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.

PLAINTIFFS' OPPOSITION TO DEFENDANTS' MOTION TO EXCLUDE THE TESTIMONY OF PLAINTIFFS' EXPERT PROFESSOR DANIEL R. FISCHEL

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I. INTRODUCTION

Defendants' motion should be denied since Professor Fischel's methodology meets the *Daubert* standard and his opinions comply with the Seventh Circuit's directive. In his initial reports, Fischel employed a method accepted by the courts that involves the use of an event study to identify fraud related disclosures, and a regression analysis to estimate inflation (damages) from those statistically significant declines by excluding the effect of market or industry price declines. Fischel's traditional specific disclosure model clearly understated damages since its calculation of $7.97 of inflation was far less than the amount Household underperformed the market and its peers ($23.94). In fact, Household's stock price declined 53% – far in excess of the market (25%) and its peer group (21%) during the period of November 15, 2001 to October 11, 2002, when the fraud was disclosed (the "Disclosure Period" or "Leakage Period"). Due to extensive evidence of the "leakage" of the fraud, to which market participants – and the defendants themselves – attributed Household's stock price decline, rather than something else that was company-specific, Fischel also prepared a leakage model to estimate inflation.

The use of the leakage model is supported by academic literature and the Seventh Circuit in this case found it to be an appropriate way to show loss causation and measure damages. *Glickenhaus & Co. v. Household Int'l*, 787 F.3d 408, 421-23 (7th Cir. 2015). By definition, the leakage model includes all days during the Leakage Period – whether statistically significant or not. The Seventh Circuit's only criticism was that Fischel's opinion – that no significant nonfraud news specific to Household distorted his model – was too conclusory. *Id.* at 421-22. Fischel's Second Supplemental Report responded to the Seventh Circuit's opinion by analyzing ***all*** of the information disclosed on the 27 statistically significant dates where there were declines during the Leakage Period, in addition to the 10 fraud-related statistically significant stock price decline dates identified in his specific disclosure approach. After Fischel analyzed all of these dates, he concluded that only one date involved news that was specific to Household and unrelated to the fraud, but that decline was cancelled out two trading days later with a stock price increase, and, therefore, no adjustment to his leakage model is necessary. Under the Seventh Circuit's decision, it was then defendants' burden to identify firm-specific nonfraud information released on statistically significant dates that would support a showing that this nonfraud information caused Household's stock price decline. *Id.* at 422.

In response, defendants jettisoned their loss causation/damages trial expert Bajaj, and submitted reports from three new experts – Bradford Cornell, Allen Ferrell and Christopher James. Incredibly, despite the jury's finding of fraud, and the analyst consensus during the Leakage Period that Household's business was performing well but that its stock price was declining due to partial disclosures related to predatory lending, reaging, and the restatement, defendants' new experts maintain that investors suffered ***no*** damages. Cornell's report is a rehash of his prior submissions (made after the expert disclosure deadline) in support of defendants' prior *Daubert* and Rule 50 motions. The points Cornell raised – and repeats again – were rejected by Judge Guzmán. Ferrell and James both use the ***same*** methodology as Fischel, even using Fischel's regression method that employs the S&P 500 and S&P Financials Index as the market and peer variables. None of defendants' experts identify any significant negative news specific to Household that was ***not*** fraud related and caused its stock price to decline. This is not a surprise since the Seventh Circuit noted that "the defendants haven't identified any firm-specific nonfraud related information that could have significantly distorted the model." *Id.* Fischel's Second Rebuttal Report[1] addresses each piece of information defendants' experts claim is specific to Household and explains why it was either fraud related or not specific to Household since it was market or industry related.

In fact, the non-fraud Household-specific disclosures during the Leakage Period were overwhelmingly positive. During the Leakage Period, Household reported "record" financial results for three straight quarters, and based on those results securities analysts covering the Company touted

[1] The Second Rebuttal Report of Daniel R. Fischel, including exhibits, dated November 23, 2015, is attached as Ex. 1 to the Declaration of Luke O. Brooks in Support of Plaintiffs' Opposition to Defendants' Motion to Exclude the Testimony of Plaintiffs' Expert Professor Daniel R. Fischel, filed herewith ("Brooks Decl.").

Household's "strong outlook" and "recession proof" business model. Thus, Household's own disclosures about its operating performance completely contradict defendants' position that firm-specific performance was dragging down the stock. Instead, as Fischel demonstrates, analysts were lowering their earnings estimates and price targets for fraud-related reasons.

With nothing company-specific to show, both Ferrell and James point to various market- and industry-related news that was not specific to Household, and argue that Fischel used the wrong peer index. Defendants' prior expert Bajaj made the same argument (using a different group of companies), which was rejected by Judge Guzmán. The Seventh Circuit cited Fischel's peer index, comprised of the peer group Household compared itself to in its SEC public filings, with approval and held that "Fischel's models controlled for market and industry factors and general trends in the economy – the regression analysis took care of that." *Glickenhaus*, 787 F.3d at 421 (recognizing the "S&P Financials Index [is] an index of S&P 500 companies in the same industry category as Household"). *Id.* at 416.

In sum, Fischel's method is appropriate under *Daubert* and Rule 702, and complies with the Seventh Circuit's direction. His testimony should be presented to the jury.

II. ARGUMENT

A. Fischel Is Well Qualified to Render an Opinion in This Matter

Fischel is highly qualified to render an opinion in this case. In fact, "he's ***the*** expert for this kind of financial analysis"; defendants themselves "acknowledge Fischel's prominence in the field." *Glickenhaus*, 787 F.3d at 415 n.3 (emphasis in original). Fischel's seminal article on the fraud-on-the-market theory was cited by the Supreme Court, *Basic Inc. v. Levinson*, 485 U.S. 224, 246 n.24 (1988), and he has been qualified as an expert on loss causation and damages issues by courts around the country. 2nd Supp. Rpt., Appendix D.[2] In short, as the Seventh Circuit recognized, Fischel is "one of the best in the field" and more than qualified to render opinions on loss causation and damages. *Glickenhaus*, 787 F.3d at 412.

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[2] The Second Supplemental Report of Daniel R. Fischel, with exhibits, dated September 22, 2015 is attached as Ex. 2 to the Brooks Decl.

B. Fischel's Opinions Are Admissible Under Federal Rule of Evidence 702 and *Daubert* and Comply with the Seventh Circuit's Opinion

Rule 702 "requires that expert testimony be relevant, reliable, and have a factual basis." *Lapsley v. Xtek, Inc.*, 689 F.3d 802, 809 (7th Cir. 2012). The Court's gatekeeper role in evaluating the admissibility of expert testimony is not intended to supplant the adversary system or the role of the jury, including judgments as to "credibility and accuracy." *Id.* at 805. Instead, these issues are "to be tested before the jury with the familiar tools of 'vigorous cross-examination, presentation of contrary evidence, and careful instruction on the burden of proof.'" *Id*. (quoting *Daubert v. Merrell Dow Pharms.*, 509 U.S. 579, 596 (1993)).

