No. _____

In The
Supreme Court of the United States

SAMUEL GIANCARLO, Individually and on Behalf of All Others Similarly Situated; CARLOS ALSINA, M.D.,

Petitioners,

v.

UBS FINANCIAL SERVICES, INCORPORATED; UBS SECURITIES, L.L.C.; UBS AG; UBS O'CONNOR, L.L.C.,

Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

APPENDIX

DAWN R. MEADE, *Counsel of Record*
DAVID AUGUSTUS
BONNIE E. SPENCER
THE SPENCER LAW FIRM
4635 Southwest Freeway, Suite 900
Houston, Texas 77027
Telephone: (713) 961-7770
dawnmeade@spencer-law.com
davidaugustus@spencer-law.com
bonniespencer@spencer-law.com
Attorneys for Petitioners

COCKLE LEGAL BRIEFS (800) 225-6964
WWW.COCKLELEGALBRIEFS.COM

APPENDIX TABLE OF CONTENTS

Page

United States Court of Appeals for the Fifth Circuit, Opinion, February 26, 2018 ..... App. 1

United States Court of Appeals for the Fifth Circuit, Judgment, February 26, 2018..... App. 24

United States District Court for the Southern District of Texas, Order, March 9, 2012..... App. 26

United States District Court for the Southern District of Texas, Opinion and Order of Dismissal, August 2, 2016 ..... App. 28

United States District Court for the Southern District of Texas, Opinion and Order Denying Motion to Reconsider, November 30, 2016 .... App. 152

United States Court of Appeals for the Fifth Circuit, Order Denying Petition for Rehearing, March 28, 2018..... App. 157

Relevant Statutes, Regulation and Rules..... App. 159

Docket, United States District Court for the Southern District of Texas, 4:03-cv-04359..... App. 192

Motion for Leave to File Second Amended Class Action Complaint ..... App. 239

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 16-20663

SAMUEL GIANCARLO, Individually and on behalf of all others similarly situated; CARLOS ALSINA, Medical Doctor,

Plaintiffs-Appellants

v.

UBS FINANCIAL SERVICES, INCORPORATED;UBS SECURITIES, L.L.C.; UBS AG; UBS O'CONNOR, L.L.C.,

Defendants-Appellees

Appeal from the United States District Court
for the Southern District of Texas,
USDC No. 4:03-CV-4359

(Filed Feb. 26, 2018)

Before: DENNIS, CLEMENT, and GRAVES, Circuit Judges.

PER CURIAM:*

This putative securities class action stems from the collapse of the energy-and-commodities giant, Enron Corporation. Plaintiffs, Enron investors, allege that Defendants, entities comprising the investment bank UBS, were complicit in structuring financial vehicles to enable Enron to mislead the public as to its fiscal performance. Plaintiffs claim that Defendants learned through their commercial relationships with Enron that Enron's prospects were poor. They further allege that Plaintiffs purchased Enron debt using one of the defendants as a broker because of Defendants' failure to disclose material information about Enron's instability.

The district court dismissed Plaintiffs' amended complaint for failure to state a claim. On appeal, Plaintiffs argue that their amended complaint sufficiently pled violations of federal securities law and, in the alternative, that it was error for the district court to dismiss their claims on the basis of the first amended complaint, filed in 2006, as the court should have granted Plaintiffs' 2011 motion for leave to file a proposed second amended complaint.

Plaintiffs have failed to establish that Defendants' knowledge and actions can be aggregated for purposes of assessing liability, which, due to the nature of their factual allegations and legal arguments, is fatal to

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* Pursuant to 5TH CIR. R. 47.5, the court has determined that this opinion should not be published and is not precedent except under the limited circumstances set forth in 5TH CIR. R. 47.5.4.

their claims. As for their motion for leave to amend, Plaintiffs have not shown that they were diligent, given their unexplained years-long delay, or that their proposed amendments were important. For these reasons, as explained more fully below, we AFFIRM the district court's judgment of dismissal.

I

Defendants UBS Financial Services, Inc. (formerly known as UBS PaineWebber, Inc., and referred to herein as PaineWebber), UBS Securities LLC (formerly known as UBS Warburg, LLC, and referred to herein as Warburg), and UBS AG are related but distinct corporate entities.[1] Together they constitute "UBS," one of the largest banks in the world. Defendants had several important professional connections with Enron, once the world's seventh-largest corporation by revenue. According to Plaintiffs' complaint, by 2000, Enron had begun "to seriously manipulate [its] financials" so as to make the company appear more robust than it was. As relevant here, Enron and the UBS entities engaged in a series of transactions Plaintiffs characterize as part of Enron's "financial chicanery." The complaint discusses multiple "off-balance[-]sheet" transactions between Defendants and Enron and alleges that each of these transactions was, in reality, a loan from the Defendants to Enron that was

[1] PaineWebber and Warburg are, or were at the relevant times, subsidiaries of UBS AG.

structured in a manner that permitted Enron to avoid logging the transaction as a liability.

In August 2001, Enron's Chief Executive Officer announced his retirement, which was followed by a precipitous drop in Enron's share price. Plaintiffs allege that Defendants immediately began to unwind their financial entanglements with Enron and to sell off their own Enron investments. By November 2001, Enron was making a series of financial disclosures and restatements, had placed its Chief Financial Officer (CFO) on a leave of absence, and had announced an internal investigation. Enron filed for bankruptcy in December 2001.

Plaintiffs are former PaineWebber clients who bought Enron bonds or other debt instruments using PaineWebber as their broker. Plaintiffs' basic theory of liability is that Defendants knew of Enron's financial manipulations and impending demise and owed Plaintiffs a duty to disclose such knowledge. In 2002, a multidistrict litigation (MDL) was established for the purpose of coordinating all cases "concerning allegedly negligent and/or fraudulent conduct relating to the financial collapse of Enron." The instant case was filed in 2003 and was transferred to the MDL to coordinate pretrial proceedings in early 2004. After the conclusion of fact discovery in 2006, Plaintiffs elected to proceed independently from the class certified in "*Newby,*" a case involving claims by purchasers of Enron stock against banks that allegedly facilitated Enron's misrepresentation of its financial condition. *See Regents of*

the Univ. of Cal. v. Credit Suisse First Bos., 482 F.3d 372, 377 (5th Cir. 2007).

Plaintiffs filed their first amended complaint in August 2006. Plaintiffs alleged, in pertinent part, that Defendants violated § 10(b) of the Securities Exchange Act, 15 U.S.C. § 78j(b), and Securities and Exchange Commission Rule 10b-5, 17 C.F.R. § 240.10b-5, by failing to disclose information tending to show that Enron's financial state was precarious. Defendants filed a motion to dismiss in September 2006, arguing, inter alia, that although Warburg and PaineWebber were distinct legal entities, "[P]laintiffs [made] essentially no attempt to plead, with the requisite specificity, who at what defendant had what knowledge or wrongful intent." Plaintiffs filed a response, incorporating a boilerplate motion for leave to amend in the event the trial court found the complaint deficient. Briefing was completed in January 2007.

In March 2007, this court decertified the class in *Newby*. *See Regents*, 482 F.3d at 394. The following day, the district court stayed proceedings in *Newby* and most other coordinated and consolidated cases in the Enron MDL. In April 2007, Plaintiffs requested a determination that the stay order did not apply to their case. In June 2007, the trial court confirmed that the stay order *did* apply to Plaintiffs' case and that it was in effect pending potential certiorari in *Newby* and the Supreme Court's then-pending decision in *Stoneridge Investment Partners, L.L.C. v. Scientific Atlanta, Inc.*, 552 U.S. 148 (2008), which addressed aiding and abetting liability under § 10(b).

In January 2008, the Supreme Court decided *Stoneridge* and, separately, denied certiorari in *Newby*. *See Regents of the Univ. of Cal. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 552 U.S. 1170 (2008); *Stoneridge*, 552 U.S. 148.[2] Two years later, Plaintiffs forwarded a copy of their proposed second amended complaint to Defendants. In July 2010, Plaintiffs filed a motion to lift the stay in their case. Over a year later, the court lifted the stay, and one week after that, Plaintiffs filed a motion for leave to file their second amended complaint. In March 2012, the district court denied leave to amend "in light of the long history of deadlines and extensions in the *Newby* action."

Over four years later, in August 2016, the district court granted Defendants' motion to dismiss. The court found that Plaintiffs failed to plead facts demonstrating that Defendants' separate corporate status should be disregarded, and thus Plaintiffs had failed to adequately plead their "single, fully integrated entity theory" of liability. The court held that Plaintiffs' allegations were insufficient to support a duty to disclose on the part of UBS AG or Warburg, finding that the amended complaint contained no factual allegations showing a direct relationship between Plaintiffs and Warburg or UBS AG that would give rise to a duty of disclosure. The court further held that, although PaineWebber owed some duties to Plaintiffs as retail brokerage clients, PaineWebber had not breached its

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[2] The district court granted summary judgment in *Newby* in early March 2009. *See Newby v. Enron Corp. (In re Enron Corp. Secs.)*, 610 F. Supp. 2d 600 (S.D. Tex. 2009).

limited duties. The court also held that Plaintiffs failed to sufficiently allege PaineWebber's scienter inasmuch as they failed "to identify specific brokers and allege facts that demonstrate each had an intent to deceive, manipulate or defraud or acted with severe recklessness." Finally, the court held that Plaintiffs failed to establish that PaineWebber's alleged brokerage practices caused their losses, reasoning that PaineWebber's actions in no way related to Enron's fraud, which was the actual cause of Plaintiffs' economic damages.[3]

Plaintiffs filed a motion for reconsideration, arguing that the court erred in denying leave to amend their complaint and in finding that Plaintiffs failed to adequately plead their § 10(b) claims. The district court denied reconsideration. Plaintiffs filed a notice of appeal designating specifically, and only, the district court's order granting Defendants' motion to dismiss.

II

We review the sufficiency of a complaint de novo. *Ind. Elec. Workers' Pension Tr. Fund Ibew v. Shaw Grp., Inc.*, 537 F.3d 527, 533 (5th Cir. 2008). "The plaintiff's well-pleaded facts are to be accepted as true and viewed in the light most favorable to her." *Daugherty v. Convergent Outsourcing, Inc.*, 836 F.3d 507, 510 (5th

[3] The court also dismissed Plaintiffs' claims under 15 U.S.C. § 78t-1(a), a provision concerned with insider trading. Plaintiffs do not make any arguments related to this holding on appeal and therefore have abandoned any such arguments. *See, e.g., United States v. Charles*, 469 F.3d 402, 408 (5th Cir. 2006) ("Inadequately briefed issues are deemed abandoned.").

Cir. 2016). "[C]onclusory allegations, unwarranted deductions[, and] legal conclusions" are not "well-pleaded facts" for purposes of evaluating a complaint. *See Southland Sec. Corp. v. INSpire Ins. Sols. Inc.*, 365 F.3d 353, 361 (5th Cir. 2004). When deciding a motion to dismiss a claim for securities fraud, a court may consider the contents of certain public documents filed with the Securities and Exchange Commission (SEC), *Lovelace v. Software Spectrum, Inc.*, 78 F.3d 1015, 1017 (5th Cir. 1996), and "documents that a defendant attaches to a motion to dismiss . . . if they are referred to in the plaintiff's complaint and are central to her claim," *Collins v. Morgan Stanley Dean Witter*, 224 F.3d 496, 498-99 (5th Cir. 2000) (quoting *Venture Assocs. Corp. v. Zenith Data Sys. Corp.*, 987 F.2d 429, 431 (7th Cir. 1993)).

Where fraud is alleged, Federal Rule of Civil Procedure 9(b) "creates a heightened pleading requirement that 'the circumstances constituting fraud or mistake shall be stated with particularity.'" *United States ex rel. Rafizadeh v. Cont'l Common, Inc.*, 553 F.3d 869, 872 (5th Cir. 2008) (quoting FED. R. CIV. P. 9(b)). "[A]lthough the requirement for particularity in pleading fraud does not lend itself to refinement, . . . directly put, the who, what, when, and where must be laid out." *Southland*, 365 F.3d at 363 (quoting *ABC Arbitrage Plaintiffs Grp. v. Tchuruk*, 291 F.3d 336, 349 (5th Cir. 2002)). A class-action complaint alleging a violation of § 10(b) must allege fraud in accordance with the heightened pleading standard of Rule 9(b). *See id.*

III

To state a securities-fraud claim under § 10(b) and Rule 10b-5, Plaintiffs must allege that Defendants engaged in deceptive conduct in connection with the purchase or sale of securities, that such conduct was committed with scienter, that Plaintiffs acted in reliance on Defendants' conduct, and that the conduct caused Plaintiffs' losses. *See, e.g., Dura Pharm., Inc. v. Brando*, 544 U.S. 336, 341-42 (2005). Plaintiffs' allegations regarding deceptive conduct, scienter, and reliance are interlinked inasmuch as Plaintiffs rest their case on the presumption announced in *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128 (1972). In *Affiliated Ute*, the Supreme Court held that, in the case of an alleged material nondisclosure, reliance can be presumed from the materiality of the omission. *Id.* at 153-154. To invoke the "*Affiliated Ute* presumption," Plaintiffs must allege a claim based on material omissions or non-disclosure and must show that Defendants owed them a duty of disclosure. *See Regents*, 482 F.3d at 384. In order to evaluate these issues, we must first address Plaintiffs' contention that Defendants formed a joint venture, which, they claim, permits us to aggregate Defendants' knowledge and actions for purposes of assessing liability.

A

Plaintiffs' amended complaint generally refers to Defendants as if they were a single entity. On appeal, Plaintiffs argue that we can attribute each defendant's

actions and knowledge to a single entity called "UBS" because Defendants formed a "de facto joint venture." Plaintiffs claim that their allegations are supported by Defendants' SEC filings, which included statements referring to Defendants as an "integrated investment services firm," referring to "UBS's business groups," and calling UBS "an integrated group."

Plaintiffs argue that, under Delaware law, the "generally recognized" factors relevant to determining whether a joint venture exists are: "(1) a community of interest in the performance of a common purpose, (2) joint control or right of control, (3) a joint proprietary interest in the subject matter, (4) a right to share in the profits, (5) a duty to share in the losses which may be sustained." *Warren v. Goldinger Bros., Inc.*, 414 A.2d 507, 509 (Del. 1980) (quoting *Kilgore Seed Co. v. Lewin*, 141 So. 2d 809, 810-11 (Fla. App. 1962)).[4] Plaintiffs fail to explain how the allegations identified in their brief on appeal support finding a joint venture under this test. None of the allegations allude to profit sharing, or loss sharing, *see N.S.N. Int'l Indus., N.V. v. E.I. DuPont de Nemours & Co., C.A.*, No. 12902, 1994 Del. Ch. LEXIS 46, at *20-21 (Del. Ch. Mar. 31, 1994) (no joint venture where agreement between parties did not contemplate loss sharing), and none establish that the Defendants have a joint right to control the purported

[4] Plaintiffs' brief suggests in a footnote that federal common law or Texas law is relevant to our analysis of whether a joint venture exists, but otherwise exclusively relies on Delaware law. Plaintiffs also contended at oral argument that Delaware law governs, so we will assume this is the case.

joint venture,[5] *see In re Del. Bay Surgical Servs.*, No. 2121-S, 2002 Del. Ch. LEXIS 158, at *8 (Del. Ch. Jan. 28, 2002) (no joint venture where parties did not have joint right of control). Plaintiffs' allegations – principally references to Defendants' vague corporate platitudes about their integration as a firm – may logically support that Defendants shared a community of interest in their business activities, but this alone is insufficient to support joint venture liability. *See, e.g., Warren*, 414 A.2d at 509 (five factors "must be" present); *In re Coffee Assocs.*, No. 12950, 1993 Del. Ch. LEXIS 263, at *15 (Del. Ch. Dec. 3, 1993) ("A community of economic interest. . . . is not sufficient to create a joint venture."). Thus, Plaintiffs have not established the existence of a joint venture, and they have not put forth any other theory that permits us to aggregate the actions and knowledge of the defendant entities for purposes of assessing liability.

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[5] We note that, at oral argument, Plaintiffs alluded to additional supportive allegations in Defendants' public SEC filings and Plaintiffs' proposed second amended complaint. Our present analysis is limited to the first amended complaint. Moreover, we ordinarily do not consider points raised for the first time at oral argument. *See Vargas v. Lee*, 317 F.3d 498, 503 n.6 (5th Cir. 2003). Federal Rule of Appellate Procedure 28(a)(8) requires appellants to brief their arguments and to support their contentions with citations to the record. Although Plaintiffs are correct that we can consider certain documents filed with the SEC, it is Plaintiffs' burden to point us to relevant portions of the relevant filings in their briefing.

B

Plaintiffs contend that Defendants were in possession of material, non-public information and that Defendants owed Plaintiffs a duty to disclose this information. Specifically, Plaintiffs allege that Defendants ought to have disclosed "UBS's knowledge that Enron's public financial statements were manipulated and materially misleading."[6] However, Plaintiffs have not sued any entity called "UBS," or, as previously discussed, established that any such legal entity exists. It is, therefore, not sufficiently particular to allege that "UBS" knew material non-public information due to "UBS's" interactions with Enron. *See Southland*, 365 F.3d at 363 (heightened pleading requires plaintiff to, at minimum, allege "who" engaged in deceptive conduct). *Cf. Fin. Acquisition Partners LP v. Blackwell*, 440 F.3d 278, 289 (5th Cir. 2006) (allegations not sufficiently particular where they failed to demonstrate which specific defendants of a group of defendants had the duty to disclose information). Moreover, even a searching review of the relevant documents supports, at most, that Warburg and UBS AG had some insider knowledge of Enron's financial situation, as those are the defendants that participated in the transactions

[6] For reasons made clear below, we have no occasion to decide whether Plaintiffs' allegations plausibly support that Defendants knowingly or recklessly participated in Enron's fraud. We assume, arguendo, that the transactions Plaintiffs detail in their amended complaint were sufficient to impart material, non-public knowledge to the participating defendants.

identified by Plaintiffs.[7] Thus, Plaintiffs must show that Warburg or UBS AG owed them a duty of disclosure.

Plaintiffs point to several supposed sources of Defendants' duty of disclosure. Plaintiffs first argue that, under applicable self-regulatory organization rules, "UBS had an affirmative duty to disclose its knowledge concerning Enron's financial manipulations to its retail clients who were placing orders with UBS to purchase Enron securities." However, Plaintiffs do not divulge in their brief what rules they are referring to, or how such rules imposed a duty of disclosure on any of the Defendants. Plaintiffs' amended complaint appears to only discuss the role of self-regulatory organization rules in one paragraph, and the only rule specifically discussed is a National Association of Securities Dealers (NASD) rule requiring that

> [a]ll member communications with the public shall be based on principles of fair dealing and good faith and should provide a sound basis for evaluating the facts in regard to any particular security or securities or type of

[7] To the extent Plaintiffs sufficiently allege that any individual employee or officer at one of the defendant corporations possessed material, non-public information regarding Enron's finances, we might be able to impute that knowledge to a particular defendant. But Plaintiffs fail to indicate which individuals work for which defendant. We will not strain to come up with a theory of each defendant's knowledge when Plaintiffs have offered none in their briefing. *Cf. United States v. Caldwell*, 302 F.3d 399, 421 n.19 (5th Cir. 2002) ("Because Caldwell fails to provide any supporting analysis for this claim, we consider it abandoned as inadequately briefed.").

> security, industry discussed, or service offered. No material fact or qualification may be omitted if the omission, in the light of the context of the material presented, would cause the communications to be misleading.

This rule does not appear to impose a duty of disclosure in the absence of a "communication[]." The only defendant alleged to have "communicated" with Plaintiffs is PaineWebber, and Plaintiffs have not sufficiently alleged that any person at PaineWebber had knowledge concerning Enron's financial manipulations. Thus, even if we accepted Plaintiffs' invitation to hold that NASD rules can impose a duty of disclosure for purposes of § 10(b) liability,[8] Plaintiffs have not shown that any defendant violated such rules.[9]

Next, Plaintiffs rely on *Affiliated Ute* for the proposition that Defendants' "special relationship" with Plaintiffs gave rise to a fiduciary-like duty of disclosure. Plaintiffs first allege that "UBS gained significant amounts of material, non-public information concerning Enron, its finances, and its practices via . . . numerous interactions and overlapping relationships" with Enron. This purported "special relationship" is, in fact, just an argument that insider knowledge itself gives rise to a duty of disclosure, an argument that the

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[8] We have previously declined "to address the existence of a private cause of action under the [New York Stock Exchange] and NASD rules." *Jolley v. Welch*, 904 F.2d 988, 993 (5th Cir. 1990).

[9] Additionally, Plaintiffs repeatedly contend that their claims are not based on any statements, so it is unclear how an NASD rule governing communications supports their theory of liability.

Supreme Court has rejected. *See Chiarella v. United States*, 445 U.S. 222, 230 (1980) ("[A] duty to disclose under § 10(b) does not arise from the mere possession of nonpublic market information."). And, to the extent Plaintiffs rely on allegations as to Defendants' active participation in Enron's misleading financial transactions, this court has already held that such behavior is not sufficient to establish a duty of disclosure. *See Regents*, 482 F.3d at 384-85.

Next, Plaintiffs allege that a duty to disclose arose from the fact that "UBS was entirely familiar with the prevailing market for Enron shares at all material times"; "UBS was a market maker[10] for Enron and its related businesses," based on participation in financial transactions with Enron; "UBS itself traded Enron securities in the world's securities markets via UBS accounts"; and "UBS took advantage of its access to and significant knowledge of Enron's secret financial reality, eliminated its own risk by selling its Enron holdings in the months prior to Enron's bankruptcy, and even created UBS securities tied to Enron's default as part of that process."

The only authority Plaintiffs cite in support of this "special relationship" is *Affiliated Ute.* In *Affiliated Ute*, plaintiffs, owners of restricted stock, alleged that two bank officers bought their stock without disclosing

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[10] "A market maker is a broker-dealer firm that assumes the risk of holding a certain number of shares of a particular security in order to facilitate the trading of that security." *Market maker*, INVESTOPEDIA, http://www.investopedia.com/terms/m/marketmaker.asp.

that they had created a secondary market in which the stock would be resold at a significant profit. *See* 406 U.S. at 133-39, 144-47. The bank, which was the exclusive transfer agent for the stock, had agreed to act on behalf of the individual stockholders. *Id.* at 145, 152. The Court held that the bank officers had committed securities fraud because they had "devised a plan and induced the [sellers] to dispose of their shares without disclosing to them material facts that reasonably could have been expected to influence their decisions to sell," namely that "the defendants were in a position to gain financially from their sales and that their shares were selling for a higher price in th[e] market" that the defendants had created. *Id.*

Plaintiffs' relationship to Defendants is not analogous to that of the parties in *Affiliated Ute.* In contrast to *Affiliated Ute*, there were "other market makers and underwriters" trading in Enron securities and Plaintiffs were not required to deal with any of the Defendants. More importantly, Plaintiffs have not successfully alleged that the defendants who engaged in market-making activities (UBS AG or Warburg) sold them securities. Documents attached to the pleadings discuss the role of "UBS Warburg AG" in several transactions and indicate that that [sic] "UBS Warburg" was the "joint lead manager of Credit Linked Notes for Enron." Plaintiffs specify that their brokers were employees of PaineWebber. Plaintiffs do not argue that PaineWebber had any special knowledge of the market for Enron debt securities, and UBS AG's and Warburg's dealings

with Enron cannot support that PaineWebber had a duty of disclosure.

Finally, Plaintiffs argue that their retail relationship with Defendants gave rise to a duty of disclosure. But, again, even assuming that Plaintiffs' retail relationship with PaineWebber gave rise to a duty of disclosure, Plaintiffs have not demonstrated that PaineWebber had any material, non-public knowledge to disclose. Thus, Plaintiffs have failed to establish that any one defendant had material non-public knowledge and a duty to disclose this knowledge to Plaintiffs. Accordingly, the district court properly dismissed Plaintiffs' amended complaint for failure to state a claim.

IV

Plaintiffs argue that, even if their first amended complaint was properly dismissed for failure to state a claim, the district court ought not to have dismissed the action without granting them leave to file a second amended complaint. Plaintiffs sought leave to amend their complaint long after the time to amend had expired and Defendants' motion to dismiss was fully briefed. The district court denied leave to amend "in light of the long history of deadlines and extensions in the *Newby* action."

As a preliminary matter, Defendants argue that Plaintiffs have not properly appealed the denial of leave to amend because their notice of appeal only, and specifically, designated the district court's order granting the motion to dismiss. However, Defendant's [sic]

construction of Federal Rule of Appellate Procedure 3 – which governs the required content of a notice of appeal – is formalistic in a manner that we have already rejected.

In *New York Life Insurance Co. v. Deshotel*, 142 F.3d 873, 884 (5th Cir. 1998), an appellee argued that, because the notice of appeal only designated the order dismissing the action, we lacked jurisdiction over the appellant's challenge to an earlier district court order denying her motion to remand. We rejected the appellee's argument because (1) the order designated in the notice of appeal was the final judgment, and therefore the notice preserved all prior orders intertwined with that judgment; (2) the issues in the final order were "inextricably intertwined" with the prior order inasmuch as the final judgment was predicated on the district court's exercise of removal jurisdiction; and (3) any doubts as to the appellant's intent to preserve her arguments on appeal were resolved by the opening brief, which addressed such arguments. *Id.* We therefore concluded that "the notice of appeal coupled with the opening briefs gave [the appellee] adequate notice" of the matters at issue in the appeal and that the appellee "fail[ed] to demonstrate that it was prejudiced by any deficiency in the notice of appeal." 816 F.3d at 328.

Defendants argue that the order designated here was not a "final judgment" because the notice of appeal designates only the August 2, 2016 dismissal order and not the docket entry administratively terminating the case. But that docket entry reflects that the case was

"[t]erminated per" the "opinion and order of dismissal" specifically designated by the Plaintiffs. Intent to appeal the conclusive order can be inferred from Plaintiffs' notice of appeal and the opening brief, *see Deshotel*, 142 F.3d at 884, and review of that order "clearly encompasses the prior orders leading up to it," *see Xerox Corp. v. Genmoora Corp.*, 888 F.2d 345, 349 (5th Cir. 1989). Defendants have fully addressed the motion for leave to amend on the merits and fail to argue that they were prejudiced by Plaintiffs' inartful notice of appeal. Consequently, we are satisfied that we have jurisdiction over this issue, the merits of which we now turn to address.

"While Federal Rule of Civil Procedure 15(a) provides that leave to amend shall be 'freely' given, [Federal] Rule [of Civil Procedure] 16(b)(4) limits modifications to a scheduling order to situations where good cause is shown." *United States ex rel. Bias v. Tangipahoa Par. Sch. Bd.*, 816 F.3d 315, 328 (5th Cir. 2016). Four factors are relevant to whether good cause has been shown for purposes of Rule 16(b)(4): "(1) the explanation for the failure to timely move for leave to amend; (2) the importance of the amendment; (3) potential prejudice in allowing the amendment; and (4) the availability of a continuance to cure such prejudice." *Id.* (cleaned up). The district court has broad discretion in considering whether to grant an untimely motion for leave to amend. *See Fahim v. Marriott Hotel Servs.*, 551 F.3d 344, 348 (5th Cir. 2008).

Plaintiffs argue that the district court abused its discretion by denying leave to amend. They claim that

they failed to timely amend their complaint (1) because they needed to add information from the deposition of Enron CFO Andrew Fastow; (2) because of their "desire to include allegations based upon UBS's expert witness testimony"; and (3) because Defendants' disavowal of the UBS joint venture was unforeseeable. Plaintiffs argue that their amendments are "[c]learly" important, in light of the district court's dismissal. Plaintiffs contend that there is no evidence that the amendment would result in prejudice to Defendants. Plaintiffs further argue that they themselves caused no delay, so the district court's explanation for denying leave – delay in the *Newby* case – was unjustified.

Plaintiffs' explanations for their failure to timely amend their complaint do not explain their long delay in seeking leave to amend, nor establish their diligence. *See Fahim*, 551 F.3d at 348 (under Rule 16(b), a party must show that "the deadlines cannot reasonably be met despite the diligence of the party needing the extension"). First, Fastow was deposed in October 2006. This case was not stayed until March 2007, and Plaintiffs did not concede that their action was stayed until June 2007. Plaintiffs had at least four months before their action was stayed to request leave to amend to incorporate the Fastow deposition. Nonetheless, Plaintiffs did not send Defendants a copy of their proposed amended complaint until January 2010. By that time, they had known of Fastow's deposition for over four years, and the basis for the stay had been fully resolved for at least nine months. *See Newby*, 610

F. Supp. 2d at 655. Consequently, Fastow's October 2006 deposition does not explain Plaintiffs' delay.

Second, as to the "UBS expert testimony" Plaintiffs added to their proposed second amended complaint, three of the cited depositions were taken months before Plaintiffs' first amended complaint was filed. The one that was not occurred in November 2006. Plainly, then, these depositions do not explain Plaintiffs' delay.

Third, Plaintiffs suggest that they were caught off-guard by Defendants' disavowal of the "UBS joint venture." But Plaintiffs should have known of Defendants' position by September 2006, at which time Defendants filed their motion to dismiss highlighting that Warburg and PaineWebber were separate legal entities and arguing that Plaintiffs had not shown scienter because Plaintiffs made "essentially no attempt to plead, with the requisite specificity, who at what defendant had what knowledge or wrongful intent." Plaintiffs failed to take any concrete steps to amend their complaint with this information until 2010. Therefore, Plaintiffs have failed to demonstrate that they were diligent in seeking leave to amend.

In any event, Plaintiffs have failed to demonstrate the need for the amendments. In a single line, Plaintiffs contend that their amendments were important in light of "the dismissal and the extent to which it is the correct legal decision." But Plaintiffs do not explain what additional allegations would cure which deficiencies, and the correlation is not self-evident. Elsewhere

in their briefing, Plaintiffs imply that Fastow testified that he told Defendants that Enron was in poor financial shape and hid it through intentionally misleading manipulation. Even if this were the case, Plaintiffs do not argue that Fastow had any dealings with PaineWebber specifically and therefore have not shown how these additional allegations would resolve the earlier-discussed inability to attribute insider knowledge to PaineWebber. Plaintiffs also contend, generally, that their additional allegations would "bolster the joint venture allegation," but fail to explain how they would do so. Similarly, they argue that allegations based on "UBS's expert witness testimony [would] support[ ] the[ir] §10(b) claim," without any explanation as to what the additional testimony consists of, or how it supports their claims. Thus, the few specific arguments Plaintiffs do raise fail to show that the proposed amendments were important, and Plaintiffs have otherwise failed to sufficiently brief this issue. *See* FED. R. APP. P. 28(a)(8) (briefing "must contain . . . appellant's contentions and the reasons for them, with citations to" supporting authority). Inadequately briefed arguments are generally deemed to have been forfeited, *see, e.g., SEC v. Life Partners Holdings, Inc.*, 854 F.3d 765, 784 (5th Cir. 2017), and we see no reason to deviate from the usual rule here.

Plaintiffs have failed to demonstrate that they were diligent in pursuing their amendments or that these amendments were important. Accordingly, even assuming that the other two factors favor the Plaintiffs, the district court did not abuse its discretion by

denying leave to amend. *See Fahim*, 551 F.3d at 348 (no abuse of discretion in denial of leave to amend where two factors "weighed heavily against" amendment and two factors weighed in favor).

* * *

For these reasons, we AFFIRM the district court's denial of leave to amend as well as its dismissal of Plaintiffs' first amended complaint.

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 16-20663

D.C. Docket No. 4:03-CV-4359

SAMUEL GIANCARLO, Individually and on behalf of all others similarly situated; CARLOS ALSINA, Medical Doctor,

Plaintiffs-Appellants

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UBS FINANCIAL SERVICES, INCORPORATED; UBS SECURITIES, L.L.C.; UBS AG; UBS O'CONNOR, L.L.C.,

Defendants-Appellees

Appeal from the United States District Court
for the Southern District of Texas

Before DENNIS, CLEMENT, and GRAVES, Circuit Judges.

JUDGMENT

(Filed Feb. 26, 2018)

This cause was considered on the record on appeal and was argued by counsel.

It is ordered and adjudged that the judgment of the District Court is affirmed.

IT IS FURTHER ORDERED that plaintiffs-appellants pay to defendants-appellees the costs on appeal to be taxed by the Clerk of this Court.

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

In Re ENRON CORPORATION SECURITIES, DERIVATIVE & "ERISA" LITIGATION,	§ § §	MDL 1446
MARK NEWBY, ET AL., Plaintiffs VS. ENRON CORPORATION, ET AL., Defendants	§ § § § § § §	CIVIL ACTION NO. H-01-3624 AND CONSOLIDATED CASES
KEVIN LAMPKIN, et al., Individually and On Behalf of All Others Similarly Situated, Plaintiffs, VS. UBS FINANCIAL SERVICES, INC. and UBS SECURITIES, LLC, Defendants	§ § § § § § § § § § § §	CIVIL ACTION NO. 02-0851

SAMUEL GIANCARLO, Individually and on Behalf of All Others Similarly Situated,	§	
Plaintiffs,	§	CIVIL ACTION NO. H-03-4359 COORDINATED CASE
VS.	§	
UBS FINANCIAL SERVICES, INC., UBS SECURITIES, L.L.C., UBS AG and UBS O'CONNOR, L.L.C.,	§	
Defendants.	§	

ORDER

(Filed Mar. 9, 2012)

Pending before the Court in the above referenced causes are (1) a motion for leave to file fourth amended class action complaint in H-02-0851 (instrument #198) and a motion for leave to file second amended class action complaint in H-03-4359. In light of the long history of deadlines and extensions in the *Newby* action, the Court

ORDERS that the untimely motions are DENIED.

SIGNED at Houston, Texas, this 9th day of March, 2012.

/s/ Melinda Harmon
MELINDA HARMON
UNITED STATES
DISTRICT JUDGE

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

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SAMUEL GIANCARLO, Individually and on Behalf of All Others Similarly Situated, Plaintiffs, VS. UBS FINANCIAL SERVICES, INC., UBS SECURITIES, L.L.C., and and [sic] UBS AG, Defendants.	§ § § § § § § § § §	CIVIL ACTION NO. H-03-4359 COORDINATED CASE

OPINION AND ORDER OF DISMISSAL

(Filed Aug. 2, 2016)

Pending before the Court in the above referenced putative class action,[1] alleging violations of Section 20A of the Securities Exchange Act of 1934 (a/k/a "the

[1] The First Amended Class Action Complaint (#81 at ¶¶ 11-12) identifies Samuel Giancarlo ("Giancarlo") and Carlos Alsina, M.D. ("Alsina"), as class representatives seeking to represent three putative classes: "(1) all persons and/or entities who purchased and/or acquired Enron Corp. ("Enron") notes, debt or other debt instruments through [UBS Financial Services Inc. f/k/a PaineWebber] during the Class Period [November 5, 2000 – December 2, 2001]; (2) all persons and/or entities who purchased and/or acquired Enron Zero Coupon Convertible Senior Notes due 2021 (Registration No. 333-62168) through [PaineWebber] during the Class Period; and (3) all persons and/or entities who purchased and/or acquired UBS owned Enron Debt during the Class Period." Each of the two named Plaintiffs acquired these securities "in reliance on the information provided to him, and UBS PaineWebber, Inc.'s non-disclosure of information, and without knowledge of the facts underlying the federal securities fraud claims asserted herein." Additionally, both acquired [their] securities "without any knowledge of the false statements contained in the referenced registration statements and/or prospectuses." *Id.* at ¶¶ 5 and 6.

1934 Act"),[2] as amended, 15 U.S.C. §§ 78j(b)[3] and 78(t),[4] *et seq.*,[5] and the Private Securities Litigation Reform

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[2] To state a claim under § 10(b) of the 1934 Act and Rule 10b-5, 17 C.F.R. § 240.10b-5, the plaintiff must plead in connection with the purchase or sale of securities, "'(1) a misstatement or omission (2) of material fact (3) made with scienter (4) on which plaintiff relied (5) that proximately caused [the plaintiff's] injury.'" *Nathenson v. Zonagen, Inc.*, 267 F.3d 400, 406 (5th Cir. 2001), *quoting Tuchman v. DSC Communications Corp.*, 14 F.3d 1061, 1067 (5th Cir. 1994). An omission is material for purposes of federal securities law if there is a "substantial likelihood that the disclosure of omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information available." *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976); *Basic, Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988) ("adopt[ing] *TSC Industries* standard of materiality for the § 10(b) and Rule 10b-5 context").

[3] Section 78j(b), addressing manipulative and deceptive devices, provides, "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange – [t]o use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

For purposes of § 10(b), during the legislative history of the Securities Exchange Act it appears that Congress sought to reach two forms of wrongdoing, manipulative and deceptive conduct, neither of which is defined in the statute. James C. Dugan and Todd G. Cosenza, *The Future of Secondary Actor Liability Under Rule 10b-5 After Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc., 5 NYU J. of Law & Bus.* 793, 796 (Summer 2009). "'[M]anipulative . . . refers generally to practices such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity.'" *Id.*, *quoting Santa Fe Indust., Inc. v. Green*, 430 U.S. 462, 476 (1977).

See also H.R. Rep. No. 1383, 73-1383, at 15 (1934) (manipulative trading schemes such as wash sales or matched orders that were "designed to create a misleading appearance of activity with a view to enticing the unwary into the market"). "Deceptive" conduct involves " '[f]alse and misleading statements designed to induce investors to buy when they should sell and to sell when they should buy.' " *Id.*, *citing* H.R. Rep. No. 73-1383, at 10 (1934).

[4] Under Section 20A, 15 U.S.C. § 78t-1(a), insider trading can constitute a derivative violation of the 1934 Act:

> Any person who violates any provision of this chapter or the rules and regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.

For greater detail see ¶¶ 228-31. To plead a § 20A cause of action, the plaintiff must (1) allege a requisite independent, predicate violation of the Exchange Act or its rules and regulations, e.g., § 10(b), and (2) show that he has standing to sue under § 20A because he "contemporaneously with the purchase of sale of securities that is the subject of such violation has purchased . . . or sold . . . securities of the same class" as the insider defendant. 15 U.S.C. § 78t-1(a). Arising "from a recognition that '[s]ince identifying the party in actual privity with the insider is virtually impossible in trades occurring on an anonymous public market, the contemporaneous standard was developed as a more feasible avenue by which to sue insiders.' " *In re MicroStrategy, Inc.*, 115 F. Supp. 2d 620, 662 (E.D. Va. 2000) ("Thus, by requiring a showing of contemporaneity in the trades by the insider and the suing investor, Section 20A seeks to ensure that, where contractual privity would otherwise be impractical if not impossible to show, there nonetheless was a sufficiently close temporal relationship between the trades that the investor's interests were implicated by trades made by the insider while in possession of material, nonpublic information.").

Act ("PSLRA"), 15 U.S.C. §§ 78(u)(4) and 78(a), *et seq.*, is Defendants UBS Financial Services, Inc.,[6] UBS Securities LLC ("Warburg"),[7] and UBS AG's[8] (collectively, "the UBS Defendants'" or "UBS's") motion to dismiss (instrument #84) the First Amended Class Action Complaint (#81). Also pending are Lead Plaintiffs' motion for class certification (#124) and Plaintiffs' opposed joint motion for amended scheduling order, for additional briefing, and for a ruling (instrument #173).

Plaintiffs Giancarlo and Alsina, two Paine Webber (sometimes referred to as "PW") retail-brokerage

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Plaintiffs' Complaint, ¶ 25, alleges,

> Additionally, Plaintiffs bring claims against UBS pursuant to § 20A of the Securities Act of 1934 as a result of UBS's sale of Enron debt securities, contemporaneous with Plaintiffs' purchase of such securities, while UBS was in possession of material, non-public information regarding Enron.

[5] Specifically §§ 10(b), 10(b)(5), 20, and 20A.

[6] f/k/a UBS Paine Webber, Inc. ("PW"). #81, p. 2, ¶7. PW is a Delaware corporation authorized to do business in Texas and is a subsidiary of Swiss banking conglomerate UBS AG. *Id.*

[7] f/k/a UBS Warburg, LLC ("Warburg"). #81, p.2. ¶8. Warburg is a Delaware limited liability company authorized to do business in Texas and a subsidiary of Swiss banking conglomerate UBS AG. *Id.*

[8] UBS AG is a foreign corporation registered in Connecticut and authorized to do business in Texas. #81, p. 2, ¶ 9.

UBS, one of the largest banks in the world, "is an integrated bank offering traditional commercial loans, investment banking opportunities and retail brokerage services." #81 at ¶ 26.

Warburg and PW are wholly owned subsidiaries of UBS AG. Warburg and PW are separate legal entities with no ownership interests in each other.

customers, in this suit against the UBS Defendants, have elected to proceed independently of the consolidated amended complaints in the *Newby* and *Tittle* actions. #79.

I. Standards of Review

A. Rule 12(b)(6)

When a district court reviews a motion to dismiss pursuant to Fed. R. Civ. P. 12(b)(6), it must construe the complaint in favor of the plaintiff and take all well-pleaded facts as true. *Randall D. Wolcott, MD, PA v. Sebelius*, 635 F.3d 757, 763 (5th Cir. 2011), *citing Gonzalez v. Kay*, 577 F.3d 600, 603 (5th Cir. 2009). The plaintiff's legal conclusions are not entitled to the same assumption. *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) ("The tenet that a court must accept as true all of the allegations contained in a complaint is inapplicable to legal conclusions."), *citing Bell Atlantic Corp. v. Twombly*, 556 U.S. 662, 678 (2007); *Hinojosa v. U.S. Bureau of Prisons*, 506 Fed. Appx. 280, 283 (5th Cir. Jan. 7, 2012).

"While a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, . . . a plaintiff's obligation to provide the 'grounds' of his 'entitle[ment] to relief' requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do. . . ." *Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955, 1964-65 (2007) (citations omitted). "Factual allegations must be enough to raise a right to relief above the speculative

level." *Id.* at 1965, *citing* 5 C. Wright & A. Miller, *Federal Practice and Procedure* § 1216, pp. 235-236 (3d ed. 2004) ("[T]he pleading must contain something more . . . than . . . a statement of facts that merely creates a suspicion [of] a legally cognizable right of action"). "*Twombly* jettisoned the minimum notice pleading requirement of *Conley v. Gibson*, 355 U.S. 41 . . . (1957) ["a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief"], and instead required that a complaint allege enough facts to state a claim that is plausible on its face." *St. Germain v. Howard*, 556 F.3d 261, 263 n.2 (5th Cir. 2009), *citing In re Katrina Canal Breaches Litig.*, 495 F.3d 191, 205 (5th Cir. 2007) ("To survive a Rule 12(b)(6) motion to dismiss, the plaintiff must plead 'enough facts to state a claim to relief that is plausible on its face.'"), *citing Twombly*, 127 S. Ct. at 1974). "'A claim has facial plausibility when the pleaded factual content allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.'" *Montoya v. FedEx Ground Package System, Inc.*, 614 F.3d 145, 148 (5th Cir. 2010), *quoting Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). The plausibility standard is not akin to a "probability requirement," but asks for more than a "possibility that a defendant has acted unlawfully." *Twombly*, 550 U.S. at 556. Dismissal is appropriate when the plaintiff fails to allege "'enough facts to state a claim to relief that is plausible on its face'" and therefore fails to "'raise a right to relief above the speculative level.'" *Montoya*, 614 F.3d at 148, *quoting*

Twombly, 550 U.S. at 555, 570. "[T]hreadbare recitals of the elements of a cause of action, supported by mere conclusory statements do not suffice" under Rule 12(b). *Iqbal*, 129 S. Ct. at 1949.

Dismissal under Rule 12(b)(6) is proper not only where the plaintiff fails to plead sufficient facts to support a cognizable legal theory, but also where the plaintiff fails to allege a cognizable legal theory. *Kjellvander v. Citicorp*, 156 F.R.D. 138, 140 (S.D. Tex. 1994), *citing Garrett v. Commonwealth Mortgage Corp.*, 938 F.2d 591, 594 (5th Cir. 1991); *ASARCO LLC v. Americas Min. Corp.*, 832 B.R. 49, 57 (S.D. Tex. 2007). "A complaint lacks an 'arguable basis in law' if it is based on an indisputedly meritless legal theory' or a violation of a legal interest that does not exist." *Ross v. State of Texas*, Civ. A. No. H-10-2008, 2011 WL 5978029, at *8 (S.D. Tex. Nov. 29, 2011).

As noted, on a Rule 12(b)(6) review, although generally the court may not look beyond the pleadings, the court may examine the complaint, documents attached to the complaint, and documents attached to the motion to dismiss to which the complaint refers and which are central to the plaintiff's claim(s), as well as matters of public record. *Lone Star Fund V (U.S.), L.P. v. Barclays Bank PLC*, 594 F.3d 383, 387 (5th Cir. 2010), *citing Collins*, 224 F.3d at 498-99; *Cinel v. Connick*, 15 F.3d 1338, 1341, 1343 n.6 (5th Cir. 1994). *See also United States ex rel. Willard v. Humana Health Plan of Tex., Inc.*, 336 F.3d 375, 379 (5th Cir. 2003) ("the court may consider . . . matters of which judicial notice may be taken"). Taking judicial notice of public records

directly relevant to the issue in dispute is proper on a Rule 12(b)(6) review and does not transform the motion into one for summary judgment. *Funk v. Stryker Corp.*, 631 F.3d 777, 780 (5th Cir. 2011). "A judicially noticed fact must be one not subject to reasonable dispute in that it is either (1) generally known within the territorial jurisdiction of the trial court or (2) capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned." Fed. R. Evid. 201(b).

B. Rule 9(b)

Federal Rule of Civil Procedure 9(b) provides,

> In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person must be averred generally.

"In every case based upon fraud, Rule 9(b) requires the plaintiff to allege as to each individual defendant 'the nature of the fraud, some details, a brief sketch of how the fraudulent scheme operated, when and where it occurred, and the participants." *Hernandez v. Ciba-Geigy Corp. USA*, 200 F.R.D. 285, 291 (S.D. Tex. 2001). In a securities fraud suit, the plaintiff must plead with particularity the circumstances constituting the alleged fraud: Rule 9(b) requires the plaintiff to "'specify the statements contended to be fraudulent, identify the speaker, state when and where the statements were made, and explain why the statements

were fraudulent.'" *Southland Securities Corp. v. INspire Ins. Solutions, Inc.*, 365 F.3d 353, 362 (5th Cir. 2004), *quoting Williams v. WMX Technologies, Inc.*, 112 F.3d 175, 177-78 (5th Cir. 1997), *cert. denied*, 522 U.S. 966 (1997). "'In cases concerning fraudulent misrepresentation and omission of facts, Rule 9(b) typically requires the claimant to plead the type of facts omitted, the place in which the omissions should have appeared, and the way in which the omitted facts made the representations misleading.'" *Carroll v. Fort James Corp.*, 470 F.3d 1171, 1174 (5th Cir. 2006), *quoting United States ex. rel. Riley v. St. Luke's Hosp.*, 355 F.3d 370, 381 (5th Cir. 2004).

Unlike the alleged fraud, Rule 9(b) allows a plaintiff to plead intent to deceive or defraud generally. Nevertheless a mere conclusory statement that the defendant had the required intent is insufficient; the plaintiff must set forth specific facts that raise an inference of fraudulent intent, for example, facts that show the defendant's motive. *Tuchman v. DSC Communications Corp.*, 14 F.3d 1061, 1068 (5th Cir. 1994) ("Although scienter may be averred generally, case law amply demonstrates that pleading scienter requires more than a simple allegation that a defendant had fraudulent intent. To plead scienter adequately, a plaintiff must set forth specific facts that support an inference of fraud."); *Melder v. Morris*, 27 F.3d 1097, 1102 (5th Cir. 1994).

The particularity requirement of Rule 9(b) also governs a conspiracy to commit fraud. *Southwest Louisiana Healthcare System v. MBIA Ins. Corp.*, No. 05-1299,

2006 WL 1228903, *5 & n.47 (W.D. La. May 6, 2006); *Hernandez v. Ciba-Geigy Corp. USA*, No. Civ. A. B-00-82, 2000 WL 33187524, *4 (S.D. Tex. Oct. 17, 2000) ("The weight of Fifth Circuit precedent holds that a civil conspiracy to commit a tort that sounds in fraud must be pleaded with particularity."); *In re Ford Motor Co. Vehicle Paint Litigation*, No. MDL 1063, 1994 WL 426548, *34 (E.D. La. July 30, 1996); and *Castillo v. First City Bancorporation of Texas, Inc.*, 43 F.3d 953, 961 (5th Cir. 1994).

A dismissal for failure to plead with particularity in accordance with Rule 9(b) is treated as a Rule 12(b)(6) dismissal for failure to state a claim. *Lovelace v. Software Spectrum, Inc.*, 78 F.3d 1015, 1017 (5th Cir. 1996).

C. The Exchange Act and the PSLRA's Heightened Pleading Requirements

The PSLRA "installed both substantive and procedural controls" that were "[d]esigned to curb perceived abuses of the § 10(b) private action – nuisance filings, targeting deep-pocket defendants, vexatious discover [sic] requests and manipulation by class action lawyers." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 208, 320 (2007). The PSLRA heightened the particularity requirements for pleading securities fraud in two ways: (1) the plaintiff must "specify each statement alleged to have been misleading and the reason or reasons why the statement is misleading . . . ," 15 U.S.C. § 78u-4(B)(1)(B); and (2) for "each act or omission

alleged" to be false or misleading, the plaintiff must "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind," 15 U.S.C. § 78u-4(b)(2). *Indiana Elec. Workers' Pension Trust Fund IBEW v. Shaw Group, Inc.*, 537 F.3d 527, 533 (5th Cir. 2007). As noted, Rule 9(b) requires the plaintiff in a securities fraud suit to "'specify the statements contended to be fraudulent, identify the speaker, state when and where the statements were made, and explain why the statements were fraudulent.'" *Southland*, 365 F.3d at 362, *quoting Williams v. WMX Technologies, Inc.*, 112 F.3d 175, 177-78 (5th Cir. 1997), *cert. denied*, 522 U.S. 966 (1997). *See* 15 U.S.C. § 78u-4. In other words, "'[p]leading fraud with particularity . . . requires 'time, place and contents of the false representations, as well as the identity of the person making the misrepresentation and what [that person] obtained thereby.'" *Williams*, 112 F.3d at 177 (5th Cir. 1997), *quoting Tuchman*, 14 F.3d at 1068.

"'In cases concerning . . . omission of facts, Rule 9(b) typically requires the claimant to plead the type of facts omitted, the place in which the omissions should have appeared, and the way in which the omitted facts made the representations misleading.'" *Carroll v. Fort James Corp.*, 470 F.3d 1171, 1174 (5th Cir. 2006), *quoting United States ex. rel. Riley v. St. Luke's Hosp.*, 355 F.3d 370, 381 (5th Cir. 2004). To meet the requirement of materiality, "there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as

having significantly altered the 'total mix' of information made available" and would have actually been significant "in the deliberations of the reasonable shareholder." *Basic, Inc.*, 485 U.S. at 231-32; *Southland*, 365 F.3d at 362. *See also Lormand v. US Unwired, Inc.*, 565 F.3d 228, 248-49 (5th Cir. 2009) ("Once the defendants engaged in public discussion . . . , they had a duty to disclose a 'mix of information that is not misleading."). Thus the standard for misrepresentation in this context is whether the information disclosed, understood as a whole, would mislead a reasonable potential investor. *L.W. Laird v. Integrated Resources, Inc.*, 897 F.2d 826, 832 (5th Cir. 1990). The Fifth Circuit has "long held under Rule 10b-5, a duty to speak the full truth arises when a defendant undertakes a duty to say anything. Although such defendant is under no duty to disclose every fact or assumption underlying a prediction, he must disclose material, firm-specific adverse facts that affect the validity or plausibility of that prediction." *Lormand*, 565 F.3d at 249. "The omission of a known risk, its probability of materialization, and its anticipated magnitude, are usually material to any disclosure discussing the prospective result from a future course of action." *Id.* at 248 These facts "must be laid out before access to the discovery process is granted." *Williams*, 112 F.3d at 178.

The Fifth Circuit does not permit group pleading of securities fraud suits. *Owens v. Jastrow*, 789 F.3d 529, 537 (5th Cir. 2015), *citing Southland*, 365 F.3d at 365 ("[T]he PSLRA requires the plaintiffs to distinguish

among those they sue and enlighten *each defendant* as to his or her particular part in the alleged fraud. . . . [W]e do not construe allegations contained in the [second amended complaint] against 'defendants' as a group as properly imputable to any particular defendant unless the connection between the individual defendant and the allegedly fraudulent statement is specifically pleaded.").[9] "Corporate officers are *not* liable for acts solely because they are officers or where their day-to-day involvement in the corporation is pleaded." *Financial Acquisition Partners LP v. Blackwell*, 440 F.3d 278, 287 (5th Cir. 2006). A corporate officer may be liable if plaintiff identifies him and alleges he made materially misleading statements with scienter at a shareholder meeting or he signed documents on which statements were made or which he was involved in creating. *Id.* Group pleading, or the group publishing doctrine, fails to satisfy the heightened pleading standards of the PSLRA. *Southland*, 365 F.3d at 363 n.9.

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[9] The group pleading or group publishing doctrine permits plaintiffs to presume that statements in prospectuses, registration statements, annual reports, press releases, etc. are collectively attributable to persons with direct involvement in the regular business of the company. *Southland*, 365 F.3d at 363 n.9. In its most expansive form it allows "unattributed corporate statements to be charged to one or more individual defendants based solely on their corporate title. Under this doctrine, the plaintiff need not allege any facts demonstrating an individual defendant's participation in the particular communication containing the misstatement or omission where the defendants are 'insiders or affiliates' of the company." *Id.* at 363.

The Fifth Circuit further requires that scienter or the requisite state of mind, which for the PSLRA is "an intent to deceive, manipulate, or defraud," or "'severe recklessness' in which the 'danger of misleading buyers or sellers . . . is either known to the defendant or is so obvious that the defendant must have been aware of it,'"[10] must be pleaded for each act or omission for each defendant in a multiple defendant case sufficiently to create "a strong inference that the defendant acted with the required state of mind." *Id.* at 364-65. *See also Owens v. Jastrow*, 789 F.3d at 536 ("Severe recklessness is limited to those highly unreasonable omissions or misrepresentations that involve not merely simple or inexcusable negligence, but an extreme departure from the standard of ordinary care, and that present a danger of misleading buyers or sellers which is either known to the defendant or is so obvious that the defendant must have been aware of it."), *quoting Abrams v. Baker Hughes, Inc.*, 292 F.3d 424, 430 (5th Cir. 2002). To determine whether a statement made by a corporation was made with the requisite intent, it is appropriate to look into the state of mind of the corporate official who made the statement rather than to the collective knowledge of all of the corporation's officers and employees acquired in the course of their employment. *Southland*, 365 F.3d at 366; *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135, 142 (2011) ("[T]he maker of a statement is the person or entity with ultimate authority over the statement, including

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[10] *Quoting Broad v. Rockwell Int'l Corp.*, 642 F.2d 929, 961-62 (5th Cir. 1981) (*en banc*).

its content and whether and how to communicate it."). "A defendant corporation is deemed to have the requisite scienter for fraud only if the individual corporate officer making the statement has the requisite level of scienter, i.e., knows that the statement is false or is at least deliberately reckless as to its falsity, at the time he or she makes the statement." *Id.* at 366.

"In determining whether the pleaded facts give rise to a 'strong' inference of scienter, the court must take into account plausible opposing inferences." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 323 (2007). Furthermore, the inference of scienter ultimately must be "'cogent and compelling,' not merely 'reasonable' or "permissible.'" "Congress required plaintiffs to plead with particularity facts that give rise to a 'strong' – *i.e.*, a powerful or cogent – inference." *Id. Indiana Elec. Workers' Pension Trust Fund IBEW v. Shaw Group, Inc.*, 537 F.3d 527, 533 (5th Cir. 2008), *quoting Tellabs, Inc.*, 551 U.S. at 324. "To determine whether the plaintiff has alleged facts that give rise to the requisite 'strong inference' of scienter, a court must consider plausible, nonculpable explanations for the defendant's conduct, as well as inferences favoring the plaintiff. The inference that the defendant acted with scienter need not be irrefutable, *i.e.*, of the 'smoking-gun' genre, or even the 'most plausible of competing inferences.'" *Id.* at 323-24. But it must be "at least as compelling as any opposing inference one could draw from the facts alleged." *Id.* at 324. "[A] tie favors the plaintiff." *Owens v. Jastrow*, 789 F.3d 529, 536 (5th Cir. 2015), *quoting Lormand v. US Unwired, Inc.*, 565 F.3d

228, 254 (5th Cir. 2009), *citing Tellabs*, 551 U.S. at 324. "The inquiry is whether all of the facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegations, scrutinized in isolation, meet that standard." *Lormand*, 565 F.3d at 251, *citing Tellabs*, 551 U.S. at 322-23. While allegations of motive and opportunity may serve to strengthen the inference of scienter, such allegations alone are insufficient to satisfy the requirement. *Flaherty & Crumrine Preferred Income Fund, Inc. v. TXU Corp.*, 565 F.3d 200, 208 (5th Cir. 2009); *Owens v. Jastrow*, 789 F.3d at 539.

If the plaintiff fails to satisfy the pleading requirements for scienter, "the district court 'shall,' on defendant's motion to dismiss, 'dismiss the complaint.'" *Nathenson*, 267 F.3d at 407, citing § 78u-4(b)(3).

Under the PSLRA, 15 U.S.C. § 78u-4(b)(4), a plaintiff must also allege and ultimately prove "the traditional elements of causation and loss," 'that the defendant's misrepresentations (or other fraudulent conduct) proximately caused the plaintiff's economic loss." *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336, 346 (2005). The plaintiff must plead economic loss and loss causation, i.e., a causal connection between the material misrepresentation or omission and the loss. *Id.* at 341-42. "[A]n inflated purchase price will not itself constitute or proximately cause the relevant loss. *Id.* at 342. To establish proximate causation, the plaintiff must prove that when the "relevant truth" about the fraud began to leak out or otherwise make its way into the marketplace, it caused the price of the

stock to depreciate and thereby proximately caused the plaintiff's economic injury. *Lormand*, 565 F.3d at 255 ("[W]e conclude that Rule 8(a)(2) requires the plaintiff to allege, in respect to loss causation, a facially 'plausible' causal relationship between the fraudulent statements or omissions and plaintiff's economic loss, including allegations of a material misrepresentation or omission, followed by the leaking out of relevant or related truth about the fraud that caused a significant part of the depreciation of the stock and plaintiff's economic loss."), *citing Dura* at 342, 346.

II. Applicable Substantive Law

A. The 1934 Act and Rule 10b-5

Section 10(b) of the Securities Exchange Act states in relevant part,

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of any facility of any national securities exchange . . .
>
> (b) To use or employ in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement (as defined in [S]ection 206B of the Gramm-Leach-Bliley Act), any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

The Securities and Exchange Commission ("SEC") promulgated Rule 10b-5 pursuant to the statute:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) to employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, 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.

B. Primary v. Secondary Violators: Central Bank, Stoneridge and Janus

For many years plaintiffs in securities fraud suits brought claims under § 10(b) and Rule 10b-5 against secondary actors,[11] including investment bankers, lawyers

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[11] Judge Jose A. Cabranes in *Pacific Inv. Management Co., LLC v. Mayer Brown LLP*, 603 F. 3d 144, 148 n.1 (2d Cir. 2010), *cert. denied*, 564 U.S. 1018 (2011), defines "secondary actor" as a term for "lawyers . . . , accountants, or other parties who are not employed by the issuing firm whose securities are the subject of allegations of fraud." *Id., citing Stoneridge Investment Partners,*

and accountants, who participated with primary violators in a scheme to defraud investors. In the last twenty years, the Supreme Court has greatly limited the reach of a private right of action against secondary actors under Rule 10b-5(a) and (c). Despite the fact that for three decades secondary actors had been found liable under the federal securities laws as aiders and abettors in lower courts, given the 1934 Act's silence as to aiding and abetting, the Supreme Court has concluded, "The section 10(b) implied private right of action does not extend to aiders and abettors." *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 158 (2008); *see also Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 177-78 (1994) (for private parties[12] Section 10(b) "does not itself reach those who aid and abet" a primary wrongdoer's violation of the securities laws because while the statute prohibits the making of a material misstatement or omission or the commission of a manipulative act, the "proscription does not "include giving aid to a person who commits a manipulative or deceptive act"; "We cannot amend the statute to create liability for acts that are not themselves manipulative or deceptive within the meaning of the statute." 511 U.S. at 177-78. Instead to impose liability, a

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LLC v. Scientific-Atlanta, Inc., 552 U.S. 148, 166 (2008) ("using the term '[s]econdary actors' to refer to an issuing firm's customers and suppliers"), and *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 191 (1994).

[12] The PSLRA added Section 20(e), 15 U.S.C. § 78t(e), to the 1934 Act, affirming the right of the SEC to prosecute aiders and abettors in enforcement actions.

plaintiff must establish that each named defendant committed its own primary violation of the securities laws to be held liable under § 10(b). Moreover the Supreme Court concluded that in some circumstances secondary actors, like lawyers, investment banks, and accountants, "who employ[ ] a manipulative device or make[ ] a material misstatement (or omission) on which a purchaser or seller of securities relies," can be liable as primary violators if "*all* the requirements for primary liability under Rule 10b-5 are met." *Id.* at 191. *In accord,Stoneridge*, 552 U.S. at 158 (For a secondary actor to be held liable under § 10(b), that person or entity "must satisfy each of the elements or preconditions for [primary] liability.").

The six elements of a private cause of action for a primary violation under § 10(b) are "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation." *Stoneridge*, 552 U.S. at at [sic] 157.

"Where liability is premised on a failure to disclose rather than on a misrepresentation, 'positive proof of reliance[13] is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have

[13] "[P]roof of reliance ensures that there is a proper 'connection between a defendant's misrepresentation and a plaintiff's injury.' " *Erica P. John Fund, Inc. v. Halliburton Co.*, 563 U.S. 804, 810 (2011), *quoting Basic, Inc.*, 485 U.S. 243.

considered them important in the making of this decision. . . . This obligation to disclose and the withholding of a material fact establish the requisite element of causation in fact.'" *Regents of Univ. of Cal. v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372, 383-84 (5th Cir. 2007) (*quoting Affiliated Ute Citizens of the State of Utah v. U.S.*, 406 U.S. 128, 153-54 (1972)), *cert. denied sub nom. Regents of Univ. of Cal. v. Merrill Lynch, Pierce, Fenner & Smith*, 552 U.S. 1170 (2008). *See also Basic, Inc.*, 485 U.S. at 243 ("[W]here a duty to disclose material information had been breached . . . the necessary nexus between the plaintiffs' injury and the defendants' wrongful conduct had been established.").

"When an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak." *Central Bank*, 511 U.S. at 174, *quoting Chiarella v. U.S.*, 445 U.S. 222, 235 (1980). A duty to disclose arises only from "a fiduciary or other similar relation of trust and confidence between [parties]"; it "does not arise from the mere possession of nonpublic market information." *Chiarella*, 445 U.S. at 228, 235. "Silence, absent a duty to disclose, is not misleading under Rule 10b-5." *Basic, Inc. v. Levinson*, 485 U.S. 224, 239 n. 17 (1988). The omission of a material fact by a defendant with a duty to disclose establishes a rebuttable presumption of reliance upon the omission by investors to whom the duty was owed. *Affiliated Ute Citizens of the State of Utah v. U.S.*, 406 U.S. 126, 153-54 (1972). "To invoke the *Affiliated Ute* presumption of reliance on an omission, a 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." *Regent of Univ. of Cal.*, 482 F.3d at 384. "This presumption is a judicial creature. It responds to the reality that a person cannot rely upon what he is not told." *Smith v. Ayres*, 845 F.2d 1360, 1363 (5th Cir. 1988). "[A]dministrative and judicial interpretations have established that silence in connection with the purchase or sale of securities may operate as a fraud actionable under § 10(b)" when there is "a duty to disclose arising from a relationship of trust and confidence between parties to a transaction." *Chiarella*, 445 U.S. at 230.

"Whether a fiduciary duty exists is a question of law for the court's determination." *Stevenson v. Rochdale Investment Management, Inc.*, No. Civ. A. 3:97CV1544L, 2000 WL 1278479, at *3 (N.D. Tex. Sept. 7, 2000), *citing Fuqua v. Taylor*, 683 S.W. 2d 735, 737 (Tex. App. – Dallas 1984, writ ref'd n.r.e.). Nevertheless the factfinder determines whether the facts give rise to a fiduciary duty. *Id.*

In *Kinzbach Tool Co. v. Corbett-Wallace Corp.*, 138 Tex. 565, 160 S.W. 2d 509, 512-13 (Tex. 1942), the Texas Supreme Court wrote,

> The term "fiduciary" is derived from the civil law. It is impossible to give a definition of the term that is comprehensive enough to cover all cases. Generally speaking, it applies to any person who occupies a position of peculiar confidence toward another. It refers to integrity and fidelity. It contemplates fair dealing and

> good faith, rather than legal obligation, as the basis of the transaction. The term includes those informal relations which exist whenever one party trusts and relies upon another, as well as technical fiduciary relations.

See also Fisher v. Roper, 727 S.W. 2d 78, 81 (Tex. App. – San Antonio 1987, writ ref'd n.r.e.):

> A fiduciary relationship exists when the parties are under a duty to act for or give advice for the benefit of another upon matters within the scope of the relation. It exists where a special confidence is reposed in another who in equity and good conscience is bound to act in good faith and with due regard for the interest of the one reposing confidence. A fiduciary relationship generally arises over a long period of time when parties have worked together toward a mutual goal. To establish a fiduciary relationship, the evidence must show that the dealings between the parties have continued for such a period of time that one party is justified in relying on the other to act in his best interest. To transform a mere contract into a fiduciary relationship, the evidence must show that the dealings between the parties have continued for such a period of time that one party is justified in relying on the other to act in his best interest. [citations omitted].

For example, because of the relationship of trust and confidence between the shareholders of a corporation and "those insiders who have obtained confidential information by reason of their position with that corporation," courts have imposed a duty to disclose on

a corporate insider when the corporate insider trades on the confidential information ("intended to be available only for a corporate purpose and not for the personal benefit of anyone") and makes secret profits. *Chiarella*, 445 U.S. at 227-28. "Trading on such [material, nonpublic] information qualifies as a 'deceptive device' under § 10(b) . . . because 'a relationship of trust and confidence [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, 651-52 (1997)*, citing Chiarella*, 445 U.S. at 228. "That relationship . . . gives rise to a duty to disclose [or to abstain from trading] because of the 'necessity of preventing a corporate insider from . . . tak[ing] unfair advantage of . . . uninformed shareholders.'" *O'Hagan*, 521 U.S. at 652, *quoting Chiarella*, 445 U.S. at 228-29. A corporate insider with material information is required to disclose it to the investing public or, if he cannot because he must protect a corporate confidence, or if he chooses not to disclose, he must abstain from trading in or recommending securities concerned while the inside information remains undisclosed. *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 848 (2d Cir. 1968) (*en banc*) ("[A]nyone 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."), *cert. denied sub nom. Kline v. SEC*, 394 U.S. 976 (1969).

An individual or entity that does not fit within the traditional definition of a corporate insider may become a "temporary insider" if the person "by entering into a special confidential relationship in the conduct of the business of the enterprise is given access to information solely for corporate purposes." *SEC v. Cuban*, 620 F.3d 551, 554 (5th Cir. 2010), *citing Dirks v. SEC*, 463 U.S. 646, 655 n.13 (1983). The duty to disclose or abstain from trading arises from the corporate insider's duty to his shareholders, and it applies not only "to officers, directors and other permanent insiders of a corporation," but also to "attorneys, accountants, consultants and others who temporarily become fiduciaries of the corporation." *O'Hagan*, 521 U.S. at 228-29, *quoting Dirks v. SEC*, 463 U.S. 646, 655 n.14 (1983).

Violations of Rule 10b-5(a) and (c), which prohibit "employ[ing] any device, scheme or artifice to defraud" or "engag[ing] in any act, practice or course of business which operates . . . as a fraud or deceit upon any person" in connection with the sale of securities, were designated by some courts as scheme liability. In *Stoneridge* (5-3), the Supreme Court addressed the issue, "when, if ever, an injured investor may rely upon § 10(b) to recover from a party that neither makes a public misstatement nor violates a duty to disclose, but does participate in a scheme to violate § 10(b)" and rejected the theory because a plaintiff cannot rely on a defendant's concealed deceptive acts. 552 U.S. at 156, 159-60. Justice Kenney [sic] wrote for the majority,

> Reliance by the plaintiff upon the defendant's deceptive acts is an essential element of the

> § 10(b) private cause of action. It ensures that, for liability to arise, the "requisite causal connection between a defendant's misrepresentation and a plaintiff's injury" exists as a predicate for liability. . . . We have found a rebuttable presumption of reliance in two different circumstances. First, if there is an omission of a material fact by one with a duty to disclose, the investor to who the duty was owed need not provide specific proof of reliance. . . . Second, under the fraud-on-the-market doctrine, reliance is presumed when the statements at issue become public. The public information is reflected in the market price of the security. Then it can be assumed that an investor who buys or sells stock at the market price relies upon the statement. . . .
>
> Neither presumption applies here. Respondents had no duty to disclose; and their deceptive acts were not communicated to the public. No member of the investing public had knowledge, either actual or presumed, of respondents' deceptive acts during the relevant times. Petitioner, as a result, cannot show reliance upon any of respondents' actions except in an indirect chain that we find too remote for liability.

Id. at 769.

In *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135, 137-38, 142, 167 (2011) (5-4), examining what it means to "'make any untrue statement of material fact' in connection with the purchase or sale of securities" under Rule 10b-5 and "mindful

that [the Court] must give 'narrow dimensions' " to the implied right of action under § 10(b) since Congress did not authorize it,[14] the majority of the Supreme Court attempted to further clarify the distinction between a primary violation and aiding and abetting by holding, "For purposes of Rule 10b-5, the maker of a statement is the person with ultimate authority over the statement, including its content and whether and how to communicate it. Without control, a person or entity can merely suggest what to say, not 'make' a statement in

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[14] The majority of the Supreme Court began by construing the word "make" in Rule 10b-5 very narrowly:

> One "makes" a statement by stating it. When "make" is paired with a noun expressing the action of a verb, the resulting phrase is "approximately equivalent in sense" to that verb. 6 Oxford English Dictionary 66 (def. 59) (1933) (hereinafter OED). . . . For instance, "to make a proclamation" is the approximate equivalent of "to proclaim," and "to make a promise" approximates "to promise." See 6 OED 66 (def. 59). The phrase at issue in Rule 10b-5, "to make any . . . statement." is thus the approximate equivalent of "to state."

In the dissent, Justice Breyer, joined by Justices Ginsburg, Sotomayor, and Kagen [sic], opined,

> In my view, . . . the majority has incorrectly interpreted the Rule's word "make." Neither common English nor this Court's earlier cases limit the scope of that word to those with "ultimate authority" over a statement's content. To the contrary, both language and case law indicate that, depending upon the circumstances, a management company, a board of trustees, individual company officers, or others, separately or together, might "make" statements contained in a firm's prospectus – even if a board of directors has ultimate content-related responsibility.

Id., 564 U.S. at 149-50.

its own right. One who prepares or publishes a statement on behalf of another is not its maker."[15] *See also Halliburton Co. v. Erica P. John Fund, Inc.*, 134 S. Ct. 2398, 2403 (2014) (Section 10(b) and Rule 10b-5 liability should not be extended "to entirely new categories of defendants who themselves had not made any material public misrepresentation."). Thus *Janus* restricts liability under a § 10(b) private right of action to a person or entity with ultimate authority over a false statement on which an investor relied to his detriment in purchasing or selling a security.

