

REQUEST FOR COMMISSION ACTION

Control No.:

S-02-274-

Investigations involving Qwest

DETERMINED TO BE AN ADMINISTRATIVE MARKING
E.O. 12065, Section 8-102
By Jimi NARS, Date 5/2/2013

STED:

PRIVILEGED & CONFIDENTIAL

July 11, 2002

ACTION MEMORANDUM

TO: The Commission
FROM: Office of Legislative Affairs
RE: Congressional request for access to documents relating to SEC investigations involving Qwest Communications International, Inc. ("Qwest") and Global Crossing Ltd. ("Global Crossing").

RECOMMENDATION: That the Commission (1) authorize submission of a letter substantially in the form attached to Chairmen W.J. "Billy" Tauzin, Chairman of the House Energy and Commerce Committee ("Committee"), and James C. Greenwood, Chairman of the Committee's Subcommittee on Oversight and Investigations ("Subcommittee"), and (2) authorize SEC staff to provide staff of the Committee and Subcommittee with access to investigative testimony taken in the subject investigations as described further herein and to provide similar access to the same investigative testimony to other committees and subcommittees of Congress upon receipt of an initial written request and one day's advice memorandum notice to the Commission.

ACTION REQUESTED BY: Seriatim consideration.

SUNSHINE ACT STATUS: Not applicable.

PRIOR COMMISSION ACTION: Global Crossing and Qwest

On June 13, 2002, the Commission authorized SEC staff to brief staff of the Committee and Subcommittee with respect to the subject investigations and to provide briefing updates upon further request from the Committee or Subcommittee.

DETERMINED TO BE AN
ADMINISTRATIVE MARKING
E.O. 12965, Section 6-102
By *JMV* NARS, Date *5/2/2013*

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Global Crossing

On February 5, 2002, the Commission authorized a formal order of private investigation concerning Global Crossing.

On February 28, 2002, the Commission authorized SEC staff to brief the staff of the House Financial Services Committee concerning the Global Crossing investigation, provide briefing updates upon further request from the Committee, and to provide similar briefing updates to other committees and subcommittees of Congress upon receipt of an initial written request and with one day's advice memorandum notice to the Commission.

Qwest

On April 3, 2002, the Commission authorized a formal order of a private investigation concerning Qwest.

NOVEL, UNIQUE OR
COMPLEX ISSUES:

None.

OTHER OFFICES OR
DIVISIONS CONSULTED:

Division of Enforcement/Linda Thomsen
Office of General Counsel/Gordon Seymour
Central Regional Office/Randall Fons
Pacific Regional Office/Randall Lee

SOURCE OF CASE:

Not Applicable.

SMALL ENTITY STATUS:

Not Applicable.

PERSONS TO CONTACT:

Linda Thomsen
Peter Kiernan

202-942-4501
202-942-0015

DETERMINED TO BE AN
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 E.O. 12065, Section 6-102
 By JWH NARS, Date 5/2/2012

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I. BACKGROUND

On June 4, 2002 Chairmen Tauzin and Greenwood wrote to Chairman Pitt (see letter contained in Attachment A) regarding the Committee's investigations of Global Crossing and Qwest. The June 4 letter asked "that the Commission (staff) provide the Committee staff by June 17, 2002 a private briefing covering the details of the Commission's investigations of Global Crossing and Qwest." The Commission authorized the requested briefing on June 13, and the briefing took place on June 25.

Following the briefing, Committee staff contacted the Office of Legislative Affairs and requested an opportunity to review investigative testimony taken by SEC staff in connection with these investigations from the following persons:¹

Qwest Investigation:

Depositions from Messrs. Nacchio, Mohebbi, Wright² and Szdiga.

Global Crossing Investigation:

Depositions from Messrs. Rissik, Yaremko, Walsh, Lawlor, Casey, Wright,² and Perrone.

II. GLOBAL CROSSING AND QWEST INVESTIGATIONS

For a description of the Global Crossing and Qwest investigations see the staff's prior memo to the Commission, dated June 12, 2002, (see Attachment A) in which the staff sought authority to brief the Committee and Subcommittee. (As noted above, the Commission approved this memorandum on June 13).

