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State of New Jersey, Department of Treasury, Division of Investment, by Treasurer John E. McCormac, Plaintiff, -against- Qwest Communications International, Inc.; Philip F. Anschutz; Joseph P. Nacchio; Robin R. Szeliga; Robert S. Woodruff; Stephen M. Jacobsen; Drake S. Tempest; Marc B. Weisberg; James A. Smith; Lewis O. Wilks; Craig D. Slater; and Arthur Andersen LLP, Defendants.	SUPERIOR COURT OF NEW JERSEY LAW DIVISION -- MERCER COUNTY DOCKET NO. ________________ CIVIL ACTION COMPLAINT JURY TRIAL DEMANDED

Plaintiff State of New Jersey, Department of Treasury, Division of Investment, by Treasurer John E. McCormac ("Plaintiff" or "New Jersey"), as and for its Complaint against the defendants, alleges the following:

INTRODUCTION

1. Plaintiff New Jersey brings this action to recover the damages it incurred purchasing over 4 million shares of common stock issued by Qwest Communications International, Inc. ("Qwest" or the "Company") during the period November 2000 through November 2001 at prices artificially inflated by defendants' wrongful acts. The defendants, which include Qwest, its top officers and directors, and its former auditor, Arthur Andersen LLP, caused Qwest's stock to trade at artificially inflated prices by employing improper accounting practices, and by issuing false statements about Qwest's business, revenues and profits, all as alleged more fully below. As a result, New Jersey purchased its Qwest stock at prices as high as $54.40 per share. On and after September 22, 2002 the truth began to emerge and Qwest ultimately admitted to having committed accounting violations, and that it would restate nearly ***$1 billion*** in revenues it previously recognized. Qwest stock plummeted to just over $1.00 per share, causing New Jersey to incur tens of millions of dollars in losses. In September and October 2002, Qwest acknowledged its accounting fraud to the market by posting restatements of prior years' and quarters' revenues and earnings, and acknowledged that more restatements would be forthcoming.

JURISDICTION AND VENUE

2. This Court has subject matter jurisdiction over the claims set forth herein pursuant to R 4:3-1.

3. This Court has personal jurisdiction over the defendants pursuant to R 4:4-4. The defendants intentionally disseminated false and misleading statements concerning Qwest's financial statements, reports and its accounting and business practices in and to this State which were designed to sell securities in this State, and induced Plaintiff New Jersey to invest large sums of money from State pension funds in Qwest, and to refrain from selling those securities which could have mitigated New Jersey's losses. Relying upon the defendants' misrepresentations and omissions, Plaintiff New Jersey purchased and held substantial amounts of defendant Qwest's securities. As a direct result of the defendants' misconduct, Plaintiff New Jersey and its pension funds sustained substantial financial losses. In addition, jurisdiction is proper because the defendants transact business, own property and/or have committed acts within this State or outside this State that have cause foreseeable injury within New Jersey.

4. Venue is proper in this judicial district pursuant to R 4:3-2(a)(2) because the causes of action arose, in material part, in this County.

THE PARTIES

5. Plaintiff New Jersey is a political entity dedicated to serving the interests of its citizenry.

a. The Office of the State Treasurer is one of the oldest units of New Jersey state government. Under the direction of State Treasurer John E. McCormac, the

Department of the Treasury administers the State budget. The Treasury Department also performs at least three other major functions: revenue collection and generation, assets management, and statewide support services.

b. The Division of Investment is among the 50 largest public or private money managers in the United States. Pension funds constitute the bulk of the assets the Division manages, which represent the retirement plans for over 600,000 active and retired New Jersey employees. The remaining monies are managed in over 170 additional separate funds, such as the State's Deferred Compensation Plan in which more than 33,000 employees participate. The Division also manages various other funds such as the New Jersey Better Educational Savings Trust (NJBEST) college savings plan which encourages New Jersey families to save for college by providing incentives that include a federal tax deferral and a state tax exemption on investment earnings. The program also provides a scholarship to savers who meet minimum participation requirements and attend college in New Jersey.

c. The Division of Investment manages the investment portfolios of, among others, the following State pension funds: the Public Employees' Retirement System ("PERS"); the Teachers' Pension and Annuity Fund ("TPAF"); the Police and Firemen's Retirement System ("PFRS"); the State Police Retirement System ("SPRS"); and the Judicial Retirement System ("JRS").

d. The Division of Investment employs research analysts who assist Division personnel in developing investment strategies for the pension and other funds that are managed by the Division. The Division's research analysts are responsible for reviewing the regulatory filings, corporate reports, press releases and other documents disseminated by public

companies in order to make investment recommendations informed by those companies' public statements. The research analysts also routinely participate in conferences sponsored by securities firms and other entities. The Division's research analysts and other personnel rely and relied upon the accuracy, veracity and completeness of Qwest's public filings, quarterly and annual reports, corporate disclosures, announcements and other statements in making investment recommendations and decisions concerning the investment of the public pension and other public monies they manage in Qwest securities.

e. During the period November 2000 through November 2001, Plaintiff New Jersey purchased at least 4,053,000 shares of Qwest common stock for in excess of $147 million. A summary chart setting forth the dates, amounts and prices of Plaintiff New Jersey's purchases of Qwest stock is attached as Exhibit A.

6. Defendant Qwest provided telecommunications, wireless and directory services in at least 14 states located primarily in the western United States, and internet, broadband and related communications services nationally and internationally. In its Form 10-K annual report for the year 2000 filed with the Securities and Exchange Commission (the "SEC"), Qwest described itself as "a leading broadband Internet communications company that provides advanced communication services, data, multimedia and Internet-based services on a national and global basis; and wireless services, local telecommunications and related services and directory services in the 14 state local service area." Qwest is incorporated in Delaware, and maintains its principal executive office in Denver, Colorado. Qwest's common stock trades and has traded on the New York Stock Exchange ("NYSE") under the symbol "Q".

7. a. Defendant Philip F. Anschutz ("Anschutz") is Qwest's founder and controlling shareholder, and is a Director of the Company. Anschutz served as Qwest's Board Chairman since 1993. In addition, Anschutz has also been a Director and Chairman of the Board of Anschutz Company and involved with several other related entities, certain of which do business with Qwest. Among others, the entities Anschutz controlled include Anschutz Company, The Anschutz Corporation, and Anschutz Investment Company.

b. Defendant Joseph P. Nacchio ("Nacchio") served as Qwest's Chairman and CEO from April 1999 until he resigned those positions on June 17, 2002. During Nacchio's tenure, he served on the Board's Executive Committee. Nacchio has also served as the Chairman and as a Director of Qwest's affiliate, KPNQwest N.V. ("KPNQwest").

c. Defendant Robin R. Szeliga ("Szeliga") has been Qwest's Executive Vice President, Finance and Chief Financial Officer since April 2001. From October 1999 to March 2001, Szeliga was a Senior Vice President, Finance, and from March 2001 until April 2001, Qwest's Interim Chief Financial Officer. Szeliga is a certified public accountant.

d. Defendant Robert S. Woodruff ("Woodruff") became a Director and Executive Vice President, Finance, Chief Financial Officer, and Treasurer of Qwest in February 1997. Mr. Woodruff has also been a Director of KPNQwest and Qwest Cyber.Solutions LLC since 1999. Prior to joining Qwest, Woodruff had been a partner in the accounting firm Coopers & Lybrand, where his responsibilities included providing services to communications companies. Woodruff retired from Qwest in March 2001.

e. Defendant Stephen M. Jacobsen ("Jacobsen") became Qwest's Executive Vice President, Global Business Markets, in September 1998.

f. Defendant Drake S. Tempest ("Tempest") was Executive Vice President, General Counsel, Chief Administrative Officer and Corporate Secretary of Qwest. According to Qwest's Proxy Statement filed with the SEC on March 16, 2001, Tempest was "responsible for guiding legal policy, assuring compliance with legal requirements, and supervising our regulatory and legislative activities." In the wake of the Company's Restatement and admission to certain accounting "errors," Qwest announced on November 14, 2002 that Tempest will resign from the positions of General Counsel and Executive Vice President effective December 8, 2002.

g. Defendant Marc B. Weisberg ("Weisberg") was Qwest's Executive Vice President, Corporate Development, since October 2000, and before that was Senior Vice President since September 1997. Weisberg served as Executive Vice President until September 2001 and, in that role, oversaw Qwest's merger and acquisition activity and strategic alliances. In addition, Weisberg served as President and CEO of Qwest Investment Company, a wholly owned venture capital subsidiary of Qwest.

h. Defendant James A. Smith ("Smith") became Qwest's Executive Vice President, Small Business and Consumer Markets, in January 2001, and before that had been President of Dex, Qwest's directory services unit since June 2000.

i. Defendant Lewis O. Wilks ("Wilks") became Qwest's Executive Vice President, Internet Business Development, and Chief Strategy Officer in October 2000. Before that Wilks served as Qwest's President, Internet and Multimedia Markets, since 1998 and earlier as its President, Business Markets. The Proxy Statement Qwest filed with the SEC on March 16, 2001 noted that "Mr. Wilks has extensive senior-level management experience in

delivering communications services to the corporate sector." Wilks resigned from the Company in September 2001.

j. Defendant Craig D. Slater ("Slater") was a Director of Qwest, serving on the Board's Compensation Committee and Executive Committee. In addition, Slater is an officer of additional companies controlled by Anschutz, certain of which do business with Qwest. For example, Slater has been President of Anschutz Investment Company since August 1997; Executive Vice President of Anschutz Company and The Anschutz Corporation since August 1995; and held various other positions with these companies from 1988 through 1995.

