UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

AMALGAMATED BANK, as Trustee for the LONGVIEW COLLECTIVE INVESTMENT FUND, LONGVIEW CORE BOND INDEX FUND and CERTAIN OTHER TRUST ACCOUNTS, Individually and On Behalf of All Others Similarly Situated, Plaintiff, vs. KENNETH L. LAY, JEFFREY K. SKILLING, ANDREW S. FASTOW, RICHARD A. CAUSEY, JAMES V. DERRICK, JR., J. CLIFFORD BAXTER, MARK A. FREVERT, STANLEY C. HORTON, KENNETH D. RICE, RICHARD B. BUY, LOU L. PAI, ROBERT A. BELFER, NORMAN P. BLAKE, JR., RONNIE C. CHAN, JOHN H. DUNCAN, WENDY L. GRAMM, ROBERT K. JAEDICKE, CHARLES A. LEMAISTRE, JOE H. FOY, JOSEPH M. HIRKO, KEN L. HARRISON, MARK E. KOENIG, STEVEN J. KEAN, REBECCA P. MARK-JUSBASCHE, MICHAEL S. MCCONNELL, JEFFREY MCMAHON, CINDY K. OLSON, J. MARK METTS, JOSEPH W. SUTTON and ARTHUR ANDERSEN, LLP, Defendants.	§	Civil Action No. H 01-4198 CLASS ACTION

PLAINTIFF'S *EX PARTE* APPLICATION FOR (1) A TEMPORARY RESTRAINING ORDER AND ORDER TO SHOW CAUSE WHY A PRELIMINARY INJUNCTION SHOULD NOT BE ENTERED FREEZING AND IMPOSING A CONSTRUCTIVE TRUST OVER INSIDER TRADING PROCEEDS, (2) ACCOUNTING OF INSIDER TRADING PROCEEDS, AND (3) LIMITED EXPEDITED DISCOVERY

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

CASES **Page**

Page

Page

Page

Page

STATUTES RULES AND REGULATIONS

Page

LEGISLATIVE HISTORY

By counsel and pursuant to Rules 64 and 65 of the Federal Rules of Civil Procedure, plaintiff submits this *ex parte* application for a temporary restraining order and order to show cause why a preliminary injunction should not issue, and for particularized expedited discovery, with memorandum of points and authorities.

MEMORANDUM OF POINTS AND AUTHORITIES

I. Introduction

This action was filed by Amalgamated Bank, a Trustee for the LongView Collective Investment Fund, Longview Core Bond Index Fund and certain other trust accounts ("Amalgamated"), on behalf of a class of all persons who purchased Enron Corporation's ("Enron" or the "Company") publicly traded securities between October 19, 1998 and November 27, 2001 (the "Class Period"). Amalgamated is America's oldest union owned and operated Labor Bank, and it has investment relationships with over 200 employee benefit funds, including union plans. Amalgamated purchased over 113,000 shares of Enron stock and $6 million in Enron bonds during the Class Period and lost over $10 million as a result of what appears to be one of the most serious securities frauds in history. By this *ex parte* application, plaintiff seeks a temporary restraining order imposing a constructive trust on over $1.1 billion in insider trading proceeds obtained by the Individual Defendants[1] in this action, pending a hearing on an Order to Show Cause why a preliminary injunction should not issue. Plaintiff also seeks an order providing for an accounting of the insider trading proceeds obtained by the Individual Defendants and expedited, particularized discovery pursuant to PSLRA §21D(b)(3).[2]

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[1] The Individual Defendants are: Kenneth L. Lay; Jeffrey K. Skilling; Andrew S. Fastow; Richard A. Causey; James V. Derrick, Jr.; J. Clifford Baxter; Mark A. Frevert; Stanley C. Horton; Kenneth D. Rice; Richard B. Buy; Lou L. Pai; Robert A. Belfer; Norman P. Blake, Jr.; Ronnie C. Chan; John H. Duncan; Wendy L. Gramm; Robert K. Jaedicke; Charles A. LeMaistre; Joe H. Foy; Joseph M. Hirko; Ken L. Harrison; Mark E. Koenig; Steven J. Kean; Rebecca P. Mark-Jusbasche; Michael S. McConnell; Jeffrey McMahon; J. Mark Metts; Cindy K. Olson; and Joseph W. Sutton.

[2] "PSLRA" refers to the Private Securities Litigation Reform Act of 1995, codified at 15 U.S.C. §78u-4.

A. Basis for the Temporary Restraining Order[3]

1. Summary of Facts Concerning the Enron Fraud and Individual Defendants' Insider Trading

a. Enron's Record Earnings 1997-2001

Enron was an "energy merchant" which traded in natural gas, electricity and communications to wholesale and retail customers. In the four quarters of 2000 and first and second quarters of 2001, Enron reported sales and net income, respectively, of $13 billion and $338 million, $16 billion and $289 million, $30 billion and $292 million, $41 billion and $347 million, $50 billion and $406 million, and $50 billion and $404 million. Jaconette Decl., Exs. 1-6. And, in the past four years, Enron's reported annual revenue grew fivefold, from $20 billion to $101 billion. Jaconette Decl., Ex. 7. Those financial results, attested to by the Company's officers and directors as being in conformity with Generally Accepted Accounting Principles ("GAAP"), were manipulated and falsely inflated by hundreds of millions of dollars.

b. The Bogus Transactions and Accounting Falsities

To inflate Enron's reported profits and hide the Company's true debt burden, Fastow, Skilling, and other top Enron executives created limited partnerships which they called Special Purpose Entities ("SPE"). The purported SPEs were actually "strawmen" and were not independent from Enron. *See* Jaconette Decl., Ex. 14; Ex. 13 at 9-13, 18-20; Ex. 13 at Ex. 99.1 (Enron press release). Enron executives controlled the limited partnerships with the Company and Enron financed their operations. Jaconette Decl., Ex. 13 at 9-12.[4] The limited partnerships borrowed huge sums to purchase assets such as Broadband network cable used by Enron. They also did billions of dollars in paper transactions with Enron, such as trading Enron stock or assets in exchange for notes

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[3] The cited assertions made by plaintiff in this section, in addition to being supported by the Exhibits attached to the Declaration of James I. Jaconette ("Jaconette Decl."), are supported by information gathered from the investigation of plaintiff's counsel.

[4] Indeed, as reported by securities analysts, two "strawmen" being investigated by the SEC, are Cayman Islands limited partnerships "LJM Cayman LP" ("LJM1") and "LJM2 Co-Investment LP" ("LJM2") formed and operated by defendant Fastow, former Chief Financial Officer of Enron, which were named with the initials of each first name of Fastow's children. *See* Jaconette Decl., Ex. 14. Enron "now" believes that Fastow made in excess of $30 million from the limited partnerships while serving as Enron's CFO. Jaconette Decl., Ex. 13 at 10.

receivable to Enron which Enron then falsely reported as "assets" on Enron's balance sheet. Jaconette Decl., Ex. 13 at 7-8 ("Accounting Basis for $1.2 Billion Reduction in Shareholders' Equity"), at 11-12 ("General Summary of LJM Transactions" and "Sale of Assets").

Two of the limited partnerships alone, "Chewco" and "JEDI," concealed hundreds of millions of dollars of both debt and losses during 1997-2000. Jaconette Decl., Ex. 13 at 5 ("Table 1"). In 2000-2001, Enron's falsified balance sheet reflected over $1 billion in equity which did not exist. *Id*. In 2000 and 2001, Enron's falsified balance sheet reflected $728 million and $1 billion in assets, respectively, which also simply did not exist. *Id*. Bogus transactions with Fastow's "LJM1" limited partnership in 1999 alone were used to inflate the assets on Enron's balance sheet by $222 million. *Id.* Using these bogus transactions to inflate the Company's reported net income and assets on its balance sheet, Enron sold billions of dollars of debt and stock on the public securities markets. ¶17.[5]

c. Insider Trading of the Individual Defendants Exceeded $1.1 Billion

Enron's consistently improving reported financial performance artificially inflated the price of the Company's stock to as high as $90.75 during the Class Period.[6] ***Meanwhile, Enron's top insiders sold 17.3 million shares of their Enron stock for proceeds of $1.1 billion***.

Defendant/Position	**Shares Sold**	**Proceeds**
Pai, CEO, Enron Accelerator	5,031,105	$353,712,438
Lay, Chairman of the Board, CEO (86-2/01)	1,810,793	$101,346,951
Rice, CEO, Enron Broadband Services	1,138,370	$ 72,786,034
Mark, Vice Chairman, Director	1,410,262	$ 79,526,787
Harrison, CEO, Enron subsidiary, Director	1,004,170	$ 75,211,630
Skilling, Pres, COO (98-2/01),CEO (2/01-8/01)	1,119,958	$ 66,924,028
Frevert, CEO, Enron Wholesale Services	830,620	$ 50,269,504
Belfer, Director, Executive Comm. Member	1,052,138	$ 51,080,967
Horton, CEO, Enron Transportation Services	734,444	$ 45,472,278

[5] All paragraph references ("¶__") are to the Class Action Complaint for Violations of the Federal Securities Laws filed by Amalgamated.

