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

LEHMAN BROTHERS INTERNATIONAL (EUROPE) (in administration), Plaintiff, - against - AG FINANCIAL PRODUCTS, INC., Defendant.	Index No. 653284/2011

<u>POST-TRIAL RESPONSE BRIEF OF AG FINANCIAL PRODUCTS INC.</u>

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PRELIMINARY STATEMENT

As Assured demonstrated in its opening brief, the evidence at trial established that Assured determined its Loss reasonably and in good faith by following the language of the Agreement and calculating the benefit of the bargain that it lost when LBIE defaulted on the Transactions.[1] Having failed to satisfy its burden at trial to show that Assured breached the Agreement, LBIE relies in its opening brief on a distorted and incomplete summary of the record, ignoring key evidence that is devastating to its claims (including inconsistencies in the testimony of its own experts), and cherry-picks from purported custom and practice evidence that is anything but uniform. Critically, LBIE also ignores the contractual language and actual economic bargain struck by the parties, and it fails to provide a basis for the Court to instead adopt LBIE's damage calculation, which relies on a litigation-driven, after-the-fact model that there is no evidence anyone ever used in the real world, especially in 2009.

In its opening brief, LBIE invents implausible and unsubstantiated explanations for why no one was willing to pay any amount to replace LBIE in the Transactions and face Assured as the seller of credit protection after LBIE defaulted in September 2008, but the trial record is clear: LBIE tried for months to novate the Transactions, but failed to do so; LBIE tried to create a complex structured assignment called "Project Rioja" to attract interest, but again failed; and, after the termination, Assured ran a robust auction, and not one of the dealer banks that participated bid on even one of the Transactions. The only plausible conclusion to draw from these indisputable facts is that no market participant in 2009 ascribed any value to the Transactions, much less the hundreds of millions of dollars of value that LBIE claims as

[1] All capitalized terms not defined in this brief have the meaning ascribed to them in Assured's opening brief. Def.'s Post-Trial Br., D.I. 779 (Apr. 22, 2022) ("Assured Br.").

damages in this lawsuit.

After receiving no bids at the auction, Assured calculated its Loss. The Court observed in its summary judgment decision that Assured's methodology "appears on its face to be a reasonable method for calculating the value to Assured of the terminated Transactions."[2] That is because Assured followed the contractual language and determined its "loss of bargain" by calculating the value to it of the economic bargain it lost as a result of LBIE's default. To do so, Assured netted the present value of the aggregate premium payments LBIE would have owed over the life of the Transactions against the present value of the amounts Assured would have been required to pay to cover expected shortfalls in interest and principal payments on the reference obligations (which it determined based on its regular-course-of-business models).

For the two ABX transactions, Assured determined that its payments to LBIE would have exceeded the amount of premium payments LBIE would pay Assured, that termination of the ABX Transactions therefore resulted in a net gain for Assured, and that Assured owed LBIE the amount of that net gain (approximately $24 million, which Assured was relieved of paying as a result of the termination). For the other 26 Transactions, the reference obligations had remained investment grade throughout the worst of the financial crisis, and Assured's internal models did not project that any payments would ever be owed to LBIE. For those Transactions, termination resulted in a loss to Assured, and Assured determined that LBIE owed it the present value of the premium payments that LBIE was relieved of making as a result of the termination.

LBIE's opening brief would have you think that this case is about an entirely different set of transactions and agreements than those the parties actually entered into. LBIE ignores that the

[2] *Lehman Bros. Int'l (Europe), In Administration v. AG Fin. Prods., Inc.*, No. 653284/2011, 2018 WL 3432593, at *18 (Sup. Ct. N.Y. Cnty. July 2, 2018) (hereinafter "D/O").

CDS here had non-standard terms and did not require collateral posting or cash or physical settlement, and that all of these differences affected the contracts' value (as LBIE's own internal memos and communications recognized in 2008 and 2009). LBIE also avoids addressing the facts that Assured did not trade CDS the way dealer banks do, that CDS in general did not trade in a liquid market with executable prices, and that in 2009 there was no interest from any other market participants in entering into these transactions with Assured, because they did not believe these Transactions had any value and did not want to purchase any CDS from a monoline.

LBIE's focus on the parties' selection of a "standard unamended" termination provision misses the point. Assured had no reason to seek changes to the Loss definition because it plainly states that Assured "need not" use market prices, and it grants Assured, as the Non-Defaulting Party, broad discretion in calculating its Loss, including, as this Court has said, "the discretion to make the determination as to whether use of market prices to calculate Loss is appropriate in a particular case."[3] The Loss definition [does not] require that any particular methodology be used. Instead, it simply permits the Non-defaulting Party to calculate what the value of its economic bargain would have been if the Defaulting Party actually performed its obligations. That is what Assured did, and what LBIE's damages calculation does not even purport to do.

LBIE disregards the parties' actual contractual terms and economic bargain in favor of asking the Court to impose a purported "uniform market practice," but the trial evidence showed there was no relevant uniform market practice—and certainly none requiring a party to calculate a market price that has no relationship to its economic bargain. As this Court held at summary judgment (and the First Department affirmed), custom and practice evidence "*may*" be one factor that is informative in assessing reasonableness, but only if there is a "uniform or highly

[3] D/O at *12.

consistent practice" for acting "under similar circumstances" that is known to the defendant.[4] Far from establishing such a practice "beyond doubt," as LBIE asserts, the evidence showed that the large and diverse marketplace never coalesced around a single, fixed, and uniform practice for calculating Loss. To the contrary, the market understanding and practice was that Loss afforded the Non-defaulting Party substantial flexibility and discretion.

Nor does the evidence back up LBIE's refrain that Assured's calculation was "subjective and self-serving." Every estimation of the future performance of complex financial products is subjective in that it requires the application of judgment—this is true of both Assured's methodology and the litigation-driven models that LBIE's expert advanced. But LBIE ignores the extensive evidence demonstrating the reliability of Assured's methodology and showing that the judgments Assured made were well-supported. This includes evidence that Assured's calculations followed the documentation and were derived from its contemporaneous business records (without any regard for whether those numbers were favorable to its position in this litigation or not), that Assured used the same methodology for multiple business purposes, that its methodology was subject to extensive internal and external scrutiny and verification (including by Assured's Board of Directors and its independent auditors, PwC), and that its modeling judgments and ultimate calculations were consistent with contemporaneous judgments made by independent rating agencies (Standard & Poor's ("S&P") and Moody's). In contrast, the damages model created by LBIE's expert for this lawsuit is the epitome of self-serving and unreliable: it was designed solely to justify a windfall recovery for LBIE, there is no evidence

[4] D/O at *10 & n.11 (emphasis added), *14 ("[E]vidence of market practice would not be admissible to aid in understanding a contractual term unless it was fixed and notorious.") (first citing *L. Debenture Tr. Co. of N.Y. v. Maverick Tube Corp.*, 595 F.3d 458, 466 (2d. Cir. 2010); and then citing *J.P. Morgan Inv. Mgt. Inc. v. AmCash Grp.*, 106 A.D.3d 559, 559–60 (1st Dep't 2013)).

that it was ever used by any market participants for any purpose ever (and certainly not in 2009), and it suffers from many glaring defects.

In sum, LBIE does not come close to satisfying its burden to prove that Assured's calculation of Loss was not done reasonably or in good faith. For all the reasons explained further below, the Court should enter judgment for Assured, dismiss LBIE's claim and award Assured damages for its counterclaim.

ARGUMENT

I. LBIE's Opening Brief Misstates The Applicable Law

While LBIE stresses the importance of interpreting the 1992 ISDA Master Agreement so as to promote "legal certainty,"[5] LBIE asks this Court to accept novel, litigation-driven legal interpretations and arguments that, if accepted, would seriously undermine that goal. The way to promote legal certainty is to apply well-settled New York law and follow the language of the Agreement, which is exactly what Assured urges here—and what LBIE's approach fails to do.[6]

The sole issue at trial was whether Assured's Loss calculation was reasonable.[7] The Court already ruled that LBIE, as the plaintiff, bears the burden of establishing that Assured's Loss calculation was unreasonable "[d]espite the discretion afforded to [Assured] under the parties' agreements to calculate its loss."[8] This question is governed by the New York standard

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[5] Pl.'s Post-Trial Br. at 22, D.I. 777 (Apr. 22, 2022) ("LBIE Br.") (citation and quotation marks omitted).

[6] Assured Br. at 40–43; *see also In re Lehman Bros. Holdings Inc.*, 2015 WL 7194609, at *10 (S.D.N.Y. Sept. 16, 2015) (hereinafter "*Intel*") (observing that "[o]n the face of the ISDA Master's definition of 'Loss,' [the Non-defaulting Party] has broad discretion in determining its Loss, so long as its methodology is reasonable," and finding that there is "nothing in the text of the definition of Loss that explicitly mandates any particular calculation method or otherwise modifies the plain meaning" of the agreement).

[7] D/O at *11, *14.

[8] *Lehman Bros. Int'l (Europe) v. AG Fin. Prods., Inc.*,168 A.D.3d 527, 528 (1st Dep't 2019); *see also* Order Determining Burden of Proof and Various Evidentiary Issues at 1, D.I. 774 (March 1, 2022); Feb. 28, 2022 Hr'g Tr. 4:18–5:17. LBIE continues to attempt to improperly shift this

for determining reasonableness for any contract—whether the actions taken by Assured were consistent with what a reasonable Non-defaulting Party in Assured's position would have done in light of the circumstances facing Assured at the time.[9] LBIE ignores but does not dispute this standard. Instead, LBIE either misstates the governing law or relies on inapposite cases.

First, LBIE argues that its litigation-driven, after-the-fact purported "market" valuation is the *only* objectively reasonable methodology that could have been applied.[10] In doing so, LBIE suggests that "objective reasonableness" requires something more than the ordinary test of reasonableness under New York law.[11] But it does not. It is well-settled New York law that there is only one standard for reasonableness, which is already an objective standard and which permits consideration of a party's own facts and circumstances.[12] LBIE's contention that Assured's calculation cannot satisfy this standard because it was "subjective" is mere word play.[13] As LBIE's own expert conceded, all models are subjective in the sense that they require the application of judgment—this applies equally to Assured's regular-course-of-business model and LBIE's litigation-driven model. The evidence at trial showed that Assured's calculation was reasonable because its model was reliable and its judgments were sound, while LBIE's model was not, for the reasons discussed in § IV.

The cases cited by LBIE, which were discussed in the Court's summary judgment

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burden to Assured by arguing that Assured must prove the reasonableness of its Loss calculation with evidence of other similar Loss calculations, but Assured, as the defendant, has no such burden.

[9] D/O at *11, *14; *see also* Assured Br. at 39 (citing cases).

[10] LBIE Br. at 20, 29 (asserting that "[Assured]'s failure to calculate Loss by reference to available market prices was a breach of contract" because it was not "objectively reasonable").

[11] *Id.* at 1 ("The issue before this Court is whether [Assured's Loss calculation] . . . was objectively reasonable and made in good faith") (emphasis omitted); *see also id.* at 22–24.

[12] Assured Br. at 39.

[13] LBIE uses the word "subjective" or "subjectively" 23 times to refer to Assured's Loss calculation in its opening brief.

decision, do not hold otherwise. *MBIA* and *Christie's* confirm the existence of this single New York standard of reasonableness.[14] And *Hoag* merely held that "[i]n determining whether conduct is objectively reasonable, industry norms *may* be appropriately considered," but as this Court previously held, LBIE must first prove that there was a "uniform or highly consistent [market] practice" that was "fixed and notorious,"[15] and even then a departure from that market practice by Assured could be reasonable depending on the circumstances.[16] For the reasons explained in Assured's opening brief and below, LBIE has failed to prove the existence of any such market practice, much less that Assured knew of and unreasonably departed from it.[17]

Second, LBIE incorrectly argues that New York law requires damages to be determined using "fair market value" as of the date of breach.[18] New York law measures damages based on loss of bargain, which means putting the non-breaching party in the same economic position he or she would have occupied had the breaching party performed the contract.[19] As part of this assessment, New York courts have recognized that "the value of a security may not be equivalent to its market price" in a dislocated market, which is why, under such circumstances, a DCF

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[14] *MBIA Ins. Corp. v. Patriarch Partners VIII, LLC*, 842 F. Supp. 2d 682, 704–05 (S.D.N.Y. 2012); *Christie's Inc. v. SWCA, Inc.*, 22 Misc. 3d 380, 383–84 (Sup. Ct. N.Y. Cnty. 2008) (observing that a contractual requirement to "reasonably determine" something suggests that the parties intended for an objective standard of reasonableness to apply to that determination).
[15] D/O at *14; *see also id*. at *10 n.11 (clarifying that "evidence of market practice would not be admissible to aid in understanding a contractual term unless it was fixed and notorious").
[16] D/O at *11 (noting that "in determining whether conduct is objectively reasonable, industry norms *may* be appropriately considered.") (emphasis added) (citing *Hoag v. Chancellor, Inc.*, 246 A.D.2d 224, 231 (1st Dep't 1998).
[17] *See infra* § III; *see also* Assured Br. at 43–59.
[18] LBIE Br. at 24–26.
[19] *See* Assured Br. at 40–41. *Anthracite*, on which LBIE has repeatedly relied, *see* LBIE Br. at 22–23, 26, 28, similarly recognizes that the definition of Loss in the 1992 Master Agreement was intended to be "illuminated by reference to the general common law (or New York law)" with the purpose of "identifying the [N]on-defaulting [P]arty's loss of bargain." *Anthracite Rated Invs., Ltd. v. Lehman Bros. Fin. S.A. in Liquidation*, [2011] EWHC (Ch) 1822 [117] (Eng.).

analysis is a "generally accepted method for valuing an asset."[20] None of the case law that LBIE cites holds otherwise.

LBIE misplaces reliance on Justice Friedman's decision in *UBS* in arguing that damages must be determined using "market value" as of the date of breach. But the *UBS* case did not involve interpretation of the Loss definition or even an ISDA contract at all.[21] The non-ISDA contract at issue in *UBS* contained a specific formula for calculating liquidated damages, and the disputed issue in that suit—namely, which transactions should have been included in a collateral call calculation—have no relevance to this case.[22] For the same reason, *UBS* also does not support LBIE's argument that the failure of the Market Quotation Auction in September 2009 is "irrelevant to the value of the trades on July 23, 2009, which is undisputedly the relevant valuation date."[23] LBIE omits the actual language in the Loss definition, which permits Assured to calculate its loss as of the Early Termination Date or "'*as of the earliest date thereafter as is reasonably practicable*.'"[24] The Court already rejected a similar argument by LBIE regarding nearly identical language in the Market Quotation definition, which similarly provided for Assured to conduct its auction "as soon as reasonably practicable after the Early Termination Date."[25] Specifically, LBIE argued that Assured breached the Agreement because it "unduly delayed" its auction until September 2009, but the Court rejected that argument and dismissed LBIE's claims related to the auction in their entirety.[26] Given that the Court already found the

[20] *See* Assured Br. at 41.
[21] LBIE Br. at 24–26.
[22] Decision and Order After Trial at 12, *UBS Secs. LLC et al. v. Highland Cap. Mgmt., L.P. et al.*, No. 650097/2009, (Sup. Ct. N.Y. Cnty. 2019), NYSCEF Doc. No. 641.
[23] LBIE Br. at 41.
[24] JX-01 at 15 (1992 ISDA Master Agreement) (emphasis added).
[25] *Id*. at 16.
[26] D/O at *7–8.

timing of the auction in September 2009 to be "as soon as reasonably practicable" and that Assured was only required to determine Loss *after* the auction failed, it makes no sense for LBIE to argue that determining Loss as of September 2009 was somehow unreasonable.[27]

LBIE also relies on other cases that did not involve ISDA agreements, and that are also inapposite. In *Sharma*, there was no dispute that the assets in question, tankers, had a "determinable market value," but the debtors in that case sought to recover not only their market price but also damages equal to the profits that they would have earned from the tankers in future years, which the court rejected.[28] In *Schonfeld*, the issue was whether a television station that never successfully launched could recover damages for lost income-producing assets in the form of programming licenses. The licenses did not have an easily ascertainable market value because there was no "standardized market or exchange where [the television station] could have sold its contract rights," and where they "would change hands between a willing buyer and a willing seller," although there had been a firm offer to purchase one of the two contract rights at issue, which the *Schonfeld* court used as a "benchmark" to assess the market value of both contracts.[29]

These decisions do not support LBIE's position in this lawsuit because the evidence at trial showed that the Transactions did not have a "determinable market value." There were no bids on the Transactions at the Market Quotation auction or during LBIE's repeated efforts at

[27] The Court's comments regarding "hindsight" evidence in its summary judgment decision are also irrelevant to this issue, as they did not relate to the timing of Assured's Loss calculation, but rather to evidence that Assured proffered from nearly a decade after LBIE's default that Assured's calculations had proven to be far more accurate than the litigation-driven calculations put forward by LBIE in this lawsuit. *See* D/O at *19.
[28] *Sharma v. Skaarup Ship Mgmt. Corp.*, 916 F.2d 820, 825 (2d Cir. 1990). LBIE also cites *White v. Farrell*, 20 N.Y.3d 487, 494 (2013), but the issue in that case was whether to measure damages as of the date of the breach of contract to purchase a piece of land or as of the date the land was resold. *Id*. at 489.
[29] *Schonfeld v. Hilliard*, 218 F.3d 164, 177–78, 182–83 (2d Cir. 2000).

novation. In addition, there were no market prices available for the actual Transactions here, as LBIE's experts conceded. Instead, the purported market price data cited by LBIE relates to CDS with materially different terms or to completely different instruments altogether, and, because of market dislocation at the time, those proxies are irrelevant to the actual economic value of the Transactions in this case.[30]

LBIE also cites three cases that involved ISDA agreements but which do not support its position in this case. In *Credit Lyonnais*, the court held that a Market Quotation auction was conducted in bad faith because the bank that held it improperly tried to influence the bidders.[31] That decision is only relevant in that it supports Assured's position that the steps LBIE took in soliciting indicative bids—including by redacting information about Assured being the counterparty and obtaining one set of bids from a former colleague who pretended not to know the identity of Assured despite having been responsible for analyzing the Transactions and trying to novate them while at LBIE—were plainly improper. In contrast, *Credit Lyonnais* has no bearing on Assured's Market Quotation auction, which the Court held at summary judgment was designed and executed reasonably and in good faith.[32] The other cases, *Bank of America* and *Ballyrock*, are both disputes about whether "priority provisions" of the ISDA agreement could be enforced under the Bankruptcy Code. Neither involved the valuation of transactions executed under an ISDA agreement, let alone the Loss definition, and both are irrelevant to this case.[33]

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[30] LBIE's main response that "[t]here is no evidence . . . that the markets for CDS were 'disrupted' such that it was impossible to determine a market price," LBIE Br. 39, fails to understand the point that market disruption and dislocation in 2009 made market prices, where available, an unreliable and inappropriate indicator of value.

