UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF ILLINOIS

EASTERN DIVISION

LAWRENCE E. JAFFE PENSION PLAN, ON BEHALF OF ITSELF AND ALL OTHERS SIMILARLY SITUATED,	Lead Case No. 02-C5893 (Consolidated)
Plaintiff,	CLASS ACTION
- against -	Judge Ronald A. Guzman
HOUSEHOLD INTERNATIONAL, INC., ET AL.,	
Defendants.	

APPENDIX OF UNREPORTED AUTHORITIES SUBMITTED IN SUPPORT OF DEFENDANTS' OMNIBUS MOTION *IN LIMINE* TO EXCLUDE OR LIMIT 14 CATEGORIES OF EVIDENCE

CAHILL GORDON & REINDEL LLP
80 Pine Street
New York, New York 10005
(212) 701-3000

EIMER STAHL KLEVORN & SOLBERG LLP
224 South Michigan Avenue
Chicago, Illinois 60604
(312) 660-7600

Attorneys for Defendants Household International, Inc., Household Finance Corporation, William F. Aldinger, David A. Schoenholz, Gary Gilmer and J. A. Vozar

TABLE OF CASES

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Exhibit 1

LEXSEE 2005 US DIST LEXIS 531

IRENE ABRAMS, on behalf of herself and all others similarly situated, Plaintiffs, v. VAN KAMPEN FUNDS, INC., VAN KAMPEN INVESTMENT ADVISORY CORPORATION, VAN KAMPEN PRIME RATE INCOME TRUST, RICHARD F. POWERS, III, STEPHEN L. BOYD, and DENNIS J. McDONNELL, Defendants.

No. 01 C 7538

UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION

2005 U.S. Dist. LEXIS 531; Fed. Sec. L. Rep. (CCH) P93,072

January 12, 2005, Decided
January 13, 2005, Docketed

SUBSEQUENT HISTORY: Settled by, Claim dismissed by *Abrams v. Van Kampen Funds, Inc., 2006 U.S. Dist. LEXIS 2129 (N.D. Ill., Jan. 18, 2006)*

PRIOR HISTORY: *Abrams v. Van Kampen Funds, Inc., 2004 U.S. Dist. LEXIS 11730 (N.D. Ill., June 24, 2004)*

DISPOSITION: Plaintiffs' Motions In Limine granted in part and denied in part.

COUNSEL: [*1] For IRENE ABRAMS, ON BEHALF OF HERSELF AND ALL OTHERS SIMILARLY SITUATED, Plaintiff: Marvin Alan Miller, Matthew Eric Van Tine, Jennifer Winter Sprengel, Miller Faucher and Cafferty, LLP, Chicago, IL; Joel H Bernstein, Christopher J. Keller, Stephanie E Katz, David J Goldsmith, Goodkind, Labaton, Rudoff & Sucharow, New York, NY; Paul Jeffrey Geller, Cauley Gellar Bowman & Coates, LLP, Boca Baton, FL.

For VAN KAMPEN FUNDS, INC., INVESTMENT VAN KAMPEN, INVESTMENT ADVISORY CORP., HOWARD TIFFEN, RICHARD F POWERS, III, STEPHEN L BOYD, DENNIS J MCDONNELL, JEFFREY W MAILLET, Defendants: Michael B Slade, Kirkland & Ellis LLP, Chicago, IL; William H. Pratt, Joseph Serino, Jr, Maria Ginzburg, Kirkland and Ellis, New York, NY.

For VAN KAMPEN PRIME RATE INCOME TRUST, Defendant: Charles F. Smith, Jr., Lee Price Garner, Skadden Arps Slate Meagher & Flom, LLP, Chicago, IL; Joseph Serino, Jr, Maria Ginzburg, Kirkland and Ellis, New York, NY; Victoria Aisen Birov, Law Offices of Victoria A. Birov, Wilmette, IL

JUDGES: WILLIAM T. HART, UNITED STATES DISTRICT JUDGE.

OPINION BY: WILLIAM T. HART

OPINION

MEMORANDUM OPINION AND ORDER

A. BACKGROUND

This is a consolidated class action alleging [*2] federal securities violations involving defendant Van Kampen Prime Rate Income Trust's (the "Fund") valuation of senior loans and is subject to the Private Securities Litigation Reform Act of 1995 ("PSLRA"), *15 U.S.C. § 77z-1*. A class has been certified consisting of all persons who purchased shares in the Fund between September 30, 1998 and March 26, 2001, inclusive, with defendants and certain related parties excluded. *See Abrams v. Van Kampen Funds, Inc., 2002 U.S. Dist. LEXIS 16022, 2002 WL 1989401 (N.D. Ill. Aug. 27, 2002)* ("*Abrams II*"). Named as defendants are the Fund; Van Kampen Funds, Inc. ("Van Kampen"), the Fund's administrator; Van Kampen Investment Advisory Corp. (the "Adviser"), the Fund's investment adviser; Richard Powers, Fund Chairman of the Board, President, and Trustee during the relevant time period; Dennis McDonnell, former Fund Chairman of the Board, President, and

Trustee and Fund Portfolio Manager from July 1999 until December 1999; and Stephen Boyd, Fund Executive Vice President and Chief Investment Officer and Adviser Officer during the relevant time period. Count I of the Consolidated Amended Complaint alleges violations of § 11 of the [*3] Securities Act, *15 U.S.C. § 77k*, against Van Kampen, the Fund, Powers, McDonnell, and Boyd. Against Van Kampen and the Adviser, Count III alleges control person liability under § 15 of the Securities Act, *15 U.S.C. § 77o*, based on the alleged *§ 11* violations. [1] Following a ruling on the parties' cross motions for summary judgment, *see Abrams v. Van Kampen Funds, Inc., 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 (N.D. Ill. June 25, 2004)* ("*Abrams III*"), the parties filed their final pretrial order. Pending are the parties' various motions in limine.

1 Claims for violations of § 12 of the Securities Act, *15 U.S.C. § 77l*, and state law claims, as well as claims against two individual defendants, were voluntarily dismissed. Following notice and a fairness hearing, the voluntary dismissal of those claims was approved by the court. *See* Order dated Dec. 8, 2004. *See also Abrams v. Van Kampen Funds, Inc., 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 *1 n.1, *9 n.3 (N.D. Ill. June 25, 2004).*

[*4] Plaintiffs contend that defendants violated *§ 11* by making the following misrepresentations in various prospectuses that were issued during the class period. First, plaintiffs contend that defendants misrepresented the value of shares of the Fund in that they overvalued the loans held by the Fund. Plaintiffs contend that using available market quotations and properly determining fair value based on what the loans would have currently sold for would have resulted in lower daily net asset values ("NAV") for the Fund. Second, plaintiffs contend the prospectuses contained misrepresentations that the Fund used market quotations where available when this was not done. [2]

2 Allegations regarding misrepresentations as to the Fund's goals were dismissed on summary judgment. *See Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *9.*

To succeed on their *§ 11* claims, plaintiffs must show that defendants were responsible for untrue statements of material fact or omitted material facts in a prospectus. *See Herman & MacLean v. Huddleston, 459 U.S. 375, 381-82, 74 L. Ed. 2d 548, 103 S. Ct. 683 (1983)*; [*5] *Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *1*; *Ong v. Sears, Roebuck & Co., 2004 U.S. Dist. LEXIS 19425, 2004 WL 2534615 *16 (N.D. Ill. Sept. 24, 2004)*. There is no scienter or reliance requirement; instead responsible persons are liable for the material and misleading statements contained in a prospectus unless they can affirmatively make certain showings as to their knowledge and diligence. *See Herman, 459 U.S. at 382*; *Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 2534615 at *1*; *Ong, 2004 U.S. Dist. LEXIS 19425, 2004 WL 2534615 at *16*. A misstatement is material if there is a substantial likelihood that it would be viewed by a reasonable investor as significantly altering the total mix of available information and thus important to the investor's decision to invest. *TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449, 48 L. Ed. 2d 757, 96 S. Ct. 2126 (1976)*; *Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *1*; *Ong, 2004 U.S. Dist. LEXIS 19425, 2004 WL 2534615 at *32*.

Here, a central issue for plaintiffs' claims is the method of valuing the senior loans held by the Fund. The parties do not dispute that the applicable general principle is that the loans were to be valued on a daily basis at the amount that could have [*6] been obtained from a current sale. *See* SEC Accounting Release Series No. 118, 1970 WL 5621 *4 (Dec. 30, 1970) ("ASR 118"); *Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *2*; *In re Allied Capital Corp. Securities Litigation, 2003 U.S. Dist. LEXIS 6962, 2003 WL 1964184 *1 (S.D.N.Y. April 25, 2003)*; *In re Eaton Vance Corp. Securities Litigation, 206 F. Supp. 2d 142, 151-52 (D. Mass. 2002)*. *See also 15 U.S.C. § 80a-2(a)(41)(B)*; *17 C.F.R. § 270.2a-4(a)*. The parties also agree that current value is to be determined by "market quotations" where "readily available," or by "fair value" methods if market quotations are not readily available. *See 15 U.S.C. § 80a-2(a)(41)(B)*; *17 C.F.R. § 270.2a-4(a)(1)*; ASR 118, 1970 WL 5621 at *3; *Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *2*; *Eaton Vance, 206 F. Supp. 2d at 147*. Regarding the class period, the parties disagree as to whether the pricing services that were then available qualified as readily available market quotations. To qualify as readily available market quotations that [*7] must be used to value securities, the pricing services must provide quotes that are sufficiently timely, sufficiently frequent, and sufficiently accurate. *Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *2*; *Eaton Vance, 206 F. Supp. 2d at 148-49*. On summary judgment, it was held that genuine factual disputes existed as to when market quotations first became readily available. *See Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *4-6*. It was also held that genuine factual disputes existed as to defendants' affirmative defense that they acted with due diligence in exercising their business judgment in determining that market quotations were not yet readily available. *See 2004 U.S. Dist. LEXIS 11730, [WL] at *6*. Additionally, it was held that genuine factual disputes existed as to whether defendants determined the value of loan assets in the manner described in the pertinent prospectuses. *See 2004 U.S. Dist. LEXIS 11730, [WL] at *7-8.* The parties' agreed statement of contested issues of fact and law is consistent with the foregoing. *See* Proposed Final Pretrial Order Exh. B.

In light of the contested issues and other background described above, rulings will be made as to the pending motions in limine. Plaintiffs' motions [*8] in limine will be considered first.

B. PLAINTIFFS' MOTIONS IN LIMINE

1. To Bar Evidence that Traders Issued False Loan Pricing Data [138-1]

Defendants contend that certain pricing services were unreliable because they were based, in part, on market participants reporting the price at which they would sell or purchase loans, not actual sales. Defendants contend such reports were particularly unreliable because a significant number of market participants would overstate or understate the price so as to gain an advantage when actually selling or buying. Plaintiffs seek to bar any evidence of such manipulative price reporting on the ground that any such evidence is hearsay based on rumors, with there being no potential testimony based on personal knowledge.

Defendants contend that Allison Taylor can properly provide such testimony. She is a former senior loan trader, a founding member of the Loan Syndication and Trading Association ("LSTA"), [3] LSTA's initial Chairman, and, since 1998, the executive director of LSTA and LSTA/LPC. Defendants contend she can testify from personal experience and knowledge regarding her observations as to how LSTA/LPC functions. [*9] Defendants also point to disclaimers on LSTA/LPC forms regarding the pricing being based on estimated values provided by dealers, not necessarily actual trades. Taylor certainly can testify as to LSTA/LPC's procedures and methodologies. The question is whether any testimony that she believes market participants manipulated price reports would be inadmissible speculation or an observation based on personal experience.

3 LSTA is a senior loan pricing service first formed in 1995. In 1999, it merged with the Loan Pricing Corporation ("LPC"), which had began gathering data on senior loans in 1985. *See Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *5-6.*

Since neither party provides Taylor's deposition testimony that is pertinent to this motion [4], this issue cannot be resolved on the documents before the court. If Taylor were to testify that others told her participants were manipulating their price reports, that would be inadmissible hearsay. If she were to testify that she determined that actual participants [*10] were manipulatively reporting prices, that would likely be testimony based on personal observations. As long as there is a proper foundation, she could report such observations and conclusions. She need not be an expert to provide such testimony. *See Fed. R. Evid. 701.* At this time, with a very limited description of the testimony, no ruling can be made as to the admissibility of Taylor's testimony on this subject. Also, a question remains as to whether defendants actually relied on Taylor's findings.

4 Short excerpts of Taylor's deposition testimony in this case and another case are provided regarding other motions in limine.

Defendants also contend that they have "corroborating evidence" that is consistent with Taylor's observations. This consists of testimony from Van Kampen representatives regarding conversations with senior loan market participants making clear they had no intention of honoring bids or asks they had reported and an email from a Citibank trader expressing [*11] concerns about price reporting manipulation. Defendants do not contend that this evidence is admissible to prove the truth of the matters reported by the participants and Citibank trader. They instead contend that it is admissible to show defendants' reasoning in not accepting certain price information. Plaintiffs contend that is an irrelevant purpose because intent need not be shown to prove a *§ 11* violation. However, information available to defendants would be relevant to defendants' business judgment defense. This evidence will not be excluded. If desired, plaintiffs may submit a proposed limiting instruction regarding the jury's use of this evidence.

This motion in limine will be denied as to the "corroborating evidence." As to Taylor's testimony, the motion will be denied without prejudice to raising objections at trial.

2. To Exclude the Testimony of Kevin Meenan and Anthony DeLuca [139-1]

At trial, defendants intend to call Kevin Meenan as a witness and may call Anthony DeLuca. Meenan started a senior loan pricing service while working for his own firm. That firm was later purchased by Societe Generale Bank ("SocGen") and Meenan continued to provide pricing [*12] services through SocGen. SocGen was one of the pricing services used by the Fund. DeLuca was a managing director for Morgan Stanley, the parent of Van Kampen. In 1999, DeLuca conducted a review of third-party pricing of senior loans, including pricing by LPC, and reported his findings to Van Kampen's Board.

Plaintiffs object to both witnesses on the ground that they were not disclosed in response to interrogatories. Plaintiffs also contend that these two would be expert witnesses, but were not disclosed as such and no expert reports were provided. Defendants contend they did not have to update their interrogatory responses because these two potential witnesses were disclosed to plaintiffs during deposition testimony. Defendants contend they are fact witnesses, not experts.

There is no dispute that Meenan and DeLuca were omitted from certain discovery responses for which their names and knowledge or involvement would have been responsive to the queries. However, defendants were not required to supplement those prior responses if the corrective information was otherwise made known to plaintiffs during the discovery process. *See Fed. R. Civ. P. 26(e)* [*13] . Also, even if there was an improper failure to disclose, the evidence should not be excluded if the nondisclosure was harmless. Here, Meenan's role at SocGen was disclosed during two depositions, including a Van Kampen Vice President testifying that Meenan was the person at SocGen most knowledgeable about third-party pricing. DeLuca's involvement in the review was disclosed in the deposition of Van Kampen's General Counsel and the Board minutes for the meeting at which he made his report. Meenan's and DeLuca's knowledge and potential as witnesses were adequately disclosed during discovery. Therefore, defendants were not obliged to supplement their prior interrogatory responses.

Plaintiffs still complain that the witnesses were not disclosed as providing expert testimony. Since these witnesses were not retained or specially employed to provide expert testimony, the requirement of providing an expert report cannot apply to their testimony. *See Fed. R. Civ. P. 26(a)(2)(B)*; *Musser v. Gentiva Health Services, 356 F.3d 751, 756-57 (7th Cir. 2004)*. If some of their testimony would include opinions "based on scientific, technical, [*14] or other specialized knowledge," then they should have been disclosed as expert witnesses in accordance with *Fed. R. Civ. P. 26(a)(2)(A)*. *Musser, 356 F.3d at 756* & n.2.

It is doubtful that Meenan and DeLuca would be testifying as experts. Like Taylor, Meenan can testify about practices at SocGen, including drawing conclusions and expressing some opinions about what happened there, without having to rely on scientific, technical, or specialized knowledge. And even if his testimony could be properly characterized as including some expert testimony, the deposition testimony disclosing his role at SocGen would have served to disclose that possibility. Meenan's testimony would not be excluded for failure to name him as an expert. DeLuca's testimony also does not appear likely to include expert testimony. Presumably he will testify as to what he reported to the Board and possibly as to methods he used during his investigation. But, even if some of DeLuca's testimony is properly classified as expert testimony, his potential testimony was also adequately disclosed. His testimony will not be excluded.

Although there was discovery in [*15] which Meenan and DeLuca were disclosed and therefore no technical violation of *Rule 26*, defendants still should have clarified to plaintiffs that Meenan and DeLuca were potential witnesses, especially if defendants have any intention of eliciting expert testimony from either witness. Counsel for defendants likely were aware of Meenan's and DeLuca's roles prior to their names being mentioned at depositions and should have disclosed them prior to the depositions. Moreover, as plaintiffs point out, they were limited as to the number of witnesses they were permitted to depose and therefore focused on persons who were expressly named by defendants as potential witnesses. Had Meenan and DeLuca been expressly identified by defendants, plaintiffs may have chosen to depose one or both of them. The court will exercise its discretion to reopen discovery for the limited purpose of permitting the deposition of these two witnesses. However, DeLuca is listed as a possible witness, not a definite witness. If defendants represent to plaintiffs that they have decided not to use him as a witness, plaintiffs will not be permitted to depose DeLuca and defendants will not be permitted to present him at [*16] trial.

For the foregoing reasons, this motion in limine will be granted in part and denied. Plaintiffs may depose Meenan and DeLuca within 45 days after the date of today's order.

3. To Exclude the Testimony and Report of Michael P. McAdams [140-1]

Michael P. McAdams, whom defendants intend to use as an expert witness, has more than 20 years of experience in investment management and banking. From its inception in 1988 until 1995, he managed Pilgrim Prime Rate Trust, the first retail, floating-rate loan fund. Since 1995, he has had high-level positions at two other asset management firms. He was an early member of LSTA and has served on its Board, including as Chairman of the Board. He has also been a member of LSTA's valuation project committee. Plaintiffs do not dispute that he has the credentials to be an expert in the field of senior loans. However, plaintiffs contend that the opinions expressed in his expert report are not adequately supported and therefore he does not meet the requirements to testify as an expert that are set forth in *Fed. R. Evid. 702* and *Daubert v. Merrell Dow Pharmaceuticals, Inc., 509 U.S. 579, 125 L. Ed. 2d 469, 113 S. Ct. 2786 (1993)*. [5]

5 Although the title of plaintiffs' motion refers to excluding McAdams's report, the request for relief refers only to excluding his testimony. The report itself would not be admissible evidence absent a stipulation by the parties that the report itself represents McAdams's testimony.

[*17] In 2000, *Rule 702* was amended to conform with *Daubert* and its progeny, including *Kumho Tire Co. v. Carmichael, 526 U.S. 137, 143 L. Ed. 2d 238, 119 S. Ct. 1167 (1999)*. Expert testimony is not to be presented to a jury unless "(1) the testimony is based upon sufficient facts or data, (2) the testimony is the product of reliable principles and methods, and (3) the witness has applied the principles and methods reliably to the facts in the case." *Fed. R. Evid. 702*. *Daubert, 509 U.S. at 592-94*, sets forth a list of factors to consider in determining reliability. The list is not definitive; particular factors in that list may or may not be pertinent in evaluating particular expert testimony. *Kumho, 526 U.S. at 150-51* (quoting *Daubert, 509 U.S. at 593*); *United States v. Romero, 189 F.3d 576, 584 (7th Cir. 1999), cert. denied, 529 U.S. 1011, 146 L. Ed. 2d 232, 120 S. Ct. 1286 (2000)*. The *Rule 702* inquiry is "flexible." *Kumho, 526 U.S. at 150* (quoting *Daubert, 509 U.S. at 594*). The flexibility of the inquiry is particularly important to keep in mind when the field of expertise is not a scientific [*18] one as in *Daubert*. *See Romero, 189 F.3d at 584*; *Pease v. Prod. Workers of Chi. & Vicinity Local 707, 2003 U.S. Dist. LEXIS 14751, 2003 WL 22012678 *4 (N.D. Ill. Aug. 25, 2003)*. In determining the reliability of the proffered testimony, the focus must be on the soundness of the methodology that is used, not on whether the conclusions that the expert reaches are correct. *Deputy v. Lehman Brothers, Inc., 345 F.3d 494, 506 (7th Cir. 2003)*; *Dewick v. Maytag Corp., 324 F. Supp. 2d 894, 898 (N.D. Ill. 2004)*; *Pease, 2003 U.S. Dist. LEXIS 14751, 2003 WL 22012678 at *4*.

McAdams presently offers the following five opinions: [6]

> 2. Market quotations in the traditional sense--i.e. prices that reflect where bona fide transactions between willing buyers and sellers actually took place or where a buyer or seller definitely would transact business--do not exist in the senior loan market except in the most unusual and unpredictable circumstances. Market indications are not the same thing as market quotations.
>
> 3. From September 1998 through January 25, 2000, Van Kampen's method of valuing senior loans, and particularly how it used third-party pricing data when [*19] and if it was reasonably available, was consistent with the markets' development at that time and was consistent with the methodology set forth in the prospectus.
>
> 4. In January 2000, Van Kampen's decision to base its fair value determinations on LSTA/LPC indications where there were at least three bids, three asks and a spread of less than 100 basis points was reasonable given the market's development at that time and was consistent with the methodology set forth in the prospectus.
>
> 5. In November 2000, Van Kampen's decision to base its fair value determinations on LSTA/LPC indications where there were at least two bids, two asks and a spread of less than 200 basis points, was reasonable given the status of the market's development at that time, and was consistent with the methodology set forth in the prospectus.
>
> 6. In making its fair value determinations, Van Kampen made a good-faith effort to consider factors important to an arms-length [sic] buyer in assessing what they would pay for the loans on a current sale.

McAdams Report at 5-6 (April 4, 2003).

6 The opinion numbered 1 is no longer at issue following the court's ruling on summary judgment.

[*20] Plaintiffs do not dispute that McAdams is an expert in the field. His experience qualifies him to testify as to how pricing services function, particularly how LSTA/LPC functioned. Opinion 2 is essentially descriptive and historical. It does not require applying any sort of testing or statistical methodology in order to be reliable. This opinion also does not involve a particularized application to the Fund's procedures. Therefore, questions that plaintiffs raise regarding McAdams's knowledge of the Fund's procedures are not pertinent to this opinion. McAdams's experience is enough to support reliability as to Opinion 2. *Cf. Den norske Bank AS v. First National Bank of Boston, 75 F.3d 49, 57-58 (1st Cir. 1996)* (employee of defendant bank with 40 years of banking experience was qualified to testify as to banking industry practices); *Dahlin v. Evangelical Child & Family Agency, 2002 U.S. Dist. LEXIS 24558, 2002 WL*

*31834881 *6-7 (N.D. Ill. Dec. 18, 2002)* (expert was qualified to testify as to history of adoption practices and information being provided to adoption professionals at various periods of time).

Opinion 3 is different than Opinion 2. While it still requires an expert [*21] understanding of the pricing services that were available, it also requires an understanding of the Fund's actual practices. Plaintiffs contend that McAdams was not fully informed as to the Fund's practices because defendants did not supply him with all the pertinent evidence. Plaintiffs also contend that this opinion is unreliable because McAdams never examined the Fund's particular valuations to determine if they were accurate.

Plaintiffs contend that McAdams is not qualified to opine as to whether the Fund's practices corresponded with pricing resources available in the market because McAdams has insufficient knowledge of the Fund's actual practices. In particular, plaintiffs complain that (a) McAdams has not read a July 1999 Pricewaterhouse-Coopers LLC ("PwC") review of the Fund's valuation practices and (b) at his deposition, McAdams could not recall SEC correspondence questioning the Fund's valuation methods. While familiarity with the PwC report may have provided McAdams with additional information about the Fund's actual practices, the other documents that he was provided should have been sufficient to allow McAdams to be familiar with the practices. His lack of complete familiarity [*22] and recall goes more to the weight of his opinion, not whether it is admissible. The jury will be able to determine whether McAdams's assumptions about actual practices of the Fund correspond with the evidence of actual practices that will be presented at trial. Similarly, to the extent the SEC correspondence sets forth factual findings and not legal analysis, McAdams's failure to recall details of the correspondence goes to the weight to be given his testimony and the jury will resolve factual questions as to the actual practices that were in place. Plaintiffs do not contend that McAdams was not shown the correspondence when preparing his report, only that, at the time he was disposed, he could not recall having seen it.

The other issue raised by plaintiffs is that McAdams should not be permitted to testify about the Fund reasonably applying valuation methods when he never tested the accuracy of the valuations. Plaintiffs contend McAdams is not qualified to testify as to the efficacy of the Fund's actual valuation procedures because he made no comparison between the values given to particular loans and the prices the loans may have sold at during the same time period. According to [*23] McAdams's admissible testimony, however, there is only limited available data as to actual prices that loans sold for in the secondary market. Plaintiffs would like to rely on pricing information provided by LSTA/LPC and other services as being accurate, but the accuracy of those prices is a question of fact for the jury. McAdams may properly testify that the valuation practices of the Fund complied with the price information for loans that was contemporaneously available. Plaintiffs may cross examine him as to the lack of any price comparison study in order to raise questions as to the weight or credibility of his testimony, but that is not enough to make his testimony inadmissible.

Plaintiffs also generally raise the contention that McAdams's opinions are conclusory and lack supporting details. *See generally Mid-State Fertilizer Co. v. Exchange National Bank of Chicago, 877 F.2d 1333, 1339-40 (7th Cir. 1989).* McAdams's discussion of Opinion 3, however, is sufficiently detailed and not conclusory. *See* McAdams Report at 21-24.

There is one aspect of Opinion 3 as to which McAdams will not be permitted to testify. He opines that the Fund's actual valuation practices [*24] were consistent with the description of those practices contained in the prospectuses. That is a purely factual question of comparing the evidence of actual practices with the descriptions contained in the prospectuses. No expertise is required to make such a comparison. McAdams's testimony as to this issue would not assist the jury. McAdams will not be permitted to testify as to that aspect of Opinion 3.

Opinions 4 and 5 both concern whether the particular practices involved, the "3 x 3 x 100 screen" and "2 by 2 x 200 screen," *see Abrams III, 2004 U.S. Dist. LEXIS 11730, 2004 WL 1433620 at *6*, were reasonable in light of pricing information then available in the market. His testimony concerns the reasonableness of each particular practice in light of then-available information, not whether the Fund's actual application produced accurate valuations. McAdams may properly testify as to these opinions. As with Opinion 3, however, McAdams will not be permitted to testify as to whether the Fund's actual practice was consistent with the descriptions of the practices contained in the prospectuses.

Although McAdams's summarized statement of Opinion 6 refers only to the Fund's good-faith intent, the [*25] specifics of this opinion explain why it is unnecessary to discount from the par value of a loan to take into account the illiquid nature of senior loans. He opines that the "illiquidity discount" is taken into account at the time par is first set. He also opines as to the effect on the value of a loan that a breach of a bank covenant or a bankruptcy filing may have. McAdams may testify regarding his opinions on these subjects. However, he will not be permitted to testify as to whether he believed any defendant acted in good faith in determining the price an arm's length buyer would pay for a loan. That is a factual issue of intent that is for the jury to decide. The jury's determination of intent would not be assisted by McAdams's opinion on that issue. *See Dahlin, 2002 U.S. Dist. LEXIS 24558, 2002 WL 31834881 at *3.*

For the foregoing reasons, this motion in limine will be granted in part and denied in part. This motion will be denied except that McAdams will not be permitted to testify as to (a) whether any actual valuation practice of the Fund is consistent with a description of the practice contained in a prospectus nor (b) whether any defendant acted in good faith or with some other type [*26] of intent.

4. To Exclude Testimony of Expert Witnesses Daniel R. Fischel and David J. Ross [141-1]

Defendants intent to use Daniel Fischel and David Ross as damages liability experts. The two provided a joint report, but defendants now clarify that they intend to have Fischel testify regarding two of the opinions expressed therein and Ross testify as to one. Plaintiffs argue that neither of the witnesses should be allowed to testify as to one of the opinions. Plaintiffs also argue that the two witnesses are duplicative and only one should be permitted to testify.

Both experts are officers of Lexecon Inc., a consulting firm that specializes in the application of economics to legal and regulatory issues. Plaintiffs do not question the qualifications of either of these experts. Plaintiffs only question the methodology used to reach the conclusions contained in Opinion 1 below. [7]

7 In a separate motion in limine, plaintiffs also object to an aspect of Opinion 2. *See* § B(5) *infra.*

Fischel [*27] and Ross were retained to examine the conclusions set forth by plaintiffs' valuation expert, Linda Allen, and damages expert Michael J. Barclay. Allen opines as to the amounts by which the Fund overvalued its NAV during the class period. Barclay, in part based on Allen's overvaluation calculations, provides a calculation of damages to the class of plaintiffs.

As summarized by defendants, Fischel's and Ross's opinions and defendants' contention as to the related evidence they will submit may be summarized as follows:

Opinion 1: Barclay's calculations do not account for factors other than the alleged wrongdoing that caused the Fund's NAV to decline during the Class Period. The experts opine that adverse market conditions account for all or a substantial portion of the decline in NAV, in particular an increase in loan default rates and a widening credit spread. Defendants intend to introduce testimony regarding Opinion 1 through Fischel. This will include evidence that is intended to show that all senior loan funds and a published index of senior loans experienced declines in value comparable to the decline in the NAV of the Fund.

Opinion 2: Barclay's calculations do not measure [*28] the class's economic loss attributable to the alleged overpricing of the Fund. A drop in NAV does not strictly correlate with economic loss to the class plaintiffs. Defendants intend to introduce testimony regarding Opinion 2 through Fischel. Defendants will present evidence that they contend will show that Barclay's methodology for calculating damages is flawed because it creates windfall recoveries that bear no relationship to the alleged overpricing of the Fund's shares.

Opinion 3: On the assumption that the Fund should have used LPC prices, Ross calculates the amount that the NAV was overvalued to be somewhat different from Allen's initial calculation. Ross then uses this overvaluation calculation and a different methodology than Barclay to calculate the amount of purported damages to be substantially less than Barclay's total. Ross proposes a number of alternative calculations based on different methods or assumptions. In their report, this Opinion is stated to be that of Ross only. Defendants intend to introduce testimony regarding Opinion 3 through Ross.

In Opinion 1, defendants' experts rely on a Standard & Poor/Loan Syndication and Trading Association ("S&P/LSTA") index [*29] of loans to establish an increase of loans in default or bankruptcy during the pertinent time period, from near zero in 1996 to significantly higher from 1999 through 2001. As stated in their report: "An increase in default rates obviously will reduce the value of senior loans and the value of funds holding such loans." Fischel & Ross Report at 6 (April 30, 2003). They also rely on the London Interbank Offered Rate ("LIBOR") to establish an increasing credit spread between October 1998 and October 2001. LIBOR is the rate at which major international banks in London lend dollars to each other and is often used as a benchmark for floating rates. The credit spread relied upon is the difference between the yield of leveraged loans and LIBOR. As stated by defendants' experts: "Because there is an inverse relationship between the price of any given loan and the relevant credit spread, the increase in credit spreads also reduced the value of senior loans and the value of funds holding such loans."

