SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

MBIA INSURANCE CORPORATION, Plaintiff, - against - CREDIT SUISSE SECURITIES (USA) LLC, DLJ MORTGAGE CAPITAL, INC., and SELECT PORTFOLIO SERVICING, INC. Defendants.	Index No. 603751/09

PLAINTIFF MBIA INSURANCE CORPORATION'S MEMORANDUM OF LAW IN FURTHER SUPPORT OF ITS MOTION TO COMPEL

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Credit Suisse bases its opposition to this motion on the false premise that it is moot. It presumes that MBIA's fraud claim has been dismissed, disregarding the Court's most recent statement that it is considering the many precedents identified by MBIA – issued before and after the Court's August 9, 2010 denial of Credit Suisse's motion to dismiss – that sustain fraud claims analogous to the one asserted by MBIA. Further, Credit Suisse wholly misconstrues MBIA's breach of contract claims, which would in any event warrant the disclosure sought. The requested disclosure is directly relevant (i) to MBIA's material breach of contract claim, (ii) to its claims that Credit Suisse breached its contractual covenants to give prompt notice of, and to repurchase, breaching loans, and (iii) as admissions of Credit Suisse's breaches of its contractual warranties.

Credit Suisse's opposition also confirms that it has thwarted the requested discovery based upon flagrant misrepresentations to the Court. First, Credit Suisse avoided disclosure of documents reflecting recoveries on its own repurchase demands to originators for HEMT 2007-2 Loans owned by the Trust (the "Repurchase Documentation") by denying such transactions existed. Based on MBIA's showing, however, Credit Suisse now is forced to concede. That is, in a 180-degree reversal from its prior representations to the Court, ***Credit Suisse no longer denies that it obtained recoveries on its own repurchase demands to originators pertaining to Loans in the HEMT 2007-2 Trust*** and did not pass the recoveries on to the Trust as contractually required. Nor does it dispute that it made repurchase demands ***for the very same types of breaches that MBIA has cited as a basis for its own repurchase requests, each of which Credit Suisse has rejected***. MBIA presented evidence of those recoveries that it was able to glean from the existing, piecemeal, production. But the Court should require disclosure of comprehensive accounting records, sufficient to show the materiality of the consideration

received by Credit Suisse in connection with repurchase demands, repricings, or settlements related to the HEMT 2007-2 Loans. MBIA has forcefully and without dispute laid the evidentiary basis that the Court advised would warrant the requested production and, therefore, the discovery should be ordered produced.

Second, after MBIA accurately recounted the history of the discovery proceedings concerning the production of structured data, Credit Suisse now concedes in its opposition that it did in fact represent to the Court that it would ***fully*** comply with the Court's June 24, 2010 Order to produce all relevant data from its PBS Database. But its opposition also confirms that it never did, and it takes the position that it never will.

The PBS Data contains critical evidence concerning Credit Suisse's quality control and repurchase processes. MBIA properly demanded the production of such information to evaluate what Credit Suisse knew about the loans that it sampled and reviewed in relation to the HEMT 2007-2 Loans, whether Credit Suisse complied with its own policies and representations about its quality control practices, and how it interpreted its own warranties and repurchase obligations. Contrary to the Court's prior orders, Credit Suisse did not even disclose the existence of the PBS database until MBIA found references to it in produced documents. Having been caught red-handed, Credit Suisse now takes the remarkable position that, because it has made some piecemeal production of quality control data, it need not make a complete production of the most relevant and comprehensive materials. That, frankly, is an egregious disregard of its discovery obligations.

As to the substantive relevance of the discovery sought, Credit Suisse does not address at all the evidence and arguments made by MBIA. Credit Suisse instead focuses on one issue: In addition to demanding repurchase of HEMT 2007-2 Loans for defects that constituted violations

of Credit Suisse's warranties to MBIA, Credit Suisse also demanded and obtained repurchase recoveries on HEMT 2007-2 Loans based upon early payment defaults ("EPDs") and "no fraud" warranties, which Credit Suisse did not specifically provide to MBIA. What Credit Suisse ignores, however, is the overwhelming and undisputed evidence that it ***knew*** the EPDs were red flags for defective underwriting and borrower misrepresentations, both of which triggered Credit Suisse's repurchase obligations to the Trust. Credit Suisse deliberately disregarded those red flags, and worse, implemented policies and designed its quality control protocols specifically to avoid revealing securitization breaches, in an attempt to circumvent its repurchasing obligation.

This conduct is similar to that which has led to enforcement activity against other securitization sponsors. And Credit Suisse is now the subject of an investigation by the Securities and Exchange Commission, which issued a subpoena this week seeking the same types of documents as MBIA seeks with this motion. In addition, recently disclosed documents bolster MBIA's arguments on this motion, all of which reinforces that MBIA has set a proper foundation for the disclosure it seeks. MBIA's motion should be granted.

ARGUMENT

I. MBIA's Motion is Not Moot

Credit Suisse asserts that MBIA's motion is "moot" because the Court stated on April 7, 2011, in connection with an order it issued in *Ambac Assurance Corp. v. DLJ Mortgage Capital, Inc.*, that it would reconsider its August 9, 2010 Decision and Order (the "August 9 Order") in this action, denying Credit Suisse's motion to dismiss MBIA's fraud claim.[1]

Credit Suisse's argument is presumptuous and premature; the Court has not rescinded its August 9 Order. And for the reasons set forth in MBIA's letter to the Court dated April 11,

[1] *See* Memorandum of Law of Defendants Credit Suisse Securities (USA) LLC, DLJ Mortgage Capital, Inc. and Select Portfolio Servicing, Inc. in Opposition to Plaintiff MBIA Insurance Corporation's Motion to Compel ("Defs. Mem.") at 1, 9, 12.

2011,[2] MBIA respectfully submits that the August 9 Order was correctly decided, is in accordance with each of nine other cited opinions addressing similar allegations,[3] and should not be rescinded. Furthermore, MBIA expects that with an appeal pending in *MBIA v. Countrywide Home Loans, Inc.*, No. 602825/08, the Appellate Division will express its agreement with all of the trial courts that have reached decisions in harmony with this Court's August 9 Order.

More specifically, the two fundamental conclusions upon which the Court's *Ambac* opinion rests – i.e., that Ambac's fraud and breach of contract claims are duplicative and that Ambac had access to all of the same information as Credit Suisse did, precluding a pleading of justifiable reliance on Credit Suisse's misrepresentations – are inapplicable here. First, because MBIA alleges that Credit Suisse misrepresented or omitted material ***present facts*** concerning its existing business practices and characteristics of the HEMT 2007-2 Loans, MBIA's fraudulent inducement claim is not duplicative of its breach of contract claim. *See First Bank of Americas v. Motor Car Funding, Inc.*, 257 A.D.2d 287, 291-92 (1st Dep't 1999) (misrepresentations of present fact may sustain a fraud claim alongside a claim based on breach of contractual warranties).

Second, with respect to justifiable reliance, MBIA alleges at length the reasonable due diligence it ***did*** conduct. And MBIA alleges at length that Credit Suisse did ***not*** provide MBIA with access the information that Credit Suisse had, as the aggregator of the loans that conducted

[2] *See* Docket No. 94.

[3] *See Ambac v. EMC*, 08 Civ 9464, Slip. Op., Feb. 8, 2011, 2011 WL 566776 (S.D.N.Y.) (Berman, J.); *Ambac v. EMC*, 08 Civ 9464, Slip. Op., Jan. 28, 2011 (Katz, M.J.); *MBIA Insurance Corp. v. GMAC Mortgage, LLC*, 600837/10, 30 Misc. 3d 856 (December 10, 2010) (Fried, J.); *MBIA Ins. Co. v. Royal Bank of Canada*, 12238/09, 2010 WL 3294302 (N.Y. Sup. Ct. Aug. 19, 2010) (Scheinkman, J.); *MBIA Ins. Co. v. Countrywide et al.*, 602825/08 (N.Y. Sup. Ct. Apr. 29, 2010) (Bransten, J.); *Syncora Guarantee Inc. v. Countrywide Home Loans*, 650042/09 (N.Y. Sup. Ct. Apr. 2, 2010) (Bransten, J.); *MBIA Ins. Co. v. Residential Funding Co., LLC*, 603552/08, 2009 WL 5178337 (N.Y. Sup. Ct. Dec. 22, 2009) (Fried, J.); *MBIA Ins. Co. v. Countrywide et al.*, 602825/08, 2009 WL 2135167 (N.Y. Sup. Ct. July 8, 2009) (Bransten, J.). *See also Financial Guaranty Ins. Co. v. Countrywide Home Loans, Inc.*, 650736/09 (N.Y. Sup. Ct. June 15, 2010) (prev. uncited).

the loan-by-loan re-underwriting and had exclusive possession of the HEMT 2007-2 Loan files (containing the complete set of documents upon which the loans were underwritten).[4] To facilitate the transaction, Credit Suisse gave MBIA representations and warranties that the Loans bore certain characteristics, and provided MBIA with high-level information summaries, warranted to be truthful, that it intended MBIA to rely upon in evaluating the risk of the Transaction.[5] Those summaries, including the loan tape and due diligence reports, ***contained false information that MBIA had no way of knowing was false***. MBIA relied upon the representations that the information was correct, and to protect itself, had those representations confirmed in contractual warranties.[6]

II. MBIA Has Established the Evidentiary Basis as Required by the Court for Disclosure of All Repurchase Documentation and PBS Data

In January, this Court stated that it would compel disclosure of records reflecting Credit Suisse's treatment of recoveries related to HEMT 2007-2 Loans if MBIA could provide a foundation to conclude that such recoveries existed. The undisputed evidence in MBIA's moving papers, admissions in Credit Suisse's opposition, and newly discovered evidence submitted here, all unquestionably establish that they did.

Indeed, Credit Suisse no longer denies that it demanded repurchase of HEMT 2007-2 Loans for defects that triggered Credit Suisse's (unperformed) obligation to repurchase breaching loans from the Trust.[7] It cannot, based upon the evidence supplied by MBIA.

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[4] *See* Affirmation of Erik Haas, dated March 25, 2011 ("Haas Aff."), Ex. 24 (Complaint) ¶ 29.

[5] *Id.* ¶¶ 22, 29-32.

[6] All of this presumes that MBIA must show "justifiable reliance" upon Credit Suisse's misrepresentations, and not simply that the misrepresentations were material to the risk that MBIA insured. If the misrepresentations denied MBIA the ability to evaluate the risk it was insuring, MBIA – as an insurer – may avoid liability under the insurance policy. *See* N.Y. Ins. L. § 3105.

