

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

United States Courts
Southern District of Texas
FILED

5 MAY 20 2003

In re ENRON CORP. SECURITIES
DERIVATIVE, & "ERISA" LITIGATION

MDL-1446

Michael N. Milby, Clerk

MARK NEWBY, et al., Individually and On
Behalf of All Others Similarly Situated,
Plaintiffs,

C.A. No. H-01-3624
AND CONSOLIDATED CASES

v.

ENRON CORP., et al.,
Defendants.

**ARTHUR ANDERSEN LLP'S AND ARTHUR ANDERSEN INDIVIDUALS'
REPLY TO THE RESPONSE OF NEAL BATSON,
THE ENRON CORP. EXAMINER, TO THEIR MOTION FOR PROTECTION
FROM BANKRUPTCY RULE 2004 SUBPOENAS**

I. INTRODUCTION

Arthur Andersen LLP ("Andersen") and the Andersen Individuals hereby reply to the Examiner's Response to their Motion for Protection from Bankruptcy Rule 2004 Subpoenas (the "Motion"). The Examiner's Response is insufficient to defeat the Motion for three principal reasons. First, notwithstanding the Examiner's contention that he is a "neutral" investigator, he still must demonstrate a legitimate need to take the examinations he seeks, and he has failed to do so here. Second, the Examiner's Response relies on two orders of this Court denying motions to quash Rule 2004 subpoenas directed to other parties. Those orders are not controlling because the factual and legal basis for the instant Motion is quite different from the prior motions. Among other things, the prior motions did not address the issue of the Examiner's need for the

1404

discovery sought in light of the Examiner's detailed reports and conclusions, and further those prior motions did not raise the critical need for coordination with *Newby*.¹ Finally, new facts available since the filing of the present motion further confirm that the Examiner's discovery is duplicative and unduly burdensome. In particular, the Examiner revealed just a few days ago that he has conflicts of interest with the investigation of three banks and two accounting firms, and advocated the appointment of a second examiner, thus raising the possibility that the second examiner may seek discovery of Andersen witnesses on accounting issues. Accordingly, if the Examiner's requested examinations go forward at all, they should be coordinated with potential discovery by the other examiner and the discovery in *Newby*. Regarding *Newby*, the Examiner candidly admits that he did not attempt to coordinate with the *Newby* plaintiffs until the very day he filed his Response -- surely before duplicative discovery of the breadth he proposes is allowed to go forward, more effective efforts to coordinate should be undertaken.

II. ARGUMENT

A. The Examiner Has Made No Attempt to Rebut the Showing That He Has No Need for the Examinations He Seeks

The Examiner makes no attempt in his Response to rebut the showing by Andersen and the Andersen Individuals that he has no need whatsoever for the examinations he seeks in order to determine whether the Enron estate has unasserted legal claims to assert. Indeed, the Examiner never states that he cannot make that determination without examinations of Andersen witnesses, nor does he identify the information he believes he is lacking to make that determination. Instead, the Examiner begs the question by asserting that the witnesses "possess

¹ Andersen and the Andersen Individuals were unable to address in their Motion the Court's recent rulings on the motions to quash brought by Sherron Watkins, Annmarie Tiller, and R. Davis Maxey as the ruling on those motions was issued after Andersen and the Andersen Individuals filed the present Motion. Similarly, Andersen and the Andersen Individuals were unaware of the Court's order in respect to the motion for protection filed by certain Enron officers. Although the motion for protection was filed before this Court in the *Newby* Litigation (and posted to the website as was the Examiner's response), this Court's order on that motion was apparently not posted to the www.es13624.com website from which the parties to the *Newby* Litigation customarily receive service.

substantial knowledge regarding Enron's use of SPEs and its accounting" and, therefore, their examinations are needed to make the Examiner's investigation "complete." Response at 5. Unable to justify the examinations as necessary to determine the legal claims the estate may have, the Examiner makes plain his true purpose: He argues that the "testimony of these Witnesses will greatly aid th[e] important purpose" of "expos[ing] corporate abuses."² Response at 2. The Examiner's implicit contention is that he has absolute authority to seek discovery from any person with knowledge about Enron's collapse in order to complete his definitive report on the collapse of Enron, whether it serves any purpose of the estate or not.

