

**UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION**

LAWRENCE E. JAFFE PENSION PLAN,)	
On Behalf of Itself and All Others Similarly)	
Situated,)	
)	
Plaintiffs,)	
)	
v.)	No. 02 C 5893
)	
HOUSEHOLD INTERNATIONAL, INC., et al.,)	Judge Nan R. Nolan
)	
Defendants.)	

ORDER

Plaintiffs have filed this securities fraud class action alleging that Defendants Household International, Inc., Household Finance Corporation, and certain individuals (collectively, “Household”) engaged in predatory lending practices between July 30, 1999 and October 11, 2002 (the “Class Period”). In September 2004, the court deferred Plaintiffs’ damages disclosure obligations under Rule 26(a)(1)(C), explaining that “damages in securities fraud cases are generally an issue addressed by experts.” *Lawrence E. Jaffe Pension Plan v. Household Int’l, Inc.*, No. 02 C 5893, 2004 WL 2108410, at *1 (N.D. Ill. Sept. 21, 2004). In setting an expert discovery schedule several years later, the court reminded the parties to provide supplemental responses to discovery requests based on the expert reports. (Minute Order of 6/29/07, Doc. 1116.)

On August 15, 2007, Plaintiffs served Defendants with the expert report of Professor Daniel R. Fischel, quantifying the alleged artificial inflation in Household’s stock price during the Class Period. Exhibits 53 and 54 to the report present an “estimate of the stock’s true value (*i.e.*, the price at which the stock would have traded but for the alleged fraud, calculated as the difference between the stock price and artificial inflation) on each day of the Class Period.” (Report, at 23.) Professor Fischel also “quantified the amount of artificial inflation in Household’s stock price including the leakage of information related to the alleged fraud.” (*Id.* at 25.) Defendants argue that this report is deficient because it “does not indicate any amount of damages claimed by Plaintiffs, or provide

any method by which they contend damages should be computed, or offer any guidance as to which categories of class members would be eligible to recover in the event that Plaintiffs could prove any of their claims.” (Def. Mem., at 2.) For the reasons set forth here, the court finds Plaintiffs’ expert report inadequate in several respects, and grants the motion to compel.

DISCUSSION

Federal Rule 26(a)(1)(C) requires a party to provide “a computation of any category of damages claimed by the disclosing party,” including “the documents or other evidentiary material, not privileged or protected from disclosure, on which such computation is based, including materials bearing on the nature and extent of injuries suffered.” Failure to do so may result in a party being precluded from presenting the withheld information at trial. FED. R. CIV. P. 37(c)(1). Defendants argue that Plaintiffs should supplement their damages information in accordance with Rule 26(a)(1)(C), or be precluded from presenting any theory or calculation of damages not explicitly set forth in the Fischel report.

To prevail on a claim for damages under § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78(j)(b), and Rule 10(b)(5) promulgated thereunder, 17 C.F.R. § 240.10b-5, Plaintiffs must establish, among other things, (1) economic loss that is (2) caused by a material misrepresentation or omission by Defendants – i.e., “loss causation.” *Ray v. Citigroup Global Markets, Inc.*, 482 F.3d 991, 994 (7th Cir. 2007) (citing *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336, 341-42 (2005)); *In re Motorola Sec. Litig.*, ___ F. Supp. 2d ___, 2007 WL 487738, at *24 (N.D. Ill. Feb. 8, 2007). Defendants are correct that Plaintiffs cannot satisfy loss causation merely by showing that, at the time of purchase, the price of Household’s stock was artificially inflated by Defendants’ omissions or misrepresentations. *Dura*, 544 U.S. at 338. Professor Fischel’s report, however, is not limited to a statement that Household’s stock was artificially inflated. Rather, Professor Fischel identifies a variety of alleged misrepresentations or omissions made by Defendants, then specifies the amount by which Household’s stock price dropped when the truth

about those omissions and misrepresentations was revealed. (Report, at 6-18.) In making this assessment, Professor Fischel uses an event study regression analysis to “take out” non-fraud factors that caused Household’s stock price to decline. This sufficiently explains Plaintiffs’ theory of the causal connection between the decline in the price of Household’s stock and the revelation of the truth that was concealed by Defendants’ omissions or misrepresentations. *Dura*, 544 U.S. at 345.

