SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

LORELEY FINANCING (JERSEY) NO. 3 LTD.; LORELEY FINANCING (JERSEY) NO. 4 LTD.; LORELEY FINANCING (JERSEY) NO. 8 LTD.; LORELEY FINANCING (JERSEY) NO. 12 LTD.; LORELEY FINANCING (JERSEY) NO. 19 LTD.; LORELEY FINANCING (JERSEY) NO. 22 LTD.; LORELEY FINANCING (JERSEY) NO. 24 LTD.; LORELEY FINANCING (JERSEY) NO. 26 LTD.; LORELEY FINANCING (JERSEY) NO. 28 LTD.; LORELEY FINANCING (JERSEY) NO. 31 LTD.; and LORELEY FINANCING (JERSEY) NO. 32 LTD.,

Plaintiffs,

-against-

DEUTSCHE BANK SECURITIES, INC.; DEUTSCHE BANK AG; HBK INVESTMENTS, LP; HBK PARTNERS II LP; HBK MANAGEMENT LLC; STATIC RESIDENTIAL 2005-C LTD.; STATIC RESIDENTIAL 2005-C CORP.; STATIC RESIDENTIAL 2006-B LTD.; STATIC RESIDENTIAL 2006-B CORP.; CARINA CDO LTD.; CARINA CDO CORP.; BARRAMUNDI CDO I LTD.; GEMSTONE CDO VII, LTD.; GEMSTONE CDO VII CORP.; PINE MOUNTAIN CDO III LTD.; and, PINE MOUNTAIN CDO III CORP.,

Defendants.

Index No._________________
Date Purchased: October 5, 2011

Plaintiffs designate New York County as the place of trial

The basis of venue is contractual election pursuant to CPLR § 501 and residence of one of more of the parties pursuant to pursuant to CPRL § 503

SUMMONS

TO THE ABOVE NAMED DEFENDANTS:

YOU ARE HEREBY SUMMONED to answer the Complaint in this action and to serve a copy of your answer, or if the Complaint is not served with this summons, to serve a notice of appearance on Plaintiffs' attorneys within 20 days after the service of this summons, exclusive of the day of service (or within 30 days after the service is complete if this summons is not personally delivered to your within the State of New

York); and in the case of your failure to appear or answer, judgment will be taken against you by default for the relief demanded in the Complaint.

Dated: New York, NY
October 5, 2011

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& FRIEDMAN LLP

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Plaintiffs Loreley Financing (Jersey) Nos. 3, 4, 8, 12, 19, 22, 24, 26, 28, 31, and 32 Ltd. (each, "LFJ" followed by the applicable number, and collectively, "Plaintiffs"), as and for their complaint against Defendants Deutsche Bank Securities, Inc. ("DBSI") and Deutsche Bank AG ("DB AG," and together with DBSI, "Deutsche Bank"); HBK Investments, LP ("HBK Investments"), HBK Partners II LP ("HBK Partners"), and HBK Management LLC ("HBK Management," and together with HBK Investments and HBK Partners, "HBK"); STAtic ResidenTial 2005-C Ltd. and STAtic ResidenTial 2005-C Corp. (collectively, "START 2005-C"); STAtic ResidenTial 2006-B Ltd. and STAtic ResidenTial 2006-B Corp. (collectively, "START 2006-B," and together with START 2005-C, the "START CDOs"); Carina CDO Ltd. and Carina CDO Corp. (collectively "Carina"), Barramundi CDO I Ltd. ("Barramundi"); Gemstone CDO VII, Ltd. and Gemstone CDO VII Corp. (collectively, "Gemstone VII"); and Pine Mountain CDO III Ltd. and Pine Mountain CDO III Corp. (collectively, "Pine Mountain III"), allege on knowledge as to themselves and their own actions, and on information and belief as to all other matters, as follows:

SUMMARY OF THE ACTION

1. This action arises out of Defendants' fraudulent misrepresentations and concealment in arranging and convincing Plaintiffs to invest in six collateralized debt obligations ("CDOs") between 2005 and 2007. Each of these CDOs – START 2005-C, START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III – was a fraudulent investment vehicle created and exploited by Defendants for their own benefit and the benefit of certain preferred Deutsche Bank clients looking to profit from the imminent collapse of the subprime mortgage market. In total, Deutsche Bank and the other Defendants defrauded Plaintiffs into investing

nearly $440 million in CDOs that Deutsche Bank knew were destined – and, indeed, designed – to fail.

2. During the relevant time period, Deutsche Bank was one of the most active financial institutions in the subprime capital markets, and had detailed information about the health of the industry that Plaintiffs did not have.

3. By its own admission, Deutsche Bank was a "leading player" in the business of packaging pools of subprime mortgage loans into residential mortgage-backed securities ("RMBS"). To grow that lucrative business (for which it earned fees of up to $8 million per deal), Deutsche Bank acquired two subprime lenders for the stated purpose of procuring a "steady source of product" (*i.e.*, subprime mortgages). When even this could not meet its RMBS business's demand for loans, Deutsche Bank resorted to purchasing mortgages from subprime lenders it knew were unscrupulous, including Fremont Investment and Loan ("Fremont"), Countrywide Home Loans ("Countrywide"), and New Century Mortgage Corp. ("New Century"). Deutsche Bank encouraged these and other lenders to generate ever-larger numbers of subprime loans – the grist for Deutsche Bank's massive RMBS operation – by bankrolling them with billions of dollars in funding through warehouse lines of credit, and in some cases agreeing to purchase loans before they were even generated. As lucrative as these businesses were, Deutsche Bank earned even richer fees – as high as $10 million per deal – packaging RMBS into CDOs for sale to long investors, including Plaintiffs. Between 2004 and 2008, Deutsche Bank arranged a total of 47 CDOs valued at over $32 billion, and in 2006 and 2007 Deutsche Bank was the fourth largest arranger of CDOs in the world.

4. By late 2005, based on its inside knowledge of the industry, Deutsche Bank became aware that the foundations supporting the subprime capital markets were cracking and

that the "CDO machine" (in the words of Deutsche Bank's top global CDO trader) was a house of cards ready to collapse. Based on detailed due diligence reports Deutsche Bank received as an originator of subprime loans and a securitizer of RMBS based on those loans, Deutsche Bank knew that more than one in every three of the subprime loans it was purchasing for its securitization business failed to satisfy the underwriting guidelines of the loans' originators and of Deutsche Bank itself. As Deutsche Bank well knew, these loans were much more likely to default (and to default earlier) than were conforming loans and were much more likely to be tainted by fraud (on the part of the borrowers, the lenders, or both). An ethical, responsible, arranging bank would have put these non-conforming loans back to the originators and conducted a thorough investigation of the other loans it was planning to securitize. Instead, Deutsche Bank waived half of these toxic, non-conforming loans into its RMBS, which it then packaged into CDOs and sold to investors, including Plaintiffs, without disclosing their toxicity, generating huge fees for Deutsche Bank.

5. When Deutsche Bank was marketing the CDOs at issue in this complaint to Plaintiffs, Deutsche Bank knew – but concealed from Plaintiffs – that the RMBS underlying those CDOs were considerably riskier than represented and already were experiencing elevated rates of default. Deutsche Bank exploited its peculiar knowledge by offloading these toxic RMBS from its own books into the CDOs it was marketing to Plaintiffs, while at the same time recommending that its preferred clients place massive short[1] bets against these same assets.

[1] An investor who takes a "long" position in a security stands to gain when the security performs or increases in value; by contrast, an investor who stands to profit when the security fails to perform or falls in value is referred to as having a "short" position or to be "short" that security.

6. For example, Deutsche Bank and Defendant HBK were aware that Plaintiffs were interested in investing in the less risky, highly-rated, highly-subordinated[2] senior tranches of CDOs, and they therefore marketed one of the CDOs at issue in this case, Gemstone VII, as an opportunity that met Plaintiffs' investment criteria. Yet, as detailed by the U.S. Senate Permanent Subcommittee on Investigations in its recently-issued report on the financial crisis, Deutsche Bank internally knew those representations to be false and misleading. Greg Lippmann, Deutsche Bank's head global CDO trader, described – to certain preferred clients, but not to Plaintiffs – the CDO business as a "Ponzi scheme," and actively encouraged his clients to bet against – *i.e.*, to short –RMBS that he described as "horrible," "pigs," and "crap." Simultaneously, however, Lippmann's trading desk helped to place many of these same assets into the Gemstone VII portfolio – even as they were "blowing up," suffering from "serious delinquencies," and poised to undergo "payment shock."

7. Unlike Deutsche Bank and HBK, Plaintiffs had neither close institutional relationships with loan originators and mortgage servicers, nor access to the underlying loan-level data. Consequently, Plaintiffs had no way of knowing how toxic the collateral underlying the CDOs really was.

8. As another example, Deutsche Bank colluded with a hedge fund known as Magnetar Capital LLC ("Magnetar"), now notorious as the architect of more than 26 Constellation CDOs which it used as vehicles for its undisclosed short-trading strategy designed to reap huge profits from the collapse of those very same deals. Deutsche Bank was intimately

[2] In the structured finance context, "subordination" refers to the existence of classes of notes with a lower payment priority in the event that the pool from which payment can be made is insufficient; hence, a "highly-subordinated" investment is one that benefits from the existence of a large cushion of notes with a lower payment priority.

involved in Magnetar's strategy from its early days, having served as equity co-sponsor on the first and subsequent Constellation CDOs.

9. Unbeknownst to the general investing public and Plaintiffs, but well known to Deutsche Bank, Magnetar sponsored these CDOs by purchasing their hard-to-sell equity tranches (which carry the most risk but earn the highest returns) at discounted prices, while at the same time secretly placing inexpensive leveraged short bets against those same CDOs through credit default swaps ("CDS") which generated enormous net profits for Magnetar when the CDOs failed.

10. The Carina CDO followed this pattern. Deutsche Bank marketed Carina to Plaintiffs as a legitimate long investment opportunity meeting Plaintiffs' stringent investment requirements, without disclosing these material facts. Deutsche Bank knowingly allowed Magnetar, a short investor with interests that were adverse to the success of Carina, to dictate the collateral selection criteria and deal structure, yet failed to disclose to unsuspecting investors that these parameters had been devised and implemented by Magnetar in furtherance of its clandestine short-trading scheme. Moreover, unbeknownst to Carina's long investors, Deutsche Bank caused the Carina CDO to sell credit protection to Magnetar via CDS contracts at below-market prices. Again, none of this was disclosed to Plaintiffs. In short, Deutsche Bank helped Magnetar stack the deck, and then knowingly misled and concealed from Plaintiffs and other long investors that the deck had been stacked – indeed, that the game itself had been rigged – so that Magnetar, unlike Plaintiffs, would win no matter which way the cards were dealt.

11. While the details of these and other CDOs at issue in this complaint vary, a common theme runs through them: Deutsche Bank and the other Defendants stuffed these investment vehicles with "pigs" and "crap" assets that they wanted to unload onto long investors

for the benefit of themselves and preferred short clients who were betting that these assets would fail; at the same time, Defendants fraudulently marketed these CDOs to Plaintiffs and other long investors as high-grade investments whose portfolios had been selected for the benefit of long investors and in the interest of the deals' success. In short, Deutsche Bank, working together with the other Defendants, used and abused the information it gained from its special position as a "leading player" in the subprime industry to profit on the backs of – in Greg Lippmann's words – the "[s]tupid Germans" (a reference to Plaintiffs' investment advisor) who "take rating agencies seriously" and "believe in the rules."

12. In the end, Defendants' conduct caused Plaintiffs to lose nearly $440 million.

13. Plaintiffs therefore bring this action seeking compensatory and punitive damages, as well as rescission, arising from Defendants' fraud, aiding and abetting fraud, conspiracy to defraud, fraudulent conveyance, and unjust enrichment.

THE PARTIES

A. The Plaintiffs

14. Plaintiff LFJ 3 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 3 invested in and is the owner of $35 million of Carina Class B-2 Notes.

15. Plaintiff LFJ 4 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 4 invested in and is the owner of $20 million in Gemstone VII Class A-2 Notes.

16. Plaintiff LFJ 8 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 8 invested in and is the owner of $21 million in START 2006-B Class B-2 Notes.

17. Plaintiff LFJ 12 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 12 invested in and is the owner of $30.5 million in Carina Class C-1 and $19.5 million in Carina Class C-2 Notes.

18. Plaintiff LFJ 19 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 19 invested in and is the owner of approximately $38.5 million in START 2005-C Class A-2 Notes, $4 million in START 2005-C Class B Notes, and $17.5 million in START 2005-C Class C Notes.

19. Plaintiff LFJ 22 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 22 invested in and is the owner of $18 million in Barramundi Class C Notes.

20. Plaintiff LFJ 24 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 24 invested in and is the owner of $39 million in START 2006-B Class A-2 Notes and $30 million in START 2006-B Class B-1 Notes.

21. Plaintiff LFJ 26 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 26 invested in and is the owner of $15 million in Carina Class B-1 Notes.

22. Plaintiff LFJ 28 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 28 invested in and is the owner of $61 million in Barramundi Class B Notes.

23. Plaintiff LFJ 31 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 31 invested in and is the owner of $44.875 million in Pine Mountain III Class A-3 Notes.

24. Plaintiff LFJ 32 is a company organized and existing under the laws of Jersey, Channel Islands, located at 26 New Street, St. Helier, Jersey JE2 3RA, Channel Islands. Plaintiff LFJ 32 invested in and is the owner of $44.875 million in Pine Mountain III Class A-3 Notes.

B. The Defendants

25. Defendant START 2005-C Ltd. is a Cayman Islands limited liability company located at P.O. Box 1984 GT, c/o Deutsche Bank (Cayman) Limited, Elizabethan Square, George Town, Grand Cayman, Cayman Islands. START 2005-C Ltd. is the issuer of the START 2005-C Class A-2 Notes, Class B Notes, and Class C Notes (collectively, the "START 2005-C Notes") sold to Plaintiff LFJ 19. Pursuant to the Offering Circular issued in connection with the START 2005-C Notes, START 2005-C Ltd. appointed CT Corporation, located at 111 8th Avenue, 13th Floor, New York, New York 10011-5252, as its agent for service of process.

26. Defendant START 2005-C Corp. is a Delaware corporation located at 850 Library Avenue, Suite 204, Newark, Delaware 19715. START 2005-C Corp. is the co-issuer of the START 2005-C Notes sold to Plaintiff LFJ 19.

27. Defendant START 2006-B Ltd. is a Cayman Islands limited liability company located at P.O. Box 1984 GT, c/o Deutsche Bank (Cayman) Limited, Elizabethan Square, George Town, Grand Cayman, Cayman Islands. START 2006-B Ltd. is the issuer of the START 2006-B Class A-2 Notes and Class B-1 Notes sold to Plaintiff LFJ 24, and the Class B-2 Notes sold to Plaintiff LFJ 8 (collectively, the "START 2006-B Notes"). Pursuant to the Offering Circular issued in connection with the START 2006-B Notes, START 2005-B Ltd.

appointed CT Corporation, located at 111 8th Avenue, 13th Floor, New York, New York 10011-5252, as its agent for service of process.

28. Defendant START 2006-B Corp. is a Delaware corporation located at 850 Library Avenue, Suite 204, Newark, Delaware 19711. START 2006-B Corp. is the co-issuer of the START 2006-B Notes sold to Plaintiff LFJ 8 and to Plaintiff LFJ 24.

29. Defendant Carina CDO Ltd. is a Cayman Islands exempted limited liability company located at P.O. Box 1984, Grand Cayman KY1-1104, c/o Deutsche Bank (Cayman) Limited. Carina CDO Ltd. is the issuer of the Carina Class B-2 Notes sold to LFJ 3, the Carina Class C-1 and C-2 Notes sold to LFJ 12, and the Carina Class B-1 Notes sold to LFJ 26 (collectively the "Carina Notes"). Pursuant to the Offering Memorandum issued in connection with the Carina Notes, Carina CDO Ltd. appointed CT Corporation System, located at 111 8th Avenue, 13th Floor, New York, New York 10011-5252, as its agent for service of process.

30. Defendant Carina CDO Corp. is a Delaware corporation located at 1011 Centre Road, Suite 200, Wilmington, DE 19805-1266. Carina CDO Corp. is the co-issuer of the Carina Notes sold to LFJ 3, LFJ 12 and LFJ 26.