8. a. The individuals named as defendants in 7(a)-(j) are referred to collectively as the "Individual Defendants".

b. The Individual Defendants participated in drafting, and in many cases signed, the reports and filings Qwest made with the SEC which the Complaint alleges are false and misleading. For instance, Individual Defendants Szeliga, Anschutz, Nacchio, and Slater signed Qwest's Forms 10-K for the years 2000 and 2001. Individual Defendant Woodruff signed various of the Company's Form 10-Q's, including the first three quarters of 2000. These and other Individual Defendants also signed or participated in drafting many other SEC filings and related documents for the Company.

c. Because of their positions with the Company, the Individual Defendants possessed the power and authority to control the content of Qwest's quarterly and annual reports and SEC filings, press releases and representations to securities analysts, money and portfolio managers, and institutional investors. Each of the Individual Defendants was timely provided with copies of the Company's reports and statements alleged to be misleading,

and each had the ability and opportunity to prevent their issuance or cause them to be corrected. Because of their positions and access to material non-public information, each of the Individual Defendants knew that the adverse facts alleged in this Complaint had not been disclosed to, and were in fact actually being concealed from, investors, and that the positive representations which were being made about Qwest's financial position and accounting practices were, at the time they were made, materially false and misleading. The Individual Defendants are also liable for the false statements alleged in this Complaint because those statements are "group-published" information and, thus, the result of the collective actions of all of the Individual Defendants.

d. In addition, each of the Individual Defendants engaged in substantial insider sales of Qwest common stock throughout the past few years. These insider stock sales served as a powerful motive for each of the Individual Defendants to engage in the violations alleged, and had the effect of enabling these Defendants to sell millions of Qwest shares at artificially inflated prices. For instance, defendant Anschutz sold over 33 million Qwest shares in mid-1999 for total proceeds of more than $1.5 billion. Subsequently, in April or May of 2001, Anschutz entered into two "forward contracts" related to the future delivery of 4.6 million of his Qwest shares -- in effect, a guarantee against Qwest stock dropping substantially in value -- for which he received an additional $179 million. In total over the past two or so years alone, Anschutz sold at least $408 million of his Qwest shares. Further, the other Individual Defendants also allegedly engaged in substantial insider sales of Qwest shares, as follows:

DEFENDANT	NO. OF SHARES SOLD	PROCEEDS	% OF HOLDINGS SOLD
Nacchio	4,983,467	$213,477,073	49%
Szeliga	10,000	$410,000	7%
Woodruff	1,155,000	$52,792,495	75%
Jacobsen	1,036,900	$49,566,197	83%
Tempest	466,600	$20,876,780	63%
Weisberg	793,750	$37,836,107	89%
Smith	281,826	$11,477,470	49%
Wilks	1,415,000	$65,163,770	98%
Slater	866,771	$38,403,875	90%
Total:	11,009,314	$490,003,766	62%

9. Defendant Arthur Andersen LLP ("Arthur Andersen") served as Qwest's independent public accountants and auditors until May 29, 2002, when it was replaced by KPMG LLP. Arthur Andersen issued an opinion certifying Qwest's 2000 year-end financial results, and consented to the inclusion of its opinion certifying those results in Qwest's Form 10-K for that year, filed on or about March 31, 2001. In addition, Arthur Andersen participated in and blessed Qwest's illicit swap transactions and the improper accounting practices alleged in this Complaint, and was a substantial participant in the violations alleged.

FACTUAL ALLEGATIONS

Background

10. After Qwest issued its initial public offering of common stock to investors in June 1997, the Company began to expand rapidly. The Company's expansion was fueled primarily by acquiring other companies, usually for Qwest stock rather than cash. For example,

in 1998 alone, Qwest acquired four other communications companies, including LCI, EUnet International, Phoenix Network and Icon CMT Corporation.

11. By June 1999, Qwest had embarked upon its largest merger proposal ever, offering to acquire U S West, Inc., a regional "Baby Bell" operating company, for some $60 billion in Qwest stock. Because of the size of the merger and the need for regulatory approval, Qwest did not complete this acquisition until June 2000. At that time, each outstanding share of U S West common stock was converted into the right to receive 1.72932 shares of Qwest common stock (and cash in lieu of fractional shares). In addition, all outstanding U S West stock options were converted into options to acquire Qwest common stock. Although the merger was reportedly accounted for as a reverse acquisition under the purchase method of accounting, with U S West being deemed the acquirer for accounting purposes and Qwest the acquired entity, Qwest management was in control of the surviving entity. The total value of the merger consideration at the time the transaction closed was approximately $44 billion in Qwest stock.

12. Qwest purportedly organized itself, on the basis of the products and services the Company offered, into four business segments: retail services, wholesale services, network services, and directory services. The retail services segment includes communications services such as Internet, wireless, data and long distance services, and local exchange telephone services. The wholesale services segment provides, among other things, network exchange services nationally, primarily to telecommunications companies and Internet service providers. The network services segment provides access to Qwest's telecommunications network, and the directory services segment publishes White and Yellow Page telephone directories and provides electronic directory and other information services.

Defendants' False Financial
Reporting Begins

13. In its Form 10-Q for the quarter ended March 31, 2000, Qwest touted that it would be "the first company in 2000 to introduce an all-optical Internet network coast-to-coast with maximum reliability." In addition, Qwest also said in that Form 10-Q that through KPNQwest, its European joint venture, the Company would build and operate a similarly extensive "11,800-mile network spanning 46 business markets in Europe."

14. That Form 10-Q also reported that for the first quarter of 2000, Qwest achieved net earnings of $12.6 million, compared to $4.8 million for the same period in 1999. Excluding certain expenses for its U S West merger and gains on the sale of certain investments, Qwest stated that it would have reported net earnings of $30 million. With respect to the Company's communications services, Qwest stated that revenues increased from $737.2 million for the first quarter of 1999, to $1.216 billion for the first quarter of 2000, and falsely attributed the increased revenues as follows:

> During the three months ended March 31, 2002, as compared to the same period of the prior year, Communications Services revenue increased due to the growth in Internet, multimedia, data and voice services sold to business, government and wholesale customers. With the completion of the Company's network, Construction Services no longer generates revenue from network construction.

15. The Company also represented in that Form 10-Q that its accounting practices and financial statements conformed to GAAP[1] and SEC rules, as follows:

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[1] GAAP (generally accepted accounting principles) are those principles recognized by the accounting profession as the conventions, rules, and procedures necessary to define accepted accounting practices at a particular time. Regulation S-X of the Securities and Exchange Commission (the "SEC"), 17 C.F.R. § 210.4-01(a)(1), states that financial statements filed with the SEC which are not prepared in compliance with GAAP are presumed to be misleading and inaccurate, despite footnote or other

> The accompanying unaudited condensed financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the condensed consolidated financial statements include all adjustments, consisting of normal recurring items, necessary to fairly present the results of operations, financial position and cash flows for the periods presented.

16. On March 31, 2000, Qwest stock closed in trading on the NYSE at $48 per share.

17. By June 2000, Qwest had completed its acquisition of U S West. In its Form 10-Q for the quarter ended June 30, 2000, Qwest continued to report revenue increases, as follows:

> Revenue growth for the quarter ended June 30, 2000 was primarily attributable to greater wireless sales ($63 million), increased demand for basic telephone services ($49 million) and increased sales of calling services ($16 million). Revenue growth for the six months ended June 30, 2000 was primarily attributable to greater wireless sales ($129 million), increased demand for basic telephone services ($74 million) and increased sales of calling services ($39 million). Also contributing to revenue growth were greater revenues from interconnection, increases in the subscriber base of our MegaBit (TM) data services, paging services and LNP charges. Offsetting these increases in revenue were regulatory rate changes and accruals for regulatory proceedings of $36 million and $17 million for the three and six months ended June 30, 2000, respectively.

18. The Company also represented in that filing that its accounting practices and reported revenues and results "fairly present" Qwest's financial condition, as follows:

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disclosure.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

> Basis of Presentation. The condensed consolidated interim financial statements are unaudited. We prepared these financial statements in accordance with the instructions for Form 10-Q and therefore, did not include all information and footnotes required by generally accepted accounting principles. In our opinion, we made all the adjustments (consisting only of normal recurring adjustments) necessary to fairly present our consolidated results of operations, financial position and cash flows as of June 30, 2000 and for all periods presented.