The law, however, is to the contrary. The Examiner is not permitted to conduct a broad ranging, academic investigation of Enron's collapse without regard for the interests of the estate and its creditors. Indeed, the transcript the Examiner himself cites makes clear that, not only does the Examiner have a duty to the Bankruptcy Court, but he is also charged with acting in the best interest of the estate. *See* Examiner Ex. 10 at 19 ("the Examiner really works on the best interest of the estate standard"). Thus, while the Examiner is not to take an adversarial role in the proceedings, his purpose is necessarily to serve the interests of the estate. *See* 11 U.S.C. § 1104(a)(2) and (b)(1) (permitting appointment of an examiner when "such appointment is in the interests of creditors, any equity security holders, and other interests of the estate"); *In re Lenihan*, 4 B.R. 209, 212 (Bankr. D. R.I. 1980) ("The question of the appointment of an examiner, and also of a trustee, is clearly one that is equitable and discretionary; will such an appointment benefit the estate of the debtor and the interests of creditors"); *In re American Bulk Transport Co.* 8 B.R. 337, 341 (Bankr. Kan. 1980) ("Ultimately, the appointment of an examiner depends upon whether the appointment is in the best interests of creditors, equity security holders, and other interests of the estate . . .").

² Indeed, the argument that the Examiner's report serves some necessary "public purpose" (Response at 2) to expose wrongdoing at Enron has no basis here where the collapse of Enron has been the subject of Congressional investigation, inquiry by the SEC, indictments and investigation by the Department of Justice, numerous civil suits, and extraordinary press coverage.

In the present circumstance, the investigation with which the Examiner is charged serves the estate by identifying and investigating potential claims. Once that purpose is served, there is no need for the Examiner to continue to spend tens of millions of dollars of the estate's assets to "complete," in excruciating detail, aspects of his investigation with no further purpose. Indeed, the case law makes clear that bankruptcy examiners, by virtue of their position as "neutral" fact-finders, are *not immune* -- as the Examiner suggests -- from having to show a substantial need for the discovery they seek. As the court wrote in *In re Wilcher*:

[T]he examiner bears the burden of proving that good cause exists for taking the requested discovery. . . . Good cause may ordinarily be shown by a claim that the requested [discovery is] **necessary to establish the movant's claim** or that denial . . . would cause undue hardship or injustice, however the burden of showing good cause is an affirmative one and is not satisfied merely by a showing that justice would not be impeded by [permitting the discovery]. That the burden should initially lay **on the examiner** is especially appropriate in this matter where the requested discovery is extensive and may place substantial compliance difficulties on [the party from whom the discovery is sought].

56 B.R. 428, 434-435 (N.D. Ill. 1995) (quashing subpoena issued by court-appointed examiner)(emphasis added; citations omitted).

Accordingly, the Examiner cannot merely rely on his "neutral" investigatory role to justify his broad discovery of any person who might have knowledge of Enron's collapse, but rather he must make an affirmative showing of good cause by demonstrating that the discovery is "necessary to establish" a claim or that the estate would suffer "hardship or injustice" without it. The Examiner's professed need for the discovery to "complete" his already extensive investigation, without more, does not even come close to satisfying the standard set out in *Wilcher*. The Examiner must show that examinations of Andersen and the Andersen Individuals advance the interests of the estate or its creditors. The Examiner has failed to make that showing here.³

³ The Examiner argues that the Bankruptcy Court has authorized the discovery he now seeks to take, and, therefore, this Court should defer to Judge Gonzalez. Response at 4. Andersen and the Andersen Individuals, however, are not parties to the bankruptcy proceeding. Accordingly, they did not, and had no obligation to, raise the issues presented here with Judge

