IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF DELAWARE

In re	:	**Chapter 11**
SEMCRUDE, L.P., *et al.*,	:	**Case No. 08-11525 (BLS)**
Debtors.	:	**Jointly Administered**

FINAL REPORT OF LOUIS J. FREEH

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I. BACKGROUND

On July 22, 2008, SemCrude, L.P. ("SemCrude"), its parent company, SemGroup, L.P. ("SemGroup"), and certain entities directly or indirectly related to them (individually referred to herein by the name of the respective entity, or, collectively, as the "Debtors"), each filed voluntary petitions for relief under Chapter 11 of Title 11 of the United States Code in the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court").[1] The Honorable Brendan L. Shannon was assigned to the Debtors' cases.

On August 12, 2008, Roberta A. DeAngelis, Acting United States Trustee for Region 3, filed a Motion for an Order Directing the Appointment of an Examiner in the Bankruptcy Court. *See* Exhibit 1.[2] The Bankruptcy Court granted the Motion pursuant to the Order Directing United States Trustee to Appoint an Examiner on September 10, 2008 (the "Examiner Order"). *See* Exhibit 2. Thereafter, the United States Trustee selected Louis J. Freeh, Esq., to serve as the examiner (the "Examiner"). The Bankruptcy Court approved Mr. Freeh's appointment as the Examiner pursuant to an Order entered on October 14, 2008. *See* Exhibit 3. On November 24, 2008, after presenting his work plan to the Bankruptcy Court in accordance with the Examiner Order, the Examiner formally commenced his examination.

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[1] (1) SemCrude, L.P.; (2) Chemical Petroleum Exchange, Incorporated; (3) Eaglwing, L.P.; (4) Grayson Pipeline, L.L.C.; (5) Greyhawk Gas Storage Company, L.L.C.; (6) K.C. Asphalt, L.L.C.; (7) SemCanada II, L.P.; (8) SemCanada, L.P.; (9) SemCrude Pipeline, L.L.C.; (10) SemFuel Transport, L.L.C.; (11) SemFuel, L.P.; (12) SemGas Gathering, L.L.C.; (13) SemGas Storage, L.L.C.; (14) SemGas, L.P.; (15) SemGroup Asia, L.L.C.; (16) SemGroup Finance Corp.; (17) SemGroup, L.P.; (18) SemKan, L.L.C.; (19) SemManagement, L.L.C.; (20) SemMaterials Vietnam, L.L.C.; (21) SemMaterials, L.P.; (22) SemOperating G.P., L.L.C.; (23) SemStream, L.P.; (24) SemTrucking, L.P.; and, (25) Steuben Development Company, L.L.C. On October 22, 2008, the following additional entities filed voluntary petitions for relief under Chapter 11: (26) SemGroup Holdings, L.P.; and (27) SemCap, L.L.C.

[2] The Exhibits referenced herein are filed separately in an appendix labeled as "Exhibits to Final Report of Louis J. Freeh."

The Examiner was directed by the Bankruptcy Court to: (1) investigate the circumstances surrounding the Debtors' trading strategy and the transfer of the New York Mercantile Exchange ("NYMEX") account; (2) investigate the circumstances surrounding the Insider Transactions (as defined in the Examiner Order) and the formation of SemGroup Energy Partners L.P. ("SGLP"); (3) investigate the circumstances surrounding the potential improper use of borrowed funds and funds generated from the Debtors' operations and the liquidation of their assets to satisfy margin calls related to the trading strategy for the Debtors and certain entities owned or controlled by the Debtors' officers and directors; (4) determine whether any directors, officers or employees of the Debtors participated in fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the Debtors; and (5) determine whether the Debtors' estates have causes of action against current or former officers, directors, or employees of the Debtors arising from any such participation.

The Examiner has reviewed more than 100,000 hard copy documents and more than 200,000 electronic documents. The Examiner has interviewed more than 100 people, some on several occasions, including current and former employees of the Debtors, and other individuals with knowledge of the Debtors' operations, its financial matters, and its trading activities. The Examiner has also interviewed representatives of, and obtained documents from, various entities that are or were associated with the Debtors. *See* Exhibit 4.

The Examiner interviewed representatives of PricewaterhouseCoopers ("PwC"), who conducted audits at SemGroup, and reviewed its work papers. The Examiner did not obtain any information from PwC that was inconsistent with his investigative conclusions.

Three of the Debtors' former principals (former Chief Executive Officer Thomas L. Kivisto ("Kivisto"), former Chief Financial Officer Gregory C. Wallace ("Wallace"), and former Treasurer Brent Cooper ("Cooper") refused the Examiner's requests for interviews. They also each invoked their Fifth Amendment privilege against self-incrimination during the Examiner's subsequent depositions of them.

The Examiner has been in contact with the following Governmental entities during his examination: (1) the United States Trustee's Office (Region 3); (2) the United States Attorney's Office for the Northern District of Oklahoma; (3) the Federal Bureau of Investigation (Oklahoma); (4) the United States Securities and Exchange Commission; (5) the United States Commodities Futures Trading Commission; (6) the United States Department of Justice (Fraud Section); (7) the United States Department of the Treasury (Office of the Comptroller of the Currency); (8) the United States Attorney's Office for the Southern District of New York; and (9) the Federal Bureau of Investigation (New York). The Examiner wishes to express his appreciation for the assistance that has been provided to him by the Government during his examination.

The Examiner's Report is divided into an Executive Summary, which contains a summary overview of the results of his examination, and the Examiner's Findings, which includes a detailed analysis of the specific areas of inquiry identified in the Examiner Order.

II. THE EXAMINER'S EXECUTIVE SUMMARY

SemGroup was founded in February 2000 (as Seminole Transportation and Trading) by three principals, each with a different area of expertise. Kevin L. Foxx ("Foxx"), SemGroup's

former Executive Vice President and Chief Operating Officer, and SGLP's current President and Chief Executive Officer, was responsible for its operations and transportation issues. Wallace, SemGroup's former Chief Financial Officer, was responsible for its financial and administrative matters. Kivisto, SemGroup's former President and Chief Executive Officer, was responsible for its oil and commodities trading activities.

SemGroup provided gathering, transportation, storage, distribution, and marketing and other midstream services to independent producers and refiners of petroleum products. SemGroup expanded rapidly from 2000 through 2008 through acquisitions and capital infusions, including the profits realized from a successful commodities trading program (from 2000 to 2006). Other sources of capital included the increased use of bank loans, private equity investments, bond and stock offerings, and the adoption of a Master Limited Partnership ("MLP") business model in 2007.

Although SemGroup's businesses maintained a rapid growth, something that did not change was that its three principals continued to be the key decision makers in their respective areas of expertise. Foxx, who maintained an office in Houston, worked almost exclusively on SemGroup's operations and transportation issues, until he assumed additional responsibilities with SGLP in 2007. Wallace, with the assistance of Cooper, made SemGroup's key financial decisions. Kivisto maintained control of SemGroup's trading functions.

SemGroup's rapid growth was also reflected in an overall lack of administrative managerial controls. As an example, an experienced Human Resources ("HR") manager was hired in February 2008. She stated that she was surprised at the lack of structure in the HR Department, which had developed no job descriptions and conducted few performance reviews,

and in SemGroup as a whole, which had little coordination among its business units and no meetings in which its business unit leaders could discuss long-term issues. More importantly, top managers did not know or understand the added risk that Kivisto's trading policies and strategies imposed upon SemGroup during a turbulent time in commodities trading in 2007 and 2008.

A. Commodities Trading

Kivisto personally conducted and directed most of SemGroup's options trading activity from 2000 until approximately 2005. In late 2004, Kivisto selected two individuals (Ms. Mia Oven ("Oven") and Mr. James Coen ("Coen")) to assist him in executing his options trading strategy. *See* Exhibit 5 for a glossary of commodities trading terms and definitions.

Kivisto tightly controlled SemGroup's trading strategy and was responsible for hiring Coen and Oven, and for recruiting Mr. Joe Shimonov ("Shimonov") in 2005, to assist him in implementing the strategy. Kivisto knew that these individuals had little, if any, prior commodity options trading experience, and could be trusted to do what he directed. Similarly, Mr. William Allen ("Allen") was later chosen as SemGroup's Risk Director, with no prior risk management experience. He did not serve adequately in this role.

With the exception of SemCrude and, to a lesser extent, SemCanada, SemGroup's other business units, and the employees who primarily dealt with physical commodities transactions, generally adhered to common, mostly risk-averse strategies that rarely incorporated the use of options.

B. Kivisto's Trading Strategy

Kivisto engaged in a complex trading strategy that was known only to him and a few trusted confidants. There were aspects of Kivisto's trading strategy that were speculative and that placed SemGroup at increased risk which, when coupled with the unprecedented rise in and volatility of the price of oil in 2007 and 2008, led to the filing of the Debtors' bankruptcy petitions. The speculative aspects of Kivisto's trading strategy were inappropriate and violated SemGroup's internal risk policies and its lender covenants.

An important part of Kivisto's trading strategy, according to Oven and Coen, was his philosophy that oil prices would always return to a normalized price range. Kivisto's trading strategy did not allow for options trading losses. Rather, the options positions that neared expiration with a Mark to Market ("MtM") loss would be reset, or "rolled forward," with the anticipation that the price of oil would eventually return to a "normal" price range. The goal of Kivisto's strategy, according to Coen and Oven, was to increase trading revenue through the sale of options and to prevent the realization of losses arising from options sales through the sale of more options. The anticipated return of the price of oil to a "normal" range did not occur before the margin costs, which as a result of Kivisto's trading strategy, consumed SemGroup's available cash and credit.

In essence, Kivisto "bet" that the price of oil would return to a more normal trading range, and that the unrealized losses associated with the "rolled forward" trades would eventually expire worthless. SemGroup's virtually blind deferral to Kivisto on trading matters, and its failure to develop or implement a suitable risk management policy, was central to its problems.

As SemGroup's "rolled forward" trading positions and its unrealized losses increased, and as the price of oil and volatility of the price of oil increased, the margin requirements it needed to pay to maintain its trading accounts also increased. Although SemGroup was desperately using funds from various sources to meet its escalating margin and margin call requirements in 2007 and 2008, to keep the ball afloat, so to speak – generally without the full knowledge or assent of its lenders and investors – it eventually ran out of the money to do so and to continue its business operations. On July 10, 2008, SemGroup advised its lenders that it had run out of money. Last minute attempts by it to increase its credit facility failed. Since SemGroup could no longer engage in trading activity because it did not have the necessary funds to meet its margin call requirements, it transferred its NYMEX trading book to Barclays, on July 15, 2008. As a result, SemGroup's approximate $2.5 billion unrealized MtM loss previously booked on its financial statements became a realized loss for financial reporting purposes. SemGroup's total trading losses exceeded $3 billion.

An analogy of sorts can be drawn, for illustrative purposes, between Kivisto's options trading strategy and a game of chance. When playing roulette, an individual can bet on "red" or "black." If an individual placed a bet on "black" and lost, that person could stop playing the game or place another bet and play again. If the person stopped playing the game at that point, he or she would realize a loss. If the person played again, the loss could be "rolled forward," by placing another bet. However, additional money would be required to place the bet. If the person continued to double the bet until the person won, his or her previous losses would be eliminated. However, the person would need to continue risking an increasingly large amount of money on the bets, and could do so only for as long as he or she had sufficient funds to place additional bets.

SemGroup was like the person in the previous hypothetical who bet on "black." In this context, "black" represents the belief that the price of oil would decline in the future, while "red" represents the belief that the price of oil would continue to rise. SemGroup continued to lose by betting on "black." In other words, "red" was the winning bet in 2007 and 2008 because the price of oil continued to rise. However, SemGroup continued to place bets. It engaged in an increasing volume of options trades, in part to obtain additional cash from the premiums it received from them, with the hope that, eventually, "black" would be the winning bet, and SemGroup's "rolled forward" trading losses would evaporate.

In this context, the money needed to place additional bets represents the margin and margin call amounts that SemGroup was required to pay to continue its trading activity. However, by engaging in additional trades and "rolling forward" its positions, its losses mounted. Before "black" became a winning bet, SemGroup ran out of the money it needed to continue to place more bets. That is, the ongoing margin and margin call drain that SemGroup experienced as a result of its trading strategy in 2007 and 2008 eventually exhausted its available cash supply. It no longer had the money required to pay its margins and margin call requirements, which meant it could no longer engage in trading activity.

In addition, at times, options trades were placed on the books of SemGas, SemFuel, SemMaterials, SemEuro and SemStream by Coen and/or Oven, under Kivisto's direction and generally without the prior knowledge of the business unit leaders. For example, the MtM losses for the options trades placed on SemEuro's books in approximately March 2008 grew to more than $100 million. After SemEuro complained that these MtM losses were negatively affecting its banking relationship and had the potential of rendering it insolvent, the trades were removed from SemEuro's books and placed on SemCrude's books.

The options trading directed by Kivisto was, at best, loosely linked to inventory capacity and not current inventory levels. As an example, Coen stated that, under Kivisto's direction, some of the options trades he placed on the books of SemStream and SemMaterials were executed to protect the underlying physical inventory assets, while other trades were placed to enhance marketing (commodities trading) revenues. Coen admitted that he engaged in options trades that were unrelated to physical inventory or purchases, under the direction of Kivisto.

C. Risk Management

In approximately 2003, SemGroup established a Risk Management Policy ("RMP") as a requirement of its lender's covenants. *See* Exhibit 6. SemGroup's RMP was insufficient given the nature of its trading activity, and toothless in several important respects. For instance, although Kivisto tightly controlled SemGroup's options trading activity, the RMP required that trading violations be reported to *him*, rather than to a separate oversight component. In other words, SemGroup's RMP required *Kivisto* to monitor *Kivisto's* trading activity. Essentially, because of the power he had from the RMP as CEO, and because he was also SemGroup's head trader, Kivisto was in position to approve his own trading behavior, and that of others.

The written RMP required that a Risk Management Committee ("RMC"), consisting of the CEO, COO, CFO, and CAO, meet at least once each month to evaluate the Debtors' trading activity. However, there is no evidence that SemGroup's RMC ever met. Although there were likely discussions among some of its members during the course of their day-to-day activities, they never met for the specific purposes as required by the RMP.

The position limits and stop-loss limits referenced in the RMP failed to adequately monitor or report the risks associated with Kivisto's options trading strategy. Those limits were

frequently violated. SemGroup's traders also failed to comprehend fully the effects of price volatility on its portfolio.

The RMP further required, in effect, that SemGroup's trading activity be supported by physical inventory, and that it not engage in trading in "naked options," which would be, by definition, speculative trading. At times, SemGroup's main traders *assumed* that SemGroup had sufficient physical inventory to support their trading activity or they disregarded inventory levels altogether when executing trading transactions. As the Examiner has determined, and as one of SemGroup's traders acknowledged, SemGroup *did not* always have sufficient physical inventory to support its options trades. SemGroup therefore engaged in some "naked options" transactions (which included the sale of naked call and put options).

It should be noted that SemGroup included the options premiums it collected in its cumulative stop-loss calculation, although the RMP does not specifically define the calculation. (A stop-loss figure generally represents the maximum amount of trading losses that a company is willing to incur. If the value of that calculation reaches the policy-defined limit, trading personnel are forced to reduce or eliminate their trading positions). The inclusion of premiums collected through the sale of options provided traders with a mechanism to conceal SemGroup's realized or MtM losses. SemGroup's stop-loss calculation allowed traders to appear to offset losses simply by selling options and generating income from the premiums it received. When experiencing a large MtM loss, SemGroup traders could maintain compliance with the cumulative stop-loss limit through the sale of large quantities of options. While options transactions may serve legitimate business needs, the sale of options for the purpose of collecting premiums can introduce adverse market risk into the trading process. The inclusion of option

premiums in its stop-loss calculation allowed for the inaccurate portrayal of the true financial condition of SemGroup's trading operations.

D. Westback Purchasing Company, L.L.C.

The RMP also contained a restriction which prohibited SemGroup's traders from engaging in trades for the benefit of the trader's own account. *See* Exhibit 6, Section 4.4. Kivisto, and the traders he controlled, violated this restriction by conducting trades on behalf of, or by using, Westback Purchasing Company, L.L.C. ("Westback"), a limited liability trading partnership which Kivisto owned and controlled. Such trades were made for Kivisto's personal benefit through the account of Eaglwing, a SemGroup business unit.

Between 2000 and 2007, a substantial number of trades were conducted on behalf of Westback in the Eaglwing account. Until 2007, these trades yielded substantial profits for Kivisto. Indeed, in 2006 alone, Kivisto and his wife, Mrs. Julie Kivisto, had a net taxable income of approximately $26 million from Westback.

The trading strategy Kivisto utilized with the Westback trades was consistent with the trading strategy he employed on behalf of SemGroup. However, the accounting for the Westback transactions was supervised by SemGroup's employees. Moreover, SemGroup essentially "fronted" the margins and margin call requirements for Kivisto's personal Westback options trades using Eaglwing.

In addition to options trading, Kivisto engaged in physical commodities trades for SemGroup through Westback, his alter ego. Pursuant to a verbal agreement among Kivisto, Cooper, and Wallace, Kivisto, through Westback, arranged for physical commodity transactions

on behalf of Eaglwing, a SemGroup business unit, for which Eaglwing paid Westback (Kivisto) what could be considered a commission. Eaglwing paid Westback (Kivisto) approximately $4.14 million in commissions from January 2007 through July 2008 for Kivisto's physical commodities trades. However, this activity was within the scope of Kivisto's duties at SemGroup, for which he was already compensated. By conducting physical commodities trades for SemGroup through Westback, and by receiving commissions for them from Eaglwing, Kivisto improperly received additional compensation from SemGroup for the performance of his duties.

There were also unsupported payments from Eaglwing to Westback, which appear to be settlements for actual barrels of oil purchased by Westback, although it is unclear. The total amount of these transactions was $21.9 million.

Although Kivisto's connection to Westback was known to some SemGroup executives – it was referenced in Kivisto's employment agreements, and SemGroup had considered purchasing Westback from Kivisto around the time of SemGroup's formation – Kivisto was not specifically authorized to use SemGroup's resources and funds for his personal use. By 2006, the Westback transactions became the subject of concern to some of SemGroup's personnel, and its outside attorneys and accountants. However, the SemGroup executives with knowledge of Westback did not put a halt to the Westback transactions. They allowed them to continue, which exposed SemGroup to additional risk.

According to non-management members of SemGroup's Management Committee ("MC"), the MC was not made aware of the trading relationship with Westback, and was not

informed by SemGroup of Westback's utilization of its resources or Westback's resulting debt to SemGroup until July 2008, shortly before the filing of the Debtors' bankruptcy petitions.

The options conducted in the Eaglwing account on behalf of Westback in 2007 and 2008 resulted in large unrealized losses. When SemGroup ran out of money and its trading book was sold to Barclays, on July 15, 2008, Westback owed SemGroup approximately $290 million. If Westback (Kivisto) had reimbursed SemGroup for this amount, it might have affected the timing of, or the necessity of, SemGroup's bankruptcy filing.

E. Master Limited Partnership (MLP) – The "Dropdown" of Assets

An MLP business model was suggested to SemGroup as early as 2003, and was eventually implemented by it in 2007. The MLP business model is commonly used in the energy industry, and it was a reasonable business decision by SemGroup to utilize the MLP concept. The MLP business model allowed for capital infusions to the parent company through public offerings, as a return on capital to investors, and as a source of cash to be made available to the parent for subsequent acquisitions or working capital requirements.

SemGroup's adoption of the MLP business model resulted in the July 2007 formation of SGLP, and the subsequent "dropdown" of assets to it in January and May 2008. The dropdowns were part of a long-term MLP planning process developed in early 2007. Additional dropdowns were scheduled by SemGroup to occur in the fourth quarter of 2008, as well as in 2009 and 2010. *See* Exhibit 7. As a result of the aforementioned dropdown transactions, SemGroup's investors, including Riverstone Management and Ritchie Capital Management (whose members sat on SemGroup's MC), and SemGroup's unit holders, including Kivisto, Wallace, and Foxx, received

returns on their investments and proceeds from their respective ownership interests in SemGroup.

Some of the money SemGroup received from the dropdown of assets was used to pay daily margin calls from its trading activities. However, the MLP business model strategy was not planned or designed for the purpose of managing or paying required margins. There is also no evidence that the valuations of the dropdown assets were unreasonable. Fairness opinions from independent, credible entities, and MC and SGLP Board of Director authorizations, were obtained prior to the dropdowns.

The implementation of the MLP business model and the addition of SGLP, a publicly owned company, moved SemGroup away from being a purely privately controlled entity that could be more easily managed by its principals, towards being a more public one that should not have permitted Kivisto's tight control over the Debtors' trading activity, the Westback trades, and Kivisto's other personal business dealings with SemGroup. This evolution magnified the flaws that were inherent in the management of the Debtors' businesses.

F. <u>The Examiner's Conclusions</u>

1. Kivisto engaged in a complex trading strategy that introduced increased risk to SemGroup at the time of an unprecedented rise in the price of oil. There were aspects of Kivisto's trading strategy that made it speculative and which ultimately led to the filing of the Debtors' bankruptcy petitions. Kivisto engaged in mismanagement in this regard.

2. Kivisto tightly controlled SemGroup's trading strategy. He was responsible for hiring Coen and Oven, and he recruited Shimonov, to assist him in implementing his options

trading strategy, knowing that they had little or no prior commodity options trading experience, but could be trusted to do what he directed. Similarly, Allen was chosen as Risk Director although he had no prior risk management experience. Kivisto engaged in mismanagement in this regard.

3. Wallace, Kivisto and Cooper failed to integrate properly the commodities trading function into SemGroup's financial controls, which subjected SemGroup to additional risk. They engaged in mismanagement in this regard.

4. As SemGroup's founders and business leaders from 2000 to 2008, Foxx, Wallace and Kivisto failed to develop a suitable risk management policy or to integrate one into SemGroup's business controls. Further, they failed to comply with the RMP that did exist. They engaged in mismanagement in this regard.

5. At various points in time, members of SemGroup's senior management team (Kivisto, Wallace, Cooper and Mr. Alex Stallings ("Stallings")) were aware that Kivisto was using SemGroup's funds and resources to engage in options trading activity on his own behalf (through Westback), and that such activity had the potential to expose, and did expose, SemGroup to increased risk, yet they failed to stop it. They engaged in mismanagement in this regard.

6. Kivisto, Wallace and Cooper engaged in mismanagement and misconduct by allowing Kivisto to engage in physical commodity trades for SemGroup through Westback, for which Kivisto received additional compensation from SemGroup for activity that was within his normal scope of duties.

7. Kivisto engaged in misconduct by concealing or attempting to conceal the full nature and extent of Westback's relationship with SemGroup from SemGroup's MC and others.

8. Kivisto engaged in mismanagement and misconduct by using SemGroup's resources and its personnel to further his personal, business and financial interests, including Westback, Gallery KH, KN Art Gallery and D'Novo Lean Gourmet.

9. Cooper, and perhaps other SemGroup personnel, engaged in mismanagement and misconduct, by: (A) incorrectly categorizing SemGroup's commodities trading positions in the MtM and Position Reports submitted to SemGroup's lenders, which made the position reports for each affected category incorrect; (B) falsely claiming in MtM and Position Reports that SemGroup personnel had operated within the guidelines of SemGroup's RMP, when, in fact, SemGroup was in violation of its trading limits and its bank covenants on numerous occasions during the reporting periods; (C) submitting data in MtM and Position Reports which did not match the data contained in SemGroup's internal Summary Position and MtM spreadsheets; and (D) submitting at least one false "Borrowing Base Report" on July 11, 2008, which showed that SemGroup had in excess of $72 million of credit available as of July 7, 2008.

10. Kivisto engaged in misconduct and mismanagement, by engaging in, or causing others to engage in: (A) "naked options" transactions; and (B) transactions for his personal benefit, through Westback, an entity he owned and controlled (an "Affiliate," as defined in SemGroup's Pre-Petition Credit Agreement, defined below), all in violation of SemGroup's banking covenants.

11. Kivisto engaged in mismanagement by placing, or causing to be placed, the results of his options trading strategy on the books of other SemGroup business units, including

SemGas, SemFuel, SemMaterials, SemEuro and SemStream, thereby subjecting these entities to increased risk.

12. Kivisto and Wallace engaged in misconduct and mismanagement by approving the semi-annual bonuses paid to themselves and other executives without MC approval, and by personally benefiting from their own decisions in this regard, in violation of their employment agreements.

13. Kivisto, Wallace and Cooper provided inaccurate and misleading information to members of SemGroup's MC that SemGroup's trading activity was supported by its physical inventory.

14. Kivisto, Wallace and Cooper provided false and misleading information to Bank of Oklahoma ("BOK") representatives during their meetings and conversations with them about SemGroup's trading-related activities.

15. Wallace provided false and misleading information to representatives of J. Aron, by claiming that SemGroup's liquidity issues were exaggerated, and that it did not have similar trading exposure with other brokers.

16. Kivisto had a conflict of interest by authorizing substantial bonus payments to Oven (approximately $1.5 million in 2007), a trader he hired with no previous trading experience to assist him in implementing his trading strategy, and someone with whom he had a close personal relationship.

17. Kivisto and Wallace breached the terms of their employment agreements by accepting semi-annual bonuses for themselves that had not been approved by the MC.

18. Kivisto, Wallace and Foxx had a conflict of interest by permitting Ms. Anna Hollinger ("Hollinger"), their outside business partner and a person with whom Kivisto had a close personal relationship, to engage in, and to reap the benefits of, a business relationship with SemGroup. They did so without notifying SemGroup's MC of their ownership interest in the vendor company, or of Kivisto's personal relationship with their co-owner, Hollinger.

G. Potential Causes of Action

The Debtors' estates have potential claims or causes of action including, without limitation, the following:

1. Negligence/Mismanagement:

a. Against Kivisto, for engaging in and controlling a complex options trading strategy that was speculative in certain aspects during the time of an unprecedented rise in and volatility of the price of oil, thereby subjecting SemGroup to increased risk.

b. Against Kivisto, Wallace, and Cooper, for their failure to integrate properly the commodities trading function into SemGroup's financial controls, thereby subjecting SemGroup to increased risk.

c. Against Foxx, Wallace and Kivisto, for their failure to develop a suitable risk management policy or integrate a suitable risk management policy into SemGroup's business controls, and for their failure to comply with the Risk Management Policy that did exist, thereby subjecting SemGroup to increased risk.

d. Against Kivisto, Wallace, Cooper and Stallings, for their failure to stop Kivisto from engaging in trading activity on his own behalf through Westback, thereby subjecting SemGroup to increased risk and losses.

e. Against Kivisto, Wallace and Cooper, for providing inaccurate and misleading information to members of SemGroup's MC that SemGroup's trading activity was supported by its physical inventory.

f. Against Kivisto, for placing, or causing others to place, the results of his options trading strategy on the books of other SemGroup business units, including SemGas, SemFuel, SemMaterials, SemEuro and SemStream, thereby subjecting these entities to increased risk.

2. Fraud/False Statements:

a. Against Cooper, and any other individuals who were involved in the submission of false and misleading reports (MtM and Position Reports and Borrowing Base Reports) and information to SemGroup's lenders.

b. Against Kivisto, for his failure to comply with the covenants of SemGroup's Pre-Petition Credit Agreement.

c. Against Kivisto, Wallace and Cooper, for providing false and misleading information to BOK representatives during their meetings and conversations with them.

d. Against Wallace, for providing false and misleading information to representatives of J. Aron, by claiming that SemGroup's liquidity issues were exaggerated, and that SemGroup did not have similar trading exposure with other brokers.

3. Conversion/Corporate Waste:

a. Against Kivisto, for improperly converting SemGroup's funds and resources to his own use, in connection with his: (i) personal options trading activities through Westback; (ii) other personal business ventures; and (iii) physical commodities trading activity for SemGroup through Westback, his alter ego.

4. Unjust Enrichment:

a. Against Kivisto, for improperly converting SemGroup's funds and resources to his own use, in connection with his: (i) personal options trading activities through Westback; (ii) other personal business ventures; and (iii) physical commodities trading activity for SemGroup through Westback, his alter ego.

b. Against Kivisto and Wallace, for approving the semi-annual bonuses paid to themselves without MC approval, and by personally benefiting from their own decisions in this regard, in violation of their employment agreements.

5. Breach of Fiduciary Duties:

a. Against Kivisto, for depriving SemGroup of his honest and faithful services as an officer and employee, by using SemGroup's resources and its personnel: (i) to engage in personal trading activities through Westback; and (ii) for his other personal business interests, and by making, and causing to be made, false, misleading and fraudulent statements and representations in connection with them.

b. Against Kivisto, for depriving SemGroup of his honest and faithful services as an officer and employee, by engaging in physical commodity transactions through Westback, his alter ego, and receiving additional money from SemGroup for activity that fell within his normal scope of duties, and by making, and causing to be made, false, misleading and fraudulent statements and representations in connection with it.

c. Against Kivisto and Wallace, for approving the semi-annual bonuses paid to themselves and other executives without MC approval, and by personally benefiting from their own decisions in this regard, in violation of their employment agreements.

d. Against Wallace and Cooper, for permitting Kivisto to engage in physical commodity trades for SemGroup, which were within the scope of Kivisto's duties at SemGroup, through Westback, thereby enabling Kivisto to receive additional compensation from SemGroup.

e. Against Kivisto, for authorizing substantial bonus payments to Oven (approximately $1.5 million in 2007), a trader he hired with no previous trading experience to assist him in implementing his trading strategy, and someone with whom he had a close personal relationship.

6. Breach of Contract

a. Against Kivisto and Wallace, for accepting semi-annual bonuses for themselves that had not been approved by the MC, in violation of their employment agreements.

III. THE EXAMINER'S FINDINGS REGARDING THE DEBTORS' TRADING STRATEGY AND THE TRANSFER OF THE NYMEX ACCOUNT

A. Circumstances Surrounding the Debtors' Trading Strategy

1. SemGroup – Background Information

SemGroup was founded in April 2000 and is headquartered in Tulsa, Oklahoma. It provides gathering, transportation, storage, distribution, marketing and other midstream services primarily to independent producers and refiners located from the Gulf Coast of the United States to central Canada, as well as the West Coast of the United Kingdom. Its assets primarily consist of pipelines, gathering systems, processing plants, storage facilities, terminals and distribution facilities located between North American production and supply areas and areas of high demand. It also has storage, terminal and marine facilities at Milford Haven in the United Kingdom. *See* Exhibit 8.

2. SemGroup's Corporate Structure

SemGroup made approximately 64 acquisitions from 2000 until 2008, the offshoots of which resulted in the formation of numerous subsidiaries and related companies. SemGroup had eight primary business segments: SemCrude, SemFuel, SemCanada, SemStream, SemMaterials, SemEuro, and SemGroup Holdings (via its publicly traded MLP–SGLP). *See* Exhibit 8. From a financial perspective, SemEuro, SemMexico and SGLP were standalone companies, with separate bank accounts. *See* Exhibit 9.

SemCrude gathers, transports, stores, blends, markets and distributes crude oil in the United States. SemCrude's sales of crude oil are primarily to refiners and other resellers in various types of sale and exchange transactions. SemGroup utilized an entity known as

Eaglwing, a trading vehicle it owned, to conduct and report trades through SemCrude. Westback, Kivisto's personal trading company, also utilized Eaglwing's services to conduct Westback's trades through SemCrude's account.

SemFuel purchases, ships, stores, markets and distributes refined products in the United States.

SemCanada is an independent natural gas marketing and energy-asset management business in Canada, engaged in gathering and marketing operations, and crude oil marketing and blending operations.

SemMaterials purchases, produces, stores, and distributes liquid asphalt cement products and residual fuel throughout most of the United States and Mexico.

SemStream purchases, transports, terminals, stores, markets, and distributes propane and other natural gas liquids ("NGLs") in the United States.

SemGas primarily acquires and develops storage and gathering pipeline systems for natural gas assets.

SemEuro was established in 2006 as the result of the purchase of the largest storage facility in the United Kingdom.

SemGroup Holdings was formed in July 2007 to hold SemGroup's investment in future MLP entities, initially SGLP. SemGroup Holdings controls SGLP through the ownership of its general partner.

All business segments, except SemGroup Holdings, were included in SemGroup's consolidated financial statements. Each business segment had its own President and accounting section. Each segment, except SemGroup Holdings, conducted its own day-to-day decision making, somewhat independently, with the central coordination of some functions, such as commodities trading and cash management.

Because of its acquisitions and rapid growth, SemGroup always needed to expand its capital base and, therefore, frequently had liquidity concerns. SemGroup's trading strategy in 2007 and 2008, and the unprecedented rise in the price of oil during that period, exacerbated its liquidity problems.

3. SemGroup's Cash Management System

SemGroup employed a centralized cash management system. Cooper, an acquaintance of Wallace and Foxx from college, was the head of SemGroup's Treasury component, which reconciled SemGroup's overall cash flows from its business units.

Kivisto, as SemGroup's main leader, was instrumental in setting its business vision. He also had longstanding relationships with oil producers in the region and maintained them, in part, through commodity purchases and sales. Wallace was responsible for SemGroup's overall financial affairs, while Cooper was responsible for many of its day-to-day financial decisions. Cooper monitored the cash flows among SemGroup's various business units, although they operated with a significant degree of independence and made many of their own decisions. Because of Cooper's health concerns, many financial meetings were conducted in his office. Cooper would utilize two large "white boards" during such meetings to facilitate discussions. The information displayed on the white boards included cash balances, cash needs, cash uses,

sources of cash, margin positions, cash devoted to margin positions, borrowing ability, liquidity and "to-do" lists. Kivisto and Wallace frequently met with Cooper in his office.

Foxx dealt primarily with SemGroup's operating business units. Stallings, with a background as a manager and accountant, was hired by SemGroup in 2003 and held the position of Chief Accounting Officer. Mr. Michael Brochetti ("Brochetti") had a background in the banking industry and was hired by SemGroup in 2005 as its Senior Vice President of Finance. He managed SemGroup's relationships with its creditors and assisted in raising additional loan capital and in negotiating loan documents.

SemGroup's business units had over 60 different bank accounts that were "swept" daily into its main bank account at the Bank of Oklahoma. Distributions and withdrawals were made from SemGroup's centralized bank account as needed.

4. SemGroup's Risk Management Policy (RMP)

a) The Need for Risk Management

As part of its marketing (commodities trading) strategy, SemGroup was involved in the trading of crude oil, refined products such as heating oil and gasoline, natural gas, and NGLs such as propane and other related products. SemGroup traded these commodities on a physical and financial basis and used a variety of instruments to execute transactions, including futures, options, and swaps.

The execution of energy commodity and derivative transactions is an inherently risky activity. It introduces additional risk to trading and requires robust risk management processes and controls.

b) SemGroup's Written RMP

It is unclear precisely when SemGroup's written RMP came into existence, and when it was revised. According to Foxx, SemGroup's RMP came into existence in approximately 2003 as a requirement of its lenders' covenants. According to Stallings, the RMP was implemented as a result of a condition in SemGroup's loan agreement with BNP Paribas, and was copied and adapted, with the involvement of Cooper and others, from a RMP that had been in existence at another company. Stallings did not know if the RMP changed over time, although he assumed that it had been updated. In response to the Examiner's subpoena for all versions of SemGroup's RMP, the Examiner was provided with at least two undated versions. *See* Exhibits 6 and 10. Based upon the content, Exhibit 10 appears to be an older version.

This section of the Examiner's report provides a better understanding of SemGroup's risk management processes and controls with respect to its derivative transactions, and how those processes and controls compare to industry practice.

(1) Governance Structure

The RMP defines SemGroup's RMC as consisting of the CEO, COO, CFO, and the CAO, and appropriate members of its operating subsidiaries. The policy places responsibility for several important risk management activities with the RMC. Such responsibilities include preparing new policies and updating existing policies, and reviewing the principal risks faced by SemGroup and ensuring that appropriate risk management policies are created, implemented and enforced. The RMC is also responsible for approving new products and strategies, and for approving limits governing trading activities. SemGroup's RMP dictates that the RMC should meet at least monthly and is responsible for ensuring that SemGroup operates within acceptable

and defined risk parameters. It is also responsible for monitoring positions, profit/loss and overall marketing strategies. To accomplish these tasks, the RMP states that management should utilize reports such as daily position reports, and daily MtM and Position Reports. The establishment of a RMC is consistent with industry practice, as is making it responsible for the activities listed above.

(a) Deviations from Industry Practice

There are areas regarding governance structure where SemGroup's RMP is inconsistent with industry practice. The RMP dictates that SemGroup's trading policies are to be approved by the CEO "subject to the Board of Director's overall risk management approval." Additionally, the RMP states that the RMC reports to the CEO. Industry practice holds that the RMP should be approved by the board of directors and that the RMC should report to an audit committee. In the absence of an audit committee, the RMC should report to the MC. Failure to have a proper risk management structure creates what are known as "segregation of duties" issues. Segregation of duties issues are somewhat analogous to conflict of interest issues. In the case of SemGroup, the CEO and head trader were the same person – Kivisto.

Mr. Don Spaugy ("Spaugy"), SemGroup's Vice President of Financial Services, was asked during an interview if, based on his experience, it was unusual for SemGroup's CEO to establish its RMP and to dictate its trading limits and strategies. Spaugy responded by stating that he found it very unusual, and that he was frequently compelled to address this question when outside agencies reviewed the company's operations. Spaugy stated that, since he was uncertain how to best answer this question, he would frequently state that Kivisto would only act in the best interests of the company because he owned 25% of it.

The RMP allowed Kivisto, the CEO, to approve a policy that allowed him, as the head trader, to take on more risk than the MC may have been comfortable with at the time. Essentially, because of the power he had from the RMP as CEO, and because he was also SemGroup's head trader, Kivisto was in position of oversight of himself. He was in a position to approve his own trading behavior and that of others.

The RMP states that, in cases where position limits are exceeded, the Treasurer informs the CFO and the CEO, who then decide on a case-by-case basis the appropriate course of action. This type of trading governance structure goes against industry practice because of the risk that a person may self-approve activities that could be inconsistent with overall corporate objectives, and thereby cause the company to be exposed to undue financial risks.

(2) Trading Instruments

In addition to approving positions that introduce fixed price exposure, SemGroup's RMP discusses three general spread strategies – time spread, commodity spread, and basis spread – that are used "to minimize market risk while attempting to optimize arbitrage and fundamentally driven market opportunities." Consistent with industry practice, the RMP lists approved trading instruments used to execute the strategies, including physical forwards, futures, over-the-counter ("OTC") and exchange-traded options, and swaps. Additionally, the RMP sets volume, spread and stop-loss limits with the intent that they be used to manage the risk of the trading activities.

(a) Deviations from Industry Practice

Although the listing of approved instruments in the RMP is consistent with industry practice, the language in SemGroup's RMP regarding the sale of options is inconsistent with

industry practice. The RMP allows for the purchase of OTC and exchange traded options, but states, in two different locations in the RMP, the following: "As a seller of options, SemGroup faces significant market risk. *Therefore it is SemGroup's policy not to sell naked options*." (Emphasis added). However, SemGroup's RMP allows for the sale of options to offset other positions or as "part of a defined marketing program approved by the CEO." These exceptions to the rule against naked options sales are poorly written and provide for a great deal of discretion on the part of traders and the CEO. SemGroup's RMP does not define a set standard for identifying the specific positions against which the sold options are intended to offset. Nor does its RMP limit in any way the types of positions against which options sales would be approved. Further, it does not demand that the position and the offsetting option be of like commodity, location, or time period. For example, under the first exception, a trader would be allowed to sell a June call option on North Sea Brent crude oil to "offset" an inventory of number 2 low sulfur diesel held at Green Bay, Wisconsin. Industry practice would have the risk policy define which commodities and instruments are allowed to offset others.

Additionally, SemGroup's RMP seems to allow for the sale of naked options as long as it is part of a defined marketing (commodities trading) program approved by the CEO. Coen indicated that Kivisto's trading strategy included the sale of naked options and that the RMP allowed for options sales as part of a defined CEO strategy. However, Kivisto's trading strategy, as communicated in interviews with Oven, Shimonov, and Coen is *not* defined in SemGroup's RMP. Given that the CEO, Kivisto, was the head trader, and that his trading strategy included the profligate use of options, the RMP, as it relates to the sale of options, provided ambiguous guidance, at best. *It is clear, however, that naked options sales are prohibited by the Bank of America ("BOA") Pre-Petition Credit Agreement*. Industry practice would seek to more

narrowly and specifically define the situations in which options sales would be approved and would not allow blanket exceptions to RMP provisions, as was the case with SemGroup's RMP.

(3) Trading Limits

Limit monitoring is a common control used to manage open volumetric positions and dollars associated with derivative transactions within a portfolio. Many industry participants monitor positions with respect to limits such as profit & loss, volume, tenor, value-at-risk ("VaR"), and counterparty credit. Industry practice holds that well-defined limits should be set to control the financial risks to a company arising from trading activity. SemGroup's RMP establishes a "cumulative stop-loss" limit as well as a daily stop-loss limit. Further, it establishes outright position and spread position volume limits. SemGroup's RMP sets volume limits by trader and states which commodities may be transacted by each trader. These limits are detailed on pages 9-11 of the RMP. *See* Exhibit 6. These limits are also incorporated in Schedule 7.13-1 of the Amended and Restated Credit Agreement, dated as of October 18, 2005 (as amended, the "Pre-Petition Credit Agreement"). *See* Exhibit 11.

(a) Deviations from Industry Practice

Although SemGroup established limits as part of its RMP, the limits it set were not in line with industry practice, for many reasons. First, the RMP states that "the CEO establishes risk limits with input from the RMC." Industry practice dictates that an oversight committee should establish risk limits with input from the trading organization. This is another example of an area where Kivisto's dual responsibilities as a trader and as a CEO conflict. Next, the calculation of the "cumulative stop-loss" limit fails to provide insight into the financial performance of the trading function and fails to curb additional losses, contrary to the usual

intended purpose of such a limit. The daily stop-loss limit is ineffective as defined. The calculation of the outright and spread position limits improperly categorizes commodities positions for inclusion in reports. Also, the outright and spread positions do not consider concentration risk or whether spread positions are adequately aligned with company strategies.

As a control, SemGroup calculates a cumulative stop-loss value and compares this value to a policy limit. The creation of a cumulative stop-loss limit is consistent with industry practice, and the stated basis for the SemGroup cumulative loss, 20% of a net available working capital value of $200 million, is accepted as well. The general purpose of such a limit is to allow company management to specify its loss appetite, which is usually the maximum amount of trading losses it is willing to incur. The inclusion of policy limits in the Pre-Petition Credit Agreement indicates that the lenders relied upon these limits to restrain trading activity to within a defined comfort level. Normally, the stop-loss calculation takes into account realized and unrealized gains and losses over a specified time period. If the value of that calculation reaches the policy-defined limit, trading personnel are forced to reduce or eliminate their trading positions.

Although a calculation is not specifically defined in SemGroup's RMP, in practice, its cumulative stop-loss value is calculated as the difference between the current MtM value and the MtM value as of the beginning of the most recent four quarter period, *plus* net gains or losses from transactions that have been settled since the beginning of the most recent four quarter period, *plus* net premium dollars paid or collected since the beginning of the most recent four quarter period, *plus* net premium dollars paid or collected prior to the most recent four quarter period for options that had yet to expire as of the beginning of the most recent four quarter period. SemGroup's RMP language inaccurately describes this metric when it states "[w]hen the

MTM reaches the pre-determined loss limit. . . ." The previous statement infers that the cumulative stop-loss limit is purely a MtM value, when it is not.

The RMP also fails to mention that option premiums are included in the cumulative stop-loss calculation. *The inclusion of option premiums collected defies industry practice because the inclusion of premiums collected through the sale of options provides traders with a mechanism to conceal realized or MtM losses*. SemGroup's calculation allows traders to offset losses simply by selling options and generating income from premiums. When experiencing a large MtM loss, SemGroup traders would have been able to maintain compliance with the cumulative stop-loss limit through the sale of large quantities of options. *See* Exhibit 12. While options transactions may serve legitimate business needs, the sale of options for the purpose of collecting premiums may introduce adverse market risk, and provides traders with an incentive to do so.

Footnote 2 of Schedule 7.13-1 of the Pre-Petition Credit Agreement states: "Note: a large length/shortness is ultimately controlled by the Stop-Loss limits." *See* Exhibit 11. However, the inclusion of options in the cumulative stop-loss calculation may reduce the effectiveness of the limit as a control. Stop-loss limits should serve to prevent further losses, not allow the compounding of current losses with the introduction of more risk. The methodology for calculating the cumulative stop-loss value should have been specifically defined in SemGroup's RMP, and the inclusion of option premiums collected allowed for the inaccurate portrayal of the true financial condition of SemGroup's trading operation. *See* Exhibit 13.

SemGroup's RMP also sets daily stop-loss limits. While the RMP fails to define the calculation of the limit, information gathered from interviews indicates that the limits were calculated as the change in the MtM value from two business days prior as compared to the

previous days' MtM value. The design of this limit provides, at best, limited benefit to SemGroup as a risk management tool. Because the limit is calculated by looking back, it does not help to prevent trading losses, since it is impossible to change events that have already transpired. Accordingly, and as Coen acknowledged, SemGroup's traders were never affected by the daily stop-loss limit.

SemGroup's RMP does not define how it aggregated the position volumes for limit testing purposes. It appears from the MtM and Position Report that SemGroup aggregated the position values from each entity for each forward month for each limit category and presented this as the position value to be compared to the RMP limit. However, a deeper examination of the aggregation methodology revealed inaccuracies. Further, the methodology SemGroup used may allow for the incorporation of greater risk into the trading portfolio than intended, by allowing for concentration risk and positions that contradict stated trading strategies.

BOA has provided its position regarding the MtM and Position Reports required of and submitted by SemGroup. BOA's view is that the Pre-Petition Credit Agreement required the position reports to be submitted to the banks every Friday, and for the reports to contain position information as of the preceding business day (Thursday). BOA believed that a positive figure in the position column of the report indicated that SemGroup had that quantity of unhedged product on hand. However, even though the position column of the reports appeared to indicate the sum total volume of all commodities transactions executed for that category, a positive value in the position field of the report did not necessarily indicate that SemGroup had that quantity of the commodity on hand, in tank storage, unhedged. A positive value in the position field could simply indicate that SemGroup had a larger volume of derivatives purchases than sales for future months.

Additionally, an examination of the aggregation of positions for inclusion in the MtM and Position Report showed that commodities positions were incorrectly categorized. For example, the "US & Canada Crude/Asphalt (Bls)" category does not include crude oil positions from the SemStream and SemFuel entities. Additionally, this category contains domestic natural gas positions from SemCrude, SemGas, and SemMaterials. Also, the "Domestic NGL" category contains crude oil positions for SemStream as well as domestic natural gas positions for SemStream. The "SemFuel Outright Position" includes crude oil positions from that entity. Also, the "Domestic Gas (MMBtu)" category contains no positions from any entity. *These categorization inaccuracies make the positions reported for each affected category incorrect and, thus, diminish the usefulness of the position limits as controls*. The data and formulas for aggregating the positions into position limits categories were provided by SemGroup.

