

The Australian

Basis on the trail of Timberwolf

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Eric Lewis is in Australia to prepare Basis Capital's \$1 billion court action against Goldman Sachs. Picture: Nikki Short

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WASHINGTON lawyer Eric Lewis, who is acting for hedge fund Basis Capital in its \$1 billion court action against Goldman Sachs over collateralised debt obligation deals in 2007, is used to playing a long game.

He has been in Australia preparing the case, which he had moved to the New York State Supreme Court last year after the US District Court in Manhattan declined to hear it because the deals did not take place in the US.

He admits the case probably won't go before a jury until next year, with a motion to dismiss filed by Goldman and the whole discovery process likely to take most of this year.

Basis Capital of Sydney had put its Basis Yield Alpha Fund into provisional liquidation in August 2007 after losing about \$US56 million in less than six weeks on a Goldman CDO called Timberwolf, which according to Mr Lewis's statement of claim involved Goldman "knowingly making misleading statements and omissions" about the valuation and potential of what he called an "invented product".

And he's not giving up.

"Goldman Sachs issued \$US1bn worth of Timberwolf. What Goldman Sachs knew, and Basis Capital didn't, was that Bear Stearns was about to go belly-up and Goldman had already bought back \$US300m worth and is still holding \$US400m. On June 12 or 13, 2007, Goldman sold Basis Capital two \$US50m lots of Timberwolf, at 78 per cent and 82 per cent of face value, even though in May 2007 Goldman had conducted an internal pricing exercise that priced Timberwolf, depending on metrics, at 24-64 per cent.

"So even on a best-case scenario, Basis was in the hole for \$US15m on day one or, worst case, \$US54m," he said yesterday.

If it was not sold, Timberwolf "was going to sit there like an albatross", Mr Lewis said.

Bear Stearns first hit trouble in August 2007 when two of its funds went bankrupt and had to be rescued in March 2008 by the US government merging it with JPMorgan.

Mr Lewis said yesterday the issue of the origins of the subprime meltdown in mid-2007 was becoming more, rather than less, public as the US economy began to recover.

President Barack Obama's State of the Union address had announced a special joint state-federal committee headed by the Federal Criminal Justice Department and New York Attorney-General Eric Schneiderman to coordinate investigations of the causes of the 2007 subprime mortgage crises.

"There's a strong government regulatory wind blowing into the investigation of these investments," said Mr Lewis, whose wife is the sister of Eliot Spitzer, a predecessor of Mr Schneiderman.

The US Senate's Levin inquiry, which had access to internal Goldman Sachs emails, handed down a 640-page report in April that noted: "Despite doubts about its performance and asset quality, Goldman engaged in an aggressive campaign to sell the Timberwolf securities."

It also quoted the comment by then Goldman executive Tom Montag by internal email that Timberwolf was "one shitty deal".

A Goldman Sachs Australia spokesman said last night: "We believe that we acted appropriately and refute in the strongest possible terms any suggestion that Basis Capital was misled in any way. Basis Capital advertised itself as one of the world's most experienced hedge funds and CDO investors."
