UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

United States Courts
Southern District of Texas

OCT 1 4 2003

Michael N. Milby, Clerk

In re ENRON CORPORATION SECURITIES LITIGATION	§	
	§	
This Document Relates To:	§	
	§	
MARK NEWBY, et al., Individually and On Behalf of All Others Similarly Situated,	§	Consolidated Civil Action No. H-01-3624
Plaintiffs,	§	
vs.	§	
ENRON CORP., et al.,	§	
Defendants.	§	

REPLY MEMORANDUM OF LAW IN SUPPORT OF
THE DEUTSCHE BANK ENTITIES' MOTION TO DISMISS

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REPLY MEMORANDUM OF LAW IN SUPPORT OF THE DEUTSCHE BANK ENTITIES' MOTION TO DISMISS

Deutsche Bank AG ("DB"), Deutsche Bank Trust Company Americas (formerly known as Bankers Trust Company) ("DBTC"), and Deutsche Bank Securities Inc. (formerly known as Deutsche Banc Alex. Brown Inc.) ("DBSI") (collectively, the "DB Entities") respectfully submit this reply memorandum of law in further support of their motion to dismiss the First Amended Consolidated Complaint in the Newby action (the "Amended Complaint" or "Am. Compl."). The DB Entities' initial brief will be referred to as "DBE Mem." DB's initial briefs in support of its successful motion to dismiss the original Consolidated Complaint (the "Newby Complaint" or "Newby Compl.") will be referred to as "DB Mem." and "DB Reply."

PRELIMINARY STATEMENT

Plaintiffs' opposition to the DB Entities' motion to dismiss ("Pl. Mem.") and to that of the other bank defendants ("Pl. Omnibus Mem.")[1] attempts to hide their failure to plead properly the elements of securities fraud under Section 10(b)/Rule 10b-5 by arguing that any deficiency to state a claim under one prong ignores allegations under another. The problem, however, is that plaintiffs fail to state a claim under ***any*** of the prongs of Rule 10b-5.

Plaintiffs' mischaracterization of the DB Entities' motion to dismiss as an attempt to re-write their complaint (Pl. Mem. at 1–6, 14) is simply a device deployed to distract the Court from these pleading deficiencies. The DB Entities were willing to wait for plaintiffs to amend their complaint to add allegations based on the Examiner's Third Report. Plaintiffs declined. Instead, plaintiffs agreed to allow the DB Entities additional time to file their motion to dismiss to

[1] For the convenience of the Court, and in the interest of brevity, we have not repeated arguments made by other bank defendants in their replies to the Pl. Omnibus Mem. To the extent applicable, however, those arguments are adopted and incorporated in the DB Entities reply in further support of their motion to dismiss.

incorporate responses to the Third Report, and it is entirely proper for this Court to consider public documents referenced in the complaint. DBE Mem. at 4.

Plaintiffs contend that the DB Entities have "ignore[d] the breadth of [their] conduct that occurred throughout the Class Period . . . . includ[ing] a broad range of securities violations arising out of false and misleading analyst reports and securities offering documents, as well as involvement in LJM2." Pl. Mem. at 7. This contention is despite the fact that the DB Entities explicitly incorporated in this motion DB's briefing on its original motion to dismiss which this Court granted and which addressed these other aspects of DB's relationship with Enron.

As detailed below, plaintiffs' current theory is to bootstrap all the allegations dismissed by this Court in the December Order to the six structured transactions discussed by the Examiner (the "SSTs"). Absent the allegations of fraud tied to the SSTs, plaintiffs have not altered the Newby Complaint to remedy the deficiencies that supported its dismissal. Given that plaintiffs cannot premise fraud claims on the SSTs, the allegations as to analyst reports, LJM2 and other dealings with Enron remain deficient and should be dismissed with prejudice.

As discussed below, plaintiffs' newly added claim under Section 12(a)(2) of the 1933 Act, and their allegations against the DB Entities relating to the SSTs are time-barred by the three-year statute of repose. Plaintiffs cannot avoid this bar by relying on the so-called "continuing violation" doctrine, a form of equitable tolling which was prohibited by the Supreme Court in Lampf. (Point I, below.) Plaintiffs' new Section 12(a)(2) claim against DBSI also must be dismissed because the four Rule 144A/Regulation S private placement resales (the "Four note resales" (see DBE Mem. at 26)), which were properly made without a prospectus, are not subject to Section 12(a)(2) of the 1933 Act based on the Supreme Court's decision in Gustafson. In any event, plaintiffs also lack standing to bring this claim. (Point III, below).

The complaint also fails because plaintiffs still fail to meet the high pleading hurdles for fraud and scienter as to the DB Entities. Plaintiffs continue to allege facts suggesting at best that ***Enron*** made material misstatements or omissions about the SSTs. There are no well-pled facts, however, suggesting that the SSTs were fraudulent in and of themselves or that the DB Entities were severely reckless in not knowing that the SSTs were being used by Enron to allegedly create fraudulent financial disclosures.

Plaintiffs simply disregard their heightened pleading burden by seeking to elevate to fraud the Examiner's limited and highly qualified opinions relating to potential claims for aiding and abetting breaches of fiduciary duty by Enron insiders. Not only do the Examiner's conclusions fail to support a claim of fraud, but, as shown below, the Examiner and JCT findings undercut any claims of fraud or scienter by documenting, among other things, (i) the steps the DB Entities took to ensure that the transactions were proper; (ii) that various of the SST structures were vetted with federal regulators; (iii) that the SSTs involved real assets and the real long-term transfer of risk in which the DB Entities shared on a continuing basis; (iv) that the DB Entities did not control how Enron accounted for ***or*** disclosed the SSTs after consultation with ***its*** auditors and outside counsel; and (v) that none of the SSTs has been challenged by the IRS. Moreover, plaintiffs cannot even credibly claim that the effects of the SSTs were hidden, in that Enron's financial statements expressly disclosed Enron's effective tax rate, which was reduced in part by certain SSTs, was indeed significantly lower than that of other companies, and resulted in a comparatively higher net income. (Point II, below.)

These facts, all available in sources relied upon by plaintiffs (e.g., the Examiner's Reports, the JCT Report, and even the analyst reports cited in the complaint), make it impossible

for plaintiffs to assert fraud or scienter against the DB Entities. Accordingly, the Amended Complaint must be dismissed with prejudice.

ARGUMENT

POINT I

PLAINTIFFS' NEWLY ADDED ALLEGATIONS AGAINST THE DB ENTITIES ARE TIME-BARRED

A. The Statute Of Limitations Has Expired As To The SSTs

Plaintiffs themselves acknowledge that the statute of limitations period for Section 10(b)/Rule 10b-5 commences on the date that the defendant commits the allegedly ***fraudulent act***, not the date of the purchase or sale. Pl. Mem. at 8. The DB Entities agree that the three-year statute of repose period for Rule 10b-5 should begin when the alleged fraudulent act occurred rather than the date of any purchase or sale. As the court in Wafra Leasing Corp. v. Prime Capital Corp., (the case upon which plaintiffs rely) explained: "[t]hat the cause of action has not accrued . . . is beside the point, because the defendant has committed a fraudulent act. . . . This distinction is particularly clear where . . . the defendant . . . is not the seller." 192 F. Supp. 2d 852, 864 (N.D. Ill. 2002) (citation omitted). The court in Wafra held that all securities fraud claims against the accounting firm KPMG, a secondary actor, were time-barred because the alleged knowingly false representation made by KPMG occurred outside the three-year repose period. Id. at 864–65.

Also unchallenged by plaintiffs is that no claims were advanced as to the SSTs until more than three years after the last transaction closed. DBE Mem. at 8. Indeed, as to the four transactions that are the principal focus of plaintiffs' claims regarding Enron's net income, the Amended Complaint comes more than four to six years after those transactions closed. See Pl. Mem. at 1 (Projects Teresa, Steele, Tomas and Cochise); DBE Mem. at 8. To surmount this

hurdle, plaintiffs have been forced to contend that the DB Entities' role in promoting and structuring the SSTs up until the closing do not give rise to securities violations. Pl. Mem. at 7.

Alternatively, plaintiffs claim that their allegations are timely because the close of each SST was part of a "continuing" violation due to the DB Entities' acts thereafter in allegedly holding, selling and buying assets, or collecting fees from Enron for the SSTs. Am. Compl. ¶¶ 797.18, 797.20, 797.27; Pl. Mem. at 7–12. As discussed below, however, (i) the DB Entities' acts following the close of the SSTs do not give rise to a claim of primary liability; (ii) the continuing violation doctrine does not apply to private securities actions; and (iii) Sarbanes Oxley does not save plaintiffs' new claims against DBTC and DBSI as defendants or plaintiffs' new claim under Section 12(a)(2).

1. The So-Called Continuing Violation Doctrine Does Not Apply

What plaintiffs steadfastly ignore is that each SST had a discrete closing date on which substantial amounts of money and assets moved from Enron and the DB Entities to put the SSTs in place. The Examiner's Second Report documented the steps taken ***at closing*** as to each transaction.[2] It was only because these real steps were completed as of the closing dates that Enron could obtain the tax and financial accounting benefits of the transactions, and it would have been as of those closing dates that Enron's alleged disclosure duties would have arisen.