The outright and spread position limits established by SemGroup in the RMP do not account for concentration risk in any single month, and allow for positions that may be contrary to stated corporate trading strategies. For example, assume the risk policy of Company A had an outright position limit of 12 million barrels of crude and Company A had only executed transactions for five months – months 1, 2, 3, 4, and 5. Assume that the position values for months 1 through 5 are negative 36 million barrels, 1 million barrels, 1 million barrels, 1 million barrels, and 21 million barrels. The aggregate position would be negative 12 million barrels (-36+1+1+1+21), a position in compliance with the outright limit. However, because of the way the position is aggregated, Company A fails to monitor adequately the increased risk brought about by the concentration positions in months 1 and 5. Because SemGroup aggregated positions in the same manner as this scenario, the volume limit established by its RMP allowed SemGroup to sell a greater volume of crude/asphalt than could be stored in its storage tanks.

SemGroup also set spread limits. But, again, SemGroup did not define the methodology for calculating a spread position for comparison with a policy limit in its RMP. To calculate a spread position, SemGroup summed the volumes in each limit category for each entity for forward months with a positive volume position, summed the volumes in each limit category from each entity from forward months with a negative position, and compared the absolute value of each sum. The sum with the lowest absolute value was used as the spread position in that spread limit product category for that entity. The spread positions from each entity were then summed for comparison to the spread position limit for each category. When calculating a spread position, SemGroup incorrectly categorized products in the exact same manner as described previously for outright positions. This information regarding aggregation was gained from a review of the SemGroup internal documents.

Using the same hypothetical example as demonstrated for the outright position limits, the spread position would also be in compliance with SemGroup spread limits. Thus, the methodology used by SemGroup to calculate spread positions also failed to address adequately concentration risk. Additionally, SemGroup's RMP does not direct that spread positions coincide with stated trading strategies such as contango or a summer propane build. Correspondingly, the methodology used by SemGroup for calculating both outright and spread position limits would not reveal that a position was unsuitable for a contango or summer propane build strategy, although Footnote 3 of Schedule 7.13-1 of the Pre-Petition Credit Agreement states the intent of the outright limit for the NGL (barrels) category: "Allows for cyclical summer inventory builds/draws to meet winter demands." *See* Exhibit 11. Industry practice indicates that a company should specifically define methodologies for limit testing in its RMP.

Also, it should establish limits that fully consider all risks, and design limits and limit-testing methodologies that accomplish the intended purposes.

Finally, the volume limits set by SemGroup's RMP for each trader represent per transaction limits. This type of limit definition fails to control adequately trader activity. For example, if a trader with a per transaction limit of 25,000 units wanted to transact 100,000 units, the trader would merely need to execute four separate transactions of 25,000 units each in order to comply with the policy limit. In order to control effectively volumes executed by each trader, industry practice holds that a company should set an overall position limit, a daily aggregate volume limit, an aggregate position limit for the appropriate time period, or an aggregate position limit by product or region. Setting per trader limits is consistent with industry practice, but the per transaction limits listed in SemGroup's RMP are not effective as written. Additionally, the RMP allows traders to exceed the per trader policy limits after discussion with and approval from the CEO – Kivisto – or the President of the business unit.

(4) Risk Analytics and Reporting

(a) Deviations from Industry Practice

Industry practice suggests that companies involved in commodities trading specifically define methodologies for calculating various risk factors as well as formats for reporting those risks. Considering the large volume of options executed by SemGroup traders, SemGroup's risk analytics and risk reporting were inadequate. The most widely circulated report was a position report that showed SemGroup's various commodities positions versus internal limits as defined in the RMP, as well as the aggregate MtM and MtM for each entity. This report failed to sufficiently communicate the risks inherent in the trading portfolio because it provided delta-

adjusted positions and did not provide insight into other risks due to market factors, such as volatility. Anyone wanting to gain a comprehensive understanding of the risks imbedded in the SemGroup portfolio would not have been able to do so from this basic position report, which was distributed daily to traders and management and, in a simpler form, weekly to the banks. Although other risk analytics were performed, traders questioned their accuracy and they were not distributed to all stakeholders.

When reporting outright position limits and spread position limits, SemGroup personnel reported delta-adjusted positions. While not against industry practice, when a portfolio contains options, the delta-adjusted approach fails to consider fully the potential for increased position size created by market price movements or the volatility of market price movements. SemGroup's brokers would calculate the deltas on options daily and communicate that information to SemGroup in the daily broker statements. In order to calculate a position for comparison with a limit, SemGroup would multiply the volume of an options contract times the delta as provided by the broker. For example, if SemGroup sold 100 contracts worth of NYMEX crude oil call options and the broker indicated that the delta on those option contracts was .25, SemGroup would report a sale position of 25,000 barrels for use in calculating position limits. (Each sold NYMEX contract is for 1,000 barrels times .25, which is the probability of exercise, which equals 25,000 barrels). An analysis demonstrates that a delta-adjusted position can be vastly different than a position that includes the total notional volume of all contracts. *See* Exhibit 14.

Due to the nature of options contracts, a company selling naked call options may face increased financial risk arising from its position as the market price rises sharply and becomes more volatile. Under such market price movement scenarios, the delta-adjusted methodology

used by SemGroup for calculating positions to be included in the MtM and Position Report would not depict adequately the true potential position of the company and, correspondingly, would not portray adequately the true risk of the portfolio. *Because of the increased complexity of options activity, companies usually employ more sophisticated tools to calculate risks from options contracts*, such as VaR. These calculations help traders and management to understand the potential portfolio risk created under various market conditions. VaR calculations take into account commodity risk factors such as volume, price, volatility and correlations and run thousands of scenarios to help understand portfolio risk. *Companies executing large volumes of options transactions also tend to purchase sophisticated software systems specifically designed for such a purpose.*

In March 2007, Allen was promoted to the newly created position of "Risk Director." The risk management function had previously been the responsibility of Cooper. Stallings recommended that Allen and Alisa Perkins ("Perkins") be transferred to Risk Management because Cooper appeared to be overworked, and due to his health issues. However, Perkins was made Assistant Treasurer instead.

Allen had no previous commodities trading experience prior to assuming his new position. Stallings stated that he was unsure if Allen was ever able to tie SemGroup's financial position to its physical inventory. Mr. Terrence Ronan ("Ronan") stated that he considered Allen a "risk monitor." Although Allen held the position of Risk Director, it was Foxx's opinion that Allen had neither the authority nor the courage to question directly Kivisto regarding Kivisto's trading strategy. Brochetti echoed this view, and opined that Allen was handicapped by both a lack of knowledge and a fear of confronting Kivisto. He stated that, as a practical matter, Kivisto monitored risk, and, in essence, Kivisto was the Risk Manager for both SemGroup and himself.

Coen did not believe that Allen had the authority to compel compliance with risk limits or to administer ramifications for non-compliance. *Coen stated that there was no compliance function at SemGroup*.

According to Coen, if Allen identified that position limits were exceeded in a day, the information would be communicated to the traders who would then confer with each other and take action to bring their positions back within limits. Coen believed that Allen would also advise Kivisto when a limit was reached. According to Foxx, although Allen was required to track the daily trading numbers, he doubted that Allen would take any action except to notify Cooper if the trading losses were inordinately high, with the hope that Cooper would share the information with Kivisto.

The vast majority of SemGroup's personnel did not see, and were, at best, only vaguely familiar with, SemGroup's RMP. Coen had a copy of it sent to him on July 1, 2008, shortly before the Debtors' bankruptcy petitions were filed (he received it as an attachment to an e-mail from Cooper). Although Mr. Darrell Weakland ("Weakland"), another trader, assumed that SemGroup had a RMP, he never saw it. Weakland was unaware that the RMP had a trading limits requirement. Shimonov stated that he was unaware there was a RMP, and that he never observed a written RMP. He was also unaware of the existence of SemGroup's RMC. Shimonov also stated that he did not believe Allen knew very much about Risk Management, and that he was trying to learn aspects of it on the job. It was Shimonov's belief that Cooper continued to be more engaged in assessing daily risk than Allen. *SemGroup's RMP was never integrated into SemGroup's policies and procedures and its day-to-day trading decisions*.

In February 2008, Allen began to perform an analysis called the "Delta Swing Analysis." This analysis attempted to quantify the change in the delta of certain SemGroup commodity positions with the upward or downward change in the market price of each commodity. However, this analysis did not consider the increase in market volatility as a risk factor, and consequently, did not anticipate the consequences of extreme market price moves. The maximum oil price movement considered by this spreadsheet analysis was a $5.00 movement, upward or downward. While the spot price of NYMEX crude exhibited a daily move greater than or equal to $5.00 on only nine occasions from January 2007 through July 2008, the price rose from approximately $50 in January of 2007 to $145 in July 2008. The delta swing analysis did not anticipate such a move. Additionally, the delta swing spreadsheets considered only trades based through NYMEX brokers and did not include OTC trades.

Allen also created other spreadsheet analysis tools that were intended to help SemGroup traders and management understand the financial impact on the company due to market price movements. Allen generated what were referred to as "stress tests." These "Stress Risk" or "Price Shock" reports calculated the gain or loss on SemGroup's portfolio given incremental positive and negative changes in the market prices of commodities such as crude oil, heating oil and reformulated gasoline. *See* Exhibit 15. These analyses were not created prior to January 30, 2008, and were not performed regularly until April 2008. Beginning in June 2007, Allen also generated "Risk Graph" spreadsheets that demonstrated the profit and loss effects of upward or downward price movements by +/- 20%. The "Risk Graphs" showed the "payoff" of positions held in each commodity and by the positions held at each broker. However, a price move of 20% when the price of oil is $50, as it was in January 2008, represents a $10 move. Again, the spot price of NYMEX crude moved from around $50 in January 2008 to above $140 in July

2008. Clearly, the analyses generated by Allen did not demonstrate the financial effects on SemGroup of extreme and prolonged price movements. Additionally, Coen stated that the traders struggled with the accuracy of the in-house tests performed by Allen.

Spaugy indicated that he was involved in a series of stress tests that had been run by JP Morgan on the various positions held by SemGroup. Spaugy stated that the results of the stress tests run by SemGroup and J.P. Morgan differed, causing JP Morgan to become uncomfortable with its relationship with SemGroup.

SemGroup traders have acknowledged in interviews that the failure to fully incorporate volatility as a risk factor was a mistake. Oven admitted that up until May 2008, volatility as a risk factor was not considered by SemGroup traders or risk management. Oven stated that it was "not on the radar." Coen admitted that volatility wasn't focused upon as much as it should have been, and that it was only after the Debtors' bankruptcy petitions that SemGroup calculated the effects of volatility on a daily basis.

SemGroup's RMP failed to address adequately areas relevant to the calculation of risks associated with options trading and failed to instruct that such risks must be communicated to all stakeholders. Additionally, SemGroup failed to calculate sufficiently the risks of the trading portfolio because it did not possess the tools normally employed by companies involved in options trading. This failure to calculate properly the risks of the portfolio prevented the adequate communication of those risks to stakeholders such as traders, management, and banks.

(5) "Dealing for Your Own Account" Prohibition

Section 4.4 of SemGroup's RMP states that "Deal makers shall comply with the provision prohibiting deal makers to market energy commodities for their own account." *See* Exhibit 6. Industry practice mandates that traders execute transactions solely for the benefit of the employer, so this policy is consistent with industry practice. Such prohibitions seek to minimize the risk that a trader would personally profit from commodities transactions to the detriment of the employer. Kivisto's name is the first name appearing on page 10 of the RMP under Section 3.5, "Deal Maker," so it is clear that he is bound by Section 4.4. *Id.*

From a review of transaction data, Kivisto did not execute any transactions during the 2007 - 2008 timeframe for any SemGroup entities. However, Oven and Coen both stated that they acted at the direction of Kivisto and entered into commodities transactions for Westback (also known as "Eaglwing 2") from January 2007 through early 2008. Additionally, there are multiple e-mails that clearly demonstrate that Westback had a commodities trading account through Newedge Financial, Inc. ("Newedge"). An e-mail dated June 16, 2008, titled "6/16 Confirm," is an example of a communication between Kivisto and Steffen van Keppel, a representative of Newedge, about the Westback trading account. *See* Exhibit 16. These e-mails demonstrate that Kivisto was actively trading in the Westback Newedge account. Kivisto's activities in this regard were in violation of SemGroup's RMP.

(6) Risk Management Committee (RMC) Meeting Requirement

SemGroup's RMP mandates that the RMC meet regularly. All SemGroup personnel who were interviewed, including Foxx, Allen, Stallings, Brochetti, Oven, Shimonov and Coen, stated that they did not remember a single RMC meeting ever being held. No RMC meeting minutes

have been found in SemGroup's documents. Many of SemGroup's employees, such as Coen, were unaware that a RMC even existed, and others, such as Brochetti, were unaware of the members of the RMC. SemGroup's management and personnel failed to comply with the RMP requirement that meetings be held as needed, but at least once each month.

(7) Policy Acknowledgement

Industry practices dictate that a risk policy contain an acknowledgement that is to be reviewed and signed annually by company personnel involved in the trading activities. By signing the acknowledgement, employees are verifying, among other items: (1) an understanding of their responsibilities as explicitly delineated in the policy; (2) a commitment to full compliance with risk management governance documents; (3) that they have no knowledge of current violations; (4) an agreement to report any future policy violations; and (5) an understanding that violations may be grounds for sanctions, up to and including employee termination.

(a) Deviations from Industry Practice

SemGroup's RMP includes a statement mandating that all relevant personnel read it at least annually, and any updates as received. However, SemGroup's RMP does not require an acknowledgement as described above. The failure to include such an acknowledgement requirement is inconsistent with industry practice.

(8) Compliance Function

(a) Deviations from Industry Practice

Industry practice dictates that limits and other provisions must be enforced for a risk policy to be effective at managing the financial risk of the company arising from the participation in commodities markets. There should also be defined consequences for policy breaches and a defined process for communicating and memorializing policy breaches and subsequent resolution. SemGroup's RMP states that the RMC "ensures appropriate risk management policies are created, implemented, and enforced." To this end, the RMP states that SemGroup's "administrative group, supervised by the CFO, is responsible for monitoring, controlling, and reporting risks." Although the RMP does not define the role, SemGroup later employed Allen as its Risk Manager. From the interviews that have been conducted, Allen and other people in SemGroup's Treasury group monitored and reported risks by generating MtM and position reports and other ad hoc reports, such as stress tests.

However, Allen described himself as more of a risk reporter than a risk "cop." While the limits in the MtM and Position Report were violated 335 times in 2007 and 214 times in 2008, no documentation has been reviewed which demonstrates that these violations resulted in any specific consequences.

The Examiner analyzed these risk limit violations by comparing SemGroup internal documents to the MtM and Position Reports which were generally signed by Cooper, and provided to SemGroup's banks. *See* Exhibit 17.

The Examiner noted three instances in which the data in the MtM and Position Reports from January 4, 2007 to June 27, 2008 did not match the data in the Summary Position and MtM spreadsheets, as detailed in the chart below. S*ee* Exhibit 18.

Date	Category	MTM Report	MTM Spreadsheet	Difference
1/12/2007	Canadian Gas Spread Position	$ 20,487,746.00	$ 20,586,779	$ (99,033)
11/29/2007	Cumulative Stop-Loss	219,902,300	243,097,521	(23,195,221)
6/12/2008	Daily Stop-Loss Limits Combined	9,334,251	24,368,826	(15,034,575)

The MtM and Position Reports were to be submitted to BOA every week on Friday, and were meant to reflect Thursday's trading data. This was a requirement of the Pre-Petition Credit Agreement. However, a review of these weekly reports revealed multiple weeks when they did not reflect data from the expected Thursday. The reports which did not reflect Thursday's data would either reflect Friday's data (17 occasions) or Monday's data (2 occasions). It is possible that the reports which reflected Friday's data could have been sent to the banks on time (by close of business Friday), but reflected data from the wrong day. However, the instances in which Monday's data was reported would have clearly been sent in late. In all cases, however, SemGroup was in violation of its trading limits on Thursday, but was back within its limits on the Friday or Monday dates referenced in its reports. The number of times when MtM and Position Reports appear to have been delayed, and in which SemGroup was in violation of its trading limits on the Thursday in question, are shown below:

	2007	2008
Submitted Data Delayed	12	7
Over Limit on Proper Due Date	12	7

The last MtM and Position Report sent to BOA was on Friday, June 27, 2008. This was the last date on which SemGroup was in compliance with its trading limits. SemGroup exceeded its trading limit for the Cumulative Stop-Loss from July 1, 2008, forward. Since SemGroup was never able to get back within its trading limits, it never sent another MtM and Position Report to the banks.

Additionally, the following represents a breakdown by year of the number of days and number of overall occurrences in which SemGroup was in violation of its trading limits[3]:

	Days with a Violation in 2007	Number of Violation Occurrences in 2007	Days with a Violation in 2008	Number of Violation Occurrences in 2008
Positive Violations Only[4]	98	160	72	121
Positive and Negative Violations[5]	153	335	97	214

The loan covenants that SemGroup had with its banks pursuant to the Pre-Petition Credit Agreement were less strict with respect to trading limits than the limits SemGroup imposed upon itself. The loan covenants note that "Daily Stop-Loss Limits Combined" must be greater than negative $32.8 million. The loan covenants allow room for SemGroup to exceed its limit with its

[3] Footnote (2) of Schedule 7.13-1 of the Pre-Petition Credit Agreement indicates that short positions are allowed: ". . . a large length/shortness is ultimately controlled by the Stop Loss limits." See Exhibit 11. This language implies that the position limit for crude oil is not only 12 million barrels on the plus side, but also minus 12 million barrels on the down side. Thus, under the terms of the Pre-Petition Credit Agreement, SemGroup was prohibited from having an aggregate crude oil length position of greater than 12 million barrels, and also prohibited from having an aggregate short position larger than negative 12 million barrels.

[4] A positive violation indicates when SemGroup breached the position limit by having a larger long (purchase position than allowed under the Pre-Petition Credit Agreement (i.e. a position of 13 million barrels).

[5] A negative violation would be incurred when SemGroup breached the limit by having a larger short (sales) position than that allowed under the Pre-Petition Credit Agreement (i.e. a position of negative 13 million barrels).

Domestic crude or Canadian crude as long as the "Combined" account is within the proper limits. The following information was revealed by factoring in the situations in which SemGroup exceeded its trading limits in either Domestic or Canadian crude but was still within the "Combined" limit:

	Days with a Violation in 2007	Number of Violation Occurrences in 2007	Days with a Violation in 2008	Number of Violation Occurrences in 2008
Positive and Negative Violations	118	300	76	183

See Exhibit 18 for a detailed breakdown by category of the number of RMP trading limit violations that SemGroup incurred during 2007 and 2008.

Foxx admitted that SemGroup may have relied on third parties (auditors, lending officers, etc.) to monitor its risk. Ms. Jamie Cooper ("Jamie Cooper"), SemGroup's Treasury Analyst, who prepared reports comparing SemGroup's previous day positions to its position limits, could not recall any enforcement of trader compliance with SemGroup's trading limits. Additionally, there is no documentation that demonstrates that SemGroup's trader "per transaction" limits were monitored at all. SemGroup's RMP also fails to define the methodology for enforcing such limits. Instead, the policy states that "[w]hen position limits are exceeded, the Treasurer informs the CEO and CFO. The CEO will determine the appropriate course of action, on a case-by-case basis. . . ." *See* Exhibit 6 at Section 3.3.

Industry practice does not allow for a trader to decide what course of action should be taken in cases of limit violations. Industry practice holds that a compliance group should be completely independent of the trading function. Traders may have input into the course of

action, but should not be the decision makers. The RMP should have a defined course of action for a variety of violations and all violations and remediation activities should be documented.

While SemGroup's RMP may be comparable with risk policies from other companies that purchase, transport, store and market crude oil and other related commodities, it is inadequate in comparison to the risk management policies of other companies who transact similar volumes of options or engage in intricate options trading strategies. SemGroup's RMP was insufficient to properly govern the risks arising from its options trading.

(9) Comments Regarding SemGroup's RMP/Written RMP

(a) SemGroup's Management Committee (MC)

SemGroup's MC consisted of the following individuals during portions of 2007 and 2008: Mr. Andrew Ward ("Ward"), Mr. Bartow Jones ("Jones") (Ward and Jones were the MC designees of Riverstone Capital), Mr. Thane Ritchie ("Ritchie") (Ritchie was the MC designee of Ritchie Capital Management ("RCM"), Messrs Foxx, Wallace and Kivisto. The MC met most frequently by telephone conference.

(i) Thane Ritchie

Ritchie stated that after he joined the MC in April 2006, there were perhaps two meetings per year for 2006 and 2007, and that most meetings were for the purpose of approving acquisitions. Meeting dates and activities which required MC approval were documented in Memorandum of Action ("MOA") resolutions. A review of the MOAs prepared for the MC meetings from January 2007 to July 10, 2008, did not reveal any documented discussion of any

trading issues at SemGroup. Nor did they reflect the MC's review of, or revision to, SemGroup's RMP.

Ritchie stated that he did not remember the subject of SemGroup's written RMP coming up during RCM's due diligence (2003-2004), when RCM was evaluating whether to invest in SemGroup. Ritchie did not recall ever seeing a copy of SemGroup's RMP until July 2008, after the formation of the special committee. Ritchie did not recall reviewing it prior to investing, because he was told that all SemGroup trading was hedged against physical inventory.

(ii) Andrew Ward

According to Ward, there were no formal mechanisms in place to ensure that the MC monitored SemGroup's compliance with its RMP. However, Ward stated that he and the other non-management members of the MC had frequent contact with SemGroup's management, and that no one ever raised any problems to the MC regarding SemGroup's trading activity. Ward stated that he frequently inquired of management whether all of SemGroup's trading positions were back-to-back, that is, whether they were supported by physical inventory, and he was consistently advised that they were so supported.

Ward stated that he recalled reviewing and approving changes to SemGroup's RMP while he was a member of the MC, including approving using hedges on trading transactions to protect against large movements in commodity prices, a strategy which was referred to internally as "wings." Ward described "wings" as a tool for hedging against risk as commodity prices increased significantly and the standard commodity-trading band got wider. If there was a big swing in the price of oil in that instance, Ward stated that SemGroup would have a low cost "out-of-the-money" option as protection.

The MC received the same weekly positions reports (MtM and Position Report) required under the terms of SemGroup's Pre-Petition Credit Agreement that were sent to the bank syndicate. Ward recalled that these reports were usually signed by Cooper, although they were occasionally signed by Brochetti and, on one occasion, by Ronan. The position reports contained, among other things, a signed certification that SemGroup was in compliance with its RMP ("Since the last submitted positions report, all Restricted Persons have operated within the guidelines of the Company's Risk Management Policy"). According to Ward, the MC relied upon those certifications and did not independently verify the contents of the position reports. Ward stated that he believed the position reports were accurate prior to the Debtors' bankruptcy filings, but he now believes that they were inaccurate.

(iii) Bartow Jones

Jones stated that SemGroup's RMP and its agreements with creditors precluded speculative trading. He advised that this issue was specifically addressed during Riverstone's due diligence investigation, because Riverstone was not interested in investing in a company that took speculative positions. SemGroup managers consistently advised Jones and other non-management members of the MC that SemGroup was using a back-to-back hedge policy, which meant to Jones that SemGroup did not hedge more product than it actually owned. SemGroup was required to provide weekly "position" reports to the banks, and Riverstone received copies of them. These reports certified that SemGroup was not violating its RMP, which required back-to-back trading, or, in other words, trades that were backed by physical inventory.

(b) Capstone Advisory Group, L.L.C.

Capstone Advisory Group, LLC ("Capstone") was retained on or about July 12, 2008, by BOA to review the financial status of the Debtors in connection with their request for Debtor-in-possession ("DIP") financing. In connection with its duties, Capstone reviewed SemGroup's RMP within days of being retained, and made preliminary observations after its review.

Capstone observed that, while the RMP had some weaknesses, it was fairly standard for a company that engaged in physical commodities trading and had a hedging policy. The primary shortcoming of SemGroup's RMP, in Capstone's view, appeared to be its lack of accountability, or checks and balances, since all risk management decisions were ultimately made by Kivisto, SemGroup's CEO and head trader. Capstone further noted that, while a RMC is generally composed of independent board members, SemGroup's RMC included its management personnel.

Capstone concluded that the only centralized risk function in SemGroup's RMP was the RMC. According to its RMP, the RMC was responsible for (1) approving comprehensive trade limit structures, new products and new marketing strategies and (2) ensuring that SemGroup operated within risk parameters and monitored its positions, profit and loss and overall marketing strategies.

Capstone noted that SemGroup's RMP prohibited deal makers from (1) entering into transactions for their own account; (2) selling valued options, unless to offset other positions or as a part of a defined marketing program approved by the CEO (Kivisto); and (3) engaging in speculative trading. Capstone noted that, while the genesis of the language in SemGroup's RMP

permitting trading activities that are part of an "approved marketing plan" was unclear, it seems to have been designed to give Kivisto a large degree of discretion.

Capstone further noted that SemGroup's RMP contemplated decentralized risk control, where managers/dealmakers were responsible for controlling risks. Also, while some of SemGroup's business lines used different trade capture systems, the decentralized trade capture systems were aggregated at the corporate level. However, some of the transactions did not appear to be aggregated properly per management.

A Capstone representative also spoke with Oven and Coen. Both traders told him that they had no options trading experience prior to being hired as traders at SemGroup and that Kivisto personally provided all of their training in that regard. Both of them stated that they were aware of the existence of SemGroup's RMP. Although the traders did not indicate to Capstone that they knew they were violating the RMP, Capstone believed, based upon its review of the RMP, its discussions with Coen and Oven, and its examination of some of the positions that Coen and Oven showed to it during their meeting, that they must have known they were not hedging commodities, and were trading in financial options instead.

(c) Bank of Oklahoma (BOK)

A representative of BOK's Risk Management Department stated that he had seen SemGroup's written RMP. The representative stated that, from a conservative analysis, he would have wanted to see other, smaller trading limits with more levels of authority in SemGroup's RMP. He also stated that there was a pronounced lack of independence for overrides (Kivisto, as CEO, had the authority to override and perform trading), and that having the CEO on the RMC was not a good risk management concept.

(d) James Bowen (May 2007 Report)

Mr. James Bowen ("Bowen") is an attorney who stated that he was hired by Fleet Bank in 2004, to assist in an examination of Seminole Transportation Group's (SemGroup's) risk management policy in accordance with a renewal of its credit facility agreement. According to Bowen, after he conducted his initial review of the risk management policy in 2004, he was asked by Fleet Bank to do an update review, not a full examination, of SemGroup's risk management policies in 2005 and 2006. Bowen explained that Fleet Bank was acquired by BOA.

Bowen stated that in 2007 BOA asked him to perform an update review again, but he indicated that he wanted to do a full examination of SemGroup's RMP and procedures, given the lapse in time since his original examination. The examination Bowen conducted in 2007 was a stand-alone examination and the report that he prepared, dated May 25, 2007 (the "May 2007 Report"), did not rely on the findings in his previous examinations or updates. *See* Exhibit 19. The May 2007 Report was the last time Bowen performed an analysis at SemGroup. Bowen issued SemGroup a satisfactory report. Bowen explained that when he issues an opinion, it is either satisfactory or not satisfactory. The May 2007 Report was sent to BOA. Bowen also verbally communicated the information contained in the report to Cooper.

Bowen stated that he reviewed SemGroup's RMP and its audited financial statements from December 31, 2006 but he did not recall if he saw the notes to the financial statements. He also reviewed a schedule of SemGroup's open positions in the market compared to the overall positions of the market. Additionally, Bowen conducted interviews of SemGroup employees to gain an understanding of its overall business strategy and how risk management fit within that

strategy, and what roles and responsibilities individuals had in the management of its risk. Bowen also separately tracked an asphalt transaction and a crude oil transaction from inception to booking in the general ledger of the company, to understand the flow of transaction information through the organization.

It was Bowen's conclusion that SemGroup deviated very little from the RMP and that the paper trail for the asphalt and crude oil transactions was strong. Bowen cited three examples of constraint on the company: volumetric limitations, aggregate stop-loss amounts, and the availability of margin. Bowen had the impression that SemGroup spent more time managing broker margins compared to other companies similar in size. Bowen did not have a view as to the accuracy of the MtM and Position Reports submitted to the banks because he did not audit this information. Bowen noted that he considered the company's policy to incur no price risk on inventory a strength of its policy. Cooper provided Bowen a report showing the barrels bought in the offsetting transactions to protect the price. Bowen indicated that he did not audit those reports.

Bowen recalled an incident in January 2007 when SemGroup violated the RMP because it exceeded its stop-loss limit. SemGroup's explanation was that its inventory was delta-hedged, and that the value of the options used to create the delta hedge did not move as fast as the value of the inventory, causing a breach of the stop-loss limit. Bowen noted that the RMP would have required SemGroup to close out of its options position, however, it did not do that. He stated that it chose to wait a day or two for the market to catch up. Bowen commented that the decision to wait for the market to catch up was not inappropriate, but that SemGroup should modify its RMP to reflect how it would handle such situations.

Bowen also indicated that he thought SemGroup was doing too much trading for a company of its size. He stated that the amount of working capital tied to the collateral margin accounts was large for a company of SemGroup's size. To Bowen, this was indicative of too much trading activity. To gain an understanding of SemGroup's presence in the market, Bowen compared SemGroup's activity for the December 2006 timeframe and found that SemGroup comprised 20% of the overall market positions for crude oil options beyond three months to expiry. Bowen indicated that SemGroup was surprised by this because it thought the market was much deeper.

Regarding trading strategy, Bowen was aware that SemGroup rolled hedges from one month to the next as they were about to expire, and noted that doing so could be a very profitable strategy if done properly.

Bowen noted that perhaps the company's system of limits and controls had become too rigid and inflexible for application of a company of its size, indicating that SemGroup would have violated the physical limits before their stop-loss limits. Bowen suggested that SemGroup implement VaR to manage its trading risks.

Bowen noted that Oven and Coen worked directly for Kivisto, who was both the head trader and CEO. It was Bowen's view that Oven and Coen just executed the trading orders and did not have the discretion to be decision makers when it came to trading. Bowen noted that this structure is not very common in the industry.

B. The Debtors' Trading Strategies

1. Overview

SemGroup's business unit leaders, and the individuals who dealt primarily with physical commodities transactions, generally adhered to common, mostly risk-averse strategies that rarely incorporated the use of options.

The individuals with primary trading responsibilities for SemGroup were Kivisto, Coen and Oven in Tulsa, Shimonov at SemCanada, Weakland and Mr. Don Jensen ("Jensen") at SemFuel, and Mr. John Spencer ("Spencer") at SemEuro.

SemGroup business unit leaders were aware of options transactions that were executed on their behalf by Coen and Oven, and under the direction of Kivisto. Some business unit personnel questioned whether the transactions executed on their behalf were appropriate and supported their core business strategies.

Interviews with Oven and Coen revealed that they, under the direction of Kivisto, were engaged in a trading strategy known as managing "to expiry," that included the sale of naked call and put options. A goal of this strategy, according to Oven and Coen, was to increase marketing (commodities trading) revenue through the sale of options, and to prevent the realization of losses arising from options sales through the sale of more options.

2. Scope of Trading Documents Reviewed

In connection with the Investigation, the Examiner considered, among other things, the following:

a. SemGroup's policies and controls relevant to its trading procedures, including limits on trades and other positions;

b. Models used by SemGroup for trader support and valuation;

c. SemGroup's valuation methodology and its risk analytics;

d. SemGroup's RMPs;

e. Trading data was queried to identify transactions for further analysis, and supporting documents were reviewed;

f. SemGroup's daily position reports and risk reports;

g. SemGroup's aggregate equity product position was compared to its commodities derivatives position;

h. Westback's general ledger activity with SemGroup entities; and

i. Westback and SemGroup accounting data.

3. Trading Strategies by SemGroup's Other Business Units

a) By SemGas

Mr. Tim O'Sullivan ("O'Sullivan"), President of SemGas's business unit, stated that SemGas employees pursued relatively simple, asset-based strategies during the normal course of business. O'Sullivan also stated that other traders at the corporate level – Coen, Oven, and Kivisto – executed transactions unrelated to his business, and allocated at least part of the results to SemGas.

In describing its routine business activities, O'Sullivan indicated that SemGas would move natural gas through pipelines owned by SemGas, treat and process the natural gas at facilities owned by it, and then deliver the gas and NGLs to interstate natural gas pipelines or NGL market centers. (Raw natural gas is split into natural gas and NGLs at a processing facility.)

O'Sullivan stated that SemGas generated revenues in a couple of ways. Under one scenario, SemGas would purchase natural gas from the well owner, then treat, process, sell and deliver the natural gas and NGLs. Under another scenario, SemGas would charge a flat fee for gathering, treating, processing and delivering natural gas owned by others. Alternatively, for gas owned by others, SemGas would retain 25% of volumes routed through its assets. According to O'Sullivan, the majority of natural gas volumes were sold at a first-of-the-month ("FOM") index, with some daily fixed priced sales. O'Sullivan also stated that sales of NGL volumes were transacted at monthly average prices. Selling natural gas and NGLs at FOM indices or at monthly average prices allows market participants such as SemGas to contract for future deliveries of products, without creating the risk inherent in a fixed price sale. Accordingly, O'Sullivan stated that SemGas was a price-taker across the board, meaning that fixed price risk was not introduced by personnel at the business unit level.

O'Sullivan stated that he was not aware of specific transactions executed by Kivisto, Coen or Oven, but that he was aware of trades attributed to his business unit through financial statements prepared by the corporate office. O'Sullivan indicated that his business unit prepared a set of financial statements for SemGas, and that the parent company prepared a set of financial statements for SemGas as well. O'Sullivan noted that the only difference between the two sets of financial statements was a line item labeled marketing. He believed that this line item

represented trading activities executed by Kivisto, Oven and Coen. O'Sullivan stated that he did not know for sure exactly where the number came from, but that, to his knowledge, the transactions which comprised the marketing value were not related to his business. Additionally, O'Sullivan did not execute any options transactions for the period from January 1, 2007, through July 19, 2008.

b) By SemFuel

Jensen, a former Vice President at SemFuel, stated that he and former SemFuel President Darrel Weakland employed risk-averse, asset-based strategies during the normal course of its business. However, Jensen also stated that he was aware of options transactions executed by Oven, Coen, or Kivisto that did not directly support the underlying core business of SemFuel.

Jensen stated that he and Weakland implemented two main strategies: contango and basis spread. Under a contango strategy, for example, trades are conducted based upon the historical premise that the winter price of gasoline is lower than the summer price of gasoline. Jensen indicated that, with such a winter-summer price relationship, market participants who owned storage, as SemFuel did, would be able to nearly simultaneously buy winter gasoline and sell summer gasoline, locking in a profit while doing so. SemFuel would then take delivery of the gasoline in the winter, hold it in storage, and deliver it in the summer.

Under a basis spread strategy, Jensen stated that he would monitor the price of refined products in the Gulf Coast and Chicago. Jensen stated that if the price differential between the two locations was greater than the cost of transport, SemFuel would seek to buy Gulf Coast product and sell Chicago product simultaneously, thereby locking in a profit. (The actual mechanics of the contango and basis spread strategies are more detailed. Such detail is not

needed to provide an understanding of the strategies.) Jensen stated that he monitored his positions closely, and that if he ever had a position that was not close to zero (a zero position would equal no fixed price exposure), it was due to a mistake.

In a separate interview, Weakland confirmed that strategies executed at the SemFuel level were risk adverse strategies that sought to eliminate fixed priced exposure, such as contango and the rack marketing business. Under the rack marketing strategy, SemFuel would sell truckloads of fuel to smaller wholesalers, or "jobbers," at a price that was a few cents per gallon above SemFuel's purchase price.

Jensen stated that he did not execute options transactions during the normal course of business and that Weakland may have executed options transactions, but only rarely. Jensen also stated that he and Weakland maintained separate trade books and that Jensen is aware of only one occasion when a dollar value trade was placed on his book without his prior consent, and the value was insignificant.

Through conversations with Weakland, Jensen became aware that certain of the dollar values being placed on the SemFuel books came from options trading activity executed by the Tulsa traders (Kivisto, Coen, and Oven). Weakland confirmed this when he advised that he received a monthly profit and loss statement from the SemGroup accounting department, which included a line item called "Options." Jensen could not state whether or not he thought the options strategies underlying the dollar value placed on his book were actually a result of trades that supported his strategy. He did state that, in a couple of cases, it appeared that the options strategies placed on Weakland's book were in support of Weakland's core strategy, such as hedging unexpected inventory. Jensen also expressed the opinion that there were options trades

executed by the Tulsa traders and placed on Weakland's book that did not directly support Weakland's core underlying business. He surmised that those trades might have been refined products trades, but he did not know for sure. With respect to the line item called "Options" that Weakland received in the financial statements, he stated that he never knew its significance.

The "SemFuel Sold Options" chart shows that there were no options sales executed by anyone other than Oven and Coen from January 1, 2007, to July 19, 2008. *See* Exhibit 20.

c) By SemEuro

Mr. Lee Bullock ("Bullock"), Coordination Manager, SemEuro, stated that he and Spencer, Managing Director of SemEuro, were responsible for SemEuro's hedge commodities trading. Bullock stated that SemEuro generated revenue primarily from two core business strategies: a fee-based terminalling and storage business, and capturing price differences between Europe and the United States. Bullock stated that SemGroup's Tulsa traders (Kivisto, Coen and Oven) placed options transactions on SemEuro's books, and that the MtM losses associated with those trades eventually grew to more than $100 million.

Spencer stated that SemEuro reported its trading through SemFuel. Spencer stated that he had dotted line reporting to both SemFuel and Mr. Randy Majors ("Majors"), SemEuro's President. If he thought it was worth moving gasoline from the United Kingdom to the United States, he would discuss the proposed transaction with Jensen, who reported to Weakland. Spencer stated that Bullock ran SemEuro's day-to-day operations and supervised its accounting, bank relationships and reporting. Bullock also performed analyses of SemEuro's trade book.

Spencer indicated that options activity was not part of SemEuro's cross-Atlantic strategy and he does not believe there was any reason to execute options trades in addition to his hedges because options trades provided no additional price-risk protection. He stated that he never personally executed an options trade. Spencer stated that his trading strategy was asset-based and was not speculative.

Bullock stated that one of SemEuro's business strategies was to charge a fee to other companies who wished to use SemEuro's storage and terminal facility in Milford Haven, UK. He described Milford as a multi-product terminal with 82 tanks and a total capacity of 783,000 barrels. Three of the tanks held crude oil and the other 79 tanks held gasoline and jet fuel. Additionally, Bullock stated that SemEuro generated revenue by shipping gasoline from Europe to the United States, and by shipping jet fuel and diesel from the United States to Europe. Following a locational basis strategy similar to that implemented by Jensen at SemFuel, Bullock and Spencer would monitor commodities prices in the United States and Europe. When prices were such that SemEuro could nearly simultaneously buy gasoline in Europe and arrange for delivery in a future month in the United States, they would execute the transactions for the commodities as well as transportation fees, and lock in a profit. Bullock stated that they would also look for price relationships that allowed them to lock in a profit when buying diesel and jet fuel in the United States, shipping it to Europe, and delivering it at a profit amount that was locked in at the inception of the deal.

Bullock stated that SemEuro personnel were solely responsible for: (1) the purchase of physical quantities; (2) the hedging of the cross-continent transportation of the cargo; and (3) executing the appropriate financial hedges. Bullock stated that SemEuro would notify the Tulsa-based SemGroup traders once a transaction had been executed, or that SemEuro would

collaborate with them to discuss trading strategy. However, to his knowledge, commodities or derivatives transactions covering all normal business activities for SemEuro were executed solely by SemEuro personnel. Spencer stated that he did not execute any options as part of the cross-Atlantic strategy or SemEuro's supply contango strategy, and he believed that all fixed-priced risk was completely hedged without the use of options. Spencer did confirm that SemEuro had incorporated options into a crude oil hedging strategy that was executed in late 2006. However, he stated that those hedges would have expired in early 2007, and that otherwise, he and Bullock did not execute any options through July 22, 2008.

Bullock stated that even though he believed all fixed-priced exposure was to be hedged by SemEuro's personnel, he was aware of options executed on behalf of SemEuro by SemGroup personnel in Tulsa, and carried on the SemEuro books. Records indicate that options sales were transacted by Oven and Coen in 2007 and 2008 for SemEuro. *See* Exhibit 21. Bullock stated that his awareness of the options transactions came from a month-end report he received from SemGroup in Tulsa. Bullock stated that he would receive the month-end recap from Tulsa, verify it against broker statements, and book it on SemEuro's financials.

Bullock assumed that these trades were executed by Kivisto, Oven, or Coen. He also surmised that, even though SemEuro personnel were solely responsible for executing all appropriate hedges for SemEuro, the Tulsa-based traders might have seen "additional opportunities" around the SemEuro book. Spencer recalled phone conversations with SemFuel employees about the placement of dollar values on SemFuel's books that did not represent activity executed by SemFuel personnel. Spencer could not remember which SemFuel employee he had spoken to, but thought that it was either Jensen or Weakland, who conveyed to him that SemFuel was having a monthly dollar value placed on its books as well.

Bullock stated that from 2006 through October 2007, those "additional opportunities" were profitable. However, near the end of 2007, Bullock stated that those "additional opportunities" were no longer profitable, and that he and Spencer agreed that the negative MtM on SemEuro's books due to those trades was not representative of what it should have been (it did not correlate with SemEuro's core business activities). Bullock stated that the MtM loss on SemEuro's books was inappropriate and too high, based on what was in storage at SemEuro and what was in transit. Bullock stated that SemEuro raised the issue of the inappropriate MtM losses with SemGroup personnel in Tulsa, and that those discussions went on for several months.

Bullock stated that SemEuro's bankers began to ask questions about the large MtM loss on its books after the first quarter of 2008 audited financial statements were released. Spencer then asked Wallace to make an adjustment on SemEuro's books, to correct the MtM trade losses in excess of $100 million. Bullock stated that this situation was resolved in approximately May 2008, when all 2008 options trades executed by U.S.-based SemGroup personnel were taken off SemEuro's books. *Bullock described the moved options trades as trades that "should have been on Tulsa's books to begin with."* Bullock added that trades for 2007 were not adjusted, and that he was comfortable with the end results of the entry adjustments made in May 2008.

On June 17, 2008, Spencer e-mailed Wallace concerning the large negative MtM losses on SemEuro's financial statements as of May 2008. *See* Exhibit 22. Spencer indicated that, as of the end of May 2008, there was approximately $125 million of negative MtM on SemEuro's books resulting from Tulsa-based options trading activities. He also indicated that SemEuro liabilities, which included the negative $125 million from Tulsa derivative activities, exceeded SemEuro's assets by $69 million. Spencer expressed concern that the situation had the potential to render SemEuro insolvent. *Spencer noted in his e-mail that he had "important legal duties*

not to recklessly allow the company to trade itself into insolvency or continue to trade if insolvency cannot be avoided." See Exhibit 22.

Spencer stated that several conference calls were held regarding the large MtM that was placed on SemEuro's books. Spencer stated that he participated in these calls. He stated that other participants included Kivisto, Ronan (then SemGroup's Sr. Vice President of Finance), Perkins (a member of SemGroup's Treasury Department), and Oven. Spencer recalled that in one of the calls, Oven made a speech about how the placement of transactions on SemEuro's books had been made in error. Spencer noted that, in the short term, he felt the situation had been resolved satisfactorily.

Coen stated that the options trades placed on SemEuro's books were done by Oven. He stated that they were removed because the Tulsa traders felt that the residual assets belonged to SemCrude.

(1) SemEuro Transaction, dated May 16, 2008

The Examiner determined that pursuant to a purchase agreement SemCrude sold 200,000 barrels of crude oil to SemEuro for $25 million on May 16, 2008. *See* Exhibit 23. Through interviews it was noted that there may have been a guaranteed buyback provision, whereby SemCrude would buy back the oil from SemEuro within 90 days at a price higher than the market price, resulting in a profit to SemEuro. (A review of the May 16, 2008 contract did not reveal confirmation of the buyback provision. It is possible that it was an oral agreement).

Perkins noted that the purpose of the transaction was to increase SemGroup's liquidity. Perkins indicated that she did not think this was an unusual transaction, but did note that this was

the first time she had seen a buyback provision for a transaction at SemGroup. She suggested that Cooper, Wallace and Foxx would be in a position to provide more information because it was her understanding that they initiated this transaction. When asked about it, Foxx indicated that he knew that there was an inventory purchase agreement between SemCrude and SemEuro, but knew of no further details. (It should be noted that Foxx signed the contract on behalf of SemCrude.)

Brochetti, SemGroup's Senior Vice President for Finance, and later, Chief Financial Officer for SGLP, stated that he heard about the transaction, although he was with SGLP at the time it occurred. He stated that it came as no surprise to him and he did not feel there was anything out of the ordinary about the transaction. Although he did not know the details, he understood that the purpose of it was to benefit SemEuro, which had a large credit facility but was generating little cash. The crude oil market was attractive at the time so SemEuro was able to make a profit on the sale to SemCrude, which, in turn, sold it on the market for a profit.

When asked about a sale and repurchase transaction with a U.S. SemGroup entity, Bullock stated that in May 2008, Cooper and Perkins told him that SemCrude was going to sell SemEuro $125 million (the contract for this transaction was actually $25 million) worth of crude in tanks in Cushing, Oklahoma. This transaction was to be effective in May 2008 and SemCrude was to buy back the crude in August 2008, providing a profit of $5 million to SemCrude. Bullock indicated that he did not think much about the transaction because it was directed from Tulsa, and it was not unusual for personnel in Tulsa to have different strategies. However, this was the first time that he was aware of Tulsa personnel telling SemEuro what to do in regard to its business operations. Bullock stated that he received the contract and executed it. He believed the benefit to SemEuro was $5 million and the increased use of credit lines.

d) By SemStream

Coen stated that when he entered trades for SemStream, the business unit would purchase propane in the summer, knowing that the winter sales period was coming. Coen stated that when SemStream was filling the storage tanks with purchased propane, he would sell NYMEX winter month propane futures contracts or sell NYMEX winter month propane call options. He stated that SemGroup's preferred strategy was to sell call options because of the premiums it received. Coen stated that when he executed transactions for other business units, the transactions were always put in the appropriate sub-account with the broker and in the appropriate TradeLog database file.

Coen also stated that he executed "the strategy" of enhancement of revenues through the sale of options and obtaining premiums for those SemGroup business units that did not execute their own futures. Coen stated that there were monthly or bimonthly conversations with leaders of the SemStream and SemMaterials business units regarding inventory and the expected size of any positions. Coen stated that some of the transactions were executed to protect assets and others were executed to enhance revenues.

Mr. Larry Payne ("Payne"), President of SemStream, advised that SemStream provided NGL supply, storage, marketing, and terminal services in North America. SemStream owns and operates eleven private propane terminals in seven states, with combined throughput capacity of more than 325 million gallons per year. All of the terminals operate twenty-four hours a day, seven days a week, and serve customers throughout the Mid-South and Midwestern United States.

Payne stated that SemStream made its profit by buying and accumulating propane and heating fuel in the warmer months of April through September. The products were stored and then sold for profit from October through February. He stated that he was knowledgeable about the NGL trading at SemStream, but that his group did not execute trades, such as futures and options, but that Coen did so.

Payne stated that he believed the SemStream and SemGroup trading strategy was to hedge seasonal costs, and that the trading strategy was asset-based and not speculative. Payne stated that in late May or early June 2008, liquidity and cash for SemGroup were "tight," and there was a re-consideration of inventory build up by Kivisto, Wallace and Foxx. Upon their instruction, Payne ceased purchasing inventory.

e) By SemCanada

(1) Joe Shimonov

Shimonov was responsible for executing physical and financial crude oil transactions for SemCanada. He held the title of crude oil trader at SemCanada from late 2003 through 2008. During an interview, Shimonov explained his duties in more detail, which included a discussion regarding the implementation of Kivisto's options trading strategy.

