

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF LOUISIANA
LAFAYETTE-OPELOUSAS DIVISION

IN RE: STONE ENERGY CORP.
SECURITIES LITIGATION

Civil Action No. 6:05CV2088 (LEAD)
6:05CV2109 (MEMBER)
6:05CV2220 (MEMBER)

JUDGE TUCKER L. MELANÇON
MAG. JUDGE MILDRED E. METHVIN

CONSOLIDATED CLASS ACTION COMPLAINT
FOR VIOLATIONS OF THE SECURITIES LAWS

I. NATURE OF THE ACTION

1. This action is brought by El Paso Firemen and Policemen's Pension Fund, pursuant to §§ 10(b) and 20(a) of the Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §§ 78j(b) and 78t(a), and Rule 10b-5, 17 C.F.R. § 240.10b-5, promulgated thereunder, on behalf of itself and other persons and entities who purchased or otherwise acquired the common stock of Stone Energy Corporation ("Stone" or the "Company"), from May 2, 2001 through and including March 10, 2006 (the "Class Period"), and were damaged thereby.

2. Stone has now admitted that it overstated its proved oil and gas reserves by over twenty percent over a four and one-half year period in violation of U.S. Securities and Exchange Commission ("SEC") rules for reporting proved reserves, and that the overstatements resulted in the material understatement of its operating expenses and the overstatement of its net income in each quarter during that period.

3. The overstatements of proved reserves were not the product of negligence or mistake. Rather, as ultimately admitted by Stone and confirmed by Lead Plaintiff's investigation as detailed below, the reserve overstatements were the product of intentional conduct by senior management aimed at overstating Stone's proved reserves and inflating Stone's stock price.

4. This fraud was orchestrated by defendant D. Peter Canty ("Canty"), Stone's former Chief Executive Officer ("CEO") and then Director, who was principally responsible for determining and reporting Stone's proved reserves. Canty signed Stone's reported financial results filed with the SEC and certifications pursuant to the Exchange Act and the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley Act"). As detailed below, throughout the Class Period, defendant Canty:

- Re-drew geological maps of oil and gas reservoirs to manufacture false reserve numbers;

- Violated SEC requirements for booking proved reserves; and
- Intimidated and verbally abused Stone employees for calculating proved reserves that were lower than Canty wanted.

5. Stone's audit committee of the Board of Directors forced Canty to resign as a Stone Director following Stone's investigation into its overstatement of proved reserves.

6. Other top executives within Stone, including its Senior Vice President for Exploitation, Gerald Yunker, and its Reservoir Engineer Manager, Mindy Stuart, participated with Canty in pressuring employees into overstating proved reserves and manufacturing reserve numbers. Following Stone's investigation into its reserves overstatement, Stone's audit committee of the Board of Directors forced Yunker and Stuart to resign as a result of their involvement in the reserves overstatements. Stone's audit committee also replaced Atwater Consultants, Ltd. ("Atwater"), its outside engineering firm that had previously evaluated and audited Stone's reserves in the Gulf of Mexico, where the overstatements occurred.

7. Defendant David H. Welch became Stone's CEO as of April 1, 2004. As detailed below, Stone personnel informed Welch of Stone's overstated proved reserves within two months of his joining Stone, but Welch continued overstating Stone's proved reserves for nearly two years. Welch signed Stone's reported financial results filed with the SEC and certifications pursuant to the Exchange Act and the Sarbanes-Oxley Act.

8. Defendant James H. Prince ("Prince") was Stone's Chief Financial Officer ("CFO") from 1999 to August 1, 2005. Under Prince's direction as its CFO responsible for Stone's financial reporting, the Company violated Generally Accepted Accounting Principles ("GAAP"), as detailed more fully below, regarding the determination and disclosure of its proved reserves. Prince signed Stone's reported financial results filed with the SEC, along with

certifications pursuant to the Exchange Act and the Sarbanes-Oxley Act. Prince retired from the Company and sold substantial amounts of his Stone stock as the Company was beginning the investigation into its reported proved reserves, and two months before Stone disclosed its overstated proved reserves. Following Prince's retirement, defendant Kenneth H. Beer ("Beer") became Stone's CFO. Beer signed the certification of Stone's financial results for the second quarter of 2005 pursuant to the Exchange Act and Sarbanes-Oxley Act.

9. While the Company was inflating its proved reserves and issuing materially false financial statements, Company insiders with knowledge of the fraud were selling their personal holdings of Stone common stock at prices they knew were artificially inflated by the proved reserves overstatement. Indeed, during the Class Period, with knowledge of the adverse material facts discussed below, defendants Canty and Prince, along with other company insiders, including Gerald Yunker, sold over one million shares for nearly \$50 million.

10. On October 6, 2005, Stone announced a downward revision of its previously reported proved reserves. In response to this news, Stone's stock price plummeted \$7.93 per share. Stone's stock price continued to fall when Stone announced the full time-period and quantity of its overstated proved reserves and the restatement of its financial statements, and when Moody's Investor Service ("Moody's") downgraded Stone's bond ratings.

11. Stone ultimately admitted that "[a] material weakness in internal control over financial reporting existed," and that because of the material weakness, Stone's "disclosure controls and procedures were not effective in recording, processing, summarizing and reporting information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934."

12. As a result of Stone's announcements, the SEC instituted an inquiry into the proved reserves overstatement, and the Philadelphia Stock Exchange instituted an investigation into insider trading by Stone officers and directors prior to Stone's initial disclosure on October 6, 2005.

II. JURISDICTION AND VENUE

13. The Court has jurisdiction over the subject matter of this action under § 17 of the Exchange Act, 15 U.S.C. § 78aa. The claims asserted herein arise under §§ 10(b) and 20(a) of the Exchange Act codified at 15 U.S.C. §§ 78j(b) and 78t(a), Rule 10b-5, 17 C.F.R. § 240.10b-5, promulgated thereunder.

14. Venue is proper in this District pursuant to 28 U.S.C. § 1391(b) and 15 U.S.C. § 77v. Many of the acts giving rise to the violations of law complained of herein, including the preparation and dissemination to the investing public of false and misleading financial statements and proved reserves information, occurred in this District. Stone is a Delaware Corporation with its principal place of business in this District at 625 East Kaliste Saloom Road, Lafayette, Louisiana.

15. In connection with the acts, conduct and other wrongs complained of herein, defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, the United States mail and the facilities of a national securities market.

III. SOURCES

16. The allegations contained herein are based upon review and analysis of publicly available materials and investigation of counsel, including information obtained from the following confidential witnesses ("CW"):

(a) CW1 worked for Stone, including most recently as a Production Manager, for over ten years and left the Company in mid-2005. CW1's responsibilities included producing wells, bringing wells online and taking them off, and remedying any issues with the wells. In this position, CW1 directly addressed reserves issues because Stone's reservoirs consistently produced less than the amount that Stone had recorded as proved reserves in its SEC filings. CW1 attended meetings where reserves and the procedures for determining proved reserves were discussed by defendant Canty and geologists and reservoir engineers, and where the reserves were increased at Canty's demand. CW1 is knowledgeable about the Company's reserve report and what tests were run to determine the proved reserves. CW1 has personal knowledge of how proved reserves were calculated and overstated at Stone and the identity of members of senior management involved in overstating proved reserves. CW1 participated in due diligence for acquisitions, including assessing reserves and production of acquired properties. CW1 reported to Michael Madden (Vice President for Reserves), who reported to defendant Canty.

(b) CW2 worked for Stone as a Reservoir Engineer from 1994 to mid-2004. CW2 has personal knowledge of Stone's internal calculation of proved reserves and the determinations of proved reserves provided to Stone management.

(c) CW3 worked for Stone as a Reservoir Engineer between 1999 and mid-2005. CW3 is familiar with the SEC requirements for calculating proved reserves and has personal knowledge of how Stone's reserve reports deviated from SEC requirements.

(d) CW4 worked for Stone from 1997 to 2004, and as a Reservoir Engineer, has personal knowledge of how proved reserves were calculated at Stone, including the quality control for data kept in "black books." As a Reservoir Engineer, CW4 had personal knowledge of the data used to calculate proved reserves and of the calculations themselves, and updated the

data set that contained the calculations for proved reserves. CW4 calculated data used in determining proved reserves at Stone and provided this data directly to Mindy Stuart, Stone's former Reservoir Engineer Manager, who was CW4's direct supervisor.

IV. PARTIES

17. Lead Plaintiff El Paso Firemen and Policemen's Pension Fund ("El Paso Fire and Police") is a public pension fund system located in El Paso, Texas, organized for the benefit of retired municipal police officers and fire personnel in the City of El Paso. El Paso Fire and Police was appointed Lead Plaintiff by Court Order dated March 17, 2006. During the Class Period, El Paso Fire and Police purchased shares of Stone common stock and suffered damages as a result of the violations of securities laws alleged herein.

18. Defendant Stone is an oil and gas company engaged in the acquisition and subsequent exploration, development, operation and production of oil and gas properties, primarily offshore in the Gulf of Mexico, in various basins of the Rocky Mountains, and in the Williston Basin of North Dakota and Montana.

19. (a) Defendant D. Peter Canty, a trained petroleum geologist, served as Stone's CEO from January 1, 2001, President from March 1994, and Director from March 1993 through December 2005. Canty resigned as President and CEO effective April 1, 2004. According to the Company's 2005 Proxy Statement, upon Canty's resignation as President and CEO, "the Company agreed to a consulting arrangement with Mr. Canty whereby he was paid \$235,000 for consulting services for the period April 1, 2004 through December 31, 2004."