It is also well settled that disputes about an expert's particular application of an accepted methodology go to the weight of the evidence, not its admissibility. *Manpower, Inc. v. Ins. Co. of Pa.*, 732 F.3d 796, 808 (7th Cir. 2013) ("The reliability of data and assumptions used in applying a methodology is tested by the adversarial process and determined by the jury; the court's role is generally limited to assessing the reliability of the methodology – the framework – of the expert's analysis."). Thus, the question here is whether Fischel has described "in nonconclusory terms the basis for [his] opinion" (*Glickenhaus*, 787 F.3d at 422), *i.e.*, "the framework," that he used in reaching his conclusion that significant company-specific non-fraud information did not impact his models.[3] Fischel has met this test.

1. The Seventh Circuit Endorsed Fischel's Loss Causation and Damages Methodologies

Fischel conducted two separate analyses to determine the amount of artificial inflation in Household's stock price and the causal link to the economic losses suffered by Class members as a

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[3] The Seventh Circuit's opinion contemplates that the jury, not the Court, will determine whether company specific non-fraud information impacted the leakage model after "plaintiffs' expert ***testifies***" on the subject. *Glickenhaus*, 787 F.3d at 422 (here, as elsewhere, emphasis is added and citations omitted unless noted otherwise). Thus, defendants' request for exclusion based on anything other than a methodological challenge under *Daubert* is improper.

result of the gradual revelation of defendants' fraud. Fischel Rpt., ¶¶30-42,[4] Brooks Decl., Ex. 4 (Trial Tr.) at 4289:9-4292:2.[5] The first analysis (the "specific disclosures" model) was an event study and via regression analysis found statistically significant declines caused by certain fraud-related disclosures. By using a market index and index of companies comparable to Household (peer index), Fischel removed the effect of any market and industry stock price declines from the damages calculation. Fischel Rpt., ¶¶30-33. These disclosures each revealed significant information about defendants' fraud pertaining to predatory lending, re-aging and accounting manipulations. Fischel Rpt., ¶¶34-37. In connection with this analysis, Fischel analyzed and rejected non-fraud reasons for Household's stock price decline. *See* Fischel Rebuttal Rpt.,[6] ¶¶20-24 & Appendix; 2nd Supp. Rpt., ¶4 n.4; 2nd Rebuttal Rpt., ¶¶102-117. As each piece of fraud related information came out, artificial inflation was removed from the stock. Using the specific disclosure analysis, Fischel identified a collective decline of artificial inflation of $7.97 even though Household declined by $32.70 (53%) during the Disclosure Period and vastly underperformed the peer group – the S&P Financials (21% decline) – identified in Household's SEC filings as the Company's stock performance peer group. Fischel Rpt., ¶29. The Seventh Circuit agreed that the specific disclosures model properly "identified 14 separate" corrective disclosures. *Glickenhaus*, 787 F.3d at 421. As the court held, "plaintiffs proved that Household's share price declined after the truth came out, so the problem identified in *Dura* is not present here." *Id*. at 420.

It is Fischel's expert opinion that the specific disclosures approach "significantly understates" damages because "a ***steady stream*** and ***extensive amount*** of incomplete information related to Defendants' alleged fraud was disclosed beginning at least as early as November 15, 2001 . . . but only some of these disclosures were associated with statistically significant residual returns."

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4 The Report of Daniel R. Fischel, dated August 15, 2007, is attached as Ex. 3 to the Brooks Decl. The exhibits were previously attached to Dkt. No. 1361-2.

5 Fischel's Second Supplemental Report incorporated his prior reports and trial testimony by reference. 2nd Supp. Rpt., ¶1 n.1.

6 The Rebuttal Report of Daniel R. Fischel, dated February 1, 2008, is attached to the Brooks Decl. as Ex. 5. The exhibits were previously attached to Dkt. No. 1361-6.

Fischel Rpt., ¶¶39-40. The Seventh Circuit agreed. *Glickenhaus,* 787 F.3d at 416 ("One problem with the specific-disclosure model is that the information contained in a major disclosure event often leaks out to some market participants before its release. If this happens, the model will ***understate*** the truth's effect on the price and thus the amount that the stock was overpriced before the truth became known."). For this reason, Fischel performed a second analysis, also an event study and regression analysis, which utilized a leakage model. Fischel Rpt., ¶¶38-42. The leakage model was published to address situations "in which fraud was revealed slowly over time, including one in which 'a slow flow of increasingly negative news fueled a rising tide of doubts and rumors' with the result that 'only a few dramatic announcements were associated with [statistically significant declines]'" and using residual price changes in those cases "'only on disclosure days will understate damages.'"[7] The leakage model quantified a cumulative drop in artificial inflation of up to $23.94 over the Disclosure Period of November 15, 2001 through October 11, 2002.

Fischel testified at trial that the leakage model provides "the better estimation of the inflation" because it "takes into account the economic reality" that negative news came out slowly over time. Ex. 4 (Trial Tr.) at 2855:8-23.[8] Fischel's opinion is supported by the "cascade of negative information that came out about HH" (*id.* at 2671:14-2672:15; *see also id.* at 2839:2-2840:17; Fischel Rpt., ¶12-29, 39), the overall 53% decline in Household's stock price, and its underperformance compared to the market and industry indices over that same period. Fischel Rpt., ¶29; 2nd Rebuttal Rpt., ¶8; Ex. 4 (Trial Tr.) at 2671:14-2682:2.

The evidence of leakage is overwhelming and plainly supports using the leakage model to estimate damages – "[d]efendants themselves produced an analysis at trial identifying 93 days on

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[7] Fischel Rpt., ¶38 (quoting Bradford Cornell & R. Gregory Morgan, *Using Finance Theory to Measure Damages in Fraud on the Market Cases,* 37 UCLA L. Rev. 883, 905-06 (1990) ("Cornell & Morgan")); *see also* 2nd Rebuttal Rpt., ¶¶9-10.

[8] *See also* Ex. 4 (Trial Tr.) at 2671:14-2672:15, 2675:21-2678:10; Ex. 6 (Fischel Depo. Tr.) at 165:10-16.

which fraud-related information was disclosed during the Leakage Period."[9] 2nd Rebuttal Rpt., ¶8; Brooks Decl., Ex. 7. The analysts covering Household, the company's investor relations department, defendants' now-abandoned trial expert Bajaj, and even Household's CEO, defendant Aldinger, all recognized that the company's underperformance during the Disclosure Period was caused by a steady and increasingly intense leakage of fraud-related disclosures. Fischel Rpt., ¶¶12-29, 39; 2nd Rebuttal Rpt., ¶8; Exs. 8-11. The Seventh Circuit agreed, finding the leakage model was supported by "***evidence that the content of the disclosures was leaking out to the market gradually prior to their release.***" 787 F.3d at 421.[10]

The Seventh Circuit endorsed Fischel's leakage model, rejecting defendants' myriad "broad[] attack[s]." 787 F.3d at 413. After concluding that both the Supreme Court and the Seventh Circuit have "generally recognized that the truth can leak out over time," and that "other circuits have acknowledged the viability of the leakage theory," the court expressly rejected defendants' argument that the model must "perfectly exclude" all firm-specific non-fraud related factors "that may have contributed to the decline in a stock price," because such a requirement "likely would doom" any practical application of "the leakage theory as a method of quantifying loss." *Id.* at 422.[11]

The court reversed and remanded, however, because it found that Fischel's testimony that the quantification including leakage was not distorted by firm-specific non-fraud disclosures was too "general on this point." *Id.* Rather than require "perfect[] exclu[sion]" of any and all firm-specific non-fraud impact, the court required Fischel to account for "***significant*** negative information about Household unrelated to [fraud-related] corrective disclosures (and not attributable to market or industry trends)." *Id.* at 419. Because such information would "overstate the effect of the

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[9] Had those dates been included in the specific disclosures quantification the inflation would have been $7.00 more. 2nd Rebuttal Rpt., ¶8 at n.12 (citing Trial Tr. at 2628:22-2629:12).

