

United States Courts
Southern District of Texas
FILED
FEB 27 2002
Michael N. Milby, Clerk

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

In re ENRON CORPORATION SECURITIES
LITIGATION

Civil Action No. H-01-3624
(Consolidated)

CLASS ACTION

This Document Relates To:

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

Plaintiffs,

vs.

ENRON CORP., et al.,

Defendants.

U.S. COURTS
SOUTHERN DISTRICT
OF TEXAS

2002 FEB 28 AM 8:03

FILED

**LEAD PLAINTIFF'S REPLY REGARDING SUPPLEMENTAL BRIEFING
PURSUANT TO THE COURT'S JANUARY 8, 2002 ORDER
CONCERNING PARTICULARIZED DISCOVERY**

329

TABLE OF CONTENTS

	Page
I. INTRODUCTION	1
II. ARGUMENT	2
A. Lead Plaintiff Has Demonstrated the Discovery Stay Should Be Lifted	2
1. The Purposes Underlying the PSLRA's Discovery Stay Are Not Implicated Here	2
2. When (As Here) Plaintiff Lacks Information to Demonstrate Dissipation in Support of a Freeze Motion, Particularized Discovery Should Be Allowed to Prevent Undue Prejudice	5
B. The PSLRA Does Not Require Plaintiff to Show "Particularized Facts" Before the Discovery Stay May Be Lifted	6
C. Lead Plaintiff's Discovery Requests Are Particularized	7
D. Enron's Bankruptcy Does Not Preclude the Discovery Lead Plaintiff Seeks	9
III. CONCLUSION	12

TABLE OF AUTHORITIES

CASES	Page
<i>A.H. Robins Co. v. Piccinin</i> , 788 F.2d 994 (4th Cir. 1986)	11
<i>Arnold v. Garlock, Inc.</i> , 278 F.3d 426, 2001 U.S. App. LEXIS 27275 (5th Cir. 2001)	10
<i>Carway v. Progressive County Mut. Ins. Co.</i> , 183 B.R. 769 (N.D. Tex. 1995)	10
<i>Credit Alliance Corp. v. Williams</i> , 851 F.2d 119 (4th Cir. 1988)	10
<i>DM Research, Inc. v. College of Am. Pathologists</i> , 170 F.3d 53 (1st Cir. 1999)	7
<i>Faulkner v. Verizon Communs., Inc.</i> , 156 F. Supp. 2d 384 (S.D.N.Y. 2001)	9
<i>In re American Hardwoods</i> , 885 F.2d 621 (9th Cir. 1989)	11
<i>In re Arrow Huss, Inc.</i> , 51 B.R. 853 (Bankr. D. Utah 1985)	10
<i>In re CFS-Related Sec. Fraud Litig.</i> , 179 F. Supp. 2d 1260 (N.D. Okla. 2001)	6
<i>In re Carnegie Int'l Corp. Sec. Litig.</i> , 107 F. Supp. 2d 676 (D. Md. 2000)	8
<i>In re Continental Airlines</i> , 177 B.R. 475 (D. Del. 1993)	12
<i>In re First Cent. Fin. Corp.</i> , 238 B.R. 9 (Bankr. E.D.N.Y. 1999)	12
<i>In re Johns-Manville Corp.</i> , 26 B.R. 405 (Bankr. S.D.N.Y. 1983)	9
<i>In re Johns-Manville Corp.</i> , 26 B.R. 420 (Bankr. S.D.N.Y. 1983), <i>rev'd on other grounds</i> , 41 B.R. 926 (S.D.N.Y. 1984)	11
<i>In re Lowenschuss</i> , 67 F.3d 1394 (9th Cir. 1995)	11
<i>In re Sunbeam Sec. Litig.</i> , 89 F. Supp. 2d 1326 (S.D. Fla. 1999)	7

<i>In re Trump Hotel S'holder Derivative Litig.</i> , No. 96 Civ. 7820, 1997 U.S. Dist. LEXIS 11353 (S.D.N.Y. Aug. 5, 1997)	6
<i>In re Tyco Int'l, Ltd. Sec. Litig.</i> , MDL No. 00-MD-1335-B, 2000 U.S. Dist. LEXIS 11659 (D.N.H. July 27, 2000)	4
<i>In re Websecure, Inc. Sec. Litig.</i> , No. 97-10662-GAO, 1997 U.S. Dist. LEXIS 19600 (D. Mass. Nov. 26, 1997)	1, 5
<i>Medical Imaging Ctrs. of Am., Inc. v. Lichtenstein</i> , 917 F. Supp. 717 (S.D. Cal. 1996)	4, 5
<i>Migdal v. Rowe Price-Fleming Int'l</i> , 248 F.3d 321 (4th Cir. 2001)	7
<i>Newby v. Enron Corp.</i> , No. H-01-4198, 2002 WL 200956 (S.D. Tex. Jan. 9, 2002)	1
<i>Teachers Ins. & Annuity Ass'n v. Butler</i> , 803 F.2d 61 (2d Cir. 1986)	10
<i>Underhill v. Royal</i> , 769 F.2d 1426 (9th Cir. 1985)	11
<i>Wedgeworth v. Fibreboard Corp.</i> , 706 F.2d 541 (5th Cir. 1983), <i>vacated in part on other grounds</i>	10

STATUTES, RULES AND REGULATIONS

11 U.S.C.	
§362	9
§362(a)	9, 10
§524(3)	10

SECONDARY AUTHORITIES

H.R. Conf. Rep. No. 104-369, at 37 (1995), <i>reprinted in</i> 1995 U.S.C.C.A.N. 679, 736	3
H.R. Conf. Rep. No. 95-595, at 340, <i>reprinted in</i> 1978 U.S.C.C.A.N. 5963, 6297	10

I. INTRODUCTION

After determining the Court had the equitable power to enter the freeze order Lead Plaintiff seeks, Judge Rosenthal ordered the parties to brief whether, and to what extent, plaintiffs were entitled to discovery to gather evidence in support of their request for an injunction.¹ In response, Lead Plaintiff relied on (among other authorities) *In re Websecure, Inc. Sec. Litig.*, No. 97-10662-GAO, 1997 U.S. Dist. LEXIS 19600 (D. Mass. Nov. 26, 1997), which held the PSLRA's discovery stay may be lifted to obtain evidence of asset dissipation in support of an injunction freezing assets. Plaintiffs also demonstrated the rationale underlying the PSLRA's discovery stay is not implicated where, as here, a plaintiff does not seek merits-based discovery to bolster securities fraud allegations lacking merit.

