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

REPLY MEMORANDUM OF LAW OF THE HOUSEHOLD DEFENDANTS IN SUPPORT OF THE PRIVILEGED NATURE OF THE ERNST & YOUNG COMPLIANCE ENGAGEMENT WORK PAPERS

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Defendants Household International, Inc. ("Household"), Household Finance Corporation, William F. Aldinger, David A. Schoenholz, Gary Gilman and J.A. Vozar (collectively, the "The Household Defendants" or "Defendants") submit this Reply Memorandum of Law to respond to several of the arguments made by Plaintiffs in their May 11, 2007 Memorandum of Law in Support of Production of the Work Papers Created by Ernst & Young LLP and Draft Report ("Pls. Mem."), including Plaintiffs' new and frivolous assertion that E&Y's draft report to Household's General Counsel is not privileged.

PRELIMINARY STATEMENT

Plaintiffs' Memorandum is striking, and ultimately self-defeating, in the extreme position it advocates — that *none* of the output of E&Y's Compliance Engagement, including a draft final report to Household's General Counsel, is privileged. As Defendants demonstrated in their initial Memorandum, this assertion flies in the face of the relevant facts and the applicable law, and cannot be reconciled with the explicit prior rulings of this Court.

Plaintiffs continue to ignore the implications of this Court's December 6, 2006 ruling that the July 2002 E&Y Compliance Engagement was a privileged retention. Their position that not a single page of E&Y's output is privileged would require reversal of already-affirmed key findings, including:

- "It is clear from the Compliance Engagement that E&Y was acting as an agent of Household's General Counsel's office."
- "Both Household & E&Y understood that the engagement was to assist in-house counsel in providing legal advice regarding pending or anticipated litigation."
- The court is satisfied, however, that Defendants retained E&Y to conduct complex quantitative analyses and extensive information gathering that was beyond Household counsel's resources and abilities, but was uniquely within E&Y's qualifications."

(Slip Opinion at 8-9, affirmed by Judge Guzman's February 1, 2007 opinion)

Instead of grappling with these findings in the context of the subject work papers and draft report, Plaintiffs proceed on the fiction that it is Defendants' burden to "establish [ ] that these documents reflect legal advice" (Pls. Mem. at 1). This argument perpetuates the same logical fallacy that the Household Defendants highlighted in their May 4 Memorandum ("Def. Mem."). While it is true that a document conveying legal advice in a "to/from" written format is generally privileged, Plaintiffs cannot substantiate their overly narrow and unfounded assumption that a document that does not conform to that model is not entitled to protection. Indeed, Plaintiffs can advance their artificially narrow standard only by ignoring (i) the character and purpose of the documents actually at issue here and the context in which they were created (*see* Def. Mem. at 5-7 and the Robin and Keller Affidavits attached as Exs. A-C), and (ii) the extensive body of case law presented in Defendants' Memorandum to the effect that the compilation and analysis of material by a company's accountant to assist the company's lawyer in rendering legal advice is privileged (*see* Def. Mem. at 7-11 and cases cited therein).

A. The Compliance Engagement Draft Report And Work Papers Are Privileged

If Household's General Counsel's Office had possessed the "resources and abilities" to conduct the Compliance Engagement within its own office, Plaintiffs would have to concede, based on authority they cite in their Memorandum, that the "complex quantitative analyses and extensive information gathering" that was necessary to be able to advise Mr. Robin, the General Counsel, would be privileged. In *Stafford Trading, Inc.* v. *Lovely*, No. 05-C-4868, 2007 U.S. Dist. LEXIS 13062 (N.D. Ill. Feb. 22, 2007), a case relied on by Plaintiffs (Pls. Mem. at 9, 10, 13), Magistrate Judge Keys agreed with the analysis by Judge Denlow in *McCook Metals L.L.C.* v. *Alcoa, Inc.*, 192 F.R.D. 242, 255 (N.D. Ill. 2000), that "although communications between in-house counsel are not communications directly to or from the client, it appears implicit in present day litigation with multiple attorneys required for proper representation that attorneys must be allowed to confer with each other regarding the repre-

sentation of a client on a privileged basis in the same way that clients must be able to discuss the advice of counsel amongst themselves on a privileged basis." (*Id.* at *22-23)

There is no substantive difference in Mr. Robin's relying on attorneys on his staff in the General Counsel's office, which was held to be within the attorney-client privilege in *Stafford* and *McCook Metals*, and his actual reliance on E&Y, which this Court found to be acting as Mr. Robin's agent in carrying out the privileged Compliance Engagement. Instead of relying on other lawyers or personnel in the General Counsel's Office, Mr. Robin relied on E&Y because, as the Court also found, his Office did not have the requisite "abilities or resources" to conduct the "complex quantitative analyses and extensive information gathering" that would be required by the Compliance Engagement. (Dec. 6 Order at 9) As a result, the work done by E&Y pursuant to the Compliance Engagement, *i.e.*, the work papers it created and the draft report it prepared, are privileged to the same extent as if E&Y had been a group of lawyers on Mr. Robin's staff.