[31] *The High Risk Opportunities Hub Fund Ltd. v. Lyonnais*, No. 600229/00, 2005 WL 6234513, at *5, 7–8 (Sup. Ct. N.Y. Cnty. July 6, 2005).

[32] D/O at *7.

[33] In *Bank of America*, a dispute between two big banks, the court briefly described the Loss definition as background, but then made clear that while Market Quotation was used for some of

Notably, LBIE omits any meaningful reference to the *Intel* decision, which specifically addresses the purposes of the Loss definition in the 1992 ISDA Master Agreement, and makes clear that there is "no single 'correct' methodology for calculating Loss," which is why "[N]on-defaulting [P]arties are afforded discretion in choosing a method to calculate Loss, so long as such calculation is ultimately performed 'reasonably and in good faith.'"[34] In fact, the *Intel* court rejected the argument made by LBIE here (and made in that case by the U.S. Lehman entities) that the counterparty was required to use market quotations and prices to determine its Loss. In doing so, the *Intel* court, citing the ISDA User's Guide, said that "Loss is intended to provide parties flexibility in selecting a method to calculate their Early Termination Payments,"[35] and held that "the descriptions of Loss in the ISDA Master and the ISDA User's Guide are *not consistent with a mandatory methodology for calculating Loss*."[36]

Lastly, despite arguing that the sole reasonable measure of Loss is a market price, LBIE takes the internally inconsistent position that, as a matter of law, Assured's creditworthiness should not be considered in the valuation of the Transactions. This is nothing more than LBIE trying to have its cake and eat it too: LBIE's own experts admitted that market prices for CDS

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the Transactions and Loss was used for others, "the method of calculation has no material effect on the dispute here." *Lehman Bros. Special Financing Inc. v. Bank of Am., N.A.*, 553 B.R. 476, 481, 485 n.28 (Bankr. S.D.N.Y. 2016). The *Ballyrock* case does not even mention the Loss definition or address the use of market prices to determine Loss. *Lehman Bros. Special Fin. Inc. v. Ballyrock ABS CDO 2007-1 Ltd.*, 452 B.R. 31 (Bankr. S.D.N.Y. 2011).

[34] *Intel*, 2015 WL 7194609, at *19. This conclusion is consistent with the history and purpose of the Loss provision, which was designed to give significant discretion to the Non-defaulting Party. *See* Assured Br. § VIII.A.3.

[35] *Intel*, 2015 WL 7194609, at *11. ISDA's own amicus brief in the *Intel* case explains that the Loss provision in the 1992 ISDA Master Agreement was crafted in order to "allow flexibility" and that Loss is "open to a universe of calculation methods." *See* ISDA's Amicus Brief in Supp. of Def. Intel Corp.'s Mot. for Summ. J. at 3, 15, ECF No. 57-2, *Lehman Bros. Holdings Inc. v. Intel Corp. (In re Lehman Bros. Holdings Inc.)*, Case No. 13-1340-scc (Bankr. S.D.N.Y. Jan. 20, 2015).

[36] *Intel*, 2015 WL 7194609, at *15 (emphasis added).

always took counterparty credit risk into account.[37] LBIE's invocation of cases that say "economic inability to perform contractual obligations, even to the extent of insolvency or bankruptcy, is [] not a valid basis for excusing compliance" is also irrelevant to evaluating Assured's Loss calculation.[38] Assured did not discount its Loss calculation based on its creditworthiness or cite that as an excuse for not complying with the Agreement, which were the issues in the three cases that LBIE cites.[39] It was *LBIE* that defaulted on the contract due to its "economic inability to perform." Assured then calculated its Loss based on what was needed to put it "in the same economic position it would have been in had both parties fully performed," consistent with the holdings in *Adar Bays* and *Anthracite*, cases that LBIE itself cites.[40]

The market's perception of Assured's creditworthiness at the time and the resulting reluctance of dealer banks to add monoline exposure, as demonstrated by the evidence[41] and

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[37] *See* Trial Tr. 140:13–141:12 (Rahl); *see also id.* at 927:12–928:1 (Bruce); *id.* at 1445:15–1446:9 (Niculescu); *id.* at 609:8–610:1 (Viegas).

[38] LBIE Br. at 26–27.

[39] LBIE Br. at 26–27 (first citing *In re Highland Superstores, Inc.*, 154 F.3d 573, 580 n.9 (6th Cir. 1998) (addressing collectability in making a damages calculation); and then *Kucin v. Devan*, 251 B.R. 269, 273 (D. Md. 2000) (same); and then citing *Peregrine Fixed Income Ltd. v. Robinson Dep't Store Public Co.* [2000] EWHC (Comm) 99 [30] (Eng.) (finding that the contract's value cannot be discounted based on the "chance that the obligor will fail to perform")).

[40] *Adar Bays, LLC v. GeneSYS ID, Inc.*, 37 N.Y.3d 320, 339 n.8 (2021); *see also Anthracite*, [2011] EWHC at [116].

[41] AX-40005 at 1 (BNP Paribas Email to Henderson) (BNP has "simply no appetite to increase [its] exposure to monolines"); AX-40003 at 1 (UBS Email to Henderson) (UBS was "unable to obtain internal Credit approval to face [Assured] on bought cds protection"); AX-40001 at 1 (Citibank Email to Henderson) (Citibank "had a number [of] clients very interested in buying protection on []quite a few of the line items that were auctioned, but none of them were prepared to step into the existing contracts and face Assured Guaranty [due] to counterparty risk"). In order to "complete[] the narrative" about the indicative bids, Trial Tr. 3524:21 (Pirrong), the Court allowed Assured to present evidence that banks, even some of the same banks that submitted indicative bids to LBIE, declined to bid in Assured's Market Quotation auction.

reflected in admissions made in LBIE's own contemporaneous assessments,[42] is relevant only (but importantly) to understanding why no replacement transactions were available—that is, to understanding why LBIE's attempts at novation failed, why no one wanted to bid on the Transactions at the Market Quotation auction, and ultimately why these contracts carried no real-world value for anyone looking to step into LBIE's shoes.[43] LBIE's attempt to blame Assured for the failed novation—claiming "it was undisputed at trial that AGFP ***never*** agreed to approve such a novation"[44]—is jaw-dropping. There is no evidence that any third party was prepared to enter into a novation, let alone that Assured prevented a willing third party from doing so. Nor is there any support for LBIE's suggestion that Assured was prohibited from entering into novations of the Transactions. Assured's then-president testified that a novation of these Transactions would not be affected by the risk limits set by Assured as it would have been an assignment of an existing trade.[45] He also testified that he flew to London on the day of the auction with full authority to enter into any bids received.[46]

[42] JX-67 at 2 (Valuation Memorandum) (explaining that the value of the contracts was "significantly diminish[ed]" due in part to Assured's counterparty credit risk and that the appetite of other market participants to step into LBIE's shoes was "severely limited" because of it).
[43] Assured Br. at 68–72. The DCF analysis that Assured conducted to determine its Loss also revealed that the Transactions were not valuable to LBIE due to the strength of the underlying reference obligations. This was consistent with the hold-to-maturity valuation that LBIE itself did in 2008. JX-67 at 2, 3 (Valuation Memorandum); AX-30010 at 3–5 (LBIE Slide Deck on Credit Exposure to Assured). Any party looking to step into LBIE's shoes would likely have conducted a similar type of analysis. Further, for the hypothetical replacement transaction valuation that Niculescu does, the market's perception of Assured's credit risk is also critically relevant because it would have to be factored into what a third-party would be willing to pay to step into LBIE's shoes and enter into agreements with Assured.
[44] LBIE Br. 13.
[45] *See* Trial Tr. 2366:15–2368:2 (Schozer).
[46] *Id*. at 2209:24–2210:4 (Schozer) (describing how he had been ready to "authorize executing the transaction" if there had been any bids); *see also id*. at 2367:1 (Schozer).

II. LBIE's Opening Brief Is Premised On Ignoring The Contractual Language, Evidence Of Assured's Economic Bargain And That LBIE's Default Entitled Assured To Receive The Benefit Of That Bargain After Termination

In its presentation of the Agreement, LBIE entirely ignores the contractual terms and other evidence that explain the economic bargain that the parties struck, even though *the* question for trial was whether Assured's valuation of that bargain was reasonable.

As Assured demonstrated in its opening brief, to calculate the termination amount, Assured followed the terms of the parties' Agreement. LBIE and Assured selected Second Method and Market Quotation as the provisions that would govern in the event of an early termination. Where Market Quotation fails, as was the case here, the Agreement required Assured to calculate the loss or gain *to it* resulting from LBIE's default. The Loss definition expressly enumerates a number of potential approaches to doing so, including by calculating "any loss of bargain," as Assured did.[47] It also expressly states that "*[a] party may (but need not) determine its Loss by reference to quotations of relevant rates or prices from one or more leading dealers in the relevant markets.*"[48] The only other requirement is that the calculation be made "reasonably" and "in good faith."[49]

The Loss definition does not dictate a specific formula or other rigid procedures for how to calculate the Non-defaulting Party's loss of bargain. Rather, it gives Assured broad discretion to value the underlying economic bargain it had struck with LBIE, and New York law is clear that loss-of-bargain damages are simply the amount of money that would "put the [non-breaching party] in the same economic position he would have occupied had the breaching party

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[47] JX-01 at 15 (1992 ISDA Master Agreement).
[48] *Id.* (emphasis added).
[49] *Id.*. LBIE focuses on the fact that ISDA Master Agreement was originally executed between LBIE and ACE Capital Re Overseas Ltd., LBIE Br. at 3, but that is irrelevant. LBIE entered into all of the Transactions directly with AGFP after the ISDA Master Agreement was assigned to Assured. *See generally* JX-05 through JX-32 (confirmations).

performed the contract."[50] That is exactly what Assured calculated.

There is no dispute that, under the terms of the Transactions, Assured guaranteed the scheduled payment of interest and principal that investors were to receive on the underlying reference obligations, and in exchange, it received regular, fixed premium payments from LBIE until the reference obligations matured.[51] It follows that the value to Assured of the CDS is the present value of the sum of all of the fixed premium payments that Assured expects to receive, minus the sum of any floating payments that Assured expects to make to cover actual losses.[52]

Assured calculated the premium payments that LBIE owed it over the life of the contracts and deducted from that the cash payments that Assured expected to pay LBIE over the life of those contracts which had been previously calculated and incorporated in its internal and external financial records. This calculation took account of the non-standard features of the contracts, and factored in the impact of those features on the bargain for Assured.[53] Assured did not use market prices for CDS issued by other parties, because they were irrelevant to Assured's bargain.

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[50] *Boyce v. Soundview Tech. Grp., Inc.*, 464 F.3d 376, 384, 391 (2d Cir. 2006) (applying New York law); *see also Sager v. Friedman*, 270 N.Y. 472, 481 (1936) (breach-of-contract damages are "the difference between the value of what has been received under the contract and the value of what would have been received if the contract had been performed according to its terms").

[51] *See* Assured Br. at 4–5.

[52] *See id.* at 59–60.

[53] First, under their "pay-as-you-go" structure, Assured was only obligated to pay actual shortfalls, if any, in interest and principal payments owed under the reference obligations as the payments came due, and was not required to make any payments based on changes in the market prices of the reference obligations. Trial Tr. 2131:2–11 (Schozer) (the CLO transactions and CDO transaction were pay-as-you-go), 2163:22–2164:1 (Schozer) (the CDS on the ABX 2006-02 was pay-as-you-go), 2168:7–22 (Schozer) (the CDS on ABX 2007-01 was pay-as-you-go), 3003:2–24 (Prager) (discussing Assured's obligations under the CDS at issue here, noting the general obligation to make payments in event of credit defaults and principal at "legal final maturity"). Second, Assured did not provide for physical or cash settlement, which would expose a protection seller to changes in the market prices of the reference obligations. *Id.* at 2113:25–2114:13 (Schozer). Third, Assured did not post collateral based on changes in the market prices of the reference obligations. *See id*. at 4256:18–25 (Bruce), 1028:23–24 (Bruce) ("[I]t's the normal practice of banks to post collateral.").

Unlike many standard CDS, Assured's payment obligations under the terms of the Transactions were not tied to or determined by market prices. Additionally, Assured only *sells* protection on transactions; it is not a dealer bank or hedge fund that buys and sells protection, it does not trade CDS,[54] and it does not earn profits (or suffer losses) based on changes in market prices.[55]

In its opening brief, LBIE completely ignores these details about the parties' economic bargain and says nothing about the evidence showing that the methodology Assured used to calculate its Loss reflected the parties' actual economic obligations under the contracts based on their non-standard terms. Instead, LBIE blithely refers to the Agreement as a "standard-form" and "industry-standard" ISDA Master Agreement, as though this means that Assured's economic bargain can be judged by other, different transactions documented under the same forms.[56] But the evidence showed that, as LBIE itself acknowledged internally in 2008, the Transactions have several features that are non-standard and that negatively affected their value to LBIE.[57] LBIE's own internal documents explained that because of these non-standard features, market prices of the underlying reference obligations did not reflect the value of the Transactions.[58] LBIE's arguments about the ISDA not being "an insurance contract" or defendant AGFP not being a monoline insurance company are pure misdirection.[59] Assured's business model helps to explain

[54] Trial Tr. 1293:15–21 (Rosenblum).
[55] *See* Assured Br. at 59. Assured's expert Joshua Cohn distinguished Assured from other market participants by explaining that it functioned as a "market utility for a specific purpose." Trial Tr. 2611:10–12 (Cohn).
[56] LBIE Br. at 4.
[57] JX-67 at 2–4 (Valuation Memorandum) (noting that LBIE's contract exposure to AGO involved "non-standard documentation," meaning that "[t]he adjusted value of these CDS Contracts is therefore a fraction of any estimate based on standard terms").
[58] *See id.* Of course, whether or not the Transactions were standard has nothing to do with the fact that under the plain language of the Agreement, Assured was entitled to calculate its loss of bargain. LBIE's focus on the "standard unamended" payment provisions, LBIE Br. at 5, conveniently overlooks this "plain and unambiguous language." D/O at *12.
[59] *See, e.g.*, LBIE Br. at 3, 7.

why the Agreements here have non-standard terms, but Assured is not seeking special treatment because it is a monoline. To the contrary, Assured has simply followed the contractual language and New York law in calculating the value of its economic bargain.

As explained above, while the Agreement identifies loss of bargain as one measure of Loss, it only raises, but does not answer the key question of what Assured's economic bargain was had there been no default, whether the default and termination caused Assured to suffer a loss or gain, or how to reasonably calculate that loss of its bargain. And there is nothing inherent in the termination provision the parties selected that would alter Assured's economic bargain or its obligations under the Agreement. It cannot be that Assured's termination of LBIE, and the termination provision alone, entitles LBIE to a windfall of hundreds of millions of dollars that LBIE could never have received under the Agreement if it had not defaulted and that bears no relation to any gain or loss to Assured.[60] LBIE does not even try to argue—because it cannot—that it would have been entitled to the damages it seeks if it had not defaulted and had instead performed its obligations under the Agreement through maturity.

That Assured did not negotiate a bespoke termination provision for the Transactions—like the walkaway provision included in the nine transactions terminated in December 2008—does not change the meaning of the Loss provision or otherwise support LBIE's argument. Michael Schozer explained that Assured negotiated for a walkaway provision in those specific Transactions because its surveillance group needed LBIE to provide the information in the

[60] LBIE's assertion that it is being "deprived" of hundreds of millions of dollars of funds that belong, in part, to "other CDS counterparties who had brought protection from LBIE" is supported by no trial evidence, and LBIE cites no support other than its complaint. *Id.* at 20.

trustee reports for the referenced CLOs in order to monitor their performance.[61] Terminating under the walkaway provision still allowed Assured to recover approximately $4 million in unpaid premiums owed by LBIE, and doing so made sense, as Schozer explained, because Assured believed it would be simpler and would result in "less conflict risk."[62] As the saga of this litigation has shown, there was nothing "irrational," as LBIE claims, about that decision.[63]

LBIE's related contention that Loss must be calculated based on market prices unless parties include a bespoke termination provision like a walkaway is belied by its own lawsuit here.[64] Despite Assured terminating those nine transactions based on a walkaway, LBIE still sued (in this action) and asserted that it was entitled to damages on those transactions based on market prices. This speaks volumes to LBIE's willingness to ignore the actual contract language and rewrite it to fit whatever theory suits its litigation goals. Moreover, LBIE's argument can simply be flipped around, meaning if LBIE had wanted to prevent Assured from calculating its "Loss" by solving for its own economic "loss of bargain" without regard to market prices or inputs, then LBIE should have bargained for a bespoke termination provision striking the contract language that expressly permits Assured to do so.

LBIE also argues that the Agreement "required . . . the party who was 'out of the money' [to] mak[e] a payment to the party that was 'in the money' in accordance with the Second Method."[65] But this misleadingly suggests that "Second Method" somehow required payments based on market prices. The last sentence of the Loss definition plainly says the opposite, and it

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[61] Trial Tr. 2195:14–25 (Schozer); *see also id.* at 1213:10–1214:2 (Rosenblum) (describing the use of trustee reports in calculating loss reserves), 2438:1–8 (Schozer) (explaining that Assured could not access the information in the trustee reports from public sources like Intex).
[62] *Id.* at 2196:15–19 (Schozer).
[63] LBIE Br. at 13.
[64] *Id*. at 6.
[65] *Id*.

is undisputed that Assured otherwise had no obligations under the Agreement to make any payments to LBIE based on market prices. Equally misleading is LBIE's mischaracterization of Second Method as a "no-fault provision."[66] While there is no dispute that under Second Method either the Defaulting Party or Non-defaulting Party may be required to make a payment to the other in the event of an early termination, nothing in that provision changes that, per section 6(e)(i)(4) and the definition of Loss in the Agreement, Loss is defined as the *Non-defaulting Party's* loss or gain or that Loss is "a general indemnification provision" for the Non-defaulting Party.[67] Losses that the Defaulting Party may incur as a result of its own default are not relevant to the calculation (not that LBIE actually has any).[68] What matters is Assured's loss or gain, which is expressly permitted to be based on the value of its economic bargain under the Agreement; for that determination, market prices (even if they existed) are irrelevant.