(b) Throughout Canty's tenure at Stone, including after resigning as President and CEO, Canty was a member of Stone's executive, investment, pricing and strategy committees. CW1 confirms that after Canty resigned as President and CEO, as a Director, Canty

remained in close contact with Gerald Yunker, Stone's Senior Vice President for Exploitation, who, along with Mindy Stuart and Canty, determined the proved reserves, and that Canty continued "calling the shots" regarding reported proved reserves

(c) By virtue of his positions as CEO, President, Director and consultant during the Class Period, and his day-to-day involvement in the management and operation of Stone and, in particular, his hands-on involvement in determining the proved reserves that were recorded in Stone's SEC filings and public statements to investors as particularized below, Canty was a controlling person of the Company and exercised his power and influence to cause Stone to engage in the wrongful conduct complained of herein. According to the Company's March 1, 2004 press release, Canty was "the primary designer of the acquisition and exploitation strategy that has been responsible for the successful development and growth of Stone Energy since its formation."

(d) Canty, along with defendant Prince, was responsible for ensuring the accuracy of Stone's financial reports and filings with the SEC, for the fiscal years 2001, 2002, and 2003. Canty certified to the SEC and investors with regard to the Company's annual reports for those years that: (i) he reviewed the annual report; (ii) the annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by the annual report; and (iii) the financial statements, and other financial information included in the annual report, fairly present in all material respects the financial condition, results of operations and cash flows of Stone.

(e) Canty also certified to the SEC and investors that the reports fully complied with the requirements of §§ 13(a) or 15(d) of the Exchange Act, pursuant to §§ 302 and

906 of the Sarbanes-Oxley Act. Specifically, in the Company's Forms 10-Q for the second and third quarters of 2002 and the first, second and third quarters of 2003, and the Forms 10-K for 2002 and 2003, Canty certified that: (i) the information contained in the report fairly presented, in all material respects, the financial condition and results of operations of the Company; (ii) he was responsible for establishing and maintaining disclosure controls and procedures, as well as evaluating the effectiveness of such disclosure controls and procedures; (iii) he reviewed and evaluated the effectiveness of Stone's disclosure controls and procedures; and (iv) based on this evaluation, Stone's disclosure controls and procedures were effective to assure that the required information is disclosed.

(f) Canty, along with defendant Prince, was principally responsible for the Company's communications to securities analysts and investors from May 2, 2001 through at least March 2004. Canty commented on the Company and its financial performance in press releases during the Class Period, including those dated September 25, 2002; December 20, 2002; March 23, 2003; August 4, 2003; and November 3, 2003. Canty also communicated directly with investment analysts concerning the Company and its financial results in analyst conference calls and "analyst day" meetings held during the Class Period.

(g) According to CW1 and CW3, and as more fully described below in ¶¶30-45, Canty directed that Stone's proved reserves be overstated, and regularly redrew geological maps of oil and gas reservoirs to inflate Stone's reported proved reserves. Canty had frequent disputes with Stone engineers regarding the amount of reported proved reserves. Indeed, at daily 8:00 a.m. "morning meetings" with Stone production and engineering personnel, Canty verbally abused Stone engineers who determined that proved reserves were lower than Canty wanted.

(h) During the Class Period, Canty owned 421,970 shares of Stone common stock and he sold 168,409 shares, or 40% of his holdings, for proceeds of over \$8 million.

(i) Canty retired as CEO and President effective April 1, 2004, but remained as a Stone Director. Following the findings and recommendations of Stone's independent investigation into its reported proved reserves, Canty was forced to resign as a Director effective December 2, 2005 because of his involvement in overstating reserves as described herein.

20. (a) Defendant David H. Welch was appointed President, CEO, and a Director of the Company effective April 1, 2004 upon defendant Canty's resignation as President and CEO.

(b) By virtue of his positions as President, CEO and Director during the Class Period, and his day-to-day involvement in the management and operation of Stone, Welch was a controlling person of the Company and exercised his power and influence to cause Stone to overstate its reported proved reserves and to materially misstate its financial results. Beginning in March 2004, Welch was principally responsible for the Company's communications to securities analysts and investors. Welch communicated directly with investment analysts concerning the Company and its financial results in analyst conference calls held during the Class Period.

(c) From April 2004 through the present, Welch was responsible for ensuring the accuracy of Stone's financial reports and filings with the SEC. Welch signed Stone's annual report on Form 10-K for the year 2004. With regard to the Company's 2004 annual report, Welch certified to the SEC and investors that: (i) he reviewed the annual report; (ii) the report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were

made, not misleading with respect to the period covered by the report; and (iii) the financial statements, and other financial information included in the report, fairly present in all material respects the financial condition, results of operations and cash flows of Stone.

(d) Welch also certified to the SEC and investors that Stone's financial reports fully complied with the requirements of §§ 13(a) or 15(d) of the Exchange Act, pursuant to §§ 302 and 906 of the Sarbanes-Oxley Act. Specifically, in the Company's Forms 10-Q for the first, second and third quarters of 2004 and the first and second quarters of 2005, and the Form 10-K for 2004, Welch certified that: (i) the information contained in the report fairly presented, in all material respects, the financial condition and results of operations of the Company; (ii) he was responsible for establishing and maintaining disclosure controls and procedures, as well as evaluating the effectiveness of such disclosure controls and procedures; (iii) he reviewed and evaluated the effectiveness of Stone's disclosure controls and procedures; and (iv) based on this evaluation, Stone's disclosure controls and procedures were effective to assure that the required information is disclosed.

(e) According to CW1, within two months after Welch joined Stone in April 2004, he was informed by CW1, Michael Madden (Vice President for Reserves) and Larry Wellborn (a Stone Reservoir Engineer) that Stone's reported proved reserves were overstated, as detailed below. *See* ¶¶44-45. According to CW1, Wellborn told Welch at least three times that there were "grave problems" with Stone's overstated proved reserves. Yet, Welch caused Stone to continue to report false and misleading financial results.

21. (a) Defendant James H. Prince served as Stone's CFO since August 1999, and Executive Vice President since April 2004. He previously served as Stone's Chief Accounting

Officer and Controller from 1993 to June 1999 and Treasurer from June 1999 to February 2004. In April 2002, Prince became a Senior Vice President.

(b) By virtue of his senior executive and officer positions at Stone and day-to-day involvement in the management and operation of Stone, as particularized below, Prince was a controlling person of Stone and exercised his power and influence to cause Stone to engage in the wrongful conduct complained of herein. Prince, along with defendants Canty and Welch during their respective years as CEO, was principally responsible for the Company's communications to securities analysts and investors from May 2, 2001 through at least July 2005. Prince communicated directly with investment analysts concerning the Company and its financial results in analyst conference calls and "analyst day" meetings held during the Class Period.

(c) Prince, along with Canty and Welch during their respective years as CEO, was responsible for ensuring the accuracy of Stone's financial reports and filings with the SEC, for the fiscal years 2001, 2002, 2003, and 2004. Prince certified to the SEC and investors with regard to the Company's annual reports for those years that: (i) he reviewed the annual report; (ii) the annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by the annual report; and (iii) the financial statements, and other financial information included in the annual report, fairly present in all material respects the financial condition, results of operations and cash flows of Stone.

(d) Prince also certified to the SEC and investors that the reports fully complied with the requirements of §§ 13(a) or 15(d) of the Exchange Act, pursuant to §§ 302 and

906 of the Sarbanes-Oxley Act. Specifically, in the Company's Forms 10-Q for the second and third quarters of 2002, the first, second and third quarters of 2003, the first, second and third quarters of 2004, and the first quarter of 2005, and the Forms 10-K for 2002, 2003, and 2004, Prince certified and stated that: (i) the information contained in the report fairly presented, in all material respects, the financial condition and results of operations of the Company; (ii) he was responsible for establishing and maintaining disclosure controls and procedures, as well as evaluating the effectiveness of such disclosure controls and procedures; (iii) he reviewed and evaluated the effectiveness of Stone's disclosure controls and procedures; and (iv) based on this evaluation, Stone's disclosure controls and procedures were effective to assure that the required information is disclosed.

(e) During the Class Period, Prince owned 320,622 shares of Stone common stock and sold 33,435 shares, or 10.4% of his holdings, for proceeds of \$1,609,738.10.

(f) Defendant Prince resigned as Executive Vice President and CFO effective August 1, 2005, when, unbeknownst to investors and as explained below, Stone management was aware that its proved reserves were overstated and officially commenced an internal review of its reported proved reserves.

22. (a) Defendant Kenneth H. Beer has been Stone's Senior Vice President and CFO since August 1, 2005.

(b) By virtue of his positions as Senior Vice President and CFO, and his day-to-day involvement in the management and operation of Stone, Beer was a controlling person of the Company and exercised his power and influence to cause Stone to overstate its reported proved reserves and to materially misstate its financial statements. Beginning in August 2005, Beer was principally responsible for the Company's communications to securities analysts and

investors. Beer communicated directly with investment analysts concerning the Company and its financial results in analyst conference calls held during the Class Period.

(c) Beer, along with Welch, was responsible for ensuring the accuracy of Stone's financial reports and filings with the SEC, for the quarter ended June 30, 2005. Beer certified to the SEC and investors with regard to the Company's report for that quarter that: (i) he reviewed the annual report; (ii) the annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by the report; and (iii) the financial statements, and other financial information included in the report, fairly present in all material respects the financial condition, results of operations and cash flows of Stone.

(d) Beer also certified to the SEC and investors that Stone's financial reports fully complied with the requirements of §§ 13(a) or 15(d) of the Exchange Act, pursuant to §§ 302 and 906 of the Sarbanes-Oxley Act. Specifically, in the Company's Form 10-Q for the second quarter of 2005, Beer certified that: (i) the information contained in the report fairly presented, in all material respects, the financial condition and results of operations of the Company; (ii) he was responsible for establishing and maintaining disclosure controls and procedures, as well as evaluating the effectiveness of such disclosure controls and procedures; (iii) he reviewed and evaluated the effectiveness of Stone's disclosure controls and procedures; and (iv) based on this evaluation, Stone's disclosure controls and procedures were effective to assure that the required information is disclosed.

