Oral Argument Requested

11-2762-cv

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

NECA-IBEW HEALTH & WELFARE FUND, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,

Plaintiff-Appellant,

—against—

GOLDMAN, SACHS & CO., GOLDMAN SACHS MORTGAGE CO., DANIEL L. SPARKS, MICHELLE GILL, GS MORTGAGE SECURITIES CORP., KEVIN GASVODA,

Defendants-Appellees,

(*CAPTION CONTINUED ON FOLLOWING PAGE*)

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR DEFENDANTS-APPELLEES

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GS MORTGAGE SECURITIES CORP., GSAA HOME EQUITY TRUST 2007-3, GSAA HOME EQUITY TRUST 2007-4, GSAMP TRUST 2007-HE2, GSAMP TRUST 2007-FM2, GSAA HOME EQUITY TRUST 2007-5, GSAA HOME EQUITY TRUST 2007-6, GSAA HOME EQUITY TRUST 2007-7, GSAA HOME EQUITY TRUST 2007-8, GSR MORTGAGE LOAN TRUST 2007-4F, GSAMP TRUST 2007-HSBC1, GSAMP TRUST 2007-HEI, STARM MORTGAGE LOAN TRUST 2007-4, GSAA HOME EQUITY TRUST 2007-10, GSR MORTGAGE LOAN TRUST 2007-5F, GSR MORTGAGE LOAN TRUST 2007-3F, GSR MORTGAGE LOAN TRUST 2007-OA2, SUNTRUST ROBINSON HUMPHREY, INC.,

Defendants,

THE POLICE AND FIRE RETIREMENT SYSTEM OF THE CITY OF DETROIT,

Intervenor.

CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1, Defendants-Appellees Goldman, Sachs & Co., Goldman Sachs Mortgage Company and GS Mortgage Securities Corp. state that they are directly or indirectly wholly-owned subsidiaries of The Goldman Sachs Group, Inc. ("GS Group"), which is a corporation organized under the laws of Delaware and whose shares are publicly traded on the New York Stock Exchange. GS Group has no parent corporation, and to the best of GS Group's knowledge, no publicly held company owns 10% or more of the common stock of GS Group.

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Certificates	GSAA Home Equity Trust 2007-5 Class 1AV1 and GSAA Home Equity Trust 2007-10 Class A2A
Complaint or TAC	Third Amended Complaint in *NECA-IBEW Health & Welfare Fund* v. *Goldman, Sachs & Co.*, No. 08 Civ. 10783 (MGC) (S.D.N.Y.), dated March 31, 2010
CD	Civil Docket in *NECA-IBEW Health & Welfare Fund* v. *Goldman, Sachs & Co.*, No. 08 Civ. 10783 (MGC) (S.D.N.Y.)
JA	Joint Appendix
Goldman Sachs	Goldman, Sachs & Co.
GSAA 2007-5	GSAA Home Equity Trust 2007-5
GSAA 2007-10	GSAA Home Equity Trust 2007-10
GSMC	Goldman Sachs Mortgage Co.
GS Mortgage	GS Mortgage Securities Corp.
MBS	Mortgage-backed security
NECA	Plaintiff-Appellant NECA-IBEW Health & Welfare Fund
NECA Br.	Plaintiff-Appellant's Opening Brief
SA	Special Appendix
SEC	United States Securities and Exchange Commission
Second Amended Complaint	Second Amended Complaint in *NECA-IBEW Health & Welfare Fund* v. *Goldman, Sachs & Co.*, No. 08 Civ. 10783 (MGC) (S.D.N.Y.), dated November 9, 2009
Section 11	Section 11 of the Securities Act of 1933

Section 12	Section 12 of the Securities Act of 1933
Securities Act	Securities Act of 1933

JURISDICTIONAL STATEMENT

This Court has jurisdiction pursuant to 28 U.S.C. § 1291.

STATEMENT OF THE ISSUES PRESENTED

1. Did the district court correctly conclude that NECA lacks standing to sue under Sections 11(a) and 12(a)(2) of the Securities Act of 1933 (a) with respect to 15 offerings of mortgage-backed securities from which NECA did not purchase any certificates, and (b) with respect to tranches of mortgage-backed securities other than those that NECA actually purchased?

2. Did the district court correctly hold that NECA failed adequately to allege a cognizable economic loss under Sections 11(a) and 12(a)(2) as to MBS certificates it purchased and held at the time of suit because NECA did not allege any facts to support its conclusory assertion that the value of the certificates had decreased?

3. Should the Court affirm the district court's dismissal of NECA's claims on the alternative grounds that:

   a. all claims are barred by the statute of limitations because NECA was on inquiry, if not actual, notice of the conduct underlying its claims more than one year before bringing this action, as evidenced by NECA's own

allegations in this action and in its earlier complaint in a similar MBS action; or

b. the Complaint failed to state any claim because the Complaint (i) did not allege that Defendants had a duty to disclose any of the allegedly omitted information; (ii) did not plead any actionable misrepresentation in the relevant offering documents, which provided investors with details regarding the underlying loans and disclosed the inherent risks of those loans; or (iii) did not allege the materiality of any alleged misrepresentation?

4. Did the district court act within its discretion when it denied NECA's untimely request to amend its Complaint for a fourth time?

STATEMENT OF THE CASE

NECA-IBEW Health & Welfare Fund appeals from the dismissal of its Third Amended Complaint in a putative securities class action involving mortgage pass-through certificates. In a series of rulings, the United States District Court for the Southern District of New York (Cedarbaum, J.) scaled back the claims on well-established standing grounds, and ruled that NECA failed—despite four opportunities—to state a claim under Sections 11, 12(a)(2) and 15 of the Securities Act with respect to MBS certificates that it purchased.

NECA admittedly purchased only two certificates—GSAA Home Equity Trust 2007-5 Class 1AV1 and GSAA Home Equity Trust 2007-10 Class A2A—but its initial, first amended and second amended complaints purported to assert claims on behalf of a putative class of purchasers of *all* certificates in more than *seventeen* separate MBS offerings. The district court followed numerous other recent decisions when it dismissed NECA's claims with respect to the fifteen MBS offerings from which NECA did not purchase any certificates on the ground that NECA did not have Article III or statutory standing to bring those claims. The district court further held that NECA could bring claims only with respect to the specific tranches, or Certificates, it did purchase. In the same ruling, the district court found that NECA failed to allege a cognizable loss for the Certificates it purchased and held at the time, but granted NECA an opportunity to amend its complaint with respect to those two offerings.

NECA's Third Amended Complaint fared no better. The district court dismissed NECA's Section 11 claims for failure to allege a cognizable loss. The district court observed that NECA had not suffered any actual damages because it still held the Certificates and continued to receive its promised monthly principal and interest payments. The district court also found that NECA's conclusory assertion that the Certificates had diminished in value was insufficient to plead a cognizable loss in the unique context of MBS transactions.

After the district court dismissed the Section 11 claims and denied its motion to certify that dismissal as a final judgment or for interlocutory appeal, NECA claimed it had sold one of its Certificates, thus precluding its Section 12(a)(2) rescission remedy, and sought (several months after the "sale") to amend its Complaint to allege that it had sold the Certificates at a loss. The district court denied as untimely NECA's motion for leave to amend, and entered final judgment at NECA's request. This appeal followed.

STATEMENT OF FACTS

A. The Parties and Claims

NECA purports to represent a putative class of investors that purchased mortgage pass-through certificates issued by seventeen trusts in seventeen different offerings pursuant to seventeen separate sets of offering documents. (NECA Br. 5.) With respect to each of the seventeen offerings, NECA purports to assert claims (i) under Section 11 against all Defendants (NECA Br. 5; JA-236–38 ¶¶ 95-106); (ii) under Section 12(a)(2) against Goldman Sachs, as underwriter of the offerings (NECA Br. 5; JA-238–39 ¶¶ 107-11); and (iii) under Section 15 against Goldman Sachs, GSMC, GS Mortgage and three current or former officers of GS Mortgage as "control persons" (NECA Br. 5; JA-239–40 ¶¶ 112-17).

Defendant GSMC was the sponsor of all seventeen offerings, but originated none of the underlying mortgage loans. (NECA Br. 22; JA-207 ¶ 11.) Instead, in connection with each offering, GSMC had purchased the loans at arm's length from third-party originators, and then pooled and conveyed those loans to the depositor, GS Mortgage. (NECA Br. 22; JA-207 ¶ 12.) GS Mortgage then conveyed the loan pool to the respective trust. (NECA Br. 23; JA-207 ¶ 12.) In exchange for the loan pool, the trust transferred certificates to GS Mortgage, which then sold those certificates to investors through an underwriter, Goldman Sachs. (NECA Br. 23; JA-207 ¶ 12.) Each offering consisted of different certificates (also called "tranches") with different characteristics, including the interest rate paid; the degree of "subordination" that protects against risk of default; the expected time to maturity; and, in some cases, entirely different underlying loans. (*See infra* I.B.2.)

B. The Certificates NECA Purchased

NECA alleged that it purchased the Class 1AV1 Certificate of GSAA 2007-5 and the Class A2A Certificate of GSAA 2007-10, but did not allege that it purchased (a) any of the other tranches of certificates from those two offerings or (b) any certificates at all from any of the other fifteen challenged offerings. (NECA Br. 22; JA-206 ¶ 9.)

The Certificates were offered and issued pursuant to (i) a registration statement filed with the SEC on January 31, 2007; (ii) a base prospectus dated

February 13, 2007; (iii) separate prospectus supplements dated April 27, 2007 (for GSAA 2007-5) and October 29, 2007 (for GSAA 2007-10); and (iv) separate free writing prospectuses filed contemporaneously with the respective prospectus supplements. (*See* JA-204 ¶ 1; CD99 Exs. A, B.) Neither the registration statement nor the base prospectus contains any information about the mortgages underlying the certificates in a particular offering; that information is provided only in the prospectus supplement and accompanying free writing prospectus for each offering. (CD67 4:16-23.)

The offering documents disclosed that the certificates are backed by pools of alternative mortgage loans owned by the issuing trusts. (JA-204 ¶ 2, JA-210 ¶ 26.) The certificates entitle their holders to a share of the interest and principal payments made by borrowers on an underlying pool of mortgage loans. (JA-210 ¶ 26.) As borrowers make their monthly mortgage payments, the trusts "pass through" a portion of these payments to certificateholders based on the class of their certificates. (JA-210 ¶ 26.) NECA does not allege that it failed to receive any payment to which it is entitled. (CD99 Ex. D at 19:22-25, 21:13-16.)

Collectively, the offering documents for the Certificates that NECA purchased comprise hundreds of pages of factual disclosures regarding the trusts' structures, the certificates issued and the inherently risky nature and credit quality of the loans underlying the certificates. (*See* CD99 Exs. A, B.) For example, the

offering documents disclosed that the loans underlying "Group II" of GSAA Home Equity Trust 2007-5 had a combined loan-to-value ratio of over 85% and over 90% were "interest only mortgage loans." (CD99 Ex. A at S-59.)