19. On June 30, 2000, Qwest common stock closed at $49.6875 per share.

20. In its Form 10-Q for the quarter ended September 30, 2000 filed with the SEC on November 14, 2000, Qwest reported that revenues had increased from $12.0 billion for the same nine month period in the prior year, to $13.9 billion. According to that Form 10-Q:

> Margins from the retail services segment increased due to revenue growth. Revenues from the retail services segment increased 54% and 23% for the three and nine months ended September 30, 2000, respectively over the comparable 1999 periods. The revenue increases were partially offset by higher operating expenses driven by growth initiatives. Margins from the wholesale services segment increased as a result of greater demand for access and interconnection services, partially offset by price reductions as mandated by both federal and state regulatory authorities and higher operating costs associated with access charge expenses. Margins from the network and access operations segment decreased due to higher operating expenses associated with enhancing customer service. Margins from the directory services segment increased due to price increases, increased sales of directory-related Internet products and increased efforts to control costs.

21. The Company continued to falsely portray in that Form 10-Q that its accounting practices and financial results were presented "fairly", as follows:

> The condensed consolidated interim financial statements are unaudited. We prepared these financial statements in

> accordance with the instructions for Form 10-Q and therefore, did not include all information and footnotes required by accounting principles generally accepted in the United States. In our opinion, we made all the adjustments (consisting only of normal recurring adjustments) necessary to fairly present our consolidated results of operations, financial position and cash flows as of September 30, 2000 and for all periods presented.

22. On September 29, 2000, Qwest common stock closed at $48.125 per share.

23. Around the time Qwest filed its third quarter 2000 Form 10-Q with the SEC, Plaintiff had been acquiring substantial amounts of Qwest shares. For example, in November 2000 alone, New Jersey purchased at least 1,490,000 Qwest shares for an aggregate of $62,018,701, or an average price of $41.62 per share. However, at the time of these purchases, New Jersey was unaware that the defendants had been engaging in accounting improprieties and that, as a result, Qwest had been materially overstating its revenues and earnings and would subsequently have to restate those results.

Qwest's Improper Swap Transactions

24. Beginning at least as early as 2000, the defendants embarked upon a plan and scheme to artificially inflate Qwest's reported revenues and earnings. One key component of this scheme involved Qwest's participation in "swap" transactions with customers which appeared to substantially increase Qwest's growth rate, revenues and earnings, but which in fact had no legitimate economic purpose. In these transactions, Qwest purported to sell capacity on its optical telecommunications network to another carrier, while simultaneously buying a nearly identical amount from the other carrier. In complete violation of GAAP, Qwest recognized revenue from the sale, but booked the corresponding purchase as a capital expenditure rather

than as an operating cost. This accounting practice permitted the defendants to improperly inflate Qwest's reported revenues, and would ultimately force the Company to massively restate its books, revenues, profits, and accounts.

25. In addition to improperly booking these transactions, Qwest also prematurely recognized revenue from swap contracts in the first year despite the fact that the contracts usually spanned several years and the customers were only obliged to pay over the contract's full term. This acceleration of revenue forward further improperly inflated Qwest's reported revenues.

26. For example, Qwest's Form 10-Q for the quarter ended September 30, 2000 reported that its revenues from commercial services increased 104% from the third quarter of 1999, to $2.4 billion. However, the Company failed to disclose that a material portion of this purported revenue increase was illusory because it was attributable directly to swap transactions. Instead of accurately disclosing these transactions, the Company stated as follows:

> COMMERCIAL SERVICES. Commercial services revenues are derived from Internet, data, voice and wireless products and services to both retail and wholesale business customers. The increases in commercial services revenues for the three and nine months ended September 30, 2000 were primarily attributable to the Merger. Also contributing to the increases, were growth in sales of data products and services. We believe revenues from data products and services will account for an increasingly larger portion of commercial services revenues in future periods.

27. Qwest concealed the true nature and impact of its swap transactions and booked hundreds of million of dollars in additional fictitious revenues in the fourth quarter of 2000, including one allegedly for over $250 million with Cable & Wireless. Although Qwest's Form 10-K for 2000 mentioned the transactions, the defendants falsely sought to minimize their

impact, stating that the transactions "were not significant in either fiscal 2000 or 1999" as follows (emphasis added):

> The Company's revenues are generated from a variety of services and products. Commercial, consumer and small business services revenues are derived from retail and wholesale services such as Internet and data products and services, including Web hosting and Internet access, frame relay and digital subscriber line ("DSL"). Also included in this category are voice services such as basic monthly fees for telephone service wireless services, fees for calling services such as voice messaging and caller identification, special access and private line revenues from end-users buying local exchange capacity to support their private networks and inter- and intraLATA (local access and transport area) long-distance services. To a lesser extent, the Company sells capacity under indefeasible rights of use contracts. ***Revenues from these contracts are included in commercial services and were not significant in either fiscal 2000 or 1999***. Directory services revenues are generated primarily from selling advertising in the Company's published directories. Switched access services revenue is derived principally from charges to interexchange carriers ("IXCs") for use of the Company's local network to connect customers to their long-distance networks.

28. The Company's Form 10-K for 2000 also falsely stated that Qwest properly recognized revenues "ratably over the term of" these contracts when, in fact, the opposite was true. According to the Form 10-K:

> Occasionally, the Company sells capacity on its network to other telecommunication providers. Sales of capacity are accounted for as either sales-type leases, operating leases or service agreements depending upon the terms of the transaction. Revenues related to sales of capacity that meet the criteria of a sales-type lease are recognized at the time of delivery of the capacity to the customer. If title is not transferred or if the other requirements for sales-type lease accounting are not met, revenue is recognized ratably over the term of the agreement.

29. On December 29, 2000 -- the last trading day of that year -- Qwest common stock closed at $40.875 per share.

30. Although the Company minimized their significance in public statements and continued to portray Qwest's accounting and financial practices as accurate and conservative, the actual truth was that Qwest's bogus revenue recognition from swap transactions continued unabated through 2001. For example, Qwest allegedly entered into two $100 million swaps with the now bankrupt Global Crossing which are described more fully below. Additionally, the Company also allegedly entered into an additional $15 million swap in 2001 with Sonus Networks, and another swap reportedly valued at some $500 million with Enron Corp. which, according to a March 29, 2002 article in *The New York Times*, enabled Qwest to inflate its 2001 third quarter results by at least $195.5 million. According to that article:

> Enron and the telecommunications giant Qwest Communications struck a deal last fall to swap fiber optic network capacity and services at exaggerated prices in an effort to improve each company's financial picture, executives close to the deal said this week.
>
> Details of the deal, which was not announced at the time but has been disclosed in recent filings in Enron's bankruptcy case, indicate that the two companies raced to complete the transaction as the third quarter was ending in September. Enron and Qwest valued the transaction at more than $500 million, but analysts said the timing and the valuation would be hard to justify because a glut of fiber optic capacity had sent network prices plummeting.
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> * * *
>
> But executives close to the Qwest-Enron deal, one of the largest recorded, said the swap had other objectives. It helped Qwest, the executives said, soften a deteriorating situation in profit and revenue at the end of last year's third quarter.
>
> The deal, they said, also allowed Enron, which was tumbling toward a bankruptcy court filing, to avoid recording a huge loss by selling an asset whose value had plummeted on the open market.

> "Qwest said we will overpay for the assets, and you will overpay me on the contract," one former Enron executive said. "They had a pinch in the third quarter and needed a deal."
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> * * *
>
> Then, on Sept. 30, a Sunday and the final day of the third quarter, Qwest signed a deal to pay Enron $308 million for assets that included so-called dark fiber along a route from Salt Lake City to New Orleans. Dark fiber refers to idle network strands that require additional investments in electronic equipment before they can be put into service. In exchange, Enron agreed to pay Qwest $195.5 million for "lit wavelength," or active fiber optic cable services, over a 25-year period; each company exchanged checks for about $112 million around the close of the deal.
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> * * *
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> Qwest did not announce the Enron deal after it was made, although the company had regularly issued news releases for smaller deals, including a $20 million contract with Perot Systems Inc. on Sept. 27.

31. In addition, in early 2001, following a presentation by Nacchio, Afshin Mohebbi, Qwest's President of Worldwide Operations, engaged in meetings with William A. Trent. Mr. Trent is an accountant and research analyst employed by Plaintiff New Jersey to assist in investing New Jersey's pension assets. Mohebbi touted the Company's financial position and, during a question and answer session with Mr. Tent and another analyst, falsely explained that Qwest's large capital expenditures were the result of the Company's growth strategy. In fact, rather than implementing a growth strategy, Qwest's capital expenditures were inflated because this category of expenses was the accounting item that the Company used to hide the swap transactions.

32. On June 20, 2001, Morgan Stanley issued a research report identifying what it suspected might be accounting irregularities in Qwest's financial statements. That same

day, Qwest held a conference call with investors. Plaintiff New Jersey, through its representative, participated in that call and relied on the statements the Company and Nacchio made. On that call, Nacchio explicitly represented to Plaintiff New Jersey that the Morgan Stanley report was "unprofessional and irresponsible." Nacchio also identified himself during that call as "a fiduciary of your investment money" and repeatedly misrepresented the veracity of Qwest's accounting by, among other things, stating as follows:

a. "there are no accounting issues or improprieties in Qwest's financial report";

b. "there is nothing about any judgments on purchase accounting that will affect our ability to go forward with anything that we have said . . ."; and

c. all writeoffs have been "forthright".

