UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

IN RE WORLDCOM, INC. SECURITIES LITIGATION	:	MASTER FILE 02 Civ. 3288 (DLC)
This Document Relates To: All Actions	:	

REPLY MEMORANDUM OF LAW OF H. CARL McCALL, COMPTROLLER OF THE STATE OF NEW YORK, AS ADMINISTRATIVE HEAD OF THE NEW YORK STATE AND LOCAL RETIREMENT SYSTEMS AND AS TRUSTEE OF THE NEW YORK STATE COMMON RETIREMENT FUND, IN FURTHER SUPPORT OF THE NYSCRF'S MOTION FOR AN ORDER PARTIALLY LIFTING THE PSLRA DISCOVERY STAY

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H. Carl McCall, Comptroller of the State of New York, as Administrative Head of New York State and Local Retirement Systems and as Trustee of the New York State Common Retirement Fund, the Court-appointed Lead Plaintiff in the above-captioned action (the "NYSCRF" or "Lead Plaintiff"), respectfully submits this reply memorandum of law in further support of the NYSCRF's motion for an order partially lifting the PSLRA discovery stay.[1]

Preliminary Statement

At the November 18, 2002 conference concerning the ERISA Litigation, the Court stated that all concerned should presume that document discovery will soon proceed "full throttle" in both the ERISA and Securities Litigations. While the authorities cited in the NYSCRF's opening brief – and the unique circumstances of this case – underscore the wisdom of proceeding expeditiously with that plan, certain Defendants in the Securities Litigation have predictably opposed any lifting of the PSLRA discovery stay, partial or otherwise.[2] However, there is nothing in their papers that should persuade the Court to proceed differently. Defendants ignore the facts of *this particular case*, and instead ask the Court to treat this litigation as if it were an ordinary, everyday run-of-the mill securities case. It is not.

There is no dispute that this is an admitted fraud – the largest accounting fraud in history, with four senior WorldCom officers already having pled guilty to securities fraud – and that massive discovery in this action is inevitable. The documents that Lead Plaintiff seeks by this motion are the

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[1] All capitalized terms not otherwise defined here shall have the meaning given to them in Lead Plaintiff's opening brief ("Opening Br."). References to the "Securities Litigation" are to the above-captioned matter. References to the "ERISA Litigation" are to *In re WorldCom, Inc. ERISA Litigation*, 02 Civ. 4816 (DLC).

[2] The Director Defendants submitted a brief in opposition to Lead Plaintiff's motion, which the Underwriter-Related Defendants have joined in pursuant to letter dated November 18, 2002. Arthur Andersen also has opposed Lead Plaintiff's motion. All references here to "Def. Br." are to the brief filed by the Director Defendants.

same documents which WorldCom has already produced in connection with the various governmental and internal investigations of the very fraud at issue in this case, and they can be produced to Lead Plaintiff expeditiously, with no discernable burden on WorldCom (as the Bankruptcy Court has already ruled) and no burden whatsoever on any Defendant. Further, the U.S. Attorney's Office, which is prosecuting Defendant and former WorldCom Chief Financial Officer Scott Sullivan for securities fraud and is continuing its investigation as to others, has advised Your Honor in writing that "the Government has no objection to *full* document discovery from WorldCom at this time." (Emphasis added). That November 15 letter from the Government is utterly ignored by Defendants.

The facts that are beyond dispute and unique to this case warrant lifting the PSLRA discovery stay. As the court in In re Enron Corp. Sec. Litig. explicitly recognized just three months ago in circumstances virtually identical to these, the PSLRA discovery stay was *not* intended to apply in such circumstances, that is, where the fraud is undisputed and the documents being sought have already been produced – where "[i]n a sense this discovery has already been made" to every party-in-interest but the lead plaintiff in the securities case. See In re Enron Corp. Sec., Deriv. & ERISA Litig., No. H-01-3624 (S.D. Tex. 2001), Order dated August 16, 2002, Coffey Decl. Ex. E at 3.

In addition, Lead Plaintiff has established sufficient undue prejudice. Defendants do not take issue with the definition of "undue prejudice," which merely requires a showing of "improper or unfair treatment" and falls far short of a demonstration of irreparable harm. Rather, Defendants contend that simply because the Government has access to these documents does not mean that the putative Class would suffer unfair treatment. However, it is not only the Government which has access to these (and other) documents, but private parties-in-interest, including the Creditors' Committee, Wilmer Cutler & Pickering, and the Bankruptcy Court-appointed Examiner. Indeed, it is now apparent that another

significant private constituency – the plaintiffs in the ERISA Litigation – will have access to these and other documents, as well they should. If, as this Court has stated, the ERISA and Securities Litigations are truly to proceed in tandem, then Lead Plaintiff should be afforded the same access to documents. But as Defendants would have it, the only party-in-interest who would not have access to these documents is Lead Plaintiff, solely because of the "strictures of a statute" that was designed to prevent frivolous cases from being filed. Enron, August 16 Order at 1-3, Coffey Decl. Ex. E. That is the very definition of unfair treatment.