C. Alleged Misrepresentations in the Offering Documents

NECA asserts that the offering documents contained false and misleading information about the underwriting guidelines of certain mortgage loan originators, the underlying property appraisals, the risks associated with the Certificates and methodologies used by the rating agencies. (*See* NECA Br. 26, 29, 34.) Not only do the offering documents themselves refute these general allegations, but neither NECA's Brief nor any of its four complaints provides a single fact about the loans underlying the Certificates at issue here, the underwriting practices used for those loans or the ratings methodologies employed for those Certificates. Instead, NECA relies on allegations about the subprime mortgage and securitization markets as a whole, based on little more than the widespread public attention that those markets received amid the evolving economic crisis. NECA also did not allege that the loans at issue performed any differently than similarly situated loans in the context of a nationwide housing crash of unprecedented proportion.

SUMMARY OF ARGUMENT

NECA had four opportunities to state a claim under Sections 11, 12(a)(2) and 15, but nonetheless failed to remedy the deficiencies in its allegations. (JA-195/38:4-19.) This Court should affirm the district court's dismissal with prejudice, whether on the grounds relied on by the district court, or on alternative grounds for affirmance fully briefed below and properly considered on this appeal. *See Blackman* v. *N.Y.C. Transit Auth.*, 491 F.3d 95, 100 (2d Cir. 2007) (per curiam).

First, the district court correctly held that NECA lacks standing with respect to the fifteen MBS offerings from which NECA never purchased any certificates. NECA alleged that it purchased certificates in only two of the seventeen offerings in question—the GSAA 2007-5 and GSAA 2007-10 offerings. Many courts, including the U.S. Court of Appeals for the First Circuit, have held that a plaintiff lacks standing to assert claims with respect to securities it did not buy. *See Plumbers' Union Local No. 12 Pension Fund* v. *Nomura Asset Acceptance Corp.*, 632 F.3d 762, 771 (1st Cir. 2011). As the district court held, this conclusion applies with equal force to tranches of certificates within a single offering that plaintiff did not purchase. (JA-259/7:20-21 ("[NECA] may only represent the same certificate, not other people's purchases.")); *see also Stichting Pensioenfonds ABP* v. *Countrywide Fin. Corp.*, No. 10-CV-07275 (MKP),

2011 WL 3558173, at *2 (C.D. Cal. Aug. 9, 2011); *Me. State Ret. Sys.* v. *Countrywide Fin. Corp.*, No. 2:10-CV-0302 MRP, 2011 WL 4389689, at *2 (C.D. Cal. May 5, 2011) ("*Maine State II*"). Moreover, as NECA concedes (JA-381/7:14-25), it lacks standing under Section 12 as to the GSAA 2007-5 certificates because NECA did not purchase those certificates in the initial public offering.

Second, the district court also correctly held that NECA failed to plead a cognizable economic loss, an essential element of its claims under Sections 11 and 12(a)(2). NECA did not allege a single missed or late payment, let alone a default, on either of the Certificates. Instead, NECA relied on the assertion—without any supporting *factual* allegations—that "the value of the Certificates has diminished." (JA-235 ¶ 92.) Leaving aside whether such a conclusory allegation may be sufficient for securities with liquid markets, the district court repeatedly noted that NECA's allegations that its Certificates are not marketable at the prices it paid for them must be viewed in the context of express disclosures about the lack of a liquid secondary market and "the express warning that [the Certificates] might not be resalable." (JA-320.) Despite several chances to allege cognizable loss, NECA failed to plead facts to support its assertion of diminished value.

Third, the Court may affirm the dismissal of this action on the alternate basis that the applicable statute of limitations bars NECA's claims. The

record below established that a sea of public information—on which NECA bases its Complaint rather than allegations about the specific Certificates at issue—makes clear that NECA had at least inquiry notice of its purported claims more than one year before it filed its initial complaint in December 2008. Moreover, NECA's substantially identical allegations against Goldman Sachs in *Plumbers' Union Local No. 12 Pension Fund* v. *Nomura Asset Acceptance Corp.*—similarly based largely on public information about the MBS industry—demonstrate that NECA had actual notice of the claims here more than one year before December 2008. (CD99 Ex. F.)

Fourth, the Court may affirm dismissal on the additional basis that NECA failed to allege any actionable misstatement or omission. NECA asserted that the offering documents understated the risk of borrower default—and, therefore, the risk of diminished pass-through payments—by failing to describe accurately the originators' underwriting guidelines for the underlying loans, the role of independent property appraisers and the methods employed by the third-party rating agencies. But SEC Regulation AB, 17 C.F.R. § 229.1100 (2005), requires that MBS offering documents disclose only *known* deviations from underwriting guidelines, and NECA did not properly allege any facts suggesting that Defendants—which originated none of the mortgages but instead acquired them at arm's length from third-party originators—had such knowledge.

See Blackmoss Invests. Inc. v. *ACA Capital Holdings, Inc.*, No. 07-CV-10528, 2010 WL 148617, at *9 (S.D.N.Y. Jan. 14, 2010) (Sweet, J.) (interpreting Item 303 of SEC Regulation S-K (17 C.F.R. § 229.303)); *see also J&R Mktg., SEP* v. *Gen. Motors Corp.*, 549 F.3d 384, 391-92 (6th Cir. 2008); *Steckman* v. *Hart Brewing, Inc.*, 143 F.3d 1293, 1296-97 (9th Cir. 1998). Moreover, its allegations about appraisals and ratings involve inherently inactionable opinions (not facts). And NECA did not provide *any* factual information about the specific loans underlying the two Certificates at issue here. Again, NECA merely borrowed generalized allegations from other MBS lawsuits, which in turn collected snippets from public reports criticizing mortgage originators and rating agencies—not only establishing that NECA was on notice for limitations purposes, but also that there was no basis to tie those industry generalizations to these specific securities.

Finally, the district court did not abuse its discretion in denying NECA's belated request to file a *fourth* amended complaint.

STANDARD OF REVIEW

This Court reviews *de novo* the district court's dismissal of the complaint under Rule 12(b)(6) of the Federal Rules of Civil Procedure. *See Burch* v. *Pioneer Credit Recovery, Inc.*, 551 F.3d 122, 124 (2d Cir. 2008) (per curiam). The Court may affirm the judgment on any ground supported by the record; it is not restricted to the ground on which the district court relied. *See Blackman*,

491 F.3d at 100. This Court reviews the denial of leave to amend based on untimeliness or delay for abuse of discretion. *See Parker* v. *Columbia Indus.*, 204 F.3d 326, 339 (2d Cir. 2000).

ARGUMENT

I. THE DISTRICT COURT CORRECTLY RULED THAT NECA DOES NOT HAVE STANDING TO BRING CLAIMS WITH RESPECT TO CERTIFICATES IT DID NOT PURCHASE.

The district court correctly held that NECA does not have standing to pursue claims under Sections 11 and 12(a)(2) with respect to certificates that NECA did not purchase. First, the district court held that NECA lacked standing to assert claims based on offerings from which it did not purchase certificates. Second, the district court determined that NECA had standing to bring claims only based on the tranches of certificates it purchased.

A. NECA Does Not Have Standing to Bring a Claim Regarding Offerings from Which It Did Not Purchase Certificates.

The district court correctly ruled that NECA lacks standing to assert claims based on the fifteen securitizations from which NECA did not purchase certificates:

> The Act only grants standing for claims by purchasers. Plaintiffs did not purchase certificates from the 15 trusts other than 2007-10 and 2007-5. And plaintiff has not shown that the injuries it alleges based upon purchases of those two trusts are the same injury as those allegedly suffered by purchasers of outlying trusts backed by

> distinct sets of loans. Other district courts addressing this issue have reached the same conclusion.

(JA-198/41:2-9.)

Article III standing requires an injury in fact; that is, a personal injury to the plaintiff itself, not injury occasioned upon other, unidentified members of a class it purports to represent. *See Warth* v. *Seldin*, 422 U.S. 490, 502 (1975). A plaintiff with one sort of injury lacks standing to challenge a different, though perhaps related, injury because "standing is not dispensed in gross." *Lewis* v. *Casey,* 518 U.S. 343, 358 n.6 (1996). A Section 11 claim can be asserted only by "any person acquiring such security," 15 U.S.C. § 77k(a), and a Section 12(a)(2) claim can be asserted only by "the person purchasing such security," *id.* § 77*l*(a).

1. Courts Have Unanimously Held That Standing Must Be Established at Least at the Offering Level for MBS-Related Claims.

"Every court to address the issue in a MBS class action has concluded that a plaintiff lacks standing under both Article III of the U.S. Constitution and under Sections 11 and 12(a)(2) of the [Securities] Act to represent the interests of investors in MBS offerings in which the plaintiffs did not themselves buy." *Me. State Ret. Sys.* v. *Countrywide Fin. Corp.*, 722 F. Supp. 2d 1157, 1163 (C.D. Cal. 2010) ("*Maine State I*") (collecting decisions). For example:

- In *Nomura*, the First Circuit concluded that "claims related to the six trusts from which the named plaintiffs never purchased securities were properly dismissed[.]" 632 F.3d at 771. The court reasoned that

"the named plaintiffs have no stake in establishing liability as to misconduct involving the sales of those certificates" that they did not purchase. *Id.*

- In *Employees' Retirement System of the Government of the Virgin Islands* v. *J.P. Morgan Chase & Co.*, No. 09 Civ. 3701 (JGK), 2011 WL 1796426, at *6 (S.D.N.Y. May 10, 2011), Judge Koetl held that "plaintiff was not harmed by, and thus has no standing to sue for, alleged misrepresentations contained in other prospectuses or registration statements offering other securities that it did not purchase."

- In *Public Employees' Retirement System of Mississippi* v. *Merrill Lynch & Co.*, 714 F. Supp. 2d 475, 480-81 (S.D.N.Y. 2010), Judge Rakoff dismissed claims based on 65 of 84 MBS offerings at issue because plaintiffs had not purchased securities in those offerings, reasoning that standing "requires plaintiffs to have been personally injured, and plaintiffs thus have no standing to assert claims in relation to [offerings] in which plaintiffs did not personally invest." *Id.* (internal quotation marks omitted).

- In *City of Ann Arbor Employees' Retirement System* v. *Citigroup Mortgage Loan Trust Inc.*, 703 F. Supp. 2d 253, 260 (E.D.N.Y. 2010), Judge Wexler held that "Plaintiffs must be able to prove falsity with respect to statements, or omissions regarding the mortgages in which they purchased interests."

- In *New Jersey Carpenters Vacation Fund* v. *Royal Bank of Scotland Group, PLC*, 720 F. Supp. 2d 254, 266 (S.D.N.Y. 2010), Judge Baer concluded that "Plaintiffs need to show an injury connected to the offerings they challenge as misleading, and therefore Plaintiffs' claims with regard to offerings they did not purchase are dismissed for lack of standing."

