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**UNITED STATES DISTRICT COURT**

**CENTRAL DISTRICT OF CALIFORNIA**

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| SECURITIES AND EXCHANGE COMMISSION,<br><br>Plaintiff,<br><br>vs.<br><br>ANGELO MOZILO, DAVID SAMBOL, AND ERIC SIERACKI,<br><br>Defendants. | Case No.<br><br>**COMPLAINT FOR VIOLATIONS OF THE FEDERAL SECURITIES LAWS**<br><br>**DEMAND FOR JURY TRIAL** |

Plaintiff Securities and Exchange Commission ("Commission") alleges as follows:

## JURISDICTION AND VENUE

1. This Court has jurisdiction over this action pursuant to Sections 20(b), 20(d)(1), 20(e) and 22(a) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. §§ 77t(b), 77t(d)(1), 77t(e), and 77v(a), and Sections 21(d)(1), 21(d)(2), 21(d)(3)(A), 21(e), and 27 of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §§ 78u(d)(1), 78u(d)(2), 78u(d)(3)(A), 78u(e) & 78aa. Defendants have directly or indirectly made use of the means or instrumentalities of interstate commerce, of the mails, or of the facilities of a national securities exchange in connection with the transactions, acts, practices and courses of business alleged in this complaint.

2. Venue is proper in this district pursuant to Section 22(a) of the Securities Act, 15 U.S.C. § 77v(a), and Section 27 of the Exchange Act, 15 U.S.C. § 78aa, because defendants reside and transact business within this district and certain of the transactions, acts, practices and courses of conduct constituting violations of the federal securities laws alleged in this complaint occurred within this district.

## SUMMARY

3. This matter involves a disclosure fraud by the three most senior executives of Countrywide Financial Corporation, a mortgage lender formerly based in Calabasas, California, and insider trading by Countrywide's former chairman of the board and chief executive officer, Angelo Mozilo.

4. From 2005 through 2007, Mozilo, along with David Sambol, chief operating officer and president, and Eric Sieracki, chief financial officer, held Countrywide out as primarily a maker of prime quality mortgage loans, qualitatively different from competitors who engaged primarily in riskier lending. To support this false characterization, Mozilo, Sieracki, and Sambol hid from

investors that Countrywide, in an effort to increase market share, engaged in an unprecedented expansion of its underwriting guidelines from 2005 and into 2007. Specifically, Countrywide developed what was referred to as a "supermarket" strategy, where it attempted to offer any product that was offered by any competitor. By the end of 2006, Countrywide's underwriting guidelines were as wide as they had ever been, and Countrywide was writing riskier and riskier loans. Even these expansive underwriting guidelines were not sufficient to support Countrywide's desired growth, so Countrywide wrote an increasing number of loans as "exceptions" that failed to meet its already wide underwriting guidelines even though exception loans had a higher rate of default.

5. Countrywide was more dependent than many of its competitors on selling loans it originated into the secondary mortgage market, an important fact it disclosed to investors. But Mozilo expected that the deteriorating quality of the loans that Countrywide was writing, and the poor performance over time of those loans, would ultimately curtail the company's ability to sell those loans in the secondary mortgage market. Mozilo and the company's chief risk officer warned Sambol and Sieracki about the increased risk that Countrywide was assuming. Thus, each of the defendants was aware, but failed to disclose, that Countrywide's current business model was unsustainable.

6. Mozilo, Sambol, and Sieracki were responsible for Countrywide's fraudulent disclosures. From 2005 through 2007, these senior executives misled the market by falsely assuring investors that Countrywide was primarily a prime quality mortgage lender which had avoided the excesses of its competitors. Countrywide's Forms 10-K for 2005, 2006, and 2007 falsely represented that Countrywide "manage[d] credit risk through credit policy, underwriting, quality control and surveillance activities," and the 2005 and 2006 Forms 10-K falsely stated that Countrywide ensured its continuing access to the mortgage backed securities market by "consistently producing quality mortgages."

