UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

UNITED STATES OF AMERICA	§	
	§	
v.	§	Cr. No. H-03-
	§	
KEVIN HOWARD	§	Violations: 15 U.S.C. §§ 78j(b) and 78ff;
MICHAEL KRAUTZ	§	17 C.F.R. § 240.10b-5 (Securities Fraud); 18 U.S.C. §§ 1001 (False Statements); 1343 (Wire Fraud); 371 (Conspiracy); and 2 (Aiding and Abetting).

INDICTMENT

The Grand Jury charges:

INTRODUCTION

1. At all times relevant to this Indictment, Enron Corp. ("Enron") was a publicly traded Oregon corporation with its headquarters in Houston, Texas. Enron was, among other things, the nation's largest natural gas and electricity marketer. By 2001, Enron was number seven on the list of Fortune 500 companies. Enron's stock was traded on the New York Stock Exchange, and Enron filed quarterly and annual financial statements with the United States Securities and Exchange Commission ("SEC").

2. Enron engaged in a large number of transactions with various counter-parties, including banks, companies, and special purpose entities, designed to improve Enron's balance sheet. A number of these transactions were fraudulent, in that, among other things, Enron employees made secret promises to counter-parties in order to induce them to enter into transactions. These and other transactions enabled Enron to present itself more attractively to

investors and others, as measured by criteria favored by Wall Street investment analysts, credit rating agencies, and others.

3. Prior to 1997, Enron was not involved in the telecommunications business. On July 1, 1997, Enron acquired a public utility, Portland General Corporation, based in Portland, Oregon. As part of that acquisition, Enron acquired Portland General's telecommunications division, FirstPoint Communications, Inc. ("FirstPoint"). In 1998, Enron changed the name of FirstPoint to Enron Communications, Inc. ("ECI") and expanded the business. In January 2000, ECI was renamed Enron Broadband Services ("EBS"). At all times relevant to this Indictment, ECI/EBS was a wholly-owned subsidiary of Enron engaged in the telecommunications business.

The Defendants

4. The defendant KEVIN HOWARD is a resident of Houston, Texas. HOWARD was Vice President of Finance at ECI/EBS from approximately August 1, 1999 to September 2001.

5. The defendant MICHAEL KRAUTZ is a resident of Houston, Texas. KRAUTZ was Senior Director of Transactional Accounting at ECI/EBS from approximately August 16, 1999 to October 3, 2001.

THE SCHEME TO DEFRAUD

6. In April 1999, Enron announced that it had built a software-powered telecommunications network capable of delivering advanced video and data products and services. In approximately June 1999, Enron announced that EBS had been made a "core business" at Enron. Enron made EBS a major focus of the annual conference that it hosted for securities analysts on January 20, 2000. The presentation was received favorably by analysts and

investors, and that day the share price of Enron stock increased from approximately $54 to $67, largely on the strength of Enron's representations about its telecommunications business. However, many of the representations made about Enron's network and software at the January 20, 2000 analyst conference were false, in that Enron did not possess the network software or capabilities that it claimed. Subsequently, EBS failed to generate any significant recurring revenue from its telecommunications business.

<u>The Blockbuster Agreement</u>

7. On April 5, 2000, EBS signed a 20-year exclusive agreement with Blockbuster, Inc. ("Blockbuster"), the nation's largest video rental company, to stream movies to customers' homes. Under the agreement, Blockbuster was responsible for obtaining digital rights to film content from studios and other sources. EBS was responsible for encoding the movies and streaming them over its telecommunications network to customers' homes. This business was known as "video on demand," or "VOD," because the customers were supposed to be able to access and watch movies in their homes whenever they wanted.

8. The Blockbuster contract specified, among other things, that if EBS failed to sign distribution agreements with each regional Bell operating company by December 2000, Blockbuster had the right to terminate the agreement. EBS failed to meet this requirement, and EBS faced a serious risk that Blockbuster would terminate the contract. In order to prevent termination, EBS negotiated an extension with Blockbuster in December 2000 in which both parties agreed not to terminate the agreement before March 2001. EBS and Blockbuster eventually announced the termination of the contract on March 9, 2001.

