The following constitutes the order of the Court.

Signed December 9, 2005 **United States Bankruptcy Judge**

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

IN RE:	§	
	§	
ENRON CORPORATION, et al.,	§	CASE NO. 01-16034-AJG
	§	(Southern District of New York)
D E B T O R S.	§	
	§	
	§	
OFFICIAL EMPLOYMENT-RELATED	§	
ISSUES COMMITTEE OF ENRON CORP.,	§	
PLAINTIFF,	§	
	§	
VS.	§	ADVERSARY NO. 03-3522
	§	
JOHN D. ARNOLD,[1] et al.,	§	
DEFENDANTS.	§	
	§	

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[1] Both Mr. Arnold and Mr. Lavorato have settled their respective disputes with Plaintiff; however, all parties have continued to refer to the foregoing cases as noted *supra*. Therefore, the foregoing adversaries will continue to be styled as noted *supra*.

	§	
OFFICIAL EMPLOYMENT-RELATED	§	
ISSUES COMMITTEE OF ENRON CORP.,	§	
PLAINTIFF,	§	
	§	
VS.	§	ADVERSARY NO. 03-3721
	§	
JOHN LAVORATO,[1] et al.,	§	
DEFENDANTS.	§	

MEMORANDUM OF DECISION

I. THE BANKRUPTCY FILING AND PARTIES TO THE ADVERSARIES

Enron Corporation ("ENE"), Enron North America Corporation ("ENA"), and certain other affiliated entities filed for bankruptcy protection on Sunday, December 2, 2001, at 4:56 a.m. in the Southern District of New York.[2] In this decision, the court will generally refer to ENE, ENA, and the affiliated entities as Enron, except where circumstances dictate otherwise.[3]

The Enron entities were not consolidated prepetition although they had consolidated financial statements. In the Disclosure Statement for the Fifth Amended Joint Plan for Reorganization (the "Disclosure Statement"), ENA is listed as one of ENE's 172 affiliated entities. ENA is listed as one of fifty-eight filing debtors that were part of ENE's wholesale services division.

On March 29, 2002, the United States Trustee appointed the

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[2] When Enron declared bankruptcy, it was the seventh largest publicly traded company in the United States. *See* Ex. 45 at 11.

[3] In Judge Greendyke's opinions of April 19, 2004 and May 24, 2004, as well as Judge Felsenthal's opinions referred to hereafter, such Judges also referred to Enron Corporation, Enron North America Corporation, and other related entities collectively as Enron.

Official Employment-Related Issues Committee of Enron Corporation (the "Employment Committee") as an official creditors' committee authorized to pursue these avoidance claims. The Employment Committee, on March 28 and May 27, 2003, filed these adversary proceedings, initially involving over three hundred defendants, seeking to avoid transfers as (1) avoidable postpetition transfers under 11 U.S.C. §§ 549 and 550; (2) voidable preferences under 11 U.S.C. §§ 547 and 550; and (3) fraudulent transfers under 11 U.S.C. §§ 544(b), 548, and 550, and applicable state law.[4] *Official Employment-Related Issues Comm. of Enron Corp. v. Lavorato (In re Enron Corp.)*, 319 B.R. 128, 130 (Bankr. S.D. Tex. 2004). "Since the filing of [this] complaint, the Enron plan of reorganization has been confirmed." *Id.* at 132 (citation omitted).

II. JURISDICTION

A proceeding to determine, avoid, or recover fraudulent conveyances or preferences constitutes a core matter over which this court has jurisdiction to enter a final judgement. 28 U.S.C. §§ 157(b)(2)(F) and (H), and 1334; *see Sherman v. FSC Realty LLC (In re Brentwood Lexford Partners, LLC)*, 292 B.R. 255, 260 (Bankr. N.D. Tex. 2003).

The foregoing and following are the court's findings of fact and conclusions of law under Bankruptcy Rule 7052. Where appropriate, a finding of fact shall be construed to be a

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[4] *I.e.*, TEX. BUS. & COMM. CODE ANN. § 24.001-.013 (Vernon 2004).

conclusion of law and vice versa.

III. PROCEDURAL HISTORY

By memorandum of decision and order signed May 24, 2004, in the Arnold adversary, this bankruptcy court, Judge Greendyke presiding, previously denied certain Defendants' motion for summary judgment, which claimed that the Employment Committee was judicially estopped to assert fraudulent conveyance claims. Additionally, in further support of Judge Greendyke's conclusion, the New York Bankruptcy Court's order of January 22, 2002, from the January 18, 2002 hearing approving the sale of Enron's wholesale trading business to UBS AG ("UBS"),[5] specifically stated:

> 34. Nothing contained in this Order, the Agreements, or any of the other Related Agreements shall be deemed to waive, release or otherwise affect the Debtors or their respective estates' rights under Chapter 5 of the Bankruptcy Code, including, without limitation, commencing any avoidance action against any party.
> 35. To the extent of any inconsistency between the provisions of the Agreements, any of the other Related Agreements and this Order, the provisions contained herein shall govern.

(Exs. 691, 692.) Generally, for the reasons stated in such opinion by Judge Greendyke, the abovesigned also finds and concludes that the Employment Committee's fraudulent conveyance claims are not barred by judicial estoppel.

By memorandum of decision and order signed April 19, 2004, in the Arnold adversary, Judge Greendyke held that all Defendants were

[5] The aforementioned sale will be referred to hereafter as the "UBS sale."

granted summary judgment, denying the Employment Committee's 11 U.S.C. § 549 postpetition claims.

By order dated November 19, 2004, in the Lavorato adversary, Judge Felsenthal denied certain Defendants' motion for summary judgment to dismiss such adversary for the Employment Committee's alleged lack of standing. *In re Enron Corp.,* 319 B.R. at 128. For the reasons stated in such opinion, the court finds and concludes that the Employment Committee has such standing to prosecute all the avoidance claims asserted herein.

By opinion dated November 23, 2004, Judge Felsenthal granted summary judgment in the Arnold adversary, holding that the transfers in question in such suit were made within ninety days before the filing of bankruptcy. *Official Employment-Related Issues Comm. of Enron Corp. v. Arnold (In re Enron Corp.)*, 318 B.R. 655, 664 (Bankr. S.D. Tex. 2004). For the reasons stated in such opinion, the abovesigned also finds and concludes that the transfers in question were made within ninety days before the filing of bankruptcy.

On June 8, 2005, the Employment Committee filed amended complaints and motions for leave to file same, which complaints included § 549 causes of action. In his Scheduling Order, Judge Felsenthal[6] ruled that the amended complaints were struck from the

[6] Judge Greendyke resigned from the bench, at which time this case was assigned to Chief Judge Steven A. Felsenthal for the Northern District of Texas. Subsequently, Judge Felsenthal resigned from the bench, at which time this case was assigned to Judge Robert C. McGuire.

record because they

> would untimely add causes of action after the discovery deadline and on the eve of trial. As a result, the defendants would be prejudiced in their preparation or the trial would be delayed. No party has requested a delay of the trial. To the extent that the plaintiff seeks to preserve positions or address defenses, the plaintiff can negotiate for the inclusion of those matters in the pretrial order[.]

(Scheduling Order ¶ P, July 13, 2005.)

The Employment Committee, on September 1, 2005, filed a motion for reconsideration of Judge Greendyke's April 19, 2004 ruling on § 549 causes of action, which was heard on September 19, 2005. The Employment Committee's motion for reconsideration is denied and found to be without merit, untimely, and dilatory.

IV. BACKGROUND

In this proceeding, Defendants are former Enron officers and employees. Defendants in the Arnold adversary (03-3522) are energy traders and marketers formerly employed by ENA (the "Arnold Defendants"). Defendants in the Lavorato adversary (03-3721) are not ENA energy traders or marketers, but instead individuals who supported the trading operation or were deemed necessary to support the Enron Debtors' operations during the bankruptcy, including employees in the areas of information technology, operations, credit, market risk, research fundamentals, human resources, accounting, and legal functions (the "Lavorato Defendants").

Both of these groups received the transfers at issue. The Arnold Defendants and the Lavorato Defendants can and will

sometimes be discussed in tandem because many of the employment contracts and agreements are similar and were executed under like circumstances. For example, as stipulated in the Pretrial Order, on or about November 29, 2001, the Arnold Defendants signed memoranda in the form of Exhibit 63, and the Lavorato Defendants signed memoranda in the form of Exhibit 28. Both memoranda were referenced as "Subject: Performance Bonuses" and were agreements.

The November 29, 2001 memoranda refer to a performance bonus provided to the recipient under the ENE bonus plan for 2001. Under the agreement, the recipient waived any other 2001 bonus. To accept the terms of the bonus, the recipient had to sign the memorandum by close of business on November 30, 2002 or the memorandum expired, and the offer contained therein was revoked. The recipient agreed to repay 125% of the performance bonus if the recipient voluntarily left the company within ninety days of receipt or if such recipient disclosed same to outsiders.

The names of the remaining defendants and the gross principal monetary claims against them are as follows:

Arnold Adversary

1. Defendants who appeared and defended: The following are the remaining defendants in the Arnold proceeding who appeared through and were represented by counsel during the trial of this matter and who have not resolved the claims against them by way of settlement:

Defendant	Bonus Amount
Robert Badeer	$1,300,000
Robert Benson	1,750,000
Craig Breslau	200,000
Mark D. Davis	1,800,000
Frank Ermis	850,000
Douglas Gilbert-Smith	275,000
Andrew Lewis	650,000
Laura Luce	250,000
Lawrence May	850,000
Bradley McKay	300,000
Matthew Motley	2,300,000
Kevin Presto	2,000,000
Kevin Ruscitti	325,000
Fletcher Sturm	1,750,000
Michael Swerzbin	2,600,000
Barry Tycholiz	650,000

2. Defendant who failed to defend: The following defendant in the Arnold proceeding failed to appear or otherwise defend himself during the trial of this matter:

Defendant	Bonus Amount
Berney Aucoin	$150,000

Lavorato Adversary

1. Defendants who appeared and defended: There are no defendants remaining in the Lavorato proceeding who have appeared through counsel or otherwise defended themselves during the trial of this matter.

2. Defendants who failed to defend: The following defendants in the Lavorato proceeding failed to appear or otherwise defend themselves during the trial of this matter:

Defendant	Bonus Amount
Sally Beck	$350,000
Michelle Bruce	45,000
Fang Tzu Chang	12,000
Tandra Coleman	9,500
Whitney Fox	50,000
Mark Frank	50,000
Paul Garcia	25,000
Anamaria Hernandez	5,000
Matthew Lenhart	18,000
Jozef Lieskovsky[7]	10,500
Kori Loibl	12,000
Peter Makkai	18,000
Omar Peck	50,000
Mikie Rath	30,000
Robert Richey	40,000
David Ryan	75,000
Shawana Simon	20,000
Stephen Stock	70,000
Karen Williams	12,000

The foregoing defendants received the foregoing gross amounts on the dates set forth hereinafter, less the amount withheld for their Internal Revenue Service ("IRS") taxes. Since Defendants effectively also received the amounts paid to the IRS for their benefits, only the gross amount will be referred to herein. *See Old Colony Trust Co. v. Comm'r*, 279 U.S. 716, 729-31 (1929).

Enron had a compensation-driven culture. Its stated compensation philosophy was "pay for performance," which meant that

[7] Jozef Lieskovsky listened to opening statements via telephone on August 2-3, 2005, but he has not appeared or otherwise defended himself during the course of the trial of this adversary proceeding. On September 21, 2005, after the evidence had been closed for all non-insolvency issues, Mr. Lieskovsky requested that he be permitted to offer evidence in support of his defenses via telephone. This request was denied as untimely. Moreover, in providing for parties to listen to opening statements via telephone, this court, acting through Judge Felsenthal, ruled that no parties would be permitted to formally appear or otherwise participate in the trial telephonically.

compensation was to rise and fall with company and individual performance. Typically, a trader's base salary constituted a small percentage of the trader's total compensation. In fact, traders received most of their compensation through year-end performance bonuses, which were paid out in cash and equity in January and February of the year following the year of performance. Enron policy demanded that corporate and individual performance be measured prior to bonus payment. Under Enron's compensation plan, these annual bonuses were entirely discretionary, and Enron reserved the right, at all times, not to pay any performance bonus in a given year. The Compensation Committee of the Enron Board had the responsibility for enforcing Enron's compensation policies.

Enron had publicly stated that its compensation was market-based, with data provided by outside compensation consultants. Enron's stated policy was to pay annual salaries at the fiftieth percentile and target total compensation at the seventy-fifth percentile, *i.e.*, as paying within the top fifty percent and seventy-five percent, respectively, of Enron's competition. Enron followed a uniform compensation and annual bonus policy in all of its subsidiaries. According to this policy, all positions received standard compensation components, and Enron created a corporate-wide bonus pool funded with approximately twenty-five to twenty-seven percent of ENE's after-tax net income.

Enron employment contracts had provisions designed to retain

officers and employees. Most Arnold Defendants, *i.e.*, traders, had employment contracts with ENA. Most of the other defendants also had employment contracts. Many of the defendants received new employment contracts in 2001.

When individual defendants are focused on hereafter, their employment contracts will be more specifically discussed. Exhibit A to Mr. Arnold's[8] ENA employment contract states in part:

> Performance Bonus: *Employee may be eligible to participate in the Enron Corp. Annual Incentive Plan ("Plan") or any appropriate replacement bonus plan of ENA.* All Performance Bonuses are discretionary and shall be paid in accordance with the terms and provisions of the Plan, a portion of which may be paid in cash and a portion of which may be paid in stock options and/or restricted stock.

(Ex. 79 at 7)(emphasis added). This Exhibit A was a typical Exhibit A to the traders' employment contracts and also other Enron employment contracts. Thus, by working at an Enron-related company such as ENA, an employee might be entitled to participate in the ENE Annual Incentive Plan or "any appropriate replacement bonus plan of ENA." The November 29, 2001 cash bonus memoranda for traders' bonuses in Enron were signed by ENA agents. *See* Ex. 63.

In the face of Enron's mounting problems[9] as year 2001

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[8] *See supra* note 1.

[9] The Employment Committee's insolvency expert, Israel Shaked, produced an accurate time-line of some of the chaos surrounding Enron from November 1, 2001 to December 2, 2001. *See* Demonstrative Ex. 740 at 79. There

progressed, Enron’s traders became concerned that they might not receive any bonuses for the year 2001.

As of October 25, 2001, many of Enron’s traders were awarded guaranteed annual 2001 calendar year performance bonuses, payable on February 15, 2002. *See, e.g.,* Exs. 80-81. For example, Mr. Arnold[10] was guaranteed a minimum $5 million 2001 bonus, payable in February 2002 (Exs. 80-81), and Mr. Swerzbin was guaranteed a 2001 calendar year bonus of $1.5 million, payable on February 15, 2002 (Ex. 90). These bonuses were contrary to Enron’s stated compensation policy because the amounts were not (1) contingent, (2) based on market surveying, or (3) negotiated. Further, the guaranteed bonuses were generally higher than the annual bonus paid for year 2000's purportedly stellar performance.[11]

The October 2001 first amendments were quickly superceded by events. On November 9, 2001, Enron announced that it would be acquired by its competitor Dynegy, Inc. (“Dynegy”), through a merger transaction that was expected to be completed in 2002. As a result of the agreed merger, Enron received a much needed $1.5 billion cash infusion from Dynegy in early November 2001.

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was credible testimony about pressured, chaotic Enron meetings taking place over the 2001 Thanksgiving holiday weekend.

[10] *See supra* note 1.

[11] Appendix 1 attached hereto is incorporated herein by reference. It is a three page chart of all Arnold proceeding October 2001 through November 2001 active defendants’ employment contracts with Enron regarding bonuses. The facts and statements contained therein are found to be accurate, true, and correct.

Enron's traders were unhappy with the prospect of a merger with Dynegy because of Dynegy's lower compensation structure and were vocal in their dissatisfaction. However, these same traders were viewed as essential to the value that Dynegy was acquiring in the merger. The merger agreement with Dynegy obligated Enron to use commercially reasonable efforts to retain them. As part of the merger agreement, Enron agreed not to increase employee compensation outside the ordinary course of business absent Dynegy's written consent. *See* Ex. 84. Enron violated this prohibition in entering into bonus contracts with Defendants.

The aforementioned events spawned the creation of the November 17 memoranda. Some Arnold Defendants who received amendments to their employment contracts in October 2001 were part of the group offered the November 17, 2001 memoranda. *See, e.g.,* Ex. 86 (guaranteeing Mr. Tycholiz a 2001 bonus payment of $325,000 on January 4, 2002, and $325,000 on February 5, 2002). These traders were required to execute a document voiding the October amendments before they could accept the terms of the November 17 memorandum. The November 17 memorandum was signed by certain trader employees at various times between November 17-26, 2001. Such November 17, 2001 memorandum required the employee to forfeit and repay all paid 2001 bonuses if the individual voluntarily left employment at Enron before February 5, 2002 or voluntarily disclosed such bonus. None of the remaining

defendants herein, who signed the November 17 memoranda, played any role in the decision to adopt or implement this bonus program.

