UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION

LAWRENCE E. JAFFE PENSION PLAN, ON BEHALF OF ITSELF AND ALL OTHERS SIMILARLY SITUATED, Plaintiff, - against - HOUSEHOLD INTERNATIONAL, INC., ET AL., Defendants.	Lead Case No. 02-C5893 (Consolidated) CLASS ACTION Judge Ronald A. Guzman Magistrate Judge Nan R. Nolan

REPLY MEMORANDUM OF THE NON-SETTLING HOUSEHOLD DEFENDANTS PURSUANT TO THE PSLRA WITH RESPECT TO PLAINTIFFS' PROPOSED SETTLEMENT WITH DEFENDANT ARTHUR ANDERSEN LLP

EIMER STAHL KLEVORN & SOLBERG LLP
224 South Michigan Ave.
Chicago, Illinois 60604
Suite 1100
(312) 660-7600

CAHILL GORDON & REINDEL LLP
80 Pine Street
New York, New York 10005
(212) 701-3000

Attorneys for Defendants Household International, Inc., Household Finance Corporation, William F. Aldinger, David A. Schoenholz, Gary Gilmer and J. A. Vozar

TABLE OF CONTENTS

TABLE OF AUTHORITIES

This reply memorandum is respectfully submitted on behalf of non-settling Defendants Household International, Inc., Household Finance Corp., William F. Aldinger, David A. Schoenholz, Gary Gilmer and J.A. Vozar (collectively, "Household" or the "Household Defendants") pursuant to the Private Securities Litigation Reform Act of 1995 ("PSLRA") with respect to Plaintiffs' proposed settlement with Arthur Andersen LLP ("Andersen").

INTRODUCTION

Plaintiffs' "motion to strike" is no more than a thinly veiled attempt to take yet another shot at the Household Defendants' fully submitted *Dura* Motion[1]—acknowledging thereby the strength of that motion and the weakness of their claims against **both** Andersen and the Household Defendants. Plaintiffs ask the Court to strike Defendants' Settlement Submission,[2] which specifically *does not object* to the proposed settlement. Plaintiffs do not contest the factual observations Defendants make concerning the proposed settlement. Plaintiffs just do not like the inescapable implications of those facts. Nonetheless, Defendants fully support Plaintiffs' proposed settlement with Andersen for the reason presented by Plaintiffs to the absent class members and to the Court: it fairly reflects the expected value of Plaintiffs' claims. Moreover, the proposed settlement is commensurate with any expected settlement with the Household Defendants.

---

1 "*Dura* Motion" refers to Household Defendants' Motion to Dismiss Based on the Supreme Court's Recent Decision in *Dura Pharmaceuticals, Inc.* v. *Broudo*.

2 "Settlement Submission" or "DSS" refers to Defendants' Memorandum of the Non-Settling Household Defendants Pursuant to the PSLRA with Respect to Plaintiffs' Proposed Settlement with Defendant Arthur Andersen LLP. Likewise, "Response" or "PR" refers to Lead Plaintiffs' Response to the Memorandum of the Non-Settling Household Defendants Pursuant to the PSLRA with Respect to Plaintiffs' Proposed Settlement with Defendant Arthur Andersen LLP.

ANALYSIS

I. Plaintiffs' Second Attempt Improperly to Supplement Their Response to the *Dura* Motion Is in Direct Violation of the Court's December 15, 2005 Ruling and Must Be Stricken

On December 13, 2005, Plaintiffs attempted to supplement their opposition to the *Dura* Motion by filing Plaintiffs' *Dura* Supplement.[3] In that filing, Plaintiffs asked the Court to take judicial notice of recent case law as well as additional facts *dehors* the Complaint[4]—two appended documents that Defendants had produced to Plaintiffs in the course of discovery (*See Dura* Supplement and Exhibits and Appendix thereto). On December 15, 2005, the Court, while agreeing to take notice of all case law, specifically refused to take notice of any documents *dehors* the Complaint (Tr. 16:1-18:3, Dec. 15, 2005), characterizing Plaintiffs' Supplement as an attempt to "supplement your argument by arguing other facts in support of your complaint that you had not previously argued which you think would establish a cause of action in the face of the challenge made by the defendants' motion to dismiss...." (Tr. 16:1-5, Dec. 15, 2005.)

