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

AMERICAN INTERNATIONAL GROUP, INC., AIG SECURITIES LENDING CORPORATION, AMERICAN GENERAL ASSURANCE COMPANY, AMERICAN GENERAL LIFE AND ACCIDENT INSURANCE COMPANY, AMERICAN GENERAL LIFE INSURANCE COMPANY, AMERICAN GENERAL LIFE INSURANCE COMPANY OF DELAWARE, AMERICAN HOME ASSURANCE COMPANY, AMERICAN INTERNATIONAL GROUP RETIREMENT PLAN, CHARTIS PROPERTY CASUALTY COMPANY, CHARTIS SELECT INSURANCE COMPANY, CHARTIS SPECIALTY INSURANCE COMPANY, COMMERCE AND INDUSTRY INSURANCE COMPANY, FIRST SUNAMERICA LIFE INSURANCE COMPANY, LEXINGTON INSURANCE COMPANY, NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PA, NEW HAMPSHIRE INSURANCE COMPANY, SUNAMERICA ANNUITY AND LIFE ASSURANCE COMPANY, SUNAMERICA LIFE INSURANCE COMPANY, THE INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA, THE UNITED STATES LIFE INSURANCE COMPANY IN THE CITY OF NEW YORK, THE VARIABLE ANNUITY LIFE INSURANCE COMPANY, and WESTERN NATIONAL LIFE INSURANCE COMPANY, **Plaintiffs,** **-against-** **BANK OF AMERICA CORPORATION,**	**Index No. ___________** **COMPLAINT**

BANC OF AMERICA SECURITIES LLC, BANK OF AMERICA, NATIONAL ASSOCIATION, BANC OF AMERICA FUNDING CORPORATION, BANC OF AMERICA MORTGAGE SECURITIES, INC., ASSET BACKED FUNDING CORPORATION, NB HOLDINGS CORPORATION, MERRILL LYNCH & CO., INC., MERRILL LYNCH MORTGAGE LENDING, INC., FIRST FRANKLIN FINANCIAL CORPORATION, MERRILL LYNCH MORTGAGE CAPITAL INC., MERRILL LYNCH CREDIT CORPORATION, MERRILL LYNCH, PIERCE, FENNER & SMITH INC., MERRILL LYNCH MORTGAGE INVESTORS, INC., COUNTRYWIDE FINANCIAL CORPORATION, COUNTRYWIDE CAPITAL MARKETS LLC, COUNTRYWIDE HOME LOANS, INC., COUNTRYWIDE SECURITIES CORPORATION, CWABS, INC., CWALT, INC., CWHEQ, INC., and CWMBS, INC.,

Defendants.

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Plaintiffs American International Group, Inc., AIG Securities Lending Corporation, American General Assurance Company, American General Life and Accident Insurance Company, American General Life Insurance Company, American General Life Insurance Company of Delaware, American Home Assurance Company, American International Group Retirement Plan, Chartis Property Casualty Company, Chartis Select Insurance Company, Chartis Specialty Insurance Company, Commerce and Industry Insurance Company, First SunAmerica Life Insurance Company, Lexington Insurance Company, National Union Fire Insurance Company of Pittsburgh, Pa., New Hampshire Insurance Company, SunAmerica Annuity and Life Assurance Company, SunAmerica Life Insurance Company, The Insurance Company of the State of Pennsylvania, The United States Life Insurance Company in the City of New York, The Variable Annuity Life Insurance Company, and Western National Life Insurance Company (collectively, "AIG"), by its attorneys, Quinn Emanuel Urquhart & Sullivan LLP, for its Complaint against Bank of America Corporation, Banc of America Securities LLC, Bank of America, National Association, Banc of America Funding Corporation, Banc of America Mortgage Securities, Inc., Asset Backed Funding Corporation, NB Holdings Corporation (collectively, "Bank of America"), Merrill Lynch & Co., Inc., Merrill Lynch Mortgage Lending, Inc., First Franklin Financial Corporation ("First Franklin"), Merrill Lynch Mortgage Capital Inc., Merrill Lynch Credit Corporation, Merrill Lynch Pierce, Fenner & Smith, Inc. ("MLPF&S"), Merrill Lynch Mortgage Investors, Inc. (collectively, "Merrill Lynch" or "Merrill"), Countrywide Financial Corporation ("Countrywide Financial"), Countrywide Capital Markets LLC, Countrywide Home Loans, Inc. ("Countrywide Home Loans"), Countrywide Securities Corporation ("Countrywide Securities"), CWABS, Inc., CWALT, Inc., CWHEQ, Inc., CWMBS, Inc. (collectively, "Countrywide") (all collectively, "Defendants") allege as follows:

NATURE OF ACTION

1. This case arises from a massive fraud perpetrated by Defendants Bank of America, Merrill Lynch, and Countrywide that has resulted in more than $10 billion in damages to AIG, and ultimately American taxpayers. AIG brings this action as part of its overall efforts to recoup such damages from these defendants and other parties.

2. Between 2005 and 2007, Defendants fraudulently induced AIG to invest in nearly 350 residential mortgage-backed securities ("RMBS") at a price of over $28 billion. Driven by a single-minded desire to increase their share of the lucrative RMBS market and the considerable fees generated by it, Defendants created and marketed RMBS backed by hundreds of thousands of defective mortgages.

3. The Offering Materials used to sell the RMBS fraudulently misrepresented and concealed the actual credit quality of the mortgages by providing false quantitative data about the loans, thus masking the true credit risk of AIG's investments. The Offering Materials also falsely claimed that the mortgages had been issued pursuant to objective underwriting guidelines. In fact, the loan originators, including Defendants, encouraged borrowers to falsify loan applications, pressured property appraisers to inflate home values, and ignored obvious red flags in the underwriting process.

4. The stated underwriting guidelines had been replaced by an undisclosed governing principle: Defendants would originate or acquire any loan that could be sold to third-party investors like AIG through RMBS securitization, no matter how risky. To make matters worse, Defendants provided to the rating agencies the same false credit metrics that riddled the Offering Materials, thus allowing Defendants to engineer inflated credit ratings for the RMBS, which they also used to market the securities. AIG, which suffered more than $10 billion in

losses as a result of Defendants' misconduct, would not have purchased the securities if it had known the truth.

5. As Defendants knew, the true quality and value of the RMBS it was offering for sale depended on the credit quality of the mortgage loans underlying the RMBS. Investors like AIG assessed the risk of investing in RMBS based on quantitative, risk-related metrics regarding the loans backing the RMBS such as loan-to-value ("LTV") ratios, combined loan-to-value ("CLTV") ratios, and owner-occupancy statistics. These metrics are used to assess a borrower's ability to repay a loan, and the likelihood of repayment. For investors, they are important measures of anticipated default rates and possible foreclosure recoveries in the mortgage pools. In the Offering Materials for every one of the RMBS at issue, Defendants materially misrepresented this critical information and thus grossly understated the riskiness of the mortgage loans that backed these securities.

6. Before filing this suit, AIG conducted an exhaustive forensic investigation of the loan pools underlying the RMBS it purchased to determine the extent of Defendants' misconduct. AIG sampled loans from each RMBS transaction for which data was available. In total, AIG analyzed over 262,000 loans. For each of these loans, AIG analyzed public records, and conducted a retroactive appraisal using an industry leading valuation model and historical data. The results of AIG's forensic investigation are startling:

- *Defendants dramatically understated LTV and CLTV ratios*. On average, 34.27% of the sampled loans actually had LTV ratios more than 10 percentage points higher than what was represented to AIG. Similarly, on average, 44.4% of the sampled loans actually had CLTV ratios more than 10 percentage points higher than what was represented to AIG.

- *In almost every RMBS, Defendants falsely represented that not a single mortgage had an LTV ratio above 100%.* In fact, on average, 16.8% of the mortgage loans in the sampled mortgage pools had LTV ratios above 100%, meaning the loans

exceeded the value of the mortgaged properties themselves and were "underwater" ***from the date of origination***.

- *Defendants grossly misrepresented the properties backing the mortgages as owner-occupied*. It is a well known fact in the mortgage industry that loan default rates on owner-occupied homes are much lower than second or third homes or investment properties. On average, Defendants overstated owner-occupancy by 14.1 percentage points.

- *Defendants' misrepresentations in the Offering Materials were based on false metrics in a staggering 40.2% of the sampled loans*. Of the 262,322 loans tested, 105,568 were inconsistent with one or more of Defendants' metrics by 10 percentage points or more.

The enormity of these numbers demonstrates that Defendants were engaged in a massive scheme to manipulate and deceive investors, like AIG, who had no alternative but to rely on the lies and omissions made by Defendants.

7. The results of AIG's forensic analysis are just the tip of the iceberg. The systemic misrepresentations regarding LTV, CLTV, and owner-occupancy address only a subset, albeit an important subset, of the representations Defendants made concerning the quality of the loan pools. These are the representations that AIG was able to analyze using forensic tools outside of the information in the loan files themselves. A myriad of other key factors that further address the integrity (or lack thereof) of Defendants' loan underwriting process—such as borrowers' income, employment verification, and the supposed compensating factors that were considered in approving "exceptions" to stated guidelines—can only be scrutinized by reviewing the actual loan files. AIG is confident that a review of the complete loan files in discovery will demonstrate that the fraud perpetrated by Defendants was even more rampant than AIG's forensic analysis reveals.

8. Despite multiple requests by AIG, AIG has been unable to gain access to the loan files for nearly all of the RMBS underwritten by Defendants. A sample of loan files in a deal

underwritten by Bank of America and for which AIG has been able to obtain loan files shows that a staggering 82% of the loans did not comply with underwriting guidelines, including examples such as these:

- ***Misrepresentation of Employment***. The borrower stated on the loan application that she was self-employed as a builder for 25 years, earning $35,000 per month, and the co-borrower stated that he was also self-employed as a builder earning $30,000 per month. The borrower also listed on the application that she had been the owner of her building/construction business for 25 years; however, her year of birth was 1971, which would have made the borrower ***10 years old*** when she became the owner of the business. Additionally, the loan file contained letters of incorporation for both the borrower and co-borrower's businesses with inception dates of 9/28/1993 and 2/26/2002, respectively. A reasonably prudent underwriter should have noticed that the age discrepancy was a red flag and questioned the validity of the information contained on the loan application. The loan defaulted.

- ***Misrepresentation of Income***. The borrower stated on the application that she was self-employed as a personal chef with a monthly income of $10,166.67, or $122,000.00 annually. The borrower's tax returns, ***contained in the loan file***, showed a gross income for the entire year of 2007 of $3,126.00 for services as a personal chef, and $27,225 as a self-employed personal assistant. The borrower earned monthly income that was $675 less than the amount of the subject loan mortgage payment in the year following the mortgage closing. The borrower made only one payment on the mortgage, and defaulted.

- ***Misrepresentation of Debt Obligations***. The application failed to disclose that the borrower simultaneously closed on a second mortgage, originated by the ***same lender***, in the ***same condominium*** complex. Public records show that the Borrower acquired a mortgage on the same day as the subject loan for $414,000 with a monthly payment of $4,995 for a property located in Dallas, Texas. The origination underwriter failed to include the monthly payment in the borrower's debt-to-income ratio ("DTI") for the subject loan, resulting in an imprudent underwriting decision. A recalculation of DTI based on the borrower's undisclosed debt, and recalculated income of $1,200 per month, yields a **DTI** of ***1,129.08%***, which exceeds the guideline maximum allowable DTI of 55%. The loan defaulted.

9. Not only did Defendants create RMBS with shoddy loans, but they also engineered unduly positive credit ratings for these securities. Defendants knew that investors like AIG required RMBS to meet stringent credit ratings criteria, and thus duped the rating agencies into rating the senior tranches of these securities AAA. Defendants gave the rating

agencies the same misrepresented data about loan characteristics and underwriting guidelines provided to AIG. The rating agencies analyzed their performance based on the false assumptions Defendants supplied. Because these assumptions understated the risks of the collateral pools, the rating agencies assigned unduly high credit ratings for the securities. Defendants then marketed the RMBS with the inflated ratings and misrepresented in the Offering Materials that the artificially high ratings were an accurate measure of their credit quality based on the misstated collateral pool data.

10. Also misstated in every one of the RMBS at issue were the underwriting guidelines that the lending banks were supposedly following. Both in the Offering Materials and at in-person due diligence meetings with AIG credit research personnel, Defendants represented that the collateral loans were issued pursuant to rational, objective criteria that would assess each borrower's ability to pay and the market value of the underlying properties. Defendants misled AIG into believing that the loans in the pools were issued pursuant to the disclosed underwriting guidelines, when in fact those guidelines had been long abandoned. In fact, the only measure of whether a loan would be approved was whether it could be sold into a securitization.

11. Defendants' abandonment of underwriting practices has been revealed through regulatory and public scrutiny of Defendants' unscrupulous business practices. Investigations by the New York Attorney General, the Securities and Exchange Commission, the U.S. Senate Permanent Subcommittee on Investigations ("SPSI"), and Attorneys General for the states of California, Illinois, Florida, Washington, Indiana, and West Virginia, as well as interviews of Defendants' senior officers and other key employees conducted by the Financial Crisis Inquiry Commission ("FCIC"), have brought to light Defendants' shoddy practices. Just last week, the New York Attorney General filed papers in this Court asserting that Countrywide and Bank of

America face both Martin Act liability and liability for "persistent illegality in the conduct of business" under Executive Law § 63(12) for, among other things, making "repeated false representations in the Governing Agreements [of RMBS] that the quality of the mortgages sold into the Trusts would be ensured" and "repeatedly breaching representations and warranties concerning loan quality."

12. Creating and selling RMBS was an extremely profitable business. Defendants' internal documents, testimony from senior officers and other key employees under oath, as well as confidential interviews of former employees conducted by AIG prior to the filing of this complaint demonstrate that, during the subprime lending "gold rush" years of 2004 to 2007, each of the Defendants—Countrywide, Merrill, and Bank of America—competed fiercely to increase their market share and ratchet up profits from RMBS. In the process, Defendants brought to market hundreds of RMBS sold to AIG collateralized by loan pools that did not come close to satisfying the underwriting guidelines touted in the prospectus supplements.

13. Countrywide was one of the worst offenders. Its own senior officers and internal auditors have ***admitted*** that Countrywide compromised its underwriting integrity for the sake of fueling its profit machine:

- Countrywide Financial's co-founder and CEO, Angelo Mozilo, stated to Wall Street analysts that his goal for Countrywide Financial was to "dominate" the mortgage market and "to get our overall market share to the ultimate 30% by 2006, 2007."

- A former senior regional vice president of Countrywide was quoted in *Business Week* as saying that Countrywide "approached making loans like making widgets, focusing on cost to produce and not risk or compliance. Programs like 'Fast and Easy' where the income and assets were stated, not verified, were open to abuse and misuse. The fiduciary responsibility of making sure whether the loan should truly be done was not as important as getting the deal done."

- In a November 2007 internal report, Countrywide admitted: "We were driven by market share, and wouldn't say 'no' (to guideline expansion). … Market share, size and

dominance were driving themes . . . . Created huge upside in good times, but challenges in today's environment. Net/net it was probably worth it."

14. Countrywide implemented a matching strategy in which it adopted any lending practice of its competitors, no matter how liberal—a practice which resulted in Countrywide offering a dizzying array of toxic loan products. For example:

- In internal e-mails, Mozilo himself characterized Countrywide's new subprime loan products as "toxic," "poison," and "the most dangerous product in existence." Mozilo also observed that there was a "disregard for process [and] compliance with guidelines."

- A former finance executive at Countrywide explained that: "To the extent more than 5 percent of the [mortgage] market was originating a particular product, any new alternative mortgage product, then Countrywide would originate it . . . . [I]t's the proverbial race to the bottom."

- John McMurray, Countrywide's Chief Risk Officer, testified before the SEC that he agreed that whether Countrywide was "ceding our credit policy to the most aggressive players in the market" was a "pretty serious concern."

- In an internal e-mail, Frank Aguilera, a Countrywide Managing Director responsible for risk management, reported that over 23% of the subprime loans at the time were generated as exceptions, even taking into account "all guidelines, published and not published, approved and not yet approved." Aguilera wrote that "[t]he results speak toward our inability to adequately impose and monitor controls on production operations."

15. Though touting Countrywide's adherence to underwriting guidelines publicly, Countrywide senior officers internally admitted that "saleability"—that is, whether Countrywide could sell the loan on the secondary market, rather than compliance with underwriting guidelines—became the sole factor governing whether a loan would be approved:

- In his testimony to the SEC, David Sambol, Countrywide Home Loans' President and Chief Operating Officer, identified a February 13, 2005 e-mail he wrote that said that "our pricing philosophy" should be expanded so that "we should be willing to price virtually any loan that we reasonably believe we can sell/securitize without losing money, even if other lenders can't or won't do the deal."

- In an internal e-mail, Countrywide's Executive Vice President of Credit Risk Management, Christian Ingerslev, asked "should the line in the sand still be 'unsaleable'? After looking at the performance, it's hard to recommend anything other than no.

Heretofore that has been a challenging edict for Credit to implement (for obvious reasons) and the outcry is to just price the risk - regardless of performance."

16. Countrywide's senior management *knew* that its loan origination guidelines were not being followed and that Countrywide was making loans that carried a high—and undisclosed—probability of default:

- In a May 22, 2005 internal e-mail, Chief Risk Officer McMurray warned President and COO Sambol that "exceptions are generally done at terms even more aggressive than our guidelines" and recommended that "[g]iven the expansion in guidelines and the growing likelihood that the real estate market will cool, this seems like an appropriate juncture to revisit our approach to exceptions." He continued: "As a consequence of [Countrywide's] strategy to have the widest product line in the industry, we are clearly out on the 'frontier' in many areas," adding that that "frontier" had "high expected default rates and losses."

- In the same e-mail thread, McMurray told Sambol that the company could face liability for its faulty underwriting practices and misrepresentations to investors: "We've sold much of the credit risk associated with high risk transactions away to third parties. *Nevertheless, we will see higher rates of default on the riskier transactions and third parties coming back to us seeking a repurchase or indemnification based on an alleged R[epresentation] & W[arranty] breach as the rationale.*" (Emphasis added).

- In a February 11, 2007 e-mail to Sambol, McMurray reiterated his concerns, stating: "I doubt this approach would play well with regulators, investors, rating agencies, etc. To some, this approach might seem like we've simply ceded our risk standards . . . to whoever has the most liberal guidelines."

- McMurray also testified before the SEC that he was aware that there were instances where his credit risk department "reject[ed] proposals for new products and the people in sales nevertheless used the exceptions procedure to achieve the same result."

- In an internal report forwarded to CEO Mozilo, Countrywide admitted that "borrower repayment capacity was not adequately assessed by the bank during the underwriting process for home equity loans" for mortgages originated by Countrywide in 2006 and 2007.

17. Moreover, Countrywide's own diligence demonstrated that the loans it was pooling failed the criteria, but Countrywide ignored the results of its own analysis. Documents recently disclosed by the FCIC show that Countrywide retained the third-party due diligence firm Clayton Holdings, Inc. ("Clayton") to analyze the loans it was considering placing in its

securitizations. Clayton's reports reveal that from the fourth quarter of 2006 to the first quarter of 2007, ***26% of the mortgages Countrywide submitted to Clayton for review were rejected as outside underwriting guidelines.*** Of the mortgages that Clayton found defective, 12% were subsequently ***"waived in"*** by Countrywide and included in securitizations like the ones in which AIG invested. Clayton's reports also include statistics on loans originated by Countrywide and submitted to Clayton for review, including Countrywide loans that were sold on the secondary market and included in non-Countrywide securitizations. During the same time period, Clayton found that between 13% and 24% of those loans were outside underwriting guidelines.

18. Merrill Lynch also systematically departed from its stated underwriting guidelines. Like Countrywide, starting in 2004, Merrill took aggressive action to climb to the top of the RMBS pile. In return for a guaranteed stream of mortgage loans for its securitizations, Merrill began offering "warehouse" financing to originating banks, which the lenders used to originate subprime mortgages, at little to no cost. At the same time, Merrill adopted liberal standards regarding the type of mortgage loans it was willing to acquire. In 2005, Merrill purchased a stake in subprime lender Ownit Mortgage Solutions, Inc. in order to control the stream of mortgage loans it could pool and then sell. In 2006, Merrill announced plans to buy another subprime lender, First Franklin. In his book on the financial crisis, David Faber summarized Merrill's RMBS business strategy in no uncertain terms: "[Merrill] wanted to originate more mortgages, buy more mortgages, package more mortgages into securities, and package more of those securities into CDOs [collateralized debt obligations]. And of course, it wanted to sell those securities and CDOs as fast as it possibly could, because that's where the money was."

19. Intense industry competition led Merrill to loosen underwriting guidelines and to make as many loans as possible appear to pass muster under those guidelines. Merrill encouraged subprime lenders—including its own affiliates—to originate more low- and no-documentation loans. These types of loans were frequently referred to as "liar loans" within the mortgage industry because of the frequency with which borrowers lied on their applications, often with the originators' knowledge or active assistance. Merrill knew from its experience with loan securitization that "liar loans" were plagued by fraud, but it encouraged its affiliates and other subprime lenders to generate these loans anyway in order to increase loan volume and the price it could obtain for RMBS. Indeed, William Dallas, the chief executive of Ownit, stated that Merrill paid Ownit a greater amount for no-income verification loans than for full-documentation loans.

20. Confidential witnesses interviewed by AIG prior to the filing of this complaint revealed that Merrill's origination arms, Ownit and First Franklin, abandoned their underwriting guidelines to fuel Merrill's securitization machine. For example, a former senior underwriter at Ownit told AIG that Ownit loan officers themselves were falsely inflating incomes and ***"fudging the numbers"*** to get stated income loans approved. This same former employee said that, at Ownit, the appraisal process was "owned by the loan officers" who enjoyed "a cozy relationship" with the appraisers. She stated that ***"excessive adjustments"*** were made to inflate appraisals and these adjustments were never challenged. A former underwriter at First Franklin stated that some of the lending practices at First Franklin were ***"basically criminal"*** and that First Franklin required its underwriters to depart from stated underwriting guidelines in a way "that we did not agree with, but had to do" in order to keep their jobs. When she and another former underwriter "spoke out" about the problematic lending practices taking place at First

Franklin, they were both ***fired*** for attempting to "blow the whistle" on First Franklin's problematic lending practices. Another former First Franklin underwriter disclosed to AIG that if an underwriter rejected a loan because did not meet underwriting criteria, her manager would re-direct the loan application to a certain loan processor who would ***"sign behind your back."***

21. Merrill issued RMBS with loans that it knew failed to meet stated guidelines. Like Countrywide, it conducted its own due diligence that revealed that loans it purchased from originators failed to meet disclosed underwriting standards. Merrill also retained Clayton to perform due diligence. ***Clayton found that 23% of the loans it reviewed for Merrill "failed to meet guidelines."*** The loans had been granted despite the lack of any purported compensating factors justifying an exception. Yet Merrill "waived in" to its pools 32% of the toxic loans that Clayton identified as being outside the guidelines and sold them to investors like AIG.

22. Merrill's former CEO John Thain summed up Merrill's problem when he commented in a September 2010 interview: "[W]hen you have a system where you pay someone for originating mortgages simply on volume and nothing happens to them if the credit quality is bad, and nothing happens to them if the borrower is fraudulent on his loan application, and nothing happens to him if the appraisal's fraudulent, then that's probably not a very smart system." This was precisely the system Merrill used to originate or acquire loans, securitize them into RMBS, and sell the securities to AIG and other unsuspecting investors.

23. Bank of America also departed from its own underwriting standards in order to keep pace with the market and to guarantee mortgage loans for its own securitizations. Bank of America was an aggressive competitor on the mortgage market, offering products that other lenders could not beat. Indeed, in an internal Countrywide e-mail, Mozilo himself noted Bank of

America's "aggressive move into mortgages" and complained that even Countrywide could not match some of Bank of America's riskier products.

24. Confidential witnesses interviewed by AIG confirmed Bank of America's improper origination and securitization practices. For example, one former employee revealed that Bank of America loan officers themselves inflated borrower income and ***"doctored the numbers"*** to get stated income loans approved. Another former Bank of America loan processor divulged that when borrowers accidentally submitted documentation for stated income loans that directly contradicted the income claimed by the borrowers, management told the loan processors to simply ignore the documentation: ***"we didn't have to consider evidence"*** that directly contradicted borrowers' claims about their income. And according to yet another former employee, loan officers would often call appraisers and tell them ***"I need you to come in at this amount."*** The appraisers would then return with the requested valuation. A confidential witness also revealed to AIG that Bank of America diverted severely credit-blemished loan applicants to its so-called "Plan C" group, which employed ***alternative underwriting criteria*** to approve and fund loans. The "Plan C" group had wide latitude to grant exceptions to Bank of America's stated underwriting guidelines, and the group's mandate was to find ways to fund loans that otherwise would be rejected—loans that one former Bank of America employee believed ***"should not have been funded under any circumstances."***

25. Clayton, which Bank of America also retained to perform due diligence, informed Bank of America that ***30% of the loans it reviewed were defective.*** But Bank of America nevertheless "waived in" 27% of these toxic loans and included them in securitizations. Another confidential witness—a former Clayton employee—told AIG that Bank of America was not actually interested in the fundamental credit quality of the loans reviewed during Bank of

America's due diligence process. Instead, this former Clayton employee revealed that a Vice President of Structured Products at Bank of America specifically told him that he "***didn't give a flying f*** about DTI*** [debt-to-income ratios]" and other credit characteristics of the loans being reviewed. The Bank of America VP told this former Clayton employee that, ***"we [Bank of America] can sell [the loans] to whoever"*** and ***"we [Bank of America] can sell [the loans] down the line."***

26. These facts are only illustrative of Defendants' pattern of misconduct, which is discussed in further detail below. Defendants' misconduct can be explained quite simply. Countrywide, Merrill, and Bank of America did not tell AIG the truth about the loans that collateralized the securities. AIG reviewed and relied on the misleading misrepresentations about loan characteristics, favorable ratings, and embellished underwriting practices. It would not have purchased these securities had it known the truth. As a result, AIG lost over $10 billion.

PARTIES

27. ***The Plaintiffs.*** Plaintiff American International Group, Inc. ("AIG Parent" and, together with its subsidiaries, "AIG") is an international insurance organization. Plaintiffs purchased the RMBS at issue as identified in Exhibit A.

28. AIG Parent is a Delaware corporation with its principal place of business at 180 Maiden Lane, New York, New York, 10038. AIG Parent was a purchaser of certain of the RMBS at issue.

29. Plaintiff AIG Securities Lending Corporation (f/k/a AIG Global Securities Lending Corporation) ("AIG GSL Corp.") is an indirect, wholly-owned subsidiary of AIG Parent. It is a Delaware corporation with its principal place of business in New York, New York. AIG GSL Corp. purchased certain of the RMBS at issue as part of AIG's securities lending

program (the "Global Securities Lending" or "GSL" program). Under the GSL program, AIG GSL Corp. loaned securities owned by various AIG subsidiaries to financial institutions. AIG GSL Corp. then received cash collateral from these borrowers and invested it in fixed income securities, primarily RMBS.

30. Beginning on September 28, 2007, AIG Parent entered into a series of make whole agreements and made payments to offset losses in AIG GSL Corp.'s investment pool. Upon making these payments, AIG Parent became equitably subrogated to all of the respective rights and remedies of AIG GSL Corp. with respect to these RMBS-related losses.

31. Plaintiff American General Assurance Company is an indirect, wholly-owned subsidiary of AIG Parent engaged in the business of selling life insurance in the United States. It is an Illinois corporation with its principal offices in Houston, Texas.

32. Plaintiff American General Life and Accident Insurance Company sells life insurance, annuity, and accident and health products to American consumers. It is a Tennessee corporation, has its principal offices in Nashville, Tennessee, and is an indirect, wholly-owned subsidiary of AIG Parent.

33. Plaintiff American General Life Insurance Company is an indirect, wholly-owned subsidiary of AIG Parent engaged in the business of selling life insurance to American consumers. It is a Texas corporation with its principal offices in Houston, Texas.