1. The January 2004 Draft Report is Privileged

During the April 12, 2007 telephone status conference, after reviewing E&Y's draft final report *in camera*, the Court said that Plaintiffs "are not getting the report," *i.e.*, it is protected by the attorney-client privilege (4/12/07 Transcript at 33, attached hereto at Tab A.) Although that conclusion is indisputably correct, Plaintiffs have come up with a handful of meritless grounds to argue that the draft report — prepared and used to report and discuss the findings of the privileged Compliance Engagement — is somehow not privileged.

Plaintiffs first assert incorrectly that the draft report was never provided to anyone. They derive this supposed insight from the fact that Defendants' privilege log entry for the report initially did not contain a "to" or "from" line on the document, and from the allegation that Mr. Keller's April 24, 2007 Affidavit (his initial Affidavit) "does not state this draft report was prepared with the requisite intent of sharing it." (Pls. Mem. at 12-13) These objections are frivolous at best. As Plaintiffs well know from the April 24, 2007 Keller Affidavit, Mr. Keller specifically confirmed in paragraph 20: "This draft report was provided to

Household's Office of General Counsel on or about January 26, 2004. E&Y representatives met with Household representatives, including Mr. Robin and other lawyers for Household, to discuss the draft report." In view of this information, on May 14, 2007, Defendants corrected the "N/A" designation in the recipient column of their privilege log entry as to the January 2004 draft report to indicate that the report was received by, among others, Mr. Robin.[1]

Plaintiffs also ignore that one of the purposes of the privileged Compliance Engagement was to have E&Y prepare a report of its work and findings to be shared with Household. The engagement letter for the July 1, 2002 Compliance Engagement says, in the very first paragraph, that E&Y is "to prepare a report describing the work performed and related findings and recommendations." The report then is defined in the Engagement Letter as "the "Work Product" of the Engagement and the Letter says that the addressees of the Engagement Letter, Kenneth J. Robin, Household's General Counsel and Kathleen Curtin of Household's General Counsel's Office, "will be utilizing the Work Product [*i.e.*, the report] in order to provide legal advice to your client, Household, in your capacity as General Counsel." In view of this explicit language on the first page of the Engagement Letter, and Mr. Keller's sworn confirmation that E&Y shared and discussed the draft report with Household's General Counsel, Plaintiffs' argument that the draft report is not privileged is wholly without merit.

2. E&Y's Work Papers Are Privileged

As the draft report is privileged, it follows that the work papers comprising and reflecting the analysis summarized in the privileged draft report are likewise protected from disclosure (other than the few work papers dated prior to October 12, 2002 that, according to the Court's application of *Garner,* is not privileged vis-a-vis Plaintiffs). Plaintiffs fail

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[1] Plaintiffs also claim that the report is not privileged because it did not provide "legal advice," but only the "[i]dentification of overcharges and refunds." (Pls. Mem. at 13) This argument is foreclosed by the Court's December 6, 2006 ruling that E&Y was acting as agent for Mr. Robin to assist him in providing legal advice to the Company.

in their attempts to distinguish *United States v. Kovel*, 296 F.2d 918 (2d Cir. 1961) and its progeny. For example, Plaintiffs repeatedly refer to the E&Y work papers as nothing more than "memos to file" (Pls. Mem. at 7), and cite to cases that have held that documents correctly characterized as such are not protected by the attorney-client privilege. The rationale for not affording attorney-client protection to such documents is that a genuine "memo to file," as the words indicate, is not intended to be communicated to the client or to another attorney. However, this is not the case with the E&Y work papers. *All* of E&Y's Compliance Engagement work was performed with the objective, as stated in the July 2002 Engagement Letter, of preparing a report to Household's General Counsel. As Mr. Keller's Affidavit confirms, E&Y provided the January 2004 draft report to Household, and all of the underlying work papers were created as integral parts of the process of organizing and analyzing selected information for use by Household's General Counsel in rendering legal advice. It would make no sense to recognize that the summary report that culminated this process is privileged while allowing disclosure of the underlying ingredients of this report.