Despite the Court's clear determination that such supplemental arguments and documents may not be submitted, Plaintiffs brazenly attempt to do just that, not only by supplementing their argument in the form of a four page tangent within their Response but also by appending to their Response *the exact same documents the Court has already rejected.* (PR at 3-6, Ex. A, B.).

This time Plaintiffs do not even attempt to rationalize their tactic with any case law. Instead, Plaintiffs masquerade this clearly improper submission as a necessary response to Defendants' Settlement Submission, which Plaintiffs posit (ironically) is an improper re-argument

---

3 "*Dura* Supplement" refers to Lead Plaintiffs' Notice of Recent Authority and Request for Judicial Notice in Further Support of Lead Plaintiffs' Response to Household Defendants' Motion Based on the Supreme Court's Decision in *Dura Pharmaceuticals, Inc. v. Broudo.*

4 "Complaint" or "AC" refers to Plaintiffs' Corrected Amended Consolidated Class Action Complaint for Violation of the Federal Securities Laws.

of the *Dura* Motion. (PR at 3-4.) Plaintiffs' characterization of Defendants' Settlement Submission as an attempt to reargue the *Dura* Motion is a transparent attempt to excuse their improper submission.

The substantive discussion of the *Dura* Motion contained in Defendants' Settlement Submission is limited to three sentences summarizing that pending motion and is mentioned as only one of the many factual and legal defects that have properly motivated Plaintiffs' settlement with Andersen. (DSS at 8.) Plaintiffs characterize this as an improper supplement to the pending *Dura* Motion and take it as their duty to "respond briefly." (PR at 4.) However, Plaintiffs' "brief response" is a four page diatribe—dwarfing all other sections of their Response—citing to case law, statutes, previous filings, and even the two previously rejected documents, which are once again submitted as exhibits. (PR at 3-6.) Such conduct is equivalent to an unauthorized (indeed, forbidden) supplement to their *Dura* argument, and should be stricken in accordance with the Court's previous decision. (Tr. 16:1-18:3, Dec. 15, 2005); Fed. R. Civ. P. 12(f).

II. Defendants' Settlement Submission Is Properly Before the Court

A non-settling defendant who perceives itself prejudiced by a proposed settlement has the right to object to the settlement on that basis. *See Agretti* v. *ANR Freight System, Inc.*, 982 F.2d 242, 247 (7th Cir. 1992) (*citing Quad/Graphics, Inc.* v. *Fass*, 724 F.2d 1230, 1232 (7th Cir. 1983) ("[I]n multi-party lawsuits, non-settling defendants often seek the court's intervention to invalidate or alter partial settlements.")). As Household Defendants would have standing to *object* to the settlement, Defendants' Settlement Submission, which *does not object* to the settlement with Andersen, is likewise permitted.[5] In fact, Plaintiffs fail to cite even one case limiting a non-settling defendant's rights to *acquiesce* to settlement.

---

[5] The purpose of the standing requirement is to limit those who may request relief from the court. *Barron's Law Dictionary* (standing is "the legal right of a person to challenge in a judicial forum the conduct of another...."). In situations where the party is not requesting relief on its behalf,

Footnote continued on next page.

III. Plaintiffs' Proposed Settlement Is Consistent with the Value of Their Weak Claims Generally and Commensurate with any Potential Settlement with the Household Defendants

Plaintiffs' request to strike the Household Defendants' Settlement Submission is curious considering that the Household Defendants are not objecting to the settlement. Defendants' submission simply observes facts about the settlement. It is not these facts that Plaintiffs deny. Specifically, Plaintiffs do not contest that (1) no discovery into Andersen's financial condition was taken prior to the proposed settlement; (2) Andersen's pecuniary hardship was not among the reasons for settlement disclosed to the class; (3) the class was told that the settlement was based on the merits of Plaintiffs' claims, *vel non*; (4) Plaintiffs presented no factual support for Andersen's putative financial limitations when appearing before the Court; and (5) the Court was told that the settlement was a reflection of the merits of Plaintiffs' claims. Plaintiffs do not disagree with any of the above facts. Plaintiffs just do not like the implications which necessarily follow from these facts—*viz*, that Plaintiffs' remaining claims against the Household Defendants are equally devoid of vitality.

