

OCT 15 2003

Michael N. Milby, Clerk

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

2003 OCT 15 PM 5:09

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In Re ENRON CORP. SECURITIES,
DERIVATIVE, & ERISA LITIGATION

U.S. COURTS
SOUTHERN DISTRICT
OF TEXAS

MDL 1446

This Document Relates To:

MARK NEWBY, et al.,

Plaintiffs,

CIVIL ACTION NO. H-01-3624
AND CONSOLIDATED CASES

vs.

ENRON CORP., et al.,

Defendants.

**FIRST AMENDED CROSS-COMPLAINT OF BANC OF AMERICA SECURITIES LLC
AGAINST ARTHUR ANDERSEN LLP**

Banc of America Securities LLC ("Banc of America"), Defendant and Cross-Claimant, by and through its undersigned counsel, brings these cross-claims (the "Cross-Claims") against Arthur Andersen LLP ("Andersen"), Defendant and Cross-Defendant, for breach of contract, professional negligence, negligent misrepresentation, statutory and common law fraud, and contribution. Cross-Defendant Andersen has not served a responsive pleading to the Cross-Complaint of Banc of America Securities LLC Against Arthur Andersen. As discussed below, the Cross-Claims herein arise from Andersen's deficient performance of procedures it agreed to perform for the benefit of Banc of America, and its review, audit, and/or certification of Enron Corp.'s ("Enron") financial statements for the period 1997 to 2001, including those financial statements incorporated by reference in the offering documents distributed in connection with (i) Enron's \$500 million 7.375% Notes due May 15, 2019 (the

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“7.375% Notes”), (ii) Enron’s \$222 million 7% Exchangeable Notes due July 31, 2002 (the “7% Exchangeable Notes”), and (iii) Marlin Water Trust II and Marlin Water Capital Corp. II’s \$475 million 6.31% Senior Secured Notes due 2003 and £515 million 6.19% Senior Secured Notes due 2003 (collectively, the “Marlin Notes”), as well as other work undertaken for Enron and/or for the benefit of Banc of America. In support of these Cross-Claims, Banc of America, upon knowledge as to itself, and upon information and belief as to all other matters, states as follows:

I.

JURISDICTION AND VENUE

1. This Court has subject matter jurisdiction over the Cross-Claims asserted herein pursuant to 28 U.S.C. §§ 1331 and 1367. The Cross-Claims arise out of the transaction or occurrence that is the subject matter of the original underlying consolidated action and are so related to the claims in the underlying consolidated action that they form part of the same case and/or controversy.

2. The underlying action, Newby v. Enron, et al., No. H-01-3624, was filed in the United States District Court for the Southern District of Texas on or about October 22, 2001.

3. On or about December 1, 2001, the Court ordered that the action be consolidated with other federal actions concerning Enron. The federal securities cases concerning Enron were consolidated under Newby v. Enron, et al., No. H-01-3624, as the lead case. On or about February 15, 2002, The Regents of the University of California was appointed Lead Plaintiff.

4. Venue is proper in this District pursuant to 28 U.S.C. § 1391(b).

II.

BACKGROUND

A. The Underlying Action & Banc of America's Cross-Claims

5. Plaintiffs brought the underlying action against former Enron executives, Andersen, Enron's outside legal counsel, Bank of America Corp. ("BAC"), Banc of America, and eight other financial institutions relating to the sale of, among other things: (i) Enron's 7.375% Notes; (ii) Enron's 7% Exchangeable Notes; and (iii) the Marlin Notes. On or about May 14, 2003, Plaintiffs filed their First Amended Consolidated Complaint. Plaintiffs allege that certain Defendants—other than Banc of America—violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (the "1934 Act") and Rule 10b-5 promulgated thereunder, and/or Articles 581-33A(2) and/or 581-33F(1) of the Texas Securities Act. As to Banc of America and certain other Defendants, Plaintiffs allege violations of Sections 11, 12(a)(2), and 15 of the Securities Act of 1933 (the "1933 Act") in connection with Plaintiffs' purchases of the 7.375% Notes, the 7% Exchangeable Notes, and the Marlin Notes. Banc of America served as an underwriter or dealer of these notes.

6. Banc of America denies Plaintiffs' allegations and hereby seeks appropriate relief for the injury and damages it has suffered and continues to suffer by reason of Andersen's breach of contract, negligence, and recklessness. In addition, to the extent that Plaintiffs prevail on any of their claims, Banc of America seeks contribution from Andersen, whose wrongdoing is the proximate cause of any alleged injury suffered by Plaintiffs.

7. In that regard, Andersen was Enron's long-time auditor and reviewed, audited, and/or certified Enron's financial statements and undertook numerous other engagements for Enron during the period 1997 to 2001. In that time, Enron was one of Andersen's largest and most profitable clients, and Andersen was a "Big Five" nationally-

recognized accounting firm. Among the financial statements Andersen reviewed and/or audited were those incorporated by reference in the offering documents distributed in connection with the sale of Enron's 7.375% Notes, Enron's 7% Exchangeable Notes, and the Marlin Notes.

8. For instance, the prospectus distributed in May 1999 in connection with the 7.375% Notes incorporated by reference Enron's annual report on Form 10-K for the year ended December 31, 1998 (the "1998 Form 10-K"), Enron's report on Form 8-K dated March 18, 1999 (the "March 1999 Form 8-K"), and Enron's quarterly report on Form 10-Q for the quarter ended March 31, 1999 (the "1Q 1999 Form 10-Q"), which previously had been filed with the United States Securities and Exchange Commission (the "SEC"). Andersen audited and certified the financial statements contained in the 1998 Form 10-K. In addition, with respect to the 1998 Form 10-K and the 1Q 1999 Form 10-Q, Andersen provided certain additional assurances to Banc of America, in the form of a "comfort letter," dated May 19, 1999 (the "7.375% Notes Comfort Letter"). In the 7.375% Notes Comfort Letter, Andersen represented to Banc of America that it had performed additional tests and procedures to assure Banc of America of the reliability of the financial information contained in the offering documents for Enron's 7.375% Notes and that the financial statements contained therein were accurate as of the time of the offering. Andersen also provided Banc of America with a "bring down" letter dated May 24, 1999, "reaffirming" all statements made in the Comfort Letter as of May 24, 1999 (the "Bring Down Letter"). Furthermore, Andersen issued to Banc of America a comfort letter, dated August 10, 1999, in connection with the 7% Exchangeable Notes (the "7% Exchangeable Notes Comfort Letter"), as well as a comfort letter, dated July 12, 2001, in connection with the Marlin Notes (the "Marlin Notes Comfort Letter").

9. In the 7.375% Notes Comfort Letter Andersen provided to Banc of America in connection with the offering of the 7.375% Notes, Andersen, among other things:

- represented that it had audited the consolidated balance sheets of Enron as of December 31, 1998 and 1997, and the related consolidated statements of income, comprehensive income, cash flows, and changes in shareholders' equity for each of the years ended December 31, 1996, 1997, and 1998, all included in Enron's 1998 Form 10-K and March 1999 Form 8-K, and the related financial statement schedule included in Enron's 1998 Form 10-K;
- certified that these audited financial statements included in the 1998 Form 10-K complied "in all material respects with the applicable accounting requirements" of the 1933 Act and the Securities Exchange Act of 1934 (the "1934 Act") and related SEC rules and regulations;
- represented that it had performed the procedures specified by the American Institute of Certified Public Accountants (the "AICPA") for a review of interim financial information, as described in SAS No. 71, on the unaudited consolidated condensed balance sheet as of March 31, 1999 and the unaudited consolidated condensed statements of income and cash flows for each of the three-month periods ended March 31, 1999 and 1998, all included in Enron's 1Q 1999 Form 10-Q;
- certified that "[n]othing came to [Andersen's] attention as a result of the foregoing procedures" that caused Andersen to believe that these unaudited financial statements did not comply "in all material respects with the applicable accounting requirements" of the 1934 Act and related SEC rules and regulations, or that any material modifications were required to bring these statements into conformity with "generally accepted accounting principles"; and
- performed additional procedures as to the period from April 1, 1999 to May 14, 1999, and represented that "nothing came to [Andersen's] attention that caused [it] to believe" that there was any decrease, as compared with the corresponding period in 1998, in consolidated operating revenues, net income, or basic or diluted earnings per share of common stock.

10. In the Bring Down Letter, dated May 24, 1999, Andersen, among other

things:

- "reaffirm[ed]" as of May 24, 1999 "all statements made" in the Comfort Letter, except as otherwise noted; and, in that regard:
- as to the period from April 1, 1999 to May 19, 1999, represented that "nothing came to [Andersen's] attention that caused [it] to believe" that there was any decrease, as compared with the corresponding period in

1998, in consolidated operating revenues, net income, or basic or diluted earnings per share of common stock.

11. Unbeknownst to Banc of America, however, Andersen did not fulfill its professional accounting and auditing responsibilities in connection with Enron. Rather, Andersen breached its contractual commitments to Banc of America and committed negligence and recklessness in its review, audit, and certification of Enron's financial statements, including those incorporated by reference in the offering documents distributed in connection with the 7.375% Notes, the 7% Exchangeable Notes, and the Marlin Notes.

B. The Parties

12. Cross-Claimant Banc of America is a subsidiary of BAC, with its principal place of business at 100 North Tryon Street, Charlotte, North Carolina 28255. Banc of America is an investment bank and brokerage firm, and served as an underwriter or dealer or placement agent of various Enron securities.

13. Cross-Defendant Andersen, a limited liability partnership organized and existing under the laws of the state of Illinois, was one of the "Big Five" global accounting firms. Upon information and belief, Andersen was engaged by Enron during the relevant time period to provide, among other things, expert tax, management consulting, accounting, and auditing services to Enron, and to perform expert audits and reviews of the consolidated balance sheets and other financial statements included in the annual and quarterly reports Enron filed with the SEC. Upon information and belief, Andersen was paid tens of millions of dollars in annual fees in connection with such services. As regards its auditing and other work for Enron, Andersen performed its work for Enron in many locations, including in Houston, Texas, where it also installed a team of experts within Enron's Houston offices. As Enron's long-time consultant, accountant, auditor, and resident expert, Andersen was intimately involved and fully familiar with Enron's business affairs and finances, and was responsible for the interim reviews, auditing,

and/or certification of Enron's financial statements. In light of the above and under all other circumstances, Banc of America reasonably and justifiably relied upon the financial statements that were reviewed, audited, and certified by Andersen with respect to Enron, and reasonably believed that Andersen would require Enron to properly apply Generally Accepted Accounting Standards ("GAAS") and Generally Accepted Accounting Principles ("GAAP").

14. Lead Plaintiff is The Regents of the University of California. Purported class representatives include the Washington State Investment Board; San Francisco City and County Employees' Retirement System; Employer-Teamsters Local Nos. 175 & 505 Pension Trust Fund; Hawaii Laborers Pension Plan; Staro Asset Management LLC; Amalgamated Bank as Trustee for the LongView Collective Investment Fund, LongView Core Bond Index Fund, and Certain Other Trust Accounts; Robert V. Flint; John Zegarski; Mervin Schwartz, Jr.; Steven Smith; the Archdiocese of Milwaukee; Greenville Plumbers Pension Plan; and Nathan Pulsifer, Trustee of Shooters Hill Revocable Trust. Plaintiffs and/or members of the purported class allegedly purchased, among other things, certain of the 7.375% Notes, the 7% Exchangeable Notes, and the Marlin Notes, and, allegedly, have sustained damages as a result.

15. Non-party Enron is an Oregon corporation with its principal place of business at 1400 Smith Street, Houston, Texas 77002. On or about December 2, 2001, Enron filed a petition under Chapter 11 of the United States Bankruptcy Code. During the relevant time period, however, Enron was one of the world's leading energy, commodities and services companies. Throughout its sixteen-year history (and up until the time it filed for bankruptcy), Enron retained Andersen as its sole independent auditor.

C. The 7.375% Notes

16. On or about May 24, 1999, Enron offered the 7.375% Notes for sale pursuant to a registration statement on Form S-3, No. 333-70465 (the "Registration Statement"), as described in the Prospectus Supplement dated May 19, 1999 (the "Prospectus").

17. As noted above, the Prospectus incorporates by reference the following reports filed by Enron with the SEC:

- (a) the 1998 Form 10-K;
- (b) the March 1999 Form 8-K; and
- (c) the 1Q 1999 Form 10-Q.

18. Accompanying the 1998 Form 10-K were Enron's audited consolidated balance sheets as of December 31, 1998 and 1997, consolidated statements of income, comprehensive income, cash flows, and changes in shareholders' equity for each of the years ended December 31, 1996, 1997, and 1998, and a related financial statement schedule. Also included in the 1998 Form 10-K were, among other things, Andersen's report of its audit of each such financial statement, Andersen's report of its audit of the related financial statement schedule, and Andersen's consent to the incorporation of such audit reports in the Registration Statement.

19. By consenting to the incorporation of its audit reports and to all references to its firm and its expertise in, among other things, the Registration Statement, Andersen thereby professed to special competence with regard to the information supplied. As more fully described below, Banc of America reasonably and justifiably relied on Andersen's expertise and careful exercise of its contractual obligations to Banc of America, as well as its professional duties, in connection with the audit, review, and other procedures performed with respect to

these financial statements. Andersen, however, breached its contractual and professional duties in auditing and certifying Enron's financial statements.

20. The 1Q 1999 Form 10-Q included unaudited consolidated balance sheets as of March 31, 1999 and December 31, 1998, and consolidated condensed statements of income and cash flows for each of the three-month periods ended March 31, 1998 and 1999. While Andersen did not audit these financial statements, as noted above, it represented in the Comfort Letter that it had followed procedures as specified in SAS No. 71 for the review of interim financial statements. Andersen concluded that "[n]othing came to [its] attention" that caused it to believe that the consolidated balance sheet as of March 31, 1999 and consolidated condensed statements of income and cash flows for each of the three-month periods ended March 31, 1998 and 1999 did not comply in all material respects with the applicable accounting requirements of the 1934 Act and related SEC rules and regulations, or that any material modifications were required to bring these statements into conformity with "accounting principles generally accepted in the United States."

D. The Comfort and Bring Down Letters

21. In deciding to underwrite the 7.375% Notes for what was at the time one of the largest and most successful investment-grade companies in the country (and which had in the past issued many debt and equity securities), Banc of America reasonably and justifiably relied on the expertise and representations of Andersen.

22. On or about May 19, 1999, Andersen issued the 7.375% Comfort Letter to Banc of America. As regards Andersen's review, auditing, and/or certification of Enron's financial statements incorporated by reference in the Prospectus, the 7.375% Comfort Letter (attached hereto as Exhibit A) states, in part:

May 19, 1999

LEHMAN BROTHERS INC.
BANC OF AMERICA SECURITIES LLC
CIBC WORLD MARKETS CORP.

As Underwriters
named in the Underwriting Agreement
dated May 19, 1999, relating to the issuance of
\$500,000,000 of 7.375% Notes due May 15, 2019

Dear Ladies and Gentlemen:

This letter is written at the request of Enron Corp. (an Oregon corporation) and subsidiaries ("Enron"). This letter relates to Amendment No. 1 to Form S-3 Registration Statement (Registration No. 333-70465) filed by Enron with the Securities and Exchange Commission ("Commission") under the Securities Act of 1933, as amended ("Act"), on February 3, 1999 ("Registration Statement"), with respect to the registration and sale by Enron of \$500,000,000 aggregate principal amount of 7.375% Notes due May 15, 2019, pursuant to an underwriting agreement dated May 19, 1999 ("Underwriting Agreement"). References to the "Prospectus" shall refer to the prospectus contained in the Registration Statement as supplemented by a prospectus supplement dated May 19, 1999, filed with the Commission pursuant to Rule 424(b)(2). Such Registration Statement and Prospectus incorporate by reference, among other documents filed with the Commission, the following:

- Enron's Annual Report on Form 10-K for the fiscal year ended December 31, 1998 ("1998 Form 10-K");
- Enron's Current Report on Form 8-K dated March 18, 1999 ("March 18, 1999 Form 8-K"); and
- Enron's Quarterly Report on Form 10-Q for the quarter ended March 31, 1999 ("March 31, 1999 Form 10Q").

We have audited the consolidated balance sheet of Enron as of December 31, 1998 and 1997, and the related consolidated statements of income, comprehensive income, cash flows and changes in shareholders' equity for each of the three years in the period ended December 31, 1998, all included in the March 18, 1999 Form 8-K and the 1998 Form 10-K, and the related financial statement schedule included as Item 14(a)2 included in the 1998 Form 10-K, all incorporated by reference in the Registration Statement and Prospectus; our reports with respect thereto, as

appearing in the March 18, 1999 Form 8-K and the 1998 Form 10-K, are also incorporated by reference in the Registration Statement and Prospectus.

In connection with the Registration Statement and Prospectus:

1. We are independent certified public accountants with respect to Enron within the meaning of the Act and the applicable rules and regulations thereunder adopted by the Commission.
2. In our opinion, the consolidated financial statements and financial statement schedule audited by us and incorporated by reference in the Registration Statement and Prospectus comply as to form in all material respects with the applicable accounting requirements of the Act and the Securities Exchange Act of 1934 ("Exchange Act") and the related rules and regulations adopted by the Commission.

* * *

We have carried out other procedures to May 14, 1999, as follows . . . :

With respect to the three-month periods ended March 31, 1999 and 1998, we have:

- (i) Performed the procedures specified by the American Institute of Certified Public Accountants for a review of interim financial information as described in SAS No. 71, Interim Financial Information, on the unaudited consolidated condensed balance sheet as of March 31, 1999, and the unaudited consolidated condensed statements of income and cash flows for the three-month periods ended March 31, 1999 and 1998, all included in the March 31, 1999 Form 10-Q, incorporated by reference in the Registration Statement and Prospectus.
- (ii) Inquired of certain officials of Enron who have responsibility for financial and accounting matters whether the unaudited consolidated condensed financial statements referred to in (i) comply as to form in all material respects with the applicable accounting requirements of the Exchange Act as it applies to Form 10-Q and the related rules and regulations adopted by the Commission.

