David Einhorn & Dan Loeb:. New Century Financial

With no further ado, a contribution from DEEP CAPTURE on Dan Loeb & David Einhorn....

I guess that listening to the ill-advice of useless attorneys who advised Dan to sign degradation contracts with Prem Watsa OR to respect his faux friendship with Dave Einhorn was just more important than a shot at Prudential fraud findings..
AGAIN, see Leon Black's Top 45 US insurer MODCO list! At least I know that Dan Loeb is capable of an honest campaign, whereas David prefers only dishonest ones. Dave's door swings only one way!

How "Activist Investors" David Einhorn and Dan Loeb Brought Their Special Talents to Bear On New Century Financial

ou don't hear much about it, but the March 2007 bankruptcy of a company called New Century Financial was arguably one of the most important events leading up to the financial crisis that nearly caused a second Great Depression.

It was the demise of New Century, then the nation's second largest mortgage lender, that triggered the collapse of the market for collateralized debt obligations. And it was the collapse in the value of collateralized debt obligations (a majority of which contained New Century mortgages) that hobbled a number of big financial firms. Once hobbled, the likes of Bear Stearns and Lehman Brothers were ripe targets for unscrupulous hedge fund managers who amplified their problems by spreading exaggerated rumors while bombarding them with illegal naked short selling.

So we must ask: Why did New Century Financial go bankrupt? Did the company die of natural causes, or did miscreants orchestrate its destruction? And if miscreants destroyed New Century, did they do so planning to profit from the broader economic calamities that were certain to result from its collapse?

I do not yet have definitive answers to these questions. But interviews with sources close to New Century and a review of documents, including the oddly biased 500-page New Century bankruptcy report, make it clear that at least two hedge fund managers — David Einhorn of Greenlight Capital and Dan Loeb of Third Point Capital — played a significant role in creating the conditions that made New Century vulnerable to catastrophe. And they did so while building massive short positions in Bear Stearns, Lehman Brothers, MBIA and other companies that were likely to be seriously damaged if New Century were to go bankrupt.

Einhorn was a major *investor* in New Century and took a seat on the company's board in early 2006. He has gone to lengths to suggest that he lost a lot of money from his investment. But given that his activities on the board were so contrary to New Century's best interests, and given that he was otherwise so heavily invested in the collapse of the mortgage markets, it is reasonable to ask if he was in fact short selling New Century's stock, or buying credit default swaps that would pay out in the event of the company's bankruptcy.

Moreover, some banks, most notably Goldman Sachs, created and sold collateralized debt obligations containing New Century mortgages while simultaneously betting that the CDOs would plummet in value. Multiple media stories (such as this one in "Investment News") have speculated that Goldman Sachs actually designed these CDOs in such a way that they would be certain to implode, delivering large profits to Goldman and preferred hedge fund clients. Those CDO could not have been created without Einhorn and his allies inside New Century delivering the mortgages that went into them. And there is no doubt that Goldman Sachs delivered the knock-out punch that put New Century out of business, ensuring that the CDOs would, in fact, implode. This constellation of facts may be coincidental, of course. Or not. This essay lays them out, and leaves it to the reader to decide.

New Century's problems began in December 2005, when board member Richard Zona drafted a letter in which he threatened to resign if senior executives did not agree to sell a greater percentage of the mortgage loans on its books to various banks, such as Goldman Sachs. In his letter, Zona explicitly stated that he was making this demand in league with David Einhorn and Dan Loeb.

Unfortunately, according to the bankruptcy report, New Century's executives never saw that letter. Zona stashed the draft letter on his computer and instead submitted a letter making a similar demand, but omitting all mention of Einhorn and Loeb. In all likelihood, Zona changed his letter because he knew that New Century's executives had good reason to doubt whether Einhorn and Loeb, who had recently reported large shareholdings in New Century, were acting in the company's best interests.