7. In fact, the credit risk that Countrywide was taking was so alarming to Mozilo that he internally issued a series of increasingly dire assessments of various Countrywide loan products and the risks to Countrywide in continuing to offer or hold those loans, while at the same time he, Sambol, and Sieracki continued to make public statements obscuring Countrywide's risk profile and attempting to differentiate it from other lenders. In one internal email, Mozilo referred to a particularly profitable subprime product as "toxic," and in another he stated that the company was "flying blind," and had "no way" to predict the performance of its heralded product, the Pay-Option ARM loan. Mozilo believed that the risk was so high and that the secondary market had so mispriced Pay-Option ARM loans that he repeatedly urged that Countrywide sell its entire portfolio of those loans. Despite their awareness of, and Mozilo's severe concerns about, the increasing risk Countrywide was undertaking, Mozilo, Sambol, and Sieracki hid these risks from the investing public.

8. Defendants misled investors by failing to disclose substantial negative information regarding Countrywide's loan products, including:

- the increasingly lax underwriting guidelines used by the company in originating loans;
- the company's pursuit of a "matching strategy" in which it matched the terms of any loan being offered in the market, even loans offered by primarily subprime originators;
- the high percentage of loans it originated that were outside its own already widened underwriting guidelines due to loans made as exceptions to guidelines;
- Countrywide's definition of "prime" loans included loans made to borrowers with FICO scores well below any industry standard definition of prime credit quality;
- the high percentage of Countrywide's subprime originations that had a loan to value ratio of 100%, for example, 62% in the second quarter of 2006; and

- Countrywide's subprime loans had significant additional risk factors, beyond the subprime credit history of the borrower, associated with increased default rates, including reduced documentation, stated income, piggyback second liens, and LTVs in excess of 95%.

Mozilo, Sambol, and Sieracki knew this negative information from numerous reports they regularly received and from emails and presentations prepared by the company's chief credit risk officer. Defendants nevertheless hid this negative information from investors.

9. During the course of this fraud, Mozilo engaged in insider trading in Countrywide's securities. Mozilo established four sales plans pursuant to Rule 10b5-1 of the Securities Exchange Act in October, November, and December 2006 while in possession of material, non-public information concerning Countrywide's increasing credit risk and the risk that the poor expected performance of Countrywide-originated loans would prevent Countrywide from continuing its business model of selling the majority of the loans it originated into the secondary mortgage market. From November 2006 through August 2007, Mozilo exercised over 5.1 million stock options and sold the underlying shares for total proceeds of over $139 million, pursuant to 10b5-1 plans adopted in late 2006 and amended in early 2007.

## DEFENDANTS

10. **Angelo Mozilo**, age 70, is a resident of Thousand Oaks, California. Mozilo was a founder of Countrywide and was its chairman and chief executive officer ("CEO") from its formation in 1969 until Countrywide was acquired by Bank of America in 2008.

11. **David Sambol**, age 49, is a resident of Hidden Hills, California. He was Countrywide's president and chief operating officer ("COO") from September 2006 until its acquisition by Bank of America in 2008. Sambol was Countrywide's executive managing director, business segment operations from April 2006 until September 2006, and executive managing director and chief of mortgage banking

and capital markets from January 2004 until April 2006. Sambol was a member of the Countrywide board of directors from 2007 until July 2008. Sambol also held executive positions at certain Countrywide subsidiaries, including Countrywide Bank.

12. **Eric Sieracki**, age 52, is a resident of Lake Sherwood, California. Sieracki was Countrywide's chief financial officer ("CFO") from the first quarter of 2005 until its acquisition by Bank of America in 2008.

