



THE SUBPRIME BOOMERANG: AFTER THE WRITEDOWNS COMES THE LITIGATION

MARCH 11, 2009

NAVIGANT
CONSULTING

Agenda

- Introduction
- Presentation
 - Veronica Rendon, Arnold & Porter LLP
 - Richard Swanson, Arnold & Porter LLP
 - Jeff Nielsen, Navigant Consulting, Inc.
- Questions and Answers — (*anonymous*)
- Slides — now available on front page of Securities Docket
 - > www.securitiesdocket.com
- Wrap-up



Webcast Series

- Series of webcasts — every other week
- Next: March 25, 2009:
 - **The JDS Uniphase Verdict One Year Later: Lessons from the Largest Securities Class Action Trial in History**
 - **Jordan Eth, Morrison & Foerster LLP**
 - **Allan Kleidon, Cornerstone Research**
- www.securitiesdocket.com/webcasts



Panel



Veronica Rendon



Richard Swanson

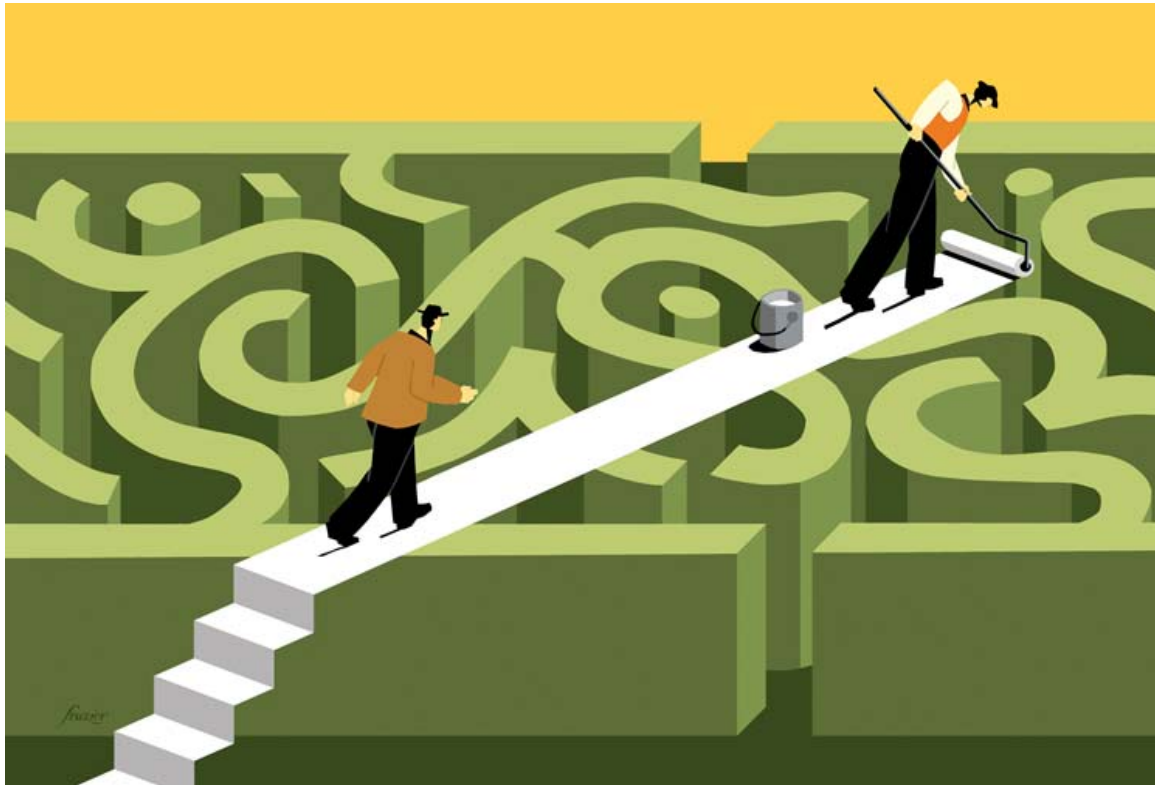


Bruce Carton



Jeff Nielsen





The Subprime Boomerang

*After the Writedowns
Comes the Litigation*

JEFF NIELSEN
Navigant Consulting, Inc.