The idea that the three-year repose period of the securities laws should be tolled by the continuing-violation doctrine is refuted by the Supreme Court's ruling in Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson, 501 U.S. 350 (1991). The Supreme Court made it clear that the "equitable tolling doctrine is fundamentally inconsistent with the 1-and 3-year structure." 501 U.S. at 363.

[2] See, e.g., 2d Report, App. J at 27–29 (Project Steele); id. at 31–33 (Project Cochise); id. at 48–49 (Project Teresa); id. at 79–83 (Project Tomas).

> The 1-year period, by its terms begins after discovery of the facts constituting the violation, making tolling unnecessary. ***The 3-year limit is a period of repose inconsistent with tolling. . . . Because the purpose of the 3-year limitation is clearly to serve as a cutoff, we hold that tolling principles do not apply to that period.***

501 U.S. at 363 (emphasis added).

In support of their contention that the SSTs are timely as a part of "continuing conduct" plaintiffs rely on two inapposite cases. Pl. Mem. at 7. Huckabay v. Moore, inter alia, concerned defendants' alleged violation of Title VII for creating a hostile work environment. 142 F.3d 233, 238 (5th Cir. 1998). In contrast to securities claims, however, an employment discrimination claim "is subject to equitable doctrines such as tolling or estoppel." National R.R. Passenger v. Morgan, 536 U.S. 101, 113 (2002).

The sole securities case plaintiffs cite is a civil action brought by the SEC. Pl. Mem. at 7. The SEC, however, is not subject to ***any*** statute of limitations for civil enforcement actions seeking equitable relief. SEC v. Ogle, No. 99 C 609, 2000 WL 45260, at *4–5 (N.D. Ill. Jan. 11, 2000). At issue in Ogle, was whether the continuing violation doctrine could apply to the five-year statute of limitations for seeking civil ***penalties*** pursuant to 28 U.S.C. Section 2462. Id. The district court analogized the application of the continuing violation doctrine to hostile work environment claims under Title VII (which constitute a series of acts that give rise to a single claim) with market manipulation which "by definition involves ***violations*** over time" and is "fluid and ongoing and not a discrete goal." Ogle, at *5 (emphasis added).

As the Fifth Circuit remarked "[c]ourts, including this one, are wary to use the continuing violation doctrine to save claims outside the area of Title VII discrimination cases." McGregor v. Louisiana State Univ. Bd. of Supers., 3 F.3d 850, 866 n.27 (5th Cir. 1993); see also Abrams v. Baylor Coll. of Med., 805 F.2d 528, 533 (5th Cir. 1986) ("This theory of continuing violation has

to be guardedly employed because within it are the seeds of the destruction of statutes of limitation in Title VII cases."). Plaintiffs offer no authority for altering this rule.

Furthermore, even if Lampf did not bar the continuing violation theory from applying to private securities claims, "[a] plaintiff cannot use the continuing violation theory 'to resurrect claims . . . concluded in the past, even though its effects persist.'" McGregor, 3 F.3d at 867 (citation omitted); Reece v. Houston Lighting & Power Co., Civ. A. No. H-95-1025, 1995 WL 862342, at *3 (S.D. Tex. Aug. 10, 1995) (Harmon, J.) (quoting McGregor, 3 F.3d at 867). Thus, plaintiffs would have to allege specific facts showing that each DB Entity engaged in a new fraudulent act within the three-year statute of repose period.

Here, what plaintiffs have alleged is continuing conduct by DBTC and DB in participating in Enron's implementation of the SSTs. Even if such a claim were consistent with the factual record established by the JCT and Examiner's Reports, that would not give rise to new claims of primary liability.[3] Instructive are cases in the antitrust context discussing whether acts are in furtherance of a conspiracy.[4] "The holding or use of assets is by its nature an 'unabated inertial consequence[]' of the initial acquisition" and does not give rise to a new overt act in furtherance of a conspiracy. Concord Boat Corp. v. Brunswick Corp., 207 F.3d 1039, 1052 (8th Cir. 2000) (citation omitted).

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[3] Moreover, plaintiffs' claims are in fact at odds with the Examiner's findings regarding what the DB Entities did. As to two of the SSTs, Projects Renegade and Valhalla, the Examiner concluded that the structures and accounting for these transactions were proper and, indeed, were beneficial to Enron. See 3d Report, App. G at 19, 93. As to Projects Teresa, Steele and Cochise, the DB Entities were passive investors in entities controlled by Enron, and so, did not hold, sell or buy assets. See, e.g., 2d Report, App. J, Annex 4 at 5–9 (Project Teresa); 2d Report, App. J, Annex 1 at 4–9 (Project Steele); 2d Report, App. J, Annex 2 at 6–7 (Project Cochise). Finally, as revealed in the JCT Report, DBTC's fees were set at closing, and included pre-set payments due in installments thereafter, subject only to an actual change in law or accounting rules (something which has not occurred) that reduced the benefits allowed to Enron in the transaction. See, e.g., JCT Report, App. B at B-215, B-260. There was no provision for DBTC to monitor the benefits Enron booked on an ongoing basis.

[4] As this Court recently held, plaintiffs cannot pursue claims under RICO for civil conspiracy where such claims are substantially identical to and/or grounded in alleged securities violations. See generally, In re Enron Corp. Sec. & Derivative & ERISA Litig., Civ. A. No. H-01-3913, slip. op. at 250260 (S.D. Tex. Sept. 30, 2003).

> [C]ontinuing conduct within the limitations period which merely furthers the initial antitrust violation does not prevent the running of the statute of limitations. . . . Even assuming that [defendant] continued to mislead its agents . . . this continuing conduct is not an injurious act separate from the prior alleged misconduct. An antitrust suit 'must be based on some injurious act actually occurring during the limitations period, not merely abatable but unabated inertial consequences of some pre-limitations action.'

United Farmers Agents Ass'n, Inc. v. Farmers Ins. Exch., 892 F. Supp. 890, 912 (W.D. Tex. 1995) (citations omitted). Here, the closing of each SST created the pool of assets and the structure that then supported the economic benefits flowing from the transactions.

Accordingly, the continuing violation theory cannot be used to resurrect claims about DBTC's or DB's role in the SSTs even if the alleged effects of the SSTs persisted in the earnings Enron reported in its financial statements.

2. Sarbanes Oxley Does Not Apply To Plaintiffs' New Claims

Plaintiffs attempt to rely on the arguments set forth in Pl. Omnibus Mem. for the proposition that the Public Company Accounting Reform and Investor Protection Act of 2002 ("Sarbanes Oxley") applies to their addition of DBTC and DBSI as defendants and their new claim under Section 12(a)(2) of the 1933 Act. Pl. Mem. at 5. This Court, however, has already determined that Sarbanes Oxley does ***not*** apply to this proceeding. In re Enron Corp. Sec. Derivative & ERISA Litig., 258 F. Supp. 2d 576, 601 (S.D. Tex. 2003) (Sarbanes Oxley amended the limitations period "for ***suits*** commenced on or after July 30, 2002. This amended limitations period does not apply to Newby.") (emphasis added); accord De La Fuente v. DCI Telecomms., Inc., 259 F. Supp. 2d 250, 259 & n.5 (S.D.N.Y. 2003).

Plaintiffs make a thin attempt to construe the term "proceeding" as referencing each "claim" or party in a lawsuit. Under plaintiffs' reasoning the assertion of existing claims against new parties or the addition of entirely new claims to an existing action after the enactment of Sarbanes Oxley would be viewed as new "proceedings." In support of this expansive

proposition plaintiffs rely on Friedman v. Rayovac Corp., No. 02-C-308-C, No. 02-C-325-C, No. 02-C-370-C, slip op. (W.D. Wis. May 29, 2003). Pl. Omnibus Mem. at 8–9. Not only is this case not binding on this Court, but, to the extent that it treats the addition of new claims or parties as new "proceedings," it was incorrectly decided.

In Friedman, the district court reasoned that the fact that (i) the Federal Rules provide that "[a] civil action is commenced by filing a complaint with the court," and (ii) Fed. R. Civ. P. 15(c) requires a plaintiff seeking to add a new party to show that the amendment relates back to the initial complaint, "suggests that serving an additional party with a complaint commences a new 'proceeding,' even if the new claim is part of a lawsuit that was filed previously" because "otherwise, there would be no statute of limitations problem because the date of the original filing would always control." slip op. at 22–23. This, however, is a different approach than that suggested by the Fifth Circuit. See National Union Fire Ins. Co. v. Willis, 296 F.3d 336, 342 (5th Cir. 2002) ("A suit begins in federal court with the filing of a complaint. After the original filing, the suit is considered to be pending. Thus the amendment of the . . . complaint . . . does not constitute a new filing of the case.") (citing Ameriwood Indus. Int'l Co. v. American Cas. Co., 840 F. Supp. 1143, 1152 (W.D. Mich. 1993)).

The mistaken premise in Friedman is that since Rule 15(c)'s relation back provision allows plaintiffs to file new claims or add parties otherwise time-barred, such added claims or parties must be treated as separate "proceedings." In essence, the court conflates the meaning of claim with proceeding. "The term 'claim,' in its common acceptance, denotes a demand for money or property as of right." United States v. Tieger, 138 F. Supp. 709, 710 (D.N.J. 1954), citing inter alia Hobbs v. McLean, 117 U.S. 567, 575 (1886). Thus, the addition of a new claim

would be an additional demand for recovery such as under Section 12(a)(2) or the demand for recovery from a new party.

