United States Courts
Southern District of Texas
ENTERED

SEP 17 2002

Michael N. Milby, Clerk

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

MARK NEWBY, Plaintiff, VS. ENRON CORPORATIOIN, *et al.*, Defendants.	CIVIL ACTION NO. H-01-3624 (Consolidated Securities Cases)
TITTLE, *et al.*, Plaintiffs, VS ENRON CORPORATION, *et al.*, Defendants.	CIVIL ACTION NO. H-01-3913 (Consolidated ERISA Cases)

MEMORANDUM AND ORDER

Pending before the Court are the following motions filed before the appointment of lead plaintiff and lead counsel, and before the filing of the Consolidated Complaint:

(1) Various motions for limited reconsideration of the Court's Order of January 8, 2002 regarding the Court's authority to order a prejudgment restraint of defendants' assets (Instruments Nos. 257, 261, 266);

(2) Two motions to lift the discovery stay to allow particularized expedited discovery in aid of plaintiffs' motion to freeze the individual defendants' alleged insider trading proceeds (Instruments Nos. 180 and 251);

1031

(3) A motion to lift the discovery stay to allow particularized expedited discovery from certain Enron executives regarding document preservation (Instrument No. 259).

(4) Motion of the *Tittle, Rinard* and *Kemper* Plaintiffs for a Prelminary Order Freezing and Imposing a Constructive Trust Over Individual Defendants' Assets and Limited Expedited Discovery Into Those Assets (Instrument No. 292 in *Newby* and No. 77 in *Tittle*).

LIMITED RECONSIDERATION

A number of defendants have moved for reconsideration of the order of the Honorable Lee H. Rosenthal entered January 8, 2002 (Instrument No. 111) finding authority in this Court to order a prejudgment restraint of defendants' assets in the proper circumstance. Much of the briefing is a repetition of the argument made to Judge Rosenthal. On February 19, 2002 defendant Rebecca Mark-Jusbasche filed a response in support of the motions for reconsideration in which she brought to the Court's attention a new Supreme Court case, *Great-West Life & Annuity Ins. Co. v. Knudson, et al.*, No. 99-1786, slip op.–January 8, 2002, 534 U.S. ___, 122 S.Ct. 708 (2002). Defendant argues that the reasoning in the *Great-West* case makes clear that the extraordinary pre-judgment equitable remedies sought by the securities plaintiffs in the *Newby* case are unavailable. The Court has re-read Judge Rosenthal's order in light of the *Great-West* case and the other cases cited by Judge Rosenthal. Although *Great-West* sheds a great deal of light on the distinction between equitable restitution and legal restitution, it is inapplicable to these Enron cases because plaintiffs here are seeking the equitable remedies of constructive trust and an equitable accounting for profits of specific assets, the proceeds of alleged insider trading. Having reconsidered Judge Rosenthal's order of January 8, 2002, the Court believes that its reasoning is correct.

LIFTING OF DISCOVERY STAY

In Judge Rosenthal's order of January 8, 2002 she found that a district court has the power to freeze assets, pre-judgment, under some circumstances, but she denied Amalgamated Bank's (Amalgamated) motion for a temporary restraining order to freeze the proceeds derived from the sales, from October 19, 1998 to November 27, 2001, of Enron securities by twenty-nine defendants, current and former officers and directors of Enron Corporation. She found there was insufficient evidence to "distinguish among the defendants on the basis of their involvement in the alleged securities violations, their trades, or their present or future risk of asset concealment or dissipation." (Instrument No. 111, at 40). Nor, Judge Rosenthal found, did "the pleadings and submissions distinguish among the individual defendants on the basis of their current activities or present or future risk of asset concealment or dissipation." (Instrument No. 111, at 40). She further found lacking in the record "the necessary showing that the individual defendants will remove the assets from the reach of the plaintiffs, so as to cause irreparable injury absent an asset freeze." (Instrument No. 111, at 40).

