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Our Ref: NY:160365.1

March 17, 2004

## **VIA HAND DELIVERY**

The Honorable Arthur J. Gonzalez  
United States Bankruptcy Judge  
United States Bankruptcy Court  
The Old Customs House  
One Bowling Green  
New York, NY 10004

**Re: Enron Corp. v. J.P. Morgan Securities, Inc., Adv. Proc 03-92677 (AJG);  
Enron Corp. v. Mass Mutual Life Insurance Co. Adv. Proc. 03-92682 (AJG)**

Dear Judge Gonzalez:

Allen & Overy represents The Bond Market Association ("TBMA"), which is a global trade organization that represents approximately 200 brokers, dealers and banks that underwrite, trade and sell fixed-income securities in the U.S. and international markets. TBMA believes that the issues presented in the above-referenced adversary proceeding are of vital importance to the US financial markets. Accordingly, TBMA has filed the enclosed motion seeking leave to file a Brief and Memorandum of Law, as Amicus Curiae (the "Amicus Brief") so that the Court can have the benefit of market's perspective on these vital issues.

We have conferred with Enron's counsel, Frank Oswald and Michael Schatzow, about the filing of the Motion and Amicus Brief. We have also provided copies of both documents to counsel by email. Counsel has indicated to us that Enron is likely to oppose TBMA's Motion. We therefore request that the Court either schedule a telephonic conference to discuss this filing or set the matter for hearing.

Please feel free to contact me if you have any questions concerning this matter.

Respectfully submitted,

Hugh M. McDonald



Enclosure

cc: Frank Oswald, Esq.  
Michael Schatzow, Esq.  
Greg Zipes, Esq.

*The firm is a multinational partnership, including Members of the Bar of the State of New York, Solicitors of the Supreme Court of England and Wales, Members of the Bar of the Netherlands and Foreign Legal Consultants in the State of New York. A list of names of the partners and their professional qualifications is open to inspection at the above office.*

AMSTERDAM ANTWERP BANGKOK BEIJING BRATISLAVA BRUSSELS BUDAPEST DUBAI FRANKFURT HAMBURG HONG KONG  
LONDON LUXEMBOURG MADRID MILAN MOSCOW NEW YORK PARIS PRAGUE ROME SINGAPORE TIRANA TOKYO TURIN WARSAW

UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK

----- X  
In re: : Chapter 11  
: :  
ENRON CORP., et al., : Case No. 01-16034 (AJG)  
: :  
Debtors. : (Jointly Administered)  
: :  
----- X

ENRON CORP., :  
Plaintiff, :  
: :  
v. : Adv. No. 03-92677 (AJG)  
: :  
J.P. MORGAN SECURITIES, INC., et al., :  
Defendants. :  
: :  
----- X

ENRON CORP., :  
Plaintiff, :  
: :  
v. : Adv. No. 03-92682 (AJG)  
: :  
MASS MUTUAL LIFE INSURANCE CO., et al., :  
Defendants. :  
: :  
----- X

**MOTION FOR LEAVE TO FILE "BRIEF AND MEMORANDUM OF LAW OF  
THE BOND MARKET ASSOCIATION, AS *AMICUS CURIAE*, IN SUPPORT OF  
DEFENDANTS' MOTION TO DISMISS THE AMENDED COMPLAINTS"**

---

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Counsel for The Bond Market  
Association

The Bond Market Association ("TBMA") respectfully moves for permission to file the attached "Brief and Memorandum of Law of The Bond Market Association, as *Amicus Curiae*, in Support of Defendants' Motion to Dismiss the Amended Complaints" (the "Amicus Brief"), in support of the motions to dismiss the amended complaints of each of the defendants named in the amended complaints filed by Enron Corp. ("Enron") in the adversary proceedings Enron Corp. v. J.P. Morgan, et al. (Adv. Pro. No. 03-92677) (as amended on December 1, 2003) and Enron Corp. v. Mass Mutual Life Insurance Co., et al (Adv. Pro. No. 03-92682) (as amended on December 1, 2003).

These adversary proceedings seek to avoid and recover various pre-petition payments made in connection with Enron's repurchase of its commercial paper. Enron's claims stand in direct contravention of the safe harbor provisions set forth in the Bankruptcy Code. A ruling upholding plaintiff's position and concluding that commercial paper payments are not protected settlement payments would acutely disrupt the highly liquid commercial paper market in which many of TBMA's members are active participants and upset the advances Congress and other government agencies have made to protect the integrity and efficiency of the U.S. financial markets.

TBMA respectfully seeks to have the views of its members, comprised of approximately 200 brokers, dealers and banks that underwrite, trade and sell fixed-income securities in the U.S. and international markets, heard by this Court. TBMA is uniquely positioned to evaluate and comment on the application of the Code to the commercial paper transactions at issue in this adversary proceeding. Accordingly, TBMA respectfully seeks leave to file its attached Amicus Brief.

Wherefore, TBMA respectfully requests that the Court enter an order granting TBMA permission to file the Amicus Brief and grant such other relief as is just and proper.