The word "proceeding," however, references cases or suits, ***not*** added parties or claims:

> ['P]roceeding' means the form in which actions are to be brought and defended, the manner of intervening in suits, of conducting them, the mode of deciding them, of opposing judgments and of executing. Ordinary proceedings intend the regular and usual mode of carrying on a suit by due course of common law.

Statter v. United States, 66 F.2d 819, 822 (9th Cir. 1933) (citation omitted). Similarly,

> '[t]he term [suit] is . . . understood to apply to any proceeding in a court of justice by which an individual pursues that remedy which the law affords. The modes of proceeding may be various; but, if a right is litigated in a court of justice, the proceeding by which the decision of the court is sought is a suit.

Kohl v. United States, 91 U.S. 367, 375 (1875). Likewise, "[t]he term 'action' in its usual sense, at least its usual legal sense, means a suit brought in court, a formal complaint within the jurisdiction of a court of law." Pathman Constr. Co. v. Knox County Hosp. Ass'n., 326 N.E.2d 844, 854 (Ind. Ct. App. 1975). In other words, a suit or action is a type of proceeding, whereas a claim or remedy is a demand for relief that is asserted within or as a part of a proceeding.

The Second Circuit, construing the term "action" for purposes of interpreting the "effective date" of the PSLRA, rejected plaintiffs' view that a new action was created each time plaintiffs amended their complaint. Gerber v. MTC Elec. Techs. Co., 329 F.3d 297, 309–10 (2d Cir. 2003). The Second Circuit reasoned that it was doubtful "that Congress intended that courts would apply different sets of substantive and procedural rules to groups of plaintiffs asserting identical claims in a single action, depending on when those plaintiffs were added to the complaint." Id. at 310.

Here, plaintiffs' expansive reading of the term "proceeding" would similarly subject different defendants in the same action to a different statute of limitations. For example, a three-year statute of repose would apply to Section 10(b) claims against DB while a five-year statute of

repose would apply to all claims against DBTC and DBSI (DB affiliates) and the new Section 12(a)(2) claim as to DB.[5] There also is no evidence that Sarbanes Oxley applies retroactively to existing cases. If Congress had intended this, it could have made Sarbanes Oxley expressly applicable to all proceedings pending on or commenced after the date of enactment. This, Congress did not do. See Landgraf v. USI Film Prods., 511 U.S. 244, 259–60 (1994) (if Congress had intended to prescribe "a general rule of retroactivity. . . . surely [it] would have used language comparable to . . . 'shall apply to all proceedings commenced on or after the date of the enactment of this Act.'"); Martin v. Hadix, 527 U.S. 343, 354 (1999) (requiring an "express command" for retroactive application).[6]

Accordingly, as this Court has already recognized, the statute of repose adopted by the Supreme Court in Lampf, governs this case. March Order, 258 F. Supp. 2d at 601 n.20 (citing Lampf, 501 U.S. at 359–60). Under Lampf, any allegations concerning any of the DB Entities' actions prior to April 8, 1999 (assuming the new allegations concerning the SSTs relate back) cannot be used to state a claim under Section 10(b)/Rule 10b-5. This rules out any claims based on the DB Entities' role in structuring all of the SSTs but one—and as to that one (Project

[5] Plaintiffs also cannot take advantage of the expanded statute of limitations under Sarbanes Oxley by filing a new action. Glaser v. Enzo Biochem, Inc., Civ. A. No. 02-1242-A, 2003 WL 21960613, at *5 (E.D. Va. July 16, 2003) (rejecting plaintiffs' attempt to file a second complaint after the enactment of Sarbanes Oxley to revive their federal securities claim); see also Hughes Aircraft Co. v. United States, 520 U.S. 939, 950 (1997) ("a newly enacted statute of limitations that lengthens the applicable statute of limitations may not be applied retroactively to revive a plaintiff's claim that was otherwise barred under the old statutory scheme.") (citation omitted). A plaintiff cannot file a new complaint to avoid procedural rules governing the amendment of complaints. See, e.g., Oliney v. Gardner, 771 F.2d 856, 859 (5th Cir. 1985) ("the district court must ensure that the plaintiff does not use the incorrect procedure of filing duplicative complaints to expand the procedural rights he would otherwise enjoy—particularly for the purpose of circumventing the rules pertaining to the amendment of complaints.") (citation omitted).

[6] The DB Entities also incorporate by reference the arguments made by other bank defendants in reply to the Pl. Omnibus Mem. concerning the inapplicability of (i) Sarbanes Oxley to Plaintiffs' new Section 12(a)(2) claim (which expressly asserts only negligence claims and does not sound in fraud (Am. Compl. ¶ 1016.3)) and (ii) relation back under Rule 15(c).

Valhalla) the Examiner specifically concluded that there was no basis for an aiding and abetting claim, let alone a fraud claim.[7] DBE Mem. at 8.

Plaintiffs also do not dispute that the limitations period under Lampf, applies to Section 10(b)/Rule 10b-5 against DB, which was renamed by plaintiffs after this court dismissed all claims against it. Thus, even if this Court holds that Sarbanes Oxley applies to DBTC and DBSI and to the newly added Section 12(a)(2) claim, this longer period cannot be used to plead claims against DB under Section 10(b)/Rule 10b-5.

B. The Statute Of Limitations Has Expired As To DBTC And DBSI

Plaintiffs made a strategic decision to view DB and its various affiliates and subsidiaries as a single entity under the so-called "one-entity approach"[8] and ***chose*** only to name DB in the Newby Complaint. Plaintiffs have now decided to add DBTC and DBSI as defendants while continuing to set forth allegations under their one-entity approach. Am. Compl. ¶ 107(a). Plaintiffs want it both ways—they want to avoid making specific allegations as to the acts of distinct legal entities by treating those entities as a single unit, yet they ***now*** want to name specific defendants without making specific allegations as to each defendant. This is group pleading in its worst form and is simply not permitted under the heightened standards of the PSLRA. DBE Mem. at 12. Plaintiffs claim that their addition of DBTC and DBSI is proper based on facts learned from the release of the JCT Report and the Bankruptcy Examiner's Second and Third Reports. This, however, only permits the plaintiffs to add new allegations (to the extent that such additions are amplifications of their original claims), ***not*** new defendants.

[7] The only SST to close after April 8, 1999 was Project Valhalla. The Examiner, however, found that this transaction was beneficial to Enron and did not involve any questionable accounting. 3d Report, App. G at 93. Thus, this transaction was not deemed to support any claim against any DB Entity and cannot serve as the basis for a fraud claim here.

[8] In re Enron Corp. Sec., Derivative & ERISA Litig., 235 F. Supp. 2d 549, 564 n.5 (S.D. Tex. 2002) (hereinafter "December Order").

There was no mistake of identity in this case. There was no mistake of law either. Similarly, plaintiffs' claims of collateral estoppel (Pl. Omnibus Mem. at 14–17) have no bearing on the DB Entities because this court dismissed DB from this action in its entirety. Thus, plaintiffs' newly added allegations are time-barred.

POINT II

PLAINTIFFS HAVE FAILED TO STATE A CLAIM UNDER SECTION 10(B) AND RULE 10B-5 AS TO THE DB ENTITIES

A. The DB Entities Did Not Engage In Fraudulent Transactions With Enron

Eager to avoid the statute of repose, plaintiffs now argue that it was not the "close" of the SSTs but the DB Entities' alleged activities in continuing to implement them that give rise to liability. Pl. Mem. at 8. Plaintiffs, however, have once again failed to plead anything other than ordinary business activities such as receiving the proceeds of invested money, continuing to hold assets and receiving installment payments of fees which had been previously earned. This is not fraud, and the Examiner's Reports and the JCT Report fail to support any allegation of fraud.

At the outset, it is important to recall that the Examiner found no fraud. Rather, the Examiner made much more limited findings as to ***three*** of the SSTs. As to Projects Steele and Cochise, the Examiner found non-compliance with GAAP because "it is more likely than not" that the IRS could disallow Enron's claimed tax benefits from the transactions. The Examiner admitted that this finding involved "a degree of professional judgment" and that the tax opinions provided to Enron by its outside counsel "sets forth arguments expressing a different professional judgment."[9] As to Project Teresa, the Examiner found non-compliance with GAAP because the recording by Enron of the deferred tax asset associated with the transaction was

[9] 2d Report, App. J, Annex 3 at 13 (Steele) and 35 (Cochise).

"premature" notwithstanding the legal opinions provided to Enron by outside counsel.[10] Based on these limited and highly qualified opinions, the Examiner determined that potential claims of aiding and abetting breaches of fiduciary duty by Enron's insiders might lie as against the DB Entities.[11] Breaches of fiduciary duty, however, do not give rise to securities fraud claims.[12]

Moreover, none of the DB Entities were connected to ***Enron's*** alleged failure to comply with GAAP in accounting for three of the SSTs in its financial statements. Plaintiffs do not allege ***facts*** suggesting that the structures of the SSTs violated GAAP or were otherwise fraudulent. Indeed, the facts disclosed by the Examiner defeat any claim that the SSTs were fraudulent in and of themselves. For example, to ensure that the SST structures complied with GAAP and the tax laws, the DB Entities had those structures reviewed by outside accountants ***and*** leading national law firms. 3d Report, App. G at 15-16, 30, 39, 45, 49, 76. The Examiner then disagreed with the conclusions of Enron's lawyers that the tax treatment would be sustained, finding instead that ***Enron's*** accounting treatment of some of the SSTs, ***as implemented,*** violated GAAP. Id. at 28, 35, 42–43, 49; Pl. Mem. at 14–15 n.11. Faced with

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[10] 2d Report, App. J, Annex 4 at 26–28. With regard to Project Tomas, the Examiner concluded that it "probably" violated GAAP solely because ***Enron*** failed to record valuation allowances or tax reserves for that transaction. 2d Report, App. J at 88. As to Projects Renegade and Valhalla, the Examiner concluded that the structures and accounting were proper. 3d Report, App. G at 19, 93.