- In *In re IndyMac Mortgage-Backed Securities Litigation*, 718 F. Supp. 2d 495, 501 (S.D.N.Y. 2010), Judge Kaplan held that "named plaintiffs have standing only with respect to offerings in which they purchased securities," and dismissed "the claims based on the [91] offerings in which named plaintiffs [had] not purchased."

NECA does not mention any of these cases, other than the First Circuit's *Nomura* decision.[1] (NECA Br. 61 n.25.) These decisions—and numerous others that NECA also ignores[2]—apply basic principles of Article III standing and the plain text of Section 11. Because NECA did not purchase in those other offerings, it had no "personal stake in the outcome" of an action based on them, and suffered no harm in those offerings that could be redressed by the court. *Clarry* v. *United States*, 85 F.3d 1041, 1049 (2d Cir. 1996); *see also Virgin Islands*, 2011 WL 1796426, at *6; *Maine State I*, 722 F. Supp. 2d at 1163.

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[1] NECA cannot distinguish *Nomura*. (NECA Br. 61 n.25.) Although the *Nomura* court said that the standing issue was "not so simple," it held that offering-level standing must be established. 632 F.3d at 768. Rather than having its "hands . . . tied" (NECA Br. 61 n.25) by a prior First Circuit decision, the court concluded that it was "inclined . . . to follow [the] lead" of that decision. 632 F.3d at 770.

[2] *See*, *e.g.*, *N.J. Carpenters Health Fund* v. *Novastar Mortg., Inc.*, No. 08 Civ. 5310 (DAB), 2011 U.S. Dist. LEXIS 36363, at *19 (S.D.N.Y. Mar. 31, 2011); *Pub. Emps.' Ret. Sys. of Miss.* v. *Goldman Sachs Grp., Inc.*, No. 09 CV 1110 (HB), 2011 WL 135821, at *7 (S.D.N.Y. Jan. 12, 2011); *N.J. Carpenters Health Fund v. DLJ Mortg. Capital, Inc.*, No. 08 Civ 5653 (PAC), 2010 WL 1473288, at *4 (S.D.N.Y. Mar. 29, 2010); *In re Wells Fargo Mortg.-Backed Certificates Litig.*, 712 F. Supp. 2d 958, 965 (N.D. Cal. 2010); *Mass. Bricklayers & Masons Fund* v. *Deutsche Alt-A Sec.*, No. CV 08-3178, 2010 WL 1370962, at *1 (E.D.N.Y. Apr. 6, 2010); *In re Lehman Bros. Sec. & ERISA Litig.*, 684 F. Supp. 2d 485, 490-91 (S.D.N.Y. 2010); *In re Wash. Mut., Inc. Sec., Deriv. & ERISA Litig.*, 259 F.R.D. 490, 504 (W.D. Wash. 2009).

2. NECA Cannot Establish Standing by Reference to a Common Shelf Registration.

Despite failing to purchase any certificates from fifteen of the offerings it seeks to challenge, NECA contends that it "has standing to represent purchasers of Certificates from the 15 other Trusts via Prospectus Supplements, because each of those false and misleading supplements were issued pursuant to the ***same*** false and misleading Registration Statement." (NECA Br. 55.) This is wrong. NECA's argument ignores the applicable SEC regulations governing shelf registration statements and the terms of the Registration Statement itself. Every court to have considered NECA's argument has rejected it.

The shelf registration process enables qualified issuers to offer securities periodically by first filing a "base" registration statement and then subsequently filing separate prospectus supplements for each offering.[3] *See* 17 C.F.R. § 230.415 (2008); Delayed or Continuous Offering and Sale of Securities, Securities Act Release No. 33-6423, 47 Fed. Reg. 39,799 (Sept. 2, 1982). These supplements add information about the securities offered and *alone* contain the descriptions of loan underwriting standards, loan characteristics and

[3] The shelf registration statement is a "base prospectus" that need not contain complete information regarding the terms of the securities to be offered and is not a "final prospectus" under the Securities Act. *See* 17 C.F.R. § 230.430B (2008); Securities Offering Reform, Securities Act Release No. 33-8591, 70 Fed. Reg. 44,722, 44,770-74 (Aug. 3, 2005).

features of the securities offered. *See* 17 C.F.R. § 229.512(a)(1) (2008). Thus, as the court in *Maine State I* explained:

> Even where there is a common shelf registration statement, that statement contained only an illustrative form of a prospectus supplement. It was the final prospectus supplement filed with the SEC at the effective date of the offering of the Certificates that contained a description of the mortgage pool underlying the Certificates and the underwriting standards by which the mortgages were originated.

722 F. Supp. 2d at 1164 (internal quotation omitted).

The SEC has provided by regulation that "for the purpose of determining any liability under the [Securities Act], each . . . post-effective amendment [to a shelf registration statement, such as a prospectus supplement,] shall be deemed to be *a new registration statement* relating to the securities offered therein." 17 C.F.R. § 229.512(a)(2) (2008) (emphasis added); *accord In re Wells Fargo*, 712 F. Supp. 2d at 964. As this Court has recognized, "§ 229.512(a)(2), operating in the context of securities offered pursuant to the post-effective registration, deems the offering date to be the post-effective registration date, not the initial registration date." *Finkel* v. *Stratton Corp.*, 962 F.2d 169, 174 (2d Cir. 1992). Each of the seventeen offerings that NECA seeks to challenge is thus subject to a *separate* "registration statement"—consisting of the original shelf registration statement and prospectus, as well as the applicable prospectus supplement.

That each of the offerings was issued pursuant to a different "registration statement" under SEC regulations dooms NECA's textual standing argument (NECA Br. 54, 59-60), because "*the* registration statement" referred to in Section 11 is different for each offering, even if all of those registration statements include the base prospectus. *See*, *e.g.*, *In re Wachovia Equity Sec. Litig.*, 753 F. Supp. 2d 326, 370 (S.D.N.Y. 2011) ("defining the field of possible misstatements does not thereby enlarge the field of possible plaintiffs"); *In re Wells Fargo*, 712 F. Supp. 2d at 964 ("[T]he case law is clear that a named plaintiff has standing under Section 11 only as to the documents that governed his own purchase of securities. . . . Therefore, plaintiffs cannot gain standing purely as a result of the common Registration Statements.")

The shelf registration statement relating to NECA's Certificates contained no information about the certificates or the mortgage collateral involved in any of the offerings.[4] Indeed, when the shelf registration statement was filed, the individual trusts had not yet been created and the loans underlying them may not yet have been originated. Each trust issues its certificates only after filing the detailed prospectus supplements. As with other MBS, "the representations made in

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[4] *See* Registration Statement No. 333−139817, *available at* http://sec.gov/Archives/edgar/data/807641/000091412107000261/gs6950500-s3a1.txt (last visited September 25, 2011).

the prospectus supplements accompanying the issuance of those securities [were] themselves unique, focused on the specific loans underlying each offering and the specific underwriting standards and origination practices in effect at the time those specific loans were originated." *Maine State I*, 722 F. Supp. 2d at 1164; *see also N.J. Carpenters Vacation Fund*, 720 F. Supp. 2d at 265 ("the underlying details . . . are unique to each of the offerings"; "the harm Plaintiffs may have suffered based on misstatements in the Offering Documents for the Certificates they purchased has no bearing on any harm suffered by other investors based on alleged misstatements in other offering documents"). Indeed, NECA conceded that a prior iteration of its complaint did not even attempt to allege that the generic shelf registration statement contained any actionable misstatements or omissions. (CD67 4:16-23.)

3. The Non-MBS Cases Cited by NECA Are Inapposite.

NECA defends its erroneous standing theory by citing a number of decisions not involving MBS. (NECA Br. 55-56.) This reliance is misplaced. *In re Countrywide Financial Corp. Securities Litigation*, 588 F. Supp. 2d 1132 (C.D. Cal. 2008), on which NECA primarily relies (NECA Br. 55-56), examined standing in the context of three corporate debt offerings issued by Countrywide, and concerned disclosures about Countrywide's business and financial condition. *In re Countrywide*, 588 F. Supp. 2d at 1144-45. Indeed, two of the three offerings

shared a common prospectus and pricing supplements. *Id.* at 1165 & n.36. The court found that the disclosures in the offerings contained common misrepresentations concerning Countrywide and stressed "the narrow application of [its] analysis," noting that "it is possible that later issuances could incorporate very different alleged violations and have in common only a minor common misrepresentation or omission." *Id.* at 1167. Here, in contrast, the disclosures in the shelf registration statement pursuant to which NECA purchased the Certificates contained no information about the loan originators and loans underlying the certificates issued pursuant to later prospectus supplements. For that reason, the *Countrywide* court's "narrow application of [its] analysis" would not apply. For these same reasons, *In re Citigroup Inc. Bond Litigation*, 723 F. Supp. 2d 568, 584-85 (S.D.N.Y. 2010), and *In re American International Group, Inc. 2008 Securities Litigation*, 741 F. Supp. 2d 511, 538 (S.D.N.Y. 2010), which both relied on *In re Countrywide's* analysis in the context of corporate debt offerings, are inapposite.[5]

[5] The remainder of NECA's authority (NECA Br. 56 & n.22) is likewise inapposite. None involves a shelf registration statement (let alone an MBS shelf registration). Instead, each involves a conventional registered offering under which no prospectus supplement was filed.

B. NECA Has Standing to Bring Claims Based Only on Certificates That It Actually Purchased.

In addition to holding that NECA could bring claims only with respect to offerings from which it purchased Certificates, the district court also correctly limited NECA's claims to those specific tranches of Certificates that it purchased. (JA-259/7:14-25; JA-260/8:2-5; JA-261/16-19.) For the same reasons as offering-level standing, certificate-level standing is required by the plain text of Sections 11 and 12, and is warranted by the economic realities of the structure of MBS. *See Maine State II*, 2011 WL 4389689, at *3-8.

1. Sections 11 and 12 Confer Standing Only for the Specific Security Plaintiff Purchased.

Section 11 provides a cause of action for "any person acquiring *such security*" pursuant to an allegedly false or misleading offering statement. 15 U.S.C. § 77k(a) (emphasis added). Similarly, Section 12 provides recourse to "the person purchasing *such security*" by means of an untrue prospectus. *Id.* § 77*l*(a) (emphasis added). Accordingly, "[Section] 11(a) of the 1933 Act confines the cause of action it grants to 'any person acquiring such security' while the remedy granted by [Section] 12 of that Act is limited to the 'person purchasing such security.'" *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 736 (1975). "The text of Sections 11 and 12(a)(2)" thus "precludes . . . Plaintiffs from bringing claims for losses in securities they never purchased or acquired."

Wachovia Equity, 753 F. Supp. 2d at 369; *see also City of Ann Arbor*, 703 F. Supp. 2d at 260 ("Section 11 requires a plaintiff to show that he was a purchaser of the security at issue."); *In re Paracelsus Corp.*, 6 F. Supp. 2d 626, 631 (S.D. Tex. 1998) ("A plaintiff bringing suit under either Section 11 or Section 12 of the Securities Act at least must allege that he or she purchased or acquired the security at issue.").

