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

UNITED STATES OF AMERICA,	§	
Plaintiff,	§	
	§	
v.	§	**CR. NO. H-03-363 (Werlein, J.)**
	§	
DANIEL BAYLY,	§	
JAMES A. BROWN, and	§	
ROBERT S. FURST,	§	
Defendants	§	

JAMES A. BROWN'S MOTION TO DISMISS INDICTMENT

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MOTION TO DISMISS THE INDICTMENT

This motion is dispositive of this case as to all Defendants and renders all other motions moot. Recent decisions of the Fifth Circuit, and other precedent, mandate dismissal of this indictment.[1] *United States v. Ratcliff*, 488 F.3d 639 (5th Cir. 2007); *Regents of University of California v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372 (5th Cir. 2007). The indictment is facially, fundamentally and fatally flawed.

Accordingly, Defendant James Arthur Brown moves to dismiss the indictment. Brown faces a second trial for conspiracy to commit wire fraud and to falsify Enron's books and records and two substantive counts of wire fraud. However, this literally unprecedented prosecution must be dismissed. On its face, with honest services redacted, the indictment fails to state a wire fraud offense. Further, these statutes simply do not –and cannot–reach the conduct of these businessmen, who had no responsibility for *Enron's* bookkeeping, owed no duty to Enron or its shareholders, and, sought no personal gain. Defendants obtained neither money nor property, nor sought to deprive anyone of any legally cognizable property interest.

In short:

- **The substantive wire fraud counts (II and III) and wire fraud conspiracy (I) fail**.
  - *On its face*, the indictment fails to allege a legally sufficient wire fraud offense (or conspiracy to commit wire fraud).

[1] The government, of course, can appeal this Court's dismissal of this indictment, but it requires the approval of the Solicitor General to do so. A Deputy Solicitor General recently argued, and lost, the government's appeal of the trial court's dismissal of a similarly overreaching wire fraud indictment in a decision just issued by the Fifth Circuit on May 31, 2007, revised on August 13, 2007. *Ratcliff*, 488 F.3d at 644-46 (the scheme alleged failed to wrong the *victim's property* rights). The same office and Deputy argued and lost *Arthur Andersen, LLP v. United States*, 544 U.S. 696, 701, 125 S.Ct. 2129, 2134 (2005), in the Supreme Court. The indictment of the Merrill Defendants is even more overreaching and defective than the *Ratcliff* or *Andersen* charges.

- With honest services redacted, it does not even facially allege that Brown schemed to obtain or deprive anyone of specific money or property. It alleges no self-enrichment. This omission is fatal to the wire fraud and conspiracy to commit wire fraud charges.

- The indictment is also defective as a matter of law because the statutes cannot be stretched to reach this conduct.

  - Brown neither sought nor obtained nor deprived another of any legally cognizable property interest.

  - Neither Enron nor its shareholders were "victims," and Brown owed no duty to Enron or its shareholders.

  - Wire fraud cannot rest on an "intangible" property theory where Defendants owed no duty to the putative victims.

- **The conspiracy to falsify Enron's books and records count (I) fails**.

  - The statute only reaches *issuers*, and the government has conceded in other cases that it cannot prosecute someone for conspiracy who is not within the reach of the substantive statute.

  - This charge also fails because this transaction is immaterial as a matter of law, and materiality to the market must be required.

- **The SEC has the authority to police the conduct alleged here**. At most, this case should have been a civil action by the SEC, and it did file one here. Notably, Defendant Brown *has never been charged* by the SEC or otherwise sanctioned by any regulatory agency. Neither was William Fuhs, whose convictions in this Court were unanimously reversed and acquittal rendered by the Fifth Circuit. *United States v. Brown*, 459 F.3d 509 (5th Cir. 2006), *cert. denied*, 127 S.Ct. 2249 (2007).

Finally, an overriding defect of constitutional magnitude riddles this indictment. It must be dismissed in its entirety for lack of fair warning. The criminalization of this conduct is literally unprecedented. If the government has even approached similar conduct previously, it has only done so in civil enforcement proceedings through the SEC. The plain text of the statutes charged do not reach Brown's conduct, and prior judicial and SEC interpretations have not

criminalized it either. Due Process requires dismissal of the indictment in its entirety because Brown had no fair warning that his role in this business transaction could be a criminal offense. Indeed, it was not criminal.[2]

I. THE REDACTED INDICTMENT–ON ITS FACE–FAILS TO CHARGE A WIRE FRAUD OFFENSE.

This Court must dismiss the charges of conspiracy to commit wire fraud (Count I) and two substantive counts of wire fraud (Counts II and III), in violation of 18 U.S.C. §§ 371[3] and 1343,[4] because the indictment as redacted does not state an offense under these statutes.[5] In the absence of the deprivation of honest services, on which the entire indictment was premised, the indictment fails to allege that Brown schemed to obtain or deprive anyone of any specific object. Merely tracking the language of the statute with the bald and generic words, "money or property," is legally insufficient.[6] *Russell v. United States*, 369 U.S. 749, 764-66, 82 S.Ct. 1038, 1047-48 (1962). Three

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[2] The Fifth Circuit reached only the honest services flaw in the indictment and reversed without reaching these or any other issues. *Brown*, 459 F.3d at 517.

[3] "If two or more persons conspire either to commit any offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined under this title or imprisoned not more than five years, or both." 18 U.S.C. § 371.

[4] "Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, transmits or causes to be transmitted by means of wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice, shall be fined under this title or imprisoned not more than 20 years, or both. If the violation affects a financial institution, such person shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both." 18 U.S.C. § 1343.

[5] This Court has not yet ruled on the government's motion to redact the indictment, so we do not yet have the actual charging instrument. We reserve the right to make other arguments that may arise once we do have that document.

[6] The deprivation of honest services having been redacted, the indictment now reads only that the Merrill Defendants, along with Fastow and others at Enron "conspired to (a) knowingly and intentionally

Fifth Circuit decisions, one quite recent, compel the dismissal of this indictment for its failure to state a wire fraud offense. *Ratcliff*, 488 F.3d at 641 (affirming dismissal of mail fraud indictment for failure to allege property violation)[7]; *United States v. Herron*, 825 F.2d 50, 54 (5th Cir. 1987) (reversing wire fraud convictions for failure of indictment to allege property violation); *United States v. Marcello*, 876 F.2d 1147, 1152 (5th Cir. 1989) (indictment failed to state an offense under wire fraud statute where it contained no property allegation whatsoever); *see also United States v. Bermingham*, — F.Supp.2d —, 2007 WL 1052600 (S.D.Tex. 2007).

A. The Wire Fraud Charges Are Facially Defective And Must Be Dismissed.

A defendant may not be tried or convicted on facts or theories for which he has not been charged. *Marcello*, 876 F.2d at 1152; *United States v. Griffin*, 324 F.3d 330, 355-56 (5th Cir. 2003). In reviewing a motion to dismiss the indictment for failure to state an offense, this Court must take the allegations of the indictment as true and determine whether it states an offense. *United States v. Kay*, 359 F.3d 738, 742 (5th Cir. 2004) (FCPA indictment for foreign bribery). The accused must be apprised of the charges "with sufficient clarity and certainty" to conform to constitutional standards. *Id*. The indictment must (i) contain the elements of the offenses charged and fairly inform defendant of the charge he must defend, and (ii) enable him to plead an acquittal or conviction in bar

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devise a scheme and artifice to defraud Enron and its shareholders and to obtain money and property by means of materially false and fraudulent pretenses, representations and promises . . . " (Count I). Counts II and III are no more specific. They charge: ". . . Brown . . . having devised a scheme and artifice to defraud Enron and its shareholders, and to obtain money and property by means of materially false and fraudulent pretenses, representations and promises. . . ." No count (or overt act) charges that Brown sought or obtained an actual object of money, or property from any victim, or deprived Enron or its shareholders of any object of money or property, now that the honest services object is redacted.

[7] It is well settled that legal authority and interpretation of the mail fraud statute are equally applicable to interpretation and analysis of the wire fraud statute. *United States v. Mills*, 199 F.3d 184, 188 (5th Cir. 1999); *accord United States v. Bermingham*, — F.Supp.2d —, 2007 WL 1052600, *4 (S.D.Tex. 2007).

of future prosecution for the same offense. *Id*. Upon redaction of an indictment, "the central inquiry is whether the *remaining* allegations allege a viable, independent offense." *Bermingham*, 2007 WL 1052600 at *2 (emphasis in original). Here, unlike the *Bermingham* indictment, the remaining allegations do not sufficiently allege an offense–either on the face of the indictment,[8] or as a matter of law. [9]

Upon the redaction of the honest services charge–the only basis alleged for this wire fraud–this indictment simply fails to allege a viable wire fraud offense.[10] There is no allegation that Brown sought to obtain or deprive anyone of specific money or property–making it impossible for Brown to defend against unspecified "deprivations" or unspecified "objects" of the alleged scheme, or, to plead an acquittal in bar of any future prosecution. As in the Fifth Circuit's recent opinion in *Ratcliff*, this "indictment d[oes] not allege a scheme to defraud anyone of money or property." *Ratcliff*, 488 F.3d at 641 (affirming dismissal of a creative fourteen count mail fraud indictment.).

In a similar situation, the Supreme Court has spoken directly to this issue:

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[8] After redaction of the honest-services charge, the face of the *Bermingham* indictment still alleges that defendants wrongfully pocketed $7,352.626.00 from the alleged scheme. As this Court held there, "What remains charged in the Indictment under § 1343, however, is a scheme by which defendant fraudulently deprived GNW and obtained for themselves . . . GNW's tangible property interests having a value of more than $7 million." *Bermingham*, 2007 WL 1052600 at *4 (emphasis added). Brown's indictment has no such allegation–nor could it–as he neither sought nor obtained any personal gain, and unlike the *Bermingham* indictment, there is no allegation that Brown deprived Merrill Lynch of anything. We note that the *Bermingham* indictment has not been appealed, and Bermingham has not been tried.

[9] See sections I.B. and II, *infra*. *Cf. Bermingham*, 2007 WL 1052600 (Indictment with allegations of self-enrichment: "a scheme to convert most of GNW's interest to themselves;" "to skim for themselves the balance of GNW's Swap Sub interest"; "divided the proceeds . . . and kept the balance for himself.").

[10] The mere breach of a fiduciary duty to one's employer, in the absence of some detriment, does not constitute fraud under the mail fraud statute *or, by implication under § 1343*. *Bermingham*, 2007 WL 1052600 at *4, *citing United States v. Brown*, 459 F.2d 509, 519 (5th Cir. 2006) (citing *United States v. Ballard*, 663 F.2d 534, 540 (5th Cir. 1981), *as modified on rehearing*, 680 F.2d 352 (5th Cir. 1982)).

> It is an elementary principle of criminal pleading, that where the definition of an offence, whether it be at common law or by statute, includes generic terms, **it is not sufficient that the indictment shall charge the offence in the same generic terms as in the definition; but it must state the species–it must descend to particulars.**
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> * * *
>
> A cryptic form of indictment in cases of this kind requires the defendant to go to trial with the chief issue undefined. It enables his conviction to rest on one point and the affirmance of the conviction to rest on another. It gives the prosecution a free hand on appeal to fill in the gaps by proof by surmise or conjecture.

Russell, 369 U.S. at 764-66, 82 S.Ct. at 1047-48 (emphasis added); *United States v. Diecidue*, 603 F.2d 535, 547 (5th Cir. 1979) (indictment must descend to particulars). In other words, and at a minimum, the indictment must allege and specifically identify a legally cognizable money or property interest–actual money or property–*sought to be obtained by the Defendant from the victims*. *Ratcliff*, 488 F.3d at 643 (emphasis added). Because the indictment does not allege this essential element, the indictment must be dismissed. *Accord Marcello*, 876 F.2d at 1150 (No crime alleged where the wire fraud indictment "contains no property interest allegation whatsoever.").

Prior to the redaction required by the Fifth Circuit's reversal in this case, the only deprivation or object that Brown's indictment alleged was the deprivation of "the intangible right of honest services of its [Enron's] employees." The entire indictment, factually and legally, rested on the premise that the Merrill Defendants joined Fastow's scheme to deprive *Enron* of the "honest services" of Enron employees. It does not allege a scheme by Brown to seek or obtain Enron's money or property–or that of Enron shareholders, or, to deprive them of *any* object of money or property. It states no allegation of self-enrichment or "naked self-interest." *Cf. Bermingham*, 2007 WL 1052600 at *6. Redacting the honest services charge–the only object ever alleged–eviscerated

the wire fraud charges. This was purely an honest services charge. Without it, the indictment does not state an offense. *Ratcliff*, 488 F.3d at 645; *Herron*, 825 F.2d at 54.

The fatal defects in this indictment are self-evident from the government's own Motion to Strike Surplusage. There, the government wrote, **"the United States will proceed to trial against Defendants solely on the ground that they deprive Enron and its shareholders** [of what?] **and to obtain money and property** [What money? What property? From whom?] **by means or** [sic] **materially false pretenses, representations and promises."** (Dkt. 935:4). The government did not specify an object of "obtaining" or "deprivation" in its Motion to Strike because the indictment does not contain one. It does not allege what money or what property Defendants schemed to seek–or from whom–much less that anything was obtained. In contrast to the Natwest indictment, there is no allegation of Brown's personal gain–sought or obtained.[11] There is no allegation of conversion or skimming. And in the absence of the honest services allegation, there is no allegation that anyone (including Enron and its shareholders) were deprived of any "intangible" right–much less *any* tangible property, *or any* money *at all*.[12] *Cf. Bermingham*, 2007 WL 1052600, *2, 3.[13]

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[11] In *Bermingham*, multiple paragraphs of the indictment on its face allege defendants' scheme for self-enrichment. *Bermingham,* 2007 WL 1052600 at *3. Unlike *Brown*, the "record evidence" of which this Court specifically noted was "quite different" from the facial allegations in *Bermingham*, the *Bermingham* decision states that the defendants' *alleged* "conduct was reasonably calculated, indeed *intended*, to deceive GNW of Swap Sub's value and to conceal their naked self interest in recommending its sale–at a grossly undervalued price–a conclusion that is reinforced by their structuring of a complex series of transactions designed to hide their receipt of over $7 million in proceeds that might otherwise have gone to their employer." *Id.* at *1, 6 (emphasis in original).

