United States Courts
Southern District of Texas
FILED
FEB 28 2002
Michael N. Milby, Clerk

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

HAROLD AHLICH, et al., Plaintiffs,	§	
	§	CIVIL ACTION No. H-02-0347
v.	§	CONSOLIDATED LEAD H-01-3624
ARTHUR ANDERSEN, L.L.P., et al., Defendants	§	

DEFENDANT ARTHUR ANDERSEN LLP'S
RESPONSE TO PLAINTIFFS' MOTION TO REMAND.

Defendant Arthur Andersen LLP ("Andersen") respectfully submits this response in opposition to Plaintiffs' Motion to Remand.

A. INTRODUCTION

This action is a one of at least seven lawsuits brought by the law firm of Fleming & Associates, L.L.P. ("the Fleming firm") on behalf of shareholders of Enron Corporation who allege certain defendants defrauded them.[1] Andersen removed this action from state court because the claims in it have been preempted and made removable by the Securities Litigation Uniform Standards Act of 1998 ("SLUSA").

Plaintiffs' motion to remand relies on a single argument as to why this case should not be adjudicated in this Court; namely, that it is not a "covered class action" as defined in SLUSA because it is brought on behalf of fewer than 50 persons. As an initial matter, plaintiffs'

[1] This Court has already recognized five such suits. *See Newby v. Enron Corp.*, No. 01-CV-3624, mem. op. at 2 (S.D. Tex., Feb. 15, 2002) (hereafter "Fleming Firm Order") ("The *José* case represents the fifth in a series of lawsuits filed by Fleming & Associates, L.L.P. on behalf of shareholders of Enron Corporation who allege defendants defrauded them."). The Fleming firm has filed at least two other cases on behalf of Enron shareholders that this Court has yet to mention. *See Delgado v. Fastow, et al.*, Cause No. 2002-00569, Harris Co., Texas, *removed to* United States District Court for the Southern District of Texas, Houston Division, C.A. No. H-02-0673; *Pearson v.Fastow, et al.*, Cause No. 2002-00609, Harris Co., Texas *removed to* United States District Court for the Southern District of Texas, Houston Division, C.A. No. H-02-0670.

#335

argument runs counter to its own pleadings and is inconsistent with the plain language of SLUSA.

This suit is part and parcel of a broad scheme orchestrated and controlled by plaintiffs' attorneys to file a series of actions, each on behalf of fewer than 50 persons but collectively on behalf of hundreds (or possibly thousands) of persons to avoid preemption and removal under SLUSA. *See* Fleming Firm Order at 4 ("The inevitable inference" of the Fleming firm's collection of plaintiffs in groups less than 50 "is that [it] thereby hopes to avoid the prohibitions of SLUSA"). Each of the Fleming firm's lawsuits "recites essentially the same facts giving rise to essentially the same claims against essentially the same defendants." *See* Fleming Firm Order at 5; *see also* exhibits 4 & 5. This attempt to evade SLUSA's removal provisions is contrary to Congress's clear intent, is extremely wasteful and duplicative of counsel and judicial resources, and if permitted to succeed would undermine SLUSA. This Court should conclude that all of the lawsuits controlled by the Fleming firm constitute a single lawsuit for purposes of SLUSA.

B. PROCEDURAL BACKGROUND AND PLAINTIFFS' ALLEGATIONS

The forty-five plaintiffs in this lawsuit initiated this action in the 272nd Judicial District of the District Court of Brazos County, Texas on or about January 29, 2001, alleging state law claims against Andersen, some of its partners, and other defendants related to the financial difficulties of Enron Corporation. On the same day, plaintiffs sought a Temporary Restraining Order in the Brazos County court. Andersen filed a Notice of Removal in this Court on January 30, 2002, and plaintiff filed the instant motion to remand on February 8, 2002.

