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

2003 OCT 23 P.M. 3:57
U.S. DISTRICT COURT
SOUTHERN DISTRICT
OF TEXAS
United States Courts
Southern District of Texas
FILED
OCT 2 3 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,	§	
Plaintiffs,	§	Civil Action No. H-01-3624 (Consolidated)
v.	§	
ENRON CORP., *et al.*,	§	
Defendants.	§	
THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, *et al.*, Individually and On Behalf of All Others Similarly Situated,	§	
Plaintiffs,	§	
v.	§	
KENNETH L. LAY, *et al.*,	§	
Defendants.	§	

VINSON & ELKINS L.L.P.'S OPPOSITION TO CLASS CERTIFICATION

The susceptibility of this case to class-action treatment hinges on plaintiffs' ability to invoke the fraud-on-the-market theory of presumed reliance. The applicability of that theory with respect to a particular securities fraud defendant, however, depends on facts showing that the defendant communicated a misrepresentation to the relevant market, thereby distorting the market price for the security in question – the integrity of which is presumably relied on by all buyers and sellers of that security. That theory cannot be applied to the claims against V&E in this case because there is absolutely no evidence that V&E communicated any

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misrepresentation to the markets for Enron securities. As a result, Plaintiffs cannot meet their burden under the "rigorous analysis" required for certification of class action fraud cases in the Fifth Circuit.

BACKGROUND

Plaintiffs' Amended Complaint, alleging that V&E violated Section 10(b) of the Securities Exchange Act of 1934, is brought under Federal Rule of Civil Procedure 23 on behalf of "all persons who acquired Enron's publicly traded securities." Amended Compl. ¶ 986. This class of persons, according to Plaintiffs, encompasses "thousands of investors" holding "750 million shares of [Enron] common stock" as well as other Enron securities. Id. ¶ 987.

On May 28, 2003, Plaintiffs filed an amended motion seeking to have this sprawling class certified. Recognizing that individual class members' reliance on misleading statements must be proved in order to establish a cause of action under Section 10(b), and that the reliance element ordinarily bars class certification because it requires proof with respect to each specific plaintiff, Plaintiffs nevertheless argue that class treatment is appropriate. Plaintiffs purport to "avail themselves of the fraud-on-the-market presumption," Amended Mot. for Class Cert. at 26, which *in appropriate cases* permits individual reliance to be assumed, thus removing an otherwise insurmountable obstacle to class certification. V&E explains below that the fraud-on-the-market presumption does not apply here.

ARGUMENT

The burden of proving that a class action is appropriate rests with the proponent of class treatment. Castano v. Am. Tobacco Co., 84 F.3d 734, 740 (5th Cir. 1996). The party seeking certification must satisfy all of the prerequisites for certification under Rule 23(a) and must establish one of the circumstances warranting class certification under Rule 23(b). See

Stirman v. Exxon Corp., 280 F.3d 554, 561-64 (5th Cir. 2002). The Supreme Court and the Fifth Circuit have made it clear that district courts are to conduct a "rigorous analysis" of the Rule 23 prerequisites before certifying a class. Castano, 84 F.3d at 740 (citing Gen. Tel. Co. v. Falcon, 457 U.S. 147, 161 (1982)); Henry v. Cash Today, Inc., 199 F.R.D. 566, 569 (S.D. Tex. 2000). Courts should "treat[] each claim individually and certify[] the class with respect to only those claims for which certification is appropriate." Bolin v. Sears, Roebuck & Co., 231 F.3d 970, 976 (5th Cir. 2000). Plaintiffs' claims against V&E in this case cannot survive such rigorous analysis.

I. Absent a Presumption of Class-Wide Reliance, Individualized Issues of Reliance Predominate in a Securities Fraud Case, Precluding Class Certification.

Certification under Rule 23(b)(3) requires that Plaintiffs establish (1) that common issues of fact and law *predominate* over individual issues, and (2) that a class action is *superior* to other methods of adjudicating Plaintiffs' claims. Fed. R. Civ. P. 23(b); Cash Today, 199 F.R.D. at 570. If a court determines that "the legal or factual questions that qualify each class member's case" will require individualized proof to establish each class member's claim, then the "predominance" requirement is not met. See Amchem Prods. v. Windsor, 521 U.S. 591, 623-24 (1997) (affirming denial of certification of asbestos victim class where causation and damages constituted "disparate questions undermining class cohesion"). These requirements are "far more demanding" than the "commonality" prerequisite of Rule 23(a), Amchem, 521 U.S. at 624, and they are not met by Plaintiffs in this case.

