United States Courts
Southern District of Texas
FILED
MAY 0 8 2002
Michael N. Milby, Clerk

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

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| In re ENRON CORPORATION SECURITIES LITIGATION<br>- - - - - - - - - - - - - - - - - - - - - - - - - - - - - - - -<br>This Document Relates To:<br><br>MARK NEWBY, et al., Individually and On Behalf of All Others Similarly Situated,<br><br>Plaintiffs,<br><br>- against -<br><br>ENRON CORP., et al.,<br><br>Defendants, | §<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§ | Civil Action No. H-01-3624<br>(Consolidated) |
| THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, et al., Individually and On Behalf of All Others Similarly Situated,<br><br>Plaintiffs,<br><br>- against -<br><br>KENNETH L. LAY, et al.,<br><br>Defendants. | §<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§<br>§ | CLASS ACTION |

MOTION OF THE INDIVIDUAL ANDERSEN DEFENDANTS TO
DISMISS COUNT I OF PLAINTIFFS' CONSOLIDATED COMPLAINT

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MOTION OF THE INDIVIDUAL ANDERSEN DEFENDANTS TO DISMISS COUNT I OF PLAINTIFFS' CONSOLIDATED COMPLAINT

Defendants Thomas H. Bauer, Michael L. Bennett, Joseph F. Berardino, Debra A. Cash, Donald Dreyfus, James A. Friedlieb, D. Stephen Goddard, Jr., Gary B. Goolsby, Gregory W. Hale, Michael D. Jones,[1] Michael M. Lowther, Benjamin S. Neuhausen, Richard R. Petersen, Danny D. Rudloff, John F. Sorrells, John E. Stewart, William E. Swanson, Nancy Temple and Roger D. Willard (collectively, the "Individual Andersen Defendants")[2], respectfully move this Court to dismiss the Consolidated Complaint dated April 8, 2002 against each of them individually pursuant to Rules 12(b)(6) and 9(b) of the Federal Rules of Civil Procedure, and section 21D(b)(3) of the Securities and Exchange Act of 1934 (the "Exchange Act"), as amended.

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[1] Defendant Michael Jones independently moves to dismiss the Complaint as to him pursuant to Rule 12(b)(5), Fed. R. Civ. P., on the ground that service was defective. The Hague Convention on the Service Abroad of Judicial and Extra-Judicial Documents in Civil or Commercial Matters applies to all cases "where there is occasion to transmit a judicial or extraterritorial document for service abroad." Nov. 15, 1965, 20 U.S.T. 361, 362, Art. 1, reprinted in 28 U.S.C.A. Fed. R. Civ. P. 4 (West 1992) (hereafter the "Hague Convention"). Compliance with the terms of the Hague Convention is mandatory in all cases to which it applies. See Volkswagenwerk AG v. Schlunk, 486 U.S. 694, 699 (1988). The United States and the United Kingdom are both signatories to the Hague Convention (ratified Nov. 17, 1976, as amended Oct. 28, 1997).

Here, plaintiffs sent the Complaint to Jones international mail, specifically via United Parcel Service. While courts in the Fifth Circuit are split as whether Article 10(a) of the Hague Convention permits service of process via mail abroad, Jones submits that Article 10(a) does not permit such service. Thus, the attempted service of the Complaint on him was improper. See Postal v. Princess Cruises, Inc., 163 F.R.D. 497, 499 (N.D. Tex. 1995) (holding that Article 10(a) does not permit service of process by mail); but see Lafarge Corp. v. M/V Macedonia Hellas, No. Civ. A. 99-2648, 2000 WL 687708, at *10-11 (E.D. La. May 24, 2000) (holding that Article 10(a) permits service of process by mail).

[2] The Individual Andersen Defendants include Michael C. Odom, although Mr. Odom will be filing a separate Motion to Dismiss.

## PRELIMINARY STATEMENT

The Consolidated Complaint names over 80 defendants and spans more than 500 pages, with over 1,000 paragraphs. It incorporates more than 225 documents – 139 analyst reports, 40 press releases, 19 presentations to analysts, 17 registration statements, 4 financial statements, 4 Form 10Ks and 3 annual reports – alleged to contain false or misleading statements. It discusses approximately 50 transactions and covers a period of over 5 years.

One needs to literally scour the Consolidated Complaint to locate the few scattered references to the 20 named Individual Andersen Defendants. Once found, the references are conclusory and far more remarkable for what they fail to say than for what they do say. Not one of the allegations claims that any of these individuals made a false statement; for this reason alone, none of these individuals can be held primarily liable for securities fraud. There are no allegations that plaintiffs reasonably relied to their detriment on anything said or done by an Individual Andersen Defendant. Moreover, the facts that are alleged are not sufficiently particularized and, even if proved, do not show a strong inference of scienter with respect to any one of the Individual Andersen Defendants, as required by Rule 9(b) of the Federal Rule of Civil Procedure ("F.R.C.P.") and the Private Securities Litigation Reform Act of 1995 (the "PSLRA").

Nor does the Consolidated Complaint adequately plead "control person" liability under § 20(a) against Joseph F. Berardino or against any other Individual Andersen Defendant. Any such liability is, in the first instance, dependent on a showing of a primary violation by the allegedly controlled entity, Arthur Andersen, LLP ("Andersen"). As set forth in Andersen's separate motion to dismiss the Consolidated Complaint, plaintiffs have failed to allege such a primary violation. In any event, plaintiffs have not adequately alleged the requisite control over

either Andersen or the transactions at issue to allege a violation of § 20(a).

Thus, the Consolidated Complaint fails to state a claim against any of the Individual Andersen Defendants for violations of § 10(b) of the Exchange Act, SEC Rule 10b-5 promulgated thereunder, or § 20(a) of the Exchange Act. Because these are the only claims in the Consolidated Complaint asserted against the Individual Andersen Defendants, the Consolidated Complaint should be dismissed as against each and every one of them.[3]

## SUMMARY OF ALLEGATIONS

For purposes of deciding a motion to dismiss under F.R.C.P. 9(b) or 12(b)(6), the Court may accept as true only well-pleaded allegations of fact.[4] See In re Sec. Litig. BMC Software, Inc., 183 F. Supp. 2d 860, 866 n.13 (S.D. Tex. 2001) (Harmon, J.) (citing Lawal v. British Airways, PLC, 812 F. Supp. 713, 716 (S.D. Tex. 1992)). Conclusory allegations should be disregarded. See Tuchman v. DSC Communications Corp., 14 F.3d 1061, 1067 (5th Cir. 1994).

According to the Consolidated Complaint, Plaintiffs purchased shares of Enron Corp. ("Enron") from October 19, 1998 through November 27, 2001. Compl. ¶ 1.[5] Plaintiffs allegedly

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[3] The Consolidated Complaint is defective under F.R.C.P. 8 in that it fails to specify which claims are being asserted against which defendants. For instance, in Count I plaintiffs allege that "Defendants violated §§ 10(b) and/or 20(a) of the 1934 Act and Rule 10b-5." Compl. at ¶ 995. Based on this, each one of the 20 Individual Andersen Defendants (as well as the additional 51 defendants named in this Count) is left to try to determine whether plaintiffs' allegations are intended to charge him or her with a § 10(b) violation, or a § 20(a) violation, or both.

