UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF ILLINOIS

EASTERN DIVISION

LAWRENCE E. JAFFE PENSION PLAN, ON BEHALF OF ITSELF AND ALL OTHERS SIMILARLY SITUATED, Plaintiff, *- against -* HOUSEHOLD INTERNATIONAL, INC., ET AL., Defendants.	Lead Case No. 02-C-5893 (Consolidated) CLASS ACTION Judge Ronald A. Guzman Magistrate Judge Nan R. Nolan

MEMORANDUM OF LAW IN SUPPORT OF THE HOUSEHOLD DEFENDANTS' MOTION TO COMPEL RESPONSES TO DEFENDANTS' FOURTH SET OF INTERROGATORIES TO LEAD PLAINTIFFS

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This memorandum is respectfully submitted on behalf of Defendants Household International, Inc., Household Finance Corp., William F. Aldinger, David A. Schoenholz, Gary Gilmer and J.A. Vozar (collectively, "Household" or "Defendants") in support of the Household Defendants' Motion to Compel Responses to Defendants' Fourth Set of Interrogatories To Lead Plaintiffs (the "Interrogatories").[1]

INTRODUCTION

The close of fact discovery is now less than two months away and the time set by the Court for Plaintiffs' counsel to explain in detail their contentions in this securities fraud case has arrived. Unfortunately, instead of the expected responses, counsel provided only groundless objections to the Interrogatories that are the subject of this motion. Consistent with their practice, no actual responses were provided at all. These Interrogatories seek no less than the identification of the facts that Plaintiffs allege were misrepresented to and/or omitted from the market. This information is not merely centrally relevant to the litigation but in fact the cornerstone of Plaintiffs' allegations of securities fraud. Plaintiffs' counsel's refusal to provide non-frivolous responses is indefensible.

The Securities and Exchange Act of 1934 specifically states that to succeed on any claim of securities fraud a plaintiff must prove that defendants either made a material misrepresentation, or omitted information that they had a duty to disclose. It is discovery of the specific details of these contentions that Defendants seek through the Interrogatories.

Plaintiffs' objections spuriously assert that that identifying each alleged misrepresentation is "unduly burdensome" and that identifying each alleged omission would involve a "counterfactual hypothetical question." Such objections are wholly without merit. It cannot be an undue burden for Plaintiffs to disclose the specifics upon which their claims of securities fraud are founded because their burden at any trial of this action would be exactly that — and this Court has already ruled that the time for Plaintiffs to reveal their contentions is at hand. Each alleged misrepresentation and

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[1] "Interrogatories" refers to Household Defendants' Fourth Set of Interrogatories to Lead Plaintiffs served on October 31, 2006. (See Affidavit of David R. Owen dated December 22, 2006 ("Owen Aff."), Ex. 5.)

omission will be the focus of summary judgment practice and, if necessary, trial. Plaintiffs' refusal to identify them specifically is nothing less than an improper effort to evade this scrutiny and set the stage for a hoped-for trial by ambush.

These dilatory objections also reflect Plaintiffs' pattern of refusing to provide any information until directly ordered by the Court to do so.[2] The Plaintiffs themselves have almost no documents and Defendants have been denied the right to take any depositions. Interrogatories are the only means by which Defendants can affirmatively discover the specifics of Class counsel's allegations and begin to prepare a defense. Yet after years of responding to their voluminous and ever expanding discovery demands, Defendants have been afforded only a few weeks to gain this information and conduct any necessary follow-up before the close of fact discovery. By unjustifiably refusing to respond to contention interrogatories absent a court order, Plaintiffs have deliberately hindered Defendants' ability to serve any additional requests to follow-up the responses that should have been forthcoming weeks ago. Plaintiffs are well aware that even baseless objections will delay this process at least another month or so. This conduct and the burdens it imposes should not be rewarded.