[11] The Examiner's Third Report further qualifies the opinions, explaining:

> The Examiner has reviewed a substantial amount of evidence, including documentary and testimonial evidence, and has noted reasonable inferences that could be drawn from the evidence. Moreover, there are certain defenses to aiding and abetting liability and equitable subordination available to BT/Deutsche. Whether BT/Deutsche will succeed on one or more of these defenses will depend upon the fact-finder's resolution of the facts.

3d Report, App. G at 5–6.

[12] See, e.g., Santa Fe Indus. v. Green, 430 U.S. 462, 477–80 (1977); Goldstein v. MCI Worldcom, 340 F.3d 238, 254 (5th Cir. 2003); Tuchman v. DSC Communications Corp., 14 F.3d 1061, 1070 (5th Cir. 1994) ("corporate mismanagement does not, standing alone, give rise to a 10b-5 claim, and mea culpa does not sufficiently satisfy the scienter requirements of pleading in securities fraud cases unless it is shown to relate to activities that have a definable nexus or relationship with the sale or purchase of a security.").

this, plaintiffs now try to argue that technical compliance with GAAP may still violate Rule 10b-5.

In so arguing, plaintiffs state that the "Eighth Circuit *held*: A securities fraud complaint need not allege GAAP violations to establish that a material misstatement occurred in a company's financial statements." (Pl. Mem. at 15 (quoting In re K-Tel Int'l Sec. Litig., 300 F.3d 881, 906 (8th Cir. 2002) (emphasis added)). The Eighth Circuit held no such thing. In fact, this quote comes from the ***dissenting opinion*** which cites two cases, both of which were decided prior to the enactment of the PSLRA's heightened pleading standards. 300 F.3d at 906.

Far from supporting plaintiffs' position, the Eighth Circuit, in affirming the district court's dismissal with prejudice, re-emphasized that "'[a]llegations of GAAP violations are insufficient, standing alone, to raise an inference of scienter. Only where these allegations are coupled with evidence of corresponding fraudulent intent might they be sufficient.'" 300 F.3d at 890 (citation omitted). The court further explained that under the PSLRA plaintiffs must allege "'facts or further particularities that, if true, demonstrate that the defendants had access to, or knowledge of, information contradicting ***their*** public statements when they were made.'" Id. (citation omitted). Thus, if anything, K-Tel reasons in favor of dismissing Plaintiffs' Section 10(b) claim against the DB Entities.

Plaintiffs' next argument is that the SSTs were fraudulent because Enron used them to manipulate earnings. Pl. Mem. at 15. Again, the focus here is ***Enron's*** decision as to how to account for and disclose the SSTs. Plaintiffs have pled ***no facts*** to show that the DB Entities had any role in Enron's disclosure decisions. In addition, plaintiffs studiously ignore the fact that the market ***did*** know that Enron's earnings were increased through the reduction of its effective tax rate.

Enron's financials, like the financials of every public company, openly disclosed its effective tax rate and reconciled Enron's effective tax rate with the federal tax rate of 35%.[13] These financial statements were published on multiple occasions during the Class Period. Indeed, Standard & Poor's repeatedly published tables showing that Enron's effective tax rate was significantly lower than its peer companies.[14] It is axiomatic that if Enron was paying much less in taxes, this would by necessity leave more to net income. Thus, the markets did know that by lowering its effective tax rate – as opposed to increasing income from operations—Enron was increasing its net income.[15] See, e.g., Enron Corp. 2000 Annual Report F-3, F-8 (2000). To the extent that plaintiffs contend that the specific details of the SSTs should have been disclosed, they point to no support. There is no precedent for the proposition that a company such as Enron must disclose the particulars of every single transaction.[16] Indeed, the Examiner acknowledged that, to the extent Enron's accounting for the SSTs was correct, Enron's disclosures would have been adequate. 2d Report, App. D at 69.

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[13] A company's effective tax rate is calculated by dividing that company's income tax payments by its earnings before taxes.

[14] See, e.g., Standard & Poor's, Income Statement Statistics for Gas Pipeline Companies, (June 1999). Included in this report are the elements needed to calculate a particular company's effective tax rate, namely income taxes and earnings before taxes. Enron's then effective tax rate was 18.3%. See also, e.g., Standard & Poor's, Income Statement Statistics for Gas Pipeline Companies, (Feb. 1999) (including information showing that Enron's effective tax rate for the 12 months ending September 30, 1998 to be 21.4%; JCT Report, App. B at B-106 (showing Enron's average effective tax rate between 1998 and 2000 was 19.9%, while based on public information that of the Fortune Pipeline Group was 37%.).

[15] This same data also was widely disseminated in the very analyst reports cited in the Amended Complaint (Am. Compl. ¶¶ 227, 249, 268, 270, 285, 321, 769). See, e.g., CIBC World Markets, Enron Corp. March Quarter Exceeds Expectations, 5 (Apr. 12, 2000); Salomon Smith Barney, Enron Corp. EPS Up as Online Trading Boosts Wholesale Energy Volumes, 2 (July 24, 2000); Lehman Bros., Enron Corp. Franchise Position Highlighted by Results, 3Q EPS Up 26%, 1 (Oct. 18, 2000); Salomon Smith Barney, Enron Corp. Wholesale Engine Running on Full Throttle, 2 (Oct. 18, 2000); Credit Suisse First Boston Corp., Enron Corp. Analyst Meeting Shows Power of ENE Platforms for Growth, 5, 7 (Jan. 26, 2001); Merrill Lynch, Enron Corp. Raising the Bar Again, 4 (Apr. 18, 2001).

[16] In addition, plaintiffs' assertion that FAS 131 and 17 C.F.R. § 229.303(3) required that ***Enron*** reveal the SSTs is inconsistent with an allegation of scienter as to the DB Entities. See Pl. Mem. at 21 & n.14. First, these provisions only relate to ***Enron's*** disclosure duty. The DB Entities did not craft and did not play a role in what or how Enron disclosed. Moreover, the Examiner, having considered all of the FAS rules nowhere deemed these rules to be applicable. Perhaps that is because these rules would only apply if the Enron Tax Department qualified as an operating segment, which it does not.

That ***Enron's*** alleged decision to use the SSTs to manipulate earnings does not plead fraud against the DB Entities is confirmed by plaintiffs' cases. For example, In re Terayon Communications Systems, Inc. Securities Litigation, No. C 00-01967 MHP, 2002 U.S. Dist. LEXIS 5502, at *21-22 (N.D. Cal. Mar. 29, 2002) (Pl. Mem. at 15), actually supports the conclusion that DBTC's involvement in the SSTs was neither unlawful nor fraudulent. In Terayon, plaintiffs alleged, among other things, that where Shaw and Rogers (the company's largest customers and shareholders) purchased an unusually large number of modems and the ***company*** issued its first and only press release pre-announcing revenues in excess of analysts' estimates, plaintiffs adequately pled a claim that the ***company*** manipulated the sale to overshadow the negative impact of a news article concerning other aspects of the company. 2002 U.S. Dist. LEXIS 5502, at *21. The court held that these allegations were sufficient to maintain a claim against the ***company***. Id. Shaw and Rogers, however, were not even defendants in the action and the court made no suggestion that their actions were in any way fraudulent. Id. Thus, how ***Enron*** chose to account for the SSTs does not plead fraud against the DB Entities.[17]

[17] The type of accelerated sales allegedly made in Terayon are sometimes referred to as "channel stuffing." A company's realization of earlier earnings through activities such as "channel stuffing" is not inherently fraudulent. "Channel stuffing" is "'overselling' products to distributors with the knowledge that they would not be able to resell the products to end-users at rates consistent with the company's own sales." Berger v. Compaq Computer Corp., 257 F.3d 475, 477 (5th Cir. 2001). Courts have concluded that the activity itself is not unlawful; rather, it is the way the channel stuffing activity has been misrepresented by companies in their financial statements and other statements to the public that may give rise to a Section 10(b) and Rule 10b-5 claim. See, e.g., Greebel v. FTP Software, Inc., 194 F.3d 185, 202 (1st Cir. 1999) ("There is nothing inherently improper in pressing for sales to be made earlier than in the normal course . . . ."); Tracinda Corp. v. DaimlerChrysler AG, 197 F. Supp. 2d 42, 81–82 (D. Del. 2002) ("At least one circuit, the Ninth Circuit, has rejected channel stuffing claims as speculative hindsight.") (citations omitted); In re Delmarva Sec. Litig., 794 F. Supp. 1293, 1307 & n.22 (D. Del. 1992) (channel stuffing allegations were nothing more than an inactionable allegation of corporate mismanagement). Indeed, to hold the company's customers or business partners somehow liable for engaging in arm's-length transactions, which ***the company*** used to misrepresent its financial statements would be directly at odds with Central Bank.