34. Plaintiff American General Life Insurance Company of Delaware offers life insurance, fixed annuities, accident and health products, and worksite benefits to consumers in the United States. It is a Delaware corporation, has its principal offices in Houston, Texas, and is an indirect, wholly-owned subsidiary of AIG Parent.

35. Plaintiff American Home Assurance Company is a New York corporation with its principal offices at 175 Water Street, New York, New York, 10038. It provides property and casualty insurance products to businesses, including public entities, educational institutions, and transportation and construction companies. It is an indirect, wholly-owned subsidiary of AIG Parent.

36. Plaintiff American International Group Retirement Plan is a retirement plan for AIG's employees. The plan is administered in New York.

37. Plaintiff Chartis Property Casualty Company is a Pennsylvania corporation with principal offices at 175 Water Street, New York, New York, 10038. It provides property and casualty lines of insurance and is an indirect, wholly-owned subsidiary of AIG Parent.

38. Plaintiff Chartis Select Insurance Company is a Delaware corporation with principal offices in New York, New York. It provides excess casualty and financial insurance and is an indirect, wholly-owned subsidiary of AIG Parent.

39. Plaintiff Chartis Specialty Insurance Company is an Illinois corporation with principal offices in New York, New York. It offers property and casualty insurance and is an indirect, wholly-owned subsidiary of AIG Parent.

40. Plaintiff Commerce and Industry Insurance Company is a New York corporation with principal offices at 70 Pine Street, New York, New York, 10270. It offers insurance brokerage services and is an indirect, wholly-owned subsidiary of AIG Parent.

41. Plaintiff First SunAmerica Life Insurance Company is a New York corporation with principal offices in New York, New York. It provides tax-deferred annuities for retirement savings through financial institutions, and is an indirect, wholly-owned subsidiary of AIG Parent.

42. Plaintiff Lexington Insurance Company is a surplus lines insurer. It is a Delaware corporation with principal offices in Boston, Massachusetts, and is an indirect, wholly-owned subsidiary of AIG Parent.

43. Plaintiff National Union Fire Insurance Company of Pittsburgh, Pa. is a Pennsylvania corporation with its principal offices at 175 Water Street, New York, New York, 10038. It is an insurance company and an indirect, wholly-owned subsidiary of AIG Parent.

44. Plaintiff New Hampshire Insurance Company provides property and casualty insurance services. Founded in 1869, it is a Pennsylvania corporation with principal offices at 175 Water Street, New York, New York, 10038. It is an indirect, wholly-owned subsidiary of AIG Parent.

45. Plaintiff SunAmerica Annuity and Life Assurance Company is an issuer of variable annuities. It is an Arizona corporation, has its principal offices in Phoenix, Arizona, and is an indirect, wholly-owned subsidiary of AIG Parent.

46. Plaintiff SunAmerica Life Insurance Company is an indirect, wholly-owned subsidiary of AIG Parent engaged in the business of selling life insurance. It is an Arizona corporation with its principal offices in Los Angeles, California.

47. Plaintiff The Insurance Company of the State of Pennsylvania is an insurance company incorporated in Pennsylvania, with its principal offices at 175 Water Street, New York, New York, 10038. It is an indirect, wholly-owned subsidiary of AIG Parent.

48. Plaintiff The United States Life Insurance Company in the City of New York ("USL") is a New York insurance company incorporated in New York in 1850. USL's principal offices are at One World Financial Center, 200 Liberty Street, New York, New York, 10281 and it is an indirect, wholly-owned subsidiary of AIG Parent.

49. Plaintiff The Variable Annuity Life Insurance Company is a financial services company. It is a Texas corporation, has its principal offices in Houston, Texas, and is an indirect, wholly-owned subsidiary of AIG Parent.

50. Plaintiff Western National Life Insurance Company is a life insurance company. It is a Texas corporation, has its principal offices in Amarillo, Texas, and is an indirect, wholly-owned subsidiary of AIG Parent.

51. ***The Defendants.*** All of the Defendants in this action are now subsidiaries of Bank of America Corporation, including some entities that were acquired by certain Defendants by reason of a sale or transfer of all or a portion of its assets.

52. ***The Countrywide Defendants***. Defendant Countrywide Financial Corporation is a corporation organized under the laws of the State of Delaware with its principal executive offices in Calabasas, California. Countrywide Financial Corporation, itself and through its subsidiaries, engaged in mortgage lending and other real estate finance-related businesses, including mortgage lending, securities dealing, and insurance underwriting. It was the corporate parent of all of the Countrywide Defendants. Pursuant to a transaction completed on July 1, 2008, Countrywide Financial was merged into a subsidiary of Bank of America Corporation. As of April 27, 2009, Countrywide Financial ceased operating under the brand name Countrywide. Now combined with Bank of America's pre-existing mortgage and home loan business, Countrywide Financial's main businesses operate as Bank of America Home Loans, a division of Bank of America. It acted as the seller for certain of the offerings at issue, as detailed in Exhibits 1 to 349. It is a Seller Defendant.

53. Defendant Countrywide Capital Markets LLC, a wholly-owned subsidiary of Countrywide Financial Corporation, is a corporation organized under the laws of the State of

California with its principal place of business in Calabasas, California. Countrywide Capital Markets operated through its two main wholly-owned subsidiaries, Defendant Countrywide Securities Corporation and Countrywide Servicing Exchange.

54. Defendant Countrywide Home Loans, Inc., a wholly-owned subsidiary of Countrywide Financial Corporation, is a corporation organized under the laws of the State of New York with its principal place of business in Calabasas, California. It acted as the sponsor, seller, and/or loan originator for certain of the offerings at issue, as detailed in Exhibits 1 to 349. It is a Sponsor, Seller, and Originator Defendant.

55. Defendant Countrywide Bank, N.A. (a/k/a Countrywide Bank, F.S.B.) was a federal savings bank with its principal place of business in Alexandria, Virginia and operated as a subsidiary of Countrywide Financial Corporation. In 2008, it became a subsidiary of Bank of America Corporation. In 2009, it merged with Bank of America, N.A, which is a wholly-owned subsidiary of Bank of America Corporation. As a result of this merger, Defendant Bank of America, N.A. assumed all of the liabilities of Countrywide Bank, N.A., and therefore Bank of America N.A. is liable for the wrongful acts of Countrywide Bank, N.A., as alleged herein. Countrywide Bank, N.A. acted as the loan originator for certain of the offerings at issue, as detailed in Exhibits 1 to 349. It is an Originator Defendant.

56. Defendant Countrywide Securities Corporation is a corporation organized under the laws of the State of California, with its principal place of business in Calabasas, California. It operated as a subsidiary of Countrywide Financial Corporation. Countrywide Securities Corporation was the underwriter for certain of the offerings at issue, as detailed in Exhibits 1 to 349. It is an Underwriter Defendant.

57. Defendant CWABS, Inc. is a Delaware corporation and a limited purpose finance subsidiary of Countrywide Financial Corporation with its principal place of business in Calabasas, California. It is an indirect, wholly-owned subsidiary of Bank of America Corporation. CWABS, Inc. was the depositor for certain of the offerings in which AIG invested, the registrant for certain Registration Statements filed with the SEC, and an issuer of certain mortgage-backed certificates purchased by AIG, as detailed in Exhibits 1 to 349. The depositor is considered the issuer of the certificates within the meaning of Section 2(a)(4) of the Securities Act of 1933, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a), 15 U.S.C. § 77k(a). It is a Depositor Defendant.

58. Defendant CWALT, Inc. is a Delaware corporation and a limited purpose finance subsidiary of Countrywide Financial Corporation with its principal place of business in Calabasas, California. It is an indirect, wholly-owned subsidiary of Bank of America Corporation. CWALT, Inc. was the depositor for certain of the offerings in which AIG invested, the registrant for certain Registration Statements filed with the SEC, and an issuer of certain mortgage-backed certificates purchased by AIG, as detailed in Exhibits 1 to 349. The depositor is considered the issuer of the certificates within the meaning of Section 2(a)(4) of the Securities Act of 1933, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a), 15 U.S.C. § 77k(a). It is a Depositor Defendant.

59. Defendant CWHEQ, Inc. is a Delaware corporation and a limited purpose finance subsidiary of Countrywide Financial Corporation with its principal place of business in Calabasas, California. It is an indirect, wholly-owned subsidiary of Bank of America Corporation. CWHEQ, Inc. was the depositor for certain of the offerings in which AIG invested, the registrant for certain Registration Statements filed with the SEC, and an issuer of certain

mortgage-backed certificates purchased by AIG, as detailed in Exhibits 1 to 349. The depositor is considered the issuer of the certificates within the meaning of Section 2(a)(4) of the Securities Act of 1933, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a), 15 U.S.C. § 77k(a). It is a Depositor Defendant.

60. Defendant CWMBS, Inc. is a Delaware corporation and a limited purpose finance subsidiary of Countrywide Financial Corporation with its principal place of business in Calabasas, California. It is an indirect, wholly-owned subsidiary of Bank of America Corporation. CWMBS, Inc. was the depositor for certain of the offerings in which AIG invested, the registrant for certain Registration Statements filed with the SEC, and an issuer of certain mortgage-backed certificates purchased by AIG, as detailed in Exhibits 1 to 349. The depositor is considered the issuer of the certificates within the meaning of Section 2(a)(4) of the Securities Act of 1933, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a), 15 U.S.C. § 77k(a). It is a Depositor Defendant.

61. ***The Merrill Defendants*.** Merrill Lynch & Co., Inc. purports to be a leading global trader and underwriter of securities and derivatives across a broad range of asset classes and a strategic advisor to corporations, governments, institutions and individuals worldwide. It was the underwriter for certain of the offerings at issue, as detailed in Exhibits 1 to 349. Merrill Lynch & Co., Inc. is a Delaware corporation. During the relevant time frame, Merrill Lynch & Co., Inc.'s principal place of business was New York, New York. On January 1, 2009, Merrill Lynch & Co., Inc. became a wholly-owned subsidiary of Bank of America Corporation. It is an Underwriter Defendant.

62. Defendant Merrill Lynch Mortgage Lending, Inc. is a Delaware corporation with its principal place of business in New York, New York and is a subsidiary of Bank of America

Corporation. It is engaged in the business of, among other things, acquiring residential mortgage loans and selling those loans through securitization programs. It acted as the sponsor and seller for certain of the offerings at issue, as detailed in Exhibits 1 to 349. It also acted as an originator for certain of these offerings through its division, Specialty Underwriting & Residential Finance, as detailed in Exhibits 1 to 349. It is a Sponsor, Seller, and Originator Defendant.

63. Defendant First Franklin Financial Corporation ("First Franklin") is a Delaware corporation with its principal executive offices in San Jose, California. It is a home mortgage lender that specialized in subprime home loans and was acquired by Merrill in December 2006. First Franklin was the sponsor, seller, and/or loan originator for certain of the offerings at issue, as detailed in Exhibits 1 to 349. It is now a subsidiary of Bank of America Corporation. It is a Sponsor, Seller, and Originator Defendant.

64. Defendant Merrill Lynch Mortgage Capital Inc. is a Delaware corporation with its principal executive offices in New York, New York, and is a subsidiary of Bank of America Corporation. It acted as the seller for certain of the offerings at issue, as detailed in Exhibits 1 to 349. It is a Seller Defendant.

65. Defendant Merrill Lynch Credit Corporation is a Delaware corporation with its principal executive offices in Jacksonville, Florida. It was the originator for certain of the offerings at issue, as detailed in Exhibits 1 to 349, and is now a subsidiary of Bank of America Corporation. It is an Originator Defendant.

66. Defendant Merrill Lynch, Pierce, Fenner & Smith Inc. ("MLPF&S") is a Delaware corporation and registered broker-dealer and investment advisor with its principal place of business in New York, New York. MLPF&S acted as an underwriter for certain of the

offerings at issue, as detailed in Exhibits 1 to 349. On January 1, 2009, it became a wholly-owned subsidiary of Bank of America Corporation. It is an Underwriter Defendant.

67. Defendant Merrill Lynch Mortgage Investors, Inc. is a Delaware corporation with its principal place of business in New York, New York. It is a subsidiary of Bank of America Corporation. Merrill Lynch Mortgage Investors, Inc. was the depositor for certain of the offerings at issue here, the registrant for certain Registration Statements filed with the SEC, and the issuer for certain of the offerings at issue in this action, as detailed in Exhibits 1 to 349. The depositor is considered the issuer of the certificates within the meaning of Section 2(a)(4) of the Securities Act of 1933, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a), 15 U.S.C. § 77k(a). It is a Depositor Defendant.

68. ***The Bank of America Defendants*.** Defendant Bank of America Corporation purports to be one of the world's largest financial institutions, serving individual consumers, small-and-middle-market businesses, large corporations and governments with a full range of banking, investing, asset management and other financial and risk management products and services. It is a Delaware corporation with substantial business operations and offices at the Bank of America Tower at One Bryant Park, New York, New York 10036. Every defendant named in this action is a subsidiary of Bank of America Corporation.

69. Defendant Banc of America Securities LLC ("BAS"), a wholly-owned broker-dealer subsidiary of Bank of America Corporation, acted as the underwriter for certain of the deals at issue, as detailed in Exhibits 1 to 349. BAS was a Delaware limited liability corporation with its principal place of business in New York, New York. On November 1, 2010, BAS merged into MLPFS, with MLPF&S as the surviving corporation. As a result of this merger, MLPF&S remained a direct wholly-owned broker-dealer subsidiary of ML & Co. and an indirect

wholly-owned broker-dealer subsidiary of Bank of America Corporation. It is an Underwriter Defendant.

70. Defendant Bank of America, National Association is a nationally-chartered United States bank with substantial business operations and offices at the Bank of America Tower at One Bryant Park, New York, New York 10036. It acted as a sponsor, seller and loan originator for certain of the offerings at issue, as detailed in Exhibits 1 to 349. It is a wholly-owned subsidiary of Bank of America Corporation. It is a Sponsor, Seller, and Originator Defendant.

71. Defendant Banc of America Funding Corporation is a Delaware corporation with substantial business operations and offices at the Bank of America Tower at One Bryant Park, New York, New York 10036, and is a subsidiary of Bank of America Corporation. Banc of America Funding Corporation was the depositor for certain of the offerings at issue here, the registrant for certain Registration Statements filed with the SEC, and the issuer for certain of the offerings at issue in this action, as detailed in Exhibits 1 to 349. The depositor is considered the issuer of the certificates within the meaning of Section 2(a)(4) of the Securities Act of 1933, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a), 15 U.S.C. § 77k(a). It is a Depositor Defendant.

72. Defendant Banc of America Mortgage Securities, Inc. is a Delaware corporation with substantial business operations and offices at the Bank of America Tower at One Bryant Park, New York, New York 10036, and is a subsidiary of Bank of America Corporation. Banc of America Mortgage Securities, Inc. was the depositor for certain of the offerings at issue here, the registrant for certain Registration Statements filed with the SEC, and the issuer for certain of the offerings at issue in this action, as detailed in Exhibits 1 to 349. The depositor is considered

the issuer of the certificates within the meaning of Section 2(a)(4) of the Securities Act of 1933, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a), 15 U.S.C. § 77k(a). It is a Depositor Defendant.

73. Defendant Asset Backed Funding Corporation is a Delaware corporation with substantial business operations and offices at the Bank of America Tower at One Bryant Park, New York, New York 10036, and is a subsidiary of Bank of America Corporation. It was the depositor for certain of the offerings at issue here, the registrant for certain Registration Statements filed with the SEC, and the issuer for certain of the offerings at issue in this action, as detailed in Exhibits 1 to 349. The depositor is considered the issuer of the certificates within the meaning of Section 2(a)(4) of the Securities Act of 1933, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a), 15 U.S.C. § 77k(a). It is a Depositor Defendant.

74. Defendant NB Holdings Corporation is a Delaware corporation with principal offices in Charlotte, North Carolina, and is a subsidiary of Bank of America Corporation.

75. Defendants Bank of America Corporation, Bank of America, N.A., and NB Holdings Corporation participated in Bank of America's acquisition of substantially all of Countrywide Financial Corporation through a series of acquisitions and shares that commenced on July 1, 2008. They are the successors-in-interest to the Countrywide Defendants.

76. At all relevant times, Defendants committed the acts, caused or directed others to commit the acts, or permitted others to commit the acts alleged in this Complaint. Any allegations about acts of the corporate Defendants means that those acts were committed through their officers, directors, employees, agents, and/or representatives while those individuals were acting within the actual or implied scope of their authority.

JURISDICTION AND VENUE

77. This Court has jurisdiction over this proceeding pursuant to CPLR §§ 301 and 302. Almost all activity pertaining to the securitization of the mortgage loans at issue occurred in New York, including the underwriting, negotiating, drafting, and signing of the operative agreements, the formation of the trusts, and the compilation and transmission of the Offering Materials. Each of the Defendants also maintains offices, derives substantial revenue from, and/or regularly transacts or have transacted business within the State.

78. Venue is proper in this Court pursuant to CPLR § 503. American International Group, Inc. is a resident of New York County, New York.

BACKGROUND

I. THE MECHANICS OF MORTGAGE SECURITIZATION

79. RMBS take the form of mortgage "certificates." The certificates represent interests in a pool of mortgage loans; they are "shares" in the pool that are sold to investors. The certificates entitle the holder to payments from the pool of mortgages. Although the structure and underlying collateral may vary by offering, the basic principle of pass-through certificates remains the same: as borrowers make payments on the loans in the mortgage pool, that cash flow is "passed through" to the certificate holders based on their share of the pool.

80. The "sponsor" for the securities (also typically referred to as the "seller" prior to the year 2006) puts together the transaction. The sponsor originates the loans or acquires the loans from other mortgage originators. Then a "depositor" acquires an inventory of loans from the "sponsor" or "seller." The types of loans in the inventory may vary, including conventional, fixed-rate or adjustable-rate mortgage loans (or mortgage participations), secured by first liens, junior liens, or a combination of first and junior liens, with various lifetimes to maturity. Upon acquisition, the depositor transfers, or deposits, the acquired pool of loans to an "issuing trust."

81. The issuing trust then "securitizes" the pool of loans so that the rights to the cash flows from the pool can be sold to investors in the form of certificates. The securitization transactions are structured such that the risk of loss is divided among different levels of investment, or "tranches." Any losses on the underlying loans - whether due to default or otherwise - are generally applied in reverse order of seniority. As such, the most senior tranches of certificates receive the highest credit ratings. Junior tranches, being less insulated from risk, typically obtain lower credit ratings, but offer greater potential returns.

82. Once the tranches are established, the issuing trust passes the securities or certificates back to the depositor, who becomes the issuer of the securities. The depositor then passes the securities to one or more underwriters, who market and sell the securities to investors.

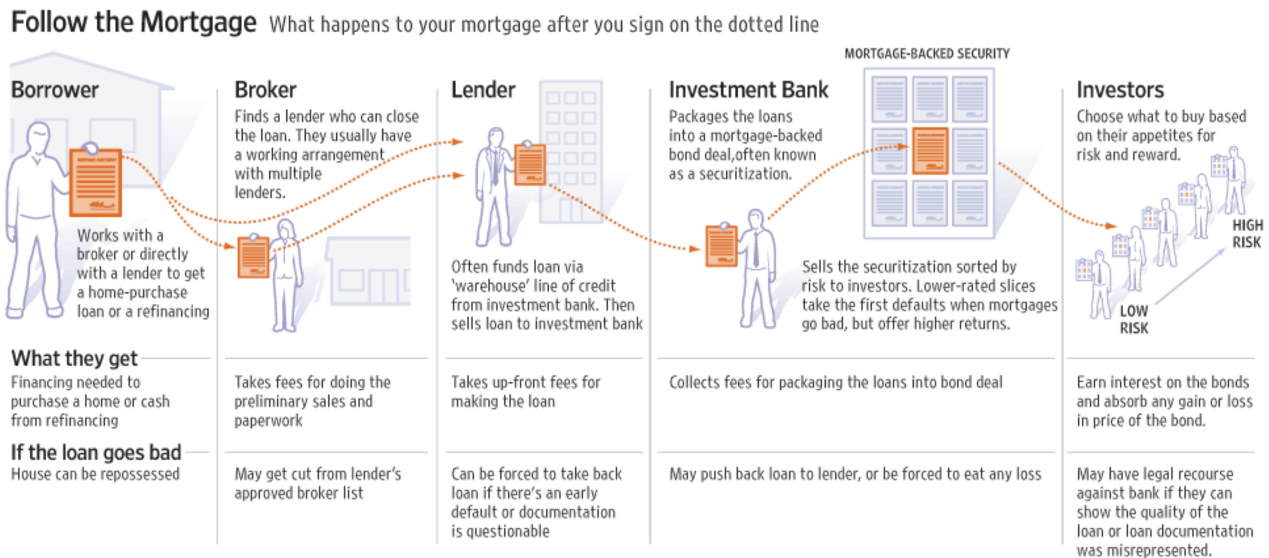
83. The underwriters, often Wall Street banks and financial institutions, play a critical role in the securitization process by purchasing the securities from the issuing trust through a depositor and then selling them to investors. Significantly, the underwriters directly provide the information that potential investors like AIG use to decide whether to purchase the securities.

84. Because the cash flow from the loans in the collateral pool of a securitization is the source of payments to holders of the securities issued by the trust, the credit quality of the securities depends directly upon the credit quality of the loans in the collateral pool. The most important information about the credit quality of the loans is contained in the "loan files" that the mortgage originator develops while making the loans. For residential mortgage loans, each loan file normally contains documents including the borrower's application for the loan; verification of the borrower's income, assets, and employment; references; credit reports on the borrower; an appraisal of the property that will secure the loan and provide the basis for measures of credit quality, such as loan-to-value ratios; and a statement of the occupancy status of the property.

85. The collateral pool for each securitization usually includes thousands of loans. Instead of having each potential investor go through what would be an impractical, inordinately expensive and time consuming task of reviewing thousands of loan files, the underwriters were generally responsible for gathering loan data from the sponsor, seller, and originators, and then verifying and presenting to potential investors accurate and complete information about the loans that are deposited into the issuing trust. Here, information about loan characteristics was provided to AIG by Defendants through a variety of offering materials, including term sheets, prospectus supplements, free writing prospectuses and in response to AIG's specific requests for data. In addition, AIG conducted in-person meetings with Defendants to assess their underwriting standards.

86. Before the RMBS was issued, Defendants also provided the rating agencies with information about loan characteristics and the deal structure. Relying on this information, the ratings agencies assigned each tranche of a securitization a credit rating reflecting their assessment of its risk. The offering materials used to market and sell the securities to investors like AIG disclosed these ratings. The credit ratings were an important tool for many investors, including AIG, to assess risk. Indeed, AIG GSL Corp's investment policy required 95% of its asset-backed investments to be AAA rated.

87. The *Wall Street Journal* has summarized the securitization process as follows:



II. THE RAPID EXPANSION OF MORTGAGE SECURITIZATION TRANSFORMS THE INDUSTRY

88. Traditionally, mortgage originators financed their mortgage business through customer deposits, retained ownership of the loans they originated, and directly received the mortgage payment streams. This became known as the "originate to hold" model. When an originator held a mortgage through the term of the loan, the originator also bore the risk of loss if the borrower defaulted and the value of the collateral was insufficient to repay the loan. As a result, the originator had a strong economic incentive to verify the borrower's creditworthiness through prudent underwriting and to obtain an accurate appraisal of the value of the underlying property before making the mortgage loan.

89. In the 1980s and 1990s, most mortgage securitizations were conducted through the major Government Sponsored Enterprises (the "Agencies"), *i.e.*, the Federal National Mortgage Association ("Fannie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac"), and the Government National Mortgage Association ("Ginnie Mae"). The Agencies

purchased loans from originators and securitized the loans. These Agency securitizations had high credit quality because the Agencies required the underlying loans to be originated in accordance with strict underwriting guidelines.

90. In the 2000s, the volume of non-Agency mortgage securitizations skyrocketed, led by the Wall Street investment banks. Mortgage loan securitization shifted the traditional "originate to hold" model to an "originate to distribute" model, in which originators sold the mortgages and transferred credit risk to investors through the issuance and sale of RMBS. Under the new model, the economic incentives are radically shifted because the originators no longer hold the mortgage loans to maturity. Instead, by selling the mortgages to investors, the originators obtain the funds to make more loans. Securitization also enables originators to earn most of their income from transaction and loan-servicing fees, rather than from the spread between interest rates paid on deposits and interest rates received on mortgage loans, as in the traditional model.

91. Thus, securitization gives originators an incentive to increase the number of mortgages they issue and reduces their incentive to ensure the mortgages' credit quality. As the SPSI found: "When lenders kept on their books the loans they issued, the creditworthiness of those loans determined whether the lender would turn a profit. Once lenders began to sell or securitize most of the loans, volume and speed, as opposed to creditworthiness, became the keys to a profitable securitization business." (SPSI Report, at 4.) Nevertheless, contractual terms and good business practices obligate originators to underwrite loans in accordance with their stated policies, obtain accurate information from borrowers to enable them to assess the credit quality of the loans, and obtain accurate appraisals of the mortgaged properties.

III. DEFENDANTS OPERATED ON EVERY LEVEL OF THE SECURITIZATION PROCESS

92. Countrywide, Merrill, and Bank of America operated—and made huge profits—on every level of the securitization process, acting as originators, underwriters, sponsors, sellers, depositors, and servicers in the deals at issue. Indeed, in many of the deals, Defendants acted in multiple, if not all, of these roles (so-called "vertical integration"), allowing them to control the securitization machine and further providing them with actual knowledge of the abuses at each level of the transaction.

93. Defendants adopted multiple strategies in order to gain control of the securitization process. Because they wanted to ensure a steady supply of mortgage loans to securitize, investment banks, who underwrote the deals, often acquired their own loan originators. For example, Merrill acquired First Franklin Financial Corporation ("First Franklin") and a stake in Ownit Mortgage Solutions, Inc. ("Ownit"), both of which were subprime lenders. Controlling a subprime lender allowed an investment bank like Merrill to dictate the underwriting standards at the origination level and guaranteed a constant stream of loans to securitize and sell to investors like AIG. Because Merrill needed high volumes of loans to securitize—and passed off high default risk to investors—it had every inventive to, and in fact did, lower the underwriting standards at its affiliated lenders.

94. The investment banks also engaged in a practice known as "warehouse lending." Under these type of arrangements, investment banks would extend a line of credit to a third-party loan originator to fund a mortgage loan. The warehouse loan typically lasted from the time it was originated to the time when the underlying mortgage loan was sold on the secondary market, whether directly or through a securitization. In connection with this process, the originating banks provided the investment banks with documents about the underlying loans, including

performance characteristics—information that the originators had reason to expect would be relayed to investors like AIG, as they understood the purpose of the sale was to put the loans into a pool for securitization.

95. Both Merrill and Bank of America engaged in warehouse lending. As a result of these close financial ties with otherwise unaffiliated originating lenders, the investment banks had abundant information about the third-party originators' abandonment of publicly disclosed underwriting guidelines and predatory lending practices.

96. Investment banks like Merrill and Bank of America also entered into purchase agreements with third-party originators to buy batches of mortgages to securitize. As part of those agreements, the investment banks typically set the prices and quantities of the types of loans it wanted to buy, and also gained access to loan information prior to purchase.

97. Conversely, Countrywide, a loan originator, formed its own underwriter so it could securitize its loans without paying fees to the Wall Street banks.

98. Moreover, as originators, Countrywide, Merrill, and Bank of America understood and expected that the loans they were generating would end up in securitizations like those purchased by AIG. They provided information regarding collateral loans to the sponsors and underwriters, which they knew and had reason to expect would be distributed to investors like AIG.

99. In many cases, for example, the originator sold its loans directly to the depositor of the securitization and was a party to the pooling and servicing agreement that established the securitization trust. Countrywide-sponsored deals typically reflected this structure. For example, in CWALT 2007-OC2 and CWL 2007-S3, Countrywide Home Loans sold the loans in the mortgage pools to depositors CWALT, Inc. and CWHEQ, Inc., respectively. Countrywide

Home Loans thus knew that its loans were being securitized and sold to investors like AIG, as it played a direct part in building the RMBS.