Each MBS certificate issued pursuant to a given prospectus supplement represents a different tranche within an offering and is a distinct security. Thus, in *Maine State II*, the court "conclude[d] that the plain text of the Securities Act dictates that Plaintiffs must have acquired or purchased the security on which they sue. It is undisputed that each Certificate is a separate security. Thus, Plaintiffs have standing to assert their claims with respect only to those Certificates a named Plaintiff has purchased." 2011 WL 4389689, at *6.

2. The Nature and Structure of MBS Require a Certificate-Level Standing Inquiry.

Standing should be evaluated on a certificate-level basis in the context of MBS for the same reasons that other courts have required offering-level standing. *See Maine State II*, 2011 WL 4389689, at *3-8; *Stichting*, 2011 WL 3558173, at *2 (adopting reasoning of *Maine State II*). Just as courts have reasoned that plaintiffs' factual allegations in MBS cases "focus on the underlying details contained in the . . . prospectus supplements and are unique to each of the

offerings: the downgrade in credit ratings, the particular guidelines used by the mortgage originator for that pool of loans, and the default and delinquency rates all differ based on the particular offering," these variances exist at the certificate level, as well. *N.J. Carpenters Vacation Fund*, 720 F. Supp. 2d at 265. Similarly, concerns at the offering level—that a plaintiff "would have to show that the practices of which [it] complain[s] occurred with respect to the mortgages in which [it] invested, and thereby caused injury"—are equally valid at the certificate level. *City of Ann Arbor*, 703 F. Supp. 2d at 260.

Both GSAA 2007-5 and GSAA 2007-10—the two offerings from which NECA purchased—consisted of multiple certificates, each of which was a separate security with its own rights, original principal balance, interest rate, credit rating, specific payment rights and priority for receiving cash flow distributions from the loans underlying the trust. Certificates in both offerings were backed by different loan pools. For example, the prospectus supplement for GSAA 2007-5—in which NECA purchased the Class 1AV1 Certificate—offered forty-two separate classes of certificates, divided into two separate groups, with each group backed by a different loan pool. These loan pools contained different types of underlying loans: Group 1 certificates were backed largely by fixed-rate loans, whereas Group 2 were backed by adjustable-rate loans. The originators of these loans varied as well: 75% of the Group 1 loans were acquired from various loan sellers

under the GS Conduit program, whereas 69% of the Group 2 loans were originated by Countrywide. The trustee reports for the GSAA 2007-5 offering show that each certificate has received different monthly payments of principal and interest depending on the certificate's distribution priority and payment rights, and the performance of the specific loans backing that certificate.[6]

Each certificate is a separate security with different fundamental characteristics. As the court stated in *Maine State II*:

> The variety in terms of type of loan products, length of the term, credit rating and interest rate, existed at the tranche level to allow each investor to choose the characteristics of the security that best matched its needs. Some investors forwent the opportunity for a higher return and chose safer investments, such as the most senior tranches. Other investors decided the riskiest tranches met their needs. In all cases, each tranche provided a different investment opportunity with unique characteristics.

2011 WL 4389689, at *7.

Given the characteristics of each separate certificate in each offering, and that certain certificates referenced *different* underlying loans, any effect of the alleged misrepresentations on a GSAA 2007-10 Class A2A Certificate, for example, differs from the potential effect on other certificates in the GSAA

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[6] July 2011 GSAA Home Equity Trust 2007-5 Certificateholder Distribution Summary (publicly available via http://www.sec.gov, as specified in the offering documents, and also through Bloomberg).

2007-10 offering. Requiring standing at the certificate level is justified by the practical reality that different certificates have different investment characteristics and may suffer different harm based on the non- or under-performance of sometimes differing underlying loans.

C. A Determination of Standing Is Appropriate on a Motion to Dismiss and Should Not Be Deferred.

NECA argues that the district court should have deferred deciding on which certificates NECA could sue until consideration of class certification issues. (NECA Br. 62.) That is incorrect: "Standing concerns the scope of the court's power in the first instance," and "is antecedent to the class certification issue." *Hoffman* v. *UBS-AG*, 591 F. Supp. 2d 522, 532 (S.D.N.Y. 2008).

Although "a suit may be a class action," this "adds nothing to the question of standing[.]" *Lewis*, 518 U.S. at 357 (internal quotation marks omitted). "[E]ven named plaintiffs who represent a class must allege and show that they personally have been injured, not that injury has been suffered by other, unidentified members of the class to which they belong and which they purport to represent." *Id.*

Courts have repeatedly rejected NECA's position. "[I]t is black letter law that a rule of procedure cannot create standing." *Pub. Emps. Ret. Sys. of Miss.* v. *Merrill Lynch*, 714 F. Supp. 2d at 480. As a result, plaintiffs "cannot bypass the injury requirement by simply invoking Rule 23." *Wachovia Equity*, 753

F. Supp. 2d at 369; *see also*, *e.g.*, *Maine State I*, 722 F. Supp. 2d at 1163 & n.6 (collecting MBS-related Section 11 decisions determining lack of standing); *Hoffman*, 591 F. Supp. 2d at 530-32 (granting motion to dismiss Securities Act claims based on lack of standing); *In re AIG Advisor Group Sec. Litig.*, No. 06 CV 1625 (JG), 2007 WL 1213395, at *3-6 (E.D.N.Y. Apr. 25, 2007) (same); *In re Merrill Lynch Inv. Mgmt. Funds Sec. Litig.*, 434 F. Supp. 2d 233, 236 (S.D.N.Y. 2006) (same); *see also Wells Fargo*, 712 F. Supp. 2d at 964 (lead plaintiffs' purchase of certificates from less than one-third of challenged offerings "concerns the lead plaintiffs' standing, not their fitness as class representatives under Federal Rule of Civil Procedure 23's typicality analysis.").

The decisions NECA cites do not support delaying a determination of standing. For example, *In re Salomon Smith Barney Mutual Fund Fees Litigation* (NECA Br. 63 n.26) held "that the Article III standing determination should *precede* that of class certification" and dismissed claims "[w]ith regard to the sixty-eight funds of which Plaintiffs own no shares," "because Plaintiffs cannot satisfy the standing requirements." 441 F. Supp. 2d 579, 607 (S.D.N.Y. 2006) (emphasis added).

The remainder of the securities cases NECA cites (NECA Br. 63-64) all arise under Section 10(b) of the Securities Exchange Act and not Section 11 or 12 of the Securities Act. *See Green* v. *Wolf Corp.*, 406 F.2d 291 (2d Cir. 1968);

In re XM Satellite Radio Holdings Sec. Litig., 237 F.R.D. 13 (D.D.C. 2006); *In re Enron Corp. Sec. Litig.*, 206 F.R.D. 427 (S.D. Tex. 2002). Unlike Sections 11 and 12, Section 10(b) "allows a plaintiff to claim that it was harmed by fraudulent representations that are 'connected to' a security that the plaintiff purchased or sold." *Virgin Islands*, 2011 WL 1796426, at *6. Consequently, a "plaintiff need not have purchased or sold every security that was affected by the alleged scheme to defraud to sue a defendant for the alleged scheme to defraud and to seek to represent a class of purchasers or sellers who similarly relied on the same scheme to defraud, even if they purchased different securities." *Id.* Standing under Sections 11 and 12, in contrast, is narrowly defined by the statutes; Section 10(b) decisions are thus wholly inapposite.[7]

II. THE DISTRICT COURT CORRECTLY RULED THAT NECA FAILED TO ALLEGE ADEQUATELY A "COGNIZABLE INJURY" UNDER SECTION 11.

"Although a plaintiff has no obligation to plead damages under Section 11 of the Securities Act, the plaintiff must nevertheless satisfy the court that she has suffered a cognizable injury under the statute." *In re AOL Time*

[7] Several other cases that NECA cites (NECA Br. 62) do not even discuss the securities laws. *See Cent. States Se. & Sw. Areas Health & Welfare Fund* v. *Merck-Medco Managed Care, LLC*, 504 F.3d 229 (2d Cir. 2007) (ERISA); *Comer* v. *Cisneros*, 37 F.3d 775 (2d Cir. 1994) (housing discrimination); *Grasty* v. *Amalgamated Clothing & Textile Workers Union*, 828 F.2d 123 (3d Cir. 1987) (RICO and labor laws).

Warner, Inc. Sec. & "ERISA" Litig., 381 F. Supp. 2d 192, 246 (S.D.N.Y. 2004) (citations omitted). Section 11 provides for damages of "the difference between the amount paid for the security" and either "(1) the value thereof as of the time such suit was brought, or (2) the price at which such security shall have been disposed of in the market before suit, or (3) the price at which such security shall have been disposed of after suit but before judgment." (NECA Br. 46 (quoting 15 U.S.C. § 77(k)(e)).) When NECA filed its Third Amended Complaint, it still held the Certificates at issue and had not suffered any missed payments on the Certificates. Thus, the narrow question before this Court is whether NECA adequately pleaded a diminution in the value of the Certificates at the time NECA brought suit. *See Bell Atl. Corp.* v. *Twombly*, 550 U.S. 544, 570 (2007) (plaintiff must plead "enough *facts* to state a claim to relief that is plausible on its face" (emphasis added)); *Ashcroft* v. *Iqbal*, 129 S. Ct. 1937, 1951 (2009) ("[A] formulaic recitation of the elements of a cause of action will not do.") (citing *Twombly*).

Although NECA argues that its "allegations suffice[d] to allege the Fund's injury in fact" (NECA Br. at 48), an examination of the Complaint reveals that it did not plead adequately a diminution in value of the Certificates in the unique context of the product and market at issue. The district court correctly held that the existence of a secondary market cannot be presumed here because the offering documents specifically disclaimed the existence of a secondary market,

and NECA's conclusory allegations do not suffice to plead a diminished secondary market price for the Certificates. NECA also failed to plead any facts that, given the absence of a secondary market for the Certificates, would establish that the value of the Certificates has declined. When recovery is dependent on plaintiff's alleging the diminution in value of a security, courts have refused to allow speculative estimates of potential loss to replace factual allegations of cognizable loss. *See*, *e.g.*, *Jackson Nat'l Life Ins. Co.* v. *Ligator*, 949 F. Supp. 200, 207-08 (S.D.N.Y. 1996). Here, as in the *IPO* case, "plaintiff has no conceivable damages under Section 11" and NECA's "claims must be dismissed." *In re Initial Pub. Offering Sec. Litig.*, 544 F. Supp. 2d 277, 299 (S.D.N.Y. 2008); *see also Stark Trading* v. *Falconbridge Ltd.*, 552 F.3d 568, 573-74 (7th Cir. 2009); *In re Broderbund/Learning Co. Sec. Litig.*, 294 F.3d 1201, 1203-05 (9th Cir. 2002).

