UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

United States Courts
Southern District of Texas
FILED

AUG 12 2005

Michael N. Milby, Clerk of Court

UNITED STATES OF AMERICA,	§	
	§	
Plaintiff,	§	
	§	
v.	§	**Cr. No. H-04-025**
	§	
RICHARD A. CAUSEY, JEFFREY K. SKILLING, and KENNETH L. LAY,	§	
	§	
	§	
Defendants.	§	

DEFENDANT LAY'S REPLY TO THE GOVERNMENT'S RESPONSE TO HIS MOTION TO DISMISS THE SECURITIES FRAUD AND WIRE FRAUD COUNTS

(DEFENSE MOTION NO. 2)

Michael Ramsey
State Bar No. 16521000
Chip Lewis
State Bar No. 00791107
2120 Welch
Houston, Texas 77019
(713) 523-7878
(713) 523-7887 (Fax)

ATTORNEYS IN CHARGE FOR DEFENDANT KENNETH L. LAY

Bruce W. Collins
State Bar No. 04604700
Carrington, Coleman, Sloman & Blumenthal, L.L.P.
200 Crescent Court, Suite 150
Dallas, Texas 75201
(214) 855-3000
(214) 855-1333 (Fax)

George McCall Secrest, Jr.
State Bar No. 17973900
Bennett & Secrest, L.L.P.
808 Travis Street, 24th Floor
Houston, Texas 77002
(713) 757-0679
(713) 650-1602 (Fax)

OF COUNSEL:

Earl Silbert
DLA Piper Rudnick
Gray Cary US, LLP
1200 19th Street, N.W.
Washington, D.C. 20036-2412
(202) 861-6250
(202) 223-2085 (Fax)

TABLE OF CONTENTS

Page

I. INTRODUCTION 1

II. PLEADING "MATERIALITY" ALONE IS NOT SUFFICIENT IN THIS CASE 1

III. THE COURT MAY DETERMINE IMMATERIALITY NOW 2

- A. The Court has everything it needs to decide whether the alleged misrepresentations are immaterial as a matter of law. 2
- B. The Government mischaracterizes Lay's "context" analysis. 3

IV. THIS COURT HAS THE POWER TO DISMISS COUNTS GROUNDED ON STATEMENTS THAT ARE IMMATERIAL AS A MATTER OF LAW 5

- A. Federal Rule of Criminal Procedure 12(b)(2) allows this Court to dismiss an indictment when its factual allegations fail to state a crime. 5
- B. *United States v. Gaudin* does not foreclose the Court from determining that statements are immaterial at this stage of the proceedings. 6
- C. The cases cited by the Government are not on point. 7

V. THE ALLEGED STATEMENTS ARE IMMATERIAL AS A MATTER OF LAW 8

- A. The Government mischaracterizes the "puffing" analysis 8
- B. The Government mischaracterizes *Virginia Bankshares v. Sandberg* 9