Plaintiffs next posit that "[v]iolating the Tax Code to inflate financial results runs afoul of Rule 10b-5." Pl. Mem. at 15–16.[18] Once again, however, plaintiffs ignore the public facts that confirm that the SSTs were not fraudulent devices designed by the DB Entities to violate the Tax Code.

First, the SSTs were specifically designed to comply with the Tax Code, because otherwise neither Enron nor the DB Entities would achieve the business purpose of the transactions. The IRS also has nowhere challenged the transactions.[19] Second, the DB Entities (which included public companies) disclosed the SST structures to their banking regulator prior to any dealings with Enron (3d Report, App. G at 19 n.71) ***and*** implemented various of the transactions for the bank's own account. 3d Report, App. G at 18–19 & n.71, 84–85. Third, the SST structures were vetted by tax experts from nationally recognized law firms and nationally recognized tax accountants separate from the Andersen audit team. Id. at 15–16. No party designing fraudulent transactions would take such steps. Finally, as noted above, Enron—and rating agencies and analysts—disclosed its reduced effective tax rate and its correspondingly increased net income. Such public disclosure belies any idea of fraud.

Moreover, whether the SSTs as implemented by Enron complied with the business purpose rule under the tax laws (Pl. Mem. at 16–18) and could thus be subject to challenge as "sham" transactions also does ***not*** suggest that they were ***fraudulent***. Indeed, the idea of "sham"

[18] Plaintiffs' cases are entirely inapposite because they all involve misrepresentations concerning actual tax liabilities. In re CINAR Corp. Sec. Litig., 186 F. Supp. 2d 279, 285 (E.D.N.Y. 2002) (alleging company made public announcements misrepresenting the company's potential tax liability for its false attribution of works by American authors to Canadians to receive tax benefits); Ritchey v. Horner, 244 F.3d 635, 637 (8th Cir. 2001) (alleging claim for misrepresentations concerning tax liabilities); Gerson v. Rapoport, 651 F. Supp. 395, 396, 399 (N.D.N.Y. 1987) (RICO claim alleging failure to disclose substantial tax liability and ongoing tax evasion scheme in connection with privately owned company stock sale). As needed, the SSTs did not hide actual tax liabilities, nor did Enron's reporting of the final SSTs mask any of Enron's tax liabilities.

[19] Indeed, as to Project Cochise, the IRS has already decided to propose no adjustments. JCT Report at 157. As to Project Teresa, the Examiner acknowledged that there will be no IRS challenge. 2d Report, App. J, Annex 4 at 26.

under the tax laws is wholly unrelated to this Court's use of the term in the December Order, (see, e.g., 235 F. Supp. 2d at 614) and its colloquial meaning. Under the sham transaction doctrine, where a transaction is eventually treated as a "sham-in-substance" for violating the business purpose rule, the taxpayer (Enron) is required to return the claimed tax benefits and, to the extent that the taxpayer was ***negligent*** in failing to comply with the business purpose rule, the court may impose interest penalties. That a transaction is so disallowed has ***nothing*** to do with fraud. See generally, Weiner v. United States, 255 F. Supp. 2d 673, 678–82 (S.D. Tex. 2002) (discussing the business purpose rule and the background of a "sham" transaction in the tax context); 131 Main Street Assocs. v. Manko, 897 F. Supp. 1507, 1518 (S.D.N.Y. 1995) (distinguishing sham-in-substance from sham-in-fact).[20]

Similarly inapposite is In re Lernout & Hauspie Securities Litigation, 236 F. Supp. 2d 161, 171 (D. Mass. 2003). Pl. Mem. at 27 & n.20. In Lernout, the court held that plaintiffs stated a claim based on the defendants' substantial participation in a scheme that did not involve

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[20] In Manko, the court insightfully distinguished a "sham-in-substance" from fraud:

> [i]t is clear that tax shelters can be risky ventures for reasons ***wholly unrelated to fraud***. . . . One common reason, litigated . . . is that the tax authorities simply disagree with the taxpayer that a given transaction falls within the meaning of one of the tax code's terms of art . . . . ***This potential for disagreement over the merits of a given transaction for tax purposes arises out of the so-called 'sham-in-substance' doctrine***, which requires courts and tax authorities 'to look beyond the form of the transaction and to determine whether its substance is of such a nature that expenses or losses incurred in connection with it are deductible . . . . If a transaction's form complies with the Code's requirements for deductibility, but the transaction lacks the . . . economic substance that form represents, then expenses or losses incurred in connection with the transaction are not deductible.'

897 F. Supp. at 1518 (citations omitted; emphasis added). In contrast, the so-called "sham-in-fact" involves a challenge by tax authorities

> not because they dispute the taxpayer's characterization of the underlying transaction for tax purposes, but because the transaction itself is not what the taxpayer represents it to be . . . . Things being other than what they are claimed to be is not a matter of ***differing interpretations***; it is the essence of fraud.

Id. (emphasis added); accord Compaq Computer Corp. v. Commissioner, 277 F.3d 778, 781 n.1 (5th Cir. 2001); Weiner, 255 F. Supp. 2d at 678–79 (citing Compaq).

arm's-length transactions. 236 F. Supp. 2d at 175–76. Even assuming this case was correctly decided, it is nonetheless inapposite as to the DB Entities.

Lernout involved a venture capital fund ("FLV") which was formed by L&H and an insurance company ("Mercator"). 236 F. Supp. 2d at 167. Plaintiffs alleged specific facts showing (i) L&H, FLV and Mercator disregarded corporate formalities; (ii) L&H entered into "strategic partnerships" for purported software licensing agreements with "shell" companies that had "no employees, financial resources or technical expertise"; and (iii) that the "strategic partnerships" never involved a true passing of risk. Id. at 166–168, 174. Based on these allegations, the court held that plaintiffs sufficiently pled that FLV and Mercator substantially participated in the scheme. Id. at 175–176.

Here, plaintiffs have not and cannot allege these failings as to the SSTs. The Examiner's Reports nowhere found that corporate formalities were disregarded in any of the SSTs. Moreover, Enron and the DB Entities invested real and substantial assets into the companies created as part of the SSTs and the transactions created real and ongoing tax and economic risk for the parties. The presence of real and ongoing economic risk supports the business purpose of the transactions.[21] Moreover, unlike the scheme in Lernout, the effects of the SSTs on Enron's earnings were disclosed through public documents showing the company's disproportionately low effective tax rate.

[21] Indeed, what Plaintiffs studiously ignore in their jaundiced and inaccurate descriptions of the SSTs (Pl. Mem. at 9–12) is that the Examiner nowhere labeled any of the SSTs fraudulent. The Examiner's criticism of three SSTs was limited to Enron's decision to use short amortization periods or small valuation allowances to accelerate the tax benefits conferred by the transactions. With regard to the passing of risk, plaintiffs again ignore that the Examiner never accused a DB Entity of not accepting real and on-going risk with respect to each SST. See DBE Mem. at 17–18.

Accordingly, plaintiffs have failed to plead facts showing that the SSTs as designed by the DB Entities were in any way fraudulent or that any DB Entity engaged in a fraudulent scheme, course of business or contrivance through the SSTs.

B. Plaintiffs Fail To Plead That Any Of The DB Entities Made Material Misstatements Or Omissions Concerning Enron Or Enron-Related Securities

Plaintiffs have failed to allege specific facts showing that the DB Entities made any material misstatements or omissions concerning Enron. In the December Order, this Court explained that it only examined the "specifically and successfully pled" allegations in the Newby Complaint, "[r]ather than focusing upon deficiencies . . . especially conclusory or boiler plate allegations, of which the Court agree[d] there [were] many." 235 F. Supp. 2d at 692. Thus, where plaintiffs allege that the DB Entities made material misstatements or omissions in analyst reports and offering materials based upon their participation in "implementing" the SSTs, they must "specify the statements contended to be fraudulent, identify the speaker, state when and where the statements were made, and explain why the statements were fraudulent." In re BMC Software Sec. Litig., 183 F. Supp. 2d 860, 865 n.14 (S.D. Tex. 2001 (Harmon, J.) (quoting Williams v. WMX Techs., Inc., 112 F.3d 175, 177 (5th Cir. 1997)). The Amended Complaint, however, fails to meet this heightened pleading standard. Instead, plaintiffs continue to rely upon bare quotes from analyst reports (see, e.g., Am. Compl. ¶¶ 127, 131, 146, 152, 159, 243, 253, 257, 796) without explaining which statements were misleading and why such statements were false or misleading ***when*** made by any DB Entity.

The problem for plaintiffs is that there is absolutely no evidence that the DB Entities knew or should have known the specific accounting decisions that Enron made in implementing the SSTs. Thus, nowhere did the Examiner ever find that the DB Entities had anything to do with how Enron set amortization periods, tax reserves or valuation allowances relating to the

SSTs, nor did the Examiner find that the DB Entities knew what reserves or allowances had been set. Thus, there is no link between any alleged wrong by Enron in connection with the SSTs and the DB Entities.

Moreover, as noted above, what was publicly known was that Enron's publicly disclosed earnings were increased by a publicly disclosed and disproportionately low effective tax rate. For example, a June 9, 1999 analyst report (cited in the Newby Compl. ¶ 153; Am. Compl. ¶ 153) made specific reference to Enron's low tax rate:

> Enron has a low tax rate thanks to $1.4 billion in net operating loss carryforwards . . . Also, equity earnings of international subsidiaries are not subject to U.S. tax. They are predominantly noncash since Enron is reinvesting its earnings from those projects locally, and they are in tax advantaged structures.