ARGUMENT

"The Federal Rules of Civil Procedure contemplate liberal discovery, and 'relevancy' under Rule 26 is extremely broad." *For Your Ease Only, Inc.* v. *Calgon Carbon Corp.*, No. 02 C 7345, 2003 U.S. Dist. LEXIS 20267, at *4 (N.D. Ill. Nov. 10, 2003) (Nolan, M.J.). "Under Fed. R. Civ. P. 26(b)(1) 'parties may obtain discovery regarding any matter, not privileged, that is relevant to the claim or defense of any party.'" *Trading Technologies International, Inc.* v. *eSpeed, Inc.*, No. 04 C 5312, 2005 U.S. Dist. LEXIS 10686, at *2 (N.D. Ill. Apr. 28, 2005) (citation omitted). Interrogatories that seek to clarify the basis for or scope of an adversary's legal claims and require the answering party to commit to a position and give factual support for that position are appropriate and require a response. *Ziemack* v. *Centel Corp.*, No. 92 C 3551, 1995 WL 729295, at *2 (N.D. Ill. Dec. 7, 1995).

[2] Even the direct order of the Court has failed to move Plaintiffs to participate in discovery. As the Court may remember, despite the Court's September 19, 2006 Order instructing Plaintiffs to respond to Defendants third set of interrogatories on December 1, 2006, Plaintiffs still refused to provide any responses.

The Interrogatories at issue on this motion ask Plaintiffs to provide the most basic facts regarding their claims of securities fraud—identification of each misrepresentation and omission allegedly made by Defendants.[3]

A. Plaintiffs Must Identify Which Statements Were Misrepresentation and What Information Was Withheld from the Market (Interrogatories No. 36-43)[4]

The foundation of every fraud-on-the-market securities fraud claim is the allegation that the defendant lied to the public. A plaintiff's claim will fail unless he or she successfully pleads and proves that the defendant either affirmatively misrepresented specific information to the market or that the defendant withheld information that they had a duty to disclose. *Basic Inc.* v. *Levinson*, 485 U.S. 224, 231-232 (1988); *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 474-75 (1977).

"[F]raudulent misrepresentations must be separately identified. An allegation of fraudulent misrepresentation is not sufficient if it merely states that misrepresentations were made." *Spicer* v. *Chicago Board Options Exchange, Inc.*, No. 88 C 2139, 1990 U.S. Dist. LEXIS 14469, at *25-31 (N.D. Ill. Oct. 24, 1990) (dismissing all allegation of fraud by misrepresentation in view of Plaintiffs' failure to identify "a single false or misleading statement" and analyzing each of the three alleged omissions separately.). Correspondingly, "[a]n allegation of an omission alleges what it is that allegedly was not said". *Id*. at 31; *see Spatz* v. *Borenstein*, 513 F. Supp. 571, 578-80 (N.D. Ill. 1981) (on a motion for summary judgment, analyzing sentence by sentence each alleged "affirmative misrepresentation" and each alleged omission (e.g. that defendant "failed to disclose that 25 of 562 units in the Laurel Glen apartment complex were 'below grade' and thus uninhabitable")).

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[3] As a result of the teleconference meet and confer held on December 18, 2006, Plaintiffs stated that they would supplement their responses to Interrogatories No. 41-43 in the event that their objections before Judge Guzman are denied. Given that Plaintiffs continue to rely on counting objections to Judge Guzman, refuse to state that their supplement would completely and substantively respond without objection to Defendants requests, and the shortness of time left in discovery, this motion will address Plaintiffs' first set of responses to the Interrogatories, [the only responses presently available].

[4] Plaintiffs have renumbered Defendants' interrogatories despite the Court's September 19, 2006 Order rejecting Plaintiffs' numbering. Reference herein will always be to Defendants' original numbering unless otherwise stated.