9. EBS began a test of the VOD service on approximately December 15, 2000. The

test ran for several months. EBS never developed a cost-effective way to stream movies to customers' homes, and Blockbuster and EBS never obtained sufficient quantities of premium content to distribute over the system. During this test period, customers participating in the test were not charged for EBS's VOD service, which, as a result, generated no significant revenue. Enron subsequently abandoned the VOD business.

The Braveheart Transaction

10. In approximately fall of 2000, the defendant KEVIN HOWARD ordered Enron employees who reported to him to examine the Blockbuster agreement to see if there was any way Enron could derive accelerated earnings for the fourth quarter of 2000. The structured finance transaction that resulted was known at EBS by the code name "Project Braveheart" and was designed to allow EBS to "monetize" the Blockbuster agreement. The monetization first involved calculating the net present value of the VOD business, based upon estimated future earnings from the VOD business, and then creating a joint venture that would allow EBS to sell those future earnings to a third party as a financial asset. EBS could then recognize the gain from this sale as revenue immediately at the time of the monetization, rather than gradually over the life of the agreement.

11. In order to complete the Braveheart transaction, EBS created a joint venture with two investors: nCube, a small VOD technology company based in Beaverton, Oregon, and "Thunderbird," an investment vehicle owned by an Enron-controlled investment fund called "Whitewing." nCube and Thunderbird purportedly combined to contribute 3% of the equity of the joint venture, which was called EBS Content Systems LLC. The joint venture was purposely "deconsolidated" from Enron's books so that the results of its operations were not reflected on

Enron's financial statements. EBS assigned the Blockbuster contract to the joint venture. EBS then sold a portion of its interest in the joint venture for approximately $115 million to an investment structure called "Hawaii 125-0," which previously had been created and funded by the Canadian Imperial Bank of Commerce ("CIBC").

12. Enron recognized approximately $111 million of the $115 million it received from CIBC as revenue in the fourth quarter of 2000 and the first quarter of 2001. During these quarters, the vast majority of EBS's revenue came from the Braveheart transaction. In the fourth quarter of 2000, $53 million of EBS's reported $63 million in revenue came from Braveheart, while in the first quarter of 2001, $58 million of EBS's $85 million in revenue was from the transaction. Enron reported this revenue publicly in its annual 2000 10-K form filed with the SEC on March 30, 2001 and quarterly 10-Q form for the first quarter of 2001 filed with the SEC on May 14, 2001. Absent the Braveheart revenues, EBS would have fallen far short of its stated earnings goals for both reporting periods.

Accounting Requirements for the Braveheart Transaction

13. Under relevant accounting rules, Enron could recognize earnings from the Braveheart transaction only if, among other things, three basic accounting requirements were met: (1) EBS did not control the joint venture; (2) nCube and Thunderbird made at risk equity investments in the joint venture, and these investments remained at risk for the duration of the joint venture; and (3) the Hawaii 125-0 trust's capital structure included at least a 3% at risk equity investment. The defendants HOWARD and KRAUTZ were aware of and understood these requirements. If these requirements were not met, the proceeds Enron received from CIBC would have to have been reported as debt, not revenue.

14. The defendants KEVIN HOWARD, MICHAEL KRAUTZ and others intentionally violated these accounting requirements in order to complete the transaction and record $111 million in revenue for Enron. Among other things, the defendants HOWARD, KRAUTZ, and others (1) selected nCube as a joint venture partner because they knew that nCube, an EBS vendor, would, and did, allow EBS to control the joint venture; (2) promised nCube that it could sell its interest in the joint venture to EBS or an EBS designee in early 2001 and would receive at that time its investment plus a fixed return; and (3) "sold" an interest in the joint venture to CIBC even though HOWARD and others knew that Enron had promised CIBC that it would not lose money on its Hawaii 125-0 transactions.

15. The defendants KEVIN HOWARD, MICHAEL KRAUTZ and others also intentionally deceived Arthur Andersen accountants working on the transaction by failing to disclose, among other things, that the Braveheart transaction deliberately had been structured in a way that violated applicable accounting requirements. As the defendants knew, had all of the facts about the transaction been disclosed, Enron would not have been able to report any of the $111 million in revenue.