100. The originators expressly agreed to provide information about their loans to the depositor or sponsor, or more generally to assist with the securitization process, often in agreements that documented the RMBS. For example, First Franklin originated the loans in the mortgage pool for FFML 2006-FFH1 and sold them to Bank of America (the sponsor) pursuant to a Flow Sale and Servicing Agreement. Section 10.01 of that agreement required First Franklin to "use its best efforts to facilitate" any securitization of its loans. Similarly, for BAFC 2006-B, Bank of America, NA originated the loans and sold them to the depositor, Banc of America Funding Corp. pursuant to a Mortgage Loan Purchase Agreement. That purchase agreement stated that Banc of America Funding "will convey the Mortgage Loans to Banc of America Funding 2006-B Trust" pursuant to a pooling and servicing agreement it had already executed. In Section 6, Bank of America, NA expressly "agree[d] to furnish any and all information, documents, certificates, letters or opinions with respect to the mortgage loans, reasonably requested by [Banc of America Funding] in order to perform any of its obligations or satisfy any of the conditions on its part to be performed or satisfied" to complete the underwriting of the securities issued for the deal, and in particular to permit Banc of America Securities to complete and file with the SEC the free writing prospectus used to induce AIG and other investors to purchase the securities.

101. In this way, Defendants gained control of the entire securitization process, giving them unique and special knowledge about every aspect of the process, from loan origination to sale to AIG. The FCIC confirmed that "[s]ecuritization and subprime originations grew hand in hand" as "[t]he nonprime mortgage securitization process created a pipeline through which risky

mortgages were conveyed and sold throughout the financial system. This pipeline was essential to the origination of the burgeoning numbers of high-risk mortgages." (FCIC Report at 70, 125.) The FCIC concluded that:

> [F]irms securitizing mortgages failed to perform adequate due diligence on the mortgages they purchased and at times knowingly waived compliance with underwriting standards. Potential investors were not fully informed or were misled about the poor quality of the mortgages contained in some mortgage-related securities. These problems appear to have been significant.

(FCIC Report, at 187.)

ALLEGATIONS

IV. DEFENDANTS' MATERIAL MISREPRESENTATIONS

A. Defendants' Offering Materials

102. AIG purchased over $28 billion worth of certificates in Defendants' residential mortgage backed securities. The particular RMBS investments at issue in this litigation are set forth in Exhibit A, which lists, among other things, the name, tranche level, purchaser, purchase date, and purchase price for each of these investments.

103. AIG purchased the certificates pursuant to registration statements, prospectuses, prospectus supplements, free writing prospectuses, presentations, term sheets, customized spreadsheets provided upon request of AIG, and other written materials (the "Offering Materials"). The AIG employees responsible for managing Plaintiffs' portfolios and making the purchase decisions for all the RMBS at issue were located in New York, New York. These same employees conducted the due diligence described below.

104. The Offering Materials were prepared by Defendants. Defendants intended for investors like AIG to rely on the Offering Materials, and AIG relied to its detriment on the Offering Materials in making its purchase decisions. The depositors filed a Form S-3 Registration Statement with the SEC indicating its intention to sell mortgage-backed securities.

Exhibits 1 to 349 set forth the date the relevant registration statements were filed with the SEC for the deals at issue.

105. The certificates were issued pursuant to a prospectus. The prospectuses provide that the issuing trusts would offer a series of certificates representing beneficial ownership interests in the related trust, and that the assets of each trust would generally consist of a pool or pools of fixed or adjustable interest rate mortgage loans secured by a lien on a one- to four-family residential property. The prospectuses also advised that a prospectus supplement would be filed with the SEC at the time of the offering of the certificates.

106. The prospectus supplements provided the specific terms of a particular certificate series offering. The prospectus supplements contained a more detailed description of the mortgage pools underlying the certificates, including (but not limited to) the type of loans, the number of loans, the mortgage rates and net mortgage rates, the aggregate scheduled principal balance of the loans, the purported original weighted-average loan-to-value ratio and combined loan-to-value ratio, the borrowers' debt-to-income ratios, the property type, the owner-occupancy data, and the geographic concentration of the mortgaged properties. Exhibits 1 to 349 set forth the date the relevant prospectus supplements were filed with the SEC.

107. Term sheets and free writing prospectuses were also provided to AIG that contained detailed information on the mortgage pools underlying the certificates, such as owner-occupancy statistics, LTV and CLTV ratios, credit ratings, and credit enhancement. Exhibit B provides examples of such term sheets and free writing prospectuses. AIG often directly requested that the underwriter for a security provide additional analytical information about the certificates being offered in customized spreadsheets that AIG had developed to assess the securities. AIG sent the underwriters spreadsheets requesting that the underwriters populate

columns of quantitative data about the collateral loans in the securities. These spreadsheets asked for mortgage loan information on loan terms and loan types, FICO scores, LTV and CLTV ratios, debt-to-income ratios, owner-occupancy levels, and documentation programs. Exhibit C provides an example of this spreadsheet. The quantitative data at issue provided by the Defendants in the term sheets, free writing prospectuses, and the spreadsheets was substantively the same as data provided in the prospectus supplements.

108. In addition, Defendants made representations to AIG, both orally and in writing, when AIG conducted its own diligence of Defendants' loan underwriting processes. AIG visited Defendants' origination arms on site, and questioned their practices using, among other things, a questionnaire AIG developed for such meetings. For example, AIG met with Countrywide in November 2005 and August 2007, and it met with Merrill's originator, First Franklin, in February 2007. At these meetings, Defendants continued to provide false assurances about the quality of the same loan underwriting practices that were misrepresented in the Offering Materials, perpetuating the fiction of a rigorous underwriting process. For example, at one of these due diligence field visits, First Franklin provided a pitchbook to AIG falsely touting First Franklin's alleged robust underwriting practices. In particular, First Franklin represented that it conducted a "full credit underwriting … on all loans prior to funding," and to prevent fraud, it performed "due diligence … on every loan transaction." First Franklin further represented that it conducted "[v]erbal verification of employment on all borrowers regardless of doc type" and had guidelines in place to address "red flags revealed in the loan file." It also represented it had a robust process to manage exceptions and supposedly never gave exceptions based on FICO or LTV. AIG relied on these false assurances in making its investment decisions.

B. Defendants' Misrepresentations Regarding Loan Underwriting Standards and Practices

109. The Offering Materials for each of AIG's certificates describe underwriting guidelines purportedly employed by Defendants to evaluate the underlying mortgage loans. In particular, Defendants misrepresented that, as part of their underwriting process, they had: (i) evaluated the credit standing and repayment ability of prospective borrowers and the value and adequacy of the mortgaged property as collateral; (ii) granted exceptions to the underwriting guidelines only if based on compensating factors; (iii) calculated each borrower's debt-to-income ratio and included in the collateral pool only mortgage loans with a debt-to-income ratio below a threshold level; and (iv) reserved reduced documentation programs for borrowers with excellent credit histories that demonstrated an established ability to repay or ensured that such programs required greater emphasis on other loan characteristics. Defendants also misrepresented that certain loans were eligible for sale to Fannie Mae and Freddie Mac, even though their actual credit characteristics made them ineligible to sell to these entities. Defendants fraudulently omitted to disclose that high numbers of loans had been rejected by the due diligence process, yet "waived" into the collateral pools anyway. Specific misrepresentations for each deal are referenced in Exhibits 1 to 349. Exemplary representations are set forth in Table 1 below.

110. The underwriting process used to originate the mortgage loans underlying AIG's certificates was material to AIG and an important factor in its decision to purchase securities from a particular sponsor or including loans from a particular originator because the underwriting process is designed to ensure loan quality. Loan quality in turn determines the risk of the certificates. If underwriting guidelines are not actually followed, then the underlying loans will be of lesser quality than represented, increasing the probability of defaults by borrowers and shortfalls in principal and interest payments to investors. A systemic underwriting failure

decreases the reliability of *all* the information investors have about the loans, and thus greatly increases their perceived and actual risk, and greatly decreases the market value of the certificates for which such loans comprise the collateral.

111. Defendants' statements regarding underwriting standards and practices were untrue and misleading because they had abandoned these standards, as set forth in detail in Section V.E.

Table 1: Sample Misrepresentations Regarding Underwriting Guidelines

Defendant	**Misrepresentations**
Countrywide	• "All of the Mortgage Loans originated by Countrywide Home Loans have been underwritten pursuant to Countrywide Home Loans' Standard Underwriting Guidelines." CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006 at S-50. • "Countrywide Home Loans' underwriting standards are applied by or on behalf of Countrywide Home Loans to evaluate the prospective borrower's credit standing and repayment ability and the value and adequacy of the mortgaged property as collateral. Under those standards, a prospective borrower must generally demonstrate that the ratio of the borrower's monthly housing expenses (including principal and interest on the proposed mortgage loan and, as applicable, the related monthly portion of property taxes, hazard insurance and mortgage insurance) to the borrower's monthly gross income and the ratio of total monthly debt to the monthly gross income (the 'debt-to-income' ratios) are within acceptable limits." CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006 at S-47. • "As part of its evaluation of potential borrowers, Countrywide Home Loans generally requires a description of income. If required by its underwriting guidelines, Countrywide Home Loans obtains employment verification providing current and historical income information and/or a telephonic employment confirmation. Such employment verification may be obtained, either through analysis of the prospective borrower's recent pay stub and/or W-2 forms for the most recent two years, relevant portions of the most recent two years' tax returns, or from the prospective borrower's employer, wherein the employer reports the length of employment and current salary with that organization." CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006 at S-47. • "The maximum acceptable debt-to-income ratio, which is determined on a loan-by-loan basis varies depending on a number of underwriting criteria, including the Loan-to-Value Ratio, loan purpose, loan amount and credit history of the borrower. In addition to meeting the debt-to-income ratio guidelines, each prospective borrower is required to have sufficient cash resources to pay the down payment and closing costs." CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006 at S-47-48. • "Under its Standard Underwriting Guidelines, Countrywide Home Loans generally permits a debt-to-income ratio based on the borrower's monthly housing expenses of up to 33% and a debt-to-income ratio based on the borrower's total monthly debt of up to 38%." CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006 at S-49. • "Exceptions to Countrywide Home Loans' underwriting guidelines may be

Defendant	Misrepresentations
	made if compensating factors are demonstrated by a prospective borrower." CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006 at S-48. • "Countrywide Home Loans' underwriting standards are applied in accordance with applicable federal and state laws and regulations." CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006, at S-46.
Merrill	• "The Mortgage Loans were originated generally in accordance with the underwriting criteria, standards and guidelines of each Originator." MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006 at S-32. • "[U]nderwriting guidelines are designed to evaluate a borrower's credit history, his or her capacity, willingness and ability to repay the loan and the value and adequacy of the collateral." MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006, at S-34. • "Capacity, which is the borrower's ability to repay, is determined by cash flow. It must be clearly shown that the borrower has a proven, historical cash flow, which will support the requested loan amount. This approach anticipates that the loan is going to be repaid from the borrower's recurring cash inflows, not from the sale of the collateral. Job stability and length of time in current residence are also strong factors in determining a borrower's capacity. Continuity of employment is a strong factor in establishing the income used as a basis for repayment." OWNIT 2006-4 Prospectus Supplement dated June 22, 2006, at S-32. • "Based on the data provided in the application and certain verifications (if required), a determination was made by the original lender that the mortgagor's monthly income (if required to be stated) should be sufficient to enable the mortgagor to meet its monthly obligations on the mortgage loan and other expenses related to the mortgaged property (such as property taxes, standard hazard insurance and other fixed obligations on the mortgage loan during the first year of its term plus taxes and insurance and other fixed obligations equal to no more than a specified percentage of the prospective mortgagor's gross income. The percentage applied varies on a case-by-case basis depending on a number of underwriting criteria, including the loan-to-value ratio of the mortgage loan. The Originators may also have considered the amount of liquid assets available to the mortgagor at the time of origination." MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006, at S-33. • "The maximum allowable debt-to-income ratio under the Score More Full Documentation Program is 55%... The maximum allowable debt-to-income ratio under the Score More No Income Verification and Limited Documentation Program is 55%... The maximum allowable debt-to-income ratio under the Premier Score Full Documentation Program is 55%.... The maximum allowable debt-to-income ratio under the Premier Score No Income Verification Program is 50%." MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006, at S-37, S-38, S-39, S-40. • "[E]xceptions to the underwriting standards described herein may have been made in cases where compensating factors were demonstrated by a prospective mortgagor." MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006, at S-33, S-42. • "All loans are subject to a specific post-funding loan test, including high-cost tests, to verify that First NLC's originations comply with any applicable laws or regulatory requirements." MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006, at S-36.
Bank of America	• "The Mortgage Loans originated by Bank of America and originated or acquired by Countrywide Home Loans or National City Mortgage will have been underwritten materially in accordance with the applicable underwriting

Defendant	Misrepresentations
	standards set forth below . . . . The underwriting standards used by the Originators are intended to evaluate the Mortgagor's credit standing and repayment ability and the value and adequacy of the mortgaged property as collateral." BAFC 2007-A Prospectus Supplement dated January 30, 2007, at S-39. • "Regardless of the channel in which the loan was originated, a mortgage application is completed containing information that assists in evaluating the mortgagor's credit standing, capacity to repay the loan and adequacy of the mortgaged property as collateral for the loan. During the application process, the applicant is required to authorize Bank of America to obtain a credit report that summarizes the applicant's credit history with merchants and lenders and any record of bankruptcy or prior foreclosure." BAFC 2007-A Prospectus Supplement dated January 30, 2007, at S-39. • "As part of the underwriting evaluation, the applicant's "Debt-to-Income Ratio" is calculated as the amount of the monthly debt obligations (including the proposed new housing payment and related expenses such as property taxes and hazard insurance) to his or her gross monthly income. Bank of America's Debt-to-Income Ratio guidelines are based on the loan instrument, loan term, Credit Score, loan-to-value ratio, property type, and occupancy characteristics of the subject loan transaction." BAFC 2007-A Prospectus Supplement dated January 30, 2007, at S-40. • "As of the Cut-off Date, the weighted average Debt-to-Income Ratio at origination of the Mortgage Loans (excluding the Mortgage Loans for which no Debt-to-Income Ratio was calculated) is expected to be approximately 37.33%." BAFC 2007-A Prospectus Supplement dated January 30, 2007, at A-26. • "The automated underwriting decision engine and/or the underwriter may utilize compensating factors to offset one or more features of the loan transaction that may not specifically comply with the product guidelines." BAFC 2007-A Prospectus Supplement dated January 30, 2007, at S-40. • "Countrywide Home Loans' underwriting standards are applied in accordance with applicable federal and state laws and regulations." BAFC 2007-A Prospectus Supplement dated January 30, 2007, at S-46.

C. <u>Defendants' Misrepresentations Regarding Loan-to-Value and Combined Loan-to-Value Ratios</u>

112. The loan-to-value ("LTV") ratio is the ratio of a mortgage loan's original principal balance to the appraised value of the mortgaged property. The related combined LTV ("CLTV") takes into account other liens on the property, such as a second mortgage.

113. The Offering Materials presented detailed LTV and CLTV data for the underlying mortgage loans, including the number of mortgage loans within specified ranges and a weighted average by aggregate balance. Defendants also stated that there were maximum LTVs and

CLTVs based on the relevant underwriting guidelines and documentation program used. It was typically represented that no mortgage loan had an LTV or CLTV above 100%.

114. The prospectus supplement for each Offering also describes the valuation methods purportedly employed by appraisers in arriving at appraised values for the mortgaged properties. These appraised values were used to calculate the LTV and CLTV data discussed above. Defendants claimed that appraisers were independent and/or met certain standards. LTV and CLTV statistics for each deal are excerpted in Exhibits 1 to 349. Exemplary representations are set forth in Table 2 below.

115. The Offering Materials omitted to state that the appraised values used to calculate LTV and CLTV were inflated because of the intense pressure Defendants placed on appraisers in order to increase origination volume, and that Defendants did not genuinely believe the appraisal values used to calculate LTV and CLTV rations. AIG's forensic analysis has demonstrated that the LTV and CLTV ratios were materially understated in each of the 349 RMBS.

116. Thus the LTV and CLTV ratios were in reality materially higher than represented, as discussed further in Sections V.A & V.B.

Table 2: Sample Misrepresentations Regarding LTV and CLTV Ratios

Defendant	Misrepresentations
Countrywide	• The prospectus supplement for CWALT 2006-OA16 represented that the weighted average LTV ratio of the aggregate pool at origination was 75.1%. CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006, at S-36. • The term sheet for CWALT 2006-OA16 represented that the weighted average LTV ratio of the aggregate pool at origination was 75.0%. CWALT 2006-OA16 Term Sheet Computational Materials dated August 4, 2006, at 2. • "Except with respect to mortgage loans originated pursuant to its Streamlined Documentation Program, whose values were confirmed with a Fannie Mae proprietary automated valuation model, Countrywide Home Loans obtains appraisals from independent appraisers or appraisal services for properties that are to secure mortgage loans. The appraisers inspect and appraise the proposed mortgaged property and verify that the property is in acceptable condition. Following each appraisal, the appraiser prepares a report which includes a market data analysis based on recent sales of comparable homes in the area and, when deemed appropriate, a replacement cost analysis based on the current cost of constructing a similar home. All appraisals are required to conform to Fannie Mae or Freddie Mac appraisal standards then in effect."

Defendant	Misrepresentations
	CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006 at S-48.
Merrill	• The prospectus supplement for MLMI 2006-HE3 represented that the weighted average LTV ratio of the aggregate pool at origination was 82.0% and the weighted average CLTV ratio of the aggregate pool at origination was 88.5%. MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006, at A-II-6. • The free writing prospectus for MLMI 2006-HE3 represented that the weighted average LTV ratio of the aggregate pool at origination was 82.0% and that the weighted average CLTV ratio of the aggregate pool at origination was 88.5%. MLMI 2006-HE3 Free Writing Prospectus dated June 7, 2006, at 12. • "The adequacy of the mortgaged property as security for repayment of the related mortgage loan will generally have been determined by an appraisal in accordance with pre-established appraisal procedure guidelines for appraisals established by or acceptable to an Originator. All appraisals conform to the Uniform Standards of Professional Appraisal Practice adopted by the Appraisal Standards Board of the Appraisal Foundation and are on forms acceptable to Fannie Mae and/or Freddie Mac. Appraisers may be staff appraisers employed by an Originator or independent appraisers selected in accordance with pre-established appraisal procedure guidelines established by or acceptable to an Originator. The appraisal procedure guidelines generally will have required the appraiser or an agent on its behalf to personally inspect the property and to verify whether the property was in good condition and that construction, if new, had been substantially completed. The appraisal generally will have been based upon a market data analysis of recent sales of comparable properties and, when deemed applicable, an analysis based on income generated from the property or a replacement costs analysis based on the current cost of constructing or purchasing a similar property." MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006, at S-34.
Bank of America	• The prospectus supplement for BAFC 2007-A represented that the weighted average LTV ratio of the aggregate pool at origination was 73.80%. BAFC 2007-A Prospectus Supplement dated January 30, 2007, at S-11. • The term sheet for BAFC 2007-A represented that the weighted average LTV ratio of the aggregate pool at origination was 73.80%. BAFC 2007-A Term Sheet - Collateral Appendix dated January 24, 2007, at 26. • "A mortgage loan with secondary financing is evaluated to determine if the Total Loan-to-Value Ratio and Combined Loan-to-Value Ratio meet the requirements for the program under which the application is submitted or if the application contains compensating factors to warrant an exception to the applicable guidelines." BAFC 2007-A Prospectus Supplement dated January 30, 2007, at S-41. • "Bank of America conducts a valuation of the mortgaged property as collateral for each mortgage loan. This collateral valuation may be determined by (i) an interior inspection appraisal, (ii) a tax assessed value, (iii) a desktop appraisal, (iv) a drive-by appraisal, (v) an automated valuation model, or (vi) reference to the collateral valuation obtained in connection with the origination of the previous loan if the loan is a refinance of a mortgage loan that was previously serviced by Bank of America. . . . In certain instances, the interior, desktop or drive-by appraisal reports may be conducted by an employee of Bank of America or an affiliate. The appraisal report, however, may be performed by an independent appraiser contracted by Bank of America or an affiliate of Bank of America on direct channel originations. Appraisal reports on indirect channel originations are generally performed by an appraiser selected by the originating lender but indirect channel appraisers

Defendant	Misrepresentations
	cannot be performed by appraisers that have been deemed to be ineligible to perform appraisals by Bank of America." BAFC 2007-A Prospectus Supplement dated January 30, 2007, at S-42, S-43.

D. Defendants' Misrepresentations Regarding Owner-Occupancy

117. The Offering Materials contained detailed occupancy statistics for the underlying mortgage loans. Occupancy statistics for each deal are identified in Exhibits 1 to 349. Exemplary representations are set forth in Table 3 below.

118. Occupancy type was material to AIG because high owner-occupancy rates should have made the certificates safer investments than certificates backed by second homes or investment properties. Homeowners who reside in mortgaged properties are less likely to "walk away" and default than owners who purchase properties as investments or vacation homes. The personal disruption involved in defaulting on a primary residence—finding another place to live, re-enrolling children in new schools, and the emotional loss of losing one's home—exact a far greater toll than defaulting on a vacation or investment property. As a result, borrowers are far more incentivized to satisfy their mortgage obligations on the property they occupy rather than default.

119. The Offering Materials materially overstated the mortgages as owner-occupied as further discussed in Section V.C.

Table 3: Sample Misrepresentations Regarding Owner-Occupancy Statistics

Defendant	Misrepresentations
Countrywide	• The prospectus supplement for CWALT 2006-OA16 represented that 2,519 mortgage loans in the aggregate pool, or 84.8% by principal balance at origination, were secured by owner-occupied properties. CWALT 2006-OA16 Prospectus Supplement dated August 29, 2006, at S-38. • The term sheet for CWALT 2006-OA16 represented that 2,064 mortgage loans in the aggregate pool, or 85.7% by principal balance at origination, were secured by owner-occupied properties. CWALT 2006-OA16 Term Sheet Computational Materials dated August 4, 2006, at 7.
Merrill	• The prospectus supplement for MLMI 2006-HE3 represented that 2,822 mortgage loans in the aggregate pool, or 95.8% by principal balance at origination, were secured by owner-occupied properties. MLMI 2006-HE3 Prospectus Supplement dated June 19, 2006, at A-II-8.

Defendant	Misrepresentations
	• The free writing prospectus for MLMI 2006-HE3 represented that 2,822 mortgage loans in the aggregate pool, or 95.8% by principal balance at origination, were secured by owner-occupied properties. MLMI 2006-HE3 Free Writing Prospectus dated June 7, 2006, at 20.
Bank of America	• The prospectus supplement for BAFC 2007-A represented that 1,047 mortgage loans in the aggregate pool, or 81.62% by principal balance at origination, were secured by owner-occupied properties. BAFC 2007-A Prospectus Supplement dated January 30, 2007, at A-23. • The term sheet for BAFC 2007-A represented that 1,047 mortgage loans in the aggregate pool, or 81.62% by principal balance at origination, were secured by owner-occupied properties. BAFC 2007-A Term Sheet - Collateral Appendix dated January 24, 2007, at 27.

E. Defendants' Misrepresentations Regarding Credit Ratings

120. Credit ratings are assigned to RMBS tranches by the credit rating agencies, including Standard & Poor's ("S&P"), Moody's Investors Service ("Moody's"), and Fitch Ratings ("Fitch"). Each credit rating agency uses its own scale with letter designations to designate various levels of risk. In general, AAA ratings are at the top of the credit rating scale and are intended to designate the safest investments. C and D ratings are at the bottom of the scale and refer to investments that are currently in default and exhibit little or no prospect for recovery. Prior to the housing crisis, investments with AAA ratings historically experienced an expected loss rate of less than .05 percent. Investments with BBB ratings historically experienced an expected loss rate of under 1 percent. As a result, RMBS certificates with credit ratings between AAA through BBB- were generally referred to as "investment grade."

121. Credit ratings have been an important tool for AIG to gauge risk. For almost a hundred years, investors like pension funds, municipalities, insurance companies, and university endowments have relied on credit ratings to assist them in distinguishing between safe and risky investments. In addition, a variety of U.S. statutes and regulations explicitly reference and are keyed off credit ratings, lending credibility to the credit ratings process. For example, the amount of risk-based capital that a bank must hold is determined in part by the credit ratings of

its investments. Some investors, like pension funds, are prohibited from buying assets that are below investment grade. Credit ratings were particularly important and material to AIG because they provided additional assurances about the risks associated with RMBS. Indeed, certain of the AIG purchasers were required to purchase investments with certain ratings. For example, AIG's securities lending cash collateral investment policy required that 95% of its asset-backed securities (which included RMBS) be invested in transactions that were rated AAA/Aaa.

122. Each tranche of the RMBS at issue received a credit rating reflecting the rating agencies' assessment of its risk profile. The Offering Materials disclosed the ratings of each tranche of the deals, including the certificates purchased by AIG, based on ratings analyses performed by one or more rating agencies. The credit ratings for each of the certificates is identified in Exhibit A. Ratings representations for each deal are excerpted in Exhibits 1 to 349.

123. Defendants' representations to AIG regarding credit ratings were false and misleading because Defendants engineered artificially high credit ratings by misrepresenting to the rating agencies the credit quality of the loan collateral and the guidelines used to originate the loans, as described in further detail in Section V.D.

V. DEFENDANTS' REPRESENTATIONS TO AIG WERE FALSE

124. AIG recently commissioned a forensic review of the mortgage loans underlying the certificates to analyze the accuracy of the quantitative representations Defendants made regarding material characteristics of the RMBS. AIG's analysis confirms that Defendants misrepresented material characteristics of the mortgage loan pools for the RMBS at issue.

125. Without direct access to all the underlying loan files, AIG developed a framework to conduct a retroactive analysis of certain key numerical representations made by Countrywide,

Bank of America, and Merrill.[1] AIG sampled loans from each of the 349 RMBS in which it invested and for which data was available to test Defendants' representations regarding the risk metrics of the underlying mortgage pools, including owner-occupancy statistics, loan-to-value ("LTV") ratios, and combined loan-to-value ("CLTV") ratios. Sampling is widely accepted as a reliable methodology to establish conclusions about broader data ranges and, accordingly, is customarily used by courts, government agencies, and in the private sector. Experts in RMBS cases have found that a sample of loans can provide statistically significant data regarding the overall mortgage pool.

126. AIG analyzed these statistics across AIG's investments with Bank of America, Countrywide, and Merrill. For all 349 RMBS for which data was available, AIG analyzed an average of 797 loans from each mortgage pool.[2] In general, the sample sizes ranged from 400 to 6,632 loans.[3] In total, AIG conducted loan-level analyses on 262,322 mortgage loans across these 349 RMBS and identified 105,568 mortgage loans where Defendants' risk metrics were false. In other words, Defendants representations in the Offering Materials were based on false metrics in a staggering 40.2% of the sampled loans. The magnitude of the misrepresentations in

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[1] The loan files themselves were not available to AIG prior to its purchase decisions. As part of its investigation, AIG has contacted trustees for numerous deals at issue and requested access to the underlying mortgage loan files. However, the trustees and/or the servicers have flat-out refused to cooperate with respect to the vast majority of the deals. AIG has also contacted Defendants, requesting their assistance in obtaining loan files for these transactions—requests that have been ignored. For the small number of loans AIG has been able to access, AIG has been conducting a re-underwriting review and found significant and material misrepresentations. Defendants' refusal to cooperate and provide loan files for review underscores their intent to conceal the rampant misrepresentations made with respect to the RMBS. AIG's inability to access information in the loan files also demonstrates that the information in the files are within Defendants' peculiar, unique and specialized knowledge.

[2] For some transactions, public data was not available for all loans analyzed.

[3] For seven transactions for which there was insufficient public data, the sample sizes ranged from 176 to 388 loans.

the samples AIG tested is clear evidence of systemic misrepresentations in the mortgage pools as a whole.

