

**UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF ILLINOIS  
EASTERN DIVISION**

LAWRENCE E. JAFFE PENSION PLAN, On )	Lead Case No. 02-C-5893
Behalf of Itself and All Others Similarly )	(Consolidated)
Situated, )	
	) <u>CLASS ACTION</u>
Plaintiff, )	
	) Judge Ronald A. Guzman
vs. )	Magistrate Judge Nan R. Nolan
	)
HOUSEHOLD INTERNATIONAL, INC., et )	
al., )	
	)
Defendants. )	
_____ )	

**DECLARATION OF AZRA Z. MEHDI IN SUPPORT OF FINAL APPROVAL  
OF THE PROPOSED SETTLEMENT WITH AUDITOR DEFENDANT  
ARTHUR ANDERSEN LLP**

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I, AZRA Z. MEHDI, declare as follows:

I am an attorney duly licensed to practice before all of the courts in the States of California, New York and in the Northern District of Illinois. I am a partner with the law firm of Lerach Coughlin Stoia Geller Rudman & Robbins LLP, Lead Counsel for the Class in the above-entitled action. I have personal knowledge of the matters stated herein and, if called upon, I could and would competently testify thereto. I submit this declaration in support of Lead Plaintiffs' Motion for Final Approval of the Settlement with Arthur Andersen LLP ("Andersen") as set forth in the Stipulation of Settlement dated as of June 16, 2005.

## **I. INTRODUCTION**

1. The purpose of this declaration is to set forth the nature of the investigation and negotiations that led to the settlement with Andersen, the former auditor of Household International, Inc. ("Household" or the "Company").<sup>1</sup> This declaration demonstrates why the settlement is fair, reasonable and adequate as to Andersen and should be approved by the Court.

2. The settlement with Andersen is for \$1.5 million in cash (the "Settlement Fund") and Andersen's agreement to cooperate with Lead Plaintiffs in ongoing litigation against the Household Defendants<sup>2</sup> (the "Cooperation Component"). On May 23, 2005, Lead Counsel participated in an arm's length mediation session with all defendants under the supervision of retired United States District Court Judge Layn Phillips. The mediation and subsequent extensive negotiations culminated in this partial settlement, which confers an immediate and substantial benefit on the Class and eliminates the risk of lengthy litigation under circumstances where a favorable outcome against an

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<sup>1</sup> This declaration focuses primarily on events and discovery related to Lead Plaintiffs' case against Andersen. Discovery is ongoing with respect to the remaining defendants.

<sup>2</sup> The "Household Defendants" are Household, Household Finance Corporation ("HFC") and William F. Aldinger, David A. Schoenholz, Gary Gilmer and J.A. Vozar (the "Individual Defendants").

auditor defendant cannot be assured. The \$1.5 million Settlement Fund was deposited into an interest bearing escrow account for the benefit of the Class on December 16, 2005.

3. This declaration is intended to provide the Court and Class Members with facts sufficient to determine that the Class claims against Andersen have been thoroughly explored and aggressively pursued and that the settlement with Andersen consisting of the \$1.5 million Settlement Fund and the Cooperation Component is in the best interest of the Class.

4. Lead Plaintiffs reached this partial settlement only after the following events gave Lead Plaintiffs and Lead Counsel grounds to believe a \$1.5 million cash settlement and Andersen's cooperation with Lead Plaintiffs' ongoing litigation against the Household Defendants is in the best interest of the Class:

(a) An extensive factual investigation was conducted prior to filing the [Corrected] Amended Consolidated Class Action Complaint for Violations of the Federal Securities Laws (the "Consolidated Complaint") on March 13, 2003. The investigation included, among other things, a review of SEC filings issued by Household and HFC, as well as regulatory filings and reports, news articles, securities analyst reports, advisories about the Company, press releases and other public statements issued by the Company or its representatives, media reports about the Company, and interviews of, among others, former Household employees and other persons with knowledge of defendants;