[7] Plaintiff MBIA Insurance Corporations' Memorandum of Law in Support of Its Motion to Compel, dated March 25, 2011 ("Pl. Mem.") at 8-14 (citing instances in which Credit Suisse demanded and

Moreover, documents produced and identified since this motion was noticed show additional Credit Suisse repurchase demands to originators for HEMT 2007-2 Loans, based upon the same types of breaches MBIA has cited in its putback requests to Credit Suisse, which Credit Suisse has denied.

For example, in August of 2007, Credit Suisse demanded repurchase of loan for breaches including failure to comply with the Truth in Lending Act and failure to comply with underwriting standards, both violations of representations and warranties that MBIA obtained from Credit Suisse.[8] Despite discovering that this loan breached the HEMT 2007-2 securitization warranties, Credit Suisse did not notify MBIA of the defect or repurchase the loan from the Trust, as contractually required.[9] Credit Suisse subsequently received an $80,000 in settlement of this and other loan repurchase demands.[10] But even after receiving this payment, Credit Suisse left the breaching loan in the Trust, from which it was eventually released by defendant SPS to another Credit Suisse affiliate, without consideration.[11] Other examples from Credit Suisse's recent production are loan , put back for fraud, failure to comply with underwriting guidelines, and appraisal irregularities;[12] loan , put back

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obtained recoveries because, e.g., "[t]he loan was not documented according to the applicable underwriting guidelines," and for misstatements of income and occupancy).

[8] Affirmation of David Slarskey ("Slarskey Aff."), dated April 29, 2011, Ex. 1, CS_M0006053869-72 (produced on March 22, 2011). *See also* Affirmation of Darren Teshima, dated Apr. 15, 2011 ("Teshima Aff."), Ex. C at CS_M0000006596, (ii) (truth-in-lending warranty) and (iv) (underwriting warranty).

[9] *See* Teshima Aff., Ex. C (Pooling and Servicing Agreement ("PSA") Excerpts), Section 2.03(e) ("Upon discovery by any of the parties hereto of a breach of a representation or warranty … that materially and adversely affects the interests of the Certificateholders or the Certificate Insurer in any Mortgage Loan, the party discovering such breach shall give prompt notice thereof to the other parties and the Certificate Insurer.")

[10] Slarskey Aff., Ex. 2, CS_M0006040466-68 (repurchase demand) (produced on April 14, 2011).

[11] *See* Trustee Loan Level Data for Apr. 2008, *available at* https://trustinvestorreporting.usbank.com. This practice constitutes a breach of SPS's contractual obligations. *See* Haas Aff., Ex. 24, ¶¶ 63-67.

[12] Slarskey Aff., Ex. 3, CS_M0006053873-76 (repurchase demand).

for borrower misrepresentation and failure to comply with underwriting guidelines;[13] and loan , put back for appraisal problems.[14] Credit Suisse did not provide notice of these defective Loans or repurchase them from the Trust.[15] Nonetheless, it admits that in these types of transactions, "Credit Suisse and the originator sometimes reached a negotiated settlement whereby ***the loan was re-priced at a discount*** that the originator ***paid to Credit Suisse*** in exchange for a release."[16] MBIA seeks disclosure to show all of the recoveries related to any HEMT 2007-2 Loans, whether by repricing, settlement, or other means.

The recoveries on HEMT 2007-2 Loans owned by the Trust, and the related Repurchase Documentation, are relevant both to MBIA's fraud ***and*** breach of contract claims: They show Credit Suisse's motivation and scienter for fraudulently inducing MBIA to participate in the Transaction. Credit Suisse did so, in part, to obtain double-recoveries on the defective Loans by shoveling them into the Trust, profiting from their securitization, and then recovering again when it demanded that the originators of those Loans repurchase them, ***even though Credit Suisse no longer owned the Loans***. The magnitude of the recoveries also will contribute to an award of punitive damages. In addition, the recoveries will show that Credit Suisse violated its obligations to inform MBIA when it discovered HEMT 2007-2 Loans that breached warranties, and to repurchase the same from the Trust.

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[13] Slarskey Aff., Ex. 4, CS_M0005995736-44 (repurchase demand and supporting documentation, with corresponding MLPA showing the basis of the repurchase demand).

[14] Slarskey Aff., Ex. 5, CS_M0005984807-37 (repurchase demand and supporting documentation). *See also id.*, Ex. 6, CS_M0005985955-57 (detailing why the appraisal was faulty).

[15] *See* Trustee Loan Level Data for November 2007 (showing loan "charged off," not repurchased), June 2008 (same for loan), and October 2007 (same for loan), *available at* https://trustinvestorreporting.usbank.com.

[16] Defs. Mem. at 5. Note that this is ***not*** describing "global settlements," for which disclosure has already been ordered in the Jan. 26 Order. Credit Suisse has admitted loan-by-loan repricings and payments received.

Instead of responding to this evidence, Credit Suisse misleadingly suggests that it only "sought to enforce its rights pursuant to the fraud reps and EPD provisions" in its contracts with originators.[17] This suggestion is not only false (as shown above), but misses the point. Credit Suisse knew that EPDs and fraud were red flags that the Loans were originated in violation of underwriting requirements or based upon misrepresentations, breaches that triggered Credit Suisse's notice and repurchase obligations to MBIA.[18] Indeed, Credit Suisse's own RMBS Manual links a finding of EPDs to substandard underwriting.[19] Nonetheless, Credit Suisse intentionally disregarded those breaches, in violation of its contractual notice and repurchase obligations, and in contravention of its representations about its quality control practices.[20]

All of this took place within the context of a broader, ongoing fraudulent scheme. *See Oster v. Kirschner*, 77 A.D.3d 51, 56 (1st Dep't) ("intent to defraud is to be divined from surrounding circumstances"); *DDJ Mgmt., LLC v. Rhone Group L.L.C.*, 78 A.D.3d 442, 443 (1st Dep't 2010) (same). Credit Suisse does not dispute that it systematically manipulated its quality control processes to ***avoid finding*** securitization breaches.[21] As part of its undisclosed policy to avoid "creating a record of possible rep/warrant breaches in deals," Credit Suisse management shut down quality control efforts designed to detect securitization breaches,[22] ignoring clear evidence of such breaches in, e.g., loans it described as "fishy," while putting the loans back to

[17] Defs. Mem. at 5.

[18] *See* Pl. Mem. at 9-10.

[19] *See* Slarskey Aff., Ex. 7, CS_M0004252914 et seq. (RMBS Conduit Process Control Manual ("RMBS Manual")) at CS_M0004253417 (linking EPDs to substandard underwriting).

[20] *See* Pl. Mem. at 14-19.

[21] *See* Pl. Br. at 9-10; *see also* Slarskey Aff., Ex. 8, CS_M0005988876-77 ("[s]ince the EPD request is outstanding, I will not sen[d] the QC review").

[22] Haas Aff., Ex. 11; *see also* Slarskey Aff., Ex. 9, CS_M0005718731 (instructing employees to "hold off" on doing quality control for loans that "tanked" but did not qualify as EPDs).

originators as EPDs and pocketing the recoveries.[23] That is because when it ***did*** review EPD loans it ***found*** credit breaches, which trigger Credit Suisse's (again unperformed) obligation to repurchase securitized loans.

In 2006, Alex Huang, a key Credit Suisse employee who later assembled the HEMT 2007-2 Trust, asked for a review of a group of EPD loans "to find out what went wrong." Credit Suisse determined that 60 percent of the EPD loans did not meet underwriting guidelines.[24] By 2007, management discouraged such reviews, so as not to cause "problems and confusion," and deliberately recalibrated its quality control processes to maximize its own EPD putbacks while minimizing findings of securitization breaches.[25] Credit Suisse ***has admitted*** that delinquencies were caused by bad underwriting, misstated incomes and originators "coaching" borrowers to obtain loans, any of which requires repurchase.[26]

In the case of several high-volume originators of HEMT 2007-2 Loans, Credit Suisse issued credit to originators to finance the origination of loans that Credit Suisse ***knew were sub-standard and likely to default***. Credit Suisse nonetheless agreed to purchase these defective loans intending to securitize them quickly put large numbers of loans back for EPD violations – thus doubly profiting first from the securitization and then from the repurchase recoveries. This practice, developed over a period of years, had ripened by 2007 so that by the time Credit Suisse securitized 2,320 New Century loans into the HEMT 2007-2 transaction (nearly 15 percent of the deal by loan count), it was well aware that New Century loans actually suffered from high rates

[23] *See* Slarskey Aff., Ex. 10, CS_M0005987452-55 (putting back loans for EPD despite evidence of underwriting, documentation, appraisal, and fraud); Ex. 11, CS_M0005979360-61 (ignoring evidence of other violations because EPD "[is] a stronger case for us").

[24] *See* Slarskey Aff., Ex. 12, CS_M0005522336-38.

[25] *See* Pl. Mem. at 9 and Slarskey Aff., Ex. 9, CS_M0005718731.

[26] *See* Slarskey Aff., Ex. 13, CS_M0004263535-38; Ex. 14, CS_M0005718734-35.

of delinquency and deficient underwriting, because ***Credit Suisse was putting back hundreds of New Century loans at a time***.[27] Still, Credit Suisse warranted to MBIA the underwriting of the New Century loans, and denied the breaches when MBIA later found them.

More specifically, in September 2006, Huang emailed the servicer of a pool of New Century loans slated for securitization expressing "concern[] about the amount of deli[n]quent loans in this pool."[28] By March 2007, while assembling the HEMT 2007-2 pool, Huang was "sure" that a number of the New Century loans would default and have to be put back.[29] Indeed, in March, because New Century was on the brink of bankruptcy and the scheme had become unsustainable, Credit Suisse was contemplating an exit strategy for the New Century loans it had bought off the warehouse financing line.[30] A Credit Suisse employee called the collateral backing the loans "a little ugly," in particular because the second liens have "fico [] lower than we normally securitize."[31] Nonetheless, with this ***actual knowledge*** of defective underwriting, Credit Suisse securitized more than 2,000 New Century loans into the HEMT 2007-2 Transaction, gave warranties as to the Loans' qualities, but then denied all of MBIA's repurchase demands when it discovered the same deficiencies that Credit Suisse had known about.

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[27] On February 15, 2007, days after it first met with MBIA, Credit Suisse put back 101 delinquent New Century loans; eighteen of these were nonetheless securitized in HEMT 2007-2 just a few months later. *See* Slarskey Aff., Ex. 15, CS_M0006063214-15. Just two weeks later, Credit Suisse put back an additional 146 loans (55 of which were securitized in the Transaction). *See id*, Ex. 16, CS_M0006060119-22. As of August 2007, Credit Suisse had 658 outstanding putback requests to New Century, totalling over $44 million. *Id.* Ex. 17, CS_M0005641034-35 (attaching repurchase schedule). Of those 658 loans, 252 were securitized in HEMT 2007-2.