V. OVERVIEW OF THE FRAUDULENT SCHEME

23. Stone is an oil and natural gas company engaged in the acquisition, exploration, development, operation and production of oil and gas properties. An oil and gas company's reported proved reserves indicate the estimated quantities of crude oil, natural gas, and natural gas liquids that will be recoverable by the company in future years. The reported reserves of an oil and gas company are its most important asset and an important performance metric for investors for three reasons. First, its reserves are the strongest indicator of what the company will likely produce in the future – a factor of most importance to investors. Second, the value of the company's oil and gas reserves determines its borrowing base which, in turn, is used to acquire additional properties in order to increase its reserves. Third, the quantity of proved reserves impacts the depletion, depreciation and amortization expense ("DD&A") – an oil and gas company's largest expenses – and, therefore, has a material impact on a company's net income and earnings per share.

24. Throughout the Class Period, Stone represented its business strategy as seeking "to increase reserves, production and cash flow through the acquisition, exploitation and development of mature properties located primarily in the Gulf Coast Basin." Stone reported in a February 16, 2004 press release – just before Stone's stock price reached a peak – that "[s]ince going public in 1993, Stone has grown estimated proved reserves at a compounded annual rate of 24% with an annual average reserve replacement ratio of 254%."

25. Pursuant to SEC rules, proved reserves may be reported in SEC filings only if geological and engineering data demonstrate with "reasonable certainty" that the oil or gas will be recoverable from the ground, given available technology and existing economic conditions.

As explained below in ¶52, SEC rules prohibit reporting proved reserves if there is “reasonable doubt” as to whether the oil or gas will be recoverable.

26. Stone systematically inflated its reported proved reserves throughout the Class Period. The Company has now admitted that it overstated its proved reserves by 237 billion cubic feet of natural gas equivalent (“Bcfe”) in its Form 10-Ks filed with the SEC for the years ended December 31, 2001 through 2004. The Company has further admitted that the reserve overstatement resulted in its financial statements for the years ended December 31, 2001 through 2004, and the first two quarters of 2005, being false and requiring a restatement.

27. Under GAAP, the restatement of previously issued financial statements is reserved for circumstances where no lesser remedy is available. Under Accounting Principles Board Opinion No. 20, *Accounting Changes*, restatements are required to correct material accounting errors that existed at the time the financial statements were prepared and issued.

28. The following chart quantifies the amount of the overstatement of proved reserves and the effect on Stone’s restatement of its financial statements for the four years and six months ended June 30, 2005, as admitted by Stone in its annual report on Form 10-K for the quarter and year ended December 31, 2005 and filed with the SEC on March 13, 2006:

Proved Reserves (millions of cubic feet of natural gas equivalent (“Mmcfe”))				
	Reported	Restated	Difference	Percentage Overstated
6 Mos. End 6/30/05	***	***	80,000	***
2004	824,950	668,210	156,740	23.46%
2003	816,295	647,326	168,969	26.10%
2002	750,766	620,644	130,122	20.97%
2001	775,015			

Net Income (\$ thousands)				
	Reported	Restated	Difference	Percentage Overstated
6 Mos. End 6/30/05	85,824	77,391	8,433	10.90%
2004	134,903	119,668	15,235	12.73%
2003	134,407	123,192	11,215	9.10%
2002	55,399	45,803	9,596	20.95%
2001	(71,375)	(116,665)	(45,290)	63.45%
Earnings Per Share (\$)				
	Reported	Restated	Difference	Percentage Overstated
6 Mos. End 6/30/05	3.20	2.89	0.31	10.73%
2004	5.07	4.50	0.57	12.67%
2003	5.10	4.67	0.43	9.21%
2002	2.10	1.74	0.36	20.69%
2001	(2.73)	(4.47)	(1.74)	63.74%
Depletion, Depreciation & Amortization Expense (\$ thousands)				
	Reported	Restated	Difference	Percentage Understated
6 Mos. End 6/30/05	121,868	134,420	12,552	9.34%
2004	188,153	210,861	22,708	10.77%
2003	170,845	188,813	17,968	9.52%
2002	160,762	175,496	14,734	8.40%
2001	158,893	164,150	5,257	3.20%

Source: Stone's report on Form 10-K for the quarter and year ended December 31, 2005.

*** Stone did not provide restated proved reserves for the six months ended June 30, 2005, but disclosed that the reserves were overstated by 80,000 Mmcfe for that period.

29. As admitted by the Company and confirmed by Lead Plaintiff's investigation, the proved reserve overstatement was not the product of negligence or mistakes, but rather was caused by senior management's intentional conduct aimed at overstating Stone's proved reserves and inflating its stock price. Below are specific examples of how Stone and its top level management intentionally overstated Stone's reported proved reserves.

Falsifying Reserve Reports

30. According to CW1, Canty created reserve reports that listed all of Stone's reservoirs and wells and showed when they began producing, what they produced and when they were plugged or taken off line. Stone's production forecasts were generated from Canty's reserve reports. According to CW1, Canty included data in the reserve reports that he knew was false.

Redrawing Geological Maps

31. According to CW1, defendant Canty regularly redrew geological maps of Stone's oil and gas reservoirs to be bigger than they really were to inflate Stone's proved reserves, and often told Stone geologists that their maps were wrong and instructed Stone engineers to enlarge maps of reservoirs to increase reserves.

Rejecting Reserve Numbers From Engineers And "Creating" Reserves

32. According to CW1, CW2, CW3, and CW4, Stone's reserves information and the tools used to measure proved reserves (such as logs of pressure and drilling information) were kept under "tight hold," and only a select few people, including defendant Canty, Gerald Yunker (Senior Vice President for Exploitation), Mindy Stuart (Reservoir Engineer Manager), and Lettie Barnes (a clerk doing reservoir work for Canty and Stuart) had access to the information. According to CW3, Canty would caucus with Gerald Yunker and Mindy Stuart and decide whether or not they would accept the reserve numbers calculated by Stone's engineers, and, if not, Lettie Barnes would then "slice and dice" the reserve numbers.

33. According to CW1 and CW3, Stone management frequently disagreed with Stone's reservoir engineers regarding the amount to be reported as proved reserves. Indeed,

CW3 recalls instances when CW3 recommended that reserve numbers be reduced, but management refused, including with respect to reserves at Stone's Clovelli field.

34. According to CW1 and CW3, Stone's upper management, in particular Canty, was "secretive" about certain of Stone's oil and gas fields, including its Clovelli, South Pelto 23, Eugene Island 243, Vermillion 255, 256, 267, 268, and 277 fields, and the wells in Weeks Island. According to CW1 and CW4, Canty and Mindy Stuart "created" or "made up" reserve numbers for fields, including for Stone's Vermillion 255 field.

Verbally Abusing And Intimidating Stone Personnel To Overstate Reserves

35. According to CW2, defendant Canty, along with Gerald Yunker and Mindy Stuart, verbally abused and intimidated Stone employees involved in calculating the reserve numbers and pressured Stone geologists and geophysicists to inflate Stone's reserve numbers.

Refusing to Write Down Reserves When The Well "Watered Out"

36. According to CW1, in 2003 or 2004, Stone personnel learned that a well in the South Pelto Block 23 field had produced the reserves attributed to an adjacent well. According to CW1, Canty knew the well had watered out but refused to reduce reserves accordingly. Stone later admitted in its October 6, 2005 press release, that the proved reserves for the South Pelto 23 field had been overstated by 20 billion cubic feet equivalent ("Bcfe").

Production Not Meeting Reserves

37. Since Stone's production forecasts were based on inflated proved reserves numbers, there was a continuous trend of Stone producing significantly less than the amount that had been reported as proved reserves. CW1 and CW2 confirmed that when production did not match the production forecasts because the forecasts had been based on inflated reserve numbers, management blamed production personnel and refused to write off reserves. For example, CW1

confirmed that when Canty would forecast that a well would produce five Bcfe and, in reality, it only produced one Bcfe, Canty would appear in CW1's office with a reserve report rolled up in his hand, shake it at CW1, and say "I don't care what you do, you just follow this report."

38. According to CW1, on June 4, 2004, a meeting was held in the third floor conference room at Stone that lasted several hours. Gerald Yunker said the meeting was to discuss "production problems." During the meeting, it was shown that Mindy Stuart did not consult with Stone engineers when determining Stone's proved reserves.

VI. SCIENTER

39. Throughout the Class Period, defendants had actual knowledge or, at a minimum, were severely reckless in disregarding, that Stone's proved reserves were overstated, and that the Company's financial statements were materially misstated. The following are indicia of defendants' scienter:

Defendants' Direct Involvement In Overstating Proved Reserves

40. CW1 and CW3 both confirmed that Canty controlled the determination of Stone's reported proved reserves. According to CW2, Canty reviewed the reserves for every field.

41. As explained above, defendant Canty, along with other senior management, including Gerald Yunker and Mindy Stuart, redrew geological maps to make them bigger to inflate reserves, threatened and intimidated employees into inflating reserves, and rejected attempts by Stone personnel to lower the reserves numbers.

42. As a result of the reserves overstatements, Stone's audit committee of the Board of Directors forced the resignation of those members of Stone's top management that pressured Stone personnel into overstating reserves – defendant Canty, Gerald Yunker and Mindy Stuart.

Defendants' Knowledge That Stone's Proved Reserves Were Overstated

43. As explained above, defendant Canty knew that Stone's proved reserves were overstated; indeed, Canty, Yunker, and Stuart orchestrated the overstating of proved reserves.

44. According to CW1, within two months of defendant Welch replacing Canty as President and CEO of Stone in April 2004, Welch knew that Stone's reported proved reserves were overstated. Specifically, according to CW1, beginning in May 2004, Larry Wellborn told Welch at least three times that "there were grave problems with the reserve estimations." CW4 confirmed that when Welch replaced Canty, Welch began researching Stone's reserve numbers and discovered that a substantial write down was in order (approx. 40 Bcfe).

45. In a conversation in the end of May 2004 between CW1, defendant Welch and Michael Madden (Vice President for Reserves), CW1 informed defendant Welch and Madden that Stone was experiencing problems meeting its production forecasts. When Welch asked CW1 why Stone's production unit could not meet the production forecasts, CW1 explained that it was because Stone's production forecasts were based on bogus, overstated reserve numbers.