III. DISCUSSION

In its attached memorandum of June 12 to the Commission, the staff indicated that "Chairmen Tauzin's and Greenwoods' request...did not request access to any nonpublic documents. Accordingly, we are not requesting authorization to provide such documents at this time. Should such access be requested, the staff will return to the Commission with another recommendation."

¹ Only some of the requested investigative testimony have been taken as of this date. Should the Commission approve this recommendation access to those investigative testimony requested which have been taken thus far will be offered now. Access to those investigative testimony which have been requested but which have not yet been taken will be offered after they have been taken.

² Wright's testimony has been taken in the Qwest investigation. She was a Global Crossing employee. Her testimony has not yet been taken in the Global Crossing investigation.

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The staff is concerned about providing access to sensitive nonpublic information and documents such as the investigative testimony in question here and takes very seriously the need to preserve their nonpublic status. The staff, including the Division of Enforcement and the Regional Offices, in particular, are concerned that news leaks such as the Wall Street Journal's article of June 26, 2002 about the Qwest investigation (attached at B) have interfered with and harmed and, if they continue, may further interfere with and harm our investigative efforts in these cases as well as parallel criminal investigations. That concern has been expressed to the staff of the Committee and the Subcommittee when they were briefed on these matters and has subsequently been re-emphasized to the Committee staff following their request for access to these investigative testimony. Moreover, Committee and Subcommittee staff will be required to review the documents at the Commission and not allowed copies (although, as is the usual practice, they will be permitted to take notes.) Further, Committee and Subcommittee staff members permitted access will not be open-ended and will be subject to reasonable limitation.

IV. RECOMMENDATION

Given the Committee's and Subcommittee's interest in this matter and their jurisdiction over the Commission and the laws relating to the matters under investigation, we recommend that: the Commission (1) authorize submission of a letter substantially in the form attached (see Attachment C) to Chairmen W.J. "Billy" Tauzin, Chairman of the Committee and James C. Greenwood, Chairman of the Subcommittee, and (2) authorize SEC to provide staff of the Committee and Subcommittee with access to investigative testimony taken in the subject investigations enumerated above and to provide similar access to the same investigative testimony to other committees and subcommittees of Congress upon receipt of an initial written request and one day's advice memorandum notice to the Commission.

The investigative testimony which Committee and Subcommittee staff will have access to here contain nonpublic information, making Commission authorization necessary because members and employees of the Commission may not divulge nonpublic information without such authorization.³

The proposed response letter indicates that the documents to which access is being provided contain nonpublic and sensitive information. The letter requests that the Committee and Subcommittee not publicly disclose this information without prior consultation with the Commission and asks that the staff's access to these documents and the attached proposed staff response also be kept nonpublic.

³ Rule 3-7 of the Commission's Rules of Conduct, 17 C.F.R. § 220.753-3(b)(7), applies generally to all requests for nonpublic information. Rule 3-7 requires Commission authorization for disclosure for any nonpublic Commission documents, and information contained in such documents, or any confidential Commission information.

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E.O. 12065, Section 6-103
By *JMV* NARS, Date *5/2/2012*

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ATTACHMENTS:

- (A) Staff memorandum to the Commission dated June 12, 2002.
- (B) Wall Street Journal article of June 26, 2002 headlined "Qwest Gets a Hard Time from SEC....."
- (C) Proposed staff letter advising that access to investigative testimony has been approved.

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By JWH E.O. 12065, Section 6-102
NARS, Date 5/2/2012

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June 12, 2002

ACTION MEMORANDUM

TO: The Commission
FROM: Office of Legislative Affairs
RE: Congressional request for a briefing concerning Qwest Communications International, Inc. ("Qwest") and Global Crossing Ltd. ("Global Crossing").