Plaintiffs do not dispute the general principles that increased default rates and an increased credit spread will result in a general decline in the value of floating-rate loans, nor do they dispute [*30] that default rates and the credit spread increased during the pertinent time period. Plaintiffs, however, object that the experts failed to apply any methodology for connecting the general economic conditions to an effect on senior loans in general or the Fund's NAV in particular. The experts provide no data purporting to show how much of the Fund's drop in NAV was caused by these conditions. The experts do not give any consideration to the actual loans held by the Fund nor do they attempt to correlate the Fund's NAV changes over the class period with particular changes in economic conditions during the class period. Under *§ 11*, decreases in the value of the security are presumed to be caused by the material misstatements that are shown. *McMahan & Co. v. Wherehouse Entertainment, Inc., 65 F.3d 1044, 1048 (2d Cir. 1995), cert. denied, 517 U.S. 1190, 134 L. Ed. 2d 781, 116 S. Ct. 1678 (1996)*; *Pirelli Armstrong Tire Corp. Retiree Med. Benefits Trust v. Dynegy, Inc. (In re Dynegy, Inc.), 339 F. Supp. 2d 804, 867 (S.D. Tex. 2004)*; *In re Initial Public Offering Securities Litigation, 241 F. Supp. 2d 281, 351 n.80 (S.D.N.Y. 2003)*. If plaintiffs prove liability, the burden is on defendants to show that drops [*31] in NAV were caused by something other than the alleged misstatements in the prospectuses. [8] *15 U.S.C. 77k(e)*; *In re Adams Golf, Inc. Securities Litigation, 381 F.3d 267, 277 (3d Cir. 2004)*; *McMahan, 65 F.3d at 1048*; *Dynegy, 339 F. Supp. 2d at 867-68*; *Nielsen v. Greenwood, 1996 U.S. Dist. LEXIS 14441, 1996 WL 563539 *12 (N.D. Ill. Oct. 1, 1996)*. Here, however, the experts do not attempt to connect changes in loan default rates and the credit spread to changes in the Fund's NAV nor do they make any attempt to show how much of an effect there may have been. Therefore, it has not been shown that this testimony is relevant to the damages issues in this case.

> 8 This is often referred to as the defense of "negative causation." *See McMahan, 65 F.3d at 1048*.

Defendants' experts do point to general data regarding decreases in loan values and senior loan fund NAV's during the class period. The loan indices used, however, do not index senior [*32] loans. Instead, the indices used were for all loans, B-grade loans, and BB-grade loans. While there is some overlap between the indices used and the types of loans held by the Fund, apparently none of the indices correspond with the mix of loans held by the Fund. Fischel and Ross do not explain the correlations or possible differences between the indices used and the assets of the Fund. Also, Fischel and Ross provide no statistical or other sufficient method for correlating changes in the indices to changes in default rates or credit spreads. [9] As to other senior loan funds, the experts generally do not consider similarities and differences with the Fund nor whether the other funds may or may not have overstated NAV.

> 9 In rebuttal, Barclay opines that multiple regression analysis shows a lack of statistically significant correlations between the indices and changes in the Fund's NAV.

Because not supported by adequate methodology nor shown to be relevant to issues in the present case, Fischel and Ross will not [*33] be permitted to testify regarding Opinion 1.

Still to be considered is whether both Fischel and Ross will be permitted to testify. Defendants agree that ordinarily only one expert per side should opine on a particular subject. *See* N.D. Ill. Loc. R. Form 16.1.1 n.7; *Dahlin, 2002 U.S. Dist. LEXIS 24558, 2002 WL 31834881*. Defendants contend, however, that Fischel will testify as to Opinion 2 and Ross as to Opinion 3. The two opinions, however, are closely related. Ross will not be able to opine as to Opinion 3 without also addressing many aspects of Opinion 2. Defendants will be precluded from using both experts. They may choose which expert they prefer to use. [10] *See id.*

> 10 Fischel did not join in Opinion 3. Therefore, testimony as to both Opinions would probably require the use of Ross. No ruling is made as to whether Fischel could testify as to Opinion 3 if, prior to trial and because he fully agrees with Ross as to Opinion 3, he supplements his report by adopting Opinion 3 as well.

For the foregoing reasons, [*34] this motion in limine will be granted in part and denied in part. Fischel and Ross will be barred from testifying as to Opinion 1 and defendants will be limited to using one expert to testify as to the remaining opinions contained in the Fischel/Ross Report.

5. To Preclude Evidence and Argument Concerning Dividends Paid by the Van Kampen Prime Rate Income Trust to Shareholders [142-1]

Section 11 itself contains a provision as to damages for violations of *§ 11(a)*.

> The suit authorized under subsection (a) of this section may be to recover such damages as shall represent the difference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and (1) the value thereof as of the time such suit was brought, or (2) the price at which such security shall have been disposed of in the market before suit, or (3) the price at which such security shall have been disposed of after suit but before judgment if such damages shall be less than the damages representing the difference be-

> tween the amount paid for the security (not exceeding the price at which the security was offered to the public) and the value thereof as [*35] of the time such suit was brought: Provided, That if the defendant proves that any portion or all of such damages represents other than the depreciation in value of such security resulting from such part of the registration statement, with respect to which his liability is asserted, not being true or omitting to state a material fact required to be stated therein or necessary to make the statements therein not misleading, such portion of or all such damages shall not be recoverable. . . .

15 U.S.C. § 77k(e).

As discussed in § B(4) *supra*, the decrease in value of a security (in this case, effectively the decrease in NAV of the Fund) is presumed to have been caused by any material misstatements that are proven to have been included in one or more of the Fund's prospectuses. On the issue of damages, the burden is on defendants to prove that any such decrease was caused by factors other than the material misstatements. The decrease in value of the security (during the relevant time period) is the exclusive measure of damages for violations of *§ 11(a)*; other standard measures of contractual damages are inapplicable under the statute. *McMahan, 65 F.3d at 1048*; [*36] *Goldkrantz v. Griffin, 1999 U.S. Dist. LEXIS 4445, 1999 WL 191540 *3 (S.D.N.Y. April 6, 1999), aff'd by unpublished order, 201 F.3d 431 (2d Cir. 1999).*

Defendants want to introduce evidence that members of the plaintiff class received dividend payments from the Fund. They contend that evidence would show that an investor who held a single share of the Fund during the class period would have had a drop in NAV of $ 1.18, but also would have received $ 1.69 in dividends for a net gain of $ 0.51 on the share. Defendants contend this evidence will fit into the statutory method for measuring damages because the receipt of dividends is part of their evidence showing negative causation. Defendants contend that paying dividends caused a decrease in the Fund's NAV. They point to a conclusory statement in their damages experts' report as supporting this contention. *See* Fischel & Ross Report at 8 n.7 (April 30, 2003) ("Professor Barclay's calculations do not measure Class members' out-of-pocket losses because he ignores the dividends paid by the Fund to its shareholders."). *See also* Ross Suppl. Report at 8-9 (Oct. 17, 2003) ("I understand that the defendants contend that plaintiffs [*37] cannot recover under *Section 11* for declines in the value of a security attributable to factors other than the alleged material misstatements and omissions. If defendants' contention is correct, then an offsetting adjustment for dividend payments should be made, because the payment of dividends necessarily caused the value of the fund to decline by the amount of dividends paid.").

In a somewhat lengthier, but still essentially conclusory manner, plaintiffs' damages expert stated that the payment of dividends does not decrease NAV. As he sees it, the effect of dividends on NAV is that retaining dividends, instead of distributing them, would increase NAV.

> Q. And if a fund pays out dividends, what impact, if any, would that have on the NAV Of the fund?
>
> * * *
>
> A. At some level, it's correct that a dividend paid on the fund would reduce the NAV of the fund. However, it's clear from looking at the fund's NAV that it was possible to pay these dividends over a long period of time without having the fund's NAV vary from $ 10 per share by more than a penny or two.
>
> So what happens in these cases is that the senior loans held by the fund pay interest to the fund. The fund takes those interest [*38] payments that are received from the loans and passes them through to investors.
>
> So rather than thinking about the dividends as reducing NAV, which clearly they didn't over the history of the fund prior to the class period, since the fund's NAV never varied by more than a couple of pennies from $ 10 per share, what you're doing is paying out those dividends rather than retaining them in the fund and reinvesting them which, in fact, would tend to increase the fund's NAV.

Barclay Dep. at 75-76.

One issue that goes to the admissibility of the testimony is whether the potential effect of dividends on NAV is a question of law as to the measure of damages or a question of fact as to whether or not paying dividends affects NAV. Here, the Fund's stated goal was to achieve a high level of current income consistent with preservation of capital. If, as Barclay indicates, dividends simply represented the distribution of interest earned on the loans, such a distribution would be independent of the value of the shares themselves that is represented by NAV. Defendants point to no evidence that this is not true. Therefore, for purposes of ruling on this motion in limine, it is assumed that [*39] dividends represented interest earned on the loans and were separate from the loan asset itself that represented the value of the Fund's shares. Therefore, as a matter of law, the payment of dividends would not be part of the calculation of damages based on a decline in share value (NAV).

Even if that should not taken as true, defendants have not shown that they have admissible evidence that the distribution of dividends negatively affected NAV. All they can point to is conclusory statements by their damages experts. Such unsupported, conclusory statements are not admissible evidence. *See Huey v. UPS, 165 F.3d 1084, 1087 (7th Cir. 1999)*; *Mid-State Fertilizer, 877 F.2d at 1339-40*; *Ab v. Sekendur, 2004 U.S. Dist. LEXIS 21715, 2004 WL 2434220 *6 (N.D. Ill. Oct. 28, 2004)*; *Comer v. American Electric Power, 63 F. Supp. 2d 927, 936-37 (N.D. Ind. 1999)*. Alternatively, since the evidence related to the effect of distributing dividends is inadmissible in form, defendants will not be permitted to present it.

Defendants also argue that evidence as to dividends is admissible so that the jury will have a complete picture. They contend [*40] that the jury should know that class members received dividends as well as any proceeds from the redemption of their shares. Defendants contend the jury may make a decision based on sympathy for the plaintiffs if the jury believes the plaintiffs had a net loss. The jury will be instructed that they are not to decide the case based on sympathy for a party. Since, as discussed above, dividends are not relevant to calculating damages, there is no reason for the jury to know the amount of dividends received by class members. Defendants will not be permitted to present evidence regarding the amount of dividends distributed by the Fund. As part of the basic background for this case, including evidence as to how the Fund functioned, the parties are not precluded from presenting evidence that the loans held by the Fund earned interest and that the interest was distributed in the form of a dividend. The parties are only prohibited from presenting evidence as to the amount of the dividend and any effect the distribution of dividends may have had on the Fund's NAV.

For the foregoing reasons, this motion in limine will be granted. The parties will not be permitted to present evidence as to the [*41] amount of dividends that the Fund paid nor will they be permitted to argue that any distribution of dividends affected the Fund's NAV or the amount of damages to be awarded in this case. This includes that Fischel or Ross will not be permitted to testify as to the aspect of Opinion 2 that is based on the distribution of dividends affecting NAV and damages.

C. DEFENDANTS' MOTIONS IN LIMINE

1. To Exclude the Testimony and Report of Linda Allen [137-1]

Plaintiffs' valuation expert, Linda Allen, has a Ph.D. in Economics and Finance from New York University and is currently a Professor of Finance at Baruch College of the City University of New York and an Adjunct Professor of Finance at New York University. She is the author or coauthor of three books and numerous articles, primarily in the field of loan valuation and credit risk analysis. Her books include *Understanding Market, Credit and Operational Risk: The Value at Risk Approach* and *Credit Risk Measurement: New Approaches to Value at Risk and Other Paradigms*.

Allen opines that, during the class period, the LPC database was a reliable benchmark of market prices for a majority of the loans held by [*42] the Fund. She bases this opinion on "(a) the number, sophistication and financial resources of dealers providing market quotations to LPC, (b) the number of quotes provided for each loan, (c) the quality controls put in place by LPC in response to the demand for quality by its customers, (d) the general acceptability of the database in the market, (e) the general acceptability of the database for the purposes of academic research, and (f) the internal studies conducted by LPC comparing LPC quotations to actual trade prices." Additionally, Allen opines that, during the class period, there was a secondary loan market for syndicated bank loans and readily available market quotations for a majority of the loans in the Fund's portfolio. The latter conclusion was based in part on data regarding the average number of bid quotes and ask quotes available for loans held by the Fund. Further, taking available LPC pricing data as accurate, Allen recalculated NAV for each day of the class period and determined how much NAV was overvalued on each day of the class period. She also compared LPC pricing data to the Fund's valuation of its loans, resulting in statistically significant evidence that [*43] the Fund generally overvalued loans.

Defendants do not dispute that Allen is qualified as an expert on finance. They contend, however, that she lacks expertise to opine on the senior loan secondary market because she has never traded in that market, she has never worked for a senior loan fund, and she has never been associated with LPC or LSTA. Defendants contend that being a generalist on loan markets is not good enough, that she must be a specialist as to the senior loan market in order to be able to provide useful testimony for the jury. This objection is without merit. Allen's educational background and the research background shown by her publications show that she is well versed on loans, factors and conditions that affect loan markets, and other aspects of the pertinent financial markets. Her report also exhibits an understanding of the senior loan market and how it functions. One need not have been a participant in a particular market in order to qualify as an academic expert who can provide useful testimony. *Compare Crowley v. Chait, 322 F. Supp. 2d 530, 554-55 (D.N.J. 2004)* (Fischel's academic and consulting expertise in economics qualified him to provide [*44] useful testimony related to insurance accounting, loss reserve, and management issues).

Defendants also contend that Allen's statistical evidence comparing LPC pricing to the Fund's valuation of loans would not be useful to the jury because it assumes LPC pricing is accurate. This objection is without merit for two reasons. First, Allen also provides competent and admissible evidence supporting that LPC pricing was reliable and readily available. Second, even if she did not personally provide such support, the reliability of LPC pricing is a disputed issue of fact in this case. The jury will decide the extent to which LPC/LSTA pricing information qualifies as reliable and readily available market quotations. In light of that finding, the jury will accordingly consider and apply Allen's testimony comparing the LPC pricing to the Fund's valuations.

This motion in limine will be denied in its entirety.

2. To Exclude the Eaton Vance Documents [143-1]

Eaton Vance is a senior loan fund unrelated to the Fund. A lawsuit is pending against Eaton Vance regarding their valuations of senior loans. Some of the same attorneys represent the plaintiffs in both this case and the [*45] Eaton Vance case. When deposed in the Van Kampen case, Taylor testified that monthly LSTA pricing information was not available to buy-side institutions like Van Kampen and Eaton Vance until September 1999. After fact discovery closed in the Van Kampen case, Taylor was deposed in the Eaton Vance case. At that time, Taylor corrected her testimony and stated that the reports were available to buy-side "founding" or "full" members as of July 1998. Van Kampen did not become a full member of LSTA until 2000, but could have become a full member in 1998. Eaton Vance was a full member in 1998 and therefore received the reports beginning in 1998. Those reports were disclosed in discovery in the Eaton Vance case. In the Eaton Vance case, reliability studies were also disclosed in which Eaton Vance had compared LPC market prices to actual prices Eaton Vance had paid for senior loans. Both the reports and reliability study are included as plaintiffs exhibits in the Van Kampen case. The reliability study was considered by Allen in rendering her opinions. Defendants object to use of these documents on the ground that they were not properly disclosed in discovery in the Van Kampen case and on grounds [*46] of relevance.

While defendants had some notice of the existence of these documents prior to the time the pretrial order was prepared, plaintiffs do not dispute that they should have provided fuller notice and also do not dispute that the actual documents were not provided to defendants until defendants filed the present motion in limine. Plaintiffs indicate that the failure to provide the documents was an oversight, but also note that defendants were informed of the documents during the time the final pretrial order was being prepared and did not take the opportunity to request copies at that time. Defendants were also offered the opportunity to further depose Allen regarding these documents, but decided not to do so. Defendants do not dispute that they now have the documents and do not point to any manner in which the delayed disclosure has prejudiced their preparation for trial. The documents will not be barred based on failure to timely and adequately disclose them if the deficiencies were harmless. *See Fed. R. Civ. P. 37(c)(1).* Here, there is no indication that defendants were prejudiced in any manner by the delays. No sanction will [*47] be imposed.

Defendants' other objection is relevance. Since the reports were available to entities like the Fund, the reports are relevant to the issue of whether there were readily available market quotations. The reports will not be stricken as exhibits. The reliability study represents a method for testing the accuracy of LPC pricing information and was relied upon one of plaintiffs' experts. The studies are also relevant evidence.

For the foregoing reasons, this motion in limine will be denied.

3. To Exclude the Testimony of Thomas Hudson [144-1]

Thomas Hudson has been a senior loan trader at Goldman Sachs and was on the Distressed Loan Committee of LSTA. Plaintiffs represent that they decided to use him as a witness after defendants proposed Meenan and DeLuca as witnesses. Plaintiffs intend to use Hudson to rebut all or some of the testimony of Meenan and DeLuca. Plaintiffs do not dispute that Hudson was not previously disclosed in response to interrogatories. However, neither had defendants expressly disclosed Meenan and DeLuca in response to interrogatories. *See* § B(2), *supra*. Unlike Hudson, though, Meenan and DeLuca had been mentioned during deposition [*48] testimony. In any event, defendants have not been prejudiced by the delayed disclosure. Hudson will not be barred as a witness, but, if they desire, defendants may depose Hudson within the next 45 days.

4. To Exclude Evidence Of, or Reference To, the SEC Letters [145-1]

In November 1999, the Midwest Regional Office of the SEC conducted an on-site inspection of Van Kampen. The inspection was not limited to the Fund, but it did include an examination of valuation procedures used by the Fund. Related to this inspection, there was correspondence between Van Kampen officials and SEC officials. Defendants move to exclude from evidence three letters from the SEC to Van Kampen, dated October 20, 1999, March 28, 2000, and June 28, 2000. [11] Plaintiffs contend all three letters are admissible under *Fed. R. Evid. 803(8).*

11 There are also four letters from Van Kampen to the SEC. Plaintiffs point out that the motion does not raise any objection to those letters. In the final pretrial order, however, defendants object to those letters as well. *See* Pl. Exh. 3, 6, 8, 10. Any issues that exist regarding the admissibility of the letters written by Van Kampen officials would be distinct from the *Rule 803(8)* issues raised regarding the letters from the SEC that are the subject of the present motion.

[*49] In a letter dated September 1, 1999, Van Kampen's General Counsel, A. Thomas Smith, wrote to the SEC's Chicago Branch Chief of Investment Company Examinations. This letter included a lengthy explanation of Van Kampen's methods for valuing loans. [12] In a letter dated October 20, 1999, which is one of the letters that is a subject of this motion in limine, the SEC's Midwest Regional Office Assistant Director wrote to Smith confirming an October 18 conversation. The letter referred to the SEC's upcoming inspection regarding three SEC senior loan funds, including the Fund, which would begin November 1, and requested certain additional documents.

12 Neither side's brief attaches a copy of this letter. The remainder of its content is not disclosed in the briefs and neither side makes any representation as to what caused the General Counsel to write this letter. Presumably, it was a response to a prior inquiry from the SEC.

According to Smith's deposition testimony, the inspection lasted approximately one week. The [*50] inspection team interviewed Smith, the Fund's President and Portfolio Manager, and the Fund's Assistant Portfolio Manager. Records were also examined.

In January 2000, the Fund adopted the 3 x 3 by 100 screen and requested a meeting with the SEC to discuss it. This meeting took place on January 25, 2000 in Washington, D.C. With a letter dated February 1, 2000, Van Kampen sent additional documents to the SEC.

In a letter dated March 28, 2000, which is one of the letters that is a subject of this motion in limine, the SEC's Assistant Regional Director wrote to the Fund's President. The letter sets forth findings made during the November inspection. The SEC sets forth a number of deficiencies that were found with the pricing guidelines that were in effect as of November 1999 (the "Old Guidelines"). The inspection found a failure to adequately consider secondary market indications, including market quotations received directly from market makers or indirectly through LPC. A failure to consider fluctuations in spreads over the base rate of interest for pricing purposes was also found. In the letter, the Assistant Regional Director also commented on the new 3 x 3 x 100 pricing procedure [*51] (the "Proposed Guidelines") and found deficiencies. It was found that the Proposed Guidelines too readily permitted the Adviser to override prices otherwise indicated by the 3 x 3 x 100 procedure. Where 3 x 3 x 100 data was not available for pricing a loan, the Proposed Guidelines still failed to adequately consider spread when fair valuing a loan. The letter also criticizes Van Kampen for finding that no Fund Board Member was on the Adviser's Pricing Committee that made fair value determinations. The Board was also criticized for having made no attempt to compare fair valuation determinations with actual recoveries on distressed loans.

In a response letter dated April 27, 2000, Smith responded to the SEC's findings as to the Proposed Guidelines and the criticisms of the Board. Smith noted new procedures that limited overrides of market indicators to one day, required daily approval by the Pricing Committee, and quarterly review by the Board. He disagreed with the criticism regarding not adequately considering spreads on the ground that it required too complex an application to be feasibly implemented. As to the Board criticisms, Smith noted that the Board would not be reviewing certain [*52] information on a quarterly basis and that it would be provided reports comparing distressed loan recoveries with their valuations.

The last letter to which defendants object is the SEC's Regional Director's June 28, 2000 letter to Smith, which was a response to Smith's April 27, 2000 letter. The June letter notes that the valuation techniques used by the three funds had been discussed with the Division of Investment Management's Office of Chief Counsel and that that office concurred with the views expressed in the June letter.

First, the June letter reemphasized that, when available, the law requires that market quotations be used to price financial instruments and that the funds had to look to other possible sources for quotations when LPC supplied quotes could not be used.

> It is our understanding that the Funds do not seek other sources of market quotations whenever LPC-supplied quotes were deemed unreliable. We were not shown any evidence that explained precisely why the LPC-supplied quotes did not reflect current market values other than the fact the quotes fell outside the predetermined parameters. We also did not see any documentation evidencing that the Funds made a determination [*53] in these circumstances that reliable market quotations were not readily available.

June 28, 2000 SEC Letter at 2.

The letter again criticized the three funds' applications of fair value methodology.

> In a majority of situations in which the Funds used fair value to price their portfolio instruments, the fair value methodology used resulted in such instruments being valued higher than the LPC-supplied quotes. We also noted that in most circumstances when valuations are not based on LPC-supplied quotes, loans were fair valued at approximately par value.
>
> The Funds have not provided us with any analysis and documentation that supported the use of such higher values. . . . The only support presented for valuation at par was that this reflected the amount the Funds would receive if instruments were held to maturity or the loan prepaid. As discussed in the Division of Investment Management's December 8, 1999 letter to the ICI, the Staff has consistently rejected a policy of equating fair value with par value absent evidence that an instrument could be sold currently at approximately par.

Id.

The letter agreed that certain factors suggested by Van Kampen could appropriately [*54] be considered when it was appropriate to apply fair value methodology, but emphasized that these were not the only factors to consider. "All relevant factors" were to be considered.

> . . . The following issues suggest that all relevant factors are not being considered in using fair values to price certain of the Funds' portfolio instruments:
>
> > . The substantial difference that often exists between quotations provided by LPC and fair values used by the Funds in situations where Van Kampen's price discovery mechanism does not produce alternative market quotations that Van Kampen deems reliable.
> >
> > . The absence of any demonstrated analysis on an instrument-by-instrument basis supporting a valuation at approximately par value.

Id. at 3.

Rule 803(8) provides:

> Records, reports, statements, or data compilations, in any form, of public offices or agencies, setting forth (A) the activities of the office or agency, or (B) matters observed pursuant to duty imposed by law as to which matters there was a duty to report, excluding, however, in criminal cases matters observed by police officers and other law enforcement personnel, or (C) in civil actions and proceedings and [*55] against the Government in criminal cases, factual findings resulting from an investigation made pursuant to authority granted by law, unless the sources of information or other circumstances indicate lack of trustworthiness.

Fed. R. Evid. 803(8).

Plaintiffs contend that the October 29, 1999 letter is admissible under *Rule 803(8) (A)* and that the other two letters are admissible under *Rule 803 (8) (C)*. The October letter is a request for information that occurred prior to the November inspection; it does not include any factual findings that would bring it within the purview of subsection (C). The trustworthiness clause of *Rule 803(8)* still applies to subsection (A). *See Nachtsheim v. Beech Aircraft Corp., 847 F.2d 1261, 1273 (7th Cir. 1988)*; *United States v. Koontz, 143 F.3d 408, 412 (8th Cir. 1998)*; *Chapman v. San Francisco Newspaper Agency, 2002 U.S. Dist. LEXIS 18012, 2002 WL 31119944 *2 (N.D. Cal. Sept. 20, 2002)*; *United States v. May, 18 M.J. 839, 842-43 (1984)*. The October 29 letter, however, certainly is trustworthy as to what it is, a simple statement confirming that additional documents had [*56] been requested. The October 29 letter is nonhearsay in accordance with *Rule 803(8) (A)*. Whether other grounds for excluding it exist will be discussed below.

The other two letters contain findings based on the November inspection. To be nonhearsay, they must satisfy the criteria of *Rule 803(8) (C)*, including that they do not have indicia of lacking trustworthiness. If the threshold requirements of being factual findings resulting from an investigation made pursuant to authority granted by law are satisfied, trustworthiness is presumed and the burden is on the party opposing admission to show a lack of trustworthiness. *Amtrust Inc. v. Larson, 388 F.3d 594, 599 (8th Cir. 2004)*; *Bridgeway Corp. v. Citibank, 201 F.3d 134, 143 (2d Cir. 2000)*; *Huff v. State of Illinois*, 2003 WL 168630 *5 (N.D. Ill. Jan. 23, 2003); *Klein v. Vanek, 86 F. Supp. 2d 812, 820 (N.D. Ill. 2000)*. Here, the letters contain factual findings [13] that were made following an SEC inspection performed pursuant to authority of law. Therefore, the findings are presumed to be trustworthy.

13 Conclusions and opinions that are factual in nature may fall within the *Rule 803(8)(C)* exception. *Beech Aircraft Corp. v. Rainey, 488 U.S. 153, 162, 102 L. Ed. 2d 445, 109 S. Ct. 439 (1988)*; *United States v. Romo, 914 F.2d 889, 896 (7th Cir. 1990), cert. denied, 498 U.S. 1122, 112 L. Ed. 2d 1183, 111 S. Ct. 1078 (1991)*; *United States v. Peitz, 2002 U.S. Dist. LEXIS 17750, 2002 WL 31101681 *5 (N.D. Ill. Sept. 20, 2002)*. However, legal conclusions of an agency will not be admitted under the *Rule 803(8)(C)* exception. *Hines v. Brandon Steel Decks, Inc., 886 F.2d 299, 302-03 (11th Cir. 1989), cert. denied, 503 U.S. 971, 118 L. Ed. 2d 305, 112 S. Ct. 1587 (1992)*; *Miranda-Ortiz v. Deming, 1998 U.S. Dist. LEXIS 17147, 1998 WL 765161 *1 (S.D.N.Y. Oct. 29, 1998)*. To the extent any of the SEC letters contain legal conclusions; any admissible portions would be limited to those findings that are factual in nature. *Cf. Peitz, 2002 U.S. Dist. LEXIS 17750, 2002 WL 31101681 at *5*.

[*57] In evaluating trustworthiness, four nonexclusive factors set forth in the Advisory Committee Notes to *Rule 803(8)* are generally considered. *See Coleman v. Home Depot, Inc., 306 F.3d 1333, 1342 (3d Cir. 2002)*; *Klein, 86 F. Supp. 2d at 820*. They are the timeliness of the investigation; the special skill or expertise of the official; whether a hearing was held; and possible motivational problems with the investigator. Additional factors that have been considered include the finality of the findings; the extent to which the findings are based on materials that would not be admissible in evidence; the degree to which any hearing complied with due process; the extent to which there is an ascertainable record; the extent to which the findings represent an implementation of a policy in contrast to findings of fact; whether the findings incorporate findings of another agency that may not have been trustworthy; and, if expert opinions were involved, the extent to which the usual criteria for such opinions was present. *Coleman, 306 F.3d at 1342 n.4* (quoting *Zenith Radio Corp. v. Matsushita Electrical Industries Co., 505 F. Supp. 1125, 1147 (E.D. Pa. 1980),* [*58] *aff'd in part, rev'd in part on other grounds, In re Japanese Electronic Products Antitrust Litigation, 723 F.2d 238 (3d Cir. 1983), rev'd, Matsushita Electrical Industrial Co. v. Zenith Radio Corp., 475 U.S. 574, 89 L. Ed. 2d 538, 106 S. Ct. 1348 (1986))*.

Here, no questions are raised regarding the SEC's motivation. The subject of the investigation was well within the expertise of the SEC. The inspection was conducted in November and the first letter was issued within a few months. Timeliness is also satisfactory. Defendants contend there are indicia of a lack of trustworthiness because no formal hearing was held and the findings were made by the Midwest Regional Office without ever being adopted by the Commission itself.

It is true that findings following a formal hearing with full due process procedures are more likely to be found to be trustworthy. However, findings based on other investigative procedures may still be admissible. *Bank of Lexington & Trust Co. v. Vining-Sparks Securities, Inc., 959 F.2d 606, 617 (6th Cir. 1992)*; Michael H. Graham, *Federal Practice & Procedure* § 7049 at 498 n.24 (2d Interim Ed. 1997). *See, e.g., Coleman, 306 F.3d at 1341-43* [*59] (determination letter based on EEOC investigation); *Bank of Lexington, 959 F.2d at 616-17* (letters of caution from National Association of Securities Dealers); *United States v. Peitz, 2002 U.S. Dist. LEXIS 17750, 2002 WL 31101681 *5 (N.D. Ill. Sept. 20, 2002)* (SEC action memorandum). Here, there is nothing presented by defendants to indicate that the SEC's inspection was not thorough or adequate. Although no hearing was held, the correspondence shows the SEC provided Van Kampen with a number of opportunities to provide additional documentation or evidence as well as opportunities to argue that the three funds' valuation procedures were adequate. Defendants contend the inspection was not intended to fully examine the Fund's valuation procedures because one of the letters refers to the inspection as being pursuant to § 31 of the 1940 Act, *15 U.S.C. § 80a-30*, which defendants contend is an inspection to ensure that proper records are kept. Although § 31 (a) (*15 U.S.C. § 80a-30 (a)*) requires that certain records be maintained, the examination provided for in § 31(b) (*15 U.S.C. § 80a-30 (b)*) is not limited [*60] to an examination to determine compliance with the recordkeeping requirement of *§ 31(a)*. "All records required to be maintained and preserved in accordance with subsection (a) of this section shall be subject at any time and from time to time to such reasonable periodic, special, and other examinations by the Commission, or any member or representative thereof, as the Commission may prescribe." *15 U.S.C. § 80a-30(b)*. The correspondence makes clear that the inspection was not intended merely to confirm that certain records were maintained. Defendants do not show that the SEC employed inspection procedures that raise questions as to the findings' trustworthiness.

