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AIG set to sue BofA for \$10.5bn

By Tom Braithwaite and Brooke Masters in New York



Bank of America shares dropped as much as 23 per cent on Monday, making it the worst performer in the Standard & Poor's 500, as the bank faced a \$10.5bn lawsuit from AIG over the sale of residential mortgage-backed securities allegedly "marred by fraud, misrepresentations and omissions".

The lawsuit filed in the New York Supreme Court on Monday, alleges that BofA and its subsidiaries wrote "defective" mortgages to borrowers who were not in a position to repay, packaged them into supposedly low-risk securities, and sold \$28bn-worth to AIG using offering documents that misrepresented the quality of the loans.

The claim is one of the largest institutional claims to arise from the 2008 financial crisis and stems from AIG's purchase of mortgage-backed securities. The group is attempting to rebuild after disastrous losses on separate credit default obligation insurance forced it to seek a \$180bn government bail-out. The BofA claim is expected to be followed by a flurry of other lawsuits against other investment banks on similar grounds.

Despite the massive losses sustained from the collapse of the mortgage market, relatively few claims have been filed over the past three years.

While MBIA, the monoline insurer, and HSH Nordbank have pending lawsuits, many institutional investors have held back in taking legal action, preferring to negotiate privately for compensation. Some of the biggest losers are reluctant to sue because they are subsidiaries of financial groups that also sold structured products.

Regulators and prosecutors, too, have been relatively cautious, although Goldman Sachs agreed to pay \$550m last year to settle allegations from the Securities and Exchange Commission that it committed fraud in its marketing of mortgage-backed securities known as Abacus. Goldman did not admit any wrongdoing.

The AIG suit focuses on alleged misdeeds at BofA and two of its crisis-era acquisitions – Merrill Lynch and Countrywide Financial. It alleges that the offering

documents for the 593 securities misrepresented the quality of the underlying mortgages and “grossly understated the riskiness”. Among other things, the securities allegedly overstated the loan-to-value ratios, the rate of owner occupancy and the credit ratings of the borrowers.

The complaint alleges that one BofA employee said he “didn’t give a flying f***” about debt-to-income ratios” as “we [Bank of America] can sell [the loans] to whoever”.

BofA responded: “AIG recklessly chased high yields and profits throughout the mortgage and structured finance markets. AIG is the very definition of an informed, seasoned investor, with losses solely attributable to its own excesses and errors. We reject AIG’s assertions and allegations.”

AIG responded in turn that: “It is disappointing but unsurprising that Bank of America continues to attempt to blame others for its own misconduct. Investors, no matter how sophisticated, were entitled to rely on its numerous written representations about the securities it sold. Now that it is clear that those representations were false, Bank of America must be held to account.”

Shares in Bank of America closed down 20 per cent at \$6.51, amid widespread selling in the bank sector.

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