[6] All share and per share amounts are adjusted to reflect Enron's 2-for-1 stock split in August 1999.

Defendant/Position	**Shares Sold**	**Proceeds**
Sutton, Vice Chairman	614,960	$ 40,093,346
Baxter, Vice Chairman, Chief Strategy Officer	577,436	$ 35,200,808
Hirko, CEO, Enron Broadband Services	473,837	$ 35,168,721
Fastow, CFO (98-10/01)	561,423	$ 30,463,609
Causey, Chief Accounting Officer	197,485	$ 13,329,743
Derrick, General Counsel	230,660	$ 12,656,238
Koenig, Vice President	129,153	$ 9,110,466
Olson, Vice President	83,183	$ 6,505,870
Kean, Director	64,932	$ 5,166,414
Duncan, Director	35,000	$ 2,009,700
Buy, Chief Risk Officer	54,874	$ 4,325,328
McMahon, Treasurer, Enron	39,630	$ 2,739,226
McConnell, President, Enron Global Markets	30,960	$ 2,353,431
Blake, Director	21,200	$ 1,705,328
Foy, Director	31,320	$ 1,639,590
Metts, Vice President, Director	17,711	$ 1,448,937
LeMaistre, Director, Compensation Comm.	17,344	$ 841,768
Jaedicke, Director, Audit Comm. Member	13,360	$ 841,438
Chan, Director, Audit Comm. Member	8,000	$ 337,200
Gramm, Director, Audit Comm. Member	10,256	$ 276,912
TOTALS:	**17,344,584**	**$1,102,544,672**

See Jaconette Decl., Ex. 24 (detailing insider sales by date and amount). *See also* Ex. A attached hereto (graph depicting the Individual Defendants' massive insider selling as the price of Enron's stock peaked and just before revelation of the fraud).

Enron's directors accounted for over $300 million of Enron's insider sales, including three members of Enron's audit committee, who reportedly "***are not independent, according to corporate***

governance experts and standards." Jaconette, Decl., Ex. 15 (emphasis added). As reported by *Bloomberg*, "Enron's Board Was Compromised by Financial Ties." *Id.*[7]

The true extent of the insider selling is not known. Amalgamated's counsel are informed and believe that certain top Enron insiders sold hundreds of thousands more in Enron derivative securities such as zero-cost collars and equity swaps through the Company's investment bankers, while not reporting these transactions. (Amalgamated seeks discovery of these trades. *See infra* §IV.A.)

d. To Avoid Credit Downgrades and Resulting Bankruptcy and Liability Exposure, the Fraud Was Desperately Hidden Until the Very End

Enron's true financial performance during this massive insider bailout was much worse than reported. In truth, its net income was falsely inflated by hundreds of millions of dollars, its shareholder equity was inflated by billions of dollars and its true debt level was understated by billions as well.

Concealing its true debt levels and inflating its reported profits was critical to Enron's illusion of success in the financial markets. As *The Wall Street Journal* reported on November 8, 2001:

> But to make all of its growth dreams possible, Enron had to make sure that its balance sheet didn't become too laden with debt. Too much debt would lead major ratings agencies, such as Moody's Investors Service and Standard & Poor's, to lower Enron's credit rating. Such downgrades could significantly increase the company's cost of borrowing and make it more difficult to finance its continued expansion.

Jaconette Decl., Ex. 8. Consequently, as late as August 29, 2001, defendant Lay lied – he assured securities analysts that the unexpected resignation of Enron's CEO, Skilling, was not cause to fear

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[7] ***John Wakeham***, who sits on the Audit Committee, has a $72,000-a-year consulting contract. Jaconette Decl., Ex. 15. ***LeMaistre*** headed the MD Andersen Cancer Center, and ***John Mendelsohn***, who sits on the Audit Committee, and who is president of the MD Andersen Cancer Center, received over $567,000 in donations to the Cancer Center in the last five years from Enron and Lay, and the Enron Foundation pledged $1.5 million for a new clinic. *Id.* Indeed, ***Wakeham***, ***Gramm*** and ***Mendelsohn***, who comprise half of Enron's Audit Committee, "are not independent, according to corporate governance experts and standards." *Id*. ***Belfer's*** Belco Oil & Gas Corp. had $32 million in trade settlements and $1 million in option premiums with Enron Trade Resources Corp., an Enron subsidiary. *Id*. ***John Urquhart*** received an annual consulting fee from Enron of almost $200,000 a year as a special advisor to Lay. *Id.* ***Herbert Winokur's*** Natco Group Inc. garnered $370,294 in sales to Enron subsidiaries in 2000 alone. *Id*.

that "the Company may be hiding dire financial news" and that there was "nothing wrong with the Company." ¶82.

e. The Restatements, Credit Downgrades and Bankruptcy

Two weeks later, Enron suddenly revealed that it would incur losses of $1 billion, and would reduce shareholder's equity on its balance sheet by $1.2 billion. Then, on November 8, 2001, ***Enron announced it was restating its results for 1997-2000, and the first two quarters of 2001 to correct for errors which had inflated Enron's net income by $591 million in those years***. The impact of the multiple restatements was enormous:

	1997	1998	1999	2000
Recurring Net Income				
As reported	$515,000,000	$698,000,000	$957,000,000	$1,266,000,000
As restated	$419,000,000	$585,000,000	$707,000,000	$1,134,000,000
Debt				
As reported	$6,254,000,000	$7,357,000,000	$8,152,000,000	$10,229,000,000
As restated	$6,965,000,000	$7,918,000,000	$8,837,000,000	$10,857,000,000
Shareholders' Equity				
As reported	$5,618,000,000	$7,048,000,000	$9,570,000,000	$11,470,000,000
As restated	$5,305,000,000	$6,600,000,000	$8,736,000,000	$10,306,000,000

Upon these shocking revelations, Enron's stock dropped to as low as $8.20 on November 8, 2001, some 91% below the Class Period high of $90.75. Then, two weeks later, the Company revealed a $690 million note on one of the limited partnerships was being called. Jaconette Decl., Ex. 16. By late November, the rating agencies had cut Enron's debt rating to "junk" status and Enron's stock collapsed to $0.28 per share. Jaconette Decl., Ex. 9. As one securities analyst stated, "Enron is finished as a going concern." Jaconette Decl., Ex. 17. Now Enron has made the largest Chapter 11 bankruptcy filing ever. Jaconette Decl., Ex. 18. Even with these catastrophic events, the Company has admitted that it has ***not completed*** its restatements or review of its accounting practices with respect to the limited partnerships and other questionable areas of its business. Jaconette Decl., Ex. 16.

f. The Enron Fraud Destroyed Retirements and Investor Confidence, Thus Private Equitable Remedies Are Imperative

Enron is a grotesque fraud – a financial monstrosity of manipulation and falsification. As a result, thousands of investors have been cheated out of billions of dollars and countless lives and retirements have been destroyed. Yet the perpetrators have over $1 billion in their pockets.[8] For illustration, had these Individual Defendants sold their stock at market prices reflecting the ***true state*** of Enron's financial condition, the Individual Defendants would have received only one percent of the $1.1 billion they reaped by selling at artificially inflated prices. *See* Jaconette Decl., Ex. 19. Conversely, public investors, including Amalgamated, who were on the buying side of the Individual Defendants' insider sales, lost over $25 billion. ***As a result of purchasing just the stock sold in the market by Enron insiders, public investors lost over $1 billion***.

The Individual Defendants, top executives at the Company who were knowledgeable about the limited partnerships and the financial manipulations, must accept responsibility for their blatant violations of the federal securities laws now exposed. As reported by *The Wall Street Journal*:

> [W]hat is most striking about the latest disclosures is that they show Enron's misstatements weren't limited merely to judgment calls and gray areas for the green-eyeshade crowd to debate. Portions of Enron's accounting practices amounted to violations of elementary accounting principles ....

Jaconette Decl., Ex. 23. Concerning Enron's restatements, the former Chief Accountant for the SEC, Lynn Turner, stated: "***It is basic accounting that you don't record equity until you get cash, and a note doesn't count as cash***." *Id*.

As Mr. Turner and numerous other securities experts recognize, the severe and flagrant nature of the Enron fraud upon its revelation is destroying investor confidence in the securities markets:

> ***Coming on the heels of a rash of similar situations – Cendant, Sunbeam, Waste Management, Xerox, Lucent, it goes on – this is just the tsunami that's going to destroy public confidence***.

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[8] We have been informed by sources that it was widely known inside Enron that top officers of the Company were pocketing additional large sums via the "sale" of Enron stock, using so-called "costless collar" transactions arranged by investment banking firms in a manner so that these "sales" were not reported via Form 4 filings.

