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-C-5893 (Consolidated) CLASS ACTION Judge Ronald A. Guzman Magistrate Judge Nan R. Nolan

DEFENDANTS' STATUS REPORT FOR THE JANUARY 24, 2007
STATUS CONFERENCE BEFORE MAGISTRATE JUDGE NOLAN

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The Household Defendants respectfully submit this Status Report to summarize the current status of the action and to raise several matters that Defendants believe should be discussed at the January 24, 2007 status conference and to provide the Court with the context in which these matters arise. Defendants believe that the Court's consideration, and, where appropriate, resolution of these matters, will greatly assist the parties in concluding fact discovery (but for the previously-authorized exceptions for specific depositions) by the January 31, 2007 cut-off.

1. Recent Rulings by Judge Guzman

On January 22, the parties received electronic notification of two rulings by Judge Guzman on objections filed by Plaintiffs to two of this Court's Orders.

a. In a January 17 ruling, Judge Guzman affirmed this Court's July 6, 2006 Order as to the Arthur Andersen audit letters. The Court granted Andersen's motion for the return of certain privileged documents (Household audit letters) that were inadvertently produced to Plaintiffs during discovery, and denied Plaintiffs' cross-motion to compel production of certain additional audit letters and allegedly related documents, *e.g.*, a litigation database and litigation reserves information. Judge Guzman ruled that this Court "applied the correct law to the instant facts. The long and short of it is that they [the audit letters] were prepared because of pending or threatened litigation, and they evaluate Household's response to liability on a case-by-case basis." Judge Guzman also noted that "[t]his litigation involves millions and millions of documents, the production of the particular documents at issue was inadvertent, the delay in rectifying the error was reasonable and Household and KPMG are making a concerted effort to recall and secure the return of the audit report and related documents."

b. In a January 19 ruling, Judge Guzman affirmed this Court's September 20, 2006 Order (actually issued on September 19) regarding the counting of Defendants' interrogatories and "adopt[ed] the order in full." Judge Guzman noted that Magistrate Judge Nolan "has supervised all discovery matters in this case for over two years and she shall be afforded great deference when it comes to regulating the time, scope and format of permissible discovery" and "it has been necessary for her to become intimately familiar with the minute details of the discovery in this case." Judge Guzman concluded that this Court "did not err in holding that Household has not yet exceeded its eighty-five interrogatory limit."

2. Plaintiffs' Bad-Faith Responses to Defendants' Court-Authorized Supplemental Interrogatories

In its January 10, 2007 ruling on Defendants' Motion for Sanctions and to Compel Responses to Supplemental Interrogatories authorized by the Court's August 10, 2006 Order, the Court addressed the need for what the Court described during the conference as a "bill of particulars" that identified each allegedly illegal product or policy and the illegal revenues obtained thereby so that Defendants would be informed of the specifics of the alleged "illegal predatory lending scheme."

In its January 10 Order, the Court found Plaintiffs' responses inadequate a second time and again instructed Plaintiffs to provide new answers to the five interrogatories proposed by Defendants and edited by the Court (and read into the record during the January 10 status conference). The revised answers were due by January 19, and the Order itself expressly cautioned Plaintiffs that the answers to these interrogatories (and to another set of interrogatories discussed in the Order) must be "specific and complete."

Plaintiffs served their latest "answers" to these interrogatories (Defendants' Court-authorized supplemental interrogatories as rewritten by the Court) six hours after defense counsels' close of business on January 19. Unfortunately, as briefly described below, Plaintiffs' responses are neither "specific" nor "complete" and include, *inter alia*, the following defects:

1. The latest answers continue to identify only facially legal products sold by any lender (e.g., "real estate secured loans" and an increasingly lengthy list of legal variants thereof) with no identification of the particular illegal products or policies upon which their alleged "illegal predatory lending scheme" is premised, in contravention of the Court's instructions that Plaintiffs provide a "bill of particulars" that specifically identifies the illegality alleged.

2. The latest answers still provide no quantification of the "illegal revenues" allegedly obtained by Defendants during the class period, in contravention of the Court's order requiring identification of "the revenues illegally derived," and continue to rely only on settlement materials (that concede no illegality whatsoever) as the sole explanation of their claim that illegal revenues were actually obtained.

3. The latest answers still consist principally of objections, including repeated reservations of rights to supplement with further information at a later time, in contravention of: (a) the Court's instruction that the answers must be complete, and (b) the instruction that Plaintiffs' proof at trial is limited to those matters identified in these responses.

