



to preserve evidence or to prevent undue prejudice. This showing must be directed to each Defendant, not to any group of Defendants. Plaintiff cannot meet this burden with respect to Fastow.

Apart from hype and speculation of what Fastow might do, Plaintiff does not offer a single fact to support an argument that Fastow would destroy evidence or that discovery from him is necessary to prevent undue prejudice. Below, Fastow examines every mention of his name in the papers Plaintiff filed on this issue – from the false accusation of a trip to Toronto to buy a ticket to Israel to the speculation that he will hide assets in an offshore bank account because he knows how to use off-shore companies – and will show that no fact underlies any of these baseless claims.

**1. The PSLRA Mandates a Stay of Discovery.**

In 1995, Congress adopted the PSLRA, 15 U.S.C. § 78u-4(b)(3)(B) which provides for a stay of discovery as follows:

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

The purpose of the act is to:

restrict abuses in securities class-action litigation, including: (1) the practice of filing lawsuits against issuers of securities in response to any significant change in stock price, regardless of defendants' culpability; (2) the targeting of "deep pocket" defendants; (3) the abuse of the discovery process to coerce settlement; and (4) manipulation of clients by class action attorneys.

*In re Advanta Corp. Sec. Litig.*, 180 F.3d 525, 530-31 (3d Cir. 1999).

The statute provides that plaintiff can overcome the stay in only two ways: either (1) it must demonstrate that it is necessary to "preserve evidence" or (2) it must prove that delaying discovery will lead to "undue prejudice." Plaintiff Amalgamated Bank has done neither with respect to Fastow.

**2. Even at face value, Plaintiff's charges do not prove that discovery is necessary to prevent "undue prejudice" or that Fastow is likely to destroy evidence.**

Plaintiff Amalgamated Bank filed this Motion for Expedited Discovery in connection with its effort to freeze pre-judgment the alleged insider trading profits of 29 individual defendants. With respect to Fastow, Plaintiff Amalgamated claims it needs the discovery to aid it in learning what he has done with the proceeds of his (limited) Enron stock sales; Amalgamated does not accuse Fastow of destroying evidence.

By terms of the PSLRA, however, discovery of what an alleged insider-trader did with the proceeds from a stock sale does not qualify as discovery "necessary to preserve evidence" or discovery "to prevent undue prejudice." Instead, the discovery Amalgamated seeks is relevant only to secure a judgment after verdict – a procedural step clearly inappropriate here, where there has been no verdict or judgment against Fastow. Accordingly, Plaintiff's argument to lift the discovery stay with respect to Fastow fails facially, even before the particulars of Amalgamated's arguments are examined.

Nonetheless, here follows a list of every charge Plaintiff Amalgamated makes in its moving papers in support of its claim of undue prejudice or of a necessity to preserve evidence with respect to Fastow:

**Plaintiffs' Ex Parte Application dated December 5, 2001:**

- P.1: Names Fastow as a defendant.
- P.2: States that "Fastow, Skilling, and other top Enron executives created limited partnerships which they called Special Purpose Entities."
- P.2: n.4: Refers to the LJM partnerships and Fastow's alleged compensation from those partnerships.
- P.3: Makes a passing reference to the alleged affect of the LJM1 partnership on the reporting of Enron's earnings.

- P.4: Refers to Fastow's supposed proceeds from sale of Enron stock, without any adjustment for taxes or purchase price. Even so inflated, Fastow's total sales rank well below numerous other executives.
- P.17: Alleges that Amalgamated Bank traded Enron stock on the same day as Fastow.

As is apparent from these references to Fastow, Plaintiff's December 5, 2001 Ex Parte Application makes no evidentiary showing at all, much less one that would support lifting the mandatory discovery stay required by the PSLRA.