In their oppositions, some defendants labeled this litigation frivolous while others claimed Lead Plaintiff seeks discovery concerning defendants' insider-trading proceeds to support unfounded allegations. This is not so. Enron's Special Investigative Committee has already found Enron's earnings were artificially inflated by more than \$1 billion from a "systematic and pervasive" attempt to misrepresent Enron's financial condition, and that participants in the wrongdoing "include ... Enron's management, Board of Directors, and outside advisors." *See* Amalgamated Bank's and Regents' Motion for Particularized Discovery, filed Feb. 8, 2002, Ex. F. Former CEO Kenneth Lay complains the requested discovery is intrusive, yet just several weeks ago Mrs. Lay appeared on national television and publicly discussed the details concerning their private financial affairs. *See* Plaintiffs' Sec. Supp. Brf., filed Feb. 7, 2002, Ex. C. And the Lay's situation illustrates the importance to Lead Plaintiff of gathering discovery to support Lead Plaintiff's motion to freeze insider-trading proceeds. Mr. Lay, one of the most conspicuous insider traders, now claims that proceeds from his stock sales are gone. *Id.*

¹"This court orders Amalgamated to file such a brief, explaining what discovery is requested and why the request should be granted Defendants may file a response" *Newby v. Enron Corp.*, No. H-01-4198, 2002 WL 200956, at *17 (S.D. Tex. Jan. 9, 2002). Several defendants have filed briefs requesting the Court reconsider Judge Rosenthal's January 8, 2002 Order. Plaintiffs will address these reconsideration requests in a separate, unified opposition.

Defendants also seek to impose upon Lead Plaintiff an evidentiary requirement *not* contained in any order from Judge Rosenthal or in the PSLRA. They argue plaintiffs were required to make an additional evidentiary "showing" to support their request for discovery. *See, e.g.*, Fastow Opp. at 6 ("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."); Skilling Opp. at 1-2 ("the Plaintiffs have not come forward with any additional evidence"). The PSLRA imposes no such requirement and this meritorious case far from requires the showing defendants request.

As Judge Rosenthal's Order dated January 8, 2002 states, plaintiffs need only explain why discovery should be permitted in support of the motion to freeze insider trading proceeds (which the Court has the power to grant) and, if the discovery stay is lifted, the scope of the discovery. *See* n.1, *supra*. Lead Plaintiff has clearly demonstrated why the discovery sought is needed – to evidence defendants' dissipation of the insider-trading proceeds. Ordering defendants to produce documents concerning (among other things) their off-shore accounts, money transfers, and compensation from illicit partnerships, does not run counter to the underlying purpose of the PSLRA's discovery stay. The particularized discovery Lead Plaintiff seeks is critical to Lead Plaintiff's ability to secure an important source of equitable recovery for Enron's defrauded investors.

II. ARGUMENT

A. Lead Plaintiff Has Demonstrated the Discovery Stay Should Be Lifted

1. The Purposes Underlying the PSLRA's Discovery Stay Are Not Implicated Here

The Outside Directors claim the discovery sought here is "flatly inconsistent" with the PSLRA's purpose of protecting corporate defendants from plaintiffs' counsel ""discovering' their way into facts which could allow them to amend an initially frivolous complaint so as to state a claim." Outside Directors' Opp. at 14-15 (citation omitted). Defendant Mark-Jusbasche argues discovery concerning the defendants' asset dissipation is "precisely the abusive fishing expedition that impelled Congress to require a discovery stay in the PSLRA in the first place." Mark-Jusbasche Opp. at 9. Defendant Lay claims this is an attempt to uncover information to support scienter allegations against Lay. *See* Lay Opp. at 16 n.7. And Fastow goes so far as to argue the requested

discovery is contrary to not only the PSLRA but also the Federal Rules of Civil Procedure, Fastow Opp. at 6, and Lead Plaintiff is attempting to "bolster its Complaint." *Id.* at 10. Plainly, defendants overstate the case.

Contrary to what defendants claim, the PSLRA's discovery stay is not necessary to prevent discovery from being initiated here to sustain baseless allegations. *See* H.R. Conf. Rep. No. 104-369, at 37 (1995), *reprinted in* 1995 U.S.C.C.A.N. 679, 736. Given the state of the public record, it is already apparent that Lead Plaintiff's claims are well founded. Enron's Special Investigative Committee has already uncovered "a systematic and pervasive attempt by Enron's management to misrepresent the company's financial condition." *See* Amalgamated Bank's and Regents' Motion for Particularized Discovery, filed Feb. 8, 2002, Ex. E. The Committee's Report of Investigation, or "Powers Report," found off-balance-sheet partnerships were used by Enron management to enter into transactions that Enron could not, or would not, do with unrelated commercial entities and that many of the most significant transactions "apparently were designed to accomplish favorable financial statement results, not to achieve *bona fide* economic objectives or to transfer risk." *Id.* at Ex. F. Referring to transactions with the off-balance-sheet partnerships used to "offset losses," the Powers Report states:

They allowed Enron to *conceal* from the market very large losses resulting from Enron's merchant investments by creating an appearance that those investments were hedged – that is, that a third party was obligated to pay Enron the amount of those losses – when in fact that third party was simply an entity in which only Enron had a substantial economic stake. ***We believe these transactions resulted in Enron reporting earnings from the third quarter of 2000 through the third quarter of 2001 that were almost \$1 billion higher than should have been reported.***