* * *

5. Nothing came to our attention as a result of the foregoing procedures, however, that caused us to believe that:
 - (i) Any material modifications should be made to the unaudited consolidated condensed financial statements described in 4(i), incorporated by reference in the Registration Statement and Prospectus, for them to be in conformity with generally accepted accounting principles.
 - (ii) The unaudited consolidated condensed financial statements described in 4(i), incorporated by reference, do not comply as to form in all material respects with the applicable accounting requirements of the Exchange Act as it applies to Form 10-Q and the related rules and regulations adopted by the Commission.
6. Enron officials have advised us that no consolidated financial statements as of any date or for any period subsequent to March 31, 1999, are available; accordingly, the procedures carried out by us with respect to changes in financial statement items after March 31, 1999, have, of necessity, been even more limited than those with respect to the periods referred to in 4. We have inquired of certain officials of Enron who have responsibility for financial and accounting matters whether (a) at May 14, 1999, there was any change in the capital stock, increase in combined short-term and long-term debt or any decrease in consolidated net assets or shareholders' equity of Enron as compared with amounts shown on the March 31, 1999, unaudited consolidated condensed balance sheet, included in the March 31, 1999 Form 10-Q, incorporated by reference, in the Registration Statement and Prospectus, or (b) for the period from April 1, 1999, to May 14, 1999, there were any decreases, as compared with the corresponding period in the preceding year, in consolidated operating revenues, net income or basic or diluted earnings per share of common stock. On the basis of these inquiries and our reading of the minutes as described in 4, nothing came to our attention that caused us to believe that there was any such change, increase or decrease, except in all instances for changes, increases or decreases that the Registration Statement and Prospectus disclose have occurred or may occur, except that capital stock increased \$61 million.
7. For purposes of this letter, we have also read the information contained in Item 7. – "Management's Discussion and Analysis of Financial Condition and

Results of Operations” and “Quarterly Financial Data (Unaudited)” appearing in Note 16 to the consolidated financial statements, all included in the 1998 Form 10-K (included at Exhibit II); the information contained in Item 1. - “Business,” Item 2. - “Properties,” Item 3. - “Legal Proceedings,” Item 5. - “Market for the Registrant’s Common Equity and Related Shareholder Matters” and Item 6. - “Selected Financial Data (Unaudited),” all included in the 1998 Form 10-K (included at Exhibit III); “Computation of Ratio of Earnings to Fixed Charges (Unaudited)” on Exhibit 12 included in the 1998 Form 10-K (included at Exhibit IV); Item 2. - “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in the March 31, 1999 Form 10-Q (included at Exhibit V); “Computation of Ratio of Earnings to Fixed Charges (Unaudited)” on Exhibit 12 included in the March 31, 1999 Form 10-Q (included at Exhibit VI); and “Capitalization” and “Ratio of Earnings to Fixed Charges” included in the Prospectus (included at Exhibit VII) and performed the additional procedures stated in Exhibit I with respect to such information.

* * *

11. This letter is solely for the information of [Banc of America and the other] addresses and to assist [Banc of America and the other] underwriters in conducting and documenting their investigation of the affairs of Enron in connection with the offering of the securities covered by the Registration Statement and Prospectus . . . [R]eference may be made to it in the Underwriting Agreement or in any list of closing documents pertaining to the offering of the securities covered by the Registration Statement and Prospectus.

Very truly yours,

/s/

ARTHUR ANDERSEN LLP

23. The 7% Exchangeable Notes Comfort Letter and the Marlin Notes Comfort Letter contain similar assurances. On or about May 24, 1999, Andersen issued the Bring Down Letter to Banc of America. As regards Andersen’s review, auditing, and/or

certification of Enron's financial statements incorporated by reference in the Prospectus in connection with the 7.375% Notes, the Bring Down Letter (attached hereto as Exhibit B) states, in part:

May 24, 1999

LEHMAN BROTHERS INC.
BANC OF AMERICA SECURITIES LLC
CIBC WORLD MARKETS CORP.
As Underwriters
named in the Underwriting Agreement
dated May 19, 1999, relating to the issuance of
\$500,000,000 of 7.375% Notes due May 15, 2019

Dear Ladies and Gentlemen:

We refer to our letter of May 19, 1999, relating to Amendment No. 1 to Form S-3 Registration Statement (Registration No. 333-70465) filed by Enron Corp. (an Oregon corporation) and subsidiaries ("Enron") with the Securities and Exchange Commission ("Commission") under the Securities Act of 1933, as amended ("Act"), on February 3, 1999 ("Registration Statement"), with respect to the registration and sale by Enron of \$500,000,000 aggregate principal amount of 7.375% Notes due May 15, 2019, pursuant to an underwriting agreement dated May 19, 1999 ("Underwriting Agreement"). References to the "Prospectus" shall refer to the prospectus contained in the Registration Statement as supplemented by a prospectus supplement dated May 19, 1999, filed with the Commission pursuant to Rule 424(b)(2).

We reaffirm as of the date hereof (and as though made on the date hereof) all statements made in that letter except that, for the purposes of this letter:

- a. The reading of minutes described in paragraph 4 of that letter has been carried out through May 19, 1999 . . .
- b. The references to May 14, 1999, in paragraph 4 and 6 of that letter are changed to May 19, 1999 . . . , with the following exceptions noted in c below.
- c. As described in paragraph 6 of our letter dated May 19, 1999, Enron officials have advised us that no consolidated financial statements as of any date or for any period subsequent to March 31, 1999, are available. We have inquired of certain

officials of Enron who have responsibility for financial and accounting matters whether (a) at May 19, 1999, there was any change in the capital stock, increase in combined short-term and long-term debt or any decrease in consolidated net assets or shareholders' equity of Enron as compared with amounts shown on the March 31, 1999, unaudited consolidated condensed balance sheet included in the March 31, 1999 Form 10-Q, incorporated by reference in the Registration Statement and Prospectus, or (b) for the period from April 1, 1999, to May 19, 1999, there were any decreases, as compared with the corresponding period in the preceding year, in consolidated operating revenues, net income or basic or diluted earnings per share of common stock. On the basis of these inquiries and our reading of the minutes as described in *a*, nothing came to our attention that caused us to believe that there was any such change, increase, or decrease, except in all instances for changes, increases, or decreases that the Registration Statement and Prospectus disclose have occurred or may occur, except that capital stock increased \$61 million and combined short-term and long-term debt increased \$143 million.

d. This letter is solely for the information of [Banc of America and the other] addressees and to assist [Banc of America and the other] underwriters in conducting and documenting their investigation of the affairs of Enron in connection with the offering of the securities covered by the Registration Statement and Prospectus . . . [R]eference may be made to it in the Underwriting Agreement or in any list of closing document pertaining to the offering of the securities covered by the Registration Statement and Prospectus.

Very truly yours,

/s/

ARTHUR ANDERSEN LLP

24. The Comfort and Bring Down Letters establish Andersen's and Enron's intent that Banc of America directly benefit from their contract, as well as Andersen's awareness of its duties to Banc of America, and its breach thereof, including the following:

(a) Andersen was aware or should have known that its work, reports and representations, including those contained in or incorporated by reference or referred to in the Comfort and Bring Down Letters, the Registration Statement, and the Prospectus, were to be

used for a particular purpose, i.e., Banc of America's due diligence in connection with the underwriting of the 7.375% Notes;

(b) Banc of America was specifically known to Andersen as the entity for whose benefit Andersen's reports and representations were directly intended and were in fact made;

(c) Andersen understood Banc of America's reliance in this regard; and

(d) Banc of America reasonably and justifiably relied on Andersen's reports and representations.

E. Andersen's Breach of Contract, Negligence, and Fraud Are for the First Time Discovered by Banc of America and Others Who Relied on Andersen

25. On October 16, 2001, Enron issued a press release announcing a \$618 million total net loss for the third quarter of 2001. That same day, Enron announced to analysts that it would reduce shareholders' equity by approximately \$1.2 billion.

26. Upon information and belief, Andersen at all relevant times was aware of or should have known the following material but as yet publicly undisclosed facts:

(a) The \$1.2 billion reduction in shareholder equity was caused by the improper categorization of hundreds of millions of dollars as an increase, rather than as a decrease, to shareholders' equity;

(b) Andersen did not object to or otherwise attempt to correct the statements in Enron's October 16, 2001 press release that characterized as non-recurring certain charges against income (which characterization Andersen previously had concluded was inappropriate);

(c) Andersen knew or should have known of possible improprieties and accounting errors at Enron, as Sherron Watkins, a then-current Enron employee and former Andersen employee, had reported such conduct to an Andersen partner;

(d) In its work related to Enron, the Andersen team assigned to the Enron audit had contravened the very methodology approved by the specialists within Andersen's Professional Standards Group for the conduct of such audits; and

(e) The Andersen team assigned to the Enron audit had received a poor evaluation in 2000.

27. On or about October 17, 2001, the SEC instituted an informal inquiry into Enron, and requested that Enron voluntarily provide it with information regarding transactions between Enron and certain related parties.

28. On or about October 23, 2001, while on notice of the SEC's investigation of Enron, Andersen apparently executed a plan to destroy Enron-related documents. Destruction of Enron-related documents was undertaken in Andersen's Houston, Texas; Chicago, Illinois; Portland, Oregon; and London, England offices.

29. On or about October 31, 2001, the Board of Directors of Enron (the "Board") elected to the Board William C. Powers, Jr. and appointed him Chairman of a newly-appointed special committee charged with conducting an investigation of transactions between Enron and certain related parties (the "Special Investigative Committee of the Board"). The Special Investigative Committee of the Board also was charged with communicating with the SEC, which had, by this time, launched a formal investigation into Enron.

30. On November 8, 2001, Enron filed with the SEC a report on Form 8-K, wherein Andersen's breach of contract, and the extent of Andersen's negligence and recklessness, is indicated by, among other things, the following:

(a) The admission by Enron that the "financial statements for these periods and the audit reports relating to the year-end financial statements for 1997 through 2000 should not be relied upon"; and

(b) Admissions by Enron that a restatement of Enron's financial statements from 1997 to 2000 and the first and second quarters of 2001 (to reflect the \$1.2 billion reduction to shareholders' equity and various adjustments to certain income statements and balance sheets) was required in order to correct numerous accounting and auditing errors, because:

(i) the financial activities of Chewco Investments, L.P. ("Chewco"), a related party vis-à-vis Enron and an investor in Joint Energy Development Investments Limited Partnership ("JEDI"), should have been consolidated into Enron's financial statements beginning in November 1997;

(ii) the financial activities of JEDI, in which Enron was an investor and which was first consolidated into Enron's financial statements during the first quarter of 2001, should have been consolidated beginning in 1997; and

(iii) the financial activities of a wholly-owned subsidiary of LJM Cayman, L.P. ("LJM1"), which had engaged in structured transactions with Enron, should have been consolidated into Enron's financial statements beginning in 1999.

31. On or about December 2, 2001, Enron and certain of its subsidiaries filed with the United States Bankruptcy Court for the Southern District of New York voluntary petitions for reorganization pursuant to Chapter 11 of the United States Bankruptcy Code.

32. In or about December 2001, upon information and belief, Andersen's CEO, Joseph Berardino, admitted to the SEC that the financial statements audited by Andersen were misleading because of the improper failure to consolidate transactions between Enron and certain related parties, as required by GAAP.

33. On or about February 1, 2002, the Special Investigative Committee of the Board issued its report of its investigation of Enron (the "Powers Report"). The Powers Report,

which does not contain any findings of wrongdoing by Banc of America, contains certain findings with respect to Andersen. These findings include the following:

(a) Enron's accounting treatment of the Chewco and LJM1 transactions was "clearly wrong," and caused by mistakes in structuring the transactions "or in basic accounting."

The Special Investigative Committee of the Board further found that:

[i]n other cases, the accounting treatment was likely wrong, notwithstanding creative efforts to circumvent accounting principles through complex structuring of transactions that lacked fundamental economic substance. In virtually all of the transactions, Enron's accounting treatment was determined with extensive participation and structuring advice from Andersen, which Management reported to the Board. Enron's records show that Andersen billed Enron \$5.7 million for advice in connection with the LJM and Chewco transactions alone, above and beyond its regular audit fees;

(b) Andersen approved certain asset sales and hedging transactions, which "appear to have been designed to circumvent accounting rules" and which raised certain accounting and financial reporting issues;

(c) Andersen's CEO had admitted in Congressional testimony that "the firm had simply been wrong" with respect to certain conclusions regarding whether Enron's transactions with certain related parties met the "threshold accounting requirement" for non-consolidation;

(d) Andersen had approved certain disclosures, which "were obtuse, did not communicate the essence of the transactions completely or clearly, and failed to convey the substance of what was going on between Enron and the partnerships";

(e) There was an absence of, among other things, "objective and critical professional advice" on the part of Andersen;

(f) Andersen “did not fulfill its professional responsibilities” in connection with its audits of Enron or its responsibility to bring to Enron’s attention concerns regarding related party transactions. Specifically, the Powers Report noted:

Andersen has admitted that it erred in concluding that the Rhythms transaction was structured properly under the SPE non-consolidation rules. Enron was required to restate its financial results for 1999 and 2000 as a result. Andersen participated in the structuring and accounting treatment of the Raptor transactions, and charged over \$1 million for its services, yet it apparently failed to provide the objective accounting judgment that should have prevented these transactions from going forward. According to Enron’s internal accountants, Andersen also reviewed and approved the recording of additional equity in March 2001 in connection with this restructuring. In September 2001, Andersen required Enron to reverse this accounting treatment, leading to the \$1.2 billion reduction of equity. Andersen apparently failed to note or take action with respect to the deficiencies in Enron’s public disclosure documents.

According to recent public disclosures, Andersen also failed to bring to the attention of Enron’s Audit and Compliance Committee serious reservations Andersen partners voiced internally about the related-party transactions. An internal Andersen e-mail from February 2001 released in connection with recent Congressional hearings suggests that Andersen had concerns about Enron’s disclosures of the related-party transactions. A week after that e-mail, however, Andersen’s engagement partner told the Audit and Compliance Committee that, with respect to related-party transactions, “[r]equired disclosure [had been] reviewed for adequacy,” and that Andersen would issue an unqualified audit opinion. From 1997 to 2001, Enron paid Andersen \$5.7 million in connection with work performed specifically on the LJM and Chewco transactions. The Board appears to have reasonably relied upon the professional judgment of Andersen concerning Enron’s financial statements and the adequacy of controls for the related-party transactions. Our review indicates that Andersen failed to meet its responsibilities in both respects;

(g) “[T]he responsibility for [the] inadequate disclosures” with regard to related parties was borne in part by Andersen;

(h) The Powers Report further noted that, pursuant to AICPA standards, “[a]uditors are under an obligation not to agree to such disclosures without substantiation”;

(i) Andersen “did not function as an effective check” on the disclosure approach used by Enron. For instance, the Powers Report noted:

Andersen was copied on drafts of the financial statement footnotes and the proxy statements, and we were told that it routinely provided comments on the related-party transaction disclosures in response. We also understand that the Andersen auditors closest to Enron Global Finance were involved in the drafting of at least some of the disclosures. An internal Andersen e-mail from February 2001 released in connection with recent Congressional hearings suggests that Andersen may have had concerns about the disclosures of the related-party transactions in the financial statement footnotes. Andersen did not express such concerns to the Board. On the contrary, Andersen’s engagement partner told the Audit and Compliance Committee just a week after the internal e-mail that, with respect to related-party transactions, “[r]equired disclosure [had been] reviewed for adequacy,” and that Andersen would issue an unqualified audit opinion on the financial statements.

34. In June 2002, a federal grand jury convicted Andersen of obstruction of justice for its destruction of Enron-related documents while on notice of a federal investigation. Upon information and belief, Andersen’s license to practice auditing has since been revoked. On October 16, 2002, Andersen was sentenced to five years probation and a \$500,000 fine in connection with its criminal conviction.

III.

COUNT I. – BREACH OF CONTRACT (THIRD PARTY BENEFICIARY)

35. The allegations in Paragraphs 1 through 34 of the Cross-Claims are incorporated by reference as if fully set forth herein.

36. Andersen contracted with Enron to perform a variety of services, including work in connection with the Comfort and Bring Down Letters referred to herein, as well as auditing and accounting functions relating to, among other things, Enron's offering of the 7.375% Notes, the 7% Exchangeable Notes, and the Marlin Notes, and to exercise the standard of care, skill, and diligence expected of independent, qualified certified public accountants and expert auditors.

37. Andersen and Enron intended, and Andersen was required, to bestow upon Banc of America the direct and primary benefit of such services, as evidenced by, among other things, the Comfort and Bring Down Letters. This benefit was to be bestowed upon Banc of America, in satisfaction of certain of Enron's legal duties to Banc of America, and with Andersen's knowledge, understanding, and intent that Banc of America would rely on it, as evidenced by, among other things, the Comfort and Bring Down Letters.

38. Andersen incompetently and inaccurately performed the services and procedures referred to in the Comfort and Bring Down Letters and its review and/or audit of the financial statements of Enron, in breach of its contractual duties to Enron and to Banc of America, the intended third party beneficiary of the contract between Andersen and Enron with regard to the work performed by Andersen in connection with the Comfort and Bring Down Letters.

39. Andersen, by the breach of its contractual duties with regard to the services and procedures referred to in the Comfort and Bring Down Letters and the review and audit of Enron's financial statements, including those incorporated by reference in the Registration Statement and Prospectus, breached its duty to act in good faith and to deal fairly with Banc of America in this regard.

40. As a direct and proximate result of Andersen's breach of contract, Banc of America has suffered and continues to suffer damages, for which it hereby seeks appropriate relief.

COUNT II. - PROFESSIONAL NEGLIGENCE

41. The allegations in Paragraphs 1 through 34 and 38 of the Cross-Claims are incorporated by reference as if fully set forth herein.

42. As evidenced by, among other things, the Comfort and Bring Down Letters, Andersen owed a duty of care to Banc of America in the performance of its Enron-related auditing, accounting, and other procedures and functions, including, but not limited to, those referred to in the Comfort and Bring Down Letters, by exercising the standard of care, skill, and diligence expected of independent, qualified certified public accountants and expert auditors. Andersen was aware that Banc of America was an existing underwriter of or placement agent for various Enron securities, including Enron's 7.375% Notes, Enron's 7% Exchangeable Notes, and the Marlin Notes, and that Banc of America intended to rely on Andersen's skill and expertise in connection with Enron's financial statements, including those incorporated by reference in the Prospectus.

