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1 UNITED STATES DISTRICT COURT
1 SOUTHERN DISTRICT OF NEW YORK
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3 DEXIA SA/NV; DEXIA HOLDINGS,
3 INC.; FSA ASSET MANAGEMENT
4 LLC; and DEXIA CREDIT LOCAL
4 S.A.,

5
5 Plaintiffs,

6
6 v.

12 Civ. 4761 (JSR)

7
7 BEAR, STEARNS & CO.; INC.; THE
8 BEAR STEARNS COMPANIES, INC.;
8 BEAR STEARNS ASSET BACKED
9 SECURITIES I LLC; EMC MORTGAGE
9 LLC, formerly known as EMC
10 Mortgage Corporation;
10 STRUCTURED ASSET MORTGAGE
11 INVESTMENTS II, INC.; J.P.
11 MORGAN ACCEPTANCE CORPORATION
12 I; J.P. MORGAN MORTGAGE
12 ACQUISITION CORPORATION; J.P.
13 MORGAN SECURITIES LLC;
13 formerly known as JPMorgan
14 Securities, Inc.; WAMU Asset
14 Acceptance Corp.; WAMU Capital
15 Corp.; WAMU Mortgage
15 Securities; JPMorgan Chase &
16 Co.; and JPMorgan Chase Bank,
16 N.A.,

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17 Defendants.

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New York, N.Y.
February 22, 2013
5:00 p.m.

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21 Before:

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22 HON. JED S. RAKOFF,
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23 District Judge

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APPEARANCES

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BY: DANIEL SLIFKIN
WES EARNHARDT
HECTOR VALDES

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1 (Case called)

2 MR. DeLANGE: Good afternoon, your Honor, Timothy
3 DeLange with Bernstein Litowitz Berger & Grossmann on behalf of
4 the plaintiffs.

5 MR. VAN KWAWEGEN: Good afternoon, your Honor, Jeroen
6 Van Kwawegen with Bernstein Litowitz Berger & Grossmann on
7 behalf of the plaintiffs.

8 MR. BERGER: Good afternoon, your Honor, Max Berger,
9 Bernstein Litowitz on behalf of the plaintiffs.

10 MR. SLIFKIN: Good afternoon, your Honor, Daniel
11 Slifkin from Cravath Swaine & Moore for the defendants.

12 MR. EARNHARDT: Good afternoon, your Honor, Wes
13 Earnhardt from Cravath Swaine & Moore for the defendants.

14 MR. VALDES: Good afternoon, your Honor, Hector Valdes
15 from Cravath Swaine & Moore on behalf of defendants.

16 THE COURT: Good afternoon.

17 My law clerk, who was the same law clerk who worked on
18 the matter that you just heard, told me that she really likes
19 all the attorneys on this matter. Of course, past performance
20 is no guarantee of future results, but I was delighted to hear
21 that.

22 We are here on summary judgment. I should mention, I
23 got out one of the two memoranda that I owed you from prior
24 decisions last week. The second memorandum, which I really had
25 hoped to have before today, will be issued either on Monday or

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1 Tuesday. It's in the final editing process. But I looked at
2 it carefully to make sure there was nothing about it that would
3 impact the argument here today. And there is nothing, so we
4 can go forward.

5 Let me hear from moving counsel.

6 MR. SLIFKIN: Thank you, your Honor.

7 There were four topics I would like to address this
8 afternoon. And I would like to address them in the following
9 order, unless the Court has a different preference. The topics
10 are: Standing to sue, which of plaintiffs, if any, have
11 standing to bring these claims; the second topic is reliance,
12 whether there is evidence of actual and justifiable reliance,
13 which we submit there is not; the third topic is causation; and
14 the fourth topic is underwriter liability.

15 THE COURT: So based on the papers, I would think
16 you'd be prudent to spend most of your time on the first two
17 topics.

18 MR. SLIFKIN: On the first topic, your Honor?

19 THE COURT: On the first two topics. I don't want you
20 to conclude that I thought the other two arguments were
21 unpersuasive, but you might infer that.

22 Let's hear about the first two arguments.

23 MR. SLIFKIN: I may try to persuade you out of that a
24 little later. I'll try and do the first thing at greater
25 length.

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1 With respect to standing, your Honor, the certificates
2 that are at issue here, there is no dispute they were purchased
3 by an entity called FSAM, and I will return to FSAM later.

4 So the question presented then is, given the
5 certificates were bought by FSAM, how do the various Dexia
6 entities -- and I will call them all Dexia for short, Dexia SA,
7 Dexia Holdings, and Dexia Credit -- how do they have standing
8 to sue?

9 THE COURT: What about equitable subrogation?

10 MR. SLIFKIN: I can start there, if you like, your
11 Honor.

12 THE COURT: I'm just saying, you are right, they don't
13 have standing under the approach that you're focusing on. If I
14 understand this argument, it's that somehow the defendants are
15 off the hook because some of the other plaintiffs covered the
16 FSAM's losses, but that, it seems to me, tentatively -- nothing
17 I say here is not any ruling, just a thought -- would raise a
18 classic case of equitable subrogation, yes?

19 MR. SLIFKIN: Let me tell you why we don't think the
20 tests are met there, your Honor. There are really two
21 categories of equitable subrogation cases. The first, there is
22 a body of rules that have been developed quite specifically to
23 deal with the insurance contract, and then there are rules that
24 apply more generally.

25 With respect to the insurance contract, there is no

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1 question here that that does not apply. This is not an
2 insurance payment pursuant to an insurance contract.

