Materiality Analysis of RMBS Misrepresentations

In *National Credit Union Administration Board v. Credit Suisse Securities (USA) LLC, et al.* (D. Kan. No. 2:12-cv-02648) and *National Credit Union Administration Board v. UBS Securities, LLC, et al.* (D. Kan. No. 12-cv-02591), plaintiff alleged that defendants violated Sections 11 and 12(a)(2) of the Securities Exchange Act because material facts about certain characteristics of the loans underlying the RMBS certificates were allegedly misstated and originators' compliance with underwriting guidelines was misrepresented in the offering documents.

The Vega team was engaged to support Dr. Ethan Cohen-Cole to analyze whether the allegedly misrepresented loan characteristics would have been material to a reasonable investor's assessment of risk based on the total mix of information available at the time of issuance.

Dr. Cohen-Cole created an industry-standard loan performance model to assess whether plaintiff's claims, if assumed to be true, would have resulted in risk levels that an investor would not have reasonably expected at the time of the issuance based on the disclosures of the supporting loan group's characteristics in the prospectus supplements.

Dr. Cohen Cole's model compared two scenarios, one reflective of the plaintiff's loan characteristic claims ("Plaintiff's Claims Scenario") and one reflective of the maximum risk disclosed in the prospectus supplements ("Disclosed Risk Scenario"). If the expected risk in the Plaintiff's Claims Scenario was higher than the expected risk in the Disclosed Risk Scenario, Dr. Cohen-Cole assessed whether the additional expected risk would have been covered by credit enhancements provided to the investors. *See* Example Model Results: *Comparison of Plaintiff's Claims Scenario and Disclosed Risk Scenario* below.

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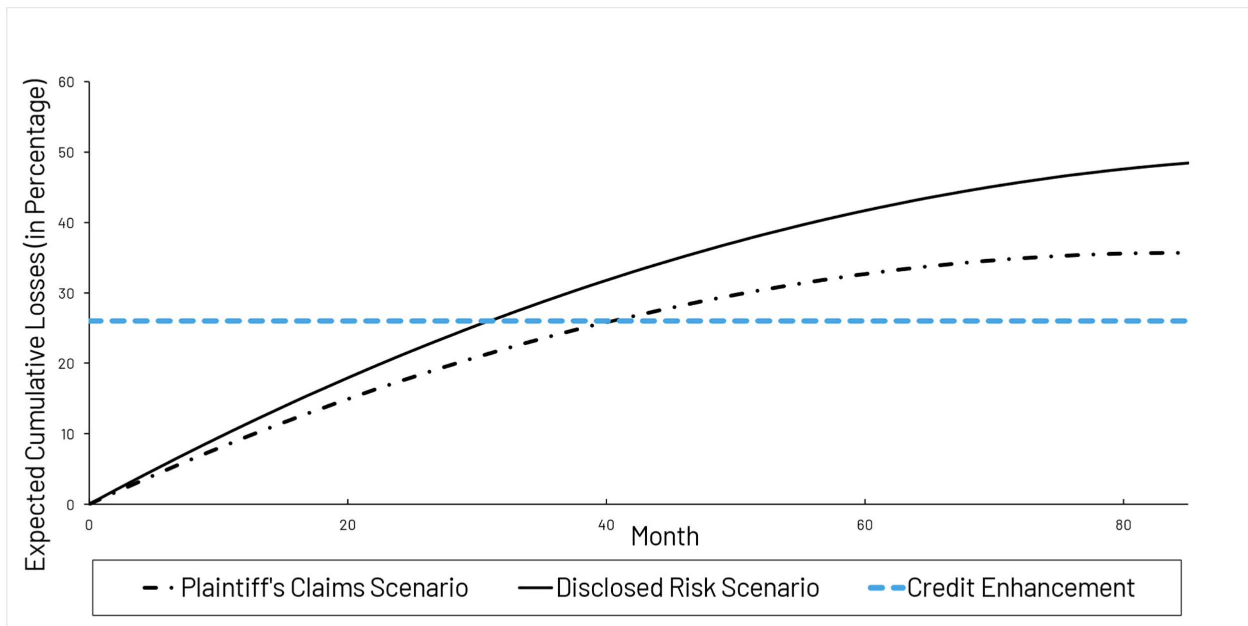
Example Model Results: *Comparison of Plaintiff's Claims Scenario and Disclosed Risk Scenario*



The example model results show that the expected risk in the Plaintiff's Claims Scenario is lower than the expected risk in the Disclosed Risk Scenario. In other words, even if the loan characteristics had been misrepresented, they would not have been material to a reasonable investor's assessment of risk based on the total mix of information available at the time of issuance.

Plaintiff argued that Dr. Cohen-Cole's testimony should be excluded because he failed to apply the correct standard for materiality. Plaintiff further argued that Dr. Cohen-Cole improperly assumed what an investor would find material, the very basis of his analysis.

The Court found that Dr. Cohen-Cole, as an expert with experience in the field, could offer his opinion concerning what a reasonable investor would have considered or found significant in deciding whether to purchase the securities.

Moreover, the Court noted that Dr. Cohen-Cole was not conducting a quantitative analysis to determine which facts a reasonable investor would find material, but instead opining that a reasonable investor would rely on this type of modeling, and his analysis was intended to show the results of the modeling that the investor would have performed. The Court denied Plaintiff's motion to exclude Dr. Cohen-Cole's analysis.

In the past five years, the Vega team has supported experts in over 30 securities fraud cases where plaintiffs have alleged violations of Sections 11 and 12(a)(2) of the Securities Exchange Act and associated state securities acts.