition Accounting

Let me turn now to the second gimmick.

In recent years, whole industries have been remade through consolidations, acquisitions and spin-offs. Some acquirers, particularly those using stock as an acquisition currency, have used this environment as an opportunity to engage in another form of "creative" accounting. I call it "merger magic."

I am not talking tonight about the pooling versus purchase problem. Some companies have no choice but to use purchase accounting -- which can result in lower future earnings. But that's a result some companies are unwilling to tolerate.

So what do they do? They classify an ever-growing portion of the acquisition price as "in-process" Research and Development, so -- you guessed it -- the amount can be written off in a "one-time" charge -- removing any future earnings drag. Equally troubling is the creation of large liabilities for future operating expenses to protect future earnings -- all under the mask of an acquisition.

Miscellaneous "Cookie Jar Reserves"

A third illusion played by some companies is using unrealistic assumptions to estimate liabilities for such items as sales returns, loan losses or warranty costs. In doing so, they stash accruals in cookie jars during the good times and reach into them when needed in the bad times.

I'm reminded of one U.S. company who took a large one-time loss to earnings to reimburse franchisees for equipment. That equipment, however, which included literally the kitchen sink, had yet to be bought. And, at the same time, they announced that future earnings would grow an impressive 15 percent per year.

"Materiality"

Let me turn now to the fourth gimmick – the abuse of materiality – a word that captures the attention of both attorneys and accountants. Materiality is another way we build flexibility into financial reporting. Using the logic of diminishing returns, some items may be so insignificant that they are not worth measuring and reporting with exact precision.

But some companies misuse the concept of materiality. They intentionally record errors within a defined percentage ceiling. They then try to excuse that fib by arguing that the effect on the bottom line is too small to matter. If that's the case, why do they work so hard to create these errors? Maybe because the effect can matter, especially if it picks up that last penny of the consensus estimate. When either management or the outside auditors are questioned about these clear violations of GAAP, they answer sheepishly, "It doesn't matter. It's immaterial."

In markets where missing an earnings projection by a penny can result in a loss of millions of dollars in market capitalization, I have a hard time accepting that some of these so-called non-events simply don't matter.

Revenue Recognition

Lastly, companies try to boost earnings by manipulating the recognition of revenue. Think about a bottle of fine wine. You wouldn't pop the cork on that bottle before it was ready. But some companies are doing this with their revenue -- recognizing it before a sale is complete, before the product is delivered to a customer, or at a time when the customer still has options to terminate, void or delay the sale.

ACTION PLAN

Since U.S. capital market supremacy is based on the reliability and transparency of financial statements, this is a financial community problem that calls for timely financial community action.

Therefore, I am calling for immediate and coordinated action: technical rule changes by the regulators and standard setters to improve the transparency of financial statements; enhanced oversight of the financial reporting process by those entrusted as the shareholders' guardians; and nothing less than a fundamental cultural change on the part of corporate management as well as the whole financial community.

This action plan represents a cooperative public-private sector effort. It is essential that we work together to assure credibility and transparency. Our nine-point program calls for both regulators and the regulated to not only maintain, but increase public confidence which has made our markets the envy of the world. I believe this problem calls for immediate action that includes the following specific steps:

Improving the Accounting Framework

First, I have instructed the SEC staff to require well-detailed disclosures about the impact of changes in accounting assumptions. This should include a supplement to the financial statement showing beginning and ending balances as well as activity in between, including any adjustments. This will, I believe, enable the market to better understand the nature and effects of the restructuring liabilities and other loss accruals.

Second, we are challenging the profession, through the AICPA, to clarify the ground rules for auditing of purchased R&D. We also are requesting that they augment existing guidance on restructurings, large acquisition write-offs, and revenue recognition practices. It's time for the accounting profession to better qualify for auditors what's acceptable and what's not.

Third, I reject the notion that the concept of materiality can be used to excuse deliberate misstatements of performance. I know of one Fortune 500 company who had recorded a significant accounting error, and whose auditors told them so. But they still used a materiality ceiling of six percent earnings to justify the error. I have asked the SEC staff to focus on this problem and publish guidance that emphasizes the need to consider qualitative, not just quantitative factors of earnings. Materiality is not a bright line cutoff of three or five percent. It requires consideration of all relevant factors that could impact an investor's decision.

Fourth, SEC staff will immediately consider interpretive accounting guidance on the do's and don'ts of revenue recognition. The staff will also determine whether recently published standards for the software industry can be applied to other service companies.

Fifth, I am asking private sector standard setters to take action where current standards and guidance are inadequate. I encourage a prompt resolution of the FASB's projects, currently underway, that should bring greater clarity to the definition of a liability.

Sixth, the SEC's review and enforcement teams will reinforce these regulatory initiatives. We will formally target reviews of public companies that announce restructuring liability reserves, major write-offs or other practices that appear to manage earnings. Likewise, our enforcement team will continue to root out and aggressively act on abuses of the financial reporting process.

Improved Outside Auditing in the Financial Reporting Process

Seventh, I don't think it should surprise anyone here that recent headlines of accounting failures have led some people to question the thoroughness of audits. I need not remind auditors they are the public's watchdog in the financial reporting process. We rely on auditors to put something like the good housekeeping seal of approval on the information investors receive. The integrity of that information must take priority over a desire for cost efficiencies or competitive advantage in the audit process. High quality auditing requires well-trained, well-focused and well-supervised auditors.

As I look at some of the failures today, I can't help but wonder if the staff in the trenches of the profession have the training and supervision they need to ensure that audits are being done right. We cannot permit thorough audits to be sacrificed for re-engineered approaches that are efficient, but less effective. I have just proposed that the Public Oversight Board form a group of all the major constituencies to review the way audits are performed and assess the impact of recent trends on the public interest.

Strengthening the Audit Committee Process

And, finally, qualified, committed, independent and tough- minded audit committees represent the most reliable guardians of the public interest. Sadly, stories abound of audit committees whose members lack expertise in the basic principles of financial reporting as well as the mandate to ask probing questions. In fact, I've heard of one audit committee that convenes only twice a year before the regular board meeting for 15 minutes and whose duties are limited to a perfunctory presentation.

Compare that situation with the audit committee which meets twelve times a year before each board meeting; where every member has a financial background; where there are no personal ties to the chairman or the company; where they have their own advisers; where they ask tough questions of management and outside auditors; and where, ultimately, the investor interest is being served.

The SEC stands ready to take appropriate action if that interest is not protected. But, a private sector response that empowers audit committees and obviates the need for public sector dictates seems the wisest choice. I am pleased to announce that the financial community has agreed to accept this challenge.

As part eight of this comprehensive effort to address earnings management, the New York Stock Exchange and the National Association of Securities Dealers have agreed to sponsor a "blue- ribbon" panel to be headed by John Whitehead, former Deputy Secretary of State and retired senior partner of Goldman, Sachs, and Ira Millstein, a lawyer and noted corporate governance expert. Within the next 90 days, this distinguished group will develop a series of far-ranging recommendations intended to empower audit committees and function as the ultimate guardian of investor interests and corporate accountability. They are going to examine how we can get the right people to do the right things and ask the right questions.

Need for a Cultural Change

Finally, I'm challenging corporate management and Wall Street to re-examine our current environment. I believe we need to embrace nothing less than a cultural change. For corporate managers, remember, the integrity of the numbers in the financial reporting system is directly related to the long-term interests of a corporation. While the temptations are great, and the pressures strong, illusions in numbers are only that – ephemeral, and ultimately self-destructive.

To Wall Street, I say, look beyond the latest quarter. Punish those who rely on deception, rather than the practice of openness and transparency.

CONCLUSION

Some may conclude that this debate is nothing more than an argument over numbers and legalistic terms. I couldn't disagree more.

Numbers in the abstract are just that – numbers. But relying on the numbers in a financial report are livelihoods, interests and ultimately, stories: a single mother who works two jobs so she can save enough to give her kids a good education; a father who labored at the same company for his entire adult life and now just wants to enjoy time with his grandchildren; a young couple who dreams of starting their own business. These are the stories of American investors.

Our mandate and our obligations are clear. We must rededicate ourselves to a fundamental principle: markets exist through the grace of investors.

Today, American markets enjoy the confidence of the world. How many half-truths, and how much accounting sleight-of-hand, will it take to tarnish that faith?

As a former businessman, I experienced all kinds of markets, dealt with a variety of trends, fads, fears, and irrational exuberances. I learned that some habits die hard. But, more than anything else, I learned that progress doesn't happen overnight and it's not sustained through short cuts or obfuscation. It's induced, rather, by asking hard questions and accepting difficult answers.

For the sake of our markets; for the sake of a globalized economy which depends so much on the reliability of America's financial system; for the sake of investors; and for the sake of a larger commitment not only to each other, but to ourselves, I ask that we join together to reinforce the values that have guided our capital markets to unparalleled supremacy. Together, through vigilance and trust, I know, we can succeed.

Thank you.

REPORT AND RECOMMENDATIONS

OF THE

BLUE RIBBON COMMITTEE ON

IMPROVING THE EFFECTIVENESS OF

CORPORATE AUDIT COMMITTEES

U.S. Senate Permanent Subcommittee on Investigations

EXHIBIT #79b

Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees

JOHN C. WHITEHEAD
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Former Deputy Secretary of State and Retired Co-Chairman and Senior Partner
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National Association of Securities Dealers

COMMITTEE STAFF:
PAULA LOWITT, ESQ.
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A few Committee members had varying degrees of comfort with a few of the recommendations advanced in this Report. Nevertheless, the Report reflects a fair consensus of Committee members' viewpoints.

Additional copies of this Report can be obtained by contacting Murray Teitelbaum at the New York Stock Exchange at (212) 656-2017, or Andrew MacMillan at the National Association of Securities Dealers at (202) 728-8340. The Report may also be found on-line at www.nyse.com or www.nasd.com.

Overview and Recommendations

Recommendations for the performance of audit committees must be founded in the practices and attitudes of the entire board of directors. We, therefore, at the outset, urge boards of directors to understand and adopt the attitude of the modern board which recognizes that the board must perform active and independent oversight to be, as the law requires, a fiduciary for those who invest in the corporation. Board membership is no longer just a reward for "making it" in corporate America; being a director today requires the appropriate attitude and capabilities, and it demands time and attention.

The measure of the board, then, is not simply whether it fulfills its "legal" requirements but, more importantly, the board's attitude and how it puts into practice its awareness and understanding of its responsibilities. Is the board simply going through the motions, or has it demonstrated awareness of its important role by having some form of independent leadership that can act without relying only on management's initiative? Has the board established guidelines or operational procedures for its own functioning? Do the independent directors meet alone periodically to evaluate management and company performance and strategy? Does the board engage in individual director and full board evaluation? From self-generated measures such as these, one can infer that the board is aware, independent, professional and well-governing, or at least is endeavoring to be distinct from management. In essence, these signs show that a board is moving from being passive to active.

If a board is functioning properly, the audit committee can build on and relate to these very same board-wide principles. If the board is dysfunctional, the audit committee likely will not be much better. We cannot, however, suggest a single appropriate template for oversight by all audit committees. Just as "one size doesn't fit all" when it comes to board governance, "one size can't fit all" audit committees. Within broad parameters, each audit committee should evolve and develop its own guidelines suited to itself and its corporation.

A starting point for the development of audit committee guidelines is a recognition of the audit committee's position in the larger governance process as it relates to the oversight of financial reporting. Certainly, it is not the role of the audit committee to prepare financial statements or engage in the myriad of decisions relating to the preparation of those statements. The committee's job is clearly one of oversight and monitoring, and in carrying out this job it acts in reliance on senior financial management and the outside auditors. A proper and well-functioning system exists, therefore, when the three main groups responsible for financial reporting -- the full board including the audit committee, financial management including the internal auditors, and the outside auditors -- form a "three-legged stool" that supports responsible financial disclosure and active and participatory oversight. However, in the view of the Committee, the audit committee must be "first among equals" in this process, since the audit committee is an extension of the full board and hence the ultimate monitor of the process.

Turning from awareness and execution of responsibilities to another modern element of governance, we note that disclosure and transparency have become the first hallmark of good governance looked to by investors. The lack of disclosure and transparency no doubt contributed to the recent flight of capital from Asia. If a corporation is to be a viable attraction for capital, its board must ensure disclosure and transparency concerning the company's true financial performance as well as its governance practices. Accounting games may be short-term fixes, but they are not long-term bases for financial credibility.

Our recommendations, therefore, build on these two essentials: first, an audit committee with actual practices and overall performance that reflect the professionalism embodied by the full board of which it is a part, and second, a legal, regulatory, and self-regulatory framework that emphasizes disclosure and transparency and accountability.

The Committee wishes to stress that while the recommendations in this Report appear separately, they together form a mosaic to enhance financial reporting and oversight ot that process; in this light, the Committee views the recommendations as an integrated set of objectives that must be adopted in its entirety in order to accomplish the intended results. The need for such an integrated approach is of even greater importance given the fact that implementation will require action by a number of entities including the Securities and Exchange Commission (SEC), the securities markets through the self-regulatory organizations (SROs), the accounting profession, and, of course, boards and audit committees.

Notably, while several of the recommendations that apply to public companies contemplate an exemption for smaller entities due to the burdens involved, the Committee urges all companies regardless of size to make a good faith attempt to follow these recommendations. Similarly, while a number of the recommendations propose amendments to the listing standards applied by the NYSE and the NASD, the Committee hopes that these proposed amendments to listing standards be considered by any market that is a primary venue for U.S. equities.

It is with these perspectives the Committee advances the recommendations outlined in summary form below. The section of this Report, entitled "The Audit Committee as Catalyst for Effective Financial Reporting," more fully describes the rationale and intentions underlying each of these recommendations.

Summary

The first two recommendations are aimed at strengthening the independence of the audit committee:

Recommendation 1

The Committee recommends that both the New York Stock Exchange (NYSE) and the National Association of Securities Dealers (NASD) adopt the following definition of independence for purposes of service on the audit committee for listed companies with a market capitalization above $200 million (or a more appropriate measure for identifying smaller-sized companies as determined jointly by the NYSE and the NASD):

Members of the audit committee shall be considered independent if they have no relationship to the corporation that may interfere with the exercise of their independence from management and the corporation. Examples of such relationships include:

- a director being employed by the corporation or any of its affiliates for the current year or any of the past five years;
- a director accepting any compensation from the corporation or any of its affiliates other than compensation for board service or benefits under a tax-qualified retirement plan;
- a director being a member of the immediate family of an individual who is, or has been in any of the past five years, employed by the corporation or any of its affiliates as an executive officer;
- a director being a partner in, or a controlling shareholder or an executive officer of, any for-profit business organization

to which the corporation made, or from which the corporation received, payments that are or have been significant* to the corporation or business organization in any of the past five years;

- a director being employed as an executive of another company where any of the corporation's executives serves on that company's compensation committee.

A director who has one or more of these relationships may be appointed to the audit committee, if the board, under exceptional and limited circumstances, determines that membership on the committee by the individual is required by the best interests of the corporation and its shareholders, and the board discloses, in the next annual proxy statement subsequent to such determination, the nature of the relationship and the reasons for that determination.

Recommendation 2

The Committee recommends that in addition to adopting and complying with the definition of independence set forth above for purposes of service on the audit committee, the NYSE and the NASD require that listed companies with a market capitalization above $200 million (or a more appropriate measure for identifying smaller-sized companies as determined jointly by the NYSE and the NASD) have an audit committee comprised solely of independent directors.

The Committee recommends that the NYSE and the NASD maintain their respective current audit committee independence requirements as well as their respective definitions of

* The Committee views the term "significant" in the spirit of Section 1.34(a)(4) of the American Law Institute Principles of Corporate Governance and the accompanying commentary to that section.

independence for listed companies with a market capitalization of $200 million or below (or a more appropriate measure for identifying smaller-sized companies as determined jointly by the NYSE and the NASD).

Our second set of recommendations is aimed at making the audit committee more effective:

Recommendation 3

The Committee recommends that the NYSE and the NASD require listed companies with a market capitalization above $200 million (or a more appropriate measure for identifying smaller-sized companies as determined jointly by the NYSE and the NASD) to have an audit committee comprised of a minimum of three directors, each of whom is financially literate (as described in the section of this report entitled "Financial Literacy") or becomes financially literate within a reasonable period of time after his or her appointment to the audit committee, and further that at least one member of the audit committee have accounting or related financial management expertise.

The Committee recommends that the NYSE and the NASD maintain their respective current audit committee size and membership requirements for companies with a market capitalization of $200 million or below (or a more appropriate measure for identifying smaller-sized companies as determined jointly by the NYSE and the NASD).

Recommendation 4

The Committee recommends that the NYSE and the NASD require the audit committee of each listed company to (i) adopt a formal written charter that is approved by the full board of directors and that specifies the scope of the committee's responsibilities, and how it carries out those responsibilities, including structure, processes, and membership requirements, and (ii) review and reassess the adequacy of the audit committee charter on an annual basis.

Recommendation 5

The Committee recommends that the Securities and Exchange Commission (SEC) promulgate rules that require the audit committee for each reporting company to disclose in the company's proxy statement for its annual meeting of shareholders whether the audit committee has adopted a formal written charter, and, if so, whether the audit committee satisfied its responsibilities during the prior year in compliance with its charter, which charter shall be disclosed at least triennially in the annual report to shareholders or proxy statement and in the next annual report to shareholders or proxy statement after any significant amendment to that charter.

The Committee further recommends that the SEC adopt a "safe harbor" applicable to all disclosure referenced in this Recommendation 5.

Our final group of recommendations addresses mechanisms for accountability among the audit committee, the outside auditors, and management:

Recommendation 6

The Committee recommends that the listing rules for both the NYSE and the NASD require that the audit committee charter for every listed company specify that the outside auditor is ultimately accountable to the board of directors and the audit committee, as representatives of shareholders, and that these shareholder representatives have the ultimate authority and responsibility to select, evaluate, and, where appropriate, replace the outside auditor (or to nominate the outside auditor to be proposed for shareholder approval in any proxy statement).

Recommendation 7

The Committee recommends that the listing rules for both the NYSE and the NASD require that the audit committee charter for every listed company specify that the audit committee is responsible for ensuring its receipt from the outside auditors of a formal written statement delineating all relationships between the auditor and the company, consistent with Independence Standards Board Standard 1, and that the audit committee is also responsible for actively engaging in a dialogue with the auditor with respect to any disclosed relationships or services that may impact the objectivity and independence of the auditor and for taking, or recommending that the full board take, appropriate action to ensure the independence of the outside auditor.

Recommendation 8

The Committee recommends that Generally Accepted Auditing Standards (GAAS) require that a company's outside auditor discuss with the audit committee the auditor's judgments about the quality, not just the acceptability, of the company's accounting principles as applied in its financial reporting; the discussion should include such issues as the clarity of the company's financial disclosures and degree of aggressiveness or conservatism of the company's accounting principles and underlying estimates and other significant decisions made by management in preparing the financial disclosure and reviewed by the outside auditors. This requirement should be written in a way to encourage open, frank discussion and to avoid boilerplate.

Recommendation 9

The Committee recommends that the SEC require all reporting companies to include a letter from the audit committee in the company's annual report to shareholders and Form 10-K Annual Report disclosing whether or not, with respect to the prior fiscal year: (i) management has reviewed the audited financial statements with the audit committee, including a discussion of the quality of the accounting principles as applied and significant judgments affecting the company's financial statements; (ii) the outside auditors have discussed with the audit committee the outside auditors' judgments of the quality of those principles as applied and judgments referenced in (i) above under the circumstances; (iii) the members of the audit committee have discussed among themselves, without management or the outside auditors present, the information disclosed to the audit committee described in (i) and (ii) above; and (iv) the audit committee, in reliance on the review and discussions conducted with management and the outside auditors pursuant to (i) and (ii) above, believes that the company's financial statements are fairly presented in conformity with Generally Accepted Accounting Principles (GAAP) in all material respects.

The Committee further recommends that the SEC adopt a "safe harbor" applicable to any disclosure referenced in this Recommendation 9.

Recommendation 10

The Committee recommends that the SEC require that a reporting company's outside auditor conduct a SAS 71 Interim Financial Review prior to the company's filing of its Form 10-Q.

The Committee further recommends that SAS 71 be amended to require that a reporting company's outside auditor discuss with the audit committee, or at least its chairman, and a representative of financial management, in person, or by telephone conference call, the matters described in AU Section 380, Communications With the Audit Committee, prior to the filing of the Form 10-Q (and preferably prior to any public announcement of financial results), including significant adjustments, management judgments and accounting estimates, significant new accounting policies, and disagreements with management.

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June 21, 2002

BY HAND

Mary Robertson
Chief Clerk
U.S. Senate Permanent Subcommittee on Investigation

Dear Ms. Robertson:

Enclosed please find a copy of the May 7, 2002 Transcript of Proceedings before the Senate Permanent Subcommittee on Investigations of the Governmental Affairs Committee. This copy contains the edits and clarifications of Messrs. Blake, Duncan, and Winokur, and Drs. Jaedicke and LeMaistre.

Pages 109-116 of the transcript contain questions from Senator Fitzgerald regarding each witness's Enron stock shares and options. At the time they testified, each witness approximated the amount of shares and options he owned, related cost basis information, etc. The witnesses have clarified this testimony and now provide more precise information in response to Senator Levin's Supplemental Questions for the Record, which ask for similar information.

Dr. Jaedicke seeks to clarify his testimony that appears on pages 143-44 of the transcript. The exchange between Dr. Jaedicke and Senator Levin on those pages relates to Senator Levin's question of whether there was any limit on how much Enron stock, preferred or otherwise, that had to be sold, if necessary, to pay back the bondholders associated with the Whitewing transactions. Dr. Jaedicke misunderstood Senator Levin's question and now clarifies his testimony as follows:

> When we approved the restructuring of Whitewing transactions, the minutes reflect that a specific number of preferred and common shares were set aside for credit support in these transactions. The number of shares dedicated to this credit support could not exceed that limit without Board approval.

Mr. Winokur seeks to clarify his testimony on page 141, where Senator Levin asks:

> Now, were the bondholders—did they have a guarantee that if the assets did not generate cash to pay them back on their bonds, that Enron shares would be used to pay them back?

Mr. Winokur clarifies his response as follows:

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EXHIBIT #80

HOWREY SIMON ARNOLD & WHITE
HOWREY ATTORNEYS AT LAW

Mary Robertson
Chief Clerk
June 21, 2002
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I believe that, based upon the resolution authorizing this transaction, there was contingent credit support provided in the form of convertible preferred shares. This was not an open-ended guarantee.

Mr. Winokur also clarifies his response to the exchange between Senator Levin and him that appears on pages 188-190, as follows:

On pages 188-190, I was confused by Senator Levin's questions concerning the assets that had been contributed to the Raptor vehicles. I correctly stated that Enron was contributing to the Raptor structures unrealized gains on forward contracts on Enron stock. I was confused, however, by Senator Levin's reference to the use of Enron stock as "collateral" for these hedges. As is disclosed in Enron's Form 10Ks, and as was explained to the Board when it approved these transactions, the Raptor structures involved the sale of certain shares of Enron stock to the vehicles in exchange for a note receivable from each Raptor entity.

More generally, the Board was advised that each of these structures involved a fixed number of Enron shares that would be at risk on the Enron Derivative and on the Securities Agreements. (*See* Board Minutes of May 2, 2000 at pg. 6 ("the maximum number of shares of Company Common Stock (i) subject to the ENE Derivative shall not exceed 7.5 million shares and the ENE Derivative shall provide that any payment required to be made by Harrier or the company thereunder may be made in either cash or shares of the Company's Common Stock, at the Company's sole option, and (ii) issuable under the Securities Agreement shall not exceed 4.2 million shares."); Executive Committee Minutes of June 22, 2000 ("the maximum number of shares of Company Common Stock (a) subject to the Enron Derivative shall not exceed 8.0 million shares, and (b) issuable under the Securities Agreement shall not exceed 8.0 million shares."); and Board Minutes of August 7, 2000 ("the maximum number of shares of Company Common Stock (a) subject to each ENE Derivative shall not exceed 8.0 million shares, and (b) issuable under each Securities Agreement shall not exceed 8.0 million shares; and the maximum number of shares of Company Common Stock (a) subject to all ENE Derivatives contemplated...shall not exceed 16 million shares and issuable under all Securities Agreements contemplated...shall not exceed 16 million shares."). As it pertains to the transactions we knew as Raptors I, II and III, the existence of these derivatives was disclosed in Enron's Form 10K at note 11, relating to Common Stock, and at note 16, concerning the Related Party transactions.

Senator Carl Levin
Supplemental Questions For The Record
Permanent Subcommittee on Investigations' Hearing
The Role of the Board of Directors In Enron's Collapse
May 7, 2002

For Each Board Member Who Testified:

1. In accordance with the Subcommittee's previous requests and Senator Fitzgerald's question from the hearing, please provide the Subcommittee with the following information:

   a. How many Enron options do you currently hold?

   b. How many Enron shares do you currently own?

   c. How many of these shares were purchased outright and how many were the result of options exercised?

   d. The dates, number of shares and dollar value associated with any Enron share sale since January 1, 1997.

   Response to Question 1:

   See Exhibit A (attached).

