UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

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| In re ENRON CORPORATION SECURITIES LITIGATION | Civil Action No. H-01-3624 **(Consolidated)**<br><br>CLASS ACTION |
| This Document Relates To:<br><br>MARK NEWBY, et al., Individually and On Behalf of All Others Similarly Situated,<br><br>Plaintiffs,<br><br>vs.<br><br>ENRON CORP., et al.,<br><br>Defendants. | |
| THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, et al., Individually and On Behalf of All Others Similarly Situated,<br><br>Plaintiffs,<br><br>vs.<br><br>KENNETH L. LAY, et al.,<br><br>Defendants. | |

**SUPPLEMENT TO THE FIRST AMENDED CONSOLIDATED COMPLAINT (DOCKET NO. 1388) AS TO BARCLAYS FILED PURSUANT TO THE DECEMBER 4, 2006 ORDER (DOCKET NO. 5242)**

## GENERAL OVERVIEW

**Involvement of Barclays**

106. (d) Barclays (including the following named defendants: Barclays PLC, Barclays Bank PLC and Barclays Capital, Inc.) is a huge financial services institution that had an extensive and extremely close relationship with Enron.[1] During the Class Period, Barclays provided both commercial banking and investment banking services to Enron and, in addition, structured, funded and implemented several illicit and fraudulent transactions including JEDI/Chewco, J.T. Holdings, Nikita/Besson, the Nixon Prepay, the Roosevelt Prepay, the CSFB Prepay, Metals (Camelot) and $SO_2$, which were intended to, and had the primary purpose to falsify Enron's financial condition and deceive Enron's outside auditors, the rating agencies and investors in Enron's public securities. Specific details of Barclays' conduct in each of the challenged transactions are provided. Contemporaneous documents, including incriminating e-mails, demonstrate Barclays' knowingly deceptive conduct. Testimony by current and former employees of Barclays, Enron and Arthur Andersen ("Andersen"), as well as the findings by the Court-appointed Bankruptcy Examiner, provide specificity and context to Barclays' conduct as a primary violator under the securities laws.

(e) Barclays Capital was the center point for many transactions that occurred between Enron and Barclays. Barclays' own internal documents acknowledge this: "Enron, particularly Andy Fastow, CFO of Enron Corp, are keen to have a relationship with the top management of Barclays Capital. (The relationship at the transaction level is strong.)" Enron and Fastow clearly achieved this relationship with Bob Diamond, the CEO of Barclays Capital. Multiple transactions with Enron had to go through Barclays Capital Committee for exposure approval.

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[1] The paragraph references in this Supplement to the First Amended Consolidated Complaint as to Barclays supplement and in some cases replace, the paragraph references relating to Barclays in the First Amended Consolidated Complaint filed May 14, 2003 (Docket No. 1388).

Barclays Capital worked with Barclays Bank in syndicating many Enron deals, including, but not limited to Chewco, J.T. Holdings, Metals, $SO_2$, and the Prepay transactions.

(f) For instance, Barclays Capital served as the Syndicating Agent for the Revolving facility Agreement in JEDI executed by Enron Corp. On October 8, 1997, George McKean, a Director at Barclays Capital contacted Michael Kopper along with other Enron management to discuss "structural issues" pertaining to the JEDI/Chewco transaction. McKean noted in his communication with Kopper that "[i]n addition to structural issues, there [were] credit and return issues which [remained] open for discussion . . . once a structural agreement is agreed upon." It is clear Barclays Capital had a significant role in creating and structuring the Chewco transaction to perpetuate the Ponzi scheme in this case. Barclays Capital also acted as resource to others within the bank for information regarding the transaction even after it closed.

(g) Barclays Capital was actively engaged with Enron and Barclays Bank in the structuring and approval of the $SO_2$ monetization. Barclays Capital officers and attorneys engaged in structuring and approving the transaction. Barclays Capital was "very keen to proceed on a 'best efforts' basis . . . applying all necessary internal approvals in connection with the Facility and its structure, . . . drafting the documentation[,] and finalising" the work which needed to be done in connection with $SO_2$.

(h) Moreover, Richard Firth, a Barclays Capital attorney, structured, approved, and signed off on various Enron deals, including J.T. Holdings and the Prepay transactions. Barclays' internal documents reflect Firth's approval and bear his signature for the transactions.

(i) Additionally, Barclays Capital is listed as an initial purchaser on the offering memorandum in the Zero Coupon Notes Offerings of February and July of 2001. Its involvement in the July 2001 Notes Offerings is evident in Enron's July 18, 2001 Prospectus.

752. Barclays acted as a placement agent and/or reseller with respect to the following public offerings of Enron securities:

| DATE | SECURITY |
|---|---|
| 2/01 | $1.9 billion zero coupon convertible notes |

753. In addition, Barclays underwrote the sale of Enron-related securities. For instance:

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| 2/00 | Yosemite Securities Co. Ltd. £200,000,000 8.75% Series 2000 A Linked Enron Obligations |

754. In addition, during the Class Period, Barclays was one of the principal commercial lending banks to Enron engaging in over $3 billion in bank loans to Enron. For instance:

- Barclays was the lead lender on a $2.3 billion debt facility to finance Enron's purchase of Wessex Water in 1998.
- Barclays was a co-arranger of a $250 million loan to Enron in November 1997.
- Barclays had a role in the September 1998 $1 billion credit facility for Enron as well as the August 2001 $3 billion debt facility for Enron, which were used to back up Enron's commercial paper debt.
- Barclays had a portion of a $250 million revolving credit facility for Enron arranged in November 1998.
- Barclays worked to arrange a $500 million credit facility for JEDI in May 1998.

755.1 (Replacing ¶751 of FACC) Barclays' relationship with Enron was so extensive that senior executives at the bank constantly interacted with top financial executives of Enron, *i.e.*, Causey, McMahon, Glisan and Fastow, throughout the Class Period, discussing Enron's business, financial condition, financial plans, financing needs, its partnerships and SPEs. By its own conduct, Barclays actively engaged in and furthered the fraudulent scheme and fraudulent course of conduct and business, not only making loans to Enron during the Class Period and working with the Company to enable it to raise almost $2 billion from the investing public via the sale of new securities, but also by structuring, implementing and funding bogus transactions which were vehicles utilized by Barclays to deceive Enron's auditors, lawyers, the credit rating agencies and investors in

Enron's publicly traded securities. These transactions falsified Enron's reported financial results by creating the false appearance of legitimate business transactions generating GAAP-compliant revenues, profits and cash flow from operations, when in reality they were bogus and contrived transactions involving shell and sham entities deceptively generating false revenues, phony profits and hiding what was really "***plain ol' debt***."[2]

755.2 Barclays' own conduct actively furthered the fraudulent scheme and course of business that operated as a fraud and deceit on purchasers of Enron's publicly traded securities by engaging in deceptive and manipulative acts in these transactions, the principal purpose and effect of which was to distort Enron's publicly reported finances, thus inflating the prices of Enron's publicly traded securities. Barclays' own conduct, irrespective of how Enron later accounted for the transactions, was fraudulent, as it involved acts of deception, manipulation and the use of contrivances and artifices to deceive which directly impacted and deceived Enron's outside auditors, lawyers, the credit rating agencies and the investors in Enron's publicly traded securities. Barclays demanded secret side agreements inconsistent with formal deal documentation, created and/or used sham/shell entities to engage in deals violating known accounting rules, and structured fictional, circular transactions which deprived the transactions of economic substance and eliminated financial risk to Barclays, knowing such transactions had the principal purpose and effect of distorting Enron's finances. This deceitful and illicit conduct was meant to create the appearance of business transactions of substance, with economic risk to Barclays involving entities that were GAAP-compliant when they were not, thus deceiving Enron's outside auditors and lawyers who had important roles and duties respecting Enron's financial and legal probity, and the credit rating agencies whose investment rating grade for Enron's debt was indispensable to keep the scheme

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[2] Citations and footnotes are omitted and emphasis is added unless otherwise noted.

going. In return for its deceptive and fraudulent acts, Barclays was enriched with huge fees from Enron, payments ***far in excess*** of what it would have received had the transactions been disclosed to be and labeled what they truly were – borrowings. Barclays admitted in its internal documents that "***Enron was always willing to pay higher compensation***" for the deals it did with the bank and Fastow has corroborated these payoffs.

755.3 Barclays was willing to engage in the fraudulent scheme because such conduct provided enormous profits for Barclays which would continue as long as the Enron scheme continued – something that Barclays was in a unique position to ensure. Barclays continued to advance large sums – in actuality loans – to Enron in transactions Barclays deceitfully structured to make them appear to be business transactions, receiving huge fees – well beyond what would have been paid on ordinary loan transactions. These transactions, therefore, had the principal purpose and effect of deceiving the market.

755.4 In addition, Barclays was limiting or eliminating its risk of loss on these and other transactions with Enron with secret no-loss guarantees via structured repurchase arrangements making the transactions themselves inherently deceptive. It also knew that its actions, along with the actions of other banks which were part of the scheme, allowed Enron to wrongfully maintain its investment-grade credit rating and continue to falsely report strong current period financial results and credibly forecast strong ongoing revenue and profit growth, and access the capital markets which allowed Enron to continue to periodically raise hundreds of millions if not billions of dollars of fresh capital from public investors which would be used to maintain Enron's liquidity and repay or reduce Enron's debt, including the loans from Barclays to Enron, so that the process could continue.

755.5 In fact, the proceeds of almost all of Enron's securities sales during the Class Period, including those where Barclays acted as an underwriter, were utilized in significant part to repay

Enron's existing commercial paper and bank indebtedness, including indebtedness to Barclays. Thus, during the Class Period, Barclays was pocketing millions of dollars a year in fees, interest payments, syndication fees and investment banking fees by engaging in the Enron scheme to defraud and stood to continue to collect these huge amounts on an annual basis going forward so long as it engaged in the Enron Ponzi scheme.

755.6 According to Fastow, Enron's CFO, "Barclays, one of Enron's Tier-1 Banks, engaged in at least eight transactions during 1997 to 2001, including Chewco, J.T. Holdings, Nikita, Prepays, Metals and $SO_2$. These transactions contributed to causing Enron to report lower balance sheet debt and created the false appearance of funds flow from operations."[3] Fastow is well-qualified to provide these facts, as he stated he "was involved in all of the [Barclays] transactions because, at a minimum, these transactions were executed by people who ultimately reported to [him]."

755.7 According to Fastow, Enron's most important criteria in choosing its Tier One banks was the financial institution's ability to "lead/structured complex, mission-critical deals." Fastow defined mission-critical deals as "deals that helped [Enron] meet [its] financial reporting objectives." Tier One banks, including Barclays, consistently "[devised] structures and transactions that would help Enron creatively solve its financial reporting problems."

755.8 Fastow would typically outline, as part of his regular dialogue with Barclays' senior bankers, including Barclays' relationship officer on the Enron account, Richard Williams, and others, what Enron's financial problems were that the Company needed to be fixed. According to Fastow, there were three general categories of problems, all of which had an impact on either the credit rating process or the perception of Enron by outside investors; *i.e.*, "The Street." These three

[3] According to Fastow, "In doing these eight transactions, I or my staff met or spoke with Richard Williams, Eric Chilton, John Sullivan, George McKean, Bob Diamond and others at the bank."

areas included: (1) funds flow from operations – Enron in truth and in fact did not have the funds flow from operations necessary to maintain its investment grade rating so it needed the fraudulent deals done by Barclays and others to hide this fact, (2) balance sheet debt – Enron wanted to hide its true debt levels on its balance sheet so it would appear to have a stronger financial condition than it in fact possessed, and (3) income – there were a number of quarters and year-ends where Enron did not have enough income through its regular operations to meet "The Street's" expectations of earnings so deals done only for accounting reasons by Barclays and others were required. In many cases, Barclays created and implemented structured finance deals that Enron executed with Barclays to solve these problems. The "banks brought transaction structures . . . to Enron, and these were transactions that Enron did with the intent of changing the way its reported financials appeared," Fastow said. Barclays regularly brought such structures to Fastow and his staff and effectuated/carried out transactions that concealed Enron's debt and created the false appearance of cash flow from operations and income.

755.9 According to Fastow, Barclays was fully aware of the deceptive and fraudulent purpose and effect of the transactions it created and executed with Enron *i.e.*, the distortion of Enron's financials and deception of investors. Barclays knew Enron desired to alter its financial appearance by perpetuating unrealistic and deceptive reporting. Fastow stated, "***[m]y conversations with senior bankers led me to believe that [Barclays] understood that some of the transactions were done primarily for generating certain accounting benefits and financial-reporting objectives for Enron, including higher funds flow from operations, lower debt and increased (current period) income***." Fastow also stated that, "***[he] believed that an investor would have had great difficulty understanding the true financial condition of Enron due to certain transaction structures and how they were disclosed***." Fastow has testified that "based upon my conversations with [Barclays], based upon the structures that [the bank] brought back to [Enron] to help us solve

[its] problems and based on some internal documents that [he] received from the banks since [he] left Enron, . . . [he] conclud[ed] that [Barclays] understood [Enron's intent] very well." The goal was to make "Enron look healthier to the outside world than it looked internally."

755.10 According to Fastow, Barclays also understood that because it was a Tier One bank, it would "typically get more lucrative business." Enron paid premium amounts to its Tier One banks for creating, structuring and executing deals that concealed Enron's financial problems and changed the way its financials appeared. Fastow stated that Enron was willing to pay banks like Barclays premium fees because the banks "provided extra value to Enron in changing how its financials looked." "They [the deceptive deals] required more work from the bank, [in] either devising the structures or implementing the structures, and [Fastow] believed [Enron] needed to compensate banks who brought [Enron] value like this so they'd continue to bring [Enron] value, additional value in the future." He said the amount Enron paid in premiums for structured finance transactions was "in excess of a hundred million dollars, maybe hundreds of million of dollars."

755.11 Fastow has stated Barclays understood that in connection with these illicit and deceptive transactions, Enron was not seeking to engage in straight ordinary borrowings or "plain vanilla" deals. Barclays knew Enron was willing to pay "premiums – in the aggregate, hundreds of millions of dollars – in order to engage in structured-finance transactions that contributed to causing Enron to report its financial statements in the desired manner." Fastow said that "[he] believed Barclays received fees on these . . . transactions above what it would have earned for standard loans. I discussed the purpose of these transactions with the bankers involved and I believe that they understood they were being paid a premium of the impact of these structures on Enron's public financial statements." Barclays knew that if it "were to compare the amount of cash [Enron] paid the bank in . . . fees and interest or implied interest in a transaction, . . . structured finance transactions were – were typically more expensive than normal borrowings."

755.12 Barclays' deceptive and manipulative conduct in manipulating Enron's finances was coldly – and ruthlessly – calculated conduct engaged in for its own economic gain regardless of the deception or damage it inflicted on others. Because of its conduct, Barclays ***was ranked as one of Enron's "Tier 1" banks for eight years running***; Enron was Barclays "***most important*** relationship in the Energy sector;" and "'Enron [was one of Barclays'] ***most important and profitable accounts***'" and "'among the most profitable of the energy group's clients.'" Barclays knew that "***Enron's tier one banks [received] a disproportionate share of the company's total wallet***," and Enron paid "***higher compensation***" to the banks like Barclays who facilitated its financial manipulations. In other words, Barclays got excess profits for its deceptive conduct while exposing unknowing investors in Enron's public securities to the high risk of huge losses – in the billions of dollars – when the truth came out, the scheme collapsed, the falsification of Enron's financial statements became known and its stock collapsed.

755.13 Fastow has admitted that the principal ***purpose and effect*** of the transactions that Barclays engaged in with Enron was to create the ***false appearance*** of fact and that as a result of those transactions it falsely appeared that Enron was a ***financially healthy*** company. But in fact it was not. Barclays knew that the principal ***purpose and effect*** of the Barclays/Enron transactions identified herein, that it structured for and entered into with Enron, was to disguise the Company's ailing condition from its auditing firm, lawyers, the rating agencies and the securities markets. With that knowledge, Barclays structured, implemented, and executed materially deceptive transactions to mislead investors, analysts and "The Street."

755.14 Barclays itself engaged in deceptive conduct to mislead investors because the bank disguised its transactions with Enron as something other than what they in substance truly were, including, but not limited to, creating the appearance of legitimate commodity swaps, synthetic leases, inventory financings, FAS 125/140 transactions and others with real economic substance and risk when in fact the reality of these transactions was quite different as detailed herein. A summary of the deceptive and misleading transactions involving Barclays is set forth below:

| TRANSACTION/ DATE | BARCLAYS' DECEPTIVE AND COLLUSIVE CONDUCT, CONTRIVANCES, ARTIFICES AND MANIPULATIONS | | ENRON FINANCIAL STATEMENT IMPACT |
|---|---|---|---|
| **JEDI/Chewco: 12/97** | Demanded concealed cash set aside via secret side letter with Enron controlled entities that contradicted formal deal documentation | Fund sham non-GAAP compliant SPE to deceive auditors and others. Mislead external auditors as to "at-risk" equity of SPE and whether transactions qualified for off-balance-sheet status. | Created $405 million false income in 1997-2000; Concealed $685 million debt between 12/31/97-01 |
| **JT Holdings: 12/00** | Demanded Enron's secret promise to repurchase Barclays' 3% "at risk" SPE equity. Created sham/pretend non-GAAP compliant SPE to deceive auditors and others. | Loan based on secret, no loss promise to cover up over-valuation of assets, create false appearence of value. Mislead external auditors as to at-risk equity of SPE and whether transactions qualified for off-balance-sheet status. | Concealed $110 million in debt @ 12/31/00 and thereafter |
| **Nikita/Besson Trust: 9/01** | Demanded Enron's secret promise to repurchase SPE 3% at risk equity to protect Barclays from loss | Created and used sham/pretend non-GAAP compliant SPE; disguised loan as arms-length asset sale. Mislead external auditors as to "at-risk" equity of SPE and whether transactions qualified for off-balance-sheet status. | Created $10 million phony income and $80 million false operating cash flow; hid $80 million in debt @ 9/01 |
| **Nixon Pre-Pay: 12/99-3/00** | Structured contrived commodities trade with circular swaps that eliminated all price/market risk to Barclays | Contrived oil/gas commodity trade to create fiction of legitimate trade and disguise loan to manipulate Enron's financial statement; deceptively structured transactions to create fiction of legitimate trade | Concealed $324 million in debt; created $324 million in false operating cash flow @ 12/99 and 3/00 |
| **Roosevelt Pre-Pay: 12/98-9/99** | Structured contrived commodities trade with circular swaps that eliminated all price/market risk to Barclays | Contrived oil/gas commodity trade to create fiction of legitimate trade to disguise loan to manipulate Enron's financial statement; deceptively structured transactions to create fiction of legitimate trade | Concealed $500 million in debt; created $500 million in false operating cash flow @12/98-9/99 |
| **CSFB Pre-pay: 12/00-9/01** | Structured contrived commodities trade with circular swaps that eliminated all price/market risk to Barclays | Contrived oil/gas commodity trade to create fiction of legitimate trade to disguise loan to manipulate Enron's financial statement; deceptively structured transactions to create fiction of legitimate trade | Concealed $150 million in debt; created $150 million in false operating cash flow @ 12/00-9/01 |
| **Metals (Camelot) I & II: 9/00 & 10/00** | Structured contrived commodities sale with circular swaps to eliminate price/market risk to Barclays; used sham option with Enron's secret agreement to "always exercise" to protect Barclays from loss | Sham/pretend option with secret promise to exercise to protect against loss | Concealed $1.4 billion in debt and created $1.4 billion in false operating cash flow |
| **SO2: 9/01 & 10/01** | Created and used shell/sham non-GAAP compliant SPE; Used fictional/non-economic trades to season SPE; demanded secret Enron promise to repay the SPE "at-risk" equity | Disguised loan by making it look like legitimate sale of $SO_2$ credits. Mislead external auditors as to "at-risk" equity of SPE and whether transactions qualified for off-balance-sheet status. | Concealed $168 million in debt @ 9/30/01 and created $168 million in false operating cash flow @ 9/30/01 |

755.15 Barclays' own action in these transactions had ***a deceptive purpose and effect***:

- Barclays engaged repeatedly in transactions whose sole purpose was to create the false appearance of revenues or cash flow from operations – or to hide debt – to manipulate Enron's financial picture – advancing the overall scheme.

- Barclays created a sham/shell SPE (Colonnade), caused it to do fictitious/meaningless transactions to season it to create the deceptive appearance it was a legitimate GAAP-compliant SPE to deceive Enron's outside accountants and lawyers into thinking $SO_2$ was an arm's-length, bona fide commodities transaction with Enron.

- Barclays structured fictitious and ***circular*** prepaid commodities transactions to make them deceptively look like real commodities trading actions, but secretly structured them to eliminate any price or market risk to the bank, disguising what, in truth, were loans to Enron.

- Barclays ***demanded secret side agreements*** that contradicted the formal deal documents to create sham – pretend – SPEs that did not meet the 3% "at risk" equity test so Enron's outside auditors or lawyers would be deceived as to the true nature of the deals if, as or when they examined them.

- Barclays engaged in deceptive conduct in funding transactions, knowing the assets involved were overvalued, making it appear the underlying assets had substantial value, while accepting ***secret promises*** that shielded the bank from the risk of that undervaluation or loss on the transaction.

- Barclays engaged in fictional commodities trades which it knew were not legitimate trades, to eliminate all price and market risk to itself and where no commodities were ever meant to be traded or delivered. Rather, the truth was the transactions were loans to Enron with riskless, fixed-rate returns to Barclays.

755.16 This illicit conduct by Barclays also enabled it to obtain other economic benefits from the scheme by being treated as one of Enron's favored, *i.e.*, "Tier One" banks, thus inducing Enron to allow it to have a role in other Enron transactions from which Barclays received substantial profits. Because the Barclays' bankers involved were financially sophisticated, and knew Enron was a public company with publicly issued financial statements, they knew the distortion of Enron's financial statements, which was caused by the transactions they put together and engaged in, would necessarily have a deceptive impact on purchasers of Enron's securities exposing them to a significant risk of economic loss and damage due to the artificial inflation of Enron securities.

755.17 As set forth in The Reports of the Bankruptcy Examiner, Neal Batson ("Batson" or "Bankruptcy Examiner"), Appendix F (Role of Barclays and its Affiliates), Third Interim Report of Neal Batson, Court-Appointed Examiner ("Batson III, App. F"), the independent examiner Batson[4] concluded:

> Barclays' ***conduct*** in respect of the Chewco Transaction, the J.T. Holdings Transaction, the Nikita FAS 140 Transaction, the $SO_2$ Transaction and the three Prepays ***enabled*** Enron to: (i) record approximately $410 million of income that should not have been recorded; (ii) receive cash flow from financings of approximately $1 billion, all of which Enron erroneously recorded as cash flow from operating activities; and (iii) erroneously omit almost $1.77 billion of debt in its 1997, 1998, 1999, 2000 and 2001 financial statements.
>
> Enron erroneously omitted approximately $685 million in debt between 1997 and 2001 as a result of failing to consolidate Chewco (and JEDI); approximately $106.2 million in 2000 as a result of the J.T. Holdings Transaction; approximately $71.9 million in 2001 as a result of the Nikita Transaction; approximately $138.5 million in 2001 as a result of the $SO_2$ Transactions; and a total of approximately $760 million as a result of its conduct in Prepay Transactions, of which $500 million occurred in 1998, $100 million in 1999, and $150 million in September of 2001. *See also* Report, Appendix F (Role of Barclays and its Affiliates); First Interim Report, Section III, The Nikita Transaction: Second Interim Report, Annex 2 to Appendix M (FAS 140 Transactions); First Interim Report, Section III, The $SO_2$ Transaction; Second Interim Report, Annex 1 to Appendix F (Miscellaneous Transactions); Second Interim Report, Annex 1 to Appendix L (Related Party Transactions); and Report, Appendix D (Role of Citigroup and its Affiliates).