[12] It is a settled rule of law that a bill of particulars cannot save an invalid indictment. *Russell*, 369 U.S. at 770, 82 S.Ct. at 1050; *accord United States v. Hoover*, 467 F.3d 496, 498 n.2 (5th Cir. 2006).

[13] As this Court specifically noted in *Bermingham*, "the facts recited in the [*Bermingham*] Indictment . . . are quite different from the record evidence in *United States v. Brown*, 459 F.3d 509 (5th Cir. 2006)." *Bermingham*, 2007 WL 1052600 at *1.

In *Ratcliff*, the government alleged election law violations as a mail fraud, contending that the salary and employment benefits of elected office constituted money or property under the mail fraud statute, and that Ratcliff obtained office with illegal funding and by concealing his violations from the Board of Ethics. *Ratcliff*, 488 F.3d at 644.[14] The Fifth Circuit affirmed the district court's dismissal of the indictment. The Circuit held that a "deprivation must involve the wronging of the victim's property rights." *Id*. at 645 n.8. The parish was not deprived of money or property by means of Ratcliff's misrepresentations to the board of ethics, "[n]or would the parish be deprived of control over the money by means of Ratcliff's fraud . . ." *Id*. at 645. "Indeed, there are no allegations that the parish would be deceived either directly, or indirectly, into taking any action at all." *Id*. The same is true here.

Further, the Circuit panel said, "the alleged scheme must be one to defraud the victim. Ratcliff's indictment provides no basis to find a scheme to defraud Livingston Parish through misrepresentations made to the board of ethics. The misrepresentations simply did not implicate the parish's property rights." *Id*. at 645-46. Likewise, here, Enron was neither deceived nor deprived of control over its money. There is no allegation that it was. The charged conduct simply does not implicate *anyone's* property rights–Enron's or shareholders'.[15]

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[14] The indictment charged Ratcliff with "a scheme to defraud Livingston Parish of the money and property represented by 'the powers, privileges, salary, and other benefits' of his elected office." *Ratcliff*, 488 F.3d at 644. Brown's indictment does not even allege that much. There is no allegation identifying what money or property he schemed to obtain or from whom–nothing states what the bald "money or property" language of the statute is "represented by," as was alleged in *Ratcliff*. In that regard, this indictment is closer to an indictment that had no money or property allegation at all and required reversal in *Marcello*, 876 F.2d at 1150 (only an intangible rights theory was alleged).

[15]Neither is this element (money or property) one which can be inferred–unlike the materiality or intent elements–from the facts as alleged in the indictment. *Ratcliff*, 488 F.3d at 644 n.4.

These requirements are so fundamental that in *Herron*, the Fifth Circuit, *sua sponte*, raised the issue, held that the facts in the indictment did not constitute a cognizable wire fraud violation, and reversed defendant's wire fraud convictions. 825 F.2d at 51. In *Herron*, before amendment of the currency transaction reporting laws, the government tried to prosecute bank *customers* for scheming to defraud the government of information on the CTR forms by structuring deposits to avoid triggering the banks' reporting requirements. Noting that the wire fraud statute is not "limitless," and the indictment did not allege that defendants sought a tangible or economic advantage to themselves, the court held that "deprivation of CTR information from financial institutions fails to satisfy the 'money or property' requirement . . . ." *Id*. at 56-57. The court further held that even though the defendants in *Herron* "were clearly aware of the CTR reporting requirements, [] neither defendant could reasonably expect that his conduct constituted wire fraud." *Id*. at 57.[16]

Based on this fatal, facial insufficiency, this Court must dismiss the substantive wire fraud counts (2 and 3), and that portion of Count 1 which alleges a conspiracy to commit wire fraud. *McNally v. United States*, 483 U.S. 350, 358-59, 107 S.Ct. 2875, 2881 (1987), *superseded by statute* on other grounds by 18 U.S.C. § 1346. It is that simple. *Ratcliff*, 488 F.3d at 645-49, *Herron*, 825 F.2d at 54-57; *see Marcello*, 876 F.2d at 1150 (No crime is alleged where the wire fraud indictment "contains no property interest allegation whatsoever.").

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[16] Brown, in this case, is similarly situated to the *Herron* defendants who had no duty and were not in the class of persons governed by the statute charged. The statutes alleged do not reach Brown. Like the banks in *Herron*, only Enron had any duty to report, and the indictment does not allege that Brown sought, obtained or deprived anyone of cognizable money or property. *Herron*, 825 F.2d at 57. *See infra,* notes 18 and 23 and accompanying text, and section III. *Unlike* the defendants in *Herron* whose scheme included pocketing a percentage of the "suitcases" of cash they deposited in amounts below the $10,000 reporting trigger, Brown sought no personal gain or property from Enron or its shareholders.

B. As A Matter Of Law, Without An Honest Services Charge, The Wire Allegations Fail.

The Fifth Circuit's opinion in Barge I rejected the Government's theory of wire fraud predicated on deprivation of "honest services." 18 U.S.C. § 1346. By this holding alone, it is now axiomatic that any allegations–in the indictment–that Defendants committed wire fraud, 18 U.S.C. § 1343, or conspired to commit wire fraud, 18 U.S.C. § 371, 18 U.S.C. § 1343, must necessarily fail. The Government's theory of fraud cannot change, and it has been foreclosed from application of the only theory of conviction that was alleged (honest services in violation of § 1346).[17] The indictment cannot be re-characterized now to state a tangible money or property offense. It has never alleged one. *Cf. Bermingham*, 2007 WL 1052600 (replete with allegations of self-enrichment with the money or property of others).

Where, as here, that theory of harm fails (as it did by virtue of the opinion of the Fifth Circuit), resort simply to § 1343 is untenable. *Herron*, 825 F.2d at 54-58. Well-settled legal authority interpreting § 1346 establishes that § 1343 standing alone, without resort to and as distinct

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[17] As the Fifth Circuit opined in *United States v. Gray*, 96 F.3d 769, 773-74 (5th Cir. 1996), *cert. denied*, 520 U.S. 1129, 117 S.Ct. 1275 (1997), it is only "in light of" and through application of § 1346, that the wire fraud statute can be extended to reach allegations of fraud *not* involving deprivation of identifiable (tangible) property or identifiable harm to an identifiable victim. *See Gray*, 96 F.3d at 773-74; *see also Griffin*, 324 F.3d at 355-56 (prohibiting end run around wire fraud statute–through resort to § 1346–where intangible rights theory was not charged in the indictment); *United States v. Jain*, 93 F.3d 436, 442 (8th Cir. 1996) (§ 1346 "modifies the definition of 'scheme or artifice to defraud' in § 1341 [and § 1343]."), *cert. denied*, 520 U.S. 1273, 117 S.Ct. 2452 (1997); *United States v. Ervasti*, 201 F.3d 1029, 1036 (8th Cir. 2000) (§ 1346 "enlarged the definition of 'scheme or artifice to defraud' under § 1341 [and § 1343]."). In other words, § 1346 was the only, even remotely, possible "way in" to allege criminal fraud in the attenuated circumstances alleged in the instant case. *Cf. United States v. Turner*, 465 F.3d 667, 673 (6th Cir. 2006) ("§ 1346, by its terms, did not restore the application [disapproved in *McNally*] of the mail fraud statute to all "intangible rights," but only to the deprivation of honest services). Indeed, the (new) application of § 1346 was the *only* basis upon which the Fifth Circuit in *Gray* could distinguish the holding in *United States v. Walters*, 997 F.2d 1219, 1224 (7th Cir. 1993) ("§ 1341 [and by extension § 1343] does not cover the waterfront of deceit."). *Gray*, 96 F.3d at 773-74.

from § 1346, requires stricter standards–as to concreteness of identifiable harm and obtaining of identifiable property. *Ratcliff*, 488 F.3d at 644-46. Those standards are not met here, and they cannot be met. *See infra* sections I.A. and II. Now that the honest services charge has failed, and the *only* allegation of deprivation of any cognizable money or property has been redacted from the indictment, the entire wire fraud charge collapses. The indictment has no legal basis, states no cognizable or concrete object, and, the statute does not reach the conduct alleged here. *See United States v. Haga*, 821 F.2d 1036, 1044-45, n.18 (5th Cir. 1987) (implied acquittal on theory charged bars reprosecution);[18] *Bermingham*, 2007 WL 1052600 at *4 ("mere breach of a fiduciary duty to one's employer, in the absence of some detriment, does not constitute fraud under the mail fraud statute, or by implication, under § 1343.").

The Fifth Circuit has repeatedly refused to stretch § 1343, standing alone, to encompass novel theories of fraud premised on novel concepts of property. Most recently, in *Ratcliff*, the court affirmed the dismissal of a creative 14-count mail fraud indictment because "the misrepresentations simply did not implicate [the victims] property rights." 488 F.3d at 645-46. The court specifically rejected the government's attempt to stretch the mail fraud statute "because, [as here] it invites us to approve a sweeping expansion of federal criminal jurisdiction in the absence of a clear statement

[18] Further, (1) absent access to an honest services theory to support the government's wire fraud charges, coupled with the government's (2) failure to identify any concrete money or property interest, the government is required to demonstrate some form of duty flowing from the Defendants to the putative victims in the case. *Carpenter v. United States*, 484 U.S. 19, 25, 27-28, 108 S.Ct. 316, 320-22 (1987); *Griffin*, 324 F.3d at 355-56; *Gray*, 96 F.3d at 773-74; *Herron*, 825 F.2d at 54, 57-58; *United States v. Ballard*, 663 F.2d 534, 540-41 (5th Cir. 1981); *Cf. Turner*, 465 F.3d at 671 (Pre-§ 1346 applications of mail fraud premised on "intangible" property theories, and brought against "private persons," required government to demonstrate a "clear fiduciary dut[y]."). *See also Chiarella v. United States*, 445 U.S. 222, 228-29, 100 S.Ct. 1108, 1114-15 (1980). It cannot do so here. It has already been determined in this Circuit that *Brown had no duty to Enron or its shareholders*. *Regents*, 482 F.3d at 393. The indictment fails on this basis as well.

by Congress." *Ratcliff*, 488 F.3d at 639 (quoting *Cleveland v. United States*, 531 U.S. 12, 24, 121 S.Ct. 365, 373 (2000)).

"[T]o the extent that the meaning of the word 'property' [is] ambiguous," Fifth Circuit applies the rule of lenity under authority of the Supreme Court. *Griffin*, 324 F.3d at 354. Where, as here, there is no fair notice that specific conduct is forbidden–or compelled–that conduct cannot be prosecuted. *See United States v. Harriss*, 347 U.S. 612, 617, 74 S.Ct. 808, 812 (1954); *accord Griffin*, 324 F.3d at 354. Here, more so than in *Herron*, "neither defendant could reasonably expect that his conduct constituted wire fraud." 825 F.2d at 57. Without the critical underpinning of the honest services provision, Brown cannot be charged with wire fraud as a matter of law.[19] As in *Ratcliff*, "the terms of the statute . . . simply do not proscribe the conduct for which [he] was indicted." 488 F.3d at 649.

II. IN ADDITION, THE CONSPIRACY AND WIRE FRAUD STATUTES DO NOT REACH THE CONDUCT ALLEGED.

Nothing in the plain text of the wire fraud statute applies to Brown's conduct. No prior decision has reached so far to inculpate facially innocent commercial conduct by employees of

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[19] In addition, given the extensive and careful regulation of our securities industry by the SEC, and the Congressional intent and scheme of our securities laws, stretching the wire fraud statute to reach this conduct appears precluded. *See Credit Suisse Securities (USA) LLC v. Billing*, — US —, 127 S.Ct. 2383, 2397 (2007) (holding that an antitrust suit was precluded by the securities laws); *id.* at 2400 (Thomas, J., dissenting) (noting that the majority opinion effectively holds that the Securities Act precludes wire fraud charges in like circumstances).

The wire fraud statute cannot be used to make an end-run around the Securities Act. "Securities fraud," which the government has repeatedly used to characterize this case, is "an area of the law that demands certainty and predictability." *Regents*, 482 F.3d at 386. Branding Merrill Lynch investment bankers as criminals for what distills to *Enron's* accounting responsibilities and the *timing* of its reported gain would *more than* "give rise to confusion about the extent of secondary actors' obligations and invite vague and conflicting standards of proof in diverse courts." *Id*. It violates Due Process, the Rule of Lenity and the requisites of fair warning.

another corporation. As the Supreme Court has assured, "§ 1341 does not cover the waterfront of deceit." *United States v. Walters*, 997 F.2d 1219, 1224 (7th Cir. 1993) (reversing mail fraud conviction of a sports agent who violated NCAA Rules but did not obtain property) (referring to *McNally v. United States*, 483 U.S. 350, 107 S.Ct. 2875 (1987) (*superseded by statute* on other grounds by 18 U.S.C. § 1346)). While the language of the statute "proscribes 'any scheme or artifice to defraud,' this is not to suggest the wire fraud statute is limitless." *Herron*, 825 F.2d at 54.

Here, (1) the Merrill Defendants neither sought nor obtained money or property so as to support a wire fraud indictment; (2) in any case, the indictment does not and cannot identify a cognizable object of property sought to be obtained from, or, of which Enron or its shareholders could be deprived as victims, by the alleged fraud; (3) these counts necessarily fail because the Merrill Defendants owed no duty to Enron or its shareholders; and, (4) precedent of the Fifth Circuit forecloses resort to the novel theory of fraud alleged in the indictment.[20]

The rules for construing the wire fraud statute's application to facts alleged are well settled:

(1) The clauses in the statute are read in the conjunctive, and it is therefore essential that the indictment specify legally cognizable money or property which Defendants either sought to obtain or of which they sought to deprive another. *Cleveland*, 531 U.S. at 26, 121 S.Ct. at 374; *McNally*, 483 U.S. at 358-59, 107 S.Ct. at 2881; *Ratcliff*, 488 F.3d at 643-644 n. 5; *United States v. Males*, 459 F.3d 154, 157 (2d Cir. 2006).