Nacchio concluded by stating, in sum, that there are "no improprieties, nothing wrong with our accounting." Justifiably relying on the fraudulent statements made by Messrs. Anschutz and Mohebbi in 2001 in conjunction with the statements contained in the Company's regulatory filings and other public statements, New Jersey and the Division of Investment continued to invest state pension and other public funds that it managed in Qwest securities.

33. An article in *The Wall Street Journal* on February 13, 2002 cited Qwest's use of swaps and termed the Company "[a]mong the most aggressive" in accounting for these transactions, as follows:

> Qwest Communications International Inc. has been doing some creative revenue boosting of its own.
>
> In four deals during the past two years, Qwest sold equipment valued at $450 million to a company, and, in turn, Qwest agreed to pay the buyer hundreds of millions of dollars for

Internet services using the equipment it had sold. Qwest – a telecommunications company that doesn't make equipment but had instead bought the gear – booked the equipment sales as revenue. Meanwhile, the buyer, KMC Telecom Holdings Inc., financed the equipment and put the debt on its books.

* * *

For investors, however, this type of transaction raises a Question about how to best assess the financial position of the company.

"It gives the impression that they're growing at a higher-than-expected rate," said Drake Johnstone, an analyst with Davenport & Co. in Richmond, Va. While the sales may be small, Mr. Johnstone added, they are still significant enough "to affect Qwest's growth."

The KMC transactions are interesting both because Qwest is a service provider, not an equipment provider, and the services KMC is providing for Qwest are Qwest's specialty. In essence, Qwest agreed to outsource some Internet and telecom services to KMC, a privately held Bedminster, N.J., firm. KMC, which pulled a planned initial public offering in October 2001 due to market conditions, provides telecommunications services in about 37 markets. Qwest said it did not incur any debt to purchase the equipment; it bought the gear and sold it to KMC at essentially the same time.

* * *

In March 2001, Qwest sold $65 million of equipment to KMC to route phone calls through the Internet. KMC agreed to install the gear at its facilities and handle service for Qwest for 48 months. Qwest agreed to pay about $28.7 million per year.

In June 2001, Qwest sold KMC $83 million of routers and switches capable of handling high-speed Internet traffic. Qwest agreed to pay $42.4 million per year for the service. The pact runs through 2006.

The largest deal occurred in June 2000, when KMC agreed to buy about $168 million of "Internet infrastructure" and maintain it for Qwest until August 2004. Service terms weren't disclosed.

> In March 2000, KMC bought $134 million of "portal equipment" from Qwest and agreed to maintain the equipment for 42 months.

34. By February 13, 2002, Qwest common stock had plummeted to just over $8 per share.

35. Another article published in *The Wall Street Journal* on February 13, 2002 discussed Global Crossing's use of swaps to enhance its reported revenues, and the concomitant effects at Qwest, as follows:

> Now, the Securities and Exchange Commission and the Federal Bureau of Investigation are probing whether Global Crossing falsely inflated revenues by booking hundreds of millions of dollars in swaps of capacity it might not have needed.
>
> * * *
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> At the center of the debate is a type of telecommunications lease known as an Indefeasible Right of Use. Pioneered decades ago when AT&T Corp. was still a monopoly, the leases allowed competitors to gain access to the costly undersea cables that only Ma Bell could afford to build.
>
> Today, so-called IRUs allow a telecom carrier to buy all types of telecom capacity and gear at low rates, typically for periods of 20 to 25 years. Since IRUs are technically rights to a physical part of an underground cable, they can be considered an asset. That means their cost isn't part of a company's operating results, but of the property, plant, and equipment line listed on a firm's balance sheet.
>
> That isn't controversial. What the SEC and other investigators want to determine is whether Global Crossing abused this longstanding practice by entering into back-to-back transactions that allowed the company to artificially inflate revenues. Another big unknown is how prevalent the practice is through the industry.
>
> The type of transaction under scrutiny works like this: Company A sells an IRU to Company B for $100 million, and books the incoming cash as revenue. Meanwhile, Company A

buys a different IRU from Company B for $100 million, and treats the transaction as an asset purchase. Even though its cash position doesn't budge, Company A books $100 million in new sales without recognizing a corresponding operating expense.

* * *

Not all the companies account for them in the same way. In some cases, the impact was dramatic. Among the most aggressive was Qwest, which booked revenue from the swaps up front. For the first nine months of 2001, Qwest sold $870 million worth of network capacity to vendors from which it also bought $868 million worth of capacity in separate transactions. Qwest, which began as an entrepreneurial fiber company and then bought the Baby Bell U S West, said it recognized $664 million in revenue on the sales of capacity to these vendors. The additional $206 million is for operation and maintenance contracts that Qwest will recognize over the life of the agreement.

The sales had a big effect on Qwest's revenue for the first nine months of 2001. Revenue including the swaps increased 8% to $15 billion, compared with $13.9 billion in the same period a year earlier. Without the sales, however, revenue grew less than 3% to $14.4 billion.

* * *

In particular, Mr. Olofson notes one $150 million exchange transaction with 360networks, which he says was done for North American and Atlantic routes on which Global Crossing already had substantial capacity. Another first-quarter deal was with Qwest, worth $100 million. In his public statement, he says Global Crossing "roundtripped" the cash by purchasing $100 million of capacity from Qwest.

36. According to a *Dow Jones* report that same day, Qwest continued to defend its accounting treatment of the swaps, but acknowledged that the KMC deals had not been timely disclosed, as follows:

Qwest Communications International Inc. said it accounted for all equipment sales to KMC Telecom Holdings Inc. properly

> and said it discussed the transactions at an analysts' meeting in December.
>
> * * *
>
> Qwest said the December meeting was the only time it mentioned KMC to investors. The meeting took place several months after the Denver telecom company came under fire for a similar equipment sale to a start-up called Calpoint LLC. The meeting was broadcast over the Internet and via conference call and is still available as a video. Qwest has never disclosed the KMC deals in any regulatory filings with the SEC, as reported in Wednesday's article.
>
> Analysts and investors say that Qwest should have disclosed the transactions in their filings because they were included as revenue and therefore skewed its financial picture. A spokesman for Qwest said the company didn't detail the KMC transactions in any SEC filings because it "doesn't break out the companies that we sell equipment to."

37. A complaint filed February 26, 2002 by Global Crossing's former Vice President of Finance, Roy Olofson (who had been quoted extensively in *The Wall Street Journal* on February 13, 2002),[2] described Qwest's role in the reciprocal transactions:

> 29. On August 3, 2001, Global Crossing Ltd.'s CFO, defendant Cohrs, circulated an e-mail to defendant Casey and others commenting on a press story regarding Qwest Communications. In that e-mail Cohrs not only acknowledges the fact that Global Crossing Ltd.'s revenue recognition policies were suspect but he specifically indicated that he was concerned that related issues at Global Crossing Ltd.'s customer, Qwest Communications, was drawing attention to the issue. Cohrs' e-mail stated: "Qwest is booking sales type lease revenue as GAAP revenue and not breaking it out. At least we get credit for breaking it out. *The bad news is that this is raising visibility on the swaps issue*."

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[2] Olofson v. Winnick, Case No. CV-02-01693 (C.D. Cal. - Western Div.).

* * *

> 30. Plaintiff is informed and believes and thereupon alleges that Cohrs' fear of visibility of the "swap issue" reflects his concern that a possible investigation of Qwest's accounting practices would reveal, inter alia, that Qwest and Global Crossing Ltd. had swapped approximately $100 million of capacity in each of the first two quarters, some of which had not even been defined at the time of sale, that each company accounted for the transaction differently despite having the same firm of outside auditors (Andersen), and that further investigation could lead to the conclusion that these transactions were non-monetary exchanges of capacity that should not have been booked as revenue at all. In other words, Cohrs and by implication Global Crossing Ltd. feared that the public would be made aware that through this and related transactions, Global Crossing Ltd. was giving the impression that it was generating cash revenues when, in actuality, these transactions did not increase the cash position of Global Crossing Ltd. in any material sense. Furthermore, Global Crossing Ltd. was listing the payments to Qwest as a capital expenditure, which allowed Global Crossing Ltd. to report none of the expense (or at most a very small portion) in the current period.

38. Defendants' concealment of the true nature of Qwest's swaps was highly significant to investors because, among other things, capacity asset sales are non-recurring in nature. This non-recurring component of the swaps was also not disclosed to Plaintiff or other investors. Instead, the defendants continually sought to downplay -- indeed, conceal -- the integral importance these swaps bore to Qwest's ability to "report" revenue and earnings growth. In fact, the defendants failed to disclose the effects these swaps had on Qwest's reported results through each of the first three quarters of 2001; instead, Qwest's Form 10-Q's for each of those quarters, like those for the first three quarters of 2000, represented as follows:

> The condensed consolidated interim financial statements were unaudited. Qwest Communications International Inc. ("Qwest" or the "Company" or "we" or "us" or "our") prepared these financial statements in accordance with the instructions for Form 10-Q. In compliance with those instructions, certain information and footnote disclosures normally included in the financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. In management's opinion, all adjustments (consisting only of normal recurring adjustments) necessary to fairly present the consolidated results of operations, financial position and cash flows as of [respectively, March 31, June 30, and September 30], 2001 and for all periods presented were made.