Defendants also contend that the letters are untrustworthy because they were never adopted by the Commission itself. Where recommendations are being made to the Commission, findings made by SEC officials may be found to be untrustworthy if not adopted by the Commission. *See Peitz, 2002 U.S. Dist. LEXIS 17750, 2002 WL 31101681 at *5*. That, however, is not the present situation. The Regional Office had not made any recommendation to the Commission. The investigative procedures that were employed had not reached [*61] a stage that required Commission approval. As the last letter indicated, the Regional Office did get the concurrence of the Chief Counsel's Office. The findings in the letters will not be found untrustworthy simply because they were not approved by the Commission.

There is nothing to support that the Regional Office's findings based on its inspection were untrustworthy. The presumption of trustworthiness remains intact. Therefore, in accordance with *Rule 803(8)*, the factual findings contained in the three letters are not hearsay. However, legal conclusions contained in the letters would not be admissible to prove the truth of the matters contained therein. Statements that the funds failed to use market quotations that were readily available would itself be an admissible factual statement. The additional statements that such conduct violated statutes or regulations would not be admissible.

Although factual findings in the letters are not excluded as hearsay, it still must be considered whether the findings should be excluded on other grounds. Statements that fall within a *Rule 803* exception may still be excluded as unduly prejudicial under *Rule 403* or as irrelevant. *See Cooper v. Carl A. Nelson & Co., 211 F.3d 1008, 1018 (7th Cir. 2000)*; [*62] *Klein, 86 F. Supp. 2d at 820*.

Defendants argue that the present case involves misstatements of fact that violated *§ 11* whereas the letters address violations of § 2 of the 1940 Act which is not the issue in this case. As previously held, however, the legal conclusions regarding compliance with the 1940 Act are not parts of the letters that are nonhearsay under *Rule 803(8)(C)*. Facts supporting possible violations of the 1940 Act, though, are the same facts that support misstatements or omissions in the prospectuses. Basically, some of the alleged misstatements in the prospectuses were that the Fund was following valuation procedures, ones that complied with statutory requirements, but in actuality it was not. These facts will be before the jury. The jury would not be confused by being told that the SEC found facts that are consistent with plaintiffs' allegations regarding the Fund's actual valuation practices. They will not be told that the SEC found or indicated such practices violated the 1940 Act.

Defendants' other contention is that it would be unfairly prejudicial to provide evidence showing that the SEC reached conclusions that go to core issues that plaintiffs [*63] must prove to the jury. *See Klein, 86 F. Supp. 2d at 820-21*. Defendants argue the jury will have before it the same evidence that was before the SEC plus more and that, without knowing the conclusions reached by the SEC, the jury can conclude for itself whether there were readily available market quotations that the Fund did not adequately take into account when valuing its holdings. There is case law supporting that it is within the trial court's discretion to exclude *Rule 803(8)(C)* evidence on this ground. *See Tulloss v. Near North Montessori School, Inc., 776 F.2d 150, 153-54 (7th Cir. 1985)*; *Klein, 86 F. Supp. 2d at 820-21*. *See also Young v. James Green Management, Inc., 327 F.3d 616, 624-25 (7th Cir. 2003)*. Defendants do not cite any case holding that it is necessarily an abuse of discretion to admit such evidence. The Supreme Court has held that, as with expert and lay opinions (*see Fed. R. Evid. 704 (a)*), *Rule 803 (8)(C)* evidence that goes to ultimate issues may be admitted. *See Beech Aircraft, 488 U.S. at 169-70*.

Here, the jury will not simply be presented [*64] with evidence of the pricing information available to the Fund and then decide whether, contrary to representations in the prospectuses, there were readily available market quotations that were not used by the Fund in valuing loans or pertinent pricing information that was not considered when using fair value methods. Each side will also present experts who will opine as to whether such quotations or pricing information was available. In other words, even without the SEC letters, there will be experts opining as to some of the factual issues that must be decided by the jury. The SEC letters are analogous to having another expert's testimony regarding such ultimate issues, but an expert who is not biased by being connected to a particular party. Unlike the actual experts, the SEC letters will not be subject to cross examination. However, the parties will still be able to challenge the SEC's conclusions through the testimony of their own experts as well as in closing arguments.

The SEC letters apparently would also be relevant and admissible for another reason. Defendants will raise a business judgment defense based on their believing alleged misstatements in the prospectuses are actually [*65] true. The criticisms contained in the letters from the SEC, to the extent known by particular defendants and only as to prospectuses issued after such knowledge, would go to the question of those defendants' good faith beliefs regardless of whether the letters are admitted for the truth of the matters contained therein.

It is found that admission of the SEC letters would not be unfairly prejudicial to defendants. Therefore, in redacted form as discussed above, none of the letters will be excluded from evidence.

For the foregoing reasons, this motion in limine will be granted in part and denied in part. The letters will not be excluded from evidence except that legal conclusions must be redacted from the letters. The parties are to meet in an attempt to agree upon redacted versions of the letters.

D. CONCLUSION

The parties previously attempted to settle this case with the aid of a mediator, but could not reach an accord. Perhaps, in light of today's ruling, the parties will now be able to settle the case. Within one week, the parties shall contact each other to discuss the possibility of settlement. As a possible aid in the process, this case will be referred to the assigned [*66] magistrate judge to conduct settlement proceedings. The parties shall promptly contact the minute clerk of the assigned magistrate judge to arrange for a date to appear before the magistrate judge.

At the next status hearing, the parties shall report on the possibility of settlement.

IT IS THEREFORE ORDERED that:

(1) Plaintiffs' Motion In Limine To Bar Evidence that Traders Issued False Loan Pricing Data [138-1] is denied, but without prejudice to objecting to Taylor's testimony at trial.

(2) Plaintiffs' Motion In Limine To Exclude the Testimony of Kevin Meenan and Anthony DeLuca [139-1] is granted in part and denied in part. Within 45 days, plaintiffs may depose Meenan and DeLuca.

(3) Plaintiffs' Motion In Limine To Exclude the Testimony and Report of Michael P. McAdams [140-1] is granted in part and denied in part. McAdams will not be permitted to testify as to (a) whether any actual valuation practice of the Fund is consistent with a description of the practice contained in a prospectus nor (b) whether any defendant acted in good faith or with some other type of intent.

(4) Plaintiffs' Motion In Limine To Exclude Testimony of Expert Witnesses Daniel R. Fischel and David [*67] J. Ross [141-1] is granted in part and denied in part. Fischel and Ross will be barred from testifying as to Opinion 1 (the effect of adverse market conditions on the Fund NAV) and defendants will be limited to using one expert to testify as to the remaining opinions contained in the Fischel/Ross Report.

(5) Plaintiffs' Motion In Limine To Preclude Evidence and Argument Concerning Dividends Paid by the Van Kampen Prime Rate Income Trust to Shareholders [142-1] is granted. The parties will not be permitted to present evidence as to the amount of dividends that the Fund paid nor will they be permitted to argue that any distribution of dividends affected the Fund's NAV or the amount of damages to be awarded in this case.

(6) Defendants' Motion In Limine To Exclude the Testimony and Report of Linda AAllen [137-1] is denied.

(7) Defendants' Motion In Limine To Exclude the Eaton Vance Documents [143-1] is denied.

(8) Defendants' Motion In Limine To Exclude the Testimony of Thomas Hudson [144-1] is granted in part and denied in part. Within 45 days, defendants may depose Hudson.

(9) Defendants' Motion In Limine To Exclude Evidence Of, or Reference To, the SEC Letters [145-1] [*68] is granted in part and denied in part. Legal conclusions must be redacted from the SEC letters.

(10) This case will be referred to the assigned magistrate judge to supervise settlement discussions.

(11) A status hearing before Judge Hart will be held on March 16, 2005 at 11:30 a.m.

ENTER:

WILLIAM T. HART

UNITED STATES DISTRICT JUDGE

DATED: JANUARY 12, 2005

Exhibit 2

H Only the Westlaw citation is currently available.

United States District Court, N.D. Illinois, Eastern Division.

BASF CORPORATION, Plaintiff,

v.

THE OLD WORLD TRADING COMPANY, INC., Defendant.

No. 86 C 5602.

Sept. 8, 1992.

MEMORANDUM OPINION AND ORDER

LEINENWEBER, District Judge.

***1** On May 25, 1992, the court made Findings of Fact and Conclusions of law upon which judgment was entered in favor of the plaintiff, BASF Corporation ("BASF"), in the amount of $2,498,726, together with prejudgment interest and attorney's fees. BASF now seeks to alter or amend the judgment pursuant to Federal Rules of Civil Procedure 59(e) and to amend the Findings of Fact and Conclusions of Law pursuant to Rule 52(b).

Rule 59(e) Motion

1. BASF points out that on the Rule 58 judgment order entered by the court, the last sentence inadvertently ends with the words "this case is dismissed in its entirety." What the court meant to say was that all of BASF's claims had been dealt with and disposed of. The last sentence of the Rule 58 judgment order is hereby amended to read as follows:

"The court has previously granted Old World's motion for summary judgment on Count II. The court reserves jurisdiction over the award of costs, attorney's fees, and prejudgment interest."

2. BASF next contends that the court erroneously failed to award BASF its profits on lost customer sales occurring in the 1988 antifreeze year, i.e., the period between April 1, 1987 and March 31, 1988. With respect to lost customer sales for the 1988 antifreeze year, the court made Finding of Fact No. 36 that defendant, Old World Trading Company, Inc. ("Old World"), terminated its business relationship with Dearborn Chemical Company ("Dearborn") with the conclusion of the 1987 antifreeze year which was March 31, 1987, and did not purchase inhibitor chemicals from Dearborn after that date. The court, therefore, declined to award BASF any lost profits due to lost 1988 antifreeze sales. BASF asks the court to amend the judgment to include damages for at least a portion of 1988 because it contends that Old World continued to blend the Dearborn formula up to at least July 24, 1987.

The basis for the court's Finding of Fact was the testimony of George Beck ("Beck") and other witnesses called by BASF, and the absence of any direct evidence of sales of the Dearborn formula to Old World customers in 1988, even though there was some evidence that Old World continued to blend the Dearborn formula at some of its blending stations.

Specifically, Beck, a salesman for Dearborn in charge of the Old World account, testified that Dearborn lost the Old World account for the 1988 season, when Old World went exclusively with the Peak formula and gave Dearborn no more orders (Tr. 1225-1226). Richard Tumm, Dearborn's director of sales, testified in a similar vein (Tr. 444 and 458-459). John Hurvis, Old World's chairman, testified that the relationship with Dearborn ended on or about that date (Tr. 612 and 632-633). The evidence to the contrary consisted of blending records which indicate some blending may have occurred after April 1, 1987 (presumably with leftover Dearborn inhibitors in stock). There was also testimony of Larry Birch ("Birch") of Citgo attempting to interpret a reference in a memorandum to the effect that Old World was holding 90,000 gallons of the Dearborn formula for sale by Citgo. However, in the same memo, Birch is advised of the BASF lawsuit against Old World based on the formula failing to met Ford's specifications. There was no evidence that Citgo ever sold or even took possession of this product.

***2** BASF next argues that the records Old World produced and identified through Jeff Grizzle at his deposition show that all of Old World's blenders continued to blend the Dearborn formula for varying periods of time after April 1, 1987, up until July, 1987. However, these records were to the best of the court's knowledge not submitted to the court as part of the record in the case. These records, at least the summary prepared and submitted by BASF, does not tell to whom the antifreeze was sold. The evidence was that the heaviest call for antifreeze commenced in late July or early August (Tr. 458). Finally, the customers claimed lost by BASF were aware of BASF's pending lawsuit against Old World and the charge that the Old World antifreeze did not meet its claims. It is hard to believe that BASF lost any sales because of the false claims of Old World after April 1, 1987.

3. BASF also claims that the court's market share analysis improperly used the entire antifreeze market instead of just the private label market. It contends that its share of the non-Old World private label market was 28 percent in 1985 and rose to 34 percent in 1988, instead of the 15.6 percent to 21.2 percent of the total antifreeze market utilized by the court in its damage calculations. However, BASF did not introduce evidence of the respective market shares in the private label market.

BASF in its reply brief explained how it computed its percentage of the private label market. It deducted the market share percentage of Union Carbide, manufacturer of Prestone, from the total market and computed BASF's percentage share of that remaining on the theory that all of Union Carbide's market share was in the branded market. However, the evidence disclosed that Union Carbide was a strong player in the private label market and did not exit this portion of the antifreeze market until near the end of the 1987 antifreeze year [FN1] (Finding of Fact No. 20). Thus, during the damage period as established by the Findings of Fact, Union Carbide was a strong competitor of BASF in the private label market. *See* Defendant's ex.D. It may well have been the competition provided by Old World that led Union Carbide to the decision to get out of the private label market, which, of course, greatly benefited those that remained in it, such as BASF and Old World. Therefore, in the absence of direct testimony on the subject, to conclude what the respective market shares are of the private label market would require the court to undergo a great deal of speculation, which the court is unwilling to do.

It can be argued that the court in awarding damages to BASF based on market share of the total antifreeze market has already engaged in speculation. *See* Findings of Fact and Conclusions of Law, p. 24, n. 2. However, the court had no choice but to speculate in order to award BASF some damages, which the court felt was deserved. Some speculation is always required when it is necessary to construct a world absent some offending conduct. This is usually referred to as requiring the wrongdoer to bear the risk of the uncertainty which his wrong created. *Otis Clapp & Son, Inc. v. Filmore Vitamin Co.,* 754 F.2d 738 (7th Cir.1985). BASF's trial strategy was to go for the "home run" and shoot for 100 percent of the business that went from BASF to Old World and ignore the probability that some or most of the business would go elsewhere. This forced the court to devise its own formula for the award of damages and, in doing so, the court used the best available evidence introduced at trial.

*3 It was clear from the testimony of representatives of each of the customers in question who were called to testify by BASF and Old World, that each was angered at BASF because of perceived price inflexibility, that each had a relationship with one or more of BASF's other private label competitors before it purchased from Old World, that each considered others at the time it was considering purchasing from Old World, and that some of them did purchase a portion of their requirements from others besides Old World. In fact, both Citgo and Phillips had actually terminated BASF as a supplier before awarding the business to Old World. Phillips said it would not have purchased from BASF under any circumstances. Findings of Fact Nos. 50 and 51. The court rejected Old World's argument that it should award BASF nothing for these accounts (and the five others to which there was no testimony) because it was possible in a market where Old World was not making misrepresentations that BASF might well have been more competitive (Finding of Fact No. 54). However, being competitive is not the same as getting orders. It is not enough to say that the accounts had they not gone to Old World would have gone (or remained) with BASF. "*Post hoc ergo propter hoc* will not do...." *Schiller & Schmidt, Inc. v. Nordisco Corporation,* Nos. 91-2195, 91-2781, slip op. 10-11(7th Cir. July 23, 1992). The short of the matter is that BASF presented damage opinion evidence that gave the court no alternative short of total victory, to which it was clearly not entitled. The court attempted to fashion as fair an award as possible under the circumstances and the evidence. This is all it was required to do. *Otis Clapp,* at 744. The court declines to alter the award of damages or the Findings of Fact in support of them.

4. BASF complains next about the court's failure to order disparagement of profits, enhancement, or punitive damages. Under the Lanham Act, an award is governed by equitable principles. The court exercised its discretion in declining to apply any of these three elements to the award. The court sees no reason to alter these portions of the court's Conclusions.

5. BASF was awarded prejudgment interest to "be compounded annually." The year is the anti-freeze year, i.e., April 1 to March 31. The prejudgment interest is to continue until the judgment is final. BASF's two calculations are rejected and it is ordered to submit a third.

Old World's Counterclaim

The court found in favor of Old World on its claim against BASF for product disparagement. There was evidence that BASF employees told customers that Old World used reclaimed glycol or "bottoms." The court found that this charge was not true. Accordingly, the court will not disturb the counterclaim.

Rule 52(b) Motion

Request to Amend Findings

Finding No. 4

The court fails to see any inaccuracy in Finding No. 4.

Finding No. 37

The evidence at the trial disclosed that the engine by which Janeway Engineering was conducting the Dynamometer test overheated, which the court equated with equipment failure.

Finding No. 33

*4 The court found that Old World had misrepresented its product by claiming that it met certain specifications for which it had not tested. The purpose of quality control it to insure that a product is within certain specifications. Since the Old World product was not within specifications, quality control is irrelevant, unless it claimed that it performed to a certain quality control level, which Old World did not.

Finding No. 17

BASF attempted to call as witnesses certain individuals who were dissatisfied with the Old World product. The court disallowed this evidence partially on the basis of Rule 403. The court felt, and continues to feel, that anecdotal evidence, unless accompanied by testimony that such evidence was statistically significant, was irrelevant and would consume too much time. The court did suggest that BASF compile a list of consumer complaints and, if accompanied by testimony that the number of complaints was statistically significant, the court would consider the evidence. BASF did not provide the court with the statistical significance of the number of complaints. Admission of such evidence would invite Old World to call satisfied customers and the trial would still be going on.

Finding No. 34

The court found that the Old World product met the Cummins' specification. By that, the court meant to find that the Old World product met the Cummins' low silicate level. Accordingly, the court will amend the last sentence of Finding No. 34 to read as follows:

"The court, therefore, finds that Old World did not make a misrepresentation to the extent that it claimed that its AF met the Cummins' low silicate specification."

Finding Nos. 37 and 38

The court declines to make any changes in Finding Nos. 37 and 38.

CONCLUSION

The court amends the Rule 58 judgment entered in the case as described in paragraph 1 above. The court also amends the last sentence of Finding of Fact No. 34. The remainder of BASF's motion is denied.

IT IS SO ORDERED.

FN1. It should be recalled that the antifreeze year runs from April 1 of the previous year to March 31 of the year in question. *See* Findings of Fact and Conclusions of Law, p. 4 n. 1.

N.D.Ill.,1992.
BASF Corp. v. Old World Trading Co., Inc.
Not Reported in F.Supp., 1992 WL 232078 (N.D.Ill.)

END OF DOCUMENT

Exhibit 3

Only the Westlaw citation is currently available.

United States District Court, N.D. Illinois, Eastern Division.

Dan BERAHA, M.D., Plaintiff,

v.

BAXTER HEALTHCARE CORPORATION, Defendant.

No. 88 C 9898.

Sept. 6, 1994.

MEMORANDUM OPINION AND ORDER

CASTILLO, District Judge.

***1** Defendant, Baxter Healthcare Corporation ("Baxter"), and plaintiff, Dan Beraha, M.D. ("Beraha"), have filed various motions *in limine* which the court will address in turn.

A. *Beraha's Motion in Limine to Exclude Letters Containing Offers of Compromise.*

Beraha's motion seeks to exclude four letters sent by Baxter which referenced the possible settlement of the parties' dispute. Baxter in response has stated that it does not intend to introduce the letters to prove or disprove liability. Rather, Baxter intends to offer the letters to establish: (1) it did not act with any improper motive or bad faith by delaying the termination of the agreement; (2) it did not delay or fail to respond to a letter Beraha wrote to Baxter; and (3) that Beraha failed to mitigate his damages.

Settlement offers are inadmissible if offered to prove liability or damages. Fed.R.Evid. 408; *Cates v. Morgan Portable Bldg. Corp.*, 780 F.2d 683, 691 (7th Cir.1985). However, the exclusionary rule does not apply when the evidence is offered "for another purpose, such as proving bias or prejudice of a witness, negativing a contention of undue delay, or proving an effort to obstruct a criminal investigation or prosecution." Fed.R.Evid. 408. Whether evidence should be admitted for another purpose is within the discretion of the district court. *Bhandari v. First Nat'l Bank of Commerce*, 808 F.2d 1082, 1103 (5th Cir.1987).

Courts generally have excluded evidence of settlement offers unless the party seeking to exclude the evidence has put the contents of the offers in issue. For example, in *Boston Sea Party Restaurants, Inc. v. Luiggi's of Schaumburg, Inc.*, No. 90 C 269, 1990 WL 207442 (N.D.Ill. Dec. 1, 1990), the defendant argued that plaintiff had failed to mitigate its damages by unreasonably delaying attempts to relet the premises after defendants breached the lease. The court allowed plaintiff to admit evidence of settlement discussions in which the defendants had given plaintiff assurances of their performance under the lease to demonstrate that it reasonably relied on defendants' assurances, and therefore did not unreasonably delay in mitigating damages. *Id.* at *5. *See also* *Urico v. Parnell Oil Co.*, 708 F.2d 852, 854-55 (1st Cir.1983) (court allowed plaintiffs to introduce settlement discussions to show that insurer wrongfully refused to make a reasonable settlement offer to rebut defendant's argument that plaintiff failed to mitigate damages).

In the present case, Baxter has not claimed that Beraha has put the contents of the letters at issue with respect to his duty to mitigate. Rather, Baxter intends to use the letters to prove that Beraha could have mitigated his damages by accepting its settlement offer: "If Beraha had accepted Baxter's offer, Beraha would have been able to offer a license to another company on presumptively advantageous terms." Def.'s Resp. at 6. This purpose is exactly what is impermissible under Rule 408. As stated in *Anheuser-Busch Inc. v. Algonquin Road Limited Partnership*, No. 89 C 1468, 1992 WL 373159, at *2 (N.D.Ill. Dec. 10, 1992): "[S]ettlement offers do not trigger the duty to mitigate. There is no duty to surrender the claim in order to mitigate damages." *See also* *Pierce v. F.R. Tripler & Co.*, 955 F.2d 820, 826-28 (2d Cir.1992) (court would not allow employer to admit evidence that as part of a settlement it offered plaintiff back his job in order to show that plaintiff failed to take reasonable steps to mitigate his damages). Therefore, Beraha's motion is granted to the extent he seeks to exclude from evidence offers of compromise designed to show that Beraha failed to mitigate his damages by rejecting Baxter's settlement offer.

***2** However, if Beraha makes reference to the letters at trial, or in any way "opens the door" to their admission, the court will reconsider this decision. Thus, Baxter may be permitted to use the offers of compromise for the sole purpose of rebutting any argument which is offered by Beraha that Baxter either (1) failed to respond to Beraha's July 1988 letter or (2) attempted to perpetuate the parties' agreement in bad faith and with improper motive. *See, e.g.,* Barr Co. v. Safeco Ins. Co., No. 83 C 2711, 1988 WL 64558, *6 (N.D.Ill. June 15, 1988) (allowing plaintiff to admit settlement offer into evidence because it was germane to the question of defendant's bad faith in delay).

The motion is GRANTED in part.

B. *Baxter's Motions in Limine*

1. *Motion in Limine to Preclude Evidence Contrary to the Law of the Case as set forth in Beraha v. Baxter Healthcare Corp., 956 F.2d 1436 (7th Cir.1992).*

Baxter has moved to preclude the admission of evidence which it considers contrary to the dictates of the Seventh Circuit's earlier opinion in this case.

Both parties have quoted selectively only those portions of *Beraha v. Baxter Healthcare Corp.,* 956 F.2d 1436 (7th Cir.1992) which are helpful to their respective positions. The court's own review of the opinion reveals that the Seventh Circuit envisioned any application of the covenant of good faith and fair dealing to include consideration of *both* whether Baxter's actions comport with a judgment reasonable to an ordinary business person and what Baxter's and Beraha's expectations were at the time they entered into the contract. In a contract that vests one party with discretion, the covenant of good faith and fair dealing requires that such a party "must exercise that discretion reasonably and with proper motive, and may not do so arbitrarily, capriciously, *or* in a manner inconsistent with the reasonable expectations of the parties." *Id.* at 1443 (quoting *Dayan v. McDonald's Corp.,* 466 N.E.2d 958, 972 (Ill.App.Ct.1984)) (emphasis added); *see also* *Michigan Avenue Nat'l Bank of Chicago v. Rogers,* No. 93 C 2932, 1994 WL 330275, *4 (N.D.Ill. July 1, 1994).

Thus, the court denies Baxter's attempts to prevent the jury from hearing evidence relating to Beraha's subjective expectations regarding Baxter's performance, evidence relating to the "Chaltiel letter," and evidence relating to Baxter's representations to Beraha. All of this evidence, although insufficient to form the basis of independent causes of action, is still relevant to the breach of contract claim that remains in this case. Ultimately, the trier of fact will determine whether the parties' expectations were reasonable.

The motion is DENIED.

2. *Motion in Limine for Separate Trials of Liability and Damages.*

Baxter has moved to bifurcate the liability and damages portions of the trial. In response, Beraha cavalierly states that the trial of the damage issue is likely to add no more than 1-2 hours to the overall length of the trial, and that he will be prejudiced by a bifurcation.

***3** Federal Rule of Civil Procedure 42(b) states in relevant part:

The court, in furtherance of convenience or to avoid prejudice, or when separate trials will be conducive to expedition and economy, may order a separate trial of any claim ... or issues.

Local Rule 21 further states:
The court, however, may proceed to trial upon all or any combination of issues if, in its discretion, and in furtherance of justice, it shall appear that a separate trial will work a hardship upon any of the parties or will result in protracted or costly discovery.

Ultimately, whether to separate the issues of liability and damages in a civil case is reserved to the discretion of the trial court. *Davis v. Freels,* 583 F.2d 337, 343 (7th Cir.1978); *Keyes Fibre Co. v. Packaging Corp. of America,* 763 F.Supp. 374, 375 (N.D.Ill.1991).

Despite his cavalier response, during oral argument Beraha's counsel was not able to identify any specific way in which a bifurcated trial would unfairly prejudice his position. Moreover, it is evident that several witnesses, including expert witnesses, will testify solely with respect to the issue of the proper damages to be awarded in this case. The court's own experience indicates that a bifurcated trial therefore may save considerable trial time, a precious commodity in this day and age. Accordingly, the court has decided to bifurcate the liability and damages phases of this trial, with the understanding that the damages phase will begin immediately if Beraha succeeds in establishing liability.

The motion is GRANTED. Fed.R.Civ.P. 42(b), Local Rule 21.

3. *Motion in Limine to Preclude Reference to Attorney-Client Communications.*

Lastly, Baxter moves to prevent any reference to attorney-client communications between Paul C. Flattery, one of its in-house attorneys, and other Baxter employees, including specifically Victor Chaltiel. Baxter is concerned that Beraha is seeking to have an adverse inference drawn from the mere fact that such attorney-client communications took place.

Beraha in response states that he is not attempting to inquire into the substance of any privileged communication. It is axiomatic that mere reference to the fact that a conversation between attorney and client occurred is not privileged. 8 Charles A. Wright & Arthur R. Miller, Federal Practice and Procedure § 2017 (1970). Normally, mere reference to an attorney-client communication therefore is not prohibited by the attorney-client privilege.

Nevertheless, in this case it is evident from the oral argument made by Beraha's counsel that the only purpose for which Beraha seeks to admit evidence of the fact that these communications occurred is to enable the jury to draw an adverse inference therefrom. This is exactly what is prohibited. *Hamann v. Johnson & Johnson,* No. 4-81-922, 1985 WL 2461, *5 (D.Minn. July 22, 1985); *A.B. Dick v. Marr,* 95 F.Supp. 83, 101 (S.D.N.Y.1950). Therefore, the court finds that the probative value of the mere fact that these privileged conversations occurred is substantially outweighed by its potentially unfair prejudicial effect. *See*Fed.R.Evid. 403.

***4** The motion is GRANTED.[FN1]

The parties are ordered to advise their respective witnesses of this order prior to the time they testify at trial.

The parties also are advised that the rulings contained in this order may be modified as the court hears evidence within the context of the trial.

SO ORDERED.

FN1. This ruling will in no way prohibit Beraha from introducing evidence regarding his dealings with Paul Flattery to the extent Flattery was involved in the contract negotiations. These are not covered by the attorney-client privilege.

N.D.Ill.,1994.
Beraha v. Baxter Healthcare Corp.
Not Reported in F.Supp., 1994 WL 494654 (N.D.Ill.)

END OF DOCUMENT

Exhibit 4

LEXSEE 2007 US DIST LEXIS 42754

MARY COLLEEN BROESKI, Plaintiff, vs. PROVIDENT LIFE AND ACCIDENT INSURANCE COMPANY, Defendants.

No. 06 C 3836

UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION

2007 U.S. Dist. LEXIS 42754

June 8, 2007, Decided
June 8, 2007, Filed

COUNSEL: [*1] For Mary Colleen Broeski, Plaintiff: Edward M Kraus, LEAD ATTORNEY, Chicago-Kent College of Law, Illinois Institute of Technology, Chicago, IL.

For Provident Life and Accident Insurance Company, Defendant: Michael J. Smith, LEAD ATTORNEY, Attorney at Law, Chicago, IL; W. Sebastian von Schleicher, Michael J. Smith & Associates, Chicago, IL.

JUDGES: SIDNEY I. SCHENKIER, United States Magistrate Judge. Judge Robert Gettleman.

OPINION BY: SIDNEY I. SCHENKIER

OPINION

MEMORANDUM OPINION AND ORDER

Plaintiff has filed this ERISA action, pursuant to *29 U.S.C. § 1132(a)(1)(B)*, seeking an award of disability benefits pursuant to a group policy for long term disability ("LTD") benefits issued by defendant Provident Life and Accident Insurance Company ("Provident Life"). [1] Plaintiff alleges that as a result of injuries she suffered during a battery, plaintiff was unable to continue her employment as a registered nurse and thus began receiving LTD benefits beginning on November 28, 2000. Under the terms of the group policy, after a two year period, plaintiff was eligible for continued LTD benefits only if she were unable to work not only in her occupation as a registered [*2] nurse, but more broadly in any occupation for which she was or may become suited by education, training or experience. By letters dated December 22, 2003 and January 27, 2004, Provident Life concluded that plaintiff did not meet that standard, and thus terminated plaintiff's LTD benefits. Provident Life reaffirmed that decision in a letter dated July 14, 2004.

1 The complaint also named as a defendant UnumProvident Corporation ("Unum"), which plaintiff alleges is the parent corporation of Provident Life (Compl., PP 6-7). By an order dated October 3, 2006, the presiding district judge dismissed the complaint as to Unum (doc. # 15).