3 Then you just look at the general rule. And I believe
4 we cited the Court to Hamlet at Willow Creek Development
5 Company, which is from the Second Department in New York, 64
6 A.D. 3rd 85. And the test there is as follows: Subrogation
7 includes every instance in which one party pays a debt for
8 which another is primarily answerable, and, with the equity and
9 good conscience, should have been discharged by the latter, so
10 long as the payment was made either under compulsion or for the
11 protection of some interests of the party making the payment
12 and in discharge of an existing liability.

13 What we would submit here, your Honor, if you follow
14 through on that test, this is not a debt and it's not an
15 existing liability. There is nothing that has been
16 crystallized either in the contract sense of a debt or in the
17 sense of an existing liability, as opposed to a contingent
18 liability. There is no compulsion here. This is not a case
19 where the debtor entities were forced into this contract, nor
20 is this a case where they are simply pursuing or fulfilling
21 their preexisting contractual obligations -- they decided to
22 enter into this contract after the fact -- nor was it to
23 protect DCL's interest. It's DCL, Dexia Credit Local, is the
24 entity that purchased the certificates.

25 THE COURT: You have to forgive our reporter. He

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1 doesn't speak the Queen's English.

2 MR. SLIFKIN: We know each other from the Vivendi
3 cases. At least I'm not speaking in French today. He did tell
4 me to be slow and clear, so I will make an effort.

5 If you put that together, if you look at the test that
6 the Second Department set forth in Hamlet at Willow Creek, and
7 you say to yourself, well, this isn't the insurance context, as
8 I said, not a debt, not an existing liability, there is no
9 compulsion and it's not protecting DCL's interests and,
10 therefore, the test is simply not met.

11 It's simply not the case that by purchasing the assets
12 at par, they automatically get the assignment rights.
13 Equitable subrogation is not a back door way to get around the
14 pretty clear New York law that there needs to be an express
15 assignment of the rights in litigation, the fraud claim, nor
16 have the courts interpreted to do that, your Honor. So that's
17 our response with respect to equitable subrogation.

18 I don't know where the Court wants us to proceed.
19 With your permission, I'll start from the beginning.

20 THE COURT: I do want to make clear, I have not
21 reached any conclusion on any of the issues, but let me flag
22 for you, and really for your adversary, I thought the most
23 troubling issue for the Court on the first reading of the
24 papers was the reliance issue, and plaintiffs seem to have
25 moved away from some of the representations that they, in their

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1 pleadings, say they relied on, and I will flag for plaintiffs
2 right now, because this is going to be the question I'll put to
3 them when counsel for the plaintiffs gets up, is, show me with
4 some precision what it is exactly you say you relied on to your
5 detriment in this case.

6 On a first reading, at least, and, of course, the
7 papers here are quite voluminous, the exhibits were boxes and
8 boxes and it is fortunate because it's very cold outside and I
9 certainly need to have something to burn in the fireplace, but
10 I really, still, with all of that, had difficulty putting my
11 finger on what it is exactly that plaintiffs now say, based on
12 the record that's before the Court, as opposed to just the
13 pleadings they relied upon.

14 But you're welcome to address anything you want. I
15 just wanted to flag that for you. It might be helpful to your
16 argument as well.

17 MR. SLIFKIN: Why don't I do this, if it's okay with
18 the Court. I'll start with reliance, since you've identified
19 that issue. Then, given whatever time we have, I'll spend a
20 little more time on the assignment issue, standing issue, and
21 we can either do that after a response or before.

22 THE COURT: We have until 6:00. Why don't you spend
23 at least 10 or 15 minutes on reliance, if you like, and then we
24 will hear from plaintiffs' counsel, and then we will go back to
25 you. That's a good idea.

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1 MR. SLIFKIN: Great.

2 So our submission on reliance is as follows, your
3 Honor. The key, the core alleged misrepresentation here, as we
4 discussed when we were here on motion to dismiss, is whether or
5 not there was compliance with underwriting guidelines. There
6 is a representation that there was compliance with underwriting
7 guidelines, generally, and what we understood the core of this
8 case to be is, is that correct or not correct.

9 Now, essentially, all of the appendix to the
10 complaint, which identifies various alleged misrepresentations,
11 concerns alleged misstatements in prospectuses and prospectus
12 supplements. I say essentially all because there are a couple
13 of private-placement memoranda. If you lump those together,
14 they are essentially prospectuses and prospectus supplements.

15 We now know however, that FSA didn't read the
16 prospectus supplements and, therefore, cannot have relied upon
17 them under New York law, which requires actual eyeball
18 reliance. That's crystal clear from Mr. Hendrickson's
19 testimony. The question is: You were making your investment
20 decisions before the PROSUPPS were available?

21 THE COURT: I understand that part of your argument.
22 I think there is some force to that part of your argument. So
23 then the question is, what's left that they rely upon?

24 MR. SLIFKIN: Right.

25 So let me briefly touch on what might be left with

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1 respect to the allegation with respect to compliance with
2 guidelines.

3 In Exhibit 72 to Mr. DeLange's affidavit --

4 THE COURT: Let me pull that out since both parties
5 refer to that repeatedly.

6 Go ahead.

7 MR. SLIFKIN: I am not going to go through page by
8 page, but let me summarize for the Court the point we want to
9 identify.

10 That's a chart identifying representations to Dexia.
11 There were 51 offerings here. For 18 of those offerings, if
12 you work your way or your clerk works her way through the
13 chart, for 18 of those offerings you will see there is no
14 representation whatsoever about compliance with underwriting
15 guidelines, so those 18 fall away on that allegation.