Examples of Other Accounting and
Related Financial Reporting Violations

39. In addition to swaps, Qwest was also involved in a variety of other accounting improprieties which further concealed the Company's true financial performance. For example, in June 1999, Qwest entered into a $15 million contract with another telephone company, Warwick Valley, with a five-year term. Instead of recognizing the revenue ratably over the five-year period, Qwest recorded the full $15 million as soon as the contract was signed.

40. In September 2000, Qwest entered into a contract with Genuity for network services worth $260 million over the five-year term. Under the contract, Qwest was to receive a payment of $100 million in exchange for shipping certain equipment to Genuity. However, Qwest did not have the equipment, but instead had to acquire it from outside vendors which it did for $40 million. Instead of booking $60 million in profit by recording revenues of $100 million and costs of $40 million, however, Qwest recorded $20 million of the costs as an asset and booked $80 million in profits.

41. Qwest also improperly categorized certain write-offs as being post-merger costs associated with the US West merger which, in fact, were not associated with that merger at

all. For instance, Qwest booked as post-merger costs charges associated with the Company's failed effort to build an enhanced digital subscriber line in Arizona and Colorado.

42. Qwest also improperly deducted from Qwest's pension plan certain severance payments to executives who departed the Company after the US West merger instead of deducting those payments from operating earnings. In fact, in August 2001, the SEC required Qwest to amend its Form 10-K for 2000 and forced the Company to disclose that its reported results for 2000 had benefitted from a pension credit of $299 million pre-tax compared to a charge of $8 million in 1999. The $299 million credit represented some 16% of Qwest's reported operating income for the year.

43. In late 2000, defendant Nacchio and others also caused Qwest to materially overstate the results of the Company's directory services business. This was accomplished by accelerating the time the Company recognized revenue from the directories it shipped. For example, the directory for Colorado Springs, which annually had been shipped in January, was changed to be shipped in December 2000, and thus, revenue from two annual Colorado Springs' directories were recognized within one fiscal year. This gambit permitted Qwest to report significantly increased sales for 2000.

44. Defendant Nacchio and the other defendants also artificially accelerated revenue from directory services by ordering that a substantial number of the directories be switched from yearly to 13-month directories. Doing so enabled Qwest to recognize the full amount of the directory as revenue in the quarter it was shipped. However, since it billed many customers on a monthly basis, Qwest was not assured that customers would pay for the extra

month, and certainly in all events had not received those purported revenues at the time the Company had recorded them.

45. The defendants' accounting gimmicks with respect to Qwest's directory services enabled the Company to inflate its revenues many millions of dollars in the fourth quarter of 2000. The extensions affected directories in Denver (which alone was worth aproximately $72 million in revenues per year), Portland and Seattle.

46. Instead of disclosing these manipulative practices as the reason for the increase in directory services revenue, the Company's 2000 Form 10-K falsely stated as follows:

> Directory services revenues for 2000 increased by almost $100 million due principally to higher advertising rates, an increase in the number of directories published and an increase in the number of premium quality advertisements.

47. As a consequence, the defendants expressly and purposefully concealed the fact that the majority of the increase in directory service revenues resulted from Qwest's manipulation of the directory delivery dates and terms. Subsequent disclosures in Qwest's Form 10-Qs were no more revealing. For example, Qwest's Form 10-Q for the period ending March 31, 2001 stated:

> The decrease in directory services revenues for the three months ended March 31, 2002 was primarily attributable to a change in the mix of directories published in the three months ended March 31, 2001 versus the three months ended March 31, 2000, partially offset by increased advertising rates.

48. The Company finally began to admit that it had altered certain directory delivery dates and terms only after it announced that the SEC was investigating these very issues. Specifically, the Company's 2001 Form 10-K stated as follows:

> Directory publishing revenues.

> In 2000, the Company shortened the service life of one of its directories to 11 months, resulting in the directory being published in both January and December of 2000. This resulted in the Company recording an additional $28 million of revenue in 2000 relating to this directory.
>
> In 2001, the Company extended to 13 months or shortened to 11 months the service lives of certain of its directories, resulting in 2001 revenues being $42 million higher than if the service lives of the directories had not been extended or shortened.

49. The foregoing accounting improprieties resulted in a material overstatement of Qwest's reported financial results and violated GAAP and the following fundamental accounting principles, among others:

a. that interim financial reporting should be based upon the same accounting principles and practices used to prepare annual financial statements (Accounting Principles Board Opinion ("APB") No. 28, ¶10);

b. that financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and similar decisions (Financial Accounting Standards Board ("FASB") Statement of Concepts No. 1, ¶34);

c. that financial reporting should provide information about the economic resources of an enterprise, the claims to those resources, and effects of transactions, events and circumstances that change resources and claims to those resources (FASB Statement of Concepts No. 1, ¶40);

d. that financial reporting should provide information about how management of an enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to it. To the extent that management

offers securities of the enterprise to the public, it voluntarily accepts wider responsibilities for accountability to prospective investors and to the public in general (FASB Statement of Concepts No. 1, ¶50);

e. that financial reporting should provide information about an enterprise's financial performance during a period. Investors and creditors often use information about the past to help in assessing the prospects of an enterprise. Thus, although investment and credit decisions reflect investors' expectations about future enterprise performance, those expectations are commonly based at least partly on evaluations of past enterprise performance (FASB Statement of Concepts No. 1, ¶42);

f. that financial reporting should be reliable in that it represents what it purports to represent. That financial reporting should be reliable as well as relevant is a notion that is central to accounting (FASB Statement of Concepts No. 2, ¶¶58-59);

g. that financial reporting should be complete, which means that nothing is left out of the information that may be necessary to insure that it validly represents underlying events and conditions (FASB Statement of Concepts No. 2, ¶79); and

h. that conservatism be used as a prudent reaction to uncertainty to try to ensure that uncertainties and risks inherent in business situations are adequately considered. The best way to avoid injury to investors is to try to ensure that what is reported represents what it purports to represent (FASB Statement of Concepts No. 2, ¶¶95, 97).

50. In addition, defendants' accounting violations, including with respect to Qwest's swap transactions, write-offs, pension credits and directory revenue recognition practices, *inter alia*, violated the following specific GAAP requirements that full and adequate

disclosure be provided to users of the financial statements on either the face of the financial statements or the footnotes thereto:

a. FASB Statement of Concepts No. 5, which provides, *inter alia*:

> Information disclosed in notes . . . amplifies or explains information recognized in the financial statements. That sort of information is essential to understanding the information recognized in the financial statements and has long been viewed as an integral part of financial statements prepared in accordance with generally accepted accounting principles.

b. FASB Statement of Concepts No. 1, ¶34, which provides, *inter alia*:

> Financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and similar decisions. The information should be comprehensible to those who have a reasonable understanding of business and economic activities and are willing to study the information with reasonable diligence.

c. FASB Statement of Concepts No. 1, ¶¶42, 47, which emphasizes the reliance users of financial statements place on information about an enterprise's financial performance during a specific period, as follows (footnote omitted):

> Financial reporting should provide information about an enterprise's financial performance during a period. Investors and creditors often use information about the past to help in assessing the prospects of an enterprise. Thus, although investment and credit decisions reflect investors' and creditors' expectations about future enterprise performance, those expectations are commonly based at least partly on evaluations of past enterprise performance.
>
> * * *
>
> Investors, creditors, and others often use reported earnings and information about the components of earnings in various ways and for various purposes in assessing their prospects for cash flows from investments in or loans to an enterprise.

d. FASB Statement of Concepts No. 2, which mandates that reliability is a primary quality that makes accounting information useful for decision making, and provides that,

to be reliable information must have representational faithfulness and it must be verifiable and neutral, and defines reliability as follows (emphasis added):

> The quality of information that assures that information is reasonably free from error and bias and **faithfully represents what it purports to represent**.

e. APB No. 22, ¶¶7, 12 which provide the following (emphasis added):

> The accounting policies adopted by a reporting entity can affect significantly the presentation of its financial position, changes in financial position, and results of operations. Accordingly, the **usefulness** of financial statements for purposes of making economic decisions about the reporting entity **depends significantly upon the user's understanding of the accounting policies followed by the entity**.
>
> * * *
>
> Disclosure of accounting policies should identify and describe the accounting principles followed by the reporting entity and the methods of applying those principles that **materially affect** the determination of financial position, changes in financial position, or **results of operations**. In general, the disclosure should encompass important judgments as to appropriateness of principles relating to recognition of revenue and allocation of asset costs to current and future periods . . . .

51. Further, the defendants also violated the following GAAP provisions relating to revenue and expense recognition, among others:

a. FASB Statement of Concepts No. 5, ¶83(b), which states, in part, that "[r]evenues are not recognized until earned";

b. FASB Statement of Concepts No. 2, ¶160, which states in part:

> The quality of reliability and, in particular, of representational faithfulness leaves no room for accounting representations that subordinate substance to form . . . ;

c. FASB Statement of Concepts No. 6, ¶80, which provides, as follows (footnote omitted):

> Expenses are outflows or other using up of assets or incurrences of liabilities (or a combination of both) from delivering or producing goods, rendering services, or carrying out other activities that constitute the entity's ongoing major or central operations.

