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, vs. HOUSEHOLD INTERNATIONAL, INC., et al., Defendants.	Lead Case No. 02-C-5893 (Consolidated) CLASS ACTION Judge Ronald A. Guzman

REPLY BRIEF IN SUPPORT OF PLAINTIFFS' MOTION FOR ENTRY OF JUDGMENT AND AN AWARD OF PREJUDGMENT INTEREST

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I. INTRODUCTION

Defendants agree that judgment should be entered at this time for at least $1,476,490,844, the total amount of all undisputed claims on List 1 submitted by the Special Master. *See* Dkt. No. 1860, Ex. A. The Court should enter findings, as set forth below, in support of the entry of judgment. Defendants also agree that prejudgment interest should be awarded at a compounded rate but dispute the rate to be used. Under Seventh Circuit law, the Court has the discretion to calculate prejudgment interest at the average prime rate, compounded monthly from October 11, 2002 to the date of entry of judgment. Defendants urge the Court to reject the prime rate and award prejudgment interest based on one defendant's commercial paper borrowing rate. Although this Court has broad discretion, the adoption of defendants' refined rate setting will not adequately compensate the Class for its injury suffered at defendants' hands.

The most recent Seventh Circuit authority emphasizes that the focus should be on plaintiffs, not defendants, in providing full compensation. In addition, Household/HSBC Finance ended their commercial paper program in Q22012, and used other sources for its capital needs, at a higher interest rate. Household/HSBC's average cost of debt was much higher. Moreover, defendants focus on Household's short-term borrowing rate but fail to even address the borrowing rate of the other three defendants – Aldinger, Schoenholz and Gilmer. Defendants also fail to address the fact that two of these individual defendants sold Household stock to claimants at inflated stock prices and have had the use of the claimants' funds for over 12 years. Finally, in looking at the plaintiffs' borrowing rate, the average borrowing rate for the overwhelming majority of class members on List 1 undoubtedly exceeded the prime rate, which warrants using the prime rate in the calculation of prejudgment interest.

II. ARGUMENT

A. Judgment Should Be Entered

Defendants concede that entry of judgment pursuant to Rule 54(b) in favor of List 1 claimants is appropriate if their Post-Trial Motions are denied. Defs' Brf. at 4-7 (Dkt. No. 1875). The Seventh Circuit encourages district courts to provide their reasoning for entry of a Rule 54(b) judgment.[1] Accordingly, plaintiffs propose that the Court make the following findings supporting entry of a Rule 54(b) judgment if it denies defendants' Post-Trial Motions:

> (1) Judgment in favor of List 1 Claimants is final and there is no just reason for delaying entry of it. *See* Fed. R. Civ. P. 54(b).
>
> (2) The Court's denial of defendants' Post-Trial Motions renders a final decision as to the List 1 claimants. *See Bank of Lincolnwood v. Federal Leasing, Inc*., 622 F.2d 944, 947 (7th Cir. 1980). None of the issues remaining to be resolved in this Court as to non-List 1 claimants will affect in any way the List 1 claimants' rights or the entry of judgment in their favor. An order directing judgment in favor of List 1 claimants is therefore a final adjudication as to those parties. *See id*.; *Marseilles*, 518 F.3d at 463 (Rule 54(b) judgment is appropriate "when everything having to do with a particular party is wrapped up").
>
> (3) Consideration of the equities involved and judicial administrative interests indicate that there is no just reason to delay entry of judgment in favor of the List 1 claimants. *See Curtiss-Wright Corp. v. General Electric Co.*, 446 U.S. 1, 8 (1980).
>
> (4) The following equitable considerations favor immediate entry of judgment in favor of List 1 claimants:
>
> > (a) This case has been pending since 2002, and the jury rendered its verdict in favor of the Class in May 2009, over four years ago. *See Continental Datalabel*, No. 09-C-5980, 2012 U.S. Dist. LEXIS 173722, at *11 (fact that case has been pending for more than three years weighed in favor of entering Rule 54(b) judgment).

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[1] *See, e.g.*, *Marseilles Hydro Power, LLC v. Marseilles Land and Water Co.*, 518 F.3d 459, 463 (7th Cir. 2008) (noting that "the district court made the findings necessary to 'direct entry of a final judgment as to one or more, but fewer than all, claims or parties'" by resolving the particular claims and making explicit findings as to why there was no just reason for delay) (citation omitted); Fed. R. Civ. P. 54(b) (requiring court to "expressly determine[]" that there is no just reason for delay); Defs' Brf. at 6 n.3. *See also Continental Datalabel, Inc. v. Avery Dennison Corp.*, 09-C-5980, 2012 U.S. Dist. LEXIS 173722, at *2-*12 (N.D. Ill. Dec. 7, 2012) (setting forth the court's rationale for entering Rule 54(b) judgment).