43. Andersen failed to conform to the generally recognized and accepted principles and standard of care required of its profession in connection with Enron's financial statements, including those incorporated by reference in the Prospectus.

44. As a direct result of Andersen's professional negligence, Banc of America has suffered and continues to suffer damages, for which it hereby seeks appropriate relief.

COUNT III. – NEGLIGENT MISREPRESENTATION

45. The allegations in Paragraphs 1 through 34, 38, and 43 of the Cross-Claims are incorporated by reference as if fully set forth herein.

46. Andersen, in the course of its engagement with Enron (including the Comfort and Bring Down Letters), negligently supplied materially false information for the benefit and guidance of Banc of America. This information was supplied by Andersen with the knowledge that Banc of America was an existing underwriter of or placement agent for various Enron securities, including Enron's 7.375% Notes, Enron's 7% Exchangeable Notes, and the Marlin Notes, and with the knowledge, understanding, and intent that Banc of America would rely on such information.

47. Andersen, in breach of its contractual and professional duties, did not exercise reasonable care or competence in obtaining or communicating such information to Banc of America.

48. Banc of America reasonably and justifiably relied on Andersen's representations in connection with, among other things, the offerings of Enron's 7.375% Notes, Enron's 7% Exchangeable Notes, and the Marlin Notes.

49. As a result of its justifiable reliance on the information supplied by Andersen in breach of Andersen's duties, Banc of America has suffered and continues to suffer damages, for which it hereby seeks appropriate relief.

COUNT IV. – COMMON LAW FRAUD (RECKLESS DISREGARD FOR THE TRUTH)

50. The allegations in Paragraphs 1 through 34, 38, and 43 of the Cross-Claims are incorporated by reference as if fully set forth herein.

51. Andersen recklessly made numerous false representations concerning material facts related to Enron's 7.375% Notes, Enron's 7% Exchangeable Notes, and the Marlin

Notes. These material misrepresentations include, without limitation, the representations in the Comfort and Bring Down Letters and in Andersen's certifications of the financial statements incorporated by reference in the Registration Statement and Prospectus.

52. Banc of America was intended to—and did in fact, reasonably and justifiably—rely upon these material misrepresentations, as evidenced by, among other things, the Comfort and Bring Down Letters.

53. As a direct and proximate result of such reliance, Banc of America has suffered and continues to suffer damages, for which it hereby seeks appropriate relief.

COUNT V. – STATUTORY FRAUD

54. The allegations in Paragraphs 1 through 34, 38, 43, and 51 of the Cross-Claims are incorporated by reference as if fully set forth herein.

55. Andersen made numerous reckless representations to Banc of America, concerning past and existing material facts related to Enron. These material misrepresentations include, without limitation, the representations in the Comfort and Bring Down Letters and in Andersen's certifications of Enron financial statements.

56. Andersen knew that Banc of America would rely upon Andersen's reckless representations, and Banc of America did in fact rely upon Andersen's reckless representations.

57. As a result, and pursuant to the provisions of Chapter 27 of the Texas Business and Commerce Code, Banc of America has suffered and continues to suffer damages, for which it hereby seeks appropriate relief.

COUNT VI. – STATUTORY CONTRIBUTION

58. The allegations in Paragraphs 1 through 57 of the Cross-Claims are incorporated by reference as if fully set forth herein.

59. Andersen contracted with Enron to perform auditing and accounting functions relating to, among other things, the offerings of Enron's 7.375% Notes, Enron's 7% Exchangeable Notes, and the Marlin Notes.

60. Andersen intended to bestow upon Banc of America the direct benefit of such services, as evidenced by, among other things, the Comfort and Bring Down Letters. This benefit was bestowed upon Banc of America, with Andersen's knowledge, understanding, and intent that Banc of America would rely on it, as evidenced by, among other things, the Comfort and Bring Down Letters.

61. Andersen owed a duty to, among others, Banc of America to exercise the standard of care and skill expected of independent, qualified certified public accountants and expert auditors in its work in connection with the Comfort and Bring Down Letters, providing the Comfort and Bring Down Letters to Banc of America, and its review and audit of Enron's financial statements.

62. Andersen incompetently and inaccurately performed its services in connection with the Comfort and Bring Down Letters and its review and audit of the financial statements of Enron, in breach of its contractual duties to Enron and to Banc of America.

63. Banc of America and Andersen, therefore, are not in pari delicto, and Banc of America bears no fault for the injury alleged by Plaintiffs.

64. To the extent that Banc of America is assigned any fault for any injury alleged by Plaintiffs in connection with their purchase of Enron securities, such fault would be of

a lesser degree than that of Andersen, as Andersen's active wrongdoing was the proximate or primary and efficient cause of any such injury.

65. As a result, and pursuant to the provisions of Chapter 33 of the Texas Civil Practice and Remedies Code, Banc of America is entitled to contribution from Andersen for any damages, interest, expenses, and/or other costs assessed against it.

IV.

PRAYER FOR RELIEF

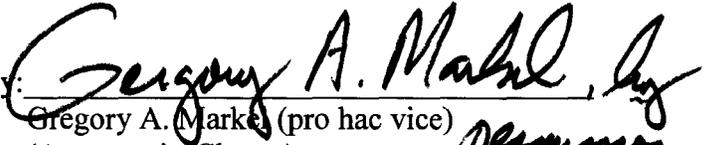
For all of the foregoing reasons, Cross-Claimant Banc of America requests the following relief against Cross-Defendant Andersen:

- (a) Judgment against Andersen for damages as provided by law;
- (b) Judgment against Andersen for contribution as provided by law;
- (c) Prejudgment interest as provided by law;
- (d) Attorneys' fees;
- (e) Post-judgment interest as provided by law;
- (f) Costs of suit; and
- (g) Such other and further relief to which it may be entitled.

Dated: October 15, 2003

Respectfully submitted,

CADWALADER WICKERSHAM & TAFT LLP

By: 

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Attorneys for Defendant and Cross-Claimant
Banc of America Securities LLC

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing instrument was served upon all known counsel of record by website, <http://www.esl3624.com>, pursuant to the Court's order dated August 7, 2002 (Docket No. 984), on this the 15th day of October, 2003.

A handwritten signature in black ink, appearing to read "Charles G. King", written over a horizontal line.

Charles G. King

ARTHUR ANDERSEN LLP

Enron Corp.
\$500,000,000 aggregate principal amount of
7.375% Notes
Due May 15, 2019

Comfort Letter
May 19, 1999

EXHIBIT A

ARTHUR ANDERSEN

May 19, 1999

Arthur Andersen LLP

LEHMAN BROTHERS INC.
BANC OF AMERICA SECURITIES LLC
CIBC WORLD MARKETS CORP.

Suite 1300
711 Louisiana Street
Houston TX 77002-2786
713 237 2323

As Underwriters
named in the Underwriting Agreement
dated May 19, 1999, relating to the issuance of
\$500,000,000 of 7.375% Notes due May 15, 2019

Dear Ladies and Gentlemen:

This letter is written at the request of Enron Corp. (an Oregon corporation) and subsidiaries ("Enron"). This letter relates to Amendment No. 1 to Form S-3 Registration Statement (Registration No. 333-70465) filed by Enron with the Securities and Exchange Commission ("Commission") under the Securities Act of 1933, as amended ("Act"), on February 3, 1999 ("Registration Statement"), with respect to the registration and sale by Enron of \$500,000,000 aggregate principal amount of 7.375% Notes due May 15, 2019, pursuant to an underwriting agreement dated May 19, 1999 ("Underwriting Agreement"). References to the "Prospectus" shall refer to the prospectus contained in the Registration Statement as supplemented by a prospectus supplement dated May 19, 1999, filed with the Commission pursuant to Rule 424(b)(2). Such Registration Statement and Prospectus incorporate by reference, among other documents filed with the Commission, the following:

- Enron's Annual Report on Form 10-K for the fiscal year ended December 31, 1998 ("1998 Form 10-K");
- Enron's Current Report on Form 8-K dated March 18, 1999 ("March 18, 1999 Form 8-K"); and
- Enron's Quarterly Report on Form 10-Q for the quarter ended March 31, 1999 ("March 31, 1999 Form 10-Q").

We have audited the consolidated balance sheet of Enron as of December 31, 1998 and 1997, and the related consolidated statements of income, comprehensive income, cash flows and changes in shareholders' equity for each of the three years in the period ended December 31, 1998, all included in the March 18, 1999 Form 8-K and the 1998 Form 10-K, and the related financial statement schedule included as Item 14(a)2 included in the 1998 Form 10-K, all incorporated by reference in the Registration Statement and Prospectus; our reports with respect thereto, as appearing in the March 18, 1999 Form 8-K and the 1998 Form 10-K, are also incorporated by reference in the Registration Statement and Prospectus.

In connection with the Registration Statement and Prospectus:

1. We are independent certified public accountants with respect to Enron within the meaning of the Act and the applicable rules and regulations thereunder adopted by the Commission.
2. In our opinion, the consolidated financial statements and financial statement schedule audited by us and incorporated by reference in the Registration Statement and Prospectus comply as to form in all material respects with the applicable accounting requirements of the Act and the Securities Exchange Act of 1934 ("Exchange Act") and the related rules and regulations adopted by the Commission.
3. We have not audited any financial statements of Enron as of any date or for any period subsequent to December 31, 1998; although we have conducted an audit for the year ended December 31, 1998, the purpose (and therefore the scope) of the audit was to enable us to express our opinion on the consolidated financial

ARTHUR ANDERSEN

Page 2
May 19, 1999

statements as of December 31, 1998, and for the year then ended, but not on the financial statements for any interim period within that year. Therefore, we are unable to and do not express any opinion on the unaudited consolidated condensed balance sheet as of March 31, 1999, and the unaudited consolidated condensed statements of income and cash flows for the three-month periods ended March 31, 1999 and 1998, all included in the March 31, 1999 Form 10-Q, incorporated by reference in the Registration Statement and Prospectus, or on the financial position, results of operations or cash flows as of any date or for any period subsequent to December 31, 1998.

4. For purposes of this letter we have read the 1999 minutes of meetings of the directors, shareholders, and committees of Enron, Enron Capital and Trade Resources Corp., Enron Gas Processing Company, Enron International Inc., Enron Power Corp., Enron Development Corp., Houston Pipe Line Company, Northern Plains Natural Gas Company, Northern Natural Gas Company, Transwestern Pipeline Company, Enron Oil & Gas Company, and Portland General Electric Company, as applicable, as set forth in the minute books as of May 14, 1999, officials of Enron having advised us that the minutes of all such meetings through that date were set forth therein, except that our work did not extend to the following minutes which had not been finalized:

<u>Meeting</u>	<u>Date of Meeting</u>
Enron -	
Compensation and Management Development Committee	January 25, 1999
Audit and Compliance Committee	February 7, 1999
Finance Committee	February 7, 1999
Compensation and Management Development Committee	February 7, 1999
Nominating and Corporate Governance Committee	February 7, 1999
Nominating and Corporate Governance Committee	March 8, 1999
Executive Committee	March 22, 1999
Executive Committee	April 13, 1999
Nominating and Corporate Governance Committee	May 3, 1999
Audit and Compliance Committee	May 3, 1999
Finance Committee	May 3, 1999
Compensation and Management Development Committee	May 3, 1999
Board of Directors	May 4, 1999
Northern Natural Gas Company-	
Board of Directors	March 10, 1999
Special Meeting of Board of Directors	April 2, 1999
Enron Oil & Gas Company -	
Board of Directors	May 4, 1999
Special Meeting of Board of Directors	May 8, 1999

We have carried out other procedures to May 14, 1999, as follows (our work did not extend to the period from May 15, 1999, to May 19, 1999, inclusive):

ARTHUR ANDERSEN

Page 3
May 19, 1999

With respect to the three-month periods ended March 31, 1999 and 1998, we have:

- (i) Performed the procedures specified by the American Institute of Certified Public Accountants for a review of interim financial information as described in SAS No. 71, Interim Financial Information, on the unaudited consolidated condensed balance sheet as of March 31, 1999, and the unaudited consolidated condensed statements of income and cash flows for the three-month periods ended March 31, 1999 and 1998, all included in the March 31, 1999 Form 10-Q, incorporated by reference in the Registration Statement and Prospectus.
- (ii) Inquired of certain officials of Enron who have responsibility for financial and accounting matters whether the unaudited consolidated condensed financial statements referred to in (i) comply as to form in all material respects with the applicable accounting requirements of the Exchange Act as it applies to Form 10-Q and the related rules and regulations adopted by the Commission.

The foregoing procedures do not constitute an audit conducted in accordance with generally accepted auditing standards. Also, they would not necessarily reveal matters of significance with respect to the comments in the following paragraph. Accordingly, we make no representations regarding the sufficiency of the foregoing procedures for your purposes.

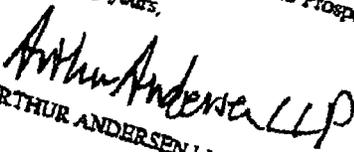
5. Nothing came to our attention as a result of the foregoing procedures, however, that caused us to believe that:
 - (i) Any material modifications should be made to the unaudited consolidated condensed financial statements described in 4(i), incorporated by reference in the Registration Statement and Prospectus, for them to be in conformity with generally accepted accounting principles.
 - (ii) The unaudited consolidated condensed financial statements described in 4(i), incorporated by reference, do not comply as to form in all material respects with the applicable accounting requirements of the Exchange Act as it applies to Form 10-Q and the related rules and regulations adopted by the Commission.
6. Enron officials have advised us that no consolidated financial statements as of any date or for any period subsequent to March 31, 1999, are available; accordingly, the procedures carried out by us with respect to changes in financial statement items after March 31, 1999, have, of necessity, been even more limited than those with respect to the periods referred to in 4. We have inquired of certain officials of Enron who have responsibility for financial and accounting matters whether (a) at May 14, 1999, there was any change in the capital stock, increase in combined short-term and long-term debt or any decrease in consolidated net assets or shareholders' equity of Enron as compared with amounts shown on the March 31, 1999, unaudited consolidated condensed balance sheet included in the March 31, 1999 Form 10-Q, incorporated by reference, in the Registration Statement and Prospectus, or (b) for the period from April 1, 1999, to May 14, 1999, there were any decreases, as compared with the corresponding period in the preceding year, in consolidated operating revenues, net income or basic or diluted earnings per share of common stock. On the basis of these inquiries and our reading of the minutes as described in 4, nothing came to our attention that caused us to believe that there was any such change, increase, or decrease, except in all instances for changes, increases, or decreases that the Registration Statement and Prospectus disclose have occurred or may occur, except that capital stock increased \$61 million.
7. For purposes of this letter, we have also read the information contained in Item 7 - "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Quarterly Financial Data (Unaudited)" appearing in Note 16 to the consolidated financial statements, all included in the 1998 Form 10-K (included at Exhibit II); the information contained in Item 1 - "Business," Item 2 - "Properties," Item 3 - "Legal Proceedings," Item 5 - "Market for the Registrant's Common Equity and Related Shareholder Matters" and

ARTHUR ANDERSEN

Item 6. - "Selected Financial Data (Unaudited)", all included in the 1998 Form 10-K (included at Exhibit III); "Computation of Ratio of Earnings to Fixed Charges (Unaudited)" on Exhibit 12 included in the 1998 Form 10-K (included at Exhibit IV); Item 2. - "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in the March 31, 1999 Form 10-Q (included at Exhibit V); "Computation of Ratio of Earnings to Fixed Charges (Unaudited)" on Exhibit 12 included in the March 31, 1999 Form 10-Q (included at Exhibit VI); and "Capitalization" and "Ratio Of Earnings To Fixed Charges" included in the Prospectus (included at Exhibit VII) and performed the additional procedures stated in Exhibit I with respect to such information.

8. Our audits of the consolidated financial statements for the periods referred to in the second paragraph of this letter comprised audit tests and procedures deemed necessary for the purpose of expressing an opinion on such financial statements taken as a whole. For none of the periods referred to therein, or for any other period, did we perform audit tests for the purpose of expressing an opinion on individual balances of accounts or summaries of selected transactions or other data such as those enumerated in the attached Exhibits, and, accordingly, we express no opinion thereon.
9. It should be understood that we make no representations as to the explanations for increases or decreases in specific amounts or percentages contained in "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in the 1998 Form 10-K (included at Exhibit II) and the March 31, 1999 Form 10-Q (included at Exhibit V). Further, we have addressed ourselves solely to the amounts and percentages as set forth and make no representations regarding the adequacy of disclosure or regarding whether any material facts have been omitted.
10. It should be understood that we make no representations regarding questions of legal interpretation or regarding the sufficiency of the procedures enumerated in this letter and in the attached Exhibits. Also, such procedures would not necessarily reveal any material misstatement of the amounts or percentages listed therein. Further, we have addressed ourselves solely to the foregoing data as set forth in the Registration Statement and Prospectus and make no representations regarding the adequacy of disclosure or regarding whether any material facts have been omitted.
11. This letter is solely for the information of the addressees and to assist the underwriters in conducting and documenting their investigation of the affairs of Enron in connection with the offering of the securities covered by the Registration Statement and Prospectus, and it is not to be used, circulated, quoted, or otherwise referred to within or without the underwriting group for any other purpose, including but not limited to the registration, purchase, or sale of securities, nor is it to be filed with or referred to in whole or in part in the Underwriting Statement and Prospectus or any other document, except that reference may be made to it in the Underwriting Agreement or in any list of closing documents pertaining to the offering of the securities covered by the Registration Statement and Prospectus.