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[4] The Batson Reports have been appropriately incorporated by reference by Lead Plaintiff throughout its pleadings and those Reports relating to Barclays are incorporated in this amended complaint. *See* Exs. A-G attached to the Appendix of Exhibits Incorporated by Reference Into the Supplement to the First Amended Consolidated Complaint (Docket No. 1388) As to Barclays Filed Pursuant to the December 4, 2006 Order (Docket No. 5242) ("Complaint Appendix") filed concurrently herewith. This Court's December 22, 2005 Order described Enron North America's Court-Appointed Bankruptcy Examiner Harrison J. Goldin's report to the bankruptcy court regarding transactions with Enron-related special purpose entities as a "central part of the complaint" and explained that "[g]enerally Federal Rule of Civil Procedure 10(c) allows a party to incorporate 'any written instrument which is an exhibit' to a pleading." *In re Enron Corp. Sec. Litig.*, No. H-04-0087, 2005 U.S. Dist. LEXIS 41240, at *35, *40 n.20 (S.D. Tex. Dec. 22, 2005). In *In re WRT Energy Sec. Litig.*, the court agreed that "[i]t is proper for the Court to rely on the Bankruptcy Examiner's Report because it is attached to the Complaint, and as such can be considered." *In re WRT Energy Sec. Litig.*, No. 96 CV 3610 (JFK), 1999 U.S. Dist. LEXIS 3883, at *40 n.9 (S.D.N.Y. Mar 31, 1999).

***The evidence would allow a fact-finder to conclude that Barclays***:

- ***Obtained verbal assurances*** from Enron in which Enron promised to cover Barclays' equity risk positions in two SPEs, likely knowing that the assurances would not be disclosed to Enron's auditors and that, had they been disclosed, Enron could not have accounted for the transactions as it did;

- ***structured and closed*** the $SO_2$ Transaction knowing the transaction was not a "true sale," that it was designed to manipulate the Debtors' financial statements, and that it resulted in the dissemination of financial information known to be materially misleading;

- ***caused*** Enron to structure a [Chewco] transaction involving an SPE such that Enron covered 60% of the equity risk position in the SPE, knowing that would prevent Enron from properly giving the structure off-balance-sheet accounting treatment; and

- ***participated in*** three Prepay Transactions and one monetization transaction that Barclays knew were designed to manipulate the Debtors' financial statements and did result in the dissemination of financial information known to be materially misleading.

***Note the emphasis on Barclays' conduct***, ***which was inherently – indeed – deliberately deceptive***.[5]

755.18 Barclays' own conduct created deception when it demanded and received verbal assurances against risk and/or loss on transactions it did with Enron. Fastow has stated "Barclays ***required assurances or structural enhancements to certain transactions in order to minimize Barclays' financial risk. I intended those assurances to operate as guarantees, and I do not believe that Barclays would have entered into the transaction without them." "[T]hese assurances or structural features were critical in order for them [Barclays] to do the deals." According to Fastow, these guarantees were given secretly – and orally – so that there would not be a written record of the assurances that would have confounded the desired accounting treatment and revealed the transactions for what they truly were – loans***. According to Fastow, Barclays

[5] The conclusions of the Batson Report were backed up by pages and pages of detail, including sworn statements of present and former Barclays personnel and internal Enron and Barclays documents which had been obtained by the Bankruptcy Examiner through the authority of the bankruptcy court.

concealed the fact that "they wouldn't lose money" and that it would "receive . . . a predetermined return on their investment . . . in a defined period of time" by accepting the assurances orally rather than including the guarantees in the deal documents. Therefore, Barclays ***own conduct*** concealed the true nature of the transactions and made the deals outwardly misleading.

755.19 Fastow has said this pattern of concealment by Barclays and Enron became commonplace, Barclays began to accept the oral guarantees from others at Enron, lower down the reporting chain than Fastow, including Treasurer Ben Glisan. Fastow explained to Barclays why Enron was obliged to honor their oral guarantees:

> ***What I would typically say to bankers, Barclays included, was that it's just not – the way they should look at those investments and the three percent equity is that it is not in Enron's interest to have the bankers lose any money on such a small dollar amount because I understood, as CFO of Enron, that if they lost money in those, they wouldn't do any more of those types of transactions***.
>
> ***It might result in the curtailment or elimination of the lending from Barclays to Enron and that I would be concerned that Barclays would let our other important banks know that they had lost money. And all of this together might result in the banks not doing business with Enron anymore, which would be devastating for the company***.
>
> ***So to boil that down, what I meant to tell them was if we let you lose money on this little investment, my view is it might kill Enron***. So I wanted his take-away to be for a few million dollars, or whatever it was, he's not going to – he's not going to put Enron at risk.
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> * * *
>
> ***I believe I was clear in what I said. My intent was to convey a very strong assurance to them that they wouldn't lose money***, and they – in most cases, they engaged in the transaction following my conversation with them.

Moreover, Barclays could look to what the bank described as, and Fastow agreed was, as Barclays' senior credit officer John Meyer wrote in the "Post-Mortem" document in the Spring of 2002, Enron's "history of protecting lenders to its SPVs, either through overcollateralization, a tight structure or verbal assurances that often translated into near virtual guarantees."

755.20 Barclays did all of the above with a full understanding of the 3% independent equity at risk rule it was circumventing via deception and contrivances. Fastow has testified that he and Richard Williams of Barclays had conversations about the 3% equity at risk rule. "[M]y take-away from our conversation was that he understood – that we both understood what it meant." Fastow and Williams understood "the three percent is meant to be equity and that the owner of that equity ought to enjoy certain risks and rewards associated with that equity." Nevertheless, Barclays required and accepted verbal assurances which directly subverted *i.e.*, eliminated, the risk required by the rule for the accounting on those transactions to be legitimate.

755.21 Barclays' conduct involved acts undertaken voluntarily and knowingly – acts falsifying Enron's financial situation and deceiving investors. As early as 1999, one of Barclays' top managers in London, Jonathan Taylor, internally expressed concern about "***the way [Enron] conducts business" concluding that Enron was "extremely creative about their financial engineering and they appear to be able to make their published figures read just about anything they want them to***." In considering one of Enron's requests that Barclays provide money, he noted that Enron was "***so desperate for the money***" that it looked like a company "***pedaling harder and harder to stay ahead of the wolves***," observing that Enron's figures concerning a proposed contrived "prepay" deal were "***the same smoke and mirrors that the group is so expert at using***." This e-mail was sent to Richard Williams, John Meyer, George McKean, Brian Smith and Ian Jefferson, some of the top Barclays' bankers. Barclays knew Enron wanted it to engage in transactions with Barclays solely to manipulate Enron's financial statements to hide its actual debt levels, *i.e.*, deceive investors. As senior credit officer, John Meyer, wrote in response to Taylor's e-mail, "***[d]on't for a second think that Enron is satisfying an operating need by selling these commodities forward . . . in actual fact, they are only borrowing money***" and it was to Barclays "***painfully obvious that the transaction's essence is not about deferred revenue, but rather about plain ol' debt***."

755.22 In the spring of 2002, Barclays prepared a "post-mortem" of the bank's dealings with Enron, detailing the bank's conduct regarding Enron over the previous years. The document was drafted by John Meyer at the direction of Bob Clemmens, Barclays' Chief Credit Officer at the time. Meyer testified that he wrote the document. This document detailed Barclays' ***own conduct*** in furtherance of Enron's financial fraud. It acknowledged that Enron had a history of protecting lenders to its SPV's through ***verbal assurances that translated into*** "***guarantees***," and that "***Enron was always willing to pay higher compensation***" for this type of complicity. It acknowledged that the purpose for its transactions with Enron "***was mostly to achieve an accounting objective rather than shed risk***," and that "the driving force for ***each*** SPV transaction was to raise debt that was either (i) ***off the balance sheet entirely*** or (ii) if on the balance sheet, then ***disguised*** as an operating liability." Barclays ***admitted*** that verbal assurances from Enron were "***near virtual guarantees***" in deals "***transacted purely for accounting reasons***." Similarly, the total return swaps it engaged in with Enron ***were "preferable" to outright guarantees because "it was less obvious on the financial statements***." This is not the description of normal arm's-length business dealings or of transactions engaged in for legitimate business purposes with actual economic risk, which were later transmogrified by a dishonest issuer's accounting. To the contrary, it describes years of deals artificially structured by Barclays to avoid economic risk, secret side deals it extracted to conceal the true nature of the transactions, and secret agreements and promises to protect Barclays against loss or protect it from the risk of loss on assets it knew to be overvalued – to deceive Enron's accountants and/or lawyers (and others), seasoned with extra profits to pay off Barclays!

755.23 Internally, Barclays understood that its Enron transactions, in the words of John Meyer, allowed debt to "***masquerade***" as something else on Enron's financial statements. When calculating Enron's true debt levels for its own purposes however, which it did for years, Barclays ***reclassified Enron's structured financings with it (and others) as debt, stressing that it was*** "***essential [to] take these considerations into account***" when calculating Enron's leverage or its actual cash flow. As a result of these internal calculations, Barclays knew, for example, that Enron's actual year-end 1998 debt was at least $11.9 billion as opposed to the publicly reported amount of $7.4 billion – ***a 38% understatement***. Barclays calculated Enron's true debt in 1999 as at least $14.3 billion rather than the $10.7 billon Enron reported – a 25% understatement. This pattern continued in 2000 when Barclays added back $6.1 billion onto Enron's balance sheet. Because of this hidden debt, Barclays' highest sanctioning body noted in the minutes of its meeting on July 7, 1999 "***that Enron was paddling underneath the surface to hold on to its investment grade status***."

755.24 In each of Barclays' transactions involving Enron that are detailed in the following paragraphs, the principal purpose and effect was to create the false appearance of fact – to conceal and/or disguise the true nature of the transaction – which enabled the falsification of Enron's financial statements. In each instance, Barclays' ***own conduct*** in the transactions had a deceptive purpose and effect which created the appearance of economic substance and risk in transactions that were, in truth, fictional deals without risk to Barclays, not entered into for any legitimate purpose but only to falsify Enron's real financial condition and deceive investors, while generating large payments to Barclays to pay it off for its conduct in engaging in the scheme.

## DETAILS OF SPECIFIC TRANSACTIONS

### JEDI/Chewco – December 1997

757.1 The JEDI/Chewco transaction at year-end 1997 served as a template for frauds engaged in by Enron, Barclays and other banks over the following years. While it predates the Class Period, JEDI/Chewco shows Barclays' intent, knowledge and method of acting in the scheme to falsify Enron's finances.[6] As Barclays acknowledged in an internal e-mail discussion, "this [was]

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[6] The Court previously held:

not a structure [it] would consider for just anyone." Barclays and Enron created and funded a non-GAAP-compliant entity that they ***used at year-end 1997 and continued to use from 1998-2001 to falsify Enron's reported financial condition***, thus furthering the Ponzi scheme during the Class Period.

758.1 Chewco was an SPE set up and financed by Barclays and Enron at year-end 1997 to take the place of CalPERS in an existing joint venture known as JEDI. Enron had been properly accounting for transactions with the entity and the debt of JEDI was properly "off-balance sheet," as CalPERS was independent from Enron. But, if CalPERS withdrew from JEDI, then JEDI's debt would have to be put on Enron's balance sheet – something Enron had to avoid. In order for JEDI to remain unconsolidated, *i.e.*, "off balance sheet," some entity had to take over CalPERS' 50% interest. Chewco was formed to buy CalPERS' interest. Barclays and J.P. Morgan were to loan Chewco the purchase price money (guaranteed by Enron). If Chewco was a legitimate SPE, it could be considered independent of Enron – ***but if and only if***, Chewco had an investor ***independent*** of Enron with at least 3% "***at risk***" equity. Barclays' demands in the deal caused Chewco to fail this test.

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> Lead Plaintiff has responded that it is not seeking to recover damages for alleged misconduct that occurred more than three years before the suit was filed, but is pleading such purported violations solely to establish evidence of a scheme and of scienter. Such evidence is admissible for this purpose. ***The Court agrees and considers those allegations to be admissible solely for the purpose of establishing a scheme and/or scienter***.

*In re Enron Corp. Sec. Litig.*, 235 F. Supp. 2d 549, 689 (S.D. Tex. 2002). Regardless of its lack of liability impact, Barclays' conduct surrounding JEDI/Chewco is relevant to show the existence of the scheme and Barclays' conduct in it, as well as proof of "motive, intent, preparation, plan, or knowledge," as it is one of several transactions which Barclays, as part of a pattern of conduct, engaged in. *See* Fed. Rules of Evid. 404(b).

758.2 Barclays loaned the 3% equity money to the Chewco investors (basically limited partnerships controlled by Enron employees). Barclays, knowing of the 3% independent equity "at risk" rule, nevertheless insisted its 3% advance of the equity money ***not bear risk*** and rather be substantially protected by a ***secret*** side agreement with Enron, creating millions of dollars of secret offsetting cash deposits into cash collateral accounts which reduced the $11.49 million equity loan it had provided to purportedly meet the 3% "at risk" equity requirement by more than 50% – to $6 million. These secret cash accounts were established at Barclays' insistence and placed at Barclays, under its control. Thus, due to Barclays' ***conduct*** in requiring the secret side deal, secretly holding onto over $6 million of the supposed Chewco "at risk" equity, Chewco was a sham entity,[7] an imitation, pretend SPE – not a legitimate, GAAP-compliant SPE as it never had 3% "at risk" equity. Due to Barclays' own conduct, this contrived arrangement presented the false appearance of fact, *i.e.*, that Chewco was a legitimate SPE, GAAP-compliant with $11.49 million in at-risk equity and that the Chewco purchase of CalPERS' JEDI interest was a legitimate arm's-length business

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[7] The term "sham" has a ***very broad*** meaning:

*Black's Law Dictionary* 1407 (8th ed. 2004):

- Sham: ***Something that is not what it seems*** . . . .

Merriam-Webster OnLine, http://www.m-w.com (last visited Dec. 28, 2006):

- A ***trick*** that deludes . . . .
- An ***imitation*** . . . purporting to be genuine.

Ask Oxford, http://www.askoxford.com (last visited Dec. 28, 2006):

- Noun: 1. a person or thing that is ***not what they are claimed to be***. 2. pretence
- Adjective: ***bogus***, ***false***.
- Verb: (shammed, shamming) pretend or ***pretend to be***.

Wordnet Princeton University, http://wordnet.princeton.edu (last visited Dec. 28, 2006):

- feign: ***make believe with the intent to deceive***.

deal when it was not. This avoided putting millions in debt on Enron's balance sheet and allowed Enron to record millions of dollars of revenues from transactions with a non-independent entity ***in later years***, 1998-2001, during the Class Period. Meanwhile, Barclays received handsome fees for its part in the scheme and was repaid every penny of the money it invested in the deal.

758.3 Barclays knew that Enron wanted to keep JEDI "***off balance sheet***," *i.e.*, to avoid reporting millions in debt on Enron's balance sheet and that this was, as Henry Pullman, Director of Barclay's Credit Risk Management Division, wrote in an e-mail: "***JEDI's raison d'etre***." This was understood to be the ***sole purpose*** of the Chewco SPE involvement in the deal, as Enron had guaranteed 100% of the JEDI purchase price loan to Chewco by Barclays and J.P. Morgan, and thus there had to be a 3% independent, "at risk" equity in Chewco for it to be a legitimate, GAAP-compliant SPE. For this to occur legitimately via an arm's-length transaction with a GAAP-compliant SPE, Barclays knew that the Chewco entity had to have at least 3% equity ($11.49 million) "at risk" at all times during the transaction. Barclays' bankers were financially sophisticated and familiar with structured finance transactions, which they knew were done to achieve specific financial statement impact for public companies. They also knew that a transaction of this size – especially given its year-end timing and Enron's explicit guarantee of the purchase price loan – would likely attract the attention of Enron's auditors, who ***would carefully examine the transaction for its strict compliance with the 3% "at risk" equity requirement***.

758.4 The "official" documentation of the JEDI/Chewco deal, including Barclays' JEDI Loan Revolver, expressly contemplated and provided for 3% independent at-risk equity – which made the deal look legitimate. To fund the transaction, Enron caused JEDI to make a special $16.6

million distribution to Chewco.[8] However, a secret side letter agreement dated December 30, 1997 (the "Chewco Side Letter"), required that part of the $16.6 million would be used to "fund . . . reserve accounts [at closing] . . . in [an] amount equal to $6,382,600" held at Barclays. This was done in response to Barclays' demands that the Bank be shielded from the required risk in the transaction. The cash offset reserve accounts reduced Chewco's 3% purported equity investment of $11.49 million by $6.58 million. This negated the 3% "at risk" equity that supposedly existed according to the formal deal documentation – ***including Barclays' JEDI Loan Revolver Agreement***. Barclays' secret cash offset reserve accounts were not mentioned in the official deal documents. Because of Barclays' conduct, Enron auditors looking at the deal documents would be deceived, seeing a fictional transaction with a 3% equity "at risk," GAAP-compliant SPE involved. Deceiving them was a necessary step to falsifying Enron's financial statements and deceiving Enron's investors.

758.5 Chewco was never a legitimate SPE meeting the requirements for non-consolidation treatment because the 3% equity investment in Chewco was ***never*** at risk. It was a sham, giving the appearance of an SPE that was compliant with the accounting rules when, in fact, it violated them. The Chewco equity investment, which Enron and Barclays structured together, was never at risk because Barclays demanded that a huge secret cash offset – called "***reserve accounts" – be established with it to effectively reduce Barclays' loan of the equity money***, so there would be no risk of loss to it or to the Chewco "investors" of the offset amount.[9] The cash offset accounts gave

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[8] In late November, JEDI had sold one of its assets. Chewco's proceeds of that sale were $16.6 million.

[9] Chewco was structured as a limited partnership – Big River Funding was its limited partner. Michael Kopper, an Enron employee who controlled Big River, was the sole owner and manager of Chewco. At the time, Kopper was employed by Enron's Global Capital department which became the Enron Global Finance group headed by Fastow. Barclays was well aware of Kopper's many hats

Barclays millions in ***cash collateral*** which it held at all times. As a result of Barclays' conduct, Chewco's equity at risk was ***always less than 3%,*** making Chewco a sham – not a legitimate – SPE.

758.6 ***The Chewco Side Letter was dated December 30, 1997, the same date as the Chewco closing***. Of course, it is "***unusual***" to have a side letter dated the same date as the closing documents. As Andersen expert John Foster stated, one "***would expect to see the terms of the agreement in the main documents***." Moreover, ***the Chewco Side Letter was created in advance of the execution of the JEDI Revolver with Barclays – but its terms, which secretly modified critical provisions of the JEDI Revolver, are neither contained nor referenced in the JEDI Revolver***. Barclays knew this. A ***draft of the Chewco Side Letter was sent to George McKean at Barclays on December 6, 1997, before the close of the Chewco transaction. Barclays' bankers have admitted that the Chewco Side Letter was also a part of Barclays' documents for the Chewco transaction***. Therefore, the Chewco Side Letter was not memorializing an additional or new agreement between the parties that was arrived at after the deal closed as one would expect from such a document. Instead, it was a preconceived agreement that impermissibly shielded Barclays from risk while hiding that fact from Enron's auditors by not including the substance of the deal in the primary transaction documents. Why would an auditor ask about the existence of a side letter dated the same day as closing documents which claimed to be a complete representation of the parties' agreement? The Chewco Side Letter that Barclays demanded and received to impermissibly shield itself from risk on the deal was inherently deceptive.

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in the transaction but engaged in the deal anyway. Big River's sole member was Little River Funding. The required 3% equity for Chewco to be a legitimate SPE was $11.49 million. Barclays made the "equity loans" to Big River (Chewco's limited partner) and Little River (Big River's sole member). But, before it would make the loans, Barclays required Big River and Little River to set aside $6.6 million in cash "reserve accounts," which were held by Barclays – beyond the control of Big River and Little River. This effectively reduced Barclays' equity loan to $5+ million, far less than 3%.

758.7 This fiction that Chewco was a legitimate SPE ***directly*** falsified Enron's financial statements – by hundreds of millions of dollars as detailed below – because Chewco, as Barclays knew, was actually structured and financed in such a way that it should have been consolidated into Enron's financial statements from November 1997 and on through 1998, 1999 and 2000. The ***sole*** purpose of the JEDI/Chewco transaction was to avoid the reconsolidation of JEDI on Enron's balance sheet at year-end 1997, so Enron could do financial transactions with JEDI to generate phony profits and hide debt going forward. All this depended on Chewco appearing to be a legitimate SPE, which false appearance was created by way of the secret Chewco Side Letter and cash offset demanded by Barclays.

758.8 Fastow confirmed the fraudulent nature of Chewco/JEDI. He confirmed Barclays' own conduct created deception when it entered into a secret side agreement, memorialized by the Chewco Side Letter, that altered the revolving credit facility underlying the Chewco transaction. The Chewco Side Letter required that cash collateral accounts be funded at closing and that destroyed the 3% independent equity at risk requirement. He said:

> I and Michael Kopper, who had a carried interest in Chewco, controlled the entity. I believe that Chewco should have been consolidated with Enron because it did not have at least 3% at-risk equity, which was required for SPE accounting of the entity. Chewco did not have 3% at-risk equity because of two structural features, including one in which ***Barclays required*** that its equity loan be partially secured by cash collateral.
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> ***The bank required that cash-reserve accounts be established at Barclays in order to provide security for its loan that funded the 3% equity. I discussed with senior Barclays executives how the cash-reserve account would become funded. The process is described in a side letter***.

758.9 To someone looking at Enron's financials, it would appear that there was equity at risk in the Chewco transaction when in fact the required equity was not at risk because the deal was back levered.[10] Thus the disparity between the fiction of the JEDI Revolver and Enron's financials and the reality of the Chewco Side Letter is significant. As Fastow stated:

> ***My understanding of the side letter is that it, in essence, changed the way proceeds were distributed within the JEDI and Chewco structure [by modifying the JEDI Revolver]. So in this particular instance, my recollection is that JEDI was disposing of an asset called Coda and the proceeds of that asset, instead of dropping through the normal, what I call waterfall, or application of proceeds formulas, – this side letter caused the proceeds to be able to circumvent the normal waterfall and go at least in part to these reserve accounts***.
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> * * *
>
> ***[T]he modification was done to accommodate Barclays' requirement that they have less risk in the equity***.