VI. COUNTS TWELVE AND THIRTEEN FAIL TO ALLEGE A CRIME WITHIN THE WIRE FRAUD STATUTE 11

VII. CONCLUSION 12

TABLE OF AUTHORITIES

Page

CASES

ABC Arbitrage Plaintiffs Group v. Tchuruk,
291 F.3d 336 (5th Cir. 2002) 2, 7
Basic, Inc. v. Levinson,
485 U.S. 224, 108 S. Ct. 978 (1988)........ 4
Casella v. Webb,
883 F.2d 805 (9th Cir. 1989) 3
Cleveland v. United States,
531 U.S. 12, 121 S. Ct. 365 (2000)........ 12
In re Azurix Corp. Sec. Litig.,
198 F. Supp. 2d 862 (S.D. Tex. 2002) 2, 3, 8
In re Blockbuster Inc. Sec. Litig.,
No. 3:03-CV-0398-M, 2004 WL 884308 (N.D. Tex. Apr. 26, 2004) 3, 9
In re MCI WorldCom, Inc. Sec. Litig.,
191 F. Supp. 2d 778 (S.D. Miss. 2002)........ 3, 10
In re Michaels Stores, Inc. Sec. Litig.,
No. Civ. A. 3:03-CV-0246, 2004 WL 2851782 (N.D. Tex. Dec. 10, 2004) 3, 10
Kapps v. Torch Offshore, Inc.,
379 F.3d 207 (5th Cir. 2004) 3
Kurtzman v. Compaq Computer Corp.,
No. Civ. A. H-99-779, 2002 WL 32442832 (S.D. Tex. Mar. 30, 2002)........ 3, 11
McNamara v. Bre-X Minerals Ltd.,
57 F. Supp. 2d 396 (E.D. Tex. 1999)........ 11
Nathenson v. Zonagen,
267 F.3d 400 (5th Cir. 2001) 3, 9
Neder v. United States,
527 U.S. 1, 119 S. Ct. 1827 (1999)........ 12
Nolte v. Capital One Fin. Corp.,
390 F.3d 311 (4th Cir. 2004) 10
Shaw v. Digital Equip. Corp.,
82 F.3d 1194 (1st Cir. 1996)........ 11
TSC Industries, Inc. v. Northway, Inc.,
426 U.S. 438, 96 S. Ct. 2126 (1976)........ 7
United States v. Boyd,
309 F. Supp. 2d 908 (S.D. Tex. 2004) 5
United States v. DeSantis,
134 F.3d 760 (6th Cir. 1998) 6
United States v. Falkowitz,
214 F. Supp. 2d 365 (S.D.N.Y. 2002)........ 8
United States v. Ferro,
252 F.3d 964 (8th Cir. 2001) 8

United States v. Flores,
F.3d 320, 325 (5th Cir. 2005) 5
United States v. Gaudin,
515 U.S. 506, 115 S. Ct. 2310 (1995) 6, 7
United States v. Jackson,
196 F.3d 383 (2d Cir. 1999) 7
United States v. Jacques Dessange, Inc.,
No. 99-CR-1182-DLC, 2000 WL 280050 (S.D.N.Y. Mar. 14, 2000) 7
United States v. Kay,
359 F.3d 738 (5th Cir. 2004) 5
United States v. Kim,
184 F. Supp. 2d 1006 (N.D. Cal. 2002) 5
United States v. Peterson,
101 F.3d 375 (5th Cir. 1996) 9
United States v. Polychron,
841 F.2d 833 (8th Cir. 1988) 5
United States v. Stern,
No. 03-CR-81(MBM), 2003 WL 22743897 (S.D.N.Y. Nov. 20, 2003) 7, 8
Virginia Bankshares v. Sandberg,
501 U.S. 1083, 111 S. Ct. 2749 (1991) 10, 11

STATUTES

Private Securities Litigation Reform Act 2

RULES

Federal Rule of Civil Procedure 9(b) 2
Federal Rule of Criminal Procedure 12(b)(2) 5

I. INTRODUCTION

The Government is trying to change the subject. Recognizing that it cannot articulate a colorable argument to convince this Court that vague statements like "[Elektro is] not a bad asset, it's a good asset" are material, the Government virtually ignores the arguments presented in Lay's opening brief. Rather, the Enron Task Force wastes considerable energy rebutting arguments that Lay never made -- addressing irrelevant issues such as intent, reliance, and the "bespeaks caution" doctrine. Similarly, the Government manipulates Lay's argument that the alleged misrepresentations must be evaluated "in context" to mean that remote extrinsic evidence must be considered. That is not Lay's argument either.

Rather than responding to Lay's detailed explanation of why each specific alleged misrepresentation cannot survive an objective materiality analysis, the Task Force argues that this Court is powerless to dismiss the counts in the Second Superseding Indictment (the "Indictment") at this stage of the proceeding. In fact, if the Government fails to plead an actionable misrepresentation, and therefore fails to state a crime, this Court may dismiss the Indictment. And in this case, dismissal is appropriate.

II. PLEADING "MATERIALITY" ALONE IS NOT SUFFICIENT IN THIS CASE

The Enron Task Force argues that it need do nothing more than use the magic word "material" in the Indictment in order to proceed to trial. (Response at p. 13) The Government is wrong because the misrepresentations alleged in the Indictment are immaterial and merely labeling them as "material" does not insulate them from dismissal. It is this Court, not the Enron Task Force, that has the final say on whether an alleged misrepresentation is immaterial as a matter of law.

