

**Complaint for Violation of the Federal Securities Laws (Malone v. Providian Financial Corp., et al., Case No. C-01-21001-JF)**

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UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF CALIFORNIA

MICHAEL F. MALONE, On Behalf of	)	No. C-01-21001-JF
Himself and All Others Similarly	)	
Situated,	)	<u>CLASS ACTION</u>
	)	
Plaintiff,	)	COMPLAINT FOR VIOLATION
	)	OF THE FEDERAL SECURITIES
vs.	)	LAWS
	)	
PROVIDIAN FINANCIAL	)	
CORPORATION, DAVID ALVAREZ,	)	
JAMES ROWE and SHAILESH J.	)	
MEHTA,	)	
	)	
Defendants.	)	<u>DEMAND FOR JURY TRIAL</u>

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1. This is a securities fraud class action on behalf of persons who purchased the publicly traded securities of Providian Financial Corporation ("Providian" or the "Company") between June 6, 2001 and October 11, 2001 (the "Class Period"), against Providian and its CEO, Vice Chairman and CFO, for violations of the federal securities laws arising out of defendants' dissemination of false and misleading statements concerning the Company's operations and prospects for Q2 and Q3 2001. ***In late June 2001, Providian changed the way it processes its bankruptcy filings and thus changed when it recognizes losses and deferred the recognition of approximately \$30 million of charge-offs from June (and Q2 01) into July. Providian manipulated its financial statements for Q2 01 and shaved 40 basis points off its Q2 01 managed net charge-off rate of 10.3% and boosted reported EPS by \$0.06. Without this change, the loss rate would have been 10.7%. This is well above defendants' guidance of 9.5%-10%. Defendants made no mention of this change on the conference call or in Providian's Q2 01 10-Q.*** In fact, management only admitted this change after they came under pressure from analysts following a flood of calls to their investor relations department in late August 2001. During the Class Period, taking advantage of the inflation in Providian stock, defendants Alvarez, Mehta and Rowe dumped almost \$22 million worth of their own Providian stock at artificially inflated prices of as much as \$49.30 per share. These sales were out of line with their prior trading history.

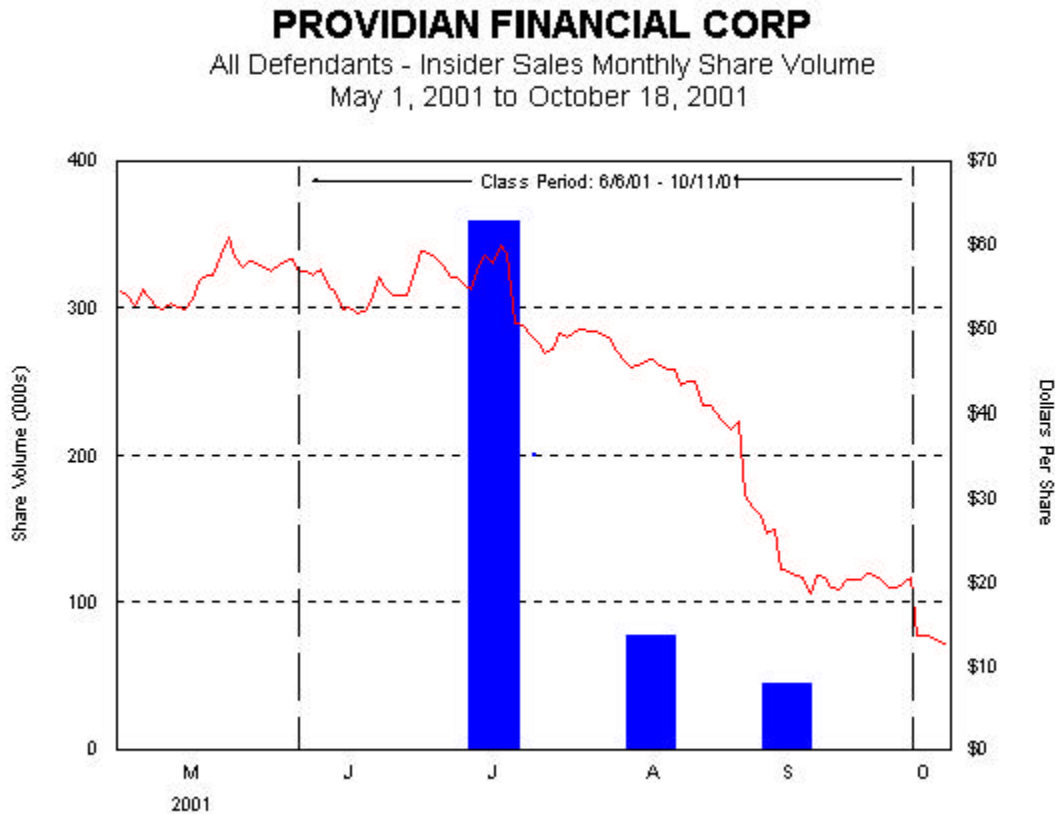
**SUMMARY OF THE ACTION**

2. Providian is a diversified consumer lender. The Company offers a variety of loan products, including credit cards, revolving lines of credit, secured credit cards, and fee-based products. Providian operates in the United States.

3. At the beginning of the Class Period, defendants represented that Providian would have sequential EPS growth as it had in each and every quarter since its inception as a public company. Defendants assured investors that Providian would improve in its Q3. However, defendants actually knew that the quality of Providian's balance sheet was eroding. Throughout June, July and August 2001, defendants repeatedly stated that Providian's Q2 and Q3 01 estimates were easily achievable.