16 For 13 additional offerings there is a representation
17 with respect to underwriting guidelines, but it appears only in
18 a prospectus or prospectus supplement, and we know they didn't
19 read them. So that leaves only 20 offerings where there is
20 even a possibility of reliance with respect to the allegation
21 of noncompliance.

22 But there is absolutely no evidence whatsoever that
23 for those 20 offerings FSA, FSAM, specifically relied on the
24 statements about underwriting compliance. We have the Albus
25 testimony and we have the Hendrickson affidavit, which we put

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1 in on summary judgment, and neither of those does it for
2 plaintiffs. Neither of those says, on those 20, yes, we have
3 looked at that language and we relied upon that point.

4 If I might just quickly talk about the Albus
5 testimony, which is relied upon by plaintiffs in their papers,
6 and this is obviously in the record, it's the Earnhardt Exhibit
7 17. And we refer the Court to specifically page 126 to 127 of
8 that transcript where Mr. Albus, having testified that he
9 received term sheets, what he calls term sheets, which are
10 preliminary materials, and what he calls a CDI file, which is
11 an electronic data file, which really doesn't have any textual
12 representations in it at all. It's just a computer file of
13 numbers. He is asked: Okay. For a fact do you have a
14 specific recollection -- I'm paraphrasing pages 126 to 127 --
15 do you have a specific recollection of what it is you relied
16 upon, what representations you received?

17 "A. I don't recall the specific conversations or information
18 that was gathered."

19 Of course, as your Honor knows, under New York law,
20 everything has to be proven by clear and convincing evidence.

21 Then we go to Mr. Hendrickson's affidavit, which was
22 submitted on summary judgment, and that is very carefully
23 drafted. And it's very carefully drafted to not say he relied
24 upon the representations regarding underwriting compliance.

25 Paragraph 3 of that affidavit says: They received and

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1 relied on the first statements contained in the documents
2 prepared by or provided by the defendants in this action prior
3 to the purchase of the certificate. But there is no
4 specificity whatsoever. This wouldn't, we believe, pass muster
5 on a pleading motion. It certainly shouldn't pass muster on
6 summary judgment where we are saying, is there something a
7 reasonable juror could say is clear and convincing evidence of
8 reliance.

9 Now, then you have paragraph 4 of Mr. Hendrickson's
10 affidavit, and he says --

11 THE COURT: Let me pull that out while we are talking
12 about it. Do you have some other reference?

13 THE LAW CLERK: Do you have an exhibit number?

14 MR. SLIFKIN: Hendrickson's affidavit.

15 MR. VALDES: It's not an exhibit.

16 MR. SLIFKIN: An affidavit that the plaintiff
17 submitted.

18 MR. BERGER: We can hand it to you.

19 MR. SLIFKIN: Paragraph 3 I just covered, your Honor.
20 Essentially, it doesn't say which statements they are. It says
21 contained in the documents.

22 Then in paragraph 4 he says: In the ordinary course
23 of business, FSAM maintained deal files containing offering
24 materials for each of the certificates in a central database.
25 True and correct copies of those documents are attached. But

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1 then he doesn't say he relied upon those.

2 THE COURT: I agree with you that this is a less than
3 crystal clear affidavit. The record should reflect that it's
4 quite short. In the first paragraph he says that in 2006 and
5 2007, he was portfolio manager at FSA and the second paragraph
6 he says: I testified in a deposition in this matter on
7 December 21, 2012 as a 30(b)(6) witness for plaintiff FSAM,
8 which made all of the initial purchases of the certificates at
9 issue in this action.

10 Let me pause there. Is there anything in this
11 affidavit that contradicts, in your view, what he said in his
12 deposition?

13 MR. SLIFKIN: No, your Honor. Because I believe it's
14 very carefully drafted not to do so. You are correct in making
15 the link that he is the 30(b)(6) who said the PROSUPPS were not
16 read. The PROSUPPS are included in the documents identified in
17 his paragraph 4 in schedule A. If you were to read his
18 affidavit as saying, if you were to combine those two --

19 THE COURT: Just so we are clear on the record,
20 paragraph 3 says: In the ordinary course of business, FSAM
21 received and relied on the statements contained in the
22 documents prepared by or provided by the defendants in this
23 action prior to the purchase of the certificates. I have great
24 doubts about the admissibility under the Federal Rules of
25 Evidence of that statement, let alone whether it carries

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1 plaintiffs' burden.

2 And then the fourth paragraph it reads: In the
3 ordinary course of business, FSAM maintained deal files
4 containing offering materials for each of the certificates in
5 the central database, true and correct copies of those
6 documents are attached hereto as exhibits listed in schedule A.

7 So I'll want to hear from plaintiff as to what their
8 basis is for believing this adds anything to summary judgment,
9 but I understand the point you are making now.

10 MR. SLIFKIN: On that point, your Honor, we actually
11 cited your Honor's own decision in BUSA Corp. v. Ecogloves --

12 THE COURT: You must have been very desperate.

13 MR. SLIFKIN: Consistent with longstanding precedent,
14 you cannot defeat summary judgment by putting in an affidavit
15 inconsistent with prior deposition testimony.

16 So we think that's the sum total of the evidence with
17 respect to the compliance with underwriting guidelines.

18 Now, it is absolutely true that plaintiffs did receive
19 other data and they now appear to be contending, well, what
20 they did was to review empirical data that were in the
21 marketing materials and that were in these electronic files,
22 and they appear to be making some kind of reliance claim with
23 respect to that.