A. Under Section 11, Plaintiff Must Plead a Cognizable Loss.

NECA does not dispute that under Section 11, plaintiff must plead a cognizable loss. (*See* JA-45.) "[P]laintiff must plead *facts* demonstrating that he suffered the particular type of injury contemplated by the statute." *In re Mut. Funds Inv. Litig.*, 384 F. Supp. 2d 845, 866 (D. Md. 2005) (emphasis added); *see also Metz* v. *United Cntys. Bancorp*, 61 F. Supp. 2d 364, 378 (D.N.J. 1999) ("[U]nder Section 11, it is not enough to merely plead injuries"; instead, "plaintiff[] must plead a certain kind of injury.").

These required allegations include facts that plaintiff sold the security at issue or plausibly "could have sold" the security "at the time suit was filed . . . for an amount less than [it] paid." *In re Mut. Funds Invest. Litig.*, 384 F. Supp. 2d at 867. In other words, plaintiff must adequately plead "diminution in the value of securities caused by the false or misleading statements or omissions of the defendant." *Metz*, 61 F. Supp. 2d at 378. As the Seventh Circuit has explained, "[e]ven notice pleading requires pleading the elements of a tort, and one element of the section 11 tort is sale at a loss." *Stark Trading*, 552 F.3d at 574.

B. NECA Has Not Suffered Any Actual Loss from Missed Payments Under the Certificates.

A holder of mortgage pass-through certificates is entitled to a stream of principal and interest payments funded by payments from the borrowers on the underlying loans. *See*, *e.g.*, *Luminent Mortg. Capital, Inc.* v. *Merrill Lynch & Co.*, 652 F. Supp. 2d 576, 578 (E.D. Pa. 2009) ("[M]ortgage-backed securities are long-term debt instruments that represent the income stream from a pool of mortgages."). The Complaint did not allege any missed payment from the trusts, and NECA admits that no payments have been missed. (NECA Br. 46.) Publicly available trustee reports detail the payments made to each class of certificates and show that, as of January 2011, GSAA 2007-5 had made all scheduled principal and

interest payments to holders of the Class 1AV1 Certificates.[8] Likewise, as of January 2011, GSAA 2007-10 had made all scheduled principal and interest payments to holders of the Class A2A Certificates.[9] Accordingly, NECA neither alleged nor suffered actual loss from its investment in the Certificates at the time the district court dismissed its Section 11 claims.

C. NECA Failed to Allege Facts Supporting a Permissible Inference That the Value of the Certificates Had Declined.

The district court correctly held that NECA failed to plead facts sufficient to support a permissible inference that the Certificates had declined in value at the time it filed suit. The district court first addressed the issue in connection with the Second Amended Complaint and found the threadbare allegations insufficient. (*See* JA-183–84/26:25-27:1 ("How can you complain about the sales price if you are not trying to sell?"); JA-199/42:20-22 ("The [Second Amended] [C]omplaint does not appear to allege facts permitting an inference that the plaintiff suffered a cognizable loss.").) After granting NECA an opportunity to provide support for its assertion regarding the price of the security,

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[8] January 2011 GSAA Home Equity Trust 2007-5 Certificateholder Distribution Summary (publicly available via http://www.sec.gov, as specified in the offering documents, and also through Bloomberg).

[9] January 2011 GSAA Home Equity Trust 2007-10 Certificateholder Distribution Summary (publicly available via http://www.ctslink.com, as specified in the offering documents, and also through Bloomberg).

the district court again ruled that merely asserting that the Certificates had declined in value was inadequate to show a cognizable loss. (JA-320-21 ("The complaint also fails in turn to allege any facts regarding the actual market price for the Certificates at the time of suit. Thus, even if NECA could raise a cognizable injury by claiming a decline in market price, it has failed to provide factual enhancement of that assertion.").)

"There is no single, objectively acceptable method for valuing the complex asset-backed instruments at issue here." *Yu* v. *State St. Corp.*, 686 F. Supp. 2d 369, 379 (S.D.N.Y. 2010). Unlike liquid securities, MBS are "non-exchange listed securities, the valuation of which may differ depending on the model used in the calculations." *Alteram S.A.* v. *Beacon Hill Asset Mgmt., LLC.*, No. 03 Civ. 2387 (LAK), 2004 WL 367709, at *2 n.5 (S.D.N.Y. Feb. 27, 2004). A plaintiff cannot simply "look[] up closing prices [of MBS] in the *Wall Street Journal*" on a given day because transactions are infrequent and their prices are not public, and therefore valuation "involve[s] the exercise of judgment." *Fraternity Fund Ltd.* v. *Beacon Hill Asset Mgmt. LLC.*, 376 F. Supp. 2d 385, 396 (S.D.N.Y. 2005).

The district court (1) correctly ruled that NECA failed to allege a liquid secondary market for the Certificates, and (2) as a result, required that NECA allege at least some facts to support its assertion regarding the "diminished"

price of the Certificates. (JA-235 ¶ 92.) NECA failed to do so, despite the district court's warning and NECA's representation to the district court that it had an expert who could substantiate its valuation of the Certificates (JA-184/27:2-4).

1. No Liquid Secondary Market Exists for the Certificates.

The district court correctly concluded that it could not presume the existence of a secondary market for the Certificates, because "the Certificates were issued with the express warning that they might not be resalable." JA-320. The Offering Documents for both Certificates expressly warned that:

> **Your Investment May Not Be Liquid.** The underwriter intends to make a secondary market in the offered certificates, but it will have no obligation to do so. We cannot assure you that such a secondary market will develop or, if it develops, that it will continue. Consequently, you may not be able to sell your certificates readily or at prices that will enable you to realize your desired yield.

(CD99 Ex. A at S-50; Ex. B at S-35–36.)[10] NECA invested in the Certificates knowing that a secondary market for the securities might not exist. NECA was required to do more than simply allege "the hypothetical price of the Certificates" in a secondary market, the existence of which was not established. (JA-320.)

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[10] The district court noted that it was "unsurprising" that the Certificates were issued with an express disclaimer regarding the lack of a secondary market "given the structure of asset-backed securities, which are 'primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period." (JA-320 (quoting 17 C.F.R. § 229.1101(c)).)

NECA contends that the district court erred in "brushing off" and "disbeliev[ing]" its allegations of a secondary market for the Certificates. (NECA Br. 52.) Yet the Third Amended Complaint's "allegations" regarding the existence of a secondary market consist of one conclusory sentence: "There is a secondary market for the purchase and sale of the Certificates." (JA-236 ¶ 93.) The Complaint alleges no facts about the secondary market. Rather, NECA alleged that "[t]here has been a market for the resale of investments ***like the Certificates*** since at least 2007" and that "[t]he trading volume of Certificates ***like those at issue*** was at least $1-$1.5 billion during December 2008." (*Id.* (emphasis added).) These allegations say nothing about the Certificates themselves, but instead make assertions about securities purportedly similar to the Certificates in some undisclosed way. NECA's attempt to rely on "investments like the Certificates" without identifying those investments to establish a secondary market must fail, and the district court correctly disregarded such opaque pleading.

2. NECA Failed to Allege Facts to Support Its Assertion That the Value of the Certificates Had Declined.

In the absence of well-pleaded allegations of a secondary market for the Certificates capable of generating a reliable value for the Certificates, the district court correctly required NECA to plead facts that, when taken as true, would plausibly establish that the value of the Certificates at the time it brought this action was less than the value at the time of NECA's purchases. *See Twombly*,

550 U.S. at 570; *Iqbal*, 129 S. Ct. at 1940 (plaintiff must plead "factual content that allows the court to draw the [necessary] reasonable inference"). NECA's conclusory pleading did not meet its burden.

Courts have long refused to allow speculative estimates of potential loss to stand in the place of allegations of cognizable loss. For instance, in *First Nationwide Bank* v. *Gelt Funding Corp.*, this Court, in the context of a RICO action that required plaintiff to plead actual damages, stated that plaintiff cannot "allege actual injury by simply claiming that it incurred additional risk of loss as a consequence of the fraud." 27 F.3d 763, 768 (2d Cir. 1994). Likewise, in *Jackson*, the court addressed whether plaintiff adequately alleged a diminution in value of certain notes it held on which defendants had not yet defaulted and concluded that "[a] mere 'unlikelihood'" of repayment did not amount to "provable, nonspeculative damage." 949 F. Supp. at 207-08. Examples of loss allegations that "are phrased in the conditional tense or in generalized terms," such as losses that a securityholder "might" suffer, are insufficient because plaintiff "must allege more than just a tendency to cause economic loss." *Luminent*, 652 F. Supp. 2d at 591.

The district court correctly refused to credit NECA's unsupported assertion that "in a non-forced sale in the secondary market in December 2008, [NECA] and the Class would have netted, at most, between 35 and 45 cents on the

dollar." (JA-236 ¶ 93.) NECA supplied no basis for how it arrived at this hypothetical sale price and, significantly, did not allege that it was based on an actual sale of the Certificates. This failure is especially glaring given NECA's representation to the district court that its expert could substantiate its valuation of the Certificates. (JA-184/27:2-4.) Neither NECA's bare assertion of additional risk of loss (JA-205 ¶ 6), nor its allegation that the credit ratings for the Certificates were downgraded to "junk" status (JA-205 ¶ 6; JA-235 ¶ 90) is sufficient to support a plausible inference that the Certificates decreased in value. "Valuation of mortgage-backed securities . . . essentially is an exercise in estimating future cash flows." *In re First Union Corp. Sec. Litig.*, 128 F. Supp. 2d 871, 894 n.22 (W.D.N.C. 2001). NECA continued to receive the full monthly payments due on the Certificates and thus failed to allege any impairment of "future cash flows." *Id.*[11]

Nor can NECA find refuge in its allegations regarding the value of "like securities." (JA-236 ¶ 93.) As NECA acknowledges (NECA Br. 53), in

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[11] Defendants respectfully submit that *New Jersey Carpenters Health Fund* v. *DLJ Mortgage Capital, Inc.*, No. 08 Civ. 5653 (PAC), 2010 WL 1473288, at *5-6 (S.D.N.Y. Mar. 29, 2010), on which NECA relies (NECA Br. 48, 50-51), was wrongly decided as to this issue. Further, unlike in *DLJ Mortgage*, NECA's Third Amended Complaint does not even allege the specific diminution in value of the Certificates. *See id.* at *5 ("Plaintiff points to the fact that the value of its Certificates plummeted by 79% since the offering.").

McMahan & Co. v. *Wherehouse Entertainment, Inc.*, 65 F.3d 1044, 1048-49 (2d Cir. 1995), this Court recognized that "the value of a security may not be equivalent to its market price," because "under certain circumstances, the market price may not adequately reflect the security's value." Thus, the price at which a certificate has sold in the secondary market may not reflect the true "value" of the security, as that term is used in Section 11. Alleging a range of supposed market values without so much as disclosing the basis of such an estimate is wholly inadequate, even under Rule 8(a). *See*, *e.g.*, *Twombly*, 550 U.S. at 545 ("Factual allegations must be enough to raise a right to relief above the speculative level . . . .").