Shimonov stated that in 2003 when he was first hired at SemCanada, he only transacted physical barrels of crude oil. He stated that one of his physical strategies included aggregating small volumes of crude from small producers and then selling it to refineries. He stated that since refineries preferred to deal in larger quantities, this provided SemCanada with an opportunity to make a profit aggregating crude from smaller producers. Shimonov also stated

that he was always looking for contango opportunities. He stated that although SemCanada did not own storage, storage could be leased. This meant that contango opportunities were usually a consideration.

Shimonov advised that, in early 2004, he became concerned about a trading position that he inherited that he did not understand. He stated that the position in question was a sold calls position that was "getting hurt" (losing money). Shimonov stated that he called Kivisto and Kivisto told Shimonov to gather information on all of his trading positions, and that he (Kivisto) would fly to see Shimonov and explain what to do. Kivisto arrived in Canada and introduced Shimonov to his trading strategies.

According to Shimonov, Kivisto told him that the market was backwardated 70% of the time and that, because of the backwardation, Kivisto's strategy was to sell crude oil call options in near term commodities contract months, and, at the same time, purchase futures contracts for the same or less volume as the call options, but for contract months approximately six months later. Shimonov stated that Kivisto told him that his trading strategy relied upon the concept that "the market can't be in two places at once." The shorter term sold calls would be rolled over until the last rolled call was for the same contract month as the initially purchased futures contract (about six months after the first trades were made). Because Kivisto never wanted to pay for the rolled trades for sold calls that were deep in-the-money, to finance the rolled calls, Kivisto instructed Shimonov to obtain premiums by selling puts, calls or a combination of the two. Shimonov stated that in 2008, as crude oil prices were rising, he would sell puts, straddles and strangles in order to finance the roll of the sold call options.

Shimonov indicated that at about six months from the first trades, the options contracts and the futures contracts would both be allowed to settle out and offset each other. Shimonov stated that the theory behind the strategy was that, in a market with upward moving prices, premiums could be collected, and any loss on the sold options would be offset by the purchased futures contracts.

Shimonov stated that he "backtested" this trading strategy and that it seemed to have worked over time. He also stated that he never transacted options until Kivisto taught him how to execute Kivisto's trading strategy. Shimonov stated that, initially, he thought the strategy was sound and thought it was asset-based. Shimonov now thinks that Kivisto's options strategy was speculative, although he did not elaborate.

Shimonov indicated that Kivisto was always seeking to get back to a delta-neutral position. However, Shimonov knew that there were naked positions being held by the company, and he was aware of naked positions in July of 2008. Shimonov stated that the position was not delta-neutral at all times, meaning that there were times when the potential volume liability represented by the sold calls was not offset with an equal number of purchased futures.

Shimonov reported that Kivisto repeatedly warned him to "never call the market" indicating Kivisto's belief that the crude oil market would always return to trading within its historical boundaries. While Kivisto had "mouthed the words" to "never conduct speculative trades" and there were assets behind some of the trades, with the benefit of hindsight, Shimonov had little doubt in his mind that SemGroup was engaging in speculative trading with no physical backed assets.

According to Shimonov, Kivisto's trading philosophy never changed, and because of the rise and volatility of the price of oil, many more positions were being put on the trading book during 2008. The cost of more options being traded grew, and so did the number of sold puts, calls, straddles and strangles, in an attempt to pay for the rolled trades. The cost of carrying these positions became extremely expensive. SemGroup's positions were growing larger and it was rolling more and more options.

(2) Other SemGroup Employees' Comments about SemCanada Trades

Oven stated that she felt that the naked trades which were reflected on SemCanada's books were appropriate because the trading transactions were part of Kivisto's trading strategy.

4. SemCrude's Trading Strategy (involving Eaglwing and Westback)

a) Kivisto Controlled his Closely-Held Trading Strategy, which he Considered to be Proprietary

Interviews of SemGroup executives, including Foxx, Stallings, Mr. Mark Lietzke ("Lietzke"), SemGroup's Controller, Spaugy, Ronan, and Brochetti revealed that none of them fully understood Kivisto's trading strategy, and that only Coen, Oven, and Shimonov were likely to understand the details of Kivisto's trading strategy and how it was implemented.

Interviews of Oven, Coen and Shimonov, and an analysis of their trading activities, revealed that they, under the direction of Kivisto, were engaged in a trading strategy described as managing "to expiry," that included the sale of naked call and put options. One goal of this strategy, according to Oven, Coen and Shimonov, was to increase marketing (commodities trading) revenue through the sale of options, and to prevent the realization of losses arising from options sales through the sale of more options. Employing Kivisto's strategy on behalf of

SemCrude and other SemGroup business units, Oven and Coen executed increasing volumes of options sales through the spring and early summer of 2008, which ultimately led to SemGroup's realization of approximately a $2.5 billion loss in its NYMEX trading account alone, a total trading loss in excess of $3 billion, and the filing of the Debtors' bankruptcy petitions.

Coen stated that Kivisto established all of SemGroup's corporate trading theories, and that it was his and Oven's responsibility to execute them. Coen stated that he spoke with Kivisto almost daily, and that, without exception, he and Oven confined themselves to Kivisto's trading philosophy. If Coen or Oven wished to stray outside of Kivisto's' trading theories, they would always discuss it with him before executing any trades. Kivisto's trading theories were very closely held, and he did not like to write them down. On the few occasions he did reduce something to writing, Kivisto made it clear that he did not want the information to be disseminated to others. As an example, an undated document was found in Kivisto's work space which states, in pertinent part, as follows: "P-plus Roll Program … We don't write this down … we don't want it out." *See* Exhibit 24.

Coen stated that, if Kivisto was out of the office, he and Oven would engage in transactions within the parameters Kivisto had established. Coen added that, to his knowledge, Kivisto never experienced trading losses like the losses at SemGroup in 2007 and 2008.

It was Coen's understanding that the RMP precluded the company from engaging in naked short sales of options unless the sales were part of a defined strategy approved by Kivisto. When asked if Kivisto's strategy was ever formally documented, Coen stated that he had never actually seen Kivisto's trading policy written down anywhere on paper, but that Kivisto verbally

defined the policy to him and Oven. Coen stated that the RMP permitted Kivisto to authorize any variations in SemGroup's trading policy.

Stallings reported that he was responsible for supervising the implementation of certain aspects of SemGroup's Information Technology ("IT") function. When IT personnel were attempting to construct a trade capture system, Kivisto informed them that they would not be able to incorporate his trading strategy into the IT system because he considered his trading strategy to be proprietary information, and he didn't want to reveal it to anyone. Stallings also stated that Kivisto instructed others that if any questions were raised regarding SemGroup's trading strategy by banks or other parties as part of any due diligence inquiries, they should only be directed to Kivisto.

As an example of Kivisto's adherence to his trading philosophy, Ronan stated that he became concerned about SemGroup's liquidity and trading and spoke to Kivisto about it in June 2008. Kivisto told Ronan that his number one rule was to "never call the market." Ronan replied that his number one rule was to "never run out of money." Kivisto always assumed that funding would be available to allow his trading philosophy the time it needed for the price of oil to return to a normalized trading range.

Coen stated that he believed Kivisto's trading strategy worked well as long as the price of crude oil traded within a historical range. He stated that problems arose when the price of oil moved in one direction only. He stated that SemGroup's purchase contracts were viewed as long options and that inventory was a secondary consideration. Coen stated that SemGroup would sell a straddle or strangle primarily to obtain the premiums on the options trades. *Coen stated that the increased revenues SemGroup received as a result of the option premiums it received*

became a main driver of Kivisto's options trading strategy, and marketing (commodities trading) revenues were added as an enhancement.

As an example of premium options payments received by SemGroup, an e-mail from Kivisto to Oven and Ms. Sharon Pens ("Pens"), dated March 26, 2007 (*see* Exhibit 25), states as follows:

> The only 'beef' Conagra has…is that they don't want to be out any more than $75,000,000 of option premium to Sem entities. Right now, for months May 07 forward, they believe we have collected $127,000,000 in premiums. This is obviously $52,000,000 over their self imposed limit.

Ms. Debbie Jaeger ("Jaeger"), a SemGroup Administrator, stated that she did not consider Kivisto to be a manager of SemGroup's employees. Rather, he managed SemGroup's trading, as well as Oven and Coen. Although Wallace would deal with Kivisto when he needed to do so, as Kivisto's interests outside of SemGroup grew, he (Kivisto) would stay in his office more and more.

b) Coen's Description of Kivisto's Trading Strategy

Coen described his trading activity as falling into two main categories: hedging crude oil from lease purchases and managing residual options positions. In executing these hedging and marketing (commodities trading) strategies that Coen stated were designed by Kivisto, Coen sold options that were unrelated to physical inventory or purchases.

Coen stated that SemCrude acquired approximately 80,000 barrels of crude oil per day from lease purchases that were not priced until the date of delivery. To hedge these oil purchases, Coen would execute two initial transactions at nearly the same time, which he referred to as a spread trade. As described by Coen, a spread trade is the sale of prompt month

crude oil and the purchase of crude oil for a different future contract month. Coen's first transaction would be a sale of approximately 80,000 barrels worth of NYMEX prompt month crude oil futures. This sale established a mechanism to effect eventual physical re-delivery of the purchased crude oil, but this sale was at a fixed price. Lease purchased barrels did not price until delivery but, since Coen needed to arrange for somewhere for that oil to go before delivery began, he sold the NYMEX prompt month contracts. Selling the NYMEX prompt month crude at a fixed price while a purchase price for lease purchase crude was undetermined created a short price position for SemCrude. (To explain further, SemCrude would sell oil at a fixed price on NYMEX before it knew the price it would pay for lease purchased oil, which it did in order to physically dispose of the oil that would be delivered as a result of lease purchases.) In an attempt to offset this fixed price risk created by the short NYMEX position, Coen stated that he would contemporaneously execute a second NYMEX transaction, which was a purchase of approximately 80,000 barrels of oil for a further dated contract month. Although not exact, Coen anticipated any losses on the fixed-price NYMEX sale to be offset by gains on the fixed priced NYMEX purchase. Coen stated that he would execute this spread trade daily until it was time to start transacting for the next prompt month.

Coen stated that when SemCrude began to take daily delivery of the lease purchased crude oil, the purchase price of that oil would also be set daily. To Coen, this daily delivery and pricing meant that the longer dated component of the spread hedge was no longer needed. But, instead of simply selling the longer dated NYMEX position which he had purchased as part of the spread hedge, Coen executed a different transaction. Coen stated that it was Kivisto's strategy to enhance marketing (commodities trading) revenues by selling call options in the same quantity and same contract month as the longer dated component of the spread position. Coen

stated that this call option sale was the theoretical exit of the spread position. Coen stated that if the market price of crude oil went above the strike price of this sold call option (*i.e.*, the call was "in-the-money"), Kivisto's strategy would have been to avoid realizing a loss on the option sale. To avoid realizing a loss on the sold option, Coen would sell even longer dated options (puts and calls) and use the premiums collected to purchase call options identical to those sold as the "exit" to the spread strategy. *This strategy allowed SemCrude to offset a current liability by creating a future liability and allowed SemCrude to forego the realization of MtM losses on the sale of options.* Coen described this process as rolling the position or as managing a residual position.

Coen indicated that it was Kivisto's strategy to never realize a loss on an option. Accordingly, Coen stated that he pulled a report every morning that showed which options were in-the-money, which report would guide his daily trading. *Coen also stated that part of Kivisto's philosophy was that the price of crude oil would eventually return to within historical ranges, and that, when it did, the options sold through the "rolling" process would expire worthless. Correspondingly, Coen indicated that it was Kivisto's strategy to continue to roll the in-the-money options until all options expired worthless. Coen stated that, after the first roll, any subsequent options transactions could no longer be considered as tied to a physical barrel.*

Coen also stated that inventory was not a factor in his daily decision making process. Coen stated that his main daily trading priorities were enacting spread hedges and rolling "in-the-money" options. Again, Coen stated that after the first options roll, that the residual options position could no longer be tied to a physical barrel of oil. Coen stated that, during management of the residual position, he executed options on products other than crude oil to diversify risk. Coen also indicated that he implemented Kivisto's strategy for SemMaterials and SemStream, meaning that he attempted to enhance revenues through the sale of options, and then

would roll forward any "in-the-money" options. Records confirm that Coen sold options for various entities, including Westback. *See* Exhibits 26A and 26B.

During the spring and early summer of 2008, options positions became much larger and more challenging due to the incredible volatility and one way price movement of the oil market. Coen stated that at this point the market simply overwhelmed SemGroup's investment strategy and that market conditions were outside of what the strategy was prepared to handle. He stated that the financial situation worsened and that, in May and June 2008, SemGroup's ability to maintain its margin payments grew increasingly problematic on a day-to-day basis. *Coen stated that in the last one or two months prior to the filing of its bankruptcy petitions, on a daily basis, SemGroup was on the verge of not being able to make its margin payments.* Also, in the months immediately prior to bankruptcy, Coen stated that Kivisto was trying to revamp his trading strategy in an attempt to address exceptionally challenging market conditions. The traders were also trying to stay within position limits and in compliance with debt covenants. Coen stated that he believes the traders always stayed within their trading limits. They were buying many options, employing a wings strategy to protect their positions. Coen also stated that the cost of the options purchases was increasing because of the increased market volatility and the number of options that SemGroup purchased.

Coen stated that a part of the trading strategy was managing "in-the-money" sold options as "residual positions" until the options could be allowed to expire worthless. *Coen also stated that the traders never believed that the losses would be realized, and that the "residual position" could be managed until the sold options eventually expired worthless.*

Coen contended that he never observed what he perceived to be a shift in the trading strategy.

Coen advised that the majority of his time was devoted to trading on behalf of SemCrude and Eaglwing, and later Westback. Coen stated that, to a lesser extent, he also spent some of his trading day working on SemMaterials and SemStream trades.

Coen indicated that there were occasions when, based on the size of the positions they had, Kivisto might instruct him and Oven to convert their crude oil positions to RBOB (reformulated gasoline) or heating oil to diversify. Coen stated that, after the diversification into RBOB or heating oil, any residual positions would have been managed using the same residual position strategy as crude oil. Coen advised that the trading strategy and management of residual positions was consistent for all entities for which he traded. Coen stated that traders viewed storage as a short option and producer contracts as long options.

Coen stated that on some occasions they engaged in day trading, which was based on Kivisto's analysis. Coen stated that Kivisto would ask at the beginning of the day whether the trading book would be hurt more by an up or down move in the price of crude. Based on the answers of Oven and Coen to Kivisto's question, at Kivisto's direction, they would offset the existing positions and the risk in the book or "the pain they would feel" by purchasing or selling futures and holding them throughout the day. Coen stated that they would exit out of this temporary position at the end of the day.

c) Oven's Description of Kivisto's Trading Strategy

Oven advised that her primary trading responsibility involved the execution of options transactions designed to provide price protection for business unit commodities. However, Oven also applied Kivisto's managing "to expiry" strategy which led to increased volumes of options sales transactions.

Oven used the example of a costless floor when describing her hedging activity, and to demonstrate how the implementation of it led to the rolling of options. She stated that she would have conversations with business unit leaders during which they may have indicated their intent to accumulate inventories of propane during the summer, in anticipation of the winter propane usage season. To protect the value of this inventory, Oven stated that she would purchase "at the money" puts that would pay off in the event of a downward move in the price of propane. This pay off was intended to offset any losses from the decline in the value of propane inventory.

To offset the cost incurred from the purchase of these puts (the premiums paid), Oven stated that she would sell "out-of-the-money" put options. Because Oven achieved the inventory price protection without incurring an initial cost, the structure is known as a costless floor. Oven indicated that near options expiry (which was also near the anticipated sale of the propane inventories), if the purchased puts were "in-the-money," they would be exercised. Further, if the market price of propane fell to where the sold put options were "in-the-money" near expiry, Oven would sell further dated puts and calls and use the premiums to offset any losses on the put options that were originally sold as part of the costless floor hedging strategy.

It is at this point in the trading strategy where Oven's description matches Coen's description. She indicated that it was Kivisto's strategy to never realize a loss on an options

transaction. Oven described selling options (both puts and calls) to manage a residual position. Oven indicated that Kivisto's philosophy was that prices would always return to within historical ranges, so she and Coen thought that the losses would never be realized because the position could be rolled until the options expired worthless. Records confirm that Oven sold options for various entities, including Westback. *See* Exhibits 27A and 27B.

d) Data Analysis (Technical Analysis)

SemGroup had a total MtM liability of $2.04 billion on December 31, 2007 based on its Consolidated Financial Statements (*See* Exhibit 45C, pages 2 and 26), and a MtM liability of $2.4 billion from options transactions. SemGroup internal documents show that on July 11, 2008, SemGroup had a MtM balance of negative $2.7 billion, with a negative $4.0 billion MtM balance from options transactions. An analysis of transaction data (*see* Exhibits 28A and 28B) shows that Coen and Oven were solely responsible for all options transactions executed for all SemGroup entities other than SemCanada, in 2007 and 2008. Shimonov was the only other trader to execute an options transaction during this timeframe. Kivisto did not personally execute options sales transactions during the 2007 and 2008 timeframe for SemGroup business units, although he directed Coen, Oven and Shimonov to do so. The analyses focused on options sales to the exclusion of options purchases because options purchases give the buyer the right, but not the obligation, to transact. As such, options purchases cannot create MtM liability.

Coen and Oven each described how the volume of residual positions from the managing "to expiry" strategy grew throughout 2007 and mid-2008, due to the rise in crude oil prices and the need to roll increased volumes of "in-the-money" options. Exhibits 28C and 28D, which show only those options sold by Coen and Oven, demonstrate the increase in the volume of

options sold from January 2007 through July 2008. Options sales volumes ranged from 71,896 contracts in February 2007 and peaked in May 2008 at 241,704 contracts. These volumes include options sales for all products transacted, so they cannot be directly correlated to a volume of crude oil sold. These volumes represent sales of puts and calls from all SemGroup entities and Westback for all commodities.

The Pre-Petition Credit Agreement Schedule 7.13-1 (*see* Exhibit 11) states: "Domestic crude option writing program is limited to the volume of physical storage available to SemCrude, L.P. and Eaglwing, L.P." and lists a storage capacity of 8 million barrels of crude oil for the United States and Canada. *As of May 12, 2008, SemCrude and SemFuel had a combined delta equivalent short position of 56,464 barrels of crude oil from the sale of call options. With each contract being equal to 1,000 barrels of oil, SemCrude and SemFuel had sold the equivalent of 56 million barrels of crude oil via sales of call options as of May 12, 2008.*

On April 17, 2008, Prudential Bache Commodities, LLC ("PBC"), one of SemGroup's brokers, posed questions in an e-mail to Kivisto, entitled "Client Review," about the nature of SemGroup's options positions at PBC. S*ee* Exhibits 29A and 29B. Part of this communication summarized an analysis which PBC performed, which stated as follows: "All scenario analysis shocking the underlying energy prices up and down result in a negative P&L in the account." This meant that if prices moved up or down, SemGroup's position at PBC would lose money.

In a May 7, 2008 e-mail (*see* Exhibit 30), PBC expressed concern to SemGroup regarding its use of options, whether its options activity coincided with the hedging of physical barrels and whether SemGroup was in compliance with its RMP. In the same e-mail, PBC cited the April 30, 2008 sale of 1,000 contracts of December straddles, and requested an explanation of how

those specific transactions related to hedging. The Examiner has been unable to determine whether SemGroup provided the specific explanation requested by PBC. During their interviews, Coen and Oven discussed the sales of straddles and strangles as options structures they employed when executing the roll of residual positions. On July 14, 2008, SemGroup showed a MtM liability of $2.7 billion, with greater than 83% of that liability attributed to SemCrude and SemFuel.

The following analyses compare inventory volumes to the cumulative commodities positions for each entity. The cumulative commodities positions include all fixed priced physical and financial purchases and sales listed in the daily MtM spreadsheet for each entity.

Although the total cumulative position was positive on many of the dates, during 2008, SemCrude was frequently short in the front month contracts while having length in later dated contract months. Exhibits 31 and 32 show the breakdown of SemCrude's inventory position versus its month-by-month net commodities position. *While the sum total of SemCrude monthly positions was positive for most report dates, the near-term short position exceeded the volume of inventory carried by SemCrude for all the dates shown in February and all but one of the dates shown for the month of March. Although the volumes of purchased commodities in the longer dated contract months would be expected to offset some of the gains or losses from the sales of near-term contract months, having a volume of commodity sales in near-term contract months that exceeded the volume of inventory on hand would be considered a speculative activity*. The inventory volumes used for the comparison charts were taken from SemGroup's Hedge Price Calculation spreadsheets. Jamie Cooper indicated that she used these spreadsheets to calculate the value of inventory volumes for use in the borrowing base reports. The monthly contract positions shown are the opposite of what would be expected for the execution of a contango

strategy. Under a contango strategy, near-term length and later dated sales positions would be expected. This net short near-term position persisted until April 2008, when SemCrude's purchased volume of prompt month futures contracts combined with inventory on hand exceeded the volume of sold contracts in other near-term months.

During March and April 2008, the SemCrude position for the June 2008 contract month changed drastically. The position for the June 2008 contract month went from net short (sales) greater than 10 million barrels on March 24 to net short (sales) greater than 15 million barrels on March 31, to a net long position of greater than 5 million barrels on April 14. The one week change in position from April 7 to April 14 was approximately 15 million barrels. The June 2008 contract month position subsequently increased to approximately 20 million barrels on April 21. SemCrude's June contract month net length remained near or above 20 million barrels for approximately three weeks, when it was reduced to approximately 10 million barrels of length on May 12. *Considering that SemCrude's crude oil storage capacity was less than 10 million barrels, carrying near-term contract length that exceeded the company's ability to store the product indicated that this trading activity was not completely backed by physical inventory.*

SemFuel net sales of all products exceeded its inventory positions from April 7, 2008, through July 14, 2008, with the exception of three dates shown. On those dates the net short position exceeded the inventory position by as much as 4.7 million barrels, with the majority of the short position being comprised of short crude oil contracts. Exhibits 33 and 34 show SemFuel inventory versus the cumulative net short position and inventory versus month by month contract positions for 2008. *Such a net short position would indicate speculative activity.*

Coen, Shimonov and Oven indicated that they implemented a strategy known as managing "to expiry," and that this strategy involved the sale of options that were not related to inventory. They indicated that the volumes of sold options increased as the price of oil rose outside of an anticipated price range. Coen, Shimonov and Oven indicated that they executed this strategy at the direction of Kivisto. Further, while no options transactions were executed by anyone other than Coen, Oven and Shimonov in 2008, the MtM liability from sold options for all SemGroup entities increased from $2.4 billion at the end of 2007 to $4.0 billion in July of 2008. This means that the total increase in negative MtM can be attributed to the activities of Coen, Oven and Shimonov, under the direction of Kivisto.

e) Other References to Kivisto's Trading Strategy

Mr. Gregory Price ("Price") stated that he was an accountant for Kivisto from 1994 until July 2008. Price stated that from 1994 to 2000, Kivisto would buy and sell barrels of crude oil, which he (Price) sometimes referred to as marketing. After Kivisto became affiliated with SemGroup, Price noted that there was a steady growth in the number of barrels of oil marketed. Price believes that there was real oil associated with Kivisto's marketing in those years, and no speculative trading.

Price stated that at some point (possibly in 2001 or 2002), he began to notice a significant amount of options trades for Eaglwing. However, he never had a discussion with Kivisto or Pens about the reason for them. Although the trading activity increased, he never understood the trading strategy or the reason for those trades, except that they became more and more of a profit producer.

Initially, Kivisto did all of the trading, with some administrative assistance from Pens. Beginning in approximately 2004, Kivisto became increasingly involved in SemGroup's acquisitions. Kivisto then began to receive help from Coen and Oven. Kivisto also began to use more brokers to conduct trades, and most of them were options trades.

Price stated that in 2007, after years of very good profits, he began to observe significant losses for the first time. The losses carried over into 2008 and worsened. While the profits associated with physical barrel trading seemed to be steady, Kivisto appeared to have a mindset to continue to grow through the use of options trading. Price stated that the crude barrel trading seemed modest by comparison, and became "a nice little sideline." He stated that he never felt he could have confronted Kivisto or even Pens regarding the growth of the options trading and the associated losses. He was not informed about the trading losses by Kivisto or Pens, although he stated that he observed the numbers.

Price stated that he saw huge losses in the November and December 2007 timeframe and had the feeling that something was going on as he worked on the closing book entries for those months. The losses continued into 2008. He stated that he would see a $2 million profit on the physical barrel marketing and a $30 million loss for the options trading.

Mr. J. Michael Vess ("Vess"), President, Chief Executive Officer and principal owner of Vess Oil, Wichita, Kansas, stated that Vess Oil was founded in 1979 and is engaged in the exploration, production and acquisition of oil and natural gas reserves.

Vess stated that he has known Kivisto since approximately 1994 when Kivisto, doing business as MKM, provided consulting services to the oil and gas industry. MKM was providing services to Vess Oil by attempting to maximize its lease price and well head price and increase

the financial returns to it. Vess explained that Kivisto was able to do this by bringing a number of competitors into the market who would bid up the price of the product. He stated that Kivisto employed a similar strategy through 2005 while operating Eaglwing for SemGroup.

Vess stated that he did not know and could not explain Kivisto's trading strategy, although he knew he was a good trader.

Stallings advised that Kivisto oversaw all of the commodities trading activity for SemGroup and its business units, and would work with business unit heads on specific trading-related issues. For example, although Spencer conducted trades in Europe, Kivisto would become involved if the trades involved transported physical crude. Stallings indicated that it was his understanding that physical crude cargos were obtained in Europe and delivered in places around the world, including the United States.

Stallings stated that Kivisto oversaw and directed all trading regarding crude oil and also directed all trading involving options. Stallings was of the opinion that only Kivisto, Coen and Oven would have known Kivisto's trading strategy.

Foxx stated that he and Wallace had complete faith in Kivisto's trading expertise, which they never questioned, and that Kivisto was highly regarded in the industry as a very intelligent trader. Conversely, Kivisto depended upon Foxx to provide the necessary crude oil for Kivisto to trade. According to Foxx, in the years before 2007, it was an arrangement that worked extremely well, as evidenced by the fact that marketing (commodities trading) was providing a huge portion of SemGroup's yearly revenue. Foxx estimated that, prior to 2007, approximately 50% of SemGroup's revenues came from operations and 50% came from marketing.

Foxx stated that Kivisto's trading strategy never seemed to be considered a factor in the company's liquidity problems because everyone in the company seemed to be of the opinion that, "Tom will fix it." Everyone fully expected Kivisto to resolve all of SemGroup's problems until the very end.

Brochetti stated that his background was strictly financial and that, although he had a general knowledge of commodities trading, it did not include trading strategies. Brochetti stated that Kivisto was totally responsible for SemGroup's trading function, including its trading strategy and decision making. According to Brochetti, no one received any trading-related training, other than Coen and Oven.

Weakland stated that he did not know SemGroup's trading strategy apart from what SemFuel did. However, he did know that Kivisto was engaged in options trading. Weakland's strategy with SemFuel was to do everything on a hedge basis. He did not want to be subject to the exposure of NYMEX, and he only used NYMEX when it was required by his trading partner. Even then he would move quickly to pay off the NYMEX position as soon as the trade was completed.

f) References to "Asset-Based" Trading

According to Coen, Kivisto's trading strategy was an asset-based theory. However, Coen stated that *the strategy was not based on what was physically in SemGroup's system, but rather on its storage capacity*.

Foxx stated that he always assumed that SemGroup's trading policy was asset-based. Lietzke, SemGroup's Controller, stated that it was his understanding that all trading began with physical transactions.

Stallings stated that the combination of SemGroup's mounting liquidity issues and the rising price of oil led it to seek bankruptcy protection. Stallings stated that he and others at SemGroup did not fully appreciate what was happening at the time, and that, in hindsight, they should have addressed SemGroup's liquidity issues, and the severity of its problems, in a different manner. Stallings indicated that SemGroup should have had more controls in place with respect to its commodities trading activities, and a better understanding of its trading book. *Stallings stated that Cooper had a spreadsheet "early on" that matched SemGroup's physical inventory positions with the derivative transactions related to them, but that, in hindsight, the physical inventory became unlinked from the financial trades. He stated that SemGroup should have had a better system to reconcile its physical inventory with its trading activity.*

Mr. Michael Hill ("Hill"), SemGroup's Tax Manager, described his function at SemGroup, as it related to trading, was to report net income for the company at the end of the year, after backing out unexercised and/or unexpired option premiums. The premiums were withheld from SemGroup's tax returns until such time as the options were exercised, when they would be reflected on subsequent tax returns.

Hill advised that the premiums SemGroup received increased significantly by the end of 2007. Because the amount of the premiums was such a large adjustment, he asked Cooper about SemGroup's trades and inquired if they were speculative. Hill stated that Cooper assured him that all of SemGroup's trades were hedged, and that there were no speculative transactions being

conducted by SemGroup's traders. To support his claim, Cooper produced a trading form, which contained boxes that the traders needed to check off when conducting a trade. According to Hill, Cooper stated that the boxes reflected that the trades were hedged. Hill further stated that he went to Cooper with the same question every year – Did SemGroup engage in speculative trading? – and he always received the same answer, that it did not.

On July 16, 2008, a representative of Capstone, met with, among others, Ronan, Oven and Coen and, based upon interviews with Coen and Oven, a review of the RMP and an excel spreadsheet that reflected some of SemGroup's trading transactions, concluded that SemGroup had engaged in speculative trading.

A report commissioned by BOA, prepared by Evergreen Collateral Consulting ("Evergreen"), dated May 2, 2008, also references SemGroup's trading activity.[6]

[6] The report, in part, stated as follows: "SemGroup attempts to hedge its inventory as close to 100% as possible to protect against unfavorable price fluctuations. The hedging prices and methodology that are used to value the inventory were discussed with Jamie Cooper and Brent Cooper in the Treasury Department, and others. The Company's policy is to cover inventory positions with back-to-back purchases and future sales contracts on the NYMEX. The inventory per the borrowing base is valued using the optimal pricing based on the average hedged price of the open contracts that give the optimal inventory value, or the market price, whichever is higher. Jamie Cooper receives the open contracts weekly to determine the average hedge price to be used for the borrowing base value. The optimal value is determined from the open contracts and compared to the current market price, and the highest and best value is used based on guidelines outlined in the loan agreement. The examiner [Evergreen] scope is to validate the open contracts per the brokerage statements and that the volume is sufficient to support the hedged inventory reported on the BBC borrowing [borrowing base certificate] at December 31, 2007. The examiner [Evergreen] limited the testing to the domestic inventory (not Canada), which comprises more than 95% of the hedged inventory reported on the BBC at December 31, 2007. The testing also did not include SemStream inventory which is comprised of butane, propane, and NGLs, for which there is no direct hedge. The Company hedges the SemStream inventory with 'dirty' hedges of crude and heating oil contracts. Discussion with management indicated that there were enough open contracts outstanding at December 31, 2007 to cover the hedging of SemSteam inventory. . . .[T]he futures contracts are sufficient to cover the volume of inventory reported on the borrowing base at December 31, 2007. . . . The chart above indicates that the open contracts of 6,822M barrels cover the inventory volume of 6,518M barrels that were reported on the BBC by more than 304 M barrels. . . ." *See* Exhibit 35, at 20-21.

Coen stated that it was his belief, as defined by Kivisto's trading strategy, that they never sold naked options; however, he admitted that he did sell options for which he did not have physical inventory, to back up the options sales. Coen stated that, since SemGroup owned 12 million barrels of storage, and since the trading limits were based on this storage capacity, SemGroup's policy was backed by physical inventory as long as the traders stayed within the trading limits.

g) MC Comments Regarding Trading Strategy

(1) Thane Ritchie

Ritchie stated that he had invested in SemGroup because of its pipeline and storage capacity. Accordingly, there was not much initial discussion about commodities trading or the trading of physical crude inventory. About the time that RCM invested in SemGroup, Ritchie recalls having one brief discussion with Kivisto about trading activity.

Ritchie advised that the first MC meeting he attended was in April 2006 at the Peninsula Hotel in New York. Kivisto, Wallace and Foxx were present on behalf of SemGroup's management, and the purpose of the meeting was to approve approximately seven or eight acquisition transactions. During the meeting, Ritchie and the Riverstone members asked about the effect that rising oil prices would have on the profitability of SemGroup's trading. He stated that the answers they received from Kivisto, Wallace and Foxx were confusing. The MC members had believed that only a contango market would be profitable for SemGroup, but Kivisto, Foxx and Wallace claimed that SemGroup's trading strategy allowed it to make money in both contango and backwardation markets.

In a telephonic MC meeting in late 2007, during which a large unrealized loss figure was discussed, the members were told that the loss resulted from short NYMEX futures positions and long physical positions, the latter of which could not yet be included in the loss/gain calculations. One of SemGroup's traders (Ritchie did not remember who it was, but it might have been Weakland) was put on the phone to explain how the eventual sale of physical inventory would recapture the profit and mitigate the loss. The explanation made sense to Ritchie at the time.

(2) Andrew Ward

Ward stated that members of SemGroup's management team told him on numerous occasions that SemGroup did not make speculative trades in its hedging operations. According to Ward, this matter was discussed during Riverstone's due diligence investigation and after it had invested in SemGroup. Ward was always told that SemGroup was utilizing a back-to-back hedge policy, which to Ward meant that SemGroup did not hedge more product than it actually owned. Ward believes that he was misled regarding this issue by all members of SemGroup's senior management, including Kivisto, Wallace, Stallings, Cooper, and Brochetti.

(3) Bartow Jones

Jones stated that during meetings in Tulsa on July 15 and July 16, 2008, he talked to several SemGroup executives about the trading book. Jones asked Cooper about his knowledge of the trading book. Cooper talked about a wings trading strategy, which had been developed to deal with wider swings in the price of oil, and stated that it had not been successful. Cooper advised Jones that SemGroup had rolled highly unprofitable options forward, which had the effect of keeping the losses unrealized. Jones opined that Cooper seemed to be very familiar

with the details of the trading account, while other management team members seemed to be trying to come to grasp with the situation.

Jones had a conversation with Wallace at that time regarding the state of the trading account. Wallace seemed surprised and angry when he was told an analysis showed there were speculative trades.

Jones also discussed the trading book with Ronan, who told him that he (Ronan) had looked at the trading book and realized that there had been speculation. It was Jones' impression that Ronan had previously been unaware of this issue.

h) BOK's Review of SemGroup's Trading Strategy

The Risk Management Department at BOK conducts risk management services for its energy trade accounts. SemGroup had an energy trading account with BOK under the name SemCrude, with an initial trading line of credit of $5 million, which was subsequently raised in several stages to $50 million. SemCrude's account also had a seven million barrel per month trading limit, which was never exceeded.

The basic trading model for an energy company with a BOK commodities trading account was that it would buy oil from producers and sell it for about $2 per barrel higher to customers. The traditional hedge is to lock in a sale price as a low risk strategy to reduce the risk from price fluctuation.

(1) SemCrude Exceeded BOK's Trading Limits in 2007

BOK's Risk Management Department monitored the SemCrude account for the prescribed limits from 2003 until approximately September 2007, without noting any exceptions.

(In approximately August 2007, the SemCrude account reached 80% of its $50 million dollar trading limit, and SemCrude was sent a warning.) In September 2007, SemCrude exceeded its $50 million dollar trading limit for the first time.

In addition to monitoring SemCrude's trading limits, BOK's Risk Management Department also monitored the types of trades being conducted in the SemCrude trading account. In October 2007, BOK determined that SemCrude was engaged in rolled forward trades. SemCrude had been selling calls against inventory. In other words, SemCrude was typically selling an option to buy oil in the future at a certain price (the "strike" price), for which it would be paid a premium. The premium amount typically could be $3 per barrel. Selling calls is not considered to be very risky if it is a covered call, because if the price of oil increases, the possibility exists to sell the inventory underlying the trade at the current market price. When SemCrude began rolling trades forward in October 2007, the strategy was not, by itself, considered unusual. However, BOK's Risk Management Department was not comfortable with SemCrude's deep "in-the-money" rolled trades, that is, with the trades in which the strike price was relatively low compared to the current price of oil, which generated a higher premium payment to SemCrude. In other words, as the price of oil increased and options trades came due with a loss, SemCrude would receive a larger premium payment on rolled options trades if the new strike price was further removed from the current price of oil. The larger the difference between the strike price and the current price of oil, the "deeper in-the-money" the options trades would be, which would further increase SemCrude's MtM exposure.

(a) November 2007 Meeting between BOK and SemGroup

In November 2007, a meeting was held at SemGroup to discuss the trading in SemCrude's account at BOK. Kivisto, Cooper, Coen and Oven attended the meeting on behalf of SemGroup.

BOK representatives told SemGroup's representatives that it had noted that SemCrude had been making trades that were "deep in-the-money." BOK wanted to understand the economics for making them and the trading strategy that was being utilized.

Kivisto gave a "rapid but thorough" explanation of the trades during the meeting. He referred to SemCrude's trading strategy as a "covered call" strategy that SemGroup had been engaged in for several years. Kivisto also stated that this strategy had been successful and that its profits had augmented SemGroup's income.

When asked during the meeting if SemGroup had the necessary cash to pay for the rolled trades, Kivisto assured BOK that it did. Kivisto also advised that oil was going to be delivered to SemGroup in the near future, which would yield additional cash, and that the fourth quarter of 2007 was going to be a "great" quarter for SemGroup. Kivisto told BOK that SemGroup did not wish to settle the trades, and that it decided to roll them forward because of the timing of anticipated sales of oil in the immediate future.

Based on Kivisto's explanation, BOK representatives felt that if Kivisto anticipated that SemGroup would collect a significant amount of cash in early 2008, as he claimed, that he had a legitimate reason for making the "rolled forward" trades, assuming, of course, that SemGroup had the physical inventory to support them.

(b) January 2008 Meeting between BOK and SemGroup

In December 2007, BOK's exposure reached $130 million – $80 million more than SemGroup's trading limit – as a result of SemGroup's continued "deep in-the-money" trades. BOK decided to recommend a strategy to SemGroup to discontinue its "deep in-the-money" trading activity, and to enable it to reduce its exposure to BOK.

The BOK Risk Management Department prepared some guidelines that would potentially bring SemGroup's exposure down to its $50 million trading limit. The BOK Risk Management Department guidelines included the following:

1) SemGroup could not roll more than $10 per trade (meaning that the strike price could not be more than $10 different from the current price for a barrel of oil). This would limit the amount of the premium SemCrude would obtain from the trade, and also reduce SemCrude's MtM exposure;

2) SemGroup would have to provide BOK with earnest money ($10 million cash);

3) SemCrude would have to protect its rolled calls, by placing an additional call at a higher strike price to protect against extreme increases in the price of oil (referred to as a wings protection strategy); and

4) If BOK's exposure was greater than the $50 million trading limit by July 1, 2008, SemGroup would have to post a cash margin for the full amount in excess of the $50 million trading limit.

Cooper, Oven and Coen represented SemGroup at its second meeting with BOK. Kivisto did not attend the meeting, but he came into the room for a brief time to say hello near the end of the meeting.

During the meeting, Cooper claimed that SemGroup's trading activity was backed by physical inventory. This was very important to BOK because, as previously noted, if the trade was supported by physical inventory, and if the price of oil thereafter increased and the trade lost money, the underlying oil could be sold to satisfy the loss. On the other hand, if there was no

inventory to support the trade, SemCrude would be responsible for the loss with no physical inventory to back it up, which is by definition a naked trade.

BOK's guidelines were presented to SemGroup's representatives during the meeting. SemGroup was told that it could not do any more trading in the SemCrude account at BOK, except to close its existing trades, unless SemGroup agreed to its conditions. Within a few days of the meeting, SemGroup agreed to BOK's terms. SemGroup sent $10 million to BOK, which was placed in a money market mutual fund. Thereafter, BOK's Risk Management Department monitored SemGroup's trading at BOK to ensure that all rolled trades were within the $10 limit and that SemGroup employed a wings protection strategy with them. (SemGroup did not employ a wings protection strategy on its BOK trades prior to January 2008.)

(c) May 2008 Meeting between BOK and SemGroup

In late May 2008, BOK called a meeting with Wallace to discuss SemGroup's liquidity issues. Wallace provided assurances to BOK that SemGroup was liquid, and noted that it was imminently expecting a large infusion of cash.

In May 2008, when an amendment to SemGroup's credit agreement with BOK was being considered for approval, a BOK representative called Cooper for the specific purpose of confirming that all derivative trades were backed by SemCrude's physical inventory of crude oil. When asked that specific question, Cooper responded in the affirmative.

SemGroup continued to roll trades forward at BOK until July 2008. BOK did not impose the requirement that SemGroup post a cash margin for the full amount of its trading limit overage as of July 1, 2008, because SemGroup told BOK that it was within days or weeks of

raising equity capital through an agreement with Goldman Sachs, and that it would use some of the proceeds from it to pay down the BOK account to its $50 million limit. The last trade placed in BOK's account was on Friday, July 10, 2008.

BOK's understanding of SemGroup's trading strategy was that, regardless of the instruments SemGroup used to facilitate its trades, SemGroup was engaged in asset-based trading. Anything else would have been speculative trading, in BOK's view. BOK, as well the other lenders, relied upon the information SemGroup provided in its position reports to confirm that its trading was based upon assets on hand.

If SemGroup was not engaged in asset-based trading, or if its position reports did not accurately reflect SemGroup's net trading positions, BOK would have reconsidered its credit facility status with SemGroup.

i) Moody's Review of SemGroup's Options Trading

The purpose of Moody's analysis and rating of a company is to evaluate the risk of investing in it. Part of the process of determining whether Moody's will begin issuing ratings of a company is to meet with the company's management. Moody's had a meeting with SemGroup officials in approximately 2004 in New York. Kivisto, Wallace and perhaps two other SemGroup officers were present. Moody's was impressed with SemGroup because the company's management seemed to be smart and to have a thorough knowledge of the midstream business.

A question Moody's asked at the initial meeting was whether or not SemGroup was running a matched trading book. The response from SemGroup was that part of its business was

a contango trading book, long on hydrocarbon. The SemGroup executives stated that the book was always perfectly matched, and Moody's worked on the assumption that what they stated was true.

In evaluating a midstream company such as SemGroup, the rate of increase in oil prices is always a pivotal issue. As oil prices increase, both the company's costs of doing business and the cost of its cash margin requirements increase. The rate of oil price increases proved to be an issue for Moody's with SemGroup. Moody's became alarmed about SemGroup's situation sometime in the first quarter of 2008, when it saw oil prices rising steeply and SemGroup's level of borrowing rising as well. Moody's expectation in a situation like this was that SemGroup would "roll off" positions and decrease its volume of business. However, SemGroup did not do so. In Moody's view, SemGroup did not know when to "turn the valve off." The issue, as a Moody's representative expressed to SemGroup, was "When are you going to lower your volume to what you can afford?"

Despite Moody's warnings, SemGroup did not reduce its trading volume. Moody's raised this concern to SemGroup on a number of occasions, usually by e-mail. While Moody's dealt directly with Wallace at first, it later added Brochetti and Stallings as routine recipients of its e-mails.

A Moody's representative confirmed that he sent an e-mail to Brochetti, Stallings, Ronan, Cooper and Nancy Baker ("Baker") on June 9, 2008, inquiring about a rumor in the industry that SemGroup had been "on the wrong side of a bad trade" on June 6, 2008. *See* Exhibit 36. He also asked about the effect of the surge in oil prices on SemGroup's ability to fund its working

capital and margin calls. The Moody's representative also warned that he would prefer not to have to issue a cautionary press release.

Someone at SemGroup (the Moody's representative did not recall who it was, but thinks it was Brochetti) responded promptly that SemGroup had also heard the same rumor, and that the trade in question did not involve SemGroup. The Moody's representative did not know if the statement was true, but at the time assumed it was true, partly because of the promptness of the response and the categorical nature of the denial.

The Moody's representative also confirmed sending an e-mail on July 16, 2008, to the same officials asking for SemGroup's consolidating statements for March 31, 2008, April 30, 2008 and May 31, 2008. *See* Exhibit 37. Those reports were supposed to have been submitted seven weeks after the end of each month, and Moody's was anxious to see them, because SemGroup still had not reduced its volume. Baker sent the requested reports that same afternoon, in response to Moody's e-mail.

On July 17, 2008, the Moody's representative sent an e-mail to Ronan, Brochetti, Wallace and Cooper, inquiring why SemGroup had not reduced its level of market activity as oil prices continued to surge, and asking whether SemGroup was following a trading strategy that assumed that prices were poised to fall. *See* Exhibit 38. He could not recall SemGroup's response to the e-mail.

Moody's was becoming increasingly agitated with SemGroup for not following its advice to reduce its trading volume and thereby to lower its operating costs and margin requirements. SemGroup's financial statements told Moody's that SemGroup was making lots of money, but only if it was running a matched trading book. Moody's is not sure when it began to suspect that

SemGroup was not running a matched book, but it was clear to Moody's that it had not done so once it filed for bankruptcy protection.

j) Goldman Sachs' Review of SemGroup's Options Trading

SemGroup began negotiations with Goldman Sachs ("Goldman") in December 2007 for a non-public 144A equity offering, in an initial effort to raise $700 million. A 144A offering, which provides for confidentiality, is an issuance of tradable securities that can only be marketed to a group of private investors or institutions. Goldman had previously conducted two successful 144A offerings on their "GS TruE" platform and SemGroup liked the concept. The goal was to market the securities to a couple of hundred investors at a pre-determined price. The negotiations continued until early July 2008, at which time the amount of SemGroup's potential financing had increased to $1.5 billion. SemGroup's financing effort was referred to as "GS TruE."

Although this was to be a private equity offering, Goldman's due diligence requirements were the same as if it was an initial public offering ("IPO").

In approximately June 2008, Goldman's review of SemGroup's financial data revealed that SemGroup's trading losses were approaching $2 billion, and that its margin calls were devouring its capital. Goldman began to wonder exactly what SemGroup was doing with respect to its commodities trading and whether it was really operating a matched book, as it claimed. In response to Goldman's inquiries, SemGroup explained that, since hedge accounting constricted it, SemGroup engaged in options trading which required daily financial MtM accounting, resulting in huge unrealized losses.

Goldman stated that it began to realize that the GS TruE offering was not going to occur before September 2008, if at all, because it would be impossible to market a company like SemGroup with so many significant issues. In late June 2008, Goldman requested that Kivisto turn over SemGroup's trading book to Goldman for analysis.

Goldman advised that two events occurred within 48 hours that convinced it that it would not do any more business with SemGroup. One was when Kivisto called Goldman and advised it that SemGroup's credit line was low and that he had decided to sell one third to one half of its trading book. Kivisto did not reveal a possible buyer. The second was when Goldman completed its analysis of SemGroup's trading book, which revealed that SemGroup was short 18 million barrels of crude assets. This convinced Goldman that SemGroup was not hedging based upon physical inventory. A Goldman representative subsequently had a telephone conversation with Kivisto, in which Kivisto expressed disagreement with Goldman's analysis of SemGroup's trading book.

Goldman opined that Kivisto believed that he could use SemGroup's storage capability to overcome his short options trading positions, although investors wanted a matched book. Goldman concluded that SemGroup's trading strategy was more than just hedging.