As Enron's financial situation continued to deteriorate in 2001, Enron's traders became even more concerned that Enron would be unable to pay their 2001 guaranteed bonuses in February 2002. To reassure the traders that their expected bonuses would be paid and to assist in implementing the Dynegy merger, Enron management proposed to put guaranteed annual bonuses into a grantor trust. *See* Ex. 5. The creation of the trust was to assist in retention of personnel for the Dynegy merger or other sale of the trading unit and to avoid perceived probable delays or refusals in obtaining approval of the bonuses by the bankruptcy court if the bankruptcy of Enron became necessary.[12]

The Compensation Committee and the Enron Board of Directors approved the "special bonus plan."[13] The Compensation Committee was mislead into believing that Dynegy had approved the new bonus structure, as it was informed that Dynegy had approved the bonus plan, which was untrue.

The name of the trust was the "Performance Bonus Trust" (the "Trust"). *See id.* § 1.01. ENA was grantor of the Trust.

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[12] At this juncture, the bankruptcy of Enron was a distinct, realistic, and probable scenario.

[13] The Enron Board of Directors approved the Trust on November 18, 2001.

See id. The Trustee was Wachovia Bank, N.A. ("Wachovia"). The Trust account was opened with Wachovia on November 16, 2001 (Ex. 2) and signed by Wachovia on November 19 or 20, 2001 (Smith Dep. at 66:13-21, July 30, 2003). Wachovia was a conduit for defendant recipients of Trust checks.

Exhibit 6 credibly shows the Trust was funded with $50 million by ENE on November 20, 2001. *See* Ex. 6; Smith Dep. at 31:1-8, 66:10-12, 118:6-16, July 30, 2003. Seven months later in July 2002, substantially postpetition, intercompany Enron emails from confused Enron personnel (Ex. 225) purport to show that the $50 million was wired to Wachovia Bank by ENE, but internally at Enron charged to an ENA cost center. The credible evidence is that the Trust was funded initially by ENE prepetition. Regardless of whether the payment came from ENE or ENA, the Employment Committee was assigned these avoidance causes of action and authorized to prosecute all these causes of action on behalf of the Enron debtors' estates.

On Wednesday, November 28, 2001, Dynegy made public its withdrawal from its merger with Enron. That same day, credit agencies downgraded Enron's credit rating to junk status.

Judge Greendyke, in his April 19, 2004 opinion, found that Wachovia received the beneficiary designations of the Trust on November 29, 2001, as Smith, from Wachovia, also testified. *See* Ex. 18; Smith Dep. at 68-70, July 30, 2003. Judge Greendyke's

April 19, 2004 opinion specifically states:

> Defendants contend that, according to the terms of the Trust Agreement, an irrevocable transfer of property from Enron to the Trust was completed as of November 29, 2001, when Enron provided the payment schedule ("Appendix B") to Wachovia identifying each individual bonus recipient and their corresponding payment amount. Defendants argue that from that point on, the beneficiaries were the "beneficial owners of the Trust . . . subject to the terms and provisions of this Trust Agreement, the Program and the Agreements. (Trust Agreement § 3.01)
>
> The term "Beneficiaries" is defined in the Trust Agreement as "the Key Employees named in Appendix B annexed hereto, as amended from time to time." (Trust Agreement § 1.03(b)) Appendix B had not been finalized when the Trust was established (on or about November 16, 2001), but instead was provided to Wachovia on November 29, 2001. (Deposition Transcript of John N. Smith, III, pp. 68-70) The Court notes that the Trust Agreement expressly prohibited any amendment to the Trust "that would have the effect of reducing the beneficial interest of any Beneficiary at any time." (Trust Agreement § 12.01(a)) Additionally, Appendix A to the Trust Agreement provided that "[i]n no event may a Payment Schedule be modified to eliminate a Beneficiary or to change the amount of, or postpone, a Payment for any Beneficiary." (Appendix A § 4) Consequently, when the Trust was funded and the beneficiaries and payments identified through delivery of Appendix B, there was no going back.
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> As of that date, Enron had no ability to access the Trust assets earmarked for the beneficiaries, eliminate a beneficiary, reduce the amount payable to a beneficiary, or delay any payment to a beneficiary. Under the Trust Agreement, the only interest retained by Enron was a residual interest in any trust assets remaining after all obligations of the Trust to the employees, taxing authorities, and Wachovia as trustee had been satisfied. (Trust Agreement § 5.03(b)) Accordingly, this Court finds that, as of November 29, 2001, the transfer from Enron to the Trust and its beneficiaries was complete, and all conditions precedent for payment of the Trust funds to Defendants were satisfied.

Judge William Greendyke, April 19, 2004 Memorandum of Decision and Order, *see also Ebert v. Dailey Directional Servs. (In re Gibraltar Res., Inc.)*, 202 B.R. 586, 588-89 (N.D. Tex. 1996) ("When a debtor makes an absolute assignment to a creditor, of money that the debtor is entitled to receive from a third party, a transfer is perfected and complete when the assignment is executed rather than when the money is disbursed to the creditor.")(citations omitted). At this juncture, Enron key employees and the Enron Board of Directors knew Enron was going to immediately file for bankruptcy. Such designations would complete its paperwork necessary to consummate the completion of the transfers of the bonuses to Arnold Defendants and thereby Enron would avoid perceived probable delays or refusals in obtaining bankruptcy court approval of such bonuses. Checks from the Trust to the Arnold Defendants were dated November 30, 2001. *See* Ex. 8.

On November 29 and 30, 2001, the Arnold Defendants executed the November 29, 2001 Performance Bonus Memoranda guaranteeing them the new, higher performance bonuses. *See, e.g.*, Ex. 91. To accept the new performance bonuses, all of the Arnold Defendants had to sign "Performance Bonus" memoranda. The parties stipulated that "[t]he Defendants signed memoranda, dated November 29, 2001, in the basic forms of Exhibit 63 (for the Arnold Defendants) and Exhibit 28 (for the Lavorato Defendants)

before and as a condition of receiving the above payments." (Pretrial Order at 9, B(3))(emphasis added). The payments are the stipulated gross amounts in the pretrial order each defendant received, also shown *supra*, which are the same amounts as sued for herein.

There was much interdependence between ENE and ENA. At all relevant times, ENE filed consolidated financial statements for itself and its subsidiaries, including ENA. Exhibit 63 is signed by ENA awarding a 2001 cash bonus under the ENE bonus plan. Exhibit 28 is signed by ENE awarding a 2001 cash bonus under same.

The use of the term "performance bonus" was intentional in the November 29, 2001 memoranda and where used elsewhere. Early drafts of the "Performance Bonus" memos used the term "retention bonus." Enron management intentionally substituted the term "performance bonus" for the "retention bonus" whenever that term appeared in the original draft. Enron also intentionally used the term "performance bonus" in the Performance Bonus Trust with Wachovia. That the performance bonuses may have been paid, in part, to retain employees does not alter their character as performance bonuses for the year 2001.

The bonuses paid out of the Trust per the November 29, 2001 memoranda were substantially greater than the October guarantees. Defendants were to receive the following in cash:

Swerzbin, $2.6 million, 173.33% of his October guaranty;
Motley, $2.3 million, 176.92% of his October guaranty;
Presto, $2 million, 166.67% of his guaranty;
Davis, $1.8 million, 180% of his October guaranty;
Benson, $1.75 million, 175% of his October guaranty;
Sturm, $1.75 million, 145.83% of his October guaranty;
Badeer, $1.3 million, 216.67% of his October guaranty;
Ermis, $850,000, 170% of his October guaranty;
May, $850,000, 242.86% of his October guaranty;
Lewis, $650,000, 162.5% of his October guaranty;
Tycholiz, $650,000, 185.71% of his October guaranty;
Ruscitti, $325,000 (no October guarantee);
B. McKay, $300,000 (no October guarantee);
Gilbert-Smith, $275,000 (no October guarantee);
Luce, $250,000 (no October guarantee); and
Breslau, $200,000 (no October guarantee).

Concurrently with the events, a special meeting of the Enron Board of Directors was held on November 28, 2001, to implement a similar retention plan with respect to other critical personnel. *See* Ex. 60. At that meeting, the Chairman of Enron's Compensation Committee presented a recommendation to establish an ENE bonus plan for the "purposes of retaining key people given the uncertainty surrounding the Company's business and the need to maximize the value of the Company." (Ex. 60 at 5.) Enron identified 528 non-trader employees for these retention payments, scaled down from 1,350 previously considered. This group included the employees named in the Lavorato action who supported the trading business in the areas of information technology, operations, credit, market risk, research fundamentals, human resources, accounting, and legal functions.

To avoid the possible delays or refusals in obtaining bankruptcy approval of the bonuses and possible loss of employees

occasioned by its imminent bankruptcy, which was known to the Enron Board, the Board decided to prepay annual 2001 bonuses to such group of employees, including the Lavorato Defendants.

The Lavorato Defendants executed November 29, 2001 Performance Bonus Memoranda calling for immediate payment of performance bonuses for their 2001 performance. To receive the early bonus payments, such defendants had to promise to stay ninety days, to keep the bonuses confidential, and to repay 125% of same if they voluntarily left the company within ninety days of receipt of the bonus. The bonus payments were made after the Lavorato Defendants signed the November 29, 2001 Performance Bonus Memoranda. Payments to the Lavorato Defendants were made by cashier's checks and delivered prepetition.[14]

Enron's management went to extraordinary lengths to try to deliver the bonuses prepetition. Enron employees delivered checks by plane in order to avoid the effect of the bankruptcy filing. Defendants were given only one day to accept the terms of the agreement, and the bonuses were paid immediately thereafter. The Arnold Defendants were paid with bank Trust checks, which cleared postpetition.

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[14] Mr. Goldstein, Defendant's expert, testified that there were approximately 20,000 employees in the Trading Group and approximately three percent received bonuses totaling $104 million. The bonuses were paid out of two programs: $50 million through the Trust and $54 million through non-Trust payments.

V. ADDITIONAL BACKGROUND AND FINDINGS ON SOME DEFENDANTS WHO ACTIVELY PARTICIPATED IN THE TRIAL

Significant data regarding Defendants who actively participated in the trial is set forth in Appendix 1 hereto in abbreviated form to flesh out some of the typical fact scenarios and chronology. It appears that the following additional background is helpful.

A. Michael Swerzbin

The Plaintiff's claim against Mr. Swerzbin is for a $2.6 million gross cash bonus paid to Mr. Swerzbin by reason of his November 29, 2001 memorandum with ENA. He was a vice president of ENA at the time. Mr. Swerzbin began his career at Enron in 1997, after having spent eight years with Portland General Electric Company ("PGE") before it was acquired by Enron. Mr. Swerzbin became a power trader for PGE in 1995 and was among a small group of PGE traders who Enron retained following its acquisition of that company. He worked as a long-term trader of electric power for the northwestern United States. In particular, he worked on Enron's West Power Trading Desk located in Portland, Oregon. He was a market-maker.

According to Enron's records, Mr. Swerzbin was one of Enron's most successful traders on a cumulative basis, if not the most successful, generating significant profits during January 1, 2000, through October 30, 2001, and prior thereto. As set forth herein, the court has found the accuracy of Enron's records

questionable. However, many of the employees discussed herein and their immediate superiors regarded the records they dealt with as accurate because of their input in the records regarding their performance and the performance of those they supervised. Significant parts of Enron's profit and loss figures related to future liquidations, which by their nature were speculative.

Mr. Swerzbin received high evaluations from his superiors during his Enron tenure. In August 2001, he signed a three year employment contract with ENA in the form of Exhibit 600U, which contained a non-compete covenant, with a base salary of $200,000 on an annualized basis. At such time, he received a signing bonus of *$300,000* in cash and a half million in stock options and a half million in restricted stock. He negotiated the $300,000 cash signing bonus. This $1.3 million is not part of Plaintiff's claims in this suit. Exhibit 600U was in effect at the filing date. Postbankruptcy, Mr. Swerzbin stayed with Enron until February 2002 when he went to work for UBS as part of the UBS sale.

For year 2000, he received a performance bonus of $4 million payable in February 2001, consisting of $2 million in cash and $2 million split between stock options and restructured stock (hereinafter called equity). Because of Enron's continuing 2001 financial deterioration, Mr. Swerzbin and similarly situated Enron employees never realized any money from the year 2000 stock

bonuses.

On October 20, 2001, ENA and Mr. Swerzbin signed a "First Amendment to Employment Agreement" ("First Amendment" agreement). *See* Ex. 601R (identical to Ex. 90). Under such amendment, ENA agreed to pay him a 2001 calendar year bonus of a minimum cash bonus of $1.5 million on or before February 15, 2002, provided that he was still employed by ENA on such date. His October 25, 2001 agreement was typical of October 2001 agreements referred to in Appendix 1 hereto.

On November 17, 2001, Mr. Swerzbin signed another performance bonus memorandum with ENA (Ex. 603Q), replacing the October 2001 agreement. Under the November 17, 2001 agreement, ENA agreed to pay him the following bonus for calendar year 2001 performance: $1.3 million on January 4, 2002, and $1.3 million on February 5, 2002, provided he was with ENA or an affiliate on the dates the bonus was payable.[15] He agreed to forfeit and repay any such bonus in the event he voluntarily terminated his employment with ENA prior to February 5, 2002. This was typical of other November 17, 2001 memoranda referred to in Appendix 1 hereto.

On November 19, 2001, ENA and Mr. Swerzbin signed a document entitled "Termination of First Amendment to Employment Agreement" (Ex. 602P), whereby the parties agreed that the November 17, 2001

[15] The format of the November 17, 2001 contracts referred to herein was the same, although the bonus amounts were different.

agreement (Ex. 603Q) took the place of the October 25, 2001 "First Amendment" agreement (Ex. 601R).

Thereafter, on November 30, 2001, ENA and Mr. Swerzbin signed the November 29, 2001 Performance Bonus Memorandum (Ex. 604X), agreeing to a $2.6 million gross bonus. He received the check after he signed the memorandum. Under such memorandum, Mr. Swerzbin agreed to stay at Enron ninety days or else pay back a 125% penalty. There were no negotiations over the amount of his bonus, and he was not involved in fixing the bonus amounts for himself or others.[16]

During the ninety days following November 29, 2001, Mr. Swerzbin assisted Enron in its efforts to market the trading business by counseling prospective purchasers on their due diligence. He also assisted Enron in settling various contracts. He then went to work for UBS.

At UBS, his base salary was $200,000. He received a $900,000 cash bonus, payable in equal installments at six month and one year anniversaries, and $900,000 in restricted stock as a signing bonus and eligibility for year-end bonus at ten percent of earnings before interest and taxes. He lost $1 million as a trader at UBS in 2002 and received no bonus. *See* Demonstrative

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[16] There was no showing that any of the remaining defendants negotiated the amount of their November 29, 2001 bonuses. It was always a take it or leave it proposition, although because of the "generous" amounts and short employment requirement, "leave it" was not in all likelihood a realistic possibility.

Ex. 726[17] and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting various additional statistics and contracts of Mr. Swerzbin).

B. Matthew Motley

Plaintiff's claim against Mr. Motley is for a $2.3 million gross cash bonus received by reason of his November 29, 2001 memorandum. Mr. Motley's title was Director West Power at ENA. *See* Exs. 126A, 909J. As Director West Power at ENA, Mr. Motley was responsible for managing ENA's long-term southwest electricity portfolio. This included, but was not limited to, pricing deals, proprietary trading, maintaining constant markets on Enron's electronic trading platform, and managing ENA's long-term, fixed-price power exposure in the southwest and Rocky Mountain regions. *See* Exs. 619, 909J.

Mr. Motley received consistently positive performance review while at ENA during 2000 and 2001. Mr. Motley's profit and loss for the first nine months of 2001 was $171 million with Enron. In February 2001, Mr. Motley received his bonus for 2000 as follows: $800,000, consisting of fifty percent cash and fifty percent stock.

On October 26, 2001, Mr. Motley and ENA signed the "First Amendment to Employment Agreement," under which he was to be paid

[17] An objection was sustained to the Sempra Energy references in Demonstrative Exhibit 726.

for a calendar year 2001 bonus *$1,300,000* on or before February 15, 2002. *See* Ex. 601N.

Mr. Motley has never seen a copy of the November 17, 2001 memorandum containing his own signature nor did Plaintiff offer such an exhibit into evidence at trial.

The amount of payment that Mr. Motley received on or about November 29, 2001 per his November 29, 2001 Performance Bonus Memorandum with ENA was $2.3 million gross. *See* Demonstrative Ex. 724 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. Motley).

In March 2002, Mr. Motley received various job offers. Sempra Energy specifically offered Mr. Motley a position with a base salary of $200,000, a signing bonus of $500,000 due half at signing and half at one year anniversary, and performance bonuses equal to ten percent of net income at December 31, 2002. Mr. Motley accepted this position after leaving Enron.

C. Kevin M. Presto

The claim against Mr. Presto is for a gross cash bonus of $2 million paid to him by reason of his November 29, 2001 memorandum. In September 1994, Mr. Presto began his employment in Enron's associate program, a multi-year extensive training program. During his approximately eight year tenure at Enron, Mr. Presto received various promotions and advancements.