2. A *Wall Street Journal* article from May 15, 2002, reports that a professional in Arthur Andersen's Professional Standards Group questioned, "Why would any director in his or her right mind ever approve such a scheme [an arrangement whereby a company's Chief Financial Officer manages a side fund]?" The same article reports that David Duncan of Arthur Andersen reported to Andrew Fastow that Andersen would sign off on the [LJM] transaction only if Mr. Fastow received CEO and Board approval. Were you aware of any such requirements by Andersen? On whose initiative did the code of conduct waiver come to the Board of Directors for approval?

   Joint Response of Panel Witnesses to Question 2:

   Were you aware of any such requirements by Andersen?

   No. This was not disclosed to the Board.

   On whose initiative did the code of conduct waiver come to the Board of Directors for approval?

   As is reflected in the minutes of the Board meeting in June of 1999, and in the minutes of the Finance Committee and the Board in October of 1999, the initiative for permitting Mr. Fastow to serve as a general partner of the LJM funds came to us through the recommendation of the Office of the Chairman. The minutes of each Board meeting reflect that the Board was asked to "adopt[] and ratif[y] the determination of the Office of the Chairman pursuant to the Company's Conduct of Business Affairs/Investments and Outside Business Interests of Officers and Employees that participation of [Andrew S. Fastow] as the managing partner/manager of the Partnership will not adversely affect the interests of the Company." (6/28/99 Board Meeting Minutes, p. 7; 10/11/99 Board Meeting Minutes, p. 18).

3. Enron's law firm, Vinson & Elkins, reviewed the LJM2 Private Placement Memorandum and was also responsible for reviewing Enron's code of conduct. The Private Placement Memorandum named three Enron employees who had a role in LJM2. The participation of two of the three, Michael Kopper and Ben Glisan, was in direct conflict with Enron's Code of Conduct since they had not been granted a waiver. We have identified no evidence to suggest that Vinson & Elkins brought this information to the attention of the Board of Directors. What action did the Board take upon learning that Vinson & Elkins failed to inform the Board on this matter?

   Joint Response of Panel Witnesses to Question 3:

   We believe the subcommittee is correct that Vinson & Elkins did not bring to the attention of the Board the involvement of Michael Kopper or Ben Glisan in the LJM partnerships. The Board learned of this through the subsequent investigation conducted by the Powers Committee. The Board was informed by company counsel that, as part of the bankruptcy process, claims were likely to be brought against a variety of parties, including professional advisers such as Vinson & Elkins. It is our understanding that the Examiner appointed by the Bankruptcy Court is presently considering, among other things, whether claims should be pursued against Vinson & Elkins on behalf of the debtors' estates.

4. The majority of Board Directors indicated they read Enron's financial statements. The related party disclosure from Enron's 1999 10K filing reported that "an officer of Enron has invested in the limited partner of JEDI and from time to time acts as agent on behalf of the limited partner's management." We now know that officer was Michael Kopper. You told our staffs that the Board was not aware of Michael Kopper's ownership interest in Chewco.

   a. Did you review the 1999 10K filing related party disclosure?

      Joint Response of Panel Witnesses to Question 4.a.:

      Yes.

   b. Did you know the identity of the Enron officer associated with JEDI?

      Joint Response of Panel Witnesses to Question 4.b.:

      No.

c. Did you inquire as to the identity of the Enron officer associated with JEDI? If so, whom did you ask and what were you told? If no, why not?

Joint Response of Panel Witnesses to Question 4.c.:

The existence of this disclosure was not called to the attention of any Board member during any committee or Board meeting. None of the directors, moreover, noticed this sentence when they read the 1999 Form 10K, and hence none of the Board members inquired as to the identity of the Enron officer associated with JEDI.

5. Given your experience at Enron with the Raptor structures, would you approve a similar structure (using shares or derivatives linked to shares of the parent company to support a vehicle whose main purpose was to hedge investments held by the parent) again at another company?

Joint Response of Panel Witnesses to Question 5:

It depends upon the particular facts and circumstances, and whether, upon review, we believed that the structure and transactions were in the best interests of the company and its shareholders.

6. Prior to October 2001, were you aware of the "costless collars" placed on the Raptor structures in October 2000? Were you aware of components of either the initial or modified Raptor structures that would require additional capital from Enron, either in the form of Enron shares or other sources?

Joint Response of Panel Witnesses to Question 6:

The Forms 10K for Enron for the year 2000 recited that "in late 2000, Enron entered into share-settled collar arrangements" with the Raptors "on 15.4 million shares of Enron common stock. Such arrangements will be accounted for as equity transactions when settled." (*See* 2000 Form 10K Related Party Disclosure at n. 16).

When the Raptor structure was approved by the Board, the structure described to the Board did not involve any obligation to deliver contingent equity (such as a top up) in the event the price of Enron stock declined to a particular level. Rather, the Board was advised that, in the event of a substantial decline in the price of Enron stock, the Raptor transactions would be unwound. (*See e.g.* May, 2000 Finance Committee Minutes, p. 3, and presentation materials (noting that in the event of a substantial decline in the price of Enron stock, Enron would negotiate an early termination with LJM2)).

As the Powers Report indicates, the Board was not informed of the "recapitalization" of the Raptor structures in the first quarter of 2001. The Board members did not know, therefore, whether the "modified Raptor structures" involved a commitment of additional capital from Enron in the form of Enron shares or other sources.

Senator Carl Levin
Supplemental Questions For The Record
Permanent Subcommittee on Investigations' Hearing
The Role of The Board of Directors In Enron's Collapse
May 7, 2002

Questions for Mr. Winokur:

1. As recorded in the minutes from the September 17, 1999, Special Meeting of the Board of Directors, "the primary purpose of the (Condor/Whitewing) transaction had been to convert debt to equity." As part of this transaction, you testified that Citibank was paid $570 million in 1999 on its 1997 investment of $500 million. You attributed the payment to Citibank of $70 million over the initial investment to appreciation in the value of the preferred stock in Whitewing. (Note: Enron shares appreciated in value at a cumulative average growth rate of approximately 48% from December 1997 through December 1999, and each preferred share is convertible into 200 shares of Enron common stock. The $70 million payment reflects an annual rate of return of 6.77%, which would be consistent with Enron's cost of borrowing.)

   a. Please quantify the relationship between the appreciation in value of the preferred stock and the $70 million appreciation in the payment to Citibank.

Response to Question 1.a.:

I have not seen the underlying agreement between Citibank and Enron, so I cannot quantify precisely the relationship between the accrued dividend on the preferred stock and the payment to Citibank.

The minutes of the Board meeting on February 1, 1999 reflect an initial discussion of Citibank's exit from the Whitewing transaction, with a further elaboration on that transaction at a Board meeting on September 17, 1999. The minutes of the February 1, 1999 indicate that the purchase of Citibank/Nighthawk's interest in Whitewing was to be effected pursuant to "the Purchase Option Agreement dated as of December 29, 1997 among Enron, Nighthawk and the other parties thereto."

The minutes of the September 17, 1999 meeting indicate that the proceeds of the transaction we approved were to be used, in part, "to restructure the outstanding equity of Whitewing and provide funds for the repayment of a previous structured financing (approximately $570 million)." I believe that payment included some calculated return over the life of Citibank's investment, but I do not know precisely how that was calculated.

b. When was Citibank's return and exit from Condor/Whitewing transaction negotiated?

Response to Question 1.b.:

The sale of Citibank's investment was first discussed with the Board at a meeting on February 1, 1999. The transaction was discussed again at a meeting on September 17, 1999. At the February meeting, Mr. McMahon advised the Board that the purchase of Citibank's interest was being made "pursuant to the Purchase Option Agreement dated as of December 29, 1997." I do not have a copy of this agreement and so do not know what the return was to Citibank on the transaction.

2. The hearing record reflects that Osprey bondholders had a guarantee that if Whitewing-held assets did not generate enough cash to pay investors the value of their bonds, Enron shares would be used to pay them back. You testified that there were 20 million Enron shares reserved for issuance under the Whitewing/Osprey share settlement agreement.

   a. What was your understanding of what would happen in the event these 20 million shares were not enough to meet both the preferred convertibility requirements (conversion of preferred shares into common shares) and obligations to Osprey bondholders (in the event the Whitewing-held assets did not generate sufficient proceeds)?

Response to Question 2.a.:

Based upon the relevant minutes and resolutions, my understanding is that the Osprey notes were to be repaid with proceeds generated from the assets held by Whitewing. If those assets did not generate sufficient funds for repayment, there would be a payment default on the Osprey notes. The documents available to me do not specify the precise remedies available to the noteholders in the event of a default. Based upon the relevant minutes, my understanding, however, is that the noteholders' remedies were limited to the 20,000,000 shares of common stock reserved for this transaction. In addition, the Board was advised that the liquidation preference for the preferred shares authorized for this transaction would "not exceed $1.0 billion."

   b. Was there an explicit limit on the number of shares that Enron would have to issue to comply with the share settlement agreement?

Response to Question 2.b.:

I have not seen the agreements that effected this transaction, so I do not know whether the terms were altered following the approval of this transaction by the Board.

The September 17, 1999 Board resolution authorizing this transaction states that "subject to the Board conditions, effective immediately upon issuance of the

Preferred Shares, there will be reserved 20 million additional shares of common stock of the Company and 100,000 Preferred Shares of the Company for issuance under the Share Settlement Agreement."

c. How was this number of shares reflected in the number of fully diluted shares outstanding?

Response to Question 2.c.:

The existence of these preferred shares, and their conversion ratio, is disclosed in Note 10 of Enron's Form 10K. That note, pertaining to Preferred Stock, states that the potential Whitewing exposure is 250,000 shares of Mandatorily Convertible Junior Preferred Stock (Series B), each of which is mandatorily convertible to 200 shares of Enron stock at a strike price of $48.55 per share. Upon conversion of the shares, the mandatory preferred dividend of 6.5% would be extinguished. Note 11, regarding Common Stock, states that "the Series A Preferred Stock and the Series B Preferred Stock were not included in the calculation of diluted earnings per share because conversion of these shares would be antidilutive."

This is consistent with what the Board was told at its February 1, 1999 Board meeting. The minutes of that meeting reflect that Mr. McMahon advised the Board that this transaction "would increase the number of shares of common stock outstanding but would be non-dilutive."

3. You testified that the additional shares potentially required by the Raptor transactions were included in Enron's fully diluted shares outstanding. There is evidence to suggest it would have been impossible to include the exact number of shares at risk in the Raptor transactions in Enron's fully diluted shares outstanding.

a. Was it your understanding that the number of shares at risk in the Raptor transactions was limited? Were you told that there was a limit to the number of shares Enron could be forced to issue or was that something you assumed? If you were told, who told you?

Response to Question 3.a.

Each of the Raptor structures we approved involved a specified number of Enron shares that would be at risk on the Enron Derivative and on the Securities Agreements. (*See* Board Minutes of May 2, 2000 at pg. 6 ("the maximum number of shares of Company Common Stock (i) subject to the ENE Derivative shall not exceed 7.5 million shares and the ENE Derivative shall provide that any payment required to be made by Harrier or the company thereunder may be made in either cash or shares of the Company's Common Stock, at the Company's sole option, and (ii) issuable under the Securities Agreement shall not exceed 4.2 million shares."); Executive Committee Minutes of June 22, 2000 ("the maximum number of shares of Company Common Stock (a) subject to the Enron Derivative shall not exceed 8.0 million shares, and (b) issuable under the Securities Agreement shall not exceed 8.0 million shares."); and Board Minutes of August 7, 2000 ("the maximum number of shares of Company Common Stock (a) subject to each ENE Derivative shall not exceed 8.0 million shares, and (b) issuable under each Securities Agreement shall not exceed 8.0 million shares; and the maximum number of shares of Company Common Stock (a) subject to all ENE Derivatives contemplated...shall not exceed 16 million shares and issuable under all Securities Agreements contemplated...shall not exceed 16 million shares.")).

The minutes reflect that the initial presentation on Project Raptor, including the relevant terms of the transactions, was made to the Finance Committee on May 2, 2000 by Messrs. Glisan and Causey, who were introduced by Mr. Fastow. The June 22, 2000 presentation to the Executive Committee concerning Raptor II was made by Mr. Fastow. The August 7, 2000 presentation to the Board concerning Raptor III was made by Mr. Skilling.

b. Was this fully diluted number impacted by changes in Enron's share price? Did a drop in Enron's share price result in an increase in the fully diluted number of shares outstanding?

Response to Question 3.b.:

Note 11 to Enron's Form 10K described how Enron calculated earnings per share. This note also specifically addressed the derivative instruments that were the subject of the Raptor transactions. In that disclosure, it states that "At December 30, 2000, Enron had derivative instruments (excluding amounts disclosed in Note 10) on 54.8 million shares of Enron common stock, of which approximately 12 million shares are with JEDI and 22.5 million shares are with related parties (see Note 16), at an average price of $67.92 per share on which Enron was a fixed price payor. Shares potentially deliverable to counterparties under the contracts are assumed to be outstanding in calculating diluted earnings per share unless they are anti-dilutive."

I do not know to what evidence you refer when you state that "there is evidence to suggest it would have been impossible to include the exact number of shares at risk in the Raptor transactions in Enron's fully diluted shares outstanding." Based upon what was presented to me in the Board and Committee meetings, I understood that the shares subject to the derivatives in the Raptor transactions was a known, fixed maximum amount of shares. These shares, moreover, were "assumed to be outstanding in calculating earnings per share unless they were anti-dilutive." (*See* Note 11.). Since the maximum number of shares subject to the derivatives was both known and fixed, and since the Form 10K disclosed the total number of Enron shares subject to all of derivative contracts, *see id.*, I do not believe it "would have been impossible to include the exact number of shares at risk in the Raptor transactions in the fully diluted earnings per share outstanding" as was indicated in your question.

For the reasons stated above, given that a fixed amount of shares was at issue and assumed to be outstanding in the Raptor transactions, I did not believe that a drop in Enron's share price would result in an increase in the fully diluted number of shares outstanding.

Senator Carl Levin
Supplemental Questions For the Record
Permanent Subcommittee on Investigations' Hearing
The Role of the Board of Directors In Enron's Collapse
May 7, 2002

Question for Mr. Blake:

1. You testified that even with the benefit of hindsight, you could not speculate as to what else the Board could have done to ensure that controls and procedures with regard to the LJM partnership were followed. Given that the controls did not adequately oversee the conduct of Mr. Fastow and other Enron executives, would you approve a similar arrangement against at another company?

Response to Question 1:

I believe that if Enron management and its financial and legal advisors had followed the controls and procedures that the Board instituted with regard to the LJM partnership, the oversight of Mr. Fastow and other Enron employees would have been more effective. As I indicated in my testimony, the Board and its Committees were regularly assured by Enron Management and Arthur Andersen that these controls were in place and functioning effectively. (*See, e.g.,* Presentation to Audit Committee, February 12, 2001; Presentation to Finance Committee, February 12, 2001.).

Whether I would approve a similar arrangement at another company would depend upon the particular facts and circumstances, and whether I believed that the arrangement would be in the best interests of the company and its shareholders.

Senator Carl Levin
Supplemental Questions For the Record
Permanent Subcommittee on Investigations' Hearing
The Role of the Board of Directors In Enron's Collapse
May 7, 2002

Question for Dr. LeMaistre:

1. At the hearing, you testified that it was not the Board's responsibility to monitor Kenneth Lay's line of credit with Enron, which he used to borrow nearly $80 million in cash from Enron. Who had responsibility for monitoring Mr. Lay's use of his line of credit?

Response to Question 1:

As I stated before the Subcommittee, I believe that there were three individuals who would have been in a position to monitor this matter: (1) the Treasurer of Enron, who received the request and disbursed the money; (2) an Enron in-house lawyer, who received the stock used to repay the loan; and (3) the person with whom that stock is registered and who makes the appropriate filing 45 days after the year end.

Senator Carl Levin
Supplemental Questions For the Record
Permanent Subcommittee on Investigations' Hearing
The Role of the Board of Directors In Enron's Collapse
May 7, 2002

Questions for Dr. Jaedicke:

1. Was it your understanding that the number of shares at risk in the Osprey and Raptor transactions was limited? Were you told that there was a limit to the number of shares Enron could be forced to issue or was that something you assumed? If you were told, who told you?

   Response to Question 1:

   It was my understanding that the number of shares (or forwards on Enron shares) in the Raptor transactions was limited by the initial Board (or Executive Committee) approval. The issuance of any new or additional shares would have required Board approval. Additional approvals would have been required, as well, in the event the value of the transaction exceeded the approval limits applicable to management.

   It is my understanding that Enron had reserved 20 million additional shares of Enron common stock and 100,000 preferred shares for issuance under the Share Settlement Agreement pertaining to the Osprey/Whitewing transactions. (*See* September 17, 1999 Resolution approving transaction.).

   The presentation of the Raptor transactions was made by the following individuals:

   Raptor I – Mr. Fastow introduced Mr. Glisan and Mr. Causey to present the transaction to the Finance Committee on May 2, 2000.

   Raptor II – Mr. Fastow presented this transaction to the Executive Committee at its meeting on June 22, 2000.

   Raptor III – Mr. Skilling presented this transaction to the Board at its meeting on August 7, 2000.

   The 1999 presentations concerning the restructuring of the Whitewing/Osprey transactions were made by Mr. McMahon.

2. In your testimony before the Subcommittee, you said that you took comfort in the practice of an integrated audit as it allowed for greater understanding by the auditor of a company's operations or a specific transaction by the auditor. In the case of Enron, it appears that the integrated audit resulted in Andersen's rendering an opinion of

Enron' accounting practices and transactions at Enron which Andersen helped to develop. Do you stand by your judgment that the integrated audit process is a positive practice?

Response to Question 2:

Yes. Arthur Andersen's early review and approval of the accounting disclosures for transactions developed and structured by Enron management was important to the Board. The integrated audit allowed for that.

Senator Jim Bunning
Supplemental Questions For the Record
Permanent Subcommittee on Investigations' Hearing
The Role of the Board of Directors In Enron's Collapse
May 7, 2002

__For Each Board Member Who Testified__:

1. Were any of you on the Board of Directors when the Board decided to allow Mr. Fastow to participate in the LJM partnerships?

   Yes.

   a. Can you tell us how the Board was approached with this idea?

   __Joint Response of Panel Witnesses to Question 1.a.__:

   Please see our response to Question 2 from Senator Levin.

   b. The Board seemed to put in place many controls that were supposed to balance the conflict of interest with Fastow working with the LJM partnerships, which means the Board was obviously concerned about the conflict of interest. Why didn't the Board just say "no"?

   __Joint Response of Panel Witnesses to Question 1.b.__:

   We did not say "no" because, based upon all of the information provided to the Board, we believed that this business decision was in the best interests of Enron and its shareholders.

2. How was the situation with the Watkins memo described to the Board of Directors? Did any of you take a look at the memo or want to talk to Ms. Watkins directly?

   __Joint Response of Panel Witnesses to Question 2__:

   We did not learn of the existence of the Watkins memo until after the investigation into it had been concluded. At that time, as is indicated in the relevant Audit Committee and Board minutes, we were told that an employee had raised some concerns concerning the related party transactions. Vinson & Elkins reported to the Audit Committee that it had investigated the matter, found no wrongdoing and recommended that no further investigation be conducted.

   The Audit Committee was assured that a report would be provided to Ms. Watkins about results of the Vinson & Elkins' investigation. The Board also requested a copy of the Watkins memo.

3. The Powers Report criticizes the Board of Directors for not looking into the transactions between Enron and LJM closely enough. How do you respond to this?

Joint Response of Panel Witnesses to Question 3:

On February 7, 2002, Mr. Winokur provided extensive testimony to the House Energy and Commerce Committee concerning his service on the Powers' Committee and the fact that he was not involved in that portion of its investigation pertaining to the actions of Enron's Board of Directors.

In that testimony, Mr. Winokur set out the areas in which he disagrees with the Powers' Committee's conclusions concerning the actions of Enron's Board. His criticisms of this aspect of the Powers' Report fairly reflect our views.

4. Mr. Blake, you said in your testimony that you do not feel that the Board of Directors failed in its "oversight duties." How can you argue that in light of the fact that the company is now in bankruptcy and many employees have been laid off and lost all or most of the money in their plans?

Response to Question 4:

As I explained in my written statement, I do not believe that the Board failed in its oversight duties. (Statement of Norman P. Blake, May 7, 2002, p. 3-6). I believe that the Board worked diligently and inquired sufficiently about the matters brought before it. In response, the Board instituted the necessary controls and procedures so that, if properly followed, they would have ensured that any problems or issues would have been brought to the Board's attention. Unfortunately, I believe that we were poorly served because management and outside financial and legal advisers who were responsible to report to us failed to follow these controls and procedures and give us full, complete information.

5. Dr. LeMaistre, in your testimony, you said that if Enron's management had "instituted the controls the Board installed, Mr. Fastow's compensation would have been reported to Mr. Skilling, the Audit Committee, Finance Committee and the Compensation Committee." As a member of the Compensation Committee, how often were you supposed to review Mr. Fastow's compensation with LJM? Did this happen?

Response to Question 5:

There was no frequency specified for the Compensation Committee's review of Mr. Fastow's compensation from the LJM transactions.

As Chairman of the Compensation Committee, I made attempts on two separate occasions to obtain this information from Enron staff. The first time, I was told that they had not received any information about outside compensation of 16(b) officers, which included Mr. Fastow. I received the same response upon my second inquiry several months later.

After the October 19, 2001 Wall Street Journal report about Mr. Fastow's compensation, the Board authorized a direct call to Mr. Fastow about this matter. John Duncan and I then called Mr. Fastow and obtained the information from him.

EXHIBIT A

RESPONSES TO QUESTION 1 FROM SENATOR CARL LEVIN TO EACH PANEL WITNESS

The Panel Witnesses do not recall the information requested in Question 1. These responses were compiled using data that was gathered by and at the direction of the Panel Witnesses' attorneys.

I. NORMAN P. BLAKE

Response to Question 1.a.:

As of December 31, 2001, Mr. Blake held 27,009 vested options[1] and 46,350 granted options[2].

Response to Question 1.b.:

As of December31, 2001, Mr. Blake owned 12,196 shares of common stock[3].

Response to Question 1.c.:

Since 1991, it appears that Mr. Blake made three open market purchases: 1) 2,000 shares on February 4, 1994; 2) 2,000 shares on May 4, 1994; and 3) 5,000 shares on October 24, 2001. Since Mr. Blake did not have any recorded gifts or sales after October 24, 2001, at least 5,000 shares of his current holdings are from individual purchases of stock. Mr. Blake did have open market sales and gifts after May 4, 1994, and the source of these gifts may be individual purchases or

[1] For all Panel Witnesses' responses to Question 1.a., the following applies: Vested options outstanding are computed using the vesting schedules provided in Enron's Optionee Statements. The vested options holdings are pegged to the earliest reported option holdings in the proxy statements from 1999 to 2001 and then adjusted using the Insider Trading Monitor ("ITM") transaction data and the option vesting schedules from the Enron Optionee Statements. The holdings numbers also reconcile with Proxy Statements from subsequent periods.

[2] For all Panel Witnesses' responses to Question 1.b., the following applies: Granted options outstanding are taken from Enron Optionee Statements and then adjusted using the ITM transaction data.

[3] For all Panel Witnesses' responses to Question 1.c., the following applies: Common stock holdings are computed by pegging holdings to the earliest holdings number reported in the 1999 to 2001 proxy statements. This number is then adjusted to reflect all transactions reported by ITM to December 31, 2001, data from counsel, and the Phantom Stock Program as reported in Enron's Optionee Statements and Executive Compensation Summaries. The holdings numbers also reconcile with Proxy Statements from subsequent periods.

company granted stock or options so it is a possibility that all or none of the 4,000 shares he purchased in 1994 are still in his current ownership.

Response to Question 1.d.[4]:

4,720 shares were sold on October 31, 2000 for $379,677. 3,600 shares were sold on October 31, 2000 for $289,584. 3,920 shares were sold on October 31, 2000 for $315,325. 3,840 shares were sold on October 31, 2000 for $308,890. 5,120 shares were sold on October 31, 2000 for $411,853.

II. JOHN H. DUNCAN

Response to Question 1.a.:

As of December 31, 2001, Mr. Duncan held 39,249 vested options and 58,590 granted options. A family partnership currently holds unexercised and unexpired options for 19,280 shares.

Response to Question 1.b.:

As of December 31, 2001, Mr. Duncan owned 167,822 shares of common stock.

Response to Question 1.c.:

132,622 shares were purchased prior to 1990. 35,200 shares were the result of the exercise of stock options.

Response to Question 1.d.:

35,000 shares were sold on May 9, 2001 for $2,009,700.

III. ROBERT K. JAEDICKE

Response to Question 1.a.:

As of December 31, 2001, Dr. Jaedicke held 39,249 vested options and 58,590 granted options.

Response to Question 1.b.:

As of December 31, 2001, Dr. Jaedicke owned 17,332 shares of common stock.

[4] The following applies to all Panel Witnesses' responses to Question 4.d.: The data was obtained from ITM. The number of shares is split adjusted. The share price is split adjusted.

Response to Question 1.c.:

Since 1991, it does not appear that Dr. Jaedicke made any open market purchases, so all holdings are assumed to be derived from company granted stock or options.

Response to Question 1.d.:

5,360 shares were sold on February 24, 2000 for $353,438. 8,000 shares were sold on May 2, 2001 for $488,000. These transactions involved exercises of six-year options that were due to expire within 90 days of each transaction.