[10] In addition to Fischel's testimony, the Seventh Circuit cited the following evidence: "e-mails and reports from Household executives attributing the entirety of the stock's decline to the fraud-related disclosures," "reports from market analysts primarily focused on this information," and additional "evidence loosely corroborat[ing] the inflation figure produced by the leakage model ($23.94)." *Id.* at 420.

[11] The court also held that defendants' *Comcast* argument "doesn't require us to wholly reject the leakage model." *Id.* at 423 ("the point is that the problem doesn't defeat the expert's model"). *Id.* at 424.

disclosures and in turn of the false statements" only if it was significant, the court required defendants "to shoulder the burden of identifying some ***significant***, firm-specific, nonfraud related information that could have affected the stock price" upon Fischel's satisfactory "explain[ation] in nonconclusory terms [of] the basis for [his] opinion." *Id.* at 419, 422 (distinguishing cases that rejected various applications of the leakage theory to prove loss causation, in part, because "defendants [here] haven't identified any firm-specific, nonfraud related information that could have ***significantly distorted*** the model"). As the court held, "[i]f they can't," – or if Fischel "account[s] for that specific information" – "then the leakage model can go to the jury." *Id.* at 422.[12]

Thus, Seventh Circuit was clear that Fischel need not address and account for all possible negative information. Instead, the court held, the results of Fischel's model would only be distorted by the existence of one or more negative disclosures that met all of the following criteria: (a) "significant"; (b) "about Household"; (c) "unrelated to the[] corrective disclosures" (*i.e.*, the fraud); and (d) even if about Household, "not attributable to market or industry trends." *Id.* at 419.

As discussed below, Fischel complied with the first step of the Seventh Circuit's test by explaining in non-conclusory terms the basis for his opinion that no adjustment is required to the leakage quantification that he presented at trial due to significant firm-specific, non-fraud information. 2nd Supp. Rpt., ¶¶3-70. In response, defendants sought to establish through their three new experts that the leakage quantification and the specific disclosure quantification were significantly impacted by company-specific non-fraud disclosures. Fischel's Second Rebuttal Report shows that defendants have not met their burden. Thus, Fischel's testimony is admissible, and plaintiffs have satisfied all the requirements set forth by the Seventh Circuit to present the leakage model to the jury.

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[12] The court noted that "[o]f course, this can cut both ways. If during the relevant period there was significant ***positive*** information about Household, then the model would ***understate*** the effect of the disclosures." *Id*. at 419 (emphasis in original). As explained below, the significant positive information about Household more than cancelled out the impact of any such negative information.

2. Fischel's Second Supplemental Report Describes in Non-Conclusory Terms the Basis for His Opinion that the Leakage Model's Results Are Not Distorted by Firm-Specific Non-Fraud Disclosures

In his Second Supplemental Report, Fischel did precisely what the Seventh Circuit required; he "explain[ed] in nonconclusory terms the basis for [his] opinion." *Glickenhaus*, 787 F.3d at 422. Using the well-accepted event study methodology, Fischel "analyzed whether there were any days on which 'significant, firm-specific, nonfraud related information was released' that could reasonably explain the statistically significant residual declines in Household's stock price during the period from November 15, 2001 through October 11, 2002 (the 'Leakage Period')." 2nd Supp. Rpt., ¶3. Fischel analyzed all of the available news on each day (and the days before and after) there was a statistically significant stock price decline. 2nd Supp. Rpt., ¶¶5-70. With the exception of one day, there were no days on which significant non-fraud company-specific information caused, using well-accepted econometric principles, a stock price decline. *Id.* That decline was cancelled out by a related increase two trading days later. Thus, Fischel concluded that "beginning on March 28, 2001," the first date the jury found defendants liable for all three prongs of the fraud, "no adjustment to the Quantification Including Leakage [Fischel] presented at trial is required." 2nd Supp. Rpt., ¶4. His analysis is both well-accepted in the academic literature and satisfies the standard laid out by the Seventh Circuit.

Defendants contend that Fischel's testimony should be excluded because his report is too cursory, but Fischel has plainly explained why his model is not "significantly distort[ed]" by any significant company-specific non-fraud information. Indeed, Fischel performed the same event study analysis approved by numerous courts as the "gold standard, which is accepted by both courts and economists" for determining what caused economic loss in open-market stock-fraud cases. Dkt. No. 1527 at 2 (order denying defendant's first *Daubert* motion to exclude Fischel) (collecting cases and academic literature); *see also* 2nd Rebuttal Rpt., ¶1 n.4. Consistent with the event study methodology, Fischel examined "the association between news about [Household] (good, bad, or neutral) and stock price movements" on the days Household's stock declined significantly.[13] Dkt. No. 1527 at 2; 2nd Supp. Rpt., ¶¶3-70. Damages experts in open market securities fraud cases almost always use an event study to identify statistically significant stock price reactions and then apply their expertise to analyze whether the decline was caused by fraud or non-fraud related disclosures. Whereas event studies are normally used to establish a connection (or lack thereof) between company-specific ***fraud-related*** news and price declines, they are equally effective in determining whether company-specific ***non-fraud*** related news caused price declines. 2nd Rebuttal Rpt., ¶1 n.4. In either case, "'[t]he researcher is examining whether the association between news and share price movements is strong enough to support an inference of, among other things, causation.'" Dkt. No. 1527 at 2 (quoting Marge S. Thorsen *et al.*, *Rediscovering the Economics of Loss Causation*, 6 J. Bus. & Sec. L. 93, 99 (2006)).[14]

In conducting his analysis, Fischel first identified all of the days during the Disclosure Period on which Household's stock price had a statistically significant decline. 2nd Supp. Rpt., ¶3. Fischel analyzed only days that are statistically significant since, in the absence of leakage, it is well established that in order to attribute a stock price decline on a single day to market disclosures, that decline must be statistically significant. *Use of Modern Finance Theory in Securities Fraud Cases Involving Actively Traded Securities*, 38 Bus. Law. 1, 19 (1982) (Brooks Decl., Ex. 14); Fischel Rpt., ¶¶31-33; 2nd

[13] Thus, defendants' argument that Fischel's analysis is "not peer reviewed" is incorrect. Even if it were accurate, defendants' argument would not be determinative under *Daubert*. *Smith v. Ford Motor Co.*, 215 F.3d 713, 720 (7th Cir. 2000) (reversing order excluding proposed experts on the grounds that neither expert's methodology had been peer reviewed and noting "lack of peer review will rarely, if ever, be the single dispositive factor that determines the reliability of expert testimony").