* * *

> ***It is time – given the magnitude of this loss – for there to be a criminal investigation of the entire matter. Not just Andersen, but the C.F.O. and management team, because they're the ones who created the wrong numbers***. And this is the piece that I really hate: You've got 21,000 employees, many of whom had their retirement tied up in a 401(k) plan with Enron's stock. Those 21,000 people woke up wondering whether they were going to have jobs and wondering about Christmas, because a lot of people didn't do what they were supposed to do.

Jaconette Decl., Ex. 20 (emphasis added). Now it is widely known by the investing public that these bogus transactions were not the result of some low-level managerial shenanigans in a Bolivian subsidiary of a world-wide enterprise. ***These were huge, complex transactions specifically structured by Enron's top executives and approved by its Board that generated hundreds of millions of profits and equity***. Private equitable remedies are imperative here.

2. Plaintiff Seeks a Constructive Trust Pursuant to Equitable Remedies Under §§10(b) and 20A of the Securities Exchange Act of 1934 (Disgorgement of Insider Trading Proceeds) and §11 of the Securities Act of 1933

Amalgamated brings this application *ex parte* to prevent dissipation or concealment of insider trading proceeds in order to maintain the *status quo* and preserve its equitable remedies under the federal securities laws. *See, e.g., Board of Governors v. DLG Fin. Corp.*, 29 F.3d 993, 1002 (5th Cir. 1994) ("In general, prompt ex parte action is necessary to prevent persons ... from dissipating or concealing assets."). A constructive trust and immediate accounting is necessary to protect the Individual Defendants' insider trading proceeds from dissipation.

Amalgamated and the Class are entitled to the specific equitable relief sought herein, pursuant to §§20A, 27 and 28(a) of the Exchange Act and §11 of the Securities Act. *See infra* §II.B. The constructive trust and accounting Amalgamated seeks are necessary and especially appropriate to preserve Amalgamated's §§10(b) and 20A insider trading disgorgement claims. *See infra* §II.B.1-2. Amalgamated satisfies the prerequisites for the temporary injunctive relief sought.

There is certainly a ***reasonable probability of success*** that Amalgamated will prevail on its insider trading disgorgement claims under §§10(b) and 20A and its claims under §11. Professor Steinberg is the Radford Professor of Law at Southern Methodist University and practiced as an enforcement attorney at the SEC. He has authored numerous articles regarding SEC enforcement

and private securities litigation, and numerous textbooks regarding corporate and securities law. As Professor Steinberg declares, it is reasonable to infer that the Individual Defendants knew or were reckless in not knowing about the bogus deals and false reporting, given the positions held by the Individual Defendants at Enron and the basic nature of the inside information withheld. Steinberg Decl., ¶¶4-7. Indeed, the bogus transactions at issue were continuous, massive in scope and dollar amount, and basic to Enron's operations. Ample legal precedent supports this common sense proposition. *See infra* §II.C.1.a.2. Likewise, Enron's restatement of results from operations for 1997-2000 and the first two quarters of 2001 demonstrates a *prima facia* case of liability under §11 against the Individual Defendants who served as officers or directors during the Class Period or signed the Company's registration statements for its securities offerings. See *infra* §II.C.1.b.

Amalgamated and the Class will suffer irreparable harm unless the Court imposes a constructive trust upon the Individual Defendants' insider trading proceeds. *See infra* §II.C.2. As Professor Steinberg testifies, there is significant risk that the Individual Defendants' insider trading proceeds will be dissipated or diminished in this case. Steinberg Decl., ¶14. And disgorgement of the Individual Defendants' insider trading proceeds is the only viable avenue of recovery for Amalgamated's §§10(b) and 20A claims.[9] *See infra* §II.C.2. The law strongly supports plaintiff's claims of irreparable injury in this case.

The balance of hardships favors Amalgamated and the Class of public investors whose investments in Enron securities were destroyed by this massive fraud. *See* Steinberg Decl., ¶¶12-13. This enormous fraud has sent tremors throughout our public securities markets unlike anything in recent memory. Thousands of investors throughout the United States have lost significant portions of their retirement funds and institutions and pension funds have suffered billions in losses. The continuous high-profile coverage and reporting of the Enron fraud in the popular and financial media demonstrates the importance the public places on a just resolution of this financial catastrophe, and underlines the significance of this case to investor confidence in our securities markets ***and*** in our

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[9] While Enron no doubt has directors' and officers' ("D&O") liability insurance, these types of policies exclude coverage for insider trading claims and deliberate and dishonest acts. Also, Enron's D&O carriers may well seek to rescind, claiming they too were defrauded by Enron's false financial statements.

legal system to take prompt and decisive action to protect those victimized by these apparently deliberate violations of our federal securities laws. As *The New York Times* reported from its interview of Lynn Turner:

> Q. Are there other accounting time bombs, warning signs?
>
> A. Given the way audits have been conducted, more by inquiry than by real investigation in the last few years, ***we will undoubtedly see more. This is an iceberg, and the Titanic just hit it***.

Jaconette Decl., Ex. 20 (emphasis added). The SEC has commenced a formal investigation of this fraud and criminal inquiries are also imminent or ongoing. However, the massive scope of the fraud and importance of expeditious action to protect investors means that supplemental enforcement of the federal securities laws by private securities claims (as here) is even more important than usual. *See* Steinberg Decl., ¶11. After all, neither the SEC nor the Justice Department can recover damages for investors. The public interest as well as the facts calls for the prompt yet not unfair relief sought by Amalgamated.

B. The Particularized Expedited Discovery Sought by Amalgamated

Limited expedited discovery is critical to Amalgamated's ability to seek the equitable relief needed here. Amalgamated requests that it be permitted limited expedited discovery to further establish the Individual Defendants' insider trading and to determine the location, amount, and nature of insider trading proceeds and profits derived by certain defendants from the limited partnerships used as "straw" entities.

The discovery is limited or "particularized." *See infra* §IV.D. For example, documents evidencing defendants' knowledge during the Class Period are sought by plaintiff's requests for documents concerning the review of Enron's accounting practices, the restatement workpapers, Board reports and documents provided to the SEC. *See infra* §IV.G. Plaintiff's counsel are informed and believe from their investigation that massive trading in derivatives, such as zero-cost collars and equity swaps took place by the Individual Defendants. However, Amalgamated is also unable to allege the Individual Defendants' insider trading in derivative securities, therefore Amalgamated seeks account statements and summaries concerning these securities. *Id.*

Plaintiff's counsel are also informed and believe from their investigation that the involvement of certain executives at Enron in the limited partnership "straw" entities is far greater than what has been publicly disclosed, and there are tens of millions of dollars in hidden profits derived from these entities and held by defendants. Again, Amalgamated is unable to allege this involvement in order to seek equitable relief for claims arising out of defendants' profits derived from the limited partnerships. Thus, Amalgamated seeks documents focused on identifying Enron personnel in the limited partnerships and their profits derived therefrom. *See infra* §IV.G.

Amalgamated also requests depositions of defendants limited to two hours and not to exceed the scope of the subject matter of this Application and the documents Amalgamated seeks.

Besides its limited nature, the aim of Amalgamated's discovery (in part) is to leverage efforts that have already been made by defendants to gather documents in response to the Company's internal review of its accounting practices and the SEC's investigation. Accordingly, Enron and defendants' counsel should have these core documents in their possession and ready to produce expeditiously.

The expedited discovery Amalgamated seeks is warranted. There is a significant public interest served by this proceeding and the threat of irreparable injury to Amalgamated and the Class is great. *See infra* §II.C.2-4. With Enron's bankruptcy, there is no other source that investors may seek for the equitable relief to which they are entitled under the federal securities laws. *Id.* As Professor Steinberg declares, in a case such as this there is a significant risk that the Individual Defendants' insider trading proceeds will be diminished or dissipated. Steinberg Decl., ¶14. Precedent for granting expedited discovery when there is a threat of irreparable injury, such as here, is well established in the Fifth Circuit. *See infra* §IV.C. Discovery is not stayed under the PSLRA right now and even if a motion to dismiss were filed, the discovery Amalgamated seeks should be allowed to prevent undue prejudice for the same reasons that entitle Amalgamated to equitable relief. *See infra* §IV.E-F.

II. Argument

A. Legal Standards for Injunctive Relief

Plaintiff may seek a temporary restraining order on an *ex parte* basis. *See United States v. Hall*, 472 F.2d 261, 267 (5th Cir. 1972). This "ex parte request must be supported by a sworn documentary showing of 'immediate and irreparable injury,' as well as an explanation of why notice is impracticable or should not be required." *Marshall v. Reinhold Constr., Inc.*, 441 F. Supp. 685, 692 (M.D. Fla. 1977) (citation omitted). The primary purpose of a temporary restraining order is to "preserve the status quo only until a preliminary injunction hearing can be held." *Hoechst Diafoil Co. v. Nan Ya Plastics Corp.*, 174 F.3d 411, 422 (4th Cir. 1999). By this application, plaintiff also seeks an Order to Show Cause why a preliminary injunction should not issue.