Plaintiffs' arguments to the contrary rely on their simplistic and discredited notion that attorney-client privilege protects only documents containing "to/from" designations on their face (*but see* pp. 7-11 of Defendants' Memorandum and cases cited therein) and on cases bearing no factual similarity to the matter at hand. For example, in *Stafford, supra,* the court declined to treat as privileged a memorandum prepared by an attorney for her own use in her work on a particular question. The E&Y work papers are the very antithesis of such a "memo to file." They were not prepared by Mr. Keller or one of his E&Y colleagues (such as Mr. Bianucci) for his own use, but were intended from the outset to provide the underlying analysis that would be — and was — summarized in E&Y's eventual report to Household. Even during the implementation of the Compliance Engagement, E&Y's analyses were not stuck in a drawer for its own reference, but rather were the subject of regular reporting and discussion with Household's attorneys, at meetings that averaged one per month throughout the Engagement. (Supp. Keller Afft. ¶ 18)

Plaintiffs further contend that the Court's April 27, 2007 Order requires Defendants to produce all documents dated within the Class Period from *all* of the 390 boxes of E&Y work papers. (Pls. Mem. at 1, 7) That is not a fair reading of the Order, which requires the production only of work papers in the 110 boxes of logged work papers that are dated prior to October 12, 2002. Defendants complied with that Order on May 14 and 15, 2007. The work papers in the remaining 280 boxes — the preliminary data sampling and data validation work undertaken by E&Y — remain protected from disclosure pending the Court's further instructions after application of the parties' protocol for sampling a subset of those 280 boxes of work papers. Pursuant to the Court approved protocol regarding this separate category, the Court currently has 21 boxes in chambers for *in camera* review.[2]

Plaintiffs also repeat their claim that the log "improperly lumps groups of documents together as single entries" (Pl. Mem. at 4). As Mr. Keller explained in his Affidavits, however, by virtue of the nature of the work papers created by E&Y, an individual analysis or review may contain more than a single page or several pages. Each entry on the privilege log reflects Defendants' good faith attempts to log discrete "documents" that will be meaningful to both Plaintiffs and the Court. This approach resulted in a privilege log that totaled 215 pages, covered 110 boxes of work papers, and contained 1,459 individual entries. The Court commented during the April 27 status conference that its *in camera* review of the documents summarized in a number of entries on Defendants' E&Y work papers privilege log demonstrated that the entries accurately reflected the documents at issue.

Plaintiffs' argument also ignores relevant authority, such as *SEC* v. *Thrasher*, 1996 U.S. Dist. LEXIS 3327 (S.D.N.Y. Mar. 19, 1996) (cited at page 11 of our opening brief), in which the court allowed the proponent of the attorney-client privilege to provide summaries of the documents by category when "the files in question are voluminous" and "a

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[2] Pursuant to the Court's May 22, 2007 Minute Order, the Household Defendants are compiling a log of those 21 boxes of documents to be completed by Tuesday, May 29, 2007.

document-by-document listing would be a long and fairly expensive project for counsel to undertake" (*Id.* at *3). While both of these conditions are satisfied with respect to the E&Y work papers, Defendants did not log documents by "category," but in most instances logged by discrete folders of related, integrated material that were organized as such in the boxes in question.

Defendants believe that the privilege log of the 110 boxes of E&Y's work papers and the Court's ongoing *in camera* review of a sample of those logged documents will confirm Defendants' representations about the privileged nature of those materials. Defendants likewise believe that the Court will conclude from its *in camera* review of the 21 boxes of E&Y's preliminary data validation and data sampling work papers that the documents in the remaining 280 boxes from this category need not be placed on a privilege log and need not be reviewed for the production of pre-October 12, 2002 documents, as the burden of logging or producing these documents at this late stage in the proceedings would far outweigh any marginal relevance of these preliminary data testing documents.[3]

B. Plaintiffs Have Not Overcome Work Product Protection for the Work Papers

Plaintiffs' Memorandum fails to provide any substantive response to Defendants' argument (at pp. 12-15 of their Memorandum) that Plaintiffs have not overcome the work product protection for the E&Y work papers. They fail to address *Pommer* v. *Medtech Corp.*, 961 F.2d 620, 625 (7th Cir. 1992), in which the Seventh Circuit said "[t]he truth (or falsity) of defendants' statements and their materiality, must be assessed *at the time the statements are made*, and not in the light of hindsight" (emphasis added). They do not explain — because they cannot — how any E&Y analyses or reports prepared years after the events at issue can affect the elements of Plaintiffs' securities fraud case.

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[3] Household respectfully requests an opportunity to address the 280 data sampling and data validation boxes after this Court has had an opportunity to review the 21 boxes of material pursuant to the parties' protocol.