Plaintiffs identify a § 20(a) claim against only one defendant, Joseph F. Berardino, whom they "name[ ] herein as [a] control person[ ] of Andersen pursuant to § 20(a) of the 1934 Act." Compl. at ¶ 96. However, given the ambiguities of this Consolidated Complaint it is not at all clear whether Mr. Berardino is also charged with a violation of § 10b. It is equally unclear whether any other Individual Andersen Defendant is also charged with a violation of § 20(a). For this reason alone, the Consolidated Complaint should be dismissed.

[4] In the Fifth Circuit, motions to dismiss for failure to plead fraud with particularity under F.R.C.P. 9(b) are treated as 12(b)(6) motions. See Lovelace v. Software Spectrum, Inc., 78 F.3d 1015, 1017 (5th Cir. 1996) (citing Shushany v. Allwaste, Inc., 992 F.2d 517, 520 (5th Cir. 1993)).

[5] Plaintiffs' Consolidated Complaint dated April 8, 2002 will be cited herein as "Compl."

made these purchases in reliance on numerous public statements made by multiple defendants throughout the alleged class period – including, among other statements, Enron's audited annual financial statements and unaudited quarterly financial statements, press releases by Enron, public statements by Enron officers, and reports on Enron stock by securities analysts. Compl. ¶¶ 121-394, 899, 983, 986. Plaintiffs *do not* identify a single representation made to them or to the market by any Individual Andersen Defendant, much less a false statement on which they relied in purchasing Enron stock.

On November 8, 2001, Enron filed a Form 8-K with the SEC, announcing that it would restate its annual financial statements for the years 1997, 1998, 1999 and 2000, and would restate its unaudited financial statements for the first two quarters of 2001. Compl. ¶¶ 61, 518-19; see also 11/8/01 Enron Form 8-K (attached as Tab 76 to the Master SEC Appendix, dated May 8, 2002, filed in connection with Certain Defendants' Joint Brief Relating to Enron's Disclosures).[6] This announcement reflected the consolidation of three special purpose entities ("SPEs"), namely, Chewco, Jedi, and LJM; a previously reported $1.2 billion reduction in shareholders' equity; and the inclusion of certain audit adjustments and reclassifications that Andersen previously had proposed to Enron, but which had been determined to be immaterial. Compl. ¶ 61.

In the wake of Enron's announced intent to restate its financial statements, plaintiffs allege that Enron's financial statements did not conform to generally accepted accounting principles ("GAAP") and thus were "false and misleading." Compl. ¶¶ 155, 214, 300, 339, 386,

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[6] Documents cited or quoted in whole or in part in the Consolidated Complaint are properly considered on a motion to dismiss. See, e.g., Lovelace, 78 F.3d at 1017; In re Sec. Litig. BMC Software, 183 F. Supp. 2d at 883 (citing Collins v. Morgan Stanley Dean Witter, 224 F.3d 496, 498-99 (5th Cir. 2000)).

903 and 904. Plaintiffs claim that these allegedly false financial statements – together with the other alleged misstatements on which they claim to have relied – were part of a "massive fraud" perpetrated by Enron and its officers and directors, allegedly with the assistance of its lawyers, bankers, and outside auditor, Andersen. Compl. ¶¶ 61-63.

As Enron's outside auditor, Andersen allegedly audited the annual financial statements, and "reviewed interim [19]97 through [20]01 results and press releases." Compl. ¶ 897, 899. Plaintiffs allege that Andersen's audits of the annual financial statements violated generally accepted auditing standards ("GAAS"). Compl. ¶¶ 899, 905. Plaintiffs also allege that Andersen knew of or was "involved in" the accounting for several transactions whose accounting allegedly did not conform to GAAP. Compl. ¶ 905. Plaintiffs make conclusory allegations about Andersen's fees from Enron, Compl. ¶ 906 ("an incredible level of fees"), and about Andersen's partnership compensation generally, Compl. ¶ 907 ("[h]undreds of Andersen partners were each earning in excess of $1 million per year").

The allegations actually mentioning any of the Individual Andersen Defendants are – to be generous to plaintiffs – sparse, vague and conclusory. No Individual Andersen Defendant is alleged to have made a public statement on which plaintiffs relied or that affected the market price of Enron stock. Three of the Individual Andersen Defendants, Messrs. Hale, Rudloff and Sorrells, are mentioned only once in the Consolidated Complaint, in the single introductory paragraph that alleges that each was "an integral part of the Enron audit and consulting engagements." Compl. ¶¶ 93(r), (s), (t).

That same general allegation, plus one additional allegation, is made against four defendants. The one additional allegation against Mr. Willard is that he "held a meeting with his managers and staff to ensure 'compliance' with Andersen's document retention policy," Compl.

¶ 966. The one additional allegation against Messrs. Bennett, Goddard and Goolsby is that they participated in a February 5, 2001 meeting regarding Enron, where certain risks associated with the engagement were discussed. Compl. ¶ 930.

Other Individual Andersen Defendants are given barely more notice as to what each of them allegedly did so as to be charged by these plaintiffs with violating § 10(b). As to four defendants who are also alleged to have attended the above-mentioned February 5 meeting, Compl. ¶ 930, Mr. Swanson and Mr. Odom are alleged to have been made aware of allegations by an Enron employee, Sherron Watkins, raised in the late summer and early fall of 2001. Compl. ¶ 933. Mr. Lowther and Mr. Odom are alleged to have been consulted on the structuring of transactions and to have known that an Andersen auditor, Carl Bass, disagreed with some of the accounting decisions. Compl. ¶ 952(c). Mr. Jones is alleged generally and without any specificity to have also been involved in the document destruction beginning in October 2001, at the earliest. Compl. ¶ 93(g).

The allegations against those who did not participate in the February 5 meeting are just as sparse. Mr. Berardino is alleged to have been aware of Mr. Bass's concerns and to have been involved in the approval of certain off balance sheet transactions. Compl. ¶¶ 93(a), 966. Ms. Cash is also alleged to have been involved in approving certain accounting for transactions, and to have been aware of Mr. Bass's and Ms. Watkins' concerns. Compl. ¶¶ 929, 933, 950. Messrs. Neuhausen, Petersen and Stewart are alleged to have approved mark-to-market accounting and certain transaction structures and also to have known of Mr. Bass's concerns. Compl. ¶¶ 93(j), (l), (m), 929, 940, 950. Mr. Bauer is also alleged to have known of Mr. Bass's concerns, to have been involved in structuring transactions and to have been involved in document destruction. Compl. ¶¶ 929, 932, 940, 942, 950, 952(c).