**Amalgamated Bank's Supplemental Brief dated December 21, 2001:**

- P.19: Refers to Fastow as a flight risk, claiming that he had pre-cleared customs to fly out of the country, "soon after the SEC commenced its investigation of Fastow." The brief cites no evidence to support this statement, nor even one of the many press accounts around which Plaintiff has built its case. In fact, Fastow has appeared in public on several occasions since this alleged flight. This allegation by Plaintiff is utterly without any support whatsoever.
- P.19: Asserts that Fastow failed to comply with an SEC subpoena, relying on a Motion for Order to Show Cause filed by the SEC. Fastow disputed only the reasonableness of the timing of his appearance in response to the subpoena and subsequently reached an agreement with the SEC that complied with the subpoena, as evidenced by the attached papers, in which the SEC withdrew its Motion. (Ex. 1.)

Like Plaintiff's original Ex Parte Application, the Supplemental Brief fails to make any showing that could support lifting the discovery stay.

**Amalgamated Bank's Supplemental Brief dated January 25, 2002:**

- P.1: States that Fastow earned "tens of millions" from partnerships, without explaining how that fact has any connection to undue prejudice Plaintiff might suffer by having to wait for discovery until Motions to Dismiss are decided. Income from the partnerships, moreover, has no relevance to alleged insider trading profits.
- P.2: Refers to alleged "unreported insider trading" using "sophisticated derivative instruments." Part 2.1.2 below addresses this statement.

- P.9 a reference to Judge Rosenthal's Memorandum and Order, which asked for additional briefing on expedited discovery against defendants including Fastow.

**2.1 Plaintiff has not demonstrated undue prejudice in the absence of discovery.**

Following the pattern of Plaintiff Amalgamated Bank's two prior briefs, this submission, which was supposed to focus on how the PSLRA's discovery stay would unduly prejudice Plaintiff here and has completely failed to make any evidentiary showing on that score. Although Plaintiff Amalgamated Bank has made many allegations in this litigation regarding alleged shredding of documents and destruction of evidence, it makes no such claims against Fastow because it can offer no facts on that score. Mr. Fastow has not been accused of destroying documents in this case.

Under the PSLRA, a plaintiff can only establish "undue prejudice" by demonstrating prejudice that "is improper or unfair under the circumstances." *In re: CFS-Related Sec. Fraud Litig.*, \_\_ F.Supp.2d \_\_, 2001 WL 1682815 (N.D. Okla. Dec. 27, 2001) (citing *Medical Imaging Centers of Am., Inc. v. Lichtenstein*, 917 F.Supp. 717, 720 (S.D. Cal. 1996)). "Prejudice caused by the delay inherent in the PSLRA's discovery stay cannot be 'undue' prejudice because it is prejudice which is neither improper nor unfair." *Id.* In this case, "plaintiffs have provided no evidence to bolster their wholly speculative assertions as to the risk of lost evidence and undue prejudice." *Novak v. Kasaks*, 1996 WL 467534 (S.D.N.Y. August 16, 1996). Thus, they "have not satisfied their burden of showing that exceptional circumstances exist which would justify a departure from the Reform Act's mandatory stay of discovery." *Id.*

**2.1.1 Discovery of asset location is premature at any time before judgment.**

Plaintiff's first claim of undue prejudice seems to arise from the notion that Defendants, including Fastow, may secrete their proceeds from sales of Enron stock into offshore bank accounts prior to judgment. Yet Plaintiff presents no evidence that any Defendant, much less Fastow, has to date moved a single dollar of Enron stock sale proceeds into an offshore account or even that any defendant has such an account. Thus, Plaintiff has not demonstrated any undue prejudice. "Wholly speculative assertions" do not satisfy the requirements for establishing undue prejudice. *In re: CFS Sec. Litig.*, \_\_\_ F.Supp.2d at \_\_\_; 2001 WL 1682815 at \*3; see also *In re: Trump Hotel Shareholder Derivative Litig.*, 1997 WL 442135 (S.D.N.Y. Aug. 5, 1997) (possibility of undue prejudice particularly remote where discovery sought is production of documents). In fact, Judge Rosenthal's Memorandum Opinion and Order of January 8, 2002 specifically dismissed generalized allegations of familiarity with international or offshore transactions as a basis for the relief sought by Plaintiff. Opinion, at 41. Plaintiff's briefing and affidavits submitted since that Order was issued have made no additional showing to support the relief they seek of expedited discovery.