Finally, now that the Court has ordered the parties to conduct settlement negotiations – yet another circumstance that readily distinguishes this case from any other – it is even more imperative that the PSLRA discovery stay be modified to allow for production of the documents requested here. Indeed, Defendants' brief actually underscores the need for prompt production of the requested documents, since it is now apparent that these Defendants will dispute liability in the course of settlement discussions. Consequently, Lead Plaintiff respectfully submits that if such settlement discussions are to be meaningful, Lead Plaintiff needs at least the discovery requested here.

In sum, this is a unique case, with an even more compelling basis for relief than there was in Enron. There is no good reason not to allow discovery to proceed, and many good reasons to move forward without further delay. Lead Plaintiff's motion should be granted.

ARGUMENT

I. The Discovery Stay Does Not Apply To This Case

As set forth in Lead Plaintiff's opening brief, where, as here, there is an admitted fraud and the documents at issue have already been produced to others, the PSLRA discovery stay does not apply. See Enron, August 16 Order at 1-3, Coffey Decl. Ex. E (ordering production of documents Enron had

produced to the Government and others investigating the fraud notwithstanding the fact that motions to dismiss were pending). In that case, Judge Harmon recognized that the PSLRA discovery stay was designed to "prevent fishing expeditions in frivolous securities lawsuits" and to eliminate the risk that a defendant would be forced to settle a meritless case simply to avoid the costs of discovery. Id. Indeed, as Lead Plaintiff noted in its brief, this case is an even stronger case than Enron for lifting the stay because here, unlike in Enron, senior corporate officers have already pled guilty to the fraud. There can be no dispute that a fraud was perpetrated at WorldCom.

Defendants do not, and could not, argue that any of the concerns Congress articulated in enacting the discovery stay are implicated here. Defendants do not contend that this is a frivolous case, or that they will be burdened if WorldCom is allowed to produce the documents Lead Plaintiff has requested, or that they will be pressured to settle if discovery is allowed. And Defendants do not, and could not, distinguish the facts of Enron from this case. Instead, Defendants consign their discussion of Enron to a footnote, where their analysis is simply that Judge Harmon was "wrong." Def. Br. at 4, n. 4. Lead Plaintiff respectfully submits that Judge Harmon's order was well-founded, in complete harmony with the intent of the PSLRA, and is ample precedent for the relief sought by Lead Plaintiff here.

Defendants contend that the cases upon which Lead Plaintiff relies stand for the proposition that "a securities complaint must be determined by a court to be adequately pleaded before any discovery is permitted." Def. Br. at 4, n. 4. Even assuming this was an accurate statement of the law – which it is not – there have already been numerous determinations in this District that the allegations of the Complaint state a claim for *criminal* securities fraud. As described in the NYSCRF's opening papers, four of WorldCom's most senior officers, including its Comptroller, have already had their guilty pleas

to securities fraud accepted as factually sufficient by various District Judges in this District. A grand jury sitting in this District concluded that there was probable cause that Defendant Sullivan had committed securities fraud (among other charges). And Magistrate Judge Francis has concluded that a criminal complaint with a fraction of the detail set forth in the NYSCRF's Complaint was sufficient to establish probable cause that a criminal conspiracy to commit securities fraud existed at WorldCom.[3] Defendants say *nothing* about the pleas, indictment and criminal complaint, which of course provide the Court with a much more compelling basis to lift the stay than the record before Judge Harmon in Enron. Taking into account Magistrate Judge Francis' determination alone, the Court can take note that a judicial officer in this District had taken a more difficult standard than required in this civil case – probable cause to conclude whether criminal securities fraud had occurred – applied it to a small sub-set of the allegations in the Complaint, and concluded that the standard was satisfied.

Defendants' failure to address the unique circumstances of this case is matched by their extremely overbroad and untenable reading of the PSLRA. They contend that the language of the PSLRA requires "a complete shutdown of *all* discovery while *any* motion to dismiss is pending." Def. Br. at 2 (italics in original). This is incorrect, as numerous courts have held. See, e.g., In re Lernout & Hauspie Sec. Litig., 214 F. Supp. 2d 100, 107 (D. Mass. 2002); Carlson v. Clarent, Order dated September 9, 01-03361 (CRB) (N.D. Cal. 2002). In Lernout & Hauspie, the court carefully examined the statutory language and rejected this precise argument, holding that the PSLRA may be read to mean that all discovery against a party must be stayed only during the pendency of any motion to dismiss filed by that party:

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[3] Excerpts of the guilty pleas, the indictment and the criminal complaint are referenced in the Complaint.