Plaintiffs allege several counts against Andersen, all ostensibly brought under Texas common law or Texas state statutes. (Pet., ¶¶ 116-149.) Although plaintiffs' claims facially sound in common law fraud, negligence, conspiracy, and violations of the Texas Business and

Commerce Code, they rest on allegations that Andersen and others. *See* 15 U.S.C. § 78bb(f)(1)(a). Plaintiffs also allege that Enron stock "was traded on the New York Stock Exchange." Pet. ¶ 131.

C. ARGUMENT

In 1995, Congress passed the Private Securities Litigation Reform Act (the "Reform Act") to provide uniform standards for class actions (or their equivalent) alleging violations of the federal securities laws. Among other things, the Reform Act imposed heightened pleading requirements in securities fraud actions. Seeking to avoid this new hurdle, as well as other features of the Reform Act, plaintiffs in securities class actions brought suit in state courts. Because Congress perceived that suits being brought in state court often involved federal securities claims in the guise of state law claims, Congress in 1998 moved to close this loophole by enacting SLUSA. *See* SLUSA, Pub. L. No. 105-353, § 2, 112 Stat. 3227 (1998) (codified as a note to 15 U.S.C. § 78a); *see also Coy v. Arthur Andersen LLP*, No. 01-CV-4248, mem. op. at 11 (S.D. Tex., Feb. 6, 2002) ("When . . . plaintiffs began filing in state rather than federal court, asserting claims under state statutory or common law to avoid the PSLRA's stringent procedural pleading hoops, Congress passed SLUSA in order to close the loophole."); *Wald v. C.M. Life Ins. Co.*, No. Civ. 3:00-CV-2520-H, 2001 WL 256179, at *4 (N.D. Tex. Mar. 8, 2001).

SLUSA precludes plaintiffs from maintaining "covered class actions" alleging state law claims for losses suffered due to material misrepresentations made in connection with the purchase or sale of certain securities. 15 U.S.C. § 78bb(f)(1).[2] Significantly, Congress did not

---

[2]This provision states:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging –

leave it to state courts to dismiss these state-law claims; rather, Congress expressly granted defendants access to a federal forum for this purpose, providing that these class actions "shall be removable to the Federal district court for the district in which the action is pending." 15 U.S.C. § 78bb(f)(2).[3]

In particular, a suit is removable under SLUSA if

> (1) the action is a "covered class action" under SLUSA; (2) . . . the causes of action on their face are based on state statutory or common law; (3) . . . it involves a "covered security" under SLUSA; (4) . . . it alleges Defendants have misrepresented or omitted material facts; and (5) . . . the alleged misstatement or omission was made "in connection with" the purchase or sale of the covered security.

Coy v. Arthur Andersen LLP, No. 01-CV-4248, mem. op. at 14 (S.D. Tex., Feb. 6, 2002); *see also Hardy v. Merrill Lynch, Pierce, Fenner & Smith*, No. 01 Civ. 5973 (NRB), 2001 WL 1524471, at *3 (S.D.N.Y. Nov. 30, 2001); *Green v. Ameritrade, Inc.*, No. 01-1251, 2002 WL 126170, at *4 (8th Cir. Feb. 1, 2002).

There is no dispute that the four latter requirements are satisfied here. The claims are all brought under Texas statutes or the common law. *See* Pet. ¶¶ 136-60. The Petition alleges that Enron stock "was traded on the New York Stock Exchange," Pet. ¶ 57, which makes it a

---

(A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or

(B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

[3] In doing so, Congress placed these state-law class actions beyond the ambit of the well-pleaded complaint rule relied on by plaintiffs. *See, e.g.*, *Verlinden B.V. v. Central Bank of Nigeria*, 461 U.S. 480, 494 (1983). Indeed, one of the requirements for removal under SLUSA is that the action be "based upon the statutory or common law of any State." 15 U.S.C. § 77bb(f)(1) (emphasis added). Thus, like the artful pleading doctrine, *see Terrebonne Homecare, Inc. v. SMA Health Plan, Inc.*, 271 F.3d 186, 188 (5th Cir. 2001), SLUSA does not allow a plaintiff to avoid removal simply by cloaking federal claims in state law.