According to Enron's records, Mr. Presto had a high individual profit and loss for the years 1999-2001, and he likewise supervised groups with a high profit and loss. In the years in which he went through the formal employee review process, he received either a one or two rating, the highest available.

In 2001, Mr. Presto's title was Vice President, East Power Trading in the Enron Trading Group, which was part of ENA. He held that title at the time he and the Trading Group were sold to UBS. Mr. Presto's compensation for the year prior to bankruptcy included a gross base salary of $150,000 and a gross bonus of $500,000 cash and $500,000 equity paid in February 2001.

He had an October 2001 first amendment to his employment contract, providing for a February 15, 2001 bonus of $1.2 million and a replacement contract on November 17, 2001, providing for a $1 million bonus to be paid on January 4, 2002 and a $1 million bonus to be paid on February 5, 2002. *See* Demonstrative Ex. 731 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting various additional statistics and contracts of Mr. Presto). Mr. Presto signed a November 29, 2001 memorandum for $2.3 million. He stayed with Enron during the ninety day period, helping with due diligence on the UBS sale and left ENA for UBS as part of the UBS sale.

D. Mark Davis

Plaintiff's claim against Mr. Davis is for a gross cash bonus of $1.8 million paid to him per his November 29, 2001 memorandum. Mr. Davis began his employment at Enron in September 1996 in Enron's professional development program. He soon joined the Trading Group and remained in the Trading Group for the remainder of his tenure at Enron.

During his approximate six years at Enron, Mr. Davis received various promotions and advancements. According to Enron records, Mr. Davis' individual profit and loss for the years 1999, 2000, and 2001 went up considerably each year. In addition, the group he supervised on the Northeast Power Desk purportedly had a high profit and loss in 2001. In the years in which Mr. Davis went through the formal review process, he received either a one or two ranking, the highest available.

In 2001, Mr. Davis was in charge of the Northeast Power Desk. He held that position at the time of the UBS sale. Mr. Davis' compensation for the year prior to bankruptcy consisted of $925,000, which broke down into a gross base salary of approximately $125,000 and a bonus of one half cash and one half stock totaling $800,000, paid in February 2001. His 2001 gross base salary was approximately $150,000.

As noted in Appendix 1 hereto, he had both October 2001 and November 2001 memorandum contracts with ENA. *See* Demonstrative

Ex. 723 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting various additional statistics and contracts of Mr. Davis).

Mr. Davis stayed with the Trading Group after November 29, 2001. He provided leadership, assisted with the sale and due diligence process, which included meeting with various due diligence parties, and assisted with the transition from ENA to UBS. He left ENA as part of the Trading Group that went to UBS.

E. Robert Benson

The claim against Mr. Benson is for a gross cash bonus of $1.75 million, paid to him per his November 29, 2001 memorandum. Mr. Benson began his employment at Enron in May 1996 in Canada. In 2001, Mr. Benson's title was Director, East Power Trading in the Enron Trading Group, which was part of ENA. He held that title at the time of the UBS sale.

During his six year tenure at Enron, Mr. Benson received various promotions and advancements. In the years in which he went through the formal employee review process, Mr. Benson received either a one or two ranking, the highest possible.

Mr. Benson' year 2000 compensation was $300,000, consisting of a gross base salary of $100,000 and a bonus of $150,000 cash and $50,000 of stock. His 2001 gross base salary was $115,000. According to Enron's records, Mr. Benson had a high profit and loss from 1999-2000, and a profit and loss of $108 million for the first nine months of 2001.

Mr. Benson stayed with the Trading Group after November 29, 2001. He assisted with the sale and due diligence process as well as the transition of the Trading Group from ENA to UBS. Mr. Benson left ENA as part of the group that went to UBS and he remains there employed.

Mr. Benson had October 2001, November 17, 2001, and November 29, 2001 bonus agreements with Enron. *See* Demonstrative Ex. 728 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting various additional statistics and contracts of Mr. Benson).

F. Fletcher Sturm

The claim against Mr. Sturm is for a gross cash bonus paid to him per his November 29, 2001 memorandum of $1,750,000. Mr. Sturm began his employment at Enron in October 1996 as a trader. In 2001, Mr. Sturm was Vice President Energy Trading and managed the Midwest Power Trading Desk. He held that position at the time he went to UBS as part of the UBS sale.

During his six year tenure at Enron, Mr. Sturm received various promotions and advancements. In the years in which he went through the formal employee review process, Mr. Sturm received either a one or two rating, the highest possible.

Mr. Sturm's individual profit and loss for the years 1999, 2000, and 2001, according to Enron's records, was very high. For the year 2000, he received a bonus of $1 million in cash and $1

million in equity for a total of $2 million. For 2001, his gross base salary was approximately $170,000.

Per Appendix 1 hereto Mr. Sturm had October 2001 and November 2001 bonus agreements with Enron. Per his November 29, 2001 memorandum, Mr. Sturm received a bonus in the gross amount of $1.75 million after such date. *See* Demonstrative Ex. 730 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting various additional statistics and contracts of Mr. Sturm).

Mr. Sturm stayed with the Trading Group after November 29, 2001, providing leadership and assisting with the UBS sale and due diligence process.

G. Robert Badeer

The claim against Mr. Badeer is for a gross cash bonus of $1.3 million paid to him by reason of his November 29, 2001 memorandum. Mr. Badeer signed an October 25 memorandum for $600,000 and a November 17, 2001 memorandum (Ex. 603B) and termination of October 25, 2001 memorandum for $1.3 million (Ex. 307). His year 2000 bonus was $170,000, consisting of $120,000 cash and $50,000 equity paid to him in February 2001. *See* Demonstrative Ex. 729 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. Badeer).

H. Frank Ermis

The claim against Mr. Ermis is for an $850,000 gross cash bonus paid to him per his November 29, 2001 memorandum. His year 2000 bonus was $400,000, consisting of one half cash and one half equity, paid to him in February 2001. He had an October 25, 2001 memorandum for $500,000 (Ex. 601H) and a November 17, 2001 memorandum for $850,000 (Ex. 603H). *See* Demonstrative Ex. 732 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. Ermis).

I. Lawrence J. May

The claim against Mr. May is for an $850,000 gross cash bonus paid to him per his November 29, 2001 memorandum. He received a $400,000 year 2000 bonus, consisting of $200,000 cash and $200,000 equity, in February 2001. He had both October 2001 and November 2001 contracts. *See* Demonstrative Ex. 733 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. May).

J. Andrew Lewis

The claim against Mr. Lewis is for a $650,000 gross cash bonus paid to him per his November 29, 2001 memorandum. His 2000 bonus, which was paid in February 2001, was $400,000, comprised of $200,000 cash and the remainder in equity. He had an October 2001 contract for $400,000 and a November 17, 2001 replacement contract for $650,000. *See* Demonstrative Ex. 725 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting

additional statistics and contracts of Mr. Lewis).

K. Barry Tycholiz

The claim against Mr. Tycholiz is for a $650,000 cash bonus paid to him per his November 29, 2001 memorandum. For year 2000, he received a $325,000 bonus in February 2001, $175,000 of which was cash and $150,000 of which was stock. He had an October 25, 2001 contract for $350,000 and a November 17, 2001 replacement contract for $650,000. *See* Demonstrative Ex. 727 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. Tycholiz).

L. Kevin Ruscitti

The claim against Mr. Ruscitti is for a cash bonus per his November 29, 2001 agreement (Ex. 919A), for the gross amount of $325,000. Mr. Ruscitti thought he signed a November 17, 2001 memorandum, but could not find it. Plaintiff stated in its trial brief that: "Ruscitti apparently did not have an employment contract." (Pl's. Trial Br. at 35.) This statement could refer to a standard employment contract. *See* Ex. 919A (referring to his November 17, 2001 agreement and signed by Mr. Ruscitti). It appears that in all likelihood Mr. Ruscitti signed a November 17, 2001 agreement, but not a standard Enron employment contract. Plaintiff did not produce a November 17, 2001 memorandum signed by Mr. Ruscitti.

Mr. Ruscitti's year 2000 bonus paid to him in February 2001

was $125,000, of which $100,000 was cash and the remainder equity. *See* Demonstrative Ex. 734 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. Ruscitti).

M. Bradley McKay

Plaintiff's claim against Mr. McKay is for a $300,000 cash bonus paid to him per his November 29, 2001 memorandum. He received a $200,000 cash bonus in February 2001 for a year 2000 bonus. His year 2000 bonus included no equity. *See* Demonstrative Ex. 735 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. McKay).

N. Douglas Gilbert-Smith

The claim against Mr. Gilbert-Smith is for a $275,000 gross cash bonus paid to him per his November 29, 2001 memorandum. *See* Demonstrative Ex. 736 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. Gilbert-Smith).

At trial he was presented with a copy of the November 17, 2001 memorandum signed by ENA (Ex. 513), but not signed by him. He testified that he received and reviewed this document, but never signed it. In his answer to requests for admissions, he admitted signing the November 17, 2001 memorandum. His November 29, 2001 memorandum (Ex. 916E), stated in part: "This memorandum

replaces and supercedes the November 17, 2001 Performance Bonus Memorandum to you."[18]

While Mr. Gilbert-Smith never asked leave of court to withdraw his answer to the request for admission per Bankruptcy Rule 7036, he credibly testified, without objection, that he did not sign the November 17, 2001 memorandum because he was on vacation when it came, and he did not want to jeopardize his ability to leave Enron. For purposes of antecedent debt analysis, Exhibit 513, signed by ENA, would be sufficient by itself to constitute an antecedent debt. *See* 11 U.S.C. § 547(b)(2).

In any event, as previously pointed out, the court has found that the November 29, 2001 bonus agreements constitute liquidation of antecedent debt for § 547(b)(2) purposes.

O. Laura L. Luce

The claim against Ms. Luce is for a $250,000 gross cash bonus paid to her per her November 29, 2001 memorandum. She received a year 2000 bonus of $180,000 cash. She received no equity as part of her year 2000 bonus. *See* Demonstrative Ex. 738 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Ms. Luce).

[18] All of the November 29, 2001 memoranda stated such.

P. Craig Breslau

The claim against Mr. Breslau is for $200,000 paid to him per his November 29, 2001 memorandum. He received a year 2000 bonus in February 2001 of which $165,000 was cash and $35,000 was equity. *See* Demonstrative Ex. 737 and exhibits referred to therein; *see also* Appendix 1 hereto (highlighting additional statistics and contracts of Mr. Breslau).

Q. Remaining Active Defendants Generally

None of the remaining defendants who actively participated in this trial received any money from the equity they received from Enron in February 2001 for part of their year 2000 performance bonus. Plaintiff is making no claim against the defendants for the year 2000 bonuses they received. There was no showing that any of the defendants had any input into the amount of the November 29, 2001 bonus they received.

Furthermore, none of the remaining individual defendants are being prosecuted by any governmental entity for any misdeeds or any omissions in connection with their Enron employment. There was no testimony that any of the remaining defendants committed any intentional misdeeds in connection with their Enron employment.

R. Remaining Active Defendants: Antecedent Debt

To the extent that a defendant received an October 2001 or November 17, 2001 memorandum, it appears that either would

constitute an antecedent debt under 11 U.S.C. § 547(b)(2) to the extent same constituted a portion or the whole of the defendant's November 29, 2001 Performance Bonus Memorandum amount. In any event, the court is of the opinion, previously expressed, that the November 29, 2001 agreements by themselves establish an antecedent debt under § 547(b)(2).

VI. PREFERENCES

11 U.S.C. § 547(b)[19] states:

> (b) Except as provided in subsection (c) of this section, the trustee may avoid any transfer of an interest of the debtor in property--
> (1) to or for the benefit of a creditor;
> (2) for or on account of an antecedent debt owed by the debtor before such transfer was made;
> (3) made while the debtor was insolvent;
> (4) made--
> (A) on or within 90 days before the date of the filing of the petition; or
> (B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and
> (5) that enables such creditor to receive more than such creditor would receive if--
> (A) the case were a case under chapter 7 of this title;
> (B) the transfer had not been made; and
> (C) such creditor received payment of such debt to the extent provided by the provisions of this title.

Under 11 U.S.C. § 547(g), the trustee has the burden of proving avoidability under § 547(b), and the defendant has the burden of proving non-avoidability of a transfer under § 547(c).

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[19] The amendments made to 11 U.S.C. § 547, under the the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA"), apply to any case that is pending or commenced on or after October 17, 2005.

A. Transfer of an Interest of the Debtor in Property; To or For the Benefit of a Creditor; Made Within Ninety Days of Bankruptcy

As previously indicated *supra*, Judge Felsenthal granted a summary judgment holding that the Arnold proceeding transfers were made prepetition. *See Official Employment-Related Issues Comm. of Enron Corp. v. Arnold (In re Enron Corp.)*, 318 B.R. 655, 663-64 (Bankr. S.D. Tex. 2004).

With respect to the Lavorato Defendants, it is undisputed that they received their payments by cashier's checks from Enron, delivered to them prepetition.

B. Antecedent Debt and Whether the Defendants Were Creditors

Prior to November 29, 2001, most Arnold Defendants had October and/or November 2001 guarantees of 2001 bonuses payable in 2002. *See* Appendix 1 hereto. The Lavorato Defendants had no October 2001 or November 2001 guarantees. For purposes of 11 U.S.C. § 547(b)(2), antecedent debt, where a trader had an October 2001 or November 17, 2001 full or partial guaranty of the bonus received on such trader's November 29, 2001 memorandum, such November 29, 2001 payment would clearly be based on an antecedent debt to the extent of the October 2001 or November 17, 2001 guarantee. *See* 11 U.S.C. § 547(b)(1)-(2).

A debt is antecedent if it is incurred before the transfer. *Southmark Corp. v. Schulte Roth & Zabel (In re Southmark Corp.)*, 88 F.3d 311, 316 (5th Cir. 1996). Prior to November 29, 2001, the following remaining Arnold Defendants had pre-existing

October or November 17, 2001 guarantees of at least a portion of their November 29, 2001 bonus payments. In the following discussion, the court will additionally discuss any unique facts with respect to certain individual Arnold Defendants:

Name	10/2001 Guarantee Amount	11/17/2001 Guarantee Amount	11/29/2001 Guarantee Amount
Swerzbin	$1,500,000	$2,600,000	$2,600,000
Motley	1,300,000		2,300,000
Presto	1,200,000	2,000,000	2,000,000
Davis	1,000,000	1,800,000	1,800,000
Benson	1,000,000	1,750,000	1,750,000
Sturm	1,200,000	1,750,000	1,750,000
Badeer	600,000	1,300,000	1,300,000
Ermis	500,000	850,000	850,000
May	350,000	850,000	850,000
Lewis	400,000	650,000	650,000
Tycholiz	350,000	650,000	650,000
Ruscitti[20]			325,000
McKay			300,000
Gilbert-Smith		275,000[21]	275,000
Luce			250,000
Breslau			200,000

In his May 24, 2004 opinion in the Arnold adversary, Judge Greendyke opined:

> Initially, the Court notes that this case is distinguishable in a significant way from the Fifth Circuit's *Southmark v. Marley* decision. *See generally In re Southmark*, 62 F.3d 104 (5th [sic] Cir. 1995). In *Southmark v. Marley*, it was the debtor who controlled the event upon which payment was conditioned. *Id.* As discussed above, it was only when the debtor terminated the employment contract with its employee that it

20 *See* Appendix 1 hereto.

21 Signed only by the debtor. *See* Ex. 518 and Demonstrative Ex. 736. To the extent that any November 17, 2001 agreement was deemed necessary to the determination of an antecedent debt, it appears that this November 17, 2001 contract signed by the debtor would fulfill any such requirement.

> incurred the obligation to pay severance. *Id*. Here, the operative language in the November 17 Performance Bonus Memorandum is: "I am pleased to inform you that *you shall receive* the following cash Performance Bonus amounts *... provided you are employed* with [Enron] on the Date Payable." This language indicated that from the moment the November 17 contracts were formed, Defendants' interests in their bonus payments were vested, and Enron's obligation to pay was real. No action on Enron's part could have altered that obligation. Only if Defendants had chosen to voluntarily leave before the Date Payable would their interests have divested.
>
> . . . .
>
> Based on the preceding determinations, the Court concludes that for purposes of § 547(b)(2), Enron's obligation to pay performance bonuses to each defendant in two equal installments in January and February, 2002 was *incurred* as of November 17, 2001--*before* the date of the transfers in question.

Judge William Greendyke, May 24, 2004 Memorandum of Decision and Order.

As indicated *supra*, prior to November 29, 2001, most of the Arnold Defendants had October 2001 or November 2001 guarantees of at least some of their 2001 bonuses. The Lavorato Defendants did not have such October 2001 or November 17, 2001 bonus guarantees from Enron.