127. For AIG's 211 RMBS involving Countrywide, AIG analyzed 195,385 loans and identified 78,146 mortgage loans with false metrics, meaning that Countrywide's metrics for 40.0% of the sampled loans were false. For AIG's 91 RMBS involving Bank of America, AIG analyzed 44,614 loans and found 18,466 mortgage loans with false metrics, meaning that Bank of America's metrics for 41.4% of the sampled loans were false. For AIG's 81 RMBS involving Merrill, AIG analyzed 42,408 loans and identified 17,396 mortgage loans with false metrics, meaning the Merrill's metrics for 41.0% of the sampled loans were false. (Some RMBS involved a combination of Bank of America, Merrill and/or Countrywide.)

A. Loan-to-Value Ratios Represented by Defendants Were False

128. LTV ratio is one of the key risk factors that lenders assess when qualifying borrowers for a mortgage. As noted above, the LTV ratio expresses the amount of a first mortgage lien as a percentage of the total appraised value of real property. This ratio was material to AIG's investment because higher ratios correlate with a higher risk of default. A borrower with a small equity position in a property has much less to lose if he or she defaults on the loan. Additionally, there is a greater likelihood a foreclosure will result in a loss for the mortgage holder (here, the securitization trusts on behalf of AIG and other investors) if a property is fully leveraged. LTV ratio is a key metric for investors in evaluating both the price and the risk of RMBS. For that reason, Defendants included detailed representations regarding LTV ratios in the Offering Materials.

129. For each of the sampled loans, the underlying property was valued as of its loan origination date by an industry-standard automated valuation model ("AVM"). Mortgage originators and servicers, including Bank of America and Countrywide, routinely used AVMs as

a way of valuing properties during pre-qualification, origination, and servicing processes. AVMs produce independent, statistically-derived valuations using sales data for comparable properties in the same geographic area as the mortgaged property. This appraisal method is used by originators and servicers to support valuation conclusions and to detect fraud. Indeed, Bank of America itself markets its ValueFinder AVM product as a method to "automatically detect fraudulent and high-risk loan applications." AVMs have become so mainstream that their testing and use is specifically outlined in regulatory guidance and directly referenced in the Dodd-Frank Act.

130. The AVM used to test Defendants' representations is industry-leading; independent testing services have determined it to be one of the most comprehensive and accurate models available. It incorporates a database of more than 500 million mortgage transactions covering ZIP codes that represent more than 97% of all properties, which are occupied by more than 99.7% of the population in the United States. AIG used this AVM to conduct a retroactive appraisal for each sampled loan—an appraisal of the mortgaged property as of the time the loan was originated using the same comparable sales data that would have been available to mortgage lenders at the time.

131. AIG's appraisal analysis demonstrated that Defendants' Offering Materials materially understated the LTV ratios, and thus the risks, of the mortgage pools. The appraised values given to the mortgaged properties were significantly higher than what the properties were actually worth at the time of investment. Defendants' misconduct affected the LTV ratios by increasing the value of the properties relative to the loan amount, thus decreasing the overall LTV ratio.

132. Defendants' aggregated mortgage pool statistics regarding LTV disclosed in the Offering Materials were based on individual loan-level data that is listed in the mortgage pool's "loan tape." The loan tape is a compilation of loan-by-loan metrics (including LTV, CLTV and occupancy) for a mortgage pool. Using the AVM reappraisal, AIG was able to calculate the actual LTV for each tested loan, and then compare that to the LTV disclosed for that loan on the loan tape.

133. AIG's analysis shows that 17.2% to 69.8% of the sampled loans in each RMBS had an actual LTV ratio more than 10 percentage points higher than Defendants' metrics. On average, the LTV ratio for 34.3% of the loans in each mortgage pool was in reality 10 percentage points higher than Defendants' metrics. AIG's analysis shows that 9.2% to 55.6% of the sampled loans in each RMBS had an actual LTV ratio more than 15 percentage points higher than Defendants' metrics, with an average of 22.8% of the loans in each mortgage pool having an LTV ratio higher by at least 15 percentage points. AIG's analysis reveals that 1.9% to 32.7% of the sampled loans had LTVs more than 25 percentage points higher than Defendants' metrics, with an average of 10.3% of the loans in each mortgage pool having a LTV ratio higher by at least 25 percentage points.

134. Defendants aggregated these false loan-by-loan metrics in representations to AIG in the Offering Materials concerning weighted average LTV ratios for the pools as a whole and the number of loans falling within LTV ratio ranges. Because Defendants' representations in the Offering Materials regarding LTV ratios were based on false loan-level information, Defendants' aggregated statistics were false. Properly disclosed LTV ratios would have had a profound effect on AIG's decision to invest or take a certain position in a given RMBS. Properly

disclosed LTV ratios also would have altered the ratings for the RMBS, as further discussed in Section V.D.

135. The table below provides statistics for six RMBS to illustrate the falsity of Defendants' metrics regarding LTV ratios. Exhibits 1 to 349 identify these false metrics in the remaining RMBS.

Asset	Percentage of Loans with an LTV Ratio that was Understated by at Least 10 Percentage Points	Percentage of Loans with an LTV Ratio that was Understated by at Least 15 Percentage Points	Percentage of Loans with an LTV Ratio that was Understated by at Least 25 Percentage Points
CWALT 2005-77T1	44.37%	32.39%	17.96%
CWALT 2006-OA16	40.87%	28.15%	10.80%
MLMI 2006-AF1	35.37%	21.54%	10.57%
FFML 2007-FF2	41.63%	27.04%	14.16%
BAFC 2006-I	45.39%	32.98%	13.83%
BAFC 2007-A	35.47%	26.79%	13.21%

136. Moreover, Defendants made specific representations about the percentage of loans in each mortgage pool that had LTV ratios higher than 90%. *See* Exhibits 1 to 349. LTV ratios in excess of 90% provide the mortgage holder with very little equity cushion to protect against borrower default and foreclosure loss. Consequently, an accurate disclosure of the number of loans within a mortgage pool is important in making an investment decision. Across all sampled RMBS, the number of loans in a given RMBS with LTV ratios over 90% was understated by a range of 12.7 percentage points to 82.3 percentage points, with the average understatement being 33.4 percentage points. For the RMBS involving Countrywide, the number of loans with LTV ratios over 90% was understated by 15.9 percentage points to 71.6 percentage points, with the average understatement being 30.7 percentage points. For the RMBS involving Bank of America, the number of loans with LTV ratios over 90% was understated by

12.7 percentage points to 82.3 percentage points, with the average understatement being 36.1 percentage points. For the RMBS involving Merrill, the number of loans with LTV ratios over 90% was understated by 15.8 percentage points to 82.3 percentage points, with the average understatement being 37.6 percentage points.[4]

137. The table below provides statistics for six RMBS to illustrate the misrepresentations Defendants made regarding the percentage of loans above the 90% LTV ratio threshold. As shown in the table below, the percentage of loans with an LTV ratio of greater than 90% was substantially understated by Defendants in the Offering Materials. Exhibits 1 to 349 identify these misrepresentations in the remaining RMBS.

Asset	Percentage of Loans with an LTV Ratio of 90% or Greater, as Represented by Offering Materials	Actual Percentage of Loans with an LTV Ratio of 90% or Greater	Percentage Point Difference Between Represented and Actual Figure	Percentage Understatement
CWALT 2005-77T1	0.20%	36.62%	36.42	99.45%
CWALT 2006-OA16	3.90%	35.48%	31.58	89.01%
MLMI 2006-AF1	1.50%	26.42%	24.92	94.3%
FFML 2007-FF2	20.60%	49.36%	28.76	58.27%
BAFC 2006-I	2.50%	39.01%	36.51	93.59%
BAFC 2007-A	4.20%	33.58%	29.38	87.49%

138. In nearly every RMBS, Defendants also represented that none of the mortgage loans collateralized had LTV ratios exceeding 100%, meaning that in these RMBS not one loan exceeded the value of the property. An LTV ratio of greater than 100% is known as being "underwater," where a borrower owes more money on the property than it is actually worth. Such loans offer the mortgage holder zero equity margin and leave the mortgage holder with

[4] These statistics exclude RMBS that securitized home equity lines of credit, because only combined loan-to-value ratios were reported for these transactions.

inadequate collateral from the moment the loan is originated. Despite these representations by Bank of America, Merrill, and Countrywide, AIG's analysis found a substantial number of mortgage loans with an LTV ratio greater than 100% throughout the mortgage pools. The table below illustrates these misrepresentations in six RMBS. Exhibits 1 to 349 identify these misrepresentations in the remaining RMBS.

Asset	Represented Percentage of Loans with an LTV Ratio of 100% or Greater	Actual Percentage of Loans with an LTV Ratio of 100% or Greater
CWALT 2005-77T1	0.00%	19.72%
CWALT 2006-OA16	0.00%	16.97%
MLMI 2006-AF1	0.00%	12.60%
FFML 2007-FF2	0.00%	26.18%
BAFC 2006-I	0.00%	17.02%
BAFC 2007-A	0.00%	16.60%

139. Further, the Offering Materials materially misrepresented the weighted average LTV ratio of the mortgage loans in each pool. Across all sampled RMBS, the weighted average LTV ratio was understated by an average of 11.0 percentage points, or 12.4% on a relative basis. For the RMBS involving Countrywide, the weighted average LTV ratio was understated by an average of 11.1 percentage points, or 12.5% on a relative basis. For the RMBS involving Bank of America, the weighted average LTV ratio was understated by an average of 11.5 percentage points, or 13.3% on a relative basis. For the RMBS involving Merrill, the weighted average LTV ratio was understated by an average of 10.2 percentage points, or 11.4% on a relative basis. The table below illustrates these misrepresentations in six RMBS. Exhibits 1 to 349 identify these misrepresentations in the remaining RMBS.

Asset	Weighted Average LTV Ratio as Represented by the Defendants	Actual Weighted Average LTV Ratio	Difference Between Represented and Actual Figure	Percentage Understatement
CWALT 2005-77T1	73.10%	89.17%	16.07	18.02%
CWALT 2006-OA16	75.10%	88.20%	13.10	14.85%
MLMI 2006-AF1	69.10%	79.86%	10.76	13.47%
FFML 2007-FF2	82.60%	97.94%	15.34	15.66%
BAFC 2006-I	72.00%	89.11%	17.11	19.20%
BAFC 2007-A	73.80%	86.61%	12.81	14.79%

B. Combined Loan-to-Value Ratios Represented by Defendants Were False

140. The Combined Loan-to-Value ("CLTV") ratio is the proportion of all loans secured by a property (for example, first mortgages plus second liens or home equity lines of credit) in relation to its value. It adds additional specificity to the basic LTV ratio by indicating that additional liens on the property have been considered in the calculation of the percentage ratio. Like LTV ratio, CLTV ratio is a key metric for investors in evaluating both the price and the risk of RMBS. For that reason, Defendants included representations regarding CLTV ratios in the Offering Materials. CLTV ratio was material to AIG's investment because higher ratios correlate with a higher risk of default.

141. The Offering Materials make statistical representations about the range of CLTV ratios for the mortgage loans underlying the certificates. These statistics were false because many of the CLTV ratios were artificially low, underestimating the risks of the certificates. For example, 25.6% to 79.5% of the sampled loans in each RMBS had an actual CLTV ratio of more than 10 percentage points higher than Defendants' metrics, with an average of 44.4% of the loans in each RMBS. Of the sampled loans in the RMBS involving Countrywide, 25.6% to 76.0% had a CLTV ratios more than 10 percentage points higher than Defendants' metrics, with

an average of 43.1%. For the RMBS involving Bank of America, 33.6% to 69.4% of the sampled loans had CLTV ratios more than 10 percentage points higher than Defendants' metrics, with an average of 47.7%. For the RMBS involving Merrill, 28.6% to 79.5% of the sampled loans had a CLTV ratios more than 10 percentage points higher than Defendants' metrics, with an average of 44.1%.

142. Defendants aggregated these false loan-by-loan metrics in representations to AIG in the Offering Materials concerning weighted average CLTV ratios for the pools as a whole and the number of loans falling within CLTV ratio ranges. Because Defendants' representations in the Offering Materials regarding CLTV ratios were based on false loan-level information, Defendants' aggregated statistics were false. Properly disclosed CLTV ratios would have had a profound effect on AIG's decision to invest or take a certain position in a given RMBS. Properly disclosed CLTV ratios also would have altered the ratings for the RMBS, as further discussed in Section V.D.

143. The table below illustrates the falsity of Defendants' metrics in six RMBS. Exhibits 1 to 349 identify these false metrics in the remaining RMBS.

Asset	**Percentage of Loans with a CLTV Ratio that was Understated by at Least 10 Percentage Points**	**Percentage of Loans with a CLTV Ratio that was Understated by at Least 15 Percentage Points**	**Percentage of Loans with a CLTV Ratio that was Understated by at Least 25 Percentage Points**
CWHL 2007-15	63.91%	47.74%	27.44%
CWL 2006-16	41.46%	28.08%	13.22%
MLMI 2006-HE5	44.79%	32.05%	14.29%
FFML 2007-FF2	45.49%	34.33%	16.74%
ABFC 2006-OPT2	46.08%	31.02%	15.66%
OOMLT 2007-6	45.54%	33.93%	19.64%

144. Further, the Offering Materials materially misrepresented the weighted average CLTV ratio of the mortgage loans in each pool. Across all sampled RMBS, weighted average CLTV ratios were understated by an average of 15.8 percentage points, or 15.7% on a relative basis. For the RMBS involving Countrywide, weighted average CLTV ratios were understated by an average of 16.6 percentage points, or 16.5% on a relative basis. For the RMBS involving Bank of America, weighted average CLTV ratios was understated by an average of 18.4 percentage points, or 18.7% on a relative basis. For the RMBS involving Merrill, weighted average CLTV ratios was understated by an average of 13.4 percentage points, or 13.0% on a relative basis. The table below illustrates these misrepresentations in six RMBS. Exhibits 1 to 349 identify these misrepresentations in the remaining RMBS.

Asset	Weighted Average CLTV Ratio as Represented by Defendants	Actual Weighted Average CLTV Ratio	Difference Between Represented and Actual Figure	Percentage Understatement
CWHL 2007-15	79.50%	101.09%	21.59	21.36%
CWL 2006-16	77.60%	95.42%	17.82	18.68%
MLMI 2006-HE5	87.40%	103.31%	15.91	15.40%
FFML 2007-FF2	92.50%	112.00%	19.50	17.41%
ABFC 2006-OPT2	79.50%	93.95%	14.45	15.38%
OOMLT 2007-6	80.10%	98.77%	18.67	18.90%

C. <u>Owner-Occupancy Levels Represented by Defendants Were False</u>

145. The Defendants misrepresented in the Offering Materials of each RMBS that the mortgage pools underlying the certificates had a higher percentage of borrowers living in the mortgaged properties ("owner-occupied properties") than was actually the case.

146. Owner-occupancy statistics are material to investors because borrowers are less likely to default on mortgages for the homes in which the live than on investment or vacation properties. RMBS backed by mortgage pools with high owner-occupancy rates therefore are

safer investments than those backed mortgage pools full of mortgages on second homes and investment properties.

147. AIG utilized borrower- and property-specific public records to test whether a given borrower actually occupied the property as claimed by the Defendants. Contemporaneous property tax records were analyzed to determine whether (1) the borrower received his property tax bill for the mortgaged property at the address of the mortgaged property and (2) the borrower took a property tax exemption on the mortgaged property that is only available for owner-occupied properties. A borrower is likely to have a tax bill sent to his or her primary residence to ensure his or her ability to make timely payment. However, if a borrower has tax records sent to a different address, the borrower likely does not actually reside at the mortgaged property. And if a borrower declined to make certain tax exemption elections dependent on the borrower residing at the property, such evidence demonstrates that the borrower does not live at the mortgaged property.

148. AIG also analyzed public records to determine if the borrower owned any other properties during the same time period in which he or she owned the securitized property. AIG then examined whether the borrower consistently identified the securitized property as his or her mailing address for property tax bills on each concurrently owned property. Inconsistencies in tax bill mailing addresses for concurrently owned properties also strongly suggest that the securitized property was not, in fact, owner-occupied.

149. AIG then conducted a review of lien records on concurrently owned properties to determined whether the borrower indicated that any property other than the securitized property was owner-occupied. The test examines all liens originated after the securitized mortgage and compares owner-occupancy representations with those in the Offering Materials. It is strong

evidence that the borrower does not reside at the mortgaged property if liens on concurrently owned properties indicate that those properties are owner-occupied.

150. AIG also examined the mailing addresses identified for liens on concurrently owned properties to determine whether the address of the securitized property is listed as the mailing address for bills and other correspondence between the borrower and the lienholders. If the securitized property address is not identified, that is also a clear indication that the securitized property is not owner-occupied.

151. Finally, AIG reviewed credit records to help determine whether a given borrower occupied the mortgaged property. Specifically, AIG investigated whether creditors were reporting the securitized property's address as the borrower's mailing address six months after the origination of the loan. Within six months of closing on a mortgage, one would expect the borrower to have changed his or her billing address with each of his or her creditors. If the borrower was telling creditors to send bills to another address even six months after buying the property, it is likely the borrower was living at a different location.

152. In assessing the accuracy of Defendants' representations in the Offering Materials regarding owner-occupancy, AIG only considered instances in which a mortgage failed multiple owner-occupancy tests. Despite this high threshold, AIG's investigation revealed systemic misrepresentations of owner-occupancy within each mortgage pool.

153. The results of AIG's loan-level analysis of actual owner-occupancy rates on the mortgage loans underlying its certificates are set forth below. AIG's loan-level analysis demonstrates that the Defendants' drastically overstated the percentage of owner-occupied properties secured by mortgage loans in the collateral pools. Overall, Defendants falsely represented the number of owner-occupied properties in each RMBS by 3.9 to 24.2 percentage

points, with an average overstatement of 14.1 percentage points, or 21.2% on a relative basis. In RMBS involving Countrywide, the number of owner-occupied properties was falsely represented by 3.9 to 24.2 percentage points, with an average overstatement of 14.9 percentage points, or 23.6% on a relative basis. In RMBS involving Bank of America, the number of owner-occupied properties were falsely represented by 7.2 to 22.6 percentage points, with an average overstatement of 13.9 percentage points, or 20.9% on a relative basis. In RMBS involving Merrill, the number of owner-occupied properties were falsely represented by 7.3 to 22.4 percentage points, with an average overstatement of 12.8 percentage points, or 17.3% on a relative basis. The table below illustrates these misrepresentations in six RMBS. Exhibits 1 to 349 identify these misrepresentations in the remaining RMBS.

Asset	Percentage of Owner-Occupied Properties Represented in Offering Materials	Actual Percentage of Owner-Occupied Properties	Percentage Point Difference Between Represented and Actual Figure	Percentage Overstatement
CWALT 2005-77T1	88.60%	70.83%	17.77	25.09%
CWALT 2006-OA16	80.60%	64.95%	15.65	24.10%
MLMI 2006-AFI	90.10%	77.57%	12.53	16.16%
FFML 2007-FF2	94.90%	77.92%	16.98	21.79%
BAFC 2006-I	88.90%	75.00%	13.90	18.53%
BAFC 2007-A	76.00%	56.81%	19.19	33.78%

D. Defendants Engineered Inflated Credit Ratings

154. Throughout the relevant timeframe, Defendants marketed and sold its RMBS products based on inflated credit ratings that masked the true credit risk of those securities. Indeed, Defendants engineered artificially high credit ratings through grossly improper means—

by misrepresenting to the rating agencies the credit quality of the loan collateral and the guidelines used to originate the RMBS loans.

155. Recent government investigations have revealed this misconduct. In April 2011, the U.S. Senate Permanent Subcommittee on Investigations ("SPSI") issued its final report on the role of the investment banks and other securitizing parties, including Defendants, in the financial crisis. The SPSI report is the culmination of more than two years of Congressional investigation into the financial crisis, and is based on four Senate hearings held in April 2010, over 150 interviews and depositions, and the SPSI's review of tens of millions of pages of documents, many of which were recently disclosed in connection the SPSI report. The SPSI report includes express Congressional findings of fact on the "inflated credit ratings" Defendants procured and used to sell their RMBS products.

156. In particular, the SPSI found that Defendants used "financially engineered" credit ratings to sell their faulty products as highly rated securities:

> Wall Street firms used financial engineering to combine AAA ratings - normally reserved for ultra-safe investments with low rates of return - with high risk assets, such as the AAA tranche from a subprime RMBS paying a relatively high rate of return. Higher rates of return, combined with AAA ratings, made subprime RMBS and related CDOs especially attractive investments.

(SPSI Report, at 30.)

157. Defendants had huge incentives to procure favorable ratings on the RMBS it securitized and sold. Indeed, Defendants' RMBS would not have been issued but for the provision of the credit ratings, as almost every prospectus and prospectus supplement stated that it was a condition to the issuance of each series offered that they receive certain specified ratings from the rating agencies. Without investment grade credit ratings, Defendants would have found it virtually impossible to sell their RMBS products, as market participants would not have been

able to meet their internal investment guidelines. As such, Defendants were highly motivated to procure high ratings for their RMBS—the deals could not be issued without them.

158. Defendants engineered inflated ratings on their RMBS products by providing false data to the rating agencies that overestimated the credit quality of the underlying mortgage loans, which skewed ratings in Defendants' favor. Each credit rating agency uses a model to assign ratings to the different tranches of the RMBS deals. The inputs to the credit rating agencies' models include, among other things, the debt-to-income ratios, loan-to-value ratios, owner-occupancy status, and home values corresponding to the mortgage loans underlying the particular deal being rated.

159. Just as AIG relied on Defendants to provide accurate information concerning the credit quality of the mortgage pools, the rating agencies relied on Defendants to provide them with accurate information on which to base their ratings. The SPSI report describes the flow of information from Defendants to the rating agencies:

> For RMBS, the "arranger" - typically an investment bank - initiated the rating process by sending to the credit rating agency information about a prospective RMBS and data about the mortgage loans included in the prospective pool. The data typically identified the characteristics of each mortgage in the pool including: the principal amount, geographic location of the property, FICO score, loan to value ratio of the property, and type of loan. … In addition to data on the assets, the arranger provided a proposed capital structure for the financial instrument, identifying, for example, how many tranches would be created, how the revenues being paid into the RMBS or CDO would be divided up among those tranches, and how many of the tranches were designed to receive investment grade ratings. The arranger also identified one or more "credit enhancements" for the pool to create a financial cushion that would protect the designated investment grade tranches from expected losses.

(SPSI Report, at 250-251.)

160. In her testimony to the SPSI, Susan Barnes, the North American Practice Leader for RMBS at S&P from 2005 to 2008, highlighted the importance of accurate information to the credit ratings process:

> The securitization process relies on the quality of the data generated about the loans going into the securitizations. ***S&P relies on the data produced by others and reported to both S&P and investors about those loans.*** At the time that it begins its analysis of a securitization, S&P received detailed data concerning the loan characteristics of each of the loans in the pool - up to 70 separate characteristics for each loan in a pool of, potentially, thousands of loans. ***S&P does not received the original loan files for the loans in the pool.*** Those files are reviewed by the arranger or sponsor of the transaction, who is also responsible for reporting accurate information about the loans in the deal documents and offering documents to potential investors. (Emphasis added).

161. Defendants fed the rating agencies the same false data regarding loan-to-value ratios, owner-occupancy status, home values, and debt-to-income ratios that they provided to investors in the Offering Materials. (The false data Defendants provided for each deal at issue is detailed in Exhibits 1 to 349.) The rating agencies then input this false data into their quantitative models to assess the credit risk associated with the RMBS, project likely future defaults, and ultimately determine the ratings on Defendants' RMBS products. As a result, Defendants essentially pre-determined the ratings by feeding bad data into the ratings system. In other words, by providing data that overestimated the credit quality and value of the underlying mortgages, Defendants guaranteed that the ratings on their RMBS products would be inflated. The underwriting guidelines provided to the rating agencies further contributed to the inflation of the ratings, as Defendants did not inform the rating agencies that they had abandoned compliance with the guidelines.

162. In a non-public meeting on September 10, 2007, a transcript of which was released to the public on October 22, 2008, senior executives at Moody's confirmed that the rating agencies relied on data that they now know to be false:

- “At the end of the day, we relied on reps and warrantees that no loans were originated in violation of any state or federal law. We know that’s a lie. If none were originated in violation of any predatory lending law, we know that’s a lie. So what are you going to do about it? We can’t rely on what people tell us anymore, and so we’ve got to figure out, do we rely on third party oversight?”

- “It’s actually quite interesting that we’re being asked to figure out how much everybody lied. That’s really what we’re being asked to do.”

163. Moreover, the credit ratings assigned to senior tranches of the RMBS by the rating agencies considered the level of “credit enhancement” offered through the structure of the RMBS deals themselves. Credit enhancement represents the amount of “cushion” or protection from loss exhibited by a given security. This cushion is intended to improve the likelihood that holders of highly-rated certificates receive the interest and principal to which they are entitled. Credit enhancement can take the form of structural subordination, where senior tranches are paid first and losses affect junior tranches before senior tranches, and overcollateralization, where the par amount of underlying loan portfolio is larger than the security it backs. The level of credit enhancement offered is based on the make-up of the loans in the underlying collateral pool. Riskier pools necessarily need higher levels of credit enhancement to ensure payment to senior certificateholders. By inflating the credit characteristics of the loan pool, Defendants created the false impression that the senior tranches of the RMBS deals had meaningful credit enhancement. In reality, the “cushion” on which the rating agencies relied to issue high ratings for these tranches was illusory, because the collateral mortgages had credit characteristics that offered little or no cushion to support the cash flow to the senior tranches.

164. The credit rating agencies were understaffed and overwhelmed with the avalanche of complex structured products being brought to market at the time. In 2006 and 2007 alone, Moody’s and S&P each rated about 10,000 RMBS deals. Defendants capitalized on the rating agency overload and used it to their advantage to procure favorable ratings on their RMBS deals,

which Defendants demanded be rated and closed in increasingly short timeframes. Indeed, the rating agencies grew more and more reliant on the bankers to provide the bulk of the credit analysis for them—and this analysis was based on misrepresented loan statistics, such as those detailed in Sections V.A, V.B, and V.C above. Defendants were thus able to inflate the ratings for the RMBS by deceiving the rating agencies about the credit quality and value of the mortgage loans underlying the deals and providing a false impression that the senior tranches would have a meaningful equity cushion through credit enhancement.

165. Defendants thus knowingly procured and promoted fraudulent ratings that overstated the actual credit quality of AIG's certificates and that Defendants did not genuinely believe. As described in Section VI, Defendants knew that the collateral pool on which the ratings were based was much riskier than reflected by the data they provided the rating agencies, and thus the high quality ratings they engineered to sustain the RMBS market were false and inflated.

(1) All Deals Have Suffered Significant Credit Rating Downgrades

166. The ratings given to AIG's certificates have been significantly downgraded since the time of origination. Many of AIG's investments in the transactions initially received the highest possible Standard & Poor's ("S&P") rating (AAA) and Moody's rating (Aaa), which have historically represented an expected loss rate of less than .05%. According to S&P's white paper, *Understanding Standard & Poor's Rating Definitions*, an AAA rating represents an "extremely strong capacity to meet its financial commitments." This is the exact same rating typically given to bonds backed by the full faith and credit of the United States government. Moody's similarly describes that its highest rating represents that the investment is "judged to be of the highest quality, with minimal credit risk."

167. Predominantly because of the high delinquency, foreclosure, and default rates, the ratings given to AIG's certificates have significantly been downgraded. Despite many beginning with the same rating given to U.S. treasury bonds (*i.e.*, AAA), a large percentage of the certificates are currently rated as non-investment grade loans. Additionally, a significant percentage of the loans have fallen to "junk-bond" status—S&P's rating of CCC or below. Defendants' misrepresentations as to the true credit quality of the loans led AIG to invest and take positions in transactions they would not have "but for" the original credit ratings. Exhibit A illustrates how many of AIG's certificates have been drastically downgraded.

168. The poor performance of the loan pools and the deteriorating credit ratings have caused a massive decline in the market values of the certificates. Loan pools that were properly underwritten and contained loans with the represented characteristics would not have experienced such extensive payment problems and would have substantially lower percentages of defaults, foreclosures, and delinquencies at this time. The drastic rise of default rates, precipitous fall of credit ratings and overall abysmal performance of the mortgage loans reflects Defendants' faulty underwriting and misrepresentations.