Dated: New York, New York  
March 17, 2004

ALLEN & OVERY

By: /s/ Hugh McDonald

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UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK

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Debtors.	:	(Jointly Administered)
	:	
-----	X	
ENRON CORP.,	:	
Plaintiff,	:	
	:	
v.	:	Adv. No. 03-92677 (AJG)
	:	
J.P. MORGAN SECURITIES, INC., <u>et al.</u> ,	:	
	:	
Defendants.	:	
-----	X	
ENRON CORP.,	:	
Plaintiff,	:	
	:	
v.	:	Adv. No. 03-92682 (AJG)
	:	
MASS MUTUAL LIFE INSURANCE CO., <u>et al.</u> ,	:	
	:	
Defendants.	:	
-----	X	

**BRIEF AND MEMORANDUM OF LAW OF THE BOND MARKET  
ASSOCIATION, AS *AMICUS CURIAE*, IN SUPPORT OF DEFENDANTS' MOTION TO  
DISMISS THE AMENDED COMPLAINTS**

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## **STATEMENT OF INTEREST**

Amicus Curiae The Bond Market Association ("TBMA") submits this memorandum in support of the motions to dismiss the amended complaints of each of the defendants ("Defendants") named in the amended complaints filed by Enron Corp. ("Enron") in the adversary proceedings Enron Corp. v. J.P. Morgan, et al. (Adv. Pro. No. 03-92677) (as amended on December 1, 2003, "AC I") and Enron Corp. v. Mass Mutual Life Insurance Co., et al (Adv. Pro. No. 03-92682) (as amended on December 1, 2003, "AC II") (collectively, the "Amended Complaints"). A ruling upholding plaintiff's position and concluding that the pre-petition commercial paper payments at issue are not protected settlement payments would acutely disrupt the highly liquid commercial paper market in which many of TBMA's members are active participants and upset the advances Congress and other government agencies have made to protect the integrity and efficiency of the U.S. financial markets.

TBMA is a global trade organization that represents approximately 200 brokers, dealers and banks that underwrite, trade and sell fixed-income securities in the U.S. and international markets. All of the primary dealers of Treasury bonds, notes and bills, as recognized by the Federal Reserve Bank of New York, are members of TBMA, as are other securities dealers.

Since its inception, TBMA has worked with Congress, the Securities and Exchange Commission, the Federal Reserve Board and the Federal Reserve Bank of New York, state regulators and self-regulatory organizations to foster effective, efficient regulation and to promote the highest levels of professional standards and conduct in their respective segments of the financial markets. TBMA, in collaboration with the Depository Trust & Clearing Corporation ("DTCC"), has also released a white paper detailing issues and recommendations

regarding commercial paper settlement practices.<sup>1</sup> Those practices and the recommendations made in the white paper were designed to prevent the same type of disastrous systemic consequences that a ruling upholding plaintiff's position would cause.

The Amended Complaints present issues that are vitally important to TBMA. TBMA's members are engaged in creating valuable short-term liquidity and working capital for corporations, banks, securities firms and other financial institutions through the commercial paper market. Commercial paper has historically occupied a critical place in the balance sheets of corporate and asset-backed issuers, and the amount of commercial paper outstanding has been steadily increasing over the last ten years. Furthermore, the issuance of commercial paper with very short maturities has increased in the last decade, with approximately \$4.3 trillion in rated one to four day commercial paper issued in 2003.<sup>2</sup> The short-term nature of commercial paper makes it inherently less susceptible to risk and market participants do not expect commercial paper to be as susceptible to the perils of the economy as long-term financing.

A ruling permitting Enron to take back payments on its commercial paper would unsettle well understood market and legal expectations. The financial instability created by a threat to certainty and finality of payment in the commercial paper market would drastically restrict the ability of U.S. corporations and financial institutions to handle short-term liquidity needs in a cost-effective manner and inhibit the growth of the economy. Accordingly, TBMA submits this brief in support of Defendants' motions to dismiss.

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<sup>1</sup> The Bond Market Association & The Depository Trust & Clearing Corporation, Discussion Paper: Issues and Recommendations Regarding Commercial Paper Settlement Practices, March 2003, at <http://www.dtcc.com/ThoughtLeadership/whitepapers/cppaper.pdf>.

<sup>2</sup> Based on Federal Reserve commercial paper statistics derived from data supplied by The Depository Trust Company (DTC). See, Federal Reserve, Volume Statistics for Commercial Paper Indexes, at <http://www.federalreserve.gov/releases/cp/indexstats.htm>.