As *Deep Capture* has thoroughly documented, Einhorn and Loeb are part of a network of hedge fund managers and criminals who use a variety of dubious tactics to destroy, seize, and/or loot public companies for profit. It is not unusual for money managers in this network to appear as long investors in the companies they are attacking, and sometimes they seek to obtain a seat on a target company's board in order to be better placed to run the company into the ground for their own private profit.

Essentially everyone in this network – including Einhorn and Loeb — are connected in important ways to Michael Milken, the infamous criminal who specialized in loading companies with debt, looting them, and then profiting still more from their inevitable bankruptcies.

Einhorn spent his early career working for Gary Siegler, who was formerly the top partner in the investment firm run by Carl Icahn, a corporate raider and ne'er-do-well who owes his fortune to the junk bond finance that he received from Michael Milken in the 1980s. Icahn has various other seamy connections, and has employed people with ties to the Mafia (see "The Story of Dendreon" for details) employed people with ties to the Mafia (see "The Story of Dendreon" for details).

Prior to his attacks on Lehman Brothers and Bear Stearns, Einhorn was best known for his eminently dishonest attempt to demolish a financial company called Allied Capital. The attack on Allied began in 2002 at a hedge fund luncheon. Halfway through that luncheon, Einhorn stood up and declared that "Allied Capital is going to zero!" Sitting next to Einhorn at that luncheon was Carl Icahn.

Some weeks before the luncheon, Michael Milken had appeared in the offices of a top Allied Capital executive. "You know," Milken told the executive, "I already am quite a large shareholder of your stock – but my name will never show up on any list *you'll* see." This may have been a reference to a practice called "parking stock" (owning stock but "parking" it in the accounts of friends with whom one has made under-the-table arrangements), a practice that figured in the high-count indictment that sent Milken to prison in the 1980s. Milken appeared to the Allied executives to be threatening Allied and fishing for information, paving the way for Einhorn's more public vitriol.

The Allied story is outside the remit of this article, but it is enough to know that Einhorn proceeded to accuse the company of massive fraud and of failing to account for its loans at "fair value". With some minor exceptions, none of Einhorn's allegations of fraud were ever proven to have merit. And it was clear from the get-go that Einhorn's notion of "fair value" had nothing to do with "fair" (as in "what the market was paying"). Rather, "fair value" was an arbitrary metric that could be taken to mean whatever Einhorn said the value of the loans should be. This is important because Einhorn's outlandish "fair value" calculations featured prominently in his attacks on Lehman Brothers and Bear Stearns. In addition, as we will see, arbitrary and over-the-top "fair value" assumptions about mortgage loans featured in the bankruptcy of New Century.

As for Loeb, he is a long-time Einhorn accomplice who worked side-by-side with many of Milken's former traders at Jeffries & Co. He got his first big break by obtaining preferential access to certificates of beneficiary interest that had been issued by Milken's bankrupt operation at Drexel, Burnham, Lambert. Loeb seems to take a certain pride in his bad boy image, and has distinguished himself in all manner of chicanery, such as hiring a cast of convicted criminals and scofflaws to spread false information about public companies on the Internet. (Please search *Deep Capture*'s archives; we have compiled substantial evidence implicating Loeb in various misdeeds).

Given their backgrounds, there was every reason to doubt the merits of the demand that Einhorn and Loeb had articulated through New Century board member Richard Zona. Indeed, the majority of New Century's top managers (the company had three CEOs at the time) were opposed to the Einhorn-Loeb demand to sell off all of New Century's mortgage loans, and for good reason. Selling off all the loans would make the company entirely dependent on the banks, such as Goldman Sachs, that bought the loans. If, for some reason, the banks were to demand that New Century buy back its loans, the company would go bankrupt.

