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.	§	
	§	
THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, et al., Individually and On Behalf of All Others Similarly Situated,	§	
	§	
Plaintiffs,	§	
	§	
vs.	§	
	§	
KENNETH L. LAY, et al.,	§	
	§	
Defendants.	§	

LEAD PLAINTIFF'S SUPPLEMENTAL OPPOSITION TO PENDING MOTIONS FOR SUMMARY JUDGMENT (DOCKET NOS. 4816, 4817, 4818, 4824, 4825 AND 5333)

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STATUTES, RULES AND REGULATIONS

I. INTRODUCTION

During the course of this litigation, Lead Plaintiff, The Regents of the University of California ("The Regents"), amassed evidence establishing that the defendant financial institutions (the "Banks") engaged in transactions that falsified Enron's reported financial condition (the "Transactions"). Prior to the recent decisions of the Supreme Court in *Stoneridge* and the Fifth Circuit in this case, the law – as embodied in the position of the Securities and Exchange Commission ("SEC") and decisions from other courts – indicated that defendants could be held liable under §10(b) ***solely*** for their conduct in the Transactions (given certain conditions). In other words, the existence of deceptive conduct – *i.e.*, conduct that had both the ***purpose and effect*** of creating a false impression of earnings, cash flow or debt – was thought to be sufficient in and of itself to support findings on the issues of deception ***and*** reliance. This Court, in certifying this case for class action treatment, adopted this legal standard and further found that two classwide presumptions of reliance were available. Accordingly, the focus of The Regents' theory of reliance remained on the Transactions.

The law, however, has now changed. While the Supreme Court's *Stoneridge* decision confirms that conduct alone can be viewed as "deceptive" within the meaning of the securities laws, it rejects the view that a classwide presumption of reliance can be supported by concealed conduct without more. Critically, this decision also indicates some of the circumstances where such a presumption of reliance ***is*** available.

In response to this change in the law, The Regents now submit to this Court a revised theory of reliance that fits squarely within the framework established by the Supreme Court and Fifth Circuit decisions, and is based on long-established legal principles. The defendant Banks, unlike the *Stoneridge* defendants, engaged and interacted with the Enron market on multiple levels, through a web of market-related activities. Taken together (and in some instances taken singly) these multiple

points of contact with the market created a ***duty to disclose*** the Banks' knowledge of the falsity of Enron's reported financials.

The legal authority supporting the existence of a duty in these circumstances is venerable and vast: it extends from the Supreme Court's seminal duty-to-disclose decision, *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128 (1972), through the Fifth Circuit's announcement of a multi-factor test for determining the existence of a duty in *First Virginia Bankshares v. Benson*, 559 F.2d 1307, 1314 (5th Cir. 1977), and includes well-settled legal principles regarding the existence of a disclosure duty for those that engage in certain market-related activity. The Banks here traded in Enron and Enron-related securities, underwrote offerings in Enron and Enron-related securities, interacted with rating agencies, and at least Credit Suisse First Boston ("CSFB") and Merrill Lynch ("Merrill") issued numerous analyst reports.

This theory of reliance is clearly ***not*** foreclosed by the decisions of the Fifth Circuit and Supreme Court. As discussed, those decisions concerned the question of liability for a secondary actor based on conduct in transactions alone. ***Neither of those Courts were presented with a theory of liability where a duty to disclose is based on the defendants' activities in the market for the issuer's securities***. In fact, because the above theory of liability fits within the Fifth Circuit and Supreme Court decisional framework for determining when a presumption of reliance is available, it is confirmed as sound not despite those decisions – but because of them. And it should be for the trier of fact to determine, for each defendant, whether plaintiffs have established that each owed a duty of disclosure giving rise to classwide reliance in this case.[1]

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[1] The issue of reliance is one best reserved for the trier of fact. *See Huddleston v. Herman & MacLean*, 640 F.2d 534, 550 (5th Cir. 1981) (Although trial judge in securities fraud action believed that neither reliance nor causation was a proper issue for the jury: "We disagree. The trial court's ***failure to submit the reliance*** and causation issues ***to the jury requires us to grant a new trial***."), *aff'd in part, rev'd in part on other grounds*, *Herman & MacLean v. Huddleston*, 459 U.S. 375

The other elements of a §10(b) cause of action are also satisfied. Defendants acted with scienter, as ***senior*** personnel at each of the Banks knew of the extensive market activity that created the Banks' duty to disclose and that Enron's reported financial condition was false. The impact on Enron's financials from the Transactions alone was obviously material in that the distortion of earnings, cash flow, and debt reached into the billions. Nor is there a question that the conduct was "in connection with" the purchase or sale of securities, as it coincided with transactions in Enron's securities. As described above, the *Affiliated Ute* presumption of reliance is available because defendants had a duty to disclose and failed to do so, and economic loss under *Dura*[2] ensued as the true state of Enron's operations became known to the market.[3]

II. PROCEDURAL BACKGROUND

A. This Court's Decision on Class Certification

This case was commenced in October of 2001. Over the course of this litigation, several of the secondary-actor defendants, including the Banks, repeatedly asserted that Lead Plaintiff's claims against them were foreclosed by the Supreme Court's decision in *Central Bank, N.A. v. First Interstate Bank*, N.A., 511 U.S. 164 (1994), which eliminated liability for aiding and abetting. Lead

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(1983) (all citations are omitted and emphasis is added throughout unless otherwise noted); *Shores v. Sklar*, 647 F.2d 462, 468 (5th Cir. 1981) ("Because ***reliance is so difficult to prove***" in an omissions case, "the Supreme Court has allowed ***the trier of fact to presume reliance*** in an omission case where the plaintiffs could justifiably expect that the defendants would disclose material information.").

[2] *Dura Pharms., Inc. v. Broudo*, 544 U.S. 336 (2005).

[3] At the February 1, 2008 status conference in this case, this Court directed The Regents to present its theory of liability as a supplemental opposition to the Banks' motions for summary judgment. Thus, as to each of the elements described, the standard for summary judgment applies. Accordingly, Lead Plaintiff need not affirmatively demonstrate that the elements of §10(b) are satisfied, but rather only show that there exist triable issues of fact concerning them. *See, e.g.*, Lead Plaintiff's Opposition to the CSFB Defendants' Motion and Memorandum of Law in Support of Their Motion for Summary Judgment (Docket No. 5217) ("CSFB Opp." or "CSFB Opposition") at 16-19 (describing general summary-judgment standard).

Plaintiff maintained, in opposition, that the Banks faced primary liability for their conduct under governing law.

The SEC addressed this particular primary liability issue in another case.[4] The SEC's position was that, under certain circumstances, engaging in transactions calculated to falsify an issuer's reported financial condition was sufficient for liability under §10(b): "***Engaging in a transaction*** whose principal purpose and effect is to create a false appearance of corporate revenues constitutes a deceptive act that can support primary liability." SEC Brief (Ex. 1) at 18. Several other courts fashioned similar rules of law which found liability (under certain circumstances) solely for engaging in transactions which operated to deceive.[5] These authorities also found the reliance element satisfied under these circumstances.[6]

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[4] *See* Brief of the Securities and Exchange Commission, *Amicus Curiae*, in Support of Positions that Favor Appellant (submitted on appeal of *In re Homestore.com, Inc. Sec. Litig.*, 252 F. Supp. 2d 1018 (C.D. Cal. 2003), *aff'd*, 452 F.3d 1040 (9th Cir. 2006)) ("SEC Brief") (Ex. 1). All references to exhibits and deposition transcripts are attached to Lead Plaintiff's Appendix of Exhibits in Support of Lead Plaintiff's Supplemental Opposition to Pending Motions for Summary Judgment (Docket Nos. 4817, 4818, 5333, 4824, 4825 and 4816), filed concurrently herewith.

[5] *See, e.g., Simpson v. AOL Time Warner Inc.*, 452 F.3d 1040, 1050 (9th Cir. 2006), *cert. granted, vacated, remanded*, 128 S. Ct. 1119 (2008) ("If a defendant's conduct or role in an illegitimate transaction has the principal purpose and effect of creating a false appearance of fact in the furtherance of a scheme to defraud, then the defendant is using or employing a deceptive device within the meaning of §10(b)."); *In re Parmalat Sec. Litig.* 376 F. Supp. 2d 472, 504 (S.D.N.Y. 2005) (finding liability where "[t]he transactions in which the defendants engaged were by nature deceptive").

[6] *See* SEC Brief (Ex. 1) at 22 ("[A] prior deceptive act, from which the making of the false statements [by the issuer] follows as a natural consequence, can constitute a sufficient step in the causal chain to support a finding of reliance."); *Simpson*, 452 F.3d at 1051 ("The requirement of reliance is satisfied if the introduction of misleading statements into the securities market was the intended end result of a scheme to misrepresent revenue."); *Parmalat*, 376 F. Supp. 2d at 508-09 ("[A.] Transaction Causation . . . . In this case, the complaint alleges that the banks' actions in connection with the relevant transactions actually and foreseeably caused losses in the securities markets. The Banks made no relevant misrepresentations to those markets, but they knew that the very purpose of certain of their transactions was to allow Parmalat to make such misrepresentations.

Understandably, The Regents conceived of, and presented, its case against defendants in these terms. Again, The Regents had developed evidence establishing that defendants had engaged in transactions calculated to falsify Enron's reported financial condition. Accordingly, in seeking class certification, The Regents focused almost entirely on the Banks' conduct in engaging in the Transactions. Reliance was satisfied because the conduct at issue – which had the effect of creating a materially false impression of revenue, earnings, or other financial metrics – necessarily had such a nexus to the market that they could fairly be said to have had the requisite connection to investor losses.

This Court accepted The Regents' theory of liability in granting class certification:

> The Court finds the SEC's clarification of the distinctions between aiding and abetting and a primary violation under §10(b), and the application of reliance where the alleged wrongful conduct is nonrepresentational under Rule 10b-5(a) and (c), illuminating and helpful and hereby adopts its approach.

In re Enron Corp. Sec. Litig., 529 F. Supp. 2d 644, 707 (S.D. Tex. 2006).[7] Thus, the Banks faced liability (under certain circumstances), solely for their conduct in the Transactions.

This Court also found that the element of reliance was satisfied for this conduct. The Regents argued that on the basis of the Banks' conduct, which was not disclosed to the market, that the case was primarily one of omissions, which thus gave rise to the *Affiliated Ute* presumption of reliance. This Court rejected the Banks' argument that the *Affiliated Ute* presumption was inapplicable, finding that the duty requiring disclosure was a duty not to engage in a fraudulent course of conduct:

In these circumstances, both the Banks and Parmalat are alleged causes of the losses in question. So long as both committed acts in violation of statute and rule, both may be liable.").

[7] *See also In re Enron Corp. Sec. Litig.*, 439 F. Supp. 2d 692, 715, 721-24 (S.D. Tex. 2006) (Court relies on scheme liability analysis employed by Judge Kaplan in *Parmalat*, stating that the SEC's position "appears to be in accord with Judge Kaplan's analysis in *Parmalat*").

> Financial Institution Defendants have argued that the *Affiliated Ute* presumption does not apply because they had no duty to disclose their conduct to Plaintiffs. Courts in this Circuit have recognized "the duty not to engage in a fraudulent 'scheme' or 'course of conduct' [that] could be based primarily on an omission." . . .
>
> Thus the Court concludes that the *Affiliated Ute* presumption of reliance is available to Lead Plaintiff who has pled the necessary underlying facts.

Enron, 529 F. Supp. 2d at 739 (quoting *Smith v. Ayres*, 845 F.2d 1360, 1363 & n.8 (5th Cir. 1988)). This Court also held that the fraud-on-the market presumption of reliance was available. *In re Enron Corp. Sec. Litig*., 236 F.R.D. 313, 316 (S.D. Tex. 2006). On this basis, the Court granted class certification. *See id*. at 320.

Because this Court adopted The Regents' view that the Banks could face liability solely for their participation in the Transactions, ***The Regents had no need to focus on alternative arguments*** based on the additional evidence it had gathered on the Banks. Also, because this Court concluded that the Banks had a "'duty not to engage in a fraudulent "scheme" or "course of conduct"'" (*Enron*, 529 F. Supp. 2d at 739), which permitted application of the *Affiliated Ute* presumption of reliance, The Regents never put forward an alternative argument as to why the Banks had an independent duty to Enron shareholders to disclose their knowledge of the fraud.

B. The Fifth Circuit Appeal

The Banks sought appellate review of the Court's decision granting class certification under Federal Rules of Civil Procedure ("Rule") 23(f), arguing that the theory of liability adopted by this Court was invalid under *Central Bank*, 511 U.S. 164. The Fifth Circuit agreed to hear the appeal. *See Regents of the Univ. of Cal. v. Credit Suisse First Boston*, 482 F.3d 372, 394 (5th Cir. 2007), *cert. denied*, 128 S. Ct. 1120 (2008).

On appeal, the Banks presented the controlling issue as whether they could be held liable solely for their conduct in the Transactions.[8] The Fifth Circuit also correctly understood that Lead Plaintiff's claim was that the Banks faced liability solely for engaging in the Transactions:

> The facts are difficult to detail but easy to summarize. Plaintiffs allege that [the Banks] ***entered into partnerships and transactions*** that allowed Enron Corporation ("Enron") to take liabilities off of its books temporarily and to book revenue from the transactions when it was actually incurring debt. The common feature of these transactions is that they allowed Enron to misstate its financial condition; there is no allegation that the banks were fiduciaries of the plaintiffs, that they improperly filed financial reports on Enron's behalf, or that they engaged in wash sales or other manipulative activities directly in the market for Enron securities.

Regents, 482 F.3d at 377. The Fifth Circuit observed that this Court had sanctioned Lead Plaintiff's theory of liability, in that it accepted that the Banks' conduct of engaging in the Transactions constituted a "deceptive act" actionable under Rule 10b-5.[9]

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[8] CSFB framed the relevant issue on appeal as whether this Court erred in finding that CSFB could be a primary violator "based on CSFB's ***participation in transactions*** that Enron allegedly misreported in its audited financial and disclosure statements." *See* Brief of Appellants Credit Suisse First Boston (USA), Inc., Credit Suisse First Boston LLC and Pershing LLC filed in the *Regents v. Credit Suisse First Boston (USA), Inc.*, No. 06-20856 (5th Cir.) at 2-3. Merrill similarly understood its appeal as a challenge to the theory that it faced liability solely for its conduct in the Transactions:

> Stripped of rhetoric, the complaint alleges that Merrill Lynch and other defendants ***engaged in transactions*** with Enron that Enron misreported to improve its financial statements. (*See, e.g.*, D.E. 1388, ¶ 105(b) (alleging that Merrill Lynch "enter[ed] into fraudulent transactions with Enron that were designed to artificially manipulate Enron's publicly reported financial results").)
>
> Such conduct lies outside the universe of acts that give rise to private civil liability under Section 10(b).

Brief Of Merrill Lynch Appellants filed in *Regents v. Credit Suisse First Boston*, No. 06-20856 (5th Cir.) at 22.

[9] *See Regents*, 482 F.3d at 378 ("The court determined that a 'deceptive act' within the meaning of rule 10b-5(c) includes participating in a 'transaction whose principal purpose and effect is to create a false appearance of revenues.' The district court decided that rule 10b-5(a)'s prohibition of any 'scheme . . . to defraud' gives rise to joint and several liability for defendants who commit individual acts of deception in furtherance of such a scheme. Implicit in that ruling is the conclusion that plaintiffs have alleged that just such a scheme existed.").

The Fifth Circuit concluded that Lead Plaintiff's liability theory of the case should not have been certified for class action treatment, due to the absence of a classwide presumption of reliance. First, the Fifth Circuit rejected this Court's finding that the *Affiliated Ute* presumption was applicable. The Fifth Circuit ruled that for the presumption to be applicable, the "plaintiff must (1) allege a case primarily based on omissions or non-disclosure and (2) demonstrate that the defendant owed him a duty of disclosure." *Regents*, 482 F.3d at 384. Assuming the case was an omissions case, the Fifth Circuit rejected this Court's ruling that a duty not to engage in scheme conduct alone suffices for application of the presumption. *See id*. According to the Fifth Circuit, "[n]either *Smith* nor any other of this circuit's cases is authority for that proposition." *Id*.[10]

The Fifth Circuit also determined that engaging in the Transactions alone was insufficient for primary liability under Rule 10b-5. The Fifth Circuit found this Court's definition of "deceptive conduct too broad," agreeing with the holding in *In re Charter Commc'ns., Inc.*, 443 F.3d 987 (8th Cir. 2006), that "any defendant who does not make or affirmatively cause to be made a fraudulent misstatement or omission, or who does not directly engage in manipulative securities trading practices, is at most guilty of aiding and abetting and cannot be held liable under §10(b) or any subpart of Rule 10b-5." *Id*. at 992. Thus, the Banks could not be held primarily liable solely for their conduct in the Transactions. The Fifth Circuit's decision reversed and remanded this Court's order granting certification. *Regents*, 482 F.3d at 394.

