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.	GMR Lead Case No. 02-C5893 (Consolidated) CLASS ACTION Judge Ronald A. Guzman Magistrate Judge Nan R. Nolan

DEFENDANTS' REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF HOUSEHOLD DEFENDANTS' *DAUBERT* MOTION TO EXCLUDE THE "EXPERT" TESTIMONY OF DANIEL FISCHEL

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This Reply Memorandum is respectfully submitted on behalf of Defendants Household International, Inc., ("Household"), William F. Aldinger, David A. Schoenholz and Gary Gilmer (the "Individual Defendants" and, collectively with Household, the "Household Defendants" or "Defendants"), in further support of their motion to preclude the testimony of Daniel R. Fischel.

PRELIMINARY STATEMENT

Plaintiffs' opposition to Defendants' *Daubert* challenge is an exercise in evasion. Unable to offer a single citation to any loss causation decision that has accepted their "consistent with" formulation as a substitute for proof of a causal relationship, Plaintiffs argue that the problems "go to the weight" rather than a failure to satisfy the requirements of *Dura* and *Daubert*. (PB at 7-8). Lacking a response to substantive defects identified most glaringly in Fischel's deposition testimony, Plaintiffs assert without explanation that Defendants "improperly cite to portions of Fischel's deposition." In lieu of any response to that showing, Plaintiffs offer only evasion: "Plaintiffs will not burden the Court with an analysis of each piece of testimony, and why defendants are wrong." (PB at 12 n.11). Plaintiffs' avoidance of these issues is driven by the total lack of support for the kind of opinion they improperly seek to pass off to this Court as an expert "loss causation" showing.

Fischel acknowledged the core of the problem for Plaintiffs in his report and deposition. On Plaintiffs' instruction, Fischel: (1) assumed that the stock was already inflated on the first day of the Class Period, (2) assumed that there were "specific disclosures" on various days during the Class Period when the stock price declined which revealed "something that the company did not disclose during the class period," and (3) assumed that full disclosure occurred by the last date of the Class Period. Plaintiffs' brief offers no explanation or support at all for assumptions (1) and (3) – both of which are inconsistent with *Dura,* and both of which require exclusion. Their explanation for the second assumption is unavailing because it is the very assumption that prevents Fischel from actually offering an opinion supporting a *causal* relationship rather than a mere "consistent with" relationship. Put simply, Fischel never did the analysis of the alleged "specific disclosures" that would permit him to offer a causation opinion in conformity with governing law.[1] Accepting Plaintiffs' "consistent with" formulation of loss causation would transform almost any price decline into a recoverable fraud, something that *Dura* explicitly forbids.

Fischel's so-called "leakage model" is even worse. It compounds all these problems many-fold by abandoning all pretense about (assumed) "specific disclosures" to claim everything other than ordinary market movement for an 11-month "window" as "damages from fraud." The proffered justification for this "leakage" claim is not any prior decision that has accepted the theory. Indeed, Plaintiffs' brief barely acknowledges the many cases cited by Defendants which generally reject "leakage" theories, including those with much shorter windows. (Plaintiffs' Opposition to Defendants' Motion *In Limine* to Exclude Testimony of Expert Daniel Fischel ("PB") at 8-11). Instead, Fischel cites to an article written by an actual economist who has flatly rejected Fischel's use of his authority (and specifically rejected the 11-month window Fischel uses) in an affidavit submitted in connection with this motion. Unable to directly address the substantive problems such as the absurdly long 11-month window, Plaintiffs are left to complain (inaccurately) that these problems "were not previously raised during expert discovery" (PB at 9), and suggest that Fischel somehow knows better than the author of the one article his opinion looks to for authority.

Even the test of statistical significance that Fischel uses is inconsistent with federal law. Defendants cited numerous cases which rejected on *Daubert* grounds the *identical* standard Fischel used for statistical significance. Unable to locate even one case to support their position, Plaintiffs lamely respond that "Defendants . . . fail to cite any securities cases." (PB at 8). That is a distinction without a difference. Statistical significance is a matter of scientific method and not a

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1 What that analysis would have shown had Fischel been asked to do it, is amply evidenced by Plaintiffs' glaring failure to ask for it.

matter of context. Plaintiffs offer no case law basis at all for their argument that the requirements for statistical significance are relaxed in securities cases.

Plaintiffs' brief in response to Defendants' Daubert motion is an effort to obscure all these defects while belaboring issues that Defendants have not raised and points that Defendants do not dispute. It should not be countenanced.

ARGUMENT

Plaintiffs offer Professor Fischel as an expert for the purposes of testifying as to two issues: (1) whether there was a causal connection between the alleged misrepresentations and Plaintiffs' economic loss ("loss causation") and (2) ***if*** there was such a link between the misrepresentations and their economic loss, the amount of "inflation" that was introduced into Household's stock price as a result of the alleged misrepresentations and the amount that was removed when the "truth was revealed." As to the latter issue, Professor Fischel has put forth two distinct models -- his "Leakage Model" and his "Specific Disclosure Model." Plaintiffs failed to respond to the case law that demonstrates that Professor Fischel failed to conduct a true "event study." Plaintiffs also chose to ignore the many concessions that Professor Fischel made in his deposition. As a result, each of these opinions must be excluded.

I. Professor Fischel's Purported Causation Analysis is Not Useful to the Fact Finder

A. Professor Fischel Has Assumed His Conclusion, Making His Opinion Regarding Causation Useless to the Fact Finder

Because Professor Fischel assumed every aspect of his "loss causation" analysis, he can offer no useful testimony regarding the introduction or dissipation of inflation. Any demonstration of loss causation "must show both that the defendants' alleged misrepresentations artificially inflated the price of the stock and that the value of the stock declined once the market learned of the deception." *Ray* v. *Citigroup Global Markets, Inc.*, 482 F.3d 991, 995 (7th Cir. 2007). Despite

Plaintiffs' unsupported assertions that Professor Fischel assumed only that Defendants made false statements (PB at 11), the introduction and dissipation of inflation is what Professor Fischel explicitly assumed.

- "My analysis is premised on my ***assumption*** that artificial inflation in Household's stock price began on July 30, 1999 or no later than August 16, 1999." (Kavaler Decl. Ex. 3 (February 1, 2008 Rebuttal Report of Daniel R. Fischel ("Fischel Rebuttal")) at ¶ 36) (emphasis added).[2]

- "I am ***assuming*** that the information that came out during the period about these three different areas was something that the company did not disclose during the class period beginning from the first day of the class period." (Kavaler Decl. Ex. 2 (Transcript of the March 21, 2008 Deposition Testimony of Daniel R. Fischel (Fischel Tr.)) at 138:14-18) (emphasis added).

- "[B]ecause it's the last day of the class period, I'm ***assuming*** that full disclosure occurred as of that date, meaning that there is no further inflation to measure after that date." (***Id.*** at 202:17-20) (emphasis added).