31. Defendant Barramundi CDO I Ltd. is a Cayman Islands limited liability company located at c/o Maples Finance Limited, P.O. Box 1093GT, Queensgate House, South Church Street, George Town, Grand Cayman, Cayman Islands. Barramundi CDO I Ltd. is the issuer of the Barramundi Class B Notes sold to Plaintiff LFJ 28 and the Barramundi Class C Notes sold to Plaintiff LFJ 22 (collectively, the "Barramundi Notes"). Pursuant to the Offering Circular issued in connection with the Barramundi Notes, Barramundi CDO I Ltd. appointed National Corporate Research Ltd., located at 225 West 34th Street, New York, New York 10122-0049, as its agent for service of process.

32. Defendant Gemstone CDO VII Ltd. is a Cayman Islands limited liability company located at c/o Deutsche Bank (Cayman), Limited, P.O. Box 1984, Grand Cayman KY1-1104. Gemstone CDO VII Ltd. is the issuer of the Gemstone VII Class A-2 Notes sold to Plaintiff LFJ 4 (the "Gemstone VII Notes"). Pursuant to the Offering Circular issued in connection with the Gemstone VII Notes, Gemstone CDO VII Ltd. appointed CT Corporation System, located at 111 8th Avenue, 13th Floor, New York, New York 10011-5252, as its agent for service of process.

33. Defendant Gemstone CDO VII Corp. is a Delaware corporation located at c/o Donald Puglisi, 850 Liberty Avenue, Suite 204, Newark, Delaware 19711. Gemstone CDO VII Corp. is the co-issuer of the Gemstone VII Notes sold to Plaintiff LFJ 4.

34. Defendant Pine Mountain CDO III Ltd. is a limited liability company located at P.O. Box 1984, Grand Cayman KY1-1104, Cayman Islands. Pine Mountain CDO III Ltd. is the issuer of the Pine Mountain III Class A-3 Notes sold to Plaintiff LFJ 31 and the Pine Mountain III Class A-3 Notes sold to LFJ 32 (collectively, the "Pine Mountain III Notes"). Pursuant to the Offering Circular issued in connection with the Pine Mountain III Notes, Pine Mountain CDO III Ltd. appointed as its agents for service of process Corporation Service Company, located at 1133 Avenue of the Americas, Suite 3100, New York, NY 10036, and CT Corporation System, located at 111 8th Avenue, 13th Floor, New York, New York 10011-5252.

35. Defendant Pine Mountain CDO III Corp. is a Delaware corporation located at 850 Liberty Avenue, Suite 204, Newark, Delaware 19711. Pine Mountain CDO III Corp. is the co-issuer of the Pine Mountain III Class A-3 Notes sold to Plaintiffs LFJ 31 and 32.

36. START 2005-C Ltd., START 2005-C Corp., START 2006-B Ltd., START 2006-B Corp., Barramundi CDO I Ltd., Gemstone VII CDO Ltd., Gemstone VII CDO Corp., Pine

Mountain CDO III Ltd., and Pine Mountain CDO III Corp. are collectively referred to herein as the "Issuers."

37. Defendant DBSI is a Delaware corporation located at 60 Wall Street, New York, New York 10005. DBSI is a registered broker-dealer, and was the arranger of all of the CDO transactions at issue in this Complaint and the direct seller to Plaintiffs of all of the Notes.

38. Defendant DB AG is a German corporation located in Frankfurt, Germany. DB AG is licensed to do business in New York and maintains a regional head office located at 60 Wall Street, New York, New York 10005. DB AG is the owner of its indirect subsidiary DBSI.

39. DB AG, through its London branch, was the initial counterparty to the CDS contracts issued by the CDOs at issue in this complaint. DB AG engaged in "back-to-back" CDS transactions with preferred clients through which it effectively passed through its short position on the CDS to those clients. DB AG sold these short positions to its customers either directly or through other, intermediary, banking institutions. In the former situation, DB AG "faced" its short customers directly; in the latter, it "faced" the intermediary bank, which in turn "faced" the client with DB AG's knowledge.

40. Defendant HBK Investments is a Delaware limited partnership with offices located at One Bryant Park, Suite 4000, New York, New York 10036. HBK Investments was the collateral manager for the Gemstone VII CDO.

41. Defendant HBK Partners is a Delaware limited partnership with offices located at 2101 Cedar Springs Road, Suite 700, Dallas, Texas 75201. HBK Partners is a general partner of HBK Investments and is responsible for its liabilities.

42. Defendant HBK Management is a Delaware limited liability company with offices located at 2101 Cedar Springs Road, Suite 700, Dallas, Texas 75201. HBK Management is a general partner of HBK Partners and is responsible for its liabilities.

JURISDICTION AND VENUE

43. This Court has jurisdiction over Defendants pursuant to CPLR §§ 301 and 302.

44. Deutsche Bank maintains offices, and regularly conducts business, in New York; Deutsche Bank orchestrated the fraudulent scheme at issue in and from New York; all Defendants transacted business within New York that gives rise to Plaintiffs' causes of action; Defendants committed the alleged wrongful acts alleged herein in New York; and all Defendants regularly transact business within New York and contract to provide services within New York.

45. Moreover, the relevant documents governing START 2005-C, START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III, each provide for an express submission to the jurisdiction of the courts located in the State of New York or Borough of Manhattan in the City of New York.

46. Venue in New York County is proper under CPLR § 503 because Deutsche Bank resides in this county. Venue in New York County is also proper under CPLR § 501 because the relevant documents governing START 2005-C, START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III each provide for venue in the courts located in the State of New York, County of New York. Additionally, venue is proper because Defendants committed many of the wrongful acts alleged herein in New York County.

47. This action is appropriately assigned to the Commercial Division of the Supreme Court of the State of New York, County of New York, pursuant to the Rules of the Commercial

Division of the Supreme Court, as set forth in § 202.70 of the Uniform Rules for New York State Trial Courts.

FACTUAL ALLEGATIONS

I. Background on Plaintiffs and Their Investment Advisor

A. Plaintiffs' Decision to Invest in CDOs

48. Plaintiffs are special purpose entities formed to invest in CDOs on a long-term, buy-and-hold basis.

49. A CDO is an investment vehicle that is typically issued by a special purpose entity, commonly referred to as the "issuer." Generally, the issuer is created by an arranging bank in order to acquire a portfolio of investment assets, which serve as collateral for an issuance of various classes, or "tranches," of debt securities that are marketed and sold to investors.[3]

50. The investors in the CDO, which include noteholders and equity investors, are paid from the proceeds generated by the collateral. Amounts are paid out to investors according to a defined priority (known as a "waterfall"). The most senior tranches of notes, which have the lowest risk of loss and highest credit rating, typically receive principal and interest first. Conversely, more junior tranches are typically paid only after the senior tranches, and thus have a higher risk of loss and lower credit ratings.

51. Banks that arrange CDOs typically perform multiple roles, including: (a) structuring and modeling the CDOs; (b) marketing and selling them to investors; (c) interfacing

[3] The assets in a CDO's portfolio can be comprised of cash assets (such as RMBS), synthetic assets, or both. Synthetic assets include CDS contracts, transactions resembling an insurance contract whereby a "protection buyer" pays a "protection seller" periodic "premiums" (similar to insurance premiums) in return for the protection seller's promise to pay the protection buyer should certain "credit events" occur, such as events of payment default, loss, write-down, or a deterioration in ratings. A CDO containing both cash and synthetic assets is referred to as a "hybrid" CDO.

with ratings agencies to achieve the targeted ratings for the CDOs' tranches; (d) financing and facilitating the purchases of the collateral and holding that collateral on their own books prior to closing; and (e) facilitating hybrid structures by acting as the initial protection buyer for CDS included in the collateral pool. Moreover, as the special purpose vehicle that serves as the deal's "issuer" does not have any employees of its own, the arranging banks usually act as the "initial purchasers," buying all of the notes from the issuer at closing and then selling them to investors. For performing these functions, arranging banks typically receive millions of dollars in fees at closing.

52. IKB Deutsche Industriebank AG, along with its affiliate IKB Credit Asset Management GmbH (collectively, "IKB"), was contractually appointed as investment advisor to Plaintiffs. Plaintiffs' investment advisor identified potential investments in CDOs and performed due diligence on behalf of Plaintiffs prior to making investment recommendations to them.

53. At all relevant times, Defendants knew that IKB served as investment advisor to Plaintiffs. Defendants also knew that in its capacity as investment advisor, IKB performed diligence on, and recommended CDO investments – including the investments at issue in this lawsuit – to Plaintiffs.

54. The Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs were marketed and sold to Plaintiffs as "managed" deals. That is, Deutsche Bank and the other Defendants represented to Plaintiffs that the collateral portfolios for these deals would be selected and managed by independent and experienced "collateral managers" for the benefit of Plaintiffs whose interests, as long investors, were aligned with those of the deals' success. Collateral managers (such as HBK, in the case of Gemstone VII) are paid a fee for these

services, typically a percentage of the notional value of the transaction (*i.e.*, the total deal issuance), the cost of which is ultimately paid for by the investors in the CDO.

55. The choice of collateral manager is material to an investor's decision to invest in a CDO because the collateral manager can greatly affect a CDO's risk profile and performance with its selection of collateral. The collateral manager has a duty to analyze and select the best quality and mix of eligible assets and monitor the credit status of the individual underlying assets, reinvest payment proceeds from maturing underlying assets, and make allowed substitutions in the collateral for the benefit of long investors and in the interests of the deals' success.

56. The performance of the collateral selected for the various tranches of a CDO is critical to the deal's success. As Defendants were aware, neither Plaintiffs nor their investment advisor had relationships with servicers or originators, or access to the underlying loan information, needed to conduct due diligence on a loan-by-loan basis. Therefore, the involvement of a qualified, independent collateral manager committed to identifying and selecting the highest quality and best mix of eligible collateral in the best interests of the CDO's long investors was a material factor in Plaintiffs' investment decisions and the recommendations of their investment advisor.

57. Plaintiffs' investment decisions also were based on the ratings assigned to proposed CDO investments and their underlying collateral as indicators of the risks associated with potential investments.[4] Plaintiffs' investments focused on highly-rated tranches (primarily

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[4] Ratings agencies typically assign credit ratings to the various tranches of a CDO (except for the most junior tranche, known as the "equity" tranche). For the purposes of this complaint, and unless stated otherwise, any reference to a particular rating refers to the Standard & Poor's ratings categories.

AAA and AA)[5] and, for managed deals, on CDOs managed by experienced and independent collateral managers who were committed to exercising independent judgment in purchasing and managing the collateral for the benefit of investors and the CDOs' success.

B. Plaintiffs' Reliance on Deutsche Bank

58. Deutsche Bank had a longstanding relationship with Plaintiffs' investment advisor. Deutsche Bank promoted itself to Plaintiffs' investment advisor as a leader in structured finance CDOs, listing its track record with billions of dollars in structured credit transactions that either had already closed or were in the pipeline.

59. Plaintiffs' investment advisor specifically reviewed Plaintiffs' investment strategy and guidelines with Deutsche Bank in detail during meetings, phone conversations and in various e-mails. Deutsche Bank was also intimately familiar with Plaintiffs' investment program, as well as IKB's role as investment advisor to the Plaintiffs, and Plaintiffs' investment criteria.

60. Between 2002 and 2007, Plaintiffs' investment advisor recommended for Plaintiffs, and other special purpose entities also advised by IKB, the purchase of 26 CDO investments that had been arranged by Deutsche Bank and its affiliates, totaling approximately $2.5 billion. Deutsche Bank and its affiliates were among the largest and most trusted arrangers of CDO investments for Plaintiffs.

61. Based on their deep and lengthy relationship with Plaintiffs' investment advisor and intimate knowledge of Plaintiffs' investment program and objectives, Deutsche Bank and its affiliates knew that over the course of 2006 and 2007, Plaintiffs became increasingly interested in highly-rated CDOs with the most secure structures.

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[5] According to Standard & Poor's, a rating of "AAA" signifies an "[e]xtremely strong capacity to meet financial commitments," and a rating of "AA" signifies a "[v]ery strong capacity to meet financial commitments."

62. Plaintiffs and their investment advisor reasonably relied on Deutsche Bank to present only those CDOs that met their stringent standards.

II. Deutsche Bank's Decision to Profit from the Collapse of the Subprime Housing Market on the Backs of Unsuspecting Long Investors, Like Plaintiffs

A. Deutsche Bank's Access to Specialized Information, Unavailable to Plaintiffs, Concerning Subprime Mortgages, RMBS, and CDOs

63. During the time-frame relevant to this complaint, Deutsche Bank played a major role in virtually every aspect of the subprime capital markets: as originator of subprime loans; as provider of warehouse financing to other loan originators; as sponsor, depositor, and trustee of subprime RMBS; as the arranging bank of CDOs containing or referencing subprime RMBS; and as the arranger, initial purchaser, and initial CDS counterparty of Deutsche Bank-engineered CDOs. Because of these multiple roles, Deutsche Bank gained a unique perspective and attained peculiar knowledge – unavailable to the investing public, including Plaintiffs and their investment advisor – concerning the true nature of the CDOs it was promoting.

64. Starting at the ground level, Deutsche Bank was directly involved with the origination of residential mortgages to subprime borrowers through two affiliates: DB Home Lending LLC (f/k/a Chapel Funding, LLC) and MortgageIT Inc. As stated in its press releases, Deutsche Bank acquired these entities in 2006 in order to expand its subprime residential loan origination business and thereby provide the company with "a steady source of product [*i.e.*, residential mortgages] for distribution into the mortgage capital markets."[6]

65. Deutsche Bank – through its subsidiaries DB Structured Products, Inc. ("DBSP") and ACE Securities Corp. ("ACE") – was also a major force in securitizing pools of subprime mortgages into RMBS. This was an extremely lucrative business for Deutsche Bank – it earned

[6] *See* Deutsche Bank press releases, July 12, 2006, available at http://www.deutsche-bank.de/medien/en/content/press_releases_2011_aug.htm.

up to $8 million in underwriting fees for each securitization – and one that it actively sought to develop during the periods relevant to this complaint. *See Wall Street and the Financial Crisis: Anatomy of a Financial Collapse*, Majority and Minority Staff Report, U.S. Senate Permanent Subcommittee on Investigations, April 13, 2011 ("Levin Report"), at 318. Indeed, as Deutsche Bank explained in press releases announcing its acquisitions of DB Home Lending and MortgageIT, the benefit of vertically integrating its origination and securitization platforms was that it would advance Deutsche Bank's position as a "leading RMBS player" by providing "significant competitive advantages, such as access to a steady source of product for our securitization program."[7]

66. Despite the "steady source of product" it obtained through its acquisition of DB Home Lending and MortgageIT, Deutsche Bank could not create subprime loans fast enough to satisfy the needs of its RMBS securitization business. To meet that demand, Deutsche Bank – through DBSP – resorted to purchasing loans from unaffiliated originators, including subprime lenders such as Fremont, Countrywide and New Century. Deutsche Bank encouraged and facilitated the efforts of such originators to generate ever greater numbers of subprime loans by providing billions of dollars of financial support through warehouse lines of credit which gave originators the necessary funds to lend to borrowers. Deutsche Bank – through its subsidiary DBSP – also instituted a correspondent lending program through which it agreed to purchase loans from small originators before the loans had even been made.

67. In the prospectus supplements accompanying the RMBS it sponsored, Deutsche Bank represented that it conducted a number of quality control procedures to ensure the quality of the underlying mortgages. Among other things, Deutsche Bank claimed to perform a full re-

[7] *See* Deutsche Bank press releases, Sept. 12, 2006 and July 12, 2006.

underwriting of a random sample of the loans it purchased from originators in order to confirm the existence and accuracy of legal documents, credit documentation, appraisal analysis, and the originators' underwriting decision. In reality, Deutsche Bank lacked the capacity to perform its own due diligence on the billions of dollars of loans it purchased for securitization (on information and belief, it had five or fewer staff members in its residential mortgage due diligence department), and thus relied heavily on Clayton Holdings, Inc. ("Clayton"), a third party mortgage consultant, to assess the adequacy of the underwriting of the pools of mortgages Deutsche Bank acquired.