Misrepresentations and omissions are more than simply the origin of every securities fraud litigation. Their relevance pervades a 10(b) action, touching upon every element of the fraud claim. "To prevail on such a claim, a plaintiff must demonstrate that the defendant made a material misrepresentation or omission with scienter in connection with the purchase or sale of securities, that the plaintiff reasonably relied on the misrepresentation, and that the plaintiff suffered economic loss which was caused by the misrepresentation." *Ray* v. *Citigroup Global Markets, Inc.*, No. 03 C 3157, 2005 U.S. Dist. LEXIS 24419, at *5 (N.D. Ill. Oct. 18, 2005). Failure to prove any one of these elements with respect to any misrepresentation or omission will preclude a plaintiff's recovery for that misrepresentation or omission. *See, e.g., Searls* v. *Glasser*, 64 F.3d 1061, 1066 (7th Cir. 1995) (granting defendants' motion for summary judgment, analyzing each alleged misrepresentation and holding, *inter alia*, that "the phrase 'recession-resistant' is simply too vague to constitute a material statement of fact" because "[i]t is a promotional phrase used to champion the company but is devoid of any substantive information"); *Central Laborers' Pension Fund* v. *Sirva, Inc.*, No. 04 C 7644, 2006 U.S. Dist. LEXIS 73375 (N.D. Ill. Sept. 22, 2006) (Guzman, J.) (analyzing materiality and scienter with respect to each alleged misrepresentation and omission); *Ray*, 2005 U.S. Dist. LEXIS 24419, at *5 (granting defendants' motion for summary judgment on loss causation where defendants' stock moved in tandem with the market and did not significantly decline following the revelation of the alleged misrepresentations).

In this case, the particulars of the misrepresentations and fraudulent omissions alleged by Plaintiffs here are particularly significant because very similar claims have been dismissed for lack of any duty to make the allegedly required disclosure. *See, e.g., In re Marsh & McLennan Cos., Inc. Securities Litigation*, No. 04 Civ. 8144, 2006 U.S. Dist. LEXIS 49525, at *35 (S.D.N.Y. July 19, 2006) (granting defendants' motion to dismiss plaintiffs' claim that defendants should have disclosed they maximized contingent commission revenue through steering and bid manipulation, stating "[b]ecause the securities laws do not impose a general duty to disclose corporate mismanagement or uncharged criminal conduct, the allegations that MMC misstated its earnings merely by failing to disclose the misconduct . . . is not actionable") ("*Marsh & McLennan*"). The recent opinion in *Marsh & McLennan* goes to great lengths to distinguish and reject alleged misrepresentations of various types similar to those vaguely asserted here. *See id*. Consistent with this analysis, Defendants are entitled to Plaintiffs' explanation of exactly what misrepresentations or omissions they will try to prove here.

Defendants propounded Interrogatories No. 36-43 to obtain an identification of which statements that Plaintiffs contend were affirmative misrepresentations and what information Plaintiffs contend should have been disclosed to the market. Unable to dispute the obvious relevance of this information, Plaintiffs assert without support that identifying the alleged misrepresentations would be "unduly burdensome." (*See, e.g.*, Owen Aff., Ex. 7 at 10). Such unsupported objections must be overruled. "If the discovery appears relevant, the party objecting to the discovery request bears the burden of showing why that request is improper." *Trading Technologies International, Inc.* v. *eSpeed, Inc.*, No. 04 C 5312, 2005 U.S. Dist. LEXIS 10686, at *2 (N.D. Ill. Apr. 28, 2005).

Even passing the fact that Plaintiffs never consider burden to be an obstacle to the discovery they initiate, a "[n]aked assertion that the requested discovery is 'burdensome', without a 'specific showing' of the burden involved, is insufficient to preserve the objection." *Clark Equipment Co.* v. *Lift Parts Manufacturing. Co.*, No. 82 C 4585, 1985 U.S. Dist. LEXIS 15457, at *17 (N.D. Ill. Sept. 30, 1985) (granting motion to compel responses to contention interrogatories); *Rusty Jones, Inc.* v. *Beatrice Co.*, No. 89 C 7381, 1990 U.S. Dist. LEXIS 12116, at *4 (N.D. Ill. Sept. 11,1990) (granting defendant's motion to compel responses to contention interrogatories over burden objection). As this Court has held, the very purpose of contention interrogatories is "to clarify the basis for or scope of an adversary's legal claims." (November 10, 2005 Order of Magistrate Judge Nan R. Nolan (Owen Aff., Ex. 3 at 3)). Since the existence of misrepresentations and omissions is a necessary element of Plaintiffs' claims, Plaintiff must be required to answer. *Bell* v. *Woodward Governor Co.*, No. 03 C 50190, 2005 U.S. Dist. LEXIS 19602, at *5-6 (N.D. Ill. Sept. 8, 2005) ("[T]his court expects to find, at least, in answers to contention interrogatories those facts that a party intends to offer to prove their case-in-chief. . .."); *EMC Corp.* v. *Storage Technology Corp.*, 921 F. Supp. 1261, 1264 (D. Del. 1996) ("[C]ourts have held that where the allegations are pled with particularity, the parties may then rely upon interrogatories for specific details." (citing cases)).