The allegation against Messrs. Friedlieb and Dreyfus and Ms. Temple is that they were involved in document destruction. Compl. ¶¶ 68, 93(e)-(f), 95, 964, 966. Plaintiffs' sole allegation as to Messrs. Friedlieb and Dreyfus does not even rate a complete sentence and is set forth in its entirety in the opening clause of paragraph 966, which recites: "On 10/16/01, *after a meeting with high level partners in Chicago, including Friedlieb and Dreyfus*, Andersen's lawyer, Temple, sent an e-mail message to the Enron team suggesting changes to memoranda . . . to 'add back' Carl Bass's previously omitted criticisms to earlier memos . . ." Compl. ¶ 966 (emphasis added). Plaintiffs also attempt to implicate Mr. Berardino in connection with document destruction, alleging that he "reviewed and approved Andersen's destruction policy." ¶¶ 93(a), 966.[7]

Nowhere in their massive complaint, however, do plaintiffs allege the essential elements of a § 10(b) violation against any one, let alone each, of the Individual Andersen Defendants. See Lovelace v. Software Spectrum Inc., 78 F. 3d 1015, 1018 (5th Cir. 1996) (To establish a claim under § 10(b), "a plaintiff must prove (1) a misstatement or omission (2) of material fact (3) made with scienter (4) on which the plaintiff relied (5) that proximately caused the plaintiff's injury"). Plaintiffs have failed miserably to allege any of these essential elements with respect to any of the Individual Andersen Defendants. There is no allegation that a false statement was made by any Individual Andersen Defendant, let alone a material misstatement of fact upon

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[7] The allegations regarding illegal document destruction seem to assume, incorrectly, that plaintiffs can assert a claim against an Individual Andersen Defendant as a result of his or her alleged involvement in such destruction. However, plaintiffs cannot plead such a claim because there is no causal connection whatsoever between any document destruction and plaintiffs' claim that Enron stock was inflated as a result of alleged misrepresentations by Andersen in its audit opinions, the last of which was, according to plaintiffs, incorporated into a registration statement issued on July 25, 2001, almost three full months before any document destruction is alleged to have occurred. Compl. ¶¶ 899, 966. Moreover, plaintiffs could not allege any reliance on the actions taken in connection with the alleged document destruction. See Nathenson v. Zonager, Inc., 267 F.3d 400, 413 (5th Cir. 2001) ("Reliance . . . generally requires that the plaintiff have known of the particular misrepresentation complained of have believed it to be true and because of that knowledge and belief purchased or sold the security in question.")

which the proposed plaintiffs' class reasonably relied and that caused damage to plaintiffs. Plaintiffs, having chosen to sue each individual under § 10(b), must meet their pleading obligation with respect to each individual. Plaintiffs have not done this and cannot do this. See In re Sec. Litig. BMC Software, 183 F. Supp. 2d at 886 (explaining that to support a § 10b claim a plaintiff's allegations must be specific as to each defendant). To the extent that plaintiffs' theory is that the Individual Andersen Defendants can be held secondarily liable for the misstatements of others, any such claim is barred by Central Bank v. First Interstate Bank, 511 U.S. 164 (1994).

Even if plaintiffs had alleged that any of Individual Andersen Defendants made a misstatement of material fact, at no point does the Consolidated Complaint set forth with the required particularity any allegations that would show that any one of these individuals knew that the statement was false at the time it was made, what precise information was known by them, when it was known, how it was learned, or even how plaintiffs know what the Individual Andersen Defendant allegedly knew. See In re Sec. Litig. BMC Software, 183 F.Supp. 2d at 886 ("Plaintiffs must allege what actions each defendant took in furtherance of the alleged scheme and specifically plead what he learned, when he learned it, and how Plaintiffs know what he learned.") (citing McNamara v. Bre-X Minerals, Ltd., 57 F. Supp. 2d 396, 423 (E.D. Tex. 1999)). Plaintiffs' pleading against the Individual Andersen Defendants is improperly based entirely upon conclusory assertions, irrelevancies, speculation, and innuendo. The Consolidated Complaint must therefore be dismissed.

## ARGUMENT

### I. PLAINTIFFS HAVE FAILED TO PLEAD A CLAIM UNDER SECTION 10(b) OR RULE 10(b)-5 AGAINST ANY OF THE INDIVIDUAL ANDERSEN DEFENDANTS

#### A. Plaintiffs Have Failed to Plead that Any of the Individual Andersen Defendants Made a Material Misstatement or Omission, or Any Other Element of Section 10(b)

In order to state a claim under § 10(b), a plaintiff must allege as a threshold matter that the defendant, acting with scienter, made a misstatement or omission of a material fact. See, e.g., Lovelace, 78 F.3d at 1018 (citing Cyrak v. Lemon, 919 F.2d 320, 325 (5th Cir. 1990)). The Consolidated Complaint does not contain in its more than 500 pages a single allegation that any one of the Individual Andersen Defendants made a material misstatement or omission.

As a result, plaintiffs have not alleged an essential element of a § 10(b) claim as to any of the Individual Andersen Defendants. See Lovelace, 78 F.3d at 1018; Wright v. Ernst & Young LLP, 152 F.3d 169, 175-76 (2d Cir. 1998) (applying Central Bank, and holding that absent an allegation that the defendant has made an actual misrepresentation, even "substantial involvement" in the preparation of a statement is insufficient as a matter of law to state a claim under the securities laws); see also Vosgerichian v. Commodore Int'l, 862 F. Supp. 1371, 1378 (E.D. Pa. 1994) (applying Central Bank to dismiss a § 10(b) claim against an accounting firm because the plaintiff alleged that the firm helped structure a fraudulent transaction but failed to allege that the firm made any material misstatement apart from mere involvement in that transaction). Accordingly, plaintiffs' § 10(b) claims as to each of the Individual Andersen Defendants should be dismissed.

Moreover, plaintiffs cannot circumvent the material misstatement element of § 10(b) by

asserting in some conclusory manner that any one of the Individual Andersen Defendants participated in a scheme to defraud. See, e.g., Compl. at ¶ 907. "Scheme" allegations have been rejected as inconsistent with Central Bank's prohibition of "conspiracy" pleading. See, e.g., Shapiro v. Cantor, 123 F. 3d 717, 720 (2d Cir. 1997) (affirming motion to dismiss where plaintiff did not allege misstatement by defendant on the ground that "allegations of 'assisting,' 'participating in,' 'complicity in' and similar synonyms, all fall within the prohibitive bar of Central Bank"); In re HI/FN, Inc. Sec. Litig., No. C-99-4531, 2000 U.S. Dist., LEXIS 11631, *35 (N.D. Cal. Aug. 9, 2000) (noting that scheme allegations are insufficient to support a § 10b claim because "each defendant must meet all the requirements for primary liability under Rule 10b-5" and there is no cause of action for aiding and abetting.). Accordingly, "allegations of a scheme to defraud by individual defendants who are not alleged to have made statements do not support a claim for violation of § 10(b)." In re HI/FN, 2000 U.S. Dist. LEXIS 11631, at *35.

Because Plaintiffs have failed to allege that any of the Individual Andersen Defendants made a misstatement or omission, an essential element of a claim pursuant to § 10(b), or that any such statement was made with scienter, or that any Plaintiff reasonably relied and was damaged thereby, Plaintiffs' claims against each of the Individual Andersen Defendants should be dismissed.

### B. Plaintiffs Have Failed to Plead Particularized Facts Which, If Proven, Would Give Rise to a Strong Inference that Any of the Individual Andersen Defendants Possessed Scienter

#### 1. The PSLRA and Federal Rule of Civil Procedure 9(b) Impose Stringent Particularity Requirements for Pleading Federal Securities Fraud

Plaintiffs' claims also fail for an independent reason: their Consolidated Complaint does

not satisfy the standards of pleading scienter under the PSLRA and F.R.C.P. 9(b), which impose strict pleading requirements on plaintiffs asserting federal securities fraud claims. "To satisfy Rule 9(b) and the PSLRA, a Plaintiff must plead facts and avoid reliance on conclusory allegations." Schiller v. Physicians Res. Group, Inc., No. 3:97-CV-3158-L, 2002 WL 318441 at *4 (N.D. Tex. Feb. 26, 2002). Under F.R.C.P. 9(b), "[c]ourts have uniformly held inadequate a complaint's general averment of the defendant's knowledge of material falsity unless the complaint also sets forth specific facts that make it reasonable to believe that defendant knew that a statement was false or misleading." Coates v. Heartland Wireless Communications, Inc., 55 F. Supp. 2d 628, 634 (N.D. Tex. 1999) (internal quotations and citations omitted); see also Lovelace, 78 F.3d at 1018 ("In order to adequately plead scienter [under F.R.C.P. 9(b)], a plaintiff must set forth specific facts to support an inference of fraud.").