Shortly before Zona submitted his letter demanding that New Century sell off its loans, one of the company's co-founders, Patrick Flanagan, said by sources to be an ally of Einhorn and Loeb, left the company. After a brief time, Flanagan went to work for hedge fund Cerberus Capital. Cerberus Capital was run by Ezra Merkin, famous for being one of the biggest feeders to the Bernard Madoff fraud, and Stephen Feinberg, who was formerly a top employee of Michael Milken. Cerberus is also the proud owner of an Austrian bank called Bawag, which was at the center of a scandal that wiped out Refco, once one of the most abusive naked short selling outfits on Wall Street. (Refco's former CEO, Phillip Bennett, and executive Santo Maggio have been convicted and are serving prison sentences, while one of its naked short selling clients, Thomas Badian, is still living in Austria as a fugitive from US law)..

Sources tell *Deep Capture* that Cerberus made massive profits from the demise of New Century, and if so, it is likely that Flanagan had a hand in this. It is perhaps also no coincidence that Cerberus now also employs Thomas Marano, the former head of mortgage trading at Bear Stearns, and Brendan Garvey, the former head of mortgage trading at Lehman Brothers. Marano and Garvey helped sink their companies by buying New Century's repackaged loans from Goldman Sachs and a few other banks.

While still at Bear Stearns, Marano seemed almost eager to see the bank collapse. At one point he called Roddy Boyd, a reporter with close connections to the Einhorn-Milken nexus of hedge funds, to leak an account of Bear Stearns' problems, though as we have documented, that leak seems to have been exagerrated when Marano made it. One has to wonder why he was leaking about his employer, and also wonder at the coincidence of the fact that he was doing this while preparing to go to work for a large hedge fund that was betting *against* that employer.

After Flanagan left New Century, Zona organized a highly unusual "off site" board meeting. The directors at this meeting (which excluded all opposing viewpoints) decided to implement a radical change to New Century's management structure. Among other changes, CEOs Ed Gotchall and Bob Cole were removed from their posts, and the company was put under the sole leadership of the third CEO, Brad Morrice.

Einhorn and Loeb orchestrated this change. Sources say the two hedge fund managers had considerable input at the "off site" board meeting even though Einhorn was not yet a director. And Zona stated in the initial draft of his letter (the one that stated that he was making his demands in alliance with Einhorn and Loeb) that Gotschall was "immature and disruptive," while Cole was "not fully engaged" – because they opposed the demand to sell off the loans.

In Morrice, Einhorn and Loeb had a CEO whom they could work with. Prior to entering the mortgage business, Morrice had been the founding partner, along with Richard Purtrich, of law firm King, Purtrich & Morrice. In 2008, Purtrich was sentenced to prison for funneling illegal kickback payments from a crooked law firm called Milberg Weiss. Milberg's top partners, Bill Lerach and Melvyn Weiss, were also indicted in the scheme.

According to the DOJ, the kickbacks were paid to plaintiffs who filed bogus class action lawsuits against public companies "anticipating that their stock prices would decline." *Deep Capture* has published extensive evidence showing that Milberg prepared those bogus lawsuits in cahoots with hedge funds in David Einhorn's network. The hedge funds, of course, profited from short selling the targeted companies, and it is indeed likely that the bribed plaintiffs were "anticipating that the stock prices would decline" because they *knew* that the hedge funds were going to attack the companies via illegal naked short selling and other tactics.

So it is fair to say that Morrice (whose former partner was funneling kickbacks to plaintiffs who were conspiring with Einhorn's hedge fund network to attack public companies) was intimately familiar with the tactics of Einhorn's hedge fund network.

In any case, soon after Morrice took the helm at New Century, he quickly set about meeting Einhorn's demand to sell off New Century's mortgage loans. Whole loan sales comprised less than 70% of New Century's secondary market transactions in 2005. By September of 2006, whole loan sales comprised a full 95% of New Century's mortgage lending. As a result, whereas in all of 2005, New Century had sold a mere $256 million worth of loans at a discount, during the first nine months of 2006, New Century sold $916 million worth of loans at a discount.

Much of the income from those loan sales was not used to build New Century's liquidity. Rather, at Einhorn's suggestion, it was used to buy back stock and pay out massive dividends to shareholders like Einhorn. At the end of 2005, New Century was paying $1.65 a share in dividends. In January 2007, two months before New Century's bankruptcy, the company was paying dividends of $1.90 a share. If we accept the proposition that Einhorn might have profited from New Century's collapse, it is clear that he planned first to profit from his long position. This is similar to a classic "pump and dump" scam, except that the strategy is to pump and *destroy*.