"covered security" under SLUSA. *See* 15 U.S.C. §§ 78bb(f)(5)(E), 77r(b)(1)(A). The Petition further alleges that the defendants "made various untrue and deceptive statements of material facts and omitted to state material facts ... not misleading" which "induced Plaintiffs to purchase and/or retain Enron common stock at artificially inflated prices." Pet. ¶ 137.

A. Plaintiffs' Claims are Part of a "Covered Class Action"

This Court should deny plaintiffs' motion to remand because plaintiffs' filing in state court is part of counsel's artificial, manipulative scheme to evade SLUSA's removal provisions. Plaintiffs' sole contention is that this case is not a "covered class action" because this action does not meet the "50 person or prospective class member" threshold. *See* 15 U.S.C. § 78bb(f)(5)(B)(i)(I). However, plaintiffs' counsel represents over 750 clients who seek or will seek recovery related to Enron's financial difficulties from Andersen and the other defendants. *See* Fleming Firm Order at 3. Each of the Fleming firm's lawsuits "recites essentially the same facts giving rise to essentially the same claims against essentially the same defendants." *See* Fleming Firm Order at 5.

Plaintiffs' counsel have sought to avoid removal under SLUSA by bringing a series of different lawsuits in different courts, each with 50 or fewer plaintiffs and each not expressly styled as a class action. These include:

A. *Fred Rosen, et al. v. Andrew Fastow, et al.*, now pending in the United States District Court for the Southern District of Texas, Houston Division, Cause No. H-02-CV-0199, (removed from Cause No. 2001-57517 in the 333rd District Court of Harris County, Texas) (13 plaintiffs named plus the Houston Federation of Teachers on behalf of its 5,700 members);

B. *Jane Bullock, et al. v. Arthur Andersen, L.L.P., et al.*, now pending in the United States District Court for the Western District of Texas, Austin Division, Cause No. A-02-CA-070-SS (removed from Cause No. 32716 in the 21st Judicial District Court of Washington County, Texas) (12 plaintiffs named);

C. *David Jose v. Arthur Andersen, L.L.P., et al.*, now pending in the U.S. District Court for the Western District of Texas, San Antonio Division, C.A. SA-02-CA-

01870G (removed from the 57th Judicial District Court of Bexar County, Texas, (4 plaintiffs);

D. *Delgado v. Fastow, et al.*, in the the U.S. District Court for the Southern District of Texas, Houston Division, consolidated under C.A. H-01-3624; (removed from Cause No. 2002-00569, in the 55th Judicial District Court of Harris Co., Texas) (2 plaintiffs named);

E. *Pearson v. Fastow, et al.*, pending in the U.S. District Court for the Southern District of Texas, Houston Division, consolidated under C.A. H-01-3624 (removed from Cause No. 2002-00609, in the 164th Judicial District Court of Harris Co., Texas) (2 plaintiffs named); and

F. *John Odam et al. v. Enron Corp., et al.*, in the United States District Court for the Southern District of Texas, Houston Division, Cause No. H-01-CV-3914 (6 plaintiffs named);

G. This action (45 plaintiffs named).

The Fleming firm actions contain an apparently random grouping of plaintiffs from around the country. The plaintiffs in this *Ahlich* case are citizens of twelve different states: Arizona, Florida, Texas, California, Massachusetts, New York, Georgia, Ohio, Michigan, Georgia, Utah, and North Carolina. *See* Pet. ¶¶ 2-34. Plaintiffs in the *Rosen* action include citizens of Tennessee, Kentucky, Mississippi, Wisconsin, Florida, Arizona, and West Virginia–grouped together only at the whim of the Fleming firm. *See Rosen* Pet. ¶¶ 6-14. The sole rational for groupings is to artificially avoid SLUSA. *See* Fleming Firm Order at 4 ("Jez is careful to point out that his suits are not denominated class actions and they do not aggregate 50 or more plaintiffs in any one suit. The inevitable inference is that he thereby hopes to avoid the prohibitions of SLUSA").