68. Through the aggressive expansion of its mortgage origination business and its activities as warehouse funding provider to unaffiliated originators, Deutsche Bank succeeded in its stated goal of "becoming a top player in the US residential lending and securitization markets in short order."[8] Between 2004 and 2006, Deutsche Bank's RMBS securitizations tripled (reaching $24 billion). In 2006, this massive growth produced over €262 million in gains for Deutsche Bank.[9]

69. Further, Deutsche Bank – through its subsidiaries Deutsche Bank National Trust Company and Deutsche Bank Trust Company Americas – served as trustee for the RMBS securitized by DBSP and other, non-affiliated, RMBS sponsors. Among other things, an RMBS trustee's tasks include ensuring that all required documentation for the underlying mortgage loans is present and complete. During the time period relevant to this complaint, Deutsche Bank served as trustee for more U.S. asset-backed securitizations than any other bank, and was one of the largest – if not the largest – trustees of RMBS in the world.

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[8] *See* Deutsche Bank press release, July 12, 2006.

[9] *See* DB AG 2006 Annual Report, available at: http://annualreport.deutsche-bank.com/2006/ar/notes/notes3-14/9assetsecuritizations.html?dbiquery=4%3A19%2C735.

70. In addition to its role as a "leading RMBS player," Deutsche Bank also pursued a lucrative business arranging CDOs – earning between $5 million and $10 million per CDO – and placing CDOs in the secondary market. *See* Levin Report, at 318. Between 2004 and 2008, Deutsche Bank arranged a total of 47 CDOs for a total issuance of $32.2 billion. *See id.* at 335. In 2006 and 2007, Deutsche Bank ranked fourth globally in CDO issuances, arranging 15 new CDOs securitizing nearly $11.5 billion between December 2006 and December 2007. *See id.* at 333, 335.

71. Through the multiple roles it played from the ground up, as mortgage originator, warehouse lender, RMBS sponsor, trustee, and CDO arranger, as well as the detailed reports it received from Clayton, Deutsche Bank had peculiar knowledge about the quality and performance of the subprime loans that it and other banks were packaging into RMBS and, ultimately, the CDOs of RMBS that it was marketing to Plaintiffs and other potential investors, including the CDOs at issue in this complaint.

B. Deutsche Bank's Knowledge that the Subprime Market Was Poised to Collapse

72. In or about late 2005, Deutsche Bank became acutely aware that the foundation upon which its lucrative RMBS and CDO businesses depended was beginning to crumble.

73. As alleged above, Deutsche Bank relied heavily on Clayton to perform due diligence on the subprime loans it was acquiring for securitization to confirm whether these loans met the originators' – and Deutsche Bank's – underwriting guidelines. In testimony provided to the congressional Financial Crisis Inquiry Committee ("FCIC"), an executive who served as a vice president in Deutsche Bank's due diligence department explained that Clayton would review a sample of loans – generally around 30% of the total number – and then provide

Deutsche Bank with an evaluation of whether the sampled loans conformed to applicable underwriting standards.

74. Based on documents it produced to the FCIC as part of its investigation, between 2006 and 2007 – the period when Deutsche Bank arranged and marketed to Plaintiffs the investments at issue in this complaint – Clayton found that 35% of the mortgages it analyzed for Deutsche Bank failed to conform to underwriting standards, and recommended that Deutsche Bank put these loans back to their originators.

75. Remarkably, Deutsche Bank routinely overrode the recommendations of Clayton, the firm it had retained to perform the due diligence that Deutsche Bank lacked the staff to perform itself, and "waived" half of these non-conforming loans into the RMBS loan pools despite their unsuitability.[10]

76. Deutsche Bank should have exercised its contractual rights to put these non-conforming loans back to their originators. Moreover, after learning that such a large portion of the sample loans was non-conforming, Deutsche Bank, at a minimum, should have conducted further investigation to identify the additional non-conforming loans in the pools and removed those non-conforming loans from the pools as well.

77. Instead, Deutsche Bank acted only to maximize profits at investors' expense. Rather than expand the sample size of the loan pools it was purchasing in order to identify all non-conforming loans, or cease purchasing loans from problem originators altogether, Deutsche

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[10] Of the 23,183 loans that Clayton rejected, Deutsche Bank "waived" 11,610. *See* Clayton All-Trending Report, FCIC, Sept. 23, 2010, http://fcic-static.law.stanford.edu/cdn_media/fcic-testimony/2010-0923-Clayton-All-Trending-Report.pdf. Among the nine banks investigated by the FCIC, Deutsche Bank ranked among the worst of the worst – second out of nine – both in terms of the number of loans originally rejected by Clayton and the number of loans subsequently waived in by the sponsoring bank. *See* Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States, Jan 2011 (the "FCIC Final Report"), at 167.

Bank instead negotiated lower prices from the originators and pocketed the discount.[11] Deutsche Bank concealed from investors that a substantial proportion of the loans it was packing into RMBS, which it was in turn packing into CDOs, were non-conforming and that the bank had received a discount from the originators for this very flaw.

78. Equally important, Deutsche Bank knew as a result of these actions that the RMBS it was securitizing were deeply flawed, and that their underlying mortgages had a far greater likelihood of default than the ratings agencies could discern when analyzing the loan pools. Based on its inside information and communications with Clayton, originators, and other market participants, Deutsche Bank knew or at a minimum had a very strong reason to believe that its competitors were facing similar problems, and thus that the RMBS arranged by them were similarly flawed.

79. Because of its roles in originating and securitizing mortgages, Deutsche Bank also had more timely and more accurate information than investors (including Plaintiffs) about the performance of subprime mortgages and RMBS composed of those mortgages.

80. For example, as detailed by the U.S. Department of Justice, at the time Deutsche Bank acquired MortgageIT, Deutsche Bank was aware of serious lapses in MortgageIT's underwriting practices, including its chronic failure to verify basic information concerning its subprime borrowers, such as income and employment status, and to review early payment

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[11] *See* Testimony of Vicki Beal, Senior Vice President of Clayton Holdings, Inc., before the FCIC, Sept. 23, 2010 ("[O]ur clients use Clayton's due diligence to identify issues with loans, negotiate better prices on pools of loans they are considering for purchase, and negotiate expanded representations and warranties in purchase and sale agreements from sellers."); Jonathan R. Laing, *Banks Face Another Mortgage Crisis*, *Barron's*, Nov. 20, 2010 ("Apparently the Clayton data were merely employed by the securitizers to negotiate lower prices on the mortgages from the originators without passing any price discount or higher yield on to the investors.").

defaults in the subprime loans it originated.[12] According to the Department of Justice, these fundamental lapses in underwriting standards not only continued after Deutsche Bank acquired MortgageIT, they got worse.

81. Moreover, in July 2010, the Financial Industry Regulatory Authority ("FINRA") fined Deutsche Bank $7.5 million for misrepresenting the delinquency rates of mortgages that it securitized into RMBS during the 2006 – 2007 time period. *See FINRA Letter of Acceptance, Waiver and Consent No. 20080128087*, CRD No. 2525.

82. In contrast to a multi-faceted market participant such as Deutsche Bank, a mere investor could not have known the truth about these securities. In fact, neither Plaintiffs nor their investment advisor possessed or had access to any of the above-described information.

C. Deutsche Bank's Strategy to Protect Itself and Profit from the Impending Subprime Meltdown

83. Based on its insider's knowledge, by late 2005 Deutsche Bank knew that the subprime market had increasingly come to resemble a house of cards teetering on the verge of collapse. Yet Deutsche Bank was unwilling to forego the hefty fees it could earn securitizing RMBS and arranging CDOs backed by RMBS for sale to unsuspecting long investors. Deutsche Bank thus set out to find ways that it could continue to profit from its lucrative businesses while offloading its own exposure to the impending financial meltdown.

84. To reduce its own risk, Deutsche Bank began unloading deteriorating RMBS and CDO positions from its own books into CDOs that it was arranging, including the deals at issue in this complaint. To further limit its risk, Deutsche Bank allowed its top global CDO trader, Greg Lippmann, to take a massive short position against subprime RMBS and CDOs. By the end of 2005, Deutsche Bank had already purchased $1 billion worth of credit swap protection on

[12] *See U.S. v. Deutsche Bank AG and MortgageIT, Inc.*, No. 11-CIV-2976 (S.D.N.Y.).

these securities. This position increased dramatically during the course of 2006, and by the end of 2007 totaled $5 billion (and, by some publicly reported accounts, as much as $10 billion).

85. At the same time, Deutsche Bank continued to pursue its other profit centers by sponsoring and marketing RMBS and CDOs to long investors – but it withheld from those investors its insider's knowledge that the same investments it was touting were plagued by poor underwriting and infected with fraud. In fact, far from giving Deutsche Bank pause, this knowledge drove Deutsche Bank to pick up the pace. In the months immediately preceding and following the initial wave of ratings downgrades in July 2007, Deutsche Bank arranged 15 new CDOs – at the rate of more than one a month. *See* Levin Report, at 333.

86. Deutsche Bank also began an organized pitch to preferred clients that it believed might be interested in shorting the very same market it was promoting to investors like Plaintiffs. As discussed in more detail below, Deutsche Bank's top CDO trader actively encouraged its preferred clients to take short positions against the very same assets that comprised the collateral of the CDOs it was then marketing to Plaintiffs and other long investors. In fact, during pitches to a hedge fund known as FrontPoint Partners LLC, Deutsche Bank referred directly to Plaintiffs' investment advisor: when asked who would be taking the long side of the short transactions that Deutsche Bank was marketing, Greg Lippmann, Deutsche Bank's top CDO trader, responded, "Düsseldorf," where Plaintiffs' investment advisor, IKB, is headquartered. *See* Michael Lewis, *The Big Short*, at 65-67 (2010).

III. Deutsche Bank's Knowing Concealment of Material Facts Concerning "Pigs" and "Crap" Assets in the CDOs It Arranged and Marketed to Plaintiffs

87. Between July 2006 and July 2007, Deutsche Bank marketed four CDOs to Plaintiffs' investment advisor for potential investment by Plaintiffs – Carina, Barramundi, Gemstone VII, and Pine Mountain III. While the CDOs involved different collateral managers,

they shared one thing in common: their portfolios were stocked with RMBS that Deutsche Bank – and, in the case of Barramundi and Gemstone VII, the collateral managers – knew to contain a disproportionate share of non-conforming loans from problem mortgage originators. In other words – indeed, in the words of Deutsche Bank's Greg Lippmann – these deals were stocked with the very same "pigs" and "crap" securities that Deutsche Bank was simultaneously advising its favored clients to short.

88. The reason Deutsche Bank continued to market those deals to investors, like Plaintiffs, was to off-load risk that it knew was present in an increasingly dysfunctional market – a market which, in Lippmann's view, had become a "Ponzi scheme" (see Levin Report, at 330) – and to earn fees at its other clients' expense. In a candid e-mail to a preferred hedge fund client, Lippmann wrote:

> [T]he demand for this crap is virtually entirely technically driiven [sic], all cdos. And each person at the table thinks someone else is the fool – cdo equity, ostensibly only two buyers one mutual fund[] in australia, hard to call them smart money, and one hedge fund in chicago, [M]agnetar; who is actually putting on a bearish correlation trade; [CDO tranches rated] bbb sold mostly ponzi-like to other cdos with limited distribution in Europe and asia … again hard to call that smart money. Aa and Junior AAA sold mostly to high grade cdos and to a certain extent European and asian banks, and lastly the senior AAA, this may ultimately break the cdo market.
>
> …
>
> Why have we [Deutsche Bank] done this? It is not without reluctance we are looking for ways to get out of this risk, but for now the view has been, we like the fees and the league table credit (and dammit we have a budget to make)….

August 26, 2006 e-mail from Greg Lippmann (cited in the Levin Report, at 362, n. 1420).

A. <u>Gemstone VII</u>

1. Deutsche Bank's and HBK's Misrepresentations and Omissions with Respect to Gemstone VII

89. Beginning in January 2007, Defendants Deutsche Bank and HBK aggressively marketed Gemstone VII as an investment opportunity for the Plaintiffs. Synthetic assets comprised approximately 65% of the CDO's total $1.1 billion collateral pool.

90. The collateral manager of Gemstone VII was Defendant HBK. HBK had structured six previous CDOs with the "Gemstone" moniker, in addition to engaging in other activities in the subprime market, including underwriting RMBS and purchasing tranches of those subprime securities.

91. On or about January 18, 2007, Deutsche Bank and HBK first presented Plaintiffs' investment advisor with a draft of a Debt Investor Presentation (later superseded by a version dated February 8, 2007, which is hereinafter referred to as the "Gemstone Presentation") with the knowledge and expectation that it or the substance of its contents would be conveyed to Plaintiffs, which it was. The Gemstone Presentation stated that HBK carefully "source[d] high quality opportunities for the portfolio" and explained how HBK created its own RMBS portfolio by screening loans, purchasing them from originators, and packaging them into pools that were securitized in the form of RMBS; by purchasing new issue RMBS from others after extensive loan-level due diligence; and by purchasing existing RMBS on the secondary market. See Gemstone Presentation, at 29.

92. The Gemstone Presentation further represented that HBK's "investment process integrates expertise in capital markets, structural analysis, collateral and loan-level analysis, due diligence, and in-house surveillance. *HBK is seen as* [sic] *not as a trader, but as a vigilant*

investor that maximized value through intensive analysis and surveillance." *Id.* at 5 (emphasis added).

93. The Gemstone Presentation also represented that "HBK's investment model utilizes proprietary default, prepay, and severity loan level models to make investments in the residential market," that "HBK analyze[s] originators for underwriting consistency and monitor[s] changes to the competitive landscape," that HBK "conduct[s] due diligence of underlying loan collateral to formulate investment assumptions," and that HBK "develops loan level models, with delinquency and default forecasts, loss severity forecasts, and prepayment forecasts." *Id.* at 23, 29-30.

94. The Gemstone Presentation represented that HBK had a unique ability to identify and dispose of underperforming assets, claiming that it "is able to pick up on trends before they adversely impact the CDO" (*id.* at 41) and that it "aggressively pursue[s] exit strategies when investments significantly underperform, … especially in cases where fraud … may be a factor." *Id.* at 31. When necessary, the Gemstone Presentation asserted, HBK would force originators to repurchase substandard loans that should never have been included in the asset in the first place: "HBK works with dealers and originators to customize pools by kicking out problem loans." *Id.* at 41.

95. Representations such as these were intended to convey to investors the highest level of assurance in HBK, the quality of the assets that would be selected for Gemstone VII, and the care and diligence that HBK would exert to maintain that high quality for the benefit of long investors, including Plaintiffs.

96. After receiving the Gemstone Presentation, Plaintiffs' investment advisor, on behalf of Plaintiffs, conducted due diligence into the proposed investment, including into HBK

itself. This due diligence included meetings with HBK in Las Vegas, Nevada and in New York City in or about late January and early February 2007. Representatives of Plaintiffs' investment advisor also met with HBK in New York in September 2006, in connection with potential investment opportunities that predated Gemstone VII. In those meetings, HBK was represented by Kevin Jenks, who was later the senior collateral manager for Gemstone VII; Marco Lukesch, an analyst; and Rachel Wish, another HBK employee.

97. During those meetings, HBK reiterated the representations contained in the Gemstone Presentation. HBK repeated that it had a superior ability to conduct quantitative loan-by-loan analysis based on the most recent data. HBK, with the knowledge and expectation that those representations or the substance thereof would be conveyed to Plaintiffs, which they were, even showed Plaintiffs' investment advisor its loan surveillance database and monitoring system, including its proprietary software for modeling portfolio performance. The only reasonable inference that could have been drawn from these representations was that these systems would be used for the Gemstone VII portfolio to ensure superior performance, and that is precisely the inference HBK intended Plaintiffs and their investment advisor to make.

98. HBK also represented that its own investments in RMBS gave it particularly close relationships with important loan originators, enabling HBK to compel those originators to repurchase non-conforming loans. In fact, HBK represented that Gemstone VII had a high concentration of loans issued by certain originators because HBK was leveraging its relationships with those originators so that HBK could improve its monitoring and increase its pressure on them to repurchase non-conforming loans.

99. HBK further stated that its economic interests were aligned with those of noteholders both because it took equity interests in the CDOs and because it also had interests in

the underlying pools of RMBS. HBK acquired the equity in Gemstone VII at a substantial (nearly 50%) discount.

100. HBK received a high fee for managing Gemstone VII – 30 basis points which translated into $3.3 million per year based on the size of the deal. *See id.* at 9. In light of HBK's large fee, and based on the representations made as to HBK's abilities and experience, Plaintiffs' investment advisor reasonably expected HBK to employ particular diligence and expertise in selecting and managing the portfolio.