Plaintiffs' proposed settlement should be approved because it fairly represents the expected value of their claims. *See Mars Steel Corp.* v. *Continental Illinois National Bank & Trust Co.,* 834 F.2d 677, 682 (7th Cir. 1987). As Plaintiffs have represented to the absent class members as well as the Court, the $1.5 Million settlement represents Plaintiffs' concerns about the general risks of protracted litigation, including the expense, length and ultimate danger of

Footnote continued from previous page.

> standing is not necessarily required. *See e.g. Ryan* v. *CFTC*, 125 F.3d 1062, 1063 (7th Cir. 1997) (standing is not required to submit an amicus brief). Specifically, in the context of challenging a partial settlement, the standing requirement exists to "implement[] the policy consideration of encouraging the voluntary resolution of lawsuits...." *Quad/Graphics* ,724 F.2d at 1233. Here, the Household Defendants are not objecting to the settlement and are not requesting any relief from the Court. Rather, consistent with the underlying policy, they are "encouraging the voluntary resolution of [the] lawsuit[]." *Id.* Therefore, the Court may consider Defendants' Settlement Submission. *See Ryan* 125 F.3d at 1063 (holding that the court may accept an amicus brief when it will help the court beyond what the parties are able to provide).

little or no recovery, and the problems of proof under and defenses to the securities law violations asserted in the complaint (Stipulation[6] at 3-4)—specifically the "major issues proving up scienter...." (Tr. 7:24-8:2, Dec, 15, 2005.)

However, Plaintiffs' assertion that the proposed settlement was negotiated for any reason other than the factual and legal defects of their claim is inaccurate and insupportable. Plaintiffs attempt in their Response to support, for the first time, their oral claim that Andersen's financial limitations were the reason for settlement. Plaintiffs' assertion has not improved with time—the deficiencies are the same. Specifically, Plaintiffs' claim that the $1.5 Million reflects the largest amount that Andersen has available to pay (i) is not reflected in the notice Plaintiffs sent to absent class members (*see* Stipulation) and (ii) was devoid of any factual support when orally presented to the Court. (Tr. 7:1-8:16, Dec. 15, 2005.) Even in their Response, Plaintiffs are unable to reference any discovery into Andersen's financial condition that was done prior to negotiating the settlement. Instead, Plaintiffs desperately cite to a court decision from 2004 that notes Andersen's financial difficulties. (PR at 7.) Despite these musings, Andersen—in the following year—agreed to settlements totaling in excess of $100 Million.[7] However, regardless of any assertions that Plaintiffs may make now, it is clear that the reasons that the settlement with Andersen was reached *at the time* had absolutely nothing to do with Andersen's pecuniary hardships. The basis for the settlement is exactly as has been described to the absent class members and to the Court—"the inherent problems of proof under and possible defenses to the securities law violations asserted in the complaint." (Stipulation at 4; *See* Tr: 7:24-8:2, Dec. 15, 2005.)

---

6 "Stipulation" refers to Plaintiffs' Stipulation of Settlement with Arthur Andersen LLP.

7 In 2005 Andersen settled with Charter Communications, Inc. for $2.25 Million, Dynegy, Inc. for $1.05 Million, Global Crossing, Ltd. for $25 Million, I2 Technologies, Inc. for $2.9 Million, Qwest Communications International, Inc. for $10 Million and WorldCom, Inc. for $65 Million. *See* Stanford Law School Securities Class Action Clearinghouse, http://securities.stanford.edu/.

