UNITED STATES DISTRICT COURT
DISTRICT OF COLUMBIA

BERKLEY INSURANCE CO., et al., *Plaintiffs*, v. THE FEDERAL HOUSING FINANCE AGENCY, et al., *Defendants*.	Case No. 1:13-cv-1053-RCL
IN RE FANNIE MAE/FREDDIE MAC SENIOR PREFERRED STOCK PURCHASE AGREEMENT CLASS ACTION LITIGATIONS __________________________ This document relates to: ALL CASES	Case No. 1:13-mc-1288-RCL

MOTION FOR CLARIFICATION REGARDING THE COURT'S JULY 21, 2023 DECISION REGARDING THE ADMISSIBILITY OF DR. ATTARI'S TESTIMONY

With this motion, Plaintiffs seek clarification as to the scope of permissible testimony concerning Dr. Attari's Bond Event Study. The Court's July 21, 2023 memorandum opinion held that Dr. Attari will be permitted to testify that the Bond Event Study shows that the Third Amendment caused the decline in yield spreads. Plaintiffs do not seek reconsideration of this decision. Instead, Plaintiffs ask the Court to preclude Dr. Attari from offering the opinion that the Bond Event Study shows that the decline in yield spreads was attributable to bond investors' (or any investors') increased confidence in the GSEs' creditworthiness. He should not be permitted to offer that opinion because he cannot reliably exclude an alternative and much more likely explanation that is reflected in FHFA's internal documents that the decline in yield spreads was

attributable to an expectation of future declining supply of GSE bonds.[1] The documentation at the time shows that market observers believed that both the Net Worth Sweep and the accelerated reduction of the retained portfolio signaled to the bond market that GSE bonds would be substantially declining in supply, thus triggering more buying of GSE bonds, an increase in price, and a reduction in yield spread.

In short, Dr. Attari's Bond Event Study shows only that yield spreads declined in response to the announcement of the Third Amendment; it cannot distinguish between the investor confidence rationale and the declining supply rationale or explain the reason why bond yield spreads declined in response to the Third Amendment. Accordingly, while Dr. Attari can offer the opinion that the Third Amendment caused GSE bond yield spreads to change, he should not be permitted to testify that the change in yield spreads indicates an increase in bond investor confidence in the GSEs' creditworthiness, as opposed to a perception that the supply of GSE bonds would be substantially declining.[2]

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[1] The Court separately held that Defendants and Dr. Attari may not claim that mortgage-backed securities investors were reassured about the GSEs' creditworthiness. *See* Class ECF No. 336 at 3-5. This ruling necessarily precludes him also from stating that a broader undifferentiated group of "investors" or "the market" were reassured as well.

[2] Defendants have attempted through cross-examination of Dr. Mason to criticize Dr. Mason's use of the ***Equity*** Event Study with Plaintiffs' criticism of Dr. Attari's use of his ***Bond*** Event Study. As we have shown previously, *see* Class ECF No. 315 at 9 and note 7, there is a distinct and material difference between the two. The law requires an expert to account for potentially confounding causes of an event only when there is an "obvious alternative explanation." *Cain v. Harris Teeter, Inc.*, 954 F.Supp.2d 17, 21 (D.D.C. 2013) (quoting *Miller v. United States*, 287 Fed. Appx. 982, 984 (3d Cir. 2008)); *Packgen v. Berry Plastics Corporation*, 847 F.3d 80, 87 (1st Cir. 2017) (quoting Fed. R. Evid. 702 Advisory Comm. Note). With respect to the 50% drop in stock prices, the only plausible cause is the Third Amendment's Net Worth Sweep, which gave 100% of all future profits and net worth to the Treasury, guaranteeing that private shareholders could never receive anything. The existence of the Net Worth Sweep makes it completely irrelevant whether the GSEs were going to accelerate the reduction of their retained mortgage portfolio (or do anything else with the portfolio). Further, there is ***zero*** evidence from the time suggesting that anyone thought the stock drop related to the change from a 10% reduction in the portfolio to a 15%

ARGUMENT

In its July 21 opinion, the Court held that Dr. Attari may testify that his Bond Event Study shows the Third Amendment caused a decline in yield spreads in the small set of long-term bonds he examined. The Court concluded that this testimony is relevant to whether shareholders could "reasonably have expected FHFA, under the circumstances, to agree to a major part of" the Third Amendment is its role as conservator.