III. Stock Broker Standards

At issue in this case is whether PW, in its brokerage relationship with the investors in the Enron Stock Option program, had a fiduciary duty to disclose material information to its investor retail clients.

Firms in the securities market operate in three main capacities: broker, broker-dealer, and investment advisor. Thomas Lee Hazen, "Are Existing Stock Broker Standards Sufficient?," 2010 Colum. Bus. L. Rev. 710, 730 (2010).

A "broker" is defined in *Black's Law Dictionary* (6th ed. West 1990), as, "An agent employed to make

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[15] The high court compared the relationship between the aider and abettor and the primary violator to that between a speechwriter and a speaker: "Even when a speechwriter drafts a speech, the content is entirely within the control of the person who delivers it. And it is the speaker who takes credit – or blame – for what is ultimately said." *Id.* at 143.

bargains and contracts for compensation. A dealer in securities issued by others. . . . An agent of a buyer or seller who buys or sells stocks, bonds, commodities, or services, usually on a commission basis." *See also Rauscher Pierce Refsnes, Inc. v. Great Southwest Sav., F.A.*, 923 S.W. 2d 112, 115 (Tex. App. – Houston [14th Dist.] 1996) ("The relationship between a broker and its customer is that of principal and agent."). Under the Exchange Act, 15 U.S.C. § 78c(a)(4)(A), a broker is "any person engaged in the business of effecting transactions in securities for the account of others."

A "broker-dealer" is defined as a "securities brokerage firm, usually registered with the S.E.C. and with the state in which it does business, engaging in the business of buying and selling securities to or for customers." *Black's Law Dictionary* (6th ed. West 1990).[16] There is no explicit fiduciary standard applicable to

[16] Under the Exchange Act a "dealer" is a person who engages in "the business of buying and selling securities . . . for such person's own account," and not as part of a regular business. 15 U.S.C. § 78c(a)(5)(A). The term broker-dealer includes persons who act as brokers, dealers, or both brokers and dealers. Tuch, *Self-Regulation*, 83 Geo. Wash. L. Rev. at 117. In the context of securities offerings, an investment banker plays two roles: it counsels the corporate issuer and, if it underwrites the offering on a firm-commitment basis, commits to acquiring the issuer's securities, and it sells those securities to investors. *Id.* at 114-15. Investment banks are correctly designated as broker-dealers, as evidenced by FINRA rules and the SEC's *Guide to Broker-Dealer Registration*. *Id.* at 118. In particular they qualify as brokers where they advise on security offerings, are involved in the sale or exchange of securities and receive fees for that service, negotiate between the issuer and the investor, and counsel on structuring transactions. *Id.* at 118-20.

broker-dealers under the Exchange Act,[17] but when they do more than act as order takers for their clients' transactions, they must meet other standards, including of suitability in making investment recommendations to their clients, and they must satisfy the self-regulatory organizations ("SROs"), including national securities exchanges and the Financial Industry Regulatory Authority ("FINRA," the self-regulatory body for broker-dealers)") that oversee them. Thomas Lee Hazen, "Fiduciary Obligations of Securities Brokers," 5 Law Sec. Reg. § 14:133 (March 2016 update).

Thus while a broker owes his investor-client a fiduciary duty, that duty varies in scope with the nature of their relationship, and determining that nature requires a fact-based analysis. *Romano v. Merrill Lynch, Pierce, Fenner & Smith*, 834 F.2d 523, 520 (5th Cir. 1987), *cert. denied*, 487 U.S. 1205 (1988). The nature of the account, whether nondiscretionary or discretionary, is one factor to be considered, as are the degree of trust placed in the broker and the intelligence and qualities of the customer. *Id.* A broker's duty is usually restricted to executing the investor's order when "the investor controls a nondiscretionary account and retains the ability to make investment decisions[18]; however,

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[17] Section 913(g) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111-203, 124 Stat. at 1827-28, gives the SEC rulemaking authority to impose a fiduciary duty on broker-dealers.

[18] On the other hand, where the broker's duty simply consists of bringing parties together so they can negotiate a sale by themselves, he is merely a middleman and not necessarily an "agent" of any. *Rauscher*, 923 S.W. 2d at 115. The question whether an

when investors "lack the time, capacity, or know-how to supervise investment decisions" and "delegate authority to a broker who will make decisions in their best interests without prior approval," in a discretionary account there well may be a duty to disclose. *Town North Bank, N.A. v. Shay Financial Services, Inc.*, Civ. A. No. 3:11-CV-3125-L, 2014 WL 4851558, at *17 (N.D. Tex. Sept. 30, 2014), *citing Martinez Tapia v. Chase Manhattan Bank, N.A.*, 149 F.3d 404, 412 (5th Cir. 1998),[19] and *SEC v. Zandford*, 535 U.S. 813, 823 (2002). Under Texas law,

> In a non-discretionary account, the agency relationship begins when the customer places the order and ends when the broker executes it because the broker's duty in this type of account, unlike those of an investment advisor or those of a manager of a discretionary account, are "only to fulfill the mechanical, ministerial requirements of the purchase or sale of the security. . . ." As a general proposition, a broker's duty in relation to a nondiscretionary account is complete, and his authority ceases, when the sale or purchase is made and the receipts therefrom accounted for. Thus, each

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agency relationship exists is usually a question of fact. *Coleman v. Klockner & Co.*, 180 S.W. 3d 577, 587 (Tex. App. – Houston [14th Dist.] 2005)

[19] *Citing Hill v. Bache Halsey Stuart Shields, Inc.*, 790 F.2d 817, 825 (11th Cir. 1996) ("fiduciary duty in the context of brokerage relationship is only an added degree of responsibility to carry out pre-existing, agreed-upon tasks properly"); *Limbaugh v. Merrill Lynch Pierce, Fenner & Smith*, 732 F.2d 859, 862 (11th Cir. 1984) ("duty owed by the broker was simply to execute the order").

> new order is a new request that the proposed agent consents to act for the principal. There is no on-going agency relationship as there would be with a financial advisor or manager of a discretionary account.

Hand v. Dean Witter Reynolds, Inc., 889 S.W. 2d 483, 493-94 (Tex. App. – Houston [14th Dist.] 1994, writ denied) (citations omitted).

In a discretionary investment account, in contrast, a broker is a "fiduciary of his customer in a broad sense" and is required to

> (1) manage the *account* in a manner directly comporting with the needs and objectives of the customer as stated in the authorization papers or as apparent from the customers' investment and trading history; (2) keep informed regarding the changes in the *market* which affect his customer's interest and act responsively to protect these interests; (3) keep his customer informed as to each completed *transaction*; and (4) explain forthrightly the practical impact and potential risks of the *course of dealing* in which the broker is engaged.

Anton v. Merrill Lynch, 36 S.W. 3d 251, 157-58 [sic] (Tex. App. – Austin 2001, rev. denied) (citations omitted, emphases added), *quoting Leib v. Merrill Lynch, Fenner &*

Smith, Inc., 461 F. Supp. 951, 953 (E.D. Mich. 1978), *aff'd*, 647 F.2d 165 (6th Cir. 1981).[20]

Although there is no statutorily mandated heightened pleading of fiduciary duty for brokers, Thomas Lee Hazen, a noted scholar in the field, points out that "there is plenty of authority under the existing law that recognizes heightened obligations of securities broker-dealers, at least when they are acting in a capacity beyond that of mere order taker. . . . The law, regulations, and regulatory interpretations to date make clear that broker-dealers have fiduciary or fiduciary-like obligations when they provide services beyond executing customer orders." Hazen, "Are Existing Stock Broker Standards Sufficient?," 2010 Colum. Bus. L. Rev. 710, 713-14 (2010). These legal sources include the Investment Advisers Act of 1940, regarding which the Supreme Court has held that, even though the word "fiduciary" does not appear in the statute, investment advisers are fiduciaries to their clients and must meet the fiduciary duties of care and loyalty, i.e., they must [sic] "must fully disclose material facts about prospective investments . . . [and] all conflicts of interests when giving advice." *Id.* at 716, *citing SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 191-92 (1963). A

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[20] Also cited by other courts in the Fifth Circuit, e.g., *In re Rea*, 245 B.R. 77, 88, 89-90 (N.D. Tex. 2000); *Puckett v. Rufenacht, Bromagen & Hertz*, Civ. App. No. H88-0035(W), 1989 WL 265340, at *5 (S.D. Miss. May 31, 1989), *aff'd in part by* 903 F.2d 1014 (5th Cir. 1990), *amended by* 919 F.2d 992 (1990), *certified question* ("*What duty of care under Mississippi law does a commodities broker owe to commodities customers in a nondiscretionary account?*") *answered by* 587 So. 2d 273 (Miss. 1991).

fundamental purpose common to a number of statutes enacted in the 1930's, including the Investment Advisers Act and the 1934 Act, "was to substitute a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the securities industry." *SEC v. Capital Gains Research Bureau*, 375 U.S. at 186.

The Investment Advisers Act of 1940, 15 U.S.C. § 80b-2(a)(11), however, defines "investment adviser" in relevant part as follows:

> "Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities, but does not include . . . (C) any broker or dealer whose performances of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor. . . ."

The Court concludes from the allegations in the complaint and the lack of mention of any special compensation for investment advisor advice that PW does not qualify as an investment advisor under subsection (C). *See, e.g.*, *Banca Cremi, S.A. v. Alex. Brown & Sons, Inc.*, 132 F.3d 1017, 1039 (4th Cir. 1997) ("In this case, it is clear that, to the extent that Epley and Alex. Brown

provided 'investment advisory services,' such services were "'solely incidental to the conduct of business as a broker dealer'" and "the Bank was not an 'advisory client' of the defendants."),

Furthermore the Supreme Court has held that private rights of action under the Investment Advisers Act of 1940 are restricted to suits for equitable relief for rescission of investment adviser contracts and restitution under section 215; damages are not available. *Transamerica Mortg. Advisors, Inc. v. Lewis*, 444 U.S. 11 (1979). "'[T]he rescinding party may have restitution of the consideration given under the contract, less any value conferred by the other party.'" *Douglass v. Beakley*, 900 F. Supp. 2d 736, 745 (N.D. Tex. 2012), *citing Transamerica Mortg. Advisors*, 444 U.S. at 18-24. The SEC may enforce the Act by obtaining an injunction mandating that a registered investment adviser disclose to his clients any of the adviser's violations of his duties under the Act. *Capital Gains*, 375 U.S. at 181.[21]

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[21] As the Fifth Circuit observed in *Laird v. Integrated Resources, Inc.*, 897 F.2d 826, 833-37 (5th Cir. 1990), "Other circuits understand the investment adviser's fiduciary status to require disclosure of any conflicts of interest for the purpose of assessing liability under rule 10(b)-5." *Id.*, *citing and discussing SEC v. Blavin*, 760 F.3d 706, 711-12 (6th Cir. 1985) ("As a fiduciary, the standard of care to which an investment adviser must adhere imposes 'an affirmative duty of 'utmost good faith, and full and fair disclosure to all material facts,' as well as an affirmative obligation to 'employ reasonable care to avoid misleading' his clients.") (citing *Capital Gains*), and *Zweig v. Hearst Corp.*, 594 F.2d 1261, 1267-68 (9th Cir. 1979) (addressing section 206(1) and (2) ("It shall be unlawful for any investment adviser, by use of the mails

Relevant to the determination whether broker-dealers have fiduciary or fiduciary-like obligations when they provide services beyond executing customer orders are SEC rules, particularly addressing "(a) conflicts between the firm's obligations to its customers and its own financial interests, and (b) trading in or recommending securities in the absence of adequate information about the issuer," made pursuant to the general anti-fraud provisions of sections 10(b), 15 U.S.C. § 78j(b), and 15(c), 15 U.S.C. § 78o(c), of the 1934 Act, section 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a),[22] and section 206 of the Investment

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and any means or instrumentality of interstate commerce, directly of indirectly (1) to employ any device, scheme, or artifice to defraud any client or prospective client; (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client. . . ."), which tracks the language in Rule 10b-5, of the Investment Advisers Act, as amended 15 U.S.C. § 80b-6(1,2), as analogous to § 10(b) and Rule 10b-5 of the Securities Exchange Act) ("The plaintiffs here do not argue that Campbell was an investment adviser as defined in the statute; thus *Capital Gains* is not controlling. But the failure to bring the case within the Investment Advisers Act does not mean that the claim under Section 10(b) and Rule 10b-5 should fail. We hold that as applied to the facts we must assume in this case, the Investment Advisers Act was not meant to limit the Securities Exchange Act or Rule 20b-5. Instead, we believe these provisions complement each other and provide different means to curb slightly different types of 'fraud or deceit.' . . . A number of cases since *Capital Gains suggest that Rule 10b-5 requires the disclosure of conflicts of interests in situations similar to the facts of this case*.").

[22] Section 77q(a), addressing "Use of interstate commerce for purpose of fraud or deceit, states,

> It shall be unlawful for any person in the offer or sale of any securities (including security-based swaps) or

Advisers Act, described *supra.* Hazen, "Are Existing Stock Broker Standards Sufficient?," 2010 Colum. Bus. L. Rev. at 722.

In the late 1930's, Congress amended the Exchange Act to authorize self-regulatory organizations for broker dealers. *See, e.g.*, Andrew F. Tuch, *The Self-Regulation of Investment Bankers*, 83 Geo. Wash. L. Rev. 101, 112 & n.50 (December 2014), *citing* Securities Exchange Act of 1934, Pub. L. No. 73-291, 48 Stat. 8881 (codified as amended at 15 U.S.C. §§ 78a-78pp (2012)). Hazen particularly highlights the SEC and FINRA[23]

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any security-based swap agreement (as defined in section 78c(a) (78) of this title) or by use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

[23] The governing complaint, #81 at ¶ 43, states,

43. The 1934 Act established a self-regulating scheme by means of self-regulatory organizations ("SROs"), including the National Association of Securities Dealers, Inc. ("NASD") and the New York Stock Exchange ("NYSE"). The Securities and Exchange Commission ("SEC"), in turn, supervises these SROs. The SROs developed rules of professional conduct to act as industry

[formed in 2007 to replace the National Association of Securities Dealers ("NASD")] regulations[24] as sources of fiduciary-like duties. *Id.* at 733-55. Sections 6(b)(5) and 15A(b)(6) of the Securities Exchange Act require stock exchanges and associations of brokers and securities dealers to establish rules to protect the investing public from fraudulent and manipulative practices in the securities market. 15 U.S.C. § 78o-3(b)(6). In response, a number of national exchanges and SROs

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standards, some of which focus on customer protection and investor rights. Although the 1934 Act provides no specific right of action for a violation of a SRO rule or regulation, nevertheless a breach of such a rule or regulation implicates a violation fo [sic] Section 10(b)/Rule 10b-5. During the 1934 Act Class Period, as well as today, SRO rules and regulations governed UBS's communications and relationship with its retail clients. By way of example, NASD Rule 2210(d) is one of a number of NASD and NYSE rules generally requiring its members, such as UBS, to deal fairly with their customers. It mandates that:

> All member communications with the public shall be based on principles of fair dealing and good faith and should provide a sound basis for evaluating the facts in regard to any particular security or securities or type of security, industry discussed, or service offered. No material fact or qualification may be omitted if the omission, in light of the context of the material presented, would cause the communications to be misleading.

[24] For example, Article III, NSAD [sic] Rules of Fair Practice, NASD Manual (CCH) ¶ 2151 provides, "A member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade."

have adopted "suitability rules" for brokers. The NASD adopted Rule 2310(a), which provides,

> In recommending to a customer the purchase, sale or exchange of any security, a member shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs." This is the so-called "suitability rule," and its purpose is to protect unsophisticated investors of publicly-held corporations from the sometimes devious practices of unscrupulous securities transactions experts.

The NYSE adopted a similar, "know your customer rule," NYSE Rule 405(a), which requires the officers of member organizations to "use diligence to learn essential facts relative to every customer, every order, every cash or margin account accepted or carried by such organization." Generally regulatory rules of conduct do not provide a private right of action for individual investors, but are for actions brought by the SEC or state regulatory investors. As a result, aggrieved individual investors must frame their securities complaints as claims under § 10(b) of the Exchange Act and Rule 10b-5. Steven D. Irwin, Scott A. Lane, and Carolyn W. Mendelson, *Wasn't My Bother* [sic] *Always Looking Out For My Best Interests? The Road to Become a Fiduciary*, 12 Duquesne Bus. L. J. 41,44-45 (Winter 2009) ("In itself, the regulatory violation does not state an independent claim for economic relief in a civil proceeding for the

investor who suffered a loss at the hands of a broker who has made an unsuitable trade recommendation. Instead, the aggrieved investor must state a valid claim under Rule 10b-5. The plaintiff must allege, in connection with the purchase or sale of securities, the misstatement or omission of a material fact, made with scienter, upon which the plaintiff justifiably relied and which proximately caused the plaintiff's injury.").

Hazen comments that regarding violations of NYSE, FINRA or NASD rules, "it is generally held that violation of a rule or a self regulatory organization will not, by itself, support a private right of action. However, a violation of an exchange or FINRA rule can form the basis of a 10b-5 action, provided of course, that all of the elements of a 10b-5 claim can be established." "Market Regulation: Broker-Dealer Regulation; Credit Rating agencies," 5 Law Sec. Reg. § 14:175 (updated March 2016). The courts are split in a variety of ways over whether a private right of action exists for violations of such rules and regulations.

The Fifth Circuit has deliberately chosen not to decide whether rules for brokers established by national exchanges and SROS, such as the NASD suitability rule or the NYSE "know your customer rule," provide a private cause of action for individual investors, but found they may be used as evidence of industry standards and practices. *Miley v. Oppenheimer & Co., Inc.*, 637 F.2d 318, 333 (5th Cir. 1981) (*en banc*) (in a churning case "NYSE and NASD rules are excellent tools against which to assess in part the reasonableness or excessiveness of a broker's handling of an

investor's account," the other five factors being the nature and objectives of the account, the turnover rate, in-and-out trading, the holding period of the respective securities, and the broker's profit), *abrogated on other grounds*, 470 U.S. 213 (1985).

The Securities Exchange Act has no express civil remedy for a violation of an exchange or association rule. In a seminal opinion in *Colonial Realty v. Bache and Co.*, 358 F.2d 178, 181 (2d Cir. 1965), *cert. denied,* 385 U.S. 817 (1966), in which a client sued his broker-dealer for failure to conduct its dealings in accordance with just and equitable principles of trade in violation of NYSE and NASD rules, Judge Henry J. Friendly opined that since a private remedy is not expressly stated in the 1934 Act, the finding of an implied private cause of action should be based on the court's duty to effect Congress's purpose in the statute and the federal policy it has adopted. A court may find an implied right of action under the Securities Exchange Act where there is explicit condemnation of certain conduct in the statute and when the statute provides a general grant of jurisdiction to enforce liability. *Id.* Judge Friendly concluded that there could be no general rule as to when a private claim can be maintained for a violation of NYSE and NASD rules because "the effect and significance of particular rules may vary with the manner of their adoption and their relationship to provisions and purpose of the statute and SEC regulations thereunder." An implied action may arise from the protection intended by the legislature and the ineffectiveness of existing administrative and judicial remedies to

accomplish. The court must examine the nature of the specific rule and its role in the regulatory scheme, with the party seeking to impose liability bearing a heavier burden of persuasion than the violation of the statute or of an SEC regulation would require. *Id.* at 182. Judge Friendly concluded, "The case for implication of liability would be strongest when the rule imposes an explicit duty unknown to the common law." *Id.* Judge Friendly found that a private cause of action may exist under section 6 of the 1934 Act, which requires a securities association like the NASD to adopt disciplinary rules. *Id.* 181-83. He found an implied cause of action where the rule that was violated either constituted a substitute for an SEC regulation and where the rule that was violated established an explicit duty unknown to the common law. *Id.* at 182.

As indicated in *Miley*, the Fifth Circuit has been hesitant to recognize a private cause of action based only on a violation of a NYSE or NASD rule. *See also Porter v. Shearson Lehman Bros., Inc.*, 802 F. Supp. 41, 61 (S.D. Tex. 1992), in which the Honorable Ewing Werlein, noting Judge Friendly's opinion, emphasized that the 1934 Act "did not specifically authorize actions for violation of private associations rules," including the "suitability" rule of NASD, which "requires generally that a broker recommend a purchase or sale only after determining that the recommendation is suitable to the customer, and that he use due diligence to learn essential facts regarding the customer. . . . Congress could not have meant that NASD should be given the authority to define new crimes." Observing that district courts

within the Fifth Circuit were split about whether an implied cause of action may be based on the NASD or stock exchange rules, Judge Werlein observed that in *Miley* and in *Jolley v. Welch*, 904 F.2d 988, 993 (5th Cir. 1990), *cert. denied*, 498 U.S. 1050 (1981), the Fifth Circuit permitted the NYSE and NASD rules to be considered as one of six factors in determining an element of an excessive trading violation (churning), but not as a private cause of action. *Porter*, 802 F. Supp. at 62-63. *See also Lange v. H. Hentz & Co.*, 418 F. Supp. 1376 (N.D. Tex. 1976) (NASD rules are evidence of the standard of care NASD members should provide and are admissible in determining the question what fiduciary duties are owed by a broker to his investor).

In 1988 Congress passed Section 15(f) of the Exchange Act, 15 U.S.C. § 78o(f),[25] and Section 204A of the Investment Advisers Act, 15 U.S.C. § 8ob-4a,[26]

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[25] Section 78o(f) provides,

> Every registered broker or dealer shall make appropriate rules or regulations about these policies and procedures. *See* 17 C.F.R. §§ 230.37 [sic], 230.138, 230.139. Thus an investment bank is required to erect a Chinese wall between its securities analysts' research department and its divisions providing commercial banking, underwriting, or other services to issuers of securities to prevent information from the latter influencing the former.

[26] Section 204A of the Investment Advisers Act, 15 U.S.C. § 8ob-4a ("Prevention of misuse of nonpublic information") provides,

> Every investment adviser subject to section 80b-4 of this title shall establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of such investment adviser's

which require broker-dealers and investment advisers to establish, maintain, and enforce written policies and procedures reasonably designed to preclude unlawful use of material nonpublic information.

Federal common law has also imposed fiduciary duties in federal securities cases. For example, because a brokerage relationship is a principal/agent relationship, some courts have found fiduciary duties that generally accompany such a relationship, including that "the broker must act in the customer's best interests and must refrain from self-dealing unless the customer consents after full disclosure." Hazen, "Are Existing Stock Broker Standards Sufficient?," 2010 Colum. Bus. L. Rev. at 736-37 & n.127. When a broker recommends securities or transactions, heightened duties have been found to apply that parallel those under the Investment Advisers Act that arose from judicial interpretation. *Id.* at 738.

Under the "shingle theory" of the common law, "by hanging up a shingle, a broker implicitly represents

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business, to prevent the misuse in violation of this chapter of the Securities Exchange Act of 1934 [15 U.S.C.A. § 78a et seq.], or the rules and regulations thereunder, of material nonpublic information by such investment adviser. The Commission, as it deems necessary or appropriate in the public interest or for the protection of investors, shall adopt rules or regulations to require specific policies or procedures reasonably designed to prevent misuse in violation of this chapter or the Securities Exchange Act of 1934 [15 U.S.C.A. § 78a et seq.] (or the rules or regulations thereunder) of material nonpublic information.

that he or she will conduct business in an equitable and professional manner." *Id.* at 749, 738-39.[27] As an extension of the common law doctrine of "holding out," it has been long and well established that "a securities broker occupies a special position of trust and confidence with regard to his or her customer when making a recommendation, and that any recommendation of a security carries with it an implicit representation that the broker has an adequate basis for the recommendation." *Id.* at 750-51, *citing Hanly v. SEC*, 415 F.2d 589, 506 (2d Cir. 1969). The "shingle theory" holds that the SEC and self-regulatory rules require broker-dealers to adhere to standards of fair and equitable principles of trade and that breach of the implied representation that a broker will deal fairly with the public [even at arm's length] will be actionable in a private action under the securities laws only if a plaintiff customer can show a causal relationship between the alleged breach and injury to the plaintiff; a breach of fiduciary duty,

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[27] The complaint, #81 at ¶ 44, asserts,

> Federal common law during the 1934 Class Period, and continuing today, placed a legal duty on UBS not to treat its retail clients unfairly. Under the "shingle" doctrine of broker conduct, when a broker-dealer hangs out its shingle it implicitly represents that it will deal fairly with the public and in accordance with the standards of the profession. Thus, the 1934 Act, SEC rules, SRO rules and regulations, as well as federal common law all required UBS either to notify its retail clients about the material information known by UBS relating to Enron securities purchased or acquired in BUS [sic] accounts or if UBS could not disclose this information for any reason, then to restrict trading and suspend research coverage of those securities.

alone, does not violate federal securities laws. *Id.* at 750, *citing Charles Hughes & Co. v. SEC*, 139 F.2d 434 (2d Cir. 1943), *cert. denied*, 321 U.S. 786 (1944). Nevertheless, the Court has been unable to find a single Texas case, no less a case in the Fifth Circuit, that applies the shingle theory, so presumably it has not been adopted in Texas.

"[A]ccountability for the implied representations that may arise out of a fiduciary duty will not violate the securities laws' antifraud provisions in the absence of showing that the defendant acted with the requisite scienter." Thomas Lee Hazen, "Fiduciary Obligations of Securities Brokers," 5 Law Sec. Reg. § 14:133 (updated March 2016), *citing In the Matter of Michael Flanagan, Ronald Kindschi, and Spectrum Administration, Inc.*, Release No. 160, Release No. ID-160, 71 SEC Docket 1415, 2000 WL 98210, *24 (S.E.C. Release No. 2000). The SEC also directs attention to the "basic principle" that by holding itself out as a broker-dealer, "a firm is representing that it will act in the customer's best interests." *Id.* & n.57 (and cases cited therein).

In addition, "[e]ven in the context of federal claims against a broker-dealer, the federal courts may look to state law to determine whether a fiduciary duty existed." Hazen, "Are Existing Stock Broker Standards Sufficient?," 2010 Colum. Bus. L. Rev. at 740, *citing Press v. Chem. Inv. Servs. Corp.*, 166 F.3d 529, 536 (2d Cir. 1999) (finding no fiduciary duty under New York common law for 10b-5 claims relating to mark-ups); *SEC v. Pasternak*, 561 F. Supp. 2d 459, 499 (D.N.J. 2008) ("To determine the existence of a fiduciary relationship

in federal securities fraud actions, district courts generally look to state law."). Hazen concludes that the "apparent majority of cases applying state common law" found that although "there is no blanket fiduciary relationship between a broker-dealer and a client as a matter of law," certain circumstances "can suffice to create a fiduciary duty," especially when the broker holds itself out as having investment expertise and the customer places faith, confidence, and trust in the broker. *Id.* at 741-46. Even where there is no discretionary account, the degree to which the broker cultivates a degree of trust and confidence in the customer affects the obligations that the broker has to the customer. *Id.* at 748. Among the duties that may be owed by a broker to a customer in a non-discretionary account[28] are "the duty to recommend a stock only after studying it, sufficiently to become informed as to its nature, price and financial prognosis," "the duty to inform the customer of the risks involved in purchasing or selling a particular security," "the duty to refrain from self-dealing or refusing to disclose any personal interest the broker may have in a particular recommended security," and "the duty not to misrepresent any fact material to the transaction." *Id.* at 748-49, *citing Leib v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 461 F. Supp. 951, 953 (E.D. Mich. 1978) (and cases cited therein).

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[28] A nondiscretionary account is one in which the customer must approve all transactions before they are effected. *Hand v. Dean Witter Reynolds, Inc.*, 889 S.W. 2d 483, 492 (Tex. App. – Houston [14th Dist.] 1994, writ denied). A discretionary account is one in which the broker makes the investment decisions and manages the account. *Id.*

The Texas Supreme Court has opined that "the term 'fiduciary' is derived from the civil law and contemplates fair dealing and good faith, rather than legal obligation, as the basis of the transaction. Further, that term includes those informal relations which exist whenever one party trusts and relies upon another, as well as technical fiduciary relations." *Texas Bank and Trust Co. v. Moore*, 595 S.W. 2d 502, 507 (1980), *citing Kinzbach Tool, Inc. v. Corbett-Wallace Corp.*, 138 Tex. 565, 160 S.W. 2d 509 (1942). The Supreme Court in *Texas Bank* quoted the Illinois Supreme Court in *Higgins v. Chicago Title & Trust Co.*, 312 Ill. 11, 18, 143 N.E. 482, 484 (1924),

> A fiduciary relation is not limited to cases of trustee and cestui que trust, guardian and ward, attorney and client, nor other recognized legal relations, but it exists in all cases in which influence has been acquired and abused, in which confidence has been reposed and betrayed, and the origin of the confidence is immaterial, and may be moral, social, or domestic or merely personal.

Moreover, "a fiduciary relationship exists when the parties are 'under a duty to act for or give advice for the benefit of another upon matters within the scope of the relation.' It exists where a special confidence is reposed in another who in equity and good conscience is bound to act in good faith and with due regard to the interests of the one reposing confidence.'" *Id.*, *quoting Lappas v. Barker*, 375 S.W. 2d 248, 251 (Ky. 1964). "The problem is one of equity and the circumstances out of

which a fiduciary relationship will be said to arise are not subject to hard and fast lines." *Id.* at 508.

In Texas, to state a claim for breach of fiduciary duty, the plaintiff must plead "(1) a fiduciary relationship between the plaintiff and defendants; (2) the defendant must have breached his fiduciary duty to the plaintiff; and (3) the defendant's breach must result in injury to the plaintiff or benefit to the defendant." *Billiteri v. Securities America, Inc.*, No. 09-CV-1568-F, 2010 WL 6785484, *9 (N.D. Tex. July 26, 2010), *citing Jones v. Blume*, 196 S.W. 3d 440, 447 (Tex. App. – Dallas 2006, pet. denied). Texas law recognizes two types of fiduciary duty, a formal relationship arising as a matter of law, and an informal relationship, where there is a close personal relationship of trust and confidence. *Navigant Consulting, Inc. v. Wilkinson*, 508 F.3d 277, 283 (5th Cir. 2007) and *Willis v. Donnelly*, 199 S.W. 3d 262, 277 (Tex. 2006). The latter arises from a "moral, social, domestic, or purely personal relationship of trust and confidence." *Meyer v. Cathey*, 167 S.W. 3d 327, 331 (Tex. 2005); *Thigpen v. Locke*, 363 S.W. 2d 247, 253 (Tex. 1962). "The existence of the fiduciary relationship is to be determined from the actualities of the relationship between the persons involved." Thigpen, 363 S.W. 2d at 253.

Under Texas law the formal relationship between a broker and its customer is one of principal and agent. *Rauscher Pierce Refsnes, Inc. v. Great Southwest Savings, F.A.*, 923 S.W. 2d 112, 115 (Tex. App. – Houston [14th Dist.] 1996), *citing Magnum Corp. v. Lehman Bros. Kuhn Loeb, Inc.*, 794 F.2d 198, 200 (5th Cir. 1986)

("The relationship between a securities broker and its customer is that of principal and agent. . . . The law imposes upon the broker a duty to disclose to the customer information that is material and relevant to the order."). The relationship between an agent and a principal is a fiduciary relationship under Texas law. *West v. Touchstone*, 620 S.W. 2d 687, 690 (Tex. App. – Dallas 1981), *citing Restatement (Second) of Agency* § 1 (1958). Nevertheless that fiduciary relationship is a narrow one, starting with and restricted to the scope of the agency. *Hand v. Dean Witter Reynolds, Inc.*, 889 S.W. 2d 483, 492 (Tex. App. – Houston [14th Dist.] 1994, writ denied). "In a non-discretionary account, the agency relationship begins when the customer places the order and ends when the broker executes it, because the broker's duties in this type of account, unlike those of an investment advisor or those of a manager of a discretionary account, are 'only to fulfill the mechanical, ministerial requirements of the purchase or sale of the security or future[s] contracts on the market. As a general proposition, a broker's duty in relation to a non-discretionary account is complete and his authority ceases, when the sale or purchase is made and the receipts therefrom accounted for." *Id.* 493-94, *citing Robinson v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 337 F. Supp. 107, 111 (N.D. Ala. 1971), *aff'd*, 453 F.2d 417 (5th Cir. 1972). In *Rauscher*, 923 S.W. 2d at 115 (citations omitted), the Fourteenth Court of Appeals explains,

> An agent is one who consents to act on behalf of, and subject to, the control of another, the

> principal, who has manifested consent that the agent shall so act. Agency is a consensual relationship, and the agency or broker/customer relationship does not come into existence until the order has been placed and the broker has consented to execute it. . . . If a broker, under his contract with his principal, is charged with no responsibility and is not obligated to exercise any discretion, but his duty consists of merely bringing the parties together so that between themselves, they may negotiate a sale, and the sale is made in that manner, the broker is considered a mere "middleman" and is not necessarily the "agent" of either party.

The *Restatement (Third) of Agency* § 1.01 (2006) defines "agency" as follows: "Agency is the fiduciary relationship that arises when one person (a 'principal') manifests assent to another person (an 'agent') that the agent shall act on the principal's behalf and subject to the principal's control, and the agent manifests assent or otherwise consents so to act." An innate duty of good faith and fair dealing, honest performance, and strict accountability is owed by an agent to his principal, and is required in every transaction on behalf of the principal. *Vogt v. Wamock*, 107 S.W. 3d 778, 782 (Tex. App. – El Paso 2003, pet. denied), *citing Sassen v. Tanglegrove Townhouse Condominium Ass'n*, 877 S.W. 2d 489, 492 (Tex. App. – Texarkana 2001, pet. denied). Moreover, under Texas law, to impose an informal fiduciary duty in a business transaction, "the special relationship of trust and confidence must exist *prior to* and *apart from* the agreement that formed the

basis of the suit." *Aubrey v. Barlin*, ___ F. Supp. 3d ___, No. 1:10-CV-00076-DAE, 2016 WL 393551, at *7 (W.D. Tex. Feb. 1, 2016), *citing Meyer v. Cathey*, 167 S.W. 3d 327, 331 (Tex. 1998). "[T]he fact that a business relationship has been cordial and of extended duration is not by itself evidence of a confidential relationship." *Floyd v. CIBC World Market, Inc.*, 426 B.R. 622, 651 (S.D. Tex. 2009), *quoting Lexington Ins. Co. v. North Am. Interpipe, Inc.*, Civ. A. No. H-08-3589, 2009 WL 1750523, at *3 (S.D. Tex. June 19, 2009). Whether a fiduciary duty exists is a question of law for the court. *Fuqua v. Taylor*, 683 S.W. 2d 735, 737 (Tex. App. – Dallas 1984, writ ref'd n.r.e.). The facts giving rise to a fiduciary duty, however, are to be determined by the fact finder. *Id.* at 737-38. Texas courts do not create a fiduciary relationship lightly. *Schlumberger Tech. Corp. v. Swanson*, 959 S.W. 2d 171, 177 (Tex. 1997); *Meyer*, 167 S.W. 3d at 331.

IV. Allegations of Plaintiffs' First Amended Class Action Complaint (#81)

The Court refers the parties to the governing complaint for its general summary of UBS's and Enron's background histories. #81 at p. 9, ¶ 33 through p. 23, ¶64.

In light of Enron's rapid and extensive expansion, Enron required substantial cash infusions and considered high credit ratings to be essential for its success and its ability to maintain adequate liquidity. #81 ¶ 55. To reach that goal, in the 1990's Enron began what

became a policy of engineering and manipulating its reported financial status by such stratagems as (1) significant, aggressive, and excessive use of off-balance sheet accounting, which is not reflected on the company's audited financial statements nor in the company's published leverage ratios; (2) beyond reasonable business levels, 50% percent [sic] or less owned joint ventures to reduce the appearance of balance sheet leverage; (3) equity swaps and equity forward contracts; and (4) adoption and expansion of mark to market accounting to hide losses, including the loss of billions of dollars by PW's retail customers. In the fall of 2001, Enron made a series of financial disclosures and restatements of its financial statements, ultimately leading to its bankruptcy filing. The Court has documented these events in numerous other *Newby* orders and refers the parties to them. Its focus in this action is on the relationship between Plaintiffs and UBS with respect to the 1934 Act.

Plaintiffs' complaint brings fraud claims against UBS based upon "nonrepresentational acts," for "engaging in a scheme or course of conduct violation [sic] Section 10(b) of the 1934 Act as implemented through subsections (a) and (c) of Rule 10-b." #81, ¶ 20. *Stoneridge's* rejection of scheme liability was not issued until two years after Plaintiffs filed the governing complaint in this case. Nevertheless Plaintiffs also allege that when UBS merged with PW at the beginning of the Class Period and acquired PW's retail brokerage business, through which it then generated profits from trades in Enron securities by PW's retail clients who constitute

the putative class in this action, UBS became a primary violator of Rule 10b-5 as to these investors. Accordingly, the Court focuses on the complaint's allegations to determine whether Plaintiffs have stated facts that could support a plausible claim of primary liability against UBS Defendants under the 1934 Act.

According to the governing complaint, UBS, one of the biggest banks in the world, is an integrated bank that offers traditional commercial loans, investment banking opportunities, and retail brokerage services. #81, ¶ 26. This integrated status resulted in a situation in which it had conflicting interests.[29] On December 11,

[29] Hazen, in *Multiservice Brokerage Firms' Information Barriers: The Chinese Wall or Fire Wall*, Treatise on the Law of Securities Regulation, 5 Law Sec. Reg. § 14:120, observes,

> A typical multiservice firm performs numerous functions. These functions typically include (1) investment banking (including underwriting and rendering advice to corporate issuers); (2) research (which services all of the firm's departments); (3) sales, which includes both retail sales and investment management; and (4) generally firms will have their own trading desk which operates in the over-the-counter markets and also performs arbitrage for their own account. . . . These varied functions give rise to conflicts of interest as the firm has a duty to guard the confidentiality of any non-public information it received from a corporate client. A major problem is that while the research department is supplying information to each of the other departments, the research department should be basing its evaluation on independent research, not from confidential information acquired from the firm's other departments. The antifraud provisions of the security laws require the firm to disclose all material nonpublic information it has or abstain from using it in trading or recommending the security in question. This "disclose

> or abstain" rule further obligates firms to refrain from executing or recommending transactions unless justified in light of all information known to the firm. In response to these conflicting duties, multiservice firms have established internal policies and procedures to restrict the flow of material nonpublic information from the department in which it originates. These procedures are colloquially referred to as "Chinese Walls" or "fire walls.

The SEC has long recommended the use of Chinese Walls (isolating trading side of firm from investment banking side), restricted lists ("prohibit[ing] recommendations to customers relating to, or solicitation of customers' orders to purchase or sell a particular security, and prohibit[ing] trading for the firm's own account in the security" or preventing "issuance of a research recommendation concerning a security"), and watch lists ("monitor[ing] trading activity to determine whether any leaks in the Chinese Wall have occurred"). *See, e.g.*, 43 S.E.C. 933, Release No. 34,8459 Release No. 8459, 1968 WL 86072 (S.E.C. Release No. 1968); *Slade v. Shearson Hammill & Co.*, 517 F. 2d 398, 403 (2d Cir. 1974); *S.E.C. v. First Boston*, 86 Civ. 3524 (S.D.N.Y. May 5, 1986); *Koppers Company, Inc. v. Am. Express Co.*, 689 F. Supp. 1413, 1416 (W.D. Pa. 1988). *See also* Rule 14e-3 of the Exchange Act, 17 C.F.R. § 240.14e-3 ("the SEC's formalization of the propriety of the information barrier as a way of avoiding liability for misuse of information"), adopted in 1980 to prohibit insider trading by those in possession of material nonpublic information in connection with tender offers. Rule 14e-3(b) "provides a safe harbor exclusion for firms adopting adequate information barriers if the firm is able to show that (1) the individual making the investment decision had no knowledge of the non-public material information and (2) the firm had implemented 'one or a combination of policies and procedures, reasonable under the circumstances' to ensure that those making investment decisions for the firm do not violate 14e-3.", *Multiservice Brokerage Firms' Information Barriers*, 5 Law Sec. Reg. § 14.120. In 1988 Congress passed the Insider Trading and Securities Fraud Enforcement Act, Pub. L. No. 100-704, 102 Stat. 4677 (1988), which *inter alia* amended section 15 of the Exchange Act to mandate that broker-dealers establish a system of internal, written procedures to prevent misuse of

1998, UBS executives (Ken Crews, the North American head of UBS's corporate finance department, and Jim Hunt, a Managing Director in the corporate finance department in UBS's Dallas, Texas Office) met with Enron's Andrew Fastow, with the meeting resulting in UBS's commitment as an investment bank to a relationship with Enron. #81 ¶ 49. The complaint, #81 ¶ 50, asserts what was well evidenced in numerous cases consolidated in *Newby,*

> It was well known within the banking industry that Enron rewarded banks, who provided credit capacity, by paying exorbitant amounts of money on investment banking fees. From 1998 forward, the Crews/Hunt team of executives at UBS's investment bank worked tirelessly to expand UBS's credit capacity for Enron so that UBS could participate in capturing a portion of the more than $100 million in non-credit related investment banking dollars Enron paid annually.

As noted above, in 2000 UBS merged with PW and acquired its brokerage business. The result was that

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nonpublic information by their employees. *Id. See generally also* Marc I. Steinberg and John Fletcher, *Compliance Programs for Insider Trading*, 47 SMU L. Rev. 1783 (July/August 1994).

At the same time, the S.E.C. has warned that if the multiple roles of these multiservice entities were prohibited, " 'the capital raising capability of the industry and its ability to serve the public would be significantly weakened.' As stated in the 1963 Report of the Special Study of the Securities Markets, the total elimination of potential conflicts in the securities industry 'is obviously quite out of the question.' " *Koppers Company*, 689 F. Supp. at 1415-16 (citations omitted) (letter from SEC to district court).

UBS "positioned itself between two classes of clients – its retail brokerage clients and its corporate client [Enron], such that UBS could not fulfill its legal obligations to both Plaintiffs and Enron concurrently." #81 ¶ 23.

"UBS and Enron's relationship was a mutually self-serving relationship that took precedence over and conflicted with the interests of UBS's retail customers." #81 ¶ 64. As Plaintiffs' broker and/or investment advisor, "UBS assumed concrete duties of disclosure as to these retail clients," and its silence regarding its material knowledge about Enron, garnered from its participation with Enron in financing devices to inflate the appearance of Enron's financial status and to conceal the substantial risk that Enron would be unable to service its debts and would suffer financial collapse, violated § 10(b). Nor did it disclose "the conflicts under which it operated its brokerage business." #81 ¶ 23. PW provided to Enron millions of retail investors to whom UBS could funnel Enron and Enron-related securities, effectively transferring Enron risk to the marketplace." #81 ¶ 64. "Ignorant of this undisclosed information, Plaintiffs acquired and/or held Enron debt securities which were either purchased through their UBS retail brokerage accounts, or which were owned by and sold to them by UBS, during the 1934 Act Class Period." #81 ¶ 24. This course of business operated as "a fraud upon the Plaintiffs and deceived them into believing the price at which they purchased or held their Enron securities was determined by the natural interplay of supply and demand." #81 ¶ 21.

In return, Enron provided PW with a "goldmine" in giving it exclusive administration of the all-Enron-employee stock option program, with the first opportunity to access Enron employee wealth and to generate retail fees and income for PW. More specifically the complaint recites that Rocky Val Emery ("Emery"), originally a financial adviser with PW, in 1993 learned from a client, Bill Roamy, an executive with Enron-owned EOG Resources, that Enron was creating an "all employee" stock option program and putting it out for bids from investment firms for a contract to administer the Stock Option Program, #81 ¶ 65. Seeking to make a lot of money, Emery put together a plan that impressed Enron, and PW was chosen in 1994 to be the exclusive Administrator of the Enron Employee Stock Option Plan,[30] with Emery given the primary responsibility for overseeing services to Enron and the Enron employees who opened accounts. Emery's group in PW was known as the Emery Group, which continued to

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[30] The complaint, #81 at ¶ 45, emphasizes,

> Another fact distinguishing Plaintiffs' claims from every other Enron-related claim is the exclusive relationship between UBS and Enron at the retail brokerage level. When UBS acquired PW, UBS also acquired all of the rights and obligations associated with PW's role as the exclusive administrator of Enron's stock option plans. By letter agreement dated October 19, 1998, PW contracted to assume exclusively the administrative function for Enron's stock option plans in exchange for the exclusive right to be the brokerage firm for all stock option exercises by Enron employees. Through this administrative role, UBS acquired an instant retail brokerage relationship with nearly every employee of Enron and its affiliate companies.

expand and provide services to PW for four years. In 1998 PW and Enron entered into a written, three-year contract which provided that when an Enron employee chose to exercise his stock options, he had to do so exclusively through PW. # 81 ¶¶ 45, 67-68. Once he exercised the stock options, he could either stay with PW or move his business to another firm. #81 ¶ 66. To get the retail business, PW did not charge Enron any fee to administer the Employee Stock Option program and thereby insure that it would be PW that would receive a stream of wealth from the arrangement.

With its goal being to retain wealth generated by Enron employees as they exercised their stock options, with its business model PW was gradually capturing and retaining about 60% of that wealth.[31] #81 ¶ 70. The way the arrangement worked, each time an Enron employee received a grant of stock options, PW would send that employee a packet of information regarding that stock grant, the exercise price, vesting dates, tax treatments, and other data about how to exercise those options and a new account form for the employee to apply; in addition it would inform the employee as a lure that PW charged a negligible six cents per share for them to exercise stock options. #81 ¶¶ 67-68. It emphasized to the employee that it provided free services to employees who opened PW accounts, including not

[31] The complaint at ¶ 69 states that by 1999 about 45,000-50,000 Enron employees participated in the Employee Stock Option Plans. Of these, 25% signed up immediately by filling out the forms provided in the introductory packed [sic]; 25% opened accounts when they exercised their stock options; and another 25% would slowly flow in over a few months.

only the Resource Management Account itself ($85 per year value), but also free stock option analysis and free financial plans worth hundreds of dollars. *Id.* When an employee wanted to exercise his stock options, he could call PW. If the employee was an insider or had options worth $500,000 or more, he was transferred to Emery; otherwise he was forwarded to one of the brokers in the Emery group on a rotating basis. When a PW broker answered the call, the broker would immediately offer the employee a free "financial plan," which would then automatically assign the employee account to that broker, and the employee became an advisory client of UBS under the Investment Advisers Act of 1940. #81 ¶ 71. One broker described this lucrative flow of money to PW "like shooting fish in a barrel." #81 ¶ 72.

Furthermore to keep this money flowing, PW made a secret "gentlemen's agreement" with Enron, unknown to PW's clients, that PW financial advisors would not recommend advising their retail customers to sell Enron stock, would advise them to exercise the Enron options, and would say nothing about Enron that might be perceived as negative. While PW advisors were permitted to advise their clients to diversify, those advisors had to speak with clients in code language, in which they intended "diversify" to mean "sell," in violation of the rules of the National Association of Securities Dealers, Inc. ("NASD"). PW did not reveal that communications between it and its clients were limited nor that there would be no full disclosure. The communications were intentionally misleading. Furthermore, whenever a PW client asked his financial advisor

about Enron, the financial advisor was required to give the client the managing director of the energy group at UBS Equity Research Ron Barone's "Strong Buy" rating on Enron's stock, despite the fact that Barone did not intend that rating to be a "buy" recommendation.[32] As an example of the deception, Plaintiff Alsina's broker urged him to buy Enron debt even though UBS's debt analyst had issued a "Sell" rating on the notes in question; instead of the "Sell" report, the broker sent Alsina a copy of Barone's "Strong Buy" report.

Because many of the high level executives at Enron had accounts at PW, when a "sudden firestorm of selling Enron stocks began within the ranks of upper level executives at Enron" in mid summer 2000, supported in the complaint by charts showing precise sales by specific, identified executives on pp. 30-32 in #81,[33] PW knew from these red flags that there was

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[32] Barone sent a Note with each rating to the PW brokers to indicate that it was a rating, not a recommendation, and he expected they would read and understand it and discuss with their client whether a stock was appropriate for his account holder, but this information was never revealed to PW clients. ¶ 76.

[33] Defendants argue that these pages of trades do not demonstrate knowledge by PW of Enron's deteriorating financial condition. Plaintiffs fail to indicate how many shares of Enron stock each insider retained and whether he sold most of his holdings or retained substantial exposure to Enron. Moreover allegations of sales of the company's stock by insiders, without more, are insufficient to plead knowledge of the corporation's declining financial state even by those insiders. *In re Advanta Corp. Sec. Litig.*, 180 F.3d 525, 540 (3d Cir. 1999) ("The Third Circuit has held that it "will not infer fraudulent intent from the mere fact that some officers sold stock.").

trouble at Enron. Within thirteen months twenty-one insiders sold more than half a billion dollars in Enron stock and generated hundreds of thousands of dollars in fees for PW, which did not warn its retail clients, but instead focused on keeping them invested in Enron securities. Enron would not permit any adverse comments about its stock.

Plaintiffs describe the experience of various PW employees who disclosed negative information about Enron's financial status and were disciplined for doing so.

Heritage Branch Manager Patrick Mendenhall, Heritage Branch Sales Manager Willie Finnigan, and Rocky Emery warned brokers in the branch on various occasions that if they communicated "any adverse information about Enron to Enron employees, they would be reprimanded, sanctioned, yanked from the Enron account, or even terminated." #81 ¶ 80. Whenever someone crossed that line, the brokers were told about the incident and the person was exposed. The brokers were given flat notice, "If you 'piss off' Enron, 'you're done.'" *Id.* During the summer of 2000, David Loftus, an employee in management, raised questions about Enron's

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The Court notes that in *Advanta Corp.*, *id.*, the Third Circuit went on to say "But if the stock sales were unusual in scope or timing, they may support an inference of scienter." *Citing Shaw v. Digital Equipment Corp.*, 82 F.3d 1194, 1224 (1st Cir. 1996) ("[A]llegations of 'insider trading in suspicious amounts or at suspicious times' may permit an inference that the trader – and by further inference, the company – possessed material nonpublic information at the time.").

business decisions to another passenger on a plane and was subsequently criticized for doing so and admonished not to say anything negative about Enron. In 2001 Craig Ellis, a consultant to help PW's sales force with various investments, at a sales meeting characterized the company as "'cook the books' Enron"; Ken Logsdon, one of Rocky Emery's right-hand men and an elite member of the Emery Group, told Patrick Mendenhall, who "silenced Ellis." *Id.* ¶ 81.

As an extreme example of Enron's repression of broker communications to clients, the complaint also goes into great detail about a PW broker, Chung Wu ("Wu"), whose client base was largely comprised of Enron employees and former employees who had opened their accounts when exercising their Enron stock options. In 1990 Wu warned one of his clients who was also an Enron employee that a report on Dow Jones news that Enron was considering selling all of its overseas assets might be a negative sign. A few days later Ken Logsdon told Wu not to convey unfavorable information about Enron to Enron employees as such conduct would "displease Enron management." ¶ 79. Watching Enron closely because he believed expectations for its stock were too optimistic, Wu realized that his clients were overly concentrated in Enron stock, and, as a financial advisor under a duty to do due diligence before taking a contrary position on Enron, Wu did his own research on the value of Enron stock. In 2001 Eu [sic] corresponded with his clients about Enron's "worsening condition"; all the while, PW was facilitating the higher Enron executives' mass liquidation of

their Enron stock. By August 20, 2001 Wu was convinced that Enron's financial state was disastrous and sent out a warning the next day to his investors, urging them to sell their Enron securities. One of the recipients who had an account with Wu was Jeff Donahue ("Donahue"), Enron's Senior Vice President of Corporate Development. Donahue forwarded the email to Kelly Boots, Tim Despain, and Hunt, who sent it on to Barone, and asked to have Wu fired. Other Enron employee/Wu clients also received his email and sent it on to higher managers, some like Mary Joyce ("Joyce"), Senior Vice President of Executive Compensation at Enron, who was one of those executives who had liquidated all of her Enron holdings. Joyce called Mendenhall, who "chewed out" Wu. The correspondence resulted in Wu's immediate termination from PW. PW then worked hard to cover the disclosure up, issued an apologetic retraction letter drafted by UBS's in-house counsel and signed by Mendenhall to those who had been sent the email, and reassured these clients. According to the complaint, not a single recipient of Wu's email followed Wu's advice. PW also purportedly immediately implemented a written policy requiring compliance with the secret "gentlemen's agreement" to prevent another such incident. PW management forbade its financial advisors from giving any advice to their retail clients regarding stock option issuers like Enron after August 21, 2001, and instead ordered them to refer the clients to UBS's current research report and rating on the stock. Not only did Barone's deceptive "Strong Buy" rating remain unchanged until November 28, 2001, when it was merely downgraded to

"Hold,"[34] but even "the Chief Executive Office [sic] of UBS's retail brokerage business, the man who was responsible for the corporate gag policy on UBS brokers," like the clients, misinterpreted it to mean he should buy Enron stock. #81 at p. 46, ¶ 112; p. 49, ¶ 115.

UBS, however, allegedly used its extensive information about Enron's financial status, gained in part through its active participation in Enron transactions and financial manipulations[35] in which UBS played significant parts to maximize its Enron-derived income at the expense of and in conflict with the interests of PW's retail customers and to limit its own exposure to Enron. The complaint describes in substantial detail numerous transactions in which UBS's active participation gave it material, nonpublic information about Enron's deteriorating financial condition that Plaintiffs contend UBS had a duty to disclose to its investor clients, who purchased, acquired, and/or held Enron securities through UBS. UBS's involvement with Enron in these Enron transactions, was designed to create a false appearance of Enron's financial position by concealing significant losses as well as to generate income and conceal secret loans to Enron, hidden by off-balance sheet and mark to market accounting, in other words, actions in which UBS aided

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[34] The complaint points out that by the first week of September UBS had begun its review to downgrade Enron's internal rating and determined by October that such a downgrade would take place.

[35] Including use of and 1999 and 2000 amendments of existing Equity Forward Contracts, the Osprey and Yosemite IV financial structures, and the Enron E-Next Generation loan.

and abetted Enron in its fraud on the investing public generally, now invalidated as primary violations of Exchange Act and Rule 10b-5 by *Central Bank* and *Stoneridge*. Because UBS's participation in these allegedly illegal acts does not constitute a primary violation of the 1934 Act as to Enron, the Court does not summarize them but refers the parties to the complaint's descriptions.

The complaint charges that UBS, as broker, broker-dealer, and/or investment advisor to its retail customers, had a duty to disclose to them this knowledge of Enron's fraud, which it gained from participating in these deals, but that it failed [sic] comply with that duty. Section 10(b) prohibits nondisclosure of material information in violation of a duty to disclose as a deceptive act. In failing to disclose material information to its retail clients, UBS therefore committed a primary violation of Rule 10b-5, according to Plaintiffs. Moreover UBS violated tax and accounting principles, industry standards, and its own internal policies of participation in complex or unusual transactions only if it had done its own due diligence, requiring an engagement letter establishing the responsibilities of the parties in the due diligence for the transaction, and taking part only if it understood the economic and tax consequences of the transaction.

In the five months starting June 2001, tellingly UBS eliminated almost all of its trading and credit exposure to Enron before Enron filed for bankruptcy on December 2, 2001, as detailed in #181 [sic] at pp. 77-83.

When that undisclosed material information was revealed to the public, the price of Enron securities plummeted, causing injury to Plaintiffs. The nondisclosure of material information in violation of a duty to disclose constitutes deception in securities fraud cases. *In re Enron Corp. Sec., Derivative & ERISA Litig.*, 235 F. Supp. 2d 549, 568 n.9 (S.D. Tex. 2002), *citing Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 470 (1977) (defining "deception" in § 10(b) as meaning the making of a material misrepresentation or the nondisclosure of material information in violation of a duty to disclose).

The complaint highlights UBS's purportedly fraudulent claims that its equity research aimed to benefit investing clients with objective, reasonable, and balanced research regarding companies, industries, and countries to determine value and to predict future movement of securities. Moreover it represented that it would not use its Equity Research to advance UBS's interests over those of its clients nor advance its analysts' own interests.

The complaint asserts that UBS's deceptive course of business is partly evidenced by its willingness to permit Ron Barone to continue his recommendations on Enron when UBS knew those positions were wrong and requiring Barone's "Strong Buy" Research Notes be given to every client who asked questions about Enron's financial condition. The pleading also complains that UBS "allowed Barone to accept, apparently blindly, Enron's upper management's nonsensical explanations and ignore known hard data. More importantly, UBS did not manage Barone, took advantage of Barone's

contrary rating to mitigate UBS's exposure to Enron, and used Barone to serve Enron, UBS's 'true' client, by enhancing its investment banking and retail revenues at the complete expense of Plaintiffs, to whom UBS owed concrete regulatory duties of disclosure." #181 [sic] at ¶ 208. Moreover, UBS hired and paid Barone, purportedly in 1999 "a $200,000.00 base salary, a guaranteed incentive bonus of at least $1,800,000.00, plus payment in 'customary fashion for investment banking revenue he generated,'" to lure in investing banking business but failed to disclose his activities and payments to the investing public, including Plaintiffs. #181 [sic] ¶ 215. In October 2000 under a new employment contract with UBS Barone's guaranteed incentive bonus was increased to at least $2,300,000.00, and the next year to at least $3,000,000.00.

In contrast to Barone, who reported on Enron equity and concentrated on movement in stock values, UBS Debt/Credit analyst Stewart Morel reported on Enron bonds and focused on whether a company has the ability to pay its debts by comparing the amount of cash generated relative to the amount of debt outstanding. #81 ¶¶ 219-22. Morel observed a persistent increase in Enron's debt from the third quarter of 2000 until Enron's demise. He was aware of Osprey and Marlin because they were public bond transactions, and he worried because Enron's worsening credit and potential loss of investment grade status could cause an acceleration of these obligations and increase the amount of short-term money Enron would require to pay its debt. Until November 2000, Morel listed Enron

debt as a "Buy"; after that he changed his rating to "Hold"; and in early 2001 he issued a "Sell" rating on Enron bonds based on his comparison of the relative strength of 80 companies. Unlike Barone's research notes, which were distributed by UBS advisors to retail clients by UBS's investment advisors providing them erroneous information, Morel's report and rating were not circulated to retail investors, a violation of UBS's policy to require a broker's recommendation to a client that is contrary to the analyst's position be provided to the client. Focusing on fraudulent practices relating to UBS analysts, the complaint asserts that the manner in which UBS actively employed Barone's research and concealed Morel's was part of the scheme and artifice to deceive its retail clients. While touting its research as objective, sound, fair, and reasonable, UBS did not disclose the truth to its clients, i.e., that in a scheme to assist UBS investment bankers, UBS analysts would communicate with top management of companies they covered, find investment banking opportunities, and alert UBS bankers, who would contact the Equity Research department and pressure it to initiate coverage of companies with which the bankers wanted to do business, and the Equity Research department would "capitulate." #181 [sic] at ¶¶ 210, 223-24. Analysts in turn were paid significant sums for their roles in investment banking activity. The complaint states that when an investment bank has negative knowledge that differs from its analysts' recommendations, the bank should stop the analysts' coverage on the stock, suspend the stock's marketing activity and the research coverage, and initiate an investigation. #181 [sic] at ¶ 226.

Instead UBS was hedging its risk by ridding itself of all Enron exposure and securing its future while mandating that its retail clients receive Barone's incorrect information and/or opinions about Enron's financial condition and stock, which supported the market's incorrect perception of the stock's value.

Finally as alleged violations of § 20A, the complaint states that in 2001 UBS, while in possession of all this material nonpublic information about Enron's financial status, bought 800,000 units of Enron Zero Coupon Notes, which UBS claimed to have "accumulated" as a market-maker to fill a "buy" order from Fidelity Investments, but it has not provided any evidence of a sale of the notes to Fidelity. In addition UBS AG bought 250 million units of the same notes, which it claims it holds as a "custodian" for UBS AG London's prime brokerage clients. Again, UBS has not submitted any evidence of the sale or transfer of the notes to UBS AG London. Moreover in July 2001 Enron amended its registration statement and changed the registration, listing Warburg and UBS as the owners, allowing Warburg and UBS AG to sell them on the U.S. market while also making them security holders and underwriters. The result was that UBS had another duty to disclose to the investing public that would foreseeably be purchasing the registered securities the material nonpublic information that UBS had about Enron. If it was unable to reveal this information, it had a duty to keep the securities and seek repayment from the issuer, Enron.

V. Defendants' Motion to Dismiss (#84)

Aside from the claim of scheme liability, which cannot survive under *Central Bank* and *Stoneridge*, Defendants's motion to dismiss argues that none of the five transactions, through which Plaintiffs claim Defendants injured them by creating "a false public appearance of Enron's financial position" (#81 ¶¶ 51-52), asserts a viable claim under § 10(b). First (#81, ¶¶ 116-66), Plaintiffs allege that Warburg participated in the following transactions that obscured Enron's reported financial condition: (1) underwriting a follow-on offering of Osprey notes; (2) underwriting a follow-on offering of "Yosemite IV" credit-linked notes; (3) extending credit to E-Next Generation, LLC; and (4) twice settling existing equity forward contracts by delivering stock to newly created special purpose [vehicles ("SPVs")]. Second (*id.* at ¶¶ 52, 116-17, 167-87), purportedly based on material, nonpublic information, which was not shared with UBS's retail clients, through trades Warburg lowered its own financial exposure to Enron late in 2001. Third (*id.* at ¶ 207), Warburg failed to stop UBS research analyst Ron Barone from rating Enron stock a "Strong Buy" even though other Warburg employees purportedly knew facts demonstrating that Barone's opinion was "wrong." Fourth (*id.* at ¶ 52), PW did not disclose to its customers material nonpublic information that Warburg bankers allegedly knew. Fifth (*id.* at ¶ 25), PW failed to disclose the conflicts of interest arising from its administration of Enron's employee stock option program. Thus UBS "failed to disclose knowledge it possessed . . . regarding the

manipulation of Enron's public financial appearance, some of which was accomplished through UBS, nor did UBS disclose the conflicts under which it operated its brokerage business." *Id.* at ¶ 23. Plaintiffs claim that by failing to disclose to Plaintiffs the material information known to UBS about Enron and by participating in financing devices and schemes to present an inflated picture of Enron's financial status, as well as concealing the risks that Enron would not be able to service its debt and would thus suffer financial collapse, UBS was a significant contributing cause of Enron's foreseeable economic disintegration.[36]

Furthermore, Defendants assert that Plaintiffs fail to plead the essential element of loss causation as to claims against them, i.e., that allegedly fraudulent brokerage practices at PaineWebber relating to the purchase or sales of Enron stock by PaineWebber's retail brokerage customers, were completely unrelated to Enron's financial-statement fraud and were uncovered only after Enron's stock price had dropped to zero.

Plaintiffs also pursue a claim for insider trading under Section 20A of the Exchange Act, 15 U.S.C. § 78t-1, based on UBS's purported sales of "UBS owned Enron

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[36] In their memorandum of law in response to UBS's motion, Giancarlo and Alsina state that their claims are based on "UBS's knowledge of Enron's financial manipulations from its extensive interaction, planning and participation with Enron in the five (5) identified fraudulent transactions, as well as its other investment banking activities with Enron, and not on the specific transactions as Securities Act Violations." #108 at p. 4, citing Complaint (#81) at ¶¶ 20-25, 116-76.

Debt" during the Class Period, while an unnamed UBS employee or entity allegedly had knowledge of material, nonpublic information about Enron. *Id.* at ¶¶ 25, 12. Defendants contend that there is no support for Plaintiffs' allegations that UBS AG and Warburg were "dumping" their holdings in Enron Zero Coupon Notes on PW clients or otherwise fraudulently selling those notes based on material, nonpublic information. The complaint does not identify what specific information about Enron was known to each officer selling his stock, no less demonstrate that the information was material and nonpublic or that the information motivated the trading decisions of any other UBS AG or Warburg employees.

In addition, Defendants maintain that, as in the *Newby* class action, Plaintiffs allege that PW did not disclose to its customer investors that Warburg defrauded them by providing "disguised loans" to Enron and by participating, though less so than in *Newby*, in off-balance-sheet financings. The Court previously found in *Newby* that similar claims against other banks, including Deutsche Bank and Barclays, merely amounted to aiding and abetting Enron's fraud and thus failed to state a viable primary § 10(b) violation against them. *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994) (holding that Section 10(b) does not permit a private cause of action for aiding and abetting); *Stoneridge Investment Partners LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 158 (2008) ("The § 10(b) implied private right of action does not extend to aiders and abettors. The conduct of a secondary

actor must satisfy each of the elements or preconditions [of a primary violation] for liability.").[37]

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[37] With respect to the Osprey transaction, Defendants point out that this Court has rejected similar, but much stronger claims against Deutsche Bank in *Newby*, e.g., for underwriting debt issued by the Osprey Trust or Enron, or for structuring Osprey to fund Whitewing while knowing that Enron sold assets to Whitewing at inflated values to falsify Enron's earnings, or for designing Osprey "to transfer billions of dollars of debt off Enron's balance sheet." *In re Enron*, 529 F. Supp. 2d 777 & n. 158; *Newby*, #4735 at 183 & n. 158. The Court rejected these stronger claims, concluding that the *Newby* Plaintiffs had failed to allege "specific facts demonstrating that Deutsche Bank established an innately illicit deceptive entity or device." *Id.* Thus Deutsche Bank "was at most merely aiding and abetting any subsequent deceptive use of these entities by Enron, the trustees, and Enron's auditor." *Id.* Unlike Deutsche Bank, Warburg did not "structure" Osprey, but served merely as one of several co-managers in a "follow-on offering of notes." Plaintiffs do not identify any "innately deceptive entities or devices" employed by Warburg in the Osprey offering nor allege they purchased any notes in any Osprey offering as they could not have done so since the Osprey notes were sold in private placements to qualified institutional buyers. *Id.* at 657. As for scienter, or intent to deceive, manipulate or defraud, or severe recklessness, Plaintiffs have simply alleged that two bankers at Warburg knew that Enron needed to complete the transaction for "year end balance sheet purposes," an allegation that does not give rise to a strong inference of scienter. Furthermore the allegations that Warburg engaged in such reckless due diligence that it did not recognize that "Enron used the Osprey structure to generate income by parking overvalued, non-performing assets in the structure" "are too general and clearly lack the kind of specific facts that would support a strong inference of scienter under the PSLRA." *Id.* at 775.

In the same vein, urge Defendants, Plaintiffs (1) fail to plead facts showing that any alleged trades in the Zero Coupon Notes were based on nonpublic information or were otherwise intended to defraud investors; (2) they fail to identify any connection between

research reports rating Enron stock as a "Strong Buy" and Enron's contemporaneous SEC filing listing UBS AG and Warburg as selling security-holders of these notes other than temporal proximity; and (3) they do not identify any specific nonpublic information possessed by any Warburg or UBS AG employee in August 2001. Plaintiffs' quotation from news clippings about a bond analyst fired from some other financial institution in August 2011 has no relation to the state of mind of anyone at Warburg or UBS AG. Thus they have failed to plead scienter.

Defendants define a "prepay" as "a 'circular' transaction among a bank, a 'conduit' entity, and Enron whereby the bank gave Enron cash up front, which Enron would repay to the 'conduit' entity with interest in the future, which finally would be delivered to the bank. These payments were made pursuant to commodity derivative transactions that did not transfer commodity price risk." #84-1 at p. 18 n. 14, *citing* Lomuscio Decl., Ex. 6 (Third Batson Report App. D) at 51-53. Regarding the Yosemite IV credit-linked notes offering and prepay transaction, this Court dismissed Deutsche Bank from *Newby* even though it underwrote credit-linked debt associated with Citibank's Yosemite transactions. It also dismissed Barclays, which had executed prepay transactions and which the Court held "are not *per se* illegal and Lead Plaintiff does not specify what about these purportedly made them improper. Alleging that what were 'loans' from Barclays were classified as cash flow from operations by Enron does not state an actionable claim against Barclays. Moreover, the inaccurate accounting of cash flow, debt, etc. that deceived investors is allegedly to have been done by Enron, its officers, and accountants." *In re Enron Corp.*, 439 F. Supp. 2d 692, 722 (S.D. Tex. 2006). In the instant case, Plaintiffs allege that Warburg defrauded them by underwriting credit linked notes in Yosemite IV and by knowing that "Enron used these Yosemite transactions to obtain what in economic substance were loans, despite their public characterization as funds flow from operations." The allegations do not state a primary violation because the inaccurate accounting was allegedly done by Enron, its officers, and its accountants. Nor do such conclusory allegations as that Warburg was aware of the Yosemite IV prepay raise a strong inference of scienter to plead a primary violation of Section 10(b) or Rule 10b-5, insist Defendants. The claims against Warburg bankers Kimberly Blue and Karsten Berlage (Complaint,

#81 at ¶ 158) are also vague. Nor does Plaintiffs' contention that if Warburg did not know that the prepay was a disguised loan to Enron, its due diligence must have been severely reckless, raise a strong inference of scienter.

The two equity forward contract "restructurings" in mid 1999 and early 2000 asserted by Plaintiffs occurred before the Class Period and at a time when PW was not affiliated with Warburg or UBS AG. Plaintiffs claim the restructures, which allegedly had all the traditional components of a loan, were "undocumented and undisclosed loans to Enron," designed to "support manufactured hedge transactions between Enron and two related party entities which Enron used improperly to manage its income," while Warburg knew that the undocumented loans were not accounted for as debt and "the manufactured hedge positions were used to preserve [mark-to-market] income by negating the possibility of loss in connection with [the assets hedged by the related parties]." Complaint, #81 at ¶ 122. Defendants insist they were not disguised loans, but modifications of the terms of pre-existing equity forward contracts between Warburg and Enron because Enron's stock had appreciated in value since the contracts were signed in the mid-1990's and UBS owed Enron value in excess of the value Enron owed UBS under the contracts. The restructurings would economically reset Warburg's obligation to Enron to zero and permit an Enron Special Purpose Entity ("SPE") to accept Enron stock and put in place new equity forward contracts reflecting the market price of Enron stock at that time. See #84-1 at pp. 23-25 for details of two restructurings. Even if they had been disguised loans to Enron, argue Defendants, the restructurings simply aided and abetted Enron in concealing its debt and falsely represent its financial state to possible investors. Defendants insist that no element of the restructurings was innately illicit or deceptive. If Warburg was involved in designing the LJM, Cayman, and Harrier SPEs, it would not be a primary violator of § 10(b) because it was not the creation of the SPEs that violated the statute, but Enron's use of the SPEs was a primary violation. The complaint admits that the transfers of Enron stock comprising the restructurings actually took place and the sales were not shams. *Newby*, 4874 at 62.

Defendants insist that Plaintiffs' allegations that Warburg and UBS AG provided routine banking work for Enron fail to state a claim for a primary violation

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As for the E-Next Generation LLC Credit facility, allegedly structured to keep the facility off Enron's balance sheet and to provide Enron with a $600 million loan, Defendants claim that Plaintiffs have failed to plead facts showing a primary violation of § 10(b). Defendants argue that "a bank making a loan to a borrower, even where it knows the borrower will commit securities fraud, is aiding and abetting." *Newby*, #4735 at 181. "Financings and investments are not sham transactions if there is no suggestion that the transactions were something other than what they purported to be." *Id.* The facility was not a sham, as several banks agreed to lend money for legitimate business purposes of obtaining turbines and other equipment and commencing development activity in Phase I and finding locations and constructing a number of gas-fired electric generating plants in Phase II. Complaint at ¶ 162. Any deceptiveness was in Enron and/or its auditors' description of the transactions on Enron's balance sheet. Moreover there is no showing of scienter because the documents on which Plaintiffs rely demonstrate that UBS expected that the E-Next facility would be properly disclosed. Richard J.L. Lomuscio Decl., #85-102, Ex. 12 (Lending Commitments Committee Proposal, UBS/LAM 020276-88), at UBS/LAM 20177, cited by Complaint in ¶ 165). Plaintiffs allege no facts suggesting that any Warburg or UBS AG employee knew that E-Next would be improperly kept off balance sheet by Enron. It is not the creation of an unqualified SPV, "but the use of it to obtain an unwarranted off-balance-sheet treatment" that is a primary violation of § 10(b). *Newby*, #4874 at 62.