The legal and factual defects that have lead to the current settlement with Andersen will also prevent any substantial recovery from Household. Plaintiffs admit that the legal basis for the claims against Andersen and Household are similar. (PR at 7.) Securities fraud claims against a company's auditors generally follow legal theories identical to the claims against the company while the key questions of fact overlap substantially. As is evident from Plaintiffs' Complaint, this case is no different. (*See* AC ¶¶ 3, 6, 46, 176, *citing* AC ¶¶ 102-06 and AC ¶¶ 125-55.) Both sets of claims will rise and (more likely) fall on the same analysis.

Plaintiffs' only attempt to distinguish the claims against Andersen from those against the Household Defendants is that proving scienter is more difficult against an auditor than against an issuer. (PR at 7.) This is not true. Whether the defendant is a primary defendant company or the secondary defendant auditor, the standard for proving scienter is the same—high. *See Robin* v. *Arthur Young & Co.,* 915 F.2d 1120, 1126 (7th Cir. 1990), *cert. denied,* 499 U.S. 923 (1991). Plaintiffs assert that as against an auditor they must demonstrate "an egregious refusal to see the obvious, or to investigate the doubtful, or that accounting judgments made were such that no reasonable accountant would have made the same decision." (PR at 7.) However, this is the same standard that is applied to all Rule 10b-5 defendants. The Seventh Circuit in *Sundstrand* defined recklessness under the scienter standard as "a proper legally functional equivalent for intent." *Sundstrand Corp.* v. *Sun Chemical Corp.,* 553 F.2d 1033, 1045 (7th Cir. 1977). It is an "extreme departure from the standards of ordinary care, such that its danger is either known to the defendant or so obvious that the defendant must have been aware of it." *Davis* v. *SPSS, Inc.,* 385 F. Supp. 2d 697, 712 (N.D. Ill. 2005) (*citing Sundstrand* 553 F.2d at 1045).

In fact, the very standard for auditor scienter that Plaintiffs champion as the sole distinction between the claims against Andersen and those against the Household Defendants—"an egregious refusal to see the obvious, or to investigate the doubtful"—is likewise applied to companies (not just auditors) in the Northern District of Illinois. *E.g., In re Motorola Secs. Litig.,*

No. 03 C 287, 2004 U.S. Dist. LEXIS 18250 at *98 (N.D. Ill. Sept. 9, 2004) (stating that "an egregious refusal to see the obvious, or to investigate the doubtful" may constitute scienter by the defendant Motorola). Indeed, the phrase was originally coined to generally express scienter for primary liability, not secondary liability. *See Goldman* v. *McMahan, Brafman, Morgan & Co.*, 706 F. Supp. 256, 259 (S.D.N.Y. 1989) (discussing *principal* liability under Rule 10b-5). This equal application to companies and auditors, whether primary or secondary actors, is consistent with the Seventh Circuit's determination that primary and secondary actors must each commit the proscribed act with the same intent. *Robin,* 915 F.2d at 1126. Thus, not only is proving scienter similar for Andersen and Household, it is *exactly the same. Id; see Goldman,* 706 F. Supp. at 259; *In re Motorola*, 2004 U.S. Dist. LEXIS 18250 at *98

Accordingly, it is clear that the claims against Andersen and Household are on a parallel footing. The settlement with Andersen reflects the substantial failings—facially and factually—of Plaintiffs' claims against both Andersen and the Household Defendants. Thus, every "risk" or "concern" that brought about the proposed settlement with Andersen—that Household securities were not artificially inflated during the relevant period and that Defendants did not make false or misleading statements, and certainly not with scietner— also exists with regard to Household and will preclude any substantial recovery. (*See, e.g.,* Pls.' Notice of Pendency and Proposed Partial Settlement of Class Action, Ex. A-1, at 1-2 (noting concerns regarding the following issues in the case: "(1) the method for determining whether Household securities were artificially inflated during the relevant period; (2) the amount of any such inflation; (3) the extent that various facts alleged by Lead Plaintiffs were materially false or misleading; and (4) the extent that various facts alleged by Lead Plaintiffs influenced the trading prices of Household securities during the relevant period.")) Some of these defects have already been elaborated in the *Dura* Motion currently pending before the Court, while others will be detailed in summary judgment motions to the extent that such motions may prove necessary.