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In March 2006, with the support of Morrice and Zona, Einhorn obtained a seat on New Century's board of directors. At this point, according to one member of senior management, the "activist investors" on the board did become extremely "active," agitating for more loan sales while pushing for changes in New Century's accounting. Many of these changes were based on the premise that New Century was not accurately recording the "fair value" of loans that it had to repurchase from Goldman Sachs and other buyers.

Meanwhile, Einhorn convinced the board to create a finance committee and presented himself as the man to run it. According to the bankruptcy report, this committee met "unusually often," and according to sources, its principal activity was to handle New Century's relationships with Goldman Sachs and the 13 other banks that were buying New Century's mortgage loans. In June 2006, at Einhorn's behest, New Century hired a woman named Lenice Johnson to serve as chief credit officer, responsible for managing those same relationships.

As we shall see, two of those relationships – especially the one with Goldman Sachs – would later mysteriously deteriorate, leading to New Century's demise. And soon after New Century went bankrupt, Johnson went to work at the above-mentioned Cerberus Capital (the Milken-crony hedge fund). You may remember that Cerberus Capital was mentioned above because Thomas Marano the head of Bear Stearns' mortgage trading desk, sunk Bear Stearns by buying Goldman-packaged new Century debt, then leaked information about Bear Stearns' financial condition to New York Post reporter Roddy Boyd (Boyd is *Deep Capture* All Star; his dishonesty has been fodder for many of our stories), a few weeks before joining the hedge fund – Cerberus Capital — that was betting against Bear Stearns. In sum, then: Cerberus Capital bet that New Century would face a credit crunch and bet against Bear Stearns for buying New Century's debt, then hired the New Century chief credit officer and the head of the Bear Sterns desk that was making the bad bets.

As Einhorn and Morrice eagerly sold off all of New Century's loans, other board members became alarmed. In August 2006, board member Fred Forster wrote a letter to Einhorn stating: "Whatever we do, we need to be very comfortable that less capital/liquidity does not in any material way threaten the very existence or viability of New Century."

It needs to be stressed that at this point New Century was seemingly in good health. Defaults on its mortgages had increased only slightly, and in the third quarter of 2006, the company recorded a profit of more than $200 million. The problem was that nearly 100 percent of the mortgages it wrote were now being sold to Goldman Sachs and 13 other banks. With no mortgages on its books, the company depended entirely on the banks for income. If just one of those banks were to pull the plug, the company would go bankrupt. And as we know, one of those banks, Goldman Sachs, was placing large short bets on CDO's containing New Century mortgages, meaning that Goldman had a motivation to see New Century fail. In other words, New Century climbed into Goldman's life support chamber while Goldman kept its hand on the plug and bought insurance that would pay out in the event of New Century's death.

Of course, as we know, Goldman was also selling CDOs that had been stuffed with New Century's subprime mortgages. No doubt, Einhorn and his allies at New Century aided the proliferation of these CDOs by selling Goldman ever-larger numbers of subprime mortgages. Again, the problem was not that the subprime mortgages had high default rates. The mortgages were always expected to have high default rates. That's why they were called "subprime." The problem was that Goldman (perhaps with encouragement from their key client Einhorn) was selling the subprime mortgages in essentially fraudulent CDOs that disguised the subprime mortgages as AAA rated debt.

It was just a matter of time before the markets would discover the true nature of these CDOs. That, no doubt, is one reason why Goldman was simultaneously shorting them. All the better for Goldman if New Century were to collapse before the CDO scam was discovered. According to a McClatchy news report, when New Century did collapse, Goldman was prepared with shell companies in the Cayman Islands through which it could offload the last of its New Century debt to unwitting foreign investors.