VERONICA RENDON, Esq.
Arnold & Porter LLP

RICHARD SWANSON, Esq.
Arnold & Porter LLP

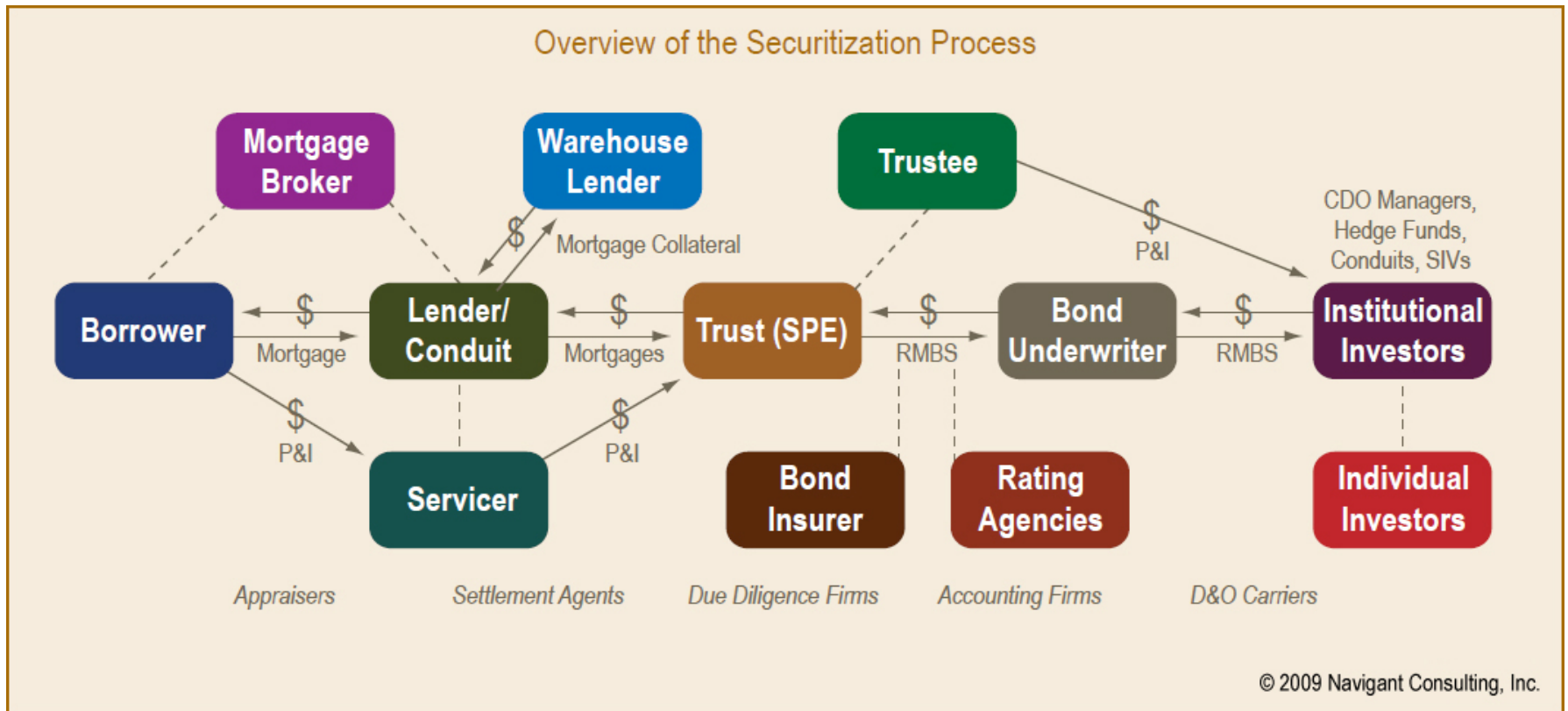
Heightened Litigation / Regulatory Risk

- Staggering Economic Losses +
- Intense Media Coverage +
- Strong Political Winds +