This motion does not seek reconsideration of that ruling. Instead, Plaintiffs submit this motion to clarify one specific but important issue as to the scope of Dr. Attari's permissible testimony on the Bond Event Study—namely, whether Dr. Attari may testify (and whether Defendants may argue) that the decline in yield spreads documented in the Bond Event Study specifically demonstrates that the Third Amendment increased bond investors' confidence in the GSEs' creditworthiness.

There is no basis for any such opinion or argument. In the prior trial, Dr. Attari did not merely testify that the Bond Event Study showed that the Third Amendment caused the decline in yield spreads (which the Court has permitted him to do again at this trial). Instead, he went beyond that testimony to assert that the Third Amendment caused the decline in yield spreads ***because it reassured investors about the GSEs' creditworthiness***. For example, he testified:

> **Q.** And so the way you've described it here, those bond prices changed in a favorable way in direct response to the announcement of the Third Amendment?
>
> **A.** Yes.

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reduction – whereas there is ample contemporaneous evidence attributing the stock drop to the Net Worth Sweep. By contrast, with respect to the small change in bond yields that occurred after the Third Amendment, there is substantial contemporaneous evidence showing that the change was caused by the perception that the supply of GSE bonds would be reduced, as shown above. Thus, Dr. Attari's failure to conduct a reliable analysis of how to disaggregate confounding causes is wholly unlike what Defendants are trying to argue about Dr. Mason's use of the stock drop study.

> **Q.** So the bonds that were getting traded around in a secondary market, the prices ***improved in a way that indicated they were safer***?
>
> **A.** Yes.
>
> **Q.** And you mentioned here ***"increased investor confidence in Fannie and Freddie."*** What does that refer to?
>
> **A.** ***Well, that refers to the fact that the bond prices, the increase in bond prices, is kind of telling us that investors are now more confident***. Because if they become less confident, prices would have gone down. If there had been no change in confidence, prices would have been unchanged.

Trial Tr. 1968:11-1969:1 (emphasis added).

Dr. Attari should not be permitted to offer that opinion because, as Plaintiffs have shown, there is a well-documented alternative explanation for the change in bond prices that Dr. Attari offers no reliable methodology for excluding—namely, that the Third Amendment created an expectation that there would be declining supply in the number of GSE bonds issued. FHFA itself explained that the "rationale" for the observed decline in yield spreads "is that as the Enterprises wind down there will be less longer-term debt issued, leaving investors to fight over existing supply." *See* Ex. A (PX-282) at 2. FHFA further explained in a separate report that "GSE debt spreads should stay tight given diminished forward supply on faster wind-down plans" and that "the prospect of fewer years of new issues remaining served as a 'last call' of sorts, particularly for longer maturities that may not be tapped again." *See* Ex. B (FHFA-DDC-0320333) (emphasis added). The same document stated that "GSE debt had its biggest one-day tightening since 2008 after the Treasury Department announced plans to accelerate the wind-down of Fannie Mae and Freddie Mac, instantaneously making outstanding issues more valuable *given the prospect of less forward looking supply*." *See id*. (emphasis added). *See also* Class ECF No. 290 at 6-8 (discussing

other documents identifying an expectation of declining supply as the reason why yield spreads declined).

Further, FHFA attributed this perception of an impending reduction in supply of GSE bonds to both the Net Worth Sweep and the accelerated reduction in the retained portfolio. *See* Ex. A at 2 (attributing the decline in yield spreads to the "Treasury Department's announcement earlier today regarding *changes* to the Preferred Stock Purchase Agreements (PSPAs)"); Ex. B at 1 (the "Treasury Department announced plans to accelerate the wind-down of Fannie Mae and Freddie Mac"); *see id*. ("GSE debt spreads gapped tighter after Treasury Department announcement sparked buying").

The key issue for this motion is therefore not Dr. Attari's inability to distinguish between which aspect of the Third Amendment caused the decline in yield spreads. Instead, it is Dr. Attari's inability to determine whether the cause of the change in bond yield spreads in response to the Third Amendment resulted from (1) an increase in investors' confidence in the GSEs' creditworthiness or (2) the perceived impending reduction in supply of GSE bonds, as FHFA's own documents reflect.

Defendants and Dr. Attari offer the jury no reliable basis for adopting the investor confidence explanation in lieu of the declining supply rationale. Because he has no reliable basis for doing so, Fed. R. Evid. 703 and 403 establish that he should not be permitted to argue that the Bond Event Study shows that there was an increase in bond investors' confidence in the GSEs' creditworthiness.