Supposing that miscreants did want New Century to go bankrupt, all that was required was some precipitating event – an event that would allow one of the 14 banks (say, Goldman Sachs) to force New Century to repurchase its mortgage loans under the terms of its contractual repurchase agreement.

As it happened, the foundations for that precipitating event were laid in November 2006, when New Century demoted its chief financial officer, Patti Dodge, and hired a man named Taj Bindra to take her place. As Morrice, the New Century CEO, told the bankruptcy examiner, Zona and Einhorn "had expressed doubts about Dodge's capabilities and competence to be the company's CFO," and sources tell *Deep Capture* that Bindra was hired at Einhorn's behest.

Prior to joining New Century, Bindra had been the vice president of mortgage banking at Washington Mutual. A lawsuit filed by a consortium of respected insurance companies that were investors in Washington Mutual alleges that JP Morgan conspired with "investors" (read: "short sellers") to drive down Washington Mutual's share price and manufacture falsehoods about its financial health so that JP Morgan could take the company over at a substantial discount. As part of this scheme, the lawsuit alleges, JP Morgan "deceptively gained access to Washington Mutual's confidential financial records through the use of 'plants' and 'moles' engaged in corporate espionage." The lawsuit alleges that one of the "moles" was … Taj Bindra. It is this same Taj Bindra who then went on to bigger things as CFO of New Century Financial.

Whether or not you believe that Bindra was part of a conspiracy to take down Washington Mutual, it is clear that his actions as CFO of New Century Financial were strange. Understanding why, however, requires delving into a bit of accounting arcara.

According to one source, Bindra had been CFO for "no more than two days" before he began asking questions about New Century's accounting for mortgage loans that the company had so far repurchased from Goldman Sachs and the 13 other buyers. Specifically, Bindra asked why New Century did not include so-called "income severity" (i.e. a mark down of the value of repurchased loans to reflect their actual resale value) in its reserve calculation.

Normally, one wants reserves in any financial company to properly estimate the risks of certain events, and their potential costs. However, Bindra's question was somewhat esoteric (especially for a CFO who had only been at New Century for two days) because it referred specifically to an obscure change in New Century's accounting that had been made in the second quarter of 2006. That change was as follows: instead of recording the mark-down in its reserves, it recorded it in "loans held for sale." This does *not* mean that New Century had stopped including income severity in its calculations, but rather, had moved it to another (and equally or more visible) part of its balance sheet. The books continued to balance (that's why they call it a "balance sheet") and, accounting experts tell *Deep Capture,* the change had absolutely no effect on New Century's bottom line, nor was it any less transparent. Multiple New Century executives explained this to Bindra. In addition, KPMG, New Century's accountants, confirmed to Bindra that the change did not affect earnings.

But Bindra persisted. And, according to the bankruptcy report, "such inquiries by Bindra led in relatively short order to the discovery of material accounting errors." Those "material accounting errors" were none other than the obscure change in accounting for income severity – i.e. the change that had no effect on New Century's earnings. By remarkable coincidence, just as Bindra discovered this supposed "error" in December 2006 (which was long before the "error" was mentioned in any other public forum), the Center for Financial Research and Analysis, an outfit known to cater to short sellers, published a report that alluded to this very same "error."

When Bindra took this supposed "error" to the board, there was much confusion among most of the directors. But Einhorn and Zona insisted adamantly that New Century would have to restate its earnings. This was strange not only because the change in how the company recorded income severity had no material effect on earnings, but also because Einhorn had eagerly signed off on the change in the first place. In fact, the change had been one of the board's first initiatives after Einhorn took over the finance committee. Given this, it certainly appears possible that Einhorn initiated the accounting change so that his hand-picked CFO would have some "irregularity" to point to a few months later.

In any case, on February 7, 2007, New Century announced that it had violated accounting rules and would have to restate earnings for the previous year. Oddly, New Century never indicated by how much it would have to restate earnings. It simply said that it would restate. Given that the "violation" discovered by Bindra had no effect on earnings, it makes sense that the company would not provide a figure. That is to say, the figure could not be provided because, as far as anyone at New Century knew at the time, the figure was zero. But this "restatement" announcement was nonetheless catastrophic for New Century, and the beginning of the end for the stability of the American financial system.