Insider Trading

46. According to CW1, CW2, CW3, and CW4, it was common knowledge within the Company that Stone was overstating its proved reserves. The reserve overstatement caused Stone's reported net income and earnings per share to be overstated, and its reported depreciation, depletion and amortization ("DD&A") expense to be understated, for each quarter during the Class Period. Consequently, the price for Stone common stock was artificially inflated during the Class Period, while insiders reaped proceeds of \$50 million by selling over one million shares of their personal holdings of Stone stock. The insiders' sales, including that of Canty, Prince, and Yunker, were suspicious in timing and amount as follows:

47. During the Class Period, Canty sold 168,409 shares, or 39.91% of his holdings, thereby reaping \$7,718,028. Canty sold 12,500 shares on May 27, 2003 for a total of \$154,750; 3,909 shares on July 14, 2003 for a total of \$154,718; 42,000 shares on April 7, 2004 for \$2,013,060; and 110,000 shares on April 12, 2004 for \$5,395,500.

48. Defendant Prince reaped \$1,609,738 through insider sales during the Class Period by selling 10.44% of his holdings in July 2003 and June and August 2005, shortly after the Company began its investigation into the reporting of reserves, but before the Company first disclosed that its proved reserves were overstated.

49. Others in Stone's senior management who knew of the fraud similarly profited from the overstatement of proved reserves during the Class Period and resulting inflated stock price. For example, Gerald Yunker (Senior Vice President for Exploitation) sold 58.82% of his holdings in March 2005 (following the Company's announcement of year end 2004 financial results which were false as explained below at ¶¶107-110), reaping \$505,000.

50. The Philadelphia Stock Exchange has commenced an investigation into the Company's insider sales prior to the Company's first disclosure of its reserve overstatement on October 6, 2005.

Other Indicia Of Scienter

51. The following examples further demonstrate defendants' knowing and severely reckless conduct and that they had additional motives to overstate Stone's proved reserves:

(a) *Compensation Based On Reserves.* Stone implemented a bonus system which, contrary to established industry standards, rewarded employees based upon growing reserves. Beginning in February 2003, Stone adopted a Revised Annual Incentive Plan which awarded bonuses based on, among other things "the achievement of certain strategic objectives

as defined by our board of directors on an annual basis.” In Stone’s 2004 Form 10-K filed March 9, 2005, Stone disclosed that the “performance factors” which determined bonuses included “growing reserves.”

(b) *Increase Stone’s Asset Base, Credit and Borrowing Power.* As disclosed in the Company’s reports on Form 10-K for the years 2001 through 2005, “Stone’s borrowing based under [its credit facility], which is re-determined periodically, is based on an amount established by the bank group resulting from an evaluation of the value of our proved oil and gas reserves.” Based on Stone’s overstated proved reserves, the Company was able to increase its credit facility from \$200 million at the beginning of the Class Period to a high of \$500 million. Maintaining a high credit facility allowed defendants to fund acquisitions. For example, in October 2001, Stone acquired properties from Conoco using funds from its credit line and a bond offering which purportedly increased Stone’s proved reserves by 35%; and in November 2004, Stone acquired properties in the Williston Basin which then accounted for 8% of Stone’s proved reserves, and acquired additional working interests in the South Timbalier Blocks 143, 164, 165, 166, and 171, all of which were purchased using funds from its credit line, as reported in Stone press releases dated October 10, 2001 (Conoco), November 26, 2001 (Conoco), December 27, 2004 (Williston Basin), and November 18, 2004 (South Timbalier). Following revelations that Stone’s proved reserves had been overstated for at least four and one-half years, its banks reduced the Company’s credit line by \$200 million.

(c) *Fund Acquisitions Using Stock.* By overstating proved reserves, net income and earnings per share, defendants artificially inflated the price of Stone common stock, which was used as currency to acquire additional oil and gas properties. For example, in

February 2001, Stone acquired Basin Exploration, Inc. in a stock-for-stock merger valued at \$458 million – the largest acquisition in Stone’s history – using artificially inflated stock.

(d) *Boost Stone’s Credit Ratings.* Stone’s inflated proved reserves and financial results also caused credit rating agencies to rate the Company and its bond issues higher than they would have if the true condition of the Company had been known. During the Class Period, Stone made two bond offerings and used the funds, in part, to acquire additional oil and gas properties. On January 31, 2002, Stone issued \$200 million of bonds in a private offering and used the proceeds, in part, to fund its acquisition of properties from Conoco, as reported in Stone’s press release dated Dec. 5, 2001. Moody’s rated the 2002 Stone bond issue “B2.” On March 28, 2005, Stone announced that it had completed an exchange of \$200 million in senior subordinated notes for notes registered under the Securities Act of 1933. These notes also received a “B2” rating from Moody’s. As news of Stone’s overstated proved reserves and misstated financial results began to emerge, Moody’s downgraded its ratings of the Company, dropping from Ba3 to B1, and its debt, dropping its senior subordinated notes from B2 to B3.

(e) *Inadequate Internal Controls.* Defendants knew or were severely reckless in disregarding that Stone’s internal controls were inadequate. During the Class Period, Canty, Welch, Prince and Beer each certified with respect to Stone’s financial reports filed with the SEC that: (i) he was responsible for establishing and maintaining disclosure controls and procedures; (ii) he reviewed and evaluated the effectiveness of Stone’s disclosure controls and procedures; and (iii) based on this evaluation, Stone’s disclosure controls and procedures were effective to assure that the required information was disclosed. As Stone’s admissions now establish, there was no reasonable basis for such certifications. Stone has now admitted that there were “deficiencies in our internal controls that did not prevent the overstatement of our proved oil and

natural gas reserves,” and that the deficiencies “constituted a material weakness in our internal control over financial reporting.” Under GAAP, AU 325.15, a material weakness in internal control is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

VII. APPLICABLE REPORTING STANDARDS

SEC Standards For Reporting Proved Reserves

52. SEC rules dictate when a Company can report proved reserves in its SEC filings. Specifically, SEC Rule 4-10(a) of Regulation S-X establishes the financial accounting and reporting standards for entities engaged in oil and gas producing activities. It provides that a company can book “proved reserves” only if it can be demonstrated with “reasonable certainty” from geological and engineering data that the estimated quantities of crude oil, natural gas, and natural gas liquids will be recoverable from known reservoirs under existing economic and operating conditions. A reserve is “proved” if economic producibility is supported by either actual production or conclusive formation tests. Rule 4-10(a) delineates the specific situations in which proved reserves may be booked, and, importantly, specifically prohibits the recording of proved reserves in SEC filings where there is reasonable doubt that the well will produce oil or gas in the future. Rule 4-10(a)(2) provides in part:

i. Reservoirs are considered proved if economic producibility is supported by either actual production or conclusive formation test. The area of a reservoir considered proved includes (A) that portion delineated by drilling and defined by gas-oil and/or oil-water contacts, if any, and (B) the immediately adjoining portions not yet drilled, but which can be reasonably judged as economically productive on the basis of available geological and engineering data. In the

absence of information on fluid contacts, the lowest known structural occurrence of hydrocarbons controls the lower proved limit of the reservoir.

ii. Reserves which can be produced economically through application of improved recovery techniques (such as fluid injection) are included in the proved classification when successful testing by a pilot project, or the operation of an installed program in the reservoir, provides support for the engineering analysis on which the project or program was based.

iii. Estimates of proved reserves ***do not include the following:*** (A) oil that may become available from known reservoirs but is classified separately as indicated additional reserves; (B) crude oil, natural gas, and natural gas liquids, ***the recovery of which is subject to reasonable doubt because of uncertainty as to geology, reservoir characteristics, or economic factors;*** (C) crude oil, natural gas, and natural gas liquids, that may occur in undrilled prospects; and (D) crude oil, natural gas, and natural gas liquids, that may be recovered from oil shales, coal, gilsonite and other such sources. (Emphasis added.)

Generally Accepted Accounting Principles

53. As disclosed in Stone's financial statements for the fiscal year ended December 31, 2005, its estimate of proved reserves was revised downward during the year by 237 Bcfe. As a result, Stone restated its financial statements for prior years, for each of the quarters in 2001 through 2004, and for the first two quarters of 2005. The reduction in proved reserves impacted the amount of DD&A expense charged against income in Stone's consolidated income statements for the aforementioned periods and the carrying value of its proved oil and gas properties in its consolidated balance sheet as of December 31, 2004.

54. Statement of Financial Accounting Standards 19, Financial Accounting and Reporting by Oil and Gas Producing Companies ("SFAS 19"), requires the acquisition costs of proved properties to be amortized (depleted) by the unit-of-production method so that each unit produced is assigned a pro rata portion of the unamortized acquisition costs. Accordingly, the smaller the proved reserves (*i.e.*, the lesser the number of units), the greater is the unit cost. Therefore, the downward revision of estimated proved reserves resulted in an increase in unit costs and, consequently, an increase in DD&A expense of \$22,708,000 for 2004; \$17,968,000

for 2003; \$5,829,000 for the quarter ended March 31, 2005; \$6,723,000 for the quarter ended June 30, 2005; \$6,556,000, \$6,157,000, and \$5,395,000 for the quarters ended March 31, June 30, and September 30, 2004, respectively; and \$3,714,000, \$3,588,000 and \$3,941,000 for the quarters ended March 31, June 30, and September 30, 2003, respectively. DD&A expense is by far the largest component of Stone's operating expenses, comprising 60% or more of total operating expenses in each of the years 2005, 2004 and 2003.