In fact, the details of the alleged misrepresentations and omissions are precisely the type of information contention interrogatories are expected to discover. *See Towers Financial Corp.* v. *Soloman*, 126 F.R.D. 531, 536 (N.D. Ill. 1989) (denying motion to dismiss for failure to plead the details of each alleged misrepresentations and omissions and noting that "this information is the type of evidentiary detail more properly required to be disclosed during discovery"); *Ivers* v. *Keene Cor-*

p., 780 F. Supp. 185, 190 (S.D.N.Y. 1991) ("Although the Complaint does not specify exactly where and how the alleged misrepresentations were made, this information is obtainable through interrogatories or depositions.").[5]

Plaintiffs also object to Interrogatories No. 36-40—which seek identification of the facts that Plaintiffs claim were omitted from the market, claiming they pose "counterfactual hypothetical questions." This objection is also without merit. First, Defendants' Interrogatories are not "counterfactual" or "hypothetical". Defendants are not asking Plaintiffs to speculate as to what would have happened under a different set of facts. Rather, Defendants are asking Plaintiffs to state their contentions—what information they allege was withheld from the market that Defendants had a duty to disclose.[6] For example, Interrogatory No. 36 states:

> Identify the particular facts Plaintiffs contend would have been necessary and sufficient, if disclosed by Defendants, to inform the market that Household was engaged in "Illegal Predatory Lending Practices" as alleged and set forth in Part VI.A of the Complaint. (AC ¶¶ 50-106).

(Owen Aff., Ex. 5 at 2).

Plaintiffs' fraud allegation is based on the premise that Defendants should have disclosed particular things to the market differently from how they actually did. Defendants are entitled to know what those "things" are and what they allegedly "should have said" instead. *Spicer*, 1990 U.S. Dist. LEXIS 14469, at **25-31 ("An allegation of an omission alleges what it is that allegedly

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5 Moreover, it is not overly burdensome in a case of this size to require Plaintiffs to set forth the specific statements and/or omissions that they allege gave rise to their claims instead of forcing Defendants to hunt through the 400 paragraph Complaint and guess which statements Plaintiffs allege are actionable. *Rusty Jones, Inc.*, 1990 U.S. Dist. LEXIS 12116, at *4 (finding in a case where plaintiff's complaint consisted of over 142 paragraphs and plaintiffs were demanding damages in excess of one hundred million dollars "given the number of allegations in the complaint and defendant's potential liability, the [contention] interrogatories are not overly burdensome").

6 Plaintiffs' remaining objection is that Defendants did not define the terms "products", "restructure policies and practices", and "accurately informed the market." (Owen Aff., Ex. 7 at 15,17). Plaintiffs clearly have an understanding of these terms. The Complaint repeatedly alleges that "Defendants manipulated Household's credit quality numbers by improperly 'reaging' or 'restructuring' delinquent accounts" (AC ¶¶ 2,117,217), using the terms restructure and reage are referenced in at least 12 and 40 paragraphs, respectively. Likewise, "market" is cited in at least 14 paragraphs. Defendants cannot be required to define the terms Plaintiffs use in their allegations in order for Plaintiffs to respond to questions about them.

was not said. . ..."); *see, e.g., In re Marsh & McLennan Cos., Inc. Securities Litigation*, 2006 U.S. Dist. LEXIS 49525, at *39 (granting defendants' motion to dismiss the allegation that defendants failed to disclose the fact of disputed practices or the future risk that those practices could be discontinued as a result of litigation, the court held that "there is no requirement 'to make disclosures predicting such litigation,' absent an allegation that the litigation 'was substantially certain to occur during the relevant period'") (citation omitted).