E. <u>Defendants Ignored Stated Underwriting Guidelines</u>

169. Defendants' representations regarding the underwriting processes, underwriting quality, loan selection, credit enhancements, use of exceptions and alternative documentation programs, and ratings were all untrue. The mortgage loans underlying AIG's certificates did not comply with the underwriting standards the Offering Materials described because those standards were systemically ignored. In their roles as both originators and as acquirers of the loans, Defendants ignored borrowers' actual repayment ability and the value and adequacy of mortgaged property used as collateral. Systematic, bulk exceptions to underwriting standards were granted without consideration of any compensating factors. Defendants also materially

omitted that they were systematically abusing "exceptions" and alternative documentation programs in order to further circumvent their purported underwriting standards. As the FCIC explained, these abuses led to the recent financial crisis:

> [I]t was the collapse of the housing bubble - fueled by low interest rates, easy and available credit, scant regulation, and toxic mortgages - that was the spark that ignited a string of events, which led to a full-blown crisis in the fall of 2008. Trillions of dollars in risky mortgages had become embedded throughout the financial system, as mortgage-related securities were packaged, repackaged, and sold to investors around the world.

(FCIC Report, at xvi.)

(1) Countrywide Ignored Its Underwriting Guidelines

170. The scope and breadth of Countrywide's fraudulent schemes and other unlawful conduct have been revealed through a substantial number of public and private inquiries, investigations, and actions. The actions are based, in part, upon acts and misconduct by Countrywide that are inconsistent with its representations in the Offering Materials and that occurred at the same time the loans underlying AIG's certificates were originated and securitized.

171. On June 4, 2009, the Securities and Exchange Commission ("SEC") filed a civil complaint against former Countrywide executives for their fraudulent disclosures relating to Countrywide's purported adherence to conservative loan origination and underwriting guidelines, as well as insider trading by Angelo Mozilo, Countrywide's former CEO. In connection with this action, the SEC recently made public many of Countrywide's internal documents and communications as well as testimony given by Countrywide's former executives.

172. The Financial Crisis Inquiry Commission ("FCIC") investigated Countrywide's role in the financial crisis and recently made public internal Countrywide documents and

interviews of Countrywide executives in connection with a report published by the Commission in January 2011.

173. A number of States have also announced investigations of Countrywide's lending practices, and several commenced actions against Countrywide, including:

- In *People of the State of California v. Countrywide Financial Corp.,* the Attorney General for the State of California filed a civil action on behalf of Countrywide borrowers in California against Countrywide and its senior executives, asserting statutory claims for false advertising and unfair competition based on a plan to increase the volume of mortgage loans for securitization without regard to borrower creditworthiness.

- In *People of the State of Illinois v. Countrywide Financial Corp.,* the Attorney General for the State of Illinois filed a civil suit on behalf of Illinois borrowers against Countrywide and Mozilo, asserting state consumer protection and unfair competition statutory claims, alleging that beginning in or around 2004, Countrywide engaged in unfair and deceptive practices, including loosening underwriting standards, structuring unfair loan products with risky features, and engaging in misleading marketing and sales practices.

- In *State of Connecticut v. Countrywide Financial Corp.,* the Connecticut Insurance Commissioner commenced a civil action asserting that Countrywide violated state unfair and deceptive practices law by deceiving consumers into obtaining mortgage loans for which they were not suited and could not afford.

- In *Office of the Attorney General for the State of Florida v. Countrywide Financial Corp.,* the Florida Attorney General commenced a civil action against Countrywide and Mozilo, asserting state unfair practices statutory claims, and alleging that since January 2004, Countrywide promoted a deceptive scheme to originate subprime mortgage loans to unqualified borrowers, and a related fraudulent scheme to sell securities. The Attorney General alleges that Countrywide violated state statutory lender laws by falsely representing that Countrywide originated each mortgage loan in accordance with its underwriting guidelines and that each borrower had the ability to repay the mortgage loan. The Attorney General also asserts state securities law claims, alleging that Countrywide sold mortgage-backed securities based on fraudulent misrepresentations.

- In *State of Washington v. Countrywide Financial Corp.,* the Washington Attorney General filed a civil action asserting that Countrywide violated state anti-discrimination laws in 2005 and 2006 by engaging in racially discriminatory lending.

- In *State of Indiana v. Countrywide Financial Corp.,* the State of Indiana filed a civil action asserting that Countrywide violated the state's unfair and deceptive practices law from 2005 through 2008 by deceiving consumers into obtaining mortgage loans for which they were not suited and could not afford.

- In *State of West Virginia v. Countrywide Financial Corp.,* the West Virginia Attorney General has asserted civil claims against Countrywide alleging violations of state unfair competition statutes.

174. On October 6, 2008, these seven states, plus 23 others, all joined in a settlement with Bank of America, pursuant to which Bank of America (as the successor-in-interest to the Countrywide Defendants) agreed to pay $150 million for state foreclosure relief programs and loan modifications for borrowers totaling $8.4 billion.

175. On August 4, 2011, New York Attorney General Eric T. Schneiderman moved to intervene and object to Bank of America's proposed $8.5 billion settlement with Bank of New York Mellon ("BoNY") related to 530 RMBS underwritten by Countrywide and for which BoNY served as Trustee. The NYAG seeks to intervene "to protect the marketplace and the interests of New York investors," in part because the NYAG's investigation found that Countrywide and Bank of America "face Martin Act liability because there are repeated false representations in the Governing Agreements [for RMBS] that the quality of the mortgages sold into the Trusts would be ensured." In addition, Countrywide and Bank of America face liability for "persistent illegality" in violation of Executive Law § 63(12) for "repeatedly breached representations and warranties regarding loan quality."

(a) Countrywide Schemes to Increase Its Market Share But Pledges Continued Rigorous Underwriting

176. In the face of fierce competition from other originators, Countrywide witnessed remarkable growth from 2003 to 2007. Countrywide's growth was fueled by its success in pooling residential mortgages, "securitizing" the pool by issuing securities backed by it, and then selling the securities to investors. By March 31, 2008, Countrywide was the largest originator

and servicer of mortgage loans in the country. In the first quarter of 2008 alone, despite a sharp decline in residential home sales, Countrywide originated $73 billion in mortgage loans and serviced and administered $1.5 trillion of residential loans—generating $1.4 billion in total revenues.

177. Countrywide's rapid expansion was not accidental, but rather the result of a concerted effort on the part of Countrywide executives, including Angelo Mozilo, Countrywide Financial's co-founder and CEO, and David Sambol, who ran Countrywide's loan production machine as President and Chief Operating Officer of Countrywide Home Loans. Around May 2003, Sambol became particularly close to Mozilo and emerged as a major force within Countrywide Financial and Countrywide Home Loans, taking complete charge of loan production in 2004. Countrywide executives, and Sambol in particular, sent a clear message to loan origination and underwriting employees that overall volume was far more important than creditworthiness. Rather than relying on its publicly stated underwriting standards to maintain Countrywide's profitability, Sambol argued that by originating and procuring a large volume of loans, regardless of their relative risk, Countrywide would be able to cover any losses incurred on the riskier loans by the profits it generated on other loans.

178. In a conference call with analysts in 2003, Mozilo made Countrywide's market share objectives explicit, stating that his goal for Countrywide Financial was to "dominate" the mortgage market and "to get our overall market share to the ultimate 30% by 2006, 2007." At the same time, Countrywide made public assurances that its growth in originations would not compromise its strict underwriting standards. Indeed, Mozilo publicly stated that Countrywide would target the safest borrowers in this market in order to maintain its commitment to quality:

"Going for 30% mortgage share here is totally unrelated to quality of loans we go after.... There will be no compromise in that as we grow market share. Nor is there a necessity to do that."

179. Throughout the relevant time frame, Countrywide continued to reassure its shareholders and investors in its RMBS, like AIG, that its underwriting procedures and credit risk management remained highly rigorous. For example, in its 2005 10-K, Countrywide represented that:

> [Countrywide] ensure[s] . . . ongoing access to the secondary mortgage market by consistently producing quality mortgages and servicing those mortgages at levels that meet or exceed secondary mortgage market standards . . . . [W]e have a major focus on ensuring the quality of our mortgage loan production and we make significant investments in personnel and technology to support the quality of our mortgage loan production.

180. In particular, Countrywide touted its underwriting guidelines, claiming to ascertain facts about "borrower and collateral quality" including applicant assets and liabilities, income, employment history, and other demographics and personal information, as well as a full property appraisal. Countrywide claimed that it obtained all applicable income, liability, asset, employment, credit, and property information, on the basis of which it ascertained debt-to-income ratios (the ratio of a borrower's total monthly debt obligations to gross monthly income), LTV ratios, and CLTV ratios. Because the guidelines are ostensibly designed to ensure that loans perform over time, Countrywide knew that the quality of its guidelines—and its adherence to them—would materially affect the risks of investing in or guaranteeing its securitizations.

181. Throughout Countrywide's expansion, Mozilo consistently represented that Countrywide would not sacrifice the strict and disciplined underwriting standards that had made it an industry leader in responsible lending. During a March 15, 2005 conference with analysts, Mozilo responded to a question about Countrywide's strategy for increasing market share, and again assured Countrywide's constituents:

> Your question is 30 percent, is that realistic, the 30 percent goal that we set for ourselves 2008? . . . Is it achievable? Absolutely . . . But I will say this to you, that under no circumstances will Countrywide ever sacrifice sound lending and margins for the sake of getting to that 30 percent market share.

182. Other Countrywide senior officers echoed that Countrywide had not, and would not, loosen its underwriting standards. For example, in an April 2005 conference call with analysts, Eric Sieracki, Countrywide's Chief Financial Officer, responding to a question asking whether Countrywide had changed its underwriting protocols, said: "I think they [FICO scores, combined loan-to-value and debt-to-income ratios] will remain . . . consistent with the first quarter and most of what we did in 2004. We don't see any change in our protocol relative to the volume [of] loans that we're originating." In a July 2005 conference call, Sieracki further stated that as to the Countrywide-originated HELOCs: "The credit quality of our home equities should be emphasized here as well. We are 730 FICO on these home equities, and that's extraordinary throughout the industry."

183. Contrary to its public assurances, Mozilo's mandate of a 30% market share required Countrywide to systemically depart from its underwriting standards and this resulted in a "culture change" starting in 2003. A former senior regional vice president of Countrywide was quoted in a [January 17, 2008] *Business Week* article as saying that Countrywide "approached making loans like making widgets, focusing on cost to produce and not risk or compliance. Programs like 'Fast and Easy' where the income and assets were stated, not verified, were open to abuse and misuse. The fiduciary responsibility of making sure whether the loan should truly be done was not as important as getting the deal done." Indeed, in an interview with the FCIC, Mozilo stated that a "gold rush" mentality overtook the housing market during the relevant time frame, and that he was swept up in it.

184. In November 2007, Countrywide prepared an internal post-mortem analysis that included observations from interviews of Countrywide's employees and culminated in an internal presentation. In this analysis, Countrywide admits that it was singularly focused on market share:

- "We were driven by market share, and wouldn't say 'no' (to guideline expansion)."
- "The strategies that could have avoided the situation were not very appealing at the time. Do not produce risky loans in the first place: This strategy would have hurt our production franchise and reduced earnings."
- "Market share, size and dominance were driving themes . . . . Created huge upside in good times, but challenges in today's environment. Net/net it was probably worth it."

(b) Countrywide Cedes Its Underwriting Policy to the Market's Lowest Common Denominator Through Its "Matching" Mandate

185. To increase its market share, Countrywide instituted an aggressive "matching" program that effectively ceded its "theoretical" underwriting standards to the market and resulted in a proverbial race to the bottom. Under Countrywide's "matching" policy, Countrywide would match any product that a competitor was willing to offer. A former finance executive at Countrywide explained: "To the extent more than 5 percent of the [mortgage] market was originating a particular product, any new alternative mortgage product, then Countrywide would originate it . . . . [I]t's the proverbial race to the bottom."

186. Countrywide's matching policy did not, however, end with the particular mortgage products offered on the market. Instead, Countrywide mixed and matched the individual *terms* offered by multiple lenders, taking the worst of each. The resulting composite offering was thus *even more* aggressive than that of any one competitor who had a particular

feature matched. Countrywide's aggressive mortgage products resulted in "layered" risks created by its undisclosed "matching" philosophy.

187. The testimony of Frank Aguilera, a Managing Director responsible for risk management, confirms that Countrywide followed a "matching strategy." To support this strategy, Countrywide created a large database of products offered by competitors so that if somebody tried to convince Countrywide to approve a new product all it had to do was to check the database to see if someone else had already approved it. Aguilera testified that he did not think investors were aware of Countrywide's internal "matching" strategy.

188. Aguilera further testified that he was "surprised" that this strategy was deployed not just to the more well-developed prime loans, but also to riskier subprime loans. He stated that "from a credit perspective, my view, it's not a tolerable process." Aguilera raised his concerns formally with at least two other managers at Countrywide.

189. Countrywide's Chief Risk Officer John McMurray also expressed concerns about the "composite" effects of Countrywide's "matching strategy." In a November 16, 2006 e-mail to Sambol and Bartlett, McMurray wrote: "The most widely held belief is that our guiding principle is simply doing what anyone else in the market is doing: if it's in the market, we have to do it." He testified:

> [I]f you match one lender … on certain guidelines for certain products and then you match a separate lender on a different product or a different set of guidelines, then in my view the composite of that - of that two-step match would be more - would be more aggressive than either one of those competitor reference points viewed in isolation.

McMurray further testified that he was concerned about "companion mitigants" that would allow competitors to use the products Countrywide was matching only because they had additional terms not in Countrywide's system, such as additional credit history requirements. In short, "the

chief concern on [the matching strategy] is that some of your risk standards get ceded to other institutions by following that strategy. That is my chief concern."

190. McMurray testified he agreed that whether Countrywide was "ceding our credit policy to the most aggressive players in the market" was a "serious concern," and that he raised this issue with others within Countrywide. Indeed, in a November 2, 2006 e-mail to Kevin Bartlett, Countrywide's Chief Investment Officer, McMurray directly asked whether Countrywide "want[s] to effectively cede" its underwriting policies to the market. This e-mail was then forwarded to Sambol.

191. In its November 2007 "Lessons Learned" post-mortem analysis, Countrywide repeatedly admitted that the "matching" strategy led to product development far outpacing its risk-assessment procedures and misaligned the incentives of its employees:

- "With riskier products, you need to be exquisite in off-loading the risk. This puts significant pressure on risk management. Our systems never caught up with the risks, or with the pace of change."

- "Risk indicators and internal control systems may not have gotten enough attention in the institutional risk and Board committees."

- "Not enough people had an incentive to manage risk."

- "Decentralized and local decision making were another characteristic of our model . . . . The downside was fewer risk controls and less focus on risk, as the local decision makers were not directly measured on risk."

- "Our wide guidelines were not supported by the proper infrastructure (credit, risk management). We need to take a longer-term view of decisions, and do a better job of vetting risk."

- "[W]e did not put meaningful boundaries around the [broad product] strategy, even when our instincts might have suggested that we do so, and we allowed the model to outrun its critical support infrastructure in investment and credit risk management . . . . Our risk management systems were not able to provide enough counterbalance . . . ."

- "The focus of production was volume and margin, not credit risk. There was also massive emphasis on share."

- "Structure and capabilities of credit/secondary not in-sync with production."

192. Mozilo himself has stated that he witnessed the mortgage industry's lending standards "come unglued" during the relevant time frame. In his testimony to the SEC, Mozilo admitted that "[i]f the only reason why you offered a product, without any other thought, any other study, any other actuarial work being done is because somebody else was doing it, that's a dangerous game to play." Yet Countrywide stuck to its "matching" strategy in order to increase loan volume and gain market share.

(c) Countrywide's Use of "Exceptions" Guaranteed that Virtually Every Loan Would Be Approved

193. Countrywide implemented its "matching" program through the widespread use of "exceptions" to its stated underwriting guidelines. This guaranteed that virtually every loan would be approved. Unknown to AIG and contrary to Defendants' representations, these exceptions were not based on any countervailing compensating factors. Instead, exceptions were granted merely to allow Countrywide to "match" what competitors were offering, and because Countrywide believed the loans could be sold in the secondary market to investors like AIG. The evidence shows that Countrywide abandoned its underwriting guidelines in favor of an "exceptions" based system at the same time that Countrywide was originating the mortgage loans underlying AIG's certificates.

194. Countrywide deployed its "matching" strategy by expanding the number of employees who could grant exceptions throughout the underwriting process. A wide range of employees received authority to grant exceptions and to change the terms of a loan, including underwriters, their superiors, branch managers, and regional vice presidents. In this way, even if Countrywide's computer system recommended denying a loan, an underwriter could override that denial by obtaining permission from his or her supervisor.

195. According to the SEC, Countrywide created an underwriting process that incorporated at least four ways loans could be approved. First, loans were processed by an automated system that would either approve the loan or refer it to manual underwriting. Second, if the automated system recommended denying the loan, a manual underwriter would then seek to determine if the loan could be approved under his or her exception authority. Third, if the loan exceeded the underwriter's exception authority, it was then referred to the Structured Lending Desk, where underwriters with broader exception authority attempted to get the loan approved. Fourth, if all prior attempts to find an "exception" failed, it would be referred to the Secondary Markets Structured Lending Desk, where the sole criterion for approving a loan was whether it could be sold on the secondary market.

196. Countrywide routinely approved "exception" loans that did not satisfy even Countrywide's weakened "theoretical" underwriting criteria through a high-volume computer system called the Exception Processing System—but only after Countrywide charged these high risk borrowers extra points and fees. Countrywide made enormous profits from these higher fees. The Exception Processing System was known to approve virtually every borrower and loan profile with a pricing add-on when necessary, and was known within Countrywide as the "Price Any Loan" system.

197. According to the California Attorney General's complaint against Countrywide and Mozilo, a former supervising underwriter at Countrywide stated that up to 15% or 20% of the loans that Countrywide generated were processed via the Exception Processing System, of which very few were ever rejected. One former Countrywide employee remarked that he could "count on one finger" the number of loans that his supervisors permitted him to reject as an underwriter with Countrywide's Structured Loan Desks.

198. According to the SEC, in mid 2006 attendees at an internal credit meeting were informed that one-third of the loans referred out of Countrywide's automated underwriting system violated "major" underwriting guidelines, 23% of the subprime first-lien loans were generated as "exceptions," and that "exception" loans were performing 2.8 times worse than loans written within guidelines. That the loans approved by exceptions were performing so much worse than other similar loans is itself strong evidence that the "exceptions" were not being granted based on any purported countervailing circumstances in the borrowers' credit profile.

199. According to the SEC, Countrywide's culture of "exceptions" started at the top, with Mozilo personally approving loans by way of guideline exceptions pursuant to a "Friends of Angelo" program. And Mozilo and Sambol personally authorized the establishment of the exception-based Structured Loan Desk in Plano, Texas to grant exceptions from the underwriting guidelines that Countrywide told the public it followed.

200. In his testimony to the SEC, Chief Risk Officer McMurray admitted that Countrywide's "matching strategy" was a "a corporate princip[le] and practice that had a profound effect on credit policy." In fact, he thought it was not possible to understand Countrywide's underwriting policies without understanding the matching strategy, and that the strategy was rolled out by use of "the exception desks," which happened "routinely." McMurray also agreed that the use of exceptions, even as a general matter, made the process more risky: "Almost by definition, you are dealing with a riskier transaction" when the loan is approved by an exception, and, in fact, there were areas where his group found a "big disparity" in performance between "exception" loans and others. Again, that the "exception" loans were

performing so much worse is strong evidence that the exceptions were not being used based on countervailing positive features of the borrower's credit profile.

201. McMurray also admitted that underwriting "guidelines … were expanding" at Countrywide from September 2003 and the middle of 2007—*i.e.*, throughout the period when Countrywide was originating and securitizing the mortgage loans underlying AIG's investments. This guideline "drift" was a concern of his because "even if you undertake measures to transmit that risk outside the company, you're still starting with more risk that needs to be distributed." He admitted that "the idea of risk being sold off … was a key part of Countrywide's strategy." McMurray conceded in his testimony that "there's [a] relationship between expanding underwriting guidelines and a probability of a loan going to default or serious delinquency." McMurray testified that he shared his concerns about this correlation with others at Countrywide, including Mozilo, Sambol, and Sieracki.

202. Frank Aguilera, a Countrywide Managing Director responsible for risk management, also confirmed that Countrywide's "matching" strategy was implemented through the "exception" process. Indeed, Aguilera testified that "90 percent" of his time as the person responsible for Countrywide's "technical manuals" was spent on "expansions" of the guidelines. Aguilera also testified about the "particularly alarming" results of an internal review on June 12, 2006. He reported to others in Countrywide that 23% of the subprime loans at the time were generated as exceptions, even taking into account "all guidelines, published and not published, approved and not yet approved." Aguilera wrote at the time that "[t]he results speak towards our inability to adequately impose and monitor controls on production operations." The exception rate for "80/20" products (which are particularly risky because they provide 100% financing)

was even higher. AIG's certificates included many such loans. The CWHL 2005-19, CWHL 2006-11, and CWHL 2006-8 deals that AIG invested in, for example, included such 80/20 loans.

203. In February 21, 2007 Aguilera disputed a belief stated by someone else in a prior meeting that there were adequate controls with regard to exceptions in certain areas, and stressed how the guidelines were meaningless when so many exceptions were being granted: "Our review of January data suggests that these controls need to be reviewed. Any Guideline tightening should be considered purely optics with little change in overall execution unless these exceptions can be contained."

204. As an example, Aguilera provided data on loans that were approved as "exceptions" despite having high loan-to-value ratios. He found "significant levels of exceptions" under "all high risk programs." Full Spectrum Lending, Countrywide's subprime-mortgage affiliate was singled out for "in particular exceed[ing] any imaginable comfort level." Aguilera's e-mail highlighted that 52% of 100% LTV loans by Full Spectrum Lending were issued by way of "exceptions." Overall, 37% of such loans studied required "exceptions."

205. Countrywide used exceptions to make loans to individuals with a high risk of default. During a March 12, 2007 meeting of Countrywide's Credit Risk Management Committee, the Risk Management department reported that 12% of Countrywide loans that were reviewed internally were rated "severely unsatisfactory" or "high risk" because the loans had loan-to-value ratios, debt-to-income ratios, or FICO scores outside of Countrywide's already-liberal underwriting guidelines. And, according to the SEC, on May 29, 2007 Sambol and Sieracki attended a Credit Risk Committee Meeting, in which they were informed that "loans continue[d] to be originated outside guidelines," primarily via the Secondary Structured Lending Desk without "formal guidance or governance surrounding" the approvals. In a December 13,

2007 internal memo from Countrywide's enterprise risk assessment officer to Mozilo, the officer reported that Countrywide had re-reviewed mortgages originated by Countrywide in 2006 and 2007 "to get a sense of the quality of file documentation and underwriting practices, and to assess compliance with internal policies and procedures." Countrywide found that "borrower repayment capacity was not adequately assessed by the bank during the underwriting process for home equity loans."

206. Ultimately, Countrywide's exception policy was designed to ensure that all loans were approved. For example, in an April 14, 2005 e-mail chain, various managing directors were discussing what FICO scores Countrywide would accept. One Managing Director wrote that the "spirit" of the exception policy was to "provide flexibility and authority to attempt to approve all loans submitted under an approved program/guideline which are later determined to be outside." He continued: "I would argue that the [exception] policy would also contemplate more general exceptions such as . . . to keep pace with fast changing markets prior to submitting a formal product change."

207. Another internal Countrywide document described the objectives of Countrywide's Exception Processing System to include "[a]pprov[ing] virtually every borrower and loan profile," with "pricing add on" (*i.e.*, additional fees) if necessary to offset the risk. The objectives also included providing "[p]rocess and price exceptions on standard products for high risk borrowers." In his testimony to the SEC, Sambol identified a February 13, 2005 e-mail he wrote that similarly said that the "purpose of the [Structured Loan Desk] and our pricing philosophy" should be expanded to so that "we should be willing to price virtually any loan that we reasonably believe we can sell/securitize without losing money, even if other lenders can't or won't do the deal."

(d) Through Countrywide's Matching Program and Its Use of Exceptions, "Saleability" Became the Sole Criteria Used to Approve a Loan

208. Through its matching program and use of exceptions, Countrywide effectively abandoned its stated underwriting guidelines. Instead, "saleability"—that is, whether a loan could be sold on the secondary market—was the sole factor governing whether a loan would be approved. Unknown to AIG, the only underwriting principles at work within Countrywide were: (1) is another company doing it, and/or (2) can we sell it. Countrywide applied this criteria at the same time when many of the mortgage loans underlying AIG's certificates would have been or were about to be generated.

209. In his interview with the Financial Crisis Inquiry Commission, Sambol was explicit that Countrywide was "selling virtually all of its production to Wall Street in the form of mortgage-backed securities or in the form of mortgage whole loans." Countrywide's essential business strategy was "originating that which was saleable into the secondary market."

210. Nathan Adler, the President of many of the Depositor Defendants here, confirmed that "saleability" was the key metric and testified before the SEC about the "evolution" of the Structured Loan Desk. He testified that Countrywide's exception policy had "core guidelines." If those were not met, the company also had "shadow" guidelines. If even those were not met, the loans were given to "Secondary Marketing to determine if the loan could be sold given the exception that was being asked for." Thus "saleability" was a "factor in the determination of whether to make a loan on an exception basis." Indeed, by the time the loan reached Adler whether the loan could be sold in the secondary market was "the only criteria that [Countrywide] followed."

211. Similarly, in June 2007, Countrywide's Executive Vice President of Credit Risk Management Christian Ingerslev provided a "granular performance assessment of 2006 Vintage

Non-Conforming 1st lien loans that have been (or should be) going to the Secondary [Structured Loan Desk] for exception approval . . . plus loans that [Correspondent Lending Division] is buying in bulk outside the guidelines." In other words, Ingerslev was reviewing the type of loans that were all being done outside of Countrywide's already liberal underwriting standards. In this report, Ingerslev wrote: "There is currently no formal policy or agreed upon process which identifies what Secondary can or should price, other than what they have identified as 'unsaleable' (same goes for CLD bulk bids). While I've asked, I have not seen a comprehensive list of what they are saying no to."

212. Ingerslev directed his report to Chief Investment Officer Kevin Bartlett, commenting: "I understand you are directing a project to make Production's theoretical requirement to underwrite a reality. Under that scenario, should the line in the sand still be 'unsaleable'? After looking at the performance, it's hard to recommend anything other than no. Heretofore that has been a challenging edict for Credit to implement (for obvious reasons) and the outcry is to just price the risk - regardless of performance."

(e) Countrywide Abused the No-Documentation Loan Process and Falsified Loan Applications

213. Another way Countrywide found to get around its "theoretical" underwriting policies was through the systematic abuse of no- and low-documentation loan processes. With these type of loan products, the borrower is not required to provide the normal confirmations and details for credit criteria such as annual income or current assets. Low-documentation mortgages were originally designed for professionals and business owners with high credit scores, who preferred not to disclose their confidential financial information. Traditionally, these loans also required low loan-to-value ratios. Countrywide repeatedly represented to investors like AIG that

risky products such as low-documentation loans adhered to these traditional guidelines by making these products available to only to the most sophisticated and creditworthy borrowers.

214. To the contrary, low-documentation loans were instead used as a tool to get around Countrywide's "theoretical" underwriting standards. When a loan officer knew an application would not be approved on the basis of the applicant's actual financial condition, the officer often steered applicants into low-documentation products. Once in those programs, Countrywide coached borrowers on how to falsify the application to ensure it would be approved, and in some instances would even fill out the required misrepresentations without the borrower's knowledge. Countrywide's abuse of these alternative-documentation procedures is directly relevant to AIG's certificates, which often included a significant quantity of loans approved through these procedures.

