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UNITED STATES DISTRICT COURT

FOR THE CENTRAL DISTRICT OF CALIFORNIA

WESTERN DIVISION

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

MICHAEL W. PERRY AND A. SCOTT KEYS,

Defendants.

Case No. CV 11-1309-R JC(x)

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT MICHAEL W. PERRY'S MOTION IN LIMINE TO EXCLUDE ANALYST TESTIMONY

Date: June 18, 2012
Time: 10:00am
Judge: Honorable Manuel L. Real
Courtroom: No. 8

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I. INTRODUCTION

Defendant Michael W. Perry seeks an order precluding the SEC from calling stock analysts to provide lay opinion testimony regarding the purported materiality of alleged omissions in IndyMac's May 12, 2008 SEC filings.

In the Ninth Circuit, admissible lay opinion testimony must be "based upon personal observation and recollection of concrete facts." *United States v. Beck*, 418 F.3d 1008, 1015 (9th Cir. 2005) (internal quotation marks omitted). Here, however, the SEC seeks to have IndyMac stock analysts assume the truth of facts alleged in the SEC's Complaint concerning information purportedly omitted from IndyMac's May 2008 filings, and then speculate about how they might have reacted in May 2008 had those purported "facts" been known to them at the time. The SEC seeks such speculation even from two analysts who had ceased covering IndyMac by May 2008. This does not come close to satisfying the Ninth Circuit standard. The testimony should be excluded.

II. BACKGROUND

After the Court's May 21 decision granting Mr. Perry's motion for partial summary judgment, only two issues remain in this case: whether IndyMac needed to disclose additional details in its May 12, 2008 SEC filings concerning (a) an $18 million capital contribution from IndyMac Bancorp to IndyMac Bank (the "Bank"); and (b) the Office of Thrift Supervision's notification to IndyMac in February 2008 that the Bank no longer needed to calculate its capital ratio by double risk-weighting its subprime assets. The SEC alleges that such additional information was necessary to make investors aware of the Bank's tenuous hold on well-capitalized status. In fact, IndyMac's filings made it abundantly clear that the Bank was on the verge of ceasing to be well capitalized, and the May 12, 2008 10-Q even specifically disclosed that, if a downgrade of bonds held by the Bank had occurred just 24 days earlier, the Bank's capital ratio at March 31 would have been 9.27 percent—a full 73 basis points below the well-capitalized minimum of

10 percent. *See* Michael W. Perry's Memorandum of Contentions of Fact and Law (Dkt. No. 67) at 17 (¶ III.F.8).

The SEC intends to call seven IndyMac stock analysts to testify at trial that the purported omission of information about the $18 million capital contribution and risk-weighting of subprime assets was nonetheless material.[1] Five of these analysts (Jason Arnold, Frederick Cannon, Bruce Harting, Matthew Howlett, and Robert Lacoursiere) published reports on IndyMac that were publicly disclosed. The other two (Gregory Haendel and Michael Rogers) provided analysis and recommendation for internal use at their firms, which purchased Bank preferred securities in 2007.

Two of the analysts (Haendel and Lacoursiere) had stopped covering IndyMac before May 2008. *See* Decl. of Gregory D. Haendel (May 25, 2012) (Exh. A to Maskay Decl.) ¶ 3; Bank of America Equity Research Report (Mar. 28, 2008) (Exh. B to Maskay Decl.). By May 2008, all five of the others had noted the profound capital adequacy challenges IndyMac faced or had downgraded their estimates for IndyMac stock. *See, e.g.*, Decl. of Jason Arnold (May 3, 2012) (Exh. C to Maskay Decl.) ¶¶ 7-8.

According to the SEC, the seven analysts are expected to opine that additional disclosures by IndyMac about the $18 million capital contribution and the subprime double risk-weighting issue "would have been important for their assessment of IndyMac's common stock" or that they "believed" the disclosures IndyMac made were false and misleading. *See* SEC Mem. of Contentions of Fact and Law (Dkt. No. 71), at 26-27. The SEC obtained declarations from some of

[1] The SEC's Witness List names the following analysts: Jason Arnold, Frederick Cannon, Bruce Harting, Gregory Haendel, Matthew Howlett, Robert Lacoursiere, and Michael Rogers. *See* Dkt. No. 69.

the analysts in 2011 and 2012, which the SEC claims express such views. *See, e.g.*, Decl. of Gregory D. Haendel (Dec. 23, 2011) (Exh. D to Maskay Decl.).