Receiving complete and substantive good faith responses to these contention interrogatories is essential to Defendants' ability to prepare for summary judgment and trial (if any). "Answers to such interrogatories are useful because they, amongst other things, aid the propounding party in 'pinning down' a party's position and determining the proof required to rebut the party's position." *Bell*, 2005 U.S. Dist. LEXIS 19602, at *5-6 and "allow parties to prepare for trial by narrowing the scope of the issues and minimizing the possibility of surprise at trial" *Id*. at 6. Plaintiffs' baseless refusal to identify the very misrepresentations and omissions which spawned this litigation is nothing more than bad faith obstruction and they must be compelled to substantively respond.

B. The Court Has Already Determined That Plaintiffs Must Provide Facts Supporting Their Claims of Loss Causation (Interrogatory No. 35)

Plaintiffs have previously stated that the first day on which the "truth" of Household's alleged fraud was revealed to the market was August 14, 2002. *See* Lead Plaintiffs' Response to Household Defendants' Motion Based on the Supreme Court's Decision in *Dura Pharmaceuticals, Inc. v. Broudo* filed August 18, 2005, filed August 18, 2005, excerpted. (Owen Aff., Ex. 1) ("*Dura* Brief"). In their *Dura* Brief, Plaintiffs represented to Judge Guzman the following:

> The Complaint also pleads the requisite 'causal connection' between defendants' scheme and plaintiffs' economic loss: On August 14, 2002, investors began to learn of the true facts about Household's financial and operating condition concealed by the multi-component fraud scheme

(*Id*. at 10).[7] Seeking factual support for this statement, Interrogatory No. 35 states:

[7] In their *Dura* Brief Plaintiffs stated that there was only one "multi-component fraud scheme." It is this "fraud scheme" that Plaintiffs claim first began to be revealed to the market on August 14, 2002. (*Dura* Brief, Owen Aff., Ex. 1 at 9-10).

> Identify all documents and alleged facts that Plaintiffs contend support their statement in Plaintiffs' *Dura* Brief that 'August 14, 2002' was the date that 'investors began to learn of the true facts about Household's financial and operating condition concealed by the multi-component fraud scheme.' *Dura* Brief at 10.

(Owen Aff., Ex. 5 at 1-2)[8]. Plaintiffs refused to respond. However, they provided absolutely no reason why this information cannot or should not be discovered. Plaintiffs' baseless objection is all the more offensive since this Court has already held that information relating to loss causation and Plaintiffs' contentions in their *Dura* Brief is relevant and discoverable. (*See* September 19, 2006 Order of Magistrate Judge Nan R. Nolan (Owen Aff., Ex. 4 at 2-3)). In its September 19, 2006 Order, the Court noted that Plaintiffs invoked the August 14, 2002 date in both the *Dura* Brief and the *Foss* Brief and held that the former was relevant while the latter was not. (*Id*. at 3) ("To be sure, Defendants' Interrogatory No. 29 is inartfully drafted to the extent it seeks information based ***solely*** on a statement made in [the *Foss* Brief]".) (emphasis added). In ordering Plaintiffs to answer all of Defendants' interrogatories that were "not limited to statements made in the *Foss* Brief" (*id*), the court stated "[s]ignificantly, Plaintiffs also raised the August 14, 2002 date in their *Dura* Brief, which had nothing to do with inquiry notice and instead addressed the pleading requirements for loss causation. . . . The court agrees that facts and documents setting forth the disclosures that purportedly put the market on notice of Household's alleged fraud, as requested in Interrogatory Nos. 30-33, are relevant and discoverable." (*Id.* at 3-4).