(b) Lead Plaintiffs and Lead Counsel consulted extensively with Lead Plaintiffs' forensic accountants concerning Andersen's adherence to accounting guidelines and regulations;

(c) Lead Plaintiffs and Lead Counsel consulted extensively with Lead Plaintiffs' damages and materiality consultants to assess the extent of losses suffered by the Class and Andersen's potential provable responsibility for such losses;

(d) Lead Plaintiffs and Lead Counsel evaluated the current financial condition of Andersen, which ceased operations, relinquished or consented to revocation of its firm permits and liquidated the majority of its assets in August 2002;

(e) Counsel for Andersen represented in the Initial Disclosure filed by defendant Andersen pursuant to Rule 26(a)(1) of the Federal Rules of Civil Procedure: “There is no insurance agreement under which any person carrying on an insurance business may be liable to satisfy part or all of a judgment which may be entered in the action or to indemnify or reimburse for payments made to satisfy the judgment.” Counsel for Andersen additionally represented to Lead Counsel that there was no insurance coverage for any claims filed after May 31, 2002;

(f) Lead Plaintiffs and Lead Counsel researched the law and evidence relating to Lead Plaintiffs’ claims and Andersen’s defenses;

(g) Lead Plaintiffs and Lead Counsel filed a detailed Consolidated Complaint with allegations based on Lead Plaintiffs’ investigation that the Court found sufficiently particularized in denying both the Household Defendants’ and Andersen’s motions to dismiss;

(h) After defendants’ motions to dismiss were denied and formal discovery was permitted, Lead Counsel issued document and other discovery requests to Andersen and the other defendants, subpoenaed numerous third parties, including Household’s current auditor KPMG LLP (“KPMG”), and reviewed nearly four million pages of documents produced by Household, Andersen, and various third parties;

(i) After Lead Plaintiffs filed a motion for class action certification and the parties engaged in certain class certification-related discovery, the parties entered into a stipulation

certifying a class of all persons who purchased or otherwise acquired Household securities during the period beginning October 23, 1997 through and including October 11, 2002;<sup>3</sup> and

(j) The parties participated in a mediation session before the Honorable Layn Phillips. While no settlement was reached with the Household Defendants, Lead Plaintiffs successfully negotiated a settlement with Andersen that is favorable to the Class.

5. The Settlement Fund will be held in escrow and will be distributed, subject to Court approval, or as otherwise ordered by the Court, in connection with a future settlement or judgment against the Household Defendants in this Litigation.

6. The settlement is contingent on Andersen's continued cooperation with Lead Plaintiffs in their prosecution of this action against the Household Defendants.

7. Lead Counsel intend to postpone their Fee and Expense Application and is not making such an application in connection with the approval of this partial settlement.

## **II. HISTORY OF THE ACTION**

### **A. Summary of Lead Plaintiffs' Claims Alleged in the Consolidated Complaint**

8. This action is brought on behalf of all persons who purchased or otherwise acquired publicly traded securities of Household during the period beginning October 23, 1997 through and including October 11, 2002 (the "Class Period").<sup>4</sup>

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<sup>3</sup> On March 19, 2004, Judge Guzman denied Andersen's and the Household Defendants' motions to dismiss with respect to the violations of §10(b) and Rule10b-5 claims asserted in the Consolidated Complaint; and largely denied their motions to dismiss the claims for violations of §11, but eliminated certain time-barred §11 claims. On October 10, 2004, the parties entered a stipulation and [proposed] order regarding class action certification, which contained the definition of the Class. On June 30, 2005, the Household Defendants filed a motion to partially dismiss the Consolidated Complaint pursuant to a recent Seventh Circuit decision in *Foss v. Bear, Stearns Co.* Judge Guzman converted the motion to dismiss to a motion for judgment on the pleadings and on February 28, 2006, Judge Guzman dismissed with prejudice claims based on any misrepresentations or omissions that occurred before July 30, 1999. Consequently, the current operative class period is July 30, 1999 through October 11, 2002.