> A close reading of the statutory provision suggests that its meaning is not as plain as defendants contend. The language "all discovery shall be stayed during the pendency of any motion to dismiss" suggests two competing reasonable interpretations. One, which defendants support, would read "any" as "all," suggesting that no discovery may proceed against any party to an action until all motions by all parties are resolved. The provision could also be read to mean that all discovery against a party must be stayed during the pendency of any motion to dismiss filed by that party.
> I conclude that the provision is ambiguous on its face.

214 F. Supp. 2d at 105. The court then looked to the legislative history of the PSLRA, and concluded that Congress did not intend for discovery to be stayed once the court had determined that the complaint stated a claim. Id. As a result, even before all motions to dismiss were decided, the court allowed certain discovery to go forward.

The cases cited by defendants in support of their contention that all discovery must be stayed are inapposite. For example, in Faulkner v. Verizon Communications, Inc., 156 F. Supp. 2d 384 (S.D.N.Y. 2001), the court *granted* the defendants' motions to dismiss and specifically found that the plaintiffs sought "to lift the [discovery] stay for the sole purpose of uncovering facts to support" the fraud allegations. Id. at 400, 402. Similarly, in In re Carnegie Int'l. Corp. Sec. Litig., 107 F. Supp. 2d 676 (D. Md. 2000), the court held that "the discovery appears to the Court to be nothing more than a fishing expedition ... to obtain evidence that can form the basis of a case" against the company's auditors. Id. at 680. In In re CFS-Related Sec. Fraud Litig., 179 F. Supp. 2d 1260 (N.D. Okla. 2001), a magistrate judge applied the stay to block discovery from a defendant who had not moved to dismiss, because the court had not yet had the opportunity to weigh the allegations of the complaint. These decisions all reflect the intent of the discovery stay – which is to prevent plaintiffs in cases that are highly questionable from engaging in a fishing expedition to discover a claim. That is a far cry from this

case.[4]

Defendants also argue that Lead Plaintiff contends that the discovery stay should not apply because the discovery is sought from WorldCom, which is not a party to this litigation. Def. Br. at 4. That is not correct. Lead Plaintiff does not argue here that the discovery stay distinguishes between discovery sought from parties and non-parties. However, the fact that the production will be made by WorldCom obviates any argument that *defendants* will be burdened if Lead Plaintiff's motion is granted. Defendants here do not, and could not, contend that they will suffer undue burden if this discovery is allowed. And, importantly, the court with jurisdiction over WorldCom – the Bankruptcy Court – has already approved of Lead Plaintiff's obtaining the discovery sought from WorldCom, conditioned only on this Court ruling that such discovery should be allowed.

II. Lead Plaintiff's Discovery Request Falls Within The PSLRA's Undue Prejudice Exception

Contrary to Defendants' contentions, Lead Plaintiff's discovery request falls squarely within the undue prejudice exception of the PSLRA. First, the NYSCRF's discovery request is sufficiently particularized, because it seeks production only of those documents that have already been selected and produced to governmental and other investigatory entities. Second, if Lead Plaintiff's limited discovery request is not granted here, Lead Plaintiff and the Class will suffer undue prejudice, because all other governmental and certain *private* litigants already have, or, will shortly have, access to these materials and documents.

A. Lead Plaintiff's Discovery Is Sufficiently Particularized

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[4] Defendants also rely heavily on the decision in Hilliard v. Black, 125 F. Supp. 2d 1071 (N.D. Fla. 2000). However, while the court in that case continued the stay after denying a motion to dismiss filed by one defendant, the opinion contains no discussion of the statutory provision, and no discussion of the stay beyond the order itself.

Defendants' assertions that Lead Plaintiff's discovery requests are not "tied to allegations in this action" or "are so broad that they are not even defined to particular categories" are specious. Def. Br. at 5. Lead Plaintiff's discovery request here is carefully tailored to meet the requirements of the PSLRA, to address the concerns of the United States Attorney's Office, to ameliorate any potential burden on WorldCom – and to hew closely to the on-point Enron precedent. The documents that Lead Plaintiff seeks are the *same* documents which have already been produced in connection with various investigations of the *same* accounting fraud at WorldCom that forms one of the bases for the NYSCRF's Complaint. Moreover, Lead Plaintiff's discovery request sufficiently defines categories of requested documents because most, if not all, of these documents were produced by WorldCom to governmental entities pursuant to detailed subpoenas or document requests.