Moreover, Plaintiff cannot seek a lifting of the discovery stay to determine the location of Defendants' assets because Plaintiff has no basis for obtaining any such discovery prior to judgment, regardless of whether the PSLRA stay applies. See *Oriental Commercial & Shipping Co., Ltd. v. Rosseel, N.V.*, 125 F.R.D. 398, 401 (S.D.N.Y. 1989); *Sears v. Atchison, Topeka & Santa Fe Rwy. Co.*, 1982 WL 500 (D. Kan. Dec. 1, 1982), at \*3. Pre-judgment discovery under FED. R. CIV. P. Rule 26 applies only to requests that seek information reasonably calculated to lead to admissible evidence. *Id.*; cf. Fed. R.

Civ. P. 69(a) (expressly allowing *post-judgment* discovery to aid in collection). Because it does not relate to any claims or defenses, discovery that seeks to determine the location of a defendant's assets falls outside the scope of Rule 26 altogether. *Id.*

Indeed, if the Court were to permit a lifting of the PSLRA discovery stay to allow discovery of the location of Defendants' assets, then every Plaintiff in a securities fraud case with allegations of insider trading could seek that same relief. *See Novak*, 1996 WL 467534 at \*1 (requiring "exceptional circumstances" to justify lifting the PSLRA discovery stay). Not only would such a decision emasculate the PSLRA discovery stay, it would undermine Rule 26's general prohibition on collection-related discovery prior to judgment.<sup>1</sup>

**2.1.2 Plaintiff's fantastic allegations regarding "unreported insider trading" have no bearing on question of undue prejudice.**

To further support its claim of undue prejudice, Plaintiff makes unsubstantiated allegations regarding "unreported insider trading" through the use of "sophisticated derivative instruments." The source of these allegations is a hearsay (double, triple, and maybe more) affidavit by Francis Karam, a member of the Milberg Weiss firm, counsel for Amalgamated Bank. In the hearsay-laden affidavit, Mr. Karam admits that he has prepared the affidavit on the basis of "information . . . provided anonymously . . . obtained from persons who have requested that their identities be kept confidential, or . . . from persons who have not witnessed the transactions first hand." Pl. Ex. 6, ¶ 4.

Without providing any more specifics about his sources or the particulars of any alleged

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<sup>1</sup> *In re: Websecure, Inc.*, 1997 WL 770414 (D. Mass. Nov. 26, 1997), a case upon which Plaintiff relies, allowed expedited discovery regarding a company's use of IPO proceeds only after the plaintiff in that case made a showing that "raise[d] a serious question of asset dissipation." *Id.* at \*3. Specifically, the company's Form 10-Q filing showed that "operating expenses were increasing sharply, without producing much in the way of revenue." *Id.* Plaintiff in this case has made no such showing.

transaction, Mr. Karam asserts: “[D]efendants Jeffrey Skilling, Kenneth Lay, Lou Pai, Andrew Fastow, and Kevin Hannon, *may have* received cash for certain rights derived from their stock and options without triggering the need to report the transaction . . .” *Id.* (emphasis added). If Mr. Karam has these sources of information regarding these supposed derivative trades, then it follows that Plaintiff (his client) will suffer no prejudice from having to follow the usual procedures for discovery under the PSLRA, including abiding by the discovery stay. Plaintiff can get whatever information it needs from these unidentified sources upon whom Mr. Karam relied upon to prepare his affidavit. If Plaintiff does not have these sources of information, then it should not have submitted an affidavit based on pure speculation and hearsay.