See Certain Defendants' Joint Brief Relating To Enron's Disclosures at 236 (citation omitted) (S.D. Tex. May 8, 2002) (docket no. 735 in the Newby case).

No facts relating to the SSTs show that at the time DB and DBSI issued analyst reports they knew or were severely reckless in not knowing that any of its opinions about Enron were material misstatements or omissions. See DB Mem. at 14–18. Indeed, all of the analyst reports cited include information that had already been released or announced by Enron and were consistent with other research reports cited by Plaintiffs. Unlike other banks' reports, DB's and DBSI's research reports maintained a consistent "buy" recommendation, never raised Enron to a higher level and stopped following Enron in 2000. Plaintiffs also have failed to plead facts sufficient to show that any of the DB or DBSI research opinions were released with an intent to defraud. As DB discussed in its motion to dismiss the Newby Complaint, opinions are generally not actionable because they are not statements of ***fact***. DB Mem. at 17–18. Accordingly, Plaintiffs have failed to allege that any of the DB Entities made any material misstatements or omissions concerning any public offering of Enron or Enron-related securities.

C. Plaintiffs Have Once Again Failed To Plead Facts Giving Rise To A Strong Inference Of Scienter As To The DB Entities

"Under the PSLRA, it is not enough to particularize false statements or fraudulent omissions made by a corporate defendant. Plaintiffs must also particularize intent allegations raising a 'strong inference of scienter.'" Goldstein, 340 F.3d at 249. Furthermore, allegations of motive and opportunity even when sufficiently particularized alone are insufficient to withstand dismissal. Id. at 250.

Indeed, the Examiner's Reports establish that the DB Entities had every reason to believe that the SSTs were GAAP compliant and certainly not fraudulent, thus undercutting any basis for scienter. Among the public facts ignored by plaintiffs are that:

(i) Prior to presenting the SSTs to Enron, the DB Entities vetted the structures with accountants at Andersen who were completely unrelated to Enron's auditors from Andersen. 3d Report, App. G at 15, 85–89. Andersen issued SAS-50 letters confirming the accounting treatment for the SSTs. Id. at 15–16.

(ii) Each SST also was vetted by reputable outside counsel which provided legal memoranda confirming the tax law effects of each transaction. Id.

(iii) The SST structures that became Projects Teresa, Steele and Cochise were all presented to the Federal Reserve Bank of New York which was the primary regulator for DBTC. 3d Report, App. G at 18–19 & n.71, 84. This was done ***before*** these structures were presented to Enron. Id.

(iv) The DB Entities (which included Bankers Trust Company—then a public company) actually implemented various of the SST structures. 3d Report, App. G at 84–85.

(v) With respect to ***every*** SST, Enron had to seek review and approval by ***its*** outside auditor, and at least one and sometimes more of its outside counsel and were presented to

Enron's Executive Committee and Finance Committee. See, e.g., id. at 18; 3d Report, App. C at 22 & n.92; see generally, 3d Report, App. G at 27–57.

(vi) Each SST had the indicia of a legitimate arm's-length business transaction as the DB Entities made investments in each transaction, as a result of which money properly changed hands and there was a real and continuing transfer of risk (which is evident from the fact that the DB Entities' investment in any SST was reliant on expected, but not guaranteed, tax results).[22] See 2d Report, App. J at 80–83; 3d Report, App. G at 18; see generally, id. at 56.

(vii) The effect of the SSTs was reflected in Enron's publicly filed financial statements.[23]

(viii) As noted above (see supra at 14), even with the benefit of hindsight, the Examiner only reached a limited and highly qualified opinion that three of the SSTs did not comply with GAAP, an opinion the Examiner acknowledged rested on a difference in "professional judgment" from the legal opinions provided to Enron by its outside counsel.

Thus, the DB Entities were in no way reckless in believing that the SSTs complied with GAAP or the Tax Code. Moreover, plaintiffs' allegations that the SSTs, in fact, violated GAAP are conclusory and are otherwise contradicted by the public record:

(i) The IRS has not made any filing in the Enron bankruptcy proceedings challenging the legitimacy of any of the SSTs.

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[22] There also is ***no*** evidence that Enron and the DB Entities engaged in any verbal assurances, either explicitly or implicitly, whereby Enron relieved any risk from the DB Entities, or that the DB Entities ever attempted to otherwise hedge their risk in any of the SSTs – factors this Court deemed strong indicia of the presence of scienter and the absence of arm's-length transactions as to other defendants. See December Order, 235 F. Supp. at 696–99, 702–03.

[23] This list of facts, all ignored by plaintiffs, also undercuts any attempt by plaintiffs to plead fraud or scienter via the so-called Cochise Planes. (Pl. Mem. at 9.) All that plaintiffs offer is the bare assertion that Project Cochise was a fraud. Plaintiffs wholly ignore the Examiner's findings that there was a real passing of risk to the DB Entity involved with respect to real assets (airplanes) for which there was a liquid market, and that the gain reported by Enron would have been recognized upon the sale of the planes to any third-party. DBE Mem. at 18–19. These findings show that these transactions bear the indicia of arm's-length transactions and are markedly different from the types of transactions which this Court has held may support allegations of fraud or scienter. See December Order, 235 F. Supp. 2d at 580.

(ii) Far from being concealed, Project Teresa was in fact a registered tax shelter. JCT Report at 173 ("Enron received a tax shelter registration number in connection with Project Teresa.").

(iii) Plaintiffs' assertion that Maliseet, the real estate investment trust ("REIT") formed in connection with Project Cochise was "phony" (Pl. Mem. at 9), completely ignores the IRS's finding that Maliseet was in fact properly formed as a REIT. Having determined this and that Maliseet properly operated as a REIT for the tax years under review, the IRS stated that it "would not review Project Cochise any further and would propose no tax liability adjustments relating to Project Cochise." JCT Report at 157.[24]

In addition, the fact that the Examiner opined that Projects Teresa, Cochise, and Steele violated GAAP does not in any way show scienter.[25] See, e.g., 3d Report at 35, 42–43. In addition to being limited and highly qualified, the Examiner's conclusions directly contradict the opinions of both Andersen and the law firms that represented Enron in connection with the SSTs that each was GAAP compliant. As the Examiner acknowledged, his opinions regarding GAAP compliance reflected nothing more than a difference of "professional judgment" between the

[24] Plaintiffs' allegations attempt to spin the findings of Congress and the Examiner, as well as newspaper articles, to support their bare allegations that the SSTs failed to comply with GAAP and that the DB Entities had scienter. See, e.g., Am. Compl. ¶ 797.7. As more fully discussed in the DB Entities' Motion to Dismiss, however, plaintiffs do not merely finesse words, but rather refashion facts to support their allegations. See DBE Mem. at 19–23. In fact, neither Congress, the Examiner, nor any newspaper article has found the SSTs to be fraudulent or passed judgment on the DB Entities' state of mind. Moreover, the JCT Report in fact acknowledges that the SSTs "were designed to satisfy the literal requirements of the corporate tax laws." JCT Report at 109. Ultimately, the JCT Report recommended that Congress consider changes to the tax laws, reconfirming that the SSTs were in compliance with the tax laws as they existed at the time the transactions were designed and implemented. It is a matter of public record that Congress has not chosen to change the applicable tax laws.

[25] Although the Examiner also concluded that Project Tomas probably did violate GAAP, he did so solely on the basis of "***Enron's*** failure to record any Valuation Allowance or Tax Cushion in connection" with the transaction. 2d Report, App. J at 88. As noted by the Examiner, decisions regarding Enron's allocation of tax reserves did not and would not involve the DB Entities. See 3d Report, App. G at 85. Moreover, the Examiner never formed an opinion as to whether "the tax benefits claimed from the Tomas Transaction could withstand scrutiny by the IRS and the courts." Id. As noted above, the IRS has not appeared in the bankruptcy proceeding to challenge any of the SSTs, including Project Tomas.

Examiner and Enron's professionals which is hardly sufficient to sustain a finding of scienter as to the DB Entities. Indeed, as the Fifth Circuit made clear in Lovelace v. Software Spectrum Inc., 78 F.3d 1015, 1020–21 (5th Cir. 1996), the term GAAP "encompass[es] a wide range of acceptable procedures" such that "a difference in judgment about GAAP does not establish conscious behavior on the part of Defendants."

Plaintiffs' assertion that the DB Entities may not properly argue reasonable reliance on the advice of outside experts (Pl. Mem. at 17) contradicts this Court's March 2003 opinion dismissing the Outside Directors and Officers. In that opinion, this Court held that "Lead Plaintiff has not provided any facts that were presented to and that led or should have led an Outside Director to know or recklessly disregard that there was fraudulent accounting at Enron." March Order, 258 F. Supp. 2d at 629.