In this lawsuit, plaintiff challenges the decision by Provident Life to discontinue her LTD benefits. Plaintiff seeks a judgment requiring payment of benefits since the date of discontinuation (with prejudgment interest); a judgment requiring continued LTD benefits to be paid into the future so long as plaintiff meets the requirements for eligibility; and attorneys' fees and costs. [*3] There appears to be no dispute that the group policy grants Provident Life discretionary authority to make benefit decisions (Def.'s Resp., Ex. A, at 27), with the result that Provident Life's decision to discontinue plaintiff's LTD benefits must be reviewed under an arbitrary and capricious standard -- "the least demanding form of judicial review of administrative action." *Semien v. Life Ins. Co. of North America, 436 F.3d 805, 812 (7th Cir. 2006)* (quoting *Trombetta v. Cragin Fed. Bank for Savings Employee Stock Ownership Plan, 102 F.3d 1435, 1438 (7th Cir. 1996))*. Under that standard, "when there can be no doubt that the application was given a genuine evaluation, judicial review is limited to the evidence that was submitted in support of the application for benefits, and the mental processes of the Plan's administrator are not legitimate grounds of inquiry any more than they would be if the decisionmaker were an administrative agency." *Perlman v. Swiss Bank Corp. Comprehensive Disability*

Protection Plan, 195 F.3d 975, 982 (7th Cir. 2000). Thus, in suits seeking judicial review of benefit decisions under an arbitrary and capricious [*4] standard, discovery will rarely be permitted. *See Semien, 436 F.3d at 814.*

But, rarely does not mean never. And, in the motion now before the Court, plaintiff argues that this is a case in which limited discovery is appropriate because she has alleged that the decision denying benefits was affected by bias or misconduct. Based on this theory, plaintiff seeks leave to conduct discovery (doc. # 30). Specifically, plaintiff seeks leave to serve eight interrogatories and eleven document requests on Provident Life. Provident Life resists the motion, arguing that plaintiff's allegations are insufficient to open the door to discovery. For the reasons set forth below, we agree with Provident Life, and therefore deny plaintiff's motion for leave to conduct discovery.

I.

The Seventh Circuit has explained that "[a]lthough discovery is normally disfavored in the ERISA context, at times additional discovery is appropriate to insure that Plan administrators have not acted arbitrarily and that conflicts of interest have not contributed to any unjustifiable denial of benefits." *Semien, 436 F.3d at 814-15.* In *Semien,* the Court held that "[a] claimant [*5] must demonstrate two factors before limited discovery becomes appropriate. First, a claimant must identify a specific conflict of interest or instance of misconduct. Second, a claimant must make a *prima facie* showing that there is a good cause to believe limited discovery will reveal a procedural defect in the Plan administrator's determination." *Semien, 436 F.3d at 815.* The *Semien* court commented that "[w]hile this standard essentially precludes discovery without an affidavit or factual allegation, we believe that this approach is the only reasonable interpretation of ERISA." *Id. at 815.*

We analyze below the two allegations that plaintiff makes in an effort to satisfy the *Semien* test. We conclude that neither of the allegations warrants the discovery under *Semien.*

A.

Prior to the decision to discontinue LTD benefits, Provident Life sent plaintiff to Dr. Marshall Matz for an independent medical examination ("IME"). As a result of that IME, Dr. Matz wrote a seven-page letter analyzing plaintiff's condition and concluding that, "[f]rom a neurosurgical perspective, I find no restrictions or limitations with regard to [plaintiff] [*6] returning to work in her prior capacity" (Def.'s Resp., Ex. D, at 7). Plaintiff alleges that Dr. Matz's opinion was the only report that Provident Life cited for the decision to discontinue LTD benefits (Compl. P 29). Plaintiff further alleges that Dr. Matz is regularly retained by insurers, disability plans or other institutional defendants "to provide medical opinions and testimony in support of the position that a particular individual is not disabled;" that, as a result of that work, Dr. Matz "has a bias for insurers/defendants in disability matters and against plaintiffs seeking to prove that they are disabled;" and that Provident Life was aware that Dr. Matz "was not truly an independent and unbiased medical examiner at the time that they selected him to review Plaintiff's claim" (Compl., PP 30-31). These allegations of bias by Dr. Matz are insufficient to trigger discovery under *Semien.*

First, these allegations are conclusory, and are not supported by affidavit or factual allegations (*i.e.,* evidence) as required by *Semien.* The fact that a doctor is regularly consulted by an insurance company (or defense interests more generally) does not, *ipso facto,* render [*7] the doctor biased. Were that the case, any time an insurer used in-house doctors in deciding eligibility for benefits, a plaintiff challenging a denial of benefits could claim bias and open the door to discovery. Such a result would make discovery in those cases the rule and not the exception, which plainly is not the law. *Davis v. Unum Life Ins. Co. of America, 444 F.3d 569, 575 (7th Cir.), cert. denied, 127 S. Ct. 234, 166 L. Ed. 2d 147 (2006)* (rejecting a claim that an administrator's use of in-house doctors creates a conflict of interest).

Second, plaintiff's reference to a letter she wrote complaining about Dr. Matz's conduct during the IME (Pl.'s Mem. at 6-7) fails to provide *prima facie* evidence of bias or misconduct. We understand that a claimant, who was denied LTD benefits, such as plaintiff here, naturally would be dissatisfied with the doctor who opined that she was not disabled. Indeed, we think it would be a rare plaintiff who would not be unhappy with a doctor under those circumstances. That reality underscores why a plaintiff's criticism of a doctor as "biased" is not sufficient to satisfy the *Semien* standard for opening the door to discovery; [*8] again, were it otherwise, discovery plainly would be the norm and not the exception. Moreover, in this case, there is an additional reason to find that the plaintiff's criticisms of Dr. Matz are insufficient to meet the *Semien* standard. She did not raise any of the criticisms she now levels against Dr. Matz, including the criticisms of his conduct toward plaintiff during the IME, until after Dr. Matz had issued his opinion.

Third, plaintiff fails to address the evidence offered by Provident Life that Dr. Matz's opinion did not stand alone. Dr. Thomas reviewed Dr. Matz's IME and found it to be "credible": he stated that the conclusions reached by Dr. Matz "appear to be based upon reasonable review of the information and are consistent with the evaluation"

(Def.'s Resp., Ex. E). In addition, after Dr. Matz's review, Dr. Sternbergh found that "medical evidence, to a reasonable degree of medical certainty, would support the claimant's ability to do sedentary work, with accommodation to prevent repetitive flexions/extensions of the cervical spine, as well as repetitive reaching or overhead work with the left upper extremity" (*Id.*, Ex. F, at 4). Plaintiff does not suggest that [*9] either Dr. Thomas or Dr. Sternbergh were biased, and their views either agreed with that of Dr. Matz (in the case of Dr. Thomas) or, despite some differences, nonetheless would support denial of LTD benefits (in the case of Dr. Sternbergh). This evidence -- offered in defendant's response and ignored in plaintiff's reply -- further undermines plaintiff's ability to make a *prima facie* showing that the discovery sought as to Dr. Matz would reveal "a procedural defect in the Plan administrator's determination." *Semien, 436 F.3d at 815.*

B.

In support of her request for discovery, plaintiff also alleges that a governmental investigation, which resulted in a "regulatory settlement agreement," "raises significant concerns relating to systematic unfair claims adjudication practices by UnumProvident and its subsidiaries identical to the ones presented in this matter and during the same time period" (Compl., P 33). This reference to the regulatory settlement agreement, even when coupled with the conclusory assertion that it raises "significant concerns relating to systemic unfair claims adjudication practices," does not satisfy plaintiff's obligation under *Semien* [*10] to offer a *prima facie* showing of misconduct. A settlement agreement is not an adjudication (or even evidence of) misconduct. Indeed, the regulatory settlement agreement upon which plaintiff relies specifically makes this point: it states that the settlement is without any admission of fault or liability, and that the settlement may not be offered as evidence of any admission of liability or wrongdoing (Pl.'s Mem., Ex. 1, PP 11-12). Moreover, the settlement agreement specifically provides that it may not be interpreted to create any rights of participants in ERISA-covered plans, "including any appeal or review rights under the Plan" (*Id.* P 13).

To the extent that plaintiff uses the regulatory settlement agreement to establish misconduct by Provident Life, that effort flies in the face of these provisions making clear that the settlement did not include an admission of liability (as might be the case in a consent decree or judgment). In addition, plaintiff's attempted use of the regulatory settlement agreement is at odds with at least the spirit of *Federal Rule of Evidence 408*, which provides that evidence of a settlement agreement cannot [*11] be used to prove liability. Allowing plaintiff to use the settlement agreement in this fashion would run contrary to the intent of the parties to the agreement, and could create disincentives toward entering into settlement agreements.

Finally, the sense of plaintiff's argument is that the settlement agreement shows that Provident Life routinely deprives claimants of fair consideration of their benefits requests. Thus, were we to accept plaintiff's effort to obtain discovery based on this settlement agreement, that would open the door to allowing discovery in every case challenging a Provident Life decision denying benefits. A voluntary settlement agreement that contains no findings or admissions of misconduct cannot bear this weight that plaintiff seeks to place upon it. [2] For all of these reasons, we conclude that plaintiff's allegation concerning the regulatory settlement agreement does not entitle her to discovery under the standards set forth in *Semien.* [3]

2 In a further effort to establish that Provident Life routinely deprives claimants of fair consideration, plaintiff cites a number of cases in which conduct by Unum or Provident Life has been criticized (Pl.'s Mem. at 9-10). Defendant responds by citing cases finding that Unum and Provident Life and related subsidiaries provided "full and fair" review in the exercise of discretionary authority (Def.'s Resp. at 10). We agree that the cases cited by plaintiff do not satisfy their burden under *Semien* of making a *prima facie* showing of a conflict of interest or instance of misconduct with respect to the LTD benefit denial at issue here.

[*12]

3 Plaintiff cites to a number of decisions outside this circuit which have allowed discovery to proceed (see, *e.g.,* Pl.'s Mem. at 8). We conclude that those cases reflect an approach to discovery in ERISA cases different than that set forth in *Semien*, which is controlling Seventh Circuit authority that we are bound to follow.

CONCLUSION

For the foregoing reasons, plaintiff's motion for leave to conduct discovery (doc. # 30) is denied. The matter is set for a status conference on June 21, 2007, at 9:00 a.m.

SIDNEY I. SCHENKIER

United States Magistrate Judge

Dated: June 8, 2007

Exhibit 5

H

United States District Court, S.D. New York.
Frederick W. CRIGGER, Dsmckee Investments Inc., Jack Schueler, Eva Schueler, and Csdesign Inc., Plaintiff,
v.
FAHNESTOCK AND COMPANY, INC., and Aurelio Vuono, Defendants.
No. 01CIV781JFK.

April 14, 2005.

MEMORANDUM OPINION and ORDER

KEENAN, J.
*1 Defendant Fahnestock and Company, Inc. ("Fahnestock") moves to admit into evidence the terms of the settlement agreement between Plaintiffs and former defendant Raymond Minicucci. Plaintiffs object. For the reasons that follow, the Court will permit Fahnestock to introduce evidence of the *fact* of Plaintiffs' settlement with Minicucci, but not evidence of the *amount* of the settlement.

Fahnestock makes two arguments in favor of admitting the terms of the settlement. First, Fahnestock claims that it was unfairly prejudiced by a portion of Plaintiffs' opening statement. Mr. Kim, Plaintiffs' counsel, told the jury:

The reason we're here, ladies and gentlemen, is that two of the parties involved in this scheme have refused to take any responsibility for what happened.

(Tr. 40:23-25). The jury already knows that Plaintiffs did not sue Messrs. Mason, Capland and Feldman, the three Canadian promoters. Fahnestock and Vuono are in Court. The jury could infer from the foregoing facts that Minicucci is the only party who has taken "responsibility"-*i.e.,* settled. Fahnestock argues that the jury can further infer from Mr. Kim's statement that Minicucci settled on "onerous" terms, leading to the prejudicial conclusion that Fahnestock is liable under *respondeat superior* for the Minicucci's "serious wrongdoing." This inference would be incorrect because the settlement actually was rather modest, given the amount of recovery sought in the Complaint. Fahnestock wants to dispel this misconception, if it exists. (*See* Ltr. from Proskauer Rose to Court, Apr. 12, 2005).

Second, Fahnestock seeks admission of the settlement in order to impeach Minicucci, if he is called to the witness stand. Fahnestock contends that Fed.R.Evid. 408 provides that evidence of a settlement may be offered to prove the witness's bias or prejudice. In the event that Minicucci testifies and makes statements inconsistent with his deposition testimony, or otherwise opens the door to impeachment, Fahnestock seeks to prove the fact and amount of the settlement. (*Id.*).

Rule 408 excludes evidence of compromises or compromise negotiations tending to prove liability for, or invalidity of, a claim. This rule is applicable regardless of which party offers the evidence concerning a settlement or settlement offer. *Pierce v. F.R. Tripler & Co.,* 955 F.2d 820, 828 (2d Cir.1992). The rule also applies with equal force whether the settlement involves the litigants or a litigant and a third party. *Kennon v. Slipstreamer, Inc.,* 794 F.2d 1067, 1069 (5th Cir.1986); *McInnis v. A.M.F.,* Inc., 765 F.2d 240, 247 (1st Cir.1985).

According to *Weinstein's Federal Evidence* § 408.04 (2d ed.2005):

Rule 408 codifies the general practice of the federal courts in making compromise agreements inadmissible in such circumstances as proof of liability for, or invalidity of, the claim or its amount.... Even if the fact of the settlement is admissible for a purpose other than proof of liability, disclosure of the settlement amount may constitute reversible error.

*2 This is sound policy. The jury might be inclined to speculate why a person in Mr. Minicucci's position is not in the courtroom with Fahnestock and Mr. Vuono. Disclosure of the *fact* of the settlement will prevent any juror confusion or speculation on this front. As evidence of the Minicucci settlement would not be offered to prove liability for, or invalidity of, the claim, Rule 408 is not offended.

Once the jury learns of the settlement, disclosure of its amount serves no purpose and could result in additional speculation. If the amount is high, the jury might infer that the settling defendant bears more responsibility for the plaintiff's injury than the non-settling defendant; if the amount is low, the jury might infer the opposite. *Kennon*, 794 F.2d at 1070. Either inference is potentially prejudicial and best avoided by keeping the settlement amount from the jury, regardless of who seeks to offer the evidence. *See e.g., Vincent v. Louis & Marx & Co.*, 874 F.2d 36, 42 (1st Cir.1989); *Kennon*, 794 F.2d at 1070; *Pioneer Hi-Bred Int'l, Inc. v. Ottawa Plant Food, Inc.*, 219 F.R.D. 135, 144 (N.D.Iowa 2003).

Fahnestock's arguments do not overcome these considerations. The Court disagrees that the jury may infer from Mr. Kim's remark that Minicucci settled for an "onerous" amount The most the jury can infer from Mr. Kim's opening statement is that Minicucci settled, and the Court is permitting evidence of the fact of the settlement to clear up any potential confusion here. The Court also notes that neither defendant objected to Mr. Kim's statement when he made it. (Tr. 40:23-25).

As for Minicucci, Fahnestock surely may use the fact of his settlement for impeachment purposes, if necessary. Fahnestock is technically correct that Rule 408 would not prevent the introduction of the amount of settlement for this purpose. Nevertheless, the Court finds that the well-known factors listed in Fed.R.Evid. 403 outweigh the probative value of the settlement amount in this context. While Rule 403 does not govern this issue, the Court notes that a Rule 403-type balancing of prejudice and relevance is appropriate in resolving a Rule 408 challenge to the admissibility of a settlement amount. *See Kennon*, 794 F.2d at 1076-77 (Thornberry, J., dissenting); *United States v. Am. Soc'y of Composers, Authors and Publishers*, 1989 WL 222654 at *9 (S.D.N.Y.1989), *aff'd sub nom Am. Soc'y of Composers, Authors and Publishers v. Showtime/The Movie Channel, Inc.*, 912 F.2d 563 (2d Cir.1990).

In light of the foregoing analysis, Plaintiffs' objection to introduction of the *fact* of Minicucci's settlement will be OVERRULED. Plaintiffs' objection to introduction of the *amount* of Minicucci's settlement will be SUSTAINED.

SO ORDERED.

S.D.N.Y.,2005.
Crigger v. Fahnestock and Co., Inc.
Not Reported in F.Supp.2d, 2005 WL 857368 (S.D.N.Y.), 66 Fed. R. Evid. Serv. 1239

END OF DOCUMENT

Exhibit 6

NOTICE: THIS IS AN UNPUBLISHED OPINION.

(The Court's decision is referenced in a "Table of Decisions Without Reported Opinions" appearing in the Federal Reporter. Use FI CTA9 Rule 36-3 for rules regarding the citation of unpublished opinions.)
United States Court of Appeals, Ninth Circuit.
Patrick CROSBY, Petitioner,
v.
UNITED STATES DEPARTMENT OF LABOR; Hughes Aircraft Company, Respondents,
No. 93-70834.

Argued and Submitted April 7, 1995.
Decided April 20, 1995.

Petition to Review Decision of the Secretary of Labor, No. 0973-2.
DOL

PETITION DENIED.

Before: McKAY,[FN*] REINHARDT, and FERNANDEZ, Circuit Judges.

FN* Hon. Monroe G. McKay, Senior United States Circuit Judge, United States Court of Appeals for the Tenth Circuit, sitting by designation.

MEMORANDUM [FN**]

FN** This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except as provided by Ninth Circuit Rule 36-3.

*1 Patrick Crosby appeals the Secretary of Labor's adoption of an administrative law judge's recommended decision and order to the effect that Crosby was not discriminated against by his former employer, Hughes Aircraft Company, in violation of the whistleblower provisions of various federal environmental statutes.[FN1] The Secretary ruled that Crosby had not shown that Hughes had terminated him for protected rather than non-discriminatory business reasons. We deny the petition.

FN1. Originally, Crosby brought his action under the provisions of the Clean Air Act, 42 U.S.C. § 7622, and the Toxic Substances Control Act, 15 U.S.C. § 2622. The Secretary granted his post-trial motion to amend his complaint to include a cause of action under the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. § 9610.

If an employee has made out a prima facie case of retaliatory discharge, the burden of production shifts to the employer to show that it had legitimate, non-discriminatory reasons for its actions.See St. Mary's Honor Ctr. v. Hicks, U.S. , , 113 S. Ct. 2742, 2747, 125 L. Ed. 2d 407 (1993). If it does so, the production burden shifts back to the plaintiff to show that those reasons were pretextual.Id. More to the point for purposes of this appeal, once an employment discrimination case has been tried, as this one has been, the only truly relevant question is whether the plaintiff has met his ultimate burden of proving to the trier of fact that he was the victim of intentional discrimination.See id. at , 113 S. Ct. at 2747-48.

The Secretary's decision should be upheld unless it is unsupported by substantial evidence or is arbitrary, capricious, an abuse of discretion or otherwise not in accordance with the law.5 U.S.C. § 706(2)(A), (E) (Administrative Procedure Act); Lockert v. United States Dep't of Labor, 867 F.2d 513, 516-17, 520 (9th Cir. 1989).

Here the Secretary determined that the reasons for Crosby's termination were that his work was not good and he was often insubordinate. Moreover, the final straw was his absolute refusal to work on the PPUP project because he did not like the protocol for the performance of that task. We understand that he sought to retract the refusal; alas, the decision had already been made.

Crosby does not contend that the actual working conditions related to the PPUP project were unsafe or unhealthy."Employees have no protection ... for refusing to work simply because they believe another method, technique, procedure or equipment would be better or more effective."Pensyl v. Catalytic, Inc., Case No. 83-ERA-2, at 8 (Sec. Dec. Jan. 13, 1984). When an employee's refusal to work does not meet the Pensyl test, an employer may legitimately terminate the employee.Wilson v. Bechtel Constr., Inc., Case No. 86-ERA-34, at 12 (Sec. Dec. Jan. 9, 1988). The record is filled with evidence of incidents of Crosby's supervisors' dissatisfaction with his work, which began long before he engaged in any protected activities at issue here. From the very beginning of his work for Hughes he resisted completing assignments given to him, refused to work on certain projects and even refused to pass on information to those who were brought in to complete the projects. Finally, he was asked to perform work on PPUP. His reaction was characteristic. He objected to the whole thing and finally said he would not work on the project at all. In short, there is evidence that Crosby fairly bristled with antagonism, complaints, foot dragging, insubordination, and fractiousness. The ALJ and the Secretary decided that his termination was based upon that. There is substantial evidence to support the decision.

***2** It is noteworthy that the individuals who terminated Crosby did not even know of most of his alleged protected activity. While they did hear him complain about PPUP, they did not understand that he was complaining about a possible environmental problem related to a gas detector system if PPUP were used with that system. What they did understand was that Crosby was, once again, refusing to do work that he was directed to do. The Secretary did not err when he found that Crosby was discharged for proper reasons.[FN2]

> FN2. The parties spill much ink over whether Crosby spelled out a prima facie case. We, of course, recognize that a prima facie case is the first step in a trial of this kind. However, given the ultimate determination, there is no need for us to delve into the intricacies of prima facie case building.

Crosby, however, complains of the procedures used to reach a decision in this case. He says that he was entitled to a continuance because certain discovery was delivered late. But though that continuance was denied him, after two days of hearings the proceeding was adjourned for five weeks. Thus, he effectively got his continuance anyway. He also asked that adverse inferences be drawn against Hughes because of the lateness of the discovery and because Hughes asserted a privilege as to some discovery which was sought. But the issue of sanctions is left to the discretion of the ALJ, and we see no abuse of that discretion here.See29 C.F.R. § 18.6(d)(2)(i). Moreover, it is not appropriate to draw adverse inferences from the failure to produce documents protected by the attorney-client and work product privileges.SeeWigmore on Evidence § 291 (rev. 1979).

Crosby further complains that he did not get to examine certain subpoenaed witnesses after the district court refused to enforce a subpoena for them. He said that adverse inferences should have been drawn, but the ALJ determined that their testimony would have been immaterial. Moreover, Crosby did have an opportunity to examine the officials who actually fired him. We see no reversible error.

Finally, Crosby complains that certain offers of proof were improperly relied upon. Those were made when the ALJ refused to hear testimony from certain Hughes witnesses and allowed Hughes to protect the record by stating what the witnesses' testimony would have been. The ALJ did not rely upon the offers at all. While the Secretary did refer to them, those occasional references were not necessary to the final decision and were accompanied by references to proper evidentiary matter. We are unable to say that Crosby's substantial rights were affected by those stray, though improper, references.See29 C.F.R. § 18.103.

PETITION DENIED.

C.A.9,1995.
Crosby v. U.S. Dept. of Labor
53 F.3d 338, 1995 WL 234904 (C.A.9)

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Exhibit 7

Only the Westlaw citation is currently available.

United States District Court, N.D. Illinois, Eastern Division.

Joardis DAVIS, Plaintiff,

v.

Harold M. ROWE, individually and doing business as Rowe Company Fine Arts; and the Rowe Company Fine Arts, Inc., an Illinois corporation, Defendants.

No. 91 C 2254.

Feb. 10, 1993.

MEMORANDUM OPINION

KOCORAS, District Judge:

***1** This matter comes before the Court on defendants' six motions in limine seeking to prohibit the plaintiff from presenting certain evidence and witness testimony at trial. For the following reasons, the motion is granted in part and denied in part.

First Motion in Limine: The Hartford Letter, the Rowe Statement, and the Davis Letter

Plaintiff, Joardis Davis ("Davis"), filed this suit to recover for the loss of art she had consigned to defendants, Harold M. Rowe, individually and doing business as Rowe Company Fine Arts, and the Rowe Company Fine Arts, Inc. (collectively referred to as "Rowe"). The art was destroyed in a fire on April 15, 1989. Under the Illinois Consignment of Art Act, Rowe is responsible to Davis for the fair market value of the Davis art in its possession at the time of the fire. Ill.Ann.Stat. ch. 121 1/2 , para. 1402(5) (Smith-Hurd Supp.1992). In addition, Rowe is responsible for paying Davis a portion of the insurance proceeds it received due to an insurance contract that Rowe procured in fulfillment of a consignment agreement between Davis and Rowe. On May 20, 1992, this Court denied Rowe's motion for summary judgment, finding that Davis' claims depended upon the fair market value of the art lost and that the fair market value of the consigned art at the time of the fire was an issue of fact to be determined by the jury at trial.

Citing Federal Rule of Evidence 408, Rowe asks this Court to prohibit Davis from submitting several statements made by Rowe concerning the value of the Davis art collection that was lost in the fire. The first statement that Rowe seeks to exclude from the jury was made October 19, 1989 by Harold M. Rowe ("the Hartford letter"). Harold Rowe indicated that "the value of the collection was $4,635,000." He later affirmed this under oath ("the Rowe statement"). Rowe secondly seeks to exclude a letter that was sent by the Rowe Company to Davis ("the Davis letter"), which states, "The total value of the art library and the works of art destroyed in the Rowe Company Gallery far exceeded the insurance coverage." [FN1] The Davis letter additionally states that "the parties ... recognize and acknowledge that the value of the consigned works of art of Warren Davis far exceeded $250,000."

Before we determine the merits of Rowe's motion in limine as to these statements, we first shall recount the principles of law that apply under Rule 408.

A. *The Legal Standard Under Rule 408*

Rule 408 makes inadmissible evidence of offers, acceptances, conduct, or statements made during settlement negotiations that are presented to prove a party's liability for or the invalidity of a claim or its amount.[FN2] Rule 408"does not require exclusion when the evidence is offered for another purpose, such as proving bias or prejudice of a witness...."

In *Kritikos v. Palmer Johnson, Inc.*, 821 F.2d 418 (7th Cir.1987), the Seventh Circuit commented upon the policy behind Rule 408 in addressing the situation of a plaintiff who had refused to accept late delivery of a yacht from the defendant shipbuilder on the ground that the yacht failed to meet specifications. Shortly after the plaintiff refused to accept late delivery of the yacht, the plaintiff's representative wrote letters summarizing discussions with the boat architects, discussions which indicated that the defendant was not responsible for all of the delays in delivery. The court held that the letters were not admissible under Rule 408 because they were written with the objective of advising the plaintiff of a possible compromise solution before legal action was commenced.

According to the court, the purpose of Rule 408 is "to encourage settlements. The fear is that settlement negotiations will be inhibited if the parties know that their statements may later be used as admissions of liability." *Kritikos,* 821 F.2d at 423 (quoting, *Central Soya Co., Inc. v. Epstein Fisheries, Inc.,* 676 F.2d 939 (7th Cir.1982)); *see also, U.S. v. Lorince,* 773 F.Supp. 1082, 1101 (N.D.Ill.1991). In view of this policy, documents prepared in connection with settlement efforts should not be admitted as evidence. *Lorince,* 773 F.Supp. at 1101 (citing, *Blu-J, Inc. v. Kemper C.P.A. Group,* 916 F.2d 637, 642 (11th Cir.1990) (holding that an independent evaluation prepared for purpose of exploring settlement was inadmissible under Rule 408; *Ramada Development Co. v. Rauch,* 644 F.2d 1097 (5th Cir.1981) (finding a report detailing flaws in construction of motel, which was commissioned as a basis for settlement negotiations, inadmissible)).

***2** Therefore, if we find that the statements that Davis seeks to admit into evidence were made within the context of settlement efforts, we shall exclude them under Rule 408. The question presented by the parties is how broadly to construe the term "settlement efforts." As Judge Moran noted in *Prudential Ins. Co. v. Curt Bullock Builders, Inc.,* 626 F.Supp. 159, 164 (N.D.Ill.1985), the admission of any statement made during, or any document prepared for, any kind of conciliation effort raises a Rule 408 issue. However, in order for this evidence to be excluded, a claim must actually be in dispute at the time the statement was made or that the document was prepared. *Id.* Several courts have found that an actual dispute existed sufficient to invoke Rule 408 even though the parties had not yet asserted their claims. *See e.g., E.E.O.C. v. Gear Petroleum, Inc.,* 948 F.2d 1542, 1544-45 (10th Cir.1991) (refusing to admit a letter from the defendant even though it was sent prior to the completion of the EEOC investigation); *Mundy v. Household Finance Corp.,* 885 F.2d 542, 546-47 (9th Cir.1989) (upholding the exclusion of a settlement offer to a former employee made after the employee's termination and after he had retained legal counsel, but prior to the employee's filing his claim). In addition, although Rule 408 applies where an actual dispute exists, an apparent difference of opinion between the parties as to the validity of a claim is enough to call the Rule into play. *Alpex Computer Corp. v. Nintendo Co.,* 770 F.Supp. 161, 163-65 (S.D.N.Y.1991) (citing, *Dallis v. Aetna Life Ins. Co.,* 768 F.2d 1303, 1307 (11th Cir.1985); 2 J. Weinstein and M. Berger, *Weinstein's Evidence,* ¶ 408[01] at 408-10 (1990)).

For the reasons stated below, we find that at the time Rowe made the statements at issue, an adversarial relationship existed between the parties that can be deemed an actual dispute. On this basis, we conclude that Rule 408 prohibits the statements' admission into evidence.

B. *The Hartford Letter and the Rowe Statement*

At the time of the fire on April 15, 1989, the Rowe gallery contained art belonging to Rowe and contained art it had received on consignment from other individuals, including art created by Warren Davis, now deceased, and owned by Joardis Davis. Prior to the Davis consignment, Rowe had secured business interruption insurance and insurance covering furniture and fixtures from Hartford. Harold M. Rowe also had insurance from Hartford that would cover his and his wife's personal property located in the gallery. After executing the consignment agreement with Davis, the Rowe Company secured an additional $250,000 of fine arts insurance from Lloyds.

On May 24, 1989, Rowe's counsel gave formal notice to Hartford of its claim under the business interruption insurance. The business interruption insurance covered losses incurred by Rowe equal to its net income for a year after the fire. The business interruption insurance policy did not include any recovery limitations based upon Rowe's prior operating history. Thus, Rowe indicated to Hartford that it intended to include in its claim projected sales from art collections from which it had never sold art prior to the fire. These projected sales would include future sales from the Davis art collection, which was a collection from which Rowe had never sold art prior to the fire.

***3** Hartford responded to Rowe's assertion by hiring counsel and an accounting firm. Hartford made it clear that it would oppose any Rowe claim that included projected sales and that did not stem from historical experience. Counsel for Rowe responded by sending a letter to Hartford on October 20, 1989 ("the Hartford letter"). In the letter, Harold M. Rowe stated that "the value of the collection was $4,635,000." According to Rowe, the purpose of this letter was to convince Hartford that the Rowe Company could have sold some art in the year after the fire from art collections from which it had never sold previously. Rowe suggests that it was attempting to settle the business interruption claim without suit.

After sending the Hartford letter, Rowe and its counsel participated in meetings and telephone negotiations with an adjuster and an attorney for Hartford. During the course of these discussions, Hartford's attorney requested that Rowe provide a sworn statement ("the Rowe statement") in connection with the projected sales figures earlier given to Hartford. Rowe did provide such a statement under oath.

Notwithstanding these efforts, the parties could not reach an agreement over the interpretation of the business interruption policy. Hartford continued to take the position that the Davis art had no value prior to its consignment and could not have been sold or promoted successfully. Suit was filed, and Rowe and Hartford settled, "primarily on the basis of the Rowe Company's actual sales prior to the fire."

