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Local Attorney Ahead Of Banking Suits

By **David Forster**
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DAVID TESELLE was cross-examining a witness from a large investment bank when he had his Perry Mason moment.

He was representing a Connecticut financial services firm that lost millions on an investment. In 2007, the company bought collateralized debt obligations, or CDOs, from a major investment bank. The obligations were rated commercial grade — a safe bet. Two weeks later they were downgraded to junk status.

TeSelle was questioning the person who headed up the CDO department at the investment bank. He asked the witness to explain an email he sent to some people in his department, telling them to mark a day in July 2007 on their calendars.

The answer was a turning point in TeSelle's investigation. He began looking at the agency that had rated the CDOs. And this is how he wound up on the front lines of unraveling the role that ratings agencies played in the massive market collapse that brought the U.S. economy to its knees in 2008.

Last month, attorneys general from several states, including Colorado, announced they were joining the U.S. Justice Department in suing the nation's three major ratings agencies, accusing them of inflating ratings.

TeSelle, an attorney at Denver law firm Burg Simpson Eldredge Hersh & Jardine, filed a similar lawsuit two years ago for the state of Wyoming, which like many states lost a lot of money investing in products that came with gold-plated ratings but turned out to be garbage.

"We were at the forefront," he said. "When you look at the complaint filed by the DOJ it really follows the logic of what we've been filing and pursuing for the past few years."

What the witness from UBS, a major global investment bank, told TeSelle during that cross-examination in Connecticut was

DAVID TESELLE

that in July 2007 Standard & Poor's, one of the big three ratings agencies, was going to announce a major downgrade of investment products.

Other ratings agencies did the same, and almost overnight billions of dollars worth of investments became virtually worthless. The illusory foundation propping up the nation's superheated housing market fell away. The economy went into free-fall, and everyone wondered what the hell happened.

TeSelle was already beginning to piece together the answer to that question. He deposed people from Moody's, which had rated the CDOs bought by his client. Congress, meanwhile, was conducting its own investigation into the market meltdown, as were reporters with major newspapers and magazines.

They all shared what they were learning with each other, and the picture that began to emerge was this: Ratings agencies were slapping inflated ratings on investment products, under pressure from the banks, TeSelle said.

"The three major ratings agencies were fighting tooth and nail over market share and the investment banks were saying if you don't give this false rating I'll go somewhere else," he said.

The ratings agencies and investment banks deny this.

After the meltdown, TeSelle began approaching states to share what he'd learned. Wyoming hired him to sue Standard & Poor's, Moody's and Fitch, the third major ratings agency. TeSelle opted to file in state court. Like most states, Wyoming has a law that prohibits making false or misleading statements in connection with the sale of a security.

Although the allegations implicate federal securities laws, TeSelle didn't want to end up arguing the case in the federal district court in Manhattan, the defendants' home turf. The agencies filed a motion to move the case to federal court, and the judge is expected to announce his decision soon.

Meanwhile, the agencies are mounting a free speech defense, TeSelle said. They argue their ratings are opinions, and the First Amendment protects opinions even if they cause harm. TeSelle said this is the argument Consumer Reports would make if it were sued over a product review.

The difference, he said, is that the consumer magazine doesn't get paid for its reviews, whereas the crux of his case is that the agencies were inflating their ratings to keep the investment banks as clients.

The First Amendment doesn't protect knowingly false statements, especially when they're held out as neutral and independent, and people are counting on this to make major financial decisions, TeSelle said.

"You don't have a First Amendment right to defraud people." •

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