Because these issues go to the heart of Plaintiffs' claims of securities fraud, it remains vital and indispensable that Plaintiffs be required to provide a clear and specific statement on these subjects that meets the standard now twice ordered by this Court. A further order is evidently necessary. Defendants are prepared to submit additional briefing with respect to Plaintiffs latest answers (their fourth attempt) if the Court would find it helpful, although given the Court's firm instructions at the last status conference, and Plaintiffs' defiance of those instructions, Defendants renew their request for sanctions and for a recommendation of dismissal with appropriate reference to Plaintiffs' most recent round of obstruction.

Defendants also note that Plaintiffs' answers to Defendants' Fifth Set of Interrogatories are to be served by January 24, but Defendants assume that they will not have

received them by the time of the Status Conference before the Court, which is scheduled for 3:00 p.m., CT, that day. The Court noted in its January 10 Order, that "[i]n light of the Court's rulings regarding Defendants' Fourth and Supplemental interrogatory requests, the parties are expected to meet and confer about Defendants' Fifth Set of Interrogatories . . . ." Plaintiffs have not sought to have any meet and confer about our Fifth Set, either because they had no such questions or issues or because they intended to rely on their objection (now overruled) to the Court's ruling regarding the counting of interrogatories. Various other interrogatory responses are also shortly due as a result of the rejection of Plaintiffs' counting objection.[1] Defendants sincerely hope that Plaintiffs' forthcoming responses to all interrogatories will in fact be specific and complete as ordered by the Court in its January 10 Order.

3. Defendants' Compliance with the Court's January 10 Order

Since the last status conference on January 10, 2007, Defendants have complied with the following deadlines that were established and discussed during that conference and in the Court's January 10, 2007 Order issued immediately thereafter.

a. On January 12, Defendants provided the Court with a list of the KPMG audit letter documents that are (i) identical to or (ii) similar to the Arthur Andersen audit letter documents that the Court held were protected as attorney work product in its July 6, 2006 ruling. That ruling has been affirmed by Judge Guzman. Pursuant to this ruling, this Court should order Plaintiffs to return the inadvertently produced KPMG audit letter documents, all of which have

[1] In view of Judge Guzman's January 19 ruling denying Plaintiffs' objection to this Court's September 2006 Order as to the counting of Defendants' interrogatories, and pursuant to prior orders of the Court, Plaintiffs' answers to Defendants' Third Set of Interrogatories (held by the Court to be contention interrogatories) and Defendants' Fourth Set of Interrogatories both are due by Monday, January 29, 2007. (The former was due seven days after receipt of Judge Guzman's Order affirming this Court and the latter was due five days after this Order.)

been recalled by KPMG (but not yet returned by Plaintiffs).

b. On January 12, Defendants produced an installment of their rolling privilege log that contained descriptions of all of the previously unlogged documents that Defendants had withheld or redacted on the basis of privilege, including the privileged documents shown on the Household/HSBC merger disclosure schedules.

c. On January 16, Defendants submitted a brief response to the "waiver by delay in logging" argument asserted in Plaintiffs' "Motion to Compel Household Defendants to Produce Missing Documents, Documents Improperly Withheld or Redacted and For a Finding of Waiver Due to Defendants' Failure to Assert Privilege Over Withheld or Redacted Documents that Are Not on Their Privilege Log." Plaintiffs indicated at the January 10, 2007 status conference that they will not be filing a reply brief on this motion.

d. On January 17, Defendants submitted an opposition to Plaintiffs' "Motion to Compel Andrew Kahr Documents Improperly Withheld as Privileged or Destroyed by the Household Defendants," and also provided the Court, for its *in camera* review, with a full set of the Kahr-related documents withheld or redacted on the basis of attorney-client privilege.

e. On January 19, Defendants informed Plaintiffs that a partial production of documents responsive to the Court's January 10 Order (ruling on Plaintiffs' motion to compel with respect to their Fourth Document Demand) was available to Plaintiffs in Chicago. Defendants expect to complete this production by January 23, as directed by the Court during the January 17 telephone conference.

f. On January 19, Defendants produced documents we indicated we would

produce after reviewing documents that Plaintiffs claimed should have been on our privilege log.