9. Household is a large consumer lender holding company that provides consumer loans, mortgage services, auto finance and credit insurance products, and credit card services. ¶¶7, 37.<sup>5</sup> Household's customer base is primarily composed of nonconforming, nonprime or subprime customers. ¶¶8, 107. Such customers generally have limited credit histories, modest incomes or high debt-to-income ratios or have experienced credit problems caused by occasional delinquencies, prior charge-offs or other credit-related actions. *Id.*

10. This securities fraud class action arises out of a massive scheme and wrongful course of conduct by defendants Household, certain of its senior officers, and the Company's auditor, Andersen, during the Class Period. Defendants' scheme allowed Household to report "record" financial results during the Class Period by, among other things:

- Engaging in illegal and deceptive lending techniques designed to maximize amounts loaned to subprime borrowers – without any regard to benefits to the borrowers – at unconscionable interest rates in violation of the Truth-in-Lending Act;
- Arbitrarily "reaging or restructuring" delinquent accounts to conceal true levels of defaults and delinquencies in order to manipulate and delay charging them off, thereby allowing the Company to maintain inadequate reserves in violation of Generally Accepted Accounting Principles ("GAAP"); and
- Manipulating the accounting of expenses associated with various credit card partnership agreements in violation of GAAP.

11. When defendants' fraud was ultimately uncovered, it cost shareholders billions:

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<sup>4</sup> Excluded from the Class are Andersen, the Individual Defendants, Household, members of the immediate families of the Individual Defendants, any entity in which Andersen, any Individual Defendant or Household has or had a controlling interest or which is related to or affiliated with Andersen, Household or any Individual Defendant, current or former directors and officers of Household or Andersen, and the legal representatives, heirs, successors, or assigns of any such excluded person or entity. Also excluded from the Class are those Persons who timely and validly request exclusion from the Class pursuant to the Notice of Pendency and Proposed Partial Settlement of Class Action.

<sup>5</sup> All paragraph ("¶\_\_") references are to the Consolidated Complaint filed on March 13, 2003.



- Defendants would pay \$484 million to the Attorneys General from all 50 states to settle charges that Household engaged in predatory lending tactics – resulting in a \$525 million charge to Household’s financials;
- Household entered into a Consent Order with the United States Securities and Exchange Commission (“SEC”) on March 18, 2003 in which defendants agreed to cease and desist from engaging in improper reaging of delinquent accounts to prevent or delay charge-offs; and
- Household restated its financials due to improper accounting of expenses – a \$600 million restatement that lowered earnings by \$386 million.

**B. The Parties**

12. On December 18, 2002, the Court appointed the Glickenhau Institutional Group comprising of Glickenhau & Company, PACE Industry Union Management Pension Fund (“PACE”) and The International Union of Operating Engineers Local No. 132 Pension Plan as Lead Plaintiffs pursuant to §21D(a)(3)(B) of the Securities Exchange Act of 1934 (“Exchange Act”), 15 U.S.C. §78u-4(a)(3)(B).

13. The defendants are Household, HFC, the Individual Defendants and Andersen.<sup>6</sup>

**C. The Commencement of the Action; Consolidation and the Appointment of Lead Plaintiffs**

14. On and after August 16, 2002, the following actions were filed in the United States District Court for the Northern District of Illinois as a securities class action on behalf of purchasers of Household securities during a defined period of time:

<b>Abbreviated Case Name</b>	<b>Case Number</b>	<b>Date Filed</b>
<i>Jaffe v. Household International, Inc. et al.</i>	02-CIV-5893	08/16/02
<i>Abrams v. Household International, Inc. et al.</i>	02-CIV-5934	08/20/02
<i>Eisberry Holdings, Ltd. v. Household</i>	02-CIV-6130	08/27/02

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<sup>6</sup> The Consolidated Complaint also named Household’s directors and two investment advisors, Goldman Sachs & Co., Inc., and Merrill Lynch, Pierce, Fenner & Smith, Inc., whose motions to dismiss were granted and who were dismissed on March 19, 2004.