The PSLRA heightens the F.R.C.P. 9(b) standard. See Schiller, 2002 WL 318441, at *4; In re Sec. Litig. BMC Software, 183 F. Supp. at 866 n.15. In particular, the PSLRA states that "the complaint shall specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed." 15 U.S.C. § 78u-4(b)(1)(B).

In order to satisfy the pleading requirements of the PSLRA and F.R.C.P. 9(b), the complaint must adequately demonstrate that *each* defendant possessed the requisite state of mind or scienter. The PSLRA expressly requires that "the complaint shall, with respect to *each* act or omission alleged to violate this chapter, state with particularity *facts* giving rise to a *strong inference* that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2) (emphasis added); see also Nathenson v. Zonagen Inc., 267 F.3d 400, 407 (5th Cir. 2001); Hart

v. Bayer Corp., 199 F.3d 239, 239 (5th Cir. 2000); Williams v. WMX Techs., Inc., 112 F.3d 175, 177-78 (5th Cir. 1997).

Prior to the PSLRA, a plaintiff merely had to plead facts that "support an inference of fraud"; to meet the heightened requirement of pleading a "strong inference" of scienter, a plaintiff must now allege facts demonstrating intentional misconduct or severe recklessness. See Nathenson, 267 F.3d at 407. Allegations of a defendant's motive and opportunity to commit fraud will not suffice to plead scienter under the PSLRA, see id. at 410-12, and "plaintiffs may not rely on fraud by hindsight to establish a claim for securities fraud . . . or seize upon disclosures in later reports and allege they should have been made in earlier ones." Schiller, 2002 WL 318441, at *10 (internal quotations and citations omitted). Nor can a plaintiff plead scienter by merely alleging participation in a fraud based on the defendants' executive positions, access to internal corporate documents, day-to-day responsibilities, attendance at management and board meetings and/or the location of their office. See In re Sec. Litig. BMC Software, 183 F. Supp. 2d at 885 (finding such allegations inadequate to support scienter). Rather, plaintiffs "must allege what actions *each* defendant took in furtherance of the alleged scheme and specifically plead what he learned, when he learned it, and how plaintiffs know what he learned." Id. at 886 (emphasis added).

Plaintiffs may not avoid this obligation to plead particularized facts relating to *each* of the Individual Andersen Defendants by vague references in the Consolidated Complaint to "Andersen," even if coupled with allegations of that individual's status within the partnership. As this Court has stated, "[b]ecause . . . a more stringent pleading is required by the PSLRA, [this Court] agrees with those district courts that find the group pleading doctrine is at odds with the PSLRA and has not survived the Amendments." Id. at 901 n.45 (S.D. Tex. 2001); see also

Marra v. Tel-Save Holdings, Inc., Master File No. 98-3145, 1999 U.S. Dist. LEXIS 7303, *14 (E.D. Pa. May 18, 1999) (citing Coates, 26 F. Supp. 2d at 916). The group pleading doctrine "permit[ted] an inference of wrongdoing not based on defendant's conduct, but solely on defendant's status as an officer or director of a corporation." Allison v. Brooktree Corp., 999 F. Supp. 1342, 1350 (S.D. Cal. 1998). The PSLRA, in contrast, "requires plaintiffs to distinguish among those they sue and enlighten each defendant as to his or her particular part in the alleged fraud." Schiller, 2002 WL 318441, at *5 (internal quotations and citation omitted).

Moreover, the failure of an auditing firm to discover fraud by its client does not imply that any of the individual auditors committed fraud, or even violated GAAS. As recognized under GAAS:

> "Because of the characteristics of fraud, particularly those involving concealment and falsified documentation . . ., a properly planned and performed audit may not detect a material misstatement. . . . [A]uditing procedures may be ineffective for detecting an intentional misstatement that is concealed through collusion among client personnel and third parties or among management and employees of the client."

AU § 230.12 (attached as Exhibit C to Declaration of Andrew Ramzel in Support of Defendant Arthur Andersen LLP and the Individual Andersen Defendants' Motions to Dismiss, "Ramzel Decl.").

2. Plaintiffs Have Not Adequately Alleged that Any One of the Individual Andersen Defendants Is Liable as a Principal Under Section 10(b) or Rule 10b-5

a. Plaintiffs' Generalized and Conclusory Allegations Regarding Each Individual Andersen Defendant's Role With Respect to the Enron Engagement Do Not Give Rise to a Strong Inference of Scienter

With respect to Messrs. Hale, Rudloff and Sorrels, the Consolidated Complaint states merely that each was "an integral part of the Enron auditing and consulting engagements." Compl. at ¶¶ 93(r)-(t). There is not a single additional reference as to what any of these individuals knew or what they did linking them to Enron audits or any particular transaction. These bare allegations clearly fail to satisfy the pleading requirements of F.R.C.P. 9(b) and can not support any, let alone a strong, inference of scienter. See 15 U.S.C. § 78u-4(b)(2); Lovelace, 78 F.3d at 1019; Nathenson, 267 F.3d at 407.

Plaintiffs use similarly vague and conclusory allegations – including the boilerplate allegation that most of the Individual Andersen Defendants were "an integral part of the Enron auditing and consulting engagements" – to describe the roles of the other Individual Andersen Defendants with respect to the Enron engagement. Compl. ¶ 93(a)-(t). Plaintiffs provide no more specificity than this to describe what role, if any, the individual Andersen Defendants played in connection with the issuance of the alleged misstatements;[8] they do not even specifically allege the time periods during which any of these individuals were supposedly in a

[8] Messrs. Jones, Dreyfus and Friedlieb and Ms. Temple are not even alleged to have had any nexus whatsoever to the performance of the Enron audits, and their roles are described in an equally conclusory matter by plaintiffs as "an integral part of the destruction of Andersen's documents relating to Enron." Compl. ¶¶ 93(e)-(f), 95, 966. As to Mr. Jones, the allegation is that he "caused Enron-related documents to be destroyed in Andersen's London office," and that he participated in the February 5, 2001 meeting regarding Enron. Compl. ¶¶ 93(a), 930.

position within Andersen to work on the Enron audits at issue. As this Court has held, Plaintiffs cannot plead scienter merely through allegations about the defendant's executive positions, day-to-day responsibilities, and/or the location of their office. See In re Sec. Litig. BMC Software, 183 F. Supp. 2d at 885.

b. Plaintiffs' Allegations that an Andersen Accountant Disagreed with Aspects of Enron's Accounting Do Not Give Rise to a Strong Inference that Any of the Individual Andersen Defendants Possessed Scienter (Allegations Referencing Bauer, Berardino, Cash, Lowther, Neuhausen, Odom, Petersen, Stewart)

Plaintiffs try to suggest scienter by alleging that some of the Individual Andersen Defendants were aware that Andersen partner Carl Bass disagreed with certain aspects of Enron's accounting. Compl. ¶¶ 93(a), (j)-(l), 928-29, 932, 950, 952(c). But any suggestion that this disagreement over accounting treatment of transactions in and of itself demonstrates fraud reflects a misunderstanding of both GAAS and GAAP.