24 However, there is no allegation, no allegation of what
25 data in that great mass of data that was provided with each of

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1 these deals, what is false, what defendants knew to be false,
2 what plaintiffs relied upon, or what caused their harm. So,
3 again, that's inadequate for a pleading, particularly a Rule 9
4 pleading, and certainly can't pass muster on summary judgment.

5 And so we are clear, we submit there is absolutely no
6 evidence of falsity. And aside from reliance on specific
7 pieces of information, there is no evidence of falsity with
8 respect to the data. We might have a debate as to some of the
9 evidence about due diligence and I know your Honor is familiar
10 with the EV1, EV2, EV3. We can debate that back and forth, and
11 we are expressly not doing that on summary judgment.

12 But when it comes to the data, the numbers, the
13 metrics and so forth, about the loan pools underlying the
14 certificates, the mortgages themselves, there is no allegation
15 of falsity. There isn't a single mortgage that's identified or
16 single number where they say that number is wrong, let alone,
17 and you knew it and we relied upon it and it caused our harm.

18 Now, there is one statement, argument the plaintiffs
19 make in their papers which said, if you did bad underwriting,
20 if you did bad due diligence in re-underwriting, then the
21 numbers must be wrong.

22 THE COURT: I do think that's a large part of their
23 argument and I, again, flag for plaintiff, I'm finding it very
24 difficult to get my arms around that argument as a legal
25 matter.

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1 But why don't you go ahead and say what you wanted to
2 say about that and I'll have some questions for them.

3 MR. SLIFKIN: I didn't have much to say beyond what
4 you just said, your Honor. We don't understand that. Let's
5 say a FICO score is 650. That may comply with the guidelines,
6 it may not comply with the guidelines. Let's say it doesn't
7 and that's missed. And so there is poor re-underwriting. It
8 doesn't make the number false. It just doesn't, as a matter of
9 law. Nor is there any witness who has really testified to
10 that.

11 They cite to Mr. Miller of JP Morgan. He doesn't say
12 that at all. It's just not said in his testimony. They cite
13 to Mr. Beck of Washington Mutual. Again, I think if you read
14 the whole of Mr. Beck's testimony, which is identified in
15 DeLange Exhibit 64, and we would refer your Honor to pages 244
16 to 245, it's very confused, the testimony, but he certainly
17 doesn't say what I just said, which is bad underwriting makes
18 the numbers wrong, and there were no witnesses from Bear
19 Stearns whatsoever that they even bother to cite on this topic.

20 Let me say about a word about justifiable reliance and
21 then maybe go back to standing if and when your Honor wants to
22 hear more about it.

23 THE COURT: Let's hear from plaintiffs' counsel on
24 reliance, and then we will come back to the other issues.
25 Thank you.

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1 MR. SLIFKIN: Thank you, your Honor.

2 MR. DeLANGE: Thank you, your Honor. Timothy DeLange
3 with Bernstein Litowitz on behalf of the plaintiff. I want to
4 respond directly to the Court's questions during Mr. Slifkin's
5 argument.

6 There is evidence of direct reliance and at
7 Mr. Hendrickson's deposition he made very clear what FSAM
8 relied upon when they were making purchase decisions for
9 mortgage-backed securities, and I can point you to our separate
10 statement and it's really contained in paragraphs 191 through
11 194.

12 THE COURT: I'm sorry. 191 through 194 of what?

13 MR. DeLANGE: Of plaintiffs' affirmative 56.1
14 statement of additional facts. And specifically, your Honor, I
15 would point you to paragraph 192, which talks about the
16 information that was relied upon.

17 For example, Hendrickson says at page 28, line 16
18 through page 29, line 17: Important factors in Dexia's
19 investment decision included LTV ratios, FICO scores, whether
20 property was owner occupied or investor owned, percentage of
21 second liens, and geographic distributions. There is
22 additional testimony --

23 THE COURT: So this gets to the last point I was just
24 discussing with counsel. The thrust of your complaint appeared
25 to be that there was not compliance with guidelines, as had

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1 been represented in the prospectus and prospectuses. Now, all
2 sorts of problems have arisen with respect to anything in the
3 prospectuses.

4 If the claim is, we relied on various things about LTV
5 ratios, FICO scores, whether property was owner occupied or
6 investor owned, et cetera, the alleged failure of the
7 defendants to comply with their guidelines does not render any
8 of that data false, per se, let alone any individual plaintiff.

9 So I'm having trouble following exactly what your
10 argument is here.

11 MR. DeLANGE: I can answer your question. The first
12 point I want to highlight, defendants didn't move on falsity
13 and they are arguing falsity, and we have to come forward with
14 falsity and I'll give you a specific example to respond to your
15 question.

16 The EV3s, when they come from the due diligence
17 provider, they identify what the problems are with those loans.
18 And those EV3s --

19 THE COURT: I think the reason they didn't argue
20 falsity is because you didn't identify, unless I missed it, in
21 your complaint any given FICO score that was false, any given
22 LTV ratio that was false. That wasn't the thrust of what you
23 said was false. What you said was false was the representation
24 that they complied with their guidelines, yes?

25 MR. DeLANGE: That's not correct, your Honor. The
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1 attached exhibits to the complaint allege violations of
2 guidelines and also allege falsity with respect to LTV ratios,
3 falsity with respect to debt-to-income ratios.