If simply labeling alleged statements as "material" were sufficient to survive dismissal, this Court would not be able to dismiss a securities fraud count in a criminal case even if the

Court concluded as a matter of law that the Government could not prevail. As a result, the Court would be powerless to dismiss allegations supported by fatally vague statements such as that a company's "fundamentals are strong" and that a project possesses "considerable potential both for the community and for the company." In the context of a civil case, however, this Court has held that such statements are not actionable under the same securities fraud statute that is at issue in this criminal case. *See In re Azurix Corp. Sec. Litig.*, 198 F. Supp. 2d 862, 886-87 (S.D. Tex. 2002). The Government's argument -- that the same alleged misrepresentations judged against the same statute may be dismissed in a civil case but not in a criminal case -- defies logic.[1]

Nonetheless, the Government endorses this illogical result and claims that this Court is literally powerless to dismiss even the most frivolous of allegations. According to the Task Force, therefore, an indictment of fraud alleging that a corporate officer misrepresented his golf handicap could not be dismissed as long as the indictment alleged that the statement was "material." In fact, the mere use of the word "material" in an indictment does not strip a court of its power to determine whether alleged misrepresentations are immaterial as a matter of law. If the misrepresentations identified in an indictment are not material, a defendant in a criminal case is entitled to dismissal.

III. THE COURT MAY DETERMINE IMMATERIALITY NOW

A. The Court has everything it needs to decide whether the alleged misrepresentations are immaterial as a matter of law.

Contrary to the Government's argument, this Court need not make "predictions as to the evidence" in order to determine materiality. (Response at p. 21) The Court has before it all that

[1] The Government's contention that civil cases may be distinguished because they apply the pleading standards of the Private Securities Litigation Reform Act ("PSLRA") and Federal Rule of Civil Procedure 9(b) misses the mark. (Response at pp. 17-20) These pleading standards require specificity as to intent and falsity, but these elements are irrelevant to a determination of materiality. *See ABC Arbitrage Plaintiffs Group v. Tchuruk*, 291 F.3d 336, 350 (5th Cir. 2002) (explaining the pleading requirements of the PSLRA and Rule 9(b)).

it needs to evaluate materiality. The alleged statements are quoted in the Indictment, and Exhibits A, B, C, F and G to Lay's opening brief -- the conference call transcripts and transcripts of employee meetings during which the relevant statements were made -- provide the necessary context. Civil courts often dismiss allegations relating to statements that are immaterial as a matter of law with no more information than this.[2] The Government, itself, admits that materiality is judged by an objective standard. (Response at p. 24) If the Court waits until the close of the Government's case to decide materiality, it will have no more information relevant to the materiality inquiry than it has now, even though hundreds of thousands of federal dollars and countless hours of this Court's and jurors' time would have been wasted.

B. The Government mischaracterizes Lay's "context" analysis.

In an attempt to argue that dismissal is premature, the Government misconstrues Lay's explanation that a statement should be considered "in context" by claiming that examining a statement "in context" requires an examination of extrinsic facts and circumstances. (Response at p. 17 n.5) It does not.

Viewing a statement "in context" means examining it in light of other statements made during the same conversation or in the same document. *Kapps v. Torch Offshore, Inc.*, 379 F.3d 207, 211 (5th Cir. 2004) ("We do not find the statement . . . to be materially misleading when read in the context of the prospectus as a whole."); *Nathenson v. Zonagen*, 267 F.3d 400, 422 n.20 (5th Cir. 2001) (examining the materiality of the alleged statements in light of "the document as a whole"); *Casella v. Webb*, 883 F.2d 805, 808 (9th Cir. 1989) (statements made

---

2 *See, e.g.*, *In re Michaels Stores, Inc. Sec. Litig.*, No. Civ. A. 3:03-CV-0246, 2004 WL 2851782 (N.D. Tex. Dec. 10, 2004); *In re Blockbuster Inc. Sec. Litig.*, No. 3:03-CV-0398-M, 2004 WL 884308 (N.D. Tex. Apr. 26, 2004); *Kurtzman v. Compaq Computer Corp.*, No. Civ. A. H-99-779, 2002 WL 32442832 (S.D. Tex. Mar. 30, 2002); *In re MCI WorldCom, Inc. Sec. Litig.*, 191 F. Supp. 2d 778 (S.D. Miss. 2002); *In re Azurix Corp. Sec. Litig.*, 198 F. Supp. 2d 862 (S.D. Tex. 2002).