Plaintiffs have no serious response to the problems illuminated by Professor Fischel's admissions in his deposition.[3] Instead they manufacture issues for which they do have cases to cite, unremarkably asserting that it is appropriate for experts to assume that "defendants' statements were false and misleading." (PB at 11). Defendants do not dispute that experts are permitted to make assumptions about things they are not supposed to demonstrate. It is not appropriate, however, to offer testimony from an expert who has been asked to assume precisely what his

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[2] "Kavaler Decl." refers to the Declaration of Thomas J. Kavaler in Support of the Household Defendants' *Daubert* Motion to Exclude the "Expert" Testimony of Daniel R. Fischel, dated January 30, 2009.

[3] Indeed, they hide their meager arguments on these central issues at the end of their brief, providing only a few sentences to explain their position. (PB at 11-12).

analysis *is* supposed to demonstrate. Nor can such assumed "analysis" survive a ***Daubert*** challenge. *See, e.g.*, *Clark* v. *Takata Corp.*, 192 F.3d 750, 757 (7th Cir. 1999) (finding expert's opinion unhelpful because expert assumed the very fact he had been hired to prove). By the terms of Professor Fischel's assumptions, any testimony that he provides would not assist the trier of fact in determining the very inflation that he has assumed.

Plaintiffs' brief overlooks the problem of Professor Fischel's improper assumption that some unspecified fraud introduced inflation into Household's stock price before the Class Period began. As Defendants' opening brief demonstrated (DB at 14-15), these unwarranted and unjustified assumptions preclude any consideration of non-fraud alternative explanations, and are therefore inconsistent with ***Daubert***, ***Dura***, and Rule 702.[4] *See*, *e.g.*, *In re Williams Securities Litigation*, 496 F. Supp. 2d 1195, 1267 (N.D. Okla. 2007) (holding that plaintiffs' loss causation expert's methodology was neither relevant nor reliable where he simply assumed that the truth was revealed to the market because "[i]n securities litigation, non-fraud causes of a loss in value are 'obvious alternative explanations,'" which he failed to address). Plaintiffs' brief makes no argument to the contrary, effectively conceding the point.

Plaintiffs have likewise ignored the fact that Professor Fischel himself previously testified in another case that assumptions of this nature are fundamental flaws in methodology. (*See* DB at 15). In *In re Blech*, Professor Fischel criticized a loss causation expert for using the same methods that Professor Fischel employed here, concluding,

> Dr. Nye's report does not analyze the alleged manipulative transactions or present any evidence which establishes which, if any, of the alleged manipulative transactions caused any price inflation. In fact, Dr. Nye merely assumes (as his report states) that the alleged manipulative transactions caused the prices of the Blech Securities to be artificially inflated.

4 "DB" refers to the Memorandum of Law in Support of Household Defendants' ***Daubert*** Motion to Exclude the "Expert" Testimony of Daniel Fischel.

(Kavaler Decl. Ex. 7 (Report of Daniel R. Fischel in *In re Blech Securities*, No. 94 Civ 7696 (RWS)) at 2). Having no response to such fatal testimony, Plaintiffs choose to ignore it, brazenly stating "Plaintiffs will not burden the Court with an analysis." (PB at 12 n.11). If Plaintiffs had a valid response to offer, it is unlikely in the extreme that would have declined to "burden" the Court with it in their responsive brief.

B. Professor Fischel Did Not Evaluate Any Causal Connection

The Supreme Court, in *Dura Pharmaceuticals, Inc.* v. *Broudo*, established that a plaintiff in a securities fraud action must prove loss causation, ***i.e.***, "a causal connection between the alleged material misrepresentation and the plaintiff's loss." 544 U.S. 336, 341-42 (2005). This means that "plaintiffs must show both that the defendants' alleged misrepresentations artificially inflated the price of the stock and that the value of the stock declined once the market learned of the deception." *Ray* v. *Citigroup Global Markets, Inc.*, 482 F.3d 991, 995 (7th Cir. 2007). Any loss causation expert must independently analyze and opine on the "link" between the alleged misleading statements and the economic loss resulting from the revelation of the truth regarding those specific statements.

Professor Fischel has not done this. Indeed, he does not even identify a single misleading statement to which he would purport to "connect" the alleged economic loss. Rather than analyze Plaintiffs' position, Professor Fischel *assumed* that all of Household's public filings between July 30, 1999 and November 14, 2001 were misrepresentations (Kavaler Decl. Ex. 2 (Fischel Tr.) at 127:18-128:4) and *assumed* those misrepresentations were later corrected (*Id.* at 138:14-18). Having *assumed* the misrepresentations and corrective disclosures, Professor Fischel then simply measured Household's stock price movement on each day. Without evaluating whether the alleged disclosures "corrected" the previous statements, Professor Fischel admits that he cannot conclude that the alleged fraud caused Plaintiffs' losses. (*Id.* at 135:19-21).

Professor Fischel did not evaluate whether the alleged corrective disclosures related to the alleged misleading statements, presumably because he does not know which, if any, of Household's statements introduced artificial inflation. Rather, he simply assumed that any disclosure that even mentioned "re-aging," "predatory lending," or the "restatement" contained some facts that were previously unknown. (*Id.* at 138:14-18). By forgoing any analysis of whether there is any connection between the facts allegedly misrepresented and the facts disclosed in the alleged "corrective disclosures," Professor Fischel undercut his ability to provide any opinion related to causation. *Dura* 544 U.S. at 342 (loss causation is the "connection between the material misrepresentation and the plaintiff's loss"). The "consistent with" opinion reflects Fischel's acknowledgment that he has not done the analysis that would permit him to exclude alternative explanations. *See id.* at 343 ("To 'touch upon' a loss is not to *cause* a loss, and it is the latter that the law requires").

Plaintiffs' opposition brief completely glosses over the litany of assumptions that Professor Fischel acknowledged during his deposition. Indeed, Professor Fischel's deposition is not cited once in Plaintiffs' entire brief. Plaintiffs dedicate only a single paragraph to their explanation, blandly asserting that Professor Fischel's analysis "links 'new' information about each prong of defendants' fraudulent scheme -- predatory lending, reaging and the restatement -- to the decline in Household's stock price." (PB at 5) Plaintiffs refer generally to 12 pages of Professor Fischel's report where he listed negative articles that came out in 2002. Nowhere in these 12 pages does he assert either that (1) these disclosures are "linked" or "connected" to any previous statement made by the company, whether false or not, or (2) that any of the articles he lists revealed any "new" information, whether a revelation of a fraud or not. To the contrary, as revealed by his deposition testimony, Fischel concedes that he assumed the actual loss causation analysis that Plaintiffs are inaccurately claiming he performed:

> Q: If the company is accused of being a predatory lender . . . and you are trying to analyze the movements of that stock price in response to allegations about predatory lending, doesn't it matter whether some of

> the things that are being criticized were known to the marketplace or not?