215. In a June 2006 e-mail chain that included both McMurray and Sambol, Countrywide circulated the results of an audit it had conducted. Among the findings were that "approximately 40% of the Bank's reduced documentation loans . . . could potentially have income overstated by more than 10% and a significant percent of those loans would have income overstated by 50% or more." McMurray admitted that was "obviously the case" that "perhaps many" of these overstatements were the result of misrepresentations. Another Countrywide Risk Officer, Clifford Rossi, agreed, testifying to the SEC that "the vast majority" of the overstated income amounts was "likely" due to misrepresentations. This analysis of misstatements in the applications for reduced-documentation loans is highly relevant to AIG's certificates, because the analysis was conducted at the same time many of the mortgage loans at issue here were generated, and because many of the mortgage loans were issued on a reduced-documentation basis.

216. In addition to outright fabrication of information, Countrywide also failed to confirm that the information being provided to it by loan applicants was accurate. For full-documentation loans, Countrywide failed to verify that asset and income information being provided to it by borrowers was accurate, as required under those programs. Moreover, according to the California Attorney General's complaint against Countrywide and Mozilo, a former supervising underwriter at Countrywide explained that the company declined to check bank balances for applicants applying for stated-income, stated-asset loans that provided account information. Countrywide also had the right to verify the income stated on a loan application by use of Internal Revenue Service data, but only 3% to 5% of the loans that Countrywide issued by 2006 were checked.

217. For stated-income loans, where Countrywide promised that it would exercise discretion, during the 2005-2006 period the company directed loan officers to support their assessments by referring to the website www.salary.com. Again, this period covers many of the loans that would have collateralized AIG's certificates. This practice was reported by former employees cited in the Illinois Attorney General's complaint against Countrywide. The website did not provide specific salary information for any particular borrower, but provided a range of salaries for particular job titles based upon the borrower's zip code. And even when the stated salaries were outside the ranges, Countrywide did not require its employees to follow-up with the borrower.

218. The Federal Home Loan Bank of Indianapolis studied the information it was able to obtain from loan servicing companies regarding the loans underlying many of its investments. It found that Countrywide had overstated by 18% the number of underlying loans that were underwritten pursuant to the much lower risk, full-documentation procedures. This study

included a Countrywide transaction that included loans being originated at the same time as the mortgage loans underlying AIG's certificates and approved pursuant to the same purported underwriting standards.

219. **Former employees confirm that Countrywide abused the no- and low-documentation loan process and falsified loan applications.** Mark Zachary is a former Regional Vice President of Countrywide who claims he was fired for airing his concerns about Countrywide's underwriting practices. He told Larry King of CNN that if a borrower did not qualify for a conventional loan, Countrywide's loan officers would often steer the borrower into the so-called "liar loans"—riskier loans that did not require documentation,

220. On February 13, 2007, Zachary e-mailed one of his supervisors, the Senior Vice President Divisional Manager of Countrywide KB Home Loans, and stated that "it seems to be an accepted practice for [Countrywide] to have a full doc loan and then if it can't be approved … we flip to a stated[-income loan] and send to FSL [Full Spectrum Lending, Countrywide's subprime-mortgage affiliate] under non-prime (sub-prime business unit)."

221. Once in the low-documentation process, "the income stated on those loans generally was not a true representation of what the person normally makes." Zachary confirmed that Countrywide employees were coaching applicants to lie, including overstating their income by as much as 100% to qualify for a loan. According to Zachary, loan officers would coach potential homeowners on the income levels needed to qualify for a given mortgage loan and would then accept revised loan applications from those borrowers which contained an inflated reported income.

222. Other former employees have similarly disclosed that Countrywide coached borrowers how to falsify their low- or no-documentation loan applications in order to circumvent

the normal underwriting process. For instance, a former Countrywide loan officer described in the California Attorney General's complaint against Countrywide reiterated the fact that borrowers were coached on how to lie. He explained that a loan officer might say, "with your credit score of X, for this payment, and to make X payment, X is the income you need to make." And NBC News reported that it spoke to six other former Countrywide employees, who worked in different parts of the country, who described the same "anything goes" corrupt culture and practices. Some of those employees even said that borrowers' W-2 forms and other documents were falsified to allow for loan approval. One employee stated that "I've seen supervisors stand over employees' shoulders and watch them . . . change incomes and things like that to make the loan work."

223. One Countrywide employee estimated that approximately 90% of all reduced-documentation loans sold out of the employee's Chicago office had inflated incomes. One of Countrywide's mortgage brokers, One Source Mortgage Inc., routinely doubled the amount of the potential borrower's income on stated income mortgage applications. Similarly, according to a confidential witness relied on by plaintiffs in other actions, as much as 80% of the loans originated by Countrywide out of its Jacksonville processing center between June 2006 and April 2007—*i.e.*, when many of the loans at issue here were being generated—had significant variations from Countrywide's theoretical underwriting standards.

224. **Borrowers confirm that Countrywide falsified loan applications and encouraged them to falsify their loan applications.** Julie Santoboni, who took out a Countrywide mortgage on her family's home in Washington, D.C., was interviewed on National Public Radio. She explained that she has owned several homes and that she and her husband are professionals. Nonetheless, when the family reached out to Countrywide to refinance their

home's adjustable-rate loan, a Countrywide loan officer pressured her to lie about her income to obtain a more attractive loan, since she had taken off two years of work for her children. The employee said that he could increase her husband's listed income, that the underwriters would not question the income because her husband's job title included the word "manager," and that the employee's boss would also not verify the stated income.

225. Santoboni also said that the Countrywide loan officer wanted her to write a letter stating she made $60,000 during each of the past two years and get her accountant to sign it, even though that would have been fraudulent, since she had no income. The loan officer continued to give her a "hard sell," pressuring her to lie about her income in order to obtain a more favorable interest rate on the loan. Santoboni followed up with Countrywide to complain about the incident but received no response as of the time of the interview. She made a complaint with the Federal Office of Thrift Supervision about the wrongdoing.

226. Another Countrywide borrower, Bruce Rose, described obtaining a mortgage loan from Countrywide that stated his monthly income as $12,166, as he realized only later, even though his income at the time was only around $16,000 a year.

227. One borrower told NBC News that her Countrywide loan officer told her to claim she made more than twice her actual income in order to gain approval for her loan.

228. A potential Countrywide customer known to Zachary complained to Countrywide in a September 19, 2006 e-mail: "I was told that my loan had been turned over to Countrywide's internal fraud department for review because a loan officer increased my income figures without authorization in order to get me approved for the stated-income loan. I was told by several people at Countrywide that this was done just to get me qualified and that nobody would check on it."

229. According to Francisco San Pedro, the former senior vice president of special investigations, Countrywide had about 5,000 internal referrals of potentially fraudulent activity in its mortgage business in 2005, 10,000 in 2006, and 20,000 in 2007. The company, however, filed only 850 Suspicious Activity Reports ("SARs") to the Financial Crimes Enforcement Network in 2005, 2,895 in 2006, and 2,621 in 2007. (FCIC Report, at 162).

(f) Countrywide Ignored Its Internal Risk Department Who Warned That Underwriting Standards Had Been Abandoned

230. Throughout the relevant time period, Countrywide's internal risk department expressed serious concerns about the company's wholesale abandonment of its stated underwriting guidelines. In particular, John McMurray, Countrywide's Chief Risk Officer, and Christian Ingerslev, Countrywide's Executive Vice President of Credit Risk Management, repeatedly warned Mozilo, Sambol, and other Countrywide executives that the company's matching strategy and use of exceptions resulted in riskier loans with high default rates. Countrywide, however, ignored the risk department's many warnings and continued with its efforts to increase market share and loan volume.

231. As early as 2005, McMurray warned Sambol that loans which were originated as exceptions to Countrywide's stated origination guidelines would likely experience higher default rates. On May 22, 2005, he wrote that "exceptions are generally done at terms even more aggressive than our guidelines" and recommended that "[g]iven the expansion in guidelines and growing likelihood that the real estate market will cool, this seems like an appropriate juncture to revisit our approach to exceptions." McMurray also warned Sambol that "as a consequence of [Countrywide's] strategy to have the widest product line in the industry, we are clearly out on the 'frontier' in many areas," adding that that "frontier" had "high expected default rates and losses." He told Sambol that because of the "matching" strategy, Countrywide's guidelines "will be a

composite of the outer boundaries across multiple lenders," and that the resulting "composite guides [sic] are likely among the most aggressive in the industry."

232. McMurray continued to express concern throughout 2006 and 2007. Indeed, in a February 11, 2007 e-mail to Sambol, McMurray reiterated his concerns about Countrywide's strategy of matching any type of loan product offered by its competitors, which he said could expose the company to the riskiest offerings in the market: "I doubt this approach would play well with regulators, investors, rating agencies[,] etc. To some, this approach might seem like we've simply ceded our risk standards . . . to whoever has the most liberal guidelines."

233. Mozilo himself even expressed concerns about the abandonment of Countrywide's underwriting guidelines. In an April 13, 2006 e-mail, Mozilo wrote to Sieracki and others that he was concerned that certain subprime loans had been originated "with serious disregard for process [and] compliance with guidelines," resulting in the delivery of loans "with deficient documentation":

> I want Sambol to take all steps necessary to assure that our origination operation "follows guidelines" for every product that we originate. I have personally observed a serious lack of compliance within our origination system as it relates to documentation and generally a deterioration in the quality of loans originated versus the pricing of those loan[s]. In my conversations with Sambol he calls the 100% sub prime seconds as the "milk" of the business. Frankly I consider that product line to be the poison of ours. Obviously as CEO I cannot continue the sanctioning of the origination of this product until such time I can get concrete assurances that we are not facing a continuous catastrophe. Therefore I want a plan of action not only from Sambol but equally from McMurray as to how we can manage this risk going forward.

234. Yet when McMurray attempted to enforce a set of underwriting guidelines, his efforts were quashed, and his repeated warnings were ignored by Countrywide's senior executives. On February 9, 2006, McMurray circulated policy guidance expressing his concerns about Countrywide's matching strategy and use of exceptions and asked "should we really even be offering this product?" McMurray complained at the time that he was "continuing to

encounter resistance to my efforts and instructions to rein in this program." The next month, McMurray circulated a "Policy on High Risk Products." He wrote that there were also "many meetings and other conversations" where his concerns, as expressed in his draft policy, were discussed. On November 16, 2006, McMurray wrote to Sambol regarding the "fundamental deficiencies" within Countrywide with regard to risk and referenced his policy:

> First, we need to agree on a risk vision and guiding principles that the entire enterprise will follow. I previously created a set of guiding principles, but there hasn't been acceptance from some of the key business units. The most widely held belief is that our guiding principle is simply doing what anyone else in the market is doing; if it's in the market, we have to do it.
>
> Second, we should require everyone to follow established risk guidance and policies[;] a product cannot be rolled out or transactions closed without required approvals. There are several recent examples where products or transactions proceeded without the required risk approvals or in contradiction of established policy.

On September 7, 2007, over a year after circulating his proposed policy, McMurray conceded: "I was never supported on this and Secondary, Production, and CCM basically continued to operate as though they never received this policy."

235. McMurray also testified that he was aware that there were instances where his credit risk department would "reject[] proposals for new products and the people in sales nevertheless used the exceptions procedure to achieve the same result." He was "surprised, angry, and disappointed," for instance, when he found out that despite being previously rejected, Countrywide had advertising fliers promoting loans that had a low FICO requirement, only required a stated (non-documented) income, and provided 100% financing.

236. McMurray believed those loans were being issued through exceptions despite such a program being previously rejected by his team. More generally, he also testified that he was "fairly certain" he had conversations with others in Countrywide, including Sambol, about the fact that exceptions were being made without sufficient compensating factors.

237. Christian Ingerslev, Countrywide's Executive Vice President of Credit Risk Management, also warned Sambol and others about the consequences of Countrywide's failure to adhere to underwriting guidelines. In a November 16, 2006 e-mail, Ingerslev confirmed that internal documentation showed that products and transactions were even going forward "without the required risk approvals or in contradiction of established policy." He testified that there was no "systemic way" to stop this from happening because "you're talking about human beings, not systems." He also testified there was no "consequence or penalty" for originating loans that had not been signed off by McMurray. Instead, the sales team ruled at Countrywide. In a March 7, 2005 e-mail, Ingerslev complained:

> [S]ounds like they got on the line with the traders, and long story short, they now think they can sell them . . . . [I]t's frustrating to try and hold the line and then just be overridden with whining and escalations…. [J]ust reinforces that sales can have anything they want if they yell loud enough to [D]rew [Gissinger, President of Countrywide Home Loans].

(g) Countrywide's Inflated Appraisals Skewed Loan-to-Value Figures Reported to Investors Like AIG

238. Falsely overstated appraisals were a systemic problem within Countrywide's loan origination process. The overstated appraisals meant that the stated LTV ratios for the mortgage loans underlying AIG's certificates were false and misleading and contained omissions of material fact because they were based on inaccurate values. The properties' actual LTV ratios would have been much higher because the mortgaged properties' value was so frequently overstated.

239. Countrywide touted the mortgage loans' low LTV ratios, emphasizing that they were based on the use of "independent" appraisers. In fact, Countrywide Home Loans regularly engaged appraisers that were affiliated with Countrywide, including appraisers that were owned or controlled by Countrywide. This was done either directly or indirectly through intermediate

subsidiaries or otherwise subject to Countrywide's influence. This created a conflict of interest. As both originator and securitizer of the loans, Countrywide had an incentive to inflate the value of properties because doing so would result in lower LTV ratios. A lower LTV ratio would allow a loan to be approved when it otherwise would not be, and would appear less risky to AIG and other investors when it was sold into a securitization. But loans based on inflated appraisals are more likely to default and less likely to produce sufficient assets to repay the second lien holder in foreclosure.

240. Ingerslev himself thought it was an "intuitive" conclusion that loans with higher loan-to-value ratios have a higher risk of default. He testified:

> [People default] when an income disruption event happens in their lives . . . and when that unexpected event happens in people's lives, if they have an equity cushion in their home, they have something to sort of stem off the short-term problem . . . . If people were buying homes, you know, beginning without any cushion, they were going to be more susceptible to this income disruption event. And, again, this is intuitive sense based on my experience in the business and not necessarily analytical, but then when we attempted to model it, our modeling group attempted to model it, you know, we showed some more results where the expected default rates were going to be pretty high.

241. In practice, the appraisals were not intended to determine the adequacy of the collateral in the event of a default, but rather to ensure that a large volume of mortgages were rapidly originated, underwritten, and securitized with no regard to the value of the collateral. Countrywide did not genuinely believe the appraisal values used to calculate LTV and CLTV statistics because it knew that property values were being purposefully and baselessly inflated in order to increase the amount of money that could be given to a borrower.

242. In September 2006, Mark Zachary (former Regional Vice President of Countrywide), informed Countrywide executives that there was a problem with appraisals performed on KB Home properties being purchased with mortgage loans originated by Countrywide. According to Zachary, Countrywide executives knew that appraisers were

strongly encouraged to inflate appraisal values by as much as 6% to allow homeowners to "roll up" all closing costs. According to Zachary, this practice resulted in borrowers being "duped" as to the true values of their homes. This also made loans more risky because when values were falsely increased, loan-to-value ratios calculated with these phony numbers were necessarily incorrect.

243. Zachary brought his concerns to executives of the Countrywide/KB Homes joint venture, as well as Countrywide executives in Houston, Countrywide's Employee Relations Department and Countrywide's Senior Risk Management Executives. According to Zachary, Countrywide performed an audit investigating these matters in January 2007, and the findings of the audit corroborated his story. According to Zachary, the findings of this audit were brought to the attention of Countrywide executives.

244. According to Capitol West Appraisals, LLC, a company that has provided real estate appraisals to mortgage brokers and lenders since 2005, and is a "review appraiser" for Wells Fargo, Washington Mutual and other lenders, Countrywide Financial and Countrywide Home Loans engaged in a pattern and practice of pressuring even non-affiliated real estate appraisers to increase appraisal values artificially for properties subject to Countrywide Home Loans mortgages. Capitol West stated that Countrywide Home Loans officers sought to pressure Capitol West to increase appraisal values for three separate loan transactions. When Capitol West refused to vary the appraisal values from what it independently determined was appropriate, Countrywide Home Loans retaliated.

245. In particular, according to Capitol West, from at least 2004, and likely before, and continuing through at least 2007—*i.e.*, for the relevant period when the mortgage loans at issue here were being originated and securitized into the certificates—Countrywide Home Loans

maintained a database titled the “Field Review List” containing the names of appraisers whose reports Countrywide Home Loans would not accept unless the mortgage broker also submitted a report from a second appraiser. Capitol West was placed on the Field Review List after refusing to buckle under the pressure to inflate the value of the properties. No mortgage broker would hire an appraiser appearing on the Field Review List to appraise real estate for which Countrywide Home Loans would be the lender because neither the broker nor the borrower wanted to pay to have two appraisals done. Instead, the broker would simply retain another appraiser who was not on the Field Review List.

246. According to Capitol West, Countrywide Home Loans created certain procedures to further enforce its blacklisting of uncooperative appraisers like Capitol West. Specifically, if a mortgage broker were to hire an appraiser that happened to be on the Field Review List, Countrywide’s computer systems automatically flagged the underlying property for a “field review” of the appraisal by LandSafe, Inc., a wholly owned subsidiary of Countrywide Financial. LandSafe would then issue another appraisal for the subject property that, without exception, would be designed to “shoot holes” in the appraisal performed by the blacklisted appraiser such that the mortgage transaction could not close based on that appraisal. Indeed, according to Capital West, in every instance, LandSafe would find defects in the appraisal from the blacklisted appraiser, even if another, non-blacklisted appraiser had arrived at the same value for the underlying property and the non-blacklisted appraiser’s appraisal was accepted. According to Capitol West, this exact set of facts happened with respect to an appraisal it submitted after it was placed on the Field Review List.

247. Because Countrywide was one of the nation’s largest mortgage lenders, a substantial portion of any mortgage broker’s loans was submitted to Countrywide. Because a

broker could not rule out that Countrywide would be the ultimate lender, and because mortgage brokers knew from the blacklist that a field review would be required if a blacklisted appraiser were chosen, with the likely result that a mortgage would not be issued with that appraisal, and that its mortgage applicant would have to incur the cost of retaining another appraiser, such a broker had a strong incentive to refrain from using a blacklisted appraiser. By these means, Countrywide systematically and deliberately enlisted appraisers in its scheme to inflate appraisals and issue low-quality, extremely risky loans.

248. Several claims have been filed against Countrywide and related entities which describe individual homeowners' experiences with inflated property appraisals in obtaining mortgages from Countrywide. Such lawsuits include two class actions brought by homebuyers against KB Home, a building company that used Countrywide as its exclusive lender:

- *Zaldana v. KB Home*, No. 3:08-cv-03399 (MMC), currently pending in the United States District Court for the Northern District of California; and *Bolden v. KB Home*, No. BC385040, currently pending in Los Angeles County Superior Court.
- *Bolden v. KB Home* describes the experiences of Deborah and Lonnie Bolden, who purchased a KB Home residence in a new development in California's Central Valley. She obtained an appraisal on the property from LandSafe, Countrywide's in-house appraisal company. She also used Countrywide's in-house real-estate agents and mortgage brokerage. The property was appraised at $475,000. But a neighbor with an identical home was given an appraisal from an outside company, not affiliated with Countrywide, of $67,000 less.
- Bolden found that the outside company had based the appraisals on sales of comparable homes in the same subdivision, whereas an investigation at the county assessors' office showed that LandSafe had made its appraisal based on erroneous comparable-sales data,

using properties outside of the immediate area and properties in the development with misstated purchase prices, which artificially inflated her property's value. For example, the listed purchase price for one property in the development was $469,000 but its actual sale price was $408,000; another property's listed price was $480,500, instead of $410,000.

- Bolden says that KB Home, the Countrywide affiliate, never gave her a satisfactory answer. Another couple, David and Dolores Contreras, purchased a home in the same Countrywide-affiliated subdivision and made similar allegations that LandSafe overstated their property value based on comparisons to properties that were out-of-town, and thus not comparable, or inaccurately inflated. The appraisers' blatant misstatements make the inflated appraisals easy to identify.

249. Countrywide and its appraisal subsidiary, LandSafe, have also been sued by Fannie Mae and Freddie Mac investors for damages arising from inflated appraisals for property underlying mortgage packages sold to both Fannie Mae and Freddie Mac.

(h) Countrywide Encouraged Staff Through Compensation and Other Incentives To Put Borrowers Into Higher Risk Loans More Profitable to Countrywide

250. Riskier loans were more profitable for Countrywide because Countrywide charged higher fees on these loans. Brokers were thus incentivized to systematically encourage the use of riskier products. A former employee provided documents to the *New York Times* indicating that Countrywide's profit margins ranged from three to five percent on regular subprime loans, but on loans that included heavy burdens on borrowers, such as high prepayment penalties that persisted for three years, Countrywide's profit margins could reach as high as fifteen percent of the loan.

251. Because Countrywide had a higher incentive to originate higher-risk loans, it similarly incentivized its employees to do so. For instance, it paid employees who originated

loans in part based on the volume and dollar value of the loans they approved. A substantial portion of the salary of Countrywide's sales employees was based on commissions, which gave the employees a strong incentive to maximize sales volume and close the maximum number of mortgage loans regardless of quality. For example, Countrywide's wholesale account executives, the employees who dealt with brokers, were paid only on commission—they had no base salary.

252. Because of the higher origination fees charged with respect to nontraditional loans, employees and independent mortgage brokers were paid more when originating nontraditional loan products than when they originated standard loans. Former Countrywide mortgage brokers reported that brokers received commissions of 0.50% of the loan's value for originating subprime loans, while their commission was only 0.20% for less-risky loans. Moreover, adding a three-year prepayment penalty to a mortgage loan would generate an extra commission for the Countrywide employee of 1% of the loan's value. Persuading someone to add a home equity line of credit to a loan carried an extra commission of 0.25%.

253. Countrywide's senior management also imposed intense pressure on underwriters to approve mortgage loans, in some instances requiring underwriters to process 60 to 70 mortgage loan applications in a single day and to justify any rejections they made. This created an incentive not to review loans thoroughly but instead simply to rubber-stamp them "approved." That pressure even came from the most senior levels of management. According to the *Wall Street Journal*, a former executive reported that Sambol was "livid" at a 2005 meeting because call-center employees were not selling enough adjustable-rate mortgages, which began with "teaser" rates but quickly reset to higher rates and thus were highly profitable for Countrywide.

(i) Countrywide Developed Toxic "Exotic" Loan Products With Extreme Risk

254. To pump volume Countrywide developed "exotic" products for borrowers who could not afford the homes they owned. Mozilo himself characterized some of Countrywide's exotic products as "toxic," "poison," and "the most dangerous product in existence." Many of these exotic products made their way into AIG's certificates. In a May 7, 2007 letter to the Office of Thrift Supervision, Countrywide admitted: "Specifically looking at originations in the fourth quarter of 2006, we know that almost 60% of the borrowers who obtained subprime hybrid ARMs [from Countrywide] would not have qualified at the fully indexed rate." Countrywide also admitted that "almost 25% of the borrowers would not have qualified for any other [Countrywide] product."

255. Perhaps the most egregious of these products was the so-called pay-option ARM. In a pay-option ARM, the borrower can make a payment even less than that required to pay off accruing interest. In other words, the balance of the loan increases rather than decreases over time. If the borrower continues to pay less than the accrued interest, the amount of his or her payment is eventually reset, resulting in a sudden increase in the minimum payments—thus making it even more difficult for the homeowner to pay the mortgage he or she could not afford in the first place.

256. In a June 1, 2006 e-mail regarding pay-option ARMs, Mozilo warned Sambol and other executives that borrowers "are going to experience a payment shock which is going to be difficult if not impossible for them to manage." Mozilo's e-mails regarding pay-option ARMs are directly relevant here, because many of AIG's certificates included such loan products. Mozilo warned that "we know or can reliably predict what's going to happen in the next couple

of years." Mozilo reiterated his concern that the majority of pay-option ARMs were originated using stated income, and that evidence suggested that borrowers were misstating their incomes.

257. In a September 26, 2006 e-mail Mozilo admitted that with respect to pay-option ARMs "we are flying blind on how these loans will perform" in a stressed environment. Countrywide's Chief Risk Officer McMurray later would testify that he thought "you could generalize [this] observation to a much broader set of loans than just pay option."

258. To conceal its greatly increased production of subprime loans, Countrywide also employed an internal, undisclosed definition of prime versus subprime. As a result, in its public reports, Countrywide Financial classified loans as "prime" that clearly were subprime under well-established industry standards. A former senior underwriter at Countrywide reported that Countrywide regularly classified loans as "prime" even if they were issued to non-prime borrowers, including people who recently went through bankruptcy. According to the SEC, Countrywide included in the prime category loans with FICO scores below 620, and further included loan products with increasing amounts of credit risk such as reduced or no-documentation loans and pay-option adjustable-rate mortgages ("ARMs").

(j) Countrywide Admits to Using Adverse Selection in Pooling Loans, Keeping the Best Loans For Itself

259. Countrywide knowingly offloaded high risk assets on investors like AIG by selectively "cherry picking" high quality loans to keep on its balance sheet, while securitizing the riskier loans and selling them on the secondary market.

260. On August 2, 2005, Sambol actually questioned the company's policy of "cherry picking" the best loans for itself while leaving the higher-risk leftovers for securitization:

> While it makes sense for us to be selective as to the loans which the Bank retains, we need to analyze the securitization implications on what remains if the bank is only cherry-picking and what remains to be securitized/sold is overly concentrated with higher risk loans. This concern and issue gets magnified as we

> put a bigger percentage of our pay option production into the Bank because the remaining production then increasingly looks like an adversely selected pool.

261. Mozilo responded the same day:

> I absolutely understand your position however there is a price we will pay no matter what we do. The difference being that by placing less attractive loans in the secondary market we know exactly the economic price we will pay when the sales settle. By placing, even at 50%, into the Bank we have no idea what economic and reputational losses we will suffer not to say anything about restrictions placed upon us by the regulators.

262. McMurray testified that he also raised concerns about Countrywide's policy of picking the best loans to keep on its balance sheet:

> There's another element that we need to bring in here that's important with respect to securities performance. Countrywide's bank tended to - on - on some of the key products, tended to select the best loans out of the ones that were originated. By best - I'm talking about from a credit risk standpoint, so let me clarify that. So as - as those loans are drawn out of the population, what's left to put into the securities were not - are not as good as what you started out with, and then that can have an adverse effect on securities performance.

263. That Countrywide was "cherry-picking" the loans it would keep for itself was also confirmed by the testimony of Clifford Rossi, a Countrywide Risk Officer, who testified that the "bank was to originate and to cherry pick the better quality assets."

(k) Third-Party Due Diligence Firms Conclude that Countrywide Loans Are Defective

264. Investment banks performed due diligence on mortgages before purchasing them from originators. Prior to a loan auction, originators provided investment banks with bid sheets, which, among other things, dictated: (1) the percentage of the pool on which the investment banks would be permitted to conduct due diligence (*e.g.*, 25%); and (2) the number of loans the investment banks could "kick out" due to borrower deficiencies, payment delinquencies, early payment defaults, lack of documentation, and other problems. Prior to bid submission, originators also sent the investment banks spreadsheets known as loan tapes, which contained

various loan data. The investment banks were supposed to "crack" the loan tapes, analyze them, and determine what prices to bid for the loan pools. Once this "bid package" analysis was complete, the investment banks submitted their bids.

265. If the originator accepted a bid, the investment bank typically had a short period of time prior to the settlement date to conduct due diligence on the loans. The investment banks sometimes hired third-party due diligence firms such as Clayton Holdings, Inc. ("Clayton") or the Bohan Group ("Bohan") to conduct this review under their supervision.

266. Due to strong demand, originators such as Countrywide gained bargaining power over investment banks seeking to purchase mortgages and sponsor securitizations. One way originators exercised this bargaining power was to insist that investment banks limit their due diligence to smaller percentages of loans prior to purchase. If an investment bank chose to kick out a large number of loans from a pool (*e.g.*, because the loans failed to conform to the mortgage originator's guidelines or did not contain adequate documentation), it risked being excluded from future loan purchases. As a result, investment banks performed increasingly cursory due diligence on the loans they securitized.