III. LBIE's Opening Brief Confirms That It Has Failed To Prove The Existence Of A Uniform Market Practice To Calculate Loss Based On Market Prices

The Court determined at summary judgment that a trial was necessary to assess whether there was in fact a "uniform or highly consistent practice of calculating Loss in a particular manner under similar circumstances," as LBIE contends, and, if so, whether it was unreasonable for Assured to depart from that practice under the circumstances of this case.[69] After a five-week trial and extensive briefing, it is clear that the expert testimony and other evidence offered by LBIE falls far short of establishing the existence of a "uniform market practice of determining Loss under an ISDA Master Agreement by reference to, or at the very least consistent with,

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[66] *Id.*
[67] *See* JX-72 at 35 (1992 ISDA User's Guide).
[68] *See Anthracite*, [2011] EWHC at [127] ("[I]t is by no means axiomatic that, in relation to derivatives, one party's loss approximates to the other party's gain.").
[69] D/O at *14.

prevailing market prices."[70] As Assured showed at trial, the Court need only look at prior litigation involving LBIE's own experts to find multiple examples of Loss being calculated in materially different ways. The evidence of private settlements that LBIE and its U.S. affiliates reached with certain counterparties on materially different transactions is irrelevant. And the remaining evidence on which LBIE relies—which consists of treatises and CRMPG reports—actually establishes that the large and diverse derivatives market never aligned on a single and unvarying approach to calculating Loss. LBIE also ignores numerous publications and statements by ISDA itself, consistent over decades, that contradict the narrow interpretation of the Loss provision that LBIE urges. Finally, even if the evidence had established a uniform practice of calculating Loss using market prices (which it did not), LBIE failed to prove that it was unreasonable for Assured to depart from that practice and use an approach consistent with the actual economic bargain struck in the Transactions, especially given the extensive evidence of market dislocation at the relevant time, which distorted what limited market data was available and rendered it meaningless.

A. The Experience Of LBIE's Own Experts Disproves The Existence Of A Single, Uniform Practice For Calculating Loss

At trial, LBIE offered testimony from four expert witnesses to support its assertion that there was a single, uniform practice of calculating Loss based on prevailing market prices. One simply had no experience with the calculation of Loss for a terminated CDS (Evy Adamidou),[71] and the other three had either previously calculated Loss without reference to prevailing market prices (Leslie Rahl[72] and Peter Niculescu[73]) or seen that done by others (Graham Bruce).[74] The

[70] LBIE Br. at 1–2.
[71] *See* Trial Tr. 1812:13–24 (Adamidou); *see also id.* at 1813:3–7, 1814:20–25 (Adamidou).
[72] AX-90026 at 8 (Rahl Devonshire Report).
[73] Trial Tr. 1587:10–13 (Niculescu).
[74] *Id*. at 1033:21–23, 1034:11–1035:14 (Bruce).

conclusory assertions about a uniform market practice that LBIE's experts offered in this litigation simply do not hold up in the face of their own prior experiences to the contrary; their actions speak louder than their words.

1. Rahl Previously Calculated Loss Using A Different Approach Than What LBIE Contends Was The Uniform Practice

Despite testifying in support of LBIE's claim that a uniform and universal market practice required Loss to be calculated as a market price as of the date of termination, Rahl admitted on cross-examination that she had developed a different, "unique" approach to calculating Loss in the *Devonshire* case.[75] In stark contrast to LBIE's assertion that, regardless of the circumstances, and "even where derivatives markets are not functioning," it was "nonetheless industry practice to determine the market price as of the date of termination" when valuing terminated CDS,[76] Rahl factored in the particular circumstances in *Devonshire*, including disrupted market conditions in 2009 caused by the financial crisis, and chose to calculate Loss as a theoretical market price that could have existed on a *different* date (either before or after, but not during, the disrupted conditions of the global financial crisis).

Rahl explained at trial that, in her view, the two components of an asset's *market price* on a given date are its projected future cash flows and the risk premium prevailing *on that date*.[77] In *Devonshire*, however, Rahl "estimate[d] loss by adding a cash flow projection of losses to a *normalized* risk premium."[78] But Rahl's "normalized" risk premium was *not* the risk premium that prevailed in the market as of the termination date (January 2009). Instead, citing "the extreme market illiquidity and dislocated pricing on that date" resulting from the abnormal

[75] *Id*. at 269:5–6 (Rahl).
[76] LBIE Br. at 37.
[77] Trial Tr. 105:1–106:7 (Rahl); *see also id*. at 231:14–19, 232:12–17 (Rahl) (agreeing that Loss is supposed to be calculated as of "the value on the date of the termination").
[78] AX-90026 at 8 (Rahl Devonshire Report) (emphasis added).

conditions of the financial crisis,[79] Rahl substituted a different ("normalized") risk premium roughly equivalent to those that prevailed in the market before and after the financial crisis.[80] Notably, the date Rahl chose when identifying the after-crisis risk premium that was no longer distorted by illiquidity and dislocation was April 2010, nearly a year later than the calculation date for the Transactions in this case.[81] The result of Rahl's methodology was a materially different valuation than what was implied by then-prevailing market prices in 2009.[82] As a consequence, there can be no question that Rahl did *not* model a theoretical price for the Devonshire transactions "as of the termination date" as LBIE argues is required here. The valuation approach she took in *Devonshire* is also consistent with the extensive evidence Assured put forward at trial showing that market practitioners understood Loss to give the Non-defaulting Party broad discretion to choose from a variety of valuation approaches depending on the specific circumstances.[83]

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[79] *Id.* at 23. In calculating its Loss, Assured was solving for the value of the bargain it lost, which was to hold the Transactions through maturity. As a result, it was not necessary or appropriate for Assured to factor in a risk premium to its Loss calculation. In contrast, the Non-defaulting Party in *Devonshire* was a dealer bank, Barclays, which measured its value based on the price at which it could trade in and out of the Transactions at issue in that case. For that reason, Rahl opined in that case that Barclays should be permitted to include normalized risk premium in its Loss calculation.

[80] AX-90026 at 33, Ex. 10 (Rahl Devonshire Report). Ultimately, Rahl chose to apply the prevailing risk premium from April 2010. *See also id.* at 10–11.

[81] *Id.* at 19 Ex. 5.

[82] Trial Tr. 345:2–4 (Rahl) (contrasting her approach with a "standard calculation" that would have resulted in value in excess of one billion dollars); *see also* AX-90026 at 8–9 (Rahl Devonshire Report) (calculating a combined swap value of $234 million).

[83] *Id*. at 2733:15–25 (Cohn) (agreeing that Loss permitted Rahl to do what she did in *Devonshire*). LBIE's attempts to justify Rahl's departure from the purported uniform market practice by arguing that the financial markets were not "active and liquid" in January 2009, LBIE Br. at 38, actually support Assured's position, because there is extensive evidence that the markets continued to be dislocated in July 2009, as explained in detail below. *See infra* at § IV.E; *see also* Assured Br. at 31–36. This is confirmed by Rahl's own decision in *Devonshire* to reach forward to April 2010 to find market prices that she believed were not dislocated.

Unable to deny that their own market practice expert "invent[ed]" a "unique methodology"[84] different from the purportedly uniform and unvarying practice LBIE claims existed, LBIE pivots to argue that Rahl's approach in *Devonshire* was justified by reasons not applicable to Assured, because "here, there was no standstill, and the markets for the CDS at issue were active and liquid."[85] But the evidence in this case shows that the financial markets were illiquid and dislocated as in *Devonshire*, as explained further below.[86] And the standstill in the *Devonshire* case is nothing more than a red herring. In 2007 Barclays negotiated a standstill agreement and that standstill continued until January 12, 2009. Finally, even though the calculation in *Devonshire* was governed by the same "standard" Loss provision that is at issue in this case, Rahl intentionally chose not to calculate a market price as of January 2009.[87]

2. <u>Niculescu Also Previously Calculated Loss Using A Different Approach Than What LBIE Contends Was The Uniform Practice</u>

Niculescu's prior experience calculating Loss under a 1992 ISDA Master Agreement also directly contradicts LBIE's claims that Assured's approach in this case was inconsistent with uniform market practice. Niculescu admitted during cross-examination that he was previously retained by a monoline in the *Solstice* litigation to value a terminated swap.[88] As in this case, the parties had selected Market Quotation, but the Market Quotation auction failed to generate sufficient bids.[89] There was ultimately a damages inquest proceeding in the Southern District of

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[84] Trial Tr. 268:20–269:22 (Rahl).
[85] LBIE Br. at 38. At trial, Rahl also repeatedly explained that her approach in Devonshire was driven by her concerns about "fairness, and what is equitable." *See, e.g.*, Trial Tr. 257:23–258:18.
[86] *See infra* at § IV.E; *see also* Assured Br. at 31–36.
[87] *Barclays Bank PLC v. Metcalf & Mansfield*, 2011 CarswellOnt 9183 (Can. Ont. Sup. Ct. J.) (WL) at ¶ 375 ("For the purpose of determining Barclays' [L]oss on the assumption that Devonshire was in default and Barclays was the [N]on-defaulting [P]arty, I see no basis to ignore the contractual requirement for the evaluation to be made as of January 13, 2009.").
[88] Trial Tr. 1585:22–1586:25 (Niculescu).
[89] *Id.* at 1587:1–9 (Niculescu).

New York to determine the Loss under the 1992 ISDA Master Agreement for the terminated swap, in which Niculescu put forward a Loss calculation.[90] Niculescu conceded that his calculation in the *Solstice* case reflected the "net present value of the part[ies'] future contingent payment obligations under the swap."[91] In other words, Niculescu performed a DCF analysis similar to the type of analysis that Assured relied on here to calculate its Loss. And he further conceded that he "intended [these] calculations to be consistent with market practice."[92] On re-direct, Niculescu explained that he used a DCF analysis in *Solstice* because "there were no market prices available" and because the transaction had "bespoke" terms and was "non-tradeable."[93] But these same facts apply equally to the Transactions here, which had monoline-specific terms, and for which there were no trading prices available, as proven by the lack of bids at the Market Quotation auction and LBIE's failure to novate.

3. <u>Bruce Offers Only Irrelevant, Speculative, And Unsupported Testimony</u>

LBIE also relies on Bruce's testimony to support its claims about market practice.[94] At the time of trial, Bruce, who had not worked as a trader in more than a decade, was serving as a litigation consultant for Lehman entities in three separate lawsuits.[95] LBIE touts that Bruce "traded CDS in 2009" while at Commerzbank,[96] but omits that Bruce traded "standard" CDS with materially different terms than those at issue here, and that he did so predominantly with

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[90] *Id.* at 1586:16–22 (Niculescu); *see also Bank of New York Mellon Tr. Co., Nat'l Ass'n v. Solstice ABS CBO II, Ltd.*, 910 F. Supp. 2d 629 (S.D.N.Y. 2012); *Bank of New York Mellon Tr. Co., Nat'l Ass'n v. Solstice ABS CBO II, Ltd.*, No. 09 CIV. 9415 (DAB), 2012 WL 13070212, at *7 (S.D.N.Y. Mar. 28, 2012).
[91] Trial Tr. 1587:10–13 (Niculescu).
[92] *Id.* at 1587:23–25 (Niculescu).
[93] *Id*. at 1768:19–20 (Niculescu).
[94] LBIE Br. at 32–33.
[95] Trial Tr. 993:5–994:15.
[96] LBIE Br. at 32.

other major banks.[97] Moreover, Bruce admitted that he had no direct experience with closing out a derivative contract following a counterparty default (the circumstance in this case) and "stayed away" from Lehman-related closeouts.[98] In addition to failing to conduct or cite any studies or surveys about what the market practice was for valuing CDS,[99] Bruce admitted that he has not taught, lectured, or published anything on the subject (or any other subject).[100] Bruce's testimony about how bank traders valued CDS different than those at issue here is both irrelevant and speculative.[101] And Bruce's testimony that he had not seen an example of a party employing a termination methodology like the one Assured used[102] ignores both the fact that Lehman's bankruptcy created an unprecedented situation for Assured and that LBIE did not, and could not, point to one example of a monoline insurer closing out a derivatives contract with a bank counterparty doing anything differently than Assured did here.

Bruce—who has neither experience nor expertise in accounting—cited to a "hierarchy of inputs" found in FAS 157, a technical accounting rule involving "fair value,"[103] for the proposition that the same hierarchy was uniformly used by market participants valuing terminated CDS.[104] At trial, Bruce admitted that this assertion is unsupported by anything other

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[97] Trial Tr. 811:3–812:6 (Bruce).
[98] *Id*. at 998:24–999:16 (Bruce).
[99] *Id*. at 997:4–13 (Bruce).
[100] *Id*. at 4250:23–4251:3 (Bruce); *see also id*. at 997:1–3 (Bruce).
[101] As such, the Court should not credit his testimony. *See Cornell v. 360 W. 51st St. Realty, LLC*, 22 N.Y.3d 762, 781 (2014) (expert opinions should be rejected when "there is simply too great an analytical gap between the data and the opinion proffered" such that the opinion is "connected to existing data only by the *ipse dixit* of the expert") (internal quotations omitted).
[102] Trial Tr. 970:19–979:11 (Bruce).
[103] *Id.* at 1000:8–1002:11 (Bruce).
[104] *See* LBIE Br. at 32–33.

than his own say-so[105] and that traders did not use this accounting rule when valuing trades on a daily basis.[106] Bruce also admitted that his claim that Assured "used" that same hierarchy to value CDS in its public disclosures was in fact based on Assured's description of the application of technical accounting rules,[107] which Assured clearly warned were not a meaningful measure of value for its CDS including because Assured "did not have the intent and/or ability to trade" the CDS and did not have "the ability to realize such [fair value] gains or losses."[108]

Separately, relying on testimony from Bruce, LBIE argues in a footnote that Assured "did not even attempt numerous other reasonable approaches" to find replacement counterparties for the terminated CDS.[109] But these supposedly "reasonable approaches"—such as taking on a new obligation to post collateral[110]—would have required Assured to incur costs and burdens far beyond what was contractually required under the Agreement. The evidence showed that Assured followed the language of the Agreement, allowed LBIE time to attempt novation (despite having no obligation to do so), and conducted a well-designed auction.[111] There is no

[105] Trial Tr. 1000:8–1002:3 (Bruce) (admitting that the slide he used at trial to describe his "hierarchy of inputs" is supported only by his own expert report, which itself did not cite any authorities other than FAS 157).
[106] *Id*. at 1071:14–1072:1 (Bruce). Bruce also acknowledged during cross-examination that fair value accounting was itself the subject of controversy in the United States and overseas, something he failed to mention in his direct testimony or his report. *See id*. at 1072:2–1073:10 (Bruce); *see also* AX-90026 at 97 (Rahl Devonshire Report) (noting that "consensus opinion about the appropriateness of various valuation techniques was being debated and reassessed in 2008 and 2009" resulting in the Financial Accounting Standard Board "significantly alter[ing] the accounting for fair value . . . to permit more latitude in using . . . cash flow projections when liquid market quotes were not available or reliable").
[107] Trial Tr. 4219:7–4221:2 (Bruce); *see also id.* at 1001:2–1002:3 (Bruce).
[108] AX-70008 at 96–97 (Assured 2009 10-K).
[109] LBIE Br. at 41 n.37 (citing only to Trial Tr. 4192:13–22, 4194:1–4197:2 (Bruce)).
[110] Trial Tr. 4192:18–4197:2 (Bruce) (describing the hypothetical steps that he believed Assured could have taken including his suggestion that "Assured could have offered to post collateral"); *see also id.* at 4256:15–4257:16 (Bruce) (describing Assured posting collateral as one option, while also acknowledging that there was no requirement for Assured to post collateral to LBIE).
[111] D/O at *7.

basis in the law, the Agreement, the evidence, or common sense to require Assured to do more, and speculation about such hypothetical measures deserves no weight.[112]

4. Adamidou's Testimony Lacks Any Reliable Basis And Is Irrelevant

LBIE attempts to rely on the testimony of Adamidou to support its argument that there was a "consistent market practice to value derivatives using market-based inputs,"[113] but Adamidou was unable to identify any relevant personal experience, any relevant analysis she had conducted, or any authoritative sources that support her broad generalizations about market practice. Her monoline experience was limited to working at two failed monolines, AMBAC and CIFG,[114] and Adamidou admitted at trial that she had no experience at either company (or ever) with terminations on default or with calculating Loss for a terminated CDS. She also admitted to having no experience with a CDS transaction that was terminated on a mark-to-market basis, as LBIE argues should have been done here.[115] Adamidou also confirmed at trial that she never undertook any surveys or conducted any literature review on market practice or how monolines viewed termination provisions under a 1992 ISDA Master Agreement, and did not rely on any in formulating her opinions.[116] LBIE argues that Adamidou's expertise is based on her past involvement with settlement negotiations surrounding "voluntary terminations of CDS trades,"[117] but voluntary terminations by definition do not involve the calculation of Loss or Market Quotation or the application of any other termination provisions in the 1992 ISDA Master Agreement. In short, Adamidou's testimony is based on nothing more than her own say-

[112] *See* Trial Tr. 4217:22–23 (Bruce) (the Court reserving on the admission of Bruce's testimony on this topic because, among other things, "it seems to me like you're asking a lot of Assured right now").
[113] LBIE Br. at 31.
[114] Trial Tr. 1807:21–1808:19.
[115] *See id.* at 1812:13–24 (Adamidou); *see also id.* at 1813:3–7 (Adamidou), *id.* at 1814:22–25.
[116] *See id.* at 1955:15–1956:9 (Adamidou).
[117] LBIE Br. at 33.

so, and her alleged expertise has no relevance to the issues in this case.

B. The Other Evidence Cited By LBIE Fails To Prove A Uniform Market Practice

1. LBIE's Private Settlements Of Transactions With Materially Different Terms Are Irrelevant To Establishing A Market Practice For The Transactions Here

Like LBIE's expert evidence, its evidence relating to Loss calculations by other LBIE counterparties also fails to prove the existence of a universal market practice to value derivatives by reference to market prices. The only non-expert evidence that LBIE points to in its efforts to paint Assured's Loss calculation as an "extreme outlier" is the Viegas Spreadsheet.[118] According to LBIE, the Viegas Spreadsheet (LX-92b) proves that all of its other counterparties used market prices when calculating early termination payment amounts with LBIE.[119] On this thin basis, LBIE claims that Assured's results were inherently unreasonable.

But the spreadsheet does not actually provide any information about how the transactions referenced in it were valued, because it merely records the final amounts agreed to between LBIE and the listed counterparties. LBIE asks the Court to infer that those counterparties used a market-based methodology, despite clear testimony from Viegas that the settlement amounts sometimes reflected global compromises that included many different types of transactions and despite explicit statements on the face of the document that in many cases, LBIE itself could not determine what methodology its counterparty had used.[120]

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[118] *Id*. at 20.
[119] *Id*. at 31 ("The sharp contrast between AGFP's intentional disregard of market pricing and the uniform practices of all of LBIE's other counterparties demonstrates that AGFP acted unreasonably in breach of its contractual obligations.").
[120] *See, e.g.*, Trial Tr. 735:18–25 (Viegas) ("Q. You're saying, there may be trades beyond what's accounted for in this spreadsheet that were part of Lehman's assessment of whether the counterparty's valuation was consistent with Lehman's valuation? A. Yes, because they were not trades related to ABS and CDS, and I think . . . even yesterday I said . . . that we've done this analysis on a counterparty-aggregated basis."); *see also* LX-92b (Viegas Spreadsheet) ("Unique

Even if this spreadsheet proved that other counterparties had calculated early termination payments differently than Assured had (which it does not), it would be irrelevant to the reasonableness of Assured's Loss calculation because it concerned transactions with materially different economic terms. The evidence showed nearly all the transactions listed on the spreadsheet involved collateralized CDS and/or required physical settlement. This means that the parties to these transactions—which included "investment banks, pension funds, hedge funds, and commercial banks," but not monolines—had agreed to payment obligations based on market price-based calculations.[121] Far from the "exactly-on-point evidence of market practice" that LBIE claims it is,[122] this spreadsheet is irrelevant to determining whether a uniform market practice of calculating Loss by reference to market prices existed for transactions like those at issue here.