Here, the DB Entities were not insiders and were provided with reasonable outside expert assurances that the SSTs were valid transactions (and later understood that Enron had vetted the transactions with its outside auditors and outside counsel). Indeed, based on these outside expert opinions, the DB Entities vetted these transaction structures with their ***federal regulator*** and implemented some of them for themselves. Just as Enron's Outside Directors were not reckless in failing to discern the wrongful activities of various Enron insiders, the DB Entities cannot be deemed reckless in failing to discern that Enron was not properly accounting for the SSTs.[26]

[26] Plaintiffs also claim that the amount of DBTC's fees were linked to the magnitude of the accounting benefits realized by Enron, such that DBTC knew how Enron was accounting for the SSTs (Pl. Mem. at 21.) The fee letters published in the JCT Report belie this allegation. DBTC's fees were set at closing, with pre-set portions to be paid out over time. To the extent an actual change in laws or accounting rules ***reduced*** the benefits allowed to Enron in the transactions, DBTC's fees would be reduced. See, e.g., JCT Report, App. B at B-215, B-260. Other than in that limited circumstance, involving a public change in law of accounting practice, DBTC's fees in no way indicated to DBTC the precise accounting Enron was employing to implement the SSTs. Thus, there was no adjustment to the fees paid based on how Enron actually benefited from the transactions. Moreover, an allegation concerning a defendant's compensation or fees would be insufficient to plead motive. See December Order, 235 F. Supp. 2d at 573. Furthermore, even if such a pleading were sufficient to plead motive, this Court and the Fifth Circuit have

Another purported indicia of scienter offered by plaintiffs actually supports the opposite conclusion. Plaintiffs assert that Enron and DBTC "agree[d] to secrete their actions from scrutiny" by going so far as to "provide a contractual clause ***nullifying*** Project Steele if it ever had to be disclosed." Id. (emphasis in original). As the actual agreement published in the JCT Report states, however, Enron and DBTC entered a non-binding exclusivity agreement, which provided that only the letter's ***exclusivity provisions*** were non-binding if the transaction was required to be registered as a "tax shelter." JCT Report App. B-200–B-201.[27] Thus, by its terms, this provision did not nullify Project Steele if tax shelter registration was required, it simply allowed Enron to do the transaction with someone other than DBTC.[28] Moreover, the assertion that registration of a particular SST as a tax shelter would dissuade DBTC or Enron from engaging in that transaction is belied by the fact that Project Teresa ***was*** registered as a tax shelter.

Plaintiffs' allegation that the SSTs did not have a valid business purpose is also insufficient to plead scienter. Pl. Mem. at 15-18. Whether the SSTs are ultimately found to have violated the business purpose rule of the tax law is irrelevant to the Court's analysis of scienter. "Good faith reliance on professional advice concerning tax laws is a defense" to a tax court's preliminary finding of negligence provided that the taxpayer's reliance is "objectively

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unequivocally held that motive and opportunity standing alone are insufficient to give rise to a strong inference of scienter. Goldstein, 340 F.3d at 250.

[27] "If any law enacted after the date of this letter shall require that the Transaction be registered as a 'tax shelter' . . . then, on the effective date of such law, ***this letter*** shall be null and void." (JCT Report App. B-200–B-201). The suggestion that once Project Steele had closed, the parties would declare the transaction null and void if it had to be publicly disclosed is simply wrong and wholly unsupported by ***any*** facts in the JCT or Examiner's Reports.

[28] The Amended Complaint quotes from a news article for the assertion that Project Steele "included an 'unusual provision nullifying the deal' if it had to be disclosed." Am. Compl. ¶ 797.15. The article is presumably one journalist's spin on the JCT Report and, as shown, is simply wrong. Cf. Am. Compl. ¶ 797.15; with JCT Report at 137 & n.313. This article also only opines on the need for new regulations to address concerns raised by what is actually ***allowed*** by current IRS regulations. Mike France, The Rise of the Wall Street Tax Machine, BusinessWeek, Mar. 31, 2003, at 84–87.

reasonable". Chamberlain v. Commissioner, 66 F.3d 729, 732–33 (5th Cir. 1995) (reversing imposition of interest penalty and tax court's finding of negligence where taxpayer reasonable relied on expert tax opinion). Here, it was Enron, as the taxpayer, and not DBTC that relied on Enron's outside tax counsel's opinion that the SSTs "should" be valid. That DBTC relied upon tax and accounting opinions regarding the SST structures presented to Enron belies any inference that any DB Entity was severely reckless in not knowing that the SSTs could be treated as a "sham-in-substance" much less a "sham-in-fact." DBE Mem. at 4, 16–17.[29]

Thus, even with a now voluminous public record, plaintiffs still have not pled facts giving rise to a strong inference of scienter as to any of the DB Entities—a failure that mandates dismissal of their Section 10(b)/Rule 10b-5 claim with prejudice.

D. The Fraud-On-The-Market Theory Does Not Apply To The DB Entities' Activities In Connection With The SSTs

Plaintiffs argue that they may invoke the fraud-on-the-market theory by simply alleging that the SSTs enabled Enron to present a falsely positive picture of Enron's financial condition. Pl. Mem. at 26. As this Court has explained, however, the fraud-on-the-market theory presumes (i) investors rely on the price of a company's stock, and (ii) the price of a company's stock reflects all of the available material information about a company. December Order, 235 F. Supp. 2d at 574.

[29] Similarly unavailing are two other allegations plaintiffs now advance. As DB has previously established, the involvement of any DB Entity in LJM2 cannot support an inference of scienter because, as this Court recognized in its December Order, DB was a passive limited investor in LJM2. See December Order, 235 F. Supp. 2d at 704; DB Reply at 9-12. Still missing from the Amended Complaint are any specific factual allegations regarding documents, meetings or other facts that would support the idea that any DB Entity (even as a member of the limited partners' "advisory" committee) was ever given a window into the alleged fraud perpetrated by Enron, let alone actively participated in that alleged fraud. Plaintiffs also now claim that "[b]y 2000, Deutsche Bank learned Enron's undisclosed off-balance sheet debt was significantly higher than anyone knew." (Pl. Mem. at 25.) Once again, there is no factual support for this. Indeed, to the contrary, the Examiner's Report upon which plaintiffs purport to rely (citing 3d Report, App. G at 22-23) actually found that "[i]n light of Enron's prior assurances [received from Enron] BT/Deutsche was surprised to learn that additional obligations of $25.116 billion were not shown on Enron's balance sheet." 3d Report, App. G at 26.

DBTC's and DB's involvement in structuring the SSTs, as even Plaintiffs concede (Pl. Mem. at 8), were not in connection with the purchase or sale of securities and did not have an effect on the material information about Enron. Even after Enron and its accountants and tax advisors finalized the SSTs the market was not affected. It was only after Enron and its accountants reported earnings from the SSTs that allegedly material information entered the marketplace upon which investors could be presumed to rely. The market, however, was never made aware of DBTC's or DB's involvement in structuring the SSTs. See Nathenson v. Zonagen Inc., 267 F.3d 400, 414 (5th Cir. 2001) ("a fraud-on-the-market theory may not be the basis for recovery in respect to an alleged misrepresentation which does *not* affect the market price of the security in question.") (emphasis in original). The only nexus between the SSTs and the market price of Enron or Enron-related securities was the accounting treatment that Enron and its accountants determined was the appropriate accounting for the transactions – which treatment, as noted above, was in fact then reflected in Enron's publicly disclosed effective tax rate. DBE Mem. at 24.

In addition, plaintiffs' allegations treat the actions of DBTC and DB on the one hand and the actions of Enron and its accountants on the other as if they were one and the same. This Court, however, rejected a similar theory espoused by the State Attorneys General which argued that "participants in a scheme to defraud, no matter how small, are liable for other participants' conduct in furtherance of the scheme even if the participants did not commit a key act that ***itself*** violated § 10(b) and Rule 10b-5." December Order, 235 F. Supp. 2d at 589 n.31 (emphasis added). As the Supreme Court has already made clear, under Section 10(b), the acts of ***each*** defendant must be evaluated ***separately*** – defendants are not liable for the "acts that are not ***themselves*** manipulative or deceptive within the meaning of the statute." Central Bank of

Denver, N.A. v. First Interstate Bank of Denver N.A., 511 U.S. 164, 177–78 (1994) (emphasis added).

Thus, plaintiffs' allegation that the SSTs "'operated to present a falsely positive picture of Enron's condition . . . thereby artificially inflating the value of Enron's publicly traded securities'" (Pl. Mem. at 26, citing December Order, at 693) is insufficient for the purpose of invoking the fraud-on-the-market theory because it only refers to actions by Enron and its accountants. In plaintiffs' own words, the SSTs allegedly served no purpose other than "enabling Enron to report the potential benefit of speculative future tax deductions in an erroneous and misleading manner." Pl. Mem. at 3, quoting 3d Report, App. G at 3–4. Under plaintiffs' own characterization, it was the acts of the alleged enablee, Enron, not those of the alleged enablors, DBTC/DB, that were relied upon by the investors under the fraud-on-the-market theory. Accordingly, the fraud-on-the-market theory may only be invoked to presume reliance as to the acts of Enron and its accountants, not those of DBTC or DB.

E. Plaintiffs Fail To Plead Loss Causation As To The DB Entities

As the DB Entities showed in their moving papers, plaintiffs fail to plead loss causation because they do not allege that any DB Entity was a direct causal link between any material misstatement or omission and their losses. DBE Mem. at 23–26. Plaintiffs now attempt to circumvent the requirement that they show a "'direct causal link between the misstatement and [their] economic loss'" (December Order, 235 F. Supp. 2d at 573 n.13 (citation omitted)) simply alleging that "Deutsche Bank was a primary participant in the fraudulent scheme that caused plaintiffs' losses." Pl. Mem. at 27. But as noted above, the claim really is that the DB Entities simply facilitated Enron's acts by presenting the SST structures which ***Enron*** then implemented and chose to either disclose or not as it did.