## SUMMARY OF THE COMPLAINTS

Before Enron filed its bankruptcy petition on December 2, 2001 ("Petition Date"), it periodically took advantage of the inexpensive financing available in the commercial paper markets by issuing and selling commercial paper to various entities. AC I ¶ 134; AC II ¶ 93. Various financial institutions which have been made parties to this litigation served as dealers for Enron's commercial paper program, and at various times acted as intermediaries and for their own account as market makers. See, e.g., AC I ¶ 138. Approximately one month before the Petition Date, Enron borrowed from its committed bank lines to effect a broad market purchase program to buy back its outstanding and expiring commercial paper. See AC I ¶ 138; AC II ¶ 97. In a series of transactions from October 26, 2001 through November 6, 2001, Enron bought its outstanding commercial paper from the Defendants in this litigation. See AC I ¶ 38; AC II ¶ 97. Enron seeks to avoid, and recover from Defendants and/or their customers the payments identified in paragraph 139 of the Amended Complaint I and paragraph 98 of the Amended Complaint II, under sections 544(b), 547(b), 548(a) and 550 of the Code<sup>3</sup>, as preferences or fraudulent transfers. AC I ¶¶ 143-169; AC II ¶¶ 102-128.

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<sup>3</sup> 11 U.S.C. §§ 544, et seq.

## **PRELIMINARY STATEMENT**

Enron's Amended Complaints fail to state a claim upon which relief can be granted in so far as they seek recovery from the Defendants to recover protected "settlement payments" made in regards to the repurchase of its commercial paper. Section 546(e)<sup>4</sup> of the Bankruptcy Code ("Code") expressly prohibits Enron from avoiding pre-petition "settlement payments" made by or to a "stockbroker" or "financial institution" or through a "securities clearing agency." "Security" is broadly defined in the Code and unambiguously includes commercial paper. "Settlement payments," also defined broadly in the Code, include all settlement payments on securities made at any time prior to the commencement of a proceeding. Lastly, all the Defendants to this litigation qualify either as stockbrokers or financial institutions, or qualify because they received payments by, to or through a stockbroker, financial institution or securities clearing agency. Therefore, as a matter of law, Enron's claims seeking recovery of the payments made to purchase its commercial paper must fail.

Congress has endeavored to preclude the systemic damage to financial markets that the avoidance by Enron of settlement payments to holders of its commercial paper would cause. Section 546(e) of the Code, exempting settlement payments in the commodities industry, was enacted and later expanded to cover securities such as commercial paper to prevent the bankruptcy of one party from spreading to other parties and possibly threatening a market collapse. A ruling permitting Enron to take back payments on its commercial paper would be in conflict with Congress' clear intent to protect the commercial paper market.

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<sup>4</sup> 11 U.S.C. § 546(e).

The commercial paper market is a "critical financial market" that provides "the means for banks, securities firms, and other financial institutions to adjust their cash and securities positions and those of their customers in order to manage liquidity, market, and other risks to their organizations."<sup>5</sup> A decision to unwind Enron's commercial paper settlements would drastically unsettle this critical market. This would be severely detrimental for the U.S. economy as it would result in a dramatic increase in financing costs for U.S. companies and financial institutions generally, and the unavailability of commercial paper financing for others.

In short, the complaints should be dismissed as a matter of the clear meaning of the law, which is supported by Congressional intent and sound public policy.

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<sup>5</sup> Federal Reserve System Docket No. R-1128, Dept. of Treasury Office of the Comptroller of the Currency Docket No. 03-05, SEC Release No. 34-47638, April 7, 2003 Interagency Paper on Sound Practices to Strengthen the Resilience of the U.S. Financial System, at <http://www.sec.gov/news/studies/34-47638.htm>; see, also, Gregory Zuckerman, Sinking Commercial Paper Market Broadens Effects of Enron Troubles, Wall St. J., March 28, 2002 ("For years, the commercial-paper market has served as the corporate world's automated teller machine, spitting out a seemingly endless supply of cash for businesses at super-low interest rates.").

## ARGUMENT

### **A. Commercial Paper Is A Critical Source Of Financing And Its Stability Is Of Paramount Importance**

Commercial paper has historically played an important role in the financing and growth of U.S. corporations. The commercial paper market is a "critical financial market" that provides "the means for banks, securities firms, and other financial institutions to adjust their cash and securities positions and those of their customers in order to manage liquidity, market, and other risks to their organizations."<sup>6</sup> Non-financial firm issuers use commercial paper as a source of working capital, while public utilities use commercial paper to purchase raw materials and fund construction. State governments use commercial paper to finance public works projects, such as mass transit projects in New York, and to provide disaster relief funds.<sup>7</sup> Large finance companies also rely heavily on the commercial paper market as their second most important source of funds, accounting for about 18% of the sector's funding.<sup>8</sup> It is this broad access to inexpensive financing afforded by the commercial paper market that Congress has recognized (as described below) as warranting special legislative protection from the hazards of a market participant's insolvency.

Courts have correctly observed that in typical circumstances commercial paper is very safe, as evidenced by its low default rate and short maturity. In fact, historically, the default rate on commercial paper is much lower than that on ordinary commercial loans.<sup>9</sup> Commercial paper

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<sup>6</sup> Federal Reserve System Docket No. R-1128, Dept. of Treasury Office of the Comptroller of the Currency Docket No. 03-05, SEC Release No. 34-47638, April 7, 2003 Interagency Paper on Sound Practices to Strengthen the Resilience of the U.S. Financial System, at <http://www.sec.gov/news/studies/34-47638.htm>; see, also, Zuckerman, Sinking Commercial Paper Market Broadens Effects of Enron Troubles, Wall St. J., March 28, 2002.