<i>International, Inc. et al.</i>		
<i>Jannett v. Household International, Inc. et al.</i>	02-CIV-6326	09/05/02
<i>Dolowich v. Household International, Inc. et al.</i>	02-CIV-6352	09/05/02
<i>Hanschman v. Household International, Inc. et al.</i>	02-CIV-6859	09/25/02
<i>Friedel v. Household International, Inc. et al.</i>	02-CIV-7067	10/02/02

15. The above actions were consolidated by an order of the Court dated December 9, 2002. On December 18, 2002, the Court appointed Lead Plaintiffs and Lerach Coughlin Stoia Geller Rudman & Robbins LLP (formerly Milberg Weiss Bershad Hynes & Lerach LLP), Lead Counsel for Lead Plaintiffs and the Class.

**D. Lead Plaintiffs' Investigation and the Preparation of the Consolidated Complaint**

16. Prior to and after the Court appointed Lead Plaintiffs, Lead Plaintiffs and Lead Counsel conducted an extensive investigation to thoroughly understand: (1) the business of Household; (2) its competitors; (3) factors impacting its operation; (4) the Company's financial results prior to, during and after the Class Period; (5) the nature of the restatement; (6) Household's settlement with a multi-state group of attorneys general; (7) applicable provisions of GAAP, SEC rules and the Company's publicly reported accounting policies; (8) the price of the Company's stock before, during and after the Class Period; and (9) how the price of the Company's stock performed relative to its peer group and general market.

17. Specifically, Lead Plaintiffs' investigations encompassed among other things, the following in order to prepare a complaint that satisfied the stringent pleading requirement of the PSLRA:

- Researching defendants' public statements about Household, including statements made in conference calls, documents filed with the SEC, press releases and in analyst reports;
- Analyzing the restatement, including the determination of how the Company's originally reported financial results violated GAAP, SEC rules and Household's publicly reported accounting policies;

- Researching the compensation of the defendants and their job responsibilities prior to, during and after the Class Period;
- Researching the subprime lending industry;
- Reviewing analyst reports concerning Household and the subprime lending industry in general;
- Analyzing the price of Household stock, the stock of Household's peers and the changes in the NYSE and other stock markets;
- Interviewing individuals, including former employees of Household; and
- Preparing preliminary estimates of damages.

18. In addition, before the initiation of the Litigation and continuing throughout, Lead Counsel conferred with consultants with expertise in accounting issues and in analyzing potential recoverable damages and the materiality of defendants' statements – key issues of dispute between Lead Plaintiffs and all of the defendants.

19. Prior to the initiation of this Litigation and continuing throughout, Lead Counsel also consulted with forensic accountants about the alleged accounting improprieties, the restatement and factors that indicated the defendants knew or recklessly disregarded that their accounting practices violated GAAP, SEC rules and Household's publicly reported accounting policies, including the following:

- Assisting Lead Counsel on issues relating to GAAP, generally accepted auditing standards ("GAAS") and SEC rules applicable to this case, including Statement of Financial Accounting Standards ("SFAS") No. 5; American Institute of Certified Public Accountants ("AICPA") Audit and Accounting Guide Audits of Financial Companies with Conforming Changes as of 5/01/00, ¶¶2.114-2.118; SEC Regulation S-X, 17 C.F.R. §§210.4-01(a)(1), 210.10-1(a) and 229.303(a)(3); Financial Accounting Standards Board ("FASB") Statement of Concepts ("FASCON") 1 and 2; Accounting Principles Board ("APB") No. 20; SFAS No. 91; Emerging Issues Task Force Issue No. 93-1 ("EITF 93-1"), Accounting for Individual Credit Card Acquisitions; APB No. 28; Statement of Auditing Standards ("SAS") No. 32 and 82 (AU §§110, 150, 220, 316, 317, 431); Principles and Rules of the Code of Professional Code ("ET") §§53, 54, 55, 102, 501. ¶¶103-106, 126, 129-133, 142-144, 147-148, 153-155, 179, 182, 185-191.
- Assisting Lead Counsel in drafting accounting-related sections of the Consolidated Complaint;