2. <u>The CRMPG Reports Demonstrate The Absence Of Any Market-Wide Consensus About How To Calculate Loss</u>

LBIE relies on the August 6, 2008 report of the Counterparty Risk Management Policy Group for the proposition that market participants understood that "market pricing should be used to value terminated trades."[123] In fact, as explained in Assured's opening brief, the CRMPG III report shows the *absence* of any industry-wide consensus on how to value terminated transactions.[124] That report was preceded by two earlier CRMPG reports that outlined recommendations aimed at "harmonizing" disparate and varied industry close-out

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Ctpy List" tab, column H, and "Ctpy Values" tab, column O noting, "no info" for how the counterparty determined Loss).

[121] *See* Trial Tr. at 3130:15–3131:10 (Prager) (explaining that 44 out of the 46 ISDA agreements produced by LBIE referenced collateral postings, and noting that 19 of the 20 CLO confirmations that LBIE produced called for physical settlement); *see also* AX-50076 (LBIE Produced Master Agreements and Confirms); LBIE Br. at 30.

[122] LBIE Br. at 30.

[123] *Id*. at 36.

[124] Assured Br. at 54–55 (citing JX-64 at 135 (CRMPG III)).

procedures—recommendations that would have clearly been unnecessary if LBIE's purported uniform market practice existed. And all three reports addressed the challenges to developing an industry-wide consensus. CRMPG I explained that "the Policy Group recognizes that achieving enhancements and harmonization to standard industry close-out procedures could take considerable time."[125] And "CRMPG II and CRMPG III were unable to reach agreement calling for the broad application of Close-out Amount as an industry standard."[126] LBIE's selective quotation of one passage from CRMPG III ignores this broader history and context.

Additionally, on its face, the language LBIE quotes—that there was "general agreement that in determining close out amounts market inputs should be used unless doing so would produce a commercially unreasonable result"[127]—does not prove that any uniform practice existed. Vaguely directing that "market inputs" be "used" is not a specific methodology. Moreover, the use of "should" reflects that the report is making a recommendation, not recording a practice already in place.[128] Ultimately, the CRMPG III report merely suggested that "another attempt to come up with a potential industry-wide approach could be worthwhile,"[129] again unquestionably demonstrating that a consensus had not been reached.

3. The Ambac Rehabilitation Involved DCF Calculations Of Value

While LBIE points to the Ambac rehabilitation as support for its claimed universal practice of using mark-to-market valuations on termination,[130] what actually happened contradicts LBIE's contention. Ambac was a monoline insurer that "verged on insolvency" and

[125] AX-50013 at 48 (CRMPG I); *see also* Assured Br. 54–55.
[126] JX-64 at 135 (CRMPG III); *see also* Assured Br. at 54–55.
[127] JX-64 at 137 (CRMPG III); *see also* LBIE Br. at 36.
[128] *See* JX-64 at 137 (CRMPG III).
[129] *Id.* at 136.
[130] LBIE Br. at 37.

was about to default[131] (the opposite of this case, where it was a monoline insurer's bank counterparty, LBIE, that defaulted).[132] As a result, Ambac's bank counterparties (like Assured in this case) were in a position to determine the valuation methodology and measure *their* losses. For some transactions, market pricing was available and did not produce an unreasonable result when used for the calculations, but for others "there was little to no visible trading activity or market prices" available.[133] BlackRock, retained as an independent appraiser and not as a litigation consultant for any single party, determined the net present value of the Transactions at issue using DCF models—just as Assured did in this case.[134] Bruce admitted that BlackRock's approach was "consistent with market practice" (his weak attempt to walk this back at trial notwithstanding).[135] Additionally, like Assured, BlackRock considered research and reports from the federal reserve bank, the U.S. Treasury, the Federal Home Loan Association, as well as statements from the Federal Reserve Chairman,[136] all of which Bruce admitted were relevant data points.[137] Nothing about the termination value calculations performed in connection with Ambac's rehabilitation supports LBIE's claims in this case.

4. <u>The Lehman Framework</u>

LBIE asserts that the Lehman Derivatives Claims Settlement Framework (LX-35)

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[131] Trial Tr. 1031:14–1032:2 (Bruce); *see also* AX-50039 at 15–16 (Ambac Disclosure Statement to Wisconsin Regulators).
[132] Trial. Tr. 1033:14–20 (Bruce).
[133] *Id.* at 1034:11–12 (Bruce).
[134] *Id.* at 1033:21–23, 1034:11–18 (Bruce); *see also id.* at 1034:15–1035:3 (Bruce) ("All three scenarios used a discounted cash flow model."); AX-50039 at 33 (Ambac Disclosure Statement to Wisconsin Regulators).
[135] Trial Tr. 1035:4–1037:9 (Bruce).
[136] *Id.* at 1043:16–21, 1044:14–17 (Bruce).
[137] *Id.* at 1044:10–17 (Bruce). *See, e.g., id.* at 1639:22–1641:25 (Niculescu) (discussing the U.S. Treasury's view that into 2009 there would be a negative economic cycle); *see also id.* at 3024:8–23 (Prager) (same), 3391:15–25, 3026:21–3027:4 (Prager) (referencing Federal Reserve Chairman Bernanke's statements and actions by the Federal Reserve and Treasury).

embodies LBIE's purported uniform market practice for calculating Loss.[138] As explained in Assured's opening brief, the Framework does not and cannot demonstrate the existence of a uniform market practice.[139] The very nature of the Framework—a settlement agreement arrived at between dealer groups and Lehman two years after the termination in this case, the parties to which agreed to a compromise of their full contractual rights—is not evidence of the ordinary course of business.[140]

Additionally, the compromise reached in the Framework between Lehman and certain "Big Bank" counterparties does not replicate what LBIE claims is the uniform market practice (i.e. to value terminated CDS as a price, actual or theoretical, based on other market prices). Rather, the Framework approach was designed to be broad enough to cover a large variety of transactions that are not even CDS and gave Lehman discretion to entirely disregard the Framework's "proposed claims calculation methodology"[141] and to substitute a different, subjective value for an *actual* price paid for a particular replacement transaction if Lehman deemed that price unreasonable.[142] If this is evidence of anything, it is evidence that market participants understood that departure from market prices was permitted in order to reach a reasonable result.

C. LBIE's Opening Brief Ignores Relevant Market Practice Evidence That Contradicts Its Claims

ISDA publications and several treatises introduced at trial clearly and powerfully

[138] LBIE Br. at 36–37.
[139] Assured Br. at 55.
[140] LX-35 at 3 (Lehman Derivatives Claims Settlement Framework) (The Framework itself explicitly states that it was "strictly private," "for settlement purposes" and "represents material concessions . . . in the interest of settlement.").
[141] *Id.* at 3 ("Debtors shall not be bound by anything contained in the Framework Methodology, including, without limitation, the proposed claims calculation methodology set forth herein, in any litigation or dispute.").
[142] *Id.*

contradict LBIE's assertions about the meaning of Loss. Yet, in its opening brief, LBIE does not even attempt to explain why this evidence is not fatal to its claim.[143]

ISDA, "the voice of the derivatives industry," educated the market about the Master Agreement through its User's Guides.[144] In its earliest User's Guide in 1985, ISDA explained that Loss in its earliest form (embedded in a provision entitled "Indemnification") "allow[ed] the parties to calculate damages on the basis of a general indemnity."[145] In its 1986 User's Guide, ISDA noted that "[m]any ISDA members ha[d] a preference for 'indemnification'"—which had not changed substantively since 1985—"because of its simplicity."[146] The Loss definition also did not change from 1986 to 1987, when ISDA published its first Master Agreement,[147] and the 1987 User's Guide continued to explain Loss as "a general indemnification provision."[148] In the 1992 Master Agreement, Loss included a reasonableness requirement for the first time.[149] But ISDA explained that, in substance, it remained the same "general indemnification provision" that it had been at its origin, through "which a party reasonably determines in good faith its total losses . . . and gains."[150] As Cohn explained, the changes that the Loss provision has undergone over time related to other aspects of the Master Agreement and have not altered its fundamental

[143] LBIE only cites to the 1992 ISDA User's Guide for the notion that "when Unpaid Amounts are calculated separately . . . Market Quotation and Loss are both intended to reflect 'the future value of the Terminated Transactions'"—a point that is unrelated to the development of the Loss provision and supports Assured's calculation of Loss based on the expected future value of the Transactions. LBIE Br. at 24.
[144] *See* Trial Tr. 170:2 (Rahl); *see also id.* at 2606:11–13 (Cohn 72:13–17 (Rahl).
[145] AX-50063 at 6 (Guide to 1985 Swaps Code).
[146] AX-50064 at 14 (1986 Swaps Code); *see also* Trial Tr. 2622:2–20 (Cohn); ADX-01-01 ("Loss: 1985-1986").
[147] Trial Tr. 2627:19–23; *see also* ADX-01-02 ("Loss: 1986-1987").
[148] AX-50066 at 12 (Guide to 1987 ISDA Master Agreement).
[149] JX-01 at 15 (1992 ISDA Master Agreement); *see also* ADX-01-03 ("Loss: 1992").
[150] AX-50002 at 35 (Guide to 1992 ISDA Master Agreement); *see also* Trial Tr. 2634:9–16 (Cohn).

nature as an indemnification provision.[151] LBIE's opening brief fails to engage with any of this.

ISDA also expressed its views on the operation of the 1992 Loss provision to the market by submitting amicus briefs in cases of interest.[152] While ISDA often submits amicus briefs "[t]o help explain the ISDA Master Agreement," in *Intel*, it had a greater sense of urgency because it "was concerned that Lehman's argument [that Loss required a mark-to-model approach] was terribly contrary to ISDA's view."[153] In that brief, ISDA explained that "[t]he Loss provision in the ISDA Master was carefully crafted as an alternative to Market Quotation, to allow flexibility in the determination of the Non-defaulting Party's Loss following early termination. Any reasonable, good faith calculation consistent with [New York] law comports with the Loss definition."[154] Confronted with this evidence that the voice of the derivatives industry expressly disagreed with LBIE's position in this case, LBIE again offered no response in its opening brief.

The authoritative treatises on which LBIE's expert witnesses relied also directly contradict LBIE's position in this case.[155] For example, Gooch and Klein stated that "market participants had largely abandoned" Formula and other liquidated damages approaches in favor of Loss—"a general indemnification" provision—or, instead of Loss, "various *alternatives* that call for quantifying damages by reference to what the market would charge or pay to enter into *replacement transactions*," such as Market Quotation.[156] The Durham treatise described Loss as

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[151] Trial Tr. 2622:2–20 (Cohn); *see also id.* at 2627:19–23 (Cohn), 2634:9–16 (Cohn).
[152] *Id.* at 2654:12–19 (Cohn).
[153] *Id.* at 2658:6–7 (Cohn).
[154] ISDA's Amicus Brief in Support of Def. Intel Corp.'s Mot for Summ. J., ECF No. 57-1, *Lehman Bros. Holdings Inc. v. Intel Corp. (In re: Lehman Bros. Holdings Inc.)*, Case No. 13-1340-scc (Bankr. S.D.N.Y. Jan. 20, 2015) at 3–4.
[155] Trial Tr. 136:4–11 (Rahl) (confirming that the Firth, Durham, and Gooch & Klein treatises were all authoritative sources on market practice for calculating Loss under the 1992 ISDA Master Agreement).
[156] AX-90023 at 54 (Gooch & Klein, 2002) (emphasis added); *see also* AX-90022 at 16 (Gooch & Klein, 1993) (describing Loss as a "general indemnification provision").

"a more subjective measure of the value of the transaction and a more subjective determination of the early termination amount, because it represents the losses suffered by the [N]on-defaulting [P]arty . . . which may be unique to that party."[157] Durham further stated that even the Close-out Amount methodology in the 2002 ISDA Master Agreement, which is less flexible than Loss, "does not require that the determining party utilize [market data and information relating to the replacement value of the terminated transactions]."[158] The same is necessarily true for Loss.[159] Finally, the Firth treatise recognized that under Loss, "[t]he determining party is expressly given a choice between assessing the cost of replacing the material terms and option rights (or the gain involved in doing so) or determining their economic equivalent. The former would take into account the price that would be paid for one or more replacement transactions, while the latter would involve assessing the value, as at the Early Termination Date, of the remainder of the contract."[160] The latter is what Assured did here. Firth further noted that "[h]ow loss is assessed may . . . depend on market conditions at the time of the termination."[161] Notably, "*[w]here there is no available market for a replacement transaction* . . . it may not be possible to establish Loss by reference to the market price. It follows that the use of quotations (whether firm or indicative) or *valuations of the cost of a replacement transaction is inappropriate*."[162] In the face of these authorities, LBIE again offered no response.

Likewise, at trial, the experts who had relied on these treatises tellingly did not even

[157] AX-90024 at 24 (Durham Treatise).
[158] *Id.* at 47.
[159] Trial Tr. 2704:9–2705:12 (Cohn) (explaining that Close-out Amount was more rigid than other alternatives that ISDA considered, and certainly less flexible than Loss).
[160] AX-90021 at 236 (Firth Treatise).
[161] *Id.* at 204.
[162] *Id.* at 211 (emphasis added).

attempt to persuade the Court that their contents supported LBIE's claims.[163] After cross-examination of Rahl demonstrated that each of these authorities contradicted her and LBIE's assertions, counsel for LBIE attempted to present snippets from a portion of the Gooch & Klein treatise as though it were representative of the entire source.[164] This language was taken from the general introduction to the chapter titled "Damages and Close-Out Settlement," which addresses a broad range of agreements and calculation methodologies, and is not specific to Loss.[165] In contrast, the portions of the treatise shown to Rahl during her cross-examination come from subsections that specifically explain Loss, each of which directly contradicts LBIE's position in this case.[166] Here, too, LBIE's opening brief offered no response.

In contrast, the market understanding reflected in ISDA's publications and treatises were consistent with the testimony of Joshua Cohn, who had the broadest and deepest experience on which to speak to the market's understanding of the Loss provision. Cohn's experiences give him a wider perspective than LBIE's expert witnesses, whose formative experiences all involved trading derivatives for and with large banks.[167] Cohn's "work with ISDA led him to interact with a large and diverse set of market participants," and he was tasked with educating the market about the Loss provision as part of the public rollout of the 1992 ISDA Master Agreement and throughout the years relevant to this case.[168] As a result, he had countless opportunities to discuss the Loss provision with market participants from all corners of the industry. Based on

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[163] *See generally* Trial Tr. 55:9–123:3 (Rahl).
[164] *Id.* at 298:11–300:7 (Rahl) (discussing AX-90023 at 34 (Gooch & Klein 2002)).
[165] Accordingly, the portion of treatise referenced by LBIE during Rahl's redirect examination even uses qualifiers such as "likely," "generally," and "often" when discussing its applicability. AX-90023 at 33–34 (Gooch & Klein, 2002).
[166] Trial Tr. 149:12–157:10 (Rahl) (discussing AX-90023 at 49, 53–54, 55–57 (Gooch & Klein, 2002)).
[167] *See* Assured Br. at 45–46.
[168] *See id.* at 46.

that experience, he testified that Loss provides market participants with a "universe of possibility" for valuing terminated derivatives transactions.[169] As ISDA explained, Loss in its earliest form "allow[ed] the parties to calculate damages on the basis of a general indemnity."[170] The market understood this to be different from the provision that became Market Quotation.[171] That understanding of Loss did not change with the advent of the 1987 Master Agreement,[172] nor did the market understand Loss to have substantively changed between 1987 and 1992,[173] at which time it still understood Loss and Market Quotation to be different methodologies.[174] Contrary to LBIE's assertions in this case, Cohn explained that the market never understood Loss to solely be a measure of replacement value.[175] In fact, when a British court issued the *Peregrine* decision suggesting that Loss calculations should emulate the results of a Market Quotation process,[176] ISDA was "upset" and market participants "were dumbfounded."[177]

LBIE entirely failed to engage with the substance of Cohn's testimony in its opening brief.[178] At trial, LBIE focused on establishing that Cohn is not a monoline expert and does not personally calculate values for derivative transactions.[179] But that does not take away from

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[169] Trial Tr. 2635:10–20 (Cohn).
[170] AX-50063 at 6 (Guide to 1985 Swaps Code).
[171] Trial Tr. 2618:16–2619:3 (Cohn).
[172] *Id.* at 2629:2–4 (Cohn).
[173] *Id.* at 2637:13–19 (Cohn).
[174] *Id.* at 2652:13–17 (Cohn); *see also id.* at 2734:1–5 (Cohn) ("Q. At the time that Assured entered into and then terminated the CDS [T]ransactions at issue, was there a uniform market practice for always valuing derivatives by reference to market prices? A. No.").
[175] *Id.* at 2734:6–8 (Cohn).
[176] *See generally Peregrine Fixed Income Ltd. v. Robinson Dep't Store Public Co.*, [2000] EWHC 99 (Comm) (Eng.).
[177] Trial Tr. 2642:17–22 (Cohn), 2644:21–2645:2 (Cohn).
[178] To the extent that they attempt in their reply to belatedly rebut Cohn's testimony or argue that it should be given less weight, their failure to address it in their opening brief deprives Defendants of an opportunity to respond.
[179] *See, e.g.*, Trial Tr. 2740:2–4 (Cohn); *see also id.* at 2743:10–15 (Cohn).

Cohn's deep experience with the market's understanding of the 1992 ISDA Master Agreement's Loss provision—the actual subject matter of his testimony. LBIE's cross-examination of Cohn also focused on "Mastering the Storm," an article written by Cohn for Risk Magazine, whose audience chiefly consisted of those working at banks and other financial institutions.[180] At trial, LBIE cherry-picked excerpts from a single paragraph of the article that sought to explain that (atypically) Second Method permits the defaulting parties to recover a gain, stating that Second Method "mandates the in-the-money party receives the mark-to-market value upon closeout[,] even if that party is in default."[181] Cohn testified that this was his attempt to explain Second Method at a high level to a novice audience, in effect "trying to shorthand the effect of Second Method in a mark-to-market termination valuation close-out."[182] Far from contradicting Cohn's testimony about Loss, the article confirms it: in the very next paragraph (which actually explains the operation of Loss, and not some other provision), which LBIE conveniently ignored, the article states that Loss is "intended to be a general indemnification provision allowing a good deal of freedom to the [N]on-defaulting [P]arty to choose how it wishes to calculate losses."[183]

None of the few cherry-picked snippets of Cohn's testimony that LBIE cited in its opening brief address the central question in this case. First, LBIE cited Cohn's testimony to support the assertion "that it was 'common' practice for Lehman's counterparties to terminate and value derivatives trades with reference to market prices . . . and that he would advise clients terminating CDS trades 'to look at the market price.'"[184] But this is just another example of LBIE answering a question that they have posed to themselves, rather than the question posed to

[180] *Id.* at 2724:8–16 (Cohn).
[181] *Id.* at 2780:2–5 (Cohn).
[182] *Id.* at 2727:22–23 (Cohn).
[183] *Id.* at 2820:4–6 (Cohn); *see also id.* at 2821:9–15 (Cohn).
[184] LBIE Br. at 35 (internal citations omitted).

them by this Court.[185] Whether or not market prices were "common[ly]" used in performing Loss calculations does not tell us whether there was a *uniform* practice to do so, or if Assured was bound to follow such practice under the specific circumstances of this case. Second, LBIE cited to Cohn's testimony to support the assertion "that a Non-defaulting Party may be out of the money."[186] This point is not in dispute, and merely reflects the operation of Second Method, which Cohn explained is "not a calculation method at all."[187] LBIE's continuing effort to muddy the waters by focusing on Second Method in a trial about the reasonableness of Assured's Loss calculation method reflects that they have nothing to say on the salient issue.