(Kavaler Decl. Ex. 2 (Fischel Tr.) at 196:11-18).

> A: [M]y analysis under both my quantification of specific disclosures and my leakage method of quantification focuses on changes in stock price. . . . [A] determination that something was or was not disclosed in a securitization prospectus wouldn't have any obvious effect on any of my opinions.

(*Id*. at 196:21- 197:18). Indeed, Professor Fischel also conceded in his deposition that he assumed the existence of a connection between these disclosures and previous statements and that these disclosures revealed unspecified "new" information:

> "I am ***assuming*** that the information that came out during the period about these three different areas was ***something*** that the company did not disclose during the class period beginning from the first day of the class period."

(*Id*. at 138:14-18) (emphasis added)

Fischel flatly concedes that he conducted no analysis of the "specific disclosures" at all. This failing is further evident from examining the very disclosure that Plaintiffs use as an example. Plaintiffs allege that the truth regarding Household's predatory lending scheme was first revealed to the market on November 14, 2001 when "the *Associated Press* and *Los Angeles Times* reported that the California Department of Corporations sued Household for $8.5 million, alleging the Company engaged in predatory lending practices." (PB at 6; *see also* Kavaler Decl. Ex. 5 (Lead Plaintiffs' Third Amended Objections and Responses Defendants' [Fifth] Set of Interrogatories to Lead Plaintiffs, 02/01/2008), at 13). By then, that information was a week old. The details of the lawsuit had been reported on November 9, 2001, a day when Household's stock price actually increased. (Kavaler Decl. Ex. 6 (*Abusive Lending*, City News Service, Nov. 9, 2001)). The information on November 15 was without a doubt "old." The only possible way to make it "new" was for Professor Fischel to assume it (counter-factually or not). This is precisely what Fischel says he did.

These assumptions and related problems that Fischel explicitly acknowledged in his deposition show conclusively that Plaintiffs' contention that Professor Fischel "did perform a loss causation analysis" (PB at 5) is false.

The Court of Appeals' recent decision in *Tricontinental* demonstrates the inadequacy of a securities fraud claim that lacks a clear nexus between alleged fraud and the loss that it allegedly caused. The plaintiff in *Tricontinental* alleged that the defendant had made material misrepresentations in a 1997 audit statement, and that the plaintiff had been injured when the price of the audited company's stock declined upon the issuance of 1998 and 1999 audit statements. In an effort to connect the alleged fraud with an apparently unrelated market reaction, the plaintiff argued that the 1997 misrepresentations were part of an "ongoing scheme" that was reinforced by later audit statements. *Tricontinental*, 475 F.3d 824, 842 (7th Cir. 2007). In affirming the dismissal of this § 10(b) claim, the Court of Appeals held that the plaintiff's position could not be reconciled with the Supreme Court's emphasis in *Dura* on the requirement of establishing "a causal connection between the alleged material misrepresentation and the loss, not simply that the misrepresentation touches upon a later economic loss." *Id.* at 843 (quoting *Dura*, 544 U.S. at 342, 342) (citations and internal quotation marks omitted). The Court specified that the plaintiff's burden was to show that the contested 1997 audit contained a material misrepresentation that caused the plaintiff a loss when *that* material misrepresentation became generally known. Alleging market losses triggered by disclosure of the 1998 and 1999 audits was not sufficient to state a claim for losses arising from the alleged 1997 fraud, notwithstanding the plaintiff's invocation of a supposed interrelated scheme. *Tricontinental*, 475 F.3d at 843.

Because Professor Fischel admits that he did not analyze whether there was any connection to a misrepresentation or whether the alleged disclosures contained any new information, his testimony must be excluded. His reliance on unwarranted assumptions in favor of actual economic analysis or "sufficient facts or data" renders his opinion inadmissible. *See Korte* v. *Exxon-*

mobil Coal USA, Inc., 164 Fed. Appx. 553, 557 (7th Cir. 2006) (finding a doctor's testimony inadmissible because his opinion was based on the assumption that defendant's coal dust caused the plaintiffs' injuries, and yet he had failed to test the dust); *Gayton* v. *McCoy*, 521 F. Supp. 2d 841, 850 (C.D. Ill. 2007) ("But general scientific truths . . . cannot be reliably applied to an individual case . . . without first establishing the facts or factual assumptions upon which that application is based.").[5]

C. Professor Fischel's Conclusion That There is Economic Evidence "Consistent With" Plaintiffs' Allegations is Inadmissible

Nowhere in Professor Fischel's Report, Rebuttal Report, Supplemental Report or deposition transcript does Professor Fischel assert that he made any economic determination that the alleged fraud *caused* the alleged economic losses he identifies (although Plaintiffs are fond of baselessly asserting that he did). Nor do Plaintiffs in their Opposition refute Defendants' argument that Professor Fischel's unsupported "consistent with" formulation is an attempt to tip-toe around an inadmissible opinion. Plaintiffs' brief cites to *no cases* that have adopted their novel reformulation of the causation requirement.

Having assumed the fraud, the inflation, and its dissipation at the end of the Class Period, Professor Fischel cannot conclude that the alleged fraud actually "caused" Plaintiffs' losses

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5 Plaintiffs also mistakenly argue that Professor Fischel's loss causation "analysis" is sufficient because "Professor Fischel's regression analysis removed the impact of market and industry factors and found a statistically significant decline in Household's stock due to partial revelations of the fraud." (PB at 5). Apart from being erroneous, (because Professor Fischel acknowledged that he had not isolated particular revelations of fraud, it is irrelevant. As the Supreme Court held, loss causation is the connection between the economic loss and the alleged misrepresentation, not an alleged disclosure. *Dura* at 341. Stock price declines are always connected to bad news. The key to a federal securities fraud claim is that they must be linked to a misrepresentation. As discussed above, the fact that Professor Fischel made no determination as to any connection or as to whether the disclosures contained new information, any stock price movement that may have occurred on these days is by definition irrelevant to a loss causation determination. Moreover, Professor Fischel's Leakage Model explicitly did not even "link" any *disclosures* to "statistically significant declines," which only highlights that his entire method is flawed, not just his Leakage Model.

(as *Dura* requires). Implicitly acknowledging this shortcoming, he concludes only that there is economic evidence "consistent with" Plaintiffs' allegation.[6] (Kavaler Decl. Ex. 1 (August 15, 2007 Report of Daniel R. Fischel ("Fischel Report")) at ¶ 29). Plaintiffs' attempt to present the jury with this watered-down conclusion must be rejected. Any opinion that falls short of an actual causation determination is useless to the jury and would put undue weight on a legally insufficient formulation and confuse the jury. *See Oscar Private Equity Investments* v. *Allegiance Telecom, Inc.*, 487 F.3d 261, 270 (5th Cir. 2007) (denying class certification because "[t]he plaintiff's expert report did not establish loss causation"); *In re Omnicom Group, Inc. Securities Litigation*, 541 F. Supp. 2d 546, 554 (S.D.N.Y. 2008) (granting summary judgment for the defendant because plaintiffs' expert's event study failed to demonstrate loss causation); *see also In re Williams Securities Litigation*, 496 F. Supp. 2d at 1266; *Malletier* v. *Dooney & Burke, Inc.*, 525 F. Supp. 2d 588, 669 (S.D.N.Y. 2007) (rejecting a regression analysis "because [plaintiff] has not set forth any credible testimony from a knowledgeable witness that the obvious alternatives were considered, analyzed and ruled out").

