FREQUENTLY ASKED QUESTIONS

Beverly Adkins, *et al.* v. Morgan Stanley, filed October 15, 2012 in U.S. District Court for the Southern District of New York.

What is the lawsuit about?

This lawsuit alleges that Morgan Stanley discriminated against black homeowners in the Detroit region and violated federal and Michigan law with its mortgage securitization business. As a result of Morgan Stanley's policies, New Century Mortgage Corp. targeted the origination of loans with unjustifiably high costs and risk of foreclosure in minority neighborhoods and to minority borrowers. Morgan Stanley provided the up-front funding and set loan volume goals and established criteria for the mortgage terms.

How does this lawsuit differ from other suits that have been filed recently in connection with mortgage-backed securities and securitization?

This case is the first that draws the connection between securitization and racial discrimination, and it will be the first to affirm the principle that when Wall Street banks interact with home mortgage finance they must comply with the Fair Housing Act and other federal anti-discrimination laws. It is also the first case where a prospective class of affected homeowners victimized by subprime lending abuses is directly suing an investment bank rather than one of the subprime lenders whose businesses were designed to feed Wall Street's securitization machine.

Who is suing in the case announced today?

The case is being filed in federal district court in New York on behalf of five black Detroit homeowners who were victimized by Morgan Stanley's practice of purchasing and financing predatory mortgages that were later bundled into tranches of mortgage-backed securities, and Michigan Legal Services, which expended considerable resources helping affected homeowners.

Is this a class-action suit?

The legal team connected to the case will seek to have the case certified as a class-action suit after it is filed.

If the class is granted how many people could join the lawsuit as part of the class?

We estimate there are approximately 5,000-6,000 people in the Detroit region who were affected by these practices.

How did this occur?

Morgan Stanley ramped up its mortgage-backed securities business starting in 2004. It needed a reliable supply of subprime loans it could then securitize and sell to investors, including financial institutions and pension funds. To ensure that supply, it became the principal financier of New Century Mortgage Corp., a leading subprime lender. Because mortgage-backed securities earned Morgan hefty fees, it pressed New Century to provide a high volume of loans that became increasingly risky and economically unviable for the homeowners. Our clients obtained their loans through New Century.

Why was this wrong?

Our clients were sold loans defined by a combination of high-risk and high-cost features, including hefty prepayment penalties and increased payments after an introductory period. These Combined Risk Loans were disproportionately sold to black homeowners, and the black community was adversely impacted. Because minority residents of the Detroit region have been subjected to decades of housing and lending discrimination, and had fewer alternative sources of credit, New Century faced less competition and these borrowers were easy to target with unfavorable loans.

How do we know this?

An analysis of filings required under the Home Mortgage Disclosure Act, shows that black borrowers in the Detroit region received 10 times as many New Century subprime loans as New Century prime loans from 2004 to 2006. In contrast, white borrowers received 3.7 times as many subprime loans than prime loans. Controlling for income, loan amount and other loan features reported, black New Century customers in the Detroit area were 70 percent more likely to receive subprime loans than white borrowers.

But if it was New Century that issued the loans, why go after Morgan Stanley?

Morgan Stanley, as the primary buyer of New Century loans, fundamentally guided the company's lending business. It provided New Century the credit needed to originate the loans, so it would have more mortgages to securitize. Morgan Stanley also dictated the terms of the loans it wanted and ultimately purchased for its securitized pools. Morgan Stanley continued funding New Century right up to the point when New Century declared bankruptcy in 2007. With an increasing appetite for risky, high-interest loans, Morgan Stanley incentivized New Century to issue mortgages that would have a high rate of foreclosure.

If Morgan Stanley was just trying to make a profit, how is that discrimination?

The law places the burden on Morgan Stanley to make sure that its policies do not result in discrimination. In passing the Fair Housing Act and the Equal Credit Opportunity Act, Congress recognized it is not enough to outlaw overt racism; it is also necessary to monitor all policies, even those that appear neutral, to make sure they do not perpetuate or magnify historical patterns of discrimination. Our clients were given loans defined by a combination of high-risk features, including hefty prepayment penalties, increased payments after an introductory period and the failure to disclose that payments did not include taxes or insurance.

Did the actions alleged occur only in Detroit?

The plaintiffs all live in Detroit and this suit concerns the harms they suffered. At the same time, the practices we allege Morgan Stanley engaged in were endemic during the last decade throughout much of the financial services industry and across the nation.

Wasn't Morgan Stanley sued by the state of Massachusetts in a similar case?

Yes. However, that case was brought under the state's consumer protection law and only sought to address problems in Massachusetts. And, it did not seek to address the problem that Wall Street and Morgan Stanley's abusive practices were racially discriminatory, markedly and unjustifiably causing adverse impact on black homeowners.

What remedies are you seeking in this case?

We want to ensure that Morgan Stanley does not pursue these policies in the future and adheres to both the spirit and letter of the Fair Housing Act and Equal Credit Opportunity Act. Our clients will ask the court to order Morgan Stanley to disgorge the profits earned from its discriminatory lending practices. The suit will also seek individual damages for the five named plaintiffs. Our clients will ask the court to find that Morgan Stanley violated these laws when its securitization policies resulted in a disparate impact upon the black community in greater Detroit.