758.10 Fastow spoke directly to Richard Williams of Barclays regarding the Chewco Side Letter's effect on the waterfall provision of the JEDI Revolver:

> ***[M]y take-away from my discussion with Mr. Williams was he was very familiar with how [the deal] worked. The concern he expressed to me was whether, in fact, the cash would, – from the Coda sale, would be realized, and that he understood that, if realized, it would follow the application of proceeds outlined in the side letter***.

758.11 Enron followed through with Barclays' structural requirements for the Chewco deal and funded the cash collateral accounts held at and controlled by Barclays. According to Fastow:

> [T]here were what I would call cash collateral accounts, or at least an account that was established, in order to make sure that there were some proceeds available to repay what I refer to as the equity loan or Barclays' proceeds that they had put into the deal through . . . one of Michael Kopper's partnership. . . . My understanding, from talking with Mr. Kopper, was that this [partially securing the equity loan was] . . . something that was necessary in order to complete the transaction in the manner we wanted to complete it.

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[10] Fastow defined back levering as "borrowing money, which would then be used . . . as dollars to make an equity investment."

Furthermore, Fastow testified: "My view is that the cash collateral in . . . that reserve account or accounts made the equity less risky than it otherwise would have been without those reserve accounts."

758.12 The ultimate effect of Barclays' misconduct is evident. As Fastow stated: "[I] think, as a result of Chewco purchasing the – the CalPERS' interest, Enron was able to record earnings that were substantial – in my opinion, a substantial part of that year's [1997] earnings." And "***I believe it contributed [to Enron's reported earnings], to some degree, in those in – at least some years subsequent to '97***."

758.13 The deceptive nature of Barclays' conduct in this transaction between Enron and Barclays is confirmed by Andersen partners who have stated that they had no knowledge of the secret side deals present in Chewco and that, had they known of these secret deals, which were not in the official deal documents, Andersen would ***never*** have approved the accounting for these deals.

758.14 Carl Bass, an accountant in Andersen's Professional Standards Group, called the Chewco transaction "***the Chewco concealment***." The secret side letter which modified the Barclays' JEDI revolver, and negated the controls for maintaining 3% "at risk" equity, was not seen by anyone at Andersen. "***[I]t had been concealed from us***." Bass stated, this "***critical document***," changed the accounting treatment and that collusion existed between Barclays and Enron in the "Chewco concealment." He said:

> Well, as I – as I talked about yesterday, if we became aware of oral side agreements or collusion between management and management and third parties, then it would require us to conduct an investigation to determine whether or not – obviously, the impact on the accounting of those transactions, as well as whether or not our opinions should stay in force.

758.15 Debra Cash, an Andersen partner who worked on Chewco, has said "Barclays knew about such arrangements [the reserve accounts] and, in essence, ***misled Andersen***" in not disclosing those. Cash explained why she believed Barclays had misled Andersen:

> [M]y understanding, given the sophistication of an entity of Barclays' size and stature – was aware of the implications of such an arrangement, which may lead me to believe that they understood the accounting impact, entered into such arrangement anyway, and that such arrangements was known not to be known by Andersen.

758.16 Stephen McEachern, an accounting expert saw "evidence that there were secret oral agreements, some of which were later reduced to writing and remained secret; some that were put in writing initially and remained secret." ***He found there was collusion between Enron and Barclays on the Chewco*** deal – the side letter shows a deceptive purpose in connection with the funding of the reserve accounts in Chewco and "***prevention of detection was also key***."

758.17 John Foster, another accounting expert, confirmed that Enron and Barclays intended to conceal material information from Andersen in the Chewco transaction. Indeed, he said there was no reason – other than to escape detection – for the secret side letter and cash offset reserve accounts to exist in the Chewco transaction:

> ***After the collapse of Enron, it was discovered that there was a secret side agreement between JEDI and Chewco, that provided for the funding of a reserve account that was dedicated to protect Barclays's equity investment in Chewco. Andersen was not aware of the existence of the side agreement***. The effect of the reserve account was to reduce Barclays's investment at risk in Chewco to well below the 3 percent required by Issue 90-15. Consequently, Chewco failed the 3 percent equity at risk test at its inception and should have been consolidated by Enron. By consolidating Chewco, Enron would have held 100 percent of the partnership interests in JEDI, and accordingly would have controlled, and thus consolidated, JEDI as well.

758.18 Andersen never had the chance to fully determine the impact the Barclays' secret side deals had on the accounting of Chewco in 1997-2001 because, due to Barclays' actions, the true facts were withheld from it ***– the JEDI/Chewco deal Andersen saw was a fiction –*** one involving a legitimate, GAAP-compliant SPE, the key to the accounting treatment utilized.

758.19 However, once Andersen found out about the Chewco Side Letter, Andersen withdrew its audit opinion and Enron was forced to restate, in part, based on the reserve accounts Barclays demanded which destroyed the off-balance-sheet treatment. When it came out that there was the secret side letter and Chewco was a sham SPE, it was apparent that JEDI should have been consolidated with Enron from 1997 on.

758.20 The Batson Report – which this Court has relied upon in the past and is incorporated here – concludes that Chewco was never a valid SPE, the entire JEDI/Chewco deal at year-end 1997 was a fraud and that post-1997 Enron/JEDI transactions based on its false structure were also illegitimate. These facts would cause a fact finder to conclude that Barclays "***caused*** Enron to structure a transaction involving an SPE such that Enron covered 60% of the equity risk position in the SPE, ***knowing*** that would prevent Enron from properly giving the structure off-balance sheet accounting treatment." Consolidation was required by the true facts but avoided by Barclays' ***acts of deception***. This resulted in a large reduction in Enron's reported net income and a massive increase in its reported debt.

758.21 According to expert Saul Solomon, the JEDI/Chewco deal:

- eliminated $405 million in income over the period primarily related to the elimination of earnings related to the appreciation of the Enron stock held as an investment in JEDI,
- reduced equity by an aggregate of $800 million at December 31, 2000 to reflect elimination of earnings Enron had recorded related to gains on the Enron stock held by JEDI . . . to reflect elimination of $179 million in amounts previously due from JEDI related to settlement of swaps related to the Enron stock held by JEDI, and to reflect a reduction in treasury stock related to the shares of Enron stock held by JEDI, and
- increased debt by $711 million at December 31, 1997 and $628 million in debt at December 31, 2000 which reflects the addition of debt recorded on Chewco and JEDI's financial statements.

758.22 Every governmental agency or examiner that has looked at the year-end 1997 JEDI/Chewco transaction has concluded it was fraudulent. The SEC complaint against Fastow states that Chewco "failed to meet SPE non-consolidation requirements" and "should have been consolidated onto Enron's financial statements beginning the fourth quarter of 1997." *United States*

*Securities and Exchange Commission v. Andrew S. Fastow*, No. H-02-0665, Complaint (S.D. Tex. Oct. 2, 2002) at ¶¶29, 32. The JEDI/Chewco deception resulted in criminal prosecutions and pleas.

758.23 Barclays' ***own deceptive conduct*** in the JEDI/Chewco deal was a key part of the scheme. Like CIBC-Braveheart, there was a secret side agreement regarding the bank's financial commitment to a key part of the deal that eliminated risk and destroyed the legitimacy of the SPE involved, rendering it a sham and the accounting that depended on its legitimacy false. Like Merrill Lynch and the barge deal where a secret repurchase agreement caused the transaction to be a sham sale, here there was a secret side agreement with Barclays that deprived this transaction of a critical and necessary component – 3% "at risk" equity – for it to be legitimate, causing it to be a sham SPE.

758.24 In summary, regarding Chewco:

- Barclays knew JEDI's "*raison d'etre*" or reason for being was to hide debt off Enron's balance sheet.

- The Chewco Side Letter was created in advance of the execution of the JEDI Revolver with Barclays, but its terms, which secretly modified critical provisions of the JEDI Revolver, are neither contained nor referenced in the JEDI Revolver. Barclays knew this and agreed to it for the purpose of hiding the truth and impermissibly securing its investment. A draft of the Chewco Side Letter was sent to George McKean at Barclays on December 6, 1997, before the close of the Chewco transaction. Barclays' bankers have admitted that the Chewco Side Letter was also a part of Barclays' documents for the Chewco transaction.

- The Chewco Side Letter agreement regarding the reserve accounts, dated December 30, 1997, the same day as the formal deal documents, deceived the auditors, as the content of the side letter was not included in the deal documents. This is clear evidence of Barclays' deception.

- Because Barclays had 60% cash collateral at closing in the reserve accounts held at the bank, the requisite 3% equity was never at risk.

758.25 Thus, as to the Chewco/JEDI transaction, Barclays actually used or employed a shell or sham entity, *i.e.*, Chewco, as a deceptive device and/or contrivance to:

(i) create the appearance of substance where it was lacking, *i.e.*, by requiring reserve accounts which ensured Barclays would have access to more than 60% of its supposed "equity investment" at closing, thus bringing its 3% independent at-risk equity portion well below what was required by the accounting rules which Barclays was familiar with. Additionally, Barclays saw a draft of the Chewco Side Letter regarding the reserve accounts prior to closing and knew this side letter would modify the JEDI Revolver;

(ii) create a fiction, *i.e.*, that Chewco was capitalized with at least 3% independent at-risk equity when Barclays knew that they would have access to more than 60% of the "equity" at closing because of the secret Chewco Side Letter which modified the main deal documents; and

(iii) create a false appearance of substantial revenues or operating cash flow which falsified Enron's financial statements.

759.1 In engaging in this conduct in JEDI/Chewco transaction, Barclays engaged in an act or practice which operated as a fraud or deceit in connection with the purchase or sale of Enron's publicly traded securities, and combined with all of the Barclays/Enron transactions complained of between 1997 and 2001, a scheme and course of business that operated as a fraud or deceit on those purchasers of Enron's publicly traded securities.

760.1 Barclays acts in connection with the JEDI/Chewco transaction created the appearance of a legitimate or conventional financing transaction when, in fact, it was a bogus transaction. Without Barclays' conduct in this bogus transaction, there would not have been a sham deal.

761.1 The principal purpose and effect of the Chewco fictional transaction was to create the false appearance of fact. Namely, that JEDI was a properly unconsolidated entity which did not show upon Enron's balance sheet. This was done with Barclays playing a key role to falsify Enron's accounting and deceive the rating agencies, Enron's auditors and ultimately, investors in Enron stock and other publicly traded securities.

761.2 Barclays' conduct in the JEDI /Chewco transaction significantly contributed to and, as part of the scheme alleged by Lead Plaintiff, had the foreseeable effect of concealing the risk that Enron would be unable to service its debt and end in bankruptcy, thereby causing plaintiffs' losses.

**$SO_2$ – September/October 2001**

761.3 Barclays and Enron engaged in two $SO_2$ transactions in September and October 2001, providing Enron with $167.6 million in funds through a concealed loan disguised by Barclays as a "sale" of Enron $SO_2$ credits.[11] The "sale" was to a sham SPE called Colonnade, created and run by Barclays, in a deal Barclays structured in a circular manner to eliminate economic risk or risk of loss to Barclays, rendering the sale fictional. Colonnade was a ***sham – a shell –*** from its inception. ***It was capitalized with a mere $2 and had no employees***; it had no business office; Barclays paid its legal fees; and it did no business other than deals conducted by Barclays with Enron. In fact, after a "contest" to name the SPE, Barclays settled on the name Colonnade, the name of the street where Barclays' UK headquarters is located. Colonnade was simply a front for Barclays. Barclays knew that since it set up and controlled Colonnade, any transactions it had with Colonnade would not be arm's-length.

761.4 In fact, the sole purpose of the $SO_2$ transactions was to create the false appearance of funds flow from operations for Enron. A Barclays $SO_2$ Executive Summary explains:

> The underlying driver behind this [Enron's] request is a desire by Enron to "monetize" its trading stock. A significant business relationship already exists between the Commodities Team and Enron. Discussions have continued, based on this track record, to seek ways of meeting the company's needs through innovative financing structures. It is this need which this structure aims to satisfy but by a mechanism which leaves Barclays fully secured, with a sufficient margin and no or minimal Enron risk.

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[11] $SO_2$ Credits are Sulfur Dioxide Emission Allowances, which provide authorization by the Administrator of the EPA under the Clean Air Act to emit at least one ton of sulfur dioxide during or after a specified calendar year.

In other words, Barclays was to create a structure to generate the deceptive appearance of funds flow on Enron's balance sheet. Note that Paul LeVersha, Barclays Director of Global Financial Risk Management, put the word monetize in quotes. This is because it was being used as a code word to signify that the transaction's purpose was solely to generate a deceptive balance-sheet impact – there was no business purpose to the transaction. How this deceptive transaction was structured, and even the particular commodity involved, was determined by the problem-solving bankers. As Brian Smith of Barclays Business Management explained, Enron was indifferent to what commodity was used in the transactions and Barclays decided on $SO_2$ emission allowances: "Martin Woodhams [of Barclays Structured Products] primarily looked at this transaction, but ***I recall reviewing part of it with him and we considered many issues concerning the practicalities and other implications of dealing with the initial range of commodities that Enron came to us with***." Likewise, the structuring and execution of the transaction, including setting up the sham/shell SPE, was done by Barclays. As of September 13, 2001, a Barclays product proposal for $SO_2$ boasts, "Off-balance sheet commodity monetizations are a product category that the Commodities group has ***delivered*** in varying structural forms to a number of clients, including Enron . . . ."

761.5 In the $SO_2$ transaction, Barclays was aware of the deceptions it would have to use to give the deal the false appearance necessary for passing Andersen's heightened ***smell test*** for off-balance-sheet treatment of an SPE. In preparation for creating a structure for Enron, Barclays studied Andersen's requirements. An April, 25, 2001 Barclays e-mail explains how to get past the Andersen smell test:

> Arthur Andersen have applied a US GAAP ***smell test*** on SPV's stating that any financing structure that uses a run of the mill SPV will not be given off-balance sheet treatment.
>
> Enron have successfully used a structure that is an orphan SPV ***with a few twists that passes the smell test***.
>
> Key characteristics:

> Entity is not called an SPV, they referred it to [sic] as a swapco
>
> Bank is the sponsor of the swapco but has zero equity holding, the swapco does not consolidate up on to the banks balance sheet.
>
> ***Swapco has been established for some number of years***.
>
> ***Swapco has had a history of multiple transactions pushed through it***.
>
> * * *
>
> In the case where swapco has no transaction history, the bank will state to Enron ***that the swapco will in the future do different transactions***.

Knowing these guidelines, Barclays deceptively structured $SO_2$ so as to appear that the illusory SwapCo (Colonnade) met Andersen's requirements. A Barclays banker admitted that "Barclays was – was the arranger of the transaction." In sum, Barclays ***created a sham SPE – a shell entity – to use in a circular, fictional sale*** of emission credits, which it structured to create an appearance of cash flow from operations, when, in reality, it was cash flow from financing, *i.e.*, a disguised loan.

761.6 In late June 2001, Barclays came up with what was originally termed the SwapCo proposal, in response to Enron's request for a transaction to falsely create the appearance of funds flow. The key ingredient in the SwapCo subterfuge was a sham/shell SPE. Barclays knew that, to create the false appearance of GAAP compliance, the hedge in the transaction had to be "transacted between three independent parties, necessitating an SVP." [sic] As Benoit DeVirty, Managing Director of Barclays' Commodities Division, stated, "Barclays had set up . . . Colonnade, . . . on behalf of Enron, yes." But the Colonnade SPE was not an independent party. Rather, it was created and controlled by Barclays and was a sham – a shell from its inception on September 4, 2001.

761.7 To create the deceptive appearance of Colonnade meeting the then-heightened requirements for SPEs to permit off-balance sheet treatment on Enron's financial statements, Barclays deceptively "***seasoned***" this SPE, to make it appear to be legitimate under this more stringent test. To do this, Barclays ran "short-dated," *i.e.*, economically meaningless, *i.e.*, sham, transactions through Colonnade (which had no risk to Barclays) to create the illusion of compliance with GAAP regulations. ("Prior to commencing the transaction below, the SPV will undertake the following deals with counterparties external to Barclays. ***At no stage will the economic interest be passed back to Barclays***.") This was done to create a fiction, so that if outsiders looked at Colonnade, it would appear to be an SPE of substance – a legitimate, GAAP-compliant SPE, when in truth, it was a sham, *i.e.*, a pretend SPE.

761.8 Colonnade was a sham, shell entity created for only one purpose – the $SO_2$ financial-statement deal for Enron. But to conceal this – and to make Colonnade appear to be the seasoned entity that it was not, Barclays caused Colonnade to engage in a few riskless transactions, to create the deceptive appearance, *i.e.*, fiction, of having satisfied the requirement that "swapco has a history of multiple transactions pushed through it." A September 5, 2001 Barclays' e-mail details the non-economic transactions Barclays planned to run through Colonnade to "season" it:

> 2. Prior to commencing the transaction below, the SPV will undertake the following deals with counterparties external to Barclays. ***At no stage will the economic interest be passed back to Barclays***.
>
>     a) Colonnade buys USD VS HKD from Citibank and exits the position with Citibank 2 days later.
>
>     b) Colonnade buys silver VS USD from CIBC and sells it back to Citibank 2 days later.
>
>     c) Colonnade buys copper VS USD from CIBC and sells it back to CIBC 2 days later.

Ultimately, two four-day trades of precious metals with the bank Westpac took place – trades with no risk to Barclays.

761.9 These buy-and-sell-back-days-later transactions had no legitimate purpose. They were artifices to defraud, contrived transactions to create the fiction of a trading history for the SPE Colonnade to give it the misleading appearance of legitimacy – and of meeting Enron's auditors' requirements for off-balance-sheet treatment. These trades, and the purpose behind them, was known within Barclays. One Barclays' banker, Martin Woodhams, admitted:

The monetization receives off balance sheet accounting treatment by fulfilling the following two conditions. a) Occurrence of an inventory true sale, whereby legal title and beneficial ownership passes from the client to another party. b) A true sale and resulting hedge that is transacted between three independent parties, necessitating a SVP [sic]. ***Recent tightening of US GAAP regulations with regard to SVP's [sic] has led to the need of incorporating an SVP [sic] that closely resembles an operating company***. ***To this end, the SVP [sic] will before it transacts with Enron, undertake a number of short dated FX, metal funding and murabaha transactions. This diverse transactional trading history is crucial to the success of achieving off-balance sheet treatment for our client***. ***Once the Enron transaction closes, it is not intended that any further transactions will be entered into by the SPV***.

761.10 Barclays' banker, Paul Leversha, conceded:

Q. Did you understand that there had to be some number of trades that were entered into by Colonnade before it could enter into trades with Enron?

* * *

A. ***I did understand that there needs to be one or more transactions undertaken by the company prior to the SOX transaction*** to meet certain technical criteria.

In addition, Barclays' banker, Benoit DeVitry stated:

A. ***Colonnade was set up at the request of Enron a couple of weeks . . . before transactions with Enron was done, and there were some transactions done beforehand. Therefore, yes, technically they had multiple transactions***.

* * *

Q. And why was it important to have transactions on their balance sheet before they transacted business with Enron?

* * *

A. ***You know, I'm not an accounting expert, but my understanding is at the request of Enron, at the request of Arthur Andersen, that was one of the conditions required***.

761.11 Colonnade was a ***sham***/shell throughout. Colonnade not only had no legitimate pre-$SO_2$ transactions, it also never engaged in any transactions after $SO_2$. "In the case where swapco has no transaction history, the bank will state to Enron that the swapco will in the future do different transactions." Yet Barclays' banker Brian Smith admitted:

Q. Do you know of any transactions that Colonnade entered into subsequent to the September and October 2001 sulfur dioxide transactions other than selling the sulfur dioxide transactions to some Barclays entity – sulfur dioxide credits to some Barclays entity?

A. ***No*** . . . .

In addition, Barclays' banker Benoit DeVitry admitted:

Q. ***Was it intended that Colonnade would be used with clients other than Enron?***

A. ***No***.

Q. ***Was Colonnade ever used after the SOX transactions?***

A. ***I don't believe so***.

761.12 A Barclays' document admitted, "***Once the Enron transaction closes it is not intended that any further transactions will be entered into by the SPV***." (Emphasis in original.)

761.13 After Barclays set up and deceptively "seasoned" Colonnade to make it look legitimate and GAAP-compliant, Barclays and Enron proceeded with the first $SO_2$ transaction, ***an extremely important 3Q01 end deal***[12] – done at a time Enron was fighting back against rumors surrounding its business and finances that were swirling through the market, putting downward pressure on its stock, threatening to cause the scheme to implode. Barclays recognized the importance of getting the deal done – noting "[t]he urgency of this deal arises because of the approaching quarter-end reporting date." In September 2001, the following transaction occurred:

- Enron purportedly sold Colonnade 757,975 emission credits for $138.5 million. Colonnade financed the purchase by obtaining a loan from Barclays. Colonnade pledged the emission credits as well as the put and call options described below as security. Because the SPE was created and controlled by Barclays, the money came from Barclays.

[12] At the same time, Barclays was engaging in the contrived CSFB "prepay," a fictional commodities trade, and Nikita/Besson Trust, a sham FAS 140 deal with a secret no-loss guarantee from Enron. These bogus deals created over $700 million in false operating cash flow/revenue while concealing the same amount of debt. This is important "context."

- Herzeleide LLC ("Herzeleide"), a wholly owned subsidiary of Enron formed for the transaction, bought a call option from Colonnade that allowed Herzeleide to purchase at market price up to 757,975 emission credits from Colonnade (the same number of emission credits sold to Colonnade by Enron). In exchange for the call option, Herzeleide paid Colonnade $426,659.37. Given the strike price of the call option was the market price at the exercise date, the option was always "at-the-money." Therefore, the option premium was the "Cost of Carry till the Option Expiry Date." The premium payment was calculated based on the interest that would accrue during the option period on the purchase price of the emission credits (*i.e.*, the payment by Herzeleide is the equivalent of prepaid interest to Colonnade on the $138.5 million "loan").

- Herzeleide sold a put option to Colonnade that allowed Colonnade to require Herzeleide to purchase at market price up to 757,975 emission credits at specified times or upon the occurrence of specified conditions (*i.e.*, a default by Enron). In exchange for the put option, Colonnade paid Herzeleide $500.

761.14 Therefore, in connection with the closing of the September 2001 transaction, Enron and Colonnade (actually Barclays) ***simultaneously*** entered into swap agreements with Barclays in order to ensure that 100% of the market risk related to the emission credits stayed with Enron despite the purported sale. Under the Enron/Barclays swap, Enron would make a fixed payment (equal to the sum of the fixed price per emission credits) to Barclays at the settlement date. In exchange, Barclays would make a floating payment to Enron based on the current market price of the emission credits at settlement date. Under the Colonnade/Barclays swap, Barclays would make a fixed payment (equal to the sum of the fixed price per emission credits) to Colonnade. In exchange, Colonnade would make a floating payment to Barclays based on the market price of the emission credits at settlement date. Lead Plaintiff's expert Joel Finard concluded: "Given these contractual features, ***true ownership of the $SO_2$ credits never passed from Enron to Colonnade. Rather, the economic risks and rewards of ownership of the credits continued to reside with Enron***."