Indeed, even in the face of Defendants' explicit challenge to his method, Professor Fischel refuses to assert that his "analysis" was a causation determination. In his "Supplemental Report," attached to Plaintiffs Opposition Brief, Professor Fischel again repeats that he will not give a causation opinion: "[M]y principal conclusion [is] that the economic evidence is consistent with Plaintiffs' claim." (Supplemental Report of Daniel R. Fischel at 1). And Plaintiffs make absolutely

6 Lacking any analysis that might support a causal connection, Professor Fischel does not even establish a statistical correlation between the economic evidence and Plaintiffs' allegations. Of course, even a statistical correlation is insufficient in this Circuit as a basis to prove a causal relationship. *See*, *e.g.*, *Sheehan* v. *Daily Racing Form, Inc.*, 104 F.3d 940, 942 (7th Cir. 1997) (excluding an expert's testimony in an age discrimination case because "his equating a simple statistical correlation to a causal relation . . . indicates a failure to exercise the degree of care that a statistician would use in his scientific work, outside of the context of litigation").

no effort in their Opposition to demonstrate that Professor Fischel provides a causation opinion or that his "consistent with" opinion is admissible.

In his deposition (which Plaintiffs' brief chooses to ignore and inexplicitly faults Defendants for citing), Professor Fischel emphasized that the economic evidence he considered could ***not*** support an opinion that the alleged fraud caused Household's stock price to become artificially inflated and later caused Household's stock price to decline when the truth was revealed. Professor Fischel stated:

> I'm not expressing an opinion on whether there were in fact misrepresentations or omissions [that produced inflation]. *The economic evidence that I've looked at does not allow me to express an opinion on that subject.* I can express an opinion as to whether the economic evidence is consistent with those allegations . . . .

(Kavaler Decl. Ex. 2 (Fischel Tr.) at 49:11-26) (emphasis added).

D. Plaintiffs' Arguments Are Contradicted By Fischel's Actual Opinion

In irrelevantly analyzing whether the economic evidence is "consistent with" Plaintiffs' claims of inflation, Professor Fischel considered the misleading statements alleged by Plaintiffs:

> [T]he plaintiffs allege that all public statements from the beginning of the class period contained material nondisclosures relating to the three different areas that I discuss in my report, and what I've attempted to do is, based on that assumption, attempt to quantify the amount of inflation that resulted, and how that inflation varied over time as different disclosures occurred, which either increased or decreased inflation during the class period.

(Kavaler Decl. Ex. 2 (Fischel Tr.) at 127:18-128:4). Professor Fischel concluded that ***none*** of the alleged misleading statements introduced inflation into Household's stock price. (*Id*. at 123:8-11 (explaining that "***I didn't find any statistically significant price increases that resulted in inflation*** from the beginning of the period, and through November 15, 2001" when inflation began to decrease) (emphasis added)). Having determined with his analysis that no inflation was introduced by any of the alleged misleading statements, Professor Fischel simply ***assumed that the inflation was already there***. He stated:

> "My analysis is premised on my assumption that artificial inflation in Household's stock price began on July 30, 1999 or no later than August 16, 1999."

(Kavaler Decl. Ex. 3 (Fischel Rebuttal) at ¶ 36) (emphasis added). Having assumed inflation that his analysis did not actually show, Fischel runs into another problem that Plaintiffs' brief does not address, because "a valid loss causation methodology . . . must be able to analyze the inflationary effects of the alleged misrepresentations or omissions ***and*** the alleged corrective events." ***Fogarazzo*** v. *Lehman Bros.*, 232 F.R.D. 176, 189 (S.D.N.Y. 2005) (emphasis added).

Contradicting Fischel's own statements, Plaintiffs' brief now counterfactually asserts that Professor Fischel's analysis actually says that "Defendants' statements clearly ***introduced inflation*** into Household's stock price ***each time*** defendants made false and misleading statements to investors." (PB at 13) (emphasis added). As the above quoted statements prove, this contention is not accurate. That is not his opinion. He said exactly the opposite, and Plaintiffs' argument is a deception. For example:

> Q: I want to understand in the sense that you use the words 'to become inflated,' how the stock price is becoming inflated on any of those days?
>
> A: . . . [A]s a result of my quantification of what I am assuming to be a series of nondisclosures on the first day of the class period where the inflation ***remained constant***, until there was a disclosure either increasing the amount of inflation or decreasing the amount of inflation which, based on my analysis, occurred on November 15th of 2001 [when the identified inflation began to decline].

(Kavaler Decl. Ex. 2 (Fischel Tr.) at 132:21-133:7) (emphasis added)).

Plaintiffs' brief actually confuses the matter further, asserting that "Professor Fischel's reports rejected as 'incorrect and misleading' the contention that his analysis 'explicitly assumes that no inflationary events occurred prior to November 15, 2001'" (PB at 12). This is precisely the point. The problem with Fischel's analysis is not that he assumed that ***"no inflationary events occurred,"*** the problem is that he looked for inflationary events, found none and then counter-factually assumed that ***inflationary events did occur.***[7]

II. Professor Fischel's "Inflation" Models Do Not Support Loss Causation

Throughout their Opposition, Plaintiffs repeatedly refer to Professor Fischel's "inflation models" as independent support for the required showing that the alleged fraud "caused" Plaintiffs' loss. (PB at 1,3,5,11). First, as described above, Professor Fischel explicitly stated that he is not providing a causation opinion in this case (but only an inadmissible "consistent with" opinion). Second, Professor Fischel states that neither of his "inflation models" are support for his underlying analysis. Rather, these models are the *product* of his "consistent with" opinion contained in Section III of his Report and various non-loss causation assumptions which may not be proven at trial. As Professor Fischel testified:

[7] The remainder of Plaintiffs' argument on this point is an attempt to confuse the Court by conflating an increase in stock price with an increase in inflation. Federal securities law is only concerned with the latter. As Professor Fischel testified, the omission/misrepresentation distinction is irrelevant for purposes of measuring inflation. "[A] disclosure which contains an omission cannot create inflation even if there is no price reaction to it." (Kavaler Decl. Ex. 2 (Fischel Tr.) at 126:7-9). Nevertheless, Fischel stated that "Regression analysis [] can be used in this case to calculate the amount of artificial inflation resulting from an alleged omission on any day during the Class Period." (Kavaler Decl. Ex. 3 (Fischel Rebuttal) at ¶ 39). "[I]f I make the opposite assumption that plaintiffs claim particular statements of misrepresentations as opposed to omissions, and there is no statistically significant price reaction to them . . . . I would still conclude that those statements would not be the basis of a material misrepresentation which would be included in my quantification of specific disclosures, because there is no statistically significant price reaction as a result. *So nothing really for my purposes turns on whether these statements are considered to be omissions or misrepresentations.*" (Kavaler Decl. Ex. 2 (Fischel Tr.) at 124:22-125:12 (emphasis added)). Plaintiffs' repeated attempt to confuse the Court as to what Professor Fischel has analyzed and what he has assumed should be recognized and rejected for what it is.