The standard for a preliminary injunction requires that plaintiff demonstrate: (1) a substantial likelihood of success on the merits; (2) a substantial threat that the movant will suffer irreparable injury if the injunction is not issued; (3) that the threatened injury to the movant outweighs any damage the injunction might cause the opponent; and (4) that the injunction will not disserve the public interest. *See Blue Bell Bio-Medical v. Cin-Bad, Inc.*, 864 F.2d 1253, 1256 (5th Cir. 1989).

B. Amalgamated Is Entitled to the Equitable Relief Sought Herein Pursuant to the Federal Securities Laws

Section 27 of the Exchange Act confers general equity power upon district courts. *See SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1307 (2d Cir. 1971). And this Court has the power to grant the requested injunctive relief to preserve an equitable remedy. *See FDIC v. Dixon*, 835 F.2d 554, 560 (5th Cir. 1987) ("case law ***does*** allow district court [sic] to exercise its equitable powers in ordering a preliminary injunction to secure an equitable remedy"); *In re Estate of Marcos, Human Rights Litig.*, 25 F.3d 1467, 1480 (9th Cir. 1994); *SEC v. Int'l Swiss Inv. Corp.*, 895 F.2d 1272, 1276 (9th Cir. 1990) ("[t]he power to grant a preliminary injunction which freezes assets is among the district court's inherent equitable powers"); *International Controls Corp. v. Vesco*, 490 F.2d 1334, 1347 (2d Cir. 1974). Indeed, when justified, "a district court should temporarily freeze defendants' assets to insure that they will be available to compensate public investors." *SEC v. Manor Nursing Ctrs., Inc.*, 458 F.2d 1082, 1106 (2d Cir. 1972).

1. Imposition of Constructive Trust Over Insider Trading Proceeds

Amalgamated requests that a constructive trust immediately be placed over the Individual Defendants' insider trading proceeds to preserve Amalgamated's express remedy of disgorgement pursuant to §§10(b) and 20A of the Exchange Act and remedies under §11 of the Securities Act.[10] In this case, plaintiff seeks an order requiring each Individual Defendant to segregate all proceeds from Enron stock sales during the Class Period, in whatever present form those proceeds may be, and invest them in short-term (six months or less) United States Treasury securities.

As the Supreme Court stated in *J.I. Case Co. v. Borak*, 377 U.S. 426, 433 (1964), "[i]t is for the federal courts 'to adjust their remedies so as to grant the necessary relief' where federally secured rights are invaded." (Citation omitted.) It is well settled that the Court may impose a constructive trust as to a defendants' ill-gotten gains. *See Dixon*, 835 F.2d at 560; *Philippines v. Marcos*, 806 F.2d 344, 355 (2d Cir. 1986). Indeed, as the Fifth Circuit stated in *Dixon*, "there is no doubt that [a plaintiff] has the right (and even the responsibility) to pursue equitable causes of action such as a constructive trust, an accounting, and [disgorgement] when ... defrauded." 835 F.2d at 562. And this is especially appropriate "where the evidence strongly indicates that the assets were ill-gotten gains at the expense of an interest of the public protected by law." *Id.*; *see also SEC v. American Capital Invs.*, No. 95-55385, 1996 U.S. App. LEXIS 27685, at *8 (9th Cir. Oct. 22, 1996) (court may impose a constructive trust "'whenever required to prevent a person from being unjustly enriched by his wrongful conduct, even though there is no fiduciary or confidential relationship between the parties'") (citation omitted).[11]

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[10] Disgorgement is "an equitable remedy designed to deprive a wrongdoer of his unjust enrichment and to deter others from violating the securities laws." *SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1230 (D.C. Cir. 1989). Indeed, "disgorgement is rather routinely ordered for insider trading violations." *Id.* Courts in this circuit have similarly recognized disgorgement as "an equitable remedy designed to deprive defendants of all gains flowing from their wrong, rather than [merely] to compensate the victims of the fraud." *SEC v. AMX, Int'l*, 872 F. Supp. 1541, 1544 (N.D. Tex. 1994).

[11] The Texas court of appeals has recognized that "[t]he equitable remedy of constructive trust is broad and flexible." *Newman v. Link*, 866 S.W.2d 721, 725 (Tex. App. – Houston [14th Dist.] 1993). "'It is imposed by law because the person holding the title to property would profit by a wrong or would be unjustly enriched if he were permitted to keep the property.'" *Id.* (quoting *Omohundro v. Matthews*, 341 S.W.2d 401, 405 (1960)). "A transaction may, depending on the

The wrongs alleged by Amalgamated under §§10(b) and 20A, insider trading, relates perfectly to the equitable remedy of disgorgement of the insider proceeds which plaintiff seeks. Amalgamated's equitable remedy is expressly provided for under §§10(b) and 20A of the Exchange Act and this Court is authorized to secure that remedy. *See, e.g., SEC v. Brooks*, No. 3:99-CV-1326-D, 1999 U.S. Dist. LEXIS 10858, at *8 (N.D. Tex. July 12, 1999) ("the court is empowered to freeze defendants' assets to preserve the status quo and prevent dissipation of ill-gotten gains so that they remain available to pay subsequent disgorgement orders"); *SEC v. Hughes Capital Corp.*, 124 F.3d 449, 455 (3d Cir. 1997) ("[d]isgorgement is an equitable remedy designed to deprive a wrongdoer of his unjust enrichment'") (citation omitted).[12]

Likewise, plaintiff may seek such an equitable remedy for statutory violations under the Securities Act. *See* 15 U.S.C. §77k(a); *Deckert v. Independence Shares Corp.*, 311 U.S. 282, 287-88 (1940). *Accord Franklin v. Gwinnett County Pub. Sch.*, 503 U.S. 60, 68 (1992). In *Deckert*, securities purchasers sought an accounting, appointment of a receiver, and injunction *pendente lite*, and rescission in an action filed under §12 of the Securities Act. 311 U.S. at 288. The Supreme Court held that plaintiffs who have been injured as the result of defendants' violations of the federal securities laws may seek equitable relief to redress their injuries. *Id.* at 288-90.

2. Immediate Accounting of Insider Trading Proceeds

Amalgamated also requests an accounting of the insider trading proceeds to prevent dissipation. By asking for an accounting, Amalgamated requests that the Court order the Individual Defendants to provide, among other things, the name and account number for all bank accounts held by the defendants, every transaction in which any funds or assets were taken from those accounts,

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circumstances, provide the basis for a constructive trust where one party to that transaction holds funds which in equity and good conscience should be possessed by another." *Meadows v. Bierschwale*, 516 S.W.2d 125, 131 (Tex. 1974).

[12] *See also SEC v. Cross Fin. Servs.*, 908 F. Supp. 718 (C.D. Cal. 1995); *Neomonitis v. Blackie*, No. SA CV 94-379 AHS (RWRx), Order (C.D. Cal. June 20, 1994) ("*Platinum*") (Jaconette Decl., Ex. 10); *Miller v. Telios Pharms., Inc.*, No. 94-1554-IEG (RBB), Temporary Restraining Order and Order to Show Cause re: Preliminary Injunction to Freeze or to Impose a Constructive Trust Over Remaining Proceeds From Public Stock Offering (S.D. Cal. Jan. 11, 1995) ("*Telios*") (Jaconette Decl., Ex. 11); *In re California Micro Devices Sec. Litig.*, No. C-94-2817-VRW, Preliminary Injunction Order (N.D. Cal. May 29, 1996) (Jaconette Decl., Ex. 12).

and a listing of all transactions involving investments of funds from stock sales. *See SEC v. Bankers Alliance Corp.*, 881 F. Supp. 673, 677 (D.D.C. 1995).[13] When a constructive trust is imposed on defendants' ill-gotten gains, defendants must make an accounting to the court and plaintiff. *See FDIC*, 835 F.2d at 560; *USACO Coal Co. v. Carbomin Energy, Inc.*, 689 F.2d 94, 97 (6th Cir. 1982). An "accounting" is "an action for equitable relief against a person in a fiduciary relationship to recover profits taken in a breach of the relationship." *Blacks Law Dictionary* at 20 (7th ed. 1999). The purpose of an accounting is "'avoiding unjust enrichment. In this sense it reaches monies owed by a fiduciary or other wrongdoer, including profits produced by property which in equity and good conscience belonged to the plaintiff.'" *Id.* (quoting Dan B. Dobbs, *Law of Remedies* §4.3(5), at 408 (2d ed. 1993)). The accounting of funds in this case will assist the parties and the Court in preventing the dissipation of insider trading proceeds upon which the constructive trust is placed.[14] *See FDIC*, 853 F.2d at 560.