during an oral presentation must be viewed "in the context of the total presentation"). In this case, Lay's alleged statements should be analyzed in light of other statements made during the analyst calls, employee meeting, and the employee forum.[3]

To view a statement in context, therefore, the Court need look no further than the document or discussion in which the statement was made. Viewing a statement "in context" does not, as the Government claims, include analysis of each and every remotely related fact or circumstance, regardless of its relevance or temporal proximity. If it did, a court would never be able to determine materiality as a matter of law. Of course, courts frequently do precisely that.[4]

In essence, by claiming that remote facts and circumstances must be considered, the Enron Task Force argues that a statement immaterial on its face may be rendered material by remote information. According to the Government's theory, even a statement that is obviously puffery, such as "[our] fundamentals are strong," could not be dismissed because remote information may render the statement material. This theory has no basis in the law. While it is true in certain cases that cautionary warnings in an offering document or SEC filing may render an otherwise material statement to be immaterial, it does not follow that the opposite proposition -- that remote information may transform an immaterial fact into a material one -- is also true. *E.g., Basic, Inc. v. Levinson*, 485 U.S. 224, 238, 108 S. Ct. 978, 987 (1988) (rejecting the view that an undisclosed immaterial fact becomes material solely because the fact was later denied).

---

[3] Although the Government accuses Lay of analyzing the statements out of context, (Response at p. 23, n.10), the opposite is true. When drafting the Indictment, the Government excised statements from their immediate context, even using ellipses when necessary. In paragraph 75 of the Indictment, for example, the Government used ellipses to omit Lay's warning that many of Enron's senior management were financially unable to purchase additional stock.

[4] See the numerous cases cited above in footnote 2.

IV. THIS COURT HAS THE POWER TO DISMISS COUNTS GROUNDED ON STATEMENTS THAT ARE IMMATERIAL AS A MATTER OF LAW.

A. Federal Rule of Criminal Procedure 12(b)(2) allows this Court to dismiss an indictment when its factual allegations fail to state a crime.

This Court has the power to dismiss the Government's defective counts. The Fifth Circuit has approved using Rule 12(b)(2) to dismiss an indictment when a trial is unnecessary. *United States v. Flores*, 325 F.3d 320, 325 (5th Cir. 2005). This approach "avoids the waste of judicial resources that results from 'legally meritless cases being sent to trial.'" *Id.* In the case before this Court, dismissal of some or all of the securities and/or wire fraud counts will reduce significantly the issues to be decided by a jury in this already complicated trial.

In *United States v. Boyd*, this Court recognized that Rule 12(b) vests a court with the authority to determine pretrial whether the facts alleged in an indictment state an offense. 309 F. Supp. 2d 908, 911 (S.D. Tex. 2004). Numerous other courts have also recognized that a criminal indictment should be dismissed pretrial if the indictment fails to allege facts for which criminal liability could be imposed. *See United States v. Kay*, 359 F.3d 738, 742 (5th Cir. 2004) (when analyzing a motion to dismiss an indictment, the court must determine if an offense has been stated); *United States v. Polychron*, 841 F.2d 833, 834 (8th Cir. 1988) ("In order to be valid, an indictment must allege that the defendant performed acts which, if proven, constitute the violation of law for which he is charged. If the acts alleged in the indictment do not constitute a violation of law, the indictment is properly dismissed."); *United States v. Kim*, 184 F. Supp. 2d 1006, 1015 (N.D. Cal. 2002) ("[A]t the motion to dismiss stage the question before the Court is whether the allegations in the indictment, assuming they are true, support a jury finding that [an element of the crime was satisfied]."). There is no reason why the issue of materiality should be treated differently. Nothing prevents the Court from dismissing patently defective counts -- except the Government's desire to try to take advantage of pre-existing

prejudice to confuse the jury into believing that benign comments made by the defendant were significant.