> [I]f, for example, the evidence at trial . . . suggest[s] that the alleged disclosure defects are different from the analysis in my report, that could have an effect on the amount of artificial inflation that could be taken into account either by me, or by a court, or by an opposing expert, or by the fact finder, depending on what the relevant facts and circumstances are.

(Kavaler Decl. Ex. 2 (Fischel Tr.) at 66:6-14).

As Professor Fischel explained, these models are hypothetical exercises measuring what (if any) inflation was present in Household's stock price if the assumptions about assumed matters distinct from loss causation are borne out. What the models clearly do not do, despite Plaintiffs' unwarranted suggestion otherwise, is independently establish the causal connection (unsupplied by Fischel) that is required even to reach a damages calculation stage when they might become relevant.[8]

A. Professor Fischel's Leakage Model Fails to Account for Non-Fraud Firm-Specific Information that Affected Household's Stock Price

Any economic analysis that purports to measure inflation resulting from an alleged fraud must specifically exclude all non-fraud firm-specific information. *Dura Pharmaceuticals, Inc.* v. *Broudo*, 544 U.S. 336, 342-43 (2005). Professor Fischel readily admits that his Leakage Model did not do this. In fact, he explicitly confirms that his Leakage Model attributes inflation to other firm-specific disclosures that have nothing to do with the alleged fraud. (Kavaler Decl. Ex. 2 (Fischel Tr.) at 57:12-16). The Leakage Model even identifies "inflation" on days when absolutely

[8] Indeed, Plaintiffs admit that "Professor Fischel [] assumed liability in this case." (PB at 11) As discussed above, Defendants do not take issue with the fact that Professor Fischel assumed any portion of Plaintiffs' claims that he is not charged with independently demonstrating. However, as the Supreme Court held in *Dura* "liability" under the federal securities laws includes loss causation. *Dura*, 544 U.S. at 342 (identifying the elements of securities fraud as misleading statements, materiality, reliance, scienter, loss causation, and economic loss). Fischel is not entitled to assume that portion of "liability" that includes loss causation and then opine that he independently determined it. Certainly, his "inflation models," which he admits are only relevant if the jury finds liability (including loss causation), cannot be used by Plaintiffs as "evidence" of loss causation.

no information about the company was released by any source. Plaintiffs' "support" for Fischel's leakage model deliberately ignore this fundamental flaw by arguing a legal issue that Defendants never raised and do not dispute here -- that the truth can be revealed through several "disclosing events" and that such disclosures can come from sources other than the company. (PB at 9-10).[9]

Plaintiffs' side-show argument deliberately misses the point. As courts have repeatedly held, the problem with the Leakage Model proposed by Professor Fischel is not that it identifies multiple disclosing events or that the disclosing events come from sources outside the company. Indeed, Plaintiffs' "Specific Disclosures" model already incorporates these less reliable features. The problem lies in the substance of the method -- the Leakage Model attributes every single stock price movement that is not attributable to the market or the industry to the fraud. It fails to exclude all the other company-specific non-fraud related news that affects the stock price. As the Supreme Court held:

> If the purchaser sells later after the truth makes its way into the marketplace, an initially inflated purchase price might mean a later loss. But that is far from inevitably so. When the purchaser subsequently resells such shares, even at a lower price, that lower price may reflect, not the earlier misrepresentation, but changed economic circumstances, changed investor expectations, new industry-specific or ***firm-specific facts***, conditions, or other events, which taken separately or together account for some or all of that lower price. . . .

Dura Pharmaceuticals, Inc. v. *Broudo*, 544 U.S. 336, 342-43 (2005).[10]

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9 Plaintiffs cite several cases to support these straw man propositions. ***In re Bradley Pharms., Inc. Sec. Litig.***, 421 F. Supp. 2d 822 (D.N.J. 2006); ***In re Motorola Securities Litigation***, 505 F. Supp. 2d 501, 543 (N.D. Ill. 2007); ***In re Flag Telecom Holdings, Ltd. Securities Litigation***, 245 F.R.D. 147, 166-67 (S.D.N.Y. 2007). None of these cases deal with a model that, like Professor Fischel's Leakage Model, attributes all non-market and non-industry declines to the alleged fraud. Defendants do not dispute that there can be more than one disclosing event or that such disclosures can come from outside sources. Plaintiffs' citation to these cases is blatantly misleading but not surprising as they can cite to no case that has ever permitted a model that fails to remove firm-specific non-fraud factors.

10 Plaintiffs ironically cite to questions posed by Justices to counsel during oral arguments in *Dura* as "support" for their "leakage" theory. (PB at 10 n.10). Plaintiffs omit the obvious. *Dura* was de-

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Professor Fischel explicitly acknowledged that his Leakage Model attributed residual stock price declines to the alleged fraud even though they had nothing to do with Plaintiffs' allegations. (Kavaler Decl. Ex. 2 (Fischel Tr.) at 57:12-16 ("Q: So there are a bunch of stock price movements that were significant under your regression analysis that were not attributable to fraud related disclosures? A: Correct.")). For example, Professor Fischel identifies July 9 and 10, 2002 as statistically significant residual declines, however, he identifies no information regarding Household or even the consumer finance sector being released between July 2 and July 10. (Kavaler Decl. Ex. 1 (Fischel Report) Appendix 49 at page 40). The Leakage Model improperly nevertheless incorporates these non-fraud stock price declines in the calculation of inflation from fraud. ***See In re*** *Imperial Credit Industries, Inc. Securities Litigation*, 252 F. Supp. 2d 1005, 1014-15 (C.D. Cal. 2003) ("[a] proper measure of damages in the securities context . . . requires elimination of that portion of the price decline or price difference which is unrelated to the alleged wrong"), ***aff'd sub nom.*** *Mortensen* v. *Snavely*, 145 Fed. Appx. 218 (9th Cir. 2005).[11] Indeed, courts have held that even where "plaintiffs' expert does detail[ed] event studies supporting a finding that [the stock] reacted to the *entire bundle* of negative information . . . this reaction suggests only market efficiency, not loss causation, for there is no evidence linking the ***culpable*** disclosure to the stock-price move-

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cided ***against*** the plaintiffs and explicitly held that any loss causation analysis must exclude firm-specific non-fraud factors. ***Dura*** at 342-43. The fact that a Justice may have been playing "devil's advocate" prior to explicitly rejecting Plaintiffs' position is not only irrelevant, it refutes Plaintiffs' position. Plaintiffs need to rely on such "support" for their theory and Professor Fischel's model only highlights the hopelessness of their position.