The Fleming firm's actions constitute a clear abuse of the SLUSA provision permitting certain small, non-class actions to remain in state court. As this Court has found:

> It is now abundantly clear, contrary to the inferences [the Fleming firm] wished the court to draw from [its] representations on January 30, 2002, that in the absence of an injunction prohibiting Fleming from filing new actions and seeking emergency relief, Fleming will proceed on a county-by-county basis throughout the State of Texas filing actions and seeking the same emergency relief undertaken in the *Bullock*, *Ahlich*, and *Jose* cases.

Fleming Firm Order at 7-8. The federalism concerns that motivated this provision would be seriously undermined by a flood of nearly identical state court actions, inefficiently spread out through courts across the state. Recognizing the inefficiency of having similar cases pending in separate courts, Texas law – as discussed in further detail below – grants defendants a right to consolidate these cases. But there is no reason to believe that, faced with motions to consolidate, the games-playing plaintiffs lawyers who devised this strategy to evade SLUSA would not attempt to defeat that right by strategic dismissals and re-filings of these cases. The resulting litigation would represent an needless burden on the state courts, consuming state judicial resources; at best, it would result in eventual consolidation and removal to federal court. Either way, Congress did not, in its solicitude for the state judiciary, intend to overwhelm state courts with claims by large numbers of plaintiffs from around the country whose claims are strategically split up and inefficiently spread throughout courts across the state.

To the contrary, SLUSA was adopted to ensure that certain actions that are, in substance, federal securities law claims are not brought in state court, under state law, to avoid the application of the Reform Act. Fleming Firm Order at 4; *Coy v. Arthur Andersen LLP*, No. 01-CV-4248, slip op. at 11 (S.D. Tex., Feb. 6, 2002); *Lander*, 251 F.3d at 108. Further, "[a]ccording to Congress, [SLUSA] should be interpreted broadly to reach mass actions and <u>all other procedural devices</u> that might be used to circumvent the class definition." *Bertram v. Terayon Communications Systems, Inc.*, No. 00-CV-12653 (SVW), 2001 WL 514358 (C.D. Cal., March 27, 2001) (holding that plaintiff could not avoid SLUSA simply by seeking equitable relief as opposed to damages) (emphasis added) (citation omitted.)

The scheme devised by plaintiffs' counsel attempts to evade not only the Reform Act but SLUSA itself, and plainly contravenes the purpose behind the statute's enactment. Just as "artful

pleading" will not allow a plaintiff to defeat removal, *see, e.g.*, *Terrebonne Homecare, Inc. v. SMA Health Plan, Inc.*, 271 F.3d 186 (5th Cir. 2001); *Aaron v. National Union Fire Ins. Co.*, 876 F.2d 1157, 1160-62 (5th Cir. 1989), "artful filing" of the kind engaged in here should not permit avoidance of Congress's clear intention to preempt all claims covered by SLUSA. As one court has held, "[a] rule that allows a plaintiff to defeat a defendant's right to remove a class action through such a hollow procedural maneuver would surrender [SLUSA's] application to the class action plaintiffs the statute seeks to keep at bay." *Gibson v. PS Group Holdings, Inc.*, No. 00-CV-0372, 2000 WL 777818, *4 (S.D. Cal., June 14, 2000) (finding plaintiff's intentional removal of a prayer for damages in an attempt to avoid SLUSA was ineffectual, but remanding on other grounds). "Clearly SLUSA was enacted to prevent just such gamesmanship ... ." *See* Fleming Firm Order at 4.

Plaintiffs might counter by arguing that, for better or for worse, they are merely exploiting loopholes in SLUSA. But statutory interpretation is not blind to the distinction between invoking an exception and abusing it, and SLUSA can be read to authorize removal under these circumstances. In particular, the group of lawsuits brought by plaintiffs' counsel should not be naively viewed as proceeding separately. Rather these coordinated lawsuits, which collectively seek damages on behalf of more than 50 people, must be seen as "proceed[ing] as a single action." 15 U.S.C. s 78bb(f)(5)(B)(ii). This Court should determine that all actions brought by the Fleming Firm arising out of Enron's financial difficulties constitute in reality a single action.