4. In addition to having actual knowledge of the falsity of these statements, defendants had the motive and the opportunity to perpetrate the fraudulent scheme and course of business described herein, in order to sell nearly \$22 million worth of their own Providian shares at prices as high as \$49.30 per share, or 73% higher than the price to which Providian shares dropped as Providian's true prospects began to reach

the market, as depicted in the chart below:



5. As shell-shocked Providian shareholders watched their shares crumble in value to around \$13 per share - down more than 40% from the preceding trading day and more than 75% from the Class Period high of \$59.95 per share - the financial media began to question how defendants could timely sell almost \$22 million worth of their own stock after they had manipulated Providian's quarterly projections and financial results and that Providian would fall seriously short of its forecasted results. Even corporate-friendly news companies like UBS Warburg, Deutsche Banc and ABN Amro were outraged and ran stories following Providian's September 4, 2001 report, including articles questioning the veracity of Providian's statements to its shareholders, and stating:

- "In our view, this change was inadequately disclosed previously. The timing of the change and the poor disclosure surrounding it has further reduced managements' credibility ...." UBS Warburg, September 4, 2001.
- "[G]iven the damage to management credibility, is there a basis in its explanation...?" Deutsche Banc Alex. Brown, September 10, 2001.
- "[Q]uestionable management credibility lead[s] us to continue to avoid this stock ...." ABN Amro, Inc., October 12, 2001.

6. Finally, on October 11, 2001, Providian revealed that, contrary to prior assurances by defendants of

Providian's continuing revenue and EPS growth, including defendants' assurances weeks earlier that Providian would post another quarter of sequential EPS growth, Providian announced that it would post no EPS growth and that its EPS would be only a small fraction of what defendants had led the market to believe, sending Providian's shares into a free fall.

7. This disclosure shocked the market, causing Providian's stock to decline to less than \$13 per share before closing at \$13.45 per share on October 12, 2001, on volume of more than 25 million shares, inflicting billions of dollars of damage on plaintiff and the Class. Defendants' misconduct has wiped out over \$13 billion in market capitalization as Providian stock has fallen over 75% from its Class Period high of over \$59.95 per share as the truth about Providian, its operations and prospects began to reach the market.

### **JURISDICTION AND VENUE**

8. The claims asserted herein arise under §§10(b) and 20(a) of the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. §§78j(b) and 78t(a), and Rule 10b-5. Jurisdiction is conferred by §27 of the 1934 Act, 15 U.S.C. §78aa.

9. Venue is proper here pursuant to §27 of the 1934 Act. Acts and transactions giving rise to the violations of law complained of occurred here.

### **THE PARTIES**

10. Plaintiff Michael F. Malone purchased Providian publicly traded securities as detailed in the attached certification and was damaged thereby.

11. Defendant Providian is a diversified consumer lender. The Company offers a variety of loan products, including credit cards, revolving lines of credit, secured credit cards, and fee-based products. Providian operates in the United States. During the Class Period, Providian had approximately 284 million shares of common stock outstanding, which shares traded in an efficient market on the New York Stock Exchange.

12. Defendant Shailesh J. Mehta ("Mehta") is Chief Executive Officer, President and a director of the Company. During the Class Period, defendant Mehta was in possession of confidential adverse information concerning Providian. Mehta took advantage of his false statements and the artificial inflation caused thereby and sold 75,000 shares of Providian stock at artificially inflated prices as high as \$49.08 per share for proceeds of more than \$3.6 million. Following the revelations discussed herein, Mehta agreed to resign from the Company.

13. Defendant David Alvarez ("Alvarez") is Vice Chairman of the Company. During the Class Period, defendant Alvarez was in possession of confidential adverse information concerning Providian. Alvarez took advantage of his false statements and the artificial inflation caused thereby and sold 395,867 shares of Providian stock at artificially inflated prices as high as \$48.23 per share for proceeds of more than \$17.8 million.

14. Defendant James Rowe ("Rowe") is the Chief Financial Officer of the Company. During the Class Period, defendant Rowe was in possession of confidential adverse information concerning Providian. Rowe took advantage of his false statements and the artificial inflation caused thereby and sold 10,000 shares of Providian stock at artificially inflated prices as high as \$49.30 per share for proceeds of \$493,000.

15. Defendants are liable for the false statements pleaded herein at ¶¶29 and 32, as those statements were each "group-published" information for which they are responsible. Defendants Alvarez, Mehta and Rowe (the "Individual Defendants"), by reason of their stock ownership and positions with Providian as Vice Chairman, CEO and CFO, were controlling persons of Providian. Providian in turn controlled the Individual Defendants. The Individual Defendants and Providian are liable under §20(a) of the 1934 Act.

### **BACKGROUND, SCIENTER, SCHEME ALLEGATIONS**

16. Providian is a diversified consumer lender. The Company offers a variety of loan products, including credit cards, revolving lines of credit, secured credit cards, and fee-based products. Providian operates in the United States.

17. Defendants are Providian's President and CEO, Vice Chairman, and Chief Financial Officer. They ran Providian as a "hands-on" managers, dealing with important issues facing Providian's business, *i.e.*, its customer base, and the eroding value of its receivables and its need to increase reserves, Providian's market share position, and its ability to achieve growth in its business in fiscal 2001 in light of the dramatic adverse developments which had been affecting Providian's core customers since Q1 01.