D. LBIE's Opening Brief Confirms That It Failed To Prove That Assured Knew That The Purported Uniform Market Practice Existed

LBIE is also wrong in arguing that any trial evidence shows that Assured "acknowledge[d] market practice for valuing CDS trades upon termination."[188] As Assured explained in its opening brief, when properly read in context, the snippets from Assured's 10-K that LBIE points to address what could happen if Assured's *counterparties* "'exercised their right to terminate'" their CDS if Assured is the defaulting party.[189] LBIE claims this distinction is not in the document.[190] Not true—the language just doesn't appear in LBIE's opening brief, because LBIE deletes it by employing an ellipsis.[191] Further, LBIE says nothing about the heading of the

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185 *See* D/O at *11 (holding that "the ISDA Master Agreement is not ambiguous to the extent that it provides that Loss need not be calculated using market quotations in every case").
186 LBIE Br. at 6.
187 Trial Tr. 2727:19 (Cohn).
188 LBIE Br. at 38.
189 Assured Br. at 57 (citing JX-57 (Assured 2008 10-K)).
190 LBIE Br. at 38–39.
191 *Id.* at 38; *see also* JX-57 at 84 (Assured 2008 10-K) ("If a credit derivative is terminated, the Company could be required to make a mark-to-market payment as determined under the ISDA documentation. For example, if AGC's rating were downgraded to A+, under market conditions at December 31, 2008, if the counterparties exercised their right to terminate their credit derivatives, AGC would have been required to make payments that the Company estimates to be approximately $261 million.").

section—"A downgrade of the financial strength or financial enhancement ratings of any of our insurance subsidiaries would adversely affect our business and prospects and, consequently, our results of operations and financial condition"—which highlights that the entire risk factor is about a scenario where Assured defaults because of a downgrade to its credit rating.[192]

LBIE also cites to a statement in a slide presentation Assured made to the SEC in September 2010, arguing that Assured acknowledged a market practice of making market-based termination payments on its CDS, even if it was a Non-defaulting Party. Again, this is false. The document merely acknowledges that a "[r]isk of mark-to-market termination payments exists."[193] But it is uncontroverted that in some (but hardly all) circumstances, a risk of a mark-to-market termination payment does exist—if Assured is a Defaulting Party, or if it calculates a termination payment pursuant to the Market Quotation provision. LBIE fails to acknowledge that there is nothing in the presentation to suggest that a calculation of Loss *requires* a mark-to-market calculation—or anything about Loss at all.

LBIE relies on a brief reference to a mark-to-market payment in a copy of a draft presentation, but as Assured explained in its opening brief,[194] that slide merely reflected the undisputed point that Market Quotation is a mark-to-market or market price concept. Like the SEC slide, that says nothing about what Loss requires or whether Assured believed there was an established market practice for calculating Loss requiring the use of market prices.

Finally, LBIE's argument that Assured's conduct in 2008 and 2009 supports its claims about the Agreement completely distorts the evidence.[195] LBIE claims that LX-170 shows that

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[192] JX-57 at 55 (Assured 2008 10-K).
[193] LBIE Br. at 38 (quoting LX-169 at 7 (Assured Presentation to SEC on Dodd-Frank Act)).
[194] Assured Br. at 59.
[195] LBIE Br. at 11.

Assured "recognized" in September 2008 that it was "out of the money" on all of the Transactions at that time and that they had become a liability due to the financial crisis.[196] But this spreadsheet does no such thing; it reflects calculations for Assured's GAAP accounting, but it is incomplete because (as stated in the document) it does not factor in the impact of AGC's credit risk, as is required under FAS 157.[197] Even more importantly, as every Assured witness uniformly testified and as Assured told its investors at the time, Assured's GAAP mark-to-market reporting was "not meaningful at all" to its business or its expectations about Loss, and "[c]hanges in the fair value of [Assured's] credit derivatives that do not reflect actual or expected claims or credit losses have no impact on [Assured's] claims paying resources."[198] As explained in its opening brief, Assured did conclude that losses on the two ABX Transactions would exceed the total premium owed by LBIE, so for those two CDS Transactions Assured did calculate a payment from Assured to LBIE.[199] But LX-170 is unrelated and irrelevant to those calculations.

E. Even If LBIE's Purported Market Practice Existed, LBIE's Opening Brief Confirms It Has Not Met Its Burden To Prove That Assured Unreasonably Departed From That Market Practice

As LBIE itself acknowledges, at summary judgment, the Court held that evidence that Assured departed from a uniform industry practice would not be conclusive but rather simply "a

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196 *Id.*

197 *See* Trial Tr. at 2851:24–2852:18 (Bailenson) (explaining that GAAP mark-to-market accounting is not reflective of "ultimate economic or expected loss" under a transaction for several reasons, including that it fails to take into account "the actual credit spread of Assured Guaranty"). As reflected in AX-20033, after taking into account Assured's CDS spread, Assured recognized a loss of approximately $20 million from terminating the Transactions. AX-20033 (Assured Summary of Transactions with LBIE) (in the Q2 2009 tab, determining the mark-to-market value of the Transactions to be $19,821,946 in Assured's favor).

198 AX-70008 at 72, 118 (Assured 2009 10-K); Trial Tr. 2848:1–6 (Bailenson); *see also* Assured Br. at 29–30.

199 Assured Br. at 24–26.

factor, among others, to be considered in assessing [Assured's] reasonableness and good faith in calculating Loss."[200] Not only did LBIE fail to prove the existence of a uniform, unvarying market practice, it also failed to prove that it was unreasonable for Assured not to use the poor proxies for market prices available at the time to calculate Loss given market conditions in 2009.

As Assured demonstrated in its opening brief, there were numerous reasons why it was reasonable for Assured not to use market prices (let alone the poor proxies available at the time) to calculate its Loss.[201] First, Assured is a monoline insurer, not a bank or a hedge fund, and did not value its CDS based on market prices.[202] It was reasonable (and consistent with the contractual language) for Assured to calculate Loss in accordance with the value of the Transactions *to Assured*.[203] Because Assured held all of its CDS to maturity, the value of the Transactions to Assured was the sum of all of the fixed premium payments that Assured expected to receive, less the sum of any floating payments that Assured expected to make to cover actual losses.[204] Second, there were no market prices for the Transactions, as confirmed by the lack of bids at the Market Quotation auction, meaning there was no one willing to enter into any replacement transactions that would maintain Assured's bargain.[205] And the market prices of the other instruments that LBIE relies on were severely dislocated because of the financial crisis. As a result, those prices were not a reflection of the expected losses that Assured would have to pay under the Transactions.[206] Third, unlike LBIE's litigation-driven models, Assured's

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[200] LBIE Br. at 21, 23 (citing D/O at *14).
[201] Assured Br. at 59–67.
[202] *See id.* at 29–30 (citing Trial Tr. 2861:10–2863:18 (Bailenson), AX-70008 at 96 (Assured 2009 10-K)).
[203] Assured Br. at 59.
[204] *Id.* at 59–60.
[205] *Id.* at 62.
[206] *Id.* at 61–62. As discussed above, Rahl drew the same conclusion in her *Devonshire* report, where she explained that where a market is "detached from fundamental considerations of loss

calculation of Loss was performed in accordance with its regular-course-of-business models and was consistent with Assured's core expertise as an insurance company in valuing expected losses.[207] Finally, because these non-standard CDS transactions were not collateralized, and because Assured had no obligations to make payments based on market price fluctuations, market price movements simply were not relevant to their value to Assured.[208] Mark-to-market calculations merely reflected fluctuations in the market price for the reference obligations, and were not indicative of the underlying economics of the Transactions, or the performance of the reference obligations.[209] In sum, even if LBIE had been able to establish the existence of a uniform market practice for calculating Loss using market price (which it did not), it still would have been reasonable for Assured to depart from such a practice under the circumstances.

IV. LBIE Has Not Met Its Burden To Prove That Assured's Loss Calculation Reached An Unreasonable Result Or That It Is Entitled To Any Damages

LBIE's opening brief confirms that LBIE failed to carry its burden to establish that Assured's Loss calculation was unreasonable or that LBIE should be awarded the windfall damages it seeks. The record is clear that Assured's methodology for calculating its Loss on the Transactions satisfies each of the inquiries relevant to assessing its reasonableness and that the litigation-driven damages model created by LBIE's expert does not. Specifically, Assured's methodology (A) was designed to answer the question set out in the Agreement, namely, what was Assured's loss of bargain; (B) was developed through a robust process with independent checks and was used for multiple purposes; (C) generated results consistent with other evidence

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due to extraordinary illiquidity, actual loss projections provide[] a better indicator of long-term expected performance and value than [] market pricing." *Id*. at 61 (citing AX-90026 at 106 (Rahl Devonshire Report)).

[207] *Id*. at 62–67.

[208] *Id.* at 1, 29.

[209] *Id*. at 29–30.

of valuations of the Transactions; (D) relied on appropriate data inputs and well-supported judgments; and (E) was consistent with contemporaneous analysis by two independent ratings agencies. LBIE's opening brief does not raise any meaningful challenge to these assessments. Rather, LBIE ignores many of the key facts altogether and instead elevates a series of nitpicking criticisms, which are irrelevant or based on mischaracterizations of the record, and which, in most cases, would not even have materially changed Assured's Loss calculation.

A. Unlike LBIE's Model, Assured's Methodology Answers The Question Posed By The Agreement

Assured employed its regular-course-of-business model to solve for the "loss of bargain" it suffered on the 28 Transactions as a result of LBIE's default.[210] As explained above, Assured used a DCF model to determine the value of the economic bargain it had lost: it calculated the net present value of the premiums owed to it by LBIE and subtracted from that amount the net present value of the payments Assured expected to make to LBIE over the life of the Transactions.[211] In doing so, Assured properly considered the actual economic terms of the Transactions, which only required it to make floating payments for interest and principal shortfalls (if any) on the reference obligations as they came due.[212] LBIE does not and cannot dispute that Assured's methodology was designed to answer the question posed in the Agreement: namely, what was the economic bargain that Assured lost as a result of LBIE's default. And, as explained above, LBIE's opening brief largely ignores the specific economic terms of the Transactions, despite the fact that those terms were materially different from standard CDS.

LBIE's damages model, in contrast, does not even purport to calculate Assured's loss of

[210] JX-01 at 15 (1992 ISDA Master Agreement); *see also* Assured Br. at 23–24.
[211] *See* Assured Br. at 40–43.
[212] *See id.*

bargain. Rather, it explicitly aims to calculate a hypothetical "market price" for the Transactions based on various pricing proxies that relate to different transactions, with materially different terms than the Transactions in this case.[213] At summary judgment, LBIE took the position that, despite express language to the contrary in the Agreement, uniform market practice required parties to calculate Loss based on market prices or, as here, where market prices are not available, to use a hypothetical pricing model like the one created by its expert for this lawsuit.[214] As discussed in § III, *supra*, LBIE failed to meet its burden of showing the existence of a uniform custom and practice that effectively rewrites the Agreement. As a result, LBIE's model tries to answer a question that is legally irrelevant.[215]

Recognizing its inability to prove a uniform custom and practice that required Loss to be calculated based on a hypothetical pricing model like the one created by its expert for this lawsuit, LBIE at trial and in its opening brief argued in the alternative that Assured's methodology was unreasonable because it generated results that differed from the expected losses calculated by other market participants.[216] This is factually untrue: Assured's calculations were consistent with the two most reliable and transparent contemporaneous calculations, as discussed in § IV.E, *infra*. Tellingly, in making this argument, LBIE actually acknowledges that many other market participants, including independent rating agencies, regularly conducted

[213] *See* LBIE Br. at 42 ("Dr. Niculescu explained in detail how he used that available information to determine an objectively reasonable market value for each of the trades at issue.").
[214] D/O at *9.
[215] LBIE's arguments about whether market data was available to Assured, including information Assured used for its GAAP accounting, miss the point entirely. LBIE Br. 39–40. Assured's argument isn't premised on the unavailability of market pricing data; it is rather that pricing data, even where available, was not a reliable indicator of value and that it would have been unreasonable for Assured to rely on market prices or to calculate a market price because that approach would not have appropriately valued Assured's economic bargain.
[216] *See id*. at 61–69.

analysis of expected losses on the reference obligations.[217] And the evidence at trial established that LBIE itself performed similar "hold-to-maturity" analysis of the Transactions (generating results similar to Assured's) and that LBIE's own experts have used DCF models based on analysis of expected losses to calculate the value of terminated swaps in other instances.[218] In other words, far from being an idiosyncratic "insurance reserve model" or "the remotest of remote outliers compared to all of the other market participants,"[219] Assured's calculation of expected losses was consistent with common market practice.

B. Unlike LBIE's Model, Assured's Methodology Was Developed Through A Robust Process, Independently Verified And Used For Multiple Purposes

Assured introduced extensive, unrebutted evidence at trial that the methodology it used to calculate expected losses on the Transactions was developed through a robust process, verified by both internal stakeholders and its external auditor, and used for multiple purposes across Assured's business unrelated to this litigation.[220] This evidence strongly supports the conclusion that it was objectively reasonable for a party in Assured's position to use this well-established and regular-course-of-business methodology to determine its loss of bargain. LBIE's response in its opening brief is to ignore this evidence and instead attack a caricature.

For example, LBIE mischaracterizes Assured's determination of its expected losses on the Transactions as being based on a "handful of assumptions through an off-the-record conversation among Reserve Committee members about their personal beliefs."[221] This is a gross distortion of the facts. The record is clear that Assured's expected loss modeling was

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[217] *See* Assured Br. at 26, 64–65; *see also* Trial Tr. 3064:3–3065:18 (Prager) (explaining that Assured's initial loss severity parameter was right in the "middle of the pack" compared to other monolines and the ratings agencies).
[218] *See infra* § IV.C; *see also supra* § III.A.
[219] LBIE Br. at 1; *see also* Trial Tr. 20:23–25 (LBIE Opening).
[220] *See* Assured Br. at 26–30.
[221] LBIE Br. at 17, 56.

developed by experts in its surveillance group and by its Chief Actuary, Benjamin Rosenblum, based on consultation with and input from its Loss Reserve committee.[222] LBIE omits that this Committee was comprised of senior management with decades of experience, including Assured's CEO, CFO, Chief Surveillance Officer, and Chief Accounting Officer, and senior officers of FSA, which Assured had recently acquired.[223] LBIE also omits that Assured's methodology, far from being "off-the-record," was subject to extensive documentation, including a formal memo and presentation, which were introduced at trial.[224] LBIE also omits that this specific methodology, used by Assured for all transactions referencing subprime US RMBS, including but not limited to the ABX transactions in this case, was reviewed by the independent directors of Assured's ultimate parent holding company and independently audited by its external auditor, PwC.[225]

LBIE's attempts to denigrate Assured's methodology as "a subjective insurance reserve

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[222] *See* JX-34 at 8–10 (Statement of Calculations); *see also* AX-20020 (AMMC CLO Class A1R Spreadsheet); AX-20038 at 1 (Assured International RMBS Portfolio Email); Trial Tr. 1295:11–1300:20 (Rosenblum) (discussing surveillance runs for the CLO and CDO Transactions), 1300:21–1301:6 (Rosenblum), 1303:2–1310:24 (Rosenblum) (discussing surveillance runs for the UK RMBS Transactions), 1287:19–1288:2 (Rosenblum) (noting that the "expected losses for the ABX transactions in this case . . . were assessed [using] . . . the same scenarios that [they] ran for the rest of [their] subprime transactions"); *see also* Assured Br. § IV.

[223] *See* Trial Tr. 1237:20–1238:9 (Rosenblum) (testimony as to committee members), 1239:21–1241:3 (Rosenblum) (describing the Reserve Committee's process).

[224] *See, e.g.*, Trial Tr. 1253:17–1293:12 (Rosenblum) (discussing JX-70 (B. Rosenblum Q3 2009 Loss Reserve Memo); *see also* JX-71 (Assured Presentation on Q3 2009 Loss Projections)).

[225] *See* Trial Tr. 1237:8–1239:20 (Rosenblum) (describing the role of the surveillance department, the reserve committee, the audit committee, and independent auditors in the loss reserves process), 1238:23–1239:5 (Rosenblum), 2873:10–15 (Bailenson) (describing PwC's review as "a full audit" in which "[t]hey would agree with the assumptions and they issued an unqualified opinion for the company"), 3041:7–10 (Prager), 3042:1–2 (Prager), 3042:19–23 (Prager); *see also* Trial Tr. 1699:2–6 (Niculescu) ("THE COURT: [I]t is not lost on me that the same company audited – audited Assured and was also advising the committee. I don't know if that's a problem, I guess it remains to be seen, but it is – I've noticed that from the very beginning.").

model" also fall flat.[226] First, Assured's approach was no more subjective than any other models presented during trial. Models necessarily require the application of judgment, as LBIE's own damages expert conceded.[227] Second, the fact that Assured, as a regulated financial guarantee insurance company that is part of a group whose ultimate parent holding company is publicly-listed, used the same methodology to calculate expected losses for purposes of reporting to its regulators[228] supports the reasonableness of using that methodology to determine expected losses in this case. Third, LBIE ignores altogether the multiple other core business purposes for which Assured used the same methodology. These included underwriting new transactions,[229] monitoring its insured portfolio, which comprised "literally hundreds of transactions" unrelated to this action,[230] reporting to stockholders,[231] and valuing securities that it was considering purchasing for its investment portfolio.[232] The only reasonable conclusion to be drawn from the

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[226] *See* LBIE Br. at 1, 46.
[227] *See* Trial Tr. 1581:24–1582:5 (Niculescu).
[228] LX-244 at 14 (Assured Annual Statement filed with Maryland regulator (FY 2009)); *see also* Trial Tr. 2836:4–2838:10 (Bailenson) (discussing use in connection with regulatory filings and according to statutory requirements), 2935:13–22 (Bailenson) (discussing filing with Maryland regulators).
[229] *See* AX-20006 at 4 (Underwriting Memo for ABX 2006-2); *see also* Trial Tr. at 2144:24–2145:3 (Schozer) (describing Loss projection methods included in underwriting memo); JX-65 at 5 (Underwriting Memo for ABX 2007-01); Trial Tr. 2156:15–24 (Schozer) (explaining expected Loss process done in connection with underwriting).
[230] Trial Tr. 3040:10–12 (Prager), 1126:15–1127:10 (Rosenblum), 2213:3–17 (Schozer).
[231] *See* AX-70008 at 23–26, 96–97, 160 (Assured 2009 10-K); *see also* AX-70006 at 34–35, 48–49 (Assured Q2 2009); JX-50 at 68 (Assured Q2 2009 10-Q) (Assured used "stressed loss assumptions" to reflect its view of the "maximum probable deterioration likely to occur on these transactions"); Trial Tr. 2836:4–2838:10 (Bailenson) (discussing use in connection with regulatory filings and according to statutory requirements), 2862:16–18 (Bailenson) ("We were explaining to the reader that these non-GAAP measures were the most appropriate measure that investors should look at when evaluating the underlying economics of the company.").
[232] Trial Tr. 1284:7–1285:21 (Rosenblum) ("[I]f we saw a bond that we insured in the market, in many cases it was a good economic play, it was a good opportunistic economic play to go ahead and purchase that bond . . . We used the same loss reserve assumptions to figure out if it was a good economic play for us to purchase those bonds as we used . . . in a loss reserve analysis."); *see also id.* at 2859:8–2861:3 (Bailenson).

fact that Assured relied on the same methodology for a wide variety of business purposes is that Assured's methodology was designed to produce a reasonably accurate assessment of expected losses. Otherwise, Assured would have risked exposing itself to significant negative economic, regulatory and reputational consequences.