[14] In their prior, unsuccessful (and unappealed) attempt to exclude Fischel's testimony, defendants argued, relying on an affidavit submitted by Cornell, that Fischel's leakage model had "no support in the scientific community," as Cornell had explicitly "rejected" Fischel's application of the leakage model in this case. *See* Dkt. No. 1364 at 33-36; Dkt. No. 1458-2 at 2, 18. Judge Guzmán considered and rejected this argument. *See* Brooks Decl., Ex. 12 (table listing arguments in defendants' motion that were previously raised and rejected). Defendants' attempt to raise this argument again runs afoul of this Court's Order limiting defendants' arguments to those "that were not raised before and rejected by Judge Guzmán." Dkt. No. 2042 at 6; *see also Lapsley*, 689 F.3d at 808 ("defendant[s'] disagreement with [an expert's] theory on causation [can] not be the sole reason for excluding it").

Rebuttal Rpt., ¶119 n.58.[15] Furthermore, as discussed, the Seventh Circuit repeatedly emphasized that only "significant" non-fraud information and "significant distortion" of the leakage model's results need to be accounted for (787 F.3d 419, 421-23); as the court held, "perfect exclu[sion]" is not required. *Id.* at 422. Fischel identified the statistically significant declines by referencing the event study presented in his original expert report. 2nd Supp. Rpt., ¶3. To determine whether the decline on each day could be explained by company-specific non-fraud related information, Fischel next analyzed more than 15,000 pages of market evidence, comprising all available media about Household from six comprehensive databases.[16] 2nd Supp. Rpt., Ex. 2.[17] Finally, for each of the statistically significant declines Fischel presented the results of his analysis. 2nd Supp. Rpt., ¶¶5-70.

Only one statistically significant price decline during the Disclosure Period, on January 11, 2002, was caused by the release of significant firm-specific non-fraud information – Fitch's revision of its long-term Rating Outlook to Negative from Stable resulting from Fitch's belief that Household had not "'demonstrated adequate market accessibility . . . which could be tapped in times of stress.'" *Id.*, ¶¶5-6. However, this price decline did not require an adjustment to the Leakage Quantification – let alone "significantly distort[] the model" (*Glickenhaus*, 787 F.3d at 421-22) – because two trading days later, analysts refuted Fitch's analysis, concluding that Household's "funding vulnerability" was "quite low" and pointing out that two other rating agencies which continued to give Household stable outlooks had factored any funding vulnerability into their ratings. 2nd Supp. Rpt., ¶¶5-7. This news caused Household's stock price to rebound. *Id.*, ¶¶7-8. As Fischel explained, the

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[15] By definition, days that are not statistically significant are appropriately included in the calculation under the leakage model in cases where, as here, "[t]he combination of the significant stock price decline, the concurrent leakage of fraud-related information, and market participants' attribution of the decline to this fraud-related information is strong economic evidence" that the Company's underperformance during the Leakage Period "was caused by leakage of artificial inflation from the price." Fischel Rpt., ¶39; *see also* 2nd Rebuttal Rpt., ¶¶17, 118-120.

[16] The databases are Dow Jones Factiva, LexisNexis, Bloomberg, Thomson Research's Investext Investment Research, Reuters Knowledge, and S&P Capital IQ. *Id.* at 5 n.6

[17] Defendants did not submit the Second Supplemental Report's exhibits with their motion. Plaintiffs have attached the Second Supplemental Report's Exhibit 2, which identifies the 15,000 pages of documents Fischel analyzed to reach his conclusion. *See* Brooks Decl., Ex. 13. Plaintiffs also have lodged with the court a disc containing those documents.

cumulative impact of those two days was not statistically significant, and thus "the positive nonfraud information 'cancelled out' the negative nonfraud information." *Id*.[18]

Defendants contend Fischel did not provide "specificity or ***actual*** methodological analysis of the non-fraud firm-specific information that could have affected Household's stock during the disclosure period." Defs' Mem. at 9 (Dkt. No. 2059) (emphasis in original). Defendants are incorrect. As explained, Fischel used the event study methodology. As for specificity, Fischel set forth the precise information he analyzed to reach his conclusion that non-fraud company-specific information did not impact Household's share price – more than 15,000 pages of analyst reports and news media – and provided all of the documents he analyzed to defendants with his report. 2nd Supp. Rpt., ¶6 n.6 & Ex. 2. His results are detailed in 66 paragraphs in the Second Supplemental Report. *Id.*, ¶¶5-70.

The court wanted Fischel to explain "in nonconclusory terms ***the basis*** for this opinion." 787 F.3d at 422. He has done this. Defendants, or anyone else looking at Fischel's reports, can easily understand what was done and, if they desire, replicate the analysis. In fact, that is precisely what defendants' three new experts did after receiving Fischel's report. Ferrell, hired by defendants to testify that the leakage quantification "could have" or "may have" been impacted by company-specific non-fraud related disclosures, took the same approach as Fischel. Ferrell Rpt., ¶¶56-118 (Dkt. No. 2060-3). He reviewed the news on each of the relevant days and drew conclusions based upon his economic judgment. *Id.*[19] In his Rebuttal Report, Fischel addressed all of the information Ferrell and defendants' other experts claim is company-specific, non-fraud, and "could have" impacted Household's stock

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[18] Defendants and their new experts insist that the residual decline from these two dates was $0.27, and therefore the Leakage Quantification must be adjusted. Defs' Mem. at 12 n.5. As Fischel explains in his Second Rebuttal Report, "the net effect of these two price movements is not statistically significant, and hence there is no reliable evidence that the net effect of this firm-specific, non-fraud related information caused any 'significant distortion' of my Quantification Including Leakage." 2nd Rebuttal Rpt., ¶18 n.24. In addition, there was another residual stock increase of $1.22 that was firm-specific and non-fraud on June 11, 2002 when Household announced the planned sale of $1.3 billion in asset backed securities secured by home equity loans. Plfs' Trial Ex. 1391 at 39 (Dkt. No. 1880-3); 2nd Rebuttal Rpt., ¶18 n.24. Thus, the net effect due to this category of firm-specific non-fraud information was positive. In any event, the model can be adjusted to eliminate the impact of any significant firm-specific non-fraud disclosures that distorted the model's result. 2nd Rebuttal Rpt., ¶17 n.23.