Goldman advised that while Kivisto and Wallace were personable individuals, it was disappointed in them because it did not appear that they had been completely forthright in their representations regarding SemGroup's financial troubles. Goldman was upset that it had to find out about SemGroup's financial difficulties through its own due diligence.

In early July 2008, Goldman decided to discontinue its business relationship with SemGroup, and provided official notification of its decision to SemGroup.

k) Capstone Advisory Group Comments Regarding the Trading Strategy

On July 16, 2008, during a breakfast meeting in Tulsa, Oklahoma with a representative of The Blackstone Group, Capstone was told that Blackstone had determined that SemGroup had been utilizing a speculative trading strategy, which was referred to as "strangle trades." Later that day, Capstone interviewed Oven and Coen. At the outset of the meeting, Capstone's representative told them that he wanted to hear about SemGroup's speculative trading. Oven and Coen then described the strategy, which they called "trading to expiry." They stated that the "trading to expiry" strategy for crude oil utilized offsetting options. SemGroup sold "call" options above the market and sold "put" options below the market. Both sales would generate a premium for SemGroup. The options would be sold within the historic range for crude oil. Ideally, both options would expire naturally within the historic range of oil prices, and there would be no exposure to SemGroup. If the market price of oil went above the call price, they would issue two or more options at higher prices, hoping that the new options would expire worthless. Oven and Coen were open about this policy and acknowledged that SemGroup was using bank collateral to finance its options trades.

Capstone's representative stated that Coen and Oven showed a document to him that purported to summarize SemGroup's trading positions. They claimed that the document was incomplete and stated that it needed to be updated. They promised to do so and to provide it to him. On July 17, SemGroup's trading offices were "dark." Coen and Oven were not present for the remainder of Capstone's visit, and no one else was available to answer additional questions about trading matters. Capstone was never provided with SemGroup's updated trading positions documents.

l) Eaglwing and Westback

Michael Cooke ("Cooke"), an attorney with Hall Estill, stated that Hall Estill handled all of the legal work when Eaglwing Trading Inc. merged with Seminole Transportation, Inc. ("Seminole") in August or September 2000. Cooke had been Kivisto's personal and business attorney since 1996.

Cooke stated that Energy Spectrum, a venture capital company, was a significant investor when Seminole was formed. He stated that it insisted that Eaglwing become part of the merged company and that Kivisto be hired as one of its executives. Although there was some discussion about Westback being included in the merger, Kivisto and the other principals could not agree on a price for Westback. Seminole purchased Eaglwing from Kivisto (a 20% owner), Mr. David Murfin ("Murfin") (a 40% owner) and Vess (a 40% owner).

(1) Westback's Relationship with Eaglwing/SemCrude/SemGroup

Westback is an entity wholly owned and controlled by Kivisto and his wife, Julie Kivisto. It was established in 1996 to conduct hedging and trading transactions for Kivisto. *See* Exhibit 39. Greg Price, who performed accounting services for Kivisto, Westback, and some of Kivisto's other businesses, stated that Kivisto attempted to sell Westback to SemGroup around the same time in 2000 that Eaglwing was sold to SemGroup, but that Kivisto and SemGroup could not agree on a sale price. This was also confirmed by Foxx. In a memorandum prepared by Stallings about Westback, dated March 20, 2008, he reported that since the inception of SemGroup in April 2000, Westback had used Eaglwing as an agent to enter into and to execute trading contracts on Westback's behalf. *See* Exhibit 47.

Coen stated that in 2007, he offered to help Kivisto manage the Westback transactions, because he knew Kivisto "had a lot going on." He stated that a similar trading strategy was used for the Westback trades as was used for the Eaglwing trades. He stated that he was unaware of any physical assets owned by Westback. He also stated that Kivisto operated Westback from SemGroup's offices. Coen stated that Pens, Kivisto's Administrative Assistant at SemGroup, made some physical purchases/hedges of crude oil for Westback, and coordinated all of Westback's activities on behalf of Kivisto.

Coen and Oven both stated that when the ConAgra Trading Group, Inc. ("ConAgra") positions closed and the Westback positions were moved from ConAgra to a sub-account to SemGroup's account at Merrill Lynch, it was Coen and Oven that renamed Westback "Eaglwing 2 (ETI2)." Coen stated that they did so because they could see that Kivisto pursued a similar trading strategy with Westback as he did for Eaglwing and other SemGroup entities, and because they assumed that Westback and Eaglwing were related.

Coen stated that he never viewed the simultaneous trading in the two accounts – Eaglwing and Westback (ETI2) – as a conflict of interest because he was unaware of the purpose of the Westback entity. Coen stated that he never discussed why Westback/ETI2 was a separate entity with Kivisto, and didn't push for an explanation from him, because he understood that Westback/ETI2 had always been a separate business owned by Kivisto.

Stallings stated that when ConAgra left the commodities exchange business at the end of 2007 or early 2008, whatever futures trades were still active had to be closed. Stallings stated that ConAgra looked to SemGroup to satisfy all of the transactions in the Eaglwing account, including the Westback transactions. Ms. Kathy Lewallen ("Lewallen"), SemCrude's Controller,

expressed a concern to Stallings when the ConAgra trades were closed about reconciling and distinguishing between the Eaglwing, Westback, and SemCrude transactions, since ConAgra had treated all of the trades the same. As a result, Lewallen had to go back and attempt to separate the Westback transactions from the Eaglwing/SemCrude transactions. Kivisto transferred the remaining Westback transactions in the ConAgra account into a Merrill Lynch account. According to Lewallen, the "Eaglwing 2" account at Merrill Lynch was used exclusively for Westback trades.

Stallings stated that, after July 22, 2008, he learned that Westback had made physical purchases and sales of crude oil through Eaglwing in SemGroup's trading account at ConAgra. Stallings stated that it was his understanding that Kivisto would then make trades "around" this physical crude (Kivisto would make option trades hedging the crude oil that had been purchased). After ConAgra discontinued its commodities trading business, Westback engaged in no further physical trading activity through Eaglwing/SemGroup.

(2) Kivisto's Employment Agreement Identifies Westback

Article II of Kivisto's employment agreement, dated August 4, 2000, provides Kivisto with the right to conduct business for Westback. *See* Exhibit 41A. The agreement states at Section 2.1 as follows:

> The Executive agrees to devote all of his business time, efforts and attention to the business and affairs of the Company on an exclusive basis, and not to engage in any other business activities for any person or entity, other than as expressly provided in this Section 2.1. The Executive may engage in personal investment activities which do not materially affect the performance of the Executive's duties hereunder. Such activities shall include, without limitation, continuing to serve as a managing member of various limited liability companies and shareholder and officer of various corporations in which the Executive currently has investments.

> Such companies and corporations include Westback Purchasing L.L.C., Eaglwing Energy, L.L.C. . . .

Article II of Kivisto's employment agreement, dated April 30, 2004, also provides Kivisto with the right to conduct business for Westback. *See* Exhibit 41B. The agreement states at Section 2.1 as follows:

> The Executive agrees to devote all of his business time, efforts and attention to the business and affairs for the Company and SemGroup, L.P., on an exclusive basis, and not to engage in any other business activities for any person or entity, other than as expressly provided in this Section 2.1. The Executive may engage in personal investment activities which, in the good faith opinion of the Management Committee, do not materially affect the performance of the Executive's duties hereunder. Such activities are set forth on Exhibit A attached hereto. In the event the Executive is presented opportunities to participate financially (other than as allowed pursuant to the penultimate sentence of Section 7.3) in businesses or transactions which relate to the then business of the Company or SemGroup, L.P., prior to accepting such opportunities the Executive will present them to the Management Committee. . . .

See Exhibit 41B.

Exhibit A to Kivisto's employment agreement provides:

> (Permitted Activities Under Section 2.1)
>
> Pursuant to Section 2.1. of the Employment Agreement, the Executive may engage in personal investment activities that, in the good faith opinion of the Management Committee, do not materially affect the performance of the Executive's duties under the Employment Agreement. The permitted activities include, without limitation, continuing service, as a managing member of the following Limited Liability Companies: 1. Westback Purchasing, L.L.C. [and] 2. Eaglwing Energy, L.L.C."

See Exhibit 41B.

(3) Pertinent Pre-Petition Credit Agreement Provisions

However, Section 7.09 of Article VIII (Negative Covenants) of the Pre-Petition Credit Agreement states that the loan party (SemGroup) shall not:

> Enter into any transaction of any kind with any Affiliate of any Loan Party, whether or not in the ordinary course of business, other than on fair and reasonable terms substantially as favorable to such Loan Party as would be obtainable by such Loan Party at the time in a comparable arm's length transaction with a Person other than an Affiliate, provided that the foregoing restriction shall not apply to transactions between or among any Loan Party and any of its Restricted Subsidiaries.

See Exhibit 42 at Section 7.09.

Additionally, the Pre-Petition Credit Agreement at Section 7.12 states:

> Limitation on Credit Extensions. Except for Investments permitted under Section 7.02 and Swap Contracts permitted under Section 7.02(k)(f) hereof, extend credit, make advances or make loans other than normal and prudent extensions of credit to customers buying goods and services in the ordinary course of business or to another Loan Party in the ordinary course of business, which extensions shall not be for longer periods than those extended by similar businesses operated in a normal and prudent manner.

See Exhibit 42. Both of these provisions were violated with respect to the trading activities conducted on behalf of Westback/Kivisto through Eaglwing/SemGroup.

(4) Accounting Issues Relating to Eaglwing and Westback Transactions

The accounting for the Westback transactions was conducted by SemGroup's employees and/or individuals associated with SemGroup. Westback was a subject of concern to some of SemGroup executives and its outside auditors from at least 2006 onward. As noted earlier, Kivisto, Coen, and Oven were responsible for the placement of the Westback trades by SemGroup. Pens and Price did the bookkeeping entries for Westback's options trades and its physical trades.

Pens, Kivisto's Administrative Assistant, worked exclusively for Kivisto, and was responsible for the accounting for Westback and Kivisto's other personally owned entities and

financial interests. Price, who was initially hired on a part-time basis by Kivisto in approximately 1994, and who prepared Kivisto's personal and business-related tax returns, also performed accounting functions for Westback and Eaglwing, as well as Kivisto's other business interests. The Westback and Eaglwing commodities trades were initially accounted for separately from SemGroup's accounting system and were not integrated into Oracle, like SemGroup's other business units. Eaglwing's accounting was also handled differently than SemGroup's other business segments.

When it came time to integrate Eaglwing's trading results into SemGroup's accounting system, the Westback trades that were conducted through Eaglwing were removed by Pens and/or Price, so that they would not be reported to SemGroup. However, as a SemGroup business unit, Eaglwing's results needed to be provided to SemGroup. Lewallen worked with Pens and Price to make sure that the Westback trades were removed before Eaglwing's results were provided to SemCrude and, ultimately, to SemGroup. *See* Exhibit 43.

Price stated that he was an accountant who only performed accounting functions for Kivisto. He asserted that he did not have a deep knowledge of Westback's and Eaglwing's trading activities. Price advised that Pens was responsible for the "heavy lifting" with respect to Westback, and that he was only responsible for accounting issues.

Jaeger stated that, in July 2008, after Kivisto and Pens were placed on administrative leave by SemGroup, Price asked her for his paycheck, at which point she learned that he had been paid by Pens from an Eaglwing account for the services he performed for Kivisto.

Stallings was aware that Price and Pens worked together in performing the accounting work for Eaglwing and Westback. Stallings felt that, since the Eaglwing accounting information

was being forwarded to SemCrude as required, and since he was unaware of any problems with the work Pens and Price performed, he did not alter the arrangement. Stallings also stated that the arrangement predated his employment with SemGroup and was being performed at Kivisto's request, and pursuant to his direction.

(5) Kivisto's Use of Eaglwing for Physical Trades/Westback Profits

Price stated that as SemGroup's balance sheet became stronger through bank loans and acquisitions, Kivisto was able to use that strength to "hitch a ride" for Westback in options trading. Price explained that Westback did not have the same credibility to trade in large quantity options trades as easily as Eaglwing/SemGroup could, and, by using Eaglwing's account for Westback trades, Westback was able to make larger trades, which resulted in larger potential profits for Westback/Kivisto. As an example, he stated that it was his understanding from Pens and Kivisto that ConAgra wanted the large wire transfer amounts for the Westback options trades to be made from the Eaglwing account, not a Westback account.

Price stated that Kivisto used Westback's bank accounts to take regular draws for himself and his wife for their living expenses. Kivisto also used the account to make payments for his personal needs, such as vehicle payments, property purchases, personal loans, personal investments, donations to charity, etc. The funds in the Westback account were co-mingled with Westback's commodities trading gains and losses.

Price stated that, pursuant to a verbal agreement between Kivisto, Cooper and Wallace, Westback operated as an agent for Eaglwing for the physical commodities trades Kivisto conducted for SemGroup. Under this agreement, Kivisto, on behalf of Westback, arranged physical commodities transactions for Eaglwing/SemGroup, and Eaglwing would pay Westback

(Kivisto) a commission, or "service fee," for them. *See* Exhibit 44. Price noted that Eaglwing/SemGroup benefited from the profits associated with Kivisto's physical trades on its behalf through Westback. Price stated that Pens calculated the commissions due from Eaglwing to Westback (Kivisto), although he did not know how the commission amount was determined. Pens provided Price with a hard copy document that contained the amount payable to Westback (Kivisto) from Eaglwing, and Price booked the entry. Price stated that he did not receive any further supporting documentation for the commission amounts that Westback (Kivisto) received. Price acknowledged that this service fee arrangement was not reciprocated, that is, Eaglwing did not receive a commission fee for executing any transactions on Westback's behalf.

During the period from January 2007 through July 2008, there appear to have been over $4.14 million in "service fee" related payments from Eaglwing to Westback (Kivisto) for the oil Kivisto purchased on SemGroup's behalf. Documents obtained from Pens' office reflect a single, nondescript line item with an amount payable to Westback from Eaglwing, indicating no basis for how the amount was calculated. SemGroup was unable to locate any detailed support for these payments, and the other payments delineated in Exhibit 44.

Price stated that one could conclude that Kivisto was acting as an agent for Eaglwing in finding physical barrels of oil for SemGroup, and as an agent for Westback in paying for them and marketing the oil to SemGroup. When asked why Kivisto was receiving a profit from these transactions (through Westback, his alter ego) since he was a SemGroup employee and should have been working on its behalf on these trades, Price opined that Kivisto felt that he was providing his trading expertise to Westback and SemGroup, and that Eaglwing was benefiting from Kivisto's prior contacts within the energy industry. Price stated that since the industry settled physical trades on or about the 20th day of each month, the monthly profit to Kivisto for

these transactions would also be reflected on Westback's General Ledger on or about the 20th of each month.

A review of the Eaglwing and Westback transactions revealed additional payments to Westback from Eaglwing that, according to Price, appear to be settlements for actual barrels of oil purchased, although he was not certain of this. The total amount of those transactions was $21.9 million. SemGroup was unable to provide the Examiner with any supporting documentation for those transactions.

Additionally, a review of the Eaglwing and Westback transactions revealed that Eaglwing recorded a $13.1 million receipt from Westback in the general ledger on July 25, 2007. However, this cash inflow could not be identified on Eaglwing's BOK account statement. Eaglwing then recorded a payment to Westback of $13.1 million on August 20, 2007, as reflected on its BOK account statement.

When asked about these transactions, Price stated that he believed they were related to the closing of the ConAgra account. SemGroup was unable to provide the Examiner with any supporting documentation for them.

(6) Impact of Westback's Accounting on SemGroup

Several SemGroup employees expressed concerns that the trading relationship between SemGroup and Westback made it difficult to report accurately Eaglwing's financial results. For example, Lewallen expressed concern to Stallings when SemGroup was closing its ConAgra account, stating that it was sometimes difficult for her to distinguish Westback transactions from Eaglwing transactions. Lewallen stated that all of the Westback financials and bank accounts

were separate from SemGroup, and that the Westback trades were separated from Eaglwing before the Eaglwing account data was incorporated into SemGroup's books.

Lewallen stated that she first learned about Westback in approximately 2006, when Wallace told her that she would observe that an entity named Westback was conducting commodities trades through Eaglwing in SemGroup's ConAgra trading account. Wallace also told Lewallen that the trading contracts would indicate that the trades were being done by Eaglwing, rather than Westback. Wallace further stated that Pens would provide her with the necessary back-up information for purposes of her reporting. Lewallen told Wallace that she would have to discuss the Westback situation with PwC, to ensure that she reported the Westback transactions properly.

Lewallen brought the matter to the attention of PwC. She told a PwC auditor about the nature of the Westback transactions – that is, there was an outside entity trading through SemGroup, which operated from Pens' office. The auditor stated that he would look into the matter. Pens does not know if the information regarding Westback was already known to PwC. However, she stated that when she looked at that quarter's financial statement, she noted that Westback had been reported through a footnote to the financial statement. The footnote did not specifically identify Westback by name, however, and only made reference to a related party.

Lewallen was responsible for handling requests regarding SemCrude from PwC's auditors. If a request was made that involved a question relating to Eaglwing or Westback, Lewallen would ask Pens and/or Price for the necessary information to answer PwC's question. For example, if the auditor had a question which required reviewing an Eaglwing bank account statement, she would ask Pens about it, because Pens maintained all of the Eaglwing bank

account statements. She would then report what she learned to PwC. As another example, if PwC's auditors asked for a specific trading invoice because they could not follow a particular transaction from inception to completion, Lewallen might speak to Pens about it, and the two of them would make certain that all of the Westback trades had been segregated from Eaglwing. Lewallen stated that this type of situation particularly occurred when SemGroup was attempting to close out its ConAgra trades for year-end 2007.

In approximately February 2008, Lewallen stated that PwC's auditors questioned SemGroup about the collectibility of the Westback receivable, because the amount of it had increased and had not been paid. For that reason, Lewallen stated that Kivisto was asked to provide a personal financial statement to SemGroup to determine if he had sufficient personal assets to cover the amount of the receivable.

Lewallen stated that soon after Wallace spoke to her about Westback in approximately 2006, she also reported the Westback situation to her immediate supervisor, Stallings. Stallings told her that he would look into the situation and see how to handle the accounting. PwC's auditors subsequently mentioned to Lewallen that a contract had been drafted between SemGroup and Westback regarding the relationship between them.

Lewallen stated that she did not know why Westback used Eaglwing to make trades. In her experience as an auditor, Lewallen stated that she had never encountered a similar situation – where an outside entity was permitted to trade through the subsidiary of a parent company. Lewallen felt that her actions in making the Westback relationship known to PwC's auditors and her supervisor, Stallings, were appropriate and reasonable attempts by her to address her concerns about this unusual situation.

Lewallen stated that it was her understanding that Price performed the accounting entries for both the Eaglwing and Westback general ledgers. Price was paid by Pens through a separate account that was not normally used for SemGroup's employees. Lewallen noted that there were some occasions when she was required to remove the Westback entries from the Eaglwing account at the last minute, because Price, who worked part-time, and Pens were not available to do so.

Lewallen advised that Pens would transfer cash between the Westback and Eaglwing ledgers if one of the entities owed the other money because of the Westback trades. Lewallen stated that she never saw any invoices between Eaglwing and Westback, although she did observe some wire transfers between them.

Lewallen stated that from approximately January to March 2008, when SemGroup was attempting to close out all of its ConAgra positions, she was asked to settle the Eaglwing account at ConAgra. In order to do so, she explained that she needed to record the close-out positions as either receivables or payables. She and Pens then reviewed the statement summaries and divided them into Eaglwing, Westback and SemCrude entries. She noted that all three names were listed on the brokerage invoices.

Lewallen stated that either Stallings or Wallace asked her to provide information regarding Westback's daily balances for 2008 to Kivisto, Wallace, Stallings, Perkins and Cooper by e-mail, which she did. She was told the information was being requested because Kivisto was attempting to close out transactions in the Eaglwing 2 account at Merrill Lynch. She obtained the data from Mark Akers ("Akers"), who was a member of SemGroup's risk group. Akers, in

turn, would have obtained the information from broker statements. Lewallen noted that some of the Westback trades were originally made in 2007, when ConAgra was still in operation.

Jamie Cooper stated that Westback's Merrill Lynch trading account (which was referred to as Eaglwing 2) was a sub-account of SemGroup's master Merrill Lynch trading account. She also stated that the Westback transactions were included in SemGroup's margin calculations. Lietzke stated that the MtM adjustments for the Westback trading transactions were carried in SemGroup's derivative liability account, and that Westback's trading margins were posted with SemGroup's trading margins, thereby exposing SemGroup to Westback margin requirements and losses.

Mr. Joseph Tanksley ("Tanksley"), SemGroup's Treasury Analyst, stated that he found it odd that all of SemGroup's business segment accounts had to be swept daily into the SemGroup master account, with the exception of the Eaglwing account. He also found it odd that he could transfer funds into the Eaglwing account, but that the transfer of funds from Eaglwing to SemGroup was only handled by Pens.

(7) Westback's Accounts

Westback had at least three main bank and brokerage accounts: (1) a BOK cash account under the name Westback; (2) a Merrill Lynch brokerage account under the name Eaglwing 2, which was a sub-account of SemGroup's master Merrill Lynch trading account; and (3) a ManFinancial brokerage account.

(8) SemGroup's Receivable from Westback

According to Price, when SemGroup's ConAgra trading account was required to close, there was an in-house dispute regarding what Westback owed to SemGroup because some of its accounts had not been removed from Eaglwing's accounts. After that time, some separate accounts were opened for Westback.

SemGroup's balance sheet accounted for the Westback trading relationship as either an asset or liability – that is, as either an accounts payable or an accounts receivable. Based on the PwC audits, and beginning in approximately 2005, SemGroup began disclosing in a related party transaction footnote in its financial reporting that it had a relationship with a related party. *See* Exhibit 45A. However, it did not name the related party.[7]

The related party transactions footnotes in SemGroup's other Consolidated Financial Statements have substantially similar language. *See* Exhibits 45A, 45C, 45D. It is noted that this footnote appears with several pages of other footnotes regarding related party transactions, and does not readily stand out as being unusual. Moreover, it does not name Kivisto or Westback.

[7] The related party was Westback. For example, the related party transactions footnote in the notes to Condensed Consolidated Financial Statements dated January 30, 2008 and December 31, 2007, states as follows: "The Partnership acts as an agent for an entity owned by certain unitholders and an officer of the Partnership. Under its agency relationship, the Partnership enters into certain derivative transactions with its counterparty on behalf of the related entity. At January 31, 2008, the Partnership recorded on the condensed consolidated balance sheet net accounts receivable from the entity of $49.6 million and $11.8 million payable to the counterparty for transactions completed during 2008. At December 31, 2007, the Partnership recorded on the condensed consolidated balance sheet, net accounts receivable from the entity of $68.6 million and $72.6 million payable to the counterparty for transactions completed during 2007. At January 31, 2008 and December 31, 2007, the Partnership recorded on the condensed consolidated balance sheets accounts receivable from the entity of $213.8 million and $255.3 million, respectively, related to unexpired derivative positions transacted on behalf of the entity and a corresponding derivative liability to the counterparty. There was no impact to the condensed consolidated statement of operations and comprehensive income." *See* Exhibit 45B at page 19.

Stallings noted that during its second and third quarter 2007 reviews, PwC questioned the growth of the Westback receivable, which was confirmed by the Examiner's review of financial statements. As of December 31, 2005, SemGroup's total receivable from Westback was $19.8 million. The receivable amount increased to $136.3 million as of December 31, 2006, and to $323.8 million as of December 31, 2007.

Despite the large receivable due from Westback, SemGroup continued to make large payments to Westback during 2007 and 2008, including payments of $27.3 million and $8.0 million on February 20, 2008, and payments of $5.0 million and $2.7 million on February 29, 2008. In total, between February 20, 2008, and April 18, 2008, Westback received approximately $45 million from Eaglwing.

(9) March 20, 2006 Agreement between Westback and Eaglwing

Stallings stated that the Westback receivable was identified as a potential problem in approximately 2005 by PwC. PwC suggested that SemGroup have a written agreement documenting the relationship between SemGroup and Westback. As a result, Stallings prepared the following agreement on Eaglwing letterhead, dated March 20, 2006 (*see* Exhibit 40), which Kivisto and Wallace signed:

> Re: Contracts entered into by Eaglwing Trading L.P., on behalf of Westback Purchasing, L.L.C. … This letter confirms the understanding between Eaglwing Trading, L.P., an Oklahoma limited partnership ("Eaglwing"), and Westback Purchasing Company, L.L.C., an Oklahoma limited liability company ("Westback"), with respect to those contracts listed on Exhibit A attached hereto and any other contracts entered into by Eaglwing on behalf of Westback (the "Contracts"). When entering into the Contracts, Eaglwing is doing so only as Westback's authorized agent and representative, and all obligations and benefits under the Contracts shall be for the sole account of Westback. If you are in agreement with the contents of this letter, please indicate by signing below and returning a copy to my attention.

The letter agreement is signed by Gregory C. Wallace as Vice President and Secretary of Eaglwing Trading, L.P, by SemOperating G.P., L.L.C., and by Thomas L. Kivisto.

(10) February and March 2008 Westback Documents

Stallings stated that as the Westback receivable amount continued to grow, and particularly after it increased significantly from approximately June 2007 to September 2007, Stallings knew that he had to learn more about Westback. He noted that until that point in time he had assumed that Westback consisted of a group of Kansas oil producers, and that Kivisto had executed trades for Westback and on their behalf. Stallings stated that he had discussed PwC's interest in the receivable with Wallace in early 2007, at which time Wallace stated that he would follow up on the matter. In approximately February 2008, because PwC told Stallings that Wallace had not addressed the Westback receivable with it in sufficient detail, Stallings decided to speak to Kivisto about the receivable.

Stallings asked Kivisto who owned Westback, and Kivisto told him that he (Kivisto) was the sole owner. According to Stallings, that was the first time he knew that Kivisto was the owner of Westback. Stallings then asked Kivisto for a personal financial statement, to use as a form of collateral to establish that the Westback receivable amount could be paid by Kivisto.

A letter dated February 25, 2008 on SemGroup letterhead from Stallings addressed to "Westback LLC, Tom Kivisto, President and CEO" states as follows (*see* Exhibit 46A):

> Our auditors, PricewaterhouseCoopers LLP, are performing an audit of our financial statements. Please confirm the following balances due us as of December 31, 2007 which is shown on our records as:

December Conagra Settlement	$72,581,820
Open Derivative Positions Mark-to-Market Value- Merrill Lynch	227,219,090
Open Derivative Positions Mark-to-Market Value- Conagra	35,809,150
Open Derivative Positions Mark-to-Market Value- SemCrude	2,303,500
Net Payable to Westback LLC	(4,018,607)
Total Net Receivable to SemGroup	$333,894,953

Please indicate in the space below whether this amount agrees with your records. If there are differences, please provide any information that will assist our auditors in reconciling the difference. Please sign and date your response and mail your reply directly to PricewaterhouseCoopers LLP, 6120 South Yale, Suite 1850, Tulsa, OK 74136, in the enclosed return envelope.

Kivisto's signature appears to be signed on the bottom of the document, dated March 18, 2008.

Another version of the document has been located with the following changes: The "Open Derivative Positions Mark-to-Market Value – Conagra" figure is $25,745,700; the "Total Net Receivable to SemGroup" figure is $323,831,503; and Kivisto appears to have signed this version on March 19, 2008. *See* Exhibit 46B.

On March 18, 2008, Kivisto gave SemGroup a personal net worth statement, which indicated that he had a net worth of $252 million. According to Kivisto's net worth statement, this amount was "to be considered . . . available to support the creditworthiness of the outstanding WB [Westback] account receivable." Other information on the personal net worth statement included Kivisto's estimated compensation for 2008 of $15 million and 15,000 barrels of oil a day that Westback "controlled through the Mull, Vess, Murfin, McCoy, LD Drilling relationship."

In a Memorandum dated March 20, 2008 "Re: Evaluation of Westback Credit" to "Files" with a copy designated for PwC (*see* Exhibit 47), Stallings stated that:

> Since inception of SemGroup (the "Partnership") in April 2000, Westback ("WB") has utilized Eaglwing (a wholly owned subsidiary of the partnership) as an agent and representative to enter into and execute trading contracts on its behalf and for the sole account of Westback.
>
> WB is 100% wholly owned by Tom Kivisto and was established to conduct hedging and trading for Tom and on behalf of certain of the Kansas producers (Murfin and Vess). WB primarily consists of a Bank of Oklahoma cash account (see attached – excluded from WB's receivable with SemGroup), Merrill Lynch (ETI2) brokerage account (included in WB's receivable balance with SemGroup) and a Man Financial brokerage account (see attached – excluded from WB's receivable balance with SemGroup). There are no other trading (brokerage) accounts included within WB nor does Tom maintain any other derivative positions outside of these accounts. Further, WB at 2/29/08 has no liabilities other than the amounts due SemGroup.
>
> In our Related Party Transactions footnote of our consolidated financial statements we disclose the agency relationship and the respective amount of net accounts receivable/payable related to current monthly settlement amounts and a net receivable amount related to unexpired derivative positions transacted on behalf of WB.
>
> The following table details amounts recorded in our financial statements at December 31, 2005, 2006, and 2007:

(in Millions)	2005	2006	2007
Accounts receivable/(payable)	($8.4)	$40.6	$68.5
Accounts receivable related to the mark-to-market value of unexpired derivative positions	28.2	95.7	255.3
Total receivables	$19.8	$136.3	$323.8

> As a result of the growth in the amount of the total receivable we believe it necessary to examine the financial wherewithal of WB to determine whether it is a reasonable credit risk to the Partnership.
>
> We are considering the assets of WB and of Tom personally in determining the overall credit worthiness of the account receivable from WB. This assumption and conclusion has been confirmed and acknowledged in writing by Tom.

> Tom provided us a summarized financial statement (see attached) which detailed his combined financial position as of February of 2008. . . . In the overall assessment of the net $323.8 million receivable at 12/31/07 . . . the following was performed/considered . . .
>
> • Obtained bank statements and records substantiating that in January, WB paid $72.6 million of cash to settle December Conagra activity. Per discussion with Tom the proceeds used to settle the $72.6 million were derived from a combination of prior option sales to Conagra and personal funds.
>
> • After payment of the $72.6 million and other January activity the total amount of the WB receivable at January 31, 2008 was $264.4 million, a reduction from the December receivable of $69.5 million. [sic]
>
> • Obtained bank statements and records substantiating that in February of 2008, WB paid $11.8 million to settle January Conagra activity.
>
> • Obtained bank statements and records substantiating that in February of 2008, WB paid an additional $18 million to settle a portion of the February – July Conagra activity that was settled in total by the partnership in January of 2008.
>
> • The balance of the WB receivable at February 29, 2008 is $265.6, remaining consistent with the balance at January 31, 2008. . . .
>
> My conclusion is that as of December 31, 2007, the overall creditworthiness of WB and Tom Kivisto considered in aggregate is adequate to support the amount of the receivable. . . .

See Exhibit 47.

After "testing" the Westback receivable as of December 31, 2007, PwC concurred with SemGroup's assessment that no impairment of the Westback receivable balance was required. It relied upon Stallings' evaluation of Kivisto's creditworthiness.

Stallings stated that it was clear from the financial statement provided by Kivisto that his largest asset was his ownership in SemGroup. Stallings subsequently asked Kivisto for and received additional information regarding his personal assets and copies of his income tax returns.

Although Stallings believed that the Westback situation was unusual, he did not view it as a major problem until the receivable became larger and questions were raised about its collectability. Stallings stated that at the end of 2007, he asked Lewallen to track the Westback receivable balance on a daily basis, and to send e-mails to Kivisto, Wallace, himself, and possibly others, about the balance.

(11) July 14, 2008 Invoice from SemGroup to Westback

Stallings stated that, by the week of July 14, 2008, the balance due from Westback to SemGroup was approximately $290 million. At that time, Wallace asked Stallings to prepare an invoice for the Westback receivable to Kivisto. Stallings believes that the July 14, 2008, invoice was the first invoice ever issued to Westback.

The invoice, dated July 14, 2008, and noted as "INVOICE #001" was presented to Kivisto. *See* Exhibit 48.

An undated and unsigned SemGroup document apparently prepared for presentation to the Management Committee and others on or about July 16, 2008 (*see* Exhibit 49) states in part as follows:

> Because these derivative transactions are currently in a realized loss position, *the economic effect of the transactions is that the Partnership has been effectively extending credit to Wesback [sic] by placing these trades and funding the related required margin in offset for the physical lease crude*. (Emphasis added).

The document goes on to state that "[t]he Partnership has informed Wesback [sic] that the Partnership will no longer hold or enter into derivative transactions for the account of Wesback [sic] and has presented an invoice in the amount of $289,990,637." *See* Exhibit 49.

(12) Concealment of Westback

Mr. Peter Schwiering ("Schwiering"), SemGroup's Vice President for Operations, stated that he had never heard of Westback. Schwiering stated that he was amazed that Kivisto was engaged in personal commodities trading, and that he felt betrayed by him. He also felt that Kivisto was spending too much time on his outside interests.

Spaugy, SemGroup's Vice President of Finance, stated that he had never heard of Westback until after July 22, 2008. Prior to July 2008, he became aware of a large receivable due SemGroup from Kivisto and asked Cooper about it. Cooper brushed off the question, responding somewhat flippantly that Kivisto would be able to resolve the receivable by additional trading.

Lietzke stated that he first became aware of Westback when he became SemGroup's Comptroller in June 2007. He also stated that he had expressed a concern to other SemGroup managers about Westback being personally owned by Kivisto.[8]

Ronan, who joined SemGroup in March 2008, stated that he considered Westback to be a "top secret" operation within SemGroup. He stated that it was owned by Kivisto with the agreement that he would keep it separate from SemGroup. Ronan stated that he once asked

[8] An e-mail dated May 16, 2008 from Lietzke to Kivisto regarding "MD&A Language" states, in part: "PwC wants the new language . . . 'We utilize futures and options contracts to minimize our exposure to market changes. . .to enhance our gross margins on our purchased petroleum products and to manage our liquidity risk associated with margin deposit requirements on our overall derivative positions' Alex and Brent are ok with the language. Are you comfortable with us stating we enhance our margins with futures and options and use these contract [sic] to help manage our liquidity risk associated with margin deposits? . . . PwC['s] . . . contention with the old language has been we do more than just manage our price risk. A component of our strategy is to enhance our margins with the options program and use derivatives to help manage our margin deposits. . . ." Kivisto replies "Great. I'm good." *See* Exhibit 50.

Cooper if he (Cooper) knew anything about Westback. Cooper's reply was, "You don't want to know what it is."

Mr. Eric Dreyer ("Dreyer"), an IT analyst at SemGroup, stated that he first became aware of Westback sometime in 2007, when a trade between SemGroup and Westback showed up on a report generated by one of the computer programs he was working on. The report listed Pens as the contact person for Westback.

Coen stated that the trades he conducted for Westback were executed solely at Kivisto's direction. Coen saw himself as someone who merely executed transactions when it came to Westback. Coen was unaware of who paid the margins on the Westback trading book.

Brochetti stated that he knew about the existence of Westback from disclosures in the company's financial statements. He also knew that it was owned by Kivisto, although he did not know its ownership structure. He stated that he was unaware of Westback's relationship with SemGroup. He further stated that he did not know who maintained the books and records for Westback, and he did not know of any invoices between Kivisto, Eaglwing and Westback.

(13) Profitability of Eaglwing and Westback

Price stated that Eaglwing's profits became a significant part of SemGroup's profits. Price estimated that for approximately three years (possibly 2003, 2004, and 2005), Eaglwing and Westback had annual profits of many millions of dollars, and he estimated that Westback's profits were about a fourth to a third of Eaglwing's profits.

A 2006 Partnership U.S. Tax Return for Westback lists business income of $26.26 million. The tax matters partners, each of whom had a 50% interest, were listed as Thomas L. Kivisto and Julie Kivisto.

(14) Pertinent Reference to Eaglwing and Westback in Evergreen's Report

BOA commissioned Evergreen to conduct a financial examination of SemGroup. *See* Exhibit 51 (describing the scope of the examination). Evergreen identified Eaglwing and Westback in its report.[9]

(15) Baker Botts Draft Document Regarding Westback

An e-mail from Cooke to Kivisto, with the subject "Drafting Session," dated July 1, 2008, states as follows: "This is what went to the GSTru team. So far as I know it has not gone to the Board." *See* Exhibit 52. An attachment to the e-mail, entitled "Draft Westback Disclosure DOC," contains a Baker Botts draft document, dated June 30, 2008, which states as follows:

> In August 2000 Seminole Transportation and Trading, Inc ("STT"), an entity in which Mr. Thomas L. Kivisto, our Chief Executive Officer, owned a significant interest, was merged with Eaglwing Trading, Inc., a company which was then wholly owned by Mr. Kivisto. Following the merger, Mr. Kivisto and his spouse

[9] Specifically, the report states that: "Eaglwing is the entity that handles the trading activity for SemGroup. Eaglwing does not maintain any product inventory or operating assets other than Accounts Receivable. Eaglwing is housed in the Tulsa home office . . . Eaglwing Trading's ("ETI" or "Eaglwing") primary business relates to trading activity that results in the physical movement of crude oil . . . As ETI has no assets to store any excess products, [Eaglwing] tries to balance its trading and sells excess product to sister companies merely for storage purposes. . . ETI generates its monthly settlements between its trading partners, counterparties, other customers, and suppliers in the same manner as SemCrude. Trading partners that both purchase and sell crude to Eaglwing (counterparties) are netted on the 20th and settled through the federal banking wire system . . . . The receivables are netted out prior to inclusion in the borrowing base . . . .The examiner [Evergreen] obtained the reconciliation for billed and unbilled receivables outstanding as of December 31, 2007 . . . ." Under reconciling items, the following information is noted: "Accrued AR (Westback) $258,429,[000] . . . The reconciling items noted above are not included in the borrowing base." Under "Sales Concentration by Customer (ETI)" through fiscal year ended December 2007, Evergreen listed SemGroup's top three customers, by percentage of sales, as ConAgra Trade Group Inc. (91%); Plains Marketing (5.5%); and Westback Purchasing Co LLC (1.1%). *See* Exhibit 35, at pages 33, 35.

and trusts which they control, continued to own all of the equity interest of another company, WestBack Purchasing L.L.C. or "WestBack", a company which had significant relationships with several Kansas oil producers. WestBack controlled the marketing rights to approximately 16,000 Bbls of crude oil per day and had a significant line of credit. This line of credit was used extensively to support trading in oil derivative transactions by WestBack and by STT and SemCrude, L.P., which is a wholly-owned subsidiary of the Partnership. Initially, both WestBack and SemCrude established accounts with Conagra, Inc.

In (•) ConAgra required the consolidation of these accounts. As a result, it was determined that a portion of these trading activities would continue to be conducted for the account of WestBack, with WestBack (rather than our Partnership and initial investors) ultimately funding any losses and bearing the other risk of loss. These derivative transactions are similar in nature to those entered into on an ongoing basis by the Partnership as part of its trading and risk management activities. As the Partnership has grown, a greater proportion of the derivative trading activities have been conducted by the Partnership for its own account as part of its trading and risk management activities, although a number of derivative transactions have continued to be conducted for the account of WestBack. In 2007 Conagra elected to reduce (and ultimately eliminate) its trade book. Westback and the Partnership elected to move all positions held by the Partnership [but Westback was left at settlement in 2007] with a strongly negative position.

These derivative positions have consistently been included on the Partnership's balance sheet as an asset or liability, offset by a corresponding amount of accounts payable to or accounts receivable from WestBack. As of March 31, 2008 and December 31, 2007, these derivative positions had a negative value, and the Partnership's balance sheet reflected accounts receivable from WestBack of $255.9 million and $255.3 million, respectively, with a corresponding derivative liability relating the positions [as well as $ ___ and $ ___ of margin deposits, respectively, associated with these derivative positions]. Because these derivative transactions are currently in a loss position, the economic effect of the transactions is that the Partnership has been effectively extending credit to WestBack by placing these trades and funding the related required margin deposits. See Note 13 to the audited annual and unaudited interim financial statements included elsewhere in this offering circular for additional information on the financial statement treatment and impact of these transactions.

Concurrently with the closing of this offering, the Partnership will enter into a credit facility in the nature of a secured account receivable facility, which we refer to as the "WestBack Credit Facility," with WestBack which will provide WestBack with the opportunity to reduce and ultimately eliminate the WestBack trading activity over time in an economically beneficial manner. Pursuant to the WestBack Credit Facility, the Partnership will provide Westback with a $330 million revolving facility loan, and WestBack will use borrowings under the revolving facility loan to fund payment of the receivable to the Partnership and to

satisfy margins in its trading account (which will be limited by the size of the facility). Mr. Kivisto will use the proceeds he receives from the sale of his interests in SemGroup G.P., L.L.C. and his Class A Units in the Partnership to SemGroup, Inc. in this offering, plus additional funds to repay ($•) million of the outstanding borrowings under the WestBack Credit Facility, which will permanently reduce the commitment. In addition, the commitment will be reduced over the term of the facility as follows: from January 1, 2009 to June 30, 2009, the commitment will be $197.5 million; from July 1, 2009 to December 31, 2010, the commitment will be $165.0 million; from January 1, 2010 to June 30, 2010, the commitment will $132.5 million; and from July 1, 2010 to December 31, 2010, the commitment will be $100.0 million. On December 31, 2010 the WestBack Credit Facility will terminate and all amounts outstanding thereunder will be due and payable.

Mr. Kivisto and his family members will pledge all of the partnership interests they hold in the Partnership, and WestBack will pledge all of its assets (with the exception of some illiquid minority interests in partnerships), as collateral (the "Collateral") for borrowing under the Westback Credit Facility. In addition, Mr. Kivisto will guarantee the facility.

In addition, WestBack will transfer the right to receive hydrocarbon production from certain leases and wells to the Partnership and the Partnership will pay WestBack ($•) for each barrel purchased by the Partnership. The amount actually paid by the Partnership to WestBack will be netted against the interest owed by WestBack to the Partnership under the WestBack Credit Facility.

Following this offering, WestBack will continue to enter into, exit and settle derivative transactions in its own name as part of a strategy (the "Trading Strategy") designed to provide WestBack with the opportunity to reduce or eliminate the aggregate negative net value of the derivative transactions entered into by the Partnership from the account of WestBack.

These arrangements present a number of risks that you should carefully consider before investing in Class A Common Stock, including the following:

The Trading Strategy will require Mr. Kivisto's significant time and attention, which could otherwise be devoted to our business.

Mr. Kivisto is our CEO and President, as well as a director, and has been central to our formation and success throughout our history. We depend on his continued attention and performance to meet the challenges and complexities of our business. In particular, Mr. Kivisto [manages/oversees] the risk management aspect of our business, including the use of derivatives to reduce our exposure to commodity price changes, protect margins and manage liquidity risk. Mr. Kivisto will have a significant personal incentive to devote a substantial amount of his time and attention to managing the Trading Strategy in a manner so as to minimize his personal exposure and protect the Collateral. It is possible that these

efforts will reduce the time and attention that he devotes to our business, which could adversely impact us.

The Trading Strategy may create conflicts of interest for Mr. Kivisto.

The transactions that Westback enters into under the Trading Strategy will be largely similar in nature to activities that we engage in on a day-to-day basis as part of our risk management efforts, which are also managed by Mr. Kivisto. It is possible that particular transactions or opportunities may arise that would be beneficial for the Partnership to enter into as a business matter but that also would be beneficial to the Trading Strategy. [While we have policies in place with respect to the appropriate allocation of opportunities,] it may be difficult for us to monitor compliance with these policies in all cases or to determine whether Kivisto is favoring the Trading Strategy over our business interests in entering into derivative or other transactions. Any such misallocation of opportunities could materially adversely affect our financial condition or results of operations, including our risk exposure and our liquidity. [Describe any policy relating to allocation of corporate or trading opportunities.]

If the Trading Strategy is unsuccessful, the Collateral may not be adequate to cover our remaining exposure under the WestBack Derivatives.

If the Trading Strategy does not succeed in causing the WestBack Derivatives to have a non-negative net value within the three years following consummation of this offering, then our primary recourse will be the acquisition of the Collateral and pursuit of the guaranty. While the acquisition of the equity interests constituting the Collateral will reduce our amount of equity outstanding and thereby have an antidilutive effect on our other equity holders, including holders of the Class A Common Stock, there can be no assurance that this will be sufficient to offset any losses the Partnership may incur in connection with the WestBack Credit Agreement. To the extent the negative value of the WestBack derivatives exceeds the positive value of the Collateral, the difference will remain an accounts receivable from Mr. Kivisto and WestBack. This accounts receivable will be uncollateralized and the Partnership will be subject to the credit risk of Mr. Kivisto and WestBack; there can be no assurance that the Partnership will be able to collect these amounts following a default. [adds risks to pursuit of guaranty]

In the event of a default on the Pledge, Mr. Kivisto's equity stake in our business will be reduced, possibly to zero.

The members of our senior management, including Mr. Kivisto, have been and are generally expected to continue to be significant equity holders in our business. We believe that this helps motivate our management and aligns their interests with those of shareholders. [We expect a significant component of Mr. Kivisto's compensation on an ongoing basis to arise from earnings on, and value increases of, his equity interests in our business.] In the event of a default under the

> WestBack Credit Agreement, Mr. Kivisto will forfeit some or all of his equity stake to our business. [Mr. Kivisto is not contractually bound to continue to work for us, and there can be no assurance that he will determine to continue to devote his time and attention to our business in the event that his equity stake in our business is significantly reduced, unless alternative compensatory arrangements are successfully negotiated between him and us.] The loss of Mr. Kivisto's services, or any additional compensation (including equity grants) required to retain him, could materially adversely impact our financial condition or results of operations.
>
> **[Add other risks depending on nature of arrangements, such as (i) credit facility having a maximum amount that may not be adequate to fund all margin deposits, (ii) any requirements from Merrill Lynch to move the account, (iii) changes in market regulation, (iv) if the trading account is not denominated in WestBack's name and (v) whether the Partnership is still liable for margin calls.]**

See Exhibit 52. (Emphasis in original)

(16) Westback's influence on SemGroup's Financing Options – GS TruE

As reflected in Cooke's July 1, 2008, e-mail and its June 30, 2008 Baker Botts attachment, noted above (*see* Exhibit 52), Cooke forwarded to Kivisto a draft of what SemGroup had already furnished to Goldman, in an attempt to mitigate Goldman's concerns about Kivisto's Westback receivable.

Goldman, as part of its due diligence, had a meeting with PwC, SemGroup's auditors, which SemGroup was not permitted to attend. During this meeting, Goldman learned about Westback. PwC explained that Westback was a legacy company owned by Kivisto, which conducted its commodities trading through SemGroup, and that it currently owed SemGroup approximately $260 million. This revelation was a major concern to Goldman, and Goldman subsequently advised SemGroup that it could not market the equity offering with Westback on its balance sheet.

Goldman suggested to Kivisto that SemGroup attempt to obtain third party financing to pay off the Westback account, and then proceed with the GS TruE offering. However, credit markets were tight and several months elapsed without SemGroup obtaining the necessary funds to do so. In approximately late May 2008, Goldman proposed an alternate plan to remedy the Westback issue. It suggested that SemGroup and Westback formalize an agreement in which Westback would stop all trading and pay off its debt to SemGroup over a two year period.

During this same time period, Goldman and SemGroup personnel (including Kivisto and Wallace) traveled to the Middle East in an attempt to obtain an "Anchor Investor," which is a standard practice for this type of offering. They visited several countries, including Kuwait, with the goal of raising an initial $500 million. Kuwait's investors appeared to have the most interest. Goldman participated in only one trip, but SemGroup representatives made additional visits to Kuwait. The attempts to obtain initial investment capital were unrelated to Westback, and those funds, had they been obtained, were not intended to pay off the Westback receivable.