Judge Rosenthal also found that the Private Securities Litigation Reform Act of 1995 (PSLRA) stayed all discovery in the case "until the Court has determined the sufficiency of the Plaintiff's pleadings, unless the Plaintiff can establish one of the exceptions." (Instrument No. 111, at 43).[1] At the conclusion of her order Judge Rosenthal addressed the request of Amalgamated that

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[1]The Act provides an exception to the discovery stay where undue prejudice would result or evidence would be lost:

> (B) Stay of discovery. In any private action arising under this title, all discovery and other proceedings shall be stayed during the pendency of any motion to dismiss, unless the court finds upon the motion of any party that particularized discovery is necessary to preserve evidence or to prevent undue prejudice to that party.

it be given "the opportunity to brief whether, and to what extent, it is entitled to such discovery as to the individual defendants, particularly as to the officers allegedly liable as control persons, Kenneth Lay, Jeffrey Skilling, and Andrew Fastow." (Instrument No. 111, at 43-44). Judge Rosenthal granted that request and ordered Amalgamated to file a brief "explaining what discovery is requested and why the request should be granted. . . ." (Instrument No. 111, at 44).

On January 28, 2002 Amalgamated filed its Supplemental Brief in Response to the Court's January 8, 2002 Memorandum and Order. (Instrument No. 180) In this filing Amalgamated seeks a lift of the discovery stay imposed by the PSLRA to conduct particularized discovery of various current or former Enron officers and directors alleged to have engaged in insider trading in order to determine whether there is evidence that the proceeds of those alleged trades have been dissipated or concealed.[2] Defendants are adamantly opposed to discovery and to the particular discovery proposed by the plaintiffs because it is too broad and not limited to the matters sought to be proved.

Amalgamated relies in this filing upon two circumstances. First, it relies upon its allegations that the various defendants from whom discovery is sought were inside traders who reaped vast gains from those trades. Next, it alleges that Enron Corporation utilized a multitude of partnerships and offshore entities and accounts to keep secret from regulators and the public the Corporation's true financial situation. From these two sets of allegations Amalgamated concludes that particularized discovery of the past and current financial positions of the twenty-nine defendants

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15 U.S.C. Sec. 78u-4(b)(3)(B).

[2]In exhibits 9 and 10 to Instrument No. 180, Amalgamated poses Requests for Production of Documents and Interrogatories, respectively, to twenty-nine defendants.

is necessary in order to prevent the dissipation and secreting of their assets to the detriment of the plaintiffs in the case.

In response defendants point out that the discovery sought is not necessary to prevent undue prejudice and it is not particularized. Lay, in his response filed February 8, 2002, argues that "if Amalgamated is allowed to conduct the discovery it wants and to continue these injunction proceedings, it will succeed in turning the PSLRA on its head." (Instrument No. 256, at 2) This is because Amalgamated will be allowed to take both merits and post-judgment discovery before the Court has tested the adequacy of the pleadings. Lay argues on his own behalf, but his arguments are applicable to any one of the twenty-nine defendants, and is echoed by many of them in their own responses, that Amalgamated's request for discovery is based on the speculation that Lay and the others might try to conceal assets in which the putative class members may be able to demonstrate they have an interest. Lay points out further that the discovery into his and his family's financial affairs would not be available, prior to judgment, in an ordinary lawsuit, one that did not have a Congressionally mandated discovery stay. A review of the proposed request for production of documents and interrogatories reveals that Lay's description of the discovery in his response (Instrument No. 256, at 2) as "extraordinarily board and intrusive" is not mere hyperbole. It is not narrowly targeted; it does not limit the discovery to documents or information relating to the alleged secretion of assets, but seeks production of documents from the defendants relating to all compensation received from any source for two and one-half years, transactions in Enron stock, and interests in any entity outside Enron. The discovery also seeks from the twenty-nine defendants tax returns during the last four years and the identities of legal, tax, and financial professionals utilized by the defendants during the last eleven years.