In the prior briefing, Defendants attempted in passing to assert that the Bond Event Study was confined to long-term bonds, and thus that the change in yield spreads could not be explained by the accelerated decline in the retained portfolio. That assertion fails for two reasons. First, as

shown above, the announcement of the Net Worth Sweep provision of the Third Amendment also triggered a perception that the supply of GSE bonds would decline – indeed, it is the principal signal of a "wind down." It is therefore beside the point whether the accelerated decline alone could have caused it. Second, as FHFA itself explained, the decline in spreads was ***more pronounced*** for longer term bonds, not less so, as Defendants' argument would have the Court believe. *See* Ex. A at 2 ("While spreads across the curve are tighter, ***the farther out the maturity, the tighter the spread***.") (emphasis added); Ex. B (stating that the "prospect of fewer years of new issues remaining served as a 'last call' of sorts, ***particularly for longer maturities that may not be tapped again***") (emphasis added).

While this issue was raised in our prior motion as another basis to exclude Dr. Attari's testimony about his event study in its entirety, Class ECF No. 290 at 8-10, 15-16; Class ECF No. 315 at 8-9, it was not resolved by the Court's July 21 ruling. For purposes of evaluating the Bond Event Study's admissibility, the Court held that it did not matter that Dr. Attari's methodology could not distinguish the impact of one aspect of the Third Amendment from the other.[3] By contrast, for purposes of evaluating whether Dr. Attari should be permitted to testify that the decline in yield spreads was due to increased investor confidence, it is relevant whether Dr. Attari can reliably assert the investor confidence rationale over the declining supply rationale as the explanation for the decline in yield spreads. Because he offers no reliable way to do so, Dr. Attari should not be permitted to opine that the Bond Event Study shows that bond investors were reassured about the GSEs' creditworthiness.

[3]*See* Class ECF No. 336 at 2 ("Specifically, plaintiffs argue that the event study does not isolate the NWS from other parts of the Third Amendment not at issue in this case, rendering it both unreliable and confusing to the jury.").

CONCLUSION

For the foregoing reasons, Dr. Attari should be precluded from offering the opinion, and Defendants should be precluded from arguing, that the Bond Event Study shows that the Third Amendment or Net Worth Sweep increased bond investors' (or any investors') confidence in the GSEs' creditworthiness.

Dated: July 28, 2023

Respectfully Submitted,

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EXHIBIT A

Message

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Sent: 8/17/2012 3:22:08 PM

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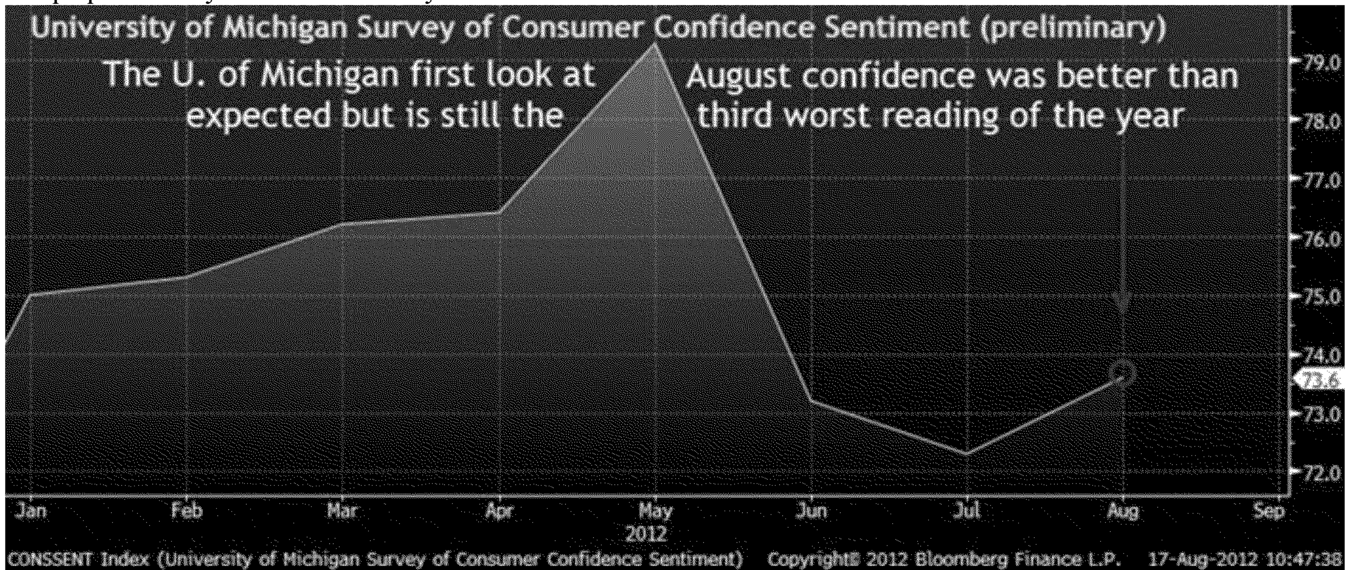
Subject: Capital Markets Update...Treasuries bouncing from worst levels of week...Credit spreads...Consumer Confidence...Treasury announcement tightens agency debt spreads, less impact on MBS...EU...Later

