ANNEX 1[1]

Between February 2006 and August 2007 (the "Relevant Period"), Nomura securitized over $13 billion worth of mortgage loans in 18 residential mortgage-backed securities (RMBS) (collectively, the "Subject Deals") in which Nomura made repeated misrepresentations and omissions in publicly filed offering documents and other marketing materials provided to investors. A list of the Subject Deals is provided below.

As detailed below, Nomura knew, based on its own loan-level due diligence and its continued dealings with shoddy mortgage loan originators, that thousands of loans securitized in the Subject Deals: (1) did not comply with applicable loan underwriting guidelines; (2) were not originated in compliance with applicable laws and regulations; or (3) were supported by fraudulent or inflated appraisals. Despite this knowledge, Nomura securitized these high-risk loans in the Subject Deals, while concealing these deficiencies from investors.

Nomura's securitization of defective loans in the Subject Deals—in spite of numerous red flags—reflected a conscious decision by senior Nomura personnel to compete for market share in a highly competitive RMBS market. As one member of Nomura's RMBS team wrote, Nomura could not just "buck the entire marketplace when [it was] hammered to grow." And, as stated by Nomura's head of RMBS due diligence (in the context of proposed changes to one of Nomura's loan supply channels), Nomura was "turning into the lemming of the mortgage business," "following the herd," and compromising its standards "to comply with the masses in p[u]rsuit of volume."

In presentations to investors, Nomura outlined a rigorous and, so it claimed, industry-leading securitization process. In practice, however, Nomura regularly disregarded the findings of third-party due diligence vendors and knowingly securitized extremely risky loans in the Subject Deals. Moreover, Nomura continued to do business with loan originators, such as Alliance CA, People's Choice, and Quick Loan, that, according to Nomura's due diligence personnel, were "extremely dysfunctional," had "systemic" underwriting issues, and employed "questionable" origination practices. Indeed, in October 2006—a month in which Nomura securitized over $1.5 billion worth of loans—a member of Nomura's RMBS origination sales team sent an email to the entire Nomura RMBS group stating that "advertising will be a great career when all these loans finally blow up . . . (I will be selling vacuum cleaners door to door when the market goes by the way)."

Ultimately, by acquiescing to loan originators and by compromising its much heralded due diligence processes, Nomura shifted substantial, undisclosed risks (and ultimately, substantial losses) to investors, which included university endowments, retirement funds, and federally-insured financial institutions.

[1] As stated in the Agreement of Settlement and Release, this Annex consists of allegations of the United States, which Nomura disputes.

I. NOMURA'S RMBS DUE DILIGENCE PROCESS

According to Nomura's presentations regarding its RMBS platform, which Nomura modified from time to time, its due diligence process was "extensive," "disciplined," and "carefully developed." Nomura also told investors that it only worked with "hand-picked industry leading" due diligence vendors, and that, as a result of its superior standards and due diligence processes, "Nomura's loan performance should surpass industry standards."

The main purpose of RMBS due diligence, according to Nomura employees, was to confirm the accuracy of Nomura's representations to investors. Nomura's due diligence process had two components. The first component, "credit and compliance" due diligence, was intended to determine whether the loans complied with underwriting guidelines and all applicable laws and regulations. The second component, "valuation" due diligence, was intended to assess the reasonableness of originator-provided appraisal values and to confirm the accuracy of various representations based on those values. Nomura hired third-party due diligence vendors to assist with those determinations.

A. Credit and Compliance Due Diligence

The percentage of loans that Nomura reviewed during credit and compliance due diligence depended on whether Nomura purchased the loans as part of "bulk pools" (single purchases with a face value of more than $25 million), "mini-bulk" pools (single purchases with a face value of less than $25 million), or through Nomura's "loan-by-loan" channel (individual loan purchases).

Nomura's general practice for bulk pools, which accounted for nearly 60% of all loans securitized in the Subject Deals, was to review an adversely selected sample of loans representing 25% of the pool. Nomura understood that, if there was a high percentage of defective loans identified in its samples, there would also be defective loans in the unreviewed portions of its loan pools.

For loans purchased in mini-bulk pools or through Nomura's loan-by-loan channel, Nomura purported to conduct "100%" due diligence. According to Nomura, all of these loans were subject to some form of individualized credit and compliance review.