[19] Like Fischel, Ferrell did not regurgitate every piece of information during the Leakage Period, which would have been impractical.

price, and explained why it did not. 2nd Rebuttal Rpt., ¶¶9-127. As Fischel showed, defendants failed to supply any reasonable explanation for Household's substantial underperformance during the Leakage Period other than the revelation of their fraud. *Id.*

Defendants also contend Fischel's testimony should be excluded because his methodology for assessing whether firm-specific non-fraud related information significantly impacted the leakage quantification is too subjective. Defs' Mem. at 14-16. This argument simply repackages the primary argument defendants advanced on appeal, "that to be legally sufficient, ***any*** loss-causation model must ***itself*** account for, and perfectly exclude, any firm-specific, nonfraud related factors that may have contributed to the decline in a stock price." *Glickenhaus*, 787 F.3d at 422 (emphasis in original). The Seventh Circuit rejected defendants' proposed requirement that the model – as opposed to an expert's other forms of analysis – must be the exclusive means to address impact from firm-specific non-fraud information as too stringent, in favor of the "middle ground" approach detailed in the opinion. *Id*. The court expressed concern that because "[i]t may be very difficult, if not impossible, for any statistical model" to eliminate the impact of significant company-specific non-fraud related information (if any existed), "[a]ccepting the defendants' position likely would doom the leakage theory as a method of quantifying loss causation" – an untenable result under Supreme Court and Seventh Circuit precedent "recogniz[ing] that the truth can leak out over time." *Id*.

The court's "middle ground" approach plainly contemplates that Fischel's conclusion will rely in part on his expert judgment as to whether non-fraud related information significantly distorted his model – the court safeguarded that process by requiring him to explain the basis for his opinion "in nonconclusory terms." *Id*.[20] Experts often exercise their judgment, and ***always*** must do

[20] As *Bricklayers & Trowel Trades Int'l Pension Fund v. Credit Suisse Secs. (USA) LLC*, 752 F.3d 82, 96 (1st Cir. 2014), cited by defendants, held, "'the question of admissibility must be tied to the facts of a particular case.'" *Id.* at 93. The "subjective analysis" criticized in *Bricklayers*, cited by defendants, was an allocation, without any basis, of specific portions of single-day, statistically significant, stock price declines between fraud and non-fraud company specific factors simultaneously announced to the market. *Id.* at 96. This is far different from using expert judgment, as Fischel did here, to determine whether information in the market is company-specific or relates to the fraud. Here, there was no need to parse single-day declines, because such an exercise is inapplicable to the leakage

so in assessing what caused a particular stock-price decline – no model can do that. *Id.* at 422; accord Dkt. No. 1527 at 2 (rejecting defendants' prior *Daubert* challenges to Fischel's use of event study methodology and finding, "[t]o the extent that defendants take issue with Fischel's analysis, they are, in essence, questioning the validity of the use of an event study to establish materiality and causation"); *see also* 2nd Rebuttal Rpt., ¶1 n.4.[21] Notably, defendants and their experts fail completely to identify any alternative methodology that Fischel should have employed to identify significant company-specific non-fraud disclosures, suggesting instead that there are no damages at all from defendants' fraud.

3. Fischel's Analysis Properly Tests for the Possible Impact of Significant Non-Fraud Firm-Specific Disclosures on All Days of the Leakage Period

Fischel's Second Supplemental Report analyzes the days on which Household's stock price had statistically significant declines because the task at hand, as established by the Seventh Circuit, was to determine whether any ***significant*** firm-specific non-fraud related disclosures distorted his leakage model. 2nd Supp. Rpt., ¶3. This does not mean that Fischel ignored all other days or that Fischel attributed to the fraud inflation from declines caused by significant company-specific non-fraud disclosures. Defendants' argument to the contrary ignores the purpose of the leakage model and

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quantification, and there is no need to parse any of the specific declines in the specific disclosures quantification since there was no company-specific non-fraud information released on any of those days.

[21] The orders defendants cherry-pick discussing Fischel are inapplicable. As noted above, Fischel is one of the preeminent loss causation experts in the field. In addition to the Seventh Circuit's recognition of Fischel's expertise in this case, dozens of courts have admitted Fischel as an expert. Fischel Rpt., Ex. 1 (Dkt. No. 1361-2); 2nd Supp. Rpt., App. D. To the extent any of defendants' cases can be construed as precluding Fischel from exercising his expert judgment in determining whether the leakage model was distorted, they conflict with the Seventh Circuit's opinion, which is the law of the case. *See Glickenhaus*, 787 F.3d at 422. Additionally, these cases have no bearing on the question at issue – whether Fischel has the expertise and used a proper methodology to render opinions on loss causation and damages in this case – for "[t]he District Court applies the *Daubert* analysis to evaluate an expert on a case by case basis and [should] not [be] convinced to depart from that analysis by the finding of other Courts." *Demouchette v. Dart*, No. 09 C 6016, 2012 WL 6568232, at *7 (N.D. Ill. Dec. 14, 2012) (rejecting argument that plaintiffs' expert witness should be excluded because he was previously disqualified in a different case). Finally, the cases are distinguishable. In *United States v. Nacchio*, 555 F.3d 1234, 1258 (10th Cir. 2009), the court found that defendants' counsel failed to present evidence in support of Fischel's methodology or request an evidentiary hearing, not that Fischel's methodology was unreliable. In *SEC v. Dubovoy*, No. 15-6076, 2015 WL 6122261, at *2 n.3, *7-*8 (D.N.J. Oct. 16, 2015), the court did not exclude Fischel, but in its fact-finding capacity was not persuaded by Fischel's opinions. *In re Pfizer, Inc. Secs. Litig.*, No. 04 Civ. 9866, slip op. at 1-2 (S.D.N.Y. May 21, 2014), which is pending on appeal in the Second Circuit, Fischel's testimony concerned adjustments to the specific disclosures methodology, not a leakage analysis.

"is implausible on its face given the massive evidence of leakage of the fraud." 2nd Rebuttal Rpt., ¶¶6, 17. Defendants contend it is improper to include net inflation from (1) 171 days without a statistically significant decline ***and*** (2) all statistically significant days on which Fischel has not expressly attributed the full decline to the fraud. This argument amounts to nothing more than a contention that the leakage model is inappropriate under any circumstances – if these categories were excluded, only the specific disclosures would remain. Since the Seventh Circuit rejected this argument, it is not grounds for Fischel's exclusion.

Citing Fischel's article, *Use of Modern Finance Theory in Securities Fraud Cases Involving Actively Traded Securities*, 38 Bus. Law. 1, 19 (1982) (Brooks Decl., Ex. 14), defendants contend that "with respect to the 171 days in which there was no statistically significant residual price movement, there is no proper scientific basis to attribute stock price movement to an alleged disclosure of the fraud." *See* Defs' Mem. at 13 n.6, 18, 21. Defendants raised the exact same argument in support of exclusion the last time around, claiming that the leakage model improperly attributed to the alleged fraud all residual stock price declines on every day, including the "171 days" on which there was no statistically significant price movement, in violation of "well-accepted" tenets of economics. In support, defendants even cited the very same article authored by Fischel that they rely on here. Brooks Decl., Ex. 12. Given that this argument was "raised before and rejected by Judge Guzmán," this Court should decline to consider it again. Dkt. No. 2042 at 6.