In sum, the five transactions identified by Defendants cannot state a claim against Warburg or UBS AG under the 1934 because the misconduct charged at most was aiding and abetting frauds committed by Enron and because Plaintiffs fail to allege scienter for either. Nor have Plaintiffs shown a fiduciary relationship with a duty to disclose by Warburg and UBS AG with PW's brokerage customers. They have also failed to plead with particularity any material nonpublic information possessed by UBS.

of section 10(b).[38] *In re Enron Corp. Securities, Derivative & "ERISA" Litig.*, 529 F. Supp. 2d 644, 775 (S.D. Tex. 2006) (instrument # 4735 in *Newby*, 4:01-cv-3624),[39] subsequent determination, 236 F.R.D. 313 (S.D. Tex. July 5, 2006), *rev'd and remanded on other grounds*, 482 F.3d 372 (5th Cir. 2007), *cert. denied*, 552 U.S. 1170 (2008).

The complaint asserts that UBS owed Plaintiffs a duty of disclosure, arising from the 1934 Act and UBS's

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[38] Plaintiffs respond that this argument is meritless in the face of UBS's own investment bank standards, set out in written protocols, which specify self-prohibited tax, legal, accounting and regulatory-sensitive transactions that UBS should not have undertaken because of its subjective awareness of Enron misconduct. #108 at pp. 27-28, citing Complaint (#81) at ¶¶ 51, 148 ("due diligence must be undertaken for all transactions), 154, 155, 157. Declaration of David L. Augustus ("Augustus"), #109-123, "Attachment 23" (discovery responses indicating UBS's policies during Class Period).

[39] In that opinion, *id.*, this Court wrote,

> The proposed amended allegations that Deutsche Bank provided standard [banking] services, i.e., underwrote billions of dollars of Enron related securities, lent money to Enron, provided commercial banking and investment banking services to Enron, and earned a lot of money in fees from Enron, or that its employees who performed due diligence on Enron projects had an obligation to ensure that statements in offering memoranda are full, fair and accurate, in an effort to plead scheme liability under § 10(b), are too general and clearly lack the kind of specific facts that would support a strong inference of scienter under the PSLRA. Moreover, under the SEC's examples these acts constitute aiding and abetting and thus are not actionable under § 10(b) in this case pursuant to the hold of *Central Bank*.

retail brokerage relationship with Plaintiffs, which UBS breached by knowing of, and participating in, a false public characterization of Enron's financial state, that was in conflict with the interests of its retail clients. Defendants argue that although Warburg and PW are wholly owned subsidiaries of UBS AG and were separate and distinct entities during the Class Period, Plaintiffs fail to distinguish among the three and to plead with the required specificity who at which defendant had knowledge or wrongful intent; moreover when Plaintiffs do allege that an employee of one knew something about Enron, the allegations are impermissibly general and vague. *Southland*, 365 F.3d at 365. Warburg and UBS AG are distinct legal entities, separated from PW by "Chinese Walls." Moreover Warburg and UBS AG did not have a retail relationship with Plaintiffs; only PaineWebber had such a relationship with Plaintiffs. In *Newby* this Court's opinions detailed the legal duties owed by banks to Enron investors like Plaintiffs here. Because Plaintiffs here plead no facts that differentiate their claims against Warburg and UBS AG from those already dismissed against the banks in *Newby*, Plaintiffs' "banking" claims against Warburg and UBS must be dismissed for the same reasons the Court dismissed claims against banks in *Newby.*

In addition, Plaintiffs fail to allege with sufficient particularity facts giving rise to a strong inference that Warburg or UBS acted with scienter.

Nor under Section 20A did Warburg or UBS unlawfully trade on inside information when in a conflict

of interest they acted to eliminate their credit exposure to Enron by selling their Enron Zero Coupon notes into the marketplace while at the same time urging PW's retail clients to purchase and hold Enron equity securities without disclosing what they knew about Enron's primary violations of the 1934 Act. Nor does the complaint identify what material nonpublic information Warburg or UBS Ag possessed. Nor have Plaintiffs pleaded that their purchase of Enron Zero Coupon Notes were "contemporaneous" with any wrongful trades by Warburg or UBS AG. "[A]ny person who [wrongfully] purchas[es] or sell[s] a security while in possession of material, nonpublic information shall be liable . . . to any person who, contemporaneously . . . has purchased . . . or sold . . . securities of the same class." *Newby*, #1269 at 35. Plaintiffs purchased their Zero Coupon Notes on October 24, 2001, more than two months afer [sic] UBS AG and Warburg's status as "selling security holders" of those securities was disclosed. In addition, Plaintiffs' trades took place more than a week after Enron began "a series of financial disclosures and restatements of its financial statements pertaining in large part to certain related party transactions [that] triggered a chain of evens culminating in Enron's unprecedented bankruptcy filing 'starting with' an earnings release on October 16, 2001." Complaint ¶ 61. Moreover Plaintiffs fail to allege fact as to when and what Warburg and UBS AG allegedly "knew"; thus it is impossible to determine whether any information remained nonpublic or material after Enron's October 16 earnings release. Finally Defendants point out that Plaintiffs failed to assert

any Section 20A claims in their original complaint so any claims arising out of trades executed before August 15, 2001 (five years before they filed their Amended Complaint) are time-barred under 15 U.S.C. § 78t-1(b)(4).

Not only does the complaint fail to identify any trades by UBS AG or Warburg with particularity, with the possible exception of their purchases of Enron debt through PW and the alleged settlement of Warburg's equity forward contracts in late 2001, but because Enron voluntarily provided Warburg in September 2001 with the information on which Warburg and UBS AG purportedly traded to cause Warburg to extend the equity forward contracts, Warburg and UBS AG did not violate Rule 10b-5 under the misappropriation[40] or

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[40] The high court explained, 521 U.S. at 652,

> The "misappropriation theory" holds that a person commits fraud "in connection with" a securities transaction, and thereby violates § 10(b) and Rule 10b-5, when he misappropriates confidential information for securities trading purposes, in breach of a duty owed to the source of the information. . . . Under this theory, a fiduciary's undisclosed, self-serving use of a principal's information to purchase or sell securities, in breach of a duty of loyalty and confidentiality, defrauds the principal of the exclusive use of that information. In lieu of premising liability on a fiduciary relationship between company insider and purchaser or seller of the company's stock, the misappropriation theory premisses [sic] liability on a fiduciary-turned-trader's deception of those who entrusted him with access to confidential information.

This theory was formed "to protec[t] the integrity of the securities markets against abuses by 'outsiders' to a corporation who have

classical[41] theories of insider trading. *United States v. O'Hagan*, 521 U.S. 642, 650-54 (1997). Under the misappropriation theory full disclosure "forecloses liability" "[b]ecause the deception essential to the misappropriation theory involves feigning fidelity to the source of the nonpublic information, there is no 'deceptive device' and thus no § 10(b) violation." *Id.* at 655. Defendants argue that Warburg sold its hedge shares after Enron and Warburg settled the equity derivative forward contracts (Complaint at ¶ 185-86). Thus Warburg and UBS AG did not "deceive" Enron by selling stock to hedge transactions that Enron knew were terminated.

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access to confidential information that will affect th[e] corporations's security price when revealed, but who owe no fiduciary or other duty to that corporation's shareholders." *Id.* at 653.

[41] In *O'Hagan*, 521 U.S. at 651-52, the Supreme Court opined,

> Under the "traditional" or "classical" theory of insider trading liability, § 10(b) and Rule 10b-5 are violated when a corporate insider trades in securities of his corporation on the basis of material, nonpublic information. Trading on such information qualifies as a "deceptive device" under § 10(b) . . . because "a relationship of trust and confidence [exists] between the shareholder of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation." *Chiarella v. United States*, 445 U.S. 222, 228 . . . (1980). That relationship . . . gives rise to a duty to disclose [or abstain from trading] because of the necessity of preventing a corporate insider from . . . tak[ing] unfair advantage of . . . uninformed . . . stockholder.'" *Id.*, at 228-229. . . . The classical theory applies not only to officers, directors, and other permanent insiders of a corporation, but also to attorneys, accountants, and others who temporarily become fiduciaries of a corporation. *See Dirks v. SEC*, 463 U.S. 646 n.14 . . . (1983).

Nor did they improperly trade on this information under the classic theory of insider trading, which requires the breach of a duty of trust and confidence owed by a corporate insider to corporate shareholders when a corporate insider trades in the securities of his corporation based on material, nonpublic information. While "outsiders" like underwriters or consultants may become temporary fiduciaries, they may do so only by "enter[ing] into a special confidential relationship in the conduct of the business of the enterprise and [receiving] access to information solely for corporate purposes." *Dirk*, 463 U.S. at 655 & n.14. "For such a duty to be imposed, however, the corporation must expect the outsider to keep the disclosed nonpublic information confidential, and the relationship at least must imply such a duty." *Id.* n.14. Parties to a bilateral derivatives trade, in which one party's gain is the other's loss, do not have a special confidential relationship. Moreover even if Warburg did assume a duty to aid Enron to conduct the business of the enterprise by extending the equity forward contracts, Plaintiff fails to plead a basis for a continuation of that duty after termination of the equity forward contracts, after which Warburg sold its hedge shares. Complaint ¶ 186. Plaintiffs' aiding and abetting allegations do not state a claim under the 1934 Act.

In addition, Warburg and UBS AG's alleged failure to provide inside information about Enron's "true" financial condition, gleaned from their participation in various transactions with Enron, does not state a securities fraud claim, insist Defendants. Plaintiffs do

not allege that their agreement to administer Enron's employee stock option plan assisted Enron to conceal anything, nor that the stock option plan gave PW any knowledge of Enron's financial condition. Plaintiffs fail to show how the too vaguely described "gentlemen's agreement" between PW and Enron, which allegedly barred PW brokers from advising customers to sell Enron securities or from saying anything negative about Enron, defrauded its PW retail investing customers.

Plaintiffs fail to show that PW was a primary violator since it allegedly engaged in routine business transactions and failed to disclose another party's fraud in the absence of any duty to do so. Plaintiffs do not claim that PW engaged in any banking transaction used by Enron to conceal its actual financial state, nor do they allege that Enron used the employee stock option plan administered by PW to defraud investors. Even if they had, those allegations are insufficient to state a claim that PW was a primary violator. PW maintains that the accounts of its retail customers are nondiscretionary and that the investors retain the ability to make investment decisions, PW's duties as their broker are restricted to executing the investors' order. *Martinez Tapia v. Chase Manhattan Bank, N.A.*, 149 F.3d 404, 412 (5th Cir. 1998); *see also Hand v. Dean Witter Reynolds, Inc.*, 889 S. 2d 483, 492-93 & n.5 (Tex. App. – Houston [14th Dist.] 1994, writ denied) (under Texas law "the fiduciary duty owed to the customer [holding a nondiscretionary account] is very narrow – primarily not to make unauthorized trades."). The complaint does not assert that PW did not faithfully

execute its customers' orders. Plaintiffs' fraud claims are based on PW's silence when its customers purchased, acquired or held Enron securities or when UBS traded its securities to eliminate its credit exposure to Enron. These claims fail because PW did not owe to its customers a duty to disclose its business relationship with Enron or transactions in Enron securities, no less those of Warburg or UBS AG, the alleged sources of UBS's knowledge about Enron. *Romano v. Merrill Lynch, Pierce, Fenner & Smith*, 834 F.2d 523, 530 (5th Cir. 1987) (broker did not breach any duty to customer trading in silver futures by failing to disclose "its own activity in silver futures market"), *cert. denied*, 487 U.S. 1205 (1988).

Regarding the termination of Chung Wu by Defendants' branch manager Pat Mendenhall, Defendants comment that even if he was wrongfully fired solely to curry favor with Enron's human resources executives, Plaintiffs fail to provide a logical ink [sic] between that termination and their securities fraud claim that someone at PW knew something about Enron's true financial condition, but failed to disclose that information to PW customers despite having a duty to do so.

Defendants contend that a statement of opinion, such as an analyst's rating on a stock, is not "false" unless the rating is both objectively false and the public rating does not reflect the analyst's truly held private opinion. *See, e.g.*, *Greenberg v. Crossroads Sys.*, 364 F.3d 657, 670 (5th Cir. 2004) ("A statement of belief is only open to objection where the evidence shows that the

speaker did not in fact hold that belief and the statement made asserted something false or misleading about the subject matter."); *Joffee v. Lehman Bros., Inc.*, 410 F. Supp. 2d 187, 193-94 (S.D.N.Y. 2006) ("[U]nder the Supreme Court's decision in *Virginia Bankshares v. Sandberg*, 501 U.S. 1083, 1095-96 . . . (1991), statements of opinion are actionable only to the extent that they are not honestly held. Thus to plead that such statements of opinion actually caused Plaintiffs' damages, it is critical for Plaintiffs to allege that the 'relevant truth,' i.e., the alleged dishonesty of the opinions, is revealed to the market."), *aff'd*, 209 Fed. Appx. 80 (2d Cir. Dec. 19, 2006); *Podany v. Robertson Stephens, Inc.*, 350 F. Supp. 2d 375, 379-80 (S.D.N.Y. 2004) (to satisfy scienter requirement, a plaintiff must allege not merely that an analyst's opinions were wrong, misguided, or unjustly optimistic, but also that he deliberately misrepresented his true opinion of the value of securities in reports he issued). Defendants contend that although in general, falsity and scienter are different elements, as a statement may be both objectively false and, at the same time, believed in good faith by the speaker to be true; in an alleged false opinion case, however, the same analysis for determining whether an analyst's opinion is false applies to determining whether the analyst acted with scienter under the PSLRA, i.e., whether the statement was subjectively false. *Brown v. Credit Suisse First Boston, LLC (In re Credit Suisse First Boston Corp. Sec. Litig.*), 431 F.3d 36, 48-47 [sic] (1st Cir. 2005) (noting that in false opinion cases "the subjective aspect of the falsity

requirement[42] and the scienter requirement essentially merge"), *overruled on other grounds by Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308 (2007) (holding that the court must consider competing inferences and plaintiff must plead facts rendering the inference of scienter at least as likely as any plausible opposing inference in determining whether a complaint gives rise to a strong inference of scienter under the PSLRA)[43]; *In re Salomon Analyst Level 3 Litig.*, 350

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[42] The *Credit Suisse* panel states, "A plaintiff can challenge a statement of opinion by pleading facts sufficient to indicate that the speaker did not actually hold the opinion expressed (throughout this opinion we refer to such allegations as claims of 'subjective falsity')." 431 F.3d at 47.

[43] In *ACA Financial Guaranty Corp. v. Advest, Inc.*, 512 F.3d 46, 52 (1st Cir. 2008), the First Circuit discusses how *Tellabs* affected its earlier pleading standard in *Credit Suisse*:

> *Tellabs* has altered this circuit's prior standard, as set forth in [*Credit Suisse*], for determining the sufficiency of pleadings of scienter in securities fraud cases under Rule 12(b)(6). *Tellabs* affirms our case law that plaintiffs' inferences of scienter should be weighed against competing inferences of non-culpable behavior. *Tellabs* also affirms our rule that the complaint is considered as a whole rather than piecemeal. Finally, we hold that under the reasoning of *Tellabs*, the PSLRA does not alter the liberal amendment policy of Fed. R. Civ. P. 15.

Specifically the First Circuit identified two alterations effected by *Tellabs, id.* at 59:

> *Tellabs* has overruled one aspect of the rule this court stated in *Credit Suisse. Credit Suisse* held that where there were equally strong inferences for and against scienter, this resulted in a win for the defendant. This is no longer the law.

Now the court must "consider not only inferences urged by the plaintiff . . . but also competing inferences rationally drawn from

F. Supp. 477, 490 (S.D.N.Y. 2004). Defendants argue that by withdrawing their allegation that Ron Barone acted with scienter (Complaint, # 81 at ¶ 223),[44] Plaintiffs

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the facts alleged." *Id.*, *citing Tellabs*, 551 U.S. at 314. In addition, the panel in *ACA* pointed out, *id.*, *citing id.* at 310,

> *Tellabs* held that a "strong inference" of scienter "must be more than merely plausible or reasonable – it must be cogent and at least as compelling as any opposing inference of nonfraudulent intent." In other words, where there are equally strong inferences for and against scienter, *Tellabs* now awards the draw to the plaintiff.

[44] Paragraph 223 of the complaint states,

> This is not an "analyst" case. Plaintiffs do not sue UBS because Barone's research was wrong or because Morel's research was right. However, the manner in which UBS actively ***used*** Barone's Research notes, and hid Morel's, was part of a scheme and artifice to deceive its retail clients. As described above, UBS required that its investment advisors send copies of Barone's research to retail clients. In fact, post-8/21/01, UBS instituted a policy at the Heritage Branch, requiring its financial advisors to ***only*** provide Barone's research, couched as advice, to retail clients.

The Court concludes that although scheme liability is no longer a viable claim post-*Stoneridge*, the same allegation could support a breach of fiduciary duty claim. In addition to conceding that "[t]here is a relative dearth of authority speaking to the topic of whether a plaintiff has adequately pleaded subjective falsity in a false opinion case," the First Circuit in *Credit Suisse*, 431 F.3d at 48, expressly stated, "[W]hether [the falsity element] also entails an inquiry into objective falsity is a matter on which we take no view." The next paragraph of the complaint asserts,

> At the same time UBS represented to retail clients that its research was objective, fair, sound and founded upon a reasonable basis. UBS did not reveal to its retail clients that the "objective" research analyst received significant amounts of money as a result of investment banking activity, cozied up to corporate management

have abandoned their claim that Barone's research was "false" and that it acted as a fraud on the market.

Observing about the complaint's assertion at ¶ 207 of a strange scheme in which UBS participated in a "fraudulent course of business" by "allow[ing] Barone to continue coverage when he espoused positions that UBS ***knew*** were ***wrong***," not only does the Fifth Circuit reject group pleading, but to hold a defendant liable for failing to correct a false statement made by another defendant, the complaint must "identify which defendant(s) made an statement and who remained silent." *Financial Acquisition Partners LP v. Blackwell*, 440 F.3d 278, 388 (5th Cir. 2006). Plaintiffs fail to identify who in UBS knew that Barone's opinion was wrong but failed to stop him from publishing it, as well as to plead facts showing that Barone acted with scienter. Nor was allowing Barone to publish his research "an extreme departure from the standards of ordinary care" in light of Barone's thirty years' experience as a top-rated natural gas analyst (complaint at ¶ 206). "A securities fraud action may not rest on allegations that amount to second-guesses of defendants' opinions about the future value of issuers' stock – second-guesses

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> in order to determine whether there was investment banking business to be had, and even covered companies, at the request of the Bank to facilitate investment banking business. This knowledge would be absolutely material to any investor who was inundated with Barone's research opinions and would be necessary information for the investor to know as to make an informed investment decision.

made all too easy with the benefit of hindsight." *Podany*, 318 F. Supp. 2d at 154. Alleging that other analysts were more negative than Barone does not show that Barone acted with scienter. *R2 Investments LDC v. Phillips*, 401 F.3d 638, 644 (5th Cir. 2005) ("Knowledge of an omission does not itself necessarily raise a strong inference of scienter" where the alleged omission is a failure to disclose "a 'worst case' estimate" of the company's financial status.).

Moreover the complaint's allegation at ¶¶ 219-23 that UBS hid Stewart Morel's "Sell" recommendation is false; Morel's June 2001 research report recommended that investors "REDUCE exposure to Enron Corp. (ENE) senior paper and BUY ENE structured offerings." Lomuscio Dec. Ex. 19 (Morel June 21, 2001 research report, UBM/LAM 09845-96) at 10, cited at complaint ¶ 222). Morel's rating was his opinion that structured Enron debt paid a higher interest rate than ordinary Enron debt, not that Enron was not creditworthy.[45] Moreover, since Plaintiffs do not allege that Morel's opinion was not sincerely held, the fact that

[45] Plaintiffs disagree. #108 at p. 33. "Reduce" means "to make or become less"; an analyst's "reduce" rating means "sell." Morel downgraded Enron's bonds in his June 21, 2001 report. Moreover his recommendation that clients purchase structured paper was not a recommendation of Enron securities. Unlike bonds, "structured paper" is a secured investment and not Enron direct debt; if a company goes bankrupt, the holders of its structured paper may still retain the value of their investment, depending upon the asset that secures the paper. *Id.* Thus Plaintiffs maintain that Morel was telling his clients to dump Enron debt and protect themselves with secured investments which might provide them with some recovery in the event of bankruptcy.

Plaintiffs did not receive his research reports cannot be the basis of a fraud claim.

Plaintiffs also fail to allege that UBS's business practices, no matter how conflicted, caused Enron to collapse. They also failed to allege scienter regarding any alleged omissions involving Enron's fiancial state. The complaint does not plead any facts showing that any PW employees knew or were severely reckless in failing to discover adverse nonpublic information about Enron's financial condition. No facts are alleged giving rise to a strong inference that any PW personnel possessed nonpublic financial information about Enron or "questionable business practices" allegedly known to UBS. Nor are any facts asserted that show PW was extremely reckless in failing to obtain nonpublic information from Warburg employees. It is well established that retail brokers are barred from seeking material nonpublic information from another division of a financial institution to guide clients' investment choices and must by law establish "Chinese Wall" policies that restrict the flow of information within a multi-service institution and prevent their employees from improperly obtaining and trading on material nonpublic information. H.R. Rep. No. 98-355, at 11 (1984), *as reprinted in* 1983 U.S.C.A.A.N. 2274, 2284.

Loss causation must be pleaded as to each act or omission alleged to violate Rule 10b-5, as to each defendant. 15 U.S.C. § 78u-(b)(4); *Southland*, 365 F.3d at 365 ("the PSLRA requires the plaintiffs to 'distinguish among those they sue and enlighten *each defendant* as to his or her particular part in the alleged fraud.

[emphasis in original].'"). The complaint's allegations of loss causation fail to distinguish among PW, Warburg, and UBS AG. Plaintiffs fail to identify what actions or inactions, perpetrated or concealed by which defendant, caused their losses. Although reciting numerous wrongful business practices and omissions by PW, the complaint fails to plead causation as to any acts or omissions attributable to PW. No allegations are connected to Enron's ability to service its debt.

VII. Plaintiffs' Memorandum of Law in Response (#108)

The Court also does not address Plaintiffs' scheme liability aiding and abetting claims, which are no longer viable in the wake of *Central Bank* and *Stoneridge*.

Giancarlo and Alsina distinguish their claims from those in *Newby* by explaining that their claims arise from UBS's relationship to Plaintiffs as their securities broker, as a U.S. broker-dealer, and as a member of self-regulated securities organizations, that owed Enron investors an admitted duty[46] "to comply with the associated regulations establishing the practices and standards of care such broker-dealers are required to follow in connection with their retail customers." #108 at p. 5, citing Complaint (#81) at

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[46] *See* Declaration of David L. Augustus ("Augustus"), #109-123, "Attachment 1," UBS Form F-1 Registration Statement at 42-45; *id.* "Attachment 2," UBS Compliance Sales Practice Policy Manual at pp. 215-21.

¶¶ 43-44, 117-18, 226-27. UBS allegedly elevated Enron's business interests and UBS's own profits above its retail Enron investors' interests, in a conflict of interest in which UBS breached its brokerage duties to Plaintiffs. UBS also planned and participated with Enron in the five transactions identified in the complaint and other investment banking activities, which provided UBS with the knowledge that Enron's public financials were misstated (Complaint, #81 at ¶ 116-76). In violation of its duties to its retail investor clients, UBS (1) made undisclosed agreements with Enron not to fulfill UBS's duty to its retail investor customers, who were acquiring, purchasing and/or holding Enron securities (*id.* at ¶¶ 64-119); (2) secretly allowed Enron control over UBS's retail operations (*id.* at ¶¶ 74-75, 78-81, 92-115); (3) did not follow UBS's established protocols and procedures to protect its Enron-owning retail customers from the Enron fraud and accounting violations of which UBS was aware (*id.* at ¶¶ 223-2270 [sic]; and (4) failed to disclose its substantial conflict of interest when it was rapidly minimizing its own Enron default exposure into the public securities market while promoting the purchase of Enron securities to its retail customers (*id.* at ¶¶ 187-90). UBS's actions "violated [its] communications duties and created additional duties of care, full disclosure, and fair dealing, arising from UBS's own policies and industry regulations implementing the federal securities laws."[47] #108

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[47] *See GMS Group, LLC v. Benderson*, 326 F.3d 75, 81-82 (2d Cir. 2003) (Although there is no right of action for simply violating NASD rules, violation of NASD Rules 2860(19) and 2310, which govern the conduct of NASD members and address the suitability

at p. 6. Plaintiffs contend that the fact that UBS undertook these self-prohibited transactions, by itself, raises a strong inference of scienter (knowledge or extreme recklessness).

As for the structure of UBS, although Defendants attempt to distinguish among the three entities comprising UBS, Plaintiffs argue that the complaint (¶¶ 27, 32, 35-44, 94-95) asserts, and the Court must accept as true for purposes of the motion to dismiss, that UBS is an "integrated business enterprise," with Warburg and PW under UBS AG, as evidenced by its business operations during the Class Period. #108, pp. 7-16. *See also* Augustus, #109, Att. 1 (SEC Form F-1, filed with the SEC on Dec. 27, 2000), p. 11; *Id.*, "Attachment 3," p. 18, *The Making of UBS* (3d ed. March 2006); *Id.*, "Attachments 4-19."

Plaintiffs call meritless Defendants' claim that UBS only engaged in routine banking activities. The complaint identifies transactions which were structured to achieve certain tax, legal, accounting, and regulatory treatments as "window dressing" to alter Enron's financial appearance and which were prohibited by UBS's own investment bank protocols. The fact that it engaged in these self-prohibited transactions raises a strong inference of intent to deceive, manipulate or

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of securities recommendations, are relevant for purposes of § 10(b) unsuitability claims); *Hoxworth v. Blinder, Robinson & Co.*, 903 F.3d 186, 200 (3d Cir. 1990) (violations of NASD rules may be probative in demonstrating a course of conduct amounting to fraud); Declaration of Augustus, #109, "Attachment 2," at pp. 10, 12, 29-33, and 55-57.

defraud or severe recklessness. For example, the two restructurings of equity forward contracts between UBS and Enron did not result in "settlement" of the contracts, demonstrating that the restructuring was a disguised loan. The E-Next Generation Loan, also a disguised loan to Enron, not the E-Next SPE, was structured to achieve off-balance-sheet accounting treatment, avoid accounting regulations, and hide Enron's actual financial condition. UBS knew that the Yosemite prepay transactions, in which it insists UBS participated, were shams, structured so as not to transfer any commodity price risk.

Plaintiffs observe there are two kinds of claims under § 10(b) as implemented by and delineated in Rule 10b-5: (1) under Rule 10b-5(b), liability for materially false or misleading statements or omissions; and (2) under Rule 10b-5(a) and (c) liability for nonrepresentational acts ("employ[ing] any device, scheme or artifice to defraud" or "for engag[ing] in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person.").

Unlike in *Newby*, the complaint here is not centered on UBS's participation in how and by whom the manipulation of Enron's financial statements was effected. Instead the focus is on UBS's institutional knowledge that the financial statements were manipulated and on UBS's failure to disclose that knowledge to its retail clients purchasing Enron securities (complaint at ¶¶ 21-14 [sic], 42, 52, 116-18, 173, 188-90) or to act in accordance with its own established guidelines requiring it under the circumstances to suspend

analyst coverage and restrict stock sales (*id.* at ¶¶ 226-27), constituting the nonrepresentational act of which Plaintiffs complain. The particular nonrepresentational, deceptive act at issue is UBS's continuous failure to disclose to its retail clients, to whom UBS owes a duty to disclose, that Enron's financial appearance was unreliable and materially misleading because its books were "cooked," as UBS knew from its participation in transactions with Enron to create that false financial appearance.

As an on-point case, Plaintiffs cite to *Slade v. Shearson, Hamill & Co.*, No. 42 Civ. 4779, 1974 WL 376 (S.D.N.Y. Mar. 18, 1974) (certifying to the appellate court the question, "Is an investment banker/securities broker who receives adverse material nonpublic information about an investment banking client precluded from soliciting customers for that client's securities on the basis of public information which (because of its possession of inside information) it knows to be false or misleading?"), 517 F.2d 398, 403 (2d Cir. 1974) (finding certification for interlocutory appeal under 28 U.S.C. § 1292(b) was improvidently granted because of unresolved factual issues and "a complexity of interlocking [legal] questions"), *remanded*, *Odette v. Shearson Hammill & Co.*, 394 F. Supp. 946 (S.D.N.Y. 1975). The district court in *Slade* was seeking an answer to the question, whether once a multiservice investment banker that is also a broker-dealer received adverse nonpublic inside information on an investment banking client, in that case Tidal Marine International Corporation ("Tidal") stock, was it precluded from soliciting

purchases for that client's securities? Shearson, Hammill & Co. ("Shearson") moved for summary judgment on the ground that even if its corporate finance department knew the negative information about Tidal stock, the firm was barred from using that inside information to prevent the solicitation of purchases of the stock by its retail sales force. This Court notes that Judge Carter found the issue to be one of first impression, as well as one with "far-reaching ramifications for the structure of the securities industry." 1974 WL 376, at *2. The district court denied the motion for summary judgment, noting that an investment banker cannot reveal inside information; simultaneously it observed that because Shearson voluntarily entered into a fiduciary relationship with its investment banking customers, it could not recognize its duty to its investment bank clients while ignoring its duty to the stock investing retail clients, and it had to bear whatever commercial disadvantage each obligation entailed. Judge Carter opined, *id.*,

> To require organizations like defendant's to refrain from effecting transactions in securities of companies about which they have learned adverse inside information may be to render it exceedingly difficult for any such organization to function as an investment banker for a company and at the same time function as a brokerdealer in that company's securities. On the other hand, so long as such organizations continue to exercise a dual function, they incur dual (sometimes conflicting)

> fiduciary obligations which neither they nor this court can properly ignore.

During the litigation, in a brief the SEC urged to resolve the problem the use of a "Chinese Wall" that would bar transmission of inside information between Shearson's investment banking and broker-dealer departments, as well as the use of a "restricted list" of companies whose securities Shearson could not recommend because of an existing bank relationship. *Id.*

Plaintiffs do not discuss the significant aftermath of the case. The district court certified the question as a permissible interlocutory appeal under 28 U.S.C. § 1292(b) to the Second Circuit, which did not reach the merits of the issue, but instead found the interlocutory appeal improvidently granted because the factual basis had not been developed below and because there was "a complexity of interlocking questions," and remanded the case to the district court, where it settled, leaving the answer to the question unsettled. 517 F.2d 398, 403 (2d Cir. 1974). Thus the Second Circuit did not resolve the issue and the district court's opinion is of questionable precedential value. In subsequently approving the settlement, Judge Carter commented regarding the question whether a firm operating as both investment and securities broker may solicit customers or its client's securities in light of negative inside information, "[I]t is clear that the success of the *Shearson* subclass case at trial was not a foregone conclusion."

Slade v. Shearson, Hammill & Co., 79 F.R.D. 309, 313 (S.D.N.Y. 1978).[48]

Plaintiffs also point to the rules of the self-regulatory associations, the NASD, and the NYSE, as establishing obligatory standards under the 1934 Act for all broker-dealers. *See, e.g., Mihara v. Dean Witter & Co.*, 619 F.2d 814, 824 (9th Cir. 1980). While not providing a private right of legal action, violations of the NASD or the NYSE rules are relevant to demonstrating a course of conduct or deceptive act constituting fraud under § 10(b) and Rule 10b-5. *See, e.g., GMS Group, LLC v. Benderson*, 326 F.3d 75, 82 (2d Cir. 2003); *Hoxworth v. Blinder, Robinson & Co.*, 903 F.2d 186, 200 (3d Cir. 1990). SEC statutes and rules impose duties on those subject to them, including an affirmative duty of disclosure. Those duties run to both the SROs and to the broker-dealers' clients. A principle inherent in the relationship between a dealer and customer is that the customer will be dealt with fairly and in accordance with the standards of the profession. Plaintiffs contend that under the shingle theory, UBS had an affirmative duty to disclose its knowledge about Enron's financial manipulations at the time UBS's retail clients were purchasing Enron securities, and UBS's failure to disclose is a deceptive act under § 10(b) and Rule 10b-5.

Plaintiffs claim that UBS, as a single, fully integrated entity, violated the antifraud provisions of the

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[48] Defendants respond that the *Slade* case is more than thirty years old and has been superseded by legislative and regulatory action.

securities laws by failing to disclose to its retail investor clients its knowledge that Enron manipulated its public financial image in a materially misleading way, as evidenced by its own documents, and/or failed to act in accordance with its own established guidelines to suspend analyst coverage and restrict sales. Plaintiffs insist they have not indulged in impermissible group pleading, but instead have identified specific officers of UBS at the managing director level and above who had knowledge of this negative information. A core group of top executives at UBS, including Jim Hunt, Kimberly Blue, Michael Collins, Karsten Berlage, and Wendy Field, managed UBS's relationship with Enron, while an executive credit team composed of Bill Glass, Bob Verna, Roger Bieri, Chris Glockler, and Steve Landowne served as a major repository of information about Enron. Complaint at ¶¶ 49-50, 130, 139-42, 150, 157-58, 161, 163-65, 176-77. UBS understood the danger presented to it by Enron. It made Enron pay it $375 million in cash in September and October of 2001. Complaint at 182-86. In April 2001, Bill Glass, UBS Head of North American Credit, labeled Enron as one of three companies UBS did not like and transactions subsequently closed creating credit exposure to Enron had to be approved subject to the requirement that the exposure to Enron be sold or hedged. Complaint at ¶ 164. UBS also took positive steps to limit its credit exposure to Enron. As an example, in June and July 2001 Enron issued and sold approximately $163 million worth of UBS debt securities to a foreign investor, under which UBS's repayment obligations were linked to Enron's creditworthiness: if Enron filed for bankruptcy

or otherwise defaulted on its payment obligations to UBS, UBS could avoid repayment of its debt to this institutional investor. Complaint ¶ 174. Plaintiffs describe other efforts by UBS to reduce its exposure to Enron, including negotiating to prevent early termination of the equity forward contracts and in July 2001 selling Zero Coupon Convertible Senior Notes Due in 2012. #108 at pp. 49-52.

Situated in a conflict of interest between its retail brokerage clients and Enron, UBS learned of material nonpublic information about corporate malfeasance at Enron during a period when it had a regulatory duty of disclosure to its retail clients to whom UBS was recommending purchase of Enron securities. Under industry standards UBS should have suspended the stock market-making activities and analyst research coverage and authorized an investigation. Complaint at ¶ 226. Instead UBS actively peddled Barone's "Strong Buy" opinion while it knew that Enron's public financial statements were unreliable and materially misleading and while UBS moved to rid itself of all its Enron exposure, with the result that Enron's bankruptcy hardly affected UBS.

The "in connection with" language of § 10(b) and Rule 10b-5 is satisfied where a defendant's activities coincide with the purchase or sale of a security. *SEC v. Zandford*, 535 U.S. 813, 820, 825 (2002). Here the alleged violation is UBS's course of business concluding with UBS's failure to disclose its knowledge of the financial manipulations at Enron while Plaintiffs purchased Enron securities and/or UBS's failure to act in

accordance with its own established protocol to suspend analyst coverage and restrict sales.

Regarding the causation element of a § 10(b) claim, Plaintiffs assert that Defendants "attempt[] to mold the concept of loss causation into something it is not." #108 at p. 56. For loss causation, Plaintiffs must demonstrate that the loss complained of was foreseeable and that it was caused by the materialization of the concealed risk. *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 173 (2d Cir. 2005) ("Put another way, a misstatement or omission is the 'proximate cause' of an investment loss if the risk that caused the loss was within the zone of risk *concealed* by the misrepresentations and omissions alleged by a disappointed investor."), *cert. denied*, 546 U.S. 935 (2005). "Thus to establish loss causation, 'a plaintiff must allege . . . that the *subject* of the fraudulent statement or omission was the cause of the actual loss suffered, *i.e.*, that the misstatement or omission concealed something from the market that, when disclosed, negatively affected the value of the security. Otherwise, the loss in question was not foreseeable." *Id., citing Suez Equity Investors, LP v. Toronto-Dominion Bank*, 250 F.3d 87, 95 (2d Cir. 2001). Here UBS's omissions allegedly concealed the purported market manipulation that caused Plaintiffs' losses, a concealed risk which materialized, with losses of the type to be expected; without these omissions Plaintiffs would likely not have purchased the Enron securities or would have sold them before they imploded.[49] In

[49] Defendants reply that if a PW broker seeking a trade in Enron securities did not know any nonpublic information, he could

their memorandum of law supporting their response, Plaintiffs explained, #108 at p. 58,

> The risk concealed from Plaintiffs by UBS was the risk associated with the manipulation of Enron's public financial appearance. The market value of Enron securities began to diminish when questions were raised regarding Enron's financial status, its liquidity, disclosures were made regarding Enron's use of related parties and off-balance sheet financing

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not make a misrepresentation or omission about Enron's fiancial [sic] condition. Furthermore, if the broker could not disclose nonpublic information about Enron's financial information, he could not wrongfully omit to disclose "the risk that caused the loss." *Lentell*, 394 F.3d at 173. Any failure to suspend all trading in Enron securities while properly remaining silent regarding the reason for the suspension "does not speak to the relationship between fraud and the loss of the investment." *Id.* at 174. Rather this at most amounts to *transaction causation* – a showing that "but for the claimed . . . omissions, the plaintiff would not have entered into the detrimental securities transaction." *Id.* at 172. Transaction causation " 'is akin to reliance, and requires only an allegation that "but for the claimed misrepresentations or omissions, the plaintiff would not have entered into the detrimental securities transaction.' " *Id.*, *quoting Emergent Capital Inv. Mgmt., LLC v. Stonepath Group, Inc.*, 343 F.3d 189, 197 (2d Cir. 2003). In contrast, loss causation " 'is the causal link between the alleged misconduct and the economic harm ultimately suffered by the plaintiff.' " *Id., citing id.* Loss causation is described in the terms used for tort law's proximate cause, i.e., the damages caused by plaintiff must be a foreseeable consequence of a misrepresentation or material omission,' " or "a misstatement or omission is the 'proximate cause' of an investment loss if the risk that caused the loss was within the zone of risk *concealed* by the misrepresentations and omissions alleged by a disappointed investor." *Id.* at 172-73, *citing id.*, and *AUSA Life Ins. v. Ernst & Young*, 206 F.3d 202, 238 (2d Cir. 2000).

> vehicles, etc. Ultimately, all confidence in Enron was lost and bankruptcy ensued. UBS knew Enron's public financial appearance was materially misleading (Complaint ¶¶ 25, 188), knew Enron used related parties and off-balance sheet financing vehicles to achieve this appearance (Complaint ¶¶ 116-173), and, once the markets began to ask questions, UBS appreciated the risk of an Enron bankruptcy. (Complaint ¶¶ 174-187). This appreciation of the materiality of the non-public information possessed by UBS is evidenced by UBS's systematic shifting of its Enron exposure to the markets. (Complaint ¶¶ 174-187).

Plaintiffs also point out that reliance on unknown information may be presumed where the undisclosed information is material. *Affiliated Ute*, 406 U.S. at 153-54 ("Under the circumstance of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recover. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision."). Although UBS attempts to cloud the issue by erroneously insisting that Plaintiffs' claims are based on Barone's Research Notes, UBS's distribution of the Notes constitutes another reason why UBS had a duty of disclosure to the putative class or to otherwise act in accordance with its own procedures. Barone's Notes are an element of the course of business undertaken by UBS vis-a-vis the putative class, but Plaintiffs' claims do not depend on the existence of or the material in Barone's Research

Notes. Furthermore, given UBS's knowledge of undisclosed information about Enron, under its own protocol and procedures there should not have been any Barone Research Notes.

VIII. Defendants' Reply (#125)

Complaining about Plaintiffs' shifting but consistently vague theories of liability in the course of the litigation and insisting that Plaintiffs cannot cite a single case supporting their theory of securities fraud, Defendants identify key deficiencies in Plaintiffs' pleadings warranting their dismissal under Rule 12(b)(6).

First, Plaintiffs fail to allege scienter adequately with the requisite particularity: they do not distinguish among and give particular, individual notice to the Defendants as to the specific role each played in the fraud, but rely on impermissible group pleading and attempt to attribute knowledge allegedly held by a few individuals at Warburg or UBS AG to PaineWebber by melding these legally distinct corporations and calling them a "single business enterprise" with "institutional knowledge."[50] Indeed Plaintiffs fail to allege

[50] Because federal courts apply the law of the state of incorporation to determine whether to disregard the corporate form and pierce the corporate veil, Delaware law governs disregarding the corporate forms of PaineWebber and Warburg. Complaint at ¶¶ 7-8; *House v. 22 Tex. Servs.*, 60 F. Supp. 2d 602. 609 (S.D. Tex. 1999); #125 at p. 11 n.5. Under Delaware law, "Ownership [of a subsidiary, such as UBS AG's ownership of Warburg and PW] alone is not sufficient proof of domination or control." *Albert v. Alex. Brown Mgmt. Servs.*, C.A. No. 762, 2005 WL 2130607, at *10 (Del Ch. Aug. 26, 2005). "The legal entity of a corporation will not

even one instance when any PW employee learned Enron-related, material, nonpublic information from Warburg, UBS AG, Enron, or anyone else. Not only do Plaintiffs fail to allege the "who" of scienter, but they fail to allege precisely "what" nonpublic, Enron-related knowledge was known by any employee of any of the three named Defendants. Logically Plaintiffs cannot argue that any PW employee failed to disclose information about Enron's financial condition that Plaintiffs have not shown that PW employee possessed.

Second, Plaintiffs failed to plead loss causation. Plaintiffs have conceded that it was ***Enron's*** "manipulation of its financials" that caused the price of its stock to drop. #108 at p. 57. Plaintiffs contend that UBS caused Plaintiffs' losses because the losses were "foreseeable"

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be disturbed until sufficient reason appears." *Mason v. Network of Wilmington, Inc.*, C.A. No. 19434, 2005 WL 1653954, at *2 (Del. Ch. July 1, 2005). To pierce the corporate veil, "the corporation must be a sham and exist for no purpose other than as a vehicle for fraud." *Wallace ex rel. Cencom Cable Income Partners II, Inc. v. Wood*, 752 A.2d 1175, 1184 (Del. Ch. 1999). Defendants point out that the complaint "nowhere alleges, for example, that either PW or Warburg are undercapitalized or did not observe corporate formalities." #125 at p.11 n.5, *citing Mason*, 2005 WL 1653954, at *2-3. Plaintiffs have failed to show that the corporate forms of the three Defendants should be disregarded and they should be treated as a single entity. This Court agrees. *See, e.g.*, *Trevino v. Merscorp, Inc.*, 583 F. Supp. 2d 521 (D. Del. 2008); *In re Foxmeyer Corp.*, 290 B.R. 229 (D. Del. 2003). Moreover, even if the three UBS Defendants were "one commonly controlled business enterprise," Chinese Walls are required to separate the Warburg investment banking and the UBS AG commercial banking personnel who allegedly knew nonpublic things about Enron from PW retail brokers with whom Plaintiffs dealt.

if the market discovered Enron's fraud and that Defendants were somehow also a proximate cause because they were aware of Enron's numerous fraudulent acts. Nevertheless PW fails to allege that any of PW's alleged "brokerage practices" (e.g., the "gentlemen's agreement, the termination of Wu, or a violation of its "restricted list") were disclosed before Enron filed for bankruptcy, so the practices could not have caused Plaintiffs' losses. Warburg's or UBS AG's involvement with Enron constituted at most aiding and abetting Enron's financial-statement fraud, not primary violations of the securities laws. The five highlighted transactions were made fraudulent by Enron and its accountants, who used them to falsify Enron's financial statements, rather than by UBS or Warburg. Nowhere, however, do Plaintiffs plead specific details showing that the structure of an entity or a transaction that was created by the bank was inherently deceptive or used by the bank to deceive investors, nor have Plaintiffs pleaded details showing that the bank engaged in acts, practices or a course of business that operated as a fraud or deceit upon any person in connection with the purchase or sale of an Enron security to establish a primary violation of the 1934 Act by Defendants. Instead Plaintiffs conclusorily charge, without factual support, that Enron, its officers, and its accountants subsequently used the transactions to cook its books. There is no attempt to plead how any PW brokerage acts directly affected Enron securities' prices or that prices dropped because of any public disclosure of PW's business relationship with Enron.

Although Plaintiffs claim their loss was occasioned by PW's failure to comply with its own "restricted list" or policy guidelines (Complaint at ¶¶ 226-27), that allegation also fails. The governing complaint does not assert that PW's purported policy violations were a violation of Rule 10b-5 or that they caused Plaintiffs' losses. PW was not the sole source of information about Enron for those desiring to know, especially given Enron's SEC filings and public statements, nor was PW the only brokerage firm that could trade Enron securities for Plaintiffs. Plaintiffs' claims that had they known what Defendants knew, Plaintiffs would not have entered into the securities transactions at issue, pleads only transaction causation.[51] Not only did

[51] "Loss causation" is a causal connection between the misrepresentation or omission (the defendant's deceptive conduct) and the plaintiff's claimed economic loss. *Dura Pharmaceuticals*, 544 U.S. at 336, *citing* 15 U.S.C. § 78u-4(b)(4) ("In any private action arising under this chapter, the plaintiff shall have the burden of proving that the act or omission of the defendant alleged to violate this chapter caused the loss for which the plaintiff seeks to recover damages."); *Erica P. John Fund*, 563 U.S. at 807, 812-13 ("Loss causation . . . requires a plaintiff to show that a misrepresentation that affected the integrity of the market price also caused a subsequent economic loss" to the plaintiff; if other intervening factors, "such as changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events" occurred and "were responsible for the loss or part of it, a plaintiff would not be able to prove loss causation to that extent"). In sum, regarding loss causation, a plaintiff must plead "a facially 'plausible' causal relationship between the fraudulent statements or omissions and plaintiff's economic loss, including allegations of material misrepresentation or omission, followed by the leaking out of relevant or related truth about the fraud that caused a significant part of the depreciation of the stock and plaintiff's economic loss." *Lormand*, 565 F. 3d at 258.

Plaintiffs fail to allege that PW's policy guidelines were violations of Rule 10b-5 or caused Plaintiffs' losses, or that there was a causal relationship between PW's restricted list[52] and Plaintiff's losses, but Defendants maintain that Plaintiffs cannot show that Warburg or UBS AG committed a primary violation of the

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In cases relying on the fraud-on-the-market doctrine, the element of reliance is often called "transaction causation." *Dura Pharmaceuticals*, 544 U.S. at 341-42, *citing Basic, Inc.*, 485 U.S. at 248-49) ("nonconclusively presuming that the price of a publicly traded share reflects a material misrepresentation [or omission] and that plaintiffs have relied upon that as long as they would not have bought the share in its absence"). *Id.* at 812. Under the fraud-on-the-market theory that the market price of shares traded on well-developed markets reflects all publicly available information, including any material misrepresentations. "Because the market 'transmits information to an investor in the processed form of a market price,' " it is presumed that "an investor relies on public misstatements whenever he 'buys or sells stock at the prices set by the market.' " *Id.*

[52] Arguing that Plaintiffs mischaracterize PW's "restricted list" policy, Defendants contend that this "restricted list" allegation is undermined by the precise document on which Plaintiffs rely. PW's policy manual did not require PW to "suspend analyst coverage and restrict sales' whenever an employee in the global UBS network obtained material nonpublic information about; instead it stated that securities may be placed on the Legal Restricted List "for a number of reasons," none of which is found in the portion of the policy manual that Plaintiffs cite. Thus it does not support Plaintiffs' claim that Enron should have been placed on the restricted list. Furthermore Plaintiffs did not include the pages immediately following those on which they relied, a section entitled, "The Information Barrier," which reflects that PW's policy did not require that the brokerage activities be suspended whenever and investment banker obtained material, nonpublic information. *See* Supplemental Decl. of Richard J.L. Lomuscio, Ex. 1, 35-37.

securities laws by participating in a transaction that affected Enron's financial statements. Thus they cannot plead loss causation against Defendants simply by alleging the Enron's financial statements were misleading.[53]

Third, argue Defendants, even if Plaintiffs had properly pleaded that the entities had material nonpublic information about Enron, UBS Ag, Warburg and PW had an affirmative duty ***not*** to share that information because federal law required that PW be separated from Warburg and UBS AG by Chinese Walls, and, in addition, insider trading laws barred the three entities from sharing any material nonpublic information with Plaintiffs. Instead Plaintiffs pleaded that the Chinese Wall was observed by the UBS entities. The controlling complaint does not identify a single communication between Warburg or UBS AG and PW brokers in violation of the Chinese Wall. Even if such nonpublic material information had reached PW brokers, PW could not legally disclose it to Plaintiffs. Furthermore, the SEC has indicated that procedures developed to restrict the flow of nonpublic information within a financial institution are "a means to avoid securities law liability." *Koppers*, 689 F. Supp. at 1416 (letter from SEC to district court).

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[53] Even if it could, the Court would point out that under *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. at 142-43, Plaintiffs could not state a claim for misrepresentations against any of the Defendants because a Defendants [sic] would not be the ultimate authority over the content of Enron's financial statements.

Moreover, insist Defendants, Warburg and UBS AG had no fiduciary relationship with PW's customers, and Plaintiffs fail to plead facts showing that they had a fiduciary relationship even with PW, so their omission-based fraud theory fails. Defendants maintain that the SEC, federal common law, Defendants' compliance policies, and "industry standards" do ***not*** require a brokerage to automatically suspend operations or disclose nonpublic information whenever a banker learns material nonpublic information regarding an issuer. It is well established that a broker who advises his client to trade based on inside information violates Rule 10b-5. *See, e.g.*, *Dirks v. SEC*, 463 U.S. 64, 646-47 (1983); *U.S. v. Chestman*, 947 F.2d 551 (2d Cir. 1991) (broker's advice to client to buy stock was an unlawful "tip"); *SEC v. Sekhri*, No. 98 Civ. 2320, 2002 WL 31100823, at *17-18 (S.D. Tex. July 22, 2002) (broker ordered to disgorge both his own and his clients' profits from insider trades).

Each of Defendants' affirmative duties not to disclose material nonpublic information to Paine Webber or to Plaintiffs forecloses Plaintiffs' claims.

Given the complaint's conclusory allegations without specific factual support, Defendants insist that here Paine Webber owed no fiduciary duties to its retail customers beyond the faithful execution of their orders. *Tapai*, 149 F.3d at 412. Brokers owe no duty to disclose the brokerage firms' proprietary positions or trades of securities to their retail customers. *Romano*, 834 F.2d at 530. Thus the fraud claims should be dismissed.

In addition, Plaintiffs fail to state a § 20A claim based on Warburg's and UBS AG's alleged aftermarket sales of Enron Zero Coupon Notes on nonpublic information because the claims are asserted here by PW's retail customers. The duty not to engage in insider trading is owed to the source of that information, not to the counterparty to the trade, so Plaintiffs' relationship to PW is irrelevant. Simultaneously Plaintiffs charge that Defendants violated § 10(b) by failing to help Plaintiffs trade on the same information. Plaintiffs have not alleged and cannot allege facts showing that the trades in late October 2001 were "contemporaneous" with any purported trades by Warburg or UBS AG in Enron debt as required by 15 U.S.C. § 78t-1(a). Even more basic, Plaintiffs fail to plead with specificity what material nonpublic information was ever possessed by Warburg or UBS AG, and therefore Plaintiffs cannot show that the information was material and nonpublic when Plaintiffs purchased their Enron debt in late October 2001. (The complaint asserts that Warburg's and UBS AG's trades occurred in August 2001.). In *In re Enron Corp. Sec., Derivative & ERISA Litig.*, 258 F. Supp. 2d 576, 500-600 (S.D. Tex. 2003), this Court discussed the lack of agreement on what the word "contemporaneous" means, but generally the range required the insider and the investor/plaintiff to have traded anywhere from the same day, to less than a week, to within a month to "the entire period while relevant and nonpublic information remained undisclosed. *Id.* (citing cases). After examining various cases, the Court determined that "two or three days, certainly less than a week, constitute a reasonable

period to measure the contemporaneity of a defendant's and a plaintiff's trades under § 20A" and that "the plaintiff's trades must have taken place after the challenged insider trading transaction." *Id.* at 600. The Court applies the same measure here. Furthermore any such claim fails here because Plaintiffs have not alleged with factual support that any Paine Webber broker knew any nonpublic information regarding Enron. To recover under § 20A a plaintiff must at minimum demonstrate that the defendant was "aware" of the material nonpublic information upon which the defendant purportedly traded. 17 C.F.R. § 240.10b-5-1(b).

IX. Court's Decision

The Court agrees with Defendants that the alleged actions of the three UBS entities in relation to Enron, as participants in a scheme to artificially make Enron falsely appear financially sound and creditworthy, constituted aiding and abetting, and did not qualify as primary violations of § 10 and Rule 10b-5. Therefore § 10b and Rule 10b-5 do not reach their actions, and Plaintiffs fail to state a claim or impose liability on UBS separately or as an integrated entity under the statute and Rule 10b-5 relating to their vaguely and conclusorily alleged joint involvement with Enron. *Central Bank*, 511 U.S. at 177-78; *Stoneridge*, 552 U.S. at 58. Moreover, the relationship of the three UBS Defendants to Enron in that scheme was not a fiduciary relationship with a duty to disclose, but a commercial business relationship between a public company and an underwriter/lender bank.

In contrast, the § 10(b) claims based on material omissions which Plaintiffs bring, as PW's retail clients/investors in the Enron Stock Option Program against PW in its capacity as their broker/broker-dealer, arise in a fiduciary relationship, in which PW has a duty to disclose that is defined and limited by the nature and scope of that relationship. PW's self-interested business involvement with Enron, which conflicted with the interests of its retail investor customers, only becomes relevant if PW's duty to disclose is sufficiently extensive to require it to act only in the investors' self interest and refrain from self-dealing unless the customers consent to PW's conflicting roles after full disclosure.

It is therefore significant that PW's relationship with the clients in the Enron Stock Option Program was established at least in part in the context of, and by, a contract between Enron and PW, in which presumably the parties to that contract were free to define and limit the scope of duties owed to suit their needs and intentions, either implicitly or explicitly. Viewed from this perspective, the fiduciary duty of PW to those exercising their Enron stock option grants is, to some extent, a matter of contractual interpretation.[54] Once the Enron stock option participants made the decision to exercise their stock options, the contract between

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[54] *See, e.g.*, Donald C. Langevoort, *Brokers as Fiduciaries*, 71 U. Pitt. L. Rev. 439, 442-43 (Spring 2010) ("[B]ecause most fiduciary relationships arise within contractual ones[,] . . . the precise content of a fiduciary's responsibility is just a form of contract interpretation.").

Enron and PW gave PW exclusive control of the process of exercising those stock options. Once the options were exercised, however, the investors had free choice whether to stay with PW and open an account or move their stock to another firm, regardless of what lures PW extended. Furthermore, if they opened accounts with PW, those accounts were nondiscretionary. There are no allegations or descriptions in the complaint of incidents in which PW acted contrary to an investor's instructions in selling or purchasing securities or that PW effected securities transactions without the authorization of the account holder.

Moreover the allegations reflect that PW acted only as an order taker and order executor, and thus it had a very limited duty to the investor clients compared with that of a broker managing a discretionary account. Under federal law, "where the investor controls a nondiscretionary account and retains the ability to make investment decisions, the scope of any duties owed by the broker will generally be confined to executing the investor's order." *Martinez Tapia*, 149 F.3d at 412, *citing Romano*, 834 F.2d at 530, and *Hill v. Bache Halsey Stuart Shields, Inc.*, 790 F.2d 817, 825 (10th Cir. 1986) ("fiduciary duty in the context of a brokerage relationship is only an added degree of responsibility to carry out pre-existing, agreed-upon tasks properly"), and *Limbaugh v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 732 F.2d 859, 862 (11th Cir. 1984) ("duty owed by the broker was simply to execute the order."). See also *Chiarella*, 445 U.S. at 230 ("[N]o duty of disclosure would exist if the bank merely acted as a

transfer agent."). Absent a specific duty to disclose material, nonpublic information, silence is not misleading and not a basis for Rule 10b-5 liability. *Basic, Inc.*, 485 U.S. at 239 n.17. Given the allegations of the complaint, such is the case here.

As noted, under Texas law, the broker/investor relationship is one of agent/principal, but "[i]f a broker, under his contract with his principal, is charged with no responsibility and is not obligated to exercise any discretion, but his duty consists of merely bringing the parties together so that between themselves, they may negotiate a sale, and the sale is made in that manner, the broker is considered a mere 'middleman' and is not necessarily the 'agent' of either party." *Rauscher*, 923 S.W. 2d at 115. Moreover, generally even in a simple

> non-discretionary account, the agency relationship begins when the customer places the order and ends when the broker executes it because the broker's duty in this type of account, unlike those of an investment advisor or those of a manager of a discretionary account, are "only to fulfill the mechanical, ministerial requirements of the purchase or sale of the security. . . ." As a general proposition, a broker's duty in relation to a nondiscretionary account is complete, and his authority ceases, when the sale or purchase is made and the receipts therefrom accounted for. Thus, each new order is a new request that the proposed agent consents to act for the principal. There is no on-going agency relationship as there

> would be with a financial advisor or manager of a discretionary account.

Hand, 889 S.W. 2d at 493-94. Moreover, under Texas law, as indicated *supra*, to impose an informal fiduciary duty in a business transaction, "the special relationship of trust and confidence must exist *prior to* and *apart from* the agreement that formed the basis of the suit." *Aubrey*, 2016 WL 393551, at *7, *citing Meyer v. Cathey*, 167 S.W. 3d at 331 (Tex. 1998). Such is not the case with PW and its investor clients. "[T]he fact that a business relationship has been cordial and of extended duration is not by itself evidence of a confidential relationship." *Floyd*, 426 B.R. at 651, *quoting Lexington Ins. Co. v. North Am. Interpipe, Inc.*, 2009 WL 1750523, at *3.

Moreover, Plaintiffs fail to allege scienter adequately, to state with particularity for each alleged material omission facts giving rise to a strong inference that PW acted with the required state of mind. They fail to identify specific brokers and allege facts that demonstrate each had an intent to deceive, manipulate or defraud or acted with severe recklessness.

Regarding Plaintiffs' theory that the three UBS Defendants form a single enterprise which is liable to them for all their alleged violations of the Securities Exchange Act, when an entity's corporate form is at issue, courts standardly hold that the law of the state of incorporation of that entity applies to determine whether its corporate form should be disregarded, whether to pierce the corporate veil. *Ace American Ins.*

Co. v. Huntsman Corp., 255 F.R.D. 179, 195 (S.D. Tex.) (and cases cited therein). PW and Warburg were incorporated in Delaware; thus the Court applies Delaware's law to determine if their corporate forms should be disregarded and UBS should be treated as a single enterprise Defendant.

To pierce the corporate veil under an alter ego theory, Delaware law requires a showing of fraud or similar injustice. *Id.* at 196 (and cases cited therein). Thus under Delaware law, "[t]he corporate fiction may be disregarded to prevent fraud, and a wholly-owned subsidiary may sometimes be treated as an instrumentality of the parent. *Buechner v. Farbenfabriken Bayer Aktiengesellschaft*, 38 Del. Ch. 490, 493 (Del Ch. 1959). "In the absence of fraud, the separate entity of a corporation is to be recognized. This principle has been enunciated by all the courts of the state." *Stauffer v. Standard Brands, Inc.*, 40 Del. Ch. 202, 178 A.2d 311 (1962).

The Court observes that Plaintiffs have failed to plead their single, fully integrated entity theory of the three UBS Defendants to satisfy requirements under Delaware law by pleading facts demonstrating that the three UBS entities' corporate status should be disregarded. In the context of parent/subsidiary relationships, treating separate legal entities of a corporation as alter egos is closely related to disregarding a corporation's separate legal identity by "piercing the corporate veil." *Harper v. Delaware Valley Broadcasters, Inc.*, 743 F. Supp. 1076, 1085 (D. Del. 1988). In *ASARCO LLC v. Americas Min. Corp.*, No. Civ. 1:07 CV 00018,

2009 WL 2168778, t *6-7 (S.D. Tex. July 20, 2009), the Honorable Andrew Hanen opined,

> Under Delaware law, a court of equity may pierce the corporate veil on an alter-ego theory where (1) the companies operated as a single economic unit; and (2) an overall element of injustice or unfairness is present. *In re Foxmeyer Corp.*, 290 B.R. 229, 235 (Bankr. D. Del. 2003). "Simply phrased, the standard may be restated as: whether [the two entities] operated as a single economic entity such that it would be inequitable for the Court to uphold a legal distinction between them." *Harper v. Del. Valley Broadcasters, Inc.*, 743 F. Supp. 1076, 1085 (D. De. 1990).

In accord, *Fletcher v. Atex, Inc.*, 68 F.3d 1451, 1457 (2d Cir. 1995). In *Skouras v. Admiralty Enterprises, Inc.*, 386 A.2d 674, 681 (Del. Ch. 1978), *citing Buechner v. Farbenfabriken Bayer Aktiengesellschaft*, 154 A.2d 684 (Del. Supr. 1959), and *State ex rel. Rogers v. Sherman Oil Co.*, 117 A. 122 (Del. Supr. 1922), the Delaware Court of Chancery emphasized that mere control and even total ownership of one corporation by another is not sufficient to warrant the disregard of a separate corporate entity under Delaware law: [a]bsent a showing of a fraud or that a subsidiary is in fact the mere alter ego of the parent, a common central management alone is not a proper basis for disregarding separate corporate existence." *In accord, eCommerce Industries, Inc. v. MWA Intelligence, Inc.*, C.A. No. 7471-VCP, 2013 WL 5621678, at *27 (Del. Ch. Oct. 4, 2013). In *Skouras*, the court found that the parent corporation's "subsidiary

corporations were so organized and controlled and their affairs are so conducted as to make them adjuncts or instrumentalities of the defendant company," and it listed factors that might be considered in determining whether a parent corporation is liable for the wrongdoing of a subsidiary because they operated as a single economic unit, including whether

> all of the subsidiary corporations were engaged in the same general business as the parent; the parent owned all of the shares . . . of the subsidiaries; all the members of the boards of directors of . . . the subsidiary corporations were also directors of defendant, and a majority of members of the boards of the remaining . . . subsidiaries were directors of defendant. Furthermore, the books of the subsidiaries were not in defendant's possession, custody, or control. Upon determining that the separate subsidiary corporations had been formed for fraudulent purposes, this court granted plaintiffs' demand for inspection of the books of defendant's subsidiaries. . . .

Id. at 681.

Plaintiffs in the instant suit have failed to allege any facts supporting their single enterprise theory that UBS Defendants must be treated as a single entity to avoid fraud or miscarriage of justice. *See, e.g., Pauley Petroleum, Inc. v. Cont'l Oil Co.*, 43 Del. Ch. 516, 521, 239 A.2d 629, 633 (Del. 1968) (holding that corporate entities may be disregarded and "the parent be regarded in law and fact as the sole party in a particular transaction" "only in the interest of justice, when such

matters as fraud, contravention of law or contract, public wrong, or where equitable consideration among members of the corporation require it, are involved."). As noted, Plaintiffs here fail to state a fraud claim under § 10(b) against UBS AG and/or its subsidiary, Warburg. The only possible § 10(b) primary violator is PW, so there is no reason to disregard its corporate form.

Moreover, as pointed out by Defendants, not only are there no factual allegations showing a direct relationship of Plaintiffs to Warburg and UBS AG, which were not parties to the contract between Enron and PW and which therefore did not serve as brokers for PW's retail investor clients nor in any fiduciary capacity of trust and confidence which would require them to disclose any nonpublic information they may have discovered about fraud by Enron. Even if Plaintiffs had alleged such facts, Plaintiffs fail to satisfy the PSLRA's heightened pleading standards by specifying exactly what nonpublic, material information they knew about Enron, who discovered it, when, how, and under what circumstances and why it was fraudulent. Under the facts that Plaintiffs did plead, Warburg and UBS AG had no duty to disclose any material omissions to Plaintiffs, and Plaintiffs have not and cannot state a claim against them under § 10(b) and Rule 10b-5.

Nor have Plaintiffs pleaded facts showing that their broker PW's alleged fraudulent brokerage practices caused Plaintiffs' loss. These practices in no way related to Enron's fraud, i.e., "cooking its books," which, when revealed, caused the price of its securities to plummet and Plaintiffs to suffer economic loss.

Furthermore, as noted, the Fifth Circuit has deliberately chosen not to decide whether rules for brokers established by national exchanges and SROS, such as the NASD "suitability" rule or the NYSE "know your customer rule," provide a private cause of action for individual investors, but found they may be used as evidence of industry standards and practices. *Miley*, 637 F.2d at 333. Because this is a material omissions case and because the Court has concluded that Plaintiffs have not pleaded facts establishing a fiduciary relationship with PW with a duty to disclose, the Court find [sic] no reason to reach those rules and regulations here.

Finally, the Court concurs with Defendants that Plaintiffs have failed to state a claim under § 20A, 15 U.S.C. § 78t-1(a) (1) Plaintiffs lack standing to assert such a claim against UBS Defendants because the duty not to engage in insider trading is owed to the source of the nonpublic information, not to the counterparty to the trade; (2) Plaintiffs have not alleged and cannot allege facts showing that they have standing because their securities trades in late October 2001 were "contemporaneous" with (within a week of) those of Warburg or UBS AG in August 2001; and (3) Plaintiffs fail to plead with factual specificity what material nonpublic information was known to any PW broker (or employee of Warburg or UBS AG) when Plaintiffs sold their Enron stock or when they purchased their Enron debt in late October 2001 or that this information motivated the trading decisions of UBS.

Accordingly, for the reasons stated above, the Court

ORDERS that Defendants' motion to dismiss pursuant to Federal Rules of Civil Procedure 12(b)(6) and 9(b) and the PSLRA is GRANTED. The Court further

ORDERS that Lead Plaintiffs' motion for class certification (#124) and Plaintiffs' opposed joint motion for amended scheduling order, for additional briefing and for a ruling (instrument #173) are MOOT.

SIGNED at Houston, Texas, this 2nd of August, 2016.

/s/ Melinda Harmon

MELINDA HARMON
UNITED STATES
DISTRICT JUDGE

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

In Re ENRON CORPORATION SECURITIES, DERIVATIVE & "ERISA" LITIGATION,	§ § §	MDL 1446
MARK NEWBY, ET AL., Plaintiffs VS. ENRON CORPORATION, ET AL., Defendants	§ § § § § § § §	CIVIL ACTION NO. H-01-3624 AND CONSOLIDATED CASES
SAMUEL GIANCARLO, Individually and on Behalf of All Others Similarly Situated, Plaintiffs, VS. UBS FINANCIAL SERVICES, INC., UBS SECURITIES, L.L.C., UBS AG and UBS O'CONNOR, L.L.C., Defendants.	§ § § § § § § § § § §	CIVIL ACTION NO. H-03-4359 COORDINATED CASE

OPINION AND ORDER DENYING MOTION TO RECONSIDER

(Entered Nov. 30, 2016)

Pending before the Court in the above referenced cause is an opposed motion for reconsideration of the Court's August 2, 2016 Opinion and Order of Dismissal (#175), filed by Plaintiffs Samuel Giancarlo and Dr. Carlos Alsina, Individually and on Behalf of All Others Similarly Situated, along with a request that the Court grant Plaintiffs leave to file a Second Amended Complaint (#176).

Standard of Review

Although the Federal Rules of Civil Procedure do not recognize a general motion for reconsideration, courts address such motions under Rule 54(b) for interlocutory orders or under Rules 59(e) (a motion to alter or amend) and 60(b) (a motion for relief from final judgments). *Dos Santos v. Bell Helicopter Textron, Inc. Dist.*, 651 F. Supp. 2d 550, 553 (N.D. Tex. 2009), *citing Teal v. Eagle Fleet, Inc.*, 933 F.2d 341, 347 (5th Cir. 1991). The Court's August 2, 2016 Opinion and Order of Dismissal was a final judgment. Whether such a motion falls under Rule 59(e) or 60(b) depends on the time in which it is filed. If filed within twenty-eight days of the final judgment it is governed by Rule 59(e); after that time it is governed by Rule 60(b). *Barry v. Medtronic, Inc.*, Civ. A. No. 1:14-cv-104, 2015 WL 10936047, at *1 (E.D. Tex. Aug. 28, 2015). The instant motion was filed within 28 days and is thus governed by Rule 59(e).

Rule 59(e) motions "'serve the narrow purpose of allowing a party to correct manifest error of law or fact or to present newly discovered evidence.'" *Basinkeeper v. Bostick*, No. 15-30952, 2016 WL 4709860, at *3 (5th Cir. Sept. 8, 2016), *citing Waltman v. Int'l Paper Co.*, 875 F.2d 468, 473 (5th Cir. 1989). Given this narrow purpose, the Fifth Circuit has found that "'[r]econsideration of a judgment after its entry is an extraordinary remedy that should be used sparingly.'" *Id.*, *citing Templet v. HydroChem Inc.*, 367 F.3d 473, 479 (5th Cir. 2004). *See also McGillivray v. Countrywide Home Loans, Inc.*, 360 Fed. Appx. 533, 537 (5th Cir. Jan. 11, 2010) (finding that the district court may grant a Rule 59(e) motion if there is "an intervening change in the controlling law" or "to correct a clear error of law or prevent manifest injustice"), *citing In re Benjamin Moore & Co.*, 318 F.3d 626, 629 (5th Cir. 2002). "[T]he standards applicable to Rule 59(e) . . . favor denial of motions to alter or amend a judgment." *Southern Constructors Group, Inc. v. Dynalectric Co.*, 2 F.3d 606, 611 (5th Cir. 1993). District courts have wide discretion in deciding whether to grant such a motion and reopen a case. *Johnson v. Diversicare Afton Oaks, L.L.C.*, 597 F.3d 673, 677 (5th Cir. 2010). A Rule 59(e) motion is not the proper vehicle for rehashing evidence, legal theories, or arguments that could have been offered or raised before the entry of judgment." *Id., citing Simon v. U.S.*, 891 F.2d 1154, 1159 (5th Cir. 1990). Where the motion asserts discovery of new evidence, it should only be granted if "'(1) the facts discovered are of such a nature that they would probably change the outcome; (2) the facts alleged are actually newly discovered and

could not have been discovered earlier by proper diligence; and (3) the facts are not merely cumulative or impeaching.'" *Johnson*, 597 F.3d at 677, *quoting Infusion Res., Inc. v. Minimed, Inc.*, 351 F.3d 688, 696-97 (5th Cir. 2003).

The Fifth Circuit has affirmed the denial of leave to amend when the movant has "engaged in undue delay." *Goldstein v. MCI Worldcom*, 340 F.3d 238, 254 (5th Cir. 2003), *citing Little v. Liquid Air Corp.*, 952 F.2d 841, 846 (5th Cir. 1992). It has also affirmed court decisions where the movant has tried to present theories of recovery serially to the district court. *Southern Constructors*, 2 F.3d at 612.