267. Countrywide knew of the red flags raised by the due diligence conducted by Clayton and Bohan. As an originator, Countrywide was aware of the pressure on investment banks to scale back their due diligence and limit the number of loans kicked out of a securitization. In addition, Countrywide itself retained third-party due diligence firms such as Clayton to perform due diligence with respect to the securitizations it sponsored.

268. Congressional testimony by Clayton's Vice President Vicki Beal indicates that the investment banks determined the type and scope of review performed on the loan pools. Yet, rather than directing the firms to conduct thorough reviews that were more likely to identify

defective loans, the investment banks pressured the loan reviewers to disregard problematic loans through exceptions and offsets that did not satisfy the applicable underwriting guidelines.

269. Further compounding the problems, Clayton employees were instructed to review fewer loans in the loan pools as the securitization market grew. According to Beal's 2010 testimony, as the securitization markets grew even more frenzied Clayton's clients were only asking for samples of 5% of the loan pools. Showing how careless underwriters were when other people's money was at stake, according to the Los Angeles Times, Bohan President Mark Hughes contrasted these low figures with the 50% to 100% sample sizes consistently seen where loan buyers were keeping the loans for themselves.

270. As reported by the Los Angeles Times, Clayton and Bohan employees (including eight former loan reviewers who were cited in the article) "raised plenty of red flags about flaws so serious that mortgages should have been rejected outright—such as borrowers' incomes that seemed inflated or documents that looked fake—but the problems were glossed over, ignored, or stricken from reports." Ironically, while the investment banks pressured third-party reviewers to make exceptions for defective loans, they often utilized information about bad loans to negotiate for themselves a lower price for the pool of loans from the seller (*i.e.*, the originator). Indeed, according to September 2010 testimony before the FCIC by Clayton's former president, D. Keith Johnson, this was one of the primary purposes of the due diligence review.

271. Clayton provided the FCIC with documents showing the defect and waiver rates for some of the investment banks that retained Clayton to conduct loan pool due diligence. Clayton produced a report containing the rejection and waiver rates for loans originated by Countrywide. Those rates are as follows:

	1Q 2006	2Q 2006	3Q 2006	4Q 2006	1 Q 2007
Rejection rate	24%	23%	13%	14%	16%
Waiver rate	8%	14%	16%	11%	14%

272. The Clayton documents also include statistics on the rejection and waiver rates for loans Countrywide submitted to Clayton for review and that Countrywide was considering including in its own securitizations. Clayton's report reveals that from the fourth quarter of 2006 to the first quarter of 2007, 26% of the mortgages Countrywide submitted for potential inclusion in its securitizations were rejected, which included a finding by Clayton that the loans had been granted despite the lack of any purported compensating factors justifying an exception. Of the mortgages that Clayton rejected, 12% were subsequently "waived in" by Countrywide and included in securitizations like the ones in which AIG invested.

273. Nevertheless, Countrywide never disclosed to AIG that the due diligence conducted by Clayton and Bohan demonstrated that a substantial number of the loans in the pools backing Countrywide's securities were defective, that Countrywide had waived the defects as to a substantial number of the loans, or that the underwriters were using this information to negotiate a lower price for the loan pools.

(l) Analysis by Parties With Access to Actual Loan Files Shows that Countrywide Abandoned Its Underwriting Guidelines

274. Third parties with access to the complete loan files for certain Countrywide securitizations have performed additional analysis of the mortgage loans underlying Countrywide's offerings. These include, among others, MBIA Insurance Corporation ("MBIA") and Syncora Insurance Company ("Syncora"). Their analyses provide additional evidence that essential characteristics of the mortgage loans underlying the certificates were misrepresented,

that Countrywide omitted material information, and that the problems in Countrywide's underwriting practices were systemic.

275. MBIA is a New York-based monoline insurer that wrote insurance on certain Countrywide mortgage-backed securities offerings. After the financial meltdown, MBIA conducted an investigation into Countrywide's loan files after it was asked to make payments to certain other investors.

276. MBIA's analysis included at least six of the same deals in which AIG invested: CWL 2006-S8, CWL 2006-S9, CWL 2007-S1, CWL 2007-S2, CWL 2006-S10, and CWL 2007-S3.

277. In carrying out its review of the approximately 19,000 Countrywide loan files—including loans that were securitized and sold to AIG—MBIA found that 91% of the defaulted or delinquent loans in those securitizations contained material deviations from Countrywide's underwriting guidelines. MBIA's analysis shows that the loan applications frequently "(i) lack key documentation, such as verification of borrower assets or income; (ii) include an invalid or incomplete appraisal; (iii) demonstrate fraud by the borrower on the face of the application; or (iv) reflect that any of borrower income, FICO score, debt, DTI [debt-to-income,] or CLTV [combined loan-to-value] ratios, fails to meet stated Countrywide guidelines (without any permissible exception)." MBIA also found that the defective loans cover Countrywide's securitizations from 2004 to 2007. Because MBIA's findings show that Countrywide's violation of its underwriting guidelines was systemic, they are equally applicable to *all* of AIG's certificates.

278. Syncora, another insurance company that insured Countrywide's securitizations, has conducted a similar re-review analysis of defaulted loans in the securitizations that it insured

to determine whether the loans had been originated in accordance with Countrywide's representations. Syncora's analysis focused on two deals—CWHEL 2005-K and CWHEL 2006-D—both of which AIG also purchased and are at issue here. Syncora found that 75% of the loans it reviewed "were underwritten in violation of Countrywide's own lending guidelines, lack any compensating factors that could justify their increased risk, and should never have been made." Syncora's review is probative of the problems underlying AIG's certificates because it again shows Countrywide's failures during this period of 2005 to 2007 were systemic.

279. Syncora gave examples of individual loans that diverged from Countrywide's guidelines. The individual defective loans analyzed by Syncora reflected a long list of misstatements by Countrywide. Many loans violated the DTI ratios and LTV ratios set forth in Countrywide's underwriting guidelines, without adequate compensating factors to justify the increased risk of default, due in part to borrowers' exaggerated incomes and exaggerated property values. Loan amounts routinely exceeded the maximum amounts permitted under the Company's guidelines for each given borrower, based on a borrower's credit score, documentation, and property values. Countrywide also improperly issued loans to borrowers when their loan files lacked adequate documentation of borrowers' income, assets, credit, employment, cash reserves, or property values.

280. In its complaint against Countrywide, Syncora included several examples of these violations:

- One non-performing loan from the CWHEL 2006-D mortgage pool had a CLTV of 112% (when properly calculated using the lower of the purchase price or appraised value), whereas the maximum CLTV allowable under the applicable guidelines was 80%. In addition, the borrower claimed to make $13,500 a month as a realtor—an amount three times greater than the 90th percentile of the highest earning realtors in the area, based on data from salary.com. In other words, even if the borrower's salary was only a third of the stated amount, it would still be higher than the salary of 90% of comparable realtors in the area. A more realistic

income would have produced a debt-to-income ratio dramatically greater than permitted under the guidelines. In addition, the borrower had less than half of the minimum payment reserves required under the guidelines. Finally, the loan file lacked required documentation, such as the terms of the borrower's first lien and documents supporting the claimed property value.

- A loan from the CWHEL 2005-K mortgage pool was made to a borrower who claimed to make $13,520 monthly as a room service attendant in Atlantic City. The stated income was nearly five times greater than the 90th percentile for that occupation and location, based on the salary.com data. A more realistic income would have produced a debt-to-income ratio of 300%, six times greater than the guidelines' maximum of 50%. Even if the stated income were accurate, the loan would still have a debt-to-income ratio of 67% once the negative rents on the borrower's rental property were properly calculated.

- Another loan from the CWHEL 2006-D pool had a CLTV of 89.20%, exceeding the guidelines' maximum of 80%. The borrower claimed to make $17,250 monthly as an academic director of a charter school, even though that income was twice the 90th percentile income for that position in the area, based on the salary.com data. Even if the borrower's income were taken at face value, the debt-to-income ratio would have still exceeded the guidelines. In addition, the borrower's credit score was 11 points below the required minimum of 660. Finally, the borrower had payment reserves for only 2.9 months—less than half of the applicable guidelines' minimum.

- Another loan from the CWHEL 2006-D mortgage pool had a CLTV of 111% when properly calculated, even though the guidelines' maximum was 100%. The borrower's stated monthly income of $13,333 as an engineer was twice the 90th percentile of the engineers in the area, based on the salary.com data. A more realistic salary would have produced a debt-to-income ratio in excess of the guidelines' maximum. The borrower also failed to meet the guidelines-mandated reserves amount requirement.

- Another loan was made to a borrower who claimed to make $16,754 a month as a stylist—an amount five times greater than the 90th percentile for that occupation and that location, based on the salary.com data. In addition, the file lacked any verification of minimum assets or the required residence history. Finally, the file did not include an employment verification, even though such verification was required under the guidelines.

281. In addition, the Illinois Attorney General reviewed the sales of Countrywide loans by an Illinois mortgage broker and found that the vast majority of the loans had inflated incomes stated in the documentation, almost all without the borrowers' knowledge. This study covered the time period of 2004 to 2007, again the same time period during which Countrywide was

generating the loans at issue in this case. Likewise, a review of 100 stated-income loans by the Mortgage Asset Research Institute revealed that 60% of the income amounts were inflated by more than 50% and that 90% of the loans had inflated income figures of at least 5%. Again, this is highly probative of the problems underlying AIG's certificates as it covers the time period of 2004 to 2007.

(2) Merrill Ignored Its Underwriting Guidelines

282. Just like Countrywide, Merrill systematically abandoned its underwriting guidelines in its quest to increase loan volumes and the number of its RMBS securitizations, and therefore its profits. All the while, Merrill knew that it was selling RMBS that included toxic loans to investors like AIG, but proceeded anyway.

(a) Merrill Seeks To Increase Its Market Share

283. When the mortgage securitization business began to take off in the early 2000s, Merrill was not initially a dominant market player. In "league tables" that ranked top issuers of asset-backed securities (including RMBS) by volume, Merrill sat low in the rankings, outperformed by other institutions such as Royal Bank of Scotland, Morgan Stanley, Credit Suisse, Citigroup, Lehman Brothers, and Bear Stearns. (Paul Muolo & Matthew Padilla, *Chain of Blame: How Wall Street Caused the Mortgage and Credit Crisis*, at 186 (2008).)

284. In 2004, Merrill, led by then-Chief Executive Officer E. Stanley O'Neal, was determined to take aggressive action and to climb to the top of the league tables for asset-backed securities and in particular, RMBS. (*Id.* at 189.) O'Neal revamped his trading desk by hiring new people, including Michael Blum, who would lead Merrill's global asset-based finance operations, and George Davies, a trader whose task was to increase the volume of mortgage loans coming into Merrill's trading desks. (*Id.*)

285. With its securitization operations revamped, Merrill began buying up immense volumes of subprime mortgage loans. (*Id.*) With the competitive field more crowded with underwriters, Merrill began paying more for loans than every other firm on Wall Street. (*Id.*) Merrill also decided to use its other operations to entice subprime lenders to sell their loans to Merrill. (*Id.* at 190.) For example, Merrill began offering the subprime lenders "warehouse" financing (which the lenders needed to originate subprime mortgages) at very little or no cost so long as the lender continued to sell Merrill its subprime loans. (*Id.*) In other words, Merrill sacrificed its warehouse lending business for a bigger share of the securitization business. At the same time, Merrill adopted liberal standards as to what mortgage loans it was prepared to acquire and routinely purchased loans that did not comply with the underwriting standards it was disclosing to investors. (*Id.* at 196-97.)

286. Merrill's ascent was quick. Soon it was buying and securitizing residential mortgages in enormous volumes and at break-neck pace. In the fall of 2005, Merrill purchased a 20 percent stake in subprime lender Ownit Mortgage Solutions, Inc. ("Ownit") to ensure a steady supply of loans. (*Id.* at 196.) Around 2006, Merrill announced that it was planning to buy another subprime lender, First Franklin, in a transaction which Merrill finalized in February 2007 for $1.3 billion. (*Id*. at 200.) Over that period, Merrill aggressively pursued its strategy to capitalize on RMBS by controlling a constant stream of loans to securitize and sell. As O'Neal explained in a recently-disclosed September 2010 interview with the FCIC, Merrill purchased First Franklin in order "to control our [own] source of origination," echoing the interviewer's comment that Merrill made the purchase "to vertically integrate." (O'Neal Tr. 87:5-21, Sept. 16, 2010.) The plan worked: Merrill's securitization of RMBS increased from $67.8 billion for the

nine-month period ending September 29, 2006 to $92.6 billion for the nine-month period ending September 28, 2007. (Merrill Form 10-Q, Nov. 7, 2007.)

287. In his book *And Then The Roof Caved In: How Wall Street's Greed and Stupidity Brought Capitalism to its Knees*, David Faber describes Merrill's focus on RMBS and other mortgage-related securities in the heyday of this business, in 2006 and 2007:

> As Merrill headed into 2007, it had . . . a mission to get even bigger in the one area that had been so instrumental to all its success: mortgages. It wanted to originate more mortgages, buy more mortgages, package more mortgages into securities, and package more of those securities into CDOs [*i.e.*, collateralized debt obligations]. And of course, it wanted to sell those securities and CDOs as fast as it possibly could, because that's where the money was. It was also happy to keep increasing the leverage on its balance sheet as its assets ballooned past $1 trillion, driven by the addition of all those mortgages.

(*And Then The Roof Caved In*, at 131 (2009).)

288. During that time, Merrill continued to face a key problem in its quest to the top—fierce competition from an increasing number of market players. The intense competition led Merrill to loosen the underwriting guidelines and to make as many loans as possible appear to pass muster under those guidelines. (*Chain of Blame,* at 196-97.) For instance, Merrill began ignoring the results of its own due diligence. Merrill often outsourced its review of the loans that it purchased to entities such as Clayton. (*Id.*) According to a report recently released by the FCIC, Clayton informed Merrill that 23% of the loans it was looking to purchase were improperly underwritten. (FCIC Report, at 167.) Notwithstanding that knowledge, Merrill proceeded to include those loans in securitization pools anyway, so as to increase its production volume and market share.

289. Within only a few short years, Merrill moved to the top of the underwriters of RMBS securities. (*Chain of Blame* at 190-91.) Between 2003 and 2006, Merrill's operating profit averaged $5.2 billion, more than double the $2.1 billion it averaged in the preceding five

years. (*Id.* at 194.) These huge profits came at the expense of investors, which were purchasing RMBS backed by loans far riskier than was being disclosed.

(b) Merrill Instructed Subprime Originators to Increase Their Origination Volumes and Originate Riskier Loans

290. As Merrill sought to expand its market share in RMBS, it also encouraged subprime lenders—including Ownit—to originate more low- and no-documentation loans. In a *New York Times* article published on January 26, 2007, William Dallas, the chief executive of Ownit, stated that Merrill and other Wall Street firms were paying him a greater amount for no-income-verification loans than for full-documentation loans. (Vikas Bajaj & Christine Haugheny, *Tremors at the Door*, N.Y. Times, Jan. 26, 2007.) Dallas is quoted as saying: "The market is paying me to do a no-income-verification loan more than it is paying me to do the full documentation loans. What would you do?" (*Id.*) In effect, Merrill was paying Ownit to commit fraud by incentivizing it to accept reduced documentation loan applications from unqualified borrowers.

291. Reduced-documentation and no-documentation "liar" loans are riskier than conventional loans because the borrower provides less information to substantiate his or her income, assets, and other crucial data. With less verified data in the loan file, it is more likely that the loan files contained errors and misrepresentations.

292. Loans originated pursuant to reduced documentation programs were originally intended for wealthy borrowers with complicated personal finances, for whom it is difficult to effectively document their incomes in loan application forms. They typically had low loan-to-value ratios meaning the homeowner had significant equity in the home. For wealthy individuals, these low-documentation and no-documentation loans present little risk of loss.

That changed when they were extended to lower-income borrowers that were unable to obtain traditional loans.

293. Lacking a sufficient pipeline of safe, legitimate borrowers, and under pressure from Merrill and its peers, subprime lenders opened their doors to fraudulent loans. Merrill knew from its experience with loan securitization that "liar loans" were plagued by fraud. It also knew these loans would be securitized and sold to investors. Nonetheless, Merrill encouraged Ownit and other subprime lenders to generate these loans anyway in order to increase loan volume. Merrill was unconcerned that the loans were risky and non-conforming, since the company was transferring the risk of loss on its RMBS to investors like AIG.

294. Merrill also encouraged its affiliated loan originators to demand that appraisers inflate appraisals or face never doing business again. In fact, a 2007 survey of 1,200 appraisers conducted by October Research Corp.—a firm in Richfield, Ohio that published *Valuation Review*—found that 90% of appraisers reported that mortgage brokers and others pressured them to raise property valuations to enable deals to go through. The same study found that 75% of appraisers reported "negative ramifications" if they did not cooperate, alter their appraisal, and provide a higher valuation. This pressure succeeded in generating artificially inflated appraisals, skewing LTV figures reported to investors like AIG.

295. According to David Faber, Merrill gradually favored First Franklin over Ownit as a source of mortgages because "First Franklin wasn't seeing (or admitting) the problems that Ownit was, and Merrill was happy to focus its energy on its new acquisition rather than a firm that was still trying to play by the old [stricter] rules of underwriting." (*And Then The Roof Caved In,* at 76.) Ownit shut its doors in 2006 "rather than make mortgages that were going to go bad only months after they had been funded," as Faber describes. (*Id.* at 77.)

296. Former Merrill executives have since acknowledged the rampant fraud that resulted from a system where originators were paid based solely on volume. As former Merrill Chief Executive Officer John Thain commented in a September 2010 interview with the FCIC: "[W]hen you have a system where you pay someone for originating mortgages simply on volume and nothing happens to them if the credit quality is bad, and nothing happens to them if the borrower is fraudulent on his loan application, and nothing happens to him if the appraisal's fraudulent, then that's probably not a very smart system." (Thain Tr. 98:7-14, Sept. 17, 2010.)

297. Prior to filing this complaint, AIG interviewed former employees of Merrill's origination arms Ownit and First Franklin. These former employees confirmed that both Ownit and First Franklin abandoned their stated underwriting guidelines. For example, a former director at Ownit stated that, during the relevant timeframe, there was such a strong demand for mortgage loans from Merrill and other banks that "there was more a quest for volume than for quality." Similarly, a former regional vice president at Ownit indicated that the pressure to deliver volumes of loans was so great that Merrill was essentially "screaming at [Ownit] to deliver product." Former employees also confirmed that banks like Merrill were fully involved with and informed about the nature and quality of the loans being acquired from Ownit. Indeed, a former Ownit director stated: "Someone from the [bank] buying [the loan pool] was always sitting in on the closing of the pools." Typically, the bank representative came from "credit risk side of the firm" and was involved "all the way through" the evaluation and purchase of Ownit's loans.

298. A former corporate underwriter at Ownit from 2004 to 2006, who sat in on product development meetings with Ownit's top executives, explained to AIG that Ownit's goal was to be "a non-mainstream" lender that would do "loans no one else would do." This former

employee was tasked with conveying the ever-changing underwriting guidelines established at Ownit's corporate headquarters to the personnel in Ownit's lending centers. Based on her review of Ownit's underwriting guidelines, she believed that there was "never an offset to risk," which explained to her why other lenders would not want to make the loans that Ownit did. This former employee had previously worked at both Countrywide and Washington Mutual and stated that Ownit was "the worst example" of a lender making risky, indiscriminate loans that should never have been made in the first place.

299. Another former employee of Ownit, a senior underwriter responsible for originating loans between September 2004 and July 2006, revealed to AIG that Ownit loan officers were falsely inflating incomes on stated income loans and "fudging the numbers" to get the loans approved. Many times this former employee "did not believe" the incomes being claimed on stated income loans, and after looking up comparable salaries from resources such as salary.com, she would tell her managers responsible for the loan "there's no way" the borrower could make the income claimed. However, rather than investigating further, the claimed income would simply be accepted. A former loan funder with Ownit from December 2004 to December 2006, who was responsible for actually disbursing the funds to borrowers once a loan was approved, also observed stated income loan applications with questionable claimed incomes. For example, this former employee observed one loan application where a self-employed gardener claimed to be making $20,000 a month. When she brought this and other related issues to her supervisors, she was told to "mind her own business" and to just fund the loans that had already been approved.

300. The former senior underwriter mentioned above also disclosed to AIG that, at Ownit, the appraisal process was "owned by the loan officers" who enjoyed "a cozy

relationship" with the appraisers. She stated that "excessive adjustments" were made to inflate appraisals and these adjustments were never challenged. As a result, Merilll could not and did not genuinely believe the appraisal values used to calculate LTV and CLTV statistics because it knew that property values were being purposefully and baselessly inflated in order to increase the amount of money that could be given to a borrower.

301. A former underwriter interviewed by AIG and with First Franklin from 2005 to 2007 noted that similar problems plagued First Franklin's lending operation. Indeed, this former employee said that some of the lending practices at First Franklin were "basically criminal" and that First Franklin required its underwriters to depart from stated underwriting guidelines in a way "that we did not agree with, but had to do" in order to keep their jobs. With respect to the appraisal process, this former employee divulged that her managers would call appraisers directly if "they didn't get exactly what they wanted" and request a re-appraisal until a satisfactory number was returned. When she and another former underwriter "spoke out" about the problematic lending practices taking place at First Franklin, they were both fired for attempting to "blow the whistle" on the First Franklin's problematic lending practices.

302. Another former senior underwriter, with First Franklin until 2005, told AIG that her branch manager would often override her decisions not to fund loans because First Franklin audited only about 5% of its closed loans, and the branch manager felt the odds that problematic loans he approved would be identified were low. For example, this former employee recalled one instance where a borrower who worked as a cocktail waitress at a restaurant called Blueberry Hill (which she likened to the International House of Pancakes) claimed on the loan application to earn $5,000 a month. This former employee rejected the loan because she did not believe the claimed income was accurate, but her branch manager overrode her decision, reasoning that

some cocktail waitresses might be able to validly claim a high income if they worked at a high-end establishment—Blueberry Hill was similar to a diner. Another time, this former employee recalled a borrower who had an auto-detailing business who claimed to make $7,500 a month. This former employee rejected the application, but she was ultimately overruled by her branch manager without any further verification. This former employee also remembered several instances where borrowers who were strippers claimed very high income on their loan applications. This former employee conceded that strippers who worked in very high-end establishments might be able to legitimately claim the high incomes, but that these individuals worked at "the diviest places" in Las Vegas. On that basis, this former employee would reject those applications, but her branch manager routinely ruled that these claims of high income were acceptable and overrode her decision.

303. This same former employee also told AIG that First Franklin engaged in problematic conduct concerning appraisals. This former employee revealed that, although comparable properties in an appraisal were supposed to be within one mile of the property at issue, her branch manager routinely "signed off" on appraisals with comparables that were further away than a mile, including some that were "crazy." This former employee also stated that her branch instructed appraisers to change their appraisals and omit certain key details. For instance, she called one situation where the appraiser had indicated in the appraisal that the property had a roof that was approximately 40 years old. The former employee considered this an important detail since it implied that the roof would likely need to be replaced in the near future. However, her branch manager told the appraiser to remove this detail about the roof from the appraisal, saying "we don't need that added." This former employee also revealed that her branch manager would pick certain appraisers because he knew they would return with a

favorable (and overstated) appraisals: "He would pick the appraiser who would do what he wanted… he'd say, 'don't use that guy, use this guy.'" Finally, this former employee told AIG that First Franklin's bonus structure motivated underwriters to close and fund as many loans as possible. For her part, this former employee received $50 for every loan she closed and funded, ultimately making over $150,000 a year while at First Franklin, although her base salary was $55,000.

304. Another former First Franklin underwriter interviewed by AIG revealed that certain fellow underwriters "would approve anything" because First Franklin's compensation structure "created an incentive" to close risky loans and depart from stated underwriting practices. This former employee emphasized that the bonus structure was not based on the total number of loans reviewed within a month, which would include loans that were approved as well as loans that were rejected, but only on the number of loans that the underwriter actually funded and closed. She stated that the monthly bonuses for meeting volume targets were as much as $2,000 - $3,000 per underwriter, in addition to base salary. In addition, this former employee revealed that if an underwriter rejected a loan because it did not meet underwriting criteria, her manager would re-direct the loan application to a certain loan processor who would "sign behind your back." This former employee also recalled an instance where she was "one thousand percent convinced" that the income verifications submitted along with a loan were fraudulent, as the borrower's payroll deductions for Social Security and Medicare fell below the acceptable ranges for such deductions, resulting in an inflated net "take-home" pay for the borrower. She presented this evidence to her manager, who rejected her concerns. The loan was approved even though this former employee believed the deductions were illegitimate and the paystub was fraudulent.

(c) Merrill Waived Loans That Failed To Meet Underwriting Guidelines

305. When purchasing loans from originators, Merrill performed due diligence to assess the quality of the loans it was purchasing. Merrill *knew* that a substantial portion of its loans did not meet published underwriting guidelines, but securitized them anyway. As described by Stanley O'Neal in his September 2010 interview with the FCIC, Merrill conducted "spot checking" of the mortgages that it purchased from third parties, according to written underwriting guidelines. (O'Neal Tr. 84:18, Sept. 16, 2010.) Jeff Kronthal, the former head of Merrill's structured-products division, likewise told the FCIC that Merrill performed due diligence on the mortgages it purchased from Ownit. (Kronthal Tr. 94:1-5, Sept. 14, 2010.) Merrill's analysis involved the individualized review of thousands of mortgage loans in each pool. To perform this review, Merrill employed a team of underwriters that evaluated a sample of the loans to confirm that they both conformed with the representations made by originators and complied with the Merrill's own underwriting guidelines.

306. Merrill's own due diligence revealed that a significant percentage of loans purchased from originators did not meet applicable underwriting standards, yet Merrill granted these non-conforming loans unjustified exceptions. Merrill also relied on outside firms to conduct due diligence on underlying loans, including Clayton. As the FCIC put it: "Because of the volume of loans examined by Clayton during the housing boom, the firm had a unique inside view of the underwriting standards that originators were actually applying—and that securitizers were willing to accept." (FCIC Report, at 166.)

307. For each group of loans it was hired to review, Clayton checked for: (1) adherence to seller-credit underwriting guidelines and client-risk tolerances; (2) compliance with federal, state and local regulatory laws; and (3) the integrity of electronic loan data provided

by the seller to the prospective buyer. (Beal Testimony, at 2.) This review was commonly referred to as a "credit and compliance review." (*Id.*) Contract underwriters reviewed the loan files, compared tape data with hard copy or scanned file data to verify loan information, identified discrepancies in key data points, and graded loans based on compliance with the originator's underwriting guidelines and Defendants' tolerances. (*Id.* at 4.) This included answering such questions as whether the "loans meet the underwriting guidelines," whether they "comply with federal and state laws, notably predatory-lending laws and truth-in-lending requirements," and whether "the reported property values [are] accurate." (FCIC Report, at 166.) For stated income loans, where income was reported by the borrower, Clayton evaluated the "reasonableness of that income." (Beal Testimony, Sept. 23, 2010, at 172.) To the extent a loan was deficient, Clayton also "critically" analyzed whether there were any "compensating factors" justifying a deviation from the underwriting guidelines. (FCIC Report, at 167.)

308. Each day, Clayton generated reports that summarized its findings, including summaries of the loan files that failed to meet the relevant underwriting standards. (Beal Tr. 43:17-25, 44: 1-11, Sept. 23, 2010.) This included giving loans three grades—Grade 3 loans "failed to meet guidelines and were not approved." (FCIC Report, at 166.) Importantly, these Grade 3 loans did not contain any "compensating factors." (*Id.*) According to one contract underwriter who worked at Clayton, "[y]ou weren't supposed fail loans unless they were horrendous." (*Chain of Blame*, at 197.) He also stated that he was told by his supervisors never to use a certain word—"fraud." (*Id.*)

309. Tellingly, only 54% of the nearly one-million loans reviewed by Clayton "met guidelines," a number that its former president, Keith Johnson, admitted indicated "there [was] a quality control issue in the factory" for mortgage-backed securities. (FCIC Report, at 166.)