C. Amalgamated Satisfies the Prerequisites for Injunctive Relief

1. Amalgamated Has a Substantial Likelihood of Success on the Merits

In determining the probability of success on the merits, courts apply a flexible approach. *See Regents of University of Cal. v. Am. Broad. Cos.*, 747 F.2d 511, 515 (9th Cir. 1984). Thus, although a plaintiff seeking an injunction bears the burden of showing probability of success,

> [he] is not required to prove to a moral certainty that his is the only correct position. The prerequisite, as an absolute, is more negative than positive: one cannot obtain a preliminary injunction if he clearly will not prevail on the merits; however, that he is unable, in an abbreviated proceeding, to prove with certainty eventual success does not foreclose the possibility that ***temporary restraint*** may be appropriate.

Texas v. Seatrain Int'l, S.A., 518 F.2d 175, 180 (5th Cir. 1975) (emphasis added). Hence, "[i]n a preliminary injunction context, the movant need not prove his case." *See Lakedreams v. Taylor*, 932

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[13] *See also FTC v. Sage Seminars*, 1995-2 Trade Cas. (CCH) ¶71,256, at 76,117-18 (N.D. Cal. 1995); *SEC v. Telecom Mktg., Inc.*, 888 F. Supp. 1160, 1170 (N.D. Ga. 1995); *Bankers Alliance*, 881 F. Supp. at 676; *FTC v. International Computer Concepts*, 1995-2 Trade Cas. (CCH) ¶71,178, at 75,705-06 (N.D. Ohio 1995); *SEC v. Parkersburg Wireless Ltd. Liab. Co.*, 156 F.R.D. 529, 532 (D.D.C. 1994).

[14] Plaintiffs seek and are entitled to a ***full*** accounting of all Enron stock transactions by insiders, ***not*** just the publicly reported insider sales. This information regarding costless collar and other transactions whereby Enron insiders got money for Enron stock or stock options must be provided.

F.2d 1103, 1109 n.11 (5th Cir. 1991). The standard has been described as both a probability that the necessary facts can be proved and a fair chance of success on the merits. *Sierra On-Line, Inc. v. Phoenix Software*, 739 F.2d 1415, 1423 (9th Cir. 1984).

a. Sections 10(b) and 20A Insider Trading Claims

To prevail on a claim for insider trading under §§10(b) and 20A of the Exchange Act, a plaintiff need only establish that he traded "contemporaneously" with insiders who traded while possessing material inside information. *See Neubronner v. Milken*, 6 F.3d 666, 670 n.5 (9th Cir. 1993); *accord United States v. O'Hagan*, 521 U.S. 642, 650-51 (1997).[15] Amalgamated demonstrates a reasonable probability of success in establishing insider trading claims here.

(1) Amalgamated Traded Contemporaneously with the Individual Defendants

When Congress passed §20A, it intentionally refused to define what constituted "contemporaneous," instead intending to adopt the definitions developed through case law. *Neubronner*, 6 F.3d at 670 n.5. In passing the statute, however, Congress cited three cases which exemplified "contemporaneous" insider trading. *Id.* One of those cases, *O'Connor & Assocs. v. Dean Witter Reynolds, Inc.*, 559 F. Supp. 800 (S.D.N.Y. 1983), found that trades within seven days were contemporaneous. *Id.* at 805 n.5. Accordingly, in enacting §20A, Congress, at a minimum, intended a seven-day period was contemporaneous.

Amalgamated traded on the ***same day*** with as many as thirteen of the Individual Defendants, and thus traded contemporaneously with Baxter's stock sales on 1/31/00; with Belfer's stock sales

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[15] Section 10(b) of the Exchange Act and SEC Rule 10b-5 promulgated thereunder impose civil liability if a person employs devices, schemes and artifices to defraud; makes untrue statements of material facts or omits to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or engages in acts, practices and a course of business which operates as a fraud or deceit in connection with the purchase or sale of a security. *See* 15 U.S.C. §78j(b); 17 C.F.R. §240.10b-5.

Rule 10b-5 bars not just individual misleading statements or omissions, but "any device, scheme, or artifice to defraud." 17 C.F.R. §240.10b-5. Anyone who engages in a fraudulent scheme can be liable under §10(b). *See Shores v. Sklar*, 647 F.2d 462, 468-69 (5th Cir. 1981) (en banc). "It is no answer to urge that ... defendants may have made no positive representation or recommendation." *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 153 (1972); *accord O'Hagan*, 521 U.S. at 650-51.

on 5/15/00; with Derrick's stock sales on 2/5/99, 6/11/01 and 6/12/01; with Fastow's stock sales on 4/30/99 and 11/1/00; with Frevert's stock sales on 4/30/99, 9/12/00 and 12/20/00; with Harrison's stock sales on 4/30/99, 5/15/00 and 9/1/00; with Hirko's stock sales on 4/20/00; with Horton's stock sales on 9/14/00; with Lay's stock sales on 9/3/99, 4/20/00, 11/1/00, 11/22/00, 12/1/00, 12/21/00, 12/22/00, 2/2/01, 3/6/01, 4/3/01, 5/18/01, 6/11/01, 6/12/01 and 6/20/01; with Olson's stock sales on 12/22/00; with Pai's stock sales on 4/20/00, 5/15/00 and 5/18/01; with Rice's stock sales on 4/19/00, 2/2/01, 3/6/01, 4/3/01, 5/18/01, 6/11/01 and 6/12/01; with Skilling's stock sales on 4/16/99, 9/1/00, 11/1/00, 11/22/00 and 12/20/00; and with Sutton's stock sales on 9/14/00.

Plaintiff submits that the breadth of Amalgamated's stock purchases contemporaneous with the Individual Defendants' insider trading throughout the Class Period makes Amalgamated more than adequate as a Class representative for purposes of §§10(b) and 20A claims. However, plaintiff's counsel represent numerous individuals and institutions whose stock trading data, too voluminous to detail here, will likely include contemporaneous purchases (under any standard) with each of the Individual Defendants' insider sales.

(2) The Individual Defendants Traded While Possessing Material Inside Information

Enron's restatements of its financial statements for 1997-2000 and the first two quarters of 2001 are an admission that material inside information at Enron severely contradicted the Company's publicly reported results from operations. *See* Jaconette Decl., Ex. 13 at 5 ("Table 1"). And the Individual Defendants, top executives at the Company, knew that inside information, namely that, among other things, Enron was doing billions of dollars of bogus deals with "straw" entities, formed in part by Enron executives, to increase reported earnings and reduce reported debt. Former SEC enforcement attorney Professor Steinberg states in his declaration that it is reasonable to infer that the Individual Defendants knew (or were reckless in not knowing) about the bogus deals and false reporting, given the positions held by such Individual Defendants at Enron.

First, it is well established that a restatement of earnings is an admission of materially false financial statements. *See, e.g., In re Cendant Corp. Litig.*, 60 F. Supp. 2d 354 (D.N.J. 1999); *Mowbray v. Waste Mgmt. Holdings, Inc.*, 189 F.R.D. 194, 195-96 (D. Mass. 1999) ("restatement

constituted an admission that [defendant] had breached its warranty to [investors] that its financial statements adequately represented the fiscal health of the company"), *aff'd*, 208 F.3d 288 (1st Cir. 2000); *In re Physician Corp. of Am. Sec. Litig.*, 50 F. Supp. 2d 1304, 1317 n.17 (S.D. Fla. 1999) ("facts demonstrating [an] overstatement of revenues and income in violation of GAAP may constitute the false and misleading statements of material fact necessary for alleging a violation of Rule 10b-5"). Public disclosure, including information in periodic reports, must be accurate and complete. 17 C.F.R. §240.12b-20; Item 303 of Regulation S-K; Regulation S-X, Section 4-01(a). Periodic reports containing financial statements not prepared in accordance with GAAP are presumed to be misleading. *See* Regulation S-X, Section 4-01(a)(1); *see also In the Matter of Frank J. Cooney*, Exchange Act Release No. 40170, 1998 SEC LEXIS 1363, at *5 n.4 (July 6, 1998).

Charles Drott is a Certified Fraud Examiner with over 37 years of professional experience who practiced as an audit partner at two major accounting firms. *See* Declaration of Charles Drott ("Drott Decl."), ¶¶1-5. As Mr. Drott states:

> ***The restatement of previously issued financial statements is a significant non-routine event that can dilute investor confidence in the financial reporting process.*** Reporting the correction of errors is a primary reason for the restatement of previously issued financial statements. Errors in financial statements result from mathematical mistakes, mistakes in application of accounting principles, or oversight or misuse of facts that existed at the time the financial statements were prepared. In contrast, a change in accounting estimate results from new information or subsequent developments and accordingly from better insight or improved judgment. Thus, an error is distinguished from a change in estimate. Accounting Principles Board Opinion ("APB") 20, ¶13. The correction of an error in the financial statements of a prior period discovered subsequent to their issuance should be reported as a prior period adjustment. APB 20, ¶36.
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> * * *
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> ***The occurrence of a restatement also indicates that the error was material.*** *See* APB No. 20, ¶38.
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> ***In sum, Enron's restatement clearly indicates that the financial statements at issue, were in error and materially misstated at the time they were originally reported.***

Drott Decl., ¶¶10, 13-14 (emphasis added).