IV. CHARLES A. LeMAISTRE

Response to Question 1.a.:

As of December 31, 2001, Dr. LeMaistre held 39,249 vested options and 58,590 granted options.

Response to Question 1.b.:

As of December 31, 2001, Dr. LeMaistre owned 17,272 shares of common stock.

Response to Question 1.c.:

Since 1991, it does not appear that Dr. LeMaistre made any open market purchases, so all holdings are assumed to be derived from company granted stock or options.

Response to Question 1.d.:

1,984 shares were sold on January 8, 1999 for $58,964. 7,360 shares were sold on December 28, 1999 for $313,683. 8,000 shares were sold on May 10, 2001 for $469,120. These three transactions involved the sale of ten-year options that were due to expire on May 8, 1999, May 14, 2000, and May 13, 2001.

V. HERBERT S. WINOKUR, JR.[5]

Response to Question 1.a.:

As of December 31, 2001, Mr.Winokur held 39,249 vested options and 58,590 granted options and unvested restricted shares.

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[5] Mr. Winokur's holdings do not include shares held in a charitable foundation for which he has no pecuniary interest.

Response to Question 1.b.:

As of December 31, 2001, Mr. Winokur owned 76,740 shares of common stock.

Response to Question 1.c.:

Mr. Winokur currently holds 76,740 shares that have a cost basis of approximately $1.8 million. 50,872 of these shares were the result of the exercise of stock options or the vesting of restricted shares.

Response to Question 1.d.:

It does not appear that any of Mr. Winokur's shares were sold.

Supplemental Questions for the Record
and
Responses by Michael H. Sutton

Question:

The New York Times reported that Enron received an exemption from the Securities and Exchange Commission from Investment Company Act regulation with respect to its investments in foreign assets. Are exceptions commonly granted? Is there a documented discussion surrounding this decision that would be available to the Subcommittee? How can the Subcommittee determine if Enron was granted any other exceptions by the SEC?

Response:

I am not able to provide much insight in response to this series of questions. My experience at the SEC did not include dealing with issues relating to exemptions from the Investment Company Act. Rather, as Chief Accountant, my experience generally was directed to dealing with accounting and disclosure issues of SEC registrants, including registrants under the Investment Company Act. Specifically, I do not know if exemptions are commonly granted.

There well may be documentation of discussions surrounding the referenced decision. I respectfully suggest that you might direct your questions relating to that decision to the Division of Investment Management. Questions relating to other possible exceptions granted Enron might be directed to the Office of the Chairman or the Office of General Counsel.

* * * * * * *

Question:

How would you address the concern that if too much responsibility is placed on the board and, subsequently, the board is open to excessive liability, it will be difficult to get qualified individuals to sit on boards?

Response:

I discount suggestions that improvements in the corporate governance process will expose directors to grave new risks and, therefore, discourage qualified individuals from sitting on boards. In my view, this assertion has become a "red herring". The real concern may well be that a truly responsible and responsive board will accomplish the desired objective – effective oversight of management and independent auditors on behalf of investors.

U.S. Senate Permanent Subcommittee on Investigations
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Supplemental Questions for the Record
and Responses by Michael H. Sutton

Concerns about "excessive liability" should be aired, however, and to the extent good public policy permits, addressed in any needed enabling legislation or regulation. Also, we should note that the litigation risks of board service have been, and should continue to be, insurable.

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Question:

Some directors of the Enron board have been criticized for their membership on numerous corporate boards, calling into question their ability to dedicate time and focus to issues at Enron. Would you be in favor of limiting the number of corporate boards an individual may serve simultaneously?

Response:

Yes. Clearly, there is some limit on the number of boards an individual can serve on and do so effectively. Service on more than four to six boards concurrently would raise questions about the ability of an individual to devote adequate time and attention to the governance responsibilities of each board.

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Question:

How would you amend current rules for Special Purpose Entities ("SPEs") to make them less "nonsensical"? How would you amend the accounting rules for consolidations and off-balance-sheet financing?

Response:

The reason the current accounting rules for SPEs are "nonsensical" is that they do not accurately portray the underlying economics of the arrangements. In virtually all of the arrangements, the sponsoring entity retains substantial risks and retains the ability to control substantial benefits associated with the assets and operations transferred to the SPE. The current accounting rules have been designed to permit the removal of assets and operations from the sponsor's financial statements if certain bright-line tests are met, even though meeting those tests has little bearing on the sponsor's ultimate risks and benefits. Thus, we have accounting rules that have permitted distorted financial reporting when as little as 3% of total investment in the SPE comes from outside, at-risk capital. And, sometimes even that capital is not truly at risk.

The current approach being pursued by the FASB to address the criticism of the current rules does little to bring the accounting and underlying economics in line. It would merely move the bright line from 3% to 10% (though even the proposed 10% test would be framed as a "rebuttable presumption") and add a few more tweaks that would have the effect of changing deal structures, but do little to improve the quality of financial reporting. As I indicated in my testimony, the FASB is subject to great pressure from business managers, deal makers, and financial intermediaries to continue rules that permit, through creative structuring, the kind of obfuscation in financial reporting that became apparent to the world in the Enron case. As I also have stated, only a truly independent standards-setting process, supported by those who have the greatest stake in truly transparent financial reporting, will bring about the kind of change that is essential.

I would urge the FASB to develop accounting standards that fully respect the underlying economics of SPEs and require consolidation in all cases in which the sponsor bears significant risks and receives significant benefits from the SPEs assets and operations. If the sponsor bears more than an insignificant risk of loss and has the ability to receive more than an insignificant benefit from the assets and operations of the SPE, the SPE should be consolidated.

The SPE issues really are a subset of the broader consolidation and off-balance-sheet financing issues, and my comments above about the need for accounting to reflect the underlying economics would apply to those broader issues as well. Today, companies are able to finesse the consolidation rules and, thereby, manage the financial results they present to investors. For example, they have used unconsolidated entities to park equity method losses off the income statement, to create the appearance that transactions with affiliated entities are bona fide transactions with independent third parties, to permit the netting of losses on securities investments with gains on other securities investments, and to hold indirectly risky assets that regulators forbid them to hold directly.

Current practice abuses can be rationalized only through concepts-based standards that meaningfully inform investors about the underlying economic performance of the company. I would urge the FASB to develop standards that look more broadly at the issues than the current narrow focus of trying to define "control" in a bright line context. Rather, it should seek to identify the economic characteristics commonly associated with ownership, and if an arrangement substantially conveys those risks and benefits to a parent, sponsor, or venture, consolidation should be required.

* * * * * * *

Question:

Why do you think it was so easy for Enron's management to withhold information from the board of directors?

Response:

Because I have no direct knowledge of the Enron case, I can only hypothesize based on the public record and my prior experience.

Supplemental Questions for the Record
and Responses by Michael H. Sutton

I sense that, in part, the board was willing to accept, without a great deal of inquiry or challenge, the information that management was willingly to provide. The board seemed to be a group that was comfortable in yielding to management, even in circumstances in which more probing clearly seemed to be called for. A compliant board can be the result of careful selection, careful conditioning, or both. Overly generous compensation for services as a director, coupled with generous consulting and other arrangements, could increase the conditioning effect and lead to less independent oversight and judgment.

I also sense that the audit committee's dialogue with the independent auditors had a strong "management filter". By that, I mean that an aggressive management can have substantial influence on, if not control of, what information comes to, and what dialogue takes place with, the audit committee and the board. Financial incentives to the auditor to not disturb a good relationship with management can exacerbate the problem.

A combination of those two influences – a passive board and muted communications and dialogue with the auditors – can lead to ineffective board oversight. That is the basis for my testimony that we should "revisit and rewrite our corporate governance policies and guidelines to clearly break the bonds between management and the independent auditor, and to unmistakably spell out the responsibilities of boards of directors and audit committees to shareholders and the investing public".

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Question:

In his testimony, Mr. Jaedicke used a quote from Warren Buffet. Mr. Buffet said, "An audit committee that meets for a few hours several times a year is simply not going to pick up anything that is missed by the outside auditors ... therefore, the task of the audit committee should be to hold the feet of the outside auditors to the fire." How do you respond to that?

Response:

As stated in my testimony, I believe that an important function of the audit committee is "to see to it that auditors do their jobs". I assume that is what Mr. Buffett means by "the task of the audit committee is to hold the feet of the outside auditor to the fire." But, the role of the audit committee should not be viewed narrowly as receiving and challenging the report of the independent auditor. As I have indicated previously, monitoring and overseeing the quality of financial reporting presented by management should be a shared goal and responsibility of the audit committee and the independent auditor. The independent audit should be viewed as a valuable resource of the audit committee, and the principle relationship between the company and the independent auditor should be with the audit committee. That relationship should result in a better informed and effective audit committee and stronger support for the right kind of work and decisions by the independent auditor.

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Supplemental Questions for the Record
and Responses by Michael H. Sutton

Question:

What is the most important thing a board can do to maintain its independence?

Response:

One thought is that a board of directors should have a clear understanding with, and acknowledgement by, management that the independence of the board is critical to an effective governance process – a "contract". The contract between the board and management should clearly articulate the expected independent role and relationship that effective governance demands, and clearly spell out the authority and responsibility of the board to exercise its independent judgment. An effective board must see itself as the overseer of management and have the authority to give meaning to that role.

* * * * * * *

Question:

What percentage of other boards do you think have the same problem as Enron?

Response:

It would be difficult to quantify a response to this question in percentage terms. If we define the "problem" at Enron as being a situation in which the board was not sufficiently diligent and challenging in its oversight of management and, through its audit committee, not sufficiently engaged in overseeing the work and evaluating the findings of the independent auditors, I would say that those conditions are not uncommon among boards of directors of public companies. I base that opinion on my experience as a practicing auditor and as a capital market regulator. As I stated in my testimony, "We would like to believe that Enron is an anomaly – that the governance issues raised are isolated to this case – but it is not. While Enron has become a 'poster child' for a system out of control, the underlying concerns about the diligence of boards of directors and audit committees reach far more broadly into our corporate and capital market culture."

Exemption Won In '97 Set Stage For Enron Woes

By STEPHEN LABATON

WASHINGTON, Jan. 22 — As it expanded aggressively overseas in the 1990's, the Enron Corporation won an exemption from a Depression-era law that would have prevented its foreign operations from shifting debt off their books and that barred executives from investing in partnerships affiliated with the company.

The exemption enabled Enron's foreign operations to engage in the kind of financial engineering that experts now say was reminiscent of some of the corporate excesses of the 1920's that led to the 1940 law and that were an important element of the company's meteoric rise and startling collapse.

Had Enron not been granted the exemption, some of its operations in South America and in Europe would not have been able to structure financial operations to both conceal them from investors and shift debt off their books.

Enron's initial efforts in 1996 to persuade Congress to change the law were thwarted by opposition from a powerful trade group and some federal regulators. The company responded by hiring the former boss of a leading staff official at the Securities and Exchange Commission to represent it in negotiations with the agency. In an unheralded five-paragraph order in March 1997, the S.E.C. official, Barry P. Barbash, gave En-

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New York Times
1/23/02

REGULATIONS

Law Exemption in 90's Set Stage for Enron

Continued From Page A1

ron's foreign operations a broad exemption from the law — the Investment Company Act of 1940.

How Enron came to get its exemption from the severe restrictions of the law clearly illustrates the ways the company lobbied Washington and the response by the regulatory system. That system was devised during the Depression to protect investors and customers of utilities from a wide range of corporate abuses that investigators think ultimately took place at Enron.

Both Congress and the S.E.C. are reviewing the exemption to the Investment Company Act and earlier exemptions that were given to the company by the agency, including a 1993 exemption from the tough restrictions imposed by the Public Utility Holding Company Act of 1935.

Experts say that the S.E.C. rulings unshackled the company from significant accounting restraints and business dealings between the Enron companies and their executives. The 1997 exemption, in particular, cleared the path for the company to both expand overseas and make greater use of the special partnerships that have caused the company so much turmoil.

"From a regulatory standpoint, this raises a flag," said Joseph V. Del Raso, a former official at the S.E.C. in the 1980's and an expert on the Investment Company Act. "It gave them carte blanche to go all over the world and set up subsidiaries and affiliated entities that would have been prohibited under the act."

Another expert on the act, Mark A. Sargent, the dean of the Villanova law school, agreed.

"The Enron structure was not a single company with stockholders engaged in operations like an ordinary corporation," he said. "It was similar to an investment company with investments in a bunch of different companies. The decision to exempt those from the kind of protections to investors is now coming home to roost."

Arthur Levitt, who was the chairman of the S.E.C. when the 1997 exemption was granted, said today that he had no recollection of it. But he said it could be a potentially significant part of the agency's role in failing to oversee Enron.

"It may be one of those cases of the nail in the shoe of the horse," he said. "It may be one of those things that seemed insignificant at the time but can wind up being determinative."

Mr. Barbash, the lawyer at the S.E.C. who approved the exemption, said in an interview this week that he viewed the exemption as narrow because it applied only to the foreign operations of Enron and some of its subsidiaries. He said that it was successful in that it managed to head off Enron's efforts to have a broadly worded exemption written into the law "that companies could have then driven trucks through."

"Enron knew the regulatory boxes, and they tried to fashion their businesses to fall outside of those boxes," Mr. Barbash said. "Much of what's been written so far about the company is that it turned itself inside out like a pretzel to fall outside of restrictions — accounting restrictions, taxpayer restrictions and regulatory restrictions."

'Giving Enron an inch and they took miles,' a former S.E.C. official says.

Another former S.E.C. official who is an authority on the Investment Company Act, was more critical.

"This was a case of giving Enron an inch and they took miles," said the former official, who spoke on the condition of anonymity. "They were given a significant new opportunity, and they took it and flew it smasho into the ground."

Mark Palmer, an Enron spokesman, did not return a call seeking comment.

Mr. Barbash, who at the time was director of the investment management division at the S.E.C., said that Enron's lawyers came to him in 1996 after the company had failed to persuade Congress to grant the company broad exemption to the 1940 law.

Enron and several of its subsidiaries said they needed the exemption because their foreign operations were quickly taking on the characteristics of investment companies. The act, which regulates mutual funds and other kinds of investment companies, generally applies to companies that hold at least 40 percent of their assets in securities that are passive investments and not controlling interests.

A lawyer who represented Enron said that although the company and its foreign subsidiaries had actually controlled many of their overseas ventures, like power plants, they were unable to have a 51 percent stake in them because of local rules and political constraints.

In 1996, Congress rewrote parts of the act but refused to grant an exemption to Enron because of significant opposition from both the S.E.C. and the Investment Company Institute, the main trade organization for the mutual fund industry and a strong supporter of the law. Mr. Barbash said that in 1996, Congressional aides advised Enron's lawyers to seek an exemption directly from the agency.

The company decided to retain Joel H. Goldberg, a former director of the investment management division at the S.E.C., who said today that he did not know how the company came to hire him.

An Enron official said the company had retained Mr. Goldberg knowing that he had previously been Mr. Barbash's boss and was his predecessor at the S.E.C. Mr. Goldberg had been Mr. Barbash's supervisor at the S.E.C. in the 1980's and the Labor Department in the 1970's. The two lawyers are now partners at the international law firm of Shearman & Sterling.

Mr. Goldberg said he viewed the exemption as a narrowly tailored one intended to permit the company to continue its overseas projects. But he acknowledged that had the company not been granted the exemption, it would have been constrained from using any partnerships or shifting debt off the books in its foreign operations.

"I guess on the one hand, if they had been subject to the Investment Company Act, they probably could not have done these transactions," he said. "The subsidiaries would not have existed, and they would have had to make another plan."

826 Orange Avenue
PMB 608
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June 3, 2002

Senator Carl Levin
Senator Susan M. Collins
U. S. Senate Permanent Subcommittee on Investigations
Washington, DC 20510-6250

Dear Senators Levin and Collins:

In your letter of May 24th you asked me to respond to three follow-up questions concerning your investigation of *The Role of the Board of Directors in Enron's Collapse.* My response is as follows:

QUESTION 1. During your testimony you argued in favor of more complete disclosure of the relationship between a director and the corporation. Would you also be in favor of certain limits or prohibition policies whereby directors would be precluded from entering into business relationships (i.e. consulting contracts) with the corporation? Would you be in favor of either eliminating or limiting the dollar amount of donations a company could make to special interests affiliated with its directors?

My Response:

I personally believe that it is wrong for a director to have a consulting relationship with the company on whose board they serve. The director is paid a retainer for their services and the CEO or other senior management should feel free to consult at any time with the director on matters that he or she has some level of expertise. In my mind that is why the director is paid a retainer (to answer questions and give advice either during the board meeting or after). If more extensive consulting is needed and a contract and additional compensation is necessary, then a new relationship has been established, and the director is rapidly on the way to losing independence.

There will be difficulty, however, with the government trying to regulate in an attempt to limit that type of behavior. If a company is determined to give additional compensation to its directors, it will find innovative ways to do so, and the regulators will forever be trying to catch up. For example, the SEC a number of years ago stated that companies should not provide a retirement plan for directors. As a result, most companies announced that they had eliminated their existing retirement plans, but many took the annual dollar value of the plan and put it in a deferred savings account for the director that pays out upon retirement. The company can now legitimately claim it no longer has a retirement plan for directors, but I believe that most shareholders would feel that in reality little has changed. Also, if you ban consulting contracts for the director, what about their spouse, or other relatives? The regulator will forever be in a "catch-up" mode.

I believe that the most effective approach for the government to insure that corporations follow good governance practices is as follows:

First, have the SEC publish a list of desired governance practices that they believe first class boards should embrace. Include in that listing all of the desirable practices that have been identified over the past several years. The list should be evolutionary and be updated as new ideas come forward, or as new corporate abuses surface in the future.

Second, require that all corporations publish their governance practices annually in their proxy so that all shareholders have a better idea how their company is being managed. I also believe that every board should form a committee of outside directors with the responsibility of reviewing,

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #82

updating and publishing the governance practices of that company.

Third, I believe (as I stated in my prepared remarks) that a very detailed description of the total relationship between each director and the company should be published annually in the proxy – especially detailing all forms of compensation and benefits that the director and their relatives receives from the corporation. If you are being asked, as a shareholder, to vote for someone to represent you during the board deliberations, you deserve to know how independent the proposed director truly is. I also believe that with this information in hand, shareholders will be more likely to question the prospective directors during the annual meeting on any issues of concern. By publishing all of the benefits a director derives from the corporation, the abuses will be quickly identified, and I suspect that the large number of shareholder activist groups in this country will highlight and publicize those that they feel are particularly abusive. That will bring about change in the vast majority of corporations and will be much more effective than trying to have the government legislate good behavior.

Fourth, the SEC should attach severe penalties to any director or corporation that knowingly does not disclose ANY form of compensation or benefit, or ANY relationship that exists between a director and the company. If a director or a company are found to have knowingly hidden a relationship or benefit from the shareholders, then publicizing that director by name and requiring that they resign from all of their corporate boards would insure that "everything" is out in the open. It is important to realize that most of the benefits or relationships are already made public today by most corporations. In almost all instances, the information is dispersed throughout the myriad of financial documents that are required by the SEC but seldom read by the shareholders. That's why having it available annually in the proxy, on one page, in easily understood language is critical to successful disclosure.

You also asked for my opinion on contributions by corporations to charities of interest to the director. I believe that it is not necessarily wrong for a company to match the contribution that a director makes to charity (as long as it is part of the total disclosure mentioned above). Personally, I believe there should be a cap on the company's contribution (e.g. $10,000 per year). But if a corporation wants (as part of their director compensation plan) to have a disproportionate amount of the benefit be in the form of contributions to charity, AND if the disclosure is made clearly in the proxy, AND if the shareholders do not object to that form of compensation for their directors, THEN why should the government get involved in trying to limit it? Large contributions to charities on behalf of directors are no more or less compromising to the director's independence than excessive retainer fees.

<u>QUESTION 2.</u> One weakness that became apparent in the Subcommittee's interviews with Enron's directors was a lack of interaction between directors and Enron employees outside of formal Board and Committee meetings. While the Board expected Enron employees to bring sensitive issues that were not adequately addressed by management to the Board, directors and employees typically did not have relationships that would encourage such disclosure to directors. While regulating such relationships is impossible, what best practices would you recommend to foster such relationships?

<u>My Response:</u>

You stated that the Enron board expected Enron employees to bring sensitive issues to their attention that were not adequately addressed by management. I seriously doubt they believed that would occur. In the corporate world, any employee who decides to bypass the CEO and take an issue directly to the board better have an excellent reason for doing so because chances are they (or the CEO) are on the verge of a "career ending move". The reason directors should be familiar with a wide spectrum of the senior management team is to get a feel of the "tone at the top" and morale within the corporation. Their knowledge of and contact with this management group is also invaluable when the question of CEO succession is raised

To accomplish this there are the obvious and frequently used methods of occasionally having the directors meet the management team at a holiday dinner, golf outing, etc. There is however a "best practice" that I believe effective. It involves inviting and expecting each director to have a one-on-one breakfast or lunch meeting with a member of the management team when they come to town for board meetings. My experience is the directors will then be better prepared to deal with executive succession issues when they arrive, and they will also have a better chance of learning how things are going within a corporation.

QUESTION 3. Some directors of the Enron board have been criticized for their membership on numerous corporate boards, calling into question their ability to dedicate time and focus on issues at Enron. Would you be in favor of limiting the number of corporate boards an individual may serve simultaneously?

My Response:

I believe that limits should be placed, but it is best done by a board governance committee rather than government regulators. Personally I believe that when a man or woman first becomes a Chairman / CEO they should be required to go on an outside corporate board to gain the experience of what it is like to be on the "other side of the table".

However I also believe that an active Chairman / CEO, or for that matter any director who has a full time job, should be on no more than two or three outside boards.

Individuals who are retired or not fully emplolyed potentially have the time to devote to their responsibilities as directors of a greater number of companies. But what the correct number is is not clear. Four or five seems perfectly reasonable..... nine or ten does not.

Probably the best answer is to list the number of boards a director is on and allow the shareholders at the annual meeting to raise the question if they feel it is excessive. Having the shareholders ask these types of questions of the director candidates at the annual meeting would a positive step forward in the world of corporate governance. Once again, that is why I believe that a major change is needed in the way information on the relationship between a director candidate and the corporation is displayed in the proxy.

Thank you for the opportunity to respond to these questions, and good luck with your investigation.

Sincerely,

Robert H Campbell

826 Orange Avenue
PMB 608
Coronado, CA 92118
June 10, 2002

Senator Carl Levin
Senator Susan M. Collins
U. S. Senate Permanent Subcommittee on Investigations
Washington, DC 20510-6250

Dear Senators Levin and Collins:

In your letter of May 29, you asked me to respond to four follow-up questions concerning your investigation of *The Role of the Board of Directors in Enron's Collapse.* My response is as follows:

QUESTION 1. Why do you think it was so easy for Enron's management to withhold information from the board of directors?

My Response: Based on what I have read and heard about the Enron situation, I believe this was a board of directors that was too willing to accept the word of management and not do their job of diligent probing to discover the complete story. Once that boardroom behavior became the norm, it would be relatively easy for management to lead the board wherever they felt necessary or desirable.

I realize that at the hearing in Washington DC on May 7th the Enron directors said that was not the case – they claimed that they did a thorough job of questioning. I just can't believe that to be true. The Enron directors who testified seemed to indicate that they did the best job humanly possible, but were lied to by management and that was the problem. It has been my experience that some members of management sometimes have a tendency to not want to pass on bad news or reveal the complete story, in hope that the situation will get better before the board meets again. So they tell part of the story and leave it to the directors to probe and discover the rest. This is obviously a horrible practice and once discovered can quickly erode the confidence of the directors in management. But I don't believe that many members of management will deliberately and knowingly lie to their directors. If they do, and it is discovered, then the element of trust is completely destroyed, and either the management is gone or any right thinking director will resign.

QUESTION 2. In his testimony, Mr. Jaedicke used a quote from Warren Buffet. Mr. Buffet said, "An Audit Committee that meets for a few hours several times a year is simply not going to pick up anything that is missed by the outside auditors...therefore, the task of the audit committee should be to hold the feet of the outside auditors to the fire." How do you respond to that?

My Response: I agree with what Warren Buffet said. If the independent auditors miss something – or if they and management agree to not reveal some set of facts or behavior, then it is not likely than an audit committee will ferret out the truth until the abuse has created a situation that is obvious to all. Most of today's major corporations are very complex operationally and financially, and any audit committee that meets several times per year for a relatively short period of time has little chance of discovering any fact missed or hidden by a staff of internal and independent auditors.

This is why it is extraordinarily important for the audit committee to set the correct tone with both the internal and independent auditors. It must be thoroughly understood by all that they (the audit committee) expect complete disclosure and candor in all areas at all times. The internal auditors work for management, and the independent auditors work for the audit committee and the board. They are not two pieces of the same organization that are meant to simply share the load. These two groups are meant to provide a set of checks and balances, which is all the more reason why it makes absolutely no sense for the independent auditors to also be performing any part of the internal audit.

QUESTION 3. What is the most important thing a Board can do to maintain its independence?