<sup>7</sup> Dusan Stojanovic and Mark D. Vaughan, The Commercial Paper Market: Who's Minding the Shop?, The Federal Reserve Bank of St. Louis, at <http://www.stls.frb.org/publications/re/1998/b/re1998b3.html>.

<sup>8</sup> Bank of International Settlements, BIS Quarterly Review: International banking and financial market developments, 8 (Dec. 2003), at [http://www.bis.org/publ/qtrpdf/r\\_qt0312.pdf](http://www.bis.org/publ/qtrpdf/r_qt0312.pdf).

<sup>9</sup> A.G. Becker Inc. v. Bd. of Govs. of the Fed. Reserve Sys., 693 F.2d 136, 149 (D.C. Cir. 1982).



is also a cost-effective form of financing with rates typically several percentage points below those of longer-term bonds and loans from banks.<sup>10</sup> These low financing rates reflect the lack of credit risk associated with commercial paper.

The benefits of commercial paper are so great that it has largely displaced short-term and medium-term corporate credit issued by banks to large corporations.<sup>11</sup> The amount of commercial paper outstanding has increased significantly over the last ten years. As of December 31, 2003, there was \$1.29 trillion in U.S. commercial paper outstanding, as compared to \$4.4 trillion in total corporate long-term debt outstanding.<sup>12</sup> Furthermore, the issuance of commercial paper with very short maturities has also increased in the last decade, with approximately \$4.3 trillion in rated one to four day commercial paper issued in 2003.<sup>13</sup>

Commercial paper issuers generally "roll over" outstanding issues; that is, they sell new paper to pay off maturing paper. Under certain unfavorable financial conditions, however, issuers must replace their commercial paper with longer-term debt by drawing on their lines of credit or other standby facilities. This practice of replacing commercial paper with debt under lines of credit is indicative of the fact that commercial paper is not priced to take into account credit risk in the same manner as longer-term debt. The Federal Reserve has recognized the importance to market stability of the orderly settlement of commercial paper through access to standby financing. For example, the orderly settlement of billions of dollars of commercial

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<sup>10</sup> Zuckerman, Sinking Commercial Paper Market Broadens Effects of Enron Troubles, Wall St. J., March 28, 2002.

<sup>11</sup> David M. Eaton, The commercial banking-related activities of investment banks and other nonbanks, 44 Emory L.J. 1187, 1211 (1995). George G. Triantis & Ronald J. Daniels, The Role of Debt in Interactive Corporate Governance, 83 Calif. L. Rev. 1073, 1083 (1995).

<sup>12</sup> The Bond Market Association, Research Quarterly (February 2004), at [http://www.bondmarkets.com/research/Research\\_Quarterly\\_February\\_2004.pdf](http://www.bondmarkets.com/research/Research_Quarterly_February_2004.pdf).

<sup>13</sup> Based on Federal Reserve commercial paper statistics derived from data supplied by The Depository Trust Company (DTC). See, Federal Reserve, Volume Statistics for Commercial Paper Indexes, at <http://www.federalreserve.gov/releases/cp/indexstats.htm>.

paper by drawing on bank lines in the wake of market uncertainty caused by the terrorist attacks of September 11, 2001 was hailed as an example of "the ability of our economy to circumvent difficulties and innovate around obstacles."<sup>14</sup>

In the immediate case, Enron borrowed \$1.9 billion from committed bank lines of credit to purchase outstanding commercial paper from holders, thereby exiting the commercial paper market for its short-term liquidity needs and replacing it with longer-term debt.<sup>15</sup> This is a common practice for an issuer facing financial difficulties and liquidity concerns. While Enron was not able to stave off insolvency, in many other cases the ability of an issuer to replace commercial paper with longer-term debt has helped avoid a financial crisis.<sup>16</sup> If the finality of this process of settling out of the commercial paper market is over-turned, both the usefulness and availability of commercial paper financing will be severely impaired.

The commercial paper market is the most cost-effective form of financing, in part, because it is considered to be safe from a trustee's avoidance powers because of Section 546(e) of the Code. The market, however, as Congress has stated, needs "certain protections . . . to prevent the insolvency of one . . . security firm from spreading to other firms and possibly

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<sup>14</sup> Alan Greenspan, The September 11 tragedy and the response of the financial industry (Oct. 23, 2001) (taped statement), at <http://www.bis.org/review/r011025b.pdf>.

<sup>15</sup> Enron Corp. 10-Q filed Sept. 30, 2001 at 12, 68, at <http://www.sec.gov>.