(2) Legal authority and interpretation of the mail fraud statute are equally applicable to interpretation and analysis of the wire fraud statute. *See supra* note 7 and accompanying text. *Mills*, 199 F.3d at 188.

(3) Any ambiguity as to the wire fraud statute's application to the crime charged and the facts as alleged must be *strictly construed* in favor of the Defendant. *Cleveland*, 531

[20] This portion of the indictment fails for another reason: Materiality is a required element under the wire fraud statute. *Ratcliff*, 488 F.3d at 644. Therefore, to the extent a transaction, deprivation, or obtaining is immaterial as a matter of law, a wire fraud prosecution cannot be maintained. *See infra*, section III.

U.S. at 25, 121 S.Ct. at 373-74; *Fasulo v. United States*, 272 U.S. 620, 627-28, 47 S.Ct. 200, 201-02 (1926).[21]

(4) When substantive counts of wire fraud fail for these reasons, then the conspiracy to commit wire fraud count against the Defendant premised on the same alleged conduct must also fail. *McNally*, 483 U.S. at 358-59, 107 S.Ct. at 2881. *Cf. Ballard*, 663 F.2d at 542-43.

A. Brown Neither Sought Nor Obtained, Nor Deprived Another Of Money Or Property Cognizable Under The Wire Fraud Statute.

Brown *obtained no money or property* as a result of the transaction which forms the basis for this indictment. Indeed, there was no personal gain, of money or property, by any defendant. Neither did Brown *seek to obtain money or property* pursuant to the alleged scheme to defraud. Brown was simply doing his job. Because Brown did not seek or scheme to obtain a cognizable object of property, the Government cannot maintain a claim for wire fraud, and Counts 2 and 3, and that portion of Count 1 alleging a conspiracy to commit wire fraud, must be dismissed.

To fall within the parameters of the wire fraud statute, the Defendant's conduct must have been "acquisitive" as to the/an "object" of the purported fraud. *Monterey Plaza Hotel Ltd. P'ship v. Local 483*, 215 F.3d 923, 927 (9th Cir. 2000); *Walters*, 997 F.2d at 1227; *accord United States v. Baldinger,* 838 F.2d 176, 180 (6th Cir. 1988); *United States v. Gimbel*, 830 F.2d 621, 626-27 (7th Cir. 1987); *Herron*, 825 F.2d at 57; *United States v. Alsugair*, 256 F.Supp.2d 306, 312 (D.N.J. 2003); *Cf. Cleveland*, 531 U.S. at 16, 121 S.Ct. at 368 ("It does not suffice, we clarify, that *the object of the fraud* may become property in the recipient's hands; for purposes of the [wire] fraud statute, the *thing obtained* must be property in the hands of the victim.") (emphasis added); *United States v.*

[21] As the Court stated in a mail fraud case years ago: "There are no constructive offenses; and before one can be punished, it must be shown that his case is plainly within the statute." *Fasulo*, 272 U.S. at 629, 47 S.Ct. at 202.

Shelton, 848 F.3d 1485, 1494 (10th Cir. 1988) ("[T]he indictment does not provide any notice that the transfer of money or property from the victim to the defendant is an essential element of mail fraud against which [defendant] had to prepare a defense."); *United States v. Rothenberg*, — F.Supp.2d —, 2007 WL 2300556, *5 (S.D.Tex. 2007) ("mail fraud statute seeks to deter fraud by preventing use of the mail to perpetuate any 'scheme to defraud' *of money or property*.") (emphasis added); *see also McNally*, 483 U.S. at 360, 107 S.Ct. at 2882 (mail fraud statute is "limited in scope to the *protection* of property rights.") (emphasis added). No such conduct is alleged here.

B. Brown Did Not–And Could Not–Seek To Deprive Enron Or Its Shareholders Of A Legally Cognizable Property Interest.

Even assuming that the wire fraud statute could be expanded to reach a pure "deprivation,"[22] distinct and not conjoined with any conduct by the defendant designed to seek or obtain property, the indictment still fails to state a claim: the Government does not and cannot allege any legally cognizable property interest of which Brown sought to deprive *any* putative victims–Enron or its shareholders. *Cf. Cleveland*, 531 U.S. at 16, 121 S.Ct. at 368 (fraud statute requires a legally cognizable *object* of property.).

(i) First, the indictment in this case simply fails on its face to identify an object (money or property) that Brown allegedly schemed to obtain by fraud. *See supra* section I.A.. Nor can the government amend the indictment at this late stage, by bill of particulars or otherwise, to remedy this

[22] *See*, *e.g.*, *Males*, 459 F.3d at 158-60; *United States v. Hedaithy*, 392 F.3d 580, 602 n. 21 (3d Cir. 2004), *cert. denied*, 544 U.S. 978, 125 S.Ct. 1882 (2005); *but see United States v. Loney*, 959 F.2d 1332, 1334-36 (5th Cir. 1992) (defendant must have sought some object and some harm must have resulted); *accord United States v. St. Gelais*, 952 F.2d 90, 95 (5th Cir. 1992) ("Not only must a defendant intend to defraud or deceive, but he must intend for some harm to result from the deceit."), *cert. denied*, 506 U.S. 965, 113 S.Ct. 439 (1992).

facial defect. *Russell v. United States*, 369 U.S. 749, 770, 82 S.Ct. 1038,1050 (1962); *accord Hoover*, 467 F.3d at 498 n.2.

(ii) Second, the indictment does not allege an "intangible" property interest as an object of a "scheme," and such an object, in the absence of § 1346, is not cognizable under the wire fraud statute. *United States v. Griffin*, 324 F.3d 330, 355 (5th Cir. 2003) (wire fraud statute does not extend to purely "abstract or theoretical" "property interests."); *cf. Herron,* 825 F.2d at 57 ("deprivation of [] information from financial institutions fails to satisfy the 'money or property' requirement of *McNally*."); *see Bermingham*, 2007 WL 1052600 at *4 (in absence of honest services charge, and some actual detriment, there is no fraud by implication under § 1343). Because the government does not and cannot allege this essential element, the indictment must be dismissed. *Marcello*, 876 F.2d at 1150.[23]

(iii) Third, "the deceit must be coupled with a contemplated harm to [a] victim." *United States v. Starr*, 816 F.2d 94, 98 (2d Cir. 1987). *Accord St. Gelais*, 952 F.2d 90, 95 (5th Cir. 1992). The identification of a "victim" or "intended victim" is intertwined with the concepts of "money or property" and/or "obtaining" and/or "deprivation."[24] The indictment here fails as to these elements

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[23] In *United States v. Starr,* 816 F.2d 94 (2d Cir. 1987), the Court stated that "the harm contemplated [in a scheme to defraud] must affect the very nature of the bargain itself. Such harm is apparent where there exists a 'discrepancy between benefits reasonably anticipated because of the misleading representations and the actual benefits which the defendant delivered, or intended to deliver.'" *Id.* at 98 (quoting *United States v. Regent Office Supply Co.,* 421 F.2d 1174, 1182 (2d Cir.1970)). In *Starr,* as here, there was no such discrepancy; the defendants "in no way misrepresented to their customers the nature or quality of the service they were providing." *Starr*, 816 F.2d at 99.

[24] Nor do the putative victims (either Enron or its shareholders) in this case fall within any definition of an *intended* victim fashioned by the Courts in prior precedent. For example, in *Ratcliff*, the Fifth Circuit held that "[a]lthough the charged scheme involves [Defendant] ultimately receiving money from the ["alleged victim"], it cannot be said that the ["alleged victim"] would be deprived of this money by means of [Defendant's] representations, as the financial benefits [ultimately transferred to one in the Defendant's position] go to [one in the Defendant's position] regardless of who that person is." *Ratcliff*, 488 F.3d at 645.

both in isolation and as considered as a "whole." *See also Ratcliff*, 488 F.3d at 644-45. It is beyond debate that to maintain a cause for wire fraud under 18 U.S.C. § 1343, the indictment must identify a victim, or an intended victim whose money or property is the object of the defendant's fraud. *Ratcliff*, 488 F.3d at 644 (Question before court on challenge to the charging instrument is "whether the indictment alleges a scheme to defraud the alleged victim."); *id*. at 645 ("Though the misrepresentations in a [wire] fraud scheme need not be made directly to the scheme's victim, the alleged scheme must nevertheless be one *to defraud the victim*.") (emphasis added) (citation omitted); *United States v. D'Amato*, 39 F.3d 1249, 1257 (2d Cir. 1994) (Defendant "must intend to harm the [alleged] fraud's victims.").

In *Brown*, 459 F.3d at 522, the Fifth Circuit noted that Enron was not a victim under the facts alleged here. And, only *Enron* owed a duty to its shareholders–from whom Brown sought nothing. *Regents*, 482 F.3d at 393. In addition to the fact that the indictment fails to allege that Brown sought money or property from Enron *or* its shareholders, or deprived them of cognizable property, it is also beyond dispute that no duty flowed between the Merrill Defendants and either Enron or its shareholders. *Regents*, 482 F.3d at 393.[25]

See also Herron, 825 F.2d at 57 ("deprivation of [] information from financial institutions fails to satisfy the 'money or property' requirement of *McNally*."). Here, the scheme did not even contemplate Brown receiving money or property from anyone.

[25] Indeed, Brown's attenuated position in this case renders utterly baseless the government's novel attempt to fabricate a federal criminal fraud out of an innocuous business transaction, vetted with auditors and counsel and among two sophisticated business entities. Even a prosecution premised on § 1346 requires something *more than* a breach of a fiduciary duty. *United States v. Brumley*, 116 F.3d 728, 734 (5th Cir. 1997) (*en banc*), *cert. denied*, 522 U.S. 1028, 118 S.Ct. 625 (1997). Certainly the same result must inhere where the government proceeds, assuming they do so here, on a wire fraud theory premised on other "intangible rights." *Cf. Turner*, 465 F.3d at 671 (government must demonstrate a "clear fiduciary dut[y]."). The Fifth Circuit has expressly refused to extend the wire fraud statute in analogous circumstances to "create a new strand in the bundle of property rights" to give an entity [there, the government] ownership interest in information not already possessed and *which the law did not already compel the individual to divulge*."

As the Fifth Circuit recently held in *Regents* concerning this very transaction, "To impose liability for securities fraud on one party to an arm's length business transaction in goods or services other than securities because that party knew or should have known that the other party would use the transaction to mislead investors in its stock would introduce potentially far-reaching duties and uncertainties for those engaged in day-to-day business dealings. Decisions of this magnitude should be made by Congress." *Regents*, 482 F.3d at 393 (quoting *In re Charter Communications, Inc., Securities Litigation*, 443 F.3d 987, 992-93 (8th Cir. 2006), *cert. granted*, *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.,* 127 S.Ct. 1873 (2007) (No. 06-43)). *Cf. Brown*, 459 F.3d at 534 ("[W]e lack the constitutional power to . . . define what constitutes criminal conduct on an *ex post facto* and *ad hoc* basis.") (DeMoss, J., concurring in part and dissenting in part). To impose *criminal liability* for *wire fraud* on that same "party to an arm's length business transaction in goods or services other than securities because that party knew or should have known that the other party would use the transaction to mislead investors in its stock," would be far more devastating "for those engaged in day-to-day business dealings." Indeed, it is a decision of an even greater "magnitude [which] should be made by Congress." *Regents*, 482 F.3d at 393.

III. THE CONSPIRACY TO FALSIFY ENRON'S BOOKS AND RECORDS FAILS TO ALLEGE AN OFFENSE COGNIZABLE UNDER THOSE STATUTES.

The government's proposed redacted indictment also charges Brown with conspiracy to falsify Enron's books and records in violation of 18 U.S.C § 371, 15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(4) and (5) (Count I). The government does not assert a substantive books and records charge

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Herron, 825 F.2d at 54, 57-58 (emphasis added).

against Brown, nor could it. By its plain text, the statute applies only to issuers and requires internal controls.

A. By Its Plain Text, The Books And Records Provision Applies Only To The *Issuer*–Not To Brown.

In the 30 years since the books and records provision of the FCPA was enacted, it has been used to prosecute only executives and employees of the *issuer* for falsifying the *issuer's* books and records. No doubt, this is because the plain text of the statute applies only to *issuers*–those who have control over and responsibility for the *issuers*' books and records.[26] Specifically § 78m(b)(2) "identifies the class of persons who must comply with the statute's requirements." *United States v. Wilson*, 2001 WL 798018, *7 (S.D.N.Y. 2001). This class includes only *issuers* charged with maintaining their *own* books and records. The class does not include the Merrill Lynch Defendants in this case. To give fair warning, a criminal statute must "define the ... offense with sufficient definiteness that ordinary people can understand what conduct is prohibited ..." *Kolender v. Lawson*,

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[26] As further evidence that § 78m(b)(2) was never designed to reach Brown, one need only review § 78m(b)(6), which provides a good faith exception as to § 78m(b)(2), for issuers who own less than 50% of a business concern. In essence, because a minority owner could not be expected, nor any sanction be imposed for failing, to control or make proper recordings in the books and records of the majority owner of that concern, Congress immunized them from any sanction–civil or criminal–where that minority owner was operating in good faith. 15 U.S.C. § 78m(b)(6). In the instant case, Merrill occupies a significantly more remote position as to the issuer, and § 78m(b)(6) is additional evidence militating against the criminal sanction. Further, the fact that § 78m(b)(6) identifies a minority owner (*of the issuer*) as an entity to be governed, is additional evidence that the statute is confined to only *issuers* (and/or minority owners of *issuers*), and is not meant to reach an entity in as attenuated a position as Merrill or Brown was in this case. The headings of the various subsections of § 78m simply confirms this application: 15 U.S.C. § 78m(a) ("Reports by issuer of security; content."); 15 U.S.C. § 78m(d) ("Reports by persons acquiring more than five per centum of certain classes of securities."); 15 U.S.C. § 78m(e) ("Purchase of securities by issuer."); 15 U.S.C. § 78m(i) ("Real time issuer disclosures."). *See United States v. Menasche*, 348 U.S. 528, 538-39, 75 S.Ct. 513, 519-20 (1955) (Court should "give effect, if possible, to every clause and word of a statute.") (citations omitted); *accord TRW, Inc, v. Andrews*, 534 U.S. 19, 31, 122 S.Ct. 441, 449 (2001); *In re Supreme Beef Processors, Inc.*, 468 F.3d 248, 253 (5th Cir. 2006) (*en banc*).