Enron has embarked upon a massive restatement of its results from operations for a four-and-a-half year period. Accordingly, material inside information at Enron was inconsistent with the Company's publicly reported results from operations.

Second, given that the transactions with the limited partnerships (among others) were continuous, massive in scope and dollar amount, and so basic to Enron's operations, the Individual Defendants must have directly participated in the transactions or known of their existence. Indeed, each of the Individual Defendants held top level positions at Enron. *See* Table *supra* at 3-4. These facts entitle Amalgamated to a strong inference that the Individual Defendants were in possession of the inside information – that disintegrated Enron upon disclosure – when the Individual Defendants traded their stock during the Class Period. *See, e.g., Nathenson v. Zonagen Inc.*, 267 F.3d 400 (5th Cir. 2001) (plaintiff entitled to a strong inference of scienter against director and CEO who possessed material, nonpublic information concerning company's core products); *Cosmas v. Hassett*, 886 F.2d 8, 12-13 (2d Cir. 1989); *In re Triton Energy Ltd. Sec. Litig.*, No. 5:98-CV-256, 2001 U.S. Dist. LEXIS 5920, at *6-*11 (E.D. Tex. Mar. 30, 2001); *STI Classic Fund v. Bollinger Indus.*, No. 3-96-CV-823-R, 1996 U.S. Dist. LEXIS 21553, at *7 (N.D. Tex. Oct. 25, 1996); *Epstein v. Itron, Inc.*, 993 F. Supp. 1314, 1326 (E.D. Wash. 1998) ("facts critical to a business's core operations or an important transaction generally are so apparent that their knowledge may be attributed to the company and its key officers").

In *Cosmas*, the Second Circuit held plaintiffs pleaded "facts which give rise to a strong inference that the defendants possess the requisite fraudulent intent" by alleging facts from which one could reasonably infer sales to a foreign country were a significant part of the company's business. 886 F.2d at 12-13. The Second Circuit explained the facts of which the company's directors were allegedly aware affected a "potentially significant source of income for the company," thus giving rise to a strong inference of the defendants' knowledge and fraudulent intent. *Id.* at 13.

District courts in Texas permit this strong inference when accounting irregularities arise. In *Triton*, plaintiffs filed suit against Triton because, among other things, the company's financial statements contained a number of material misrepresentations and were in violation of GAAP. 2001

U.S. Dist. LEXIS 5920, at *6-*11. The *Triton* court held plaintiffs' allegations were sufficient to impute knowledge to the defendants, including the company's chairman, CEO, and CFO:

> Plaintiffs do not simply argue scienter by virtue of Defendants' positions and experience. Rather, as discussed above, Plaintiffs contend that Defendants' positions and experience are factors that pled with others (e.g., the size of the accounting irregularities and that they pertained to Triton's most important assets) state scienter with the required measure of specificity.

Id. at *35. Chief Judge Buchmeyer of the Northern District of Texas has applied the same common-sense analysis to find a strong inference that senior management knew of serious problems affecting their business. *See STI*, 1996 U.S. Dist. LEXIS 21553, at *7 ("Based upon their respective positions with the company, a strong inference may be drawn that they were knowledgeable about the methods and billing practices ... which led to the over-stated sales and revenues ...."). Moreover, although plaintiff need not demonstrate this to support §20A claims, as shown herein, the bases for Enron's restatements support an inference that ***fraud*** caused Enron's materially false and misleading financial statements.[16]

The facts above, given their due inference, demonstrate a *prima facie* case of liability under §20A of the Exchange Act, and a reasonable probability of success on Amalgamated's §20A claims.

b. Section 11 Claims Pursuant to the Securities Act

Section 11 imposes liability if "any part of the registration statement ... contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statement therein not misleading." 15 U.S.C. §77k(a). Section 11 was designed to assure compliance with the disclosure provisions of the Securities Act by imposing a stringent standard of liability on parties who play a direct role in a registered offering. *Herman & MacLean v. Huddleston*, 459 U.S. 375, 381-82 (1983). "Under Section 11 a purchaser of securities

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[16] *See, e.g., In re Discovery Zone Sec. Litig.*, 943 F. Supp. 924, 937 (N.D. Ill. 1996) ("the alleged GAAP violations alone support an inference of fraudulent intent," where defendants "allegedly used improper accounting methods to 'artificially enhance ... profits'") (citation omitted); *Sirota v. Solitron Devices, Inc.*, 673 F.2d 566, 573 (2d Cir. 1982) ("subsequent admissions of misrepresentations, coupled with the defendants' continuous intimate knowledge of company affairs," permitted inference that defendants knew or should have known about previous misstatements in financial statements). *Cf. Malone v. Microdyne Corp.*, 26 F.3d 471, 478 (4th Cir. 1994) ("We cannot find a single precedent ... holding that a company may violate FAS 48 and substantially overstate its revenues by reporting consignment transactions as sales without running afoul of Rule 10b-5.").

need only show a material misstatement or omission in a registration statement to establish a *prima facie* case." *Greenwald v. Integrated Energy, Inc.*, 102 F.R.D. 65, 71 (S.D. Tex. 1984).

Numerous cases have adopted a *per se* rule that misrepresenting a company's financial performance is material misstatement. *See, e.g., SEC v. Murphy,* 626 F.2d 633, 653 (9th Cir. 1980); *Rubinstein v. Collins*, 20 F.3d 160, 169 (5th Cir. 1994); *Cendant*, 60 F. Supp. 2d 354; *Physician Corp.*, 50 F. Supp. 2d at 1317 n.17 (description *supra* at 17); *Mowbray,* 189 F.R.D. at 195-96 (description *supra* at 17). Enron's restatements are an admission that the Company's results from operations were materially misstated. *See supra* §II.C.1.a.(2); Jaconette Decl., Ex. 13 at 5 ("Table 1"). Accordingly, by presenting evidence of Enron's restatements, Amalgamated has established a *prima facie* case for liability. Each Individual Defendant who signed Enron's registration statements and each Individual Defendant who served as an Enron director during the Class Period is expressly liable for securities violations under §11 unless they can establish a successful due diligence defense. 15 U.S.C. §77k(a)(1)-(3). Amalgamated thus demonstrates a reasonable probability of success on the merits of its §11 claims.

2. Plaintiffs Will Suffer Irreparable Harm Unless the Court Freezes Individual Defendants' Insider Trading Proceeds

Disgorgement of the Individual Defendants' insider trading proceeds is the only viable avenue of recovery for Amalgamated's §§10(b) and 20A claims and equitable claims under §11. D&O liability insurance – even if it exists and is effective – will provide a minuscule fraction of the $25 billion-plus damages arising out of defendants' violations of the federal securities laws. The Enron fraud presents significant potential for liability of accountants, lawyers, and investment bankers; however, there can be no assurance of recovery from these actors and none of them face a §20A insider trading claim nor are they in possession of over $1 billion in insider trading proceeds. Enron's bankruptcy forecloses any reasonable probability of recovery against it. Therefore, the threat that the Individual Defendants' insider trading proceeds will be dissipated means that, absent a constructive trust, Amalgamated and the Class will be irreparably injured.

When (as here) a plaintiff seeks equitable relief, "'[t]he absence of an available remedy by which the movant can later recover monetary damages'" raises a presumption of irreparable injury.

Dixon, 835 F.2d at 560 n.1 (citation omitted). Likewise, plaintiff is ***not*** required to prove that future uncollectibility is a certainty; rather, the ***possibility*** that property will be irretrievably dissipated "is itself sufficient to support a finding of irreparable injury." *Republic of Panama v. Panama Air Internacional, S.A.*, 745 F. Supp. 669, 674 (S.D. Fla. 1988). In similar circumstances, courts have consistently held that preliminary injunctive relief in the form of an asset freeze/constructive trust is appropriate to prevent the dissipation of assets before judgment. *See, e.g., Board of Governors*, 29 F.3d at 1002 ("In general, prompt ex parte action is necessary to prevent persons ... from dissipating or concealing assets."); *Deckert*, 311 U.S. at 290 (upholding preliminary injunction and asset freeze to preserve the plaintiffs' damages remedy); *Republic of Philippines v. Marcos*, 862 F.2d 1355, 1364 (9th Cir. 1988) (same); *Nguyen v. FundAmerica*, [1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶95,498, at 97,586 (N.D. Cal. 1990) (same); *Commodity Futures Trading Comm'n v. Morgan, Harris & Scott, Ltd.*, 484 F. Supp. 669, 678 (S.D.N.Y. 1979) (same).[17]

In *Heckmann v. Ahmanson*, 168 Cal. App. 3d 119, 134-35 (1985), the California Court of Appeals recognized that "absent an injunction, the proceeds ... of the transaction would be dissipated by the time a final judgment could be obtained," destroying plaintiffs' equitable remedy and rendering any final judgment ineffectual. *Id.* at 137. The *Heckmann* court enjoined defendants from "transferring, investing or disposing of the profit from its sale of ... stock except in accordance with the standards applicable to a prudent trustee," and required that defendants "notify plaintiffs and the court of every change in the form or vehicle of investment of the entire proceeds." *Id*. at 125 (footnote omitted).