101. On or about February 14, 2007, and on several occasions thereafter, Deutsche Bank circulated drafts of an Offering Circular for Gemstone VII (culminating in a final version dated March 17, 2007, which is hereinafter referred to as the "Gemstone Circular") to potential investors, including Plaintiffs through its investment advisor. The Gemstone Circular had been prepared by Deutsche Bank and HBK and stated that HBK would "select, monitor, and provide the Issuer with certain information relating to the portfolio of Underlying Assets" – the cash and synthetic RMBS assets in Gemstone VII – pursuant to a collateral management agreement, and that all acquisitions or dispositions of the CDO's collateral would be conducted on an "arm's-length basis." Gemstone Circular, at 165, 166.

102. The collateral management agreement for Gemstone VII provided that HBK would select and manage the portfolio to maximize the likelihood that the noteholders would be repaid (*i.e.*, a "timely performance of all payment obligations of the Issuer under the Indenture") and, to the extent not inconsistent with that, to maximize HBK's own return as equity-holder. Those representations reinforced Deutsche Bank's and HBK's prior representations that HBK would engage in careful loan-by-loan analysis and market surveillance to protect the interests of the Gemstone VII noteholders.

2. In Reality, Deutsche Bank and HBK Stocked Gemstone VII with "Pigs" and "Crap" Assets as they Rushed to Close the CDO Before the Market "Falls Off a Cliff"

103. As alleged above, the marketing materials for Gemstone VII stated that HBK alone would be responsible for selecting the deal's collateral. In reality, however, a private engagement agreement and a risk sharing agreement with Deutsche Bank – neither of which was disclosed to investors – explicitly gave Deutsche Bank the right to approve or reject assets proposed by HBK for the CDO's portfolio. *See* Levin Report, at 353-54.

104. Specifically, in practice, once HBK had identified securities for inclusion in the Gemstone VII portfolio, it would send an e-mail to Deutsche Bank's head CDO trader, Greg Lippmann, requesting that Deutsche Bank place the identified securities into the CDO's warehouse account. Lippmann's group could either approve the assets or reject them. *See id.* Documents reviewed by the Senate Subcommittee indicate that on several occasions Lippmann and other traders from his desk voiced concerns over assets proposed by HBK. *See id.* at 354-55.

105. Significantly, in addition to heading the CDO Trading Desk, Lippmann was also the head of risk management for all CDOs arranged by Deutsche Bank. Between those two positions, Lippmann was "involved in underwriting, structuring, marketing and hedging [Deutsche Bank's] warehouse risk for new issue [CDOs]." *Id.* at 336-37.

106. Deutsche Bank's insider knowledge of the rapidly deteriorating state of the subprime RMBS market, coupled with the ability of Lippmann's group to accept or reject assets proposed by HBK, should have served as a backstop ensuring that Gemstone VII's portfolio consisted of quality collateral. Instead, while HBK was stocking the CDO with RMBS from problem originators, Deutsche Bank also seized the opportunity to dump over $27 million in assets that it wanted to unload from its own books into the CDO and onto its long investors, such as Plaintiffs.

107. As revealed in the Levin Report, nearly one-third of the cash and synthetic collateral selected for Gemstone VII involved subprime residential mortgages issued by three subprime lenders – Long Beach, Fremont, and New Century – that were known to insiders like Deutsche Bank (but not to outsiders such as Plaintiffs or their investment advisor) for issuing particularly risky loans and securities. *See id.* at 358.

108. Loans originated by New Century had suffered significant deterioration in quality during the preceding two years, as evidenced by dramatically increasing rates of early payment defaults and a large backlog of unresolved repurchase claims. New Century's situation was so dire, in fact, that it declared bankruptcy within two weeks of Gemstone VII's closing.

109. Similarly, during the ramp-up for Gemstone VII, HBK was involved in an ongoing dispute with Fremont over the substandard quality of Fremont's loans and was demanding that Fremont repurchase large numbers of loans – a fact that HBK never disclosed to Plaintiffs or their investment advisor. By March 2007, Fremont was forced to stop originating loans altogether, and eventually it also went bankrupt.

110. The problems with loans originated by Long Beach were even worse. Though it was one of the largest subprime lenders in the country, Long Beach employed no loan officers of its own; instead, Long Beach obtained all of its loans from third party mortgage brokers, and its "account executives" were compensated by the volume of loans they brought in with little regard to their quality. *See id.* at 75. Long Beach's subprime loans were among the worst performing in the industry, suffering from chronically high rates of fraud, delinquencies, and early payment defaults. *See id.* In March 2006, Washington Mutual acquired Long Beach; in July 2007, Washington Mutual decided to discontinue Long Beach as a separate entity, and within three months shut it down entirely. *See id.* at 80, 84-85.

111. Tellingly, at the same time the RMBS from these problem originators were being selected by HBK and submitted for the CDO Trading Desk's approval for inclusion in Gemstone VII, Deutsche Bank was internally disparaging many of these same assets and advising its preferred clients to take short positions on them.

112. For example, on October 20, 2006, one of Deutsche Bank's clients sought Lippmann's advice about certain subprime bonds issued by Long Beach Mortgage Loan and Trust ("LBMLT"). Lippmann's candid response left no doubt about his insiders' knowledge of Long Beach's problems:

> LBMLT-06-5 M9-375. Long beach is one of the ***weakest names on the market.*** We shorted this bond to a CDO … on Oct. 13[.] Deal was done before S&P changed their [rating] criteria on July 1. Lots of 40 year mortgages…. ***Less than half the loans have full documentation*** and 10% are investor properties. ***This is a real pig***.

Id. at 359, n. 1397 (emphasis added). Yet this peculiar knowledge was not disclosed to Gemstone VII investors. To the contrary, with Deutsche Bank's knowledge and approval, Gemstone VII acquired $25 million of this very same bond, of which $20 million was purchased on October 24, 2006, just four days after Lippmann's e-mail. By closing, a total of $79.5 million in "pig" bonds from "one of the weakest names in the market" ultimately made their way into Gemstone VII.

113. Internally, Deutsche Bank had similar knowledge of RMBS containing subprime loans originated by Fremont, yet with Deutsche Bank's knowledge and approval these toxic RMBS were purchased for the Gemstone VII collateral pool. On November 29, 2006, Lippmann described an RMBS containing Fremont loans known as SABR 2005-FR4 B3 to a Deutsche Bank colleague as a ***"pig,"*** and two days later he advised a client that the security was ***"blowing up."*** *See id.* at 359-60 (emphasis added). Five days later, Gemstone VII acquired $20 million of

this security. *See id.* at 359. Similarly, Gemstone VII acquired $1 million in another RMBS containing Fremont loans despite Deutsche Bank's knowledge that this security, too, was a ***"pig."*** *See id.* at 360 (emphasis added). Again, Deutsche Bank concealed and did not disclose these facts to Plaintiffs.

114. Securities containing loans originated by New Century were likewise included in Gemstone VII despite Deutsche Bank's peculiar knowledge of New Century's problems. On November 28, 2007, Lippmann noted that an RMBS containing New Century loans known as MABS 2005-NC2 M9 would soon experience a ***"huge payment shock,"*** yet on January 17, 2007, Gemstone VII acquired $10 million of this security, with Deutsche Bank's knowledge and approval. *Id.* (emphasis added). On December 8, 2006, Lippmann characterized another RMBS containing New Century loans, GSAMP 06-NC2 M8, as "an absolute pig," yet between November 13 and December 21 Gemstone VII acquired $30 million in securities from a *lower tranche* with *less subordination* from the same securitization. *See id.* (emphasis added). Deutsche Bank did not disclose these facts to long investors, including LFJ 4, either.

115. Deutsche Bank had similar knowledge of New Century loans securitized by its subsidiary, ACE. On September 21, 2006, when asked by a colleague for his opinion about an RMBS known as ACE 2006-NC1 M9, Lippmann responded that ACE was "***generally horrible.***" *Id.* (emphasis added). And on March 2, 2007, just weeks before Gemstone VII closed, a client sent an e-mail to Lippmann stating "[Y]ou were right – ***ACE is crap***," to which Lippmann replied "***INDEED – IT IS.***" *Id.* at 361 (emphasis added, capitalization in original). Despite this assessment, Gemstone VII went on to purchase $10 million of ACE 2006-NC1 M9. *See id.* Once more, Deutsche Bank did not disclose this to long investors, including LFJ 4.

116. Deutsche Bank's internal knowledge of the collateral acquired by Gemstone VII was not limited to RMBS containing loans from these three problem originators. As recounted in the Levin Report, Gemstone purchased another $82 million of other RMBS that Lippmann described as "***piece[s] of crap***." *See id.* (emphasis added).

117. HBK also was aware of problems with these and other subprime mortgage originators, yet did not share this peculiar knowledge with investors in Gemstone VII. In fact, at the time Deutsche Bank and HBK were touting the collateral manager's ability to put back non-conforming loans, HBK was embroiled in ongoing, but undisclosed, disputes with at least five subprime mortgage originators, including Fremont, concerning the originators' obligations under the loan purchase agreements to repurchase loans in default.

118. Even more shockingly, Deutsche Bank and HBK caused Gemstone VII to purchase five RMBS totaling $27 million directly from Deutsche Bank's inventory despite Deutsche Bank's knowledge of the problems with these securities. The result was to shift the risk of those assets from Deutsche Bank's balance sheet to the noteholders of Gemstone VII.

119. For example, in an instant message conversation in December 2006 concerning ACE 2006-HE1 M10, an RMBS in which over 75% of the loans had been originated by Fremont, Lippmann wrote to one of the traders on his desk "***DOESNT [sic] THIS DEAL BLOW***," to which the trader replied "***yes it blows I am seeing 20-40% writedowns***." *Id.* (emphasis added). Nonetheless, that same month HBK purchased $10 million of this asset for Gemstone VII directly from Deutsche Bank through one of Lippmann's traders. *See id.* The net result was the transfer from Deutsche Bank to Gemstone VII's investors of an asset which Deutsche Bank knew to be underperforming and at substantial risk of imminent failure.

120. Similarly, on December 12, 2006, Gemstone VII acquired $5.5 million of an RMBS known as SABR 2005-OP1 directly from Deutsche Bank's inventory. Yet less than four months earlier, Deutsche Bank had advised a preferred short client that numerous securities, including SABR 2005-OP1, were incurring ***"serious delinquencies"*** and were ***"blowing up"*** as a result. *Id.* at 362 (emphasis added).

121. Other examples revealed in the Levin Report confirm that Deutsche Bank transferred millions of dollars more of "crap" assets from its inventory to Gemstone VII, all without any disclosure to Plaintiffs.

122. HBK also transferred subprime RMBS assets that it wanted to unload from its own balance sheet to Gemstone VII. HBK sold these assets to Gemstone VII for hundreds of millions of dollars not because it believed they represented good value for the CDO and its investors, but rather because HBK, like Deutsche Bank, was aware that the subprime loans underlying these RMBS were experiencing defaults and delinquencies at a rapidly escalating rate and it wanted to offload the associated risks from its own books to the CDO and its investors.

123. Obviously, this information – including that Deutsche Bank was actually recommending that certain preferred clients bet *against* these same securities through short positions – was material and would have been of substantial importance to potential investors in Gemstone VII, including Plaintiffs. Yet none of this information was ever disclosed to the CDO's investors. In other words, Deutsche Bank thought this information was important enough to convey to its preferred short clients, but not to the long investors – including the "stupid Germans" (in Lippmann's expression) – that it was trying to induce to invest in the CDOs it was arranging. In fact, it was imperative to Deutsche Bank and HBK that long investors *not* know the truth about the subprime RMBS assets that they were placing in Gemstone VII.

124. As revealed in the Levin Report, in December 2006 Deutsche Bank's CDO Group prepared a credit report for the credit risk management group to obtain internal approval for securitization of Gemstone VII. In that report, the CDO Group disclosed a concern that the bank would be unable to unload $400 million of Gemstone VII's securities due to a "significant vintage risk" arising from the CDO's heavy concentration of 2005 (67.6%), 2006 (20.2%), and 2007 (1.9%) vintage assets. *Id.* at 357. The marketing materials provided to potential investors in Gemstone VII concealed and failed to disclose this and other risks Deutsche Bank had identified in its internal credit report. *See id.*

125. Deutsche Bank's concern proved to be well founded. Correspondence between Deutsche Bank and HBK in early 2007 shows that both firms were deeply focused on offloading their own exposure to Gemstone VII on unsuspecting investors as quickly as possible.

126. On January 9, 2007, Kevin Jenks, a collateral manager at HBK, sent an e-mail to Michael Lamont, the head of Deutsche Bank's CDO Group, urging Deutsche Bank to close the CDO as quickly as possible: "[W]ith this market this way and probably going to get worse we would like to really move on the cdo. Please allocate the resources to expedite this." *Id.* at 365.

127. A month later, on February 7, 2007, Lamont told the CDO Group trader tasked with structuring Gemstone VII: "***we need to sell [Gemstone VII] now while we still can***." *Id.* at 366 (emphasis added). That same day, Lamont wrote to HBK's Jenks: "Keep your fingers crossed but ***I think we will price this just before the market falls off a cliff.***" *Id.* (emphasis added).

128. Some potential investors in Gemstone VII also inquired about the "mark to market" (or "MTM") value of the assets in the CDO's warehouse – *i.e.*, the value at which the assets could be currently sold in the marketplace as of the day they were marked. The

significance of MTM values is that it allows potential investors to determine if the CDO's underlying assets have lost value since they were purchased by the warehouse. During the marketing phase for Gemstone VII, both Deutsche Bank and HBK prepared MTM valuations of the CDO's portfolio. Deutsche Bank's marks generally showed an even greater deterioration in value than did HBK's marks. *See id.* at 368.

129. Upon learning that HBK's marks were more favorable than Deutsche Bank's, Deutsche Bank instructed its traders to provide HBK's marks to potential investors inquiring about the MTM value of Gemstone VII's portfolio. *See id.* For example, on January 24, 2007, Deutsche Bank's syndicate group was instructed to provide HBK's marks – which showed a $9.4 million loss – rather than Deutsche Bank's marks, which showed a $19 million loss. *See id.* HBK also wanted to show higher marks (*i.e.*, smaller losses) to potential investors. On February 27, 2007, HBK's collateral manager, Jenks, instructed an assistant HBK trader to provide investors with whichever of HBK's marks for the previous two months that were more favorable: "use dec[ember] or jan[uary] depending on which is better." *Id.* at 369.

130. In the end, despite the foregoing misrepresentations and omissions, Deutsche Bank and HBK ultimately were unable to place $400 million (or 36%) of the Gemstone VII's securities and were forced to keep those assets on their books.

3. Deutsche Bank and HBK Caused Gemstone VII to Pay Above-Market Rates for Cash Collateral and to Accept Below-Market CDS Premiums on its Synthetic Collateral

131. The $27 million that the Gemstone VII CDO paid for assets purchased directly from Deutsche Bank's inventory did not reflect fair market value because their poor quality was not generally known to market participants. Likewise, the prices at which HBK sold assets from its own books to Gemstone VII were inflated and did not reflect fair market value. In other words, at a time when both Deutsche Bank and HBK knew internally that the subprime market

was about to "fall[] off a cliff," they caused the Gemstone VII CDO to pay more for these assets than they would have obtained – had the truth about these "pigs" and "crap" been disclosed – in an open market *bona fide* trade. As such, Deutsche Bank's and HBK's representation that the CDO's collateral would be acquired on fair, arm's-length terms was also fraudulent.

132. Not only did they knowingly sell problem assets from their own balance sheets to the CDO at above-market prices, Deutsche Bank and HBK also knowingly caused Gemstone VII to pay above-market prices for its cash collateral at closing. The market value of Gemstone VII's portfolio of cash assets had decreased substantially in value between the time they were put into the warehouse and closing.

133. Indeed, between January 2007 and March 2007, assets of the type, vintage, and ratings that HBK and Deutsche Bank had purchased for the Gemstone VII portfolio experienced a decline in market value of 15% to 20%. Although they knew or should have known that asset values had drastically fallen during the first quarter of 2007, Deutsche Bank and HBK nevertheless caused Gemstone VII to purchase those assets at closing, not at their lower then-current market values, but instead at the higher prices based on the putative market value of those assets months earlier when they had been placed into the CDO's warehouse facility.