461 U.S. 352, 357, 103 S.Ct. 1855, 1858 (1983). No person or court except the Enron Task Force has read this statute to criminalize the conduct of Merrill Lynch employees for *Enron's* bookkeeping.

In construing a statute, it is axiomatic that the court must look first to the language of the statute itself in its context. *Bailey v. United States*, 516 U.S. 137, 144-45, 116 S.Ct. 501, 506-07 (1995). At most, a books and records charge could reach only conduct of *Enron's employees*. Congress never intended a criminal prosecution of a books and records violation to be expanded to persons like Brown who had no responsibility for, or control over, Enron's books and records. In fact, as a matter of law, Brown had no duty for them, or to Enron, or, to its shareholders. *See Regents of University of California v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372, 384 (5th Cir. 2007) (banks including Merrill Lynch owed no duty to disclose to Enron's shareholders the nature of the transactions). According to the plain text of the statute, Brown is not in the class of persons who can be charged with falsifying *Enron's* books and records.

1. The Text Of The Statute Requires Dismissal Of The Indictment.

Title 15 U.S.C. § 78m(b) focuses exclusively on, and applies only to, *issuers* and establishes rules for *internal* controls. It limits liability (in pertinent part) to those who "*knowingly falsify* any book, record, or account," and criminally punishes only what must also be a "willful" violation. 15 U.S.C. § 78m(b)(2) (emphasis added) mandates:

> "Every **issuer** . . . which is required to file reports . . . shall (A) make and keep books, records and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer;
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> ***
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> (5) No person shall knowingly circumvent or knowingly fail to implement a system of internal accounting controls or knowingly falsify any book, record or account described in paragraph (2)."

The applicable portion of §78ff(a) states:

> "Any person who willfully violates any provision of this chapter . . . shall upon conviction be fined not more than $5,000,000, or imprisoned not more than 20 years, or both."

2. The Legislative History And SEC Actions Demonstrate That Congress Intended To Establish Internal Controls, Primarily For SEC Civil Enforcement Of Issuer Conduct.

The disclosure and accounting provisions of the FCPA, separate from provisions criminalizing the payment of bribes (15 U.S.C. §§ 78dd-1-2), are appropriately characterized as *internal* accounting controls. *See* H.R.CONF.REP.NO. 100-576 at 916, *reprinted in* 1988 U.S.C.C.A.N. 1547, 1946.[27] They were enacted, amended, and until recently have been used primarily, to give teeth to civil enforcement remedies for the SEC against high-ranking executives of *issuers* who knowingly falsified[28] their own company's books and records.[29] Moreover, to read

[27] U.S. General Accounting Office, Report To The Congress: Impact Of Foreign Corrupt Practice Act In U.S. Business 69 (1981) ("[T]he accounting provisions were intended largely as a self-regulatory measure.").

[28] The 1988 Amendments deleted the "reason to know" standard as a basis of liability and replaced it with the more onerous, and less inclusive standard: "no person shall knowingly circumvent or . . ." H.R. CONF. REP. 100-576, P.L. 100-418, Omnibus Trade And Competitiveness Act House Conference Report No. 100-576, April 20, 1988.

[29] The provision has been used by the SEC in civil enforcement actions against high ranking executives for the *issuer*. The remedies sought for books and records violations have included injunctions to require compliance, officer and director bars, disgorgement of ill gotten gains, and civil fines. *See McConville v. S.E.C.*, 465 F.3d 780 (7th Cir. 2006) (affirming cease and desist order against former CFO for keeping false books and records, securities fraud and failing to maintaining adequate internal accounting controls); *S.E.C. v. Smyth*, 420 F.3d 1225 (11th Cir. 2005) (civil action against company president); *S.E.C. v. Hawk*, — F.Supp.2d —, 2007 WL 2257321 (D.Nev. 2007); (civil enforcement action against senior officers of issuer); *S.E.C. v. Baxter*, — F.Supp.2d —, 2007 WL 2013958 (N.D.Cal. 2007) (civil enforcement action against company vice president of finance); *S.E.C. v. Cohen*, — F.Supp.2d —, 2007 WL 1192438 (E.D.Mo. 2007) (on civil complaint for fraud and books and records violations, refusing to enjoin former CFO, noting that misstatements associated with the falsified books were immaterial); *S.E.C. v. Hopper*, 2006 WL 778640 (S.D.Tex. 2006) (civil action for permanent injunction, disgorgement, and monetary penalties against vice president (CEO of relevant subsidiary) and CFO).

the statute to cover anyone other than issuers would read out of the statute the provisions requiring internal accounting controls so that the books and records can be reviewed and corrected. 15 U.S.C. §§ 78m(b)(2)(B)(i-iv) & 78m(i). *Accord In re IKON Office Solutions, Inc.*, 277 F.3d 658, 672 (3d Cir. 2002) (deficiencies in internal accounting controls of company are immaterial to outside auditors because they are matters of which only management would be aware.); *Rocker Management, L.L.C. v. Lernout & Hauspie Speech Products N.V.*, 2005 WL 3658006, *12 (D.N.J. 2005) (Auditors had no motive *or opportunity* to commit fraud). One should not be held criminally liable for knowingly falsifying books that one has no authority, duty or even access to correct. *See supra* note 26 and accompanying text.[30]

"Congress' use of the terms 'records,' suggests that any tangible embodiment of information made or kept by *an issuer* is within the scope of 13(b)(2)(A)." *S.E.C. v. World-Wide Coin Investments, Ltd.*, 567 F.Supp. 724, 748-49 (N.D.Ga. 1983) (emphasis added). This provision has been described as "a highly technical statutory requirement." *United States v. Lake*, 472 F.3d 1247, 1266 (10th Cir. 2007) (reversing convictions against two officers of issuer). The statute repeatedly and specifically establishes requirements only for the *issuer*, and its terms are mandatory: "*Every issuer* . . . *shall* . . ." 15 U.S.C. § 78m(b)(2) (emphasis added). Both by the plain text of the statute, and its legislative history, these provisions do not reach Brown. Having no role on behalf of, or duty to, the *issuer*, he is not in the class of persons who could be charged with the substantive books and

[30] *See also* § 78m(b)(2) (Requiring "level of detail and degree of assurance as would satisfy prudent officials in the conduct of *their own affairs*.") (emphasis added).

records offense.[31] *See Wilson*, 2001 WL 798018, *7; *S.E.C. v. Dauplaise*, 2006 WL 449175, *7-8 (M.D.Fla. 2006).

"[A] statute that is not unambiguous in its terms and that if applied here would render a wide range of conduct violative of federal law, a legislative history that fails to evidence congressional awareness of the statute's claimed scope, . . . " must be narrowly construed. *Williams v. United States*, 458 U.S. 279, 290, 102 S.Ct. 3088, 3094 (1982). *Accord United States v. Enmons*, 410 U.S. 396, 411, 93 S.Ct. 1007, 1015 (1973); *Brown*, 459 F.3d at 535 (DeMoss, J., concurring in part and dissenting in part). Even assuming (*minimal*) ambiguity, "[w]here it is doubtful whether the text includes the penalty, the penalty ought not be imposed." *United States v. R.L.C.*, 503 U.S. 291, 309, 112 S.Ct. 1329, 1340 (1992 (Scalia, J., concurring); *accord United States v. Orellana*, 405 F.3d 360, 370 (5th Cir. 2005) (applying rule of lenity because of the "ambiguity" of the statute, "questionable interpretation" used to criminalize conduct, "and the absence of binding case law").[32] Accordingly,

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[31] If they could, and this were used and enforced as an independent federal felony (which carries a 20-year prison sentence) the books and records provision must have substantive parameters to guide both prosecutors and issuers. *See Williams v. United States,* 458 U.S. 279, 286, 102 S.Ct. 3088, 3092 (1982) (statute should not be interpreted to "make a surprisingly broad range of unremarkable conduct a violation of federal law"); *Brown*, 459 F.3d at 536 ("Such [preliminary business] negotiations should not be the fodder for criminal indictments.") (DeMoss, J., concurring in part and dissenting in part). No case had addressed or established the essential elements for a felony conviction under this provision when Brown was indicted. Under the rule of lenity, statutory language far more explicit than that of 78m(b)(2) is needed to find that *Congress intended* to place the Department of Justice in the business of criminally prosecuting employees of all companies on all sides of a business transaction for a bookkeeping entry that arguably resulted in the *issuer* falsifying its books–no matter how financially insignificant the false entry. Indeed, such a novel holding is unprecedented and, consequently, barred by Due Process. *United States v. Lanier*, 520 U.S. 259, 266, 117 S.Ct. 1219, 1225 (1997); *Brown*, 459 F.3d at 535 (DeMoss, J., concurring in part and dissenting in part).

[32] The Supreme Court has often had to reverse criminal convictions because the government has tried to expand the reach of various statutes, and there was no fair warning. *See, e.g.*, *Arthur Andersen,* 544 U.S. at 703-04, 125 S.Ct. at 2134-35; *City of Chicago v. Morales*, 527 U.S. 41, 56, 119 S.Ct. 1849, 1859 (1999); *Lanier*, 520 U.S. at 266, 117 S.Ct. at 1225; *Dowling v. United States*, 473 U.S. 207, 213-14, 105 S.Ct. 3127, 3131 (1985); *Liparota v. United States,* 471 U.S. 419, 427, 105 S.Ct. 2084, 2089 (1985); *Kolender,* 461 U.S. at 357, 103 S.Ct. at 1858; *Dunn v. United States*, 442 U.S. 100, 112, 99 S.Ct. 2190, 2197 (1979); *Marks v.*

under the text and its legislative history, the Merrill Lynch Defendants cannot be charged with a substantive violation regarding *Enron's* books.

3. No Judicial Interpretation Has Extended The Books And Records Provision To Criminally Prosecute Anyone Outside The Issuer.

Extensive research has disclosed **no other criminal case prosecuted under the books and records provision against a person who did not work for the *issuer***. All reported criminal cases, most decided *after* the conduct charged here, have been charged against *only* high-ranking executives and other employees of the *issuer,* who had responsibility for the company's books and records, *and*, who obtained substantial personal gain from their crimes. *United States v. Livesay*, 484 F.3d 1324 (11th Cir. 2007) (reversing sentence of probation for Corporate Controller who plead guilty to 78m(b)(5) for role in $1.4 billion HealthSouth fraud)[33]; *Lake*, 472 F.3d at 1247 (78m(b)(5) convictions against CEO and Chief Strategic Officer for circumvention of internal accounting controls, vacated on appeal)[34]; *United States v. Martin*, 455 F.3d 1227 (11th Cir. 2006) (reversing

United States, 430 U.S. 188, 191-92, 97 S.Ct. 990, 992-93 (1977); *Smith v. Goguen*, 415 U.S.566, 572-74, 94 S.Ct. 1242, 1247-48 (1974); *Rabe v. Washington,* 405 U.S. 313, 92 S.Ct. 993 (1972) (*per curiam*); *Papachristou v. City of Jacksonville*, 405 U.S. 156, 162, 92 S.Ct. 839, 843 (1972); *United States v. Bass,* 404 U.S. 336, 347-348, 92 S.Ct. 515, 522-523 (1971); *Coates v. City of Cincinnati*, 402 U.S. 611, 614, 91 S.Ct. 1686, 1688 (1971); *Bouie v. City of Columbia,* 378 U.S. 347, 351, 84 S.Ct. 1697, 1701 (1964); *Wright v. Georgia*, 373 U.S. 284, 293, 83 S.Ct. 1240, 1246 (1963); *Raley v. Ohio*, 360 U.S. 423, 437, 79 S.Ct. 1257, 1266 (1959); *Harriss,* 347 U.S. at 617, 74 S.Ct. at 811-812; *Winters v. New York*, 333 U.S. 507, 519-20, 68 S.Ct. 665, 672 (1948); *Lanzetta v. New Jersey*, 306 U.S. 451, 453, 59 S.Ct. 618, 619 (1939); *Gebardi v. United States*, 287 U.S.112, 122-23, 53 S.Ct. 35, 38 (1932); *McBoyle v. United States,* 283 U.S. 25, 27, 51 S.Ct. 340, 341 (1931); *Krichman v. United States*, 256 U.S. 363, 367-68, 41 S.Ct. 514, 516 (1921); *United States v. Gradwell*, 243 U.S. 476, 486, 37 S.Ct. 407, 411 (1917); *United States v. Wiltberger*, 5 Wheat. 76, 95, 5 L.Ed. 37 (1820) (Marshall, J.).

[33] *See also United States v. Livesay*, 146 Fed.Appx. 403 (11th Cir. 2005).

[34] *See also United States v. Wittig*, 425 F.Supp.2d 1196 (D.Kan. 2006).

sentence of probation upon guilty plea by Health South CFO)[35]; *United States v. Botts*, 135 Fed.Appx. 416, 2005 WL 1432476 (11th Cir. 2005) (reversing sentence of probation upon guilty plea by former Health South tax department executive for conspiracy to commit securities fraud, mail fraud and books and records violation); *United States v. Polishan*, 336 F.3d 234 (3d Cir. 2003) (affirming conviction, challenged only on evidentiary grounds, of Senior Vice President and CFO for books and records violation), *cert. denied*, 540 U.S. 1220, 124 S.Ct. 1521 (2004); *United States v. Bradstreet*, 135 F.3d 46 (1st Cir. 1998) (charging company president and CFO of knowingly falsifying the books and records to hide his securities fraud), *cert. denied*, 523 U.S. 1122, 118 S.Ct. 1805 (1998); *United States v. O'Hara*, 960 F.2d 11 (2d Cir. 1992) (refusing to accept plea withdrawal of employee who facilitated bribery of foreign officials); *United States v. Howard*, 471 F.Supp.2d 772 (S.D.Tex. 2007) (vacating convictions against CFO for books and records violation); *United States v. Gagalis*, — F.Supp.2d —, 2006 WL 931909 (D.N.H. 2006) (denying motion to dismiss books and records charges against officers of issuer); *United States v. Cummings*, 189 F.Supp.2d 67 (S.D.N.Y. 2002) (action for restitution against CFO who plead guilty to knowingly falsifying company's books and records).[36,37]

Thus, "neither the statute nor any prior judicial decision has fairly disclosed" Brown's conduct to be within the scope of the books and records provision.[38] "Due Process bars [this] Court

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[35] *See also United States v. Martin,* 135 Fed.Appx. 411 (11th Cir. 2005).