The comparison to how LBIE's damages model was created and used is revealing. LBIE's model was constructed by a paid expert solely for asserting a damages claim in this lawsuit, and it has never been reviewed or verified by anyone else or used for any other purpose. LBIE's opening brief asserts that Niculescu conducted his analysis using a "completely market-standard process," but that is based on nothing more than Niculescu's say-so.[233] LBIE failed to introduce any evidence of other market participants using Niculescu's model to value CDS generally, let alone CDS with the unique economic terms of the Transactions here.[234] And Niculescu admitted at trial that he did not rely on any surveys that "show[ed] market participants taking the same steps [he] took to determine how much they would pay for one of the CDS at issue in this case."[235] To the contrary, the evidence showed that 11 sophisticated financial institutions, who were given the opportunity to bid on the actual Transactions at issue in this case, could not possibly have valued the Transactions using Niculescu's approach; otherwise, they would have been willing to bid at least some amount.[236]

The lack of any independent verification or use of LBIE's damages model demonstrates that it is unreliable and should not be credited. Unlike Assured, LBIE faces no adverse consequences outside of this litigation if its damages model misstates the purported value of the

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[233] *See* LBIE Br. at 44.
[234] *See* Trial Tr. 3156:9–19 (Prager), 3163:1–3 (Prager).
[235] *See id.* at 1599:9–14 (Niculescu).
[236] *See infra* § IV.C.

Transactions to LBIE (as the evidence shows was the case).[237] Nor can LBIE claim that Niculescu, the creator of LBIE's damages model, was impartial. During the course of his testimony, Niculescu repeatedly omitted relevant information where that information was unhelpful to LBIE's litigation position, even if it appeared in sources that he explicitly relied on. When confronted with one of several such examples during cross-examination, Niculescu explained that he did not disclose information that "would make Assured's number look more reasonable" because "I thought that was not my responsibility. I didn't disclose it. I concluded that was Assured's responsibility rather than mine."[238] In light of what is effectively an admission by LBIE's damages expert that he was not impartial, LBIE's criticism of Assured for failing to hire a third party to calculate Assured's Loss cannot be taken seriously.[239] Not only was Assured not required to do so by the Agreement, but Assured's use of an independently validated, regular-course-of-business methodology was clearly more reliable than hiring a paid expert to create a one-off, biased calculation.

C. Unlike LBIE's Model, Assured's Methodology Generated A Valuation Consistent With The Pre-Litigation Assessments Of LBIE And Others

There was extensive evidence at trial that LBIE's candid internal assessment—before it filed this lawsuit—was that the Transactions had little to no value to LBIE in the real world, as well as evidence of similar assessments by others in the market, including those that participated in the Market Quotation auction. LBIE devoted several trial days and many pages in its opening brief, to evidence of the purported valuations of CDS transactions with materially different terms between it and third parties, but LBIE fails to grapple with the evidence that relates to the

[237] *See infra* § IV.D.
[238] *See* Trial Tr. 1549:20–1550:8 (Niculescu); *see also id.* at 1631:17–25 (Niculescu) (conceding that he did not disclose the search parameters used to search for relevant documents in CMRA's archives).
[239] LBIE Br. at 56.

Transactions at issue in this case. That is because the evidence that is actually relevant to the value of these Transactions plainly demonstrates that Assured's Loss calculation was reasonable and that LBIE is seeking an unjust windfall based on its own default.

LBIE cannot explain away the fact that Assured's Loss calculation is consistent with the internal assessments about the value of the Transactions made by LBIE before it filed this lawsuit. This includes assessments in emails, memos and PowerPoints authored by senior PwC personnel such as Paul Copley (appointed as a Joint Administrator for LBIE in November 2011)[240] and by two of LBIE's "most knowledgeable" traders, Juan Quintas and Francisco Cuccovillo, who were retained even after LBIE's insolvency.[241] For example, Assured's calculation aligns with LBIE's conclusion in October 2008 that "[t]he CDS Contract exposure to [Assured] is, in most scenarios, unlikely to generate cash for LBIE."[242] Like Assured's assessment of the Transactions, LBIE's pre-litigation analysis stressed the "overall credit soundness" of the underlying reference obligations, and LBIE's internal modeling concluded that, if the Transactions were held until maturity, the total floating payments owed by Assured would only exceed the premium payments by between $10 and $21 million.[243] LBIE's valuation expert, Niculescu, conceded at trial that "you could probably fairly characterize [LBIE's internal pre-litigation analysis] as an attempt to do a [] present value of all future losses on the contracts in question. . . . [Y]ou could summarize it as a hold-to-maturity analysis."[244] And he agreed that Assured's Loss calculation was solving for the same question—"what losses Assured would

[240] *See* Copley Dep. Tr. 26:24–27:5.
[241] Trial Tr. 573:24–574:7 (Viegas).
[242] JX-67 at 4 (Valuation Memorandum); *see also* Assured Br. § III(B).
[243] JX-67 at 3–4 (Valuation Memorandum); *see also* Trial Tr. 1660:23–1661:7 (Niculescu) (stating that the Valuation Memorandum was a "hold-to-maturity" analysis).
[244] Trial Tr. 1661:3–7 (Niculescu).

have been obligated to pay if the [Transactions] had been held to maturity."[245] The fact that LBIE and Assured independently reached similar valuations is compelling evidence of the reasonableness of Assured's calculation. In stark contrast, LBIE's pre-litigation analysis cannot be squared with Niculescu's litigation-driven model, which generates a valuation that is hundreds of millions of dollars in LBIE's favor. Not surprisingly, Niculescu admitted that he did not reference LBIE's internal pre-litigation analysis or any other internal LBIE assessments of the value of the Transactions in formulating his damages model or in his attacks on the reasonableness of Assured's calculation.[246]

Nor can LBIE explain away the real-world evidence that no market participant was willing to pay even one dollar to step into the shoes of LBIE in the Transactions. At trial and in its opening brief, LBIE stated that Niculescu attempted to determine what a hypothetical third party would be willing to pay to enter into the Transactions.[247] But that puzzle was already solved. The results of the Market Quotation auction demonstrated that no market participant was willing to pay *anything* for the Transactions, which fundamentally calls into question the validity of Niculescu's litigation exercise and his claim that the Transactions were theoretically worth

[245] *Id.* at 1658:12–16 (Niculescu).
[246] *Id.* at 1660:14–17 (Niculescu). Other internal LBIE materials prepared at the time reflected similar judgments. For example, LBIE, in creating a special financial structure to aid in its efforts in assigning the Transactions, stated that it would cash in if "either [Assured] . . . does not default or the [reference obligations] do not default (or both)," which LBIE explained was "a high probability scenario." AX-30010 at 8 (LBIE Slide Deck on Credit Exposure to Assured). Similarly, in December 2008, Billy Radicopoulos, another LBIE trader, sent an email to Viegas stating that a market-based valuation of the Transactions "grossly exaggerates" their value. AX-30020 at 1 (Radicopoulos Email to Viegas).
[247] *See* LBIE Br. at 42 ("Dr. Niculescu explained in detail how he used that available information to determine an objectively reasonable market value for each of the trades at issue.").

hundreds of millions of dollars to LBIE.[248]

Recognizing that the auction evidence is fatal to its damages claim, LBIE tries to diminish the significance of the auction by retreading arguments—such as that the auction was a mere pricing exercise—that this Court already rejected and that are contrary to the express contemporaneous comments of market participants.[249] In its summary judgment decision dismissing the auction-related claim, this Court concluded that LBIE has failed to challenge "in any material respect" Craig Pirrong's opinion that "the structure and design of the auction was reasonably calculated to increase the likelihood that the Market Quotation process would be successful."[250] LBIE's conjectures about why attempts to obtain Market Quotations in other circumstances may not have been successful are completely irrelevant.[251] There is no place for such speculation because we actually know the principal reasons why the auction resulted in no bids here. As this Court recognized, Assured's inability to obtain bids from counterparties "was a result of a lack of appetite in the market for these products."[252] This conclusion is further reinforced by LBIE's failed novation attempts. LBIE's assertion that Assured was somehow responsible for the lack of market appetite is unsupported by the evidence at trial, which

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[248] *See, e.g.*, Assured Br. at 20–23. Tellingly, Niculescu never attempted to validate his models by looking at how market prices subsequently moved in a normalized period. *See* Trial Tr. 1708:4–5 (Niculescu) (noting that he did not look at data subsequent to the summer of 2009).
[249] *See, e.g.*, LBIE Br. at 15.
[250] D/O at *6.
[251] *See* LBIE Br. at 15; *see also* AX-40005 at 1 (BNP Paribas Email to Henderson) (regarding refusal to bid at Market Quotation auction); *see also* AX-40006 at 1 (JPMC Email to Henderson) (same); AX-40007 at 1 (Morgan Stanley Email to Henderson) (same); AX-40003 at 1 (UBS Email to Henderson) (same); AX-40004 at 1 (Credit Suisse Email to Henderson) (same); AX-40002 at 1 (HSBC Email to Henderson) (same); AX-40001 at 1 (Citibank Email to Henderson) (same); AX-40010 at 1 (RBS Email to Henderson) (same); AX-40009 at 1 (Nomura Email to Henderson) (same); AX-40011 at 1 (Barclays Email to Henderson) (same); LX-411 at 1 (Barclays Internal Email) (same); AX-20028 (Henderson Internal Email) (same).
[252] D/O at *5 (quoting Pirrong Initial Report at 1, 39–40).

demonstrated that LBIE, like Assured, was unable to identify anyone willing to pay even a single dollar to step into LBIE's shoes in the Transactions.[253]

The only evidence relating to valuations of the actual Transactions in this case that LBIE relied on at trial were three indicative bids[254] that provide no meaningful information about the value of the Transactions. Contemporaneous emails from LBIE personnel explicitly described the indicative bids as part of an attempt by LBIE to bolster its litigation position before Assured terminated the Transactions.[255] LBIE provided incomplete information (including redacting all references to the fact that the counterparty was a monoline), and, in response, the bidders made clear they were unwilling to provide firm quotes and instead gave heavily caveated "indications," in most cases only for partial amounts.[256] And the only bidder to provide a complete indicative bid was Quintas, the former LBIE trader who had analyzed the Transactions closely before he began working at Nomura, but who unbelievably pretended not to know who the counterparty was.[257] Recognizing the extensive evidence of foul play surrounding these bids, LBIE's valuation expert, Niculescu, despite having relied on these bids in his expert disclosures, retreated from them at trial, stating that he was no longer relying on them and that he was "not

[253] *See* Trial Tr. 2203:19–20 (Schozer) (from Lehman's insolvency through July 2009, Schozer was not aware of any proposal from LBIE to novate or assign the Transactions).
[254] *See id.* at 560:22–563:20 (Viegas) ("Well, from our perspective, those [indicative] quotes would be what we called market color, would be indicative market data of where these transactions or these underlyings would be trading at at [sic] that stage on termination date."), 562:11–563:17 (Viegas) (stating that the indicative bids signified to him that the trades were valuable).
[255] *See* AX-30013 at 1 (Copley Email to Pearson); *see also* Assured Br. at 17.
[256] *See* LX-73 (Porter Email to Unidentified Banks) (containing documents LBIE sent to potential bidders where it redacted Assured's name from the confirms with a permanent marker); *see also* LX-74 (Porter Email to Viegas Re: Indicative Bids) (compiling all indicative bids received).
[257] *See id.*

ready to opine on their reliability."[258] LBIE's continued reliance in its opening brief on these indicative bids to try to suggest that Nomura was willing to pay hundreds of millions of dollars for the Transactions strains credulity.[259]

The extensive real-world evidence that market participants were unwilling to pay a single dollar to enter into LBIE's shoes on the Transactions highlights the inapplicability of the so-called "cross-check principle," which LBIE urges the Court to apply here. As this Court explained in its summary judgment decision, the "cross-check principle . . . stands for the proposition that a Non-[d]efaulting Party's Loss (however calculated) should generally be within the range of what the market would pay for a replacement transaction."[260] Putting aside that there is no New York or U.S. law applying this standard or principle, the two British cases LBIE relies upon in its attempt to demonstrate that the cross-check principle should be applied here—*Anthracite*[261] and *Brittania Bulk*—addressed a significantly different fact pattern than that in this case. First, LBIE fails to point out that neither of the determining parties in those cases used market prices as the basis for its Loss calculation.[262] Further, in both cases, the issue in dispute was whether the Non-defaulting Parties, in making their Loss calculations, needed to value "clean," meaning to assume that, but for the default and resulting termination, the Transactions

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[258] *See* Trial Tr. 4042:22–4043:11 (Niculescu).
[259] *See* LBIE Br. at 13.
[260] D/O at *16.
[261] *Anthracite* applies a highly deferential standard in evaluating the Non-defaulting Party's Loss calculation, *see Anthracite Rated Invs., Ltd. v. Lehman Bros. Fin. S.A. in Liquidation,* [2011] EWHC (Ch) 1822 [117] (Eng.) (noting that Loss is "intended to be illuminated by reference to the general common law (or New York law) meaning," which is "identifying the non-defaulting party's loss of bargain"). LBIE cannot cherry-pick the foreign law principles it likes while ignoring other core aspects of the same foreign court's analysis.
[262] LBIE tellingly omits that the *Anthracite* court affirmed that "the definition of 'Loss' in Section 14 of the 1992 Master Agreement entitles, but does not oblige, the [N]on-defaulting [P]arty to determine its Loss by reference to quotations of relevant rates or prices from one or more leading dealers in the relevant markets." *Id.* at [114].

would have continued through the life of the Agreements and all payments would have been made by both parties.[263] There is no dispute here that Assured did exactly that. And in both cases, the parties selected Second Method and Loss as the primary method, meaning that, unlike Assured here, they were not calculating Loss after receiving the results from a Market Quotation auction demonstrating that there were no executable bids. The cross-check doctrine has never been applied to a situation like the one here, where a party fell back to Loss after Market Quotation failed to generate any bids that could be used as a cross-check.[264] Even more attenuated is the idea of testing Loss against hypothetical quotations generated by a defaulting party's litigation model, as LBIE advocates here. As *Anthracite* noted, for market prices to be used as a determiner of value (based on the cost of a replacement transaction), there has to be "a market for the obtaining of a replacement contract."[265] So, even if some version of the cross-check test were applied here, the results of the Market Quotation auction support the reasonableness of Assured's Loss calculation because there was no "market for the obtaining of a replacement contract," as no one was willing to pay anything to take LBIE's place in the Transactions.[266] In contrast, Niculescu's calculation would fail the cross-check test, as his model

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[263] Assured satisfies this "nil loss" scenario discussed in these cases because Assured fairly took into account the anticipated floating payments it would have had to make to Lehman in calculating Loss. *See Brittania Bulk Plc [in liquidation] v. Pioneer Nav. Ltd.*, [2011] EWHC (Comm) 692 [14] (Eng.).
[264] *See* Def's Pre-Trial Br. at 22, D.I. 731 (May 24, 2021) ("Assured's Pre-Trial Br.").
[265] *Anthracite*, [2011] EWHC (Ch) at [117].
[266] At summary judgment, this Court suggested that the cross-check principle may be applicable to this case and welcomed the parties to further argue it at trial. D/O at *16. Based on the evidence produced by Assured at trial and discussed in § IV.C, the indicative bids were heavily caveated, partial bids (except in the case of the Nomura, where Juan Quintas feigned to not recognize the Transactions) and should not be given any weight nor serve as a number against which Assured's Loss can be checked. Further, application of the cross-check principle in this case assumes a false equivalency between Assured's loss and LBIE's loss, as the indicative bids (payable to LBIE) were for stepping into LBIE's shoes, and did not purport to measure the loss of bargain suffered by Assured.

cannot be squared with the results of the Market Quotation auction.

D. Unlike LBIE's Model, Assured's Methodology Relied On Timely And Relevant Data Inputs And Well-Supported Judgments

LBIE's opening brief fails to come up with any material criticism of Assured's valuation methodologies. *First*, LBIE has not presented any basis to challenge the actual calculation of expected loss on the 26 UK RMBS, CLO, and CDO transactions. *Second,* for the two ABX transactions, Assured made use of observable and timely data to calculate its expected losses through 2012—the same data relied on by the rating agencies, banks, and LBIE's own valuation expert. *Third*, Assured applied well-supported judgments to the 2009 data to calculate its expected losses beyond 2012, while LBIE's criticisms of Assured's model are cherry-picked, trivial, and wrong. *Fourth*, LBIE's expert, Niculescu, used inappropriate proxies and data points in his model, rendering it untethered from any real-world application or verification.

1. <u>LBIE Failed To Raise Any Material Criticism Of Assured's Valuation Of The 26 UK RMBS, CLO And CDO Transactions</u>

The evidence at trial showed that Assured's surveillance group conducted rigorous analysis of the 26 UK RMBS, CLO, and CDO Transactions in the ordinary course of business.[267] Even under "stress case" scenarios, this analysis showed that there would be no losses to the tranches insured by Assured because of the extensive structural protections built into these reference obligations.[268] LBIE failed to present any evidence at trial that called into question the reasonableness of Assured's calculations on these 26 Transactions. To the contrary, Assured's conclusions were consistent with its detailed underwriting analysis, which stated that, due to the framework of the Transactions, Assured would not incur a single dollar of loss on the UK

[267] *See* Assured Br. at 23–30. Because Assured submitted actual evidence to support the reasonableness of its determination with respect to these 26 Transactions, the cases on which LBIE relies are inapposite. *See* LBIE Br. at 47.
[268] *See* Assured Br. at 12–15.