<sup>16</sup> See, e.g., Xerox Corp. 10-Q, filed Nov. 11, 2001, at <http://www.sec.gov> ("The primary sources of funding have been cash flows from operations and borrowings under our commercial paper and term funding programs....Since the beginning of October 2000, [Xerox] has experienced a significant reduction in its ability to access capital markets and uncommitted bank lines of credit....As a result, as of October 31, 2000 we had drawn down \$5.3 billion under our \$7 billion Revolving Credit Agreement..."); Lucent Technologies Inc. 10-Q, filed Aug. 13, 2001, at 27, at <http://www.sec.gov> ("As a result of the reductions of our credit ratings earlier in fiscal 2001, commercial paper and some other types of borrowings became unavailable to us and the costs of our financings increased...[Our credit facilities] were used to fund our operations and pay down commercial paper. We had no commercial paper outstanding as of June 30, 2001."); see, also, Dan Ackman, Lucent Bankrupt? -- Not!, *Forbes*, April 5, 2001, at <http://www.forbes.com/2001/04/05/0405topnews.html> ("rumors suggested that Lucent was running out of cash and was dipping into its \$6.5 billion line of credit. While Lucent may be using its credit line--that's what credit lines are for-----").

threatening the collapse of the affected market."<sup>17</sup> If Enron prevails in this case, precisely that systemic insolvency risk will be imposed on the commercial paper market. Furthermore, the fear that commercial paper settlements might be unwound will result in a dramatic increase in financing costs for issuers as they compensate purchasers for this new risk.<sup>18</sup>

In summary, the commercial paper market is a critical and well established financial market that provides companies and financial institutions access to cost-effective financing. An adverse ruling in this case permitting Enron to undo hundreds of settled securities transactions would create instability in, and damage access to, the commercial paper market and cause substantial damage to the economy.

**B. Congress Has Endeavored To Preclude The Damage To Financial Markets That The Avoidance Of Payments By Enron To Holders Of Its Commercial Paper Would Cause**

Justice Cardozo's recognition of "the overmastering need of certainty in the transactions of commercial life" is as apt today in regards to the commercial paper market as it was eighty years ago.<sup>19</sup> A decision allowing a trustee-in-bankruptcy or debtor-in-possession to avoid pre-petition settlement payments made to purchase outstanding commercial paper would contradict the intention of Congress to ensure stability in the commercial paper market, thereby "threatening the collapse" of the commercial paper market.<sup>20</sup>

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<sup>17</sup> H.R. REP. NO. 97-420, at 1-2 (1982), reprinted in 1982 U.S.C.C.A.N. 583, 583.

<sup>18</sup> See, e.g., Michael J. Herbert, The Trustee Versus The Trade Creditor II: The 1984 Amendment to Section 547(c)(2) of the Bankruptcy Code, 2 Bank. Dev. J. 201, 205 (In regards to trade creditors who extend credit to a debtor, the author states, "To the extent that the preference laws enter into the trade creditor's calculation of whether to do business with the debtor or not, they provide a disincentive to deal, because they increase the risk of eventual non-payment."). Even in the absence of an adverse court decision, the financial jitters caused by Enron's collapse resulted in a temporary but severe tightening of the market for commercial paper. In February 2002, Sprint, which had been relying on the commercial paper market for \$3 billion of working capital, was forced to take on long-term debt that cost the company almost \$200 million in additional annual borrowing costs. Zuckerman, Sinking Commercial Paper Market Broadens Effects of Enron Troubles, Wall St. J., March 28, 2002.

<sup>19</sup> Benjamin N. Cardozo, Growth of the Law 110 (1924).

<sup>20</sup> H.R. REP. NO. 97-420, at 1-2 (1982), reprinted in 1982 U.S.C.C.A.N. 583, 583.

The risks to the commercial paper market posed by past versions of the Code were corrected many years ago. Section 546(e) of the Code had its origins in Congress' response to the concern that avoidance of pre-petition payments in the commodities market would result in a "domino effect" chain of insolvencies.<sup>21</sup>

In Seligson v. New York Produce Exchange<sup>22</sup>, the Court refused to find that a \$12 million margin payment made by a bankrupt commodities broker was exempt from the avoiding powers of the broker's trustee-in-bankruptcy. Alarmed by the threat to market stability, Congress responded by adopting Section 546(d)<sup>23</sup>, later redesignated as 546(e)<sup>24</sup>, exempting margin and settlement payments in the commodities markets. Congress intended to provide protection from the types of claims represented by Seligson and to prevent the bankruptcy of one party in the commodities clearance and settlement chain from spreading to other parties and possibly threatening a market collapse.<sup>25</sup> Realizing that the protection afforded to the commodities markets had not been explicitly extended to securities, Congress in 1982 extended the Code's protection to the securities markets, thereby insuring that the avoiding powers of a trustee-in-bankruptcy would not be used to set aside margin or settlement payments in respect of securities.<sup>26</sup> Congress again addressed this issue in 1984 when it amended Section 547 to make

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<sup>21</sup> Bankruptcy of Commodity and Securities Brokers, 1981: Hearing Before the Subcomm. on Monopolies and Commercial Law of the House Comm. on the Judiciary, 97th Cong., 1st Sess. 203 (1981) (statement of Edmund Schroeder); H.R. REP. NO. 97-420, supra, at 1; Neil M. Garfinkel, Note: No Way Out: Section 546(e) is No Escape for the Public Shareholder of a Failed LBO, 1991 Colum. Bus. L. Rev. 51, 61-62 (1991).