[36] *See also United States v. Wilson*, 2001 WL 798018 (S.D.N.Y. 2001).

[37] *See also Crop Growers Corp.*, 954 F.Supp. 335 (action against corporation for violation of books and records provision); *United States v. Lockheed Corp.*, 1995 WL 17064259 (N.D.Ga. 1995) (same).

[38] It is simply unfair to make an individual guess at his peril as to what a a court will hold in a new situation never before encountered by the courts. 1 Wayne R. LaFave, Substantive Criminal Law §2.1(f), at 117 (2d ed. 2003).

[] from applying a novel construction" of the statute to prosecute Brown now. *Lanier*, 520 U.S. at 266, 117 S.Ct. at 1225; *Accord Marks*, 430 U.S. at 191-92, 97 S.Ct. at 992-93 (reversing transporting and conspiracy to transport obscene material charges for lack of fair warning). In other words, "when choice has to be made between two readings of what conduct Congress has made a crime, it is appropriate, before we choose the harsher alternative, to require that Congress should have spoken in language that is clear and definite. We should not derive criminal outlawry from some ambiguous implication." *United States v. Universal C.I.T. Credit Corp.*, 344 U.S. 218, 221-22, 73 S.Ct. 227, 229 (1952). Indeed, an "unforeseeable judicial enlargement of a criminal statute, applied retroactively, operates precisely like an *ex post facto* law, such as Art. I, s 10, of the Constitution forbids." *Bouie*, 378 U.S. at 353-54, 84 S.Ct. at 1703. *Accord Brown*, 459 F.3d at 534 (DeMoss, J., concurring in part and dissenting in part).

B. The Government Cannot Use The General Conspiracy Statute To Prosecute A Defendant Who Cannot Be Prosecuted For A Substantive FCPA Violation.

Exhaustive research has disclosed no reported decision citing the books and records provision, before (or after) Brown's indictment–by the SEC as a civil action or otherwise–that seeks to impose civil *or* criminal liability on an *employee of another company* for *conspiracy to falsify* an issuer's books and records. The government cannot unilaterally amend or expand the statute by a conspiracy charge or otherwise to reach beyond the *issuer*. *See*, *e.g.*, *Central Bank of Denver v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 176-79, 114 S.Ct. 1439, 1448-49 (1994) (refusing to expand civil liability through an aiding and abetting charge under the Securities Act § 10b); *United States v. Castle*, 925 F.2d 831-32 (5th Cir. 1991) (refusing to expand liability through a

conspiracy charge under a criminal provision of the FCPA); *United States v. Chestman*, 947 F.2d 551, 570-71 (2d Cir. 1991) (*en banc*) (same), *cert. denied*, 503 U.S. 1004, 112 S.Ct. 1759 (1992).

1. The Government Could Not And Did Not Charge Brown With A Substantive FCPA Violation, And It Cannot Expand The Statute Through A Conspiracy Charge.

The government did not charge Brown with the substantive offense of violating the books and records provision. Indeed, it could not do so. As demonstrated above, the statute applies only to "issuers" and "internal controls"–codifying an affirmative legislative decision to sanction *only issuers*, while leaving the myriad business entities tangentially related to the alleged violations unpunished (and unindicted), lest any and all entities who conduct business with an issuer get swallowed up by the provision and incur guilt by association. *United States v. Williamson*, 235 F.Supp. 836, 838 (S.D.Tex. 1964) (By its express terms, statute condemns a single class of persons, and cannot be expanded by conspiracy to encompass other class of persons). *See Gebardi v. United States*, 287 U.S.112, 123, 53 S.Ct. 35, 38 (1932).

In *Williamson*, the Government charged a "shipper" with conspiring with a "carrier" to violate a substantive statutory provision related to transportation in interstate commerce which, by its plain terms, was only applicable to the "carrier." *Williamson*, 235 F.Supp. at 837. In explaining the relationship between the two parties, this Court stated: "The relationship of these parties was solely that of shipper-carrier, and [the shipper] had no interest or control over [the carrier's] trucks, nor did it induce or encourage [the carrier] to ship goods in interstate commerce without authority [in violation of statute], unless this patronage of his illegal activity constitued such inducement. Furthermore, there is no evidence that the charges for such transportation paid by [the shipper] were

other than the usual and normal tariffs charged for like transportation by duly authorized carriers. No rebates, concessions, or 'kickbacks' were involved." *Id*.

Under these circumstances, this Court refused to extend the statute to include a conspiracy charge: "The penalties of the statute are too clearly directed against the acts of the [carrier] as distinguished from the consent of the subject of the transportation." *Id*. at 838. "Such conduct *merely makes it possible for the carrier to violate the law*." *Id*. at 839 (emphasis added). Here, it is not even clear that Enron violated the law in this transaction, where the only accounting issue is the *timing* of part of its total $53 million gain, and no restatement was required. It is clear that the books and records statute only reaches *issuers*.

In enacting 78m(b)(2), Congress made it an offense for an "issuer" to "knowingly" falsify the *issuer's* books and records by improperly accounting for transactions *necessarily* conducted with other business entities. In other words, an agreement by a separate entity to enter into some predicate business transaction with the issuer is "impliedly required" under the terms of the books and records provision. *See United States v. Nasser*, 476 F.2d 1111, 1119 (7th Cir. 1973).[39] And, "[s]o far as [78m(b)(2)] goes, it is immaterial whether the [separate business entity] had knowledge of the facts which would make the [issuer] guilty of the offense, and the [separate entity] *is not made guilty of the offense under any circumstances*." *Id*. at 1119 (emphasis added).[40] *Accord United States v.*

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[39] In *Nasser*, the Seventh Circuit refused to approve the Government's attempt to expand the reach of a statute (including a conspiracy charge), which penalized ex-government attorneys who engage in "forbidden matters" (such as working on cases they were involved with while in government service), to entities who employed an ex-government attorney on those "forbidden matters." *Nasser*, 476 F.2d at 1114-15, 1118.

[40] Paraphrasing, the Court's further pronouncement in *Nasser* applies with equal force here: "[I]n evaluating the intent of Congress in failing to prescribe a penalty in [78m(b)(2)] for the [non-issuer], regardless of [its] degree of guilty knowledge or culpable intent, we think it more reasonable to read the omission as precluding punishment for the [non-issuer] than as leaving punishment for the [the non-issuer]

Herron, 825 F.2d 50, 57 (5th Cir. 1987) (defendants were aware of banks' CTR requirements but not guilty of wire fraud for making deposits deliberately structured not to trigger the required reporting). It would contravene the legislative intent demonstrated here "to hold the immunity which the [books and records provision] itself confers [to non-issuers] is taken away by the conspiracy statute." *Nigro v. United States*, 117 F.2d 624, 629 (8th Cir. 1941).

2. The Government Has Conceded It Cannot Prosecute By Conspiracy Persons It Cannot Reach With The Substantive Charge.

Furthermore, under Fifth Circuit precedent, the government's concession, and other relevant case law, the government cannot expand the reach of the books and records provision by a conspiracy charge to those who, by the plain text of the statute, cannot be charged with the substantive offense. *United States v. Bodmer*, 342 F.Supp.2d 176, 189-90 (S.D.N.Y. 2004); *United States v. Castle*, 925 F.2d 831, 832 (5th Cir. 1991). Indeed, **the government has conceded in other litigation that if the FCPA's criminal penalties do not apply to the defendant for a substantive charge, then the government cannot circumvent that limitation by charging the defendant with conspiracy to violate the FCPA**. *Bodmer*, 342 F.Supp. at 190. *Accord Gebardi*, 287 U.S. at 121-22, 53 S.Ct. at 37-38; *Castle*, 925 F.2d at 832. Accordingly, by the government's prior concession and as a matter of law, it may not prosecute Brown for conspiracy to falsify *Enron's* books because it could not charge him (and, notably, did not charge him) with the substantive offense.

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with guilty knowledge, up to a much greater maximum than that provided by [78m(b)(2)] for the [issuer], to the operation of the conspiracy statute." *Nasser*, 476 F.2d at 1120. Stated differently.

C. The Books And Records Prong Must Also Be Dismissed Because The Transaction Was Immaterial As A Matter Of Law.

The indictment charges, via conspiracy, a knowing and willful falsification of books and records by an *issuer* required to file reports–a violation punishable only under § 78ff of the Exchange Act. Section 78ff, in the contexts in which it had been applied in criminal prosecutions at the time of Brown's indictment, involved *filings* or some other *dissemination* of false information. However, this case was *not* brought under the filings clause of § 78ff or as a Rule 10b-5 (15 U.S.C. § 78j(b)) violation.[41] It was brought, instead, in the form of *only* a books and records conspiracy.

Throughout Barge I and to date, the government has repeatedly described this as a "securities fraud" and a "fraud on the public markets." In addition to the fatal flaw that the books and records prong does not reach persons beyond the *issuer*, and the government cannot charge a conspiracy to falsify books and records against a non-issuer, the charge also and alternately fails because a legally *immaterial* transaction cannot be prosecuted as a federal felony under the Securities Act.[42]

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[41] Despite the government's assertion that defendants conspired to conceal information from Arthur Andersen, the government did not charge Brown with false statements to auditors under § 78m(a) and 17 C.F.R. § 240.13b2-2, which *plainly* require proof of materiality. Here again, the Merrill Defendants had *no duty* to say anything to Enron's auditors.

[42] *See*, *e.g.*, *Krim v. BancTexas Group, Inc.*, 989 F.2d 1435, 1446 n.9 (5th Cir. 1993) ("[F]ailure to establish the materiality of the alleged omissions or misrepresentations is the death knell to [a] claim[] under both the Securities Act of 1933 and the Securities Exchange Act of 1934, for materiality is an essential element of a claim under each statute."); *Greenhouse v. MCG Capital Corp.*, 392 F.3d 650, 660 (4th Cir. 2004) ("Reading the law otherwise, as [the Government] would have us do, simply reads materiality out of the statute. Under this theory, almost any misrepresentation by a[n] officer – including, perhaps, one about his or her marital fidelity, political persuasion, or golf handicap – that might cause investors to question management's integrity could, as such, serve as the basis for a securities fraud [] action."); *see also Isquith v. Middle South Utilities, Inc.,* 847 F.2d 186, 207-08 (5th Cir. 1988), *cert. denied,* 488 U.S. 926, 109 S.Ct. 310 (1988). *And see Missouri Portland Cement Co. v. H.K. Porter Co., Inc.*, 535 F.2d 388, 393 (8th Cir. 1976) (§ 78m "is founded on the principle that full and fair disclosure of all *material* facts must be made.") (emphasis added).

The Enron Task Force plucked the books and records provision from approximately 30 years of relative obscurity and elevated it to a federal felony *per se* by indicting Brown for conspiracy to violate it. Misapplying the text and intent of the FCPA, the Task Force has turned the Exchange Act upside down to create a new genre of criminal securities fraud unprecedented in federal jurisdiction. The Supreme Court has held that fair warning requires dismissal where, as here, an "old law," "never before been resorted to as applicable" to the conduct charged, is resurrected in an attempt to bypass the legislative function. *United States v. Gradwell*, 243 U.S. 476, 486, 37 S.Ct. 407, 411 (1917). Before a man can be exposed to the criminal sanction under the federal law, "his case must be plainly and unmistakably within the provisions of some statute." *Id*. at 485, 37 S.Ct. at 411.[43]

Materiality is implicated throughout the Exchange Act and required for conviction when false information is disseminated–either in a filing, to the public, or to the issuers' auditors and accountants. *See Taubenfeld v. Hotels.com*, 385 F.Supp.2d 587, 592 (N.D.Tex. 2004) ("In order to be actionable [under the Exchange Act], a misrepresentation or omission of information must be material."). As evident in the text of 78m(b)(2), the books and records provision was originally intended to apply as an *internal* control, reasonably allowing for corrections to be made. For example, a division head at XYZ Corp. could deliberately book a gain or a loss that is unwarranted, but such an entry, even though made with the purpose of falsifying, would necessarily be reviewed on other levels at XYZ Corp. and may be modified or disregarded *internally* based on the

[43] *See also Morissette v. United States*, 342 U.S. 246, 263, 72 S.Ct. 240, 250 (1952) ("[W]here Congress borrows terms of art [here knowing falsification/misrepresentation in the securities context] in which are accumulated the legal tradition and meaning of centuries of practice, it presumably knows and adopts the cluster of ideas [here, materiality] that were attached to each borrowed word in the body of learning from which it was taken and the meaning its use will convey to the judicial mind unless otherwise instructed.").

determination of an accountant. The provisions are drafted to encourage and require such *internal review* and *correction* without expanding federal criminal jurisdiction to immaterial violations.

If a books and records violation is plucked from its place as an SEC tool to require the *issuer's employees* to correct entries *internally*, and it is elevated to a discrete criminal securities fraud under § 78ff, *against non-issuers*, it would be punishable by twenty years in prison and a $5 million fine. Under these circumstances, materiality *must* be required. *Cf. United States Gypsum*, 438 U.S. at 436-43, 98 S.Ct. at 2873-76 (Supreme Court reading an intent requirement into the Sherman Act for purposes of criminal enforcement, but not otherwise.).

