UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF ILLINOIS

EASTERN DIVISION

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

THE CLASS' MOTION FILED BY LEAVE OF COURT PURSUANT TO THE FEBRUARY 12, 2007 ORDER TO COMPEL PRODUCTION OF E-MAILS AND DEPOSITION TESTIMONY BY MORGAN STANLEY PURSUANT TO THE CLASS' MARCH 7, 2006 SUBPOENA

(REDACTED VERSION)

I. INTRODUCTION

The Class respectfully moves the Court to compel Morgan Stanley ("Morgan Stanley" or the "Company") to produce e-mails pursuant to the Class' March 7, 2006 third party subpoena. The Class endeavored for almost a year to cooperate with Morgan Stanley to impose the minimum quantum of burden possible under the circumstances. To that end, the Class agreed with Morgan Stanley's in-house counsel, Riche McKnight, to interview witnesses on an informal basis and to a limited agreed-upon e-mail production following those interviews. Mr. McKnight reneged on that agreement on January 19, 2007 and the Company's newly-hired outside counsel, Todd Fishman of Allen & Overy, made it clear only on the last day of fact discovery of January 31, 2007 that Morgan Stanley would produce no e-mails at all, despite their prior agreement to do so. The Class' request for e-mails is eminently reasonable. The Class asked the Company to search the e-mail boxes of one New York investment banking employee and two New York research analysts. These e-mail boxes belong to the two deposition witnesses offered by Morgan Stanley and one research analyst assistant. The Class requests the Court order Morgan Stanley to produce responsive e-mails from the three e-mail boxes at issue by February 28, 2007.

Separately, Morgan Stanley had offered to produce two witnesses for its deposition: Jonathan Pruzan, an investment banker who worked on the merger with HSBC Holdings, plc ("HSBC"); and Kenneth Posner, a research analyst who covered Household during the Class Period. The Class finds the witnesses acceptable. The Class is willing to conduct the deposition at the location and on a date that is convenient for the witnesses, and has agreed to depose each individual for no more than one-half day. The Class must take this deposition as soon as possible. The Class therefore requests the Court order the deposition to occur before March 16, 2007.

II. RELEVANT BACKGROUND

On March 7, 2006, the Class served a third-party subpoena on Morgan Stanley. *See* Ex. 1.[1] The Class thereafter communicated with Mr. McKnight, who made it clear during that period that he understood the subpoena covered both research analyst topics and the merger with HSBC. *See* Davis Decl., ¶2. The Class granted Morgan Stanley several months to comply with the subpoena and on July 25, 2006, as requested, the Class further explained the reasons why the requested discovery was relevant to the Class' claims. *See* Ex. 2.

Over the course of the next few months, Class counsel continued to cooperate with Mr. McKnight and he made a number of productions from Morgan Stanley's New York offices. On October 23, 2006, Class counsel expressed concern that the rolling document production had thus far included few e-mails. *See* Ex. 3. Thereafter, Mr. McKnight communicated his understanding that the Class would seek e-mails only if the hard copy document production indicated the e-mail search was sensible. *See* Ex. 4. The Class clarified it did indeed seek e-mail production, and conferred with Mr. McKnight on how to conduct the search most efficiently. *See* Ex. 5.

On December 29, 2006, Mr. McKnight agreed to work with the Class to produce e-mails, provided search terms were sufficiently tailored to the Morgan Stanley technology system. *See* Davis Decl., ¶3. He informed Mr. Davis and Mr. Baker that after the search terms were agreed upon the entire process of searching ***and*** producing responsive e-mails would take no longer than a week. *Id.*

On January 2, 2007, the Class provided search terms to Morgan Stanley's counsel, and the parties had another conversation on the topic. *See* Ex. 5. At this point in time, the Class was willing

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[1] All exhibits are attached to the Declaration of Jason C. Davis in Support of The Class' Motion Filed by Leave of Court Pursuant to the February 12, 2007 Order To Compel Production of E-Mails and Deposition Testimony by Morgan Stanley Pursuant to the Class' March 7, 2006 ("Davis Decl."), filed herewith.

(i) to conduct informal interviews of Mr. Pruzan and Mr. Posner in order to determine the extent of their knowledge about relevant matters, and (ii) to further tailor e-mail search terms following the interviews. *See* Davis Decl., ¶3. After months of cooperation, Mr. McKnight agreed to produce the witnesses for an informal interview on January 19, 2007. *See* Ex. 5.

On Friday, January 19, 2007, at the same time that the interviews were about to commence, Mr. McKnight informed Class counsel that defense counsel from Cahill Gordon & Reindel LLP was present and would attend the interviews, changing the entire process from informal to adversarial. The Class told Mr. McKnight that the informal interviews were no longer acceptable and requested deposition dates for the two witnesses. *See* Davis Decl., ¶4.