4 THE COURT: Let me take a look at that.

5 Here we have the amended complaint, a typically short
6 and plain statement, as Rule 8 requires, consisting of 144
7 pages plus exhibits.

8 Now, before we get to the exhibits, point me to where
9 you allege in the body of the complaint the falsity other than
10 the falsity with respect to the noncompliance with the
11 guidelines.

12 MR. DeLANGE: Paragraph 237 is where I would start,
13 your Honor. And paragraph 237 states, and then I can continue
14 the specific allegations, but it states very clearly:
15 Defendants made specific representations about the quality of
16 the mortgages backing the RMBS in the offering materials.
17 Defendants sent plaintiffs marketing materials, free writing
18 prospectuses and term sheets describing the quality of the
19 mortgage pools and the anticipated RMBS credit ratings to
20 induce plaintiffs to purchase certificates in the offerings.
21 That's exactly what happened. That's exactly --

22 THE COURT: That paragraph is, as you know, other than
23 as a prelude, meaningless, because it's totally conclusory. It
24 doesn't specify the representations.

25 MR. DeLANGE: That's right, your Honor. And I want to
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1 complete that paragraph because that's important as to what has
2 occurred here. Defendants made the same or substantially
3 similar representations about the quality of the securitized
4 mortgage pools and the final RMBS credit ratings in the
5 registration statements, prospectus, and prospectus supplements
6 that the defendants filed publicly with the SEC. You then
7 continue and there is all of these specific false statements
8 that we allege. And, for example, on page 108 of the
9 complaint --

10 THE COURT: The first one you talk about, this is in
11 paragraph 238, is the representations about compliance with the
12 underwriting guidelines, right?

13 MR. DeLANGE: That is correct, your Honor. And then
14 on page 104 we talk about false statements with respect to loan
15 selection and due diligence practices.

16 THE COURT: Let's look at that. Defendants
17 represented that the loans in the securitizations were
18 carefully selected and properly underwritten, right? That's
19 the same thing. I'm not saying where you say --

20 MR. DeLANGE: I can give you specifics. Let me get
21 you to the specific numbers, the LTVs that you're looking for,
22 your Honor. The falsity with respect to owner occupancy rates
23 is on page 110, starting at paragraph 263. And then the
24 attached exhibits --

25 THE COURT: Just bear with me a second. I'm sorry.

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1 I'm reading from the complaint, 263: Defendants made
2 an affirmative representation about the occupancy rates of the
3 collateral. And then you say, at paragraph 266, that you
4 relied on that to make an investment. And then you say, 267:
5 The statements set forth above, the substantially similar
6 statements in Exhibit E, materially overstated the percentage
7 of mortgages that were secured by owner occupancy residences
8 and thereby materially understated the credit risk of the RMBS
9 at issue. Defendants did not disclose that no due diligence
10 was done on the vast majority of loans included in the
11 securitizations at issue, including New Century loans that
12 could have been approved in 12 seconds or less, and ResMAE
13 loans where the property didn't even exist, it was like a
14 vacant lot, but yet we had an address and pictures. That's all
15 in quotes.

16 In addition, Bear Stearns did not disclose that it
17 expressly instructed its due diligence vendor that occupancy
18 misrepresentations were not a securitization breach and ordered
19 the vendor not to verify the occupancy status and not to order
20 occupancy inspections. 268: Defendants knew that their loan
21 origination and securitization practices materially increased
22 the risk that the mortgage pools backing the certificates
23 included many more mortgages that are not secured by an
24 owner-occupied home than represented in the offering materials.

25 Here is the problem I'm having. You are saying that

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1 the failure in this case to do due diligence and the failure
2 previously referenced to comply with the underlying guidelines
3 were the cause of overstatements, but you still don't say
4 exactly what was the truth that was misstated. So, for
5 example, just going back to the paragraph you drew me to, 267:
6 The statements set forth above and the substantially similar
7 statements in Exhibit E materially overstated the percentage of
8 mortgages that were secured by owner occupied residences.

9 What is your evidence, as far as summary judgment,
10 that these were overstated? We know that you're alleging that
11 the failure to do what they should have done in terms of due
12 diligence, underwriting, so forth, led to you saying a false
13 statement, but I don't see where you are saying exactly in what
14 respect the statements were false.

15 MR. DeLANGE: I can tell you exactly, your Honor. And
16 I can get an exact exhibit. I'll summarize it for you and then
17 I'll get the exhibit and the information to point you to it.

18 Again, I want to back up. This information was all
19 pled in the complaint. I can cite you to the LTV ratios, the
20 credit ratings. It was all pled in the complaint.

21 THE COURT: I'm accepting that for the moment.

22 MR. DeLANGE: And the reason I want to point that out
23 is because defendants didn't move on falsity and we didn't
24 submit evidence of falsity of all of these parameters and
25 variables for every offering. We do have evidence that I will

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1 point you to now that demonstrates this.

2 THE COURT: Go ahead. Let me not interrupt you so
3 much. Go ahead.

4 MR. DeLANGE: Let me tell you what the evidence is.
5 They hired an independent third-party due diligence provider.
6 They reviewed the loan files to make a determination as to
7 whether or not they complied with guidelines. They sent back
8 their results, this independent due diligence provider. The
9 results would highlight loans that did not comply with
10 guidelines. And they would have a breakout of the reasons why
11 they didn't comply with guidelines. Some of those reasons
12 would be, there is no evidence of owner occupancy, for example.
13 There would be evidence in there that there is appraisals
14 overstated or beyond guidelines, which would affect your LTV
15 ratios. There is indications in there that the income is not
16 reasonable or it's not verified. That would affect the
17 debt-to-income ratios.