After reviewing the record and the applicable law, the Court fully concurs with the opposition memorandum of law filed by Defendants UBS Securities, L.L.C. (f/k/a UBS Warburg, L.L.C.), UBS Financial Services, Inc. (f/k/a Paine Webber, Inc.) and UBS AG (collectively, "Defendants"). Plaintiffs fail to meet the standards for granting their motion for reconsideration. As detailed in Defendants' memorandum, Plaintiffs repeat and rehash old arguments and fail to identify manifest errors of fact or law, and they unreasonably delayed in moving to reconsider the Court's March 2012 denial of their motion for leave to file a second amended complaint as also untimely (#156).

Accordingly, the Court

ORDERS that Plaintiffs' motion to reconsider (#176) is DENIED.

SIGNED at Houston, Texas, this 30th day of November, 2016.

/s/ Melinda Harmon
MELINDA HARMON
UNITED STATES
DISTRICT JUDGE

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 16-20663

SAMUEL GIANCARLO, Individually and on behalf of all others similarly situated; CARLOS ALSINA, Medical Doctor,

Plaintiffs-Appellants

v.

UBS FINANCIAL SERVICES, INCORPORATED; UBS SECURITIES, L.L.C.; UBS AG; UBS O'CONNOR, L.L.C.,

Defendants-Appellees

Appeal from the United States District Court
for the Southern District of Texas

ON PETITION FOR REHEARING

(Filed Mar. 28, 2018)

Before DENNIS, CLEMENT, and GRAVES, Circuit Judges.

PER CURIAM:

IT IS ORDERED that the petition for rehearing is [Denied.]

ENTERED FOR THE COURT:

/s/ James L. Dennis
UNITED STATES
CIRCUIT JUDGE

Relevant Statutes, Regulation and Rules

15 U.S.C.A. § 78j

Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange –

(a)(1) To effect a short sale, or to use or employ any stop-loss order in connection with the purchase or sale, of any security other than a government security, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(2) Paragraph (1) of this subsection shall not apply to security futures products.

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement[1] any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(c)(1) To effect, accept, or facilitate a transaction involving the loan or borrowing of securities in contravention of such rules and regulations as the Commission may prescribe as necessary or

[1] So in original. Probably should be followed by a comma.

appropriate in the public interest or for the protection of investors.

(2) Nothing in paragraph (1) may be construed to limit the authority of the appropriate Federal banking agency (as defined in section 1813(q) of Title 12), the National Credit Union Administration, or any other Federal department or agency having a responsibility under Federal law to prescribe rules or regulations restricting transactions involving the loan or borrowing of securities in order to protect the safety and soundness of a financial institution or to protect the financial system from systemic risk.

Rules promulgated under subsection (b) that prohibit fraud, manipulation, or insider trading (but not rules imposing or specifying reporting or recordkeeping requirements, procedures, or standards as prophylactic measures against fraud, manipulation, or insider trading), and judicial precedents decided under subsection (b) and rules promulgated thereunder that prohibit fraud, manipulation, or insider trading, shall apply to security-based swap agreements to the same extent as they apply to securities. Judicial precedents decided under section 77q(a) of this title and sections 78i, 78***o***, 78p, 78t, and 78u-1 of this title, and judicial precedents decided under applicable rules promulgated under such sections, shall apply to security-based swap agreements to the same extent as they apply to securities.

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15 U.S.C.A. § 78u-4

Private securities litigation

(a) Private class actions

(1) In general

The provisions of this subsection shall apply in each private action arising under this chapter that is brought as a plaintiff class action pursuant to the Federal Rules of Civil Procedure.

(2) Certification filed with complaint

(A) In general

Each plaintiff seeking to serve as a representative party on behalf of a class shall provide a sworn certification, which shall be personally signed by such plaintiff and filed with the complaint, that –

(i) states that the plaintiff has reviewed the complaint and authorized its filing;

(ii) states that the plaintiff did not purchase the security that is the subject of the complaint at the direction of plaintiff's counsel or in order to participate in any private action arising under this chapter;

(iii) states that the plaintiff is willing to serve as a representative party on behalf of a class, including providing testimony at deposition and trial, if necessary;

(iv) sets forth all of the transactions of the plaintiff in the security that is the

subject of the complaint during the class period specified in the complaint;

(v) identifies any other action under this chapter, filed during the 3-year period preceding the date on which the certification is signed by the plaintiff, in which the plaintiff has sought to serve as a representative party on behalf of a class; and

(vi) states that the plaintiff will not accept any payment for serving as a representative party on behalf of a class beyond the plaintiff's pro rata share of any recovery, except as ordered or approved by the court in accordance with paragraph (4).

(B) Nonwaiver of attorney-client privilege

The certification filed pursuant to subparagraph (A) shall not be construed to be a waiver of the attorney-client privilege.

(3) Appointment of lead plaintiff

(A) Early notice to class members

(i) In general

Not later than 20 days after the date on which the complaint is filed, the plaintiff or plaintiffs shall cause to be published, in a widely circulated national business-oriented publication or wire service, a notice advising members of the purported plaintiff class –

(I) of the pendency of the action, the claims asserted therein, and the purported class period; and

(II) that, not later than 60 days after the date on which the notice is published, any member of the purported class may move the court to serve as lead plaintiff of the purported class.

(ii) Multiple actions

If more than one action on behalf of a class asserting substantially the same claim or claims arising under this chapter is filed, only the plaintiff or plaintiffs in the first filed action shall be required to cause notice to be published in accordance with clause (i).

(iii) Additional notices may be required under Federal rules

Notice required under clause (i) shall be in addition to any notice required pursuant to the Federal Rules of Civil Procedure.

(B) Appointment of lead plaintiff

(i) In general

Not later than 90 days after the date on which a notice is published under subparagraph (A)(i), the court shall consider any motion made by a purported class member in response to the notice, including any motion by a class member who is not

individually named as a plaintiff in the complaint or complaints, and shall appoint as lead plaintiff the member or members of the purported plaintiff class that the court determines to be most capable of adequately representing the interests of class members (hereafter in this paragraph referred to as the "most adequate plaintiff") in accordance with this subparagraph.

(ii) Consolidated actions

If more than one action on behalf of a class asserting substantially the same claim or claims arising under this chapter has been filed, and any party has sought to consolidate those actions for pretrial purposes or for trial, the court shall not make the determination required by clause (i) until after the decision on the motion to consolidate is rendered. As soon as practicable after such decision is rendered, the court shall appoint the most adequate plaintiff as lead plaintiff for the consolidated actions in accordance with this paragraph.

(iii) Rebuttable presumption

(I) In general

Subject to subclause (II), for purposes of clause (i), the court shall adopt a presumption that the most adequate plaintiff in any private action arising

under this chapter is the person or group of persons that –

(aa) has either filed the complaint or made a motion in response to a notice under subparagraph (A)(i);

(bb) in the determination of the court, has the largest financial interest in the relief sought by the class; and

(cc) otherwise satisfies the requirements of Rule 23 of the Federal Rules of Civil Procedure.

(II) Rebuttal evidence

The presumption described in subclause (I) may be rebutted only upon proof by a member of the purported plaintiff class that the presumptively most adequate plaintiff –

(aa) will not fairly and adequately protect the interests of the class; or

(bb) is subject to unique defenses that render such plaintiff incapable of adequately representing the class.

(iv) Discovery

For purposes of this subparagraph, discovery relating to whether a member or members of the purported plaintiff class

is the most adequate plaintiff may be conducted by a plaintiff only if the plaintiff first demonstrates a reasonable basis for a finding that the presumptively most adequate plaintiff is incapable of adequately representing the class.

(v) Selection of lead counsel

The most adequate plaintiff shall, subject to the approval of the court, select and retain counsel to represent the class.

(vi) Restrictions on professional plaintiffs

Except as the court may otherwise permit, consistent with the purposes of this section, a person may be a lead plaintiff, or an officer, director, or fiduciary of a lead plaintiff, in no more than 5 securities class actions brought as plaintiff class actions pursuant to the Federal Rules of Civil Procedure during any 3-year period.

(4) Recovery by plaintiffs

The share of any final judgment or of any settlement that is awarded to a representative party serving on behalf of a class shall be equal, on a per share basis, to the portion of the final judgment or settlement awarded to all other members of the class. Nothing in this paragraph shall be construed to limit the award of reasonable costs and expenses (including lost wages) directly relating to the representation of the class to any representative party serving on behalf of a class.

(5) Restrictions on settlements under seal

The terms and provisions of any settlement agreement of a class action shall not be filed under seal, except that on motion of any party to the settlement, the court may order filing under seal for those portions of a settlement agreement as to which good cause is shown for such filing under seal. For purposes of this paragraph, good cause shall exist only if publication of a term or provision of a settlement agreement would cause direct and substantial harm to any party.

(6) Restrictions on payment of attorneys' fees and expenses

Total attorneys' fees and expenses awarded by the court to counsel for the plaintiff class shall not exceed a reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class.

(7) Disclosure of settlement terms to class members

Any proposed or final settlement agreement that is published or otherwise disseminated to the class shall include each of the following statements, along with a cover page summarizing the information contained in such statements:

(A) Statement of plaintiff recovery

The amount of the settlement proposed to be distributed to the parties to the action, determined in the aggregate and on an average per share basis.

(B) Statement of potential outcome of case

(i) Agreement on amount of damages

If the settling parties agree on the average amount of damages per share that would be recoverable if the plaintiff prevailed on each claim alleged under this chapter, a statement concerning the average amount of such potential damages per share.

(ii) Disagreement on amount of damages

If the parties do not agree on the average amount of damages per share that would be recoverable if the plaintiff prevailed on each claim alleged under this chapter, a statement from each settling party concerning the issue or issues on which the parties disagree.

(iii) Inadmissibility for certain purposes

A statement made in accordance with clause (i) or (ii) concerning the amount of damages shall not be admissible in any Federal or State judicial action or administrative proceeding, other than an action or proceeding arising out of such statement.

(C) Statement of attorneys' fees or costs sought

If any of the settling parties or their counsel intend to apply to the court for an award of attorneys' fees or costs from any fund established as part of the settlement, a statement indicating which parties or counsel intend to make such an application, the amount of fees and costs that will be sought (including the amount of such fees and costs determined on an average per share basis), and a brief explanation supporting the fees and costs sought. Such information shall be clearly summarized on the cover page of any notice to a party of any proposed or final settlement agreement.

(D) Identification of lawyers' representatives

The name, telephone number, and address of one or more representatives of counsel for the plaintiff class who will be reasonably available to answer questions from class members concerning any matter contained in any notice of settlement published or otherwise disseminated to the class.

(E) Reasons for settlement

A brief statement explaining the reasons why the parties are proposing the settlement.

(F) Other information

Such other information as may be required by the court.

(8) Security for payment of costs in class actions

In any private action arising under this chapter that is certified as a class action pursuant to the Federal Rules of Civil Procedure, the court may require an undertaking from the attorneys for the plaintiff class, the plaintiff class, or both, or from the attorneys for the defendant, the defendant, or both, in such proportions and at such times as the court determines are just and equitable, for the payment of fees and expenses that may be awarded under this subsection.

(9) Attorney conflict of interest

If a plaintiff class is represented by an attorney who directly owns or otherwise has a beneficial interest in the securities that are the subject of the litigation, the court shall make a determination of whether such ownership or other interest constitutes a conflict of interest sufficient to disqualify the attorney from representing the plaintiff class.

(b) Requirements for securities fraud actions

(1) Misleading statements and omissions

In any private action arising under this chapter in which the plaintiff alleges that the defendant –

(A) made an untrue statement of a material fact; or

(B) omitted to state a material fact necessary in order to make the statements made, in the light of the circumstances in which they were made, not misleading;

the complaint shall specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed.

(2) Required state of mind

(A) In general

Except as provided in subparagraph (B), in any private action arising under this chapter in which the plaintiff may recover money damages only on proof that the defendant acted with a particular state of mind, the complaint shall, with respect to each act or omission alleged to violate this chapter, state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind.

(B) Exception

In the case of an action for money damages brought against a credit rating agency or a controlling person under this chapter, it shall be sufficient, for purposes of pleading any required state of mind in relation to such action, that the complaint state with particularity facts giving rise to a strong inference that the credit rating agency knowingly or recklessly failed –

(i) to conduct a reasonable investigation of the rated security with respect to the factual elements relied upon by its

own methodology for evaluating credit risk; or

(ii) to obtain reasonable verification of such factual elements (which verification may be based on a sampling technique that does not amount to an audit) from other sources that the credit rating agency considered to be competent and that were independent of the issuer and underwriter.

(3) Motion to dismiss; stay of discovery

(A) Dismissal for failure to meet pleading requirements

In any private action arising under this chapter, the court shall, on the motion of any defendant, dismiss the complaint if the requirements of paragraphs (1) and (2) are not met.

(B) Stay of discovery

In any private action arising under this chapter, all discovery and other proceedings 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.

(C) Preservation of evidence

(i) In general

During the pendency of any stay of discovery pursuant to this paragraph, unless

otherwise ordered by the court, any party to the action with actual notice of the allegations contained in the complaint shall treat all documents, data compilations (including electronically recorded or stored data), and tangible objects that are in the custody or control of such person and that are relevant to the allegations, as if they were the subject of a continuing request for production of documents from an opposing party under the Federal Rules of Civil Procedure.

(ii) Sanction for willful violation

A party aggrieved by the willful failure of an opposing party to comply with clause (i) may apply to the court for an order awarding appropriate sanctions.

(D) Circumvention of stay of discovery

Upon a proper showing, a court may stay discovery proceedings in any private action in a State court, as necessary in aid of its jurisdiction, or to protect or effectuate its judgments, in an action subject to a stay of discovery pursuant to this paragraph.

(4) Loss causation

In any private action arising under this chapter, the plaintiff shall have the burden of proving that the act or omission of the defendant alleged to violate this chapter caused the loss for which the plaintiff seeks to recover damages.

(c) Sanctions for abusive litigation

(1) Mandatory review by court

In any private action arising under this chapter, upon final adjudication of the action, the court shall include in the record specific findings regarding compliance by each party and each attorney representing any party with each requirement of Rule 11(b) of the Federal Rules of Civil Procedure as to any complaint, responsive pleading, or dispositive motion.

(2) Mandatory sanctions

If the court makes a finding under paragraph (1) that a party or attorney violated any requirement of Rule 11(b) of the Federal Rules of Civil Procedure as to any complaint, responsive pleading, or dispositive motion, the court shall impose sanctions on such party or attorney in accordance with Rule 11 of the Federal Rules of Civil Procedure. Prior to making a finding that any party or attorney has violated Rule 11 of the Federal Rules of Civil Procedure, the court shall give such party or attorney notice and an opportunity to respond.

(3) Presumption in favor of attorneys' fees and costs

(A) In general

Subject to subparagraphs (B) and (C), for purposes of paragraph (2), the court shall adopt a presumption that the appropriate sanction –

(i) for failure of any responsive pleading or dispositive motion to comply with any

requirement of Rule 11(b) of the Federal Rules of Civil Procedure is an award to the opposing party of the reasonable attorneys' fees and other expenses incurred as a direct result of the violation; and

(ii) for substantial failure of any complaint to comply with any requirement of Rule 11(b) of the Federal Rules of Civil Procedure is an award to the opposing party of the reasonable attorneys' fees and other expenses incurred in the action.

(B) Rebuttal evidence

The presumption described in subparagraph (A) may be rebutted only upon proof by the party or attorney against whom sanctions are to be imposed that –

(i) the award of attorneys' fees and other expenses will impose an unreasonable burden on that party or attorney and would be unjust, and the failure to make such an award would not impose a greater burden on the party in whose favor sanctions are to be imposed; or

(ii) the violation of Rule 11(b) of the Federal Rules of Civil Procedure was de minimis.

(C) Sanctions

If the party or attorney against whom sanctions are to be imposed meets its burden under subparagraph (B), the court shall award

the sanctions that the court deems appropriate pursuant to Rule 11 of the Federal Rules of Civil Procedure.

(d) Defendant's right to written interrogatories

In any private action arising under this chapter in which the plaintiff may recover money damages, the court shall, when requested by a defendant, submit to the jury a written interrogatory on the issue of each such defendant's state of mind at the time the alleged violation occurred.

(e) Limitation on damages

(1) In general

Except as provided in paragraph (2), in any private action arising under this chapter in which the plaintiff seeks to establish damages by reference to the market price of a security, the award of damages to the plaintiff shall not exceed the difference between the purchase or sale price paid or received, as appropriate, by the plaintiff for the subject security and the mean trading price of that security during the 90-day period beginning on the date on which the information correcting the misstatement or omission that is the basis for the action is disseminated to the market.

(2) Exception

In any private action arising under this chapter in which the plaintiff seeks to establish damages by reference to the market price of a security, if the plaintiff sells or repurchases the subject security prior to the expiration of the 90-day period

described in paragraph (1), the plaintiff's damages shall not exceed the difference between the purchase or sale price paid or received, as appropriate, by the plaintiff for the security and the mean trading price of the security during the period beginning immediately after dissemination of information correcting the misstatement or omission and ending on the date on which the plaintiff sells or repurchases the security.

(3) "Mean trading price" defined

For purposes of this subsection, the "mean trading price" of a security shall be an average of the daily trading price of that security, determined as of the close of the market each day during the 90-day period referred to in paragraph (1).

(f) Proportionate liability

(1) Applicability

Nothing in this subsection shall be construed to create, affect, or in any manner modify, the standard for liability associated with any action arising under the securities laws.

(2) Liability for damages

(A) Joint and several liability

Any covered person against whom a final judgment is entered in a private action shall be liable for damages jointly and severally only if the trier of fact specifically determines that such covered person knowingly committed a violation of the securities laws.

(B) Proportionate liability

(i) In general

Except as provided in subparagraph (A), a covered person against whom a final judgment is entered in a private action shall be liable solely for the portion of the judgment that corresponds to the percentage of responsibility of that covered person, as determined under paragraph (3).

(ii) Recovery by and costs of covered person

In any case in which a contractual relationship permits, a covered person that prevails in any private action may recover the attorney's fees and costs of that covered person in connection with the action.

(3) Determination of responsibility

(A) In general

In any private action, the court shall instruct the jury to answer special interrogatories, or if there is no jury, shall make findings, with respect to each covered person and each of the other persons claimed by any of the parties to have caused or contributed to the loss incurred by the plaintiff, including persons who have entered into settlements with the plaintiff or plaintiffs, concerning –

(i) whether such person violated the securities laws;

(ii) the percentage of responsibility of such person, measured as a percentage of the total fault of all persons who caused or contributed to the loss incurred by the plaintiff; and

(iii) whether such person knowingly committed a violation of the securities laws.

(B) Contents of special interrogatories or findings

The responses to interrogatories, or findings, as appropriate, under subparagraph (A) shall specify the total amount of damages that the plaintiff is entitled to recover and the percentage of responsibility of each covered person found to have caused or contributed to the loss incurred by the plaintiff or plaintiffs.

(C) Factors for consideration

In determining the percentage of responsibility under this paragraph, the trier of fact shall consider –

(i) the nature of the conduct of each covered person found to have caused or contributed to the loss incurred by the plaintiff or plaintiffs; and

(ii) the nature and extent of the causal relationship between the conduct of each such person and the damages incurred by the plaintiff or plaintiffs.

(4) Uncollectible share

(A) In general

Notwithstanding paragraph (2)(B), upon motion made not later than 6 months after a final judgment is entered in any private action, the court determines that all or part of the share of the judgment of the covered person is not collectible against that covered person, and is also not collectible against a covered person described in paragraph (2)(A), each covered person described in paragraph (2)(B) shall be liable for the uncollectible share as follows:

(i) Percentage of net worth

Each covered person shall be jointly and severally liable for the uncollectible share if the plaintiff establishes that –

(I) the plaintiff is an individual whose recoverable damages under the final judgment are equal to more than 10 percent of the net worth of the plaintiff; and

(II) the net worth of the plaintiff is equal to less than $200,000.

(ii) Other plaintiffs

With respect to any plaintiff not described in subclauses (I) and (II) of clause (i), each covered person shall be liable for the uncollectible share in proportion to the percentage of responsibility of that covered person, except that the total

liability of a covered person under this clause may not exceed 50 percent of the proportionate share of that covered person, as determined under paragraph (3)(B).

(iii) Net worth

For purposes of this subparagraph, net worth shall be determined as of the date immediately preceding the date of the purchase or sale (as applicable) by the plaintiff of the security that is the subject of the action, and shall be equal to the fair market value of assets, minus liabilities, including the net value of the investments of the plaintiff in real and personal property (including personal residences).

(B) Overall limit

In no case shall the total payments required pursuant to subparagraph (A) exceed the amount of the uncollectible share.

(C) Covered persons subject to contribution

A covered person against whom judgment is not collectible shall be subject to contribution and to any continuing liability to the plaintiff on the judgment.

(5) Right of contribution

To the extent that a covered person is required to make an additional payment pursuant to paragraph (4), that covered person may recover contribution –

(A) from the covered person originally liable to make the payment;

(B) from any covered person liable jointly and severally pursuant to paragraph (2)(A);

(C) from any covered person held proportionately liable pursuant to this paragraph who is liable to make the same payment and has paid less than his or her proportionate share of that payment; or

(D) from any other person responsible for the conduct giving rise to the payment that would have been liable to make the same payment.

(6) Nondisclosure to jury

The standard for allocation of damages under paragraphs (2) and (3) and the procedure for reallocation of uncollectible shares under paragraph (4) shall not be disclosed to members of the jury.

(7) Settlement discharge

(A) In general

A covered person who settles any private action at any time before final verdict or judgment shall be discharged from all claims for contribution brought by other persons. Upon entry of the settlement by the court, the court shall enter a bar order constituting the final discharge of all obligations to the plaintiff of the settling covered person arising out of the action. The order shall bar all future claims for contribution arising out of the action –

(i) by any person against the settling covered person; and

(ii) by the settling covered person against any person, other than a person whose liability has been extinguished by the settlement of the settling covered person.

(B) Reduction

If a covered person enters into a settlement with the plaintiff prior to final verdict or judgment, the verdict or judgment shall be reduced by the greater of –

(i) an amount that corresponds to the percentage of responsibility of that covered person; or

(ii) the amount paid to the plaintiff by that covered person.

(8) Contribution

A covered person who becomes jointly and severally liable for damages in any private action may recover contribution from any other person who, if joined in the original action, would have been liable for the same damages. A claim for contribution shall be determined based on the percentage of responsibility of the claimant and of each person against whom a claim for contribution is made.

(9) Statute of limitations for contribution

In any private action determining liability, an action for contribution shall be brought not later than 6 months after the entry of a final,

nonappealable judgment in the action, except that an action for contribution brought by a covered person who was required to make an additional payment pursuant to paragraph (4) may be brought not later than 6 months after the date on which such payment was made.

(10) Definitions

For purposes of this subsection –

(A) a covered person "knowingly commits a violation of the securities laws" –

(i) with respect to an action that is based on an untrue statement of material fact or omission of a material fact necessary to make the statement not misleading, if –

(I) that covered person makes an untrue statement of a material fact, with actual knowledge that the representation is false, or omits to state a fact necessary in order to make the statement made not misleading, with actual knowledge that, as a result of the omission, one of the material representations of the covered person is false; and

(II) persons are likely to reasonably rely on that misrepresentation or omission; and

(ii) with respect to an action that is based on any conduct that is not described in clause (i), if that covered person

engages in that conduct with actual knowledge of the facts and circumstances that make the conduct of that covered person a violation of the securities laws;

(B) reckless conduct by a covered person shall not be construed to constitute a knowing commission of a violation of the securities laws by that covered person;

(C) the term "covered person" means –

(i) a defendant in any private action arising under this chapter; or

(ii) a defendant in any private action arising under section 77k of this title, who is an outside director of the issuer of the securities that are the subject of the action; and

(D) the term "outside director" shall have the meaning given such term by rule or regulation of the Commission.

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17 C.F.R. § 240.10b-5

Employment of manipulative and deceptive devices.

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, 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.

Federal Rules of Civil Procedure Rule 8

General Rules of Pleading

(a) Claim for Relief. A pleading that states a claim for relief must contain:

(1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;

(2) a short and plain statement of the claim showing that the pleader is entitled to relief; and

(3) a demand for the relief sought, which may include relief in the alternative or different types of relief.

(b) Defenses; Admissions and Denials.

(1) ***In General.*** In responding to a pleading, a party must:

(A) state in short and plain terms its defenses to each claim asserted against it; and

(B) admit or deny the allegations asserted against it by an opposing party.

(2) ***Denials – Responding to the Substance.*** A denial must fairly respond to the substance of the allegation.

(3) ***General and Specific Denials.*** A party that intends in good faith to deny all the allegations of a pleading – including the jurisdictional grounds – may do so by a general denial. A party that does not intend to deny all the allegations must either specifically deny designated allegations or generally deny all except those specifically admitted.

(4) ***Denying Part of an Allegation.*** A party that intends in good faith to deny only part of an allegation must admit the part that is true and deny the rest.

(5) ***Lacking Knowledge or Information.*** A party that lacks knowledge or information sufficient to form a belief about the truth of an allegation must so state, and the statement has the effect of a denial.

(6) ***Effect of Failing to Deny.*** An allegation – other than one relating to the amount of damages – is admitted if a responsive pleading is required and the allegation is not denied. If a responsive pleading is not required, an allegation is considered denied or avoided.

(c) Affirmative Defenses.

(1) ***In General.*** In responding to a pleading, a party must affirmatively state any avoidance or affirmative defense, including:

- accord and satisfaction;
- arbitration and award;
- assumption of risk;
- contributory negligence;
- duress;
- estoppel;
- failure of consideration;
- fraud;
- illegality;
- injury by fellow servant;
- laches;
- license;
- payment;
- release;
- res judicata;
- statute of frauds;
- statute of limitations; and
- waiver.

(2) ***Mistaken Designation.*** If a party mistakenly designates a defense as a counterclaim, or a

counterclaim as a defense, the court must, if justice requires, treat the pleading as though it were correctly designated, and may impose terms for doing so.

(d) Pleading to Be Concise and Direct; Alternative Statements; Inconsistency.

(1) ***In General.*** Each allegation must be simple, concise, and direct. No technical form is required.

(2) ***Alternative Statements of a Claim or Defense.*** A party may set out 2 or more statements of a claim or defense alternatively or hypothetically, either in a single count or defense or in separate ones. If a party makes alternative statements, the pleading is sufficient if any one of them is sufficient.

(3) ***Inconsistent Claims or Defenses.*** A party may state as many separate claims or defenses as it has, regardless of consistency.

(e) Construing Pleadings. Pleadings must be construed so as to do justice.

Federal Rules of Civil Procedure Rule 9

Pleading Special Matters

(a) Capacity or Authority to Sue; Legal Existence.

(1) ***In General.*** Except when required to show that the court has jurisdiction, a pleading need not allege:

(A) a party's capacity to sue or be sued;

(B) a party's authority to sue or be sued in a representative capacity; or

(C) the legal existence of an organized association of persons that is made a party.

(2) ***Raising Those Issues.*** To raise any of those issues, a party must do so by a specific denial, which must state any supporting facts that are peculiarly within the party's knowledge.

(b) Fraud or Mistake; Conditions of Mind. In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally.

(c) Conditions Precedent. In pleading conditions precedent, it suffices to allege generally that all conditions precedent have occurred or been performed. But when denying that a condition precedent has occurred or been performed, a party must do so with particularity.

(d) Official Document or Act. In pleading an official document or official act, it suffices to allege that the document was legally issued or the act legally done.

(e) Judgment. In pleading a judgment or decision of a domestic or foreign court, a judicial or quasi-judicial tribunal, or a board or officer, it suffices to plead the judgment or decision without showing jurisdiction to render it.

(f) Time and Place. An allegation of time or place is material when testing the sufficiency of a pleading.

(g) Special Damages. If an item of special damage is claimed, it must be specifically stated.

(h) Admiralty or Maritime Claim.

(1) ***How Designated.*** If a claim for relief is within the admiralty or maritime jurisdiction and also within the court's subject-matter jurisdiction on some other ground, the pleading may designate the claim as an admiralty or maritime claim for purposes of Rules 14(c), 38(e), and 82 and the Supplemental Rules for Admiralty or Maritime Claims and Asset Forfeiture Actions. A claim cognizable only in the admiralty or maritime jurisdiction is an admiralty or maritime claim for those purposes, whether or not so designated.

(2) ***Designation for Appeal.*** A case that includes an admiralty or maritime claim within this subdivision (h) is an admiralty case within 28 U.S.C. § 1292(a)(3).

APPEAL,CLOSED,ENRON-NEWBY,MDL,
MEMBER,MOTREF

U.S. District Court
SOUTHERN DISTRICT OF TEXAS (Houston)
CIVIL DOCKET FOR CASE #: 4:03-cv-04359
Internal Use Only

Giancarlo, et al v. UBS Financial Servic [sic], et al
Assigned to:
Judge Melinda Harmon
Demand: $0
Related Case:
4:01-cv-03624
Cause: 28:1331 Fed. Question: Securities Violation

Date Filed: 10/10/2003
Date Terminated:
08/02/2016
Jury Demand: Plaintiff
Nature of Suit:
850 Securities/
Commodities
Jurisdiction:
Federal Question

Plaintiff

Samuel Giancarlo
Individually and on behalf of all others similarly situated

represented by
Bonnie E. Spencer
The Spencer Law Firm
4635 Southwest Frwy
Suite 900
Houston, TX 77027
713-961-7770
Fax: 713-961-5336
Email: bonniespencer@spencer-law.com
LEAD ATTORNEY
ATTORNEY TO BE NOTICED

Dawn Renee Meade
The Spencer Law Firm
4635 Southwest Frwy
Suite 900

	Houston, TX 77027 713-961-7770 Fax: 713-961-5336 Email: dawnmeade@ spencer-law.com *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*
Plaintiff **Carlos Alsina** *M.D.*	represented by **Dawn Renee Meade** (See above for address) *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED* **Bonnie E. Spencer** (See above for address) *ATTORNEY TO* *BE NOTICED*
V.	
Defendant **UBS Financial Services Inc**	represented by **Charles Rodney Acker** Norton Rose Fulbright US LLP 2200 Ross Ave Suite 3600 Dallas, TX 75201-7932 214-855-8000 Fax: 214-855-8200 Email: rodney.acker@ nortonrosefulbright.com *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*

Charles Rodney Acker
(See above for address)
ATTORNEY TO
BE NOTICED

Kerry Marc McMahon
Porter Hedges LLP
1000 Main St
36th Fl
Houston, TX 77002
713-226-6657
Fax: 713-226-6257
Email: kmcmahon@
porterhedges.com
ATTORNEY TO
BE NOTICED

Defendant

UBS Securities LLC

represented by
Charles Rodney Acker
(See above for address)
LEAD ATTORNEY
ATTORNEY TO
BE NOTICED

Charles Rodney Acker
(See above for address)
ATTORNEY TO
BE NOTICED

Kerry Marc McMahon
(See above for address)
ATTORNEY TO
BE NOTICED

Defendant **UBS AG**	represented by **Charles Rodney Acker** (See above for address) *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED* **Charles Rodney Acker** (See above for address) *ATTORNEY TO* *BE NOTICED* **Kerry Marc McMahon** (See above for address) *ATTORNEY TO* *BE NOTICED*
Defendant **UBS O'Connor LLC**	represented by **Charles Rodney Acker** (See above for address) *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED* **Charles Rodney Acker** (See above for address) *ATTORNEY TO* *BE NOTICED*
Claimant **Dr. Carlos Alsina**	represented by **Dawn Renee Meade** (See above for address) *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*

Movant **Credit Suisse (USA) Inc**	represented by **Lawrence David Finder** Baker & McKenzie LLP 700 Louisiana Suite 3000 Houston, TX 77002 713-427-5030 Fax: 713-427-5099 Email: lawrence.finder@ bakermckenzie.com *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*
Movant **Credit Suisse Securities (USA) LLC**	represented by **Lawrence David Finder** (See above for address) *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*
Movant **Allen Meyer**	represented by **Lawrence David Finder** (See above for address) *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*
Movant **Pershing LLC**	represented by **Lawrence David Finder** (See above for address) *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*

Interested Party **Stonehurst Capital Inc**	represented by **Andrew J Mytelka** Greer Herz Adams LLP One Moody Plz 18th Fl Galveston, TX 77550 409-797-3200 Fax: 409-766-6424 Email: amytelka @greerherz.com *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*
Interested Party **Westboro Properties LLC**	represented by **Andrew J Mytelka** (See above for address) *LEAD ATTORNEY* *ATTORNEY TO* *BE NOTICED*

Date Filed	#	Docket Text
10/10/2003	1	COMPLAINT by Samuel Giancarlo filed; FILING FEE $ 150.00 RECEIPT # 536849 (ncavazos) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 10/17/2003)
10/10/2003	2	Order setting Initial Pretrial and Scheduling Conference on Friday at 4:00 p.m. 3/26/04 9th Floor Room 9136 before Judge Ewing Werlein, Jr and Order to Disclose Interested Persons, filed. ( ) Parties notified. (ncavazos) Additional

		attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 10/17/2003)
10/10/2003		Four SUMMONS issued for UBS Financial Servic [sic], UBS Securities LLC, UBS AG, UBS O'Connor LLC (ncavazos) (Entered: 10/17/2003)
10/21/2003	3	RETURN OF SERVICE executed as to UBS Financial Servic [sic] 10/14/03 filed. Answer due on 11/3/03 for UBS Financial Servic [sic] (sjones) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 10/21/2003)
10/21/2003	4	RETURN OF SERVICE executed as to UBS Securities LLC 10/14/03 filed. Answer due on 11/3/03 for UBS Securities LLC (sjones) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 10/21/2003)
10/27/2003	5	CERTIFICATE OF INTERESTED PARTIES by Samuel Giancarlo, filed. (sjones) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 10/29/2003)
11/17/2003	6	STIPULATION of Adjournment, by Samuel Giancarlo, UBS Financial Servic [sic], UBS Securities LLC, UBS AG, UBS O'Connor LLC, filed. (kprice) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 11/20/2003)

11/17/2003		(Court only) **Added for UBS Financial Servic [sic], UBS Securities LLC, UBS AG, UBS O'Connor LLC attorney Rodney Acker (kprice) (Entered: 11/20/2003)
11/24/2003	7	MOTION to dismiss the original class action complaint, by UBS Financial Servic [sic], UBS Securities LLC, UBS AG, Motion Docket Date 12/14/03 [7-1] motion, filed. (psmith) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 11/26/2003)
11/24/2003	8	MEMORANDUM OF LAW by UBS Financial Servic [sic], UBS Securities LLC, UBS AG in support of [7-1] motion to dismiss the original class action complaint, filed (psmith) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 11/26/2003)
11/24/2003	9	APPENDIX by UBS Financial Servic [sic], UBS Securities LLC, UBS AG to [7-1] motion to dismiss the original class action complaint, [8-1] support memorandum, filed. (psmith) Additional attachment(s) added on 7/10/2006 (mgoolsby,). Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 11/26/2003)

11/26/2003	10	RETURN OF SERVICE executed as to UBS AG 10/21/03 filed. Answer due on 11/10/03 for UBS AG (sjones) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 12/03/2003)
11/26/2003	11	RETURN OF SERVICE executed as to UBS O'Connor LLC 10/20/03 filed. Answer due on 11/9/03 for UBS O'Connor LLC (sjones) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 12/03/2003)
12/09/2003	12	MOTION for appointment of lead pltf, and for approval of lead counsel, by Samuel Giancarlo, Motion Docket Date 12/29/03 [12-1] motion, 12/29/03 [12-2] motion, filed. (psmith) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 12/15/2003)
12/09/2003	13	MEMORANDUM by Samuel Giancarlo in support of [12-1] motion for appointment of lead pltf, [12-2] motion for approval of lead counsel, filed (psmith) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 12/15/2003)
12/09/2003	14	DECLARATION of Bonnie Spencer in support of [12-1] motion for appointment of lead pltf, [12-2] motion for approval of lead counsel, filed. (psmith) Additional

		attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 12/15/2003)
12/18/2003		Motion(s) referred: [12-1] motion for appointment of lead pltf referred to Magistrate Judge Frances H. Stacy, [12-2] motion for approval of lead counsel referred to Magistrate Judge Frances H. Stacy (sguevara) (Entered: 12/19/2003)
12/19/2003		Motion(s) no longer referred: [12-1] motion for appointment of lead pltf, [12-2] motion for approval of lead counsel (sguevara) (Entered: 12/22/2003)
12/29/2003		Motion(s) no longer referred: [12-1] motion for appointment of lead pltf, [12-2] motion for approval of lead counsel (sguevara) (Entered: 12/29/2003)
01/07/2004	16	RESPONSE by Samuel Giancarlo to Defts [7-1] motion to dismiss the original class action complaint, filed. (psmith) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 01/12/2004)
01/08/2004	15	ORDER granting Pltfs [12-1] motion for appointment of lead pltf and granting [12-2] motion for approval of lead counsel, entered; Parties notified. Samuel Giancarlo is APPOINTED lead pltf and Bonnie Spencer is recognized as Pltfs attorney in charge. (signed by Judge

		Ewing Werlein, Jr) (psmith) (Entered: 01/09/2004)
01/26/2004	17	UNOPPOSED MOTION for leave to file a reply memorandum in support of deft's motion to dismiss the original class action complaint, and for plaintiff to file a sur-reply by UBS AG, UBS Financial Services Inc, UBS O'Connor LLC, UBS Securities LLC, Motion Docket Date 2/15/04 [17-1] motion, 2/15/04 [17-2] motion, filed. (ltien) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 01/28/2004)
01/26/2004	18	REPLY by UBS AG, UBS Financial Services Inc, UBS O'Connor LLC, UBS Securities LLC in support of their [7-1] motion to dismiss the original class action complaint, filed. (ltien) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 01/28/2004)
01/29/2004	19	ORDER granting [17-1] motion for leave to file a reply memorandum in support of deft's motion to dismiss the original class action complaint and granting [17-2] motion for plaintiff to file a sur-reply, entered; Parties notified. (signed by Judge Ewing Werlein, Jr) (psmith) (Entered: 01/30/2004)

02/06/2004	20	Notice of change of address by atty for Samuel Giancarlo, filed. (sguevara) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 02/09/2004)
02/11/2004	21	SURRESPONSE by Samuel Giancarlo to defts' [7-1] motion to dismiss the original class action complaint, filed. (sguevara) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 02/12/2004)
03/12/2004	22	MOTION for coordination of pretrial proceedings by Samuel Giancarlo, Motion Docket Date 4/1/04 [22-1] motion, filed. (sguevara) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 03/16/2004)
03/16/2004	23	CERTIFICATE OF INTERESTED PARTIES by UBS Financial Servic [sic], UBS Securities LLC, UBS AG, UBS O'Connor LLC, filed. (sfedele) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 03/18/2004)
03/17/2004	24	NOTICE that the Rule 16 Conference is this case scheduled for 03/26/04 is CANCELLED as the Pltfs have filed a motion to consolidate with another action in U.S. Judge Harmon's Court, entered;

		Parties notified. ( ) (khightower) (Entered: 03/18/2004)
03/17/2004		(Court only) **Terminated deadlines (khightower) (Entered: 03/18/2004)
03/17/2004	25	JOINT DISCOVERY/Case Management Plan by Samuel Giancarlo, UBS Financial Servic [sic], UBS Securities LLC et al, filed. (sguevara) Additional attachment(s) added on 7/10/2006 (mgoolsby,). (Entered: 03/19/2004)
03/25/2004	26	ORDER of Coordination with MDL 1446 and Newby; granting [22-1] motion for coordination of pretrial proceedings; H-02-4359 is TRANSFERRED to the undersigned judge's docket. The scheduling conference set before the Honorable Ewing Werlein on 3/26/04 is CANCELLED and this case shall proceed according to the schedule established in Newby; terminated deadlines, entered; Parties notified. (signed by Judge Melinda Harmon) (ltien) (Entered: 03/29/2004)
03/25/2004		CASE reassigned to Judge Melinda Harmon (ltien) (Entered: 03/29/2004)
03/25/2004		Coordinated Member Case Lead Case Number: 01-3624 (ltien) (Entered: 03/29/2004)

03/29/2004		Consolidated Member Case; Lead Case Number: MDL 1446 (tward) (Entered: 03/30/2004)
12/20/2004	28	Letter from RODNEY ACKER TO JUDGE HARMON IN RESPONSE TO PLTF'S 12/28/04 LETTER, filed. (sguevara,) (Entered: 01/05/2005)
12/29/2004	27	Letter from JOSEPH J. HROCH TO JUDGE HARMON REQUESTING THE COURT CONSIDER THE MOTION TO DISMISS PENDING IN THIS CASE, filed. (sguevara,) (Entered: 01/05/2005)
01/05/2005	29	Letter from Joseph J. Hroch re: Response to Deft's letter of December 30, 2004., filed. (htippen,) (Entered: 01/05/2005)
02/17/2005	30	MEMORANDUM AND ORDER re: 7 Motion to Dismiss; UBS' Motion to Strike References are GRANTED; UBS' Motion to Dismiss Claims under the 1933 Act as time barred is Granted with prejudice; UBS' Motion to dimiss 1934 Act Claims as to UBS O'Connor only is Granted and that the entity is Dismissed from this action without prejudice; UBS' Motion to dismiss 1934 Act Claims against all other Defts is Denied.(Signed by Judge Melinda Harmon) Parties

		notified.(kmurphy,) (Entered: 02/18/2005)
02/24/2005	31	CLERKS NOTICE re: 30 Order, filed. (kmurphy,) (Entered: 02/24/2005)
08/01/2005	32	ORDER – Defendants to file an expedited response by August 5, 2005, with a courtesy copy to chambers, to Plaintiffs' Emergency Motion to Compel, filed August 1, 2005.(Signed by Judge Melinda Harmon) Parties notified.(htippen,) (Entered: 08/01/2005)
08/05/2005	33	BRIEF IN OPPOSITION to Pltfs Purported "Emergency" Motion to Compel, by UBS Financial Services Inc, UBS AG, filed.(psmith,) (Entered: 08/08/2005)
08/05/2005	34	DECLARATION of Richard JL Lomuscio, by UBS Financial Services Inc, UBS AG, filed. (Attachments: # 1 Exhibit # 2 Exhibit # 3 Exhibit # 4 Exhibit # 5 Exhibit # 6 Exhibit # 7 Exhibit) (psmith,) (Entered: 08/08/2005)
08/08/2005	35	This entry is duplicative of entry 34. DECLARATION of Richard J.L. Lomuscio re: 33 Brief by UBS AG et al, filed. (Attachments: # 2 Continuation Exh. A# 3 Continuation Exh. B# 4 Continuation Exh. C# 5 Continuation Exh. C) (hlerma,) Modified on 8/11/2005 (hlerma,).

		Modified on 8/11/2005 (ltien,). Additional attachment(s) added on 8/11/2005 (kmurphy,). (Entered: 08/11/2005)
08/08/2005	36	DECLARATION J. L. Lomuscio re: 33 Brief by UBS AG et al, filed. (Attachments: # 2 Continuation Tab 1# 3 Continuation Tab 1# 4 Continuation Tab 1# 5 Continuation Tab 1# 6 Continuation Tab 1# 7 Continuation Tab 1# 8 Continuation Tab 1) (hlerma,) Additional attachment(s) added on 8/11/2005 (hlerma,). Additional attachment(s) added on 8/11/2005 (hlerma,). Additional attachment(s) added on 8/11/2005 (hlerma,). Additional attachment(s) added on 8/11/2005 (hlerma,). (Entered: 08/11/2005)
08/08/2005	37	DECLARATION of Richard JL Lomuscio, filed.(psmith,) (Entered: 08/12/2005)
08/11/2005	38	SUPPORT for Pltfs Emergency Motion to Compel by Stonehurst Capital Inc, Westboro Properties LLC (CA H 03-1276), filed. (kmurphy,) (Entered: 08/12/2005)
08/12/2005	39	MOTION to Compel Responses to Discovery by Samuel Giancarlo, filed. Motion Docket Date 9/1/2005. (Attachments: # 1 Emergency Motion to Compel) (Meade, Dawn) (Entered: 08/12/2005)

08/26/2005	40	WITHDRAWAL of re 38 Submission in Support of Plaintiffs Emergency Motion to Compel UBS Production by Stonehurst Capital Inc, Westboro Properties LLC, filed.(kmurphy,) (Entered: 08/30/2005)
11/16/2005	41	ORDER: Pltf Samuel Giancarlo's 39 BRIEF/MOTION to Compel Responses to Discovery is STRICKEN. If pltf wishes to apply for the same relief again, he may properly file a motion to compel.(Signed by Judge Melinda Harmon) Parties notified.(psmith,) (Entered: 11/17/2005)
11/21/2005	42	*5th Amendment Questions to Mary Joyce* by Samuel Giancarlo, filed.(Meade, Dawn) (Entered: 11/21/2005)
12/05/2005	43	MOTION to Compel Responses to Request for Production by Samuel Giancarlo, filed. Motion Docket Date 12/27/2005. (Attachments: # 1 Exhibit A# 2 Exhibit B# 3 Exhibit C# 4 Exhibit D) (Meade, Dawn) (Entered: 12/05/2005)
03/24/2006	44	MOTION to Quash Subpoena on Allen Meyer, MOTION for Protective Order by Credit Suisse (USA) Inc, Credit Suisse Securities (USA) LLC, Allen Meyer, Pershing LLC, filed. Motion Docket Date

		4/17/2006. (Attachments: # 1 Proposed Order) (jbradford,) Modified on 3/27/2006 (jbradford,). (Entered: 03/27/2006)
03/24/2006	45	DECLARATION of Andrew B. Kratenstein In Support re: 44 MOTION to Quash Subpoena on Allen Meyer MOTION for Protective Order MOTION to Quash Subpoena on Allen Meyer MOTION for Protective Order, filed.(jbradford,) (Entered: 03/27/2006)
03/28/2006	46	RESPONSE in Opposition to 44 MOTION to Quash Subpoena on Allen Meyer MOTION for Protective Order MOTION to Quash Subpoena on Allen Meyer MOTION for Protective Order, filed by Samuel Giancarlo. (Attachments: # 1 Declaration of Dawn Meade# 2 Exhibit Ex. A – Court's Deposition Protocol Order) (Meade, Dawn) (Entered: 03/28/2006)
03/29/2006	47	PROPOSED ORDER re: 46 Response in Opposition to Motion„ filed.(Meade, Dawn) (Entered: 03/29/2006)
03/29/2006	48	ORDER denying 44 Motion to Quash, denying 44 Motion for Protective Order.(Signed by Judge Melinda Harmon) Parties notified.(htippen,) (Entered: 03/29/2006)

04/17/2006		(Court only) ***Motions terminated: 43 MOTION to Compel Responses to Request for Production. (htippen,) (Entered: 04/17/2006)
05/01/2006	49	Joint Emergency MOTION to Compel Production of Documents and REQUEST for Expedited Consideration by Samuel Giancarlo, filed. Motion Docket Date 5/22/2006. (Attachments: # 1 Proposed Order# 2 Proposed Order Granting Expedited Consideration) (Meade, Dawn) Modified on 5/15/2006 (ltien,). (Entered: 05/01/2006)
05/01/2006	50	ORDER granting expedited consideration of 49 Plaintiffs Mtn to Compel Production of Documents. Parties to respond by 05/05/06 with a courtesy copy to chambers.(Signed by Judge Melinda Harmon) Parties notified.(htippen,) (Entered: 05/01/2006)
05/05/2006	51	RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (Attachments: # 1 Affidavit Declaration of Brendan P. Cullen) (McMahon, Kerry) (Entered: 05/05/2006)
05/07/2006	52	EXHIBITS 1-3 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of

		Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	53	EXHIBITS 4-8 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	54	EXHIBITS 9-15 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	55	EXHIBITS 16-21 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	56	EXHIBITS 22-24 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)

05/07/2006	57	EXHIBITS 25-26 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	58	EXHIBITS 27-30 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	59	EXHIBITS 31-32 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	60	EXHIBITS 33-34 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	61	CONTINUATION OF EXHIBIT 34 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc.

		(McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	62	EXHIBIT 35 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	63	EXHIBITS 36-37 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	64	EXHIBIT 38 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	65	EXHIBITS 39-43 to the RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/07/2006	66	EXHIBIT 44 to the RESPONSE in Opposition to 49 Joint MOTION to

		Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) Modified on 5/8/2006 (espencer,). (Entered: 05/07/2006)
05/08/2006	67	REPLY to Response to 49 Joint MOTION to Compel Production of Documents, filed by Samuel Giancarlo. (Meade, Dawn) (Entered: 05/08/2006)
05/09/2006	68	Supplemental RESPONSE in Opposition to 49 Joint MOTION to Compel Production of Documents, filed by UBS Financial Services Inc. (McMahon, Kerry) (Entered: 05/09/2006)
05/15/2006	69	PLEADING STRICKEN PER ORDER 76 RESPONSE to Westboro and Stonehurst Plaintiffs' Submission in Support of the Giancarlo and Lamkin Plaintiffs' 49 Emergency MOTION to Compel Production of Documents, filed by UBS Financial Services Inc, UBS Securities LLC. (McMahon, Kerry) Modified on 5/25/2006 – linked to #49 (ltien,). Modified on 6/8/2006 (espencer,). (Entered: 05/15/2006)
05/15/2006	70	Agreed RESPONSE *to Bank Defendants' and Enron's Motion to Extend Expert Deadlines in the Consolidated and Coordinated Cases,* filed by Samuel Giancarlo.

		(Meade, Dawn) (Entered: 05/15/2006)
05/15/2006	71	ORDER On Joint Emergency Motion to Compel Production And Request For Expedited Consideration.(Signed by Judge Melinda Harmon) Parties notified.(blacy,) Modified on 5/17/2006 (blacy,). (Entered: 05/17/2006)
06/01/2006	72	DESIGNATION OF EXPERT WITNESS LIST by Samuel Giancarlo, filed.(Meade, Dawn) (Entered: 06/01/2006)
06/01/2006	73	MOTION for Extension of Time as to the Expert Report of Scott D Hakala PHD CFA by Samuel Giancarlo, filed. Motion Docket Date 6/21/2006. (Meade, Dawn) (Entered: 06/01/2006)
06/01/2006	74	PROPOSED ORDER re: 73 MOTION for Extension of Time as to the Expert Report of Scott D Hakala PHD CFA, filed.(Meade, Dawn) (Entered: 06/01/2006)
06/06/2006	75	RESPONSE to 73 MOTION for Extension of Time as to the Expert Report of Scott D Hakala PHD CFA, filed by UBS Financial Services Inc, UBS Securities LLC, UBS AG. (McMahon, Kerry) (Entered: 06/06/2006)
06/07/2006	76	ORDER striking 69 Response,. Pleading does not comply with

		Order (No. 4018) in CA 01-3624 issued 10/11/05.(Signed by Judge Melinda Harmon) Parties notified.(espencer,) (Entered: 06/08/2006)
06/07/2006	77	ORDER granting 73 MOTION for Extension of Time as to the Expert Report of Scott D Hakala PHD CFA. To clarify the record since the date has passed, retroactively the court ORDERS that the motion is granted.(Signed by Judge Melinda Harmon) Parties notified.(espencer,) (Entered: 06/08/2006)
06/09/2006	78	ORDER striking 70 Response. Pleading does not comply with Order (No. 4018) in CA 01-3624 issued 10/11/05.(Signed by Judge Melinda Harmon) Parties notified.(espencer,) (Entered: 06/09/2006)
07/17/2006	79	NOTICE *to Proceed on UBS Class Complaint* by Samuel Giancarlo, filed. (Meade, Dawn) (Entered: 07/17/2006)
07/18/2006	80	NOTICE *of Production of Expert Reports* by UBS Financial Services Inc, filed. (McMahon, Kerry) (Entered: 07/18/2006)
08/15/2006	81	First AMENDED Complaint with Jury Demand against UBS Financial Services Inc, UBS Securities LLC, UBS AG filed by Samuel

		Giancarlo.(Meade, Dawn) (Entered: 08/15/2006)
08/15/2006	82	DESIGNATION OF EXPERT WITNESS LIST by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 08/15/2006)
08/15/2006		(Court only) ***Party Carlos Alsina rep by Dawn Rene Meade added. (ltien,) (Entered: 08/18/2006)
08/31/2006	83	Agreed MOTION For A Distinct Scheduling Order by Samuel Giancarlo, Carlos Alsina, filed. Motion Docket Date 9/20/2006. (Attachments: # 1 Proposed Order Distinct Scheduling Order) (Meade, Dawn) (Entered: 08/31/2006)
09/29/2006	84	NOTICE *of Motion to Dismiss* by UBS Financial Services Inc, filed. (Attachments: # 1 Memorandum in Support of Motion to Dismiss# 2 Proposed Order – Giancarlo# 3 Affidavit Lomuscio Declaration) (McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	85	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Lomuscio Declaration Exhibit 2) (McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	86	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Lomuscio Declaration

		Exhibit 4# 2 Errata Lomuscio Declaration Exhibit 5) (McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	87	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	88	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	89	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	90	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	91	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	92	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	93	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Lomuscio Declaration Exhibit 9# 2 Exhibit Lomuscio Declaration Exhibit 10) (McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	94	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Lomuscio Declaration Exhibit 12# 2 Exhibit Lomuscio Declaration Exhibit 13# 3 Exhibit

		Lomuscio Declaration Exhibit 14) (McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	95	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Lomuscio Declaration Exhibit 16# 2 Exhibit Lomuscio Declaration Exhibit 17) (McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	96	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Lomuscio Declaration Exhibit 19) (McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	97	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Lomuscio Declaration Exhibit 21# 2 Exhibit Lomuscio Declaration Exhibit 22) (McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	98	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	99	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	100	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	101	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)

09/29/2006	102	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 09/29/2006)
09/29/2006	84	Notice of MOTION to Dismiss 81 First Amended Class Action Complaint by UBS Financial Services Inc, UBS Securities LLC, filed. Motion Docket Date 10/19/2006. (Attachments: # 1 Memorandum of Law in Support# 2 Proposed Order # 3 Declaration of Richard J.L. Lomuscio) (Entered: 12/11/2006)
10/31/2006	103	Agreed MOTION for Extension of Time to Respond to Defendants' Motion to Dismiss The First Amended Class Action Complaint by all plaintiffs, filed. Motion Docket Date 11/20/2006. (Meade, Dawn) (Entered: 10/31/2006)
10/31/2006	104	Agreed PROPOSED ORDER re: 103 Agreed MOTION for Extension of Time to Respond to Defendants' Motion to Dismiss The First Amended Class Action Complaint, filed.(Meade, Dawn) (Entered: 10/31/2006)
11/06/2006	105	ORDER extending Plaintiffs' Response Deadline to Defendants' Motion to Dismiss Plaintiffs' Third Amended Class Action Complaint 103 Motion for Extension of Time (Signed by Judge Melinda Harmon)

		Parties notified.(sbyrum,) (Entered: 11/07/2006)
11/06/2006		(Court only) ***Set/Reset Deadlines: Responses due by 11/27/2006 Replies due by 1/8/2007 (sbyrum,) (Entered: 11/07/2006)
11/14/2006	106	ORDER granting 83 Agreed Motion for A Distinct Scheduling Order.(Signed by Judge Melinda Harmon) Parties notified.(chorace,) (Entered: 11/16/2006)
11/27/2006	107	RESPONSE to 124 MOTION to Dismiss 81 First Amended Clas [sic] Action Complaint, filed by Samuel Giancarlo, Carlos Alsina. (Meade, Dawn) Modified on 12/11/2006 – linked to #124 (ltien,). (Entered: 11/27/2006)
11/27/2006	108	MEMORANDUM of Law in Support of Plaintiffs Samuel Giancarlo and Carlos Alsina's, Individually and on Behalf of All Others Similarly Situated 107 Response to the UBS Entities' 124 Second Motion to Dismiss, by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) Modified on 12/11/2006 – linked to #124 (ltien,). (Entered: 11/27/2006)
11/27/2006	109	*Declaration of David L. Augustus and Attachments 1 and* 2 by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)

11/27/2006	110	*Attachment 3* by all plaintiffs, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	111	*Attachments 4 – 8 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	112	*Attachment 9 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	113	*Attachments 10-11 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	114	*Attachments 12-13 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	115	*Attachments 14-15 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	116	*Attachment 16 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo,

		Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	117	*Attachments 17-20 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	118	*Attachments 21-24 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	119	*Attachments 25-31 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	120	*Attachments 32-35 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	121	*Attachment 36 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
11/27/2006	122	*Attachments 37-39 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)

11/27/2006	123	*Attachments 40-44 to Plaintiffs' Response to Defendants' Motion to Dismiss* by Samuel Giancarlo, Carlos Alsina, filed.(Meade, Dawn) (Entered: 11/27/2006)
01/02/2007	124	First MOTION to Certify Class by all plaintiffs, filed. Motion Docket Date 1/22/2007. (Attachments: # 1 Exhibit A, Declaration of Scott Hakala# 2 Exhibit B, Affidavit of Samuel Giancarlo# 3 Exhibit C, Affidavit of Carlos Alsina) (Meade, Dawn) (Entered: 01/02/2007)
01/08/2007	125	REPLY in Support of 84 MOTION to Dismiss 81 Amended Complaint/ Counterclaim/Crossclaim etc. MOTION to Dismiss 81 Amended Complaint/Counterclaim/Cross-claim etc., filed by UBS Financial Services Inc. (Attachments: # 1 Supplement Supplemental Declaration) (McMahon, Kerry) (Entered: 01/08/2007)
01/08/2007	126	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 01/08/2007)
01/08/2007	127	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Exhibits 1-3 (cont)) (McMahon, Kerry) (Entered: 01/08/2007)

01/08/2007	128	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Exhibits 1-3 (cont)) (McMahon, Kerry) (Entered: 01/08/2007)
01/08/2007	129	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 01/08/2007)
01/08/2007	130	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 01/08/2007)
01/08/2007	131	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 01/08/2007)
01/08/2007	132	APPENDIX by UBS Financial Services Inc, filed.(McMahon, Kerry) (Entered: 01/08/2007)
01/08/2007	133	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Exhibits 4-5 (cont)) (McMahon, Kerry) (Entered: 01/08/2007)
01/08/2007	134	APPENDIX by UBS Financial Services Inc, filed. (Attachments: # 1 Exhibit Exhibits 4-5 (cont)) (McMahon, Kerry) (Entered: 01/08/2007)
01/30/2007	135	NOTICE of Change of Address by Rodney Acker and Ellen Sessions, counsel for UBS Financial Services Inc, UBS Securities LLC, UBS AG,

		filed. (Acker, Charles) (Entered: 01/30/2007)
01/30/2007	136	Agreed MOTION for Extension of Time Class Certification Briefing by UBS Financial Services Inc, UBS Securities LLC, UBS AG, filed. Motion Docket Date 2/20/2007. (Acker, Charles) (Entered: 01/30/2007)
01/30/2007	137	Agreed PROPOSED ORDER re: 136 Agreed MOTION for Extension of Time Class Certification Briefing, filed.(Acker, Charles) (Entered: 01/30/2007)
02/01/2007	138	ORDER granting 136 Agreed Motion to Amend Briefing Schedule for Class Certification.(Signed by Judge Melinda Harmon) Parties notified.(ltien,) (Entered: 02/02/2007)
04/02/2007	139	Joint MOTION for Clarification by all plaintiffs, filed.Motion Docket Date 4/23/2007. (Meade, Dawn) (Entered: 04/02/2007)
04/02/2007	140	(CORRECTED DOCKET ENTRY. Plaintiffs Joint Notice of Dispute And Motion For Determination Regarding the Court's Stay Order, Newby #5638) Joint MOTION for Clarification by all plaintiffs, filed.Motion Docket Date 4/23/2007. (Meade, Dawn) Text

		Modified on 6/27/2007 (htippen,). (Entered: 04/02/2007)
04/03/2007	141	NOTICE *in Opposition* re: 139 Joint MOTION for Clarification, 140 Joint MOTION for Clarification by UBS Financial Services Inc, UBS Securities LLC, UBS AG, UBS O'Connor LLC, filed. (Acker, Charles) (Entered: 04/03/2007)
04/23/2007	142	NOTICE *Regarding Stay* re: 139 Joint MOTION for Clarification, 140 Joint MOTION for Clarification by UBS Financial Services Inc, UBS Securities LLC, UBS AG, UBS O'Connor LLC, filed. (Acker, Charles) (Entered: 04/23/2007)
06/14/2007	143	ORDER granting 139 Joint MOTION for Determination regarding the Court's Stay Order (#185 in H-02-851 and #139 in H-03-4359). The Court ORDERS that the motion for determination is GRANTED. The Court concludes that not only the appeal of the reversal of this Court's class certification in Newby, but also the Supreme Court's granting a writ of certiorari in the Charter Communications action warrant continuing the stay in these two suits until the Supreme Court issues an opinion on the scope of § 10(b), STAYED flag set..(Signed by Judge Melinda

		Harmon) Parties notified.(htippen,) (Entered: 06/14/2007)
06/14/2007		(Court only) ***Motion(s) terminated by 143 Order granting 139 motion: 140 Joint MOTION for Clarification. (htippen,) (Entered: 06/27/2007)
07/28/2010	144	Joint MOTION to Lift Stay by Carlos Alsina, Samuel Giancarlo, filed. Motion Docket Date 8/18/2010. (Meade, Dawn) (Entered: 07/28/2010)
08/05/2010	145	RESPONSE to 144 Joint MOTION to Lift Stay filed by UBS AG, UBS Financial Services Inc, UBS Securities LLC. (Acker, Charles) (Entered: 08/05/2010)
08/06/2010	146	Joint REPLY to Response to 144 Joint MOTION to Lift Stay, filed by Carlos Alsina, Samuel Giancarlo. (Meade, Dawn) (Entered: 08/06/2010)
08/06/2010	147	PROPOSED ORDER re: 144 Joint MOTION to Lift Stay, filed.(Meade, Dawn) (Entered: 08/06/2010)
08/09/2010	148	EXHIBITS re: 146 Reply to Response to Motion by Carlos Alsina, Samuel Giancarlo, filed.(Meade, Dawn) (Entered: 08/09/2010)
11/16/2010	149	MOTION Notice of Pending Motions by Carlos Alsina, Carlos

		Alsina, Samuel Giancarlo, filed. Motion Docket Date 12/7/2010. (Meade, Dawn) (Entered: 11/16/2010)
11/18/2010		(Court only) ***Motion(s) terminated (NOT A MOTION): 149 MOTION Notice of Pending Motions. (htippen,) (Entered: 11/18/2010)
08/11/2011	150	ORDER granting in part and denying in part 144 Joint MOTION to Lift Stay; granting the motion to lift the stay, but denying the motion as to the scheduling converence [sic]. The Court will address the pending motion to dismiss shortly, STAYED flag cleared..(Signed by Judge Melinda Harmon) Parties notified.(htippen,) (Entered: 08/11/2011)
08/18/2011	151	MOTION for Leave to File File [sic] Second Amended Complaint by Carlos Alsina, Samuel Giancarlo, filed. Motion Docket Date 9/8/2011. (Attachments: # 1 Exhibit A, # 2 Exhibit A Supp 1, # 3 Exhibit A Supp 2, # 4 Exhibit A Supp 3, # 5 Exhibit A Supp 4, # 6 Exhibit A Supp 5, # 7 Exhibit A Supp 6, # 8 Exhibit A Supp 7, # 9 Exhibit A Supp 8, # 10 Exhibit B, # 11 Proposed Order) (Meade, Dawn) (Entered: 08/18/2011)

09/07/2011	152	Agreed MOTION for Extension of Time Extend Briefing Deadlines for Plaintiffs' Motions for Leave to Amend in Lampkin v. UBS Financial Services, Inc., et al. and Giancarlo v. UBS Financial Services, Inc., et al. by UBS AG, UBS Financial Services Inc, UBS Securities LLC, filed. Motion Docket Date 9/28/2011. (Attachments: # 1 Order Granting Agreed Motion to Extend Briefing Deadlines for Plaintiffs' Motions for Leave to Amend in Lampkin v. UBS Financial Services, Inc., et al. and Giancarlo v. UBS Financial Services, Inc., et al.) (Acker, Charles) (Entered: 09/07/2011)
09/13/2011	153	ORDER denying 152 Motion for Extension of Time. Defts shall file a response within 2 days.(Signed by Judge Melinda Harmon) Parties notified.(htippen,) (Entered: 09/13/2011)
09/15/2011	154	RESPONSE in Opposition to 151 MOTION for Leave to File File [sic] Second Amended Complaint, filed by UBS AG, UBS Financial Services Inc, UBS Securities LLC. (Attachments: # 1 Proposed Order) (Acker, Charles) (Entered: 09/15/2011)
09/20/2011	155	Agreed MOTION to Vacate 138 Order on Motion for Extension of

		Time by Carlos Alsina, Samuel Giancarlo, UBS AG, UBS Financial Services Inc, UBS Securities LLC, filed. Motion Docket Date 10/11/2011. (Attachments: # 1 Proposed Order Proposed Order [sic]) (Meade, Dawn) (Entered: 09/20/2011)
03/09/2012	156	ORDER denying 151 Motion for Leave to File.(Signed by Judge Melinda Harmon) Parties notified.(htippen,) (Entered: 03/12/2012)
07/03/2012	157	ORDER granting 155 Motion to Vacate Amended Briefing Schedule for Class Certification re: 138 Order on Motion for Extension of Time.(Signed by Judge Melinda Harmon) Parties notified.(bthomas,) (Entered: 07/03/2012)
07/09/2013	158	ORDER. Status Report due within thirty days.(Signed by Judge Melinda Harmon) Parties notified.(rvazquez) (Entered: 07/09/2013)
07/19/2013	159	Joint MOTION to Perpetuate Testimony by Carlos Alsina, Samuel Giancarlo, filed. Motion Docket Date 8/9/2013. (Meade, Dawn) (Entered: 07/19/2013)

08/08/2013	160	STATUS REPORT by UBS AG, UBS Financial Services Inc, UBS Securities LLC, filed.(Acker, Charles) (Entered: 08/08/2013)
08/08/2013	161	RESPONSE in Opposition to 159 Joint MOTION to Perpetuate Testimony, filed by UBS AG, UBS Financial Services Inc, UBS Securities LLC. (Attachments: # 1 Proposed Order) (Acker, Charles) (Entered: 08/08/2013)
08/29/2013	162	NOTICE of Referral of Motion to Magistrate Judge Frances H. Stacy re 159 Joint MOTION to Perpetuate Testimony, filed. (rvazquez) (Entered: 08/29/2013)
09/03/2013	163	MOTION for Oral Hearing on Motion to Perpetuate Testimony Hearing re: 159 Joint MOTION to Perpetuate Testimony by Carlos Alsina, Samuel Giancarlo, filed. Motion Docket Date 9/24/2013. (Spencer, Bonnie) (Entered: 09/03/2013)
09/04/2013	164	NOTICE of Referral of Motion to Magistrate Judge Frances H. Stacy re 163 MOTION for Oral Hearing on Motion to Perpetuate Testimony Hearing re: 159 Joint MOTION to Perpetuate Testimony, filed. (rvazquez) (Entered: 09/04/2013)

09/04/2013	165	ORDER granting 159 Motion to Perpetuate the Testimony of Expert Witnesses.(Signed by Magistrate Judge Frances H Stacy) Parties notified. (wbostic) (Entered: 09/04/2013)
09/05/2013	166	RESPONSE in Opposition to 163 MOTION for Oral Hearing on Motion to Perpetuate Testimony Hearing re: 159 Joint MOTION to Perpetuate Testimony, filed by UBS AG, UBS Financial Services Inc, UBS Securities LLC. (Acker, Charles) (Entered: 09/05/2013)
09/05/2013	167	NOTICE *of Filing of Deposition Transcripts* by Carlos Alsina, Samuel Giancarlo, filed. (Attachments: # 1 Exhibit Exhibit 1, # 2 Exhibit Exhibit 2, # 3 Exhibit Exhibit 3) (Meade, Dawn) (Entered: 09/05/2013)
09/06/2013	168	REPLY to Response to 163 MOTION for Oral Hearing on Motion to Perpetuate Testimony Hearing re: 159 Joint MOTION to Perpetuate Testimony, filed by Carlos Alsina, Samuel Giancarlo. (Spencer, Bonnie) (Entered: 09/06/2013)
09/11/2013	169	ORDER denying as moot 163 Motion for Hearing; granting 59 Motion to perpetuate expert witnesses.(Signed by Magistrate Judge Frances H Stacy) Parties

		notified.(bwhite, 4) (Entered: 09/11/2013)
10/21/2013	170	Unopposed MOTION for Extension of Time to Perpetuate Expert Testimony by Carlos Alsina, Samuel Giancarlo, filed. Motion Docket Date 11/12/2013. (Attachments: # 1 Exhibit Exhibit A) (Meade, Dawn) (Entered: 10/21/2013)
10/23/2013	171	ORDER granting 170 Motion for Extension of Time.(Signed by Judge Melinda Harmon) Parties notified.(rvazquez) (Entered: 10/28/2013)
12/10/2013	172	NOTICE *of Supplement of Documents for Experts' Reports* re: 72 Designation of Expert Witness List by Carlos Alsina, Samuel Giancarlo, filed. (Attachments: # 1 Exhibit Exhibit 1) (Meade, Dawn) (Entered: 12/10/2013)
06/16/2014	173	Opposed MOTION Motion to Rule by Carlos Alsina, Samuel Giancarlo, filed. Motion Docket Date 7/7/2014. (Attachments: # 1 Exhibit Exhibit A, # 2 Exhibit Exhibit B) (Meade, Dawn) (Entered: 06/16/2014)
07/07/2014	174	RESPONSE to 173 Opposed MOTION Motion to Rule filed by UBS AG, UBS Financial Services Inc, UBS Securities LLC. (Effinger, Lauren) (Entered: 07/07/2014)

08/02/2016	175	OPINION AND ORDER OF DISMISSAL. Defendants' motion to dismiss is GRANTED. Lead Plaintiffs' motion for class certification document 124 and Plaintiffs' opposed joint motion for amended scheduling order, for additional briefing and for a ruling document 173 are MOOT. (Signed by Judge Melinda Harmon) Parties notified.(jdav, 4) (Entered: 08/02/2016)
08/02/2016		(Court only) ***Case Terminated per 175 Opinion and Order of Dismissal. (rhawkins) (Entered: 08/22/2016)
08/30/2016	176	MOTION for Reconsideration of 175 Memorandum and Opinion, by Carlos Alsina, Samuel Giancarlo, filed. Motion Docket Date 9/20/2016. (Attachments: # 1 Exhibit Exhibit A, # 2 Exhibit Exhibit B, # 3 Proposed Order Order) (Meade, Dawn) (Entered: 08/30/2016)
09/20/2016	177	RESPONSE in Opposition to 176 MOTION for Reconsideration of 175 Memorandum and Opinion, filed by UBS Financial Services Inc, UBS Securities LLC. (Attachments: # 1 Proposed Order) (Acker, Charles) (Entered: 09/20/2016)

09/28/2016	178	NOTICE OF APPEAL to US Court of Appeals for the Fifth Circuit by Carlos Alsina, Samuel Giancarlo (Filing fee $ 505, receipt number 0541-17302774), filed. (Meade, Dawn) (Entered: 09/28/2016)
09/29/2016	179	Clerks Notice of Filing of an Appeal. The following Notice of Appeal and related motions are pending in the District Court: 178 Notice of Appeal. Fee status: Paid, filed. (Attachments: # 1 Notice of Appeal, # 2 Opinion and Order of Dismissal, # 3 Public Docket Sheet) (rnieto, 1) (Entered: 09/29/2016)
09/29/2016		Appeal Review Notes re: 178 Notice of Appeal. Fee status: Paid. The appeal filing fee has not been paid, and the appellant is represented by counsel.No hearings were held in the case – no transcripts. Number of DKT-13 Forms expected: 1, filed. (rnieto, 1) (Entered: 09/29/2016)
10/04/2016		Notice of Assignment of USCA No. 16-20663 re: 178 Notice of Appeal, filed.(avleal, 1) (Entered: 10/04/2016)

10/13/2016	180	DKT13 TRANSCRIPT ORDER REQUEST by Plaintiffs/Dawn Meade. No hearings This order form relates to the following: 178 Notice of Appeal, filed. (Meade, Dawn) (Main Document 180 replaced on 10/13/2016) (dnoriega, 1). (Entered: 10/13/2016)
10/13/2016		(Court only) Set/Cleared Flags. Appeal_Nat flag cleared. (dnoriega, 1) (Entered: 10/13/2016)
10/19/2016		(Court only) Set/Cleared Flags. Appeal_Nat flag set. (dnoriega, 1) (Entered: 10/19/2016)
10/19/2016		(Court only) ***ROA rejected as premature; will request when needed.***(PRIVATE ENTRY), filed. (dnoriega, 1) (Entered: 10/19/2016)
10/19/2016		(Court only) ***Pending motion notification email sent to CM re: 176 (PRIVATE ENTRY), filed. (dnoriega, 1) (Entered: 10/19/2016)
11/30/2016	181	OPINION AND ORDER DENYING MOTION TO RECONSIDER (Signed by Judge Melinda Harmon) Parties notified.(rhawkins) (Entered: 11/30/2016)
12/01/2016		(Court only) ROA requested by USCA (No. 16-20663) due by 12/16/2016. Set/Cleared Flags.