## RELATED PARTY

13. **Countrywide Financial Corporation**, a Delaware corporation, was a mortgage lender based in Calabasas, California. During all times relevant to this complaint, its stock was registered pursuant to Section 12(b) of the Exchange Act and was listed on the New York Stock Exchange, and, until the demise of the Pacific Stock Exchange, it was listed on that Exchange as well. On July 1, 2008, Countrywide merged with Bank of America and is now a wholly owned subsidiary of Bank of America. Countrywide's remaining operations and employees have been transferred to Bank of America, and Bank of America ceased using the Countrywide name in April 2009. On July 1, 2008, the NYSE filed a Form 25 to deregister and delist Countrywide's common stock, and on July 22, 2008 Countrywide filed a Form 15 deregistering its common stock under Section 12(g) of the Exchange Act.

## FACTS

14. From 2005 through 2007, in Countrywide's periodic filings with the Commission and in other public statements, Mozilo, Sambol, and Sieracki held Countrywide out as primarily a maker of prime quality mortgage loans, qualitatively different from competitors who engaged primarily in riskier lending. To support this false characterization, the proposed defendants hid from investors that Countrywide was engaged in an effort to increase market share and sustain

revenue generation through unprecedented expansions of its underwriting guidelines, taking on ever-increasing credit risk.

### A. Countrywide's Business

15. Countrywide originated, sold, and serviced both prime and subprime (which Countrywide's periodic filings referred to as "nonprime") mortgage loans. By 2005, Countrywide was the largest U.S. mortgage lender in the United States, originating over $490 billion in mortgage loans in 2005, over $450 billion in 2006, and over $408 billion in 2007. Countrywide recognized pre-tax earnings of $2.4 billion and $2 billion in its loan production divisions in 2005 and 2006, respectively, and a pre-tax loss of $1.5 billion in its loan production division in 2007.

16. Countrywide pooled most of the loans it originated and sold them in secondary mortgage market transactions. Countrywide sold the pooled loans either through whole loan sales or securitization. In whole loan sales, Countrywide sold the loans to investors and recorded gains on the sales. In securitizations, Countrywide sold interests in the pooled loans, i.e., mortgage-backed securities. Countrywide's loan sales were run out of its capital markets division. In 2005, Countrywide reported $451.6 million in pre-tax earnings from capital market sales, representing 10.9% of its pre-tax earnings; in 2006, it recognized $553.5 million in pre-tax earnings from that division, representing 12.8% of its pre-tax earnings, and in 2007 it recognized a mere $14.9 million in pre-tax earnings from that division, reporting a pre-tax loss overall.

17. Historically, Countrywide's primary business had been originating prime conforming loans that were saleable to the Government Sponsored Entities ("GSEs"). In the fiscal years 2001, 2002, and 2003, Countrywide's prime conforming originations were 50%, 59.6%, and 54.2% of its total loan originations, respectively. In 2003, United States residential mortgage production reached a record level of $3.8 trillion. Countrywide experienced record earnings in that year,

with net earnings of $2.4 billion, an increase of $1.5 billion, or 182%, over 2002. In 2004, in a market where originations were declining overall, Countrywide maintained net earnings of $2.1 billion, and increased its market share from 11.4% to 12.7%.

18. Countrywide achieved this result in large part by moving away from its historical core business of prime mortgage underwriting to aggressively matching loan programs being offered by other lenders, even monoline subprime lenders. As a result, as reported in Countrywide's periodic filings and reflected in the chart below, in 2004, 2005, and 2006, Countrywide wrote more non-conforming, subprime, and home equity loans than in any prior period:

| | **2001** | **2002** | **2003** | **2004** | **2005** | **2006** |
|---|---|---|---|---|---|---|
| **Prime Conforming** | 50% | 59.6% | 54.2% | 38.2% | 32% | 31.9% |
| **Prime Non-Conforming** | 16.5% | 24.5% | 31.4% | 38.7% | 47.2% | 45.2% |
| **Home Equity** | 6.8% | 4.6% | 4.2% | 8.5% | 9.0% | 10.2% |
| **Nonprime (Subprime)** | 7.8% | 3.7% | 4.6% | 11.0% | 8.9% | 8.7% |
| **FHA/VA** | 18.9% | 7.6% | 5.6% | 3.6% | 2.1% | 2.8% |
| **Commercial** | 0.0% | 0.0% | 0.0% | 0.0% | 0.8% | 1.2% |