18. By late May 2001, problems with Providian's receivables had reached crisis proportions. Defendants also knew, from their frequent conversations with management of their Pleasanton, California servicing facilities and other Providian employees, that Providian's ability to achieve Q2 projections was dubious at best and its ability to hit Q3 projections was a fallacy.

19. Thus, on June 1, 2001, Providian's top officers knew Providian faced increasingly bleak short-term and long-term prospects. Nevertheless, defendants wanted to sell their shares before the truth began to be revealed about Providian's true prospects. Thus, defendants disseminated false information about Providian's business and prospects by secretly manipulating the manner in which Providian recognizes losses associated with bankruptcies. ***Historically, Providian would recognize bankruptcies upon notification.*** This was and is the standard methodology used in the industry. Providian's competitors, including Capital One and Metris, use the same methodology.

20. In mid-June 2001, defendants were scrambling to find ways to meet their projected Q2 results. ***Unbeknownst to Providian shareholders, on June 18, 2001, the Company changed the way it processes bankruptcy filings, moving from "daily processing" to "batch processing," essentially collecting two weeks' worth of bankruptcy filings and then recognizing those losses.*** Previously, PVN had recognized these filings and the related losses daily. Of concern, ***this change had the impact of pushing losses out of June (and Q2 01) and into July.*** As such, the Q2 01 managed NCO rate of 10.3% was ***understated*** (and manipulated downward) by this move, and would have been 10.7% had this change not taken place. The change affected the entire portfolio, not just the securitized portion. Moreover, this had an effect of overstating Q2 EPS by \$0.06.

21. Defendants were personally familiar with Q2 and Q3 01 revenues as they monitored Providian's sales, closely monitoring the performance of Providian's operations via reports from Providian's Finance Department, which were generated and provided to Alvarez, Rowe and Mehta on a regular basis. The reports summarized orders, dollar volume, buyer name, credit terms, and product type. As a result of their monitoring, defendants were aware that Providian would be unable to meet its projected results, as its core business was slowing and its customers were becoming less and less creditworthy in light of the dramatic adverse developments of the United States economy in Q1 01 and mid-Q2 01. However,

because the "appearance" of future sequential EPS growth was so critical to defendants' plan to inflate the price of Providian shares, defendants continued to maintain throughout the Class Period that Providian would post Q2 EPS of at least \$0.79 and Q3 EPS of \$0.83, when, in reality, defendants knew that Providian could not possibly achieve such performance.

22. In addition to having actual knowledge of the falsity of their statements, defendants had the motive and the opportunity to perpetrate the fraudulent scheme and course of business described herein, in order to sell nearly \$22 million worth of their Providian shares at prices as high as \$49.30 per share, or 73% higher than the price to which Providian shares dropped at the end of the Class Period, as Providian's true prospects began to reach the market.

23. Thus, at the time Providian reported its Q2 01 results, it faced increasingly bleak short-term and long-term prospects. Nevertheless, defendants wanted to sell their shares before the truth began to be revealed about Providian's true prospects. Thus, defendants disseminated false information about Providian's business and prospects, concealing the fact that even in May 2001 defendants were seeing an erosion of Providian's balance sheet and the need to increase reserves.

24. Moreover, defendants also knew that they would be unable to show any sequential earnings growth in Q2 or Q3. Defendants knew that Providian's inability to post sequential growth would devastate Providian's share price and their ability to profit from their Providian shares. As depicted below, Providian had reported sequential EPS growth each and every quarter during its existence as a public company:

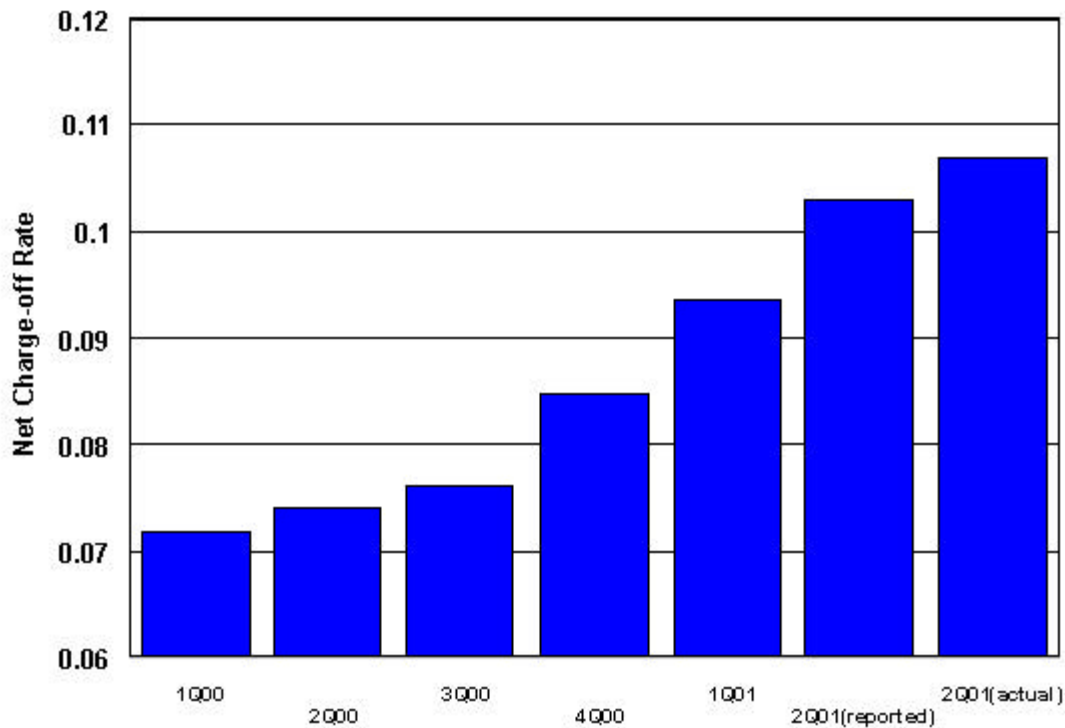
**PROVIDIAN'S HISTORICAL EPS**

<b>Year</b>	<b>Q1-March</b>	<b>Q2-June</b>	<b>Q3-September</b>	<b>Q4-December</b>
2001	.78	.79	<b>.83*</b>	
2000	.60	.65	.68	.80
1999	.39	.44	.52	.55
1998	.20	.22	.29	.33
1997	.15	.16	.17	.19

\*Class Period Company projections

25. Defendants were also keenly aware that their ability to achieve Q2 EPS of \$.79 was contingent upon their ability to manipulate the charge-off rates for Providian. The charge-off rate has been rising in past quarters and was coming close to the threshold of 10% which was of great concern to defendants and alarming Providian shareholders.

## Net Charge-Off Rate For Providian



### FALSE AND MISLEADING STATEMENTS DURING THE CLASS PERIOD

26. On June 5, 2001 and June 6, 2001, Providian executives held investor meetings and offered tours of their servicing facilities in Pleasanton, California. In a formal presentation and in break-out sessions at the Pleasanton facilities, they told the assembled analysts, money and portfolio managers and institutional investors that:

- The Company would easily achieve Q2 and Q3 EPS of \$0.79 and \$0.83, respectively.
- "Charge-offs" would decline in Q3 and would hit 10% in Q2 01.
- The quality of Providian's portfolio was improving.
- The Company was then experiencing lower delinquency rates.

27. On July 6, 2001, J.P. Morgan issued a report on Providian by Michael Freudenstein. It was issued only after Freudenstein had extensive discussions with Mehta and Rowe and forecast Q2 01 EPS of \$0.79. It also stated:

- The Company's net charge-off ratio for Q2 01 was 10%.

- The Company "***charges off bankrupt accounts upon notification.***"

28. On July 19, 2001, subsequent to the release of its Q2 01 results, Providian held a conference call for analysts, money and portfolio managers, institutional investors and large Providian shareholders to discuss Providian's Q2 results, its business and prospects. The Company reported Q2 EPS of \$0.79. During the call - and in follow-up conversations with analysts - Mehta and Rowe stated:

- The Company's loss ratio was 10.29% and would "decline" in its Q3 01.
- That despite consistently adding to reserves in prior quarters, the Company did not need to in Q2 01.
- The Company would report Q3 01 EPS of \$0.83.
- The Company's process for charging off bankrupt accounts remained unchanged.

29. On July 19, 2001, Providian announced 23% earnings per share growth in the Q2 01, in a press release which stated in part:

Providian Financial Corporation today announced 24% net income growth resulting in a 23% earnings per share growth for the second quarter of 2001. Earnings totaled \$232.4 million, or \$0.79 per diluted share, compared to earnings of \$187.6 million, or \$0.64 per diluted share, for the second quarter of 2000, before one-time adjustments.

During the second quarter, total customer accounts grew to 17.7 million, a 27% increase over the end of the second quarter of 2000, driven by new account originations and continued strong customer retention. Total managed credit card loans increased by \$2.1 billion during the quarter to \$30.5 billion, a 39% increase over the end of the second quarter of 2000.

***"We are pleased with our continued growth and strengthening of our consumer franchise, which enables us to deliver consistent returns to our shareholders,"*** said Shailesh Mehta, chairman and chief executive officer....

Total managed revenue, comprised of managed net interest income and non-interest income, climbed to \$1.76 billion in the second quarter of 2001, a 29% increase over the second quarter of 2000, before one-time adjustments. In the second quarter, managed net interest income was \$962.2 million and managed non-interest income was \$802.4 million, an increase of 40% and 18%, respectively, over the second quarter of 2000, before one-time adjustments. The managed net interest margin on loans rose to 13.13% in the second quarter of 2001 from 12.77% in the first quarter of 2001.

***Consistent with the Company's expectations for the seasoning of the portfolio and the rise in year-to-date consumer bankruptcies, the managed net credit loss rate in the second quarter was 10.29% versus 9.34% in the first quarter of 2001.*** The 30+ day managed delinquency rate was 8.04% at quarter end, a slight increase from 7.64% at the end of the first quarter of 2001. Based on the trend in the 90+ day delinquency rate the Company continues to expect an improved credit loss rate in the third quarter 2001. The Company's loan loss reserves totaled \$1.53 billion at the end of the second quarter, representing 10.55%

of reported loans.

The Company's non-interest expense for the second quarter was \$621.6 million, leading to an improvement in the efficiency ratio to 35% for the quarter from 37% in the second quarter of 2000, before one-time adjustments, despite absorbing higher collection costs. The efficiency ratio improvement was driven in part by continued cost savings from the integration of the Company's credit card platforms.

The Company's return on managed assets was 2.71% and return on equity was 40.08% for the second quarter. The Company ended the quarter with a strong balance sheet, with capital and loan loss reserves totaling \$4.1 billion, which represented 19.5% of reported assets and 11.3% of managed assets at quarter end.