GAAP is not an inflexible set of calculations yielding only one possible accounting treatment for any particular transaction. Rather, "GAAP is a term of art that encompasses a wide range of acceptable procedures." In re IKON Office Solutions, Inc., 277 F.3d 658, 675 n.22 (3d Cir. 2002). As the Supreme Court has explained:

> "Accountants long have recognized that 'generally accepted accounting principles' are far from being a canonical set of rules that will ensure identical accounting treatment of identical transactions. 'Generally accepted accounting principles,' rather, tolerate a range of 'reasonable' treatments, leaving the choice among alternatives to management."

Thor Power Tool Co. v. Commissioner, 439 U.S. 522, 544 (1979) (internal footnote omitted); see also In re Glenfed, Inc. Sec. Litig., 42 F.3d 1541, 1549 (9th Cir.1994) (en banc) (as

accounting concepts are flexible, circumstances will give rise to fraud only where differences in calculations are the result of a falsehood, "not merely the difference between two permissible judgments"); Godchaux v. Conveying Techniques, Inc., 846 F.2d 306, 315 (5th Cir. 1988) (citing Thor and noting that "generally accepted accounting principles are flexible"). As a result,

> "[A] difference in judgment about generally accepted accounting principles does not establish conscious behavior on the part of Defendants. The term generally accepted accounting principles, as we have often noted, is a term of art encompassing a wide range of acceptable procedures, such that an ethical, reasonably diligent accountant may choose to apply any of a variety of acceptable accounting procedures when that accountant prepares a financial statement."

Lovelace, 78 F.3d at 1021 (internal quotations and citation omitted). In this context, far from raising an inference of scienter for securities fraud purposes, debate among auditors and accountants concerning the application of GAAP to particular transactions is a natural and entirely appropriate part of the auditing process. If an auditor could be sued for fraud based on allegations that they were "aware" of disagreement, then diligence would become a basis for liability, and auditors would have a huge incentive not to consult others on accounting issues, and thus to avoid awareness of divergent views.[9]

In any event, plaintiffs' conclusory allegations of awareness of different views are insufficient to satisfy the PSLRA's requirement that they plead facts that, if proved, would give rise to a strong inference of scienter.

c. Plaintiffs' Allegations Regarding the Structuring of the LJM2 and the Raptor Transactions and Enron's Mark-to-Market Accounting Do Not Give Rise to a Strong Inference that Any of the Individual

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[9] Moreover, proper perspective on GAAP shows that debate among accountants about the proper application of GAAP to particular transactions is a sign of diligence, not of fraud. Under GAAS, an auditor is required to be skeptical. See AU § 230.07 ("Due professional care requires the auditor to exercise *professional skepticism*.") (emphasis in original) (attached as Ex. C to Declaration of Andrew Ramzel ("Ramzel Decl.")

Andersen Defendants Possessed Scienter
(Allegations Referencing Berardino, Cash, Lowther, Neuhausen, Odom, Petersen, Stewart)

Although plaintiffs identify dozens of allegedly fraudulent transactions, they make only two allegations that reference any of the Individual Andersen Defendants in connection with specific transactions:

> "Defendants David Duncan, Cash, Stewart and Neuhausen and others were heavily involved in the structuring of the entity, the decisions to allow Enron to improperly account for the LJM2 entity, and were aware of Bass's disagreement with the LJM2 accounting beginning in [20]00." Compl. ¶ 950.
>
> "Andersen also made the decision to allow Enron to improperly avoid recording individual impairment charges for Raptor investments that had significantly and permanently declined in value. Andersen e-mails between Cash, David Duncan and Stewart throughout the Class Period reveal that defendants David Duncan, Cash, Lowther, Odom, Stewart and others were deeply involved in this accounting decision, and were aware that Bass thought the Raptor accounting was improper." Compl. ¶ 952(c).

Plaintiffs make no allegation to suggest that the difference in view between Bass and others was anything other than that – a difference in view under GAAP. See Point I.b.2, supra. Moreover, plaintiffs make no attempt to differentiate the roles of each of the Individual Andersen Defendants in the transactions. Instead, they rely on conclusory allegations that groups of individuals were "heavily involved" or "deeply involved" in a transaction. This pleading falls far short of the requirements that a "complaint shall, with respect to *each* act or omission alleged to violate this chapter, state with particularity *facts* giving rise to a *strong inference* that the defendant acted with the required state of mind," 15 U.S.C. § 78u-4(b)(2) (emphasis added), and that a complaint "must allege what actions *each* defendant took in

furtherance of the alleged scheme and specifically plead what he learned, when he learned it, and how plaintiffs know what he learned." In re Sec. Litig. BMC Software, 183 F. Supp. at 886 (emphasis added); Nathenson, 267 F.3d at 407.

Plaintiffs have simply not met their pleading burden, notwithstanding their statement that they have relied on e-mail messages for their conclusory allegation of "dee[p]" involvement. Compl. ¶¶ 928-29.[10] They have not alleged what knowledge any of these individuals had that would have led them to conclude the accounting was improper. The allegation that Carl Bass occasionally reached a different judgment does not mean that other individuals at Andersen were engaged in fraud. The fact that the accounting has been challenged or changed and that judgments may turn out not to have been correct at the time made, likewise is not sufficient to allege fraud. See In re IKON Office Solutions, 277 F.3d at 673; Melder v. Morris, 27 F.3d 1097, 1101 n.8 (5th Cir. 1994) ("These allegations boil down to plaintiffs' attempt to chastise as fraud business practices that, in hindsight, might have been more cautious. Misjudgments are not, however, fraud").

Plaintiffs' allegation that "PSG partners Stewart, Petersen and Neuhausen continued to approve Enron's use of mark-to-market accounting as Enron became more egregious in revenue recognition," Compl. ¶ 940, does not give rise to any inference of scienter whatsoever.[11] Plaintiffs nowhere allege that the use of mark-to-market accounting is inherently fraudulent; nor could they, as GAAP required the use of mark to market accounting for certain transactions. See EITF 98-10: Accounting for Contracts Involved in Energy Trading and Risk Management

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[10] In addition, as discussed above, there is no liability under § 10(b) or Rule 10(b)-5 for alleged mere "involvement" in the fraud of others. See Shapiro, 123 F.3d at 720 (relying on Central Bank).

[11] Moreover, as discussed above, there is no liability under § 10(b) or Rule 10(b)-5 for mere "approval" of an allegedly fraudulent statement of another. See Shapiro, 123 F.3d at 720.

Activities, Nov. 18-19, 1998 (energy trading contracts should be marked to market) (attached as Tab 57 to the Master Appendix, dated May 8, 2002, filed in connection with certain Defendants' Joint Brief Relating to Enron Disclosures). Moreover, Plaintiffs fail to specify the transactions for which Stewart, Petersen, and Neuhausen – individually – allegedly "approved" mark-to-market accounting, what those individuals allegedly knew that should have resulted in their concluding that such accounting was fraudulent and when they allegedly knew it.