Very truly yours,


ARTHUR ANDERSEN LLP

Oct-10-03 14:00

From-JDRP V 3

212-755-7906-3

T-205 P 07/29 F-100



<u>Symbol</u>	<u>Explanation of Symbols Used in Exhibits II through VII</u>
A	We compared the indicated amount or percentage to the corresponding amount or percentage appearing on an analysis schedule prepared by Enron and found such amounts or percentages to be in agreement, after rounding. We recomputed the amount or percentage appearing on the analysis schedule and found such amount or percentage to be arithmetically correct. We compared the components of the computation of the amount or percentage appearing on the analysis schedule to the corresponding amount appearing on the consolidated balance sheet, as of the applicable date, or the related consolidated statements of income, cash flows or changes in shareholders' equity or notes to the consolidated financial statements, for the applicable year, included in the 1998 Enron Form 10-K, 1997 Enron Form 10-K, or the 1995 Enron Form 10-K, as applicable, and found such amounts or percentages to be in agreement, after rounding.
B	We compared the indicated amount or percentage to the corresponding amount or percentage appearing on an analysis schedule prepared by Enron and found such amounts or percentages to be in agreement, after rounding. We recomputed the amount or percentage appearing on the analysis schedule and found such amount or percentage to be arithmetically correct. We compared the components of the computation of the amount or percentage appearing on the analysis schedule to the corresponding amount included in Enron's accounting records and found such amounts to be in agreement, after rounding.
C	We compared the indicated amount to the corresponding amount appearing on the consolidated balance sheet, as of the applicable date, or the related consolidated statements of income, cash flows or changes in shareholders' equity or notes to the consolidated financial statements, for the applicable year, included in the 1998 Enron Form 10-K, 1997 Enron Form 10-K, or the 1995 Enron Form 10-K, as applicable, and found such amounts to be in agreement, after rounding.
D	We compared the indicated amount to the corresponding amount included in Enron's accounting records and found such amounts to be in agreement, after rounding.
E	We compared the indicated amount or ratio to the corresponding amount or ratio appearing on an analysis schedule prepared by Enron and found such amounts or ratios to be in agreement, after rounding. Such analysis schedule reflects the amounts used in the computation of the ratio of earnings to fixed charges including (1) "Income from continuing operations," (2) "Undistributed earnings and losses of less than 50% owned affiliates," (3) "Capitalized interest of nonregulated companies," (4) "Minority interest," (5) "Income tax expense," (6) "Interest expense," (7) "Rental expense representative of interest factor," (8) "Earnings available for fixed charges," (9) "Fixed charges" and (10) "Ratio of earnings to fixed charges." We compared (1) and (4) for the applicable period, as described above, to the corresponding amount appearing on the unaudited consolidated condensed statement of income included in the March 31, 1999, Enron Form 10-Q, or on the consolidated statement of income included in the 1998 Enron Form 10-K or the 1995 Enron Form 10-K, as applicable, or included in Enron's accounting records, as applicable, and found such amounts to be in agreement, after rounding. We compared (2), (3), (5), (6) and (7) for the applicable period, as described above, to the corresponding amounts appearing on an analysis schedule. We recomputed the amounts appearing on the analysis schedule and found such amounts to be arithmetically correct. We compared the components of the computation of the amounts appearing on the analysis schedule to the corresponding amounts appearing on the unaudited consolidated condensed statement of income included in the March 31, 1999, Enron Form 10-Q, or on the consolidated statement of income included in the 1998 Enron Form 10-K or the 1995 Enron Form 10-K, as applicable, or included in Enron's accounting records, as applicable, and found such amounts to be in agreement, after rounding. We recomputed (9) for the applicable period, as described above, as the sum of (6) and (7), as described above, and found such amount to be arithmetically correct. We recomputed (8) for the applicable period, as described above, as the sum of (1), (4), (5) and (9), as described above, less the sum of (2) and (3), as described above, and found such amount to be arithmetically correct. We recomputed (10), as described above, as (8), as described above, divided by (9), as described above, and found such ratio to be arithmetically correct.

Symbol	Explanation of Symbols Used in Exhibits II through VII
F	We compared the indicated amount or percentage to the corresponding amount or percentage appearing on an analysis schedule prepared by Enron Oil & Gas Company and found such amounts or percentages to be in agreement, after rounding. We recomputed the amount or percentage appearing on the analysis schedule and found such amount or percentage to be arithmetically correct. We compared the components of the computation of the amount or percentage appearing on the analysis schedule to the corresponding amount or percentage appearing in the Enron Oil & Gas Company's 1998 Form 10-K or Enron Oil & Gas Company's accounting records, as applicable, and found such amounts to be in agreement, after rounding.
G	Not used.
H	Not used.
I	Not used.
J	Not used.
K	Not used.
L	We compared the indicated amount to the corresponding amount appearing on an analysis schedule prepared by Enron and found such amounts to be in agreement, after rounding. Such analysis schedule reflects (1) average number of common shares outstanding on a diluted basis, assuming the conversion of preferred shares to common shares, (2) average number of common shares outstanding on a diluted basis and (3) additional common shares issuable upon conversion of preferred shares. We compared (2), as described above, to the corresponding amount appearing on the consolidated statement of income included in the 1997 Enron Form 10-K and found such amounts to be in agreement, after rounding. We compared (3), as described above, to an analysis schedule prepared by Enron and found such amounts to be in agreement, after rounding. We recomputed the amount appearing on the analysis schedule and found such amount to be arithmetically correct. We compared the components of the computation of the amount appearing on the analysis schedule to the corresponding amount appearing in the notes to the consolidated financial statements included in the 1997 Enron Form 10-K or in Enron's accounting records, as applicable, and found such amounts to be in agreement, after rounding. We recomputed (1), as described above, as the sum of (2) and (3), as described above, and found such amount to be arithmetically correct. It should be noted that Statement of Financial Accounting Standards No. 128 requires that diluted earnings per share for each earnings component should not include the anti-dilutive effect of the assumed conversion of preferred shares to common shares.
M	We compared the indicated amount to the corresponding amount appearing on an analysis schedule prepared by Enron and found such amount to be in agreement, after rounding. We recomputed the amount appearing on the analysis schedule and found such amount to be arithmetically correct. Such analysis schedule utilizes a foreign currency exchange rate to convert Great Britain Pounds to US dollars. We compared the send-or-pay payments amount appearing on the analysis schedule to the corresponding amount included in Enron's accounting records and found such amounts to be in agreement, after rounding.
N	We compared the indicated amount to the corresponding amount appearing on an analysis schedule prepared by Enron and found such amounts to be in agreement, after rounding. We recomputed the amount appearing on the analysis schedule and found such amount to be arithmetically correct. We compared the components of the computation of the amount appearing on the analysis schedule to the corresponding amount appearing on the unaudited consolidated condensed statement of income included in the September 30, 1998, Enron Form 10-Q, or appearing on the consolidated statement of income included in the 1998 Enron Form 10-K, as applicable, and found such amounts to be in agreement, after rounding.

<u>Symbol</u>	<u>Explanation of Symbols Used in Exhibits II through VII</u>
O	We compared the indicated amount to the corresponding amount appearing on an analysis schedule prepared by Enron Oil & Gas Company and found such amounts to be in agreement, after rounding. We recomputed the amount included on the analysis schedule and found such amount to be arithmetically correct. We compared the components of the calculation of the amount appearing on the analysis schedule to the corresponding amount appearing in the notes to the consolidated financial statements, for the applicable year, included in Enron Oil & Gas Company's 1998 or 1997 Form 10-K, as applicable, and found such amounts to be in agreement, after rounding.
P	We compared the indicated amount or percentage to the corresponding amount or percentage appearing on an analysis schedule prepared by Enron and found such amounts or percentages to be in agreement. We recomputed the amount or percentage appearing on the analysis schedule and found such amount or percentage to be arithmetically correct. We compared the components of the computation of the amount or percentage appearing on the analysis schedule to the corresponding amount or percentage appearing on the unaudited consolidated condensed balance sheet or the related unaudited consolidated condensed statements of income, cash flows or notes to the unaudited consolidated condensed financial statements, for the applicable period, included in the March 31, 1999, Enron Form 10-Q, the September 30, 1998, Enron Form 10-Q, the June 30, 1998, Enron Form 10-Q or the March 31, 1998, Enron Form 10-Q, as applicable, and found such amounts or percentages to be in agreement, after rounding.
Q	We compared the indicated amount to the corresponding amount appearing on the unaudited consolidated condensed balance sheet, as of the applicable date, or the related unaudited consolidated condensed statements of income, cash flows or notes to the unaudited consolidated condensed financial statements, for the applicable period, included in the March 31, 1999, Enron Form 10-Q, September 30, 1998, Enron Form 10-Q, the June 30, 1998, Enron Form 10-Q or the March 31, 1998, Enron Form 10-Q, as applicable, and found such amounts to be in agreement, after rounding.
R	Not used.

EXHIBIT I

Symbol

Explanation of Symbols Used in Exhibits II through VII

- S We compared the indicated amount or percentage to the corresponding amount or percentage appearing on an analysis schedule prepared by Enron and found such amounts or percentages to be in agreement. Such analysis schedule reflects income before interest, minority interest, income taxes and unallocated expenses of (1) Enron Capital & Trade Resources North America ("ECTNA"), (2) Enron Capital & Trade Resources Europe ("ECTE"), (3) Enron International ("EI"), (4) Enron Capital Management ("ECM"), (5) Enron Engineering & Construction Corp. ("EE&CC") and (6) Wholesale Energy Operations and Services. We recomputed the amounts appearing on the analysis schedule and found such amounts to be arithmetically correct. We compared (5), as described above, to the corresponding amounts included in Enron's accounting records, and found such amounts to be in agreement. We compared (1), (2), (3) and (4) for the applicable period, as described above, to the corresponding amounts appearing on the applicable line of business analysis schedule and found such amounts to be in agreement. We recomputed the amounts appearing on the line of business analysis schedule for (1), as described above, to the corresponding amounts included in Enron's accounting records, and found such amounts to be in agreement, after rounding. The line of business analysis schedule for (2), (3) and (4), as described above, reflect (a) income before interest, minority interest, income taxes and unallocated expenses, as applicable; (b) adjustments for certain allocations of income and expense items among (2), (3) and (4), as described above; and (c) income before interest, minority interest, income taxes and unallocated expenses, as applicable, after adjustments. We compared (a), as described above, to the corresponding amounts shown in Enron's accounting records and found such amounts to be in agreement, after rounding. We compared the components of (b), as described above, on a scope basis, to the corresponding amounts shown in Enron's management reports or other analysis schedules. We compared the components of such management reports or analysis schedules, on a scope basis, to Enron's accounting records and found such amounts to be in agreement, after rounding. We recomputed (c), as described above, as the sum of (a) and (b), as described above, and found such amounts to be arithmetically correct, after rounding. We recomputed (6), as described above, and found such amounts to be in agreement, after rounding. We compared the allocation of income and expense items among (1), (2), (3) and (4), as described above, and found such amounts to be in agreement, after rounding. It should be noted that the allocation of income and expense items among (1), (2), (3) and (4), as described above, and to unallocated expenses is on a basis determined appropriate solely by management. As such, we make no representation with respect to such allocations.
- T We compared the indicated amount to the corresponding amount appearing on the consolidated statement of income, for the applicable year, included in Enron Oil & Gas Company's 1998 Form 10-K, and found such amounts to be in agreement, after rounding.
- U We compared the indicated amount to the corresponding amount included in Enron's minutes of the meetings of the Board of Directors or attachments thereto, as applicable, and found such amounts to be in agreement, after rounding.



U



Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following review of the results of operations and financial condition of Enron Corp. and its subsidiaries and affiliates (Enron) should be read in conjunction with the Consolidated Financial Statements.

RESULTS OF OPERATIONS

Consolidated Net Income

Enron's net income for 1998 was \$703 million compared to \$105 million in 1997 and \$584 million in 1996. Enron's operating segments include Exploration and Production (Enron Oil & Gas Company), Transportation and Distribution (Gas Pipeline Group and Portland General), Wholesale Energy Operations and Services (Enron Capital & Trade Resources and Enron International), Retail Energy Services (Enron Energy Services) and Corporate and Other, which includes certain new businesses. The results of Portland General have been included in Enron's Consolidated Financial Statements beginning July 1, 1997. See Note 2 to the Consolidated Financial Statements. Items impacting comparability are discussed in the respective segment results. Net income includes the following:

(In Millions)	1998	1997	1996
After-tax results before items impacting comparability	\$ 698	\$ 515	\$ 493
Items impacting comparability: (a)			
Gain on sale of 7% of Enron Energy Services shares	-	61	-
Gains on sales of Enron Oil & Gas Company stock	45	-	90
Charge to reflect losses on contracted MTBE production	(40)	(74)	-
Charge to reflect impact of amended J-Block gas contract	-	(463)	-
Gains on sales of liquids and gathering assets	-	66	59
Reserve for qualified facilities disposition	-	-	(54)
Other	-	-	(4)
Reported net income	\$ 703	\$ 105	\$ 584

(a) Tax affected at 35%, except where a specific tax rate applied.

Diluted earnings per share of common stock were as follows:

	1998	1997	1996
Diluted earnings per share:			
After-tax results before items impacting comparability	\$2.01	\$1.74	\$1.82
Items impacting comparability:			
Gain on sale of 7% of Enron Energy Services shares	-	0.21	-
Gains on sales of Enron Oil & Gas Company stock	0.13	-	0.33
Charge to reflect losses on contracted MTBE production	(0.12)	(0.25)	-
Charge to reflect impact of amended J-Block gas contract	-	(1.57)	-
Gains on sales of liquids and gathering assets	-	0.22	0.22
Reserve for qualified facilities disposition	-	-	(0.20)
Other	-	-	(0.01)
Effect of anti-dilution(a)	-	(0.03)	-
Reported diluted earnings per share	\$2.02	\$0.32	\$2.16

(a) For 1997, the conversion of preferred shares to common shares for purposes of the diluted earnings per share calculation was anti-dilutive by \$0.03 per share. However, in order to present comparable results, per share amounts for each earnings component were calculated using 225 million shares, which assumes the conversion of preferred shares to common shares.

Income Before Interest, Minority Interests and Income Taxes

The following table presents income before interest, minority interests and income taxes (IBIT) for each of Enron's operating segments (see Note 17 to the Consolidated Financial Statements):

(In Millions)	1998	1997	1996
Exploration and Production	\$ 128	\$ 183	\$ 200
Transportation and Distribution:			
Gas Pipeline Group	351	466	524
Portland General	285	114	-
Wholesale Energy Operations and Services	968	654	466
Retail Energy Services	(119)	(107)	-
Corporate and Other	(32)	(745)	48
Reported income before interest, minority interests and taxes	\$1,582	\$ 565	\$1,238

Exploration and Production

Enron's exploration and production operations are conducted by Enron Oil & Gas Company (EOG).

Wellhead volume and price statistics (including intercompany amounts) are as follows:

	1998	1997	1996
Natural gas volumes (MMcf/d) (a)			
North America	776	758	706
Trinidad	139	113	124
India	56	18	-
Total	971	889	830
Average natural gas prices (\$/Mcf)			
North America	\$1.86	\$2.20	\$1.92
Trinidad	1.06	1.05	1.00
India	2.41	2.79	-
Composite	1.78	2.07	1.78
Crude oil/condensate volumes (MBbl/d) (a)			
North America	16.6	14.2	11.6
Trinidad	3.0	3.4	5.2
India	5.1	2.3	2.8
Total	24.7	19.9	19.6
Average crude oil/condensate prices (\$/Bbl)			
North America	\$12.67	\$19.33	\$21.08
Trinidad	12.26	18.68	19.76
India	12.86	20.05	20.17
Composite	12.66	19.30	20.60

(a) Million cubic feet per day or thousand barrels per day, as applicable.

The following analyzes the significant components of IBIT for Exploration and Production:

(In Millions)

	1998	1997	1996
Net revenues	\$769	\$783	\$730
Corporate hedging activities	19	(8)	(4)
Operating expenses	219	210	181
Exploration expenses	121	102	89
Depreciation, depletion and amortization	315	278	251
Operating income	133	185	205
Other income, net	(5)	(2)	(5)
Reported income before interest, minority interests and taxes	\$128	\$183	\$200

Net Revenues

Exploration and Production's revenues, net of gas sold in connection with natural gas marketing, decreased \$14 million (2%) in 1998 after increasing \$53 million (7%) in 1997. The 1998 change reflects lower average wellhead natural gas prices and crude oil and condensate prices, partially offset by increased production volumes of both natural gas and crude oil and condensate. The 1997 increase reflected both increased average wellhead natural gas prices and increased production volumes. Other marketing activities, which include hedging, trading and natural gas marketing transactions by EOG, reduced net revenues by \$4 million in 1998 and \$61 million in 1997, compared with an increase of \$4 million in 1996. Net revenues also include gains on sales of crude oil and gas reserves and related assets of \$26 million in 1998, \$9 million in 1997 and \$20 million in 1996.

Costs and Expenses

Operating expenses and depreciation, depletion and amortization (DD&A) increased in 1998 and 1997 primarily due to expanded operations and increased worldwide production volumes in both years and a higher DD&A rate in North America in 1998.

(B)

Exploration expenses increased 19% in 1998 and 15% in 1997 as compared to the prior year, primarily as a result of increased exploratory drilling activities and expenses related to lease acquisitions in North America.

Outlook

EOG plans to continue to focus a substantial portion of its development and exploration expenditures in its major producing areas in North America. In addition, EOG anticipates additional spending for the continued development of its projects in India, Trinidad and China.

In December 1998, Enron received an unsolicited indication of interest from a third party with respect to exploring a possible transaction pursuant to which the third party would acquire Enron's shares of EOG common stock and offer to acquire the remaining shares of outstanding EOG common stock. There can be no assurance that any such transaction will be consummated.

Transportation and Distribution

Transportation and Distribution consists of Gas Pipeline Group and Portland General. Gas Pipeline Group includes Enron's interstate natural gas pipelines, primarily Northern Natural Gas Company (Northern), Transwestern Pipeline Company (Transwestern), Enron's 50% interest in Florida Gas Transmission Company (Florida Gas) and Enron's interest in Northern Border Pipeline. Portland General results are included for the period since the July 1, 1997 merger (see Note 2 to the Consolidated Financial Statements).

Gas Pipeline Group. The following table summarizes total volumes transported by each of Enron's interstate natural gas pipelines.

	1998	1997	1996
Total Volumes Transported (Bbtu/d) (a)			
Northern Natural Gas	4,098	4,364	4,577
Transwestern Pipeline	1,608	1,416	1,341
Florida Gas Transmission	1,341	1,341	1,296
Northern Border Pipeline	1,770	1,800	1,801

(a) Billion British thermal units per day. Amounts reflect 100% of each entity's throughput volumes. Florida Gas and Northern Border Pipeline are unconsolidated affiliates.