Plaintiff makes no showing that Fastow did in fact enter into any of these supposed “sophisticated derivative transactions.” Rather, Mr. Karam’s affidavit states only that he *may have* done so. Of course, that holds true for every corporate executive who might have held stock options, in Enron and in every other company that issued such options. The mere possibility of such derivative trading does not constitute the “exceptional circumstances” required to “justify a departure” from the discovery stay. *Novaks*, 1996 WL 467534 at \*1; *see See In re CFS Sec. Litig.*, \_\_\_ F.Supp.2d at \_\_\_; 2001 WL 1682815 at \*3. Plaintiff will suffer no more prejudice in having to wait for discovery on the question of these supposed derivative trades than is inherent in the stay enacted by Congress. *See id.*

**2.2 Plaintiff has not made any showing to support an order of expedited discovery to preserve evidence.**

Plaintiff makes no showing that there exists any risk that Fastow poses a risk to spoliage evidence. Rather, Plaintiff says only that evidence “has been lost” and that “concrete evidence of document destruction has been shown” without making any proffer of supporting evidence or tying the alleged “lost evidence” or “evidence destruction” to Fastow. Plaintiff’s speculative assertions do not justify lifting the §78u-4(b)(3)(C) discovery stay. *See In re: CFS Sec. Litig.*, \_\_\_ F.Supp.2d at \_\_\_, 2001 WL 1682815, at \*3; *Novaks*, 1996 WL 467534, at 1; *In re: Fluor Corp. Sec. Litig.*, 1999 WL 817206 (C.D. Cal. Jan. 15, 1999).

**2.3 Plaintiff has not limited its requests to “particularized discovery.”**

Even if a plaintiff makes the necessary showing for lifting the discovery stay, under the PSLRA, it may still only obtain “particularized discovery.” *See* 15 U.S.C. § 78u-4(b)(3)(C). Although the purported justification for Plaintiff’s expedited discovery request involves allegations of insider trading, the proposed discovery requests attached to Plaintiff’s Brief go well beyond discovery of the sale proceeds of Enron stock. For this reason the requests are not particularized. Furthermore, the requests improperly seek discovery of information that Plaintiff may attempt to use in the next amendment of its Complaint.

For instance, Plaintiff requests all bank and bank brokerage accounts of Defendants, their children and spouses, regardless of whether those accounts had any connection to Enron. The interrogatories ask for information regarding attorney and accountant relationships (Pl. Ex. 10, Interrogatory No. 4), in addition to broad questions about banking and brokerage accounts. Plaintiff even wants bank and tax information for

any entity in which a Defendant was a partner, officer, or director, regardless of that entity's connection to Enron or the allegations in this case. This discovery is not particularized because it goes well beyond the "insider trading" theory upon which Plaintiffs base their application for lifting the stay. See *Faulkner v. Verizon Comm., Inc.*, 156 F.Supp.2d 384, 404 (S.D.N.Y. 2001) (requests that go beyond the basis for Plaintiffs' expedited discovery requests are not particularized). Plaintiff's proposed discovery requests seek an "open-ended, boundless universe" of documents, and thus fail to meet the particularization requirement of the PSLRA. *Mishkin v. Ageloff*, 220 B.R. 784, 793 (S.D.N.Y. 1998).

Moreover, Plaintiff's requests impermissibly seek information that it may use to satisfy the PSLRA's pleading requirements. See *SG Cowen Sec. Corp. v. United States District Court*, 189 F.3d 909, 912-13 (9<sup>th</sup> Cir. 1999). Plaintiff has relied heavily on published information regarding insider sales in its original and Amended Complaints. Plaintiff's requests, as they stand, would permit discovery of information that Plaintiffs may try to use in bolstering the legal sufficiency of their Complaint. Indeed, some of Plaintiff's requests have nothing to do with sales of Enron stock, but rather pertain to various partnerships referred and other entities referred to in its Complaint. See Pl. Ex. 9, Request No. 2. Allowing Plaintiff to obtain discovery on matters that it could use to bolster its Complaint would depart from the narrow exceptions to the PSLRA discovery stay, which contemplates that district courts will allow discovery "only after the court has sustained the legal sufficiency of the complaint." *Novak*, 1996 WL 467534, at \*1 (quoting Sen. Comm. on Banking, Housing, Urban Affairs, Private Securities Litigation Reform Act, S. Rep. No. 98, 104<sup>th</sup> Cong., 1<sup>st</sup> Sess. 14 (1995)); *SG Cowen*, 189 F.ed at

912-13. For these reasons, Plaintiff has not met the PSLRA's particularized discovery requirement.