55. As required by SFAS 19, Stone capitalizes the costs of its oil and gas producing assets. Indeed, Stone's proved oil and gas properties, which are reflected net of accumulated DD&A expense, are by far the largest asset on its consolidated balance sheet. They comprise, as of December 31, 2005 and 2004, nearly 75% and approximately 80% of total assets, respectively. As a result of the downward revision of estimated proved reserves and resulting increase in DD&A expense discussed above, Stone's accumulated DD&A expense as of December 31, 2004 was restated from \$1,516,620,000 as originally reported to \$1,640,362,000. This increase in accumulated DD&A expense as of December 31, 2004 is largely responsible for the decrease in the carrying value of Stone's proved oil and gas properties as of that date from \$1,489,498,000 as originally reported to \$1,376,151 as restated.

VIII. DEFENDANTS' MATERIALLY FALSE AND MISLEADING STATEMENTS AND OMISSIONS

56. Defendants' overstatements of Stone's proved reserves and misstatements of Stone's financial results inflated the price of Stone's common stock throughout the Class Period. Specifically, beginning with the Company's first quarter 2001 earnings release issued May 2, 2001, defendants made false statements regarding Stone's proved reserves and financial results. The results of the overstatement of the proved reserves and restated financial statements are quantified above in ¶28. The materially false and misleading statements were as follows:

Q1 2001

57. On May 2, 2001, the first day of the Class Period, defendants issued a press release reporting net income of \$39.3 million and earnings per share (“EPS”) of \$1.49 for the first quarter of 2001, the period ended March 31, 2001. The Company also reported net proved oil and gas properties valued at \$742 million and stated that its DD&A expense on oil and gas properties for the quarter totaled \$36.2 million. On May 3, 2001, Canty and Prince discussed Stone’s reserves and financial results during an earnings conference call with securities analysts and investors.

58. On May 14, 2001, Stone filed with the SEC its quarterly report on Form 10-Q for the first quarter of 2001, including the Company’s financial results reported in the Company’s earnings release dated May 2, 2001. Defendant Prince signed Stone’s Form 10-Q.

59. Each of the statements identified in ¶¶57-58 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company’s financial statements were false. Contrary to defendants’ representation, Stone’s proved reserves were not reported in accordance with SEC rules. Defendants overstated the quantity and value of Stone’s proved reserves causing a material overstatement of Stone’s net income and earnings per share and a material understatement of the Company’s DD&A expenses; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q2 2001

60. On August 2, 2001, Stone issued a press release reporting its financial results for the second quarter of 2001, the period ended June 30, 2001. The Company reported net income of \$29.1 million and EPS of \$1.10 per share for the quarter. The Company also reported net proved oil and gas properties valued at \$788 million and stated that its DD&A expense on oil and gas properties for the quarter totaled \$41.9 million. On August 7, 2001, defendants Canty and Prince discussed the Company's financial results during an earnings conference call with analysts and investors.

61. On August 9, 2001, Stone filed with the SEC its quarterly report on Form 10-Q for the second quarter of 2001, including the Company's financial results reported in the Company's earnings release dated August 2, 2001. Defendant Prince signed Stone's Form 10-Q.

62. Each of the statements identified in ¶¶60-61 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share and a material understatement of the Company's DD&A expense; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q3 2001

63. On November 5, 2001, Stone issued a press release reporting its financial results for the third quarter of 2001, the period ended September 30, 2001. The Company reported a loss of \$145.1 million or \$5.54 per share for the quarter. The Company also reported net proved oil and gas properties valued at \$593 million and stated that its DD&A expense on oil and gas properties for the quarter totaled \$47.1 million.

64. On November 13, 2001, Stone filed with the SEC its quarterly report on Form 10-Q for the third quarter of 2001, including the Company's financial results reported in the Company's earnings release dated November 5, 2001. Defendant Prince signed the Form 10-Q.

65. Each of the statements identified in ¶¶63-64 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the estimate of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share and a material understatement of the Company's DD&A expense; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q4 2001

66. On February 14, 2002, Stone issued a press release entitled "Stone Energy Corporation Announces 2001 Year-End Reserves and 2002 Capital Expenditures Budget" in

which it announced 2001 year-end proved reserves totaling 775.0 Bcfe. The Company stated that its proved reserves were prepared and presented “in accordance with the guidelines established by the SEC.”

67. On March 4, 2002, defendants issued a press release reporting a net loss of \$71.4 million or \$2.73 per share for year-end of fiscal 2001, and net income of \$5.4 million, or \$0.20 per share for the quarter ended December 31, 2001. The Company reported proved oil and gas properties valued at \$880.5 million at year-end and stated that its DD&A expense on oil and gas properties for the quarter and the year totaled \$32.8 million and \$158.9 million, respectively.

68. On March 19, 2002, Stone filed with the SEC its consolidated Annual Report on the Form 10-K for the year ended December 31, 2001, including the Company’s fourth quarter and Fiscal 2001 financial results reported in the Company’s earnings release dated March 4, 2002. The report was signed by defendants Canty and Prince. Stone reported in its 2001 Form 10-K that its estimated proved reserves totaled 775 Bcfe and that the reserve estimates were prepared in accordance with SEC rules.

69. Each of the statements identified in ¶¶66-68 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company’s financial statements were false. Stone’s reported proved reserves were overstated and, contrary to defendants’ representation, the estimate of proved reserves was not prepared in accordance with SEC rules. Defendants’ overstatement of the quantity and value of Stone’s proved reserves caused a material overstatement of Stone’s net income and earnings per share and a material understatement of the Company’s DD&A expense. As the Company later admitted, because the Company overstated its proved reserves, its loss for the year was understated by over 63%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q1 2002

70. On May 1, 2002, defendants issued a press release reporting net income of \$6.3 million, or \$0.24 per share, for the first quarter of 2002, the period ended March 31, 2002. The Company also reported net proved oil and gas properties valued at \$892 million and stated that its DD&A expense totaled \$40.7 million for the quarter. During an earnings conference call with analysts and investors on May 2, 2002, defendants Canty and Prince discussed the Company's reserves and financial results for the quarter.

71. On May 9, 2002, Stone filed with the SEC its quarterly report on Form 10-Q for the first quarter of 2002, including the Company's financial results reported in the May 1, 2002 earnings release. Defendant Prince signed Stone's Form 10-Q.

72. Each of the statements identified in ¶¶70-71 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination proved reserves was not prepared in accordance with SEC rules. Defendants determination the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share and a material understatement of the Company's DD&A expense; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results

of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q2 2002

73. On August 5, 2002, defendants issued a press release reporting net income of \$16.0 million and EPS of \$0.60 per share for the second quarter of 2002, the period ended June 30, 2002. The Company also reported net proved oil and gas properties valued at \$902.4 million and DD&A expenses of \$42.2 million for the quarter. On August 6, 2002, defendants Canty and Prince discussed the Company's reserves and financial results for the quarter during an earnings conference call with analysts and investors.

74. On August 14, 2002, Stone filed with the SEC its quarterly report on Form 10-Q for the second quarter of 2002, including the Company's financial results reported in the August 5, 2002 earnings release. Defendant Prince signed Stone's Form 10-Q. In addition, defendants Canty and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

75. Each of the statements identified in ¶¶73-74 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share and a material understatement of the Company's DD&A expense; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results

of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q3 2002

76. On November 11, 2002, defendants issued a press release reporting third quarter 2002 net income of \$13.7 million and EPS of \$0.52 per share. The Company also reported net proved oil and gas properties valued at \$920.5 million and DD&A expense of \$39.7 million. On November 12, 2002, defendants Canty and Prince, along with Gerald Yunker, discussed Stone's reserves and financial results during an earnings conference call with analysts and investors.

77. On November 12, 2002, Stone filed with the SEC its quarterly report on Form 10-Q for the third quarter of 2002, including the Company's financial results reported in the Company's earnings release dated November 11, 2002. Defendant Prince signed Stone's Form 10-Q. In addition, defendants Canty and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

78. Each of the statements identified in ¶¶76-77 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share and a material understatement of the Company's DD&A expense; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results

of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q4 2002

79. On February 18, 2003, defendants issued a press release entitled “Stone Energy Corporation Announces 2002 Year-End Reserves and 2003 Capital Expenditures Budget,” in which the Company announced year-end 2002 proved reserves of 750.8 Bcfe. Stone also stated that its proved reserves were “prepared in accordance with the guidelines established by the SEC.”

80. On March 10, 2003, defendants issued a press release reporting net income of \$19.5 million and \$55.4 million, or \$0.74 and \$2.09 per share, respectively, for the fourth quarter and year-end of 2002. The Company also reported net proved oil and gas properties valued at \$940.5 million for the year-end 2002, and DD&A expense of \$38.2 million and \$160.8 million for the quarter and year-end, respectively. On March 11, 2003, defendants Canty and Prince, along with Gerald Yunker, discussed the Company’s reserves and fourth quarter and year-end 2002 financial results in an earnings conference call with analysts and investors.

81. On March 19, 2003, Stone filed with the SEC its consolidated Annual Report on the Form 10-K for the year ended December 31, 2002, including the Company’s financial results for the fourth quarter and fiscal 2002 reported in the Company’s earnings release dated March 10, 2003. Stone further reported in the 2002 Form 10-K that its proved reserves totaled 750.8 Bcfe and that the reserves were prepared in accordance with SEC rules. Defendants Canty and Prince signed Stone’s Form 10-K. In addition, defendants Canty and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

82. Each of the statements identified in ¶¶79-81 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Defendants overstated Stone's reported proved reserves and, contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves by 21% causing a material overstatement of Stone's net income and earnings per share by 21% as of December 31, 2002 and a material understatement of the Company's DD&A expense by 8%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q1 2003

83. On May 7, 2003, defendants issued a press release entitled "Stone Energy Corporation Announces 773% Growth in Comparable Quarterly Earnings and Deep Gas Discovery in Coastal Louisiana Waters," in which the Company reported first quarter 2003 net income of \$55.9 million, or \$2.11 per share. The Company also reported net proved oil and gas properties valued at \$1.0 billion and a DD&A expense of \$41.7 million. On May 8, 2003, defendants Canty and Prince, along with Gerald Yunker, discussed the Company's reserves and first quarter 2003 financial results in an earnings conference call with analysts and investors.