Significant components of IBIT are as follows:

(In Millions)

	1998	1997	1996
Net revenues	\$640	\$665	\$719
Operating expenses	276	310	316
Depreciation and amortization	70	69	66
Equity in earnings	32	40	35
Other income, net	25	38	44
IBIT before items impacting comparability	351	364	416
Gains on sales of liquids and gathering assets	-	102	90
Other	-	-	18
Reported income before interest and taxes	\$351	\$466	\$524

Net Revenues

Revenues, net of cost of sales, of Gas Pipeline Group declined \$25 million (4%) during 1998 and \$54 million (8%) during 1997 as compared to the applicable preceding year. The decrease in net revenue in 1998 compared to 1997 was primarily due to the warmer than normal winter in Northern's service territory and the reduction of transition costs recovered through a regulatory surcharge at Northern. The decrease in net revenues in 1997 compared to 1996 was primarily due to the sale of natural gas liquids assets in early 1997 and the turnback of capacity at Transwestern, resulting in reduced transportation revenues beginning in November 1996.

Operating Expenses

Operating expenses of Gas Pipeline Group decreased \$34 million (11%) during 1998, primarily as a result of the reduction of transition costs at Northern and lower overhead costs. Operating expenses declined \$5 million (2%) during 1997, primarily due to a reduction of transition costs at Northern.

Equity in Earnings

Equity in earnings of unconsolidated affiliates decreased \$8 million in 1998 after increasing \$5 million during 1997 as compared to 1996. These changes were primarily due to higher 1997 earnings from Citrus Corp. (Citrus), which holds Enron's 50% interest in Florida Gas. Earnings from Citrus were higher in 1997 due to a contract restructuring.

Other Income, Net

Other income, net decreased \$13 million (34%) in 1998 as compared to 1997 primarily as a result of income recognized in 1997 related to liquids assets sold in 1997. Included in 1998 were gains of \$21 million recognized from the monetization of an interest in an equity investment, substantially offset by charges related to litigation.

Items Impacting Comparability

Gains of \$102 million were recognized in 1997 related to the sales of liquids assets, including processing plants and Enron's interest in Enron Liquids Pipeline L.P. During 1996, gains of \$90 million related to the disposition of non-strategic natural gas gathering facilities were recognized, and gains of \$18 million were recorded as a result of favorable resolution of litigation.

Portland General. Results for Portland General have been included in Enron's Consolidated Financial Statements beginning July 1, 1997. Since that date, Portland General realized IBIT, as follows:

(In Millions)	1998	1997(a)
Revenues	\$1,196	\$746
Purchased power and fuel	451	389
Operating expenses	295	154
Depreciation and amortization	183	91
Other income, net	19	2
Reported income before interest and taxes	\$ 286	\$114

(a) Represents the period from July 1, 1997 through December 31, 1997.

The 1998 results were impacted by a warmer than normal winter and the transfer of the majority of its electricity wholesale business to the Enron Wholesale segment, partially offset by an increase in sales to retail customers.

Statistics for Portland General for 1998 and for the period from July 1 through December 31, 1997 are as follows:

	1998	1997
Electricity Sales (Thousand MWh) (a)		
Residential	7,101	3,379
Commercial	6,781	3,618
Industrial	3,562	2,166
Total Retail	17,444	9,163
Wholesale	10,869	13,448
Total Electricity Sales	28,313	22,611
Resource Mix		
Coal	16%	10%
Combustion Turbine	12	5
Hydro	9	5
Total Generation	37	20
Firm Purchases	56	74
Secondary Purchases	7	6
Total Resources	100%	100%
Average Variable Power Cost (Mills/KWh) (b)		
Generation	8.6	8.7
Firm Purchases	17.3	18.9
Secondary Purchases	23.6	13.2
Total Average Variable Power Cost	15.6	17.2
Retail Customers (end of period, thousands)	704	685

(a) Thousand megawatt-hours.

(b) Mills (1/10 cent) per kilowatt-hour.

Outlook

Transportation and Distribution should continue to provide stable earnings and cash flows during 1999, including steady growth over 1998 levels.

Gas Pipeline Group continues to expand its pipeline system to provide services to existing customers and new markets. Florida Gas has an expansion planned to provide new capacity of 270 MMcf/d into Southwest Florida by the year 2001 and is evaluating other expansions to meet Florida's expected strong growth in gas consumption. Future results of Northern Border Pipeline will reflect its 700 MMcf/d extension of service to the Chicago market area. A further expansion to

Indiana through a 35-mile, 545 MMcf/d extension of its pipeline will be placed in service in the year 2000. Transwestern is considering expansions to bring in additional supplies from the San Juan basin to California.

Portland General anticipates continuing retail customer growth in one of the fastest growing service territories in the U.S. In late 1997, Portland General filed a Customer Choice Plan proposal and rate case with the Oregon Public Utility Commission (OPUC) which would open its service territory to competition. Under the proposed Customer Choice Plan, Portland General would separate its generation business from its transmission and distribution businesses and Portland General would become a regulated transmission and distribution company focused on delivering, but not selling, electricity. In July 1998, the OPUC staff issued its position, disagreeing with Portland General's proposal for full customer choice.

In January 1999, the OPUC issued an order, which is contingent upon the adoption of certain regulatory changes by the Oregon Legislature, with recommendations that included allowing small retail customers a limited set of options including the ability to continue to purchase rate-regulated electricity, allowing most commercial and industrial users to have the ability to choose their electricity provider and allowing Portland General to sell its coal- and gas-fired generation plants but rejecting Portland General's request to sell its hydroelectric assets. Additionally, the order requires Portland General, should it choose to adopt OPUC's recommendations, to file a new rate case. Portland General is reviewing the OPUC order, but will not implement any of the recommendations until the changes are agreed upon by all parties. The issue of restructuring will be further addressed by the 1999 Oregon Legislature. Portland General will support legislation that creates a comprehensive approach to the electricity industry that helps develop a market that is truly competitive.

Wholesale Energy Operations and Services

Enron's wholesale energy operations and services business (Enron Wholesale) operates in North America, Europe and other countries. Activities are conducted primarily by Enron Capital & Trade Resources and Enron International. Enron Wholesale is categorized into two business lines: (a) Commodity Sales and Services and (b) Energy Assets and Investments. Integrated energy-related products and services related to these business lines are offered to wholesale customers in varying degrees in each of Enron Wholesale's markets.

Enron manages its commodity and asset portfolios in order to maximize value, minimize the associated risks and provide overall liquidity. In this process, Enron utilizes portfolio and risk management disciplines including certain hedging transactions to manage portions of its market exposures (commodity, interest rate, foreign currency and equity exposures). Enron Wholesale from time to time monetizes its contract portfolios (producing cash and transferring counterparty credit risk to third parties) and sells interests in investments and assets.

The following table reflects IBIT for each business line:

(In Millions)	1998	1997	1996
Commodity Sales and Services	\$411	\$249	\$348
Energy Assets and Investments	709	565	263
Unallocated expenses	(152)	(160)	(145)
Reported income before interest, minority interests and taxes	\$968	\$654	\$466

The following discussion analyzes the contributions to IBIT for each business line.

Commodity Sales and Services. Enron Wholesale provides reliable delivery of energy commodities at predictable prices. The commodity sales and services operations includes the purchase, sale, marketing and delivery of natural gas, electricity, liquids and other commodities, restructuring of existing long-term contracts and the management of Enron's commodity contract portfolios. In addition, Enron provides risk management products and services to energy customers that hedge movements in price and location-based price differentials. Enron's risk management products and services are designed to provide stability to customers in markets impacted by commodity price volatility. Also included in this business is the management of certain operating assets that directly relate to this business, including domestic intrastate pipelines and storage facilities.

Enron Wholesale markets and transports a substantial quantity of energy commodities as reflected in the following table (including intercompany amounts):

	1998	1997	1996
Physical Volumes (BBtue/d) (a) (b)			
Gas:			
United States	7,418	7,654	6,998
Canada	3,486	2,263	1,406
Europe and Other	1,251	660	289
	13,155	10,577	8,693
Transport Volumes	559	460	544
Total Gas Volumes	12,714	11,037	9,237
Crude Oil and Liquids	3,570	1,677	1,507
Electricity(c)	11,024	5,256	1,648
Total Physical Volumes (BBtue/d)	27,308	17,970	12,392
Electricity Volumes Marketed (Thousand MWh)			
United States	401,843	191,746	60,150
Europe and Other	529	100	-
Total	402,372	191,846	60,150
Financial Settlements (Notional) (BBtue/d)	75,266	49,082	35,259

(a) Billion British thermal units equivalent per day.

(b) Includes third-party transactions by Enron Energy Services.

(c) Represents Electricity Volumes Marketed, converted to BBtue/d.

The earnings from commodity sales and services operations increased **65%** in 1998 as compared to 1997. The change is primarily due to increased earnings from originations of risk management products and services in North America, including contract restructurings, and increased power marketing earnings, where volumes have increased over 100%, partially offset by fewer originations in Europe. Lower earnings related to domestic operating assets and higher expenses.

The earnings from commodity sales and services operations decreased **28%** in 1997 as compared to 1996 primarily due to lower domestic gas and power margins in 1997 compared with 1996. Although volumes were higher in 1997, greater seasonal volatility of domestic natural gas prices provided higher margins in 1996. Domestic liquids marketing activity was also lower in 1997 compared with 1996. These decreases were partially offset by increased activity in the European markets related to natural gas and power contracts, including originations with utilities and independent power producers (IPPs) in 1997. Originations

(S)

from long-term contracts in North America decreased in 1997 for both natural gas and power.

Energy Assets and Investments. Enron Wholesale's energy assets and investments activities include investments in debt and equity securities of oil and gas producers and other energy-intensive companies. Additionally, Enron Wholesale develops, constructs, operates and manages a large portfolio of energy investments such as power plants and natural gas pipelines. Earnings primarily result from changes in the market value of merchant investments held during the period, equity earnings and gains on sales or restructurings of energy investments. See Note 4 to the Consolidated Financial Statements for a summary of these investments.

Earnings from energy assets and investments increased 25% in 1998 as compared to 1997 primarily as a result of earnings from the sale of interests in the Puerto Rico, Turkey, Italy and U.K. power projects, from which Enron realized the value created during the development and construction phases, partially offset by development costs and decreased earnings from the management of Enron Wholesale's merchant investments. Some of these transactions involved securitizations in which Enron retained certain interests associated with the underlying assets.

Earnings from energy assets and investments increased 115% in 1997 compared with 1996 due primarily to a significant increase in the market value of its investments, including the positive impact of a change in the structure of a joint venture investment, as well as increased earnings from originations and earnings from the sale of interests in U.K. power projects. Also contributing to the increase were fees earned on projects in the U.K.

Unallocated Expenses. Net unallocated expenses include rent, systems expenses and other support group costs.

Outlook

Enron anticipates continued growth in Enron Wholesale during 1999 due to further expansion into new products and markets. In the commodity sales and services business, volumes are expected to continue to increase as Enron maintains or increases its market share in the growing unregulated U.S. power market and the European gas and power markets. In addition, Enron expects to benefit from opportunities related to its substantial portfolio of commodity contracts. Enron also expects to continue increased integration of financial products with its energy commodity portfolio. In the energy assets and investments business, Enron will continue to benefit from opportunities related to its energy investments, including sales or restructurings of appreciated investments, and in providing capital to energy-intensive customers. Equity earnings from operations are expected to increase as a result of commencement of commercial operations of new power plants and pipeline in early 1999 including the larger power project in India.

As December 31, 1998, the following international projects were under construction:

	Size/Capacity	Estimated Commercial Operations Date
Pipeline(a)		
Bolivia/Brazil (Phase I)	1,180 miles	2Q 1999
Power Plants(a)		
Cuiaba - Brazil (Phase I)	150 MW(b)	1Q 1999
Dabhol - India (Phase I)	826 MW	1Q 1999
Piti - Guam	80 MW	1Q 1999
Sutton Bridge - U.K.	790 MW	1Q 1999
Trakya - Turkey	478 MW	1Q 1999
Corinto - Nicaragua	71 MW	2Q 1999
EcoElectrica - Puerto Rico	507 MW	3Q 1999
Nowa Sazyma - Poland	116 MW	4Q 1999
Sarlux - Italy	551 MW	1Q 2000

(a) Enron holds varying interests in these projects.
(b) Megawatts.

Earnings from Enron Wholesale are dependent on the origination and completion of transactions, some of which are individually significant and which are impacted by market conditions, the regulatory environment and customer relationships. Enron Wholesale's transactions have historically been based on a diverse product portfolio, providing a solid base of earnings. Enron's strengths, including its ability to identify and respond to customer needs, access to extensive physical assets and its integrated approach to meeting customers needs, are important drivers of the expected continued earnings growth. In addition, significant earnings are expected from Enron Wholesale's commodity portfolio and investments, which are subject to market fluctuations. External factors, such as the amount of volatility in market prices, impact the earnings opportunity associated with Enron Wholesale's business. Risk related to these activities is managed using naturally offsetting transactions and hedge transactions. The effectiveness of Enron's risk management activities can have a material impact on future earnings. See "Financial Risk Management" for a discussion of market risk related to Enron Wholesale.

Retail Energy Services

Enron Energy Services (Energy Services), formed in late 1996, is extending Enron's energy expertise to end-use business customers. This includes sales of natural gas, electricity and outsourcing energy management services directly to commercial and industrial customers. Energy Services reported losses before interest, minority interests and taxes of \$119 million in 1998 and \$107 million in 1997 related to significant investments in building its sales and service capabilities, developing products and services, establishing a support system to service its contracts and supporting Energy Services' regulatory efforts.

During 1998, Energy Services completed a significant number of transactions which will provide future revenues and margins. Energy Services revenues totaled \$1.1 billion during 1998, a 57% increase from 1997.

In late 1997, Enron sold approximately 7% of its ownership of Energy Services for \$130 million, to defray startup costs and establish a valuation for this new business. The transaction resulted in an after-tax gain of \$61 million, which has been reflected in Corporate and

Other. This sale of Energy Services ownership reflected a total enterprise value of \$1.9 billion. Since that time, significant new customers and long-term contracts have been obtained.

Outlook

During 1999, Enron anticipates continued growth in the demand for energy outsourcing solutions. Energy Services will focus on delivering these services to its existing customers, while continuing to expand its commercial and industrial customer base for total energy outsourcing. Energy Services also plans to continue integrating its service delivery capabilities, focusing on the development of best practices, nation-wide procurement opportunities, efficient use of capital and centralized decision making. Energy Services expects reduced losses in 1999.

Corporate and Other

Corporate and Other includes results of Azurix Corp., which provides water and wastewater services, Enron Communications, Inc. (ECI), which is building a national Internet-protocol fiber-optic network to deliver high content media to business customers, Enron Renewable Energy Corp. (EREC), EOTT Energy Corp. (EOTT) and the operations of Enron's methanol and MTBE plants. Significant components of IBIT are as follows:

(In Millions)	1998	1997	1996
IBIT before items impacting comparability	\$ 7	\$ (31)	\$ (22)
Items impacting comparability:			
Gain on sale of 7% of Enron Energy Services shares	-	61	-
Gains on sales of Enron Oil & Gas Company stock	22	-	178
Charge to reflect losses on contracted MTBE production	(61)	(100)	-
Charge to reflect impact of amended J-Block gas contract	-	(675)	-
Reserve for qualified facilities disposition	-	-	(83)
Miscellaneous reserves and other items	-	-	(25)
Reported income before interest and taxes	\$ (32)	\$ (745)	\$ 48

Results in 1998 were favorably impacted by increased earnings related to ECI from the sale of capacity on its fiber-optic network and increases in the market value of certain corporate-managed financial instruments, partially offset by higher corporate expenses.

During 1998, Enron recognized a pre-tax gain of \$22 million on the delivery of 10.5 million shares of EOG stock held by Enron as repayment of mandatorily exchangeable debt. Enron also recorded a \$61 million charge to reflect losses on contracted MTBE production.

During 1997, Enron recorded a non-recurring charge of \$675 million, primarily reflecting the impact of Enron's amended J-Block gas contract in the U.K. and a \$100 million charge primarily to reflect losses on contracted MTBE production. In 1996, a gain of \$178 million was recognized, primarily related to the sale of 12 million outstanding shares of EOG stock held by Enron. The 1996 results included an \$83 million reserve related to the required disposition of certain assets in connection with the merger with Portland General.

Interest and Related Charges, Net

Interest and related charges, net of interest capitalized, increased \$149 million in 1998 and \$127 million in 1997. The increase in 1998 as compared to 1997 was primarily a result of higher debt

levels, including the issuance of approximately \$2.1 billion in debt between November 1997 and the end of 1998, mainly to finance capital expenditures and investments. The 1998 interest expense also reflects the impact of twelve months of interest expense on debt related to the merger with Portland General. The 1997 increase was primarily due to higher debt levels, including debt of \$1.1 billion from Portland General following the merger on July 1, 1997 (see Note 2 to the Consolidated Financial Statements). Interest capitalized, which totaled \$66 million, \$18 million and \$12 million for 1998, 1997, and 1996, respectively, increased in 1998 as a result of the commencement of construction of several power projects.

Dividends on Company-Obligated Preferred Securities of Subsidiaries

Dividends on company-obligated preferred securities of subsidiaries increased from \$34 million in 1996 to \$69 million in 1997 and to \$77 million in 1998, primarily due to the issuance of \$215 million and \$372 million of additional preferred securities by Enron subsidiaries during 1996 and 1997, respectively. Company-obligated preferred securities of subsidiaries also increased by \$29 million in 1997 for securities of Portland General.

Minority Interests

Minority interests were \$77 million in 1998 compared to \$80 million in 1997 and \$75 million in 1996. Minority interests in 1998 include EOG and the minority owner's share of dividends on preferred stock issued in connection with the formation of an Enron-controlled joint venture in late 1997. See Note 8 to the Consolidated Financial Statements. Minority interests in 1997 and 1996 relate to EOG and Enron Global Power & Pipelines, L.L.C. (EPP) until Enron's acquisition of the EPP minority interest in November 1997.

Income Tax Expense

Income tax expense increased in 1998 as compared to 1997 primarily as a result of increased earnings, partially offset by differences between the book and tax basis of certain assets and stock sales.

Income tax expense decreased for 1997 as compared to 1996 primarily as a result of pretax losses due to the non-recurring charges for the restructuring of Enron's J-Block contract and for losses on contracted MTHE production. In addition, the 1997 tax provision was reduced for differences between the book and tax basis of certain assets and stock sales.