18 All of that information that they are receiving from
19 the due diligence providers, they are not providing that
20 information to investors and they are not providing that
21 information to the rating agencies when they are securing their
22 triple A ratings that they are going out to sell to investors.
23 I can give you a specific example and walk you through that and
24 that's the evidence that we have that we have gathered.

25 THE COURT: Give me your specific example.

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1 MR. DeLANGE: Your Honor, I am going to start with,
2 Exhibit 23 to Mr. Hendrickson's affidavit declaration has --

3 THE COURT: Hold on. Let me get that.

4 MR. DeLANGE: You may or may not need it. I am going
5 to orient you. This is the information that was sent to us by
6 defendants that has all the various representations of owner
7 occupancy, LTV ratios, FICO scores, the information that was
8 relied upon pursuant to what's been testified by numerous
9 employees.

10 Exhibit 103 to my declaration.

11 THE COURT: I need to see that.

12 MR. DeLANGE: For your law clerk's benefit, I am also
13 going to refer to Exhibit 76.

14 THE COURT: I already have 76.

15 MR. DeLANGE: We have extra copies that we can hand up
16 if that helps.

17 THE COURT: It's all right. She needs the exercise.

18 MR. DeLANGE: I apologize. I'll probably refer to
19 Exhibit 106 as well.

20 THE COURT: I got that. We will start with 103.

21 MR. DeLANGE: Your Honor, just by way of example,
22 Exhibit 103 is an e-mail from Clayton to Joel Readence at JP
23 Morgan and it's identifying the fact that they have reviewed
24 396 loans and 214 of those loans have been identified as EV3.

25 If you turn to Exhibit 76, these are excerpts from the

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1 deposition testimony of Mr. Readence.

2 THE COURT: Hang on just a second. Okay. Which page?

3 MR. DeLANGE: I'm sorry, your Honor. I am going to
4 refer you to Exhibit 76, the excerpts, starting on page 87.

5 THE COURT: Go ahead.

6 MR. DeLANGE: I am questioning in this exchange in the
7 transcript Mr. Readence about the EV3 reports on this same pool
8 of loans. I will represent to the Court the specific document
9 that I'm questioning Mr. Readence on was not submitted with our
10 summary judgment papers for two reasons. One, falsity was not
11 at issue, but, number two, the actual document contains all the
12 listing of the borrower names and information, and we submitted
13 the summary e-mails identifying the number of EV3s as opposed
14 to the specifics that would reveal that personal borrowing
15 information.

16 But during the questioning, for example, on page 87,
17 line 16:

18 And do you see the description is income does not meet
19 guidelines for gray doc type? Do you see that?

20 Yes, I do. Yes, I do.

21 Is that a missing doc issue?

22 That's more than a missing doc issue.

23 If you are being told that the income doesn't meet the
24 guidelines, that's going to affect your debt-to-income ratios
25 on that particular pool.

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1 Turning to the next page, page 88, starting at line 9:
2 Including the property type is unacceptable under the
3 guidelines, correct?

4 Yes, I see that, property type unacceptable under
5 guidelines.

6 That can mean various different things, but it could
7 mean that it's an investment property as opposed to owner
8 occupancy.

9 And then it continues with additional testimony about
10 EV3s that are being told to defendants where the income does
11 not meet guidelines.

12 Moving on to page 90, I reference Mr. Readence to a
13 particular loan.

14 There the EV3 was because appraisal form does not
15 match property type.

16 This is at page 90, line 13.

17 Do you see that?

18 Yes, I do.

19 This is the type of evidence that the defendants are
20 receiving on each of these loans when they conduct due
21 diligence and there is problems with the appraisals, there is
22 problems with the property types, there is problems with the
23 income. All of that goes into the variables of the LTV ratios,
24 the debt-to-income ratios that we alleged in the complaint and
25 now are going to prove at trial.

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1 As I said, your Honor, that is one example. And to
2 conclude with our story, if you look at Exhibit 106, after
3 defendants have conducted their practice of waiving and
4 overwriting these, there is now only 25 EV3s in that loan pool
5 and, of course, that information was not disclosed to FSAM, nor
6 was it ever disclosed to the rating agencies.

7 Started at 214 they were identified by the independent
8 due diligence provider. It ends up with 23 of them. They
9 waived in or overrode the rest of them.

10 That's the evidence that exists for the falsity of LTV
11 ratios, debt-to-income ratios, the owner occupancy, those
12 various allegations in the complaint that we identified and
13 pled and then also had specific exhibits and appendices
14 attached to the complaint.

15 THE COURT: Let me hear from your adversary on this
16 point. Thank you.

17 MR. SLIFKIN: So specifically on this point on what we
18 moved on and what was in the complaint, your Honor, let me
19 first refer you to page 18 of our opening brief, where we
20 absolutely said we were moving against the allegations
21 regarding computational data. I'll quote you from the bottom
22 of page 18.

23 With respect to the alleged misstatements about
24 computational data, plaintiffs have adduced no evidence
25 whatsoever that any such data was misstated, much less that it

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1 was materially and knowingly misstated. So this isn't
2 something I am bringing right now. This was in our opening
3 papers.

4 THE COURT: In any event, I think it would be implicit
5 because if your argument is, even if you hadn't said what you
6 just read, if your argument was, it there was no reliance,
7 that's only meaningful if there has been a showing that there
8 was a false statement. So, in any event, go ahead.