[28] Slarskey Aff., Ex. 18, at CS_M0005805595-96.

[29] Slarskey Aff., Ex. 19, CS_M0004277351-53.

[30] Slarskey Aff., Ex. 20, CS_M0004302745.

[31] *Id.* This finding of low FICO scores matches with the statement of Rob Sacco, Credit Suisse's head of underwriting, that New Century and other originators of HEMT 2007-2 Loans were "subprime," even though Credit Suisse represented them to MBIA as originators of higher quality "Alt-A" loans. Slarskey Aff., Ex. 21, CS_M0004303573-74.

The deceit in these practices does not depend on New Century's financial condition, or the risk that the performance of loans (if they had met the warranted characteristics) might deteriorate in the future. It is that Credit Suisse ***knowingly*** securitized defective loans, with the ***intent*** to launder them through its securitization and EPD putback scheme, and while ***concealing*** the evidence of breaches. *See, e.g.*, *Rombach v. Chang*, 355 F.3d 164, 173 (2d Cir. 2004) ("Cautionary words about future risk cannot insulate from liability for the failure to disclose that the risk has transpired").

Credit Suisse did not disclose the truth of its then-present business practices to MBIA during MBIA's consideration of whether to insure payments on the Transaction. Credit Suisse's acknowledgment that it demanded repurchase of HEMT 2007-2 Loans based upon EPDs and fraud, in conjunction with evidence that it knew those findings were hallmarks of securitization breaches, and that it intentionally subverted its quality control practices, provides powerful evidence of the fraudulent intent underlying its misconduct. Indeed, this securitization and putback scheme for defective loans is akin to the conduct that led to Morgan Stanley paying huge fines and restitution in a civil enforcement action.[32] Just this week the SEC issued a subpoena requesting the very same kinds of documents from Credit Suisse that MBIA seeks with this motion.

Finally, Credit Suisse's argument concerning its EPD repurchase demands ignores its servicing obligations. When it identified non-performing EPD HEMT 2007-2 Loans, Credit Suisse, as the servicer of the Loans, had an obligation to pass any subsequent recoveries it obtained on those Loans on to the Trust. Instead, Credit Suisse pocketed the "repricing" or

[32] *See* Appendix A, *In re: Morgan Stanley & Co. Incorporated*, 10-2538 (Sup. Ct. Suffolk County, June 24, 2010) (Assurance of Discontinuance).

"settlement" funds it obtained on those Loans and left them in the Trust to default, and to be released to yet another affiliate of Credit Suisse, without consideration.[33]

Credit Suisse irrelevantly retorts that it negotiated the so-called "no-fraud" and EPD representations that it provided to originators out of the HEMT 2007-2 securitization representations and warranties. But the issue is whether Credit Suisse knew that the Loans did not conform with the representations and warranties that it ***did*** provide. As is clear from the email Credit Suisse cites, in which it denied the EPD and fraud warranties, Credit Suisse stated that, instead of MBIA's proposed fraud and EPD reps, ***Credit Suisse expected MBIA to rely upon the "loan tape rep," the "underwriting rep," and the "compliance rep" as warranting, inter alia, the truth of the information Credit Suisse provided about the Loans*** including their compliance with underwriting guidelines, and the truth and accuracy of the information Credit Suisse provided.[34] Thus, Credit Suisse's knowledge of fraud and EPD triggered its notice and repurchase obligations, based upon the warranties that it ***did*** provide to MBIA.

In sum, far from a "fishing expedition," there is ample evidence that Credit Suisse obtained recoveries on loans owned by the HEMT 2007-2 Trust, with knowledge that those loans breached the representations and warranties Credit Suisse supplied to MBIA, and without notifying the Trust of those breaches or repurchasing the defective Loans. MBIA has met its burden to set a foundation for the Repurchase Documentation it seeks, which should be compelled as in the accompanying proposed order.

A. Credit Suisse Seeks to Evade Production of the PBS Data for All of the Relevant Quality Control Samples as Ordered by the Court

[33] *See* Haas Aff., Ex. 24 (Complaint) ¶¶ 63-65.

[34] *See* Teshima Aff., Ex. H at MBIA_CS00024912-24921 (repeatedly citing existing reps as warranting the factual attributes of the loans). *See also* Slarskey Aff., Ex. 22, Insurance Agreement, Section 2.01(j) ("Accuracy of Information" warranty).

Credit Suisse's opposition reflects its strenuous efforts to avoid disclosure of quality control data central to this litigation, as ordered by the Court in its June 24, 2010 Order of last year. To recount, as set forth in MBIA's opening brief and admitted,[35] Credit Suisse first failed to disclose the existence of the PBS Database and ***denied its existence***. When MBIA discovered the PBS Database by references in Credit Suisse's production, Credit Suisse denied it contained relevant data. When MBIA brought the issue to the Court's attention, Credit Suisse ***then*** said it would fully comply with the Court's June 24, 2010 Order and produce all of the relevant data, and that no further order was required. But Credit Suisse has not done so, and it is now clear that it has had no intention of doing so. Now Credit Suisse's position is that because it has produced some quality control data, it need not produce the central database containing the most relevant data, issuing the fiat that "MBIA Is Not Entitled to Any ***Additional*** Quality Control Information."[36] MBIA cannot obtain "additional" PBS Data because Credit Suisse has not produced any in the first place. ***Credit Suisse has no valid explanation for failing to disclose and produce data from this central repository, as ordered, and it still has not produced any of its PBS Data***.

Credit Suisse does not dispute its policy was to draw samples of loans from various pools in its inventory for quality control review, or its policy that the results of the sampling analysis were to be imputed back to the entire inventory of loans from which they were drawn, for purposes of expanding upon the review as patterns of deficiencies were found.[37] Credit Suisse

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[35] *See* Pl. Mem. at 16-17 and Def. Mem. at 8.

[36] *See* Defs. Mem. at 8 (explaining its failure to disclose in response to the Court's Order on the basis that the database "historically was used by personnel no longer employed by the company." MBIA identified the database by looking at Credit Suisse's RMBS Manual and database manuals; surely Credit Suisse could have identified its own databases) and 12 (emphasis supplied).

[37] *See* Pl. Mem. at 16-19. Quality control analysis was to include a complete "re-verification of employment, income, assets, and appraisals for 100% of the [loan] samples," with occupancy "validated on 5% of loans selected for review." *See* Haas Aff., Ex. 20 (RMBS Conduit Process Manual) at

thus intended for an inference to be drawn regarding the HEMT 2007-2 Loans from related samples, ***regardless of whether the applicable quality control sample actually contained a HEMT 2007-2 Loan***. Nonetheless, Credit Suisse reverses the Court's June 24, 2010 Order, construing it to require production only of quality control data from the samples ***actually containing*** a HEMT 2007-2 Loan, rather than ***drawn from inventory containing*** a HEMT 2007-2 Loan.[38] Plainly, Credit Suisse's construction would deny MBIA the bulk of relevant quality control data. Credit Suisse's reliance on sampling assures that many relevant samples did not actually contain any of the HEMT 2007-2 Loans.

MBIA seeks only that which is necessary to draw the relevant inferences, i.e., the PBS Data ***for the sampled loans that were drawn from inventory containing the HEMT 2007-2 Loans***. The Court's June 24, 2010 Order was based upon MBIA's (now proved) allegations about how Credit Suisse's quality control processes were supposed to work, requiring production of the relevant quality control samples so that MBIA could test the veracity of Credit Suisse's representations about its quality control practices, and its knowledge and understanding of breaches, by extrapolating from the sample sets.[39] This data will show, for example, that Credit Suisse (i) violated its quality control policies as represented; (ii) ignored breaches that

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CS_M0004253346. Properly performed, this would surface sampled loans that did not, for example, meet Credit Suisse's underwriting guidelines regarding, e.g., credit standards, liabilities, employment and income, or assets. *See, e.g.*, Slarskey Aff., Ex. 23 (Credit Suisse August 2006 Correspondent Underwriting Guidelines). And consistent with its pre-contractual representations to MBIA, when there was a "pattern of deficiencies," Credit Suisse's purported policy was to "expand on reviews" to assure the quality of its inventory. Haas Aff., Ex. 25 at CS_M0004253345.

[38] *See* Defs. Mem. at 13.

[39] *See* Pl. Mem. at 5-6 (describing Credit Suisse's pre-contractual representations regarding quality control). In a footnote, Credit Suisse dismisses the significance of the pitchbook cited by MBIA and presented by Credit Suisse at the first meeting between the two parties. *See* Def. Mem. at n.2. Credit Suisse points to fine print in its presentation that "[t]hese materials may not be used or relied upon in any way," as if by including such a disclaimer it could innoculate itself against tort liability for fraudulent business practices. This is nonsense. *See Sommer v. Fed. Signal Corp.*, 79 N.Y.2d 5470, 554 (1992) (disclaimers unenforceable against conduct that "evinces a reckless indifference to the rights of others").

disqualified loans for HEMT 2007-2 securitization or triggered repurchase requirements; and (iii) identified the same defects in its samples as formed the basis for MBIA's more than 4,000 repurchase demands, denied in their entirety by Credit Suisse.

As just one example of the prejudice caused by Credit Suisse's evasions, in the last few weeks since filing this motion MBIA has discovered a serious irregularity in a number of HEMT 2007-2 Loans: ***These loans were previously securitized by Credit Suisse and then repurchased by Credit Suisse as defective***, just months before Credit Suisse pumped them into the HEMT 2007-2 Trust.[40] ***Upon repurchasing these defective loans, Credit Suisse assigned them new loan identification numbers, wiping the slate clean***.

MBIA is unable to determine what Credit Suisse knew about the defects associated with these recycled loans that required their repurchase from other securitizations.[41] Its policies suggest that the loans should have undergone quality control review when they were repurchased. But in the absence of PBS Data, MBIA has been denied the results of that quality control analysis (both under the new or old loan number), and thus critical disclosure concerning the improper practice of repurchasing defective loans from one securitization and recycling them into HEMT 2007-2. Credit Suisse should not be permitted any longer to evade disclosure of its PBS Data as requested by MBIA and ordered by the Court last year.

[40] *See* Affidavit of Afshin Azhari, dated Apr. 29, 2011.

[41] Nor, based upon Credit Suisse's truncated production, can MBIA determine what data was maintained in connection with the loans' earlier loan numbers, or whether ***other*** HEMT 2007-2 Loans were previously assigned other loan_ids, by some other process. *See id* ¶¶ 9-10.

CONCLUSION

For the foregoing reasons, MBIA's motion to compel should be granted and MBIA's Proposed Order should issue.