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[10] The Fifth Circuit also found, and this Court concurred, that the case as presented raised no independent ***duty*** on behalf of the Banks. Simply put, "the plaintiffs had no expectation that the banks would provide them with information, there is no reason to expect that the plaintiffs were relying on their candor." *Regents*, 482 F.3d at 385. Again, because this Court had adopted the position which appeared to be supported by prior Fifth Circuit law (*Smith v. Ayres*) that one has a general duty not to violate the law and that duty satisfied the *Affiliated Ute* requirement, The Regents remained focused on the Transactions.

C. The Supreme Court's Decision in *Stoneridge*

On March 26, 2007, the Supreme Court granted a petition for writ of *certiorari* in the *Charter* case. *See Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 127 S. Ct. 1873 (2007). And on January 15, 2008, the Supreme Court issued its decision in *Stoneridge*. *See Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 128 S. Ct. 761 (2008).

In *Stoneridge*, the Supreme Court understood the case as one where the plaintiffs "sought to impose liability on entities who, acting both as ***customers and suppliers***, ***agreed to arrangements*** that allowed the investors' company to mislead its auditor and issue a misleading financial statement affecting the stock price." *Stoneridge*, 128 S. Ct. at 766. There was no allegation that the entities were active in the market for the issuer's securities.

The Supreme Court summarily rejected the Fifth and Eighth Circuits' narrow view of what constitutes a "deceptive act" within the meaning of §10(b) and Rule 10b-5, concluding that there need not be a specific oral or written statement before §10(b) liability attaches. *Id.* at 769.[11] Nonetheless, the High Court ruled that the plaintiff's theory of liability was invalid because the element of reliance was lacking. *Id*. Specifically, the *Affiliated Ute* presumption of reliance was unavailable because, under the circumstances, the entities did not have a duty of disclosure to the company's investors. *Id*. Also, because their "deceptive acts were not communicated to the public," neither was the fraud-on-the-market presumption applicable. *Id*.

In so ruling, the *Stoneridge* Court took pains to emphasize the particular role of the entities and their conduct. The Court highlighted that the flawed theory of liability there sought to apply §10(b) "beyond the securities markets – the realm of financing business – to purchase and supply

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[11] In this important regard, the Supreme Court's decision validated the position argued by The Regents and accepted by this Court that conduct alone, under certain circumstances, can lead to primary liability.

contracts – the realm of ordinary business operations." *Id*. at 770. Later in the opinion, the Court carefully re-emphasized that the subject conduct "took place in the marketplace for goods and services, not in the investment sphere." *Id*. at 774.[12]

III. ARGUMENT

A. Overview

The evidence presented in this case creates a triable issue of fact as to whether each of the remaining bank defendants had a duty to disclose ***at least*** the facts concerning its own deceptive conduct and the effects of that conduct on Enron's reported financial results. This duty arises from the complex, multifaceted, active participation of the Banks in the market for Enron securities and their efforts to encourage and induce investors to purchase those securities.

In stark contrast to the supplier/customer defendants in *Stoneridge*, who had little if any contact with the Charter Communications investment community, here the Banks engaged and interacted on many levels with Enron investors and with the market. In so doing, the Banks actively sought to encourage and induce market investors to purchase Enron securities. Among other things, some or all of the Banks:

- traded in Enron common stock in transactions known as equity swaps or equity forwards;
- underwrote new issuances of Enron securities;

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[12] On April 5, 2007, The Regents filed a Petition seeking Supreme Court review of the *Regents* decision. On January 28, 2008, the Supreme Court denied the Petition. *See Regents of the Univ. of Cal. v. Merrill Lynch, Pierce, Fenner & Smith Inc.*, 128 S. Ct. 1120 (2008). The Banks will no doubt argue that the Supreme Court's refusal to review *Regents* serves as an indication of the Court's recognition that The Regents no longer have any viable claims against them post-*Stoneridge*. However, neither the Fifth Circuit nor the Supreme Court was faced with whether plaintiffs in this case had a viable alternative theory of reliance. Plaintiffs do and to the extent the Fifth Circuit or Supreme Court decisions have an impact on this alternative theory, that impact supports – not detracts – from this theory.

- marketed Enron-related securities, *e.g.*, securities related to some of the transactions referenced above;

- interacted with credit-ratings agencies in matters related to Enron, either with regard to Enron's own securities, and/or with regard to Enron-related securities;

- transacted in Enron credit-default derivatives; and

- issued analyst reports on Enron which discussed the Company's reported financial condition and recommended the purchase of Enron stock.

Thus, the Banks' role in the Enron world was not limited to engaging in the Transactions; it extended beyond, as the Banks were intertwined with Enron's corporate financing activities, with the market in which Enron securities traded, and with various constituencies within that market. In short, the Banks sought to engage and did engage with the investor members of the plaintiff class.

In connection with several of these roles, the Banks held themselves out as experts, having special knowledge and insight into Enron. Thus they sought to, and did, create and foster relationships with Enron investors; Enron investors rightly should have been able to expect candor and to expect that the Banks were not themselves involved behind the scenes in deceptive transactions that undercut their market activity.

The point is that these investment Banks stood in very different positions than did the supplier/customer defendants in *Stoneridge*. While the *Stoneridge* defendants operated in "the marketplace for goods and services," these investment Banks operated in "the investment sphere."[13] This is perhaps another way of saying that the *Stoneridge* defendants had little if any contact with the marketplace in which Charter Communications securities were traded; in contrast, these investment Banks sought out and nurtured extensive and ongoing contacts and relationships with the marketplace in which Enron securities were traded. Having done so and then remained silent about the impact of their conduct on Enron's reported financials is to have omitted material information.

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[13] *Stoneridge*, 128 S. Ct. at 774.

As discussed below, a duty to disclose is often found where the relevant audience – here, the market – can be said to have a reasonable expectation of disclosure.[14] That expectation – disclosure of the omissions here – and consequent duty to disclose can arise from different factors. Each of these Banks held itself out as having superior knowledge of and insight into Enron; each in fact had superior knowledge, especially as to how its own deceptive acts had materially impacted Enron's reported financial results; each traded in or underwrote Enron and Enron-related securities; each had regular and continuous contacts with the market, which included the providing of information and opinions concerning Enron's financial performance and prospects; and each – in an effort to enhance its own position with Enron and thus increase its own profits – withheld this knowledge even as it sold Enron securities to the marketplace.[15]

B. The Banks' Activities in the Market for Enron and Enron-Related Securities Created Duties to Disclose[16]

1. CSFB

At the same time as the Banks were engaging in the Transactions to falsify Enron's reported financial condition, they were also active in the market for Enron and Enron-related securities. According to Fastow, because CSFB "was among the very best at structured finance," it was a "go-

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[14] Also of note is that some disclosure duties are imposed more to discourage the underlying conduct than to encourage after-the-fact information flow.

[15] In contrast, the supplier/customer defendants in *Stoneridge* did not hold themselves out as having superior knowledge about Charter; did not communicate, engage, or interact with the marketplace in which Charter securities were traded; and did not publicly opine on Charter's financial results or prospects or on the value of Charter securities. Thus – other than the fact that they engaged in the deceptive deals, which the Court held was not enough of itself to create a duty to disclose – there was no reason for the market to form a reasonable expectation of disclosure.

[16] Pursuant to an agreed motion and Order, the Complaint is deemed amended to include all allegations and evidence offered by The Regents in its oppositions to the summary judgment motions. 1/22/07 Order on Agreed Motion to Deem Complaint Amended (Docket No. 5334).

to" bank for Enron.[17] Fastow viewed CSFB as a bank that "worked to solve certain of [Enron's] financial problems."[18] CSFB also had an active role in marketing Enron and Enron-related securities. Enron needed prestigious investment banks such as CSFB to lend credibility to the Company by both selling securities in offerings and recommending the purchase of Enron stock in analyst reports. As one CSFB analyst candidly remarked to another in an internal email:

> [W]e were in love with ene and ene loved us. We were their number 1 supporter so the threat of a damaging research note was zero. ***They needed us to publicly sell the stock*** almost as much as we needed them for the fees.

Ex. 15648 (11/29/01 email from Brian Gibbons to Andy Devries).

Certain activity alone subjects CSFB to liability for its failure to abstain or disclose. Specifically, CSFB bought Enron common stock at Enron's request at various times in 2000 and 2001. CSFB entered transactions it referred to as "equity swaps" and "equity forwards," whereby it agreed to purchase Enron common stock in the open market and Enron agreed to pay CSFB the price it paid plus interest at some time in the future, typically in one year. CSFB's purchases appeared to the market to be legitimate transactions driving volume up, and supporting the price. At no time did CSFB disclose the fraud as it traded in Enron's stock.[19]

CSFB's Steve Haratunian described an equity forward as "a contract for the future delivery of stock or the future purchase of stock . . . by the counterparty, at a known price." 9/16/05 Deposition Transcript of Stephen Haratunian ("9/16/05 Haratunian Depo. Tr.") at 60:4-8. "[In] [a] typical equity forward contract, the price would be set on the current prices of the stock at the time

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[17] 10/24/06 Deposition Transcript of Andrew S. Fastow ("10/24/06 Fastow Depo. Tr.") at 433:1-21.

[18] Declaration of Andrew S. Fastow (Docket No. 5048) ("Fastow Decl."), ¶¶6, 8.

[19] Separate equity transactions also took place. For example, as part of the SAILS transaction with Enron in late 1999, CSFB's affiliate effected a short sale of Enron shares in the open market. *See* 12/1/04 Deposition Transcript of Richard H. Ivers ("12/1/04 Ivers Depo. Tr.") at 147:9-151:7.

you entered into the transaction, plus a spread or a finance . . . ." Ex. 21826 at 14:24-15:3. In a January 2000 presentation CSFB gave to Enron it stated: "Equity Forwards are contracts which provide for the repurchase at a future date of company shares at a pre-set 'forward price.' Economically, the company purchases shares immediately, while funding the purchase at a later date. . . . Off Balance Sheet Accounting: the Equity Forward is effectively an off balance sheet obligation of the company." Ex. 21829 at CSFBLLC 006362885. CSFB did such "Equity Forwards" with Enron. 9/16/05 Haratunian Depo. Tr. at 129:23-130:3. An example of one of these trades is found in CSFB's "Equity Forward Transaction, Summary of Terms and Condition" as follows: "On June 27, 2000, [CSFB] and [Enron] entered into a Forward Purchase Contract relating to the Principal Share Amount . . . . On July 11, 2000, [CSFB] and Enron amended and restated the Original Transaction as an Equity Swap Transaction. On August 9, 2000, [CSFB] and Enron terminated the Equity Swap Transaction. The parties hereto are entering into a Forward Purchase Contract relating to the Principal Share Amount with the following terms: . . . Principal Share Amount: 750,000 Enron Corp. shares . . . Trade date: August 4, 2000." Ex. 21838 at CSFBLLC 005431933. CSFB bought credit protection for itself to reduce its risk on Enron's inability to pay. Ex. 21826 at 22:1-25:25. CSFB did additional swaps in June and July 2001. Ex. 21858 at CSFBLLC 006303996. By August 2001 CSFB had outstanding "Enron Trades" of over 4 million shares of Enron common stock with a "notional" value of over $324 million. Ex. 21856 at CSFBLLC 005432037. That is, CSFB had purchased over 4 million shares of Enron stock and Enron had promised to pay CSFB over $324 million for them.[20]

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[20] In a recent hearing, counsel for Enron described these transactions as follows:

> [T]he real purpose of the transactions, these transactions were used to manipulate the market price of Enron's stock. They were used to generate what the EGF [Enron Global Finance] players characterized as income by starting out a swap, taking the

In addition, CSFB brought numerous Enron and Enron-related securities to market, in both public and private offerings.[21] Specifically, CSFB marketed securities from several of the structured finance deals it did with Enron, *i.e.*, Osprey, Marlin, Firefly, and Iguana. CSFB used both its analysts and bankers for these efforts. For example, CSFB analyst Terran Miller participated in marketing the Marlin deal to investors. *See* 7/14/05 Deposition Transcript of Brian Herman ("7/14/05 Herman Depo. Tr.") at 390:3-393:1; Ex. 13137A; 2/18/05 Deposition Transcript of Brian McCabe ("2/18/05 McCabe Depo. Tr.") at 502:1-503:10. Miller was given the opportunity to comment on draft road show materials for the deal. Ex. 13136A. Bankers Larry Nath and Dwight Scott (then of DLJ) were involved in preparing the road show presentation for the certificates of the Marlin transaction. *See* 1/13/05 Deposition Transcript of Lawrence Nath ("1/13/05 Nath Depo. Tr.")

> gain out, and converting that swap to a forward and declaring the gains as earnings, and then taking the forward and placing it on the equity side of the balance sheet where it was essentially hidden from view.

In re Enron Creditors Recovery Corp., No. 01-16034, Transcript (S.D.N.Y., dated Apr. 10, 2007) ("Bankruptcy Tr.") (Ex. 2) at 13.

[21] *See* CSFB Opp., Ex. 4 at Appendix 2. **November 1998** offering of $250 million Enron 6.95% notes; **February 1999** offering of $752.25 million of Enron common stock; **April 1999** $850 million East Coast Power notes; **June 1999** offering of $695.4 million of Azurix common stock; **February 2000** offering of $540 million in Azurix 10; **October 2000** offering of $504 million of TNPC, Inc. common stock; **December 1998** Rule 144A offering of approximately $1 billion in debt and $125 million in equity of Enron's investment through Marlins; **December 1998** $415 million bank facility and a placement of $60 million in equity in connection with Enron's monetization, through the vehicle Firefly, of its interest in Elektro, a Brazilian power company; **December 1998** $750 million debt offering in connection with the financing of international Enron assets; **September 1998** Rule 144A offering of $1.4 billion in debt and $100 million in equity in connection with Osprey; **November 1999** Rule 144A offering of $750 million of debt and a placement of $75 million equity in connection with financing the investments of Yosemite Securities Trust I; **December 1999** Rule 144A offering of $202 million in debt and a placement of $6.4 million equity in connection with Iguana and Red Salamander Trust; **January 2000** placement of $100 million of common stock, Class A warrants and Class B Warrants for EMW Energy Services Corp.; **February 2000** $540 million in Azurix notes; **March 2000** Rule 144A floating rate note offering of $1 billion for Enron; **July 2000** placement of $70 million equity and placement of $97.5 million common stock and Class A warrants for The New Power Company; **October 2000** $500 million TNPC Inc. common stock.

at 448:19-449:16. CSFB distributed presentation materials to investors in marketing the certificates from the Marlin Water Trust I (*see* Ex. 50844, October 1998) and II (*see* Ex. 50832, June 2001). CSFB created road show materials to market the Osprey notes and certificates. 8/1/05 Deposition Transcript of Dominic Capolongo ("8/1/05 Capolongo Depo. Tr.") at 74:16-75:25.

CSFB personnel also interacted with credit-rating agencies covering Enron in connection with the securities issued in some of the bank's structured-finance transactions with the Company. CSFB worked on an Enron presentation to Standard & Poor's regarding Osprey. Ex. 20544 at DBG 036891-919; 8/1/05 Capolongo Depo. Tr. at 68:18-69:25. Nath, while at CSFB, discussed some of Enron's structured-finance transactions with a representative from Standard & Poor's. 9/21/05 Deposition Transcript of Todd A. Shipman ("9/21/05 Shipman Depo. Tr.") at 354:25-356:5. Nath made a presentation to Standard & Poor's regarding the Osprey transaction. 9/22/05 Deposition Transcript of Todd A. Shipman ("9/22/05 Shipman Depo. Tr.") at 622:21-623:10. DLJ met with Standard & Poor's regarding the Marlin I transaction. 3/16/05 Deposition Transcript of Ronald Barone ("3/16/05 Barone Depo. Tr.") at 790:18-792:17. CSFB assisted Enron in presentations to Standard & Poor's regarding the Osprey transaction. 3/16/05 Barone Depo. Tr. at 804:19-23; 806:2-6. Enron's presentation to Moody's Investors Service regarding Marlin Water Trust and Marlin Water Trust II listed Nath and Capolongo as "contacts." *See* Ex. 11401 at MDY007413. Ex. 13683 (ANARPT003179-80) is a DLJ analyst report on Enron dated July 13, 1999. It states: "An affiliate of Donaldson, Lufkin & Jenrette Securities Corporation ***makes a market in this security***, has periodic positions in this security in connection with this activity and may be on the opposite side of public orders executed on a regional stock exchange where it acts as a specialist." (Original emphasis omitted.) At that time (*i.e.*, 2Q99), the transactions of Rawhide, Firefly, and Marlin operated to conceal $2.374 billion in Enron debt. *See* CSFB Opp. at 272.