=

**Increase in Civil Litigation
and Government Investigations**

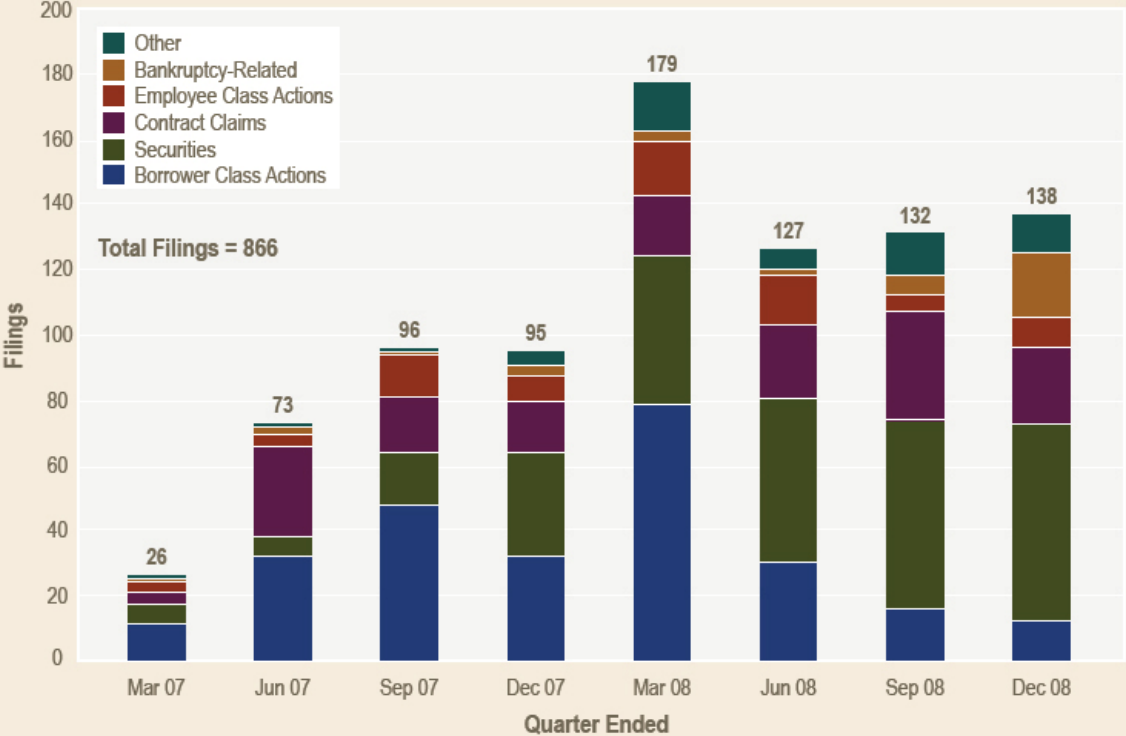
Origination & Securitization Process



Source: Nielsen, Jeff with Scott Paczosa and William Schoeffler, "Subprime Mortgage and Related Litigation – 2008: Seeking Relief," Navigant Consulting (March 2009).