134. Further, Deutsche Bank caused Gemstone VII to sell credit protection via the CDS at below-market rates. In February 2007 – one month after Deutsche Bank and HBK began marketing Gemstone VII to investors and one month before it closed – the ABX index fell from a high of $0.90 early in the month to $0.69 by the end of the month, indicating a drop of more than 23% in the value of subprime RMBS securities and a corresponding increase in risk during this period. *See id.* at 365-66. Nonetheless, the premiums at which Gemstone VII sold protection to short investors failed to reflect this changed risk.

135. Thus, the Gemstone VII CDO paid higher prices for its cash collateral and received lower premiums for CDS referencing its synthetic collateral than it would have in open-market *bona fide* trades. Because Gemstone VII did not receive fair consideration in these conveyances, the CDO was rendered insolvent as it lacked sufficient assets to meet its obligations to investors. Additionally, the conveyances left the CDO with insufficient capital to carry on business and to meet obligations as they arose.

4. **Plaintiff LFJ 4's Detrimental Reliance on Defendants' Misrepresentations and Omissions**

136. On March 19, 2007, in reasonable and justifiable reliance on the foregoing false and misleading representations and omissions, LFJ 4 purchased $87 million from Deutsche Bank and is currently the owner of $20 million of Gemstone VII Class A-2 Notes, which were rated AAA at the time.

137. Gemstone VII CDO defaulted on April 14, 2008. The Gemstone VII Notes Class A-2 Notes owned by LFJ 4 were downgraded to CC and are now worthless.

138. Deutsche Bank and HBK improperly benefited from the sale of the Gemstone VII Notes to LFJ 4, including by fraudulently obtaining $20 million from LFJ 4, the $7.5 million in fees Deutsche Bank earned, and the $3.3 million in fees HBK earned in connection with their fraudulent sale of the CDO.

B. **Carina**

1. **Magnetar's "Constellation CDO" Scheme**

139. Around the same time that Deutsche Bank was seeking to protect itself and profit from the impending subprime meltdown, Magnetar, a hedge fund, was busy pursuing its own strategy: secretly using synthetic and hybrid CDOs to place massive short bets against the subprime RMBS market.

140. In collusion with various arranging banks and collateral managers, Magnetar orchestrated a series of CDOs – known as the "Constellation" CDOs because they bear the names of astral entities – as vehicles to carry out a "devious" (in the words of Deutsche Bank's Greg Lippmann[13]) short-trading strategy. In exchange for Magnetar's agreement to purchase the equity tranches of these CDOs,[14] the arranging banks allowed Magnetar to clandestinely influence the criterion that would be used to select the deals' portfolio of assets.[15] The Carina CDO was one of these fraudulent investment vehicles.

141. Unknown to long investors – but known to the arranging banks – the parameters Magnetar established for the deals were designed for Magnetar's specific risk tolerances and trading strategy. Publicly, Magnetar would take a long position via the Constellation CDOs' equity; behind the scenes, however, Magnetar would take an even larger short position, via CDS contracts, against the CDOs. To maximize the likelihood that this short-trading strategy would pay off, Magnetar dictated a mix of assets for the Constellation CDOs that was likely to generate several large cash distributions to its equity holding (i.e., the long position) before defaulting and entitling Magnetar to claim massive credit protection payments under the CDS contracts it secretly purchased on the Constellation CDOs' synthetic collateral (i.e., the short position). Moreover, in deference to Magnetar, arranging banks caused the Constellation CDOs to sell both

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[13] *See* Levin Report, at 373.

[14] The equity tranche of a CDO is subordinated (or "junior") to all other tranches. If the CDO's assets do not generate sufficient returns to pay all noteholders, the available funds are distributed in order of seniority. Thus, the equity tranche of a CDO traditionally bears the most risk, since it is usually the first tranche that will experience losses if the CDO's assets do not perform as expected. For this reason, CDOs' equity tranches are generally the hardest to place. If a purchaser for the equity tranche cannot be found, then the deal's arranger must either purchase the equity itself (and bear the attendant risk) or cancel the deal (and lose tens of millions of dollars in arranging and warehousing fees).

[15] *See* FCIC Final Report, at 192; Levin Report, at 372-73.

the equity and the CDS contracts to Magnetar at a discount. The net result was that, unlike purely long investors such as Plaintiffs, Magnetar's trade would yield huge profits if the deals collapsed. No economically rational long investor, such as Plaintiffs, would have invested in Carina had Defendants disclosed that the CDO was structured by an investor who was betting against it.

142. As recounted by the FCIC and in the Levin Report, as well as a number of recent lawsuits and other public reports, Magnetar's influence over collateral selection took various forms, depending on the deal. In some cases, Magnetar provided lists of pre-approved assets for the collateral manager to choose from. In others, Magnetar was granted a "veto" right over any asset selected for the CDO.[16] In others still, Magnetar simply exercised trades in the name of the collateral manager.[17] In all cases, however, Magnetar's agreement to act as equity sponsor in these deals was contingent on the constitution of portfolios that would advance Magnetar's undisclosed short-trading strategy.

143. In addition to allowing Magnetar to dictate asset selection, arranging banks also deferred to Magnetar's demand that the Constellation CDOs contain structural features designed to facilitate – and fund – Magnetar's undisclosed short positions. Whereas CDOs traditionally contained tests for overcollateralization coverage and interest coverage (known as the "OC test" and "IC test," their purpose is to protect senior tranches at times when the CDO's collateral does not generate sufficient cash flow to meet those tests by suspending payments to junior and equity tranches), the banks that arranged the Constellation CDOs structured those deals – at Magnetar's

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[16] *See In re Application of IKB Industriebank AG for an Order to Conduct Discovery for Use in a Foreign Proceeding Pursuant to 28 U.S.C. § 1782*, Civ. No. 1:11-0237 (N.D.N.Y.), Ex. H. Indeed, documents produced in other litigation show that Magnetar insisted that its veto right be recorded "behind the scenes and outside of the docs." *Id.*, Ex. I.

[17] *See* FCIC Final Report, at 192.

behest – to suspend or delay the implementation of these tests. The concealed purpose of this "triggerless" deal feature was to ensure that Magnetar would continue to receive cash payments on its equity investment which it could use to fund its larger short positions – via CDS contracts – on the Constellation CDOs' synthetic collateral.

144. In short, the Constellation CDOs were constructed for the benefit of a specific investor (Magnetar) with a specific trading strategy at the expense of all other investors. When the CDOs collapsed, as they were designed to do, the hundreds of millions of dollars invested by senior noteholders would be used to pay out Magnetar's short bet against the CDOs it had created.

145. Deutsche Bank had been closely involved with Magnetar's strategy, knew exactly how it worked, and even profited directly from the strategy. Indeed from the outset, Deutsche Bank collaborated with Magnetar on Orion 2006-1, Ltd. (the "Orion CDO"), the first of the Constellation CDOs,[18] where it was the equity co-sponsor alongside Magnetar. Later, Deutsche Bank similarly collaborated with Magnetar to serve as co-equity sponsor on at least two other Constellation CDOs, known as Pyxis ABS CDO 2006-1 ("Pyxis") and Orion 2006-2 ("Orion-2").

146. In fact, the ties between Deutsche Bank and Magnetar were so close that two senior Deutsche Bank employees that were responsible for the Orion-1, Pyxis, and Orion-2 deals, Kurt Palmer and Michael Henriques, left Deutsche Bank to join Magnetar and work on its Constellation CDO program. As stated in a revealing e-mail sent by Henriques himself on November 4, 2006, while still working for Deutsche Bank on the Orion-2 deal, "[t]hese deals are not CDOs, [] they are structured separate accounts." In other words, Deutsche Bank knew that

[18] *See* Levin Report, at 373.

the Constellation CDOs that Magnetar was orchestrating were not true CDOs at all, but were instead deals tailored to suit Magnetar's specifications, for its own benefit, in furtherance of its undisclosed strategy to profit from their collapse.

2. Magnetar's Undisclosed Influence over Deal Features and Asset Selection Criteria

147. In an effort to market the Carina CDO to Plaintiffs, Deutsche Bank promoted itself and the deal's collateral manager, non-party State Street Global Advisors ("State Street"), as leaders in structured finance CDOs, touting their track record with billions of dollars in structured credit transactions.

148. During August and September of 2006, Deutsche Bank provided Plaintiffs' investment advisor with multiple drafts of a term sheet that it had prepared for the Carina CDO with the knowledge and expectation that they or the substance of their contents would be conveyed to Plaintiffs, which they were. In these term sheets, Deutsche Bank touted State Street's qualifications and represented that State Street alone would select the collateral for Carina's portfolio. Deutsche Bank repeated these representations in the offering circular it prepared and provided to Plaintiffs' investment advisor on or about September 22, 2006, with the knowledge and expectation that it or the substance of its contents would be conveyed to Plaintiffs, which it was. The purpose of these representations was to induce Plaintiffs and their investment advisor to believe that Carina's collateral would be chosen by an independent manager who would act in the best interests of long investors and the CDO's success.

149. Further, Deutsche Bank specifically represented to Plaintiffs' investment advisor, with the knowledge and expectation that its statement or the substance of its statement would be conveyed to Plaintiffs, which it was, that it would not sell assets to its clients that would "blow up completely."

150. These representations – which were intended to and did in fact lead Plaintiffs and their investment advisor to believe that the Carina portfolio was being managed for the benefit of long investors – were materially false and misleading. In collusion with and at the behest of Magnetar, Deutsche Bank allowed Magnetar to effectively dictate which assets would be included in the Carina portfolio by determining the deal's asset selection criteria. While this information was in itself material, given Deutsche Bank's representation that State Street alone would independently select Carina's collateral, the failure to disclose Magnetar's influence over collateral selection was particularly egregious because Magnetar's interests were fundamentally misaligned with those of Carina's other long investors. As Deutsche Bank well knew, the Carina CDO – like the other Constellation CDOs – was designed by Magnetar as a vehicle for implementing its secret short-trading scheme. When Magnetar's undisclosed short bet against Carina via the CDS contracts paid off, the deal's long investors – including LFJ 3, LFJ 12, and LFJ 26 – would be the ones footing the bill.

151. Magnetar's investment strategy and risk tolerance were materially different than those of Plaintiffs and other long-only investors. Magnetar claimed no expertise in assessing the investment merits of RMBS. Rather it believed it could create an arbitrage profit by buying the CDO equity tranches at a discount and by buying CDS contracts for a fraction of their nominal value and thereby massively shorting the more expensive senior CDO tranches. Thus, while Magnetar stood to reap huge profits if the CDO cratered, Plaintiffs and other long investors could only profit if the CDO performed well. Plaintiffs invested based on representations that the CDO's collateral manager was acting as an independent expert, which would select the CDO investments based on their quality to protect long investors' economic interests. In practice, the arranging bank ceded control of the portfolio selection process to Magnetar, because Magnetar

told Deutsche Bank that it would not buy the CDO's hard-to-sell equity (in which case there would be no CDO at all) unless the collateral portfolio met its investment criteria – which was directly contrary to what Defendants represented to Plaintiffs. Further, arranging banks allowed Magnetar, the same party that was shorting the deals, to designate the CDOs' portfolio parameters – in some cases, even allowing Magnetar to designate specific assets for inclusion in those CDOs' portfolios or to veto unwanted assets – and structured the deals in a way that would allow Magnetar to fund its short bets via distributions from its equity investment.

152. Deutsche Bank clearly knew at many levels precisely how this scheme worked. Indeed, apart from its direct participation in several Magnetar deals as co-equity sponsor, in e-mails from August 23, 2006, that were released publicly by the United States Senate, Deutsche Bank's Greg Lippmann, specifically described Magnetar's scheme to a client, and even referred to it as "devious."

153. As alleged above, Deutsche Bank's role at virtually every level of the subprime market gave it access to detailed information, unavailable to the public, about the deterioration of the RMBS and CDOs of RMBS, which constituted the collateral of the Carina CDO. Thus, Deutsche Bank independently knew that the asset selection criterion dictated by Magnetar resulted in RMBS containing significant portions of non-conforming loans being included in Carina's portfolio. For example, the Carina portfolio included (and in the case of synthetic assets, referenced) a number of RMBS that were securitized by Deutsche Bank (via its subsidiaries DBSP and ACE), including ACE 2005-HE6, ACE 2006-FM1, ACE 2006-HE1, ACE 2006-HE2, ACE 2006-HE3, ACE 2006-NC2, and ACE 2006-OP1. As detailed in a

complaint recently filed by the Federal Housing Finance Agency (the "FHFA"[19]) in the Southern District of New York, these and other RMBS securitized by ACE and DBSP contained high percentages of subprime mortgages with loan-to-value ratios exceeding 100% as well as disproportionate numbers of loans that were not secured by owner-occupied residences, but Deutsche Bank concealed these red flags from investors and ratings agencies by under-reporting these crucial loan statistics in the RMBS prospectuses.[20]

154. Moreover, the deal parameters dictated by Magnetar ensured that the Carina CDO would invest in tranches of other Constellation CDOs. Specifically, Carina included a cash investment of approximately $140 million in two other Constellation CDOs – Vertical Virgo 2006-1 and Cetus ABS CDO 2006-2 – that were similarly tainted by Magnetar's undisclosed influence over collateral selection and critical deal features in furtherance of its strategy to profit from the CDOs' failure.[21] Although Deutsche Bank was aware of these facts, neither Plaintiffs nor their investment advisor knew or could have known, at the time they invested in Carina, that the cash purchases of Constellation CDO securities were made at Magnetar's behest in collusion with Deutsche Bank.

[19] The FHFA is a federal agency that was created pursuant to the Housing and Economic Recovery Act of 2008 ("HERA") to oversee the Federal National Mortgage Association ("Fannie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac"), and the Federal Home Loan Banks. On September 6, 2008, FHFA was appointed conservator of Fannie Mae and Freddie Mac and in that capacity is authorized under HERA to bring suits on behalf of those entities. *See* 12 U.S.C. § 4617(b)(2).

[20] *See Federal Housing Finance Agency v. Deutsche Bank AG et al.*, 11-CV-6192 (S.D.N.Y).

[21] The undisclosed purpose of such cross-investments among Constellation CDOs was to link them so that the failure of one Constellation CDO would provoke the failure of others that invested in it, all to the benefit of Magnetar which had taken short bets against all of them.

155. Deutsche Bank knew that a substantial portion of the assets put into Carina's portfolio were the same "pigs" and "crap" that Defendant HBK had selected for Gemstone VII, but concealed and did not disclose these material facts to long investors, including Plaintiffs.

156. Further, Deutsche Bank acceded to Magnetar's demand that Carina – like the other Constellation CDOs – be structured so as to ensure that Magnetar could finance its short position (via CDS contracts issued by Carina referencing its synthetic assets) with distributions from its investment in Carina's equity tranche. As alleged above, Deutsche Bank structured Carina to delay the implementation of the OC and IC tests for the first five years of the CDO's life to ensure that Magnetar would continue to receive cash from its equity position with which it could fund premiums on its CDS contracts while waiting for the subprime market to collapse and its short positions to pay off.

157. In short, Deutsche Bank's representations to Plaintiffs and their investment advisor that Carina was a sound investment opportunity for long investors were false and misleading. In reality, the CDO which Deutsche Bank constructed – using a blueprint provided by Magnetar – was not designed to benefit long investors, but was instead designed to benefit Magnetar's undisclosed short bet against Carina's synthetic portfolio and to fund that bet with cash flows diverted from senior tranches to Magnetar's equity holding.

158. On or about November 1, 2006, in reasonable and justifiable reliance on Deutsche Bank's false and misleading representations and material omissions, LFJ 3, LFJ 12, and LFJ 26 (the "Carina Plaintiffs") purchased from Deutsche Bank a total of $100 million of notes in the Carina CDO as follows: (a) LFJ 3 purchased from Deutsche Bank $35 million of Class B-2 Notes, which at the time were rated AA-; (b) LFJ 12 purchased from Deutsche Bank $30.5 million of Class C-1 Notes, which at the time were rated A; (c) LFJ 12 purchased from Deutsche

Bank $19.5 million of Class C-2 Notes, which at the time were rated A-; and (d) LFJ 26 purchased from Deutsche Bank $15 million of Class B-1 Notes, which at the time were rated AA.