<sup>22</sup> Seligson v. N.Y. Produce Exch., 394 F. Supp. 125 (S.D.N.Y. 1975) (trustee of bankrupt commodities broker sought to recover as a fraudulent conveyance margin payments to a clearinghouse, leading to Congress' enactment of § 546(e) and other provisions to protect commodities and securities brokers and related entities).

<sup>23</sup> Formerly Section 764(c). Pub. L. No. 97-222, 96 Stat. 235 (July 27, 1982).

<sup>24</sup> Pub. L. No. 98-353.

<sup>25</sup> Neil M. Garfinkel, Note: No Way Out: Section 546(e) is No Escape for the Public Shareholder of a Failed LBO, 1991 Colum. Bus. L. Rev. 51, 61-62 (1991); H.R. REP. NO. 97-420, supra, at 1-2.

<sup>26</sup> S. REP. NO. 95-989, at 106 (1978), reprinted in 1978 U.S.C.C.A.N. 5787.

it clear that the protection of 546(e) could not be compromised.<sup>27</sup> The need for that clarification was amplified by Professor Lawrence King of the New York University School of Law who earlier had testified before Congress stating that: "it was not a purpose of the 1978 Code to cause valid and established business practices of the commercial paper market to undergo unnecessary change causing additional expense and perhaps loss of access to the commercial paper market merely to comply with a tangentially related bankruptcy law."<sup>28</sup>

Accordingly, Congress has enacted legislation to protect the pre-petition settlement of commercial paper. Permitting a debtor to circumvent or ignore this protection will only serve to undermine Congress' clear intent and thereby create the very disruption in the commercial paper market that Congress tried to prevent.

**C. Commercial Paper Is A Security And The Payments Made By Enron To Holders Of Its Commercial Paper Are Protected "Settlement Payments" Under The Code That Are Not Subject To A Trustee's Avoidance Powers**

Section 546(e) of the Code protects settlement payments made on securities by or to a "stockbroker" or "financial institution" or through a "securities clearing agency" from the threat of avoidance<sup>29</sup>, except in circumstances where payments are made with actual intent to hinder, delay or defraud any entity to which the debtor was or became indebted under Section

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<sup>27</sup> Congress eliminated the then 45-day look-back period for transfers made in connection with, among other things, commercial paper. Congress stated that its intention was to: "create an exemption to the preference section for commercial paper...in response to . . . a growing problem facing issuers, dealers and raters of commercial paper... [who] are concerned that an interpretation conceivably could be given to section 547 that might allow a trustee of a debtor's estate to force a purchaser of the debtor's commercial paper to disgorge payments received from the debtor within 90 days prior to the debtor's filing of a petition in bankruptcy if such payment was not subject to any of the exemptions found in 547(c) . . . It certainly was not the intent of the [C]ode to affect such transactions . . . ." Preference Section of the Bankruptcy Code: Hearings on S. 3023 Before the Senate Subcommittee on Judicial Machinery of the Committee on the Judiciary, 96th Cong., 2d Sess. (1980) (opening statement of Sen. DeConcini).

<sup>28</sup> Preference Section of the Bankruptcy Code: Hearings on S. 3023 Before the Senate Subcommittee on Judicial Machinery of the Committee on the Judiciary, 96th Cong., 2d Sess. (1980) (statement of Prof. Lawrence King, New York Univ. Sch. Of Law).

<sup>29</sup> 11 U.S.C. § 546(e).

548(a)(1)(A).<sup>30</sup> In this case, as explained below, the payments made by Enron to purchase its commercial paper were settlement payments made by, to or through the above statutory categories. The Amended Complaints absolutely fail to allege any facts that would enable Enron to invoke the Section 548(a)(1)(A) exception to the broad protection otherwise afforded by 546(e).

Based on the plain, unambiguous terms of the Code, (i) commercial paper is a "security" under the Code, (ii) payments of funds to settle commercial paper purchases are protected "settlement payments" and (iii) the Defendants to this litigation qualify under the statutory categories of recipients of settlement payments protected by the Code. As a result, payments made by Enron to repurchase its commercial paper are not subject to the trustee's avoidance powers. Enron's improper attempt to avoid pre-petition settlement payments made on its commercial paper is barred by the Code's safe-harbor and its claims must fail as a matter of law.

There can be no doubt that a commercial paper note is a "security" under the plain language of the Code. Section 101(49)(A) of the Code defines "security" to include "note" without limitation.<sup>31</sup> None of the exclusions to the definition of "security" set forth in Section 101(49)(B) of the Code apply to commercial paper.<sup>32</sup> Commercial paper is commonly defined as

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<sup>30</sup> 11 U.S.C. § 548(a)(1)(A).