(b) The ability of List 1 claimants to collect from the Household defendants will likely be impaired by further delay of judgment in their favor. *See Curtiss-Wright*, 446 U.S. at 12-13; *Lincolnwood*, 622 F.2d at 949, 951.

(c) The List 1 claimants' substantial financial interest in a $1.477 billion judgment and the amount of time necessary to adjudicate defendants' unresolved objections to the List 2 claims, List 4 claims and 20,000 additional claims militate in favor of entering judgment immediately for the List 1 claimants, whose claims have been fully and finally resolved. *See Curtiss-Wright*, 446 U.S. at 11; *Lincolnwood*, 622 F.2d at 951; *Continental Datalabel*, 2012 U.S. Dist. LEXIS 173722, at *11-*12. The claims remaining in this Court may not be resolved for many months, and there is no reason why List 1 claimants should be required to await resolution of those claims to have judgment entered in their favor, particularly given the length of time this action has been pending.

(d) The disparity in class members and damages represented by List 1 claimants is an additional equitable consideration favoring immediate entry of judgment. List 1 currently includes 10,902 claims valued at $1,476,490,844 before interest, while the non-List 1 claims are valued at less than half that amount.

(5) Judicial administrative interests also favor immediate entry of judgment in favor of List 1 claimants because the non-List 1 claims remaining in this Court raise only reliance issues and ministerial objections to their individual claims, which are resolved as to the List 1 claimants. The remaining proceedings in this Court therefore "are quite unlikely to make the appeal moot or even affect the issues on appeal," so that "there is no reason to delay the appeal while they are resolved." *Parks v. Pavkovic*, 753 F.2d 1397, 1401-02 (7th Cir. 1985). *See also Lincolnwood*, 622 F.2d at 951. In fact, the reverse is true here. The issues raised in defendants' Post-Trial Motions are dispositive as to the entire class, not only the List 1 claimants, so that appellate rulings as to those issues may impact the claims remaining in this Court. It would better serve judicial administration to immediately seek appellate resolution of issues impacting the entire class.

B. The Post-Judgment Interest Rate Statute Does Not Apply to an Award of Prejudgment Interest

Defendants do not dispute that prejudgment interest is warranted in this case and that it should be compounded. Rather, defendants claim that the rate to be used in the calculation should be lower than the prime rate, arguing for the one-year T-bill rate set forth in the federal post-judgment statute – 28 U.S.C. §1961. However, the Seventh Circuit has clearly rejected applying the federal ***post-judgment*** interest statute (28 U.S.C. §1961) to any calculation of prejudgment interest. *See*

Gorenstein Enters. v. Quality Care-USA, 874 F.2d 431, 437 (7th Cir. 1989) (rejecting application of §1961 – "prejudgment interest is governed by federal common law, and the courts are free to adopt a more discriminating approach"); *In re Oil Spill by The Amoco Cadiz*, 954 F.2d 1279, 1332 (7th Cir. 1992) ("as we pointed out in *Gorenstein* when expressly disapproving use of the postjudgment rate for prejudgment interest, an involuntary tort creditor is not safe"); *Cement Div. Nat'l Gypsum Co. v. City of Milwaukee* ("*Cement II*"), 144 F.3d 1111, 1114 (7th Cir. 1998) ("our review is limited to whether the district court has reasonably applied the appropriate federal common law principles").[2] From *Gorenstein* to *Cement*, the Seventh Circuit has been clear that district courts should not be "straightjacket[ed]" and cautioned them "against the danger of setting prejudgment interest rates too low by neglecting the risk, often non-trivial, of default." *Gorenstein*, 874 F.2d at 437.