Treasuries are rebounding this morning after a week that saw the 10YR Note lose 25 basis points from last Friday's close. Traders are split regarding whether this constitutes the beginning of a new trading range for the benchmark or whether today's supportive bid is simply short covering in front of the weekend. If the latter is true Treasuries might turnaround as the day wears on.

Protected Information To Be Disclosed Only In Accordance With Protective Order

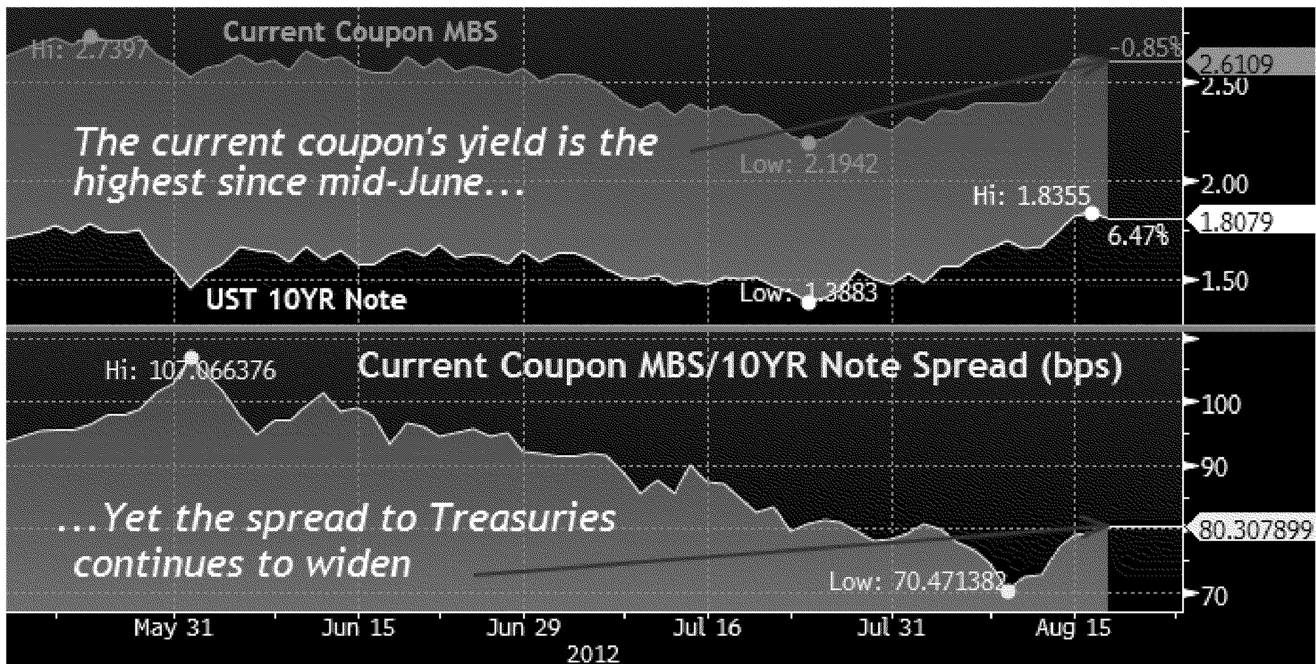
Exhibit
0002

Credit spreads are generally wider today. 3-month libor was set higher at 0.43450 in the morning fixing and swap spreads/Tsy are incrementally wider.