Loans selected for credit and compliance due diligence were sent to Nomura's third-party due diligence vendors for review, who presented their results to Nomura in detailed reports. In general, Nomura's due diligence vendors assigned every loan reviewed an "event level" grade and provided Nomura with explanatory comments for the assigned grade.[2]

A loan was graded Event Level 1 ("EV1") if the vendor determined that it was originated in accordance with all applicable underwriting guidelines, laws, and regulations. A loan was graded Event Level 2 ("EV2") if it did not comply with the originator's guidelines or all applicable laws and regulations, but sufficient and documented compensating factors offset the risk associated

with the exceptions to the underwriting guidelines.[2] A loan was graded Event Level 3 ("EV3") if (1) the loan was not originated according to underwriting guidelines and did not have sufficient documented compensating factors, (2) the loan did not comply with all applicable laws and regulations, (3) certain material documents could not be located in the loan file, or, in some instances, (4) the loan did not comply with certain additional criteria that Nomura believed warranted further review.

One of Nomura's vendors also often used a fourth designation, "EV2W," to reflect instances where Nomura instructed the vendor to change the grade of a loan from EV3 to EV2.[3] The vendor also referred to these loans as "client overrides." The "W" in the designation was short for "waiver" and was meant to "call[ ] a spade a spade" when a client overrode the vendor's EV3 determination. Nomura's other credit and compliance due diligence vendors generally did not make a record of when Nomura instructed them to modify their due diligence findings.

B. Valuation Due Diligence

In presentations outlining its valuation due diligence processes, Nomura described a multi-step valuation due diligence process through which all loans securitized in the Subject Deals were subjected to various levels of valuation review, beginning with an automated valuation model or "AVM." In these presentations, Nomura claimed that "100%" of the loans in the Subject Deals underwent an AVM review. Any loans that did not meet the parameters of Nomura's AVM review would receive further valuation review in the form of a broker price opinion ("BPO") and, ultimately, a value "reconciliation" with the originator-provided appraisal.

According to Nomura's stated valuation due diligence process, after an AVM value was generated for a property, Nomura's vendors compared that value to the original appraisal value. If the AVM value was within 10% of the originator's value for subprime loans or 15% for Alt-A loans (Nomura's stated "tolerance" levels), the loan was deemed "within tolerance." If the AVM value exceeded Nomura's tolerance levels, the loan was considered "out of tolerance" and was supposed to proceed to the next stage of valuation due diligence.

Nomura's tolerance levels also applied to subsequent steps of Nomura's valuation process, including BPOs. In general, if the final variance between a loan's original appraisal value and the value determined by Nomura's due diligence vendors was out of tolerance, the loan should not have been securitized.

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[2] For example, per one originator's guidelines, "a borrower's down payment, credit history, additional income, financial reserves, and pattern of savings" could be considered compensating factors for "lack of long-term employment history."

[3] This vendor typically did not use this designation in reports provided to Nomura.

II. NOMURA'S MISREPRESENTATIONS TO INVESTORS

Although Nomura projected unqualified confidence in its "extensive" due diligence processes, virtually every member of Nomura's RMBS team knew that a significant number of noncompliant and high-risk loans were securitized in the Subject Deals. Nomura employees knew, for example, that, even for Subject Deals where a high percentage of loans underwent due diligence review, the results of those reviews were regularly ignored, resulting in thousands of defective loans being securitized. Furthermore, even after many of these loans began to default shortly after origination, Nomura took no action to improve its review processes, and continued to do business with originators that Nomura knew employed shoddy, and in some cases fraudulent, underwriting practices.

A. Nomura Knew That Its Representations Regarding Loan Quality Were False

For each of the Subject Deals, Nomura represented to investors that the mortgage loans were originated generally in accordance with applicable underwriting guidelines, laws, and regulations. At the time those representations were made, Nomura knew they were false.