		APPEAL_NAT flag cleared. (avleal, 1) (Entered: 12/01/2016)
12/06/2016		Electronic record on appeal certified to the Fifth Circuit Court of Appeals re: 178 Notice of Appeal USCA No. 16-20663, filed.(avleal, 1) (Entered: 12/06/2016)
12/16/2016		Electronic Access to Record on Appeal Provided re: 178 Notice of Appeal to Charles R. Acker, Brenda Peter Cullen, Robert J. Giuffra, Jr., Dawn R. Meade, Ellen Bush Sessions, Bonnie E. Spencer, and William H. Wagener. Attorneys of record at the Circuit may download the record from the Court of Appeals. (USCA No. 16-20663), filed.(avleal, 1) (Entered: 12/16/2016)
12/22/2016	182	Fifth Circuit Court of Appeals LETTER advising Motion to Supplement or correct the record has been granted. (USCA No. 16-20663), filed. (Attachments: # 1 Supplement to ROA 1 of 3, # 2 Supplement to ROA 2 of 3, # 3 Supplement to ROA 3 of 3) (bcampos, 1) (Entered: 12/22/2016)

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

In re ENRON CORPORATION SECURITIES LITIGATION	§ § §	MDL 1446
SAMUEL GIANCARLO, et al., Individually and On Behalf of All Others Similarly Situated, *Plaintiffs*, VS. UBS FINANCIAL SERVICES, INC., UBS SECURITIES LLC, and UBS AG *Defendants.*	§ § § § § § § § § §	CIVIL ACTION NO. 11-03-4359

PLAINTIFFS' MOTION FOR LEAVE TO FILE SECOND AMENDED CLASS ACTION COMPLAINT

(Filed Aug. 18, 2011)

I. INTRODUCTORY STATEMENT

1. Lead Plaintiff and proposed class representatives Samuel Giancarlo and Dr. Carlos Alsina (collectively "Plaintiffs"), through their attorneys, respectfully move the Court for an Order pursuant to Rule 16(b) of the Federal Rules of Civil Procedure granting them leave to file their Fourth Amended Class Action Complaint.

2. Plaintiffs file this motion because of the occurrence of certain events subsequent to the deadline for Plaintiffs to file their pending Second Amended Complaint. The impact of these subsequent events, the most significant of which was the taking of the deposition of Enron's former Chief Financial Officer Andrew S. Fastow, could not have been reasonably anticipated at the time the pending complaint was filed and the occurrence of these events produced vital evidence Plaintiffs should be permitted to incorporate into their complaint against UBS Financial Services, Inc. and UBS Securities, LLC (collectively "Defendants"). The occurrence of these events subsequent to expiration of the deadline for Plaintiffs to file their pending complaint constitutes good cause for the requested relief.

II. BACKGROUND FACTS

3. On July 11, 2003, this Court issued a scheduling order (*Newby* Doc. #1561) for *Newby* and all coordinated and consolidated cases that stayed the filing of all amended complaints until the Court ruled on the question of class certification in *Newby.* On July 11, 2006, after the Court certified the *Newby* class, it issued its July 11, 2006 Order (*Newby* Doc. # 4848), amending its earlier order and ruling that plaintiffs in coordinated cases electing to pursue their own cases rather than joining in the *Newby* action must file any motions for leave to amend "within 30 days after filing their statement of election," i.e., by August 18, 2006. Pursuant to the Court's July 11, 2006 Order, Plaintiffs elected to proceed independently of the consolidated

amended complaints in *Newby* and *Tittle* (*Giancarlo* Doc. # 79). On August 15, 2006, after the Court granted their leave to amend, Plaintiffs filed their First Amended Class Action Complaint (*Giancarlo* Doc. # 81).

4. On September 26, 2006, over one month after Plaintiffs filed their First Amended Class Action Complaint, Andrew Fastow was sentenced to six years in prison. On that same day, Lead Plaintiff in *Newby* filed Mr. Fastow's sworn declaration in relation to certain matters then pending before the Court (*Newby* Doc. #5048). Two weeks later, on October 11, 2006, the Court entered an order setting forth the dates and parameters for Mr. Fastow's deposition (*Newby* Doc. #5098), which was then conducted over the course of several days beginning on October 23, 2006.

5. On February 5, 2007, the Fifth Circuit Court of Appeals heard oral arguments in the appeal of this Court's order certifying a class in the *Newby* case. On March 19, 2007, the Fifth Circuit Court of Appeals issued its decision reversing the class certification order. On March 20, 2007, this Court entered its order staying all actions in which plaintiffs alleged Section 10(b) claims against "secondary actors" (*Newby* Doc. # 5638). Plaintiffs in this case requested clarification of the Court's March 20, 2007 Order as it related to them, given that their Section 10(b) claims relied on an identified duty of disclosure arising out of the contractual and regulated brokerage relationship between them and UBS (*Giancarlo* Doc. # 139). On June 14, 2007, the Court granted Plaintiffs' motion for determination and

concluded it best for this case to be stayed pending the Supreme Court's decision in *Stoneridge Inv. Partners, L.L. C. v. Scientific-Atlanta, Inc.* (*Giancarlo* Doc. # 143) and further action by this Court. The Supreme Court issued its decision in *Stoneridge* on January 15, 2008.

6. In anticipation of the Court lifting the stay in this matter, on January 21, 2010, Plaintiffs forwarded a copy of their draft Second Amended Class Action Complaint to counsel for Defendants. Defendants responded on January 27, 2010 to their receipt of this draft complaint, stating that they would oppose Plaintiffs' attempts to file the document. The stay, however, continued in effect. On July 28, 2010, Plaintiffs filed a Motion to Lift Stay and for Scheduling Conference (*Giancarlo* Doc. # 144). Defendants responded on August 5, 2010 (*Giancarlo* Doc. # 145) and Plaintiffs replied on August 6, 2010 (*Giancarlo* Doc. # 146). Thereafter, on November 16, 2010, Plaintiffs filed their Notice of Pending Motion (*Giancarlo* Doc. # 149) advising the Court of Plaintiffs' pending Motion to Lift Stay and requesting a hearing and/or determination on said Motion as well as a request for a scheduling conference. On August 11, 2011 the Court lifted the stay (*Giancarlo* Doc. # 150).

III. ADDITIONS TO THE COMPLAINT

7. The changes reflected in Plaintiffs' proposed Second Amended Class Action Complaint address four primary categories of changes. A summary of these changes is attached hereto as Exhibit B. First, the most

important change proposed in Plaintiffs' Second Amended Class Action Complaint is the inclusion of allegations based on evidence obtained as the result of Mr. Fastow's deposition. Defendants took the position in connection with its attempt to dismiss Plaintiffs' First Amended Class Action Complaint that Plaintiffs' claims would "not improve with the benefit of discovery" (*Giancarlo* Doc. # 84 at p. 5). Defendants obviously did not expect Fastow to testify because, despite Defendants' representations to this Court that its employees knew nothing about the fraud at Enron, Fastow testified that he personally talked to UBS's designated relationship bankers for Enron about the financial performance problems Enron faced and the various means by which Enron and its banks addressed those issues through intentionally misleading manipulation. *See* Exhibit A at ¶ 81. Given this testimony from Mr. Fastow, and UBS's documented desire to become a Tier I bank for Enron, it is no surprise then that the evidence uncovered through discovery demonstrates efforts by UBS to be involved in each of the different types of transactions discussed by Mr. Fastow during this deposition. *See id.* A at ¶¶ 66-132. Thus, Mr. Fastow's testimony, unobtainable prior to Plaintiffs' deadline to file their First Amended Class Action Complaint, not only provides critical evidence supporting Plaintiffs' Section 10(b) claims, it also provides the best and most logical framework within which to demonstrate UBS's knowledge and, by extension, scienter.

8. Second, in Plaintiffs' First Amended Class Action Complaint, Plaintiffs allege that during the relevant time period, Defendants were members of a single, integrated banking venture known as "UBS" (*Giancarlo* Doc. # 81 at ¶¶ 26-44). As specifically detailed in Plaintiffs' proposed Second Amended Class Action Complaint, Plaintiffs relied upon UBS AG's own public filings with the Securities and Exchange Commission in asserting that Defendants were part of a single, integrated banking entity. *See* Exhibit A at ¶¶ 31-43. In moving to dismiss Plaintiffs' First Amended Class Action Complaint, despite clear and conclusive statements in UBS's public filings, Defendants denied its integrated status, instead maintaining that the Defendants operated entirely separately from one another (*Giancarlo* Doc. # 84 at, e.g., pp. 4, 8, 13, and 32). In fact, Defendants' entire argument in its attempt to have Plaintiffs' Section 10(b) claims dismissed is dependent upon the premise that Defendants operated entirely separately from one another. Although Plaintiffs' allegation that the Defendants did in fact operate as a single integrated entity must be accepted as true for purposes of a motion to dismiss, the proposed Second Amended Class Action Complaint includes several paragraphs detailing "UBS's" own admissions in SEC filings of exactly how the various UBS entities operated together as a joint venture during the relevant time period. *See* Exhibit A at ¶¶ 31-43.

9. Third, Plaintiffs allege in their First Amended Class Action Complaint that the false public

characterization of a publicly traded company's financial position is a material fact. Experts designated by UBS provided specific testimony that Enron's financial representations were material and that Enron's financial representations during the relevant time period were false and misleading. *See* Exhibit A at ¶¶ 61, 169. Because expert depositions under the governing scheduling order were conducted after the deadline for Plaintiffs to file the First Amended Class Action Complaint, this evidence could not be obtained prior to its filing. Plaintiffs desire to incorporate this testimony of UBS's experts into an active complaint for the Court's consideration in connection with Defendants' attempts to have the Plaintiffs' claims dismissed.

10. Fourth, Plaintiffs' proposed Second Amended Class Action Complaint eliminates certain claims previously made by the proposed class. Specifically, the proposed Second Amended Class Action Complaint alleges that only individuals who purchased Enron securities during the relevant fraud class period assert Section 10(b) claims against Defendants.

11. Finally, in addition to the foregoing, Plaintiffs must admit they are not blind to the "mistaken hostility towards the Section 10(b) private cause of action" demonstrated relatively recently by some courts. *See Stoneridge Inv. Partners, L.L.C. v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 128 S. Ct. 761, 779 (2008) (Stevens, J., dissenting). In response to this confusing situation, Plaintiffs desire to present the most compelling Section 10(b) case they can in documentary form in order that the Court may consider the essential

allegations, each one with a citation to the evidence Plaintiffs contend support the allegation, and determine on the merits of the case whether or not Plaintiffs state a primary violation of Section 10(b) by Defendants. To that end, Plaintiffs request leave to file their Second Amended Complaint, which essentially constitutes a marshalling of Plaintiffs' evidence (with some evidence necessarily omitted on issues such as witness credibility and the like).

IV. ARGUMENT

12. Plaintiffs' Motion for Leave to File their Second Amended Complaint is governed by Rule 16(b)(4) of the Federal Rules of Civil Procedure, which requires modifications of the Court's scheduling orders to be for "good cause." Even so, when amendment is sought after the scheduling order deadline, leave to amend should be freely given when there is good cause. *See* Fed. R. Civ. Pr. 16(b)(3)(A), (b)(4). When considering whether to allow a party to amend its complaint after the time provided for in the relevant scheduling order, the following four factors should be considered: (1) the reason(s) the party failed to move timely for leave to amend; (2) the importance of the amendment; (3) potential prejudice in permitting the amendment; and (4) the availability of a continuance to cure any prejudice. *See S&W Enterprises L.L.C. v. Southtrust Bank of Alabama, NA.*, 315 F.3d 533, 536 (5th Cir. 2003); *see also, Hawthorne Land Co. v. Occidental Chemical Corp.*, 431 F.3d 221, 227 (5th Cir. 2005), *cert. denied,* 127 S. Ct. 48 (2006).

13. Considered in connection with a case that has the unique scheduling and procedural history as *Giancarlo*, the foregoing factors seem somewhat out of place. Nevertheless, good cause exists under these factors for allowing Plaintiffs' requested leave to file their Second Amended Class Action Complaint. Obviously Plaintiffs could not have included subsequently-obtained evidence in its current complaint, and Plaintiffs should not be required to anticipate that Defendants would take positions inconsistent with their own SEC filings. As to the importance of the amendment to Plaintiffs, this can only be ascertained in hindsight, depending on the Court's inclination to deny or grant Defendants' Motion to Dismiss the First Amended Class Action Complaint.

14. Finally, there is no actual prejudice to Defendants if the Court permits Plaintiffs to amend their complaint. Over one and a half years ago Plaintiffs furnished to Defendants a draft copy of the proposed Second Amended Class Action Complaint. At the time, Plaintiffs stated their intention to seek leave of Court to file the Second Amended Class Action Complaint as soon as this Court lifted the stay that had been in place in this case since March 20, 2007. Even though counsel for Defendants responded on January 27, 2010, stating that they would oppose Plaintiffs' Motion for Leave to file the Second Amended Class Action Complaint, Defendants have nevertheless had 19 months to study the allegations and evidence contained in the proposed amended complaint.

15. Defendants will no doubt argue that allowing the amendment would cause extreme prejudice to their interests. No doubt this argument will center on costs associated with filing an additional motion to dismiss. Such an analysis of prejudice is shortsighted and fails to take into account the potential savings associated with the Court making procedural determinations based on the most developed filings the parties can offer. On balance, it is best for all parties to this litigation to have the Court's determination based on the most comprehensive record the parties are prepared and have the ability to make. The Plaintiffs' Second Amended Class Action Complaint constitutes the most comprehensive complaint the Plaintiffs can make based on the evidence produced to them by Defendants.

V. REQUEST FOR HEARING

16. Pursuant to S.D. Tex. Loc. Ct. R. LR7.8, Plaintiffs request a hearing on the foregoing motion.

VI. PRAYER FOR RELIEF

WHEREFORE, Plaintiffs pray for relief as follows:

A. An order from the Court allowing Plaintiffs leave to amend to file Plaintiffs' Second Amended Class Action Complaint, a copy of which is attached hereto as Exhibit A; and

B. Such other and further relief as the Court may deem just and proper.

Dated:
August 18, 2011

/s/ Dawn Meade

Dawn Meade,
TBN 13879750, FAN 15180
4635 Southwest Freeway,
Suite 900
Houston, Texas 77027
Tel:(713) 961-7770
Fax: (713) 961-5336
Email: dawnmeade@
spencer-law.com

OF COUNSEL:

THE SPENCER LAW FIRM
Bonnie E. Spencer, TBN 06366100; FAN 7343
David L. Augustus, TBN 24036159; FAN 33221
4635 Southwest Freeway, Suite 900
Houston, Texas 77027
Tel: 713-961-7770
Fax: 713-961-5336
Email: bonniespencer@spencer-law.com
Email: davidaugustus@spencer-law.com

ATTORNEYS FOR PLAINTIFFS, Individually and on Behalf of all Others Similarly Situated

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[Certificate Of Conference Omitted]

[Certificate Of Service Omitted]

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[1] **IN THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF TEXAS HOUSTON DIVISION**

In re ENRON CORPORATION SECURITIES LITIGATION	§ § §	MDL 1446
SAMUEL GIANCARLO, et al., Individually and On Behalf of All Others Similarly Situated, *Plaintiffs*, VS. UBS FINANCIAL SERVICES, INC., UBS SECURITIES LLC, and UBS AG *Defendants.*	§ § § § § § § § § §	CIVIL ACTION NO. H-03-4359

PLAINTIFFS' SECOND AMENDED CLASS ACTION COMPLAINT

[2] **Table of Contents**

I.	JURISDICTION AND VENUE	5
II.	PARTIES	6
III.	CLASS ACTION ALLEGATIONS	7
IV.	RESPONDEAT SUPERIOR/CONTROL PERSON LIABILITY	8
V.	PLAINTIFFS' CLAIMS	9
VI.	THE "UBS GROUP"	10

A. BANKING LEGISLATIVE HISTORY 10
B. UBS HISTORY 12
C. THE "UBS GROUP" JOINT VENTURE 15
D. THE ROLE OF PAINEWEBBER IN THE "UBS GROUP" 24
VII. HISTORY OF ENRON 30
VIII. ENRON'S MATERIALLY MISLEADING FINANICALS 34
A. BACKGROUND 34
B. ENRON'S FINANCIAL TRANSACTIONS ... 39
i. Prepays 39
ii. Share Trusts 40
iii. FAS 125/140 42
iv. Minority Interests 44
v. Accounting Hedges 45
vi. Oral Assurances 46
IX. UBS KNEW ENRON USED THESE TYPES OF TRANSCATIONS [sic] TO MISSTATE ITS FINANCIAL PERFORMANCE 46
A. UBS/ENRON RELATIONSHIP 46
[3] B. UBS KNOWLEDGE OF ENRON TRANSACTIONS 47
i. Prepays (Yosemite III and Yosemite IV) 48
ii. Share Trust (Whitewing/Osprey) ... 52
iii. FAS 125/140 (Kahuna/Waimea) ... 57

iv. Minority Interest (Rawhide) 58

v. Accounting Hedges (1999 and 2000 Equity Forward Amendments)..... 60

vi. Oral Assurances (E-Next) 73

X. UBS ALSO KNEW MATERIAL, NON-PUBLIC INFORMATION CONCERNING "EMBEDDED LOSSES" IN ENRON'S ASSETS..... 77

XI. UBS's CAREFUL MANAGEMENT OF ITS CREDIT EXPOSURE FURTHER DEMONSTRATES ITS APPRECIATION OF ENRON'S FINANCIAL SITUATION 82

XII. UBS POSSESSED THE REQUIRED STATE OF MIND FOR FRAUD..... 98

XIII. UBS's TREATMENT OF PLAINTIFFS.. 103

XIV. UBS's UNIQUE RELATIONSHIP TO ENRON EMPLOYEES..... 105

XV. UBS's FRAUD WAS IN CONNECTION WITH A SECURITIES TRANSACTION 118

XVI. UBS's FRAUD CAUSED PLAINTIFFS' ECONOMIC LOSSES 119

A. Background 119

B. Enron's Bankruptcy was Foreseeable to UBS..... 120

C. The Event Study Performed by Scott D. Hakala, Ph.D, CFA Shows Plaintiffs Realized Losses As the Market Reacted to Concerns that Enron Engaged in Transactions in Order to Report, and Did Report, Its Financial Results in a Materially Misleading Way 125

i. Background of Dr. Hakala's Event Study..... 125

ii. Discussion of the Events and Their Relationship to UBS's Conduct 126

a. The Build Up of an Inflation Component in the Price of Enron Stock..... 126

b. The Dissipation of the Inflation Component in the Price of Enron Stock..... 133

[4] iii. Plaintiffs' Fraud Damages 143

XVII. THE LAW PRESUMES PLAINTIFFS RELIED ON THE NON-DISLCOSED MATERIAL FACT 144

XVIII. PRAYER FOR RELIEF 146

[5] 1. The Plaintiffs, SAMUEL GIANCARLO and DR. CARLOS ALSINA (collectively "Plaintiffs") file this their Second Amended Class Action Compliant against UBS Financial Services, Inc. f/k/a UBS PaineWebber, Inc., UBS Securities, LLC f/k/a UBS Warburg, LLC, and UBS AG (collectively "Defendants") and would respectively show the Court as follows:

I. JURISDICTION AND VENUE

2. Original jurisdiction is proper in this Court pursuant to 28 U.S.C. §1331 because the claims arise under the laws of the United States, specifically, §§11 and 15 of the Securities Act of 1933, 15 U.S.C. §§77(k) and 77(o); §§10(b), as implemented through 17 CFR 240.10b-5, and 20 of the Securities Exchange Act of 1934, 15 U.S.C. §§78j(b) and 78(t); and is brought pursuant to the Private Securities Litigation Reform Act, 15 U.S.C. §78(u)(4) *et seq*.

3. Venue is proper in the Houston Division of the Southern District of Texas under 28 U.S.C. § 1391(b), as the Defendants have significant contacts in this district and division, and this is the district and division in which a substantial part of the events or omissions giving rise to the claim occurred.

4. In connection with the acts alleged in this complaint, Defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, including, but not limited to, the mails, interstate telephone communications, and the facilities of the national securities market.

[6] II. PARTIES

5. Plaintiff Samuel Giancarlo ("Giancarlo") is a resident of George Town, Texas. Giancarlo files this action for himself and as representative of a class of similarly situated people pursuant to Rule 23 of the Federal Rules of Civil Procedure and the Private

Securities Litigation Reform Act, 15 U.S.C. § 78u-4. Giancarlo purchased Enron Corp. ("Enron") debt securities in a UBS PaineWebber, Inc. account during the relevant time period in reliance on the information provided to him, and absence of information withheld from him, by Defendants and without any knowledge of the facts underlying the federal securities fraud claims asserted herein.

6. Plaintiff Carlos Alsina ("Alsina") is a resident of Houston, Texas. Alsina files this action for himself and as representative of a class of similarly situated people pursuant to Rule 23 of the Federal Rules of Civil Procedure and the Private Securities Litigation Reform Act, 15 U.S.C. § 78u-4. Alsina purchased Enron debt securities in a UBS PaineWebber, Inc. account during the relevant time period in reliance on the information provided to him, and absence of information withheld from him, by Defendants and without any knowledge of the facts underlying the federal securities fraud claims asserted herein.

7. Defendant UBS Financial Services, Inc., previously known as UBS PaineWebber, Inc. (hereinafter "PW"), is a Delaware corporation authorized to do business in Texas and has appeared by counsel in this lawsuit. PW is a wholly owned subsidiary of UBS AG.

8. Defendant UBS Securities LLC, previously known as UBS Warburg, LLC (hereinafter "Warburg"), is a Delaware limited liability company authorized to do business in Texas and has appeared by counsel in

this lawsuit. UBS is also a wholly owned subsidiary of UBS AG.

[7] 9. Defendant UBS AG is a foreign Corporation registered in Connecticut and authorized to do business in Texas. UBS AG has appeared by counsel in this lawsuit.

10. As described further below, "UBS" or the "UBS Group" is a joint venture including, *inter alia*, PW, Warburg, and UBS AG.

III. CLASS ACTION ALLEGATIONS

11. Plaintiffs bring this action pursuant to Rule 23 of the Federal Rules of Civil Procedure on behalf of all persons similarly situated who purchased or acquired Enron's publicly traded debt securities in a UBS account from *November 5, 2000 through and including December 2, 2001* (the "Class Period") (the "Class");

12. Excluded from the class are PW, Warburg, UBS AG and subsidiaries or affiliates of these companies, any past or present officers, directors or employees of Defendants (and members of their immediate families), or subsidiaries or affiliates of these companies or any national, state or local governmental entities/agencies or departments. Also excluded from the class are entities or individuals who have plead guilty, no contest, or have otherwise been convicted criminally, or have either admitted or been adjudicated in a civil or bankruptcy proceeding, of having engaged or

participated in a fraud in connection with Enron Corp. or any of its subsidiaries or affiliates.

13. The members of the Class are so numerous joinder of all members is impracticable.

14. Plaintiffs' claims are typical of the claims of the Class because Plaintiffs and all the Class members sustained damages that were caused by the Defendants' unlawful conduct complained of herein.

[8] 15. Plaintiffs are representative parties who will fairly and adequately protect the interests of the Class members. Plaintiffs have retained counsel who are experienced and competent. Plaintiffs have no interest that is in conflict with those of the Class they seek to represent.

16. A class action would be superior to all other available methods for the fair and efficient adjudication of this controversy. Plaintiffs know of no difficulty to be encountered in the management of this action precluding its maintenance as a class action.

17. The prosecution of separate actions by individual Class members would create a risk of inconsistent and varying adjudications, which could establish incompatible standards of conduct for Defendants. Questions of law and fact common to the Class predominate over any questions that may affect only individual members. Among the common questions of law and fact as to the securities fraud allegations under the 1934 Act are:

(a) whether the Defendants engaged in a course of conduct or adhered to certain business practices that violated the anti-fraud provisions of the 1934 Act;

(b) whether the Defendants failed to disclose to Class members material facts;

(c) whether the Defendants had a duty to disclose to Class members the alleged materials [sic] facts;

(d) whether the Defendants had a duty to take action to protect the Class members;

(e) whether a causal connection exists between the content of the non-disclosed facts and any harm actually suffered by the Class members; and

(f) the extent and the appropriate measure of damages sustained by Class members.

IV. RESPONDEAT SUPERIOR/CONTROL PERSON LIABILITY

18. Defendants' employees violated federal securities laws at a time when Defendants had the power and/or ability to control their employees' actions. Defendants' advocation of the violations complained of herein or, alternatively, their failure to prevent these violations, may not [9] be excused by any theory that they had a reasonable, and enforced, supervisory system in place. Defendants are responsible for their employees' conduct under the doctrine of respondeat superior and as control persons under § 20 of the

Securities Exchange Act of 1934, 15 U.S.C. § 78(t), as amended.

V. PLAINTIFFS' CLAIMS

19. Generally, defendants may violate the anti-fraud provisions of the Securities Exchange Act of 1934 (the "1934 Act") in two separate ways: (1) through materially false statements or statements which are materially misleading due to the omission of additional information; and (2) through non-representational acts, i.e., by employing a device, scheme, or artifice to defraud or engaging in any act, practice, or course of business which operates as a fraud. The Fraud Plaintiffs bring their claims against Defendants based upon the second category of violations, specifically for engaging in non-representational deceptive conduct which violates Section 10(b) of the 1934 Act as implemented through Subsections (a) and (c) of Rule 10b-5. Defendants' acts, practices, and course of business combined to operate a fraud upon the Fraud Plaintiffs and deceived them into believing the price at which they purchased their Enron securities was determined by the natural interplay of supply and demand. Defendants' obligations to these Plaintiffs pursuant to a direct brokerage relationship between the parties required disclosure of all which was necessary to fulfill the fundamental purpose of the securities laws. UBS positioned itself between two classes of clients – its retail brokerage clients and its corporate client – such that UBS could not fulfill its legal obligations both to

Plaintiffs and Enron concurrently. Industry standards, which UBS purportedly adopted in its corporate policies, include specific practices intended to manage and minimize the dangers associated with such conflicts. UBS both failed to employ these standards and failed to disclose the information and [10] knowledge it possessed during the Fraud Period regarding the manipulation of Enron's public financial appearance, some of which was actually accomplished through UBS. This information was material under the securities laws in the sense that a reasonable investor would have considered the information important in making decisions to trade in Enron securities. Ignorant of this undisclosed information, the Fraud Plaintiffs purchased Enron equity and preferred securities in their UBS retail brokerage accounts during the Fraud Class Period. UBS's failure to disclose to these Plaintiffs the material information possessed by UBS concerning Enron had the effect of concealing the circumstances that bore on their ultimate economic loss, e.g., it concealed, among other things, the risks that Enron would be unable to service its debt and consequently suffer financial collapse. Thus, UBS's failure to disclose material information to the Fraud Plaintiffs operated as a fraud in violation of Section 10(b) and Rule 10b-5 and was a direct and immediate proximate cause of the economic losses ultimately suffered by these Plaintiffs.

VI. THE "UBS GROUP"

A. BANKING LEGISLATIVE HISTORY

20. In the wake of the stock market crash of 1929, Congress passed the Glass-Steagall Bank Act of 1933 to erect a wall between commercial banking and investment banking activities. The Act effectively prevented banks from doing business on Wall Street through §§20 and 32. Section 20 forbade member banks from affiliating with a company "engaged principally" in the "issue, flotation, underwriting, public sale, or distribution at wholesale or retail or through syndicate participation of stocks, bonds, debentures, notes, or other securities." Section 32 prohibited member banks from having interlocking directorships or close officer or employee relationships with a firm "principally engaged" in investment banking activities.

[11] 21. Congress enacted the Glass-Steagall Act to prevent three pervasive occurrences associated with the combination of investment and commercial banking activities:

i. Risk to commercial and savings deposits when banks invest their assets in securities;

ii. Issuance of loans made to shore up the price of securities or the financial position of companies in which a bank had invested assets; and

iii. Conflicts of interest as between a bank's financial interests, an issuing client's interests, and a brokerage client's interests.

22. Post Glass-Steagall, Congress sought to further its goal of limiting the growth and resulting power of banks. As a result, during the 1930's and 1940's, banks focused on the fundamental practices of taking deposits and making loans. The 1950's, however, ushered in a new age of "aggressive" activities to once again consolidate some banking activities. Again, Congress took action to protect the public. First, in 1956 Congress enacted the Bank Holding Company Act to prevent financial-services conglomerates from amassing too much power. Then, in response to aggressive acquisitions and expansion by the insurance company TransAmerica Corp., which owned Bank of America and an array of other businesses, Congress created a barrier between banking and insurance. In passing the protectionist legislation, Congress took prudent steps to prevent the risk of loss to a bank associated with investment activities and insurance underwriting.

23. Then, in the late 1990's, decades after these legislative actions, Congress changed its attitude about the banking industry and its protection of consumers. On April 6, 1998, Citicorp and the Travelers Group announced their merger. Pre-merger, Citicorp operated as a bank holding company and Travelers operated as an insurance underwriter. Travelers also owned Salomon Smith Barney, a retail securities brokerage firm. To facilitate the merger, in November of 1999, Congress passed the Gramm-Leach-Bliley Act ("GLBA"). The GLBA [12] repealed the provisions of the Glass-Steagall Act that prohibited the combining of commercial and investment bank activities. Thus,

the GLBA eliminated the restrictions on commercial and investment banks by granting financial holding companies the ability to own commercial banks, investment banks, insurance companies, and securities firms. For the first time since the era of the Great Depression, the GLBA created an environment wherein one entity like UBS could integrate operations for the benefit of a corporate client like Enron, providing a powerful combination of lending, investment banking, and securities activities.[1] UBS moved immediately to establish itself as such an entity.

B. UBS HISTORY

24. By 1990, the banking industry as a whole was in decline and the role of banks was in question. The traditional strengths of banks as providers of capital were being undermined by the ability of borrowers to access the capital markets directly. The emergence of non-bank, stand-alone competitors increased the risk and reduced the profitability of many commercial banks. The equity values of banks suffered as a consequence. At the same time, technology was advancing

[1] The dangers associated with such a combination of businesses under one organizational umbrella continue to manifest themselves as a primary cause of the 2008 worldwide economic crisis. The very same issues which led to the fraud losses complained of herein led to the elimination of tremendous wealth from the worldwide financial markets and required taxpayers, though [sic] the hands of government, to bailout a number of organizations like UBS, whose failure to manage their own risks required the Swiss government to infuse US$5.3 billion into UBS and to agree to accept up to US$60 billion in illiquid UBS assets.

very quickly. Costs for sophisticated financial computing decreased by close to one hundred percent (100%) and deregulation and globalization were contentious issues.

25. In the midst of these issues, Swiss Bank Corporation ("SBC") began its journey down the road that would lead to its merger with Union Bank of Switzerland ("Union Bank") and the creation of the global giant UBS. On May 10, 1995, SBC acquired S.G. Warburg, Plc., a [13] European investment bank. The new company was called SBC Warburg. SBC Warburg expanded into the United States in September of 1997 by acquiring the New York investment bank Dillon Read & Co. The investment banking division then became known as SBC Warburg Dillon Read. One year later, in June 1998, SBC merged with Union Bank, creating both UBS AG and the "UBS Group."

26. Early analysis did not favor the merger between these two powerhouse Swiss banks. In February 2000, UBS restructured and branded its investment banking operations UBS Warburg. The initial focus of UBS Warburg's expansion plans turned out to be the well-established United States brokerage firm PaineWebber, Inc. In July, 2000, UBS announced it was acquiring the 121-year-old institution for $10.8 billion in cash and stock. UBS described the merger in a July 12, 2000 Media Release as follows:

> PaineWebber will become an integral part of UBS Warburg. Combining UBS Warburg's premium content and global reach with

> PaineWebber's private client franchise, and uniting the two highly complementary institutional franchises creates a preeminent global investment services firm. UBS Warburg will be one of the few financial institutions possessing top-class private, institutional and corporate client franchises, across the world, served by a full range of content, products and services.

27. Acquiring PW added more than 8,000 brokers and 2.7 million clients to the UBS Group portfolio. UBS's stated rationale for the merger was to add "a leading position with US affluent and high net worth clients to what is already the world's largest private bank." According to UBS:

> UBS Warburg has a particularly strong position in distributing non-US products to US clients, and PaineWebber brings significant equity and fixed income distribution strength and a top ten ranked US equity research team. Strong US retail distribution will also enhance the ability to win primary mandates globally. UBS Warburg provides a wealth of content with a wide range of attractive products and expertise that can be leveraged for [14] PaineWebber's private clients, from top-ranked global equity research to direct access to new issues across the world's securities markets, and a superior private equity capability.

28. UBS attracted an influx of new talent as well. In November 2000, Warburg announced the

arrival of Ken Moelis ("Moelis"), the former co-head of investment banking in the Americas for Credit Suisse First Boston. Moelis agreed to join Warburg as co-head of its American investment banking unit. John Costas, Warburg's then COO, said upon the announcement, "It is our intent to build aggressively upon our current investment banking platform and continue to accelerate our growth. Simply stated, our goal is to be among the top investment banks in the United States." Thus, by the end of 2000, UBS had quieted its critics by securing its place in the American markets and reporting global profits of $4.8 billion, an increase of $600 million over the previous year.

29. While most of Wall Street pulled out the axe in 2001, laying off hundreds of bankers, UBS did just the opposite. From March 2001 to June 2002, the firm increased its U.S. investment banking staff by 10%, according to *The Wall Street Journal*. UBS's hiring frenzy began just after Moelis helped recruit senior bankers in sectors such as real estate, technology and industrials. Moelis even poached the financial services team of Credit Suisse First Boston, the firm he left, to join UBS.

30. UBS's radical changes throughout 2000 and 2001 transformed it into a new Wall Street, and global, player. In 2001 the firm became Europe's top investment bank based on revenues generated from investment banking activities. According to the *Wall Street Journal,* the firm reported a 7.5% European market share in investment banking revenues in 2001, up from 4.5% in 2000. In the U.S., the firm broke into the

Top 10 in overall investment banking revenues. It nearly doubled its U.S. market share in 2001 to 3.2%, good enough for ninth place in [15] total investment banking revenues. UBS Warburg also broke into the U.S. top 10 list of equity underwriters. The firm reported that U.S. investment banking operations represent about 40% of total revenues, compared with less than 15% previously. UBS's ambition to be the world's most powerful bank clearly manifested itself in its business relationship with Enron.

C. THE "UBS GROUP" JOINT VENTURE

31. During the Fraud Class Period, UBS AG, UBS Warburg, LLC, and UBS PaineWebber, Inc. worked jointly together as a distinct legally recognized venture named the "UBS Group," and branded "UBS." A joint venture exists where two or more parties agree for their mutual benefit to combine their skills, property, and knowledge and to actively manage the business. *See Haley v. Talcott*, 864 A.2d 86, 94 (Del. Ch. 2004) (citing, *inter alia, J. Leo Johnson v. Carmer*, 156 A.2d 499, 502 (Del. 1959)).[2] Joint ventures do not arise

[2] Because Defendants contend Delaware law governs their corporate forms, Plaintiffs address the elements of a joint venture in the context of Delaware law. *See* Reply Memorandum of Law in Support of Defendants' Motion to Dismiss Plaintiffs' Third Amended Class Action Complaint (#122) in *Lampkin v. UBS PaineWebber Inc.* (Lampkin #167) at p. 10, n.5. "Although there appears to be no federal appellate case on point in which the elements of a joint venture under federal common law are spelled out, 'different jurisdictions generally adopt the same criteria for the establishment of a joint venture.'" *Trans-Tec Asia v. M/V*

by operation of law; rather, parties create a joint venture as a factual matter by express or implied agreement. *See Sheppard v. Carey*, 254 A.2d 260, 263 (Del. Ch. 1969). The existence of a written agreement is not necessary to prove the existence of a joint venture, as "no particular formality is required for the establishment of such a relationship." *Consolidated Fisheries Co. v. Consolidated Solubles*, 112 A.2d 30, 35, supp. op., 113 A.2d 576 (Del. Ch. 1955). While agreement between the parties is key to establishing a joint venture, the facts and circumstances [16] may demonstrate that the parties, *as a matter of fact,* created a joint venture relationship. *See Sheppard,* 254 A.2d at 263.

32. Twenty-five years after recognizing a broad definition of the *de facto "*joint venture" concept, the Supreme Court of Delaware explained the elements of a joint venture by referring to the "generally recognized elements of a joint venture." *See Warren v. Goldinger Bros., Inc.*, 414 A.2d 507, 509 (Del. 1980). These elements include:

(1) a community of interest in the performance of a common purpose;

(2) joint control or right of control;

Harmony Container, 435 F.Supp.2d 1015, 1031 (C.D. Cal. 2005) (citing *United States v. USX Corp.*, 68 F.3d 811, 826 n.30 (3d Cir. 1995)). Texas law is no exception and its application would result in an essentially identical analysis. *See Ayco Dev. Corp. v. G. E. T. Service Co.*, 616 S.W.2d 184, 186 (Tex. 1981) (citing elements of a joint venture under Texas law).

(3) a joint proprietary interest in the subject matter;

(4) a right to share in the profits; and

(5) a duty to share in the losses which may be sustained.

See id. (citing *Kilgore Seed Co. v. Lewin*, 141 So.2d 809 (Fla. Dist. Ct. App. 1962).

33. THE CONTRIBUTION OF THE PARTIES NEED NOT BE THE SAME; FOR EXAMPLE, ONE PARTY MAY CONTRIBUTE LAND, ANOTHER SKILL AND EXPERIENCE, AND THE THIRD CASH. *SEE CARMER*, 156 A.2D AT 502. ADDITIONALLY, THE LOSSES INCURRED BY THE PARTIES NEED NOT BE MONETARY LOSSES; THEY COULD, FOR EXAMPLE, BE AN EXPENDITURE OF TIME OR OUT-OF-POCKET EXPENSE. *SEE ID.*

34. The "UBS Group" describes itself as a global investment services firm that combines into a single "integrated group" the resources and expertise from all of its businesses.[3] This single "legal entity group structure of UBS is designed to support the Group's businesses within an efficient legal, tax, regulatory and funding framework."[4] UBS's stated purpose for the single group structure is to "optimize shareholder value [by] making the whole worth more than the sum of the

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[3] *See* UBS AG Form 20-F for year end 31 December 2001, Financial Report ("Financial Report") at pp. 3 and 83; *see also* UBS AG Form F-1 dated December 27, 2000, Prospectus ("Prospectus") at p. 12.

[4] Financial Report at p. 147.

parts."[5] The "UBS Group" is then operated through three Business Groups and a [17] Corporate Center.[6] The Business Groups and Corporate Center are not themselves registered legal entities, but rather function through the various registered legal entities that combine to make up the Group based on the requirements of the supervisory and regulatory regimes of the countries in which UBS operates.[7] In 2001, the Group consisted of in excess of 120 individual registered legal entities designated as "significant subsidiaries."[8]

35. The three Business Groups of the single "UBS Group" are UBS Switzerland, UBS Asset Management, and UBS Warburg, as shown in the diagram below.[9] The UBS Switzerland Business Group, which includes UBS AG, provides banking and securities services for individual and corporate clients in Switzerland.[10] The UBS Asset Management Business Group operates UBS's institutional asset management and

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[5] UBS AG Form 20-F for year end 31 December 2001, Handbook 2001/2002 ("Handbook") at p. 52.

[6] *See* Financial Report at p. 92. Plaintiffs note UBS has implemented various organizational changes since the end of relevant class period. For example, as recently as October 3, 2008 UBS announced that it is greatly reducing the size and its emphasis on the investment bank. The evidence discussed herein relates to the organizational structure existing during the Fraud Class Period.

[7] *See* Financial Report at p. 147 *and* Handbook at pp. 106 and 108.

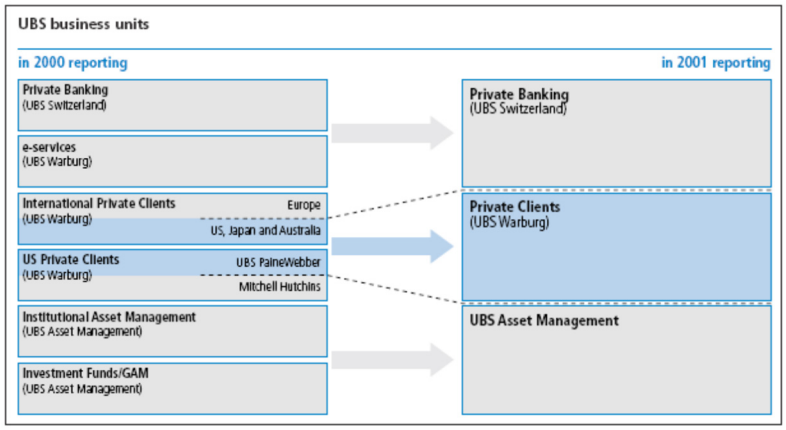
[8] *See* Financial Report at pp. 147-49.

[9] *See* Financial Report at pp. 4, 33, and 92; *see also,* Prospectus at p. 11.

[10] *See* Financial Report at pp. 4 and 92.

mutual fund provider business.[11] The UBS Warburg Business Group, which includes UBS PaineWebber, Inc. and UBS Warburg, LLC, operates as UBS's global securities, investment banking, and wealth management function.[12]

[18]



36. UBS's Corporate Center then coordinates the activities of the three Business Groups to ensure the Group functions as a coherent whole and in alignment with the UBS Group's overall goals, as shown in the following diagram:[13]

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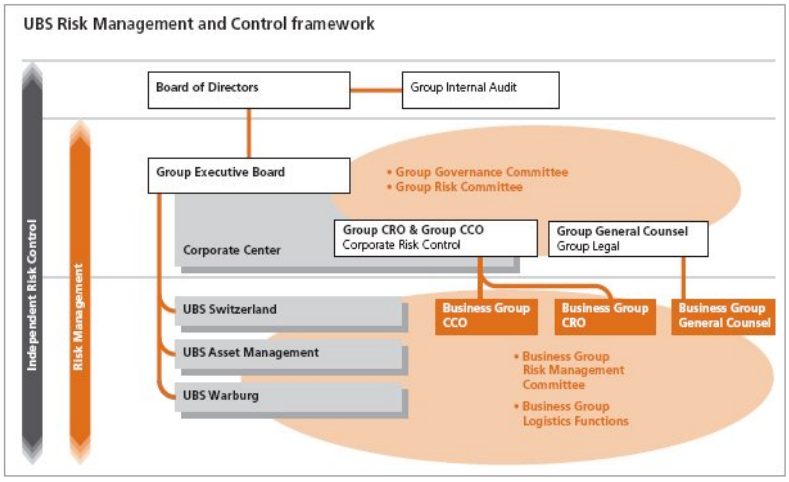
[11] *See id.*

[12] *See id.*

[13] *See id.; see also,* Handbook at p. 57.



The Corporate Center is responsible for such key functions as finance and risk management and [19] control (e.g., accounting, tax, treasury and risk management and control), controlling (financial control and accounting processes), communications and marketing (e.g., communication of strategy, values and results to employees, clients, investors, media and the public, and building the UBS brand worldwide), human resources (e.g., establishing standards, principles and procedures for performance evaluation, compensation and benefits, graduate and professional recruitment, training and development), and legal (e.g., managing UBS's legal affairs and coordinating the activities of Business Group legal departments).[14]

37. The business management responsibility for the Group venture is vested in the Group Executive Board ("GEB"), which includes the Chief Executive

[14] *See* Handbook at p. 52.

Officer of each Business Group.[15] The GEB is the Group's most senior executive body and assumes overall responsibility for the development of UBS's strategies.[16] The GEB is "responsible for the implementation and results of those strategies, for the alignment of the Business Groups to the UBS Group's integrated model and for the exploitation of synergies across the Group."[17] In other words, the GEB is the body of senior management that managed the day-to-day affairs of the UBS Group[18] The President of the GEB also assumes responsibility for the Group's business and financial planning, financial reporting, and the definition and supervision of risk control.[19] As a rule, the GEB meets at least once every month and additional meetings are held either as required or at the request of a member.[20] In 2001, the GEB included the following members:[21]

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[15] *See id.* at p. 88; *see also* Prospectus at p. 15.

[16] *See* Prospectus at p. 15.

[17] Handbook at p. 88; *see also* Prospectus at p. 15.

[18] *See* August 26, 2005 Deposition of Charles Christopher Glockler ("Glockler Deposition") at pp. 151-52.

[19] *See* Handbook at p. 88.

[20] *See* UBS AG Form 20-F for year end 31 December 2001, Organization Regulations of UBS AG ("Regulations") at p. 3.

[21] Handbook at p. 96.

[20] **The Group Executive Board**

The table below shows the membership of the Group Executive Board at 31 December 2001.

Name	Position held	Year of initial appointment to the GEB
Peter A. Wuffli	President	1998
John P. Costas	Chief Executive Officers, UBS Warburg	2001
Georges Gagnebin	Chief Executive Officer, UBS Private Banking	2000
Joseph J. Grano Jr.	Chairman and Chief Executive Officer, UBS PaineWebber	2001
Markus Granziol	Chairman, BUS Warburg	1999
Stephan Haering	Chief Executive Officer, UBS Switzerland	1998

> The business address of all members of the Group Executive Board is UBS AG, Bahnhofstrasse 45, Zurich, Switzerland. Peter Kurer, the Group General Counsel, is an ex-officio member of the Group Executive Board.

As the foregoing table reflects, Luqman Arnold, the President of the GEB during the Fraud Class Period, left the UBS Group in December 2001 and was replaced by Peter Wuffli.

38. In addition, the Group Management Board ("GMB") exists to help in the management of the Group venture.[22] The GMB usually consists of about thirty (30) to fifty (50) of the most senior managers from the Business Groups and Corporate Center who are not members of the GEB.[23] These individuals meet "at least once a year to discuss fundamental Group issues."[24] In 2001, the GMB included the following members:[25]

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[22] *See* Handbook at p. 89.

[23] *See id.* at 90; *see also*, November 9, 2005 Deposition of Ian Frank Drew ("Drew Deposition") at pp. 148-49.

[24] Drew Deposition at pp. 148-49.

[25] Handbook at p. 98.

[21] **Group Managing Board**

The following members belonged to the Group Managing Board as at 31 December 2001:

Colin Buchan	Senior Advisor, UBS Warburg
Crispian Collins	Vice Chairman, UBE Asset Management
Arthur Decurtins	Head of Asia, UBS Private Banking
Jeffrey J. Diermeier	Chief Investment Officer, UBS Asset Management
Regina A. Dolan	Chief Administrative Officer, UBS PaineWebber
Thomas K. Etcher	Head of IT, UBE Switzerland
John A. Fraser	Chief Executive Officer, UBS Asset Management
Robert Gillespie	Joint Global Head of Corporate Finance, UBS Warburg
Jürg Haller	Head of Risk Transformation and Capital Management, UBS Switzerland
Eugen Haltiner	Head of Corporate Clients, UBS Switzerland
Gabriel Herrera	Head of Europe, Middle East and Africa/Investment Funds, UBS Asset Management

Alan C. Hodson	Head of Equities, UBS Warburg
Peter Kurer	Group General Counsel
Benjamin F. Lenhardt, Jr.	Deputy Head of Business Management/Head of Americas, UBS Asset Management
Donald B Marron	Chairman UBS Americas (ex officio GMB member)
Urs. B. Rinderknecht	Group Mandates
Alain Robert	Head of Individual Clients, UBS Switzerland
Marcel Rohner	Chief Operating Officer, Deputy CEO, UBS Private Banking
Gian Pietro Rossetti	Head of Swiss Clients, UBS Private Banking
Hugo Schaub	Group Controller
Jean Francis Sierro	Head of Resources, UBS Switzerland
Robert H. Silver	Head of Operations, Technology, and Corporate Employee Financial Services, UBS PaineWebber
J. Richard Sipes	Joint Head of Europe, UBS Private Banking
Clive Standish	Chief Executive Officer Asia Pacific, UBS Warburg
Walter Stürzinger	Group Chief Risk Officer

Marco Suter	Group Chief Credit Officer
Mark B. Sutton	Head of US Private Clients, UBS PaineWebber
Rory Tanner	Joint Global Head of Corporate Finance, UBS Warburg
Raoul Weil	Joint Head of Europe, UBS Private Banking
Stephan Zimmermann	Head of Operations, UBS Switzerland

39. Beyond the GEB and the GMB, the UBS Group management structure also includes the Group Risk Committee ("GRC").[26] The GRC is a high-level committee which met monthly to approve policy and new risk frameworks.[27] Occasionally the GRC would also review very large transaction requests.[28] The members of the GRC include the CEO of the investment bank, the Group Chief Risk Officer, the Group Chief Financial Officer, the Group Chief Credit Officer, and the President of the GEB.[29]

40. Other Group management functions include: (i) the Loan Portfolio Management group, which monitored the Group's aggregate loan exposure and then

[26] *See* Drew Deposition at p. 83-84.

[27] *See* Drew Deposition at p. 83-84, 148.

[28] *See* Dew Deposition at p. 84.

[29] *See id.*

managed that risk;[30] (ii) the Business Review Group, a group of senior officers from across the UBS Group set up to [22] review unprofitable transaction requests and determine whether to approve the transaction based on existing or potential business with the client from other areas of the Group (e.g., UBS enters credit facilities not to make money on the loans, but as an accommodation to the client in hopes of making money on other Group products);[31] and (iii) the Market Risk Control group, which is responsible for setting Group limits according to various market sensitive measures to protect the Group's profit/loss statement from movements in credit spreads, interests [sic] rates, and other market forces.[32]

41. As well as managing the UBS Group as a single legal entity group structure, UBS reports to the world its "Group" financial results as "a single economic entity," thereby eliminating the effects of intra-group transactions.[33] For the purpose of monitoring the

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[30] *See* November 22, 2005 Deposition of Francesca Barnes ("Barnes Deposition") at pp. 13-14; *see also*, July 20, 2005 Deposition of David Alan Bawden ("Bawden Deposition") at p. 93.

[31] *See* Barnes Deposition at p. 172; *see also*, October 7, 2005 Deposition of Robert W. Casey ("Casey Deposition") at pp. 108-11, and August 19, 2005 Deposition of Timothy James Steele ("Steele Deposition") at pp. 47-48. *See* August 31, 2005 Deposition of Wendy Pearsall Field ("Field 30(b)(6) Deposition") at pp. 186-88 and Barnes Deposition at pp. 112-13 regarding the example provided.

[32] *See* September 15, 2005 Deposition of William Glass ("Glass Deposition") at pp. 51-53; *see also* October 20, 2005 Deposition of Christine M. Lee ("Lee Deposition") at p. 11.

[33] *See* Financial Report at p. 83.

Business Groups, however, Group-level reporting systems and policies are used to segment revenues and expenses between the Business Groups.[34] UBS admits that applying different rules would lead to the recognition of different profits and losses at the Business Group level, but would have no effect on the total Group profits.[35]

42. The Group employs revenue sharing agreements to allocate external customer revenues to Business Groups.[36] For example, if UBS's corporate finance department has a relationship with a client, equity risk management allocates fifty percent (50%) of its revenues from that client to the corporate finance department.[37] Similarly, inter-business unit charges are [23] recorded as reductions to expenses to the business unit providing the service (i.e., managed through accounting entries ultimately eliminated in Group results),[38] although at times business units within the Group provide services to other business units within the Group without any allocation of expenses between the units.[39] Similarly, the business units share the costs of operating the Corporate Center.[40] Interestingly, the Group allocates equity to its business units

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[34] *See id.* at p. 13.

[35] *See id.*

[36] *See id.* at p. 32.

[37] *See* Lee Deposition at pp. 231-33.

[38] *See* Financial Report at p. 32.

[39] *See, e.g.*, June 30, 2005 Deposition of James W. Hunt ("Hunt Deposition") at pp. 326-28.

[40] *See* Financial Report at p. 32.

as is necessary to satisfy any applicable regulatory capital requirements, and any excess Group equity remains in the Corporate Center.[41] In short, everyone who works for the UBS Group shares in the profits and the losses from the transactions and engagements that any unit of the Group undertakes with a client, especially in that the Group's bonus pool is determined at the Group level and then divided up between its various business units for allocation to the Group's employees.[42]

43. The UBS Group's operation as a single joint venture between a number of legal entities including, *inter alia*, UBS AG, UBS Warburg, LLC, and UBS PaineWebber, Inc., is evident not only from the Group's reports to the public, but from the testimony of UBS Group employees. From the employees' point of view, legal entities within UBS are irrelevant with respect to their responsibilities or the function of the Group's business.[43] In fact, many UBS employees have little or no understanding of which specific legal entity within

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[41] *See id.*

[42] *See* November 8, 2005 Deposition of Suneel Kamlani ("Kamlani Deposition") at pp. 56-58.

[43] *See, e.g.*, Barnes Deposition at pp. 51-53; Bawden Deposition at pp. 21 and 62; July 21, 2005 Deposition of Wendy Pearsall Field ("Field Deposition") at pp. 29-30; November 2, 2005 Deposition of Paul A. Freilich ("Freilich Deposition") at p. 8; August 24, 2005 Deposition of Adam Eric Frieman ("Frieman Deposition") at pp. 22-28; Glass Deposition at pp. 11-12; September 2, 2005 Deposition of David Kelly ("Kelly Deposition") at pp. 25-27; and September 14, 2005 Deposition of Gary D. Riddell ("Riddell Deposition") at p. 8.

the UBS Group they or others work for.[44] What they do know is that UBS represents itself to its clients as a [24] global team with multiple functions.[45] As the UBS Group grew and as its relationships with its clients became more complex, Group management responded by having the corporate finance division direct the relationships and act as the coordinator of the business discussions between the UBS Group and its various clients.[46] To this end, UBS Group management even established liaisons between UBS Warburg and UBS PaineWebber to facilitate the communication of business leads from one to the other.[47] As one senior UBS credit officer frankly states, the UBS Group is simply a commonly managed "conglomerate of UBS entities."[48] Stated differently, all of the activities of any particular UBS entity are undertaken as part of the UBS Group, and the UBS Group is itself a distinct entity under the law – a joint venture of various UBS legal entities including UBS AG, UBS Warbrug, LLC, and UBS PaineWebber, Inc. – where each member is legally

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[44] *See, e.g.*, Barnes Deposition at pp. 51-52; Bawden Deposition at pp. 42-43; August 18, 2005 Deposition of Karsten Berlage ("Berlage Deposition") at pp. 7-8; September 16, 2005 Deposition of Kimberly A. Blue ("Blue Deposition") at pp. 5-6; Frieman Deposition at pp. 22-23; Glockler Deposition at p. 7; Riddell Deposition at pp. 7-8; and September 1, 2005 Deposition of Scott D. Whitney ("Whitney Deposition") at pp. 190-92.

[45] *See* Whitney Deposition at pp. 159-60.

[46] *See* Lee Deposition at pp. 60-62.

[47] *See* Berlage Deposition at pp. 65-67 and November 11, 2005 Deposition of V. Robert Fisher ("Fisher Deposition") at pp. 82-83.

[48] *See* Bawden Deposition at pp. 58-59.

responsible for the acts and omissions of the other members. *See Leber v. Universal Music & Video Distrib.*, 225 F. Supp. 2d 928, 937 (S.D. Il. [sic] 2002) (citing *Hudson v. A.C. & S. Co.*, 535 A.2d 1361, 1363 (Del. Super. Ct. 1987) (stating that each joint venturer is liable to third parties for the acts of other members of the joint venture within the scope of the joint venture and that an employee of the joint venture is an employee of each of the joint venturers)).

D. THE ROLE OF PAINEWEBBER IN THE "UBS GROUP"

44. As Plaintiffs' [sic] have repeatedly and consistently insisted throughout this case, their claims in this case are very different from every other Enron-related legal action brought concerning Enron's demise. Plaintiffs seek to represent every investor who purchased or acquired Enron equity, employee stock option, and preferred securities in a PW account, during [25] the class periods. The Fraud Class Period specifically begins with PW's integration into the "UBS Group" venture.

45. UBS's integration of PW's retail brokerage business, through which the UBS Group generated profits from its retail clients' trades in Enron securities, clearly establishes the UBS members as primary violators of Section 10(b)/Rule 10b-5 as to the Fraud Plaintiffs and those they seek to represent. The integration of PW's retail brokerage business into UBS

brought to the Group concrete duties of disclosure to a specific class of investors – its own retail clients with whom it had direct and special relationships. *See, e.g.*, *Thompson v. Smith Barney, Harris Upham & Co., Inc.*, 709 F.2d 1413, 1418 (11th Cir. 1983) (citing *Dupuy v. Dupuy*, 551 F.2d 1005, 1115 (5th Cir. 1977) for the proposition that "a broker owes a duty of full and fair disclosure to a securities investor"). By remaining silent while these retail clients, to whom the UBS joint venture now owed duties of disclosure, purchased Enron equity and preferred securities during the Fraud Class Period, UBS committed a primary violation of the antifraud provisions of the Securities Exchange Act. *See, e.g.*, *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972).

46. The 1934 Act contemplates that much of the regulation of broker-dealers like UBS will be conducted by quasi-governmental self-regulatory organizations ("SROs") consisting of securities exchanges and securities associations. *See, e.g.*, 15 U.S.C. §§ 78f, 78o-3, and 78s; *see also*, *DL Capital Group, LLC v. NASDAQ Stock Market, Inc.*, 409 F.3d 93, 95 (2nd Cir. 2005) and *Austin Mun. Sec., Inc. v. Nat'l Ass'n of Sec. Dealers, Inc.*, 757 F.2d 676, 692 (5th Cir. 1985). As outlined in the 2001 Annual Report of the Securities Exchange Commission ("SEC"), in the Fraud Class Period nine (9) active national securities exchanges existed, the largest of which was the New York Stock Exchange ("NYSE"). The National Association of Securities Dealers [26] ("NASD")

was the only national securities association.[49] The 1934 Act requires all national securities exchanges and national securities associations to establish rules designed to implement the securities laws by preventing fraudulent and manipulative acts and practices by their members and to promote just and equitable principles of trade. *See* 15 U.S.C. §§ 78f(b)(5) and 78o-3(b)(6). Before such rules become effective, the SEC must, after public notice and a period for comment, approve such rules. *See* 15 U.S.C. § 78s(b). Thus, the rules of the NASD and the NYSE establish obligatory standards to which all their members are held under the industry's unique self-regulatory scheme. *See Mihara v. Dean Witter & Co., Inc.*, 619 F.2d 814, 824 (9th Cir. 1980). Through the promulgation of these rules, the NASD and NYSE serve as "a critical aid to the SEC in implementing and effectuating compliance with the securities laws." *DL Capital Group, LLC*, 409 F.3d at 95. In fact, the recognized result of the industry's unique self-regulatory scheme is that "SROs effectively 'stand[ ] in the shoes of the SEC[.]' " *Id.* (quoting *D'Alessio v. New York Stock Exchange, Inc.*, 258 F.3d 93, 105 (2nd Cir. 2001)). UBS also recognizes this result in its own internal compliance manual and its December 2000 F-1 Registration statements, which identify the NYSE, NASD and the national exchanges as sharing the primary regulatory responsibility over the

[49] SEC 2001 Annual Report at p. 40, available at http://www.sec.gov/pdf/annrep01/ar01full.pdf. The "NASD" is now the Financial Industry Regulatory Authority ("FINRA").

securities industry.[50] The UBS Group's acquisition of retail brokerage clients thus made each Group member responsible for ensuring the Group complied with the disclosure obligations it had assumed. *See Hudson*, 535 A.2d at 1363.

47. Although the NASD and NYSE rules of conduct do not themselves specifically provide the basis of a legal action, courts universally recognize violations of NASD or NYSE rules as establishing the relevant standard of conduct required under Section 10(b) of the 1934 [27] Act, as implemented by SEC Rule 10b-5. *See, e.g.*, *GMS Group, L.L.C. v. Benderson*, 326 F.3d 75, 82 (2nd Cir. 2003); *see also Hoxworth v. Blinder, Robinson & Co., Inc.*, 903 F.2d 186, 200 (3rd Cir. 1990). The issue is not whether a violation of NASD or NYSE rules creates an independent cause of action. Rather, the issue is whether NASD or NYSE rules obligate UBS to act in a certain manner which, if violated, can form the basis of a deceptive act in violation of the federal securities laws.

48. Statutes and regulatory rules can impose affirmative duties on those subject to them, including an affirmative duty of disclosure. *See In re Geopharma, Inc. Sec. Litig.*, 399 F. Supp. 2d 432, 441 (S.D.N.Y. 2005); *see also* Louis Loss & Joel Seligman, FUNDAMENTALS OF SECURITIES REGULATION at p. 888 (4th ed. 2001). UBS recognizes the existence of such duties on it. Allen Meyers, the UBS head of compliance admitted in his testimony that during the class period UBS had the

[50] *See* UBS/LAM 038063-284.

"responsibility" and was "required to comply with NASD rules that appl[y] to it."[51]

49. A broker-dealer's clients are supposed to be able to rely for their protection on the duties placed upon the broker-dealer with whom they have a special relationship governed in part by the SRO rules. In the seminal case of *In re Duker & Duker*, the SEC stated: "Inherent in the relationship between a dealer and customer is the vital representation that the customer will be dealt with fairly and in accordance with the standards of the profession." 6 S.E.C. 386, 388 (1939). By 1943, the SEC's "shingle theory" attained approval by the courts, evidencing a broad consensus among authorities that the 1934 Act imposed inherent professional obligations upon broker-dealers. *See, e.g.*, *Charles Hughes & Co. v. SEC*, 139 F.2d 434 (2d Cir. 1943); *see also*, *Cooper v. Pac. Life Ins. Co.*, 229 F.R.D. 245, 253 (2nd Cir. 2005) (extending the shingle theory [28] notion that a broker-dealer implicitly represents to the world that the conduct of all its employees will be fair and meet professional norms to issuers of variable annuities).

50. NASD Rule 2210(d) mandates that:

> All member communications with the public shall be based on principles of fair dealing and good faith and should provide a sound basis for evaluating the facts in regard to any particular security or securities or type of

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[51] April 25, 2006 Deposition of Allen Meyers ("Meyers Deposition") at pp. 30-31.

security, industry discussed, or service offered. No material fact or qualification may be omitted if the omission, in the light of the context of the material presented, would cause the communications to be misleading.

NASD Rule IM 2310-2 mandates that:

Implicit in all member and registered representative relationships with customers and others is the fundamental responsibility for fair dealing. Sales efforts must therefore be undertaken only on a basis that can be judged as being within the ethical standards of the Association's Rules, with particular emphasis on the requirement to deal fairly with the public.

NYSE Rule 472 mandates that:

"Communications With The Public

General Standards for All Communications

(i) No member or member organization shall utilize any communication which contains (i) any untrue statement or omission of material fact or is otherwise false or misleading; or (ii) promises of specific results, exaggerated or unwarranted claims; or (iii) opinions for which there is no reasonable basis; or (iv) projections or forecasts of future events which are not clearly labeled as forecasts.

> Specific Standards for Communication (j)(1) Recommendations
>
> A recommendation (even though not labeled as a recommendation) must have a basis which can be substantiated as reasonable.
>
> When recommending the purchase, sale or switch of specific securities, supporting information must be provided or offered.
>
> [29] The market price at the time the recommendation is made must be indicated.

51. In short, NASD Rule 2210(d) places an affirmative duty on broker-dealers to ensure that every communication between it and its clients includes all the known material information relevant to the subject communication. NASD Rule 2310-2 and NYSE Rule 472 require fair dealing with candid, true communications. As a member of the NASD and NYSE, UBS had a duty to disclose to its retail clients all known material information concerning Enron anytime Enron was the subject of a communication, such as when purchase orders were placed or discussed, when research was published or disseminated, or when ratings on Enron securities were maintained by the Group. The long-standing principle of the "shingle theory" underscores the fact that this duty runs directly to the client, as opposed simply to the NASD and NYSE. UBS had an affirmative duty to disclose its knowledge concerning Enron's financial manipulations at the time its retail clients were placing orders to purchase Enron securities. UBS's failure to make the required disclosures is itself a deceptive act under Section 10(b)/Rule 10b-5.

52. Another fact distinguishing Plaintiffs' claims from every other Enron-related claim is the exclusive relationship between UBS and Enron at the retail brokerage level. When UBS acquired PW, UBS also acquired all the rights and obligations associated with PW's role as the exclusive administrator of Enron's employee stock option plans ("SOPs"). By letter agreement dated October 19, 1998, PW contracted to assume the administration and management of Enron's SOPs in exchange for the exclusive right to be the brokerage firm for all employee stock option exercises by Enron employees.[52] Through this role, UBS acquired an instant retail brokerage relationship with nearly every employee of Enron and its affiliate companies. UBS's [30] complete disregard for the interests of its retail clients is especially highlighted in the story of this subclass of plaintiffs in *Lampkin v. UBS Financial Services, Inc.*, who in addition to having significant concentrations of their investments tied to Enron, also had their salaries and retirements tied to Enron. The Option Plaintiffs' 1933 Act claims stem from this exclusive relationship between UBS and Enron.

[52] *See* UBS/LAM 038288-93.

VII. HISTORY OF ENRON[53]

53. Until the late fall of 2001, Fortune 500 Rankings placed Enron as the seventh largest corporation in the world based upon revenues. It grew from a traditional energy production and transmission company in the mid-1980s to a global enterprise. As such, it was an industry leader in the purchase, transportation, marketing, and sale of natural gas and electricity, and other energy sources and related financial instruments. Further, it spearheaded the development, construction, and operation of pipelines and various types of power facilities.

54. By the mid-1990s, Enron's business and business model had changed dramatically. Starting out as a company that had a concentration in natural gas pipelines, it became over time a company that

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[53] In this section, Plaintiffs highlight the elements of Enron's background key to understanding UBS's violations of Subsections (a) and (c) of Rule 10b-5 by utilizing the various reports filed by the Court-Appointed Examiners in the Enron Corp. bankruptcy proceedings. Without specific notation, the information in this section is taken directly from portions of one or more of these reports. Such reports are admissible in evidence under the "public records" exception to the hearsay rule, because they are court-authorized officers' reports of findings in a civil proceeding resulting from an investigation made pursuant to authority granted by law. *See* FED. R. EVID. 803(8); Order Pursuant to 11 U.S.C. §§ 1104(c) and 1106(b) Directing Appointment of Enron Corp. Examiner, Case No. 01-16034 (Bankr. S.D.N.Y. Apr. 8, 2002), as expanded by the Order Expanding the Duties of Harrison J. Goldin, The Court-Appointed Examiner in the Enron North America Corp. Bankruptcy Proceeding, to Include the Investigation of Certain Entities Involved in Transactions Pertaining to Special Purpose Entities, Case No. 01-16034 (Bankr. S.D.N.Y. June 2, 2003).

depended less on pipelines and transportation and more on energy trading and investing in new technologies and businesses. In its 2000 Annual Report, Enron described its four business segments as Wholesale Services, Energy Services, Broadband Services, and Transportation Services. Enron Wholesale was highlighted as its largest and [31] fastest growing business. Enron Wholesale created trading markets in gas, oil, electricity, and other energy produced and it provided price risk management and other related services as well. Enron Energy Services, Enron's retail arm, served users of energy in the commercial and industrial markets. Enron Broadband Services, newly minted in 2000, was in the "hot" telecommunications sector. Enron Transportation Services housed Enron's pipelines and Portland General.

55. Enron's rapid expansion into new businesses made it a voracious consumer of cash. Enron's management communicated to the investment community its awareness of the issues posed by its expansion and gave assurances that Enron could manage its way through these risks without upsetting investor expectations. Enron considered its credit ratings critical to this success. As recognized in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" ("MD&A") section of Enron's 1999 Annual Report, Enron's maintenance of its investment grade status was critical to the continued operation of its wholesale business as well as its ability to maintain adequate liquidity.

56. By 1999, Enron Wholesale was by far the most significant of Enron's business segments, accounting for 66% of its 1999 income before interest, minority interests and income taxes ("IBIT"). In order to continue the growth of this business, Enron needed to trade with other market participants without being required to post collateral. Thus, the continued success of Enron's entire business depended upon the continued success of Enron Wholesale, which was in turn dependent upon Enron's credit ratings for its senior unsecured long-term debt.

57. The credit rating depended on achieving certain financial ratios. The five key credit ratios consisted of: (i) funds flow interest coverage; (ii) pre-tax interest coverage; (iii) funds flow from operations to total obligations; (iv) total obligations to total obligations plus [32] shareholders' equity and certain other items; and (v) debt to total capital. Enron identified the components in its 2000 Annual Report as follows:

- *Funds flow from operations*, defined as net cash provided by operating activities (from the cash flow statement) less cash provided from decreases in working capital (or plus cash used for increases in working capital);
- *Balance Sheet Debt*, defined as short-term and long-term debt appearing on the face of the balance sheet;
- *Total Obligations*, defined as Balance Sheet Debt, plus guarantees of debt of third parties and guarantees of lease residual values, plus any excess of price risk management

liabilities over price risk management assets. Guaranteed debt was reduced by the value Enron attributed to the assets supporting the underlying debt. Debt of unconsolidated equity affiliates was not included because (unless guaranteed) it was non-recourse to Enron;

- *Shareholders' Equity and certain other items*, defined as shareholders' equity, plus the mezzanine items, minority interests and company-obligated preferred securities of subsidiaries;
- *Adjusted Earnings for credit analysis*, defined as IBIT, less gain on sale of non-merchant assets and the excess of earnings from equity method of investees over distributions from those investees, plus impairment losses; and
- *Interest Expense*, defined as interest incurred, less interest capitalized, plus estimated lease interest expense.