**3. Conclusion**

For all of the foregoing reasons, Defendant Fastow respectfully requests that the Court deny Plaintiff's request for expedited discovery.

Respectfully submitted,

BOIES, SCHILLER & FLEXNER, L.L.P.

By: 

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**CERTIFICATE OF SERVICE**

This is to certify that on **February 8th, 2002** a true and correct copy of the above and foregoing instrument was served on all counsel of record by facsimile transmission and/or by certified mail, return receipt requested, and in accordance with the Federal Rules of Civil Procedure.

SEE ATTACHED SERVICE LIST

  
\_\_\_\_\_  
Craig Smyser

UNITED STATES DISTRICT COURT  
FOR THE  
DISTRICT OF COLUMBIA

SECURITIES AND EXCHANGE COMMISSION )  
450 Fifth Street, N.W. )  
Washington, D.C. 20549, )

Applicant, )

CASE NO. 1:01MS00456

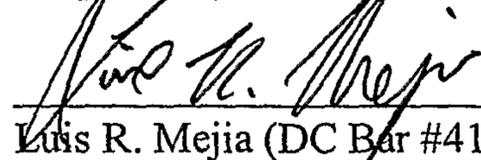
ANDREW S. FASTOW )  
1831 Wroxtton Road )  
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Respondent. )

**NOTICE OF WITHDRAWAL OF  
APPLICATION OF THE SECURITIES AND EXCHANGE COMMISSION  
FOR AN ORDER REQUIRING OBEDIENCE TO SUBPOENA**

The Securities and Exchange Commission ("Commission") hereby withdraws its Application for an Order Requiring Obedience to Subpoena. Today, Mr. Fastow appeared pursuant to the subpoena served upon him on October 31, 2001.

Respectfully submitted,

  
Luis R. Mejia (DC Bar #417043)

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Dated: December 19, 2001

EXHIBIT

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tabbles

CERTIFICATE OF SERVICE

I hereby certify that on this 19 day of December 2001, I caused true and correct copies of the foregoing, "Notice of Withdrawal of Application of the Securities and Exchange Commission for an Order Requiring Obedience to Subpoena," along with a proposed order, to be served to the following by the means specified:

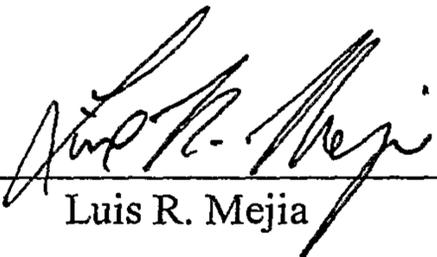
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\_\_\_\_\_  
Luis R. Mejia

UNITED STATES DISTRICT COURT  
FOR THE  
DISTRICT OF COLUMBIA

SECURITIES AND EXCHANGE COMMISSION )  
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Applicant, )

CASE NO. 1:01MS00456

ANDREW S. FASTOW )  
1831 Wroxtton Road )  
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Respondent. )

**ORDER DISMISSING APPLICATION  
FOR ORDER REQUIRING OBEDIENCE TO SUBPOENA**

The Applicant, Securities and Exchange Commission ("Commission"), having filed a Notice of Withdrawal of Application for an Order Requiring Obedience to Subpoena, and the Court having considered the Notice of Withdrawal, and good cause being shown, it is hereby,

ORDERED, that the above-captioned action is dismissed as moot.

Dated: December \_\_, 2001

\_\_\_\_\_  
UNITED STATES DISTRICT JUDGE

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UNITED STATES DISTRICT COURT  
FOR THE  
DISTRICT OF COLUMBIA

**FILED**

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450 Fifth Street, N.W. )  
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CASE NO. 1:01MS00456

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**ORDERED**, that the above-captioned action is dismissed as moot.

Dated: December 19, 2001

*Ellen S. Huvell*  
UNITED STATES DISTRICT JUDGE