Although Andersen and the Andersen Individuals do not believe the Examiner has met his burden to demonstrate a need for the discovery sought here, if indeed the Examiner is, as he suggests, acting as an officer of the Court to discover all the relevant facts in an impartial manner, he should conduct his investigation in an orderly fashion to avoid imposing undue burden on the witnesses and incurring unnecessary expense to the estate. Andersen already has allowed the Examiner to take four witness interviews and has offered the Examiner the millions of pages of documents it anticipates producing in the multi-district litigation before this Court. Andersen's documents will assuredly provide the Examiner with much of the information he seeks, and will put the Examiner in the position to obtain all the information he seeks from Andersen and the Andersen Individuals in one round of examinations without the risk of his needing additional testimony from these same witnesses. Accordingly, even if the Examiner could show some legitimate need, the discovery offered by Andersen will not only suffice to meet those needs, it will do so in a manner less burdensome to the witnesses and more efficiently for the estate.⁴

Gonzalez. Thus, the Examiner's motion for leave to take the discovery was unopposed by Andersen and the Andersen Individuals. In any event, Judge Gonzalez's orders authorizing Rule 2004 discovery are general in nature and make no particular findings as to good cause to take the examinations sought here. Finally, the bulk of the Bankruptcy Court's orders authorizing Rule 2004 discovery were issued prior to the publication of the Examiner's lengthy and detailed reports on the accounting issues, in the face of which the Examiner cannot demonstrate need.

⁴ The Examiner unfairly accuses Andersen and the Andersen Individuals of attempting to "thwart" the Examiner. Response at 11. In fact, Andersen and the Andersen Individuals fully cooperated with the Examiner until he insisted upon these duplicative and burdensome examinations. Indeed, just this week, four Andersen witnesses submitted to examination on Enron tax-related issues. Moreover, Andersen has provided the Examiner with access to its workpapers and other documents. Andersen has further offered to make available its full production of documents in the *Newby* Litigation and offered the Examiner the right to participate in depositions in *Newby*. See Declaration of Catherine Palmer ("Palmer Decl.") ¶¶ 3-5.

B. The Court's Prior Rulings Cited by the Examiner Do Not Control the Issue Before the Court

The Examiner's reliance on earlier orders of this Court denying motions to quash Rule 2004 discovery brought by other parties is misplaced. Those orders are not controlling here because the Motion raises legal and factual arguments not made in the motions those orders address.

First, the motion by Enron officers does not raise the issue of need at all, and instead focuses solely on whether the Enron directors were "affected by" other adversary proceedings. The motions filed by Davis Maxey, Sherron Watkins, and Annmarie Tiller (the "Maxey Motions") to which the Examiner cites are premised principally on burden and duplication of discovery. None of the motions on which this Court has ruled have made the detailed showing Andersen and the Andersen Individuals have made here -- namely, that the Examiner has already concluded on the issues about which he seeks to take examinations.⁵

Moreover, the Examiner's need to take discovery of former Enron officers and managers -- as all the prior movants were -- is, as the case law demonstrates, far more compelling than his need to take examinations of Andersen witnesses. One of the stated functions of an examiner is to investigate "current or former management of the debtor." *See* 11 U.S.C. § 1104(b). In contrast, the "examination of third parties is at best ancillary." *See Wilcher*, 56 B.R. at 434. Accordingly, the Examiner's authority to take the discovery sought against former Enron officers and managers is far stronger than his authority to take discovery of third party witnesses such as Andersen and the Andersen Individuals.

Second, Andersen and the Andersen Individuals are differently situated with respect to the Fastow Litigation. The Examiner does not have an agreement with the Creditors Committee

⁵ Neither the Enron officers nor the parties to the Maxey Motions could demonstrate, as Andersen and the Andersen Individuals have, that the Examiner has already reached conclusions on the issues about which they would be examined. The Examiner's reports -- consisting of over 2,000 pages -- reach voluminous conclusions as to Enron's accounting and Andersen's role in it. Motion at 5-7. The Examiner's reports, however, have not yet reached detailed conclusions as to the role of the various Enron officers.

barring the sharing of discovery from Andersen witnesses relating to the existing adversary proceedings as he had in regard to certain of the Enron officers.⁶ Moreover, even were the Court to order that the Examiner's Rule 2004 discovery not be shared with the Creditors Committee, such an order would not address the arguments raised by Andersen and the Andersen Individuals that the Examiner has no need for the discovery he seeks. Nor would such an order necessarily prevent the broad Rule 2004 discovery -- which lacks the procedural protections of the Federal Rules of Civil Procedure -- from being used against Andersen and the Andersen Individuals in the *Newby* Litigation.