58. In the autumn of 2001, Enron made a series of financial disclosures and restatements of its financial statements pertaining in large part to certain related party transactions. These disclosures, in turn, triggered a chain of events culminating in Enron's unprecedented bankruptcy filing. In an earnings release on October 16, 2001, Kenneth Lay ("Lay") announced, among other things, that Enron was taking "after-tax non-recurring charges" of $1.01 billion in the third quarter and a reduction in shareholder equity of $1.2 billion. These "non-recurring charges" resulted in a net loss for the third quarter of $618 million, compared to

reported new income of $404 million for the preceding quarter and $292 million for the third quarter of 2000. Although the earnings charge consisted of several components, one component, [33] and the entire charge to equity, related to Enron's early termination during the third quarter of certain structured finance arrangements with a "previously disclosed entity." The "previously disclosed entity" was LJM2 Co-Investment, L.P. ("LJM2"), a private investment limited partnership funded in December 1999. Andrew Fastow ("Fastow"), Enron's Chief Financial Officer, and Michael J. Kopper ("Kopper"), another Enron executive, ran LJM2. Kopper actually left Enron in order to run LJM2.

59. Several significant events followed these disclosures. On October 24, 2001, Enron announced its placement of Fastow on a leave of absence. On October 31, 2001, Enron announced that its Board of Directors formed a Special Investigative Committee to examine and recommend actions with respect to transactions between Enron and entities connected with related parties. Then, on November 8, 2001, Enron announced its intention to restate its financial statements for 1997 through 2000 and the first and second quarters of 2001 to reduce previously reported net income by an aggregate $586 million. Enron attributed the restatement to transactions involving three entities, one of which was LJM Cayman, L.P., an investment partnership whose general partner was an entity wholly owned by Fastow.

60. Enron filed its third quarter 10-Q, including interim financial statements, on November 19, 2001,

giving effect to the previously announced "non-recurring charges" and restatement of prior financial statements. In addition, Enron reported in its third quarter 2001 balance sheet total debt under generally accepted accounting principles ("GAAP") of $12.978 billion. Also on November 19, 2001, senior Enron executives met with certain of Enron's banks, including UBS, at the Waldorf Astoria hotel in New York City. At the presentation, Jeff McMahon ("McMahon"), the Enron executive selected to replace Fastow as CFO, identified a series of bad investments as the first cause of Enron's problems. The investments he listed were [34] Azurix, Broadband, Elektro, Dabhol, and certain merchant investments. Enron's merchant investments were composed of the capital that it provided, generally, to energy and technology businesses seeking debt or equity. Enron's poor investment decisions resulted in the need for cash to fund the investments and the need to avoid losses if the investments did not work. Enron was reluctant to issue equity to address its need for cash for fear of an adverse effect on its credit ratings. Enron's use of mark-to-market ("MTM") accounting accentuated the tension between cash demands and credit ratings by creating a large gap between net income and funds flow from operations.[54] This "quality of

[54] On June 11, 1991, Enron wrote to the SEC Office of Chief Accountant to inform the SEC that Enron intended to use mark to market (MTM) accounting for its gas trading business, Enron Gas Services. Under MTM accounting, assets are carried at their "fair value," based upon publicly quoted prices, or if there are none available, based upon management's estimate using the best information available to determine the fair value of the assets.

earnings" problem made it particularly challenging for Enron to raise cash without issuing equity while maintaining its credit rating.

VIII. ENRON'S MATERIALLY MISLEADING FINANICALS

A. BACKGROUND

61. Given Enron's sudden bankruptcy followed by years of investigations, plea bargains, and criminal trials, that fraud pervaded Enron at least from

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Changes in values from quarter-to-quarter are recorded as gains or losses in the income statement.

By letter dated January 30, 1992, the SEC Chief Accountant, Walter P. Schuetze, informed Enron that, based upon Enron's representations, the SEC accounting staff would not object to Enron's use of MTM accounting for its natural gas trading activities beginning in 1992. Ultimately, MTM accounting spread throughout Enron. The seeds for financial engineering were sown in 1997, when Enron determined that it should use MTM accounting for its "merchant investments." Enron analogized what it called its "merchant bank activities" to those of venture capital investment companies, which are permitted to use MTM accounting under GAAP. Through MTM accounting, Enron often recognized earnings long before its activities generated any cash. Analysts took notice of Enron's acceleration of earnings through MTM accounting, which led to a "quality of earnings" issue for Enron. By the end of 1999, Enron's quality of earnings problem – the gap between income and actual funds flow from operations – was a serious problem affecting Enron's liquidity.

As of December 31, 2000, approximately $22.8 billion of Enron's assets were accounted for using MTM accounting. The MTM accounting assets represented 35% of its $65.5 billion of total assets. A mere 5% fluctuation in value of these assets would have resulted in gain or loss of $1.1 billion, an amount greater than Enron's 2000 net income of $979 million.

1999-2001 is now a generally uncontested historical fact. Even UBS's own expert witness, securities analyst Patricia [35] Chadwick, admits "[w]ith the benefit of hindsight, we know that [Enron's] [financial] statements were fraudulent."[55] In fact, none of UBS's designated experts deny that Enron's financial statements during the class periods were misleading and UBS itself admits that "Enron's financial statements for the years ended December 31, 1997 through 2000 and the quarters ended March 31 and June 30, 2001 were materially inaccurate[.]"[56] For all the complexities of the transactions structured to manipulate the public financial appearance of Enron, the fundamentals of Enron's fraud are relatively straightforward. Enron's overall financial objective was to maximize its stock price, a goal dependant in part on Enron maintaining its investment grade credit rating due to the

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[55] *See* November 17, 2006 Deposition of Patricia Chadwick ("Chadwick Deposition") at p. 205. Ms. Chadwick's sworn testimony reiterates the position she took in her expert report, which recognizes as "established" the fact that Enron's 10-K filings "contained misleading and inaccurate information" and that discerning this fact was not possible "without access to non-public information." *See* July 17, 2006 Expert Report of Patricia W. Chadwick ("Chadwick Report") at ¶ 41.

[56] *See, e.g.*, October 5, 2006 Deposition of Sriprakash P. Kothari, Ph.D. ("Kothari Deposition") at pp. 213-15, October 26, 2006 Deposition of Guy F. Erb ("Erb Deposition") at pp. 261-64, March 1, 2007 Deposition of Keith R. Ugone, Ph.D. ("Ugone Deposition") at pp. 102-03, and November 2, 2006 Deposition of Christopher S. Beach at pp. 169-70; Responses and Objections of UBS Financial Services Inc. and UBS Securities LLC to Plaintiffs' First Set of Requests for Admissions at Response Nos. 74-83.

company's dependence on Enron Wholesale.[57] Enron focused on three key financial targets in order to further this objective. First, Enron wanted to be viewed as a growth stock in order to receive a higher valuation in the equity markets.[58] In order to be viewed as a growth stock, Enron needed to achieve an after-tax earnings-per-share growth rate between 15-20 percent.[59] Enron placed a high importance on generating earnings in order to meet this target.[60] Second, Enron adopted as its target the 40 percent debt/capital ratio the rating agencies established for companies rated BBB+ or its equivalent.[61] Consequently, Enron placed a high [36] importance on limiting the debt reported on its balance sheet in order to meet this target.[62] Third, to demonstrate to the ratings agencies its ability to manage the debt expense it did have, Enron wanted a funds flow from operations to interest expense ratio of about four.[63] Enron officers also believed that for every dollar of funds flow created, Enron could borrow seven more dollars.[64] For these reasons, Enron placed a high importance on generating funds flow from operations.

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[57] *See* October 23, 2006 Deposition of Andrew Stuart Fastow ("Fastow Deposition Vol. 1") at p. 84 and October 24, 2006 Deposition of Andrew Stuart Fastow ("Fastow Deposition Vol. 2") at pp. 555-56.

[58] *See* Fastow Deposition Vol. 1 at pp. 81-82.

[59] *See id.*

[60] *See id.*

[61] *See id.* at pp. 82-83.

[62] *See id.*

[63] *See id.* at p. 83.

[64] *See id.* at p. 123.

Enron's officers believed the company's failure to meet these targets would cause its stock price to decline.[65]

62. The fraud at Enron began because the financial results the company would have published just from its business operations were insufficient in order for Enron to meet its financial targets.[66] Instead of publishing those results, Enron's Global Finance Group and its banks structured and executed financial transactions with particular accounting effects to "fill the gaps" created by Enron's poor operational performance.[67] The three categories of recurring financial gaps at Enron related directly to Enron's key financial targets. First, Enron generally did not have enough funds flow from operations necessary to maintain its investment grade rating.[68] Second, Enron had too much debt on its balance sheet for investment grade rating purposes.[69] Third, there were a number of quarters and year-ends in which Enron did not have enough income through its regular operations to meet the investing public's expectations of earnings.[70] Enron had to correct these problems in order to remain a viable entity. Instead of correcting these problems through the improvement of its business operations, Enron's officers [37] chose to manipulate its balance sheet by

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[65] *See id.* at pp. 83-84.

[66] *See, e.g.*, *id.* at pp. 52, 74-76, 80, and 90-95.

[67] *See, e.g.*, *id.* at pp. 52-53, 75-76, 80, and 92-93.

[68] *See id.* at pp. 54-55.

[69] *See id.* at pp. 54-55, 66, and 167.

[70] *See id.* at pp. 54-55.

engaging in financial transactions structured to produce the accounting results Enron desired, and Enron's banks, including UBS, chose to help them.[71]

63. Fastow admits that the primary purpose of Enron's financial transactions was to cause the financial statements of Enron to look different to the outside world than they otherwise would have looked without doing those transactions.[72] In other words, these transactions were accounting-driven, substituted form for substance, and intended to "window dress" Enron's financial statements to make Enron appear to the public healthier financially than it actually was.[73] Enron executed a number of transactions in order to create the false public appearance it desired and basically relied on a small number of types of transactions to do so: financial prepay transactions, share trust transactions, FAS 125/140 asset sales, minority interest investments, and non-economic accounting hedges. Additionally, Enron at times provided undocumented oral assurances to its counterparties in order to entice the counterparty into a transaction documented without the assurances for reporting purposes.

64. Enron succeeded in creating a financial picture that misled the public.[74] As Fastow admits, Enron's public financial disclosures did not include

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[71] *See id.* at pp. 52-53, 75-76, 80, 89-90, 92-93, and 129-30.

[72] *See id.* at pp. 52-53, 89-90, and 129-30.

[73] *See id.* at pp. 92-93, 112-13, and 129-30.

[74] *See id.* at pp. 76 and 78; *See also*, Fastow Deposition Vol. 2 at pp. 451-52, 457, and 459-60.

information that was necessary for the public to understand how its transactions, as discussed further below, caused Enron to appear more successful economically than it really was.[75] Importantly, the factual determination of whether Enron's financial statements were misleading is not necessarily a question of whether the financial statements complied with Generally Accepted Accounting Principles ("GAAP"). Even one of UBS's own experts, S.P. Kothari, Ph.D., an accounting professor and the Head of the Department of Economics, Finance, and Accounting at the [38] Massachusetts Institute of Technology ("MIT"), admits that a company's financial statements may be misleading while not necessarily violating GAAP.[76] UBS's designated accounting expert, Christopher Beach, also recognizes this distinction.[77]

65. Enron's financial transactions, as a general rule, occurred at the end of reporting quarters or years-end.[78] As Enron approached the ends of quarters or years, Enron looked to complete financial transactions to fill the gap between the actual results from operations and what Enron wanted the outside world to see.[79] Fastow and other employees in the Global Finance Group, as part of an ongoing dialogue with UBS and Enron's other Tier I and Tier II banks (especially

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[75] *See* Fastow Deposition Vol. 1 at p. 76.

[76] *See* Kothari Deposition at pp. 216-218.

[77] *See* Beach Deposition at p. 28.

[78] *See* Fastow Deposition Vol. 1 at p. 74.

[79] *See id.*

those Tier II banks like UBS who wanted to move to Tier I status), informed these bankers of the importance Enron placed on meeting its financial targets and of its expectations that these banks would stand ready to participate in such transactions to solve Enron's financial reporting problems.[80] Enron used the carrot of investment banking fees to entice UBS and its other banks.[81] Enron's transactions were usually temporary fixes for Enron that required later amendments, extensions, and refinancing, which gave the banks another opportunity to help Enron solve the same problem again and again, getting paid fees by Enron all along the way.[82]

[39] **B. ENRON'S FINANCIAL TRANSACTIONS**

i. Prepays

66. In economic substance and by intention, financial prepays were loans that created the false

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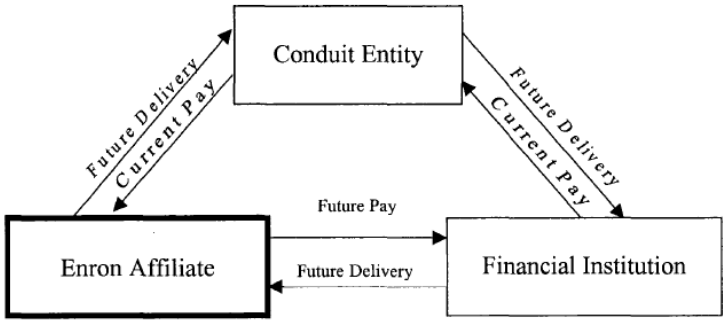
[80] *See id.* at pp. 24-25, and 74-76.

[81] *See id.* at pp. 45-46; *see also*, UBS/LAM 017053.

[82] *See* Fastow Deposition Vol. 2 at pp. 440-41. Hunt recognized that Enron's finance executives were also getting increased compensation from Enron for engaging in these transactions. In an August 2000 e-mail to UBS officer Tim Steele and copied to UBS officers Kimberly Blue, Scott Giese, Ken Crews, David Mikula, and Michael Davidson regarding the tabling of a particular transaction UBS proposed to Enron, Hunt explained that, unlike the transaction being tabled, Enron was prioritizing "the more imaginative transactions that generate income 'above the line'" because they count for more "in Enron's compensation scheme for the finance team[.]" UBS/LAM 522688-89.

appearance of funds flow from operations.[83] While the lending institution involved in a given prepay structure gave money to Enron with the expectation that it would be paid back the money in the future, the structure of the transaction made it look like Enron was receiving the cash from a normal business operation, e.g., an arms-length commodity trade.[84] The structure, shown below, was designed so as not to transfer the risks associated with a commodity trade to the other parties in the structure, and the financial institution took essentially the same risk associated with a traditional loan, i.e., Enron performance risk.[85]



Note: Entity in bold is wholly owned (directly or indirectly) by Enron.

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[83] *See* Fastow Deposition Vol. 1 at pp. 56-57, 60-61.

[84] *See id.*

[85] *See id.* at pp. 61-63.

67. If Enron had borrowed the money through a traditional financing, Enron would have had to report the money as funds flow from financing on its funds flow statement and as debt on its balance sheet.[86] Relying on the prepay structure, Enron reported the money as funds flow from operations and footnoted the associated liability as arising from its risk management activities.[87] Thus, in addition to overstating funds flow from operations and understating funds [40] flow from financing, the prepay transactions resulted in Enron underreporting its debt on its balance sheet.[88]

68. Fastow characterized the prepay transactions as "circular contrivances."[89] The transactions were circular because the risks involved in a commodities trade were transferred from party to party in the structure until they came back around to Enron.[90] The transactions were contrivances because they were all coordinated and executed simply to achieve a desired accounting result.[91] Enron used prepay transactions, such as the Yosemite IV/ECLNII prepay transaction discussed *infra*, to mislead and deceive the rating

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[86] *See id.* at 61-62.

[87] *See* Second Interim Report of Neal Batson, Court Appointed-Examiner ("Second Interim Report"), Appendix E at p. 2.

[88] *See* Fastow Deposition Vol. 1 at p. 65 and Fastow Deposition Vol. 2 at p. 344.

[89] *See* Fastow Deposition Vol. 2 at pp. 341-42.

[90] *See id.*

[91] *See id.*

agencies and the public about Enron's financial condition.[92] Enron's bankers, on the other hand, were informed by Fastow that Enron used the financial prepay transactions to report more funds flow from operations than Enron actually had.[93]

ii. Share Trusts

69. Share trusts such as Osprey were paper companies set up as Enron's "off balance sheet parking lot" or its "synthetic balance sheet."[94] Share trusts allowed Enron to borrow money but to keep it off of Enron's balance sheet.[95] Assets could be transferred to the share trust on a temporary basis until Enron could find a willing industry buyer for the asset.[96] This allowed Enron to generate cash from the transaction but to report the debt associated with those assets as the debt of an affiliate company instead of the debt of Enron.[97] Enron reported the cash generated from moving the assets from its balance sheet to the "warehouse" share trust as funds flow from operations.[98]

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[92] *See* Fastow Deposition Vol. 1 at p. 224 and Fastow Deposition Vol. 2 at p. 344.

[93] *See* Fastow Deposition Vol. 2 at pp. 344-45.

[94] *See* Fastow Deposition Vol. 1 at pp. 57-58.

[95] *See id.*

[96] *See id.*

[97] *See id.*

[98] *See* Fastow Deposition Vol. 2 at p. 535.

[41] 70. In each share trust transaction, Enron created a Delaware statutory business trust (the "Issuer") that sold notes and certificates of beneficial interest to the institutional private placement market.[99] The Issuer then contributed the proceeds from the sale of its securities to another entity (the "Holding Entity") and Enron (directly or through subsidiaries) contributed other assets to the Holding Entity.[100] The Holding Entity (i) used a portion of the cash received from the Issuer and the assets contributed by Enron to establish a reserve fund to support the payments on the Issuer's securities and (ii) used the remaining cash received to purchase assets or to repay existing financing.[101] The transactions were structured as follows:

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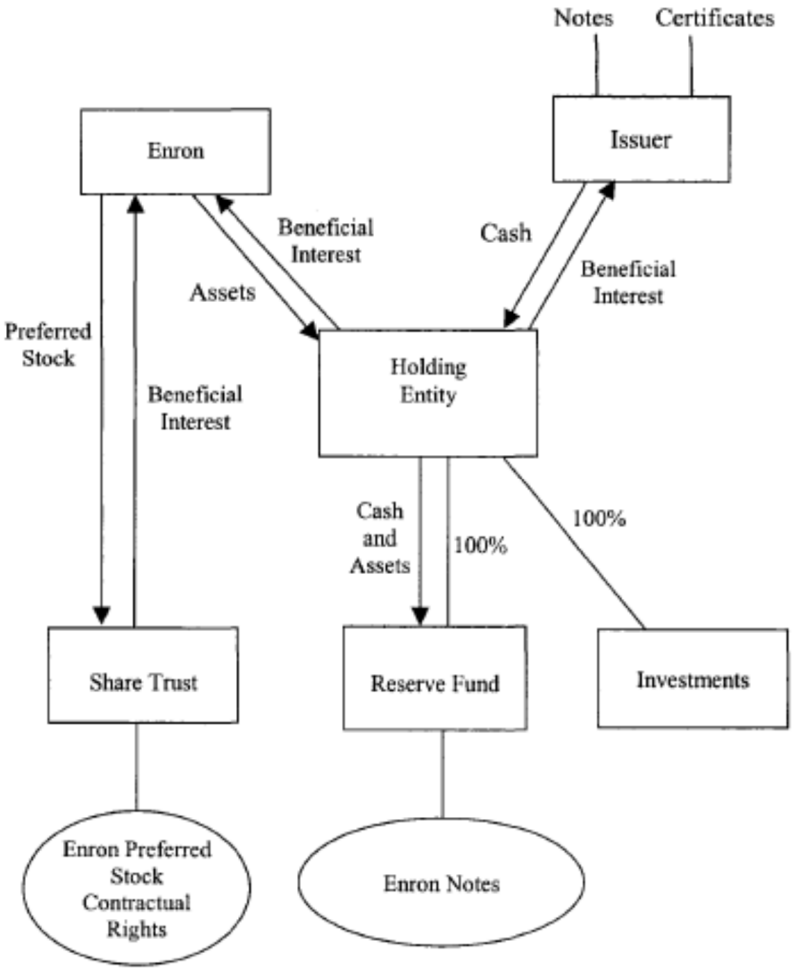
[99] *See* Second Interim Report at p. 68.

[100] *See id.*

[101] *See id.*



71. The anchor of Enron's share trust transactions was Enron's obligations with respect to its stock.[102] These obligations (collectively, the "Share Trust Obligations") consisted of the following:

[102] *See id.*

- Enron issued preferred stock to a trust (the "Share Trust");
- [42] Enron agreed to cause the Enron preferred stock (or Enron common stock into which the Enron preferred stock was convertible) to be sold in amounts sufficient to repay the Issuer's notes when due;
- In the event that the Enron stock in the Share Trust was not sufficient to generate the amounts necessary to repay the Issuer's notes, Enron agreed to issue additional shares that, when sold, would make up the shortfall; and
- If sufficient Enron shares could not be sold to raise the necessary funds, or Enron breached its obligations to issue and sell the Enron shares, Enron was obligated to provide the funds needed to repay the notes.[103]

72. The Issuer and the Holding Entity were not consolidated in Enron's financial statements.[104] As a result, Enron used these off-balance sheet structures to obtain financing based on Enron's stock and credit without reflecting the financing on Enron's consolidated balance sheet, to reduce the assets shown on Enron's consolidated balance sheet, and to achieve other financial reporting goals.[105]

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[103] *See id.* at 68-69.

[104] *See id.* at 69.

[105] *See id.*

iii. FAS 125/140

73. FAS 125/140 asset sales were, generally speaking, transactions where Enron sold an asset to a special purpose entity or related party for financial reporting purposes.[106] Enron reported funds flow from operations from these transactions and often reported earnings as well through gains realized in the "sale."[107] The transactions were intended to appear as if they were true sales to an unaffiliated arm's length third party, but the reality is that the transactions were done on a less than arm's length basis in order to generate earnings and funds flow for Enron.[108] The "sales" were typically temporary and, in a practical sense, Enron continued to control the assets.[109] Thus, the economic substance of these transactions were that they were secured loans, based on the following structure:

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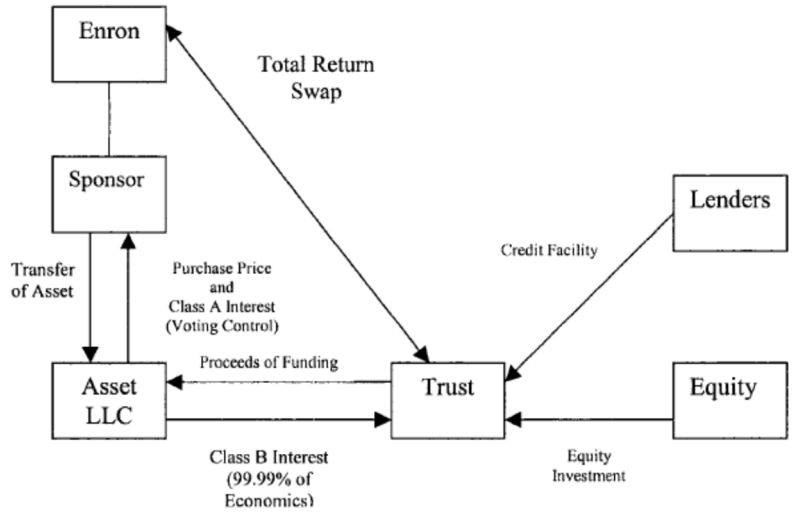
[106] *See* Fastow Deposition Vol. 1 at p. 58.

[107] *See id.* at pp. 58 and 232.

[108] *See id.* at pp. 58, 68, 72, 231-32 and Fastow Deposition Vol. 2 at pp. 463-64.

[109] *See* Fastow Deposition Vol. 1 at p. 233.



74. When Enron "monetized" an asset in a FAS 140/125 transaction, Enron agreed to make payments to its counterparty (usually a SPE created for the transaction or the lenders to the SPE) through a total return swap equal to the amount borrowed by the SPE under a credit facility.[110] The amount borrowed was roughly equal to the purchase price of the transferred asset.[111] Enron marked to market the total return swaps with the result that Enron, in fact, reported on its balance sheet, and in its income statement, the effects of subsequent decreases or increases in the value of the financed asset.[112] However, the reality was that the total return swap served as Enron's guarantee

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[110] *See* Second Interim Report at p. 109, *see also* Second Interim Report, Appendix M, at p. 7.

[111] *See id.*

[112] *See* Second Interim Report at p. 110, *see also* Second Interim Report, Appendix M, at p. 8.

of the amount borrowed by the SPE under the credit facility.[113] Enron incorporated the total return swaps in these structures in order to present the notional amount of the swap under price risk management and avoid footnote disclosure of Enron's obligation to repay the notional amount of the swap.[114]

[44] iv. Minority Interests

75. Enron used the minority interest structure to change what would otherwise be reported as debt into something that was reported as a minority interest, which was a class of equity on the balance sheet.[115] Minority interests were used to make Enron appear as if it had less debt than it truly had by converting balance sheet debt to minority interests for financial reporting purposes using the following type of structure:[116]

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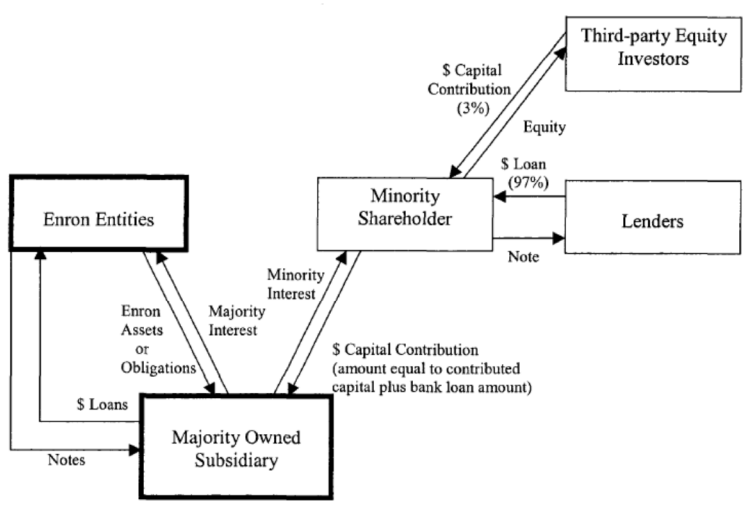
[113] *See* Second Interim Report, Appendix M, at p. 31-32.

[114] *See id.*

[115] *See* Fastow Deposition Vol. 1 at p. 65.

[116] *See id.* at pp. 65-66 and 70-71.



Note: Entities in bold included in Enron's consolidated financial statements.

76. In these financings, Enron or an affiliate formed a majority owned subsidiary (a "Majority Owned Subsidiary") that Enron consolidated for financial accounting purposes. Another entity owned the minority interest in the Majority Owned Subsidiary (the "Minority Shareholder").[117] Enron did not consolidate the Minority Shareholder for financial accounting purposes.[118] This unconsolidated Minority Shareholder generally held no other assets other than the minority interest in the Majority Owned Subsidiary.[119] Of the amount contributed by the Minority Shareholder to the Majority Owned Subsidiary, the Minority Shareholder obtained 3% from funding that was characterized as

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[117] *See* Second Interim Report, Appendix I, at p. 3.

[118] *See id.*

[119] *See id.*

equity in the Minority Shareholder and it borrowed the [45] remaining 97% from third-party lenders.[120] The Majority Owned Subsidiary, in turn, typically loaned the funds received from the Minority Shareholder to Enron or to other Enron-controlled entities that were also consolidated with Enron for financial accounting purposes, thus eliminating the intercompany loans in consolidation.[121]

v. Accounting Hedges

77. Enron used related parties to execute transactions designed to lock in the value of some of Enron's merchant investments for accounting purposes.[122] These accounting hedges, however, produced no economic benefit for Enron.[123] Enron used these transactions to address issues resulting from the nature of its assets and its method of accounting for them.[124] Enron carried its merchant investments at their fair values using the mark-to-market method of accounting.[125] As a result, changes in the values of these investments were reflected on Enron's balance sheet, and the net increases or decreases were reflected in Enron's income statement

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[120] *See id.* at pp. 3-4.

[121] *See id.* at p. 4

[122] *See* Fastow Deposition Vol. 1 at p. 199-201.

[123] *See id.* at pp. 203-04; *see also*, Second Interim Report, Appendix L, at p. 8.

[124] *See* Second Interim Report, Appendix L, at p. 7.

[125] *See id.*

as income or losses.[126] A portfolio of merchant investments whose values tended to decline would put downward pressure on Enron's earnings, so Enron designed the accounting hedges to solve the public reporting problem resulting from a combination of a volatile merchant investment portfolio and mark-to-market accounting.[127] With an accounting hedge in place, the net effect on Enron's balance sheet would be zero.[128] Additionally, the increase and decline would also offset each other on Enron's income statement.[129]

[46] vi. Oral Assurances

78. Finally, Enron executives often issued "oral assurances" to convey to its banks aspects of transactions that Enron could not document in order to receive a desired accounting treatment.[130] Enron's corporate culture developed in such a way that undocumented assurances became part of Enron's normal course of business.[131] Who from Enron actually made the oral assurance became merely the product a particular banker's level of comfort with the authority of the Enron employee to make the assurance.[132]

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[126] *See id.*

[127] *See id.* at pp. 7-8.

[128] *See id.* at p. 8; *see also*, Fastow Deposition Vol. 1 at pp. 201-02.

[129] *See* Second Interim Report, Appendix L, at p. 8.

[130] *See, e.g.*, Fastow Deposition Vol. 1 at pp. 135-36.

[131] *See* Fastow Deposition Vol. 2 at p. 349.

[132] *See id.* at p. 350.

IX. UBS KNEW ENRON USED THESE TYPES OF TRANSCATIONS TO MISSTATE ITS FINANCIAL PERFORMANCE

A. UBS/ENRON RELATIONSHIP

79. Both SBC and Union Bank dealt with Enron prior to their June 1998 merger.[133] Although Union Bank was reluctant to extend large amounts of credit to Enron due to a negative experience it had in the early 1980's with Enron's predecessor, Houston Natural Gas, Union Bank officers, led by Evans Swann ("Swann"), began meeting with Enron executives during 1997 to raise Union Bank's profile at Enron and attempted to create a greater level of institutional "comfort with the Enron 'story'" at Union Bank.[134] In late 1998, the new "UBS" sought to capitalize on the synergies of its merger by establishing a more comprehensive relationship with Enron.[135] On December 11, 1998, UBS executives met with Fastow to discuss the UBS/Enron relationship going forward.[136] Ken Crews ("Crews"), a UBS Vice-Chairman and its Global Head of the Power and Energy Corporate Finance Group, and Jim Hunt ("Hunt"), a Managing Director in the corporate finance department in UBS's Dallas, Texas office, [47] represented UBS at the meeting.[137] The

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[133] *See, e.g.*, UBS/LAM 055861-65, 059674-75.

[134] *See* UBS/LAM 055732, 055744, and 055761.

[135] *See* UBS/LAM 019321.

[136] *See id.*

[137] *See id.; see also,* Hunt Deposition at pp. 22-23.

meeting resulted in UBS's commitment to a relationship with Enron and the coordination of that relationship through the appointment of Hunt as UBS's "relationship banker" for Enron.[138]

80. It was well known within UBS and the banking industry in general at this time that Enron rewarded banks that provided credit capacity by paying exorbitant amounts of money in investment banking fees.[139] Crews and Hunt were informed going into the meeting by other UBS employees that Enron employees were "deal junkies" and that if UBS could "break into Enron's top tier banking group, [Enron was] known to take very good care of this group.[140] From 1998 forward, the Crews/Hunt team of executives at UBS's investment bank worked tirelessly to foster UBS's willingness to extend credit to Enron so UBS could then participate in capturing a portion of the more than $100 million in non-credit related investment banking dollars Enron paid annually.[141]

B. UBS KNOWLEDGE OF ENRON TRANSACTIONS

81. Fastow testified that he personally had many conversations with senior UBS officers, including Hunt and Swann, about the Enron financial reporting problems discussed above in paragraphs 61-65, as well as

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[138] *See* UBS/LAM 019321; *see also,* Hunt Deposition at pp. 20-22.

[139] *See* UBS/LAM 055744.

[140] UBS/LAM 018693-94.

[141] *See* UBS/LAM 167623-24.

about the various types of transactions Enron utilized to resolve those problems for financial reporting purposes.[142] Fastow also testified that other Enron officers had similar discussions with UBS officers.[143] Fastow's testimony by itself provides [48] competent evidence that UBS's senior officers knew Enron engaged in transactions in order to publicly report, and did report, its financial performance in a materially misleading way.[144] UBS's own documents and the testimony of UBS employees working on the Enron account then provide additional evidence to support the veracity of Fastow's testimony and the conclusion that UBS knew Enron publicly reported its financial results in a materially misleading way.

82. In fact, even as far back as June of 1997 old Union Bank credit officers noted in connection with a credit request that Enron clearly managed its earnings and used minority interest transactions to decrease its

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[142] *See* October 25, 2006 Deposition of Andrew Stuart Fastow "(Fastow Deposition Vol. 3") at pp. 849-52.

[143] *See id.* at 850. As an example, UBS officers Jim Hunt, Paul Jenison and Karsten Berlage met with Enron Energy Services' Chief Financial Officer, Cheryl Lipshutz, in February 2001 about her assignment to generate $225 million in revenues to fill in part a $400 million earnings gap. Lipschutz informed these UBS officers that these numbers were sent as preliminary "prepay" estimates that would need to be trued up later. The parties then discussed how EES could put contracts into Enron's Hawaii 1250, 1251, or 1252 "holding tank vehicles" in order to "pop earnings." *See* UBS/LAM 020354-59.

[144] Hunt describes his position at UBS in his 2000 Annual Review as "as senior as the firm has on oil and gas and service business." UBS/LAM 036473-75.

balance sheet leverage.[145] At this early date, these Union Bank officers knew that considering Enron's "material off-balance sheet obligations" would increase its balance sheet leverage to 70%.[146] The following demonstrates more particularly some of the objective evidence in this case that is consistent with the undeniable conclusion that high-ranking UBS officers from across the firm knew Enron engaged in transactions in order to publicly report its financial results in a materially misleading way.

i. Prepays (Yosemite III and Yosemite IV)

83. Enron used a prepay structure known as Yosemite to obtain what in economic substance were loans, despite the public characterization of the funds Enron received in these transactions as funds flow from operations.[147] UBS served as a joint lead manager in May of 2001 on the public issuance of notes whose proceeds funneled through the "Yosemite IV" [49] structure to Enron.[148] As the name implies, Enron had previously closed three versions of transactions similarly structured.[149]

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[145] *See* UBS/LAM 055765.

[146] *See* UBS/LAM 055766.

[147] *See* Second Interim Report at pp. 58-59.

[148] *See* UBS/LAM 155239; *see also,* Second Interim Report, Appendix E, at Annex 5.

[149] *See* Second Interim Report, Appendix E, at Annex 5.

84. Enron approached UBS regarding the transaction on April 10, 2001.[150] Fastow told Hunt that Enron instructed Salomon Smith Barney ("SSB") to include UBS as a co-lead on the transaction for "reasonable economics."[151] An announcement of the deal was expected on April 16th, which prompted UBS officer Karsten Berlage ("Berlage") to express his surprise that UBS, as a co-lead, was only presented with the draft offering memorandum a few days before.[152] UBS attempts to limit its involvement in the transaction to advising Enron with regard to various timing issues that arose, such as European holidays, and preparing a sales memorandum for UBS employees to use in soliciting investors.[153] But, UBS documents show UBS did not need time to understand the transaction, as its officers had already been working on the structure for over a year. UBS initially knew the "public" story that the Yosemite I and Yosemite II transactions were executed simply to free up credit capacity for Enron at other banks by having the trust purchase Enron's debt from these banks using the proceeds from the public issuance of notes.[154] UBS learned the true purpose of the structure, however, when Enron requested UBS's assistance in improving the structure.

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[150] *See* UBS/LAM 001656.

[151] *See* UBS/LAM 155226-27.

[152] *See id.*

[153] *See* UBS/LAM 155347; *see also,* Berlage Deposition at pp. 163, Whitney Deposition at p. 98.

[154] *See* UBS/LAM 519094, 169685, and 152133-65.

85. On February 14, 2000, Hunt e-mailed Corey Pinkston ("Pinkston"), Andrew Fishman ("Fishman"), John Convery ("Convery"), Jason Sweet ("Sweet"), Lyndon Taylor ("Taylor"), and Kimberly Blue ("Blue") to inform them that Enron executives Bill Brown, Doug McDowell, and Craig Clark would travel to UBS's New York office to discuss the Yosemite [50] structure.[155] This meeting took place on March 10, 2000.[156] UBS's presentation includes a basic review of the Yosemite I structure and then discusses UBS's considerations for a new Yosemite III structure.[157] Hunt's notes on the page of the presentation discussing the circular commodity forward contract portion of the structure evidence a discussion between the Enron executives and UBS officers in attendance that it "helps if [the SPV/Credit Bank] is a real co[mpany] that can take phys[ical] deliv[ery] . . . if it's a real co[mpany,] have to get [bankruptcy] remote (don't call it SPV)."[158] Hunt's notes also demonstrate that Enron's executives confirmed UBS's assumption that Enron needed to generate new money as part of the Yosemite III structure, not just to use the structure as a "synthetic vehicle" for banks to unload their Enron credit risk.[159]

86. During March 2000, Berlage continued work on structuring UBS's own version of the Yosemite

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[155] *See* UBS/LAM 519854.

[156] *See* UBS/LAM 018332-56.

[157] *See id.*

[158] *Id.*

[159] *See id.*

structure.[160] On April 4, 2000, Pinkston and Ron Yanagi ("Yanagi") exchanged e-mails, also copied to Mark Ritter, Berlage, and Convery, discussing specific structural issues relating to UBS's Yosemite III structure, including the need to design a "complete separation" of certain aspects of the structure in order to achieve the desired accounting treatment, how to eliminate from the structure basis risk through an interest rate swap, and UBS's progress in "tracking down" an "accomadative party" (sic) for the structure's third party.[161] On that same day, Pinkston wrote McDowell, copying Clark, Convery and Hunt, enclosing a draft of the termsheet and diagrams relating to Yosemite III.[162] Pinkston specifically notes that the document "incorporates an overall description of the entire transaction" and thus "should [51] probably be kept to a limited group."[163] These and other UBS presentation materials from this same time period all show the circular forward purchase/swap of a commodity that provided Enron with up-front cash ($750 million) without it or any other participant in the transaction taking on commodity price risk.[164] The circular structure would eliminate the commodity price risk and make the transaction, in substance and in form and as intended, nothing more than an undisclosed loan to Enron.[165]

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[160] *See* UBS/LAM 152127.

[161] *See* UBS/LAM 152244-46.

[162] *See* UBS/LAM 018292-314.

[163] *See id.*

[164] *See* UBS/LAM 152248-62.

[165] *See id.*

UBS's documents then show that in October 2000 UBS again presented its Yosemite III structure to Enron and discussed such structural considerations as using "substantially identical although completely separate" swap contracts and using pre-paid forward contracts and swap contracts with identical terms.[166] Apparently, even though UBS had already made several presentations to Enron on its "improved version" of the Yosemite structure involving amounts ranging between $500 million and $1 billion,[167] by October of 2000 UBS still had not yet determined its "appetite/ability to accept exposure" from participating in the swap counterparty role.[168]

87. With respect to the Yosemite IV transaction, Hunt's file contains notes from a conference call conducted the day before subscriptions in the May 2001 transaction were sold.[169] These notes confirm UBS was again informed about the true purpose of the transaction.[170] For example, Hunt noted the ultimate purpose of the transaction was to generate funds *for Enron* without increasing Enron's use of credit from banks,

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[166] *See* UBS/LAM 164013-43. Pinkston and Convery left UBS at some point in July 2000, but UBS officers Scott Giese and Tim Steele took over the modification of the Yosemite structure for Enron. *See* UBS/LAM 100981.

[167] *See* UBS/LAM 131996.

[168] *See* UBS/LAM 164034.

[169] *See* UBS/LAM 001656-57.

[170] *Compare, e.g.,* UBS/LAM 152248-62 *with* UBS/LAM 001657.

thereby preserving that capacity for new [52] use.[171] Additionally, Hunt's notes reflect that the underlying mechanics of the transaction were discussed, including the commodity forward contracts used to provide Enron with disguised loans from the transaction.[172] UBS documents also evidence Hunt's and Blue's participation in a concluding due diligence call the day after the subscriptions were sold.[173] Hunt noted that UBS avoided directly selling the notes to investors by specifically requesting all sale orders be funneled through SSB, although UBS did take credit for bringing in some new European investors.[174] Additionally, consistent with his involvement in engineering a UBS Yosemite-type structure, Berlage admitted in an e-mail to his colleague in late November 2001 that he advised Enron on the structuring of the Yosemite IV transaction.[175] In short, by the time of UBS's participation in the Yosemite IV transaction, UBS's own documents, including Hunt's handwritten notes, clearly show these officers knew that when stripped away from its form, the substance of the Yosemite prepay structure was nothing more than "direct [Enron] debt."[176]

88. UBS officers with documented knowledge of the Yosemite prepay structure from work on Yosemite III and/or Yosemite IV include: Karsten Berlage,

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[171] *See* UBS/LAM 001657.

[172] *See id.*

[173] *See* UBS/LAM 001658; *see also,* UBS/LAM 104332.

[174] *See* UBS/LAM 001658.

[175] *See* UBS/LAM 527342-47.

[176] *See* UBS/LAM 001657.

Kimberly Blue, John Convery, Ryan Donovan, Tom Field, Andrew Fishman, Scott Giese, Jim Hunt, Tom McErlean, Corey Pinkston, Mark Ritter, Tim Steele, Jason Sweet, Lyndon Taylor, and Scott Whitney.

ii. Share Trust (Whitewing/Osprey)

89. UBS participated as a co-manager in a follow-on offering of notes issued in connection with the Enron's Whitewing/Osprey structure in September/October of 2000.[177] In the Whitewing/Osprey transaction, Osprey was the Issuer, Whitewing Associates L.P. [53] ("Whitewing") was the Holding Entity, and the Condor Share Trust ("Condor") was the combined Share Trust and reserve fund.[178] One of UBS's initial analyses of Enron's Whitewing/Osprey structure was early in 2000 when UBS officers Hunt, Taylor, Tom Field ("T. Field") (non-officer), Pinkston, Fishman and Convery met with a number of Enron executives concerning another project.[179] A UBS presentation

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[177] *See* Blue Deposition at pp. 77-78.

[178] *See* Second Interim Report at p. 73.

[179] Hunt exchanged e-mails with other UBS officers on Friday, September 10, 1999 concerning Hunt's attempts to contact Enron executives and rumors that Enron was involved in a $1.4 billion off balance sheet, trust based structure. *See* UBS/LAM 518766. Hunt then disseminated within UBS a "Record of Business Call" documenting his Sunday, September 12, 1999 conference with Michael Kopper regarding the initial Osprey offering. *See* UBS/LAM 518780. UBS documents then evidence an analysis of the initial Osprey offering memorandum with handwritten notations concerning Enron's support of the structure through a share issuance requirement, the triggering of Enron's obligations

prepared for Enron discusses Enron's initial use of the Whitewing/Osprey structure, recognizing the purpose of the structure as allowing Enron to manage its merchant portfolio.[180] UBS characterized the structure as providing "non-recourse" financing to Enron, but noted that Enron maintained an ultimate obligation to repay the notes issued through the structure by the delivery of Enron equity shares.[181] Hunt's notes from a meeting between him, Enron executives, Corey Pinkston, John Convery, and Andrew Fishman in association with another transaction show that Enron explained to UBS how an Osprey default situation is ultimately a "cash '*put' back to* Enron."[182]

90. In a late August 2000 telephone conference between Ben Glisan, Enron's Treasurer and "friend" of UBS,[183] and UBS officers Hunt and Blue, Enron invited UBS to participate as an underwriter to the follow-on offering of notes issued through the Whitewing/Osprey structure.[184] Glisan explained to Hunt and Blue that Enron needed to complete this structured bond deal for year end balance sheet purposes and wanted UBS to [54] participate both (1) as an acknowledgment of the

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upon credit rating downgrade, and the resulting "snowball effect if stock [price] drops." *See* UBS/LAM 025194-212.

[180] *See* UBS/LAM 018510-47.

[181] *See* UBS/LAM 018520.

[182] *See* UBS/LAM 018497 (Emphasis in original).

[183] *See* UBS/LAM 520694.

[184] *See* UBS/LAM 001638-40.

work UBS had been doing for Enron and (2) to motivate UBS to work for Enron in the future.[185]

91. UBS admits that it did not conduct its own due diligence in connection with its role in the Whitewing/Osprey follow on offering, but instead relied upon due diligence carried out by Deutsche Bank Alex. Brown ("Deutsche") and Donaldson, Lufkin & Jenrette ("DLF").[186] UBS, however, entered into no agreements with, and received no documentation concerning the due diligence efforts of, the lead banks. This failure violates UBS's internal policy of creating an engagement letter clearly setting out the responsibilities of the parties in the due diligence for the transaction.[187] Further, a Deutsche representative testified that for UBS simply to rely on the due diligence conducted by it or DLJ would violate industry standards.[188] This Deutsche representative also confirmed that no agreement supporting UBS's alleged reliance on Deutsche or DLJ existed.[189]

92. Despite industry standards, UBS employees claim to have merely listened in on two conference

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[185] *See* UBS/LAM 001639.

[186] *See, e.g.*, Response Nos. 3-6, and 88 of Responses and Objections of UBS Financial Services Inc. and UBS Securities LLC to Plaintiffs' First Set of Request for Admissions; *see also*, Response Nos. 3 and 14 of Responses and Objections of UBS Financial Services Inc. and UBS Securities LLC to Plaintiffs' First Set of Interrogatories.

[187] *See* UBS/LAM 037330.

[188] *See* May 9, 2006 Deposition of David S. Bailey at p. 347.

[189] *See id.* at p. 350.

calls – an initial scheduling call and the final call before the issuance.[190] According to most UBS employees, UBS took three actions relating to the transaction: (1) it lent its name to the offering memorandum; (2) it marketed the notes to potential investors and forwarded orders for purchases of the notes; and (3) it accepted a $411,062.00 fee.[191] In fact, regarding the fee paid to UBS in connection with the transaction, UBS officer Berlage boasted to [55] a colleague, "Not too bad for preparing a sales memo and reading some documentation."[192] Berlage, however, "cannot recall" which documents he looked at, what sort of review of the transaction he undertook, or whether he did, in fact, undertake a review of the transaction at all, despite the fact that he was the UBS officer assigned to analyze the structure and present it to the UBS sales force via a sales memorandum.[193] Berlage does admit, though, that it would have made sense for him to analyze the prior Osprey securities offerings and assets put into the Whitewing/Osprey structure.[194]

93. UBS's willing admission that it failed to conduct reasonable due diligence seems convenient

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[190] *See, e.g.*, Response Nos. 3 and 14 of Responses and Objections of UBS Financial Services Inc. and UBS Securities LLC to Plaintiffs' First Set of Interrogatories; *see also*, UBS/LAM 101068 and Berlage Deposition at pp. 49-51.

[191] *See* Blue Deposition at pp. 77-78; Whitney Deposition at p. 185; *see also*, UBS/LAM 101522 and 152958.

[192] *See* UBS/LAM 152958.

[193] *See* Berlage Deposition at pp. 119, 126-27 and Whitney Deposition at p. 257.

[194] *See* Berlage Deposition at pp. 119-21.

considering the purpose for which Enron used the Whitewing/Osprey structure. In fact, UBS officers Hunt and Blue distance themselves from the responsibility for conducting due diligence on the Whitewing/Osprey structure by pointing the forger internally at the other's group as responsible for due diligence activities.[195] Whoever UBS charged with responsibility for due diligence, UBS internal policies demand that the firm only participate in any complex or unusual transactions after first forming a clear understanding of their economic and tax consequences.[196] Consistent with this mandate, testimony from the law firm hired by UBS and the other banks involved in the transaction to assist with due diligence indicates UBS did, in fact, participate in due diligence and was specifically aware of a decision to omit from the offering memorandum disclosures of how the structure would be used to purchase certain distressed assets from Enron in obvious non-arm's length transactions.[197]

[56] 94. By denying that UBS performed any due diligence on the project, UBS attempts to deny any knowledge regarding Enron's use of the Whitewing/Osprey structure. Thus, UBS attempts to deny knowing that Enron used the Whitewing/Osprey structure

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[195] *See, e.g.*, Report of Harrison J. Goldin, The Court-Appointed Bankruptcy Examiner in the Enron North America Corp. Bankruptcy Proceeding, Respecting His Investigation of the Role of Certain Entities in Transactions Pertaining to Special Purpose Entities ("SPE Report") at p. 190.

[196] *See* UBS/LAM 036920.

[197] *See* May 3, 2006 Deposition of Trayton M. Davis at pp. 27-28, 30-34, and 47-48.

to generate funds flow from operations by parking overvalued, non-performing assets in the structure and to keep the debt associated with those assets from appearing on Enron's balance sheet.[198] UBS's documents, though, demonstrate UBS officers had a clear understanding of the Whitewing/Osprey structure. Berlage, for example, prepared an internal presentation that he distributed in September 2000 to other UBS officers, part of which clearly presents the Whitewing/Osprey structure as a "hybrid structure."[199] Berlage then went on to put together a Whitewing/Osprey case study with the offering information, structure, and transaction rationale and encouraged UBS's officers throughout the world to market the structure, specifically followed up by a presentation of the structure to the UBS Global Power & Pipeline group.[200] All the while, Berlage knew from his analysis of the assets already in the structure and the removal of assets from the offering memorandum in this second

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[198] *See* Fastow Deposition Vol. 1 at pp. 57-58, 71 and Fastow Deposition Vol. 2 at p. 535.

[199] *See* UBS/LAM 153264-79.

[200] *See* UBS/LAM 153665; *see also* UBS/LAM 153690, UBS/LAM 153706, UBS/LAM 063450-57 Karsten Berlage e-mail dated October 10, 2000 to Michael Hynes, Tom McErlean, John Corcoran, Randi Nielson, Helen Clement, Steward Morel, Ray Leung, Karen Roth, Ken Crews, Jim Hunt, Jason Sweet, Stephen Arata, Tom Ming, Tom Field, James Brandi, Peter Delaney, Mark Mayer, Joseph Esteves, John McCall, David Mikula, Jorge Navarrete, John Sosnowski, Brian Sivy, John Colella, Philson Yim, Dave Harrison, Michael Kousaie, James Holland, Peter Shorthouse, Brian Ratner, Philippe Tappmoux, Anthony Cutcliffe, Marcus Elsum, and Dan Cook.

Osprey offering that Enron used its control over this structure to unload poor performing assets at inflated values. Hunt and Blue knew, from their conversation with Glisan, that Enron used its control over this structure to execute asset "sales" as needed for financial reporting purposes.[201]

[57] 95. UBS officers with documented knowledge of Enron's use of the Whitewing/Osprey structure as a warehouse for Enron assets include: Karsten Berlage, Kimberly Blue, and Jim Hunt.

iii. FAS 125/140 (Kahuna/Waimea)

96. E-mails and Hunt's notes concerning a proposed project named at different times Kahuna and Waimea support the conclusion that UBS officers knew of Enron's use of FAS 125/140 transactions to manage its financial reporting problems. Specifically, Hunt's notes of a meeting on January 20, 2000 between Enron Global Finance executives Doug McDowell and Craig Clark and UBS officers Hunt, Pinkston, Convery, and Fishman discuss, consistent with Fastow's characterization of Enron's financing transactions as temporary solutions to Enron's financial reporting problems, the consolidation and refinancing of a number of prior Enron financings.[202] As part of these discussions and in information sent in the weeks after of the meeting, Enron's Global Finance executives described for these

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[201] *See* UBS/LAM 001639.

[202] *See* UBS/LAM 018496-99; *see also*, UBS/LAM 519449-50.

UBS officers the need to refinance at least $1.47 billion in debt created by past Enron financings.[203] Many of the transactions were FAS 125/140 transactions used by Enron to book funds flow and earnings.[204] These UBS officers were informed, however, that these FAS 125/140 transactions were actually financings to "monetize" the amounts Enron had written up in the assets' values while allowing Enron to retain control over the assets.[205] Enron told UBS how its lenders received their return of principal and interest from Enron through the use of a total return swap.[206] Thus these lenders [58] only assumed Enron default risk, not interest rate risk or price risk.[207] In other words, because of the non-arms length nature of these transactions, as also described by Fastow in his testimony, these "true sales" were the equivalent of secured loans and Enron's executives told UBS's officers as much. These UBS officers were also told how Enron reported the total return swap as part of risk management activities instead of as debt on its balance sheet.[208] UBS and

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[203] *See id.*, UBS/LAM 018476-95, UBS/LAM 169320-21.

[204] *See* UBS/LAM 169320-21.

[205] *See* UBS/LAM 018496-99. In fact, in order for Enron to sell assets as part of Project Summer, discussed *infra*, Enron and UBS considered the steps necessary to unwind financing transactions whereby assets were purportedly transferred by Enron to vehicles like Condor, LJM, and Rawhide. *See, e.g.*, UBS/LAM 523385-98.

[206] *See* UBS/LAM 018496-99.

[207] *See, e.g.*, UBS/LAM 018478-82, UBS/LAM 169329-32, and UBS/LAM 018496-99.

[208] *See* UBS/LAM 018496-99.

Enron met over the next several months attempting to structure a packaged refinancing transaction that would eliminate the total return swap payments by Enron, but a final deal was never executed.[209]

97. UBS officers with documented knowledge of Enron's use of FAS 125/140 transactions through their work on Project Kahuna include: Karsten Berlage, Kimberly Blue, John Convery, Thomas Field, Andrew Fishman, Jim Hunt, Art Penn, Corey Pinkston, Jason Sweet, and Lyndon Taylor.

iv. Minority Interest (Rawhide)

98. Rawhide was a transaction Enron closed in late 1998 and introduced to Enron's banks for syndication early in 1999, just weeks after the important relationship meeting between Fastow, Hunt, and Crews. Rawhide was a minority interest transaction in which Enron was loaned $750 million dollars against $2.4 billion in merchant assets.[210] UBS officers regarded the deal as risky and complicated, but recognized Enron critically needed the transaction for balance sheet and rating agency creditability reasons.[211] UBS also regarded it as one of Fastow's pet projects that would be a test of UBS's "new team."[212] As UBS officer Douglas

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[209] *See* UBS/LAM 519854, UBS/LAM 519867, UBS/LAM 151921-50.

[210] *See* UBS/LAM 025131.

[211] *See* Casey Deposition at pp. 208-10; *see also,* UBS/LAM 132598-600 and UBS/LAM 208915-17.

[212] *See* UBS/LAM 132563-64.

Renfield-Miller informed other UBS officers on January 7, 1999 concerning his understanding of this [59] transaction, "like past Enron 'securitizations', [this] is mainly *disguised* Enron risk."[213] UBS's officer Robert Casey ("Casey") admits he understood at the time, which he communicated to others, that the transaction was so highly structured simply to accomplish the accounting result whereby a loan would be funneled to Enron while Enron treated the transaction as a tax deductible minority interest on its balance sheet.[214]

99. UBS turned down participation in the transaction and prepared a relatively detailed memorandum "to serve as a record of the review of the Rawhide transaction" focusing on regional exposure concentrations and firm policies.[215] However, Hunt acknowledges that even though UBS did not participate in the Rawhide transaction, through his own "intellectual curiosity" and "wisdom," and by speaking with others who had looked at other Enron transactions prior to Rawhide, he understood the structure as hiding what was nothing more than a direct loan to Enron.[216] In the spring of 2001, UBS officers Crews, Sal Giannetti, Gina Hubbell, Hunt, Gary Luciani, Art Penn, Kevin Reynolds, and Whit Williams reexamined the Rawhide structure for ideas in creating a similar structure

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[213] *See* UBS/LAM 132565. (Emphasis added).

[214] *See* Casey Deposition at pp. 208-10; *see also,* UBS/LAM 132598-600.

[215] *See* UBS/LAM 132643-45.

[216] *See* Hunt Deposition at pp. 91, 97; *see also* UBS/LAM 021629.

whereby Enron could generate $2 billion in "new" money from its international assets.[217]

100. UBS officers involved in the review and refusal to participate in Enron's minority interest transaction known as Rawhide in early 1999 include: Linda Bammann, Robert Casey, Larry Charleson, Karyn Conway, Ian Drew, Richard Ennis, Joseph Esteves, Lorenzo Gaggini, Eric Hanson, Jim Hunt, Scott James, Parker Knight, David Mikula, Bill Powell, Douglas Renfield-Miller, Bruce Richards, Jason Sweet, Erik Velastegui, and Robert Verna. Additionally, UBS officer Gary Luciani, the head of UBS's mezzanine department in 2001, was described by [60] Hunt in April 2001 when UBS sought to put together a Rawhide look-alike as "instrumental in doing Rawhide" for his prior employer.[218]

v. Accounting Hedges (1999 and 2000 Equity Forward Amendments)

101. In March 1998, Enron invested $10 million in the stock of Rhythms NetConnections, Inc. ("Rhythms"), a privately held Internet service provider, by purchasing 5.4 million shares of stock at $1.85 per share.[219] In April 1999, Rhythms went public at $21.00 per share.[220] By June 1999, Enron's investment in Rhythms was worth approximately $260 million, but a

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[217] *See* UBS/LAM 025150.

[218] *See* UBS/LAM 525433-35.

[219] *See* Second Interim Report, Appendix L, Annex 2 at p. 1.

[220] *See id.*

lock-up agreement prohibited Enron from selling its shares before the end of 1999.[221] Enron accounted for the investment as part of its merchant portfolio, meaning it would have to record the investment in its second quarter 1999 financial statements using mark-to-market accounting.[222] Unfortunately for Enron, while it would recognize earnings for the second quarter of 1999, Enron executives believed the market value of Rhythms would decrease significantly before Enron could sell the investment.[223] In other words, Enron believed its Rhythms investment would add losses to its income statement in subsequent quarters.[224]

102. Enron wanted to create a related party with whom Enron could execute a transaction whereby Enron could permanently lock in the gain on its Rhythms investment and avoid reporting publicly any subsequent losses.[225] Enron itself funded this related party and executed the desired transaction by forwarding to the related party the proceeds of an unrecorded [61] loan from UBS. UBS knew Enron's reason for requesting UBS's assistance and knew that Enron would not account for the value it transferred as a loan.

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[221] *See id.* at pp. 1-2; *see also*, Fastow Deposition Vol. 1 at pp. 202-03 and Fastow Deposition Vol. 3 at pp. 855-57.

[222] *See* Second Interim Report, Appendix L, Annex 2 at p. 1.; *see also,* Fastow Deposition Vol. 1 at p. 200 and Fastow Deposition Vol. 3 at pp. 855-57.

[223] *See* Fastow Deposition Vol. 1 at pp. 199-201 and Fastow Deposition Vol. 3 at pp. 855-57.

[224] *See id.*

[225] *See id.* at p. 199.

103. Prior to the merger between SBC and Union Bank, both banks entered into forward contracts with Enron on Enron's own stocks (herein called "SBC Forward Contracts" and "Union Bank Forward Contracts," respectively, or "Equity Forward Contracts," collectively).[226] The Equity Forward Contracts were financial instruments whereby, on a specific future date (the "Settlement Date"), Enron was contractually obligated to purchase from UBS, and UBS was contractually obligated to deliver to Enron, a specific number of Enron shares at a specific price (the "Forward Price").[227] The Equity Forward Contracts were derivative financial instruments in that the value of the contracts, but not their terms, fluctuated with the market price of Enron stock. If at any given time the market price of Enron stock was greater than the Forward Price of the Equity Forward Contracts, the contracts were "in the money" for Enron (i.e., UBS owed Enron value in excess of the value Enron owed UBS). If at any given time the market price of Enron stock was less than the Forward Price of the Equity Forward Contracts, the contracts were "out of the money" for Enron (i.e., Enron owed UBS value in excess of the value UBS owed Enron).

104. The Equity Forward Contracts could be settled in one of two ways.[228] The first settlement option

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[226] *See* UBS/LAM 017052-53; *see* also, EC04619A0070723-27, EC001513610-18, and EC001513622.

[227] *See* EC04619A0070723-27, EC001513610-18, and EC001513622.

[228] *See* UBS/LAM 056386-88; *see also,* EC04619A0070723-27, EC001513610-18, and EC001513622.

was to "physically settle" the contracts, meaning that UBS would deliver shares to Enron and Enron would deliver cash to UBS.[229] Another option was to "net share settle" the contracts.[230] If a contract was "net share settled" at a time when the contract was "in the money" for Enron, UBS would deliver to Enron the amount of shares necessary at the current [62] market price as equaled the net value of the contract to Enron.[231] If the contract was "out of the money" for Enron at the time it was "net share settled," Enron would deliver to UBS the amount of shares necessary at the current market price as equaled the net liability of Enron under the contract.[232]

105. After the merger of SBC and Union Bank, the Equity Forward Contracts covered over 7.8 million shares of Enron stock with Forward Prices of approximately $44.00 per share.[233] In May of 1999, Enron stock was trading around $74.00, thus the Equity Forward Contracts were "in the money" to Enron in excess of $230 million.[234] To hedge its obligations under the contract, UBS had purchased shares of Enron stock

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[229] *See* UBS/LAM 056386-88; *see also,* Frieman at pp. 102-03 and Lee Deposition at pp. 21-22.

[230] *See* UBS/LAM 056386-88.

[231] *See* EC04619A0070723-27, EC001513610-18; *see also*, Lee Deposition at pp. 21-22. If the Equity Forward Contracts were "net share settled," the equation would also take into account an underwriter discount. This discount is ignored for ease of explanation.

[232] *See* Lee Deposition at pp. 21-22.

[233] *See* UBS/LAM 017052-53 and UBS/LAM 095404.

[234] *See* UBS/LAM 095404.

when it entered into the contracts.[235] On May 17, 1999, Fastow approached Hunt with a proposition for UBS to make a loan to Enron using those hedge shares.[236]

106. Fastow asked UBS to reset the Forward Price of a portion of the Equity Forward Contract shares, to the "present" market value.[237] Then, Fastow asked UBS to assign, to a third party, its obligations as to the remaining number of shares subject to the Equity Forward Contracts, as well as that same number of Enron shares held by UBS as a hedge to the contracts.[238] The reset price would be calculated to achieve a constant notional amount of the contracts.[239] Fastow described the amendment, which Enron needed to complete by the end of [63] the quarter, as a "favor" he could use internally at Enron to get UBS investment banking business.[240]

107. UBS takes the position that by amending the Equity Forward Contracts, it simply satisfied its contractual obligation under the contracts.[241] UBS's position is that (1) Enron had the contractual right to terminate the Union Bank Forward Contract at any

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[235] *See* November 17, 2005 Deposition of Daniel B. Coleman ("Coleman Deposition") at pp. 78-79 and Frieman Deposition at pp. 58-60.

[236] *See* UBS/LAM 017052-53.

[237] *See id.*

[238] *See id.*

[239] *See id.*

[240] *See id.*

[241] *See* August 25, 2005 Deposition of Michael David Collins ("Collins Deposition") at pp. 79-80.

time;[242] (2) UBS acquiesced to the amendments; and (3) its acquiescence was purely an administrative task for the purpose of preserving the economics of the Equity Forward Contracts on its own books.[243] But, as is evident from the following, UBS knew Enron was manipulating its financial appearance by manufacturing a non-economic accounting hedge with an entity it controlled on an illiquid position Enron believed would create losses on its income statement and was doing it through a loan from UBS that Enron would not publicly disclose.[244]

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[242] Enron had the contractual right to terminate the Union Bank Forward Contract at any time. *See* EC001513610-18. If Enron terminated the Union Bank Forward Contract in June 1999, the result to Enron would be the receipt of Enron shares from UBS, a larger number of shares at an out-of-pocket cost if the contract was physically settled, or a lesser number of shares at no out-of-pocket cost if the contract was net share settled. There were two problems for Enron with physical settlement. First, Enron did not want to pay for the shares used to populate the SPV because that would "hurt [Enron's] funds flow ratio (for credit rating purposes)." UBS/LAM 017331; *see also,* UBS/LAM 004790.0009. Second, Enron's receipt of shares in settlement of the Union Bank Forward Contract would have a negative impact in that those shares would become regarded as treasury shares which could not be used by Enron for operational profit purposes due to GAAP prohibitions. *See* UBS/LAM 017331; *see also*, Collins Deposition at pp. 154-55. From UBS's perspective, termination of the contract meant UBS would lose $1 million in annual revenues associated with the settlement of half of the Union Bank Forward Contract. *See* UBS/LAM 058779.

[243] *See, e.g.*, Lee Deposition at p. 89.

[244] Hunt notes the loan aspect of the transaction by the fact that the "write up of forwards creates *value* in forwards wh[ich]

108. The driving force behind the amendments to the Equity Forward Contracts was to provide "seed" capital to an unconsolidated special purpose vehicle ("SPV") from which Enron could receive a derivative instrument designed to hedge its Rhythms investment.[245] This SPV ended up being LJM Cayman, L.P. ("LJM1"), controlled by Fastow and, by extension, Enron.[246] [64] Had Enron simply purchased the stock from UBS and provided it to LJM1, Enron could not use the derivative instrument received from LJM1 as a hedge.[247] UBS knew about and discussed this issue with Enron.[248] When a company reacquires its own stock, GAAP requires that the company either retire the stock or account for it as treasury stock.[249] Under both GAAP and the Internal Revenue Code, Enron would then be prohibited from recognizing gains or losses on the derivative instrument received in exchange for its own stock.[250] In order for the derivative instrument received from LJM1 to counteract as an accounting hedge against the movement in value in Enron's Rhythms investment, Enron had to be able to

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is equiva[lent] to [market] value of [stock] assigned to SPV." UBS/LAM 017333.

[245] *See* UBS/LAM 017331-37 and UBS-LAM 004790.0009-10.

[246] *See* UBS/LAM 052546-64.

[247] *See* UBS/LAM 017331.

[248] *See id.*; *see also*, Collins Deposition at pp. 154-55.

[249] *See* Beach Deposition at pp. 65-66.

[250] 26 U.S.C. § 1032(a): Nonrecognition of Gain or Loss – No gain or loss shall be recognized to a corporation on the receipt of money or other property in exchange for stock (including treasury stock) of such corporation.

recognize any gain or loss associated with the derivative instrument.[251] Consistent with Fastow's testimony that Enron discussed its problems with its banks and relied upon them to help Enron find solutions to these problems, Enron and UBS discussed this hurdle in connection with the restructuring of the Equity Forward Contracts and attempted to structure a transaction around it.[252]

109. On June 25, 1999, officers of UBS and Enron engaged in a conference call. Present on the call for UBS were Hunt, Michael Collins ("Collins"), Paul Freilich ("Freilich"), and David Kelly ("Kelly") (UBS in-house counsel).[253] Present on the call for Enron were Kopper and Glisan.[254] Also present on the call was Petrina Chandler, a lawyer from the Houston, Texas law firm of Vinson & Elkins, L.L.P.[255] Glisan characterized the purpose of the conference call as an opportunity for Enron to provide UBS with "full(er) disclosure" of Enron's [65] goals for the transaction.[256] Glisan explained to these UBS officers in more detail the future losses expected from the Rhythms investment.[257] The parties then discussed the prohibitions that would prevent Enron from recognizing a gain or loss on the derivative instrument if Enron received it in exchange for Enron's

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[251] *See* UBS/LAM 017331.

[252] *See* UBS/LAM 017331-37.

[253] *See id.*

[254] *See id.*

[255] *See id.*

[256] *See id.*

[257] *See id.*

issuance of stock.[258] UBS and Enron then devised a transaction that purports to change the substantive accounting treatment of Enron's "in-the-money" position in the Equity Forward Contracts.

110. The self-described "elegant solution" addressed two separate problems with gains in two separate assets: (1) Enron had a gain in its Rhythms investment that it could not protect because it was illiquid and accounted for by using MTM accounting; and (2) the Equity Forward Contracts had value in them that Enron could not account for or recognize as income because of the prohibitions of GAAP and Section 1032.[259] In the resulting transaction, UBS transferred Enron common stock with a current market value of approximately $275 million to LJM1 in exchange for Enron's agreement to embed approximately $150 million of value to UBS in the Equity Forward Contracts, as well as a "transaction fee" of $300,000.00.[260] LJM1 then provided Enron with a promissory note and, through a limited partnership, a derivative instrument hedging the Rhythms investment, these two assets also having a combined value of

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[258] *See id.*

[259] *See id.* Section 1032 also applies to gains in forward contracts and states, "No gain or loss shall be recognized by a corporation with respect to any lapse or acquisition of an option to buy or sell its stock (including treasury stock)."

[260] *See* UBS/LAM 052546-64 and UBS/LAM 106263.

approximately $150 million on the date of the transaction.[261]

[66] 111. UBS and Enron divided the SBC Forward Contract into two separate contracts and divided the Union Bank Forward Contract into two separate contracts.[262] The resulting "Amendments" constituted the effective contracts after June 30, 1999:[263]

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[261] *See* Second Interim Report, Appendix L, Annex 2 at pp. 9 and 12-13. At some point after June 30, 1999, the promissory note was amended to result in a total obligation to Enron by LJM of $64 million. This amendment appears subsequent to UBS's role in the transaction and thus is immaterial to an analysis of UBS's intentions with respect to the transaction. By way of explanation, however, Enron sought a fairness opinion from Price WatterhouseCoopers that the value of the Enron shares received by LJM1 was consistent with the value of the promissory note and derivative contract UBS received from LJM1. The fairness opinion received by Enron does not analyze the underlying transaction.

[262] *See* UBS/LAM 052546-64.

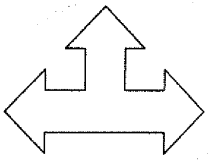
[263] *See id.*

Original SBC Contract[264]

No. of Shares: 1,099,773

Forward Price: $43.2714

Total Price: $47,588,714.00



SBC – Amendment A		**SBC – Amendment B**	
No. of Shares:	610,325	No. of Shares	489,448
Forward Price:	$79.8177	Forward Price:	$0.08882
Total Price:	$48,714,737.75	Total Price:	$43,472.77

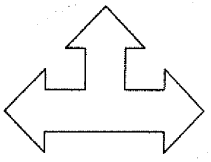
[264] The figures cited are taken from internal UBS documents submitted during the transaction review process. The calculations are incorrect in that the forward price as indicated in the contract was $44.0750, making the total notional value of the original SBC contract $48,472,494.98.

Union Bank Contract[265]

No. of Shares: 6,703,300

Forward Price: $44.6078

Total Price: $299,019,465.74



Union Bank – Amendment A		**Union Bank – Amendment B**	
No. of Shares:	3,815,051	No. of Shares	2,888,249
Forward Price:	$78.00	Forward Price:	$0.08882
Total Price:	$297,573,978.00	Total Price:	$256,534.28

[67] 112. UBS transferred to LJM1: (i) the shares covered by Amendment B to the SBC Forward Contract and Amendment B to the Union Bank Forward Contract, a total of 3,377,697 shares of Enron stock; as well as (ii) UBS's contractual rights and obligations under Amendment B to the SBC Forward Contract and Amendment B to the Union Bank Forward Contract.[266] The market price of Enron stock closed on June 29, 1999 at $81.186, making the value of the Enron stock transferred to LJM1 equal to $274,221,708.64. In

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[265] The Union Bank Forward Contract included a floating forward price that was reset on the 12th day of every month. The calculation of the forward price with a closing date of June 28, 1999 was $44.6078.

[266] *See id*.

exchange for the shares, UBS and Enron added $149,580,721.37 in cumulative value to portions of the amended contracts remaining with UBS.[267]

113. The transaction was memorialized through an Assignment and Assumption Agreement between UBS, Enron, and LJM1, as well as the written confirmations effecting the four amendments described above.[268] The Assignment and Assumption Agreement evidences UBS's transfer of shares to LJM1 and UBS's transfer of its rights and obligations under the Amendment B confirmations to LJM1.[269] This agreement also contains a "Tax Characterization" provision whereby UBS, Enron, and LJM1 all agreed that the "economic substance" of the transaction was "the purchase by Enron of the Assigned Shares by early settlement . . . with the purchase price paid for such shares being paid by means of a readjustment to the forward price that applies to the remaining underlying shares[.]"[270] This "Tax Characterization" provision creates a fiction in a number of ways.