The Treasury Department's announcement earlier today regarding changes to the Preferred Stock Purchase Agreements (PSPAs) that are intended to expedite the wind-down of Fannie Mae and Freddie Mac is having more of an immediate impact on agency debt than MBS. While spreads across the curve are tighter, the farther out the maturity, the tighter the spread. 2- and 3-year bullets are 1.0 to 1.5 bps tighter, 5-year paper is 2.0-3.0 bps tighter and the 10YR Freddie Mac Reference Note (FHLMC 2.375% 1/13/2022) is 6 bps tighter. The rationale is that as the Enterprises wind down there will be less longer term debt issued, leaving investors to fight over existing supply. Also, it is more likely that buyers will squirrel away existing holdings, reducing the float of available supply in the secondary market. The Fannie Mae 3YR Benchmark Note that was priced +12.0 bps/Tsy earlier this week is currently quoted 9.5 – 8.5 on the broker screens.

The reaction in MBS trading has been almost a non-event. The reason is that the Enterprises still remain the primary conduit for mortgage finance, so production is unlikely to be effected by today's announcement. The current coupon MBS continues to widen vs. long Treasuries this morning even though the current coup's yield is the highest in two months. The takeaway is that investors are still cautious about catching a falling market and that the 10YR Note could just as easily be above 2.00% a week from now as below 1.70%.

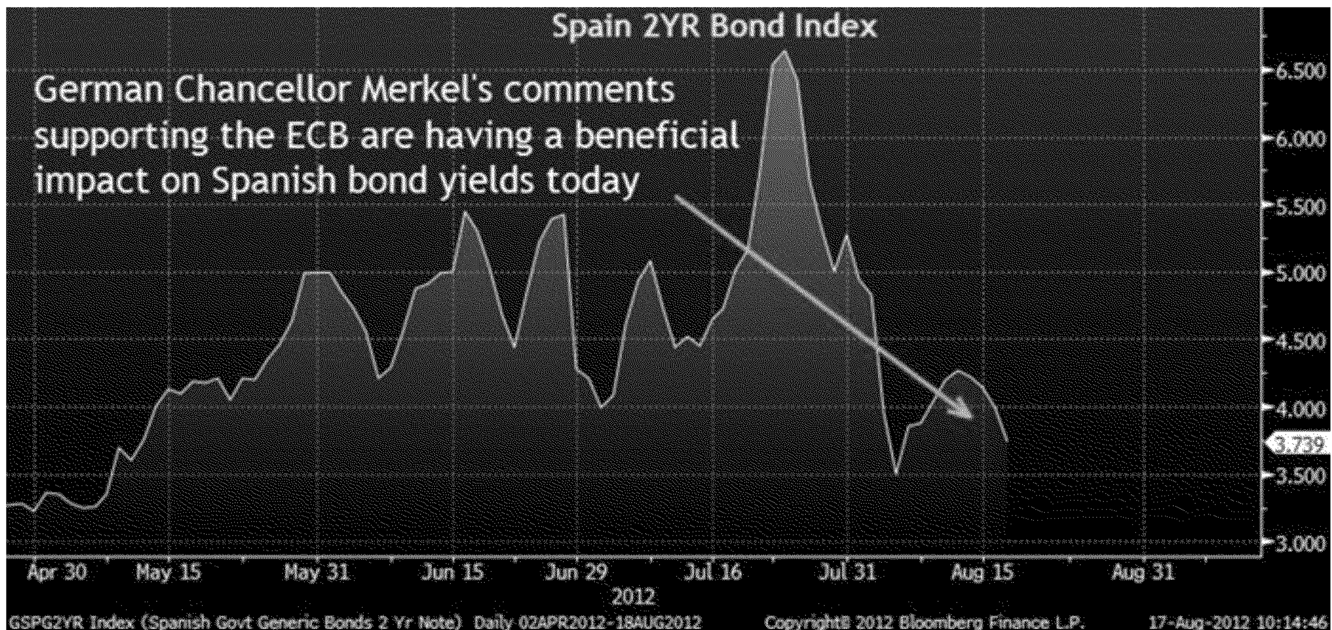


The coupon stack reflects the price action in Treasuries; cusp coupons are higher while higher coups are close to unchanged. One exception is the Freddie 6.00% coup, but the spike higher may be more a function of a lack of supply than anything else.

Fannie Cpn.	Px.	Change
3.00	102-06	+6/32
3.50	104-22	+4/32
4.00	106-10	+3/32
4.50	107-18	+1/32
5.00	108-20	+1/32
5.50	109-12	+1/32
6.00	110-00	+1/32
Freddie Cpn.	**Px.**	**Change**
3.00	101-28	+5/32
3.50	104-16	+4/32
4.00	106-02	+4/32
4.50	106-27	+1/32
5.00	107-30	+2/32
5.50	109-00	+3/32
6.00	109-26	+7/32

EU…Developments today:

- German Chancellor Angela Merkel's comments supportive of the ECB yesterday happened concurrent with the close of European markets and thus were not fully priced in when trading ceased yesterday. The knock-on effect is showing up in today's prices, though, and yields for Spanish, Portuguese and Italian sovereign debt are trending lower.