Several documents containing analysis and presentation materials for GS TruE have been located. One of them, dated May 19, 2008, entitled "GSTruE Equity Offering Underwriter Due Diligence," summarizes SemGroup's business units, operations, etc., and notes SemGroup's attempts to "minimize exposure to commodity price risk by . . . option contracts. . . ." *See* Exhibit 53 at page 16. *A second document, entitled "Preliminary Valuation Analysis, Goldman Sachs & Co., June 2008," contains "Summary Observations and Considerations," including the consideration that "significant marked to market accounting differences arise between the mismatch between physical transactions and financial derivatives. . . ." See* Exhibit 54. A third document, dated June 2008, is a SemGroup proposal for presentation to Kuwait Petroleum. S*ee* Exhibit 55.

In June 2008, the Westback issue had still not been resolved. According to Goldman, other concerns about SemGroup's financial picture, including its liquidity, had also surfaced. In early July 2008, Goldman advised SemGroup that it had decided to cancel its interest in GS TruE.

Foxx stated that there were discussions during the GS TruE negotiations about Goldman providing a loan to Kivisto to pay off the Westback receivable. In order to do so, Kivisto was willing to sell all his stock in SemGroup to pay off the debt. However, the Goldman loan was never consummated.

Stallings confirmed that Goldman made data requests to SemGroup during its due diligence inquiry regarding the types of trades that SemGroup had entered into, including a break-down by commodity type and types of positions.

(17) MC knowledge of Westback

(a) Thane Ritchie

Ritchie stated that he first heard of Westback in mid-July 2008, during the week preceding the Debtors' bankruptcy filings, when Ritchie was on a conference call led by a Blackstone representative. During this call, Wallace read a letter, the substance of which was that Kivisto owed SemGroup approximately $300 million. Ritchie asked for further clarification, but he did not get an answer before Wallace left the room.

Stallings then came in and stated that Kivisto had guaranteed a $300 million dollar loan with his personally owned stock, and that Stallings had not previously thought that the transaction had to be disclosed to the MC. Ritchie then asked if there were any other conflicts of

interest, and Stallings mentioned Lean Gourmet. Stallings expressed the view that Lean Gourmet was not material, and that only the Westback receivable was an issue. The Blackstone representative then stated that he had seen a document in which a two-paragraph footnote purportedly disclosed the Westback receivable, but that "it would take a genius" to fully understand what was being disclosed in the footnote.

Stallings stated that SemGroup's auditors were aware of the receivable, but were unaware that trading had caused it. Ritchie had the impression from this account that Kivisto's debt had grown dramatically over time.

In his July 1, 2008 e-mail, Cooke commented that the June 30, 2008, Baker Botts draft had not been sent to the "Board" (SemGroup had a MC rather than a board of directors because it is a partnership). *See* Exhibit 52. This e-mail is consistent with the statements of the non-management members of the MC that they were unaware of the full nature of Westback or of the large receivable owed by it to SemGroup, until July 2008.

(b) Andrew Ward

Ward stated that he was "familiar" with Westback through the initial due diligence conducted by Riverstone prior to its investment in SemGroup. Ward stated that he became aware of Kivisto's employment agreement, which referenced Westback, as a result of the due diligence process, sometime before January 2005.

According to Ward, Westback was never discussed at the MC level. Ward stated that he was unaware of the Westback receivable until days prior to the filing of the Debtors' bankruptcy petitions, and that it was unclear that it would have an impact on SemGroup's balance sheet.

Ward stated that the MC should have been told about the Westback arrangement much earlier, and that SemGroup, including its outside accountants (PwC), had an obligation to do so.

(c) Bartow Jones

Jones stated that he participated in numerous meetings on July 15 and 16, 2008, at SemGroup's office in Tulsa, Oklahoma. On Wednesday, July 16, 2008, members of the MC were advised that Westback, which Kivisto owned, owed $289 million to SemGroup. Jones was previously unaware that Kivisto owned Westback or that this receivable existed. Jones stated that, as a MC member, he would never have approved this kind of a business relationship or allowed it to exist.

Jones advised that SemGroup's relationship with Westback should have been disclosed more clearly to the MC. Allowing Kivisto to personally trade with SemGroup funds, thereby effectively extending credit to Kivisto (by way of Westback), served no business purpose or function. Jones explained that a company, such as SemGroup, might be compelled to extend credit to a business that it might earn income from, upon full disclosure of the nature of the relationship. However in this case, Jones stated that SemGroup could not have earned any income from the Westback relationship, and the best that SemGroup could hope for was to have its money returned to it.

(18) Michael Vess

Vess advised that Kivisto approached him in 2000 about the purchase of a small oil company named Dynegy. Vess provided a portion of the financial backing to purchase Dynegy and, as a result, was a percentage owner in what later became SemGroup. Vess could not recall

what percentage he owned, although he made a number of capital calls and increased his investment in SemGroup. His investments in SemGroup came from three separate sources: Vess Energy Group, Eaglwing Energy, and his personal accounts. Vess indicated that Eaglwing Energy, which was never affiliated with SemGroup, ceased to exist when SemGroup filed for bankruptcy protection.

Vess stated that he was familiar with the name "Westback," as it provided financial backing for some of Vess Oil's drilling projects. Vess explained that Westback purchased working interests in some oil wells that Vess Oil had drilled. He also stated that there were a few instances when Kivisto hedged some of his oil using Westback.

Following SemGroup's bankruptcy filing, Vess spoke with Kivisto. Vess stated that he offered to buy Kivisto's Westback position in one of Vess' business interests at that time.

Vess recalled receiving a mailing dated July 10, 2008, from SemGroup, referencing a capital call in the amount of $400 million. Vess stated that he attempted to put together a group of investors in response to the letter, but was unsuccessful.

m) The ConAgra Exchange

In late 2007, ConAgra decided to exit the commodities futures trading business. Coen stated that SemGroup was disappointed by ConAgra's decision, due, in part, to the work involved in moving all of SemGroup's trades from the ConAgra account to a NYMEX account. Also, NYMEX's changing margin requirements were more challenging than ConAgra's margin requirements.

n) SemGroup's Other Accounts

SemGroup had trading accounts with six brokerage facilities. Several of them, including those noted below, were identified as having concerns in 2008 about their respective SemGroup accounts. Also, one of SemGroup's counterparties, Magellan, had similar concerns. Representatives of those brokerage facilities and Magellan were interviewed by the Examiner, and they provided specific information regarding their concerns and actions in the months leading to SemGroup's bankruptcy filings.

(1) With Prudential Bache Commodities, LLC (PBC)

On January 31, 2007, SemGroup opened an account with PBC. When the account was opened, SemGroup executed a "Hedge Account Agreement," in which SemGroup certified that the account would be used for "bona fide hedge transactions," which enabled SemGroup to receive more favorable terms and margin requirements. When the account was opened, PBC conducted its customary new account due diligence investigation, which focused heavily on creditworthiness.

PBC's representative assigned to the account had his first personal contact with SemGroup representatives in March 2008. Due in part to the volatility of the credit and futures markets, PBC was looking at some of its larger accounts with large exposures. PBC met with Wallace, Cooper, Ronan, and Allen at SemGroup's Tulsa office. Kivisto was not physically present for the meeting. During the meeting, the management team members repeatedly assured PBC that all of SemGroup's trading was hedged and that they were not making speculative trades. SemGroup's management team provided very little detail, however, and PBC was concerned that they might not be aware of what was actually happening. It was also PBC's

impression that SemGroup was a "one man show." PBC requested that SemGroup provide it with a copy of SemGroup's written RMP.

The PBC representative had numerous follow-up telephone conversations with SemGroup regarding certain trading positions that SemGroup held. According to PBC, SemGroup consistently advised that its positions, which might appear to be speculative, were offset by gains in the physical market or by trading positions SemGroup held with other Futures Commission Merchants ("FCMs"). SemGroup traded with several FCMs and therefore PBC contended that it was impossible for PBC to verify what positions it held with another FCM or how much physical crude oil SemGroup owned.

An April 17, 2008 e-mail from PBC to Kivisto read in part as follows: "Our review began on March, 19th when several senior members of our team visited your office. . . . One of the most important aspects of our continued review will be our meeting on April 30, 2008 when we meet with you, your head trader, and risk management. We have identified several questions or issues still unresolved. . . ." *See* Exhibits 29A and 29B.

During May 2008, PBC was still concerned about the SemGroup account. On May 7, 2008, PBC sent another e-mail to Kivisto, requesting an explanation of SemGroup's trading policy.[10] *See* Exhibit 30.

[10] The e-mail states as follows: "[T]he Head of our risk department has the following questions. As we initially stated during our recent due diligence visit to Semgroup our primary concern is the naked selling of short options. We have reviewed extensively your firm's risk management policy which you recently forwarded to us. As specifically underscored in paragraph 2.6 your policy states it is Semgroup's policy not to sell naked options. The policy further states that options can only be sold to offset other positions or as part of a 'defined marketing program' approved by you (CEO). The positions currently on with Prudential clearly indicate a large naked option position where Semgroup is substantially short volatility which would not appear to be hedging any physical assets. As an example on April 30, SemGroup sold short 1000 calls and also sold short 1000 puts for the same expiration date (Dec 08) and at the same strike price of 113. We therefore request

PBC subsequently had a telephone conversation with Kivisto regarding its concerns. During the telephone conversation, Kivisto conceded to PBC that the SemGroup trading policy was not 100% hedging, but stated that it was also not 100% speculative. Kivisto stated that SemGroup's trading policy was somewhere in the middle, and he claimed that SemGroup had offsetting positions elsewhere. PBC considered Kivisto's responses to be very vague, which added to its concerns.

During May and June 2008, PBC began to ask SemGroup to reduce some of its trading positions. Although PBC asked SemGroup to provide details to support its inventory claims, SemGroup never did so. PBC then advised SemGroup that it would terminate its relationship with SemGroup unless SemGroup reduced its trading positions. However, SemGroup continued to make the required margin payments on its account.

A June 19, 2008 e-mail from Spaugy to Cooper stated in part, the following: "have we started the process of winding down the Prudential account per their guidelines . . ." *See* Exhibit 56.

(2) With Calyon

Calyon entered into its first lending relationship with SemGroup in November 2007, when it committed to $50 million of the increase of the $1,420 million working capital facility, and $50 million of the increase of the $495 million revolving credit facility, as part of the $2,115 million senior secured credit facility.

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that you specifically explain how these short option positions currently executed via Prudential are within your firm policy guidelines and related to a hedging strategy as opposed to directional trading risk. . . ." *See* Exhibit 30.

A Calyon representative stated that SemGroup had been on Calyon's prospect list for some time prior to fall 2007. As part of its due diligence, Calyon's representatives visited SemGroup offices in Tulsa during the third week of September 2007. During the visit, they had meetings with Wallace, Perkins and, possibly, Cooper. One of the primary focuses of their due diligence investigation was to be absolutely certain that SemGroup was not involved in speculative trading. The due diligence investigation did not produce any surprising information and Calyon believed SemGroup's assurances that it was not speculating. A secondary goal of the due diligence review was to understand the amount and quality of the collateral pledged by the company. Calyon did not recall hearing anything about Westback during its due diligence review. If Calyon had heard anything about it, it would have been a concern that would have resulted in additional investigation by it. The results of Calyon's due diligence review determined that Kivisto was well regarded in business circles and in the community.

Calyon entered into the SemGroup Pre-Petition Credit Agreement during November 2007, and entered into an ISDA agreement with SemGroup and began making crude oil trades in the OTC Market. During the period from January 15, 2008 through January 25, 2008, Calyon made approximately 14 trades with SemGroup. Calyon stopped at that time because SemGroup's $100 million trading facility had been completely utilized.

During March 2008, Calyon representatives again conducted a due diligence visit to SemGroup offices in Tulsa. They met with Cooper, Perkins, Oven, Brochetti and Kivisto on that occasion. During the meeting, Kivisto gave an explanation of SemGroup's business and trading strategy. Kivisto's explanations were "circular" and not straightforward, and the Calyon representatives became uncomfortable with his account. Kivisto's explanation of SemGroup's trading strategy appeared to be incomplete, and Calyon believed that some of the SemGroup

representatives, Oven in particular, didn't seem to have a strong understanding of what Kivisto was saying. Based on the meeting, Calyon decided it would not make any additional trades with SemGroup until it knew more about SemGroup's trading practices. At the conclusion of the meeting, SemGroup agreed to provide Calyon with additional information regarding its trading book. However, it did not do so.

During June 2008, SemGroup wanted to roll its January trades at Calyon at the original strike price. Calyon did not authorize those trades and did not understand why SemGroup wanted to make them, noting that, while "rollovers" of options are not illegal per se, Calyon wanted to satisfy itself that SemGroup was not rolling over its options trades to disguise an unhealthy financial condition.

Calyon sent an e-mail to Perkins, dated June 23, 2008, stating that Calyon had a problem with the proposed trades. *See* Exhibit 57. It resulted in a meeting on June 30, 2008, at the Calyon Bank in New York, among Calyon representatives and Kivisto, Perkins and Ronan. SemGroup renewed its request that Calyon roll the January trades at the original strike price. Calyon advised SemGroup that it would not consider rolling the trades at the original strike price, but it would consider rolling them if SemGroup could explain how its trading was hedged and not speculative. Kivisto attempted to explain the SemGroup trading strategy, and it became clear that the proposed trades were not hedged positions. Kivisto claimed to have "wings," which he described as a reverse of the open positions that SemGroup held with Calyon. Calyon representatives felt that since Kivisto was "in the business," he should have been able to clearly describe what he was doing with SemGroup's trading strategy. At the conclusion of the meeting, Calyon advised SemGroup that it would consider the requested trades only after examining SemGroup's trading book and physical inventory on hand to determine that the trades were not

speculative. SemGroup promised to make the book available to Calyon, however, Calyon did not receive it from SemGroup. Calyon never made a determination of whether SemGroup was hedging or speculating with its trades, but it became convinced that it should not make any further trades with SemGroup. The trades were not rolled and SemGroup filed for bankruptcy protection a few weeks later.

A Calyon representative advised that he first remembers hearing about Westback during a bankers' conference call with SemGroup on July 15 or 16, 2008. The conference call was led by BOA and included many of the banks that were part of the credit facility that was managed by BOA. During the conference call, there was a discussion regarding the SemGroup receivable from Westback that had resulted from Westback's trading activities through SemGroup. Calyon's representative had been previously unaware of it and believed that the other bankers participating in the call were unaware of it as well. During the conference call, Wallace told the bankers that they should have known about it, because it was mentioned in a footnote in SemGroup's financial statement. Calyon and many of the bankers were outraged by Wallace's contention.

Calyon subsequently reviewed the footnote and believes it was inadequate. Calyon explained that it is not unusual for a company to do business with their CEO; however, it is a matter that, if known, would be thoroughly examined during a due diligence review. Particular emphasis would be placed on the nature and amount of the relationship relative to the size and value of the company. If Calyon had known about the SemGroup relationship with Westback, it would have been a matter of "tremendous concern" to it. Calyon believes that the Westback relationship should have been "put on the table" by SemGroup, rather than it relying on the bankers' ability to uncover it by independent means.

Calyon was familiar with the provisions prohibiting speculative trading in the Pre-Petition Credit Agreement. Calyon had access to the weekly position reports; however, Calyon believes that the reports did not provide sufficient information to make a determination regarding speculative trading. Calyon believes that SemGroup's statements that it ran a hedged book and that it did not speculate were false.

(3) With Magellan

In May 2008, Magellan, a Tulsa-based midstream energy company, noticed a negative cash flow that was apparent from its analysis of SemGroup's financial statements. As a result, it began a due diligence inquiry of SemGroup. After Magellan made contact with SemGroup officials (Spaugy and Lietzke), and based upon the due diligence it conducted, Magellan became uncomfortable with SemGroup's financial stability, and it made the decision not to enter into any additional contracts with the Company.[11]

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[11] An e-mail from Lietzke to a representative of Magellan and Spaugy, dated May 15, 2008 (*see* Exhibit 58) states in pertinent part as follows: "Your question on how do we get comfortable with the negative operating cash flow is the same question our auditors ask. Generally, we would expect to have positive operating cash flow before the effects of changes in working capital. I look at working capital in two components – margin deposits and everything else. The margin deposits is a function of our open positions which I will discuss shortly. The remaining changes in working capital I would expect to be negative each year, and I expect it will continue in the future for 2 reasons. 1. we expect to continue growing our business. We have increased our storage capacity from 3 million barrels in 2002 to nearly 40 million barrels in 2008. Along with this storage be [sic] buy, store and market more and more product every year. . . . Crude oil has increased from $65 a barrel a year ago to $125 a barrel today. . . . We continue to buy, store and market a high volume of commodity products. . . . For margin deposits, this has been the primary item to impact our operating cash flows for 2007. We enter into derivative positions to manage our commodity price risk on the petroleum barrels we buy, store and market. These derivative positions have been significantly impacted over the past 6 months or so since Crude has run from $65 a barrel to $125 barrel. This increase in commodity prices resulted in a $1 billion unrealized loss in 2007. We are required to post margin on our derivative positions. Typically, we are 100% collateralized on our derivative positions. Therefore, when we incurred the $1 billion unrealized loss in 2007, we were also required to post about the same amount in margin requirements. Margin deposits do pose a liquidity risk for us as you pointed out. Once Crude hit about $90 barrel, we began and continue to enter into derivative positions to manage our margin deposits. *In essence, we have bought contracts that if the market blows out, these contracts will create cash flows to offset the margin calls on our existing positions.* Basically, we have bought insurance or protection from liquidity risk for our margin deposits. This has been working very effectively for the past several months. Our Treasury group manages this very closely on a daily basis,

(4) With J. Aron

A representative of J. Aron, a wholly owned subsidiary of Goldman stated that in early 2007, SemGroup's SemStream business unit came to its attention as a potential customer. An account was opened at J. Aron in the name of SemGroup, sometime in mid-2007.

J. Aron provided hedging services, and SemGroup was already involved in that type of trading. However, J. Aron was willing to provide SemGroup with the ability to trade in a margin account without requiring SemGroup to match dollar for dollar when margins increased. This service was offered to good clients with good credit histories and allowed SemGroup to avoid tying up large amounts of cash.

In November 2007, the banking group within Goldman became a participant in the credit facility for SemGroup, allowing J. Aron to become a secured creditor for derivative obligations, thereby limiting its risk. Thereafter, J. Aron conducted transactions with SemGroup, in which J. Aron purchased crude oil. SemGroup wanted to hedge stored product, and J. Aron made the purchase on a futures contract. Transactions continued on a consistent basis, with SemGroup removing more and more of its NYMEX positions to J. Aron, to avoid posting collateral. Eventually, SemGroup was hedging all of its stored products with J. Aron. Sometime in first quarter 2008, SemGroup was executing a larger volume of option sales (rolling more

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they run sensitivity analysis to make sure we have the right positions on to manage this risk. . . . our derivatives are all market to market. In 2007 we recorded an unrealized loss on derivatives of $1 billion. . . . To get to the $1 billion unrealized loss in the cash flow statement, two lines must be combined. You must add the unrealized loss line and the changes in derivatives line. . . I have attached the reconciliation we give our banks. Up until a year or so ago, we recorded the unrealized loss in one line so it was easy to see. PWC had us start breaking it out between different line items. . . ." *See* Exhibit 58. (Emphasis added).

"in-the-money" options) in the course of managing its residual position. When J. Aron inquired as to the reason, SemGroup replied that it wanted to move these trades from NYMEX to J. Aron.

In early 2008, a J. Aron representative traveled to Tulsa, to better "get to know the company." He met with Kivisto and Wallace briefly, and visited the company's trading room. He was introduced to Oven and Coen, and spent a couple of hours watching them execute trades. He also met with SemStream and SemMaterials personnel and observed the storage and transportation facilities. He returned to New York feeling less concerned about the company's trading strategy. The hedging appeared straightforward and transactions continued through April 2008, without any unusual activity.

In May 2008, oil prices were continuing to increase and SemGroup's margins were increasing. On May 21, the derivative liability increased substantially and SemGroup was facing a margin call of approximately $80-$100 million. J. Aron contacted SemGroup and advised it to expect the margin call, whereupon SemGroup suggested that J. Aron buy more crude to offset the payment. J. Aron countered with an offer to purchase additional crude in the future, but that the funds from those sales would be placed in a collateral account. SemGroup resisted this offer at first, because it would require it to front its own cash, but it eventually accepted the arrangement. An amended agreement was put into effect in early June 2008, for the monthly payment due on June 20.

J. Aron revised its monitoring protocols in order to anticipate what might be coming in the form of a margin call for the following month. The June payment was deposited into the collateral account and SemGroup was able to draw from it within five to seven days to even out the transaction.

During this same time period, SemGroup's trading increased, as the company represented that it was still moving positions from NYMEX to J. Aron. J. Aron requested financial data from SemGroup, including its most recent quarterly statements. An analysis of them revealed that SemGroup was facing liquidity and credit constraints. J. Aron's credit department then called Wallace about the company's financial status. During that telephone call, Wallace stated that the company's liquidity issues were exaggerated. When asked about the company's trading portfolio, Wallace replied that it had no similar exposure with other brokers, only J. Aron. Although this was the answer J. Aron had hoped for, it began to monitor closely SemGroup transactions, because it did not have information on other SemGroup accounts.

SemGroup conducted a few small trades in July 2008, but then requested that J. Aron sell back some call options for August 2008, which J. Aron had purchased from SemGroup. This would have required a large amount of cash from SemGroup, so it offered to sell J. Aron January 2009 call options to buy out its short position. However, since this would have extended J. Aron's risk too far out into the future, its credit department refused the deal. J. Aron called Coen and told him that the offer had been declined.

On July 17, 2008, J. Aron became aware of SemGroup's serious financial difficulties. A conference call was held with SemGroup and members of J. Aron and Goldman, at which time SemGroup advised that it was out of cash.

J. Aron's trading agreement and payment strategy protected it from SemGroup's financial difficulties. Subsequent to the Debtors' bankruptcy filings, J. Aron owed SemGroup approximately $90 million.

C. The Transfer of SemGroup's NYMEX Account to Barclays

Based upon discussions with a representative from Barclays, in 2007 or early 2008, Barclays was approached by SemGroup about joining its banking consortium and entering into a trading relationship with it. SemGroup's position at that time was that if a party wanted to trade with it, it must participate in the lending consortium as well. Barclays was not prepared to join the consortium at that time and declined SemGroup's offer, citing a lack of familiarity with SemGroup.

In approximately June or July 2008, Spaugy had a telephone conversation with Barclays, in which Spaugy stated that SemGroup's business could be available if Barclays would be able to provide a revolving credit facility to SemGroup. Spaugy stated that a $50 million credit facility commitment would get Barclays into the SemGroup commodities business, and a $100 million credit facility commitment would get it into SemGroup's capital markets business. Barclays' personnel considered the offer; however, due in part to the existing financial markets, Barclays declined to commit to the requested revolving credit facility.

The Barclays representative advised that during late June or early July 2008, he called Kivisto, and Kivisto arranged for Barclays to speak with Ronan. A Barclays representative subsequently had telephone conversations with Ronan and Spaugy, during which he suggested that SemGroup provide documentation to Barclays, such as its financials statements and by-laws, so that Barclays could conduct a due diligence investigation in anticipation that some sort of business relationship between them could be arranged.

SemGroup provided its 2007 audited financial statements to Barclays. Barclays representatives requested more current financials from SemGroup, but were advised that they

were not ready. Although Barclays' due diligence investigation had made progress regarding compliance issues, the financial due diligence component of its investigation required more time and was incomplete.

On July 8 or 9, 2008, Barclays received a telephone call from either Ronan or Spaugy, to arrange for a meeting with Kivisto in New York.

On July 10, 2008, two Barclays representatives met Kivisto at the Peninsula Hotel in New York. During the meeting, which lasted thirty to forty five minutes, Kivisto suggested the novation of SemGroup's NYMEX account. At that time, Kivisto indicated to Barclays that SemGroup was looking to offload its margin calls and that he would consider moving the position to Barclays to "unlock the collateral position." Kivisto also indicated that SemGroup had a revolving credit facility with BOA that he was having trouble renewing. Given the huge market volatility at the time (crude reached its all time high of $145 per barrel less than a week later), Barclays indicated that SemGroup's liquidity issues were not surprising or particularly troubling to it. Barclays told Kivisto that it had experience with novations, and the parties agreed to follow up after the meeting.

Later that same day, Barclays received a telephone call from Perkins, inquiring how SemGroup should send its trading positions data to Barclays. She was told to send it on a spreadsheet, which happened the following day. When Barclays received the first spreadsheet, it was shocked at how enormous SemGroup's negative MtM position was. (SemGroup's first spreadsheet showed a $1 billion position. SemGroup sent a total of three separate spread sheets to Barclays, which reflected a total negative MtM of almost $3 billion.) Barclays had numerous telephone conversations with Perkins regarding the specific data on the spreadsheets.

Barclays assembled a team to deal with the potential novation and to quantify the risk involved. Barclays began internal discussions about how much to charge SemGroup to take on the risk. Thirty to forty Barclays employees worked through the weekend of July 12 and 13, 2008, to figure out how the acquisition would impact Barclays' existing book — *i.e.*, whether, and to what extent, the acquired positions would offset Barclays' existing positions. This analysis was necessary to determine whether the transaction would be beneficial to Barclays.

SemGroup's NYMEX book was represented by 400,000 lines of entries, consisting primarily of short puts exercisable between October and December 2008. Taking into account SemGroup's large positions plus market volatility, Barclays priced the transaction at between six and seven volatility points, or approximately 6.5 multiplied by $23 million, equaling a total risk premium of $143 million. On July 13, 2008, Kivisto wrote a letter to SemGroup's MC, recommending the transfer of SemGroup's trading book to Barclays.

Late on Sunday night or early Monday morning, July 13 or 14, 2008, SemGroup and Barclays agreed on the $143 million fee. Barclays also requested a $50 million advance as a "good faith deposit," which was paid by SemGroup and subsequently returned by Barclays. The purpose of the deposit was to protect Barclays when it started moving the positions before the margin deposits were transferred.

On July 15, 2008, the purchase and sale agreement between SemGroup and Barclays was executed. Three of SemGroup's six brokers moved half of their trades to Barclays immediately, and the second half were moved later that day. However, three of SemGroup's brokers did not move their trades until after the markets had closed. At mid-day, only 25% of SemGroup's trading book had been transferred to Barclays. Because it only managed 25% of the book,

Barclays paid $10 million of SemGroup's margin calls and asked SemGroup to cover the remaining $30 million due. However, SemGroup refused — Kivisto stated that SemGroup could not make the payment, and that its MC wouldn't approve any additional payments. Although Barclays believed that it could have exercised a clause in its agreement with SemGroup and terminated the novation at that point, it decided to complete it based on a cost-benefit analysis and, it claimed, to avoid potential harm to SemGroup.

1. Barclays' Position Regarding the Novation

Barclays viewed the novation as a trade and, as a result, the transaction did not require approval of Barclays' management or credit committees. Because SemGroup's NYMEX book consisted of exchange-traded contracts, Barclays' credit exposure with respect to the trades was minimal. If SemGroup had filed for bankruptcy prior to the novation, NYMEX would have sold off the positions and the result with respect to the open positions would have been virtually the same.

Regarding the current status of the trades Barclays obtained from SemGroup's book, a Barclays representative stated that the bulk of those positions had been closed out, but that some longer positions might still be held. However, Barclays stated that it was impossible to tell, since it claimed that it didn't track the positions individually.

Barclays claims that it was motivated to proceed with the novation out of a concern for the market. According to Barclays, if SemGroup had gone into default and if all of SemGroup's positions had been "released immediately," it could have damaged the market and possibly moved the price of oil.

2. NYMEX Comments Regarding the Sale of SemGroup's Trading Book

A Managing Director of NYMEX stated that SemGroup became a NYMEX member firm in 2007. As part of its member firm requirements at the time, SemGroup was required to have two NYMEX "bundles," *i.e.*, a trading right coupled with 75,000 NYMEX Holdings shares. NYMEX records indicate that SemGroup purchased these "bundled" seats on March 22, 2007 and April 2, 2007, for $9.8 million and $9.96 million, respectively. The NYMEX Holdings shares were cashed out by SemGroup during August 2008. NYMEX records indicate that separate NYMEX memberships were not held by Kivisto, Eaglwing or Westback. As a NYMEX member firm, SemGroup received the benefit of favorable rates on its trading activity and increased flexibility in making trades, such as the utilization of the Globex Trading Platform, which allowed trading activity at times when the exchange was closed.

NYMEX had numerous telephone conversations with Kivisto and others during the novation of SemGroup's trading book in July 2008. During one of those conversations, Kivisto told NYMEX that he was concerned that a "world event" could cause a "liquidity crisis" for SemGroup. Kivisto stated that SemGroup had been trading futures and options, and that when the trades didn't work out, SemGroup had tried to "roll them over." Kivisto advised that, in retrospect, SemGroup's strategy did not work, and that he was planning to switch to a "P Plus" methodology. NYMEX believed that Kivisto was referring to a "price posting plus" strategy that is commonly used in the Mid-Continent area, such as in Cushing, Oklahoma. NYMEX found Kivisto's comments and his explanation to be "pedestrian" and stated that they lacked sufficient detail. However, because Kivisto's comments were a "sidebar" to the purpose of the novation, it did not pursue them further.

NYMEX advised that it has regulatory jurisdiction over NYMEX member firms, and that no violations were observed during the novation process. NYMEX noted that speculative trading was not an issue that would trigger a NYMEX investigation.

3. Comments of SemGroup Executives Regarding the Sale of Its NYMEX Book

Foxx stated that there was considerable conversation regarding the merits of novating SemGroup's trading book. In this regard, Foxx stated that Kivisto thought that SemGroup should "take its lumps" and do away with trading so it could "live to fight another day." According to Foxx, Kivisto also felt that SemGroup should go back to making money "the old fashioned way," through its operations.

Cooper was of the opinion that SemGroup would be able to get some money back from the sale of its trading book to Barclays. However, in the long run, the book was transferred to Barclays along with SemGroup's payment of approximately $143 million, and SemGroup had to assume more than $2 billion in MtM losses.

Brochetti stated that he first heard of the possible sale of the trading book during the week of July 6, 2008. He stated that he had no involvement in the sale. What he heard was that Barclays required $143 million before it would complete the purchase, which it claimed it needed in order to accept the risk of implied volatility that came with SemGroup's trading book.

D. Margin/Margin Calls

NYMEX had two types of margin required for commodity trades. First, when a company executes a futures transaction or an option sales transaction, the company must post what is

known as an initial margin. The initial margin requirements are set by the exchange as fixed dollar amounts per contract. Next, a company would be required to post a maintenance margin if the MTM loss on a futures contract exceeded the dollar value of the initial margin. The maintenance margin for option sales contracts is calculated differently than the maintenance margin for futures contracts due to factors such as volatility. Companies would be required to post a maintenance margin on sold options contracts at the determination of NYMEX.

Foxx stated that Kivisto managed SemGroup's margin call needs along with SemGroup's Treasury group (Cooper). Stallings stated that any time there was a rapid directional move in the price of crude, it would stress the company's liquidity. In approximately July 2007, the price of crude skyrocketed, which put stress on SemGroup's balance sheet.

As previously noted, Coen stated that part of Kivisto's strategy included managing "in-the-money" sold options as "residual positions" until the options could be allowed to expire worthless. Throughout the spring and summer of 2008, the market price of oil had become extremely volatile, and the price of crude oil continued to rise. The price volatility put a huge strain on SemGroup's ability to remain liquid and to meet its margin calls. As market prices went up, the corresponding margin amounts per contract increased as well.

1. SemGroup's Attempts to Predict Margin Requirements

Stallings stated that SemGroup developed a "stress test" system in the first or second quarter of 2008 to predict margin call requirements. Stallings was unaware of any system in place prior to that time to predict margin requirements, although Cooper may have had such a system.

Mr. Michael Brotherman ("Brotherman"), an IT analyst at SemGroup, performed the stress test (or "price shocking"), which produced data that looked at underlying market volatility. Brotherman stated that Jamie Cooper had previously used a program called "PC Span," published by the Chicago Board of Trade. He stated that SemGroup traders were not completely happy with the consistency of the results, however, so they asked IT to develop a price shock program.

Brotherman stated that he would download NYMEX information daily. He would view current prices, futures, options and broker statements. He would then run the report and provide it to the traders (through Allen), who, in turn, would use it in connection with SemGroup's trading strategy.

He stated that a price shock had nothing to do with moving averages, but relied on the historical portfolio (the previous day's volatility). If that volatility changed dramatically, the test would not be accurate. He stated that his goal was to come within $1 million in a projected amount, but that figure was rarely achieved.

In Spring 2008, Dreyer, a SemGroup IT analyst, was working on a program to estimate margin calls, referred to internally as "Marginator." Dreyer stated that Allen seemed to be satisfied with its accuracy. Prior to that time SemGroup's margin estimates were considered to be unreliable.

Tanksley, a SemGroup Treasury analyst, compiled information detailing the cash status of each business unit and forwarded it to Cooper (he also sent it to Ronan and Perkins). After Cooper reviewed the information, Tanksley would draw down from existing lines of credit and make the required margin call payments. The daily operational reports that Tanksley prepared

were supposed to forecast events for two to three weeks into the future. However, the forecast became irrelevant beyond two or three days because of trading market volatility.

The cash reports did not include margin call amounts. Tanksley would receive daily margin requirements from Allen. If Tanksley needed to draw on a line of credit, he had the authority to do so, and would keep Cooper advised of those transactions. Due to the volatility of the market, Tanksley stated that he was not surprised by the amount of the margins. On average, he stated that he would transfer $5 to $10 million per day, and, at times, from $40 to $50 million per day. Tanksley also stated that margin call amounts of $75 million were not something that would be a huge cause for concern at SemGroup. He estimated that the largest margin call he remembered was for approximately $100 million.

During the first week of June 2008, Ronan stated that he was contacted by BOA's Bond Director, who informed him of a $10 a barrel uptick in the market. BOA wanted to know how the increase had affected SemGroup. Ronan then called Allen, and was informed that the shock report showed a loss for the day of $6 million. Ronan relayed this information to BOA, and its response was, "That's not bad. Others were hit worse." Ronan later received a call from Perkins, who asked if he had talked to Wallace. She went on to state that, in fact, the loss was $66 million, not $6 million as he had previously been told.

Ronan indicated that the cash used to fund SemGroup's margin calls came from SemGroup's operating earnings, its bank borrowings and from the sales of assets to SGLP.

2. References in Interviews and Company E-mails Regarding SemGroup's Attempts to Cope with Margin Amounts

Brochetti stated that, in May, June and July of 2008, he repeatedly heard comments at SemGroup about adding trading positions to help with margin calls. He stated that he thought those trading positions were put in place to provide insurance against margin calls. Even though SemGroup's required margin ultimately reached over $2 billion, he assumed that SemGroup's trading strategy remained asset based.

Coen stated that it was ultimately Wallace's responsibility to manage margin call issues, but that a lot of the activity went through Cooper's office. Coen believes that the frequent presence of Wallace in Copper's office was at least in part caused by the increasingly challenging margin situation. Coen was unaware of precisely how the company was dealing with its margin calls. The margin call pressure was known to everyone in the trading department, and there were discussions between Coen, Oven and Kivisto about paring down the trading book in an effort to reduce margin.

Coen indicated that they could not simply remove positions because it would cause a loss to be realized, contrary to one of the central tenets of Kivisto's trading strategy - never to realize a loss from the sale of an option. Coen stated that the traders never reached a conclusion about how to effectively remove positions while staying within SemGroup's bank covenants.

Foxx stated that SemGroup's margin amount was $1 billion at the end of 2007. Cooper told Foxx that the time value of the margin was actually half of that amount, because some of the margin amount would be returned to SemGroup. Foxx was very concerned about the margin amount, and asked Kivisto about it in approximately June 2008, at which time Kivisto told him

that he (Kivisto) was in the process of shrinking the size of his trading book. In July 2008, Kivisto told Foxx that he wanted to get out of trading because there was too much volatility and the price of oil was too high.

Coen stated that he was on the phone all day during the weekend of June 6 and 7, 2008. He stated that SemGroup's Treasury, Risk Management, and Trade components were all working to attempt to develop strategies regarding SemGroup's liquidity problems. Coen indicated that SemGroup was able to get through that crisis by moving some of its trades from NYMEX to OTC, because OTC had lower margin requirements. From this point on, Coen stated that SemGroup had tightening liquidity issues almost daily.

E. MC Comments about Liquidity Issues

1. Thane Ritchie

Ritchie stated that in early July 2008, Kivisto told him that he (Kivisto) was looking to sell SemGroup's NYMEX trading book to a Wall Street firm. Ritchie recommended Barclays and Deutsche Bank. Kivisto flew to New York on a weekend and, a couple of days later, told Ritchie that he had consummated the sale of the book to Barclays.

On July 13, 2008, Kivisto informed Ritchie that SemGroup was going to sell some of its assets to Plains All-American. When the public company's stock price fell sharply, Plains All-American's interest in purchasing assets from SemGroup ceased. Ritchie stated that when SemGroup's bankruptcy filing became imminent, he recommended hiring an energy banker to advise SemGroup, but Blackstone was hired for this purpose.

Ritchie flew to Tulsa on approximately July 14, 2008 and, in conjunction with Riverstone's MC members, decided that a change in management was necessary at SemGroup. SemGroup's MC recommended full disclosure of all of its obligations.

While in Tulsa, Ritchie asked Kivisto for a meeting with SemGroup's traders, and was introduced to Oven and Coen. Ritchie had Oven and Coen walk him through their trading positions. In the course of this discussion, Ritchie discovered that SemGroup had an approximately $850 million OTC trading book, of which Ritchie had previously been unaware, and that the book had not posted, meaning that an OTC creditor could call it in at any point. These losses were in addition to the losses resulting from NYMEX trading. Ritchie spoke with Wallace and Kivisto and asked them if they realized that they needed to raise an additional $850 million for the OTC losses. Wallace acknowledged that he was right, and Ritchie advised Wallace and Kivisto that his firm would not help SemGroup raise the $850 million.

2. Andrew Ward

Ward stated that on Friday, July 11, 2008, Wallace told him during a telephone conversation that SemGroup was working out the transfer of its trading book to Barclays, which included a profit sharing agreement. Ward told Wallace that he wanted him to give a presentation about it to the MC on Sunday, July 13, 2008. On the evening of July 13, 2008, Wallace addressed the MC during a conference call, and told its members that SemGroup would have to pay approximately $150 million to Barclays to take the trading book off its hands, and that there would be no profit sharing. According to Wallace, this move would crystallize all of SemGroup's losses at $2.9 billion. This revelation stunned the MC members and resulted in a five hour conference call. The MC decided to bring in outside bankruptcy counsel at that point.

3. Bartow Jones

Jones stated that during the first six months of 2008, SemGroup's liquidity constraints were not unexpected, as other similar companies were also experiencing liquidity problems due to market conditions. He stated that Goldman was considering brokering a major investment in SemGroup, and likely would have done so had it not been for SemGroup's bankruptcy filings.

F. Issues Leading to the Debtors' Bankruptcy Filings

1. Growth of Unrealized Losses and Liquidity

Foxx stated that cash was always tight at SemGroup because its business grew so quickly. He stated that it was continually seeking investors and had deals in the works at all times to add to its assets. Marketing (commodities trading) was making a significant contribution to SemGroup's annual profit line, although, in Foxx's opinion, the company would have been able to operate profitably without engaging in commodities trading.

Foxx thought that SemGroup would not have had to file for bankruptcy protection if it had been able to bring in a partner, which it had been attempting to do in the months leading to the bankruptcy filings. In Foxx's opinion, the members of the MC were pushing for SemGroup to file for bankruptcy as the ultimate resolution of its liquidity issues.

Brochetti also felt that, while marketing was making a significant contribution to SemGroup's annual profit line, SemGroup would have been a viable company without it. Although cash was tight in 2008, Brochetti believed that was the case since the inception of the company, because SemGroup was constantly looking for opportunities to expand.

Stallings stated that going into First Quarter 2008, the price of crude continued to increase, which continued to stress SemGroup's liquidity position. He also stated that SemGroup's margin payments and margin calls were becoming the focus of its liquidity problems.[12]

Ronan stated that a series of meetings were held after the cumulative margin posted had reached approximately $2.5 billion. The people who attended the meetings included Ronan, Kivisto, Cooper, Foxx, Allen, Wallace, and Perkins. Ronan stated that the group was looking to Kivisto for guidance, and everyone thought he could handle the situation. "That seemed to be the strategy — let Tom handle it." Ronan stated that it was his opinion that the company had been profitable at one time and that it would have maintained its profitability if it had stayed with asset-based trading.

A MC telephone conference call meeting was held beginning late in the evening of Sunday, July 13, 2008. The call lasted for 5 hours, and concluded in the early morning hours of July 14. Ward stated that he learned for the first time during the call that SemGroup was in critical condition, and "that the Company was going to run out of cash." SemGroup told the MC that it would execute a novation of its trading book, which would require it to pay Barclays approximately $150 million, and would result in a total loss of $2.9 billion. Ward stated that the non-management members of the MC were stunned. They agreed to meet at SemGroup on July

[12] The May 2, 2008 Report of Evergreen Collateral Consulting, L.L.C. (*see* Exhibit 35 at page 4) noted the following: "SemGroup reported a net loss of $611,955M on sales of $14,184,772M for the twelve months ended December 31, 2007. This is compared to FYE net income of $65,958M on sales of $14,744,680M for the year ended December 31, 2006. December 31, 2007 net income is $385,769M after adjusting for $997,778M of Net Unrealized Loss on Derivative contracts compared to $411,272M of unrealized losses for FYE December 31, 2006. The derivative loss will not likely be realized since the contracts will execute at maturity." The Evergreen position that the derivative loss would not likely be realized since the contracts would expire at maturity assumed that SemGroup would not be forced to realize the losses.

15. It is Ward's opinion that the MC should have been notified of the novation transaction much earlier.

Ward stated that the MC had been told on July 11, 2008, that: (1) SemGroup's commodities trading business could be unwound; (2) its MtM accounting would not result in any cash losses; and (3) no liability would be incurred by SemGroup if its marketing business was stopped.

Foxx was a participant in the MC conference call on July 14-15, 2008. He stated that Ward told Kivisto during the call that he thought SemGroup had engaged in speculative trading, which Kivisto denied.

Ward stated that the Barclays novation was one of the largest novations to ever occur on NYMEX.

2. Time Line of Liquidity Concerns from Late 2007 to July 2008

Late 2007	Mr. Frank Panzer ("Panzer"), SemMaterials President, began to feel uneasy about SemGroup's liquidity. He repeatedly tried to talk to Kivisto about his concerns but his calls were not returned. Panzer stated that he didn't want to talk to Wallace because he considered him to be erratic. He stated that he was eventually able to see Kivisto, who told him not to worry.
January 2008	Spaugy first became concerned about SemGroup's liquidity when the amount of cash on the daily cash reports dropped below $200 million.
March 2008	Ronan expressed concern about the liquidity of the company.
April 28, 2008	E-mail from Lietzke to Spaugy regarding "SemGroup Financial Statements": " . . . I am comfortable saying we will have $300 to $400 million in expansion/project capital . . . . At March 31, 2008 our equity was in excess of negative $700 million so 1Q results won't make your job any easier." *See* Exhibit 59.

May 6, 2008	E-mail from Ronan to Wallace voicing concern about SemGroup's liquidity. "I recommend we start making phone calls, or we risk being underwater by Friday." Wallace replies, "What is borrowing base projection." Ronan replies, "Flat to 10 MM is best estimate. . . ." *See* Exhibit 60.
May 20, 2008	A first quarter 2008 SemGroup Conference Call presentation document entitled "Liquidity Discussion" states as follows: "As a result of dramatic increases in commodity prices, margin deposits have increased. In response to the commodity price increase, organic growth, and seasonal inventory builds we: - increased working capital facility from $1.4 billion to $1.7 billion - amended revolving credit facility from $445.0 million to $665.0 million. . . Liquidity as of March 31, 2008 . . . was approx. $300 million . . . ." *See* Exhibit 61.
June 2008	Employee and executive bonuses were suspended. Per Ward, SemGroup told the MC that it had liquidity issues and that it might need additional capital.
June 12, 2008	An e-mail from Ronan states, "Cash and availability is currently $150 million. . . ." *See* Exhibit 62.
June 28, 2008	Crude oil reaches a new high of $142.99 per barrel.

3. Time Line of Liquidity Concerns for July 2008

July 7, 2008	MtM analysis comparing MtM on December 31, 2007 ($1.691 billion) and July 7, 2008 ($3.325 billion) notes that the "difference in mtm can be attributed to the rising prices and large increase in volatilities." *See* Exhibit 63.
July 10, 2008	Ronan e-mailed BOA and reported that SemGroup was out of money. *See* Exhibit 64.
July 11, 2008	Crude oil reaches a new high of $147 per barrel. Wallace told Ward that SemGroup was working out the transfer of its trading book, which would include a profit sharing agreement. Ward requested a detailed presentation to the MC on Sunday, July 13, 2008. Wallace stated that he was pleased that the transfer would be a "quick and smooth" transaction.

July 13, 2008	E-mail chain between Kivisto and BOK representatives, in which Kivisto attempts to obtain additional financing. *See* Exhibit 65.
	E-mail from Oven to Allen and Coen stating that: "We would like to see how much cash could potentially be freed up if we neutralize the nymex position." *See* Exhibit 66.
	E-mail from Perkins to Foxx regarding "NYMEX Seats": "great program that got out of control that we didn't catch the risk soon enough." Foxx reply: "If u had a billion could you get it back" *See* Exhibit 67.
	Letter from Kivisto to Thomas LaSala of NYMEX recommending the transfer of SemGroup's trading book to Barclays: "Semgroup has to date employed an oil pricing strategy based on a combination of NYMEX futures and associated options on a delta basis. . . . [C]urrent market conditions . . . will likely result in an adverse liquidity situation for SemGroup. . . ." *See* Exhibit 68.
	Invoice #001 for "Agent Services" dated July 14, 2008 for $289,990,637 from SemGroup, L.P. to Westback Purchasing Co., L.L.C. *See* Exhibit 48.
July 15, 2008	Ward stated that PwC representatives arrived in Tulsa and were instructed to review SemGroup's trading book. PwC's review was limited to SemGroup's OTC positions because it was the only ongoing trading liability remaining on SemGroup's books. PwC reported early in its review that SemGroup was using "strangles" as a trading strategy.
	Crude oil declines $8 per barrel.
July 16, 2008	The transfer of SemGroup's NYMEX trading book to Barclays converted its unrealized loss into a recognized loss of approximately $2.4 billion, including a $290 million loss by Westback.
	Wallace went to the MC, told them about the invoice to Westback (*see* Exhibit 48) and resigned. Wallace told the MC that Westback was owned by Kivisto.
July 17, 2008	12:26 p.m. e-mail from Cooper to Kivisto, *et al*., announcing his resignation and advising that he was filing for disability. *See* Exhibit 69.
July 18, 2008	Kivisto was removed as CEO and placed on administrative leave by SemGroup. Kivisto and Pens were escorted from the building.
July 21, 2008	Foxx resigned from SemGroup but remained with SGLP. *See* Exhibit 88.
July 22, 2008	SemGroup files for bankruptcy protection.