B. *United States v. Gaudin* does not foreclose the Court from determining that statements are immaterial at this stage of the proceedings.

The decision rendered in *United States v. Gaudin* does not change the result. In fact, the Supreme Court explicitly recognized that when the element of materiality fails as a matter of law a court should not submit the issue to the jury.

> Some of the opinions cited by the Government, asserting that materiality was a question of "law" for the judge, appear to have involved either demurrers to the indictment or appeals from convictions in which the case for materiality was so weak that no reasonable juror could credit it -- so that even on our view of the matter the case should not have gone to the jury.

515 U.S. 506, 517, 115 S. Ct. 2310, 2317 (1995).[5] *See also United States v. DeSantis*, 134 F.3d 760, 764 (6th Cir. 1998) (confirming that the issue of materiality should not be submitted to the jury if "no reasonable mind could find a statement or omission to be material").

The sole issue before the Supreme Court in *Gaudin* was whether it was constitutional for a trial judge to decide that a statement was material as a matter of law, rather than submitting the issue to the jury. *Gaudin*, 515 U.S. at 511, 115 S. Ct. at 2314. The Court held that a criminal defendant has the right under the Fifth and Sixth Amendments to submit the issue of materiality to the jury. 515 U.S. at 522-23, 115 S. Ct. at 2320. This does not mean that a court is powerless to dismiss when no reasonable juror could find a statement pleaded in the indictment to be material.

---

[5] The Government attempts to sidestep this portion of the *Gaudin* opinion by parsing between a court's holding of immateriality at the motion to dismiss stage of proceedings and a court's holding of immateriality after the introduction of evidence. (Response at pp. 14 & 15 n.4) According to the Government, *Gaudin* somehow forecloses the former but not the latter. (Response at pp. 14 & 15 n.4) This flawed reading of *Gaudin* has no basis in the opinion.

Attempting to read *Gaudin* in a way more to its liking, the Government relies on dicta stating that the materiality inquiry involves "delicate assessments of the inferences a 'reasonable [decisionmaker]' would draw from a given set of facts and the significance of those inferences to him . . . [and is] peculiarly on[e] for the trier of fact." (Response at p. 14, quoting *Gaudin*) In connection with this comment, however, the *Gaudin* court quoted *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 450, 96 S. Ct. 2126, 2133 (1976), and the Fifth Circuit has recently explained that the relevant text from *TSC Industries* does not prevent a court from holding that a statement is immaterial as a matter of law:

> Plaintiffs argue that it is improper for a court deciding a Rule 12(b)(6) motion to dismiss a complaint on the basis of materiality. We cannot agree with this assertion, so broadly cast. It is well-established that, "[b]ecause materiality is a mixed question of law and fact, it is usually left for the jury." At the same time, as we have recently affirmed, a court can determine statements to be immaterial as a matter of law on a motion to dismiss.

ABC Arbitrage Plaintiffs Group v. Tchuruk, 291 F.3d 336, 359 (5th Cir. 2002). The Government's reliance on dicta in *Gaudin*, therefore, is unfounded.

C. The cases cited by the Government are not on point.

The Government's cases purporting to support its erroneous conclusion fall short. In fact, in *United States v. Jacques Dessange, Inc.*, the court analyzed at the motion to dismiss stage whether a reasonable jury could find the alleged representations to be material, which is exactly what Lay urges this Court to do. No. 99-CR-1182, 2000 WL 280050, at *4 (S.D.N.Y. Mar. 14, 2000). The Government's reliance on *United States v. Jackson* is also misplaced. 196 F.3d 383 (2d Cir. 1999). In dicta, the court explained that the trial court in a pre-*Gaudin* case found a statement to be material as a matter of law rather than submitting the issue to the jury, contrary to the holding in *Gaudin*. *Id.* at 384. Similarly, *United States v. Stern* is wholly inapposite. No. 03-CR-81(MBM), 2003 WL 22743897 (S.D.N.Y. Nov. 20, 2003). The case merely holds that it is irrelevant to the materiality analysis whether the recipient was actually misled. *Id.* at *2.