During the Class Period, CSFB issued analyst reports (or other written communications to the market)[22] that were overwhelmingly positive, featuring emphatic recommendations that investors purchase Enron stock. *See* CSFB Opp. at 213-222.

CSFB used its research arm not as an independent voice to fairly evaluate Enron's securities, but rather as a cheerleader for the Company, to sell its stock to the investing public. Because of CSFB's interest in receiving lucrative investment banking business from Enron – *i.e.*, fees from the offerings listed above and from financing transactions – "the threat of a damaging research note was zero." Ex. 15648. CSFB sent draft (*i.e.*, pre-publication) analyst reports to Enron personnel, such as Jeff Skilling and Mark Koenig, asking for "comments/changes." *See* Ex. 15911; 9/13/05 Deposition Transcript of Philip Salles ("9/13/05 Salles Depo. Tr.") at 121:16-123:12. CSFB analysts Salles and Launer made a presentation concerning Enron at an industry conference; in preparing the presentation, these two discussed selecting the information presented in order to make Enron "look better." Ex. 15914; 9/13/05 Salles Depo. Tr. at 143:24-145:16. CSFB bankers worked to "recraft the [E]nron story" for the Company's road show presentations. Ex. 21303; 1/6/05 Deposition Transcript of Dominic Capolongo ("1/6/05 Capolongo Depo. Tr.") at 367:18-369:19.

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[22] CSFB issued analyst reports on Enron on at least the following dates: 06/09/99; 06/11/99; 07/06/99; 07/13/99; 07/14/99; 07/21/99; 08/16/99; 08/20/99; 08/23/99; 09/02/99; 09/10/99; 09/22/99; 10/08/99; 10/12/99; 11/24/99; 11/29/99; 11/30/99; 12/16/99; 12/17/99; 01/02/00; 01/10/00; 01/13/00; 01/14/00; 01/18/00; 01/21/00; 01/24/00; 02/28/00; 03/07/00; 04/12/00; 04/13/00; 05/22/00; 07/24/00; 10/12/00; 10/16/00; 10/17/00; 10/18/00; 10/20/00; 10/23/00; 11/06/00; 11/13/00; 12/04/00; 12/11/00; 01/12/01; 01/22/01; 01/26/01; 01/29/01; 02/05/01; 02/20/01; 03/05/01; 03/12/01; 03/19/01; 03/22/01; 03/26/01; 04/16/01; 04/17/01; 04/18/01; 04/23/01; 04/26/01; 05/18/01; 05/21/01; 05/29/01; 06/11/01; 06/25/01; 06/27/01; 07/09/01; 07/12/01; 07/16/01; 07/26/01; 08/14/01; 08/15/01; 08/17/01; 08/20/01; 08/27/01; 09/04/01; 09/10/01; 09/17/01; 10/01/01; 10/08/01; 10/09/01; 10/15/01; 10/16/01; 10/17/01; 10/19/01; 10/22/01; 10/23/01; 10/24/01; 10/25/01; 10/26/01; 10/29/01; 11/05/01; 11/12/01; 11/16/01; 11/19/01; 11/20/01; 11/21/01; 11/23/01 and 11/26/01. *See* CSFB Opp. at 234 n. 256; *see also* CSFB Opp., Ex. 76.

CSFB, in a presentation to Enron's New Power Company concerning the IPO process, vowed that its "[r]esearch [c]overage" would feature "positioning themes," and that it would "[p]articipat[e] in preparation of roadshow presentation and marketing materials." Ex. 13139A at CSFBLLC 005249273; 2/18/05 McCabe Depo. Tr. at 505:11-506:24. Ultimately, analyst Salles assisted Enron in crafting its road show presentation for the New Power IPO, to make it "more effective" to encourage investors to buy shares. 9/13/05 Salles Depo. Tr. at 177:3-25. Analyst Launer also participated in the "preparation of road show presentation and marketing materials" for the New Power IPO. 5/11/05 Deposition Transcript of Curt Launer ("5/11/05 Launer Depo. Tr.") at 371:22-372:17; Ex. 13139A. Launer further made "continuous calling efforts to potential investors" for the New Power offering. 5/11/05 Launer Depo. Tr. at 373:11-16.

2. Merrill

Merrill provided information and opinions to the market that conspicuously omitted any mention of the deceptive transactions in which Merrill itself was involved – the 1999 year-end Nigerian Barge deal, Power Trades, and LJM2 deals, which together fraudulently boosted Enron's fourth quarter 1999 earnings by approximately 30%; the subsequent Raptor and other LJM2 transactions, which also had very significant but hidden effects on Enron's reported financial results for 2000 and 2001 and on the market's perception of Enron's strength and prospects.

For example, on January 20, 2000 – only days after Merrill's deceptive acts had been used to create the appearance that Enron had met its 4Q99 earnings number, when in fact it had missed that number by about 30% – Merrill published a glowing research comment which not only repeated without qualification the earnings number Enron had just published, but also extolled the Company

for its "solid quarter," the "[s]trong IBIT growth in the wholesale energy services division [which] again fueled the quarter," and the "standout" performance of the wholesale energy business.[23]

Further, through the Spring of 2000 Merrill marketed the LJM2 vehicle to a select group of its institutional and high-net-worth clients – just the kind of investors who are most likely to move or support the market, and who are important to the operation of an efficient market. In the course of this marketing activity, Merrill discussed and provided written information about Enron's financial performance and prospects – again without any mention of the Nigerian Barge deal or the Power Trades, or of how those phony transactions affected Enron's reported financials or perceived strength. Moreover, in the Fall of 2000 Merrill actively marketed LJM3 to the same kinds of clients.

In addition to the above, Merrill engaged in transactions in Enron's common stock which gave rise to an independent duty to abstain or disclose. Merrill did neither. Between June 2000 and October 2001, Merrill was a counterparty to certain equity swaps. Ex. 4 (MLNBY 0306649-63). For example, starting on June 28 up and through July 6, 2000, Merrill purchased 1,388,100 shares of Enron common stock on the open market.[24] It did so at the request of Enron, in order to enter into a share-swap transaction which was a total return swap under which Enron would receive the economic benefit associated with the shares (including price appreciation), and Merrill would receive its purchase price plus interest and incidental charges. The share swap was traded on June 28, 2000, and was effective as of July 13, 2000, according to a Share Swap Transaction confirmation

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[23] Merrill published analyst reports (often multiple reports on a single day) on the following days: 1/18/00, 1/20/00, 1/21/00, 1/24/00, 4/12/00, 5/24/00, 7/24/00, 7/25/00, 9/7/00, 10/17/00, 10/18/00, 10/27/00, 12/20/00, 1/22/01, 1/23/01, 3/12/01, 3/21/01, 4/17/01, 4/18/01, 5/18/01, 5/24/01, 6/6/01, 6/27/01, 7/12/01, 8/15/01, 10/9/01, 10/16/01, 10/22/01, and 10/24/01 (Ex. 3).

[24] *See* Ex. 5 (MLNBY 0158414-16).

dated October 16, 2000.[25] These purchases were visible to the market, in the sense that it was aware of the buy-side demand and the volume of shares purchased, but the market did not know that Merrill was the purchaser or that it had purchased at the request of Enron. Nor was the market aware of the share-swap transaction.[26]

Subsequently, according to documents produced by Merrill, the share swap was terminated and was replaced by a Forward Purchase Contract involving the same 1,388,100 shares, under which Enron agreed to purchase those shares one year later for the price originally paid plus a pre-determined rate of interest and associated purchase and carrying charges.[27] It appears this change was backdated, such that the termination of the share swap and the inception of the forward contract were deemed to have occurred on August 4, 2000.[28]

Merrill's engagement in these transactions is important on several levels. First, because Merrill went into the open market and purchased a very large block of Enron common stock – at a time when it already knew material non-public information about its prior deceptive acts and their impact on Enron's reported financials – Merrill had a duty to disclose under the disclose-or-abstain rule. Second, this series of transactions, which were backdated to appear to have taken place in

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25 *See* Ex. 6 (MLNBY 0258669-74).

26 *See* Ex. 6 (MLNBY 0258669-74).

27 *See* Ex. 7 (MLNBY 0258675-76); Ex. 8 (MLNBY 0258682-86).

28 *Id.* Enron's bankruptcy counsel recently explained to Judge Gonzalez that the share swaps (which were transacted by CSFB as well as Merrill) were directed by Messrs. Skilling, Fastow, and Glisan because they "were extremely hot to have swaps happen at particular points in time when they perceived their stock price was vulnerable" and that "these transactions were used to manipulate the market price of Enron's stock." Bankruptcy Tr. (Ex. 2) at 7:19-22; 13:5-7. Enron's counsel further explained the reason for switching from a swap to a forward purchase transaction structure: "They were used to generate what the [Enron Global Finance] players characterized as income by starting out with a swap, taking the gain out, and converting that swap to a forward and declaring the gains as earnings, and then taking the forward and placing it on the equity side of the balance sheet where it was essentially hidden from view." *Id*. at 13:7-12.

particular quarters (apparently so as to create the false appearance of economic activity), could be viewed by a reasonable jury as additional instances of deceptive conduct and/or market manipulation on the part of Merrill.

Merrill's "sell-side" analysts also regularly communicated with "buy-side" analysts working for institutional investors.[29]

Merrill also acted as a market maker – defined as "a firm that stands ready to buy and sell a particular [security] on a regular and continuous basis at a publicly quoted price" – in connection with Enron's debt and certain other securities.[30]

Throughout 2000 and 2001, Merrill acted as underwriter, lead arranger, and sole market runner for certain Enron debt securities.[31] In so doing, Merrill communicated with institutional investors, and as underwriter it vouched for the accuracy of Enron's reported financial statements (which were incorporated by reference) and purchased and sold the referenced debt securities.

Merrill not only bought and sold Enron securities as an underwriter, but it also transacted in Enron securities and Enron credit-default derivatives for its own account.[32]

Finally, Merrill interacted with the credit-rating agencies on a number of occasions for Enron-related securities. For example, in late 1999, Merrill employee Brian Keegan opened

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[29] *See, e.g.*, testimony of former Regents' investment manager Jeffrey Heil: All of UC's buy-side analysts "talk[ed] with [sell-side] research analysts . . . . I'm sure he [UC analyst Arild Holm] spoke to the five or six largest the most; you know, Morgan Stanley, Goldman Sachs, Salomon, Merrill, J.P. Morgan." 8/25/03 Deposition Transcript of Jeffrey Heil at 45-46.

[30] The definition of "market maker" is provided by the SEC at http://www.sec.gov/answers/mktmaker.htm. *See, e.g.*, Ex. 9 (MLNBY 0267288-91 (7/12/01 Merrill Lynch Fixed Income Research Report)): "MLPF&S usually makes a market in the bonds of this company [Enron]."

[31] *See, e.g.*, Ex. 10 (MLNBY 0249345-69); Ex. 11 (MLNBY 0022723-76); Ex. 12 (MLNBY 0249300-04); Ex. 13 (MLNBY 0249560-64); Ex. 14 (MLNBY 0249613-16); Ex. 15 (MLNBY 0249617-20); Ex. 16 (MLNBY 0249716-19).

[32] *See, e.g.*, Ex. 17 (MLNBY 0919656-60).

discussions with Ron Barone of S&P, as well as John Diaz of Moody's, concerning Enron.[33] Moreover, in connection with the large yen-denominated Euro-note offerings which it underwrote and managed in 2000 and 2001, Merrill interacted closely with R & I Ratings, the largest credit-rating agency in Japan, and obtained a very favorable rating for Enron.[34] Merrill also helped obtain ratings by S & P, Moody's, and Fitch for these yen-denominated Euro-note offerings.[35]

Merrill's deceptive conduct and its various market activities were pieces of a whole – all that Merrill did was aimed at snaring its share of the highly (some would say obscenely) lucrative Enron business. Merrill did not engage in the year-end 1999 transactions because they were profitable on a stand-alone basis, or to show its appreciation for the business Enron had sent its way in the past.[36] ***Merrill engaged in these deceptive deals, and agreed to keep quiet about the secret side arrangements that rendered them deceptive, because senior Merrill bankers believed that doing so was necessary as a quid pro quo in order to get highly lucrative corporate finance "mandates" from Enron***.

These same senior Merrill bankers – Schuyler Tilney and others – also knew that Enron had imposed another condition to letting Merrill into the "wildly profitable deals": Merrill had to continue publishing regular and favorable analyst reports extolling Enron's results and prospects.[37]

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33 *See* Ex. 18 (MLNBY 0065768-69); Ex. 19 (MLNBY 0065770).

34 *See* Ex. 20 (MLNBY 0133590-91); Ex. 21 (MLNBY 0121058); Ex. 22 (MLNBY 0075591).

35 *See, e.g.*, Ex. 14 (MLNBY 0249613-16); Ex. 13 (MLNBY 0249560-64); Ex. 16 (MLNBY 0249716-19).

36 Indeed, some senior bankers argued against consummating these deals, precisely because they knew they were dirty and thus entailed significant "reputational risk" for Merrill. These voices, however, were overwhelmed by those for whom profit came before honor.

37 Ex. 23 (MLNBY 0050913) ("wildly profitable deals").

So, they knew that ***Merrill had to continue to speak to the market about Enron – dropping coverage of Enron was simply not an option***. The problem – and Tilney and the other senior Merrill bankers knew it – was that when Merrill spoke to the market, it simply could not tell the truth about what it knew.

And of course, the corporate-finance mandates Merrill hoped to win from Enron would necessarily entail, among other things, communications with the market in which Merrill would necessarily continue to keep quiet about the deception.[38]

Merrill specifically discussed the impact of its activities on Enron's stock. Merrill's Tilney, in discussing the "***unwind***," "***at yearend when we did this trade***," of the Power Trades, emphasized that circumstances had not changed to justify a lower fee, for "***they [Enron] knew what we were making at . . . the quarter and year (which had great value in their stock price, not to mention personal compensation***)." Ex. 50028 at MLBE 0370956. Merrill's Gordon agreed: "in light of their earnings number (and personal compensation benefits), ***the $17 million does not seem too significant for them***." *Id*. Thus, Merrill was well aware that its deceptive conduct was impacting the "***value***" of Enron's stock in the market.

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[38] Some of Merrill's offerings and other interaction with the market included: **September 1999** acquisition of AMX by Azurix (Advisor); **February 1999** $752 million Enron common; **August 1999** $116 million of debt Enron Teesside Operations Ltd.; **May 1997** $150 million bonds Sutton Bridge; **December 1999** LJM2 equity fund private placement; **December 1999** Merrill interest in Enron Nigeria Barge, Ltd.; **December 1999** proprietary investment in private equity fund ($5 million); **April 2000** feeder fund investment in private equity fund with participation by Merrill employees ($16.6 million); **June 2000** Merrill sale of interest in Enron Nigeria Barge, Ltd.; **June 1999-March 2001** energy derivative trades; **June 2000-November 2001** interest rate swaps with Enron North America; **Mid-1999-November 2001** spot and forward foreign exchange transactions with Enron North America; **March 2000-October 2001** credit default swaps and credit default basket transactions; **June 2000-October 2001** equity swaps with Enron North America. *See* Ex. 4 (MLNBY 0306649-63).

Illustrative of the intertwined Enron/Merrill relationship was Enron's requirement that Merrill issue positive analyst reports to induce the purchase of Enron securities for further transactional work.[39] According to Merrill's Tilney,[40] Fastow approached him about a large ($800 million-$1 billion) equity offering in early 1998.[41] Fastow told Tilney extreme secrecy was necessary.[42] Based on his conversations with Fastow, Tilney expected that Merrill would be either lead or co-lead manager of the potential offering.[43] Fastow later called Tilney to tell him the offering was going forward, but Merrill would have no part of the offering.[44] Tilney was upset and asked Fastow why Merrill was being excluded from the offering. According to Tilney, Fastow told him, "it was a decision of the two senior managers in the company, Mr. Lay and Mr. Skilling, and that they were disappointed with [Merrill's] research coverage and that that was the reason for [Merrill] not being included."[45]

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[39] John Olson was an equity analyst at Merrill Lynch covering the energy sector, including Enron, from 1992 until 1998. In July of 1997, Olson lowered his rating on Enron stock from accumulate to neutral in the intermediate term, with a long-term buy rating. *See* Ex. 24 at ELIB00000621-00001-00004 (7/17/97 John E. Olson, Merrill Lynch, Comment: "Enron Corp. – ENE will Rise Again and Fight Another Day: But Not Today"). *See also* Ex. 52190 at 43; Ex. 25 at 1 ("Intermediate Term: Neutral") (1/23/97 Olson Analyst Report); Ex. 26 at 1 (Intermediate Term: "Neutral") (10/16/97 Olson Analyst Report); Ex. 27 at 1 (Intermediate Term: "Neutral") (3/31/98 Olson Analyst Report); Ex. 28 at 1 (Intermediate Term: "Neutral") (7/16/98 Olson Analyst Report).