YEAR 2000

The Year 2000 problem results from the use in computer hardware and software of two digits rather than four digits to define the applicable year. The use of two digits was a common practice for decades when computer storage and processing was much more expensive than today. When computer systems must process dates both before and after January 1, 2000, two-digit year 'fields' may create processing ambiguities that can cause errors and system failures. For example, computer programs that have date-sensitive features may recognize a date represented by '00' as the year 1900, instead of 2000. These errors or failures may have limited effects, or the effects may be widespread, depending on the computer chip, system or software, and its location and function.

The effects of the Year 2000 problem are exacerbated because of the interdependence of computer and telecommunications systems in the United States and throughout the world. This interdependence certainly is true for Enron and Enron's suppliers, trading partners, and customers, as well as for governments of countries around the world where Enron does business.

Summary

Enron has a plan to deal with the Year 2000 challenge and believes that it will be able to achieve substantial Year 2000 readiness with respect to the mission critical systems that it controls. However, from a forward-looking perspective, the extent and magnitude of the Year 2000 problem as it will affect Enron, both before and for some period after January 1, 2000, are difficult to predict or quantify for a number of reasons. Among these are: the difficulty of locating "embedded" chips that may be in a great variety of mission-critical hardware used for process or flow control, environmental, transportation, access, communications and other systems; the difficulty of inventorying, assessing, remediating, verifying and testing Outside Systems; the difficulty in locating all mission-critical software (computer code) internal to Enron that is not Year 2000 compatible; and the unavailability of certain necessary internal or external resources, including but not limited to trained hardware and software engineers, technicians, and other personnel to perform adequate remediation, verification and testing of mission-critical Enron systems or Outside Systems. Accordingly, there can be no assurance that all of Enron's systems and all Outside Systems will be adequately remediated so that they are Year 2000 ready by January 1, 2000, or by some earlier date, so as not to create a material disruption to Enron's business. If, despite Enron's reasonable efforts under its Year 2000 Plan, there are mission-critical Year 2000-related failures that create substantial disruptions to Enron's business, the adverse impact on Enron's business could be material. Additionally, while Enron's Year 2000 costs are not expected to be material, such costs are difficult to estimate accurately because of unanticipated vendor delays, technical difficulties, the impact of tests of Outside Systems and similar events. Moreover, the estimated costs of implementing the Plan do not take into account the costs, if any, that might be incurred as a result of Year 2000-related failures that occur despite Enron's implementation of the Plan.

NEW ACCOUNTING PRONOUNCEMENTS C

On April 3, 1998, the AICPA issued Statement of Position 98-5 (SOP 98-5), "Reporting on the Costs of Start-Up Activities," which requires that costs for all start-up activities and organization costs be expensed as incurred and not capitalized in certain instances, as had previously been allowed. SOP 98-5 is effective for financial statements for fiscal years beginning after 1998 and initial adoption is required to be reflected as a cumulative effect of accounting change. Although Enron continues to evaluate the impact of adopting SOP 98-5, it expects to recognize an after-tax charge of approximately \$130 million in the first quarter of 1999 related primarily to differences in timing of commencement of capitalization of project development costs compared to Enron's current policy. This charge will be reflected net of tax as a separate line item in Enron's Consolidated Income Statement.

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded on the balance sheet as either an asset or liability measured at its fair value. The statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the income statement, and requires that a company must formally document, designate and assess the effectiveness of transactions that receive hedge accounting.

SFAS No. 133 is effective for fiscal years beginning after June 15, 1999. A company may also implement the Statement as of the beginning of any fiscal quarter after issuance, however, SFAS No. 133 cannot be applied retroactively.

Enron has not yet determined the timing of adoption of SFAS No. 133. Enron believes that SFAS No. 133 will not have a material impact on its accounting for price risk management activities but has not yet quantified the effect on its hedging activities or physical base contracts.

In December 1998, the Emerging Issues Task Force reached consensus on Issue No. 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities" (EITF 98-10). EITF 98-10 is effective for fiscal years beginning after December 15, 1998 and requires energy trading contracts to be recorded at fair value on the balance sheet, with the changes in fair value included in earnings. The effect of initial application of EITF 98-10 will be reported as a cumulative effect of a change in accounting principle. Because Enron currently records its trading activities at fair value, management believes that the adoption of EITF 98-10 will not have a materially adverse impact on its financial position or results of operations.

FINANCIAL CONDITION

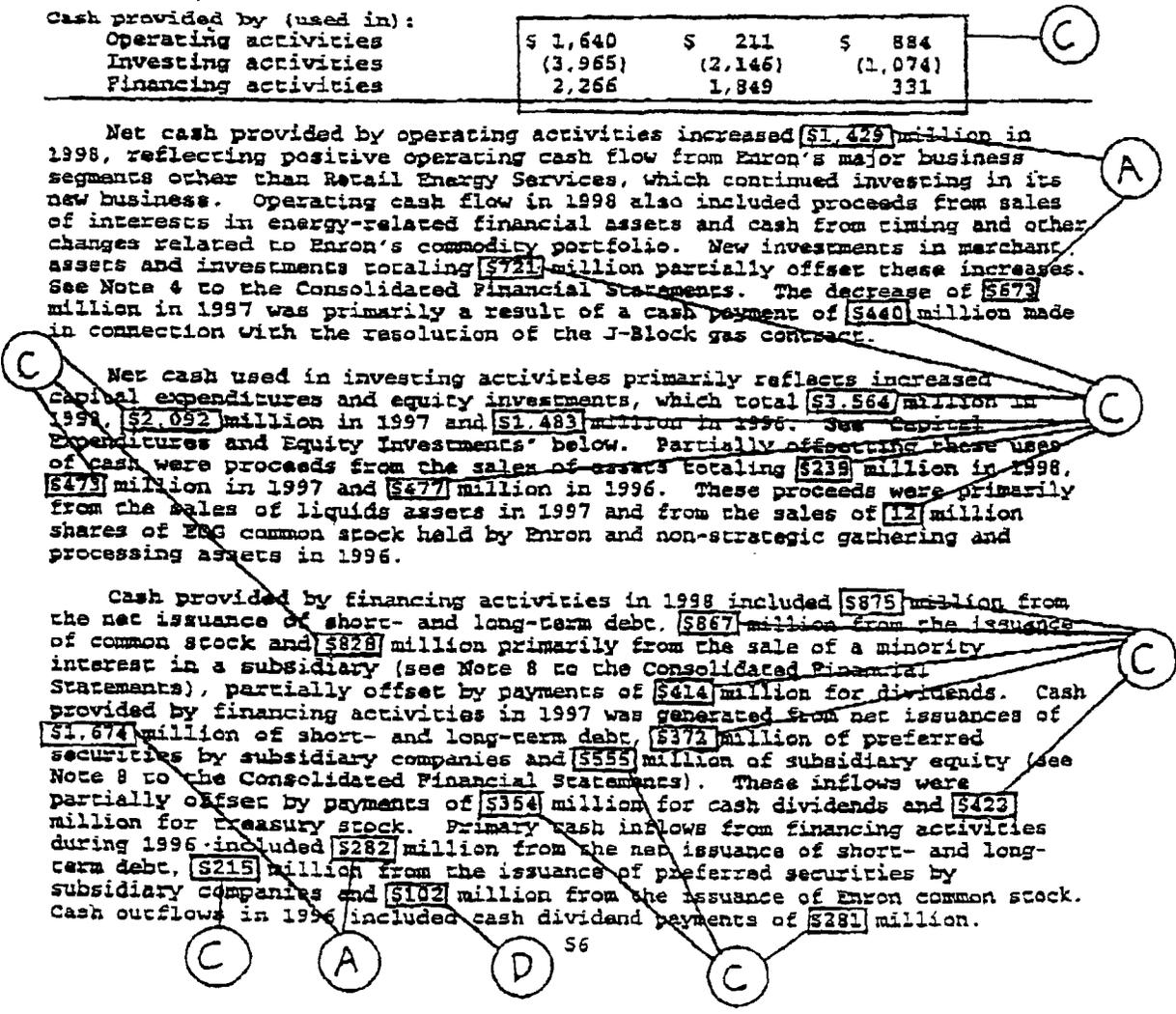
Cash Flows

(In Millions)	1998	1997	1996
Cash provided by (used in):			
Operating activities	\$ 1,640	\$ 211	\$ 884
Investing activities	(3,965)	(2,146)	(1,074)
Financing activities	2,266	1,849	331

Net cash provided by operating activities increased \$1,429 million in 1998, reflecting positive operating cash flow from Enron's major business segments other than Retail Energy Services, which continued investing in its new business. Operating cash flow in 1998 also included proceeds from sales of interests in energy-related financial assets and cash from timing and other changes related to Enron's commodity portfolio. New investments in merchant assets and investments totaling \$721 million partially offset these increases. See Note 4 to the Consolidated Financial Statements. The decrease of \$573 million in 1997 was primarily a result of a cash payment of \$440 million made in connection with the resolution of the J-Block gas contract.

Net cash used in investing activities primarily reflects increased capital expenditures and equity investments, which total \$3,564 million in 1998, \$2,092 million in 1997 and \$1,483 million in 1996. See "Capital Expenditures and Equity Investments" below. Partially offsetting these uses of cash were proceeds from the sales of assets totaling \$238 million in 1998, \$473 million in 1997 and \$477 million in 1996. These proceeds were primarily from the sales of liquids assets in 1997 and from the sales of 12 million shares of EGS common stock held by Enron and non-strategic gathering and processing assets in 1996.

Cash provided by financing activities in 1998 included \$875 million from the net issuance of short- and long-term debt, \$867 million from the issuance of common stock and \$828 million primarily from the sale of a minority interest in a subsidiary (see Note 8 to the Consolidated Financial Statements), partially offset by payments of \$414 million for dividends. Cash provided by financing activities in 1997 was generated from net issuances of \$1,674 million of short- and long-term debt, \$372 million of preferred securities by subsidiary companies and \$555 million of subsidiary equity (see Note 8 to the Consolidated Financial Statements). These inflows were partially offset by payments of \$354 million for cash dividends and \$423 million for treasury stock. Primary cash inflows from financing activities during 1996 included \$282 million from the net issuance of short- and long-term debt, \$215 million from the issuance of preferred securities by subsidiary companies and \$102 million from the issuance of Enron common stock. Cash outflows in 1996 included cash dividend payments of \$281 million.



Working Capital

At December 31, 1998, Enron had a working capital deficit of \$174 million. Enron has credit facilities in place to fund working capital requirements. At December 31, 1998, those credit lines provided for up to \$3.4 billion of committed and uncommitted credit, of which \$149 million was outstanding at December 31, 1998. Certain of the credit agreements contain prefunding covenants. However, such covenants are not expected to restrict Enron's access to funds under these agreements. In addition, Enron sells commercial paper and has agreements to sell trade accounts receivable, thus providing financing to meet seasonal working capital needs. Management believes that the sources of funding described above are sufficient to meet short- and long-term liquidity needs not met by cash flows from operations.

Capital Expenditures and Equity Investments

Capital expenditures by operating segment are as follows:

(In Millions)	1999			
	Estimate	1998	1997	1996
Exploration and Production(a)	\$ 550	\$ 690	\$ 626	\$540
Transportation and Distribution	310	310	337	175
Wholesale Energy Operations and Services	410	706	318	136
Retail Energy Services	40	75	36	-
Corporate and Other	300	124	75	13
Total	\$1,610	\$1,905	\$1,392	\$864

(a) Excludes exploration expenses of \$70 million (estimate), \$89 million, \$75 million and \$68 million for 1999, 1998, 1997 and 1996, respectively.

Capital expenditures increased \$513 million in 1998 and \$528 million during 1997 as compared to the previous year. During 1998, increased expenditures in Exploration and Production were primarily a result of the acquisition of producing properties in the Gulf of Mexico, and Enron Wholesale expenditures increased primarily related to domestic and international power plant construction. During 1997, increased expenditures in Exploration and Production reflect increased development expenditures in the United States and increased property acquisitions in Canada. Transportation and Distribution expenditures increased due to expansion projects by the interstate natural gas pipelines. Included in Enron Wholesale were send-or-pay payments totaling \$63 million in 1998 and \$167 million in 1997 related to a transportation agreement in the U.K.

Cash used for equity investments by the operating segments is as follows:

(In Millions)	1999			
	Estimate	1998	1997	1996
Exploration and Production	\$ 80	\$ -	\$ -	\$ -
Transportation and Distribution	120	27	3	-
Wholesale Energy Operations and Services	600	703	580	511
Retail Energy Services	210	-	-	-
Corporate and Other	120	92	117	108
Total	\$1,130	\$1,659	\$700	\$619

Equity investments increased in 1998 as compared to 1997 primarily due to the acquisitions of Elektro and Wessex, net of proceeds from transactions reducing Enron's interest in these investments. See Note 9 to the Consolidated Financial Statements.

The level of spending for capital expenditures and equity investments will vary depending upon conditions in the energy markets, related economic conditions and identified opportunities. Management expects that the capital

spending program will be funded by a combination of internally generated funds, proceeds from dispositions of selected assets, short- and long-term borrowings and proceeds from the sale of common stock in February 1999.

CAPITALIZATION

Total capitalization at December 31, 1998 was \$17.5 billion. Debt as a percentage of total capitalization decreased to 41.9% at December 31, 1998 as compared to 44.6% at December 31, 1997. The decrease primarily reflects the issuance during 1998 of approximately 17 million shares of common stock and the conversion in late 1998 of 10.5 million Exchangeable Notes into EOG shares held by Enron, partially offset by increased debt and minority interest.

Enron is a party to certain financial contracts which contain provisions for early settlement in the event of a significant market price decline in which Enron's common stock falls below certain levels (prices ranging from \$15 to \$37.84 per share) or if the credit ratings for Enron's unsecured, senior long-term debt obligations fall below investment grade. The impact of this early settlement could include the issuance of additional shares of Enron common stock.

Enron's senior unsecured long-term debt is currently rated BBB+ by Standard & Poor's Corporation and Baa2 by Moody's Investor Services. Enron's continued investment grade status is critical to the success of its wholesale businesses as well as its ability to maintain adequate liquidity. Enron's management believes it will be able to maintain or improve its credit rating.

In February 1999, Enron issued 13.8 million shares of common stock in a public offering and approximately 3.8 million shares of common stock in connection with the acquisition of certain assets.

Enron has investments in entities whose functional currency is denominated in Brazilian Reals. Subsequent to December 31, 1998 the exchange rate for Brazilian Reals to the U.S. dollar has declined. As a result, Enron anticipates recording a non-cash foreign currency translation adjustment, reducing shareholders' equity, in the first quarter of 1999. Based on the exchange rate in mid-February, the equity reduction would be approximately \$600 million.

Item 7A. FINANCIAL RISK MANAGEMENT

Enron Wholesale offers price risk management services primarily related to commodities associated with the energy sector (natural gas, crude oil, natural gas liquids and electricity). These services are provided through a variety of financial instruments including forward contracts, which may involve physical delivery of an energy commodity, swap agreements, which may require payments to (or receipt of payments from) counterparties based on the differential between a fixed and variable price for the commodity, options and other contractual arrangements. Interest rate risks and foreign currency risks associated with the fair value of its energy commodities portfolio are managed in this segment using a variety of financial instruments, including financial futures, swaps and options.

In order to mitigate the risk associated with its merchant investments, Enron actively manages the systematic or market risks inherent in the investments. Using various analytical methods, Enron generally disaggregates and manages the equity index, interest rate and commodity risks embedded in the investments, leaving the specific asset or idiosyncratic risk which is diversified among the investments.

Enron's other businesses also enter into forwards, swaps and other contracts primarily for the purpose of hedging the impact of market fluctuations on assets, liabilities, production or other contractual

Total rent expense incurred during 1998, 1997 and 1996 was \$147 million, \$156 million and \$149 million, respectively.

Enron guarantees certain long-term contracts for the sale of electrical power and steam from a cogeneration facility owned by one of Enron's equity investees. Under terms of the contracts, which initially extend through June 1999, Enron could be liable for penalties should, under certain conditions, the contracts be terminated early. Enron also guarantees the performance of certain of its unconsolidated affiliates in connection with letters of credit issued on behalf of those unconsolidated affiliates. At December 31, 1998, a total of \$209 million of such guarantees were outstanding, including \$44 million on behalf of EOTT. In addition, Enron is a guarantor on certain liabilities of unconsolidated affiliates and other companies totaling approximately \$755 million, including \$356 million related to EOTT trade obligations. The EOTT letters of credit and guarantees of trade obligations are secured by the assets of EOTT. Enron has also guaranteed \$453 million in lease obligations for which it has been indemnified by an "Investment Grade" company. Management does not consider it likely that Enron would be required to perform or otherwise incur any losses associated with the above guarantees. In addition, certain commitments have been made related to 1999 planned capital expenditures and equity investments.

16 QUARTERLY FINANCIAL DATA (Unaudited)

Summarized quarterly financial data is as follows:

(In Millions, Except Per Share Amounts)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total Year
1998					
Revenues	\$5,682	\$6,557	\$11,320	\$7,701	\$31,260
Income before interest, minority interests and income taxes	471	345	405	361	1,582
Net income	214	145	168	176	703
Earnings per share:					
Basic	\$ 0.69	\$ 0.44	\$ 0.50	\$ 0.52	\$ 2.14(a)
Diluted	0.65	0.42	0.47	0.49	2.02(a)
1997					
Revenues	\$5,344	\$3,251	\$ 5,806	\$5,872	\$20,273
Income (loss) before interest, minority interests and income taxes	429	(548)	311	373	565
Net income (loss)	222	(420)	134	169	105
Earnings (loss) per share:					
Basic	\$ 0.88	\$(1.71)	\$ 0.44	\$ 0.55	\$ 0.32(a)
Diluted	0.81	(1.71)	0.42	0.53	0.32(a)

(a) The sum of earnings per share for the four quarters may not equal earnings per share for the total year due to changes in the average number of common shares outstanding. Additionally, certain items in the diluted earnings per share computation were antidilutive in the second quarter and total year 1997.