On Thursday, January 25, 2007, Todd Fishman of Allen & Overy informed the Class that he had been retained by Morgan Stanley to respond to the Class' subpoena. *See* Ex 6. On Friday, January 26, 2007, the Class had an extensive conference call with Mr. Fishman and defense counsel. Later that day, Mr. Fishman sent an e-mail to defendants and the Class, proposing several dates for the deposition of Mr. Posner and Mr. Pruzan but was silent on the production of e-mails. *See* Ex. 7. The Class followed up with Mr. Fishman about the e-mail production issue on the same day and Mr. Fishman communicated he was looking into the matter. *See* Ex. 8.

Over the course of the next few days, the Class continued to negotiate depositions and e-mail production with Morgan Stanley's counsel and defendants. *See* Ex. 7. Then, on January 31, 2006, Mr. Fishman stated Morgan Stanley refused to produce any e-mails on the bases of burden and relevance. *See id.* On February 1, 2007, the Class sought clarification and learned at that time that Morgan Stanley had completely reneged on its prior agreement to produce e-mails. *See id.*[2]

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[2] For the purpose of clarity, it should be noted that Morgan Stanley had not agreed to produce "all" or any range of e-mails but agreed to work with the Class to develop appropriate search terms for a reasonable e-

February 1, 2007 was the first time that Morgan Stanley had taken the position that it would produce ***no*** e-mails under any circumstances short of a court order. The Class was therefore forced to seek Court assistance to resolve this matter.

III. ARGUMENT

A. The Court Has Jurisdiction Over This Matter

On January 26, 2007, Morgan Stanley consented to this Court's jurisdiction should the parties required judicial assistance to resolve any issues. *See* Ex. 8.

B. The Morgan Stanley E-mails Are Highly Relevant and Necessary in Advance of the Morgan Stanley Deposition

Federal Rule of Civil Procedure 45(d) governs subpoenas served on third parties and permits discovery within the scope of Rule 26(b). *See, e.g., Centurion Indus., Inc. v. Warren Steurer & Assocs.*, 665 F.2d 323, 325 (10th Cir. 1981). This Court has repeatedly recognized that "parties may obtain discovery regarding any matter, not privileged . . . if the discovery appears reasonably calculated to lead to the discovery of admissible evidence."[3] Fed. R. Civ. P. 26(b)(1). The two categories of discovery at issue are directly relevant to the Class' claims.

The first category of discovery relates to Morgan Stanley's financial evaluation of Household's common stock and negotiations leading to the $14 billion merger between Household and HSBC, announced on November 14, 2002. As noted above, Morgan Stanley was HSBC's financial advisor for this transaction. According to Mr. McKnight, Jonathan Pruzan is a Morgan Stanley investment banker who worked on the transaction. Following weeks of due diligence by

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mail search. *See* Davis Decl., ¶3. In other words, Morgan Stanley had agreed to produce e-mails. Any disagreement was over the scope of the production.

[3] *See also Schlagenhauf v. Holder*, 379 U.S. 104, 114-15 (1964); *accord Rubin v. Islamic Republic of Iran*, 349 F. Supp. 2d 1108, 1111 (N.D. Ill. 2004) ("[u]nder Rule 26(b)(1) of the Federal Rules of Civil Procedure, the scope of discovery is generally very broad, incorporating any nonprivileged documents and/or tangible things that are relevant to the subject matter involved in the action").

HSBC, Morgan Stanley was privy to substantial business and non-public information about Household. On the basis of this information, Morgan Stanley provided its opinion to the HSBC Board of Directors, which the Board relied upon to determine the transaction was "fair" to HSBC shareholders from a financial point of view. *See, e.g.*, Ex. 9 at 3.

As illustrated in the merger contract, Morgan Stanley had access to information regarding predatory lending litigation; investigations by the SEC; other state regulatory investigations; and the fact that Household was going to change its accounting policies on how it reaged or restructured its delinquent accounts. *See, e.g.*, Ex. 13 at HSBC 022823 (delinquency accounting changes); HSBC 0022824 (SEC investigation and other regulatory investigations); HSBC 022826 (Elaine Markell matter); and HSBC 022827-28 (various lending practices settlement disclosures). All of these non-public disclosures are directly related to the Class' allegations,[4] and were revealed to HSBC and Morgan Stanley in connection with merger negotiations. The data's impact on the merger with HSBC is highly probative of materiality.

The second category of information relates to Morgan Stanley's analyst coverage of Household during the Class Period. The Class has alleged that information about the Attorneys General ("AG") Settlement was leaked to the market prior to its formal announcement on October 11, 2002. *See* Complaint, ¶6 ("As news of the massive predatory lending settlement leaked out during the first week of 10/02, the price of Household stock dropped to as low as $20.00 per share, 70% below its Class-Period high."). In addition, the Securities and Exchange Commission was very concerned about the AG Settlement leaks, and required Household to produce a chronology of the settlement discussions and related documents and interviewed Household witnesses in connection

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[4] *See, e.g.*, Complaint, ¶¶51-106 (predatory lending allegations); ¶¶107-133 (reaging or restructuring allegations); and ¶¶134-153 (restatement and credit card allegations).

with the matter. Defendants argued, however, that the Class' predatory lending claims cannot provide a basis for relief under the securities laws because Household's stock price increased on the day the formal AG Settlement was announced. *See, e.g.*, Dkt. No. 295 at 1 (Defendants "*Dura*" Reply Brief) at 5-6. Defendants' assertions are severely undermined by the fact that a great deal of information was not disclosed to the market on a single day but instead leaked through various sources.