[40] *See* Ex. 40052 at MLBE0087040-41 (4/18/98 memorandum to Allison from Gordon and Tilney); Ex. 52190 at 50-51, 68-70; Ex. 29 at MLBE0156663 (5/22/98 email from John Olson to Andrew Melnick, Merrill).

[41] 8/17/06 Deposition Transcript of Schuyler Tilney ("8/17/06 Tilney Depo. Tr.") at 152:24-153:18.

[42] 8/17/06 Tilney Depo. Tr. at 154:14-16.

[43] 8/17/06 Tilney Depo. Tr. at 156:5-157:4.

[44] 8/17/06 Tilney Depo. Tr. at 162:11-163:14.

[45] 8/17/06 Tilney Depo. Tr. at 164:12-16.

According to Fastow, he "drew a short straw" among Enron's senior management in that he was asked to deliver the message to Merrill "that it would be difficult, if not impossible, for Enron to give Merrill the business of leading an equity offering for Enron because their equity analyst was saying not to buy the stock."[46] In other words, Olson's research cost Merrill a role in the equity offering.[47] Tilney testified this was the "sole reason . . . or the primary reason," Merrill was cut out of the deal.[48] Indeed, "it was well-known to the investment banking community that in order to be a friend of Enron, the analysts had to be on board in giving strong ratings."[49]

3. Barclays

Barclays was also active in the market for Enron securities, in that it underwrote two major securities offerings for Enron: A February 2000 Yosemite Securities Co. Ltd. £200,000,000.00 8.75% Series 2000 A Linked Enron Obligations due 2007 (the "Yosemite LEOs") (Ex. 31); and then a February 2001 Private placement of $1.9 billion Zero Coupon Convertible Senior Notes due 2021 ("Zero Coupon Notes") (Ex. 30).

As to the Yosemite LEOs, the offering memorandum provided that these would be sold to a group of initial purchasers that included Barclays Bank PLC. Barclays and the other initial purchasers would then offer the Yosemite LEOs to investors. The Yosemite LEOs were to be sold only to non-U.S. investors pursuant to Regulation S of the Securities Act. The Yosemite LEOs were set to mature on February 23, 2007, bearing interest at 8.75% per annum until that date.

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46 10/24/06 Fastow Depo. Tr. at 519:4-19.

47 8/17/06 Tilney Depo. Tr. at 165:22-24.

48 8/17/06 Tilney Depo. Tr. at 164:19-20

49 12/7/04 Deposition Transcript of John Olson at 141:14-19.

As to the Zero Coupon Notes, the offering memorandum provided that the Zero Coupon Notes would be sold by Enron to a series of initial purchasers including Barclays Capital, who would then resell them on or about February 7, 2001. The Zero Coupon Notes were to be offered and sold in the United States only to qualified institutional buyers as defined by Rule 144A of the Securities Act and to non-U.S. buyers pursuant to Regulation S of the Securities Act. The issue price of the Zero Coupon Notes was set at $655.24, with a yield to maturity of 2.125% that would be reached on February 7, 2021.

Of course, Enron utilized Barclays' services to lend credibility to the offerings. An email between Barclays personnel concerning the Zero Coupon Notes offering states that Enron paid the bank $500,000.000 "for the privilege of having Barclays on the cover of the prospectus." Ex. 11114.

4. There Is a Triable Issue of Fact Whether the Banks' Market Activities Created a Duty to Disclose Material Information Regarding Enron's Financial Condition.

Long-settled legal principles provide that the Banks' conduct in actively promoting Enron securities to investors gave rise to a duty to disclose material information of which the Banks were aware, *i.e.*, the impact of at least their own deceptive transactions which in turn inflated the prices of Enron's securities. Indeed, that conduct gave rise to several separate and independent duties to disclose, each sufficient to trigger applicability of the *Affiliated Ute* presumption of reliance.

a. This Case Remains One Primarily of Omissions

As this Court explained earlier, under Fifth Circuit law, to determine whether a case is one "primarily" of omissions, reference is made to the Rule 10b-5 subsection under which the case arises:

> To determine whether an action is "primarily a nondisclosure case or a positive misrepresentation case" for the applicability of the *Ute* presumption or the fraud-on-the-market theory, the Fifth Circuit focuses on under which subsection of Rule 10b-5 the misconduct alleged in the pleadings falls. *Finkel v. Docutel/Olivetti Corp*., 817 F.2d 356, 359-60 (5th Cir. 1987), *cert. denied*, 485 U.S. 959, 108 S. Ct. 1220, 99 L. Ed. 2d 421 (1988). A plaintiff's claim may give rise to the *Ute*

> presumption of reliance based on material omission if it arises under Rule 10b-5(a)("to employ any device, scheme, or artifice to defraud") and/or (c)("to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security"). *Ayres*, 845 F.2d at 1363 . . . .

Enron, 529 F. Supp. 2d at 681-82.

As described above, this case concerns the Banks' ***failure to disclose the impact of the fraud on Enron's reported financial conditions***. The Banks employed a device, a practice, or course of business that operated as a fraud on potential investors. That practice included the transactions that falsified the financials, coupled with the Banks' activity in the market for Enron and Enron-related securities. Indeed, the Banks' ***knowledge*** and the ***impact*** of the deceptive transactions on Enron's financials was entirely concealed from the market until the true state of Enron's operations became known to the market as Enron began its collapse.[50] Under this theory, The Regents are not relying on any material misstatement by the Banks. Thus, under Fifth Circuit precedent, the case presented by The Regents arises under Rule 10b-5(a) and (c): "Cases involving primarily a failure to disclose implicate the first and third subsections of Rule 10b-5 . . . ." *Finkel*, 817 F.2d at 360; *see also Enron*, 529 F. Supp. 2d at 682.[51]

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[50] In *Finkel v. Docutel/Olivetti Corp.*, 817 F.2d 356, 358-63 (5th Cir. 1987), the Fifth Circuit upheld a Rule 10b-5(a) and (c) claim for a scheme to defraud or course of business operating as a fraud, applying the *Affiliated Ute* presumption of reliance, wherein the scheme involved a controlling company, Olivetti, with a 46% interest in Docutel, forcing Docutel to take worthless inventory thereby defrauding Docutel investors prior to the disclosure of the writedown for such inventories.

[51] While it is clear that this case is an omissions case, even if this Court were to find that it presented some claims for affirmative misstatement, this would ***not*** prevent application of the *Affiliated Ute* presumption because the Fifth Circuit has ruled that the case need not be exclusively of omissions, but only "primarily" so. *Regents*, 482 F.3d at 384. As this Court correctly held:

> This Court follows the literal meaning of "primarily" in *Ute*, 406 U.S. at 153 . . . ("primarily a duty to disclose"), *Finkel*, 817 F.2d at 359, and progeny and concludes a mixed context does not *per se* preclude the application of the *Ute* presumption, but does require the court to find the allegations are ***primarily*** of omissions.

As the Fifth Circuit instructed in *Abell v. Potomac Insurance Co.*, 858 F.2d 1104, 1119 (5th Cir. 1988), *vacated on other grounds sub nom., Fryar v. Abell*, 492 U.S. 914 (1989), "the *Ute* presumption is limited to cases, like *Ute* itself, in which the plaintiffs have based their complaint primarily upon alleged omissions. Such non-disclosure suits are those in which the complaint is grounded primarily in allegations that the defendant has failed to disclose any information whatsoever relating to material facts about which the defendant has a duty to the plaintiff to disclose." *Id.* That is this case. The Banks said nothing to Enron investors about the fraud as they traded in Enron stock and debt, underwrote Enron-related offerings, spoke to rating agencies and issued analyst reports to induce the purchase of Enron stock.

In *Abell* the court provided examples that highlight the distinction between misrepresentations and omissions:

> To define more vividly the distinction between misrepresentations and omissions, we suggest the following hypothetical: Suppose a car owner, wishing to sell her vehicle, advertises in the newspaper that her car has a "new" battery when she knows the battery is five years old. She has communicated an outright lie, and the basis of a fraud against her is falsehood (a category of misrepresentation). If a prospective buyer asks her, "How is the engine?", she might reply, "I've never had a problem with it." If, however, she has owned the car for only a few weeks, and knows that the previous owner had the engine rebuilt two months ago, she has distorted the truth by telling only part of it--another form of misrepresentation. ***Finally, assume the owner has decided to sell her automobile because a mechanic she knows considers the vehicle "not safe at any speed." Nonetheless, she tells this only to potential buyers who specifically ask her why she is selling the car. In this last case, the owner has omitted saying anything about a particular material matter***.

Abell v. Potomac Ins. Co., 858 F.2d 1104, 1119 n.15. This case is analogous to the final example – the Banks said nothing about the Transactions or their knowledge of the fraud. Like the car seller in

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Enron, 529 F. Supp. 2d at 682 (emphasis in original).

Abell's final example, the Banks knew Enron was not "safe at any price," but the Banks omitted this information as they sold Enron to the market for their own financial gain.

b. Under *Affiliated Ute* and the Fifth Circuit's Multi-factor Test the Banks Had a Duty to Disclose

Just as in the Supreme Court's seminal *Affiliated Ute* decision, the Banks' activities in the market – activities that included encouraging, inducing, and facilitating investors' purchase of Enron securities – created a duty to investors to disclose material information of which the Banks were aware regarding those securities. The defendants in *Affiliated Ute* were market makers and sales agents for the stock of a company holding assets for certain mixed-blood Native American plaintiffs. The defendants had also helped create a market for the stock among non-Indians in which the stock traded for higher prices. The defendants failed to notify the Native Americans about the "White" market for the stock and its higher prevailing prices. The Supreme Court held that the defendants had a duty to disclose "material facts that reasonably could have been expected to influence" the plaintiffs' trading decisions, such as the existence of the higher prevailing prices in the "White" market. That duty arose not merely from the defendants' status as transfer agent. *See Affiliated Ute*, 406 U.S. at 152 ("if [defendants] had functioned merely as a transfer agent, there would have been no duty of disclosure here"). Rather, the duty was created as a result of the defendants' market activity which encouraged, induced, and facilitated the plaintiffs' stock trades. The Court noted that defendants "'were ***active in encouraging*** a market'" for the stock (*id*.), that they "devised a plan and ***induced*** the mixed-blood holders of UDC stock to dispose of their shares," and that they "***facilitate[d]*** the mixed-bloods' sales to those seeking to profit in the non-Indian market." *Id*. at 153. Also important to the Court's duty finding was the fact that the defendants had a financial interest in the existence of an active market in the stock (*id*. at 152 (defendants "received increased deposits because of the development of this market")), and that the defendants in fact had, and were understood by plaintiffs to have, superior knowledge about the market for the stock. *Id*.

A jury could reasonably find that the Banks' market activities here establish the same duty. Like the *Affiliated Ute* defendants, the Banks "encouraged," "induced," and "facilitated" investors' purchase of Enron securities through their unrelenting "buy" recommendations and their underwriting activities. Like the *Affiliated Ute* defendants, the Banks had superior knowledge about the true value of those securities as a result of their participation in the Transactions. Like the *Affiliated Ute* defendants, the Banks, through their supposedly expert analysts and their position as underwriters, invited the investing public to rely on their superior knowledge. Indeed, the Banks did the defendants in *Affiliated Ute* one better: as the Supreme Court held there, "[i]t is no answer to urge that, as to some of the petitioners, these defendants may have made no positive representation or recommendation." *Id*. at 153. Yet here the Banks ***did*** make positive recommendations, repeatedly recommending that investors "buy" Enron securities. Those recommendations alone, coming from sophisticated financial institutions with superior knowledge about Enron, gave investors a right to know that the Banks making them had engaged in transactions that profited the Banks and manipulated the price of Enron's securities by misrepresenting its financial results. *See id*. ("The sellers had the right to know that the defendants were in a position to gain financially from their sales and that their shares were selling for a higher price in that market.").

In *First Virginia Bankshares*, the Fifth Circuit established a multi-factor test for determining whether a duty to disclose exists under Rule 10b-5:

> In determining whether the duty to speak arises, we consider the [(1)] relationship between the plaintiff and defendant, [(2)] the parties' relative access to the information to be disclosed, [(3)] the benefit derived by the defendant from the purchase or sale, [(4)] defendant's awareness of plaintiff's reliance on defendant in making its investment decisions, and [(5)] defendant's role in initiating the purchase or sale. *See White v. Abrams*, 495 F.2d 724, 735 (9[th] Cir. 1974) and cases cited therein.

559 F.2d at 1314. The *First Virginia Bankshares* multi-factor test remains well-rooted in Fifth Circuit jurisprudence, and the Fifth Circuit has repeatedly turned to the test to determine the

existence of a duty to disclose. *See Kaplan v. Utilicorp United*, 9 F.3d 405, 407-408 (5th Cir. 1993); *Abbott v. Equity Group*, 2 F.3d 613 (5th Cir. 1993) (applying the factors and noting usage of the test in other Circuits).[52]

First Virginia Bankshares involved the acquisition of finance company Benson by First Virginia. For years defendant Heller, a large financing firm,[53] had served as Benson's principal financier, extending loans to it secured by Benson's notes receivable. Pursuant to this relationship, Heller conducted regular audits of Benson, which at one point revealed that Benson was falsifying its reported financial condition. First Virginia, unaware of Benson's manipulations, set about to acquire Benson. It engaged the services of a broker, Michelman, who contacted Heller for information. During the contact, Heller did not disclose to Michelman its knowledge of Benson's fraud. Moreover, Heller did not disclose additional knowledge of the fraud it gained after speaking with the broker.[54] The Fifth Circuit held that Heller had a duty to disclose its knowledge of the fraud under Rule 10b-5:

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[52] *See Abbott*, 2 F.3d at 622 ("We thus refrain from specifically defining the disclosure obligations of a surety and its agent; rather, applying relevant factors annunciated by our court in *First Virginia Bankshares v. Benson*, 559 F.2d 1307 (5th Cir. 1977), *cert. denied*, *Walter E. Heller & Co. v. First Virginia Bankshares*, 435 U.S. 952 . . . (1978), and applied by other circuits, *see Arthur Young & Co. v. Reves*, 937 F.2d 1310, 1330 (8th Cir. 1991), *cert. denied*, *Reves v. Ernst & Young*, . . . 112 S. Ct. 1165 . . . (1992); *Jett v. Sunderman*, 840 F.2d 1487, 1493 (9th Cir. 1988); *Rudolph v. Arthur Andersen & Co.*, 800 F.2d 1040, 1043 (11th Cir. 1986), *cert. denied*, 480 U.S. 946 . . . (1987) . . . ."). *See also Camp v. Dema*, 948 F.2d 455, 460 (8th Cir. 1991) (applying same test).

[53] Founded in 1919, Walter E. Heller & Co. was a giant asset-based lender. Before it was sold to G.E. Capital for over $5 billion in 2001, Heller had been for many years the largest independent commercial finance firm in the United States. *See The Man Who Likes Risk*, Time, Feb. 15, 1960 (Ex. 32); Kenneth Gilpin, *G.E. Finance Unit Will Acquire Heller Financial for $5.3 Billion*, N.Y. Times, July 31, 2001, at C6 (Ex. 33).

[54] First Virginia asserted that Heller was motivated to refrain from making disclosures because a successful purchase of Benson by First Virginia would ensure Heller's loans extended to Benson would be repaid.

> Heller had much to gain by encouraging the sale of the Bensons' company because it has more than $3,000,000 at risk in Benson debt that was secured by accounts which were tainted with poor or dishonest accounting, and the Benson operation was losing money rapidly. The jury could find that acquisition by another company would relieve Heller of risk to its $3,000,000. Also, through its May 1972 examination of the Bensons' company, Heller obtained information strongly indicating gross inaccuracy in the Bensons' books. This information was not known to any potential purchaser and was designed by the Bensons not to be discovered. As matters stood, Heller had ***superior knowledge of inside information***. On the basis of this information, ***the jury could find*** that Heller had a duty to disclose to Michelman the information uncovered by the May 1972 examination.

First Virginia Bankshares, 559 F.2d at 1317.