Indeed, at least one court has already found that a substantially similar discovery request is sufficiently particularized to justify modification of the PSLRA. See Enron, August 16 Order, Coffey Decl. Ex. E. Defendants fail to distinguish Enron and, more importantly, fail to cite any authority that would support their assertion that Lead Plaintiff's discovery request is not sufficiently particularized. Unlike in Mishkin v. Ageloff, 220 B.R. 784 (S.D.N.Y. 1998), on which Defendants heavily rely, the discovery request here does not seek "open-ended, boundless universe of discovery." Def. Br. at 5. On the contrary, Lead Plaintiff is seeking here production of only those specific documents that had already been produced to various governmental entities. As pointedly observed by the court in Enron, this is a request for discovery that "has already been made." Enron, August 16 Order at 3, Coffey Decl. Ex. E.

B. Lead Plaintiff Has Established Undue Prejudice

Contrary to Defendants' assertion, Lead Plaintiff does not argue that the delay of this action in

itself creates undue prejudice. Def. Br. at 6. Thus, the cases cited by Defendants in support of this proposition are inapposite.[5] Rather, Lead Plaintiff argues that it would be unduly prejudiced if it remained the only party-in-interest that does not have access to the requested documents. Opening Br. at 16-17. Contrary to Defendants' statement that the only other litigants here "are the United States Attorney's Office and the SEC," Def. Br. at 7, there are *numerous* private litigants that have, or, will shortly have, access to these and other documents. As noted above, on November 18, 2002, this Court stated that full document discovery will proceed in the related ERISA Litigation proceeding before Your Honor, which arises from many of the same facts and circumstances as the Securities Litigation. In addition, as noted in the opening brief, WorldCom's creditors, to at least some extent, also have access to these documents. Opening Br. at 17; Coffey Dec. Ex. A at 23. Tellingly, Defendants do not represent that the Creditors' Committee would not be given access to any of the documents at issue if it demanded it.

In a case like this one, where the corporate debtor is bankrupt and numerous other Defendants allegedly do not have sufficient assets to satisfy a judgment, precluding Lead Plaintiff from timely obtaining the same information that other victims of this fraud have will prejudice the Class. Denying Lead Plaintiff access to these documents will cause Lead Plaintiff to fall behind other litigants in prosecuting its claims, and could allow these other litigants to reach a resolution of their claims far more quickly – or on more advantageous terms – than Lead Plaintiff. Any such resolution could certainly significantly deplete one or more Defendants' resources, and could jeopardize any recovery in this case. Thus, in contrast to Defendants' assertions, Def. Br. at 8, the risk of undue prejudice to Lead

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[5] See Def. Br. at 6-7, citing to In re CFS-Related Sec. Fraud Litig., 179 F. Supp. 2d 1260, 1265 (N.D. Okla. 2001) and Sarantakis v. Gruttadauria, 2002 WL 1803750, at *2, *4 (N.D. Ill. Aug. 5, 2002).

Plaintiff here, as in Global Intellicom, is well-defined and substantial, because there is a material risk that even if Lead Plaintiff is ultimately successful, any judgment might never be satisfied.

Finally, Defendants' suggestion that Lead Plaintiff should be able to rely on documents that are already in the public domain in connection with the upcoming Court-ordered settlement negotiations is specious. This Court specifically recognized during the November 5 conference call (and on the conference call in the ERISA Litigation earlier today) that Lead Plaintiff may identify documents that it believes are necessary to conduct meaningful settlement negotiations. Defendants' position with respect to Lead Plaintiff's instant motion makes it clear that at least some Defendants in this action will be contesting liability and arguing that others are responsible for the fraud. In order to meaningfully participate in settlement negotiations with such Defendants and to accurately assess the risks of litigation with respect to these defendants, the NYSCRF must obtain documents relating to the fraud from WorldCom.[6] Lead Plaintiff's current discovery request – in addition to being fully warranted under the PSLRA – will constitute a necessary first step in enabling Lead Plaintiff to successfully conduct the upcoming settlement negotiations on behalf of the Class.

CONCLUSION

For the foregoing reasons and for the reasons set forth in the New York State Common Retirement Fund's opening brief, the Court should grant the New York State Common Retirement Fund's motion for an order partially lifting the PSLRA discovery stay as set forth in the Proposed Order.

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[6] To the extent the NYSCRF will need particularized discovery from such defendants, it will address such requests to Magistrate Judge Dolinger, who, pursuant to this Court's order, will preside over the upcoming settlement discussions.

DATED: New York, New York
November 20, 2002

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CERTIFICATE OF SERVICE

I, Beata Gocyk-Farber, Esquire, hereby certify that a copy of the Notice Of Issuance of Subpoena by Lead Plaintiff, H. Carl McCall, Comptroller of the State of New York, as Administrative Head of the New York State and Local Retirement Systems and as Trustee of the New York State Common Retirement Fund on WorldCom, Inc., was served upon all involved parties by sending a copy of the same, by first-class mail, postage prepaid, to counsel as identified on the attached service list this 21th day of November, 2002.

Dated: New York, New York
November 20, 2002

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Beata Gocyk-Farber