1. Nomura Securitized Thousands of Loans That Failed Credit and Compliance Due Diligence

The percentage of loans that received an EV2W or EV3 grade from Nomura's credit and compliance due diligence vendors, but were securitized anyway, is significant: almost 4,000 loans received a grade of EV2W or EV3 from Nomura's due diligence vendors. Moreover, when considering this number in the context of loans that actually received event grades, *i.e.*, excluding unreviewed loans and all loan-by-loan channel loans (which did not use EV grades in the due diligence process), those totals were much higher. Indeed, three of the Subject Deals had EV2W/EV3 percentages exceeding 20%, and six more Subject Deals had EV2W/EV3 percentages between 15% and 20%.

These totals only tell part of the story, however, since Nomura employees personally approved a significant number of additional "exceptions" or "waivers" for loans that did not comply with applicable underwriting guidelines, but were never recorded as "EV2Ws" in the vendor's final due diligence reports. Internal Nomura communications show that members of Nomura's RMBS due diligence group repeatedly instructed Nomura's vendors to change their findings on certain loans, without justification, or to waive in entire categories of loans.

Nomura knew that many of these waivers—especially those granted in connection with its loan-by-loan program—were improper and unrelated to valid compensating factors. In many instances, Nomura waived in defective loans as "favors" to its originator "clients." In one instance, a loan originator that asked for an exception openly lamented to Nomura's former head of RMBS due diligence that she could not call on him to help her "push . . . dogsh[*]t loans through anymore." Not only did Nomura grant the exception, but it thereafter purchased another $38 million worth of loans from that originator.

In another example, a different originator told Nomura's head of RMBS due diligence that it "need[ed] some real help!" because it was "sitting on a hot potato." That "hot potato," which Nomura's head of due diligence promised to get "off [the originator's] seat right away," was an unverified "stated income/stated asset" loan with a 100% combined loan-to-value ratio where the borrower had credit scores below guidelines, did not have sufficient savings (per the applicable underwriting guidelines), and could not afford closing costs. After telling another member of Nomura's due diligence team, "I smell blood," Nomura's head of due diligence approved the exception and the loan was purchased and securitized in NAAC 2006-AR4.

In yet another example, Nomura waived in a defective loan that Nomura's head of RMBS due diligence described as "a garbage exception" with "too much risk and reflect[ing] zero commitment by the borrower."

In many other instances, Nomura waived in defective and high-risk loans after getting originators to reduce the price that they charged Nomura for such loans. These reductions, which Nomura referred to as a "price hits," lowered Nomura's exposure to losses on those shoddy loans, but offered no similar benefit to Nomura's investors in exchange for the additional risk for the loans that were securitized. Likewise, Nomura waived in defective and high risk loans after obtaining protection against the risk of default on those loans prior to securitization. This protection, known as early payment default ("EPD") protection, reduced Nomura's exposure to loss by extending the time period (typically between 30 and 120 days) during which Nomura's originators were contractually required to repurchase delinquent loans, but, again, offered no additional protection to Nomura's investors if the loan was securitized after the extended EPD protection period.

For Nomura, price hits and EPD protection were not only useful as bargaining chips with originators, but, as the residential mortgage market started to decline, they also provided Nomura an opportunity to leverage its competitors' unwillingness to buy those same defective loans. As recounted in February 2007 by Nomura's head of RMBS due diligence, senior members of Nomura's RMBS group believed that Nomura's competitors were "not considering exceptions as much as before" and, as a result, Nomura could "squeeze out some more margin" by buying loans that other banks would not. He added that some of Nomura's originators would get "pissed" by the discounted pricing, and that extended EPD protection "scare[d] the hell out of them," but they "may have no place to go." As stated by another member of Nomura's RMBS due diligence group: "There is no such thing as a bad loan . . . just a bad price."

Finally, on several occasions, Nomura waived in large groups of loans for no apparent reason other than to improve "pull through rates" (the percentage of loans that Nomura agreed to purchase following due diligence) and to make its loan pools appear to be of a better quality than they actually were. In September 2006, for example, in an email with the subject line "Huge Favor—Fremont ASAP," Nomura's head of RMBS due diligence instructed Nomura's vendor to "override" the EV3 grade of 19 loans that Nomura (prior to his joining the company) had "for whatever reason" decided to purchase so they could securitize them less than a month later in NHELI 2006-FM2. Later, when describing Nomura's due diligence on the deal to the lead underwriter, Nomura's head of due diligence, in his own words, "took the liberty to bullsh[*]t them."