52. In addition, defendant Arthur Andersen also violated various provisions of GAAS.[3] In fact, Qwest engaged Arthur Andersen to provide independent auditing and accounting services for Qwest at all times relevant to this action. Arthur Andersen audited and certified Qwest's financial statements for the year ended December 31, 2000. Arthur Andersen's report included in Qwest's Form 10-K for that year stated that Qwest's financial statements fairly presented the Company's financial condition and the results of its operations in conformity with GAAP, and that the audit by Arthur Andersen was performed in accordance with GAAS. Arthur Andersen's unqualified audit reports were false and misleading as Qwest's financial statements were not presented in conformity with GAAP, as described above.

53. In order to opine that a company's financial statements are prepared in conformity with GAAP, the auditor is required to perform its audit procedures in accordance with GAAS. The ten basic GAAS provisions are as follows:

> General Standards
>
> 1. The audit is to be performed by a person or persons having adequate technical training and proficiency as an auditor.
> 2. In all matters relating to the assignment, an independence in mental attitude is to be maintained by the auditor or auditors.

[3] GAAS stands for generally accepted auditing standards.

3. Due professional care is to be exercised in the performance of the audit and the preparation of the report.

Standards of Field Work

1. The work is to be adequately planned and assistants, if any, are to be properly supervised.

2. A sufficient understanding of internal control is to be obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.

3. Sufficient competent evidential matter is to be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under audit.

Standards of Reporting

1. The report shall state whether the financial statements are presented in accordance with generally accepted accounting principles (GAAP).

2. The report shall identify those circumstances in which such principles have not been consistently observed in the current period in relation to the preceding period.

3. Informative disclosures in the financial statements are to be regarded as reasonably adequate unless otherwise stated in the report.

4. The report shall contain either an expression of opinion regarding the financial statements, taken as a whole, or an assertion to the effect that an opinion cannot be expressed. When an overall opinion cannot be expressed, the reasons therfore, should be stated. In all cases where an auditor's name is associated with financial statements, the report should contain a clear-cut indication of the character of the auditor's work, if any, and the degree of responsibility the auditor is taking. (American Institute of Certified Public Accountants ("AICPA") Professional Standards AU § 150).

54. In the performance of its "audit", Arthur Andersen violated the general standard of due care and did not properly plan or perform the audit. Nor did Arthur Andersen obtain the requisite understanding of Qwest's purported system of internal controls or competent

evidential matter. Among other things, Arthur Andersen violated the standards of reporting that require that a company's financial statements contain adequate disclosures, and the standard that requires the auditor to opine on whether a company's financial statements were prepared in accordance with GAAP.

55. For example, with respect to Qwest's quarterly reports for 2001, Arthur Andersen failed to require Qwest to appropriately record and/or disclose the nature of the Company's swaps, pension-related and other transactions, thus violating AICPA Professional Standards AU § 722, *Interim Financial Information,* which provides, among other things, as follows:

> The objective of a review of interim financial information is to provide the accountant, based on applying his or her knowledge of financial reporting practices to significant accounting matters of which he or she becomes aware through inquiries and analytical procedures, with a basis for reporting whether material modifications should be made for such information to conform with generally accepted accounting principles.

56. Moreover, the undisclosed, albeit critically important and adverse, financial and accounting acts and practices alleged in this Complaint were never properly or timely disclosed to Plaintiff. The omitted and misrepresented information is precisely the type of information which, because of SEC regulations, regulations of the NYSE and other national stock exchanges, and customary business practice, is expected by investors and securities analysts to be accurately and timely disclosed, and corporate officials and their legal and financial advisors are, or should be, aware of and adhere to such proper business practices.

The Truth Begins To Emerge

57. On October 31, 2001, Qwest announced its financial results for three-month period ending September 30, 2001. At that time, the Company reported a loss of $138 million, or $.08 per share, compared with a profit of $231 million, or $0.14 per share, for the comparable quarter of the prior year. Immediately upon this news, Qwest stock plummeted to as low as $12.50 per share from the previous day's close of $16, a further loss of billions of dollars in market capitalization.

58. On February 13, 2002, *The Wall Street Journal* first began to disclose some of the details regarding Qwest's swap transactions. Various Qwest shareholders filed class and other actions against the Company, certain of its top officers, and Arthur Andersen as a result. However, the Company continued to maintain that its swap transactions and the Company's accounting treatment were proper in all respects.

59. By early April 2002, Qwest announced that it was the subject of an SEC investigation into the Company's accounting practices. The Company said at this time that the investigation could "have a material effect on Qwest's reported net income or earnings per share" for the years 1999 through 2001. Qwest also disclosed at this time that it could incur charges of as much as $30 billion to write-down the value of some of its assets.

60. According to the April 6, 2002 *Rocky Mountain News*:

> The Securities and Exchange Commission's Denver office this week upgraded an informal inquiry of Qwest's accounting practices to a formal investigation giving the SEC subpoena power to obtain financial documents and interview witnesses. The SEC's

Los Angeles office already was investigating Qwest's deals with bankrupt Global Crossing.

The SEC investigation covers Qwest's fiber-optic capacity deals, telecom equipment sales and telephone directory scheduling in 2000 and 2001. Qwest has repeatedly said that its accounting was proper at all times.

The main focus is Qwest's booking of $684 million of revenue in 2001 from fiber-optic capacity swaps – the nearly simultaneous purchase and sale of communications capacity. Qwest said that it legitimately conducted the swaps to complete its global communications network, but critics charge the company did deals at inflated prices to make its financial numbers.

* * *

Nacchio and other Qwest executives sold tens of millions of dollars of stock in the first half of 2001, at a time Qwest was trumpeting double-digit revenue growth and its stock was trading at an average of $38 a share. The company's stock now trades at just about $7 a share.

61. On April 9, 2002, Qwest announced that the SEC's investigation could lead the Company to restate its earnings. Qwest shares dropped an additional 6% in after-hours trading to some $6.79 per share.

62. On June 17, 2002, Nacchio resigned as Qwest's CEO in the wake of the SEC's investigation reportedly under pressure from the Company's Board.

63. On June 26, 2002, *The Wall Street Journal* discussed the Individual Defendants' insider selling of Qwest shares, and described the SEC's investigation, as follows:

Mr. Nacchio and his top executives were heavy sellers of Qwest stock during the years that the swapping took place. Mr. Nacchio's sales alone netted him about $130 million in profits

during that period, raising questions about his motivation to keep the stock price as high as possible. Qwest insiders sold shares between January 2000 and July 2001 valued at a total of $530 million.

At issue in the SEC investigation is the difference between the way Qwest accounted for the sales and the method used by its competitors, such as Global Crossing, which is also under SEC investigation.

Like Global Crossing, Qwest sold capacity on its fiber-optic network to carriers and also purchased capacity from them. In some cases, the amount of the sale and purchase were almost identical. But unlike Global Crossing and most other players in the industry, Qwest booked the revenue from these sales all at one time instead of deferring part of it over many years.

Global Crossing, by contrast, only booked reported revenue over the life of the contract, which in some cases was as long as 20 years. (It did include the whole amount in something it called "cash revenue," its own term, separate from accepted accounting rules, for the revenue that came in for services that hadn't yet been delivered.)

While its sale was booked upfront, Qwest's purchase of fiber capacity was booked as a capital expense, meaning the company could record the purchase over time instead of all at once.

* * *

Qwest, arguably more than any other telecom company, engaged in swaps of capacity, equipment sales and other transactions that helped the company achieve **[apparent]** phenomenal growth.

The effect was marked and boosted Qwest's revenue by $1 billion in 2001 and $465 million in 2000. In 2001, it recorded total revenue of $19.7 billion, up from $16.6 billion in 2000.

* * *

> At the same time, congressional interest in Qwest's accounting also is growing. At least one Qwest executive already has been called to testify at the U.S. House Energy and Commerce Committee, according to a person familiar with the federal investigations. And House and SEC inquiries of Global Crossing have taken a strong look at Qwest's roles in telecom transactions during 2000 and 2001.
>
> A person familiar with the situation said that one official who gave extensive testimony to regulators is Robin Wright, the Global Crossing saleswoman in charge of the company's relationship with Qwest. "Qwest is the first issue" that regulators ask Global Crossing officials about, according to a person familiar with the matter.
>
> Compared with Global Crossing, Qwest is said to face more extensive questioning about its aggressive accounting treatment.

64. Immediately following *The Wall Street Journal*'s June 26, 2002 article, Qwest's shares plummeted an additional 71% that day to a low of just over $1.20 per share, and closed at $1.79 per share. By this time, investor concern became rampant that Qwest would have to restate material amounts of its previously reported financial results, at least in large part because of the Company's swap transactions.

65. By July 15, 2002, *The Wall Street Journal* reported that Qwest was in a precarious financial condition and had growing liquidity concerns. This led certain private equity firms to express interest in acquiring Qwest assets at bargain prices.