Morgan Stanley was one such source. Nearly ten weeks before the AG Settlement was announced, Mr. Posner issued a public research note quantifying the potential settlement costs of litigation related to Household's predatory lending practices. *See* Ex. 12. The note states at page one that [redacted] *Id.* at 1. This [redacted] of the ultimate $525 million charge to earnings that Household took as a result of the ACORN litigation and AG Settlement. *Id.* at 5; *see also,* Complaint, ¶5. Over the course of the next few days, Household's common stock dropped from $42.67 on July 31, 2002 to $36.98 on August 5, 2002. *See* Ex. 10 at 2-3. In light of the importance of the predatory lending allegations to the Class' Complaint, the potential impact of Morgan Stanley's report on Household's stock price, and the novel theory of loss causation advanced by defendants, the information at issue is highly relevant.

The Class seeks e-mails sourced only to the two deposition witnesses – Messrs. Posner and Pruzan – and an assistant to Mr. Posner. This limited search will yield highly relevant materials.

C. Production of the Morgan Stanley E-mails Would Not Impose an Excessive Burden on Morgan Stanley

As the party resisting a subpoena, Morgan Stanley has the burden to establish that the Class' subpoena would impose an excessive burden. *See Sullivan v. Dickson*, 283 F.2d 725, 727 (9th Cir. 1960) ("[t]he burden of quashing is on the person to whom the subpoena is directed"); *accord Horizons Titanium Corp. v. Norton Co.*, 290 F.2d 421, 425 (1st Cir. 1961) ("there is a particularly

heavy burden upon a deponent to make a substantial showing in support of a motion to quash as contrasted to some more limited protection"). Morgan Stanley cannot meet its burden to quash the Class' subpoena because the Class seeks a very narrowly tailored e-mail production.

The Class has requested Morgan Stanley search the e-mail boxes of three of its New York employees: Jonathan Pruzan, Kenneth Posner and Athina Meehan.[5] *See* Ex. 5. The Class provided specific search terms for these individual boxes, and limited searches to specific time periods. *Id.* Again, in-house counsel for Morgan Stanley, Mr. McKnight, represented that it would take no more than one week to search ***and*** produce responsive e-mails provided proper search terms were provided. *See* Davis Decl., ¶3. It is clear that Morgan Stanley's efficient search capabilities are the result of extensive experience in electronic discovery. *See, e.g., Coleman (Parent) Holdings, Inc. v. Morgan Stanley & Co., Inc.*, No. CA 03-5045 AI, 2005 WL 679071 (Fla. Cir. Ct. March 1, 2005) (widely-publicized case resulting in a judgment of over a billion dollars in part because the presiding judge granted an adverse inference against Morgan Stanley for failure to properly maintain e-mails). Indeed, Mr. McKnight expressly indicated that searches such as the one requested by the Class are conducted as a matter of course. *See* Davis Decl., ¶3. As to financial resources, Morgan Stanley reported in its latest Form 10-K (filed with the Securities and Exchange Commission on February 13, 2007) net income of $7.472 billion for the fiscal year ended November 30, 2006. *See* Ex. 11. In light of the foregoing factors, Morgan Stanley would not be unduly burdened in responding to the Class' narrowly tailored e-mail production request and the Court should order Morgan Stanley to complete that production by February 28, 2007.

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[5] Riche McKnight, in-house counsel for Morgan Stanley, advised the Class that Ms. Meehan is no longer an employee of the Company.

IV. CONCLUSION

For the reasons set forth above, the Class respectfully requests the Court (i) order Morgan Stanley to produce the e-mails at issue by February 28, 2007, and (ii) order the deposition to occur before March 16, 2007.

DATED: February 14, 2007

Respectfully submitted,

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DECLARATION OF SERVICE BY EMAIL AND BY U.S. MAIL

I, the undersigned, declare:

1. That declarant is and was, at all times herein mentioned, a citizen of the United States and employed in the City and County of San Francisco, over the age of 18 years, and not a party to or interested party in the within action; that declarant's business address is 100 Pine Street, Suite 2600, San Francisco, California 94111.

2. That on February 14, 2007, declarant served by electronic mail and by U.S. Mail to the parties the: **THE CLASS' MOTION FILED BY LEAVE OF COURT PURSUANT TO THE FEBRUARY 12, 2007 ORDER TO COMPEL PRODUCTION OF E-MAILS AND DEPOSITION TESTIMONY BY MORGAN STANLEY PURSUANT TO THE CLASS' MARCH 7, 2006 SUBPOENA (REDACTED VERSION)**. The parties' email addresses are as follows:

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I declare under penalty of perjury that the foregoing is true and correct. Executed this 14th day of February, 2007, at San Francisco, California.

s/ Marcy Medeiros
MARCY MEDEIROS