19. In 2004, Countrywide's reported production of conventional conforming loans dropped to 38.2%, its production of subprime loans had risen to 11%, its production of home equity loans had risen to 8.5%, and its production of conventional non-conforming loans had risen to 38.7%. By 2006, Countrywide had turned its prior business model on its head: a mere 31.9% of its originations were conforming, 45.2% were non-conforming, 8.7% were subprime, and 10.2% were home equity.

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### B. Countrywide's Deceptive Description of Its Loans

20. Countrywide's Form 10-Ks deceptively described the types of loans upon which the Company's business depended. While Countrywide provided statistics about its originations which reported the percentage of loans in various categories, such as those noted in the table in paragraph 18, the information was misleading because its descriptions of "prime non-conforming" and "nonprime" loans in its periodic filings were insufficient to inform investors what types of loans were included in those categories. "Prime" loans were described in Countrywide's 2005, 2006, and 2007 Forms 10-K as follows:

> Prime Mortgage Loans include conventional mortgage loans, loans insured by the Federal Housing Administration ("FHA") and loans guaranteed by the Veterans Administration ("VA"). A significant portion of the conventional loans we produce qualify for inclusion in guaranteed mortgage securities backed by Fannie Mae or Freddie Mac ("conforming loans"). Some of the conventional loans we produce either have an original loan amount in excess of the Fannie Mae and Freddie Mac loan limit for single-family loans ($417,000 for 2006) or otherwise do not meet Fannie Mae or Freddie Mac guidelines. Loans that do not meet Fannie Mae or Freddie Mac guidelines are referred to as "nonconforming loans."

21. Nothing in that description informed investors that Countrywide's "prime non-conforming" category included loan products with increasing amounts of credit risk. While guidance issued by the banking regulators referenced a credit score ("FICO score") at 660 or below as being an indicator of a subprime loan, some within the banking industry drew the distinction at a score of 620 or below. Countrywide, however, did not consider **any** FICO score to be too low to be categorized within "prime." Nor did Countrywide's definition of "prime" inform

investors that its "prime non-conforming" category included so-called "Alt-A" loan products with increasing amounts of credit risk, such as (1) reduced or no documentation loans; (2) stated income loans; and (3) loans with loan to value or combined loan to value ratios of 95% and higher. Finally, it did not disclose that Pay-Option ARM loans, including reduced documentation Pay-Option ARM loans, were included in the category of prime loans. Moreover, to the extent these extremely risky loans were below the loan limits established by the government sponsored entities that purchased these loans ("GSEs"), they would have been reported by Countrywide as prime conforming loans. In 2005 and 2006, Countrywide's Pay-Option ARMs ranged between 17% and 21% of its total loan originations. It maintained the majority of these loans in the held for investment portfolio at Countrywide Bank.

22. Significantly, the Countrywide periodic filings do not define "nonprime" in any way, and Countrywide's periodic filings failed to disclose that loans in the category of subprime were not merely issued to borrowers with blemished credit, but that this category included loans with significant additional layered risk factors, such as (1) subprime piggyback seconds, also known as 80/20 loans; (2) reduced or no documentation loans; (3) stated income loans; (4) loans with loan to value or combined loan to value ratios of 95% and higher; and (5) loans made to borrowers with recent bankruptcies and late mortgage payments.