The remaining cases are hardly resounding. In *United States v. Ferro*, the Eighth Circuit rejected the procedure of holding a pretrial hearing to evaluate the sufficiency of evidence of materiality, not of determining whether a statement is immaterial as a matter of law. 252 F.3d 964, 967-68 (8th Cir. 2001). Moreover, the court acknowledged that other cases had "recognized the possibility that the government's well-pleaded allegation of materiality might be so factually weak as to permit a pretrial determination that no reasonable jury could make the requisite finding of materiality." *Id.* at 968 (emphasis omitted). Finally, in *United States v. Falkowitz*, the court merely commented that "ordinarily" questions of materiality are not decided on a motion to dismiss. 214 F. Supp. 2d 365, 386 (S.D.N.Y. 2002).

V. THE ALLEGED STATEMENTS ARE IMMATERIAL AS A MATTER OF LAW

The Government has tacitly admitted that the alleged misrepresentations quoted in the Indictment do not survive a materiality analysis by making virtually no effort to respond to Lay's specific arguments regarding each alleged misrepresentation.[6] Trying to divert the Court from actually examining each alleged statement, the Government addresses them only in broad strokes.[7] The Government's broad arguments, however, do little to advance its case.

A. The Government mischaracterizes the "puffing" analysis.

The Government rewrites the law to conclude that evidence of intent and falsity may somehow transform puffery into a material statement. To reach this conclusion, the Government creates a unique two-pronged analysis never applied by any court. (Response at pp. 24-25)

---

[6] The Government, however, has clarified that it is not basing any of the counts on an alleged failure to disclose. (Response at p. 28) In light of this concession, the only relevant inquiry is whether the alleged statements -- on their face and in the context -- are immaterial as a matter of law. If so, the counts based thereon must be dismissed.

[7] Although the Government disparages Lay for examining the alleged misrepresentations individually and critically, (Response at p. 23 n.10), this is the appropriate analytical process. *E.g.*, *In re Azurix Corp. Sec. Litig.*, 198 F. Supp. 2d at 880-88 (analyzing, one-by-one, the materiality of the alleged misrepresentations).

First, the Government claims that the universe of statements that may be defined as "puffery" is limited to only forward-looking statements. (Response at p. 24) This is simply not the case. The decision cited by the Government in support of this proposition, *Nathenson v. Zonagen, Inc.*, 267 F.3d 400, 419 (5th Cir. 2001), does not state any such limitation. In fact, the Fifth Circuit defines puffery much more broadly, as "generalized positive statements" and "optimistic generalizations." *Id.* Puffery applies to any vague statement, not merely one that is forward-looking. *See id.* (company's statements that a new drug was "fast-acting" and an "improved formulation" were inactionable puffery).

The Government next argues that a forward-looking statement is material if the speaker has knowledge of its falsity. (Response at p. 24) In other words, the Enron Task Force attempts to import the elements of intent and falsity into the materiality analysis. (Response at p. 24) This is not the law. Intent, falsity, and materiality are separate and distinct elements of a securities fraud count. *See United States v. Peterson*, 101 F.3d 375, 379 (5th Cir. 1996) (listing the elements of securities fraud); *see also Nathenson*, 267 F.3d at 421-22 (dismissing one alleged misrepresentation as immaterial without reaching the issue of scienter); *In re Blockbuster Inc. Sec. Litig.*, 2004 WL 884308, at *7-8, 19-21 (dismissing statements as immaterial despite finding that the plaintiffs' scienter allegations were sufficient with respect to some of the speakers). For the sake of argument, even if the Court assumes that Lay possessed the requisite intent and that the alleged statements were false, it may dismiss the securities fraud counts if it finds that the statements were not material as a matter of law.