Davis asks this Court to admit the Hartford letter and Rowe statement into evidence. Davis argues that the letter and statement were made solely for the purpose of supporting Rowe's claim under the business interruption insurance policy. Under the terms of the policy, the insured, that is Rowe, possessed a duty in case of loss to prepare an inventory of damaged property and to submit a signed, sworn statement of loss incurred. According to the policy, fulfilling these duties was a condition precedent to filing suit. Hence, Davis argues that the Hartford letter and the Rowe statement were not documents or statements made during a negotiation effort, and thus excludable under Rule 408, but rather, were made as a *pro forma* step in asserting a claim under the policy. Davis argues that the Hartford letter was not made in an effort to compromise a disputed claim, but rather was made to fulfill the terms of the policy that required such information from a claimant in order to process a claim for insurance benefits. According to Davis, no actual dispute arose concerning the amount of benefits payable under the policy until this information was provided and considered by the insurer.

We reject Davis' contention. The relationship between a claimant and its insurer is inherently adversarial and can generally be assumed to be clothed in continual negotiation and conciliation efforts. When Rowe realized that it would be disallowed from including projected sales figures into its claim under the business interruption insurance, an actual dispute arose between Rowe and Hartford to which Rule 408 applied. It was at that time that Hartford engaged counsel and an accounting firm to defend its position that the claim's parameters would be set by prior operating history only. Moreover, Rowe claims that in the Hartford letter and the Rowe statement, it was providing Hartford with projected sales figures, that is, what the art could have been worth in light of Rowe's sales and promotional efforts. Without the inflation caused by Rowe's sales and promotional efforts, Rowe contends that the valuation of the Davis art is much lower. We conclude that Rule 408 precludes the admission of the Hartford letter because it was prepared as part of a negotiation effort. Davis' motion in limine is therefore granted.

C. *The Davis Letter*

***4** After the fire on April 15, 1989, Rowe communicated with all persons who had art in the gallery at the time of the fire. Rowe had numerous discussions with the plaintiff.

Rowe describes what followed next in this way. According to Rowe, during the phone conversations, Davis demanded payment of the entire $250,000 of insurance provided under the consignment agreement, and also discussed strategies whereby she and Rowe could claim additional amounts for the Davis art from those responsible for causing the fire. Rowe contends that it never agreed that Davis was contractually entitled to the $250,000, and in any event was unwilling to make any payment to Davis without a full release from liability. On May 31, 1991, Rowe prepared a letter ("the Davis letter"), which Rowe deems a settlement proposal. The draft proposed to meet plaintiff's demand in exchange for a complete release of the defendants from any further liability.

The draft included what Rowe claims was a self-serving recital, that the Davis art in the gallery at the time of the fire was worth more than the $250,000 of insurance agreed upon in the consignment contract. It said, "The total value of the art library and the works of art destroyed in the Rowe Company Gallery far exceeded the insurance coverage." This was followed by an offer to pay Davis $210,000 (the $250,000 amount less $40,000 advanced to Davis earlier). Davis seeks to admit this statement into evidence.

The draft sent to Davis was not signed by the defendants. It was delivered to Davis in June of 1989. Davis' attorney contacted defendants' counsel directly on June 27, 1989. Thereafter, several revised settlement proposals were exchanged between the attorneys. The parties signed none of these proposals.

Davis contends that, until the May 19, 1989 letter was sent to her indicating that the amount of Davis' loss "far exceeded the insurance proceeds," she had not threatened litigation. She therefore concludes that the letter was sent prior to the existence of an actual dispute between the parties. She claims that she was merely seeking the insurance proceeds that both parties agreed were payable under the consignment agreement. Only later did she retain a lawyer to obtain insurance proceeds she believed were due to her.

We again must reject Davis' contentions. Davis claims that prior to the Davis letter she was merely seeking the insurance proceeds that both parties agreed were payable under the consignment agreement. Although both parties may have agreed that Davis was owed some amount under the agreement, the parties were not in agreement over the exact amount owed at the time the Davis letter was sent, and indeed, are still in dispute over that issue. We determine that this request for a release from liability in exchange for a payment of $250,000 was a negotiation effort. In the Davis letter, Rowe did not say we agree that we owe you $250,000, but said that we "agree to make payment to you of" the $250,000. There is a subtle distinction. Rowe did not recognize that it was responsible for that liability, but merely offered to pay that amount in exchange for a release. After the Davis letter, Davis wrote two letters further demanding that the insurance proceeds payable under the consignment agreement be paid to her. The amount demanded by Davis was never paid, and we subsequently held that the amount owed to Davis depends upon the value of the art, a question that is to be determined by the finder of fact at trial. Because we believe that the Davis letter was written in an effort to settle an actual dispute, we decline to admit it in evidence.

D. *Use of the Evidence for Purposes Other Than to Prove the Claim*

***5** Rule 408 provides that exclusion of evidence is not required when the evidence is offered for a purpose other than to prove a claim amount, such as proving bias or prejudice of a witness...." Davis argues that Rowe's "receipt of insurance proceeds from Hartford Insurance in the case at bar in an amount in excess of the $250,000 insurance coverage agreed upon in the consignment agreement, and their subsequent failure to pay all of such proceeds renders Harold Rowe's expected testimony at trial concerning the value of the destroyed Warren Davis art works to be far less credible than it may otherwise appear to a jury." Davis suggests that Harold Rowe's testimony will be biased, and that the statements need to be admitted to establish this bias.

Davis' argument is off the mark. Because Harold Rowe is a defendant and is the president of the corporate defendant to the suit, he will not be testifying as a disinterested witness; his bias will be assumed. Hence, Davis need not introduce Rowe's statements to illustrate his bias. Furthermore, Davis may not use the statements to impeach Rowe. Inconsistent conduct or statements made in connection with compromise negotiations may not be used for impeachment purposes. E.E.O.C., 948 F.2d at 1545 (citing, M. Graham, *Federal Rules of Evidence* 116 (2d ed. 1987)).

Davis additionally argues that this Court must admit the Hartford letter as evidence to show Rowe's intent to defraud and convert the insurance proceeds. This argument is unfounded. The value of the art, and thus, the amount of money that Rowe owes Davis for it, is the factual question central to the claims in this dispute. We held above that Rowe's statements are inadmissible to help prove the amount of Rowe's liability to Davis. Davis attempts to subvert our holding and the policies of Rule 408 by introducing the Hartford letter under the guise of proving claims of fraud and conversion, both of which depend upon the outcome of the factfinder's determination regarding the value of the art. We therefore reject Davis' argument that the evidence should be admitted to prove her claims of fraud and conversion. In doing so, we abide by the admonition of the Tenth Circuit in *Bradbury v. Phillips Petroleum Co.* According to the *Bradbury* court, "when the issue is doubtful, the better practice is to exclude evidence of compromises or compromise offers." Bradbury v. Phillips Petroleum Co., 815 F.2d 1356, 1364 (10th Cir.1987).

To summarize, based on the facts as presented by the parties, we decline to admit either the Hartford letter, the Rowe statement, or the Davis letter into evidence. We find that the statements were made in the midst of settlement negotiations, and that admission for other purposes poses too great a risk that the evidence will be used by the fact finder in evaluating the value of the art.

The Second Motion in Limine: Amount of Insurance Received

Rowe also seeks to exclude evidence of any insurance claimed or collected by it, other than the $250,000 of insurance specified in the consignment contract. Davis responds that this information should be allowed because "[m]ost of those funds were received *only* because defendant was in possession of the plaintiff's artwork." Davis again argues that evidence of the existence of these insurance proceeds is necessary in proving her claims of fraud and conversion of those same proceeds.

***6** Unless events suggest otherwise at trial, we shall exclude all evidence of Rowe's receipt of insurance proceeds beyond the $250,000. This evidence is irrelevant to the question of the value of the Davis art. It is this question upon which the success of Davis' claims under the consignment agreement and under the Illinois Consignment of Art Act rests. Although this evidence would be relevant to claims for fraud or conversion should these claims be of merit, we hold that allowing such evidence would mislead the jury in their determination of the value of the Davis art and, thus, may be excluded under Federal Rule of Civil Procedure 403.

The Third Motion in Limine: Use of Funds Received

Rowe also asks this Court to refuse to admit evidence illustrating how Rowe used the insurance funds it received, in ways other than making payments to Davis. For example, Davis seeks to tell the jury about babysitting and hairdresser expenses paid with the proceeds of the insurance funds. Davis contends that evidence of Rowe's use of the funds should be admitted because the contract compelled the insurance to be paid over to Davis. Moreover, Davis portrays Rowe as a trustee for the funds that are owed to her and suggests that Rowe's use of the funds for purposes other than for payment to Davis violated that trust arrangement.

The Illinois Consignment of Art Act says that works of fine art received by art dealers are held in trust for the owners. The art dealer is trustee for the benefit of the artist until the work of fine art is sold to a bona fide purchaser or is returned to the artist. Ill.Ann.Stat. ch. 121 1/2 , para. 1402(3) (Smith-Hurd Supp.1992). The proceeds of the sale of a work of fine art are trust property and the art dealer is trustee for the benefit of the artist until the amount due the artist from the sale is paid in full. Ill.Ann.Stat. ch. 121 1/2 , para. 1402(4). We have not been asked to decide and shall not decide in the present motion to what extent Rowe possessed a duty to maintain insurance proceeds that it received due to the destruction of art which it held in trust, in particular, in a case where the question of the value of the art so held is in contention. We do hold, however, that until the value of the art is determined by the fact finder at trial, we shall not admit evidence of how Rowe used funds it received as a result of the fire. This information would be prejudicial and is therefore excludable under Rule 403.

Fourth Motion in Limine: Testimony of Kenneth Cone

Rowe argues that Davis' proposed witness Kenneth Cone should not be allowed to testify. According to Rowe, Kenneth Cone is merely an economist, and he has no knowledge or familiarity with art. He allegedly intends to apply the Consumer Price Index and Sotheby's Index of Contemporary American Art to 19 pieces of Davis art. Rowe points to a myriad of evidentiary problems with Cone's use of these two indices.

We decline to exclude Cone's testimony at this juncture of the litigation. At trial, we of course, shall demand compliance with Federal Rule of Civil Procedure 703. If we deem Cone's testimony admissible after a proper showing, Rowe will be allowed to cross examine Cone in order to expose the purported weakness in his testimony. Accordingly, Rowe's motion in limine as to this evidence is denied.

Fifth Motion in Limine: Testimony of Linda Durham

***7** Rowe asks the Court to exclude the testimony of

Linda Durham, an expert witness who will testify as to the value of the Davis art. Rowe contends that Durham has changed the basis of her opinion in this case from that previously stated during her deposition and requests that we exclude any testimony different from that previously testified to in her deposition.

Davis responds by arguing that Durham has not changed the basis of her opinion as set forth in the deposition. She has completed a piece by piece appraisal of the artwork based upon photos, her knowledge of the artwork, and on other information previously set forth in her answer to Rowe's interrogatory. Durham's appraisal was prepared at Davis' request, and Davis asserts that the final appraisal report will be sent to Rowe's counsel as soon as it is completed.

We decline to decide at this time whether testimony not given by Durham in her deposition will be excluded at trial. Because Davis contends that she shall provide Rowe with additional information obtained from Durham in accordance with Federal Rule of Civil Procedure 26(e)(2), we feel that it would be better to hold off on our determination. Moreover, we choose not to make such a decision based solely on a page or two of written argument, and instead, shall hear from the parties in person on this issue.

Sixth Motion in Limine: Davis' Income Tax Returns

Rowe complains that Davis has not furnished copies of her income tax returns and has failed to sign IRS forms allowing Rowe to obtain copies of the returns. Rowe argues that Davis should not be allowed to proceed with this action until her income tax returns are furnished.

According to Davis, the forms requesting copies of the returns from the IRS are being forwarded to Rowe. Therefore, unless we are otherwise advised, there seems to be no remaining basis for Rowe's request, and we deny Rowe's motion as to this matter.

CONCLUSION

For the reasons stated above, Rowe's first, second, and third motions in limine are granted and Rowe's fourth, fifth, and sixth motions in limine are denied.

FN1. Although in our Memorandum Opinion, we commented in *dictum* that this statement could later be used by Davis to prove the value of the art, we now decline to allow this statement into evidence. Upon further consideration of the policies behind Rule 408 and the context within which this statement was offered, we find this statement inadmissible.

FN2. Rule 408 of the Federal Rules of Civil Procedure provides the following:

> Evidence of (1) furnishing or offering or promising to furnish, or (2) accepting or offering or promising to accept, a valuable consideration in compromising or attempting to compromise a claim which was disputed as to either validity or amount, is not admissible to prove liability for or invalidity of the claim or its amount. Evidence of conduct or statements made in compromise negotiations is likewise not admissible. This rule does not require the exclusion of any evidence otherwise discoverable merely because it is presented in the course of compromise negotiations. This rule also does not require exclusion when the evidence is offered for another purpose, such as proving bias or prejudice of a witness, negativing a contention of undue delay, or proving an effort to obstruct a criminal investigation or prosecution.

N.D.Ill.,1993.
Davis v. Rowe
Not Reported in F.Supp., 1993 WL 34867 (N.D.Ill.)

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Exhibit 8

HOnly the Westlaw citation is currently available.

United States District Court, N.D. Illinois, Eastern Division.

Jane DOE, a Minor, By and Through her Guardians and Next Friends, G.S. and M.S., Plaintiffs,
v.
TAG, INC., n/k/a Childserv, Susan Clement, and Robin and David Swaziek, Defendants.

No. 92 C 7661.

Dec. 14, 1993.

MEMORANDUM OPINION AND ORDER

CONLON, District Judge.

*1 Jane Doe, through her guardians and next friends G.S. and M.S. (collectively "the plaintiffs"), sues Tag/ChildServ ("Tag"), Susan Clement ("Clement"), a Tag supervisor, and Robin and David Swaziek, Doe's former foster parents ("the Swazieks"), for placing and keeping Doe in a foster home in which she allegedly suffered severe physical and psychological abuse.[FN1] The plaintiffs and defendants moved *in limine* to exclude evidence. Tag and Clement move for reconsideration of some of the court's rulings.

DISCUSSION

1. Motion For Reconsideration

A motion for reconsideration serves a limited purpose. The court's rulings "are not intended as first drafts, subject to revision and reconsideration at a litigant's pleasure." *Quaker Alloy Casting v. Gulfco Industries, Inc.,* 123 F.R.D. 282, 288 (N.D.Ill.1988). Nevertheless, a motion for reconsideration may be proper to correct manifest errors of law or to present newly discovered evidence. *See* *Publishers Resource, Inc. v. Walker-Davis Publications, Inc.,* 762 F.2d 557, 561 (7th Cir.1985); *Lewis v. Hermann,* 783 F.Supp. 1131, 1132 (N.D.Ill.1991). Although a motion for reconsideration is not a vehicle for introducing new evidence or legal theories that could have been introduced prior to the earlier ruling, it may be appropriate when "the Court has patently misunderstood a party ... or has made an error not of reasoning but of apprehension." *Bank of Waunakee v. Rochester Cheese Sales, Inc.,* 906 F.2d 1185, 1191 (7th Cir.1990).

2. Evidence Regarding James C.

Tag moved to exclude evidence regarding James C., another foster child who was placed in the Swazieks' home. In denying Tag's motion *in limine,* the court found that evidence regarding James C. was relevant to this case and was not "substantially outweighed by the danger of unfair prejudice" to the defendants. *See*Fed.R.Evid. 403; Memorandum Opinion and Order, No. 92 C 7661 (N.D.Ill. Nov. 16, 1993) at 7-8.[FN2] The court noted that evidence is excluded on a motion *in limine* only if it clearly is not admissible for any purpose. *See* *Hawthorne Partners v. AT & T Technologies, Inc.,* 831 F.Supp. 1398, 1400 (N.D.Ill.1993). The court recognized one possible purpose for introducing evidence regarding James C.-proving Tag's negligence in placing Doe with the Swazieks.

On reconsideration, Tag contends that the court's reasoning was exclusive. Tag understands the court's ruling to mean that evidence regarding James C. may be introduced only for the limited purpose of proving Tag's negligence in placing Doe with the Swazieks. Tag argues that because Doe was placed with the Swazieks prior to James C.'s placement,[FN3] evidence regarding James C. is irrelevant and must be excluded.

Tag misconstrues the court's ruling, as well as the purpose of a motion *in limine.* By recognizing one possible purpose for introducing evidence regarding James C., the court was not limiting the introduction of the evidence to one purpose, but was demonstrating that the evidence is not clearly inadmissible. After noting that there is at least one legitimate purpose for the introduction of evidence regarding James C., the court deferred ruling until trial-where questions of foundation, relevancy, and potential prejudice can be resolved in their proper context. *See The Middleby Corp. v. Hussman Corp.,* 1993 WL 15129 *1 (N.D.Ill. May 5, 1993). Although James C. was placed with the Swazieks after Doe, it still may be possible to establish Tag's negligence for not removing Doe from the Swazieks' earlier. Because the evidence is not clearly inadmissible, the court's earlier ruling will not be disturbed on reconsideration.

3. Expert Testimony

***2** Clement moved to exclude expert testimony concerning Doe's current medical condition and future mental state. In denying Clement's motion, the court noted that the plaintiffs had informed the defendants that their experts would testify about Doe's current and future medical condition. The court also rejected Clement's contention that the plaintiffs' experts would be testifying on mere surmise or conjecture. *See* Memorandum Opinion and Order, No. 92 C 7661 (N.D.Ill. Nov. 16, 1993) at 2-4. In moving to exclude the expert testimony, Clement contended that the plaintiffs never disclosed that their experts would testify concerning Doe's current or future medical needs. On reconsideration, Clement concedes that the plaintiffs did notify the defendants of the content of their expert testimony, but argues that the notice was late. After contending in her motion *in limine* that the plaintiffs never disclosed the content of their expert testimony, Clement cannot raise on reconsideration the new argument that the disclosure came after the discovery cutoff date. *See* *Lewis v. Hermann,* 783 F.Supp. 1131, 1132 (N.D.Ill.1991) (party may not raise new argument on reconsideration that could have been raised in earlier proceeding).[FN4]

Clement contends that the plaintiffs' experts are not qualified to render expert opinions. The court has ruled that the experts are qualified to offer expert opinions "based on their clinical experience in addition to their work with Doe." Memorandum Opinion and Order, No. 92 C. 7661 (N.D.Ill. Nov. 16, 1993) at 3. On reconsideration, Clement cites apparent admissions that the experts are not qualified, and asserts that the plaintiffs' experts have no basis upon which to render expert opinions regarding Doe's current or future condition. However, Clement fails to note that the quoted statements were made in June and July. In the past four months the experts have been able to acquaint themselves with the case more fully through a review of Doe's files. There is no question that the experts are qualified to testify on Doe's current or future condition based on their clinical experience. The court's ruling that the plaintiffs' experts are qualified is sound, and will not be disturbed.

4. Prior Abuse In The Swaziek Household

Clement moved to exclude evidence that Robin Swaziek and Christie Stimpson were abused by a family member who did not live with the Swazieks. The court denied Clement's motion *in limine* because her arguments were conclusory, and she failed to meet the burden of showing that the evidence was inadmissible for any purpose. Memorandum Opinion and Order, No. 92 C 7661 (N.D.Ill. Nov. 16, 1993) at 4-5. The court noted that "it is not clear exactly what evidence Clement seeks to exclude." *Id.* at 5 n. 4.

Clement seeks a modification of the court's ruling so as to prohibit the plaintiffs from alluding to alleged abuse sustained by Robin Swaziek and Christie Stimpson in their opening statement. Clement is concerned that any allusion to other abuse in the Swaziek home "without a proper foundation risks poisoning the jury with potentially irrelevant, inflammatory and prejudicial comments." Motion at 2. Clement's motion is identical to her motion *in limine.* Clement once again makes conclusory statements without identifying the evidence she wishes to exclude. She fails to demonstrate why evidence of other abuse is unfairly prejudicial or even what that evidence is. Nevertheless, Clement correctly notes that such unproven allegations may be highly inflammatory, and may prejudice the jury if they are presented in the opening statement. Clement's motion for modification is granted. The plaintiffs may not allude to other alleged abuse in the Swaziek household in their opening statement.

CONCLUSION

***3** Defendant Tag/ChildServ's motion for reconsideration and defendant Susan Clement's motion for reconsideration are denied; defendant Susan Clement's motion for modification is granted.

FN1. The complaint named the Illinois Department of Child and Family Services ("DCFS"), and caseworkers and administrators of the DCFS. These defendants have been dismissed from this action. *See* Memorandum Opinion and Order, No. 92 C 7661 (N.D.Ill. Feb. 23, 1993); Memorandum Opinion and Order, No. 92 C 7661 (N.D.Ill. Oct. 18, 1993).

FN2. It is worth noting that Tag, the moving party, is not the defendant in danger of being unfairly prejudiced by the introduction of the evidence regarding James C.

FN3. The court was led to understand that James C. had been placed with the Swazieks before Doe because the sequence of events was not well-delineated in Tag's motion.

FN4. Clement's position is further undermined by the fact that the plaintiffs disclosed the content of their experts' testimony of August 16, yet the defendants never moved to reopen discovery.

N.D.Ill.,1993.
Doe By and Through G.S. v. Tag, Inc.
Not Reported in F.Supp., 1993 WL 524773 (N.D.Ill.)

END OF DOCUMENT

Exhibit 9

Only the Westlaw citation is currently available.
United States District Court, District of Columbia.
Allison Lee HAIRSTON, Plaintiff,
v.
WASHINGTON METROPOLITAN AREA TRANSIT AUTHORITY ("WMATA"), Defendant.
No. Civ. 93-2127.

April 10, 1997.

Scott William Muller, Catherine M. O'Neil, J. Bradford Gatehouse, Suzanne E. Wachsstock, Davis, Polk, & Wardwell, Washington, DC, Linda Chatman Thomsen, U.S. Securities & Exchange Commission, Washington, DC, Amy J. St. Eve, United States Attorney's Office, Chicago, IL, Allison Lee Hairston, Plaintiff.
Jacquelyne A. Wiley, Washington, DC, Jeanette J. Clark, Washington, DC, Elicia Tamara Pegues, Federal Bureau of Investigation, Washington, DC, Washington Metropolitan Area Transit Authority, Defendant.

MEMORANDUM OPINION

THOMAS F. HOGAN, District Judge.
*1 Pending before the Court are three motions in limine: plaintiff's motion in limine regarding other acts of discrimination and retaliation filed March 20, 1997, plaintiff's second motion in limine to exclude an EEOC determination filed April 1, 1997, and defendant's motion in limine filed April 1, 1997. For the reasons set forth below, the Court will grant plaintiff's motion in limine regarding other acts of discrimination and retaliation [93], grant plaintiff's motion in limine to exclude an EEOC determination [96], and grant in part and deny in part defendant's motion in limine [97]. Because there is a substantial overlap of issues among the three motions, the Court will frame its discussion around the four issues rather than consider each motion separately. Those issues are (1) the admissibility of the opinions issued in *Townsend v. WMATA* and *Jones v. WMATA;* (2) the admissibility of the EEOC determination letter regarding Mrs. Hairston's charge; (3) the admissibility of third-party testimony regarding other acts of discrimination or retaliation; and (4) the admissibility of evidence regarding Mrs. Hairston's prior grievances with WMATA.

(1) The Townsend and Jones Opinions

WMATA challenges the admissibility of plaintiff's exhibits 29 and 142, which are opinions in *Townsend v. WMATA,* 746 F.Supp. 178 (D.D.C.1990) and *Jones v. WMATA,* 946 F.Supp. 1011 (D.D.C.1996) where individual defendants, some of whom were involved in actions at issue in this case, were found to be liable for sexual harassment, retaliation, or other forms of discrimination.

WMATA cites Judge Harris' opinion in *Taylor v. WMATA,* 922 F.Supp. 665 (D.D.C.1996) in which Judge Harris granted WMATA's motion to strike the plaintiff's attempt to introduce the *Jones* and *Townsend* opinions. Judge Harris held that the fact of the existence of the other cases might be admissible, but any findings of fact issued by those cases were hearsay and not covered by any hearsay exception.

In *Taylor,* Judge Harris relied on *Nipper v. Snipes,* 7 F.3d 415 (4th Cir.1993) and *United States v. Jones,* 29 F.3d 1549 (11th Cir.1994). Neither case was a Title VII case, but both confronted the issue of the admissibility of judicial findings of fact from prior cases. In *Nipper,* a district court had allowed plaintiff's counsel to introduce into evidence an order entered in a state court case involving some of the same parties in the case before it under the Rule 803(8)(C) exception to the hearsay rule for public records or reports. *Nipper,* 7 F.3d at 417. The order included the state court judge's findings of fact, portions of which were read to the jury. *Id.* at 416. The Fourth Circuit concluded that judicial findings of fact in a court's order are not admissible in another case under Rule 803(8)(C). *Id.* at 418. The court found that the exception was not meant to cover judicial findings of fact. *Id.* at 417.

*2 The Eleventh Circuit, in *United States v. Jones,* reached the same conclusion. The court found that "the plain language of Rule 803(8)(C) does not apply to judicial findings of fact. It applies to 'factual findings resulting from an investigation made pursuant to authority granted by law.%7 D " 29 F.3d at 1554 (citing Fed.R.Evid. 803(8)(C)). According to the court, "a review of the advisory committee note to Rule 803 reveals that the drafters intended this portion of the rule to apply to findings of agencies and offices of the executive branch" rather than to judicial findings. *Id.*

In addition to the failure of such evidence under Fed.R.Evid. 803(8)(C), in *Nipper* the court noted that such evidence should also be excluded under Fed.R.Evid. 403, because "judicial findings of fact 'present a rare case where, by virtue of their having been made by a judge, they would likely be given undue weight by the jury, thus creating a serious danger of unfair prejudice.'"*Id.* at 418 (citing *Zenith Radio Corp. v. Matsushita Elec. Indus. Co.*, 505 F.Supp. 1125, 1186 (E.D.Pa.1980)).

In contrast to Judge Harris' opinion and the opinions in *Nipper* and *United States v. Jones* is a recent opinion by Judge Lamberth in which the court found that the *Townsend* opinion was admissible under the residual hearsay exception, Fed.R.Evid. 803(24). *Jones v. WMATA*, 946 F.Supp. 1011 (D.D.C.1996). Judge Lamberth found that the evidence (1) had circumstantial guarantees of trustworthiness, (2) was offered on a material fact, and (3) the evidence was more probative on the point for which it was offered than other reasonably available evidence. *Id.* at 1019. In addition, Judge Lamberth found that defendant had had adequate pre-trial notice of the plaintiff's intent to use the prior opinions as required by Fed.R.Evid. 803(24). *Id.*

The Court is persuaded by the Eleventh and Fourth Circuits as well as Judge Harris' opinion in *Taylor.* Therefore, the Court finds that judicial findings of fact are hearsay, and not covered by the Rule 803(8)(C) public records or reports exception to the hearsay rule. In addition, this evidence must be excluded under Fed.R.Evid. 403, because its probative value is substantially outweighed by the danger of unfair prejudice. As the court in *Nipper* explained, it is likely that judicial findings of fact would be given undue weight by a jury which would result in a serious danger of unfair prejudice to the defendant. For these reasons, therefore, the Court will not permit the findings of fact from prior cases against the defendant to be used as evidence in this case.[FN1]

> FN1. Because the Court finds the evidence inadmissible under Fed.R.Evid. 403, the Court need not decide whether or not judicial findings of fact may qualify for the residual hearsay exception, Fed . R.Evid. 803(24), as held by Judge Lamberth in *Jones v. WMATA*, 946 F.Supp. 1011 (D.D.C.1996).

(2) The EEOC Determination

Plaintiff's second motion in limine addresses the admissibility of the EEOC determination letter dated July 21, 1993, which states that "[t]he preponderance of the evidence gathered in EEOC's investigation" did not "prove" Mrs. Hairston's claim that she was retaliated against when dismissed from her position as a Planner/Estimator. A copy of the letter is attached as Exhibit A to plaintiff's second motion in limine. It is entitled "DETERMINATION," and is described within the letter as a "determination on the merits of the subject charge."The letter contains only the allegations of each party and the conclusion of the EEOC officer. No evidence is discussed, nor is there any indication about the type of investigation that the EEOC performed with respect to Mrs. Hairston's complaint. Plaintiff argues that the potential prejudice substantially outweighs any probative value in the letter's admission, and, therefore, the determination letter should be excluded pursuant to Fed.R.Evid. 403. The defendant, of course, argues that the letter's substantial probative value is not substantially outweighed by the danger of unfair prejudice.

***3** As a preliminary comment, it should be noted that the Supreme Court has found that similar administrative findings fit within the hearsay exception for public records and reports, Rule 803(8)(C). *Chandler v. Roudebush*, 425 U.S. 840, 96 S.Ct. 1949, 48 L.Ed.2d 416 (1976) (holding that administrative findings with respect to claims of racial discrimination fit within Fed.R.Evid. 803(8)(C)). However, the decision of whether or not to admit the EEOC letter in this case is within the Court's discretion.

The lone case from this jurisdiction on this subject is *Kinsey v. Legg, Mason and Company, Inc.*, 1974 WL 275 (D.D.C.1974), in which Judge Gasch held that the admission of a final EEOC report lies within the discretion of the trial judge. After reviewing the final investigative report in *Kinsey,* Judge Gasch admitted it into evidence in the Title VII bench trial, but explained that it would only be given "such weight as the Court deems appropriate upon review of all the testimony and evidence presented in this trial."*Id.* at *2.

Most courts have held, as Judge Gasch did in *Kinsey*, that the decision regarding the admissibility of an EEOC letter is within the discretion of the trial court. For example, in *Johnson v. Yellow Freight System, Inc.*, 734 F.2d 1304 (8th Cir.1984), the Eighth Circuit held that the trial court did not abuse its discretion by admitting an EEOC letter in the Title VII bench portion of a trial while excluding it from the jury in the section 1981 portion of the trial. The letter stated that there was "reason to believe" that the plaintiff had been discriminated against, and, the plaintiff, understandable, wanted the jury to see that letter. *Id.* at 1308-09. The court rejected a per se rule of admissability explaining that "EEOC determinations are not homogeneous products; they vary greatly in quality and factual detail." *Id.* at 1309. Because of this, the court found that "[t]he trial judge correctly may perceive a danger of unfair prejudice to the defendant or properly may consider that time spent by the defendant in exposing the weaknesses of the EEOC report would add unduly to the length of the trial."*Id.* In addition, the court concluded that "[b]ecause substantial evidence was presented to the jury on all matters summarized in the report, there was little probative value in the EEOC's conclusory statements regarding the same evidence."*Id.See also* *Walker v. Nationsbank of Florida*, 53 F.3d 1548 (11th Cir.1995) (finding no abuse of discretion in trial court's decision to exclude two conflicting EEOC determinations due to the danger of confusion), *Hall v. United States*, 988 F.2d 1050 (10th Cir.1993) (finding no abuse of discretion where trial court determined that since "the only purpose to be served by admitting into evidence the ... report would be to suggest to the jury that it should reach the same conclusion, ... the risk of unfair prejudice to the plaintiff substantially outweighs any relevance" of the letter) (citation omitted); *Barfield v. Orange County*, 911 F.2d 644 (11th Cir.1990) (finding no abuse of discretion in trial court's decision to admit EEOC no reasonable cause letter where plaintiff's arguments under Rule 403 were not specific).