159. As Deutsche Bank and Magnetar anticipated, the Carina CDO experienced events of default long before its approximately four-year reinvestment period expired. Specifically, on or around October 26, 2007, less than a year after the Carina Plaintiffs' investments, Carina experienced an event of default as to the Class B-1, Class B-2, Class C-1, and Class C-2 notes. On or about November 1, 2007, S&P downgraded all of these notes to junk status. The rapid ratings decline for all four of those classes of notes continued, and in or about May 2009 both Moody's and S&P withdrew their ratings altogether. At present, the notes purchased from Deutsche Bank by the Carina Plaintiffs, which they still own, are virtually worthless.

160. Deutsche Bank improperly benefitted from the sale of the Carina Notes by fraudulently obtaining $100 million from the Carina Plaintiffs, as well as $10.5 million in fees.

3. Deutsche Bank Caused the Carina CDO to Accept Below-Market CDS Premiums for its Synthetic Assets

161. As alleged above, unknown to Plaintiffs, Deutsche Bank colluded with Magnetar to stock Carina with the riskiest, default-prone collateral.

162. Moreover, Deutsche Bank caused the Carina CDO to sell credit protection to Magnetar (either directly or indirectly through back-to-back hedging transactions with intermediary banks) via CDS contracts at prices that did not accurately reflect the true risk of Carina's synthetic collateral. By concealing Magnetar's shorting scheme and its involvement in adversely selecting assets for Carina, Deutsche Bank ensured that the CDS premiums Carina received were artificially low. Indeed, had this material information been publicly disclosed, the

value of credit protection on the Carina reference assets – and thus the premiums on the Carina CDS contracts in open-market *bona fide* trades – would have been substantially higher.

163. Because Carina did not receive fair consideration in these conveyances, the CDO was rendered insolvent as it lacked sufficient assets to meet its obligations to investors. Additionally, the conveyances left the CDO with insufficient capital to carry on business and to meet obligations as they arose.

C. Barramundi

164. Barramundi CDO I Ltd. was a hybrid CDO arranged by Deutsche Bank and managed by non-party C-BASS Investment Management LLC ("C-BASS").[22] Approximately 80% of the assets were synthetic.

165. C-BASS was a vertically integrated participant in the mortgage market, meaning that it performed several roles in the process of originating, servicing, securitizing, and repackaging mortgages. It was the sole owner of Litton Loan Servicing LP, a mortgage servicing company. C-BASS was also a significant arranger of RMBS assets and was itself owned by two mortgage insurance companies, thus lending an additional aura of apparent expertise and sophistication to C-BASS.

166. In marketing Barramundi, Deutsche Bank and C-BASS touted the collateral manager's vertically integrated approach as a mortgage servicer, underwriter of RMBS, and manager of CDOs. Almost all (93%) of the underlying RMBS referenced in the Barramundi portfolio were serviced by C-Bass's subsidiary and servicing arm, Litton. And Deutsche Bank and C-BASS specifically marketed the ability of Litton, a so-called "best in class servicer," to closely monitor and manage the underlying pools. Thus, while it potentially posed a conflict of

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[22] C-BASS filed for bankruptcy on November 12, 2010.

interest for C-BASS to select Litton-serviced assets for Barramundi, Deutsche Bank and C-BASS portrayed this relationship as a significant benefit to investors.

167. Deutsche Bank and C-BASS further represented that as a result of C-BASS's extensive participation in and knowledge of the market, the CDO would purchase only "high quality loans."

168. On or about October 10, 2006, Deutsche Bank sent Plaintiffs' investment advisor the preliminary term sheet ("Barramundi Term Sheet") and marketing book for Barramundi ("Barramundi Marketing Book"). The Barramundi Term Sheet and Barramundi Marketing Book were prepared by Deutsche Bank, and each page of the Barramundi Marketing Book bore Deutsche Bank's logo. These materials stressed that C-BASS had the ability to withstand severe market events because it had "long-term relationships with originators," "comprehensive risk management," "intense due diligence" and "retention of first loss classes on every deal." Barramundi Marketing Book, at 7, 21.

169. On December 1, 2006, Deutsche Bank sent Plaintiffs' investment advisor the preliminary draft of the Offering Circular for Barramundi (later superseded by a final version dated December 19, 2006, which is hereinafter referred to as the "Barramundi Offering Circular"). The Offering Circular also made extensive representations about C-BASS's expertise and abilities; it represented that "the Collateral Manager will select assets for the CDO based upon a thorough assessment of the underlying collateral quality and stress scenarios on the structure. Other important assessments are the quality, history, financial strength and information reporting systems of the servicer of the underlying collateral." Barramundi Offering Circular, at 125.

170. The Barramundi Offering Circular had been prepared by Deutsche Bank and affirmatively represented that the information set forth therein was "in accordance with the facts" and did not "omit anything likely to affect the import of such information."

171. Deutsche Bank's and C-BASS's representations were knowingly and materially false when made. Neither Deutsche Bank nor C-BASS disclosed to Plaintiffs or their investment advisor that a high proportion of the loans in the RMBS referenced by Barramundi did not meet the underwriting guidelines.[23]

172. As a significant underwriter of RMBS, C-BASS was also a customer of Clayton and its due diligence services. Clayton found that 29% of the total loans underwritten by C-BASS failed to meet the underwriting standards, but that C-BASS waived its right to reject 43% of these non-conforming loans, and included them in the RMBS it securitized anyway.

173. Additionally, as noted above, Clayton found that 35% of a sample of the loans underwritten by Deutsche Bank and its affiliates failed to meet the underwriting guidelines, that Deutsche Bank included 50% of those loans in its RMBS securitizations anyway, and, perhaps most important, that Deutsche Bank had not taken any steps to identify, let alone remove, the non-conforming loans from the much larger group of loans that was outside of Clayton's sample, and that Clayton had not tested.

174. Since Deutsche Bank and C-BASS each had similar information from Clayton, they knew or should have known that a significant percentage of the loans in the pools

[23] For example, the Barramundi portfolio referenced three tranches of the RMBS ACE 2005-AG1, which was securitized by Deutsche Bank's subsidiaries, DBSP and ACE. As alleged in the FHFA's recently-filed complaint, Deutsche Bank concealed from investors and ratings agencies that this RMBS contained high percentages of subprime mortgages with loan-to-value ratios exceeding 100% and of loans secured by non-owner occupied properties. *See Federal Housing Finance Agency v. Deutsche Bank AG et al.*, 11-CV-6192 (S.D.N.Y).

referenced by Barramundi were similarly tainted. But they concealed that information from investors.

175. Deutsche Bank and C-Bass knew that a substantial portion of the assets put into Barramundi were the same “pigs” and “crap” securities that Defendant HBK had selected for Gemstone VII. Although Deutsche Bank conveyed this material information to preferred short clients, it concealed it from Plaintiffs.

176. Deutsche Bank allowed the Barramundi portfolio to be filled with assets from originators known to be problematic. For example, the Barramundi portfolio contained a disproportionate share of loans (15%) originated by the now-notorious originator Countrywide. Similarly, the portfolio included a disproportionate share of loans originated by a single mortgage originator, Ownit Mortgage Solutions, Inc. (“Ownit”). By notional value, 31% of the loans in Barramundi had been originated by Ownit. Ownit had such severe problems in late 2006 that it went out of business eight days before Barramundi closed. Because of Ownit’s financial troubles, Deutsche Bank knew well before closing Barramundi that it would be unable to put non-conforming loans back to Ownit, severely impairing the value of those referenced RMBS.

177. Based on its role as a major player at all levels of the RMBS and CDO industries, and its insider’s access to reports from Clayton, Deutsche Bank was well aware that loans originated by Countrywide and Ownit were subject to immense, undisclosed risk.

178. Moreover, Deutsche Bank and non-party C-BASS caused Barramundi to overpay for cash assets and to accept unreasonably low credit protection premiums on CDS contracts referencing the CDO’s synthetic assets. As alleged above, both Deutsche Bank knew or should have known that the RMBS selected for Barramundi’s portfolio contained large portions of non-

conforming and fraudulent loans, yet they concealed this information from Plaintiffs and other prospective investors in Barramundi. Because the true risk associated with these assets was not disclosed, the price Barramundi paid for its cash collateral and the credit protection premiums it received on its synthetic collateral did not reflect fair market value. Because Barramundi did not receive fair consideration in these conveyances, the CDO was rendered insolvent as it lacked sufficient assets to meet its obligations to investors. Additionally, the conveyances left the CDO with insufficient capital to carry on business and to meet obligations as they arose.

179. On December 12, 2006, in reasonable and justifiable reliance on the foregoing false and misleading representations and omissions, LFJ 22 purchased from Deutsche Bank $18 million of A-rated Class C notes and LFJ 28 purchased from Deutsche Bank $61 million of AA-rated Class B notes.

180. Moody's and Fitch have since withdrawn their ratings for all the Barramundi Notes purchased from Deutsche Bank by LFJ 22 and LFJ 28. By early 2010, S&P had downgraded these Notes to D, their lowest grade.[24] The Barramundi CDO defaulted on March 13, 2009 and liquidated on January 27, 2010.

181. Deutsche Bank improperly benefitted from the sale of the Barramundi Notes by fraudulently obtaining $79 million from LFJ 22 and LFJ 28, as well as $4 million in fees.

D. Pine Mountain III

182. Pine Mountain III was a hybrid CDO deal with a portfolio consisting almost entirely of RMBS assets, approximately 65% of which were synthetic and 35% were cash. The collateral manager for Pine Mountain III was non-party Smith Breeden Associates, Inc. ("SBAI").

[24] According to S&P, a D rating signifies "payment default on financial commitments."

183. Deutsche Bank repeatedly advised Plaintiffs' investment advisor, with the knowledge and expectation that these representations or their substance would be conveyed to and relied upon by Plaintiffs, which they were, that Pine Mountain III would be managed for the benefit of long investors.

184. For example, in February 2007, Deutsche Bank provided to Plaintiffs' investment advisor, with the knowledge and expectation that it or the substance of its contents would be conveyed to Plaintiffs, which it was, a marketing book ("PM III Marketing Book") touting the qualifications of the deal's collateral manager and representing that it would "select[] securities that offer more attractive expected returns per unit of risk." PM III Marketing Book, at 30. The PM III Marketing Book had been prepared by Deutsche Bank, and in fact bore Deutsche Bank's logo on each page.

185. The PM III Marketing Book also represented that the collateral manager maintained a database of servicers and originators and claimed that through a combination of "on-site visits" and "proprietary multi-level ratings," SBAI arrived at customized estimated default rates for originators and servicers that differentiated servicers and originators at a level that even the ratings agencies could not. *Id.* at 21.

186. Further, in the Pine Mountain III offering circular ("PM III Offering Circular"), Deutsche Bank represented that all collateral assets selected for inclusion in the CDO's portfolio would be acquired on an "'arm's-length basis' for fair market value." PM III Offering Circular, at 116. The PM III Offering Circular had also been prepared by Deutsche Bank, and in fact bore Deutsche Bank's name stamped prominently on the first page.

187. These representations were false. Deutsche Bank used its position as arranger and warehouse provider to influence collateral selection for Pine Mountain III and pressured SBAI to

include RMBS in the deal's portfolio which Deutsche Bank knew among the riskiest assets eligible for inclusion in the deal and likely to fail.

188. Deutsche Bank used Pine Mountain III to offload RMBS assets from its own books on to investors. Approximately 14.5% of the cash assets in Pine Mountain III were RMBS that had been underwritten by Deutsche Bank itself. As alleged above, Deutsche Bank was well aware from the analysis provided by Clayton that a substantial portion of the loans in the mortgage pools Deutsche Bank was securitizing did not meet the bank's own underwriting standards and showed evidence of fraud.[25] Moreover, by the time the Pine Mountain III CDO closed, the RMBS securitized by Deutsche Bank already were showing dramatically worse performance than other assets, further confirming that Deutsche Bank had selected the worst assets out of its own portfolio for inclusion in the CDO.

189. Deutsche Bank knew that a substantial portion of the assets put into the for Pine Mountain III portfolio were the same "pigs" and "crap" securities that Defendant HBK had selected for Gemstone VII. Deutsche Bank conveyed that material information to preferred short clients but did not disclose it to potential long investors in Pine Mountain III, including LFJ 31 and LFJ 32. This conflict of interest was particularly acute because Deutsche Bank proposed collateral for inclusion in Pine Mountain III and pressured SBAI not to use competitive bids to acquire the best prices possible for certain assets.

190. Deutsche Bank concealed these material facts from Plaintiffs and their investment advisor. The initial Pine Mountain III portfolio was sent to Plaintiffs, via their investment

[25] For example, the Pine Mountain III portfolio referenced ACE 2006-CW1 and ACE 2006-OP1, each of which were securitized by Deutsche Bank's subsidiaries, DBSP and ACE. As alleged in the FHFA's recently-filed complaint, Deutsche Bank concealed from investors and ratings agencies that these RMBS contained high percentages of subprime mortgages with loan-to-value ratios exceeding 100% and of loans secured by non-owner occupied properties. *See Federal Housing Finance Agency v. Deutsche Bank AG et al.*, 11-CV-6192 (S.D.N.Y).

advisor, in April 2007, even though assets were still being added to the CDO's portfolio between then and the deal's closing in July 2007. In the time between Plaintiffs' review and the closing of the transaction, Deutsche Bank and SBAI stuffed the deal with RMBS assets underwritten by Deutsche Bank – including some of the riskiest assets in the portfolio – that Deutsche Bank wanted to unload.

191. Moreover, the price that Pine Mountain III paid for assets purchased directly from Deutsche Bank's inventory did not reflect fair market value because their poor quality was not generally known to market participants. As alleged above, Deutsche Bank was aware from the Clayton analysis that substantial portions of the subprime loans that it and other arranging banks were securitizing did not meet applicable underwriting standards. Yet Deutsche Bank sought to off-load its own exposure to these assets at Plaintiffs' expense by transferring them to the Pine Mountain III warehouse facility (which Deutsche Bank also controlled) at prices that did not reflect the actual risk of those assets.

192. Deutsche Bank's representations in the PM III Offering Circular that all of the CDO's collateral would be acquired at arm's length for fair market value was fraudulent.

193. Not only did Deutsche Bank knowingly sell impaired assets from its own balance sheet to Pine Mountain III at above-market prices, Deutsche Bank knowingly caused the CDO to pay above-market prices for its cash collateral at closing.

194. The market value of Pine Mountain III's portfolio of cash assets had decreased substantially in value between the time the assets were put into the warehouse and the time the CDO closed on July 10, 2007 (the same day that Moody's and S&P issued massive downgrades to huge swathes of subprime RMBS and CDOs). Indeed, between January 1, 2007 and July 10, 2007, the ABX.HE BBB 2006-1 and ABX.HE BBB 2006-2 indices (which reference assets

similar in type, vintage, and ratings to those that Deutsche Bank and SBAI had purchased for the Pine Mountain III portfolio) experienced a decline in market value of between 15% and 28%.

195. Although it knew or should have known that asset values had drastically fallen during the first half of 2007, Deutsche Bank nevertheless caused Pine Mountain III to purchase those assets at closing not at their lower, then-current market values, but instead at the higher prices based on the putative market value of those assets months earlier when they had been placed into the CDO's warehouse facility.

196. Further, Deutsche Bank caused Pine Mountain III to sell credit protection via the CDS at below-market rates. Although the subprime market was deteriorating rapidly during the ramp-up of Pine Mountain III (culminating with a massive wave of downgrades on the same day the CDO closed), the premiums at which Pine Mountain III sold protection to short investors failed to reflect this changed risk.

197. Thus, the Pine Mountain III CDO paid higher prices for its cash collateral and received lower premiums for CDS referencing its synthetic collateral than it would have in open-market *bona fide* trades. Because Pine Mountain III did not receive fair consideration in these conveyances, the CDO was rendered insolvent as it lacked sufficient assets to meet its obligations to investors. Additionally, the conveyances left the CDO with insufficient capital to carry on business and to meet obligations as they arose.

198. Moreover, prior to the closing of the Pine Mountain III CDO, Deutsche Bank had peculiar knowledge – unavailable to Plaintiffs or their investment advisor – that the assets comprising the CDO's portfolio were at risk of imminent downgrade. As early as May 2007, arranging banks – including Deutsche Bank – knew that ratings agencies were poised to begin retesting previously-issued subprime RMBS using new ratings methodologies, and the banks

knew that this would result in a tidal wave of downgrades that would in turn likely provoke a wave of defaults in CDOs containing or referencing subprime RMBS.