Incredibly, moreover, defendants' quotation of Fischel's article omits a critical qualifier to his statement that "'[i]f the difference between the actual return and the predicted return is not statistically significant, investors were not injured.'" Defs' Mem. at 18. The omitted footnote reads: "***This statement assumes that there has been no leakage of information*** . . . ." 2nd Rebuttal Rpt., ¶119 n.58; Brooks Decl., Ex. 14. Thus, far from proving an inconsistency, Fischel's article demonstrates that for more than 30 years Fischel has recognized in his academic writing that defrauded investors can be injured through leakage of the truth, even in the absence of statistically significant declines.[22] Respected economists who have studied the subject agree; thus, "[a]s Professor Cornell acknowledges in his published work, the existence of leakage is widely recognized in the academic literature." 2nd Rebuttal Rpt., ¶7 & n.9 (citing Cornell & Morgan).

Thus, while true that "it would not ordinarily be possible, absent the overwhelming evidence of leakage in this case, using standard methodology to attribute the price movement on any day or combination of days to any particular cause," it is appropriate to include the 171 days with no statistically significant price decline in the model in this case "[b]ecause of the overwhelming evidence of leakage and the ***absence*** of any showing of firm-specific, nonfraud related information that 'significantly distorted' [Fischel's] Quantification Including Leakage." 2nd Rebuttal Report, ¶119. Fischel properly "included these 171 days in [his] inflation calculation by cumulating the residual returns on these days." *Id.*

For the 27 statistically significant decline dates that are at issue, defendants contend that there are 15 days (including July 1, 2002, July 9, 2002, and July 10, 2002) on which Fischel was unable to identify the disclosure of any fraud-related information. Defendants argue it is improper for Fischel to opine that these price movements are nonetheless caused by the fraud, and therefore account for $21.40 of the inflation, as doing so violates "fundamental financial principles." *See* Defs' Mem. at 4, 12, 15, 17. First, defendants previously raised the same argument, asserting that for certain days on which Fischel identified a statistically significant price decline (*e.g.*, July 9, 2002 and July 10, 2002), Fischel did not attribute the decline to any corrective disclosures, or the release of any other information regarding Household or the consumer finance sector in general. Brooks Decl., Ex. 12. Just as they argue now, defendants claimed then that the leakage model improperly attributed these declines to the alleged fraud nonetheless. *Id.* Judge Guzmán rejected this argument, which defendants have improperly re-raised here. Dkt. No. 1527.

[22] Fischel's testimony in the *Nacchio* case is inapplicable and irrelevant for the same reason. *See* Defs' Mem. at 18 and Exhibit B. Like the hypothetical addressed in *Use of Modern Finance Theory*, and unlike this case, in *Nacchio* "there ha[d] been no leakage of information." Brooks Decl., Ex. 14.

Second, defendants' assertion that these 15 days "account for $21.40 of the inflation that Fischel attempts to ascribe to the fraud under his leakage model" (Defs' Mem. at 12) misconstrues how the leakage model quantifies inflation. Among other things, this assertion (which not even defendants' three hired experts support) ignores that those declines are more than netted out of the leakage model's inflation quantification by more than $30.00 of increases from statistically significant positive news.[23] Indeed, as Fischel demonstrated in his Second Rebuttal Report, "the cumulative residual price change . . . is a ***positive*** $0.31" for the days on which defendants contend Fischel "provided no information consistent with leakage." 2nd Rebuttal Rpt., ¶120. In other words, if all of those days were excluded, damages would go up. *Id.* In sum, defendants refuse to acknowledge that the leakage model, accepted by the Seventh Circuit, incorporates the premise that there is leakage of the fraud, and all days during the Leakage Period are properly included unless there is evidence of significant Household specific non-fraud news that caused the stock price decline on that day. However, defendants' refusal to acknowledge well-accepted economic principles is not grounds for *Daubert*.[24]

4. Fischel's Second Supplemental Report Is Consistent with His Past Reports and Testimony

Defendants argue that Fischel's Second Supplemental Report conflicts with his prior testimony, but Fischel has never opined or testified that there were numerous significant, non-fraud, Household-

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[23] As the Seventh Circuit points out, "[i]f during the relevant period there was significant ***positive*** information about Household, then the model would ***understate*** the effect of the [fraud related] disclosures." *Glickenhaus*, 787 F.3d at 419 (emphasis in original).

[24] The loss causation cases defendants cite in their brief address the traditional specific disclosure analysis and are not applicable. The Seventh Circuit in this case stated the rule for leakage analysis, and Fischel followed it. 787 F.3d at 422 (the model itself need not "perfectly exclude" the impact of all company specific non-fraud information). For example, the discussion of "confounding information" in *Bricklayers*, 752 F.3d at 95, relates to a single "event date" under the traditional specific disclosures methodology, employed in the absence of leakage evidence. Furthermore, the holding defendants cite from *Bricklayers* was derived from *In re Williams Sec. Litig.-WCG Subclass*, 558 F.3d 1130, 1137 (10th Cir. 2009), a case the Seventh Circuit found inapplicable to this case because "[h]ere, . . . the plaintiffs identified 14 separate disclosure events, and they also presented evidence that the content of the disclosures was leaking out to the market gradually." *Glickenhaus*, 787 F.3d at 421. In *Bricklayers*, moreover, the defendants "made a thorough presentation of the alleged problems of each event date" (*Bricklayers*, 853 F. Supp. 2d at 96), whereas, here, "the defendants haven't identified any firm-specific, nonfraud related information that could have significantly distorted the model." *Glickenhaus*, 787 F.3d at 422. Thus, *Bricklayers*, like the other cases defendants cited on appeal that the Seventh Circuit found inapplicable, and unlike this case, involved "firm-specific nonfraud-related information that was both ***clearly identified*** and ***significant*** in proportion to the [fraud related] disclosures." *Id.* at 421.

related disclosures during the Leakage Period. Defendants' attempt to argue otherwise distorts Fischel's testimony. Even if it were accurate, defendants' argument would bear only on Fischel's credibility, not his opinions' admissibility. *Deputy v. Lehman Bros., Inc.*, 345 F.3d 494 (7th Cir. 2003).

Fischel agreed during his deposition that there were "a bunch of" statistically significant stock price movements under his "regression analysis"; however, this unremarkable concession has no relevance to Fischel's conclusion that firm-specific non-fraud information did not distort his leakage model. The question and answer relate to the "regression analysis," a study that covered the three-year class period, a much broader time period than the Leakage Period. 2nd Rebuttal Rpt., ¶117 n.55 (citing Fischel Dep. Tr. at 51:10-57:16, 144:22-147:9). Importantly, Fischel's "inflation calculations do not attribute any of the numerous statistically significant stock price movements outside of the Leakage Period to fraud related disclosures." *Id.* Furthermore, the answer covers both positive and negative stock price movements, and movements based on company-specific and non-company-specific news. Whereas there are "a bunch" of disclosures during the Class Period that fit into one or more of these broad categories, there is only one that fits into the far narrower category relevant to this motion: significant, negative, company-specific, non-fraud, and made during the Leakage Period.[25] Defendants also point to Fischel's trial testimony that "under the leakage model, whether they did – whether they were purely fraud related, combined fraud related or not at all fraud related, they were all included in the leakage model." Defs' Mem. at 10 (citing Trial Tr. at 2960:14-17). Again, the question and Fischel's answer relate to the entire event study, and thus the whole Class Period, not the just the Leakage Period.[26] Finally, the trial testimony that the Seventh Circuit quoted (*Glickenhaus*, 787 F.3d at 419-20) and defendants repeat in their brief (Defs' Mem. at 10

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[25] Likewise, Fischel's agreement in his deposition that there were "more things going on with respect to Household than just the things that are related to plaintiffs' allegations here in terms of statistically significant price movements" (Defs' Mem. at 10 (quoting Fischel Dep. Tr. at 146:21-147:2)), encompassed the whole Class Period (not just the Leakage Period), and included both positive and negative price movements. 2nd Rebuttal Rpt., ¶117 n.57.