11 Equally inappropriately, Professor Fischel's Leakage Model attributes to the alleged fraud all residual stock price declines on every day even if the movement was not statistically significant. As Professor Fischel has acknowledged in his own writing, it is a well accepted tenet of economics that one can only attribute stock price movements to an event (fraud) if the stock price movement is statistically significant. Daniel R. Fischel, *Use of Modern Finance Theory in Securities Fraud Cases Involving Actively Traded Securities*, 38 Bus. Law. 1, 19 (1982) ("If the difference between the actual return and the predicted return is not statistically significant, investors were not injured. . . ."). Plaintiffs provide no response to this point in their Opposition.

ment." *Oscar Private Equity Investments* v. *Allegiance Telecom, Inc.*, 487 F.3d 261, 271 (5th Cir. 2007) (emphasis in original).

Plaintiffs claim that Fischel's Leakage Model is an improvement on the model rejected in *Williams* because Professor Fischel bolstered his model with the unremarkable opinion that "Household's share price substantially underperformed the market." (PB at 11). This is another distinction without a difference. In *Williams*, the court rejected the "leakage model" of plaintiffs' expert, Dr. Nye, because it (like Fischel's leakage model here) attributed all non-market and non-industry stock price declines of a telecommunications company over a lengthy 21-month period to the alleged fraud. The court found the model insufficient under Rule 702, *Daubert* and *Dura* because a leakage model that attributes all residual returns not explained by general market forces to inflation "collides directly with loss causation doctrine" because such a model "does not even purport . . . to have removed the effects of ***'[n]onfraud company-specific information***.'" *Id.* at 1266 (emphasis added). Plaintiffs do not even attempt to assert any distinction between Professor Fischel's Leakage Model and the one rejected in *United States* v. *Ferguson*, 584 F.Supp. 2d 447 (D. Conn. 2008). In *Ferguson*, the court rejected plaintiff's expert's "leakage event study" which was "an estimate of the total decline in [defendant's] stock price for that thirty-day period, after controlling for market and industry factors" because "the leakage study attributes all non-market and non-industry related declines in [defendant's] stock price to the [] fraud without accounting for other factors that may have contributed to that decline. . ."). Plaintiffs' bolstering cannot get around this case law.

Even Professor Bradford Cornell, the author of the one article upon which Professor Fischel exclusively relies for expert authority on leakage, has rejected Professor Fischel's Leakage Model because it does not account for non-fraud firm specific information.[12] As Professor Cornell

[12] Citing no support, Plaintiffs half-heartedly assert that Professor Cornell's affidavit should "not be considered by the Court" when deciding this *Daubert* motion. (PB at 9 n.9). Professor Cornell's af-

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explained the Leakage Model is not an "event study" as Professor Fischel claims, but rather a "comparable index approach," also discussed in his article, which does not account for firm-specific non-fraud factors. (Kavaler Decl., Ex. 9 (Affidavit of Bradford Cornell, dated October 30, 2008 ("Cornell Aff.") at 5). Fischel later effectively conceded that the term "comparable index approach" applies to his analysis by using the description himself. (Supplemental Report of Professor Fischel at ¶ 5).

Professor Cornell explains that regardless of whether Professor Fischel calls his Leakage Model an "event study" or a "comparable index approach" the substantive flaw is the same:

> Whether Prof. Fischel's approach is called an event approach or a comparable index approach, it still suffers from the problem that Mr. Morgan and I discuss on page 903 of our paper. There we say, 'The trouble with the comparable index approach, . . . is that it attributes any decline in the security price that is not due to movements in the market or the industry to disclosure of the fraud. If the disclosure of the fraud is associated with the release of other company-specific news, the comparable index approach will overestimate the true damages.' The recognition of this problem with the comparable index approach is not unique to Mr. Morgan and me. It has been widely documented in the academic literature, including published work by Prof. Fischel.

(Kavaler Decl., Ex. 9 (Cornell Aff.") at 5).

Notably absent from Professor Fischel's Supplemental Report is any assertion that his Leakage Model in any way accounts for firm-specific non-fraud information, which ***Daubert***

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fidavit is completely appropriate and admissible for the purposes of a *Daubert* hearing. ***See e.g. In re: Paoli Railroad Yard PCB Litigation***, 35 F.3d 717, 739 (3rd Cir. 1994) (affirming the district court's decision to allow an undisclosed expert to testify at a *Daubert* hearing). Plaintiffs have had Professor Cornell's affidavit since October 31, 2008. They have had ample opportunity in the intervening 4 months to respond to it.

and *Dura* require. It is this failing that resulted in the exclusion of similar leakage models in every case and it is the fundamental flaw that mandates the exclusion of the model here. Indeed, Plaintiffs do not cite a single case that has permitted the admission of any model (whether facially labeled "leakage", "event study" or "comparable index approach") that did not explicitly remove firm-specific non-fraud factors as *Dura* requires.

Moreover, the sheer size of Professor Fischel's Leakage Model's "event window" (11 months) mandates its exclusion. *See United States* v. *Ferguson*, 584 F. Supp. 2d 447 (D. Conn. 2008) (rejecting loss causation expert's "leakage event study" that used a 30 day window); *In re Williams Securities Litigation*, 496 F. Supp. 2d at 1266-67 (excluding loss causation expert who measured inflation over a 21-month period).[13] Dr. Cornell explicitly commented on the unreliable nature of the eleven-month window in this case:

> There is one final issue that arises when regression models are applied over long periods to predict returns as Prof. Fischel does in his leakage model. No regression model perfectly accounts for market and industry factors. Nonetheless, if the models are used to calculate residual returns over intervals of no more than a few days, the errors are generally minor. However, when a model is used to predict returns over periods hundreds of days long the errors compound. Such compounding, in turn, can produce significant errors in measured inflation. This is another reason to be skeptical of the results produced by the comparable index approach.

(Kavaler Decl., Ex. 9 (Cornell Aff.)) at 5-6).

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13 Because the cornerstone of the efficient market hypothesis is that the market incorporates all information immediately, the generally accepted size of an "event window" is one or two days. *See, e.g.*, *Goldberg* v. *Household Bank, F.S.B.*, 890 F.2d 965, 966-67 (7th Cir. 1989) ("[Plaintiff] sought $3.75 per share, the amount the stock declined on the date the truth came out. . . . When markets are liquid and respond quickly to news, the drop when the truth appears is a good measure of the value of the information. . .") (citing *Flamm* v. *Eberstadt*, 814 F.2d 1169, 1179-80 (7th Cir. 1987) and Daniel R. Fischel, *Use of Modern Finance Theory in Securities Fraud Cases Involving Actively Traded Securities*, 38 Bus. Law. 1, 12-13 (1982)); *Short* v. *Belleville Shoe Manufacturing Co.*, 908 F.2d 1385, 1392 (7th Cir. 1990) ("the market price of the securities after the news is released. . . . is fixed within days after the trading, sometimes within hours").