*4 In contrast to the cases discussed above, the Ninth Circuit has a rule of per se admissibility regarding EEOC probable cause determinations. *See Plummer v. Western International Hotels Company, Inc.*, 656 F.2d 502 (9th Cir.1981) (holding that a plaintiff has a right to introduce an EEOC probable cause determination in a Title VII lawsuit, regardless of whether it is tried to judge or jury). However, the Ninth Circuit recognizes a distinction between EEOC probable cause determinations and EEOC letters of violation. The first are per se admissible, but the admissibility of EEOC letters of violation is discretionary due to the potential for prejudice. *Heyne v. Caruso*, 69 F.3d (9th Cir.1995) (explaining that there is a significant difference between a letter of violation and a probable cause determination, because a probable cause determination does not suggest to the jury that the EEOC has already determined that there has been a violation).

Based on the above cases, it is clear that the decision whether or not to admit the EEOC determination in this case is discretionary. The letter in question in this case is more than a probable cause determination. Instead, it states that "[t]he preponderance of the evidence gathered in EEOC's investigation" did not "prove" Mrs. Hairston's claim that she was retaliated against when dismissed from her position as a Planner/Estimator, and the letter itself is described as a "determination on the merits of the subject charge."Therefore, it's likely that even the Ninth Circuit would find that this decision is discretionary.

Based on the Rule 403 balancing test, the Court concludes that any probative value of this evidence is substantially outweighed by the danger of unfair prejudice and waste of time. The letter itself discusses no facts about the case other than the conflicting allegations. Instead, it merely provides a legal conclusion. For these reasons, the Court finds that the letter has very little probative value. In contrast, the danger of unfair prejudice is high. Within the body of the letter is the assertion that the letter is a "determination on the merits of the charge."This statement, the legal conclusion which follows, and the fact that the letter comes from the EEOC all combine to create unfair prejudice for the plaintiff. Additionally, if the letter were to be offered in evidence, it is likely that the plaintiff would have to spend additional time at trial attempting to explain what this letter means as well as its significance to the jury. For these reasons, the Court finds that the low probative value of the letter is substantially outweighed by the danger of unfair prejudice and waste of time. Defendant will not be permitted to offer the EEOC letter to the jury as evidence in this case.

(3) Other Acts of Discrimination

The admissibility of alleged "other acts" of discrimination are the subject of the plaintiff's first motion in limine as well as the defendant's motion in limine. Plaintiff seeks a pre-trial determination that such evidence is admissible. While defendant seeks a pre-trial determination that such evidence is inadmissible and, therefore, plaintiff's witnesses Joseph Taylor, Avon Mackel, and Joan Lewis should not be permitted to testify regarding "other acts" of discrimination or retaliation by the defendant. Defendant objects to the evidence on the grounds that it is irrelevant, non-probative, and prejudicial. Plaintiff argues that evidence of other acts of retaliation or discrimination are admissible to prove the defendant's retaliatory or discriminatory motive or intent pursuant to Fed.R.Evid. 404(b). In addition, plaintiff urges that the evidence survives the Fed.R.Evid. 403 balancing test.

***5** While all courts are not in agreement regarding this issue, the plaintiff's position is the stronger in this circuit based on the decisions in *Morris v. WMATA*, 702 F.2d 1037 (D.C.Cir.1983), *Miller v. Poretsky*, 595 F.2d 780 (D.C.Cir.1978), and *Jones v. WMATA*, 946 F.Supp. 1011 (D.D.C.1996).

In *Morris*, plaintiff alleged that WMATA had terminated him for complaining about racial discrimination on the Authority's police force, in violation of both Title VII and the First Amendment. 702 F.2d at 1039, 1043. At trial, Morris attempted to introduce the testimony of three WMATA police officers in support of his allegation that the Authority engaged in the practice of retaliation against employees who complained about its employment practices. *Id.* at 1046. The district court excluded the testimony of two of the three, because one was to testify regarding retaliation against him for his union activities and another would have testified only to events concerning complaints about sex discrimination and safety matters while plaintiff had allegedly been retaliated against due to his complaints regarding racial discrimination. *Id.* The appellate court found this limitation erroneous for the reason that "evidence showing that the employer followed a broad practice of retaliation and responded to any protected criticism with disciplinary action has some probative value on the issue of the employer's likely motivation here."*Id.* The court followed this by stating that "[e]vidence of other acts may be admitted to show motive, intent, preparation or plan."*Id.* (citing Fed.R.Evid. 404(b)).

The district court had also held that another witness "was not allowed to testify regarding complaints made by other officers or the Authority's response to such complaints." *Id.* at 1047. The D.C. Circuit held that this was also error:

although testimony generally must be based upon personal knowledge, the requisite knowledge can be knowledge of the treatment accorded to others. If a proper foundation was laid that [the witness] had knowledge of other instances in which protected complaints were followed by official discipline-whether such knowledge came from first-hand observation, from records kept in the ordinary course of business, or from some other acceptable source-then he was competent to adduce that evidence.

Id.

Defendant argues that *Morris* is distinguishable because it is a "custom or policy" case [FN2] while the present case is not. However, *Morris* is not limited to "custom and policy" cases. The language of the court makes this clear:

FN2. In order to impose liability on a political subdivision, as distinct from its employees or officials, a section 1983 plaintiff must also show that the unlawful decision was part of a "custom or policy" of unlawful discrimination or retaliation. *See* Morris, 702 F.2d at 1045.

The question of the legitimacy of the employer's motivation in firing the employee ... is one upon which the past acts of the employer have some bearing. They *also* tend to show the existence of a "custom or policy" of unconstitutional acts, necessary to a finding of liability against the authority.... Here the plaintiff must show both that his dismissal was substantially caused by his speech and that this causation was not unique to his case but rather was customary in cases of complaint. The evidence plaintiff sought to adduce of past retaliation by the Authority for complaints from members of the Force was relevant to *both* requirements.

***6** *Id.* at 1405-6 (emphasis added).

Morris was not the first case in which the D.C. Circuit considered the admissibility of evidence of prior discrimination. In *Miller v. Poretsky*, 595 F.2d 780 (D.C.Cir.1978), a housing discrimination suit, the court held that the trial court should have admitted the testimony of other tenants regarding alleged discrimination against them, stating that "it is clear that the proffered evidence of past acts of racial discrimination was relevant to prove the landlord's motive in his actions toward appellant." *Id.* at 784. Judge Robinson's concurrence, which was expressly adopted by the court, *id.* at 785, explained why such evidence generally should be admitted. Judge Robinson found support in *McDonnell Douglas Corp. v. Green*, 411 U.S. 792, 93 S.Ct. 1817, 36 L.Ed.2d 668 (1973), in which the Court stated "[o]ther evidence that may be relevant to any showing of pretext includes facts as to ... [the defendant's] general policy and practice with respect to minorities." *Id.* at 804-5.

Judge Robinson also disposed of the Rule 403 analysis. As to prejudice, Judge Robinson noted that

> the prejudice to which Rule 403 speaks is something utterly different from the capability of the evidence to debilitate the opponent's cause in an entirely legitimate manner.... Though arguable, ... [the] testimony might have engendered some chance that the jury might penalize appellees for discriminating against someone other than appellant, its exclusion could not possibly have been justified in the face of the much more powerful considerations on the other side.... [T]he evidence [in dispute] not only is relevant ... but is the only indication other than the defendant's say-so of what his state of mind might have been when he acted.

Id. at 795. The last part of this statement is particularly important since the advisory committee note to Rule 403 indicates that the availability of other means of proof may be an appropriate factor for the Court to consider under Rule 403. See Fed.R.Evid. 403 Advisory Committee Note. Additionally, according to the advisory committee note, the Court should consider the effectiveness or lack of effectiveness of a limiting instruction. *Id.*

Judge Robinson also addressed the issue of the supposed collateral nature of third party evidence in response to appellees' argument that admission of third party testimony regarding prior acts of discrimination would interject collateral issues likely to confuse or mislead the jury. Judge Robinson concluded that

> under *McDonnell Douglas*, such [third party] evidence is not merely collateral; it is an indispensable element of the plaintiff's burden of proof.... Such evidence does not becloud any issue in this case; rather it directly addresses and sharply defines a key issue, as developed in *McDonnell Douglas* and its progeny.

Id. at 795-96 (citation omitted).

From *Miller* and *Morris* it is clear that a plaintiff may use third party evidence of prior acts of discrimination or retaliation to show the defendant's motive or intent as long as the Court finds that the evidence survives the Rule 403 balancing test in this case. *See also* *Jones v. WMATA*, 946 F.Supp. 1011 (D.D.C.1996) (finding evidence of prior discriminatory acts, as testified to by Avon Mackel, Herbert Anzueto, Joan Lewis, and Joseph Taylor, was relevant to WMATA's motive and intent in Title VII suit alleging retaliation and discrimination based on sex, race and age, and on facts of the case, the danger of unfair prejudice from the evidence did not outweigh its probative value).

***7** In this case, the Court holds that the probative value of the testimony from third-party witnesses regarding prior acts of discrimination or retaliation by the defendant is not substantially outweighed by the danger of unfair prejudice. There is no question that the evidence in question bears a high probative value with respect to the plaintiff's proof of the defendant's motive and intent. It may well be the only evidence available to prove that point. There is also no question that there would be some prejudice to the defendant if the evidence were admitted. Here, however, the probative value is not substantially outweighed by the danger of unfair prejudice. The Court has taken into account the fact that other means of proof of defendant's motive and intent may not be available for the plaintiff. The Court will also give the jury a limiting instruction with respect to this evidence. The evidence will be admitted under Fed.R.Evid. 404(b) for the limited purpose of showing the defendant's motive and intent.

(4) Plaintiff's Prior Grievances

Finally, defendant argues that evidence of plaintiff's prior grievances with WMATA should not be admitted at trial, because the result would be a number of "mini-trials." Defendant fails to provide any supporting case law on this point which demonstrates some indication of the strength of the defendant's argument. Plaintiff correctly argues that plaintiff's history of grievances, and the knowledge of WMATA's agents of this history, is central to her claim of retaliation. The Court finds that it would be improper to exclude evidence of plaintiff's prior grievances with defendant since part of the plaintiff's claim is that she was retaliated against because of her complaints regarding discrimination. Of course, she must be able to show that she, in fact, made prior complaints. The defendant's argument is rejected. Evidence of plaintiff's prior grievances with defendant, and the knowledge of defendant's agents of these complaints, is admissible at trial.

CONCLUSION

For the reasons provided above, the Court will grant plaintiff's motion in limine regarding other acts of discrimination and retaliation [93], grant plaintiff's motion in limine to exclude an EEOC determination [96], and grant in part and deny in part defendant's motion in limine [97]. The Court finds that (1) the judicial findings of fact contained in the opinions issued in *Townsend v. WMATA* and *Jones v. WMATA* are inadmissible; (2) the EEOC determination letter regarding Mrs. Hairston's charge is inadmissible; (3) the third-party testimony regarding other acts of discrimination or retaliation by the defendant is admissible; and (4) evidence regarding Mrs. Hairston's prior grievances with WMATA is admissible.

D.D.C.,1997.
Hairston v. Washington Metropolitan Area Transit Authority
Not Reported in F.Supp., 1997 WL 411946 (D.D.C.)

END OF DOCUMENT

Exhibit 10

C

United States District Court; D. Minnesota Fourth Division.
JAMES ARDITO, DIXIE M. LEEK, FRED H. HAMANN, and DAVID JOHNSON, Plaintiffs,
v.
JOHNSON & JOHNSON, Defendant.
Civil No. 4-81-922.

July 22, 1985.

MICHAEL DWYER, Esq., Mackall, Crounse & Moore, 1600 TCF Tower, Minneapolis, MN 55402, appeared on behalf of plaintiffs.
CHARLES QUAINTANCE, JR., Esq., Maslon, Edelman, Borman, Brand & McNulty, 1800 Midwest Plaza, Minneapolis, MN 55402, appeared on behalf of defendants.

MEMORANDUM OPINION AND ORDER

MURPHY, District Judge.
*1 Plaintiffs James Ardito, Dixie M. Leek, Fred H. Hamann, and David Johnson, brought this action for compensatory and punitive damages against Johnson & Johnson, Inc. (J&J), alleging breach of contract, antitrust violations, fraud, conversion, and tortious interference with contract in J&J's acquisition of Stimulation Technology, Inc. (StimTech). Jurisdiction is alleged under 28 U.S.C. §§ 1332 and 1337, 15 U.S.C. §§ 15 and 26. The matter is now before the court upon the renewal motion of J&J for summary judgment against plaintiff Ardito and Ardito's motion for summary judgment on the issues of breach of contract, causation and whether Ardito is an intended third party beneficiary.[FN1]

Background

The pertinent facts are essentially undisputed. Plaintiff Ardito is a former national sales manager of StimTech, a Minnesota corporation which became a wholly-owned subsidiary of J&J in September 1974. Prior to acquisition, StimTech manufactured and sold heart pacemakers and transcutaneous electrical nerve stimulators (TENS), portable devices which use electricity to stimulate the surface of the skin to relieve chronic pain. Defendant J&J is a New Jersey corporation which, among other things, manufactures and sells pain killing drugs through a wholly-owned subsidiary.

When StimTech was acquired by J&J, Ardito owned certain stock option rights that he apparently received from StimTech in recognition of his contribution to StimTech. Ardito claims that he exercised those option rights in mid-1974 by tendering a certified check to StimTech, but that he did not receive any shares because J&J, in its negotiations with StimTech, desired to buy all of StimTech's stock. In September 1974, when J&J agreed to buy all of the stock, Ardito relinquished his option rights for $14,000 and a five-year contingent profit sharing agreement. The agreement provided that Ardito would receive no profit share until StimTech exceeded specified sales and profit objectives. Ardito's profit share did not depend upon his continued employment, but the agreement contained a clause prohibiting him from competition with StimTech for a specified period of time.

J&J and the StimTech owners negotiated a downpayment for acquisition of the stock, but this downpayment was subsequently reduced by $50,000 when J&J agreed to the profit sharing plan for Ardito and three other employees. Ardito states that this downpayment reduction was the subject of testimony in McDonald v. Johnson & Johnson, 537 F. Supp. 1282 (D. Minn. 1982), aff'd in part, rev'd in part, vacated and remanded, 722 F.2d 1370 (8th Cir. 1983). In McDonald the former StimTech owners sued J&J, alleging the same illegal conduct as is asserted by Ardito here. Ardito claims that Charles Anderson, president of J&J Development Corporation and later Chairman of the Board of StimTech, testified that J&J recognized the profit sharing plans of the four employees as an obligation of StimTech which J&J agreed to assume. He states that Anderson further testified that the four employees were to receive the benefit of J&J's obligation.

*2 From 1975 through 1980, StimTech produced no profits and Ardito received no distributions under the profit sharing agreement.

In 1976, Ardito left StimTech and established Advanced Medical-Systems, Inc. (AMS), a distributor of medical devices including StimTech's TENS unit and pacemaker. In January 1977, Ardito filed a lawsuit against J&J in Hennepin County District Court seeking commissions, consulting fees and travel expenses, Advanced Medical Systems, Inc. v. StimTech, Inc. and Johnson & Johnson, File No. 733626. StimTech responded with a suit of its own charging Ardito with violations of the noncompete clause in his September 20, 1974 profit sharing agreement, StimTech, Inc. v. Ardito, Henn. Co. Dist. Court File No. 734452. StimTech's complaint sought, among other things, that Ardito return the $14,000 he had received from StimTech for his option rights and that the profit sharing agreement be voided.

Settlement negotiations were held, and one offer was made and refused in March 1979. Ardito discharged his attorney, Jerome Korba, in February of 1980, [FN2] and in July of that year he wrote to J&J asking that the litigation be settled. J&J replied by letter, dated August 5, 1980, which basically renewed the March 1979 offer of $4,260.78. This letter specifically advised Ardito that settlement of the cases would have to include J&J's receipt of a 'General Release from both you and Advanced Medical Systems, Inc.' J&J Ex. H.

Ardito agreed to this offer on August 11, 1980, and J&J supplied him with stipulations of dismissal for both cases and a general release. J&J also informed Ardito's attorney of record of the negotiations, although as mentioned above, Ardito had broken off contact with him in February 1980. On September 22, 1980, stipulations of dismissal, signed by Ardito's attorney and by J&J's attorneys, were filed in the Hennepin County District Court terminating both lawsuits. In the meantime, Ardito executed and had notarized a general release. The release refers to terminations of both lawsuits and states that Ardito personally and his company, AMS:

> do hereby remise, release and forever discharge . . . [StimTech and J&J] of and from any and all manner of actions, suits, claims, demands, damages, judgments, levies, and executions, whether known or unknown, fixed or contingent, direct or indirect, at law or in equity, and which the undersigned ever had, has or ever can, shall or may have or claim to have against Releasees . . ..

Ardito signed the release in two places, once in his capacity as President of AMS, and once in his individual capacity. Ardito admits that he signed the Releases. Ardito depo. at 95; J&J ex. R. Of the settlement amount, Ardito received $3,309.56 with the balance, $951.22, going to Korba for services rendered.

Almost one year before Ardito signed this release, in November 1979, he swore to a lengthy affidavit filed in the McDonald v. Johnson & Johnson case. According to this affidavit, Ardito was aware of J&J's alleged representations to the owners of StimTech and sold his shares back to the owners '[i]n reliance upon such representations.'See Ardito aff. at ¶3. Ardito admits signing the affidavit, Ardito depo. at 67, and one of the attorneys for plaintiffs in the McDonald action admits meeting with Ardito and discussing the affidavit before Ardito signed it. Darling depo. at 4-6.

*3 In addition to signing an affidavit, Ardito during this same period of time, asked his attorney, Korba, to investigate whether he had a legal claim against J&J. According to Korba, he and Ardito agreed not to spend time and money investigating until the McDonald suit was further developed. Korba depo. at 33-34, 36, 84-87.

Subsequently, Ardito discharged Korba, settled his litigation with StimTech, and entered into a general release discharging StimTech and its corporate parent, J&J, from all claims. On December 31, 1981, a few months after a very large jury verdict in McDonald v. Johnson & Johnson, Ardito filed this action. Discovery is now complete and J&J has renewed its motion for summary judgment, alleging that Ardito's claims are barred by his execution of the general release. Ardito contends that the release covered only the two Hennepin County lawsuits. He has filed a cross-motion for summary judgment on contract issues and causation, but since the release issue is potentially dispositive, the court will address it first.

Discussion

Minnesota generally favors releases as an efficient means of settling disputes and presumes them to be valid. Schmitt-Norton Ford, Inc. v. Ford Motor Co., 524 F. Supp. 1099, 1102 (D. Minn. 1981), aff'd mem., 685 F.2d 438 (8th Cir. 1982); Jeffries v. Gillitzer, 302 Minn. 402, 225 N.W.2d 17, 20 (1975). A release is only valid, however, if a party has intentionally executed it and received consideration for the party's claim. Couillard v. Charles T. Miller Hospital, Inc., 253 Minn. 418, 92 N.W.2d 96 (1958).

Factors to be considered in determining whether to dismiss a case based on a release, include: 1) whether plaintiff had an opportunity to consult an attorney before and at the time of settlement; 2) the language of the release itself and whether the plaintiff was permitted to change language in the release; 3) evidence of inequitable conduct by the defendant in obtaining the release; 4) evidence of fraud or misrepresentation in obtaining the release; 5) the existence of economic coercion in obtaining the release; and 6) evidence that the release is against public policy.See, e.g., Schmidt-Norton Ford, Inc. v. Ford Motor Co., 524 F. Supp. 1099, 1102-1103 (D. Minn. 1981), aff'd mem., 685 F.2d 438 (8th Cir. 1982).

Viewing the facts here in a light most favorable to Ardito and giving him the benefit of all reasonable inferences, as necessary upon a motion for summary judgment, the court finds that these factors weigh in favor of the validity of the release. It is undisputed that Ardito received over $4000, as well as termination with prejudice of legal claims against him, including the demand that he return the $14,000 from StimTech paid as part of his stock option-profit sharing agreement. Ardito now argues that this amount does not fully compensate him for damages allegedly suffered because of J&J's bad faith breach of the StimTech stock purchase agreement and shows that he did not intend to release such a claim.FN3 Sufficient consideration exists, however, if the releasor receives something of value to which the person had no previous right. Burns v. Northern Pac. Ry. Co., 134 F.2d 766 (8th Cir. 1943). Termination of claims of legal liability also satisfy the consideration requirement.See, e.g., Spanos Painting Contractors, Inc. v. Union Bldg. & Constr. Corp., 334 F.2d 457 (2d Cir. 1964), cert. denied, 380 U.S. 912 (1965). In the instant case, J&J gave up one of its key defenses to this lawsuit-the allegation that Ardito breached the non-compete provisions of the profit-sharing agreement. Consideration has been held to be a jury question if there are issues of whether consideration was given at all or whether a token amount is sufficient for the release. Maynard v. Durham & Southern Railway Co., 365 U.S. 160 (1961); Schmitt-Norton Ford, Inc. v. Ford Motor Co., 524 F. Supp. 1099 (1981), aff'd mem., 685 F.2d 438 (8th Cir. 1982). The consideration given here cannot be said to be a token amount and thus satisfies the minimum requirement. No material issue of fact is raised concerning consideration.

*4 The record also indicates that while Ardito chose to stop using Korba in February 1980, Korba remained as counsel of record throughout the settlement period. He testified that he read the terms of the release. Korba depo. at 78-9. He also signed the stipulations of dismissals. J&J ex. L. The record shows that Ardito had also consulted with his relative, a Minneapolis lawyer about these cases and had this lawyer available to him throughout 1980. Under these circumstances, Ardito did have an opportunity to consult an attorney.

The language of the release, another factor to be considered, encompasses the present suit. The release clearly states that Ardito and AMS releases StimTech and J&J from 'any and all manner of action . . . known or unknown . . . which [plaintiff] ever had, has or ever can, shall or may have or claim to have against Releasees . . ..' Ardito asserts that despite the broad language of the release, the correspondence between the parties limited the settlement negotiations to 'this matter.' The plain language of the release, however, is not limited to 'this matter', but includes 'any and all manner of actions, suits, claims, demands, damage, judgments levies, and executions, whether known or unknown, suspected or unsuspected . . .' The release is the operative document.

Additionally, there is no evidence, nor does the plaintiff allege, that J&J acted inequitably in negotiating the settlement and release. Nor does the record show any allegations or evidence of misrepresentation, fraud, or economic coercion. The release is not against public policy because it has no effect on any state regulatory scheme and merely disposes of a private dispute.Compare Chase Manhattan Bank, N.A. v. Clusiau Sales & Rental, Inc., 308 N.W.2d 490 (Minn. 1981).

Ardito does not argue that these factors show that the lease is invalid. Rather, he focuses on the intent of the parties at the time the release was executed. He contends that a jury must determine whether the parties contemplated releasing the claims involved in the current lawsuit.

In its previous Memorandum Opinion and Order dated August 12, 1982, the court found that the factual record was too sketchy to determine what the parties contemplated at the time of the release. At this point, however, after discovery, the record has been supplemented and no factual issues remain. Plaintiff does not dispute being aware in 1979, a year before the release was signed, of potential claims against J&J now being asserted by him. He does not dispute signing and swearing to a lengthy affidavit in McDonald v. Johnson & Johnson, which set out in detail all the basic allegations concerning J&J's alleged malfeasance now contained in this lawsuit. Nor does plaintiff deny discussing with his own attorney, around the same time he signed the McDonald affidavit, investigation of his own claims against J&J based on the allegations made by plaintiffs in the McDonald lawsuit. The record shows that plaintiff knew about his potential claims. Although he may not have known the full amount of damages which he might have been awarded, a unilateral mistake concerning the effect of a release is not a basis for setting it aside, absent evidence of fraud, misrepresentation or other inequitable conduct.See, e.g., Schmitt-Norton Ford, Inc. v. Ford Motor Co., 524 F. Supp. 1099, 1104 (D. Minn. 1981), aff'd, 685 F.2d 438 (8th Cir. 1982). And, as stated above, the consideration was more than sufficient.

***5** Ardito also argues that J&J did not intend the release to cover the claims raised in his current lawsuit. He states that local counsel for J&J who drafted the release did not know of the McDonald case or claims. That counsel has testified, however, that by including such broad language, she intended to obtain release of all claims of Ardito then in existence, of whatever type or description.See Dreher depo., February 27, 1985, pp. 42-43. Ardito also maintains that the court may draw an adverse inference from J&J's assertion of attorney-client privilege and refusal to produce files relevant to the release. Ardito did not attempt to challenge the assertion of privilege, however, and it has not been shown to be improper. No adverse inference may be drawn as a matter of law from the legitimate assertion of the attorney-client privilege.See, e.g., A.B. Dick Co. v. Marr, 95 F. Supp. 83 (S.D.N.Y. 1950), app. dsm'd, 197 F.2d 498 (2d Cir.), cert. denied, 344 U.S. 878 (1952).

To sum, no disputed issue of material fact exists. Analysis of the broad language of the instrument and the other factors used to evaluate the validity of a release, as well as the circumstances surrounding the release's execution, indicates, as a matter of law that Ardito's claims are barred by the release. Since this issue is dispositive, his motion for summary judgment is moot and it is not necessary to discuss the other issues raised by the parties.

ORDER

Accordingly, based on the above and all the files, records, and proceedings herein,

IT IS HEREBY ORDERED that

1. The motion of defendant for summary judgment is granted, and plaintiff Ardito's amended complaint is dismissed with prejudice.

2. The motion of plaintiff Ardito for partial summary judgment is denied as moot.

FN1 In a Memorandum Opinion and Order dated August 12, 1982, this court granted J&J's summary judgment motion on plaintiffs' claims for conversion and misrepresentation, but denied at that time the motion to dismiss claims of antitrust violations, tortious interference with contract, third-party contractual breach, and release. Subsequently, the factual record has been supplemented by further discovery and plaintiffs Leek, Johnson and Hamann have settled their claims against J&J. The Eighth Circuit Court of Appeals also ruled that the original owners of StimTech had no standing to pursue their antitrust claims. Ardito concedes that this ruling is applicable to his antitrust claim as well. McDonald v. Johnson & Johnson, 722 F.2d 1370 (8th Cir. 1984).

FN2 At this time, Ardito advised his attorney that he intended to seek advice from a relative who practiced law in Minneapolis. Ardito depo. at 85-86. Ardito did consult this relative and stated that he had the opportunity to ask for advice about important matters.Id. at 85-88.

FN3 He also adds that this amount corresponds to the ad damnum clause in the lawsuit he dismissed and further reveals his intent to settle only the AMS-StimTech claims.

Ardito v. Johnson & Johnson
Not Reported in F.Supp., 1985 WL 2461 (D.Minn.), 1982-2 Trade Cases P 64,954

END OF DOCUMENT

Exhibit 11

LEXSEE 2002 US DIST LEXIS 10485

ROBERT HIGDON, Plaintiff, v. ENTENMANN'S SALES CO., INC., et al., Defendants.

No. 01 C 6972

UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION

2002 U.S. Dist. LEXIS 10485

June 10, 2002, Decided
June 11, 2002, Docketed

DISPOSITION: [*1] Plaintiff's revised motions in limine granted in part and denied in part. Defendant Entenmann's motion in limine to bar opinion testimony granted. Defendant Entenmann's motions in limine to exclude evidence denied.

COUNSEL: For ROBERT HIGDON, plaintiff: Robert R. Cohen, Scott Jay Frankel, Frankel & Cohen, Chicago, IL.

For ENTENMANN'S SALES COMPANY, INC., defendant: Kim Ann Leffert, Maritoni D. Kane, Mayer, Brown, Rowe & Maw, Chicago, IL.

For LOCAL 734 INTERNATIONAL BROTHERHOOD OF TEAMSTERS, defendant: David J. Mathews, William A. Widmer, III, David Albert Iammartino, Carmell, Charone, Widmer, Mathews & Moss, Chicago, IL.

JUDGES: Suzanne B. Conlon, United States District Judge.

OPINION BY: Suzanne B. Conlon

OPINION

MEMORANDUM OPINION AND ORDER

Robert Higdon ("Higdon") sues Entenmann's Sales Company, Inc. ("Entenmann's") and International Brotherhood of Teamsters Local 734 ("Local 734")(collectively, "defendants") for violations of § 301 of the Labor Management Relations Act ("LMRA"), *29 U.S.C. § 141 et seq.* [*2] *Specifically, Higdon claims Entenmann's breached the collective bargaining agreement ("CBA") with Local 734 by terminating him without just cause and for his union activity. Higdon also claims Local 734 breached its duty of fair representation by failing to adequately contest his suspension and termination. The court denied defendants' motions for summary judgment and set the case for trial. Higdon and Entenmann's each move in limine* to bar certain evidence at trial.

DISCUSSION

I. Standard of Review

The background of this case is discussed in the court's order denying defendants' summary judgment motions. *See Higdon v. Entenmann's Sales Co., Inc., 2002 U.S. Dist. LEXIS 6982, 2002 WL 653896* (N.D. Ill. Apr. 19, 2002). The court excludes evidence on a motion *in limine* only if the evidence is clearly inadmissible for any purpose. *See Hawthorne Partners v. AT&T Technologies, 831 F. Supp. 1398, 1400 (N.D. Ill. 1993).* Motions *in limine* are disfavored; admissibility questions should be ruled upon as they arise at trial. *Id.* Accordingly, if evidence is not clearly inadmissible, evidentiary rulings must be deferred until trial to allow questions [*3] of foundation, relevancy and prejudice to be resolved in context. *Id. at 1401.* Denial of a motion *in limine* does not indicate evidence contemplated by the motion will be admitted at trial. Instead, denial of the motion demonstrates the court cannot determine whether the evidence in question should be excluded outside the trial context. *United States v. Connelly, 874 F.2d 412, 416 (7th Cir. 1989).*

II. Higdon's Motions *in Limine*

A. Disposition of Higdon's Pre-Election Protest

Higdon first moves to bar defendants from introducing any evidence relating to the International Brotherhood of Teamster's ("IBT") denial of his pre-election protest and subsequent appeal. In denying Higdon's pre-election protest, the election administrator made findings of fact based on an investigation completed by an election administrator representative. (Entenmann's Ex. 17; Local 734 Ex. 5). Thereafter, the election appeals master adopted the election administrator's findings in denying Higdon's appeal. (Entenmann's Ex. 19; Local 734 Ex. 6). Higdon contends the decisions contain inadmissible hearsay, are more prejudicial than probative [*4] and constitute improper lay or expert opinion. Local 734 and Entenmann's filed separate responses.

In its response, Local 734 argues that decisions qualify under the business record exception to the hearsay rule. Under *Federal Rule of Evidence 803(6)*, records kept in the course of regularly conducted business activity are admissible. *Fed.R.Evid. 803(6)*. However, *Rule 803(6)* does not encompass third party statements contained in the business record. *See Woods v. City of Chicago, 234 F.3d 979, 986 (7th Cir. 2000)*. Local 734 has not offered any hearsay exception encompassing the statements made to the election administrator representative who then conveyed the information to the election administrator. Therefore, the statements contained in the decisions are not admissible under *Rule 803(6)*.