RECOMMENDATION: That the Commission (1) authorize submission of a letter of response substantially in the form attached to Chairmen W.J. "Billy" Tauzin, Chairman of the House Energy and Commerce Committee ("Committee") and James C. Greenwood, Chairman of the Committee's Subcommittee on Oversight and Investigations ("Subcommittee") and (2) authorize SEC staff to brief staffs of the Committee and Subcommittee on these matters and to provide briefing updates upon further request from the Committee or Subcommittee.

ACTION REQUESTED BY: Seriatim consideration.

SUNSHINE ACT STATUS: Not applicable.

PRIOR COMMISSION ACTION: Global Crossing

On February 5, 2002, the Commission authorized a formal order of private investigation concerning Global Crossing.

On February 28, 2002, the Commission authorized SEC staff to brief the staff of the House Financial Services Committee concerning the Global Crossing investigation, provide briefing updates upon further request from the Committee and to provide similar briefing updates to other committees and subcommittees of Congress upon receipt of an initial written request and with one day's advice memorandum notice to the Commission.

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Qwest

On April 3, 2002, the Commission authorized a formal order of a private investigation concerning Qwest.

NOVEL, UNIQUE OR
COMPLEX ISSUES:

None.

OTHER OFFICES OR
DIVISIONS CONSULTED:

Division of Enforcement/Linda Thomsen 942-4501
Office of the Chief Accountant/Bob Burns 942-4400
Division of Corporation Finance/Jim Daly 942-2881
Office of the General Counsel/J. Gordon Seymour 942-0932
Pacific Regional Office/Kelly Bowers 323-965-3924
(Global Crossing)
Central Regional Office/Katherine Addleman 303-844-1070
(Qwest)

SOURCE OF CASE:

Not Applicable.

SMALL ENTITY STATUS:

Not Applicable.

PERSONS TO CONTACT:

Linda Thomsen	202-942-4501
Peter Kiernan	202-942-0015
Kelly Bowers (Global Crossing)	323-965-3924
Katherine Addleman (Qwest)	303-844-1070

I. BACKGROUND

On June 4, 2002 Chairmen Tauzin and Greenwood wrote to Chairman Pitt (see letter at Attachment A) regarding the Committee's investigations of Global Crossing and Qwest. The June 4 letter asked "that the Commission (staff) provide the Committee staff by June 17, 2002 a private briefing covering the details of the Commission's investigations of Global Crossing and Qwest."

II. GLOBAL CROSSING INVESTIGATION

Global Crossing, a telecommunications company that spent billions over the past five years building a worldwide fiber optic network, filed for bankruptcy protection in New York on Monday, January 28, 2002.¹ On Wednesday, January 30, the press reported that a former finance

¹ The Commission filed a notice of appearance in that bankruptcy, which is reportedly the fourth largest bankruptcy ever.

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officer of Global Crossing, Roy Olofson ("Olofson"), had questioned Global Crossing's accounting in a letter to the company's top lawyer five months before the bankruptcy filing. In the letter, Olofson principally questioned Global Crossing's accounting for the sale of contracts to provide fiber-optic capacity, known in the telecommunications industry as "Indefeasible Rights of Use" or "IRUs." Olofson's letter questioned Global Crossing's practice of including revenue from IRUs in the three consecutive quarters ended June 30, 2001, in its pro forma results as "Cash Revenue" and "Adjusted EBITDA." In announcing and reporting its quarterly and annual financial results, Global Crossing highlighted these non-GAAP Cash Revenue and Recurring Adjusted EBITDA numbers.²

The staff opened its informal inquiry on January 30, 2002, and obtained a formal order of investigation on February 5, 2002, to determine whether there have been violations of the antifraud provisions of Section 17(a) of the Securities Act of 1933 and Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, the financial reporting provisions of Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder, and the books and records and lying to auditors provisions of Section 13(b) of the Exchange Act and Rules 13b2-1 and 13b2-2 thereunder.

Since February 5, the staff has subpoenaed documents from Global Crossing, its auditors Arthur Andersen, Olofson, parties with whom Global Crossing purchased and sold IRUs, and securities analysts who have followed Global Crossing.³ The staff has received approximately 170 boxes of documents and 22 compact discs (of Global Crossing emails and other data) in response to these subpoenas and is currently reviewing, organizing and analyzing the documents. The staff has also interviewed Olofson, taken the testimony of seven present or former Global Crossing employees and is scheduling for June and July the testimony of seven present or former Global Crossing senior officials.