***"Our financial results for the quarter demonstrate the strength of our adaptive business model. Despite the more challenging economic environment, we continue to deliver strong top-line growth and industry leading returns on assets and equity,"*** said David Petrini, vice chairman. ***"As we look out to the balance of the year, we are well positioned to continue to produce solid returns while maintaining our leadership position in customer satisfaction."***

30. On July 20, 2001, Lehman Brothers issued a report on Providian by Bruce Harting, which was based on and repeated information provided in the July 19, 2001 conference call and in follow-up conversations with Providian's executives. The report stated:

Despite reporting a chargeoff rate above 10% in Q2, the credit performance of the company's portfolio is generally in line with expectations, reflecting recent growth and normal seasoning. Higher than initially expected bankruptcy filings (and related chargeoffs) and some variance in portfolio growth accounted for the loss rate being 10%. ***Providian receives electronic notification of bankruptcy filings and charges off those accounts almost immediately after receiving notification. July bankruptcy trends have been more favorable than during the second quarter which should have a positive impact on losses if this trend continues throughout the third quarter.*** Higher 30 day delinquencies at the end of the second quarter are the basis for the expected fourth quarter increase in the chargeoff rate. The drop in the 90 day delinquencies in Q2 makes management confident about predicting a decline in loss rates in Q3.

31. Before July 23, 2001, defendants knew that they would be unable to show sequential earnings growth in Providian's Q3. This would be the first time ever as a public company that Providian would report a declining sequential quarter in EPS growth. In fact, as depicted below, for the past five years, Providian has ***never*** had a declining sequential quarter:

### **PROVIDIAN'S HISTORICAL EPS**

Year	Q1-March	Q2-June	Q3-September	Q4-December
2001	.78	.79	<b>.83*</b>	
2000	.60	.65	.68	.80
1999	.39	.44	.52	.55
1998	.20	.22	.29	.33
1997	.15	.16	.17	.19

\*Class Period Company projections

Defendants knew that Providian's inability to post sequential growth would devastate Providian's share price and their ability to profit from their shares. Defendants saw this as an opportunity to engage in a massive selling spree wherein defendants sought to and did reap tens of millions of dollars in illegal insider trading proceeds.

32. On September 4, 2001, prior to the opening of the market and following repeated calls to corporate offices concerning rumors about the Company's Q2 financial results, the Company issued a press release entitled, "Providian Financial Revises Earnings Guidance." The press release stated in part:

Providian Financial Corporation today announced that it is revising its 2001 earnings guidance to \$3.20 to \$3.25 per diluted share, representing a 17% to 19% increase over 2000 earnings per share before one-time adjustments. In revising its guidance, the Company cited a recent slowdown in customer purchase activity, softer loan demand relative to expectations, and ongoing credit tightening by the Company. In light of these factors, the Company is planning for lower managed loan growth in the range of 29% to 31% for 2001.

*In the third quarter, the Company expects to report earnings per diluted share of \$0.82 to \$0.84 and an improvement in its managed net credit loss rate to below the second quarter rate of 10.29%.* At the currently expected loan growth levels, it is likely that the fourth quarter managed net credit loss rate will be between 10.45% and 10.75%. The Company's anticipated loan growth and mix will likely result in the managed net credit loss rate for 2002 remaining at or above the fourth quarter 2001 level. The Company plans to add \$50 to \$75 million to its loan loss reserve during the balance of 2001.

*"Providian remains highly profitable with solid returns on assets and equity and a very strong balance sheet,"* said Shailesh J. Mehta, chairman and chief executive officer. "Even though we expect to maintain industry leading profitability per account, based on our growing scale and our objective of optimizing the balance between risk and growth, we believe 15% earnings per share growth is an appropriate long-term goal. While it is too early to have a refined view of 2002, it is expected that earnings per share performance will be lower than our long-term goal."

\* \* \*

*The Company also commented on the change made to the process for recognizing charge-offs resulting from consumer bankruptcies. For improved operational efficiency, the Company now batches electronic bankruptcy notifications and charges off the related amounts once per month. The change resulted in a portion of bankruptcies, for which notification was received on or after June 18, 2001, being charged off in July. Because*

***the Company's loan loss reserves provided for estimated bankruptcies received but not yet charged-off, the change had no impact on second quarter earnings.*** For the quarter ended June 30, 2001, adjusting for the processing change, the managed net credit loss rate of 10.29% and the managed 30+ day delinquency rate of 8.04% were 10.63% and 7.99%, respectively.

33. Subsequent to its September 4, 2001 press release, where ***Providian admitted the change in its recognition of bankruptcy losses***, analysts, money and portfolio managers, institutional investors and large Providian shareholders dumped Providian shares and expressed outrage over the hidden change in Providian's policy and subsequent insider trading, repeatedly calling into question "management credibility":

- "In our view, this change was inadequately disclosed previously. The timing of the change and the poor disclosure surrounding it has further reduced managements' credibility ...." UBS Warburg, September 4, 2001.
- "[G]iven the damage to management credibility, is there basis in its explanation ...?" Deutsche Banc Alex. Brown, September 10, 2001.
- "[Q]uestionable management credibility lead[s] us to continue to avoid this stock ...." ABN Amro, Inc., October 12, 2001.

34. On September 7, 2001, defendants (Mehta, Alvarez and Rowe) met with representatives of Deutsche Banc Alex. Brown (including Mark Alpert) at Providian's San Francisco headquarters, where they admitted that they should have been open and up-front about the change in bankruptcy policy. However, defendants maintained that they would achieve Q3 EPS of \$0.83.