In its response, Entenmann's argues the decisions qualify under the public records exception to the hearsay rule. Under *Federal Rule of Evidence 803(8)*, records kept pursuant to a legal duty are admissible. *Fed.R.Evid. 803(8)*. The IBT is not a public office or agency. Therefore, the decisions are not admissible under *Rule 803(8)*.

Defendants may not offer testimony regarding the [*5] IBT's disposition of Higdon's pre-election protest. The question of whether Higdon's suspension and termination was in retaliation for his union activities must be decided by the jury. In this context, the IBT's determination that its investigation did not reveal evidence linking Higdon's union activity to his suspension and termination has little probative value. The admission of the IBT's decisions would result in a prolonged inquiry into the nature and extent of the investigation. The probative value of the decisions is substantially outweighed by the likelihood of unfair prejudice, jury confusion and waste of time on collateral issues. Higdon's motion *in limine* to exclude the disposition of Higdon's pre-election protest is granted.

B. Attorney Advice Regarding Arbitration

Higdon next moves to bar defendants from introducing evidence relating to advice given by Local 734's attorney regarding possible arbitration of Higdon's termination. Specifically, Local 734 seeks to introduce two letters from its attorneys: one relates to Higdon and an Alpha Baking employee (Local 734 Ex. 8) and the other relates to a Chicago Baking Company employee (Local 734 Ex. 9). [*6] Higdon contends the attorney's advice is inadmissible hearsay, more prejudicial than probative and should be barred based on defendants' discovery violations. Local 734 and Entenmann's filed separate responses.

Local 734 and Entenmann's argue the attorney's advice regarding arbitration of Higdon's termination is not hearsay because it is not offered to prove the truth of the matter asserted. Rather, defendants offer the attorney's advice to show Local 734's actions in processing Higdon's grievance were not arbitrary, discriminatory or in bad faith. Used for this purpose, the attorney's advice regarding possible arbitration of Higdon's termination is not hearsay. Higdon may cross-examine regarding the basis for the attorney's advice.

Nevertheless, Higdon claims Local 734's refusal to allow deposition questioning of its witnesses regarding these attorney-client communications requires exclusion of this evidence. Discovery closed on March 6, 2002. Higdon did not move to compel deposition testimony regarding these communications before discovery closed. Therefore, Higdon's motion *in limine* is denied as to attorney's advice regarding possible arbitration of Higdon's discharge. [*7] *See Nichols v. City of Chicago, 1992 U.S. Dist. LEXIS 6069, 1992 WL 92117*, at *3 (N.D. Ill. Apr. 30, 1992) (motion *in limine* denied where moving party failed to enforce discovery rights).

However, Higdon's motion *in limine* is granted as to legal advice regarding possible arbitration of other employee discharges. Neither Local 734 or Entenmann's address the relevance of this evidence. Absent any showing that the evidence is relevant to Higdon's discharge, the evidence must be excluded.

III. Entenmann's Motions *in Limine*

A. Opinion Testimony of John Sladek

Entenmann's first moves to exclude opinion testimony of John Sladek. In response, Higdon confirms Sladek will testify that: (1) Entenmann's did not follow the usual progressive discipline policy in disciplining Higdon; (2) anyone other than Higdon would not have been discharged for having a route due bill; and (3) Local 734 would have taken the case to arbitration for anyone other than Higdon. Response at 1-2.

Lay opinions must be "(a) rationally based on the perception of the witness and (b) helpful to a clear understanding of the witness' testimony or the determination of a fact in the case." *Fed.R. Evid. 701.* [*8]

Higdon has not offered evidence that Sladek has personal knowledge of Entenmann's discipline or discharge decisions for any employee, including Higdon, or Local 734's arbitration decisions for any employee, including Higdon. The fact Sladek worked for Entenmann's for 18 years and ran for Local 734 office in 1996 and 1999 does not provide him first-hand knowledge of either defendants' managerial decisions. Therefore, inferences Sladek seeks to draw are too speculative to be helpful to the jury. *See United States v. Santos, 201 F.3d 953, 962 (7th Cir. 2000).* Entenmann's motion *in limine* to exclude the opinion testimony of John Sladek is granted.

B. Damages

Entenmann's next moves to bar Higdon from introducing evidence relating to damages, including back pay loss incurred in connection with his time-barred suspension. In response, Higdon contends Entenmann's waived the statute of limitations defense by failing to plead it as an affirmative defense.

Federal Rule of Civil Procedure 8(c) requires a defendant to plead affirmative defenses, including the statute of limitations. A defendant may waive an affirmative defense by failing to include the defense [*9] in its answer *Johnson v. Sullivan, 922 F.2d 346, 355 (7th Cir. 1990)(en banc).* Indeed, the statute of limitations defense must be raised in a timely fashion. *Venters v. City of Delphi, 123 F.3d 956, 967 (7th Cir. 1997).* In the amended complaint, Higdon alleges that Entenmann's breached the CBA by suspending him. Complaint at P 59. Nevertheless, Entenmann's has not offered any reason excusing its failure to plead the statute of limitations as an affirmative defense in its answer. Therefore, Entenmann's motion *in limine* to exclude back pay losses incurred in connection with Higdon's suspension is denied.

Entenmann's moves to bar Higdon from introducing evidence of consequential and emotional distress damages. Specifically, Entenmann's claims these damages are not available in § 301 hybrid actions. Congress has not specified the remedies available in a § 301 hybrid action. *See IBEW v. Foust, 442 U.S. 42, 60 L. Ed. 2d 698, 99 S. Ct. 2121, 2125 (1979).* However, the Supreme Court has recognized "the fundamental purpose of unfair representation suits is to compensate for injuries caused by violations of employee rights." *99 S. Ct. at 2125-26.* Indeed, [*10] "relief in each case should be fashioned to make the injured employee whole." *99 S. Ct. at 2126.* Higdon's only recourse for emotional distress suffered as a result of his suspension and termination is through a § 301 hybrid action. *See Douglas v. American Information Technologies Corp., 877 F.2d 565 (7th Cir.1989)*(common law intentional infliction of emotional distress claim preempted by § 301). Therefore, Higdon may offer evidence of loss resulting from defendants' alleged violation of his rights, including emotional distress. Entenmann's motion *in limine* to exclude evidence related to damages is denied.

C. Breach of the CBA

Finally, Entenmann's moves to bar Higdon from introducing evidence it breached Article 15, Section 3 of the CBA by not properly furnishing Local 734 with the cash stop rule one week before its effective date. Specifically, Entenmann's argues Higdon's claim is barred by the statute of limitations and his failure to exhaust his administrative remedies. As discussed above, Entenmann's was required to plead the statute of limitations or risk forfeiting the defense. In the amended complaint, Higdon alleges Entenmann's breached [*11] the CBA by failing to provide Local 734 with the cash stop rule before its effective date. Complaint at PP 47, 49. Nevertheless, Entenmann's has not offered an explanation for its failure to raise the statute of limitations as an affirmative defense in its answer. Nor has Entenmann's explained why it failed to plead Higdon's failure to exhaust administrative remedies. Entenmann's waived both defenses. *Johnson, 922 F.2d at 355* (statute of limitations); *Massey v. Helman, 196 F.3d 727, 735 (7th Cir. 1999)*(failure to exhaust administrative remedies).

Entenmann's claims the probative value of the evidence is substantially outweighed by the danger of unfair prejudice. Specifically, Entenmann's claims "the jury may leap to the conclusion that it breached Articles 5 [termination without just cause] and 6 [termination for union activity] without carefully considering the facts of the case" if Higdon "were able to prove that Entenmann's breached Article 15 of the CBA." Motion at 4. Higdon responds that Entenmann's promulgation of the cash stop rule, which violated Article 15, was a pretext for violation of Articles 5 and 6. The jury is presumed to have the capacity to understand [*12] and follow jury instructions. The probative value of Entenmann's alleged breach of Article 15 is outweighed by possible prejudice to Entenmann's. Entenmann's motion *in limine* to exclude evidence of Entenmann's alleged breach of Article 15, Section 3 of the CBA is denied.

CONCLUSION

Higdon's motions *in limine* are granted in part and denied in part. The motion to bar evidence relating to the disposition of his pre-election protest is granted. The motion to bar attorney advice regarding arbitration of Higdon's discharge is denied, but is granted as to other employee discharges. Entenmann's motions *in limine* are granted in part and denied in part. The motion to bar opinion testimony of John Sladek is granted. The motions to bar evidence related to damages and to bar evidence of Entenmann's alleged breach of Article 15, Section 3 of the CBA are denied.

June 10, 2002

ENTER:

Suzanne B. Conlon

United States District Judge

Exhibit 12

NOTICE: THIS IS AN UNPUBLISHED OPINION.

(The Court's decision is referenced in a "Table of Decisions Without Reported Opinions" appearing in the Federal Reporter. See CTA4 Rule 32.1.

United States Court of Appeals, Fourth Circuit.
ICAP, INCORPORATED, Plaintiff-Appellant,
v.
GLOBAL DIGITAL SATELLITE SYSTEMS, INCORPORATED, a British Virgin Island Corporation, Defendant-Appellee.
No. 99-2087.

Argued June 6, 2000.
Decided July 31, 2000.

Appeal from the United States District Court for the Eastern District of Virginia, at Alexandria. Theresa Carroll Buchanan, Magistrate Judge. (CA-98-1209-A).

Michael Edward Geltner, Geltner & Associates, P.C., Washington, DC, for appellant.
Earl John Oberbauer, Jr., Manassas, VA, for appellee.

Before LUTTIG, TRAXLER, and KING, Circuit Judges.

OPINION

PER CURIAM
*1 Appellant ICap, Inc., brought this action against Global Digital Satellite Systems, Inc., alleging that Global breached an oral contract to pay ICap a finder's fee of $1,000,000. The parties agreed to a bench trial before a magistrate judge, *see*28 U.S.C.A. § 636(c)(1) (West 1993), who ruled against ICap on its claims.FN1 ICap appeals, and we affirm.

FN1. The magistrate judge also rejected ICap's quantum meruit claim, and ICap does not pursue that claim on appeal.

I.

Global, which manufactures and installs satellite-based telecommunications systems, was searching for a joint-venture partner to facilitate the installation of a telephone system in Egypt. Global retained the services of ICap, an investment banking firm that provides financing for national and international public infrastructure projects, to locate a qualified partner. The parties initially anticipated that, in addition to locating a partner, ICap would serve as the project manager for the joint venture. All involved agreed that ICap would be compensated for its services, although the amount and terms of the compensation were not agreed to in advance.

ICap arranged for meetings between Global and Ashraf Nour, who had located a qualified principal in Egypt. It later became apparent that Nour would manage the project, and ICap's role was reduced to that of a finder only.

In February 1998, shortly before the formalization of the agreement between Global and Nour, ICap made a concerted effort to finalize its agreement with Global. On February 14, ICap's principals placed a telephone call to Nagaraj Murthy, the person designated by Global to negotiate the terms of the agreement with ICap. According to ICap, Murthy agreed during that telephone call that ICap would be paid $1,000,000 as a finder's fee. After Murthy agreed to that figure, and while the telephone call continued, ICap faxed Global a proposed agency agreement that included the $1,000,000 finder's fee.

All three of ICap's principals who participated in the February 14 telephone conversation testified at trial that Murthy specifically agreed to a $1,000,000 fee during the call. Murthy, however, testified that he did not agree to that fee and that he told ICap the proposed agreement was too complicated and would need to be approved by Laurence Goshorn, Global's president.

Because Global did not execute the February agreement, ICap faxed another agreement to Goshorn on March 10, 1998. The letter accompanying the March agreement stated that "in order to document our agreement, we enclose a revised draft, which is based on documents discussed and negotiated with representatives of [Global] since November. We believe it also to be responsive to all issues raised by [Murthy]." J.A. 122. Although the March agreement reflected the $1,000,000 finder's fee, it contained different terms for the payment of the fee. Mark Latimer, one of ICap's principals, explained at trial that he meant to fax the February agreement to Global, but that he inadvertently sent a prior draft of the agreement. According to Latimer, he believed that ICap and Global had reached an agreement in February, and the March fax was not intended to be further negotiation of their compensation.

***2** When Goshorn received the March agreement, he faxed a response stating that he was "*shocked* at the points on your cover letter" and that the $1,000,000 finder's fee "leaves me baffled!" J.A. 125. Communications between ICap and Global broke down thereafter.

Global entered into an agreement with the Egyptian principal located by Nour to install Global's telecommunications system in Egypt. As of the time of the hearing, however, the Egyptian government had refused to issue the necessary permits, and, consequently, the joint venture had earned no money.

By July 1998, ICap had decided that it would be necessary to file suit against Global to collect its fee. ICap called Global to inform it that a lawsuit was forthcoming. A Global representative suggested that the parties make a "last ditch effort" at settling the claim. J.A. 61. After more discussions, Global faxed ICap a letter offering to pay ICap $50,000. ICap rejected that offer as "insulting low," J.A. 127, and made a counteroffer of $794,000. Global refused ICap's counteroffer, and this action followed.

After a bench trial, the magistrate judge concluded that no contract had been reached between the parties on February 14:

> [T]he statements and outward expressions of the parties after February 14, 1998, constitute on-going negotiation of [ICap's] fee. These on-going negotiations, which continued until the end of July 1998, establish that the parties never had a meeting of the minds as to the amount and terms of [ICap's] compensation.... [B]ecause payment was contingent upon the signing of the joint venture agreement and the success of the project, the Court finds that the terms of payment are a material element of the contract. Consequently, the Court finds that there was not a meeting of the minds on all material elements of the contract and there is no express oral contract that is binding on the parties.

J.A. 139-40. The court thus ruled against ICap on its breach of contract claim.

II.

ICap first argues that the magistrate judge considered settlement negotiations between the parties when concluding that no agreement had been reached, thus violating Rule 408 of the Federal Rules of Evidence. ICap contends that all of the communications with Global after February 14 were attempts to settle its claim with Global. According to ICap, the magistrate judge specifically did not make the pivotal credibility determination-whether ICap's or Global's witnesses were telling the truth about the substance of the February 14 telephone conversation-and instead resolved the case solely through an impermissible consideration of settlement evidence. We disagree.

Rule 408 provides that:

> Evidence of (1) furnishing or offering or promising to furnish, or (2) accepting or offering or promising to accept, a valuable consideration in compromising or attempting to compromise a claim which was disputed as to either validity or amount, is not admissible to prove liability for or invalidity of the claim or its amount. Evidence of conduct or statements made in compromise negotiations is likewise not admissible. This rule does not require the exclusion of any evidence otherwise discoverable merely because it is presented in the course of compromise negotiations. This rule also does not require exclusion when the evidence is offered for another purpose, such as proving bias or prejudice of a witness, negativing a contention of undue delay, or proving an effort to obstruct a criminal investigation or prosecution.

***3** We will assume for the purposes of this opinion that ICap did not waive its Rule 408 claim by introducing the disputed evidence without mentioning Rule 408 or otherwise bringing to the court's attention that the evidence should not be considered when determining the validity of ICap's claims or its amount.[FN2] With this assumption, then, the question that must be resolved is whether the evidence of the communications between the parties after February 14 in fact falls within the scope of Rule 408.

FN2. ICap did file a post-trial motion in which it argued that it reached an oral agreement with Global on February 14 and that the March 10 agreement was not intended as further negotiation of the terms of that oral agreement. However, even in that motion, ICap did not mention Rule 408 or otherwise argue that the communications after February were part of any effort to settle its breach of contract claim.

To determine whether statements come within Rule 408, the inquiry is whether the "statements or conduct were intended to be part of the negotiations for compromise." *Fiberglass Insulators, Inc. v. DuPuy*, 856 F.2d 652, 654 (4th Cir.1988). The determination that a statement does or does not fall within the rule is a factual determination that must be accepted on appeal unless clearly erroneous. *See id.*

The magistrate judge did not specifically find that the post-February communications were not negotiations to settle the disputed claim, which is not surprising given that ICap raised the issue for the first time on appeal. Nonetheless, the magistrate judge concluded that, during the February 14 telephone call, the parties did not come to a meeting of the minds as to the amount of ICap's fee or the terms for payment of the fee. This conclusion is an implicit, but inescapable, rejection of ICap's argument.

Clearly, there must first have been an agreement between ICap and Global on the essential terms of how much ICap would be paid and the terms under which that payment would be made before there could be any attempt to settle a dispute over Global's failure to comply with the agreement. By concluding that the parties did not reach an agreement on those critical terms, the magistrate judge effectively determined that the post-February communications were further, but ultimately unsuccessful, *contract* negotiations.

Contrary to ICap's argument, the magistrate judge did make a determination about the credibility of the witnesses when resolving this issue. The appealed order states that "[b]oth parties presented witness testimony on [the issue of an oral contract]" and that "[t]he Court finds the witnesses credible."J.A. 138. As we understand the order, the magistrate judge concluded that all the witnesses involved in the February 14 telephone call believed their trial testimony to be true-ICap's principals believed Murthy agreed to the $1,000,000 fee, and Murthy believed he did not agree to the fee. Thus, the magistrate judge concluded that the parties never reached an agreement on the essential terms of the contract.

Given the disputed evidence about the substance of the February 14 telephone conversation and the statements in the letter accompanying the March 10 agreement that characterized the agreement as a "revised" one that was "responsive" to issues raised by Global, the magistrate judge's no-meeting-of-the-minds finding is not clearly erroneous. And, from that finding, the conclusion that the post-February communications between the parties were contract negotiations, not settlement negotiations, necessarily follows. Under these circumstances, Rule 408 is simply inapplicable to this case.[FN3]

FN3. Even if the July discussions should be considered settlement negotiations, the substance of the March agreement and accompanying letter, when considered with the testimony about the February telephone call, is more than sufficient to support the magistrate judge's conclusion that there was no meeting of the minds as to the essential terms of the agreement between ICap and Global.

III.

***4** ICap sought to admit the testimony of an expert who would testify that Scott, one of ICap's principals, had taken and passed a polygraph examination that asked whether Murthy had agreed to the $1,000,000 fee during the February 14 telephone conversation. The magistrate judge refused to consider the evidence, concluding that the use of polygraph evidence to bolster or impeach the testimony of a witness is not allowed in this circuit.

According to ICap, the Supreme Court's opinion in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993), calls into question our prior cases establishing a *per se* rule against the use of polygraph evidence to impeach or bolster the credibility of witness. *See, e.g.,* United States v. A & S Council Oil Co., 947 F.2d 1128, 1134 (4th Cir.1991) ("This court's precedents preclude direct attacks on or bolstering of the credibility of a witness through evidence that the witness has taken a polygraph test."). ICap thus contends the magistrate judge erred in concluding that polygraph evidence is *per se* inadmissible. We find no error.

In its pre-trial memorandum addressing the testimony of its polygraph expert, ICap sought to admit the evidence only if Global attempted "to impeach Mr. Scott's credibility on the issue of whether [Global] orally agreed to the $1,000,000 finder's fee."J.A. 21. At trial, after the court denied ICap's request to call the polygraph expert, counsel for ICap noted he "thought that it would be responsive to bolstering after impeachment," J.A. 94, but that he had not heard any impeachment.

Our review of Global's cross-examination of Scott confirms that Global did not inquire into or otherwise challenge Scott's recollection of the substance of the February 14 telephone call. Because the only factual predicate under which ICap sought to admit the expert's testimony-the impeachment of Scott's testimony-did not occur, the magistrate judge committed no error in refusing to allow the expert to testify.[FN4]

> FN4. Given that the magistrate judge found ICap's witnesses to be credible, the evidence would have been cumulative in any event.

Moreover, in *United States v. Sanchez,* 118 F.2d 192 (4th Cir.1997), we reaffirmed our *per se* rejection of the use of polygraph evidence to impeach the credibility of a witness and concluded that the cases establishing that rule remain binding precedent notwithstanding the change in the law arguably worked by *Daubert.See id.* at 197 n. 3. We also note that the Supreme Court recently concluded that a *per se* rule excluding all polygraph evidence is constitutional. *See* United States v. Scheffer, 523 U.S. 303 (1998). We therefore reject ICap's challenge to the exclusion of the polygraph evidence.

IV.

Accordingly, for the foregoing reasons, the decision of the magistrate judge is hereby affirmed.

AFFIRMED.

C.A.4 (Va.),2000.
ICAP, Inc. v. Global Digital Satellite Systems, Inc.
225 F.3d 654, 2000 WL 1049854 (C.A.4 (Va.))

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Exhibit 13

HOnly the Westlaw citation is currently available.
United States District Court, N.D. Illinois, Eastern Division.
In re BALLY TOTAL FITNESS SECURITIES LITIGATION.
Nos. 04 C 3530, 04 C 3634, 04 C 3713, 04 C 3783, 04 C 3844, 06 C 3936, 04 C 4697, 04 C 1437.

July 12, 2006.

MEMORANDUM OPINION

JOHN F. GRADY, United States District Judge.
***1** Before the court are defendants' motions to dismiss the consolidated class action complaint. For the reasons explained below, the motions are granted.

BACKGROUND

Plaintiffs have filed several related securities fraud putative class actions against Bally Total Fitness Holding Corporation ("Bally"); three of its current or former officers and directors, Lee S. Hillman, John W. Dwyer, and Paul A. Toback; and Bally's former auditor, Ernst & Young, LLP, for violations of §§ 10(b) and 20(a) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78j(b) and 78t(a), and Rule 10b-5 promulgated thereunder by the Securities and Exchange Commission (the "SEC"), 17 C.F.R. 240.10b-5. Plaintiffs allege that defendants violated federal securities laws by publicly disseminating false and misleading corporate reports, financial statements, and press releases primarily through "two related fraudulent techniques": improperly recognizing revenue prematurely and improperly delaying the recordation of expenses. (Consolidated Class Action Complaint ("CCAC") ¶ 5.)

We previously granted the parties' motions for consolidation of the cases for all purposes and directed that the consolidated cases be referred to as "In re Bally [Total] Fitness Securities Litigation."(Minute Order of Sept. 8, 2004.) [FN1]We also appointed Cosmos Investment Company, LLC ("Cosmos") as lead plaintiff (Memorandum Opinion of March 15, 2005), and appointed lead and local counsel (Minute Order of May 23, 2005). On January 3, 2006, Cosmos filed a consolidated class action complaint on behalf of a class consisting of those who purchased or acquired Bally securities during the period of August 3, 1999 through and including April 28, 2004. The complaint alleges the following facts, which are taken as true for purposes of the instant motions.

FN1. The consolidated cases are as follows (abbreviating defendants to "Bally"): *Petkun v. Bally,* 04 C 3530; *Marcano v. Bally,* No. 04 C 3634;*Garco Invs., LLP v. Bally,* No. 04 C 3713;*Salzmann v. Bally,* No. 04 C 3783;*Rovner v. Bally,* No. 04 C 3844;*Koehler v. Bally,* No. 04 C 3936;*Eads v. Bally,* No. 04 C 4697; and *Levine v. Bally,* 06 C 1437.

Strougo v. Bally, No. 04 C 3864, was voluntarily dismissed on March 15, 2005, and *Rosenberg v. Bally,* No. 04 C 4342, was voluntarily dismissed on April 7, 2005.

Defendant Bally is a corporation that operates hundreds of fitness centers throughout North America with approximately four million members. Bally's securities are publicly traded on the New York Stock Exchange. During the time period relevant to this action, defendant Dwyer was Bally's Chief Financial Officer ("CFO"), Executive Vice President, and a member of Bally's Board of Directors (the "Board"); defendant Hillman was Chief Executive Officer, President, and Chairman of the Board until December 2002. Defendant Toback is Bally's current Chief Executive Officer, President, and Chairman of the Board. We will refer to Hillman, Dwyer, and Toback collectively, where appropriate, as the "Individual Defendants." The accounting firm Ernst & Young, LLP ("E & Y") was Bally's outside auditor until it resigned the engagement on March 31, 2004.

From August 3, 1999 through April 2004, Bally issued press releases and filed 8-K, 10-K and 10-Q forms with the SEC stating its financial results for various time periods. Some of the SEC filings contained certifications by Dwyer and Hillman, or Dwyer and Toback, pursuant to the Sarbanes-Oxley Act of 2002. In the Sarbanes-Oxley certifications, the

Individual Defendants attested that they had reviewed the contents of the particular report to confirm that it did not contain any untrue statement of material fact or omit a material fact necessary to make the statements not misleading.

*2 Plaintiffs allege that Bally's financial statements were materially false and misleading because, contrary to defendants' representations, they had not been prepared in conformity with Generally Accepted Accounting Principles (GAAP). Bally is alleged to have violated GAAP in the following ways:

- improperly recognizing membership revenue

- deferring costs incurred in signing up members instead of recognizing membership acquisition expenses, thereby reflecting the costs as an asset

- establishing accruals for unpaid dues on inactive membership contracts instead of writing them off as uncollectible

- improperly accounting for payment obligations in relation to the acquisition of a business

- improperly classifying proceeds from the sale of a future revenue stream

- recognizing cash received in advance of the performance of personal training services as fees earned instead of as deferred revenue

- improperly separating multiple-element bundled contracts for health club services, personal training services, and nutritional products into multiple accounting units, resulting in premature revenue recognition

- failing to estimate the ultimate cost of settling self-insurance claims for workers' compensation, health and life, and general liability, thereby materially understating its liability for these claims

- improperly capitalizing costs incurred to develop internal-use software

- failing to record and assign a fair value to certain separately identifiable acquired intangible assets

- establishing a practice of amortizing goodwill over forty years when this amortization period was inconsistent with the maximum reasonable and likely duration of material benefit from the acquired goodwill

- ignoring "trigger events" and other conditions which, at various dates, indicated that the carrying amounts of fixed assets were impaired, and failing to perform any impairment analyses or recognize impairment losses

- reporting the dollar amount of uncashed checks as income instead of as escheatment liabilities;

- capitalizing advertising costs and amortizing those costs over the estimated life of the advertising campaign instead of expensing them when the first advertisement took place

- adding maintenance costs to the costs of property and equipment and then depreciating this improperly established "asset"

- improperly deferring costs associated with start-up activities, such as rent

- failing to properly compile and record inventory on a periodic basis and failing to match appropriate costs with revenues in order to make a proper determination of the realized income

- failing to accrue obligations as of the end of each accounting period even though transactions and events giving rise to the obligations arose during the accounting period

- failing to recognize gains and losses from various foreign currency transactions that affected individual assets, liabilities, and cash flows

*3 • failing to recognize rent expense on club leases with escalating rent obligations using the required straight-line method; failing to reflect lease incentives as reductions of rental expense over the term of the lease; and improperly reflecting tenant allowances as a reduction to property and equipment and depreciating these amounts

• reflecting deferred tax assets and valuation allowances based upon improperly-determined taxable income and without having performed a realistic and objective assessment as to whether it was more likely than not that some or all of the deferred tax asset would not be realized

(CCAC ¶¶ 121-174.)

Plaintiffs also allege that E & Y, in its capacity as Bally's outside auditor during most of the relevant time period, played a role in the fraud. E & Y issued several unqualified audit opinions on Bally's consolidated financial statements for the years 1999-2003. Plaintiffs maintain that E & Y diverged from Generally Accepted Auditing Standards (GAAS) when auditing Bally in that it either identified and ignored flagrant multiple violations of GAAP or recklessly failed to identify these violations.

The complaint alleges that "[t]he truth concerning [Bally's] chronic accounting improprieties began to emerge on April 28, 2004."(CCAC ¶ 8.) On that day, Bally issued a press release announcing that its CFO, Dwyer, had resigned "pursuant to the terms of a separation agreement" and that "[s]eparately, the Company announced" that the SEC had commenced an investigation connected to Bally's recent restatement regarding the timing of recognition of prepaid dues.[FN2](*Id.* ¶ 8 (quoting from press release).) In plaintiffs' view, the press release "cast serious doubt on the accuracy and reliability of Bally's financial statements, and, significantly, on the integrity of Bally's management."(*Id.* ¶ 9.)

FN2. On April 2, 2004, Bally had issued an initial restatement of previously-reported 2003 financial results. (CCAC ¶ 8 n. 1.)

Plaintiffs assert that in response to the April 28, 2004 announcement, the price of Bally common stock fell from $5.40 per share on April 28 to $4.50 per share on April 29, a 16.6% drop. In the period of ninety trading days following the April 28 disclosure, the stock reached a mean trading price of $4.56 per share.

When Bally found out that it was being investigated by the SEC, it initiated an internal investigation of its accounting practices, spearheaded by its Audit Committee. On November 15, 2004, Bally announced that based on the internal investigation, the Audit Committee had concluded that Bally's financial statements for the years 2000 through 2003 (including the initial restatement of 2003 that had been issued on April 2, 2004) and the first quarter of 2004 could no longer be relied upon and should be restated. Bally also announced that it would be unable to issue any financial statements for the remainder of 2004 or for 2005 until it had completed the restatements, which were expected to be issued in July 2005 (but were not actually issued until November 2005).

***4** On February 8, 2005,[FN3] Bally issued a press release announcing the findings of the Audit Committee. Bally announced that it was suspending the severance pay of Hillman and Dwyer (the former CEO and CFO, respectively), who, in the Audit Committee's view, "were responsible for multiple accounting errors and creating a culture within the accounting and finance groups that encouraged aggressive accounting."(CCAC ¶ 14.) Bally also stated that it had identified deficiencies in its internal controls over financial reporting.

FN3. Plaintiffs state in their briefs that the complaint incorrectly refers to this date as February 10, 2005. (Plaintiffs' Response to E & Y's Mot. at 4 n. 2, Plaintiffs' Response to Bally Defs.' Mot. at 6 n. 3.)

On November 30, 2005, Bally filed a restatement that comprehensively restated its financial results for 2000, 2001, 2002, and 2003, and first reported results for 2004 and the first three quarters of 2005 (the "Restatement"). The adjustments in the Restatement resulted in an increase in previously-reported net loss of $96.4 million for the year 2002 and a decrease in net loss of $540 million for the year 2003. Bally also increased the January 1, 2002 opening accumulated stockholders' deficit by $1.7 billion to recognize the effects of corrections in financial statements prior to 2002.

The first of these related cases was filed on May 20, 2004. The consolidated class action complaint of January 3, 2006 contains two counts. In Count I, plaintiffs allege that the defendants violated § 10(b) of the Securities Exchange Act and Rule 10b-5. Count II is a "control person" claim in which plaintiffs allege that the Individual Defendants violated § 20(a) of the Securities Exchange Act. Plaintiffs seek compensatory damages as well as attorney's fees, costs, and expenses.

Four separate motions to dismiss the consolidated class action complaint have been filed by (1) Bally and Toback; (2) Hillman; (3) Dwyer; and (4) E & Y. Those motions are now fully briefed.