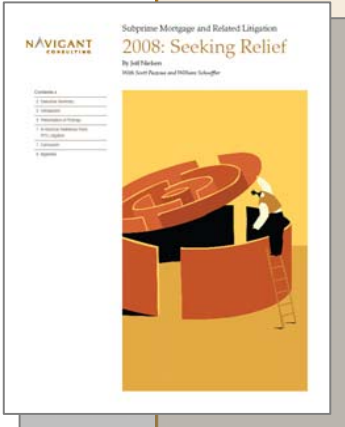
Subprime-Related Federal Filings, 2008

Subprime-Related Federal Filings by Case Type, 2007 – 2008



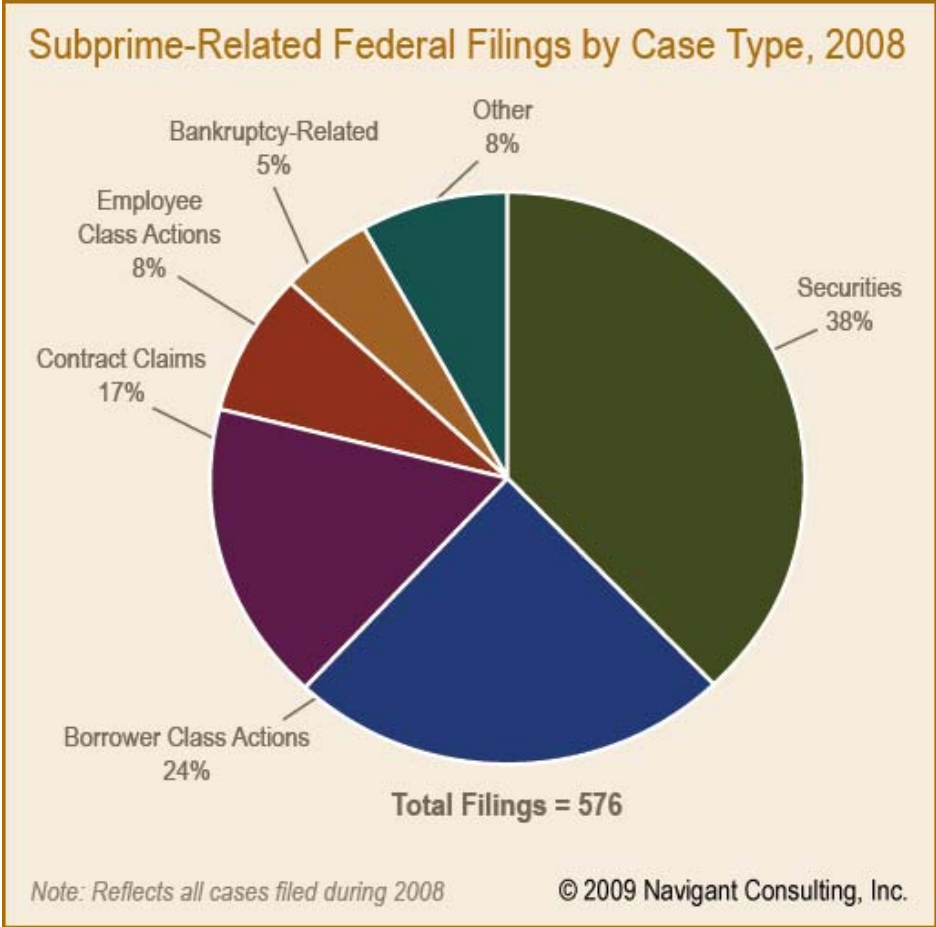
Note: Reflects all cases filed during 2007 – 2008.