The staff's investigation is currently focusing primarily on certain Global Crossing IRU transactions in which it swapped fiber-optic capacity with another telecommunications company. In these transactions, Global Crossing sold fiber-optic capacity at a certain price to another telecommunications company, and that company simultaneously sold capacity usually at an equal price to Global Crossing. Global Crossing then included its sales price in its announced pro forma Cash Revenue and Recurring Adjusted EBITDA results. These swap transactions appeared to have had a material effect on Global Crossing's pro forma results.⁴ The staff is investigating whether Global Crossing adequately disclosed the material facts regarding these

² Global Crossing's earnings announcements and periodic financial filings disclosed that the revenue from IRUs were included in the pro forma numbers.

³ The staff has been advised by counsel for Global Crossing and Arthur Andersen that, immediately upon receiving the Commission subpoenas, Global Crossing and Arthur Andersen ordered that no documents be destroyed.

⁴ For example, for the second quarter 2001, Global Crossing announced Recurring Adjusted EBITDA of \$472 million. Included in this amount was \$345 million in capacity it sold to other companies from whom Global Crossing simultaneously purchased \$358 million in capacity.

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swap transactions and properly accounted for these IRU swaps in its pro forma Cash Revenue and Recurring Adjusted EBITDA results. The staff is also investigating whether, if the company fraudulently misstated its results, any Global Crossing insider sold the company's stock using the information that the company's pro forma results had been misstated. The staff is further investigating whether broker-dealer analysts committed fraud in recommending Global Crossing to the broker-dealers' customers.⁵

The staff is coordinating its investigation with the United States Attorney's Office and the FBI in Los Angeles.

III. QWEST INVESTIGATION

Through documents obtained by the staff in the Global Crossing investigation, and information reported in the media, the staff learned in approximately March 2002 that Qwest may have improperly recognized revenue on sales of its fiber-optic capacity, or IRUs, and that such sales included large swaps with other telecommunications companies including Global Crossing and Enron.⁶ The staff obtained a formal order of investigation on April 3, 2002, to determine whether there have been violations of the antifraud provisions of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, the financial reporting provisions of Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, 13a-13 thereunder, and the books and records and lying to auditors provisions of Section 13(b) of the Exchange Act and Rules 13b2-1 and 13b2-2 thereunder. Since issuance of the formal order, the staff has subpoenaed, and is receiving documents from, Qwest, Qwest's auditors Arthur Andersen, and other telecommunications companies involved with Qwest in the purchase and sale of IRUs. Further, the staff has begun testimony of Qwest officials and other individuals.

Like Global Crossing, Qwest sold capacity on its fiber-optic network to other carriers at a fixed price for a long period, usually 20 or 25 years, and simultaneously bought capacity on the other carrier's network for a substantially similar time period and amount ("IRU swap"). Qwest recognized up-front a substantial portion of the fiber-optic capacity sold as revenue and booked the capacity acquired as a long-term asset to be expensed over the term of the IRU. The staff is

⁵ The staff is also investigating whether Global Crossing properly accounted for these swap transactions in its reported GAAP revenue in Forms 10-Q for its quarters ended on March 31, 2001 and June 30, 2001. The staff will further investigate whether Global Crossing adequately disclosed its liquidity and capital resources and the effect these matters had on its filing for bankruptcy.

⁶ The staff is investigating two other issues also relating to possible accounting fraud. Qwest may have improperly recognized revenue on and made misleading disclosures concerning the sale of capital equipment in exchange for Qwest buying Internet services or contributing equity financing. Second, Qwest may have improperly disclosed that it recognized revenue by accelerating the publication of its telephone directory and extending the lives of directories.