It was catastrophic because Goldman Sachs and the 13 other banks that were buying New Century's mortgage loans had small print in their contracts that allowed them to cut off finance and force New Century to buy back its loans if New Century were to restate earnings. Indeed, a restatement was one of the only events that would allow the banks to force New Century to repurchase all of its loans.

Still, nobody actually expected any bank to act on this small print. Presumably it would be mutually assured destruction, with New Century going bankrupt and the banks losing a fortune in the market for CDOs. Several weeks after the earnings restatement, Citigroup made a large investment in New Century, obviously reckoning that the fundamentals of the company were just fine.

But as we know, Goldman Sachs was impervious to mutually assured destruction because it had been short selling the CDOs all along. And sure enough, on March 7, 2007, Goldman, acting on that small print in its contract, sent a non-public letter demanding that New Century repurchase every single one of its Goldman-financed loans. The next day, IXIS Real Estate Capital, then a subsidiary of the French bank Natixis, sent New Century a similar letter. David Einhorn had recently become a major investor in Natixis and had been threatening to topple its management, but that is no doubt another coincidence.

Certainly not a coincidence is the fact that a massive illegal naked short selling attack on New Century began just before Goldman Sachs sent its letter. SEC data shows that there were "failures to deliver" of more than 4 million New Century shares on March 8, 2007. Since failures to deliver occur three days after the selling date, those 4 million phantom shares must have been sold by March 6, one day before Goldman sent the letter. It appears that somebody knew what Goldman had in store for New Century.

An independent company that tracks the trading of hedge funds reports that the biggest traders in New Century stock at this time were SAC Capital, run by Steve Cohen, who was once investigated for trading on inside information provided by Michael Milken's shop at Drexel Burnham, and none other than Dan Loeb, who was Einhorn's early ally in the ultimately successful effort to force New Century to sell off all its loans. We do not know for certain that those trades were short sales because the SEC does not require hedge funds to report their short positions (on the grounds that it might reveal their "proprietary trading strategies" which are, in some cases, flagrantly illegal), but it would be unlike Cohen and Loeb to invest in a company that was about to be wrecked by Goldman Sachs.

In the days after Goldman and IXIS cut off credit, New Century's remaining bankers panicked. With Goldman pulling out and naked short sellers on the rampage, it was clear that New Century's days were numbered. The other bankers pulled the plug and within a matter of weeks, New Century, a company that had reported a strong profit a few months before, declared bankruptcy. The news of the bankruptcy immediately crashed the CDO market (the market actually began to sink around the time Goldman sent New Century its letter, but it went completely under on the news of the bankruptcy). This set off shockwaves that ultimately collapsed the American economy. Meanwhile, of course, Goldman made a handsome profit, having bet that all this was going to happen – that is, it bet that the instruments with which it was flooding the US financfial system would turn toxic.

As we also know, Einhorn also earned a tidy sum — from his short sales of MBIA, which insured the CDOs, and later from his short selling of Bear Stearns and Lehman Brothers, which had bought the CDOs. Did Einhorn or others in his network profit more directly from the collapse and naked short selling of New Century? That is for the SEC to decide.

But, of course, the SEC is unlikely to look into this. Instead, it has charged New Century's former CFO, Patti Dodge, and two other New Century executives for violating accounting rules.

Yet to this date, no reputable independent body has provided evidence that the change in accounting that Bindra "discovered" in December 2006 actually affected earnings. And it is that change that prompted the disastrous announcement two months later that New Century was going to restate. KPMG, New Century's accounting firm, was never consulted about the "restatement" and was fired before it had a chance to object. The decision to announce this restatement (and to not specify by how much the restatement would affect earnings) seems to have been made entirely by Bindra, the CFO, and one of Bindra's minions, with the encouragement of David Einhorn and his ally Richard Zona.