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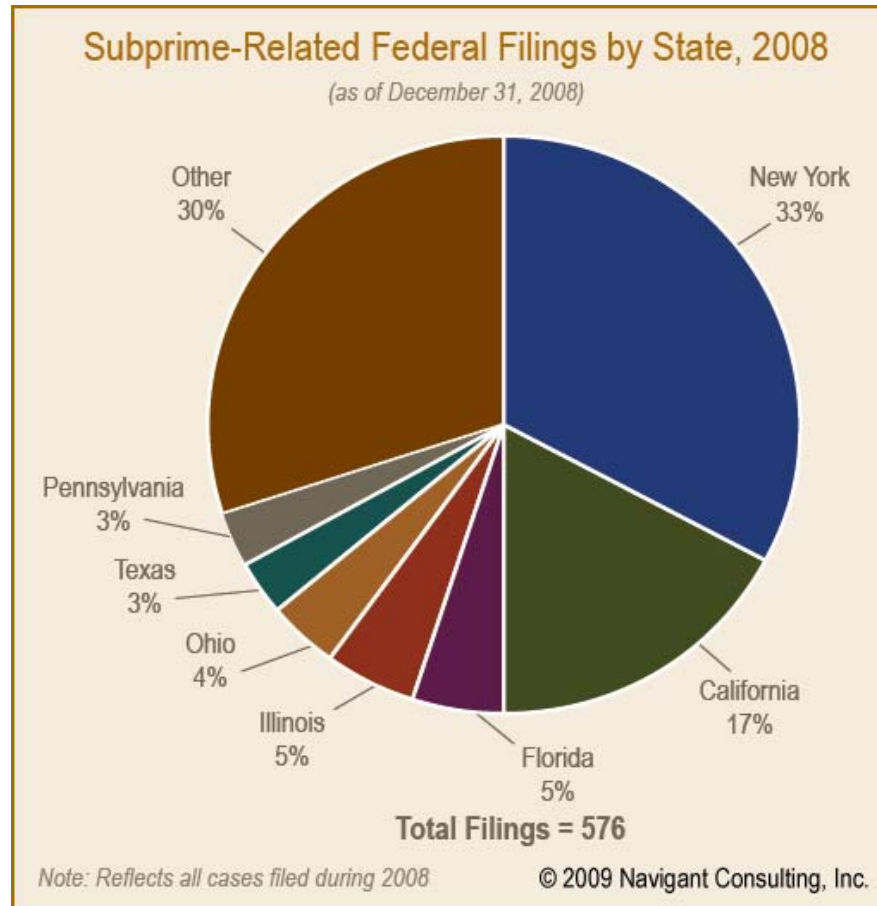
Source: Nielsen, Jeff with Scott Paczosa and William Schoeffler, "Subprime Mortgage and Related Litigation – 2008: Seeking Relief," Navigant Consulting (March 2009).

Subprime-Related Federal Filings by Case Type, 2008



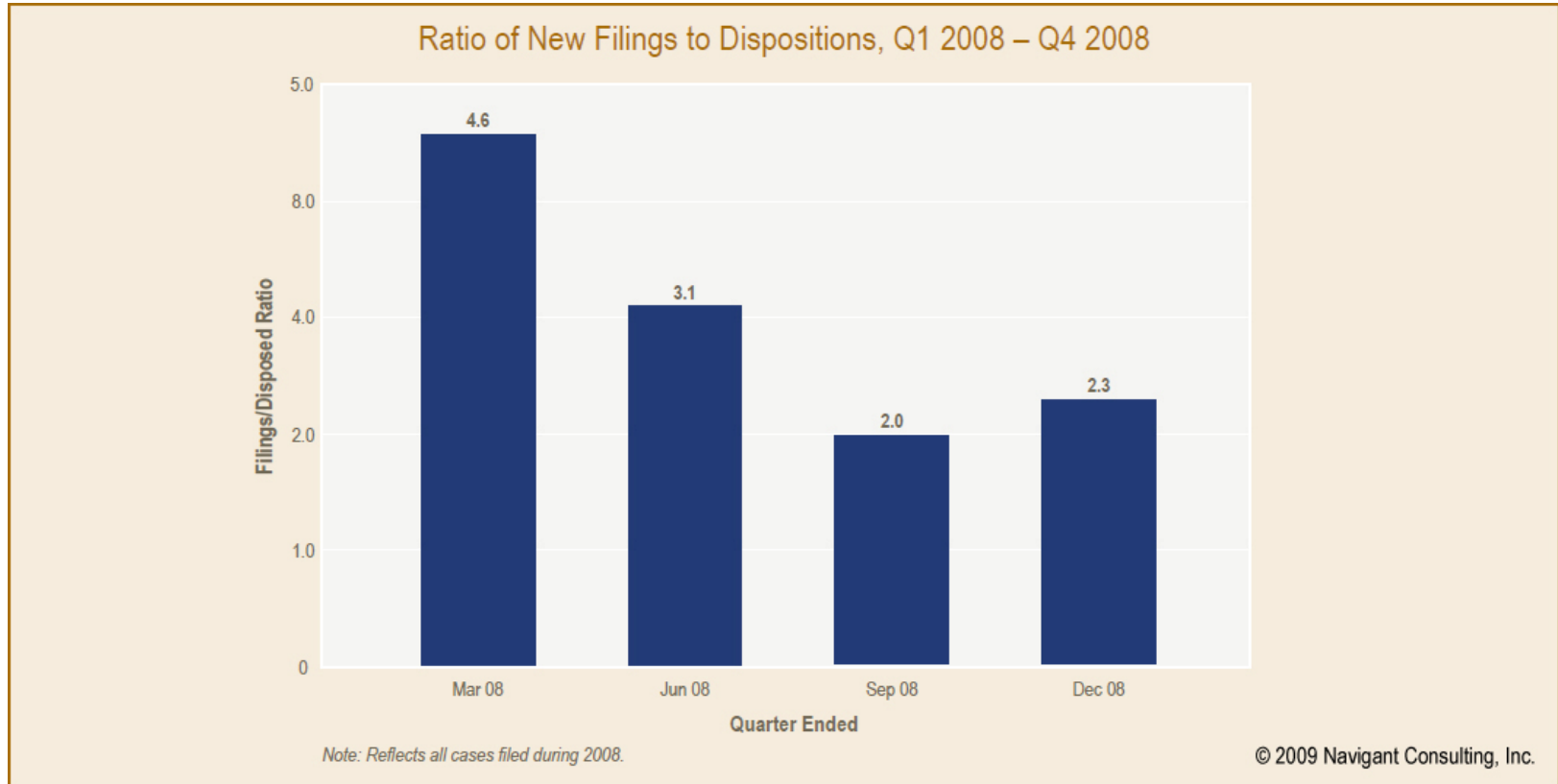
Source: Nielsen, Jeff with Scott Paczosa and William Schoeffler, "Subprime Mortgage and Related Litigation – 2008: Seeking Relief," Navigant Consulting (March 2009).