III. THE DISMISSAL MAY BE AFFIRMED ON THE ALTERNATE GROUND THAT NECA'S CLAIMS ARE TIME BARRED.

This Court may affirm the dismissal of this action on the independent, threshold ground that all of NECA's claims are time barred as demonstrated by the record below. *See*, *e.g.*, *Adirondack Transit Lines, Inc.* v. *United Transp. Union, Local 1582*, 305 F.3d 82, 88 (2d Cir. 2002) ("[W]e are entitled to affirm the district court on any ground for which there is support in the record, even if not adopted by the district court."). Section 13 of the Securities Act requires that claims based on Sections 11 and 12(a)(2) be filed within "one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence." 15 U.S.C. § 77m. The one-year period begins

to run when a plaintiff has either actual notice or "inquiry notice" of the alleged misrepresentations. *Dodds* v. *Cigna Sec., Inc.*, 12 F.3d 346, 349-50 (2d Cir. 1993).

"An investor does not have to have notice of the entire [alleged] fraud being perpetrated to be on inquiry notice." *Newman* v. *Warnaco Grp., Inc.*, 335 F.3d 187, 193 (2d Cir. 2003) (internal quotation marks omitted); *see also In re Alstom SA Sec. Litig.*, 406 F. Supp. 2d 402, 421 (S.D.N.Y. 2005). Instead, plaintiff is on notice when he obtains "notice of . . . facts, which in the exercise of reasonable diligence, would have led to actual knowledge." *LC Capital Partners, LP* v. *Frontier Ins. Grp., Inc.*, 318 F.3d 148, 154 (2d Cir. 2003) (internal quotation marks omitted).[12]

[12] In *Merck & Co.* v. *Reynolds*, 130 S. Ct. 1784 (2010), the Supreme Court addressed when claims under Section 10(b) of the Securities Exchange Act of 1934 accrue under 28 U.S.C. § 1658(b)(1), which provides that such claims must be brought no later than "2 years after the discovery of the facts constituting the violation." The Court emphasized this language in rejecting the "inquiry notice" standard for which the defendant had argued, observing that "[n]othing in the text [of the statute] suggests that the limitations period can sometimes begin *before* 'discovery' can take place." *Merck*, 130 S. Ct. at 1797. Section 13 of the Securities Act, in contrast, provides that claims under that Act are barred "unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery *should have been made by the exercise of reasonable diligence*." 15 U.S.C. § 77m (emphasis added). The courts of this Circuit have nevertheless disagreed whether the Merck holding should be extended to Section 13. *Compare*, *e.g.*, *In re IndyMac Mortg.-Backed Sec. Litig.*, No. 09 Civ 4583 (LAK), 2011 WL 2508254, at *7 (S.D.N.Y. June 21, 2011) (*Merck* inapplicable to Section 13), *with N.J. Carpenters Health Fund* v. *Residential Capital LLC*, Nos. 08 CV 8781 (HB), 08 CV 5093 (HB), 2011 WL 2020260, at *4-5 (S.D.N.Y. May 19, 2011) (extending *Merck* to Section 13). Even if the *Merck*
(footnote continued)

"Information that may be held to constitute inquiry notice includes any financial, legal, or other data, such as public disclosures in the media . . . that provide the plaintiff with sufficient storm warnings to alert a reasonable person to the probability that there may have been either misleading statements or material omissions involved in the sale of the securities at issue." *In re Alstom*, 406 F. Supp. 2d at 421; *see also Korwek* v. *Hunt*, 646 F. Supp. 953, 958 (S.D.N.Y. 1986), *aff'd*, 827 F.2d 874 (2d Cir. 1987). Moreover, "[f]or purposes of this determination, investors are presumed to have read prospectuses, quarterly reports, and other information related to their investments." *DeBenedictis* v. *Merrill Lynch & Co.*, 492 F.3d 209, 216 (3d Cir. 2007) (internal quotation marks omitted).

"Courts can readily resolve the issue of inquiry notice as a matter of law on a motion to dismiss—as has been done in a vast number of cases in this circuit—where the facts needed for determination of when a reasonable investor of ordinary intelligence would have been aware of the existence of fraud can be gleaned from the complaint and papers . . . integral to the complaint." *Staehr* v. *Hartford Fin. Servs. Grp., Inc.*, 547 F.3d 406, 412 (2d Cir. 2008) (internal quotation marks omitted).

(footnote continued)
holding were to apply here, NECA had actual notice of each element of its claims—which, unlike Section 10(b) claims, do not require scienter—more than one year before the filing of its complaint.

NECA filed this action on December 11, 2008. NECA's claims are time barred because it was on inquiry, if not actual, notice of the alleged misrepresentations challenged here well before December 11, 2007. Indeed, the Complaint itself confirms that NECA was on notice because, unlike other MBS complaints that focus on allegations of historically nonpublic statistics and "confidential" witnesses specific to the certificates and originators at issue, the complaints here relied almost exclusively on information that was widely available prior to December 11, 2007, including:

- An April 2006 study, concluding that "60% of borrowers had 'exaggerated' their income by more than 50%," which a March 2007 Credit Suisse analyst report cited. (JA-216 ¶¶ 39-41.)
- June 2007 Senate testimony that there was a "terrible conflict of interest" where appraisers "experience systemic problems with coercion" and are "ordered to doctor their reports." (JA-223 ¶ 61.)
- A publicly available February 2007 survey, reporting that "[n]ine out of 10 real estate appraisers say they've been pressured to raise property valuations by mortgage brokers [and] . . . lenders." (JA-224 ¶ 62.)

In addition, NECA's First Amended Complaint cited several more sources evidencing that NECA was on notice of its claims before December 2007:

- A May 7, 2007 letter Countrywide publicly submitted to the Office of Thrift Supervision stating that "almost 60% of the borrowers who obtained sub-prime hybrid ARMs [from Countrywide] would not have qualified at the fully indexed rate" (JA-33 ¶ 84);
- An August 2007 article about Countrywide's lending practices, stating that "potential borrowers were often led to high-cost and sometimes

unfavorable loans that resulted in richer commissions for Countrywide's smooth-talking sales force" (JA-37 ¶ 96);

- A May 2005 article in which AmNet and GreenPoint officers discuss their concerns about their companies' origination practices (JA-71–72 ¶ 162); and
- A publicly available August 2007 study, identifying SouthStar as the "riskiest of all [originators] reviewed" (JA-76 ¶ 169).

NECA's deletion of these prior references to publicly available documents in the ensuing Complaint cannot nullify those prior allegations or make its Complaint timely, because a "Plaintiff[] may not, by amending [its] [c]omplaint, undo the inquiry notice and resulting obligations conceded by [its] first complaint." *In re Integrated Res. Real Estate Ltd. P'ships Sec. Litig.*, 850 F. Supp. 1105, 1132 n.47 (S.D.N.Y. 1993); *cf. Babaev* v. *Grossman*, 312 F. Supp. 2d 407, 410 (E.D.N.Y. 2004) ("The toothpaste of an admission of actual knowledge of fraud should not so easily be squeezed back into the tube."). NECA's prior pleading, which shows it was on notice, remains an admission. *In re IPO*, 544 F. Supp. 2d at 291 n.96; *Integrated Res.*, 850 F. Supp. at 1132 n.47.

Further, NECA's allegations against defendants, including Goldman Sachs, in *Plumbers' Union Local No. 12 Pension Fund* v. *Nomura Asset Acceptance Corp.*, another MBS case, indisputably demonstrate that NECA was on notice of the problems in the subprime industry on which its present Complaint rests no later than Summer 2007. (CD99 Ex. F) In *Nomura*, NECA alleged:

- "By the summer of 2007, the truth about the performance of the mortgage loans that secured the [Nomura] Certificates began to be revealed to the public and the rating agencies began to put negative watch labels on Certificate tranches or classes, ultimately downgrading many." (*Id.* ¶ 8.)
- "On July 17, 2007, Moody's announced a possible downgrade of Nomura [certificates]." (*Id.* ¶ 169.)
- "On November 13, 2007, Moody's downgraded numerous classes of Certificates of Nomura." (*Id.* ¶ 173.)
- "On December 10, 2007, Moody's downgraded the ratings of certain investments backed by sub-prime home loans issued by Wells Fargo because borrowers were having problems keeping up with payments, raising concerns that Wells Fargo's underwriting practices were suspect." (*Id.* ¶ 174.)

The *Nomura* complaint makes clear that the industry practices NECA challenges were well publicized more than a year before NECA filed its initial complaint. Much as NECA cannot disclaim its allegations in earlier versions of complaints in this action, it too cannot escape the implications of its allegations in *Nomura*.

The wealth of information available to NECA before December 11, 2007 is summarized in a chronology that Defendants provided to the district court. This chronology shows the very allegations of which NECA complains, including that there were problems with subprime underwriting guidance; that appraisers were inflating property values; and that rating agencies had conflicts of interest when evaluating securitizations. (CD98-3.)

Unlike other actions that offer specific allegations relating to the originator and securities at issue, which ostensibly emerged only more recently,

NECA's claims are predicated on this public information, which clearly constituted notice of the same "problems" about which NECA now complains, and thus was also sufficient to trigger notice of its claims. Accordingly, NECA's claims under Sections 11 and 12(a)(2) are time barred.

IV. THE DISMISSAL MAY BE AFFIRMED ON THE ALTERNATIVE GROUND THAT THE COMPLAINT FAILS TO ALLEGE ANY MATERIAL MISSTATEMENTS OR OMISSIONS.

The district court's dismissal of this action also may be affirmed on the alternate basis that NECA failed to allege any actionable misstatement or omission. Sections 11 and 12(a)(2) require plaintiff to allege that (i) the offering documents contained a material misstatement or omission, and (ii) the defendants had a duty to disclose the allegedly misrepresented information but failed to do so. *See Panther Partners, Inc.* v. *Ikanos Commc'ns., Inc.*, 538 F. Supp. 2d 662, 668 (S.D.N.Y. 2008), *aff'd*, 347 F. App'x 617 (2d Cir. 2009).

NECA fails to allege any threshold duty to disclose exceptions to the underwriting guidelines used to originate loans. Indeed, SEC Regulation AB—the regulation that requires disclosure of loan underwriting guidelines in MBS offerings—limits the duty to disclose departures from those guidelines to "known" departures, and NECA fails to allege that Defendants originating the loans here had that knowledge. As a result, NECA's Complaint focuses on allegations that the offering documents misrepresented departures from the originators' underwriting

guidelines, even though the offering documents accurately described those guidelines. Moreover, because the Complaint is based entirely on inferences from public information about the industry, rather than allegations about *actual* loans held by the trusts issuing *these* Certificates, not only was NECA on notice of its claims for statute of limitations purposes as discussed above, but those allegations fail to establish that any of the supposedly misrepresented underwriting practices affected any (much less a material number) of the loans held by these trusts.