Similarly, in *California Micro Devices* (Jaconette Decl., Ex. 12), the court granted a preliminary injunction freezing a defendant's insider trading proceeds. There, as here, a senior

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[17] Recently, the U.S. Supreme Court in *Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund*, 527 U.S. 308 (1999), clarified that a trial court has the ability to freeze assets in actions involving equitable claims, such as unjust enrichment. *Id*. at 310 ("***in an action for money damages***," the district court does not have the "power to issue a preliminary injunction preventing the defendant from transferring assets ***in which no lien or equitable interest is claimed***") (emphasis added). Indeed, the court in *Grupo* specifically held that "[t]he preliminary relief available in a suit seeking ***equitable*** relief ***has nothing to do with*** the preliminary relief available ... in the collection of a ***legal*** debt." *Id.* at 325 (emphasis added). *See also United States ex rel. Rahman v. Oncology Assocs.*,198 F.3d 489, 492-93 (4th Cir. 1999) (holding *Grupo* inapplicable where a court exercising its equitable powers is imposing a constructive trust over assets obtained through fraud).

executive of the company profited by millions of dollars by selling company stock. Enjoining the defendant from selling "any and all" of his shares of company stock, the court held:

> WHEREAS, it appears that there is substantial likelihood that the class represented by plaintiff Colorado Public Employees' Retirement Association in the within action will recover a judgment against defendant Chan Desaigoudar in an amount greater than his assets;
>
> * * *
>
> IT IS HEREBY ORDERED that defendant Chan M. Desaigoudar be, and he hereby is, preliminarily enjoined from selling or encumbering any and all shares of California Micro Devices Corporation stock in which he has an interest ....

Order at 1-2.

Likewise, in *Platinum* (Jaconette Decl., Ex. 10), the court restricted defendants' use of unlawfully obtained insider trading proceeds, holding:

> The evidentiary submission, briefs, and arguments of plaintiffs to this Court have raised a serious question as to whether defendants named above have performed their fiduciary duties and, if not, have been unjustly enriched as a result thereof ... absent imposition of this Order, the proceeds from the insider sales by defendants may be spent or dissipated before trial and judgment. Accordingly, plaintiffs' application has satisfied applicable standards for the issuance of preliminary injunctive relief ....

Order at 1.

Here, as in the cases cited above, freezing proceeds unlawfully obtained is necessary to preserve the *status quo*.

3. The Balance of Hardships Tips Sharply in Plaintiff's Favor

The Court must also weigh the threatened injury to plaintiff against any harm to the Individual Defendants. *See Dixon*, 835 F.2d at 559. But when balancing the hardships of the public interest against a private interest, the public interest should receive greater weight. *See FTC v. World Wide Factors*, 882 F.2d 344, 346-47 (9th Cir. 1989).

As declared by Professor Steinberg, here, the balance of hardships favors plaintiff and the Class. *See* Steinberg Decl., ¶¶12-13. This enormous fraud has scandalized our public securities markets. Thousands of investors throughout the United States have lost significant portions of their retirement funds and institutions and pension funds have suffered losses measured in the billions of dollars. The intense media coverage of the Enron fraud demonstrates the importance of this financial

catastrophe, and underlines the significance of this case to investor confidence in the securities markets of the United States. Although the SEC has commenced a formal investigation, the SEC cannot recover money damages for investors. Given the massive scope of the restatements and the importance of expeditious action to protect investors, supplemental enforcement of the federal securities laws by the private securities claims asserted here is even more important than usual. *See* Steinberg Decl., ¶11. After all, neither the SEC nor the Justice Department can recover damages for investors, and the fact that wrongdoers might end up in a federal prison provides no damage recovery or compensation to victims. Compromised investor confidence in the integrity of the capital markets calls for the prompt yet not unfair relief sought by Amalgamated.

By contrast, the imposition of a constructive trust, which allows the Individual Defendants to ***retain*** the benefits and invest the proceeds of their insider trading in conservative investment vehicles, will impose little if any hardship on the Individual Defendants. Indeed, the Ninth Circuit has observed that there is no "'oppressive hardship'" in requiring the Individual Defendants to "preserve their assets from dissipation or concealment." *World Wide Factors*, 882 F.2d at 347 (citation omitted). Following this rationale, the court in *Heckmann* held "we believe the trial court reasonably concluded detriment to the plaintiffs if the proceeds and profits are dissipated or untraceable exceeds any hardship to the [defendants] in complying with the investment and accounting provisions of the preliminary injunction." 168 Cal. App. 3d at 138.

The proposed Temporary Restraining Order and Order to Show Cause will not unfairly harm the Individual Defendants because it is narrowly tailored. It only requires that the Individual Defendants account for, segregate, and invest their insider-trading proceeds. It also provides them a mechanism for release of the proceeds with the Court's permission if hardship so requires. Thus, the true "hardship" on the Individual Defendants if the requested relief is granted is *de minimis*, if any exists at all. Accordingly, the balance of hardships tips sharply in plaintiff's favor.

4. Granting Preliminary Injunctive Relief Will Serve the Public Interest

The Court must also evaluate whether the effect of the injunction will disserve the public interest. *Dixon*, 835 F.2d at 559. But, as shown above, the public interest will be ***advanced*** by the

injunctive relief sought herein.

Here, as in *Nguyen*, "[t]he public interest in preserving the integrity of the marketplace, and the enforcement of federal ... laws designed to protect investors and consumers, sharply favors the plaintiffs." ¶95,498, at 97,586. Indeed, the PSLRA itself embodies Congress's belief that private actions are an "indispensable tool with which defrauded investors can recover their losses," "promote ... confidence in our capital markets and help to deter wrongdoing." H.R. Conf. Rep. No. 104-369, at 31 (1995), *reprinted in* 1995 U.S.C.C.A.N. 679, 730. Compromised investor confidence in the integrity of the capital markets calls for the prompt yet not unfair relief sought by Amalgamated. The constructive trust sought by Amalgamated will preserve a small but critical remedy for Enron's public investors while the Court has an opportunity to render a meaningful decision on the merits of this action. Conversely, the public interest would be harmed if the Individual Defendants were permitted to unjustly enrich themselves at plaintiff's expense and deprive shareholders adequate recovery through dissipation of the massive insider trading proceeds they reaped.

III. A Bond Is Not Necessary

The posting of a bond is not a prerequisite to the issuance of a temporary restraining order or a preliminary injunction in this case because the Individual Defendants cannot demonstrate that preserving the *status quo* will cause them recognizable economic harm. *See FTC v. Southwest Sunsites, Inc.*, 665 F.2d 711, 714 n.1 (5th Cir. 1982) ("a temporary restraining order or a preliminary injunction may be granted without bond"); *see also International Controls Corp. v. Vesco*, 490 F.2d 1334, 1356 (2d Cir. 1974). Because the insider trading proceeds will be placed in an escrow account (with the cash earning interest), the Individual Defendants cannot be harmed if preliminary injunctive relief is granted. *See In re Holborn Oil Trading, Ltd. v. Interpetrol Bermuda, Ltd.*, 658 F. Supp. 1205, 1211-12 (S.D.N.Y. 1987) ("Where, as here, the preliminary injunction is phrased in terms of payment of an arbitration award into the registry of this Court such that the funds earn interest during the pendency of this action, the Court finds that the posting of a security is not necessary because there is no demonstration of harm ... as a result of the imposition of the injunction."). Moreover, in the unlikely event that the Individual Defendants are successful at trial, all withheld proceeds will be released, with interest having accrued during the interim. And, in the

event a defendant may suffer a financial hardship requiring use of their proceeds, an application may be made to the Court for relief. Accordingly, a bond is not necessary.

IV. Amalgamated Should Be Permitted to Take Limited Expedited Discovery to Further Establish the Individual Defendants' Insider Trading and Determine the Location, Amount, and Nature of Insider Trading Proceeds and Profits Derived by Certain Individual Defendants from "Straw" Entities

A. Insider Trading Discovery

Amalgamated requires limited expedited discovery to further establish the Individual Defendants' insider trading, and determine the location, amount, nature, and current or planned disposition of the Individual Defendants' insider trading proceeds. For example, at this time, plaintiff cannot allege the full extent of the Individual Defendants' insider trading. Plaintiff's counsel are aware, however, that the Individual Defendants traded in various unreported derivative securities, including, but not limited to, zero-cost collars and equity swaps. (Reporting requirements and standards for these transactions have not yet been promulgated by the SEC.) Amalgamated is unable to obtain adequate records of the Individual Defendants' trades in these securities without the availability of discovery.