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REVENUES BY BUSINESS SEGMENT

The following table presents revenues for each business segment (in millions):

	Year Ended December 31,		
	1998	1997	1996
Exploration and Production			
Natural Gas and Other Products			
Unaffiliated	\$ 728	\$ 774	\$ 620
Intersegment	114	169	197
	842	943	817
Other Revenues			
Unaffiliated	22	15	27
Intersegment	20	(61)	(20)
	42	(46)	7
TOTAL	884	897	824
Transportation and Distribution			
Natural Gas and Other Products			
Unaffiliated	16	10	11
Intersegment	-	-	8
	16	10	19
Electricity			
Unaffiliated	1,137	712	-
Intersegment	-	-	-
	1,137	712	-
Transportation			
Unaffiliated	617	639	682
Intersegment	11	10	15
	628	649	697
Other Revenues			
Unaffiliated	63	41	9
Intersegment	5	4	-
	68	45	9
TOTAL	1,849	1,416	725

Year Ended December 31,
1998 1997 1996

Wholesale Energy Operations and Services

Natural Gas and Other Products

Unaffiliated	\$11,916	\$11,778	\$10,013
Intersegment	399	595	477
	12,315	12,373	10,490

Electricity

Unaffiliated	12,714	4,376	980
Intersegment	-	-	-
	12,714	4,376	980

Transportation

Unaffiliated	11	13	25
Intersegment	1	2	2
	12	15	27

Other Revenues

Unaffiliated	2,579	1,177	395
Intersegment	105	81	12
	2,684	1,258	407

TOTAL

	27,725	18,022	11,904
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Retail Energy Services

Natural Gas and Other Products

Unaffiliated	616	649	513
Intersegment	-	2	15
	616	651	528

Electricity

Unaffiliated	84	1	-
Intersegment	-	-	-
	84	1	-

Other Revenues

Unaffiliated	372	33	-
Intersegment	-	-	-
	372	33	-

TOTAL

	1,072	685	528
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Corporate and Other

Natural Gas and Other Products

Unaffiliated	-	-	-
Intersegment	159	-	-
	159	-	-

Electricity

Unaffiliated	3	12	-
Intersegment	-	-	-
	3	12	-

Other Revenues

Unaffiliated	382	43	14
Intersegment	(28)	-	-
	354	43	14

TOTAL

	516	55	14
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Intersegment Eliminations

	(786)	(802)	(706)
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Total Revenues

	\$31,260	\$20,273	\$13,289
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Drilling and Acquisition Activities

During each of the years ended December 31, 1998, 1997 and 1996, EOG spent approximately \$769 million, \$693 million and \$599 million, respectively, for exploratory and development drilling and acquisition of leases and producing properties. EOG drilled, participated in the drilling of or acquired wells as set out in the table below for the periods indicated:

	Year Ended December 31,					
	1998		1997		1996	
	Gross	Net	Gross	Net	Gross	Net
Development Wells Completed						
North America						
Gas	478	402.80	467	352.90	396	325.04
Oil	38	34.98	94	74.85	80	57.46
Dry	79	62.16	101	80.01	80	68.77
Total	<u>595</u>	<u>499.94</u>	<u>662</u>	<u>507.76</u>	<u>556</u>	<u>451.27</u>
Outside North America						
Gas	-	-	12	3.60	-	-
Oil	21	6.30	6	1.80	1	0.30
Dry	-	-	-	-	-	-
Total	<u>21</u>	<u>6.30</u>	<u>18</u>	<u>5.40</u>	<u>1</u>	<u>0.30</u>
Total Development	<u>616</u>	<u>506.24</u>	<u>680</u>	<u>513.16</u>	<u>557</u>	<u>451.57</u>
Exploratory Wells Completed						
North America						
Gas	5	4.40	8	5.12	14	10.36
Oil	6	5.50	-	-	1	0.78
Dry	22	15.70	12	7.53	26	19.00
Total	<u>33</u>	<u>25.60</u>	<u>20</u>	<u>12.65</u>	<u>41</u>	<u>30.14</u>
Outside North America						
Gas	1	1.00	-	-	-	-
Oil	1	0.90	-	-	-	-
Dry	-	-	-	-	1	0.50
Total	<u>2</u>	<u>1.90</u>	<u>-</u>	<u>-</u>	<u>1</u>	<u>0.50</u>
Total Exploratory	<u>35</u>	<u>27.50</u>	<u>20</u>	<u>12.65</u>	<u>42</u>	<u>30.64</u>
Total	<u>651</u>	<u>533.74</u>	<u>700</u>	<u>525.81</u>	<u>599</u>	<u>482.21</u>
Wells in Progress at End of Period						
Gas	28	15.73	44	36.39	87	61.08
Total	<u>28</u>	<u>15.73</u>	<u>44</u>	<u>36.39</u>	<u>87</u>	<u>61.08</u>
Wells Acquired						
Gas	333	317.23*	227	82.45*	350	148.20*
Oil	-	1.70*	48	20.50*	5	0.65
Total	<u>333</u>	<u>318.93</u>	<u>275</u>	<u>102.95</u>	<u>355</u>	<u>148.85</u>

* Includes acquisition of additional interests in certain wells in which EOG previously held an interest.

All of EOG's drilling activities are conducted on a contract basis with independent drilling contractors. EOG owns no drilling equipment.

Trojan Investment Recovery. In early 1993, PGE ceased commercial operation of Trojan. In April 1996 a circuit court judge in Marion County, Oregon found that the OPUC could not authorize PGE to collect a return on its undepreciated investment in Trojan, contradicting a November 1994 ruling from the same court. The ruling was the result of an appeal of PGE's 1995 general rate order which granted PGE recovery of, and a return on, 87% of its remaining investment in Trojan. The 1994 ruling was appealed to the Oregon Court of Appeals and stayed pending the appeal of the OPUC's March 1995 order. Both PGE and the OPUC have separately appealed the April 1996 ruling, which appeals were combined with the appeal of the November 1994 ruling at the Oregon Court of Appeals. On June 24, 1998, the Court of Appeals of the State of Oregon ruled that the OPUC does not have the authority to allow PGE to recover a rate of return on its undepreciated investment in the Trojan generating facility. The court upheld the OPUC's authorization of PGE's recovery of its undepreciated investment in Trojan.

PGE has filed a petition for review with the Oregon Supreme Court. The OPUC has also filed such a petition for review. In addition, on August 26, 1998, the Utility Reform Project filed a Petition for Review with the Oregon Supreme Court seeking review of that portion of the Oregon Court of Appeals decision relating to PGE's recovery of its undepreciated investment in Trojan. Enron cannot predict the outcome of these actions. Additionally, due to uncertainties in the regulatory process, management cannot predict, with certainty, what ultimate rate-making action the OPUC will take regarding PGE's recovery of a rate of return on its Trojan investment. Although no assurances can be given, Enron believes that the ultimate resolution of these matters will not have a material adverse effect on its financial position or results of operations.

Environmental Matters. Enron is subject to extensive federal, state and local environmental laws and regulations. These laws and regulations require expenditures in connection with the construction of new facilities, the operation of existing facilities and for remediation at various operating sites. The implementation of the Clean Air Act Amendments is expected to result in increased operating expenses. These increased operating expenses are not expected to have a materially adverse effect on Enron's financial position or results of operations.

The EPA has informed Enron that it is a potentially responsible party at the Decorah Former Manufactured Gas Plant Site (the Decorah Site) in Decorah, Iowa, pursuant to the provisions of CERCLA. The manufactured gas plant in Decorah ceased operations in 1951. A predecessor company of Enron purchased the Decorah Site in 1963. Enron's predecessor did not operate the gas plant and sold the Decorah Site in 1965. The EPA alleges that hazardous substances were released to the environment during the period in which Enron's predecessor owned the site, and that Enron's predecessor assumed the liabilities of the company that operated the plant. Enron contests these allegations. To date, the EPA has identified no other potentially responsible parties with respect to this site. Enron has entered into a consent order with the EPA by which it has agreed, although admitting no liability, to replace affected topsoil and remove impacted subsurface soils in certain areas of the tract where the plant was formerly located. Enron completed the final removal actions at the site in November 1998, and expects to conclude all remaining site activities in the spring of 1999. In 1998, Enron's expenses related to the Decorah Site were \$300,000 as compared with \$400,000 in 1997. Enron believes that expenses incurred in connection with this matter will not have a materially adverse effect on its financial position or results of operations.

By order dated June 27, 1995, the Florida Department of Environmental Protection approved a remedial action plan for the Enron Gas Processing Company Brooker Plant in Bradford County, Florida. Soil and groundwater at the plant site had been impacted by historical releases of hydrocarbons from the now inactive liquids extraction plant. Site remedial work commenced in 1996 and is expected to continue for several years at a total cost of approximately \$5 million.

Enron has also received from the EPA an Order issued under CERCLA alleging that Enron and two other parties are responsible for the cost of demolition and proper disposal of two 110-foot towers that apparently had been used in the manufacture of carbon dioxide at a site called the "City Bumper Site" in Cincinnati, Ohio. The carbon dioxide plant, according to agency documents, was in operation from 1926 to 1966. Houston Natural Gas Corporation, a predecessor of Enron Corp., merged with Liquid Carbonic Industries (LCI) on January 31, 1969. Liquid Carbonic Corporation (LCC), a subsidiary of LCI, had title to the site. Twenty-eight days after the merger, on

February 28, 1969, the site was sold to a third party. In 1984, LCC was sold to an unaffiliated party in a stock sale. Although Enron does not admit liability with respect to any costs at this site, it agreed to cooperate with the EPA and other potentially responsible parties to undertake the work contemplated by EPA's Order. The tower demolition and removal activities were completed in October 1998, and a final project report has been prepared for submission to the EPA. In 1998, Enron's expenses related to the City Bumper Site were \$600,000. Enron does not expect to incur material expenditures in connection with this site.

Enron's natural gas pipeline companies conduct soil and groundwater remediation of a number of their facilities. In 1998, these expenses were \$1.3 million as compared with \$1.7 million in 1997. Enron does not expect to incur material expenditures in connection with soil and groundwater remediation.

In addition, Enron has received requests for information from the EPA and state environmental agencies inquiring whether Enron has disposed of materials at other waste disposal sites. Enron has also received requests for contribution from other parties with respect to the cleanup of other sites. Enron may be required to share in the costs of the cleanup of some of these sites. However, based upon the amounts claimed and the nature and volume of materials sent to sites at which Enron has an interest, management does not believe that any potential costs incurred in connection with these notices and third party claims, either taken individually or in the aggregate, will have a material impact on Enron's financial position or results of operations.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

PART II

Item 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED SHAREHOLDER MATTERS

Common Stock

The following table indicates the high and low sales prices for the common stock of Enron as reported on the New York Stock Exchange (consolidated transactions reporting system), the principal market in which the securities are traded, and dividends paid per share for the calendar quarters indicated. The common stock is also listed for trading on the Chicago Stock Exchange and the Pacific Stock Exchange, as well as The London Stock Exchange and Frankfurt Stock Exchange.

	1998			1997		
	High	Low	Dividends	High	Low	Dividends
First Quarter.....	\$48	\$38 1/8	\$.2375	\$45 1/8	\$37 7/8	\$.2250
Second Quarter.....	54 5/16	45 9/16	.2375	42 3/8	35 5/8	.2250
Third Quarter.....	58 7/16	40 5/8	.2375	42	35	.2250
Fourth Quarter.....	58 3/4	49 1/2	.2500	41 15/16	35 15/16	.2375

Cumulative Second Preferred Convertible Stock

The following table indicates the high and low sales prices for the Cumulative Second Preferred Convertible Stock ("Second Preferred Stock") of Enron as reported on the New York Stock Exchange (consolidated transactions reporting system), the principal market in which the securities are traded, and dividends paid per share for the calendar quarters indicated. The Second Preferred Stock is also listed for trading on the Chicago Stock Exchange.

	1998			1997		
	High	Low	Dividends	High	Low	Dividends
First Quarter.....	\$634	\$565	\$3.2424	\$600	\$600	\$3.0717
Second Quarter.....	684 13/16	622 3/4	3.2424	555	496	3.0717
Third Quarter.....	--	--	3.2424	540	535	3.0717
Fourth Quarter.....	732 1/2	718	3.4130	523	523	3.2424

At December 31, 1998, there were approximately 58,598 record holders of common stock and 209 record holders of Second Preferred Stock.

Other information required by this item is set forth under Item 6 -- "Selected Financial Data (Unaudited) - Common Stock Statistics" for the years 1994-1998.

Recent Sales of Unregistered Equity Securities

On December 17, 1998, Enron issued in a private placement pursuant to Section 4(2) of the Securities Act 204,800 shares of its Mandatorily Convertible Reset Preferred Stock, Series A, to Preferred Voting Trust, a Delaware statutory business trust, in exchange for all of the beneficial interests in such trust. On December 30, 1998, Enron issued in a private placement pursuant to Section 4(2) of the Securities Act 83,000 shares of its Mandatorily Convertible Reset Preferred Stock, Series B, to Agula Voting Trust, a Delaware statutory business trust, in exchange for all of the beneficial interests in such trust.

Item 6. SELECTED FINANCIAL DATA (UNAUDITED)

	1998	1997	1996	1995	1994
Operating Revenues (millions)	\$31,260	\$20,273	\$13,289	\$ 9,189	\$ 8,984
Total Assets (millions)	\$29,350	\$22,552	\$16,137	\$13,239	\$11,966
Common Stock Statistics					
Income from continuing operations					
Total (millions)	\$703	\$105	\$584	\$520	\$453
Per share - basic	\$2.14	\$0.32	\$2.31	\$2.07	\$1.80
Per share - diluted	\$2.02	\$0.32	\$2.16	\$1.94	\$1.70
Earnings on common stock					
Total (millions)	\$686	\$ 88	\$568	\$504	\$438
Per share - basic	\$2.14	\$0.32	\$2.31	\$2.07	\$1.80
Per share - diluted	\$2.02	\$0.32	\$2.16	\$1.94	\$1.70
Dividends					
Total (millions)	\$312	\$243	\$212	\$205	\$192
Per share	\$0.96	\$0.91	\$0.86	\$0.81	\$0.76
Shares outstanding (millions)					
Actual at year-end	331	307	251	245	244
Average for the year	321	272	246	244	243
Capitalization (millions)					
Long-term debt	\$ 7,357	\$ 6,254	\$3,349	\$3,065	\$2,805
Preferred stock of subsidiary	1,001	993	592	377	377
Minority interest	2,143	1,147	755	549	290
Shareholders' equity	7,048	5,618	3,723	3,165	2,880
Total capitalization	\$17,549	\$14,012	\$8,419	\$7,156	\$6,352

(C)

(A)

(C)

(A)



IV



Exhibit 12

ENRON CORP. AND SUBSIDIARIES
 Computation of Ratio of Earnings to
 Fixed Charges
 (Unaudited)

(In Millions)

	Year Ended December 31,				
	1998	1997	1996	1995	1994
Earnings available for fixed charges					
Income from continuing operations	\$ 703	\$105	\$ 584	\$ 520	\$ 453
Less:					
Undistributed earnings and losses of less than 50% owned affiliates	(44)	(89)	(39)	(14)	(9)
Capitalized interest of nonregulated companies	(66)	(16)	(10)	(8)	(9)
Add:					
Fixed charges (a)	809	674	454	436	487
Minority interest	77	80	75	27	30
Income tax expense	204	(65)	297	310	190
Total	\$1,683	\$689	\$1,361	\$1,271	\$1,142
Fixed charges					
Interest expense (a)	\$ 760	\$624	\$ 404	\$ 386	\$ 445
Rental expense representative of interest factor	49	50	50	50	42
Total	\$ 809	\$674	\$ 454	\$ 436	\$ 487
Ratio of earnings to fixed charges	2.08	1.02	3.00	2.92	2.34

(a) Amounts exclude costs incurred on sales of accounts receivable.

(E)

V

PART I. FINANCIAL INFORMATION - (Continued)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS ENRON CORP. AND SUBSIDIARIES

RESULTS OF OPERATIONS

First Quarter 1999
vs. First Quarter 1998

The following review of Enron's results of operations should be read in conjunction with the Consolidated Financial Statements.

RESULTS OF OPERATIONS

Consolidated Net Income

Enron's first quarter 1999 net income, excluding the cumulative effect of accounting changes, was \$253 million compared to \$214 million in the first quarter of 1998. Enron's operating segments include Exploration and Production (Enron Oil & Gas Company), Transportation and Distribution (Gas Pipeline Group and Portland General), Wholesale Energy Operations and Services (Enron Capital & Trade Resources and Enron International), Retail Energy Services (Enron Energy Services) and Corporate and Other, which includes certain new businesses. In the first quarter of 1999, Enron recognized a charge of \$131 million (net of tax) as a cumulative effect of accounting changes.

Basic and diluted earnings per share of common stock were as follows:

	<u>First Quarter</u>	
	<u>1999</u>	<u>1998</u>
Basic earnings per share:		
Before cumulative effect of accounting changes	\$ 0.73	\$ 0.69
Cumulative effect of accounting changes	(0.38)	-
Reported basic earnings per share	<u>\$ 0.35</u>	<u>\$ 0.69</u>
Diluted earnings per share:		
Before cumulative effect of accounting changes	\$ 0.68	\$ 0.65
Cumulative effect of accounting changes	(0.35)	-
Reported diluted earnings per share	<u>\$ 0.33</u>	<u>\$ 0.65</u>

PART I. FINANCIAL INFORMATION - (Continued)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)
ENRON CORP. AND SUBSIDIARIES

Income Before Interest, Minority Interests and Income Taxes

The following table presents income before interest, minority interests and income taxes (IBIT) for each of Enron's operating segments (in millions):

	First Quarter	
	1999	1998
Exploration and Production	\$ 12	\$ 43
Transportation and Distribution:		
Gas Pipeline Group	126	126
Portland General	92	79
Wholesale Energy Operations and Services	320	249
Retail Energy Services	(31)	(27)
Corporate and Other	14	1
Income before interest, minority interests and taxes	<u>\$533</u>	<u>\$471</u>

Exploration and Production

Enron's exploration and production operations are conducted by Enron Oil & Gas Company (EOG). IBIT of Exploration and Production totaled \$12 million and \$43 million for the first quarter of 1999 and 1998, respectively.