In similar fashion, applying the *First Virginia Bankshares* factors to the evidence in this case, "the jury could find that" the Banks owed investors a duty to disclose material information regarding Enron's true financial condition. As to the "relationship between the plaintiff and defendant" (*id*. at 1314), the Banks provided financing to Enron just as Heller did to Benson. As a result of that activity and the transactions, the Banks had knowledge of Enron's fraudulent operations. The Banks held themselves out as being in a unique position to judge the value of Enron's securities for investors. Merrill and CSFB issued analyst reports concerning Enron, which purported to offer an unbiased, independent valuation of the securities, for the benefit of the investing public. All of the Banks either underwrote the issuance of Enron securities and/or brought Enron and Enron-related securities to market – thus vouching for the purported quality of these securities.[55] In this manner, these Banks purported ***to advise the investing public*** on the quality and pricing of Enron's securities. Indeed, the relationship between the Banks and the investing public in this case is indistinguishable

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[55] *See Chris-Craft Indus. v. Piper Aircraft Corp.*, 480 F.2d 341, 370 (2d Cir. 1973) ("The investing public properly relies upon the underwriter to check . . . the ***soundness*** of the offer . . . ."). As indicated above, the Banks basically sold to Enron their imprimatur on the Company's securities. *See* Ex. 11114 (email between Barclays personnel concerning the Zero Coupon Notes offering states that Enron paid the bank $500,000.000 "[f]or the privilege of having Barclays on the cover of the prospectus"); Ex. 15648 (CSFB analyst email stating that "***[Enron] needed us to publicly sell the stock*** almost as much as we needed them for the fees.").

from the relationship between Heller and First Virginia. The jury could reasonably find that this amounts to a substantial relationship between the parties which militates in favor of finding a duty to disclose.[56]

Regarding "the parties' relative access to the information to be disclosed" (*First Virginia Bankshares*, 559 F.2d at 1314), the jury could surely find that the Banks had "superior knowledge of inside information" (*id*. at 1317) concerning Enron's reported financial condition. Again, The Regents, in its oppositions to the Banks' motions for summary judgment, exhaustively details the Banks' knowledge of the fraudulent effects of the Transactions on Enron's reported financial condition. Thus, this factor heavily weighs in favor of a jury finding a duty to disclose.[57]

As to "the benefit derived by the defendant from the purchase or sale" (*First Virginia Bankshares*, 559 F.2d at 1314), the evidence would allow a reasonable jury to find that the Banks had a tremendous financial interest in the continuing marketability of Enron securities at favorable prices. As The Regents detail in the oppositions to the Banks' motions for summary judgment, Enron was an extremely profitable client for the Banks – the Banks earned lucrative fees from Enron for structured-finance transactions, the provision of credit, and the marketing of Enron securities. The record in this case is replete with the Banks' admissions that Enron was a critical relationship for them. Also, like Heller in *First Virginia Bankshares*, the Banks had significant credit exposure to Enron.

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[56] *See Steadman v. SEC*, 603 F.2d 1126, 1129 (5th Cir. 1979), *aff'd* 450 U.S. 91 (1981) (mutual fund advisor held to have had duty to disclose material information to fund).

[57] Notably, this factor appears to have been near definitive in *First Virginia Bankshares* itself, as the parties did not have a substantial relationship, and the Fifth Circuit highlighted Heller's "superior knowledge of inside information" (559 F.2d at 1317). *See also Woodward v. Metro Bank of Dallas*, 522 F.2d 84, 97 n.28 (5th Cir. 1975) ("A duty of disclosure may exist where ***any*** person possesses ***inside information*** . . . .").

These facts could lead a jury to conclude that the Banks had a major interest in seeing investors continue to purchase Enron securities. Indeed, the jury could find that without such purchases at favorable prices, the Company would have collapsed years before it did in late 2001. A collapse of Enron would, of course, not only have ended the flow of rich fees from the Company to the Banks, but would have also jeopardized repayment of the credit the Banks had extended to Enron (as with Heller in *First Virginia Bankshares*). Because the Banks derived a benefit from investors' purchases of Enron securities, the jury could conclude that this factor too militates in favor of finding a duty to disclose.

The jury could also reasonably find that "defendant's awareness of plaintiff's reliance on defendant in making its investment decisions" (*First Virginia Bankshares*, 559 F.2d at 1314) was present here. Again, CSFB knew that Enron needed prestigious investment banks to recommend its securities specifically because investors relied on such recommendations. *See* Ex. 15648 ("[Enron] needed us to publicly sell the stock"). Merrill of course had a similar understanding, as it witnessed (and acquiesced in) Enron's insistence that Merrill analysts give favorable coverage on Enron's securities. Merrill knew that this was only because such analyst coverage yields powerful influence on the investing public. Extensive evidence would support a jury's conclusion to this effect; the SEC observes that:

> Research analysts study publicly traded companies and make recommendations on the securities of those companies . . . . They exert ***considerable influence*** in today's marketplace. Analysts' recommendations or reports can influence the price of a company's stock – especially when the recommendations are widely disseminated through television appearances or through other electronic and print media . . . .
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> * * *
>
> [A]nalysts provide an important source of information in today's markets.

Analyzing Analyst Recommendations, dated April 20, 2005 (Ex. 34). And as one court put it:

> Research analysts who study publicly traded companies and make recommendations on the securities of those companies exert considerable influence in the marketplace. The reports and/or recommendations of such analysts can influence the price of a company's stock even when nothing about the company's prospects or fundamentals have changed.

La Grasta v. First Union Sec., Inc., 358 F.3d 840, 842 (11th Cir. 2004).

Moreover, a jury could find that these two Banks (and Barclays also) of course understood that they were paid rich fees from Enron to underwrite and otherwise market Enron and Enron-related securities ***specifically because investors relied*** on the Banks' reputation as an indication of the securities' basic soundness.[58] This factor as well thus favors finding a duty to disclose.

Finally, the "defendant's role in initiating the purchase or sale," while identified by the court as a factor to be considered in evaluating the existence of a disclosure duty, played no role in the outcome of *First Virginia Bankshares*. 559 F.2d at 1314. Heller did absolutely nothing to initiate First Virginia's purchase of Benson. In *Abbott*, 2 F.3d at 621, the Fifth Circuit identified the Eighth Circuit case of *Arthur Young & Co. v. Reves*, 937 F.2d 1310 (8th Cir. 1991), as applying the Fifth Circuit's multi-factor test. In the *Arthur Young* case, the court found a duty to disclose even though the initiating factor was not satisfied. *See id*. at 1331. Yet, in this case a jury could find that the Banks ***did*** play a role in initiating the purchase of the securities through analyst reports, and Enron and Enron-related securities brought to market through underwritings or otherwise. The situation here is more analogous to the situation in *Affiliated Ute* where the Court found the defendants' activities ***induced*** the purchase and sale of the stock at issue. 406 U.S. at 153.

Given application of the *First Virginia Bankshares* factors, a jury could easily find that the Banks had a duty to disclose their "superior knowledge" (*First Virginia Bankshares*, 559 F.2d at

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[58] *See* Ex. 11114 (An email between Barclays personnel concerning the Zero Coupon Notes offering states that Enron paid the bank $500,000.000 "[f]or the privilege of having Barclays on the cover of the prospectus.").

1317) that Enron's reported financial condition was falsified generally and by the Transactions in particular. These Banks had far more contact with the aggrieved parties, and were much more involved in the fraud, than was Heller in *First Virginia Bankshares*.

c. Duty to Disclose or Abstain

It is well-established that an "insider," such as a corporate officer, who possesses material non-public information about the company is subject to a duty to "disclose or abstain" – *i.e.*, either disseminate the information to the investing public before trading in the company's securities or refrain from trading until the information has been publicized. *See, e.g., Chiarella v. United States,* 445 U.S. 222, 227, 229 (1980).

The Fifth Circuit has recognized this duty to disclose or abstain. In *Stier v. Smith*, 473 F.2d 1205 (5th Cir. 1973), the court held of an insider defendant who sold stock to the plaintiff: "What is clear, however, is that the defendant in a case like the one at hand has an affirmative duty to disclose information to which he has ready access and his plaintiff does not." 473 F.2d at 1208 n.9. *See also SEC v. Fox*, 855 F.2d 247, 252 (5th Cir. 1988) ("Rule 10b-5 imposes a duty to disclose, or abstain from trading on the basis of non-public material corporate information.").[59] This duty to disclose while trading emanates from: "'[A] relationship of trust and confidence [that exists] between the shareholders of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation.'" *United States v. O'Hagan*, 521 U.S. 642, 652 (1997).

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[59] *And see Kurtzman v. Compaq Computer Corp.*, No. H-99-779, 2000 U.S. Dist. LEXIS 22476, at *77 (S.D. Tex. Dec. 12, 2000) ("Courts have recognized that a duty to disclose material facts arises when . . . a corporate insider trades securities . . . .").

But not only corporate officers can acquire the status of "insider" and its concomitant duty to disclose. Others who obtain corporate information from the company may as well. As the Supreme Court has further held:

> Under certain circumstances, such as where corporate information is revealed legitimately to an ***underwriter***, accountant, lawyer, or ***consultant*** working for the corporation, these ***outsiders*** may become ***fiduciaries of the shareholders***. The basis for recognizing this fiduciary duty is not simply that such persons acquired nonpublic corporate information, but rather that they have entered into a special confidential relationship in the conduct of the business of the enterprise and are given access to information solely for corporate purposes.

Dirks v. SEC, 463 U.S. 646, 655 n.14 (1983).

Here the Banks engaged in extensive investment banking activities with Enron, gained knowledge of the fraud, and were counterparties to the equity swaps and forward trades. As myriad other courts have made clear, an insider "in possession of material inside information must either disclose it to the investing public, or, if he is disabled from disclosing it in order to protect a corporate confidence, or he chooses not to do so, ***must abstain from trading*** in ***or recommending the securities concerned*** while such inside information remains undisclosed." *SEC v. Tex. Gulf Sulphur Co.*, 401 F.2d 833, 848 (2d Cir. 1968) (en banc), *cert. denied sub nom. Coates v. SEC*, 394 U.S. 976 (1969); *accord Castellano v. Young & Rubicam, Inc.*, 257 F.3d 171, 179 (2d Cir. 2001); *SEC v. Platt*, 565 F. Supp. 1244, 1252 (W.D. Okla. 1983); *Bruce v. Rosenberg*, 463 F. Supp. 673, 675 (E.D. Wis. 1979); *Fridrich v. Bradford*, No. 7002, 1974 U.S. Dist. LEXIS 8066, at *36 (M.D. Tenn. June 17, 1974).[60] This Court has similarly recognized: "A corporate insider with material inside information is required to disclose it to the investing public or, if he cannot . . . ***he must***

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[60] At least one court calls the notion "black letter law": *United States v. Lang*, 766 F. Supp. 389, 399 (D. Md. 1991) ("Since [*Texas Gulf Sulphur*], it has been ***black letter law*** that" corporate insiders with undisclosed information cannot either trade in, or recommend, the securities concerned.).

abstain from trading in ***or recommending securities concerned*** while that inside information remains undisclosed." *Kurtzman*, 2000 U.S. Dist. LEXIS 22476, at *80 n.32.

The Banks here were under an obligation to disclose their knowledge of the fraud or abstain from trading in Enron's securities. They did neither. Specifically, Enron's investment bankers having engaged in and learned of the fraud undertook certain equity transactions at Enron's request. These transactions known as equity swaps or equity forwards are unique because it is the only type of swap or forward where an issuer, in this case Enron, can directly impact the underlying index. In this case, at several junctures during the Class Period, Enron requested certain banks – at least CSFB and Merrill – to go into the marketplace on a given day or timeframe and purchase Enron stock. Enron would then guarantee repayment of the cost of purchasing these shares – the market price – one year hence plus commissions and interest on the amount paid by the Banks.

These transactions impacted Enron's common stock in that the purchases increased share volume and artificially supported the price of Enron stock. As a result, the market as a whole was impacted and the Banks made no disclosure at the time of this market activity of their knowledge of the fraud. A trier of fact could easily find that this independent duty alone satisfies the *Affiliated Ute*'s duty requirement and gives rise to a presumption of classwide reliance.

In addition to the above, several courts have held that underwriters attain the status of an "insider," and thus are subject to the abstain-or-disclose duty:

> After *Dirks*, corporate insiders, such as directors and managers, and so-called temporary insiders, such as ***underwriters***, accountants, lawyers, or consultants working for a corporation, are under a duty to ***disclose or abstain***, as are tippees of either group. *Dirks*, 463 U.S. at 655 n.14, 659-61.

United States v. Bryan, 58 F.3d 933, 953 (4th Cir. 1995), overruled on other grounds.

> Allocating Underwriters were under a duty to disclose under yet another analysis: Where an insider trades in securities, it is well-settled that she is under a duty to disclose all material information. *See Chiarella*, 445 U.S. at 230. An "insider" includes "[the corporation's] agent, . . . a fiduciary, [or] . . . a person in whom the sellers [of the securities] had placed their trust and confidence." *Dirks v. SEC*, 463

> U.S. 646, 654, 77 L. Ed. 2d 911, 103 S. Ct. 3255 (1983) (alterations in original) (quoting *Chiarella*, 445 U.S. at 232). Because Allocating Underwriters certainly fall into the latter category, and because they are alleged to have sold the securities, they were under a duty to disclose.

In re Initial Pub. Offering Sec. Litig., 241 F. Supp. 2d 281, 384 n.157 (S.D.N.Y. 2003).

In acting as underwriters and choosing to trade in Enron securities, the Banks were subject to this duty to abstain from trading or disclose that Enron's reported financial condition was falsified by the Transactions. A review of just a few of the offering documents reveals the status of the Banks as underwriters and market makers in the securities:

- A Prospectus Supplement for the offering of $250,000,000 in Enron Floating Rate Notes Due March 30, 2000 (filed 9/28/98), states that "Enron has agreed to sell to" *et al.*, ***Merrill***, identified as an "'[u]nderwriter,'" and that "Enron has been advised by the Underwriters that the Underwriters intend to make a market in the Notes." Ex. 35 at 12.

- A Prospectus Supplement for the offering of $250,000,000 in Enron 6.95% Notes Due July 15, 2028 (filed 11/25/98) states that "we [*i.e.*, Enron] have agreed to sell to ***Credit Suisse First Boston Corporation*** (the 'Underwriter'), and the Underwriter has agreed to purchase, the entire principal amount of the notes. . . . The Underwriter proposes initially to offer the notes to the public . . . ." Ex. 36 at 7-8. The same document also states that: "If underwriters are used in the sale, the Offered Securities will be acquired by the underwriters for their own account and may be resold from time to time in one or more transactions . . . ." *Id*. at 33.

- A Prospectus Supplement for the offering of 12,000,000 shares of Enron common stock (filed 2/12/99) states that "we [*i.e.*, Enron] have agreed to sell to" underwriters ***CSFB*** and ***Merrill*** each 1,500,000 shares of common stock, and that "[t]he underwriters propose to offer the shares of common stock initially at the public offering price." Ex. 37 at 12.

- The Osprey Trust/Osprey I, Inc., Offering Memorandum for $1,400,000,000 Senior Secured Notes due 2003, filed September 16, 1999, identifies ***DLJ*** as one of the "Initial Purchasers" (Ex. 38 at E87909) and states that the "Initial Purchasers have agreed severally to purchase from the Issuers, and the Issuers have agreed to sell to the Initial Purchasers" the Notes. *Id*. at E87986. It also states that "[t]he Initial Purchasers propose to offer the . . . Notes for resale in transactions." *Id*.

- A 2/15/00 Supplement for an Offering Memorandum for the Yosemite LEOs identifies ***Barclays*** as one of the "Initial Purchasers," and states that "[t]he Initial Purchasers will agree to purchase the Notes from the Company. The Notes will be offered by the Initial Purchasers . . . ." Ex. 31 at i.

- The Osprey Trust/Osprey I, Inc., Offering Memorandum for $750,000,000 7.797% Senior Secured Notes due 2003 and €315,000,000 6.375% Senior Secured Notes due 2003 (filed 9/28/00), identifies ***DLJ*** and ***CSFB*** as "Initial Purchasers" (*see* Ex. 39 at 1), and states that "the Initial Purchasers have agreed severally to purchase from the Issuers, and the Issuers have agreed to

sell to the Initial Purchasers" the securities, and that "[t]he Initial Purchasers propose to offer the New Senior Notes for resale in transactions." *Id*. at 88.

- A January 31, 2001, Offering Memorandum for the Zero Coupon Notes identifies ***Barclays*** Capital, Inc. as an "Initial Purchaser" and states that these "have severally agreed to purchase, and we have agreed to sell to the initial purchasers, the notes" (Ex. 30 at 45), and that "[t]he initial purchasers are offering the notes." *Id*. at 1.

- A July 12, 2001, Offering Memorandum for Marlin Water Trust II/Marlin Water Capital Corp. II $475,000,000 6.31% Senior Secured Notes due 2003 and €515,000,000 6.19% Senior Secured Notes due 2003 identifies ***CSFB*** as one of the two "Initial Purchasers," and states that the "Initial Purchasers have agreed severally to purchase from the Issuers, and the Issuers have agreed to sell to the Initial Purchasers," the Notes. Ex. 40 at 107. It also states that "[t]he Initial Purchasers propose to offer the Senior Notes for resale in transactions." *Id*.

d. Underwriter's Duty to Disclose

A separate and independent duty of disclosure which devolved on the Banks was that created solely by their underwriting of Enron securities. As indicated, all three Banks performed such underwritings.