- According to press reports Merkel may also be reevaluating her stance against modifying terms for the Greek bailout. While Germany is still likely to hold a strident line on austerity measures, easing timelines for those moves will allow the situation to play out over a longer span, which in turn takes out some of the urgency to move into "safe" assets such as German bunds and U.S. Treasuries.
- The euro is trading lower at 1.2304 vs. the dollar.

Later…Traders are having to recalibrate their thinking regarding "over the weekend" headline risk. Whereas that overhang has been supportive of Treasury yields for much of this year the past month has shown that the needle can point in more than one direction. Look for agency debt spreads to tighten on the Treasury Dept. news but for yields to rise as investors may decide to lighten up on Treasuries as the 10YR Note struggles to establish a support level.

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Exhibit B

Office of Systemic Risk and Market Surveillance

Capital Markets Weekly – 8/19/2012

Robert F. Hynes

Treasuries extended their retreat as hopeful news from Europe dimmed the safety bid. The 10YR Note closed out the week above 1.80% for the first time since May and the 3YR Note's closing yield on Thursday (0.4248%) was the highest since April 12th. On Friday GSE debt had its biggest one-day tightening since 2008 after the Treasury Department announced plans to accelerate the wind-down of Fannie Mae and Freddie Mac, instantaneously making outstanding issues more valuable given the prospect of less forward supply. MBS spreads had a more muted reaction.

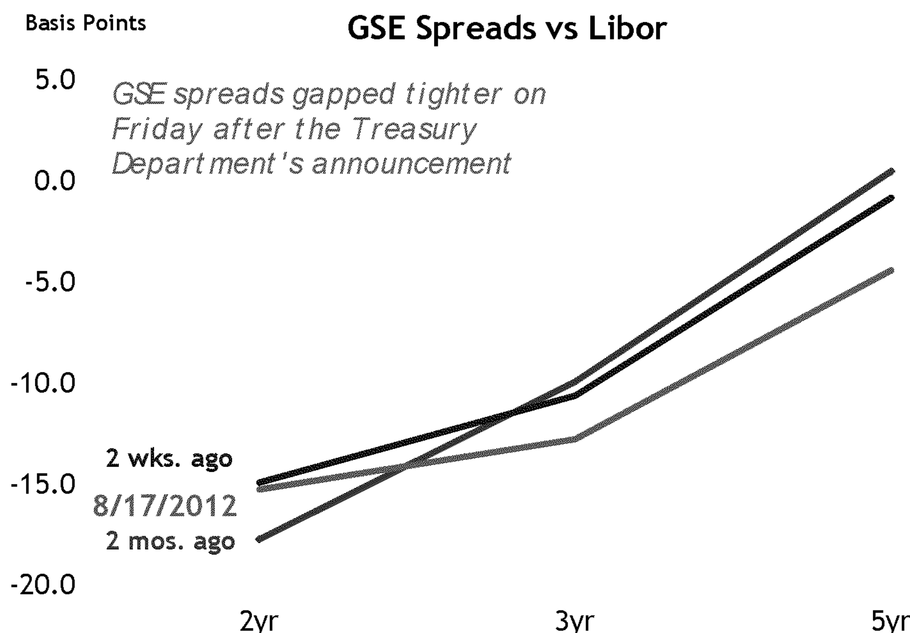
Spread Monitor

	GSE Spreads to Treasuries (in basis points)					GSE Yields to Maturity				
	2yr	3yr	5yr*	10yr	30yr	2yr	3yr	5yr	10yr	30yr
08/10/2012	0.5	6.9	23.0	28.1	22.1	0.27	0.44	0.94	1.94	2.97
08/13/2012	0.5	5.8	22.5	27.6	21.5	0.27	0.43	0.93	1.94	2.97
08/14/2012	1.3	7.6	21.0	26.6	19.6	0.29	0.47	0.96	2.00	3.03
08/15/2012	0.6	6.1	21.2	25.9	18.7	0.29	0.48	1.01	2.08	3.11
08/16/2012	0.7	7.1	21.0	26.3	20.7	0.30	0.50	1.03	2.10	3.16
08/17/2012	0.5	4.5	16.1	17.7	9.5	0.29	0.46	0.96	1.99	3.03
1-week Chg	**0.0**	-2.4	-6.9	-10.4	-12.6	**+2.0**	**+2.0**	**+2.0**	**+5.0**	**+6.0**

***Transitioned to FNMA 0.875% 8/28/2017 as reference security for 5-year agency.**

Highlights

- Treasury yields rose to highest levels since April/May on continued optimism on Europe.
- GSE debt spreads gapped tighter after Treasury Department announcement sparked buying.
- MBS spreads widened early in the week before narrowing Friday, but performance lagged debt action.
- Fannie Mae priced a $4B Benchmark Note +12.0 bps/Tsy that tightened to +6.3/Tsy on Friday.