Wellhead volume and price statistics (including intercompany amounts) are as follows:

	First Quarter	
	1999	1998
Natural gas volumes (MMcf/d) (a)		
North America	781	745
Trinidad	152	109
India	71	47
Total	<u>1,004</u>	<u>901</u>
Average natural gas prices (\$/Mcf)		
North America	1.58	1.93
Trinidad	1.06	1.09
India	1.96	2.70
Composite	1.53	1.86
Crude oil/condensate volumes (MBl/d) (a)		
North America	15.8	15.3
Trinidad	2.8	2.8
India	7.1	4.2
Total	<u>25.7</u>	<u>22.3</u>
Average crude oil/condensate prices (\$/Sbl)		
North America	11.39	14.55
Trinidad	9.63	14.03
India	9.79	15.33
Composita	10.76	14.64

(a) Million cubic feet per day or thousand barrels per day, as applicable.

PART I. FINANCIAL INFORMATION - (Continued)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)
ENRON CORP. AND SUBSIDIARIES

Portland General. Statistics for PGE for the first quarter of 1999 and 1998 are as follows:

	<u>First Quarter</u>	
	<u>1999</u>	<u>1998</u>
Electricity Sales (Thousand MWh) (a)		
Residential	2,342	2,076
Commercial	1,816	1,654
Industrial	1,020	891
Total Retail	<u>5,178</u>	<u>4,621</u>
Wholesale	<u>1,338</u>	<u>3,575</u>
Total Electricity Sales	<u>6,516</u>	<u>8,196</u>
Average Rate (Thousand MWh) (a)		
Residential	5.73	5.91
Commercial	4.91	5.07
Industrial	3.49	3.43
Total Retail	5.00	5.13
Wholesale	1.88	1.82
Total Sales	4.36	3.68
Resource Mix		
Coal	18%	15%
Combustion Turbine	4	7
Hydro	<u>13</u>	<u>9</u>
Total Generation	35	31
Firm Purchases	47	65
Secondary Purchases	<u>18</u>	<u>4</u>
Total Resources	<u>100%</u>	<u>100%</u>
Average Variable Power Cost (Mills/KWh) (b)		
Generation	8.0	7.0
Firm Purchases	16.7	16.3
Secondary Purchases	15.0	14.2
Total Average Variable Power Cost	15.0	14.4
Retail Customers (end of period, thousands)	708	688

(a) Thousand megawatt-hours.
 (b) Mills (1/10 cent) per kilowatt-hour.

Significant components of IBIT are as follows (in millions):

	<u>First Quarter</u>	
	<u>1999</u>	<u>1998</u>
Revenues	\$299	\$320
Purchased power and fuel	100	124
Operating expenses	70	76
Depreciation and amortization	46	44
Other income, net	9	3
Income before interest and taxes	<u>\$ 92</u>	<u>\$ 79</u>

Operating Results

Revenues and purchased power and fuel costs decreased \$21 million and \$24 million, respectively, in the first quarter of 1999 as compared to the first quarter of 1998, primarily as a result of the transfer of the majority of Portland General's electricity wholesale business to the Enron Wholesale segment. The impact of this transfer was partially

PART I. FINANCIAL INFORMATION - (Continued)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)
ENRON CORP. AND SUBSIDIARIES

Enron Wholesale markets and transports a substantial quantity of energy commodities as reflected in the following table (including intercompany amounts):

	First Quarter	
	1999	1998
Physical Volumes (BBcu/d) (a) (b)		
Gas:		
United States	9,088	7,276
Canada	3,954	2,876
Europe	1,792	1,125
Other	7	1
	<u>14,841</u>	<u>11,278</u>
Transport Volumes	556	450
Total Gas Volumes	<u>15,397</u>	<u>11,728</u>
Oil	3,704	1,756
Liquids	580	654
Electricity(c)	<u>9,594</u>	<u>8,262</u>
Total	<u>29,275</u>	<u>22,400</u>
Electricity Volumes Marketed (Thousand MWh)		
United States	85,962	74,272
Europe	297	82
Other	87	-
Total	<u>86,346</u>	<u>74,354</u>
Financial Settlements (Notional) (BBcu/d)	<u>94,974</u>	<u>69,918</u>

(a) Billion British thermal units equivalent per day.

(b) Includes third-party transactions by Enron Energy Services.

(c) Represents electricity transaction volumes marketed, converted to BBcu/d utilizing the input method.

The earnings from commodity sales and services increased 74% in the first quarter of 1999 as compared to the same period of 1998 primarily due to increased profits from power and gas marketing resulting from a more than 30% increase in volumes as well as favorable changes in energy and credit markets worldwide, partially offset by higher expenses.

Energy Assets and Investments. Enron Wholesale's energy assets and investments activities include investments in debt and equity securities of oil and gas producers and other energy-intensive companies. Additionally, Enron Wholesale develops, constructs, operates and manages a large portfolio of energy investments such as power plants and natural gas pipelines. Earnings primarily result from changes in the market value of merchant investments held during the period, equity earnings and gains on sales or restructurings of energy investments.

Earnings from energy assets and investments decreased 10% in the first quarter of 1999 as compared to the same period in 1998 primarily as a result of decreased earnings from the management of Enron Wholesale's merchant investments, partially offset by higher earnings from international energy asset operations and increased construction profits.

Unallocated Expenses. Net unallocated expenses such as rent, systems expenses and other support group costs increased in 1999 due to continued expansion into new markets and system upgrades.

PART I. FINANCIAL INFORMATION - (Continued)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued) ENRON CORP. AND SUBSIDIARIES

Retail Energy Services

Enron Energy Services (Energy Services) is extending Enron's energy expertise to end-use customers. This includes sales of natural gas, electricity and energy management services directly to commercial and industrial customers. In the first quarter of 1999, Energy Services continued to make significant progress in expanding its customer base and contracting activities by executing several significant commodity and services contracts with new customers. Energy Services reported an operating loss before interest, minority interest and taxes of \$31 million in the first quarter of 1999 compared to a loss of \$27 million in the first quarter of 1998. These results primarily reflect the costs associated with developing the commodity, capital and services capability to deliver on contracts signed to date by Energy Services.

Corporate and Other

Corporate and Other includes results of Azurix Corp. which provides water and wastewater services, Enron Communications, Inc. (ECI), which delivers high content media to business customers, Enron Renewable Energy Corp. (EREC), EOTF Energy Corp. (EOTF) and the operations of Enron's merchant and MTBE plants. Corporate and Other realized IBIT of \$14 million in the first quarter of 1999 compared to \$1 million for the same period in 1998. The increase is primarily the result of increased earnings from EREC related to the sale of certain facilities.

Interest and Related Charges, net

Interest and related charges, net, is reported net of interest capitalized of \$13 million and \$6 million for the first three months of 1999 and 1998, respectively. The net expense increased \$42 million in the first quarter of 1999 as compared to the same period of 1998, primarily due to an increase of approximately \$2.1 billion in debt, including approximately \$900 million due to the consolidation of Jacare, the entity that holds Enron's investment in Elektro (see Note 3 to the Consolidated Financial Statements).

Minority Interests

Minority interests increased \$8 million to \$33 million in the first quarter of 1999 compared to the same period in 1998, primarily due to the minority owner's share of the results of Jacare prior to the purchase of additional shares of Elektro (see Note 3 to the Consolidated Financial Statements), and the limited partner's share of earnings related to a partnership created in December 1998, partially offset by decreased net income from EOG in the first quarter of 1999.

Income Tax Expense

The projected effective tax rate for 1999 is lower than the statutory rate mainly due to equity earnings and differences between the book and tax basis of certain assets and stock sales. In addition, income taxes decreased during the first quarter of 1999 as compared to the first quarter of 1998 primarily as a result of a settlement of an IRS audit issue.

Cumulative Effect of Accounting Changes

In the first quarter of 1999, Enron recorded an after-tax charge of \$131 million to reflect the initial adoption (as of January 1, 1999) of SOP 98-5 and EITF 98-10. See Note 2 to the Consolidated Financial Statements.

PART I. FINANCIAL INFORMATION - (Continued)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued) ENRON CORP. AND SUBSIDIARIES

Systems. Accordingly, there can be no assurance that all of Enron's systems and all Outside Systems will be adequately remediated so that they are Year 2000 ready by January 1, 2000, or by some earlier date, so as not to create a material disruption to Enron's business. If, despite Enron's reasonable efforts under its Year 2000 Plan, there are mission-critical Year 2000-related failures that create substantial disruptions to Enron's business, the adverse impact on Enron's business could be material. Additionally, while Enron's Year 2000 costs are not expected to be material, such costs are difficult to estimate accurately because of unanticipated vendor delays, technical difficulties, the impact of costs of Outside Systems and similar events. Moreover, the estimated costs of implementing the Plan do not take into account the costs, if any, that might be incurred as a result of Year 2000-related failures that occur despite Enron's implementation of the Plan.

NEW ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded on the balance sheet as either an asset or liability measured at its fair value. The Statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the income statement, and requires that a company must formally document, designate and assess the effectiveness of transactions that receive hedge accounting treatment.

SFAS No. 133 is effective for fiscal years beginning after June 15, 1999. A company may also implement the Statement as of the beginning of any fiscal quarter after issuance, however, SFAS No. 133 cannot be applied retroactively. Enron has not yet determined the timing of adoption of SFAS No. 133. Enron believes that SFAS No. 133 will not have a material impact on its accounting for price risk management activities but has not yet quantified the effect on its hedging activities or physical base contracts.

FINANCIAL CONDITION

Cash Flows

(In Millions)

Cash provided by (used in):
Operating activities
Investing activities
Financing activities

Table with 2 columns: 1999, 1998. Rows: Operating activities (\$ (660) vs \$ 50), Investing activities ((1,130) vs (492)), Financing activities (1,975 vs 445).

Cash used in operating activities totaled \$660 million during the first three months of 1999 as compared to cash provided of \$50 million in the same period last year. The change in cash from operating activities in the first quarter of 1999 reflects an increase in net

VI

Exhibit 12

ENRON CORP. AND SUBSIDIARIES
COMPUTATION OF RATIO OF EARNINGS TO
FIXED CHARGES
(Dollars in Millions)
(Unaudited)

E

	Three Months		Year Ended December 31,			
	Ended 3/31/99	1998	1997	1996	1995	1994
Earnings available for fixed charges						
Net income	\$253	\$ 703	\$105	\$ 584	\$ 520	\$ 453
Less:						
Undistributed earnings and losses of less than 50% owned affiliates	-	(44)	(89)	(39)	(14)	(9)
Capitalized interest of nonregulated companies	(14)	(66)	(16)	(10)	(8)	(9)
Add:						
Fixed charges (1)	245	809	674	454	436	487
Minority interest	32	77	80	75	27	30
Income tax expense	62	204	(65)	297	310	190
Total	\$578	\$1,683	\$689	\$1,361	\$1,271	\$1,142
Fixed Charges						
Interest expense (1)	\$229	\$ 760	\$624	\$ 404	\$ 386	\$ 445
Rental expense representative of interest factor	16	49	50	50	50	42
Total	\$245	\$ 809	\$674	\$ 454	\$ 436	\$ 487
Ratio of earnings to fixed charges	2.36	2.08	1.02	3.00	2.92	2.34

(1) Amounts exclude costs incurred on sales of accounts receivables.

VII

CAPITALIZATION

The following table sets forth our consolidated capitalization as of March 31, 1999 and as adjusted to give effect to the issuance on April 7, 1999 of 400,000,000 ELJE (approximately \$430,000,000) aggregate principal amount of Notes due 2005 and the issuance of the notes offered hereby, and the use of the proceeds therefrom. See "Use of Proceeds."

	Actual	As Adjusted
	(In millions)	
Short-term debt		
Notes payable	\$ —	\$ —
Current maturities of long-term debt	—	—
Total short-term debt	—	—
Long-term debt		
Enron:		
Amount reclassified from short-term debt(a)	1,862	943
Notes due 2001-2028 (6.40% to 9.88%)	3,343	3,343
Notes due 1999-2000 (floating)	400	400
Other	18	18
Notes due 2005 (4.38%)	—	430
Notes due 2019 (7.38%)	—	500
Subsidiary companies:		
Notes due 1999-2035 (4.60% to 12.00%)	2,685	2,685
Notes due 1999-2031 (floating)	752	752
Other	50	50
Enron:		
Senior subordinated debentures due 2005-2012	350	350
Unamortized debt discount and premium	(41)	(46)
Total long-term debt	9,419	9,425
Minority interests	2,125	2,125
Company-obligated preferred securities of subsidiaries	1,001	1,001
Shareholders' equity		
Convertible preferred stock	1,131	1,131
Common stock	6,249	6,249
Retained earnings	2,256	2,256
Cumulative foreign currency translation adjustment	(711)	(711)
Common stock held in treasury	(50)	(50)
Other, including Flexible Equity Trust	(51)	(51)
Total shareholders' equity	8,824	8,824
Total capitalization	<u>\$21,369</u>	<u>\$21,375</u>

(a) Subsequent to March 31, 1999, our short-term debt has increased by approximately \$600 million, excluding the notes issued April 7, 1999, as a result of borrowings made under our commercial paper program and uncommitted credit facilities.

USE OF PROCEEDS

We intend to use the net proceeds from the sale of the notes (estimated to be approximately \$492,905,000 after underwriting discounts and expenses) principally to repay short-term indebtedness and for general corporate purposes. As of May 18, 1999, our weighted average interest rate on the debt to be repaid was approximately 5.0%.

RATIO OF EARNINGS TO FIXED CHARGES

	Three Months Ended March 31, 1999	Year Ended December 31,				
		1998	1997	1996	1995	1994
Ratio of Earnings to Fixed Charges	2.36	2.08	1.02	3.00	2.92	2.34

VI

3

Brigadown

ARTHUR ANDERSEN

May 24, 1999

Arthur Andersen LLP

LEHMAN BROTHERS INC.
BANC OF AMERICA SECURITIES LLC
CIBC WORLD MARKETS CORP.
As Underwriters
named in the Underwriting Agreement
dated May 19, 1999, relating to the issuance of
\$500,000,000 of 7.375% Notes due May 15, 2019

Suite 1900
711 Louisiana Street
Houston TX 77002-2786
713 237 2323

Dear Ladies and Gentlemen:

We refer to our letter of May 19, 1999, relating to Amendment No. 1 to Form S-3 Registration Statement (Registration No. 333-70465) filed by Enron Corp. (an Oregon corporation) and subsidiaries ("Enron") with the Securities and Exchange Commission ("Commission") under the Securities Act of 1933, as amended ("Act"), on February 3, 1999 ("Registration Statement"), with respect to the registration and sale by Enron of \$500,000,000 aggregate principal amount of 7.375% Notes due May 15, 2019, pursuant to an underwriting agreement dated May 19, 1999 ("Underwriting Agreement"). References to the "Prospectus" shall refer to the prospectus contained in the Registration Statement as supplemented by a prospectus supplement dated May 19, 1999, filed with the Commission pursuant to Rule 424 (b)(2).

We reaffirm as of the date hereof (and as though made on the date hereof) all statements made in that letter except that, for the purposes of this letter:

- a. The reading of minutes described in paragraph 4 of that letter has been carried out through May 19, 1999, officials of Enron having advised us that the minutes of all such meetings through that date have been furnished to us, except that our work did not extend to the following minutes which had not been finalized:

<u>Meeting</u>	<u>Date of Meeting</u>
Enron -	
Compensation and Management Development Committee	January 25, 1999
Audit and Compliance Committee	February 7, 1999
Finance Committee	February 7, 1999
Compensation and Management Development Committee	February 7, 1999
Nominating and Corporate Governance Committee	February 7, 1999
Nominating and Corporate Governance Committee	March 8, 1999
Executive Committee	March 22, 1999
Executive Committee	April 13, 1999
Nominating and Corporate Governance Committee	May 3, 1999
Audit and Compliance Committee	May 3, 1999
Finance Committee	May 3, 1999
Compensation and Management Development Committee	May 3, 1999
Board of Directors	May 4, 1999
Special Meeting of the Board of Directors	May 19, 1999

ARTHUR ANDERSEN

Page 2
May 24, 1999

<u>Meeting</u>	<u>Date of Meeting</u>
Northern Natural Gas Company- Board of Directors	March 10, 1999
Special Meeting of Board of Directors	April 2, 1999
Enron Oil & Gas Company - Board of Directors	May 4, 1999
Special Meeting of Board of Directors	May 8, 1999
Portland General Electric Company - Board of Directors	May 1, 1999
Board of Directors	May 15, 1999

- b. The references to May 14, 1999, in paragraph 4 and 6 of that letter are changed to May 19, 1999 (our work did not extend from the period from May 20, 1999, to May 24, 1999, inclusive), with the following exceptions noted in c below.
- c. As described in paragraph 6 of our letter dated May 19, 1999, Enron officials have advised us that no consolidated financial statements as of any date or for any period subsequent to March 31, 1999, are available. We have inquired of certain officials of Enron who have responsibility for financial and accounting matters whether (a) at May 19, 1999, there was any change in the capital stock, increase in combined short-term and long-term debt or any decrease in consolidated net assets or shareholders' equity of Enron as compared with amounts shown on the March 31, 1999, unaudited consolidated condensed balance sheet included in the March 31, 1999 Form 10-Q, incorporated by reference in the Registration Statement and Prospectus, or (b) for the period from April 1, 1999, to May 19, 1999, there were any decreases, as compared with the corresponding period in the preceding year, in consolidated operating revenues, net income or basic or diluted earnings per share of common stock. On the basis of these inquiries and our reading of the minutes as described in a, nothing came to our attention that caused us to believe that there was any such change, increase, or decrease, except in all instances for changes, increases, or decreases that the Registration Statement and Prospectus disclose have occurred or may occur, except that capital stock increased \$61 million and combined short-term and long-term debt increased \$143 million.
- d. This letter is solely for the information of the addressees and to assist the underwriters in conducting and documenting their investigation of the affairs of Enron in connection with the offering of the securities covered by the Registration Statement and Prospectus, and it is not to be used, circulated, quoted, or otherwise referred to within or without the underwriting group for any other purpose, including but not limited to the registration, purchase, or sale of securities, nor is it to be filed with or referred to in whole or in part in the Registration Statement and Prospectus or any other document, except that reference may be made to it in the Underwriting Agreement or in any list of closing documents pertaining to the offering of the securities covered by the Registration Statement and Prospectus.

Very truly yours,



ARTHUR ANDERSEN LLP