On February 7, 2002 the newly appointed lead plaintiff, Regents of the University of California (Regents) and Amalgamated filed a Second Supplemental Brief in Response to the Court's January 8, 2002 Memorandum and Order Concerning Particularized Discovery (Instrument No. 251) that supplemented the January 25, 2002 filing (Instrument No. 180). In this pleading Regents and Amalgamated relied upon the text of a television interview of the wife of Kenneth Lay in which Mrs. Lay made a number of statements concerning the state of the Lay finances, particularly that they were attempting to liquidate all their holdings and that they were close to bankruptcy. Regents and Amalgamated also pointed out that there were contradictions between Mrs. Lay's statements to the media and the public record of the Lay assets. These arguments were also made in briefs filed by Staro Asset Management, LLC (Instrument No. 235) and Davidson Group (Instrument No. 239).

Mrs. Lay's hearsay statements, press coverage, and the public record concerning the Lay assets do not transform what Judge Rosenthal found to be speculation into a "basis for concluding that each or any defendant is attempting to dissipate or conceal the profits gained from trading Enron stock in the Class Period, so as to make them uncollectible in the event of an award of the equitable relief Amalgamated seeks." (Instrument No 111, at 39). The briefing filed by the plaintiffs on this issue does not form an adequate basis for lifting the discovery stay as to Lay and the twenty-eight other current and former officer and director defendants so that plaintiff can discover the details of their finances. Accordingly, the motions to lift the stay will be denied.

On February 8, 2002 Amalgamated and Regents filed a Notice of Motion and Motion for an Order Granting Particularized Expedited Discovery From Enron Executives (Instrument No. 259) and a Memorandum in Support (Instrument No. 260). In this briefing plaintiffs move for a lift

of the automatic stay in order to "seek particularized discovery from certain officers and executives who are knowledgeable about the destruction of evidence at Enron." (Instrument No. 260, at 3). Specifically, plaintiffs ask for depositions and documents from eight current or former executives, including Lay, "who likely were in charge of those persons responsible for ensuring that documents would be preserved pursuant to the PSLRA, or conversely, for destroying documents in the Enron departments of which plaintiffs are aware." (Instrument No. 260, at 10).

At a hearing on January 22, 2002, counsel for Regents and Amalgamated brought into the courtroom a box of what they represented to be shredded Enron documents. At the same hearing, in response to this representation, counsel for Enron informed the court that FBI personnel had been sent to the Enron building to secure Enron's documents and to conduct an investigation into document destruction. Transcript of Injunction Hearing, January 22, 2002, at 61. At a January 30, 2002 hearing counsel for Enron also brought to the Court's attention an order of the Bankruptcy Court signed on January 25, 2002 that enjoined Enron and its employees from destroying documents. Transcript of Motion Hearing, January 30, 2002, at 37.

In light of these developments concerning Enron documents, lifting the automatic stay for discovery from the eight executives concerning their alleged involvement in or knowledge of past document destruction, would not prevent undue prejudice or preserve relevant evidence. 15 U.S.C. Sec. 78u-4(b)(3)(B). Accordingly, this motion will be denied.

***TITTLE, RINARD* AND *KEMPER* MOTIONS**

On February 14, 2002, in both the *Newby* case and the *Tittle* case, the Tittle, Rinard and Kemper plaintiffs filed a motion for a Preliminary Order Freezing and Imposing a Constructive Trust over Individual Defendants' Assets and Limited Expedited Discovery into Those Assets.

(Instruments No. 292 [in *Newby*] and 77 [in *Tittle*]). Specifically these plaintiffs ask the court to permit them to conduct discovery into the assets of Cindy Olson, Mikie Rath, Sheila Knudsen, Rod Hayslett, Tod Lindhoolm, Paula Rieker, James S. Prentice, Mary K. Joyce, William Gathman, Kenneth L. Lay, Jeffrey K. Skilling, Andrew S. Fastow, Michael Kopper, Richard A. Causey, and Richard B. Buy. The plaintiffs further ask the Court, after an evidentiary hearing, for a preliminary order freezing the assets of those individuals and placing them in a constructive trust pending the final resolution of plaintiffs' claims against these defendants.