Nomura did not disclose to investors its practice of waiving in defective loans without compensating factors. Nor did it disclose the increased risk associated with these loans. In fact, when describing the characteristics of the loans in the Subject Deals to investors, rating agencies, and securitization partners, Nomura presented loan data supplied directly from originators, which Nomura knew in many instances was materially false.

2. Nomura Knew That a Significant Number of Loans That Were Not Included in Its Samples Were Defective

Although Nomura's credit and compliance review percentages varied widely across the Subject Deals, a significant number of loans in the Subject Deals were purchased in bulk pools where due diligence was conducted on as few as 25% of the loans. In addition, despite the fact that Nomura told investors that it conducted "100%" due diligence on mini-bulk pools, Nomura also conducted sampling on many such pools. In total, over 40% of all loans in the Subject Deals were not subject to any credit and compliance due diligence.

Based on information Nomura learned during its review of sampled loans—namely, inexplicably high percentages of loans that received EV2W or EV3 grades from Nomura's due diligence vendors—Nomura knew that a significant number of the unreviewed loans also contradicted its representations to investors. Nonetheless, Nomura rarely expanded its due diligence reviews to identify and remove additional defective loans from the unreviewed portions of its loan pools—even for loan pools where as much as 30% of the due diligence sample received a final grade of EV3. Nomura simply ignored the findings of its due diligence vendors and falsely represented to investors that the loans in the Subject Deals generally complied with underwriting guidelines and applicable laws.

Altogether, among large loan pools that contributed more than 500 loans to the Subject Deals, the average final EV3 percentage was approximately 18%. Nomura employees knew that these percentages meant that there were additional defective loans throughout the remaining unreviewed loans, but disclosed neither this additional risk nor the high percentage of noncompliant loans in the Subject Deals.

B. Nomura Knew That Its Representations Regarding Property Values Were False

In addition to representations regarding compliance with applicable guidelines, laws, and regulations, Nomura also made numerous representations to investors regarding specific value-related characteristics of the securitized loans, including representations of loan-to-value ("LTV") and combined loan-to-value ("CLTV") ratios, which were dependent on originator-provided property values. Based on its due diligence, Nomura knew that many of these originator-provided appraisal values were significantly inflated—and in many instances, likely fraudulent—but did not correct its description of loan values in its offering documents, or otherwise disclose to investors what it learned about these loans during due diligence.

1. Nomura Falsely Represented That All Loans in the Subject Deals Underwent AVM Reviews

As noted above, Nomura claimed in investor presentations that its multi-stage valuation due diligence process began with a "100% AVM" review. This claim was false. Nomura did not actually conduct "100% AVM" reviews, but instead—in an effort to "keep [due diligence] cost[s] down"—Nomura pre-screened and removed nearly half of all loans securitized in the Subject Deals (over 28,000 total) from AVM review based largely on other, less expensive review tools. Unlike AVMs, these tools did not purport to assess the reliability of originator-provided appraisal values, and merely provided scores meant to signify "collateral risk." Moreover, Nomura's head of RMBS due diligence openly acknowledged that a "garbage dump" would pass some of these forms of due diligence "with flying colors."

Additionally, many other loans that were submitted for AVM review were returned to Nomura as "no hits," meaning that an AVM could not be generated for the property. Rather than upgrading these loans to the next step in Nomura's review process, Nomura waived thousands of such loans into the Subject Deals with no valuation due diligence beyond, where applicable, any appraisal review conducted as part of Nomura's credit and compliance due diligence.

2. Nomura Securitized Thousands of Out of Tolerance and Underwater Loans in the Subject Deals

Even when Nomura did conduct AVMs, it regularly abandoned its stated due diligence processes by ignoring its valuation tolerance levels and by securitizing loans that it knew were based on materially inflated appraisals. It did so knowing that appraisers were facing immense pressure from originators to "back into" pre-determined values and to "find comp[arable]s to support the loan[s]" rather than objectively assessing property values, resulting in "polluted" appraisals.

Despite these concerns, Nomura securitized over 2,000 loans in the Subject Deals that Nomura's vendors determined were out of tolerance after the final stage of appraisal review.

