United States Courts
Southern District of Texas
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IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

In Re Enron Corporation Securities, Derivative & "ERISA Litigation	§	MDL-1446
THIS DOCUMENT RELATES TO: All Cases	§	
MARK NEWBY, ET AL., Plaintiffs	§	
VS.	§	CIVIL ACTION NO. H-01-3624 ✓ CONSOLIDATED CASES
ENRON CORPORATION, ET AL., Defendants	§	
THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, et al., Individually and on Behalf of All Others Similarly Situated, Plaintiffs,	§	
vs.	§	
KENNETH L. LAY, ET AL., Defendants.	§	

ORDER

Pending before the Court is Certain Officer Defendants' (Steven J. Kean, Mark E. Koenig, Lawrence Greg Whalley, Mark A. Frevert, and Cindy K. Olson's) motion for reconsideration and clarification of the Court's denial[1] of their motions to dismiss (instrument #1318).

[1] See instrument #1299, entered 3/25/03.

#1345

After re-examining its order and the briefing, the Court responds to the challenges in the motion for reconsideration and clarification.

First, the Court concedes confusion in its references to the Executive and Management Committees, but maintains that it is immaterial to the substance of its ruling. Although Defendants emphasize that "the Complaint does not allege that any of the Officer Defendants served on that 'Executive Committee' and, in fact, none of the Officer Defendants did serve on that committee," the Court notes that in the Officer Defendants' motions to dismiss, they refer to Lead Plaintiffs' allegations that each "was on the Management Committee or Executive Committee" for some or all of the years between 1997-2000, identified by Lead Plaintiff as to each Defendant. *See, e.g.*, #656 (Koenig) at 3; #646 (Frevert) at 3; #643 (Whalley) at 3; #657 (Kean) at 3; and #641 (Olson) at 3. More important, there is no dispute that they all served for years on the Management Committee, which Lead Plaintiff has expressly alleged was composed of Enron's top executives who met weekly or biweekly to oversee and review Enron's business and which repeatedly approved "all significant business transactions of Enron," including the formation, financing and transactions of the SPEs and partnerships (deceptive devices and contrivances) at the heart to the Ponzi scheme, allegedly established to hide Enron's debt and inflate its finances at critical reporting times, while its key executives enriched themselves through derivative inflated salaries, bonuses, and stock. Complaint at 99, ¶ 88.

Defendants complain that although the complaint does not makes such allegations, the Court improperly found that Lead Plaintiff claimed that the Management Committee was an "all-powerful" body that voted on the core transactions constituting the Ponzi scheme, that each corporate Inside Director had intimate personal involvement in Enron's daily business operations, that the Management Committee was repeatedly presented with "requests to authorize virtually the same modes of enabling fraud and self aggrandizement throughout the vast business empire of Enron, yet the Committee continued to issue rubber-stamp approvals," that these Defendants were in charge of running the various entities constituting the Ponzi scheme, that their resolutions at meetings repeatedly authorized the alleged deceptive devices and contrivances at critical reporting times (when Defendants insist that none of them is alleged to have cast a single vote), and that their positions and votes on the Management Committee reflect their power to control Enron.

The Court disagrees. Paragraphs 88 and 297 of the complaint illustrate the same allegations. In rephrasing the contentions of the complaint and in describing the larger picture the complaint portrays, which is remarkably detailed in light of the fact that it was rapidly drafted without benefit of discovery, the Court has not misrepresented the pleadings. In reviewing a motion to dismiss for failure to state a claim, this Court is to accept all factual allegations in the complaint as true and is permitted to draw all reasonable inferences in the plaintiff's

failure. *Cantor Fitzgerald Inc. v. Lutnick*, 313 F.3d 704, 709 (2d Cir. 2002); *Holman v. Indiana*, 211 F.3d 399, 407 (7th Cir. 2000), *cert. denied*, 531 U.S. 880 (2000); *McNamara v. Bre-X Minerals Ltd.*, 57 F. Supp.2d 396, 402 (E.D. Tex. 1999). Lead Plaintiff has responded to Defendants' contention by stating that the Court has "simply undertaken a common-sense reading of Lead Plaintiff's allegations" in compliance with the Fifth Circuit's directive "'to construe the allegations in the light most favorable to the plaintiffs.'" Lead Plaintiff's Opposition (#1338) at 4, *quoting Nathenson v. Zonagen, Inc.*, 267 F.3d 400, 406 (5th Cir. 2001).

Moreover, the Court finds meritless Defendants' objection that the complaint does not allege a single vote or passage of any resolution by any Defendant on the Management Committee. As Lead Plaintiff, characterizing the argument as "preposterous," responds, "How else could the Management Committee approve the dubious partnership and SPE deals without its members casting a vote?" Opposition at 6.