Issuers use underwriters in part because they lend their credibility to the offering. As such, it is reasonable for the investing public to assume that underwriters will make full disclosure of any adverse facts:

> An underwriter by participating in an offering constructively represents that statements made in the registration materials are complete and accurate. The investing public properly relies upon the underwriter to check the accuracy of the statements and the ***soundness*** of the offer; ***when the underwriter does not speak out, the investor reasonably assumes that there are no undisclosed material deficiencies***. The representations in the registration statement are those of the underwriter as much as they are those of the issuer.

Chris-Craft Indus., 480 F.2d at 370.[61]

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[61] And as this Court has held, the law imposes on underwriters an investigative duty because "its role is critical to the integrity of the market and the confidence of the investing public." *In re Enron Corp. Sec. Litig.*, 235 F. Supp. 2d 549, 612 (S.D. Tex. 2002). "'[T]he relationship between the underwriter and its customers implicitly involves a ***favorable recommendation*** of the issued security. Because the public relies on the integrity, independence and expertise of the underwriter, the underwriter's participation ***significantly enhances the marketability*** of the security.'" *Id*. (quoting *Sanders v. John Nuveen & Co.*, 524 F.2d 1064, 1070 (7th Cir. 1975)).

For this reason, both the SEC and the courts recognize that underwriters assume a heightened duty to disclose material information:

> An underwriter "occupies a vital position" in a securities offering because ***investors rely*** on its reputation, integrity, independence, and expertise. *Municipal Securities Disclosure*, Exchange Act Release No. 26,100, 41 SEC Docket 1131 (Sept. 22, 1988), 1988 WL 999989, at *6, *20-21. "By participating in an offering, an underwriter makes an implied recommendation about the securities [that it] . . . has a reasonable basis for belief in the truthfulness and ***completeness*** of the key representations made in any disclosure documents used in the offerings." *Id*. at *20 (emphasis added); *see, e.g.*, *Hanly v. SEC*, 415 F.2d 589, 596 (2d Cir. 1969) ("A securities dealer occupies a special relationship to a buyer of securities in that by his position he implicitly represents he has an adequate basis for the opinions he renders."); *Disclosure Obligations*, 1994 WL 73628, at *17.
>
> An underwriter ***must investigate and disclose*** material facts that are known or "reasonably ascertainable." *Municipal Securities Disclosure*, 1988 WL 999989, at *20 (quoting *Hanly*, 415 F.2d at 597); *cf. SEC v. Dain Rauscher, Inc.*, 254 F.3d 852, 858 (9th Cir. 2001) (holding an underwriter "had a duty to make an investigation that would provide him with a reasonable basis for a belief that the key representations in the statements . . . were truthful and complete"). Although other broker-dealers may have the same responsibilities in certain contexts, ***underwriters have a "heightened obligation" to ensure adequate disclosure***. *Municipal Securities Disclosure*, 1988 WL 999989, at *21 & n.74.

Dolphin & Bradbury, Inc. v. SEC, 512 F.3d 634, 641-642 (D.C. Cir. 2008).[62] As was held in another case: "As an underwriter, Ratliff was under a duty to the investing public to make a reasonable investigation of the issuer of the bonds and to ***disclose material facts*** that he knew or that were readily ascertainable." *Shores v. M.E. Ratliff Inv. Co.*, No. CA 77-G-0604-S, 1982 U.S. Dist. LEXIS 10653, at *7 (N.D. Ala. Jan. 18, 1982).

Likewise, this Court has recognized that underwriters are liable for omissions:

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[62] *See also Kurtzman*, 2000 U.S. Dist. LEXIS 22476 ("the affirmative duty to disclose is heightened in the context of an offering") (citing *Herman & MacLean*, 459 U.S. at 381-82; *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 195 (1976)). As indicated, the *Dolphin* court found the discussion of the role of securities dealers in *Hanly v. SEC*, 415 F.2d 589 (2d Cir. 1969), applicable to underwriters. *Hanly* states of the duties of such dealers: "In summary, the standards by which the actions of each petitioner must be judged are strict. He cannot recommend a security unless there is an adequate and reasonable basis for such recommendation. ***He must disclose facts*** which he knows and those which are reasonably ascertainable." *Id*. at 597.

> An underwriter of a public offering risks exposure to such liability under §11, ***as well as to liability under §10(b)*** for any material misstatements ***or omissions*** in the registration statement made with scienter, and thus has a duty to investigate an issuer and the securities that the underwriter offers to investors.

Enron, 235 F. Supp. 2d at 612. The Court further recognized that underwriters occupy a position of "confidence and trust" in relationship to shareholders:

> Because an underwriter has access to information not generally available to the public and because the public relies on the expertise, integrity, and independent analysis of the underwriter, ***there is a relationship of confidence and trust with the investing public, and the underwriter is charged with a high standard of professional conduct*** and reasonable investigatory responsibility.

February 18, 2005 Memorandum and Order (Docket No. 30 in Case No. H-03-4359) at 24. The Fifth Circuit has held that a position of "trust" creates a duty to disclose. *See Fox*, 855 F.2d at 252 (duty to disclose arises from "a position of trust").[63]

In addition to this general duty of disclosure, Item 508(l)(1) of Regulation S-K (17 C.F.R. §229.508(l)(1)) requires that underwriters of securities disclose "any transaction that the underwriter intends to conduct during the offering that stabilizes, maintains, or ***otherwise affects the market price of the offered securities***." Virtually all of the Transactions were calculated to permit Enron to fraudulently maintain its positive credit rating – and this rating affected the market price of all of Enron's securities. Because Item 508(l)(1) thus required disclosure of the Transactions, this rule furnishes a duty to disclose that is actionable under Rule 10b-5. *See Woodward*, 522 F.2d at 97 ("A

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[63] *See also Schatz v. Rosenberg*, 943 F.2d 485, 490 (4th Cir. 1991) ("The Supreme Court has decreed that under the federal securities laws, a duty to disclose 'arises from the relationship between parties,' *Dirks*, 463 U.S. at 658, . . . and will exist if there is 'a fiduciary or other similar relation of trust and confidence between them.' *Chiarella*, 445 U.S. at 228."). In *Anixter v. Home-Stake Prod. Co.*, 77 F.3d 1215, 1227 (10th Cir. 1996), the Tenth Circuit observed that a "duty to disclose" arises "'"because of a fiduciary or other similar relation of trust and confidence between [parties]."'" (quoting *Windon Third Oil & Gas Drilling P'ship. v. FDIC*, 805 F.2d 342 (10th Cir. 1986)); *Camp*, 948 F.2d at 460 ("'Under the federal securities laws, a duty to disclose "arises from the relationship between parties," and will exist if there is "a fiduciary or other similar relation of trust and confidence between them."'").

duty of disclosure may exist where . . . the law imposes special obligations, as for accountants, brokers, or other experts, depending on the circumstances of the case. This list, however, is not intended to be exhaustive."); *Kunzweiler v. Zero.net, Inc.*, No. 3:00-CV-2553-P, 2002 U.S. Dist. LEXIS 12080, at *31-*32 (N.D. Tex. Jul. 3, 2002) ("courts have held that an affirmative duty to disclose does arise when . . . a statute or regulation requires disclosure"); *Kurtzman*, 2000 U.S. Dist. LEXIS 22476, at *78 ("Courts have recognized that a duty to disclose material facts arises when . . . a statute or regulation requires such disclosure.").

C. The Remaining Elements of a §10(b) Cause of Action Are Satisfied

The remaining elements of The Regents' §10(b) cause of action are discussed in detail, with supporting evidence, in The Regents' oppositions to defendants' motions for summary judgment. Thus, these elements will only be addressed summarily below in the context of The Regents' alternative theory of liability. Because the case remains one primarily based on omissions, the elements of scienter, materiality, "in connection with," and loss causation are virtually the same as previously briefed.

1. The Banks Acted with Scienter

Scienter encompasses "'a mental state embracing intent to deceive, manipulate, or defraud.'" *Nathenson v. Zonagen*, 267 F.3d 400, 408 (5th Cir. 2001). But:

> Strict intentional misconduct is ***not*** required to show scienter, it is sufficient to prove conduct that is an extreme departure from the standards of ordinary care and presents a danger of misleading buyers or sellers, as well as either ***knowledge of that danger***, or a danger so obvious that the actor ***must be aware of it***.

Trust Co. v. N.N.P. Inc., 104 F.3d 1478, 1490 (5th Cir. 1997). This is often formulated as a standard of "severe recklessness." *Nathenson*, 267 F.3d at 408. Thus, in order to establish the Banks' scienter, it is sufficient to demonstrate simply that CSFB, Merrill and Barclays knew, or were severely reckless in not knowing, that failure to disclose their knowledge of the fraud presented a

danger of misleading Enron's investors. How could they not? The Banks knew that earnings, cash flows, and debt were severely distorted as reported by Enron due to the Banks' transactions.

It must be noted that the fact-specific nature of the scienter inquiry renders it normally inappropriate for resolution on a motion for summary judgment: "Scienter is an inherently fact-specific issue that should ordinarily be left to the trier of fact." *In re Zonagen Sec. Litig.*, 322 F. Supp. 2d 764, 774 (S.D. Tex. 2003).[64] Thus if The Regents' evidence establishes a genuine issue of fact as to the Banks' scienter (which it does), this Court should submit it to the jury.

This Court is aware that in *Southland Sec. Corp. v. INSpire Ins. Solutions Inc.*, 365 F.3d 353, 366 (5th Cir. 2004), the Fifth Circuit ruled that:

> For purposes of determining whether a ***statement*** made by the corporation was made by it with the requisite Rule 10(b) scienter we believe it appropriate to look to the ***state of mind of the individual corporate official or officials who make or issue the statement*** (or order or approve it or its making or issuance, or who furnish information or language for inclusion therein, or the like) rather than generally to the collective knowledge of all the corporation's officers and employees acquired in the course of their employment.

Id. at 366. But, as explained above, this case does not concern affirmative statements by the Banks, but instead focuses on omissions. Thus, there is no speaker whose state of mind can be examined for scienter. As such, the proper scienter inquiry here should focus on whether relevant individuals at the Banks had knowledge that the Banks were engaging in the deceptive Transactions, that the Transactions distorted Enron's financials in a material manner, that the Banks were active in the

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[64] *See also Makor Issues & Rights, Ltd. v. Tellabs, Inc.*, 437 F.3d 588, 602 (7th Cir. 2006) ("'Scienter is normally a factual question to be decided by a jury . . . .'"); *In re Cerner Corp. Sec. Litig.*, 425 F.3d 1079, 1084-85 (8th Cir. 2005) (same quote); *Press v. Chemical Inv. Servs. Corp.*, 166 F.3d 529, 538 (2d Cir. 1999) ("'Whether a given intent existed is generally a question of fact,' appropriate for resolution by the trier of fact."); *Provenz v. Miller*, 102 F.3d 1478, 1489-90 (9th Cir. 1996) ("Generally, scienter should ***not*** be resolved by summary judgment.") (emphasis in original).

market for Enron securities, and that no disclosure of the fraud was made. As detailed above, such scienter is present in this case.

Further, *Southland* recognized that a corporation making a statement acts with scienter where an employee who furnished the "information or language for inclusion therein or ***omission therefrom***" had scienter. *Southland*, 365 F.3d at 367. *See Makor Issues & Rights, Ltd. v. Tellabs, Inc.*, 513 F.3d 702, 708 (7th Cir. 2008) ("The court in the *Southland Securities* case said that corporate scienter could be based on the state of mind of someone who furnished false information that became the basis of a fraudulent public announcement. Suppose he had knowingly supplied the false information intending to help the company. His superiors would not be liable for failing to catch the mistake, but *Southland* implies that the corporation would be liable, just as it would be in a common law tort suit."). Here, in the omissions context, The Regents have established that knowledge of the material facts omitted resided in those at senior levels in each bank.

a. CSFB – Scienter

In the CSFB Opposition, Lead Plaintiff details that CSFB bankers understood that the Transactions operated to falsify Enron's reported financial condition. *See* CSFB Opp. at 186-210. And as mentioned above, CSFB marketed securities from several of the Transactions, *i.e.*, Osprey, Marlin, Firefly, and Iguana. The bankers on these Transactions knew that the securities for them were being marketed by their own bank, as such marketing was part of the deal's execution. Further, CSFB bankers also directly participated in some of the bank's activities in the market for Enron's securities. It was CSFB bankers who worked to "recraft the [E]nron story" for the Company's road show presentations. Ex. 21303; 1/6/05 Capolongo Depo. Tr. at 367:18-369:19. And bankers Larry Nath and Dwight Scott (then of DLJ) were involved in preparing the road show presentation for the certificates of the Marlin transaction. *See* 1/13/05 Nath Depo. Tr. at 448:19-449:16. Nath, while at CSFB, discussed some of Enron's structured-finance transactions with a representative from

Standard & Poor's. 9/21/05 Shipman Depo. Tr. at 354:25-356:5. Nath also made a presentation to Standard & Poor's regarding the Osprey transaction. 9/22/05 Shipman Depo. Tr. at 622:21-623:10.

Also, the CSFB Opposition presents a large body of evidence establishing that the bank was motivated to engage in the fraudulent Transactions with the Company especially because CSFB earned a large amount of money in fees from such things as offerings for Enron. *See, e.g.*, CSFB Opp. at 190-92. Thus, these bankers of course were aware that CSFB was bringing Enron securities to market.

CSFB Managing Director Osmar Abib was the bank's relationship manager for Enron during part of the Class Period. As a "coverage team leader," Abib testified he spent "most" of his time at CSFB "trying to understand what my colleagues were doing on behalf of Enron in terms of various products and services that we might – might be – might have been providing to them at that time." 6/16/04 Deposition Transcript of Osmar Abib ("6/16/04 Abib Depo. Tr."), at 57:25-58:9. Abib attended meetings with senior Enron management "[f]rom time to time" during which senior Enron executives informed Abib about Enron's financing needs. 6/16/04 Abib Depo. Tr. at 59:8-20. And in his self-evaluations, Abib himself would write that the Enron relationship required "a considerable amount of focus and coordination internally at CSFB, in addition to a tremendous amount of time spent with the client." Ex. 10166 (Abib's self-evaluation form).

Abib communicated to both his superiors and his subordinates the importance of the Enron relationship. For example, in response to the question, "why are prospects for future investment banking business enhanced" by CSFB consummating the fraudulent Nile transaction, Abib wrote:

> Enron is a firmwide CSFB priority and CSFB is viewed by Enron as a Tier 1 relationship bank. The provision of credit by CSFB is viewed extremely important by Enron in order for CSFB to maintain its Tier 1 status. As a result, Enron fully expects our support in this transaction.

Ex. 13128A at CSFBLLC005019431.

As an informed relationship manager who regularly met with Enron's senior executives and viewed Enron as a "firmwide CSFB priority," Abib knew CSFB issued analyst reports on the Company and brought its securities to market.[65] Abib was among other high-ranking persons at CSFB, such as Robert Furst, Abib's predecessor, who "aggressively solicited Enron's business." Fastow Decl., ¶47. Abib also knew Enron's reported financial condition was falsified through the Transactions. Abib received an email stating that: "As you probably know, Osprey is a vehicle enabling Enron to raise ***disguised*** debt which ***appears*** as equity on Enron's balance sheet. . . . Osprey serves the added purpose for Enron of being an off-balance-sheet ***parking lot*** for certain assets." CSFB Opp. at 153. Abib, among others, served as a purported "'director'" of an entity in the LJM 1 Rhythms Hedge transactions to give the entity the false appearance of not being a shell. *See id*. at 53-55. Abib was informed that CSFB's 2000 and 2001 prepays were really just a "loan" to the Company. *Id*. at 93. And Abib submitted a New Bank Opportunities Form for Nile, identifying the deal as a "loan." *Id*. at 117. Abib also knew that CSFB traded Enron stock in the equity swaps and forwards, which were also referred to as "Enron Own-Share Trades." *See* Ex. 11303 (email from Abib to Ogunlesi, dated September 17, 2001). Thus, Abib knew about the Transactions, knew the bank issued positive analyst reports on the Company, and knew that CSFB traded in Enron stock through the equity swaps and forwards.

In addition, CSFB's analysts who issued positive reports on the Company also understood the Company's reported financial condition was falsified through the Transactions. CSFB vice president and research analyst Philip Salles stated in email to analyst Launer that "ENE just could

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[65] CSFB analyst Jill Sakol, who wanted to release negative information on Enron, felt pressured to, and did, send a draft report to Abib, among others. *See* CSFB Opp. at 225-27.

never tell the truth." Ex. 13698 at DPOEX00006001; Ex. 15907 at 3. Salles also wrote to Launer, in November 2000, that Enron's financials were "as clear as mud." Ex. 15918.