- Assisting Lead Counsel in analyzing and responding to defendants' motions to dismiss;
- Assisting Lead Counsel in the preparation of document requests and subpoenas to the Company's auditors; and
- Assisting Lead Counsel in the evaluation of evidence obtained through discovery.

**E. Defendants' Motions to Dismiss the Consolidated Complaint**

20. On May 13, 2003, all defendants, including Andersen, moved to dismiss the Consolidated Complaint under Rules 12(b)(6) and 9(b) of the Federal Rules of Civil Procedure.

21. Andersen also moved to strike several paragraphs of the Consolidated Complaint under Federal Rule of Civil Procedure 12(f).

22. Andersen asserted that Lead Plaintiffs did not satisfy the standard of pleading securities fraud under the PSLRA and Federal Rule of Civil Procedure 9(b) against an auditor. Specifically, Andersen contended that Lead Plaintiffs had failed to plead facts regarding Andersen's alleged GAAP and GAAS violations or that Andersen's access to Household information was sufficient to give rise to a strong inference of scienter. Andersen asserted that Lead Plaintiffs' motive allegations were also insufficient to establish a strong inference of scienter against an auditor. Andersen also raised statute of limitations and loss causation as other bases to dismiss the claims against it.

23. On June 19, 2003, Lead Plaintiffs filed their oppositions to the defendants' motions to dismiss and to Andersen's motion to strike. Lead Plaintiffs detailed specific and particularized allegations in the Consolidated Complaint that satisfied both the Federal Rule of Civil Procedure 9(b) and the PSLRA with respect to falsity and were sufficient to raise a strong inference of scienter.

24. On March 19, 2004, the Court denied in part and granted in part the Household Defendants' motion to dismiss and denied in full Andersen's motion to dismiss and its motion to strike. *Lawrence E. Jaffe Pension Plan v. Household Int'l, Inc., et. al.*, 2004 U.S. Dist. LEXIS 4659 (N.D. Ill. March 19, 2004). With respect to Andersen, the Court concluded that Lead Plaintiffs'

Consolidated Complaint satisfied Rule 9(b) and the PSLRA's requirement for particularly pointing out misleading statements related to securities sales, indicating why they were material, and relating how the statements caused Lead Plaintiffs' damages. Accordingly, the Court held that Lead Plaintiffs had "articulated the who, what, when, where, and how of the fraud with sufficient particularity." *Id.* at \*24-\*25.

25. The Court also found that Lead Plaintiffs' motive and opportunity allegations were sufficient to raise a strong inference of scienter against Andersen. *Id.* at \*28-\*29. The Court also denied Andersen's motion to strike. *Id.* at \*54-\*55. Following the Court's denial of defendants' motions to dismiss the Consolidated Complaint, the Household Defendants and Andersen filed their answers to the Consolidated Complaint on July 2, 2004.

26. On March 7, 2005, one week after Lead Plaintiffs filed a motion to compel Andersen to produce witnesses for deposition and documents, Andersen filed a motion to dismiss in part Lead Plaintiffs' Consolidated Complaint or, in the alternative, for judgment on the pleadings. The parties were discussing participating in a formal mediation and on March 9, 2005, Andersen withdrew its motion to dismiss without prejudice to refile after the mediation.

## **F. Lead Plaintiffs' Formal Discovery**

### **1. Initial Disclosures**

27. On April 26 and May 18, 2004, the parties held their Fed. R. Civ. P. 26(f) conference. Following that conference, on June 25, 2004, Lead Plaintiffs, the Household Defendants and Andersen served their Rule 26 Initial Disclosures.