Plaintiffs' Section 10(b) claim against V&E requires proof of reliance by each plaintiff on the alleged fraud in order to establish causation. See Central Bank of Denver v. First Interstate Bank, 511 U.S. 164, 180 (1994). This proximate causal link must be determined on an individualized basis with respect to *every class member's* fraud claims. See Basic, Inc. v.

Levinson, 485 U.S. 224, 242 (1988) ("Requiring proof of individualized reliance from each member of the proposed plaintiff class effectively [prevents] a class action, since individual issues then would . . . overwhelm[] the common ones."). Thus, where causation is at issue, the potential advantages of a class action are completely displaced by miring issues of fact with respect to each class member, precluding certification under Rule 23(b)(3). See Patterson, 241 F.3d at 419. This has led the Fifth Circuit to hold unequivocally that "a fraud class action cannot be certified when individual reliance will be an issue." Castano, 84 F.3d at 745; see also Perrone v. GMAC, 232 F.3d 433, 440 (5th Cir. 2000) (holding class action cannot be certified where "individual reliance is necessary to prove actual damages"); accord Henry Schein, Inc. v. Stromboe, 102 S.W.3d 675, 693-94 (Tex. 2002) (under Texas law, class certification cannot be granted where individualized issues of reliance exist). As put by the Fifth Circuit in Patterson, "Claims for money damages in which individual reliance is an element are poor candidates for class treatment, at best. *We have made that plain.*" 241 F.3d at 419 (vacating class certification) (emphasis added).

Thus, unless Plaintiffs can establish that they are entitled to a presumption of class-wide reliance on V&E's alleged misconduct, the predominance of individualized issues of reliance bars certification of a class as to V&E.

II. The Fraud-on-the-Market Theory of Presumed Reliance Cannot Be Invoked with Respect to Plaintiffs' Claims Against V&E.

Aware that their claims are rife with individualized issues of reliance, Plaintiffs attempt to invoke the fraud-on-the-market presumption of class-wide reliance on the market price of Enron securities, thereby making reliance a common question rather than an individual one. See Amended Mot. for Class Cert. at 26. But that theory cannot be applied to claims against V&E for two reasons. First, V&E is not even alleged to have communicated directly

with the market at issue. Second, Plaintiffs have not carried their burden of showing that V&E was the "creator" of Enron's securities disclosures or other public statements relied on by the market.

A. V&E Made No Statements to the Market.

In Basic, Inc. v. Levinson, 485 U.S. 224, 242 (1988), the Supreme Court recognized that class-wide reliance may be presumed in a securities fraud case when a defendant is alleged to have disseminated materially misleading statements into an efficient market where investors rely on the integrity of the market price. See id. at 241-47. "The theme of Basic and other fraud-on-the-market decisions is that public information reaches professional investors, whose evaluations of that information and trades quickly influence securities prices." West v. Prudential Secs., Inc., 282 F.3d 935, 937 (7th Cir. 2002). If those conditions do not exist, the fraud-on-the-market theory is not applicable, and class certification should be denied. See, e.g., West, 282 F.3d at 938 (denying class certification because alleged misrepresentations not communicated by defendant to public). Accordingly, the fraud-on-the-market theory cannot be invoked against a defendant who did not disseminate allegedly misleading information because the market could not have relied on it.

Plaintiffs' Amended Complaint fails to identify even one misleading statement to the investing public made by, or attributed to, V&E. Instead, plaintiffs generally and repeatedly assert that V&E should be held liable because it "drafted and/or approved the adequacy of Enron's press releases, shareholder reports and SEC filings." Amended Compl. ¶ 801; see also id. ¶¶ 67, 70(b), 136, 141, 215, 221, 292-93, 800-01, 824, 826-27, 830-32, 834-35, 838, 843-44, 846-48. Consistent with the Amended Complaint, not a single proposed class representative claimed to have received and/or relied on any direct communication from V&E. See, e.g.,

Cassidy Dep. at 193-94 (attached at Tab A); Zegarski Dep. at 195 (attached at Tab B). Plaintiffs may avail themselves of the fraud-on-the-market presumption only if the market relied on misleading statements by V&E. Because the statements to the market were those of Enron, and not V&E, the fraud-on-the-market theory would apply only if Enron's allegedly misleading statements to the market could be attributed to V&E. V&E submits that they cannot.