84. On May 13, 2003, Stone filed with the SEC its quarterly report on Form 10-Q for the first quarter of 2003, the period ended March 31, 2003, including the Company's financial results reported in the Company's earnings release dated May 7, 2003. Defendant Prince signed

Stone's Form 10-Q. In addition, defendants Canty and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

85. Each of the statements identified in ¶¶83-84 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share by 3% and a material understatement of the Company's DD&A expense by 8%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q2 2003

86. On August 4, 2003, the Company issued a press release entitled "Stone Energy Corporation Announces Second Quarter 2003 Results," in which Stone reported second quarter 2003 net income of \$28.6 million, or \$1.08 per share, and a DD&A expense of \$41.0 million.

87. On August 5, 2003, defendants Canty and Prince, along with Gerald Yunker, participated in a conference call with securities analysts in which they discussed the Company's reserves and second quarter 2003 financial results.

88. On August 8, 2003, Stone filed with the SEC its quarterly report on Form 10-Q for the second quarter of 2003, including the Company's financial results reported in the Company's earnings release dated August 4, 2003. Defendant Prince signed Stone's Form 10-Q.

In addition, defendants Canty and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

89. Each of the statements identified in ¶¶86-88 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share by 9% and 10%, respectively, and a material understatement of the Company's DD&A expense by 8%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q3 2003

90. On November 3, 2003, defendants issued a press release reporting net income of \$22.8 million, or \$0.86 per share, and a DD&A expense of \$42.0 million for the third quarter of 2003, the period ended September 30, 2003. The Company also reported net proved oil and gas properties valued at \$1.1 billion for the quarter. On November 4, 2003, defendants Canty and Prince, along with Gerald Yunker, discussed the Company's reserves and third quarter 2003 financial results during an earnings conference call with analysts and investors.

91. On November 5, 2003, Stone filed with the SEC its quarterly report on Form 10-Q for the third quarter of 2003, including the Company's financial results reported in the Company's earnings release dated November 3, 2003. Defendant Prince signed Stone's Form

10-Q. In addition, defendants Canty and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

92. Each of the statements identified in ¶¶90-91 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share by 13% and 15%, respectively, and a material understatement of the Company's DD&A expense by 9%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q4 2003

93. On February 16, 2004, defendants issued a press release entitled "Stone Energy Corporation Announces 167% Reserve Replacement in 2003." The Company reported proved reserves of 816.3 Bcfe, as of December 31, 2003. Stone represented that reserves were prepared in accordance with the SEC rules.

94. On March 8, 2004, defendants issued a press release entitled "Stone Energy Corporation Announces Fourth Quarter and Year 2003 Results," in which Stone reported net income for the fourth quarter and year ended December 31, 2003 of \$27.2 million and \$134.5 million, or \$1.02 and \$5.07 per share, respectively, and a DD&A expense of \$46.1 million and \$168.0 million, respectively. The Company also reported net proved oil and gas properties

valued at \$1.2 billion for the year-end 2003. On March 9, 2004, defendants Canty, Prince, and Welch, along with Gerald Yunker, discussed the Company's reserves and financial results in an earnings conference call with analysts and investors.

95. On March 15, 2004, Stone filed with the SEC its annual report on Form 10-K for the quarter and year ended December 31, 2003, including the Company's financial results reported in the Company's earnings release dated March 8, 2004. Defendants Welch and Prince signed Stone's Form 10-K. In addition, defendants Welch and Prince certified the annual report pursuant to § 302 of the Sarbanes Oxley Act.

96. Each of the statements identified in ¶¶93-95 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Defendants overstated Stone's proved reserves and, contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves by 26% causing a material overstatement of Stone's net income and earnings per share for the quarter and year-end by 20% and 9%, respectively, and a material understatement of the Company's DD&A expenses for the quarter and the year by 13% and 10%, respectively; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q1 2004

97. On May 5, 2004, defendants issued a press release reporting net income of \$35.8 million, or \$1.33 per share, for the first quarter of 2004, the period ended March 31, 2004. The Company also reported net proved oil and gas properties valued at \$1.25 billion and a DD&A expense of \$46.7 million. On May 6, 2004, defendants Canty, Prince and Welch, along with Gerald Yunker, discussed the Company's reserves and financial results for the quarter during an earnings conference call with securities analysts and investors.

98. On May 7, 2004, Stone filed with the SEC its quarterly report on Form 10-Q for the first quarter of 2004, including the Company's financial results reported in the Company's earnings release dated May 5, 2004. Defendant Prince signed Stone's Form 10-Q. In addition, defendants Welch and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

99. Each of the statements identified in ¶¶97-98 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share by 14% and a material understatement of the Company's DD&A expense by 12%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q2 2004

100. On August 9, 2004, defendants issued a press release reporting net income of \$35.9 million, or \$1.33 per share for the second quarter of 2004, the period ended June 30, 2004. The Company also reported proved oil and gas properties valued at \$1.31 billion and a DD&A expense of \$50.1 million for the quarter.

101. On August 9, 2004, Stone filed with the SEC its quarterly report on Form 10-Q for the second quarter of 2004, including the Company's results reported in the Company's earnings release dated August 9, 2004. Defendant Prince signed Stone's Form 10-Q. In addition, defendants Welch and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

102. On August 10, 2004, defendants Welch and Prince, along with Mindy Stuart, discussed the Company's reserves and financial results for the quarter during an earnings conference call with analysts and investors.

103. Each of the statements identified in ¶¶100-102 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share by 13% and a material understatement of the Company's DD&A expense by 11%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results

of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q3 2004

104. On November 3, 2004, defendants issued a press release reporting net income of \$25.6 million, or \$0.95 per share, for the third quarter of 2004, the period ended September 30, 2004. The Company reported net proved oil and gas properties valued at \$1.3 billion and a DD&A expense of \$46.1 million. On November 4, 2004, defendants Prince and Welch, along with Gerald Yunker, discussed Stone's reserves and financial results for the quarter during an earnings conference call with analysts and investors.

105. On November 8, 2004, Stone filed with the SEC its quarterly report on Form 10-Q for the third quarter of 2004, including the Company's financial results reported in the Company's earnings release dated November 3, 2004. Defendant Prince signed Stone's Form 10-Q. In addition, defendants Welch and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

106. Each of the statements identified in ¶¶104-105 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share by 16% and 17%, respectively, and a material understatement of the Company's DD&A expense by 10%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results

of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q4 2004

107. On February 21, 2005, defendants issued a press release entitled “Stone Energy Corporation Announces Year-End Proved Reserves and Operational Update,” in which Stone announced year-end 2004 proved reserves of 825 Bcfe. The Company represented that its reserves were prepared in accordance with the SEC rules.

108. On March 1, 2005, defendants issued a press release reporting quarterly and year-end net income of \$37.7 million and \$134.9 million, or \$1.40 and \$5.01 per share, respectively, and DD&A expenses of \$45.2 million and \$188.2 million, respectively. The Company reported net proved oil and gas properties valued at \$1.5 billion for the year-end 2004. On March 2, 2005, Stone defendants Prince and Welch, along with Gerald Yunker, discussed the Company’s reserves and financial results in an earnings conference call with analysts and investors.

109. On March 9, 2005, Stone filed with the SEC its annual report on Form 10-K for the quarter and year ended December 31, 2004, including the Company’s financial results initially reported in the Company’s earnings release dated March 1, 2005. Defendants Welch and Prince signed Stone’s Form 10-K. In addition, defendants Welch and Prince certified the annual report pursuant to § 302 of the Sarbanes-Oxley Act.

110. Each of the statements identified in ¶¶107-109 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company’s financial statements were false. Defendants overstated Stone’s proved reserves and, contrary to defendants’ representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and

value of Stone's proved reserves by over 23% causing a material overstatement of Stone's net income and earnings per share for the quarter and the year by 9% and 13%, respectively, and a material understatement of the Company's DD&A expenses for the quarter and the year by 9% and 11%, respectively; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q1 2005

111. On May 4, 2005, defendants issued a press release reporting net income of \$37.3 million, or \$1.38 per share, for the first quarter of 2005, the period ended March 31, 2005. The Company also reported net proved oil and gas properties valued at \$1.56 billion and a DD&A expense of \$56.2 million. On May 5, 2005, defendants Welch and Prince, along with Gerald Yunker, discussed the Company's reserves and financial results during an earnings conference call with analysts and investors.

112. On May 6, 2005, Stone filed with the SEC its quarterly report on Form 10-Q for first quarter of 2005, the period ending March 31, 2005, including the Company's financial results reported in the Company's earnings release dated May 4, 2005. Defendant Prince signed Stone's Form 10-Q. In addition, defendants Welch and Prince certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

113. Each of the statements identified in ¶¶111-112 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share by 12% and 11%, respectively, and a material understatement of the Company's DD&A expense by 9%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

Q2 2005

114. On August 2, 2005, defendants issued a press release reporting net income of \$48.5 million, or \$1.79 per share, for the second quarter of 2005, the period ended June 30, 2005. The Company also reported net proved oil and gas properties valued at \$1.6 billion and a DD&A expense of \$65.7 million for the quarter. On August 3, 2005, defendants Welch and Prince, along with Gerald Yunker, discussed the Company's reserves and financial results for the quarter during an earnings conference call with analysts and investors.

115. On August 5, 2005, Stone filed with the SEC its quarterly report on Form 10-Q for the second quarter of 2005, including the Company's financial results reported in the Company's earnings release dated August 2, 2005. Defendants Welch and Beer certified the quarterly report pursuant to § 302 of the Sarbanes-Oxley Act.

116. Each of the statements identified in ¶¶114-115 was materially false and misleading when made because defendants knew, or were severely reckless in disregarding, that:

(a) The Company's financial statements were false. Contrary to defendants' representation, the determination of proved reserves was not prepared in accordance with SEC rules. Defendants overstated the quantity and value of Stone's proved reserves causing a material overstatement of Stone's net income and earnings per share by 10% and a material understatement of the Company's DD&A expense by 9%; and

(b) As Stone later admitted, the Company lacked adequate internal controls to ensure that the report fairly presented in all material respects the financial condition and results of operations and did not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements not misleading.