Third, the Enron officers did not argue, as Andersen and the Andersen Individuals have, that the burden of the discovery outweighs its benefits to the Enron estate. As shown above, the need to examine Enron insiders is likely much stronger than the need to examine third parties such as Andersen and the Andersen Individuals. In addition, the officers' motion was directed principally to the production of documents, which plainly does not impose the same burden as multiple depositions. Accordingly, had the argument been made, the calculus there would not have weighed as strongly in favor of the Enron officers as it does with regard to Andersen and the Andersen Individuals here. The Maxey Motions do raise the issue of duplicative and burdensome discovery, as the Examiner notes. Response at 13-14. The Examiner fails to point out, however, that the parties to the Maxey Motions are *not* defendants in *Newby* or other significant pending litigation. Thus, the parties to those motions do not face nearly the same prospect of repeated examinations that the Andersen witnesses do. Even more significantly, since they are not defendants in pending litigation, they face far less risk in being examined pursuant to Rule 2004 -- and thus without the procedural protections of the Federal Rules of Civil Procedure -- than Andersen and the Andersen Individuals.

⁶ The Maxey Motions do not press the argument that the witnesses there are "affected by" the pending adversary proceedings. As the witnesses who filed those motions are not defendants in *Newby*, they similarly cannot claim to need protection based on their status in that litigation.

Fourth, none of the prior motions decided before this Court raised the necessity of coordinating discovery with discovery in the *Newby* Litigation. The Enron officers' motion was decided prior to the lifting of the PSLRA stay, rendering coordination impractical and Judge Gonzalez' order requiring coordination *after* the lifting of the stay inapplicable.⁷ Accordingly, the Enron officers could not and did not argue that coordination should be required.

Thus, as a result of the lifting of the stay, Andersen and the Andersen Individuals are in a different position than prior movants and are entitled to the benefit of Judge Gonzalez's order requiring coordination "to the extent practicable." Motion at 4. The Examiner provides no meaningful argument -- and certainly presents no facts -- showing that the estate's interests would be somehow harmed by coordination with *Newby*. Instead, the Examiner merely states that he "believes" that it would be impractical to coordinate because the Examiner telephoned plaintiffs' counsel in *Newby* on May 19 -- two weeks *after* issuing the Subpoenas on which he was directed to coordinate and on the very day the Examiner filed his opposition brief here -- and plaintiffs' counsel was not ready to immediately proceed with depositions. Response at 15. The Examiner's belated telephone call does not suffice to comply with Judge Gonzalez's order to coordinate, and his bare assertion that he "believes" coordination to be impractical is not a sufficient basis to disregard Judge Gonzalez's order.⁸ In the absence of strong evidence that the Enron estate would be harmed by waiting for coordination with *Newby*, such coordination should be required.

⁷ Again, as none of the witnesses are parties to *Newby*, the Maxey Motions do not argue that coordination should be enforced.

⁸ The Examiner argues that, if his Rule 2004 Subpoenas were quashed, he would have no means of compelling discovery. Response at 11. That argument is moot here because Andersen and the Andersen Individuals have already offered the Examiner the opportunity to participate in depositions in *Newby*.

C. **The Examiner's Recent Admission That He Has Conflicts of Interest Regarding Certain Banks and Accounting Firms Confirms That the Examinations Are Inappropriate at This Time**

As noted above, the Examiner's Response makes little pretense of demonstrating a need to go forward with the examinations in the absence of coordination with *Newby* and prior to the availability of all the relevant documents. Response at 15-16. In contrast with the Examiner's bare assertions of impracticability, Andersen and the Andersen Individuals have made a compelling factual showing that the Examiner's discovery will result in duplicative and burdensome discovery and will waste Andersen's resources. Motion at 21-25.