### **2. Document Requests Propounded by Lead Plaintiffs**

28. On May 17, 2004, Lead Plaintiffs served its first request for production of documents ("Document Request") to defendant Andersen. Andersen requested an extension to serve its objections and responses to the Document Request. In return for allowing Andersen to serve its

responses and objections past the 30 day deadline provided by the Federal Rules of Civil Procedure, Andersen agreed to produce to Lead Plaintiffs Andersen's 2001 audit workpapers prior to serving its objections and responses, which were served on July 9, 2004.

29. Andersen made numerous objections to Lead Plaintiffs' Document Request and did not indicate whether, when, or what documents it would produce. Lead Plaintiffs and Andersen engaged in multiple lengthy meet and confers to establish the scope, timing, and protocol for the production of Andersen's workpapers and other documents requested. Between August 17, 2004 and February 15, 2005, Andersen produced additional workpapers as well as documents responsive to certain of the requests. Andersen adamantly refused to produce documents responsive to a number of requests.

30. Upon agreeing to the settlement, Andersen has produced additional documents that it had initially refused to produce, including desk files and the table of contents of Andersen's Audit Objective and Procedures Manual. Additionally, Andersen has been more forthcoming about exchanging information regarding documents and other electronic discovery.

### **3. Protective Order**

31. Even prior to the production of documents, parties began negotiating the terms and scope of an appropriate protective order. Parties were unable to agree to the terms of the protective order and the dispute was submitted to Magistrate Judge Nan R. Nolan. After extensive briefing and pursuant to the November 1, 2004 Order by Judge Nolan, a protective order was entered on November 5, 2004.

#### **G. Andersen Depositions**

32. On June 9, 2004, Lead Plaintiffs served a notice of deposition of Andersen pursuant to Federal Rule of Civil Procedure 30(b)(6), noticing the deposition of one or more designees most

qualified to testify as to nine distinct subject matters. Andersen refused to produce a 30(b)(6) witness since Andersen, as a company, was no longer a going concern.

33. Consistent with the Cooperation Component of Lead Plaintiffs' settlement with Andersen, Andersen has been cooperating with Lead Counsel in locating relevant Andersen witnesses (who are no longer employed by Andersen since its August 31, 2002 dissolution of business) and accepting deposition subpoenas.

**H. Interrogatories Propounded by Lead Plaintiffs**

34. On July 16, 2004, Lead Plaintiffs propounded three interrogatories on Andersen. Andersen served their objections and answer on August 18, 2004, objecting to the interrogatories as premature and referring Lead Plaintiffs to Andersen's initial disclosures.

35. In light of the ongoing cooperation between the Class and Andersen, information is being exchanged formally and no additional interrogatories have been propounded.

**I. Third-Party Discovery Taken by Lead Plaintiffs**

36. In addition to discovery directed against the defendants, Lead Plaintiffs pursued discovery from various third parties, including Household's current auditor, KPMG LLP, a former Household branch manager, other plaintiffs who filed suit against Household based on similar factual allegations, and a former Household executive.

37. Lead Plaintiffs are still pursuing discovery from other third parties, including the Office of Thrift Supervision, Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation, Fitch, Moody's, S&P and several analysts.

38. During formal discovery, Lead Plaintiffs continued to pursue informal discovery from a number of different sources.

**J. Discovery Motions**

39. On March 1, 2005, Lead Plaintiffs filed a motion to compel Andersen to produce witnesses for deposition and documents. This motion was withdrawn once the Class had obtained the Cooperation Component in the settlement.

**K. Motion for Class Certification**

40. On June 30, 2004, Lead Plaintiffs filed its motion for class certification. Lead Plaintiffs produced documents and responded to interrogatories. The Household Defendants and Andersen deposed the designee for one of the Class representatives, PACE.