9 MR. SLIFKIN: Second point, your Honor, everything
10 that you were just pointing to is either an allegation or,
11 first off, it's all allegations in the complaint. Going
12 through the complaint, that's not evidence of anything.

13 THE COURT: He was saying, plaintiffs' counsel was
14 properly drawing me to the complaint because I had raised the
15 question of whether this issue had properly been pled in the
16 complaint. He was really responding to my question.

17 MR. SLIFKIN: I understand that, your Honor. But,
18 obviously, nobody in the world should confuse that with
19 evidence.

20 THE COURT: Right.

21 MR. SLIFKIN: I would also note that everything that
22 was referenced in the complaint was a prospectus supplement,
23 and we just went through how none of that was ever read.
24 Whether or not it was misstated, it wasn't relied upon.

25 But when we come to the testimony that counsel

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1 referred you to, that's about the due diligence process.
2 That's the EV2, EV3 process.

3 THE COURT: Let me just raise this. This is not the
4 argument he is making, perhaps. If you have underwriting
5 guidelines and you have due diligence in order to make sure
6 that a someone who is applying for a mortgage loan is someone
7 who you can rely upon and, more generally, that the nature of
8 the mortgages is something that you as an investor later on can
9 rely upon, and the due diligence is not performed and the
10 guidelines are not followed, does it not follow that either the
11 statements that are being given to you about the nature of the
12 mortgage pool are either very likely to be false or are made
13 with such reckless disregard for whether they are true or false
14 as to constitute a misrepresentation?

15 MR. SLIFKIN: I would argue, no, your Honor, and here
16 is why. Let's take the example that counsel referred you to
17 where they say, well, we looked in the mortgage file and we
18 looked in the mortgage file and there is income stated and
19 that's outside our guidelines. He said, well, that makes the
20 debt-to-income ratio given in the prospectus supplement or
21 marketing materials incorrect. That doesn't follow at all.

22 You would have to say, is the income which is found in
23 the underlying file, which is not in compliance with the
24 guidelines. Let's just assume arguendo that that's correct.
25 Was that the same income used in the data to give aggregate

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1 debt-to-income ratios? Because if it was, it may be outside of
2 guidelines, but it's true. It's not false. Unless they can
3 say, we looked in the file and here is a noncompliance income
4 level and there was a different level used to feed into the
5 data put into the PROSUPP, then there is no misrepresentation
6 with respect to the computational data.

7 The same with loan to value. The loan-to-value ratio
8 will be wrong, if the loan amount is wrong. I don't think
9 anybody has ever suggested -- we don't know what the loan
10 amount was, or the appraisal value was wrong, not accurately
11 transcribed. This is not about inaccurate transcription. This
12 is looking at the data in the file, the same data that was used
13 to put into the numbers and see if it complies with a
14 guidelines, but not whether that number was accurately
15 represented in the prospectus supplement.

16 And there is actually one nuance to that and I would
17 like to make one more point, your Honor. The nuance is, if you
18 actually look at the term sheet and the marketing materials,
19 you'll see that the data is given in a very aggregate manner.
20 There are either tables listing ranges or there is just an
21 average given. And the PROSUPPs regularly disclose that the
22 loan data could vary by 5 percent or 10 percent, and that's all
23 in appendix B to our reply papers. It's not even the case that
24 numbers are given on an individualized loan basis. They are
25 given in a very aggregate and summary basis and they said they

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1 can vary somewhat. So to make out a case that those
2 representations, many of which weren't even read, were false,
3 they would have to show a very significant number of data
4 errors, and the evidence they are presented doesn't show any
5 data errors whatsoever. It's all about compliance with
6 underwriting guidelines.
7 If I can make one additional point on this, your
8 Honor, I know you told me basically, don't talk about
9 causation, but I will say one point about causation, because --
10 THE COURT: I didn't say don't talk about it. I just
11 didn't promise to listen.
12 MR. SLIFKIN: If I'm quick, will you promise to listen
13 to me, your Honor?
14 THE COURT: Absolutely.
15 MR. SLIFKIN: Their case on causation is entirely
16 about causation of damage caused by misrepresentation about
17 adherence to underwriting guidelines. Look at Dr. Mason's
18 testimony, which is cited by both parties in the papers. He
19 says nothing about computational data. He does not make any
20 causal connection whatsoever. If their case has now morphed to
21 say, well, okay, fine, don't worry about compliance and
22 underwriting guidelines, I'm really talking about data level
23 errors, they have no case on causation whatsoever, your Honor,
24 none. That's my last point on that.
25 THE COURT: I am going to interrupt you again to give

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1 plaintiffs' counsel a chance to respond to what you just said
2 on the reliance issue, and if he wants to say something about
3 causation as well.

4 MR. DeLANGE: Thank you, your Honor.

5 First thing I want to make very clear is this case has
6 not morphed. This case is the same case that we pled in the
7 complaint. I identified to you all the various variables that
8 we alleged were false in the complaint. We made clear in the
9 complaint that we received term sheets, we received marketing
10 materials. And that's the same information that ended up in
11 the PROSUPPs.

12 In fact, reg AB says, if the information materially
13 changes from the term sheets to the prospectus supplements,
14 they have to notify investors and give them the opportunity to
15 rescind.