Since the filing of the Motion for Protection, Andersen and the Andersen Individuals have become aware of additional facts suggesting that they could face duplicative requests for Rule 2004 discovery, in addition to duplicative discovery in the numerous pending civil actions. Nearly a year into his investigation, on May 15 -- one day after this Motion was filed -- the Examiner informed the Bankruptcy Court that he and his law firm have debilitating conflicts of interest as to three banks and two large accounting firms⁹ that preclude him from making findings as to those parties. As a result, the Examiner advocated appointing *a second examiner* to handle the investigation and findings as to those parties. Because the investigation that may be transferred to this second examiner involves accountants and accounting issues, the second examiner may also seek to take Rule 2004 discovery of Andersen and the Andersen Individuals. In addition to the other compelling reasons that the Examiner's discovery should be coordinated with the production of documents and depositions in *Newby*, it is also unfair to Andersen and the Andersen Individuals and inefficient to permit examinations to proceed before the conflict of interest issue is resolved so that, at the least, Andersen will not be subject to requests for discovery from two different examiners.

⁹ The banks at issue are Bank of America, UBS Warburg, and Royal Bank of Canada. The accounting firms identified were KPMG and PricewaterhouseCoopers.

III. CONCLUSION

For the foregoing reasons, as well as those set forth in the Motion for Protection, this Court should grant Andersen's and the Andersen Individuals' Motion for Protection and quash the Examiner's Subpoenas. In the alternative, this Court should order that the examinations requested by the Examiner be coordinated with depositions in the *Newby* Litigation.

Dated: May 20, 2003

Respectfully submitted,

Miles N. Ruthberg by
Rusty Hardin
State Bar No. 08972800
S.D. Tex. I.D. No. 19424
Andrew Ramzel
with permission.

1201 Louisiana, Suite 3300
Houston, Texas 77002-5809
(713) 652-9000
(713) 652-9800 (fax)

Attorney-in-Charge for
Defendant Arthur Andersen LLP

OF COUNSEL

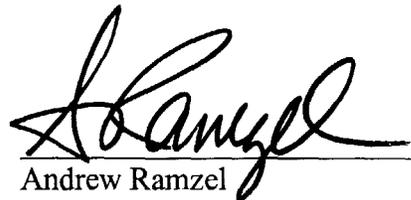
Andrew Ramzel
State Bar No. 00784184
S.D. Tex. I.D. No. 18269
RUSTY HARDIN & ASSOCIATES, P.C.
1201 Louisiana, Suite 3300
Houston, Texas 77002-5809
(713) 652-9000
(713) 652-9800 (fax)

Miles N. Ruthberg
(Cal. Bar No. 086742) (pro hac vice)
Peter A. Wald
(Cal. Bar No. 085705) (pro hac vice)
Catherine E. Palmer
(N.Y. Bar No. 1724103) (pro hac vice)
LATHAM & WATKINS LLP
633 West Fifth Street, Suite 4000
Los Angeles, California 90071-2007
Telephone: (213) 485-1234
Facsimile: (213) 891-8763
Attorneys for Defendant
Arthur Andersen LLP
(except with respect to any alleged fault of all banks
and certain other defendants for proportionate
liability or other defenses)

Eliot Lauer
(NY Bar No. EL-5590) (pro hac vice)
Benard V. Preziosi, Jr.
(NY Bar No. BP-5715) (pro hac vice)
CURTIS, MALLET-PREVOST, COLT & MOSLE LLP
101 Park Avenue
New York, New York 10178-0061
Telephone: (212) 696-6000
Facsimile: (212) 697-1559
Attorneys for Defendant
Arthur Andersen LLP
(except for certain banks)

CERTIFICATE OF SERVICE

I certify that on this 20th day of May, 2003, a true and correct copy of the foregoing pleading was served on all counsel pursuant to the Court's service orders.



Andrew Ramzel