B. <u>The Fleming Firm's Cases are "Pending in the Same Court"</u>

Moreover, as mentioned above, defendants have a right under Texas law to consolidate all of these actions before a single state court judge. *See* Tex. R. Jud. Admin. 11.4(h). This rule

provides that on a motion for consolidation:

> The presiding judge must grant the motion or request if the judge determines that: (1) the case involves material questions of fact and law common to a case in another court and county; and (2) assignment of a pretrial judge would promote the just and efficient conduct of the cases. Otherwise, the presiding judge must deny the motion or request.

Moreover, a refusal to grant a consolidation motion is subject to mandamus review by the Texas Supreme Court. *See* Tex. R. Jud. Admin. 11.5.[4] Accordingly, the actions subject to this right of consolidation are, for all practical purposes, "pending in the same court" under SLUSA.[5] Any ruling otherwise would require defendants to go through the empty formality of consolidating the cases in state court, delaying the removal mandated by Congress and thereby facilitating plaintiffs' manipulation of SLUSA. This can be avoided by recognizing that "pending in the same court" encompasses actions that the defendant has a right under State law to consolidate in the same court. This reading of SLUSA avoids needlessly forcing the defendants to go through the empty formality of consolidating these actions which they have a right to consolidate under Texas law.

---

[4]The use of the term "must," accompanied by the express availability of mandamus, makes it clear that a determination under this Rule is not discretionary. Therefore, 15 U.S.C. § 78bb(f)(5)(B) is not implicated here.

[5]This case would have been consolidated with other Enron-related cases pending in Harris and surrounding counties in the Second Administrative Judicial Region of Texas. *See* Tex. Gov't Code § 74.042(c) ("The Second Administrative Judicial Region is composed of the counties of Angelina, Bastrop, Brazoria, Brazos, Burleson, Chambers, Fort Bend, Freestone, Galveston, Grimes, Hardin, Harris, Jasper, Jefferson, Lee, Leon, Liberty, Limestone, Madison, Matagorda, Montgomery, Newton, Orange, Polk, Robertson, Sabine, San Augustine, San Jacinto, Trinity, Tyler, Walker, Waller, Washington, and Wharton.").

C. Plaintiffs Allege Removable, Federal Question Insider Trading Claims.

Notwithstanding the Court's determination of whether Plaintiffs' claims are part of a "covered class action" for purposes of SLUSA, which Andersen urges the Court to find, all of plaintiffs' claims were properly removed. Plaintiffs have alleged and seek remedies under federal law–specifically, plaintiffs assert insider trading claims. Insider trading claims are creations of federal law. Section 20A of the Securities and Exchange Act of 1934, as amended, creates the private right of action for insider trading. 15 U.S.C. § 78t-1(a); *Newby v. Enron Corp.*, C.A. No. H-01-3624, 2002 WL 200956, * at 8 (S.D. Tex., Jan. 9, 2002). Disgorgement of insider trading proceeds is a remedy authorized by the Insider Trading and Securities Fraud Enforcement Act of 1988. *See* 15 U.S.C. § 78t-1(b); *Newby v. Enron Corp.*, * at 8. Federal courts have exclusive jurisdiction over alleged violations of the Securities and Exchange Act of 1934, such as violations of section 20 A. *See* 15 U.S.C. § 78aa.

Plaintiffs claims and requests for relief clearly fall within federal court jurisdiction. Plaintiffs claim that certain defendants engaged in illegal insider trading. *See, e.g.*, Pet. ¶¶ 130. Not content to make mere factual allegation, plaintiffs also expressly seek the remedy of disgorgement: "Plaintiffs seek a disgorgement of Lay's ill-gotten gains made at the expense of Plaintiffs." *Id.*; *see also id.* ("Plaintiffs seek a disgorgement of Skillings' ill-gotten gains.").