Further, Nomura securitized over 5,000 loans in the Subject Deals that were "underwater," meaning that they had CLTV ratios greater than 100% based on Nomura's valuation due diligence, which generally included AVM reviews and, less frequently, BPOs. These underwater loans significantly increased investors' risk of loss in the Subject Deals because, in the event of a foreclosure, the anticipated proceeds from the sale of the mortgaged properties would not cover the unpaid balances of the loans. Also, as Nomura was aware, loans where the borrowers' loan balances were greater than the value of their home were far more likely to enter into delinquency, because these borrowers had a greater incentive to abandon their repayment obligations.

Nomura disregarded inflated property appraisals because, among other reasons, it understood that "test[ing] more values" on loans it purchased from originators would jeopardize its ability to purchase additional loans from those originators in the future. Thus, "for the sake of moving forward," Nomura's "pencils [could] be sharpened to bring the values back to [within the]

tolerance level." Likewise, for several very large loan pools, Nomura agreed to simply increase its tolerance levels to avoid a high number of loans being flagged for further valuation review.

Nomura did not share its valuation due diligence results with investors. Nor did it disclose that it had securitized thousands out of tolerance and underwater loans (based on its valuation due diligence tools) in the Subject Deals. Instead, Nomura presented appraisal values supplied directly from originators, many of which Nomura knew were likely to be materially inflated, and provided no additional information reflecting what Nomura learned about those property values during the due diligence process.

C. Nomura Knew That Its Allegedly "Extensive" and "Disciplined" Due Diligence Process Was Compromised

Nomura misled investors about the quality of its originators and, more generally, about the integrity of its due diligence process as a whole. Nomura claimed in certain promotional materials that it did "repeat business with sellers that ha[d] solid performance and limit[ed] business with sellers that ha[d] poor performance," and claimed that, as a result of its superior due diligence processes, the loans in its RMBS would exceed industry standards. In reality, the opposite was true: Nomura continued to work with originators that it knew employed questionable underwriting practices, and compounded this problem by failing to address known weaknesses in due diligence processes.

1. Nomura Continued to Do Business with Originators That It Knew Were Employing Questionable Underwriting Practices

As the sponsor and issuer of all of the Subject Deals, Nomura had direct communication with originators and first-hand knowledge regarding the quality of their underwriting practices. With this information, Nomura was well-positioned to decide whether to discontinue business with particular originators, and whether, on a deal-by-deal basis, additional disclosures were necessary to adequately inform investors. Nomura rarely did either.

Although Nomura's RMBS due diligence personnel frequently warned senior members of the RMBS group about problems with particular originators, their warnings were routinely ignored. In February 2006, for example, a member of the due diligence group drafted recommendations, based on due diligence findings, to limit future business with certain originators (and in some instances, to discontinue future business altogether). After the recommendations were shared at a meeting attended by a managing director of the RMBS group, Nomura continued to purchase over 1,000 loans (with an aggregate original balance of over $345 million) from originators that the draft recommended removing from the "buy/approved list." One such originator, Quick Loan, was referred to by the due diligence group as "Quick Fraud." Another, Mortgage Store, was described as being "100% outside Seller's [guidelines]. [A]lways has been."

Similarly, in May 2006, a member of Nomura's due diligence team described its trade with an originator named People's Choice as a "crap show" due to the high number of loans that failed valuation due diligence. Separately, Nomura's head of RMBS due diligence remarked that "there is obviously an inherent flaw in their origination process." Yet, even after these concerns were

identified, Nomura securitized over 2,000 loans from this originator in NHELI 2006-HE3. Nomura told investors only that the loans in the deal were "generally consistent with and conform to [People's Choice's] Underwriting Guidelines."

In fact, despite numerous red flags, Nomura was even willing to buy loans from originators that already owed Nomura tens of millions of dollars for outstanding EPD claims. For example, by September 2006, an originator named Ownit Mortgage Solutions ("Ownit") owed Nomura nearly $30 million in outstanding EPD claims, but rather than discontinuing business with this dysfunctional originator, Nomura purchased and securitized loans from another three Ownit pools between September and November of 2006—all while Ownit's EPDs remained unpaid. Ownit went out of business just six days after Nomura purchased the last of these pools.