In addition, on January 19 Defendants offered Plaintiffs deposition dates for the following former Household employees: Robin Allcock on February 14-15 in Charlotte, North Carolina and Craig Streem on February 21 or 22 in New York City. David Schoenholz had previously been offered for a deposition on February 14-15 in Tomahawk, Wisconsin. He is not available on those dates in Chicago or another major city, but would be available in Chicago on February 28 - March 1, and these dates also have been offered to Plaintiffs. We have not yet received any response from Plaintiffs. (For the Court's convenience, attached as Exhibit A is an updated version of the list of Plaintiffs' Depositions.)

4. Plaintiffs' Continued Violation of Court Orders Requiring Them to Include Defendants in the Scheduling of All Non-Party Depositions

In its January 10, 2007 Order, the Court reiterated in no uncertain terms its November 30, 2006 Order requiring Plaintiffs to include Defendants' deposition coordinator when any third party deposition is being scheduled to ensure that the dates selected are mutually agreeable. The Court's comments at the November 30 and January 10 conferences made it plain that the Court's instruction covered all forms of communications between Plaintiffs and the third parties, including letters, faxes, emails and telephone conversations. Despite the explicit, unambiguous and reiterated direction of the Court, Plaintiffs have inexcusably continued to exclude Defendants from scheduling communications with third parties or their representatives, and have deliberately kept Defendants in the dark about a scheduling order in England, and specific dates requested by or offered to Plaintiffs for certain depositions.

Defendants have just learned from counsel for Morgan Stanley & Co. International Limited ("Morgan Stanley UK") that a Master in the High Court of Justice,

Queen's Bench Division, ordered that the deposition of Morgan Stanley UK's Managing Director, Jeremy Capstick, should proceed on January 8, 2007 pursuant to the Letters of Request issued by this Court. Plaintiffs never told Defendants about this Order, and ignored Defendants' repeated request that the deposition of Mr. Capstick be coordinated with that of HSBC Holdings plc in London on January 8. On January 16, 2007 — six days after this Court admonished Plaintiffs again to include Defendants in their scheduling communications — Plaintiffs' deposition coordinator, Jason Davis, Esq., sent an email about scheduling (with no copy to Defendants) to Riche McKnight, whom Defendants understand to be an in-house attorney in the United States for Morgan Stanley & Co., Inc. ("Morgan Stanley US"). Without previously conferring with Defendants or even telling them after the fact, Mr. Davis proposed that Mr. Capstick's deposition proceed on January 19. Defendants did not learn of this email and proposal until January 18, when they were copied on an email from Morgan Stanley's UK counsel to Mr. Davis. In fact, the day before, during the January 17 telephone conference with the Court, Mr. Davis made no mention of his unilateral scheduling suggestion to Morgan Stanley, but rather unequivocally (and incorrectly) represented to the Court and Defendants that the Capstick deposition would proceed in London on January 26.

Two days later, Defendants learned that Plaintiffs had not been candid with them or with this Court (or, for that matter, with Morgan Stanley UK or with the UK court). On January 19, both deposition coordinators received an email from Peter Watson, a solicitor with the firm of Allen & Overy in London, counsel for Morgan Stanley UK and Mr. Capstick, confirming that Mr. Davis had misrepresented the January 26 date to this Court, made misrepresentations to the UK court, and failed to respond to his repeated written communications

regarding offered deposition dates. (A copy of this email is attached to this Status Report as Ex. B with Mr. Watson's permission.)

Mr. Watson wrote: "We were unaware that the US court had been informed that the deposition was going ahead on 26th. The witness had not even been informed of this. This is a clear misrepresentation of the position to the Court. The latest proposal from us suggested the 24th January." Mr. Watson noted that Plaintiffs had not responded to his communications of January 11, 16 or 18 regarding proposed dates for Mr. Capstick's deposition. (Defendants had promptly informed all relevant parties that they were available on any of the proposed dates.) Nor had Plaintiffs, according to Mr. Watson, provided him with a requested list of questions or particular issues to be raised with Mr. Capstick at his deposition, and any documents to be shown to Mr. Capstick, and Plaintiffs had not even properly served the witness with the order of the UK court. Mr. Watson concluded: "Any attempts to schedule the deposition without recourse to him are not only futile but contrary to representations made to the English court."

Late in the afternoon of Friday, January 19, after Defendants had re-confirmed their willingness to attend the deposition of Morgan Stanley UK on January 24, Mr. Capstick's only remaining available date before the discovery cut-off, Plaintiffs informed Defendants that Plaintiffs would not proceed with Mr. Capstick's deposition on either January 24 or 26, the date they had represented to the Court.