COUNT ONE
(Conspiracy to Commit Wire and Securities Fraud)

16. The allegations of paragraphs 1 through 15 are realleged as if fully set forth here.

17. In or about and between fall 2000 and May 14, 2001, both dates being approximate and inclusive, within the Southern District of Texas and elsewhere, the defendants KEVIN HOWARD and MICHAEL KRAUTZ, together with others, did knowingly and intentionally conspire (1) willfully and unlawfully to use and employ manipulative and deceptive

devices and contrivances and directly and indirectly (i) to employ devices, schemes and artifices to defraud; (ii) to make untrue statements of material facts and omit to state facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (iii) to engage in acts, practices, and courses of conduct which would and did operate as a fraud and deceit upon members of the investing public, in connection with purchases and sales of Enron stock and by the use of the instruments of communication in interstate commerce and the mails, in violation of Title 15, United States Code, Section 78j(b), 78ff and Rule 10b-5 of the SEC, Title 17, Code of Federal Regulations, Section 240.10b-5, and (2) to devise a scheme and artifice to defraud and to obtain money and property by means of materially false and fraudulent pretenses, representations, promises, and, for the purpose of executing such scheme and artifice, to cause interstate wire communications in violation of Title 18, United States Code, Section 1343.

OVERT ACTS

18. In furtherance of the conspiracy and to effect the objects thereof, within the Southern District of Texas and elsewhere, the defendants KEVIN HOWARD and MICHAEL KRAUTZ, and others, did commit and cause to be committed the following overt acts, among others:

a. In or about early fall 2000, HOWARD ordered EBS employees to examine the Blockbuster agreement to see if Enron could use it to generate revenue in the fourth quarter of 2000.

b. On or about September 19, 2000, KRAUTZ sent an e-mail message to EBS employees regarding the Blockbuster agreement and the proposed monetization.

c. On or about October 10, 2000, HOWARD sent an e-mail message to an EBS employee discussing formation of the joint venture and the relevant accounting requirements.

d. On or about November 7, 2000, HOWARD caused an EBS employee to send an e-mail message to a representative of nCube proposing formation of the joint venture.

e. On or about November 8, 2000, HOWARD met with an nCube executive to propose formation of the joint venture.

f. On or about November 22, 2000, HOWARD and KRAUTZ participated in a telephone conversation with nCube executives to discuss the proposed joint venture.

g. On or about November 22, 2000, KRAUTZ caused an EBS employee to send to nCube executives a document that set forth proposed accounting journal entries.

h. On or about November 30, 2000, HOWARD and KRAUTZ participated in a telephone conversation with nCube executives to discuss the proposed joint venture.

i. On or about December 13, 2000, KRAUTZ sent an e-mail message to Arthur Andersen and Enron employees describing the nature of nCube's investment in the joint venture.

j. On or about February 7, 2001, KRAUTZ sent an e-mail message to an EBS employee regarding possible disclosure of information to Arthur Andersen.

k. On or about February 16, 2001, HOWARD caused $1.7 million to be wired from an Enron bank account in New York to an nCube account at the Bank of America in Beaverton, Oregon.

l. On or about March 1, 2001, KRAUTZ sent an e-mail message to an EBS employee regarding EBS's performance of duties by the joint venture.

m. On or about March 15, 2001, HOWARD sent an e-mail message to EBS

employees congratulating them on the Braveheart transaction.

n. In or about April 2001, HOWARD presented an executive summary of the Braveheart transaction to senior EBS executives.

(Title 18, United States Code, Sections 371 and 3551 et seq.)

COUNT TWO
(Securities Fraud)

19. The allegations of paragraphs 1 through 15 and 18 are realleged as if fully set forth here.

20. In or about and between fall 2000 and May 14, 2001, both dates being approximate and inclusive, within the Southern District of Texas and elsewhere, the defendants KEVIN HOWARD and MICHAEL KRAUTZ, together with others, did willfully and unlawfully use and employ manipulative and deceptive devices and contrivances and directly and indirectly (i) employ devices, schemes and artifices to defraud; (ii) make untrue statements of material facts and omit to state facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (iii) engage in acts, practices, and courses of conduct which would and did operate as a fraud and deceit upon members of the investing public, in connection with purchases and sales of Enron stock and by the use of the instruments of communication in interstate commerce and the mails.