23. By increasing its origination of non-conforming and subprime loans between 2003 and 2006, Countrywide was able to originate many more loans in those years and increase its market share, even as the residential real estate market declined in the United States. As of December 31, 2003, based on its own internal estimates, Countrywide had an 11.4% share of the United States mortgage market. By September 30, 2006, it had a 15.7% share of the market. While Countrywide boasted to investors that its market share was increasing, company executives did not disclose that its market share increase came at the expense of prudent

underwriting guidelines. As a result, Countrywide's share price rose from $25.28 on December 31, 2003 to $42.45 on December 29, 2006, the last trading day of that year.

### C. Countrywide's Market Strategy Caused it To Take On Increasing Credit Risk

#### 1. Countrywide's Undisclosed Expansion of Underwriting Guidelines and the Matching Strategy

24. By the end of 2006, Countrywide's underwriting guidelines were wider and more aggressive than they had ever been. The company's aggressive guideline expansion was deliberate, and began as early as 2003. Indeed, from January 2003 until well into 2006, Countrywide's credit risk management department ("Risk Management") spent approximately 90% of its time processing requests for expansions of Countrywide's underwriting guidelines.

25. Countrywide's "matching strategy," also known as the "supermarket strategy," was a key driver of the company's aggressive expansion of underwriting guidelines. The strategy committed the company to offering any product and/or underwriting guideline available from at least one "competitor," which included subprime lenders. Thus, if Countrywide did not offer a product offered by a competitor, Countrywide's production division invoked the matching strategy to add the product to Countrywide's menu. For example, if Countrywide's minimum FICO score for a product was 600, but a competitor's minimum score was 560, the production division invoked the matching strategy to reduce the minimum required FICO score at Countrywide to 560.

26. The impact of the matching strategy was intensified by Countrywide's "no-brokering" policy, which precluded Countrywide's loan officers from referring loan applicants to other brokers and/or institutions. Prior to its implementation, loan officers could engage in a practice known as "brokering," in which the loan officer would refer those borrowers deemed too risky for Countrywide to another

lender, which in turn paid a commission to the Countrywide loan officer. The no-brokering policy increased the incentives for Countrywide's retail sales force to be aggressive in finding ways for Countrywide to underwrite a loan, regardless of whether the loan satisfied the underwriting guidelines Countrywide repeatedly touted to investors.

27. Mozilo, Sambol, and Sieracki knew that the company was taking on increased risk of defaults and delinquencies as a result of its widened underwriting guidelines and matching strategy, yet Countrywide's periodic filings concealed the unprecedented expansion of underwriting guidelines and the attendant increased credit risk.

### 2. <u>Exception Loans Magnified Countrywide's Credit Risk</u>

28. Though Countrywide proclaimed in its Forms 10-K for 2005, 2006, and 2007 that it managed credit risk through its loan underwriting, the company's increasingly wide underwriting guidelines and exceptions process materially increased Countrywide's credit risk during that time. Countrywide used an automated underwriting system known as "CLUES" to actually underwrite loans. The CLUES system applied the principles and variables set forth in the Countrywide underwriting manuals and its loan program guide. CLUES applied a device known as the "underwriting scorecard," which assessed borrower credit quality by analyzing several variables, such as FICO scores, loan to value ratios, documentation type (*e.g.*, full, reduced, stated) and debt-to-income ratios. These variables were weighted differently within the scorecard, depending upon their perceived strength in predicting credit performance. In underwriting a loan, Countrywide loan officers entered an applicant's information into CLUES, which would (1) approve the loan; (2) approve the loan with caveats; or (3) "refer" the loan to a loan officer for further consideration and/or manual underwriting.

29. The CLUES program typically did not "reject" a loan if a requirement of Countrywide's guidelines had not been met or if CLUES calculated that the loan

presented an excessive layering of risk. Instead, CLUES "referred" the loan, indicating that the loan application would have to be reviewed manually prior to approval. In these circumstances, to proceed with the loan, the loan officer would request an "exception" from the guidelines from more senior underwriters at Countrywide's structured lending desk ("SLD"). Countrywide's level of exceptions was higher than that of other mortgage lenders. The elevated number of exceptions resulted largely from Countrywide's use of exceptions as part of its matching strategy to introduce new guidelines and product changes.