My Response: Establish a committee of outside directors to be responsible for implementing the "best practices" in corporate governance. This committee must consist of strong willed and experienced independent directors. Their work cannot be considered a one-time fix; it must instead be a living and evolving process. Once this committee is established and the best practices become the "norm", all directors will assume more independent behavior, the company will be better managed, and the shareholders will benefit greatly.

I would also like to remind this committee that my testimony on May 7th spoke of the necessity for outside directors to meet at least once per year with no member of management present. There is no substitute for this meting if the outside directors are to perform their duties in a responsible manner.

Question 4. **What percentage of other Boards do you think have the same problems as Enron?**

My Response: **I really don't know the answer to that question. But I do believe there are a very large number of boards that have at least one of the problems exhibited at Enron: outlandish and seemingly unjustified compensation for executives and directors, a lack of candor at board meetings, too familiar a relationship between the independent auditors and management, a board of directors that is less than thorough in questioning management behavior, independent directors that are less independent than shareholders realize, overly aggressive accounting, an arrogant attitude about the company, it's future, and it's position in the industry, etc. But the problem is that once you begin to exhibit one of the characteristics mentioned above, it probably won't be long before others will follow.**

I would hope that the companies that currently have all of the problems exhibited at Enron are few in number – but no one knows for sure. The one thing I am sure of is that the publicity surrounding the Enron debacle, and the flood of law suits targeting the people involved, has resulted in a very large percentage of publicly traded companies and boards of directors reassessing their current behavior. The only problem is directors don't know what they don't know; and without some action by the federal government, the story will eventually cease to be on every director's mind, and bad habits will surely return.

Once again thank you for the opportunity to respond to these questions, and good luck with your investigation.

Sincerely,

Robert H Campbell

April 30, 2002

The Honorable Carl Levin
Chairman
Permanent Subcommittee of Investigations
Committee on Governmental Affairs
199 Russell Senate Office Building
Washington, DC 20510

The Honorable Susan M. Collins
Ranking Minority Member
Permanent Subcommittee on Investigations
Committee on Governmental Affairs
199 Russell Senate Office Building
Washington, DC 20510

Dear Senators Levin and Collins :

I appreciate the invitation to testify at the May 7th hearing, but unfortunately, I must decline.

Weil, Gotshal & Manges represents Enron in Chapter 11. Accordingly, I am not able to testify on this matter.

I have, however, testified before the Senate Banking Committee, and commented on general corporate governance issues arising out of the current investigations, and hearings.

I am pleased to enclose my testimony and the follow-up letter John Whitehead and I submitted to the Senate Banking Committee.

Very truly yours,

Ira M. Millstein

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U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #83

SUMMARY OF TESTIMONY

Ira M. Millstein
Co-chairman of the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees

Recent financial reporting and governance failures implicate the incentives that drive managers, boards and those who advise them to push to the limit and beyond the numbers that are meant to accurately reflect the company's financial performance and health. In the last decade, management has faced increased market pressures for short-term stock price performance and corresponding pressures to satisfy market expectations on a quarterly basis. This, coupled with increased reliance on forms of compensation that focus on short-term stock appreciation, may have created incentives that tipped the balance toward the promotion of self-interest rather than the protection and promotion of long-term shareholder value. We need to seek incentives and disincentives that are more carefully attuned to pressures in the current environment. Incentives and disincentives are needed to deal with the "given" that directors, managers, auditors, analysts and lawyers are fallible human beings (like all of us). They may not always subordinate their self interests to those on whose behalf they are acting.

Board Independence

- Boards of publicly traded corporations should be required (through listing standards) to include a substantial majority of "independent" directors under a strict definition of independence (ideally the same definition that applies to audit committees, but with some refinement).

- The definition of director independence now provided in listing rules for audit committee purposes should be reviewed to determine whether it adequately addresses all the relationships that may reasonably be expected to reduce independence.

- Boards should be required (through listing standards) to constitute a compensation committee with entirely independent directors.

- Boards should be encouraged or required (through SEC disclosure requirements based on either listing requirements or a code of best practice) to separate the position of CEO from that of board leader. Board leadership should be provided by an independent director.

- The boards of listed companies should be encouraged or required (through SEC disclosure and listing requirements) to adopt, regularly review and disclose a corporate code of conduct that addresses conflicts of interest and management and director stockholding and trading policies.

Compensation

Performance compensation based on a snapshot of stock market performance at a single point in time chosen by the manager may not provide incentives for the kind of management activity that is "good" for the company and shareholders as a whole in the long run.

- Pay-for-performance programs should be linked to measures of profitability or economic value added rather than short-term changes in stock market valuation. They should be designed to consider company performance relative to peer group performance. Consideration should be given to creating a stricter definition of what constitutes "performance based" compensation under I.R.C. § 162(m).

- Mechanisms should be developed to encourage executives and directors to hold stock they receive, whether in the form of stock grants or stock options, for a significant period of time. Ideally, companies should restrict or discourage sale of company stock during a director's tenure and require or encourage significant holding periods for executives. Consideration could be given to creating tax incentives designed to encourage executives to hold stock.

- Prompt disclosure of *all* transactions in the company's stock by corporate executives and directors should be required by SEC rules.

- Directors should be compensated fairly for the time necessary to fulfill their responsibilities, but grants of stock options to directors should be avoided.

Conflicts of Interest

- The boards of publicly-traded companies should be required or encouraged through listing standards and SEC disclosure requirements to adopt, regularly review and disclose a corporate code of conduct that addresses conflicts of interest, and management and director stockholding and trading policies. The actions taken by boards in implementing these policies should also be reported on, including disclosure of any exceptions granted under these policies and the reasons for the exceptions.

- SEC rules should be amended to mandate prompt disclosure of transactions between the corporation (or its affiliates) and members of senior management, directors or controlling shareholders.

Professional Advisors

- The presumption should be that audit and consulting don't mix. However, the audit committee should have authority to decide if and when an exception to this presumption is necessary and desirable for the company and its shareholders. (This could be encouraged through an additional SEC requirement that audit committees disclose the reason why they believed it necessary and desirable to allow an exception to the general presumption that the outside auditor should not provide consulting services.)

- The ABA should consider whether ethical conduct rules give lawyers sufficient guidance in balancing these roles; and
- The ABA should consider encouraging a set line of reporting for in-house counsel to bring to the board concerns not otherwise acted on by management.

* * *

Diligent independent directors, when properly led, informed and assisted, can circumscribe the agency (self interest) problems. If managers are not overly motivated by options to seek short-term market price appreciation, they should be less likely to push the limits. And if auditors, analysts and lawyers remove the conflicts that stand in the way of the true professionalism the public expects, they are more likely to resist.

TESTIMONY CONCERNING THE ROLE AND INDEPENDENCE OF PUBLIC COMPANY BOARDS, THE PROFESSIONALS UPON WHOSE ADVICE THEY MUST RELY AND THE ROLE OF COMPENSATION

by: Ira M. Millstein
Co-chairman of the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees, sponsored by the New York Stock Exchange and National Association of Securities Dealers, 1998-1999.

Before the Senate Committee on Banking, Housing and Urban Affairs

February 27, 2002

Chairman Sarbanes, Ranking Member Gramm, and Members of the Committee:

I am pleased to appear before you in my capacity as Co-chairman of the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees ("Committee on Audit Committee Effectiveness"). This Committee was convened in 1998 by the New York Stock Exchange ("NYSE") and the National Association of Securities Dealers ("NASD") at the request of Securities and Exchange Commission Chairman Arthur Levitt. The Report we issued in 1999 addressed concerns that are closely related to the concerns about the integrity of financial reporting, the audit and accounting profession and corporate governance that are at the heart of this hearing.

At the outset, be advised that I am a senior partner in the international law firm of Weil, Gotshal & Manges LLP. Several months ago, in the fall of 2001, my firm was hired to counsel Enron in its bankruptcy restructuring. The firm was not regular counsel to Enron previously. I am not actively engaged on the Enron matter, although my partners have consulted with me from time to time on certain corporate governance issues relating to the bankruptcy. I have no knowledge of the events leading up to the bankruptcy filing other than what has appeared in the media. In addition, over the years my firm has represented Arthur Andersen in litigation and other matters unrelated to Enron. I have no knowledge of Andersen's relationship to Enron, other than what has appeared in the media.

My testimony today as Co-chairman of the Committee on Audit Committee Effectiveness does not necessarily reflect the views of Weil, Gotshal & Manges LLP or any of my partners. I have not consulted any client in regard to this testimony, and therefore it does not reflect the views of Enron, Andersen or any other client of my firm.

You have asked that I provide recommendations for legislative and regulatory responses to what appears to be an increasing incidence of high-profile financial reporting and governance failures in recent years. Throughout my career I have counselled corporate boards, managers and investors on various corporate governance and regulatory matters and have studied closely our system of corporate governance regulation. (I have also taught graduate business school courses on corporate governance at Yale, Harvard and Columbia.) Over this period, one element has remained constant: Our market system is not static; it is dynamic -- constantly changing. Our corporate governance system continuously adjusts and improves in response to failures, whether through voluntary adjustment of board practice, new listing rule requirements, amendments to SEC disclosure rules, or various related pieces of legislation, for example, in the area of tax incentives. High-profile corporate governance failures should not be interpreted, therefore, as failures of capitalism or capital markets. Rather, these failures should be viewed as cause for further adjustments and corrections to our corporate governance system. Such adjustments should focus on the factors that are key to the problems emerging in today's corporate environment: management incentives, true independence and diligence on the part of corporate directors -- who are charged with monitoring managers -- and the professionalism of those upon whose advice directors need to rely in carrying out their role. These events present a challenge for all of us to avoid overreacting, and to limit our interventions to fine-tuning a system that usually works well.

The Current Problem

I will focus today on what I consider the core of the current problem: The incentives and disincentives that can drive managers and boards and those who advise them to push to the limit, and sometimes beyond, the numbers that are meant to reflect the company's financial performance and health. We should seek incentives and disincentives that are more carefully attuned to pressures in the current environment.

I wish we could solve today's problems by urging all participants in our market system, and particularly in our corporate governance system, to act moderately and prudently, fairly and ethically. If all did so, corrective action would not be necessary. As Oliver Wendell Holmes recognized, however, humans can not be expected to act moderately, prudently, morally and ethically at all times.[1] He noted that law and regulation generally, therefore, must address, by providing countervailing incentives and disincentives, the prospect that self-interest may lead persons to act "badly." This applies to corporate governance regulation as well. Self-interest -- which a market system relies heavily upon -- can interfere with the moral, ethical and legal obligations of directors and managers to protect and enhance the assets of the corporation that are committed to their care by, and for the benefit of, others.

An effective system of corporate governance must strive to channel the self-interest of managers, directors and the advisors upon whom they rely into alignment with the corporate, shareholder and public interest.

In the last decade, management has faced increased market pressures for short-term stock price performance and corresponding pressures to satisfy market expectations on a quarterly basis. This, coupled with increasing grants to senior executives of stock options and other incentives that are focused on short-term stock appreciation, may have created incentives that tipped the balance toward the promotion of self-interest rather than the protection and

[1] Oliver Wendell Holmes, "The Path of the Law," in The Path of the Law and its Influence: The Legacy of Oliver Wendell Holmes, Jr., 333, at 335 (Steven J. Burton, ed., 2000).

promotion of long-term shareholder value. As one of the country's leading compensation experts noted recently:

> "It is . . . possible that stock option grants have become so large at top management levels that they encourage high risks to reap high rewards. Perhaps the power of incentives to motivate is not linear. If stock options are good, are more stock options better? Once stock option grants have become sufficient in amount to provide the right balance between operational and market incentives, whatever that amount is, what is the purpose in granting more? Is it merely wasteful, or is it possible that it goes beyond waste to create perverse incentives that destabilize a company?"[2]

These concerns are magnified when the integrity of the independent auditors, financial and investment advisors and analysts, and lawyers upon whom directors, managers and the public rely for a fair picture of the company's performance and prospects, may also be skewed by self-interest.

In a general sense, these are not new concerns. The key issue in corporate governance regulation throughout the history of the joint-stock corporation, as recognized by Adam Smith in 1776, reiterated by Adolph Berle and Gardiner Means in 1932,[3] and repeated by numerous observers since, has focused on the "agency problem": It is a given that directors and managers are fallible human beings (like all of us). Therefore, they may not always subordinate their self-interests to the interests of those on whose behalf they are acting. And this is true of auditors, analysts and lawyers as well. This "agency problem" should be periodically reassessed to account for the circumstances of each era.

Over the past decade and a half, these issues have gained considerable attention as they relate to publicly traded corporations. In particular, added emphasis was given to the importance of board composition, as well as to increased transparency about corporate governance processes and structures. With respect to board composition, the theory is that a board of directors comprised of a majority of knowledgeable individuals who are not members of management and who lack business or family ties to management will be more likely to provide effective oversight of the managers, and circumscribe the "agency problem."

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[2] Frederick W. Cook & Co., Inc. Memorandum re: The Implications of "Enron" for Executive and Director Compensation at 2 (February 6, 2002) ("Frederick W. Cook Memorandum"). (A copy is attached as Exhibit A.)

[3] Adam Smith, An Inquiry into the Nature and Causes of the Wealth of Nations, Vol. II at 264-65 (E. Canaan edition, 1776); Adolph Berle & Gardiner Means, The Modern Corporation and Private Property, at 123 (1932).

A number of recommended corporate governance best practice guidelines have issued from various sources.[4] In addition, the tax code now provides tax incentives for certain performance-based compensation decisions when made by a committee of outside directors.[5] Notably, within the past two years, listing rules of the NYSE, AMEX and NASDAQ were amended to require that every listed company have an audit committee comprised of at least three independent members.[6] At the same time, SEC disclosure requirements were amended to require a significant amount of disclosure by audit committees, including disclosures about audit committee consideration of auditor independence.

We have had only one year of experience under the new listing and SEC rules, so it may be premature to determine whether these improvements have had the intended impact. Nonetheless, we should now dig down and address root causes of the problems that have arisen.

One matter that requires attention is, as noted above, the possible over-reliance on compensation devices for managers and directors that are unduly linked to short-term stock market price performance. This link may cause managers and directors to focus too heavily on their own self-interest in short-term stock appreciation. As long as the investing public focuses on short-term stock price performance rather than long-term growth -- and this is not something that will readily change (and analysts and bankers play a role here) -- we cannot expect corporate managers to be fully resistant to market pressures. This pressure is exacerbated when managers receive compensation that permits, and even induces, taking advantage of short-term rises in stock price.

The markets tend to pressure managers to "make the numbers," and self-interest compounds the problem. Boards and regulators need to keep this in mind. They can and should

[4] See National Association of Corporate Director ("NACD"), Report of the NACD Commission on Director Professionalism (1996, reissued 2001); The Business Roundtable, Statement on Corporate Governance (1997); American Federation of Labor and Congress of Industrial Organizations ("AFL-CIO"), Investing in Our Future: AFL-CIO Proxy Voting Guidelines (1997); California Public Employees; Retirement System ("CalPERS"), U.S. Corporate Governance -- Core Principles & Guidelines (Apr. 13, 1998); Teachers Insurance and Annuity Association -- College Retirement Equities Fund ("TIAA-CREF"), TIAA-CREF Policy Statement on Corporate Governance (2000); Counsel of Institutional Investors, Core Policies, General Principles, Positions & Explanatory Notes (2001). See also Organisation for Economic Cooperation and Development (OECD) Ad Hoc Task Force on Corporate Governance, OECD Principles of Corporate Governance (May 1999), *available at* www.oecd.org/daf/governance/ principles.htm (setting forth international principles of corporate governance.)

[5] I.R.C. § 162(m).

[6] See Order Approving Proposed Rule Change by the NYSE, Exchange Act Release No. 42233, File No. SR-NYSE-99-39; Order Approving Proposed Rule Change by the AMEX, Exchange Act Release No. 42232, File No. SR-Amex-99-38; Order Approving Proposed Rule Change by the NASD, Exchange Act Release No. 42331, File No. SR-NASD-99-48.

focus on creating countervailing incentives. This same concern extends to those advisors whom directors must rely on to carry out their crucial oversight role.

Another leading compensation expert predicts that boards are learning that heavily concentrating compensation on short term market priced incentives, rather than on "real" economic performance, is not good for the business -- and that boards will self-correct:

> "Re-balancing executive pay will be a major theme, as companies seek to reduce their reliance on the stock market and re-align their compensation programs to pay for "real" strategic and financial performance. There will be a new appreciation that successfully growing and running a business are of greatest value to shareholders in the long run, even if those efforts are not reflected in short-term stock price movement. This realization will result in some shift of compensation dollars from options to long-term incentives and to full-value stock grants earned on a performance basis."[7]

Even if this prediction about the developing trend in management compensation is accurate, in today's environment many may question whether this change will be broadly enough felt to deter future corporate governance failures without a push from regulators and/or legislators.

The Central Role of the Board in Controlling the "Agency Problem".

The board is the focal point of our corporate governance system. Pursuant to state statutes, it is elected by and accountable to the shareholders, and is charged generally with directing the affairs of the corporation.[8] The board fulfills its role by delegating managerial authority to the managers, which it hires, monitors incentivizes (compensates) and replaces when necessary. The board also is charged with oversight of the company's financial reporting and legal compliance. To do all this, it can -- and must -- reasonably rely on advice from professionals. Under our system, while management is responsible for maintaining the corporation's financial records and completing its financial reports, it is the outside auditors who provide assurance that the financial reports comply with generally accepted standards. The board selects the outside auditors and is charged with ensuring auditor independence necessary for attaining that assurance. The board also has available the advice of legal counsel to help assess the company's disclosure and other compliance obligations.

The board is not positioned to (and hence does not) manage, audit, practice law or render advice on the short- and long-term reactions of the market. Rather, it delegates to management, and then monitors the management and performance of the company, all on behalf

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[7] Pearl Meyer & Partners Memorandum re: Executive Pay Trends: Looking Forward and Back at 2 (February 2002) ("Pearl Meyer Memorandum") (A copy is attached as Exhibit B.)

[8] See e.g., DEL. GEN. CORP. LAW § 141 (CSC 2002).

of shareholders and the company.[9] In so doing, the board is entitled to reasonably rely on information and advice provided by managers, auditors, lawyers, bankers and others.

However, the board faces constraints in its monitoring ability that it must take into account related to pragmatics, capacity and context:

- Managers need flexibility to take the reasonable risks that are at the heart of entrepreneurialism; directors who constantly second-guess management's reasonable business judgments risk stifling management performance.

- Boards are comprised, increasingly, of directors who are not members of management, with good reason. However, this means that, as stated above, boards must place considerable reliance on managers for information about company affairs and performance and, therefore, there will always be some risk of both intentional malfeasance and unintentional failure going undetected at the board level for some period. This highlights the legal and practical importance of the reports that management (and professional advisors) make to boards. In the investigations now going on, sufficient attention should be given to this and to the consequences of inaccurate or misleading reports to directors.

- Much of what impacts company performance and can effect manager incentives may be outside the board's control, including the market's short-term focus and occasional "irrational exuberance."

The Committee on Audit Committee Effectiveness and Ensuing Reforms

Throughout the mid to late 1990s, the SEC expressed increasing concern about the integrity of financial reporting by publicly-traded corporations, fueled by a perception that corporate managers faced ever increasing pressures to match or exceed market analysts' expectations. The expressed concern was that this pressure would lead to increased corporate efforts to "manage" earnings -- to push the boundaries of Generally Accepted Accounting Principles in preparing the company's financial reports, and thereby obscure the true condition of the company. In 1998, the SEC encouraged the NYSE and the NASD to convene a private-sector Committee on Audit Committee Effectiveness to study the issues and make recommendations for encouraging greater financial reporting oversight by audit committees. I had the honor of co-chairing the committee with John Whitehead. (A copy of our Report and Recommendations (the "Report"), which includes a full list of committee members, is attached as Exhibit C.) Our Report contained ten recommendations, focusing on:

- Strengthening the independence of the audit committee;

- Improving audit committee operations; and

[9] See American Law Institute, Principles of Corporate Governance: Analysis and Recommendations § 3.02 (1994).

- Improving mechanisms for discussion and accountability among the audit committee, the outside auditors and management.

Our premise was that if boards and their auditors accepted a clear delineation of responsibilities for financial reports and the reporting process, and then acted diligently, the problem would self-correct. Our recommendations aimed to support a culture of integrity and independence. Soon after the Report was released, the vast majority of our recommendations were adopted. (They are attached hereto as Exhibit D.)

Audit committees of large publicly traded corporations appear to be abiding by the new rules. To the extent that corporate culture has been resistant to change at some companies, the current widespread concerns about auditor independence and the quality of financial reporting combined with media attention and the fear of shareholder litigation and reputational effect, are likely to shock audit committees into action. It may be premature to determine whether these improvements have yet had the intended impact. Nonetheless, it is appropriate to take a hard look at whether additional legislation, SEC regulation or listing rules could strengthen independence, provide more appropriate incentives and thereby help to restore investor confidence.

Significant legislative initiatives are already underway -- at last count, Westlaw listed over fifty pieces of Enron-related legislation.[10] In addition, the SEC has proposed certain disclosure-related reforms and is considering others. Recently, it asked the NYSE and NASD to review corporate governance listing requirements.[11] The suggestions that follow incorporate and build upon a number of suggestions advanced by others that I believe bear consideration:

Board Independence

Further and more serious consideration needs to be given to the issue of board independence, including the issue of independent board leadership. Providing objective judgement as to managerial performance, compensation, incentives and all other oversight matters is at the heart of what boards are supposed to do. Best practice recommends that, to ensure objective judgment in assessing management, boards of listed companies be comprised primarily of outside directors who in form and substance -- relationships, attitude and perspective -- are independent of management.[12] Attitude and perspective cannot be regulated, but conditions can be set to reduce the possibility that certain relationships between managers and directors will taint objectivity, and other conditions can be set to create an environment in which the right attitude and perspective is promoted. Other than the listing rules pertaining to audit

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[10] A complete list of proposed legislation is available from the Enron-bills database found at http://www.westlaw.com, searching the terms "House" or "Senate."

[11] See Press Release, Securities and Exchange Commission, Pitt Seeks Review of Corporate Governance, Conduct Codes (Feb. 13, 2002), *available at* http://www/sec/gov/news/press/2002.23.txt.

[12] See *supra* note 4.

committees (and certain tax incentives applicable to compensation committee decisions[13]), there is today no mandate regarding board independence and no widely applied definition of independence.

As to the issue of board leadership, we need to reconsider whether a corporate executive can adequately serve the board leadership function while heading up the management team that the board is charged with monitoring and incentivizing. Generally, managers disfavor separating the Chairman and CEO titles. In the U.S., the expectation among CEOs is that the culmination of a successful career includes the title of "Chairman and CEO." (Note, however, that this was the expectation in the U.K. as well, until the Cadbury Code -- and now the Combined Code -- recommended that two individuals hold the positions. Disclosure of the degree of compliance with these Codes was mandated by the listing rules of the London Stock Exchange. In the past decade, the practice of combining the titles -- and related expectations -- have changed significantly in the U.K., due solely to the pressure of this disclosure requirement.) Leading the board and leading the company are two very distinct and important jobs. Certain aspects of the board's leadership role -- those concerned with leading the review of management performance, including compensation, and potential management transactions with the corporation -- present a conflict of interest that makes it difficult, if not impossible, for a company executive to fulfill that role. Therefore:

- Boards of publicly traded corporations should be required (through listing standards) to include a majority -- I'd call for a substantial majority -- of "independent" directors under a strict definition of independence (ideally the same definition that applies to the audit committee, albeit with some refinement as described below).[14]

- The definition of director independence provided in listing rules (for audit committee purposes) should be reviewed to determine whether it adequately addresses all the relationships that may reasonably be expected to reduce independence. In particular, this review should consider relationships between directors and charities and educational institutions that receive significant grants from the corporation, and any

[13] I.R.C. § 162(m).

[14] The SEC has asked the listing bodies to review corporate governance requirements. Press Release, Securities and Exchange Commission, Pitt Seeks Review of Corporate Governance, Conduct Codes (Feb. 13, 2002), *available at* http://www/sec/gov/news/press/ 2002.23.txt. See also *The Fall of Enron: How Could It Have Happened?: Hearing Before the Senate Comm. on Governmental Affairs*, 107th Cong. (2002) [hereinafter *Governmental Affairs Hearings*] (statement of Arthur Levitt Jr., Former Chairman, Securities and Exchange Commission (1993-2000)), *available at* http://www.senate.gov/~gov_affairs/012402levitt.htm ("[S]tock exchanges, as a listing condition, should require at least a majority of the directors on company boards to meet a strict definition of independence). The current independence definitions applicable to the audit committees of listed companies can be found in the sources listed in Note 6.

consulting or other fee arrangements (other than regular compensation, within a usual range, for serving as a director) between directors and the corporation.[15]

- Boards of publicly traded corporations should be required (through listing standards) to constitute a compensation committee (much as they are currently required to have an audit committee) with entirely independent directors, using the strict definition of independence.

- Boards of publicly traded corporations should be encouraged through SEC disclosure requirements (or even required through listing requirements) to separate the position of CEO from that of board leadership. Board leadership should be provided by a non-executive director; one who is independent in all aspects. I would urge that this independent leadership be formalized in the position of Chairman, but title can be left to each board to decide.