Although Defendants suggest that the Court may have "prejudged this case, based upon media accounts and perhaps other sources," the Court has made abundantly clear in the course of its memoranda and orders the standard of review of Lead Plaintiff's allegations at this stage of the litigation. The Court has not been making findings, but examining the sufficiency of the allegations to determine whether Lead Plaintiff has stated a claim. The Court has also reiterated that in reviewing Lead Plaintiff's responses, if the Court determines that there is a

viable, factually supported claim to be made that was not stated in the amended complaint, the Court does not simply view the complaint as amended by that response; instead, as explicitly stated in the Court's previous orders, in the interests of justice it will grant, and has granted, leave to Lead Plaintiff to amend its complaint (#839) to assert such a claim, especially in view of Lead Plaintiff's explicit motion for leave to do so.[2] That amendment is to be effected by Lead Plaintiff in one document, after the Court has ruled on all the motions to dismiss, and Defendants will have a full and fair opportunity to challenge the sufficiency of any new allegations. The Court has also emphasized that the PSLRA's more stringent pleading requirements were instituted to discourage expensive and harassing strike suits, but that it does not find that any reasonable person would determine that this litigation was brought merely for such a purpose. Finally, while the Court has referenced various media accounts and information publicized about Congressional investigations of Enron in several of its orders, it has done so as these reports relate to and are consistent with allegations made by Lead Plaintiff. Its consideration of such matters also factors into the totality of the circumstances that must be considered in determining whether Lead Plaintiff has stated a claim against each Defendant. The Court's purpose is to ensure that there is a forum for those claims that Lead Plaintiff raises and can properly plead with the

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[2] The Court mooted this motion on March 12, 2003 in #1269 on the grounds that as it reviewed the pleadings, it would determine where such amendment should be permitted.

requisite factual particularity, even if Lead Plaintiff did not do so initially.

Defendants maintain that the complaint fails to allege with particularity any claims against them. They argue that the Court has allowed "group and position pleading," in essence mere membership on the Management Committee, to suffice rather than particular facts about each of them, contrary to the PSLRA and the Court's own prior opinions in this case.

As the Court indicated, Lead Plaintiff's allegations must be viewed as a whole in determining whether Lead Plaintiff has adequately stated a claim against each Defendant. The Court agrees with Defendants that a person's position in the corporation's hierarchy or membership on a committee, or his receipt of substantial compensation, by itself, is insufficient to meet pleading requirements. Nevertheless, the totality of circumstances in the complaint detailing the alleged Ponzi scheme hammers home a very different message through recurrence, frequency, scope, and timing. Not only does the complaint assert that these Defendants were insiders involved in the day to day operations of Enron and that all significant business decisions were presented to the Management Committee for the members' approval, and thus essential to effectuating the deceptive scheme, but it is very significant that these Defendants sat on the key Management Committee for ***years***. That fact is important because in this Court's eyes the outstanding feature of the alleged Ponzi scheme was regular, and soon all too predictable, reinforcing

patterns of methods effecting the purported deceit and fraud; the very regularity of the scheme, which merely duplicated or imitated again and again the models initially developed in the establishment and funding of Chewo-JEDI-LJM1 and 2, the cumulative structured financing, the recurrent and increasing abuse of mark to market accounting described in such detail in the complaint, the reiterated use of snowballing, the repeated waivers of conflicts of interest regarding Fastow in contravention of Enron's Code of Conduct without any effort of the Committee to check up on the unvarying promised safeguards, the repetitive sham hedging, and the replay of loans disguised as sales. Also critical was the timing of such recurrent contrivances, repeatedly around vital deadlines for SEC reports. Moreover, Enron was a vast company; and according to the complaint, these deceptive devices and contrivances were employed pervasively and frequently throughout its global businesses. In light of these alleged cumulative manipulations and deceptions, the purported fraud must have grown more evident, more unmistakable, and more dubious to those sitting on the Management Committee, hearing successive requests for their approval, and rubber stamping the deals. Furthermore, the Court has pointed out the numerous allegations in the complaint indicating that the employees in many areas of the company not only knew of the fraudulent techniques regularly employed, but openly joked about them, including at company parties. These Insider Defendants were part of that workplace environment. Moreover, contemporaneously these Defendants were

pocketing exceptional compensation, inflated bonuses, and stock options tied to the size of bubble they were creating; these extraordinary awards, in the context provided by Lead Plaintiff, are additional significant factors giving rise to that strong inference of scienter, though by themselves they might be insufficient. The Court cannot help but find that a strong inference exists of actual knowledge or reckless disregard on the part of these Defendants arising from Lead Plaintiff's complaint.

For these reasons, the Court

ORDERS that the motion for reconsideration and clarification is DENIED.

SIGNED at Houston, Texas, this 21st day of April, 2003.

MELINDA HARMON
UNITED STATES DISTRICT JUDGE