35. On October 11, 2001, after the close of the market, Providian announced preliminary Q3 results. The press release stated in part:

***Providian Financial Corporation today reported it expects third quarter earnings to be lower than previous guidance of \$0.82 to \$0.84 per diluted share.*** The Company cited three primary factors: actions to strengthen the balance sheet in anticipation of continued weak credit conditions, lower than expected fee and finance charge revenue in September, and higher than expected credit losses in September. Actions to strengthen the balance sheet include an incremental loan loss provision of approximately \$186 million and a charge of approximately \$85 million to recognize the estimated uncollectible portion of accrued finance charges, and to increase the estimate of uncollectible fees, on accounts which are 90+ days delinquent. Previously, these finance charges and fees were reversed against current revenue upon charge-off of the related account. The results also include a \$23 million gain from the early extinguishment of debt. ***Based on preliminary numbers, the Company now expects earnings to be in the range of \$0.19 to \$0.21 per diluted share. The managed net credit loss rate is expected to be approximately 10.33% for the quarter.***

The Company will announce its third quarter results and revised guidance for the fourth quarter on October 18th after the close of the market. Until that release, the Company does not plan to provide further updates.

36. Each of the statements made between June 6, 2001 and October 11, 2001, were false or misleading

when issued. The true but concealed facts were:

(a) The Company's net charge-off rate for Q2 01 was materially understated and actually false. In fact, the actual net charge-off rate was 10.7%, not 10.29% as reported;

(b) It was impossible for charge-offs to *decline* in Providian's Q3 as the Company had already secretly pushed 12 days of charge-offs into the Company's Q3 and the Company was seeing growth in the rate of its customers filing bankruptcy;

(c) The Company's asset quality trends were eroding and required that the Company increase its reserves. By failing to properly increase its reserves, Providian's assets were inflated in Q2 and its projections for Q3 were false;

(d) The Company's reported EPS for its Q2 01 was false. In fact, by manipulating the process of its bankruptcy filings, the Company deferred the recognition of approximately \$30 million of charge-offs from June (and Q2 01, into July (or Q3 01)), which in turn shaved 40 basis points off its 10.29% charge-off rate *and* artificially inflated its Q2 01 EPS by \$0.06; and

(e) As a result of (a)-(d) above, it was impossible for defendants to legitimately achieve Q2 and Q3 EPS of \$0.79 and \$0.83, respectively.

### FALSE FINANCIAL STATEMENTS

37. In order to overstate its earnings in 2001, Providian violated GAAP and SEC rules by failing to properly report the change in its bankruptcy policy which, unbeknownst to the public, Providian changed on June 18, 2001.

38. Providian reported the following financial results for 2001:

	Reported <u>6/30/01</u>	<u>Amount of Overstatement</u>	<u>Amount of Understatement</u>
EPS	\$0.79	\$0.06	
Charge-Off Rate	10.29%		40 bps

Providian included these "reported" results in a press release and Form 10-Q filed with the SEC.

39. These financial statements and the statements about them were false and misleading, as such financial information was not prepared in conformity with GAAP, nor was the financial information a fair presentation of the Company's operations due to the Company's improper accounting for its investment in Providian, in violation of GAAP and SEC rules. As depicted below, Providian's bankruptcy recognition was "secretly" changed, and was therefore not properly accounted for. In late June 2001, Providian changed the way it processes its bankruptcy filings and thus changed when it recognizes losses and deferred the recognition of approximately \$30 million of charge-offs from June (and Q2 01) into July. Providian manipulated its financial statements for Q2 01 and shaved 40 basis points off its Q2 01 managed net charge-off rate of 10.3% and boosted reported EPS by \$0.06. Without this change, the loss rate would have been 10.7%. This is well above defendants' guidance of 9.5%-10%. Defendants made no mention of this change on the conference call or in the Q2 01 10-Q.

40. GAAP are those principles recognized by the accounting profession as the conventions, rules and procedures necessary to define accepted accounting practice at a particular time. Regulation S-X (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. Regulation S-X requires that interim financial statements must also comply with GAAP, with the exception that interim financial statements need not include disclosure which would be duplicative of disclosures accompanying annual financial statements. 17 C.F.R. §210.10-01(a).

41. Providian ultimately admitted in a press release responding to the rumors that, in fact, *it changed its bankruptcy policy 12 days prior to the end of Q2 01.*

42. Due to these accounting improprieties, the Company presented its financial results and statements in a manner which violated GAAP, including the following fundamental accounting principles:

(a) The principle that interim financial reporting should be based upon the same accounting principles and practices used to prepare annual financial statements was violated (APB No. 28, ¶10);

(b) The principle 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 was violated (FASB Statement of Concepts No. 1, ¶34);

(c) The principle 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 was violated (FASB Statement of Concepts No. 1, ¶40);

(d) The principle 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 was violated. 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) The principle that financial reporting should provide information about an enterprise's financial performance during a period was violated. 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) The principle that financial reporting should be reliable in that it represents what it purports to represent was violated. That information should be reliable as well as relevant is a notion that is central to accounting (FASB Statement of Concepts No. 2, ¶¶58-59);

(g) The principle of completeness, which means that nothing is left out of the information that may be necessary to insure that it validly represents underlying events and conditions was violated (FASB Statement of Concepts No. 2, ¶79); and

(h) The principle 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 was violated. 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).