RMBS, unless "home prices . . . [had] declined and losses . . . [were] more severe than it ever had been experienced in the U.K. market including [during] the bombing of London and the economic fallout around those times," or on the CLOs, unless losses were "two times [historic] averages on the corporate loan losses."[269] Assured's conclusions were also consistent with the only other "expected loss" analysis on these Transactions in the record—namely the analysis conducted by LBIE before it filed this lawsuit. Like Assured, LBIE concluded that, if held to maturity, these Transactions would be assets for Assured.[270]

Recognizing that it has no substantive basis to challenge the reasonableness of Assured's determination, LBIE tries instead in its opening brief to re-litigate evidentiary quibbles based on its claim that Rosenblum lacked sufficient personal knowledge about the analysis performed by Assured's surveillance group.[271] The Court has already correctly rejected that argument.[272] Contrary to LBIE's misdirection about Rosenblum's knowledge,[273] Rosenblum testified at trial that he "spent a lot of time . . . with the surveillance department,"[274] that spreadsheets like the one presented at trial were shared with Rosenblum in the ordinary course of business,[275] and that he had full knowledge of the data that Assured's surveillance group generally considered in

[269] Trial Tr. 3001:23–3002:4 (Prager); *see also id.* at 2094:5–2095:5 (Schozer), 2119:2–2120:15 (Schozer); AX-20004 at 2 (Assured Sept. 2007 Underwriting Memo) (noting that Assured was protected between 1.66 and 2.84 times against the worst case historic losses experienced by the U.K. residential mortgage market in the late 1980s); AX-10001 at 2, 5–6 (Ballyrock CDO Underwriting Memo); *see also* Assured Br. § IV.
[270] JX-67 at 2 (Valuation Memorandum).
[271] *See* LBIE Br. at 31–36.
[272] Trial Tr. 1297:14–21 (Rosenblum) (Court agreeing that "as long as [Assured has] someone from the company who can identify [the surveillance reports] as a record from the company, that the sources of the data are prepared and maintained in the ordinary course of business and at or about the time of the events in question. That's a sufficient foundation.").
[273] *See* LBIE Br. at 16 (discussing AX-20020 (AMMC CLO Class A1R Spreadsheet)).
[274] Trial Tr. 1234:10–11 (Rosenblum).
[275] Trial Tr. 1297:2–7 (Rosenblum), 1298:6–10 (Rosenblum).

constructing similar spreadsheets.[276] There is also no factual basis for LBIE's argument that the markets for UK RMBS and CLOs were "functioning" and that there were determinable market prices at the time of Assured's Loss calculation.[277] LBIE's own expert conceded that actual market pricing was unavailable for CDS on UK RMBS or CLOs, that the indicative prices he used for CDS on UK RMBS had materially different terms from the UK RMBS Transactions here, and that the only proxies he was able to find for the CLO Transactions reflected the prices of a generic CLO index and CDS on junk bonds (neither being appropriate here).[278]

2. Assured Used Industry-Standard, Up-To-Date Data To Calculate Loss For The Two ABX Transactions

There was unrebutted testimony at trial that the initial parameters that Assured used in its calculation—the default rate, loss severity, and prepayment—were consistent with then-current data reporting actual observed defaults, delinquencies and losses on the specific loans in the securities underlying the ABX Transactions.[279] This is not surprising because Assured relied on actual market information on how the loans in the RMBS that make up the ABX baskets were performing at the time. This information was available through trustee reports and Intex, the platform used by Assured for its expected loss calculations, which LBIE's experts agreed was the industry-standard,[280] and included—how many borrowers were delinquent, how late the

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[276] Trial Tr. 1233:1–23 (Rosenblum).
[277] LBIE Br. at 39, 40 n.34.
[278] Assured Br. at 69–70.
[279] Trial Tr. 1565:21–1556:23 (Niculescu) (conceding that Assured's initial default rate of 23.5% was consistent with observed default rates for the ABX at the time); *see also id.* at 3061:15–20 (Prager) (explaining that Niculescu used the same initial default rate as Assured); *id.* at 3065:8–3066:8 (describing the loss severity rates of different market participants and explaining that a rate of 70% was historically very high); *see also* ADX03 at 11 ("Initial Loss Severity Assumptions") (depicting Assured's loss severity rate as in the middle of the range of rates used by other market participants).
[280] *Id.* at 1213:21–1214:2 (Rosenblum); *see also id.* at 1660:5–8 (Niculescu), 1951:19–21 (Adamidou) ("So we had Intex; [which was used in developing] complicated models[.]"), 1721:23–25 (Niculescu) (describing Intex as a "data library that allows people to calculate []

delinquent borrowers were, how many borrowers were in default, the severity of losses on defaulted loans, and how many borrowers were prepaying their loans.[281] That same data was also recorded in a report created by Credit Suisse that LBIE proffered as an exhibit.[282] In fact, the initial default rate of 23.5% used by Assured was even more favorable to LBIE, as it was slightly higher than the more current observed default rate reflected in the Credit Suisse report.

To distract from the fact Assured's initial parameters were consistent with actual, then-current observable data and with the initial parameters used by other market participants, LBIE makes two irrelevant (and plain wrong) complaints about the data Assured relied on to generate their initial parameters. *First*, LBIE incorrectly asserts that the liquidation rate data Assured used to generate the initial default rate parameter was "stale," because it was based on data from the last six months of 2008.[283] But the liquidation rate is merely a mechanical aspect of how Assured calculated the initial default rate parameter in its modeling, which was also based on current performance data reflecting actual delinquencies as of 2009.[284] And LBIE's own expert conceded that the actual initial default rate Assured calculated using the supposedly stale liquidation rates was completely consistent with observed market data showing actual default

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cash flows . . . [and] values"), 1722:6–7 (Niculescu) (explaining that he has used Intex throughout his career for modeling), 3004:22–3005:5 (Prager), 1233:1–23 (Rosenblum), 937:15–20 (Bruce) (explaining that he used Intex when modeling, noting that it "was the market standard one from modeling CDOs with RMBS and other constituents").

[281] *Id.* at 1213:7–18 (Rosenblum).

[282] LX263 at "Results by As_of_date" tab, Row 41 for ABX 06-2 transactions, Row 64 for ABX 07-1 transactions (Credit Suisse ABX Aug. 2009 Spreadsheet); *see also* Trial Tr. 4057:17–4060:4 (Niculescu) (discussing the monthly default rates in the 2009 Credit Suisse Remittance Report).

[283] LBIE Br. at 62–64; *see also id.* at 17.

[284] Trial Tr. 1266:3–1267:5 (Rosenblum) (explaining how Assured calculated a default rate); *id.* at 1159:10–1160:20 (Rosenblum) (explaining the difference between liquidation rates and default rates).

rates for the relevant RMBS in 2009.[285] That Assured reached an initial default rate in line with the actually observed default rates in 2009 while applying liquidation data from the second half of 2008 is not surprising, because, as Rosenblum explained at trial, "liquidation rates don't change very much" over a short time.[286] In fact, the liquidation rates Assured used from the last six months of 2008 were actually slightly higher than the liquidation rates observed in 2009 (which stands to reason because borrowers had been hit harder during the last six months of 2008 than they were in 2009, when the housing market was stabilizing).[287]

Second, LBIE complains that "AGFP started its loss severity curve off at 70%, even though the most recent data showed that loss severities among affected mortgages was actually 74%."[288] But the record showed that a large number of market participants reported the initial loss severity parameters they were using in their models at this time, and that most were clustered between 60% and 75%.[289] Many, including JP Morgan and Moody's, reported using somewhat lower rates than Assured, and a few used slightly higher rates, placing Assured "right

[285] *See* Trial Tr. 1565:21–1556:23 (Niculescu) (conceding that Assured's initial default rate of 23.5% was in the range of 20 to 25%, the observed initial default rate as reflected in LDX-06 at 7 ("ABX Default Rates Had Risen to Over 20%")); *see also id.* at 3061:15–20 (Prager), 3062:18–3063:10 (Prager); LX263 (Credit Suisse ABX Aug. 2009 Spreadsheet).
[286] *See* Trial Tr. 1259:22–23 (Rosenblum); *see also id.* at 3052:23–3054:5 (Prager) ("I disagree with [Niculescu's] characterization that this [data] was stale.").
[287] *Id.* at 3053:7–21 (Prager); *see also id.* at 1257:8–1260:14 (Rosenblum) (describing Goldman Sachs report as "conservative" because it "did not include the benefit, or the potential benefit, of any government programs . . . [and Assured's view was that Goldman's numbers were] a very good proxy for what we thought were appropriate liquidation rates"), 1552:20–1555:3 (Niculescu) (comparing the higher liquidation rates Assured used in its model (citing JX-71 at 22 (Assured Presentation on Q3 2009 Loss Projections)) with the "lower rates" in the 2009 JP Morgan report (citing LX-119 at 10 (JP Morgan July 2009 Report))).
[288] LBIE Br. at 18.
[289] *See* Trial Tr. 3065:8–3066:8 (Prager) (describing the loss severity rates of different market participants and explaining that a rate of 70% was historically very high); *see also* ADX03-11 ("Initial Loss Severity Assumptions").

in the middle of the pack."[290] In contrast, Niculescu cherry-picked the highest loss severity rate he could find from among many market participants at 75% as a point of comparison at trial.[291]

3. Assured's Judgments On How To Model Future Defaults For The ABX Transactions Were Well Supported

The key driver of the difference between the calculations that Assured made and the alternative expected loss calculations offered by Niculescu has nothing to do with initial parameters or the use of timely and relevant data by Assured. Instead, this difference is a product of judgments that Assured made as to what percentage of borrowers were likely to default from 2012 onwards. Niculescu conceded that no model could take raw data from 2009 and project the state of the housing market beyond 2012 without the developer of the model exercising such judgment.[292] Assured's judgment was that default rates for the loans collateralizing these securities would decline to levels more consistent with historical norms by approximately 2012.[293] That judgment was well-supported for two reasons.

First, Assured's judgment took into account the unprecedented government intervention to stabilize the housing market, including several programs launched by the Obama administration in 2009 that were specifically designed to decrease defaults by borrowers. In constructing its model, Assured made the professional judgment that these government programs would over time result in decreased defaults by subprime borrowers, which supported calibrating

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[290] Trial Tr. 3065:13–14 (Prager); *see also* LBIE Br. at 65–66.
[291] Trial Tr. 1393:14–20 (Niculescu); *see also id.* at 1412:2–11 (Niculescu).
[292] *Id.* at 1581:24–1582:5 (Niculescu); *see also id.* at 1644:4–15 (Niculescu).
[293] LBIE misleadingly argues that if Assured's parameters in its modeling "had been just a little bit more pessimistic . . . you would have seen . . . significant losses." LBIE Br. at 57; *see also* Trial Tr. 1750:17–20 (Niculescu). But LBIE cannot point to any evidence in the factual record suggesting that Assured's methodology was calibrated to try to minimize the amount of tranche level losses Assured projected on the ABX. To the contrary, it is undisputed that Assured's methodology was designed to deal with all subprime, first-lien U.S. RMBS—not just the 20 such RMBS referenced in the ABX. Trial Tr. 1287:19–1288:14 (Rosenblum).

Assured's modeling to provide for default rates to begin returning to historical averages by 2012.[294] Others, including Moody's, made similar judgments, noting that, "[p]otential government-sponsored modification programs, notably the Homeowner Affordability and Stability Plan (HASP), lead us to reduce our current cumulative loss forecasts."[295] Niculescu's claim at trial, which LBIE repeats in its opening brief, that the data on these programs "had come in already"[296] by November 2008 is plainly wrong. President Obama had not even taken office by November 2008 and the relevant programs had not been adopted or implemented.[297]

Second, Assured's judgment was supported by a widely recognized economic phenomenon in the housing market, referred to as burnout or "seasoning."[298] Burnout refers to the fact that, within any large pool of borrowers, those who are most likely to default typically do so at a significantly higher rate in the initial years after they purchase their home. In contrast, borrowers within the pool who are able to stay current on their mortgage payments for the first several years have a much lower likelihood of defaulting than the overall pool of borrowers.[299]

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[294] Assured Br. at 64.
[295] AX-50083 at 7 (Moody's March 2009 Report).
[296] LBIE Br. at 58.
[297] For instance, the Obama Administration was responsible for the Home Affordable Modification Program (HAMP) and the Home Affordable Refinance Program (HARP), which were expected by Moody's and others to contribute to stabilizing the housing market. Trial Tr. 3014:9–17 (Prager); *see also* AX-50044 at 3 (Moody's Aug. 2009 Report). As discussed in the Bank of America report LBIE cites, other important government assistance efforts, like the Homeowner Affordability and Stability Plan (HASP) and the Making Home Affordable program, were not implemented until 2009. LX-123 at 26 (Bank of America July 2009 Report).
[298] JX-71 at 25 (Assured Presentation on Q3 2009 Loss Projections).
[299] *Id.*; *see also* Trial Tr. 3066:17–3067:2 (Prager), 1269:16–1270:9 (Rosenblum). In its opening brief, LBIE relies on misleading ellipses to characterize Rosenblum's testimony at trial as "agree[ing] that economic pressures resulted in an extremely high likelihood that subprime borrowers would default on their mortgages." LBIE Br. at 52 (citing Trial Tr. 1366:8–1367:16 (Rosenblum)). But, as is clear from his full testimony, Rosenblum was responding to a hypothetical scenario posed by LBIE's counsel in which he was asked to assume that a borrower was unable to make mortgage payments. In that context, Rosenblum agreed that such a borrower would default.

As a result, the pool becomes more "seasoned" over time, meaning that default rates are expected to decrease. As Assured's witnesses explained at trial, "somebody who has made their payments for 24 months is more likely to make their payment on the 25th month,"[300] and the borrowers that remain current "through when the economy is starting to recover . . . should be a better quality borrower than the overall pool and . . . the [borrowers] that defaulted to date."[301] Given the economic stresses that many borrowers faced during 2008, it was reasonable to believe that the "burnout" phenomenon would be even more pronounced, as borrowers who had managed to stay current on mortgage payments through 2012, by which time the financial crisis was expected to have abated, were even less likely to default in later years.[302] Moody's explicitly discussed its expectation that burnout would curtail the severity and duration of losses for U.S. subprime mortgages.[303]

Despite criticizing Assured's judgment that default rates would, over the course of several years, return to historic levels, LBIE fails to engage on these key substantive factors that led Assured to reach that judgment.[304] LBIE also does not—and cannot—explain how it could be reasonable to ignore these factors altogether and instead assume that default rates on the

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[300] Trial Tr. 1269:16–1270:9 (Rosenblum).
[301] *Id.* at 3066:17–3067:2 (Prager).
[302] JX-71 at 25 (Assured Presentation on Q3 2009 Loss Projections) ("High initial [credit default rate] may indicate that most of the weak loans are being eliminated from the pool, suggesting that the drop in [credit default rate] will be steeper later."); *see also* Trial Tr. 1269:16–1271:2 (Rosenblum) (explaining seasoning, as referenced in JX-71 at 24 (Assured Presentation on Q3 2009 Loss Projections), and why it "generally improves the performance of a mortgage pool"); Trial Tr. 3066:17–19 (Prager) ("The other factor that will go into play with default rates is, there's a burnout effect. The worse borrowers . . . are the ones that will default early. And so if you made it through 2009 . . . those borrowers that are left currently current should be a better quality borrower[.]").
[303] Assured Br. § IV; *see also* AX-50083 at 6–7 (Moody's March 2009 Report); ADX03-12 ("Assured's Subprime Default Analysis"); Trial Tr. 3344:24–3345:5 (Prager).
[304] LBIE Br. at 14–20.

relevant mortgages would remain significantly higher than historical averages for *more than 12 years* after the onset of the financial crisis.[305] Yet this is precisely the assumption that Niculescu used when he created his alternative models of expected losses. This patently unreasonable assumption was a primary reason that Niculescu's expected loss models showed such large losses, as David Prager explained at trial.[306] And, as discussed further below in § IV.E, many independent government and academic experts specifically disagreed with this assumption in concluding that indicative prices being reported for the ABX were dislocated from actual value, demonstrating that there was no market consensus in 2009 supporting Niculescu's position.

In short, LBIE fails to raise any meaningful challenge to the reasonableness of Assured's judgment that default rates would return to historical norms in 2012 and beyond. Instead, it offers unfounded quibbles with data and assumptions that would have had little to no impact on the results of Assured's analysis in any event.