30. Further, the actual underwriting of exceptions was severely compromised. According to Countrywide's official underwriting guidelines, exceptions were only proper where "compensating factors" were identified which offset the risks caused by the loan being outside of guidelines. In practice, however, **Countrywide used as "compensating factors" variables such as FICO and loan to value, <u>which had already been assessed by CLUES in issuing a "refer" finding</u>**. Countrywide underwriting manuals were amended to explicitly prohibit this practice in mid-2007, but this serious deficiency was in place from early 2006 through early 2007, when a large volume of obviously deficient exception loans were originated by Countrywide.

## D. <u>Countrywide's Business Model Became Unsustainable</u>

31. As described above, Countrywide depended on its sales of mortgages into the secondary market as an important source of revenue and liquidity. As a result, Countrywide was not only directly exposed to credit risk through the mortgage-related assets on its balance sheet, but also indirectly exposed to the risk that the increasingly poor quality of its loans would prevent their continued profitable sale into the secondary mortgage market and impair Countrywide's liquidity. Rather than disclosing this increasing risk, Mozilo, Sambol, and Sieracki gave false comfort, again touting Countrywide's loan quality. For example, Countrywide stated in its 2005 Form 10-K: "We ensure our ongoing access to the

secondary mortgage market by consistently producing quality mortgages. . . . We make significant investments in personnel and technology to ensure the quality of our mortgage loan production." A virtually identical representation appears in Countrywide's 2006 Form 10-K. Accordingly, Countrywide's failure to disclose its widening underwriting guidelines and the prevalence of exceptions to those guidelines in 2005 and 2006 constituted material omissions from Countrywide's periodic reports.

### E. Mozilo, Sambol, and Sieracki Were Aware of the Increased Credit Risk Created By Expanded Underwriting Guidelines and Exception Loans

32. Countrywide's increasingly wide underwriting guidelines materially increased the company's credit risk from 2004 through 2007, but this increased risk was not disclosed to investors. In 2007, as housing prices declined, Countrywide began to suffer extensive credit problems as the inherent credit risks manifested themselves.

#### 1. The September 2004 Warning

33. The credit losses experienced by Countrywide in 2007 not only were **foreseeable** by the proposed defendants, they were in fact **foreseen** at least as early as September 2004. Risk Management warned Countrywide's senior officers that several aggressive features of Countrywide's guidelines (*e.g.*, high loan to value programs, ARM loans, interest only loans, reduced documentation loans, and loans with layered risk factors) significantly increased Countrywide's credit risk.

34. Countrywide was taking on more risk as a direct result of the lower credit quality of the loans it was originating. Countrywide's strategy of reducing risk through loan sales was being frustrated as the company produced smaller percentages of loans eligible for sale on a nonrecourse basis (e.g., FHA, VA and conforming loans), and larger percentages of loans (e.g., subprime and

nonconforming loans) where it retained credit risk in the form of residual interests. By September 2004, defendants knew the following trends:

- 66% of Countrywide's production was conforming in July 2003, but conforming originations **had fallen** to 35% by July 2004;

- 21% of Countrywide's production was nonconforming in July 2003, but non-conforming originations **had risen** to 40% by July 2004; and

- 2% of Countrywide's July 2003 production was subprime, but subprime originations **had risen** to 10% by July 2004.

35. The credit risk described in the September 2004 warning **worsened** from September 2004 to August 2007. Risk Management continuously had discussions with Countrywide's loan production division, which reported to Sambol, about the credit concerns identified in the September 2004 warning. In fact, Risk Management conducted studies to identify relationships among certain credit variables and their effect upon the probability that a loan would go into serious delinquency or default. One finding of these studies, the results of which were shared with Sambol and Sieracki, was that the less documentation associated with a loan, the higher the probability of default. Nevertheless, Countrywide continued to expand its underwriting guidelines, and to liberally make exceptions to those guidelines, through the end of 2006. These facts were never disclosed to investors.