C. The Court Has the Discretion to Use the Average Prime Rate Since the Purpose Is to Fully Compensate Plaintiffs

Defendants cite to *Gorenstein*, *Amoco Cadiz*, and *Cement Div. v. City of Milwaukee*, 31 F.3d 581 (7th Cir. 1994) ("*Cement I*") but curiously fail to address the other decisions in the *Cement* litigation, including the later rulings by the U.S. Supreme Court, the district court and the Seventh Circuit Court of Appeals. The *Cement* case has a long history but is relevant to this analysis since one of the cases defendants fail to mention is apparently the last word from the Seventh Circuit on the appropriate test to use. The original issue in the *Cement* district court case was whether to award prejudgment interest. The district court denied prejudgment interest, but the Seventh Circuit reversed. *See Cement I*, 31 F.3d at 581. The United States Supreme Court affirmed the appellate court, holding that "the essential rationale for awarding prejudgment interest is to ensure that an injured party is fully compensated for its loss." *City of Milwaukee v. Cement Div., Nat'l Gympsum*

[2] Defendants' reliance on *In re Vivendi Universal, S.A. Sec. Litig.*, 284 F.R.D. 144 (S.D.N.Y. 2012) is misplaced. The *Vivendi* court was bound by the Second Circuit caselaw, which unlike the Seventh Circuit, applies the post judgment statute (§1961) to awards of prejudgment interest. *See* Defs' Brf. at 10 n.4.

Co., 515 U.S. 189, 195-96 (1995). Applying that standard on remand, the district court awarded $6.4 million in prejudgment interest on a damages settlement of $1.67 million, applying the prime rate instead of the City of Milwaukee's lower borrowing rate. *Cement Div. v. City of Milwaukee*, 950 F. Supp. 904, 912 (E.D. Wis. 1996).

In *Cement II*, the Seventh Circuit affirmed the district court's decision to award prejudgment interest at the prime rate and rejection of defendants' request that interest be awarded at defendants' lower borrowing rate. 144 F.3d at 1114-15. In doing so, the Seventh Circuit affirmed the principle stated in *Gorenstein* that "'the best starting point is to award interest at the market rate, which means an average of the ***prime rate*** for the years in question.'" *Cement II*, 144 F.3d at 1114 (court's emphasis, citation omitted). The Seventh Circuit in *Cement II* also reaffirmed its prior holdings in *Amoco* and *Gorenstein* that "the district court has the discretion ***not*** to engage" in refined rate setting and "'to use the prime rate for fixing prejudgment interest where there is no statutory interest rate.'" *Id.* (citing *Amoco*, 954 F.2d at 1332; *Gorenstein*, 874 F.2d at 436) (emphasis added). The Court noted that "'we have encouraged the use of the prime rate despite recognizing that it may miss the mark for any particular party.'" *Id.* (citing *Amoco*, 954 F.2d at 1332). In sum, the law is clear that the district court has the discretion to use the prime rate and need not engage in refined rate setting.

D. If "Refined Rate" Making Is Used, Household/HSBC Finance's Commercial Paper Short-Term Rate Should Not Be Used

If the Court is inclined to engage in a refined rate analysis, instead of using the prime rate, the Court should focus on the plaintiffs' borrowing rate, rather than defendants' because the objective is to fully compensate the victim. *See Cement*, 950 F. Supp. at 908. The emphasis from the Seventh Circuit in *Gorenstein* and *Amoco Cadiz* on the defendants' borrowing rate was "before the United States Supreme Court placed the emphasis upon the full compensation for the victim in *City of Milwaukee*." *Id.* at 909. On remand, after the Supreme Court's ruling in the same case, the

district court rejected setting the rate based on the City of Milwaukee's cost of capital that was lower than the prime rate because it would not result in full compensation for the plaintiffs. In that case, the City of Milwaukee's borrowing rate was lower than what private, commercial entities had to pay. *Id.* The district court also focused on the fact that the plaintiffs' cost of funds exceeded the prime rate so the defendants could not complain about an award based on the prime rate. *Id.*[3] Consistent with the Seventh Circuit's decision in *Gorenstein* and *Amoco Cadiz* that the Treasury Bill rate was too low to compensate plaintiffs, the district court rejected the lower city borrowing rate and used the prime rate. *Id.*

On appeal, the Seventh Circuit affirmed the decision by the district court to use the prime rate and affirmed the $6.4 million award in prejudgment interest on a damages award of $1.6 million. *See Cement II*, 144 F.3d 1111-12. The Seventh Circuit noted that the plaintiffs were not voluntary creditors of the City of Milwaukee, and the municipal rate is at best "'the minimum appropriate rate for prejudgment interest because the involuntary creditors might have charged more to make a loan.'" *Id.* at 1114 (citing *Amoco Cadiz*, 954 F.2d at 1331). The court upheld the trial court's rejection of the lower municipal rate since it did not provide full compensation to plaintiffs. *Id.* at 1115.