Unable to distinguish between their claims against Andersen and those against the Household Defendants, or between companies and their auditors generally, Plaintiffs desperately attempt to discredit Defendants' analysis of the factual relationship between the settlement values attributed to companies and their co-defendant auditors. Defendants' analysis of over forty settlements entered into by the "Big Five" accounting firms over the past five years reveals that when claims are brought simultaneously against a company and its auditor, the auditor on average contributes 23.1% of the settlement, with a median value of 20.8%. (*See* DSS, Appendix A.) Plaintiffs do not contest the truth of these facts or the results of the calculations. Instead, Plaintiffs pick and choose a few "outliers" and claim they represent the whole. (PR at 8.) This is poor analysis. Defendants could just as easily refer the Court to a case in which Andersen paid 78% of a $141 Million settlement with Sunbeam Corp. (*See* DSS, Appendix A.) However, correlations are revealed from analyzing the aggregate, not the exceptions.

Applying this aggregate analysis to the $1.5 Million Andersen settlement, Plaintiffs' claims against the Household Defendants are worth approximately $5 Million. This estimated value of $5 Million is commensurate with the Household Defendants' view of the reasonable settlement value of Plaintiffs' claims against them. Therefore, Plaintiffs' proposed settlement with Andersen is (1) a fair estimate of the expected value of the merits of Plaintiffs' claims against Andersen; and (2) consistent with the Household Defendants' estimation of the reasonable settlement value of Plaintiffs' claims against Household. For these reasons Plaintiffs' settlement with Andersen should be approved. Therefore, the Household Defendants do not object to a finding that the proposed settlement is "fair, reasonable, and adequate." Fed. R. Civ. P. 23(e)(1)(C).

CONCLUSION

For the foregoing reasons Defendants (1) request that Plaintiffs' Response, which is in direct violation of the Court's December 15, 2005 ruling, be stricken; and (2) do not object pursuant to the PSLRA to Plaintiffs' proposed settlement with Andersen.

Dated: April 3, 2006
Chicago, Illinois

Respectfully submitted,

EIMER STAHL KLEVORN & SOLBERG LLP

By: s/ Adam B. Deutsch
Nathan P. Eimer
Adam B. Deutsch
224 South Michigan Avenue
Suite 1100
Chicago, Illinois 60604

-and-

CAHILL GORDON & REINDEL LLP
Thomas J. Kavaler
Howard G. Sloane
Landis C. Best
David R. Owen
80 Pine Street
New York, NY 10005
(212) 701-3000

Attorneys for Defendants Household International, Inc., Household Finance Corporation, William F. Aldinger, David A. Schoenholz, Gary Gilmer and J. A. Vozar

CERTIFICATE OF SERVICE

Adam B. Deutsch, an attorney, certifies that on April 3, 2006, he caused to be served copies of the Reply Memorandum of the Non-Settling Household Defendants Pursuant to the PSLRA with Respect to Plaintiffs' Proposed Settlement with Defendant Arthur Andersen LLP, to the parties listed below via the manner stated.

s/ Adam B. Deutsch
Adam B. Deutsch

Via E-mail and Federal Express

Patrick J. Caughlin
Azra Z. Mehdi
Cameron Baker
Luke O. Brooks
LERACH COUGHLIN STOIA & ROBBINS LLP
100 Pine Street, Suite 2600
San Francisco, California 94111
(415) 288-4545
(415) 288-4534 (fax)

Via E-mail and Federal Express

Marvin A. Miller
Lori A. Fanning
MILLER FAUCHER and CAFFERTY LLP
30 North LaSalle Street, Suite 3200
Chicago, Illinois 60602
(312) 782-4880
(312) 782-4485 (fax)

Via E-mail and Federal Express

Stanley J. Parzen
Susan Charles
MAYER BROWN ROWE & MAW LLP
71 S. Wacker Drive
Chicago, Illinois 60606
(312) 782-0600
(312) 701-7711 (Fax)