761.15 In October 2001, Barclays and Enron refinanced the September 2001 transaction. Enron sold Colonnade an additional 166,607 emissions credits for $29.1 million. Enron and Barclays then entered into three new swap agreements that had the same effect as the September transaction's swaps – a fake commodities sale. Enron paid Barclays a $10.1 million fee – actually a pay-off not called for by the original deal – to terminate the September transaction. In addition to the $10.1 million termination fee, Barclays billed Enron $850,000 as a transaction fee and £160,679 for fees and expenses. This all for a deal that lasted ***one month!*** Engaging in the scheme provided rich returns to Barclays.

761.16 The purported emission credits sale was fictional and circular, its structure contrived by Barclays to eliminate any price or market risk to it. The result of all these swaps and puts and calls was that Enron would effectively repay the $167.6 million loan with a fixed payment (including interest) to Barclays. A Barclays memo simplifies the steps of this disguised loan:

- Colonnade is an SPV set up to undertake these transactions
- Colonnade buy assets from Enron (sub 1).
- We provide a loan for this purpose.
- Enron (sub 2) has call options to repurchase assets.

* * *

- Our price risk on the assets is hedged – Barclays for Colonnade and Enron for Barclays.

761.17 But because of how Barclays deceptively structured the transaction, it would not appear to be a loan to anyone outside the deal if they looked. Rather, an outsider would see a fiction – an apparent arm's-length commodities sale.

761.18 Another deceptive act Barclays engaged in was hiring the Carey Langlois law firm to supposedly represent Colonnade, which gave the appearance of substance. But the representation was in fact a ruse because Carey Langlois was paid by Barclays. Barclays was later reimbursed this legal fee from Enron. This two-step process was necessary to meet the requirement that "Costs for setting up the swapco ***are not seemed*** to be paid by Enron." In fact, Enron reimbursed Barclays for all legal costs in setting up Colonnade – both the firm supposedly representing Colonnade, but in fact employed by Barclays, and the other firm (Allen & Overy) representing Barclays Capital.

761.19 Barclays expressed concern about the accounting-driven nature of the deal:

> ***The committee asked whether the deal was primarily for accounting/reporting reasons. The values of Barclays Bank suggest that we would be reluctant to do a deal that was done for solely accounting reasons. Given that we are on both sides of the relationship, the committee was also concerned about disclosure issues***.

Moreover, Barclays contacted Richard Oldfield of PricewaterhouseCoopers, one of its external auditors, and requested his services in connection with Barclays' accounting for the $SO_2$ transaction. But, when Oldfield saw the transaction he immediately and then repeatedly told Barclays that Enron could not achieve off-balance-sheet treatment because the transaction was not an arm's-length true sale, *i.e.*, the deal did not "work" for Barclays' client, Enron. Oldfield's view was clear:

> ***The substance of this structure ensures that Enron still has access to the economic risk, and rewards of the commodity securities it sells to the SPV by virtue of the market derivative contract it undertakes with BBPLC. As such, there is a strong argument that Enron has not managed to derecognise the assets off the balance sheet, either through not being able to achieve a sale in substance or by having to consolidate the SPV (for which it can be argued that Enron is the sponsor). Either way the asset would remain on its balance sheet***.

This was not what Barclays wanted to hear. The bank had designed the structure to have the appearance of, but not the substance of, a true sale. So, Barclays silenced Oldfield with a telephone call, indicating that the transaction had received internal signoff from both the structuring and accounting departments. This eleventh-hour call – just two days before the transaction closed – was not to address the issues Oldfield raised, but to tell him that the bank was not interested in his opinion on the matter. Barclays was certainly not interested in informing Andersen of Oldfield's view, even though ***Pritesh Pankhania, Barclays Manager of Management Accounts, admitted that in the normal course the bank would involve the client's auditors in accounting concerns***:

> Q. But in your experience, the normal course of action would be to inform the client about the concerns about their accounting?

*          *          *

> A. That would be an action that we could have – we would have done or ask the client – ***our client to also get their – get clearance from their auditors as well, for example***.

Despite this knowledge, Barclays went ahead with the deal. Barclays never took these concerns to Andersen. Instead it acted with Enron to deceive the auditors.

761.20 Barclays not only created the sham/shell SPE for the deal, it also assumed no economic risk in the actual transaction. An internal Barclays' e-mail about the transaction stated: "I guess the key things are to show ***that it is purely a financing relationship & Barclays does not benefit from the holding of the inventory (achieved through the swap structure?) and that similarly we are not exposed to the risk*** . . . ." Barclays' bankers admitted Barclays structured the transactions to eliminate any economic risk to Barclays:

> Q. And didn't it effectively reduce the risk to zero?

*          *          *

> A. In pure trading risk terms, if you have two swap transactions which are economically equal and opposite, ***then I would regard the trading risk to be eliminated***.

*          *          *

> Q. ***And then Barclays entered into a swap with Enron that transferred the price risk from Barclays to Enron; is that accurate?***
>
> A. ***At the time of the transaction that is correct, yes***.
>
> Q. In this transaction, do you know whether price risk was eliminated through the hedging transactions that occurred?

*          *          *

> A. ***Yes***.

761.21 Barclays' internal documents show "In both cases the option strike price is documented to match the floating swap price of the hedge. ***This key feature compels Enron . . . to always repurchase the entire monetized inventory***. ***Barclays actual SOX trading position is thus***

***reduced to zero***." Another document said, "The facility ***will mimic a revolving credit facility*** as Enron sells and repurchases product on a continuous basis over the term of the contract."

761.22 Barclays' bankers have admitted they were aware that the principal purpose and effect of the $SO_2$ transaction was to impact Enron's financial statements as Enron desired, and needed to be done by the end of September for this reason. Barclays knew that "***These transactions have the effect of significantly under-stating the debt level and assets on the balance sheet***." This was not an arm's-length transaction with economic substance. It was a subterfuge, having a deceptive purpose and effect – a device with the capacity to deceive Enron's investors. Barclays committed a deceptive act by structuring this transaction, which had no independent economic substance – rather, its only principal purpose and effect was to create the false appearance of fact, *i.e.*, a real sale of $SO_2$ credits in a transaction utilizing a GAAP-compliant SPE – when the truth was quite different.

761.23 Barclays knew that the $SO_2$ transaction was "***for 'window dressing' purposes***," meaning to ***give the appearance of***, *i.e.*,

> [a] transaction or potentially series of transactions, the effect of which is **– *the effect of which is to change the presentation of the company's accounts, and in particular, its balance sheet, from what it would have been without that transaction taking place***.
>
> * * *
>
> ***In a different way from how the financials would have presented had the transaction also, as a transaction, not taken place***.

761.24 Barclays knew that to achieve off-balance sheet treatment, the $SO_2$ transaction had to appear to be a "true sale." However, Barclays knew that the $SO_2$ transaction was not a true sale and schemed with Enron to hide that fact from Enron's outside lawyers as well. A September 27, 2001 e-mail from Enron warns Barclays, "***Just a heads-up: Please don't show the model I sent you to any of the lawyers, because when we calculated the Bank's Return, we treat Barclays and***

***Swapco as the same entity – which is a problem from a true-sale point of view***. ***Thank you!***" Doesn't leave much to the imagination does it?

761.25 Fastow confirmed the fraudulent nature of $SO_2$: "Barclays and Enron engaged in two $SO_2$ transactions, one in September and another in October 2001, providing the Company with funds through a structure that was intended to appear to be a sale of Enron $SO_2$ credits." ***Barclays created and controlled the crucial element in this subterfuge to produce the false appearance of funds flow from operations, a sham SPE called Colonnade***. Fastow explained:

> I understood from Mr. Glisan that Barclays was going to establish or cause to be established a special purpose entity for purposes of entering into structured finance deals with Enron. The name of this entity was Colonnade. And I wanted to understand that, in fact, Barclays controlled Colonnade and that Enron would be comfortable having them as a counterparty in the transaction.

761.26 Fastow learned from a conversation with Ben Glisan "that, in fact, Barclays was going to cause to be established and control Colonnade. And, so, [he] was comfortable having them in the transaction." "[U]sing an SPV such as Colonnade allowed the form of the transactions we were entering into with Barclay[s] to achieve desired accounting results." That is, by creating and employing the sham entity Colonnade, Barclays' own conduct generated the deceptive appearance of approximately $168 million in operating cash flow and concealed $168 million in debt.

761.27 Fastow confirmed that Colonnade was a sham entity created and acting at the direction of Barclays.

> Mr. Glisan explained to me that, generally speaking, Colonnade would – the way he described it is ***Colonnade is Barclays' version of Mahonia***. . . . I understood [that] to mean that Colonnade would be a minimally capitalized special purpose entity, probably formed in the Isle of Man or some other offshore jurisdiction, like Mahonia; that it would be ostensibly owned or controlled by some lawyers, but who were going to act at the direction of Barclays.

Colonnade purported to be something it was not – an independent third party. In reality, as Fastow confirms, it was "minimally capitalized" and "act[ed] at the direction of Barclays."

761.28 Fastow confirmed the steps Barclays took to create the deception that Colonnade was an actual business. Fastow understood "that Arthur Andersen, at that – about that time [summer of 2001], outlined certain steps Enron should take to make the special-purpose vehicles that were being used in these transactions look a certain way so they would meet GAAP." Fastow explained:

> [W]hen I say "to make it look a certain way," what I mean is, when I looked at the list of things that Arthur Andersen suggested, . . . they looked to be form – like they were form over substance, to me. For example, they said, don't call your special-purpose entity a special-purpose entity; call it SwapCo. Have – have this entity – another thing was, have this entity engage in a few transactions before it does the one transaction it was really being established for, to make it look like it was really an up-and-running business. Things like that.

Fastow recalled that this was called "seasoning," which he described as, "[d]oing a few transactions to make it look like this w[as] an operating company, even though it w[as] not." Fastow summed this behavior up simply: "I would describe that as – as wiring around the rules or form over substance."

761.29 Moreover, Fastow "understood Colonnade to be a vehicle that was meant to finance activity, not meant to be a – an industry counterparty in the traditional sense of the word." The $SO_2$ transactions were among "structured finance transactions that were done to achieve certain financial reporting objectives, like lower debt, higher income, improved funds flow from operations." These transactions created a false appearance of funds flow from operations and had "'the effect of significantly under-stating the debt level and assets on the balance sheet.'" ***Fastow agreed that he and Barclays bankers "engage[d] in a scheme by engaging in structured-finance transactions that created a false appearance of financial health by presenting a misleading picture of Enron's true business condition***."

761.30 Barclays had no intention of creating a real GAAP-compliant SPE, *i.e.*, a seasoned operating company, with Colonnade. Instead, Barclays knew that it was creating Colonnade for the sole purpose of engaging in the $SO_2$ transaction, which would deceive Enron's accountants, lawyers and investors and make Enron appear stronger financially than it actually was. Enron reported $167.6 million of cash flow from operations as a result of the $SO_2$ transaction. If the transaction had not been contrived and had been accounted for properly as a financing transaction, the $167.6 million would have been reported as debt.

761.31 According to Bankruptcy Examiner Batson, the facts surrounding this transaction would "allow a fact-finder to conclude that Barclays"

> ***structured*** and closed the $SO_2$ Transaction ***knowing*** the transaction was not a "true sale," that it was ***designed*** to manipulate [Enron's] financial statements, and that it resulted in the dissemination of financial information known to be materially misleading.

761.32 This bogus deal shares striking similarities to deals using Mahonia and Delta, bank-created sham offshore entities set up to do fictional deals with Enron that were simply disguised loans!

761.33 Thus, in summary as to $SO_2$:

- Barclays and Enron engaged in a transaction whose principal purpose and effect was to create a false appearance of cash flow from operations and to disguise debt with the intent to deceive investors in Enron stock. Barclays designed, seasoned and executed the $SO_2$ transactions for the sole purpose of creating a false appearance of cash flow from operations, intended to deceive Enron's investors. "***Barclays was – was the arranger of the transaction***." This included creating and running the "allegedly" independent Colonnade SPE.

- The $SO_2$ transactions served only "'***window dressing' purposes***," used in this context to mean giving the false appearance of cash flow from operations. The fact that the transactions' sole purpose was to create a false appearance of cash flow from operations was echoed at a Barclays meeting during which "***[t]he committee asked whether the deal was primarily for accounting/reporting reasons. The values of Barclays Bank suggest that we would be reluctant to do a deal that was done solely for accounting reasons***." Of course, Barclays did the deal anyway.

- Barclays seasoned Colonnade in order to deceive Enron's auditors. As a Barclays' memo explains: "***Recent tightening of US GAAP regulations with regard to SVP's [sic] has led to the need of incorporating an SVP [sic] that closely resembles an operating company. To this end, the SVP [sic] will before it transacts with Enron, undertake a number of short dated FX, metal funding and murabaha transactions. This diverse transactional trading history is crucial to the success of achieving off-balance-sheet treatment for our client. Once the Enron transaction closes, it is not***

> ***intended that any further transactions will be entered into by the SPV [sic]***." Therefore, Barclays schemed with Enron to effectuate transactions that were deceptive and manipulative by their very structure and were successful in deceiving both Enron's auditors and shareholders.

761.34 As to the $SO_2$ transaction, Barclays actually used or employed a shell or sham entity, *i.e.*, Colonnade, as a deceptive device and/or contrivance to:

(i) create the appearance of substance where it was lacking, *i.e.*, Barclays ran short-dated meaningless trades through Colonnade to give it the appearance of being a GAAP-compliant entity. Barclays actually created the bogus entity Colonnade and went ahead with the deal despite warnings from its own accountants that Enron would not be able to keep the transactions off-balance sheet. Barclays' committee approving the deal expressed strong reservations about entering into the transaction, but went ahead anyway;

(ii) create a fiction, *i.e.*, that Colonnade was a true operating company engaging in a "true sale" when in fact Colonnade was a front for Barclays and the risks and rewards of the commodity remained at all times with Enron; and

(iii) create a false appearance of substantial revenues or operating cash flow which falsified Enron's financial statements.

761.35 By engaging in this conduct, Barclays engaged in an act and practice which operated as a fraud or deceit in connection with the purchase or sale of Enron's publicly traded securities, and with respect to all of the Barclays transactions complained of between 1997 and 2001, a scheme and course of business that operated as a fraud or deceit on those purchasers of Enron's publicly traded securities.

761.36 Barclays' acts in connection with the $SO_2$ transactions created the appearance of legitimate or conventional transactions when, in fact, they were bogus or fake circular transactions. Without Barclays' conduct in these bogus transactions as the creator of Colonnade, who managed the entity, there would not have been a sham sale.

761.37 The principal purpose and effect of the $SO_2$ fictional transactions was to create the false appearance of revenues or cash flow from operations to inflate Enron's revenues, falsify its accounting and deceive the rating agencies, Enron's auditors and, ultimately, investors in Enron stock.

761.38 These transactions had no economic purpose other than to pay off Barclays for falsifying Enron's financial results and inflating the price of its publicly traded securities.

761.39 Barclays' conduct in the $SO_2$ transactions significantly contributed to and, as part of the scheme alleged by Lead Plaintiff, had the foreseeable effect of concealing the risk that Enron would be unable to service its debt and end in bankruptcy, thereby causing plaintiffs' losses.

**J.T. Holdings – December 2000**

761.40 Barclays and Enron engaged in the J.T. Holdings transaction whose principal purpose and effect was to create a false appearance of fact, intended to deceive investors in Enron's stock. In late 2000, Barclays and Enron restructured an existing synthetic lease transaction called J.T. Holdings, which had the principal purpose and effect of falsifying Enron's financial statements by concealing $110 million in debt. According to Fastow, in 2000 "J.T. Holdings – was set to expire, which would have caused millions of dollars of debt to be consolidated with Enron's balance sheet." In order to avoid consolidation, Fastow confirmed that "Barclays worked with Enron to ***create*** a new structure to keep the lease off [Enron's] balance sheet," including an SPE, which, of course, required 3% "at risk" equity.

761.41 In 1995, Enron had entered into a lease transaction by which Enron/NGL Trust, an SPE, purchased assets from Enron which Enron then leased back from Enron/NGL Trust for five years. By late 2000, when that lease was about to expire, Enron/NGL Trust had only two assets left – a methanol plant and a storage facility. Enron wanted a five-year synthetic lease structure involving an SPE to cover 3% of the financing. Barclays understood that in order for the synthetic lease structure to create the off-balance-sheet treatment intended by Enron, the assets had to be owned by an SPE capitalized with at least 3% independent "at risk" equity. Only this would avoid consolidation of the debt involved into Enron's financial statements. To achieve this financial statement impact in December 2000 (again a ***year-end deal***), Barclays and CSFB refinanced the synthetic lease via an SPE (Enron/NGL Trust). The 3% "at risk" equity Enron/NGL Trust needed for the entity to be a real, legitimate SPE and for Enron's financial statement treatment to be proper came 50% from Barclays and 50% from CSFB.

761.42 This transaction did not pass muster based on its own economics because the methanol plant in the structure was not believed to be worth what Enron was valuing it at. In fact, credit officer John Meyer testified "[Barclays was] concerned that [it] might end up on day-one of the lease with an asset ***whose market value was less than had been represented to [the bank]***." This level of risk was not acceptable for Barclays to do a legitimate arm's-length lease transaction. In short, the deal could not be done legitimately based on the actual value of the assets involved. Barclays' bankers stated in the Investment Banking Division Americas Minutes for November 13, 2000, that the bank believed J.T. Holdings was "***[n]ot attractive as a book and hold asset but [Barclays decided to] agree [because it]*** . . . ***considered [the transaction] important from a relationship standpoint***." Former Barclays' banker, and subsequent Enron employee, George McKean, even conceded that he "discussed possible other structures [with Enron] to avoid lease test[13] issues [but] due to the real estate nature of the assets, none seem to work."[14] This was a "***one-***

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13 McKean explained in his deposition that lease tests "refer[] to the model that was used to run . . . part of the transaction. . . . The model has a number of calculations . . . that . . . said whether [the transaction] worked or didn't work from a – leasing perspective."

14 In October 2000, George McKean, a former Barclays banker and subsequent Enron employee, notes in an e-mail that "[Andersen needs] . . . to sign off on the least test . . . ." "The risk

***off***" one time deal. Barclays did the deal as a favor to Enron, not because of the bona fide economics of the deal. Moreover, it ensured it was protected from the deal's dubious economics by a secret no-loss promise.

761.43 Because Barclays knew the assets underlying the lease were overvalued, Barclays would not do the lease deal as a straight-up arm's-length transaction. As Richard Williams explained in a November 14, 2000 e-mail to Barclays' officials Graham McGahen, David Head, Eric Chilton and John Meyer, Barclays agreed to take part in the deal only if it received "***explicit verbal support***" from Enron assuring it that "***under all circumstances Enron [would] execute its purchase option at a price sufficient to repay in full the holders of the B Notes and Certificates***," *i.e.*, the 3% equity, to Barclays. With this secret no-loss guarantee from Enron in place, Barclays engaged in this inherently deceptive transaction, the principal purpose and effect of which, as structured, was to falsify Enron's financial statements by concealing ***$110 million in debt***. The SPE in the deal was a ***sham, pretend SPE*** – it did not have 3% at-risk equity and the lease was not a legitimate arm's-length transaction because of this secret side deal, which also created the false appearance that the assets underlying the lease had sufficient value to support the transactions, while concealing over $110 million of debt on Enron's balance sheet.

761.44 Before it would engage in the J.T. Holdings transaction, Barclays demanded Enron ***secretly, verbally assure the repayment of Barclays' equity investment*** in the SPE. These verbal assurances were ***insisted*** upon because the actual value of the underlying assets would not support the financial ***structure of the transaction***. Bankers at Barclays wanted to make sure Barclays would "not lose on the underlying structure," according to a document drafted on

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is that they question the value [of the methanol plant] – as the MTBE plant was written off, it is likely they will be highly skeptical."

December 6, 2000 by Nicholas Bell to a number of senior Barclays' bankers. Again the secret no-loss guarantee of Barclays' supposed 3% at-risk equity made the transaction depend on a fiction and gave it the appearance of a conventional lease of substance in a deal with a GAAP-compliant SPE, based on bona fide asset values, when, in fact, the reality was quite different – a deal under a secret verbal no-loss guarantee to protect Barclays from the risk of economic loss on the overvalued assets, conducted via a sham, pretend SPE. Even Enron's own documents reflect Barclays' desire to make "structural changes" to the transaction to minimize its risk. In November 2000, former Barclays' banker, George McKean contacted James Moran at CSFB to discuss Barclays' "structural changes" to the transaction to ensure the bank minimized its risk. McKean notes that Barclays devised the structure as follows:

> 1) [Barclays wanted Enron] to delink [] the A Notes and B Notes, which were previously pari-passu, in order to separate the asset risk (B Notes) from the ***Enron Risk*** (A Notes) and (2) [then have Enron] cross-collateralizing the assets to provide structural enhancement to the B Note and Certificate Holders. As with other synthetic lease transactions, the expected source of repayments [was] through Enron's ability to terminate and repurchase the assets, resulting in ***Enron risk*** for repayment of the Notes and Certificates.

761.45 It is evident that Barclays had a clear motive for restructuring the J.T. Holdings transaction with Enron in this fashion – to ensure all risk remained "Enron Risk." Barclays carried out its intentions by receiving an oral assurance from Enron that Enron would carry all the risk from the deal. Fastow recalled that "Ben Glisan was told that the bank would participate only if it were to receive assurances from Enron that it would not lose its 3% equity and that certain structural features, intended to minimize its risk, were made part of the structure." Fastow told Glisan to provide the assurance they needed in sanctioning the transaction. ***Fastow also recalled personally providing Richard Williams verbal assurances that Barclays would not lose money on the J.T. Holdings transaction prior to the deal going through***. This assurance was needed because Barclays knew the methanol plant in the structure was overvalued. A November 14, 2000 e-mail from Richard Williams explains:

> In case of JT Holdings, we are not comfortable with the 5 year forecast of value attributable to the Methanol Plant – one of the two assets involved. While a credible case can be made that the value attributable to the storage facility implies a 1.56 X coverage ratio, this falls short of the norm of 4X coverages for synthetic leases.

761.46 The verbal side agreement Barclays demanded while making loans on overvalued assets was inherently misleading conduct with a deceptive impact. The SPE and lease would look legitimate, and so the truth could not be discovered by Enron's auditors in their review of the deal documents, as the formal deal documents contained no such no-loss guarantee or monetary repurchase understanding, nor did the documents reveal the overvaluation of the assets involved. Indeed, Barclays and Enron agreed, according to documents produced by Barclays, that the J.T. Holdings structure would be a "'***trust me' deal***." A handwritten note by Graham McGahen on a document outlining the structure by Meyer dated November 7, 2000, made clear that "[Barclays] would be relying on Enron's ***strong verbal assurance*** that it [was] not the intention of Enron to shift the residual value risk to the banks." Another document from Richard Williams on November 14, 2000, confirmed the unwritten promise: "[Barclays] ***agreed to go forward on the basis of explicit verbal support from the company's Treasurer***." The document continues: "Specifically, Ben Glisan . . . ***[committed] to [Barclays that] under all circumstances Enron [would exercise] its purchase option at a price sufficient to repay Barclays*** . . . ." A financial expert who has reviewed the transaction has concluded it contained "***secret verbal assurances guaranteeing repayment***" of Barclays' financial investment in the deal.