Subprime-Related Federal Filings by State, 2008



Source: Nielsen, Jeff with Scott Paczosa and William Schoeffler, "Subprime Mortgage and Related Litigation – 2008: Seeking Relief," Navigant Consulting (March 2009).

Status of Subprime-Related Federal Filings, 2008



Source: Nielsen, Jeff with Scott Paczosa and William Schoeffler, "Subprime Mortgage and Related Litigation – 2008: Seeking Relief," Navigant Consulting (March 2009).

Contact Information



Jeff Nielsen is a Managing Director in the Washington, DC office of Navigant Consulting, Inc. and leads the firm's Financial Services Disputes & Investigations service line. For more than 15 years, Mr. Nielsen has advised companies, boards of directors and their counsel on the financial, economic, accounting and data management aspects of commercial disputes and regulatory investigations, specifically matters involving the financial services industry and real estate. He has been retained on more than 75 banking matters and has extensive knowledge of mortgage markets and products, including residential and commercial loans, as well as mortgage banking, servicing, securitizations and capital markets. Mr. Nielsen is currently leading a number of the firm's major subprime-related engagements. He is a frequent speaker on mortgage-related issues and has been quoted, or has had his work cited, in publications such as *American Banker*, *National Mortgage News*, *The Wall Street Journal*, and *National Law Journal*.



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The Subprime Boomerang: After the Writedowns Comes the Litigation

March 11, 2009

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What Happened and Why Are We Here?