B. The Government mischaracterizes *Virginia Bankshares v. Sandberg.*

Similarly, the Enron Task Force's reliance on *Virginia Bankshares v. Sandberg* is misplaced. 501 U.S. 1083, 111 S. Ct. 2749 (1991). First, the *Virginia Bankshares* court interpreted a statute that is not even at issue in this litigation. *Id.* (analyzing whether statements

were actionable under section 14(a) of the Securities Exchange Act of 1934). In any event, the case stands for the unremarkable proposition that a corporate director's statements are not insulated from being material simply because they are opinions. 501 U.S. at 1090-91, 111 S. Ct. at 2757. Lay, however, is not claiming that his alleged opinions are *per se* immaterial, and the Government misconstrues *Virginia Bankshares* by arguing that Lay's status as CEO automatically converts his vague comments into material statements. (Response at pp. 27-28) In fact, there are numerous cases where a CEO's opinions were found to be immaterial as a matter of law. *E.g.*, *In re Michaels Stores, Inc. Sec. Litig.*, No. 3:03-CV-0246, 2004 WL 2851782, at *5 (N.D. Tex. Dec. 10, 2004) (dismissing as immaterial a CEO's statement that "investments we have made in our systems and infrastructure are really starting to pay off"); *In re MCI WorldCom, Inc. Sec. Litig.*, 191 F. Supp.2d 778, 785 (S.D. Miss. 2002) (dismissing as puffery a CEO's statement that "[w]e know how to put companies together and get the most out of them").

To the contrary, a corporate director's opinion is actionable as a material misrepresentation only if, among other things, the subject matter of the opinion is specific and may be verified by objective evidence. *Virginia Bankshares*, 501 U.S. at 1092-95, 111 S. Ct. at 2758-60; *see also Nolte v. Capital One Fin. Corp.*, 390 F.3d 311, 315 (4th Cir. 2004) ("[T]he Supreme Court held that in a securities fraud case, a statement of opinion may be a false factual statement if the statement is false, disbelieved by its maker, and related to matters of fact which can be verified by objective evidence."). In *Virginia Bankshares*, the statements at issue were material because they were tied to a specific dollar figure, the accuracy of which was subject to quantitative verification. 501 U.S. at 1093-94, 111 S. Ct. at 2758-59. That is not the case here.

None of Lay's alleged statements -- whether characterized as opinions or not -- can be conclusively verified by objective evidence because they are mere vague expressions of corporate cheerleading. For example, Lay's alleged characterization of Elektro as "not bad" or

"good" is not tied to a specific dollar figure and is not subject to quantitative verification. *See, e.g.*, *McNamara v. Bre-X Minerals Ltd.*, 57 F. Supp. 2d 396, 414 (E.D. Tex. 1999) (an opinion that a transaction was "fair" was immaterial as a matter of law under *Virginia Bankshares* because it was not linked to a specific dollar figure and was of a vague and unquantified nature).

Additionally, the general nature of the subject matter of Lay's alleged statements differentiates them from the subject matter of the opinions expressed in *Virginia Bankshares*. In *Virginia Bankshares*, the opinions related to the fairness of a merger proposal and recommended a specific course of action to investors. 501 U.S. at 1090-91, 111 S. Ct. at 2757. In contrast, the alleged statements in the Indictment -- such as "the balance sheet is strong" and "we have record operating and financial results" -- are mere corporate cheerleading of the type "commonly heard from corporate managers and numbingly familiar to the marketplace." *Kurtzman v. Compaq Computer Corp.*, No. Civ. A. H-99-779, 2002 WL 32442832, at *17 (S.D. Tex. Mar. 30, 2002) (quoting *Shaw v. Digital Equip. Corp.*, 82 F.3d 1194, 1217 (1st Cir. 1996)). Such statements are immaterial and the Indictment counts related to them should be dismissed.

VI. COUNTS TWELVE AND THIRTEEN FAIL TO ALLEGE A CRIME WITHIN THE WIRE FRAUD STATUTE

Similar to its response to Lay's securities fraud arguments, the Government answers Lay's explanation of the wire fraud counts by responding to arguments that Lay never made. For example, Lay is not arguing that the wire fraud counts should be dismissed because the Government has not identified a victim who *made a decision* that resulted in a loss. (Response at p. 37) Rather, Lay relies on the language of the wire fraud statute and case law to explain that a statement is material only if, at a minimum, it *is capable of* influencing a reasonable recipient's decision or course of action. *Neder v. United States*, 527 U.S. 1, 25, 119 S. Ct. 1827, 1841 (1999). The Government's failure to identify a potential decision is fatal to its case. For example, if the Government were arguing that Lay's alleged statements were material because

they would have been significant to a reasonable person's decision to buy a new television, the materiality element would fail as a matter of law because no jury could find that a reasonable person would have viewed Lay's statements as significant in making this decision.