Precisely this type of aiding and abetting allegation was carefully examined and rejected by a district court which observed that "[n]o matter how a 'scheme' is defined, Central Bank dictates that only those participants who commit 'primary violations' of the securities laws may be held liable; those who merely facilitate or participate cannot. . . . in this case, the shareholders . . . were damaged by their reliance on statements and material omissions made by Homestore, not the 'scheme' itself." In re Homestore.com, Inc. Sec. Litig., 252 F. Supp. 2d 1018, 1038 (C.D. Cal. 2003). Based on the court's careful examination of scheme liability cases the court found no support for the proposition that a business partner may be held primarily liable for material misstatements or omissions made by a company "no matter how much [the business partner] assisted or participated in transactions that led to that statement or omission." 252 F. Supp. 2d at 1039.

Indeed, in the cases where courts have held that plaintiffs stated a claim under Rule 10b-5(a) or (c) the defendants were alleged to have engaged in a scheme that directly caused the plaintiffs' injury. See, e.g., SEC v. Zandford, 535 U.S. 813, 815 (2002) (alleging broker with management discretion over securities account engaged in deceptive conduct by engaging in unauthorized trades for his own benefit without disclosure to customer).

Here, at most, plaintiffs have alleged no more than the Examiner—that the DB Entities may have somehow assisted or participated in allegedly wrongful acts by Enron insiders. That is not actionable fraud. Consequently, even taking all of plaintiffs well-pled allegations as true, plaintiffs have failed to plead loss causation as to the DB Entities. Therefore, their Section 10(b)/Rule 10b-5 claim should be dismissed with prejudice.

POINT III

PLAINTIFFS HAVE FAILED TO STATE A CLAIM UNDER SECTION 12(A)(2) AS TO DBSI

A. Plaintiffs Fail To State a Claim Under Section 12(a)(2) Because They Do Not Allege That The Four Note Resales Involved A "Prospectus"

The Amended Complaint only asserts a Section 12(a)(2) claim as to DBSI in connection with four Rule 144A/Regulation S ("Reg S") private resales (the "Four note resales"). DBE Mem. at 26; Am. Compl. ¶ 1016.4. It is undisputed that the Four note resales were exempt from the registration requirements of Section 5 of the 1933 Act. DBE Mem. at 26–27; Pl. Mem. at 32; 17 C.F.R. §§ 230.901–905; 17 C.F.R. 230.144A. Nonetheless, in a blatant attempt to extend the protections of the U.S. securities laws to transactions which the SEC has expressly exempted from the coverage of the registration requirements of the 1933 Act, plaintiffs argue that sales made to purchasers on the Luxembourg Exchange were in fact public offerings. Am. Compl. at ¶ 641.1 ("These securities were all listed and traded upon the Luxembourg stock exchange"). In support, plaintiffs cite two cases from the Fifth Circuit, both of which, however, only examined whether the subject sales were exempt from the ***registration requirements*** of Section 5 of the 1933 Act. See Hill York Corp. v. American Int'l Franchises, Inc., 448 F.2d 680, 687 (5th Cir. 1971); Doran v. Petroleum Mgmt. Corp., 545 F.2d 893, 897 (5th Cir. 1977).

Plaintiffs cite only one case for the proposition that sales made pursuant to Reg S may be treated as public offerings. See Pl. Mem. at 32 n.26, citing Sloane Overseas Fund, Ltd. v. Sapiens Int'l Corp., N.V., 941 F. Supp. 1369 (S.D.N.Y. 1996). That court, however, concluded that a Reg S offering may be subject to Section 12(a)(2) only after misreading Gustafson v. Alloyd Co., Inc., 513 U.S. 561 (1995). Sloane, 941 F. Supp. at 1376 & n.9. Specifically, the court interpreted Gustafson to define "prospectus" under Section 12(a)(2) as nothing more than documents that "relate to public offerings." Id., citing Gustafson, 513 U.S. at 577.

To the contrary, Gustafson stated that "a document is not a prospectus within the meaning of [Section 10 of the 1933 Act] if, absent an exemption, it need not comply with § 10's requirements in the first place." 513 U.S. at 569. The relevant "requirement" in Section 10 is that a prospectus "shall contain the information contained in the ***registration statement***." Id. (emphasis added). Therefore, the Court concluded, "whatever else 'prospectus' may mean, the term is confined to a document that, absent an overriding exemption, must include 'the information contained in the registration statement.'" Id.

Since the contract that accompanied the sale of securities in Gustafson "was not required to contain the information contained in a registration statement," it was not a "prospectus" under Section 10. Id. Similarly, since an offering memorandum accompanying a Reg S offering is ***not*** required to contain information contained in a registration statement, it is also not a prospectus under Section 10 and, by extension, Section 12.[30] Thus, as a matter of law, sales made pursuant to Reg S are not public offerings. Accordingly, plaintiffs cannot assert a claim against DBSI for any sales made pursuant to Reg S in connection with the Four note resales.

B. Plaintiffs Do Not Have Standing To Bring A Section 12(a)(2) Claim As To DBSI

Standing must exist at the ***commencement*** of a suit. Lujan v. Defenders of Wildlife, 504 U.S. 555, 570 n.5 (1992). ***None*** of the named plaintiffs in the Amended Complaint (Am. Compl. ¶¶ 79–81) are alleged to have purchased from ***any*** of the Four note resales. Instead, plaintiffs claim to have standing because Imperial County Employees Retirement Systems ("ICERS"),

[30] "We conclude that the term 'prospectus' must have the same meaning under §§ 10 and 12." Gustafson, 513 U.S. at 570. Moreover, the overwhelming weight of the case law since Gustafson supports this conclusion. See AIG Global Sec. Lending Corp. v. Banc of Am. Sec. LLC, 254 F. Supp. 2d 373, 389 (S.D.N.Y. 2003) (rejecting argument that Reg S sales are subject to Section 12(a)(2)); In re Sterling Foster & Co., Inc., Sec. Litig., 222 F. Supp. 2d 216, 244 (E.D.N.Y. 2002) ("liability imposed by §12(a)(2) cannot attach unless there is an obligation to distribute the prospectus in the first place.") (citation omitted); Walltree Ltd. v. ING Furman Selz LLC., 97 F. Supp. 2d 464, 470 (S.D.N.Y. 2000) (dismissing Section 12(a)(2) claim because "the Complaint does not allege the existence of a prospectus."). Indeed, even the court in Sloane recognized that Reg S securities sold by sellers like the DB Entities are exempt from the registration requirements of Section 5. 941 F. Supp. at 1377 n.11.

who allegedly purchased Marlin notes, has a motion to intervene pending before the Court.[31] Pl. Mem. at 33. Such logic fails by putting the proverbial cart before the horse—a "motion for intervention under Rule 24 is ***not*** an appropriate device to cure a situation in which plaintiffs may have stated causes of action that they have no standing to litigate." McClune v. Shamah, 593 F.2d 482, 486 (3d Cir. 1979) (citation omitted; emphasis added); see also Chiles v. Thornburgh, 865 F.2d 1197, 1212 (11th Cir. 1989) ("The standing doctrine ensures that a justiciable case and controversy exists between the parties. Intervention under Rule 24 presumes that there is a justiciable case into which an individual wants to intervene.").

Neither of the cases relied upon by ICERs (ICER Mem. at 2) addresses whether intervention may cure a lack of standing in the putative class. Rather, the issue in both cases was whether the lead plaintiff, as opposed to the named plaintiffs, needed to have standing for all claims being asserted by the putative class. See In re Initial Pub. Offering Sec. Litig., 214 F.R.D. 117, 122 (S.D.N.Y. 2002) (concluding that "for a claim to be asserted on behalf of a putative class, . . . only the ***named*** plaintiffs . . . must have standing.") (emphasis added); see also In re WorldCom, Inc. Sec. Litig., No. 02 Civ. 3288 (DLC), 2003 U.S. Dist. LEXIS 8245, at *76 (S.D.N.Y. May 19, 2003) ("The Underwriter Defendants suggest that this Court now require 'a few other plaintiffs to join with NYSCRF as lead plaintiff' in order to address their perception that a lead plaintiff must have standing to bring Sections 11 and 12(a) claims in order for such claims to be filed against them."). Therefore, plaintiffs' lack of standing mandates dismissal of their Section 12(a)(2) claim against DBSI.

[31] IHC Health Plans, Inc. mentioned by Plaintiffs as another potential intervenor (Pl. Mem. at 34) filed a notice of withdrawal from the motion to intervene on October 2, 2003.

CONCLUSION

The DB Entities respectfully request that this Court dismiss with prejudice the Amended Complaint against them, and grant DB, DBSI and DBTC such other and further relief to which they may be entitled.

Dated: October 13, 2003

Respectfully submitted,

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CERTIFICATE OF SERVICE

On October 13, 2003, I caused a true and correct copy of the foregoing document to be served on all counsel by posting said Reply Memorandum of Law in Support of The Deutsche Bank Entities' Motion to Dismiss in PDF format to the http:www.esl3624.com website.

Dated: October 14, 2003

Respectfully submitted,

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