<sup>31</sup> 11 U.S.C. § 101(49)(A);

<sup>32</sup> 11 U.S.C. § 101(49)(B).

"notes."<sup>33</sup> Enron also admits in the Amended Complaints that the commercial paper at issue is comprised of notes. AC I ¶ 136; AC II ¶ 96 (referring to the commercial paper as "Enron commercial paper notes").

"Security," as defined in the Code, also includes "[an] other claim or interest commonly known as 'security.'"<sup>34</sup> The U.S. securities laws should offer guidance in interpreting "security" under the Code. Commercial paper clearly is a security under the Securities Act of 1933 (the "Securities Act").<sup>35</sup> According to the Supreme Court, commercial paper is also a security under the Securities Exchange Act of 1934, the Banking Act of 1933, the Public Utility Holding Company Act of 1935 and the Glass-Steagall Act. The Supreme Court has stated:

In each of these...statutes, the definition of the term "security" includes commercial paper, and each statute contains explicit exceptions where Congress meant for the provisions of an Act not to apply to commercial paper. These explicit exceptions demonstrate congressional cognizance of commercial paper

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<sup>33</sup> See, e.g., Commodities Futures Trading Commission, CFTC Glossary, at [http://www.cftc.gov/opa/glossary/opaglossary\\_co.htm](http://www.cftc.gov/opa/glossary/opaglossary_co.htm) ("Commercial Paper: Short-term promissory notes issued in bearer form by large corporations, with maturities ranging from 5 to 270 days. Since the notes are unsecured, the commercial paper market generally is dominated by large corporations with impeccable credit ratings."); Federal Deposit Insurance Corporation, Glossary, at <http://www.fdic.gov/regulations/trust/trust/glos.html> ("Commercial Paper: Negotiable, short-term, unsecured promissory notes...."). It is instructive that Congress' recent definition of "securities" in regards to the Code includes "commercial paper." The Report to the Financial Contracts Bankruptcy Reform Act of 2003, which Act proposes to "minimize systemic risk in light of market developments," states that the term "securities" includes "commercial paper." H.R. REP. No. 108-277, 108th Cong., 1st Sess., pt. 1 at 17 (2003).

<sup>34</sup> 11 U.S.C. § 101(49)(A). The Code's rules of construction, specifically Section 102(3), which states "includes" and "including" are not limiting, make it clear that the Code's definition of "security" is not limiting. *Id.* § 102(3).

<sup>35</sup> Section 3(a)(3) of the Securities Act exempts from the registration and prospectus delivery requirements of Section 5 of the Securities Act "[a] note...which arises out of a current transaction or the proceeds of which have been or are to be used for current transactions, and which has a maturity at the time of issuance not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited...." The SEC has stated, "The legislative history of the [Securities Act] makes clear that Section 3(a)(3) applies...to prime quality negotiable commercial paper." Securities Act Release No. 33,4412, 26 Fed. Reg. 9158 (Sept. 20, 1961). Furthermore, issuers whose commercial paper does not qualify for the Section 3(a)(3) exemption often sell such securities through an institutional private placement under Section 4(2) of the Securities Act. 15 U.S.C. § 77d(1)-(2); Securities Industry Association, SEC No-Action Letter, 1992 SEC No-Act. LEXIS 411 ("Commercial Paper is generally issued pursuant to one of the three following exemptions from registration under the Securities Act of 1933: Section 3(a)(2), which exempts obligation of banks; Section 3(a)(3), which exempts commercial paper, as defined; and Section 4(2), which exempts any security sold in a private placement."). Obviously, if commercial paper were not a security it would need no exemption from registration.

and Congress' understanding that, unless modified, the use of the term "security" encompasses it.<sup>36</sup>

Settlement payments made on securities are protected from a trustee's avoidance powers. Section 741(8) of the Code defines "settlement payment" to include "preliminary settlement payment, a partial settlement payment, an interim settlement payment, a settlement payment on account, a final settlement payment, or any other similar payment commonly used in the securities trade."<sup>37</sup> The definition of "settlement payment" is "extremely broad."<sup>38</sup> Settlement payments include securities "transfers which are normally regarded as part of the settlement process, whether they occur on the trade date, the scheduled settlement day, or any other date in the settlement process for the particular type of transaction at hand."<sup>39</sup> Furthermore, "[t]his includes any transfers that occur during the settlement process."<sup>40</sup>

Courts have found settlement payments to have occurred even in the absence of the settlement of the securities transaction itself. In In re Comark,<sup>41</sup> Comark engaged in "matched book" transactions by trading in securities issued by the Government National Mortgage Association ("GNMAs") under repurchase agreements ("repos") and reverse repos<sup>42</sup> with parties with Comark acting as an intermediary. Upon the onset of financial difficulties, Comark withdrew from the market, and the parties to which it acted as intermediary contracted to

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<sup>36</sup> Sec. Indus. Ass'n v. Bd. of Govs. of the Fed. Reserve Sys., 468 U.S. 137, 150-51 (1984).

<sup>37</sup> 11 U.S.C. § 741(8).