IV. THE EXAMINER'S FINDINGS REGARDING THE INSIDER TRANSACTIONS AND THE FORMATION OF SEMGROUP ENERGY PARTNERS L.P.

A. MLP Business Model

A MLP business model was suggested to SemGroup as early as 2003, and was eventually implemented by it in 2007. The MLP business model is commonly used in the energy industry, and it was a reasonable business decision by SemGroup to utilize the concept. The MLP business model allowed for capital infusions to the parent company through public offerings, as a return on capital to investors and unit holders, and as a source of cash to be made available to the parent for subsequent acquisitions.

SemGroup's adoption of the MLP business model resulted in the July 2007 formation of SGLP, and the subsequent dropdown of assets to it.

At the time SemGroup received money from the dropdown of assets it was also required to pay large daily margin calls from its commodities trading activities. However, the MLP business model strategy was not planned or designed for the purpose of managing or paying required margins.

Some of the individuals the Examiner has interviewed have described the formation of a public entity as a strategy by which SemGroup could gain indirect access to public equity markets and generate capital to acquire other assets. As a result, it could then effectively "monetize" the dropdowns to the public entity. The strategy was to take assets with stable cash flows from the private entity and drop them down into a newly formed public company, creating a MLP structure.

The dropdown of assets between SemGroup (and its subsidiaries) and SGLP created a complex relationship between them, wherein their physical assets became intermingled and numerous employees split duties between the two entities.

The Examiner met with various individuals who provided information related to specific dropdown transactions, including the following: Perkins, Stallings, Foxx, Lietzke, Ronan, Panzer, Brochetti, Ward, and Mr. Brian Billings ("Billings") (a member of SGLP's Conflicts Committee).

The Examiner has also reviewed various documents related to the dropdown transactions, including the following:

1. IPO Prospectus. *See* Exhibit 70.

2. Purchase and Sale Agreement by and between SemMaterials, L.P. ("Seller") and SemGroup Energy Partners Operating, L.L.C. ("Buyer"), dated January 14, 2008, for $378.8 million. S*ee* Exhibit 71.

3. Purchase and Sale Agreement by and between SemCrude, L.P. ("Seller") and SemGroup Energy Partners, L.L.C. ("Buyer"), dated May 12, 2008, for $45 million. S*ee* Exhibit 72.

4. Purchase and Sale Agreement by and between SemCrude, L.P. ("Seller") and SemGroup Energy Partners, L.L.C. ("Buyer"), dated May 20, 2008, for $90 million. S*ee* Exhibit 73.

5. Memoranda of Action by the Management Committee of SemGroup G.P., L.L.C. dated February 13, 2008, February 15, 2008, May 8, 2008, and, May 20, 2008. S*ee* Exhibits 74A-74D.

6. Fifth Amendment to Amended and Restated Credit Agreement, executed on May 8, 2007. S*ee* Exhibit 75.

7. SMH Capital Investment Banking Group Fairness Opinion to the Management Committee of SemGroup G.P., L.L.C. in conjunction with the sale of assets from SemMaterials, L.P. ("Seller") to SemGroup Energy Partners Operating, L.L.C. ("Buyer"), dated January 4, 2008, for $378.8 million. S*ee* Exhibit 76.[13]

8. Duff & Phelps, L.L.C. ("Duff & Phelps") Fairness Opinion, dated Jan. 14, 2008, issued to the Conflicts Committee of the Board of Directors of SemGroup Energy Partners, G.P., L.L.C., in connection with the purchase of assets from SemMaterials, L.P. for $378.8 million, on January 12, 2008. S*ee* Exhibit 77.

9. Duff & Phelps Fairness Opinion, dated May 16, 2008, issued to the Conflicts Committee of the Board of Directors of SemGroup Energy Partners, G.P., L.L.C., in connection with the purchase of assets from SemCrude, L.P. for $45 million, on May 12, 2008. S*ee* Exhibit 78.

10. Duff & Phelps Fairness Opinion, dated June 3, 2008, issued to the Conflicts Committee of the Board of Directors of SemGroup Energy Partners, G.P., L.L.C.,

[13] The copy provided as an exhibit is not signed.

in connection with the purchase of assets from SemCrude, L.P. for $90 million, on May 20, 2008. S*ee* Exhibit 79.

11. SGLP Forecast Discussion Materials – Dropdown Schedule and Asset Descriptions, dated October 1, 2007. S*ee* Exhibit 7.

12. Draft SemGroup Strategic Alternatives Presentation by Merrill Lynch, dated February 23, 2007. S*ee* Exhibit 80.

13. SemGroup Energy Partners, L.P. Underwriters' Diligence Presentation, dated April 3, 2007. S*ee* Exhibit 81.

14. Proposed Sale of Asphalt Terminal Assets to SemGroup Energy Partners, L.P., dated January 2008. S*ee* Exhibit 82.

15. SemGroup, L.P. Transaction Receivables Proposal, dated May 2008. S*ee* Exhibit 83.

The MLP business model strategy was not unique to SemGroup. It was common in the energy industry. SemGroup first observed this strategic structure during its discussions with TransMontaigne ("TM"), an energy based company in Denver, Colorado, which provided a broad range of services to end-users of petroleum products, including distribution, storage, and transportation. SemGroup had considered the acquisition of TM in 2006, and, during its due diligence discussions with it, learned of TM's strategy of utilizing dropdowns from the private company to TM's public entity. This strategy was part of TM's business model, to create equity and capital for future use (to repay bank debt, to fund future acquisitions, for capital expenditures and working capital, etc.).

Stallings stated that during the 2006-2007 timeframe, SemGroup was undergoing its largest capital expenditures ever. For example, SemGroup was involved in funding the White Cliffs project, a $250 to $300 million project, and a $350 to $400 million pipeline project in Canada. Stallings stated that SemGroup knew it would need to increase its capital position to fund those kinds of projects and to ensure its continued growth. SemGroup was also considering two sizeable acquisition possibilities for 2008, including a private company and a large public MLP.

The TM acquisition did not materialize because Morgan Stanley outbid SemGroup. However, having had a detailed review of TM's MLP dropdown structure as part of its due diligence efforts, SemGroup determined that the dropdown model appeared to be a viable business model for it. Stallings also looked at the business model for other companies in the energy industry that used a similar MLP structure, including Plains All-American, Alliance, and Williams.

Brochetti, Foxx, and Stallings were the three leaders in charge of developing and executing the change in SemGroup's business plan, and the adoption of a MLP structure. Brochetti and Stallings prepared a spreadsheet, which contained various options with respect to possible dropdown transactions, and the timing of them. *See* Exhibit 7. After analyzing the economics of the MLP business model for SemGroup, Brochetti concluded that it appeared to be a very profitable business structure.

Although it was not formally memorialized by SemGroup, Ronan stated that it was never SemGroup's intention to dropdown all of its assets. Initially, Ronan stated that there were many opportunities to buy companies at low multiples. However, as the MLP business model became

more popular in the energy industry, the low multiples escalated and the prices of potential acquisitions increased.

Riverstone and RCM, two of SemGroup's investors with representatives on its MC, were supportive of the MLP concept because, in part, it would enable them to realize returns from their investments. SemGroup's MLP business model included a proposed public offering. Although Foxx recalled that Riverstone was a prime mover behind proceeding with a public offering, he stated that the idea made sense to everyone. In 2007, the MLP business model, which included a proposed public offering in July 2007, was formally presented to the MC for its consideration and approval.

1. Timing of Dropdowns

In addition to the January and May 2008 dropdowns, discussed below, additional dropdowns were scheduled by SemGroup for the fourth quarter of 2008, and in 2009 and 2010. As part of the original dropdown strategy, a dropdown of assets related to SemGas was anticipated for the third quarter of 2008, which Stallings was working on at the time of the Debtors' bankruptcy filings. A dropdown of the White Cliffs pipeline project was tentatively scheduled for the first quarter of 2009, and a SemGroup private offering was tentatively scheduled for the second quarter of 2009.

When asked about the timing of the January and May 2008 dropdown transactions, Stallings stated that they were part of SemGroup's overall MLP strategy, and he felt that the timing of them was consistent with its strategy. Stallings stated that the dropdowns were not done to raise capital to pay down margin debt. He noted that it would take about two to three

months to engineer a dropdown and that such an effort would not be consistent with attempting to manage or predict daily margin requirements.

Foxx stated that the timing of the dropdowns was not accelerated due to liquidity issues caused by margin call requirements. He stated that they were timed based on opportunities that presented themselves, noting that the asphalt dropdown in January 2008 had been strategically planned for months.

Foxx stated that the January 2008 dropdown was delayed slightly (although it had been projected during the fourth quarter of 2007) and the May 20, 2008 dropdown was accelerated slightly. The May 20, 2008 dropdown was accelerated because of the availability of assets securing a third party storage fee agreement between SemGroup and Vitol. The agreement with Vitol was scheduled to commence in the June-July 2008 timeframe, thus triggering the accelerated dropdown in May.

2. The Formation of SemGroup Energy Partners L.P. (SGLP)

Evergreen's May 2, 2008, Report discussed the MLP business model and the formation of SGLP.[14]

SGLP's IPO raised $400-$450 million, from which $100 million was distributed to SemGroup's unit owners. *See* Exhibit 70. Brochetti opined that the distribution to the unit owners was fairly modest in relation to the amount of cash generated by the underlying transactions.

[14] The Evergreen report states in pertinent part as follows: "In 2007, SemGroup, L.P. formed a master limited partnership (MLP). The MLP is traded on the NASDAQ under the symbol SGLP. The MLP owns certain hard assets but does not own the inventory or receivables of the parent company which are included in the BBC [borrowing base certificate]." *See* Exhibit 35 at page 5.

Hill, SemGroup's Tax Manager, stated that SemGroup had been considering going public with some of its assets, which resulted in the proposed dropdown schedule, which Stallings and Brochetti prepared. Hill was tasked to analyze the tax depreciation implications of the dropdown transactions. According to Hill, dropdowns were a common business strategy for energy companies with a significant amount of mid-stream assets, like SemGroup.

Ronan stated that the reasons for "going public" were twofold: 1) to allow equity holders an opportunity to realize a return on their investments; and, 2) to allow SemGroup to pay down the BOA credit facility. Ronan stated that SemGroup's dropdown strategy would also provide it with cash to develop new businesses.

3. Insider Payments Schedule

Alix Partners was retained by SemGroup as a restructuring company after it filed its bankruptcy petitions. Mr. Meade Monger ("Monger"), one of its managing directors, submitted a final status report to the Bankruptcy Court on behalf of SemGroup as of July 22, 2008. Monger referred to Schedule 3c in his submission, in which he listed the payments made to SemGroup employees from July 22, 2007 through July 22, 2008. *See* Exhibit 84. Included in his schedule are the following entries:

Name	Compensation	Bonus	MLP IPO Distribution	MLP Dropdown
Kevin Foxx	$450,000	3,034,000	4,105,553	4,561,726
Gregory Wallace	$325,000	7,534,000	3,843,861	4,270,957
Thomas Kivisto	$350,000	11,034,000	14,686,767	16,318,630
Jim Coen	$133,125	2,155,000	42,255	46,950
Melina (Mia) Oven	$130,625	1,505,000	34,799	38,665

4. Valuation of Assets

Assets associated with the IPO in July 2007 were valued by the market price of the SGLP publicly traded stock. Underwriters Citi and Merrill Lynch brought the SGLP shares to market, and the shares were priced by the market. Financial analyst's opinions regarding the stock value of SGLP were consistently positive through early 2008. *See* Exhibit 85.

For the January 14, 2008 dropdown, opinions for the fair market value of the assets transferred to SGLP were issued independently for SGLP by Duff & Phelps and for SemGroup by SMH Capital as required by the Pre-Petition Credit Agreement. *See* Exhibits 76, 77 and 78.

Although not contractually required, fairness opinions were obtained from Duff & Phelps for SGLP for the two dropdowns that occurred in May 2008. *See* Exhibits 78 and 79.

Stallings, Brochetti, Foxx, Ward, and others stated that careful consideration was given so that the assets dropped down were fairly valued. SGLP's Conflicts Committee and SemGroup both hired separate and independent financial advisors to assist them in this effort.

A package fully describing the assets was prepared by SemGroup and presented to outside Board members of SGLP (the Conflicts Committee), with a request to make a recommendation to SGLP's full Board of Directors.

Stallings stated that SemGroup's Management Committee and SGLP's Board of Directors (the "Board") had to approve the January 2008 dropdown and the two dropdowns in May 2008, ensuring that the assets were fairly valued.

The valuation amounts calculated in the fairness opinions for the value of the dropdown asset were determined by replacement costs for the company, market comparables and discounted cash flows.

5. January 14, 2008 Dropdown (closed on February 20, 2008)

a) Description of Dropdown and SemGroup Employee Comments

Pursuant to a Purchase and Sale Agreement dated January 14, 2008 (*see* Exhibit 71), SemMaterials agreed to transfer liquid asphalt assets, valued at $378.8 million, to SGLP and certain of its affiliates. The transaction closed on February 20, 2008. Foxx, along with Brochetti and Stallings, worked on the transaction for SGLP (the public entity). Wallace, and to a lesser extent, Kivisto, worked on the transaction for SemGroup (the private entity).

Foxx stated that the January 14, 2008 asphalt dropdown was the first dropdown in SemGroup's strategic plan. Foxx stated that SGLP bought the hard fee-based assets of the company so the public company would not be faced with commodity risks. He noted that when SGLP went public in July 2007, the plan (although a flexible plan) was for a dropdown to occur approximately every six months.

The transferred assets consisted of all of SemMaterials' liquid asphalt cement terminalling and storage assets located in the United States. SemMaterials retained its liquid asphalt cement inventory, along with the equipment used for processing and marketing operations, certain leased terminals used for storage, processing and marketing activities, and its Mexican asphalt operations. SGLP funded the purchase, in part, by borrowing additional amounts under its Wachovia Credit Facility.

The January 14, 2008 dropdown allowed SemMaterials to sell six million barrels of storage capacity to help it raise capital for growth, and provided income producing assets to SGLP. Subsequent to the dropdown, SemMaterials entered into a fee-based seven year terminalling and storage agreement with SGLP, and SemGroup agreed to provide general and administrative services for the transferred assets.

Panzer stated that he was skeptical about this dropdown, for several reasons. First, he noted SemGroup would not allow SemMaterials to purchase asphalt in September and November 2007, typically a prime time of the year to purchase asphalt. Second, he thought that the price of $378.8 million was too much to pay for SemMaterials, considering that it was purchased in June 2005 for $185 million.

SMH Capital considered a variety of valuation methods with respect to its fairness opinion (*see* Exhibit 76), but chose to use the following methods, which it considered to be most relevant for the industry and the specific transaction: comparable company analysis, comparable transaction analysis and discounted cash flows. Based on pro forma estimated trailing, 2008 EBITDA for the assets and comparable dropdown asset transactions, SMH Capital determined that the implied value of the assets was between $327.8 million and $449.8 million. Based on pro forma estimated trailing, 2008 EBITDA for the assets and comparable company valuations (Buckeye Partners, LP, Holly Energy Partners, LP, Magellan Midstream Partners, LP, Martin Midstream Partners, LP, NuStar Energy, LP, SemGroup Energy Partners, LP and Sunoco Logistics Partners, LP), SMH Capital determined that the implied value of the assets was between $344.8 million and $667.1 million. The discounted cash flow analysis estimated the implied value of the assets was between $346.3 million and $442.4 million.

Ronan stated that this dropdown allowed SemGroup to have $350 million in cash on hand by the end of March 2008, although not all of it went to the parent company. Foxx stated that it was Riverstone's idea to distribute a portion of the dropdown to the shareholders instead of keeping it all in working capital.

b) Cash Analysis

On February 15, 2008, SemGroup's MC authorized a $100 million partner distribution from this dropdown. On February 20, 2008, the $378.8 million purchase and sale agreement between SGLP and SemMaterials was executed.

A MOA by the MC of SemGroup G.P., L.L.C., dated February 15, 2008, was signed by Kivisto, Wallace, Foxx, Ritchie, Ward and Jones. *See* Exhibit 74B. The following was stipulated in the MOA:

> WHEREAS, SemMaterials, L.P., an Oklahoma limited partnership that is a Subsidiary of the Partnership ("SemMaterials"), is a party to that certain Purchase and Sale Agreement (the "PSA"), dated January 14, 2008, by and between SemMaterials and SemGroup Energy Partners Operating, L.L.C., a Delaware limited liability company;
>
> WHEREAS, it is proposed that after closing the transactions and agreements set forth in the PSA, including the receipt of the purchase price thereunder, that the Partnership make a $100,000,000 distribution to the partners of the Partnership in accordance with their respective ownership percentages in the Partnership within 15 days of closing the PSA (the "Partnership Distribution");

A review of the detailed cash data reveals that SemGroup made payments totaling approximately $26 million to key SemGroup personnel and/or trusts on their behalf. On February 20, 2008, SemGroup made a net payment of approximately $99 million to its brokers, and, between February 20-21, 2008, a net payment to its credit facilities of close to $325 million.

6. May 12, 2008 Dropdown (closed on May 12, 2008)

a) Description of Dropdown and SemGroup Employee Comments

On May 12, 2008, the transaction closed and SemCrude transferred additional crude oil assets (the Eagle North Pipeline) valued at $45 million to SGLP and certain of its affiliates pursuant to a Purchase and Sale Agreement, dated May 12, 2008. *See* Exhibit 72. SGLP funded the purchase with funds borrowed under the Wachovia Credit Facility. The acquired assets included a 130-mile, 8-inch pipeline that originated in Ardmore, Oklahoma, and terminated in Drumright, Oklahoma, and other real and personal property related to the pipeline.

The parties to the throughput agreement executed an amendment dated May 12, 2008 (*see* Exhibit 86), to include minimum monthly volume requirements for barrels transported on the Eagle North Pipeline, regardless of the volumes actually shipped, which obligated SemGroup to pay SGLP approximately $400,000 per month. The parties also entered into an agreement, dated May 12, 2008, to permit additional assets to be subject to the general and administrative services provided by SemGroup.

Foxx stated that the May 12, 2008 dropdown resulted in SGLP's acquisition of pipeline related assets from SemCrude for $45 million. Duff & Phelps prepared a fairness opinion for this transaction for SGLP. He stated that this was a relatively small transaction which was accomplished relatively quickly, but not because of SemGroup's liquidity issues.

Although SemGroup's cost basis was $35 million for the pipeline, Duff & Phelps valued it at $45 million, which Foxx considered to be fair because SGLP received a seven year throughput agreement that would secure a stream of revenue. SemGroup's pipeline in southern

Oklahoma was running at capacity, so additional capacity was needed for that area. Additionally, Weakland had been trying to buy some terminal assets for SemFuel. By purchasing the pipeline from Explorer Pipeline Company, and by dropping it down to SGLP, SemGroup was able to fill both needs. In turn, SGLP would be able to realize approximately $3 million a year from the assets, allowing it to recoup the premium paid for the pipeline in a relatively short period of time.

Brochetti stated that the pipeline acquisition by SGLP for $45 million went through the same vetting process as the other dropdowns and was unrelated to SemGroup's liquidity problems.

SemGroup was not required to obtain a fairness opinion for this transaction pursuant to the Pre-Petition Credit Agreement, which only required fairness opinions for asset transfers greater than $100 million.[15]

b) Memorandum of Action (MOA)

A MOA by the MC of SemGroup, dated May 8, 2008, was signed by Ritchie, Ward and Jones. *See* Exhibit 74C. The following was stipulated in the MOA:

> WHEREAS, it is proposed that SemCrude, L.P., a Delaware limited partnership that is a Subsidiary of the Partnership ("SemCrude"), offer to sell ("Offer") to SemGroup Energy Partners, L.P., a Delaware limited partnership ("SGLP"), that certain pipeline commonly referred to as the "Eagle North Pipeline System" for the approximate purchase price of $45,000,000 (the "Purchase Price") which corresponds to a purchase multiple of approximately 8.0x EBITDA;
>
> WHEREAS, in connection with the Offer and the acquisition of the Eagle North Pipeline System by SGLP from SemCrude, it is proposed that SGLP commit to

[15] Fifth Amendment to Amended and Restated Credit Agreement, executed on May 8, 2007, amended Section 2.5 – Additional Defined Terms, to include a "Minimum Consideration" section. *See* Exhibit 75.

provide, and SemCrude commit to use, certain throughput services on the Eagle North Pipeline System subject to the terms and conditions of a throughput agreement that will be on an arms length basis and will reflect what SemGroup reasonably believes to be market terms for similar types of contracts (the "Throughput Agreement");

There were no distributions to investors from the May 12, 2008 dropdown.

7. May 20, 2008, Dropdown (closed on May 30, 2008)

Pursuant to a Purchase and Sale Agreement, dated May 20, 2008 (*see* Exhibit 73), SemCrude transferred additional crude oil and terminalling facilities valued at $90 million to SGLP and certain of its affiliates. This transaction closed on May 30, 2008. The additional crude assets included crude oil storage tanks in Cushing, Oklahoma. SGLP funded the purchase with funds borrowed under the Wachovia Credit Facility.

Foxx stated that he was responsible for this dropdown transaction. At the time, SemGroup was building an additional 6.1 million barrel storage facility in Cushing at the same time that Vitol, a crude oil trader, needed storage space. SGLP was able to obtain a contract from Vitol wherein it would lease two million barrels of storage space for $11-$12 million a year. Vitol was willing to take a three-year lease for 100% of capacity at a price SemCrude was charging to the parent company. According to Foxx, this dropdown occurred when it did because the financing for it had been arranged relatively quickly (SGLP had obtained a credit facility and Vitol had good credit). According to Brochetti, SemGroup was in need of an infusion of cash for its White Cliffs pipeline and other projects, as well as its preparation for the GS TruE negotiations.

a) MOA

A MOA by the MC of SemGroup, dated May 20, 2008, was signed by Ritchie, Ward and Jones. *See* Exhibit 74D. The following was stipulated in the MOA:

> WHEREAS, it is proposed that SemCrude, L.P., a Delaware limited partnership that is a Subsidiary of the Partnership ("SemCrude"), offer to sell ("Offer") to SemGroup Energy Partners, L.P., a Delaware limited partnership ("SGLP"), certain crude oil storage tanks located at Cushing, Oklahoma with the aggregate capacity to store between 1,000,000 and 2,000,000 barrels (the "Storage Tanks") at the approximate purchase price of $35 to $40 for each barrel of storage capacity sold to SGLP (the "Purchase Price");
>
> WHEREAS, in connection with the Offer and the acquisition of the Storage Tanks by SGLP from SemCrude, it is proposed that SemCrude commit to use, and SGLP commit to provide; certain storage services with respect to the Storage Tanks subject to the terms and conditions of a to be agreed upon storage agreement (the "Storage Agreement");

Duff & Phelps prepared a fairness opinion for this transaction for SGLP (*see* Exhibit 79), although it was not required to do so pursuant to the Pre-Petition Credit Agreement.

There were no distributions to investors from the May 20, 2008 dropdown.

In addition to the two SemCrude dropdowns to SGLP and certain of its affiliates in May 2008 (for $45 million and $90 million, respectively), there was, as previously referenced, a sale of oil from SemCrude to SemEuro on May 16, 2008 for $25 million. *See* Exhibit 23. The net amount paid by SemGroup to its brokers was approximately $102 million between May 12 and May 14, 2008; $31 million between May 19 and May 21, 2008; and $18 million between May 30 and June 2, 2008. SemGroup also made a net payment of $75 million to its credit facilities between May 12 and May 14, 2008; a net payment of $111 million between May 19 and May 21, 2008; and a net paydown to its credit facilities of approximately $33 million between May 30 and June 2, 2008.

8. Andrew Ward's Comments Regarding the MLP Model

Ward stated that the creation of a MLP structure and the related public offering of SGLP began to be put together in approximately June 2006. Riverstone liked the MLP structure/IPO concept for the Company, and promoted it from the beginning of its involvement as a way to grow SemGroup and to increase its cash flows. Ward recalled that the MLP structure was discussed at many MC meetings.

Ward explained that, in general, a MLP is usually sponsored by a parent company, which contributes assets to a partnership, which is then taken public. The parent receives cash and a subordinated partnership interest (approximately 50%). Outside investors receive a yield from the cash flow created by the dropped-down assets. If there is a shortfall in cash flow, the parent gets paid last, after the public investors, or "unit holders." As cash flows in the MLP increase, the parent gets to share in the growth, receiving amounts in excess of the cash flow yields paid to the unit holders.

Ward stated that SemGroup was the third or fourth largest storage operator at Cushing, Oklahoma, the NYMEX energy hub. According to Ward, the public offering of SGLP was 10 times over-subscribed, which Ward described as uncommon. He noted that new MLPs usually price at approximately 10-12% over yield. SGLP was priced at only 4% over yield (meaning that it traded at the highest multiple of cash flows), due to market expectations that SGLP had very good prospects.

With respect to SGLP, Ward stated that the initial assets dropped down were considered to be SemGroup's most consistent cash flow producers. According to Ward, the dropdowns in

January 2008 and May 2008 were part of the original plan for the MLP, and the schedule was not changed as a result of SemGroup's liquidity issues.

Ward stated that the cash flows from SGLP flowed to SemGroup in the form of two distributions. Most of the distributions were used by SemGroup to pay off its debt, and Riverstone received a pro rata share.

9. SGLP Board of Director Comments

Billings, a member of the Board for SGLP since October 2007, stated that he was recruited as a Board member by Wallace. Billings had formerly been President of Williams Energy, as well as President of Penn Central's Energy Group. He met Wallace for the first time in 2007.

Billings stated that the other members of the SGLP Board were Kivisto (Chairman), Wallace, Foxx, Brochetti, and Mr. Andy Bishop ("Bishop") (the only other outside Board member). He stated that the Board membership changed after July 1, 2008. The current Board consists of Mr. David Miller (Elliott Management), Mr. David Bernfield (Elliot Management), Mr. Gabriel Hammond (Alerian Capital), Mr. Ed Kosnik (outside Board member), and Mr. Duke Ligon (outside Board member and current Board Chair).

Billings stated that he was not a Board member at the time SGLP went public, but was directly involved in the subsequent dropdowns in 2008. He stated that the MLP business model and the dropdowns in 2007 and 2008 were continuations of SemGroup's business strategy. He stated that SemGroup's intention to make additional dropdowns was announced at the time of SGLP's IPO in July 2007.

Billings stated that he chaired the Board's Conflicts Committee, which consisted of himself and Bishop. The SGLP Board passed a resolution giving the Conflicts Committee authority to hire an investment banking firm on behalf of SGLP, to assure impartiality and fairness of pricing during the dropdown process. From a total of four investment banking firms, the Conflicts Committee selected Duff & Phelps. He stated that Duff & Phelps had experience in dropping down assets and working with MLPs. In addition, both the public (SGLP) and private (SemGroup) companies had attorneys who provided legal advice for the transaction, to protect their respective clients' interests.

Although the Conflicts Committee was not required to vet the May dropdowns because of the amounts involved, Billings wanted to do so because SGLP was a new company, and he wanted to ensure that its dealings with the private company were transparent and above scrutiny. Billings stated that he and Bishop reviewed Duff & Phelps final reports, which assessed the pricing as fair, and they both agreed with its conclusions. Billings advised that the market reaction to these dropdowns was positive and that there were no detractors to the pricing of the transaction.

With regard to the Board memberships of Kivisto, Foxx, Brochetti, and Wallace, he believed that it was a standard procedure under the MLP business model to allow the executives of both the public and private companies to assume positions with each company. He believed that it was not a conflict of interest for the board and stated that it was fully disclosed in the IPO.

10. Kivisto's role within the MLP Business Model

Stallings stated that Kivisto was on the MLP's Board, which approved of the MLP business model and all dropdown transactions. According to Stallings, Wallace and Kivisto

were not involved in the implementation of the dropdowns. He stated that Stallings, Foxx, and Brochetti were primarily responsible.

Stallings stated that it was his opinion that Kivisto had no desire to be a CEO of a public company, and that Kivisto's focus had always been on trading and acquisitions. Stallings stated that it was his opinion that Kivisto was the visionary behind SemGroup, and that Kivisto considered SemGroup to be his personal company. Stallings also stated that Kivisto's emphasis had changed over the years. In the early years, Kivisto was very involved in SemGroup's day-to-day trading, and as time went on he became more and more involved in community and public projects, which left him less time to devote to SemGroup. Stallings stated that SemGroup went from being a "sleepy little company" to a high exposure company, in part through Kivisto's involvement in community projects and political events.

11. SemGroup Officer Changes

Brochetti was employed by both SemGroup and SGLP from July 2007 through February 2008. On March 1, 2008, he resigned as SemGroup's Vice President of Finance, but continued his duties at SGLP. On the same day, the MC elected Ronan as his successor. *See* Exhibit 87.

On July 21, 2008, Foxx resigned his position at SemGroup and as a member of its MC, but continued with his duties at SGLP. *See* Exhibit 88.

The MOA dated July 22, 2008, noted that Kivisto had been placed on administrative leave, effective July 18, 2008, and that Ronan would be the Acting CEO and President of the General Partner and SemGroup. *See* Exhibit 89.

V. THE EXAMINER'S FINDINGS REGARDING THE POTENTIAL IMPROPER USE OF BORROWED FUNDS, FUNDS FROM THE DEBTORS' OPERATIONS AND LIQUIDATION OF ASSETS TO SATISFY MARGIN CALLS RELATED TO THE TRADING STRATEGY

A. Scope of Documents Reviewed

In connection with the Investigation, the Examiner considered, among other things, the following:

1. All bank loan documents, loan amendments, covenants, waivers of covenants and reports to banks on meeting covenants;

2. The credit agreement between General Electric Capital Corporation ("GECC") and SemCrude Pipeline, and the loan agreement among SemGroup Holdings L.P. and Manchester Securities Corp. and Alerian Finance Partners, L.P.;

3. Gained an understanding of how the Company managed liquidity and cash; and

4. Analyzed the SemGroup entities' cash flows to identify key payments made to brokers, their credit facilities, SemGroup personnel and any other third parties.

B. The Debtors' Credit Relationships

1. BOK

In early 2000, BOK advised that it was approached by Wallace and Foxx, on behalf of Seminole Transportation and Trading (SemGroup), requesting a $58 million loan to purchase Dynegy Pipeline and Storage in Cushing, Oklahoma. BOK provided a loan to purchase Dynegy Pipeline, which, according to Foxx, was the lynchpin of the founding of SemGroup.

In June 2000, SemGroup acquired Petrosource. BOK was the lead bank in that purchase. Later, a bank consortium was formed by BOK, BNP Paribas and Fortis Bank, to assist SemGroup with its credit facility needs. BOK felt secure in granting the loan because BNP Paribas was recognized as one of the premier banks with energy loans, and it had the reputation of closely scrutinizing potential borrowers. It was BOK's understanding that SemGroup's strategy was to purchase and hold inventory in storage and to sell it at a later date for profit — in other words, to engage in asset-based trading.

In approximately 2003, SemGroup attempted to expand its credit facility to $100 million, which was beyond the limit of credit to which the BOK-led consortium was willing to commit. At that point, BOK contacted Fleet Bank. BOK advised Fleet that SemGroup had outgrown BOK's lending capabilities and was looking for additional financing to consolidate its credit facilities. Fleet Bank then stepped in and assumed a leadership role with the loan, although BOK and BNP Paribas continued to be participants in the credit facility. Ronan, SemGroup's current CEO, was the principal lending officer for Fleet Bank on this loan. Fleet Bank was later taken over by BOA, which assumed the position of lead lending institution.

BOK retained SemGroup's checking accounts, one for each business unit. Eaglwing and Westback also maintained checking accounts at BOK. BOK understood that Eaglwing was a trading business unit for SemGroup, and that the Westback checking account was Kivisto's personal account. BOK was unaware that Kivisto engaged in personal trading through Westback.

If BOK had any questions or needed additional information regarding SemGroup, it normally contacted Cooper, and, to a lesser extent, Wallace.

a) SemGroup's Reporting Requirements to BOK

SemGroup's reporting requirements to BOK during the years that BOK was the lead bank (2002-2003) were standard within the banking industry. After BOA became the lead bank, BOK operated under the credit agreements for the bank consortium and, since October 18, 2005, under the Pre-Petition Credit Agreement with BOA.

SemGroup's reporting requirements under that Pre-Petition Credit Agreement included monthly financial statements, borrowing base reports, compliance certificates, and position reports that included a net hedge position. *See* Exhibit 17 for all MtM and Position Reports from January 4, 2007 through June 27, 2008; *see also* Exhibits 90 and 100 for examples of Compliance Certificates and Borrowing Base Reports. These reports were not submitted directly to BOK, but were posted on an electronic system, known as "IntraLinks," by BOA.

Up until 2008, BOK had the opinion that SemGroup was a profitable company, as all of its affiliated groups seemed to be doing well. BOK was aware that there were some liquidity issues with SemGroup, since it was constantly seeking equity capital due to its rapid growth.

b) Kivisto's Duties as a Member of BOK's Board of Directors

On February 28, 2006, Kivisto became a member of BOK's Board of Directors. All BOK Board members were required to prepare a "Questionnaire for Directors and Executive Officers of BOK Financial Corporation," which Kivisto did in 2006, 2007 and 2008. *See* Exhibits 91A, 91B, and 91C.

Kivisto was a member of the Board of Director's Loan Committee. It is BOK's opinion that Kivisto had a fiduciary responsibility to disclose his interest in Westback to BOK, since it is

now aware that it was Kivisto's personally owned company, which he used to trade in and through at SemGroup.

As a member of BOK's Board of Director's Loan Committee, Kivisto abstained from voting during presentations of SemGroup matters before the Loan Committee. It is BOK's opinion that, in addition to abstaining, Kivisto had a fiduciary responsibility to inform it of his ownership interest in Westback, Westback's relationship with SemGroup, and Westback's substantial debt to SemGroup.

It is BOK's opinion that, as a member of its Board of Directors, Kivisto also had a fiduciary responsibility to report to the BOK Board if SemGroup's credit facility with BOK was in jeopardy due to SemGroup's unrealized commodities trading losses, margin calls, and/or liquidity issues. Kivisto never did so.

c) Alleged Misrepresentations to BOK by SemGroup Personnel

It is BOK's opinion that Kivisto, SemGroup and some of its personnel defrauded BOK in several ways:

First, Kivisto made a false statement in SemGroup's November 2007 meeting with BOK, when he stated that SemGroup was rolling its trades forward because of the timing of anticipated SemGroup sales of oil in the immediate future. SemGroup actually rolled its trades forward as part of Kivisto's trading strategy not to accept losses on its options trades.

Second, SemGroup, through the employees who signed its MtM and Position Reports (primarily Cooper), submitted false information in two apparent ways. *See* Exhibit 17. First, the Cumulative Stop-Loss Position figures listed by date were not accurate, since BOK understood

them to represent the net dollar trading balance for all SemGroup hedges and trades as of the dates they were submitted. For example, on June 27, 2008, the MtM and Position Report listed a Cumulative Stop-Loss figure of negative $4,855,829 (the first time it was negative). That amount appears to be false, as reflected by the more than $2 billion negative figure associated with SemGroup's NYMEX trading book alone in July 2008.

Third, BOK understood that the figures on the MtM and Position Reports represented the net MtM trading balance of all SemGroup commodity trades for all of its trading accounts, at BOK and elsewhere, as of the dates listed. It is BOK's opinion that if the Cumulative Stop-Loss Position figure did not include unrealized losses, the description "Mark to Market" on the MtM and Position Report was misleading. BOK questioned what SemGroup meant to report in its MtM and Position Reports if it did not actually report its MtM positions.

It is BOK's opinion that the second false statement on the MtM and Position Reports is the statement: "Since the last submitted report, all Restricted Persons have operated within the guidelines of the Company's Risk Management Policy," because, based upon BOK's review of SemGroup's RMP, all trading should have been, but was not, based upon physical inventory.

Fourth, Cooper made a false statement in late May 2008, when he told BOK that all of SemGroup's trades were backed by physical inventory.

Fifth, BOK had no timely knowledge of the Manchester/Alerian Loan to SemGroup in May 2008, or the GECC loan to SemGroup in June 2008, or of the negotiations leading to the issuance of those loans.

A representative of the Office of the Comptroller of the Currency ("OCC") familiar with the SemGroup trading account at BOK stated that it was his opinion, after reviewing MtM and Position Reports for 2008, that the net trading figure did not appear to be accurate, and that it appeared that SemGroup's trading activity in its BOK account was speculative.

2. Fleet Bank/Bank of America (BOA)

BOA was the lead bank in a credit facility arrangement with SemGroup, which involved approximately 140 banks. *See* Exhibits 92 and 93. BOA inherited its relationship with SemGroup from Fleet Bank in approximately 2004. The Fleet loan agreement was amended and restated in its current form as of October 18, 2005 (the Pre-Petition Credit Agreement), with BOA as administrative agent for the consortium of participating lenders. Ronan was listed in the Pre-Petition Credit Agreement as BOA's point of contact, as the Administrative Agent.

Ronan had been BOA's energy group relationship banker, responsible for negotiating loan agreements and amendments on behalf of BOA, as well as signing loan documents. He was one of the BOA employees assigned to the "SemGroup" team at the time, along with Brochetti, a senior credit officer on the team. Ronan left BOA in August 2006, spending the next three months on "garden leave," a period in which BOA employees were prohibited from working with the bank's competitors. Ronan subsequently went to work for Merrill Lynch Capital (which later became GE Capital) and, in March 2008, for SemGroup.

Brochetti left BOA in the fall of 2005 and later went to work for SemGroup. Like Ronan, Brochetti had formerly been employed by Fleet Bank. In 2003, while he was with Fleet Bank, SemGroup applied for a loan with Fleet, during which time Brochetti worked with SemGroup's Wallace to facilitate it. According to Brochetti, neither he nor anyone else he dealt

with at Fleet/BOA had misgivings about engaging in credit activity with SemGroup at the time. It seemed to him to be a solid company with a bright future. If Brochetti had not been convinced of this, he stated that he would not have accepted a position with SemGroup in 2005.

BOA was responsible for reviewing SemGroup's requests for additional credit from the consortium. It analyzed SemGroup's financial statements and other reports and made recommendations regarding the extension of new credit to it, based upon its performance and financial health.

According to BOA, it dealt primarily with Cooper regarding such issues as how funds might flow for acquisitions and questions regarding SemGroup's RMP, and with its Chief Accounting Officer, Stallings, on questions such as the reporting of unrealized losses. BOA also advised that it dealt with Brochetti, SemGroup's Senior Vice President for Finance, on working on amendments to the Pre-Petition Credit Agreement. As time went by in the relationship, BOA representatives came to know approximately 15-20 people at SemGroup, since it became routine for BOA to contact people at lower levels for the specific information it needed. Among those people were Jamie Cooper, and Jennifer Allison ("Allison").

BOA representatives traveled to Tulsa approximately twice in the fall of 2006, to attend investor meetings and to take a tour of SemMaterials. In December 2006, BOA employees visited SemGroup's offices in Tulsa, primarily to introduce the new members of its team to SemGroup. BOA had contact with SemGroup's management at a February 2007 North American Prospect Expo ("NAPE") dinner in Houston, and a March 2007 conference in New York on MLPs, at which time a BOA representative discussed an amendment to create a MLP with Brochetti (resulting in a subsequent trip to Tulsa to discuss the creation of a MLP, again

with Brochetti). Other BOA trips included a meeting in Boston in September 2007, and a trip to Tulsa in October 2007, to meet with Brochetti, Wallace, Cooper, possibly Stallings, and Perkins, who had begun taking on a larger role as assistant treasurer as Cooper's health began to decline. (Kivisto dropped in on this meeting, although Kivisto's contact with the BOA representative was not extensive.) A BOA representative also took a trip to Houston in January 2008 regarding the MLP, at which time BOA met with Stallings and possibly Foxx. BOA also visited Tulsa again sometime after the Houston meeting, with respect to the MLP amendment.

BOA advised that, in conversations with SemGroup after Ronan and Brochetti became SemGroup employees, it tended to trust them, because they were former BOA employees.

a) SemGroup's Reporting Requirements to BOA

(i) MtM and Position Reports

BOA's representative provided the following information to the Examiner: The purpose of the MtM and Position Reports was to show whether the company's trading positions were in compliance with certain limits established in Schedule 7.13-1 of the Pre-Petition Credit Agreement (*see* Exhibit 11), and indicated in the "Limit" column of the report, and to provide a signed certification by a designated company official that the positions were in compliance with the company's RMP. *See* Exhibits 6 and 90.

According to BOA, the significance of the MtM and Position Reports for the lenders was that they could only lend against hedged inventory. Section 6.02(i) of the Pre-Petition Credit Agreement required SemGroup to submit the MtM and Position Report each Friday (or the next business day if Friday was a holiday), reporting its positions as of the immediately preceding

business day (Thursday). *See* Exhibit 94. Section 7.13 of the Pre-Petition Credit Agreement provided additional context for the MtM and Position Reports. *See* Exhibit 42. Section 7.13(a) allowed transactions that were good faith violations of the RMP to be remedied within one business day of the discovery of the violation. Section 7.13(b) required price protection of physical inventory, except that there could be open positions on certain quantities of physical inventory within the limits set forth in Section 7.13(b)(i) and Schedule 7.13-1 (per Section 7.13 (b)(ii)) and any amendments to those limits). The "Limit" column of the report showed the quantity of physical product in the units indicated that SemGroup was allowed not to price protect.

BOA advised that the "Position" column showed SemGroup's actual position for each category on the effective date of the report. A positive figure in the Position column indicated that SemGroup had that quantity of unhedged product on hand, while a negative figure (in parentheses) indicated that SemGroup was short by that amount of product that it had contracted to sell at a future date.

Per BOA, the "Spread Position/Limits" section of the report reflected the effect of product price fluctuations. For example, prices historically fluctuate in a certain way between October and April (a "time spread"), or refining crude oil into various products affects price in certain ways (a "crack spread").

According to BOA, the "Daily Stop-Loss Limits" set the risk tolerance for daily changes in MtM value, *i.e.*, how much SemGroup could lose in a given day. The RMP states that if an exception occurred, *i.e.*, if a limit was violated, the Treasurer was supposed to bring the matter to

the attention of the CFO and the CEO. The normal reaction to a position approaching the daily stop-loss limit would be for SemGroup to cease trading on that day.

BOA stated that the "Cumulative Stop-Loss" is a rolling four-quarter test comparing the sum of all realized and unrealized MtM gains and losses against a limit defined as 20% of total working capital on a set date. The figures in the position column are supposed to represent all reported trading, not just the positions for bank-related trading accounts. BOA, as administrative agent for the lenders, stated that it had no authority to check the accuracy of SemGroup's reported position figures with SemGroup's brokers.

BOA provided the manner in which unrealized net losses were reported by SemGroup under the Pre-Petition Credit Agreement, and how those losses were treated in EBITDA calculations, by referring to the audited Year-End Financial Statements submitted by SemGroup with its compliance certificate for 2007. *See* Exhibit 95. On page 3 of this document, captioned "Reconciliation of Guarantor Adjusted Gross Margin and Adjusted EBITDA," SemGroup reported a net unrealized loss of over $937 million dollars as of December 31, 2007. Subsequent calculations in the same column produce a negative EBITDA of over $287 million. BOA stated that it did not consider this EBITDA figure to be meaningful, because BOA shared SemGroup's opinion that it did not reflect economic reality.

BOA's stated that SemGroup's position is set forth in footnote A at the bottom of page 3 of this document.[16] *See* Exhibit 95.

[16] The footnote states: "Net unrealized (gain) loss related to derivative instruments reflects the impact of interim valuations of the Partnership's derivatives and changes in option premiums paid or received and does not take into account the gross margin to be achieved upon the delivery of the product or the fact that the matching inventory cannot be marked to market. The Partnership believes such impact should be excluded when evaluating its financial results, as the net result of its risk management activities is to produce and protect

For that reason, subsequent calculations on page 3 of the Year-End Financial Statement produced an "adjusted EBITDA," in which net unrealized losses were removed from the calculation, and the adjusted EBITDA was a positive number. This understanding is consistent with the Pre-Petition Credit Agreement as noted in its definitions section (Article I), and the definition of such terms as "Consolidated Net Income," "Consolidated EBITDA," and "Consolidated Adjusted EBITDA." The provisions of Sections 7.18 through 7.20 of the Pre-Petition Credit Agreement are built upon those definitions (*see* Exhibit 42), and the understanding that "adjusted EBITDA," which does not include unrealized net losses, was a more accurate representation of SemGroup's financial status.

BOA advised that the provision regarding the calculation of an "adjusted EBITDA," which does not take into account net unrealized losses, is not uncommon. While it is not a feature of every loan agreement that BOA has with companies involved in energy commodities trading, it does appear in a number of other BOA loan agreements with such companies. In the case of SemGroup, this method of handling the unrealized net losses dates back to SemGroup's prior relationship with Fleet Bank, and was reincorporated into the Pre-Petition Credit Agreement by BOA.

BOA was aware, by virtue of SemGroup's Year-End financial Statement for 2007, of SemGroup's unrealized net loss of over $937 million as of December 31, 2007. The compliance certificate which enclosed this financial statement was submitted by SemGroup on or about March 28, 2008 (*see* Exhibit 96), in accordance with the Pre-Petition Credit Agreement's requirements. BOA was also aware of SemGroup's unrealized loss figures by virtue of its

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the net margin on the sale of its product inventory established at the time the derivative instruments were entered into." *See* Exhibit 95 at page 3.

monthly financial statements, which were submitted 45 days after the end of the periods they covered, in accordance with Section 6.01(d) of the Pre-Petition Credit Agreement. *See* Exhibit 97.

BOA could not state with any certainty whether or not the positive positions reported on MtM and Position Reports from January 2008 through June 2008 were accurate. BOA stated that they did not attract its attention as being unusual when they were submitted. BOA reported that it did not have access to SemGroup's trading book.

BOA did not know with certainty whether or not SemGroup had the requisite inventory to match its trading, and it declined to offer an opinion on that issue. From the Evergreen reports, BOA knew that SemGroup had inventory, and that Evergreen's spot check verified some of the reported quantities on hand at the time of Evergreen's audits.

A BOA representative discussed the issue of high unrealized losses on at least one occasion with Brochetti, and on several occasions with Cooper, in 2007. During one discussion, BOA asked Cooper to explain the circumstances in which SemGroup's unrealized losses could become realized losses. Cooper replied that he could not think of such a situation. He stated that perhaps a "9/11 type situation," in which all of SemGroup's delivery infrastructure might be destroyed, might result in having to realize a high level of unrealized losses, but that was the only possibility that he could remotely imagine. Brochetti's and Cooper's explanations to BOA about SemGroup's unrealized losses involved the assertions that SemGroup always had futures contracts for sales of product that would wipe out the unrealized losses once the sales were consummated.

Regarding the timeliness of MtM and Position Reports submissions, BOA advised that, at the Examiner's request, it reviewed the reports submitted by SemGroup in 2007 and 2008, and found only two instances of late submissions (one in October 2007 and the other in May 2008). In both instances, the reports had been due on a Friday and were submitted the following Monday. BOA's view is that, although Section 6.02 of the Pre-Petition Credit Agreement states that the Administrative Agent had no obligation to request any report or monitor compliance with any such request for delivery, it did maintain a calendar system to catch late submissions. These were the only instances that BOA could find in which SemGroup submitted its reports late. According to BOA, it did not consider the late submissions to be significant in either instance. BOA advised that it relied upon the accuracy of the certification statement at the bottom of the report that SemGroup was in compliance with its RMP.