114. First, the amendment did not result in a "settlement" of the original Forward Contracts because the same number of shares subject to those two contracts remained subject to the four contracts produced

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[267] *See id.* The value added is calculated as follows: (Δ SBC Forward Price x No. Shares covered by SBC Amendment A) + (Δ Union Bank Forward Price x No. Shares covered by Union Bank Amendment A).

[268] *See id.*

[269] *See id.*

[270] *Id.*

by the amendment.[271] Until the parties satisfy their respective obligations under the contracts, there is no settlement.[272] The documents on their face show that [68] no "early settlement" occurred with respect to the two original contracts.[273] The obligations created by the contract remained (though Enron's obligations increased) and LJM1 assumed some of UBS's obligations.[274] It is precisely because the amendments did not result in a settlement of the contracts that the restructuring was a loan.[275] UBS's transfer of Enron common stock through these amendments was the transfer of new value.[276] Enron's promise to pay (or forego) approximately $150 million in the future was a new promise.[277] Because the amendments did not settle any portion of the original contracts, but rather reflected a new promise by Enron in exchange for UBS's concurrent transfer of new value, the transaction can only be properly regarded and characterized as a loan.[278]

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[271] *Compare* EC04619A0070723-27, EC001513610-18 *with* UBS/LAM 052546-64; *see also,* Beach Deposition at p. 87.

[272] *See* Beach Deposition at p. 82.

[273] *See* EC04619A0070723-27, EC001513610-18 and UBS/LAM 052546-64; *see also,* Collins Deposition at pp. 205-08.

[274] *See id.*

[275] While the amount of the loan extended by UBS was fixed, the repayment amount of the loan was contingent upon the value of Enron's stock price at maturity.

[276] *Compare* EC04619A0070723-27, EC001513610-18 *with* UBS/LAM 052546-64; *see also,* UBS/LAM 017333.

[277] *See id.*

[278] *See, e.g.,* September 11, 2006 Deposition of A. Can Conway, CPA, FCPA, CFE, CFI ("Conway Deposition") at pp. 137-38.

115. Second, the statement in the "Tax Characterization" provision that *Enron* purchased the shares assigned to LJM1 is inconsistent with the Assignment and Assumption Agreement, which unambiguously states that "[UBS] hereby *sells, transfers and assigns to [LJM1]* all of its right, title and interest in and to the Assigned Shares."[279] Hunt's notes reflect UBS's knowledge of this inconsistency in the transaction documents.[280] However, UBS selling the shares directly to LJM1 was a necessary component of the argument to achieve a hedge against the Rhythms investment, a goal clearly not accomplished if *Enron* purchased the "Assigned Shares" and then transferred those treasury shares to LJM1.[281]

116. Not everyone at UBS was comfortable with this transaction.[282] Given the unprecedented nature of the transaction and the transfer of hundreds of millions of dollars in Enron stock to an offshore entity, a number of UBS officers analyzed the transaction, including [69] officers from UBS's trading group (Rob Morgan – head of the equity derivatives trading desk), equity risk management group (Chris Pohle – co-head of equity risk management group), risk group (Mark Wallace), legal group (David Kelly), tax group (Paul Freilich), accounting group (Mike Fehrman – chief accounting officer), compliance group (Bill Ferri), market

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[279] *See* UBS/LAM 052546-64.

[280] *See* UBS/LAM 001577-78.

[281] *See* UBS/LAM 017331-37.

[282] *See, e.g.*, UBS/LAM 017329 and 017337.

risk group (Steve Sreckovic), and credit group (Bob Verna).[283] Individuals both within UBS and Enron had concerns with the structure, especially with regard to the risk in the event of full disclosure.[284] Even the final approval received from UBS's control functions was reserved – "legal, acct & tax – have confirmed they're ok (not 100%, but) & will support transac[tion]."[285] The transaction closed and UBS scored "high profile points" with Enron and Fastow.[286]

117. Hunt's notes reflect that as a result of the "favor" Enron was now "teeing up some real deals" for UBS and Enron specifically set up a meeting with UBS to discuss its capabilities in structured finance.[287] Hunt, when e-mailing UBS officers William Powell and David Mikula in preparation for the meeting, characterized the "creative financing" in which UBS and Enron had engaged as follows:

> we (Chris Pohle's group) just completed a creative financing for Kopper, ***which on its face seemed to be a straight forward restructuring*** of a $350 million (notional) portfolio of forward stock purchase contracts. The restructuring enabled Enron to extract $260 million + in value from the forwards to capitalize a new business venture. (***There's more***

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[283] *See* 209246-47; *see also,* Collins Deposition at 79-80.

[284] *See* UBS/LAM 017329.

[285] UBS/LAM 017337.

[286] *See* UBS/LAM 106263 and UBS/LAM 209246-47.

[287] *See* UBS/LAM 017062 and UBS/LAM 001585.

> ***to the story*** which demonstrates the kind of creative thinking that Kopper's group does.)[288]

118. UBS officers involved in the June 1999 approval of the amendments to the Equity Forward Contracts include: Michael Collins, Karyn Conway, Sara Edmonston, Mike Fehrman, Bill Ferri, Paul Freilich, Rupert Hilmi, Jim Hunt, Scott James, David Kelly, Christine Lee, David [70] Lee, Michael Mchaffy, Rob Morgan, Chris Pohle, Steve Sreckovic, Bob Verna, John Wall, and Mark Wallace.

119. In March of 2000, Enron notified UBS that it again wished to amend the Equity Forward Contracts remaining at UBS for the same essential purpose as the 1999 amendments.[289] Before approving the transaction, Bob Verna ("Verna"), UBS's credit officer for Enron at the time, again wanted to run the amendments through UBS's internal control functions.[290] Collins, attempting to avoid this additional review of the transaction, quickly e-mailed Verna stating,

> Also in response to your legal, tax, and acct. issues, this is the exact same transaction we executed for [Enron] back in June. At that time we ha[d] everybody (legal, tax, acct, compliance, market risk, trading. . . .) signed off

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[288] UBS/LAM 001585. (Emphasis added).

[289] See UBS/LAM 095596. Shortly after the June 1999 amendment, Enron announced a stock split. As a result, the number of shares subject to the amended Equity Forward Contracts remaining at UBS doubled and the Forward Price was cut in half.

[290] *See* UBS/LAM 095620-21.

> on it. I would think that this means we don't need to go through this again.[291]

120. Collins emphasized the importance of the transaction to Enron from a reporting perspective by stating "this entire transaction must be done by the end of the month or my contact ends up in the 'lose her job' scenario."[292] Despite Collins' efforts, the transaction was reviewed. On March 24, 2000, Collins e-mailed the transaction review form to the larger group, including officers from UBS's trading group (Rob Morgan), equity risk management group (Adam Frieman), risk group (Mark Wallace), legal group (David Kelly), tax group (Chris Pinho), accounting group (Mike Fehrman), compliance group (Susan Agonis), market risk group (Joel Forbes), and credit group (Bob Verna).[293] Again Collins emphasized that the transaction needed to be completed within the week and that the "approval process should be fairly easy as we executed the identical transaction with Enron in June 1999."[294] As UBS's transaction approval form explained:[295]

> [71] [t]he only difference between the two transactions is that the 1999 restructuring involved assigning the forwards and stock to a Cayman Islands SPV where this transaction will be an assignment of forwards and stock to

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[291] *Id.*

[292] *Id.*

[293] *See* UBS/LAM 095646 and UBS/LAM 056877-79.

[294] UBS/LAM 095646.

[295] UBS/LAM 056877-79.

> a Delaware LLC . . . (the two members [being] wholly owned subs of Enron and the managing member [being] an investment fund which is a Delaware LP).

As per the transaction approval form, UBS also understood Enron's purpose for the transaction to be the same as in the June 1999 amendment.

> The LLC will then provide (i) some cash to ENE and (ii) derivative structures to ENE to hedge certain investments ENE has in US publicly traded stocks which otherwise cannot be economically hedged (thereby eliminating unwanted volatility in ENE's current earnings stream).[296]

121. In this same time period, UBS officers took specific note of Enron's exposure from its "sprawling trading business."[297] Collins discussed with Enron executive Anne Yeager ("Yeager") Enron's need to hedge its equity investments.[298] Yeager agreed and explained, as UBS already knew, that Enron historically hedged its positions internally from one subsidiary to another.[299] Collins recognized Enron could not produce effective, true hedges in this manner and "impressed upon Yeager the economics that are at stake by not hedging externally."[300]

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[296] *See id.*

[297] *See* UBS/LAM 123488-89.

[298] *See id.*

[299] *See id.*

[300] *Id.*

122. On March 27, 2000, Collins elevated his concerns to one of his bosses, Pohle, with his other boss, Adam Frieman ("Frieman"), and every other member of the equity risk management group being copied on the message.[301] Collins nevertheless continued his push to complete the April 2000 amendment and enable Enron to complete yet another accounting hedge. UBS, Enron, and Harrier (another Enron SPV) executed a near identical Assignment & Assumption Agreement dated April 18, 2000, also including a Tax Characterization provision [72] mischaracterizing the transaction as a settlement of the existing transactions.[302] The 2000 amendments contained the following terms:[303]

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[301] *See id.*; *see also*, UBS/LAM 052603-04.

[302] *See* UBS/LAM 052565-82.

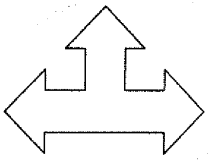
[303] Both the forward prices and the number shares subject to the contracts in the 2000 amendment reflect the noted stock split.

Original SBC Contract[304]

No. of Shares: 1,099,773

Forward Price: $40.7917

Total Price: $49,792,327.57



SBC – Amendment A		**SBC – Amendment B**	
No. of Shares:	706,274	No. of Shares	514,376
Forward Price:	$71.0499	Forward Price:	$0.080232
Total Price:	$50,180,697.07	Total Price:	$41,269.42

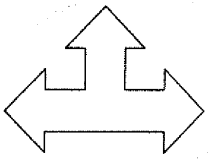
[304] The figures cited are taken from internal UBS documents submitted during the transaction review process. The figures are incorrect and should reflect a $50,101,457.19 total notional value of the original SBC contract at the forward price calculated by UBS.

1999 Amended Union Bank Contract[305]

No. of Shares: 7,630,102

Forward Price: $40.7038

Total Price: $310,573,887.00



Union Bank – Amendment A		**Union Bank – Amendment B**	
No. of Shares:	4,405,303	No. of Shares	3,224,799
Forward Price:	$70.50	Forward Price:	$0.080232
Total Price:	$310,573,861.50	Total Price:	$258,732.07

[73] 123. UBS transferred to Harrier 3,739,175 shares of Enron common stock.[306] The forward price of the contracts remaining with UBS were increased to add $112,106,553.82 of value.[307] On April 18, 2000, the effective date of the Assignment & Assumption Agreement, Enron stock closed at $68.00. Thus, the Enron shares received by Harrier were worth $254,263,900.00.

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[305] Per UBS calculation of forward price on April 24, 2000. The figures cited are taken from internal UBS documents submitted during the transaction review process. The figures are incorrect and should reflect a $310,574,145.79 total notional value of the original UBS contract at the forward price calculated by UBS.

[306] *See id.*

[307] *See id.*

124. UBS officers involved in the April 2000 review and approval of the amendments to the Equity Forward Contracts include: Susan Agonis, Roger Bieri, Michael Collins, Sara Edmonston, Michael Fehrman, Joel Forbes, Adam Frieman, Rupert Hilmi, Jim Hunt, David Kelly, Colin Kim, Christine Lee, Steve Lindgren, Robert Morgan, Chris Pinho, Robert Verna, Stephen Wade, and Mark Wallace.

125. Based upon the documents and explanations received from Enron, as described in detail above, a significant number of senior UBS officers from across the Group knew the 1999 and 2000 restructurings of the Equity Forward Contracts were for the purpose of creating hedges with the potential to create substantial accounting earnings for Enron while never translating into economic value for Enron. Logically and necessarily, then, UBS also knew these hedging transactions, which involved hundreds of millions of dollars, were illusory and executed simply to present a false appearance of Enron's financial situation. Additionally, UBS knew that it was loaning hundreds of millions of dollars to Enron to buy the Enron stock involved in these transactions and doing so in a manner in which Enron would not disclose the loan publicly.

vi. Oral Assurances (E-Next)

126. On March 20, 2001, Wendy Field ("W. Field"), an Executive Director in UBS's Investment Grade Loan Origination Group, and two other

individuals from UBS's credit [74] department, attended an "Enron one-on-one" session to discuss what UBS deemed a "structured 'secured' loan to Enron."[308] The subject project was a $600 million structured off-balance sheet construction facility named E-Next Generation LLC ("E-Next").[309] By using the E-Next facility, Enron sought to finance, off of its balance sheet, the construction of its US electric generating build out and then, once the construction was complete, bring the project onto Enron's balance sheet at a time when the project was generating revenues.[310] Enron made UBS aware of this intention in order to secure UBS's participation.[311]

127. The E-Next project was divided into three phases, on its face requiring a total seven (7) year loan commitment by UBS.[312] It was extremely important to structure the project in three phases because that was the only mechanism that could be used to keep the loan off of Enron's balance sheet.[313] Phase I consisted of acquiring the turbines and other ancillary equipment and beginning initial development activity.[314] In Phase II, Enron identified locations and constructed multiple

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[308] UBS/LAM 524995.

[309] *See* UBS/LAM 020276-88.

[310] *See id.*

[311] *See id.*; *see also*, UBS/LAM 128949-51.

[312] *See* UBS/LAM 020276-88.

[313] *See id.*

[314] *See id.*

gas-fired electric generating plants.[315] Phase III consisted simply of the operation of these plants.[316] Enron maintained an option to purchase the plants at the end of Phase II and assured UBS orally that the option would absolutely be exercised.[317] Additionally, Enron gave UBS and the other lenders a right to prevent Enron from proceeding into Phase III by forcing them to exercise the purchase option.[318] In UBS's Lending Commitments Committee Proposal for E-Next, W. Field summarized her understanding of the transaction as:

> [75] Phase III will never kick-in as this is NOT intended to be a project financing . . . To achieve off-balance sheet treatment, Enron needs to have the equipment and plans owned by another legal entity. Enron will have the right to purchase the equipment and facilities at the end of Phase II at the full cost of construction. Proceeds from the purchase will go to fully repay the loans associated with the cost of the project. ***It is Enron's intention to purchase every project at the end of Phase II . . . Thus, the entire Phase III mechanism is simply a structure which will allow off-balance sheet treatment for the debt and assets . . . [We] view the***

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[315] *See id.*

[316] *See id.*

[317] *See id.*; *see also*, UBS/LAM 128949-50.

[318] *See* UBS/LAM 020276-88.

> ***financing as 3-year senior secured Enron Corp. risk.***[319]

128. UBS credit officer Steve Landowne had the same understandings, as reflected in UBS's credit review of the transaction where he wrote:

> ***The financing is structured primarily to satisfy accounting rules . . . By having a structured deal the assets can remain off-balance sheet until project completion thus having no negative impact on [return on invested capital] . . .*** Even though the facility has a tenor of seven years, it is highly unlikely (and not intended) for it [to] extend past three years without amending the terms of the structure.[320]

129. Despite the risk associated with the form-over-substance structuring of the transaction, UBS knew the importance Enron placed on E-Next, as well as in UBS's participation in E-Next.[321] UBS initially requested to be excused from the E-Next transaction; however, Enron responded that E-Next was "critical" and that UBS was expected to commit to the facility and show its support.[322] Hunt emphasized to W. Field that she "cannot get a 'no' answer from credit" and later reminded her that she "must get approval" for the deal.[323] Hunt had reason to worry too. On April 9, 2001,

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[319] *Id*. (Emphasis added).

[320] *Id*. (Emphasis added).

[321] *See* UBS/LAM 025744-54.

[322] *See id.*

[323] *See* UBS/LAM 525000 and UBS/LAM 102198-99.

during the sequence of the E-Next approval process, Bill Glass ("Glass"), UBS's Head of North American Credit, attended a senior-level "CFI Risk Meeting" wherein Enron was individually identified as one of only three companies in the total [76] universe of UBS counterparties "we do not like."[324] Thus, when Glass approved UBS's participation in the E-Next loan facility the very next day, he specifically conditioned his approval on the requirement that UBS "sell down the position after closing."[325]

130. In addition to having the transaction reviewed and approved by UBS's Lending Commitment Committee and its Head of North American Credit, UBS had its in-house legal counsel review the transaction.[326] On April 19, 2001, UBS attorney Sandra Costin ("Costin") e-mailed W. Field with regard to a technical issue concerning Enron's guarantee of the E-Next project obligations and to note her conclusion that UBS's ability to prevent Enron from placing the assets into Phase III of the project is not "absolute."[327] W. Field responded to Costin's legal concerns in an e-mail to UBS officers Chris Glocker [sic] ("Glockler", UBS's newly appointed credit officer for Enron), and Richard Tavrow stating:

> As far as the latter point [of UBS's ability to block Phase III], again this is sort of a

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[324] *See* UBS/LAM 205365-67.

[325] UBS/LAM 138772.

[326] *See* UBS/LAM 128945-46.

[327] *See id.*

> business point. We did not look at this deal as a Project Financing and we have been more than vocal (to Enron and CSFB) about our ability to block a project entering Phase 3. Sandra's point is that in a legal sense we might not have a great leg to stand on if the economics of the project are "market" and they have met the rest of the conditions. ***Enron has stated that they will not put a project into phase 3. I have stated I will use everything in my power to prevent it. So were*** [sic] ***are we? I explained this in the approval process but I need your concurrence.***[328]

131. Ultimately, UBS received all the internal approvals necessary to participate in E-Next.[329] On April 26, 2001, UBS was informed that the Master Assignment and Assumption [77] Agreement for E-Next had been closed and the conditions precedent to funding had been met.[330] In other words, in the second quarter of 2001, UBS individually committed to issue Enron a loan in the amount of $20 million, and more generally knew that Enron was collectively being loaned $600 million, through a structure solely designed to allow Enron to keep the total loan off its balance sheet as a direct Enron obligation. From the outset, UBS knew the deal was "purely a structured 'secured' loan to Enron." The existence of this loan, the

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[328] UBS/LAM 128949-51. (Emphasis added).

[329] W. Field had to approach Glass three times in order to get his approval, but he did finally approve UBS's commitment to the project. *See* UBS/LAM 015867 and 138772.

[330] *See* UBS/LAM 139011.

necessary public disclosures regarding it, and the fact that Enron structured transactions coupled with undocumented oral assurances for the sole purpose of avoiding public disclosure, were material facts to investors, especially when considered in the context of the time and the larger universe of financial obligations to which Enron was then exposed.

132. The following UBS officers were involved in the review, approval and/or execution of the E-Next transaction: Kimberly Blue, Sandra Costin, Tom Field, Wendy Field, Bill Glass, Chris Glockler, Jim Hunt, Ed Kyritz, Steve Landowne, Dorothy McKinley, Gregory Raue, Richard Tavrow, and Bob Verna.

X. UBS ALSO KNEW MATERIAL, NON-PUBLIC INFORMATION CONCERNING "EMBEDDED LOSSES" IN ENRON'S ASSETS

133. In addition to having the operational problems highlighted above, Enron faced a dire situation during the Fraud Class Period relating to the value of its international assets. Enron publicly reported these assets at "book value," which was the value at which Enron purchased the assets.[331] However, the difference between the "book value" of these assets and the fair market value had grown such that, if Enron liquidated its assets, it would recognize material losses upon

[331] *See* Fastow Deposition Vol. 1 at p. 198 and Fastow Deposition Vol. 2 at p. 546.

disposition of the assets.[332] Fastow termed this difference the "embedded [78] losses" associated with the assets and in spring or early summer of 2001 when he took over the responsibility for Enron's corporate development.[333] Fastow believed the embedded losses in these assets to exceed $5 billion.[334] With Enron only "earning" about $1 billion a year, according to Fastow's testimony, it would have taken all of Enron's earnings for at least five (5) years simply to offset the losses on its portfolio of bad assets.[335] As Fastow acknowledged in his testimony, the market values of these assets, and thus the resulting embedded losses, were not matters of public knowledge during the Fraud Class Period.[336]

134. UBS, however, knew of these problems based on its work on a project in the summer of 2000. Known as "Project Summer" or "Enigma," a UBS team comprised of Crews, Hunt, Jason Sweet, James Sassoon, James Brennan, Stephen Arata, Tom Ming, T. Field, Taylor, Clinton Coleman, Kevin Knight, Sumeet Kanwar, and Omar Al-Salehi represented a group of Middle Eastern investors who considered buying all of Enron's international assets.[337] The transaction did not close, but many questions were raised by UBS regarding Enron's treatment of its international assets. In a memorandum dated June 21, 2000, UBS's "Desert

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[332] *See* Fastow Deposition Vol. 2 at pp. 448-50.

[333] *See id*. at pp. 447-50.

[334] *See id*. at p. 450.

[335] *See id.*

[336] *See id.* at pp. 546-47.

[337] *See* UBS/LAM 130414-17; *see also*, UBS/LAM 520660-61.

Lighting Team" posed the following questions to Enron regarding the accounting treatment for various assets analyzed in the project:

- "Why is the debt not consolidated if the rest of the project is?"
- "Several projects in which [Enron] has an ownership interest for US GAAP greater than 50% but appear to not be consolidated for US GAAP . . . Why is this the case?"
- "The US GAAP balance sheet and the project level balance sheet are quite different."[338]

[79] 135. UBS apparently received answers to these questions. In October 2000 Hunt and Brennan engaged in an interesting e-mail exchange in response to a request by CSFB, who represented Enron in the project, for UBS's execution of a confidentiality agreement regarding the various Enron businesses involved.[339] Hunt wrote Brennan saying that he did not think executing a confidentiality agreement on these asset packages was necessary because UBS would not be requesting more information on them.[340] Brennan responded back to his superior with the following:

> we need to be able to say that we have asked for and received all relevant info on these businesses, including updates to the data we

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[338] *See* UBS/LAM 522455-60.

[339] *See* UBS/LAM 524122-23.

[340] *See id.*

> received in June. Additionally, I imagine we need to have in our possession all brochures relevant to the assets we are purchasing – to ensure we know exactly what [Enron] has said about these assets (we would not want to find out down the road that certain liabilities had been disclosed in said brochures).[341]

The only logical inference from Brennan's statement is that he and Hunt, and presumably the rest of the UBS team of officers on the project, knew of "certain liabilities" associated with the assets that they did not expect Enron to disclose publicly.

136. Not only was Enron's treatment of the liabilities associated with these assets in question, Enron's valuation of these assets was also in question. One Enron executive working on this project commented that the asset values on Enron's books are "at best of little use, and at worst misleading, to outside investors. Many of the [book values] . . . have little or nothing to do with Enron's actual cash investment, market value, or any other investor-relevant markers."[342] On Hunt's copy of this document, he wrote in the column next to the foregoing statement that he [80] "couldn't agree more" and that, in light of this well

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[341] *Id.*

[342] *See* UBS/LAM 021851-53 David Haug June 29, 2000 InterOffice Memo to Jim Hunt, Joe Saddi, and Marty Klepper. Mr. Haug was Chairman and CEO of Enron Caribbean Basin, which managed all of Enron's business activities in the Caribbean and Central America, including Venezuela and Columbia, as well as Chairman and CEO of Enron's Middle East and global liquid natural gas businesses. *See* UBS/LAM 029365.

understood fact, the disclosed book values should be subject to "fair value adjustments."[343] Hunt then gave specific instructions to a UBS team member to address the definition of book value in the offering documents being prepared.[344]

137. Once Project Summer fell apart, Enron sought to raise still much needed cash by leveraging those assets in early 2001 through a project known at UBS as "Enigma II." UBS recognized that Enigma II constituted "a special assignment from the CEO and CFO . . . to raise as much [cash] as [Enron] can this quarter."[345] According to Hunt, the idea was to put together a transaction that would leverage Enron's international assets "to the limit" and pull out from them whatever cash they could, whether reasonable or unreasonable.[346] In this context, Coleman restated for the

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[343] *See* UBS/LAM 021852.

[344] *See* UBS/LAM 021839. Mr. Haug made the interesting observation that the document being prepared by UBS for potential investors was "full of disclaimers" to distance UBS from the information provided regarding Enron's assets and place any "blame" associated with the information on Enron and its management. *See* UBS/LAM 021833-36. For example, the July 18, 2000 Preliminary Information Memorandum, a draft of which was the subject of Mr. Haug comments, repeatedly informs the reader that the financial information contained in the document is "derived from information provided by Enron and by the Management of [Enron International;]" that Management was relied upon when creating the included projections; and that asset values are identified as the value reflected on the books of Enron and "may vary significantly from the actual net investment in such business by Enron." UBS/LAM 015690-808.

[345] UBS/LAM 525221.

[346] UBS/LAM 102216-17.

record that "the difference between book [earnings] and cash flow can sometimes be significant. Thus, the consolidated financials for the asset package do not tell the whole story."[347] Again, this observation directly relates to the actual value of Enron's international assets. In short, UBS had extensive exposure to Enron's assets and based on this exposure, confirmed by UBS's own admissions through notes and e-mails, UBS knew these assets exposed Enron to significant losses upon disposition to a truly independent counterparty.[348]

[81] 138. The valuation of Enron's international assets once again became an issue early in 2001 in connection with UBS's attempt to assist LJM, the Fastow-controlled investing entity disclosed in late 2001, to purchase Enron Wind. Specifically, the project numbers generated by UBS lower-level employees frustrated Hunt as being "too conservative."[349] UBS found itself wrestling with the purchase price assumption being used for the project considering the asset's "recent financial performance."[350] In other words, like Enron's other assets evaluated during Project Summer, UBS knew Enron's book value of the asset differed materially from the asset's current market value. A related issue with this potential asset acquisition was UBS's awareness of the "sensitivities" of the relationship

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[347] *Id.*

[348] *See id.* (Hunt noting the significant work UBS did with respect to these assets); *see also*, UBS/LAM 527317 (Hunt noting concerns of book losses kept Enron from selling assets).

[349] *See* UBS/LAM 525146.

[350] *See* UBS/LAM 525156-86.

between LJM and Enron.[351] In fact, Hunt made three specific disclaimers within one week to UBS officers Art Penn, Sal Giannetti, Gary Luciani, Simon Canning, and Crews that Fastow served as the general partner of the LJM fund.[352] Hunt's personal concerns with Enron, Fastow, and LJM were later confirmed when Enron began its dive into bankruptcy. In a candid mid-November 2001 e-mail exchange between Hunt and Omar Al-Salehi, the UBS officer in charge of the relationship with the Middle Eastern investors involved in Project Summer, Al-Salehi recalled how Hunt "never got comfortable . . . with Fastow and the set up when he looked at the wind assets."[353] Al-Salehi concluded that Hunt was "a good judge of character!"[354] Then, days before Enron's bankruptcy, Al-Salehi sent another e-mail to Hunt inquiring about his view on Enron's value.[355] Hunt responded with his "personal view . . . [82] developed with lots of personal experience" that it was "doubtful" Enron equity holders would receive anything by way of a bankruptcy trustee's sale of Enron's assets.[356]

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[351] *See id.*

[352] *See* UBS/LAM 525002, 525140, 525145.

[353] UBS/LAM 527171.

[354] *Id.*

[355] *See* UBS/LAM 527334.

[356] *Id.*

XI. UBS's CAREFUL MANAGEMENT OF ITS CREDIT EXPOSURE FURTHER DEMONSTRATES ITS APPRECIATION OF ENRON'S FINANCIAL SITUATION

139. As UBS's banking industry expert witness Guy Erb explains, a financial institution's credit department "protects the bank's interests by estimating the probability that a borrower will default, assessing the security available to the bank to satisfy any outstanding obligations in the event of a borrower's default and, in the context of the bank's global exposure to all clients, managing the exposure to any particular borrower on an ongoing basis."[357] In light of this responsibility, the actions of UBS's credit department with regard to Enron are very telling.

140. UBS had about $400 million in potential lending exposure to Enron in January 1999, the month after Crews and Hunt had their relationship meeting with Fastow.[358] In signing off on UBS's Annual Review for Enron on February 22, 1999, Scott James, the then UBS Head of North American Credit, instituted a cap on UBS's exposure to Enron and issued an instruction

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[357] Report of Guy F. Erb dated July 17, 2006 ("Erb Report") at p. 8.

[358] *See* UBS/LAM 139185-86. As Glockler explained in his testimony, UBS's lending exposure numbers evidence UBS's commitments to extend credit to Enron, not necessarily the amounts Enron had actually borrowed from UBS. For example, Glockler both noted in an e-mail and testified that in August 2001, though UBS had commitments at that time to lend Enron roughly $90 million, Enron had only actually borrowed roughly $5 million. *See* Glockler Deposition at pp. 98-99 and UBS/LAM 056340-41.

to reduce the amount of exposure as the credit facilities matured.[359] Soon after executing the 1999 Equity Forward amendment, UBS had reduced its potential lending exposure to Enron by roughly twenty five percent (25%), and by the time UBS executed the 2000 Equity Forward amendment, it had reduced its potential lending exposure to Enron by over seventy percent [83] (70%), a change of around $285 million.[360] UBS further reduced its total potential lending exposure to the Enron group to roughly $30 million in early 2001 before committing to the E-Next transaction in April of 2001 and to two Enron credit facilities in May of 2001, at which point UBS's potential lending exposure to Enron was about $115 million, still down by over seventy percent (70%) from December 1998's relationship meeting between Enron and UBS.[361]

141. The expiration of credit facilities and the settlement of other transactions involving commitments of credit to Enron accounts for how this reduction occurred. What speaks volumes, however, is UBS's refusal to extend new credit commitments to Enron as this reduction occurred. Throughout 1999, 2000, and nearly all of 2001, Enron had an investment grade credit rating. As UBS's former credit officer for Enron Bob Verna testified, there is a "very low probability of default" in the investment grade world.[362] Additionally,

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[359] *See* UBS/LAM 057125-32.

[360] *See* UBS/LAM 139185-86.

[361] *See id.*

[362] *See* September 21, 2005 Deposition of Robert J. Verna ("Verna Deposition") at pp. 39-40.

Ian Drew, UBS's Chief Credit Officer for the investment bank at the time, characterized UBS's general exposure level to Enron in 2001 as "relatively small" and within regional credit authority.[363] Yet during this same general time period, UBS's credit limits on Enron caused Hunt to criticize openly UBS's credit stance toward Enron and accuse it of standing in the way of a more profitable relationship between UBS and Enron.[364] In fact, UBS's lack of credit for Enron kept UBS from elevating its status to a Tier I bank for Enron.[365] Hunt's frustration caused him to initiate a special meeting with UBS's credit officers on June 7, 2001 to discuss the situation.[366] W. Field, an attendee at this meeting, testified that such a meeting was "unusual" and "outside [84] the regular course" of business at UBS.[367] Given the "very low" probability of default in the investment grade world and the characterization of the UBS Group's credit exposure to Enron by one of its most senior credit officers as "relatively small," the trepidation of the credit officers most involved with Enron is revealing. Much of this is likely explained by UBS's understanding of the extent of Enron's off-balance sheet obligations.

142. Off-balance sheet obligations are financial obligations that a company might have that are not

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[363] *See* Drew Deposition at p. 87-88.

[364] *See* UBS/LAM 519580 and 099980-81.

[365] *See, e.g.,* UBS/LAM 099980-81, 015862.

[366] *See* UBS/LAM 025690-743.

[367] *See* Field Deposition at pp. 169-72.

reported on the balance sheet as debt when they are debt-like obligations.[368] As former UBS officer and head of investment banking at PW testified, one should "absolutely" be concerned by a company's use of off-balance sheet financings because the company's liabilities are not reflected transparently in public reports.[369] Obviously, then, knowledge of off-balance sheet obligations changes the way one evaluates a company, especially when there is recourse to the company if the obligation is not met.[370] In fact, Glockler admitted in his testimony that the market's recognition of the extent of Enron's off-balance sheet obligations and use of structures that gave the appearance of declining book leverage were causative factors in Enron's demise.[371]

143. UBS's relationship with Enron provided it with information concerning Enron's off-balance sheet obligations that market participants without a similar relationship did not possess.[372] This information gave UBS a distinct advantage over market participants in evaluating Enron's financial position. Hunt testified that as early as 1999 he knew Enron did billions of dollars in off-balance sheet financings.[373] Even before

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[368] *See* Verna Deposition at p. 83.

[369] *See* November 15, 2005 Deposition of Brian M. Barefoot ("Barefoot Deposition") at p. 85-86.

[370] *See* Bawden Deposition at p. 217 and Riddell Deposition at pp. 66-67.

[371] *See* Glockler Deposition at pp. 220-21.

[372] *See* Verna Deposition at p. 106.

[373] *See* Hunt Deposition at p. 193.

that, though, Union Bank credit officers had already identified UBS's off-balance sheet obligations as "material," "beyond [85] reasonable business levels," and "excessive . . . to capital."[374] Verna, who acted as UBS's credit officer for Enron during 1999, 2000, and early 2001, testified that even when he first began to cover Enron for UBS he believed Enron's off-balance sheet obligations were excessive.[375] This recognition of excessive off-balance sheet obligations was then coupled with UBS's recognition of Enron's engaging in "earnings management" and "aggressive" accounting decisions.[376] It is no wonder then that Verna's evaluation of Enron led him to label Enron as "problematic" from a credit standpoint.[377]

144. The UBS Group's most senior officers began to take notice of Enron's situation too. A May 2000 proposal for UBS to participate in Enron's 364-day and 5-year credit revolvers went all the way to UBS's global officers in Zurich for approval despite UBS's reduction of its potential lending exposure to Enron by over seventy percent (70%) in about fifteen (15) months.[378] Dick

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[374] *See* UBS/LAM 056026-52, 055765-66, and 055836-50.

[375] *See* Verna Deposition at p. 100.

[376] *See* UBS/LAM 056026-52, 055765-66, and 055836-50. UBS's Chief Credit Officer for the investment bank testified that at UBS a credit evaluation of a company required a minimum three year historical analysis. *See* Drew Deposition at p. 109. Verna himself admits that he "probably would have looked" at these credit reviews when evaluating Enron. *See* Verna Deposition at p. 99.

[377] *See*, *e.g.*, UBS/LAM 056697.

[378] *See* UBS/LAM 132026 and UBS/LAM 210230.

Asjes, UBS's Global Senior Credit Officer for corporate counterparties, noted Enron's "significant off-balance sheet liabilities" and Marco Suter, UBS's Group Chief Credit Officer, approved the Group's participation only on the condition the 5 year commitment be fully sold or hedged in market.[379] In approving another Enron-related credit proposal at the end of the next month, Asjes again noted Enron's "significant off-balance sheet liabilities" and approved the transaction on the conditions that UBS "be fully collateralized at all times with first priority lien" on the collateral and that UBS legal department confirm that "there is no risk of [86] stay in bankruptcy or event of default that would prevent UBS from taking the collateral.[380] As UBS officer

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[379] *See id.*

[380] *See* UBS/LAM 211368. This proposed transaction between UBS and EnronCredit.com, guaranteed by Enron Corp., is interesting in that it uniquely shows UBS's willingness to circumvent the spirit of laws and regulations designed to protect the public. UBS sold shares in a UBS "Fund of Funds" to investors, but under the U.S. Bank Holding Company Act, UBS was prohibited from directly investing in hedge funds. *See* UBS/LAM 211340-55. To circumvent the U.S. Bank Holding Company Act, UBS simply invested through "middlemen." *See id.* In this proposed transaction, EnronCredit.com agreed to be the "middleman" who would invest in the hedge fund for UBS. *See id.* UBS and EnronCredit.com were to enter into a return swap through which UBS received the returns on the investment in the hedge fund. *See id.* UBS would pay interest to EnronCredit.com at LIBOR on the return swap. *See id.* UBS would deposit cash with EnronCredit.com in the face amount of the return swap, which EnronCredit.com would use to invest in the hedge fund. *See id.* UBS would receive interest from EnronCredit.com on the deposit at LIBOR minus 15 basis points, where the 15 basis points served as the fee UBS paid EnronCredit.com for being the "middleman." *See id.* The final aspect of the transaction was EnronCredit.com's

Christine Lee explained at the time to her boss, Frieman, UBS had "a major credit issue with Enron" such that "it would be difficult to get anything approved unless the deal for some reason had no credit risk."[381]

145. One of the ways UBS officers attempted to deal with the Group's "major credit issue with Enron" was to conduct their activities with Enron through already existing collateral arrangements.[382] For example, on December 20, 2000 Verna responded to a UBS trader's credit request by pointing the trader to collateralized lines with Enron North America that could be used.[383] Sure enough, on January 11, 2001 approval was sought for trading with Enron using Enron North America's collateralized line.[384] Weeks later Verna instructed a UBS trader in Japan to make certain to book a currency swap using Enron North America.[385] Booking trades through the collateralized line with

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pledge of the shares in the hedge fund as its collateral for the return swap. *See id.* UBS documents indicate this was UBS's standard structure for getting around the prohibitions of the U.S. Bank Holding Company Act. *See id.* However, UBS's legal department reversed its approval of the structure because it used an atypical total return swap format involving a financing feature that undermined much of the rational [sic] for the legal department's original support. *See* UBS/LAM 211384. According to UBS's in-house counsel, "[w]e took a pretty aggressive position in endorsing the suggested trade to begin with and I am not inclined to risk pushing our analysis over the edge with this added element." *Id.*

[381] UBS/LAM 141445.

[382] *See* UBS/LAM 210397.

[383] *See* UBS/LAM 213452.

[384] *See* UBS/LAM 213703.

[385] *See* UBS/LAM 213932-33.

Enron North America became a convenient means by which [87] UBS could avoid incurring unsecured credit exposure to Enron.[386] UBS also continued its recent practice of lending money to Enron only on the condition that the lending exposure be sold or hedged in the market.[387]

146. Given the public and non-public information available to UBS regarding Enron's financial status, Enron's declining stock price in 2001 required a much more comprehensive response than simply ensuring that future credit extensions were made on a secured basis. The Equity Forward Contracts contributed significantly to UBS's potential credit exposure to Enron. As the price of Enron's stock fell, the potential credit exposure associated with those contracts became actual credit exposure. Additionally, because UBS sold/assigned the shares it had bought to hedge the Equity Forward Contracts to Enron/LJM/Hanier, every penny that Enron's stock price declined resulted in a penny of the written up amount of the Equity Forward Contracts becoming unhedged. In other words, the amount of shares UBS kept to hedge the Equity Forward Contracts only hedged the written up portion of the amended price so long as the market price remained equal to the amended price. Once the market

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[386] *See* UBS/LAM 139496.

[387] *See* UBS/LAM 056501-15 (Glass approved UBS loan to Enron in E-Next facility on the condition that it be "100% hedged and best efforts to sell"); *see also*, UBS/LAM 056430-31 (Bawden approved UBS participation in Enron's credit facilities on the condition that the exposure either be sold or hedged).

price fell below the amended price, UBS realized unhedged, unsecured credit exposure to Enron. Compounding this problem was the equity-level claim in bankruptcy associated with equity forward trades. This combination was extremely problematic for UBS and required a significant response.

147. UBS executed its response over a six-month period in which it virtually eliminated all of its credit exposure and collected roughly $400 million in cash from Enron before Enron filed for bankruptcy protection. First, UBS dumped approximately $163 million of its exposure on a Japanese investment fund. In June and July of 2001, UBS arranged for the sale [88] of two series of UBS credit-linked notes to an investment fund in the total amount of JPY (Japanese Yen) 20,000,000,000.[388] UBS's obligations to repay the principal and interest amounts on the notes were linked to an Enron credit event, such that UBS could avoid repayment of its obligations under the notes in the event of Enron's bankruptcy or default on a payment obligation to UBS.[389] UBS used these credit-linked notes to transfer its Enron credit exposure to a party who did not possess the material non-public information UBS possessed.

148. In July 2001 UBS also began the process of selling off certain Enron debt securities it held, including to its own retail clients. In February of 2001, Enron issued and sold in a private placement a significant

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[388] *See* UBS/LAM 558237-59 and 558261-59.

[389] *See id.*

amount of Zero Coupon Convertible Senior Notes Due 2021.[390] UBS purchased a cumulative face value at maturity amount of $261,800,000.00 worth of these notes.[391] On July 13, 2001, Enron filed a S-3 registration statement with the SEC registering the notes and the common stock issuable upon conversion and identifying various entities in the UBS Group as selling security holders of the notes, with the Prospectus filed on July 25, 2001.[392] Enron then filed a supplemental prospectus on August 15, 2001 identifying additional entities from the UBS Group as selling securities holders.[393] These SEC filings enabled UBS to sell the notes in the US public markets, which UBS then proceeded to do. These actions UBS was able to execute without potentially disrupting future business mandates from [89] Enron. Things changed for UBS in August 2001, however, as Enron's falling stock price

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[390] *See* Enron Corp. Prospectus for Zero Coupon Convertible Senior Notes Due 2021, SEC Registration No. 333-62168 filed July 25, 2001, at p. 1; *see also*, UBS/LAM 524662 and UBS/LAM 101902-03.

[391] *See* Enron Corp. Prospectus for Zero Coupon Convertible Senior Notes Due 2021, SEC Registration No. 333-62168 filed July 25, 2001, at p. 45; *see also*, Enron Corp. Prospectus Supplement No. 2 for Zero Coupon Convertible Senior Notes Due 2021, SEC Registration No. 333-62168 filed August 15, 2001 at p. 1.

[392] *See* Enron Corp. Amendment No. 1 to Form S-3 Registration Statement under the Securities Act of 1933, SEC Registration No. 333-62168 filed July 13, 2001; *see also,* Enron Corp. Prospectus for Zero Coupon Convertible Senior Notes Due 2021, SEC Registration No. 333-62168 filed July 25, 2001.

[393] *See* Enron Corp. Prospectus Supplement No. 2 for Zero Coupon Convertible Senior Notes Due 2021, SEC Registration No. 333-62168 filed August 15, 2001 at p. 1.

forced UBS to respond to the ever-increasing realization of actual credit exposure to Enron.

149. In August 2001, UBS was poised to receive mandates from Enron on two separate items of investment banking business that could, in combination, result in $8 million in fees to UBS and make it one of Enron's "tier one" banks, something Hunt had been working desperately hard to achieve.[394] As Hunt noted in an e-mail to Glockler on August 15, 2001, these mandates from Enron were important to UBS attaining its budget for the year.[395] Unfortunately for Hunt, the increased likelihood of an Enron default began to reach critical mass as negative information regarding Enron's finances leaked into the market and Enron's stock price continued its associated fall. E-mail exchanges and telephone conferences involving officers from all across the Group were immediately convened to discuss how to handle the Equity Forward Contracts, as the purely objective computer software UBS utilized to compute probability of default was already putting Enron on the second rung down of "junk" credit status.[396]

150. In June of 2001 as Enron's stock price approached $50.00, UBS agreed to lower the early termination "trigger price" feature of the Equity Forward

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[394] *See* UBS/LAM 068256 and 056341-42.

[395] *See* UBS/LAM 068078-80.

[396] *See, e.g.,* UBS/LAM 174754-57, 068083, 021175-77, and 093931; *see also* Drew Deposition at p. 127 and Field 30(b)(6) Deposition at pp. 224-26.

Contracts to $40.00.[397] The Equity Forward Contracts contained a provision that gave UBS the right to force Enron to settle the contracts, prior to their Settlement Dates, if the price of Enron's stock closed at or below the set trigger price for two consecutive days.[398] Enron announced on August 14, 2001 the sudden resignation of its CEO, Jeff Skilling.[399] When Enron's stock price closed the next day below the [90] trigger price, Enron immediately requested a renegotiation.[400] Before making a decision on lowering the trigger price, UBS required Enron to provide certain non-public information regarding the number, amounts, and trigger prices of other equity forward contracts it had, as well as information specifying Enron's recent trading activity in its own shares.[401] Without knowing this information, UBS's traders were concerned a "run for the door situation" could develop before UBS had the ability to settle the Equity Forward Contracts and sell the resulting shares into the markets.[402] In other words, UBS's traders anticipated that when Enron fell, it would fall fast.

151. Enron notified UBS that it had two other similar equity forward contracts covering an equal

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[397] *See* UBS/LAM 056375-78.

[398] *See* UBS/LAM 096790-91.

[399] *See, e.g.,* UBS/LAM 093669 and UBS/LAM 526529.

[400] *See* UBS/LAM 068081-82.

[401] *See* UBS/LAM 068083, UBS/LAM 095318.200, UBS/LAM 174754-57, and UBS/LAM 526537.

[402] *See* UBS/LAM 021175-77.

number of combined shares as the UBS contracts.[403] UBS reluctantly agreed to lower the trigger price of the Equity Forward Contracts, but only upon a commitment by Enron to settle the large equity forward contract at its October maturity.[404] UBS also required Enron to increase the number of shares with which Enron could net share settle the contracts. The effect of this requirement was that only at a share price below $9.93 would UBS fail to receive enough shares from Enron to recover the full amount of value Enron owed under the contract at the time of settlement.[405] UBS could then sell any stock received from Enron into the market and convert that value into cash.[406] Finally, UBS required Enron to grant UBS "Most Favored Nation" status, meaning Enron could not allow its other equity forward trades to have a higher trigger price or more favorable unwind conditions than UBS's contracts.[407] At Glass' direction, Glockler updated UBS's most senior global executives, including Arnold, Suter, [91] Sulzer, Berry and Drew, regarding the situation, along with a note that UBS equity analyst, Ron Barone, "has been widely quoted in the press as bullish on Enron's shares."[408] Drew testified that during this period he personally became involved in analyzing Enron

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[403] *See* UBS/LAM 068223-24.

[404] *See id.*

[405] *See id.*; *see also*, UBS/LAM 056386-88.

[406] *See, e.g.,* UBS/LAM 056337-39.

[407] *See* UBS/LAM 068223-24.

[408] *See id.*; *see also*, Glass Deposition at p. 258 and Glockler Deposition at pp. 66-67.

financial condition and through conversations with Glass learned for the first time that Enron's off-balance sheet were excessive and beyond reasonable business levels.[409]

152. Internal discussions regarding the Equity Forward Contracts began again in earnest during the first week of September 2001 as Enron's stock price continued its slide toward the amended trigger price.[410] Glockler informed Frieman that simply amending the trigger prices again was not an option.[411] He also informed Hunt that UBS's credit officers wanted another visit to Enron to have a "one-on-one" between UBS's quantitative analysts and Enron's.[412] Frieman responded to Glockler, Hunt, and a number of other UBS officers on September 7, 2001 setting forth some options discussed between him and Enron's Assistant Treasurer, including UBS extending a senior status loan to Enron to provide the liquidity necessary to settle the Equity Forward Contracts.[413] As Frieman explained, making this loan would elevate UBS's creditor ranking in bankruptcy.[414] Both Glockler and Frieman expressed their agreement that extending a loan to

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[409] *See* Drew Deposition at pp. 21-22, 70, 108, 113.

[410] *See*, *e.g.*, UBS/LAM 142855 and UBS/LAM 526847.

[411] *See* UBS/LAM 056379.

[412] *See id.*

[413] *See* UBS/LAM 142856.

[414] *See id.*

Enron would be preferable to retaining the current equity position.[415]

153. The smaller of the two Equity Forward Contracts, with a notional value of approximately $54 million, had a Settlement Date of September 13, 2001.[416] The larger of the two Equity Forward Contracts, with a notional value of approximately $340 million, had a [92] Settlement Date of October 12, 2001.[417] Hunt e-mailed Glockler, Frieman, and others on September 10, 2001 regarding his conversation with Enron's Assistant Treasurer.[418] Enron proposed to settle the smaller trade completely on its settlement date and settle half of the larger trade on its settlement date, rolling the other half forward with a lower trigger price.[419] Glockler wrote back to Hunt with UBS's position that Enron's "obligation to settle [the smaller trade] is absolute, and not dependent on what [UBS] agree[s] to do with the larger forward maturing" in October.[420]

154. On September 11, 2001, the financial markets were disrupted by the terrorist attacks. Enron asked UBS for temporary relief on the settlement of the smaller equity forward contract.[421] To garner support for accommodating Enron, Hunt sent an e-mail to

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[415] *See* UBS/LAM 056369.

[416] *See* UBS/LAM 056386-88.

[417] *See id.*

[418] *See* UBS/LAM 068250-52.

[419] *See id.*

[420] *Id.*

[421] *See* UBS/LAM 021170 and UBS/LAM 105132.

Glockler on September 12, 2001 providing the details of one mandate UBS received from Enron with a minimum agreed fee of $2.5 million and of one mandate UBS hoped to receive from Enron with an expected fee of between $3.75 and $5 million.[422] According to Hunt, these mandates would gain UBS "tier one" status with Enron.[423] Glockler forwarded Hunt's e-mail to Glass, noting the business motivation.[424] Glass, however, did not want to extend the maturity date until the markets were returned to normal.[425] Instead, Glass proposed UBS buy commercial paper directly from Enron.[426] Following on Frieman's comment on September 7th, Glass found this solution better for UBS because it upgraded UBS's bankruptcy position from equity holder to [93] unsecured creditor.[427] UBS did in fact then purchase directly from Enron $104 million of two-week commercial paper, $54,342,275.36 of which was used to settle the contract and the remainder of which UBS bought specifically to provide Enron with needed short-term liquidity.[428]

155. Following from Switzerland the management of UBS's exposure to Enron, Suter e-mailed Glockler on September 18, 2001 to find out whether

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[422] *See* UBS/LAM 068256.

[423] *See id.*

[424] *See id.*

[425] *See* UBS/LAM 105131.

[426] *See id.*

[427] *See id.*

[428] *See* UBS/LAM 021171, UBS/LAM 021179, and UBS/LAM 526877.

Enron had settled the trade.[429] That same day, Enron closed below the trigger price and discussions resumed.[430] UBS prepared an early termination notice, but decided not to serve it on Enron if Enron agreed to: (1) settle immediately 42% of the remaining equity forward exposure, equating to 50% of the total exposure prior to Enron settling the smaller contract; (2) streamline the early termination notification process; and (3) fully settle at maturity the remainder of the large equity forward contract.[431] These terms did not please Enron.

156. DeSpain and Freeland told Hunt and UBS's Equity Risk Management officers "in no uncertain terms" that requiring a full settlement by the October 12th settlement date would terminate the relationship between UBS and Enron – "period."[432] Enron specifically requested that UBS not take any action to terminate the contract prior to September 30th, the end of the quarter, to avoid a balance sheet hit on Enron's debt/equity ratio.[433] Enron explained to UBS that an early settlement would have a "double dip" effect on Enron's balance sheet by reducing [94] equity and adding debt in equal amounts.[434] Enron emphasized that

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[429] *See* UBS/LAM 068259.

[430] *See* UBS/LAM 095318.214.

[431] *See* UBS/LAM 068265-66.

[432] *See* UBS/LAM 021156, 021160.

[433] *See* UBS/LAM 021160.

[434] *See id.; see also,* UBS/LAM 021159.

its other banks had "stepped up" and that "no other banks [were] asking for [an] unwind."[435]

157. After speaking with Enron, Hunt updated Crews and Moelis, UBS's co-head of its US investment banking operations, with this information.[436] Somehow UBS credit officers got wind of Moelis' involvement, and Bawden e-mailed Glass to give him a "heads up" that Moelis would be calling regarding Enron's request to roll half of the remaining trade over the year end.[437] Hunt then sent an e-mail to Glockler and copied to Collins, Frieman, Glass, Dan Hassett, Lee, Mahaffy, Spencer, Tobin, Bawden, Riddell, Crew, and Moelis proposing an escrow arrangement to enable Enron to settle half of the remaining trade after the end of the quarter and to roll the remainder of the trade past the end of the year.[438] Hunt also passed along Enron's threat to terminate the relationship and set up a conference call to discuss the matter further.[439] Finally he tried to recruit Kamlani, Blue, and Steele by asking them to call in to give their support and letting them know that "credit is threatening to kill the Enron relationship.[440]

158. Several conference calls took place that day involving Hunt, Crews, Frieman, Lee, Mahaffy, Kelly,

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[435] *See* UBS/LAM 021160.

[436] *See id.*

[437] *See* UBS/LAM 206594.

[438] *See* UBS/LAM 021156.

[439] *See id.*

[440] UBS/LAM 105151.

Spencer, Glockler, Riddell, and Bawden.[441] Bob Mills, the Chief Financial Officer of UBS's investment bank even participated.[442] Mills concluded that because a settlement would materially impact Enron's financials at the end of an already difficult quarter, UBS would be "sensitive" to Enron's concerns.[443] Coupled with the fact that UBS's Corporate Finance Department "argued strenuously for lenience in order not to jeopardize an existing [95] mandate for a debt exchange and another one being sought for a securitization" of Enron receivables, which together could generate about $8 million in fees, UBS agreed to settle half of the trade and roll the other half past the year end.[444] UBS also agreed to document the situation "as an amendment to the trade rather than an actual Early Termination" to avoid the double dip affect on Enron's balance sheet.[445] UBS required Enron to lower the trigger price on the remaining portion of the trade to $20.00 and commit sufficient shares to enable UBS to recover what it was owed on the contract at a stock price as low as $5.00.[446] Additionally, UBS specifically required a written acknowledgment from Fastow, as Enron's Chief Financial Officer, that Enron was obligated to purchase from UBS over 2.5 million shares of Enron common stock at a price per share almost $50.00 above the current

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[441] *See* UBS/LAM 021160-63.

[442] *See id.*

[443] *See id.*

[444] *See* UBS/LAM 068142-43.

[445] *See* UBS/LAM 097970.

[446] *See* UBS/LAM 098087.

market price as a condition of effectiveness of the amendment.[447] These conditions were seen to be as far as UBS could go without permanently ruining its relationship with Enron.[448]

159. Ben Glisan voiced to Hunt in a call on October 9, 2001 Enron's hard feelings about the treatment Enron received from UBS's credit and trading departments during this critical period.[449] Hunt informed Blue, Steele, and Crews that Enron considered UBS's purchase of commercial paper to fund the first equity forward settlement a small concession because "'all of [Enron's] banks' came to their rescue with liquidity."[450] More important to Enron, Hunt noted, was the fact that UBS required Enron to pay $140 million in cash and increase its balance sheet debt.[451] As Hunt relayed to Blue, Steele, and Crews, Glisan told him these actions made [96] Enron "wonder about whether [UBS could] be counted on when needed."[452] UBS did lose Enron's business too. In an October 18, 2001 e-mail concerning UBS's business pipeline, Hunt noted that UBS lost the Enron mandate for a receivables securitization

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[447] *See* UBS/LAM 068274-75, UBS/LAM 068277, UBS/LAM 068309-11, and UBS/LAM 021134.

[448] *See* UBS/LAM 056337-38.

[449] *See* UBS/LAM 527056.

[450] *Id*.

[451] *See id*.

[452] *Id*.

due to the credit department forcing Enron to early settle the equity forward contract.[453]

160. UBS's credit believed eliminating the remaining exposure UBS had to Enron was more important to the Group than the increasingly remote possibility of future business with Enron. As of October 23, 2001, UBS had $2.08 million in net loan exposure to Enron and had sold off of all its Enron commercial paper a week or more earlier.[454] Three equity derivative trades between UBS and Enron remained outstanding, the remainder of the equity forward contract and two equity swap contracts.[455] One of the equity swap contracts matured on October 24, 2001.[456] Despite Enron's request to settle the parity value of the contract, approximately $32 million, and roll the roughly $20 million remaining for six months, Glockler decided the trade should be closed out completely.[457] On that same day, with Enron stock trading below the amended trigger price on the forward contract, UBS exercised its early termination rights on the remaining forward contract as well.[458] The risk that UBS would not be able to unwind these contracts and sell its Enron equity positions into the market was simply too

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[453] *See* UBS/LAM 527063-64.

[454] *See* UBS/LAM 527117-20; UBS/LAM 056349-51; UBS/LAM 056335.

[455] *See* UBS/LAM 056349-51.

[456] *See id.*

[457] *See id.*

[458] *See* UBS/LAM 207524.

great a concern for UBS not to take this action.[459] UBS received $175.8 million from Enron to settle these two trades.[460] UBS also sold into the market approximately 2.2 million shares of Enron stock it had held as a hedge to the forward contract, receiving over $40 million in additional cash from this [97] sale of its Enron securities.[461] The day after UBS both refused to roll the equity swap as Enron requested and served Enron with its notice of early termination of the remaining equity forward contract, Enron borrowed the full amount available to it under its credit facilities.[462] UBS surely anticipated this result, as Enron has already informed it that Enron needed the cash used to settle these contracts for operational purposes.[463]

161. While forcing Enron to settle these equity trades served as one means of reducing UBS's exposure to Enron, Glockler was also actively trying during this time period to reduce UBS's other exposure to Enron.[464] On October 29, 2001, UBS's total exposure to Enron stood at approximately $12 million, and all trading with Enron was prohibited except a "sharply reduced" currency exchange trading line.[465] At this

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[459] *See* Ecv006570522-23.

[460] *See* UBS/LAM 056337-39; UBS/LAM 056320-21; UBS/LAM 207619.

[461] *See* UBS/LAM 056337-39; UBS/LAM 056326.

[462] *See* UBS/LAM 056329-30; UBS/LAM 056337-39.

[463] *See* Ecv006570522-23.

[464] *See* Glass Deposition at pp. 355-59.

[465] *See* UBS/LAM 207619-20; UBS/LAM 056294; UBS/LAM 056302-03.

same time, Glockler was telling Glass and Bawden that once UBS received its payments from Enron on the equity trade settlements, the authority to downgrade Enron further internally to "junk" status was at the regional level.[466] A downgrade of Enron to "junk" status would be significant because it would force Enron to post cash collateral for trades done under certain collateral agreements with UBS.[467] While UBS was hesitant to make such a move, after Glockler communicated what he learned regarding Enron's liquidity situation in a conference call with Hunt and Enron's Assistant Treasurer, Bawden agreed with Glockler's recommendation that Enron should be downgraded to "junk" status immediately on November 5, 2001.[468] Drew noted his agreement on the downgrade to "junk" status the next day.[469]

[98] 162. On November 8, 2001, Enron announced it was restating the last four years of earnings and consolidating JEDI, Chewco, LJM1, and LJM2.[470] After returning from an extremely confidential meeting Enron held with certain of its banks on November 19, 2001, Glockler wrote Asjes, Berry, Drew, Suter, Bawden, Glass, Riddell, and Landowne with his conclusions, including the decision to downgrade Enron

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[466] *See* UBS/LAM 068095-97.

[467] *See*, *e.g.*, UBS/LAM 207619-27 and UBS/LAM 068199-200.

[468] *See* UBS/LAM 207926-28.

[469] *See* UBS/LAM 207932.

[470] *See* UBS/LAM 363187-88.

even further still.[471] All currency exchange trading with Enron was eliminated at this time.[472] When S&P and Moody's downgraded Enron on November 28, 2001, UBS issued margin calls to Enron requiring it to post collateral on certain outstanding trades, again further downgraded Enron internally, and officially suspended all business with Enron, though UBS had effectively already done so after the bank meeting.[473] Enron filed bankruptcy on December 2, 2001. UBS's total net lending and trading exposure to Enron totaled approximately $1.5 million.[474] Thus, UBS's access to non-public information concerning Enron's finances and financial practices allow it to eliminated [sic] its net lending exposure to Enron completely and reduce its trading exposure by over eighty percent (80%) since January 1999, all while vying for and sometimes receiving Enron's business.

XII. UBS POSSESSED THE REQUIRED STATE OF MIND FOR FRAUD

163. In *Ernst & Ernst v. Hochfelder,* 425 U.S. 185 (1976), the Supreme Court considered whether an intent to deceive, manipulate, or defraud is a necessary element in a private action under Section 10(b) of the 1934 Act. *See Ernst & Ernst,* 425 U.S. at 187.[475] Relying

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[471] *See* UBS/LAM 056302-03.

[472] *See* UBS/LAM 068552-54.

[473] *See* UBS/LAM 009049-54; 527343-47; and 068552-54.

[474] *See* UBS/LAM068602-03.

[475] The plaintiffs suing Ernst & Ernst specifically disclaimed the existence of fraud or intentional misconduct and instead

on the "manipulative or deceptive" language found in the statutory provision, the Court held a private cause of action under Section 10(b) does require proof the defendant acted with [99] "scienter," defined as "a mental state embracing intent to deceive, manipulate, or defraud." *See id.* at 193 n. 12. Under the PSLRA standard for pleading this element of a Section 10(b) claim, a plaintiff must allege particular facts giving rise to a "strong inference" of the required state of mind. *See* 15 U.S.C. § 78u-4(b)(2). The Supreme Court recently articulated how courts should apply this standard.

164. To determine the sufficiency of a complaint's allegations of scienter under the PSLRA standard, a court must consider all competing inferences rationally drawn from the facts alleged in the plaintiff's complaint. *See Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 314 (2007). To qualify as "strong," an inference of the presence of the required state of mind must be *at least as compelling* as an inference of the absence of the required state of mind. *See id.* Importantly, the court's job is not to scrutinize each allegation in isolation, but rather to assess holistically the entirety of a plaintiff's allegations shedding light on the defendant's state of mind. *See id.* at 325. There need not be any "smoking gun" allegations of scienter, as circumstantial evidence can provide the necessary strength to an inference of scienter. *See id.* at

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alleged that the accounting firm failed to utilize appropriate auditing procedures. *See Ernst & Ernst*, 425 U.S. at 190.

324; *see also*, *Goldstein v. MCI WorldCom*, 340 F.3d 238, 246 (5th Cir. 2003).

165. The PSLRA speaks of scienter in terms of "the required state of mind." *See* 15 U.S.C. § 78u-4(b)(2). This language demonstrates Congress' recognition that most courts, including the Fifth Circuit, regard "severe recklessness" as satisfying the required state of mind for a claim brought under Section 10(b). *See*, *e.g.*, *Indiana Electric Workers' Pension Trust Fund IBEW v. Shaw Group, Inc.*, 537 F.3d 527, 533 (5th Cir. 2008). "Severe recklessness" applies to conduct involving "an extreme departure from the standards of ordinary care . . . that present[s] a danger of misleading buyers or sellers which is either known to the defendant or is so obvious that the defendant must have been aware of it." *See Goldstein*, 340 F.3d at 245-246 [100] (internal citations omitted). Stated differently, as opposed to actually intending to mislead an investor, severe recklessness applies to conduct outside the standard of ordinary care where the obvious result is for the investor to be mislead.

166. In securities fraud cases based on the non-disclosure of potentially material facts, plaintiffs establish scienter by demonstrating: (1) the defendant knew of the potentially material fact, and (2) the defendant knew that a failure to reveal the potentially material fact would likely mislead investors. *See City of Philadelphia v. Fleming Companies, Inc.*, 264 F.3d 1245, 1261 (10th Cir. 2001). With regard to the second prong of this scienter formulation, the standard is met where the non-disclosed fact is "so obviously material

that the defendant must have been aware both of its materiality and that its non-disclosure would likely mislead investors." *Id.* Significantly, the legal issues surrounding a defendant's duty to disclose and its failure to disclose are not part of the scienter analysis. In other words, "severe recklessness" in a private action under Section 10(b) based on non-disclosure in no way depends on whether the defendant subjectively believed it owed a duty to disclose to the plaintiff. Instead, the existence of a duty to disclose relates to whether the defendant's failure to disclose the alleged material fact violated the statute.[476] Scienter, a completely different question, considers whether the defendant knew the alleged material fact and whether the fact was so clearly material that an investor would obviously be mislead through ignorance of it.

167. The specific material fact Plaintiffs allege UBS failed to disclose to them at the time of their purchase of Enron securities is that Enron engaged in transactions in order to report, and thus did report, its financial results in a materially misleading way. Given this allegation, the Court must then determine whether the Plaintiffs alleged sufficient facts to demonstrate (i) UBS [101] knew Enron engaged in transactions in order to report its financial results in a materially misleading way, and (ii) an issuer's material manipulation of its financial performance is itself so

[476] A duty to disclose would also be relevant to the question of whether the plaintiff is entitled to a presumption of reliance under *Affiliated Ute.*

obviously material that an investor would be mislead through ignorance of the fact.

168. Plaintiffs incorporate herein by reference the allegations contained in Sections IX-XI herein. Based on these allegations, Plaintiffs specifically allege UBS knew Enron engaged in transactions in order to report, and did report, its financial results in a materially misleading way. Plaintiffs' allegation is based on its other allegations demonstrating that at least the following UBS employees possessed sufficient information to have this knowledge: Susan Agonis, Omar Al-Salehi, Linda Bammann, Karsten Berlage, Roger Bieri, Kimberly Blue, Simon Canning, Robert Casey, Larry Charleson, Michael Collins, John Convery, Karyn Conway, Sandra Costin, Ken Crews, Ryan Donovan, Ian Drew, Sara Edmonston, Richard Ennis, Joseph Esteves, Mike Fehrman, Bill Ferri, Tom Field, Wendy Field, Andrew Fishman, Joel Forbes, Paul Freilich, Adam Frieman, Lorenzo Gaggini, Sal Giarmetti, Scott Giese, Bill Glass, Chris Glockler, Eric Hanson, Rupert Hilmi, Gina Hubbell, Jim Hunt, Scott James, David Kelly, Colin Kim, Parker Knight, Ed Kyritz, Steve Landowne, Christine Lee, David Lee, Gary Luciani, Michael Mahaffy, Tom McErlean, Dorothy McKinley, David Mikula, Rob Morgan, Art Penn, Corey Pinkston, Jennifer Poccia, Chris Pohle, Bill Powell, Gregory Raue, Douglas Renfield-Miller, Kevin Reynolds, Bruce Richards, Mark Ritter, Steve Sreckovic, Tim Steele, Evans Swann, Jason Sweet, Richard Tavrow, Lyndon Taylor, Erik Velastegui,

Robert Verna, Stephen Wade, John Wall, Mark Wallace, Scott Whitney, and Whit Williams.[477]

[102] 169. The fact that Enron engaged in transactions in order to report, and did report, its financial results in a materially misleading way was itself so obviously material, UBS must have been aware that an investor would be mislead through ignorance of the fact. For example, UBS's own market analysts admit their analysis of an issuer and their investment opinions with regard to an issuer's securities depend primarily on financial information taken from the issuer's financial statements.[478] In fact, Jay Yannello, a former UBS equity analyst who covered Enron during the Fraud Class Period, testified that an issuer's financial statements are "the anchor from which to move forward" when analyzing an issuer's securities.[479] Likewise, UBS debt analyst Stewart Morel testified that

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[477] "Knowledge of a corporate officer or agent acting within the scope of authority is attributable to the corporation." 2 Thomas Lee Hazen, Treatise on the Law of Securities Regulation § 12.8[4], at 444 (4th ed. 2002); *see also*, *In re JPMorgan Chase Sec. Litig.*, 363 F. Supp. 2d. 595, 627 (S.D.N.Y. 2005) (finding defendant's officers' knowledge that certain Enron-related transactions were not *bona fide* trades was attributable to defendant), *Southland Sec. Corp. v. INSpire Ins. Solutions Inc.*, 365 F.3d 353, 366 (5th Cir. 2004), and *FDIC v. Shrader & York*, 991 F.2d 216, 224-25 (5th Cir. 1993).

[478] *See* November 18, 2005 Deposition of Ronald J. Barone ("Barone Deposition") at pp. 198-99; November 16, 2005 Deposition of Stewart E. Morel ("Morel Deposition") at pp. 11, 69-70; and April 26, 2006 Deposition of James Yannello ("Yannello Deposition") at pp. 36-39.

[479] *See* Yannello Deposition at pp. 38-39.

his rating on a debt security depends on the ability of the issuer to repay its debt, which he attempts to determine by analyzing the issuer's public financial statements.[480] UBS's own experts agree.[481] For example, UBS's securities analyst expert, Patricia Chadwick, admits that an analyst's fundamental analysis of a company necessarily "requires an analysis of publicly available financial statements."[482] Ms. Chadwick also highlighted the vital importance of an issuer's financial statements by explaining that if an investment bank becomes aware that an issuer's financial statements are the product of fraud, the investment bank would have an *obligation* to report the issuer to the SEC and an *obligation* to prevent the bank's securities analysts from writing reports on the company and its securities.[483] And it is not only the secondary securities markets to which the issuer's financial statements are of fundamental importance. UBS's due diligence expert, Guy Erb, admits that appropriate due [103] diligence by a securities underwriter requires an analysis of the issuer's financial statements.[484] Simply put, given the unquestioned and unquestionable significance of financial statements to the securities markets, the very publication of which occurs by SEC mandate,

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[480] *See* Morel Deposition at pp. 69-70.

[481] *See* Chadwick Deposition at pp. 156, 166, 205; Erb Deposition at p. 140; Ugone Deposition at pp. 58-59; and Kothari Deposition at p. 52.

[482] *See* Chadwick Report at ¶ 17.

[483] *See* Chadwick Deposition at pp. 156, 166, 205.

[484] *See* Erb Deposition at p. 140.

UBS's knowledge that Enron engaged in transactions in order to publicly report, and did report, its financial results in a materially misleading way was so obviously material that UBS must have been aware that an investor would be mislead through ignorance of the fact.

XIII. UBS's TREATMENT OF PLAINTIFFS

170. UBS generally asserts that, even assuming it knew Enron engaged in transactions in order to publicly report, and did report, its financial results in a materially misleading way, UBS could not disclose this knowledge because it is knowledge gained from confidential information.[485] UBS's position is inconsistent with its own securities analyst expert witness, Ms. Chadwick, who admits that in such situations UBS has an obligation to "blow the whistle" on Enron by disclosing what it knows to the SEC.[486] Beyond reporting Enron to the SEC, industry standards required UBS to take other affirmative steps to manage the conflict

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[485] *See*, *e.g.*, UBS's "Reply Memorandum of Law in Support of Defendants' Motion to Dismiss Plaintiffs' Third Amended Class Action Complaint (#122) in *Lampkin v. UBS PaineWebber, Inc.*" (# 167).

[486] *See* Chadwick Deposition at pp. 156, 166, 205. Consistent with Chadwick's testimony, Plaintiffs' securities industry compliance expert, Raymond Aronson, former Senior Managing Director of legal and compliance at Bear Stearns, testified that he had personal experience in reporting securities issuers to the SEC when nonpublic information known to him revealed that the issuers' public statements were false. *See* August 30, 2006 Deposition of Raymond L. Aronson ("Aronson Deposition") at p. 107.

between UBS's conditional responsibility to maintain the confidentiality of Enron's information and its absolute duty of disclosure to its retail clients. For example, industry standards required UBS to place Enron and its securities on a "legal restricted list," to use the terminology of UBS's Sales Practice Compliance Manual.[487] "The placement of a security or Issuer on the Legal Restricted List generally restricts all trading in the security or derivative, or the securities of the Issuer, [104] unless the Legal Department or Compliance Department grants an exception."[488] The placement of a security or Issuer on the Legal Restricted List also prohibits the solicitation of customer orders, the recommendation of transactions or opinions with respect to the securities or the Issuer, and the issuance of research on the securities or the Issuer.[489] Brian Barefoot, the former head of investment banking at PaineWebber, Inc. who left UBS in December 2000 after the successful integration of PW into the UBS Group, summarized the standard industry response to discovering corporate malfeasance as follows:

> Well, first of all you would ***suspend the stock*** if it were. You would ***suspend the market making activities.*** You would ***certainly suspend research coverage*** if they had equity outstanding, even if it was something like

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[487] *See* Barefoot Deposition at pp. 80-81 and Aronson Deposition at pp. 99, 161-63, 170-72. *See also*, UBS/LAM 038096.