In obtaining these declarations, the SEC asked the analysts to assume the truth of the SEC's characterizations of the information purportedly omitted from IndyMac's SEC filings, and to speculate about how they might have reacted in May 2008—years before the declarations were signed—had they known such purported facts. At the same time, the SEC—which purports to demand full and accurate disclosure from others—did *not* disclose to the analysts critical information about what actually transpired. For instance, the SEC did not disclose the crucial fact that the Bank's principal federal regulator, the Office of Thrift Supervision ("OTS"), approved IndyMac Bank including the $18 million capital contribution in calculating the Bank's capital ratio for the first quarter of 2008, and that IndyMac's outside auditor, Ernst & Young LLP ("E&Y"), likewise had no objection to the Bank doing so. *See, e.g.*, Decl. of Jason Arnold (May 3, 2012) (Exh. C to Maskay Decl.) ¶ 11; Cannon Deposition Trans. (Exh. E to Maskay Decl.) at 79:6-80:4. Indeed, analyst Jason Arnold has acknowledged that the SEC's misinformation seriously skewed the views he expressed in his declaration. Decl. of Jason Arnold (May 3, 2012) (Exh. C to Maskay Decl.) ¶ 11.

As explained below, the speculative nature of the analyst testimony sought by the SEC renders such testimony inadmissible under the Federal Rules of Evidence.

III. STANDARD OF REVIEW

Under Federal Rule of Evidence 701, testimony by a lay witness in the form of an opinion must be:

(a) rationally based on the witness's perception;

(b) helpful to clearly understanding the witness's testimony or to determining a fact in issue; and

(c) not based on scientific, technical, or other specialized knowledge within the scope of Rule 702.

A lay witness[2] must also have "personal knowledge of the matter" to which he testifies, and must offer relevant evidence. Fed. R. Evid. 602, 401, 402.

The analyst testimony that the SEC seeks to introduce here will violate all of these tenets.

IV. ARGUMENT

A. THE ANALYST OPINIONS SOUGHT BY THE SEC ARE PURE HINDSIGHT SPECULATION AND ARE NOT BASED ON PERCEPTION OR PERSONAL KNOWLEDGE.

Federal Rule of Evidence 701(a) requires lay opinion testimony to be "rationally based on the witness's perception." Such testimony must thus be "based upon personal observation and recollection of concrete facts." *Beck*, 418 F.3d at 1015 (internal quotation marks omitted); *see also United States v. Skeet*, 665 F.2d 983, 985 (9th Cir. 1982). Consistent with this rule, courts have limited analyst testimony "to what the analyst read, heard, asked about, and/or otherwise learned about [a company] from its disclosures." *United States v. Tomasetta*, No. 10-cr-1205, 2012 WL 1080293, at *4 (S.D.N.Y. Mar. 30, 2012); *see also United States v. Rigas*, No. 02-cr-1236, 2004 WL 360444, at *1 (S.D.N.Y. Feb. 26, 2004) (permitting analysts to testify "as to interaction with a Defendant, the questions they asked, the reasons why they asked those questions and why they can recall the answers they received").

The analyst testimony that the SEC seeks to introduce here cannot satisfy this requirement. That is most clear as to Lacoursiere and Haendel. Those two analysts were no longer even covering IndyMac in May 2008. Lacoursiere left his

[2] The SEC has not designated any of the analysts as expert witnesses or disclosed their testimony as required by Federal Rule of Civil Procedure 26(a)(2).

employer, Bank of America, in February 2008 and issued his last report regarding IndyMac on February 11. Bank of America then formally terminated coverage of IndyMac on March 28. *See* Bank of America Equity Research Report (Mar. 28, 2008) (Exh. B to Maskay Decl.).

Similarly, Haendel's firm completely liquidated its holdings of IndyMac Bank preferred stock by March 27, 2008. *See* Decl. of Gregory D. Haendel (May 25, 2012) (Exh. A to Maskay Decl.) ¶ 3. Because his firm "no longer had any financial interest in IndyMac or its securities, [Haendel] did not review the 10-Q or 8-K (or exhibits thereto) filed by IndyMac Bancorp with the SEC on May 12, 2008, and [he] did not listen to the investor conference call held by IndyMac Bancorp on that date." *Id.* ¶ 4. Accordingly, nothing Lacoursiere and Haendel say about the information purportedly omitted from IndyMac's May 12 filings could possibly be "based upon personal observation and recollection of concrete facts" (*Beck*, 418 F.3d at 1015), or upon "what the analyst read, heard, asked about, and/or otherwise learned about [IndyMac] from its disclosures" (*Tomasetta*, 2012 WL 1080293, at *4).

The testimony of the other five analysts is likewise inadmissible. As explained above, the only remaining claims in this case concern information that purportedly was *omitted* from IndyMac's May 2008 filings. By definition, such information could not have been personally observed by the analysts. At most, the analysts would be able to speculate about how they might have reacted in May 2008 had the information purportedly withheld been known to them at the time.