761.47 Barclays demanded this secret side deal because, according to Meyer in the "Post-Mortem," it knew of "Enron's having protected the banks (and in particular Barclays from likely/potential loss scenarios beyond its legal responsibility to do so" in other situations. The Post-

Mortem also revealed "[Enron] had a history of protecting lenders to its SPV's either through . . . verbal assurances that often translated into near virtual guarantees." According to a Barclays' memo by Meyer dated November 7, 2000: "It should be noted that Enron [had] protected its banks from loss many times." In reviewing the J.T. Holdings synthetic lease, Meyer noted the deal "should not have given rise to market risk but Barclays accepted a de facto guarantee from Enron to cover a perceived deficiency in the methanol plant's value."

761.48 Barclays clearly understood that the 3% equity component of the SPE had to be "***at risk***" in order to avoid the consolidation of the debt involved into Enron's financial statements. Specifically, Barclays' credit officer Meyer stated that the "***entity that [was] the lessor of the asset to achieve non-consolidation [had] to be capitalized with at least 3 percent at risk independent equity***." Meyer told the Bankruptcy Examiner:

> Q. But you did work with SPEs throughout your tenure at Barclays, right?
>
> A. Yes.
>
> Q. And it was always your understanding that in order for an SPE not be consolidated, it had to have three percent equity at risk. Correct?
>
> A. Yes, that's correct.
>
> Q. And it is also your understanding that if Enron guaranteed repayment of that three percent equity, that three percent equity wouldn't be at risk, right?
>
> A. ***Yeah –*** .
>
> * * *
>
> Q. How did you become familiar with those requirements, and to make sure we're on the same page, the idea that there had to be three percent equity at risk in the SPE structure?
>
> A. ***Well, that concept was just well-known within the finance world, that that was the minimum equity that you needed to have for an off-balance sheet vehicle, to be off-balance sheet***.

761.49 Fastow also confirmed that Barclays' own description of the structural enhancements and verbal assurances the bank required was accurate:

> Q. The last two lines of this section read: ***As a result of our challenge, Enron agreed to cash collateralize our residual value exposure to the methanol plant with proceeds received from the anticipated sale of the storage assets. Enron also provided verbal assurances to Barclays that their aim was to achieve an accounting objective and not to transfer a loss to its lenders***.
>
> ***Barclays accepted the valuation of the storage assets. Barclays' views the [sic] value of the methanol plant, unfortunately, have been proven correct. Barclays' views on the value***.
>
> Is that consistent, sir, with your recollection of how Enron did business with Barclays in JT Holdings?
>
> * * *
>
> A. ***That's my understanding based on my understanding of the underlying assets of the transaction and how the deal was progressing from talking with my finance people, yes***.

761.50 Moreover, Fastow stated:

> [I] do recall the assurance with them [on J.T. Holdings], and I do recall there being some features built in, structural features, I would call them, to somehow cross-collateralize the assets, be able to take value from one asset – any excess value from one access to help support the value of the other asset.

761.51 Fastow's testimony makes plain that Barclays received oral assurances that it would not lose money on deals it knew involved overvalued assets. According to Fastow, Williams, of Barclays, "was concerned about the value of . . . [the] methanol [plant involved in J.T. Holdings] and EOTT, that those assets may not be worth enough to support the transaction." "***With respect to the methanol plant [at issue in J.T. Holdings] and the EOTT [Nikita] transaction, I can say that I recall discussions with Rich Williams of Barclays regarding the valuations of those assets, and I recall giving him assurances that they'd be okay***." These ***concealed guarantees*** of repayment from Enron rendered the purported non-lending transactions inherently deceptive and, in substance, loans.

761.52 In the J.T. Holdings transaction, Barclays played a very specific role in concealing debt which falsified Enron's financial statements. Despite understanding that Enron specifically entered into transactions which had the "effect of significantly under-stating the debt level and assets on its balance sheet," Fastow noted that Barclays created the J.T. Holdings transactions with Enron to continue a masquerade of deceit and deception, concealing $110 million of debt from the investing public. Barclays sought to minimize its risk by structuring J.T. Holdings to ensure that any risk involved in transactions remained "***Enron Risk***."

761.53 According to Bankruptcy Examiner Batson, these facts and evidence would allow a fact finder to conclude that Barclays

> ***[o]btained*** verbal assurances from Enron in which Enron promised to cover Barclays' equity risk positions in two SPEs [one of which was J.T. Holdings] likely knowing that the assurances would not be disclosed to Enron's auditors and that, had they been disclosed, Enron could not have accounted for the transactions as it did.

761.54 Thus, Barclays unquestionably knew the sole purpose of the J.T. Holdings December 2000 transaction, as structured, was to manipulate Enron's financial statements to keep debt off the balance sheet and engaged in the deal only after getting a secret verbal promise to protect it against risk of loss that it knew made the structure of the deal bogus – a sham. Just like many other transactions before it that Barclays had developed with Enron, the J.T. Holdings "lease [was] important to Enron because of its off balance sheet attributes and the ability to preserve the methanol asset's book value until the right circumstance ar[ose], *i.e.*, tax and/or earnings position." Barclays noted in its own deal documents that Enron consistently "enters into off-balance sheet transactions" and "[t]hese transactions have the effect of significantly under-stating the debt level and assets on the balance sheet."

761.55 The J.T. Holdings transaction mimicked the CIBC-Braveheart deal, which included a secret side agreement that eliminated the bank risk and destroyed the legitimacy of the SPE involved, rendering it and the accounting that depended on its legitimacy a sham. And like the Merrill Lynch barge deal, in the J.T. Holdings transaction there was a secret promise that Barclays would be made whole on the deal. The secret verbal guarantee to Barclays created the false appearance of fact – *i.e.*, that the lease had been legitimately financed by a lender in an arm's-length transaction based on real asset values.

761.56 Enron's auditor was actually deceived by the secret oral promise between Barclays and Enron in the J.T. Holdings transaction. According to Andersen personnel who worked on the Enron account, "***The existence of this oral promise was concealed from and not disclosed to Andersen***." Barclays decided to conceal the true nature of the J.T. Holdings transactions, *i.e.*, secret guarantee of repayment, because the bank knew that the guarantees would destroy the required 3% accounting requirements, meaning Andersen would not approve the transaction, and Barclays would not receive its inordinate fees from the deal. Andersen personnel, including John Stewart, Richard Petersen and Carl Bass, also testified they never knew about this side agreement. It is clear that Barclays did not want Andersen to have a full review of the transaction. Barclays obviously concurred with Enron and believed, as noted in an October 2000 presentation to Barclays, that "the potential risk [was that] Andersen would ask to review the transaction and use less favorable assumptions in determining the valuation of the methanol plant."

761.57 Had Andersen known of the agreement between Barclays and Enron that Barclays would not lose its equity investment, Andersen would not have allowed it to be accounted for off-balance sheet. Andersen partner John Stewart confirmed this, stating, "Had Andersen known about these agreements . . . these oral assurances, the accounting for the asset would have been on the balance sheet of Enron – and they would have – Enron would have reflected debt on their balance sheet as opposed to nothing on their balance sheet." "[I]f Andersen had become aware of this assurance, Andersen would have concluded that Enron should consolidate the SPE." Barclays schemed with Enron to hide the true nature of the transaction from Andersen.

761.58 ***Andersen auditors, including Carl Bass and John Stewart, when later shown documents evidencing the side deal, testified they believed the internal Barclays documents referencing Enron's oral assurance in the J.T. Holdings deal showed collusion between Enron and Barclays***. "***This is evidence of collusion***," Carl Bass said in his deposition.

761.59 Auditing experts have also testified as to the deceptive nature of the verbal assurance Barclays insisted on in the J.T. Holdings transaction. Expert McEachern testified that he knew of no reasons other than to escape detection that Barclays and Enron would enter into such an oral side agreement. Foster testified: "I cannot think of another reason [other than to conceal material information from Andersen] why they would engage in this behavior." McEachern opined:

> Andersen should have been informed about Enron's secret oral assurances guaranteeing repayment of Barclays' B Notes and Equity Certificates in the J.T. Holdings Transaction. Had Andersen known of such assurances, Andersen would have disagreed with Enron's accounting and financial reporting for the J.T. Holdings Transaction.

761.60 Barclays worked closely with Enron knowing the purpose of the transaction was explicitly to impact Enron's financial statements – Barclays' documents drafted on November 17, 2000 admit that. Enron got Barclays to "extend . . . the synthetic lease structure ***to keep the financing off balance sheet***." Barclays knew that the "***the lease is important to Enron because of its off balance sheet attributes***," according to a November 14, 2000 note from Richard Williams.

761.61 In summary, as to J.T. Holdings:

- Barclays and Enron knew the methanol plant was overvalued and not worth anything close to what Enron was trying to get for it. Barclays demanded the secret promise of repayment because it knew that such a deal would not be entered into under standard business terms. The bank was worried that its loan to the lessor could be at risk because of the value of the underlying methanol plant. George McKean recalled that "there . . . [were] enough issues related to methanol that it was hard [for the bank to determine] what [the] plant would be worth in a couple of years." "[Barclays was] concerned that [it] might end up on day-one of the lease with an asset whose market value was less than had been represented to [the bank]."

- Therefore, Barclays entered into a secret side deal with Enron in which the Company promised that if Barclays implemented the deal using a "sham" SPE (to keep debt off balance sheet) the bank would be repaid in full plus interest. The J.T. Holdings synthetic lease "should not have given rise to market risk but Barclays accepted a de facto guarantee from Enron to cover a perceived deficiency in the methanol plant's value."

- In order to protect itself from loss, Barclays agreed to take part only if it received "explicit verbal support" from Enron assuring the bank that "under all circumstances Enron [would] execute its purchase option at a price sufficient to repay in full the holders of the B notes and Certificates." The bank had to ensure that it would "not lose on the underlying structure."

- The secret no-loss guarantee of Barclays' supposed 3% at-risk equity made the transaction depend on a fiction and gave it the appearance of a conventional lease of substance in a deal with a GAAP-compliant SPE, based on bona fide asset values, when, in fact, the reality was quite different – a deal under a secret verbal no-loss guarantee, to protect Barclays from the economic risk of loss due to the overvalued assets, conducted via a sham SPE.

- The facts surrounding the sham SPE, *i.e.*, the secret oral guarantee demanded by Barclays causing the deal to lack the requisite equity, were concealed from Andersen and investors.

761.62 Thus, as to the J.T. Holdings transactions, Barclays actually used or employed a shell or sham entity, *i.e.*, a synthetic lease, as a deceptive device and/or contrivance to:

(i) create the appearance of substance where it was lacking, *i.e.*, that the SPE was sufficiently capitalized with 3% outside equity even though the secret verbal assurance reduced the outside equity to zero because Barclays was promised it would not lose its investment. Moreover, Barclays' actions created the appearance that the entities in the synthetic lease (a methanol plant and storage facility) were properly valued even though Barclays knew, from its own investigation, that the methanol plant was overvalued;

(ii) create a fiction, *i.e.*, that a proper SPE with 3% outside equity existed and that the assets in the structure were properly valued in order to deceive Andersen and the market; and

(iii) create a false appearance of reduced debt levels which falsified Enron's financial statements.

761.63 In engaging in this conduct, Barclays engaged in acts and practices which operated as a fraud or deceit in connection with the purchase or sale of Enron's publicly traded securities, and with respect to all of the Barclays' transactions complained of between 1997 and

2001, a scheme and course of business that operated as a fraud or deceit on those purchasers of Enron's publicly traded securities.

761.64 Barclays' acts in connection with the J.T. Holdings transaction created the appearance of a legitimate or conventional synthetic lease transaction when, in fact, it was a bogus or fake loan transaction. Without Barclays' conduct in the bogus transaction, there would not have been a sham synthetic lease.

761.65 The principal purpose and effect of the J.T. Holdings fictional transaction was to create a misleading impression of Enron's debt levels; falsify its accounting and deceive the rating agencies, Enron's auditors and ultimately, investors in Enron stock.

761.66 This transaction had no economic purpose other than to pay off Barclays for falsifying Enron's financial results and inflating the price of its publicly traded securities.

761.67 Barclays' conduct in the J.T. Holdings transaction significantly contributed to and, as part of the scheme alleged by Lead Plaintiff, had the foreseeable effect of concealing the risk that Enron would be unable to service its debt and end in bankruptcy, thereby causing plaintiffs' losses.

**Nikita/Besson Trust – September 2001**

761.68 This FAS 125/140 deal was deceptively structured by Barclays in late September 2001 to look like a sale of Enron's interest in EOTT, but it was a pretend, sham sale – a fiction. In fact, it really was a disguised loan from Barclays to Enron. Like J.T. Holdings, Nikita was deceptively made to appear to be a transaction with 3% "at risk" equity provided by Barclays to an SPE. However, rather than actually having any equity "at risk," the deal was a sham because Barclays demanded, and got, a secret promise from senior Enron officers that Enron would "***ensure repayment***" of Barclays' 3% equity investment in the SPE. The principal purpose and effect of this transaction was to distort Enron's financials and create a false picture of the Company's financial condition, creating $10 million in phony income and $80 million in false operating cash flow, and concealing $80 million in debt at a critical time when Enron was desperate to keep the Ponzi scheme going, fighting off swirling rumors in the market and dealing with a plunging stock price.

761.69 Even though Barclays understood the requirement that an SPE have at least 3% equity at risk to be legitimate, Barclays demanded verbal assurances from Enron covering its equity in the Nikita transaction ***in order to negate that risk***. As accounting expert Charles Drott opined, "***Barclays was willing to assume the equity risk via the Total Return Swap only because it demanded and received from Enron's Treasurer (Ben Glisan) secret verbal assurance that Enron would guarantee repayment of Barclays' 3% equity investment in Besson***." Barclays' employees have admitted that they knew about and relied upon Enron's verbal assurances. According to Barclays' documents and admissions by its bankers:

- "***The market risk, however, had been covered by verbal assurances***." John Meyer, "Enron Post Mortem."
- Barclays was "***relying on [Enron's] verbal understanding to make [the bank] whole***." Graham McGahen memo, October 1, 2001.
- "***Barclays would rely on assurances from Enron's Treasurer that Enron would make up any short fall in the equity return***." Document regarding Monetization of EOTT Partnership Interests, September 25, 2001.

761.70 Not only was the SPE a sham, but Barclays also understood that the total return swap that was a feature of the transaction represented a direct payment obligation of Enron to pay the principal and interest due on Barclays' loan to the Besson Trust. Barclays was not at risk by virtue of the total return swap and the verbal assurance from Enron.[15] In fact, Barclays structured the

[15] Barclays structured that transaction so that "Besson Trust's ability to repay this loan was supported through a Total Return Swap with Enron North America (ENA), guaranteed by Enron, pursuant to which ENA was obligated to pay to Besson Trust an amount equal to the amounts payable on the Barclays loan in exchange for Besson Trust's commitment to pay to ENA all amounts received by Besson Trust with respect to the Class B interest." In other words, "payments were

loan as "***Enron Risk***." As John Sullivan explained in a memo to Sarah Abbott on September 24, 2001, "[T]he [Besson Trust] notes were accepted as ***direct Enron risk*** by virtue of the total return swap from ENA (guaranteed by Enron Corp.) in respect to both interest payment and principal repayment of the loan advanced to the Trust."

761.71 Barclays engaged in the Nikita transaction, understanding that it would result in materially misleading financial statements for Enron. This was the principal purpose and effect of the transaction. Barclays knew that although it appeared to be the equity holder, this was a fiction – it had no equity "at risk" because of Enron's secret verbal assurance to Barclays to cover such risk. The SPE involved was a sham, and the transaction was designed to create the appearance of a legitimate GAAP-compliant SPE engaging in an arm's-length transaction, when the substance was lacking – acts of deception directed at Enron's auditor and others.

761.72 Fastow summarized the Nikita transaction as follows:

> This FAS 140 deal was structured by Barclays and Enron, in late September 2001, to look like a true sale of the Company's interest in EOTT. I understand that Barclays considered the value of the underlying assets to be insufficient to justify the value of the deal; as a result, Barclays required and received an oral assurance from Ben Glisan that the Company would repay the bank's 3% equity investment in the SPE.

Fastow also recalled "having a conversation with Rich Williams about the EOTT component of the transaction."

761.73 Regarding FAS 125/140 transactions like Nikita, Fastow testified:

> ***[T]he FAS 120/140 [sic] deals were . . . generally speaking, transactions where Enron sold an asset for financial reporting purposes. It sold the asset to a special purpose entity, as opposed to selling it to an industry counterparty that may – may have wanted to own that asset***.

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funneled back on CSFB and then [CSFB] would pay [Barclays] on their total return swap, and [Barclays] would then pay [their] leg of the total return swap."

> ***Those transactions tended to generate funds flow, and they often generated earnings that Enron could report as well***.

Additionally, Fastow explained why deals like Nikita were documented as FAS 125/140 transactions as opposed to what they truly were – loans:

> Well, Enron could have borrowed the money, but that was the problem. That would show up as debt on Enron's balance sheet, and the interest payments associated with that debt would have shown up in Enron's income statement and funds flow statement.
>
> Enron desired to have what otherwise was economically, in substance, a loan look like something other than a loan so it could achieve a higher credit rating.

Therefore, the deal itself was deceptive, as was Barclays' conduct.

761.74 Fastow's testimony makes plain that Barclays received oral assurances that it would not lose money on deals it knew involved overvalued assets. According to Fastow, Williams, of Barclays, "was concerned about the value of . . . [the] methanol [plant involved in J.T. Holding] and EOTT, that those assets may not be worth enough to support the transaction." "***With respect to the methanol plant [at issue in J.T. Holdings] and the EOTT [Nikita] transaction, I can say that I recall discussions with Rich Williams of Barclays regarding the valuation of those assets, and I recall giving him assurances that they'd be okay***." These ***concealed guarantees*** of repayment from Enron rendered the purported non-lending transactions, in substance, loans.

761.75 The secret no-loss agreement in the Nikita deal was unknown to Andersen. Indeed, by its very nature, Andersen had ***no way*** of detecting such a side deal. Andersen has stated in response to discovery that "Enron orally promised Barclays that its three percent equity in the SPE involved in the Nikita/Besson Trust transaction would be repaid at or before maturity at par plus an agreed-upon yield. ***The existence of this oral promise was concealed from and not disclosed to Andersen***."

761.76 According to Andersen partner John Stewart, "[h]ad Andersen known this incremental information . . . about the verbal assurances, the accounting would have been different."

This was because the SPE would not have had the requisite 3% independent equity at risk as is necessary to have a non-consolidation treatment. As former Andersen partner Richard Petersen testified, "If Andersen was aware of the oral assurances that are in the [internal Barclays] document you have shown me, Andersen would have concluded that the SPE should be consolidated by Enron." If Andersen had found out about such side promises, Carl Bass testified, "***alarms would have gone off***." ***According to Bass, this was collusion to deceive Andersen and others about the true nature of the Nikita deal***. "***I think, equally clear, that there is evidence of – there would be evidence of collusive fraud***," Bass said under oath.

761.77 Accounting experts have also testified as to the deceptive conduct by Barclays in Nikita. Expert Foster concluded that Enron and Barclays intended to and did conceal material information from Andersen in the Nikita deal and expert McEachern opined in his report:

> Barclays was willing to assume the equity risk via the Total Return Swap only because it demanded and received from Enron's Treasurer Ben Glisan an oral assurance that Enron would guarantee repayment of Barclays' three percent equity investment in Besson.
>
> Andersen should have been told about Enron's secret oral assurance to Barclays whereby Enron would, in effect, through Barclays, guarantee repayment of CSFB's three percent equity investment in Besson.

761.78 Further, McEachern noted that "examples of fraud and concealment" such as J.T. Holdings and Nikita demonstrated that Enron and "those acting in concert with it clearly understood the accounting rules at issue in the various transactions and made a deliberate and concerted effort to insure that the true nature of these transactions was withheld from and not discovered by Andersen." Critically, as McEachern observes in his report:

> A GAAS audit can not reasonably be expected to detect the intentional withholding of oral or written agreements by senior management of a company and an independent third party, such as a major international banking institution.

According to Batson, these facts and evidence would allow a fact-finder to conclude that Barclays

> [o]btained verbal assurances from Enron in which Enron promised to cover Barclays' equity risk positions in two SPEs [including Nikita], likely knowing that the assurances would not be disclosed to Enron's auditors and that, had they been disclosed, Enron could not have accounted for the transactions as it did.

761.79 The Nikita transaction enabled Enron to misstate its financial statements for the quarter ended September 30, 2001, by improperly reporting $10 million of income and misrepresenting $80 million in financing cash flows as cash flow from operations and understating $80 million in debt – a transaction to create the false appearance of revenues making Enron's operations look more successful than they actually were and its debt lower than it actually was. Nikita was entered into at an especially critical time for Enron, as the drumbeat of bad news was beginning to reach the market during the 3Q01. Enron should have reported $80 million of debt and not $80 million it received as cash flow from financing activities.

761.80 Like CIBC-Braveheart, there was a secret side agreement protecting the bank's financial commitment on a key part of the deal that eliminated risk and destroyed the legitimacy of the SPE involved, rendering it and the accounting that depended on its legitimacy a sham. Like Merrill Lynch in the barge deal where a secret repurchase agreement caused the transaction to be a sham sale, here there was a secret side agreement with Barclays that deprived this transaction of a critical and necessary component – 3% "at risk" equity – for it to be legitimate, causing it to be a sham.

761.81 Thus, summary, as to Nikita:

- Damning admissions by Barclays that: "***The market risk, however, had been covered by verbal assurances***"; Barclays was "***relying on [Enron's] verbal understanding to make [the bank] whole***"; and "***Barclays would rely on assurances from Enron's Treasurer that Enron would make up any short fall in the equity return***."
- Barclays was only willing to assume the equity risk via a total return swap thereby creating the false appearance of an actual FAS 125/140 transaction.

761.82 As to the Nikita transaction, Barclays actually used or employed a shell or sham entity, *i.e.*, Besson Trust, as a deceptive device and/or contrivance to:

(i) create the appearance of substance where it was lacking, *i.e.*, that the SPE in the transaction was properly capitalized with 3% outside at-risk equity when the truth was that Barclays got a secret assurance that it would not lose its investment. Moreover, Barclays knew that the underlying assets (EOTT shares) were overvalued and thus a regular arm's-length transaction was not possible;

(ii) create a fiction, *i.e.*, that the assets in the structure were properly valued and that the SPE entity was properly capitalized with outside equity when the truth was that Barclays and Enron had a secret no-loss promise in place; and

(iii) create a false appearance of substantial revenues or operating cash flow and income which falsified Enron's financial statements.

761.83 In engaging in this conduct, Barclays engaged in an act and practice which operated as a fraud or deceit in connection with the purchase or sale of Enron's publicly traded securities, and with respect to all of the Barclays' transactions complained of between 1997 and 2001, a scheme and course of business that operated as a fraud or deceit on those purchasers of Enron's publicly traded securities.

761.84 Barclays' acts in connection with the Nikita transaction created the appearance of a legitimate or conventional sale transaction when, in fact, it was a bogus or fake loan transaction. Without Barclays' conduct in this bogus transaction, there would not have been a sham sale.