Id. (emphasis added). According to the Special Investigative Committee, the participants in this wrongdoing "include not only the employees who enriched themselves at Enron's expense, but also Enron's Management, Board of Directors and outside advisors." *Id.*

Thus, despite defendants' attempts to cast it as such, this is not a routine securities case. The cover-up is unprecedented. Andersen admitted that a significant but undetermined amount of Enron-related documents have been destroyed. The "undetermined" amount was at least 32 foot-locker-sized trunks and the electronic data deletion apparently concerned the transactions at issue. (This information was not provided by Andersen on its report as required.) The Court has also been

witness to evidence of document destruction at Enron's headquarters, and has noted, "This litigation is probably the largest and most complex of its kind in the history of this country...." Feb. 15, 2002 Order at 78. And defendants Lay and Fastow, along with a number of others, have invoked the protections of the Fifth Amendment in response to questioning by the House of Representatives Oversight Committee. This case merits the particularized discovery Lead Plaintiff seeks.

The PSLRA's discovery-stay provisions and the concomitant duty to preserve relevant documents "reflect a careful balance between Congress's effort to shield defendants facing frivolous claims from the burdens of discovery, on the one hand, and its desire to ensure the preservation of evidence relevant to legally cognizable claims, on the other." *In re Tyco Int'l, Ltd. Sec. Litig.*, MDL No. 00-MD-1335-B, 2000 U.S. Dist. LEXIS 11659, at *5 (D.N.H. July 27, 2000). As the *Medical Imaging* court explained:

The introductory paragraphs of the Statement of Managers for the Reform Act noted that Congress, in passing this new legislation, was "prompted by significant evidence of abuse in private securities lawsuits," which Congress found to include, "the abuse of the discovery process to impose costs so burdensome that it is often economical for the victimized party to settle." ***Congress also noted, however, the broader purpose of the federal securities laws, "to protect investors and to maintain confidence in the securities markets, so that our national savings, capital formation and investment may grow for the benefit of all Americans." Using an "undue prejudice" standard in applying the exception to the statutory discovery stay appropriately attempts to balance the competing concerns of maintaining truth and integrity in the marketplace while curbing meritless litigation.***

Medical Imaging Ctrs. of Am., Inc. v. Lichtenstein, 917 F. Supp. 717, 720-21 (S.D. Cal. 1996) (emphasis added; citation omitted). Under these circumstances, clearly the discovery Lead Plaintiff seeks is not merely an end-run around the discovery stay. The discovery requested by Lead Plaintiff poses no threat of the abusive litigation addressed by the PSLRA. Rather, Lead Plaintiff seeks to secure a much-needed remedy. Consequently, Lead Plaintiff must determine the manner and to what extent insider-trading proceeds are being dissipated and the location of those proceeds to support its motion to freeze insider-trading proceeds. Defendants therefore should not be allowed to hide behind the PSLRA to avoid Lead Plaintiff's motion for injunctive relief.²

²Defendant Skilling claims plaintiffs have engaged in a "troubling and disingenuous lack of candor before this Court" concerning plaintiffs' authority because 11 cases cited by plaintiffs were decided "***before the PSLRA was enacted***," Skilling Opp. at 7-8 (emphasis in original), and claims citation to these cases and three others is "inexcusable." *Id.* at 8. Plaintiffs, as should be apparent,

2. When (As Here) Plaintiff Lacks Information to Demonstrate Dissipation in Support of a Freeze Motion, Particularized Discovery Should Be Allowed to Prevent Undue Prejudice

Particularized discovery should be allowed so Lead Plaintiff may demonstrate defendants' dissipation of insider-trading proceeds. Defendants have failed to adequately explain why the reasoning of the court in *Websecure* should not apply here. In *Websecure*, plaintiffs moved for a preliminary injunction to freeze, or impose a constructive trust upon, cash and proceeds from Websecure's initial public offering, and sought expedited discovery concerning how such proceeds had been, and were being, spent. *Websecure*, 1997 U.S. Dist. LEXIS 19600, at *2, *9-*10, *13. As here, in *Websecure*, the district judge denied plaintiffs' freeze motion because plaintiffs had not demonstrated dissipation of assets. *Id.* at *9-*11. In *Websecure*, expedited discovery was granted, however, because plaintiffs **lacked information** to determine whether Websecure's business was dissipating assets. *Id.* at *11, *13. Accordingly, the court in *Websecure* allowed expedited discovery "concerning how the proceeds of the IPO have been, and are being, spent and what Websecure's business plans and prospects are." *Id.* at *13. Contrary to what defendants suggest, Lead Plaintiff's information concerning dissipation is no more lacking here than in *Websecure*.

Just as the court in *Websecure* allowed particularized discovery to prevent undue prejudice, Lead Plaintiff here seeks particularized discovery concerning defendants' dissipation of insider-selling proceeds to support the freeze motion. Lead Plaintiff lacks complete information concerning "how the proceeds ... have been, and are being, spent," among other things. *Id.* at *13. And this case is even more compelling than *Websecure* because the relief Lead Plaintiff seeks cannot be obtained from other defendants, whereas in *Websecure*, the court identified other actors from whom the plaintiffs could obtain relief. *See id.* at *12. Moreover, Enron's director-and-officer insurance

cited the pre-PSLRA cases for the proposition that on numerous occasions, courts have permitted expedited discovery when a plaintiff seeks injunctive relief or when relevant evidence may be lost, including discovery concerning dissipation of assets. *See* Pltfs.' Supp. Brf. at 8-9. Plaintiffs further noted evidence already had been purposefully destroyed, further highlighting the need for the requested discovery in support of injunctive relief. Defendant Skilling claims the enactment of the PSLRA renders these cases "inapposite," Skilling Opp. at 8, but ignores the fact the PSLRA permits the discovery stay to be lifted and Congress itself sought to strike a balance between "maintaining truth and integrity in the marketplace while curbing meritless litigation." *Medical Imaging*, 917 F. Supp. at 721.

coverage of approximately \$350 million does not provide coverage for insider-trading claims and, even if it did provide such coverage, the policy limit is still only a fraction of the disgorgement remedy to which plaintiffs are entitled – over \$1 billion. It is also a small fraction of the potential damages caused to investors by defendants' wrongdoing.