Defendants are entitled to this information, which is not merely relevant to a securities fraud case, but is integral to its outcome. To succeed in this litigation, Plaintiffs must prove "loss causation." *Dura Pharmaceuticals, Inc.* v. *Broudo*, 544 U.S. 336, 342 (2005) ("*Dura*"). To demonstrate loss causation Plaintiffs would have to prove that the "share price fell significantly after the truth became known." *Id*. at 347. In *Dura,* the Supreme Court held that proving purchase price inflation alone was inadequate to satisfy loss causation. *Id*. at 346-348. Instead, the fraud must also be-

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[8] Plaintiffs made a similar statement in Lead Plaintiffs' Response to Household Defendants' Motion Pursuant to the Seventh Circuit's Decision in *Foss* v. *Bear, Stearns Co.,* filed August 18, 2005, excerpted. (See Owen Aff., Ex. 2) filed the same day, stating that August 14, 2002 was the "earliest date that plaintiffs could have discovered the essential facts underlying defendants' fraud" for the purposes of inquiry notice. (*Id*. at 4).

come known to the market at some point and the stock price must significantly decline as a result, foreclosing recovery for any declines in stock price occurring prior to the corrective disclosure. *See id*. at 342-343. The Supreme Court reasoned:

> "For one thing, as a matter of pure logic, at the moment the transaction takes place, the plaintiff has suffered no loss; the inflated purchase payment is offset by ownership of a share that *at that instant* possesses equivalent value. Moreover, the logical link between the inflated share purchase price and any later economic loss is not invariably strong. Shares are normally purchased with an eye toward a later sale. But if, say, the purchaser sells the shares quickly before the relevant truth begins to leak out, the misrepresentation will not have led to any loss."

Id. at 342 (emphasis in original). "Thus to establish loss causation, a plaintiff must allege . . . that the misstatement or omission concealed something from the market that, *when disclosed,* negatively affected the value of the security." *Lentell* v. *Merrill Lynch & Co*., 396 F.3d 161, 173 (2d Cir. 2005) (emphasis added) (citations and internal quotation marks omitted). Simply put, if "plaintiffs do not allege that the scheme was ever disclosed, they fail to allege loss causation." *In re Initial Public Offering Securities Litigation*, 399 F. Supp. 2d 261, 266 (S.D.N.Y. 2005). Courts continue to echo the significance of *Dura* and the importance of the revelation of the "truth" to a plaintiff's securities fraud claim. Indeed, as recently as October, this district has held that "the economic loss occurs upon the decline in the value of the security after a defendant's ***corrective disclosures***. Because of the loss causation requirement, the Plaintiffs must then tie that decline to the disclosure." *Ong* v. *Sears, Roebuck & Co.*, No. 03 C 4142, 2006 U.S. Dist. LEXIS 80294, at *65-66 (N.D. Ill. Oct. 18, 2006) (emphasis added).

Having affirmatively suggested to the Court in their *Dura* Brief that August 14, 2002 was the first day that investors "began to learn of the true facts" regarding the alleged schemes, Plaintiffs cannot now refuse to provide Defendants with the basis for that assertion, especially since the Court relied on this statement in finding that Plaintiffs adequately pled loss causation. *See Feldman* v. *American Memorial Life Insurance Co.*, 196 F.3d 783, 791 (7th Cir. 1999) (Courts "cannot permit litigants to adopt an alternate story each time it advantages them to change the facts.").[9] Defendants

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[9] In addition to the *Dura* Brief and the *Foss* Brief, Plaintiffs made a similar assertion in the Complaint. ("[i]t was not until mid-2002 that investors began to learn of the true facts about Household's financial and operating condition." (AC ¶ 5)). Indeed, Plaintiffs continue to champion this position in their mo-

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are entitled to know the basis for Plaintiffs' factual representations about the level of information available to the market on August 14, 2002, as requested in Interrogatory 35.

CONCLUSION

For the foregoing reasons, Defendants respectfully request that Defendants' motion to compel be granted and that Plaintiffs be ordered to respond forthwith to Interrogatories No. 35-43.

Dated: December 22, 2006
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tions to the Court. Last month, Plaintiffs argued that as of July 1, 2002 "[t]here are no objective facts as to why Household feared litigation from these [] states . . . Nor is there any objective support for the concern that class action lawyers would bring 'similar claims' against defendants." (The Class' Reply in Support of Motion to Compel Production of All Documents Pertaining to Household's Consultation With Ernst & Young LLP, filed November 17, 2006, excerpted. (Owen Aff., Ex. 6 at 8).