Plaintiffs in the *Tittle, Rinard* and *Kemper* actions are suing on behalf of the Enron Corp. Savings Plan (Savings Plan), the Employee Stock Ownership Plan (ESOP), and their participants and beneficiaries (ERISA plaintiffs). They argue that they, like the securities plaintiffs in the *Newby* case, have "strong claims for equitable relief against specific individuals who wrongfully profited through the breach of duties owed to the Plans and their participants. . . ." (Instruments Nos. 293 and 78, at 3). These ERISA plaintiffs join in the securities plaintiffs' freeze motion and argue that they "have the same right to freeze the prejudgment assets of the named defendants in their actions as the securities plaintiffs do upon a proper showing in their action-- and for the same reasons." (Instruments No. 293 and 78, at 3).

As the Court has discussed above, in Judge Rosenthal's January 8, 2002 order she denied the motion of the securities plaintiffs to freeze the assets of the defendants because the evidence before her made no showing that any of the individual securities defendants were likely to hide or dissipate assets. She also found that the securities plaintiffs had not shown an entitlement to expedited discovery into the assets of the individual securities defendants. She gave the securities plaintiffs an opportunity to demonstrate entitlement to a lifting of the automatic PSLRA stay to

conduct expedited discovery into the assets of certain defendants (Instrument No. 111, at 42-44). The securities plaintiffs' supplemental briefing, as this Court has found, offered no new justification for expedited discovery and made no further attempt to show that any particular securities defendant intended to hide assets, except for a proffered transcript of a televised interview of Mrs. Lay and newspaper analyses of the Lay finances. The pending motion of the ERISA plaintiffs relies upon that briefing. Judge Rosenthal found, citing *United States ex rel. Rahman v. Oncology Associates, P.C.* 198 F.3d 489 (4th Cir. 1999) and *DeBeers Consol. Mines, Ltd. v. United States*, 325 U.S. 212 (1945) that in order to show entitlement to discovery and an asset freeze the plaintiffs must show for each defendant, (1) "a sufficient nexus between the assets sought to be frozen and the equitable relief plaintiffs request" and (2) that freezing assets "is a reasonable measure to preserve the status quo in aid of the ultimate equitable relief claimed." (Instrument No. 111, at 14-15). The ERISA plaintiffs here have not satisfied either requirement. Their motion will be denied. Accordingly, it is hereby

ORDERED, ADJUDGED, and DECREED that Defendant Andrew Fastow's Motion for Reconsideration of Memorandum Opinion and Order of January 8, 2002 (Instrument No. 257), Defendant Ken L. Harrison's Motion for Limited Reconsideration of the Court's Order of January 8, 2000 (Instrument No. 261), and The Outside Directors Motion for Limited Reconsideration of the Court's Order of January 8, 2002 Regarding the Court's Authority to Order a Prejudgment Restraint of Defendants' Assets (Instrument No. 266) are DENIED. It is further

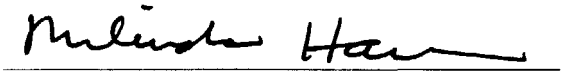
ORDERED, ADJUDGED, and DECREED that the motions filed as Amalgamated Bank's Supplemental Brief in Response to the Court's January 8, 2002 Memorandum and Order (Instrument No. 180) and Second Supplemental Brief in Response to the Court's January 8, 2002

Memorandum and Order Concerning Particularized Discovery (Instrument No. 251) are DENIED. It is further

ORDERED, ADJUDGED, and DECREED that Amalgamated Bank's and Regents' Notice of Motion and Motion for an Order Granting Particularized Expedited Discovery from Enron Executives (Instrument No. 259) is DENIED. It is further

ORDERED, ADJUDGED, and DECREED that the Motion of the *Tittle, Rinard* and *Kemper* Plaintiffs for a Preliminary Order Freezing and Imposing a Constructive Trust Over Individual Defendants' Assets and Limited Expedited Discovery Into Those Assets (Instrument No. 292 in *Newby* and No. 77 in *Tittle*) is DENIED.

Signed at Houston, Texas, this 17th day of September, 2002.



MELINDA HARMON
UNITED STATES DISTRICT JUDGE