66. On July 28, 2002 after the markets closed, Qwest announced that it expected to restate its financial results for 2000 and 2001 and that it would withdraw its

previously reduced financial projections for 2002. In a news release, Qwest said that it had uncovered misstatements that led the Company to book some $474 million in revenue for 2000 and 2001 in lump sums instead of over time; that it understated expenses in 2001 by $113 million; that it overstated expenses in 2000 by $15 million; and that it might have to restate the revenue it received from ***all*** optical capacity sales it booked in 2000 and 2001 which totaled, respectively, $486 million and $1 billion. Qwest also disclosed at this time that some $571 million in capacity sale revenue was misstated in 1999 and the first half of 2000 before the Company's merger with U S West, but that only $591 million in purported sales that was booked following the merger would have to be restated because the books in which the pre-merger misstatements were made no longer exist. Qwest's new Chairman and CEO, Richard Notebaert, said that pending the restatement, he would not be able to personally attest to the accuracy of Qwest's financial statements as required under the newly-passed Sarbanes-Oxley Act. Similarly, Qwest's new auditors, KPMG LLP, said it would not be able to offer any assurances regarding Qwest's second quarter 2002 results, because any restatements of prior periods might adversely affect those results.

67. Although the Company admitted that "it has in some cases applied its accounting policies incorrectly", it continued to deny, even at this time, that any accounting fraud took place.

68. On August 8, 2002, Qwest reported a quarterly loss for the three months ended June 30, 2002 of $1.14 billion; a charge of $926 million to write-down Qwest's stake in KPNQwest; a charge of $119 million to increase its bad-debt reserve relating to WorldCom's

bankruptcy; a revenue decline of 17% primarily from the lack of fiber-optic sales to its carriers; and a drastically reduced forecast for the year, cutting expected revenues by $1 billion.

69. According to the Company's Form 8-K filed with the SEC on August 19, 2002, Qwest admitted that its accounting for its directory publishing business had been improper since at least 1999.

70. Also, according to that same Form 8-K, the Company indicated that it was unable to quantify the extent of its accounting improprieties. The Company also disclosed that it was in danger of violating its loan covenants, that it was in negotiations with its lenders, and that it could have to file for bankruptcy protection.

71. On September 10, 2002, Qwest announced that it had temporarily withdrawn its application to sell long-distance telephone service in nine states, citing the Company's accounting problems and the pending restatements.

72. On September 19, 2002, *The Wall Street Journal* reported that Qwest's former CFO, defendant Szeliga, provided "extremely valuable" information to a Congressional committee investigating Qwest.

73. On September 22, 2002, Qwest announced that it would restate approximately $950 million in revenues it recognized in 2000 and 2001. According to the Company's press release:

> Qwest Communications International Inc. (NYSE: Q) today announced further restatement of its 2000 and 2001 financial statements as a result of its ongoing analysis of the complex accounting policies and practices relating to revenue recognition and accounting treatment for exchanges and sales of optical

capacity assets (IRUs). In restating its 2000 and 2001 financial statements with respect to these matters to be in conformance with generally accepted accounting principles, the company will reverse $950 million in revenues and related costs related to exchanges of optical capacity assets previously recognized. Some of the transactions included in this restatement were the subject of the company's July 28, 2002, announcement of determinations reached as of that date.

The company historically accounted for contemporaneous exchanges of optical capacity assets based on accounting policies approved by its previous auditor Arthur Andersen LLP. After analyzing its prior policies and practices, including the underlying accounting records, and in consultation with its new auditors, KPMG LLP, the company has concluded its policies and practices do not support the accounting treatment to allow for recognition of revenue from these exchange transactions. In conducting its analysis, the company considered discussions it had in late July 2002 with the staff of the Office of the Chief Accountant of the Securities and Exchange Commission.

The company also historically accounted for its sales of optical capacity assets for cash to third parties based on accounting policies approved by Arthur Andersen. Qwest has preliminarily concluded in consultation with KPMG that its accounting practices intended to follow these policies do not support the historical accounting treatment with respect to these optical capacity asset sales. The accounting for each of these transactions is being reviewed to assess whether and to what extent a restatement is required. Consequently, in connection with the company's restatement of its financial statements for 2000 and 2001 the approximately $531 million in revenue previously recognized from these sales of optical capacity assets for cash may require adjustment; however, the magnitude of the adjustments and the periods affected have not yet been determined.

74. On October 3, 2002, *Bloomberg News* reportedly obtained documents from a Congressional committee indicating that Qwest's Board members had warned former

CEO Nacchio a year earlier that the Company had certain accounting "credibility issues." According to the report:

> Mr. Nacchio acted as a "one-man band" who failed to communicate well with the board, according to an evaluation by directors prepared for a September 2001 board meeting. The documents were released yesterday to Bloomberg News by the House Energy and Commerce Committee, which held hearings on how Qwest and Global Crossing Ltd. accounted for sales.
>
> Qwest, the biggest local-telephone company in 14 western U.S. states, replaced Mr. Nacchio with Richard Notebaert in June after the U.S. government began probes into Qwest's bookkeeping. As board members raised red flags, Qwest publicly said its accounting was proper. The company's market value has plunged from $68.4 billion in December 2000 to $4.3 billion today.
>
> "The board really had some concerns about how Mr. Nacchio and his team were treating these accounting issues," U.S. Representative Diana DeGette, a Colorado Democrat, said yesterday at a hearing of the House panel's investigations subcommittee.
>
> The board raised concerns once, at a Dec. 5 meeting of the audit committee, Mr. Nacchio said at the hearing. In October, the compensation committee reviewed his evaluation with him, and it was largely positive, he said.

75. On October 9, 2002, *The Times of London,* noting that Individual Defendants Anschutz and Nacchio were intimately involved in the Company's day-to-day affairs, reported as follows:

> PHILIP ANSCHUTZ, the US billionaire whose entertainment company controls the Millennium Dome, is to face a second round of questioning from congressional investigators

> seeking further information about his role in the running of Qwest Communications, which has restated nearly $1 billion in revenue.
>
> The House Energy and Commerce Committee said it would again question Mr. Anschutz after Joseph Nacchio, former chairman and Chief executive of Qwest, publicly testified last week that Mr. Anschutz had played an active roll in the running of the firm.
>
> The committee is investigating whether Qwest and Global Crossing used so called “sham transactions” to boost their revenues and fool investors.
>
> Last week Mr. Nacchio told investigators that he discussed every major business decision with Mr. Anschutz and that the pair spoke up to three times a week. “Phil was very involved. He was helpful to me,” Mr. Nacchio declared.
>
> Mr. Nacchio’s testimony conflicts with that of Mr. Anschutz, who maintains that he had no involvement in the day-to-day running of Qwest.
>
> In a separate civil case, Eliot Spitzer, the New York attorney-general, is suing Mr. Anschutz and four other former executives, including Mr. Nacchio, alleging that they profited from the sale of shares allocated to them by Salomon Smith Barney, the investment banking division of Citigroup.

76. On October 29, 2002, *The Wall Street Journal* reported that Qwest would take a goodwill-impairment charge of $24 billion after completing an accounting review; that the Company would take an additional $10.8 billion in charges due to the reduced value of certain assets; and that it will defer $531 million of revenue it recorded in 2000 and 2001 from sales of optical capacity assets.

77. On October 30, 2002, Qwest announced that its third quarter 2002 losses widened to $214 million, and that its revenues fell over 13% from the previous year's third quarter. The Company reported that for the quarter, revenues declined to $3.8 billion from $4.37 billion for the same quarter of the prior year. However, the Company said that as with its second quarter 2002 results, it would also be unable to file its third quarter Form 10-Q because its auditors had not finished their review.

78. The fact that the Company has restated its financial statements, and is continuing to do so, is an admission that the financial statements it originally issued were false, and that the overstatement of revenues and income was material. Pursuant to GAAP, as set forth in APB No. 20, the type of restatement announced by Qwest was to correct for material errors in its previously issued financial statements. See APB No. 10, ¶¶ 7-13. The restatement of past financial statements is a disfavored method of recognizing an accounting change, because it dilutes confidence by investors in the financial statements, it makes it difficult to compare financial statements, and it is often difficult, if not impossible, to generate the numbers when restatement occurs. See APB No. 20, ¶ 14. Thus, GAAP provides that financial statements should only be restated in limited circumstances; i.e., when there is a change in the reporting entity, when there is a change in accounting principles used, or to correct an error in previously issued financial statements. Qwest's restatements were not due to a change in the reporting entity or a change in accounting principles, but instead because of material errors, omissions, and misstatements in previously issued financial statements. Thus, the restatement is an admission by the Company that its previously issued financial results and its public statements regarding those results, were materially false and misleading.