[488] UBS/LAM 038096.

[489] *See id.*; *see also*, Chadwick Deposition at pp. 104-08 and Aronson Deposition at pp. 99, 161-63, 170-72.

> [self-dealing] that's not equity related but it does impact. That's the first thing you would do, and I'm sure we would ***enter into some sort of a, quote, unquote, investigation,*** assign somebody the responsibility to take a look at this thing before any action, whether it was to resume offering an opinion or some other course of action.[490]

171. So, contrary to UBS's position that there was nothing it could do to protect its retail clients from purchasing Enron securities at a time when UBS knew Enron engaged in transactions in order to publicly report, and did report, its financial results in a materially misleading way, industry standards required the actions outlined above. In an extreme departure from this standard, UBS firm policy throughout the Fraud Class Period instead required its Financial Advisors to provide UBS's retail clients with UBS's "Strong Buy"[491] recommendation on Enron stock anytime the Financial Advisors expressed an "inconsistent view" with regard to Enron stock.[492]

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[490] Barefoot Deposition at pp. 80-81. (Emphasis added)

[491] UBS maintained a "Strong Buy" recommendation on Enron stock until November 28, 2001, at which time the firm's recommendation was downgraded to a "Hold." *See* UBS/LAM 038630-31.

[492] *See* UBS/LAM 038353-61; *see also*, Meyer Deposition at pp. 60-61, 105-06 and UBS/LAM 038434-45. "Strong Buy" meant that UBS believed the stock would appreciate on a total return basis by twenty percent (20%) or more within twelve (12) months. *See* Barone Deposition at p. 34.

[105] **XIV. UBS's UNIQUE RELATIONSHIP TO ENRON EMPLOYEES**

172. Most significantly affected by UBS's unjustifiable silence were Enron's own employees. In October 1998, PW entered into a "captive broker" contract with Enron Corp. whereby PW became the exclusive administrator of Enron's employee stock option plans.[493] Because of this contract, in order for an Enron employee to exercise stock options, the employee was required to open an account, and thus begin a relationship, with PW.[494] A group of Financial Advisors in the Heritage branch of PW/UBS in downtown Houston known as the "Emery Group" serviced the Enron account and the resulting relationships with UBS clients and was led by PW/UBS Financial Advisor Rocky Emery, the originator of the business model.[495]

173. When an Enron employee exercised his or her employee stock option through PW/UBS, the employee could either keep the net proceeds (stock or cash) in an account with PW/UBS or transfer the proceeds outside of PW/UBS.[496] Thus, to induce the Enron employees to keep the proceeds (and hopefully execute

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[493] *See* UBS/LAM 038288-93.

[494] *See id.*; *see also*, May 16, 2006 Deposition of Rocky V. Emery ("Emery Deposition") at p. 34; Fisher Deposition at pp. 35-36; November 30, 2005 Deposition of Kenneth L. Logsdon ("Logsdon Deposition") at p. 21; and UBS/LAM 037782-807.

[495] *See* Emery Deposition at pp. 18-20; Fisher Deposition at p. 12; and Logsdon Deposition at pp. 9-14, 39.

[496] *See* Emery Deposition at pp. 154-55 and UBS/LAM 037782-807.

trades) in an account at PW/UBS, thereby maintaining the relationship between PW/UBS and the client, PW/UBS provided a number of "services" to its Enron-employee clients free of charge.[497] Those free services included PW/UBS's "premier" account, known as a Resource Management Account, (an $85.00 per year value), stock option analyses, and financial plans (hundreds of dollars in value).[498]

174. This business model proved to be extremely lucrative.[499] Using the favorite terminology of Patrick Mendenhall, the UBS Heritage Branch Office Manager, because of the [106] employee stock option contract, getting Enron employees to begin their relationship with UBS as clients was like "shooting fish in a barrel."[500] Emery estimates that eventually PW/UBS retained approximately sixty percent (60%) of the net proceeds generated through the Enron stock option plans.[501] In fact, by the year 2000, the Heritage branch was ranked the number two UBS branch in the entire United States with $50 million in earnings.[502] Of that $50 million, Emery created $14 million himself, exclusive of the literal scores of Financial Advisors who

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[497] *See* Logsdon Deposition at pp. 23-25 and UBS/LAM 037782-807.

[498] *See id.*

[499] *See* Fisher Deposition at pp. 111-16; *see also,* UBS/LAM 583938-39.

[500] *See* November 10, 2005 Deposition of Thomas Sanchez ("Sanchez Deposition") at p. 65.

[501] *See* Fisher Deposition at p. 111-12.

[502] *See* UBS/LAM 583938-39.

also serviced the Enron-employee clients because of the stock option plans.[503] As for PW/UBS, it received 65% to 70% of the money generated by Emery and these other Financial Advisors working the Enron account.[504]

175. In order to keep the exclusive relationship with Enron, UBS agreed to compromise the interests of the retail clients it gained through that relationship. Specifically, using the label of UBS Vice President Bobby Fisher, the UBS executive who replaced Rocky Emery in managing the Enron employee stock option plan when Rocky Emery left UBS, UBS adhered to a "Gentlemen's Agreement" under which UBS agreed its Financial Advisors would generally: (1) not advise their clients to sell Enron stock except as part of a "diversification strategy;" (2) not advise Enron employees to exercise their employee stock options; and (3) not say anything about Enron that might be considered negative.[505] Financial Advisors in UBS's Heritage Branch were required to walk a fine line where they could generally advise their clients to "diversify," which necessitated the sale of Enron securities, but the Financial Advisors could [107] not espouse opinions or

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[503] *See* Fisher Deposition at p. 114.

[504] *See* Fisher Deposition at p. 46.

[505] *See*, *e.g.*, November 16, 2005 Deposition of Don R. Bosse ("Bosse Deposition") at pp. 82-83, 85-86, 89-90; Emery Deposition at pp. 87-88; Sanchez Deposition at pp. 84-87, 89-92, 105; *See also,* UBS/LAM 043296-339 Oral Deposition of V. Robert Fisher, Jr. dated August 19, 2003 in *Wu v. Olson, et al.,* Cause No. 2002-42447 in the 127th District Court of Harris County, Texas at pp. 103-05.

recommendations regarding Enron securities other than to provide their UBS retail clients with UBS's "Strong Buy" recommendation on Enron stock.[506] Additionally, given UBS's firm policy with regard to "inconsistent" statements, e.g., "diversify" out of Enron securities when there is a UBS "Strong Buy" recommendation on Enron stock, a Financial Advisor's diversification advice had to be accompanied by a statement that UBS maintained a "Strong Buy" recommendation on the stock. As former UBS Financial Advisor Thomas Sanchez testified, UBS clients were typically confused by a Financial Advisor's "diversification" suggestion when UBS carried a "Strong Buy" on the stock.[507] The August 21, 2001 termination of former UBS Financial Advisor Chung Wu ("Wu") at the demand of Enron for violating this "Gentlemen's Agreement" by directly advising some UBS retail clients to sell Enron stock due to its recent financial performance demonstrates the powerful effect of UBS's "Strong Buy" policy.[508]

176. For over fifteen years, Wu operated four Chinese restaurants in the area of Houston, Texas.[509] While operating the restaurants, he attended the University of Houston and obtained a Masters of Business Administration degree with a focus in accounting.[510] He already had an undergraduate degree in finance

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[506] *See id.*

[507] *See* Sanchez Deposition at p. 121.

[508] S*ee* UBS/JALEX 0944 and UBS/LAM 038351.

[509] *See* November 11, 2005 Deposition of Chung Wu ("Wu Deposition") at p. 48-49.

[510] *See id.* at pp. 46-47.

and five years experience as an accountant prior to operating his own businesses.[511] Wu chose to leave the restaurant business and embark upon a second career as a securities broker.[512] After a short period of time at Morgan Stanley, he joined [108] PW at the Heritage branch where he worked from April 21, 1999 until he was terminated by UBS on August 21, 2001.[513]

177. PW assigned Wu to work with the Emery Group. As such, the group of UBS clients to whom Wu was assigned was comprised almost exclusively of Enron employees and former employees who had an account with PW because of their Enron employee stock options. Like the other Financial Advisors in the Emery Group, Wu serviced UBS clients who were heavily concentrated in Enron stock and unexercised employee stock options. He understood the basic principle known to Financial Advisors that such over-concentration was a risky situation for these UBS clients. Thus, Wu started to watch Enron closely in December 2000.

178. Wu maintained a growing list of his UBS clients who wished to be updated with information regarding Enron Stock. From December 2000 through August 2001, Wu spent a significant amount of time considering the value of Enron stock by reviewing public filings and comparing Enron's reported financial

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[511] *See id.*

[512] *See id.* at p. 49.

[513] *See id.* at pp. 49, 51; *see also*, UBS/JALEX 0944.

performance to those of similarly situated, or peer, companies. Like UBS's own market analysts, Wu performed his review of Enron through publicly available documents.

179. As the months passed, Wu became suspect of UBS's "Strong Buy" rating on Enron stock. In August 2001, Wu reviewed Enron's newly reported financial data. Additionally, he had been following press releases regarding Enron and its divestment of assets, loss of management personnel, etc. The information he gathered led him to believe that Enron's financial situation was deteriorating. On August 20, 2001, Chung Wu worked late. He reviewed UBS's most recent "Strong Buy" Research Note, Enron's most recent SEC filings, Enron's 2000 10K, its April 2001 10Q, and Enron's newly issued second quarter 10Q. His concerns culminated in his last correspondence to his UBS clients:

[109] Wu, Chung

From: Wu, Chung
Sent: Tuesday, August 21, 2001 12;20 AM
Subject Most recent 10-Q report indicates liquidity problems and decline in trading margin.

Dear Clients,

Financial situation is deteriorating in Enron and price drops another $7.00 from last P/E report while most of the others stay the same or improve. Detail analysis on 10-Q will be ready after 8/29/01 and will be sent out only on a requested basis. I would advise you to take

some money off the table even at this point. For those who still has [sic] problems separating themselves from the stocks or vested options, please think shout selling "Call" against the long positions or selling "Uncovered Call" against the vested options with the consideration of having sufficient assets to satisfy the maintenance requirement.

Time is value and waiting to make a decision would cost you a fortune. For a capital asset investment we always should know the price we would sell at. *Please let me how can I help you to execute our financial plan*.

His warning was to no avail. In fact, it was his undoing, causing a ripple effect and resulting in his immediate termination from UBS.

180. Jeff Donahue ("Donahue"), Enron's Senior Vice President of Corporate Development at the time, was a UBS retail client whose account was assigned to Wu. It was Donahue with whom Hunt met to discuss Enron's plans to sell and/or leverage all of its international assets.[514] Donahue received Wu's e-mail directly on August 21, 2001.[515] Upon receipt of the e-mail, Donahue sprang into action.

181. At 6:12 a.m. on August 21, 2001, Donahue forwarded Wu's e-mail to Enron employees Kelly Boots and Tim DeSpain, expressing his desire to have Wu terminated.[516] Donahue then forwarded Wu's e-mail to

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[514] *See* UBS/LAM 526383 and UBS/LAM 526394.

[515] *See* PW/WU 01425-27.

[516] *See* ECTe022738876-77.

Hunt.[517] Hunt, in turn, forwarded Donahue's e-mail to [110] Barone.[518] Hunt explained how the e-mail was brought to his attention by "an SVP of Enron" who stated "that this PW guy should be fired[.]"[519] Hunt asked Barone to whom he should direct the e-mail.[520] Barone told Hunt to contact Lee Feinberg, the head of UBS's stock option plan business.[521] Hunt then thanked Donahue for bringing the situation to his attention and assured him that his request had been delivered to "the appropriate person."[522]

182. However, Donahue/Hunt/Barone were not the only Enron/UBS people working to terminate Wu. Joan Amero was one of Wu's clients who worked for Enron-owned Portland General in Portland, Oregon.[523] Amero forwarded the e-mail to her boss, Joyce Bell ("Bell"), who worked in PGE's Human Resources department. Joyce Bell sent a copy to her boss, Arleen Barnett ("Barnett"), asking what Barnett thought of the advice. Ultimately Bell sent a copy of the e-mail to her counterparts in Enron's Human Resources division, Aaron Brown ("Brown") and Pam Butler, both

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[517] *See* UBS/LAM 526578-81.

[518] *See* UBS/LAM 526582-85.

[519] *Id*.

[520] *See id.*

[521] *See* UBS/LAM 526588-90.

[522] *See* UBS/LAM 526586-87.

[523] *See* PW/WU 01425-27.

mid-level managers in the Employee Compensation department at Enron.[524]

183. After reading the e-mail, Brown immediately contacted his superior, Mary Joyce ("Joyce"). Joyce was the Senior Vice President of Executive Compensation at Enron.[525] She was a signatory to PW/Enron agreements regarding the Stock Option Administration Contract and was a personal client of Emery.[526] By August 21, 2001, Joyce had liquidated all of her [111] Enron holdings. Importantly, she was also the person with whom UBS would negotiate to renew the Stock Option Administration Contract, which expired in a mere two months.[527]

184. Joyce was not one to mince words. She immediately called Mendenhall. According to UBS's response to a Congressional inquiry into Enron's involvement in Wu's termination:

> Mary Joyce and Aaron Brown, the Enron personnel responsible for administering Enron's stock option plan, contacted PaineWebber on August 21, 2001, to bring Mr. Wu's e-mail to the Firm's attention. Ms. Joyce expressed her extreme displeasure that the email had been sent to dozens of Enron employees, requested that the Firm address the situation promptly,

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[524] *See* ECgg000326069-71.

[525] *See* Emery Deposition at pp. 232-33.

[526] *See* UBS/LAM 038296-97 and Emery Deposition at p. 234.

[527] *See* Emery Deposition at pp. 232-33.

and in words or tone expressed her view that strong disciplinary action be taken.[528]

185. After his conversation with Joyce, Mendenhall called Wu on his extension, around 1:08 p.m. CST, and they had the following exchange:

CW: Yes, Pat?

PM: Are you sending out an e-mail to Enron employees telling them that the financials are deteriorating and you recommend taking some stock off the table?

CW: I did, yeah, this morning.

PM: Why would you do that? You can't do that!

CW: Okay, I'm sorry.

PM: Chung, you can't, how many did you send it to?

CW: Um, 30, 30 or 40 of them.

PM: Oh Jesus Christ Chung!! What are you thinking!? You can't do that!! Enron has just crawled four feet up my ass! You cannot recommend to buy or sell that stock! You know that!

CW: Okay, I'm sorry, I didn't realize that . . .

PM: Get me a list of everyone you sent it to . . .

CW: Okay . . .

PM: Chung, this is. . . .

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[528] *See* UBS/LAM 038353-61.

CW: I . . .

[112] **PM**: Who approved the e-mail?

CW: Nobody, I was working real late last night and I sent it out around 12:30 at nighttime . . . and . . . uh . . .

PM: From here?

CW: Yes, from here, yes . . . I was studying 10Q . . .

PM: Chung, you are not an analyst . . . you cannot make a Goddamned recommendation on Enron stock! You know that! I told you 50 times! I told everybody! You don't make a recommendation on Enron!

CW: Um . . .

PM: This has gotten to the head guy at Enron now, they are calling me . . .

CW: I'm so sorry, I'm just . . .

PM: I need a list of who you sent it to, right now.

CW: Okay . . . alright . . . I'll bring it up to you . . .

186. Wu went to Mendenhall's office and gave him a copy of his e-mail. According to Wu, Mendenhall reviewed the document and said, "Chung, you are right, you are right, but why did you put it in writing? You just don't put it in writing. Mary Joyce is so pissed she's throwing things in her office." Mendenhall then obtained a copy of Wu's distribution list, told Wu that

he might be taken off the "Enron project," and instructed Wu to go back to his office and wait.

187. Brown followed up the call to Mendenhall with e-mails. The first was sent to Kurt Grunsfeld ("Grunsfeld") and copied to Mendenhall.[529] Grunsfeld was a UBS officer in the retail brokerage home office in Weehawken, New Jersey. He assisted the Heritage Branch regarding the administration of the Enron stock option plan contract. Brown's e-mail said, "please handle this situation. I've also forwarded to Pat Mendenhall. This is extremely disturbing to me."[530] The second e-mail, again sent to Grunsfeld and copied to Mendenhall, was [113] sent less than five minutes later and further stated, "Several people at PGE received this. I want to see the full distribution list."[531] Within minutes, in violation of NASD and UBS confidentiality rules, UBS assistant branch manager Patricia Trieglaff faxed a copy of the distribution list to Brown.[532] Grunsfeld then e-mailed Fisher, the UBS officer within the Heritage Branch who assumed responsibility for servicing the Enron employee stock option plan after Emery left UBS, attaching Wu's e-mail and stating, "Please read. I am calling you now to discuss."

188. Sometime thereafter, Mendenhall and UBS in-house counsel Peter Bado ("Bado") called UBS's

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[529] *See* UBS/LAM 038334-36.

[530] *Id.*

[531] UBS/LAM 038337-39.

[532] *See* EC 002896526-28.

human resources department concerning the situation.[533] The conversation was memorialized in UBS's human resources records:[534]

> – Pat Mendenhall called. Sen[t] e-mail to around 70 clients about ENRON saying that the stock is not doing well. He also sent out a chart that was not approved. This company is saying they will drop UBS PaineWebber now. Pat spoke to Peter Bado who told Pat REDACTED Pat would like to terminate trainee today.
>
> 3:30 w/Bado and BoM.
>
> BoM had already termed due to client Enron request.

[114] 189. About 2:15 p.m., Willie Finnegin ("Finnegin"), the Sales Manager for the Heritage Branch, called Wu into his office. Finnegin told Wu there was just "too much heat" over the e-mail and that UBS had to terminate Wu.

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[533] *See* UBS/LAM 038340-41.

[534] *Id.*

– Pat Mendenhall called. Sen[t] e-mail to around 70 clients about ENRON saying that the stock is not doing well. He also sent out a chart that was not approved. This company is saying they will drop UBS PaineWebber now. Pat spoke to Peter Bado who told Pat REDACTED Pat would like to terminate trainee today.

3:30 w/Bado and BoM.

BoM had already termed due to client Enron request.

190. Around 3:30 CST, Mendenhall sent the following e-mail to Joyce:

> I apologize for how I handled the conversation. I was and still am so upset and frustrated at the e-mail, that I still haven't calmed down. I should have known that if I was this frustrated, that you, as our client, were more so. It is not my intent to hide behind anyone. I take full responsibility and will remedy the situation. We will get your approval prior to any retraction being sent. The Financial Advisor has been terminated. Once again I'm sorry. Thanks. Pat[535]

191. Meanwhile, Fisher had been busy obtaining and delivering the "retraction" that would be sent to UBS's clients. After delivering the letter to Enron to review prior to sending it to UBS's clients, Fisher discussed the issues with his business partner Alan Klenke who, despite being out of town, already knew about the day's events:

AK: What's going on?

BF: Uh . . . just got back from . . . uh . . . the uh . . . whach-a-ma-call-it . . . Enron . . . delivering the uh . . .

AK: Oh yeah, how'd that go?

BF: Uh, fair. Fair.

AK: Who'd you meet with over there?

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[535] UBS/LAM 038047

BF: Uh, Aaron. I bumped right into, guess who?

AK: Mary Joyce?

BF: Yeh . . . so . . . that's a thrill a minute.

AK: What did she say?

BF: Um . . . I don't think she put together who I was until she was halfway down the hall. She was like, "Hi," and I'm like, "Hi. I just want to tell you I'm so sorry." And she was like on a beeline, and she said, "Oh, that's alright." So, like I say, I'm not sure she knew what was up, so . . .

[115] **AK**: What were you delivering, an apology letter?

BF: Yeah, a retraction letter that we were supposed to have an hour prior. We told them four and I ran it over there AT five and uh you know . . .

AK: Retracting Chung's statements?

BF: Yes. Exactly. So, and then I had to figure out how to get a.pdf copy of the research report, which I did, which everyone said I couldn't do, heh heh. So, now I'm getting ready to e-mail all 80 people, the "So Sorry" list . . .

AK: The.pdf of . . .

BF: Exactly. So, anyhow, how's your day been?

(Conversation unrelated to Wu issue)

BF: Alright, I'm in the middle of trying to get this dang e-mail out to them timely. What

else, what else happened? I'm in Chung's office right now.

AK: Uh, are you really?

BF: And I ran into him on the way back from there but I was on the phone and he was with his wife or something and he just kind of waved, with a dumb look on his face. So . . .

AK: What did he say? Any reports on his . . .

BF: Nah. He's sorry. It was late and he wanted to get it out. He knew he should have got it Compliance approved, but . . . **He said, "It's factual," which it probably is but, uhm, you know, you just don't say it** . . .

AK: **Yeah, you don't do that** . . .

192. UBS's response to Enron's demands is part of the "white glove" treatment Fisher testified that he believed in giving Enron.[536] He explained that, aside from the "gentlemen's agreement," "white glove" treatment meant the following: "If [Aaron Brown] was angry because it was raining, I would carry over an umbrella."[537] The retraction prepared as part of this "white glove" treatment of Enron, which Fisher hand delivered to Enron at 5:00 p.m. on [116] August 21,

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[536] *See* UBS/LAM 043296-339 Oral Deposition of V. Robert Fisher, Jr. dated August 19, 2003 in *Wu v. Olson, et al.,* Cause No. 2002-42447 in the 127th District Court of Harris County, Texas at p. 56.

[537] *See id.*

2001, was the following letter from Mendenhall (but, drafted by UBS's in-house counsel):

August 21, 2001

Re: Recent E-Mail Concerning Enron

I have just learned that former UBS PaineWebber Financial Advisor, Chung Wu, sent an e-mail dated August 21, 2001, to certain Enron employees and former Enron employees concerning Enron. Foremost, I wish to apologize for Mr. Wu's statements. To the fullest extent possible, on behalf of UBS PaineWebber, I hereby retract Mr. Wu's statements.

Please be assured that the e-mail was not approved by UBS PaineWebber management and was sent in violation of UBS PaineWebber policies. Mr. Wu's statements are contrary to UBS PaineWebber's current recommendation concerning Enron stock. Specifically, UBS PaineWebber analyst Ron Barone has a strong buy recommendation on the stock. Attached for your reference is a recent copy of our latest Research Note from August 17, 2001.

With Enron's approval, UBS PaineWebber will send copies of this letter to each of the Enron employees and former employees to whom Mr. Wu's email was sent.

[Spoke w/Bobby Fisher on 8/21 @ 5:18 pm]

Again, I sincerely apologize for Mr. Wu's actions and any inconvenience it has caused.

Very truly yours,

/s/ Patrick N. Mendenhall
Patrick M. Mendenhall
Sr. Vice President
Branch Manager

193. Enron produced the copy of the original letter Fisher delivered to Brown, complete with an editorial delete sign next to the paragraph that said, "With Enron's approval, UBS PaineWebber will send copies of this letter to each of the Enron employees and former employees to whom Mr. Wu's e-mail was sent[,]" and the note on the bottom in the handwriting of Bernadette Etienne ("Etienne"), Brown's secretary at Enron. The notation says, "Spoke w/Bobby Fisher on 8/21 at 5:18 p.m." Etienne has testified that (1) the editorial delete symbol on the letter was typical of those used by Joyce at Enron; (2) the note on the bottom of the letter is typically the way she notes any action she is instructed to take by Joyce or Brown, and (3) the [117] note regarding Fisher more likely than not means that she spoke with him about the deletion of the paragraph because, had she been unable to reach him, her practice would have been to note the fact that she did not talk to him on the document.

194. At 6:22 p.m. CST, without ever reviewing the holdings, investment objectives, or any other information concerning those UBS clients who received

Wu's recommendation to sell Enron stock, Mendenhall retracted Wu's sell advice by e-mailing the text of the foregoing apology letter to those UBS clients, but with the noted sentence excluded per Joyce's instruction.[538] In the area where that sentence was deleted, Mendenhall linked the electronic file of UBS's current research report for Enron, including UBS's "Strong Buy" rating on the stock. The effect of UBS's "Strong Buy" on its clients in general is seen by how these particular UBS clients responded to the retraction.[539] Mendenhall has testified that not one recipient of UBS's retraction e-mail took Wu's advice to sell their Enron securities.

195. Mendenhall also sent a copy of the retraction e-mail to Joyce.[540] The next morning Joyce responded to Mendenhall's e-mails with an e-mail stating: "This is great. Thanks."[541] About ten minutes later, she sent another e-mail to Mendenhall, and copied it to Brown: "Keep this e-mail and if we get any inquiries, please send this. Don't think we need to send to the HR Vps as yet. Let me know if any call."[542]

196. Hunt was also in the business of providing "white glove" service to Enron and wanted to make certain his Enron contact knew of Wu's termination. Hunt e-mailed Donahue to inform him that the "rogue broker" had been fired and that UBS retracted Wu's

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[538] *See* UBS/LAM 038307-08.

[539] *See id.*

[540] *See* UBS/LAM 038324-25.

[541] *See* UBS/LAM 038326-27.

[542] *See* UBS/LAM 038328.

e-mail to its clients, apologized, and sent Barone's "Strong Buy recommendation piece" to those UBS clients [118] instead.[543] Further, Hunt's daily calendar from August 24, 2001 indicates a telephone conference between he and Mendenhall.[544] After the conversation, Mendenhall sent Hunt an e-mail forwarding the retraction that UBS had already sent to Wu's clients.[545] In turn, Hunt forwarded Mendenhall's e-mail to Donahue along with an explanation.[546]

197. UBS's "Strong Buy" rating on Enron stock never wavered until just days prior to Enron's bankruptcy, thus preventing UBS's Financial Advisors from giving any information during that period other than a "Strong Buy" recommendation.[547] On November 29, 2001, the day after UBS downgraded its rating on Enron stock from a "Strong Buy" to a "Hold," UBS's senior global credit officer Dick Asjes noted his embarrassment by the press associated with the late downgrade.[548] Late, indeed. This action came on the same day Enron lost its investment grade credit rating with the rating agencies and the same day UBS downgraded Enron to D2, just above UBS's absolute worst internal credit rating.

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[543] *See* UBS/LAM 526676-77.

[544] *See* UBS/LAM 030817.

[545] *See* UBS/LAM 526678-82.

[546] *See* UBS/LAM 526683-87.

[547] *See* UBS/LAM 038630-31.

[548] *See* UBS/LAM 068560-61.

XV. UBS's FRAUD WAS IN CONNECTION WITH A SECURITIES TRANSACTION

198. Long ago the Supreme Court instructed that the "in connection with" language in § 10(b) and Rule 10b-5 must be read broadly and flexibly. *See Superintendent of Ins. of N. Y. v. Bankers Life & Casualty Co.*, 404 U.S. 6 (1971). In *SEC v. Zandford*, the Supreme Court held that Section 10(b)'s "in connection with" requirement is satisfied where a defendant's activities "coincide" with the purchase or sale of a security. 535 U.S. 813, 820 & 825 (2002); *Accord Merrill Lynch, Pierce Fenner & Smith, Inc. v. Dabit*, 547 U.S. 71, 85 (2006); *United States v. O'Hagan*, 521 U.S. 642, 656 (1997). This element of Plaintiffs' claim is easily met because the [119] alleged violation of Section 10(b)/Rule 10b-5 is UBS's failure to disclose its knowledge of the financial manipulations at Enron at the time Plaintiffs purchased Enron securities within the parameters of their relationships with UBS. In other words, not only is the nonrepresentational act "in connection with" the purchase of a security, the nonrepresentational act runs afoul of § 10(b) with respect to each member of the class at the moment each member purchased an Enron security.

XVI. UBS's FRAUD CAUSED PLAINTIFFS' ECONOMIC LOSSES

A. Background

199. Under Rule 10b-5(a) and (c), Plaintiffs must show both that their economic loss was foreseeable and

that it was caused by the materialization of the concealed risk. *See Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 173 (2nd Cir. 2005), *cert. denied*, 126 S. Ct. 421 (2005). "[T]he loss causation requirement will be satisfied if such conduct had the effect of concealing the circumstances that bore on the ultimate loss." *In re Parmalat Sec. Litig.*, 376 F. Supp. 2d 472, 510 (S.D.N.Y. 2005). If a plaintiff fails to demonstrate a causal connection between the content of the alleged nondisclosure and the harm actually suffered, a claim for fraud will not lie. *See Lentell*, 396 F.3d at 174. This is because the loss-causation requirement, akin to the foreseeability limitation in tort, is intended to fix a legal limit on a person's responsibility, even for wrongful acts. *See id.* at 172-74. As this Court recognizes, the concept of proximate cause is simply causation substantial enough and close enough to the harm to be recognized by the law.[549] A given proximate cause need not be, and frequently is not, the exclusive proximate cause of the harm.[550]

200. In *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005) the Court considered the sufficiency of the plaintiffs' pleading of loss causation, i.e., the causal connection [120] between the prohibited conduct and the loss. In rejecting the sufficiency of allegations that a plaintiff purchased a security at an inflated market price due to the defendant's fraud, the Court adopted an efficient market argument, noting

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[549] *See* this Court June 5, 2006 Order (*Newby* #4735) at p. 99 (citing *Sosa v. Alvarez-Machain*, 124 S.Ct. 2739, 2750 (2004)).

[550] *See id.*

that at the moment a plaintiff purchases the relevant security, the security has the exact value the plaintiff paid for it, whether that value was legitimate or not. In an efficient market environment, if the value of the securities changed, as reflected by a move in the price of the securities, then the market necessarily took into account some new information. The Court's opinion in *Dura* focused on the necessity of analyzing that new information and connecting it to the complained of acts. In other words, a loss causation analysis does not focus on how the price became inflated. Instead, a loss causation analysis focuses on the subsequent deflation of the price and the information made available to the market concurrent therewith to determine if there is a connection between the two. Thus, a plaintiff must demonstrate through its allegations the new information made available to the market and its connection to the conduct prohibited by Section 10(b). Only if the new information is related to the prohibited conduct can the prohibited conduct be considered to have caused a change in the price of the securities. In this case, then, the pertinent loss causation questions regarding UBS's conduct are: (1) was it foreseeable to UBS that the Plaintiffs could lose their investment in Enron securities if the markets discovered that, as alleged, Enron engaged in transactions in order to report, and did report, its financial results in a materially misleading way, and (2) are the Plaintiffs' economic losses in fact connected to the allegation that Enron engaged in transactions in order to report, and did report, its financial results in a materially misleading way.

B. Enron's Bankruptcy was Foreseeable to UBS

201. Enron's trading business was the perceived core value in Enron. The market perceived Enron as having substantial comparative advantages in trading, hedging, and structuring transactions involving various energy and related commodities such that these [121] activities allowed Enron to earn abnormal and sustainable profits with only limited capital. Enron's trading group, known as Enron Wholesale, was therefore valued at a significant multiple of operating income.

202. The problem with the reported earnings in Enron Wholesale was that they lacked "transparency." What Enron reported as operating income within Enron Wholesale included a substantial amount of mark-to-market accounting adjustments. Such accounting gains are often subjective in nature and can be extremely unreliable, and Enron refused to provide detailed breakdowns of positions and profitability by segments at the level necessary for analysts to understand Enron Wholesale.

203. Concerns regarding the lack of transparency of Enron's earnings existed throughout the 1990's. In fact, UBS's own internal analyses of Enron in the late 1990's reflect a concern that Enron's financial reports were "unclear" and "weak." However, analysts and investors looked for signs of abuses and test the quality of earnings by examining carefully the reported operating cash flows (to see if they correlate

well and match earnings) and balance sheet. Enron was able to counter investor and analyst concerns regarding its earnings quality by misrepresenting, as discussed through transactions described in detail herein, its operating cash flows and its total leverage (effective debt-to-equity ratio and level of interest expenses relative to reported operating earnings). As Enron was able to maintain the impression of quality, sustainable earnings matched by reported operating cash flows between 1995 and 2000, investors and analysts increasingly lost some of their skepticism and began to afford full values and multiples of operating income to reported operating income from Enron Wholesale's activities. In other words, Enron appeared to investors and analysts to be consistently converting its reporting trading profits in Enron Wholesale into operating cash flow. In reality, from 1997 [122] onward, Enron's trading business was experiencing losses (in a tax accounting sense) and was experiencing negative operating cash flows. Enron was insolvent by December 1998 (at least on a cash flow and undercapitalization basis) and the true value of its common shares from this point in time forward was less than one dollar.

204. Enron's ability to maintain an investment grade rating was an ultimate issue. Upon the loss of its investment grade rating, Enron would realize a credit or "death" spiral because it would have to post substantial additional collateral to support its trading positions at a time when its primary source of reported earnings would be lost. In order to restructure to

provide adequate liquidity in such a situation, Enron would have been forced to begin disposing of assets and realizing their true values. The market was particularly concerned about the quality and lack of transparency of Enron's earnings throughout the second half on [sic] the 1990's such that even modest shortfalls in Enron's financial performance, including its reported operating cash flows and debt levels, were material to investors and analysts. Just removing the transactions in which UBS was involved would have resulted in significant reductions in operating cash flows, increases in interest expenses and debt levels, and/or changes in key credit rating criteria (e.g., funds from operations relative to interest and debt; EBIDTA relative to interest and debt; debt to capital), resulting in a reduced Enron credit rating.

205. A reduction in Enron's credit rating even one or two notches would have reduced Enron's access to capital, increased Enron's cost of debt, and significantly impaired the levels of earnings and revenues in Enron Wholesale, as counterparties and creditors would have perceived greater risks in trading with or lending to Enron. UBS knew (as reflected in UBS analyst reports, Enron's various SEC filings, and Hunt's handwritten notes) that Enron's trading operations were highly dependent on Enron maintaining a "safe" investment grade credit rating and a certain [123] stock price level. Given this public knowledge coupled with the non-public knowledge UBS had regarding Enron's financial manipulations, as set forth in detail herein, the bankruptcy of Enron was absolutely a

foreseeable consequence of a realization by the market that Enron engaged in transactions in order to report, and did report, its financial results in a materially misleading way. UBS's documents prove the truth of this allegation.

206. Verna testified that in the marketplace, "ethic issues carry a lot of weight."[551] In August 2001 Daniel Coleman, the head of UBS's equities trading in the Americas, sent the following e-mail, which presumes how the market would react to learning that Enron manipulated its financials:

----Original Message-----
From: Coleman, Daniel
Sent: Thursday. August 16, 2001 12:28 PM
To: Lee, Christine; Glockler, Christopher
Cc: Bane, Bill; Collins, Michael; Frieman, Adam; Hunt, Jim+ Mundt, Trevor; Spencer, Annette; Riddell, Gary; Glass, Tobin, John; Steele, Timothy
Subject: RE: Re: Potential Trigger Unwind Event for Enron Forwards – IM

> Hi,
>
> Our exposure is about $390mm notional; short about 5.11mm 19 strike puts. We sold these puts for 0 premium. This short put position will begin to hit our stress loss limit. This put position will begin to have some impact on our ability to commit capital across all products.
>
> For the record, I am concerned that ENE has rapidly created a trading business that focuses on

[551] *See* Verna Deposition at p. 109.

> exotic structures in illiquid markets. It reminds me of Cargill's push into emerging market trading in the late 1990s. ENE would not be the first firm to blow up due to exotic derivative exposure. I think the fear on the street is that the resignation of the CEO reflects more than the telecom bubble bursting.
>
> If the stock falls through the new trigger. I would not be inclined to support a lower trigger unless ENE increased its authorized shares or decreased its swap exposure with other counter parties having the same effect.
>
> Daniel

207. Frieman described Coleman's message as a comment on the fundamental business Enron had moved into,[552] and Glass similarly described the e-mail as communicating Coleman's concern that Enron's operation of a trading business within an information void made the [124] appearance that Enron was actually making money in this business questionable.[553] Glockler candidly provided the context for Coleman's e-mail in the following testimony:

> my recollection was that there was a concern that Enron was largely a financial and trading driven business, they had a very large energy and other product trading businesses, relatively unusual for a non-financial institution, and that they were more like a financial institution than a traditional corporate

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[552] *See* Frieman Deposition at p. 218.

[553] *See* Glass Deposition at p. 306.

> counterparty. I think there is a history of corporations who attempt to grow – and financial institutions who attempt to grow trading businesses, particularly those that use derivatives, be they energy or various other things, of those transactions turning out to be very difficult to liquidate in a hurry. So when a derivatives trading firm has a financial or a liquidity problem or when the market loses confidence in the firm, it can – liquidity problems can escalate very quickly.[554]

208. In late October 2001, Glockler made essentially the same comments to Bawden, Riddell, and Glass. Glockler attributed the fall in Enron's stock price to that point to "a massive loss of credibility and confidence among investors, and increasingly creditors."[555] Glocker went on to note that the "key danger now is the spread of the contagion to the company's energy trading counterparties[,]" as the "complexity, nontransparency and (as lately revealed) often secretive nature of Enron's business and financial practices has exacerbated the vulnerability."[556] These UBS officers are forced to admit that in 2001 they understood the nature and demands of Enron's business, the historic risks associated with this type of business, and the inevitable result to companies engaged in this type of business when market and counterparty confidence is lost. In other words, UBS executives are forced to admit they were aware both of Enron's sensitive

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[554] Glockler Deposition at p. 103-04.

[555] *See* UBS/LAM 056336.

[556] *Id.*

relationship to the market and the catastrophic result driven by a liquidity crisis if the market ever learned Enron manufactured intentionally misleading financial reports.

[125] **C. The Event Study Performed by Scott D. Hakala, Ph.D, CFA Shows Plaintiffs Realized Losses As the Market Reacted to Concerns that Enron Engaged in Transactions in Order to Report, and Did Report, Its Financial Results in a Materially Misleading Way**

i. Background of Dr. Hakala's Event Study

209. An event study is based on a market model, which itself is a model of how the price of a security moves in response to news and information in relation to a market index and/or an index of peer group companies. Dr. Hakala's [sic] performed an event study composed of three stages: (1) the identification of material events; (2) the identification and analysis of possible market indices and guideline or peer group companies relative to the returns of Enron's shares; and (3) analyzing the candidate events in an integrated event study regression that explicitly corrected for changes in volatility during various time periods over the study period. Dr. Hakala's event study summary is attached hereto as Exhibit "1" and incorporated herein by reference. Also, Dr. Hakala's Enron Share Price and True Value Calculation is attached

hereto as Exhibit "2" and incorporated herein by reference.

210. The event study summarized in Exhibit "1" is based on the returns generated by Enron's common shares on a daily basis from October 4, 1999 through December 3, 2001 (the "Study Period"). The market model portion of Dr. Hakala's analysis is based on a broader market index, the Standard & Poor's 500 Index (SPX) and two narrower industry indices. The first narrow index (SUBINDEX) was created based on an equally weighted geometric index from the returns of four integrated energy companies: Duke Energy Corporation (DUK), Public Service Enterprise Group (PEG), Dominion Resources Inc. (D), and FPL Group, Inc. (FPL). The second industry index (GASINDEX) was created based on an equally weighted geometric index from returns of three companies engaged in energy production and transportation activities: National Fuel Gas Company (NFG), Questar Corporation (STR), and Kinder Morgan Inc. [126] (KMI). Collectively, the three indices were extremely significant and jointed explained approximately 28.7% of the daily variance in Enron's stock price returns on non-event days during the Study Period. Each index was statistically significant by itself in explaining the movements in Enron's share price. Dr. Hakala then combined the three indices, SPX, SUBINDEX, and GASINDEX, using the coefficients from the event regression analysis to produce a Composite Index that provided a predicted movement in Enron's share price on each

observation day and was used as the reference point for determining inflation per share and damages.

ii. Discussion of the Events and Their Relationship to UBS's Conduct

a. The Build Up of an Inflation Component in the Price of Enron Stock

211. In October and November 1999, Enron's share price was relatively stable. On November 9, 1999, Moody's raised Enron's debt rating to positive from stable and other positive news led to a modest increase in Enron's share price. Jeffries also upgraded its recommendation to buy from accumulate. This event is relevant in that, had the true facts about Enron's accounting been known, the debt rating would not have improved. On November 24, 1999, news of a purchase of Columbia Energy Group's wholesale energy market operations to Enron combined with other news to lift Enron's share price.

212. In the later part of November and in early December 1999, Enron's share price fell along with other gas companies over general market concerns. Barone, then of PW, reduced his estimates for three natural gas suppliers on December 9, 1999, but recommended "focus on a handful of fundamentally solid names" with Enron mentioned as one of three companies expected to "lead the industry, heading out this storm." As a result of this reassuring comment, Enron's share price rose significantly 7.66% relative to

the Composite Index. This event [127] demonstrates the importance of Barone's coverage of Enron as a noted and widely quoted analyst covering the gas industry.

213. On December 17, 1999, news of a bandwidth contract, and possibly news of the Nigerian barges, led to another significant increase in Enron's share price. These events had the effect of inflating Enron's share price and contributed to a significant increase in Enron's share prince [sic] in December 1999 during a period when the Composite Index and peer indices were either declining or relatively flat from mid-November to the end of 1999.

214. In January 2000, Enron's share price rose again as a result of a combination of expected increases in earnings associated with Enron Wholesale's trading operations and news regarding Enron's foray into the broadband trading business. On January 5, 2000, Enron's share price significantly increased on news of an investment related to the broadband business and a CIBC report anticipating improvements in Enron's balance sheet following the sale of PGE. On January 12, 2000, Enron's share price rose again on a positive analyst report by Schroeder and additional news regarding Enron's broadband and wholesale businesses. This increase was based on the assumption of profitability and positive cash flows in Enron's trading and development businesses. Enron could not have credibly entered new markets and created expectations for additional value creation without an investment grade

rating and/or had the true facts been disclosed regarding Enron's financial performance.

215. Enron then reinforced the share price increases on January 5 and 12 with an analyst conference on January 20, 2000, countering some of the concerns that had developed in the interim. Enron's share price increased 24.53% relative to the Composite Index on January 20. While Enron Broadband was a focus of the conference, with news of a new pact with Sun Microsystems, a primary reason for the share price increase on January 20 was Enron's bullish [128] forecast of growth in Enron Wholesale and Enron Retail due to increasing deregulation, increased contract volumes, and growth in the North American power market.

216. Duff & Phelps (DCR) responded the following day, January 21, 2000, with a reaffirmation of Enron's credit rating and raising Enron's outlook from stable to positive. Primary reasons cited for the improved outlook were the "steadily improved . . . company's credit profile based on the increase in Enron's funds from operations interest coverage (FFC/Interest), continued improvement in Enron's 'cash flow measures,' the 'expectation of continued cash flow improvement,' the 'low relative levels of leverage,' and the 'conviction of ENE's credit conscious management to continue to improve ENE's credit profile into the 'A' category.'" DCR noted that Enron's "potential for positive upward ratings movement will hinge on the realization of cash flow improvement and a high degree of confidence that cash flow improvement is sustainable

over the long term." In fact, Enron's true credit profile was deteriorating and the perception of improving cash flows and upside cash flow potential was entirely a consequence of Enron's use of off-balance sheet devices and prepays to misreport cash from financing as cash from operations, to hide debt, to understate current interest expense levels, and to inflate revenues and earnings, as detailed herein.

217. On January 24-25, 2000, Enron's share price pulled back considerably on news of the "tepid" response to Enron's weather bonds and on general concerns that Enron's share price might have advanced upward too quickly over the past month. However, news of another "data deal" with Sycamore Networks further boosted the share price of Enron on January 31, 2000. An analyst's concerns regarding the rapid increase in Enron's share price led to another downward correcting in Enron's share price on February 1, 2000.

[129] 218. Between February and July 2000, Enron's share price generally traded between $65.00 and $75.00. Despite the significant increase in the trading prices of certain Internet (dot.com) and technology stocks and the sympathetic increase in the NASDAQ Composite Index between the middle of February and March 2000, as well as the rapid declines in Internet and technology stock prices and the SPX between early April 2000 and July 2000, Enron's share price was comparatively stable during this time period. Except for certain periods in March and a few days in April 2000, Enron's share price more closely followed the SPX than a technology/Internet stock index, an

indication that the increase in Enron's share price in December 1999 and January 2000 was not solely due to news of Enron's broadband initiatives and was distinct from the Internet technology stock phenomenon. Between December 1, 1999 and July 31, 2000, Enron's share price advanced 95.3% (with 59.4% of the increase realized by January 31, 2000, and over 82% of that increase realized by February 29, 2000). By comparison, the NASDAQ Composite Index increased only 12.3% and the SPX had increased only 2.37% in the same time period. Thus, the share price of Enron was primarily driven by company-specific news and events that were distinguishable from general market and even industry specific trends.

219. Enron's share price fell substantially (6.9% relative to the Composite Index) on March 30, 2000, and substantially again (11.2% relative to the Composite Index) on April 4, 2000, as a result of general concerns and market related events. These declines were primarily attributed to reconsiderations of the prior rapid increase in Enron's share price and general concerns regarding Enron's share price level following the market share price declines. But, on May 2, 2000, Enron's share price rose 7.5% relative to the Composite Index on an announcement of increasing trading volumes on EnronOnline. This event led to expectations of further growth in earnings in Enron Wholesale, which would not have occurred absent the misleading [130] information regarding Enron's financial condition. The share price of Enron then fell modestly on news of a large filing by Enron executive Lou Pai to sell

a large block of restricted shares on May 9, 2000 and rose modestly on news of the Enron's initiative regarding New Power on May 16, 2000. A Hold rating issued by Commerzbank, despite otherwise positive comments, and other investors concerns led to a significant relative share price decline on May 22, 2000. These events are considered relevant in that they relied upon investor expectations that would not have existed had Enron's true financial condition been known and, therefore, would not have occurred assuming knowledge of the truth.

220. The events identified in the event study between June and August 2000 were not significant. Enron's share price traded within a tight (+/- 5%) range consistent with the Composite Index through late July. In the second quarter 2000 earnings announcement, Enron reported meeting expectations and did little to cause investors significant concerns, whereas, in reality, Enron was becoming further insolvent and using additional accounting-driven, noneconomic transactions to overstate earnings and operating cash flows and to hide growing interest expenses and debts. Following this earnings announcement, Enron's share price began to increase in late July and then increased further to $90.00 by August 23, 2000, before declining on August 24, 2000.

221. Enron continued to trade in line with the Composite Index in September 2000, but fell modestly on mixed news events on September 6 and 19, 2000, although neither event was statistically significant. An article in the *Wall Street Journal* on September 20,

2000, in the Texas journal, led to declines in Enron's share price on September 20 and 21, 2000. The *Wall Street Journal* article reflected the existing concerns regarding the previously discussed manner in which Enron accounted for trading activities. In this article, mark-to-market accounting was [131] discussed as a significant component of energy trading companies' earnings and constituted "unrealized, noncash gains" that may result in a "quality-of-earnings issue." The lack of detailed disclosures by energy trading companies meant that the sources and bases for such mark-to-market gains were not adequately understood or appreciated by investors.

222. The September 20, 2000 *Wall Street Journal* article was not included in the event study, as it was viewed as raising concerns about mark-to-market accounting in the energy trading industry more generally and was not sufficiently specific to Enron. The report did cause the share of a number of the gas and utility peers of Enron to experience share price declines and caused a significant decline in Enron's absolute share price over a couple day period. Enron's share price fell from $89.44 on September 18, 2000 to $80.63 on September 21, 2000, but it then recovered between September 21 and 27, 2000.

223. The *Wall Street Journal* article represented latent, but growing concerns among certain sophisticated analysts and investors and helped raise awareness of concerns regarding the quality of earnings within Enron, Dynegy, and El Paso Energy Corp. The article did cause some losses to Enron's shareholders,

but the lack of a statistically significant response to the article is explained in part by Enron's response, as quoted in the article. Enron Chief Accounting Officer Richard Causey explained in the article how "Enron's reported unrealized gains don't depend heavily on gains from long-term contracts that extend beyond the periods for which market quotes are available, reducing the potential for significant revisions. The average length of Enron's risk-management contracts is just two years . . . " Mr. Causey went on to state, "We're getting the cash in quicker than you might think . . . They don't stay unrealized very long." Thus, by pointing to positive operating cash flows and funds from operations reported by Enron [132] over twelve month periods, Enron was able to falsely allay most investors' concerns and suggest that, over time, the mark-to-market accounting tended to reflect real cash earnings.

224. Still, Enron's share price fell in the first half of October 2000. The decline was a result of a series of modest "leakage" events. A decision on the part of Enron International to withdraw a Form S-1 registration statement on October 12, 2000 explained a portion of the decline. Enron's share price then remained relatively stable from mid-October to November 28, 2000. On November 29, 2000, Enron's share price fell 9.9% relative to the Composite Index on a combination of concerns regarding the growing California energy crisis, the slowing rate of deregulation of US power markets, and concerns regarding Enron's ability to meet earnings expectations in the fourth quarter. The decline in the share price continued on November 30,

2000, with additional news of the foregoing concerns. The significance of earnings concerns meant that a portion of the decline represented dissipation of inflation in Enron's share price and, thus, made these two event days partially relevant in analyzing Enron's inflation per share.

225. Insider selling was also identified as contributing to the weakness in Enron's share price beginning in late November through early December 2000. This can be seen in the negative reaction of Enron's share price to a significant insider selling disclosure on December 13, 2000. While generally not focused on any individual trade, insider selling increased significantly in this time period and the nature of the insider selling (change in behavior relative to prior insider selling behavior) was a sell signal to some investors. More positive news regarding the California energy crisis and Enron's Dahbol Project, however, offset the insider trading concerns and allowed the share price of Enron to recover from in the middle and latter half of December 2000.

[133] 226. News regarding Enron, primarily related to the California energy crisis exposure and Dahbol, was generally negative in the first half of January 2001. Enron countered those concerns on January 22, 2001 by misleadingly asserting an increase in fourth quarter 2000 earnings and providing a positive report on Enron Wholesale. This positive, but false, earnings report led to positive analyst reports on January 22 and 23, 2001 that further inflated Enron's share price. Enron's share price recovered to over $80

per share in late January and remained around $80 per share through the first half of February. Then things began to change for Enron.

b. The Dissipation of the Inflation Component in the Price of Enron Stock

227. Enron's share price began a long period of general decline on February 15, 2001. Concerns regarding the effect of the California energy crisis contributed initially to the share price decline, but the significant event was the release of a critical *Fortune* article on Enron. The *Fortune* article was technically released in the March 2001 issue, but it was first widely available on February 20, 2001, with some apparent leakage of the pending article prior to February 20 and more general awareness of the article on the part of investors on February 21, 2001. The *Fortune* article is a common leakage event, where a reporter raises a number of valid questions from a number of sources interviewed prior to the publication such that the company and certain others interviewed become aware of the forthcoming article before it is released and then anticipate a response to its release to counter or mute any negative effect the article might have on the stock price. As a result, the *Fortune* article did not lead to a single, statistically significant event in its initial effect. Rather, it raised issues and concerns that gained greater credibility over time throughout the remainder of 2001. As investors investigated the issues raised in the *Fortune* article, the share price of Enron

fell from $80.00 on February 14 to $68.87 by March 6, 2001 (with the *Fortune* article formally dated March 5, 2001). This represented a cumulative [134] loss relative to the Composite Index of 13.8% over that period of time. As can be seen in the November 2000 to November 2001 price chart in Exhibit "3", Enron's share price began to fall permanently below the peer and Composite Indices starting February 15, 2001 and continued to decline on a relative basis thereafter. This can also been [sic] seen in the loss chart in Exhibit "3" covering the same period of time.

228. The *Fortune* article was more specific and direct in relating general concerns regarding mark-to-market accounting and the lack of transparency of reported earnings by energy trading operations to Enron in comparison with the *Wall Street Journal* article on September 20, 2000. The article stated, "Enron keeps many of the specifics confidential for what it terms 'competitive reasons.' And the numbers that Enron does present are often extremely complicated." An equity strategist at J.P. Morgan was quoted as saying, "Enron is an earnings-at-risk story . . . If it doesn't meet earnings, [the stock] could implode."

229. On March 12, 2001, Enron disclosed the termination of its agreement with Blockbuster. The relative effect of this news was a negative 8.73% on that day, but was partially offset by an analyst upgrade on March 14, 2001 and other analyst support. The reaction to news on March 12, 2001 was partially due to the confirmation of concerns raised in the *Fortune* article. This dissipated some of the inflation in Enron's

share price, as the value of Enron Broadband was based entirely on the misleading financial information regarding Enron Wholesale's cash earnings and Enron's investment grade rating.

230. Further related concerns regarding Azurix on March 16, 2001 and rumors of layoffs in Enron Broadband on March 21, 2001 continued to affect Enron's share price negatively. On March 22 and 23, 2001, Enron's management provided a series of statements reassuring investors that management remained "comfortable" with the previously announced [135] earnings estimates for 2001 and trading volume in Enron's broadband unit continued to increase. These reassurances led to a significant recovery in (and partially reinflating of) Enron's relative share price over those two days.

231. After March 26, 2001, Enron's share price generally fell until early April and then recovered again throughout most of April and early May 2001. Enron's earnings announcement on April 17, 2001 surpassed earnings expectations but initially received a mixed response. Positive analyst commentary and support by UBS, Dain Rauscher, and CSFB analysts all combined to inflate the share price of Enron modestly on April 18, 2001, just shy of statistical significance. But, on May 6, 2001, an Off-Wall Street report was issued raising significant questions regarding the valuation of Enron's shares and suggesting a fair enterprise value of only $26.86 per share. This report was not widely followed by investors and, consequently, only had a modest effect on Enron's share

price on May 7, 2001. A subsequent mention of the report in a May 10, 2001 *TheStreet.com* report, though, lead to more interest and further reduced the share price of Enron. While not statistically significant, this illustrates further the presence and contribution of leakage events on Enron's share price.

232. Speculation of losses, write-downs and disappointing earnings by Enron in the second quarter of 2001 led to a significant relative decline in Enron's share price on May 17, 2001. That speculation was almost entirely offset by an increase in the share price on May 18, 2001 as a result of analyst reports reacting to the news. Still, with these Enron-specific concerns raised, Enron's share price trended downward from May 6, 2001 through mid-June 2001. This downward trend was correlated *in part* with a downward trend in the Composite Index and peer company share prices and was, therefore, partially an industry event. The impetus for this trend related to continuing concerning [sic] regarding Enron's exposure to issues arising from the California [136] energy crisis and declining commodity prices for gas and power. These concerns turned specific to Enron on June 18, 2001, as a combination of negative news events on that day combined to reduce Enron's share price 5.3% relative to the Composite Index.

233. Between June 18, 2001 and July 23, 2001, Enron's share price stabilized and modestly increased as a result of positive earnings expectations and news from Enron. This stabilization and modest price increase occurred despite continuing news regarding the

California energy crisis and allegations of overcharging for power, as seen it [sic] the significant price decline on July 24, 2001 associated with the California Senate moving forward with its contempt citation against Enron.

234. On August 15, 2001, Enron's share price fell significantly in response to the surprise announcement of the resignation of its Chief Executive Officer, Jeffry Skilling. Analysts reiterated in part Enron's claim that the resignation was for personal reasons and did not reflect any concerns with Enron's current financial condition or prospects. Notwithstanding those claims, certain analysts and news reports noted that Skilling's resignation would further lend credibility to questions and concerns regarding Enron's earnings quality and the "aggressiveness" of Enron's operational and financial posture. Further analysis of the resignation suggested that Enron's explanation did not make sense. An August 16, 2001 *Wall Street Journal* article contributed to concerns by suggesting that Skilling's resignation was due in part to Enron's declining share price. As a result, Enron's share price fell even more on August 16, 2001 than on August 15, 2001.

235. The price of Enron's shares stabilized on August 17, 2001. After UBS analyst, Ron Barone met with Enron management, UBS issued a report on that date suggesting that investor concerns relating to Skilling's resignation were overblown and concluding that the share [137] price of Enron was likely heading higher as the dust settles. Additional reports that Enron had met with the rating agencies and its lenders

further contributed to the stabilization of the share price.

236. Despite Enron's and certain analysts' assurances, Skilling's resignation influenced investors negatively. For example, an August 21, 2001 report in *Plat's Oilgram News* stated, "Skilling's exit has renewed a raft of longstanding concerns about Enron, from aggressive accounting to dubious asset values and even corporate governance practices. More than ever, Wall Street and Enron's trade counterparties – just about anybody who buys or sells wholesale natural gas and electricity in the US – are going to question what one observer labeled Enron's 'trust me' business approach." The report went on to discuss concerns of institutional investors and analysts of the "company's complexity" and how "limited disclosures make it impossible to analyze from the outside." Additionally, the report highlighted the ability of Enron to manipulate its mark-to-market earnings and concerns over Enron's ability to set its own valuations and influence its auditor, Arthur Andersen.

237. In September 2001, the highlighted concerns following Skilling's resignation continued to depress Enron's share price. Additionally, news (positive some days, but more negative others) regarding Enron's international projects (Azurix and Dahbol) placed additional downward pressure on Enron's share price. Between September 28, 2001 and October 3, 2001, a series of positive events offset some of the recent losses in Enron's share price. A positive Sanders Morris report, upgrading Enron's shares from a hold to a buy

rating, began this recovery and facilitated an additional share price increase on the next trade day, October 1, 2001. Positive news regarding the Dahbol project and investor sentiment for wholesale energy operations led to another significant increase in Enron's share price on October 3, 2001. This share price increase [138] was then offset by news on October 4, 2001 of Enron's plans to cut its workforce in Europe and news on October 5, 2001 of Enron's possible plans to sell Portland General. By October 10, 2001, with the news of Enron's dividend, Enron's share price had fully recovered from losses realized in September 2001.

238. October 15, 2001 then began a continuous series of relevant corrective (and offsetting) events through November 28, 2001. On October 15, 2001, investors' renewed concerns (leakage) about Enron's forthcoming earnings announcement led to a significant relative reduction in Enron's share price. The actual earnings announcement on October 16, 2001 was negative, but the stock price reaction was muted by the anticipation of the news, which resulted in Enron's share price fall on October 15, 2001. On October 17, 2001, further analysis of the earnings announcement by analysts (including additional questions and clarification) and Moody's notice of a review of Enron's credit rating for possible downgrade led to another modest decline in Enron's share price.

239. On October 18, 2001, Enron's share price fell 8.4% relative to the Composite Index as further disclosures by Enron and analyses revealed more information regarding the announced write-downs and

raised additional questions regarding the connection of Fastow with the subject partnership that led to the write-downs. As more information was revealed and then analyzed, including in a *Wall Street Journal* report, Enron's share price fell an additional 11.9% relative to the Composite Index on October 19, 2001. Focus on Enron's other complex balance sheet vehicles contributed significantly to the October 19th stock price decline.

240. News on October 22, 2001 of an SEC inquiry into certain related party transactions within Enron, combined with additional analyst and news commentaries questioning the "aggressive off-balance sheet transactions," caused Enron's share price to fall another 21.0% [139] relative to the Composite Index. Comments by Ken Lay on October 23, 2001 helped slow the decline in Enron's share price on that day as he reassured investors regarding Enron's commitment to its investment grade rating. Despite Lay's comments, however, Prudential downgraded Enron's shares from hold to sell on October 24, 2001 "because of things that we potentially don't know about the company." The report suggested that management was not being forthright about Enron and led to another 15.9% relative decline in Enron's share price on that date. Positive analyst reports by SSB and Dain Rauscher helped to stabilize Enron's share price on October 25, 2001.

241. On October 26, 2001, Enron's share price fell 5.9% relative to the Composite Index as Standard & Poor's and Fitch both changed Enron's credit outlook

to negative, and Enron disclosed that it had drawn down on committed lines of credit to provide more than $1 billion in cash liquidity. Additionally, news regarding layoffs in Enron's international broadband units spread. The credit concerns led to another 10.3% relative share price decline on the following Monday, October 29, 2001. Moody's then cut Enron's credit rating from Baa1 to Baa2 and warned it may cut it again another notch.

242. On October 30, 2001, Enron's share price lost 17.1% relative to the Composite Index on news of an SEC investigation, additional fears of a credit crunch, and the lack of disclosures from Enron regarding the festering issues weighing on the stock price. Speculation on October 31, 2001 that Enron was nearing a deal for additional financing and considering being acquired caused Enron's price to recover 23.4% in relative value. However, news on November 1, 2001 confirmed the rumor of additional financing but at an amount less than was hoped for. The gain in Enron's share price from October 31st was then lost on November 1st and 2nd. News of Standard & Poor's credit rating downgrade and warning of possible additional [140] downgrades combined with additional confirmations of the SEC investigations to further depress Enron's share price on November 2, 2001.

243. Positive analyst support by CSFB and takeover speculation helped slow Enron's share price decline on November 5, 2001, but news that Enron was seeking additional financing to shore up market confidence led to another 14.2% relative decline in Enron's

share price on November 6, 2001. News of Enron's meeting with banks and leakage of information regarding Enron's credit condition continued to drive down Enron's share price on November 7 and 8, 2001 despite news and rumors of discussions between Dynegy and Enron.

244. On November 9 and 12, 2001, Enron share price advanced on news that Dynegy had agreed to buy Enron Corp. for $7.2 billion in stock. However, a downgrade of Enron's credit rating by Moody's from Baa2 to Baa3 tempered the stock price increase on November 9. News of additional investments by J.P. Morgan Chase and Citicorp, and Dynegy's assurance that it did not foresee any additional damaging disclosures by Enron helped further boost Enron's share price on November 13, 2001. The news of the Dynegy agreement continued to stabilize and slow the decline in Enron's share price between November 14 and 19, 2001 despite continuing leakage of negative news regarding accounting, liquidity, and credibility issues. A November 16, 2001 report by a CSFB credit analyst reducing CSFB's rating on Enron bonds indicated the progressively negative assessments of Enron's prospects during this period of time.

245. On November 20, 2001, Enron filed its Form 10-Q and disclosed additional downward adjustments to third quarter 2001 earnings and began to more fully disclose the extent of its liquidity problems and debt triggers. On November 21, 2001, a warning by Fitch that it may still change Enron's credit rating and its clarification that the BBB-rating was dependent on

the merger with Dynegy combined with concerns that the merger with Dynegy may failed [sic] to [141] close to further depress Enron's share price. This news and other information disclosed late on November 21st continued to press Enron's share price downward on the next trade day, November 23, 2001.

246. Enron's share price fell on November 26, 2001 due to concerns that the merger with Dynegy would have to be renegotiated given that Enron was now worth less than half what Dynegy had originally offered to pay for Enron. This concern was then reflected in a *Wall Street Journal* report on November 27, 2001, suggesting that Enron was willing to cut the price by 40% to close the merger with Dynegy. On November 28, 2001, Dynegy formally announced that it had withdrawn from the agreement to merge with Enron. Fitch, Moody's, and Standard & Poor's all cut Enron's debt rating to junk status, and Enron was forced to limit cash payments to those necessary to support its core operations. Additional information on the dire financial condition continued to be revealed on November 29 and 30, 2001, as Enron's financial condition became increasingly distressed and Enron's ability to support its operations deteriorated.

247. On December 3, 2001, Enron filed for Chapter 11 bankruptcy protection and sued Dynegy for breach of contract associated with the terminated merger. The share price of Enron recovered some of the losses over the prior two days mainly as a result of the hope that the suit against Dynegy might yield some

recovery for the shareholders of Enron post-bankruptcy. The hope for some recovery of value through restructuring in bankruptcy or through successful prosecution or settlement of the suit against Dynegy was not realistic in light of the extent of the fraudulent financial manipulations subsequently discovered in 2002 and thereafter. Thus, the closing share price remained inflated until the inflation dissipated over time in 2002 as the prospects for recovery for Enron's shareholders became remote.

[142] 248. Based on the event study, Dr. Hakala concludes that the corrective events between late November 2000 and November 28, 2001 include strong evidence of leakage consistent with the finance literature. Dr. Hakala explains that leakage, either through direct or general concerns, acts on the inflation in the stock price to dissipate the inflation and correct for the effects of fraud. Given Dr. Hakala's conclusion that Enron was insolvent at least by December 1998, Dr. Hakala further concludes that any events that revealed the true prospects for Enron were simply corrective in nature. Further, Dr. Hakala explains that inflated expectations for Enron's new ventures were contingent on Enron's investment grade rating, financial condition, and successful ventures with Enron Wholesale. In Dr. Hakala's opinion, if the market had understood that Enron Wholesale was not generating cash earnings and Enron was insolvent, then the value of Enron's shares would have collapsed to a distressed price. The events following the October 15 to 19, 2001 disclosures demonstrate that the revelation of even a modest

portion of the extent of Enron's financial manipulations would eventually result in the discovery of Enron's insolvency and the failure of Enron Wholesale to realize any value from its trading operations.

249. Dr. Hakala ultimately concludes that Plaintiffs realized losses in the Class Period through the leakage of information calling into question Enron's accounting and Enron's solvency. These questions all relate to whether Enron engaged in transactions in order to report, and did report, its financial results in a materially misleading way. In short, Plaintiffs were damaged as information that Enron did in fact engage in transactions in order to report, and did report, its financial results in a materially misleading way became discovered, realized, and/or disclosed over time.

[143] **iii. Plaintiffs' Fraud Damages**

250. Dr. Hakala's [sic] measured the losses realized by Plaintiffs' that are attributable to Enron's engaging in transactions in order to report, and reporting, its financial results in a materially misleading way. Dr. Hakala based the fixed income securities damages (for non-convertible securities) on investment losses associated with securities held on or after October 16, 2001. Dr. Hakala reviewed a variety of information on market yields to maturity between January 2000 and December 2002, including various Salomon/Citicorp Corporate Bond indices (the general corporate investment grade index of BIG and the BBB index, as well as the underlying monthly yields to maturity, market

values, and overall returns from such indices) and the Moody's Baa Bond Yield quoted daily by the Federal Reserve. He also considered information on bonds issued by Calpine in 2001 in two tranches during the year and bonds issued by Williams in August 2001. This information all suggested to Dr. Hakala that, absent the relevant events, the market prices for Enron's non-convertible, fixed income securities should have increased slightly on average from any date during the Class Period up to at least October 15, 2001. This result flows from the fact that market yields to maturity for BBB/Baa rated bonds were declining significantly in the relevant period as a result of slowing economic growth in the fourth quarter of 2000 through the third quarter of 2001 and the Federal Reserve's efforts to reduce short-term market interest rates. Generally, because Enron's fixed income, non-convertible securities traded within a tight range until late October 2001 and market yields-to-maturity were stable or declining, the market prices for fixed income securities were stable or increasing in general, and, consequently, damages are limited by and closely associated with the investment losses actually realized in this case. For Enron (non-convertible) debt securities, damages were generally not discernable until October 16, 2001. The prices of Enron's fixed [144] income securities, with few exceptions, were stable or increased slightly from November 6, 2000, through October 14, 2001, and then all declined substantially in a series of steps coinciding with corrective events between October 16 and November 29, 2001. Thus, inflationary losses equal or exceed investment losses for the fixed income securities and

damages for the fixed income securities are simply limited to the investment losses realized (the difference between the price paid and the price sold) for any securities purchased during the Class Period and sold on or after October 16, 2001. If the securities have been retained then an estimated closing price is appropriate based on a 90-day average price after November 28, 2001, which Dr. Hakala limited in this case from November 29, 2001 through December 31, 2001 due to the relatively stable price average involved.

251. For convertible fixed-income securities, investment losses were considered realized damages if the securities were held on or after March 12, 2001. With respect to convertible fixed-income securities, a noticeable price decline occurs on or around March 12, 2001 (consistent with the common shares) and more than 99% of the price decline, as demonstrated in Dr. Hakala's event study, is attributable to inflation.

252. Dr. Hakala calculates damages to the Class in excess of $9.5 million and potentially in excess of $126.5 million.

XVII. THE LAW PRESUMES PLAINTIFFS RELIED ON THE NON-DISLCOSED [sic] MATERIAL FACT

253. In *Affiliated Ute Citizens v. United States,* 406 U.S. 128, 153 (1972), the Supreme Court examined the language of Rule 10b-5 and determined that, unlike cases brought under Rule 10b-5(b), cases brought under Rule 10b-5(a) or (c) did not expressly require

proof of reliance. Instead, it held that in § 10(b) cases based primarily on failures to disclose, reliance on the unknown information may be presumed where such information is material, i.e., where a [145] reasonable investor might have considered it important in his decision to buy or sell securities. *See Affiliated Ute,* 406 U.S. at 153-54 (stating the "obligation to disclose and this withholding of a material fact establish the requisite element of causation in fact"). As confirmed by the Fifth Circuit, where fraud allegations are based on a failure to disclose, as opposed to a fraudulent misrepresentation, a plaintiff is entitled to a rebuttable presumption of reliance. *See Smith v. Ayres*, 845 F.2d 1360, 1363 (5th Cir. 1988), *cert. denied*, 508 U.S. 910 (1993).[557] "The presumption . . . responds to the reality that a person cannot rely upon what he is not told." *Id.*

254. The Fifth Circuit limits the *Affiliated Ute* presumption to cases with claims based primarily on alleged omissions under subsections (a) or (c) of Rule 10b-5. *See, e.g., Finkel v. Docutel Olivetti Corp.*, 817 F.2d 356, 359 (5th Cir. 1987), *cert. denied*, 485 U.S. 959 (1988).

> 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

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[557] A defendant may rebut the *Affiliated Ute* presumption of reliance by showing that a plaintiff's investment decision would not have been affected even if the defendant had revealed the omitted facts. *See Akin v. Q-L Investments, Inc.*, 959 F.2d 521, 529 (5th Cir. 1992).

> to material facts about which the defendant has a duty to the plaintiff to disclose. *Ute*, however, does not require the burden of persuasion to shift in cases where the plaintiffs allege either that the defendant has made false statements or has distorted the truth by making true, but misleading, incomplete statements.

Abell v. Potomac Ins. Co., 858 F.2d 1104, 1119 (5th Cir. 1988), *vacated on other grounds sub nom. Fryar v. Abell*, 492 U.S. 914 (1989). This is such a case. Plaintiffs bring fraud claims against UBS based only on its non-disclosure of the alleged fact that Enron engaged in transactions in order to report, and did report, its financial results in a materially misleading way. In so doing, based on the allegations contained herein, Plaintiffs specifically allege their entitlement to, and dependence upon, the presumption of reliance articulated by the Supreme Court in *Affiliated Ute.*

[146] **XVIII. PRAYER FOR RELIEF**

WHEREFORE, Plaintiffs pray for relief and judgment as follows:

A. Determining this action is a proper class action, and certifying Plaintiffs as class representatives under Rule 23 of the Federal Rules of Civil Procedure;

B Awarding compensatory damages in favor of Plaintiffs and the other class members against Defendants, jointly and severally, for all damages sustained as a result of Defendants' wrongdoing, in an amount to be proven at trial, including interest thereon;

C. Awarding Plaintiffs and the class members their reasonable costs and expenses incurred in this action, including counsel fees and expert fees; and

D. Such other and further relief as the Court may deem just and proper.

_____	_____
Date	Dawn Meade, TBN 13879750, FAN 15180 4635 Southwest Freeway, Suite 900 Houston, Texas 77027 Tel: (713) 961-7770 Fax: (713) 961-5336 Email: dawnmeade@ spencer-law.com

OF COUNSEL:

THE SPENCER LAW FIRM
Bonnie E. Spencer, TBN 06366100; FAN 7343
David L. Augustus, TBN 24036159; FAN 33221
4635 Southwest Freeway, Suite 900
Houston, Texas 77027
Tel: 713-961-7770
Fax: 713-961-5336
Email: bonniespencer@spencer-law.com
Email: davidaugustus@spencer-law.com

ATTORNEYS FOR PLAINTIFFS, Individually and on Behalf of all Others Similarly Situated

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[147] [Certificate Of Service Omitted]