Dated: New York, New York
April 29, 2011

PATTERSON BELKNAP WEBB & TYLER LLP

By: */s/ Erik Haas*

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Appendix A

CIVIL ACTION COVER SHEET	TRIAL COURT OF MASSACHUSETTS SUPERIOR COURT DEPARTMENT COUNTY: SUFFOLK	DOCKET NO. 10-2538 E

PLAINTIFF(S) Commonwealth of Massachusetts	DEFENDANT(S) Morgan Stanley & Co. Incorporated
ATTORNEY, FIRM NAME, ADDRESS AND TELEPHONE Glenn Kaplan, AAG, Office of the Attorney General 1 Ashburton Place, 18th Floor, Boston MA 02108 617-963-2453	ATTORNEY (IF KNOWN) Frances S. Cohen, Esq. Bingham McCutchen LLP One Federal Street Boston, MA 02110-1726 BBO# 542811
BBO# 567308	

RECEIVED
JUN 24 2010
SUPERIOR COURT - CIVIL
MICHAEL JOSEPH DONOVAN
CLERK / MAGISTRATE

Origin code and track designation

Place an x in one box only:

[X] 1. F01 Original Complaint
[ ] 2. F02 Removal to Sup.Ct. C.231,s.104 (Before trial) (F)
[ ] 3. F03 Retransfer to Sup.Ct. C.231,s.102C (X)
[ ] 4. F04 District Court Appeal c.231, s. 97 &104 (After trial) (X)
[ ] 5. F05 Reactivated after rescript;relief from judgment/ Order (Mass.R.Civ.P. 60) (X)
[ ] 6. E10 Summary Process Appeal (X)

TYPE OF ACTION AND TRACK DESIGNATION (See reverse side)

CODE NO.	TYPE OF ACTION (specify)	TRACK	IS THIS A JURY CASE?
E99	Misc Other (specify) - X track Assurance of Discontinuance, pursuant to G.L. c. 93A §5		Yes/No No

The following is a full, itemized and detailed statement of the facts on which plaintiff relies to determine money damages. For this form, disregard double or treble damage claims; indicate single damages only.

TORT CLAIMS
(Attach additional sheets as necessary)

A. Documented medical expenses to date:
1. Total hospital expenses $
2. Total Doctor expenses $
3. Total chiropractic expenses $
4. Total physical therapy expenses $
5. Total other expenses (describe) $

Subtotal $

B. Documented lost wages and compensation to date $
C. Documented property damages to date $
D. Reasonably anticipated future medical and hospital expenses $
E. Reasonably anticipated lost wages $
F. Other documented items of damages (describe) $
G. Brief description of plaintiff's injury, including nature and extent of injury (describe)

Total $ N/A

CONTRACT CLAIMS
(Attach additional sheets as necessary)

Provide a detailed description of claim(s):

TOTAL $ N/A

PLEASE IDENTIFY, BY CASE NUMBER, NAME AND COUNTY, ANY RELATED ACTION PENDING IN THE SUPERIOR COURT DEPARTMENT

"I hereby certify that I have complied with the requirements of Rule 5 of the Supreme Judicial Court Uniform Rules on Dispute Resolution (SJC Rule 1:18) requiring that I provide my clients with information about court-connected dispute resolution services and discuss with them the advantages and disadvantages of the various methods."

Signature of Attorney of Record Glen Kaplan Date: June 24, 2010

A.O.S.C. 3-2007

COMMONWEALTH OF MASSACHUSETTS

SUFFOLK, ss.

SUPERIOR COURT
DEPARTMENT OF THE TRIAL COURT

Civil Action No. 10-2538

In re: Morgan Stanley & Co. Incorporated

ASSURANCE OF DISCONTINUANCE
PURSUANT TO M.G.L. CHAPTER 93A, § 5

I. INTRODUCTION

1. Pursuant to the provisions of Massachusetts General Laws Chapter 93A, the Commonwealth of Massachusetts, by and through Martha Coakley, Attorney General, undertook an investigation into the financing, purchase, and securitization of allegedly unfair residential mortgage loans during the period late 2005 through the first half of 2007 by Morgan Stanley & Co. Incorporated (together with its affiliates involved in the mortgage financing and securitization business, "Morgan Stanley"). This is part of a market wide investigation that continues as to entities other than Morgan Stanley.

2. In lieu of litigation and in recognition of Morgan Stanley's assistance and cooperation, the Office of the Attorney General ("AGO") agrees to accept this Assurance of Discontinuance ("AOD") on the terms and conditions contained herein. The AGO and Morgan Stanley voluntarily enter into this AOD.

3. Morgan Stanley enters into this AOD for settlement purposes only and neither admits nor denies the AGO's allegations. This AOD is made without any trial or adjudication of any issue of fact or law.

II. DEFINITIONS

4. For the purposes of this AOD, the following words shall have the following definitions:

a. "CLTV" means combined loan to value ratio, defined as the ratio of the unpaid principal balance of the first lien loan and any second lien loan that may exist to the then most current value of the property;

b. "Best Efforts" means activities performed in good faith to achieve the indicated outcome;

c. "BPO Value" means any property value obtained at Morgan Stanley's request in due diligence in connection with the bulk purchase of mortgage loans from an independent real estate or valuation professional, including but not limited to a broker price opinion;

d. "Fully Indexed Mortgage Payment" means a payment that is calculated as the first month mortgage payment assuming the interest rate is equal to the then-applicable index plus the margin;

e. "Fully Indexed Rate" means the interest rate calculated by adding the index at origination and the margin;

f. "Fully Indexed DTI Ratio" means the ratio of: (i) the borrower's total monthly debt, which includes the borrower's mortgage principal and

interest amounts payable if calculated using the Fully Indexed Rate, to (ii) the borrower's total monthly income;

g. Unless otherwise noted, "LTV" means the loan to value ratio, defined as the ratio of the unpaid principal balance of the loan to the then most current value of the property;

h. "Subprime Loans" for purposes of Section IV of this AOD only, means United States residential mortgage loans purchased in bulk or securitized by Morgan Stanley on or after the date of this AOD and where the loans were originated on or after the date of this AOD, for which the average FICO score for borrowers in the pool is 660 or less at the time of origination; and

i. "UPB" means the unpaid principal balance of the loan.

III. ALLEGATIONS

A. The Relevant Entities

5. New Century Financial Corporation ("New Century") was one of the largest originators of subprime loans in the United States. New Century stopped originating loans and filed for bankruptcy in 2007.

6. Morgan Stanley is one of the nation's largest financial services companies. From 2001 to 2007, Morgan Stanley was a major participant in providing liquidity to originators of "subprime" mortgage loans, which are generally loans to borrowers with weaker credit histories. This subprime business offered Morgan Stanley a variety of profit opportunities, including lending fees and interest on loans, profits from loan purchases, and underwriting fees. While other companies also bought loans, Morgan

Stanley was the largest purchaser of whole loans from New Century, buying tens of thousands of loans. Certain Morgan Stanley investment bankers connected to the subprime mortgage market, in some documents, referred to New Century as a "partner."

B. The Subprime Process

7. Investment banks played a central role in the US subprime lending market by providing mortgage loan originators with both liquidity and access to the capital markets. Because mortgage loan originators generated profits primarily through the sale of their loans, their business was driven by volume. As a result, subprime originators sought ways to borrow money to make more loans for quick resale. A principal source of this capital for subprime lending was warehouse loans provided by entities such as investment banks. Under a warehouse lending arrangement, an investment bank provides an originator with cash through a line of credit. Money borrowed by the originator under the warehouse loan is, in turn, secured by mortgage loans. The investment bank received fees and interest income on the line of credit.

8. The subprime originators aggregated the loans into pools. Typically the originators would either deposit the loans into a trust that would issue securities backed by the loans, or it would sell the loans to an investment bank. The investment bank sought to profit from the first approach by serving as underwriter of securities and taking fees. It sought to profit from the second approach by buying the loans and depositing them into a trust that would issue securities for sale.

9. Investment banks participated in all parts of this process and typically reviewed the loans in order to determine the quality of the lending practices and of the individual loans of their originator partners. Through this process, generally referred to

as "due diligence," investment banks were able, in some instances, to determine whether there were quality problems with an originator's loans and to identify individual problem loans.

C. The Morgan Stanley-New Century Relationship

10. Morgan Stanley's relationship with New Century fell within this general pattern. Morgan Stanley provided funding to New Century for new loan originations through a warehouse facility, acted as underwriter for New Century's securitizations, and purchased New Century's loans. Morgan Stanley's warehouse facilities were lines of credit that provided New Century with access to cash and enabled New Century to quickly convert loans into cash to make additional loans. This enabled New Century to make more loans than it could have using only its own capital. Morgan Stanley, in return, obtained profits and additional business from New Century, including warehouse fees and interest as well as fees for securities underwriting.

11. As part of Morgan Stanley's relationship with New Century, from time to time, Morgan Stanley entered into agreements to purchase New Century's loans months in advance ("forward purchases"). Morgan Stanley sometimes committed to buy loans, meeting certain parameters, so far in advance that the loans that were the subject of the agreement had not yet been originated. As a result, New Century was often originating loans for the purpose of fulfilling its commitment to Morgan Stanley.

12. Of the investment banks providing billions of dollars, in the aggregate, in financing to New Century, Morgan Stanley's warehouse line of credit was the largest; it committed to provide up to $3 billion of funding during 2006 and 2007. Because the warehoused loans were rapidly sold or securitized, the warehouse line was continually re-

used to fund additional subprime loans. These loans were then sold and the process was repeated.

D. Unfair Loans

13. As New Century expanded in 2005 and 2006, it began to make larger and larger numbers of risky loans to borrowers in Massachusetts.

14. New Century, like many other originators, made a large number of adjustable rate mortgages ("ARMs") with initial "teaser" rates that reset to a much higher interest rate. A very large portion of the dollar value of New Century's subprime loans was ARMs with teaser rates.

15. When it made ARM loans, New Century typically qualified borrowers based on payments made at the teaser rate. New Century's business plan assumed that many borrowers would need to refinance their loans prior to reset. The borrower's ability to refinance depended on continuous appreciation in home prices. New Century made no effort to qualify borrowers at the Fully Indexed Rate.

16. Many of the ARM borrowers would not have qualified for loans under New Century's underwriting guidelines had New Century determined the borrowers' ability to pay the loans at the Fully Indexed Rate. In Massachusetts, a mortgage lender must determine whether a borrower has the ability to repay a prospective loan in accordance with its terms. The lender may not rely on the assumed ability of the borrower to obtain refinancing. As a result, such loans were presumptively unfair under Massachusetts law.