The Examiner's review of the MtM and Position Reports and the supporting data for them revealed 19 occasions when SemGroup submitted its weekly position reports with data from Friday (17 times) or Monday (2 times), rather than from Thursday, as was required. On each one of those Thursdays, SemGroup was not in compliance with its trading limits. The Examiner's further review revealed that there were numerous days in 2007 and 2008, and an even greater number of instances, when SemGroup was in violation of its trading limits. SemGroup was in violation of its banking covenants on each one of those occasions.

An explanation for SemGroup's behavior was found in interviews with Ms. Mary Catherine Ward ("M.C. Ward") and Coen, as follows.

M.C. Ward was transferred into SemGroup's Risk Management in February 2008. She assisted in the preparation of the MtM and Position Reports. She stated that if SemGroup was

outside of its position limits, the report would not be sent to BOA, but would be delayed a day or two until SemGroup would be in compliance with them. She also stated that she reported daily to Coen and Oven, and if SemGroup was outside of its position limits, she would highlight that to them.

Coen stated that M.C. Ward or Jamie Cooper would highlight any violations of SemGroup's trading limits. *He would then make additional trades to bring SemGroup back within its trading limits*.

On July 15, 2008, BOA sent an e-mail to M.C. Ward, asking her for MtM and Position Reports for July 3, 2008 and July 10, 2008. SemGroup never produced them. The last MtM and Position Report it submitted to BOA was dated June 27, 2008. *See* Exhibit 98.

(ii) Borrowing Base Reports (BBR)

BOA provided the following information: Section 6.02(e) of the Pre-Petition Credit Agreement established the requirement for the BBR, and required that it be submitted bi-weekly, or weekly if certain limits were being approached. *See* Exhibit 94. SemGroup voluntarily submitted the BBR on a weekly basis, rather than bi-weekly. The BBR gave a picture of SemGroup's collateral, discounted at defined rates, and showed how much borrowing ability SemGroup had left on the date of the report. The purpose of the report was to ensure that lending to SemGroup remained within defined collateral limits. The form of the BBR is provided at Exhibit I of the Pre-Petition Credit Agreement, and the various terms used on the BBR are defined in Article 1, along with the percentages by which each category of collateral was to be discounted. *See* Exhibit 99. BOA advised that having a borrowing base structure earned a higher rating from Moody's and Fitch, both of which rated bank debt. Cooper was the

official who signed the BBRs for SemGroup, certifying that, all of the information submitted was true and correct.

BOA explained the significant aspects of the various line items on the BBR. *See, e.g.,* Exhibit 100, BBR dated July 11, 2008. Under heading A, "Borrowing Base Assets," item A(1), "Eligible Cash Equivalents," is self-explanatory and is defined in the Pre-Petition Credit Agreement. The percentages applied to discount the various types of receivables in the next five line items are based upon a formula that is weighted in favor of investment-grade receivables. Items A(2) and A(3) refer to deliveries of investment-grade crude to entities with a defined Moody's rating, or which are guaranteed by an entity with such a rating. Items A(4) and A(5) refer to receivables for asphalt, and are weighted less than crude, because asphalt is generally worth less than liquid crude. Item A(6), "Other Eligible Receivables," refers to non-investment grade receivables. Item A(7), "85% of the Net Liquidating Value of Hedge Positions in Broker Accounts," only applies to items that are defined as part of the lenders' collateral. It includes margin deposits that are in excess of the required amounts due to price fluctuations, because those excess amounts would be refunded when the positions were liquidated. Item A(8), "Hedged Eligible Inventory," refers to inventory other than asphalt, and must be price protected. Item A(9), "80% of Eligible Exchange Receivables," is used for the value of transactions in which the counterparties owe each other oil, and represents the net of the amounts owed. The transactions included in this item are not to be included in any other category in the BBR.

According to BOA, item A(10) refers to transactions in which SemGroup is a buyer and is required by the seller to post a letter of credit. SemGroup, not knowing what the price would be on the effective date of the sale, would have to post a letter of credit in excess of the anticipated price. This item gives SemGroup collateral credit for 80% of the excess value of the

letter of credit. Item A(11), the "Borrowing Base Subtotal," represents the total collateral available against which lenders can lend (subject to the "Borrowing Base Limit"). When the "Borrowing Base Deductions" in Section B are subtracted from this figure, it results in line item B(4), the "Borrowing Base Subtotal." SemGroup is allowed to have total outstanding borrowing under the Agreement against an amount of collateral called the "Borrowing Base Limit," represented by the lesser figure of the "Borrowing Base Subtotal" and SemGroup's "Working Capital Availability Limit." In Section C, outstanding letters of credit and working capital loans are deducted from the Borrowing Base Limit to yield the amount of credit left available to SemGroup under the Pre-Petition Credit Agreement for letters of credit and working capital loans (Item C(5)).

BOA's view is that the BBR, dated July 11, 2008 (*see* Exhibit 100), and certified as accurate by Cooper, constituted a material misrepresentation by SemGroup, because it showed in excess of $72 million of credit availability as of July 7, 2008. It was submitted on July 11, 2008, one day after SemGroup sent BOA an e-mail (July 10, 2008) stating that it was out of money. *See* Exhibit 64.

BOA declined to offer an opinion as to whether or not any other reports submitted by SemGroup were potentially misleading.

b) IntraLinks

IntraLinks is a database used by lenders to post the information that borrowers are required to provide, so that it can be accessed by all lenders participating in the loan(s) to the borrower. It is organized into separate "rooms," so that BOA had access to the reports filed by all borrowers with whom it dealt under the terms of its agreements with them. There is a public

side and private side to IntraLinks, so that lenders can choose whether to access the private side or the public side. The information posted on IntraLinks for a given relationship, in this case for SemGroup, consisted of all of the financial reports (MtM and Position Reports, BBRs, financial statements, etc.), which the company provided under the Pre-Petition Credit Agreement, amendments to the Agreement, and the Evergreen reports (since they were required by the Pre-Petition Credit Agreement). Bowen's reports were not posted on IntraLinks, since they were not required by the Pre-Petition Credit Agreement.

c) Requests for Credit Extensions and Use of Loan Proceeds

BOA provided the following information: Under Section 4.02 of the Pre-Petition Credit Agreement, whenever SemGroup requested an additional loan amount or a letter of credit, it was required to certify that it was in compliance with all terms of the agreement, and that no default would result from the requested credit. SemGroup borrowed under the Pre-Petition Credit Agreement's loan facilities almost daily, so it was required to make this certification almost daily. Each SemGroup borrowing request, the form of which is provided in Exhibit A of the Pre-Petition Credit Agreement, was sent by SemGroup's Treasury Department, generally by Tanksley to either BOA's Dallas or Charlotte office. BOA's account representative did not routinely see the credit requests, but would ask to see them on occasions when SemGroup's liquidity was tight.

SemGroup was not required to state the purpose for which each individual borrowing was to be used. However, Section 6.11 identifies the purposes for which proceeds of working capital loans could be used, as follows: a) to swap old debt under the previous Agreement for new debt under this Agreement; b) to purchase hedged eligible inventory and contango loans; c) to fund

certain unreimbursed amounts defined elsewhere in the Agreement; d) to provide margin or similar support in connection with NYMEX obligations, *i.e.*, to pay margin calls on NYMEX; and e) for general corporate purposes not to exceed $100 million. Letters of credit, per the same section of the Agreement, could be used for the same purposes as the working capital loans. The revolver loan credit facility could be used to refinance outstanding revolver loans, to partially finance the CAMS (Central Alberta Midstream, a gas processing company in Canada) acquisition, or for general corporate purposes, not to include any purpose which violates any law or any loan document.

d) Restrictions on Trading Activity under the Pre-Petition Credit Agreement

BOA provided the following information. Section 7.13(c) of the Pre-Petition Credit Agreement prohibits "any swap, collar or similar agreement," except those related to price protecting petroleum inventory. *See* Exhibit 42. This language, according to BOA, prohibits trading in naked options. Section 7.04(b) is related to Section 7.13(c) in prohibiting all but certain defined swap contracts. Section 7.03(f) also restricts trading activity by prohibiting indebtedness for swap contracts that involve speculation or taking a market view. Also, Section 7.09, which prohibits SemGroup from entering into any transactions with affiliates, would, in BOA's opinion, prohibit the transactions that resulted in the Westback receivable, since BOA believes Westback would be considered an affiliate as defined in the Agreement.

e) Employee Comments about SemGroup's Reports.

Brochetti stated that reporting was done by SemGroup's Treasury Department, which prepared and submitted the reports to banks, including SemGroup's weekly position reports.

Brochetti considered the reporting package that SemGroup furnished to its lenders to be more robust than was normally required. He thought that SemGroup's weekly borrowing base and position reports were extensive and accurate.

Stallings stated that each business unit would provide borrowing base summary information to Treasury on a weekly basis, and that the information would include an estimate of its inventory. Treasury would then consolidate the information into an overall BBR that would be forwarded to the banks.

No one in Stalling's group attempted to compare SemGroup's overall inventory with its trading activity. In other words, to Stallings' knowledge, no one in his group, or anywhere else in SemGroup, attempted to determine if its trading was asset-based. Stallings stated that from his perspective there was no reason that the trading needed to be broken down by commodity type, or options vs. true hedging of inventory, etc.

Lewallen stated that it was virtually impossible to have precise inventory figures for a point in time because of the nature of the business, but that SemCrude used a software program referred to as "SCADA" to make estimates of physical inventories. She stated that she did not know whether or not SemGroup's other operating segments used SCADA.

f) 2007 Bowen Report Request by BOA

BOA provided the following information: It determined that on one day in January 2007, SemGroup was out of compliance with its daily stop-loss limit. BOA arranged a conference call with Brochetti, Cooper and possibly Stallings to discuss how that situation had occurred. SemGroup's executives claimed that the occurrence was an anomaly due to unexpected

fluctuations in the price of crude oil, and that everything had returned to normal when crude prices stabilized. BOA then advised them that the lenders expected the stop-loss limits to be enforced, and that it was planning to send Bowen to SemGroup to conduct an analysis. Bowen had previously conducted a report for BOA in September 2005 when SemGroup asked for new limits under the new Pre-Petition Credit Agreement, since the company had grown considerably since the existing limits had been established. Bowen was hired on that occasion to assess the existing limits and to make recommendations as to what new limits might be appropriate.

According to BOA, the purpose of Bowen's 2007 analysis was to determine whether or not SemGroup was in compliance with its RMP. Bowen was tasked to look at the RMP, the position reports, what happened on the day in January 2007 when SemGroup was not in compliance with its stop-loss limit, and what SemGroup thought at the time regarding the supposed anomaly. Bowen had a copy of SemGroup's RMP.

BOA believed that Bowen's report stated that SemGroup was in compliance with its RMP. It stated that there were no time or fee constraints placed on his work. Bowen billed SemGroup for the study, as was customary in the industry for studies requested by a lender when a debtor company was out of compliance with its limits. Bowen traveled to Tulsa to visit SemGroup in February 2007, and, BOA believed, made two or three more trips there that spring. Bowen met with SemGroup's staff and had access to its records on his visits. Bowen's report, which indicated that SemGroup's risk management was satisfactory, was delivered to BOA. Bowen made a recommendation that SemGroup implement a VaR system, which would enable it to determine how much it had at risk on a given day. He also recommended that BOA give the report to SemGroup, so that SemGroup could implement his recommendations.

Thereafter, BOA contacted Cooper, who was responsible for issues concerning SemGroup's borrowing base, and asked for his opinion on the VaR system which Bowen had recommended. Cooper responded that VaR did not work for a "physical business" and was only applicable to traders. Cooper stated that he was not eager to implement VaR at SemGroup for that reason. BOA then asked Cooper about the need that Bowen had found to implement controls in SemGroup's trading activity. Cooper responded that the non-compliance situation in January 2007 had been an anomaly, and was the result of a purely "clerical" issue.

According to BOA, Bowen found that each of SemGroup's business lines kept track of its own positions, and that there was a need to net the various positions and manage them across all of SemGroup's business lines. Cooper's response to Bowen's recommendation was that Bowen was trying to make SemGroup into more of a trading company than it really was. Cooper stated that SemGroup would continue to do business the way it had been.

Cooper's responses did not cause BOA any serious concern because the implementation of a VAR system was only a recommendation, not a practice required under the Pre-Petition Credit Agreement, and SemGroup was essentially free to manage its activities as it saw fit in this regard. Cooper was considered by all to be the interface between crude operations, trading activities and monitoring the borrowing base, and to be capable of managing all of them. BOA's representative asked Cooper during the conversation to identify who conducted SemGroup's trading. Cooper responded that only Kivisto and two other individuals handled the NYMEX trading on the crude oil side, and that only Kivisto handled gas trading.

Bowen's comment in the report about SemGroup's delta hedging resulting in a greater number of positions, totaling 20% of the overall market positions for crude oil options beyond

three months to expiry, was actually a reference to the positions totaling 20% of a certain specific *type* of contract, not the whole market, according to BOA. Bowen told BOA, however, that his comment about this situation, and about the company needing to consider margin availability as a serious business constraint, was an "eye-opener" for the company. Nonetheless, as reported above, Cooper felt that SemGroup's existing management of its positions was effective.

g) The Evergreen Reports

BOA provided the following information: Evergreen conducted annual commercial finance examinations of SemGroup, as required by Section 6.02 of the Pre-Petition Credit Agreement. *See* Exhibit 94. Section 6.02 defined the scope of Evergreen's examination, the essential purpose of which was to audit SemGroup's borrowing base. An additional benefit of having the Evergreen report prepared annually was that it was an added measure that could result in a better rating of the bank debt from companies such as Moody's.

There were no time or financial constraints placed upon Evergreen's examination by BOA, except that the Pre-Petition Credit Agreement required the examination to be conducted within 120 days of the end of each fiscal year. Pursuant to the Pre-Petition Credit Agreement, SemGroup paid the costs of the examination, and Evergreen submitted its invoice directly to SemGroup. BOA reviewed the Evergreen reports and used them to ensure that SemGroup's borrowing base corresponded to what it was reporting in the BBRs.

Regarding Evergreen's identification of an account receivable from Westback for Eaglwing, BOA advised that this information did not cause it any concern, because Westback was assumed to be a business counterparty. According to BOA, the entry in the Evergreen report

was not the result of an Evergreen auditor discovering the receivable from any concealed records, but a mere copying of the receivable from Eaglwing's own records. It is BOA's understanding that no questioning regarding the nature of the receivable was done. This understanding is based upon the statement above the table on page 33 of the report (*see* Exhibit 35), in which the Westback receivable entry appears, that Evergreen obtained the reconciliation and verified it to the general ledger and financial statements.

Because the Evergreen report did not disclose any serious findings, BOA believed that SemGroup's borrowing base was adequate and accurately reported.[17]

h) Events of mid-July 2008

According to BOA, on July 8, 2008, a BOA representative received an e-mail indicating that SemGroup had canceled a planned meeting for bankers and investors in the Bahamas. BOA explained that the reason for the cancellation, according to SemGroup, was because it was working on an equity raising project at the time (GS TruE). BOA was aware of GS TruE. Indeed, it advised that the language in Amendment 8 of the Pre-Petition Credit Agreement was written, in part, to provide for this equity raising effort, by changing the control provisions to allow for up to $1 billion to be raised. The e-mail also advised that, although the Bahamas meeting was canceled, SemGroup wanted to meet with its bankers in Tulsa on July 17, 2008.

[17] A review of the Evergreen report (*see* Exhibit 35 at page 10), dated May 2, 2008, notes the following with respect to the total loan commitment by SemGroup's lenders: "As of the date of the examination, the bank lenders (excluding the US Term Loan B) had a total commitment of $2,406,500M, with Bank of America as Administrative Agent for the bank group, BNP Paribas and Bank of Montreal as Co-Syndication Agents, and Bank of Oklahoma, N.A. and The Bank of Nova Scotia, as Co-Documentation Agents. The $2,406,500M commitment includes an aggregate revolver commitment (GCP revolver) of $665,000M and an aggregate working capital commitment (WCC) of $1,741,500M. The aforementioned amounts exclude the amount of the US Term Loan B, which was $199,000M at 12/31/07."

Later in the evening on July 8, 2008, a BOA colleague called BOA's account representative and advised her that he and another BOA representative were planning to leave the next day to meet with SemGroup's management in Tulsa on July 10, 2008, to find out what was happening.

According to BOA, on July 9, 2008, BOA's account representative was contacted by Ronan, asking that BOA bring Bowen along when BOA came to Tulsa. BOA advised that it then had a conference call with Ronan, in an effort to find out what was happening. Ronan told BOA's representatives during the call that the GS TruE deal had been postponed indefinitely, and that SemGroup was now approaching Carlyle, Riverstone and RCM about funding a capital call for approximately $240 million. Ronan stated that SemGroup's liquidity was tight.

BOA explained that at approximately 5:30 p.m. on July 9, 2008, Ronan called BOA and informed it that "things are dire."

At approximately 9:00 p.m. on July 9, 2008, Ronan called BOA and stated that SemGroup needed between $100 million and $150 million by Friday (July 11, 2008) or Monday (July 14, 2008), and that SemGroup wanted BOA to make a bridge loan to SemGroup until it could obtain a capital call from Carlyle, Riverstone and RCM. Otherwise, Ronan stated, SemGroup would be out of money. BOA then asked Ronan to explain how this situation arose. Ronan explained that SemGroup had to meet some very high margin requirements, and that they were so high that Kivisto was at that time in New York trying to find a buyer for SemGroup's trading book. BOA asked him if SemGroup's MC was aware of the severity of the liquidity issue, and Ronan replied that it was. BOA then asked why SemGroup did not simply unwind some of its positions, *i.e.*, remove positions, sell inventory and take back margin. Ronan replied,

"I don't think we can get out of it fast enough." Ronan's answer shocked BOA because it was contrary to the situation it believed existed from the reports that SemGroup had submitted to BOA. BOA did not know why SemGroup would not have been able to sell off its inventory fast enough to resolve the crisis.

According to BOA, Ronan also requested that BOA bring its "restructuring guy" to Tulsa. This statement made it even clearer to BOA that something was terribly wrong at SemGroup.

BOA advised that on July 10, 2008, there was an internal BOA conference call. During the call, the decision was made that certain BOA representatives, who were en route to Tulsa, would not go there until such time as BOA understood the situation.

Later on July 10, 2008, there was a conference call involving BOA representatives, Ronan, Brochetti and Cooper. By the time this call was made, BOA's account representative had received an e-mail from SemGroup indicating that it was out of cash. *See* Exhibit 64. In the conference call, Ronan stated that SemGroup's problem was liquidity, not capital expansion, so SemGroup was going to proceed with its capital call, and it wanted BOA to fund a bridge loan to build inventory and to meet margin requirements. Ronan went on to say that SemGroup wanted to do an orderly wind-down over a period of the next three to six months, and that it needed the bridge loan to get it through that period. BOA advised him that it would need to inform the other banks regarding SemGroup's request because any new BOA loan would prime the Pre-Petition Credit Agreement (i.e., the BOA loan would rank prior in right) and therefore consent of the other lenders was needed. According to BOA, Ronan again told BOA that Kivisto was in New York attempting to sell SemGroup's trading book. At some point during the call, BOA advised

Ronan that it was time for SemGroup to hire restructuring advisors. When Ronan asked why, BOA replied that it was because SemGroup was out of money.

According to BOA, on July 11, 2008, Cooper and Ronan participated in a telephone call with BOA. BOA advised that it told Cooper and Ronan that, in view of the fact that SemGroup's e-mail of the previous day indicated that SemGroup was $71 million "in the hole," SemGroup could not borrow any more money from BOA. Cooper responded that SemGroup had just sent BOA a "good borrowing base report" that day. BOA understood Cooper to be referring to the BBR dated July 11, 2008. BOA's representative stated that she was shocked by Cooper's attempt to persuade it to loan SemGroup money, by submitting a BBR on July 11, 2008 (*see* Exhibit 100) with figures for July 7, 2008 that painted a positive picture of SemGroup's financial situation, in light of the fact that SemGroup had told BOA on July 10, 2008, that it was out of money.

Ronan then told BOA that SemGroup needed to obtain a $150 million draw on a letter of credit in order to sell its trading book. When BOA asked to whom the book was being sold, Ronan replied that the buyer would not permit SemGroup to identify it to BOA. BOA advised Ronan that it would have to talk to the other lenders to evaluate SemGroup's request.

BOA does not believe that it had any communications with SemGroup on Sunday, July 13, 2008.

On July 14, 2008, a BOA representative attempted to contact officials at SemGroup and got no response, other than an assurance that someone would contact BOA in one hour. Eventually, Ronan called the representative back to inform her that SemGroup had novated its trading book. BOA then advised SemGroup that it was in default of its loan.

According to BOA, on July 15, 2008, there was a conference call with numerous lenders and SemGroup. Wallace advised the participants that SemGroup had novated its trading book and was now working only with physical counterparties. From statements made during this call, BOA realized that an account receivable, which SemGroup had been carrying in its BBRs as approximately $400 million from J. Aron, was really only worth approximately $100 million, because J. Aron had been netting out its transactions with SemGroup.

On July 16, 2008, BOA participated with other lenders in a conference call in which a representative of Blackstone, who had been called into Tulsa by SemGroup's MC to consult to resolve its crisis, did most of the talking. Per BOA, Blackstone's representative informed the lenders during this call that SemGroup had been engaged in speculative trading.

In a similar conference call on July 17, 2008, Blackstone's representative described SemGroup's trading activities in more detail, saying that Kivisto had been using a "strangle" trading strategy, and that SemGroup had been engaging in speculative trading. The Blackstone representative stated that the "worst" news was that Kivisto was also using the banks' money for side trading in a parallel book (Westback), and that he owed $300 million to SemGroup.

BOA declined to offer an opinion as to whether or not SemGroup had breached the covenants in the Pre-Petition Credit Agreement by engaging in speculative trading. BOA advised that the only knowledge it had about speculative trading was the statement by Blackstone to that effect.

i) Other Events

BOA advised that it was aware that SemGroup was negotiating with General Electric Capital Credit ("GECC") for a loan for the White Cliffs project in 2008. S*ee* Exhibit 101. BOA did not know that the loan had been closed and funded until July 10, 2008. BOA advised that SemGroup was not required to report the GECC loan, or a loan from Manchester and Alerian, under the terms of the Pre-Petition Credit Agreement because those loans were made to the SemGroup entities White Cliffs and SemHoldings, which were unrestricted subsidiaries pursuant to Sections 6.25 and 6.26 of the Pre-Petition Credit Agreement. According to BOA, unrestricted entities are permitted to incur debt without being required to obtain consent by the lenders participating in the Agreement.

BOA stated that it never received any PwC management letters from SemGroup. Pursuant to the Pre-Petition Credit Agreement, SemGroup was required to provide to BOA any PwC management letters if SemGroup's independent auditor, PwC, had made any significant findings in its audits.

3. Manchester Securities/Alerian Finance Partners, L.P. Loan

Manchester Securities Corp. ("Manchester") is a wholly owned subsidiary of Elliott Associates, L.P. ("Elliott"). In May 2008, a representative of Elliott was contacted by Alerian Finance Partners, L.P. ("Alerian"), who advised him that SemGroup was looking for immediate financing in order to make some business acquisitions. It was explained that Deutsche Bank was initially interested in providing the funding to SemGroup, but it had internal restrictions on capital which precluded it from making a loan at that time. Deutsche Bank was partnered with

Manchester and Alerian on the SemGroup loan, but only for a commission for bringing the deal to the eventual lenders.

In May 2008 due diligence inquiries were conducted by Elliott and Alerian. As a part of its due diligence, a conference call was made in late May or early June from Elliott to Brochetti, Stallings and James Griffin. Numerous issues were discussed about the loan at that time, including SemGroup's potential use of the proceeds. SemGroup was asked to provide financial documents, including its 2007 full year balance sheet, as well as for first quarter of 2008 (which was not posted on the company's website).

During the due diligence call, Brochetti was asked about the potential repercussions to SemGroup if oil had a $30.00 per barrel increase in one day. According to Elliott, Brochetti stated that the company was totally "hedged," and that it had additional available credit to cover its positions.

In another call in late May 2008, Elliot's representative spoke to Brochetti about SemGroup's overall needs and its intended use(s) of the loan proceeds. Brochetti advised Elliott that the money would be used by SemGroup for third party acquisitions and possibly upstreaming some capital to the parent company, SemGroup, L.P., to be used for company expenditures. According to Elliott's representative, Brochetti emphasized that he wanted to complete the loan immediately, so that SemGroup would not lose out on a deal in progress. Brochetti did not disclose any specifics of this "deal" during the conversation.

According to Elliott's representative, SemGroup had a clean record with no pending negative litigation. The loan terms had to be approved by Elliot's Board of Directors and SemGroup's MC.

Based upon the due diligence it conducted and SemGroup's representations, a loan agreement was signed by the parties on June 25, 2008, in which Manchester/Alerian would loan SemGroup Holdings, L.P., $150 million (Manchester loaned $125 million and Alerian loaned $25 million). *See* Exhibit 102. The loan was for one year at 12% interest. The loan was secured by SemGroup Holdings' 100% interest in SGLP, SemGroup's publicly traded company. In the event of a default, the lenders had the right to exercise the voting rights of the collateral.

On July 17, 2008, Elliott was informed that the public stock price of SGLP was down. Elliott and Alerian representatives contacted Brochetti that afternoon, at which time Brochetti informed them that SemGroup was having a liquidity problem and that it was trying to raise capital. According to Elliott's representative, Brochetti stated that SemGroup was attempting to sell the Manchester/Alerian loan for a profit, but he provided no details in this regard.

On July 18, 2008, Elliott had a conference call with Brochetti and Foxx regarding SemGroup's problems. Foxx stated that the upcoming Monday was "crude settlement" day, and that SemGroup would be receiving a large amount of cash from accounts due in its crude business units. Later that day, Elliott concluded that SemGroup could not survive and would most likely have to file for bankruptcy protection. It was decided that Manchester/Alerian would exercise its rights under the default clause in the loan agreement and assume control of the parent company. Manchester/Alerian served notice in writing on SemGroup Holdings to this effect, and that it was replacing three of the Board Members of the General Partner (Kivisto, Wallace and Foxx). Two independent members remained on the five member board.

a) References Made to Manchester/Alerian Loan by SemGroup Employees

According to Foxx, this loan was put together by Brochetti. Foxx thought that the loan proceeds were going to be maintained as cash on hand to show to potential investors during the GS TruE negotiations. Another reason for the loan was that SemGroup managers planned to travel for approximately three weeks as part of the GS TruE negotiations, and, given the volatility in commodity prices, SemGroup wanted to have additional cash available. Foxx signed for the loan. According to Foxx, SemGroup Holdings, a holding company with significant assets, was used as collateral.

Brochetti stated that he put the $150 million loan together (negotiations began in May 2008, with a closing in June 2008) for the purpose of enhancing the liquidity of the company. According to Brochetti, there was no specific purpose for the loan except to reflect a positive liquidity position when making "road show" presentations to potential investors in connection with the GS TruE financing effort. Brochetti indicated that the plan was never to use the cash from this loan, and only to have additional liquidity available in the event of rising commodity prices, while management focused on the road show. Brochetti stated that the loan was easily obtained since SemGroup Holdings was used as collateral. Brochetti further advised that SemGroup Holdings held 12,500 units of SGLP and that it possessed a net worth in excess of $400 to $450 million, while the loan was only for $150 million.

Ronan stated that the Manchester/Alerian loan was a $150 million loan put together by Brochetti, and was acquired with a relatively high rate of interest. Some of the loan proceeds were used to pay margin calls and the rest was used to address loan credit. He stated that he knew of no restrictions regarding the use of the loan proceeds.

(1) Alleged Misrepresentations by SemGroup

Elliott claims that SemGroup (specifically, Brochetti) misled it by representing that the loan proceeds would be used for business acquisitions and normal company expenditures. Elliot claims that SemGroup was not to use the loan proceeds to reimburse investors (by paying dividends), or to buy assets owned by investors. Based upon the fact that the company filed for bankruptcy protection less than 30 days after the loan proceeds were disbursed, Elliott believes that SemGroup's management knew that SemGroup was in trouble and needed the cash to cover the margin calls related to its trading activity.

Elliott's representative stated that it had no contact with Kivisto or Wallace. Elliott also stated that it was unaware of Westback or the potential GS TruE financing effort until after SemGroup filed for bankruptcy. Elliott claims that knowledge of either situation would have been "deal busters," because it would indicate liquidity problems at SemGroup.

Alerian's representative stated that it relied upon Brochetti's representation that SemGroup did not engage in speculative trading and ran a matched book. During the due diligence process, Alerian was led to believe that the loan was for acquisitions and normal company expenditures. Payments to margin requirements were not discussed during the negotiations for the loan. It is Alerian's opinion that Brochetti may not have had knowledge of the underlying reasons for the loan.

4. General Electric Capital Corporation (GECC) Loan

On June 17, 2008, GECC loaned SemCrude Pipeline, L.L.C. $120 million pursuant to a credit agreement with it (the "GECC Loan"). *See* Exhibit 101. GECC is also one of the lenders

to SemCrude pursuant to the Pre-Petition Credit Agreement. Further, GECC is one of the lenders to SGLP, pursuant to a credit agreement dated July 20, 2007, in which Wachovia is the administrative agent. Finally, GECC is a member of the lending group that provided the DIP loan to SemGroup.

Ronan, SemGroup's current CEO, previously worked for Merrill Lynch Capital and was the relationship manager for Merrill Lynch Capital's dealings with SemGroup. GECC acquired Merrill Lynch Capital in early 2008, and Ronan worked for GECC from the time of the acquisition until he began his employment with SemGroup, in approximately March 2008.

On July 11, 2008, Ronan, on behalf of SemCrude Pipeline, L.L.C., SemCrude, L.P., and SemOperating G.P., L.L.C., executed a drawdown certificate, in which $54,075,000 was drawn on the GECC loan. *See* Exhibit 103. Section 4 of the drawdown certificate states as follows: "(a) The proceeds of the Subject Borrowing shall be used for the purposes set forth on Schedule 1 attached hereto. Such use of proceeds is permitted under Section 7.9 of the Credit Agreement. (b) since the date of the Credit Agreement, no Material Adverse Effect has occurred."

Although Section 4(b) of the drawdown certificate appears to refer specifically to a material adverse effect with respect to the White Cliffs pipeline project, Ronan was arguably aware of a material adverse effect when he executed the drawdown certificate on July 11, 2008, that is, the potential sale of SemGroup's trading book and its worsening financial condition since the date of the loan.

As previously noted herein, Barclays required a $50 million deposit as a condition for its purchase of SemGroup's trading book. Funds from the July 11, 2008, drawdown were used to make the deposit in two $25 million increments. Barclays held the deposit for a number of days

and then returned it to SemGroup. Ronan alleged that it was permissible for SemCrude to upstream this money to SemGroup, if it demonstrated that it could complete the pipeline, which he believes it did.

However, GECC seemed to take a different view in a pleading it filed with the Bankruptcy Court. *See* Exhibit 104. In GECC's limited objection to the Debtors' Emergency Motion for Authorization to Obtain Postpetition Financing, it stated the following: "in the midst of the liquidity crisis that led to the commencement of the Debtors' chapter 11 cases, SemCrude Pipeline, LLC borrowed approximately $54 million on the GECC Loan and, on information and belief, promptly upstreamed $50 million of this money to its parent rather than using the cash to continue construction of the Pipeline." According to Sections 2.8, 7.9 and 8.5 of the GECC Loan, the loan only permits SemCrude to upstream the money to SemGroup only if the following conditions were met: (1) the distribution must be "in return of paid-in cash capital contributions to [SemCrude] in an amount not to exceed $120,000,000 in the aggregate on or after" the closing of the loan; (2) there must not be a default under the loan at the time of the transfer; and (3) SemCrude did not have a "Consolidated Leverage Ratio" (as defined in the loan) greater than 4.5 to 1.0.

When SemCrude defaulted on the Pre-Petition Credit Agreement on approximately July 16, 2008, it constituted a default of the GECC Loan. On July 17, 2008, GECC exercised its rights upon default, replaced SemCrude Pipeline as the manager of the White Cliffs project, and installed PE Pipeline Services, LLC ("PE Pipeline") as its manager.

When SemCrude Pipeline refused to recognize GECC's appointed manager on July 21, 2008, GECC filed an injunction and a request for declaratory judgment in the Delaware Court of

Chancery. On July 23, 2008, GECC and PE Pipeline commenced an adversary proceeding in the Bankruptcy Court. *See* Exhibit 105.

GECC claims that it is owed a total of $308.8 million by SemGroup.

a) References Made to GECC Loan by SemGroup Employees

Ronan stated that the GECC Loan was based on a need to continue to fund construction of the pipeline, to carry Noble Energy and Anadarko product from Colorado to Oklahoma. Ronan approached GECC for the $120 million loan. SemGroup was in the process of building the pipeline, which was called the White Cliffs Pipe Line Company. SemGroup had already spent over $100 million on the project, and it was ultimately expected to cost approximately $220 to $240 million to complete. Upon receipt of the GECC Loan, Ronan stated that approximately $50 million of it was moved into a separate account to protect it for use on the pipeline project. Barclays wanted a $50 million deposit as a condition for its purchase of SemGroup's trading book. This protected money was used to make the deposit, in two $25 million increments. According to Ronan, Barclays held the deposit for approximately one week and then returned it, where it was used for its original intent.

Stallings stated that Ronan was the main person on this loan. According to Stallings, the purpose of the loan was to continue to finance White Cliffs which was under construction. The GECC Loan was for $60 million, plus a revolving credit line of another $60 million. According to Stallings, some of the initial $60 million was forwarded to SemGroup as a project cost and applied to its margin costs.

Foxx also stated that Ronan put this deal together, and that it was designed to complete the construction of the 580-mile White Cliffs pipeline, from Colorado to Oklahoma. SemGroup had already invested approximately $120 million dollars in the project and needed approximately $120 million more to complete it. This was viewed as a solid investment by SemGroup, since it had a five-year commitment from Noble Energy and Anadarko Petroleum to transport its product from the Julesburg Basin in Colorado to Cushing, Oklahoma. Foxx, Schwiering and others from Foxx's operations group worked on the details of the pipeline. Foxx did not know if all of the proceeds from the loan were dedicated to build the pipeline.

Brochetti stated that he had no involvement in this transaction, and that Ronan was the one who put it together. According to Brochetti, the purpose of the loan was to allow SemCrude to complete the construction of White Cliffs pipeline project from Colorado to Oklahoma. Also according to Brochetti, half of the $120 million went to SemGroup, which already had $150 million invested in the project. The remaining $60 million was to be used to complete the White Cliffs project. However, it was Brochetti's understanding that $50 million of it was borrowed by SemGroup, because it needed to post $50 million to Barclays as a condition for novating its trading book. Brochetti thought that the $50 million was posted by SemGroup for only one day and was immediately returned to it, but he was not sure about that. He also thought it possible that the $50 million could have been posted to Barclays, but never physically transferred. He stated that the conditions of the loan allowed SemCrude to pay SemGroup the $60 million as a reimbursement for SemGroup's initial investment in the White Cliffs project.

5. Fortis Capital Corporation

In July 2004 Fortis Capital Corporation ("FCC") joined the SemGroup bank loan syndicate, led by BOA. FCC was a lender under the Pre-Petition Credit Agreement. In early October 2006, FCC completed its acquisition of Cinergy Marketing and Trading and Cinergy Canada, Inc., from Duke Energy, renamed Fortis Energy Marketing & Trading ("FEMT").

On September 29, 2006, FCC and others entered into a credit facility agreement with SemEuro for $575 million.

On September 20, 2007, SemCanada and FCC entered into an ISDA 2002 Master Agreement (*see* Exhibit 106), allowing SemCanada to trade with FCC with no initial or maintenance margin requirements, and freeing up liquidity for the benefit of SemCanada and SemGroup companies as a whole. SemCanada and FCC commenced trading under the ISDA Agreement on September 25, 2007, buying and selling gas swaps.

In or about March 2007, FCC, through its loan syndicate contacts in Dallas, introduced FEMT to SemGroup. On October 1 and 2, 2007, FEMT assumed SemCanada's existing gas swap positions on the NYMEX and Intercontinental Exchange ("ICE") in consideration of 1) SemCanada's purchase of substantially identical gas swaps from FCC and 2) SemCanada's payment of a $2.84 million fee to FCC.

SemCanada was required to maintain a base margin with NYMEX to cover one to two days' worth of anticipated market movement and an additional variation margin to cover any exposure resulting from SemCanada's out-of-the-money positions. The assumption by FEMT of SemCanada's gas swap positions on the NYMEX and ICE freed up an estimated $70 million in

cash or other collateral and $150 million in letters of credit that SemCanada had posted with NYMEX and ICE. SemCanada covered the NYMEX and/or ICE margins with draws on a $150 million letter of credit.

SemCanada's letter of credit had as underlying security a first priority lien on substantially all of SemCanada's assets. As a result, SemCanada gained the use of approximately $43 million that had been required as additional collateral with NYMEX and/or ICE.

By the end of February 2008, trading activity between SemCanada and FEMT began to slow and, by late April 2008, SemCanada was substantially "in-the-money" (approximately $250 million) on its positions with FEMT. In May 2008, SemGroup sought to take advantage of this positive position by having SemCanada trade in crude oil derivatives.

SemCrude began trading oil through SemCanada. On May 22, 2008, pursuant to a novation agreement with SemGroup, SemCanada assumed a large "out-of-the-money" position (approximately $55 million) from SemGroup, which had been at J. Aron (SemGroup's liability to J. Aron under a financial crude oil call, which SemGroup initially sold on February 13, 2008). *See* Exhibit 107.

FEMT then assumed the position from SemCanada pursuant to a second novation agreement with it, in return for a $360,000 fee paid to FEMT by SemCanada. According to financial records, SemCrude may have reimbursed SemCanada the $360,000 fee on or about June 9, 2008.

For the most part, the transactions in crude oil derivatives between SemCanada and FEMT consisted of SemCanada's selling financial crude oil puts and calls. On several occasions, SemCanada rolled forward a financial crude oil put or call position by purchasing a parallel put or call and selling a new financial crude oil put or call. In the aggregate, FEMT paid SemCanada $172.3 million in net option premiums.

During the course of the transactions between SemCanada and FCC/FEMT, SemCanada was paid an aggregate of $240,947,917 in initial transaction value, consisting of the sum of 1) $12,805,382 in liabilities of SemCanada to the NYMEX and ICE exchanges, assumed by FEMT on October 1 and 2, 2007; 2) the $55,842,535 liability of SemCanada to J. Aron, assumed by FEMT on May 23, 2008; and 3) $172,300,000 in net option premiums paid by FCC/FEMT to SemCanada.

Trading by SemCrude through SemCanada continued through July 15, 2008, when FCC was notified of the Company's impending financial problems during a bank group conference call. FCC had no knowledge of the Company's financial issues before the conference call. SemGroup's MtM and Position Reports, issued in accordance with the terms of the Pre-Petition Credit Agreement, all certified that the Company was in compliance with the trading covenants under the Pre-Petition Credit Agreement. According to FCC's attorneys, SemCrude delivered its last MtM and Position Report to the bank group on July 13, just two days before the conference call.

On July 16, 2008, BOA sent its notice of default under the Pre-Petition Credit Agreement to SemGroup. On July 17, 2008, FCC sent its designation of early termination of the ISDA

swaps to SemCanada. The basis for its early termination was BOA's notice of default. On July 18, 2008, FCC began liquidating its positions.

It was unclear to FCC where the cash SemCanada received from the execution of the puts/calls went, how transactions by SemCanada for SemCrude's behalf were booked or accounted for internally by SemGroup, and who bore pricing and credit risks in swaps by SemCanada on SemCrude's behalf.

It is FCC's position that it is owed, on a net basis, approximately $225,426,990 in FCC swap contracts, and that the obligations of SemGroup constitute Lender Swap Obligations. In total, as of November 22, 2008, FCC claimed that it was owed approximately $304,996,990 under the Pre-Petition Credit Agreement.

a) References Made to Fortis Transactions by SemGroup Employees

Brochetti stated that FCC had the same trading relationship with SemGroup as BOK. SemGroup had an OTC line of credit of approximately $225 million from FCC through the BOA credit facility. Brochetti thought that the amount FCC claimed it was owed was probably accurate and caused by SemGroup's MtM adjustments for its Canadian positions.

Coen stated that in the last few months before SemGroup's bankruptcy filing, SemCanada executed transactions with FCC on behalf of SemCrude. He stated that this was done because SemCrude had large negative MtM positions and margin on its NYMEX trading book, and SemCanada had a large positive MtM position with FCC. Coen indicated that SemCrude wanted to make use of the available FCC trade credit and that SemCrude was essentially trying to reduce its margin requirements by moving its large negative NYMEX MtM

position over to FCC. Coen stated that the decision to make use of SemCanada's trade credit was a group decision. Coen agreed that this activity could be described as SemCanada providing a credit "sleeve" for SemCrude.

C. GS TruE

In July 2007, a representative of Goldman joined what he referred to as the "Coverage Team" for SemGroup within Goldman. He advised that he was familiar with SemGroup and had previously advised it on some acquisitions. Discussions began between Goldman and SemGroup about ways to raise capital for the company. In approximately December 2007, and as previously referenced herein, Goldman proposed a private equity offering to SemGroup, called a 144A offering. A team from Goldman traveled to Tulsa on January 16, 2008, to meet with SemGroup personnel and its counsel. Wallace was the main point of contact with SemGroup, but the Goldman team also met with Kivisto occasionally. The original target date for the offering was for sometime in the mid-second quarter of 2008.

SemGroup's positive qualities included its health and safety records and its operational procedures. It appeared to be a profitable and well run company. Goldman's major concern was whether or not it was ready to become a public company, which required SemGroup's financials to meet certain reporting and disclosure requirements.

Baker Botts was responsible for preparing the prospectus for the GS TruE offering, with Goldman acting in an advisory capacity.

1. SemGroup Employee Comments Regarding GS TruE

Foxx stated that the idea for GS TruE came about in November 2007, after Wallace identified a couple of high-end gas business prospects ($1 billion plus) for SemGroup to purchase, and approached Goldman to help attain financing for them. Goldman did a presentation to SemGroup whereby it would sell 30% of the company via a private 144A stock offering, to raise the cash it needed for the prospective gas businesses. Foxx stated that he was hardly involved in the early stages of the negotiations. However, he later became more active in the negotiations.

As negotiations intensified in the May-June 2008 timeframe, Foxx went to New York for discussions with potential investors. He recalled that Merrill Lynch was also present as an underwriter. Wallace was present to explain the financial implications of SemGroup's stock offering, and Kivisto was there to explain the "global view" of it. Stallings also attended the meeting. Foxx recalled that Goldman had approximately ten representatives at the meeting.

Foxx remembered that Kivisto had been questioned extensively by SemGroup's officers on how he was going to explain SemGroup's $1 billion in unrealized MtM losses. However, in the long run, Kivisto seemed to be able to satisfy the attendees at the meeting, and SemGroup received the "green light" to proceed with its pursuit of the stock offering. Kuwait Oil Company came on board with a pledge of $500 million of the total $1.5 billion stock offering, with the stipulation that SemGroup maintain a certain stock price, which Foxx believed to be $100 per share. The capital raised in the proposed stock offering was specifically earmarked for SemGroup to purchase assets to grow its business, and SemGroup's executives were very excited about what the stock offering would do for its business. Foxx claimed that, around July 2008,

Goldman became leery of the current market as well as SemGroup's liquidity issues and decided not to go forward with the offering, which was suspended to await more favorable conditions.

Stallings stated that SemGroup had worked on the GS TruE financing package from January 2008 to July 2008, and there had been a tentative agreement with Kuwait Oil for $500 million, as part of the total GS TruE $1.5 billion package. Stallings stated that he went on vacation on July 4, 2008 and returned on July 7. He stated that the GS TruE financing broke down a few days later because of Goldman's liquidity concerns. He stated that Kivisto spent the next week attempting to find a counterparty to take Goldman's place.

Brochetti stated that he was not involved in this project, except to make a presentation regarding SGLP to Goldman. It was his understanding that the purpose of the offering was to raise capital for SemGroup to pursue potential future acquisitions. This transaction would be a private stock offering to qualified institutional investors, and the stock would have a quoted price on Bloomberg. The deal seemed to be going well, as SemGroup reportedly had a commitment from Kuwait Oil to invest $500 million. Brochetti was not sure why, but the deal ultimately collapsed.

Hill described GS TruE as a deal being worked out with Goldman, who had investors who were interested in SemGroup. He stated that he worked with Goldman's accountants and attorneys from Baker Botts on how to set up the best tax structure for the transaction. Among the questions SemGroup had was whether a corporation or a partnership should own the new entity. In order to determine the best option, Goldman provided certain data to SemGroup. However, the transaction never came to fruition, and was canceled shortly before SemGroup filed for bankruptcy protection.

2. Goldman's Concerns Regarding the Proposed Offering

As SemGroup's trading losses were approaching $2 billion and its margin calls were devouring its capital, Goldman began to wonder exactly what SemGroup was doing regarding its hedge fund trading, and whether it really was operating a matched book.

Goldman began to realize that the GS TruE offering was not going to occur before September 2008, if at all, because it would be impossible to market a company like SemGroup with so many significant issues. In late June 2008, Goldman requested that Kivisto turn over the company's trading book to it for analysis.

Goldman advised that two events, which occurred within 48 hours or each other, convinced it not to do any more business with SemGroup. First, Kivisto called Goldman and advised it that the company's credit line was low and that he had decided to sell one third to one half of SemGroup's trading book. Kivisto did not reveal a possible buyer. Next, Goldman completed its analysis of SemGroup's trading book, which revealed that SemGroup was short 18 million barrels of crude assets. This convinced Goldman that SemGroup was not hedging based upon physical inventory.

In early July 2008, Goldman advised SemGroup that it was discontinuing their business relationship.

Goldman's understanding of SemGroup's risk management had been based upon the belief that SemGroup utilized hedge trading to protect its assets.

3. Misrepresentations by SemGroup

It is Goldman's opinion that Kivisto believed that he could use SemGroup's storage capability to overcome his short positions while trading. Investors wanted a matched book and Goldman concluded that SemGroup's trading strategy was more than hedging.

Goldman became disappointed in Kivisto and Wallace, believing they were not forthright in their representations about SemGroup's financial troubles. Goldman stated that it had to find out about SemGroup's financial difficulties through its own due diligence.

Goldman did not suffer any financial losses related to the GS TruE project, other than its time and expenses. There is no pending litigation between Goldman and SemGroup related to the GS TruE issue.

4. MC Comments regarding GS TruE

(a) Thane Ritchie

Ritchie stated that in December 2007, when SemGroup was considering an IPO, he introduced Kivisto to representatives of Goldman. In early January 2008, Ritchie traveled to SemGroup's Tulsa office, where SemGroup did a presentation on the company's value for Goldman representatives, in order to secure its backing for the IPO.

A subsequent "pricing" meeting took place in approximately March 2008, at Goldman's offices in New York. SemGroup gave a pre-IPO presentation, at which time Kivisto stated that SemGroup would go to the Middle East to raise capital. A few weeks after the New York meeting, Wallace spoke with Ritchie and stated that it would be a great idea for Goldman to bring about $300 million dollars into SemGroup as a bridge loan for the IPO. Ritchie thought

that Goldman would be willing to provide the bridge loan and suggested approaching it about the loan. Goldman, however, did not want to make the loan, and suggested that SemGroup should look elsewhere.