DISCUSSION

Section 10 (b) of the Securities Exchange Act makes it unlawful for a person "[t]o use or employ, in connection with the purchase or sale of any security ... any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [SEC] may prescribe."15 U.S.C. § 78j(b). Among those rules is Rule 10b-5, which "prohibits the making of any untrue statement of material fact or the omission of a material fact that would render statements made misleading in connection with the purchase or sale of any security." *In re HealthCare Compare Corp. Sec. Litig.*, 75 F.3d 276, 280 (7th Cir.1996).[FN4] To prevail on a Rule 10b-5 claim, a plaintiff must establish that the defendant: (1) made a false statement or omission, (2) of material fact, (3) with scienter, (4) in connection with the purchase or sale of securities, (5) upon which the plaintiff justifiably relied, and (6) that the false statement or omission proximately caused the plaintiff's injury. *Otto v. Variable Annuity Life Ins. Co.*, 134 F.3d 841, 851 (7th Cir.1998).

> FN4. Rule 10b-5 provides:
>
> > It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
> >
> > (a) To employ any device, scheme, or artifice to defraud,
> >
> > (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
> >
> > (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.
>
> 17 C.F.R. § 240.10b-5.

The heightened pleading requirements of Federal Rule of Civil Procedure 9(b) apply here because plaintiffs' claims are based on securities fraud. *See Sears v. Likens*, 912 F.2d 889, 893 (7th Cir.1990) ("Rule 9(b)... governs claims based on fraud and made pursuant to the federal securities laws.").Rule 9(b) requires plaintiffs to plead with particularity the factual bases for averments of fraud, including "the identity of the person making the misrepresentation, the time, place, and content of the misrepresentation, and the method by which the misrepresentation was communicated to the plaintiff."*Id.* (citation omitted); *see also* *DiLeo v. Ernst & Young*, 901 F.2d 624, 627 (7th Cir.1990) (stating that the plaintiff must plead the who, what, when, where, and how of the alleged fraud).

***5** Plaintiffs' claims are also subject to the heightened pleading requirements of the Private Securities Litigation Reform Act ("PSLRA"), 15 U.S.C. § 78u-4*et seq.*,[FN5] which the Seventh Circuit recently described:

> FN5. The PSLRA "was designed to curb abuse in securities suits, particularly shareholder derivative suits in which the only goal was a windfall of attorney's fees, with no real desire to assist the corporation on whose behalf the suit was brought." *Green v. Ameritrade, Inc.*, 279 F.3d 590, 595 (8th Cir.2002).

> Unlike a run-of-the-mill complaint, which will survive a motion to dismiss for failure to state a claim so long as it is possible to hypothesize a set of facts, consistent with the complaint, that would entitle the plaintiff to relief, the PSLRA essentially returns the class of cases it covers to a very specific version of fact pleading-one that exceeds even the particularity requirement of [Rule] 9(b). Under the PSLRA, a securities fraud complaint must (1) "specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the

statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed" and (2) "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind."15 U.S.C. § 78u-4(b)(1), (2). In other words, plaintiffs must not only plead a violation with particularity; they must also marshal sufficient facts to convince a court at the outset that the defendants likely intended to deceive, manipulate, or defraud.
Makor Issues & Rights, Ltd. v. Tellabs, Inc., 437 F.3d 588, 594 (7th Cir.2006) (citations and some internal quotation marks omitted).

Defendants contend that plaintiffs have failed to plead their claims with the required particularity and that plaintiffs have failed to adequately plead the elements of scienter and loss causation.

A. ***Scienter***

To satisfy the scienter requirement of § 10(b) and Rule 10b-5, a plaintiff must demonstrate that a defendant either had the "intent to deceive, manipulate, or defraud," Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976), or a "reckless disregard for the truth of the material asserted, whether by commission or omission," Ambrosino v. Rodman & Renshaw, Inc., 972 F.2d 776, 789 (7th Cir.1992) (internal quotation marks omitted)."[R]eckless conduct may be defined as a highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it."*Sundstrand Corp. v. Sun Chem. Corp.,* 553 F.3d 1033, 1045 (7th Cir.1977), *cited in* Makor Issues, 437 F.3d at 600.

"Congress did not, unfortunately, throw much light on what facts will suffice to create [a strong inference of scienter]. Currently three different approaches toward the way to demonstrate the required 'strong inference' exist among the courts of appeals." *Makor Issues,* 437 F.3d at 601. One approach is to allow plaintiffs to state a claim by pleading either motive and opportunity or strong circumstantial evidence of recklessness or conscious misbehavior. The second approach declines to adopt the "motive and opportunity" analysis and imposes a more onerous burden of pleading in great detail facts constituting strong circumstantial evidence of deliberately reckless or conscious misconduct. *See id.*(summarizing case law). In *Makor Issues,* the Seventh Circuit chose the middle ground, which neither adopts nor rejects particular methods of pleading scienter, such as alleging facts showing motive and opportunity, but instead requires plaintiffs to plead facts that together establish a strong inference of scienter. *See id.*"[T]he best approach is for courts to examine all of the allegations in the complaint and then to decide whether collectively they establish such an inference. Motive and opportunity may be useful indicators, but nowhere in the statute does it say that they are either necessary or sufficient."*Id.*

***6** Another concern discussed in *Makor Issues* is the degree of imagination we can use in deciding whether a complaint creates a strong inference of scienter. The Seventh Circuit held: "Instead of accepting only the most plausible of competing inferences as sufficient at the pleading stage, FN6 we will allow the complaint to survive if it alleges facts from which, if true, a reasonable person could infer that the defendant acted with the required intent ."*Id.* at 602.

FN6. The Court was referring to the Sixth Circuit's pronouncement in *Fidel v. Farley,* 392 F.3d 220, 227 (6th Cir.2004), that the "strong inference" requirement creates a situation where plaintiffs are entitled only to the most plausible of competing inferences. The Seventh Circuit declined to express a view on whether the Sixth Circuit's approach is constitutional, but stated: "[W]e think it wiser to adopt an approach that cannot be misunderstood as a usurpation of the jury's role." Makor Issues, 437 F.3d at 602.

The Seventh Circuit also held in *Makor Issues* that the "group pleading doctrine," pursuant to which scienter allegations made against one defendant could be imputed to all other defendants in the same action, did not survive the heightened pleading requirements of the PSLRA. *See id.* at 603. "While we will aggregate the allegations in the complaint to determine whether it creates a strong inference of scienter, *plaintiffs must create this inference with respect to each individual defendant* in multiple defendant cases."*Id.* (emphasis added).

Defendants contend that plaintiffs have failed to plead any particularized facts sufficient to give rise to any inference, much less the requisite strong inference, of scienter. Defendants point out that plaintiffs have failed to allege any particular "red flags" that should have warned defendants of accounting problems or any particular conversations, meetings, or documents. Moreover, the complaint fails to allege that the Individual Defendants sold any stock during the class period and thereby benefited from the allegedly inflated stock prices. Defendants also argue that the complaint is problematic because it expressly relies on the "group pleading doctrine," which was rejected in *Makor Issues.*[FN7]

> FN7. The complaint states: "It is appropriate to treat the Individual Defendants as a group for pleading purposes ...." (CCAC ¶ 33.)

In their responses [FN8] to defendants' motions, plaintiffs submit that they have met their burden of pleading scienter by alleging the following, taken collectively: (1) the "admissions" in Bally's press release of February 8, 2005; (2) the characteristics of the Restatement; (3) "motive and opportunity" allegations; and (4) Bally's violation of its own internal accounting policies.[FN9] We will address each category in turn and then address each of the defendants.

> FN8. Plaintiffs filed two responsive briefs to defendants' motions. One brief responds to the motions of Bally and Toback, Hillman, and Dwyer; the second brief responds to the motion of E & Y.

> FN9. Plaintiffs categorize their allegations slightly differently, but we have reorganized them to facilitate our discussion.

Plaintiffs first point to Bally's press release of February 8, 2005, which announced the findings of Bally's Audit Committee, and quote extensively in their briefs from that press release. (The press release is also attached as an exhibit to plaintiffs' briefs.) The press release included, *inter alia,* the following statements: there had previously been numerous accounting errors; Bally had taken "aggressively optimistic positions" on accounting policies "without a reasonable empirical basis"; Hillman and Dwyer, who had both resigned by then, had been responsible for a culture of "aggressive accounting"; Dwyer had made a "false and misleading" statement to the SEC; as a result of the findings, Hillman and Dwyer's severance pay was being discontinued; two employees (who are not defendants in this action) had engaged in unspecified "improper conduct"; E & Y had "made several errors" in its audit work; and Bally's "internal controls" had numerous deficiencies. (Plaintiffs' Response to Bally Defs.' Mot. at 6-7.)

*7 Plaintiffs maintain that through these statements, Bally "admitted its own scienter." If that is the case, we find it curious that the complaint refers to the press release in only two paragraphs and quotes from it only in relation to the statement regarding Hillman and Dwyer creating a culture of "aggressive accounting." (CCAC ¶¶ 14-15.) Plaintiffs argue that they are permitted to allege additional facts in response to a motion to dismiss so long as those facts are consistent with the complaint's allegations. The cases they cite for this proposition, however, were not cases where fact pleading was required, as it is here.

Nevertheless, for purposes of this motion and so we do not have to revisit this issue, we will consider the complaint as incorporating the press release. We do not believe it assists the plaintiffs in raising an inference of scienter. First of all, the findings are vague and unspecific, and many of the terms, such as "aggressive accounting" and "aggressively optimistic," are imprecise. None of the alleged errors, aggressively optimistic positions, improper conduct, or deficiencies in controls constitute particularized allegations. And contrary to plaintiffs' argument, the fact that Bally acknowledged that false statements were made is not equivalent to admitting scienter. A false statement is one element of a securities fraud claim; scienter is a wholly separate element. The Audit Committee's findings are essentially of negligence, but not scienter. It is important to remember that simple negligence and even "inexcusable negligence" does not amount to scienter. What is required to be shown is an *extreme* departure from the standards of ordinary care. The findings do not rise to this level. Another reason why the press release does not support an inference of scienter is that the findings are simply hindsight conclusions. They do not assist in determining the state of mind behind the misstatements at the time they were made. *See generally DiLeo,* 901 F.2d at 628 ("There is no 'fraud by hindsight' ...."); *Sundstrand,* 553 F.2d at 1045 n. 19

("[T]he circumstances must be viewed in their contemporaneous configuration rather than in the blazing light of hindsight."); Davis v. SPSS, Inc., 385 F.Supp.2d 697, 714 (N.D.Ill.2005) ("Permutations of 'fraud by hindsight' do not create an inference, much less a strong inference, of *scienter.*").

The second factor relied on by plaintiffs is the Restatement and its characteristics. Plaintiffs assert that the Restatement "totaled 438% of the aggregate pre-restatement net income" and that we can infer scienter from the magnitude of the Restatement, combined with the high number and repetitiveness of the GAAP violations and the simplicity of the accounting principles that were violated. (Plaintiffs' Response to Bally Defs.' Mot. at 14-16.)

The Seventh Circuit has observed that even a very large restatement is not itself evidence of scienter:

> ***8** Four billion dollars is a big number, but even a large column of big numbers need not add up to fraud.
>
> ...
>
> The story ... is familiar in securities litigation. At one time the firm bathes itself in a favorable light. Later the firm discloses that things are less rosy. The plaintiff contends that the difference must be attributable to fraud. "Must be" is the critical phrase .... Because only a fraction of financial deteriorations reflects fraud, plaintiffs may not proffer the different financial statements and rest. Investors must point to some facts suggesting that the difference is attributable to fraud.

DiLeo, 901 F.2d at 627 (citing, *inter alia,* Goldberg v. Household Bank, F.S.B., 890 F.2d 965, 967 (7th Cir.1989), which noted: "Restatements of earnings are common.").*See also* Fidel v. Farley, 392 F.3d 220, 231 (6th Cir.2004) ("Allowing an inference of scienter based on the magnitude of fraud ... would ... allow the court to engage in speculation and hindsight, both of which are counter to the PSLRA's mandates."); Davis, 385 F.Supp.2d at 713 ("Restatements establish that misleading statements were made, but ... provid[e] no assistance in determining the intent behind the misstatements."); Chu v. Sabratek Corp., 100 F.Supp.2d 815, 824 (N.D.Ill.2000) ("A company's overstatement of earnings, revenues, or assets in violation of GAAP does not itself establish scienter.").

We are not prepared to say that the magnitude of a restatement could never contribute to an inference of scienter. But this is not such a case, especially considering that the SEC filings and press releases at issue did not consistently overstate revenues and income or consistently understate losses. Rather, the revenue for some quarters was at times understated and losses for some quarters were at times overstated during the class period. On these facts, it is clear that significant mistakes were made, but we cannot infer scienter. The same can be said for plaintiffs' argument that the number and repetitiveness of the GAAP violations and the purported simplicity of the pertinent accounting principles support an inference of scienter. These "characteristics" of the Restatement are simply another way of saying that multiple accounting errors were made, but they are not facts tending to show that defendants acted with the required intent.

Another category of allegations relied upon by plaintiffs can be deemed the "motive and opportunity" allegations. One allegation is that the Individual Defendants had the opportunity to commit fraud based on their positions in the company and their access to financial information. Scienter, however, may not rest on the inference that defendants must have been aware of a misstatement based simply on their positions within the company. *See* Davis, 385 F.Supp.2d at 713-14 (quoting Johnson v. Tellabs, Inc., 262 F.Supp.2d 937, 957 (N.D.Ill.2003) and Abrams v. Baker Hughes Inc., 292 F.3d 424, 432 (5th Cir.2002)). Plaintiffs assert that they have not pled scienter based merely on the Individual Defendants' positions in the company, but also on the Individual Defendants' personal responsibility for the accounting errors and aggressive accounting as well as their signed Sarbanes-Oxley certifications attesting that they had evaluated the company's internal controls. As noted above in relation to the Audit Committee's findings, the assertion that the Individual Defendants were personally responsible for the errors and "aggressive accounting" is conclusory; there are no facts alleged to bolster this allegation. Nor are any particular facts alleged as to what internal controls the Individual Defendants were familar with and how these related to the accounting misstatements.

***9** Plaintiffs also emphasize their allegation that the accounting misstatements were related to Bally's "core business" and contend that we can therefore infer scienter because senior executives are presumed to know facts critical to a company's core operations. They also assert that we can infer scienter from Hillman and Dwyer's backgrounds in accounting. These arguments are attempts at an end-run around the requirement that plaintiffs set forth particularized facts to suggest that defendants acted knowingly or recklessly. Plaintiffs cannot rely on a "must have known" theory. *See* *Friedman v. Rayovac Corp.,* 295 F.Supp.2d 957, 995 (W.D.Wis.2003) (stating that the inference that officers and directors are aware of the corporation's "core business matters" relies on a "must have known" logic that the Seventh Circuit has rejected even under Rule 9(b)) (citing *DiLeo,* 901 F.2d at 629).

Plaintiffs' "motive" allegations are twofold: (1) defendants were motivated to misstate Bally's financial results in order to obtain financing, refinance outstanding debt, and complete acquisitions; and (2) the Individual Defendants were motivated to misstate financial results in order to earn bonuses contingent on financial performance and stock awards pursuant to incentive plans. We will first address these allegations in relation to the Individual Defendants and will then return to the first category of allegations in relation to Bally.[FN10]

> FN10. These allegations have no relevance to the scienter of E & Y.

Neither category of "motive" allegations is evidence of scienter as to the Individual Defendants. "Motives that are generally possessed by most corporate directors and officers do not suffice; instead, plaintiffs must assert a concrete and personal benefit to the individual defendants resulting from the fraud." *Kalnit v. Eichler,* 264 F.3d 131, 139 (2d Cir.2001). We cannot infer scienter on the part of the Individual Defendants merely from their general desire for their corporation to appear profitable and thereby obtain financing and engage in mergers or acquisitions. *See id.;* *Davis,* 385 F.Supp.2d at 714 (increased company buying power afforded by an overvalued stock is a broad motive that easily applies to a majority of corporate executives and is insufficient to establish scienter); *Malin v. IVAX Corp.,* 17 F.Supp.2d 1345, 1361 (S.D.Fla.1998) (motive of maintaining a stock price in order to facilitate mergers and acquisitions "can be ascribed to virtually all corporate officers and directors" and thus fails to raise a strong inference of scienter).

Regarding the motive to earn bonuses and awards, we agree with the view of numerous courts that these allegations are too common among corporations and their officers to be considered evidence of scienter. *See, e.g.,* *Abrams,* 292 F.3d at 434 ("Incentive compensation can hardly be the basis on which an allegation of fraud is predicated.... It does not follow that because executives have components of their compensation keyed to performance, one can infer fraudulent intent."); *Sandmire v. Alliant Energy Corp.,* 296 F.Supp.2d 950, 959 (W.D.Wis.2003) ("Motivations to keep stock prices high to increase personal salaries and to boost financial standing to gain regulatory approval are so common among corporations and their officers that allowing them to satisfy the scienter allegation requirement would be tantamount to eliminating it."). As the court in *Davis* observed:

> ***10** The complaint alleges that [defendants] shared certain motives to inflate the stock price-increased compensation for the officers, an ability to meet analyst expectations, and increased company buying power afforded by an overvalued stock. Just as these broad motives apply to [defendants], they easily apply to a majority of corporate executives. The desire to increase the value of a company and attain the benefits that result, such as meeting analyst expectations and reaping higher compensation, are basic motivations not only of fraud, but of running a successful corporation. Were courts to accept these motives as sufficient to establish *scienter,* most corporate executives would be subject to such allegations, and the heightened pleading requirements for these claims would be meaningless.

Davis, 385 F.Supp.2d at 714.

As for defendant Bally, some courts (largely in the Eastern District of Pennsylvania) have held that stock-based acquisitions that occurred at the time of alleged misrepresentations can support an inference of scienter in some circumstances. *See, e.g.,* *In re NUI Sec. Litig.,* 314 F.Supp.2d 388, 412 (D.N.J.2004); *Marra v.. Tel-Save Holdings, Inc.,* No.

Master File 98-3145, 1999 WL 317103, at *8-10 (E.D.Pa. May 18, 1999). We do not believe that these allegations give rise to a strong inference of scienter here. It is not alleged that the two acquisitions that were completed during the class period were strictly for stock only, as is the situation in most of the cases where such transactions have been held to give rise to an inference of scienter. Moreover, there are no allegations that any particular financial results were misstated in order to effectuate any particular acquisition. Instead, plaintiffs allege generally that defendants were motivated to misstate results in order to artificially inflate Bally stock, and that defendants then "took advantage of th[e] artificial inflation" to obtain financing and effectuate acquisitions. (CCAC ¶ 272.) These allegations, at most, give rise to only a very weak inference of scienter on the part of Bally.

A final allegation on which plaintiffs rely in support of scienter is that Bally violated its own internal accounting policies. This allegation is similar to the allegations of GAAP violations in that it only goes toward establishing that misstatements were made. Allegations that GAAP or Bally's internal accounting policies were violated do not establish that the misstatements were made with the requisite intent. *See In re BISYS Sec. Litig.,* 397 F.Supp.2d 430, 448 (S.D.N.Y.2005).

So, where do these allegations leave us with respect to each defendant? We will begin with the Individual Defendants-Hillman, Dwyer, and Toback. None of the allegations discussed *supra* have raised a strong inference of scienter with respect to them. In addition, there are no allegations of circumstances suggestive of scienter, such as large insider stock sales or specific meetings during which particular financial representations were discussed. Plaintiffs emphasize that we have to consider the allegations in their totality. This is indeed the correct standard, see *Makor Issues,* 437 F.3d at 603 ("[W]e will aggregate the allegations in the complaint to determine whether it creates a strong inference of scienter ...."), and it is the one that we are employing. Nonetheless, even under this standard, plaintiffs' allegations fall far short of adequately pleading scienter with respect to the Individual Defendants. The complaint relies largely on conclusory allegations, speculation, and a "must have known" approach. Plaintiffs have simply failed to allege with particularity facts giving rise to a strong inference that Hillman, Dwyer, or Toback acted with the required intent or recklessness.[FN11]

> FN11. We note that Hillman also argues that he is not responsible for statements made after his retirement on December 11, 2002. Plaintiffs concede that Hillman is not responsible for any statements made after his retirement. (Plaintiffs' Response to Bally Defs.' Mot. at 25 n. 10.)

***11** Plaintiffs contend, without explanation, that even if the complaint fails to allege scienter against the Individual Defendants, it still sufficiently alleges scienter against Bally. (Plaintiffs' Response to Bally Defs.' Mots. at 27 n. 14.) Plaintiffs argue that scienter on Bally's part can be alleged based on the "collective knowledge of its employees." (*Id.* at 12.) We disagree. The Seventh Circuit has expressed doubt about an "independent corporate scienter theory." *See Caterpillar, Inc. v. Great Am. Ins. Co.,* 62 F.3d 955, 963 (7th Cir.1995); *see also Higginbotham v. Baxter Int'l, Inc.,* Nos. 04 C 4909, 04 C 7906, 2005 WL 1272271, at *8 (N.D.Ill. May 25, 2005) (rejecting the theory and noting that the Fifth Circuit and the Ninth Circuit have also rejected it)."A corporation can only 'know' those things known by persons acting on its behalf." *Ong ex rel. Ong IRA v. Sears, Roebuck & Co.,* 388 F.Supp.2d 871, 901 n. 19 (N.D.Ill.2004). Plaintiffs have failed to allege facts giving rise to a strong inference that *anyone* acting for Bally had the requisite state of mind, let alone the Individual Defendants. In addition, as stated *supra,* Bally' s acquisitions that were partly paid for in stock give rise to only a very weak inference of scienter. In any event, even if we accepted plaintiffs' argument that "collective knowledge" allegations are sufficient, there is virtually nothing in the complaint suggesting with particularity what that "collective knowledge" was.

As for E & Y, it was Bally's outside auditor, and as applied to outside auditors, "recklessness means that the accounting firm practices amounted to no audit at all, or to an egregious refusal to see the obvious, or to investigate the doubtful, or that the accounting judgments which were made were such that no reasonable accountant would have made the same decisions if confronted with the same facts." *Chu,* 100 F.Supp.2d at 823 (internal quotation marks omitted). E & Y argues that the section of the complaint setting forth plaintiffs' principal scienter allegations fails to state any facts regarding E & Y and that the complaint fails to point to any "red flags" suggesting recklessness.

Plaintiffs first contend that we can infer scienter from the fact that the press release announcing the Audit Committee's findings stated that Bally believed that E & Y had made several errors in the course of its auditing work. (CCAC ¶ 16.) In plaintiffs' view, they are "entitled to an inference that the press release reveals conduct by E & Y that was at least reckless, if not fraudulent."(Plaintiffs' Response to E & Y's Mot. at 9.) Plaintiffs are incorrect. As discussed *supra,* possible accounting errors alone do not raise an inference of scienter. *See, e. g., Fidel,* 392 F.3d at 231 (holding that a subsequent revelation of the falsity of previous statements does not imply scienter by an outside auditor); *In re Ikon Office Solutions, Inc.,* 277 F.3d 658, 673 (3d Cir.2002) ("[T]he discovery of discrete errors after subjecting an audit to piercing scrutiny post-hoc does not, standing alone, support a finding of intentional deceit or of recklessness.").

***12** Aside from allegations about the characteristics of the restatement and Bally's violation of its internal accounting policies, which we have discussed and rejected *supra* as sufficient bases for an inference of scienter, the only other argument proffered by plaintiffs regarding E & Y's scienter is that E & Y was "indifferent" to red flags during its audits. (Plaintiffs' Response to E & Y's Mot. at 10-14.) In their response brief, plaintiffs list twelve red flags that "should have prompted E & Y to exercise greater professional skepticism during its audits."(*Id.* at 12-14.) The problem is that plaintiffs fail to describe these red flags in the complaint. Plaintiffs cite cases for the proposition that we may consider facts alleged in their brief if those facts are consistent with the complaint's allegations, but those cases are inapposite because they involved notice pleading, not fact pleading as required by the PSLRA.

For the sake of judicial economy, however, we will consider the twelve "red flag" items listed in plaintiffs' brief as if they had been included in the complaint.[FN12] Although allegations of obvious "red flags" or warning signs that financial reports are misstated can give rise to a strong inference of scienter in some circumstances, *see Chu,* 100 F.Supp.2d at 824, plaintiffs' allegations are insufficient to raise a strong inference that E & Y acted with scienter. Plaintiffs' "red flags" are largely reconstituted versions of their allegations couched in the context of the Audit Standards of the American Institute of Certified Public Accountants. Four items deal with what was "revealed" in the Audit Committee's investigation. The Audit Committee's findings involve hindsight; they do not shed light on what E & Y knew at the time of the audits. Therefore, they do not constitute red flags relevant to scienter. *See, e.g., Davis,* 385 F.Supp.2d at 713-14 (red flags cannot arise out of later discoveries).

> FN12. Plaintiffs have requested leave to amend the complaint in the event that defendants' motions are granted. Plaintiffs would undoubtedly amend the complaint to include the "red flag" allegations, and the scienter issue would arise again. Better to resolve it sooner than later and avoid duplication of efforts.

None of the remaining items raises a strong inference of scienter. Five items are problematic because they are not based on facts that are actually alleged. Plaintiffs assert that the following situations constitute "red flags": where "significant portions" of management's compensation are contingent upon achieving aggressive financial targets; where management has "significant" financial interests in the entity; where a company "needs" to obtain additional debt or equity to stay competitive; where a company has an "active" merger or acquisition calendar; and where a company has "unusually rapid growth or profitability." Plaintiffs have not alleged, though, that Bally's management had incentives or financial interests that were "significant" in that they were much larger than executives at comparable entities. Nor have plaintiffs alleged that Bally needed to obtain the financing it obtained or complete the acquisitions that it did in order to stay competitive, or that Bally's merger calendar was more active than comparable entities, or that Bally had unusually rapid growth compared to other companies. It is not evident that any of these five red flags actually existed on the facts that have been alleged.

***13** The three remaining purported "red flag" items are too weak to raise a strong inference of scienter. One is management's failure "to correct known reportable conditions on a timely basis."(Plaintiffs' Response to E & Y's Mot. at 14.) Plaintiffs contend that E & Y stated in 2004 that it had been aware of material weakness in "internal accounting control" for the years 2001-2003 and took that into account in performing its audits. We do not believe that it follows from this allegation that there was a failure to correct a "known reportable condition" on a timely basis. It is not even clear what constitutes a "known reportable condition."

The final two items are not even characterized by plaintiffs themselves as red flags. One is that Bally inadequately disclosed its accounting policies and therefore E & Y should have been alerted to the risk of fraud. The other is that each of the Individual Defendants worked for E & Y prior to joining Bally and that therefore E & Y should have exercised "increased audit skepticism." These items do not strike us as red flags; rather, they are risk factors."[S]o-called 'red flags', which should be deemed to have put a defendant on notice of alleged improprieties, must be closer to 'smoking guns' than mere warning signs." Nappier v. Pricewaterhouse Coopers LLP, 227 F.Supp.2d 263, 278 (D.N.J.2002) (citation and some internal quotation marks omitted). Plaintiffs have failed to identify any true red flags, which are "specific, highly suspicious" facts or circumstances available to E & Y at the time of its audits. Riggs Partners, LLC v. Hub Group, Inc., No. 02 C 1188, 2002 WL 31415721, at *9 (N.D.Ill. Oct. 25, 2002). E & Y argues that plaintiffs have attempted to "cherry-pick a handful of very generalized risk factors, label them as 'red flags,' and stitch them together to show scienter."(E & Y's Reply at 13.) We agree. Plaintiffs have failed to allege facts tending to show that E & Y acted with the requisite scienter.

Because plaintiffs have failed to allege particularized facts sufficient to give rise to a strong inference that any of the defendants acted with the requisite intent or recklessness, Count I of the consolidated class action complaint, the § 10(b) claim, will be dismissed. Count II, the § 20(a) "control person" claim against the Individual Defendants, will also be dismissed because if there is no actionable underlying violation of the securities laws, there can be no control person liability. *See* Sequel Capital, LLC v. Rothman, No. 03 C 678, 2003 WL 22757758, at *17 (N.D.Ill. Nov. 20, 2003); *In re Allscripts, Inc. Sec. Litig.*, No. 00 C 6796, 2001 WL 743411, at *12 (N.D. Ill. June 29, 2001).

Plaintiffs have requested leave to amend the complaint in the event of a dismissal. Plaintiffs will be granted leave to amend; therefore, the dismissal will be without prejudice.

B. ***Loss Causation***

We could have ended our discussion by stating that it is unnecessary to address defendants' loss causation arguments because we are dismissing on scienter grounds. But plaintiffs have requested, and we will grant, leave to amend the complaint. In light of the possibility of another motion to dismiss, it is useful to take up the loss causation issue now.

***14** Plaintiffs suing under the PSLRA must plead and prove that the defendant's purported fraudulent statement or omission was the cause of their loss. *See*15 U.S.C. § 78u-4(b)(4); *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 347 (2005). Pursuant to *Dura,* the complaint must provide defendants "with some indication of the loss and the causal connection that" plaintiffs have in mind. *Id.* The complaint in *Dura* alleged that the price of the stock plaintiffs had purchased was inflated because of defendants' misstatements, but not that the share price had fallen after the truth became known. The Supreme Court held that the complaint was insufficient because an inflated purchase price does not itself constitute or proximately cause economic loss. *Id.*

Here, as in *Dura,* it is alleged in the complaint that as a result of defendants' false and misleading statements, Bally stock traded at artificially inflated prices during the class period. (CCAC ¶¶ 274-79.) But what it also alleges distinguishes this case from *Dura:* that when the truth became known by virtue of the April 28, 2004 announcement, the price of Bally stock "fell precipitously" and, as a result, plaintiffs suffered economic loss. (CCAC ¶¶ 280-81.)

Defendants maintain that plaintiffs have failed to plead loss causation because the "truth" actually became known in an earlier announcement indicating that Bally was planning on issuing a restatement of certain financial results. Defendants also argue that the price of Bally stock had already greatly declined over the course of the class period and thus the announcement was not the cause of plaintiffs' loss. Defendants frame their position as a *Dura* argument, but in reality it goes to the merits of plaintiffs' case. The essence of defendants' arguments is that plaintiffs cannot *prove* loss causation. But that is not an appropriate consideration on a motion to dismiss. It is axiomatic that on a motion to dismiss, we accept as true all factual allegations in the complaint. *See* *Hentosh v. Herman M. Finch Univ. of Health Sciences*, 167 F.3d 1170, 1173 (7th Cir.1999). Plaintiffs have sufficiently alleged loss causation in accord with *Dura*, and that is all that is required of them at this juncture.

CONCLUSION

For the foregoing reasons, the following motions to dismiss the consolidated class action complaint are granted: (1) the motion of Lee S. Hillman; (2) the motion of John W. Dwyer; (3) the motion of Bally Total Fitness Holding Corporation and Paul A. Toback; and (4) the motion of Ernst & Young, LLP. The consolidated class action complaint is dismissed without prejudice.

Plaintiffs may file an amended consolidated class action complaint by August 14, 2006.

A status hearing is set for September 13, 2006, at 10:00 a.m.

N.D.Ill.,2006.
In re Bally Total Fitness Securities Litigation
Not Reported in F.Supp.2d, 2006 WL 3714708 (N.D.Ill.)

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Exhibit 14