E. The Loan Purchase Process Identified Defects

17. As part of Morgan Stanley's process for purchasing and securitizing subprime loans, it engaged in a number of reviews of the quality of the originators' lending practices and loans. These included, *inter alia*, determining whether the subprime loans were originated in accordance with the originators' underwriting guidelines and assessing compliance with applicable laws ("credit and compliance diligence"), and examining property values ("valuation diligence"). These reviews increasingly demonstrated shortcomings in some of New Century's lending practices and problems with a large number of individual subprime loans.

18. One recurring issue identified by Morgan Stanley was New Century's origination of loans that violated the Massachusetts Division of Banks' borrower's best interest standard ("BBI"). Based on the process Morgan Stanley put in place to review and analyze New Century loans, Morgan Stanley generally excluded such loans from its bulk loan purchases. However, Morgan Stanley performed less due diligence on its warehouse line, and New Century used the financing provided through Morgan Stanley's warehouse line to fund certain loans that violated this Massachusetts law. Other instances where the review and diligence process identified defects in the New Century loan pools and loan origination procedures include the following:

a. Morgan Stanley DTI Analysis

19. Morgan Stanley was aware that New Century typically qualified borrowers based on the teaser rate, and that New Century made no effort to qualify borrowers at the Fully Indexed Rate.

20. Morgan Stanley conducted an analysis in 2006, based on a 2005 research report issued by Morgan Stanley's fixed income group that predicted that, in the then prevailing rate environment, upon reset borrowers could, in aggregate, expect an increase in the DTI ratio by a factor of 1.36. On this basis, a 2006 "teaser"-based DTI ratio of 41% converts into a DTI ratio of 56% at reset, and a 2006 teaser-based DTI ratio of 43% converts into a reset DTI ratio of 58%. Morgan Stanley considered borrowers with DTI ratios in excess of 55% to be unable to afford their loans; based on Morgan Stanley's analysis, the borrowers would be compelled to refinance their loans prior to reset. Borrowers unable to obtain refinancing would not be able to repay their loans. If a proxy for the rate at reset had been estimated using a 1.36 reset multiple, of the Massachusetts loans purchased by Morgan Stanley, 41% had fully indexed DTI ratios on this basis greater than 55%, and 29% had fully indexed DTI ratios on this basis over 60%. For Massachusetts loans purchased by Morgan Stanley from New Century, about 45% of the borrowers would not have qualified had the borrower's ability to pay been assessed using Morgan Stanley's reset DTI analysis.

b. Underwriting Guidelines

21. It was Morgan Stanley's stated policy not to purchase and securitize loans found to violate an originator's underwriting guidelines unless the loans had sufficient compensating factors. The primary purpose of credit and compliance diligence was to determine whether loans offered by New Century for purchase by Morgan Stanley were underwritten in accordance with the originator's underwriting guidelines or whether sufficient compensating factors existed, and whether the loans were otherwise in accordance with law.

22. To help perform credit and compliance diligence Morgan Stanley hired Clayton Services, Inc. ("Clayton"), a firm specializing in diligence and unaffiliated with Morgan Stanley or any originator. Clayton was hired as a vendor to review a sample of loans, usually 25% of the New Century loans in a given pool for purchase. Clayton reviewed the loans based on criteria provided by Morgan Stanley and reported results to Morgan Stanley's due diligence team. These criteria principally concerned whether the loans complied with the originator's underwriting guidelines and whether the loans were in compliance with applicable laws. When Clayton's examination uncovered loans that were in violation of guidelines or law in any respect, it graded the loans as "exceptions."

23. As a result of the due diligence process, Morgan Stanley was aware of quality problems with New Century subprime loan pools by late 2005. These problems included sloppy underwriting for many loans and stretching of underwriting guidelines to encompass or approve loans not written in accordance with the guidelines.

24. In late 2005 and early 2006, Morgan Stanley began rejecting greater numbers of New Century loans as a result of these findings. By March 2006, New Century complained about these rejections and pressured Morgan Stanley to increase the percentage of New Century's offered loans it purchased, suggesting that it would begin shifting its business to other buyers.

25. In April 2006, as Morgan Stanley wrestled with the possibility of losing New Century's business, Morgan Stanley's subprime mortgage team discussed a number of possible responses to this situation. As a result of these discussions, one of Morgan Stanley's senior bankers purchased loans that Morgan Stanley's diligence team had initially rejected. According to Morgan Stanley's records, 228 loans were purchased in

this way. Morgan Stanley's diligence teams began to be more responsive to New Century's desire to include additional loans in the purchase pools.

26. In Morgan Stanley's 2006-2007 New Century pools, the large majority of the loans reviewed by Clayton were identified by Clayton as having some type of exception. Most loans had multiple exceptions.

27. In instances where Clayton found material exceptions to the guidelines, Clayton reviewed the loans to determine whether compensating factors existed. Clayton found during the 2006-2007 period that approximately 9% of the loans had sufficient compensating factors to offset such exceptions.

28. During 2006 and 2007, Morgan Stanley waived exceptions on and purchased a large number of the loans found by Clayton to violate guidelines without sufficient compensating factors. In the last three quarters of 2006, Morgan Stanley waived more than half of all material exceptions found by Clayton (there can be more than one material exception on one "exception" loan), and purchased a substantial number of New Century loans found by Clayton to violate guidelines without sufficient compensating factors.

29. In addition, loans with certain exceptions such as high DTI ratios or high LTV or CLTV ratios that were in excess of underwriting guidelines but within a tolerance found acceptable to Morgan Stanley were purchased without a review by Clayton for compensating factors.

30. Portions of the diligence samples were randomly selected. In most pools during 2006 and 2007, substantial percentages of randomly sampled loans were identified by Clayton as exceptions. Overall, about a third of all randomly sampled New Century

loans were found by Clayton to violate guidelines without sufficient compensating factors.

c. CLTV Ratios Greater Than 100%

31. Appraisal quality is significant in evaluating the risk of subprime pools because poor appraisals may overstate the amount of equity a borrower has in the home. Property value is the denominator in the LTV and CLTV ratios, which are key criteria in assessing the risk of loss.

32. Starting in or around October 2005, in the course of reviewing and rejecting for purchase certain loans, Morgan Stanley became aware of problems in the quality of appraisals at New Century. The quality problems persisted through 2006 and 2007.

33. In Morgan Stanley's valuation diligence process, Morgan Stanley engaged independent providers to provide an opinion concerning the value of a sample of the properties securing the New Century loans. Generally, Morgan Stanley employed so-called broker price opinions or "BPOs" to check the value of the properties. In a BPO, a local broker evaluates the property and provides an indicated value and some additional information.

34. It was Morgan Stanley's stated policy not to securitize loans with LTV or CLTV values greater than 100%. However, Morgan Stanley did purchase and securitize numerous loans where the LTV or CLTV based on the BPO-checked value rather than the initial appraisal exceeded that threshold. Overall, 31% of the New Century loans on properties checked via BPOs in the valuation diligence process and securitized by Morgan Stanley in 2006 and 2007 had CLTV ratios based on the BPO-checked values

that were greater than 100%. In Morgan Stanley's securitizations during 2006 and 2007, 60% of the New Century loans with CLTVs based on the BPO-checked values over 100% had ratios greater than 105% on that basis, and about 19% of such loans had ratios greater than 120% on that basis. See the following chart based on information and calculations provided by Morgan Stanley:

Subprime Loans Originated by New Century and Securitized by Morgan Stanley in 2006 and 2007
Calculation of CLTV Ratios Using BPO Values (includes only Loans with BPO Values)

	All Loans		Loans with Original CLTV of 100	
CLTV Range Using BPO Value (%)	Number of Loans	% of Total	Number of Loans	% of Total
Less than or equal to 80	3,535	18.5%	374	4.2%
81 to 95	5,372	28.1%	1,624	18.1%
96 to 99	2,627	13.7%	1,737	19.4%
100	1,582	8.3%	1,416	15.8%
101 to 105	2,378	12.4%	1,733	19.3%
106 to 120	2,490	13.0%	1,603	17.9%
Over 120	1,141	6.0%	488	5.4%

35. Overall, in Morgan Stanley's securitizations with large numbers of New Century loans during this time period, about 6% of the New Century loans had BPO-based CLTVs over 100%. Moreover, many of these loans were part of the randomly sampled portion of loans reviewed in the valuation diligence process, potentially reflecting problems with the LTV and CLTV ratios of other New Century loans.

d. DTI Ratios and Stated Income Loans

36. The DTI ratio is another key factor that is used to assess the ability of the borrowers to pay the loans. The DTI values are provided to investors on the loan "tape," a spreadsheet that contains certain statistics concerning the loans.

37. On the loan tapes provided to investors in Morgan Stanley securitizations of New Century loans, the DTI ratio was typically calculated based on the teaser rate and did not reflect the Fully Indexed Mortgage Payment. Incorporating the Fully Indexed Mortgage Payment in the DTI ratio using Morgan Stanley's reset DTI analysis described above, the average DTI on the New Century tapes would be substantially higher. A large number of the ARM loans would have Fully Indexed DTI Ratios on this basis that were greater than 55%. Based on Morgan Stanley's analysis described above, such borrowers could not afford to repay these loans in accordance with their terms without refinancing. Such loans comprised a significant portion of the overall loan pools.

38. In 2005, Morgan Stanley employees were aware that stated income loans were among the riskiest newly originated subprime loans Morgan Stanley purchased and that such loans were among the most likely subprime loans to become delinquent or default. After rejecting a number of loans with overstated income in one New Century loan pool, one of Morgan Stanley's employees described the stated income method as overused to the point of abuse. Any inaccuracy in stated income would affect the reported DTI ratios, because income is the denominator of the DTI ratio.

39. As early as October 2005, Morgan Stanley's diligence team determined, in reviewing and rejecting loans for purchase, that the stated income on a number of New Century loans was unreasonable. In early 2006, a Morgan Stanley employee commented

that stated income credit was not adequately evaluated by New Century. About 36% of the loans originated by New Century and reviewed by Clayton in the diligence process were stated income loans. On average, the stated income of these borrowers was approximately 42% higher than the income of fully documented borrowers. The average stated income of these borrowers on an annual basis was about $115,000.

40. Assuming that the stated income was closer to or similar to fully documented income, the average actual DTI ratio for stated income borrowers would be much higher than the DTI ratios reported by New Century in the loan tapes (averaging 41% for stated income loans), and a substantial number of these borrowers would have DTI ratios on this basis exceeding 55%.

F. Continued Sales of New Century Loan Products

41. Notwithstanding the problems identified above, Morgan Stanley continued to provide funding for New Century to make subprime loans, and continued to purchase and securitize New Century's subprime mortgages through 2006 and the first half of 2007.