[26] As the trial transcript makes clear, Fischel was responding to a line of questions about his entire "regression analysis" similar to the question defendants asked during his deposition. Brooks Decl., Ex. 4 (Trial Tr.) at 2959:24-2960:6.

(citing Trial Tr. at 2683-84)) ***was*** about company-specific news during the Leakage Period, but ***was not*** limited to statistically significant disclosures. 2nd Rebuttal Rpt., ¶119 n.60.

In short, Fischel never testified that there were numerous statistically significant, firm-specific, negative non-fraud disclosures during the Leakage Period. Thus, Fischel's conclusion that only one statistically significant stock price decline occurred during the Leakage Period ***and*** was caused by a firm-specific non-fraud related disclosure is perfectly consistent with his prior testimony. *Id.* So is his conclusion that the disclosure was "cancelled out" a few days later. *Id.*, ¶8.

In any event, the Court should decline defendants' invitation to draw conclusions about Fischel's credibility because such determinations are not properly part of the court's *Daubert* inquiry. It is axiomatic that credibility determinations are the province of the jury. *Deputy*, 345 F.3d 494; *see also Lapsley*, 689 F.3d at 805. In *Deputy*, for example, the Seventh Circuit reversed the district court's exclusion of expert witness testimony because the court "went beyond determining admissibility and focused on credibility." 345 F.3d at 507. Here too, it would be error to exclude Fischel's testimony even if the testimony defendants cite actually conflicted with his Second Supplemental Report – which it does not.

C. Defendants Have Not Identified Significant Firm-Specific Non-Fraud Factors that Were Not Already Accounted for by Fischel's Model

Because Fischel "explain[ed] in nonconclusory terms the basis for [his] opinion," the burden shifted to defendants to establish that significant non-fraud firm-specific disclosures caused Fischel's models to materially overstate the damages. *Glickenhaus*, 787 F.3d at 422. Defendants failed to meet this burden. Instead, defendants levy the same broad attacks on the models themselves that the Seventh Circuit rejected in upholding the leakage model's validity. For the 171 days on which there was no statistically significant decline, defendants simply argue that there is no basis to attribute the decline to the fraud. These arguments ignore the overwhelming evidence of the truth's leakage into the market, supporting the conclusion that the residual decline during the 171 non-statistically significant days is the result of leakage of the fraud. 2nd Rebuttal Rpt., ¶¶118-123. For the specific days defendants do address – the 27 other statistically significant decline dates and six of the ten specific disclosure decline dates – defendants' experts have failed to show that any significant company-specific non-fraud factor was the cause of Household's residual stock price decline. *See* 2nd Rebuttal Rpt., ¶¶18-117.

1. Defendants' Arguments About Fischel's Index Were Previously Raised and Rejected and Do Not Demonstrate Significant Distortion of the Leakage Model

The Seventh Circuit was clear that defendants had to provide "significant negative information about Household unrelated to these corrective disclosures (and not attributable to ***market*** or ***industry trends***)." 787 F.3d at 419. Yet, defendants point to various market and industry-related news and argue that it is somehow specific to Household and a few other subprime lenders because Fischel uses the wrong industry index (the S&P Financials). Specifically, defendants' new experts contend Fischel should have used the nine firms in the Credit Suisse First Boston Specialty Finance Universe (Ferrell) or four firms in the consumer finance subsector of the S&P Financials Index (James). *See* Ferrell Rpt., ¶42; James Rpt. (Dkt. No. 2060-4), Ex. 4. Based on the opinion of defendants' prior expert Bajaj, who used a different group of six companies as his purported peer index, defendants made the same argument about the use of the wrong peer index in the prior *Daubert* motion. Dkt No. 1364 at 21, 29-31, 45 n.18 ("By focusing only on broad market indexes, Professor Fischel failed to consider the impact of consumer finance-specific news on Household's stock price . . . ."); Bajaj Rpt. at 79-82 (Dkt. No. 1416-7). The Court rejected this argument, and defendants did not appeal the *Daubert* order. Dkt. No. 1527. As a result, defendants are not allowed to raise this issue again. Dkt. No. 2042 at 6.

In any event, the argument is no better this time around. First, defendants' argument that Fischel did not select the right peer index for his regression goes to weight rather than admissibility, and thus cannot provide grounds for exclusion under Rule 702 or *Daubert*. *Manpower*, 732 F.3d at 808 ("[T]he Supreme Court and this Circuit have confirmed on a number of occasions that the selection of the variables to include in a regression analysis is normally a question that goes to the probative weight of the analysis rather than to its admissibility.") Second, as Fischel previously demonstrated in his reports and testimony, the event study "controlled for market and industry factors and determined whether residual stock price changes were statistically significant." 2nd Supp. Rpt., ¶3. The Seventh Circuit agreed: "Fischel's models controlled for market and industry factors and general trends in the economy – ***the regression analysis took care of that***." *Glickenhaus*, 787 F.3d at 421; *see also id.* at 416 (finding that "the S&P Financials Index [was] an index of S&P 500 companies ***in the same industry category as Household***"). Furthermore, Fischel explains why his use of the S&P Financials Index was proper. 2nd Rebuttal Rpt., ¶¶9-12. Fischel's regression analysis already accounts for industry and market news so that any stock price declines due to these factors are not included in the inflation (damages) calculation. *Id.*

Although defendants' new experts offer different indices than the one Bajaj previously championed, the results are the same. Fischel tested the relevance of the newly proposed industry indices by analyzing whether Household's stock price underperformed these groups of firms during the Leakage Period. 2nd Rebuttal Rpt., ¶11. While Household's stock declined 53.2% during the Leakage Period, the indices of firms identified by Ferrell and James declined 19% and 16.3%, respectively. *Id.* This confirms market participants' conclusions that Household's larger stock price decline was due to concerns about their unique predatory lending problems, reaging manipulations masking their credit quality, and the implications of the restatement. *Id.* Fischel also analyzed whether the newly-suggested indices in "the leakage model significantly distorts the results," by incorporating the companies identified by Ferrell and James into his regression model. *Id.*, ¶12. It did not. In fact, inclusion of those indices resulted in ***higher*** maximum damages than estimated by Fischel's model – $27.52 and $27.60 versus $23.94.[27] *Id.*, Ex. 3. In sum, the industry or macroeconomic factors defendants claim are non-fraud and Household-specific are really industry or market factors already accounted for by Fischel's model.

Defendants' reliance on *Hubbard v. BankAtlantic Bancorp., Inc.*, 688 F.3d 713 (11th Cir.