C. Whether Payments of the November 29, 2001 Bonuses to the Lavorato Defendants and to the Arnold Defendants (Without October and/or November 2001 Guarantees) Constituted Payment on an Antecedent Debt

In *Baker Hughes Oilfield Operation, Inc. v. Cage (In re Ramba, Inc.)*, 416 F.3d 394, 398-99 (5th Cir. 2005), the court stated:

> First, we inquire as to whether the transfer in this case was made in payment of an antecedent debt. We begin, as always, with the text of the statute. The Bankruptcy Code defines a "debt" as a "liability on a claim". 11 U.S.C. § 101(12). A "claim", in turn, is defined broadly as the "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured". 11 U.S.C. § 101(5). A debt is "antecedent" for purposes of § 547(b) if it was incurred before the alleged preferential transfer. *See Southmark Corp. v. Schulte Roth & Zabel*, 88 F.3d 311, 316 (5th Cir. 1996).

As previously pointed out in the Pretrial Order Statement of Stipulated Facts, Defendants stipulated:

> (2) Enron Corp. made the payments to the Defendants in the Lavorato proceeding.
>
> (3) The Defendants signed memoranda, dated November 29, 2001, in the basic forms of Exhibit 63 (for the Arnold Defendants) and Exhibit 28 (for the Lavorato Defendants) before and as a condition of receiving the above payments.
>
> (4) Exhibit A sets forth the amounts of the checks(that were delivered pursuant to a [sic] the November 29, 2001 memorandum) and related tax payments.

(Pretrial Order at 9, ¶ B(2)-(4).) Per Exhibit A to the Pretrial Order, the foregoing November 29, 2001 transfers were acknowledged by the active Arnold and Lavorato Defendants remaining herein.

Defendants argue, at the very least, that *Southmark Corp. v. Marley (In re Southmark Corp.)*, 62 F.3d 104 (5th Cir. 1995), controls Plaintiff's cases against the Arnold Defendants without October or November 2001 written memoranda (and presumably

therefore Plaintiff’s claims against the Lavorato Defendants who only signed November 29, 2001 memoranda). In *Marley*, the Fifth Circuit held that the prepetition payment to company employees was on account of a "simultaneous debt" and therefore not an antecedent debt under 11 U.S.C. § 547. *Id.* at 106-07.

In the present fact scenario under discussion, Enron’s debt was incurred by the November 29, 2001 memoranda and in some instances additionally by October 2001 and November 17, 2001 memoranda. Such November 29, 2001 memorandum, by itself, was a liquidation of an otherwise previously discretionary 2001 performance bonus for *past* performance in 2001.

Except for *Marley*, it would appear appropriate to only test such payments under the contemporaneous exchange for new value § 547(c)(1)(A) analysis rather than a "simultaneous" debt defense, which is not mentioned as a defense under 11 U.S.C. § 547.[22]

To complete the record, as discussed hereafter, the court finds that the contemporaneous exchange for new value defense of § 547(c)(1)(A) and (B) would not be available to such Defendants for the reasons stated.

Per the Pretrial Order, Defendants signed the November 29,

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[22] For cases discussing § 547(c) by its listing of defenses as possibly limiting preference defenses to what is listed, see *KMart Corp. v. Uniden America Corp. (In re KMart)*, 2004 WL 2222265 (N.D. Ill. Oct. 1, 2004) and *Gonzales v. ConAgra Foods, Inc. (In re Furrs)*, 294 B.R. 763 (Bankr. D.N.M. 2003); see also *In re Ramba, Inc.*, 416 F.3d at 399-400. *Contra Philip Servs. Corp. v. Luntz (In re Philip Servs.* (*Del.*), *Inc.)*, 267 B.R. 62 (Bankr. D. Del. 2001).

2001 memoranda before and as a condition of receiving the bonus payments. If Enron had not paid such amounts, Defendants would have had a prepetition claim against Enron. Defendants' respective interests in the bonuses were vested at least on November 29, 2001. No action on Enron's part could have altered the obligation. Only if Defendants left before ninety days would the clawback of their bonus have gone into effect. As Judge Greendyke pointed out in his May 24, 2004 opinion quoted *supra,* specifically where he referenced the November 17, 2001 agreements, in *Marley* it was the debtor who controlled the event upon which payment was occasioned, *i.e.,* severance. However, in this case, once the debtor signed the November 29, 2001 contracts, the bonus was vested subject to defeasement and clawback only if the employee left within ninety days.

D. That Enables Such Creditor to Receive More Than Such Creditor Would Receive in Chapter 7

Enron's Disclosure Statement (Exhibit 406 at 33), shows that unsecured ENE creditors would receive 17.4% of their claims in chapter 7, and ENA's creditors would receive 20.1% of their claims.

E. Made While the Debtor Was Insolvent Under 11 U.S.C. § 547(b)(3)[23]

F. Contemporaneous Exchange for New Value Given to Debtor

11 U.S.C. 547(c) states:

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[23] This will be discussed *infra*.

(c) The trustee may not avoid under this section a transfer--

(1) to the extent that such transfer was--

(A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and

(B) in fact a substantially contemporaneous exchange;

(2) to the extent that such transfer was in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee and such transfer was--

(A) made in the ordinary course of business or financial affairs of the debtor and the transferee; or

(B) made according to ordinary business terms;

Defendants have not established the factual predicates of their alleged group value defense or any individual monetary value to their alleged defenses. "[I]t [is] legal error for the bankruptcy court to interpret section 547(c)(1) to allow *some* new value to enable a creditor to protect a transfer without a calculation of the amount of that new value." *Creditors' Comm. v. Spada (In re Spada)*, 903 F.2d 971, 973 (3d Cir. 1990).

In his May 24, 2004 opinion in the Arnold proceeding, Judge Greendyke stated the following:

> It is true that maintaining the ability to sell a business unit as a going concern can be valuable in and of itself, and a debtor that makes a pre-petition investment in order to preserve that ability receives some value for purposes of fraudulent-conveyance analysis. *See, In re Fairchild*, 6 F.3d at 1127. However, the foregoing concepts do not render irrelevant an analysis of the individualized value provided by each Defendant. The Court finds the following analogy instructive: "Just because the [Houston] Astros could be sold for millions, but [may]

be worthless if they had no players, does not mean that they are not overpaying their rightfielder." (Committee's Opposition, at 46).

As a group, the Defendants in this case received over $44 million for 90 days of work, and that is in addition to their normal salaries, stock options, and any other forms of compensation. The Committee cites the following as an example of why a factual determination as to the value provided by each defendant is necessary:

> John Arnold, who had a salary of $160,000 a year, received a performance bonus of $8 million. According to the defendants' theory, Arnold is assumed to have provided new value in the allegedly promised 90-days to justify payments of $8.16 million or more than $2 million a month. Arnold, of course, was never compensated like that in his prior seven years at Enron. The amount would translate to more than $24 million a year – a sharp comparison to his $160,000 a year salary.

(Committee's Opposition at 72.)

Judge William Greendyke, May 24, 2004 Memorandum of Decision and Order.

Under the definition of new value in 11 U.S.C. § 547(a)(2), new value "does not include an obligation substituted for an existing obligation . . . ." This exclusion would apply to the trader Defendants having October 2001 or November 2001 contracts.

Further and most critically, § 547(c)(1)(A) and (B) requires a contemporaneous exchange for "*new value given to the debtor*," which did not occur in this case. *See* 11 U.S.C. § 547(c)(1)(A)-(B)(emphasis added). Judge Greendyke continued to hold in part:

The Court . . . finds persuasive the Committee's argument that value provided post-petition to the

> bankruptcy estate is not "new value" given to the debtor under § 547(c). (*See* [Committee's Opposition] at 75.) The Committee cites a Third Circuit case addressing § 547(c)(4), *Bergquist v. Anderson-Greenwood Aviation Corp. (In re Bellanca Aircraft Corp.)*, 850 F.2d 1275 (8th Cir. 1988). In *Bergquist*, the court notes that under § 547(c)(4), the creditor must have given new value to or for the benefit of the debtor. *Id.* at 1284. "These words imply that *subsequent advances of new value are only those given pre-petition, because any post-petition advances are given to the debtor's estate, not to the debtor." Id.* (emphasis in original); *see also TennOhio Transp. Co. v. Felco Comm. Serv. (In re TennOhio Transp.)* 255 B.R. 307. 310 (Bankr. S.D. Ohio 2000) ("*Postpetition advances of new value may not be applied to offset preferential transfers [because] section 547(c)(4) requires that the advances be made 'to or for the benefit of debtor,' and any postpetition transfers would not be for the debtor, but for the bankruptcy estate."*) (citations omitted). Section 547(c)(1) also requires that new value be "given to the debtor." In this case, Defendants contend they provided new value to the debtor by agreeing to remain at Enron for 90 days - through February 28, 2002. Enron, however, filed for bankruptcy on December 2, 2001, meaning that out of the 90 days of "value" Defendants provided to Enron, 89 of those days fell post-petition.

Id. (emphasis added). In *In re Ramba, Inc., the Fifth Circuit stated*:

> Certainly, Baker Hughes's dismissal of the petition began a chain of events that ultimately permitted Ramba to acquire money through the sale of its Drilling Fluids Division. The *"new value" described in 547(c)(1), however, must be "given to the debtor"* by the creditor as part of a "contemporaneous exchange". Thus, it is the precise benefit received from the creditor, and not the secondary or tertiary effects thereof, that must fit within one of the five categories of "new value"--i.e., money, goods, services, new credit, or the release of property--enumerated in 547(a)(2).[3] The controlling question, then, is whether the benefit Ramba received from Baker Hughes--that is, dismissal of the involuntary bankruptcy petition--fits within the statutory

definition of "*new value*".

416 F.3d at 399-400 (footnote omitted) (emphasis added). The court noted that:

> To hold otherwise would render the enumerated categories of "new value" in § 547(a)(2) essentially superfluous, since virtually any transaction between a creditor and debtor--including the act of paying an antecedent debt--can ultimately be traced to some subsequent financial

Id. at 400 n.3. The *Ramba* court went on to hold that where the chapter 7 debtor paid $85,654.85 to a supplier in satisfaction of a pre-existing debt on a delivery of goods in exchange for the supplier's dismissal of an involuntary proceeding the creditor brought against the debtor, such benefit that the debtor received did not constitute new value under § 547(c)(1). *See id.* at 399-400. Defendants did not prove a § 547(c)(1)(A) and (B) defense. In sum, Defendants failed to prove an 11 U.S.C. § 547(c)(1) defense.

During October 2001, and especially in late November 2001, chaos reigned with regard to Enron's bonuses. Enron found itself faced with a truly novel situation. These bonuses were not made according to the stated company bonus policies nor were they paid during the standard time of paying same. A bonus for the year 2001 would traditionally be paid in January or February 2002, and Towers Perrin, Enron's hired human resources consultant, would normally review the amount and propriety of the bonus. Although it was represented to the Board that Towers Perrin had approved same, Towers Perrin had not approved such.

As a whole, the bonuses given on November 29, 2001 were in a much larger amount than those given by Enron for the year 2000, then believed to be Enron's best year to date. The November 29, 2001 bonuses given to the Arnold Defendants were generally higher than those recited in their October 2001 contractual amendments and were accelerated to be immediately payable. There was insufficient credible proof that such November 29, 2001 payments were made in payment of debts incurred by Enron in the ordinary course of business or financial affairs of Enron and Defendants and (1) that such payments were made in the ordinary course of business or financial affairs of Enron and Defendants, or (2) made according to ordinary business terms. *See* 11 U.S.C. § 547(c)(2).[24] The payments made were made in direct anticipation of an imminent bankruptcy filing.

G. 11 U.S.C. § 550 Applicability

Under 11 U.S.C. § 550(a)(1), the Employment Committee may recover from the Lavorato Defendants and the Arnold Defendants. Since Wachovia was merely a conduit for the Arnold transferees, the Arnold Defendants are initial transferees under § 550(a)(1) and not entitled to any defense under § 550(b). *See Sec. First Nat'l Bank v. Branson (In re Coutee)*, 984 F.2d 138, 140-41 (5th Cir. 1993).

VII. INSOLVENCY

Per the Scheduling Order, the insolvency issues were tried

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[24] *See supra* note 19.

after the trial on the other issues and before any decision was reached.

As stated in *In re Brentwood Lexford Partners, LLC*,:

> Texas law parallels the Bankruptcy Code's approach to insolvency. Tex. Bus. & Com. Code Ann. § 24.003 (Vernon 2002). The Code defines insolvency as a "financial condition such that the sum of the [the] entity's debts is greater than all of [its] property, at a fair valuation ..." 11 U.S.C. § 101(32)(2002). Courts refer to this test as a balance sheet test, and engage in the "fair valuation" of the debts and property shown on the debtor's balance sheet. *In re Lamar Haddox Contractor, Inc.*, 40 F.3d 118, 121 (5th Cir. 1994); *In re Taxman Clothing Co., Inc.*, 905 F.2d 166, 169-70 (7th Cir. 1990). However, a fair valuation may not be equivalent to the book values assigned on a balance sheet. *Haddox*, 40 F.3d at 121.
>
> To perform this test, the court makes a two-step analysis. *In re DAK Indus. Inc.*, 170 F.3d 1197, 1199-1200 (9th Cir. 1999); *Taxman*, 905 F.2d at 169-70. The court must first determine whether the debtor was a "going concern" or was "on its deathbed." The court must then value the debtor's assets, depending on the status determined in the first inquiry, and apply the balance sheet test to determine whether the debtor was solvent. *Id.*
>
> For a debtor that was a going concern, the court would "determine the fair market price of the debtor's assets as if they had been sold as a unit, in a prudent manner, and within a reasonable time." *Id.* As a going concern, the debtor would not likely face a forced sale. Accordingly, a fair market valuation best determines a fair market price.

292 B.R. at 268.

The 11 U.S.C. § 101(32)(A)(i) definition of insolvency excludes from the calculation "property transferred, concealed or removed with intent to hinder, delay or defraud such entity's creditors." The Texas insolvency statute contains like

exclusions. *See* TEX. BUS. & COM. CODE ANN. § 24.003(d) (Vernon 2004) (containing similar exclusions).

The Texas fraudulent conveyance statute, under its insolvency definition, also states:

> (a) A debtor is insolvent if the sum of the debtor's debts is greater than all of the debtor's assets at a fair valuation.
>
> (b) A *debtor who is generally not paying the debtor's debts as they become due is presumed to be insolvent*.

Id. § 24.003(a)-(b)(emphasis added). From a state law uniform fraudulent transfer perspective, the credible evidence was substantially undisputed and the court finds that Enron was insolvent because it was generally not paying its debts as they became due at the time of the transfers in questions.

As to the Employment Committee's state law fraudulent conveyance claims under 11 U.S.C. § 544(b)(1), they are to be assessed under Texas law because that is where the transfers took place. *See* discussion *infra.*

Mr. Shaked ("Plaintiff's expert") was Plaintiff's insolvency expert.[25] No other expert witness was called by either side at the insolvency phase of the trial. However, to the extent relevant, the court will take into consideration the evidence from the first phases of the trial. Mr. Neslidge, present senior counsel at Enron and the only other witness at such insolvency

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[25] Plaintiff's expert credibly testified that the Enron debtors' affairs involved approximately 95 million pages of documents.

hearing, credibly testified as records custodian for Enron.[26]

The end of September 2001 signaled the accelerated financial demise of Enron. In its SEC 10-Q for the quarter ending September 30, 2001, Enron stated that if it lost its investment grade credit rating and its stock went below a certain price, a note trigger event on $3.9 billion in debt could occur. On October 1, 2001, Enron made its first negative disclosures regarding the partnerships of its former Chief Financial Officer, Andrew Fastow. On October 22, 2001, Enron disclosed that the SEC had launched an investigation into such partnerships, and on October 24, 2001, Enron discharged Fastow. Enron's stock price closed at $11.60 on October 30, 2001, down from a high of $82 per share in January 2001. This was its lowest level in nine years.

The disclosures led credit agencies to signal the possibility of downgrading Enron's credit rating to non-investment grade or junk status. Enron's credit rating dropped to Baa2 on October 29, 2001, and was followed by a downgrade to Baa3 on November 9, 2001. These downgrades significantly increased Enron's collateral and margin deposit requirements for the wholesale trading operation while at the same time limiting Enron's ability to borrow money to meet those requirements. Counterparties that traded with Enron responded to this uncertainty by reducing their transactions with Enron traders,

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[26] Significant Enron dates have been previously discussed herein in connection with other issues and will sometimes hereafter be further mentioned where appropriate.

thereby significantly curtailing Enron's business.

On November 8, 2001, Enron filed a 10K explaining that it would be filing restated financial statements for the years ending December 31, 1997 through 2000, and for the first and second quarters of 2001. The 10K cautioned readers of its financial statements that those previously issued financial statements should not be relied upon.

On November 9, 2001, Moody's downgraded Enron's debt to Baaa3, its lowest investment grade rating and kept it under review for further possible downgrading.

On November 13, 2001, speculation of an Enron possible takeover was confirmed when crosstown rival Dynegy and Enron announced a merger agreement. A $1.5 billion asset backed equity infusion by Dynegy was made to Enron. *See* Ex. 1004 at 91.

On November 19, 2001, Enron presented its financial condition to its bankers, noting that while the September 30, 2001 balance sheet reflected debt of $13 billion, the company's true debt load, including off-balance sheet financing, was in excess of $38 billion. *See* Exs. 1004 at 9, 23, 43, 45-47, 50; 260 (identical to Ex. 1142). Thus, as Enron noted, $25.116 billion of debt was off-balance sheet. *See* Ex. 169 at 9-10. Mr. Shaked's credible opinion was that Enron's debt was at least $23.9 billion on such date. *See* Ex. 1004 at 43.