Nonetheless, defendants argue plaintiffs have failed to show limited discovery is necessary to prevent undue prejudice or preserve relevant evidence. Defendants rely heavily on *In re CFS-Related Sec. Fraud Litig.*, 179 F. Supp. 2d 1260 (N.D. Okla. 2001), to support their claim that plaintiffs here have not carried their burden. *CFS* is distinguishable. In *CFS*, the prejudice plaintiffs claimed was fading witnesses memories and the possibility documents could be lost. *Id.* at *17-*18. In contrast, here, plaintiffs have demonstrated "they are faced with a type or degree of prejudice distinct from that inherent in all stays of discovery." *Id.* at *19.

Other cases cited by defendants concerning the PSLRA's stay provision are also distinguishable. Mr. Fastow relies on *In re Trump Hotel S'holder Derivative Litig.*, No. 96 Civ. 7820, 1997 U.S. Dist. LEXIS 11353 (S.D.N.Y. Aug. 5, 1997), where plaintiffs did not attempt to demonstrate undue prejudice but instead argued the PSLRA's stay provisions should not apply to their pendant state law claims because they alleged a federal securities law claim. *Id.* at *5; Fastow Opp. at 6. The *Trump* court disagreed, and held that there had been no demonstration of undue prejudice and that the discovery sought (document requests) could not cure a prejudice in any event. Lead Plaintiff does not seek discovery pursuant to state law claims and this case is likewise different than *Trump* in all other respects.

B. The PSLRA Does Not Require Plaintiff to Show "Particularized Facts" Before the Discovery Stay May Be Lifted

Defendant Lay argues that while the Fifth Circuit has never ruled on the required showing necessary to lift PSLRA discovery stay, "in another context" the PSLRA requires "particularized facts" to sustain a claim for "relief." Lay Opp. at 8. Under this construct, Lay argues Lead Plaintiff is not entitled to any discovery because plaintiff fails to make this "particularized" showing. *Id.* Relying on inapposite authorities, the Outside Directors similarly argue that Lead Plaintiff has made

no "particularized allegations" to support the request that the discovery stay be lifted. Outside Directors Opp. at 1, 11. Defendants are wrong.

First, the PSLRA has no "particularized fact" requirement for lifting the discovery stay. A plaintiff need only show "undue prejudice" or a need to "preserve evidence."

Second, none of the cases cited by the Outside Directors are PSLRA cases. Indeed, none are federal securities fraud cases. In *Migdal v. Rowe Price-Fleming Int'l*, 248 F.3d 321 (4th Cir. 2001), (which the Outside Directors mistakenly state is a Fifth Circuit decision), a case brought under the Investment Company Act, the court granted defendants' motion to dismiss because plaintiffs had failed to state a claim. The *Migdal* court denied discovery because plaintiffs sought to discover elements missing from their claim. *DM Research, Inc. v. College of Am. Pathologists*, 170 F.3d 53 (1st Cir. 1999), was a Sherman Act case where the court affirmed dismissal of a complaint for failure to state a claim. Among other distinctions, there is no issue of inadequate pleading here, as opposed to *Migdal* and *DM Research*. Here, the issue is whether, under the PSLRA, Lead Plaintiff has shown that one of the two congressionally recognized exceptions to the discovery stay provisions apply.³

C. Lead Plaintiff's Discovery Requests Are Particularized

Defendants' descriptions of the discovery Lead Plaintiff seeks are exaggerated and, to a large extent, false. For example, defendants Fastow and Mark-Jusbasche deem the requested discovery an "open-ended, boundless universe." Mark-Jusbasche Opp. at 8; Fastow Opp. at 10 (citation omitted). Defendant Skilling contends the requests "cover[] the entire universe of defendants' personal financial information." Skilling Opp. at 9. Defendant Lay states the discovery "encompasses every personal document of Mr. Lay" that plaintiffs would seek at "any stage" of this litigation, and even suggests plaintiff need this discovery to support scienter allegations against him. Lay Opp. at 14.

³The Outside Directors further accuse plaintiffs of relying on "group pleading" to plead their case. Outside Directors' Brf. at 14. To the contrary, plaintiffs do not rely on this doctrine, which allows certain group-published information (*i.e.*, annual reports) to constitute collective action for purposes of pleading scienter. *See, e.g., In re Sunbeam Sec. Litig.*, 89 F. Supp. 2d 1326 (S.D. Fla. 1999).

A fair characterization of the discovery plaintiff seeks is: (i) an inquiry of defendants' use of off-shore accounts or other asset-concealing techniques to effect dissipation or concealment of insider-trading proceeds; and (ii) the nature and amount of proceeds from insider sales, both reported and unreported. The document requests are both limited and particularized. Indeed, the discovery seeks information concerning only:

- off-shore accounts;
- monies received from the special-purpose entities Enron used to conceal debt, inflate earnings, and improperly earn huge fees for certain defendants;
- reported and unreported insider transactions in Enron securities and derivatives;
- current location of proceeds from insider trading;
- statements and check registers from off-shore accounts;
- luxury items purchased with insider trading proceeds;
- interests or participation in public and nonpublic corporations, limited partnerships, or other entities;
- tax returns;
- safe-deposit boxes and storage facilities; and
- professionals the defendants consulted concerning judgment or asset protection or disposal of proceeds beyond the Court's jurisdiction.

Accordingly, the discovery Lead Plaintiff seeks is more particularized than defendants suggest.