To hold otherwise would lead to an absurd result: Brown himself could have announced Enron's 1999 gain on the barge deal directly to the public[44] or personally signed Enron's 10-K[45] and *not committed a crime*, but he could be tried and convicted here because a *bookkeeper* at *Enron* recorded an *immaterial* gain (*merely at the wrong time*) on *Enron's books*.[46] As a matter of law, this transaction was immaterial and cannot be prosecuted against Brown under any criminal provision of the Act. *Cf. Krim*, 989 F.2d at 1446 n. 9.[47]

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[44] Rule 10b-5 requires materiality.

[45] The "filings clause" of § 78ff(a) prohibits the filing of statement that is "false or misleading with respect to any material fact."

[46] "All laws are to be given a sensible construction; and a literal application of a statute, which would lead to absurd consequences, should be avoided whenever a reasonable application can be given to it, consistent with the legislative purpose." *United States v. Katz*, 271 U.S. 354, 357, 46 S.Ct. 513, 514 (1926).

[47] The fact that this transaction was immaterial, and that Merrill would not participate in any wrongful conduct or even approach a violation of the securities laws, was clearly important to both Merrill's counsel and these Defendants. Katherine Zrike, Chief Legal Counsel of the Investment Banking Division at Merrill, who shepherded the transaction through Merrill, confirmed that during the period preceding the transaction "we [Merrill] [] arrived at a comfort level that [the transaction] was not material" (22:4097, 4103-06, 4117, 4123-24). And it was only upon this determination of non-materiality, and mindful of securities

The Exchange Act implicates materiality throughout. If the books and records provision is to be elevated to this stature, then materiality must be read into the statute, to maintain consistency in the Exchange Act, with congressional intent, precedent, policy, and prudence in the exercise of federal criminal jurisdiction. Existing criminal precedent under the Act involved filings or some form of dissemination of misleading information in which materiality is always required.[48]

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law, that Merrill proceeded with the transaction (*Id*.).

Moreover, the barges were real. Merrill Lynch paid the money to Enron. Enron kept the money. Enron reported the gain and paid taxes on the Merrill sale in 1999, and Enron reported and paid taxes on the substantial gain it made on a larger package sale to AES in 2000 (21:3712-13, 3716, 3718, 3721). Neither party was ever required by auditors, regulators, or otherwise, to restate earnings from the barge transaction (*See id*.). The **total** gain reported was **correct**. If Enron had not reported the gain from the barge sale to Merrill Lynch in accounting year 1999, then the gain it reported in 2000 would have been that much larger. At most, even the accounting issue in this case boils down to the *timing* of the reporting of the *same amount* of *total*, *legitimate gain*.

At the very core of our nation's securities laws is the premise that there must be some form of ultimate deception. In other words, if shareholders/consumers are getting "exactly what they expect," then "the conduct is neither deceptive nor fraudulent - and therefore, not within the ambit of the federal securities laws." *United States v. Finnerty*, 474 F.Supp.2d 530, 537 (S.D.N.Y. 2007) (Defendant acquitted where Government did not prove that customers (shareholders) were deceived by defendant's actions.) (quoting *Chemical Bank v. Arthur Andersen & Co.*, 726 F.2d 930, 943 (2d Cir. 1984) (Friendly, J.), *cert. denied,* 469 U.S. 884, 105 S.Ct. 253 (1984)). In this case, Enron and Enron's shareholders got actual gain from the sale of the barges.

[48] *See Touche Ross & Co. v. Reddington*, 442 U.S. 560, 570 n.10, 99 S.Ct. 2479, 2486 (1979) (15 U.S.C. § 78ff authorizes criminal sanctions for violations of statutes and rules for materially misleading statements in filings); *United States v. Tarallo*, 380 F.3d 1174, 1187-88 (9th Cir. 2004) (requiring "intentionally acting with reckless disregard for the truth of material misleading statements in a filings case"), *amended*, 413 F.3d 928 (9th Cir. 2005); *United States v. Stringer*, 2005 WL 1231183, *2 (D.Or. 2005) (implying requirement of material misstatements); *United States v. Wilson*, 2001 WL 798018, *4-5 (S.D.N.Y 2001) (quoting §78ff in pertinent part). Regardless of whether it appears in the text, materiality is, and must be, an essential element of this type of crime. *Neder v. United States*, 527 U.S. 1, 4, 119 S.Ct. 1827, 1831 (1999) (materiality is an element of federal mail fraud, wire fraud, bank fraud, and tax fraud); *Krim*, 989 F.2d at 1446 n.9 (Materiality is an essential element in all actions brought under the Exchange Act.); *accord Taubenfeld*, 385 F.Supp.2d at 592.

The government creatively crafted these charges, fought to keep materiality out of the jury instructions in Barge I,[49] and told the jury it did not have to prove materiality, because it knew it *could not* prove this element.[50] *United States v. Gaudin*, 515 U.S. 506, 509-10, 115 S.Ct. 2310, 2312-13 (1995) (materiality is an element that must be decided by the jury beyond a reasonable doubt); *accord Sullivan v. Louisiana*, 508 U.S. 275, 277-78, 113 S.Ct. 2078, 2080-81 (1993).[51]

Merrill paid Enron $7 million, and Enron kept it. Enron made a total profit of $53 million on the barges within nine months, and it reported all the gains without double-counting (21:3712-13, 3716, 3718, 3721). *See Brown*, 459 F.3d at 536 (DeMoss, J. concurring in part and dissenting in part).[52] This case involves at most, the *timing* of a $12.5 million *pre-tax* gain ($7.8 million actual

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[49] All Defendants requested a correct instruction at Barge I: "A fact is material if it has a natural tendency to influence, or is capable of influencing, the decision of investors." *United States v. Gaudin*, 515 U.S. 506, 509-23, 115 S.Ct. 2310, 2313-20 (1995).

[50] The government has consistently urged that it *"doesn't have to prove materiality with respect to Enron's* books and records. . . . that's *not* something we have to prove for you to return a verdict of guilty" (30:6526).

[51] Under the framework established in *United States v. Wells*, 519 U.S. 482, 117 S.Ct. 921 (1997), materiality must be read into this statute. *Gaudin*, 519 U.S. at 490-98, 117 S.Ct. at 926-30. Similar analysis of discrete statutes routinely requires reading materiality into a federal statute. *See Neder* 527 U.S. at 20, 119 S.Ct. at 1827 (court applied the *Wells* framework and concluded that the federal crimes of mail fraud, wire fraud, and bank fraud, include a materiality requirement, despite the absence of that term in the statutory text); *United States ex rel. A+ Homecare, Inc. v. Medshares*, 400 F.3d 428, 442-43 (6th Cir. 2004) (materiality is an essential element under 31 U.S.C. § 3729(a)(1), 31 U.S.C. § 3729(c), and 31 U.S.C. § 3729(a)(7), even though not stated in the text of these statutes), *cert. denied*, 126 S.Ct. 797 (2005); *United States v. Nash*, 115 F.3d 1431, 1436 (9th Cir. 1997) (materiality requirement for 18 U.S.C. § 1344 survives *Wells* even though not stated in the text), *cert. denied*, 522 U.S. 1117, 118 S.Ct. 1054 (1998); *accord United States v. Rodriguez*, 140 F.3d 163, 167-68 (2d Cir. 1998).

[52] There were no false invoices or false assets exchanged. This was not a sham transaction. *See, e.g.*, *Compaq Computer Corp. and Subsidiaries v. C.I.R.*, 277 F.3d 778, 781-87 (5th Cir. 2001) (Transaction with "economic substance and a business purpose"–where risk is present–is not a "sham."). To quote Judge DeMoss, "**Merrill's $7 million was absolutely at risk**." *United States v. Brown*, 459 F.3d 509, 536 (5th Cir. 2006) ("Here, [preliminary] negotiations are no evidence of the actual nature of the deal because there was no legally enforceable take-out promise in the final written agreement. . . . The Government mischaracterizes the transaction evidenced by the Engagement Letter when it labels the agreement a 'sham,'

gain) by a company (for which Brown did not work) that had revenues of $40 billion, $957 million in net profits, and was "a massive user of capital," closing more than fifty financing deals annually totaling $20 *billion* or more (20:3620; 21:3769-70; GX801, 806). The barge deal was not material as a matter of law–under any legal standard.[53] Although in Barge I, the prosecutors wrapped themselves in the mantle of "Enron shareholders" and "investors," and pleaded with the jury in defense of "the integrity of our publicly traded markets and companies," as if this were a securities fraud prosecution (30:6141, 6143, 6144; 31:6557), a conspiracy charge to knowingly falsify books and records brought against an individual who is not the issuer for a legally immaterial transaction is simply not cognizable as a crime. *Cf. Grunewald v. United States*, 353 U.S. 391, 404, 77 S.Ct. 963, 973 (1957) (Federal courts "view with disfavor attempts to broaden the already pervasive and

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and asserts that Merrill was never 'at risk' during the transaction.") (DeMoss, J., concurring in part and dissenting in part) (emphasis added in first quotation). The panel majority in *Brown* did not reach the issue of the transfer of risk from Enron.

[53] In *Basic, Inc. v. Levinson*, 485 U.S. 224, 108 S.Ct. 978 (1988), the Supreme Court adopted the materiality rule of *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 96 S.Ct. 2126 (1976), and noted that, "a plaintiff must show that the statements were misleading as to a material fact. *It is not enough that a statement is false or incomplete, if the misrepresented fact is otherwise insignificant*." *Basic*, 485 U.S. at 238, 108 S.Ct. at 987; *see In re AMDOCS Ltd. Securities Litigation*, 390 F.3d 542, 548 (8th Cir. 2004) ("Alleged misrepresentations can be immaterial as a matter of law if they ... present or conceal such insignificant data that, in the total mix of information, it simply would not matter."); *ABC Arbitrage Plaintiffs Group v. Tchuruk*, 291 F.3d 336, 359-60 (5th Cir. 2002) (misstatements concerned amounts of money too small to have been material); *Parnes v. Gateway 2000, Inc.*, 122 F.3d 539, 547 (8th Cir. 1997) (2% valuation change in total assets was immaterial); *Glassman v. Computervision Corp.*, 90 F.3d 617, 631-32, n.22 (1st Cir. 1996) ("The relevant numbers are $2.5 million in domestic sales bookings as of week seven of the third quarter of 1992 and $3.3 million for the same period in 1991– a difference of $800,000, or less than 1% of the budgeted revenues for that quarter. This difference was immaterial as a matter of law."); *Greenhouse*, 392 F.3d at 656 ("[I]f the specific fact misrepresented is immaterial, a suit cannot succeed."); *Taubenfeld,* 385 F.Supp.2d at 592-93 (Undisclosed negative financial information was "immaterial as a matter of law.")

wide-sweeping nets of conspiracy prosecutions.").[54] The Securities Act does not criminalize conduct outside the issuer in the absence of dissemination of a material misstatement to auditors or the market. The books and records provision is even narrower. It does criminalize conduct outside the issuer, *or* in the absence of dissemination of a material misstatement to auditors or the market.

If the statute can be construed to allow criminal prosecution of a non-issuer for a legally immaterial transaction, then it is unconstitutional as applied because the Merrill Defendants had no fair warning of its reach. "Such restraint is particularly appropriate here, where the act[s] underlying the [indictment] [] [are] by [themselves] innocuous." *Arthur Andersen*, 544 U.S. at 703, 125 S.Ct. at 2134. No Merrill employee could reasonably believe that he could be criminally liable for *any* accounting wrong at a company with which Merrill does business–much less an *immaterial* entry in the books of a *separate* company to which he owed no duty and over which he had no control. *Id.* at 701, 125 S.Ct. at 2134; *Neder*, 527 U.S. at 5, 119 S.Ct. at 1832; *Touche Ross*, 442 U.S. at 570, 99 S.Ct. at 2486; *Bass*, 404 U.S. at 347-48, 92 S.Ct. at 522-2; *see also Regents*, 482 F.3d at 384.

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[54] And, it is beyond debate that every federal prosecution must be sustained by statutory authority. *See Krulewitch v. United States*, 336 U.S. 440, 445-46, 69 S.Ct. 716, 719-20 (1947) ("This case illustrates a present drift in the federal law of conspiracy which warrants some further comment because it is characteristic of the long evolution of that elastic, sprawling and pervasive offense. Its history exemplifies the tendency of a principle to expand itself to the limit of its logic. The unavailing protest of courts against the growing habit to indict for conspiracy in lieu of prosecuting for the substantive offense itself, or in addition thereto, suggests that loose practice as to this offense constitutes a serious threat to fairness in our administration of justice.") (Jackson, J., concurring) (citation omitted).

IV. THE SEC'S TREATMENT OF OTHER BANKS SUPPORTS DISMISSAL OF THE INDICTMENT. AT MOST, THIS IS A CIVIL MATTER.

A. Other Financial Institutions Were Far More Culpable Than Merrill, But Neither the Other Banks Nor Their Employees Have Been Criminally Prosecuted For The Larger Roles They Played With Enron.

Conduct of other banks and individuals who dealt with Enron in far more significant transactions has been handled by the SEC in civil actions. As such, the instant prosecution is a quintessential example of the arbitrary and discriminatory enforcement sought to be proscribed by the rule of legality. *Kolender v. Lawson*, 461 U.S. 352, 357, 103 S.Ct. 1855, 1858 (1983). This rule alone requires dismissal of the entire indictment for no fair warning.[55]

The Third-Interim Report of Neal Batson, Court-Appointed Examiner,[56] identifies six financial institutions and discusses their involvement with Enron and their potential liability: Citigroup, JPMorgan Chase, Barclays, BT/Deutsche, CIBC and Merrill Lynch. As the Bankruptcy Examiner noted, "[t]here were significant differences in the level of participation by the Financial Institutions in Enron's SPE transactions."[57] The Examiner specifically noted that Merrill Lynch did *not* participate in as many SPE transactions as the other banks identified,[58] and Merrill Lynch was not even regarded by Enron as a Tier I bank.