- As a matter of best practice, independent directors and independent board committees -- including the audit committee and ideally the compensation and nominating/ governance committees -- should play a larger role in setting the "tone at the top." They should bear responsibility for company culture *vis-à-vis* financial reporting and "making the numbers," compensation and incentive decisions, management stockholding and trading policies, and policies concerning management transactions involving conflicts of interest.

- Although, the tone at the top cannot be mandated, the boards of listed companies should be required or encouraged (through SEC disclosure and listing requirements) to adopt, regularly review and disclose a corporate code of conduct that addresses conflicts of interest and management and director stockholding and trading policies. Clearly, the board should be responsible for overseeing its implementation and actions taken by boards to implement these policies should be disclosed, including any exceptions granted under the policies and the reasons therefore.

- It may be time to consider whether boards should be encouraged to rely on a small full time staff or regularly use outside advisors for support. Board work, for larger corporations, requires significant information, time and attention. For the board as a collective group of individuals who convene on a part-time basis to fulfill all that we expect may require more support than traditionally has been available. It may be fruitful for some staff resources to be explicitly devoted to supporting the work of the board. We should consider ways to encourage boards, or the independent directors as a group, to have available some staff and counsel resources of their own, distinct from staff and counsel hired by management, especially where potential conflicts with the interests of management are apparent (i.e., audit and compensation).

[15] Id.

Changes along the lines outlined above would encourage boards to be more vigilant and diligent in protecting shareholder value and in devising the best means to deal with the risk that self-interest will diverge from the corporate, shareholder and public interest.

In considering these and similar measures, one should keep in mind the variety within the universe of publicly held companies in the U.S., not to mention the tremendous variety among companies in the rest of the world who compete in what is rapidly becoming one global capital market. In a market economy, variety and diversity can be a source of strength. We should be careful that any norms that are established be flexible enough to accommodate this diversity. Experience with corporate governance listing standards in the United Kingdom and Canada, suggest that often a "comply or explain" regimen is sufficient to induce widespread adoption of recommended practices without undue restriction on diversity.[16] Specifically, under such a system, a company is required to publicly disclose whether it follows the normative, yet voluntary, standard and to explain the reasons for any non-compliance. This allows flexibility while still asserting reasonable pressure for compliance. It also provides investors significant amounts of information about the governance of companies, which can be used for investment and voting decisions. It may be time to consider what should be embedded in mandatory listing requirements and what should be encouraged through flexible "comply or explain" disclosure requirements. But more yet may be needed.

Compensation Issues – The Core

The growing practice of compensating managers with stock and stock option grants, which managers are then allowed to sell or exercise within a relatively short period of time -- and during their tenure at the company -- can, as noted above, create inappropriately short-term and stock-price focused incentives, and thereby exacerbate the agency problem in the context of a short-term oriented market. Performance compensation based on a snapshot of stock market performance at a single point in time chosen by the manager may not provide incentives for the kind of management activity that is "good" for the company and shareholders as a whole in the long run.

Over the past decade, companies have turned increasingly to stock-based compensation both as a form of pay-for-performance *and* as a means of aligning the self-interests of managers with the interests of shareholders. Indeed, I was among those who urged stock compensation as a method of aligning the interests of management (and directors) with shareholder interests. However, when managers are compensated with significant stock awards or stock options and are allowed to trade in that stock in the short-term (subject only to insider trading restrictions), their self interest in relatively short-term stock market fluctuations may conflict with their need to focus on both the long-term viability of the company and improvements in its long-term profitability. In particular, the focus on stock-based

[16] See London Stock Exchange Committee on Corporate Governance, The Combined Code: Principles of Good Governance and Code of Best Practice (July 1998), *available at* www.ecgn.org; Toronto Stock Exchange Committee on Corporate Governance in Canada, "Where Were The Directors?": Guidelines For Improved Corporate Governance in Canada (Dey Report) (December 1994), *available at* www.ecgn.org.

compensation, without conditions linking stock awards to realization by managers of long-term performance goals, may have put in place incentives that promote managerial self-interest to diverge from the corporate, shareholder and public interest. In some cases, such compensation may have crowded out other more traditional means of compensation that supported a longer term view, thereby producing an imbalance in incentive compensation that is especially counterproductive.

In 1996, Yale economist Paul W. MacAvoy and I co-authored a paper entitled "The Board of Directors in the American Corporate Form as the Instrument for More Effective Governance."[17] (A copy is attached as Exhibit E.) In it, we discussed the use of stock in pay-for-performance schemes and, in particular, the inappropriate incentives that linking such schemes solely to short term movements in stock price might create. We said:

> "stock [based compensation] plans should be further refined to motivate the managers to achieve longer term growth and to sharpen their concern for the value added from improved strategies. Stock grants can be programmatic, but with sales restrictions, or even postponement of sales until retirement, so as to focus incentives on the long term."[18]

Directors should seriously rethink stock-based compensation that creates short-term incentives to raise stock price rather than long-term incentives to improve performance and enhance value appreciation. It is with these concerns in mind that I recommend the following for consideration:

- Pay-for-performance programs should be linked to measures of profitability or economic value added rather than short-term changes in stock market valuation. In any event, they should be designed to consider company performance relative to peer group performance, and not simply generalized stock market performance. Although I have some reservations about the use of the tax laws to further corporate governance policy, consideration could be given to creating a stricter definition of what constitutes "performance based" compensation for purposes of Section 162(m) of the Internal Revenue Code.

- Mechanisms should be developed to encourage executives and directors to hold stock they receive, whether in the form of stock grants or stock options, for a significant period of time. Ideally, companies should restrict or discourage sale of company stock during a director's tenure and require or encourage significant holding periods for executives.[19] (Of course, some flexibility may be required for special

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[17] Paul W. MacAvoy & Ira M. Millstein, "The Board of Directors in the American Corporate Form as the Instrument for More Effective Governance," in The David Hume Institute: The First Decade (1996).

[18] Id at 7.

[19] Holding restrictions could apply to all stock received, or just apply to a high percentage (80 to 90 percent). See Cook, *supra* note 2, at 4 (discussing retention ratios in the context of company ownership guidelines or policies).

circumstances, for example, for start-ups that lack sufficient cash to pay executives what they are worth.) Again, while tax solutions pose concerns, consideration could be given to creating tax incentives designed to encourage executives to hold stock. Such incentives could include, for example, gradually reducing over some period of years the tax rate for grants of stock or exercise of options from the rate applicable to ordinary income to the most favorable rate for long-term capital gains. Alternatively, tax incentives could be created to encourage companies to contractually restrict the ability to transfer stock in grants of stock and stock options.

- Prompt disclosure of *all* transactions in the company's stock by corporate executives and directors should be required.[20] At the very minimum, the current rules that allow for once-a-year disclosure of sales of stock back to the company should be eliminated.

- Directors should be compensated fairly for the time necessary to fulfill their responsibilities. As a matter of best practice, however, stock options should be avoided altogether -- especially those exercisable within a short period. "The motivation of directors are and should be different from those of management. Directors are not strategic partners with management in creating value for shareholders; they are guardians of shareholders' interests." [21] And directors should be discouraged from selling stock in the company during their tenure.

These recommendations may seem a bit draconian, given what became the widely accepted compensation trend in the 1990's. However, before wide-spread use of such compensation devices, United States corporations and the economy succeeded -- and with considerable might -- by compensating high-performing managers with salaries, bonuses, and some long-term stock opportunities.

Conflicts of Interest

Transactions between the corporation and its managers, directors or large shareholders are rife with potential conflicts of interest. Most large publicly traded corporations

[20] See *Accounting and Investor Protection Issues Raised by Enron and Other Public Companies: Oversight Hearing Before the Senate Comm. on Banking, Hous., and Urban Affairs*, 107th Cong. (2002) [hereinafter *Banking, Hous. and Urban Affairs Hearings*] (statement of Richard C. Breeden, Former Chairman, Securities and Exchange Commission (1989-1993)), *available at* http://banking.senate.gov/02_02hrg/021202/ breeden.htm (suggesting that disclosure of all stock transactions by senior corporate executives be sped up); see also Legislative Solutions to Problems Raised by Events Relating to Enron Corporation Hearing Before the House Subcomm. on Capital Markets, Ins. and Gov't Sponsored Enter., 107th Cong. (2002) (statement of Harvey L. Pitt, Chairman, Securities and Exchange Commission), available at http://www.sec.gov/news/testimony/020402tshlp.htm ("One area of possible legislation already identified is the need to require corporate insiders to make public their trading activities more quickly than current law requires").

[21] Cook, *supra* note 2, at 6.

have codes of conduct for addressing such conflicts that recognize that some conflicts are inevitable. While that may be so, the corporate culture should view transactions that involve conflicts -- especially with members of senior management or directors -- as highly suspect, and to be avoided if at all possible. Therefore, as alluded to above:

- The boards of publicly-traded companies should be required or encouraged to adopt, regularly review and disclose a corporate code of conduct that addresses conflicts of interest, and management and director stockholding and trading policies. The actions taken by boards in implementing these policies should also be reported on, including disclosure of any exceptions granted under these policies and the reasons for the exceptions.

- SEC rules should be amended to mandate prompt disclosure of transactions between the corporation (or its affiliates) and members of senior management, directors or controlling shareholders.[22]

Professional Advisors

To obtain a fair picture of corporate performance and prospects, the shareholding public relies on managers and directors as well as on auditors, analysts, and those who advise the company, all of who are susceptible to self-interest. Appropriate incentives and disincentives are required to protect against self-interest from overcoming the professional responsibilities of auditors, analysts and lawyers.

Obtaining the appropriate balance in the relationship between the board, the auditor and management is key to audit integrity and both the auditors' and the board's ability to perform the role expected. Significant efforts to improve auditor independence were recently undertaken by the SEC, and it is not yet clear whether the intended outcome is being fully realized. In particular, as noted above, it is only within the last year that audit committees have been required to both determine and report on auditor independence. Nonetheless, numerous recommendations for additional reforms have already been floated. They range from bright line prohibitions, for example, absolute limitations on the provision of non-audit services to audit clients and requirements for auditor rotation, to more judgement based approaches.[23] While

[22] See Press Release, Securities and Exchange Commission, SEC To Propose New Corporate Disclosure Rules (Feb. 13, 2002), *available at* http://www/sec/gov/news/press/2002.22.txt (announcing that the SEC will propose rules that will "provide accelerated reporting by companies of transactions by company insiders in company securities including transactions with the company").

[23] See *Banking, Hous., and Urban Affairs Hearings, supra* note 20 (Statement of Richard C. Breeden) ("One means of insulating the audit firms from the pressure of keeping the audit engagement would be to provide for mandatory limits on audit engagements to a specified period of time, such as 5-7 years."); *Governmental Affairs Hearings, supra* note 14 (Statement of Arthur Levitt, Jr.) ("I also propose that serious consideration by given to requiring companies to change their audit firm – not just the partners – every 5-7 years to ensure that fresh and skeptical eyes are always looking at the numbers."); *Banking, Hous., and Urban Affairs Hearings, supra*

bright line approaches are attractive because of the certainty they create, careful consideration needs to be given to the potential for unintended consequences.

- Consider whether instead of asking the audit committee simply to review the possibility of conflicting relationships after the fact, it might be preferable to ask the audit committee to start with the decided presumption that audit and consulting don't mix. (The industry is already considering eliminating the mix, voluntarily.) Then, leave it to the audit committee to decide on creating an exception when it deems an exception necessary and desirable for the company and its shareholders.

Analysts and investment bankers also have potential conflicts of interest. The NASD has proposed changes to the rules for addressing conflicts of interest that arise when analysts are employees of investment banking or other firms having business relationships with, or who themselves own securities of, the company involved. Among other things, the proposal would mandate increased disclosure of conflicts in analyst reports and prohibit the investment banking arm from supervising or controlling research analysts or approving analyst reports. It would also prohibit approval of analyst reports by the subject company, prohibit a link between analyst compensation and specific investment banking transactions, and require disclosure in analyst reports if analyst compensation is based in part on investment banking revenues.[24] Some observers may prefer bright line prohibitions against analyst coverage of any stock in which the analyst has an ownership interest or in which the analysts' firm is engaged in a transaction.

I would be remiss if I did not discuss lawyers and their self interests. Lawyers play a critical role in both supporting the governance efforts of boards and assisting managers to structure transactions while abiding by legal requirements. A classic dilemma is posed, however. Lawyers often identify with the management team and view themselves as strategic partners in achieving the client's business goals. And they may well perceive that the more effective they are in helping to achieve management's goals, the more likely it is that they will receive additional business. Yet lawyers also are expected to provide professional judgment and counsel management about the legal boundaries and, in particular, to view their clients as more than just

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note 20 (statement of Harold M. Williams, Former Chairman, Securities and Exchange Commission (1977-1981)), *available at* http://banking.senate.gov/02_02hrg/021202/williams.htm ("I would urge the [Securities Exchange] Commission to consider a requirement that a public company retain its auditor for a fixed term..."); Harrison J. Goldin, Editorial, *Auditor Term Limits*, N.Y. TIMES, Feb. 1, 2002, at A25; *Banking, Hous., and Urban Affairs Hearings*, *supra* note 20 (statement of Roderick M. Hills, Former Chairman, Securities and Exchange Commission (1975-1977)), *available at* http://banking.senate.gov/02_02hrg/021202/hills.htm (stating that the "ultimate weakness" of the financial reporting system is that it "suffers from too many rules" and should be instead allow auditors to make their own judgements "drawn from a conceptual framework").

[24] National Ass'n Sec. Dealers, Inc., *Proposed Rule Regarding Research Analyst Conflicts of Interest*, File No. SR-NASD-2002-21, filed with Securities and Exchange Commission Feb. 7, 2002, *available at* www.nasdr.com/analyst_guide.htm; see also S. 1895, 107th Cong. (2002).

management, and to include the corporation and its shareholders. I would urge the American Bar Association to review ethical conduct rules and, in particular:

- Consider whether ethical conduct rules give lawyers sufficient guidance in balancing these roles; and
- Consider encouraging a set line of reporting for in-house counsel to bring to the board concerns not otherwise acted on by management.

I support SEC Chairman Pitt's recent call for both lawyers and accountants to "move away from wooden, rigid, literalism," and "adopt a bias in favor of the needs of the investing public."[25]

Conclusion

My suggestions can be boiled down simply to this: diligent independent directors, properly led, informed and assisted, can circumscribe the agency problems. If managers are not overly motivated by options to seek short-term market price appreciation, they should be less likely to -- consciously or unconsciously -- push the numbers, push their auditor and push the analysts. (Other compensation means are available to handsomely reward managers for true performance successes.) If auditors, analysts and lawyers remove the conflicts that stand in the way of the true professionalism the public expects, they are more likely to resist.

As I said at the outset, the great strength of our system is its ability to correct -- sometimes by self-correction, sometimes with assistance from the SROs, the SEC, the legislative bodies both state and federal, and the courts. If self-correction by the private sector will not suffice (and in many respects it does not appear likely to fully address the current concerns), then look to the listing bodies and their contractual power to bind listed companies, together with greater SEC disclosure requirements. When that won't suffice, look to legislative solutions. We must remember, however, as recently well-put by the Financial Times, that "no set of regulations, no matter how detailed, can outmanoeuvre a really determined manipulator. . . ."[26] The great conundrum is that notwithstanding all our efforts for corrections, ultimately, to considerable degree, we are left to rely on the integrity of individuals.

Ira M. Millstein

[25] Public Statement by SEC Chairman Harvey L. Pitt at the SEC Speakers Conference, Washington, DC, February 22, 2002.

[26] "Reforms to Restore Confidence in Business," Financial Times, February 19, 2002, at 14.

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August 1, 2002

The Honorable Carl Levin
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on Investigations of the Committee on
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United States Senate
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The Honorable Susan Collins
Ranking Subcommittee Minority Member
United States Senate
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Re: PSI Report No. 107-70: "The Role of the Enron Board of Directors In Enron's Collapse"

Dear Senators Levin and Collins:

On July 7, 2002, the Permanent Subcommittee on Investigations of the Senate Committee on Governmental Affairs ("PSI") released its Report, entitled "The Role of the Board of Directors in Enron's Collapse" (the "PSI Report" or "Report"). The PSI made a copy of the Report available to the former outside directors[1] at the same time the Report was released to the media and less than 48 hours before it was made public. This gave the Directors little time to analyze and prepare a response to the PSI Report before it was publicly available. Accordingly, on behalf of the former outside directors of the Board of Enron Corporation, I respectfully submit this response (the "Directors' Response" or "Response") to the PSI Report and request that it be included as part of the permanent record of the PSI and Senate Committee on the Governmental Affairs and be made publicly available.

The Directors believe that the PSI Report contains erroneous conclusions concerning the Enron Board's role in and responsibility for Enron's downfall. The Directors also believe that the PSI Report does not fully describe or accurately characterize their explanations for what occurred. The Directors submit this Response in an effort to provide evidence – all of which was available to PSI – that more accurately depicts what the Directors knew and did as board members. This includes evidence from

[1] The terms "outside director(s)" or "Director(s)," as used in this submission, refer to the following former outside directors of Enron Corp: Robert Belfer, Norman Blake, Ronnie Chan, John Duncan, Joseph Foy, Wendy Gramm, Robert Jaedicke, Charles LeMaistre, John Mendelsohn, Jerome Meyer, Paulo Ferraz Pereira, Frank Savage, Charls Walker, John Wakeham, and Herbert Winokur, Jr.

U.S. Senate Permanent Subcommittee on Investigations
EXHIBIT #85

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their Board and committee meetings that establishes that the Directors did not fail in their fiduciary responsibility to Enron's shareholders.

Fairness to the integrity of this process warrants the Directors' Response. The PSI has chosen to file its Report while the more traditional methods of fact finding are in their early stages. The plaintiffs in the Enron-related civil litigation have requested that the Court take judicial notice of the PSI Report. Without this response, the Directors are concerned that the errors in the PSI Report will go uncorrected and become ultimately unyielding to the blows of the truth.

Very truly yours,

W. Neil Eggelston

W. Neil Eggelston

THE OUTSIDE DIRECTORS' RESPONSE TO THE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS OF THE SENATE GOVERNMENTAL AFFAIRS COMMITTEE REPORT: "THE ROLE OF THE BOARD OF DIRECTORS IN ENRON'S COLLAPSE"

W. Neil Eggleston
Dimitri J. Nionakis
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August 1, 2002

EXECUTIVE SUMMARY

The Report of the Permanent Subcommittee on Investigations of the Senate Governmental Affairs Committee, entitled "The Role of the Board of Directors in Enron's Collapse," unfairly accuses the Board of a fiduciary failure. Enron's outside directors reject that accusation. These outside directors were independent, diligent, and in good faith and prudently performed their fiduciary duties based on the information provided to them.

- **The outside directors prudently executed their fiduciary duties to Enron shareholders.**

The Directors – as with any outside directors – needed reliable, complete information to execute their duties. They acted prudently, reasonably, and in good faith on the basis of the information that Enron management and outside advisors, including Arthur Andersen, provided to them. At the time, the Directors had no reason to suspect that Enron management or the company's advisors were withholding or distorting important information. As the PSI Report acknowledges, the Directors were misled and important information was withheld from them.

The Directors' reliance on internal and external advisors was necessary because the role of an outside director is limited by design. If outside directors were full-time employees and actively managed a corporation's day-to-day affairs, they would no longer be independent. In recognition of this limited role, the law fully authorizes and expects outside directors to rely on representations made to them by management and their outside experts. The Directors believe that if they had been provided with accurate information they requested or would have expected to receive from management, employees or advisors, this tragedy could have been avoided.

The PSI Report bases its conclusions on six factors that it contends demonstrate fiduciary failure. Each of these supposed factors rests on a skewed view of the facts or inappropriate conclusions.[2]

- **The Directors were not told that Enron was engaged in "high-risk" accounting practices that "push[ed] limits" or were "'at the edge' of acceptable practice."**

The Report's conclusion that the outside directors were told that Enron was engaged in "high-risk" accounting practices that "push[ed] limits," or were "'at the edge' of acceptable practice" (Report at 17-18) finds no legitimate support in the record. This conclusion is contradicted by the testimony of David Duncan and the documentary record in this matter.

  - David Duncan publicly testified that "high-risk" meant that the client "had a very complex business model, engaged in very complex transactions with difficult . . . areas to reach accounting

[2] The Directors have tried to respond to the Report's allegations, which are largely supported by undisclosed materials, unidentified witness statements, and hearsay. The Directors do not have access to the documents and witness statements upon which the PSI relied, nor to information in the hands of the people who have asserted their Fifth Amendment rights.

conclusions and that [Arthur Andersen] had a large amount of business with them." (*United States v. Arthur Andersen, LLP*, Criminal Action No. H-02-0121, Testimony of David Duncan, Trial Transcript at 2283-84 (S.D. Tex. 2002) ("Duncan *Andersen* Trial Testimony"). David Duncan testified that, out of about 3,000 publicly traded companies that were Andersen clients as of 2001, Andersen categorized "several hundred" as "high-risk." (*Id.* at 2285). David Duncan's testimony makes clear that "high-risk" did not mean Enron's accounting practices "push[ed] limits" or were "'at the edge' of acceptable practice."

- The Arthur Andersen documents on which the Report relies do not in fact state that the company was engaged in high risk accounting practices that "push[ed] the limits" and were "'at the edge' of acceptable practice." (*Id.*) Rather, as discussed below, that is an inference that the PSI drew based on the self-serving statements of outside counsel for Arthur Andersen and Arthur Andersen employees about an Arthur Andersen employee's handwritten notation that was not shown or communicated to any Director.

- In the hundreds of pages of minutes of the Audit Committee meetings, which Arthur Andersen presumably reviewed, and Arthur Andersen presentations (prior to the Fall 2001 earnings correction), there is not a single occasion on which the Audit Committee was informed that Enron was engaged in high risk accounting practices that were inappropriate, "push[ed] the limits" and were "'at the edge' of acceptable practice" (*id.*); to the contrary, in meeting after meeting, and in its formal representations in the Enron Annual Reports, Arthur Andersen continually assured the Audit Committee and the shareholders that it was comfortable with the complex accounting judgments being made and would stand behind them. Even now, David Duncan, the former Arthur Andersen partner on the Enron engagement, at his recent trial gave sworn public testimony that he was "not aware of any accounting improprieties at Enron." (Duncan *Andersen* Trial Testimony at 2020).

The Audit Committee knew that Arthur Andersen was paid specifically to ensure that the "innovative structures" conformed to GAAP, and hence took comfort that Arthur Andersen "was o.k." with them.

The Report cites three sources as support for its conclusion regarding the Directors' knowledge that Enron was engaged in high-risk accounting practices. None is reliable evidence of the Directors' knowledge:

- statements to PSI by outside attorneys for the now convicted Arthur Andersen, which faces exposure for its role in this matter and which is seeking to shift the blame;

- statements to PSI by outside counsel for Arthur Andersen employees who are also seeking to shift the blame and who refused to meet with the PSI because they asserted their Fifth Amendment right not to make statements that may incriminate themselves; and,

- internal Arthur Andersen memoranda discussing the accounting firm's discomfort over Enron's accounting practices – documents and concerns that should have been, but were not, raised in the strongest terms with the Audit Committee.

The Report's conclusion that the Directors knew that Enron was engaged in high risk accounting practices that "pushed limits" or were "at the edge" of acceptable practice (Report at 17-18) should not have been made.

- **The Directors' decision to approve the Chief Financial Officer's operation of the LJM partnerships was prudent in light of the strict controls the Board imposed, which would have been effective if management had implemented the controls and provided accurate information to the Board about the LJM transactions.**

The Report accuses the Directors of approving the CFO's participation in the LJM partnerships in the face of conflicts of interest. (Report at 3). It also alleges that the "Board exercised inadequate oversight of [the] LJM transaction and compensation controls and failed to protect Enron shareholders from unfair dealing." (*Id.*) These findings ignore the clear evidence to the contrary. The Directors' ratification of the Office of the Chairman's decision to permit the Chief Financial Officer to establish and operate the LJM partnerships was based on the Directors' belief, after reviewing management's recommendation and receiving assurances from outside advisors about accounting for and control of these partnerships, that the partnerships were in the best interests of Enron and were designed to meet specific and important business purposes. The Directors understood at the time that Enron's inside and outside accountants and legal advisors had reviewed and approved the arrangement.

Under the Code of Conduct, the CFO's involvement in these partnerships required proper oversight by Enron management. The Directors certainly recognized that the CFO's participation in these arrangements presented conflict issues that needed to be addressed and managed. The Board understood that Enron's legal advisors had reviewed and approved of the LJM partnership structure, and had approved of Mr. Fastow's involvement in LJM as long as the Board ratified the Office of the Chairman's recommendation to allow Mr. Fastow to participate consistent with the Code of Conduct. As an additional "line of defense," the Board imposed a series of independent controls specifically assigned to numerous officers in the company who did not report to the CFO, including the CEO, COO, and the Chief Accounting and Risk Officers, as well as Arthur Andersen, to ensure that every transaction between the partnerships and Enron would be in the best interests of Enron. Arthur Andersen and Enron management assured the

Board that the controls had been implemented and were effective, and the Directors had no reason to doubt those representations. At the February 12, 2001 Finance Committee meeting, Mr. Fastow reported that the controls "had been discussed with the Audit and Compliance Committee, and commented that the process was working effectively." (February 12, 2001 Finance Committee meeting minutes at 5; *see also* February 12, 2001 Audit Committee meeting minutes at 2-3). We now know that the controls were not followed, and the Directors were deprived of critical information about these transactions.