Plaintiffs' response makes no attempt to validate the patently unreasonable use of an event window of nearly a year. (PB at 9). And certainly Dr. Cornell -- the authority Professor Fischel's Report invokes -- does not validate it. As the case law on leakage models confirms, Professor Fischel's Leakage Model must be excluded.

B. Professor Fischel's Use of an Unacceptable One-Tail Test Mandates Exclusion of Both Models

Defendants are aware of no federal securities fraud case that has ever permitted a statistical analysis based on a "one-tail" test. To the contrary, the use of a "one-tail" test in a statistical analysis mandates the exclusion of that analysis. As this Court has held: "Unlike the more common 'two-tailed' standards, which assess the likelihood that any differences between two groups would occur by chance, a one-tailed standard assumes that any deviation from what might be predicted by chance will be in only one direction." *Dicker* v. *Allstate Life Insurance Co.*, No. 89 C 4982, 1997 U.S. Dist. LEXIS 4512, at *117 (N.D. Ill. Apr. 7, 1997) (Pallmeyer, M.J.). Courts have universally rejected it in discrimination cases because discrimination can occur against either sex [or race], even though the possibility may be remote. *See, e.g.*, *Palmer* v. *Shultz*, 815 F.2d 84, 95-96 (D.C. Cir. 1987); *Barnhill* v. *City of Chicago Police Department*, 142 F. Supp. 2d 948, 969 (N.D. Ill. 2001) (Pallmeyer, J.) (a one-tail test in a discrimination case was inappropriate because it did not consider that discrimination can occur against other races); *EEOC* v. *Autozone, Inc.*, No. 00-2923, 2006 WL 2524093, at *5 (W.D. Tenn. Aug. 29, 2006) (stating, in a discrimination case, that "using the two-tail rather than the one-tail probabilities is appropriate because one must look for both under-and overrepresentation, rather than looking for underrepresentation only").

It is undisputed that Professor Fischel used the "one-tail" test. Professor Fischel was asked this question point blank at his deposition and he testified that he employed the one-tail test, not the two tail test. (Kavaler Decl. Ex. 2 (Fischel Tr.) at 53:16 ("I used a 1-tail test")). Instead of finding support for the test they used, Plaintiffs assert without citation or support that a one-tail test and two-tail test are pretty much the same and that the test is acceptable in securities cases even if it has been universally rejected in discrimination cases. (PB at 8). Plaintiffs' position is nonsensical. If the two tests were really the "same" as Plaintiffs assert, then courts would not repeatedly reject the one-tail test outright. The reasons courts have repeatedly rejected a relaxed standard for statistical significance apply with at least equal force when sought to be applied to a claim of damages in the billions of dollars. Notably, Plaintiffs cite no case to support their proposition (because it is absurd). The objective principles of statistical reliability do not change depending which federal statute is invoked.

It is a simple matter of methodology. The "two-tail" test is objective, while the "one-tail" test is by definition biased because the analyst begins the examination with the assumption that the stock price will move in only one direction (in this case, decline). (Kavaler Decl. Ex. 2 (Fischel Tr.) at 147:20-23 ("using [the one-tail] test of statistical significance, you have a hypothesis of which direction stocks are going to move in response to a particular disclosure")). As courts have repeatedly and consistently held, this inherent bias of the one-tail test mandates its exclusion under *Daubert*. *See Dicker* v. *Allstate Life Insurance Co.*, No. 89 C 4982, 1997 U.S. Dist. LEXIS 4512, at *117 (N.D. Ill. Apr. 7, 1997) (Pallmeyer, M.J.) (rejecting the use of a one-tail test, and stating that "this court is unwilling to relax the standards necessary for a showing of statistical significance. . . .").

The reason that Plaintiffs had Professor Fischel use the biased one-tail test is because it would lend support to a less reliable opinion. *EEOC* v. *Federal Reserve Bank*, 698 F.2d 633, 655-56 (4th Cir. 1983) ("'Many investigators find it tempting to use a one-tailed probability level to facilitate obtaining "significant" results.'") (quoting Herbert Friedman, *Introduction to Statistics*, 146-47 (Random House, 1972)), *rev'd on other grounds*, 467 U.S. 867 (1984). For these reasons, one-tail tests have been described as "'data mining' per se,'" *i.e.*, they are used for "'manipulating data to prove a desired result.'" *Id.* at 655-56. (citing Gregory Harper, *Statistics as Evidence of Age Dis-*

crimination, 32 Hastings L.J. 1347, 1355 n.65 (1981) (citing David Freedman, Robert Pisani & Roger Purves, *Statistics* 494-96 (1978))). Professor Fischel's reliance on this inherently biased and universally rejected analysis renders his regression analysis, which is the basis for both of his "inflation models," inadmissible.

C. Professor Fischel's Specific Disclosure Model Must Be Excluded Because He Engaged in "Cherry-Picking"

Professor Fischel's Specific Disclosure Model, although not as egregious as Professor Fischel's Leakage Model in claiming inflation from non-fraud related price declines, is nevertheless still inadmissible because it uses a method guaranteed to produce a biased result. Apart from his use of the biased "one-tail" significance test (that identified the stock price declines claimed by the specific disclosures model), Professor Fischel limited his analysis to only those disclosures that coincide with a significant stock price decline. Absent from his analysis is any consideration of similar disclosures that were inconsistent with that analysis. Since disclosures that contradict Plaintiffs' claims are not part of his analysis, Professor Fischel's opinion draws all the unwarranted conclusions that naturally come from a "stacked deck." Statisticians call this type of manipulation "cherry-picking."

Plaintiffs do not deny that Professor Fischel's model is subject to this criticism. Instead, Plaintiffs' brief says the Court should just ignore this defect because it reflects nothing more than the ordinary disagreement among experts. (PB at 6 (arguing that "courts routinely reject *Daubert* attacks on damages experts based on a disagreement over which events are relevant and should be included in a loss causation and damages analysis."). On its face, this argument neither addresses nor refutes the fundamental flaw in Professor Fischel's methodology. This flaw goes directly to the method by which Professor Fischel constructed his model and is not limited to the mere inclusion or exclusion of particular days in Fischel's analysis, as Plaintiffs' brief incorrectly suggests.