Finally, plaintiffs' utterly bare allegation that Mr. Berardino "regularly reviewed and approved Enron's off balance sheet transactions," Compl. ¶ 93(a), is baseless. The Consolidated Complaint does not state where, how, or when Mr. Berardino conducted these activities. Indeed, plaintiffs do not - and cannot - point to any legitimate basis for suggesting that Mr. Berardino had or exercised any supervisory responsibility, or had any direct role with respect to Enron's off balance sheet transactions.

d. Plaintiffs' Allegations Regarding the February 5, 2001 Risk Assessment Meeting Do Not Give Rise to a Strong Inference that Any of the Individual Andersen Defendants Possessed Scienter (Allegation Referencing Bauer, Bennett, Goddard, Goolsby, Odom, Lowther, Stewart, Swanson)

Plaintiffs employ "group pleading" to allege that eight of the Individual Andersen Defendants participated in a meeting on February 5, 2001 during which business risks attendant to the Enron engagement were discussed. Plaintiffs fail to specify the role of any of the individuals at the meeting, instead alleging merely that "significant discussion ensued" about certain accounting issues. Compl. ¶ 930.

These allegations improperly attempt to twist Andersen's diligence in evaluating the risk

of retaining Enron as a client into an indication of fraud. Risk assessment is part of an annual consideration regarding whether the firm should retain a client. Accordingly, in February 2001, a group of Andersen executives conducted a review and assessment of Andersen's relationship with Enron. Compl. ¶ 930. But at the meeting, as plaintiffs allege, the participants discussed several complex accounting issues relating to the Enron engagement and identified potential risks, Compl. ¶ 930, but ultimately concluded in favor of retaining Enron as a client because they believed Andersen "had the appropriate people and processes in place to serve Enron and manage our engagement risks." Compl. ¶ 912.

The conclusion reached by the individuals participating in the February 5 meeting, *i.e.* that Andersen was appropriately managing the audit risk – whether right or wrong in hindsight – negates any inference of severe recklessness at the time by any of the Individual Andersen Defendants who participated in the conference call. See, e.g., In re IKON Office Solutions, 277 F.3d at 670 ("the relevant inquiry is bad faith not judgment.").

e. Plaintiffs' Allegations Regarding Sherron Watkins' Concerns About Enron's Accounting Fail to Plead Facts that, if True, Would Give Rise to a Strong Inference that Any of the Individual Andersen Defendant Possessed Scienter (Allegations Referencing Cash, Odom, Swanson)

Plaintiffs allege that in August 2001, Andersen alumna and Enron Vice President Sherron Watkins raised concerns about the "very issues that caused Enron's collapse" – first with a former colleague at Andersen, James Hecker, and then with Enron's Chairman. Compl. ¶¶ 933-34. According to the August 21, 2001 memorandum that plaintiffs selectively quote in the Consolidated Complaint, Mr. Hecker wrote the following:

> "I encouraged [Ms. Watkins] to discuss these issues with anyone in the company who could satisfy her about the accounting and disclosures related to these transactions. I told her that I admired her 'stand-up' attitude and that corporate introspection about these sorts of accounting and reporting issues often was very healthy and should not be suppressed."

See Memorandum by James Hecker, dated August 21, 2001, at 4 (attached as Ex. A to Ramzel Decl.). Thus, plaintiffs' allegation that Ms. Watkins' concerns were "ignored" by Andersen is contradicted by the very memorandum on which they rely. By plaintiffs' own allegation, Mr. Hecker immediately relayed Ms. Watkins' concerns to partners on the Enron engagement team, Compl. ¶ 933 ("On 8/21, Hecker called an emergency meeting with other Andersen Partners . . . to discuss Watkins' questions and concerns"), and within three months Enron announced that it would restate its financial statements to address many of the concerns that Ms. Watkins had raised, Compl. ¶ 63 (referring to the "11/01 restatements").

In any event, the knowledge by some of the Individual Andersen Defendants of Ms. Watkins' concerns cannot form the basis for a fraud by these individuals because plaintiffs do not allege that any of the Individual Andersen Defendants issued any public statements about Enron's finances *after* becoming aware of these concerns.[12] Additionally, plaintiffs never allege that Ms. Watkins' August 2001 communication demonstrates scienter as to any Individual Andersen Defendant during the period 1997 through 2000 when the allegedly false statements were made. See In re IKON Office Solutions, 277 F.3d at 670 (evidence that auditor "deliberately disregarded" concerns about accounting raised in 1998 had no bearing on auditor's "preparation of its audit opinion in 1997, the only time-period where [the auditor's] state of mind

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[12] Andersen issued its last audit report on Enron's financial statements on February 23, 2001. Compl. ¶ 903. Plaintiffs allege this audit report was subsequently incorporated into several registration statements, the latest of which was dated July 25, 2001. Compl. ¶ 899. Thus, the last statement allegedly attributable to Andersen was made well *before* any of the Individual Andersen Defendants learned of Mrs. Watkins' allegations.

is relevant to the section 10(b) claim"); Schiller 2002 WL 318441, at *14 (although there were indications that defendants "were aware of a number of accounting inaccuracies," there was no indication that defendants "knew or recklessly disregarded . . . accounting errors at the [earlier] time these 'errors' were made").

f. Plaintiffs' Allegations Regarding Mr. Willard's Meeting Fail to Plead Facts That, if True, Would Give Rise to a Strong Inference That Any Individual Andersen Defendant Possessed Scienter

The only allegation plaintiffs make concerning Mr. Willard (apart from identifying his home address and role generally as an accountant at Andersen) is a single sentence buried in a lengthy paragraph that in late October 2001 he "held a meeting with his managers and staff to ensure 'compliance' with Andersen's document retention policy." Compl. ¶ 966. On its face, this isolated allegation does not allege facts giving rise to a strong inference of scienter, nor, for that matter, of any conduct by Mr. Willard that constitutes, or that reasonably could be interpreted to constitute, securities fraud. It is a transparent attempt to mask with innuendo the total absence of any substantive allegations regarding Mr. Willard that amount to securities fraud. Such pleading must fail under the PSLRA, F.R.C.P. 9(b), or any other pleading standard.

Moreover, there is no allegation that any plaintiff knew of this late October 2001 meeting, relied on it, or was damaged thereby in connection with their purchase of Enron stock. See Nathenson v. Zonagen, Inc., 267 F.3d 400, 413 (5th Cir. 2001) ("Reliance . . . generally requires that the plaintiff have known of the particular misrepresentation complained of, have believed it to be true and *because of that knowledge and belief* purchased or sold the security in question.") (emphasis added).

g. Plaintiffs' Allegations Regarding Document Destruction Fail to Plead Facts that, if True, Would Give Rise to a Strong Inference that Any Individual Andersen Defendant Possessed Scienter (Allegations Referencing Berardino, Dreyfus, Jones, Friedlieb, Odom Temple)

Finally, plaintiffs allege that Andersen destroyed documents "that could implicate them on the Enron Fraud." Compl. ¶ 962. The allegations as to Messrs. Dreyfus and Friedlieb are particularly vague. Plaintiffs allege that following a meeting at which these Individual Andersen Defendants were present, Ms. Temple took certain action to be sure certain material was added to a memorandum. Compl. ¶ 966. There is no specific allegation as to what Messrs. Dreyfus or Friedlieb said, or did, or knew in connection with this meeting or that the meeting bore any relationship, beyond the mere temporal, with any events occurring thereafter. This allegation simply does not constitute a violation of anything – let alone § 10(b).

Moreover, the allegations of alleged document destruction cannot constitute the basis for any claim of § 10(b) liability against any Individual Andersen Defendant. The alleged events with respect to document destruction occurred in late October and early November 2001 – long after the last alleged misrepresentation on July 25, 2001. No Plaintiff could have known of these events, relied on them, or been damaged thereby in connection with their purchase of Enron stock. See Nathanson, 267 F.3d at 413 (holding that for a viable securities fraud claim in the Fifth Circuit the plaintiff must have known of the misrepresentation and actually relied upon it to his detriment).