41. On October 8, 2004, the parties filed a stipulation and [proposed] order regarding class action certification, which was submitted to Magistrate Judge Nan R. Nolan. In an October 20, 2004 Minute Order, Judge Nolan instructed the parties to file their stipulation for class certification with Judge Guzman. The parties complied and filed a joint motion for entry of the stipulation and [proposed] order regarding class action certification on October 15, 2004, which was entered by the Court on December 3, 2004.

42. On August 16, 2005, the parties jointly moved for modification to the stipulation and order regarding class action certification, which was granted on August 22, 2005.

**III. SUMMARY OF EVIDENCE OBTAINED IN DISCOVERY**

43. Discovery – both formal and informal – was extensive and is continuing in this case. By the time the parties reached this partial settlement, Lead Plaintiffs had gained a better understanding of the strengths and weaknesses of the Class’s claims against Andersen.

44. Lead Plaintiffs and Lead Counsel believe that some of the discovery received and reviewed supports Lead Plaintiffs’ allegations against Andersen. Andersen’s workpapers reveal that during the Class Period, it frequently did not conduct its own examination and review of Household’s internal controls and processes, but instead relied on the results of Household’s internal



audits. The discovery to date suggests that Andersen may have violated auditing standards requiring the independent auditor to perform its own examination. *See* AU §333.02.

45. Discovery to date also suggests that Andersen recognized that Household had failed to establish any standard criteria for reages which could lead to questionable portfolio quality. Andersen was also aware of the very same reage policies and practices that the SEC later found constituted securities laws violations as disclosed by Household to the investing public in their SEC filings. Household was forced to amend its 2001 Form 10-K/A to disclose that under its restructure policies: (1) Household (or HFC) accepted one or zero payments prior to resetting the delinquency status, and (2) restructured delinquent accounts automatically. Documents suggest that Andersen noted that Household's monitoring controls surrounding the reaging process were only partially effective and identified instances where customers were reaged where they should not have been and that risks existed that accounts would be reaged against policy, either systematically by the software program or by manual intervention by collectors.

46. The evidence further supports that Andersen knew of Household's accounting manipulation that required the Company to restate its financial statements for 1993 – 2Q02. As author of Emerging Issues Task Force ("EITF") Issue 93-1, Accounting for Individual credit Card Acquisitions ("EITF 93-1"), Andersen knew that EITF 93-1 applied to Household's co-branded credit card agreement with General Motors. Discovery obtained thus far evidences that although Andersen believed that the General Motors partnership agreement should be accounted for under EITF 93-1, Household continued to account for the partnership as though EITF 93-1 never existed, and that Andersen continued to approve this GAAP violation.

47. Further, discovery obtained thus far also indicates that Household and Andersen knew that the accounting on the AFL-CIO "Union Privilege" affinity card portfolio and the credit card marketing agreement with Kessler Financial Services were in violation of GAAP. Household

arbitrarily increased the amortization period for the Union Privilege Affinity Agreement from 10 years to 15 years, without changing the amortization period for regulatory purposes.

48. In early 2002, Household terminated its engagement of Andersen as Household's outside auditor, hiring KPMG LLP instead. On August 14, 2002, KPMG required Household to issue a restatement reducing earnings by \$386 million for the years 1993 through 2Q02.

#### **IV. SETTLEMENT DISCUSSIONS WITH ANDERSEN**

49. As noted above, all parties participated in a May 23, 2005 mediation before the Honorable Layn Phillips. After a full day of negotiations that continued into the following week, Lead Plaintiffs and Andersen reached a settlement comprised of the cash Settlement Fund and the Cooperation Component.

#### **V. REASONS FOR THE SETTLEMENT**

50. As noted above, Lead Plaintiffs' reasons for settling this action include: (1) consideration of the assets available to satisfy any judgment, including Andersen's dissolution and the lack of insurance to cover claims filed after May 31, 2002, and the fact that Andersen may be judgment-proof by the time this case goes to trial; (2) the risk of proving Andersen's scienter; and (3) both the uncertainty about the level of provable damages against Andersen and, the risk of non-recovery if Andersen's arguments prevailed at trial or on a motion for summary judgment.