Some defendants rely on *In re Carnegie Int'l Corp. Sec. Litig.*, 107 F. Supp. 2d 676 (D. Md. 2000), to claim that Lead Plaintiff's discovery is not adequately particularized. In *Carnegie*, however, the subpoena included 21 document requests and called for testimony on 32 separate subjects. *Id.* at 684. By contrast, Lead Plaintiff's requests consist of nine document requests and eight interrogatories.⁴ Further, in *Carnegie*, plaintiffs also sought "all" documents concerning the relationship between the defendants and the Company's auditor. *Id.* The court held the discovery plaintiffs sought was "nothing more than a fishing expedition by both parties to obtain evidence that

⁴Defendant Skilling objects to this number due to "subparts," Skilling Opp. at 9, but only one document Request contains seven formal subparts. See Request No. 3. And this Request only concerns trading in Enron securities and derivatives.

can form the basis of a case against [the auditor]." *Id.* at 680. Here, Lead Plaintiff is not seeking evidence to bolster insufficient scienter allegations or to discover claims against a third party.

Some defendants rely on *Faulkner v. Verizon Communs., Inc.*, 156 F. Supp. 2d 384 (S.D.N.Y. 2001), to claim that Lead Plaintiff's discovery is not adequately particularized. In *Faulkner*, plaintiffs sought to lift the stay "for the sole purpose of uncovering facts to support the fraud allegations in the Complaint." *Id.* The *Faulkner* court held the discovery requests were not particularized towards that sole purpose, based on the fraud alleged. *Id.* at 405. That is not the case here. Lead Plaintiff seeks a discrete set of documents concerning insider-trading proceeds, the location of insider-trading proceeds, and off-shore accounts and transfers. This has nothing to do with fishing for evidence to support baseless securities fraud allegations.

D. Enron's Bankruptcy Does Not Preclude the Discovery Lead Plaintiff Seeks

The Officer Defendants argue Enron's bankruptcy and ensuing litigation stay precludes discovery against these former and current officers and directors. Officer Defs.' Opp. at 8-9. The text of the relevant statutory provision (11 U.S.C. §362), its legislative history, and supporting case law show otherwise. The automatic stay provision is self-executing only against the debtor (Enron) and, in the absence of a court-ordered extension, the automatic stay does not apply to co-defendants of the debtor. Moreover, Judge Gonzalez of the United States Bankruptcy Court of the Southern District of New York has already ordered discovery against the bankrupt Enron, so that Enron employees may use the information in pending litigation. *See* Ex. 1 hereto, *In re Enron Corp.*, No. 01-16034, Order Regarding Motion to Lift the Automatic Stay Pursuant to 11 U.S.C. §362, (Bankr. S.D.N.Y. Feb. 25, 2002). Thus, the Officer Defendants are asking for relief under the bankruptcy code which has not even been afforded the bankrupt entity itself.

The bankruptcy stay as to Enron "does not have a life of its own and ... may only be accomplished within the proper boundaries of Section 362." *In re Johns-Manville Corp.*, 26 B.R. 405, 414-15 (Bankr. S.D.N.Y. 1983). The statutory text of §362(a) only prohibits the continuation of a judicial action "*against the debtor*" to recover a claim "*against the debtor*." 11 U.S.C. §362(a)

(emphasis added). And the legislative history of §362 sets forth a clear intent to limit the applicability of the stay to claims against the *debtor's* property:

The automatic stay also provides creditor protection. Without it certain creditors would be able to pursue their own remedies *against the debtor's property*. Those who acted first would obtain payment of the claims in preference to and to the detriment of other creditors. Bankruptcy is designed to provide an orderly liquidation procedure under which all creditors are treated equally, a race of diligence by creditors for *the debtor's assets* prevents that.

H.R. Conf. Rep. No. 95-595, at 340, *reprinted* in 1978 U.S.C.C.A.N. 5963, 6297 (emphasis added).⁵

Authority for the proposition that the automatic stay is inapplicable to suits against non-debtors is overwhelming. "It is well settled that Section 362 of the Bankruptcy Code, which stays actions against the debtor and against property of the estate, does not forbid actions against its nondebtor principals, partners, officers, employees, co-obligors, guarantors, or sureties." *In re Arrow Huss, Inc.*, 51 B.R. 853, 856 (Bankr. D. Utah 1985). The Fifth Circuit has uniformly followed this rule. *See, e.g., Arnold v. Garlock, Inc.*, 278 F.3d 426, 2001 U.S. App. LEXIS 27275, at *19 (5th Cir. 2001) ("Section 362 is rarely, however, a valid basis on which to stay actions against non-debtors."); *Wedgeworth v. Fibreboard Corp.*, 706 F.2d 541, 544 (5th Cir. 1983), *vacated in part on other grounds*, 37 Fed. R. Serv. 2d (Callaghan) 879 (5th Cir. 1983) ("This literal interpretation of §362(a) is bolstered by language which is notably absent from its provisions. By way of comparison, Chapter 13 specifically authorizes the stay of action against co-debtors."); *Carway v. Progressive County Mut. Ins. Co.*, 183 B.R. 769, 774 (N.D. Tex. 1995) (automatic stay provision "generally does not extend to non-debtors such as insurers and co-defendants who may have some connection to the debtor"). Moreover, refusal to extend the stay to the individual defendants makes particular sense here because some of them are no longer employed by Enron (*e.g.*, Lay, Fastow and Skilling), and the individual defendants' liability here cannot be discharged by Enron's bankruptcy. *See* 11 U.S.C. §524(3); *In re Lowenschuss*, 67 F.3d 1394, 1401-02 (9th Cir. 1995); *In re American*

⁵*Accord Credit Alliance Corp. v. Williams*, 851 F.2d 119, 121 (4th Cir. 1988) ("Congress knew how to extend the automatic stay to non-bankrupt parties when it intended to do so. Chapter 13, for example, contains a narrowly drawn provision to stay proceedings against a limited category of individual cosigners of consumer debts."); *Teachers Ins. & Annuity Ass'n v. Butler*, 803 F.2d 61, 65 (2d Cir. 1986) ("Chapter 11, unlike Chapter 13, contains no provision to protect non-debtors who are jointly liable on a debt with the debtor.")