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[55] *Brown*, 459 F.3d at 535 ("The cumulative effect of a vague criminal statute, a broad conception of conspiracy, and an unprincipled theory of harm that connects the ultimate demise of Enron to a single transaction is a very real threat, of potentially dramatic proportion, to legitimate and lawful business relationships and the negotiations necessary to the creation of such relationships.") (DeMoss, J., concurring in part and dissenting in part).

[56] "Third Interim Report" of the Enron Bankruptcy Examiner, *available at* http://www.enron.com/corp/por/examiner3.html.

[57] Third Interim Report, p. 46.

[58] *Id*. at 47.

Enron had an internal ranking system for the financial institutions with whom it worked–Tier 1, 2, or 3.[59] Tier I banks offered the ability to loan large amounts of money to Enron in a short amount of time and the ability to "come up with structures and transactions that would help Enron creatively solve its financial reporting problems." "Solv[ing] Enron's financial reporting problems" entailed helping Enron address the issue of how to handle financial results that threatened Enron's ability to maintain its investment grade credit rating or to meet its earnings targets. In comparison to Tier 2 or Tier 3 banks, Tier 1 banks devised and presented structures to Enron to help bridge the gap between reality and the appearance Enron wanted to present to the outside world. *Merrill Lynch was never designated Tier 1*.[60]

(i) Citigroup. Citigroup was considered a Tier 1 bank during the five years before Enron's collapse. Citigroup completed over sixty transactions with Enron, receiving approximately $188 million in revenue related to Enron transactions.[61] Because of its extensive involvement with Enron, Citigroup had significant access to Enron's financial information.[62] As noted by the Bankruptcy Examiner and confirmed by Fastow, Citigroup designed and helped implement complex and cutting edge structured finance transactions used by Enron to "solve its problems."[63] As Fastow stated, "My

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[59] Deposition of Andrew Stuart Fastow, October 23, 2006, I:22, ("Fastow Depo."; Exhibit 1); *see also* Third Interim Report, p. 46 n. 121.

[60] Fastow Depo. at pp. 23. Tier 1 banks included Citigroup, JPMorgan Chase, CSFB, CIBC, BT/Dcutsche, Barclays and Royal Bank of Scotland. *Id*. at pp. 24, 27-28.

[61] Third Interim Report, p. 51.

[62] *Id*. at Appendix D, pp. 16, 32.

[63] *Id*. at p. 16; Fastow Depo.I:39.

personal view of Citigroup was that they brought at least one great idea to us each year to help us solve our problems."[64]

Citigroup completed nine prepay transactions with Enron (using special purpose entities) that totaled over $4.6 *billion*.[65] The Nahanni minority interest transaction alone (which Fastow recalls was designed by Larry Nath at Citibank to allow Enron to convert debt to minority interest) "represented *41% of Enron's total reported cash flow* from operating activities for 1999."[66] The Nighthawk minority interest transaction–a year-end 1997 deal also designed by Citigroup–raised $500 million for Enron.[67] *The Citigroup prepays alone had a material impact on Enron's cash flows* from operating activities.[68]

The Examiner declared that Citigroup knew that the prepay transactions in which it was involved "were simply debt packaged as commodity swaps." Indeed, the Examiner pointed to repeated evidence that Citigroup clearly understood how Enron accounted for the Citigroup prepays, including the following passage from an internal Citigroup document:

> The transaction provides favorable accounting treatment for the customer. Although the deal is effectively a loan, the form of the transaction would allow the customer to reflect it as "liabilities from price risk management activity" on their on their [sic] balance sheet and also provide a favourable [sic] impact on reported cash flow from operations.[69]

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[64] Fastow Depo.I:39.

[65] Third Interim Report, p. 55.

[66] *Id*. at p. 60; Fastow Depo.I:66-67.

[67] Third Interim Report, pp. 60-61; Fastow Depo.I:66-67.

[68] Third Interim Report's Appendix D, pp. 47, 48.

[69] *Id*. at p. 70, quoting Minutes of Citibank CMAC, June 22, 1999 (the "CMAC Truman Minutes").

> Enron uses prepay transactions to raise quarter-end non-debt funding. Also, the mark-to-market accounting method used in the trading business results in earnings recognition prior to receipt of the associated cash flow. A prepay transaction essentially monetizes this value creation, and helps to balance earnings with cash flow.[70]

Additionally, Citigroup facilitated Enron's Yosemite I and II transactions "with a substantial belief that Enron did not intend to account for them properly under GAAP." The Examiner concluded that "Citigroup knew that the approximately $1.1 billion of proceeds would not be reflected as debt on Enron's balance sheet."[71] Appendix D to the Third Interim Report is replete with additional citations to evidence the Examiner deemed indicia of Citigroup's knowledge of the economic substance of Enron transactions.

(ii) JPMorgan Chase. JPMorgan Chase "consistently achieved and maintained Tier 1 status among Enron's banks."[72] JPMorgan Chase's relationship with Enron was lucrative, "generating annual fees in excess of $15 million and total revenues of $17 million" for the Global Oil and Gas Group of JPMorgan Chase by 1999.[73] In 2000 alone, "the 'relationship revenues' to JPMorgan Chase [from Enron] totaled $29.8 million.[74] JPMorgan Chase's most significant SPE transactions–but by no means its only transactions with Enron–were a series of prepay transactions

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[70] *Id*. at p. 71, quoting Memorandum from Michael Nepveux, Citigroup, to Bill Fox, Citigroup, regarding Enron Corp.-Sept. 30 Prepay Transaction, Sept. 19, 2001.

[71] *Id*. at p. 87.

[72] Third Interim Report, p. 62.

[73] *Id*. at p. 61, citing Memorandum from Josh Rogers, JPMorgan Chase, to Balance Sheet Committee, and copy to Robert Traband, JPMorgan Chase, Nov. 22, 1999 (date marked as "Approved").

[74] *Id*., citing Memorandum from Rick Walker, JP Morgan Chase, to Don Layton and Marc Shapiro, JPMorgan Chase, regarding Enron, Jan. 18, 2001.

called the Mahonia Transactions, occurring from 1992-2001.[75] The twelve Mahonia Transactions with JPMorgan Chase provided Enron with nearly half (over *$3.7 billion*) of the $8.6 billion in total financing that Enron obtained through all of its prepay transactions from 1992-2001.[76] The Examiner determined that "because of the magnitude of the Mahonia Transactions, *they had a material effect* on Enron's financial statements."[77] The Examiner concluded that evidence demonstrated that JPMorgan Chase knew the Mahonia Transactions were, in economic substance, loans to Enron.[78] As early as 1994, JPMorgan Chase described its Enron prepay transactions as a loan stating, "Chase would analyze credit risk resulting from the advance of funds under a prepaid forward as it would if making a loan on an unsecured basis."[79]

The Examiner also determined that evidence exists that JPMorgan Chase knew that "Enron would report its obligations under the Mahonia Transactions as price risk management liabilities rather than as debt." The proceeds were reported as cash flow from operations instead of cash flow from financing activities, which the Examiner again concluded that JPMorgan Chase knew.[80] As one JPMorgan Chase employee stated:

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[75] *Id*. at p. 62.

[76] Third Interim Report's Appendix E, p. 18.

[77] *Id*. at p. 21.

[78] Third Interim Report, pp. 63-64; *id*. at Appendix E, p. 23.

[79] Third Interim Report, Appendix E, p. 37, quoting Letter from Garland D. Sims, Vice President and Senior Associate Counsel, JPMorgan Chase, to Senior Deputy Comptroller for Bank Supervision-Operations, Office of the Comptroller of the Currency, Nov. 3, 1994.

[80] Third Interim Report, p. 64.

> Enron loves these deals as they are able to **hide funded debt from their equity analysts** because they (at the very least) book it as deferred rev or (better yet) bury it in their trading liabilities.[81]

(iii) Barclays. Barclays was designated a Tier 1 bank in 1993 and maintained that designation until Enron's bankruptcy.[82] Barclays participated in a wide array of Enron transactions and formally reviewed Enron's finances and creditworthiness on an annual basis. Every two years, Barclays' review included face-to-face meetings with Enron executives, where Barclays employees questioned Enron about financial issues, including Enron's structured financing activities. Thus, Barclays "had significantly more access to Enron's management and financial information than most others."[83]

Fastow testified that he and Barclays schemed to use structured finance transactions to create a misleading appearance of a stronger financial position than actually existed at Enron.[84] By the end of 1998, Barclays' senior management was expressing concern about Enron's off-balance sheet liabilities and "had concluded that Enron's increasing reliance on structured financing activities was having a material impact on Enron's financial statements."[85] As a result of the 1999 annual review, "Barclays' most senior credit committee stated that 'it could not shed the belief that Enron was paddling underneath the surface to hold on to its investment grade status as it became harder and

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[81] *Id.* at p. 65, quoting email from George Service, JPMorgan Chase, to Karen Simon, and copy to Jeffrey Dellapina, JPMorgan Chase, Nov. 25, 1998 (emphasis in original). Appendix E to the Third Interim Report contains additional citations to internal communications of JPMorgan Chase and its knowledge of the economic substance of the Mahonia Transactions.

[82] Third Interim Report, p. 65.

[83] Third Interim Report's Appendix F, p. 10.

[84] Fastow Depo.II:535.

[85] Third Interim Report's Appendix F, p. 11.

harder to replicate the previous years' strong performances.'"[86] Notwithstanding, Barclays continued to execute off-balance sheet transactions with Enron.

Barclays participated in a number of SPE transactions that generated significant proceeds for Enron. The SO_2 Transaction alone provided Enron with proceeds of approximately *$167.6 million*.[87] The Examiner also found that Barclays played vital roles in the Chewco Transaction, the J.T. Holdings Transaction, the Nikita FAS 140 Transaction and Three Prepay Transactions, *including requiring and receiving from Enron officers verbal assurances covering Barclays' equity risk in all of these various SPE structures*.[88] *By November 2001, Barclays' estimated exposure limits exceeded $728 million*.[89] The Examiner concluded that "*Barclays knew Enron's officers entered into the Prepay Transactions to manipulate Enron's financial statements*" and that "Barclays knew that Enron was just borrowing money through the Prepay Transactions." *Moreover, Barclays knew at least by 2000 that Enron improperly booked the cash received from prepays as cash flow from operations*.[90]

(iv) BT/Deutsche. Also a Tier 1 bank, "BT/Deutsche played a major role in six of the eleven Tax Transactions that originated in Enron's tax department during the period from 1995-2000."[91] BT/Deutsche developed and promoted the tax and accounting structures to Enron and

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[86] *Id*. at p. 14, quoting July 1999 Group Credit Committee Minutes, at 3.

[87] Third Interim Report, p. 67.

[88] *Id*. at pp. 65-66; *see also* Third Interim Report's Appendix F, pp. 8-9.

[89] Third Interim Report's Appendix F, p. 19.

[90] *Id*. at p. 58.

[91] Third Interim Report, p. 72.

then also participated in the transactions, often as the only party other than Enron affiliates.[92] Fastow testified that Deutsche Bank and he engaged in a scheme that involved structured finance transactions and tax transactions that created an inaccurate and misleading picture of the financial condition of Enron.[93] BT/Deutsche received approximately $43 million in fees for its work with Enron from 1997 until Enron's bankruptcy filing.[94] On one transaction alone, the Cochise Transaction, "*BT/Deutsche enabled Enron to erroneously report $36.5 million of gain on the sale, an amount equal to more than 10% of Enron's reported net income for the quarter*.[95]

(v) CIBC. CIBC earned Tier 1 status, likely through its involvement in Enron's FAS 140 Transactions. From 1998 until October 2001, CIBC participated in at least eleven of these deals, which earned CIBC in excess of $14 million in fees.[96] *These FAS 140 Transactions allowed Enron to record approximately $585 million of income from gain on sales of assets that Enron should not have recorded*. These CIBC transactions also allowed Enron to receive over $1.7 billion in proceeds, which Enron erroneously recorded as either cash flow from operating activities or cash flow from investing activities. *CIBC's participation allowed Enron to "understate debt by $380 million, $362.4 million, and $275.6 million* in 1998, 1999, and 2000, respectively."[97]

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[92] *Id*. at p. 73.

[93] Fastow Depo.II:536.

[94] Third Interim Report, p. 73.

[95] *Id*. at p. 76.

[96] *Id*. at p. 76.

[97] Third Interim Report's Appendix H, p. 2.

(vi) Merrill Lynch. Of the approximately thirty-five transactions Merrill Lynch entered into with Enron, the Examiner found fault with only two transactions: the Nigerian Barge Transaction and the electricity trade transactions occurring in the fourth quarter of 1999.[98] Merrill Lynch neither structured nor designed these transactions.[99] The Examiner acknowledged that Merrill Lynch had a limited relationship and role with Enron compared with other banks, such as Citigroup and JPMorgan Chase, and that Merrill Lynch played a limited role as a lender or financial advisor to Enron.[100] Merrill Lynch received only $775,000 in fees from the Nigerian Barge transactions.[101]

B. Government Actions, *If Any*, Against *All* These Other Financial Institutions And Their Employees, Have Been Purely Civil.[102]

(i) Citigroup settled with the SEC in July, 2003 for $101,250,000. No governmental actions against any of its employees have ever been instituted.

(ii) JP Morgan Chase settled with the SEC in July, 2003 for $135,000,000. No governmental actions against any of its employees have ever been instituted.

(iii) Neither Barclays nor any of its employees have faced *any* enforcement action.

(iv) Neither BT/Deutsche nor any of its employees have faced *any* enforcement action.

(v) CIBC settled with the SEC in December, 2003 for $80,000,000. The SEC also filed a civil action against Daniel Ferguson, Ian Schottlaender and Mark Wolf. Ferguson and Wolf settled for $563,000 and $60,000, respectively, in December, 2003. Schottlaender settled for $528,750 in June, 2004.

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[98] Third Interim Report's Appendix I, p. 2.

[99] *Id*. at pp. 31, 42.

[100] *Id*. at pp. 12, 15.

[101] *Id*. at p. 6, fn.14.

[102] These are not even all the banks criticized by the Enron Bankruptcy Examiners. *See* Harrison Goldin's November, 2003 Report (addressing Royal Bank of Canada) and Neal Batson's Final Report (addressing Royal Bank of Scotland, Credit Suisse First Boston, and Toronto Dominion). Discussion of those banks would only add to the force of our analysis.