CSFB analyst DeVries privately wrote to a friend that Enron "DEFINITELY [is] going to take some more charges next quarter and ***they still aren't fully disclosing things***, investors feel duped. I wouldn't touch it. Reiterate HOLD. And that's a real hold." Ex. 15659 at CSLBLLC 006303948. Devries was also privately informed that the illicit Enron partnerships were "basic money laundering operations in essence." Ex. 15637. In another email to a friend, DeVries admitted his knowledge that "all these partnerships" – *i.e.*, including LJM1 and 2 – made Enron "all smoke [and] mirrors accounting." Ex. 15660 at CSFBLLC006303944. DeVries' friend confirmed that CSFB's analysts knew about the fraudulent effect of the Transactions: "[M]an, you guys are the ones that helped set up these partnerships . . . not to mention ***you guys as analysts knew about it*** and didn't say a word to clients in your research . . . who's hiding what???" Ex. 15670 at CSFBLLC 006362849. Thus, CSFB analysts who aggressively marketed Enron's securities had knowledge that the Company's reported financial condition had been falsified through the Transactions. And CSFB knew that other banks were engaged in the deceptive transactions. As CSFB wrote internally about a SSB/Citi deal: "The beauty of the deal from Enron and SSB/Citi's stand point is that it does not appear to be 'new' money on Enron's balance sheet, and it creates new capacity for SSB/Citi to make loans to Enron." "Behind the scenes . . . Citi has basically hedged it's [sic] other Enron exposure . . . since they had laid off $500 mm of Enron exposure to the market." "The ***'market' doesn't see that behind the scenes, Citi is lending $500 mm of new money to Enron***."[66]

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[66] Ex. 14085 (email from Jennifer Powers to Osmar Abib, James Moran, Adebayo Ogunlesi, and others, August 18, 2000).

b. Merrill – Scienter

As noted above, Merrill played a variety of roles and engaged in a variety of market-related activities in connection with Enron. All of these roles, relationships, and activities, however, were known to and coordinated by a small group of senior bankers in Merrill's Houston and Dallas offices. Chief among them were Schuyler Tilney and Rob Furst. Tilney had long been one of Enron's investment bankers. Indeed, he had been involved in the mid-1980s merger that created Enron in the first place. By the mid-1990s Tilney had become the head of Merrill's Houston office and, by early 2001, he was head of Merrill's worldwide energy-and-power investment banking group.[67] Tilney was, during the relevant period, Merrill's "senior relationship manager" for its Enron relationship.[68] Rob Furst also enjoyed a long-term close relationship with Enron. Prior to coming over to Merrill in the summer of 1999, he had worked as a banker at CSFB assigned to cover the Enron account. In that role he engaged in and/or was aware at the very least of a number of other deceptive transactions between Enron and its investment banks. In the fall of 1999, Furst assumed the role of Merrill's "relationship manager" with respect to the Enron account.

Tilney and Furst were centrally involved in the Nigerian Barge transaction, the Power Trades, and LJM2.[69] They also coordinated all other aspects of the Merrill/Enron relationship,

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[67] Notably, Merrill's principal equity analysts assigned to the Enron account – first John Olson, then after Olson's firing Donato Eassey – worked in Tilney's Houston office.

[68] As we have discussed elsewhere, Tilney had very close personal relationships at Enron as well. Not only was he close personally to Andy Fastow, but his wife, Elizabeth Tilney, was a senior executive at Enron.

[69] Other very senior Merrill bankers were involved in or aware of some or all of these transactions, but it is sufficient that knowledge of all things Enron was centralized with Tilney and Furst in the late 1999-2001 time frame.

including the equity swaps and forwards.[70] Thus, they were aware of Merrill's analyst coverage of Enron, as well as its other market-related activities.

Tilney and Furst, as well as other top Merrill bankers, were also aware of, and specifically discussed internally, the impact of their activities on Enron's stock. As noted above, Tilney, in discussing the circumstances surrounding the pre-arranged pact to "unwind" the Power Trades, emphasized that "***they [Enron] knew what we were making at . . . the quarter and year (which had great value in their stock price, not to mention personal compensation***)."[71] Thus, Merrill was well aware that its deceptive conduct was impacting the "***value***" of Enron's stock in the market.

In addition, Merrill gained significant knowledge about other-bank activities when Rob Furst moved from CSFB to Merrill in the Fall of 1999. He had been one of CSFB's relationship managers for its Enron relationship, and he took over as the Enron relationship manager upon his arrival at Merrill. From his work at CSFB, Furst was fully aware of LJM1 and its Rhythms deal. Furst knew LJM1 was purchasing a part of Enron's Cuiaba interest, Ex. 50239 at DPOEX00006081, and that CSFB planned to monetize the Enron treasury shares not supporting the Rhythms hedge through a "SAILS" transaction. Ex. 11231 at CSFBLLC006359806. Furst also knew that Enron was monetizing a number of its international assets through the "Rawhide" transaction (*see* 11/10/04 Deposition Transcript of Jamie Welch at 26:14-27:13) and that Enron regularly used off-balance-sheet transactions at quarter-end to meet financial objectives.[72]

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[70] In his "Contact Report Summary" dated September 26, 2000, Furst noted that he reviewed the "forward equity swaps" with Tim DeSpain. Ex. 41 (MLNBY 0272735).

[71] Ex. 50028 at MLBE0370956 (5/30/00 email from Schuyler Tilney to Dan Gordon and Robert Furst).

[72] An internal CSFB email from March 1999, recounting a meeting with an Enron employee and forwarded to Furst, states: "***As we were aware they are very active in using off balance sheet/monetization structures to manage revenues/cash flow on a quarter to quarter basis (he said***

Finally, Merrill has accepted responsibility for the activities of these employees in its settlement with the Department of Justice. Ex. 42.

c. Barclays – Scienter

As to Barclays, The Regents have already presented evidence establishing that the Barclays bankers who worked on the Transactions understood that they operated to falsify Enron's reported financial condition.[73] These same bankers also understood that the bank brought Enron securities to market. In fact, they understood that Barclays engaged in the fraudulent Transactions specifically to earn opportunities to work on Enron offerings. For example, a Sponsor/Relationship Officer Comments memorandum listing banker John Sullivan as its author explains that Barclays executes transactions for Enron as "favors," in return for which it gets presented "new issue opportunities." Ex. 10383. An email between Barclays bankers and others references a "commodit[y] trade" with Enron (*i.e.*, a prepay transaction) and describes Barclays' chance to participate in the Zero Coupon Convertible Senior Notes offering as a "reward" for engaging in the Transactions. Ex. 50915; *see also* Ex. 50932 (Email from Barclays banker Ian Jefferson stating that "We have had a good year with Enron and they recently gave us a share in the economics of their convertible bond as a reward for the good work we have done for them on both sides of th[e] pond."). Thus, Barclays personnel

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we should make a point of calling them six weeks before the end of each quarter as that was when they were likely to be handing out its mandates)." Ex. 11181 at CSFBLLC006362179.

[73] *See* Motion for Reconsideration, or in the Alternative, Clarification of Order Granting Barclays' PLC Motion for Summary Judgment on the Pleadings (Docket No. 4874) (Docket No. 4915) ("Barclays Mot.") at 38-48 and Lead Plaintiff's Supplemental Memorandum in Support of Its Motion for Reconsideration, or in the Alternative, Clarification of Order Granting Barclays' PLC Motion for Summary Judgment on the Pleadings (Docket No. 4915) (Docket No. 5203) ("Barclays Supp. Mot.") at 12-14 (Chewco); Barclays Mot. at 60-76 and Barclays Supp. Mot. at 14-15 (prepays); Barclays Mot. at 48-55 and Barclays Supp. Mot. at 15-17 (J.T. Holdings and Nikita); Barclays Mot. at 76-87 and Barclays Supp. Mot. at 17-20 (SO_2); Barclays Mot. at 87-92 and Barclays Supp. Mot. at 20-21(Metals).

understood both that the bank was engaging in the Transactions, and that it was active in the market for Enron securities.

Barclays also knew the impact of the deceptive conduct other banks were engaging in, as Barclays noted in a 1998 annual review of Enron. Barclays described certain minority-interest transactions, such as Rawhide and Nighthawk, as structures in which "***debt masquerades as a limited partnership interest***." Ex. 10155 at BRC000106846 (Enron Corp. Annual Review, July 2, 1999). When calculating Enron's true debt, Barclays reclassified the minority interests as well as other structured financings as debt, stressing that it was "essential [to] take these considerations into account" when calculating Enron's balance-sheet leverage or cash-flow coverage of financing costs. *Id.* As a result of these reclassifications, Barclays concluded that Enron's ***1998 year-end debt was actually $11.9 billion as opposed to the year-end balance sheet amount of $7.4 billion***. *Id.* Therefore Enron's debt-to-total-capitalization ratio was actually 63%, as opposed to the ***41.9% Enron claimed***. *Id.*

2. The Undisclosed Information Was Material

Each of the Banks had knowledge that Enron's financials were distorted in a material way. As a result of their direct engagement in the Enron fraud, the Banks were aware generally that Enron undertook a significant number of transactions designed to materially alter its apparent financial condition. That fact alone, beyond the specifics of the Transactions and their individual impact on Enron's balance sheet and income statement, was highly material. In addition, the Banks were aware of the specific impact of their own transactions on Enron's financials and those impacts were material as well. The deceptive transactions each of the Banks at issue engaged in are detailed in The Regents' previously filed oppositions to motions for summary judgment.

a. CSFB – Materiality

Fastow viewed CSFB as a bank that "worked to solve certain of [Enron's] financial problems."[74] In his declaration Fastow recounted that CSFB executives Robert Furst, Osmar Abib, Adebayo Ogunlesi, and Bob Jeffe "aggressively solicited Enron's business"[75] and that CSFB's bankers, including Laurence Nath, played a key role in structuring the fraudulent transactions. *Id.* In fact, Fastow viewed Nath as the person most responsible for developing and executing the Marlin, Whitewing, Osprey, and Firefly transaction structures.[76] CSFB also engaged in numerous other deceptive transactions including LJM1-Rythms and Cuiaba; LJM2-Bob West, Nowa Sarzna, ENA CLO; Nikita, Nile, the CSFB prepay, and Iguana. These transactions alone were material and should have been disclosed. The following chart demonstrates the material impact just the CSFB Transactions had on Enron's reported numbers.

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74 Fastow Decl., ¶¶6, 8; 10/24/06 Fastow Depo. Tr. at 433:1-21.

75 Fastow Decl., ¶47.

76 Fastow Decl., ¶48.

Financial Statement Effect of Certain Transactions in Which CSFB Engaged[77]

	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/199	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Pre Tax Income Overstated/(Understated)	-	-	**14.8**	**158.0**	**226.7**	**24.4**	**95.0**	**111.6**	**147.8**	**16.6**	**33.2**	**78.7**
Nikita	-	-	-	-	-	-	-	-	-	-	-	10.0
Nile	-	-	-	-	-	-	-	-	-	-	-	18.9
LJM 1 / Rhythms				95.0	95.0	8.0	8.0	8.0	8.0	-	-	-
LJM1/Cuiaba				32.3	63.3	-	-	-	-	-	-	-
Osprey			14.8	30.7	47.3	16.4	32.9	49.5	66.1	16.6	33.2	49.8
Selected LJM2 transactions (See Note)	-	-	-	-	21.10	-	54.10	54.10	73.70	-	-	-

EARNINGS BEFORE INTEREST, TAXES AND DEPRECIATION

	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/199	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on EBITDA Overstated/(Understated)	-	-	-	**127.3**	**179.4**	**8.0**	**62.1**	**62.1**	**81.7**	-	-	**28.9**
Nikita												10.0
Nile												18.9
LJM 1 / Rhythms				95.00	95.0	8.0	8.0	8.0	8.0	-	-	-
LJM1/Cuiaba				32.30	63.3	-	-	-	-			
Selected LJM2 transactions (See Note)	-	-	-	-	21.10	-	54.10	54.10	73.70	-	-	-

CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES

	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/199	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Cash Provided by (Used in) Operating Activities Overstated	-	-	-	**345.0**	**1,154.1**	**30.6**	**60.6**	**93.4**	**825.7**	**82.9**	**236.9**	**320.9**
Iguana	-	-	-	-	208.4	-	-	-	-	-	-	-
Nikita	-	-	-	-	-	-	-	-	-	-	-	29.0
Nile	-	-	-	-	-	-	-	-	-	-	-	22.2
Rawhide	-	-	-	-	-	-	-	-	-	-	-	-
CSFB Prepay	-	-	-	-	-	-	-	-	150.0	-	-	-
Osprey				345.0	744.7	30.6	30.6	63.4	611.4	82.9	236.9	269.7
Selected LJM2 transactions (See Note)	-	-	-	-	201.00	-	30.00	30.00	64.30	-	-	-

TOTAL DEBT

	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/199	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Total Debt Overstated/(Understated)	**(2,374.0)**	**(2,374.0)**	**(2,374.0)**	**(3,106.2)**	**(4,020.7)**	**(4,041.5)**	**(3,780.6)**	**(4,461.4)**	**(4,796.2)**	**(4,430.1)**	**(4,550.4)**	**(4,441.8)**
Iguana	-	-	-	-	(208.4)	(208.4)	-	-	-	-	-	-
Nikita	-	-	-	-	-	-	-	-	-	-	-	(80.0)
Nile	-	-	-	-	-	-	-	-	-	-	-	(25.0)
Rawhide	(750.00)	(750.00)	(750.00)	(750.00)	(750.0)	(740.0)	(740.0)	(740.0)	(740.0)	(740.0)	(740.0)	(691.0)
CSFB Prepay	-	-	-	-	-	-	-	-	(150.0)	(150.0)	(150.0)	(150.0)
LJM1/Cuiaba	-	-	-	-	(200.0)	(200.0)	(200.0)	(200.0)	(200.0)	(200.0)	(200.0)	-
Firefly	(475.00)	(475.00)	(475.00)	(475.00)	(475.0)	(475.0)	(475.0)	-	-	-	-	-
Osprey				(926.30)	(1,327.4)	(1,358.2)	(1,305.7)	(2,461.5)	(2,646.3)	(2,280.2)	(2,400.5)	(2,350.8)
Marlin	(1,149.00)	(1,149.00)	(1,149.00)	(954.90)	(954.9)	(954.9)	(954.9)	(954.9)	(954.9)	(954.9)	(954.9)	(1,040.0)
Selected LJM2 transactions (See Note)	-	-	-	-	(105.00)	(105.00)	(105.00)	(105.00)	(105.00)	(105.00)	(105.00)	(105.00)

TOTAL EQUITY

	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/199	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Total Equity Overstated/(Understated)	-	-	-	**1,198.3**	**1,250.4**	**1,024.4**	**1,078.5**	**1,078.5**	**1,098.1**	**1,098.1**	**1,098.1**	**1,123.7**
Nikita												10.0
Nile												18.9
LJM 1 / Rhythms				166.00	166.0	(60.0)	(60.0)	(60.0)	(60.0)	(60.0)	(60.0)	-
LJM1/Cuiaba				32.30	63.3	63.3	63.3	63.3	63.3	63.3	63.3	-
Osprey				1,000.0	1,000.0	1,000.0	1,000.0	1,000.0	1,000.0	1,000.0	1,000.0	1,000.0
Selected LJM2 transactions (See Note)	-	-	-	-	21.10	21.10	75.20	75.20	94.80	94.80	94.80	94.80

NOTE: "Selected LJM2 transactions" are Bob West Treasure, Nowa Sarzyna, ENA CLO, MEGS LLC, Backbone, Catalytica, Avici

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[77] Source: 2/22/06 Saul Solomon Supplemental Expert Report.

b. Merrill – Materiality

Merrill funded and executed LJM2's early closing in late December 1999, and it knowingly and intentionally approved and funded several deceptive year-end LJM2/Enron transactions (Bob West Treasure, MEGS, Nowa Sarzyna, ENA CLO) that, along with the Nigerian Barges and the Power Trades transactions, caused Enron to falsely report that it had met Wall Street's earnings expectations for 4Q99. But Merrill had knowledge of much more at Enron as it traded in Enron's securities and sold Enron to the market. Rob Furst joined Merrill from CSFB in the fall of 1999. And from there Merrill just increased its deceptive activity, which was material and never disclosed to the market. Throughout 2000, Merrill continued to fund many additional LJM2 transactions – including the infamous Raptors and Backbone transactions – with full knowledge, before funding them, of the purpose and intended effect of those transactions. The Raptor transactions alone enabled Enron to conceal losses totaling $572 million in 2000 and $544.8 million in 2001.