Ritchie put Wallace in touch with Deutsche Bank, and then discontinued his involvement with the bridge loan. Despite occasional reports of delays, SemGroup told Ritchie over the next few weeks that the GS TruE project was on track. In approximately June 2008, Wallace sent Ritchie an e-mail, stating that he was traveling to Kuwait. Wallace made the trip and later informed Ritchie that the Kuwaitis were ready to invest $500 million into SemGroup, at $125 per share. Lehman completed its due diligence for the Kuwaitis in approximately May 2008, and Goldman had already done its own due diligence.

Shortly after June 30, 2008, with oil prices very volatile, Kivisto was still telling Ritchie that the IPO would happen, but that SemGroup just needed to cover the swings in oil prices. Ritchie stated that after the Manchester/Alerian loan for $150 million came through, he asked Kivisto how much more money was needed. Kivisto replied that another $150 million was needed. Ritchie responded that his firm needed full transparency from SemGroup regarding its MtM positions in oil, and asked for a presentation from Wallace. On approximately July 9, 2008, SemGroup sent him a report that provided a "snapshot" of about 10-20% of SemGroup's positions. Ritchie attended a general presentation by Wallace on July 10, 2008, at which time he (Wallace) stated that the increase in the volatility of oil prices and the restrictive credit market would force SemGroup to allow the Kuwaitis to invest at a lower price. Wallace was supposed to give a presentation on the trading positions the next day, but Kivisto left for New York to close the deal on the sale of SemGroup's trading book to Barclays, and the presentation was not

given. Ritchie believed that GS TruE was not canceled, but that it just "drifted away" when SemGroup's liquidity crisis hit in July.

(b) Andrew Ward

Ward stated that SemGroup began to consider taking SemGroup public with Goldman, which had conducted extensive due diligence. However, no one from Goldman communicated any issues or concerns regarding SemGroup to the MC. Goldman told Riverstone that it could expect valuations of ten times Riverstone's initial investment in an IPO of SemGroup.

D. April 2008 Conference Call with Bondholders

Pursuant to a bondholder agreement, SemGroup was required to hold a conference call with its bondholders on a quarterly basis. One of those calls was made on or about April 1, 2008, and the banks were invited to join the call.

During the call Kivisto discussed the state of the market and indicated that he would place additional trades to reduce margin requirements. Stallings stated that the trades Kivisto would have added would have been consistent with his overall trading strategy, which Kivisto never divulged, except Kivisto stated during the call that he would employ "wings" as part of the strategy to reduce margins.

SemGroup also discussed the need to raise equity and mentioned the GS TruE initiative as one option that was being considered. Another option was to go back to the current unit holders, such as Riverstone and RCM, and request additional investments from them. According to Stallings, this option was considered because some investors had previously indicated an interest in increasing their investments in SemGroup, if given the chance.

E. SemGroup Bankers' Trips

A BOK representative advised that on a yearly basis, SemGroup provided two or three day all expenses paid trips to the Bahamas to entertain the bank executives with whom it did business. BOK participated in those trips and felt that they were beneficial from a business standpoint. According to BOK, SemGroup canceled the 2008 trip because "something came up."

Brochetti stated that the bankers' trips provided by SemGroup were designed to build relationships with its lenders in a one-on-one environment, where the lenders had direct access to senior management, particularly Kivisto and Wallace. There was no formal structure to the outings, and they were designed to create a casual atmosphere. According to Brochetti, there were four trips to the Bahamas, which he attended. Kivisto and Wallace went on all of them, as well as on two bank trips to Monte Carlo.

Jaeger stated that she was one of the individuals at SemGroup who was responsible for planning the trips. The people invited were frequently split into two groups, because there were not enough SemGroup representatives present to work with all of them. She stated that there were normally about 25 to 30 bankers on such trips, representing a number of different banks. The July 2008 trip was canceled shortly before everyone was scheduled to depart. Jaeger stated that she knew things were getting bad for SemGroup when the trip was cancelled, because the trip had already been paid for.

Ms. Elizabeth Barclay ("Barclay"), SemGroup's Presentation Coordinator, stated that one group of guests would attend the trips from Sunday through Wednesday, while the other group would attend from Thursday through Saturday. Barclay thought that some of the Tulsa bankers

may have been flown to the Bahamas on the company jet. Although she did not remember the names of individuals who were invited, some of the banks involved were BOA, BOK, FCC, F & M and Spirit.[18]

The only other SemGroup sponsored event referred to during the course of the Examiner's investigation was a trip to the Masters Golf Tournament.

F. SemGroup Bonuses

1. SemGroup Employee Comments

Foxx stated that bonuses were automatic for virtually every SemGroup employee until 2008. No bonuses were paid in 2008 except to Foxx's crude oil transport drivers, who received safety bonuses.

Foxx stated that each department head recommended bonuses but that Kivisto had the final decision regarding who received them, and the amounts of them. Foxx never had any of his recommendations questioned, although Wallace told him that one year Kivisto cut back on the recommended bonuses for SemMaterials.

Bonuses were calculated on 15% of a yearly profit goal of $100 million, and the money went into a pool. If the $100 million goal was not met, bonuses were adjusted accordingly. To

[18] In addition to being responsible for designing and mailing the invitations, her group would print the agendas, "save the date" reminders, name tags and luggage tags. The invitations for the Bahamas trips always included some item reminiscent of the Bahamas. For example, one year a sea shell was included in each of the invitations, another year a silk bird of paradise, and another year a pair of plastic pink flamingos. Although the agenda for a trip might have had some time set aside for meetings, it was mainly a social gathering that included, among other things, a golf outing. If the people invited chose to bring their spouses, the spouses' travel was not paid by SemGroup.

Foxx's knowledge, trades were not made to inflate bonuses. Executive bonuses were discretionary and decided upon by Kivisto.

Foxx was shown a printout that broke down executive bonuses and travel and expenses, for the period of July 22, 2007 through July 21, 2008. *See* Exhibits 84 and 108. It was pointed out to Foxx that Weakland received a bonus of over $8 million during that period. Foxx did not think that Weakland's bonus was unreasonable because, as a gasoline trader, he was consistently the top income producer for SemGroup.

Foxx did not consider any of the bonuses to be excessive, with the possible exception of those given to Oven and Coen. Since he did not think either of them had any trading experience, he was surprised to see that they had received bonuses of over $1 million and $2 million, respectively, in 2007. This was especially perplexing to him since Kivisto was essentially responsible for all of the trading.

A review of e-mails exchanged between Oven and Kivisto in 2001 and 2002 reveals that Oven had an intimate relationship with Kivisto while working at SemGroup as a consultant.

According to Brochetti, bonuses were paid every six months. Brochetti stated that virtually all company employees received a bonus, and that bonuses were not paid in 2008. Brochetti had no input into the decision making process as to who received a bonus or how they were calculated, but he assumed that bonuses had to be approved by Kivisto and Wallace.

Coen stated that he believed that Kivisto was solely responsible for determining his bonus. Coen did not know the criteria utilized to determine his bonus, and he did not receive a

bonus in 2008. He was unaware of any trades made to positively affect EBITDA which would have resulted in enhanced bonuses for executives.

Jaeger stated that Wallace and Kivisto were involved in determining bonus amounts. She also stated that Foxx was involved in determining bonus amounts for SemCrude personnel. She stated that she did not know how bonuses were calculated. She stated that she has seen large bonus amounts reported in the media and questioned some of the figures. She noted that bonuses were calculated to take into account the amount that would have to be paid by the employee in taxes, and that the tax amount was added to the bonus amount. She indicated that everyone received bonuses and that they were normally paid semi-annually, in May and December.

Ms. Janell Brown ("Brown"), SemGroup's Payroll Director, stated that one of the reasons she enjoyed working at SemGroup was because of the high salary and bonuses she received. The bonuses were normally given to all employees twice each year, although no bonuses were paid in June 2008, which was the next time bonuses were expected. Browne stated that her last bonus was for $45,000, and that bonuses were typically in the $25,000 to $30,000 range. According to Browne, Kivisto and Wallace decided on the amounts of all bonuses. In December 2007, Wallace told her that there had been a change in policy, and that the bonuses would have to be approved by SemGroup's Management Committee.

See Exhibit 109 for a graphic summary of how the timing of bonus payments, margin payments, credit facility payments, and drop-downs interacted to affect SemGroup's cash flows in 2008.

2. Employment Agreements

SemGroup's executive employment agreements allowed for the payment of executive bonuses from a pool of up to 10% of SemGroup's annual EBITDA, subject to MC approval.[19] *See* Exhibits 41A, 110 and 111.

3. Bartow Jones' Comments Regarding Bonuses

Jones began serving on SemGroup's Management Committee during the spring of 2007. Jones first became aware of the issue of SemGroup executive bonuses in early 2008, when he raised the issue. In Jones' experience from serving on other corporate boards, executive bonuses were typically dealt with at the end of a fiscal or calendar year, typically in December or January. The bonus issue was not raised during the January 2008 SemGroup MC meeting. Jones later raised the issue with fellow MC member Ritchie while they were in Tulsa, at the beginning of the Goldman due diligence inquiries. At the time, Ritchie told Jones that he was not aware of what SemGroup had done previously regarding its executive bonuses. Ritchie and Jones agreed that they should explore the possibility of creating a compensation committee to deal with executive bonuses. Jones suggested the idea to Kivisto, who stated that he liked it, but that he (Kivisto) should be a member of the Committee. However, Jones stated that such committees were usually comprised of board members, and that he believed it was inappropriate for the company CEO to be a member of the committee.

[19] Specifically, the agreements provide as follows: "The total amount of such discretionary Cash Bonus Pool is expected to equal up to 10% of the total actual SemGroup L.P. EBITDA as defined in Section 3.2(d); provided, however, that the Management Committee, in it sole discretion, shall determine the amount of such Cash Bonus Pool, to be paid to management, if any. The Executive shall be entitled to a share of such Bonus Pool, as determined by the Management Committee. The Management Committee may review the foregoing to refine such Cash Bonus Program taking into consideration financial performance and similar programs from other companies. . ." *See* Exhibits 41A, 110 and 111 at Section 4.2.

Jones stated that he familiarized himself with the employment contracts of SemGroup's executives. He felt that MC approval was necessary for the payment of bonuses. During this process, Jones requested the disclosure of SemGroup bonus payments to the highest paid employees for the previous three years.

A memorandum dated February 15, 2008 from Kivisto to Ritchie and Jones, entitled "Subject: Compensation Committee" attaches "Summary of Compensation for top 25 employees for years 2005, 2006, and 2007)," was obtained from SemGroup. *See* Exhibit 108. The attachments to that memorandum for 2005, 2006, and 2007 contained the following information for Kivisto, Foxx, and Wallace.

2005	Name	Salary	Bonus	Total
	Kevin Foxx	$250,000.08	$1,701,000	$1,951,000.08
	Greg Wallace	$280,000.08	$4,801,000	$5,081,000.08
	Tom Kivisto	$350,000	$11,201,000	$11,551,000
2006	Name	Salary	Bonus	Total
	Kevin Foxx	$250,000.08	$4,450,000	$4,700,000.08
	Greg Wallace	$311,875.08	$9,800,000	$10,111,875.08
	Tom Kivisto	350,000	$17,800,000	$18,150,000
2007	Name	Salary	Bonus	Total
	Kevin Foxx	$408,333.35	$4,500,000	$4,908,333.35
	Greg Wallace	$325,000.08	$10,500,000	$10,825,000.08
	Tom Kivisto	$350,000.16	$17,000,000	$17,350,000.16

It was noted that the names or bonus amounts for Oven and Coen did not appear on these lists. Kivisto failed to disclose the bonus payments of approximately $1.5 million to Oven and $2 million to Coen in 2007, although this information was specifically requested by Jones.

Jones determined that executive bonuses for 2007 were paid while he was a member of the MC and that his approval had not been requested. (He noted that no payments were made for

the second half of 2007 or for 2008.) Ritchie advised Jones that his approval had not been sought for previous bonus payments. Jones told Kivisto that no additional bonuses should be paid without MC approval.

Prior to the filing of the Debtors' bankruptcy petitions, Jones was not aware of a personal relationship between Kivisto and Oven. Although Jones was not aware of any requirement that non-executive bonuses be approved by the MC, he opined that the MC should have been consulted prior to the payment of a bonus of that magnitude, if a personal relationship existed between the person who approved the bonus (Kivisto) and the recipient of it (Oven).

G. SemGroup Expenses/Travel

Foxx was asked how his travel and expenses could be over $1 million in a single year (from July 2007 through July 2008). *See* Exhibit 84. He explained that many of SemCrude's expenses were charged to his credit card. He stated that he purchased four season tickets each for the Houston Astros baseball team, the Houston Rockets basketball team and the Houston Texans football team to distribute to clients. He estimated that the cost for the tickets was approximately $100,000. Because Foxx's position with the company required him to travel extensively between Tulsa and Houston, he decided to buy a six to eight percent interest in a private airplane. Although SemGroup reimbursed him for the cost of the trips, it did not reimburse him for the cost of his interest in the private plane. He felt the private plane was less expensive than him using a company plane for that purpose. He was unable to recall how much he expensed for his travel in the private plane or how it compared with the cost of public transportation. Foxx stated that he also paid for a SemGroup Christmas party, which would have cost approximately $25,000. The only other large expense item he could recall was a $100,000

membership to Southern Hills Country Club (Foxx is still a member). Foxx's expenses were approved by Wallace or Kivisto.

Brochetti stated that, as far as he knew, company jets were used exclusively for company business. With respect to executive expenses, he assumed that Kivisto would have been the approving official.

Ms. Cogie Fodge ("Fodge"), a SemGroup supervisor, was questioned about the expense payments made to SemGroup executives from July 2007 through July 2008. Specifically, she was questioned about the $1.293 million paid to Foxx and the $903,000 paid to Wallace. Fodge stated that Foxx's expenses were high because of his constant commuting to Tulsa and elsewhere from his home in Texas. She also stated that Wallace's expenses were partly attributable to Kivisto and anyone else who made business trips with them (especially trips to foreign countries), because Wallace's credit card was used for those lodging and meal expenses, etc.

Jaeger stated that she had seen Wallace's actual personal expense reports, and the annual total was approximately $40,000. In her opinion, the large amounts that were reported as personal expenses for Foxx and Wallace were misleading because it included business expenses charged to their credit cards.

Based upon the following e-mails, it appears that Kivisto utilized a SemGroup company plane to fly to Cancun, Mexico, to pick up his family and fly them home to Tulsa.

On December 21, 2007, Kivisto sent an e-mail to Ann Houchin entitled "Private return from Cancun friday 28th" which states, "Can you see if the hawker is available to pick us up at noon CST in cancun bringing 5 back to tulsa? TK." *See* Exhibit 112.

On December 26, 2007, Pens sent an e-mail to Kivisto, which stated that: "The pilots need Kelsey's friend's full name for the trip back on Friday. They wanted to know all of the passengers I gave them the following but I was not sure of Kelsey's friend's name. Tom Kivisto, Julie Kivisto, Lissa Kivisto, Blake Kivisto, Kelsey Kivisto, Kelsey's friend. Thanks! Sharon." *See* Exhibit 113.

A limousine service reservation for Hollinger was found in SemGroup's records. According to the reservation, Hollinger was scheduled to be picked up at the airport in Cancun on December 17, 2007, and transported to a Marriott Hotel in Cancun. *See* Exhibit 114.

H. Kivisto's Personal Financial Interests (in Addition to Westback)

1. D'Novo Lean Gourmet, L.L.C.

(a) SemGroup Employee Comments Regarding Lean Gourmet

Jaeger stated that Hollinger had been a successful real estate broker in Tulsa when she met Kivisto, and that it was strongly rumored that they had a close personal relationship. Jaeger stated that Hollinger left her real estate business and opened a food delivery service, and later the Lean Gourmet Restaurant. She stated that Hollinger was around the office a lot and was not popular with SemGroup's employees, because of her demeanor and her requests to them. Jaeger stated that Hollinger would use Kivisto's name and ask some of SemGroup's employees to perform work for her company. She eventually obtained office space on the 8th floor, just above SemGroup's offices.

Jaeger stated that Kivisto was an investor in Lean Gourmet and that he influenced investments for Lean Gourmet from Cooke, Wallace and perhaps others. She stated that

Hollinger might be living in housing provided by SemGroup because she heard Pens say that Hollinger was living in "corporate housing."

On one occasion, Jaeger stated that she approached Kivisto and told him that using SemGroup's personnel to work on his private businesses was hard on them, and that such work should not be performed at SemGroup. Jaeger stated that she became aware of several instances where employees had expressed concern about performing work for Hollinger. One of them was Barclay, who performed work in SemGroup's communications group.

Barclay told Jaeger that she had become burdened by requests to do advertisements, to create logos, etc. for Lean Gourmet. Jaeger knew that Barclay was working late at night to get her regular work done, as well as the additional work requested of her for Lean Gourmet, Kivisto's art galleries, etc. Jaeger stated that a similar situation existed with some of SemGroup's IT specialists. One of then, Ms. Jayme Bynum ("Bynum"), told her that the demands upon her time kept increasing, and that she was working virtually full time for Kivisto's private interests. Since Barclay, Bynum and others were unsure how to address this situation, Jaeger went to Wallace and asked him what she should do. Wallace told her to talk to Kivisto, which she did. Jaeger told Kivisto that he needed to find another way to perform the work that SemGroup's employees were doing for his private interests.

Bynum, SemGroup's Manager of IT services, stated that in approximately April 2007, Kivisto gave her department instructions that it was to support Hollinger (Lean Gourmet/D'Novo) as long as it did not negatively impact SemGroup. However, Ms. Bynum advised that she had a lean staff and that it was a strain on them to complete IT build-outs for Hollinger's office and her business locations. *See* Exhibit 115 (e-mail from Bynum to Pens and

Hollinger (Hollinger's e-mail address was "thecherokeerose@aol.com")). She stated that the project became large enough that she assigned Mr. Jeff Dukes in her department to act as a project manager for it, and as a "go between" between her and Hollinger.

In Spring 2008, she discussed the matter with her manager, Mr. Greg Johnson, and explained to him that Hollinger's project was taking away from her department's dedication to SemGroup operations. In June 2008, Johnson went to Jaeger, and mentioned Bynum's concerns. Jaeger told Johnson that Bynum's department should stop providing support to Hollinger in two weeks' time.

Ms. Bynum stated that on at least one occasion, she remembers Hollinger had three or four past-due invoices for computer equipment purchased from Dell under SemGroup's account.

Barclay advised that Lean Gourmet LLC was a company in which Kivisto had an ownership interest, which was managed by Hollinger. Kivisto asked Barclay to do some of the graphics work for Lean Gourmet, which she did. However, a lot of the work had to be put on the "back burner," as Barclay was heavily involved in getting ready for SGLP's public stock offering at the time. Hollinger eventually stopped asking for Barclay's help.

Barclay stated that she never complained about the extra work Kivisto gave to her. Although Kivisto never personally paid her for doing any of the things he asked her to do for his personal businesses, he gave her an extra bonus in 2006.

(b) Interview with Michael Cooke

Cooke stated that he served as the lawyer for Lean Gourmet and assisted in its formation. He also was one of the investors in Lean Gourmet. In April 2007, he invested $125,000 and

received a five percent share. He has not received a distribution from his investment to date. He stated that other investors included Kivisto, Foxx's wife, Wallace, and Michael Fusco ("Fusco"), a local restaurateur. Cooke stated that he did not know if Hollinger had an office within SemGroup's complex, although he saw her there on occasion.

(c) Comments from the MC

Jones, a member of SemGroup's MC, stated that he knew that SemGroup had a vendor relationship with Lean Gourmet, although he knew very little about it prior to SemGroup's bankruptcy filings. Jones advised that the MC should have been informed if Kivisto had a financial interest in the company or if he had a personal relationship with its owner. He stated that the MC was not so advised.

(d) Interview with Anna Hollinger

Hollinger, President of Lean Gourmet, stated that the company consists of a restaurant named D'Novo, a restaurant named LXI, a retail specialty grocery store named Gourmet Market, and a catering and home delivery service. They are all located across the street from where SemGroup and D'Novo are headquartered.

Hollinger stated that she first talked about her Lean Gourmet business concept with Kivisto in approximately November 2006. Records indicate that the company was incorporated in Oklahoma in April 2007. *See* Exhibit 116.

Hollinger stated that, in January 2007, she approached Mr. McCarthy ("McCarthy"), SemGroup's Human Resources Director, and Wallace with her plan to supply SemGroup with food for its employees. She stated that meals were being provided to SemGroup employees at

the time by another local restaurant. Shortly thereafter, Lean Gourmet began to cater breakfast meals for SemGroup employees.

Hollinger stated that she had a desk on the 7th floor of SemGroup's office, which she utilized for her Lean Gourmet business. According to Hollinger, Lean Gourmet began leasing office space on the 8th floor of SemGroup's office in October 2007.

Hollinger stated that the initial seed money ($1 million) for the company was raised from the following investors: Kivisto Enterprises owned 65%; Hollinger owned 10%; Foxx owned 5%; Wallace owned 5%; Cooke owned 5%; Fusco (a Tulsa restaurateur) owned 5%; Drew Flatt ("Flatt) (Lean Gourmet's chef) owned 2.5%; and Mark Howard ("Howard") (Lean Gourmet's operations manager) owned 2.5%. Hollinger stated that the owners invested amounts of money equal to their stock ownership percentages, *i.e.*, Kivisto Enterprises invested $650,000. *See* Exhibit 117 (check from Westback Purchasing Company LLC, dated December 14, 2007, signed by Kivisto, in the amount of $196,000).

Hollinger stated that her beginning salary from Lean Gourmet was $150,000 per year, which was increased in January 2008 to $175,000 per year. Hollinger stated that the SemGroup business generated approximately $16,000 per month in revenues for Lean Gourmet. She stated that Lean Gourmet did not show a profit in 2007 or 2008, and is currently owed $55,000 by SemGroup.

The schedule of payments prepared by Alix Partners immediately before the Debtors' bankruptcy filing includes an entry reflecting that SemGroup's payments to Lean Gourmet, for the period from July 22, 2007 to July 22, 2008, were $286,234. *See* Exhibit 84.

Lean Gourmet's first and only board meeting was held in April 2008, at which time it was determined that a capital call of $2.5 million was needed. As a result, Howard, Fusco, Flatt and Wallace relinquished their ownership shares. Cooke and Foxx maintained their 5% ownership interests, Sharon Pens purchased a 3% stake, Hollinger increased her stake to 20%, and Kivisto Enterprises increased its share to 67%. Hollinger's portion of the call was $139,000, which she paid off in June 2008.

Hollinger stated that SemGroup provided IT services to Lean Gourmet, and that McCarthy billed Lean Gourmet for them. She also stated that Bynum billed Lean Gourmet for the computers and other IT hardware that Lean Gourmet received. She noted that Lean Gourmet paid for the services and equipment it received from SemGroup and its employees. She stated that she was not aware if Kivisto ever authorized SemGroup to perform any services for Lean Gourmet.

Hollinger stated that whenever Lean Gourmet received invoices from SemGroup or others, they would be forwarded to Pens, Kivisto's Administrative Assistant. Pens would also routinely deposit SemGroup's payments to Lean Gourmet into Lean Gourmet's bank account. Pens had access to Lean Gourmet's bank account, and utilized a rubber stamp bearing Kivisto's signature.

Hollinger stated that at approximately the time that Lean Gourmet was formed, she used a SemGroup employee to perform some of its art design work. She stated that she saw a potential market for advertising services, and, in 2007, she and Kivisto began an advertising firm called Current C Creative. She stated that she owns 25% of Current C Creative and Kivisto Enterprises owns 75% of it, jointly through a company called Quote LLC.

Hollinger stated that she made one purchase and one sale of SGLP's stock. Her purchase came in approximately June 2007, when the company went public. She stated that she purchased approximately 7,500 shares at approximately $22 per share, for a total purchase price of $165,000. Hollinger stated that she thought it would be a good investment, since SemGroup had a good reputation and was growing very quickly.

Hollinger stated that she sold all 7,500 of her shares in SGLP, at a loss of $25,000, in July 2008, on the day the stock "tanked." Hollinger stated that she had no idea that SemGroup was in financial trouble at the time of her sale, and only learned about it afterwards from media reports. She stated that even though she spent a great deal of time with Kivisto prior to SemGroup's bankruptcy filing, he never mentioned to her that SemGroup was in trouble.

Hollinger stated that she received a call from Cooke not long after the Debtors' bankruptcy petitions were filed. She stated that Cooke told her that she was on a "list of people" that were suspected of having sold their SGLP stock inappropriately.

Hollinger stated that she has resided since Spring 2008 in a single family dwelling owned by Kivisto Enterprises. She stated that she pays no rent. Hollinger stated that she has had a personal relationship with Kivisto in addition to their business relationship. Hollinger also stated that she received a divorce from her former husband in January 2008.

With respect to her personal relationship with Kivisto, she stated that she flew on SemGroup's corporate jet a few times with him. She remembers flying to Chicago at least once to visit Kivisto's KN Gallery, and stated that Wallace and two individuals from the F&M Bank in Tulsa were also on that trip.

2. Art Galleries

Barclay stated that Kivisto opened KN Gallery, an art gallery in Chicago, in 2006 and closed it during the latter part of 2008. It was originally known as Mary Bell Gallery. She stated that much of the artwork displayed at SemGroup was purchased from Mary Bell Gallery. She also indicated that SemGroup's Corporate Communications department did a great deal of graphic work for Kivisto in the process of his opening KN Gallery. Among the items produced for Kivisto were the gallery's logo, opening advertisements, media kits, catalogs for the first exhibit, and follow up catalogs for subsequent shows.

Barclay stated that it was common knowledge that the work for KN Gallery was being performed on company time. Although Kivisto later hired a graphic designer for KN, Barclay had to do much of that person's work, because of the person's inexperience. Other than ordering business cards, Barclay did not perform work for the KN Gallery after Spring 2008. According to Barclay, other SemGroup employees who performed work for KN Gallery without reimbursement were Dornblaser and Ms. Natalie Lovenburg.

Barclay stated that Gallery KH was another art gallery in Chicago that Kivisto owned, and from which SemGroup may have purchased art work.

3. Purchases of Art by SemGroup

Kivisto purchased artwork for SemGroup from various sources, including his own art galleries. The Examiner was provided with a list of all art work that was on SemGroup's properties. *See* Exhibit 118. The eleven page list contains approximately four hundred items.

As of the date of this report, approximately thirty-five pieces of artwork are missing or unaccounted for by SemGroup.

According to Barclay, approximately five pieces of artwork were shipped from SemGroup the day before Kivisto was placed on administrative leave. Barclay believes that one of the pieces of artwork that Kivisto purchased on behalf of SemGroup was worth $40,000.[20]

Jones stated that the MC was not advised that SemGroup was purchasing artwork from entities in which Kivisto had a financial interest, and that such information should have been disclosed to the MC.

In addition to the aforementioned, Kivisto had an interest in various other entities, including but not limited to the following: the Kivisto Foundation; Project Single Parent; Gusto, L.L.C.; Ivory Energy, L.L.C.; Westback Holdings, L.L.C.; Kivisto Enterprises, L.L.C.; and, Ivory Transportation. Pens performed accounting work and other services for Kivisto's businesses.

VI. THE EXAMINER'S FINDINGS REGARDING WHETHER ANY DIRECTORS, OFFICERS, OR EMPLOYEES OF THE DEBTORS PARTICIPATED IN FRAUD, DISHONESTY, INCOMPETENCE, MISCONDUCT, MISMANAGEMENT, OR IRREGULARITY IN THE MANAGEMENT OF THE AFFAIRS OF THE DEBTORS

As a result of the examination and based upon the foregoing and the information contained in the Exhibits, the Examiner has determined the following:

[20] A portion of an e-mail string between Kivisto and Pens states as follows: We need to crate-up and get all the zaslonovs we own and floor 5 to Lissa for a KH show." Pens replied: "How about the ones on 7th flr?" Kivisto replied: "and we want to mail Lis our Zaslonov books in that box on the flr in my off." Pens replied: "I also had some Zaslonov books in the storage room." Kivisto replied: "Call me." *See* Exhibit 119. Price advised that Zaslonov was an artist and Lissa is the first name of Kivisto's daughter. Kivisto's daughter managed one of the art galleries in which Kivisto had a financial interest.

Kivisto engaged in a complex trading strategy that introduced increased risk to SemGroup at the time of an unprecedented rise in the price of oil. There were aspects of Kivisto's trading strategy that made it speculative and which ultimately led to the filing of the Debtors' bankruptcy petitions. Kivisto engaged in mismanagement in this regard.

Kivisto tightly controlled SemGroup's trading strategy. He was responsible for hiring Coen and Oven, and he recruited Shimonov, to assist him in implementing his options trading strategy, knowing that they had little or no prior commodities options trading experience, but could be trusted to do what he directed. Similarly, Allen was chosen as Risk Director, with no prior risk management experience. Kivisto engaged in mismanagement in this regard.

Wallace, Kivisto and Cooper failed to integrate properly the commodities trading function into SemGroup's financial controls, which subjected SemGroup to additional risk. They engaged in mismanagement in this regard.

As SemGroup's founders and business leaders from 2000 to 2008, Foxx, Wallace and Kivisto failed to develop a suitable risk management policy or integrate one into SemGroup's business controls. In addition, they failed to comply with the RMP that did exist. They engaged in mismanagement in this regard.

At various points in time, members of SemGroup's senior management team (Kivisto, Wallace, Cooper and Stallings) were aware that Kivisto was using SemGroup's funds and resources to engage in options trading activity on his own behalf (through Westback), and that such activity had the potential to expose, and did expose, SemGroup to increased risk, yet they failed to stop it. They engaged in mismanagement in this regard.

Kivisto, Wallace and Cooper engaged in mismanagement and misconduct, by allowing Kivisto to engage in physical commodities trades for SemGroup through Westback, for which Kivisto received additional compensation from SemGroup for activity that was within his normal scope of duties.

Kivisto engaged in misconduct, by concealing or attempting to conceal the full nature and extent of Westback's relationship with SemGroup from SemGroup's MC and others.

Kivisto engaged in mismanagement and misconduct, by using SemGroup's resources and its personnel to further his personal, business and financial interests, including Westback, KH Gallery, KN Art Gallery and D'Novo Lean Gourmet.

Cooper, and perhaps other SemGroup personnel, engaged in mismanagement and misconduct, by: (1) incorrectly categorizing SemGroup's commodities trading positions in the MtM and Position Reports submitted to SemGroup's lenders, which made the position reports for each affected category incorrect; (2) falsely claiming in MtM and Position Reports that SemGroup personnel had operated within the guidelines of SemGroup's RMP, when, in fact, SemGroup was in violation of its trading limits and its bank covenants on numerous occasions during the reporting periods; (3) submitting data in MtM and Position Reports which did not match the data contained in SemGroup's internal Summary Position and MtM spreadsheets; and (4) submitting at least one false BBR on July 11, 2008, which showed that SemGroup had in excess of $72 million of credit available as of July 7, 2008.

Kivisto engaged in misconduct and mismanagement, by engaging, or causing others to engage: (1) in "naked options" transactions; and (2) in transactions for his personal benefit,

through Westback, an entity he owned and controlled (an "Affiliate," as defined in SemGroup's Pre-Petition Credit agreements), all in violation of SemGroup's banking covenants.

Kivisto engaged in mismanagement, by placing, or causing to be placed, the results of his options trading strategy on the books of other SemGroup business units, including SemGas, SemFuel, SemMaterials, SemEuro and SemStream, thereby subjecting these entities to increased risk.

Kivisto and Wallace engaged in misconduct and mismanagement, by approving the semi-annual bonuses paid to themselves and other executives without MC approval, and by personally benefiting from their own decisions in this regard, in violation of their employment agreements.

Kivisto, Wallace, and Cooper provided inaccurate and misleading information to members of SemGroup's MC, that SemGroup's trading activity was supported by its physical inventory.

Kivisto, Wallace and Cooper provided false and misleading information to BOK representatives during their meetings and conversations with them about SemGroup's trading-related activities.

Wallace provided false and misleading information to representatives of J. Aron, by claiming that SemGroup's liquidity issues were exaggerated, and that it did not have similar trading exposure with other brokers.

Kivisto had a conflict of interest by authorizing substantial bonus payments to Oven (approximately $1.5 million in 2007), a trader he hired with no previous trading experience to

assist him in implementing his trading strategy, and someone with whom he had a close personal relationship.

Kivisto, Wallace and Foxx had conflicts of interest by permitting Hollinger, their outside business partner and a person with whom Kivisto had a close personal relationship, to engage in, and to reap the benefits of, a business relationship with SemGroup. They did so without notifying SemGroup's MC of their ownership interest in the vendor company, or of Kivisto's personal relationship with their co-owner, Hollinger.

Kivisto and Wallace breached the terms of their employment agreements by accepting semi-annual bonuses for themselves that had not been approved by the MC.

VII. THE EXAMINER'S FINDINGS REGARDING WHETHER THE DEBTORS' ESTATES HAVE CLAIMS OR CAUSES OF ACTION AGAINST CURRENT OR FORMER OFFICERS, DIRECTORS, OR EMPLOYEES OF THE DEBTORS ARISING FROM ANY SUCH PARTICIPATION

A. Theories of Potential Liability

The Examiner has summarized the basic elements which support the Examiner's conclusions with respect to certain potential causes of action that the Debtors' estates may have under Delaware and Oklahoma law against Kivisto, Wallace, Foxx, Cooper, and others, and leaves the task of preparing detailed legal analyses and arguments to the fiduciaries of the Debtors' estates to the extent such claims are pursued.

1. Negligence/Mismanagement

The elements of common law negligence as summarized by Oklahoma courts, are "(1) the existence of a duty on the part of the defendant to protect plaintiff from injury; (2) a violation

of that duty; and (3) injury proximately resulting therefrom." *Sloan v. Owen*, 579 P.2d 812, 814 (Okla. 1997); *Copeland v. Tela Corp.*, 996 P.2d 931, 933 (Okla. 1999). Delaware courts apply a similar standard. The party making an allegation of negligence must be able to describe the duty breached, the identity of the person who breached it, the nature of the breach and the injury which resulted. *Myer v. Dyer,* 542 A.2d 802, 805 (Del. Super., 1987). *Graham v. Kent-Sussex Indus., Inc.*, No. 03C-05-013, 2004 Del. Super. LEXIS 291, at *5 (Aug. 12, 2004). ("[I]n order to prevail in a negligence action, the [plaintiffs] must prove by a preponderance of the evidence that [the defendant's] action breached a duty of care in a way that proximately caused injury to [the plaintiffs].").

Ordinary negligence is not usually the standard for liability with respect to officers and directors of a corporation, however, since directors and officers are protected by the business judgment rule in most instances. As discussed below, the rule effects a gross negligence standard, at least under the law of Delaware. *Smith v. Van Gorkom*, 488 A.2d 858, 893 (Del. 1985); *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984). The ordinary negligence standard applies only when the business judgment rule is unavailable, such as when a self-dealing transaction is not approved by the disinterested directors or shareholders, when liability is asserted for the failure to make a decision, or when germane information is omitted when soliciting shareholder approval. *See Aronson*, 473 A.2d at 813; *In re Anderson, Clayton S'holder. Litig.*, 519 A.2d 694 (Del. Ch. 1986).

Mismanagement is an umbrella term, rather than a cause of action, which refers to a range of wrongful corporate acts that result in harm to a corporation or its shareholders, which acts generally do not rise to the level of fraud, conversion, or intentional breaches of fiduciary duties. *See*, *e.g.*, *Porter v. Rott*, 243 P. 160, 164 (Okla. 1926) ("The officers of a corporation act

in a fiduciary capacity in respect to its property in their hands, and may be called to an account for fraud or sometimes even mere mismanagement in respect thereto."); *Exch. Bank v. Bailey*, 116 P. 812, 815 (Okla. 1911) (justifying equitable relief from wrongful actions of bank officers where "if such acts do not constitute fraud, they at least constitute . . . gross mismanagement"). *See also Santa Fe Indus., Inc. v. Green*, 430 U.S. 462 (1977); *Bangor Punta Operations, Inc.* v. *Bangor & A.R. Co.*, 417 U.S. 703 (1974).

2. Fraud/False Statements

A "false statement" is generally an element of a variety of causes of action including deceit, defamation and libel and fraud. Under Oklahoma law, in order to establish actionable fraud, the plaintiff must prove (1) a false (2) material misrepresentation (3) made with knowledge that it is false, or made as a positive assertion without knowledge of whether it is true or false and (4) made with the intent to induce action in another (5) which does in fact induce such action, and (6) proximately causes injury or damage to another. *D & H Co. v. Shultz*, 579 P.2d 821, 824 (Okla. 1978). "The liability for misrepresentation depends upon whether the person relying thereon was in fact deceived, not upon whether an ordinarily prudent person should have been misled." *Evans v. Bridgestone-Firestone, Inc.*, 904 P.2d 156, 157-58 (Okla. Civ. App. 1995) (citations omitted).

The elements of fraud under Delaware law are similar. A party claiming fraud must allege: (1) a false representation, usually one of fact, made by the defendant; (2) the defendant's knowledge or belief that the representation was false, or was made with reckless indifference to the truth; (3) an intent to induce the plaintiff to act or to refrain from acting; (4) the plaintiff's action or inaction taken in justifiable reliance upon the representation; and (5) damage to the

plaintiff as a result of such reliance. *Stephenson v. Capano Dev., Inc.*, Del. Super., 462 A.2d 1069, 1074 (1983).

Fraud is generally a contractual claim in Oklahoma, although Oklahoma tort law also provides that, "[o]ne who willfully deceives another, with intent to induce him to alter his position to his injury or risk, is liable for any damage which he thereby suffers." 76 Okla. Stat. § 2. Deceit, is defined as either: (1) the suggestion, as a fact, of that which is not true by one who does not believe it to be true; (2) the assertion, as a fact, of that which is not true, by one who has no reasonable ground for believing it to be true; (3) the suppression of a fact by one who is bound to disclose it, or who gives information of other facts which are likely to mislead for want of communication of that fact; or (4) a promise, made without any intention of performing. 76 Okla. Stat. § 3.

3. Conversion/Corporate Waste

Delaware and Oklahoma have similar elements for conversion. In Delaware, "conversion" is the act of dominion wrongfully exerted over the property of another, in denial of his right, or inconsistent with it. *McGowan v. Ferro*, 859 A.2d 1012, 1040 (Del. Ch. 2004), *aff'd*, 873 A.2d 1099 (Del. 2005). Under Oklahoma law, "conversion" is any act of dominion wrongfully exercised over another's personal property inconsistent with his rights therein. *Stroud Nat'l Bank v. Owens*, 134 P.3d 870, 876 (Okla. Civ. App. 2006).

In Delaware, a claim of corporate waste requires a determination of whether the corporation has bestowed an asset upon another in exchange for something so inadequate in value that no person of ordinary, sound business judgment would deem it worth that which the corporation has paid. *See Grobow v. Perot*, 539 A.2d 180, 189 (Del. 1988). This strict standard

requires a court to apply a reasonable person standard and deny a claim of corporate waste wherever a reasonable person might deem the consideration received adequate. A transaction will be only deemed a corporate waste when the consideration received for corporate assets is "so disproportionately small as to lie beyond the range at which a reasonable person might be willing to trade." *Lewis v. Vogelstein*, 699 A.2d 327, 336 (Del. Ch. 1997).

A claim for corporate waste under Oklahoma law is tied to a breach of fiduciary duty and the failure of an officer or director in the exercise of their business judgment, which are discussed below.

4. Unjust Enrichment

Under Delaware law, unjust enrichment is the unjust retention of a benefit to the loss of another, or the retention of money or property of another against the fundamental principles of justice or equity and good conscience. *Braintree Labs., Inc. v. Schwarz Pharma, Inc.*, 568 F. Supp. 2d 487, 499 (D. Del. 2008). The elements for unjust enrichment are: (1) an enrichment; (2) an impoverishment; (3) a relation between the enrichment and the impoverishment; (4) the absence of justification; and (5) the absence of a remedy provided by law. *Jackson Nat'l Life. Ins. Co. v. Kennedy*, 741 A.2d 377, 393 (Del. Ch. Ct. 1999).

> Similarly, under Oklahoma law, courts have found, "[A] right of recovery under the doctrine of unjust enrichment is essentially equitable, its basis being that in a given situation it is contrary to equity and good conscience for one to retain a benefit which has come to him at the expense of another . . . . [It] arises not only where an expenditure by one person adds to the property of another, but also where the expenditure saves the other from expense or loss. *N.C. Corff P'ship, Ltd. v. Oxy USA, Inc.*, 929 P.2d 288, 295 (Okla. Civ. App. 1996). To recover for unjust enrichment, "there must be enrichment to another coupled with a resulting injustice." *Teel v. Pub. Serv. Co. of Okla.*, 767 P.2d 391, 398 (Okla. 1985); *Burlington N. & Santa Fe Ry. Co. v. Grant*, 505 F.3d 1013, 1030 (10th Cir. 2007).

5. Breaches of Fiduciary Duties

"The directors of Delaware corporations have a triad of primary fiduciary duties: due care, loyalty, and good faith. Those fiduciary responsibilities do not operate intermittently." *Emerald Partners v. Berlin*, 787 A.2d 85, 90 (2001), *aff'd*, 840 A.2d 641 (Del. 2003). "With respect to the obligation of officers to their own corporation and its stockholders, there is nothing in any Delaware case that suggests that the fiduciary duty owed by officers is different in the slightest from that owed by directors." *In re Walt Disney Co.*, No. Civ. A. 15452 2004 WL 2050138, n.32 (Del. Ch. Sept. 10, 2004).

In order to satisfy the duty of care, before making a business decision, directors must inform themselves of "all material information reasonably available to them." *Paramount Commc'ns Inc. v. QVC Network Inc.*, 637 A.2d 34, 44 (Del. 1994) (citation omitted). Additionally, the directors must "use that amount of care which ordinarily careful and prudent men would use in similar circumstances." *Bridgeport Holdings Inc. Liquidating Trust v. Bayer (In re Bridgeport Holdings, Inc.)*, 388 B.R. 548, 568 (Bankr. D. Del. 2008). Director liability for a breach of the duty of care is predicated upon the concept of gross negligence. *McMullin v. Beran*, 765 A.2d 910, 921 (Del. 2000).

The duty of loyalty refers to the duty that directors owe to a corporation not to put their personal financial interests above the interests of the corporation. *Brandt v. Hicks, Musc & Co. (In re Healthco Int'l, Inc.)*, 208 B.R. 288, 302 (Bankr. D. Mass. 1997). A dispute over the breach of the duty of loyalty often arises when a director has a personal interest in a corporate transaction. *Id.* However, a claim for breach of loyalty "may be premised upon the failure of a fiduciary to act in good faith" even where the fiduciary did not act out of self interest or lacked

independence. *In re Bridgeport Holdings Inc.*, 388 B.R. at 564. Directors may also breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith when they fail to act in the face of a known duty to act. *Id.* at 577. Delaware courts have long linked the definition of a director's duty of good faith with the duty of loyalty. *See Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939). In examining the duty to act in good faith, a court may "review the substance of a business decision made by an apparently well-motivated board for the limited purpose of determining whether that decision is so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith." *In re JP Stevens & Co. S'holders Litig.,* 542 A.2d 770, 780-81 (Del. Ch. 1988).

Notably, the entities involved in these cases are not corporations, but are instead primarily limited partnerships or limited liability companies organized under the laws of Oklahoma or Delaware. Accordingly, the fiduciary duties applicable in these cases may vary somewhat from the well-established standards applicable to officers and directors of corporations described above. In particular, Oklahoma and Delaware have statutorily established certain permissible limitations on liability.

The Delaware Limited Liability Company Act does not explicitly address the imposition of fiduciary duty or any other standard of conduct, although it does provide that, to the extent that, at law or in equity, a member or manager or other person has duties (including fiduciary duties) to a limited liability company or to another member or manager or to another person that is a party to or is otherwise bound by a limited liability company agreement, the member's or manager's or other person's duties may be expanded or restricted or eliminated by provisions in the limited liability company agreement; provided that the limited liability company agreement may not eliminate the implied contractual covenant of good faith and fair dealing." § 1101(c).

The statute also provides that a member's or manager's liability for breach of a fiduciary duty may be limited under a limited liability company agreement; provided that the agreement may not eliminate liability for any act or omission that constitutes a bad faith violation of the implied contractual covenant of good faith and fair dealing. § 1101(e). Similar provisions apply to Delaware limited partnerships. Delaware Revised Uniform Limited Partnership Act, § 1101(d), (f).

Under Oklahoma law, a partnership agreement may not eliminate the duty of loyalty (although the partnership agreement may identify specific types or categories of activities that do not violate the duty of loyalty, if not manifestly unreasonable; or all of the partners or a number or percentage specified in the partnership agreement may authorize or ratify, after full disclosure of all material facts, a specific act or transaction that otherwise would violate the duty of loyalty), unreasonably reduce the duty of care, or eliminate the obligation of good faith and fair dealing. 54 Okla. Stat., § 103. Managers of an Oklahoma limited liability company are subject to duties of good faith and fair dealing. The operating agreement or articles of organization of an Oklahoma limited liability company may not limit or eliminate the liability of a manager for any breach of the manager's duty of loyalty to the limited liability company or its members, acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, or any transaction from which the manager derived an improper personal benefit. 18 Okla. Stat. § 2017.

6. Breach of Contract

Under Oklahoma law, "[i]n order to recover on its breach of contract theory, a party needs to prove: 1) formation of a contract; 2) breach of the contract; and 3) damages as a direct

result of the breach." *Digital Design Group, Inc. v. Information Builders, Inc.*, 24 P.3d 834, 843 (Okla. 2001). Similarly, under Delaware law, "[t]o establish a prima facie case of breach of contract, the Plaintiff must prove three things. First, it must show that a contract existed. Second, it must establish that the Defendant breached an obligation imposed by the contract. Finally, it must prove that it suffered damages as a result of the Defendant's breach." *A&A Air Servs. v. Richardson*, 2006 Del. C.P. LEXIS 49, *7-8 (Del. C.P., June 17, 2006) (*quoting VLIW Tech., LLC v. Hewlett-Packard Co.*, 840 A.2d 606, *612 (Del. 2003)), *aff'd, Richardson v. A&A Air Servs.*, 2007 Del. Super. LEXIS 258 (Del. Super. Ct., July 31, 2007). A contract creates legal duties between the parties to that contract. A breach of contract may be committed by prevention or hindrance of one's party's obligations under the contract or through repudiation, the rejection by a party of its own obligations under the contract. *See Corbin on Contracts* § 53.944 (2008).

VIII. CONCLUSION

As described herein, based upon the information obtained during the course of the examination, the Examiner has determined that a number of potential causes of action may be available to the estates. These claims include, but are not limited to, actions against: (i) Kivisto, Wallace, Foxx, Cooper, and Stallings for negligence and mismanagement; (ii) Kivisto, Wallace and Cooper for fraud and false statements; (iii) Kivisto for conversion and corporate waste; (iv) Kivisto and Wallace for unjust enrichment; (v) Kivisto, Wallace and Cooper for breach of fiduciary duties; and (vi) Kivisto and Wallace for breach of contract. The Examiner has not performed a detailed analysis applying the elements of these causes of action to the facts of the Debtors' cases or otherwise evaluated the strength of any particular claims the estates may have.

Nor has the Examiner analyzed potential defenses that may be available with respect to these causes of action.

Dated: April 15, 2009
Wilmington, Delaware

Respectfully submitted,

/S/ Louis J. Freeh
Louis J. Freeh, Examiner