Plaintiffs attempt to minimize these express federal insider trading claims by characterizing them as mere "factual actions [that] do not transform this action into a securities fraud case ... ." Plaintiffs' Motion to Remand at 3, n.2. Plaintiffs argument fails for three reasons. First, plaintiffs' insider trading claims are not mere "factual allegations"; plaintiffs seek affirmative relief for them. *See* Pet., ¶ 130. Second, plaintiffs expressly incorporate their illegal insider trading claims, which includes the disgorgement relief sought, as part of their fraud,

negligence, and civil conspiracy causes of action. *See, e.g.*, Pet. ¶¶ 136, 146, 156. Third, plaintiffs cite no authority to support their position.[6]

---

[6]Because Plaintiffs allege removable federal claims, Andersen's removal of any non-preempted state law claims was proper pursuant to this Court's supplemental jurisdiction under 28 U.S.C. §§ 1367 and 1441. *See* Andersen's Notice of Removal, ¶ 15. 28 U.S.C. §1367 extends federal court jurisdiction so that "in any civil action of which the district courts have original jurisdiction, the district courts shall have supplemental jurisdiction over all other claims that are so related to claims in the action within such original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution."

The Newby Court recently decided a similar matter. It determined that removal of certain federal claims was proper under SLUSA; however it exercised supplemental jurisdiction over any remaining state law claims because of the close nexus between the alleged state law claims and the federal claims. *See Coy v. Arthur Andersen LLP*, No. 01-CV-4248, slip op. at 23 (S.D. Tex., Feb. 6, 2002). In *Coy*, the Court found that:

> [I]n this case the federal and state claims are not truly separate and distinct, but involve the same case or controversy over those in the consolidated class action. Indeed, all related Enron cases currently consolidated before this Court basically allege a fraudulent scheme by Enron, aided by Arthur Andersen, L.L.P., with claims based on the same conduct, arising from the same nucleus of operative fact, resulting in a strong nexus between federal and state claims that supports federal jurisdiction.

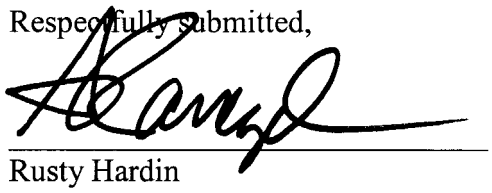
As demonstrated above, the *Ahlich* plaintiffs' state law claims are based on the same conduct, arise from the same nucleus of operative fact, and result in a strong nexus between all claims in the *Newby* action, whether federal and state in nature. This Court should exercise its supplemental jurisdiction over any remaining state law claims. Just like *Coy*, this case clearly supports the exercise of federal court jurisdiction over any state law claims that are not preempted by SLUSA.

D. CONCLUSION

For the foregoing reasons, Defendant Arthur Andersen LLP respectfully requests that plaintiffs' motion to remand this action to Texas state court be denied, and such other relief as this Court may deem just and proper.

Dated: Houston, Texas
February 28, 2002

Respectfully submitted,



Rusty Hardin
State Bar No. 08972800
S.D. Tex. I.D. No. 19424

Attorney-in-Charge for
Defendant Arthur Andersen, L.L.P.

OF COUNSEL
Andrew Ramzel
State Bar No. 00784814S.D. Tex. I.D. No. 18269
RUSTY HARDIN & ASSOCIATES, P.C.
1201 Louisiana, Suite 3300
Houston, Texas 77002
(713) 652-9000
(713) 652-9800 (fax)

Michael Carroll
Daniel Kolb
Sharon Katz
DAVIS POLK & WARDWELL
450 Lexington Avenue
New York, New York 10017
(212) 450-4000
(212) 450-3633 facsimile

CERTIFICATE OF SERVICE

I hereby certify that on this 1 day of March, 2002, the foregoing pleading was served on the following counsel of record by certified mail, return receipt requested:

Mr. G. Sean Jez
Fleming & Associates, L.L.P.
1330 Post Oak Blvd., Suite 3030
Houston, Texas 77056-3019

Mr. William Lerach
Milberg Weiss Bershad Hynes & Lerach, L.L.P.
401 B Street, Suite 1700
San Diego, CA 921010-4297

and was served on defense counsel by first class mail.

Andrew Ramzel