As this Court noted earlier:

> Although Merrill Lynch argues its actions were not unlawful and that they were merely business transactions later misrepresented by Enron in its financial statements, the factual allegations suggest knowingly deceptive conduct, concealed for unlawful purpose(s), which included misleading Enron investors whose money was needed to perpetuate the Ponzi scheme and Merrill Lynch's "money tree." Sham business transactions with no legitimate business purpose that are actually guaranteed "loans" employed to inflate Enron financial image are not above-board business practices. This Court disagrees with Merrill Lynch's contention that the alleged "'deception' did not occur until Enron allegedly misreported" the transactions.

In re Enron Corp. Sec. Litig., 310 F. Supp. 2d 819, 829 (S.D. Tex. 2004).

FINANCIAL STATEMENT EFFECT OF CERTAIN TRANSACTIONS IN WHICH MERRILL LYNCH ENGAGED

($ millions)

PRE TAX INCOME

	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Pre Tax Income Overstated/(Understated)	83.1	-	54.1	152.2	776.3	276.6	333.2	600.8
Barges	13.0	-	-	-	-	-	-	-
Electricity Trades	49.0	-	-	-	-	-	-	-
Selected LJM2 transactions (See Note)	21.1	-	54.1	152.2	776.3	276.6	333.2	600.8

EARNINGS BEFORE INTEREST, TAXES AND DEPRECIATION

	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on EBITDA Overstated/(Understated)	83.1	-	54.1	102.7	710.2	260.0	300.0	551.0
Barges	13.0	-	-	-	-	-	-	-
Electricity Trades	49.0	-	-	-	-	-	-	-
Selected LJM2 transactions (See Note)	21.1	-	54.1	102.7	710.2	260.0	300.0	551.0

CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES

	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Cash Provided by (Used in) Operating Activities Overstated/(Understated)	1,001.0	-	30.0	93.4	875.7	82.9	36.9	69.7
Selected LJM2 transactions (See Note)	1,001.0	-	30.0	93.4	875.7	82.9	36.9	69.7

TOTAL DEBT

	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Total Debt Overstated/(Understated)	(1,655.0)	(1,645.0)	(1,645.0)	(4,106.5)	(4,491.3)	(4,125.2)	(4,045.5)	(3,946.8)
Selected LJM2 transactions (See Note)	(1,655.0)	(1,645.0)	(1,645.0)	(4,106.5)	(4,491.3)	(4,125.2)	(4,045.5)	(3,946.8)

TOTAL EQUITY

	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Total Equity Overstated/(Understated)	83.1	83.1	309.2	1,357.8	1,965.3	3,053.3	3,093.3	2,344.3
Barges	13.0	13.0	13.0	13.0	13.0	13.0	13.0	13.0
Electricity Trades	49.0	49.0	49.0	49.0	49.0	49.0	49.0	49.0
Selected LJM2 transactions (See Note)	21.1	21.1	247.2	1,295.8	1,903.3	2,991.3	3,031.3	2,282.3

NOTE: "Selected LJM2 transactions" are Yosemite I, Rawhide, Fishtail/Bacchus, Osprey add-on certificates, Osprey II, Bob West Treasure, Nowa Sarzyna, ENA CLO, MEGS LLC, Backbone, Catalytica, Avici and the Raptors

Source: 2/22/06 Saul Solomon Supplemental Expert Report

c. Barclays – Materiality

Like CSFB, Barclays participated in a wide variety of transactions with Enron, including: (1) a related-party transaction (Chewco); (2) prepays (Roosevelt, Nixon, and CSFB); (3) an FAS 125/140 transaction (Nikita); (4) a synthetic-lease transaction (J.T. Holdings); (5) a product-financing transaction (Metals); and (6) the sale of emission credits disguised as a loan (SO_2). According to Fastow, "Barclays, one of Enron's Tier-1 Banks, engaged in at least eight transactions during 1997 to 2001, including Chewco, J.T. Holdings, Nikita, Prepays, Metals and SO_2. These transactions contributed to causing Enron to report lower balance sheet debt and created the false appearance of funds flow from operations."[78] In doing these eight transactions, Fastow or his staff spoke or met with Barclays' bankers Richard Williams, Eric Chilton, John Sullivan, George McKean, Bob Diamond, and others at Barclays. Fastow discussed the purpose of the transactions with Barclays' bankers and believed that they understood they were being paid a premium because of the impact the structures would have on Enron's public financial statements. Fastow Decl., ¶17. According to Fastow, Barclays required assurances or structural enhancements to certain transactions in order to minimize its financial risks. *See, e.g.*, Fastow Decl., ¶13; Ex. 10137 (verbal assurances regarding J.T. Holdings); Ex. 10460 (assurances regarding Brazos); Ex. 10450 (assurances regarding J.T. Holdings); Ex. 10430 (assurances regarding Nikita); Ex. 10491 (same). Fastow intended the assurances to operate as guarantees, and he did not believe Barclays would have entered into the transactions without them. Fastow Decl., ¶13. The assurances were critical for Barclays to do the deals. *See, e.g.*, Ex. 10491 (conditioning of Nikita deal sanction on receipt of assurances from senior Enron officers). The Spring 2002 Barclays "Post-Mortem" document confirms that these verbal assurances translated to "virtual guarantees." *See* Ex. 10156.

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[78] Fastow Decl., ¶16.

Financial Statement Effect of Certain Transactions in Which Barclays Engaged[79]

PRE TAX INCOME

	12 mo ended 12/31/1997	3 mo ended 3/31/1998	6 mo ended 6/30/1998	9 mo ended 9/30/1998	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/1999	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Pretax Income Overstated/(Understated)	**28.0**	**38.3**	**76.5**	**114.8**	**153.0**	**32.9**	**65.5**	**98.4**	**133.0**	**92.7**	**100.0**	**90.0**	**91.0**	**(6.0)**	**-**	**10.0**
Nikita	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	10.0
JEDI / Chewco	28.0	38.3	76.5	114.8	153.0	32.9	65.5	98.4	133.0	92.7	100.0	90.0	91.0	(6.0)	-	-

EARNINGS BEFORE INTEREST, TAXES AND DEPRECIATION

	12 mo ended 12/31/1997	3 mo ended 3/31/1998	6 mo ended 6/30/1998	9 mo ended 9/30/1998	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/1999	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on EBITDA Overstated/(Understated)	**25.0**	**31.8**	**63.5**	**95.3**	**127.0**	**21.7**	**43.0**	**64.7**	**88.0**	**79.2**	**72.0**	**51.0**	**25.0**	**(23.0)**	**-**	**10.0**
Nikita	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	10.0
JEDI / Chewco	25.0	31.8	63.5	95.3	127.0	21.7	43.0	64.7	88.0	79.2	72.0	51.0	25.0	(23.0)	-	-

CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES

	12 mo ended 12/31/1997	3 mo ended 3/31/1998	6 mo ended 6/30/1998	9 mo ended 9/30/1998	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/1999	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Cash Provided by (Used in) Operating Activities Overstated/(Understated)	**-**	**-**	**-**	**-**	**500.0**	**-**	**(375.0)**	**(375.0)**	**(176.0)**	**-**	**(324.0)**	**(324.0)**	**711.0**	**365.0**	**365.0**	**532.5**
Nikita	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	29.0
Camelot I & II	-	-	-	-	-	-	-	-	-	-	-	-	1,035.0	365.0	365.0	365.0
SO2	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	138.5
Roosevelt	-	-	-	-	500.0	-	(375.0)	(375.0)	(500.0)	-	-	-	-	-	-	-
Nixon	-	-	-	-	-	-	-	-	324.0	-	(324.0)	(324.0)	(324.0)	-	-	-

TOTAL DEBT

	12 mo ended 12/31/1997	3 mo ended 3/31/1998	6 mo ended 6/30/1998	9 mo ended 9/30/1998	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/1999	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Total Debt Overstated/(Understated)	**(711.4)**	**(432.4)**	**(482.5)**	**(516.4)**	**(1,061.4)**	**(1,061.4)**	**(666.4)**	**(666.4)**	**(1,008.9)**	**(1,008.9)**	**(684.9)**	**(650.9)**	**(1,773.9)**	**(1,510.0)**	**(1,510.0)**	**(1,878.5)**
Nikita	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(80.0)
Camelot I & II	-	-	-	-	-	-	-	-	-	-	-	-	(1,035.0)	(1,400.0)	(1,400.0)	(1,400.0)
JT Holdings	-	-	-	-	-	-	-	-	-	-	-	-	(110.0)	(110.0)	(110.0)	(110.0)
SO2	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(138.5)
Roosevelt	-	-	-	-	(500.0)	(500.0)	(125.0)	(125.0)	-	-	-	-	-	-	-	-
Nixon	-	-	-	-	-	-	-	-	(324.0)	(324.0)	-	-	-	-	-	-
JEDI / Chewco	(711.4)	(432.4)	(482.5)	(516.4)	(561.4)	(561.4)	(541.4)	(541.4)	(684.9)	(684.9)	(684.9)	(650.9)	(628.9)	-	-	-
CSFB Prepay	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(150.0)

TOTAL EQUITY

	12 mo ended 12/31/1997	3 mo ended 3/31/1998	6 mo ended 6/30/1998	9 mo ended 9/30/1998	12 mo ended 12/31/1998	3 mo ended 3/31/1999	6 mo ended 6/30/1999	9 mo ended 9/30/1999	12 mo ended 12/31/1999	3 mo ended 3/31/2000	6 mo ended 6/30/2000	9 mo ended 9/30/2000	12 mo ended 12/31/2000	3 mo ended 3/31/2001	6 mo ended 6/30/2001	9 mo ended 9/30/2001
Effect on Total Equity Overstated/(Understate	**258.0**	**296.3**	**334.5**	**372.8**	**391.0**	**423.9**	**456.5**	**489.4**	**544.0**	**815.7**	**823.0**	**813.0**	**814.0**	**(6.0)**	**(6.0)**	**10.0**
Nikita	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	10.0
JEDI / Chewco	258.00	296.30	334.50	372.80	391.00	423.90	456.50	489.40	544.0	815.7	823.0	813.0	814.0	(6.0)	(6.0)	-

[79] Source: 2/22/06 Saul Solomon Supplemental Expert Report.

3. The Banks' Conduct Was "In Connection With" the Purchase or Sale of Securities

As this Court recognized, the Supreme Court has held that: "[T]he phrase 'in connection with the purchase or sale of any security' must be construed broadly and flexibly to effectuate Congress' remedial goal in enacting the statute of insuring honest securities markets and promoting investor confidence." *Enron*, 235 F. Supp. 2d at 693 (citing *O'Hagan*, 521 U.S. at 658 and *SEC v. Zandford*, 535 U.S. 813, 819-20 (2002)). Under *Zandford*, for the "in connection with" requirement to be satisfied, "'[i]t is enough that the scheme to defraud and the sale of securities ***coincide***.'" *In re Enron Corp. Sec. Litig.*, No. H-04-0087, 2005 U.S. Dist. LEXIS 41240, at *49-*50 (S.D. Tex. Dec. 22, 2005).

Here, there can be no doubt that the Banks' conduct of being active in the market for Enron securities while engaging in the Transactions satisfies the "coincide" test. In fact, because these activities were specifically ***targeted*** at the purchase of Enron securities, their connection with those securities is far stronger than simply coinciding with such purchases.

4. Reliance Is Satisfied Because the *Affiliated Ute* Presumption Is Available

In *Regents*, the Fifth Circuit ruled that for the *Affiliated Ute* presumption to be applicable, "the plaintiff must (1) allege a case primarily based on omissions or non-disclosure and (2) demonstrate that the defendant owed him a duty of disclosure." *Regents*, 482 F.3d at 384. As discussed above, this is clearly an omissions case – *see* §III.B.4.a. *supra* – and the Banks' failure to disclose the impact of at least their own conduct (deceptive under §10(b)) on Enron's financials violated the Fifth Circuit multi-factor *First Virginia Bankshares* criteria and several independent duties to disclose.

Causation in fact is clearly present here. ***Had the Banks satisfied their duty to disclose, the Enron fraud would have been revealed***. And because the Banks breached this duty by keeping silent, Enron investors were harmed, as described above.[80]

Lead Plaintiff anticipates that the Banks will argue that to the extent they owed a duty of disclosure, it was not to the market at large, but only to the purchasers of those securities they marketed or recommended for purchase. But this argument is invalid for a number of reasons. First, CSFB and Merrill were active in Enron's common stock and their analyst reports addressed that market. Thus, the duty to disclose ran to this entire market. In addition, each of the Banks' extensive market activity necessarily impacted the common stock.

Second, causation in fact is present because the Banks' decision to breach their duty to disclose – even in the debt underwritings or private placements – harmed all Enron investors, as it allowed the Enron fraud to continue. When such causation in fact is present, conduct is actionable under Rule 10b-5 notwithstanding the fact that the duty of disclosure breached ran to another party. The Supreme Court made this clear in *O'Hagan*, 521 U.S. 642, where the Supreme Court held that an attorney faced liability from his breach of the disclose-or-abstain duty discussed above.

In *O'Hagan*, the defendant attorney worked for a law firm which received confidential information identifying a future tender offer target. The attorney purchased stock and options in the target company, and profited when the offer was announced – at the expense of the target's shareholders, of course.

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[80] *See Gibraltar Sav. v. LDBrinkman Corp.*, 860 F.2d 1275, 1303-04 (5th Cir. 1988) (In a case involving a fraud claim brought by a bank against a borrower: "***[W]e disagree entirely with defendants' vehement contention that Gibraltar could not have relied*** [on borrower's promise to keep its subsidiaries solvent until loan was repaid] as a matter of law. While the defendants' evidence . . . is all persuasive in comparison to the bare assertions of Gibraltar employees after the fact, such credibility choices are the jury's, not ours; ***we refuse to substitute our reading of the evidence for that of a factfinder***.").

In finding him liable, the Supreme Court observed that the attorney breached a duty of disclosure ***to his employer and the acquiring company***,[81] but this resulted in harm to another group of persons, *i.e.*, the target's shareholders. The Supreme Court found liability under Rule 10b-5 was sufficiently expansive to cover those investors:

> The securities transaction and the breach of duty thus coincide. This is so even though the person or entity defrauded ***is not the other party to the trade***, but is, instead, the source of the nonpublic information. *See* Aldave, 13 Hofstra L. Rev., at 120 ("***a fraud or deceit can be practiced on one person, with resultant harm to another person or group of persons***").

O'Hagan, 521 U.S. at 656. Thus, even if the Banks were correct (which they are not) that they owed a duty of disclosure only to those purchasers of the securities they marketed, the fact that all Enron investors were harmed nevertheless permits a finding of causation in fact.

5. Economic Loss/Loss Causation Is Satisfied

Finally, economic loss/loss causation is satisfied. This Court has adopted the loss causation analysis of *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 171 (2d Cir. 2005). *See Enron,* 2005 U.S. Dist. LEXIS 41240 (denying motion to dismiss filed by defendant Royal Bank of Canada and six of its subsidiaries); *Enron*, 439 F. Supp. 2d at 705-06. Pursuant to this adoption: "'[T]he loss causation requirement will be satisfied if [the defendant's] conduct had the effect of ***concealing the circumstances*** that bore on the ultimate loss'" – in the context of this case, knowledge of the fraud and the impact of their own conduct "'concealed, among other things, the risks that [Enron] would be unable to service its debt and consequently suffer financial collapse,'" and "that risk materialized." *Enron,* 439 F. Supp. 2d at 724.

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[81] *See O'Hagan,* 521 U.S. at 655 n.6 ("Under the misappropriation theory urged in this case, the disclosure obligation runs to ***the source of the information***, here, Dorsey & Whitney and Grand Met.").

This standard is satisfied here. The Banks' breach of their duty to disclose the truth they knew about Enron's financial condition operated to conceal the true state of affairs – *i.e.*, that Enron's reported financial condition was falsified. Because of this concealment, investors purchased Enron securities at inflated prices. When the true state of affairs "materialized," these investors suffered economic harm in that the value of their investments was greatly reduced. *See* Lead Plaintiff's Opposition to Motion for Summary Judgment filed by Defendants Merrill Lynch, Pierce Fenner & Smith Incorporated and Merrill Lynch Co. Inc. (Docket No. 5197) at 200-204.

IV. CONCLUSION

For the reasons set forth above, The Regents respectfully requests that CSFB's, Merrill's, and Barclays' motions for summary judgment be denied.

DATED: March 28, 2008

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing LEAD PLAINTIFF'S SUPPLEMENTAL OPPOSITION TO PENDING MOTIONS FOR SUMMARY JUDGMENT (DOCKET NOS. 4816, 4817, 4818, 4824, 4825 AND 5333) document has been served by sending a copy via electronic mail to serve@ESL3624.com on March 28, 2008.

Deborah S. Granger

DEBORAH S. GRANGER