Defendants object that the Fischel report nowhere uses the term “damages,” and insist that Plaintiffs must provide them with more information as to the class’ claimed aggregate economic loss. For example, Defendants argue that Plaintiffs must explain “whether investors who bought and sold their stock while the alleged inflation was in place [so-called “in-and-out” investors] would be excluded from any damages total.” Defendants also claim that they are entitled to know “whether Plaintiffs or their expert would, *inter alia*, net gains and losses resulting from multiple purchases and sales of stock by particular investors or groups of investors.” (Def. Mem., at 6.) In addition, Defendants question whether Plaintiffs intend to seek damages on behalf of class members who sold stock during the period of “negative inflation” identified in the report, and whether Plaintiffs claim damages for inflation already present in the price of the stock on the first day of the Class Period. (Def. Reply, at 3.) Plaintiffs respond that these matters may be addressed in Professor Fischel’s rebuttal report, and during the claims process to administer individual claims. (Pl. Resp., at 5.)

In the event Plaintiffs prevail at trial on the issue of liability, the next step will be to determine whether each individual class member has suffered actual economic loss. In making this determination, the court must (1) decide what methodology to employ – i.e., whether gains and losses should be aggregated or netted (the “netting approach”) or assessed individually (the “transactional approach”); and (2) determine the damage period. *Rocker Mgmt., LLC v. Lernout & Hauspie Speech Prods. N.V.*, No. 00-5965 (PGS), 2007 WL 2814653, at *14 (D.N.J. Sept. 24,

2007); *In re Cigna Corp. Sec. Litig.*, 459 F. Supp. 2d 338, 350 (E.D. Pa. 2006). “[U]sing the netting or transactional approach is a fact-sensitive inquiry . . . best accomplished on a case-by-case basis.” *Id.*

Professor Fischel’s report adequately sets forth Plaintiffs’ view of the proper damage period applicable in this case. Specifically, Professor Fischel notes that the Class Period begins on July 30, 1999; identifies November 15, 2001 as “the earliest date I found that Household’s stock price was negatively affected by the alleged fraud”; and analyzes the stock price through the end of the Class Period, October 11, 2002. (Report, at 5, 16.) *See also Rucker Mgmt.*, 2007 WL 2814653, at *15 (the damage period in a securities fraud class action is “generally the period of time during which plaintiffs allege that the stock price of the defendant corporation was inflated due to fraudulent statements made by company management, and ends when corrective statements are made (usually accompanied by a drop in price).”) To the extent Professor Fischel has found the stock price artificially inflated as of the first day of the Class Period, Defendants may depose him to determine whether this inflation stems from alleged misrepresentations made prior to the beginning of the Class Period.

As for “in-and-out” investors, Professor Fischel has supplied a quantification of the amount of artificial inflation that includes “the leakage of information related to the alleged fraud.” (*Id.* at 25.) This indicates that Plaintiffs intend to seek damages for in-and-out investors. *See In re Flag Telecom Holdings, Ltd. Sec. Litig.*, ___ F.R.D. ___, 2007 WL 2596775, at *17-18 (S.D.N.Y. Sept. 4, 2007) (noting that where plaintiffs allege multiple disclosures and prove a “leakage theory,” in-and-out investors may be able to establish loss and loss causation). That said, the court agrees that Plaintiffs must clarify which of Professor Fischel’s tables will be used for each type of investor (e.g., will Exhibit 56 apply only to in-and-out investors while Exhibit 53 will apply to other investors?)

The other element missing from Professor Fischel’s report is Plaintiffs’ view of the proper methodology to use in calculating individual damages. Though this will not become relevant until

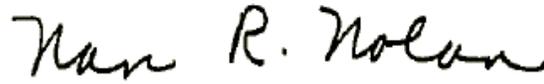
the claims process, Defendants are entitled to know Plaintiffs' theory now so their expert can provide a response. Plaintiffs need not provide specific individual calculations at this time, but they must identify their proposed method of calculating those damages should they prevail on the issue of liability. This should include a statement as to (1) whether Plaintiffs intend to use a netting or transactional approach for class members who profited from some trades but suffered losses from others; (2) Plaintiffs' proposed method of calculating damages on behalf of class members who sold their stock during the negative inflation period identified in Professor Fischel's report; (3) whether Plaintiffs intend to claim damages for inflation already present in the stock price on the first day of the Class Period; and (4) the estimated aggregate damages claimed by the class as a whole.

CONCLUSION

For the reasons stated above, Defendants' Motion to Compel [Doc. 1135] is granted. Plaintiffs must provide the supplemental information required by this Order no later than October 31, 2007.

Dated: October 17, 2007

ENTER:



NAN R. NOLAN
United States Magistrate Judge