B. Limited Partnership/"Straw" Entities Discovery

Amalgamated also requires limited expedited discovery to identify all of Enron's officers and executives who profited from Enron's "straw" entities, as well as the location, amount, nature, and current or planned disposition of those persons' ill-gotten profits from those entities. For example, it has been revealed that defendant Fastow and certain other executives at Enron formed and operated the "straw" limited partnerships that were an essential device to the fraud, and that Fastow made millions of dollars thereby. *See* Jaconette Decl., Ex. 13 at 9-11, 19-20 ("The LJM Partnerships") ("Other Employee Transactions"). Any such profits should be subject to a constructive trust, just as the Individual Defendants' insider trading proceeds. However, Amalgamated requires further information in order to apply to the Court for that equitable relief. Therefore, Amalgamated requests documents from Enron and defendant Arthur Andersen concerning the review of Enron's accounting practices, the restatement workpapers, Board reports and documents provided to the SEC.

C. This Court May Grant Expedited Discovery

The Federal Rules of Civil Procedure allow a party to seek expedited discovery. Fed. R. Civ. P. 34(b), 26(d). "It is clear from this language [Rule 34(b)] that the rules intend to vest discretion in the Court to extend or shorten time for production of documents." *First Commonwealth Corp. v. Public Investors, Inc.*, No. 90-3316, 1990 U.S. Dist. LEXIS 12743, at *2 (E.D. La. Sept. 25 1990). Precedent for expedited discovery under similar circumstances is well established in the Fifth Circuit. *See, e.g., FMC Corp. v. Varco Int'l, Inc.*, 677 F.2d 500 (5th Cir. 1982) (one week of expedited discovery before hearing on preliminary injunction); *Citizens Sav. Bank v. GLI Tech. Servs.*, No. 96-2307-L, 1996 U.S. Dist. LEXIS 19128, at *3 (E.D. La. Dec. 20, 1996) (plaintiff's motion for expedited discovery granted where plaintiff sought to recover money from a loan agreement); *Quilling v. Funding Resource Group*, 227 F.3d 231, 233 (5th Cir. 2000) (in fraudulent securities scheme, district court properly ordered discovery and froze assets); *Mesa Petroleum Co. v. Aztec Oil & Gas Co.*, 406 F. Supp. 910, 917 (N.D. Tex. 1976). Indeed, "[e]xpedited discovery is particularly appropriate when a plaintiff seeks injunctive relief because of the expedited nature of injunctive proceedings." *Ellsworth Assocs. v. United States*, 917 F. Supp. 841, 844 (D.D.C. 1996); *accord Optic-Electronic Corp. v. United States*, 683 F. Supp. 269, 271 (D.D.C. 1987).[18]

D. Limited or "Particularized" Expedited Discovery Is Warranted

Limited expedited discovery in this case is warranted given the nature of the equitable relief Amalgamated seeks and the public interest served by this proceeding, as set forth herein. *See supra* at §II.C.3-4. The threat of irreparable injury is significant here, *a fortiori*, good cause exists for expedited discovery. *See supra* §II.C.2. Amalgamated's discovery is limited in scope and duration and attempts to leverage efforts that have already been made by Enron and the Individual Defendants to gather documents. *See supra* §IV.A-B. For example, documents evidencing the Individual Defendants' knowledge during the Class Period are sought by plaintiff's requests for documents

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[18] *See also SEC v. Sterns*, No. 91-1303-ER(Tx), 1991 U.S. Dist. LEXIS 13968, at *1 n.2 (C.D. Cal. Aug. 22, 1991) ("[i]n addition to the asset freeze, this Court also granted the Commission's requests for ... an order granting expedited discovery"), *aff'd*, 993 F.2d 884 (9th Cir. 1993); *FTC v. Magui Publishers, Inc.*, 1991-1 Trade Cas. (CCH) ¶69,425 (C.D. Cal. 1991); *SEC v. International Loan Network, Inc.*, 770 F. Supp. 678 (D.D.C. 1991), *aff'd*, 968 F.2d 1304 (D.C. Cir. 1992).

concerning the review of Enron's accounting practices, the restatement workpapers, Board reports and documents provided to the SEC. Especially given the SEC's investigation, Enron and the Individual Defendants' counsel should have these core documents in their possession. In any event, production of these documents can be completed promptly.

E. Discovery Is Not Stayed Under the PSLRA at This Time

In enacting the PSLRA, Congress established a limited exception to the broad discovery provisions of the Federal Rules of Civil Procedure. In class actions arising under the federal securities laws, discovery

> shall be stayed during the pendency of any motion to dismiss, unless the court finds upon the motion of any party that particularized discovery is necessary to preserve evidence or to prevent undue prejudice to that party.

15 U.S.C. §78u-4(b)(3)(B). Thus, the plain language of the statute stays "discovery ... ***only when a motion to dismiss has actually been filed***." *Dartley v. Ergobilt, Inc.*, No. 3:98-CV-1442-G, 1998 U.S. Dist. LEXIS 17751, at *5 (N.D. Tex. Nov. 4, 1998) (emphasis added). Accordingly, allowing plaintiff to proceed with discovery in order to prevent the Individual Defendants from secreting or absconding with ill-gained proceeds does not violate the PSLRA. *Id.*; 15 U.S.C. §78u-4(b)(3)(B).

F. Even if the Individual Defendants Sought a Discovery Stay, Limited ("Particularized") Discovery Should Be Allowed to Prevent Undue Prejudice

Under 15 U.S.C. §77z-1(b)(1), "'particularized discovery'" may be allowed, despite the strictures of the PSLRA's discovery stay, to "'preserve evidence ***or*** to prevent undue prejudice'" to the party requesting discovery. *Dartley*, 1998 U.S. Dist. LEXIS 17751, at *5 (citation omitted, emphasis added). *Accord Anderson v. First Sec. Corp.*, 157 F. Supp. 2d 1230, 1242 (D. Utah 2001) (plaintiffs "may seek additional information regarding Plaintiffs' previously alleged financial manipulations and information concerning the Defendants' knowledge regarding the same); *In re Grand Casinos Sec. Litig.*, 988 F. Supp. 1270 (D. Minn. 1997). Undue prejudice would visit Amalgamated and the Class in this case absent discovery given the nature of the equitable relief Amalgamated seeks and the public interest served by this proceeding, as set forth herein. *See supra* §II.C.3-4. The threat of irreparable injury is significant here, *a fortiori*, there is a showing of undue prejudice. *See supra* §II.C.2. Amalgamated's discovery is also sufficiently "particularized" or

limited, as set forth below, hence it will not result in a fishing expedition. *Anderson*, 157 F. Supp. 2d at 1242 ("Because Plaintiffs have articulated their alleged bases of liability, such discovery will not result in a fishing expedition.").

G. The Discovery Amalgamated Seeks

The scope of discovery Amalgamated will gather prior to the Order to Show Cause hearing and in order to submit a further application for equitable relief concerning ill-gotten profits from the "straw" limited partnerships is necessarily limited. Amalgamated seeks the following core documents from the Individual Defendants and defendant Arthur Andersen:

WITHIN 7 DAYS

(1) For each purchase, sale, pledge, encumbrance, or ownership of any Enron security during the Class Period (including stock options), documents which identify the brokerage house, bank, institution, other entity or individual through whom or which the stock was transacted;

(2) All documents identifying the location of proceeds of insider sales evidenced in (1) above or any assets derived from such proceeds (including institution, account number and account name, or, if the proceeds or assets are in the possession, custody or control of a person, the identification and location of any such person);

(3) Computer printouts summarizing the Individual Defendants' options holdings, options exercised, options vested and not vested, option grant dates, option vesting schedules, and option prices during the Class Period;

(4) Computer printout summaries or other documents (*e.g.*, account statements) concerning the Individual Defendants' transactions involving margin trading or derivative securities in Enron's stock (including, without limitation, zero-cost collars, cost-plus collars or equity swaps) during the Class Period;

(5) Concerning the limited partnerships Enron transacted with: formation documents, documents identifying all limited and general partners of the partnerships including ownership percentage, documents identifying all Enron personnel who received compensation or profit from those partnerships, documents summarizing all transactions between Enron and those partnerships or between those partnerships and any Enron employee, and documents reflecting any compensation or profit resulting from the association of any Enron employee with the limited partnerships;

(6) Notes, memoranda and work papers concerning the review of accounting practices being conducted by Enron's inside and outside auditors, or concerning the restatements of Enron's previously reported results from operations;

(7) All Enron Board of Director reports and minutes generated during the Class Period;

(8) All documents produced to the United States Securities and Exchange Commission, including document indexes; and

(9) The document and computer data destruction or retention policy defendants caused Enron to adopt and implement.

In addition to these limited categories of documents, plaintiff seeks an order providing for depositions of defendants and persons most knowledgeable concerning the topics governed by the documents sought above, limited to two hours, upon three calendar days' notice.

V. Conclusion

For all the reasons stated above, plaintiff's *ex parte* application should be granted.

DATED: December 5, 2001

Respectfully submitted,

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