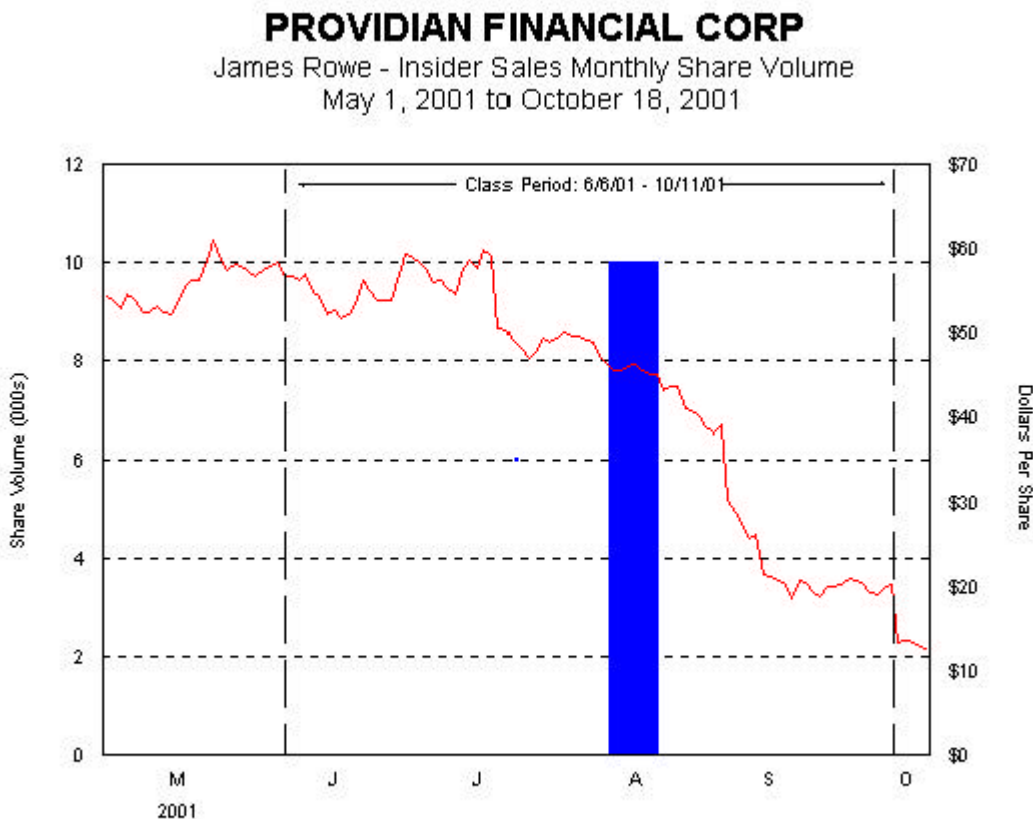
43. Further, the undisclosed adverse information concealed by defendants during the Class Period is the type of information which, because of SEC regulations, regulations of the national stock exchanges and customary business practice, is expected by investors and securities analysts to be disclosed and is known by corporate officials and their legal and financial advisors to be the type of information which is expected to be and must be disclosed.

### DEFENDANTS' INSIDER TRADING

44. During the Class Period, defendants Alvarez, Mehta and Rowe sold 395,867, 75,000 and 10,000 shares of their Providian stock for proceeds of \$17.8 million, \$3.6 million and \$493,000, respectively, despite their possession of adverse information about Providian's business which they knew had not been disclosed to the public.

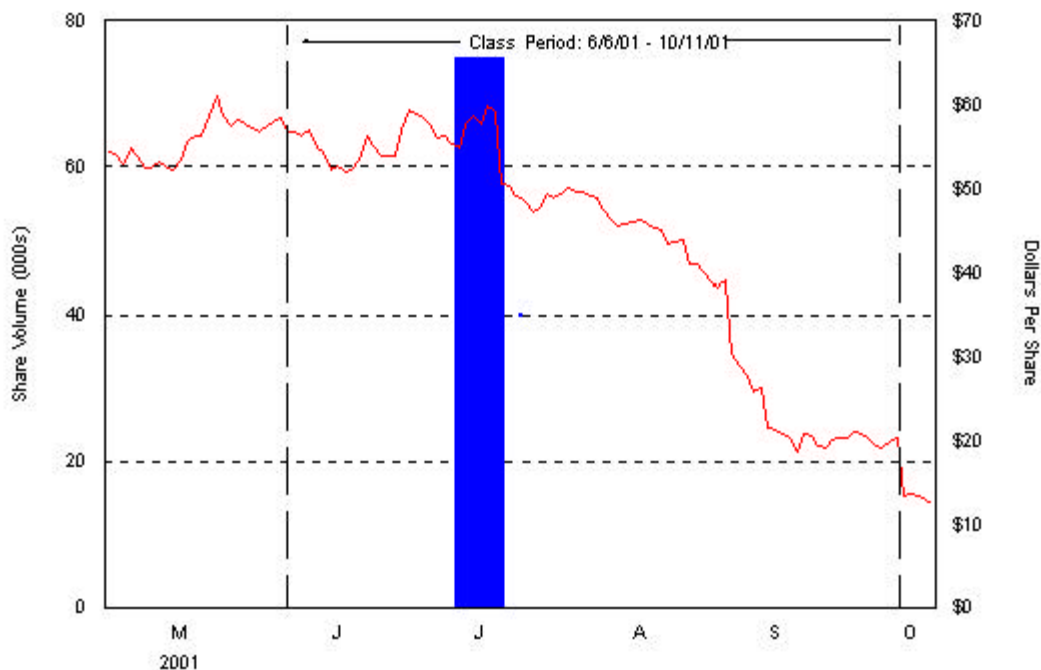
45. Defendants' insider sales during the Class Period were highly suspicious given their proximity to the date of the bad news and the fact that they occurred before the stock had dropped and while defendants were making positive statements.