The Government is similarly off base when it argues that it is "beside the point" whether the object of the alleged fraud was money or property. (Response at p. 38) This issue is directly on point. Not all schemes to defraud are within the scope of the wire fraud statute.[8] The alleged scheme must seek to defraud someone of money or property. *Cleveland v. United States*, 531 U.S. 12, 26-27, 121 S. Ct. 365, 374 (2000). As explained in Lay's opening brief, if the Government is contending that Lay engaged in a scheme to convince employees to purchase or hold Enron stock, such a scheme is not within the scope of the wire fraud statute because an employee who purchases or holds Enron stock is not deprived of "money or property." (Defense Motion No. 2 at pp. 29-32) The Government ignores completely this glaring weakness in its case, and once again pretends that Lay made an argument more to its liking -- that reliance is an element of wire fraud. (Response at pp. 38-39) The Government's discussion of reliance is irrelevant. Counts twelve and thirteen must be dismissed.

VII. CONCLUSION

The allegations in the Indictment fail to state an actionable securities fraud or wire fraud count. Lay respectfully requests that this Court dismiss Counts 12, 13, and 27 through 30.

---

[8] For example, a scheme to fraudulently obtain a video poker license from a state is not within the scope of conduct criminalized by the wire fraud statute. *Cleveland v. United States*, 531 U.S. 12, 26-27, 121 S. Ct. 365, 374 (2000).

Respectfully submitted,

MICHAEL RAMSEY
State Bar No. 16521000
CHIP LEWIS
State Bar No. 00791107
2120 Welch
Houston, Texas 77019
713-523-7878
713-523-7887 (Fax)

BRUCE W. COLLINS
State Bar No. 04604700
CARRINGTON, COLEMAN, SLOMAN
& BLUMENTHAL, L.L.P.
200 Crescent Court, Suite 1500
Dallas, Texas 75201
214-855-3000
214-855-1333 (Fax)

GEORGE McCALL SECREST, JR.
State Bar No. 17973900
BENNETT & SECREST, L.L.P.
808 Travis Street, 24th Floor
Houston, Texas 77002
713-757-0679
713-650-1602 (Fax)

Attorneys for Defendant,
Kenneth L. Lay

Of Counsel:

EARL SILBERT
DLA PIPER RUDNICK GRAY CARY US LLP
1200 19th Street, N.W.
Washington, DC 20036-2412
202-861-6250
202-223-2085 (Fax)

NO CERTIFICATE OF CONFERENCE NECESSARY

CERTIFICATE OF SERVICE

I, the undersigned, hereby certify that on this 12th day of August, 2005, a true and correct copy of the foregoing Defendant Lay's Replly to the government's Response to his Motion to Dismiss the Securities Fraud and Wire Fraud Counts has been delivered to the following, via email:

Daniel M. Petrocelli (DPetrocelli@OMM.com)
Mark Holscher (MHolscher@OMM.com)
O'MELVENY & MYERS, L.L.P.
1999 Avenue of the Stars, 7th Floor
Los Angeles, CA 90067-6035

Ronald G. Woods (RonWoodsLaw@aol.com)
5300 Memorial, Suite 1000
Houston, TX 77007

Reid H. Weingarten (Rweingarten@steptoe.com)
Mark J. Hulkower (mhulkower@steptoe.com)
STEPTOE & JOHNSON, L.L.P.
1330 Connecticut Avenue, NW
Washington, DC 20036

Sean Berkowitz (Sean.Berkowitz2@usdoj.gov)
Robb.Adkins (Robb.Adkins@usdoj.gov)
John Hueston (John.Hueston@usdoj.gov)
Kathy Ruemmler (Kathy.Ruemmler2@usdoj.gov)

Michael Ramsey

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

UNITED STATES OF AMERICA,	)	
	)	
v.	)	Cr. No. H-04-25 (S2)
	)	
RICHARD A. CAUSEY,	)	
JEFFREY K.SKILLING	)	
AND KENNETH L. LAY,	)	
	)	
Defendants.	)	

NO ORDER NECESSARY WITH THIS FILING