42. In early March 2007, as New Century moved toward bankruptcy, when other banks and investment banks stopped providing financing and/or declared an event of default on New Century's credit lines, and Morgan Stanley itself had declared an event of default on New Century's line, Morgan Stanley wet-funded New Century loans between March 8th and 13th. Wet-funding is a mechanism through which Morgan Stanley effectively provided cash directly to New Century borrowers at the closing table. Morgan Stanley's wet-funding permitted New Century to close millions of dollars in subprime loans in March 2007. Morgan Stanley agreed to provide this funding. At the

same time, New Century posted sufficient collateral to more than compensate Morgan Stanley in the event of a default, and certain of Morgan Stanley's unsecured claims against New Century were converted into secured claims.

G. Harm Stemming from These Practices

43. From fourth quarter 2005 through first quarter 2007, Morgan Stanley aided and financed the business of originating unfair mortgage loans to Massachusetts borrowers in violation of Massachusetts law in that:

--Morgan Stanley knew that many borrowers could not repay the loans according to the terms of the loans without refinancing; and

--Morgan Stanley provided substantial assistance to New Century through its warehouse funding, forward purchasing and other activities that enabled New Century to make these unfair loans to certain Massachusetts borrowers.

These borrowers were harmed by Morgan Stanley's actions.

44. In addition, two Massachusetts state entities, the Massachusetts state pension fund known as the Pension Reserves Investment Trust ("PRIT"), and a fund used for investing municipal cash, the Massachusetts Municipal Depository Trust (the "MMDT"; together with PRIT, the "state entities") purchased certain securities through an intermediary from Morgan Stanley backed by New Century loans, some of which were unfair to borrowers. As a result, funds deriving from the state entities may have been used indirectly to finance or securitize loans that were in violation of Massachusetts law, and the state entities suffered significant losses in their investments.

IV. PROSPECTIVE CONDUCT PROVISIONS

45. To the extent that Morgan Stanley continues or resumes the business of purchasing, securitizing, or providing financing secured by Subprime Loans, Morgan Stanley agrees to adopt the following practices:

(a) Morgan Stanley will only purchase Massachusetts Subprime Loans from an originator if such loans have been underwritten on the basis of the borrower's ability to repay at the Fully Indexed Rate upon origination;

(b) Morgan Stanley will continue to use a process that is reasonably designed to prevent the purchase of loans that violate G. L. c. 183, § 28C (the "BBI statute"), including any related regulations;

(c) Morgan Stanley will not purchase loans that are presumptively unfair under G. L. c. 93A, as that term is defined in Massachusetts law and court decisions, or as it may subsequently be modified;

(d) With respect to warehouse financing, Morgan Stanley will take steps reasonably designed to prevent the extension of credit to originators secured by Subprime Loans to Massachusetts borrowers that violate the BBI statute or are presumptively unfair under c. 93A, as that term is defined in Massachusetts law and court decisions, or as it may subsequently be modified. If, during the bulk purchase due diligence process, Morgan Stanley has identified material systemic or recurring compliance exceptions in an identifiable category or subcategory of an originator's loans, Morgan Stanley shall implement screens reasonably designed to prevent in advance when possible and in any event, shall

identify and remove, the funding of such Subprime Loans to Massachusetts borrowers;

(e) To the extent that Morgan Stanley obtains BPOs on Subprime Loans that are securitized on a principal basis, it will provide to investors in Massachusetts loan level and aggregate data showing the BPO values and recalculate all LTV and CLTV fields using the BPO values;[1]

(f) For adjustable rate Subprime Loans securitized by Morgan Stanley on a principal basis, Morgan Stanley will provide to investors in Massachusetts loan level and aggregate data reporting of the Fully Indexed Mortgage Payment, the originator-provided monthly income of the borrower, and the resulting DTI; and

(g) If, within the next fourteen (14) months after the date of the AOD, the Federal Government adopts no law or regulation requiring asset-backed securities disclosure of waivers or similar action that resulted in loans found by a due diligence vendor to be material exceptions to the underwriting guidelines without compensating factors being placed in the securitized pool, Morgan Stanley will make such disclosures to investors in Massachusetts.

46. Morgan Stanley will implement the practices described in paragraph 45 on a Best Efforts basis and will apply them to the purchase, financing, and securitization of Subprime Loans originated after the date of this AOD. The practices described in

[1] Where Morgan Stanley has obtained more than one BPO within six months of the date of a securitization, Morgan Stanley will provide to investors in Massachusetts loan level and aggregate data showing the latest BPO value and the lowest other BPO value, together with recalculated LTV and CLTV fields using both BPO values.

subparagraphs a-c of paragraph 45 will apply to Subprime Loans to Massachusetts borrowers purchased in bulk for securitization by Morgan Stanley on a principal basis. If Morgan Stanley can re-underwrite or modify such loans to bring them into compliance with subparagraphs a-c of paragraph 45, Morgan Stanley may do so.

47. The prospective conduct provisions set forth in paragraph 45 are intended to supplement federal law and will not require Morgan Stanley to do anything that is inconsistent with federal law. For purposes of this paragraph, an act is inconsistent with federal law when Morgan Stanley cannot comply with both the federal law and the requirements contained in paragraph 45. When an act is inconsistent with federal law, the AGO and Morgan Stanley shall amend this AOD to resolve any such conflict with respect to the pertinent sub-paragraph(s) of paragraph 45, but Morgan Stanley shall continue to follow the practices set forth in all other sub-paragraphs of paragraph 45. This paragraph is not intended to supplant governing case law regarding the application of the Supremacy Clause of the U.S. Constitution.

V. PAYMENTS

48. At a date to be agreed upon with the AGO, but in no circumstance later than twelve (12) business days after the filing of this AOD, Morgan Stanley will, per the direction and determination by the AGO, make the following payments:

a. $18,525,000 to the Commonwealth of Massachusetts, by certified check payable to the Commonwealth of Massachusetts, delivered to Cassandra Roeder, Office of the Attorney General, One Ashburton Place, Boston, MA 02108; and

b. $975,000 to the AGO pursuant to G.L. c. 12, sec. 4A, by check payable to the Office of the Attorney General, delivered to Cassandra Roeder, Office of the Attorney General, One Ashburton Place, Boston, MA 02108, which shall be used for administering the terms of this AOD, monitoring Morgan Stanley's compliance with the terms of this AOD, assisting in the implementation of the relief programs described in this AOD, and supporting the AGO's continuing investigation of the financing, purchase, and securitization of allegedly unfair residential mortgage loans.

49. At a date to be agreed upon with the AGO, but in no circumstances later than fifteen (15) business days after the filing of this AOD, Morgan Stanley shall pay $51,834,449.23 to an independent trust ("**Settlement Fund**") for purposes of making payments to provide principal forgiveness to certain borrowers as set forth in this AOD. The Settlement Fund shall be overseen by an independent trustee ("**Trustee**") to be mutually agreed upon by the AGO and Morgan Stanley within ten (10) days of the date of this AOD. If the AGO and Morgan Stanley are unable to agree on the identity of the Trustee, the AGO shall choose the Trustee in its sole discretion. The Trustee shall deposit the Settlement Fund into interest bearing accounts such that, to the extent possible: (i) all of the funds are fully guaranteed by the Federal Deposit Insurance Corporation, ("FDIC") or The United States Department of the Treasury; and (ii) the interest rates are at least equal to the highest interest rate available from among the five largest banks in the City of Boston for a fully liquid deposit account holding such a sum of money. The Trustee will make investments of and disbursements from the Settlement

Fund only with the consent of the AGO and may vary from the investment criteria of this paragraph only with the consent of the AGO.

50. At a date to be agreed upon with the AGO, but in no circumstances later than fifteen (15) business days after the filing of this AOD, Morgan Stanley shall also pay $6,000,000 to another independent trust ("**Foreclosure Relief Fund**") also overseen by the Trustee, for purposes of making payments to certain additional borrowers as set forth in this AOD. The Trustee shall deposit the Foreclosure Relief Fund into interest bearing accounts such that, to the extent possible: (i) all of the funds are fully guaranteed by the FDIC or The United States Department of the Treasury; and (ii) the interest rates are at least equal to the highest interest rate available from among the five largest banks in the City of Boston for a fully liquid deposit account holding such a sum of money. The Trustee will make investments of and disbursements from the Foreclosure Relief Fund only with the consent of the AGO and may vary from the investment criteria of this paragraph only with the consent of the AGO.

51. At a date to be agreed upon with the AGO, but in no circumstances later than fifteen (15) days after the filing of this AOD, Morgan Stanley shall pay $23,376, 744.25 to another independent trust ("**Completion Fund**"), also overseen by the Trustee, for purposes of making certain payments as determined and directed by the Attorney General to certain state entities. The Trustee shall deposit the Completion Fund into interest bearing accounts such that, to the extent possible: (i) all of the funds are fully guaranteed by the FDIC or The United States Department of the Treasury; and (ii) the interest rates are at least equal to the highest interest rate available from among the five largest banks in the City of Boston for a fully liquid deposit account holding such a sum

of money. The Trustee will make investments of and disbursements from the Completion Fund only with the consent of the AGO and may vary from the investment criteria of this paragraph only with the consent of the AGO.

52. Morgan Stanley will pay the Trustee's commercially reasonable fees and costs associated with its duties under this AOD separate and apart from all other payments required under this AOD.

VI. INFORMATION DEVELOPMENT FOR THE LOAN PRINCIPAL FORGIVENESS PROGRAM

53. No later than five (5) days after the filing of this AOD, Morgan Stanley shall provide to the AGO, pursuant to G.L. c. 93A, sec. 6, a list of borrowers who obtained loans meeting the criteria set forth in **Attachment A.** This list shall also include such information, to the extent Morgan Stanley has the information in its control or can obtain the information without undue burden, regarding the borrowers, their loans, the holder of the loans, the servicer of the loans, and the status of the loans, as the AGO shall specify ("Initial Borrower List"). The list shall also include, for each borrower on the list, the amount of principal forgiveness calculated on the borrower's loan(s) in accordance with the methodology set forth in **Attachment B.** Within sixty (60) days of receiving the Initial Borrower List, the AGO shall inform Morgan Stanley if the AGO disagrees with the content or calculations of the Initial Borrower List, and shall work in good faith with Morgan Stanley to resolve such differences. If such a resolution cannot be reached within two weeks, the AGO may make such corrections or adjustments to the Initial Borrower List as it deems appropriate in its sole discretion. The finalized version of this list shall be referred to in this AOD as the "Final Borrower List."