Hardwoods, 885 F.2d 621, 626 (9th Cir. 1989); *Underhill v. Royal*, 769 F.2d 1426, 1432 (9th Cir. 1985).

The Officer Defendants' reliance on a narrow exception carved out in a few unique cases is misplaced. In *A.H. Robins Co. v. Piccinin*, 788 F.2d 994 (4th Cir. 1986), more than 195,000 tort claims had been filed by persons seeking to recover injuries sustained through use of defendant's birth control device. The Fourth Circuit held the injunction barring action against non-debtors was within the court's equitable powers and expressly limited its holding to the unusual facts before it which included a plan for full payment of creditors claims. *Id.* at 698-701. The *A.H. Robins* court described exceptional circumstances which would have to exist to allow for an extension of the stay beyond the debtor:

This "unusual situation," it would seem, arises when there is such identity between the debtor and the third-party defendant that the debtor may be said to be the real party defendant and that a judgment against the third-party defendant will in effect be a judgment or finding against the debtor. An illustration of such a situation would be a suit against a third-party who is entitled to absolute indemnity by the debtor on account of any judgment that might result against them in the case.

Id. at 999. Further, the *A.H. Robins* court explicitly excluded from its limited exceptions instances (such as here) in which the third party is "independently liable" to the creditor. *Id.* at 999 (citation omitted).

In re Johns-Manville Corp., 26 B.R. 420 (Bankr. S.D.N.Y. 1983), *rev'd on other grounds*, 41 B.R. 926 (S.D.N.Y. 1984), is another case involving thousands of tort actions pending against non-debtor co-defendants with whom the debtors would be held jointly and severally liable. Observing the massive number of suits (among other things), the court, as in *A.H. Robins* held there must be unusual circumstances and certainly "[s]omething more than the mere fact that one of the parties to the lawsuit has filed a Chapter 11 bankruptcy must be shown in order that proceedings be stayed against non-bankrupt parties." *Johns-Manville*, 26 B.R. at 410 (citation omitted). *See also A.H. Robins*, 788 F.2d at 999. Here, it cannot be argued there is "such identity" between Enron and the officers and directors such that Enron may be said to be the real party and the circumstances here are not the "unusual" ones found in *A. H. Robins* and *Johns-Manville*.

In re Continental Airlines, 177 B.R. 475 (D. Del. 1993) is similarly inapplicable. In *Continental* the court found that there was an "identity of interest" between the debtor and non-debtors such that litigation against the non-debtor would directly affect the debtor. *Id.* at 479. Moreover, evidence was presented which showed that litigation was commenced against the non-debtor "solely in an effort to circumvent the stay." *Id.* Such is not the case here. Indeed, plaintiffs brought claims against the directors and officers before Enron ever filed for bankruptcy.

And, *In re First Cent. Fin. Corp.*, 238 B.R. 9 (Bankr. E.D.N.Y. 1999), **declined** to extend the stay to the company's officers and directors. *Id.* at 19-21.

In general, only a debtor is included within the protective umbrella afforded by the automatic stay Third-party defendants or co-defendants are typically not provided such protection. ***Therefore, lawsuits instituted against officers and directors of a corporate debtor are usually not stayed.***

Id. at 18 (emphasis added, footnote omitted). Under *First Cent.*, the result should be no different here.

The Officer Defendants may not seek shelter under Enron's bankruptcy here.

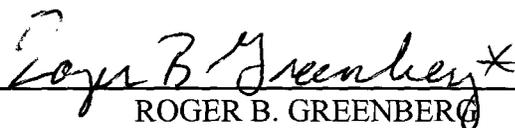
III. CONCLUSION

For the foregoing reasons, Lead Plaintiff's request for particularized discovery should be granted.

DATED: February 27, 2002

Respectfully submitted,

SCHWARTZ, JUNELL, CAMPBELL
& OATHOUT, LLP
ROGER B. GREENBERG
Federal I.D. No. 3932
State Bar No. 08390000



ROGER B. GREENBERG

Two Houston Center
909 Fannin, Suite 2000
Houston, TX 77010
Telephone: 713/752-0017

*BY PERMISSION

HOEFFNER & BILEK, LLP
THOMAS E. BILEK
Federal Bar No. 9338
State Bar No. 02313525
440 Louisiana, Suite 720
Houston, TX 77002
Telephone: 713/227-7720

Attorneys in Charge

Lead Counsel for Plaintiffs:

MILBERG WEISS BERSHAD
HYNES & LERACH LLP
WILLIAM S. LERACH
DARREN J. ROBBINS
HELEN J. HODGES
BYRON S. GEORGIOU
G. PAUL HOWES
JAMES I. JACONETTE
MICHELLE M. CICCARELLI
JAMES R. HAIL
JOHN A. LOWTHER
ALEXANDRA S. BERNAY
401 B Street, Suite 1700
San Diego, CA 92101
Telephone: 619/231-1058

MILBERG WEISS BERSHAD
HYNES & LERACH LLP
STEVEN G. SCHULMAN
SAMUEL H. RUDMAN
One Pennsylvania Plaza
New York, NY 10119-1065
Telephone: 212/594-5300

DECLARATION OF SERVICE BY MAIL

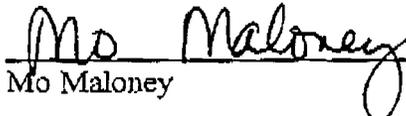
I, the undersigned, declare:

1. That declarant is and was, at all times herein mentioned, a citizen of the United States and a resident of the County of San Diego, over the age of 18 years, and not a party to or interest in the within action; that declarant's business address is 401 B Street, Suite 1700, San Diego, California 92101.

2. That on February 27, 2002, declarant served the LEAD PLAINTIFF'S REPLY REGARDING SUPPLEMENTAL BRIEFING PURSUANT TO THE COURT'S JANUARY 8, 2002 ORDER CONCERNING PARTICULARIZED DISCOVERY by depositing a true copy thereof in a United States mailbox at San Diego, California in a sealed envelope with postage thereon fully prepaid and addressed to the parties listed on the attached Service List.