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[27] Neither Ferrell nor James actually provide an alternative regression analysis that incorporates what they consider to be an appropriate industry index showing that Household did not decline more than its peers.

2012), in support of the use of a different peer index is misplaced. Whereas the court in *BankAtlantic* found that the defendant company was disproportionately impacted by the local Florida real estate market so that an index of national companies was not comparable, in this case Household compared itself in its public filings to diversified financial companies – "banks, thrifts, insurance companies, credit unions, mortgage lenders and brokers, finance companies, securities brokers and dealers." *See* 2nd Rebuttal Rpt., ¶125 n.66. Defendants' SEC filings compared Household to the broader S&P Financials Index as its peer index. As such, the index used by Fischel properly captured the issues unique to Household, and excluded any decline caused by market or industry issues. The factual situation in *BankAtlantic* is not present in this case.

2. Defendants' Other Attempts to Demonstrate that Significant Firm-Specific Non-Fraud Related Information Distorted the Leakage Model on Days With Statistically Significant Declines Are Unavailing

Defendants claim the following types of information are significant, non-fraud, Household-specific, and caused Household's stock price decline: (1) disclosures regarding Household's liquidity, access to capital markets, and widening bond spreads; (2) disclosures regarding credit quality; (3) disclosures relating to increased capital requirements for subprime lending institutions; (4) disclosures and concerns regarding future regulatory and legislative changes; (5) disclosures relating to Household's auto and credit business lines; (6) the impact of a "double-dip" recession on consumer lenders servicing subprime lenders; and (7) "random noise" with respect to stock price movement. Defs' Mem. at 20-22. However, these categories of information were either fraud related, or were not specific to Household, instead impacting all companies or Household's peers.

The following categories of information – (3) increased capital requirements for subprime lending institutions, (4) regulatory issues not specific for Household, and (6) macroeconomic factors impacting all lenders (*i.e.*, "double-dip" recession) – are not specific to Household but rather are market or industry related and Household stock price declines are accounted for by Fischel's use in his regression analysis of the S&P 500 and S&P Financial Index, an index Household compared itself to in its SEC filings. 2nd Rebuttal Rpt., ¶¶13-14, 24-27, 52-57. Household itself denied that any regulatory changes would have any effect on its business. *See* 2nd Rebuttal Rpt., ¶14. To the extent any regulatory action would be taken specifically against Household, that was clearly related to the fraudulent predatory lending practices. *Id.* With respect to the increased capital requirements, Household denied on the July 17, 2002 quarterly conference call that it would have any impact on Household and analysts did not think this industry issue applied to Household. *Id.*, ¶53. If anything, regulatory inquiry was related to Household's predatory lending practices. *Id.*, ¶55. The "double-dip" recession is also a market factor impacting all companies, including Household's peers. *Id.*, ¶56.

The other types of information raised by defendants' experts are also not company-specific, non-fraud disclosures. For example, analysts and the defendants themselves attributed Household's widening bond spreads and issues with access to capital and liquidity (category 1 above) to accounting and predatory lending concerns were being raised by analysts, and Household's restatement, which all were fraud related. *See* 2nd Rebuttal Rpt., ¶13 (citing October 11, 2002 Moody's report that legal liability for "predatory lending abuses pushed the company's bond spreads out to unprecedented levels and raised market concerns about funding access over time"); ¶24 & n.30 (citing February 8, 2002 *Chicago Sun-Times* article and statement by defendant Schoenholz to Dow Jones connecting Household liquidity issues to accounting concerns); ¶¶93, 53, 107 (Schoenholz admitting the "implication of the restatement" on capital); ¶¶13, 93 (connecting widening bond spreads to predatory lending concerns).

Any credit quality issues or rising credit losses in Household's auto business (categories 2 and 5 above) are either industry issues, immaterial, or related to Household's fraudulent re-aging practices that took place in connection with Household issuing predatory loans. 787 F.3d at 413 ("[T]he company's growth was driven by predatory lending practices. This, in turn, increased the delinquency rate of Household's loans, which the executives then tried to mask with creative accounting."); *see also* 2nd Rebuttal Rpt., ¶¶70, 84, 113. Analysts agreed. *Id.*, ¶115 (citing September 22, 2002 CIBC report ("mounting credit quality concerns related to Household's loan workout and re-aging practices have also been a drag on the stock"); ¶84 n.42 (citing September 18, 2002 UBS report that pointed out the issues of Americredit were not applicable to Household because, among other reasons, "[a]uto loans currently represent only 6.5% of [Household's] managed portfolio whereas Americredit is primarily an auto lender").

Finally, defendants' argument that "random noise" (category 7 above) is somehow responsible for Household's stock decline during the 171 non-statistically significant days was previously raised by defendants and their expert Cornell and rejected. Dkt. No. 1364 at 29. It is also without merit since, as even defendants' prior expert Bajaj admitted, most of the information disclosed during this period was fraud-related. 2nd Rebuttal Rpt., ¶8 n.12.

Defendants' position is also entirely at odds with the repeated positive announcements Household made about its business during the Leakage Period. Again, as Fischel demonstrates, Household's stock price declined ***much*** further during the Leakage Period than the indices defendants propose. Yet Household did not have a single negative "firm-specific, nonfraud related information about its business performance that can explain" the stock's underperformance. 2nd Rebuttal Rpt., ¶¶15, 16. To the contrary, Household continued to report "simply outstanding," "record" financial results for three straight fiscal quarters, including "[e]xceptional revenue growth," a "stable portfolio of loans," and strong growth projections despite an uncertain economic environment. *Id*. Analysts, too, noted the Company's solid fundamentals, "strong outlook," and "recession proof" business model, while at the same time lowering valuations because of "persistent" risks arising from market talk of Household's possible engagement in predatory lending and accounting manipulations. *Id*. Defendants agreed at the time that Household's stock price was being hurt by fraud related issues and not their general business results. *Id.*, ¶8 & n.13.

3. Defendants Have Not Shown that Significant Firm-Specific Non-Fraud Information Caused the Declines on Any of the Specific Disclosure Days

With respect to the six corrective disclosure dates in the specific disclosure model challenged by defendants, they have failed to identify non-fraud Household-specific factors that were the cause of the residual stock price decline. *See* 2nd Rebuttal Rpt., ¶¶102-117. The issues defendants raise were either: (1) industry or market news not specific to Household, or (2) were related to the fraud. *Id*. Defendants' prior expert, Bajaj made the same type of challenge, and this attack was not accepted by the Court at the *Daubert* stage. Bajaj Rpt. at 23-28, 31-37, 48-65; Dkt. No. 1527. Defendants' new expert also fails in his challenge. 2nd Rebuttal Rpt., ¶¶102-117.

III. CONCLUSION

For the foregoing reasons, defendants' motion to exclude Fischel should be denied in its entirety.

DATED: November 23, 2015

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on November 23, 2015, I authorized the electronic filing of the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the e-mail addresses denoted on the attached Electronic Mail Notice List.

I certify under penalty of perjury under the laws of the United States of America that the foregoing is true and correct. Executed on November 23, 2015.

s/ Luke O. Brooks

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