Despite the more recent Seventh Circuit decision in *Cement II*, defendants argue that the Court should engage in "refined rate" setting instead of using the prime rate. Defendants contend this Court should use the short-term commercial paper borrowing rate for Household (renamed HSBC Finance).[4] Of course, defendants cherry-pick Household's lowest possible borrowing cost

[3] In this case, it is impossible to know the borrowing rate of all class members on List 1. However, since the prime rate is only for creditworthy borrowers, it is likely that the plaintiffs' average rate is higher than the prime rate. Declaration of Bjorn I. Steinholt, CFA, filed herewith ("Steinholt 9/12/13 Decl."), ¶15.

[4] Defendants cite to the "coerced loan theory" in support of using defendants' short-term unsecured debt. *See* Defs' Brf. at 15 n.9 (citing *Knoll & Colon* article). However, the authors of that article point out that the underlying premise of their conclusion about using defendants' short-term borrowing rate is based on the suit

and do not even address the borrowing costs of the other three defendants – Aldinger, Schoenholz or Gilmer – which likely is above the prime rate. Defendant also argue that the cases plaintiffs cite to support the fact that defendants had the use of plaintiffs' funds do not apply because defendants did not have the use of plaintiffs' funds and were not "participants in the market who sold shares to claimants" at inflated prices. *See* Defs' Brf. at 8-9. Of course, the evidence showed the opposite, with defendants Gilmer and Schoenholz selling stock to claimants during the Damages Period of 3/23/01-10/11/02. *See* Defs' Ex. 763 (Gilmer sales on 7/18/01 of 25,000 shares for over $1.7 million); Defs' Ex. 797 (Schoenholz sales on 5/10/02 of 17,814 shares for $982,798).

Here, as in *Cement II*, the lower borrowing rate for Household/HSBC would not fully compensate plaintiffs. Defendants offer no valid reason why Household/HSBC's short-term commercial paper rate should be used. This litigation has gone on for more than 11 years, exposing plaintiffs to risks far greater and for far longer than Household/HSBC's short-term commercial paper lenders. As long-term "involuntary tort creditor[s]," plaintiffs were "not safe," especially when compared to Household/HSBC's short-term commercial paper lenders. *Amoco Cadiz*, 954 F.2d at 1332. Contrary to defendants' suggestion, the cases do not mandate use of the lowest rate or shortest term, even where refined rate setting is applied. The *Gorenstein* court refers to the "interest rate paid by the defendant for unsecured loans." 874 F.2d at 437. The *Amoco Cadiz* court refers to "the amount the defendant must pay for money" and notes that "Amoco has publicly traded notes and debentures." 954 F.2d at 1332. Notes and debentures are by definition longer term than short-term commercial paper. The first Seventh Circuit decision in *Cement I* did suggest that the Court could look at the short-term rate of the City, *Cement Division*, 31 F.3d at 587, but ultimately the Seventh

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being between plaintiffs and defendants that are both "publicly traded corporations with ready access to capital markets." Michael S. Knoll and Jeffrey M. Colon, The Calculation of Prejudgment Interest, at 6 (Faculty Scholarship, Paper 114, 2005), *available at* http://scholarship.law.upenn.edu/faculty_scholarship/114. The authors note that the conclusions must be modified if the plaintiff is an individual, that the defendants' unsecured borrowing rate would under-compensate such an individual plaintiff. *Id.* at 32.

Circuit in *Cement II* upheld the district court's use of the prime rate because the lower rate of the City did not adequately compensate plaintiffs. There is no clear indication that the ***shortest*** term rates, as opposed to short or medium term rates should be used in calculating defendants' costs of funds. For example, in 2003, Household/HSBC Finance had an average cost of debt of 3.4% which was twice the rate of HSBC Finance's commercial paper rate, with an even higher average rate for publicly traded debt. Steinholt 9/12/13 Decl., ¶9. There is also insufficient information provided to use Household's commercial paper rate, including the fact that the commercial paper program was terminated in the second quarter of 2012 and HSBC Finance began to rely on affiliates of HSBC for funding, which resulted in a higher interest rate than commercial paper. *Id.*