In a different context, this Court previously ruled that Plaintiffs can state a securities fraud claim against alleged "creators" of misleading statements, see Memorandum and Order Re Secondary Actors' Motions to Dismiss, at 57-58 (Dec. 20, 2002), and that V&E is alleged to be a "creator." V&E submits that in *this* context the Court should follow the rule of the majority of circuits that have considered the issue and apply a "bright line" rule prohibiting a finding of primary liability under Section 10(b) unless the secondary actor itself is the identified author of a statement to investors. See Ziemba v. Cascade Int'l, Inc., 256 F.3d 1194, 1202-07 (11th Cir. 2001); Wright v. Ernst & Young LLP, 152 F.3d 169, 175 (2d Cir. 1998); Shapiro v. Cantor, 123 F.3d 717, 720 (2d Cir. 1997); Anixter v. Home-Stake Prod. Co., 77 F.3d 1215, 1226 (10th Cir. 1996). This rule is compelled by the requirement of reliance by the plaintiff on "*the defendant's* misstatement or omission." Central Bank, 511 U.S. at 180 (emphasis added). Application of the "creator" standard to support invocation of the fraud-on-the-market theory would allow plaintiffs to "circumvent the reliance requirement" in contravention of Central Bank. Id.

Because V&E did not communicate any statements – allegedly misleading or otherwise – to the market, and because V&E should not be deemed to be responsible for *Enron's* allegedly misleading statements to the market, no V&E statement is alleged to have had any effect on the market price for Enron securities. Because V&E is not alleged to have itself made

any statements to the market, there is absolutely no basis for presuming that the entire proposed class of Enron security holders acted in reliance on any misleading statement from V&E. As a result, individualized issues of reliance make Plaintiffs' claims against V&E unsuitable for class treatment.

B. Plaintiffs Have Not Carried Their Burden of Showing That V&E Was the "Creator" of Enron's Allegedly Misleading Public Statements.

Plaintiffs' Rule 23(b)(3) "predominance" argument rests on the notion that the fraud-on-the-market theory applies, but plaintiffs have not carried their burden of establishing a critical element for fraud on the market. They have not shown that the market relied on any statement of V&E. Not only does the Amended Complaint fail to allege that V&E itself made any misleading statements that could have been relied on by the market, but Plaintiffs fail to provide any support for their unsubstantiated claim that V&E "drafted and/or approved the adequacy of Enron's press releases, shareholder reports and SEC filings." Amended Compl. ¶ 801. Plaintiff's motion cites no *evidence* to support its bald allegation in the Amended Complaint that V&E was the "creator" of Enron's allegedly misleading public statements, and accordingly that the market reacted to any misleading statements made or "created" by V&E.

The Fifth Circuit has held repeatedly that looking past the pleadings "is necessary" "to determine whether the requirements of Rule 23 have been met." Castano v. Am. Tobacco Co., 84 F.3d 734, 744 (5th Cir. 1996); accord McManus v. Fleetwood Enters., Inc., 320 F.3d 545, 548 (5th Cir. 2003); O'Sullivan v. Countrywide Home Loans, Inc., 319 F.3d 732, 738 (5th Cir. 2003). A court must assess the "relevant facts . . . in order to make a meaningful determination of the certification issues." Castano, 84 F.3d at 744.[1]

[1] Although the Supreme Court has warned that a court considering class certification may not conduct a preliminary inquiry into the merits of a suit, see Eisen v. Carlisle & Jacquelin, 417 U.S. 156, 177-78 (1974), a court may look beyond the confines of the pleadings to determine whether the requirements of Rule 23 have been satisfied. Castano, 84 F.3d at 744; accord Gen.