On November 20, 2001, $50 million was placed in the Trust at

Wachovia to fund the Performance Bonus Trust to pay traders their bonuses. Also on this date, Enron announced that a downgrade in its credit rating would trigger obligations of $690 million. Additionally, the company further restated third quarter 2001 results that indicated greater losses than initially reported. *See* Ex. 308A at 6.

On November 28, 2001, Dynegy terminated its merger agreement with Enron.[27]

On November 29, 2001, Defendants signed agreements leading to immediate payment of bonuses. Also on this date, Wachovia received the list of designated trust beneficiaries from Enron.

On December 2, 2001, Enron filed for bankruptcy in the Southern District of New York.

Plaintiff's expert credibly[28] found that on November 20 and 29, 2001, (a) using the sum of the parts valuation methodology, Enron was insolvent by at least $8.2 billion (Ex. 1004 at 12), (b) using the discounted cash flow valuation methodology, Enron was insolvent by at least $23 billion (*id.* at 52; expert testimony on Sept. 7, 2005), (c) using the sum of the parts valuation methodology, ENA was insolvent by at least $6.7 billion, and (d) using the discounted cash flow methodology ENA

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[27] Credit agencies downgraded Enron's credit rating to junk status, and Enron's stock fell to 70¢ per share.

[28] Overall, Mr. Shaked's expert testimony and conclusions were generally found credible, although he was frequently unduly defensive in response to legitimate cross examination.

was insolvent by at least $9.8 billion.

Plaintiff's expert generally approached his analyses on a conservative basis. *See, i.e.,* Ex. 1004 at 4, 9, 11, 12, 27, 33, 40, 41, 46, 47, 49.

A. Interdependency of Enron and ENA

There was an interdependence of Enron and ENA[29] which was characterized by the following facts. First, Enron managed ENA's cash through a centralized cash management system. Second, ENA had no public debt, relying instead on ENE's financing activities. Third, ENA relied on ENE's maintenance of investment grade credit rating. Fourth, ENA shared physical space with ENE. Internal Enron presentations did not make a distinction between ENE and ENA. Fifth, key Enron and ENA employees were unaware of the distinction between Enron and ENA. Sixth, outside advisors to Enron, such as McKinsey and Goldman Sachs, made no distinction between ENE and ENA. Seventh, industry analysts covering Enron made no distinction between ENE and ENA. Eighth, ENE effected and controlled asset transfers between itself and ENA.

In the Disclosure Statement, ENA is listed as one of ENE's 172 affiliated entities. As previously noted, in the Disclosure Statement, ENA is listed as one of fifty-eight filing debtors that were part of ENE's Wholesale Services division.

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[29] In simplified terms, Enron Wholesale Services was a wholly owned subsidiary of Enron. In turn, ENA was a part of Enron Wholesale Services (ENS). ENA was the largest business within Enron. The trading unit was part of ENA. *See* Demonstrative Ex. 740 at 63, 84.

Plaintiff’s expert’s uncontroverted conclusions that ENA was not a going concern and cannot be valued separate from ENE are reasonable and warranted.

B. Neither Enron Nor ENA Were Going Concerns in Late November 2001

A first step issue in determining valuation of the assets of a business on a particular date is whether it should be valued as a going concern requiring valuation of its property as a whole or on an item by item basis. *See In re Brentwood Lexford Partners, LLC*, 292 B.R. at 268 (noting generally fair market going concern price is used unless a business *is on its deathbed* in which case a liquidating value should be used); *see also In re Taxman Clothing Co. Inc.*, 905 F.2d 166, 170 (7th Cir. 1990); *Schwinn Bicycle Comm. v. AFS Cycle & Co., Ltd. (In re Schwinn Bicycle Co.)*, 192 B.R. 477, 486 (Bankr. N.D. Ill. 1996) (quoting *Util. Stationery Stores, Inc. v. Southworth Co. (In re Util. Stationery Stores, Inc.)*, 12 B.R. 170, 176 (Bankr. N.D. Ill. 1981)).

When a debtor cannot operate and bankruptcy is inevitable, the debtor is not a going concern. To be a going concern, a debtor "must have had [a] realistic capacity to manufacture and sell its product, and thus [a] going concern valuation is appropriate only if it is believed that [the] enterprise will continue as [a] going concern.” *Gillman v. Scientific Research Prods., Inc. of Del. (In re Mama D’Angelo, Inc.)*, 55 F.3d 552,

556 (10th Cir. 1995)(citation omitted). In particular, "[t]he point of peril is reached when the firm's ability to continue as a going concern--a concern that can cover its costs--is in doubt because its expected costs are greater than its expected revenue." *In re Taxman Clothing Co., Inc.*, 905 F.2d at 169. "A commercial enterprise is a going concern if it is actively engaged in business with the expectation of indefinite continuance." *Silverman Consulting, Inc. v. Hitachi Power Tools, U.S.A., Ltd. (In re Payless Cashways, Inc.)*, 290 B.R. 689, 702 (Bankr. W.D. Mo. 2003)(footnote omitted).

The "following factors [are] evidence of a going concern: (1) whether the company was operating; (2) whether the officers were optimistic; and (3) whether the managers and lenders continued to invest in the business." *Id.* at 702 (citing *Jones Truck Lines, Inc. v. Full Serv. Leasing Corp.*, 83 F.3d 253, 258 (8th Cir. 1996)). "Where bankruptcy is not 'clearly imminent' on the date of the challenged conveyance, the weight of authority holds that assets should be valued on a going concern basis." *Moody v. Sec. Pac. Bus. Credit, Inc.*, 971 F.2d 1056, 1067 (3d Cir. 1992)(citations omitted).

In *In re Mama D'Angelo, Inc.*, the court stated:

> We are mindful of the authority to the effect that fair valuation ordinarily must be made from the vantage of a going concern and that subsequent dismemberment should not enter into the picture. *See 2 Collier on Bankruptcy* ¶ 101.32 (1995); *Cissell v. First Nat'l Bank of Cincinnati*, 476 F.Supp. 474, 484 (S.D. Ohio 1979) (a

> company's assets must be valued at the time of the alleged transfer and not at what they turned out to be worth at some time after the bankruptcy intervened); *Mutual Sav. & Loan Ass'n v. McCants*, 183 F.2d 423 (4th Cir.1950). *But we "may consider information originating subsequent to the transfer date if it tends to shed light on a fair and accurate assessment of the asset or liability as of the pertinent date." In re Chemical Separations Corp., 38 B.R. 890, 895-96 (Bankr. E.D. Tenn.1984). Thus, it is not improper hindsight for a court to attribute current circumstances which may be more correctly defined as current awareness or current discovery of the existence of a previous set of circumstances.* In this case, even Scientific's witnesses acknowledge a current "discovery" or "awareness" of circumstances then in existence: "[M]ost of the problems were inherent with the original construction of the plant which, you, would have been there as of [the] day we moved into the plant," and management had "stuck millions upon millions of dollars fruitlessly into this facility." Circumstances did not change between July and the November shut-down date; it simply took management a few months to "discover" and became "aware" of those circumstances that existed beginning in July.

55 F.3d at 556 (emphasis added). Here, without an investment grade credit rating at ENE, ENA could not and was not operating and could not pay its debts when due. Therefore, as of the time of the transfers, ENA was not a going concern. Likewise, ENE could not operate without an investment grade credit rating and was therefore not a going concern as of the transfer dates.

ENE and ENA were insolvent at the time the relevant transfers were made. The foregoing and following evidence further support these findings.

The transfers were made in direct contemplation of bankruptcy. *See* Jones Dep. at 192, 204, 282, Mar. 30, 2005;

Oxley Dep. at 233-34, Mar. 7, 2005. "At the time [the November 29, 2001 Performance Bonus memos] were being drafted, the company was preparing to go into bankruptcy." (Cash Dep. at 118:8-9, Jan. 28, 2005.) Louise Kitchen testified about a trading floor meeting on Wednesday, November 28, in which "we tell everyone that it looks like bankruptcy." (Kitchen Dep. at 222:9-10, Feb. 17, 2005.)

The transfers were made at a time when Enron and ENA were not paying, and could not pay, their creditors. Enron's last SEC filing before the bankruptcy, the 10-Q Report dated September 30, 2001, stated:

> It is not possible to predict whether any or all of the actions described above (including the sale of non-core businesses and assets and the refinancing or waiver of Enron obligations that may become immediately payable upon scheduled maturities or due to an acceleration event) will be adequate to maintain Enron's investment grade credit rating or enable Enron to refinance or otherwise restructure its debt obligations that become due. An adverse outcome with respect to any of these matters would likely have a material adverse impact on Enron's ability to continue as a going concern.

(Ex. 1018 at 12.) Then, on November 28, 2001, when Dynegy terminated the discussed merger, Enron announced in a press release that it was temporarily suspending "all payments other than those necessary to maintain core operation" and that recent events had "dramatically lowered the market's confidence in Enron and its trading operations." (Ex. 671.)

Given the testimony regarding how information was shared among the Trading Group, and particularly given the importance of

these issues, the physical proximity of their workstations, and the lack of other business activities, it appears that the Arnold Defendants were aware of the imminence of Enron's bankruptcy before it was filed.

The crown jewel of Enron was supposedly the trading unit of ENA. On January 18, 2002, at a postbankruptcy hearing, the debtors' motion for the sale of the ENA trading unit to UBS was considered and granted. *See* Ex. 691. The trading unit had been for sale from before announcement of the potential Dynegy merger during November 8-13, 2001, until the Dynegy merger discussions terminated on November 28, 2001. The debtors' expert testified that the liquidation value of such unit was substantially below $50 million. *See id.* at 21. A bid had been received for $25 million, which was not accepted. *See id.* at 62. Under the transaction as approved on January 18, 2002, six hundred Enron traders were to migrate to the new company, UBS. *See id.* at 29. Enron was to receive a potential royalty out of the sale, but as of the trial of these present adversary proceedings, no royalty has ever been realized from such UBS transaction. Enron had contended that its existing book of business at petition date, which was not part of the UBS sale, was worth approximately $7 billion (*id.* at 95), but at such January 18, 2002 hearing, its value was believed to be in the range of $1.3 billion (*id.* at 149, 162, 258). The bankruptcy court approved the sale to UBS

finding the sale to have a potential value of between $1 to $2 billion. *See id.* at 259. The court further found that nothing in the order approving the UBS sale would be deemed to release or otherwise affect the debtors' or their estates' rights under Chapter 5 including avoidance actions. *See* Exs. 691, 692.

The book value of the property of ENE and ENA vastly exceeded the fair value for their assets. The liabilities of both ENE and ENA exceeded the fair value of their assets. ENE and ENA could not pay their debts when due at the time the transfers were made. ENE filed for bankruptcy because the lowering of its credit rating made it unable to pay its current obligations.

John Duncan, a member of Enron's Board of Directors testified:

> Q. Why did Enron Corp. file bankruptcy?
> A. Because they lost their financial credibility and loans were due and payable because they lost their credit rating.
> Q. Could Enron make payments on those loans with its current cash at the time --
> A. Did Enron make a payment --
> Q. No. Could Enron -- did Enron have the ability to meet those loans when they were due?
> A. No. That's why they went bankrupt.

(Duncan Dep. at 16:9-16:18, Apr. 11, 2005.)

ENE's credit rating was downgraded to well below investment grade on November 28, 2001. *E.g.*, Exs. 442 (identical to Ex.

671),[30] 1045 at 115 (STAFF OF S. COMM. ON GOV'T AFFAIRS, 107TH CONG., FINANCIAL OVERSIGHT OF ENRON: THE SEC AND PRIVATE-SECTOR WATCHDOGS 115 (Comm. Print Oct. 2002)); *see also* Ex. 1046 (STAFF OF S. COMM. ON GOV'T AFFAIRS, 107TH CONG., ENRON'S CREDIT RATING: ENRON'S BANKERS' CONTACTS WITH MOODY'S AND GOVERNMENT OFFICIALS (Comm. Print Jan. 2003)). It appears that such reports, Exhibits 1045 and 1046, are admissible under Federal Rules of Evidence 803(8)(B), 803(8)(C), or the residual exception under Rule 807. *See SEC v. Drexel Burnahm Lambert*, 837 F.Supp. 587, 617 (S.D.N.Y. 1993). Exhibits 1045 and 1046, both Senate reports, and Exhibit 70, a report by the Joint Committee on Taxation, were admitted into evidence.

This is a bench trial, and the court can properly weigh the evidence, such that the court has "considerable discretion" when deciding whether the residual exception applies and will not be overturned "absent a clear error of judgment." *Page v. Barko Hydraulics*, 673 F.2d 134, 140 (5th Cir. 1982). Such reports (1) are more probative than other available evidence that could be obtained through reasonable efforts, and (2) the general purpose of rules of evidence will be served by their admission.

According to Enron records in evidence, as of mid-November 2001, "[c]urrent maturities greatly exceed operating cash flow."

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[30] Enron Press Release dated November 28, 2001, Subject: Enron Announces Notification by Dynegy of Merger Termination; Credit Rating Downgraded; Takes Action to Preserve Core Franchise ("Chief among these is a temporary suspension of all payments other than those necessary to maintain core operations."). (Ex. 442.)

(Ex. 1142 at 4) (identical to Ex. 260). Such exhibit is the November 19, 2001 bank presentation. *See* Ex. 169 at 9-10. Enron's net cash margin during this time, including its trading contracts, was a negative $1.282 billion. *See* Ex. 1142 at 39. Enron expected negative cash flow from its operations in 2002 to total almost $4 billion. *See id.* at 50.

Enron's last 10-Q before the bankruptcy filing stated:

> In the event Enron were to lose its investment grade credit rating and Enron's stock price was below a specified price, a note trigger event would occur. This could require Enron to repay, refinance or cash collateralize additional facilities totaling $3.9 billion, which primarily consist of $2.4 billion of debt in Osprey Trust (Osprey) and $915 million of debt in Marlin Water Trust (Marlin).

(Ex. 1018 at 11.) Downgrade below investment grade triggered at least another $1.6 billion in obligations under contractual margin agreements and required the replacement of letters of credit with cash. *See* Ex. 1142 at 36 (identical to Ex. 260). The Senate Report opined that ENE's credit rating would have been downgraded much earlier if the credit rating agencies had acted with due diligence or if Enron's management had not misrepresented its financial condition. *See* STAFF OF S. COMM. ON GOV'T AFFAIRS, 107TH CONG., FINANCIAL OVERSIGHT OF ENRON: THE SEC AND PRIVATE-SECTOR WATCHDOGS 97-125 (Comm. Print Oct. 2002). ENA's

obligations were tied to ENE’s credit rating, so that a downgrade of ENE’s credit rating to below investment grade necessarily meant that ENA’s debts were greater than its assets and that ENA could not pay its debts when due.

Plaintiff’s expert’s uncontroverted testimony supports a finding of insolvency for ENA and ENE. He is qualified and utilized proper expert methodologies. His partial reliance on the expert opinions of Dr. B. Dharan and Dr. H. Bessembinder was reasonable and appropriate. His partial reliance on the reports of the United States Government was reasonable and appropriate.

Plaintiff’s experts uncontroverted conclusion that Enron’s trading operating were not a going concern on the date of the transfers is reasonable and warranted. It is uncontested that Enron’s trading operations were dependent on ENE’s credit rating. When ENE lost its investment grade trading rating, Enron immediately shut down Enron Online and ceased all active trading operations. Defendant traders conceded that Enron could not trade in its last days. Individual Defendant traders claimed that ENA’s inability to support their trading breached their employment contracts and adversely affected Enron’s ability to enforce non-competition covenants.

The dependence of Enron’s trading on an investment grade credit rating has been uncontested. Enron, itself, warned in its last prebankruptcy SEC filing that the deterioration in its credit rating would decrease profits, even though the credit

rating was still investment grade. In fact, all trading was shut down within hours of the drop in the credit rating. The Defendants' proposed finding states: "The downgrade in Enron's credit rating [on November 28, 2001] essentially brought trading to a halt since Enron could no longer meet margin requirements that would allow traders to continue trading." (Defs.' Proposed Findings #26).

Defendants concede that ENE's financial difficulties negatively impacted trading operations including through "significantly increased collateral and margin deposit requirements for the wholesale trading operation while at the same time limiting Enron's ability to borrow money to meet those requirements." (*Id.* #11.)

Government reports indicate that it was the dependence on Enron's credit rating that induced the substantial accounting manipulations set out in those reports.