(Title 17, Code of Federal Regulations, Section 240.10b-5; Title 15, United States Code, Sections 78j(b) and 78ff; Title 18, United States Code, Sections 2 and 3551 et seq.)

COUNTS THREE THROUGH SEVENTEEN
(Wire Fraud)

21. The allegations of paragraphs 1 through 15 and 18 are realleged as if fully set forth here.

22. On or about the dates specified below, within the Southern District of Texas and elsewhere, the defendants KEVIN HOWARD and MICHAEL KRAUTZ, together with others, having devised a scheme and artifice to defraud and to obtain money and property by means of materially false and fraudulent pretenses, representations and promises, did for the purpose of executing such scheme and artifice transmit and cause to be transmitted by means of wire communication in interstate commerce writings, signs, signals, pictures and sounds, as follows:

Count	Date	From	To	Description
3	11/07/00	Houston, TX	California	e-mail
4	11/17/00	Houston, TX	Oregon	e-mail
5	11/22/00	Houston, TX	Oregon	e-mail
6	11/22/00	Houston, TX	Oregon	e-mail
7	11/22/00	Houston, TX	Oregon	telephone call
8	11/30/00	Houston, TX	Oregon	telephone call
9	12/08/00	Houston, TX	Oregon	e-mail
10	12/20/00	Houston, TX	Oregon	e-mail
11	1/24/01	Oregon	Houston, TX	e-mail
12	1/26/01	Houston, TX	Oregon	e-mail
13	1/26/01	Oregon	Houston, TX	e-mail
14	2/08/01	Houston, TX	Oregon	e-mail

15	2/14/01	Houston, TX	Oregon	e-mail
16	2/16/01	Houston, TX	Oregon	e-mail
17	2/16/01	Houston, TX	Oregon	e-mail

(Title 18, United States Code, Sections 1343, 2 and 3551 et seq.)

COUNT EIGHTEEN
(False Statements: HOWARD)

23. The allegations of paragraphs 1 through 15 and 18 are realleged as if fully set forth here.

24. On or about September 12, 2002, within the Southern District of Texas, the defendant KEVIN HOWARD did knowingly and wilfully make materially false, fictitious and fraudulent statements and representations in a matter within the jurisdiction of the executive branch of the United States, to wit: the Federal Bureau of Investigation, in that the defendant KEVIN HOWARD stated that the equity stakes of CIBC and nCube were at risk; that there were no oral promises, side agreements, understandings, options, guarantees or commitments of any sort made to nCube about its equity investment; that he himself never made any guarantees or promises to nCube that it would be bought out; and that he was not aware of any proposals that EBS would buy back nCube's equity at a pre-determined price.

(Title 18, United States Code, Sections 1001 and 3551 et seq.)

COUNT NINETEEN
(False Statements: KRAUTZ)

25. The allegations of paragraphs 1 through 15 and 18 are realleged as if fully set forth here.

26. On or about August 8, 2002, within the Southern District of Texas, the defendant

MICHAEL KRAUTZ did knowingly and wilfully make materially false, fictitious and fraudulent statements and representations in a matter within the jurisdiction of the executive branch of the United States, to wit: the Federal Bureau of Investigation, in that the defendant MICHAEL KRAUTZ stated that no one ever stated or suggested to him prior to September 2001 that the nCube equity was not at risk; and that if the nCube equity was not at risk, then he had been misled.

(Title 18, United States Code, Sections 1001 and 3551 et seq.)

Dated: Houston, Texas
March __, 2003

A TRUE BILL

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FOREPERSON

JOSHUA R. HOCHBURG
Acting United States Attorney, Southern District of Texas

LESLIE R. CALDWELL
Director, Enron Task Force

By: ______________________________
JOHN R. KROGER
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