Plaintiffs say only that "[d]efendants' arguments on work product are precluded by this Court's prior rulings" (Pls. Mem. at 16) — even though the Court made it abundantly clear that its December 6 ruling was necessarily silent on the E&Y boxes because the Court was not aware at the time of the existence of hundreds of boxes of material created mostly after the start of this lawsuit. Plaintiffs argue that, in its February 27, 2007 Order, "the Court extended these rulings ["that the Class had shown good cause to overcome the work product privilege"] as to post-Class Period documents relating to the E&Y Compliance Engagement." (Pls. Mem. at 15-16) The February 27 Order does no such thing. The language quoted by Plaintiffs in their Memorandum, "Plaintiffs have demonstrated a substantial need for the E&Y information in that it may assist Plaintiffs in establishing falsity, scienter, and materiality" (*Id.* at 16), pertains only to the 187 Class Period documents that were the subject of the December 6 ruling. While the Household Defendants believe that this finding was erroneous as to the 187 documents then at issue, it is clear that the quoted language did not refer to the subsequently discovered boxes of E&Y work papers, as is evident by the fact that the next paragraph of the February 27 Order addresses the boxes of E&Y work papers.

C. The Affidavits of John M. Keller Are Properly Before the Court

Plaintiffs argue that the Court should not consider the April 24, 2007 Affidavit of John Keller of E&Y, which was submitted to the Court *in camera* on April 24, 2007 at the Court's request, and provided to Plaintiffs on May 9, 2007. Their purported ground is that the Affidavit has not been filed with the Court, which overlooks that courts, including the Court in this action, routinely consider materials submitted *in camera* (thus not entered on the public record) in issuing rulings on privilege questions. Nevertheless, to avoid requiring the Court to devote time to consider this non-issue, on May 21, 2007, Defendants filed with the Court the unredacted April 24, 2007 Keller Affidavit under seal.

Plaintiffs also complain that the May 4, 2007 Supplemental Keller Affidavit, attached as Exhibit C to Defendants' initial Memorandum, cannot be considered by the Court

because it was not made solely on Mr. Keller's personal knowledge. Mr. Keller states that his review of the documents described in the Affidavit is "based on my review and that of several of my colleagues at E&Y who are familiar with the work papers created by E&Y during this Engagement." (Defs. Mem. Ex. C at 3). There is nothing improper with an affiant's indicating that he is relying both on his personal knowledge and the relevant knowledge obtained from individuals who worked under his supervision. *See, e.g., Maher* v. *International Brotherhood of Electric Workers,* No. 90C6502, 1993 WL 57553 at *2 (N.D. Ill. Mar. 4, 1993) (motion to strike affidavit denied although union member affiant relied on both his personal observations and discussions with other members of his local union).[4]

[4] Plaintiffs' two other bolded arguments, that Defendants have not taken adequate precautions to protect the privilege and that Defendants cannot alter dates on their privilege log, are also weak. Defendants described the precautions they taken to protect the work papers and not allow them to become available to third parties in their initial Memorandum (at p. 12). And Defendants' changes to a small number of dates on the E&Y work papers privilege log of over 1,400 entries are based on information provided by E&Y and further review by Defendants, in an effort to make the log as complete and accurate as possible.

CONCLUSION

For the reasons set forth above and in Defendants' initial Memorandum of Law filed May 4, 2007, Plaintiffs' demands for production of E&Y's January 2004 draft report and the work papers created in the course of E&Y's privileged Compliance Engagement should be denied.

Dated: May 23, 2007
New York, New York

Respectfully submitted,

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TAB A

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IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

LAWRENCE E. JAFFE, Pension Plan, on behalf of itself and all others similarly situated, and GLICKENHAUS INST GRP., Plaintiffs, vs. HOUSEHOLD INTERNATIONAL, INC., ARTHUR ANDERSEN, L.L.P., W F ALDINGER, and D A SCHOENHOLD, Defendants.	No. 02 C 5893 Chicago, Illinois April 12, 2007 3:36 P.M.

TRANSCRIPT OF PROCEEDINGS - Telephone Status
BEFORE THE HONORABLE NAN R. NOLAN, Magistrate Judge

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THE COURT: Right.

MS. BEST: -- the data validation and data sampling. But what we are talking about now is the logs that we have --

THE COURT: All right.

MS. BEST: -- spent a considerable amount of time preparing already.

THE COURT: All right. All right. All right. All right. Hold on. Just hold on one minute.

(Discussion off the record.)

THE COURT: Well, I want you -- I'm kind of catching you off guard on this. But I think it would be better if you can put something in the affidavit. And I think what we'll do, and we'll make this clear on the record what I am requesting right now, is I'm -- I want to -- these documents that are -- first of all, the September documents, okay, these September documents that have got a range in them, maybe that would be good if you -- if we did an in camera review of those documents, that might be able to help me get to the next step too. Okay. So we'll talk about that at the end of this.

But I do want you when -- when Ernst & Young -- you know, Ms. Best, this is a protection for your client on this affidavit. Okay? Because we don't have anything in the record. If they are not getting the report, they are not getting the unredacted engagement letter, we need an