Likewise, in October 2006, Nomura securitized over 5,700 loans from an originator named Fremont Investment & Loan ("Fremont"), which by that time owed Nomura approximately $80 million in outstanding EPDs—the most of any Nomura originator. Nomura's due diligence on samples comprising 25% of these loan pools revealed that at least one in every four loans reviewed had a final grade of EV3.[4] Despite the high percentage of EV3s, and despite the extraordinary number of Fremont loans that were already EPDs, Nomura conducted no further credit and compliance due diligence on the loans outside of these samples, and securitized over 4,600 unreviewed Fremont loans in the Subject Deals.

2. Nomura's Alarming Due Diligence Results Nonetheless Understated the Extent of Defective Loans in the Subject Deals

As noted, Nomura knew, based on its due diligence results, that thousands of loans securitized in the Subject Deals did not comply with underwriting guidelines, were out of tolerance or underwater, or had both credit and value-related defects. But Nomura also knew that, as alarming as these due diligence findings were, they were still understating the number of noncompliant and defective loans in its review samples.

For example, Nomura received multiple reports, including independent "reunderwriting" analyses, confirming that Nomura's due diligence process was ineffective in removing deficient and noncompliant loans from Nomura's RMBS. In one instance, a third-party reunderwriting firm hired by Nomura reviewed a sample of securitized loans from the Subject Deals and identified loans that received passing grades during Nomura's credit and compliance review despite having material defects. Separately, Nomura received a research report indicating that, as described by Nomura's Chief Legal Officer, Nomura was "third from the bottom of 28 [RMBS] issuers with problems" and that "the key cause [was] poor underwriting." Nomura took no action to reform its due diligence processes as a result of these reports.

Additionally, Nomura's own due diligence personnel believed that some of Nomura's due diligence vendors may have been "compromised" because they were "too deep" with Nomura's

[4] These samples were selected using a program developed by a rating agency that a Nomura employee described as a "black box," and which Nomura's head of RMBS due diligence warned could lead to Nomura "taking on abnormal loan level credit/compliance risk."

originators, and were specifically warned about one vendor's lax reviews. Nonetheless, after Nomura removed its head of RMBS due diligence in mid-2006, and replaced him with a new head of due diligence that at one point offered to "serve the best interests of [Nomura's] trading desk," Nomura's vendors were given authority to grant certain credit "exceptions" by approving compensating factors for noncompliant loans with no further input by Nomura. Nomura also expanded its valuation program, "Value Pass," to allow loan-by-loan originators to seek property valuations directly from Nomura's vendors. As long as the loans were found within tolerance by the third-party vendors, "no questions [would be] asked" on the originator-provided appraisal values. Even Nomura's own due diligence team confessed to feeling "a little foolish" for implementing these changes when Nomura was "GOING INTO A DANGEROUS R/E MARKET."

Finally, Nomura included high-risk loans in the Subject Deals by relaxing the underwriting guidelines for loans purchased through its loan-by-loan channel. Unlike loans purchased in bulk and mini-bulk pools, which were underwritten to originator guidelines, loans purchased through Nomura's loan-by-loan channel were purchased pursuant to guidelines developed by Nomura. Therefore, Nomura could change its guidelines if it wanted to increase the number of loans that it could purchase and ultimately securitize.

Some Nomura employees were initially resistant to such changes. Nomura's head of RMBS due diligence warned, for instance, that Nomura had already "loosened guidelines in so many areas" that it was "at risk of giving away the proverbial store." Nonetheless, the prevailing view, as characterized by Nomura's RMBS trading desk, was that Nomura's "box [was] too restrictive." Thus, in April 2006, Nomura approved new guidelines that were "much more liberal across the board" and even allowed for the purchase of loans that Nomura's due diligence personnel previously described as "sheer lunacy."

SUBJECT DEALS

NHELI 2006-HE1
NAA 2006-AR2
NHELI 2006-HE2
NAA 2006-AF1
NHELI 2006-WF1
NAA 2006-AF2
NAA 2006-WF1
NHELI 2006-HE3
NAA 2006-AR3
NHELI 2006-FM2
NHELI 2006-AF1
NAA 2006-AR4
NHELI 2007-1
NHELI 2007-2
NHELI 2007-3
NAA 2007-1
NAA 2007-2
NAA 2007-3