Plaintiff's expert's conclusion that Enron's credit rating would have been reduced earlier had Enron not hidden its true financial condition, a conclusion mirrored by the United States Senate report, is reasonable and warranted. Plaintiff's expert used conservative book values to set the maximum value of many Enron assets is reasonable and overstates the value of many Enron assets. Enron's April 22, 2002 8-K ("Enron's 8-K") reported that Enron's earlier filings should not be relied upon and that Enron management believed that the book value of its assets would have

to be written down by approximately $22 to 24 billion, in part because previous values were overstated due to possible accounting errors or irregularities. *See* Ex. 1073 at 7-8. Enron's 8-K stated that $8-10 billion of the expected reduction in value related to price risk management assets, the name by which Enron denominated trading assets. *See id.* at 8.[31]

Plaintiff's expert's uncontroverted conclusion that Enron's Wholesale Division had a maximum value of $3.471 billion is reasonable and warranted. He utilized book values of the Wholesale Division's investments and trading books, which would place a higher than expected value on those assets because of negative conditions that then existed but later came to light. His valuation is conservative because he does not use liquidation values and did not give any discount because of (a) counter-parties' rights to declare default either because of (i) the drop in credit rating or (ii) Enron's trading activities; (b) Enron's mark-to-market accounting; or (c) the fact that a forced sale value would have been lower. Instead, he utilized Enron's own stated values for the contracts.

Even if the trading unit had a $1 to $2 billion going concern value as claimed by Defendants, Enron and ENA would still be insolvent. Defendants claim that Enron's trading unit "had a present [going concern] value of between $1-$2 billion." (Defs.'

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[31] Enron's book values, set before the drop in Enron's credit rating, allowed counterparties to reject the contracts.

Proposed Finding #42.) Even if true, ENE's and ENA's liabilities were more than $2 billion greater than its assets under any reasonable valuation before the court, so even if Defendants' claims were accepted as true, ENE and ENA would still be insolvent.

Plaintiff's expert's uncontroverted conclusion that assets of Enron's Transportation and Distribution Division had a conservative value of $7.4 billion is reasonable and warranted under a conservative valuation.

Plaintiff's expert's uncontroverted conclusion that assets of Enron Energy Services had a conservative value of $1.476 billion is reasonable and warranted.

Plaintiff's expert's uncontroverted conclusion that the assets of Enron Broadband Services had a conservative value of $728 million, despite the fact that Enron ascribed zero value to those assets, is reasonable and warranted under a conservative valuation approach.

Plaintiff's expert's uncontroverted conclusion that the assets of Enron Global Assets had a conservative value of $2.622 billion is reasonable and warranted under a conservative valuation approach.

Plaintiff's expert's approach, in not ascribing any corporate overhead or contingent liabilities to his values, is very conservative. He notes that internal documents show corporate overhead to total in the multiple billions of dollars.

Enron’s accounting and trading activities created substantial contingent liabilities, also in the billions of dollars. Enron settled liabilities associated with its California trading at a figure of more than $1 billion.

In addition, the analysis is conservative because it necessarily assumes a going concern value despite the strong evidence that Enron was not a going concern as a result of its reduced credit rating. Furthermore, Plaintiff’s expert did not make any deduction for ENA’s overhead expenses, which again bolsters the conservativeness of his conclusions.

Plaintiff’s expert’s uncontroverted conclusion that Enron’s total debt was no less than $23.9 billion (Ex. 1004 at 43) is conservative, reasonable, and warranted. Internal Enron documents indicate Enron’s total debt was more than $38 billion. This debt figure does not include contingent debt. There is substantial evidence related to Enron’s off-balance sheet debt, including Enron’s own records, reports of governmental agencies, and reports of the ENE and ENA Examiners.

Plaintiff’s expert’s uncontroverted conclusion that ENE was insolvent based on a review of its discounted cash flow is reasonable and warranted.

Plaintiff’s expert’s uncontroverted conclusion that ENA was insolvent based on a sum of the parts review is reasonable and warranted. His valuation was conservative. Internal records show only $2.64 billion in assets held in ENA on balance sheet

and supposedly $1.8 billion off-balance sheet. *See* Ex. 1134 at 4; *see also* discussion *supra* of testimony concerning values espoused at the January 18, 2002 bankruptcy court hearing per Ex. 691. His valuation does not include any discount for the fall in Enron's credit rating, which was an event of breach in the contracts.

The setting of ENA's price risk management ("PRM") assets at $0 is conservative. Enron documents prebankruptcy show a substantial--more than $1 billion--negative value for PRM assets within Enron. *See* Ex. 1139 at EC 095014080. Prebankruptcy statements do not include any discount for the drop in Enron's credit rating and the resulting right to call a default.

Plaintiff's expert found the total debt estimate for ENA to be $9.838 billion. *See* Ex. 1004 at 59. The court finds this estimate is conservative because it does not include any: (1) litigation or contingent debt; (2) liabilities or loss in value caused by defaults from Enron's loss of an investment grade credit rating; or (3) of the debt associated with SPE's and other off-balance sheet transactions that were conducted through ENA.

The following conclusions of government reports support a conclusion of insolvency:

(1) Enron's Board breached its fiduciary duties in allowing "Enron to engage in high risk accounting, inappropriate conflict of interest transactions, extensive off-the-books activities, and

excessive executive compensation." THE ROLE OF THE BOARD OF DIRECTORS IN ENRON'S COLLAPSE, S. REP. NO. 107-70, at 3 (2002). The aforementioned report is Exhibit 45.

(2) Enron conducted "billions of dollars in off-the-books activity to make its financial condition appear better than it was and failed to ensure adequate public disclosure of material off-the-books liabilities that contributed to Enron's collapse." *Id.*

(3) Enron's trading business necessitated access to "significant lines of credit . . . ." *Id.* at 7.

(4) Dramatic fluctuations in Enron's trading profits caused Enron to utilize questionable accounting schemes to present a more stable outlook to credit rating agencies. *Id.* at 20-23.

(5) Because Enron could not find financial institutions or unrelated parties to accept the huge risks it incurred, Enron used related entities to assume the risks. *Id.* at 7.

(6) The use of complicated off-balance sheet devices "became dominant" at Enron; "at its peak, the company apparently had between $15 and $20 billion involved in hundreds of structured finance transactions." *Id.* at 8.

(7) Enron's April 22, 2002 8-K announced that the company's financials were unreliable, and the book value of its assets would have to be written down as much as $24 billion. *Id.* at 11.

(8) Enron's "apparent intention to manipulate the

California energy market" created potential liability. *Id.* (footnote omitted).

(9) Enron apparently instructed its tax department to produce billions of dollars in company earnings through the use of complex tax shelters. *Id.*

(10) The Enron Board approved the moving of the entity Whitewing off Enron's books while guaranteeing its $1.4 billion in debt. *Id.* at 12, 40.

(11) The Enron Board was informed that Enron's international assets were overvalued on Enron's books by $2.3 billion. *Id.* at 12.

(12) In April 2001, Enron's board was told that sixty-four percent of Enron's assets were "troubled" or performing below expectation. *Id.*

(13) Enron knew and was advised by its accountants that its accounting methodologies relied extensively on subjective judgments by management and presented a high risk of non-compliance with Generally Accepted Accounting Principles ("GAAP"). *Id.* at 15.

(14) Enron's outside accountants, Arthur Andersen LLP ("Andersen"), informed Enron and its Board that "Enron has aggressive earnings targets and enters into numerous complex transactions to achieve those targets." *Id.* at 18. Andersen also apprised them that "[t]he Company's personnel are very

sophisticated and enter into numerous complex financial transactions and are often aggressive in structuring transactions to achieve desired financial reporting objectives." *Id.*

(15) Andersen also informed Enron and its Board that Enron's extensive use of mark-to-market earning was intelligent gambling. *Id.* at 19.

(16) "Enron's multi-billion dollar, off-the-books activity was disclosed to the Enron Board and received Board approval as a [sic] explicit strategy to improve Enron's financial statements." *Id.* at 38.

(17) By November 2001, Enron could not support its debt obligations. *See also* STAFF OF JOINT COMM. ON TAXATION, 107TH CONG., REPORT OF INVESTIGATION OF ENRON CORPORATION AND RELATED ENTITIES REGARDING FEDERAL TAX AND COMPENSATION ISSUES, AND POLICY RECOMMENDATIONS (Comm. Print Feb. 2003) [hereinafter the Joint Tax Report]. The aforementioned report is Exhibit 70.

(18) The Joint Tax Report also details Enron's pervasive use of off-balance sheet transactions to obscure its debt position, including numerous transactions run through ENA and its wholly owned subsidiary. *Id.*

(19) There was an "apparent pervasiveness of . . . fraudulent conduct" within Enron. STAFF OF S. COMM. ON GOV'T AFFAIRS, 107TH CONG., FINANCIAL OVERSIGHT OF ENRON: THE SEC AND PRIVATE-SECTOR WATCHDOGS 2 (Comm. Print Oct. 2002). The aforementioned report is

Exhibit 1045. Questionable practices "involved substantial--in some cases staggering--amounts of money. The loans-cum-commodity trades, for example, alone accounted for an estimated $7-8 billion in allegedly improperly recorded liabilities and cash flow; not disclosing contingent liabilities kept the potential for almost $4 billion in losses out of Enron's financial documents . . . ." *Id.* at 26 (footnotes omitted).

(20) A reduction in ENE's credit rating to below investment grade triggered an additional $4 billion in debt. *Id.* at 39.

(21) ENE's credit rating would have been downgraded much earlier if the credit rating agencies had acted with due diligence if Enron's management had not misrepresented its financial condition. *See id.* at 97-125.

(22) Enron had a distinct incentive to misuse mark-to-market accounting and did so. *See id.* at 40-47.

(a) Enron used mark-to-market accounting for long-term contracts, which required use of models, but "[t]he assumptions underlying these models were, in the best case, necessarily subjective and, in the worst [case], subject to deliberate manipulations." *Id.* at 43.

(b) "The evidence suggests that Enron, at a minimum, overestimated and very possibly manipulated the values of the energy contracts it marked to market." *Id.* at 44.

(c) "The incentives to be optimistic about the

assumptions underlying the model, moreover, were not only for Enron's executives, concerned about the next quarter's revenue numbers, but also for lower level employees whose bonuses were based on the full marked-to-market value of the deals they completed." *Id.* (footnote omitted).

(23) ENA's mark-to-market "profits" were substantial for the year 2000, accounting for more than half of ENE's reported earnings. *Id.* at 46.

(24) Enron, itself, conceded that the mark-to-market accounting for its energy trades was solely "management's best estimate considering various factors . . . ." *Id.* at 46 (citing various Enron SEC filings).

(25) ENE hid substantial losses in its Enron Energy Services division within its wholesale group. *Id.* at 44.

(26) Even the November 18, 2001 downgrade to BBB-, still investment grade, triggered about $690 million in new debt for Enron, something Enron did not disclose prior to the downgrade. *Id.* at 114.

(27) Enron drew down $3 billion in credit on October 25, 2001. *See* STAFF OF S. COMM. ON GOV'T AFFAIRS, 107TH CONG., ENRON'S CREDIT RATING: ENRON'S BANKERS' CONTACTS WITH MOODY'S AND GOVERNMENT OFFICIALS at 2 (Comm. Print Jan. 2003). The aforementioned report is Exhibit 1046.

(28) Enron could not function without an investment grade

credit rating. *Id.*

(29)

> [Enron's] investment grade rating was essential to its ability to enter into agreements with counterparties in the context of its trading operations, one of Enron's most profitable divisions; in addition, Enron had "triggers" tied to credit ratings in a number of agreements that, in the event of a downgrade, would have either constituted a default or would have required Enron to post significant amounts of cash collateral.

Id. at 2-3 (footnote omitted).

(30) "Moody's and other credit rating agencies should have downgraded Enron to below investment grade much earlier than they did (November 28, 2001)--indeed, significantly earlier than November 8, 2001." *Id.* at 18(footnote omitted).

(31) Enron misled the credit rating agencies. *See* SEC COMM'N, REPORT ON THE ROLE AND FUNCTION OF CREDIT RATING AGENCIES IN THE OPERATION OF THE SECURITIES MARKETS 16 (Jan. 2003). The aforementioned report is Exhibit 1001.

(32) Enron had credit rating "'triggers' in trading and other financial agreements" that "gave counterparties the right to demand cash collateral, and lenders the right to demand repayment of outstanding loans, once Enron's credit rating declined to certain levels." *Id.* at 29.

(33) The Senate investigated

> more than $8 billion in deceptive transactions referred to as "prepays," which Citigroup and Chase used to

> issue Enron huge loans disguised as energy trades. By characterizing the transactions as energy trades rather than loans, Citigroup and Chase enabled Enron to claim the loan proceeds were cash flow from business operations rather than cash flow from financing, thereby misleading in size of Enron's trading operations and the nature of its incoming cash flow.

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS, FISHTAIL, BACCHUS, SUNDANCE AND SLAPSHOT: FOUR ENRON TRANSACTIONS FUNDED AND FACILITATED BY U.S. FINANCIAL INSTITUTIONS, S. REP. NO. 107-82, at 1-2 (2003). The aforementioned report is Exhibit 1146.

(34) The four transactions in issue "utilized deceptive accounting or tax strategies . . . ." *Id.* at 2.

(35) The Senate investigation involved a review of more than two million pages of documents and the conducting of over one hundred interviews. *Id.*

(36) The Fishtail, Bacchus, and Sundance transactions took place between December 2000 and June 2001. *Id.* at 3. As a whole, they "resulted in a disguised, six-month loan advanced by Citigroup to facilitate Enron's deceptive accounting"--all resulting in a fictitious inflation of earnings by $112 million. *Id.*

(37) "In essence, the Slapshot transaction cloaked a legitimate $375 million loan to Enron ... inside a $1.4 billion sham loan to Enron issued by a Chase-controlled [special purpose entity]." *Id.* at 4.

(38) The Fishtail, Bacchus, and Sundance transactions were

conducted by and through ENA. *Id.* at 5, 6, 13 and 20.

Findings of the United States Bankruptcy Court for the Southern District of New York when confirming plans of reorganization of ENE and ENA reflect the following and support a finding of insolvency. *See* Ex. 1064. The Fifth Amended Joint Plan confirmed in Case No. 01-16034 in July 2004 provides:

(1) A distribution to creditors of ENE and ENA based on a 30/70 distribution formula. *See id.* at 40, 42, 48.

(2) The 30/70 distribution formula provides recovery of ENA creditors of 20.1%. *See id.* at 71. ENE's creditors will receive 17.4% on the dollar per the Disclosure Statement. *See* Ex. 406 at 33.

(3) The distribution to creditors of ENA under a stand-alone chapter 11 plan of reorganization would be only 17.4%. *See* Ex. 1064 at 71.

(4) The distribution model was "extensively diligenced by the Debtors, the Creditors Committee and its advisors and the ENA Examiner and his professionals." *Id.* at 40.

Enron's Disclosure Statement provided adequate disclosure to its creditors. *See id.* at 15. The Disclosure Statement shows that the value of ENE's assets totaled just over $13 billion, while its unsecured liabilities totaled more than $69 billion that is more than $40 billion without intercompany debt. *See* Ex. 1062 App. C-I at 61. The Disclosure Statement also shows that

the value of ENA's assets totaled approximately $6.2 billion, while its unsecured liabilities totaled more than $27 billion that is more than $13.6 billion without intercompany debt. *See id.* at 107.

Of the debtors in the Jointly Administered Case No. 01-16043, ENE was the only entity with a credit rating by the major domestic rating agencies. *See* Ex. 1064 at 50 ¶ (j). ENA did not have a credit rating of its own. *Id.* ENA depended on ENE's credit rating. *Id.* ENA became unable to continue its business operations upon the downgrade of ENE's credit rating. *Id.*

B. Conclusion on Insolvency

On November 20 and November 29, 2001, the dates of the transfers in question, it appears that the Enron debtors were on their deathbeds and insolvent, not going concerns.

It is substantially undisputed, and this court has found, that debtors were unable to pay their debts as they became due at the relevant times. Therefore, with respect to Texas, state law fraudulent conveyance claims and their state law definitions of insolvency, debtors were insolvent. *See* TEX BUS. & COM. CODE ANN. § 24.003(b) (Vernon 2004).

Only Plaintiff's expert witness was called to testify on insolvency. He testified that Enron was insolvent, using a sum of the parts methodology in the amount of at least $8.2 billion; and, on a cash flow basis, insolvent in the amount of at least

$23 billion, and that ENA was insolvent on a sum of the parts basis by at least $6.7 billion; and, on a cash flow basis, by at least $9.8 billion.

Aside from the multiple SEC filings and other exhibits discussed *supra*, it appears that two undisputed events are revealing and are convincing on the insolvency issue. On November 19, 2001, debtor met with its bankers to discuss its chaotic affairs. Debtor pointed out that while the debt reflected on its balance sheets was $12.978 billion, its actual debt was $38.094 billion because $25.116 billion of debt was off-balance sheet. *See* Exs. 169 at 9-10; 1004 at 9, 23, 43, 45-47; Ex. 1142 (identical to Ex. 260).

Enron's April 22, 2002 8-K announced that the company's SEC filings were unreliable, and the book value of its assets would have to be written down by as much as $24 billion. *See* Exs. 45 at 11; 1073 at 7-8. Such post-transfer 8-K evidence is cumulative under the retrojection doctrine and is further consistent with information revealed by Enron at the November 19, 2001 meeting with its bankers. "[I]t is not improper hindsight for a court to attribute current circumstances which may be more correctly defined as current awareness or current discovery of the existence of a previous set of circumstances." *In re Mama D'Angelo, Inc.*, 55 F.3d at 556. Under such doctrine, it is not improper for the court to assess the impact of the foregoing

revelations about Enron’s prebankruptcy activities, especially where Enron deliberately obfuscated its own books and records to confuse and manipulate public awareness of its true financial situation.