### 2. Credit Risk Management Repeatedly Alerted the Defendants to Increases in Credit Risk

36. Both Sambol and Sieracki were members of the Countrywide credit risk committee. The credit risk committee had quarterly meetings. At these meetings, the members were provided with detailed presentations highlighting Countrywide's increased credit risk. For example, at an April 6, 2005 meeting of the credit risk committee attended by Sambol, McMurray reported that (1)

Countrywide non-conforming loans originated in May 2002 were twice as likely to default as loans originated in January 2000; (2) the risk of home equity lines of credit defaulting had doubled over the past year, mainly due to the prevalence of reduced documentation in those loans; and (3) Countrywide was now a leader in the subprime market in four of six categories, whereas in December 2004 Countrywide had only been a leader in two of six categories.

37. Similarly, Sieracki attended a June 28, 2005 meeting at which the chief operating officer noted that Countrywide was taking on "too much" balance sheet risk in home equity lines of credit ("HELOCs") and subprime loans, and had taken on "unacceptable risk" from non-owner occupied loans made at 95% combined loan to value ratios, which were an exception to Countrywide's then-existing underwriting guidelines. Risk Management also reported at that meeting that non-conforming loan programs accounted for 40% of Countrywide's loan originations and that subprime production had tripled, rising from 4% to 14% of total production. Finally, at that same meeting, Risk Management reported to the committee on evidence of borrowers misrepresenting their income and occupation on reduced documentation loan applications, and the increasing credit risks associated with Pay-Option ARM loans, for example, negative amortization, payment shock, and the necessity of raising the initial interest rate to reduce the speed of negative amortization on the loans.

38. Sambol and Sieracki also learned of the risks associated with the company's aggressive guideline expansion in meetings of other company committees. For example, Sieracki was a member of the asset and liability committee, and Sambol attended certain of its meetings. If a proposed guideline expansion had a modeled expected default rate in excess of 8%, the proposal had to be submitted to this committee for approval. All proposed expansions to Countrywide's subprime menu from late 2005 through 2006 presented an expected default rate in excess of 8% and required approval of that committee. In June

2005, Sambol and McMurray engaged in a lengthy email exchange regarding the impact of Countrywide's underwriting guideline expansion related to requests for subprime product expansions that had been taken up by the asset and liability committee in the first and second quarters of 2005. In that exchange, McMurray warned Sambol that "as a consequence of [Countrywide's] strategy to have the widest product line in the industry, we are clearly out on the 'frontier' in many areas." McMurray went on to note that the frontier had "high expected default rates and losses."

39. Additionally, proposals with high expected defaults or that were otherwise controversial were referred to the Countrywide responsible conduct committee for approval. Sambol was a member of this committee, which had repeatedly approved guideline expansions. For instance, in late 2006 Countrywide's production divisions proposed expanding Countrywide's guidelines to match certain guidelines offered by Bear Stearns and Lehman Brothers, programs that were known within Countrywide as "Extreme Alt-A." Risk Management was concerned about the risks associated with these guidelines, and referred the request to the responsible conduct committee. Sambol, in his capacity as a member of that committee, approved the expansion.

40. Finally, both Mozilo and Sambol were aware as early as June 2006 that a significant percentage of borrowers who were taking out stated income loans were engaged in mortgage fraud. On June 1, 2006, Mozilo advised Sambol in an email that he had become aware that the Pay-Option ARM portfolio was largely underwritten on a reduced documentation basis and that there was evidence that borrowers were lying about their income in the application process. On June 2, 2006, Sambol received an email reporting on the results of a quality control audit at Countrywide Bank that showed that **50%** of the stated income loans audited by the bank showed a variance in income from the borrowers' IRS filings of greater