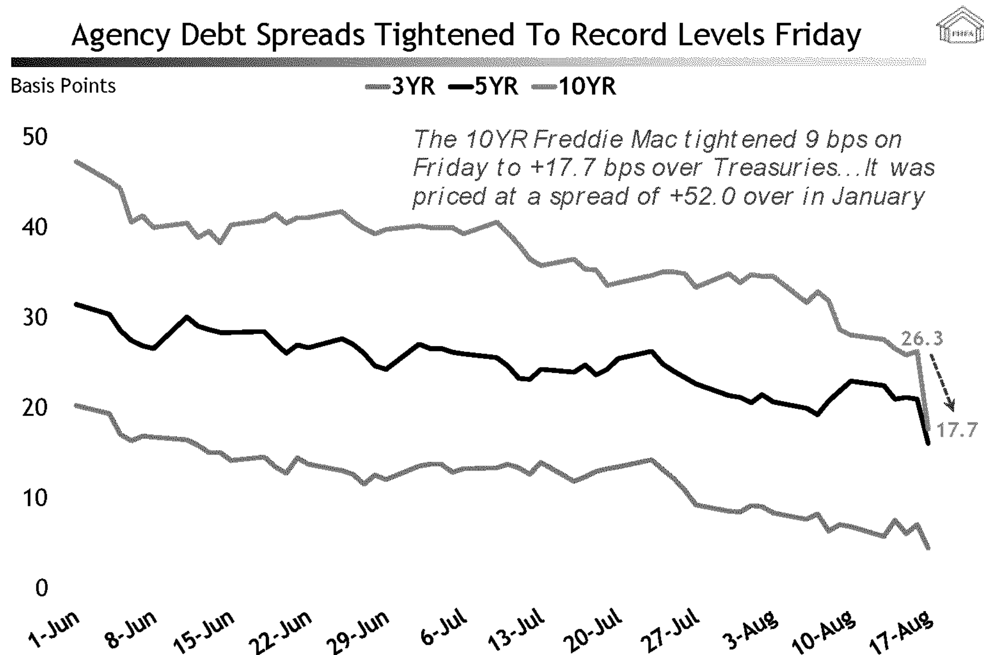
Sources: Bloomberg, FINRA TRACE (Trade Reporting and Compliance Engine) data, Fidelity Capital Markets

Market Drivers

- Treasuries will continue to be pressured if domestic data prints better than expectations.
- GSE debt spreads should stay tight given diminished forward supply on faster wind-down plans.
- Agency MBS spreads may not tighten as much as debt due to other inputs in valuations.
- FHLBanks has the option to price a Global Bond.

Chart of the Week – Last Call…Concern About Future Supply of GSE Debt Sparked Friday's Spread Collapse

Friday's grab-a-thon for agency debt was reminiscent of the dramatic tightening that occurred in late 2008 after the Fed announced it would be purchasing agency debt and MBS in the open market in what has since come to be known as QE1. This time around the tightening was caused by the Treasury Department's announcement that it would accelerate the wind-down of the Enterprises. For agency debt investors that points to fewer remaining new issues since the lifespan of Fannie/Freddie just got shorter.



Agency spreads have been tightening all year due to investors designating them as safe asset cohorts to Treasuries but the prospect of fewer years of new issues remaining served as a "last call" of sorts, particularly for longer maturities that may not be tapped again. The Freddie Mac 10YR Reference Note (FHLMC 2.375% 1/13/2022) warrants special since its closing quote on Friday left it 35 bps tighter than where it was priced in January, but all issues benefited to varying degrees. The "legacy 30YR" Freddie Mac 6.25% 7/15/2032 that rarely trade (issues with dollar prices of 149-00 tend to lose liquidity) saw round lots taken down 11 bps tighter than the previous day, with a yield only 6 bps over the reference 30YR Bond. Expect price talk for any future agency debentures to be commensurately tighter.