CLAIMS FOR RELIEF

COUNT I

(For Fraud Against Defendant Qwest And the Individual Defendants)

79. Plaintiff realleges and incorporates by reference the foregoing paragraphs as if fully set forth in this Count.

80. The Count is brought against defendants Qwest and the Individual Defendants.

81. Defendant Qwest and the Individual Defendants knowingly or recklessly made material misrepresentations of facts in connection with Plaintiff New Jersey's acquisition and holding of Qwest common stock. These defendants did so with the intention that, *inter alia*, Plaintiff and other open market purchasers would rely upon defendants' material misrepresentations, and Plaintiff did so rely. As alleged more fully herein, defendants' misrepresentations of fact included the following, among others:

a. that Qwest's financial results were free of material misstatement and "fairly present" the Company's financial results;

b. that Qwest's accounting practices conformed to GAAP and SEC regulations;

c. that Qwest's expense controls were appropriate and conformed to applicable accounting practices;

d. that Qwest had properly recognized and reported the revenues it earned, including from hundreds of millions of dollars in swap transactions involving the purported sale of equipment and capacity in reciprocal transactions;

e. that Qwest timely and properly took appropriate charges to, and wrote down the value of, certain of its assets, including its holdings in KPNQwest;

f. that Qwest properly classified its costs as expenses rather than as assets; and

g. that Qwest's reported directory service revenues accurately portrayed that important segment of the Company's business.

82. Further, the defendants knowingly and recklessly disregarded that numerous representations and statements made in Qwest's SEC filings were false and misleading and failed to timely or accurately disclose the true facts, all as alleged more fully in this Complaint. In particular, the defendants knew that because of Qwest's accounting violations, Qwest's financial statements and reports for 2000 and 2001 contained untrue statements of material fact and material omissions, and did not comply with GAAP, all because they included materially inflated statements of revenues and earnings which Qwest would later be required to, and did, restate.

83. Defendants also omitted to timely and accurately disclose various material facts which they were under a duty to disclose including, *inter alia*: Qwest's accounting violations; Qwest's actual financial performance and results; the likelihood Qwest would have to restate its earnings; the true circumstances regarding the Company's swap transactions; and the

true circumstances regarding the Company's directory services business, all as alleged more fully above.

84. The Individual Defendants were under a duty to accurately and timely disclose the truth concerning the foregoing by virtue of: their capacities as Qwest's senior officials; their role in connection with the insider transactions complained of herein; their access to confidential corporate information; their transactions in Qwest common stock; and their control of the Company and its financial reporting, all as alleged more fully above. The Individual Defendants undertook their fraudulent misconduct to obtain the perks and emoluments associated with their status as high level Qwest officials, and to enable them to realize many millions of dollars personally by selling Qwest shares at artificially inflated prices.

85. As a direct and proximate result of defendants' fraudulent misconduct, Plaintiff New Jersey justifiably relied upon defendants' knowing material misrepresentations of fact, acquired and held Qwest's shares at artificially inflated prices, and was injured thereby.

COUNT II

(Aiding and Abetting Fraud Against Defendant Arthur Andersen and the Individual Defendants)

86. Plaintiff realleges and incorporates by reference the foregoing paragraphs as if fully set forth in this Count.

87. This Count is brought against Arthur Andersen and the Individual Defendants.

88. Defendant Arthur Andersen and the Individual Defendants pursued a common plan or design, in conjunction with Qwest and each other, to commit a fraud upon Plaintiff New Jersey and other open market purchasers, by active participation, aid, encouragement, and/or ratification of the fraud alleged in this Complaint, for their own benefit.

89. Defendant Arthur Andersen pursued a common plan or design to commit fraud upon Plaintiff New Jersey by, *inter alia*: assisting Qwest and the Individual Defendants on many aspects of the Company's swaps and revenue reporting, and its expense policies and practices; concealing various financial transactions and revenue policies and practices which artificially inflated the Company's reported results; approving and giving an unqualified opinion upon Qwest's financial statements; and consenting to include its opinions in SEC filings by the Company. The Individual Defendants also participated in, pursued and aided and abetted Qwest in the violations alleged.

90. The acts of Arthur Andersen and the Individual Defendants constitute the active participation, aid, encouragement, or ratification of a common plan or design to commit fraud upon Plaintiff New Jersey, all as alleged in this Complaint.

91. Arthur Andersen's participation, aid, encouragement, and/or ratification of the common plan or design to commit fraud upon Plaintiff was done for Arthur Andersen's benefit. Among other things, Arthur Andersen was motivated to aid and abet the fraudulent misconduct alleged in this pleading to secure substantial compensation from the accounting and auditing services it provided to Qwest. In addition, Arthur Andersen was motivated to aid and

abet defendants' fraudulent practices to protect many millions of additional dollars it received from Qwest for also providing consulting services to the Company.

92. The Individual Defendants' participation, aid, encouragement and/or ratification of the common plan or design to commit fraud upon Plaintiff was done for their benefit, to protect their compensation and emoluments of corporate office, and to protect hundreds of millions of dollars of their profits from insider sales.

93. Plaintiff New Jersey was injured by the violations alleged in this Complaint, which Arthur Andersen and the Individual Defendants aided and abetted. Defendant Arthur Andersen and the Individual Defendants are therefore jointly and severally liable to Plaintiff for any and all damages Plaintiff incurred resulting from the fraud.

COUNT III

(Negligent Misrepresentation Against All Defendants)

94. Plaintiff realleges and incorporates by reference the foregoing paragraphs as if fully set forth in this Count.

95. This Count is brought against all of the defendants.

96. Each of the defendants owed Plaintiff New Jersey a duty to accurately report Qwest's actual financial performance and transactions, by virtue of their roles in the Company, their acts and practices, and their duties to public investors, all as alleged in this Complaint.

97. Each of the defendants breached their duties by at least negligently making incorrect or false statements upon which Plaintiff New Jersey justifiably relied, and which reliance resulted in Plaintiff's economic loss. Defendants' wrongful statements concerned Qwest's financial performance and results, as alleged in this Complaint. By failing to accurately and timely disclose information regarding those transactions and results, the defendants knew or should have known that Plaintiff would be injured.

98. As a direct and proximate result of defendants' breaches, Plaintiff New Jersey acquired and held Qwest's shares at artificially inflated prices and was damaged thereby.

COUNT IV

(Breach of Fiduciary Duty Against Defendant Qwest and the Individual Defendants)

99. Plaintiff realleges and incorporates by reference the foregoing paragraphs as if fully set forth in this Count.

100. This Count is brought against defendants Qwest and the Individual Defendants.

101. Defendants Qwest and the Individual Defendants owed Plaintiff New Jersey a fiduciary duty to accurately and timely disclose the truth concerning the Company's actual financial performance and results. The Individual Defendants owed this duty by virtue of their status and positions as senior officials of Qwest; their transactions in Qwest shares; their statements about the Company; and because of their superior knowledge, information and experience concerning the Company's affairs.

102. Plaintiff New Jersey reasonably reposed trust and confidence in the integrity and fidelity of said defendants' statements and conduct and, in the exercise of due diligence, could not have ascertained the truth until late 2002, at the earliest.

103. As fiduciaries, Qwest and the Individual Defendants owed Plaintiff duties of loyalty, good faith, due care and fair dealing including, *inter alia*: to refrain from misleading Plaintiff regarding the value of Plaintiff's Qwest shares; to refrain from doing any act injurious to Plaintiff, or which would deprive Plaintiff of any profit or advantage; and to not elevate their own financial interests ahead of the interests of Plaintiff and other public investors.

104. Defendant Qwest and the Individual Defendants violated the fiduciary duties they owed to Plaintiff by virtue of the wrongs alleged in this Complaint, and by placing their own financial interests ahead of those of New Jersey, and other open market investors, and above their duties to the public.

105. As a direct and proximate result of said defendants' breaches of their fiduciary duties, Plaintiff acquired and held Qwest's common stock at artificially inflated prices and was damaged thereby.

BASIS OF ALLEGATIONS

106. Plaintiff makes these allegations on information, investigation, and belief, except those pertaining to its own conduct which it makes on knowledge. Plaintiff's information and belief is based upon its investigation which included, *inter alia*, a review of SEC filings, securities analysts' reports and advisories, press releases, media reports, Qwest's admissions to

illegal acts and practices in its own press releases, and pleadings and litigation related to certain of the acts and practices described in this Complaint.

JURY TRIAL DEMAND

Plaintiff demands a trial by jury of all Counts and causes of action so triable.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff State of New Jersey prays for the following relief:

a. that judgment be entered against each of the defendants, jointly and severally, determining that they have committed the violations of law alleged in this Complaint.

b. that defendants, jointly and severally, be ordered to pay Plaintiff's compensatory, consequential, incidental and punitive damages to the full extent legally available, in an amount to be determined at trial;

c. that defendants pay Plaintiff pre-judgment and post-judgment interest, as well as costs and reasonable attorneys' fees, expert witness fees, and other costs as and to the extent permitted by law; and

d. that Plaintiff be awarded such other or different relief as this Court may deem just and proper.

November 27, 2002

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CERTIFICATION PURSUANT TO RULE 4:5-1

The undersigned hereby certifies that the within matter in controversy is not the subject of any other pending or contemplated action or arbitration proceeding and, subject to further discovery, knows of no additional parties who should be joined in this action.

I certify that the foregoing statements made by me are true. I am aware that if any of the foregoing statements made by me are willfully false, I am subject to punishment.

____
Joel H. Sterns

Dated: November 27, 2002

EXHIBIT "A"