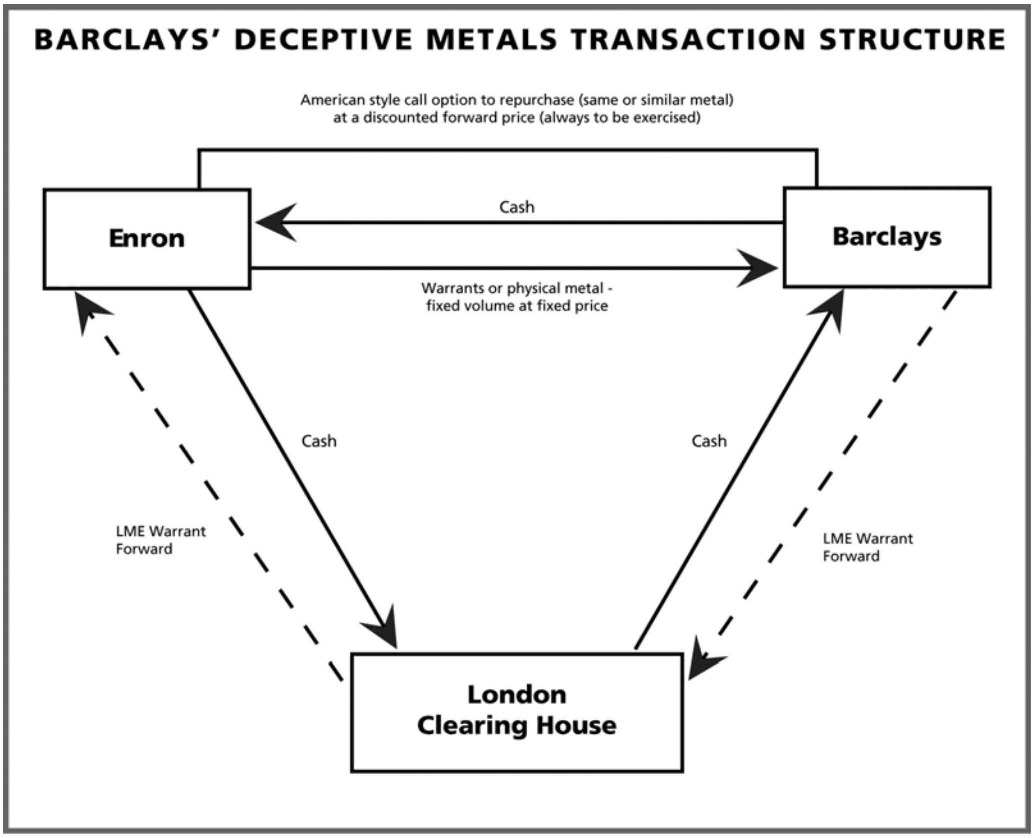
761.85 The principal purpose and effect of the Nikita fictional transaction was to create the false appearance of revenues or cash flow from operations to inflate Enron's revenues, falsify its accounting and deceive the rating agencies, Enron's auditors and ultimately, investors in Enron stock.

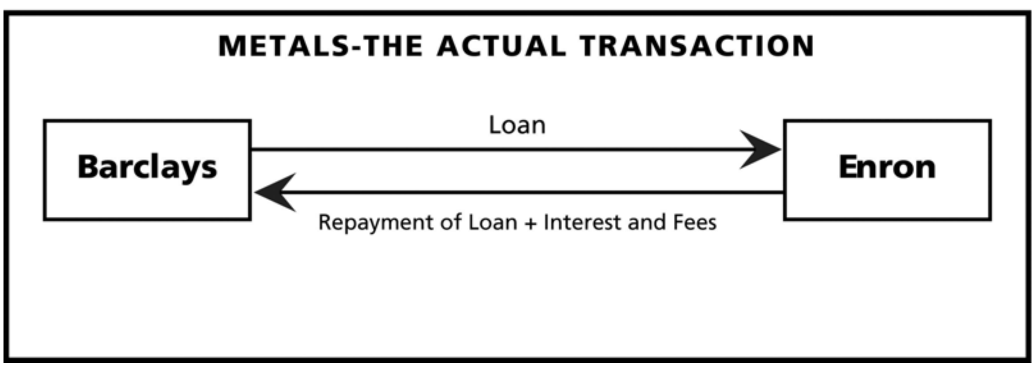
761.86 This transaction had no economic purpose other than to pay off Barclays for falsifying Enron's financial results and inflating the price of its publicly traded securities.

761.87 Barclays' conduct in the Nikita transaction significantly contributed to and, as part of the scheme alleged by Lead Plaintiff, had the foreseeable effect of concealing the risk that Enron would be unable to service its debt and end in bankruptcy, thereby causing plaintiffs' losses.

**Metals/Camelot I and II – September/December 2000**

761.88 Barclays and Enron engaged in two separate Metals transactions known as Camelot I and II with Enron in September and December 2000. These transactions were deceptively structured by Barclays to appear as commodities sales, but, in reality, were again disguised secured loans from Barclays to Enron. Both the Metals deals featured a fictional "option" as to which Barclays and Enron had a ***secret*** "***understanding***," that it would "***always***" be exercised, unlike a legitimate option which may or may not be exercised. This sham option protected Barclays from any true economic risk. The first deal closed in September 2000 for $750 million. The second closed in December 2000 for $1 billion.




761.89 In the September 2000 Metals transaction, Enron "sold" Barclays metal warrants at a 10% discount under the London Metals Exchange ("LME") price. At the same time, Barclays gave Enron the option to repurchase the warrants at the same discounted price. But Barclays and Enron also had a secret "***understanding***" that this option would ***always*** be exercised. Thus, what appeared to be a real sale with a real repurchase option was a fiction – the deal was circular from the outset due to this secret side agreement.

761.90 To further give the transaction the fictional appearance of substance, Barclays then entered into a forward contract with the London Clearinghouse ("LCH") in which Barclays would sell to LCH the same amount of warrants as the initial sale at the same discounted price. But at the same time, Enron entered into a forward contract with LCH in which LCH would sell to Enron the same amount of warrants as the initial sale at the same discounted price. Thus, the transaction continued to be ***circular and Barclays took no trading risk***. Either the option would be exercised, as agreed, or Barclays would receive the same amount of money they had paid Enron from LCH, who in turn would collect the same amount from Enron.[16] Ring around the rosy. Expert witness Saul Solomon testified regarding the purpose of having an option as part of the structure:

> It's clear to me that the intent of the parties, based on the evidence I've seen, was to have – you know, Enron sold these metals. They were going to acquire them back. And that's what everybody seems to have understood, and that's how the deal was negotiated.
>
> ***It doesn't qualify for sale treatment, . . . understand the facts to be. So, substantively, even though the – the documents may have been papered otherwise, if the understanding of the parties were that this option was intended to be exercised, that would be compelling evidence that a sale does not take place***.
>
> * * *
>
> The option is in the documents, but the ***communications between Enron and Barclays about the option is what's compelling to me, that there was an agreement that everybody's expectation was that the option would be exercised***.

761.91 The December 2000 transaction had the same structure as the September 2000 transaction. The only difference was the December 2000 transaction involved the sale of ***physical metals***, for $1 billion. Simultaneously, Barclays granted Enron an option to purchase the same metal at the same price, but again ***with a secret understanding that the option would be exercised***. To

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[16] The only risk Barclays faced was if the metals purchased under the facility was damaged or lost. To cover this risk, Barclays insisted Enron arrange an insurance policy on the metals to protect Barclays.

further the deception, Barclays again entered into a forward contract with LCH where it would sell LCH the same amount of metal at the same discounted price, and Enron also entered into a forward contract with LCH in which LCH would sell to Enron the same amount of metal as the initial sale at the same discounted price. Same deceptive conduct.

761.92 Barclays, having no interest in the metal as a commodity, did not want the metal to move locations. As an April 2001 "Barclays Off Balance Sheet Inventory Monetization Facility" presentation explains, "the material does not move locations." Barclays' proposed structure insists "metal is LME deliverable grade ***in*** LME warehouse location." Also, Barclays did not pay for the metals to be housed. In an e-mail discussion between Barclays and Enron on the transaction, Barclays explains "either the rent would be paid up or MG [Enron] would confirm to the warehouse that they would be responsible for the rent." Barclays also structured the transactions so that if the metals suffered damage or were lost while Barclays supposedly owned the metals, Enron would be responsible: "[I]t has been agreed that Enron will arrange an insurance policy under which Barclays will be a co-insured." Enron maintained the risks and rewards of ownership and effective control of the assets while the assets were supposedly Barclays. A fake sale, but papered by Barclays to appear to have substance when in fact there was none.

761.93 The sole purpose and effect of the transaction was to influence Enron's financial statements by ***creating the false appearance*** of cash from operations and hide debt. ***The Metals transactions enabled Enron to falsely report $1.4 billion as cash flow from operations. This amount should have appeared as debt on Enron's books because Enron, either through exercising the option or as a result of the forward contracts with LCH, was obligated to repay the money***. This false loan was critical because Enron desperately needed money and the revelation of the huge $1+ billion loan would have had a devastatingly negative impact on Enron's public financial position and its existing credit facilities. A call report from June 19, 2000, details Enron's initial discussions with Barclays regarding the Metals transactions. Enron gave Barclays the mission "to get the $2 billion of inventory financing off the balance sheet." Yet, according to Ian Jefferson, Barclays Account Officer, "they wouldn't have, say, ***$2 billion worth of debt through this methodology***."

761.94 Barclays designed the Metals transactions as sham commodities deals, but in reality the deals were loans disguised as sales to allow Enron to conceal debt, *i.e.*, falsify its balance sheet. ***Barclays assumed no economic risk in the Metals transactions***. Brian Smith, a senior banker at Barclays in London, admitted that the Metals transactions had an Enron guarantee:

> Q. Were you aware that the transaction required "main board level review by Enron Corporation"?
>
> A. ***I remember there being high level review because of the guarantee that was being provided, which was substantial, but I can't remember whether it was main board approval***.
>
> Q. ***The guarantee by Enron***?
>
> A. ***As part of the structure there was a guarantee and I forget whether – I forget the amount, but it was a significant guarantee***.

761.95 A Barclays' e-mail dated August 8, 2000, from Brian Smith to Bill Appleby of Enron, copying a number of high-level Barclays and Enron employees, also makes clear that "The first thing that needs to be established is that ***these are being priced on the understanding that the options are going to be exercised, i.e., it is understood that the purpose of the option is to meet accounting requirements not to give trading opportunity***." Barclays knew Enron's purpose for engaging in the Metals transactions was to raise cash and hide debt off-balance sheet using Barclays' loans to accomplish this deception.

761.96 Senior Barclays banker Paul LaVersha wrote: "We are also aware that the company [Enron] enters into off balance sheet transactions whereby it sells and subsequently has the option to repurchase assets. . . . ***These transactions have the effect of significantly under-stating the debt level and assets on the balance sheet***."

761.97 Fastow confirmed that “Barclays and Enron engaged in two separate Metals transactions - Camelot I and II – in September and December 2000.” Fastow confirmed these transactions had the principal purpose and effect of creating a false appearance of funds flow from operations:

> [M]y understanding of the intent of the transaction was to not convey to Barclays or its affiliates the commodity price risk or – or market price risk associated with this inventory, but, rather, to set up an off-balance-sheet financing vehicle which would serve to allow Enron to – or cause Enron to report lower debt and higher funds flow from operations than it otherwise would.

That is, the purpose of the transactions was not to convey a commodity, but rather, solely to create a deceptive off-balance sheet financing vehicle which caused Enron to deceptively report lower debt and higher funds flow from operations.

761.98 Fastow emphasized that the purpose of the transactions was not to be a commodities sale – “the transaction was not [to] put Barclays in a position where they were taking market price risk related to the commodity.” Rather they were loans disguised to appear as commodities sales: “My recollection is this was meant to be an off balance sheet financing and to generate funds flow from operations for Enron.”

761.99 Hence, Barclays’ own conduct was deceptive because it accepted oral assurances regarding the option which made the presentation of the transactions in the deal documents inaccurate. An outsider looking at the transaction documents would have been tricked – not knowing a secret agreement existed. Additionally, Fastow confirmed that oral assurances were consistent with the way Enron did business with Barclays and recalled hearing about a structural issue to minimize risk to Barclays in the Metals transactions. Fastow recalled, “I heard from my finance team that this was a structural issue that was necessary for accounting and that they had to give assurances to Barclays that we weren’t trying to shift some risk to them related to that.” The structural issue was an oral agreement that Enron would exercise the options to repurchase the metals or metal warrants. Fastow understood that these assurances were given: "My understanding is that there were certain assurances given to Barclays regarding those options." In the end, the Metals transactions were part of Barclays' and Enron's "scheme . . . [of] engaging in structured-finance transactions that created a false appearance of financial health by presenting a misleading picture of Enron's true business condition."

761.100 Thus, as to the Metals transactions:

- Barclays designed the Metals transactions, which had the sole purpose of deceiving Enron's investors, to fraudulently conceal debt on Enron's books. Notes from initial discussions between Barclays and Enron on the Metals transactions reveal Enron told Barclays they wanted "to get ***$2 billion of inventory financing off the balance sheet***." Barclays then designed a structure to accomplish this fraud. As Barclays in-house lawyer Richard Firth bragged, "Technical expertise has also come into play in structuring complex Commodities transactions – in particular, the inventory monetisation structure (as used in the Enron deals) ***which I was largely responsible for developing***."

- Barclays and Enron deceived Andersen by agreeing to enter into a secret side agreement that the option in the Metals transactions would be exercised, causing Andersen to believe the option was valid when it was not. Barclays told Enron in no uncertain terms, "The first thing that needs to be established is that these are being priced ***on the understanding that the options are going to be exercised, i.e., it is understood that the purpose of the option is to meet accounting requirements, not to give a trading opportunity.***" Barclays caused the accounting employed by Enron to be wrong because they agreed to deceive Enron's accountants by designing the structure to include a sham option.

761.101 Thus, as to the Metals transactions, Barclays actually used or employed a shell or sham, *i.e.*, fake, option which transformed the deal into a $2 billion loan to Enron, as a deceptive device and/or contrivance to:

(i) create the appearance of substance where it was lacking, *i.e.*, what appeared to be a traditional inventory financing was actually a deceptive way for Enron to get $2 billion off its balance sheet because Barclays and Enron had a deal that an option to buy the metals would ***always*** be exercised, thus locking in a price and removing all risk in the deal;

(ii) create a fiction, *i.e.*, that a real inventory financing was occurring; and

(iii) create a false appearance of substantial revenues or operating cash flow and disguise debt which falsified Enron's financial statements.

761.102 In engaging in this conduct, Barclays engaged in an act and practice which operated as a fraud or deceit in connection with the purchase or sale of Enron's publicly traded securities, and with respect to all of the Barclays transactions complained of between 1997 and 2001, a scheme and course of business that operated as a fraud or deceit on those purchasers of Enron's publicly traded securities.

761.103 Barclays' acts in connection with the Metals transactions created the appearance of legitimate or conventional transactions when, in fact, they were bogus or fake transactions. Without Barclays' conduct in these bogus transactions, there would not have been a sham sale.

761.104 The principal purpose and effect of the Metals transactions was to create the false appearance of revenues or cash flow from operations to inflate Enron's revenues, falsify its accounting and deceive the rating agencies, Enron's auditors and ultimately, investors in Enron stock.

761.105 These transactions had no economic purpose other than to pay off Barclays for falsifying Enron's financial results and inflating the price of its publicly traded securities.

761.106 Barclays' conduct in the Metals transactions significantly contributed to and, as part of the scheme alleged by Lead Plaintiff, had the foreseeable effect of concealing the risk that Enron would be unable to service its debt and end in bankruptcy, thereby causing plaintiffs' losses.

**Roosevelt, Nixon and CSFB Prepays –**
**December 1998, December 1999 and September 2001**

761.107 Barclays engaged in three giant "prepay" transactions with Enron: Roosevelt (December 1998), Nixon (December 1999) and CSFB (September 2001).[17] These prepay transactions were, as Barclays banker Meyer admitted, "essentially circular in nature" – in fact, disguised loans among Enron, Barclays and several other banks. In each instance, Enron received a lump-sum payment upfront, and made either a single payment or a series of payments back to Barclays, equal to the principal of the lump sum plus interest – a disguised loan, that would appear to others to be legitimate arm's-length commodities trade with market and price risk. To artificially inflate Enron's reported cash flow from operations, Barclays worked to structure these prepays to look like legitimate trade activity, when in fact, the deals were loans, eliminating all of the price and market risk that would have been present in a legitimate commodities trade. Barclays (and Enron) did this by simultaneously entering into a series of circular trades – a contrivance. As was the case with Enron's other fraudulent prepays with Citigroup and J.P. Morgan, the trading activity in the documentation for these prepays never took place because, as was prearranged and agreed, the transactions were always going to be financially settled to assure the pre-arranged financial result – cash to Enron to be repaid (debt), with a fixed rate of return to Barclays (principal plus interest on the loan). This means, as Barclays' own employee Brian Smith testified, "***instead of physically delivering a commodity [the pre-pay] would be settled by making a payment of an equivalent value***." These were ***fictional*** commodities trades where no physical delivery of goods was ever completed or risked – deceptive sham trades the same as the phony Mahonia and Delta commodities transactions Enron did with Citibank and J.P. Morgan. In fact, they copied the deceptive design of

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[17] In September 2001, Enron renewed the December 2000 oil-linked loan, engaging in a second prepay transaction with CSFB, in which Barclays replaced Morgan Stanley as the intermediary.

those contrivances and Roosevelt, one of Barclays' prepays, actually involved Citibank and the sham entity Delta.[18]

761.108 The inherently deceptive structure, nature and impact of these prepays was set forth in the guilty plea of former Enron Assistant Treasurer Timothy DeSpain. The factual statement in DeSpain's plea agreement states in relevant part:

> Another mechanism by which Enron achieved the artificial cash flow targets it set for itself was through transactions commonly referred to within the company as "prepays." The reporting of the cash received from these transactions was a means of demonstrating to the rating agencies Enron's ability to recognize cash from its mark-to-market trading book. Although the prepay transactions were accounted for as commodity transactions and reflected on Enron's books as a trading liability, the transactions in substance created debt-like obligations to the financial institutions that advanced funds to Enron through the transactions. I and others told the rating agencies that the cash generated from Enron's trading operations was from the sale or "monetization" of trading contracts or the future cash flow streams from those contracts. Fundamentally, the agencies were led to believe that Enron was generating cash by selling an asset, when in fact Enron was generating cash by incurring a future obligation that operated as debt. Over the course of my time as Assistant Treasurer, Enron's obligations under the "prepay" transactions grew to

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[18] Delta was a Cayman Island entity created and run by Citigroup, but which served as a purported independent entity in the various prepay transactions. Congressional investigators concluded Delta had no legitimate economic purpose but rather was part of a scheme to conceal billions in loans from Citigroup to Enron as "prepay" transactions that Enron could report as cash flow from operations. *See* Testimony of Robert Roach Report Chief Investigator before the Permanent Subcommittee On Investigations, The Role of The Financial Institutions In Enron's Collapse, dated July 23, 2002; Report to the Senate Committee on Finance Services, Investment Banks: The Role of Firms and Their Analysts with Enron and Global Crossing, dated March 2003 at 57. By including a third party, Delta, in these prepay transactions, Citigroup and Enron removed all commodity price risk from the transactions by moving the commodities involved in a circle – resulting in a transaction with economics identical to a loan. *See* Second Interim Report of Neal Batson, Appendix E ("Batson II, App. E") at 10, 17, 21 (Ex. C to Complaint Appendix).

> The Court concluded, in its ruling on motions to dismiss, that "the intrinsic nature of these devices and contrivances was fraudulent so that those intimately involved in structuring the entities and arranging the deals, especially more than one, would have been aware that they were an illicit and deceptive means to misrepresent Enron's actual financial state and mislead investors about Enron securities, or at a minimum, would have had to have been severely reckless as to that danger."

*Enron*, 235 F. Supp. 2d at 694.

> approximately $5 billion. I was directed by Enron's Treasurers not to reveal to, or discuss with, the credit rating agencies, the nature and extent of the prepay transactions entered into by Enron, and I complied with this direction. I and the Treasurers recognized that if the rating agencies knew about the nature and extent of Enron's prepay transactions, such information would have had a materially negative effect on Enron's credit rating.

761.109 Barclays' motivation for engaging in the prepay transactions was the extra high fees/interest amounts the transactions brought to Barclays – guaranteed no-risk return, in effect, a pay-off for being a part of the transactions – *i.e.*, its conduct in engaging in the scheme. According to a Barclays' e-mail from Ian Jefferson to Naguib Kheraj and others, dated March 13, 2000, "[t]he original 3 month bridge was done for relationship reasons and on the basis that this was recognised in a conversation between Bob Diamond and Andy Fastow, the Enron CFO." Barclays received special financial protection in the deal – "***Even if it is closed out early we will still earn a minimum of $320,000 so I think it was worth it***," Brian Smith touted to lawyer Richard Firth in 1999. Barclays and Enron knew that these were not actual arm's-length commodity trading opportunities with typical market/price risk. Barclays understood what Enron was doing with these prepays, *i.e.*, falsifying its financial statements, and how the phony accounting would be done. Saul Solomon, a financial expert, familiar with the transaction and Barclays' documents has testified:

> Q. [W]hen you say that Barclays understood, Barclays understood they were going to treat it as a price risk management liability?
>
> A. Barclays understood more than that. ***They understood that it was disguised debt and it was something that was going to be handled in such a way on the financial statements –***
>
> * * *
>
> A: ***so it could be misleading*** –
>
> * * *
>
> A. I considered the evidence that I had, which to me was compelling that – that individuals at Barclays who were involved in these transactions understood exactly what accounting benefits Enron was deriving from them and exactly what these transactions really reflected.

761.110 According to Batson, these facts would “allow a fact-finder to conclude that Barclays”

> participated in three Prepay Transactions and one monetization transaction that ***Barclays knew were designed to manipulate the Debtors’ financial statements and did result in the dissemination of financial information known to be materially misleading***.

**Roosevelt**

761.111 The December 1998[19] Roosevelt prepay was structured by Barclays as follows:

***Step 1***: Delta, a Citigroup SPE, entered into an agreement to pay Enron a lump sum of $499,916,264. In return, the documentation provided that Enron was to make monthly deliveries of 439,250 barrels of oil per month and 157,200 MMBtus per day. Since Delta did not want, and, in fact, could never accept, delivery of the physical commodities, Delta simultaneously entered into a marketing agreement with Enron to have Enron sell the commodities on the open market.

***Step 2***: The simultaneous Barclays/Delta swap required Delta to deliver 439,250 barrels of oil per month and 157,200 MMBtus per day. In exchange, Barclays made monthly payments to Delta for a total sum of $541,170,392.

***Step 3***: The simultaneous Barclays/Enron swap required Barclays to deliver 439,250 barrels of oil per month and 157,200 MMBtus per day. In exchange, Enron agreed to make fixed monthly payments totaling $541,985,934.

761.112 Barclays was aware that the Roosevelt transaction was structured and intended to falsify Enron’s financial condition. Regarding the structure of the Roosevelt transaction, Barclays senior banker Richard Williams wrote on March 19, 1999:

> [W]hile the two swaps mirror one another in all respects, they may not cross-default.