- **The outside directors did not make decisions designed to misrepresent the true financial condition of Enron.**

The Report's contention that the Board permitted Enron to engage in extensive "off-the-books" transactions to distort Enron's financial picture and thereafter failed to ensure adequate disclosure misstates both what Enron did disclose and the role of the outside directors in reviewing disclosures.

The Report continually uses the inflammatory term, "off-the-books." The Report, however, does not clarify that "off-the-books" does not mean "undisclosed." What it means is that the disclosures were in a different place in the company's annual report than the section setting forth the balance sheet. When the Report refers to "off-the-books," what it really means is "off-balance-sheet," and disclosed in footnotes to the balance sheet.

The Report's principal example of an improper "off-the-books" corporate strategy is a partnership called Whitewing. The Report's characterization of the accounting treatment of Whitewing shows that preparers of the Report do not fully understand financial reporting. The Report acknowledges that from 1997 to 1999, Whitewing was a consolidated entity. That means that Whitewing was consolidated on the balance sheet of Enron; in the Report's terms, "on-the-books," not "off-the-books." In 1999, Whitewing was deconsolidated and treated as an affiliate. When that occurred, Whitewing's assets and liabilities were included in the footnotes to the balance sheet in the Annual Report, and a single line item was reported on the balance sheet itself. Though "off-the-books" under the Report's definition, Whitewing was not "undisclosed."

The Report's discussion of these issues shows that the accurate classification and reporting of financial statements requires compliance with numerous laws, regulations and accounting conventions. The Directors were entitled to and did rely on Enron's outside experts on these matters. The outside auditor, Arthur Andersen, had to give its opinion on the validity of the financial statements, and did so year after year. The Directors also understood that Enron's auditors, Arthur Andersen, and its outside law firm, Vinson & Elkins, had reviewed and approved the adequacy and completeness of Enron's disclosures. It is wrong to blame the Directors, who relied on what they believed at the time were two of the premier professional services firms in the world, for alleged inadequate disclosures.

- **The outside directors prudently approved compensation plans for Enron executives on the advice of outside experts to assure that the company would attract and retain what Enron believed was its most valuable asset, its people.**

The Report criticizes the Compensation Committee for approving executive compensation plans that had as their goal "keeping up with competitor pay." (PSI Report at 53). The Report acknowledges that the Compensation Committee regularly sought advice from Towers Perrin, a highly respected executive compensation consulting firm. Towers Perrin advised the Compensation Committee of the need to offer compensation packages that were comparable to those offered by similarly-situated companies and entities that recruited from the same talent pool.

The outside directors believed that attracting and retaining outstanding employees was critical to the success of the company. The Report seems to disparage the notion that pay packages comparable to opportunities that employees may obtain from other companies are necessary to this goal. Yet the Report cannot realistically contest, as one director testified at the hearing on May 7, 2002, that an employee who has better opportunities at another company would simply "walk across the street."

The criticism of the Compensation Committee for failing to supervise the Chief Executive Officer's use of his line of credit is also misplaced. At the time, a line of credit as part of CEO compensation was quite common. The Directors had no reason to believe that Mr. Lay would misuse the line of credit and were not aware until recently that he had done so. The Directors agree that, by repeatedly using the line of credit to take out a loan and then immediately repaying it with stock, Mr. Lay was abusing this component of his compensation package. Dipping into the line of credit in the morning and repaying it with stock in the afternoon many times over was a violation of the Board's intention when it approved this benefit. Some of the Directors have been publicly explicit in this regard. (May 7, 2002 PSI Hearing Transcript at 219-21).

The Directors certainly would have expected Mr. Lay's conduct to have been brought to their attention by the employees, including those in legal, treasury, and control functions, who facilitated these sales. Every employee of Enron, including the CEO, had a fiduciary duty to the company as a whole.

- **The outside directors of the Board were independent of Enron. The Directors also believed that Arthur Andersen was independent of Enron. The outside directors exercised independent judgment about these matters.**

The Report contends that the Directors were too highly compensated. A contemporaneous independent study shows that the Directors' compensation was not excessive for a company of the size and complexity of Enron.

The Report also criticizes certain outside directors for having inappropriate financial ties to the company and alleges that the Board was not independent. Those ties were trivial, had no impact on the Directors' discharge of their duties, and did not affect the Board's independence.

The Chairs of the three most significant board committees did not receive any monies from Enron in addition to their director/committee chair compensation. Mr. John Duncan, who chaired the Executive Committee, and Dr. Jaedicke, who chaired the Audit Committee, do not appear on the Report's list at all. (PSI Report at 55-56). Mr. Winokur, who chaired the Finance Committee, appears only because he is an outside director and shareholder of a company that occasionally sold oilfield equipment to subsidiaries of Enron in the ordinary course of business, on arms'-length terms. Those sales averaged approximately one-half of 1% of the annual revenues of that company.

Board members Dr. Mendelsohn and Dr. LeMaistre are the current and immediate past Presidents of the Houston-based M.D. Anderson Cancer Center ("the Center"), unquestionably one of the premier cancer centers in the world. During Dr. LeMaistre's tenure as President, Enron pledged $1.5 million as part of the Center's capital campaign. This amount is less than 1% of the total amount of money that the campaign raised from private sources and the Center staff. While Dr. Mendelsohn was an Enron director, the total Enron- and Lay-related contributions comprised less than 0.1% of the private philanthropy raised by the Center during that period.

The relationship between the Enron contributions to the Mercatus Center at George Mason University, which employs former board member Dr. Gramm, is just as tenuous. Enron first contributed to the Mercatus Center before Dr. Gramm was employed there; since 1996, Enron's total contributions have been less than one-third of 1% of the Mercatus Center's budget. Finally, Lord Wakeham received a $6,000 monthly retainer fee for the additional duties he performed in connection with Enron's European business and operations. The Board specifically was asked to and did take note of these facts and found Lord Wakeham independent.

The criticism of the Audit Committee for permitting Arthur Andersen to perform consulting services in addition to audit services for the company represents a condemnation of a widespread business practice, not a criticism of this Board. The members of the PSI may believe this practice should not be permitted. At the time, however, Enron and hundreds of other companies believed that companies could obtain more effective service if the work was centralized in one accounting firm.

The Directors do not accept the conclusion of the Report that they failed in their oversight duties. The two most significant conclusions of the Report are barely discussed. The Report (1) did not find that the outside Directors benefited personally from these transactions or that they acted in other than the utmost good faith, and (2) did find that the Directors were misled by people on whom they were entitled to rely.

The Directors particularly reject the suggestion in the Report that their culpability is demonstrated by their failure to acknowledge their responsibility. These directors executed their fiduciary duties prudently, responsibly, and in good faith.

SCOPE OF RESPONSE

The Directors' Response addresses many of the most significant inaccurate findings the PSI Report makes about the role of the Directors. This Response is not intended to address all of the Report's inaccuracies. The PSI investigative process did not allow for the PSI's information (documents or access to witnesses) to be provided to the Directors. The Directors' ability to respond to findings that rest on undisclosed documents and testimony is necessarily limited.

Due to time constraints, this Response also does not address certain issues that the PSI has raised, such as the Sherron Watkins memo and certain transactions. The Directors have addressed these issues in lengthy public testimony and written statements.

We make these observations so that the severe limitations on the ability of the Directors to respond to the PSI Report will be apparent to any readers of this response. With those limitations in mind, we will endeavor to highlight some of the critical misstatements and unfounded conclusions contained in the PSI Report.

I. THE DIRECTORS FULLY EXECUTED THEIR OVERSIGHT DUTIES

The PSI Report opens with observations about the structure and operation of the Enron Board, as well as with a description of its views of the duties of outside directors In significant ways, these descriptions are misleading.

The PSI Report seeks to paint a picture of a Board lacking in diligence through a description of the length and tenor of the Board meetings. The picture is misdrawn. First, the PSI Report suggests that the Board meetings lasted only a couple of hours each.[3] The Board minutes produced to the PSI establish, however, that regular board meetings occurred five times per year and lasted five to six hours. Each Board meeting was preceded by a day of committee meetings, in which extensive discussions were held with management – and in the case of the Audit Committee, with Arthur Andersen – concerning the company's business, its financial affairs and its strategy The Audit and Finance Committees members received voluminous materials before meetings that they studied to prepare for their discussions.

The PSI Report also asserts that the Board "readily approved new business ventures and complex transactions." The Board and committee minutes again belie this contention. The Board or its committees declined to approve at least two major acquisitions suggested by management prior to 2001 and the Georgia Pacific pulp mills in 2001. Messrs. Lay and McMahon recommended the Georgia Pacific acquisition in September/October 2001 which was a clear indication to the Directors that management thought that Enron was in sound financial condition.

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[3] *Compare, e.g.,* Minutes of December 8, 1998 (meeting lasted over five hours); Minutes of December 8, 1998 (meeting lasted over five hours); Minutes of February 8, 1999 (meeting lasted over six hours); Minutes of October 11-12, 1999 (meeting lasted six and one-half hours over two days); Minutes of February 8, 2000 (meeting lasted over five and a half hours) *with* Subcommittee Report at 9 ("Full Board meetings also generally lasted between one and two hours.")

A review of the relevant facts demonstrates that the Enron Board met all of the requirements of the Blue Ribbon Committee on Improving the Effectiveness of Audit Committees cited in the Report. Throughout 2000 and into 2001, the Audit Committee worked with Arthur Andersen to make certain that it complied with the recommendations of the Blue Ribbon Committee. That effort culminated in February 2001, when the Audit Committee finalized a new charter, which the Board approved.

Enron's Board – were it presently constituted as it was in 2001 – would meet the new requirements proposed by the New York Stock Exchange. The Audit Committee met the Blue Ribbon Committee's recommendations. Its charter stated that the committee shall be comprised of three or more directors who, in the opinion of the board of directors, have no relationship to the company that may interfere with the exercise of independent judgment as a committee member. And this was the case. The Enron Board deemed all members of the Audit Committee independent.

A. Directors are Entitled to Rely in Good Faith on the Opinions and Advice of their Internal and Outside Advisors

The PSI Report asserts that Enron's Board exercised "weak oversight" of Enron's operations, PSI Report at 14, and "routinely relied on Enron management and Andersen representations with little or no effort to verify the information provided. . . ." *Id.* These statements are legally and factually inaccurate.

Governing law makes clear that it is entirely appropriate and expected for directors to rely on statements made to them by management or the company's outside auditors. Oregon law[4] states expressly that a director "is entitled to rely on information, opinions, reports or statements including financial statements and other financial data if prepared or presented by:

(a) One or more officers or employees of the corporation whom the director reasonably believes to be reliable and competent in the matters presented;

(b) Legal counsel, public accountants or other persons as to matters the director reasonably believes are within the person's professional or expert competence; or

(c) A committee of the Board of Directors of which the director is not a member if the director reasonably believes the committee merits confidence."

2001 Or. Rev. Stat. 60.357(2)(a)-(c). The Report offers no reason for the Directors at the time to have questioned the honesty or integrity of Enron management or Arthur Andersen. The corporate world and the press had lauded both groups as having extraordinary ability. Before the Fall of 2001, the Directors had no reason to doubt that characterization.

The Report acknowledges grudgingly that the Directors were misled. (PSI Report at 13). The Report fails to acknowledge the degree, frequency, and magnitude of this misconduct. An objective review of the information that has become publicly available discloses that Enron

[4] Enron was an Oregon corporation.

management repeatedly failed to apprise the Directors of the facts on many key transactions. As for Arthur Andersen, the Report discusses internal Arthur Andersen memoranda detailing Arthur Anderson's discomfort with Enron's accounting practices. (*Id.* at 18-19). The Report fails to note, however, that Arthur Andersen failed to bring those concerns to the Directors' attention.

The courts of Delaware, which are regularly called upon to discuss the duties of corporate directors, have made clear that the touchstone of any evaluation of a director's action is an assessment of the director's good faith:

> [C]ompliance with a director's duty of care can never appropriately be judicially determined by reference to the content of the Board decision that leads to a corporate loss, apart from consideration of the good faith *or* rationality of the process employed. That is, whether a judge or jury considering the matter after the fact, believes a decision substantively wrong, or degrees of wrong extending through "stupid" to "egregious" or "irrational," provides no ground for director liability, so long as the court determines that the process employed was either rational or employed in a good faith effort to advance corporate interests. To employ a different rule – one that permitted an "objective" evaluation of the decision – would expose directors to substantive second guessing by ill-equipped judges or juries, which would, in the long run, be injurious to investor interests. . . .
>
> Where a director *in fact exercises a good faith effort to be informed and to exercise appropriate judgment*, he or she should be deemed to satisfy fully the duty of attention.

In re Caremark Int'l. Inc. Derivative Litig., 698 A.2d 959, 967-68 (Del. Ch. 1996) ("*In re Caremark*") (emphasis in original).

This legal background is important for two reasons. First, it establishes that, contrary to the PSI's contentions, the Directors were entitled to rely, in good faith, upon the advice and recommendations of Enron's management and outside advisors, all of whom, at the time, were reasonably believed to be reliable and competent. Second, the law points out that the proper inquiry is not whether the PSI, with the benefit of hindsight, agrees with the decisions made by the Directors. Rather, the inquiry is "Did the Directors employ a reasonable process to inform themselves sufficiently concerning these transactions and were their decisions made in good faith?" The answer to that question, based upon the publicly available record of Board and committee meetings, is plainly "yes."

B. The Board Instituted Sufficient Mechanisms To Ensure That It Would Get The Information It Needed To Fulfill Its Duties

The Report nevertheless attacks the means by which the Board sought to remain informed of Enron's affairs. The law is clear that the ability of outside directors to inform themselves is limited:

> By force of necessity, the company's Directors could not know personally all of the company's employees. The very magnitude of the enterprise required them to confine their control to the broad policy decisions. That they did this is clear from the record. At the meetings of the Board in which all Directors participated, these questions were considered and decided on the basis of summaries, reports and corporate records. These they were entitled to rely on, not only, we think, under general principles of common law, but [by statute] as well, which in terms fully protects a director who relies on such in the performance of his duties.

Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (Del. Ch. 1963). The Directors' role was limited to putting in place a process by which information would come to their attention so that they could – as they did here – act on it in good faith. "[I]t is important that the Board exercise a good faith judgment that the corporation's information and reporting system is in concept and design adequate to assure the Board that appropriate information will come to its attention in a timely manner as a matter of ordinary operations, so that it may satisfy its responsibility." *In re Caremark*, 698 A.2d at 970.

In testimony before the House Financial Services Committee, and in their testimony before the PSI, Mr. Winokur and Dr. Jaedicke set out in detail the many overlapping and independent controls that the Board instituted. We refer the reader to that publicly available testimony for a full description of those controls. (*See* http://www.senate.gov/~gov_affairs/050702witness.htm; http://energycommerce.house.gov/107/hearings/02072002Hearing485/hearing.htm.) Arthur Andersen was an important part of that control function. Arthur Andersen, as the PSI Report notes, did not act solely as Enron's external auditor for the purpose of auditing Enron's financial statements. Arthur Andersen also provided important transaction accounting and disclosure advice and gave opinions regarding the adequacy of Enron's internal controls. In the 2000 Annual Report, for example, Andersen opined to the Audit Committee and to Enron's public shareholders that:

- "[Enron's] financial statements... present fairly, in all material respects, the financial position of Enron Corp. and [its] subsidiaries...and the results of their operations, cash flows and changes in shareholders' equity for each of the three years in the period ended December 31, 2000, in conformity with accounting principles generally accepted in the United States."
- "We have examined management's assertion that the system of internal control of Enron Corp. and subsidiaries ...was adequate to provide reasonable assurance as to the reliability of financial statements and the protection of assets from unauthorized

> acquisition, use or disposition....In our opinion, management's assertion that the system of internal control of Enron Corp. and its subsidiaries as of December 31, 2000, 1999 and 1998 was adequate to provide reasonable assurance as to the reliability of financial statements and the protection of assets from unauthorized acquisition, use or disposition is fairly stated, in all material respects, based upon current standards of control criteria."

See Enron Annual Report for 2000 at 30. Arthur Andersen's opinion that Enron's internal controls were adequate encompasses the critical years 1999 and 2000.

The PSI Report suggests that Enron's Audit Committee was unreasonable in relying upon Arthur Andersen's opinions and did not "verify the information provided." This assertion misunderstands the role of an audit committee, which is to receive reports from management and the outside auditors, to review the adequacy of management and the outside auditors, to review the adequacy of internal controls, and to oversee the filing of financial statements. "The audit committee is not the auditor's auditor. The audit committee should be an oversight body....But there is no guarantee and you do have to trust someone." *See* Testimony of Olivia Kirtley before Senate Banking Committee (March 14, 2002).

A series of commentators more authoritative than those who appeared before the PSI have noted the limited role of an audit committee. Alan Greenspan, the Chairman of the Federal Reserve, has acknowledged the important limitations of an audit committee member's role: "I've served on too many audit committees to know that even though I would consider myself independent, I would consider myself knowledgeable, I did not know what questions to ask the chief financial officer during meetings to find out what it is that conceivably is going wrong with the corporation and he wasn't about to tell me." (Hearing of the House Financial Services Committee (February 27, 2002)). The prestigious Audit Committee of Goldman Sachs has made this point quite strongly:

> The members of the Audit Committee are not professionally engaged in the practice of auditing or accounting and are not experts in the fields of accounting or auditing, including in respect of auditor independence. Members of the Committee rely without independent verification on the information provided to them and on the representations made by management and the independent auditors. Accordingly, the Audit Committee's oversight does not provide an independent basis to determine that management has maintained appropriate accounting and financial reporting principles or appropriate internal controls and procedures designed to assure compliance with accounting standards and applicable laws and regulations.

(2001 Goldman Sachs Proxy Statement at 19).

As Securities and Exchange Commission Chairman Pitt has testified, once appropriate processes are in place (as they were here), a director cannot protect the shareholders against dishonest management:

> I will also tell you that no matter what the expertise is, at the end of the day, if management is going to play games, no matter how determined, how smart, and how experienced the audit committee is, they're not going to find it. The best you can hope for is to have a process.

(Testimony of the Honorable Harvey L. Pitt, Chairman of the U.S. Securities and Exchange Commission, before the Senate Committee on Banking, Housing and Urban Affairs on March 21, 2002).

The Enron Audit Committee met five times per year and was chaired by a former Professor of Accounting and Dean of the Stanford Business School, Dr. Robert Jaedicke. The PSI Report acknowledges that the Audit Committee met the standards for financial literacy set out by the Blue Ribbon Committee. The PSI Report appears to concede that there were extensive qualitative discussions between Arthur Andersen and the Audit Committee concerning Enron's accounting, its financial affairs and its business risks. (*See, e.g.,* Report at 15).

The processes and controls that Enron's Board put in place to ensure that it received accurate information about Enron's financial condition generally and about the related-party transactions in particular were extensive and independent. If one control failed, another independent control was designed to bring particular issues to the Board's attention. Arthur Andersen, as indicated above, and Enron management were directed by the Directors to perform important internal control and reporting functions. The Board could not have anticipated that each of these independent controls would fail.

II. THE EVIDENCE DOES NOT SUPPORT THE REPORT'S CONCLUSION THAT THE DIRECTORS KNOWINGLY ALLOWED ENRON TO ENGAGE IN "HIGH-RISK" ACCOUNTING PRACTICES THAT "PUSH[ED] LIMITS" OR WERE "'AT THE EDGE' OF ACCEPTABLE PRACTICE"

The PSI Report contends that Enron's Board "knowingly allowed" Enron's use of "high risk accounting practices" that "push[ed] limits" or were "'at the edge' of acceptable practice." (Report 17-18). While the Report characterizes this purported finding as "disturbing" (Report at 14), the PSI's conclusion is based upon a distortion of the evidence.

The Directors asserted during their staff interviews, and testified at the PSI hearing that no one advised any Director that Enron was engaged in "high-risk accounting practices" that "push[ed] limits" or that were "at edge of acceptable practice." Those statements are consistent with the contemporaneous Board and Committee minutes that recorded Arthur Andersen's discussions with and disclosures to the Enron Audit Committee.

The documents on which the Report relies contradict this conclusion. In one instance, the PSI Report infers that the categorization of certain transactions as "H" in the Andersen presentation materials means that the Audit Committee was informed that Enron was engaged in "high-risk accounting." Dr. Jaedicke, Enron Audit Committee Chairman, testified that he did not understand the document that way. (May 7, 2002 PSI Hearing Transcript (Federal News Service) at 26). The minutes of the meeting do not reflect any such statements by Arthur Andersen accountants.

The Report rejects the Directors' testimony in favor of a statement by an unnamed Arthur Andersen lawyer, who "told the Subcommittee staff" that this document was "intended" to inform the Audit Committee that Enron was using a number of high-risk accounting practices. This is a thin reed upon which to rest the weighty (and otherwise unsupported) assertion that the Board was told that Enron was engaged in high risk accounting practices. Even this thin reed collapses in the face of the following:

- The Andersen accountants who allegedly "intended" to impart this conclusion to the Audit Committee said no such thing in the actual document. Rather, the chart refers to the fact that these are matters of Andersen's professional judgment concerning the application of the relevant accounting rules. The document presented and meeting minutes do not establish that Andersen indicated any discomfort or doubt about the accuracy of the judgments it was making in the course of reporting on Enron's transactions.

- In the same meeting, Arthur Andersen advised the Audit Committee that, in Arthur Andersen's opinion, no modification was required in either management's judgments on accounting estimates or reviews of interim financial information. *See* Audit Committee Minutes of February 7, 1999 at 1-2.

- The Arthur Andersen accountants who, according to their criminal defense lawyers, intended to convey this conclusion were not available to testify. Both of the Andersen accountants invoked their Fifth Amendment rights and refused to testify because it might incriminate them.

The last point is especially important. The PSI Report obscures the inherent unreliability of the Andersen lawyer's statements by papering them over with the innocuous observation that "Mr. [David] Duncan did not make himself available in response to a Subcommittee request to elaborate on this note [but] his colleague Mr. Bauer confirmed through legal counsel that Mr. [David] Duncan had conveyed this information to the Audit Committee." *See* Report at 17.

David Duncan was "unavailable" because he had pleaded guilty to obstruction of justice and had invoked his Fifth Amendment rights. Mr. Bauer, his colleague, responded "through his legal counsel" because he too refused to testify because his testimony might incriminate him. The PSI's decision to credit the assertions of these lawyers about their clients' unavailable, potentially incriminating testimony is inappropriate.

David Duncan testified at the *Andersen* trial as to what Andersen meant by "high risk." This term did not indicate that Enron's accounting practices "push[ed] limits" or were "'at the edge' of acceptable practice":

Q: Well, Mr. Weissmann asked you, do you recall, about wasn't Enron a high risk client. Do you recall that?

A: (David Duncan): Yes.

Q: And were they?

A: Yes, they were.

Q: And what do you-all mean in your world by that?

A: They were a high risk client in that they engaged in – they were in a very complex – had a very complex business model, engaged in very complex transactions with difficult – difficult areas to reach accounting conclusions and that we had a large amount of business with them.

(Duncan *Andersen* Trial Testimony at 2283-84).

The classification "high-risk" did not suggest that these clients were engaged in inappropriate account practices and was applied to a large percentage of Arthur Andersen's audit clients:

Q: All right. Tell the jury about how many of your – first of all, do you have any knowledge yourself, Mr. Duncan, about how many publicly traded companies Enron – that Arthur Andersen was doing the accounting for as of 2001?

A: I want to say somewhere in the neighborhood of 3,000, but I'm relying on long-term memory.

Q: How many would you estimate were categorized by your company as high risk?

A: I don't know if I could make an intelligent estimate.

Q: Would it be more than hundreds? Would it be several hundred?

A: I would say several hundred.

(*Id.* at 2285).

The Report also ignores what occurred at the outset of the February 7, 1999 meeting. The minutes show that David Duncan began his presentation by noting that "Arthur Andersen would submit an unqualified financial statement opinion as a result of its 1998 audit and that there would be no significant audit adjustments or new accounting policies or changes." He added that, in Arthur Andersen's opinion, no modification was required in either management's judgments on accounting estimates or reviews of interim financial information. *See* Audit Committee Minutes of February 7, 1999 at 1-2. The very facts criticized by the Report – namely, the accounting judgments being made by Enron – were matters David Duncan said Andersen agreed with at the very moment that he assured the Audit Committee Enron's financials were correct. The Report ignored this critical evidence.

The Report ignores the ensuing discussion (in the same meeting) between Andersen accountants and the Enron Audit Committee in executive session. An executive session was available at every Audit Committee meeting and allowed the Committee and Arthur Andersen to meet in the absence of Enron management so that Arthur Andersen could raise any issues or concerns. If the Andersen partners who attended the February meeting – Messrs. Duncan, Goddard, King and Bauer – were concerned that Enron was "pushing limits," engaged in "aggressive accounting" or otherwise taking actions with which Arthur Andersen disagreed, this was the time to say so – but they said no such thing. To the contrary, the minutes reflect that "[d]uring the executive session, Mr. David Duncan indicated there were no areas of significant concern." (*Id.*)

Similar observations could be made about the other Audit Committee meetings the PSI Report cites. Nowhere in any of the Audit Committee minutes is there any indication that Arthur Andersen informed the Audit Committee that Enron's accounting was "pushing limits," was "high risk," or was inconsistent with generally accepted accounting principles. In stark contrast, each and every year Arthur Andersen expressed three important opinions to the public and to Enron's Audit Committee about Enron's financials: Enron's financials presented fairly, in all material respects, the financial condition of the company; Enron's internal controls were adequate; and, Andersen had no disagreements with Enron management concerning its accounting practices. (*See*, *e.g.*, Enron 2000 Annual Report at 30 and Enron Form 10K for 2000 at 61-62).