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investigating whether Qwest's accounting treatment of IRU swaps was in conformity with GAAP. If the IRU swaps are considered an exchange of similar nonmonetary assets under GAAP or do not meet other requirements for revenue recognition, Qwest should have recognized no or little gain on these transactions. For the first nine months of 2001, Qwest sold approximately \$870 million worth of network capacity to vendors from which it also bought \$868 million worth of capacity in separate transactions, recognizing approximately \$664 million in revenue.⁷

The staff's investigation to date has revealed that some swaps involved the exchange of undefined fiber-optic capacity or capacity that could be exchanged by the purchaser. Additionally, some transactions apparently involved the "roundtripping" of cash resulting in no or little real economic gain to either party.⁸ For example, the "whistle blower" in the Commission's investigation of Global Crossing, Olofson, highlighted a \$100 million fiber-optic capacity swap between Qwest and Global Crossing in 2001 that he claims was a nonmonetary exchange of assets Global Crossing used to manufacture revenue and boost its earnings. Moreover, on September 30, 2001, the last day of the third quarter, Qwest and Enron Broadband Services, a subsidiary of Enron, agreed to buy \$112 million worth of communications network capacity from each other.

The staff investigating Qwest has met with the United States Attorney's Office and the FBI in Denver and has been advised that they will be opening investigations.

IV. RECOMMENDATION

That the Commission (1) authorize submission of a letter of response substantially in the form attached to Chairmen W.J. "Billy" Tauzin, Chairman of the Committee and James C. Greenwood, Chairman of the Subcommittee and (2) authorize SEC staff to brief staffs of the Committee and Subcommittee on these matters and to provide briefing updates upon further request from the Committee or Subcommittee.

The briefing to be provided here responds to the Committee's request for a briefing and will be similar to briefings previously authorized by the Commission and provided by SEC staff relative to other ongoing SEC investigations.

⁷ The \$206 million difference between the value of the capacity sold and the amount Qwest recognized as revenue was generally for operation and maintenance contracts that Qwest recognized as revenue over the life of the agreements.

⁸ The round-tripping of cash involves the parties exchanging identical or substantially similar amounts of cash in order to give the appearance that the transaction has economic substance.

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The proposed staff briefings will contain nonpublic information, making Commission authorization necessary because members and employees of the Commission may not divulge nonpublic information without such authorization.⁹

The proposed response letter indicates that the information being provided contains nonpublic and sensitive information. The letter requests that the Committee not publicly disclose this information without prior consultation with the Commission, asks that the briefing itself and the attached proposed staff response also be kept nonpublic.

Chairmen Tauzin's and Greenwood's request for this briefing did not request access to any nonpublic documents. Accordingly, we are not requesting authorization to provide such documents at this time. Should such access be requested, the staff will return to the Commission with another recommendation.

ATTACHMENTS:

- (A) June 4, 2002 request from Chairmen Tauzin and Greenwood.
- (B) Proposed staff response to June 4 request.

⁹ Rule 3-7 of the Commission's Rules of Conduct, 17 C.F.R. § 220.753-3(b)(7), applies generally to all requests for nonpublic information. Rule 3-7 requires Commission authorization for disclosure for any nonpublic Commission documents, and information contained in such documents, or any confidential Commission information. As noted earlier, the Commission previously authorized SEC staff on February 28, 2002 to provide briefings and briefings updates with respect to Global Crossing to committees and subcommittees of Congress upon receipt of an initial written request and with one day's advice memorandum notice to the Commission. Pursuant to such authorization, staff could have sought authorization to provide the Global Crossing briefing discussed herein by means of a separate advice memorandum. Because the current request asks for a briefing on Global Crossing AND Qwest together, however, we are seeking authorization to brief on both matters via this single action memorandum.