<sup>38</sup> Kaiser Steel Corp. v. Charles Schwab & Co., 913 F.2d 846, 848-49 (10th Cir. 1990).

<sup>39</sup> Jonas v. Resolution Trust Corp. (In re Comark), 971 F.2d 322, 325 (9th Cir. 1992) (quoting Bevill, Bresler & Schulman Asset Mgmt. Corp. v. Spencer Sav. & Loan Ass'n, 878 F.2d 742, 745 (3d Cir. 1989)).

<sup>40</sup> Id.

<sup>41</sup> Jonas v. Resolution Trust Corp. (In re Comark), 971 F.2d 322 (9th Cir. 1992).

<sup>42</sup> In a repo arrangement, the dealer sells specified securities to a purchaser, but also agrees to repurchase the securities later at the original price, plus an agreed upon additional amount usually representing interest on the original purchase price. In a reverse repo, the dealer buys securities and agrees to resell the securities to the seller in the future. Repos and reverse repos are similar to commercial paper in that they are both forms of short-term financing with a set maturity date and interest is calculated into the repurchase amount at the time of contracting.



complete the repos and reverse repos directly with each other. Comark subsequently filed for bankruptcy and Comark's trustee-in-bankruptcy sought to recover the value of its alleged preferential transfers. The trustee argued that "no trade 'settled' in this case, because Comark merely backed out of the transaction."<sup>43</sup> Comark asserted that the reverse repo transactions were not completed until much later when the firms that assumed Comark's obligations actually resold the GNMA's to the reverse repo counterparty.<sup>44</sup> The Court found that the "return of the . . . GNMA's was a step in the process of 'settling' Comark's withdrawal from the Reverse Repo arrangement" and thus, "the transfer was an unavoidable settlement payment."<sup>45</sup> Certainly Enron's payments to settle its outstanding commercial paper, in which the payments settled the transactions in their entirety, are therefore also unavoidable settlement payments.

Section 546(e) of the Code expressly prohibits Enron from avoiding pre-petition "settlement payments" made by or to a "stockbroker" or "financial institution" or through a "securities clearing agency."<sup>46</sup> Each of the Defendants qualify under these statutory categories as stockbrokers or financial institutions or received payments by, to or through a stockbroker, financial institution or securities clearing agency. The settlement payments were made through a securities clearing agency, the Depository Trust Company. The Defendants, therefore, are protected by the Code's safe harbor.

As demonstrated above, commercial paper is a "note" and is "commonly known as a 'security,'" and is therefore a security under the Code. A payment by an issuer to repurchase its commercial paper on or before the maturity date is a protected "settlement payment." Finally, Defendants qualify under the categories of recipients of settlement payments protected by the

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<sup>43</sup> Id. at 325.

<sup>44</sup> Id.

<sup>45</sup> Id. at 326.

Code. Accordingly, the Amended Complaints should be dismissed based on the plain language of the Code.

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<sup>46</sup> 11 U.S.C. § 546(e).

## CONCLUSION

For reasons discussed above, Defendants' motions to dismiss should be granted.

Dated: New York, New York  
March 17, 2004

Respectfully submitted,

ALLEN & OVERY

By: /s/ Hugh McDonald

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UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK

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In re:	:	Chapter 11
	:	
ENRON CORP., <u>et al.</u> ,	:	Case No. 01-16034 (AJG)
	:	
Debtors.	:	(Jointly Administered)
	:	
-----	X	
ENRON CORP.,	:	
Plaintiff,	:	
	:	
v.	:	Adv. No. 03-92677 (AJG)
	:	
J.P. MORGAN SECURITIES, INC., <u>et al.</u> ,	:	
	:	
Defendants.	:	
-----	X	
ENRON CORP.,	:	
Plaintiff,	:	
	:	
v.	:	Adv. No. 03-92682 (AJG)
	:	
MASS MUTUAL LIFE INSURANCE CO., <u>et al.</u> ,	:	
	:	
Defendants.	:	
-----	X	

**ORDER GRANTING MOTION OF THE BOND MARKET ASSOCIATION FOR  
LEAVE TO FILE BRIEF AND MEMORANDUM OF LAW OF THE BOND MARKET  
ASSOCIATION, AS *AMICUS CURIAE*, IN SUPPORT OF DEFENDANTS' MOTION TO  
DISMISS THE AMENDED COMPLAINTS**

THE COURT, having considered the motion (the "Motion") of The Bond Market Association ("TBMA") for leave to file the Brief and Memorandum of Law of The Bond Market Association, as Amicus Curiae, in Support of Defendants' Motion to Dismiss the Amended Complaints; and being advised of the grounds for the Motion; and notice of the Motion having

been given to all Parties to these adversary proceedings and the Office of the U.S. Trustee; and  
good and sufficient grounds appearing therefor; IT IS HEREBY

ORDERED, that the motion is GRANTED.

DATED this \_\_\_\_ of \_\_\_\_\_, 2004.

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Honorable Arthur J. Gonzalez  
United States Bankruptcy Judge