It is also important to respond to the Report's selective citations from internal Arthur Andersen documents. (*See* Report at 18). The Directors have not seen the documents discussed at pages 18-19 of the Report, but wish to emphasize that Arthur Andersen did not inform the Directors that Enron was engaged in "form over substance transactions" or took "maximum risk." (*Id.*) As the PSI Report notes, Dr. Jaedicke testified that when Andersen was questioned in executive sessions about Enron's structured transactions or about the judgments Arthur Andersen was being asked to make, "the usual expression was one of comfort. It was not, these are the highest risk transactions on a scale of one to ten." (*See* Report at 20).

Careful review of one of the internal Arthur Andersen documents illustrates the flaws in the Report. The PSI Report cites a February 6, 2001 e-mail from Mr. Jones of Arthur Andersen to Messrs. Bauer and David Duncan as "further proof that Andersen viewed Enron as engaged in risky accounting." (*See* Report at 18-19). This e-mail was not sent to any Director. The e-mail expresses Andersen's concern that neither Andersen nor Enron management had adequately communicated with Enron's Board concerning Enron's related-party transactions. (*See id.*). In the February 12, 2001 Audit Committee meeting, however, Andersen raised no concern with the Audit Committee about Enron's related-party transactions. Rather, David Duncan, despite having received the e-mail, assured Enron's Audit Committee that Andersen's "opinion on the

Company's internal controls ...would be unqualified, [that] the audit was complete and no material weaknesses had been identified." (*See* Audit Committee Minutes of February 12, 2001 at pgs. 1-2).

The concerns expressed in the internal Andersen e-mail – which Andersen did not give to the Directors – provide no evidence that Enron's Board knew Enron was engaged in risky accounting. The e-mail shows, rather, that Andersen knowingly failed in its duty to keep the Audit Committee informed. Six weeks after the February 6, 2001 e-mail, Andersen again signed Enron's Form 10K, again gave Enron a clean audit opinion, again opined that Enron's internal controls were adequate, and again indicated it had no disagreements with management concerning Enron's financial statements. (See Annual Report for 2000 at 30 ("disagreements with management" "None")). These actions provided further assurances to the Audit Committee that Enron's financial statements were in order, that Andersen was comfortable with the adequacy of Enron's internal controls, and that no additional verification was warranted.

The Report also fails to address the trial testimony of Andersen's lead accountant, David Duncan. David Duncan was called as a government witness and testified pursuant to a plea agreement. At the time of his testimony and the *Andersen* trial, he had already pleaded to a felony, the commission of obstruction of justice. The *Andersen* criminal trial was completed before the Report was issued.

Excerpts from the trial testimony, compared below with the allegations of the Report, illustrate that the erroneous conclusions reached in the Report result, in part, from a decision to ignore the *Andersen* trial testimony. Certain testimony of David Duncan controverts the Report's suggestion that David Duncan believed Enron's accounting was overly aggressive or inaccurate, as shown on the chart below.

COMPARISON OF *ANDERSEN* TESTIMONY WITH PSI REPORT

PSI ALLEGATION	*ANDERSEN* TESTIMONY
PSI Report contends that Andersen told Directors that Enron was engaged in "high-risk" accounting that "push[ed] limits" or were "'at the edge' of acceptable practice." (Report at 17-18).	David Duncan testified that, to Arthur Andersen, "high-risk" meant that its client "had a very complex business model, engaged in very complex transactions with difficult . . . areas to reach accounting conclusions and that [Andersen] had a large amount of business with them. (Tr. at 2283-84). David Duncan testified that of the 3000 clients Andersen had as of 2001, "several hundred" were "high-risk." (Tr. at 2285.)
The PSI implies that Andersen made the Audit Committee aware of improper accounting at Enron.	David Duncan was "not aware of any accounting improprieties at Enron." *Tr.* at 2020. While David Duncan believes that "it was a mistake for Enron to have booked their equity...wrongly for about $1.2 billion," *Tr.* at 2020, he does not believe that was "an intentional mistake by either Enron or [Andersen]." *Id.* David Duncan has, to his knowledge, "never for a moment thought there was anything fraudulent or anything that had to do with a misrepresentation about that." *Id.* at 2021.
The PSI asserted that Andersen was uneasy with Enron's structured finance and related-party transaction(s)	David Duncan testified that he gave advice to Enron's Rick Causey in 1999 about how to structure Enron's transaction with LJM Swap Sub, and said he "believed [that advice] was correct and appropriate at the time." *Tr.* at 2036.
The PSI suggests that Andersen had doubts about the way in which Enron presented its financial statements	David Duncan testified that "every one of the accounting positions that [he] took on behalf of Andersen" he took "with the good faith belief that what [he was] doing [was] right." *Tr.* at 2046. David Duncan testified that other than the matters at issue in Enron's subsequent restatement (*e.g.*, errors, like Raptors, or information that was allegedly withheld from Andersen, like Chewco), there were no "other accounting issues that [he] was involved in or [his] team was involved in with Enron that [he] believes were handled inappropriately." *Tr.* at 2050.[5] Even as to the matters at issue in the November 2001 restatement, David Duncan confirmed that "in each of those three cases...Arthur Andersen's advice....[was] given in good faith based on what [it] knew at the time." *Id.*

[5] The facts that David Duncan indicated were unknown to Arthur Andersen involved an undisclosed guaranty or security agreement in the structure of the Chewco transaction. As the Directors have stated publicly and in PSI interviews, neither the existence of this agreement nor the fact that Michael Kopper was an investor in Chewco was known to them.

COMPARISON OF *ANDERSEN* TESTIMONY WITH PSI REPORT	
PSI ALLEGATION	*ANDERSEN* TESTIMONY
Enron's Related Party disclosures were insufficient	David Duncan testified that it was Andersen's responsibility to "review those disclosures [to determine] whether they are appropriately in compliance with generally accepted accounting principles for disclosure taken as a whole." *Tr.* at 1739. Having conducted that review, David Duncan testified that he believed Enron's footnote disclosures of its related-party transactions were "adequate." *Id.*

Other evidence offered by the government at the *Andersen* trial demonstrates the Board's reliance on Arthur Andersen for advice on accounting issues. An inside lawyer for Arthur Andersen, Nancy Temple, took notes of a November 2, 2001 Enron Audit Committee meeting, shortly before Enron filed its restatement on November 8, 2001. Arthur Andersen accountants David Duncan, Steve Goddard, and others were present to report to the Audit Committee about the status of their review of certain of the transactions, including Chewco, LJM Swap Sub, and a $1 billion decrease in shareholders' equity. Ms. Temple's meeting notes make clear that the Audit Committee members had relied on the assurances they had consistently received from Arthur Andersen about Enron's accounting practices. This evidence, like the testimony of David Duncan, was available to the PSI before the Report was issued.

These notes show that the committee members were surprised and upset that Arthur Andersen was no longer standing by the advice the accounting firm had given Enron. With regard to the Chewco issue, one committee member asked, "who w[itheld] facts. Did Fastow know?" Director Wendy Gramm commented, "We have to tell the SEC." Mr. Causey, Enron's chief accounting officer, stated that Arthur Andersen had "changed [its] acc[ounting] guidance" and said he would "let AA explain." Mr. Causey stated that the accounting issues surrounding LJM swap sub were "known to AA @ time" and now Arthur Andersen's Professional Services Group "say not comfortable."

Ms. Temple also recorded that Audit Committee chair Dr. Jaedicke and Directors Pereira and Gramm were "all frustrated – how can [they] continue to rely on us [Arthur Andersen] – [they were] constantly told we [Arthur Andersen] have strong technical people." The Audit Committee members asked Arthur Andersen whether they were "applying new rules to old trans[actions]," and were told, "No." Mr. Lay asked "when will [Enron] know we [Arthur Andersen] have consulted w[ith] Chi[cag]o & NY & when can [Enron] rely on advice or not." Mr. Lay also commented on the issue of the restatement of the $1.2 billion in equity, stating that "[i]f we had done this right in 1Q [2001], [we] wouldn't be here today."

III. THE BOARD'S APPROVAL OF CERTAIN RELATED-PARTY TRANSACTIONS WAS APPROPRIATE AND IN THE BEST INTERESTS OF ENRON AND ITS SHAREHOLDERS

The Report does not raise – nor, for that matter, has anyone, including the Powers Report, raised – any suggestion that Enron's Directors did not act in good faith when they approved certain related-party transactions. None of the Directors had any personal interest in these transactions, their interests were aligned with those of Enron's shareholders, and all of them were people of conscience, possessed of significant business expertise and financial knowledge.

Nearly one-third of the Report, however, is devoted to a critique of the Board's decision to authorize the creation of the LJM partnerships. The Directors do not agree that these criticisms are valid given what the Directors knew at the time the authorizing resolutions were adopted. Based upon the information made available to the Board at the time it approved the first LJM transaction, and based upon the representations made to them again in connection with the subsequent authorization of LJM2 and three of the Raptor structures, the Directors believed these transactions made sense for Enron and were in the best interests of the Company's shareholders. The reasons for this belief have been the subject of testimony by Mr. Winokur and Dr. Jaedicke in two Congressional hearings. (*See* February 7, 2002 Subcommittee on Oversight and Investigations of the House Committee on Energy and Commerce Hearing Transcript; May 7, 2002 PSI Hearing Transcript;) http://energycommerce.house.gov/107/hearings/02072002Hearing 485/hearing.htm (written statements of Jaedicke and Winokur from February 7, 2002 House hearing); http://www.senate.gov/~gov_affairs/050702witness.htm (written statements of Blake, Duncan Jaedicke, LeMaistre, and Winokur). In addition, there are seven separate witness statements explaining the reasons for the Board's decisions, the factors upon which they relied and the disclosures that were and were not made to the Board concerning these transactions. (*Id.*).

The Report asserts that the Board's oversight of its internal controls was inadequate. The following facts refute this allegation:

- The specific controls that the Board implemented with regard to the related-party transactions were internal controls that fell within the scope of Andersen's internal control audit. At the May, 2000 Audit Committee meeting, David Duncan informed the committee that "structured transactions related to securitization and syndication and hedging vehicles" were among the areas on which Arthur Andersen would be spending additional time. (May 1, 2000 Audit Committee meeting minutes at 1-2). Each year the Board sought, and obtained, assurance from Andersen that there were no material weaknesses in these internal controls. (*See e.g.* February 12, 2001 Audit Committee Minutes at 1-2). Both the Audit Committee and the Board were entitled to rely on this opinion.

- The Board was assured by Enron's Chief Accounting Officer that the specific transaction approval processes and controls implemented for these transactions were "working effectively." (February 12, 2001 Finance Committee meeting minutes at 5). The Audit Committee and the Board were entitled to rely on this representation from management.

- At the October, 2000 Finance Committee meeting, in the presence of Messrs. Skilling, Lay, Causey, and Buy, Mr. Fastow told the Committee that the following mechanisms "*had been put in place*" relative to LJM: (1) [Mr. Fastow's] fiduciary responsibilities to the Company remained in effect; (2) the Office of the Chairman or the Board could ask him to resign from the LJM funds at any time; (3) Messrs. Buy, Causey, and Skilling approve all transactions between the Company and the LJM funds; (4) there was to be an annual Audit and Compliance Committee review of the Company's transactions with the LJM funds; (5) a review of his economic interest in the Company and the LJM funds was to be presented to Mr. Skilling; and (6) there was no obligation for the Company to transact with LJM funds. (October 6, 2000 Finance Committee meeting minutes at 2).

- In addition, the legal department was "responsible for maintaining audit trails/files on all transactions." (*Id.*, attached LJM presentation slide).

Independent of and in addition to these assurances, there were pre-existing transaction controls that, had they been followed, would have required company management and Arthur Andersen to prevent (or at least disclose to the Board) the existence of problematic related-party transactions.

- The transaction approval process required Board approval for any transaction with a monetary amount greater than $75 million. The Raptor III transaction, which apparently far exceeded this threshold, was not presented to the Board for approval. The Raptor recapitalization in the first quarter of 2001, which we now know exceeded $800 million in value, also should have been, but was not, presented to the Board for approval. This transaction approval process was an internal control known to Andersen and company management.

- Enron's Risk Assessment and Control Group was required, at each Finance Committee meeting, to report to the Finance Committee the Top 25 Credit Exposures to Enron Although the Raptor entities presented at least an $800 million credit exposure to Enron by the first quarter of 2001, neither they nor the LJM partnerships appeared on the list of Top 25 Credit Exposures.

- The Report notes that there were to be annual reviews of the LJM transactions with the Audit Committee. Those reviews were conducted, but the information provided was incomplete in material respects. For example, the listing of transactions completed with LJM that was provided in February 2000 was incomplete. It concealed from the Directors the existence, for example, of any of the "buyback" transactions so heavily criticized in the Powers Report.

- Enron's Code of Conduct required the disclosure of any related party or self-dealing transaction. Each employee had to complete a questionnaire disclosing his interests, if any, in a compliance process that was audited on an annual basis by Vinson & Elkins. Neither Vinson & Elkins nor any Enron employees disclosed to the Directors that employees other than Mr. Fastow (such as Messrs. Kopper and Glisan) were investors in the LJM related-party transactions. Nor did Vinson & Elkins, Mr. Fastow or Mr. Kopper disclose to the Board that Mr. Kopper was an investor in the Chewco transaction.

- Enron's Code of Conduct required that any related-party transaction be fair to Enron. In the presence of Messrs. Lay, Skilling, Causey and Buy, senior management of Enron, specifically Messrs. Buy and Causey, were charged with the responsibility to review the fairness of the LJM transactions. (October 6, 2000 Audit Committee meeting minutes at 5). Messrs. Buy and Causey were co-equals with Mr. Fastow and reported directly to the Board about the LJM transactions. They also reported to Mr. Skilling, who, by virtue of his position, was to have monitored them. Mr. Fastow said that Mr. Skilling was doing so. (*Id.*). These officers had ample opportunity to express concerns to the Directors if the LJM transactions were unfair, uneconomic or on terms not at arms' length – and were specifically directed by the Board to do so – but did not. The Directors were told that the transactions were conducted at arms-length and that the controls were working.

Had these and the other controls been followed, the transactions that were unfair to Enron may have been avoided. It is reasonably certain that proper implementation of these controls would have prevented the closing of two transactions whose improper accounting later had catastrophic consequences for Enron; namely, the Raptor restructuring (whose $800 million size required, but was not presented for, Board approval) and the Chewco transaction (whose related-party involvement also required, at a minimum, approval by the CEO and adequate disclosure to the public but which was presented to the Executive Committee as "unaffiliated."). It is also likely that the Directors would have been made aware of excessive compensation from the LJM partnership sooner.

For the reasons stated in our prior testimony and statements, and those set out here, we must therefore respectfully disagree with the Report's conclusion that the approval of certain related-party transactions reflects a fiduciary failure on the part of the Directors.

IV. THE BOARD'S APPROVAL OF OFF-BALANCE SHEET FINANCING TRANSACTIONS WAS APPROPRIATE AND FULLY DISCLOSED

If there is a prevailing refrain in the Report, it is that Enron engaged in "Extensive Undisclosed Off-the-Books Activity." (*See* Report at 3, 39-51). The term "off the books" appears intended to connote some form of secret or possibly illegal set of transactions that were concealed from investors. Many transactions cited by the Report, however, were disclosed in Enron's public filings in disclosures largely ignored in the Report. We discuss each of the transactions in more detail, below.

A. Whitewing

The PSI describes Whitewing as an "off the books vehicle" with which Enron had "extensive off the books dealings." (Report at 39, 41).

The Whitewing transactions were disclosed in detail in Enron's public financial statements. These are "the books" – to use the Report's term – that were provided to public shareholders for their review and information through filings with the SEC. Included in these public financial statements were notes explaining particular categories of financial information. These notes formed an "integral part of these consolidated financial statements" (*see, e.g.*, Annual Report for 2000 at 31), and should therefore have been considered by anyone who wanted to understand Enron's financial condition or its transactions with Whitewing, LJM or any other deconsolidated entity.

Note 9 to Enron's financials, for example, disclosed that "in 2000 and 1999, Enron sold approximately $632 million and $192 million, respectively, of merchant investments and other assets to Whitewing. Enron recognized no gains or losses in connection with these transactions." (*Id.*). Notes 3 and 10 provide additional disclosures about the Whitewing partnership. Included in these disclosures is a discussion of the fact that Enron had agreed to contribute a limited amount of Enron equity to the Whitewing partnership if the price of Enron stock fell below $48.55 per share. (*Id.*) The Whitewing transactions were "on the books" Enron filed with the SEC, and were disclosed to the public.

The Report seems to imply that because Whitewing was deconsolidated it was not disclosed. The above discussion makes clear that the opposite is true. Whitewing, which had significant outside investors, was disclosed "on the books" of Enron. The details of this partnership were made available to investors, year after year, in Enron's public filings. The suggestion that this partnership was "off the books" or that it was somehow "undisclosed" is unfounded.

B. LJM

The Report next turns to a discussion of the LJM Partnerships which, like Whitewing, were disclosed in Enron's public filings. (*See, e.g.*, Enron 2000 Form 10K at Note 16, Related-party transaction(s)). The LJM partnerships have been discussed above, so we will limit our comments to the assertion that Enron's disclosures concerning the LJM transactions were not adequate.

In any assessment of the adequacy of Enron's disclosures, it is important to recall that the notes are an integral part of the company's consolidated financial statements. The notes were audited by Arthur Andersen, which had an obligation to make sure that they contributed to a fair presentation of Enron's financial condition taken as a whole. (*See* Duncan *Andersen* Trial Testimony at 1739). David Duncan has confirmed, under oath, that Andersen actually audited Enron's related party disclosures and believed they were "adequate." (*Id.*) That testimony is fully consistent with Andersen's assurance, in Enron's Forms 10K for 1999 and 2000, that Enron's financial statements (including the footnotes) fairly presented Enron's financial condition in all material respects. Furthermore, Vinson & Elkins was extensively involved in drafting Enron's proxy statements, which also disclosed these transactions.

In addition to Arthur Andersen's representations that Enron's financial statements were accurate and presented fairly, Enron's Audit Committee was also regularly assured that there were no material weaknesses in its internal controls, and that Enron's internal controls were adequate to provide reasonable assurance as to the reliability of Enron's financial statements and the protection of its assets. (*Compare* Audit Committee Minutes of February 7, 2001 with Enron Annual Report for 2000 at 30). When they reviewed the LJM Related Party disclosures in the 1999 and 2000 Form 10Ks, no independent Board member perceived it to be inconsistent with the transactions they had authorized. Everything the Directors knew about Enron's Related Party disclosures, which were written by others, reviewed by Vinson & Elkins, and audited by Arthur Andersen, led them to believe that the disclosures were adequate and were correct.

Directors have a clear right to rely on an auditor's assurance that a company's financial statements are correct. *See* 2001 Or. Rev. Stat. 60.357(2); 15 U.S C. § 77k. Even today, the Andersen partner in charge of the Enron audit maintains that Enron's Related Party disclosures were adequate. (*See* Duncan *Andersen* Trial Testimony, *supra*.) The Report's suggestion that the Directors were not entitled to rely on these important assurances, or were responsible to "verify the information provided" to them by Andersen, (Report at 14), turns the law on its head and would cast directors in a role they have never had, namely, as auditors of the auditors.

C. The Directors Instituted Adequate Controls to Monitor Mr. Fastow's LJM-Related Compensation

The Report alleges that the Board inadequately monitored Mr. Fastow's LJM compensation. (Report at 35). This contention reflects a disregard of the record on this issue.

By virtue of his position, Mr. Skilling was generally responsible for overseeing Mr. Fastow's activities. In addition, the Board specifically placed upon Mr. Skilling the responsibility to oversee Mr. Fastow's LJM compensation. At the October 6, 2000 Finance Committee meeting, Mr. Fastow told the committee, in the presence of Messrs. Skilling, Causey, Buy and Lay, that, among the other LJM controls, he understood that "a review of his economic interest in the Company and the LJM funds was to be presented to Mr. Skilling." (October 6, 2000 Finance Committee meeting minutes at 2). Mr. Fastow also told the committee that he understood his fiduciary responsibilities to the Company, and that Messrs. Buy, Causey, and Skilling were to approve all transactions between the Company and the LJM funds. (*Id.*) Mr. Skilling thus bore the chief responsibility to monitor Mr. Fastow's LJM compensation, and he, along with Messrs. Causey and Buy, were responsible for implementing the Board-prescribed controls that, if executed properly, would have revealed that Mr. Fastow's return from the LJM partnership was excessive. Mr. Skilling testified that he met with Mr. Fastow and reviewed his LJM compensation. (*See* February 7, 2002 Oversight and Investigations Subcommittee of the House Committee on Energy and Commerce Hearing Transcript at 143-44). Mr. Skilling did not present the results of this review to the Directors.

The transactions involving LJM1 were approved on the express understanding that Mr. Fastow would have "no direct pecuniary interest, either current or future, in the Enron stock" to be held in the LJM1 partnerships. (*See* June 28, 1999 Board meeting minutes and presentation). This was represented to the Board, and the Board was entitled to rely on it. The FBI investigation in connection with the National Westminster Bank matter reflects that Mr. Fastow apparently subverted this LJM1 control in an effort to increase his personal gain from LJM1. (*See* Affidavit of C. Deanne Simpson, filed in support of criminal complaint against Messrs. Mulgrew, Darby and Bermingham, the Southern District of Texas).

In addition, Mr. Fastow told the Board the formula for his compensation from the LJM partnerships. (*See, e.g.*, June 28, 1999 and October 11, 1999 minutes presentation). That formula depended, in part, upon the performance of the underlying assets that would subsequently be held in the LJM partnerships; its precise amount could not be determined at the time the transactions were approved. The Board was subsequently advised that the rate of return being generated by LJM2 was 17.95%. (*See* May 1, 2000 Finance Committee meeting minutes). This relatively modest rate of return was consistent with Mr. Fastow's representation to the Board that he was spending only three hours per week on the LJM partnerships and did not suggest excessive compensation. *Id.* Nothing in the reports presented to the Board about the LJM Partnerships gave them reason to doubt the veracity of these representations about Mr. Fastow's compensation or how he would earn it.

Rather than consider this extensive evidence of controls put in place by the Board, the PSI Report instead focuses upon Mr. Winokur's recommendation that, in addition to the above controls, the Compensation Committee review Mr. Fastow's LJM compensation. (*Id.* at 3; Report, p. 36). Assuming that Mr. Fastow's LJM compensation would be contained in the scheduled quarterly or annual reports to the Audit or Finance Committees, Dr. LeMaistre testified that he made attempts to get this information after the first and second quarters of 2001 from Enron's senior compensation officer. (May 7, 2002 PSI Hearing Transcript at 168-71). Dr.

LeMaistre was told that the Compensation Committee staff had not received this information. (*Id.*). On October 19, 2001, following a Wall Street Journal article concerning Mr. Fastow's LJM compensation, the Board authorized Dr. LeMaistre and Mr. Duncan to contact directly Mr. Fastow to obtain this information.

The Directors instituted controls to limit and monitor Mr. Fastow's compensation from LJM. They also made reasonable efforts to obtain information about Mr. Fastow's LJM earnings. Despite these efforts, the amounts of money being generated by the LJM partnership and upon which Mr. Fastow's compensation were based were repeatedly misrepresented to the Board. It is unfair, in the face of this extensive record, to suggest that the Directors could somehow have discovered the sums of money Mr. Fastow generated for himself from transactions he did not fully disclose to the Directors.

V. THE BOARD PROPERLY RELIED UPON OUTSIDE EXPERTS TO DETERMINE EXECUTIVE COMPENSATION

The Report complains that Enron's Board "approved [executive compensation plans] with little debate or restraint." (*See* Report at 53). To the contrary, the Enron Board Compensation Committee worked with management and outside consultants to design compensation packages that would attract and retain the company's most valuable asset, its employees.

Enron's compensation philosophy, its compensation plans and the compensation paid to Enron's top executives were regularly disclosed to existing and prospective shareholders in Enron's Annual Proxy Statements. Each proxy statement devoted more than a dozen pages to the issue of executive compensation, revealing to the investor the matters that the Report criticized as undisclosed. (*See* May 4, 1999 Proxy at 14-29; March 28, 2000 Proxy at 14-29; and, March 27, 2001 Proxy at 14-29). Enron's annual and long term incentive programs are described in detail. (*Id.* at 15-16). Bonus awards for top executives were likewise disclosed. (*Id.*). The grants of significant stock options were explained in detail. (*Id.* at 22-24). Even the involvement of the executive compensation consulting firm, Towers Perrin, and the fact that the Compensation Committee relied regularly on its advice in setting compensation targets was fully disclosed to investors:

> Each year, Enron conducts an executive compensation study covering executives in the top corporate and business unit positions. The Committee utilizes the services of Towers Perrin, a consulting firm experienced in executive compensation, to conduct the study. Compensation studies evaluate total direct compensation which is defined as base salary, plus most recent actual annual incentive earned, plus the estimated annualized present value of long-term incentive grants.