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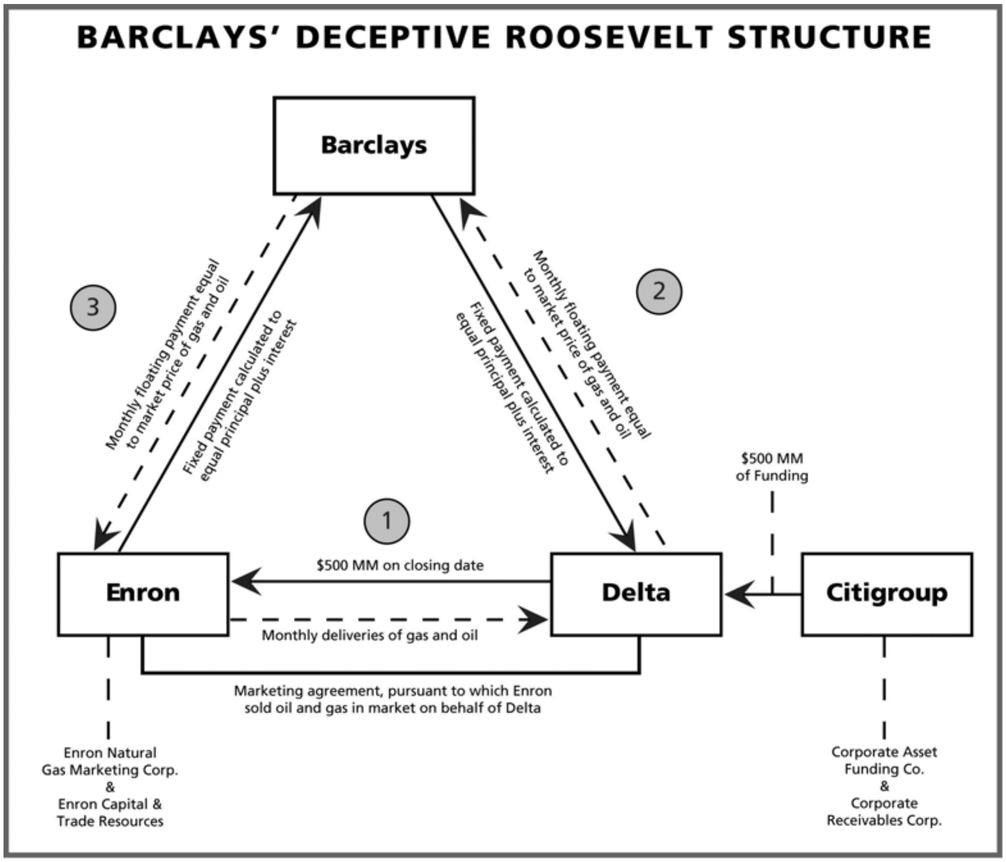
[19] Even though the transaction closed prior to April 8, 1999, Roosevelt, like Chewco, is highly relevant to show scheme and intent. *See Enron*, 235 F. Supp. 2d at 689. *See also* Fed. R. Evid. 404(b).

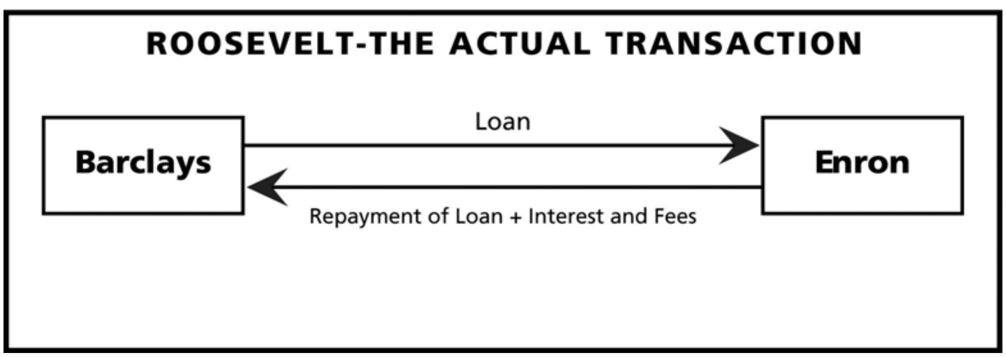
*          *          *

> ***The absence of the cross-default is to avoid tainting Enron's accounting treatment . . . . In a nutshell, the deal needs to be treated as a sale, not a financing.***

761.113 The transaction was a circular contrivance – a sham structured to eliminate the price and market risk for the sole purpose of creating a pre-arranged distortive impact on Enron's financial statements, and a fixed payment/pay-off to Barclays. The simultaneous swaps canceled each other out. At the outset, the circular structure of the transaction removed all price risk from the supposed sale of the commodities. In fact, ***no oil or natural gas was ever exchanged in any of these prepay transactions***, nor was it ever meant to. Internally, in its Roosevelt documents, Barclays ***called the swaps loans and explained the swap would "house all commodity price risk with Enron***."

761.114 An internal Barclays document explaining Roosevelt, which George McKean called "Project Delta," refers to the swap as a "loan." On the document is a reference to "P" and "I" being received by Barclays. McKean testified that "P" and "I" are standard abbreviations for principal and interest. Therefore, no doubt remains that while Barclays presented Roosevelt and the other prepays in the deal documents as commodities swaps, they were, in truth, loans. John Meyer, in charge of Barclays' credit review of Enron transactions, himself described Roosevelt as the "crude oil loan." The following charts reflect the deceptive structuring versus the actual substance of Roosevelt.




761.115 According to expert Saul Solomon, in these three prepays "[t]he commodity price risk or the potential to profit on any one of those legs of the transaction was eliminated by the other two legs of the transaction. So, effectively, there is no commodity price risk . . . ." In Roosevelt, a sham entity, the Citigroup-created Delta, served as a trade counterparty. According to Solomon, "having the third party in the transaction being this SPE, that . . . was really . . . a sham to try to affect the appearance of a separation with three independent parties."

**Nixon**

761.116 The Nixon prepay transaction was structured by Barclays and Enron as follows:

***Step 1***: In December 1999, Enron entered into simultaneous swaps with Citigroup, Barclays and The Royal Bank of Scotland ("RBS"). Each of these banks made a lump-sum payment to Enron and in return Enron was to make a floating rate payment in 90 days based on the spot price of 5,377,984 barrels of oil.

***Step 2***: Toronto Dominion ("TD") was the intermediary. Barclays, Citigroup and RBS entered into swap agreements with TD to pay TD a floating rate payment in 90 days based on the spot price of 5,377,984 barrels of oil. In return, TD agreed to pay each bank a fixed amount of $106,376,524 (Citigroup) or $112,513,644 (Barclays and RBS).

***Step 3***: TD entered into a swap agreement with Enron which required TD to pay Enron a floating rate payment in 90 days based on the spot price of 16,754,490 barrels of oil. In return, Enron agreed to pay TD a fixed amount of $331,403,812 in 90 days.

761.117 The simultaneous and circular floating rate payments canceled each other out, eliminating the substance of the apparent commodities trades, making it fictional. All that remained was a lump-sum payment to Enron in return for future fixed rate payments to Barclays, Citigroup and RBS, which were made through TD. This was a disguised loan – a fictional commodities trade, contrived to eliminate the economic, *i.e.*, price and market, risk to the banks that would have existed in a legitimate arm's-length commodities trade. The transaction was structured in this deceptive manner, *i.e.*, to look like a commodities trade so that if outsiders examined it, it would look like a legitimate trade not a loan to be shown as debt on Enron's balance sheet. George McKean, a Barclays' banker who went on to work at Enron, admitted during his deposition:

> Q. [I]t says, . . . we have no real net exposure. . . . What is meant by having no real net exposure?

* * *

A. Because ***if you've done an offsetting trade, you're not going to have any real net exposure***.

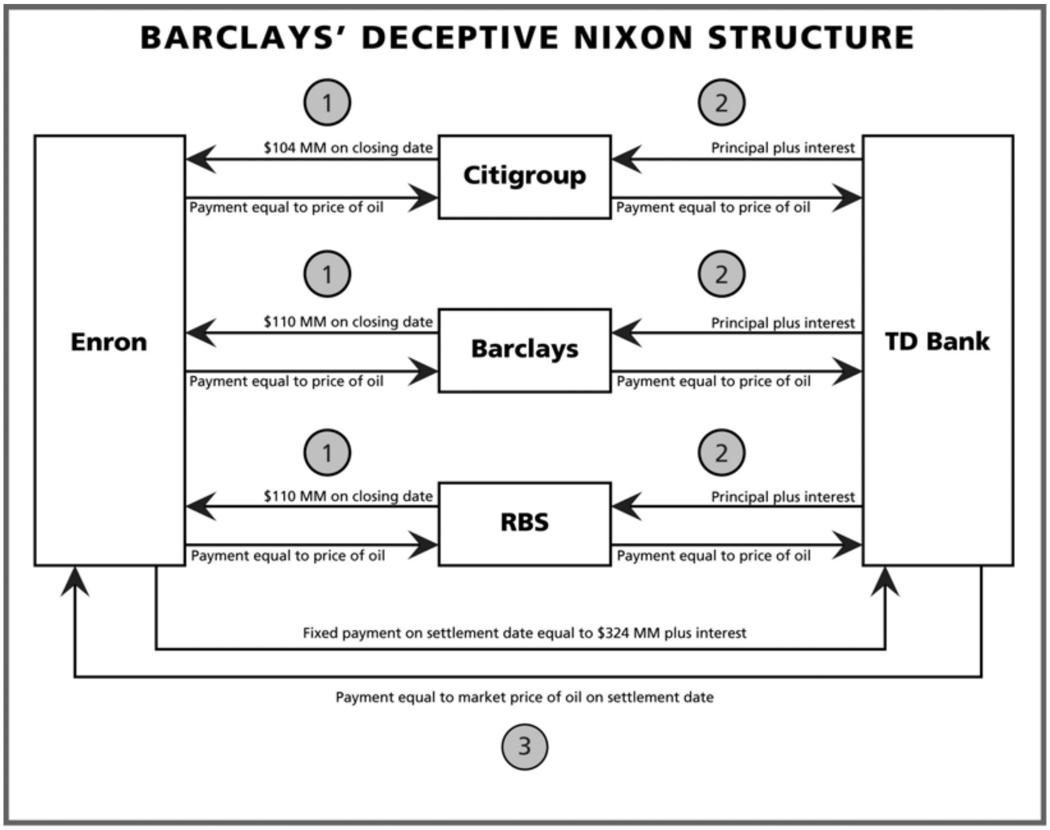
Q. The two sides kind of cancel each other out?

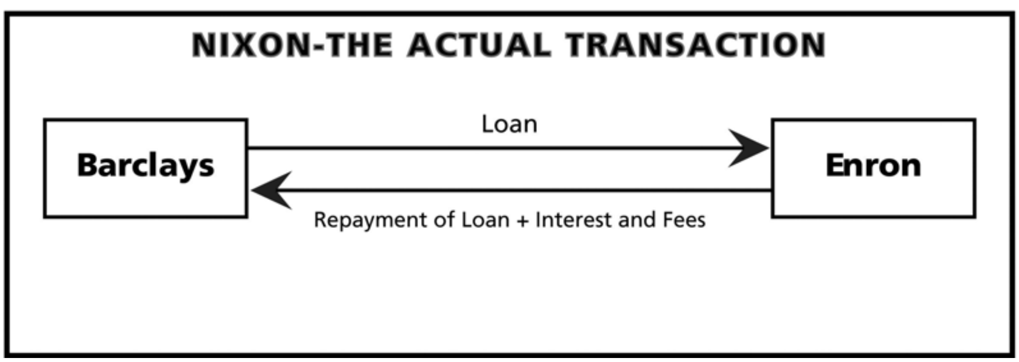
* * *

A. Yes.

Other Barclays' bankers have also described Nixon as a "loan."

761.118 The Nixon transaction was completely pre-arranged, with fixed economics – the loan to Enron and the profits to the banks, including to Barclays. No matter what happened to the price of oil, the economy or anything else, the transaction remained, as pre-arranged, with a guaranteed risk-free profit to Barclays.




761.119 A Barclays' e-mail from Brian Smith to Richard Firth, dated December 15, 1999, stated:

> As you will have guessed, the transaction was booked yesterday. The income over the 3 month duration will be a little over $400,000. Even if it is closed out early we will still earn a minimum of $320,000 so I think it was worth it.

In a legitimate commodities trade, no party to the transaction knows its profit in advance – because in a legitimate trade there is uncertainty and risk – you may win or lose. The fixed return – with a guaranteed minimum payment – to Barclays and the other banks was a payoff for their engaging in a fictitious contrivance that had the ***sole*** purpose and effect of falsifying Enron's balance sheet by providing what would look like operating cash, but was a disguised loan, deceptively packaged by Barclays so that it would not appear as a loan to Enron's creditors.

**CSFB**

761.120 The September 2001 CSFB prepay was structured this way:

***Step 1***: In 9/01, Enron and CSFB entered into a swap agreement requiring CSFB to pay Enron a lump-sum of $150,000,000. In return, Enron agreed to make quarterly floating payments to CSFB based on the spot price of 59,521 barrels of oil and a final floating payment at maturity based on 6,581,260 barrels of oil.

***Step 2***: CSFB entered into a swap with Barclays requiring CSFB to make quarterly floating rate payments to Barclays based on the spot price of 59,521 barrels of oil and a final floating payment at maturity based on 6,581,260 barrels of oil. In return, Barclays promised to pay CSFB a fixed amount of $1,368,983 each quarter and a final payment of $151,368,980.

***Step 3***: Then Barclays entered into a swap with Enron requiring Barclays to make quarterly floating rate payments to Enron based on the spot price of 59,521 barrels of oil and a final floating payment at maturity based on 6,581,260 barrels of oil. In return, Enron agreed to pay Barclays a fixed rate of $1,372,554 each quarter and a final payment at maturity of $151,763,855.

761.121 Enron got a lump-sum from CSFB, Barclays paid back CSFB (with interest) and Enron was obligated to pay back Barclays, with interest. This was a loan, not a commodities transaction, which came at a critical time when Enron was working to keep the Ponzi scheme going, fighting back against market rumors and a plunging stock price.[20] As with Roosevelt and Nixon, the

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[20] At the same time, Barclays was working on the first $SO_2$ deal, a disguised loan via a shell/sham SPE, and Nikita/Besson Trust, a fictional deal with an SPE featuring a no-loss guarantee

simultaneous and circular floating rate payments canceled each other out eliminating the substance of the apparent commodities trades. All that remained was a fiction – a loan between the parties, not, as the documents pretended, a true commodities trade with risk.

761.122 In a legitimate commodities trade, no party to the transaction knows its profit in advance – because in a legitimate trade there is uncertainty and risk – you may win or lose. The fixed return – with a guaranteed minimum payment – to Barclays and the other banks was a payoff for their engaging in a fictitious contrivance that had the ***sole*** purpose and effect of falsifying Enron's balance sheet by providing what would look like operating cash, but was a disguised loan.

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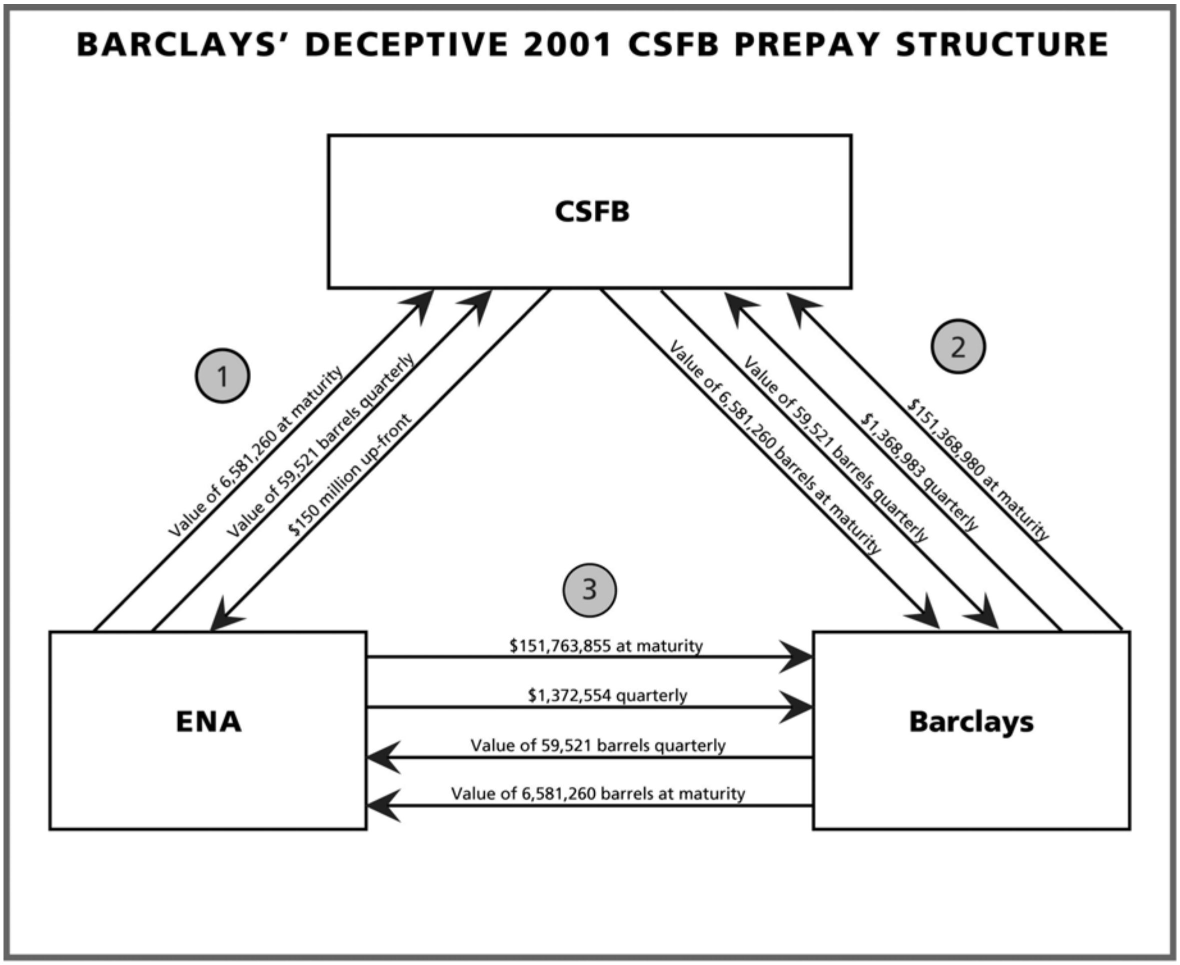
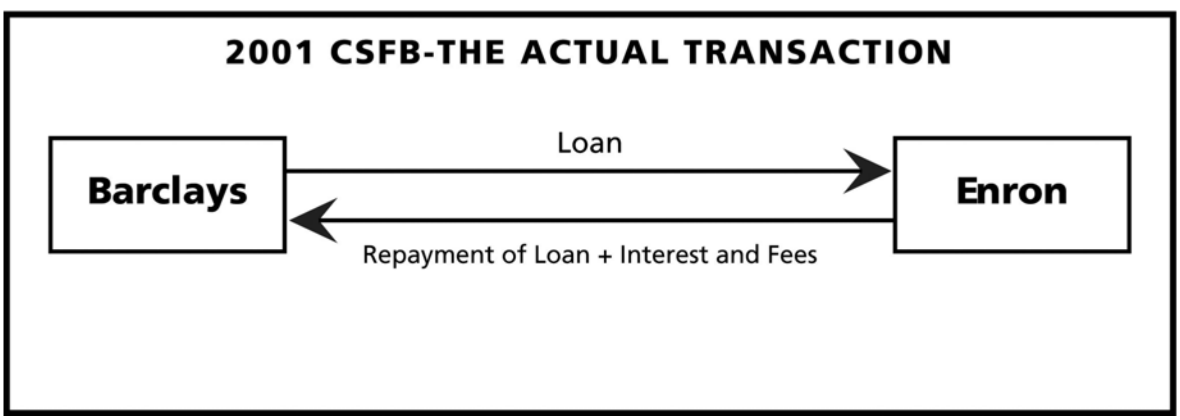
from Enron. These bogus deals created (including the prepay) over $700 million of operating cash flow/revenue and concealed millions in debt. This is important "context."




761.123 Barclays knew that the contrived and circular Roosevelt, Nixon and CSFB prepays, *i.e.*, pretend commodities trades, with Enron were not true commodities trades with economic risks but were disguised loans with assured profits for Barclays. In one e-mail dated June 24, 1999, Barclays' banker Jonathan Taylor discusses Enron's "***extremely creative . . . financial***

***engineering and [how] they appear to be able to make their published figures read just about anything they want them to***." Meyer, the senior credit officer responsible for the Enron account, confirms these observations as to these fictional commodities transactions, discussing how the fictional nature of the deals will inevitably be misaccounted for on Enron's financial statements:

> Prepaid Crude Oil and Natural Gas – ***Don't for a second think that Enron is satisfying an operating need by selling these commodities forward. Although notionally they are agreeing to deliver the commodities in satisfaction of an obligation established at the time the banks pay for the commodities, in actual fact they are only borrowing money. Their [internal] accountant will credit the Revenue account, debit Cash, debit Revenue and credit Deferred Revenue. In other words he sees a sale but sets up a liability that is satisfied only as the commodities are delivered***. . . .
>
> ***. . . Volumes at Hand – It should be troubling for their accountants that the volumes to be delivered at the latest deal's final maturity are too large for physical delivery. This should make it painfully obvious that the transaction's essence is not about deferred revenue but rather plain ol' debt***.

***This e-mail circulated throughout Barclays*** and is an admission as to the fictitious bases of these transactions, which involved huge amounts of money and several of Enron's banks – CSFB, TD, Citibank, and Barclays – all working together engaged in contrived, fictional transactions as part of their ongoing scheme to falsify Enron's financial statements. Few better examples of the incestuous operations of the largest financial fraud in U.S. history exist. One Barclays banker, Bob Clemmens, responded to this shocking internal Barclays' memo – "***[t]here should be no doubt that this note will make it to very high levels in the bank over the next few days***." No doubt it did – ***yet the deals went on***!

761.124 George McKean, a former Barclays' banker, has admitted during his deposition:

> Q. Did you agree – or do you agree now that, in actual fact – by doing these prepaid crude oil and natural gas transactions, that in actual fact, Enron was only borrowing money?
>
> A. I think it's – you know, . . . ***borrowed money*** or – I mean, it's – it's a – it's a future liability.

And Barclays' officer Pullman testified:

Q. ***As of June 24, 1999, did you have a view that Enron's prepay obligations were essentially plain ol' debt?***

A. ***Yes***.

761.125 In fact, Barclays' sophisticated bankers knew that the first of these huge prepay transactions they engaged in with Enron, *i.e.*, Roosevelt, was a disguised loan engaged in at 1998 year-end for the purpose of distorting Enron's financial reports. An e-mail drafted by Jonathan Taylor dated February 25, 1999, explaining the Roosevelt transaction stated:

> ***Enron wanted to raise $500 million before their financial year end***. . . . ***Enron set up an SPV trust called Delta which borrowed $500 million from Citibank at a fixed rate of interest***. This money was then used to buy on a prepaid basis that amount of Enron's production ratably over the next three years. Delta would then sell the production in the market using Enron as the marketing agent. Insurance companies were used to insure the performance risk of Enron for the financing. ***To remove the price risk from both sides of the transaction, Enron approached us to execute a fixed for floating swap to revert the fixed price element of the pre pay to a market rate and for similarly Delta needed the opposite swap to manage their fixed price exposure. We executed both swaps introducing a bid-offer that furnished us with a net present value of at least $250,000 and we charged an up-front fee of $250,000***.