54. Within five (5) days of the initial delivery of the Initial Borrower List to the AGO, the AGO may direct Morgan Stanley to send a mutually agreeable letter to each holder and/or servicer of a loan on the Initial Borrower List. Morgan Stanley shall send this letter within three (3) days of the AGO's direction. This letter shall seek to determine whether the holder and/or servicer will accept payments for principal forgiveness as part of the implementation of this AOD and whether the holder and/or servicer agrees to apply principal forgiveness amounts received from the Trustee to the relevant borrower's loan as a principal forgiveness ("principal forgiveness program"). The letter shall also specify that the holder and/or servicer must agree to these terms in writing within ninety (90) days of the initial mailing of the letter in order to receive the funds. The letter shall also specify that the written agreement must specify to whom funds transferred by the Trustee in accordance with this AOD shall be directed. Morgan Stanley shall undertake reasonable steps to inform the holder and/or servicer regarding the principal forgiveness program, and shall in good faith attempt to secure the holder's and/or servicer's participation as early as practicable within the ninety (90) day timeframe. On a rolling basis as received, Morgan Stanley shall inform the AGO of all holders and/or servicers that have agreed to participate in the principal forgiveness program, and shall provide the AGO with copies of the written documentation of this agreement.

55. Within one hundred (100) days of the initial delivery of the Initial Borrower List to the AGO, the AGO may direct Morgan Stanley to send a mutually agreeable letter to each person who is both (1) a borrower on the Final Borrower List ("Qualified Borrower") and (2) a borrower whose loan holder and/or servicer has agreed

to participate in the principal forgiveness program ("Qualified Borrower With Participating Holder", or "QBWPH"). This letter ("QBWPH Letter") shall inform the QBWPH of this AOD and the loan principal forgiveness available ("loan principal forgiveness program") to the QBWPH under this AOD. The QBWPH Letter shall include a web address and dedicated telephone number that QBWPHs may use to obtain information regarding the AOD, shall note that the AGO is seeking a Private Letter Ruling from the Internal Revenue Service regarding the tax implications of the loan principal forgiveness program, and shall suggest that the QBWPH consider obtaining tax advice regarding the effect of participating in the loan principal forgiveness program. The QBWPH Letter shall also include a postage paid return envelope, and a form ("Opt-in Form") that the QBWPH may use to agree to participate in the loan principal forgiveness program available under the AOD. If Morgan Stanley and the AGO cannot agree upon the content and format of the Opt-in Form within 100 days of the initial delivery of the Borrower List to the AGO, the AGO may design the content (consistent with this AOD) and form of the Opt-in Form.

56. Morgan Stanley will send the QBWPH Letter and Opt-In Form through the U.S. Postal Service ("USPS") with delivery confirmation. If any such mailing is returned to Morgan Stanley by the USPS with a forwarding address within thirty (30) days of Morgan Stanley's mailing, Morgan Stanley will re-mail the item to said forwarding address within ten (10) days of the date the QBWPH Letter is returned to Morgan Stanley by the USPS.

57. For each Opt-in Form executed and returned to Morgan Stanley within one hundred and eighty (180) days of the initial mailing, Morgan Stanley shall make a

copy for its records of the executed Opt-in Form and then provide the executed Opt-in Form to the Trustee within ten (10) days of receipt by Morgan Stanley. The Trustee shall maintain these executed Opt-in Forms in a secure fashion as directed by the AGO. In addition, the Trustee shall keep in the same manner any additional executed Opt-in Forms provided to the Trustee by the AGO within a period of time after the initial mailing as set by the AGO.

58. It is the intention of Morgan Stanley and the AGO that payments by the Trustee from the Settlement Fund comprise and constitute debt forgiveness within the meaning of the Mortgage Forgiveness Debt Relief Act of 2007 (as extended by the Emergency Economic Stabilization Act of 2008). Morgan Stanley shall assist the AGO in seeking additional guidance from the Internal Revenue Service regarding the loan principal forgiveness program of this AOD. Morgan Stanley shall provide the AGO with information relating to the loans and/or the principal forgiveness program implementation reasonably available to Morgan Stanley upon request.

VII. LOAN PRINCIPAL FORGIVENESS PAYMENTS

59. For each QBWPH who has returned an executed Opt-In Form in accordance with the previous paragraphs, the Trustee shall send a check as directed by the holder and/or servicer pursuant to the written agreement referenced in paragraph 54, along with specific information regarding the loan to which the principal forgiveness should be applied. This check shall be in the amount identified on the Final Borrower List as the principal forgiveness for the relevant QBWPH. If a holder and/or servicer fails to apply the check as principal forgiveness within a reasonable time period to be determined by the AGO, the AGO may direct that the Trustee permanently stop payment

on the check. After such instruction to stop payment, the QBWPH shall thereafter no longer be considered a QBWPH, but shall still be considered a Qualified Borrower for purposes of this AOD.

60. Morgan Stanley intends to and shall cause a Form 1099-C to be issued to each borrower reflecting the cancellation of debt associated with this principal forgiveness program. Together with the Form 1099-C, Morgan Stanley will send a letter advising that a Form 982 must be filed to claim any exclusion from gross income for the amount of principal forgiveness.

61. For any Qualified Borrower who is not a QBWPH, the AGO may direct Morgan Stanley to send a mutually agreeable letter ("Non-QBWPH Letter") to the Qualified Borrower that explains the AOD and offers the Qualified Borrower an opportunity to receive a payment for the purpose of principal forgiveness. The Non-QBWPH letter shall include a web address and dedicated telephone number that Qualified Borrowers may use to obtain information regarding the AOD, shall note that there may be tax consequences for a Qualified Borrower accepting such monies, shall note that the borrower should seek tax advice, shall provide a form ("Payment Authorization Form") which the Qualified Borrower may execute and return to Morgan Stanley if the Qualified Borrower wishes to receive such a payment, and shall explain the time frame for accepting the payment. Should Morgan Stanley and the AGO be unable to agree on the content of the Payment Authorization Form, the AGO may design the form in its sole discretion.

62. Morgan Stanley will send the Non-QBWPH letter and Payment Authorization Form through the USPS with delivery confirmation. If any such mailing is

returned to Morgan Stanley by the USPS with a forwarding address within thirty (30) days of Morgan Stanley's mailing, Morgan Stanley will re-mail the item to said forwarding address within ten (10) days of the date the Non-QBWPH letter is returned to Morgan Stanley by the USPS.

63. Morgan Stanley shall forward copies to the Trustee of all Payment Authorization Forms received within one hundred and twenty (120) days of the initial mailing of the unexecuted Payment Authorization Forms ("Delivery Time Frame"). Morgan Stanley shall provide the copies of the executed Payment Authorization Forms to the Trustee within ten (10) days of receipt by Morgan Stanley. For each Qualified Borrower for whom the Trustee receives a Payment Authorization Form from Morgan Stanley within the Delivery Time Frame, or from the AGO within a time period set by the AGO, the Trustee shall send a check to the Qualified Borrower for the amount listed on the Final Borrower List. If any check sent to a Qualified Borrower under this paragraph remains uncashed sixty (60) days after the initial mailing, the Trustee shall take reasonable efforts to contact the Qualified Borrower regarding the status of the checks, and inform the Qualified Borrower that he or she must cash the check within one hundred and twenty (120) days of the date the check was issued ("Check Issuance Date"), or payment will be permanently stopped on the check and the Qualified Borrower will no longer be eligible to receive the monies. The AGO may extend this deadline or alter this procedure as it deems appropriate in its sole discretion.

64. On July 1, 2011, the Trustee shall permanently stop payment on all outstanding uncashed checks and transfer any remaining monies from the Settlement Fund into the Foreclosure Relief Fund.

VIII. INFORMATION DEVELOPMENT FOR FORECLOSURE RELIEF

65. No later than ten (10) days after the filing of this AOD, the AGO shall provide a list of initial criteria for certain loans to Massachusetts residents that Morgan Stanley has securitized ("Foreclosure Relief Criteria"). Within thirty (30) days of receiving the Foreclosure Relief Criteria, Morgan Stanley shall provide to the AGO, pursuant to G.L. c. 93A, sec. 6, a list including borrowers who obtained loans meeting the Foreclosure Relief Criteria. This list ("Initial Foreclosure Relief List") shall also include such information, to the extent Morgan Stanley has the information in its control or can obtain the information without undue burden, regarding the borrowers, their loans, the servicer, and the history and status of the loans, as the AGO shall specify. Within fifty (50) days of receiving the Initial Foreclosure Relief List, the AGO shall provide the Trustee with criteria to be used in calculating payment amounts to be ascribed to each borrower, and the Trustee shall within ten (10) days: (i) calculate for each borrower on the Initial Foreclosure Relief List ("Foreclosure Relief Borrower") the maximum amount to be paid to the borrower ("Notional Foreclosure Relief Payment"), as well as the pro rata portion of each Notional Foreclosure Relief Payment that can be paid from the outstanding balance of the Foreclosure Relief Fund ("Initial Foreclosure Relief Payment"), (ii) add the amounts referenced in item (i) to the Initial Foreclosure Relief List, and (iii) provide the updated Initial Foreclosure Relief List to the AGO. After the Trustee has so updated the Initial Foreclosure Relief List, the AGO shall inform the Trustee if the AGO disagrees with any content of or calculations on the Initial Foreclosure Relief List, and shall work in good faith with the Trustee to resolve such

differences. If such a resolution cannot be reached within two weeks, the AGO may make such corrections or adjustments to the Initial Foreclosure Relief List as it deems appropriate in its sole discretion. If any changes occur to the Initial Foreclosure Relief List as a result of this process, the pro rata Initial Foreclosure Relief Payments shall be recalculated based on the updated list of Notional Foreclosure Relief Payments. The finalized version of this list shall be referred to in this AOD as the "Final Foreclosure Relief List."

66. Within one hundred and twenty (120) days of the initial delivery of the Initial Foreclosure Relief List to the AGO, the AGO may direct Morgan Stanley to send a mutually agreeable letter ("Foreclosure Relief Letter") to each borrower on the Final Foreclosure Relief List ("Foreclosure Relief Borrower"), informing the Foreclosure Relief Borrower of this AOD and the potential relief available ("Foreclosure Relief Program") to the Foreclosure Relief Borrower under this AOD. The Foreclosure Relief Letter shall include a web address and dedicated telephone number that Foreclosure Relief Borrowers may use to gather information regarding the AOD. The Foreclosure Relief Letter shall note that there may be tax consequences for a borrower accepting such monies and shall note that the borrower should seek individual tax advice. The Foreclosure Relief Letter shall also include a postage paid return envelope, and a form ("Foreclosure Opt-in Form", or "FOF") that the Foreclosure Relief Borrower may use to agree to participate in the Foreclosure Relief Program available under the AOD. Morgan Stanley shall undertake commercially reasonable efforts to obtain current addresses for the Foreclosure Relief Borrowers. If Morgan Stanley and the AGO cannot agree upon the content and format of the FOF within one hundred and twenty (120) days of the initial

delivery of the Initial Foreclosure Relief List to the AGO, the AGO may design the content (consistent with this AOD) and form of the FOF.