(*See id.* at 15).

The fact that Enron rewarded high performance was also disclosed:

> Approximately 75% of the total compensation of Enron's most senior executives is at risk, based strictly upon the performance of Enron relative to stated recurring after-tax net income targets, stock price performance and total shareholder return which impacts grants of performance units...Executives have the opportunity to earn at the 75^{th} percentile or higher level, subject to obtaining performance at the 75^{th} percentile or higher. Higher achievement provides higher value, while lesser performance decreases total compensation. In order to assure that an executive's compensation is tied to performance, more dollars of total compensation are placed at risk, tied to Enron absolute performance and performance relative to the S & P 500 group of companies.

(*Id.* at 15-16).

No amount of consultation and deliberation can ensure that no abuse will occur, as is illustrated by Mr. Lay's improper use of his line of credit. The facts concerning Mr. Lay's conduct are still emerging, but this much is clear. Without disclosing it to the Directors, Mr. Lay repeatedly accessed his line of credit with Enron, withdrew cash from the company, and repaid his borrowings with stock. He sometimes did this within a single day, so quickly that no interest charges were incurred. This was not disclosed to the Directors, and the Directors never condoned such actions.

Mr. Lay's loan withdrawals were an abuse of his line of credit. His withdrawals were not disclosed to the Directors as they should have been. Had they been disclosed to the Directors, Mr. Lay's repayments with stock would not have been permitted. The Directors' dismay and "outrage" concerning these events from their testimony at the PSI hearing. (May 7, 2002 PSI Hearing Transcript at 221).

VI. THE EVIDENCE ESTABLISHES THE ENRON BOARD WAS INDEPENDENT

The Blue Ribbon Committee set forth the several recommendations on audit independence. It advised that the NYSE and the NASD adopt the following definition of independence for purposes of service on the audit committee of the board of a company with a market capitalization above $200 million: "Members of the audit committee shall be considered independent if they have no relationship to the corporation that may interfere with the exercise of their independence from management and the corporation." In addition, it recommended that audit committees be comprised solely of independent directors.

The Enron Audit Committee met the Blue Ribbon Committee's recommendations. Its charter stated that the Committee shall be comprised of three or more directors who, in the opinion of the board of directors, have no relationship to the company that may interfere with the exercise of independent judgment as a committee member. The Enron Board deemed all members of the Audit Committee independent The Board made a specific finding of independence relative to Lord Wakeham, who, as explained below, received a retainer for providing advice on international energy deregulation.

The Report contends that the Board's independence as a whole was "compromised by financial ties between the company and certain Board members." This claim is unfounded. The financial ties the Report cites were *de minimus*.

The "ties" did not, as a legal or a factual matter, compromise the independence of the entire Board or that of any individual Director. The suggestion, for example, that Mr. Winokur was not independent because he also served on the Board of another public company that obtained an average of one-half of 1% of its annual revenues from sales of oilfield service equipment products to an Enron subsidiary on an arms-length basis is specious. The fees paid to Lord Wakeham, who was retained to consult with Enron concerning international energy deregulation was disclosed and not sufficient (legally or factually) to compromise his independence. Finally, while Mr. Belfer sat on the Board of another public company, Belco Oil & Gas, which engaged in hedging transactions with Enron, those transactions were disclosed, and the hedging transactions were done on a competitive basis.

The Report also suggests that the independence of three other directors, Drs. LeMaistre, Mendelsohn and Gramm, was compromised by Enron's charitable contributions to institutions with which they are associated. This contention is inaccurate. Dr. LeMaistre is the immediate past President of the M.D. Andersen Cancer Center. Enron pledged $1.5 million to the Center's capital campaign that took place during Dr. LeMaistre's tenure as President of the Center. Enron's contributions comprised less than 1% of the total contributions raised from the public (individuals, corporations, and foundations) and from the Center's staff. Dr. LeMaistre did not solicit contributions from Enron.

Dr. Mendelsohn succeeded Dr. LeMaistre as President of the Center in 1996. Dr. Mendelsohn became an Enron director on May 1, 1999. From that date through December 31, 2001, Enron gave $92,508 to the Center. The Lays, either directly or through their family foundation, gave a total of $114,500. The total amount of money raised from private philanthropy during that period was $233,624,148. The combined amount of these Enron- and Lay-related contributions comprise less than 0.1% of the private philanthropy the Center raised during that time period.

Since 1998, Dr. Gramm has been an employee of the Mercatus Center at George Mason University. Enron had been a contributor to the Mercatus Center since 1996, long before Dr. Gramm joined it. From 1996 to 2001, total contributions from Enron and the Lay Foundation to the Mercatus Center were $60,000. This amount averages $10,000 per year and is less than one-third of 1% of the Center's budget.

Although Enron's charitable contributions were certainly appreciated by their recipients, they were financially insignificant to the organizations to which they were donated. The contributions were not so large as to call into question these directors' independence.

The PSI Report contends that the compensation paid to the Directors was "more than twice the national average for Board compensation at a U.S. publicly traded corporation," suggesting that this was excessive and may have comprised the Directors' independence. (Report at 11). There is no support for this claim.

Enron's Proxy Statement disclosed every year the total directors' fees paid to each director. The Report does not suggest these disclosures were inaccurate. At the time of its collapse, Enron was one of the largest companies in the country. Given that there as many as 15,000 publicly traded companies, statistics about director compensation at thousands of companies, all but six of which were smaller than Enron in size and complexity, are not particularly informative.

Contemporaneous evidence also establishes that the Directors' compensation was not excessive. In 2000, for example, Enron commissioned an independent study from Towers Perrin to determine whether its director compensation was appropriate. The study revealed that, while Enron was in the 75th percentile in terms of size, and outperformed comparable companies in terms of financial performance, total cash and stock-based compensation to Enron's directors was slightly below the 75th percentile. (*See* Compensation Committee Minutes of May 1, 2000; *see also* April 20, 2000 Report of Towers Perrin)

Given that there was clear evidence of the amount actually paid to Enron's directors, and its significance relative to comparable companies, the PSI's conclusion that Enron's directors were compensated excessively does not bear close scrutiny.

Finally, since it is the actions of the Board as a whole that must be considered here, it is important to note that the Delaware Supreme Court has made clear that the Board's business judgment is protected unless "actual self-interest is present and affects a majority of Directors approving a transaction. . . ." *Paramount Communications, Inc. v. QVC Network, Inc.*, 637 A.2d 34, 42 n.9 (Del 1993). There is no valid suggestion that any outside Board member's independence was compromised in this case, and certainly no suggestion that the Board as a whole was not independent. The proper inquiry, therefore, remains whether the Board properly informed itself and acted in good faith.

The Report also asserts that Enron's outside auditors, Arthur Andersen, were not independent and suggests that this is another failure by the Board to ensure independence. (*See* Report at 50-51). We review here, therefore, the steps taken by the Board to ensure Andersen was independent.

Auditor independence was originally a function of rules established by the American Institute of Certified Public Accounts. The AICPA and the SEC decided to form a new "Independence Standards Board" to further independence issues. In 1998, the Blue Ribbon Committee of the New York Stock Exchange and the NASD also promulgated a series of independence guidelines. Finally, there were a series of Best Practices laid out for audit committees – including requirements of financial literacy, accounting expertise and qualitative (as well as quantitative) discussions of company financial matters – that were adhered to by Enron's Audit Committee.

On an annual basis, Andersen and Enron's Audit Committee – both independently and jointly – tested Andersen's independence and the performance of the Audit Committee against these standards. The records of these detailed reviews are reflected in Audit Committee minutes that were made available. These reviews encompassed more than twenty separate observations, and included a forthright and searching assessment of Andersen's audit and non-audit fees. Andersen represented to Enron's Audit Committee that:

- Andersen's policies regarding independence were generally *more stringent* than those required by the Securities and Exchange Commission, the AICPA and those applied by other accounting firms;
- Andersen had tested its relationship with Enron against these standards and had concluded that its "relationship and scope of practice" are appropriate for a company as large and active as Enron; and
- "We confirm that we are independent accountants with respect to Enron within the meaning of the Securities and Exchange Commission and the requirements of the Independent Standards Board."

(*See* August 9, 1999 Audit Committee meeting minutes. Slide: "Independence Initiative – Observations and Conclusions.") The Audit Committee reviewed these requirements in detail, measured Andersen's role against them and concurred in Andersen's judgment that it was independent.

Reviews of this type were conducted annually. They were rigorous, thorough and well-documented. They also refute the claim that the Board failed to address the issue of Andersen's independence.

VII. THE DIRECTORS WERE ATTENTIVE TO ENRON'S FINANCIAL CONDITION

The Report makes a series of scatter-shot assertions intended to convey the impression that Enron's Board failed to react to the company's financial difficulties. The Report takes documents out of context and ignores others in a manner that creates a misleading picture

As a part of its oversight of Enron's finances, the Board made efforts to keep itself informed of potential problems with major assets, major strategic initiatives, and matters pertinent to the company's liquidity. These efforts were appropriate and consistent with the role of a corporate director. The Report, however, inexplicably casts these efforts as fiduciary failures, apparently because the assets in question were performing poorly or had embedded risk. In fairness, that is not how a director's actions should be analyzed. The question, again, is did the Board have in place procedures that would yield this information, and did the Board act on that information in good faith? In the words of the Delaware Chancery Court, "to allege that a corporation has suffered a loss as a result of a lawful transaction, within the corporation's powers, authorized by a corporate fiduciary acting in a good faith pursuit of corporate purposes, does not state a claim" of fiduciary failure. *Gagliardi v. Trifoods Int'l, Inc.*, 683 A.2d 1049, 1052 (Del. Ch. 1996).

The Report's piecemeal review of a handful of documents presented at various committee meetings concerning troubled assets or financing risks adds nothing. That these were presented and considered by the Board confirms the Board was attentive to the Company's financial condition. As the Report points out, Mr. Winokur requested a report from Enron management concerning the stock price risk imbedded in Enron's financings. (*See* Report at 48). This stock price risk had been disclosed in Enron's public filings (*see, e.g.*, Form 10K at note 10, Common Stock). Mr. Winokur wanted the Finance Committee to review it in detail. The Finance Committee learned that even in a disaster scenario where the assets in the financing structures were entirely worthless and Enron's stock declined by 50%, Enron's shareholders would face only a potential 6% dilution risk. (*See* April, 2001 Finance Committee meeting presentation). The Committee did not believe that risk was excessive. In any event, it cannot fairly be said that the Board was inattentive to the dilution risk in Enron's financings.

The Report also makes much of documents reflecting that 64% of Enron's international assets were performing "below expectations" or were "troubled." These were reports that the Finance Committee had requested be provided on a regular basis. During their staff interviews, several Directors explained what the documents meant. First, the vast bulk of those troubled assets comprised two large power and pipeline investments in India and Brazil. Enron had made extensive disclosures about the difficulties and cost overruns it had encountered in both projects, (*see, e.g.*, Enron Form 10Q for First Quarter 2001 at 16), together with significant additional disclosures concerning currency devaluation risks, confiscation risks and the risks of project delays. It is unfair to suggest that Enron's Board acted improperly with regard to the oversight of these assets when it was attending to the difficulties presented by Enron's ownership of these assets and when those difficulties were disclosed to the investing public.

Finally, the Report's suggestions that the Board was inattentive to the implications of Mr. Skilling's resignation, (Report at 12), or to Enron's declining financial fortunes, (*id.* at 12-13), again ignores the evidence. The minutes of the August 2001 Board and committee meetings illustrate that the Board, although concerned about the likely effects of Mr. Skilling's resignation, had no reason to believe that the Company was in fundamental, financial jeopardy. Mr. Skilling's public sworn testimony supports this fact. He stated, "I left Enron on August 14, 2001 for personal reasons. At the time I left the company, I fervently believed that Enron would continue to be successful in the future. I did not believe that the company was in financial peril." (February 7, 2002 Opening Statement of Jeffrey Skilling; *see also* February 7, 2002 House Subcommittee on Oversight and Investigations hearing transcript at 122, 150).

The slides presented at the August Board meeting reflected that Enron's net income, for the year-to-date and for the second quarter, were ahead of plan, largely as a result of the overwhelming success of Enron's wholesale energy trading business. (*See* Financial and Earnings Report "Net Income" presented at August 13-14, 2001 Board meeting). Diluted earnings per share had grown by 32%, cash had increased markedly, and earnings per business segment were generally up as well. (*Id.*) The notable exceptions were in the Broadband sector –

which reflected declines that were well known, typical of Enron's competitors and fully disclosed,[6] and the issues surrounding Enron's energy trading in California. (*Id.*)

Arthur Andersen reviewed both of these matters with the Audit Committee and discussed the adequacy of the company's reserves for California trading. (*See* August 13, 2001 Audit Committee meeting minutes). Later, in the Board meeting, the Directors were assured that Enron was "fully reserved" for its receivables exposure in California and might, in fact, be owed refunds from certain customers. (*See* California Slide in Board Presentation, August 13-14, 2001 Board Meeting). Finally, and importantly, Enron appeared to be highly liquid. Previous reports to the Board had indicated Enron had "overnight liquidity" of $2.7 billion, plus significant additional, short-term liquidity. (*See e.g.* Liquidity Report as of April 18, 2001, presented to Finance Committee on April 30, 2001). The Directors had extensive discussions of the company's liquidity during the committee meetings in August 2001, and management gave every indication that the Company had sufficient liquidity to protect itself and its shareholders in the event of significant reversals of its fortunes.

It is against this backdrop of solid liquidity, increasing cash, and great success in the wholesale business that the Board's receipt of Mr. Skilling's resignation must be evaluated. Mr. Skilling told the Board that his reasons for resigning were personal and that he believed the company had never been in better financial health. The Directors did not simply accept Mr. Skilling's resignation without comment or inquiry. Rather, the Directors questioned Mr. Skilling regarding his resignation and the Company's condition. Mr. Skilling responded that there were no undisclosed problems at Enron and that Enron had never been in better financial health.

Throughout this two-day meeting, the Board (as it always did) gave close and careful attention to the state of Enron's financial affairs, the risks the company faced and its ability to withstand those risks with liquidity and robust trading controls. Andersen, as well, said nothing to the Audit Committee concerning any weakness it perceived in Enron's internal controls or any concerns it might have about the related-party transactions. While Mr. Skilling's resignation, and the attendant disruption, were certainly cause for concern, there is no basis for the Report's suggestion that this resignation should have caused the Board to believe that Enron was not in good financial health. In fact, Mr. Lay also assured the Board that Enron was in solid financial shape and "our growth prospects have never been better." "Jeffrey Skilling's Surprising Split from Enron," *BusinessWeek Online* (8/15/01).

VIII. CONCLUSION

Tragic events occurred at Enron in Fall 2001. In a matter of months, the seventh largest company in the country was in bankruptcy. The PSI and others are searching for whom to blame. In this report addressing the role of the Directors, the PSI takes isolated

[6] *See, e.g.*, Enron Form 10Q, period ending June 30, 2000 ("Broadband Services recognized a loss before interest, minority interests and taxes of $60 million in 2000"); Enron Form 10Q, period ending June 30, 2001 (stating Broadband Services recognized a loss before interest, minority interest and taxes of $102 million); *id.* ("Enron is significantly modifying the cost structure of Broadband Services to correspond to slower market development"); *id.* ("Future profitability is dependent on the recovery of the broadband communications sectors.")

facts and unsubstantiated inferences to piece together a claim that the Directors share some of the responsibility.

The conclusion is unfair. These Directors did not benefit from the transactions now associated with Enron's downfall. They acted in good faith, and in what they believed, based on the information available to them, was in the best interest of Enron.

Outside directors can only act on the basis of information provided to them. In fundamental ways, the information these Directors got was incomplete and inaccurate. They received that information from a management team they believed at the time was among the most competent in the business world and both directly and indirectly from outside advisors who the Directors then believed were also at the top of their professions. This reliance on these people was appropriate at the time. The Directors should not be faulted, on the basis of hindsight, for the decisions they made.

Respectfully submitted

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IN THIS ISSUE

Institutionalizing Good Governance: Keys to Success

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An experienced corporate director defines good governance—and reveals how Sunoco, Inc., and others have achieved it.

What is corporate governance? In my view, it is the short-hand phrase for describing the legal and practical system of power and control in the conduct of the business of a corporation, most especially the way in which the relationships between and among the shareholders, the board and its committees, the executive officers, employees, customers, and other constituencies are managed. Corporate governance is the fulcrum on which this power and control is balanced.

The "Market Value" of Governance

Corporate governance is increasingly becoming a critical success criterion for investment by large institutional investors and portfolio managers. Russell Reynolds surveys of 400 institutional investor participants, representing a minimum of $1 billion in assets each, concluded that corporate governance is increasingly one of the criteria by which CEOs and top management are judged.

- 63 percent of the respondents indicated the quality of governance practices is very important when making an investment decision.
- 67 percent indicated they have reduced or divested holdings because of poor governance practices.

Many in the investment community argue that there is a link between corporate governance and corporate performance. While current studies have not conclusively proven evidence of this link, a McKinsey & Company investor survey found that over 80 percent of survey respondents reported that they would pay more for shares of

The role of the National Association of Corporate Directors is to enhance the governance and performance of business entities. Since its founding in 1977, the NACD has pursued this goal by offering a broad spectrum of educational and membership benefits, including publications, seminars, and consultative services. The NACD lists all interested members on The Director's Registry, which is used by member companies and others that seek qualified directors. To educate the corporate community and to provide networking links among NACD chapter members, the NACD holds an annual Corporate Governance Conference, where it presents a Director of the Year Award.

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a well-governed company than for those of a poorly governed company with comparable financial performance.*

As we well know, the lack of corporate governance practices are often publicly cited when a company's performance weakens or fails over a period of time. Directors of corporate boards, in these instances, are ultimately held accountable by shareholders and the press, and their faulty corporate governance procedures are often spotlighted.

Good corporate governance standards are not often trumpeted, but they should be. When a company faces a crisis, when directors and management must focus all their energy on burning issues, investors should be assured that well-established and practiced governance guidelines will be the basis for representing and protecting all constituencies equitably.

A Global Perspective

Companies operating in multiple countries encounter varied political environments, varied corporate structures, varied laws and regulations, and varied social values and traditions. One of the many balancing acts of boards of international companies is the successful implementation of appropriate governance practices—practices that respectfully acknowledge individual national foundations of laws and social mores, while being faithful to the rights and interests of U.S. shareholders.

Developing countries are being challenged to introduce corporate governance laws and standards. It is believed that poor standards of corporate governance are one of the main factors holding back the development of the capital markets in those countries. The boards of international companies, seeking investors from around the world, must define a common sustainable measure by which their performance, as directors, can be judged. They know that investors from developing and established countries alike are focused on factors such as shareholder value, board accountability, timely disclosure, *i.e.*, all aspects of corporate governance.

*Note: For more on this survey, see "Are Investors Willing to Pay More for Good Performance?" *DM* January 2001, pp. 14-15.

Defining Good Corporate Governance

I began by stating the corporate governance is the *balancing* of the *power and control* in the conduct of the business of a corporation. So what is "good" corporate governance? Good corporate governance is a relative term. As human nature would dictate, a practice which is deemed to be "good" by the shareholders may not be deemed to be "good" by the directors. Whichever constituency is afforded more power on the balance scale will view that practice as being "good." Also the descriptor "good" is an evolutionary term. What is viewed as "good" this year may not be viewed as "good" in 2005.

The Sunoco Experience

That being said, I would like to focus on the corporate governance practices of a company where I am a director. That company is Sunoco, Inc., a leading manufacturer and marketer of petroleum and petrochemical products. Sunoco is one the largest independent refiners and marketers in the United States.

Sunoco is an excellent example of a company committed to achieving the "best" practices in corporate governance over time, recognizing that it requires a continually evolving effort. Every year, the governance committee of Sunoco's board reviews benchmarking studies, survey analysis, and emerging trends, and every year Sunoco's *Statement on Corporate Governance* is reviewed and approved by the board and published in Sunoco's proxy statement.

Sunoco has been a leader in adopting "best" practices.

- It voluntarily published the audit committee report and charter in its 2000 proxy—one year in advance of the required disclosure.
- It was one of the first companies to publish a "plain English" proxy statement.
- All of its board members (except for the chairman/CEO) meet the independence standards of the various regulatory agencies' rules and the New York Stock Exchange.
- All "key" board committees are composed entirely of independent directors (audit committee, compensation committee, governance committee, and public affairs committee).
- Sunoco has annual director elections for one-year terms.
- There is an annual director review of the three-year strategic plan at an extended off-site.
- The board holds "outside directors only" meetings at least once a year.
- There is an annual director review of management succession planning and development.
- Sunoco has a formal process to review, evaluate, and approve individual directors, as well as a formal evaluation process for the board as a whole.
- Sunoco has director and management stock ownership guidelines.
- The directors' compensation package is equity based, with over 50 percent paid in stock.
- Sunoco has a new, formalized director orientation program.
- The board has 13 members—12 of whom are independent, including three women and one African American male.

Sunoco has been nationally recognized for outstanding corporate governance practices. Sunoco was the 1999 recipient of the Board Excellence Award sponsored by the Wharton School of the University of Pennsylvania and SpencerStuart. Also, NACD's 2000 Director of the Year was Dr. William F. Pounds, who until he retired last year, had been a

DIRECTOR SUMMARY

What is corporate governance? Why is it important? How can a company achieve it and maintain it? An experienced director answers these vital questions, drawing on the example of Sunoco, Inc.

Sunoco director (since 1973), had been a member of the governance committee since 1976, and had been its chairman since 1991.

How to Institutionalize the Corporate Governance Process: Five Keys

Since good corporate governance is continually evolving and not ever locked in time, and since the balance of power and control can also shift with the sands of time, boards should consider institutionalizing a formal assessment process to evaluate corporate governance practices for their inherent "goodness" over time.

The following formula is based on my observations of boards (such as Sunoco's) that have achieved governance success thanks to the progressive attitudes of their members as reflected in their governance practices.

- ***Put current practices in writing.*** The first step in developing good corporate governance is to formalize in writing the current governance practices. This exercise forces a board to map its duties and responsibilities against how effective their policies, procedures, and practices are for helping them successfully carry out their duties to shareholders. The mismappings become obvious as do the necessary changes in board infrastructure and operations.

- ***Publish corporate governance procedures.*** Sunoco and many other corporations publish their governance guidelines and principles in their proxy statements and post them on websites. These are highly effective communication vehicles, which shareholders and investors appreciate.

- ***Charge a committee with governance tasks.*** The board of directors of a corporation should formally "charge" a board committee (usually the "governance committee") with specific governance responsibilities:

  - to keep up-to-date on emerging governance trends
  - to identify (and recommend for adoption) the best practices in the governance area, and
  - to periodically benchmark current practices to those practices of other companies, and to those practices recommended by large institutional investors and professional organizations such as NACD, as well as the American Society of Corporate Secretaries, Business Roundtable, Institutional Shareholder Services, and Investor Responsibility Research Center.

  This committee is then accountable to the full board for improving overall board effectiveness.

- ***Charge the corporate secretary to help strengthen corporate governance.*** The corporate secretary should be charged with the responsibility of keeping the governance committee fully aware of governance trends and best practices and should be directly accountable to the governance committee for this critical job function. The secretary should be a lawyer who can dedicate the significant resources of time and energy necessary to this task. The corporate secretary should carry an officer level of accountability and influence. A title such as vice president of corporate governance would further demonstrate the corporation's commitment.

- ***Strengthen the chain of influence.*** While the four practices described above are basic and obvious, the most critical success factor for good corporate governance is the *chain of influence*, from the CEO to the board.

Good governance requires CEOs who are not afraid of bringing suggested governance changes to the attention of the board, who do not insert themselves in to the process in a negative way, who are confident with themselves, and who are willing, in some cases, to give up their own perceived discretionary "power" in order to bring about the "next level" of best practices in the area of corporate governance. For example, good governance may begin with a CEO who is willing to give up a position as a member of a key board committee in order for that committee to consist entirely of independent directors.

The governance committee and the entire board of directors must be serious about the issue of corporate governance. They must fully support the concept; it is not enough for the process to be in place if the process has no substance. Good governance can happen:

- only when a board is open and receptive to the supporting staff and their research
- only when a board is willing to review emerging trends, and
- only when a board understands how emerging trends may affect future relations with their institutional investors and other shareholders will the process of corporate governance have substance and sustainability.

All these are keys to helping a company achieve a leadership position in corporate governance.

Final Reflections

Good corporate governance is a fluid and constantly evolving process. Companies must continually review their governance procedures to ensure the company's philosophy is accurately reflected and current.

Recognizing that responsibility and accountability to shareholders must be the foundation in all boardrooms, it follows that common sense and fairness will encourage directors of multinational (and really all) companies to view good corporate governance as an essential vehicle in helping to meet the challenges and effectively compete in global environments.

Good corporate governance can be described in many ways. It is the foundation of every successful corporation. It is the fulcrum for balancing power and control. It is the common bond for measuring a company's commitment to its shareholders. It is the wave that will carry a company successfully forward in the global markets of the 21st century.

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