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By *Jimi* NARS, Date *5/2/2012*

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ONE HUNDRED SEVENTH CONGRESS
U.S. House of Representatives
Committee on Energy and Commerce
Washington, DC 20515-6115

W.J. "BILLY" TAUZIN, LOUISIANA,
CHAIRMAN

June 4, 2002

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HENRY A. WAXMAN, CALIFORNIA
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DAVID J. MARVITANO, STAFF DIRECTOR
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Chairman Harvey L. Pitt
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Dear Chairman Pitt:

The Committee on Energy and Commerce has undertaken a comprehensive review over the propriety of financial statements by some telecommunications companies. Recent press reports have indicated that Global Crossing Ltd. ("Global Crossing") and Qwest Communications International Inc. ("Qwest") may have engaged in transactions that had the effect of substantially enhancing their financial position. Further allegations surround omission of material disclosures that would be necessary for Qwest's and Global Crossing's investors to understand the companies' true financial condition.

Consistent with our oversight obligations, the Committee on Energy and Commerce is investigating these matters. To assist in this investigation, we request that the Commission provide to the Committee staff by June 17, 2002, a private briefing covering the details of the Commission's investigation of Global Crossing and Qwest.

If you have any questions, please contact Jennifer Safavian, Majority Counsel, at (202) 226-2424.

Billy Tauzin
W.J. "Billy" Tauzin
Chairman

Sincerely,
James C. Greenwood
James C. Greenwood
Chairman
Subcommittee on Oversight
and Investigations

cc: The Honorable John D. Dingell, Ranking Member
The Honorable Peter Deutsch, Ranking Member
Subcommittee on Oversight and Investigations

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By *Jivi* NARS, Date *5/2/2012*

The Honorable W.J. "Billy" Tauzin
Chairman
Committee on Energy and Commerce
U.S. House of Representatives
2125 Rayburn House Office Building
Washington, DC 20515

The Honorable James C. Greenwood
Chairman
Subcommittee on Oversight and Investigations
Committee on Energy and Commerce
U.S. House of Representatives
2125 Rayburn House Office Building
Washington, DC 20515

Dear Chairmen Tauzin and Greenwood:

In further response to your letter of June 4, 2002 to Chairman Pitt regarding the Committee's and Subcommittee's interest in recent events involving Global Crossing Ltd. and Qwest Communications International, Inc. and in response to the request of your staff for access to certain specified investigative testimony taken by SEC staff in connection with those events, the staff of the Commission has sought and received authorization from the Commission to provide Committee and Subcommittee staff with access to such investigative testimony, *as discussed with Jennifer Salazar of your staff*

As we previously indicated, we understand that, absent extraordinary circumstances, it is not the practice of Congressional committees to make public disclosure of sensitive, nonpublic material without prior consultation with the responsible agency. Since the information contained in the investigative testimony to which access is being provided is sensitive and nonpublic, we respectfully request that the Committee and Subcommittee follow that practice in this instance. Consistent with this, we also request that your staff's access to these documents and this letter also be kept nonpublic. As I am sure you can understand, we have to be very concerned with the possibility of any disclosure of information that could unduly prejudice the subject of an investigation, raise questions about the independence of the Commission enforcement process, or otherwise jeopardize Commission enforcement actions.

We look forward to working with you on these important issues. Peter Kiernan, Deputy Director of SEC's Office of Legislative Affairs, is available at (202) 942-0015 to provide the Committee, the Subcommittee, and their staffs with any further assistance you may require.

Yours truly,

Giovanni Prezioso
General Counsel

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By JMV NARS, Date 5/2/2012

MINUTES OF THE SECURITIES AND EXCHANGE COMMISSION

SERIATIM DISPOSITION
PURSUANT TO 17 C.F.R. 200.42

Wednesday, July 31, 2002

COMMISSIONERS VOTING:

Harvey L. Pitt, Chairman
Isaac C. Hunt, Jr.
Cynthia A. Glassman
Harvey J. Goldschnid

The Commission considered a memorandum from the Division of Corporation Finance, dated July 31, 2002, in the matter of certification of disclosure in companies' quarterly and annual reports.

Staff recommended that the Commission issue a release providing supplemental information about the rules proposed on June 14, 2002 in light of the recent enactment of the Sarbanes-Oxley Act of 2002.

The Commission approved (4-0) the staff recommendation.

(See Release 34-46300, dated August 2, 2002.)

Margaret H. McFarland
Deputy Secretary

By: Ida Williams
Program Information Specialist