Ms. Temple, for example, is to have sent an e-mail message in October 2001 - long after the last alleged misrepresentation on July 25, 2001 - in which she allegedly urged others to

destroy documents. Compl. ¶ 966. This allegation simply cannot suffice to meet plaintiffs' burden of establishing causation or reliance for a § 10b violation. See id.

Finally, the allegations as to Messrs. Berardino, Odom and Bauer are not sufficiently specific to allege scienter. With respect to Mr. Berardino, plaintiffs allege that he "reviewed and approved Andersen's document destruction policy." Compl. ¶ 93(a). However, they do not articulate how such high-level involvement in the development of a general retention policy, even if true, relates to the underlying fraud alleged - that is, the misrepresentations contained in Enron's audits. As to Mr. Bauer, plaintiffs, relying on his deposition, allege that he admitted destroying documents. Compl. ¶ 966. However, Mr. Bauer's testimony states that he routinely followed the document retention policy and that he did not suspend his routine until told to do so by counsel on November 9, 2001. Moreover, Mr. Bauer made clear that the discarded documents did not relate to any of the issues in the Consolidated Complaint (including, for example, the Chewco or LJM transactions), and were additionally only early drafts of work product for which final versions had been retained. See Transcript of Deposition of Thomas Bauer, Feb. 19, 2002, at 45-48 (attached as Ex. B to Ramzel Decl.). In other words, the testimony upon which plaintiffs attempt to rely undermines any inference of scienter. Nowhere in the Consolidated Complaint do Plaintiffs allege that Mr. Bauer destroyed documents that contained information that he believed would show he had engaged in a fraud. Similarly, with respect to Mr. Odom, although he is alleged to have told others to follow Andersen's policy, Compl. ¶¶ 965-966, there are no allegations that he ever believed this was improper.

h. Plaintiffs' Allegations Regarding Compensation Do Not Give Rise to a Strong Inference that Any Individual Andersen Defendant Possessed Scienter

Plaintiffs allege generally that "fees were particularly important to Andersen's partners as their incomes were dependent on the continued business from Enron." Compl. at ¶ 906. Plaintiffs also describe, in generalized allegations that do not plead facts specific to any of the Individual Andersen Defendants or the Enron engagement, the alleged incentives for Andersen partners to sell consulting services to "his or her assigned clients." Id. ¶ 907.

Such vague allegations simply can not give rise to a "strong inference" that any of the Individual Andersen Defendants acted with the required scienter. First, the allegations do not mention any of the Individual Andersen Defendants, much less indicate how much in incentive compensation they received or whether the incentives were material to them. Plaintiffs allege that an Andersen partner's compensation was "based primarily upon the level of the fees that each partner 'controlled' or sold to his or her assigned clients," Compl. ¶ 907, but they fail to specify which Andersen partner or partners "controlled" the Enron fees. Under these circumstances, there is no indication that the compensation of any of the Individual Andersen Defendants depended on the level of Enron fees, or that any of the Individual Andersen Defendants received material amounts of incentive compensation (or even ever tried personally to market consulting services to Enron).

Second, the mere fact that Andersen had in place an incentive program designed to encourage its partners to sell audit and consulting work to clients is simply not a basis for concluding there is a "strong inference" of fraud. If scienter could be pleaded on that basis alone, virtually every professional service provider would be forced to defend securities fraud

actions on that basis alone. See BMC Software, 183 F. Supp. 2d at 896 (holding that motives possessed by nearly all corporate insiders, including the desire "to insure a high stock price to increase executive compensation, or to prolong the benefits of being a corporate officer, "were not sufficient to allege scienter"); see also Melder v. Morris, 27 F.3d 1097, 1102 (5th Cir. 1994) (allegation "defendant officers and directors were motivated by incentive compensation" was insufficient [to give rise to strong inference of scienter]); Acito v. IMCERA Group, Inc., 47 F.3d 47, 53 (2d Cir. 1995) (allegations that "defendant officers [of a company] were motivated to inflate the value of [that company's] stock because the increase in stock price [would have] a direct effect on their executive compensation" was insufficient to give rise to a strong inference of scienter). Thus, plaintiffs allegations regarding compensation do not meet the pleading requirements of the PSLRA.

## II. JOSEPH F. BERARDINO IS NOT LIABLE UNDER § 20(A) OF THE EXCHANGE ACT

Plaintiffs also seek to attach "control person" liability to Mr. Berardino pursuant to § 20(a) of the Exchange Act, Compl. ¶96, which provides, in relevant part:

> "Every person who, directly or indirectly, controls any person liable under any provision of this title or any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable."

See 15 U.S.C. § 78t(a).

For the reasons that follow, plaintiffs have failed to plead sufficient facts to make a prima facie showing that Mr. Berardino is liable as a "control person."

A. Mr. Berardino Cannot Be Liable Under § 20(a) Because There Is No Underlying Fraud by Andersen, the Allegedly Controlled Person

The threshold test for imputing derivative liability to an individual under § 20(a) is whether there was a primary violation of the federal securities laws. See In re Azurix Corp. Sec. Litig., No. H-00-4034, 2002 WL 562819, at *26 (S.D. Tex. Mar. 21, 2002) (Lake, J.) (dismissing claim under § 20(a) on the ground that plaintiffs did not adequately plead underlying allegations pursuant to § 10(b)); In re Sec. Litig. BMC Software,183 F. Supp. 2d 860, 888 (S.D. Tex. 2001) (Harmon, J.) (same).

The underlying fraud alleged by plaintiffs in this case against Andersen revolves around the audit reports it prepared in connection with Enron's financial statements, for fiscal years 1997 through 2000, and Andersen's consent for Enron to include those reports in registration statements. Compl. ¶ 899. As set forth in Andersen's motion to dismiss, plaintiffs do not plead factual allegations against Andersen with sufficient particularity to support a § 10(b) violation and therefore the claims against Andersen should be dismissed.

In the event that this Court grants Andersen's Motion to Dismiss, it will be required as a matter of law also to dismiss all § 20(a) claims against Berardino, and any other Individual Andersen Defendants charged thereunder because there can be no § 20(a) liability where there has been no predicate securities act violation. See RGB Eye Assoc. v. Physician Res. Group, Inc., No. 3:98-CV-1715-D, 1999 LEXIS 21940, at * 39-40 (N.D. Tex. May 13, 1999) (citing SEC v. First Jersey Secs., Inc., 101 F.3d 1450, 1472 (2d Cir. 1996) ("To plead [a § 20(a)] claim, plaintiffs must allege: (1) an *underlying primary violation* by the controlled person; (2) *each* defendant's control over the primary violator; and (3) *particularized facts as to each* controlling person's culpable participation in the fraud perpetrated by the controlled person") (emphasis

added); accord In re Advanta Corp. Sec. Litig., 180 F.3d 525, 541 (3d Cir. 1999); Halkin v. VeriFone Inc. (In re VeriFone Sec. Litig.), 11 F.3d 865, 872 (9th Cir. 1993).[13]

B. Plaintiffs Do Not Adequately Allege That Mr. Berardino Had the Requisite Control for Liability Under § 20(a)

To establish that a defendant is a control person under § 20(a), a plaintiff must allege that the defendant "had the requisite power to directly or indirectly control or influence corporate policy." Abbot v. Equity Group, Inc., 2 F.3d 613, 619-20 (5th Cir. 1993); Brown v. Mendel, 864 F.Supp. 1138, 1144 (M.D. Ala. 1994)(discussing Abbot), aff'd sub nom., Brown v. Enstar Group, 84 F.3d 393 (11th Cir. 1996). "Control" includes not only general control over the entity that is primarily liable, but also control over the specific corporate policy which resulted in the underlying claim. See, e.g., McNamara v. Bre-X Minerals Ltd., 46 F. Supp. 2d 628, 638 (E.D. Tex 1999) ("the Court will find control person liability if the Plaintiffs make a prima facie showing that the Defendant in question had the power . . . to control the transactions in question and to control the operations of [the company] in general"); accord Brown v. Mendel 864 F. Supp. 1138, 1144 (M.D. Ala. 1994)(adopting Fifth Circuit standard, and requiring a showing of general control over entity and specific control over corporate policy).