Adopting Household/HSBC's short-term commercial paper rate is also inappropriate to account for the risk of default in this case. HSBC Finance has a lower cost of borrowing because its parent (HSBC) supports it and implicitly guarantees the debt. In fact, HSBC, through itself and related entities has been supporting HSBC Finance for many years. *See* Q213 10-Q, at 95 (HSBC Finance owes $8.3 billion to HSBC subsidiaries; and $2 billion outstanding on a $4 billion credit facility); at 96 ("HSBC has historically provided significant capital in support of our operations and has indicated that they remain fully committed and have the capacity to continue that support"); at 99 ("our credit ratings are directly dependent upon the continued support of HSBC"); at 99 ("Any required funding has been integrated into HSBC North America's Funding plans and will be sourced through HSBC USA Inc. or through direct support from HSBC or its affiliates"). Unlike current creditors of HSBC Finance, plaintiffs as unsecured creditors do not have a backstop in HSBC Finance's parent, HSBC. Although HSBC is liable as a successor in interest due to its 2003 acquisition of Household, HSBC has in the past stated in its public filings that it does not recognize U.S. judgments (*see* 2008 HSBC Holdings PLC Annual Report, at 448) (attached as Ex. 1), although

it has taken that language out in its SEC filings since 2011. As a result, HSBC Finance's lower short-term borrowing rate is inappropriate to compensate plaintiffs for the risk of default.

The defendants point to the return of the S&P Financials index, asserting that it is similar to their commercial paper rate and arguing it is the correct barometer by noting that plaintiffs' expert Fischel used that index as an appropriate peer group. However, Fischel also used the S&P 500 index in his regression analysis. Dkt. No. 1876 at 8, 13 (citing trial testimony). A more appropriate benchmark would be the S&P 500 index which had a return of 158% and would result in a multiplier of 2.58. Steinholt 7/25/13 Decl., ¶1 n.2 (Dkt. No. 1871). Although class members purchased Household stock during the Class Period, it is speculative to assume they would have held Household for the entire 11 years or sold the stock and used the funds to invest in other similar financial stocks. Instead, it is more rational to assume that class members would have invested in other types of companies covered by a broad market index like the S&P 500. *See* Steinholt 9/12/13 Decl., ¶¶18-20. Despite this higher benchmark, the average prime rate is the more appropriate calculation method.

E. Prejudgment Interest Can Be Compounded Monthly Or Annually

The district court has the discretion to compound prejudgment interest monthly or annually. In support of annual compounding, defendants again cite to the ***postjudgment*** interest statute 28 U.S.C. §1961, which does not apply to prejudgment interest. The defendants also seek to place blame on plaintiffs for the 11-year duration of the case. Other than an unsupported statement about plaintiffs' "scorched earth approach to discovery" (*see* Defs' Brf. 16 at n.11), defendants provide no evidence that plaintiffs' conduct has been the cause of any undue delay. In sum, as set forth in the moving papers, it is well within the Court's discretion to compound prejudgment interest monthly.[5]

[5] Defendants dispute the starting point for calculation of prejudgment interest, arguing for an October 11, 2002 date instead of October 1, 2002 date suggested by plaintiffs. Although plaintiffs contended that October

III. CONCLUSION

The Court has the discretion to award prejudgment interest, and should calculate it at the average prime rate, compounded monthly, from October 11, 2002 to the date of Entry of Judgment.

DATED: September 13, 2013

Respectfully submitted,

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1 was appropriate because it was the date when all artificial inflation was removed from the stock, plaintiffs believe that the Court should use the more conservative October 11 starting date to avoid further litigation on this point.

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DECLARATION OF SERVICE

I, the undersigned, declare:

1. That declarant is and was, at all times herein mentioned, a citizen of the United States and employed in the City and County of San Diego, State of California, over the age of 18 years, and not a party to or interested party in the within action; that declarant's business address is 655 W. Broadway, Suite 1900, San Diego, California 92101.

2. That on September 13, 2013, declarant served by electronic mail and by U.S. Mail to the parties the following documents:

REPLY BRIEF IN SUPPORT OF PLAINTIFFS' MOTION FOR ENTRY OF JUDGMENT AND AN AWARD OF PREJUDGMENT INTEREST

The parties' e-mail addresses are as follows:

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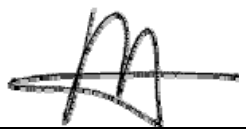
I declare under penalty of perjury that the foregoing is true and correct. Executed this 13th day of September, 2013, at San Diego, California.



Marianne Maloney