VIII. FRAUDULENT TRANSFERS

11 U.S.C. § 548(a)(1)[32] states:

> The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily–
>
> (A) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted; or
>
> (B)(i) received less than a reasonably equivalent value in exchange for such transfer or obligation; and
>
> (ii)(I) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;
>
> (II) was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the debtor was an unreasonably small capital; or
>
> (III) intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured.

The Bankruptcy Code defines “insider” in § 101(31)(B), stating:

> (B) if the debtor is a corporation--
> (i) director of the debtor;
> (ii) officer of the debtor;
> (iii) person in control of the debtor;

[32] Amendments to 11 U.S.C. § 548 under BAPCPA do not effect cases filed before October 17, 2005.

(iv) partnership in which the debtor is a general partner;
(v) general partner of the debtor; or
(vi) relative of a general partner, director, officer, or person in control of the debtor . . . .

Section 101(31)(E) defines an "insider" to include an "affiliate, or insider of an affiliate as if such affiliate were the debtor." 11 U.S.C. § 101(31). Pursuant to § 101(31)(E), a creditor who is an insider of an affiliate is also an insider of the debtor corporation. *See Wilson v. Huffman (In re Missionary Baptist Found. of Am., Inc.)*, 712 F.2d 206, 210-11 (5th Cir. 1983).

The Texas Uniform Fraudulent Transfer Act ("TUFTA") states:

(a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or within a reasonable time after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

(1) with actual intent to hinder, delay, or defraud any creditor of the debtor; or
(2) without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:
(A) was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
(B) intended to incur, or believed or reasonably should have believed that the debtor would incur, debts beyond the debtor's ability to pay as they became due.

(b) In determining actual intent under Subsection (a)(1) of this section, consideration may be given, among other factors, to whether:

(1) the transfer or obligation was to an insider;
(2) the debtor retained possession or control of

the property transferred after the transfer;

(3) the transfer or obligation was concealed;

(4) before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;

(5) the transfer was of substantially all the debtor's assets;

(6) the debtor absconded;

(7) the debtor removed or concealed assets;

(8) the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;

(9) the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;

(10) the transfer occurred shortly before or shortly after a substantial debt was incurred; and

(11) the debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.

TX CODE BUS. & COM. § 24.005(a)-(b) (Vernon 2004).

"Insider" is defined under TUFTA § 24.002(7)(B), if the debtor is a corporation as

(i) a director of the debtor;
(ii) an officer of the debtor;
(iii) a person in control of the debtor;
(iv) a partnership in which the debtor is a general partner;
(v) a general partner in a partnership described in Subparagraph (iv) of this paragraph; or
(vi) a relative of a general partner, director, officer, or person in control of the debtor . . . .

Id. at § 24.002(7)(B). TUFTA § 24.002(1) defines "affiliate" as:

(A) a person who directly or indirectly owns, controls, or holds with power to vote, 20 percent or more of the outstanding voting securities of the debtor, other than a person who holds the securities:

(i) as a fiduciary or agent without sole discretionary power to vote the securities; or

(ii) solely to secure a debt, if the person has not exercised the power to vote;

(B) a corporation 20 percent or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by the debtor or a person who directly or indirectly owns, controls, or holds, with power to vote, 20 percent or more of the outstanding voting securities of the debtor, other than a person who holds the securities:
(i) as a fiduciary or agent without sole power to vote the securities; or
(ii) solely to secure a debt, if the person has not in fact exercised the power to vote;

(C) a person whose business is operated by the debtor under a lease or other agreement, or a person substantially all of whose assets are controlled by the debtor; or

(D) a person who operates the debtor's business under a lease or other agreement or controls substantially all of the debtor's assets.

Section 24.002(9)defines a "person" as an individual, partnership, corporation, etc., or any other legal or commercial entity. *Id.* at § 24.002(9). The list of insiders is merely illustrative and not confining. *Browning Interests v. Allison (In re Holloway)*, 955 F.2d 1008, 1010-11 (5th Cir. 1992).

A fraudulent transfer may be attacked under 11 U.S.C. § 548 or pursuant to applicable state law under § 544(b)(1). Generally, the plaintiff has the burden of proof with respect to the existence of a fraudulent transfer. *See Jenkins v. Chase Home Mortgage Corp. (In re Maple Mortgage, Inc.)*, 81 F.3d 592 (5th Cir. 1996); *Butler Aviation Int'l, Inc. v. Whyte (In re Fairchild Aircraft Corp.)*, 6 F.3d 1119 (5th Cir. 1993). In *In re Brentwood Lexford Partners, LLC*, the court stated:

The trustee may avoid any transfer of an interest

> of the debtor in property that is avoidable under applicable law by a creditor holding an allowed unsecured claim. 11 U.S.C. § 544(b)(2002). Known as the strong arm provision of the Bankruptcy Code, § 544 "allows the trustee to step into the shoes of a creditor for the purpose of asserting causes of action under state fraudulent conveyance laws and confers on the trustee the status of a hypothetical creditor or bona fide purchaser as of the commencement of the case." *In re Zedda*, 103 F.3d 1195, 1201 (5th Cir. 1997) . . . .
>
> Under both the Bankruptcy Code and Texas law, the intent to hinder or delay or defraud are three separate elements. Each one on its own may make a transfer fraudulent. *"Thus, an intent merely to delay, but not ultimately prevent, a creditor from being repaid is generally sufficient to trigger the requisite culpability required by the statute."* 5 Collier on Bankruptcy ¶ 548.04[1], pp. 548-22 to 548-24 (rev. 15th ed. 2000) (citing *Shapiro v. Wilgus*, 287 U.S. 348, 53 S.Ct. 142, 77 L.Ed. 355 (1932)(debtor's transfer of all assets to newly formed corporation after creditor threatened to sue, in effort to obtain additional time to repay all creditors as part of scheme to hinder or delay creditors)).

292 B.R. at 262-63 (emphasis added).

"Under § 544(b) the trustee succeeds to the rights of an unsecured creditor in existence at the time of the commencement of the case who can avoid the transfer or obligation under applicable state or local law." 5 COLLIER ON BANKRUPTCY ¶ 544.09[1] at 544-17 (15th ed. rev. 2005). In *Stalnaker v. DLC, Ltd. (In re DLC, Ltd.)*, 295 B.R. 593, 602 (B.A.P. 8th Cir. 2003), the court stated:

> Simply put, it is the trustee's responsibility to: (1) identify an existing creditor; (2) with an allowable claim; (3) who under non-bankruptcy law could avoid the transfer, at least in part. Once the trustee

> has proven his case, the trustee, pursuant to *Moore v. Bay*, 284 U.S. 4, 52 S.Ct. 3, 76 L.Ed. 133 (1931), as interpreted, may: (4) avoid the entire transfer (even if the creditor upon whom the trustee relies could avoid it only in part); and (5) if necessary, recover the property transferred or its value under 11 U.S.C. § 550(a).

See also In re Leonard, 125 F.3d 543, 546 (7th Cir. 1997).

Under the foregoing authorities, the Employee Committee need only show, by a preponderance of the evidence, that there were unsecured creditors of Enron and ENA when the transfers to Defendants were made, *i.e.*, the last business day before Enron file for bankruptcy. The record is replete with credible evidence to such effect including:

(1) The bankruptcy schedules in evidence show such creditors. *See* Ex. 1303; *see also* Exs. 1301, 1305, 1317, 1318.

(2) All of the traders have consistently testified that their trading counterparties were concerned about getting paid and were refusing to extend additional credit.

(3) Employment-related claims were filed by Timothy Belden. *See* Ex. 405 (Proof of claims were filed in both the ENE and ENA bankruptcy cases.).

(4) Defendant Lawrence May testified that he did not think he would collect any money promised him by Enron and would expect that Enron's trade creditors would share his view. (Trial Tr. at 131-32, Sept. 13, 2005.) "I just felt like chances are if they declared bankruptcy, that I would be in the cue [sic] with the rest of the creditors." *Id.* at 135.

(5) Board minutes from November 28, 2001, show Kenneth Lay, Enron Chairman and CEO, recommending that a press release be issued that Enron would not be paying previously declared dividends and that such a release would be consistent with the Board's "previous decision to selectively pay bills and obligations . . . [to] maximize the value of the Company." (Ex. 60 at 10.)

(6) Louise Kitchen, Chief Operating Officer of ENA at the time of bankruptcy, recorded in her diary of the days leading up to bankruptcy. For Wednesday, November 28, 2001, she wrote: "Lots of people come and see me for payments--we are not paying anyone! . . . All cash stops going out." Ex. 160 at ECTe049955536-37. On November 29, 2001, she observed that "[n]o-one will get paid from now on . . . . We were supposed to get paid today and we did not--no surprizes [sic] there . . . ." *Id.* at ECTe049955537-38.

(7) In a presentation to its bankers dated November 19, 2001, Enron stated under the heading "What Happened? Current Situation" that "[c]urrent maturities greatly exceed operating cash flow." (Ex. 260 at 4)(identical to Ex. 1142).

(8) Excerpts from the disclosure statement in the main bankruptcy case indicate that ENA's general unsecured creditors are in line to recover 20.1 cents on the dollar, and ENE's general unsecured creditors are in line to recover 17.4 cents on the dollar. *See* Ex. 406 at 33.

A. The Payments Made Were Made with Actual Intent to Hinder or Delay Creditors Within the Meaning of 11 U.S.C. § 548(a)(1)(A) and TUFTA § 24.005(a)(1)

There was undisputed evidence of intent to hinder or delay. The payments were made in direct anticipation of the imminent filing of the Enron bankruptcy and to avoid the perceived delays in timely obtaining authority from the bankruptcy court, if any such authority could be obtained, to (1) pay bonuses and (2) pay bonuses in such large amounts. Individual bonuses paid to most of the Arnold Defendants were larger than those paid to similarly skilled Enron employees or to the same employees in 2000 which was previously believed to be Enron's best year.

When payments were requested and distributed, Enron knew it was going to file bankruptcy immediately thereafter. *See* Jones Dep. 192, 204, Mar. 30, 2005; Kitchen Dep. 219-22, Feb. 17, 2005; Oxley Dep. 233-34, Mar. 7, 2005; Swerzbin Dep. 58, May 18, 2005; *see also* evidence discussed *supra*. Enron's management was unwilling to allow Enron's creditors and the bankruptcy court the right to participate in any decision concerning how Enron spent the $104 million three days before the bankruptcy. Thus, the bonuses were placed outside the advance scrutiny of the creditors and the bankruptcy court. "When a debtor acknowledges transferring property with the intent of placing it beyond the reach of creditors, he demonstrates 'an actual intent to hinder or delay a creditor.'" *In re Thomas*, 172 B.R. 673, 675 (Bankr. M.D. Fla. 1994)(citing *First Beverly Bank v. Adeeb (In re Adeeb)*,

787 F.2d 1339, 1343 (9th Cir. 1986)).

State law is the same. Under Texas law, "[a] fraudulent transfer is a transfer by a debtor with the intent to hinder, delay or defraud his creditors by placing the debtor's property beyond the creditor's reach." *Flores v. Robinson Roofing & Constr. Co., Inc.* 161 S.W.3d 750, 754 (Tex. App. Forth Worth 2005)(citing *Nobles v. Marcus*, 533 S.W.2d 923, 925 (Tex. 1976); *Coleman Cattle Co., Inc. v. Carpentier*, 10 S.W.3d 430, 433 (Tex. App. Beaumont 2000)).[33]

Either intent to defraud or to hinder or to delay suffices.

> Under both the Bankruptcy Code and Texas law, the intent to hinder or delay or defraud are three separate elements. Each one on its own may make a transfer fraudulent. "Thus, an intent merely to delay, but not ultimately prevent, a creditor from being repaid is generally sufficient to trigger the requisite culpability required by the statute."

In re Brentwood Lexford Partners, LLC, 292 B.R. at 262-63 (quoting 5 COLLIER ON BANKRUPTCY ¶ 548.04[1] at 548-22 to 548-24 (15th ed. rev. 2000) (citation omitted)).

Intent to hinder, delay or defraud may be established by circumstantial evidence. *See Hibernia Nat'l Bank v. Perez (In re*

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[33] Choice of law is not an issue in this case because "there is a presumption that another state's law is the same as Texas." 12 TEXAS JUR.3D *Conflict of Laws* § 8 at 848 (2004) (citing *Excess Underwriters at Lloyd's v. Frank's Casing Crew & Rental Tools, Inc.,* 93 S.W.3d 178 (Tex. App. Houston 14th Dist. 2002), *review granted*, (Apr. 3, 2003); *In re Estate of Garcia-Chapa*, 33 S.W.3d 859 (Tex. App. Corpus Christi 2000); *Braddock v. Taylor*, 592 S.W.2d 40 (Tex. App. Beaumont 1979), *writ refused n.r.e.*, (Mar. 26, 1980); *Brand v. Eubank*, 81 S.W.2d 1023 (Tex. App. Texarkana 1935), *writ dismissed*). "Absent proper invocation of foreign law by pleading and proof, Texas courts presume the foreign law to be the same as Texas law." *Id.* (footnotes omitted).

Perez), 954 F.2d 1026, 1028 (5th Cir. 1992) (affirming bankruptcy court's finding based on circumstantial evidence that property was transferred "with the intent to, if not defraud [debtor's] creditors, at least hinder or delay their discovery of and access to certain assets")*; First Tex. Sav. Ass'n, Inc. v. Reed (In re Reed),* 700 F.2d 986, 991 (5th Cir. 1983).

In an *en banc* decision, the Third Circuit has opined in dicta, in reference to Enron specifically with respect to bonuses of this nature:

> Before bankruptcy, a debtor's management and its most powerful creditors typically try to "work out" the debtor's financial distress. In this process, managers frequently experience pressure to take extreme measures to protect the company. They may make extraordinary concessions to providers of critical services, such as . . . committing to lavish retention bonuses, or doing virtually anything else to avoiding filing for bankruptcy. Whether or not these radical actions are ultimately successful, they often reduce the assets available to the debtor's creditors.
>
> The Bankruptcy Code's avoidance powers are intended, *inter alia*, to deter this kind of managerial overreaching . . . .

Official Comm. of Unsecured Creditors of Cybergenics Corp. v. Chinery, 330 F.3d 548, 572-73 (3d Cir. 2003)(en banc)(internal citations omitted).

When a transfer is made with requisite intent under 11 U.S.C. § 548(a)(1), there is no need to address reasonably equivalent value under § 548(B)(i) or insolvency under § 548(B)(ii). *See* 5 COLLIER ON BANKRUPTCY ¶ 548.03 at 548-31 to 548-

32 (15th ed. rev. 2000).[34]

B. 11 U.S.C. 548(c) and the Arnold Defendants' Knowledge of Enron's Insolvency and Imminent Bankruptcy

11 U.S.C. § 548(c) provides:

> *Except to the extent that a transfer or obligation voidable under this section is voidable under section 544, 545, or 547 of this title, a transferee or obligee of such a transfer or obligation that takes for value and in good faith has a lien on or may retain any interest transferred or may enforce any obligation incurred, as the case may be, to the extent that such transferee or obligee gave value to the debtor in exchange for such transfer or obligation.*

(emphasis added).

Defendants contend that they accepted the bonuses for value and in good faith, citing in defense § 548(c) and TUFTA § 24.009(a). In their trial brief at page 31, Defendants expressly contend:

> Pursuant to section 548(c)(2) [sic - apparently referring to § 548(c) only] of the Code, a defendant who took a transfer in good faith and who gave value has a lien or may retain that transfer to the extent of the value given. For purposes of determining value under section 548(c), the approach shifts, from that of the recipient of "value" to that of the transferee. Any actual or constructive fraudulent motive on the part of the transferor under section 548(a) becomes irrelevant. Instead, the section 548(c) analysis examines that which transferees gave up, in consideration of that party's state of mind and point of view, to show that they took in good faith and in exchange for value. *In re Hannover Corp.*, 310 F.3d 796, 799 (5th Cir. 2002). The courts do not define "good faith," given that "[t]he unpredictable

[34] While the court has found debtor insolvent at the time of the transfers, "the existence of insolvency at the time of the challenged transfer does not necessarily prove the intent requisite under § 548(a)(1)(A)." 5 COLLIER ON BANKRUPTCY ¶ 548.04[3] at 548-32.

> circumstances in which the courts may find its presence or absence render any definition of 'good faith' inadequate, if not unwise." 5 COLLIER ON BANKRUPTCY ¶ 548.07[2][a].
>
> If the transferees meet the Section 548(c) standards, there is no need to engage in the Section 548(a) analysis of whether or nor the transfers were actually or constructively fraudulent. *Hannover*, 310 F.3d 796, 799. Rather, the Section 548(c) defense is specifically designed to protect transferees. *Hannover,* 310 F.3d 796, 802.