199. Internal e-mail correspondence from UBS Securities LLC, another major arranger of CDOs of subprime RMBS, shows that investment banks had advance knowledge of the impending downgrades. For example, a July 5, 2007 e-mail shows that UBS and other banks were involved with calls and meetings with Moody's "to discuss impacts of [asset-backed securities] subprime downgrades":

> It sounds like Moody's is trying to figure out when to start downgrading, and how much damages they're going to cause – they're meeting with various investment banks.

200. On information and belief, Deutsche Bank – then the fourth biggest issuer of asset-backed CDOs in the world (*see* Levin Report, at 335) – was one of the investment banks involved in these meetings. Obviously, information that the subprime market was poised to collapse – or, in the words of Deutsche Bank's Michael Lamont, was about to "fall[] off a cliff" (*see id.* at 366) – would have been material to investors considering investing in CDOs containing subprime RMBS, but Deutsche Bank did not disclose this information to Plaintiffs or other potential investors in Pine Mountain III.

201. On July 10, 2007, in reasonable and justifiable reliance upon the foregoing false and misleading representations and omissions, LFJ 31 and LFJ 32 each bought $44,875,000 in AAA-rated Class A-3 Pine Mountain III Notes.

202. The Pine Mountain III CDO defaulted on May 1, 2009. Plaintiffs' Notes have been downgraded to below-investment grade (CC) and are now virtually worthless.

203. Deutsche Bank improperly benefited from the sale of the Pine Mountain III Notes by fraudulently obtaining $89.75 million from LFJ 31 and LFJ 32, as well as $9.15 million in

fees as well as money from a $1.8 million "Closing Expense Account," aimed to cover closing-related fees, commissions and expenses.

IV. Deutsche Bank's Failure to Disclose the Role of Short Investors in Selecting Collateral for CDOs Marketed to Plaintiffs as High-Grade Long Investments

204. Deutsche Bank also constructed a series of unmanaged CDOs with "static" portfolios at the behest of other clients in order to allow them to capitalize on the collapse of the subprime mortgage market, at the expense of long investors such as Plaintiffs.

205. The first CDO series that Deutsche Bank constructed for the benefit of other firms' shorting strategies was known as STAtic ResidenTial ("START"). Deutsche Bank went on to arrange a series of START CDOs. Each START CDO was synthetic, thereby maximizing the value of CDS contracts that Deutsche Bank's preferred clients could use to short (or hedge) their subprime exposures.

206. Indeed, as recently reported by the Senate Subcommittee, in four of the six START deals, Paulson Advisors, an affiliate of Paulson & Co., Inc. (together, "Paulson") – a hedge fund now notorious for its short bets on the housing market – simultaneously purchased both the deals' equity tranches and CDS protection against the entire deals, thus effectively shorting the CDOs and betting that the value of their assets would fall. *See* Levin Report, at 374. In another one of the six START deals, Elliot Advisors, another hedge fund seeking to short the subprime market, simultaneously purchased the CDO's equity tranche and took a short position against the deal as the CDS counterparty. *See id.*

207. In effect, Deutsche Bank arranged and covertly employed the START CDOs as a shorting vehicle for the benefit of its preferred clients in exactly the same way that Goldman, Sachs & Co. ("Goldman") secretly used a deal known as ABACUS 2007-AC1 ("ABACUS") as a shorting vehicle for Paulson. On April 16, 2010, the SEC filed a complaint against Goldman

for securities fraud in connection with ABACUS. On July 14, 2010, Goldman reached a settlement with the SEC and paid a $550 million fine, admitting that it had been a "mistake" not to disclose that Paulson was involved in asset selection and that its interests were directly adverse to those of the CDO's long investors. *See id.* at 397.

208. Moreover, Deutsche Bank knew that the assets selected for the START CDOs were the same "pigs" and "crap" that were selected for Gemstone VII. Deutsche Bank selectively conveyed that material information to preferred short clients but did not disclose it to long investors in START, including Plaintiffs.

A. START 2005-C

209. In or about late 2005, Deutsche Bank began to market investments in the START program to Plaintiffs' investment advisor. In the course of this marketing effort, Deutsche Bank repeatedly misrepresented two highly material facts: first, that the portfolios for the START transactions were designed to be a diverse cross-section of new RMBS assets; and second, to the extent Deutsche Bank exercised any discretion in choosing the portfolio, that it exercised that discretion in favor of the CDOs' equity purchasers and long investors whose financial interests were supposedly aligned with those of Plaintiffs.

210. At an early stage of the process, Deutsche Bank provided Plaintiffs' investment advisor with a marketing book intended to induce Plaintiffs into investing in START ("START Investor Presentation").[26]

211. The START Investor Presentation stated that the START program was designed to "provid[e] a unique opportunity to invest in an 'index-like' synthetic RMBS product in a

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[26] Although it specifically concerned a transaction denominated START 2005-B, this marketing book was intended and used by Deutsche Bank to describe the START program in general, and be equally applicable to other START transactions.

cashflow CDO form," with each START CDO referencing "recent vintage RMBS." START Investor Presentation, at 2. The reference to the "index-like" nature of the START CDO indicated that noteholders would gain access to a diverse cross-section of securities from a single vintage, benefitting from the performance of that vintage as a whole while reducing the risk associated with over-concentrating in any particular category of exposure. *Id.*

212. The START Investor Presentation described an essentially mechanical "portfolio selection process" that produced this "cross section of the RMBS new issue market" for 2005. *Id.* at 12. In brief, Deutsche Bank represented that out of the universe of new RMBS transactions securitized in 2005, Deutsche Bank removed assets that were not rated by Moody's, were not rated by S&P, were not rated at the desired levels, were not "pure floating assets," and were "not conforming to shelf/servicer/rating concentrations of target portfolio." *Id.* The START Investor Presentation did not disclose that Deutsche Bank exercised any judgment or discretion in selecting the assets, let alone judgment or discretion in favor of its short clients to the detriment of potential long investors.

213. The START Investor Presentation included other representations intended to convey the safety of the investment to potential investors like Plaintiffs. For example, the marketing book represented that it was composed of a "highly diversified portfolio" and that "***all assets are rated investment grade by both Moody's and S&P***." *Id.* at 4 (emphasis in original).

214. The START Investor Presentation acknowledged that it had been prepared by Deutsche Bank for investors to use in "making an evaluation" of a potential investment in the START deals, and bore Deutsche Bank's logo on each page.

215. In addition to providing this marketing book, Deutsche Bank made additional representations to Plaintiffs' investment advisor to bolster its attempts to persuade Plaintiffs to

invest in the START CDOs. For example, in a June 21, 2005 e-mail between Plaintiffs' investment advisor and Michael George, a Deutsche Bank managing director, George represented that a previous START deal had been "driven by a strategic partner that we have for Equity." Deutsche Bank stated that it was interested in "working with" Plaintiffs' investment advisor to construct another CDO portfolio for the benefit of both Plaintiffs and Deutsche Bank's "Equity buyer." Moreover, the e-mail explicitly denied that the equity buyer had motives at odds with long investors: "THIS IS NOT A CORRELATION TRADE" (emphasis in original).

216. On October 17, 2005, Deutsche Bank provided Plaintiffs' investment advisor for ultimate transmittal to Plaintiffs with a term sheet for START 2005-C (the "START 2005-C Term Sheet"). The START 2005-C Term Sheet was also prepared by Deutsche Bank, and in fact had Deutsche Bank's name stamped in the top right-hand corner of each page. The START 2005-C Term Sheet described the CDO as a synthetic CDO of CDS that featured a "highly diversified portfolio of . . . recent-vintage transactions." START 2005-C Term Sheet, at 1.

217. In e-mails from early December, 2005 – shortly before Plaintiffs' investment advisor's final decision to recommend an investment in START 2005-C – with the intent of inducing Plaintiffs to purchase, George indicated to Plaintiffs' investment advisor that to accommodate the equity "buyer" for the CDO, the asset portfolio had been "tweaked" and "improved slightly." Deutsche Bank also represented that it was getting "feedback from other investors" and was trying to "maintain the target rating quality of the portfolio."

218. These representations were false and so incomplete as to be misleading. Deutsche Bank did not use a mechanical selection process to create an "index-like" "cross section" "representative" portfolio for START. Nor was the portfolio "tweaked" or "improved" by equity investors whose interests were aligned with those of Plaintiffs. To the contrary, Deutsche Bank

and its undisclosed short clients selected lower-quality bonds that were more likely to fail and thus benefit the short investors at the expense of unwitting long investors, including Plaintiffs.

219. On information and belief, the undisclosed "equity partner" was in fact a hedge fund that was using the CDO as a vehicle for shorting the subprime housing market.

220. In selecting impaired RMBS for inclusion in the START 2005-C portfolio, Deutsche Bank and the CDO's short investor used peculiar knowledge that was not possessed by, or readily available to, Plaintiffs or their investment advisor. Unbeknownst to Plaintiffs, the loan pools referenced by the START 2005-C portfolio already showed significantly elevated rates of delinquency, default, foreclosure, and loss compared to the universe of comparable subprime loan pools. The assets referenced by the START 2005-C CDO were chosen for the portfolio precisely because these performance statistics showed significant discrepancies from average assets.

221. Because Deutsche Bank had a long relationship with Plaintiffs through their investment advisor with whom it had worked for nearly six months on the START 2005-C transaction, Deutsche Bank was aware of the analytical procedures for CDOs and underlying RMBS assets employed by Plaintiffs' investment advisor. This knowledge enabled Deutsche Bank (and its undisclosed hedge fund clients) to select assets based on indicia that Plaintiffs' investment advisor, like other investment advisors, did not typically consider in its own analysis.

222. Deutsche Bank also had peculiar knowledge about the loans that were included in the referenced RMBS. This included the information about non-conforming loans that Deutsche Bank had received from Clayton and from others in the market, as well as accurate delinquency statistics which were not included in prospectuses for RMBS securitized by Deutsche Bank.

223. On or about October 27, 2005, based on its belief that the portfolio had not been adversely selected, and in reasonable and justifiable reliance on Deutsche Bank's false and misleading representations and omissions, Plaintiff LFJ 19 accepted its investment advisor's recommendation to invest in START 2005-C. On or about January 18, 2006, LFJ 19 purchased from Deutsche Bank and is currently the owner of: $38.5 million of START 2005-C Class A-2 Notes (rated AAA at the time); $4 million of START 2005-C Class B Notes (rated AA+ at the time); and $17.5 million of START 2005-C Class C Notes (rated AA- at the time). The START 2005-C Notes are now rated as junk and are virtually worthless.

224. Deutsche Bank improperly benefited from the sale of the START 2005-C Notes by fraudulently inducing Plaintiffs to invest $60 million in the CDO, as well as obtaining $9.5 million in fees and money from a $1.359 million "Closing Expense Account."

B. <u>START 2006-B</u>

225. In the summer of 2006, Deutsche Bank pitched a potential investment in another START CDO – START 2006-B – to Plaintiffs' investment advisor.

226. Over a period of months leading up to Plaintiffs' purchase of the START 2006-B investment, Deutsche Bank again misrepresented that the selection of the referenced assets was influenced by equity and other long investors, not by "naked" short investors including Deutsche Bank itself. Deutsche Bank also went further, stating explicitly that the assets had not been adversely selected by Deutsche Bank or other short investors.

227. On July 12, 2006, Deutsche Bank's Michael George sent an e-mail to Plaintiffs' investment advisor, with the intention of influencing Plaintiffs' investment decision, which it did, regarding "START equity placement" and the different ways that "HFs" (*i.e.*, hedge funds) could be involved in static CDO deals. George stated (ellipses in the original):

> 1. You don't want to buy a deal where the assets have been SHORTED into the deal by a HF and the equity placed to other clients ... implies that the assets have been begatively [sic] selected!!...
>
> **NOT THE CASE HERE**

Thus, Deutsche Bank expressly acknowledged its understanding that Plaintiffs did not want to invest in CDOs where the underlying assets had been adversely selected by short interests, and expressly represented that that was "not the case" with the START 2006-B transaction.

228. In the same e-mail, George continued:

> 2. If the assets are sourced independently ... DB runs a BWIC [Bid Wanted in Competition] and funds the start deal ... various different clients will sell assets into the deal with DB standing between the deal and the clients ... In this sort of deal the equity may be bought by HFs ... who'll want to insure that the assets are GOOD (different from 1, where the HF wants the assets to be BAD)
>
> **** THIS WAS THE CASE WITH THE LAST START THAT YOU BOUGHT****

Thus, George again described a situation where the equity investors chose the synthetic RMBS assets for the CDO, with Deutsche Bank operating a bidding process to ensure that the CDO got a fair price for the assets from "various different clients."

229. Also in the July 12, 2006 e-mail, George described two additional types of CDO structures, and expressly represented, with the intention of misleading Plaintiffs, that neither of these potential structures involved adverse selection of the underlying assets by a "naked" short interest.

230. Deutsche Bank's representations were intentionally false and misleading. Deutsche Bank never disclosed the truth — that because it too was shorting the subprime market, its financial interests were aligned with those of the short investors with whom it was working

hand-in-hand to choose the riskiest available RMBS assets that had an elevated probability of failure.

231. In fact, the START 2006-B collateral shows almost precisely the same indicia of adverse selection as the START 2005-C collateral – significantly elevated rates of delinquency, foreclosure, and loss relative to the universe of comparable subprime loan pools.

232. Deutsche Bank's representation that it was "standing between the deal and the clients" was also intentionally false and misleading. Deutsche Bank was not always a mere intermediary on these transactions; in some instances Deutsche Bank was the actual beneficiary of the CDS contracts with the CDO. In that capacity, Deutsche Bank had a diametrically opposite interest in the performance of the deal than investors, including Plaintiffs.

233. Deutsche Bank made these misrepresentations to mislead, and in fact misled, Plaintiffs and their investment advisor into believing that Deutsche Bank was primarily seeking to serve the interests of long investors like Plaintiffs. The capitalized emphasis that Deutsche Bank gave those representations ("GOOD," "BAD," "NOT THE CASE HERE") reflects its knowledge that those facts were highly material to Plaintiffs' investment decisions, and shows that Deutsche Bank intended and expected Plaintiffs to rely on those representations.

234. Deutsche Bank made similar misleading assertions about the purported equity buyer on a "Questionnaire" that Plaintiffs' investment advisor, for the benefit of Plaintiffs, submitted to Deutsche Bank during due diligence for the START 2006-B investment ("START 2006-B Questionnaire"). Responding to the question of whether Deutsche Bank would retain those equity positions or "Sub Notes," Deutsche Bank stated: "DB will not be retaining any Sub Notes issued by the CDO and such Sub Notes will be sold or hedged with a third party (via TRS

[*i.e.*, "Total-Return Swap"]) that is using the structure to term finance leverage the portfolio of single names in the deal." START 2006-B Questionnaire, at 1.

235. Deutsche Bank's reference to "term financing" in the questionnaire and in the July 12 e-mail suggested that the third party was long the referenced assets and wanted to hedge them, not that the third party wanted to take a net short position. This difference was material to Plaintiffs and their investment advisor because a net short interest would presumably select the worst possible assets for the deal's reference portfolio, while a party that was "term financing" its long portfolio has some interest in purchasing credit protection on the referenced assets.

236. The Offering Circular for START 2006-B also did not disclose that the CDO was being created specifically for the benefit of a short interest, nor that the portfolio assets would be adversely selected.

237. In reasonable and justifiable reliance upon Deutsche Bank's knowingly false and misleading representations and omissions, LFJ 8 and LFJ 24 invested in START 2006-B.

238. On or about August 18, 2006, LFJ 8 purchased from Deutsche Bank $21 million START 2006-B Class B-2 Notes, rated AA-. On or about the same day, LFJ 24 purchased from Deutsche Bank $39 million START 2006-B Class A-2 Notes, rated AAA, and $30 million Class B-1 Notes, rated AA+.

239. By mid-2008, the START 2006-B Notes purchased from Deutsche Bank by LFJ 8 and LFJ 24 had been downgraded to junk: D (Class A-2 and B-1) and CC (Class B-2). The START 2006-B Notes have since defaulted, and are now worthless.

240. Deutsche Bank improperly benefited from the sale of the START 2006-B Notes by fraudulently obtaining $90 million for the benefit of itself and its clients, who were the

counterparties on the CDSs sold by the CDO, as well as $8.35 million in fees and money from a $1.475 million "Closing Expense Account."