This sequence of events, and Mr. Watson's email, demonstrates that Plaintiffs, at best, have been woefully negligent in their efforts to schedule the Morgan Stanley UK deposition prior to January 31. Their lack of diligent efforts to take this deposition within the Court's deadline (including their failure to respond to three communications from the witness's counsel

on this subject and their disregard of Defendants' repeated requests for coordination with the earlier trip to London), their continued blatant defiance of this Court's Order to include Defendants in scheduling communications, and their misrepresentation to this Court and Defendants that a date certain before the fact discovery cut-off had been set for this deposition all compel the conclusion that Plaintiffs have forfeited the right to proceed with the deposition of Morgan Stanley UK or any substitute for this deposition slot. Unlike the exception granted at Plaintiffs' request for the depositions of Ms. Allcock and Mr. Schoenholz in order to accommodate a medical condition of one of Plaintiffs' counsel or Mr. Vozar to accommodate a medical emergency of one of defense counsels' family members, the deposition of Mr. Capstick did not proceed on time solely because Plaintiffs failed to schedule it on time, despite the willingness of the witness and Defendants to proceed before the cut-off date. That Plaintiffs actively sought to conceal that failure from the Court is reason enough to deny them any relief from their default in taking the deposition of Morgan Stanley UK before the expiration of the fact discovery period.

Nor should Plaintiffs be rewarded for their lack of candor by being allowed to replace this forfeited deposition with that of another witness. In particular, Plaintiffs' newly-announced intention to pursue by January 31[2] the Rule 30(b)(6) deposition of Morgan Stanley US (which they had noticed back in March 2006) should be treated as adding a new deposition to their slate, as opposed to merely replacing the forfeited deposition of Morgan Stanley UK. This result is dictated in any event by the Court's protocol for counting depositions. The deposition of Morgan Stanley US would proceed pursuant to a Rule 45 subpoena, while Plaintiffs' fumbled

[2] Defendants have received no further information from Plaintiffs regarding the scheduling of this deposition and, as this deposition was not dependent on any rulings of the Court, Defendants reserve all rights with regard to Plaintiffs' ability, vel non, to schedule this deposition prior to January 31.

plan to depose a different entity, Morgan Stanley UK through Mr. Capstick, was to proceed pursuant to Letters of Request issued pursuant to the Hague Convention.

5. Expert Discovery Schedule

The Court's January 10 Order scheduled the next status hearing for January 24 and noted that "[t]he parties should be prepared to discuss their expected need for experts and an expert discovery schedule at that time." Defendants respectfully submit that they cannot participate fully in a discussion of expert witness needs without first knowing how many experts Plaintiffs plan to call in this action and the subject matter of each such expert's planned report. Without this information, Defendants cannot predict with certainty the number or types of experts they may elect to retain, how much time will be needed for the preparation of rebuttal expert reports, and the amount of time that will be required for one or more expert depositions.

Defendants respectfully suggest that the Court direct Plaintiffs to inform the Court and Defendants as soon as reasonably possible of the number of expert reports they intend to file and the expected subject matter of each such report, together with the date(s) on which they propose to submit such report(s). Within three days of receiving such information, Defendants should be able to propose a schedule for taking related depositions and submitting rebuttal report(s). Defendants believe that this procedure will allow the Court to establish a realistic expert schedule rather than a generic schedule that may not adequately accommodate the parties' needs.

6. Plaintiffs' Failure to Safeguard Confidential Information

Plaintiffs' insatiable appetite for more and more documents from Defendants apparently is not matched by an ability to safeguard the confidential information Defendants

have already produced. In the course of a January 17, 2007 letter complaining about various aspects of Defendants' privilege log, Plaintiffs acknowledged that despite a "diligent search" they "cannot locate" 438 documents that Defendants previously had produced. In response, Defendants confirmed that these documents had in fact been produced (by providing several examples of specific cover letters pursuant to which certain of the mislaid documents had been transmitted to Plaintiffs' counsel). Defendants are dismayed by Plaintiffs' apparent failure to maintain suitable protections and controls over Household's confidential business documents, and we have notified Plaintiffs that this serious breach of confidentiality must be explored in greater detail, with the assistance of the Court if necessary. In the meantime, we have asked Plaintiffs to make a more rigorous search for the missing material before responding to their request for replacement copies.

Dated: January 22, 2007 Respectfully submitted,
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