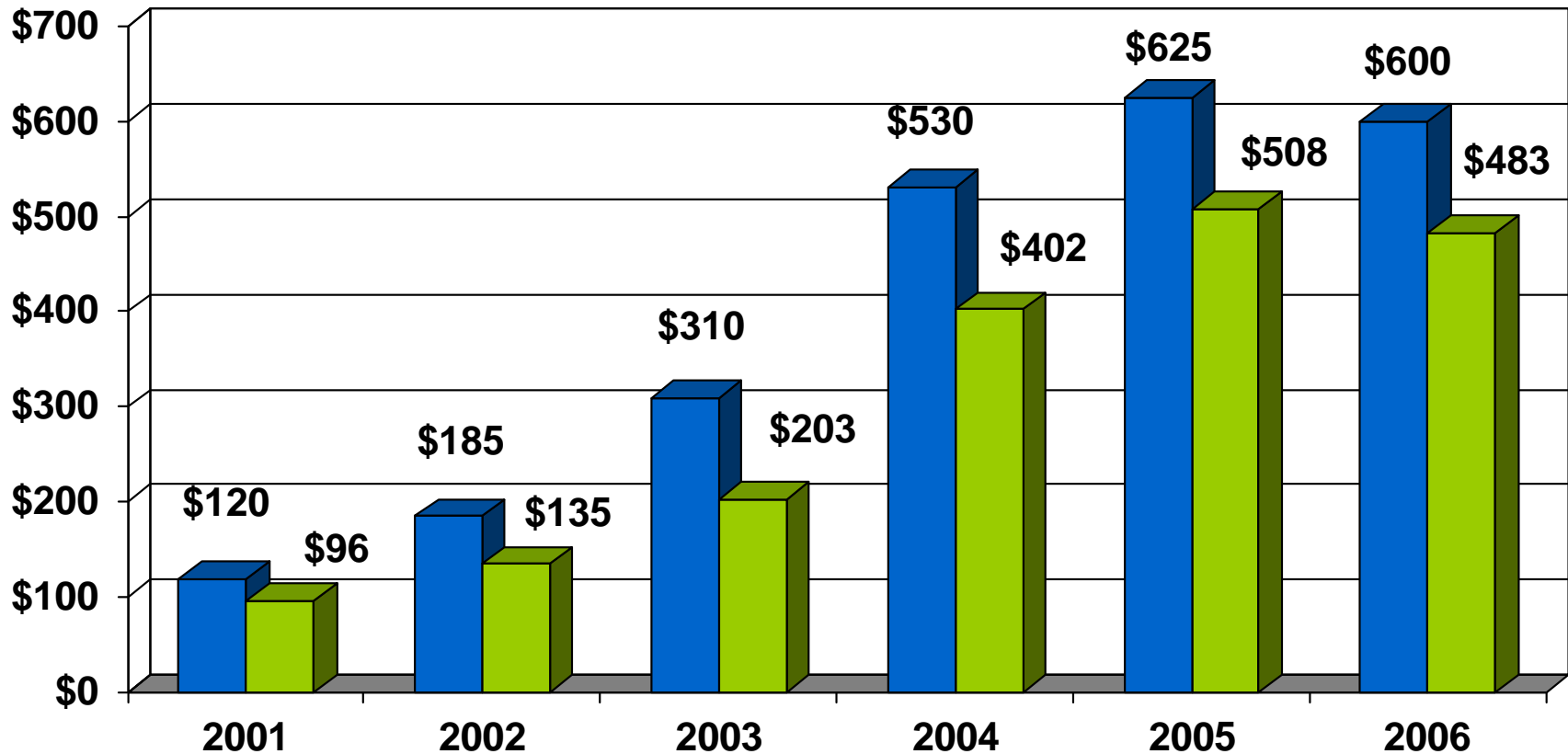
Why the Market was Ripe for Growth

- Issuance of “non agency” MBS grew from \$157 billion in 2000 to \$1.2 trillion in 2006
- Overall issuance of subprime non-agency MBS grew from \$96 billion in 2001 to \$483 billion in 2006
- Created surging demand for mortgage paper and increased competition
- Originations and MBS market share have more than doubled over the last few years

Subprime Originations and MBS Market Share

■ Originations

■ Share of MBS



Why There Is A BIG Problem

- The Fed raised interest rates 17 times since 2004
- Home prices have stagnated (or fell) throughout the country
- Delinquency and default rates have soared
- Delinquent borrowers can not refinance or sell
- Foreclosures have spiked
- Warehouse lenders cut financing to originators and have seized collateral
- Value of subprime RMBS has fallen
- Forced sales have caused further downward pricing pressure

Why There Is A BIG Problem

- 50 percent of ARM originations over past four years have been subprime
 - 80 percent of 2005 subprime originations were ARMs, most were 2/28 hybrids
 - Nearly 2 million subprime ARMs will reset by the end of 2008, with monthly payment increases of 30 percent or more

- Underwritten without consideration of layering of risk
 - No doc/low doc
 - Debt-to-income ratios based on teaser rates
 - Increasing loan-to-value ratios
 - Prepayment penalties

The Subprime Meltdown

“[T]he turbulence originated in concerns about subprime mortgages, but the resulting global financial losses have far exceeded even the most pessimistic estimates of the credit losses on these loans.”