C. **The START CDOs Did Not Receive Fair Consideration for the CDS They Sold to Deutsche Bank's Preferred Short Investor Clients**

241. As alleged above, unknown to investors, including the START Plaintiffs, Deutsche Bank and the undisclosed short investors in the START CDOs colluded to stock the CDOs' portfolios with the weakest possible reference assets.

242. Moreover, on information and belief, the START CDOs received lower premiums for CDS contracts referencing their synthetic collateral than they would have in open-market *bona fide* trades. By misrepresenting and concealing the fact that the START CDOs' collateral had been selected in collusion with, and for the benefit of, Deutsche Bank's preferred hedge fund clients, Deutsche Bank ensured that the true risk of this collateral was not accurately reflected in the CDS premiums received by the START CDOs. Had this material information been publicly disclosed, the CDS premiums the START CDOs would have received in open-market *bona fide* trades would have been substantially higher.

243. Because the START CDOs did not receive fair consideration in these conveyances, the CDOs were rendered insolvent as they lacked sufficient assets to meet their obligations to investors. Additionally, the conveyances left the CDOs with insufficient capital to carry on business and to meet obligations as they arose.

CAUSES OF ACTION

FIRST CAUSE OF ACTION

(Common Law Fraud against Deutsche Bank and HBK)

244. Plaintiffs repeat and reallege all of the foregoing paragraphs as if fully set forth herein.

245. As alleged above, Deutsche Bank in the case of each of the START 2005-C, START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs, and HBK in the case of the Gemstone VII CDO, made false and misleading representations to Plaintiffs and omitted material facts that they were under a duty to disclose .

246. Among other things, Deutsche Bank and, in the case of Gemstone VII, HBK, misrepresented and concealed: the identity and interests of the parties who selected the collateral; the quality of the assets underlying the CDOs' collateral pools; the value, credit quality, and risk of loss for the notes purchased from Deutsche Bank by Plaintiffs in these CDOs; and the likelihood that impending changes in rating methodologies would result in the collapse of CDOs investing in subprime RMBS.

247. Deutsche Bank also failed to specifically disclose to Plaintiffs and other long investors in these deals its knowledge that much of the collateral underlying these CDOs was "crap," "pigs," and was "blowing up." Notwithstanding this knowledge, Deutsche Bank placed these assets into the CDOs without disclosure even as it was advising its preferred short clients to bet against these same assets. Further, Deutsche Bank and HBK misrepresented that collateral for these CDOs would be acquired at "arm's-length" and for "fair market value," when in reality Deutsche Bank (and, in the case of Gemstone VII, HBK) transferred risky assets from its own balance sheet to the CDOs at above-market prices.

248. Deutsche Bank's and HBK's representations were materially false and misleading when made. These representations were made intentionally or with reckless disregard for the truth.

249. Deutsche Bank and HBK made these false and misleading representations and omissions to Plaintiffs directly or via Plaintiffs' investment advisor. Deutsche Bank and HBK

knew or should have known that Plaintiffs would reasonably rely on these false and misleading representations and omissions.

250. Based upon Deutsche Bank's and HBK's peculiar knowledge and expertise, and incomplete and misleading disclosures, and in light of the fact that Plaintiffs did not have access to material facts that were peculiarly within Defendants' knowledge, Deutsche Bank and HBK had an affirmative duty to provide complete and accurate disclosures of the material facts uniquely within their knowledge. Deutsche Bank intentionally or recklessly failed to provide full, complete, and accurate disclosures of these material facts. Deutsche Bank and HBK intentionally failed to provide, or recklessly disregarded their obligation to provide, full, complete, and accurate disclosures of these material facts.

251. Plaintiffs reasonably and justifiably relied to their detriment on Deutsche Bank's and HBK's false and misleading representations and omissions in purchasing the above-described notes issued in connection with the START 2005-C, START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs.

252. As a result of their fraud, Deutsche Bank is liable to Plaintiffs in an amount in excess of $438,750,000 plus interest, and HBK is liable to Plaintiffs in an amount in excess of $20,000,000 plus interest.

253. As alleged above, Deutsche Bank's and HBK's conduct constituted gross fraud and involved a high degree of moral culpability in that it contributed significantly to the global financial crisis and affected the public generally. Plaintiffs are therefore entitled to punitive damages in an amount to be determined at trial.

SECOND CAUSE OF ACTION

(Rescission Based Upon Fraud against Deutsche Bank)

254. Plaintiffs repeat and reallege all of the foregoing paragraphs as if fully set forth herein.

255. Plaintiffs purchased each of the above-described notes issued in connection with the START 2005-C, START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs from Deutsche Bank.

256. Deutsche Bank's representations and omissions with respect to the notes purchased by Plaintiffs were material, incomplete, misleading and false when made. These false and misleading representations and omissions were made intentionally or with reckless disregard for the truth.

257. Deutsche Bank made these false and misleading representations and omissions to Plaintiffs directly or via Plaintiffs' investment advisor. Deutsche Bank knew or should have known that Plaintiffs would reasonably rely on these false and misleading representations and omissions.

258. Based upon Deutsche Bank's peculiar knowledge and expertise, and incomplete and misleading disclosures, and in light of the fact that Plaintiffs did not have access to material facts that were peculiarly within Deutsche Bank's knowledge, Deutsche Bank had an affirmative duty to provide full, complete, and accurate disclosures of these material facts. Deutsche Bank intentionally failed to provide, or recklessly disregarded its obligation to provide, full, complete, and accurate disclosures of these material facts.

259. As a result of the false and misleading representations and omissions detailed above, there was fraud in the inducement of the contract for the sale of the START 2005-C

Notes, START 2006-B Notes, Carina Notes, Barramundi Notes, Gemstone VII Notes, and Pine Mountain III Notes from Deutsche Bank to Plaintiffs.

260. Plaintiffs reasonably and justifiably relied to their detriment on Deutsche Bank's false and misleading representations and omissions, in purchasing the above-described notes issued in connection with the START 2005-C, START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs.

261. Deutsche Bank's false and misleading representations and omissions fraudulently induced Plaintiffs to purchase the above-described notes from Deutsche Bank, which they would not have done had they known the truth.

262. The notes that Plaintiffs bargained for were different from what Plaintiffs received from Deutsche Bank. Plaintiffs lack an adequate remedy at law.

263. Consequently, Plaintiffs are entitled to a judgment rescinding the contracts of sale and directing Deutsche Bank to return the $438,750,000 that Plaintiffs paid for notes in those CDOs, together with interest.

264. Rescission would restore each party to its original position through Deutsche Bank tendering the original purchase price plus interest, less any benefit, to Plaintiffs, and Plaintiffs tendering their notes to Deutsche Bank.

THIRD CAUSE OF ACTION

(Conspiracy to Defraud against HBK and Deutsche Bank)

265. Plaintiffs repeat and reallege all of the foregoing paragraphs as if fully set forth herein.

266. As alleged above, Defendants Deutsche Bank and HBK made material misrepresentations and omissions for the purpose of inducing Plaintiff LFJ 4 to purchase notes

in the Gemstone VII CDO. These misrepresentations were material, incomplete, misleading, and false when made.

267. The material misrepresentations and omissions as described above constituted a fraud against LFJ 4.

268. The conduct of Deutsche Bank and HBK occurred pursuant to a common scheme and agreement in connection with Gemstone VII. Their overt acts in furtherance of that agreement included, inter alia, the material misrepresentations and omissions to LFJ 4 as described above.

269. Deutsche Bank and HBK intentionally participated in this common scheme and agreement in furtherance of a plan or purpose to, inter alia, defraud LFJ 4, earn lucrative fees, and remove some of the worst assets from their inventories at above fair-market prices, as described above.

270. The object of the foregoing conspiracy was unlawful.

271. As a direct and proximate result of the foregoing conspiracy to commit fraud in connection with the sale to Plaintiff LFJ 4 of the Gemstone VII Notes, Deutsche Bank and HBK are liable to Plaintiff LFJ 4 for damages in an amount in excess of $20 million plus interest.

FOURTH CAUSE OF ACTION

(Fraud and Aiding and Abetting Fraud against HBK and Deutsche Bank)

272. Plaintiffs repeat and reallege all of the foregoing paragraphs as if fully set forth herein.

273. As described in the preceding allegations, Defendant HBK and non-party C-BASS made materially misleading and incomplete statements to induce Plaintiffs into investing in the Gemstone VII Notes and Barramundi Notes, respectively. HBK and non-party C-BASS

falsely represented that they would select desirable assets for inclusion in the CDOs they managed, when in fact they chose reference assets that were likely to default and yield credit protection payments to Deutsche Bank and its clients, as well as cash assets that Deutsche Bank wanted to remove from its own portfolio. HBK and non-party C-BASS made these misrepresentations and omissions knowingly or recklessly to Plaintiffs' investment advisor with the knowledge and intent that they or their substance would be conveyed to Plaintiffs, which they were, and that Plaintiffs would rely on them, which they did.

274. On Plaintiffs' behalf, Plaintiffs' investment advisor agreed that the Gemstone VII CDO and the Barramundi CDO would compensate their respective collateral managers for performing a thorough and careful evaluation of the assets included in the collateral pools for these CDOs, and Plaintiffs were entitled to rely on the respective collateral managers to conduct that analysis.

275. Plaintiffs would not have purchased the Gemstone VII Notes or the Barramundi Notes had they known the truth.

276. Plaintiffs' reliance on these misrepresentations and omissions was justified.

277. Deutsche Bank knew that HBK and non-party C-BASS were misrepresenting or omitting to disclose the true nature of the CDOs they respectively managed and the quality of the underlying assets.

278. Deutsche Bank substantially assisted the collateral managers' fraud by, among other things, preparing the offering documents, having its affiliate serve as the counterparty for the CDOs, and working with its hedge fund clients to choose the least creditworthy RMBS assets for the CDOs to reference.

279. HBK knew that Deutsche Bank was misrepresenting or omitting to disclose the true nature of and the quality of the underlying assets in the Gemstone VII CDO.

280. HBK substantially assisted Deutsche Bank's fraud by, among other things, participating in the preparation of offering documents and selecting deteriorating assets for inclusion as cash and reference assets in the Gemstone VII CDO.

281. As a result of HBK's fraud and aiding and abetting of fraud and Deutsche Bank's aiding and abetting fraud in connection with the Gemstone VII CDO, HBK and Deutsche Bank are liable to Plaintiff LFJ 4 for damages in an amount in excess of $20 million plus interest.

282. As a result of Deutsche Bank's aiding and abetting fraud in connection with the Barramundi CDO, Deutsche Bank is liable to Plaintiffs LFJ 22 and LFJ 28 for damages in an amount in excess of $79 million plus interest.

283. Because Defendants' conduct affected the public generally, was gross and highly morally culpable, Plaintiffs are also entitled to punitive damages in an amount to be determined at trial.

FIFTH CAUSE OF ACTION

(Fraudulent Conveyance against All Defendants)

284. Plaintiffs repeat and reallege all of the foregoing paragraphs as if fully set forth herein.

285. Plaintiffs, as holders of the START 2005-C Notes, START 2006-B Notes, Carina Notes, Barramundi Notes, Gemstone VII Notes, and Pine Mountain III Notes are creditors of the various CDO issuers pursuant to the terms of the governing indentures and offering circulars.

286. At various dates in 2006 and 2007, Defendants bought cash assets for the Carina CDO, Barramundi CDO, Gemstone VII CDO, and Pine Mountain III CDO for consideration that greatly exceeded the fair value of those securities.

287. Moreover, at various dates in 2006 and 2007, Deutsche Bank caused the START CDOs, the Carina CDO, the Barramundi CDO, the Gemstone VII CDO, and the Pine Mountain III CDO to sell CDS contracts to Defendant DB AG and to other short investors – including non-party Magnetar – for below-market premiums.

288. The foregoing transactions (the "Conveyances") rendered the START CDOs, the Carina CDO, the Barramundi CDO, the Gemstone VII CDO, and the Pine Mountain III CDO "insolvent" within the meaning of § 271 of the DCL. By virtue of this insolvency, the Conveyances were fraudulent as to creditors under § 273 of the DCL.

289. The Conveyances were made without "fair consideration" within the meaning of § 272 of the DCL at a time when the START, Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs were or were about to be engaged in a business transaction for which the property remaining at their disposal after the conveyance was "an unreasonably small capital" within the meaning of § 274 of the DCL. Thus, the Conveyances were fraudulent as to creditors (including Plaintiffs) under § 274 of the DCL.

290. Defendants Deutsche Bank, START 2005-B, START 2006-C, Carina, Barramundi, Gemstone VII, Pine Mountain III, HBK, and non-party Magnetar, knew that as a result of the Conveyances, investors in the START, Carina, Gemstone VII, and Pine Mountain III CDOs (including Plaintiffs) would fund short positions held by DB AG and Deutsche Bank's preferred short clients, including non-party Magnetar, that were intended to drain the CDOs of their assets and defraud creditors (including Plaintiffs). Knowing these facts, Deutsche Bank – with the assistance of and in collaboration with, among others, HBK and Magnetar – caused or induced the START, Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs to make the Conveyances.

291. The Conveyances were made with actual intent "to hinder, delay, or defraud present or future creditors" and were therefore fraudulent as to creditors under § 276 of the DCL. Consequently, Plaintiffs are entitled to set these conveyances aside pursuant to § 278(a) of the DCL.

SIXTH CAUSE OF ACTION

(Unjust Enrichment against All Defendants)

292. Plaintiffs repeat and reallege all of the foregoing paragraphs as if fully set forth herein.

293. As a result of their wrongful conduct detailed above, Defendants have been unjustly enriched, and Plaintiffs are entitled to judgment ordering Defendants to disgorge to Plaintiffs all amounts they received as a result of their involvement in connection with the START 2005-C CDO, START 2006-B CDO, Carina CDO, Barramundi CDO, Gemstone VII CDO, and Pine Mountain III CDO, including without limitation: (i) the proceeds of the sales of the Notes; (ii) all collateral management fees; (iii) amounts received by Deutsche Bank and its affiliates as counterparties to CDS contracts issued by Deutsche Bank-arranged CDOs; (iv) distributions of any type from the CDOs at issue; (v) commissions or sales fees; and (vi) amounts received from the CDOs at issue in transactions involving the purchase of collateral.

WHEREFORE, Plaintiffs respectfully demand the entry of judgment in their favor and against Defendants as follows:

A. On the Second Cause of Action against Defendant Deutsche Bank rescinding, in whole or in part, each of the purchases of the above-described Notes by Plaintiffs as described above, and ordering that Deutsche Bank return to Plaintiffs the purchase prices paid for the Notes issued in connection with each of the START 2005-C,

START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs, less any benefit to Plaintiffs;

B. On the First Cause of Action, Third Cause of Action and Fourth Cause of Action against Defendants Deutsche Bank and HBK, awarding Plaintiffs: (i) damages from Defendants in amount to be determined at trial, but in no event less than $438,750,000 comprised of the entire amount of the note purchases made by each of the Plaintiffs in connection with the purchase prices paid for the Notes issued in connection with each of the START 2005-C, START 2006-B, Carina, Barramundi, Gemstone VII, and Pine Mountain III CDOs; and (ii) other damages Plaintiffs have sustained as a result of Deutsche Bank's and HBK's conduct as described above, in an amount to be determined at trial;

C. On the Fifth Cause of Action against all Defendants, an order setting aside and voiding each of the property transfers described above as fraudulent conveyances, and directing that the property transferred be made available to Plaintiffs in satisfaction of the judgment rendered in this action, together with interest and other amounts awarded to Plaintiffs;

D. On the Sixth Cause of Action against all Defendants, ordering disgorgement of Defendants' ill-gotten gains and unjustly obtained fees and profits, and ordering restitution of such gains to Plaintiffs as appropriate;

E. Awarding Plaintiffs punitive damages as a result of Defendants' intentional, deliberate, malicious, willful, and wanton conduct as detailed above;

F. Awarding Plaintiffs pre-judgment and post-judgment interest;

G. Awarding Plaintiffs their costs and fees, including, to the extent applicable, attorneys' fees and other costs incurred by Plaintiffs in bringing this action; and

H. Awarding Plaintiffs such other relief as this Court may deem just and appropriate.

Dated: October 5, 2011
New York, NY

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