3. That there is a regular communication by mail between the place of mailing and the places so addressed.

I declare under penalty of perjury that the foregoing is true and correct. Executed this 27th day of February, 2002, at San Diego, California.


Mo Maloney

ENRON (S.D. TEXAS/LEAL.
Service List - 02/27/02
Page 1

COUNSEL FOR PLAINTIFF(S)

Lynn Lincoln Sarko
(401k)
KELLER ROHRBACK LLP
1201 Third Avenue, Suite 3200
Seattle, WA 98101-3052
206/623-1900
206/623-3384 (fax)

Thomas E. Bilek
HOEFFNER & BILEK, LLP
440 Louisiana, Suite 720
Houston, TX 77002
713/227-7720
713/227-9404 (fax)

Rose Ann Reeser, Deputy Chief
Consumer Protection Division
OFFICE OF THE ATTORNEY GENERAL
P.O. Box 12548
Austin, TX 78711-2548
512/475-4632
512/473-8301 (fax)

Roger B. Greenberg
SCHWARTZ, JUNELL, CAMPBELL &
OATHOUT, LLP
Two Houston Center
909 Fannin, Suite 2000
Houston, TX 77010
713/752-0017
713/752-0327 (fax)

Justin M. Campbell, III
(401k)
CAMPBELL HARRISON & DAGLEY, LLP
4000 Two Houston Center
909 Fannin Street
Houston, TX 77010
713/752-2332
713/752-2330 (fax)

William S. Lerach
Helen J. Hodges
Byron S. Georgiou
MILBERG WEISS BERSHAD HYNES &
LERACH LLP
401 B Street, Suite 1700
San Diego, CA 92101-5050
619/231-1058
619/231-7423 (fax)

Melvyn I. Weiss
Steven G. Schulman
Samuel H. Rudman
MILBERG WEISS BERSHAD HYNES &
LERACH LLP
One Pennsylvania Plaza
New York, NY 10119-0165
212/594-5300
212/868-1229 (fax)

Steve W. Berman
Clyde A. Platt, Jr.
(401k)
HAGENS BERMAN LLP
1301 Fifth Avenue, Suite 2900
Seattle, WA 98101
206/623-7292
206/623-0594 (fax)

COUNSEL FOR DEFENDANTS

Stephen Susman *
SUSMAN GODFREY L.L.P.
1000 Louisiana Street
Suite 5100
Houston, TX 77002-5096
713/651-9366
713/653-7897 (fax)

James E. Coleman, Jr. *
CARRINGTON, COLEMAN, SLOMAN &
BLUMENTHAL
200 Crescent Court, Suite 1500
Dallas, TX 75201
214/855-3000
214/855-1333 (fax)

ENRON (S.D. TEXAS/LEAL
 Service List - 02/27/02
 Page 2

COUNSEL FOR DEFENDANTS

David Clarke, Jr *
 Keara M. Gordon
 PIPER MARBURY RUDNICK & WOLFE
 LLP
 1200 Nineteenth Street, N.W.
 Washington, DC 20036-2430
 202/861-3900
 202/223-2085 (fax)

Bruce Hiler *
 O'MELVENY & MYERS LLP
 555 13th Street, N.W.
 Washington, DC 20004-1109
 202/383-5300
 202/383-5414 (fax)

Eric Nichols *
 BECK, REDDEN & SECREST L.L.P.
 One Houston Center
 1221 McKinney Street, Suite 4500
 Houston, TX 77010
 713/951-3700
 713/951-3720 (fax)

Michael D. Warden *
 Thomas C. Green
 Luisa Caro
 SIDLEY AUSTIN BROWN & WOOD
 L.L.P.
 1501 K Street, N.W.
 Washington, DC 20005
 202/736-8000
 202/736-8711 (fax)

J. Clifford Gunter III *
 Abigail K. Sullivan
 BRACEWELL & PATTERSON, L.L.P.
 South Tower Pennzoil Place
 711 Louisiana Street, Suite 2900
 Houston, TX 77002-2781
 713/223-2900
 713/221-1212 (fax)

William F. Martson, Jr. *
 Zachary W.L. Wright
 TONKON TORP LLP
 888 S.W. Fifth Avenue
 Suite 1600
 Portland, OR 97204-2099
 503/802-2041
 503/927-3741 (fax)

Kathy D. Patrick *
 GIBBS & BRUNS, L.L.P.
 1100 Louisiana, Suite 5300
 Houston, TX 77002
 713/650-8805
 713/750-0903 (fax)

Charles G. King *
 James P. Pennington
 KING & PENNINGTON, L.L.P.
 711 Louisiana Street, Suite 3100
 Houston, TX 77002-2734
 713/225-8400
 713/225-8488 (fax)

Richard B. Drubel *
 BOIES SCHILLER & FLEXNER LLP
 26 South Main Street
 Hanover, NH 03755
 603/643-9090
 603/643-9010 (fax)

Craig Smyser *
 SMYSER KAPLAN & VESELKA, L.L.P.
 700 Louisiana Street, Suite 2300
 Houston, TX 77002
 713/221-2300
 713/221-2320 (fax)

ENRON (S.D. TEXAS/LEA)
Service List - 02/27/02
Page 3

COUNSEL FOR DEFENDANTS

John J. McKetta III *
Helen Currie Foster
GRAVES, DOUGHERTY, HEARON &
MOODY, P.C.
515 Congress Avenue, Suite 2300
Austin, TX 78701
512/480-5600
512/478-1976 (fax)

Jack C. Nickens *
Paul D. Flack
NICKENS, LAWLESS & FLACK,
L.L.P.
1000 Louisiana, Suite 5360
Houston, TX 77002
713/571-9191
713/571-9652 (fax)