Ben Bernanke, Chairman of the Federal Reserve, September 20, 2007



Significant Fallout Ripples Around the World

- Many lenders and banking institutions have failed
- Write-offs continue
- As noted in Navigant report, global write-offs over a trillion
- Bear Stearns goes under
- Freddie and Fannie go into conservatorship
- Lehman Brothers files Chapter 11
- Merrill is acquired by BoA
- AIG acquired by government, continues to struggle
- Goldman and Morgan Stanley convert to bank holding companies
- WaMu fails
- Leads the way to the largest bailout in history
- Jury still out whether it will work

Bond Insurers Are Struggling

- Significant Subprime Exposure
 - FGIC
 - MBIA
 - Ambac
 - Radian
- Their ratings have declined
- Subject of lawsuits
- Instituting lawsuits

Lawsuits, Lawsuits, Lawsuits

- Significant amount of borrower class actions
 - Alleging fraud in the borrowing process
 - Unfair and undisclosed fees
- Failure to disclose terms and consequences
- Predatory/discriminatory lending practices
- Violations of state statutes (e.g., California)
- Primary defendants: mortgage companies, commercial banks, thrifts
- Interesting downstream consequences

Lawsuits, Lawsuits, Lawsuits

- 10(b)-5 Class Actions and Derivative Suits
- “Stock drop” cases
- Shareholders claiming public companies made materially false and misleading public statements
 - Failure to disclose exposure to subprime risk
- Many classes of securities
- Targets: lenders and brokers, builders, credit insurers, rating agencies, finance companies

Lawsuits, Lawsuits, Lawsuits

- 10(b)-5 Class Actions and Derivative Suits
- Still early but...
- Mixed results for early motions to dismiss
- Tellabs and scienter pleading
- Divergence in securities and ERISA claims?
- Chancery Court dismissal for failure to monitor subprime risk
- Dura Pharmaceuticals and loss causation
- Class Certification: IPO, Allegiance Telecom, Enron, Williams

Lawsuits, Lawsuits, Lawsuits

- Purchaser of subprime asset lawsuits
- Primary targets include originators, underwriters, placement agents
- Misrepresentations in the offering documents
- Suitability
- Potential '33 Act liability as well as '34 Act
- State law claims as well
 - Common law fraud
 - Breach of contract
 - Breach of fiduciary duty

Other Securities Laws Claims

- Auction Rate Securities
 - Alleged Misrepresentations
 - Suitability
- State AG actions
- Large investor claims falling outside of regulatory settlements

Commercial Contract Disputes

- Diverse types of cases
- Hard to track
 - Often filed in state court
- Forced buy-back cases
 - Bond insurer lawsuits
- Improper servicing claims
- A lot of activity behind closed doors
- Sophisticated parties capable of extensive due diligence

Credit Default Swaps and Collateral Priority

- Many large cases involving poor documentation
- Often issuer-related credit issues drives resolution
- A lot of activity behind closed doors

SEC Enforcement Activity

“Our division of enforcement is ... actively on the lookout for possible securities fraud involving the securitized packages of these loans.”

Christopher Cox, Chairman, SEC, Testimony to House Financial Services Committee, 6/26/07

"We will look for any potential fraud, by management, auditors, lawyers, credit-rating agencies, or others."

Walter G. Ricciardi, Deputy Director, Enforcement Division, Testimony to Committee on Financial Services, 9/20/07

Where are we headed...

- Madoff madness
- Stanford
- Others?

Questions?

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SECURITIES DOCKET
GLOBAL SECURITIES LITIGATION AND ENFORCEMENT REPORT

Thank You

Thank you for attending this webcast.

Next webcast:

March 25, 2009, 2:00 pm EST

***“The JDS Uniphase Verdict One Year Later:
Lessons from the Largest Securities Class Action Trial
in History”***