67. Within five (5) days of notice from the AGO, Morgan Stanley will send the Foreclosure Relief Letter and FOF through the USPS with delivery confirmation. If any such mailing is returned to Morgan Stanley by the USPS with a forwarding address within thirty (30) days of Morgan Stanley's mailing of the Foreclosure Relief Letter and FOF, Morgan Stanley will re-mail the Foreclosure Relief Letter and FOF to said forwarding address within ten (10) days of the date the Foreclosure Relief Letter is returned to Morgan Stanley by the USPS.

68. For each FOF executed and returned to Morgan Stanley within one hundred and eighty (180) days of the initial mailing, Morgan Stanley shall make a copy of the executed FOF for its records and provide the original to the Trustee within ten (10) days of receipt by Morgan Stanley. The Trustee shall maintain these executed FOFs in accordance with instructions from the AGO. In addition, the Trustee shall similarly maintain any additional executed FOFs provided to the Trustee by the AGO within a period of time after the initial mailing as set by the AGO.

IX. FORECLOSURE RELIEF PROGRAM PAYMENTS

69. Within ten (10) days of receiving an executed FOF from Morgan Stanley or the AGO, the Trustee shall send a check to the relevant Foreclosure Relief Borrower for the Foreclosure Relief Borrower's Initial Foreclosure Relief Payment, along with an explanatory letter as directed by the AGO.

70. If any check sent to a Foreclosure Relief Borrower remains uncashed within sixty (60) days of its initial mailing, the Trustee shall take reasonable efforts to

contact the Foreclosure Relief Borrower regarding the status of the check as directed by the AGO, and inform the Foreclosure Relief Borrower that he or she must cash the check within one hundred and twenty (120) days of the Check Issuance Date, or the Trustee will permanently stop payment on the check and the Qualified Borrower will no longer be eligible for the Foreclosure Relief Program. The AGO may, in its discretion, extend this deadline.

71. On November 1, 2011, or such other date as the AGO shall determine, the Trustee shall calculate the difference between the Notional Foreclosure Relief Payment for each Foreclosure Relief Borrower and the Initial Foreclosure Relief Payment for that borrower ("Secondary Foreclosure Relief Payment"), and provide, on a pro rata basis, to the extent funds are available in the Foreclosure Relief Fund, a check for this amount to the Foreclosure Relief Borrower, along with an explanatory letter as directed by the AGO. The Trustee shall undertake reasonable efforts as directed by the AGO to locate Foreclosure Relief Borrowers and provide them with these checks. To the extent a check is uncashed sixty (60) days after it is mailed to the Foreclosure Relief Borrower, the Trustee shall place a permanent stop payment order on the check. On February 1, 2012, any remaining monies in the Foreclosure Relief Fund shall be transferred by the Trustee to the AGO pursuant to G.L. c. 12 sec. 4A for the purposes of administering the terms of this AOD, monitoring Morgan Stanley's compliance with the terms of this AOD, assisting in the implementation of the relief programs described in this AOD, and for investigation and mediation of related financial services issues.

72. If Morgan Stanley receives any letters or forms in relation to this AOD from any borrower who received an offer under this AOD, Morgan Stanley shall forward

such forms to the AGO even if such letters or forms are received outside of the time frames contemplated by this AOD.

X. FORECLOSURE RELATED SERVICES

73. Separate and apart from any other payment specified under this AOD, Morgan Stanley intends to make a donation of $2,000,000 to a not-for-profit entity or entities who provide counsel to Massachusetts borrowers, to assist consumers with issues stemming from foreclosure of subprime loans and related issues. As part of this AOD, Morgan Stanley shall:

a. make the donation of $2,000,000 within forty-five (45) days of the filing of this AOD;

b. consult with the AGO regarding the allocation of such monies, so that the combination of recipient organizations will provide coverage for consumers located in all sections of the Commonwealth in relative proportion to the number of foreclosures suffered in those sections of the Commonwealth, and provide such donation monies only to not-for-profit groups to which the AGO does not object;

c. condition the donation on the requirement that the not-for-profit groups give priority to borrowers referred to them by the AGO for assistance;

d. condition the donation on the requirement that the not-for-profit groups make available to qualified foreclosed borrowers the types of assistance as the AGO shall recommend; and

e. condition the donation on the requirement that the not-for-profit groups provide such information and reports to the AGO as the AGO requires regarding the not-for-profit groups' uses of the donation.

XI. COMPLETION FUND PAYMENTS

74. As directed and determined by the AGO, the Trustee shall within thirty (30) business days of the entry of this AOD issue the following payments from the Completion Fund:

a. $23,193,157.94 to PRIT or its designee, by certified check payable to PRIT, delivered by a method and to a PRIT representative identified by the AGO;

b. $183,586.31, to the MMDT or its designee, by certified check payable to the MMDT, delivered by a method and to an MMDT representative identified by the AGO.

75. On July 1, 2011, any remaining monies in the Completion Fund shall be transferred by the Trustee to the Foreclosure Relief Fund.

XII. COOPERATION AND RECORD KEEPING

76. Morgan Stanley shall fully cooperate with the AGO in its implementation of this AOD.

77. Morgan Stanley will comply with all reasonable requests by the AGO for documents or information related to the subject matter of the AOD as set forth in Sections I and III.

78. Morgan Stanley will create and maintain, for a period of at least five years from the entry date of this AOD, records sufficient to demonstrate Morgan Stanley's

compliance with its obligations under this AOD and will provide such records to the AGO upon request.

XIII. MISCELLANEOUS PROVISIONS

79. The AGO will not proceed with or institute a civil action or proceeding based upon M.G.L. c. 93A or any other statute or regulation, or common law, against Morgan Stanley, or any of Morgan Stanley's present or former employees (relating solely to their conduct during their employment by Morgan Stanley), agents, subsidiaries and subdivisions, successors, assigns, or any purchasers of all or substantially all of its assets, including but not limited to any action or proceeding seeking restitution, injunctive relief, fines, penalties, attorneys' fees or costs, for Morgan Stanley's actions prior to the entry date of this AOD relating to Morgan Stanley's alleged actions as set forth in Sections I and III of this AOD.

80. The AOD constitutes the entire agreement between the AGO and Morgan Stanley and supersedes any prior communication, understanding or agreements, whether written or oral, concerning the subject matter of the AOD. This AOD can be modified or supplemented only by a written document signed by both parties.

81. The AOD will be binding upon Morgan Stanley, its agents, subsidiaries and subdivisions, as well as its successors, assigns, and/or purchasers of all or substantially all of its assets.

82. Morgan Stanley represents and warrants that it has the full legal power, capacity, and authority to bind the parties for whom it is acting, including its affiliates involved in the mortgage financing and securitization business.

83. The AOD and its provisions will be effective on the date that it is filed in the Superior Court for Suffolk County.

84. All notices required under the AOD will be provided as follows:

To the AGO:

Cassandra Roeder
Office of the Massachusetts Attorney General
Public Protection & Advocacy Bureau
Insurance & Financial Services Division
One Ashburton Place 18th Floor
Boston, MA 02108
(617) 963-2812

To Morgan Stanley:

Eric Grossman
General Counsel of the Americas
Morgan Stanley
1221 Avenue of the Americas
New York, NY 10020

85. By signing below, Morgan Stanley & Co. Incorporated, on behalf of itself and its affiliates involved in the mortgage financing and securitization business, agrees to comply with all of the terms of this AOD. Any violation of this AOD may be pursued in a civil action or proceeding under M.G.L. c. 93A hereafter commenced by the AGO.

Morgan Stanley & Co. Incorporated

By: Eric J. Grossman

Title: General Counsel of the Americas

Date: June 21, 2010

Office of the Attorney General

By: Glen Kaplan

Title: Assistant Attorney General

Date: 6/24/10

ATTACHMENT A

CRITERIA FOR DETERMINING INITIAL BORROWER LIST

A. Borrowers of residential mortgage loans originated by New Century, secured by Massachusetts owner-occupied properties, purchased by Morgan Stanley from New Century, between November 3, 2005 and December 31, 2007, and securitized by Morgan Stanley between January 1, 2006 and December 31, 2007 where the loan neither paid off nor was written off as a loss prior to Loan Performance Reports of March 2010.

B. Borrowers of residential mortgage loans, secured by Massachusetts owner-occupied properties, where the loans were originated by lenders other than New Century or purchased from an entity other than New Century, that Morgan Stanley purchased and securitized between January 1, 2006 and December 31, 2007, where the loan was presumptively unfair under Massachusetts law, including existing Massachusetts Superior Court decisions, and where the loan neither paid off nor was written off as a loss prior to Loan Performance Reports of March 2010.

C. Borrowers of residential mortgage loans that either were originated by New Century or presumptively unfair under Massachusetts law, including existing Massachusetts Superior Court decisions, where the loan is secured by Massachusetts owner-occupied properties and the loan is owned by Morgan Stanley as of June 1, 2010.

ATTACHMENT B

PRINCIPAL FORGIVENESS CALCULATIONS

The principal forgiveness calculations shall be as of Loan Performance Reports of March 2010 and the amounts shall be as follows:

(a) for First Lien Performing Loans the amount shall be the lower of:
    (i) 25% of the UPB or
    (ii) so much of the UPB to bring the LTV to 96.5%;
(b) for First Lien Non-Performing Loans, the amount shall be 35% of the UPB;
(c) for Second Lien Performing Loans, the amount shall be 50% of the UPB; and
(d) for the Second Lien Non-Performing loans the amount shall be the entire UPB.

If the first and second lien loans were both purchased by Morgan Stanley (matched by property address and borrower name), and the first lien loan has a LTV before the principal forgiveness of greater than 96.5 percent, the entire second lien UPB shall be forgiven. If the first lien loan has a LTV of less than 96.5 percent before the principal forgiveness, the second lien loan shall be forgiven in accordance with sections (c) or (d) above as applicable.

The term "Performing" shall mean less than sixty days delinquent as of Loan Performance reports of March 2010 under the Mortgage Bankers' Association delinquency calculation methodology. The term "Non-Performing" shall mean greater than or equal to sixty days delinquent under the Mortgage Bankers' Association delinquency calculation methodology.

For the purposes of this attachment, the value used for the LTV calculation will be determined by applying the changes in the loan's applicable Case-Shiller Housing Price Index through first quarter 2010 to the value of the loan at the time it was securitized (or the time of purchase if the loan falls within category C of Attachment A) .