The extent of Plaintiffs' factual allegations regarding potential § 20(a) liability are that Mr. Berardino "was the Chief Executive Officer and managing partner of Andersen-Worldwide until his resignation on 3/26/02," that he was Chief Executive Officer and Managing Partner of Andersen, that he "was involved in Andersen's firm-wide policy and procedures." Compl.

[13] The Consolidated Complaint is similarly unclear concerning whether plaintiffs seek to allege Mr. Berardino's control person liability with respect to any other Individual Andersen Defendant. If this is the plaintiffs' intent, it has again been inappropriately left for defendants' speculation. However, for the reasons set forth above, there are no allegations sufficient to assert a claim under § 10(b) with respect to any Individual Andersen Defendant, and none of those allegations can form a predicate for any § 20(a) violation.

¶¶ 93(a), 979 (emphasis added). These broad allegations are insufficient to allege control person liability as they do not demonstrate that Mr. Berardino had the requisite power to control Andersen generally. They do not state when Mr. Berardino occupied these positions, whether he played a leadership role in any substantive business decisions of the audit practice, or whether he participated in the general operation of the Houston office. These are critical gaps.

Additionally, plaintiffs fail to adequately allege that Mr. Berardino had the authority to control the "transactions in question." Plaintiffs do not allege that Mr. Berardino had any ability to control the audits or the issuance of the allegedly fraudulent audit reports. Plaintiffs do not even allege that Mr. Berardino had a role in the day-to-day operations of Andersen's audit practice, a critical omission given that Andersen had various business units which placed competing demands on his time.

Plaintiffs allegations that Mr. Berardino was CEO and Managing Partner of Andersen, see Compl. ¶ 979, "had regular contact" with senior partners on the Enron engagement and "kept apprised of Enron – the firm's second largest client – on a regular basis" fall far short of demonstrating control of the Enron audits. See Paracor Fin. v. GE Capital Corp., 96 F.3d 1151 (9th Cir. 1996); see also Cameron v. Outdoor Resorts of Am., Inc., 608 F.2d 187, 195 (5th Cir. 1979) (upholding district court's finding that a director was not liable under § 20(a), despite having general control over the business entity alleged to have made a misstatement, because the director did not have day-to-day control and because there was no clear evidence that the director acted in bad faith). In Paracor, the Ninth Circuit held that a CEO was not a controlling person despite evidence that the individual had founded the company, and "was consulted on every major decision" made by the company. Id. at 1163. In particular, the Ninth Circuit reasoned that the CEO was not a controlling person because "(1) he was not involved in the

corporation's day-to-day business, and (2) he had nothing to do with the preparation of the prospectuses at issue." Id. at 1163-64. The allegations against Mr. Berardino call for this same result.

The foregoing applies with even greater force to all of the other Individual Andersen Defendants. Plaintiffs do not allege - nor could they - that any of these individuals possessed any general control over Andersen, nor do plaintiffs allege that any of these Individuals possessed the requisite day-to-day control over the specific Enron audits to satisfy the standards under § 20(a). Plaintiffs' vague and conclusory mantra that an Individual Andersen Defendant was a "partner" of Andersen and was "an integral part of the Enron audit" does not even come close to articulating "*each defendant's control* over the primary violator," as required. RGB Eye Assoc., 1999 LEXIS 21940, at * 39-40. Accordingly, even if this Court were to consider plaintiffs' highly ambiguous and confusing pleading as asserting a § 20(a) claim against the other Individual Andersen Defendants, the final result is the same. Plaintiffs have failed to plead a viable § 20(a) claim as to any of the Individual Andersen Defendants because the Consolidated Complaint insufficiently alleges that any of these individuals had the requisite control.

## CONCLUSION

For the reasons set forth above, plaintiffs' claims asserted against the Individual Andersen Defendants in Count I of the Consolidated Complaint should be dismissed.[14]

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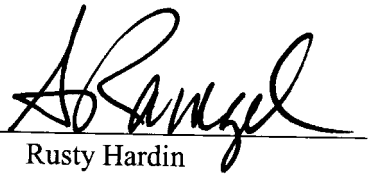
[14] Additional state law claims are alleged in certain of the consolidated Newby cases, but are not incorporated into the Consolidated Complaint. Accordingly, the Individual Andersen Defendants are not obligated to respond to these claims at this time. As set forth more fully in Andersen's Motion to Strike the First Amended Complaint in Wilt v. Fastow and Defendants' Motion for Entry of Preliminary Scheduling Order for Complaints Consolidated Into Newby and Pursued by Persons Other Than Court-Appointed Lead Plaintiff, which are being filed simultaneously with Andersen's Motion to Dismiss, the consolidation Order, dated December 12, 2001, and the subsequent scheduling orders require only that Andersen respond to the Consolidated Complaint. At such time, if ever, that this Court directs defendants to respond to these state law claims, Andersen will move to dismiss.

Dated: Houston, Texas
May 8, 2002

Respectfully Submitted,

By: 

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**CERTIFICATE OF SERVICE**

I hereby certify that on this 8th day of May, 2002, the forgoing pleading was served pursuant to the Court's April 5, 2002 Order.

Andrew Ramzel

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

| | | |
|---|---|---|
| In Re ENRON CORPORATION SECURITIES LITIGATION | § | |
| _____ | § | |
| MARK NEWBY, et al., Individually and On Behalf Of All Others Similarly Situated | § | Civil Action No. H-01-3624 And Consolidated Cases |
| vs. | § | |
| ENRON CORP., et al. | § | |
| _____ | § | |
| THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, et al., Individually and On Behalf of All Others Similarly Situated, | § | |
| v. | § | |
| KENNETH L. LAY, et al. | § | |
| _____ | § | |

ORDER

The Court grants the Motion of the Individual Andersen Defendants[1] To Dismiss Count I Of Plaintiffs' Consolidated Complaint, and dismisses with prejudice and in its entirety

[1]The "Individual Andersen Defendants" are Thomas H. Bauer, Michael L. Bennett, Joseph F. Berardino, Debra A. Cash, Donald Dreyfus, James A. Friedlieb, D. Stephen Goddard, Jr., Gary B. Goolsby, Gregory W. Hale, Michael D. Jones, Michael M. Lowther, Benjamin S. Neuhausen, Richard R. Petersen, Danny D. Rudloff, John F. Sorrells, John E. Stewart, William E. Swanson, Nancy Temple, and Roger D. Willard.

Plaintiffs' Consolidated Complaint For Violation Of The Securities Laws as against the Individual Andersen Defendants.

Signed this _____ day of _____, 2002.

_____
Melinda Harmon
United States District Judge