46. As depicted in the chart below, defendants' stock sales were suspicious in timing and amount. Moreover, the amount of shares sold dwarfed any other sale in recent history with the Company:



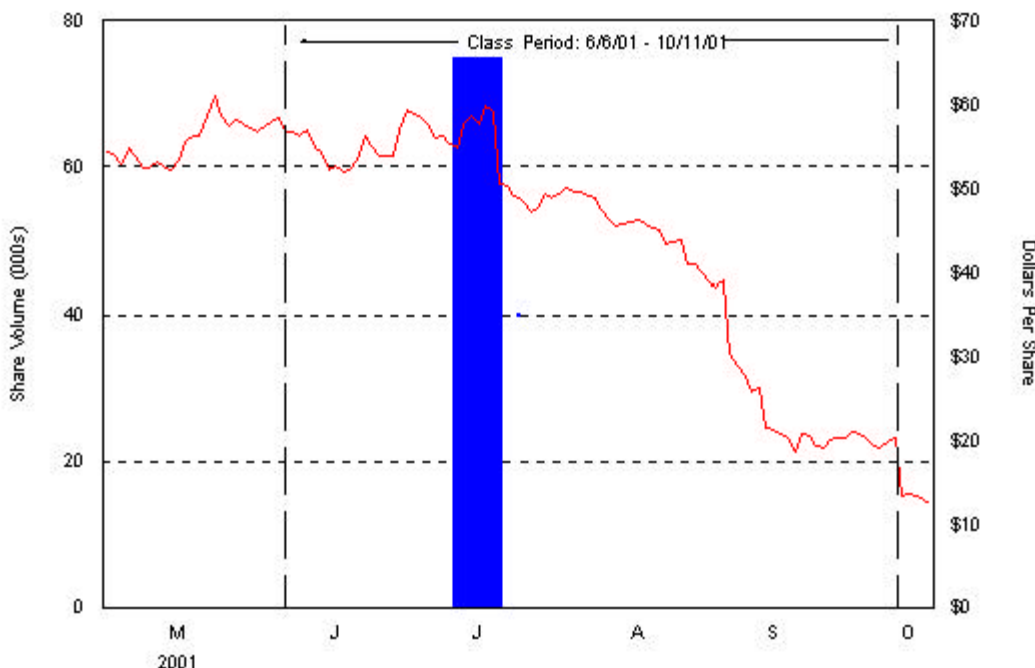
# PROVIDIAN FINANCIAL CORP

Shailesh J. Mehta - Insider Sales Monthly Share Volume  
May 1, 2001 to October 18, 2001



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### CLASS ACTION ALLEGATIONS

47. This is a class action on behalf of purchasers of Providian publicly traded securities between June 6, 2001 and October 11, 2001, excluding defendants (the "Class"). Excluded from the Class are officers and directors of the Company, as well as their families and the families of the defendants. Class members are so numerous that joinder of them is impracticable.

48. Common questions of law and fact predominate and include whether defendants: (i) violated the 1934 Act; (ii) omitted and/or misrepresented material facts; (iii) knew or recklessly disregarded that their statements were false; and (iv) artificially inflated the prices of Providian's publicly traded securities and the extent of and appropriate measure of damages.

49. Plaintiff's claims are typical of those of the Class. Prosecution of individual actions would create a risk of inconsistent adjudications. Plaintiff will adequately protect the interests of the Class. A class action is superior to other available methods for the fair and efficient adjudication of this controversy.

### CLAIM FOR RELIEF

50. Defendants violated §10(b) and Rule 10b-5 by:

(a) Employing devices, schemes and artifices to defraud;

(b) Making untrue statements of material facts and omitting to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and

(c) Engaging in acts, practices and a course of business that operated as a fraud or deceit upon the Class in connection with their purchases of Providian publicly traded securities.

51. Class members were damaged as they paid artificially inflated prices for Providian's publicly traded securities in reliance on the integrity of the market.

### **PRAYER FOR RELIEF**

WHEREFORE, plaintiff, on behalf of himself and the Class, prays for judgment as follows:

A. Declaring this action to be a class action properly maintained pursuant to Rule 23 of the Federal Rules of Civil Procedure;

B. Awarding plaintiff and other members of the Class damages together with interest thereon;

C. Awarding plaintiff and other members of the Class costs and expenses of this litigation, including reasonable attorneys' fees, accountants' fees and experts' fees and other costs and disbursements; and

D. Awarding plaintiff and other members of the Class such equitable/injunctive or other and further relief as may be just and proper under the circumstances.

### **JURY DEMAND**

Plaintiff demands a trial by jury.

DATED: October 23, 2001

MILBERG WEISS BERSHAD  
HYNES & LERACH LLP  
REED R. KATHREIN

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Attorneys for Plaintiff

**CERTIFICATION OF INTERESTED ENTITIES OR PERSONS**

Pursuant to Civil L.R. 3-16, the undersigned certifies that as of this date, other than the named parties, there is no such interest to report.

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ATTORNEY OF RECORD FOR  
PLAINTIFF MICHAEL F. MALONE