The Court of Appeals makes clear that an expert cannot ignore evidence that refutes his conclusions. ***See, e.g.*, *Barber*** v. ***United Airlines, Inc.***, 17 Fed Appx. 433, 437 (7th Cir. 2001) ("[b]ecause in formulating his opinion [the expert] cherry-picked the facts he considered to render an expert opinion, the district court correctly barred his testimony because such a selective use of facts fails to satisfy the scientific method and ***Daubert***, and it thus fails to 'assist the trier of fact'"); ***Glover*** v. ***DeLuca***, No. 2:03-CV-0288, 2006 WL 2850448, at *16 (W.D. Pa. Sept. 29, 2006) ("[T]he Court concludes that Plaintiff has 'cherry-picked' the worst outcomes from the list of some 30 projects while ignoring more positive results."). When evaluating stock price movements, cherry-picking the disclosure days that support the expert's position renders his opinion inadmissible. ***See also Bell*** v. ***Ascendant Solutions, Inc.***, No. Civ. A. 301CV0166N, 2004 WL 1490009, at *3 (N.D. Tex. July 1, 2004) (criticizing expert's method in a 10b-5 case and stating that the expert's "identification of 'information days' includes dates that appear to be consciously chosen in order artificially to support his hypothesis of efficiency").

Plaintiffs can provide no distinction between the flaw in Professor Fischel's method and the coin-flipping example in Defendants' opening brief. Just as the coin-flipper will guarantee biased results if he defines his sample as only coins that come up "tails," Professor Fischel's Specific Disclosure Model was biased because he defined his sample as only those days where there was a significant decline. The problem for conclusions drawn from this kind of biased analysis is that if an allegation of "predatory lending" is just as likely to coincide with a significant increase in stock price (or no significant movement at all) as it is to coincide with a significant decrease, then "predatory lending" disclosures cannot be said to be the cause of those price changes. Professor Fischel's model is specifically designed to prevent revealing such an unhelpful result for Plaintiffs.

Professor Fischel acknowledged the methodological problem posed by a failure to consider contradictory days which he admittedly did not analyze:

> Q: If the stock hadn't moved or had gone up significantly on those days, would you deem that fact . . . to be inconsistent with plaintiff's claims in this case? . . .
>
> A: I would say I certainly would not say that those [] hypothetical stock price reactions would support my opinion that the stock price was artificially inflated

(Kavaler Decl. Ex. 2 (Fischel Tr.) at 163:11-13). Professor Fischel's choice to ignore all evidence inconsistent with Plaintiffs' allegations or the opinion he was asked to give is textbook "cherry-picking," indicating the fundamental unreliability of Professor Fischel's methods. This is an independent basis for exclusion.

Plaintiffs' fallback position claims that Professor Fischel conducted an undisclosed analysis of "the total mix of information" and decided to exclude the days that contradicted Plaintiffs' claim (without including any reference to it in his report). (PB at 7). This new and unsupported explanation was wholly manufactured by Plaintiffs' counsel after the fact. Neither Professor Fischel nor Plaintiffs have ever described what this supposed process involved, except that the brief now asserts (without citation) that Professor Fischel "eyeballed" the "total mix of information" to reach his conclusions (which would implicitly be unsound without this undisclosed analytical step). (PB at 7). There is no indication in the Reports or otherwise of what information Fischel considered, how he weighed it or what criteria he used. Professor Fischel's winnowing process amounts to "I know it when I see it." Professor Fischel himself has admitted that such a conclusory method is unacceptable in economics:

> [I]t's not possible to analyze issues of what the market was aware of or not aware of, or what information was material or not material by what I referred to in my writings as -- I know it when I see it test.

(Kavaler Decl. Ex. 2 (Fischel Tr.) at 39:2-13). The biased nature of Professor Fischel's analysis pervades every aspect of his model, from his use of the unacceptable "one-tail" test, to his result-oriented selection process, to his additional subjective "winnowing" of disclosure days, requiring its exclusion. *See Ryan* v. *Flowserve Corp.*, 245 F.R.D. 560, 573 (N.D. Tex. 2007) ("The flawed thread interwoven throughout [the expert's loss causation study] is his results-oriented approach to the public data often discounting inconvenient but relevant facts."); ***In re Polymedica Corp. Securities Litigation***, 453 F. Supp. 2d 260, 270 (D. Mass. 2006) (rejecting loss causation study of plaintiffs' expert because, as here, the expert "self-selected" trading days to examine instead of looking at all trading days).

Plaintiffs' most sweeping and silly argument in defense of the specific disclosure model asserts that virtually any "event study" is sufficiently reliable to avoid exclusion under ***Daubert***. (PB at 2). Plaintiffs' reliance on the magic words "event study" is misplaced. Event studies are routinely excluded for failure to adhere to the rigorous admissibility requirements set forth by ***Daubert*** and the explicit substantive requirements of loss causation under ***Dura***. Failure to consider and exclude the other firm specific information released on corrective disclosure days mandates exclusion of an expert's analysis, even if the expert conducted an "event study." ***In re Omnicom Group, Inc. Securities Litigation***, 541 F. Supp. 2d 546, 554 (S.D.N.Y. 2008) (holding that plaintiffs' expert's event study failed to demonstrate loss causation because he did not remove the effects of negative characterizations of information from the affect of the information itself and that such characterizations are "among the 'tangle of factors' that plaintiffs must distinguish" from the actual fraud.) (citation omitted).

In *United States* v. *Schiff*, 538 F. Supp. 2d 818, 837 (D.N.J. 2008), the court excluded an expert's testimony because even though he performed an event study that "controll[ed] for exogenous market, industry, and economy-wide effects" and concluded that there was a "statistically significant" movement on the disclosure day, "[h]e did not, however, attempt to control for the multiple simultaneous adverse [company] news that included both events charged in the indictment and events not charged in the indictment." *Id*. The court held that "[w]ithout a causal link to the curative disclosure . . . charged in the indictment, evidence of a stock price drop is not probative of materiality of that alleged misstatement, and instead is more prejudicial or confusing than probative." *Id*. at 838.

Plaintiffs concede that Professor Fischel methodically attributed all residual stock price movements to the "fraud related" information on every single day in his Specific Disclosure Model, even when there was non-fraud news released simultaneously. Plaintiffs do not refute any of the case law that states that such failures to consider non-fraud news and its impact on damages requires exclusion. *See, e.g., Oscar Private Equity Investments* v. *Allegiance Telecom, Inc.*, 487 F.3d 261, 270 (5th Cir. 2007) (denying class certification because of plaintiffs' expert failure to show loss causation, emphasizing that in order to establish loss causation, an expert -- even if conducting an event study -- must parse out the effect of the corrective disclosure from the other firm specific information released on that day and "offer some empirically-based showing that the corrective disclosure was more than just present at the scene.")

CONCLUSION

For the foregoing reasons, Defendants respectfully request that Defendants' Motion *In Limine* to Exclude the Testimony of Plaintiffs' Proffered Expert Daniel R. Fischel be granted, and that the Court issue an Order excluding his testimony from trial for any purpose, including both inflation models contained in his Report.

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