The Week Ahead

Treasuries could get hit again tonight (Sunday) following a *Der Spiegel* report that the ECB may look to "cap" sovereign bond yields with open-ended purchases, but there is another story circulating that Germany is balking at extending austerity targets for Greece, which could revive the "safe" asset rally. We will have an update in our Monday morning report.

Message

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Sent: 8/19/2012 11:24:48 PM
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Subject: Capital Markets Weekly from the Office of Systemic Risk and Market Surveillance
Attachments: Capital Markets Weekly-187 08192012.pdf

Attached is this week's edition of Capital Markets Weekly.

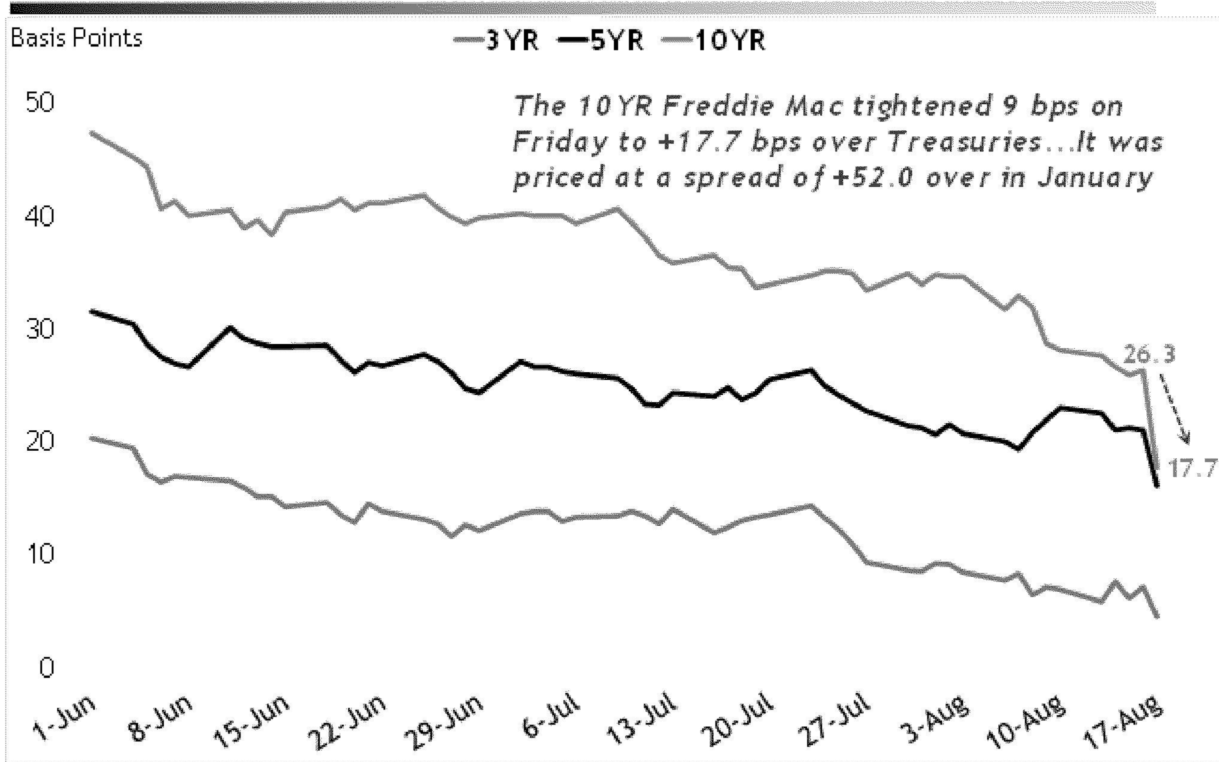
The Week Ahead

Treasuries could get hit again tonight (Sunday) following a Der Spiegel report that the ECB may look to "cap" sovereign bond yields with open-ended purchases, but there is another story circulating that Germany is balking at extending austerity targets for Greece, which could revive the "safe" asset rally. We will have an update in our Monday morning report.

Chart of the Week – Last Call…Concern About Future Supply of GSE Debt Sparked Friday's Spread Collapse

Spreads (bps)	2yr	3yr	5yr	10yr	30yr
8/16/2012	0.7	7.1	21.0	26.3	20.7
8/17/2012	0.5	4.5	16.1	17.7	9.5
1-Day Change	**-0.2**	**-2.6**	**-4.9**	**-8.6**	**-11.2**

(more inside report)



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