Ronald G. Woods *
RONALD G. WOODS, ATTORNEY AT
LAW
5300 Memorial, Suite 1000
Houston, TX 77007
713/862-9600
713/864-8738 (fax)

Dr. Bonnee Linden *
PRO SE
1226 West Broadway, P.O. Box 114
Hewlett, NY 11557
516/295-7906
516/295-1975 (fax)

Billy Shepherd *
CRUSE, SCOTT, HENDERSON &
ALLEN, L.L.P.
600 Travis Street, Suite 3900
Houston, TX 77002-2910
713/650-6600
713/650-1720 (fax)

William R. McLucas *
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, DC 20037-1420
202/663-6000
202/663-6363 (fax)

H. Bruce Golden *
GOLDEN & OWENS, LLP
1221 McKinney Street, Suite 3600
Houston, TX 77010
713/223-2600
713/223-5002 (fax)

Jeffrey W. Kilduff *
O'MELVENY & MYERS LLP
1650 Tysons Blvd.
McLean, VA 22102
703/287-2402
703/287-2404 (fax)

Rusty Hardin *
RUSTY HARDIN & ASSOCIATES, P.C.
1201 Louisiana, Suite 3300
Houston, TX 77002
713/652-9000
713/652-9800 (fax)

Barry G. Flynn *
ATTORNEY AT LAW
1300 Post Oak Blvd., Suite 750
Houston, TX 77056
713/840-7474
713/840-0311 (fax)

Paul Vizcarrondo, Jr. *
David Gruenstein
Jonathan E. Pickhardt
WACHTELL, LIPTON, ROSEN & KATZ
51 West 52nd Street
New York, NY 10019
212/403-1000
212/403-2000 (fax)

Sharon Katz *
DAVIS POLK & WARDWELL
450 Lexington Avenue
New York, NY 10017
212/450-4000
212/450-3633 (fax)

ENRON (S.D. TEXAS/LEAL
Service List - 02/27/02
Page 4

COUNSEL FOR DEFENDANTS

Barnes H. Ellis *
STOEL RIVES LLP
900 S.W. Fifth Avenue
Suite 2300
Portland, OR 97204-1268
503/224-3380
503/220-2480 (fax)

COURTESY COPIES

Carolyn S. Schwartz
UNITED STATES TRUSTEE, REGION 2
33 Whitehall Street, 21st Floor
New York, NY 10004
212/510-0500
212/668-2255 (fax)

* Denotes service via overnight mail

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

----- X
In re: : Chapter 11
: :
: : Case No. 01-16034 (AJG)
ENRON CORP., *et al.*, : :
: : Jointly Administered
Debtors. : :
----- X

**ORDER REGARDING MOTION TO LIFT THE AUTOMATIC STAY
PURSUANT TO 11 U.S.C. § 362**

Upon consideration of the motions, dated January 24, 2002 and January 31, 2002, filed by the *Tittle* and *Kemper* Plaintiffs for relief from the automatic stay as to Debtor Enron Corporation ("Enron" or "the Company" or "the Debtor") to permit them to liquidate their pre-petition claims against the Company pending in the Southern District of Texas for the Company's alleged breaches of fiduciary duty under the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. § 1001, *et seq.* ("the Motions"); the objections of the Debtors, dated February 15, 2002; the objections of the Official Committee of Unsecured Creditors, dated February 15, 2002; and oral argument of February 20, 2002, it is hereby and upon the entire record herein; and good and sufficient cause appearing,

ORDERED:

1. The automatic stay is hereby continued until June 21, 2002 except as provided below;
2. Enron will participate in the February 25, 2002 scheduling conference or further scheduling conferences to be held before the Honorable Melinda

NY1:1108895702WCR021.DOC43889.0013

Harmon of the Southern District of Texas in the ERISA cases consolidated under the caption *Titile, et al. v Enron Corp., et al*, No. H-01-3913 (S.D. Tex.), and participate in such discussions with counsel as are necessary to establish a schedule in that action;

3. Following the selection of lead counsel *and* consistent with any order, including scheduling order, entered by Judge Harmon, Enron will produce, subject to attorney client privilege or work product protection: (1) a copy of all documents and materials Enron produced since filing for bankruptcy in connection with any inquir(ies) or investigation(s) into the Company's handling of its ERISA-governed pension plans, that were provided, or that may be provided, pursuant to subpoena (a) by any committee of the Legislative branch of the United States Government, or (b) by the Executive branch of the United States Government, including but not limited to, the Department of Labor; and (2) copies of all transcripts of ~~witness interviews or depositions in Enron's possession, custody, or~~
control given or taken in connection with said inquir(ies) or investigation(s);
4. That the automatic stay as to Enron shall be LIFTED as of June 21, 2002 for all purposes, *provided that* plaintiffs shall not seek to enforce any judgment against the assets of the Debtor without further order of this Court;
5. That, subject to such scheduling orders as Judge Harmon may enter, plaintiffs in the consolidated ERISA actions may serve a Consolidated

Amended Complaint upon, and propound formal discovery to, Enron, *provided that* the Company shall be under no obligation to answer, respond, object or otherwise move until June 21, 2002 or such other later date as established by Judge Harmon;

6. This Order is without prejudice to the right of the Company to seek a reimposition of the stay at any time; and
7. This Order is also without prejudice to the right of the *Kemper* Plaintiffs or such other ERISA plaintiffs to seek a ruling from the Court that the \$85 million proceeds of the ERISA Fiduciary Liability Insurance Policy (which is the subject of the Debtors' January 18, 2002 Motion for Authorization and the *Kemper* Plaintiffs' January 31, 2002 Limited Objections thereto) are not assets of the Debtor's estate and should be available, without further order of this Court, to satisfy or partially satisfy any judgment plaintiffs may obtain in the consolidated ERISA actions against Enron.

Dated: New York, New York
February 25, 2002

s/Arthur J. Gonzalez

THE HONORABLE ARTHUR J. GONZALEZ
UNITED STATES BANKRUPTCY JUDGE