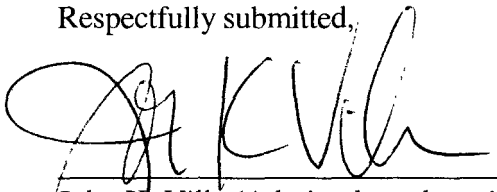
Specifically with regard to *reliance*, the Fifth Circuit has held that it is reversible error for a district court to rule based on the allegations in the complaint rather than considering whether "reliance would be an issue in individual trials." Castano, 84 F.3d at 745. Consistent with that rule, in a securities fraud case like this one in which plaintiffs attempted to invoke the fraud-on-the-market theory to permit a fraud claim to proceed as a class action, a court in this district refused to apply the theory because plaintiffs failed to introduce *evidence* establishing one of the elements necessary to show fraud on the market. See Griffin v. GK Intelligent Sys., Inc., 196 F.R.D. 298, 303 (S.D. Tex. 2000). In Griffin, defendants "present[ed] no evidence of the total trading volume" of the security, and based on that, the court found plaintiffs had not carried their burden of showing fraud on the market. Griffin, 196 F.R.D. at 303. Similarly here, Plaintiffs have failed to offer evidence that V&E was the "creator" of any misleading public statement on which the market could have relied, and thus have failed to establish that the fraud-on-the-market theory applies. Like the Griffin court, this Court should deny class certification based on plaintiffs' failure to establish an element necessary to show fraud on the market. Moreover, without identifying the specific statements V&E allegedly was involved in creating or the specific securities to which such statements purportedly relate, it is impossible to determine that class, rather than individual, issues of reliance will predominate.

Tel. Co. v. Falcon, 457 U.S. 147, 160 (1982) ("Sometimes the issues are plain enough from the pleadings . . . and sometimes it may be necessary for the court to probe behind the pleadings before coming to rest on the certification question."); Coopers & Lybrand v. Livesay, 437 U.S. 463, 469 (1978) (explaining that "the class determination generally involves considerations that are 'enmeshed in the factual and legal issues comprising the plaintiff's cause of action'"); Castano, 84 F.3d at 744 n.14 ("It is inescapable that in some cases there will be overlap between the demands of [Rule] 23(a) and (b) and the question of whether plaintiff can succeed on the merits." (quotation omitted)). Thus the fact that reliance is an element of Plaintiffs' Section 10(b) claim does not somehow remove it from Plaintiffs' burden to show reliance by the market for purposes of their Rule 23 fraud-on-the-market argument.

CONCLUSION

For the foregoing reasons, V&E respectfully requests that Lead Plaintiff's Amended Motion for Class Certification be denied.

Respectfully submitted,



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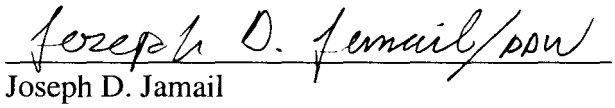

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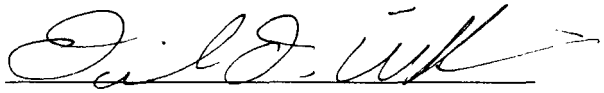
DATED: October 23, 2003

Counsel for Defendant Vinson & Elkins L.L.P.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Vinson & Elkins L.L.P.'s Opposition to Class Certification was served upon all known counsel of record by website, http://www.esl3624.com, pursuant to the Court's Order dated August 7, 2002 (Docket No. 984), on this 23rd day of October 2003.



Daniel D. Williams

1 IN THE UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
2 HOUSTON DIVISION

3 IN RE ENRON CORPORATION X CIVIL ACTION NO.
SECURITIES LITIGATION X H-01-3624 (CONSOLIDATED)
4 _____ X
X CLASS ACTION
5 THIS DOCUMENT RELATES TO: X
X
6 MARK NEWBY, ET AL., X
INDIVIDUALLY AND ON X
7 BEHALF OF ALL OTHERS X
SIMILARLY SITUATED, X
8 X
PLAINTIFFS, X
9 X
VS. X
10 X
ENRON CORP., ET AL., X
11 X
DEFENDANTS. X
12 _____ X
X
13 THE REGENTS OF THE X
UNIVERSITY OF CALIFORNIA, X
14 ET AL., INDIVIDUALLY AND X
ON BEHALF OF ALL OTHERS X
15 SIMILARLY SITUATED, X
X
16 PLAINTIFFS, X
X
17 VS. X
X
18 KENNETH L. LAY, ET AL., X
X
19 DEFENDANTS. X
20
21 ----------
22 ORAL VIDEOTAPED DEPOSITION OF
23 JOHN J. CASSIDY
24 SEPTEMBER 4, 2003
25 ----------