117. Stone admitted in the restatement that the total cumulative impact of the restatements on stockholders' equity as of June 30, 2005 was a reduction of approximately \$89.8 million, which includes a reduction in beginning stockholders' equity as of January 1, 2002 of approximately \$45.3 million.

118. Stone's restatement also establishes that the certifications made by its CFOs and CEOs during the Class Period, defendants Canty, Welch, Prince, and Beer, were false and misleading. As specified above, defendants Canty, Welch, Prince, and Beer signed Stone's financial statements and certified that they reviewed the effectiveness of Stone's controls and procedures and, based on that review, the disclosure controls and procedures were effective and the financial statements accurate. The Company has admitted in its restatement that it "identified deficiencies in our internal controls that did not prevent the overstatement of our proved oil and natural gas reserves," and that the deficiencies "constituted a material weakness in our internal control over financial reporting."

IX. THE TRUTH IS REVEALED

119. The truth about Stone's proved reserves, as well as the true state of its financial results, borrowing base and credit rating, was revealed in a series of announcements from October 6, 2005 through March 10, 2006, which caused Stone's stock price to plummet a total of \$16.99, or over 30%.

120. On the morning of October 6, 2005, in a press release entitled "Stone Energy Corporation Provides Production and Hurricane Update and Revisions to Reserves," Stone announced for the first time that it had conducted an internal review of its proved reserves resulting in a write down of 171 Bcfe, and that it was reducing its production guidance. The Company stated that no determination had been made as to the impact, if any, on prior periods, and Stone's audit committee had engaged outside consultants to review the matters.

121. Analysts and the market reacted to the negative news. For example, in an October 6, 2005 analyst report, KeyBanc Capital Markets emphasized the "bad news about large downward reserve revisions," and opined that Stone "is particularly challenged in replacing production and growing reserves." Similarly, a JPMorgan analyst report dated October 6, 2005 stated "SGY announced a writedown of 20% of its YE2004 proved reserves, erasing four years of net reserve increases."

122. Moody's reported that the "the direct impact of these reserve write-downs from a leverage perspective is significant," and lowered its ratings for Stone. The Corporate Family Rating was downgraded from Ba3 to B1. Both of Stone's senior subordinated notes were downgraded from B2 to B3.

123. As a result of the news described in ¶¶120-122, Stone's stock dropped from a closing price of \$56.07 on October 5, 2005, to \$48.14 on October 6, 2005, to \$47.93 on October 7, 2005.

124. After the close of the market on November 8, 2005, the Company announced that the reserve overstatement would require a restatement of its financial statements for 2001 through the second quarter of 2005, and that the Company hoped to file the amended reports by November 14, 2005. The Company summarized preliminary findings of the independent investigation by its outside investigators, Davis Polk & Wardwell ("Davis Polk"), including that there had been a "tone of optimism and aggressiveness set by management regarding reserve booking."

125. The next day, November 9, 2005, Stone held a conference call during which the Company provided additional information regarding the reserve overstatement and financial restatements, and further indicated that it was terminating its prior outside reserve engineering firm (Atwater) that reviewed its Gulf basin reserves, where the overstatements occurred. Defendant Welch explained that the "re-evaluation" of proved reserves was prompted when, during the prior year, Stone wrote down approximately 51 Bcfe in proved reserves. When, in the second quarter of 2005 it appeared that Stone needed to write down an additional 19 Bcfe in proved reserves, Welch became "concerned that we may have an issue that was broader than just the few reserves" so he requested a comprehensive review of all the reserves. Defendant Welch assured analysts and investors that there would not be any additional negative revisions beyond the 171 Bcfe previously reported on October 6, 2005. Stone's stock price continued decreasing due to the news described in ¶¶124-125, closing at \$42.67 on November 10, 2005.

126. On December 5, 2005, Stone announced the findings of the independent review of its proved reserves, including that: (i) Stone “lacked adequate internal guidance or training on the SEC standard for estimating proved reserves”; (ii) “some former members of Stone management failed to fully grasp the conservatism of the SEC’s ‘reasonable certainty’ standard of booking reserves”; and (iii) “there was an optimistic and aggressive ‘tone from the top’ with respect to determining proved reserves. Some of the Stone technical staff felt pressure to interpret the geological and engineering data in an aggressive manner; and there were several factors that may have prevented or discouraged the technical staff from pushing back against the optimistic tone from the top and the pressure that some perceived with respect to reserve estimation. In addition, there was evidence of a reluctance to write down proved reserves.”

127. On January 11, 2006, a Platts Oilgram News article stated that Stone is a “storm-tossed offshore operator,” that analysts “project only a 19% gain at Stone,” and that Stone “appeared primed to stay below the second quarter’s \$1.79/share with a fourth quarter projection of \$1.66.” Stone’s stock price dropped from \$47.38 on January 3, 2006 to \$45.89 on January 9, 2006, dropping again from \$46.21 on January 10, 2006 to \$44.60 on January 12, 2006.

128. On February 8, 2006, Stone provided additional information regarding the reserve overstatement, including a fourth quarter 2005 negative revision of 67 Bcfe. Also on February 8, 2006, the newspaper *The Independent* published an article titled “Stone Cold,” which criticized Stone for its overstatement of proved reserves, questioned the integrity of Stone’s management, and provided additional information about the resulting forced resignations and suspicious insider trading.

129. On February 8, 2006, RBC Capital Markets lowered its target price for Stone from \$49 to \$44. Similarly, on February 13, 2006, Lehman downgraded Stone's rating from equal to underweight.

130. In response to the February 8, 2006 news, Stone's stock dropped from \$46.53 on February 7, 2006 to \$41.59 on February 13, 2006.

131. After the close of the market on February 17, 2006, Stone announced that it had received notice of non-compliance from bondholders of over 25% of the outstanding principal amount of its 6.75% senior subordinated notes due 2014 for failure to timely file SEC reports and financials. Stone admitted that if acceleration were to occur, it would be unable to meet its payment obligations to the bondholders.

132. On February 21, 2006, Moody's downgraded Stone's Corporate Family Rating from B1 to B2. In addition, it downgraded the ratings on Stone's senior subordinated notes from B3 to Caal. Moody's stated that among other things, the ratings downgrade reflected "the company's announcement of a second significant negative reserve revision for fiscal 2005 which combined with the first announcement, results in total reserve reduction of nearly 30% from FYE 2004 levels despite the company's indication that it replaced 106% of 2005 production"

133. On February 22, 2006, the Company announced that it provided notice to Bank of America, as administrative agent for the banks party to the Credit Agreement, of receipt of the above-mentioned notices of non-compliance from bondholders. As a result of these actions, Stone was prohibited from borrowing funds until it cured the non-compliance issue.

134. On February 23, 2006, Moody's lowered Stone's Speculative Grade Liquidity Rating from SGL-3 to SGL-4 in response to the previous press release. The downgrade reflected

Stone's "announcement that it no longer has access to the undrawn capacity under the borrowing base of its revolving credit facility."

135. In response to the news in ¶¶131-134 above, Stone's stock dropped from \$44.16 on February 17, 2006 to \$41.40 on February 28, 2006.

136. After the close of the market on March 9, 2006, Stone announced its fourth quarter and year-end 2005 results and that it had completed the restatements of previously filed financial results for 2001 through second quarter 2005. Stone held an analyst conference call the next morning on March 10, 2006 and further explained its financial results. As noted by RBC Capital Markets on March 10, 2006, "[t]his was the first release of financial results since Stone announced it was taking a reserve writedown in October." RBC Capital Markets further stated:

DD&A charges were higher than expected because of the effects of the reserve writedown. This was going to be the main financial factor impacted by the reserve revision but this should not impact trading because E&Ps trade on cash flow multiples.

137. Also on March 10, 2006, Bear Stearns reported: "As of year-end 2005, SGY reported total proved reserves of 593 Bcfe, which was 28% lower than the 2004 year-end proved reserves of 825 Bcfe, which will probably be restated. Approximately 84 Bcfe of the reduction was due to production while approximately 238 Bcfe represented a downward revision of proved reserves." Thus, the market was informed that Stone's proved reserves had been overstated by 238 Bcfe, not 171 Bcfe, as the Company initially reported on October 6, 2005.

138. In response to the news, Stone's stock dropped again from \$39.49 on March 9, 2006 to \$39.08 on March 13, 2006. This stock price decrease was particularly significant in light of the *increase* in the relevant market index for energy companies (S6ENRS) during the same time period, which increased from 664.06 on March 10, 2006 to 674.51 on March 13, 2006.

139. In total, the release of the truth into the market caused Stone's stock price to plummet from a closing price of \$56.07 on October 5, 2006, to a closing price of \$39.08 on March 13, 2006, for a total of \$16.99, or over 30%.

X. CLASS ACTION ALLEGATIONS

140. Lead Plaintiff brings this action as a class action pursuant to Federal Rule of Civil Procedure 23(a) and (b)(3) on behalf of all those who purchased or acquired the common stock of Stone from May 2, 2001 through and including March 10, 2006, (the "Class"), and who were damaged thereby. Excluded from the Class are defendants, the officers, directors, and senior executives (Vice President and higher) of the Company, at all relevant times, members of their immediate families and their legal representatives, heirs, successors or assigns and any entity in which defendants have or had a controlling interest.

141. The members of the Class are so numerous that joinder of all members is impracticable. While the exact number of Class members is unknown to Lead Plaintiff at this time and can only be ascertained through appropriate discovery, Lead Plaintiff believes that the Class members number in the thousands. Record owners and other members of the Class may be identified from records maintained by Stone or its transfer agent and may be notified of the pendency of this action by mail, using the form of notice similar to that customarily used in securities class actions. As of March 30, 2006, the Company had approximately 27.27 million shares of common stock issued and outstanding.