16 Judge Cote recently had a very good decision on this
17 in the FHFA case versus Deutsche Bank, very similar situation
18 where the allegations were pled based on the PROSUPPs. They
19 actually only observed the term sheets and Judge Cote said
20 that's fine. She went through how an RMBS offering is made,
21 how the Wall Street banks go out to investors in the entire
22 process, and I direct your Honor to that.

23 I also want to get back to another specific example on
24 reliance, and I cited to the Court specific testimony from
25 witnesses at FSAM that specifically identified for defendants

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1 during their depositions the information that they relied upon.
2 Credit ratings were very important. They relied on the credit
3 ratings on all of these. They were all rated triple A. They
4 relied on the LTV ratios. They relied on owner occupancy. If
5 you look -- I am going to give you an example. It's Exhibit 46
6 to Mr. Hendrickson's declaration, which attaches all the
7 documents. And I have extra copies, if it would help, to hand
8 up.

9 Your Honor, Exhibit 46 relates to one of the WAMU
10 offerings that's at issue in this case. And this is the type
11 of information that would be sent at the initial start of the
12 process to investors, including FSAM. And if you turn to the
13 Bates page ending in 23165, you'll see there is a caret on the
14 fifth class of certificates where there is handwritten notes
15 there and that's a triple A certificate. This document comes
16 from the files of FSAM. This is what they ended up purchasing.
17 This is what they are looking at in this document and they are
18 looking at that tranche with that rating.

19 If you turn to the page ending in 175, there is check
20 marks next to various numbers and representations that are
21 being made here, including to the average FICO score.

22 Turning again to the page ending in 178, there, again,
23 are carets and notations next to the current LTV ratios
24 showing, as they testify in their depositions, this is the
25 information they are looking at when they receive documents

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1 like this asking them to invest in these certificates.

2 Turn to the next page, ending in 179, there is check
3 marks next to the documentation type, the occupancy, the
4 property type. That's the type of evidence that we have to
5 show reliance and that they actually relied, in addition to the
6 clear testimony that's been provided.

7 I want to talk briefly in response on causation,
8 unless your Honor has any further questions on reliance that I
9 can answer.

10 THE COURT: Well, here is what I want to do, because
11 notwithstanding the excellent arguments from both sides, I
12 actually still have a fair number of questions on the reliance
13 issue. I think we need to continue this argument on Monday
14 because, to me, the reliance issue remains a very important
15 issue and not one that I yet feel comfortable one way or the
16 other about.

17 With apology to counsel and to all your fans who have
18 come down to watch, what are you doing Monday afternoon, late
19 Monday afternoon?

20 MR. DeLANGE: Your Honor, I'm scheduled to be in the
21 Central District of California for an argument on a motion to
22 dismiss in a separate case.

23 THE COURT: When are you back?

24 MR. DeLANGE: I didn't want to tell you this earlier,
25 considering your first hearing, but I'm from California. I

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1 know it was the exception.

2 THE COURT: Most of my relatives are from California,
3 and I still love California.

4 MR. DeLANGE: I have that argument in court in
5 California on Monday. I can come back later next week to New
6 York and be available.

7 THE COURT: I am very sorry to hear that. But I think
8 this is an important argument. I don't think the Court should
9 shortchange counsel. The nature of summary judgment, while
10 some summary judgment motions are easy to dispose of, this one,
11 as you know, has involved a great deal of material, and I am
12 finding it very useful to have counsel point me to specifics in
13 reaction to particular questions I have.

14 So you tell me what's convenient for you. When next
15 week would you be available?

16 MR. DeLANGE: Preferably for me, if we could do it a
17 week from today, that would be best for my schedule. If you
18 want to do it earlier.

19 THE COURT: A week from today I'm going to be out of
20 town. Can you do it earlier.

21 Let's get a calendar so we don't talk anything other
22 than specific dates. Tell me when in the following couple of
23 weeks you would be available.

24 MR. DeLANGE: Other than that Monday argument and then
25 needing at least a day to travel, I could argue as soon as

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1 probably Wednesday of next week. Thursday would be more
2 preferable. I don't know the Court's schedule.

3 THE COURT: I think I'm out of town Thursday.

4 MR. DeLANGE: The following week, your Honor, I can do
5 any day.

6 THE COURT: Let's look at the Monday the following
7 week. How about 5 p.m. on Monday, March 4? And I will go
8 until we all drop.

9 Does that work for defense counsel as well?

10 MR. SLIFKIN: That's perfectly fine, your Honor.
11 Thank you.

12 THE COURT: The one other thing, and I don't want
13 anyone to assume anything from this other than just scheduling,
14 I do want, when we reconvene, to set a trial date. There may
15 not be a trial. I may very well grant the motion or I may not.
16 But I want to lock in trial dates now rather than have to worry
17 about that weeks from now. I would think that it would take me
18 at least until the end of March to decide this motion and it
19 would probably be a bottom line end of March with opinion by
20 some time in April. Assuming the motion was denied, you would
21 need some time to prepare. So I think we are talking a trial
22 date no earlier than May, no later than, truly worst case,
23 August. I just mention that so you can start looking at your
24 calendars when we get together next time.

25 I thank you counsel.

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1 MR. SLIFKIN: One very small point, your Honor. You
2 had allowed one deposition to proceed after this hearing being
3 next week.

4 THE COURT: Yes.

5 MR. SLIFKIN: I understand the gentleman involved is
6 still not permitted to travel by his doctor.

7 MR. DeLANGE: That is correct.

8 MR. SLIFKIN: If that doesn't change, would it be
9 possible to move it to the week after that?

10 THE COURT: Sure.

11 Very good. Thanks so much.

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