761.126 Barclays was fully aware that by 1998, Enron's publicly released financial statements grossly understated the Company's actual debt. Meyer discusses this in his deposition:

Q. All right, sir, by 1998, 1999, whatever was the situation earlier than that, these off balance sheet transactions had become material to Enron's balance sheet?

* * *

A. There were enough credit equivalents out there that they were becoming material enough to have to be considered.

Q. All right, sir. And you observed, did you not, sir, that if you did the analysis that you've described with debt equivalents and took them into account, Enron's debt would be billions of dollars or more than was reflected on the balance sheet?

* * *

A. ***The sum of Enron's debt as reflected on the balance sheet, plus its debt equivalents would have been several billion dollars greater than its debt alone***.

* * *

Q. And you found that Enron was reporting the cash it received in these prepays as cash from operating activities, not cash from financings; correct, sir?

A. That was my belief.[21]

761.127 Barclays also knew that the banks "[would] not take physical delivery"[22] of the crude oil, instead only money would be exchanged as prearranged at the outset – because the transactions were loans but called prepays to disguise the substance of the actual transaction. Brian Smith, a senior Barclays officer, noted, "As it [Nixon] is essentially a loan we should recognize the income over the period of the loan." The natural gas and crude oil involved in these fictional commodities trades was never delivered, nor was it ever contemplated that it would be. Nor was there ever any market or price risk to the bankers involved – including Barclays.

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21 To create a clearer picture of Enron for Barclays' internal benefit, John Meyer annually analyzed and added debt to Enron's balance sheet. In his report on Enron, John Meyer added the prepays to debt because "a prepay had enough debt-like attributes that [he] thought [prepays] should [be treated] as a debt equivalent." Therefore, Meyer added the prepays to Enron's debt. According to Robert Clemmens:

Q. And when Mr. Meyer did that analysis there would be billions of dollars in debt added to the amount of debt shown on the balance sheet, correct sir?

A. Yes.

* * *

A. I recall adjustments for prepays.

22 Jonathan Taylor admitted during deposition:

Q. In 1999 was Barclays able to take physical delivery of crude oil?

A. No, I don't believe so.

* * *

Q. Okay. So in just the commodities section that you're familiar with, was Barclays, that you're familiar with, able to take physical delivery of natural gas?

A. No.

761.128 Barclays engaged in these fictional commodities trades, *i.e.*, disguised loans, for its own financial gain. Not only did Barclays pocket the pre-agreed profits these deals created for its complicit conduct, it also ensured the Bank would play a key role in the ongoing scheme ***so it could get more profitable business from Enron*** as the scheme rolled on. Ian Jefferson, a Barclays banker, e-mailed on November 26, 1999, the following to Bob Diamond and others: "[W]hen we are able (hopefully) to confirm the bridge ***loan*** it would be valuable if you called Andy Fastow, (the CFO) and ***used our response to this approach to reinforce our credentials and v.[very] strong desire to lead manage their next Euro bond***." Tit for tat.

761.129 Thus, Barclays knew what public investors did not – that Enron reported the prepays with Barclays as liabilities from price risk management activities instead of debt. Barclays was aware of Enron's "***accounting creativity***." Meyer in 1999 noted, "***Enron excels at financial engineering*** . . . . ***Earnings can be engineered***, . . . ***and they probably are at Enron***." Engineered earnings means that Barclays knew the money that they provided Enron in constructing fictional deals deceptively structured to look like legitimate arm's-length deals, *i.e.*, commodities trades and the like, would be added to Enron's cash flow from operations, or revenues, not reported as debt. Simply put, Barclays' own conduct, without more, was deceptive and a manipulative part of Enron's financial distortions.

761.130 Barclays knew that the prepays were fictional commodities trades – in truth "***plain ol' debt***" that falsified Enron's financial statements. Therefore, the Roosevelt, Nixon and CSFB prepays were three ways that Barclays engaged in fictional contrivances and non-arm's-length transactions without economic risk – using pre-agreed economics that furthered the overall fraudulent scheme that misrepresented Enron's true financial condition.

761.131 Fastow confirmed that these three prepays were loans ***disguised to appear*** as a series of commodity swaps. Barclays' ***own conduct*** yielded this deception, because executing the transactions as ostensibly independent commodity swaps gave the ***appearance*** of commodity trades, when the ***reality*** was simply that of a loan. The prepays were deceptive because the banks involved in the deals (including Barclays) made them ***appear to be*** something they were not and Barclays purported to be something it was not – a true trade counterparty, when it was really a lender. As Fastow said:

> ***[T]he financial prepays, generally speaking, in my mind, in economic substance, were loans. In other words, the banks were giving money to Enron with the expectation that they be paid back this money in the future***.
>
> ***The structure of the prepays, however, made it look like something other than loans***, so that when it was reflected in Enron's financial statements, it looked like it wasn't a financing. It looked like it was Enron receiving the cash from a normal business operation.
>
> * * *
>
> I believe the primary purpose and effect of the conduct of Barclays and Enron, in structuring, funding, and executing the Roosevelt, Nixon, and the CSFB prepays, was to cause the Company to financially report cash flow from financing activities as funds flow from operations. In so doing, Enron presented a deceptively positive credit profile.

Moreover, Fastow confirmed that the prepays "understated debt, as compared to Enron borrowing the money, on the balance sheet."

761.132 Fastow said Barclays fully understood this:

> ***I know that***, based upon my discussions with bankers and with my own finance staff, that – that ***the people at Enron, including myself, believed that the bank understood and intended to structure the transaction so that it would not have commodity or commodity price risk embedded in the transaction, so that it would not be like a more typical commodity trade***.

"I believe that based on conversations with certain bankers, they knew that the prepays and some of the share-trust transactions created the false appearance of funds flow" – and "certain bankers" included Barclays.

761.133 Barclays was a primary violator because it went beyond funding the deals and executed and implemented them as well. As Fastow made clear, "***I am aware that they [Barclays]***

***played a role in funding and executing those transactions [the Barclays' prepays]***." "***[F]unding is actually making dollars available, delivering dollars. Executing would mean taking those steps necessary to effect the transaction or close the transaction***."

761.134 In summary as to the "prepays":

- Barclays and Enron structured the prepays to appear to be commodities trades so that if outsiders examined them, they would look like legitimate trades and not loans to be shown as debt on Enron's balance sheet. By doing so, Barclays created a false appearance of fact to deceive investors.

- In a legitimate commodities trade, no party to the transaction knows its profit in advance, because in a legitimate trade there is uncertainty and risk – you may win or lose. Barclays structured the prepays to appear as if there was commodities price risk when there was not. The fixed return – with a guaranteed minimum payment – to Barclays and the other banks was a payoff for their engaging in a fictitious contrivance.

- No oil or natural gas was ever exchanged in any of these prepay transactions, nor was it ever meant to be.

- As was the case with Enron's other fraudulent prepays with Citigroup and J.P. Morgan (Delta and Mahonia), the trading activity in the documentation for these prepays never took place, because, as was prearranged and agreed, the transactions were always going to be financially settled to assure the pre-arranged financial result – cash to Enron to be repaid at fixed-rate returns to Barclays.

761.135 Thus, as to the prepay transactions, Barclays actually used or employed a shell or sham entity, *i.e.*, in Roosevelt (Delta) or mirror image swaps, as a deceptive device and/or contrivance to:

(i) create the appearance of substance where it was lacking, *i.e.*, in all of the prepay deals the transactions were set up to look like legitimate, arm's-length commodities transactions, but in reality, they were circular deals where a lump sum was paid to Enron and in return, Barclays would receive payments equal to principle and interest on a loan. All price and market risk was removed through back-to-back hedges. And, although the transactions appeared to an outside observer to require actual commodities trades, no commodities were ever going to change hands. In fact, Barclays has admitted the amount of commodities in the prepay structures was too large for physical delivery. The deals were, in senior banker John Meyer's words, "plain ol' debt";

(ii) create a fiction of legitimate commodities trades when in reality they were circular loans; and

(iii) create a false appearance of substantial revenues or operating cash flow which falsified Enron's financial statements.

761.136 In engaging in this conduct, Barclays engaged in acts and practices which operated as a fraud or deceit in connection with the purchase or sale of Enron's publicly traded securities, and with respect to all of the Barclays transactions complained of between 1997 and 2001, a scheme and course of business that operated as a fraud or deceit on those purchasers of Enron's publicly traded securities.

761.137 Barclays' acts in connection with the prepay transactions created the appearance of legitimate or conventional prepays when, in fact, they were bogus or fake loan transactions. Without Barclays conduct as a "trader" in these bogus transactions, there would not have been sham commodities deals.

761.138 The principal purpose and effect of the prepay fictional transactions was to create the false cash flow from operations that vastly understated Enron's debt.

761.139 These transactions had no economic purpose other than to pay off Barclays for falsifying Enron's financial results and inflating the price of its publicly traded securities.

761.140 Barclays' conduct in the prepay transactions significantly contributed to and, as part of the scheme alleged by Lead Plaintiff, had the foreseeable effect of concealing the risk that Enron would be unable to service its debt and end in bankruptcy, thereby causing plaintiffs' losses.

**Loss Causation**

761.141 The financial manipulations for which Barclays is directly responsible were part of the overall fraudulent scheme that misrepresented and/or concealed, *inter alia*, Enron's true financial condition (*e.g.,* earnings, debt, and cash flow) and vulnerability to bankruptcy. This scheme perpetuated the Enron house of cards, and artificially inflated the price of Enron's publicly traded securities during the Class Period. Barclays knew that its fraudulent and manipulative financial transactions with Enron would have a significant negative effect on the price of Enron's publicly traded securities if and when Enron's financial and other misrepresentations, *i.e.*, the truth about Enron, were revealed to the market. Enron's true (impaired) financial condition, prior financial manipulations and vulnerability to bankruptcy became apparent to the market over time. This occurred as (among other things) news media and analysts commented on possible financial irregularities at Enron, CEO Skilling resigned, CFO Fastow was fired, massive insider trading was recognized, and the SEC investigated Enron. This also ultimately occurred as there were disclosures of Enron's false accounting and financial gimmickry, including abuse of SPEs and related-party transactions, resulting in negative comments and downgrades by credit rating agencies and equity analysts. Class Period purchasers of Enron's publicly traded securities suffered economic losses (*i.e.,* damages) from the substantial declines in the prices of Enron's securities caused by these events, which drove the prices of those securities lower, for they had previously purchased those securities at artificially inflated prices earlier in the Class Period. Numerous examples illustrate this.

761.142 For example, on or about February 19-20, 2001, *Fortune* magazine published an article that signaled possible financial irregularities at Enron, describing Enron as a "black box" with impenetrable financial statements. On February 22, 2001, in an interview on *CNNfn*, the article's author repeated and explained the assertions made in her article. This information, calling into question the integrity of Enron's previously reported financial results and its financial condition, caused the price of Enron securities to move substantially downward, with part of the artificial inflation coming out of the stock price as Enron's stock price dropped from $76.65, just before the article's release, to a low of $69.50 on February 23, 2001, reflecting a company-specific stock decline not caused by broader market forces. Without false reassurances in response to the article and false criticism of the article by Skilling and Enron's securities analysts, the price of Enron's securities would have declined even further. Because of them, the stock continued to trade at artificially inflated albeit lower prices.

761.143 On May 6, 2001, *Off Wall Street* issued a 26-page report that also signaled possible financial irregularities at Enron. It evaluated Enron's denials of being a "black box," and concluded Enron was using "questionable" transactions to boost its reported financial results. On May 9, 2001, *TheStreet.com* re-published and more widely circulated *Off Wall Street's* analysis, alleging that Enron's financial statements were opaque and confusing and that its earnings were of poor quality, and commenting negatively on financial results being generated by transactions with related parties, inadequate cash flow and rising debt, suspect asset-sales transactions, and suspicious stock sales by Enron's senior insiders. In response to the negative information in these reports, Enron's stock price significantly declined from a close of $59.48, just prior to *Off Wall Street's* report, to a low of $56.11 on May 9, 2001, as additional artificial inflation came out of the stock price – again reflecting a further company-specific stock decline not due to broader market forces.

761.144 Growing awareness of insider selling at Enron, and the volume of shares dumped on to the market, which many market sophisticates take as a sign of likely undisclosed adverse events inside the subject company, also significantly and negatively affected Enron's stock price throughout 2001. As the sales continued and reached massive proportions, they raised increasing suspicion that Enron's true financial condition was much worse than what was being represented to the market. Analysts (including UBS on March 12 and March 26, 2001, and Prudential on March 26 and June 26, 2001) mentioned the massive insider selling as a factor causing Enron's stock price decline. For example, on July 12, 2001, *TheStreet.com* noted Skilling's "heavy sales of company stock make him one of the biggest Enron bears in the market." *The Wall Street Journal* noted on November 5, 2001, as Enron's death rattle was becoming audible:

> Another warning signal was insider stock sales through the second half of 2000, he says. That sat awkwardly with the common refrain from Wall Street analysts that investors had to just trust management given the difficulty of analyzing how earnings were derived . . . .
>
> "You look for patterns in my business," says Mr. Chanos. "The fact that this was a 'trust me' story, while management was voting with its feet was another check. While we didn't have a smoking gun, we certainly say a reason to perhaps not trust management at its word that these earnings were what they said they were."

Others had spotted the insider bail-out earlier and saw it as an ominous warning. On November 2, 2000, the Yahoo!'s Enron message board reported: "[N]ote the insider selling. They are bailing out faster than rats off a sinking ship. The rats are selling the stock." Enron stock fell from $83.81 on November 2, 2000, to $76.75 on November 3, 2000, as part of the artificial inflation came out of the stock price, reflecting another company-specific stock decline not due to broader market forces.

761.145. On August 14, 2001, Skilling, who had become Enron's CEO just a few months earlier, suddenly quit, shocking investors and analysts. The next day, Bear Stearns and Prudential reported that this raised "tremendous questions" and "deep problems and negative issues" regarding the "aggressiveness" of Enron's finances, as Enron was already plagued by negative issues, *i.e.*, quality of earnings and financial engineering, which caused its standing with the Street to plunge. It was further reported that Skilling's resignation, with that of Baxter (Enron's Vice Chairman) just weeks earlier, "signal[s] that something is wrong at Enron." Skilling's resignation and related news media and analyst reports caused the price of Enron's securities to significantly decline. Enron's stock price collapsed from a high of $43.20 on August 14, 2001, to a low of $36.87 the next day as more of the artificial inflations came out of the stock price, on Enron's then-largest one-day trading volume in history, again reflecting a company-specific stock decline not due to broader market forces.

761.146. On October 16, 2001, after the market's close, Enron released financial results for the third quarter, reporting a one-time charge of $1 billion and a reduction in shareholder equity of $1.2 billion due to ending questionable related-party transactions. This announcement, following shortly after Skilling's abrupt and suspicious resignation, resulted in significant further investor concern regarding Enron's earlier rebuttals to reports that Enron's financial results and condition were possibly due to financial irregularities or manipulation. Enron's write-down and reduction in shareholder equity and the related reports over the next two days caused Enron's stock to significantly decline from a close of $33.84 on October 16, 2001, to a low of $25.15 on October 19, 2001, as additional artificial inflations came out of the stock price on another company-specific stock decline not due to broader market forces.

761.147. On October 22, 2001, Enron revealed that the SEC had begun an informal investigation concerning certain of its related-party transactions, and after the close of the market on October 24, 2001, Enron revealed that it had fired Fastow. These announcements signaled the possibility that Enron's financial statements had in fact been impacted by fraud. Even one of Enron's most positive analysts, David Fleischer, noted the disturbing '"appearance"' that Enron was '"hiding something,"' as reported in *The Wall Street Journal* on October 24, 2001. In response to Enron's revelations through this period, and related news media and analyst reports, Enron's stock price dropped significantly further, from $24.40 on October 22, 2001, to a low of $16 on October 25, 2001. This additional artificial inflation which came out of the stock price reflected another company-specific stock decline not due to broader market forces.

761.148. As a result of the revelations of mid-October 2001, credit rating agencies placed Enron on review for possible ratings downgrades, issued negative commentary regarding the revelations of Enron's financial condition and the SEC's inquiry, and cut Enron's credit ratings. The ratings downgrades were a further reflection of Enron's true financial condition and vulnerability to bankruptcy – compared to its previously misrepresented financial strength. And as these ratings downgrades occurred, Enron's true financial condition and vulnerability to bankruptcy was further revealed when Enron made partial disclosures reflecting its true limited liquidity. This caused a further significant decline in the price of Enron's publicly traded securities from October 16, 2001, until Enron went bankrupt on December 2, 2001. From October 25 to November 6, 2001, alone, in response to these disclosures or indications of prior financial falsification or manipulation, Enron's stock price continued its descent, from a close of $16.35 on October 25, 2001, to a low of $9.38 on November 6, 2001, as more artificial inflation came out of the stock price, reflecting further company-specific stock declines not due to market forces.

761.149. On November 8, 2001, Enron filed a report on Form 8-K with the SEC that further revealed some of the previous serious manipulation of Enron's financial statements. In it, Enron announced that it intended to restate its financial statements for the years ended December 31, 1997 through 2000, and the quarters ended March 31 and June 30, 2001, and that those financial statements as well as the annual audit reports for the past four years could not be relied upon. The report on Form 8-K also disclosed that Enron had in fact "routinely" engaged in a number of other previously undisclosed "financing arrangements with third-party financial institutions" using structures similar to those causing Enron's then-anticipated restatement – such as those transactions Barclays executed with Enron. In response, Enron's stock price entered another steep downward trajectory, declining from an open of $10 on November 8, 2001, to a low of $7.21 on November 9, 2001, reflecting a company-specific decline not due to broader market forces.

761.150. Enron's stock price would have declined even further during November 8-9, 2001, but for significant buoyancy created by a press release disseminated on First Call just ***two***

***minutes*** after the announcement of Enron's report on Form 8-K. That press release announced a possible merger with Dynegy, and contemporaneous news reports repeatedly discussed the potential infusion of cash into Enron by Dynegy. The Dynegy-related reports significantly repulsed downward price pressure imposed on Enron's securities by the filing of its report on Form 8-K. As one analyst reportedly stated in a story reported on *Dow Jones Newswires* on November 8, 2001, "'if Dynegy pulls the plug (on merger talks), you could really be totaled.'"

761.151. In fact, on November 28, 2001, Dynegy announced it had terminated the merger with Enron, and shortly thereafter rating agencies Moody's, S&P, and Fitch all downgraded Enron's debt to junk status. In response, Enron's stock price plummeted from a close of $4.01 on November 27, 2001, to a then-all-time low of $0.60 on November 28, 2001, reflecting a company-specific stock decline not due to market forces. Enron filed for bankruptcy on December 2, 2001.

761.152. Other of Enron's publicly traded securities also suffered significant price declines on the above revelations causing damage to Class members who had purchased at artificially inflated prices during the Class Period. None of the price declines pleaded above were due to changed macro economic circumstances, or new industry-specific or firm-specific facts or conditions unrelated to the alleged misrepresentations or concealments.

761.153. These are only some examples of information that revealed the true (negative) state of Enron's finances in 2001. As additional information came into the market for Enron's securities, earlier skepticism gained credibility, notwithstanding defendants' attempts to deny the truth, and the price of Enron's securities fell. By the end of the Class Period, enough of the truth regarding Enron's financial circumstances had been revealed to the market to make it evident that the Company was, and likely had been for a long time, insolvent. As a result, the artificial inflation in the price of Enron's securities that was caused by the scheme was completely dissipated. Class members who purchased at inflated prices were therefore damaged.

## CONCLUSION

761.154 In summary:

- Barclays structured several transactions with Enron whose principal purpose and effect was to falsify Enron's financial statements to create false operating cash flow and profits and hide debt, distorting Enron's financial statements.

- Barclays' own conduct or role in these illegitimate transactions created the false appearance of fact, thus using or employing a deceptive device or contrivance, to deceive Enron's auditors, among others, and inevitably Enron's investors. This was collusive conduct.[23]

- In the JEDI/Chewco transaction, Barclays with Enron structured and funded a sham SPE called Chewco, where Barclays demanded secret cash offsets and no-loss guarantees, which contradicted the formal deal documentation, negating the required 3% at-risk equity requirement of SPEs, creating a fiction so as to deceive Enron's auditors into believing Chewco was a legitimate GAAP-compliant SPE. This conduct, although occurring prior to the Class Period, demonstrates Barclays' scienter, as the Chewco deal was a template for future frauds.

- Barclays created a sham/shell SPE ("Colonnade") for the $SO_2$ deals, causing this sham/pretend SPE to engage in fictional/meaningless trades to create the deceptive appearance it was a "seasoned," *i.e.*, legitimate GAAP-compliant SPE, to deceive Enron's outside auditors into believing Colonnade met its then-heightened tests for a legitimate SPE. Barclays also structured the $SO_2$ transactions involving Colonnade to be circular where the economic risk remained with Enron, not Barclays, depriving the transactions of economic substance, creating the fiction of legitimate arm's-length commodities transactions, when the reality was far different.

- In both the J.T. Holdings and Nikita transactions, Barclays demanded secret verbal guarantees from Enron so that Barclays' own purported SPE equity investments would not be at economic risk, knowing this caused the SPEs to be sham/pretend, non-GAAP-compliant entities not having 3% equity at risk. These truths were kept from Enron's auditors, made the transactions phony, and resulted in the reporting of false revenues and operating cash flow and debt levels.

- Barclays structured the Camelot I and II (Metals) transactions to include a sham/pretend option that Enron secretly agreed it would always exercise to protect Barclays from any economic risk or loss. This secret agreement disguised the true

[23] "Collusion," a term of art in the accounting and auditing profession, is deceptive conduct by parties to a transaction that impacts the accounting for the transaction. Experts and fact witnesses in this case also agree that Barclays' conduct in connection with many of these transactions was collusive. Indeed, the collusion between Barclays and Enron permeated these transactions.

nature of the transaction, as it was never an arm's-length business deal, but rather one that was entered into solely for accounting manipulation purposes.

- Barclays (and other Enron Tier One banks) structured the Roosevelt, Nixon and CSFB "prepays" as fictional commodities trades, circularized so as to eliminate all price and market risk from Barclays (and the other banks) and to disguise that they were actually loans to Enron with fixed, profitable returns to Barclays, creating a fiction to mask the true substance and economics of the transactions.

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing SUPPLEMENT TO THE FIRST AMENDED CONSOLIDATED COMPLAINT (DOCKET NO. 1388) AS TO BARCLAYS FILED PURSUANT TO THE DECEMBER 4, 2006 ORDER (DOCKET NO. 5242) document has been served by sending a copy via electronic mail to serve@ESL3624.com on December 29, 2006.

I further certify that a copy of the foregoing document has been served via overnight mail on the following parties, who do not accept service by electronic mail on December 29, 2006.

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