142. At all relevant times, shares of Stone common stock actively traded on the New York Stock Exchange which is a highly efficient market. During the Class Period, Stone was followed and reported on by analysts at numerous securities firms, including Bear Stearns, Credit

Suisse First Boston, Hibernia Southcoast Capital, J.P. Morgan Securities, J.S. Herold & Co., Johnson Rice & Co., Key Banc Capital Markets, RBC Capital Markets, and others.

143. Lead Plaintiff's claims are typical of the claims of the members of the Class. Lead Plaintiff purchased Stone common stock during the Class Period at artificially inflated prices and has sustained damages arising out of the wrongful conduct alleged herein. Lead Plaintiff is a member of the Class and does not have interests antagonistic to, or in conflict with, the other members of the Class.

144. Lead Plaintiff will fairly and adequately protect the interests of the members of the Class and has retained counsel competent and experienced in class and securities litigation.

145. Common questions of law and fact exist as to all members of the Class and predominate over any questions solely affecting individual members of the Class. Among the questions of law and fact common to the Class are:

(a) Whether the federal securities laws were violated by defendants' acts as alleged herein;

(b) Whether statements made by defendants to the investing public during the Class Period misrepresented material facts about Stone's proved reserves and financial statements;

(c) Whether defendants acted knowingly or recklessly in misrepresenting material facts alleged herein; and

(d) To what extent the members of the Class have sustained damages and the proper measure of damages.

146. A class action is superior to all other available methods for the fair and efficient adjudication of this controversy since joinder of all members is impracticable. The expense and

burden of individual litigation makes it virtually impossible for many Class members individually to seek redress for the wrongful conduct alleged. Lead Plaintiff knows of no difficulty in the management of this action as a class action.

XI. CLAIMS FOR RELIEF

COUNT I

**Violations Of § 10(b) Of The Exchange Act And Rule 10b-5 Promulgated Thereunder
Against All Defendants**

147. Lead Plaintiff repeats and re-alleges each of the allegations set forth in the foregoing paragraphs as if fully set forth herein.

148. Throughout the Class Period, defendants individually and in concert, directly and indirectly, by the use and means of instrumentalities of interstate commerce and/or of the mails, engaged and participated in a continuous course of conduct to misstate material information about Stone, including its proved reserves and true financial results, as specified herein. Defendants employed devices, schemes and artifices to defraud while in possession of material, adverse non-public information and engaged in acts, practices and a course of conduct that included the making of, or participation in the making of, untrue and/or misleading statements of material facts.

149. Defendants Canty and Welch, as top executive officers of the Company, are liable as direct participants in the wrongs complained of herein. Through their positions of control and authority as officers of the Company, Canty and Welch were able to and did control the content of the public statements disseminated by Stone. With knowledge and/or severe reckless disregard that the reported proved reserves and financial results were false and misleading, Canty and Welch signed the false financial statements and caused the heretofore complained of public statements to contain misstatements of material facts as alleged herein.

150. Defendants Canty and Welch as CEOs and Directors, and Prince and Beer, as CFOs, are liable as direct participants in the wrongs complained of herein. Canty, Welch, Prince and Beer each signed certain financial statements indicated above and certified that: (i) he was responsible for establishing and maintaining disclosure controls and procedures, as well as evaluating the effectiveness of such disclosure controls and procedures; (ii) he reviewed and evaluated the effectiveness of Stone's disclosure controls and procedures; and (iii) based on this evaluation, Stone's disclosure controls and procedures were effective to assure that the required information is disclosed. Canty, Welch, Prince and Beer were, at a minimum, reckless in certifying the above statements, and the Company has since admitted that "[a] material weakness in internal control over financial reporting existed," and that because of the material weakness Stone's "disclosure controls and procedures were not effective in recording, processing, summarizing and reporting information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934."

151. Defendants acted with scienter throughout the Class Period, in that they either had actual knowledge of the misrepresentations of material facts set forth herein, or acted with reckless disregard for the truth. Canty, Welch, Prince and Beer were among the senior management of the Company, and were therefore directly responsible for the false and misleading statements disseminated to the public through press releases, analyst conference calls and filings with the SEC.

152. Defendants' misrepresentations were intentional or severely reckless and done for the purpose of enriching themselves at the expense of Lead Plaintiff and the Class and to conceal the Company's true condition from the investing public.

153. As a result of those deceptive practices and false and misleading statements, the market price of Stone's common stock was artificially inflated throughout the Class Period. In ignorance of the false and misleading nature of the representations described above, Lead Plaintiff and the other members of the Class, in reliance on either the integrity of the market or directly on the statements and reports of defendants, purchased Stone common stock at artificially inflated prices and were damaged thereby.

154. Had Lead Plaintiff and the other members of the Class known of the material adverse information not disclosed by defendants, or been aware of the truth behind defendants' material misstatements, they would not have purchased Stone common stock at artificially inflated prices.

155. By virtue of the foregoing, defendants have violated § 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder.

COUNT II

Violations Of § 20(a) Of The Exchange Act Against Defendants Canty, Welch, Prince and Beer

156. Lead Plaintiff repeats and re-alleges each of the allegations set forth in the foregoing paragraphs as if fully set forth herein.

157. Lead Plaintiff brings this claim against defendants Canty, Welch, Prince and Beer.

158. Defendants Canty, Welch, Prince and Beer, by virtue of their positions with Stone and their specific acts, were, at the time of the wrongs alleged herein, controlling persons of Stone within the meaning of § 20(a) of the Exchange Act. As explained above, they each had the power and influence and exercised the same to cause Stone to make the false statements alleged herein.

159. By reason of the conduct of Stone as alleged in this Complaint, defendants Canty, Welch, Prince and Beer are liable for the aforesaid false statements of Stone and liable to Lead Plaintiff and the Class for the substantial damages which they suffered in connection with their purchases or acquisitions of shares of Stone common stock as a result of Stone's violations of the Exchange Act.

XII. PRAYER FOR RELIEF

WHEREFORE, Lead Plaintiff prays for relief and judgment, as follows:

Determining that this action is a proper class action and certifying Lead Plaintiff as class representative under Rule 23 of the Federal Rules of Civil Procedure;

Awarding compensatory damages in favor of Lead Plaintiff and the other Class members against all defendants, jointly and severally, for all damages sustained as a result of defendants' wrongdoing, in an amount to be proven at trial, including prejudgment and post-judgment interest thereon; and

Awarding such other and further relief as the Court finds just and proper.

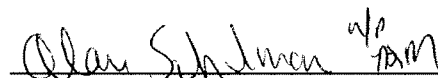
JURY DEMAND

Lead Plaintiff demands a trial by jury.

Respectfully submitted,

Dated: June 14, 2006

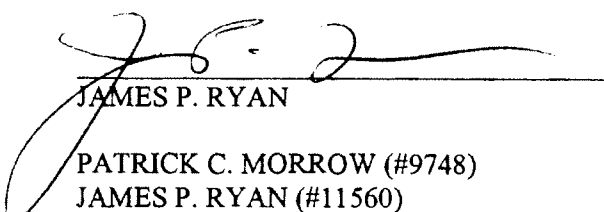
BERNSTEIN LITOWITZ BERGER
& GROSSMANN LLP


ALAN SCHULMAN

ALAN SCHULMAN
NIKI L. MENDOZA
BENJAMIN GALDSTON
MARION C. PASSMORE

12481 High Bluff Drive, Suite 300
San Diego, CA 92130
Tel: (858) 793-0070
Fax: (858) 793-0323
Lead Counsel For The Class

MORROW, MORROW, RYAN & BASSETT



JAMES P. RYAN

PATRICK C. MORROW (#9748)
JAMES P. RYAN (#11560)
Morrow, Morrow, Ryan & Bassett
Post Office Drawer 1787
Opelousas, LA 70571
(337) 948-4483
Liaison Counsel For the Class

ROBERT D. KLAUSNER
Klausner & Kaufman, P.A.
10059 N.W. 1st Court
Plantation, FL 33324
(954) 916-1202
*Additional Counsel For El Paso Firemen &
Policemen's Pension Fund*

22094.12

CERTIFICATE OF SERVICE

I, BRANDY ROBERTS, do hereby certify that on this 14th day of June, 2006, true and correct copies of the foregoing

- o CONSOLIDATED CLASS ACTION COMPLAINT
- o CERTIFICATE OF SERVICE & SERVICE LIST

were filed electronically. Those attorneys who are registered with the Electronic Case Filing (“ECF”) System may access this filing through the Court’s system, and notice of this filing will be sent to the parties by operation of the Court’s ECF System. Attorneys not registered with the Court’s ECF system will be duly and properly served via Express Mail or Federal Express (as indicated on the attached Service List), in accordance with the Federal Rules of Civil Procedure and the Court’s Local Rules.

/s/Brandy M. Roberts
BRANDY M. ROBERTS

SERVICE LIST

Patrick W. Gray
Amy E. Allums
JOHNSON, GRAY MCNAMARA
Post Office Box 51165
Lafayette, LA 70505
Tel: 337-412-6003
Fax: 337-412-6037
aea@jgmclaw.com
Electronic Notification

-and-

Walter B. Stuart IV
Hillary L. Preston
Clifford Thau
David R. Lurie
Ronald L. Oran
Ari M. Berman
Steven R. Paradise
Vinson & Elkins, L.L.P.
666 Fifth Avenue, 26th Floor
New York, NY 10103
Tel: 212/237-0000
Fax: 212-237-0100
Federal Express

Counsel for Stone Energy Corporation, David H. Welch, Kenneth H. Beer & James H. Prince, Defendants

Thomas A. Roberts
Rudy J. Cerone
MCGLINCHEY, STAFFORD
Post Office Box 60643
New Orleans, LA 70160-0643
Tel: 504-596-2786
Fax: 504-596-2760
rcerone@mcglinchey.com
Electronic Notification

Counsel for D. Peter Canty, Defendant