(vi) Merrill Lynch settled with the SEC in July, 2003, in an enforcement proceeding which also named Dan Bayly, Tom Davis, Robert Furst and Schuyler Tilney. Then, Dan Bayly, Jim Brown, Robert Furst and Bill Fuhs were:

- *indicted* in the fall of 2003;
- *tried and improperly convicted* in the fall of 2004; and,
- *sent to prison for almost a year* in 2005-2006 before the Fifth Circuit ordered their release, and ordered Fuhs acquitted.

The indictment must be dismissed in its entirety. The SEC is the enforcement agency, if any is needed, for resolving these charges.[103] **Notably, like Fuhs who was acquitted by the Fifth Circuit, Jim Brown has not even been named in the SEC action.** These Merrill Lynch executives were singled out and humiliated. They will carry the stigma of this unprecedented prosecution, as no other Enron bankers will, for the rest of their lives.[104] No other individuals or companies in

[103] There is no need to concoct novel theories to stretch the wire fraud statute or the books and records provision to protect the market or investors. For example, the SEC has broad regulatory and enforcement authority over companies within its jurisdiction. 15 U.S.C. § § 78o-1-5. It can: (1) issue injunctions, 15 U.S.C. § 77h; (2) impose disciplinary sanctions against broker-dealers; (3) pursue a panoply of administrative remedies; (4) issue cease and desist orders, including ex parte, 15 U.S.C. § 77h-1(a); (5) pursue "equitable remedies," *Mitchell v. Robert Mario Jewelry*, 361 U.S. 288, 80 S.Ct. 332 (1960); (6) order monetary sanctions including disgorgement of ill-gotten gains and fines, 15 U.S.C. 77t(d); and (7) create "novel" sanctions or "ancillary" remedies, so long as those sanctions are not "arbitrary and capricious" as assessed under the Exchange Act. 15 U.S.C. § 78o(b)(4). 15 U.S.C. § 78i prohibits "manipulation of security prices." § 78j broadly prohibits "manipulative and deceptive devices." This authority is intended to (1) vindicate the public interest in an orderly and honest securities market; (2) acknowledge the issuer's interest in mitigating liability and other private harms which might flow from violations; and (3) vindicate purchaser's interest flowing from the improvident purchase.

[104] *But see United States v. Bermingham*, — F.Supp.2d —, 2007 WL 1052600, *1 n.1 (S.D.Tex. 2007). Of course, three NatWest Bankers have been indicted, but that case involves indictment allegations of self-dealing, *monetary gain flowing to the Defendants at the expense of their employer*, and tangible objects of property ($7.3 million of self enrichment) to actually support a wire fraud charge. *Id.* at *6 (The indictment alleges: "Defendants, who were officials entrusted to represent their employer's affairs, . . . scheme[d] to defraud their employer of and to appropriate for themselves a valuable property interest belonging to their employer. The alleged conduct was reasonably calculated, indeed *intended,* to deceive GNW of Swap Sub's value and to conceal their naked self-interest in recommending its sale at a grossly undervalued price-a conclusion that is reinforced by their structuring of a complex series of transactions designed to hide their receipt of over $7 million in proceeds that might otherwise have gone to their

positions similar to Brown have been prosecuted at all–much less by the Enron Task Force–even though their conduct was clear, egregious, materal and damaging to Enron or its shareholders. The Supreme Court's decision in *Kolender*, applying the rule of legality, prohibits such arbitrary and discriminatory criminal enforcement and requires dismissal of the indictment for lack of fair warning. *Kolender* , 461 U.S. at 357, 103 S.Ct. at 1858 .

V. NEITHER THE STATUTES STANDING ALONE, AS CONSTRUED BY THE COURTS, OR, BY THE SEC, MADE IT REASONABLY CLEAR AT THE TIME THAT THE CONDUCT OF THE MERRILL DEFENDANTS WAS CRIMINAL. DUE PROCESS AND THE RULE OF LENITY REQUIRE DISMISSAL OF THE INDICTMENT.

On its face, the indictment stretches these criminal statutes beyond their limits or intent and disregards two bedrock due process principles: that ambiguities in criminal statutes must be resolved in favor of the defendant, *and*, that no one may be convicted of a crime without fair warning that his conduct was criminal. *United States v. Bass*, 404 U.S. 336, 346-47, 92 S.Ct. 515, 522-23 (1971). Long ago, Mr. Justice Holmes wrote that our citizens are entitled to "fair warning . . . in language that the common world will understand of what the law intends to do if a certain line is passed. To make the warning fair, so far as possible, the line should be clear." *McBoyle v. United States*, 283 U.S. 25, 27, 51 S.Ct. 340, 341 (1931).[105] "'The . . . principle is that no man shall be held criminally

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employer."). The facts the government alleged here, as this Court noted, are very different. The Merrill Lynch Defendants neither sought nor obtained any money or property nor did they deceive their employer, Merrill Lynch (indeed, Enron and its shareholders were not deprived of any money or property); and the Merrill Defendants were simply doing their job. This Court recognized this critical fact at Brown's sentencing, noting that Brown was "engaged in his regular job," and further, that "he was playing his ordinary role in this matter as an employee at Merrill Lynch" (41:27). It also noted the factual differences between the record evidence in *Brown* and the allegations in the indictment in *Bermingham*. *Id.* at *1.

[105] "The rule that penal laws are to be construed strictly, is perhaps not much less old than construction itself. It is founded on the tenderness of the law for the rights of individuals; and on the plain principle that the power of punishment is vested in the legislative, not in the judicial department." *United States v. Wiltberger*, 5 Wheat. 76, 95, 5 L.Ed. 37 (1820) (Marshall, J.); *accord United States v. Brown*, 459

responsible for conduct which he could not reasonably understand to be proscribed.'" *Bouie v. City of Columbia*, 378 U.S. 347, 351, 84 S.Ct. 1697, 1701 (1964) (quoting *United States v. Harriss*, 347 U.S. 612, 617, 74 S.Ct. 808, 812 (1954).

In fact, under the principle of legality, "conduct may not be treated as criminal unless it has been so defined by [a competent] authority . . . before it has taken place." Herbert L. Packer, *The Limits of the Criminal Sanction,* 80 (1968). Further, "because of the seriousness of criminal penalties and because criminal punishment usually represents the moral condemnation of the community, legislatures and not courts, should define criminal activity. This policy embodies 'the instinctive distaste against men languishing in prison unless the lawmaker has clearly said that they should.'" *Bass*, 404 U.S. at 347-48, 92 S.Ct. at 522-23 (internal citations omitted).

There are three primary corollaries to fair warning, each of which applies here:

- First, the vagueness doctrine bars enforcement of a statute which either forbids or requires commission of an act "in terms so vague that men of common intelligence must necessarily guess at its meaning and differ as to its application." *Connally v. General Construction Co.*, 269 U.S. 385, 391, 46 S.Ct. 126, 127 (1926).

- Second, the rule of lenity requires that criminal statutes be strictly construed, resolving any ambiguity so as to apply the statute only to conduct clearly covered. *Liparota v. United States*, 471 U.S. 419, 427, 105 S.Ct. 2084, 2089 (1985).

- Third, "due process bars courts from applying a novel construction of a criminal statute to conduct that neither the statute nor any prior judicial decision has fairly disclosed to be within its scope." *Lanier*, 520 U.S. at 266, 117 S.Ct. at 1225.

"In each of these guises, the touchstone is whether the statute, either standing alone or as construed, made it reasonably clear at the relevant time that the defendant's conduct was

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F.3d 509, 534 (5th Cir. 2006), *cert. denied*, 127 S.Ct. 2249 (2007) ("[W]e lack the constitutional power to . . . define what constitutes criminal conduct on an *ex post facto* and *ad hoc* basis.") (DeMoss, J., concurring in part and dissenting in part).

criminal." *Id*. at 267, 117 S.Ct. at 1225 (emphasis added). Nothing in the law before (or even after) this prosecution informs that the conduct of the Merrill defendants was criminal.

A fourth corollary also applies here: that a criminal offense be defined "in a manner that does not encourage discriminatory enforcement." *Kolender v. Lawson*, 461 U.S. 352, 357, 103 S.Ct. 1855, 1858 (1983). The varying and disparate civil enforcement and criminal actions following and related to the Enron melt-down demonstrate that the Department of Justice has made arbitrary determinations both as to which banks or other entities to charge, and within those banks or entities, as to which individuals to charge. *See supra* section IV.. Disturbingly, the Department of Justice has chosen to make deals and provide extraordinary leniency to the self-enriched architects of Enron's demise–Fastow, Glisan, and Kopper. The rule of legality is therefore "necessary in order to secure evenhandedness in the administration of justice and to eliminate the oppressive and arbitrary exercise of official discretion." *Packer*, *supra* at 80; *Kolender*, 461 U.S. at 357, 103 S.Ct. at 1858.

The line criminalizing facially innocent conduct must be clear. As Mr. Justice Holmes noted, 'it is not likely that a criminal will consider the text of the law before he murders or steals, . . .", but (paraphrasing), it is reasonable to imagine reputable businessmen, such as those here, trying to "'[steer] a careful course between violation of the statute (and lawful conduct).'" *United States v. Hood*, 343 U.S. 148, 151, 72 S.Ct. 568, 570 (1952). *And see United States Gypsum*, 438 U.S. at 441, 98 S.Ct. at 2875. ("The imposition of criminal liability [in such a situation], without inquiring into the intent with which it was undertaken, holds out the distinct possibility of overdetterence").

These concerns are even more valid and critical in the business context, where tax laws and accounting rules depend on many fine lines that often distill to a judgment call.[106] Businesses depend on clear rules within which to operate. *Arthur Andersen LLP v. United States*, 544 U.S. 696, 703-04, 125 S.Ct. 2129, 2134-35 (2005); *Dirks v. S.E.C.*, 463 U.S. 646, 659, 664, 103 S.Ct. 3255, 3264, 3266 (1983). These Merrill Lynch businessmen consulted corporate and outside counsel, trying to steer a purely lawful course in completing this financially insignificant and legally immaterial transaction with Enron. At no time did they *believe* that their conduct was unlawful, nor did they *intend* to engage in any conduct that was. As for Brown, "[w]hatever his civil liabilities, he is not a criminal and he should not have been convicted of a crime." *United States v. Phillips*, 600 F.2d 535, 541 (5th Cir. 1979).

More importantly, neither the text of the statutes, their judicial interpretations nor their SEC applications, gave the Merrill Defendants *any* warning–much less *fair* warning–that their conduct was criminal. This case starkly illustrates the need for limiting principles in the application of criminal statutes whose sweep the Government would have extend to all persons who conducted business with Enron. "Due Process bars [this] court[] from applying a novel construction of a

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[106] *See supra* section IV.. This is why issues such as these are and should be handled under our civil laws or by the SEC. *United States v. Bishop*, 412 U.S. 346, 360-61, 93 S.Ct. 2008, 2017 (1973) ("In our complex tax system, uncertainty often arises even among taxpayers who earnestly wish to follow the law," and "it is not the purpose of the law to penalize frank difference of opinion or innocent errors despite the exercise of reasonable care.") (internal citations omitted); *United States v. Crop Growers Corp.*, 954 F.Supp. 335, 348 (D.D.C. 1997) ("[C]riminal liability cannot be extended to violations of Financial Accounting Standards Board (FASB) standards not codified in criminal statutes and open to varying interpretations."). *Accord Brown*, 459 F.3d at 535 (To regulate such transactions via the criminal sanction would have a "very real threat, of potentially dramatic proportion, to legitimate and lawful business relationships.") (DeMoss, J., concurring in part and dissenting in part). *See*, *e.g.*, *United States v. Lee*, 82 F.Supp.2d 384, 389 (E.D.Pa. 2000) (Court does "not doubt that [defendant's] behavior, as alleged, was wrongful, and it seems clear that such acts [might] lead to civil liability. Absent further guidance from Congress, however, we cannot with fidelity to due process read the language of [the statute] to criminalize" the conduct alleged here.).

criminal statute to conduct that neither the statute nor any prior judicial decision has fairly disclosed to be within its scope." *Lanier*, 520 U.S. at 266, 117 S.Ct. at 1225, *quoting Marks*, 430 U.S. at 191-92, 97 S.Ct. at 992-93. *See Tanner v. United States*, 483 U.S. 107, 130-31, 107 S.Ct. 2739, 2753 (1987) (Warning against loose interpretations of criminal fraud statutes which allow the fact situation to define the crimes). None of the statutes on which this indictment is based has been construed previously to reach this conduct, and the entire indictment must be dismissed. *Lanier*, 520 U.S. at 266, 117 S.Ct. at 1225; *United States v. Ratcliff*, 488 F.3d 639, 645-46 (5th Cir. 2007); *United States v Herron*, 825 F.2d 50, 57 (5th Cir. 1987).

CONCLUSION

For these reasons, the indictment must be dismissed in its entirety. The indictment on its face fails to allege an object that was sought, obtained by or deprived of anyone. It fails to state a cognizable wire fraud. In addition, the statutes on which the government crafted this unprecedented prosecution cannot be tortured to reach the conduct of these Defendants. Brown cannot be prosecuted for a substantive books and records violation, and therefore, as the government has conceded in other litigation, he cannot be prosecuted for conspiracy to violate that provision. Brown obtained no money or property nor sought to deprive another of same. He had no duty to Enron or its shareholders.

The Defendants had no fair warning that their conduct could be criminal. Clear controlling precedent, fundamental Due Process, the rule of lenity, and the rule of legality mandate dismissal of all charges against Brown.

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CERTIFICATE OF CONFERENCE

I hereby certify that the parties have conferred on the Defendants' Motion to Dismiss the Indictment, and that AUSA Spencer advised that the Government opposes this motion.

/s/ Sidney Powell
Sidney Powell

CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing was served upon Arnold Spencer, counsel for the United States, via the ECF system. It has also been served electronically on all counsel of record.

/s/ Sidney Powell
Sidney Powell