- *The Impact of Home Prices.* LBIE chides Assured for reaching the judgment that loss severities would ultimately, over the course of several years, decline to historical norms, arguing that "[i]t takes only middle school math to disprove" that this was possible in light of housing price depreciation.[307] But the purported "math" on which LBIE relies is completely flawed, as Niculescu's calculations were based on an assumption (which he did not make explicit, let alone defend) that losses would be 25% greater than what was actually indicated by current housing prices. The Citigroup report on which Niculescu purported to rely for these calculations actually conceded that there was a "valid

[305] Trial Tr. 3078:6–3079:15 (Prager).
[306] *Id.* at 3078:9–11 (Prager) (explaining that for Niculescu to "formulaically [] get to a high loss number, [he had] to assume that the elevated default rates continue for a very long period of time").
[307] LBIE Br. at 59–60.

argument" that the discount was inappropriate because it was based on stale data from before the housing crisis.[308] In addition, LBIE fails to address the fact that other market participants were projecting a similar decrease in loss severities over time, as discussed in § IV.D below. Finally, even if Assured had used a somewhat higher loss severity in its modeling for 2012 and later years, as LBIE urges, it would not have had a material impact on its Loss calculation, because at that point Assured reasonably projected that defaults would be much smaller. As explained by Prager at trial, the proper question is "how many losses are you applying that [loss] severity to?"[309]

- *Prepayments.* LBIE also bizarrely continues to challenge Assured's assumption that prepayment rates would return to historical norms over the course of several years,[310] despite the fact that this assumption actually increased Assured's projected losses.[311] This is because when borrowers prepay their loans, the lender actually receives less money over time because it loses the opportunity to collect years of additional interest payments.[312] This phenomenon is well-documented, and referred to in the mortgage-

[308] AX-50077 at 2 n.3 (Citigroup Report). Niculescu's use of this assumption can be seen in the fact that the "sale price" he uses in his demonstrative (LDX06 at 09) is 25% less than the "market value." *See* LDX06-09 ("20% Home Price Increase Would Only Minimally Reduce Severities"). This is after already assuming that the "market value" had fallen 45% from when the loan was originated, which the Citigroup report made clear was based solely on data from California, AX-50077 at 1 (Citigroup Report), and was inconsistent with Niculescu's own demonstrative claiming that "Home Prices Had Fallen 33% Since Spring 2006 Peak." LDX-06-5. Niculescu similarly tried to hide the fact that housing prices were already beginning to stabilize by mid-2009, including by cutting off that demonstrative at April 2009, omitting data showing that in May 2009 housing prices stopped falling for the first time since early 2007, and that housing prices actually rose in June and July 2009. *See* AX-90198 at 1 (Case-Shiller U.S. National Home Price Index); Trial Tr. 1542:5–1544:19 (Niculescu).
[309] Trial Tr. 3072:23–24 (Prager).
[310] LBIE Br. at 19, 66–69.
[311] Trial Tr. 1186:16–22 (Rosenblum); *see also* JX-71 at 26 (Assured Presentation on Q3 2009 Loss Projections).
[312] Trial Tr. 1273:11–1274:3 (Rosenblum).

backed securities industry as "excess spread."[313] Because of the loss of excess spread, Assured's use of an increased prepayment rate in its modelling for the ABX transactions actually caused its model to project greater losses. LBIE also ignores the fact that Assured's reasonable judgment that prepayment rates would return to historical norms over time was consistent with the judgments it made about how default rates and severities would evolve, because if the housing market stabilized in 2010, as was then credibly projected, all three rates would be expected to return to historical levels.[314]

- _Roll Rates._ In criticizing Assured's use of a two-year 26% default rate for currently-current borrowers, LBIE compares this rate to a lifetime roll rate—another term for liquidation rate[315]—of 79% from a JP Morgan report.[316] This comparison is nonsensical. As an initial matter, LBIE mischaracterizes JP Morgan's default rate of 79% as "recent data."[317] In actuality, that rate is not data at all, but a projection by JP Morgan of future defaults. Furthermore, as the JP Morgan report makes clear and as acknowledged by Niculescu at trial,[318] JP Morgan's rate of 79% is a lifetime roll rate, reflecting how many currently-current borrowers JP Morgan projected would default over the lifetime of the mortgage. In another table in the same report, JP Morgan provides projections for five-year roll rates, reflecting how many currently current borrowers would default within five

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313 *Id.* at 1273:23 (Rosenblum).
314 *Id.* at 1216:4–18 (Rosenblum) (explaining that Assured projected increased prepayment rates back to historically normal levels to be consistent with its assumption that the default rates and loss severities would return to normal); *see also id.* at 3065:21–3066:8 (Prager) (explaining the consistency of Assured's modelling assumptions with respect to default rates and loss severity).
315 *Id.* at 3055:3–10. As discussed in § IV.D.2, the irrelevance of LBIE's argument about liquidation rates applies here as well.
316 LBIE Br. at 58.
317 *Id.*
318 LX-119 at 10 (JP Morgan July 2009 Report); *see also* Trial Tr. 1556:5–11 (Niculescu).

years.[319] JP Morgan's five year roll rate in that report was 48%, a far cry from 79%.[320] Neither of these JP Morgan tables provide a meaningful point of comparison for Assured's two-year roll rate, and indeed several of the rates used by Assured are actually more pessimistic than those that appear in JP Morgan's five-year roll rates.[321]

- *2001 Housing Crisis.* LBIE also misleadingly argues that Assured's methodology was flawed because it "reli[ed] on memories" of a 2001 housing crisis.[322] But Rosenblum testified about numerous data points and factors that Assured considered and relied on in its expected loss analysis for the different categories of transactions it insured, including subprime US RMBS, like those that comprise the ABX.[323] LBIE ignores the majority of these factors because they are plainly reasonable. Among other things, Assured considered observable data on the performance of the relevant loans,[324] a variety of macroeconomic data including housing market forecasts[325] and information regarding government initiatives,[326] and the decades of experience of other members on the Loss Reserve committee.[327] Instead, LBIE seizes on snippets of testimony in which Rosenblum recalled that certain members of the committee had experience with modeling

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[319] LX-119 at 10 (JP Morgan July 2009 Report).
[320] *Id.*
[321] Trial Tr. 1553:22–1558:1 (Niculescu).
[322] LBIE Br. at 59.
[323] Trial Tr. 1233:1–3 (Rosenblum) (explaining that Assured's surveillance department "reviewed any information that they could get a hold of"); *see also id.* at 1217:1–17 (Rosenblum) ("[I]t is hard to overstate how much work was done by Assured [] in 2009, trying to get . . . a reasonable estimate of the projections.").
[324] *Id.* at 1213:7–17 (Rosenblum).
[325] *Id.* at 1307:5–13 (Rosenblum); *see also id.* at 1280:8–18 (Rosenblum); JX-71 at 34 (Assured Presentation on Q3 2009 Loss Projections).
[326] Trial Tr. 1271:25–1272:9 (Rosenblum).
[327] *Id.* at 1237:10–17 (Rosenblum) (explaining that the Loss Reserve committee had "a lot of deep industry experience to fall on for creating [Assured's] judgments around [Assured's] reserves"); Assured Br. at 24–25, 28.

mortgages that had been affected by a more localized housing downturn in 2001, and that this was an "instructive . . . past cris[i]s [and] extrapolation point for future crises."[328] LBIE's attempt to play "gotcha" on this single data point only highlights that LBIE has ignored Rosenblum's other, more relevant testimony explaining the full mosaic of information that Assured considered in assessing expected losses.

- *Teaser and Floating Rates.* LBIE misleadingly suggests that the market was expecting higher borrower defaults on RMBS in the ABX transactions because they contained mortgages originated in 2006 with "teaser" rates and those rates would soon "balloon" (i.e., would convert to an adjustable rate mortgage).[329] This is a red herring. While it is true that some of the relevant loans converted to adjustable rate mortgages, as Prager explained, those rates are reset based off of the prime rate, and between 2006 and 2009 the prime rate had actually dropped significantly (by 5 percentage points) and interest rates were expected to stay at historic lows based on federal monetary policy.[330]

4. Niculescu's Model For The Transactions Used Inappropriate Proxies And Data Points

In contrast, Niculescu's litigation-driven model—which relied on data points for materially different transactions than the Transactions in this case and a series of subjective, one-off adjustments—produced a calculation that is not only legally irrelevant, for the reasons discussed above, but also fundamentally unreliable. LBIE fails to address these flaws, which were exposed during Niculescu's cross-examination and summarized in Assured's opening brief.[331] And the claims LBIE makes in its opening brief only underscore what the evidence

[328] Trial Tr. 1175:11–13 (Rosenblum).
[329] LBIE Br. at 49–50.
[330] Trial Tr. 3069:13–3070:22 (Prager).
[331] Assured Br. 68–73.

showed at trial: no one else used Niculescu's model to value transactions in the real world.

First, LBIE's claims that Niculescu simply looked to "market prices" for CDS like those at issue in conducting his valuations is false.[332] LBIE did not introduce a single example of a so-called "market price" for a transaction with the same terms as the ones that govern the Transactions between Assured and LBIE.[333] As Niculescu himself conceded, he could not obtain relevant data points for his model, because the CDS market was largely over-the-counter and lacked transparent pricing.[334] Instead, Niculescu resorted to proxies, and then used his own subjective judgment to adjust these proxies in a variety of ways to try to construct a so-called replacement price for the Transactions.[335] And, as explained in Assured's opening brief,[336] many of those proxies were cherry-picked and inappropriate.[337]

Second, LBIE's claim that Niculescu's application of a "bid-offer adjustment" is "consistent with market practice" is also incorrect.[338] Niculescu's sole support for this portion of his modeling was the Lehman Framework,[339] but there is no dispute that the Lehman Framework reflected a settlement achieved by Lehman with a number of big banks for transactions with different terms, that it only became public years after the Transactions here were terminated, and

[332] LBIE Br. at 42–46; *see* also Trial Tr. 1446:13–24 (Niculescu), 1448:25–1449:10 (Niculescu).
[333] *See* AX-90030 at 6 (ISDA Collateralization Practices Market Review 2010) (reporting that 97% of credit derivatives are collateralized, unlike the Transactions here); *see also* Trial Tr. 3028:25–3029:13 (Prager) (explaining that Markit does not reflect actual market prices, but that it reflects "mid market quotes" or "an indicative number").
[334] Trial Tr. 1590:23–1591:5 (Niculescu); *see also id*. at 1591:19–22 (Niculescu), 1617:21–1618:5 (Niculescu), 1625:11–13 (Niculescu), 1660:14–17 (Niculescu).
[335] Assured Br. at 69–70.
[336] Assured Br. at 45, 70; *see also* Trial Tr. 1595:22–1596:9, 1597:19–23, 1599:9–14, 1691:9–1692:10 (Niculescu).
[337] Trial Tr. 1593:5–7 (Niculescu), 1595:7–1596:9 (Niculescu), 1614:19–1615:3 (Niculescu).
[338] *See* LBIE Br. at 44–45.
[339] Trial Tr. 1463:18–1464:3 (Niculescu) (explaining that he determined his bid-to-mid adjustment by starting with the Lehman Derivatives Claims Framework); *see also* LX-35 (Lehman Derivatives Claims Settlement Framework).

that Lehman expressly disclaimed it as having any precedential value.[340]

Finally, LBIE's claims about the CVA calculations performed by Niculescu are at odds with the evidence, including the opinions of the foremost expert on CVA modelling, Professor Jon Gregory at Cambridge University. CVA is a pricing adjustment to the replacement value of a transaction based on the creditworthiness of the counterparty and the expectations it will be able to perform its obligations. In defending Niculescu's model, LBIE claims that, even if one were to assume a 100% correlation between the failure of the reference obligations and AGFP's own failure, that would only negligibly reduce the replacement value of the trades to $227 million in LBIE's favor.[341] But, as Gregory has explained, if you have 100% correlation, the value of the trades should be zero.[342] It defies common sense that someone would pay more than $200 million for transactions where there was a 100% certainty that events triggering the protection seller's obligation to make payments would also cause the seller to fail and be unable to pay anything. LBIE's assertion to the contrary shows that Niculescu's model is divorced from basic economic theory and cannot provide a stable foundation for a claim of damages.

E. Assured's Calculation Of Expected Losses Was Consistent With Contemporaneous Calculations Published By Moody's And S&P

In addition to being nearly identical to LBIE's own internal pre-litigation calculations of expected losses for the Transactions,[343] Assured's calculations were also clustered closely together with those published by two independent rating agencies: Moody's projected expected

[340] Assured Br. 55–56.
[341] *See* LBIE Br. at 46.
[342] AX-50050 at 5 (2008 Jon Gregory article); *see also* Trial Tr. 3769:16–24 (Pirrong) (agreeing with Gregory that CDS purchased from monolines on high quality assets were "effectively worthless" at this time).
[343] *See supra* § IV.C.

losses of 30% for the relevant collateral, S&P projected 32%, and Assured projected 28%.[344] Critically, of all the evidence of third-party expected loss calculations admitted at trial, only Moody's and S&P disclosed in detail the methodologies they used to reach their calculations. Those disclosures provide a basis from which the Court can assess the reliability of their results (unlike the bank reports on which LBIE purports to rely), and they also reveal that the rating agencies *considered the same economic factors* that Assured considered (including the seasoning of the borrower pool and anticipated government relief programs) and *reached similar judgments* about how those factors would cause defaults and severities to evolve over time.[345]

LBIE's attempts to cast aspersions on the reliability of Moody's and S&P's estimates ring hollow. Niculescu himself relied extensively on other portions of their reports for his analysis, although he conveniently ignored their expected loss calculations (or pretended he did not understand them) until he was confronted with them on cross-examination.[346] And there is no support for LBIE's suggestion that the rating agencies' estimates were less reliable than those of the banks. The evidence at trial showed that many market participants did not predict the full extent of the financial crisis—including Lehman and many of the failed banks whose research

[344] Trial Tr. 3103:9–14 (Prager), 3107:17–24 (Prager); *see also* AX-50083 at 1 (Moody's March 2009 Report); AX-50031 at 4–5 (S&P July 2009 Report); AX-50044 at 2 (Moody's Aug. 2009 Report).
[345] *See* AX-50083 at 6, 7 (Moody's March 2009 Report); *see also* Trial Tr. 3066:17–3067:2 (Prager), 3339:18–3342:24 (Prager), 3346:16–3348:10 (Prager).
[346] *See* Trial Tr. 1799:20–1800:7 (Niculescu); *see also id.* at 3932:11–3933:1 (Niculescu) (conceding that he relied on Moody's and S&P reports in his expert reports), 3933:13–21 (Niculescu) (conceding he did not at any point say information from Moody's was unreliable in his JX-43 expert report), 3976:16–19 (Niculescu) (conceding that he relied on Moody's Aug. 2009 Report), 1562:23–25 (Niculescu) (conceding that he relied on S&P's July 2009 Report), 1558:14–1566:23 (Niculescu) (being confronted with omission of expected loss projections published by Moody's and S&P despite having cited to Moody's and S&P for other purposes in his expert reports).

capabilities Niculescu praised.[347] It also showed that Moody's and S&P responded by implementing in 2008 and 2009 "a number of measures to enhance the quality, independence, and transparency of [their] ratings."[348] In contrast, the bank reports cited by LBIE continued in 2009 to explicitly warn that their findings "may not be independent from the proprietary interests of [their] trading desks" and as a result may present "conflict[s of] . . . interest."[349]

The expected loss figures that Niculescu purports to derive from three bank reports are not even in the same ballpark as those of Assured, Moody's and S&P, but are hundreds of millions of dollars larger. LBIE does not try to explain this chasm, but the reasons were apparent at trial. *First*, Niculescu again cherry-picked the data most favorable to his client. For example, the JP Morgan report he cites was one of multiple reports issued by JP Morgan at the time. Another JP Morgan report, also published in July 2009 by many of the same analysts, actually projected the same amount of cumulative losses as Moody's (30%).[350]

Second, although the banks provided almost no disclosure regarding their methodologies, it is clear from the face of their reports that they were performing an entirely different analysis. Rather than modeling expected losses based on actual observed current data and informed judgments about future economic trends, the banks described the figures they published as being "implied" by current market prices.[351] Such a calculation is only meaningful if market prices are being driven by expectations about the future performance of the relevant securities, but, as

[347] *Id.* at 3949:1–3 (Niculescu); *see also id.* at 3950:6–23 (Niculescu).
[348] AX-50093 at 1 (Apr. 2009 Testimony of Moody's CEO to SEC).
[349] LX-119 at 13 (July 2009 JP Morgan Report); *see also* Trial Tr. 3368:1–21 (Prager).
[350] *See* Trial Tr. 3376:12–19 (Prager); *see also id.* at 3373:1-3374: 23 (Prager) (discussing AX-50089) (JP Morgan Second Report).
[351] LX-137 (Barclays ABX Weekly Recap). This Barclays report, on which Niculescu relies, uses the term market-implied seven times despite being only five pages long. *Id.*; *see also* Trial Tr. 3364:12–3365:1 (Prager); *id.* at 3578:14–20 (Pirrong); *id.* at 4019:1–4 (Niculescu) (noting limited disclosure by Barclays of its methodology).

Niculescu conceded at trial, there was no consensus that this was the case in 2009.[352] To the contrary, government authorities and neutral experts were warning that market prices were "inconsistent with any reasonable assumptions for future default rates" and there was "no default rate high enough to support observed prices."[353] In other words, bonds were trading at low prices not because everyone in the market believed that there would be large losses, but because nobody wanted to buy them.[354] The United States Department of Treasury described the issue as a "negative economic cycle" in which declining asset prices were causing deleveraging, which was in turn causing further price declines and so on.[355] As a result of this dislocation, market price was not a reliable indicator of future losses, which are the critical factor in determining the value of the Transactions here because Assured's obligations were not tied to the trading prices of the bonds, but rather to insuring actual losses as they came due.[356]

LBIE effectively gives up the game on its claim that there is a single, "objective" methodology for calculating Loss in its opening brief, because, in addition to asserting that it is owed $485 million in damages,[357] it also puts forward a new alternative damages calculation,

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[352] Trial Tr. 1636:14–19 (Niculescu) (conceding "there were . . . others who didn't share [his] views about illiquidity in the market").
[353] AX-50056 at 25 (Bear's Lair 2009); *see also id.* at 4 (Bear's Lair 2009).
[354] Assured Br. at 32 n. 220 (citing Trial Tr. 3391:4–10 (Prager)); *see also* AX-50056 at 4 (Bear's Lair 2009).
[355] Trial Tr. 3024:8–3025:14 (Prager).
[356] *Id.* at 3363:12–3365:21 (Prager); (discussing LX-137 at 2 (Barclays ABX Weekly Recap)) ("Q. Given the dislocation in the trading market between the price of the ABX and fundamental value, Mr. Prager, how reliable would it be to calculate projected expected losses based upon the market price of the ABX at this time? A. I don't think that the market price is a reliable indicator of the future expected losses.").
[357] LBIE Br. at 73. LBIE's $485 million damages claim self-servingly excludes its own expert's calculation that potential counterparties would have actually paid Assured a substantially small amount for replacement transactions because of its credit risk. As explained above, Niculescu actually substantially understates that reduction and LBIE's arguments for ignoring credit risk have no legal support. *See supra* Section I.

which it failed to introduce at trial or preview in more than a decade of litigation: LBIE now asserts that the Court could alternatively assess damages by averaging certain "contemporaneous projections," which it calculates to be $262 million for the ABX Transactions.[358] To generate this inflated figure, LBIE includes the four largest bank report calculations—which as explained above were not even attempting to measure actual expected losses—and excludes the expected loss calculation published by Moody's, despite extensive evidence supporting its reliability.[359]

In short, there is nothing remotely objective or reasonable about LBIE's various purported damages calculations. LBIE is readily willing to urge on the Court any methodology that generates a windfall recovery for it. And thus a ruling for LBIE would not promote the certainty in the derivatives market that LBIE claims is important.[360] The only "legal certainty" that is important in a simple contract dispute such as this one is that a party like Assured will not be held to have breached its agreement when it reasonably follows the language of the contract.

CONCLUSION

For the reasons set out above and in Assured's opening brief, the Court should deny LBIE's claim for breach of contract, grant AGFP's counterclaims against LBIE for breach of contract and for attorneys' fees and costs, and enter judgment in favor of Assured.

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[358] LBIE Br. at 74. Tellingly, LBIE never introduced evidence of a any reliable third-party analysis showing expected losses on any of the other 26 Transactions in this case.

[359] *See* LBIE Br. at 74. LBIE also purports to rely on a calculation published by Fitch despite the fact that Fitch, unlike Moody's and S&P, did not explain its methodology and the "source" LBIE cited is nothing more than a spreadsheet. LX-137 (Barclays ABX Weekly Recap).

[360] LBIE presented no evidence that this dispute or its resolution would have any impact on the derivatives market generally; to the contrary, there was extensive evidence showing that the derivatives market has changed substantially since the Financial Crisis. *See, e.g.*, Trial Tr. 1229:21–23 (Rosenblum) (explaining that "by 2009 [Assured] could not sell [CDS] protection anymore."); 2880:3–17 (Bailenson) (discussing AX-70008, Assured's 2009 10-K, and explaining that in 2009 "there were no trades . . . out there for financial guarantors using credit derivative contracts. It was a very thin illiquid market.").

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Respectfully submitted,

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