A. NECA Does Not Allege a Violation of Any Duty to Disclose.

"[I]t is well established that there is no liability in the absence of a duty to disclose, even if the information would have been material." *In re Morgan Stanley Tech. Fund Sec. Litig.*, 643 F. Supp. 2d 366, 375 (S.D.N.Y. 2009), *aff'd*, 592 F.3d 347 (2d Cir. 2010). "The relevant SEC regulations answer the question as to what material facts are required to be stated in an issuer's [offering documents]." *In re N2K, Inc. Sec. Litig.*, 82 F. Supp. 2d 204, 207 (S.D.N.Y.), *aff'd*, 202 F.3d 81 (2d Cir. 2000). Here, Item 1111 of SEC Regulation AB—which "comprehensively" "provid[es] tailored disclosure requirements and guidance for [Securities Act] filings involving asset-backed securities," *Asset-Backed Securities*, 70 Fed. Reg. 1506-01, 1506 (Jan. 7, 2005)—addresses the "Information Regarding Pool Asset Types and Selection Criteria" that Defendants were required to disclose:

> A description of the solicitation, credit-granting or underwriting criteria used to originate or purchase the pool assets, including, *to the extent known*, any changes in such criteria and the extent to which such policies and criteria are or could be overridden.

17 C.F.R. § 229.1111(a)(3) (emphasis added). Thus, Item 1111(a)(3) both creates a duty to disclose loan underwriting standards, and limits the duty to disclose deviations from those standards.

"While it is true that Section 11 claims generally do not require pleading scienter," that is not applicable when an SEC regulation requires "actual knowledge." *Blackmoss*, 2010 WL 148617 at *9. A "knowledge" requirement in an SEC regulation mandates that a plaintiff "plead, with some specificity, facts establishing that the defendant had actual knowledge" of the information that the SEC regulation requires to be disclosed. *Id.* (dismissing claim under Item 303 of Regulation S-K (17 C.F.R. § 229.303), which, like Item 1111 of Regulation AB, requires disclosure of certain information only to the extent "known"); *Garber* v. *Legg Mason, Inc.*, 537 F. Supp. 2d 597, 614 (S.D.N.Y. 2008) (under Regulation S-K, "pleading a trend's *existence* is [not] enough to support a claim," rather "the trend [must] actually be *known*").[13] Even if such information is

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[13] *See also J&R Mktg.*, 549 F.3d at 391-92 (Regulation S-K imposes duty to disclose only "known trends" under Section 11 and does not require disclosure of information that may have been "knowable"); *Steckman*, 143 F.3d at 1296-97 (Regulation S-K imposes duty to disclose only "known trends" under

(footnote continued)

material, it need not be disclosed unless it is actually known by the defendant. *See*, *e.g.*, *Silverstrand Invs.* v. *AMAG Pharms., Inc.*, C.A. No. 10-10470-NMG, 2011 WL 3566990, at *6 (D. Mass. Aug. 11, 2011) (disclosure not required because reports did "not amount to a 'known trend or uncertainty'"). As in *Blackmoss*, Plaintiff has failed to plead any facts suggesting that Defendants had actual knowledge of any deviations by unaffiliated mortgage loan originators from their underwriting guidelines.

Four decisions in the U.S. District Court for the Southern District of New York have held that the knowledge requirement set forth in Item 1111 applies only to omission claims, and does not apply to misstatement claims. *See N.J. Carpenters Vacation Fund*, 720 F. Supp. 2d at 268-69; *In re Lehman*, 684 F. Supp. 2d at 493-94; *N.J. Carpenters Health Fund* v. *Residential Capital, LLC*, No. 08 CV 8781 (HB), 2010 WL 1257528, at *5 (Mar. 31, 2010); *Pub. Emps.' Ret. Sys. of Miss.* v. *Goldman Sachs Grp., Inc.*, No. 09-CV-1110 (HB), 2011 WL 135821, at *10-11 (S.D.N.Y. Jan. 12, 2011). These cases posit a distinction between omission and misstatement claims that nowhere appears in the Regulation. They also ignore that the relevant misrepresentation alleged in those cases was a supposed failure to

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(footnote continued)
Section 11); *In re Thornburg Mortg., Inc. Sec. Litig.*, No. CIV 07-0815 JB/WDS, 2011 WL 2429189, at *41 (D.N.M. June 2, 2011) (disclosure under Regulation S-K required only where defendant has "actual knowledge" of known trend).

disclose *unknown* departures from underwriting standards. Yet the very same provision of Item 1111 that requires disclosure of underwriting standards also makes explicit that departures from those standards must be disclosed only to the extent that they are "known." *See* 17 C.F.R. §§ 229.1110(b), 1111(a)(3) (2005). Because Item 1111 requires disclosure of underwriting guidelines, narrowing its application to omission cases—that is, circumstances in which the issuer did not discuss underwriting guidelines at all—would render the provision meaningless.

Indeed, apparently recognizing that Item 1111 requires actual knowledge of departures from underwriting guidelines, NECA asserts that Defendants knew that originators were departing from those guidelines. (JA-227–28 ¶ 72.) But NECA offers no support for this assertion, as is required for allegations of knowledge under Fed. R. Civ. P. 9(b), and elsewhere *disclaims* making such an allegation: "For purposes of [NECA's Section 11 claim], plaintiff expressly excludes and disclaims any allegation that could be construed as alleging fraud or intentional or reckless misconduct." (JA-236 ¶ 95; *see also* JA-238 ¶ 107.) Plaintiff has thus failed to allege facts sufficient to state a claim based on supposed deviations from loan underwriting standards.

B. Disclosures in the Offering Documents Render the Alleged Misrepresentations Not False or Misleading As a Matter of Law.

The offering documents for both the GSAA 2007-5 and the GSAA 2007-10 offerings disclosed that inherently risky loans backed their respective

certificates. Defendants' disclosure of these and similar characteristics of the underlying loans, along with other detailed disclosures in the offering documents refute NECA's allegations and demonstrate that investors were provided with all material information about the Certificates.

1. The Offering Documents Extensively Disclosed the Originators' Underwriting Guidelines and Possible Exceptions Thereto.

Stripping away NECA's rhetoric and generalized industry-wide allegations, the thrust of its allegations is that the offering documents for the Certificates failed to disclose (1) that originators could issue loans pursuant to alternative lending programs that reduced or eliminated documentation requirements or (2) that the underwriting policies themselves were only "guidelines" from which originators had discretion to deviate. (JA-204–05 ¶¶ 3-4; 211 ¶ 27; 217 ¶ 42; 218-19 ¶¶ 47-48; *see also* JA-212–216 ¶¶ 29-41; 217-18 ¶¶ 43-45; 219-220 ¶¶ 49-51.) Yet the offering documents provided detailed descriptions of these programs and their lenient lending standards, and made clear that originators could make exceptions to these already-reduced standards. (*See* CD99 Ex. A at S-65; Ex. B at S-50–55.)

For example, the GSAA 2007-5 prospectus supplement devoted nearly eight pages to Countrywide's underwriting guidelines (CD99 Ex. A at S-63–70), explaining that the "information that a borrower is required to disclose and

whether the information is verified depends, in part, on the documentation program used in the origination process," and that "[a] prospective borrower may be eligible for a loan approval process that limits or eliminates Countrywide['s] standard disclosure or verification requirements or both" (*id.* at S-66). It also disclosed that, under Countrywide's "Standard Underwriting Guidelines," alternative, reduced, oral and limited documentation programs were utilized, some of which did not even require income or asset verification. (*Id.* at S-67–68.) It further disclosed that, under Countrywide's "Expanded Underwriting Guidelines," "[t]he borrower is not required to disclose any income information [under certain programs]" and that "[u]nder the No Income/No Asset Documentation Program, no documentation relating to a prospective borrower's income, employment or assets is required." (*Id.* at S-68–69). Similar disclosures were made in the GSAA 2007-10 offering documents. (*See* CD99 Ex. B at S-50–73.)

The Prospectus Supplement for the GSAA 2007-10 securitization went even further by disclosing that, "[i]n response to current market conditions," Wells Fargo had tightened its underwriting guidelines in August and September 2007 to require additional documentation from borrowers. (CD99 Ex. B at S-73.) The Prospectus Supplement warned investors that the stricter guidelines did not apply to Wells Fargo loans underlying the offering and many loans underlying the offering would not have been made if the new guidelines had applied. These and

other similar disclosures refute NECA's claim that investors were misled that originators were issuing loans without verifying borrower information.

Although some courts have held that allegations regarding systematic departures from underwriting standards are sufficient to state a claim, those cases generally involved specific allegations documenting the complete abandonment of underwriting standards and typically were supported by first-hand reports by actual witnesses particular to the originator and securities at issue. *See*, *e.g.*, *Nomura*, 632 F.3d at 773-74 (involving specific allegations of "wholesale abandonment of underwriting standards"); *Boilermakers Nat'l Annuity Trust* v. *WaMu Mortg. Pass Through Certificates, Series AR1*, 748 F. Supp. 2d 1246, 1255 (W.D. Wash. 2010) (allegations that "underwriting guidelines ceased to exist"). Here, in contrast, the Complaint generally refers at most to "ignorance" of underwriting standards, an apparent attempt to obscure the distinction between deviations from origination standards based on compensating factors (as disclosed in the offering documents) and complete abandonment of those standards. The Complaint fails to plead any specific facts that would permit the conclusion that the key originators of the loans underlying the trusts at issue here completely abandoned their underwriting standards for those loans. (*See*, *e.g.*, JA-219 ¶ 48 (originator's underwriting guidelines were "not based upon sound loan underwriting standards"); JA-220 ¶ 50

(bare assertion that "[d]uring 2006 and 2007" originator "began to completely ignore" its loan underwriting standards).)

NECA's allegations regarding the practices of certain originators—purportedly based on its "investigation" of former employees of Defendants, unaffiliated originators and appraisers—are insufficient. (JA-210 ¶ 25; JA-217–20 ¶¶ 42-50; JA-225–26 ¶¶ 64-68.) NECA has merely recycled allegations from secondary sources cited in its prior complaints. While relying on these public sources establishes NECA's notice of its claims for limitations purposes as discussed above, NECA cannot state a claim by relying on the same conclusory allegations found in public sources and on unidentified hearsay about general market practices or other unrelated offerings. *See In re Merrill Lynch & Co. Research Reports Sec. Litig.*, 273 F. Supp. 2d 351, 374 (S.D.N.Y. 2003) ("snippets of e-mails and conclusions of [the regulator] . . . [fail] to constitute well-pleaded facts"); *First Nationwide*, 27 F.3d at 771 (rejecting "unsupported claims regarding the 'actual' value of the collateral properties when the loans were made" because "[u]nder Rule 12(b)(6) . . . unwarranted deductions of fact are not admitted") (internal quotation marks omitted).