In prosecuting Dodge and her colleagues for accounting violations, the SEC seems to have taken its cues from the bankruptcy examiners' report, which goes to lengths to paint Dodge and other New Century executives (namely, those who were not allied with David Einhorn) as criminals. But strangely, while the bankruptcy examiner insists that there were all manner of misdeeds, it nonetheless admits that it is possible that no actual accounting rules were violated.

Indeed, the bankruptcy report is convoluted beyond belief, and to this eye, biased beyond explanation. The examiner who authored this report stated that he "found no persuasive evidence" that New Century had deliberately inflated its repurchase reserve calculation. He notes that the all-important income severity component was indeed recorded in "loans held for sale" (and therefore had no effect on earnings). But he nonetheless suggests that earnings were inflated, noting that the "elimination of Inventory Severity in the LOCOM valuation account increased earnings by approximately 23.4 million" in the second quarter.

This is a actually a neat trick. The examiner is not stating here that income severity wasn't recorded accurately. He is saying that it wasn't recorded in the "LOCOM valuation" – i.e. at "fair value." As I have mentioned, notions of "fair value" are often arbitrary. Indeed, from the report itself, it would appear that the examiner pulled that $23.4 million figure out of thin air. The tactic seems to be to point to a change in accounting (one that had no effect on earnings) and suggest that this change did inflate earnings by alluding to something altogether unrelated – i.e. random assumptions about fair value.

That is, the argument (which, incidentally, is the same argument that was heard from Einhorn at New Century board meetings) seems to go like this:

Einhorn/bankruptcy examiner: "New Century changed its accounting. It didn't book income severity in repurchase reserves. Therefore, New Century inflated earnings."

Innocent executive: "But we did record income severity, in 'loans held for sale.' Earnings aren't affected by the change."

Einhorn/bankruptcy examiner: "New Century changed its accounting. Therefore, New Century must have inflated earnings."

Innocent executive: "But Einhorn signed off on the change. In fact, it was his idea. And, again, it had no effect on earnings."

Einhorn/bankruptcy examiner: "Well, there was a change. That must mean something is wrong."

Innocent executive: "No"

Einhorn/bankruptcy examiner: "Look, the problem is that income severity wasn't recorded at 'fair value.'"

Innocent executive: "What is 'fair value'?"

Einhorn/bankruptcy examiner: "Here's a number. I found it in my underpants."

Innocent executive: "That's completely arbitrary. We have a formula for marking to market that has served us for years."

Einhorn/bankruptcy examiner: "No, we should use the number from my underpants. To prove my point, I will note that New Century changed its accounting.

Innocent executive: "Changing the accounting had no effect on the calculation of the expense!"

Einhorn/bankruptcy examiner: "Right, but you changed the accounting."

Innocent executive: "I give up. This may wreck the American economy, but I give up."

Aside from the income severity issue, the bankruptcy examiner provides a litany of other accounting violations that might have been committed by New Century even though the examiner says it found no evidence that any *were* broken. None of these supposed misdeeds had anything to do with the restatement announcement that enabled Goldman to torpedo New Century, and most of the alleged violations concern supposed miscalculations of "fair value." Time after time, the examiner opines as to what the fair value of various loans should be, but not once does he explain where in the world he is getting his numbers. If anyone were to ask where he got his numbers, his answer would no doubt be: "They changed the accounting."

This sort of shifty eyed, misdirecting gobbledygook defines David Einhorn's style, so it is perhaps no surprise that the bankruptcy examiner seems to think that Einhorn is the one New Century insider who is actually a terrific fellow (though he is the one who instigated the accounting change that the bankrupcy examiner thinks is so evil).

The examiner, by the way, is named Michael Missal. Prior to becoming a bankruptcy examiner, Michael Missel was a defense lawyer for the above-mentioned, infamous Michael Milken. But that is probably another coincidence.

CONTACTING TRIXIE

E-MAIL: saynototom@outlook.com

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Please contact me with any professional questions or concerns regarding David or Tom to the email address listed

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