Such speculation will necessarily be shaped by what the analysts are told about the facts and circumstances surrounding the transactions long after the fact. For example, analyst Jason Arnold signed a declaration for the SEC stating that he might have had concerns about management integrity in May 2008 had he known more about the $18 million capital contribution. That, however, was because the SEC deliberately concealed from Arnold the fact that the contribution was

reviewed and approved by the OTS, and that E&Y had no objection to the transaction. Upon being informed of these facts, Arnold stated in a supplemental declaration that the transaction would *not* have raised concerns about management integrity. *See* Decl. of Jason Arnold (May 3, 2012) (Exh. C to Maskay Decl.) ¶ 11. This underscores that the analyst testimony the SEC seeks to introduce will be based on hindsight speculation rather than on what the analysts personally observed in May 2008. As such, the testimony is inadmissible.

B. ANALYST OPINIONS BASED ON HINDSIGHT SPECULATION ARE NEITHER "HELPFUL" NOR RELEVANT.

Moreover, lay witness opinions are only admissible if they are "helpful to clearly understanding the witness's testimony or to determining a fact in issue," Fed. R. Evid. 701(b), and are relevant under Federal Rules of Evidence 401 and 402. That is not the case here.

The SEC seeks to offer the analyst testimony to demonstrate the materiality of the alleged omissions in IndyMac's SEC filings. The standard for assessing materiality, however, is "an objective one." *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 445, 96 S. Ct. 2126, 2130, 48 L. Ed. 2d 757 (1976). Materiality must be evaluated "from the perspective of a reasonable investor *at the time of the misrepresentation*, not from the perspective of a reasonable investor looking back on how events unfolded." *Gebhardt v. ConAgra Foods, Inc.*, 335 F.3d 824, 830-31 (8th Cir. 2003) (emphasis added). Likewise, the importance of alleged omissions "should not be judged with the advantage of hindsight." *Id.*

As explained above, the analyst testimony that the SEC seeks to introduce here is not based on what the analysts perceived in May 2008. The SEC rather seeks to have the analysts judge the importance of alleged omissions from IndyMac's SEC filings with the benefit of hindsight. Such testimony is neither helpful nor relevant to assessing materiality.

Indeed, courts that have allowed analyst testimony have been careful to exclude "testimony regarding whether the analysts thought that the [relevant] disclosures would have been material to an investor, because such testimony invades the province of the [finder of fact]." *Tomasetta*, 2012 WL 1080293, at *4; *see also Milton v. Van Dorn Co.*, 961 F.2d 965, 969 (1st Cir. 1992) ("The mere fact that an investor might find information interesting or desirable is not sufficient to satisfy the materiality requirement."). The SEC seeks to introduce analyst testimony here for the *precise purpose* of trying to demonstrate what "would have been material to an investor." For this further reason, the analyst testimony here should not be allowed.

Finally, lay opinion is helpful to understanding a witness's testimony only "when a witness cannot explain through factual testimony the combination of circumstances that led him to formulate that opinion." *Fireman's Fund Ins. Cos. v. Alaskan Pride P'ship*, 106 F.3d 1465, 1468 (9th Cir. 1997). Here, the analysts' speculation about how they might have reacted in May 2008 to additional information about the $18 million capital contribution and the risk-weighting issue will be the sum total of their testimony. They have no relevant "factual testimony" to explain through their speculative opinions.

C. THE ANALYSTS' OPINIONS WOULD BE BASED ON "SPECIALIZED KNOWLEDGE" AND ARE THEREFORE INADMISSIBLE UNDER RULE 701(c).

The analyst testimony should also be excluded because it would be impermissibly "based on . . . specialized knowledge" and is thus not admissible opinion testimony by a lay witness under Federal Rule of Evidence 701(c).

When a witness's knowledge is based not on his "perceptions," but instead on his "education, training, and experience," it constitutes "specialized knowledge." *United States v. Figueroa-Lopez*, 125 F.3d 1241, 1246 (9th Cir. 1997). It is not permissible under Rule 701(c) for a party to draw on an analyst's specialized knowledge to "elicit testimony regarding what the analyst believed [a

company] should have disclosed; or how [the company] should have accounted for [certain] financials; or [to] let the analyst hypothesize as to how any alternative disclosure would have affected his analysis at the relevant time." *Tomasetta*, 2012 WL 1080293, at *4.

The SEC seeks to do precisely that here. The SEC proposes to have the analysts testify as percipient witnesses, not as experts. Based on the analysts' specialized knowledge and experience analyzing the financials of IndyMac and companies like it, the SEC then proposes to "elicit testimony regarding what the analyst believed [IndyMac] should have disclosed" and to "hypothesize as to how any alternative disclosure would have affected his analysis at the relevant time." *Id.* That is not permissible opinion testimony by a lay witness under Rule 701. For this further reason, the testimony should be excluded.

CONCLUSION

For the foregoing reasons, the seven analysts identified by the SEC should not be permitted to testify at trial.

Dated: May 25, 2012

Respectfully submitted,

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