2. The Offering Documents Disclosed the Involvement of Independent Mortgage Brokers and Appraisers.

NECA alleges that the offering documents failed to disclose sufficiently that third parties may not have followed originators' appraisal

procedures. (JA-204–05 ¶¶ 3-4; JA-211 ¶ 27; JA-222 ¶¶ 56-57, JA-223–24 ¶¶ 58-62; JA-225–28 ¶¶ 64-73.) Numerous courts have recognized, however, appraisals are subjective opinions based on the particular methods and assumptions employed by the particular appraiser and cannot constitute actionable misstatements or omissions. *See IndyMac*, 718 F. Supp. 2d at 511; *Tsereteli* v. *Residential Asset Securitization Trust*, 692 F. Supp. 2d 387, 393 (S.D.N.Y. 2010); *DLJ Mortg. Capital*, 2010 WL 1473288, at *7-8; *Fifty Assocs.* v. *Prudential Ins. Co. of Am.*, 450 F.2d 1007, 1010-11 (9th Cir. 1971) (noting that "land value is generally a matter of opinion only") (internal quotation marks omitted). Although NECA, relying mostly on industry-wide allegations and unidentified hearsay, posits that appraisers were not truly independent and were pressured to provide inflated appraisals, the complaint is "devoid of any such allegation" that Defendants *knew* that a single loan underlying the Certificates at issue here was subject to any allegedly faulty appraisal. *Tsereteli*, 692 F. Supp. 2d at 393; *see Fait* v. *Regions Fin. Corp.*, No. 10-2311-cv, 2011 WL 3667784, at *3 (2d Cir. Aug. 23, 2011) ("[W]hen a plaintiff asserts a claim under section 11 or 12 based upon a belief or opinion alleged to have been communicated by a defendant, liability lies only to the extent that the statement was both objectively false and disbelieved by the defendant at the time it was expressed."); *DLJ Mortg. Capital*, 2010 WL 1473288 at *7-8.

3. The Offering Documents Did Not Make Any Misrepresentations About Borrowers' Loan Documents.

NECA erroneously alleged that the offering documents "represented" to investors that all the documents submitted by borrowers, appraisers and others in connection with the underlying mortgage loans were free of *any* material misrepresentations. (JA-204–05 ¶¶ 3-4; JA-211 ¶ 27; JA-212–14 ¶¶ 29-36; JA-221–22 ¶¶ 52-56; JA-227–28 ¶¶ 70-72; JA-231 ¶ 78.) No such representation was ever made to investors. Instead, the excerpts that the Complaint mischaracterizes as "representations" *to investors* are in fact representations and warranties that *loan originators* did (or might) make *to loan purchasers* (here, GS Mortgage). Accordingly, this language cannot be the basis for a Section 11 or 12(a)(2) claim by an investor such as NECA. *See In re Flag Telecom Holdings, Ltd. Sec. Litig.*, 618 F. Supp. 2d 311, 321 (S.D.N.Y. 2009) ("The test for determining whether the prospectus contained a material misstatement or omission is 'whether the defendants' representations [in the prospectus], taken together and in context, would have misled *a reasonable investor*.'" (quoting *Olkey* v. *Hyperion 1999 Term Trust, Inc.*, 98 F.3d 2, 5 (2d Cir. 1996)).

Moreover, contrary to NECA's allegations, the offering documents expressly disclosed that originators were not required to verify income for certain programs and also disclosed that originators could deviate from their guidelines concerning borrowers' debt-to-income ratios. (CD99 Ex. A at S-65; CD99 Ex. B

at S-51, S-55, S-65.) Thus, the offering documents disclosed precisely what NECA alleged was misrepresented.

4. The Offering Documents Disclosed the Calculation of Loan-to-Value Ratios.

NECA alleges that the offering documents did not disclose that originators could make loans that did not meet their standard loan-to-value guidelines. (JA-204–05 ¶¶ 3-4; JA-211 ¶ 27; JA-228–231 ¶ 74-78.) Such allegations—which are duplicative of, and derived entirely from, NECA's flawed appraisal allegations—have been dismissed by numerous courts, and this Court should adopt the same approach. *See Tsereteli*, 692 F. Supp. 2d at 394; *IndyMac*, 718 F. Supp. 2d at 511; *DLJ Mortg. Capital*, 2010 WL 1473288 at *8.

5. The Offering Documents Accurately Disclosed the Certificates' Ratings.

NECA alleged that Defendants failed to disclose that the ratings assigned to the Certificates could be inaccurate and were based on supposedly "outdated" models. (JA-204–05 ¶¶ 3-4; 211 ¶ 27; 232-33 ¶¶ 79-84.) NECA does not—and cannot—dispute that the Certificates had AAA ratings when issued or that those ratings had been issued by independent ratings agencies. Numerous courts have rejected identical ratings claims, and this Court should do the same. *See*, *e.g.*, *Nomura*, 632 F.3d at 775; *J&R Mktg.*, 549 F.3d at 392-93; *In re Morgan Stanley Mortg. Pass-Through Certificates Litig.*, No. 09 Civ. 2137 (LTS), 2011

WL 4089580, at *21-22 (S.D.N.Y. Sept. 15, 2011); *Residential Capital*, 2010 WL 1257528, at *6; *DLJ Mortg. Capital*, 2010 WL 1473288, at *7-8; *N.J. Carpenters Vacation Fund*, 720 F. Supp. 2d at 270-71; *Tsereteli*, 692 F. Supp. 2d at 394-95; *In re Lehman Bros.*, 684 F. Supp. 2d at 494-95.

6. Defendants Disclosed That Goldman Sachs May Have Held Other Investments.

NECA alleged that the offering documents should have disclosed that Goldman Sachs entered into various unspecified "credit default swaps." (JA-234 ¶¶ 85-89.) Because this information has no bearing on the investments at issue and instead reflects strategies or alleged conflicts of interest that are well known to investors, Defendants were under no obligation to make such a disclosure. *See Resnik* v. *Swartz*, 303 F.3d 147, 154 (2d Cir. 2002) ("Disclosure of an item of information is not required, however, simply because it may be relevant or of interest to a reasonable investor."). Nevertheless, the offering documents disclosed the possibility that Goldman Sachs might take positions in the offered certificates or similar securities. (CD99 Ex. A at A-1-1–2-31; Ex. B at S-108.)

C. NECA Did Not Adequately Allege Materiality.

The Complaint failed to allege that any purported misrepresentations were material because NECA has tied none of the industry-wide practices described in its allegations to any of the specific loans or Certificates at issue here (much less established a material impact on them).

Despite having access to publicly filed documents describing the characteristics of *all* the loans conveyed to the trusts, NECA never alleged that any of *those* loans (i) violated any originators' underwriting guidelines, (ii) were issued based on inaccurate loan documentation, (iii) had an inaccurate property appraisal or loan-to-value ratio or (iv) contributed to inaccurate ratings for the Certificates. Even if some "improper" loans were included in the loan pools, NECA has never alleged any facts suggesting that the inclusion of those loans was material—especially in light of the huge number of loans held by the trusts (over 4,000 in the GSAA 2007-5 and GSAA 2007-10 trusts) and in comparison to the performance of similar loans in the housing downturn and eventual meltdown. This omission is particularly glaring, because the district court specifically warned NECA that it could not state a claim without such allegations to establish materiality. (JA-200/43:20-24.)

V. THE DISTRICT COURT DID NOT ABUSE ITS DISCRETION IN DENYING NECA LEAVE TO FILE A FOURTH AMENDED COMPLAINT.

When, as here, a district court denies leave to amend based on untimeliness or delay, its decision is entitled to review under the abuse of discretion standard. *See Parker*, 204 F.3d at 339.

At oral argument on NECA's motion for leave to amend on March 3, 2011—more than two years after NECA filed its initial complaint—the district court stated as follows:

> And I think that this sale, for this lawsuit, for this complaint, comes too late for me to permit you to amend. I'm not making a ruling on anything else you can do about it. You may have other avenues. But to amend the complaint to allege the sale after three and a half amendments and a dismissal, and, in addition, when the sale was made before the application was made for me to opine that this was a proper exception to the final judgment rule, I cannot grant.

(JA-383/14:24-15:6.) In short, the district court denied NECA's motion to amend its complaint for a fourth time on the ground that such a request was "just too late." (JA-381/6:9; JA-382 11:19.)

"A district court does not abuse its discretion in denying leave to amend where, as here, the motion is unduly delayed and that delay is not supported by good cause." *Nicholas* v. *Davis*, 74 F. App'x 131, 134 (2d Cir. 2003). NECA was aware of the district court's construction of Section 11 loss as early as January 2010. (JA-173/16:25 – JA-174/17:1-5.) NECA nevertheless waited until months after its sale of the securities to notify the court. *See* JA-382/12:21-23 ("[Y]ou didn't bring this motion the minute you sold. You waited until I turned you down on an exception to the final judgment rule."). Moreover, the district court was permitted to "exercise its discretion more exactingly" where NECA "had an

opportunity to assert the amendment earlier," but waited until the denial of both its motion for reconsideration and its Rule 54(b) motion before seeking leave to amend via a motion for relief under Rule 60(b). *State Trading Corp. of India, Ltd.* v. *Assuranceforeningen Skuld*, 921 F.2d 409, 418 (2d Cir. 1990); *cf. Nicholas*, 74 F. App'x at 134 (affirming denial of leave to amend where "[t]hree months elapsed between when the plaintiff learned of the alleged involvement of the defendant whom he wished to add to his complaint and the filing of his motion to amend his complaint").

Because NECA had already amended its complaint three times and then waited to notify the district court of its sale of the securities, the district court did not abuse its discretion in denying NECA's motion for leave to amend its Third Amended Complaint. *Cf. Denny* v. *Barber*, 576 F.2d 465, 471 (2d Cir. 1978) (affirming denial of leave to amend securities complaint and give plaintiffs a "third go-around," where district court "in dismissing the initial complaint, had put plaintiff's counsel on the plainest notice of what was required" and those defects were not corrected in the amended complaint).

CONCLUSION

For the foregoing reasons, the district court's dismissal of NECA's Third Amended Complaint should be affirmed.

Dated: New York, New York
September 28, 2011

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE WITH F.R.A.P. 32(a)(7)(C)

Pursuant to Rule 32(a)(7)(C) of the Federal Rules of Appellate Procedure, the undersigned counsel for Defendants-Appellees hereby certifies that this brief complies with the type-volume limitations of Rule 32(a)(7)(B). As measured by the word processing system used to prepare this brief, there are 13,924 words in this brief.

/s/ Richard H. Klapper
Richard H. Klapper

Dated: September 28, 2011

CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of September 2011 I caused the foregoing Brief for Defendants-Appellees to be served via Electronic Mail generated by the Court's electronic filing system (CM/ECF) with a Notice of Docket Activity pursuant to Local Appellate Rule 25.1. All counsel of record are registered CM/ECF users.

Six hard copies of the foregoing Brief for Defendants-Appellees were sent to the Clerk's Office by Hand Delivery to:

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