COPY

1 Q. Okay. Let me -- let me now move to yet 16:12
2 another topic and make sure that I've got everything 16:12
3 on this particular topic. You've given some 16:12
4 testimony on -- on what information you relied on in 16:12
5 your decisions to buy and hold Enron stock. 16:12
6 A. Yes. 16:12
7 Q. And you've testified that you, in part, 16:12
8 relied on what you had read in the Utility 16:12
9 Forecaster, correct? 16:12
10 A. Yes. 16:12
11 Q. And you testified that you, in part, relied 16:12
12 on some reported statement made by Mr. Lay at some 16:12
13 point about the company's prospects -- 16:12
14 A. Yes, yes. 16:12
15 Q. -- is that correct? 16:12
16 A. In the newspaper. 16:12
17 Q. And you also testified that you relied, in 16:13
18 part, upon favorable reports of Enron in the media? 16:13
19 A. Yes. 16:13
20 Q. Is there any other statement that you read, 16:13
21 saw or heard that caused you to buy or hold Enron 16:13
22 stock? 16:13
23 A. These, when I got a quarterly report, it 16:13
24 looked pretty good. The dividend reinvestment was 16:13
25 accruing. I depended on these, too (indicating). 16:13

1 Q. Anything else? 16:13
2 A. No, sir. 16:13
3 MR. HOURIHAN: I pass the witness. 16:13
4 Thank you. 16:13
5 (Deposition Exhibit S was marked.) 16:13
6 FURTHER EXAMINATION 16:13
7 BY MS. SUMOSKI: 16:13
8 Q. I'm just going to finish up here with -- 16:13
9 I'm handing you Exhibit S. Don't worry, 16:13
10 Mr. Cassidy. I'll be much faster than last time. 16:13
11 A. Oh, good. 16:13
12 Q. If you could just take a look at Exhibit S, 16:13
13 which is entitled "First Request for Production of 16:13
14 Documents Relating to Class Certification" -- oh, 16:13
15 boy. Did I hand you the correct one? 16:13
16 A. Yes, I believe so, started with Gibbs. 16:13
17 Q. -- "by the Outside Director Defendants." 16:14
18 A. Yes. 16:14
19 Q. Have you seen this document before? 16:14
20 A. No, ma'am. 16:14
21 Q. And you didn't search for any documents 16:14
22 pursuant to what was requested in Exhibit S, did 16:14
23 you? 16:14
24 A. No. I didn't see it, so I didn't know what 16:14
25 to search for. 16:14

1 UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
2 HOUSTON DIVISION

3 IN RE ENRON CORPORATION * CIVIL ACTION NO.
SECURITIES LITIGATION * H-01-3624
4 * (Consolidated)
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6 SITUATED, *
*
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14 Plaintiffs, *
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15 VS *
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16 KENNETH L. LAY, ET AL., *
*
17 Defendants. *
*
18
19 ----------
20 ORAL AND VIDEOTAPED DEPOSITION OF
21 JOHN DAVID ZEGARSKI
22 AUGUST 29, 2003
23 ----------
24
25

1 you need to aid your recollection, you're entitled to 17:35
2 request the person who's asking you the questions if 17:35
3 you can aid your recollection with a document. 17:35
4 A. Can I do that? 17:35
5 Q. (By Mr. Williams) What document would you 17:35
6 like to see? 17:35
7 A. To the -- 17:35
8 Q. Well, we'll strike that question. I'll ask 17:35
9 you a different question instead. 17:35
10 A. Okay. 17:35
11 Q. What -- what is your recollection -- sorry. 17:35
12 What do you personally believe -- sorry. Do you 17:35
13 personally believe that Vinson & Elkins made any 17:35
14 public statements in Enron's financial statements? 17:35
15 A. I -- I don't know if they made any public 17:35
16 statements within Enron's financial statements. 17:35
17 Q. Do you know of any? 17:35
18 A. I don't know of any, no. 17:35
19 Q. And do you believe that Enron -- sorry. 17:35
20 MR. WILLIAMS: No further questions. 17:35
21 Thank you. 17:35
22 FURTHER EXAMINATION 17:35
23 BY MS. STAGEN: 17:35
24 Q. Mr. Zegarski, do you know what Mr. Lay is 17:35
25 accused of in the amended complaint? 17:35