51. During the day of the mediation on May 23, 2005 and over the next couple of days, I spoke with authorized representatives of each of the Lead Plaintiffs to answer any questions that they may have regarding the proposed settlement with Andersen. They were familiar with the news of Andersen's business conditions. More importantly, each of the Lead Plaintiffs viewed the Cooperation Component of the settlement to be of significant value in light of the contested and hard fought discovery disputes that have been the norm throughout this Litigation.

**A. Assets Available to Settle**

52. It is well known, in August 2002, Andersen ceased its auditing operations and surrendered its firm licenses to practice as Certified Public Accountants in the United States. At the outset of the Litigation, counsel for Andersen had informed Lead Counsel that no insurance was available to cover claims in this Litigation and that Andersen had only few revenue-generating assets remaining. Andersen confirmed the oral representation regarding lack of insurance coverage in its initial disclosures. Andersen has also informed Lead Plaintiffs that there are numerous other ongoing litigations with significant claims against Andersen's limited remaining assets. Based on their own investigation and these representations, Lead Plaintiffs believe Andersen's cash contribution is appropriate under the circumstances. It is Lead Plaintiffs belief that in the absence of this settlement, it is likely Andersen would not have the assets available to satisfy any judgment obtained several years from now.

**B. The Risks As to Liability**

53. Lead Plaintiffs believe that there is compelling evidence showing that each of the defendants violated the Exchange Act by knowingly or recklessly causing Household to report materially false and misleading financial results. With respect to Andersen, an auditor defendant, however, Lead Plaintiffs recognize the difficulties of proof against auditors and that there is a risk the jury could find that Lead Plaintiffs failed to prove the state of mind necessary for Andersen's scienter, or that Andersen's level of fault was minimal. In addition, Lead Plaintiffs recognized that the costs of continuing to litigate the case through summary judgment and trial would increase the costs to the Class and, given Andersen's precarious financial situation, would likely not result in a significantly larger monetary recovery against Andersen and could result in no recovery against Andersen. Finally, Lead Plaintiffs also recognize that Andersen could and would likely appeal any verdict for Lead Plaintiffs and the Class.

**C. Uncertainty Regarding Provable Damages**

54. The parties continue to have widely divergent views on the measure of damages. Lead Plaintiffs recognize that even if the jury found that Andersen violated the Exchange Act, given that Andersen is an auditor defendant and will likely submit to the jury that it had been misled by the Household Defendants, or that Household had concealed material information from Andersen, there is a risk that the jury could find recoverable damages of less than \$1.5 million.

**D. Settlement Analysis**

55. Given these factors, the proposed cash settlement of \$1.5 million for the benefit of the Class and, more importantly, the Cooperation Component constitute an excellent result for Lead Plaintiffs and the Class. Because Andersen no longer operates and has no insurance that would cover any judgment against Andersen in this case, Lead Plaintiffs consider this settlement a very favorable outcome.

**VI. CONCLUSION**

56. For the reasons set forth above and in the accompanying memoranda, I respectfully submit that the settlement is fair, reasonable and adequate and should be approved.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed this 30th day of March, 2006, at San Francisco, California.

s/ AZRA Z. MEHDI  
\_\_\_\_\_  
AZRA Z. MEHDI

CERTIFICATE OF SERVICE

I hereby certify that on March 30, 2006, I electronically filed 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, and I hereby certify that I have mailed the foregoing document or paper via the United States Postal Service to the non-CM/ECF participants indicated on the attached Manual Notice List.

s/ JOY ANN BULL

JOY ANN BULL

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## Mailing Information for a Case 1:02-cv-05893

### Electronic Mail Notice List

The following are those who are currently on the list to receive e-mail notices for this case.

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