However, the court has already found that the transfers to Defendants are voidable under § 547, therefore, by express exclusion, § 548(c) does not furnish a defense to Defendants nor does 11 U.S.C. § 550 furnish any defense to Defendants. Thus, if this court's § 547 findings are upheld, then Plaintiff would be able to recover the transfers under both §§ 547 and 548(a)(1)(A) since § 548(c) would furnish no defense.

In the interest of judicial economy the court will address § 548(c) in the alternative and as a possible defense to defendants only if this court's § 547 findings are reversed on appeal. Under such circumstances only, it appears that the *Hannover* court's approach is as follows:

> With 11 U.S.C. § 548(c), Congress provided to transferees a defense against a trustee's (or debtor's) successful demonstration of an actual or constructive fraudulent transfer under, respectively, § 548(a)(1)(A) and § 548(a)(1)(B) of the Bankruptcy Code. 11 U.S.C. § 548(c) states in pertinent part: "[A] transferee or obligee of such a transfer or obligation that *takes for value* and in good faith has a lien on or may retain any interest transferred . . . to the extent that such transferee or obligee gave value to the debtor in exchange for such transfer or obligation." *The burden of proof is on the defendant transferee. See In re M &*

> *L Bus. Mach. Co., Inc.*, 84 F.3d 1330 (10th Cir. 1996); *In re Agric. Research & Tech. Group*, 916 F.2d 528 (9th Cir. 1990). To avail himself of this defense, the transferee must demonstrate that he "[took] value in good faith." To keep what he received, he must subsequently demonstrate that he "gave value."

Jimmy Swaggert Ministries v. Hayes (In re Hannover Corp.), 310 F.3d 796, 799-800 (5th Cir. 2002)(emphasis added). The court continued:

> Read in combination, §§ 548(a) and (c) are perfectly complementary. The first section affords creditors a remedy for the debtor's fraudulence or, as the case might be, mere improvidence; the second protects the transferee from his unfortunate selection of business partners. *See Fairchild,* 6 F.3d at 1126-27 (rejecting the proposition that "anyone who provides, deals with, or invests in an entity in financial straits would be doing so at his or her peril under § 548"). Each party can make a claim for cure, but only to the extent it was harmed.

Id. at 802-3.

As the *Hannover* court stated:

> As courts and commentators frequently note, the bankruptcy code does not define "good faith" and the statute's legislative history is quite thin. Moreover, there is little agreement among courts as to what conditions ought to allow a transferee this defense. This is not surprising, as the variables are manifold.
>
> The most important set of questions concerns the transferee's state of mind. *First, what level of knowledge--knowledge itself or some form of notice--vitiates a claim of "good faith"? Second, need the knowledge be actual or merely constructive? Third, what duty of inquiry does notice impose?*
>
> *The first set of questions begs the second: Knowledge of what? Of the transferor's insolvency, fraudulence, or both? If insolvency, then of what degree--actual, imminent, or potential? If fraudulence, then regarding what transactions--the*

> *enterprise involving the transferee or any of the transferor's dealings?*

Id. at 800 (internal citations omitted)(emphasis added). As the foregoing quotation from *Hannover* indicates, the courts do not define good faith given the unexpected variables that can be encountered.

The *Hannover* court discussed the good faith findings of the bankruptcy court which were upheld on appeal. *Id.* at 799-800. The court stated that the trial court found that the transferee, unlike the present case before this court, had no knowledge of the transferor's insolvency. *Id.* at 800. Upon reading of the transferor's fraudulent activities in the newspapers, it contacted the SEC and the district court and received assurances from the district court that it could continue to take option payments from the debtor. *Id.* The Fifth Circuit affirmed the bankruptcy court on its findings that the transferee thus acted in good faith within the meaning of § 548(c). *Id.* at 799-800.

When the Arnold Defendants received their November 29, 2001 contracts concerning early payment of 2001 bonuses, it appears that the Arnold Defendants remaining in this litigation knew of the imminent expected bankruptcy filing of Enron, and the fact that in all likelihood they were receiving payments that other creditors of Enron would not receive.

On Wednesday, November 28, 2001, Enron announced in a press release the termination of the Dynegy merger and that it was

suspending all payments other then those necessary to maintain core operation. *See* Ex. 671. The testimony showed that information was commonly shared among the Trading Group.

Supra in this opinion in the insolvency discussion, the court referred to Louise Kitchen's testimony about a meeting on November 28, 2001 in which "we tell everyone that it looks like bankruptcy," *i.e.*, traders were told of Enron's imminent bankruptcy. (Kitchen Dep. 222:9-10, Feb. 17, 2005.) Further, at or about November 28, 2001, it appears the remaining Arnold Defendants knew of Enron selectively paying creditors and of the substantial shut down of its trading desks because of inability to obtain capital.

As noted in the *Hannover* opinion, a defendant has the burden of proof on good faith and value under 11 U.S.C. § 548(c). 310 F.3d at 800.

The Lavorato Defendants remaining in the case did not offer any testimony or proof concerning good faith or value, therefore, they presented no § 548(c) defenses or any TUFTA § 24.009 defense.

While there is evidence in the record about Enron's questionable trading practices, tax schemes, and improper manipulation of accounting, there was insufficient evidence of any of the remaining defendants' intentional participation in such improper or illegal activities ("fraudulence") on behalf of Enron.

C. Conclusion on Good Faith Under 11 U.S.C. § 548(c)

For the reasons stated *supra*, there was insufficient evidence of the remaining Arnold Defendants taking such transfers in good faith under § 548(c). Therefore, § 548(c) would not be available as a defense to them.

IX. FURTHER ADDITIONAL OR ALTERNATIVE FINDINGS

As previously stated, § 548(c) is not available to Defendants as a defense because first, the court found Defendants received a preference, and second, Defendants did not prove a good faith defense under § 548(c) or the extent of any alleged value given.

Additionally, since the court found *supra* that Plaintiff proved the transfers were avoidable under § 548(a)(1)(A), it was unnecessary to reach § 548(a)(1)(B)(i), *i.e.*, the rule of "conclusive fraud." *See* 5 COLLIER'S ON BANKRUPTCY ¶ 548.05[3] at 548-48.

In order to complete the record, in the event of any reversal of the foregoing findings, the court makes the following additional findings.

Reasonably equivalent value under § 548(a)(1)(B)(i) is not defined in the Bankruptcy Code. Value is defined in § 548(d)(2) as "property, or satisfaction or securing of a present or antecedent debt of the debtor, but does not include an unperformed promise to furnish support to the debtor or to a relative of the debtor . . . ." Courts have struggled to come up

with a workable definition of reasonably equivalent value. In *Mellon Bank, N.A. v. Official Committee of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.)*, 92 F.3d 139, 148 (3d Cir. 1996), the court held that "the mere 'opportunity' to receive an economic benefit in the future constitutes 'value' under the Code."

The documentary evidence, in particular the October 2001 amendments, the November 17, 2001 memoranda, the November 29, 2001 memoranda, and the Performance Bonus Trust, all refer to the bonuses as performance bonuses. In addition, Defendants' expert, Mr. Goldstein, testified that if the bonuses were 100% performance bonuses, the giving of such bonuses would have been an unjustified action by the Enron Board.

States that have adopted the UFTA interpret it similarly to § 548(a)(1)(B)(i). *See Hinsley v. Boudloche (In re Hinsley)*, 201 F.3d 638, 643 (5th Cir. 2000) (discussing TUFTA § 24.005(b)(8) "reasonably equivalent" value received by debtor under TUFTA's badges of fraud).

Value is to be determined at the time of payment and not by hindsight. *See In re Hannover*, 310 F.3d at 802-3. Reasonably equivalent value is largely a question of fact, *Gaudet v. Babin (In re Zedda)*, 103 F.3d 1195, 1206 (5th Cir. 1997), although in certain instances, usually applying § 548 to prior state court determinations, it can be a matter of law. *See Ingalls v. Erlewine, (In re Erlewine)*, 349 F.3d 205, 209 (5th Cir. 2000).

A. Enron Received Less Than Reasonably Equivalent Value for the Transfers in Question Within the Meaning of 11 U.S.C. § 548(a)(1)(B)(i) and TUFTA § 24.006(a) and Was Insolvent at the Time of the Transfers Under 11 U.S.C. § 548(a)(1)(B)(ii) and Within the Meaning of TUFTA §§ 24.003(b) and 24.006(a)

As of late November 2001, it was obvious to defendants and Enron that Enron's 2001 profits, if any, from which to pay any 2001 bonuses would be significantly lower than in prior years or non-existent.[35] As of November 29, 2001, the Arnold Defendants were aware of Enron's imminent bankruptcy. Generally, the November 29, 2001 bonuses paid were substantially higher than those paid in February 2001 for the year 2000, previously believed to be Enron's best year to date. *See* Appendix 1 hereto. The November 29, 2001 bonus memorandums state they are "for calendar year 2001 performance."

During this time, chaos was reigning at Enron. The bonuses were paid prior to the events they acknowledged. The active Arnold Defendants contended that the bonuses were mainly for retention. However, the November 29, 2001 bonus memoranda required staying only until February 29, 2002, or ninety days. During that ninety days, nothing prevented such defendants from negotiating for a contract with another company to be effective March 1, 2002. If the ninety days were evaluated on an annualized basis, it would then mean, for example, in Mr. Swerzbin's case, having received a $2,600,000 bonus because of

[35] Normally Enron would use approximately twenty-five percent of after tax 2001 income, payable in early 2002, as a pool for all bonuses.

his November 29, 2001 memorandum, the same would be equivalent to a $10,400,000 annualized retainer bonus or approximately $866,667 per month for three months.

The bonus memorandums were higher than suggested by Towers Perrin or market data.

There was credible testimony from Mr. Longnecker that normally retention bonus agreements should be for longer than ninety days, and a retention bonus agreement for ninety days should be lower than performance bonuses. He further credibly testified that performance bonuses should not go up when performance goes down.

In October 2001, many of the bonus recipients had agreed to receive lower amounts in February 2002 and such amounts were dramatically raised on November 29, 2001 without any negotiation and to be paid immediately. The ninety day retention period was unusually short.

Defendants failed to prove under 11 U.S.C. § 548(c) or TUFTA 24.009(d)(1)(C) the amount of value they gave to Enron in exchange for the transfers they received.

Defendants failed to prove any defense under TUFTA § 24.009(a), (b)(1), (d)(1)(C), or otherwise. Under TUFTA § 24.005(b)(1), as indicated by Appendix 1 hereto, most of the transfers were to insiders. Under TUFTA § 24.005(b)(3), per the November 29, 2001 memoranda, Defendants were not to discuss the transfers with others than family and legal counsel. *See, e.g.,*

Ex. 63 ¶ 3.

Plaintiff is additionally entitled to recover the bonuses paid to Defendants under 11 U.S.C. § 548 and TUFTA.

Judgments will be entered in the Arnold Adversary in accordance with the foregoing opinion.

None of the following Lavorato Defendants actively participated in the trial. The following Defendants were served, filed no answer, and thereby admitted November 29, 2001 preference and fraudulent transfer claims in the following amounts:

Defendant	Bonus Amount
Fang Tzu Chang	$12,000
Paul Garcia	25,000
Anamarie Hernandez	5,000
Matthew Lenhart	18,000
Kori Loibl	12,000
Peter Makkai	18,000
Robert Richey	40,000
Shawana Simon	20,000
Stephen Stock	70,000
Karen Williams	12,000

The following defendants were served, filed answers admitting executing November 29, 2001 memoranda and receiving the following November 29, 2001 bonus amounts:

Defendant	Bonus Amount
Sally Beck	$350,000
Michelle S. Bruce[36]	45,000

[36] Ms. Bruce filed a general denial. "A general denial is not sufficient, but must be answer to sifting inquiries upon the general question." *Hinkle v. Wanzer*, 58 U.S. 353, 355 (1854); *see Provident Life and Accident Ins. Co. v. Goel*, 274 F.3d 984, 994 (5th Cir. 2001) ("[A] general denial in an original pleading is insufficient to create an issue of material fact."); *Ralston Oil and Gas Co v. Gensco, Inc.*, 706 F.2d 685, 692 (5th Cir. 1983) (Supplier's general denial that company was entitled to any recovery deemed insufficient to raise question of company's capacity to recover.

Tandra A. Coleman	9,500
Whitney S. Fox	50,000
Mark H. Frank	50,000
Jozef S. Lieskovsky	10,500
Omar C. Peck	50,000
David J. Ryan	75,000

Such defendants did not participate in the trial and the foregoing preference and fraudulent transfer claims were proved up against them by the evidence offered at trial.

Judgements will be entered against the remaining Lavorato Defendants in accordance with the foregoing opinion.

###END OF MEMORANDUM OF DECISION###

"Gensco states that it satisfied the Rule 9(a) requirements generally denying that Ralston was entitled to any recovery. Were this sufficient to raise the question of capacity, Rule 9(a) would be rendered superfluous.).

Appendix 1

Name	Gross Amount	Position/Title in 2001	2000 Performance Bonus	Oct. 25 Memo (To be paid on or before Feb. 15, 2002)	Nov. 17 Memo & Termination of Oct. 25 Memo	Nov. 29 Memo
Michael J. Swerzbin	$2,600,000	V.P. E.N.A.	$2,000,000 cash $2,000,000 equity	$1,500,000 Ex. 601r	$1,300,000, 1/4/02 $1,300,000, 2/5/02 Exs. 602p, 603q	Ex. 604x
Matthew H. Motley	$2,300,000	Director, West Power Trading Desk, E.N.A.	$400,000 cash $400,000 equity	$1,300,000 Ex. 601n	No	Ex. 604r
Kevin M. Presto	$2,000,000	V.P., Head of East Power Trading Group	$500,000 cash $500,000 equity	$1,200,000 Ex. 601o	$1,000,000, 1/4/02 $1,000,000, 2/5/02 Exs. 602m, 603n	Ex. 604t
Mark Dana Davis, Jr.	$1,800,000	Head, Northeast Power Desk (East Power Trading Group)	$400,000 cash $400,000 equity	$1,000,000 Ex. 601g	$900,000, 1/4/02 $900,000, 2/5/02 Exs. 602f, 603g	Ex. 604i
Robert C. Benson	$1,750,000	Director, East Power Trading Desk	$150,000 cash $50,000 equity	$1,000,000 Ex. 601d	$875,000, 1/4/02 $875,000, 2/5/02 Exs. 602c, 603d	Ex. 604e
Fletcher J. Sturm	$1,750,000	Head, Midwest Power and Southeast Power Desks (East Power Trading Group)	$1,000,000 cash $1,000,000 equity	$1,200,000 Ex. 601q	$875,000, 1/4/02 $875,000, 2/5/02 Exs. 602o, 603p	Ex. 604w

Name	Gross Amount	Position/Title in 2001	2000 Performance Bonus	Oct. 25 Memo (To be paid on or before Feb. 15, 2002)	Nov. 17 Memo & Termination of Oct. 25 Memo	Nov. 29 Memo
Robert Badeer	$1,300,000	Director, Long-Term CA Desk (West Power Trading Group)	$120,000 cash $50,000 equity	$600,000 Ex. 601b	$650,000, 1/4/02 $650,000, 2/5/02 Exs. 602a, 603b	Ex. 604b
Frank J. Ermis	$850,000	Risk Analyst for E.N.A.	$200,000 cash $200,000 equity	$500,000 Ex. 601h	$425,000, 1/4/02 $425,000, 2/5/02 Exs. 602g, 603h	Ex. 604j
Lawrence J. May	$850,000	Director of Trading	$200,000 cash $200,000 equity	$350,000 Ex. 601m	$425,000, 1/4/02 $425,000, 2/5/02 Exs. 602*l*, 603m	Ex. 604q
Andrew H. Lewis	$650,000	Director of Trading	$200,000 cash $200,000 equity	$400,000 Ex. 601k	$325,000, 1/4/02 $525,000, 2/5/02 Exs. 602j, 603k	Ex. 604o
Barry L. Tycholiz	$650,000	V.P. E.N.A., Origination Wholesale	$175,000 cash $150,000 equity	$350,000 Ex. 601t	$325,000, 1/4/02 $325,000, 2/5/02 Exs. 602q, 603s	Ex. 604z
Kevin Ruscitti	$325,000	Manager of Natural Gas Trading for the Midwest Desk of E.N.A.	$100,000 cash $25,000 equity	No	Per his testimony, it appears he signed a Nov. 17 memo., but Plaintiff failed to produce such document.	Ex. 919a

Name	Gross Amount	Position/Title in 2001	2000 Performance Bonus	Oct. 25 Memo (To be paid on or before Feb. 15, 2002)	Nov. 17 Memo & Termination of Oct. 25 Memo	Nov. 29 Memo
Bradley T. McKay	$300,000	Director, Northeast Basis of E.N.A.	$200,000 cash	No	No	Ex. 512
Douglas Gilbert-Smith	$275,000	Director of Trading of ENA	$125,000 cash $25,000 equity	No	$137,500, 1/4/02 $137,500, 2/5/02 Ex. 513 (only signed by Enron)	Ex. 916e
Laura L. Luce	$250,000	V.P., E.N.A.	$180,000 cash $200,000 equity	No	No	Ex. 516
Craig A. Breslau	$200,000	V.P., E.N.A.	$165,000 cash $35,000 equity	No	No	Ex. 515