310. Clayton generated regular reports for Merrill that summarized the findings of its review, including summaries of the loan files that failed to meet underwriting standards. (Beal Tr. 43:17-25, 44: 1-11.) Once Clayton identified such problems, the seller had the option to attempt to cure them by providing missing documentation or otherwise explaining to Clayton why a loan complied with the underwriting standards. (Beal Testimony, at 5.) If additional information was provided, Clayton re-graded the loan. (*Id*. at 4.) Once this process was complete, Clayton provided the underwriters and sponsors with final reports. (*Id.* at 5.)

311. Recently released internal Clayton documents show that, contrary to Merrill's representations, a startlingly high percentage of loans reviewed by Clayton for Merrill were defective, but were nonetheless included by Merrill in loan pools sold to AIG and other investors.

312. According to an internal Clayton "Trending Report" made public in September 2010, Merrill was informed by Clayton that ***23% of the loans it had reviewed failed to meet guidelines,*** which included a finding that the loans had been granted despite the lack of any purported compensating factors justifying an exception. (FCIC Report, at 167.)

313. Merrill nevertheless continued to work with the originators that failed Clayton's review and simply ignored the red flags raised in Clayton's results. ***According to Clayton's "Trending Report," Merrill "waived in" to its pools one third of those toxic loans that Clayton had rejected as outside the guidelines.*** (*Id.*) Given the initial 23% rejection rate, the waiver rate meant that approximately 8% of the loans that actually made it into Merrill's collateral pools had failed the applicable guidelines and were not subject to any compensating factors.

314. Merrill also outsourced its due diligence to the Bohan Group, another third-party due diligence firm. A former Bohan loan reviewer commented that the "the pressure was so

intense to approve as many loans as quickly as possible" that one of her supervisors would stand on a desk screaming at the employees. (*Chain of Blame,* at 197.) The reviewer said Merrill "perpetuated the whole thing," referring to the fraudulent approval and securitization of non-compliant mortgage loans. (*Id.*) She said if she identified loans as failing to comply with the stated underwriting guidelines, "a Merrill supervisor would find a way to get the loan approved." (*Id.*)

315. The hidden "waiver" of rejected loans that were not subject to any compensating factors was a fraudulent omission and rendered Merrill's disclosures regarding its underwriting and due diligence processes even more misleading. As the FCIC report concluded:

> [M]any prospectuses indicated that the loans in the pool either met guidelines outright or had compensating factors, even though Clayton's records show that only a portion of the loans were sampled, and that of those that were sampled, a substantial percentage of Grade 3 Event loans were waived in.
>
> . . . .
>
> [O]ne could reasonably expect [the untested loans] to have many of the same deficiencies, and at the same rate, as the sampled loans. ***Prospectuses for the ultimate investors in the mortgage-backed securities did not contain this information, or information on how few loans were reviewed, raising the question of whether the disclosures were materially misleading, in violation of the securities laws.***

(FCIC Report at 167, 170 (emphasis added)).

316. Merrill never disclosed to AIG that due diligence performed by Clayton and other third-party due diligence firms revealed a high percentage of defective loans, or that Merrill had waived nearly one-third of these loans into loan pools such as those backing AIG's certificates.

317. For its part, in February 2007, AIG visited Merrill affiliate First Franklin to conduct on-site due diligence. First Franklin provided a pitchbook to AIG trumpeting its alleged good underwriting practices. Among other things, First Franklin misrepresented that: (i) it

conducted a "full credit underwriting…on all loans prior to funding"; (ii) to prevent fraud, it performed due diligence on every loan transaction"; (iii) it conducted "verbal verification of employment on all borrowers regardless of doc type"; (iv) it had guidelines in place to address "red flags in the loan file"; (v) it had a robust process to manage exceptions; and (vi) it never gave exceptions based on FICO or LTV.

(3) Bank of America Ignored Its Underwriting Guidelines

318. Like Countrywide and Merrill, Bank of America plotted to increase the volume of subprime loans it originated between 2004 and 2007. In 2004, under the guise of "community development," Bank of America announced its commitment to invest $750 billion over 10 years in low- and moderate-income ("LMI") communities through consumer loans and other programs. (FCIC Report, at 97; 5/22/06 BoA Press Release.). Pursuant to this initiative, Bank of America crowed that, in 2005 alone, it provided more than $33.2 billion in mortgage loans to LMI borrowers and made "more than $40 million in loans and investments every business hour." (5/22/06 BoA Press Release.) But Bank of America used "community development" and pro-home-ownership rhetoric as a smokescreen to do away with underwriting standards and to conceal its true purpose: to originate volumes of subprime loans to sell on the secondary market and to use in its own RMBS securitizations.

319. In order to keep pace with the market and to provide mortgage loans for its own securitizations, Bank of America departed from its own underwriting standards. The FCIC reports that, in 2005, examiners from the Federal Reserve and other agencies conducted a confidential "peer group" study of mortgage practices at six companies, including Bank of America. According to Sabeth Siddique, then head of credit risk at the Federal Reserve Board's Division of Banking Supervision and Regulation, the study "showed a very rapid increase in the volume of these irresponsible loans, very risky loans. A large percentage of their loans issued

were subprime and Alt-A mortgages, and the underwriting standards for these products had deteriorated." (FCIC Report, at 172, emphasis added.) At the same time, Bank of America was providing mortgage loans to a risky class of borrowers that demonstrated a credit profile with an increased likelihood of default. As disclosed to the FCIC in June 2010, almost 17% of the LMI loans originated by Bank of America between 2004 and 2007 were delinquent at some point for 90 days or more. (6/16/10 BoA letter to FCIC, Schedule 2.5.) Bank of America, however, retained only about 50% of those LMI loans on its balance sheet and either sold or securitized the rest. (*Id*.)

320. Bank of America was one of the most aggressive competitors in the mortgage market. Indeed, in a June 13, 2005 e-mail from Angelo Mozilo to David Sambol, Mozilo complained that ***even Countrywide could not match*** some of Bank of America's riskier products: "This is the third deal in the last 10 days that BoA has offered that is impossible to beat. In fact ***the other two were substantially worse*** than this one. It appears to me that ***BofA is making an aggressive move into mortgages once again***." (Emphasis added).

321. Bank of America also participated in "warehouse lending" to ensure that it had access to a steady stream of mortgage loans to securitize and sell to investors like AIG. In 2001, Bank of America sold EquiCredit, the division of Bank of America that, at the time, was primarily responsible for making subprime loans. In order to guarantee that it could obtain sufficient mortgages to pool into its RMBS securitizations, Bank of America began to directly fund originating banks, including Countrywide and New Century Mortgage Corporation. According to *Inside Mortgage Funding*, Bank of America was the leading participant in the warehouse lending channel, with nearly 26 percent market share by 2009. (10/5/10 BoA press release, "Bank of America Exits First Mortgage Wholesale Channel.")

322. In addition, Bank of America sought to expand its share of the mortgage securities market by aggressively pursuing subprime mortgage originators, including Option One, Accredited, and GMAC Mortgage, offering to pay more for their mortgages than competing Wall Street banks and offering to perform less due diligence than its competitors. At the same time, Bank of America knew that the originating banks were churning out risky loans with high likelihood of default. As Ken Lewis, then CEO of Bank of America proclaimed on Bank of America's 2007 second quarter earnings call: ***"Broker [loans] tends to be toxic waste."***

323. Like Countrywide and Merrill, Bank of America also retained the third-party due diligence firm Clayton to review loan-level data on pools of mortgages Bank of America was considering purchasing. (The Clayton review process is described in detail in paragraphs 264-273 and 306-313 above.) And, like Countrywide and Merrill, Bank of America ignored the red flags Clayton found. According to the internal Clayton "Trending Report," Clayton analyzed about 10,200 loans for Bank of America between the second quarter of 2006 and the first quarter of 2007. On the basis of its review, Clayton informed Bank of America that ***30% of the loans it reviewed "failed to meet guidelines,"*** which included a finding that these loans had been granted despite the lack of any purported compensating factors justifying an exception. Despite Clayton's determination that these loans failed to meet applicable underwriting standards, Bank of America "waived in" 27% of these toxic loans and included them in securitizations like the ones in which AIG invested. Bank of America, however, never disclosed to AIG that the due diligence conducted by Clayton showed that a substantial number of the loans in the pools backing Bank of America's RMBS securitizations were defective and that Bank of America had waived the defects as to a substantial number of the loans.

324. In May 2011, the New York Attorney General announced that it was investigating Bank of America's mortgage-related securitization activities. As described in paragraphs 11 and 175 above, the New York Attorney General's investigation found that Bank of America "face[s] Martin Act liability because there are repeated false representations in the Governing Agreements [for RMBS] that the quality of the mortgages sold into the Trusts would be ensured." In addition, Bank of America faces liability for "persistent illegality" in violation of Executive Law § 63(12) for "repeatedly breached representations and warranties regarding loan quality."

(a) Former Employees Confirm That Bank Of America Abandoned Its Underwriting Guidelines

325. According to confidential witnesses interviewed by AIG prior to the filing of this complaint, Bank of America failed to adhere to sound underwriting practices and guidelines during the relevant time period. Like Countrywide, Bank of America employed a multiple step process for loan approval to increase the chances that a loan would be approved. In the first instance, borrower information was entered into Bank of America's "Desktop Underwriting" system. If a loan was rejected by this automated system, the loan would then be referred to a junior underwriter for manual underwriting. If a junior underwriter was unable to approve the loan, the application would be escalated to a more senior underwriter with greater "exception" authority.

326. Bank of America granted "exceptions" to stated underwriting criteria without evaluating a borrower's repayment capabilities or considering countervailing compensating factors. Indeed, one former Loan Processor/Junior Underwriter, who worked for Bank of America from early 2006 to 2008, revealed to AIG that ***Bank of America used exceptions to stated underwriting guidelines to approve loans "quite a bit."*** That same former employee

noted that the fact that an exception was used to approve a loan was not always noted in the loan file. Another former Loan Processor/Junior Underwriter, who worked for Bank of America from 2003 to 2008, disclosed that ***loans were approved even when it was clear that the borrower lacked the ability to repay***. For example, she recalled that many times loans were approved where the borrower was left with only $500 in monthly income after the borrower paid his or her monthly mortgage expenses. And yet another former Loan Processor/Junior Underwriter, who worked for Bank of America in 2005, revealed that loan officers would submit a loan application for one type of loan product and, if the application was rejected, the loan officer would submit the same application for a different product, which might also be rejected, only to be re-submitted yet again for another product until the loan was ultimately approved. In the words of a former Mortgage Underwriter with Bank of America from 2005 to 2006, ***Bank of America and its employees would do "whatever they could do to make loans"***—loans that Bank of America would then securitize and sell to investors like AIG.

327. Indeed, Bank of America maintained an entire division dedicated to approving problem loans that were unable to be funded through the more routine—but already permissive—underwriting procedures described above. Severely credit-blemished loans were diverted to Bank of America's so-called "Plan C" group, which employed alternative underwriting criteria to approve and fund loans. Similar to Countrywide's exception-based Structured Loan Desk in Plano, Texas, ***Bank of America's "Plan C" group had even greater exception authority than senior underwriters, and the group's mandate was to find ways to fund loans that were rejected under Bank of America's stated underwriting guidelines***—loans that one former Bank of America employee believed "should not have been funded under any circumstances." According to a former employee responsible for originating loans between

2005 and 2006, Bank of America's rationale for approving such loans was simply ***"if we didn't do it, someone else would,"*** demonstrating that Bank of America also competed in the race to the bottom, abandoning its stated underwriting guidelines along the way.

328. Numerous former employees interviewed by AIG revealed that Bank of America knew that borrowers were lying about their income to procure loans through the stated income loan programs. In fact, ***several former employees recounted instances in which they had actual knowledge that the income recorded by borrowers on their loan applications was false, but were told by their superiors to approve the loans anyway***. For example, a former Loan Processor/Junior Underwriter with Bank of America from early 2006 to 2008 recalled situations in which borrowers accidentally submitted information demonstrating that their actual income did not match the income stated on their applications. When this fact was raised with management, the former employee was told that stated income loans did not require income verification, so she should not worry about approving the loan. In effect, Bank of America told its employees ***"we didn't have to consider evidence" that directly contradicted borrowers' claims about their income***. Another former Loan Processor/Junior Underwriter who worked for Bank of America from 2003 to 2008 recalled an instance where she could tell by reviewing borrower bank statements that the stated income on the loan application was false. Again, after expressing her concerns about the obviously incorrect data, this former employee was told to go ahead and approve the loan anyway. In addition, former employees revealed that Bank of America loan officers themselves often inflated borrower income and ***"doctored the numbers"*** to get loans approved.

329. Bank of America also enforced a 30-day rule, under which loan officers were required to collect all necessary documentation to close and fund a loan within thirty days. If

required documentation was not collected within the thirty days, loan officers were often directed to approve the loan anyway. Indeed, a former Loan Processor/Junior Underwriter with Bank of America from early 2006 to 2008 noted several occasions where managers directed her to close and fund a loan after thirty days despite the fact that the loan was missing key supporting documentation.

330. Former employees revealed that Bank of America pressured appraisers to inflate appraisals on mortgaged properties, which allowed borrowers to take out the loans for which they applied, but skewed the LTV ratios reported to investors like AIG. Indeed, according to a former employee with Bank of America from 2003 to 2008, it was common knowledge and widely understood that some Bank of America loan officers had "close relationships" with appraisers that allowed them to obtain inflated valuations. In fact, loan officers would often call appraisers and tell them ***"I need you to come in at this amount."*** The appraisers would then return with the requested valuation, allowing the loans to be approved. As a result, Bank of America did not genuinely believe the appraisal values used to calculate LTV and CLTV ratios because it knew that property values were being purposefully and baselessly inflated in order to increase the amount of money that could be given to a borrower.

331. A former senior project lead at Clayton from 2004 to 2009 revealed that Bank of America was not actually interested in the fundamental credit quality of the loans reviewed during Bank of America's due diligence process. Indeed, this former Clayton employee revealed that a Vice President of Structured Products at Bank of America specifically told him that he "didn't give a flying f*** about DTI" and other credit characteristics of the loans being reviewed. Instead, the Bank of America VP told this confidential witness that Bank of America was concerned only that the loans met federal, state, and local lending compliance standards, *i.e.*,

predatory lending laws related to the amount of fees and points that could be charged on loans. The Bank of America VP told this former Clayton employee that he did not care about elements of the loans like appraisals, DTI, or credit because, "we [Bank of America] can sell them [the loans] to whoever" and "we [Bank of America] can sell it [the loans] down the line." On one occasion, this former employee recalled that Clayton had assigned a certain employee that was particularly knowledgeable about appraisals to review a pool of loans for Bank of America, and that this employee was kicking loans out due to inaccurate or suspect appraisals. The former employee revealed that this made the Bank of America VP angry, who told this former employee to "get rid of this f***ing guy," leading to that employee's termination.

(b) AIG's Limited Access to Loan Files Confirms Bank of America Abandoned Its Underwriting Guidelines

332. Although Defendants have refused to cooperate with AIG's efforts to obtain the documentation that would substantiate their representations in the Offering Materials regarding the securitized loans (commonly termed "loan files"), AIG nevertheless recently managed to obtain the loan files for one of the deals at issue here: OOMLT 2007-FXD2. Bank of America served as an underwriter on this deal, on which AIG has suffered over $40 million in losses.

333. AIG arranged for a third-party consultant to review a sample of the loan files to assess whether the loans met stated underwriting guidelines. Although the contents of the loan file will vary depending on the type of loan, loan files contain all of the paperwork a borrower completes in connection with a mortgage, typically including the loan application itself, documentation supporting statements relating to employment, income, and assets, and required disclosures. In addition, the loan file typically includes a property appraisal and the borrower's credit history. To conduct the loan file review, AIG also obtained copies of the underwriting guidelines that would have applied at the time the loans were originated. In other words, AIG's

third-party consultant reviewed the loans based on the same information and guidelines available to the lender at the time of origination. AIG's third-party consultant also reviewed other publicly available information regarding the borrowers and properties in order to test the information contained in the loan file.

334. The results of that review confirmed what the publicly available data discussed above already showed—Defendants' mortgage pools contain loans rife with fraud and other violations of Defendants' representations and the originators' underwriting guidelines.

A review of 100 loan files from OOMLT 2007-FXD2 revealed violations of underwriting guidelines in 82% of the loans, including blatant misrepresentations of income, employment, and owner-occupancy. Representative examples include:

- ***Misrepresentation of Employment***. The borrower stated on the loan application that she was self-employed as a builder for 25 years, earning $35,000 per month, and the co-borrower stated that he was also self-employed as a builder earning $30,000 per month. The borrower also listed on the application that she had been the owner of her building/construction business for 25 years; however, her year of birth was 1971, which would have made the borrower ***10 years old*** when she became the owner of the business. Additionally, the loan file contained letters of incorporation for both the borrower and co-borrower's businesses with inception dates of 9/28/1993 and 2/26/2002, respectively. A reasonably prudent underwriter should have noticed that the age discrepancy was a red flag and questioned the validity of the information contained on the loan application. The loan defaulted.

- ***Misrepresentation of Income***. The borrower stated on the application that she was self-employed as a personal chef with a monthly income of $10,166.67, or $122,000.00 annually. The borrower's tax returns, ***contained in the loan file***, showed a gross income for the entire year of 2007 of $3,126.00 for services as a personal chef, and $27,225 as a self-employed personal assistant. The borrower earned monthly income that was $675 less than the amount of the subject loan mortgage payment in the year following the mortgage closing. The borrower made only one payment on the mortgage, and defaulted.

- ***Misrepresentation of Debt Obligations***. The application failed to disclose that the borrower simultaneously closed on a second mortgage, originated by the ***same lender***, in the ***same condominium*** complex. Public records

show that the Borrower acquired a mortgage on the same day as the subject loan for $414,000 with a monthly payment of $4,995 for a property located in Dallas, TX. The origination underwriter failed to include the monthly payment in the borrower's debt-to-income ratio ("DTI") for the subject loan, resulting in an imprudent underwriting decision. A recalculation of DTI based on the borrower's undisclosed debt, and recalculated income of $1,200 per month, yields a DTI of ***1,129.08%***, which exceeds the guideline maximum allowable DTI of 55%.

In the same file, the borrower stated on her loan application that she was an owner of a liquor store for 13 years, and stated her monthly income as $23,000 a month. $23,000 a month for an owner of a liquor store is unreasonable and should have put the underwriter on notice for potential misrepresentation. The borrower filed a Chapter 13 bankruptcy with the Central District of California Bankruptcy Court in October 2008. Per the Statement of Financial Affairs, the borrower reported that she was retired and earned income of $14,400 annual or $1,200 per month for the year of 2006. The loan defaulted.

- ***Excessive DTI***. The lender's guidelines permitted a maximum allowable DTI of 55% for a stated income loan when the subject property was an investment property. The DTI was not accurate because the borrower's income for the year of the subject loan closing of 2006 was a ***loss*** of $200,684, or a monthly loss of $16,724 per month, and the borrower's total monthly debt was $7,878, meaning that the DTI could not be calculated because the income was ***negative***. The loan defaulted.

- ***Underwriting Guidelines Breach***. The lender's guidelines prohibited a loan amount greater than $400,000 for loans approved with a C or CC risk grade. The subject loan was approved as a C risk grade with a 5 x 30 rating due to unsatisfactory mortgage payments in the last 12 months on the borrower's secondary mortgage. Despite this requirement, the subject loan closed in the amount of $740,000, which exceeds the guideline maximum of $400,000. The loan defaulted.

F. The Economic Downturn Cannot Explain the High Default Rates, Foreclosures, and Delinquencies in the Collateral Pools

335. As illustrated in the table below, the mortgage pools securing the certificates experienced extraordinary early defaults, foreclosures and delinquencies in the mortgage pools. Economic studies have confirmed that high default rates early in a loan's life are highly correlated with misrepresentations in the loan files. This makes sense—as borrowers are put in loan products they cannot actually afford, they quickly and predictably fall behind on their

payments. Thus, the dismal performance of the mortgage loans is itself strong evidence that they were improperly written, and that they did not have the credit risk characteristics the Offering Materials claimed.

336. For example, the F.B.I. Mortgage Fraud Reports of 2006 and 2007 reported on the results of a study of three million residential mortgages that found that between 30% and 70% of early payment defaults were linked to significant misrepresentations in the original loan applications. Loans containing egregious misrepresentations were five times more likely to default in the first six months than loans that did not. Exhibit D shows that a high number of loans at issue experienced early payment defaults and many more are now delinquent, in default, have been liquidated, or foreclosed upon. The table below excerpts data from Exhibit D and illustrates the high delinquency rates for six RMBS at issue.

Transaction	Number of Months Since Issuance	Current Number of Loans in Pool	Number of Delinquent or Defaulted Loans	Percentage of Loans Delinquent
CWALT 2006-OC11	3 month	3741	250	6.68%
	6 month	3628	347	9.56%
	12 month	3476	762	21.92%
	24 month	3021	1475	48.82%
	36 month	2500	1537	61.48%
	48 month	2135	1353	63.37%
	52 month	2041	1251	61.29%
CWL 2006-16	3 month	2128	193	9.07%
	6 month	2021	298	14.75%
	12 month	1781	556	31.22%
	24 month	1477	765	51.79%
	36 month	1281	832	64.95%
	48 month	1159	784	67.64%
	55 month	1096	737	67.24%
FFML 2006-FF11	4 month	9736	1316	13.52%
	7 month	9399	1653	17.59%
	13 month	8716	2271	26.06%
	25 month	6861	3291	47.97%
	37 month	5272	2867	54.38%
	49 month	4269	2132	49.94%
MLMI 2007-MLN1	3 month	6088	1311	21.53%
	6 month	5929	1799	30.34%

Transaction	Number of Months Since Issuance	Current Number of Loans in Pool	Number of Delinquent or Defaulted Loans	Percentage of Loans Delinquent
	12 month	5407	2184	40.39%
	24 month	4033	2238	55.49%
	36 month	3247	2081	64.09%
	48 month	2990	1837	61.44%
OOMLT 2006-3	3 month	7426	933	12.56%
	6 month	7132	1262	17.69%
	12 month	6520	2347	36.00%
	24 month	4827	2389	49.49%
	36 month	3707	2123	57.27%
	48 month	3074	1618	52.64%
	54 month	2854	1381	48.39%
ABFC 2006-OPT2	4 month	4617	561	12.15%
	7 month	4397	719	16.35%
	13 month	3963	1342	33.86%
	25 month	3088	1670	54.08%
	37 month	2430	1356	55.80%
	49 month	2004	1229	61.33%
	55 month	1859	961	51.69%

VI. THE DEFENDANTS KNEW THEIR REPRESENTATIONS WERE FALSE

A. Countrywide Knew Its Representations Were False

337. AIG realleges each allegation above as if fully set forth herein.

338. The same evidence discussed above not only shows that Countrywide's representations were untrue, but that the Countrywide Defendants *knew* it was falsely representing the underlying process and the risk profiles of the mortgage loans. For instance:

- The large discrepancies in basic information such as owner-occupancy, LTV, and CLTV statistics, detailed above and in Exhibits 1 to 349, evidences a systemic underwriting failure that Countrywide could not possibly have been ignorant of given that it operated on every level of the underwriting and securitization process.

- Countrywide's post-mortem internal analysis admits that it did not "heed the warnings," and that "[l]ots of experienced people were uncomfortable."

- Countrywide's CEO's e-mails show that he saw "errors of both judgment and protocol," "massive disregard for the guidelines," and "serious lack of compliance within our origination system."

- Countrywide’s internal audits discovered that a staggering percentage of loans were being approved as “exceptions.” For instance, one “particularly alarming” audit found that over 23% of subprime loans were at the time being processed as exceptions, and another found that 52% of the subprime division’s 100% financings were done with exceptions.

- The amount of loans having to be approved as “exceptions” was seen within Countrywide as “speak[ing] toward our inability to adequately impose and monitor controls on production operations.”

- Other correspondence and testimony confirms the “exceptions” were just a tool being used to “keep pace” and to implement the “matching” strategy.

- Countrywide’s credit officers viewed the “matching” strategy as “ceding” Countrywide’s policies to the market. Another saw Countrywide’s underwriting policies as “theoretical,” and saw it as indefensible that Countrywide continued to use “saleability” as the sole criterion for approval.

- Countrywide’s risk officers wrote that the company “basically continued to act as though they never received” policies the credit officers circulated, and that it was “frustrating” to have their judgment “overridden with whining and escalations.”

- Countrywide’s documents refer to “several recent examples” where products were approved despite explicit rejections by the company’s credit risk department.

- According to former employees, borrowers who could not quality for a loan were steered into low-documentation products, then coached on how to falsify the application to ensure it would be approved.

- According to former borrowers, in some instances Countrywide’s loan officers were the ones to fill out the application with misrepresentations without the borrowers’ knowledge.

- Countrywide’s internal reviews found at one point that 40% of the reduced-documentation loans had income overstatements of 10% or more and a “significant percent of those loans would have income overstated by 50% or more.”

339. That the Countrywide Defendants knew their representations were fraudulent is further supported by additional evidence from Countrywide’s own documents and employees. For instance, Countrywide’s post-mortem internal analysis, discussed above in paragraphs 184

and 191, also shows that the company knew at the time what it was doing was wrong, but it proceeded anyway:

- "We did not fully heed the warnings of our credit models. Delinquencies were rising, and models predicted worse to come."
- "Early indicators of credit risk exposure existed. Internal control systems highlighted many of the risks that eventually transpired."
- "Lots of experienced people were uncomfortable with underwriting guidelines. Going forward, we need to rely on our experience and instinct when business practices don't make sense. In particular, stated income and high LTV was highly counter-intuitive."
- "This crisis will stay in our minds for a generation. We will probably not see a return to this type of irrational behavior for a long time to come."

340. These concerns mirror concerns the Credit Risk Committee raised long before Countrywide's problems became public, demonstrating that Countrywide's admissions were not mere hindsight. In a February 13, 2007 Board of Directors Credit Risk Committee presentation highlighting "areas of concern," alternatively known as a "wall of worries," one of the Credit Risk Committee's "areas of concern" was Countrywide's "loan quality," including "increased fraud," "exception underwriting," "guideline drift," "[a]ttribute deterioration," and "[a]ppraisal quality." This document was generated within Countrywide at the time many of the mortgage loans at issue here were being generated and securitized in AIG's investments.

341. As noted above, John McMurray, Countrywide's then-Chief Risk Officer, gave repeated, explicit, and alarming warnings to Sambol, Mozilo, and others about the financial risks of Countrywide's origination practices, and advocated for stricter origination guidelines. McMurray's SEC testimony also identified his own notes from November 3, 2006, wherein McMurray indicated that he had discussed with Sambol that he was concerned that he would be personally blamed for products that he "never advocated and often recommended against." His notes also indicated that he discussed with Sambol concerns about "the company's risk

philosophy," '"can't say no' culture, pressure from matching and no brokering policies." His testimony also indicates he raised "concerns about inadequate controls, infrastructure, etc."

342. In a May 22, 2005 e-mail, McMurray warned Sambol that the company would face liability for its faulty underwriting practices and misrepresentations to investors like AIG: "We've sold much of the credit risk associated with high risk transactions away to third parties. Nevertheless, we will see higher rates of default on the riskier transactions and third parties coming back to us seeking a repurchase or indemnification based on an alleged R& W breach as the rationale."

343. The SEC testimony of another risk manager, Ingerslev, also confirms that Countrywide was made aware internally of the risks its shoddy procedures were creating:

> In an organization like Countrywide, sales, the strategy of the company was predominantly, you know, a sales-oriented one because of our history as a mortgage banker and, you know, being able to sell off a lot of credit risk, that was one instant, one probability factor that contributes to the culture that we have…. So that - and ultimately, you know, disagreements or ties were broken, you know, to the - you know, to the side of erring on, well, we don't want to lose volume, we want to keep up the volume and keep up our market share. That was a strategy that the company had.
>
> But, you know, John [McMurray] and I and those of us in credit still felt like it was our obligation to make sure that there was perspective, and we were doing it with eyes wide open. In other words, in that environment, there was conflict. Some of it you'd expect, and some of it went beyond what you would expect and was tough.

344. Ingerslev said it was "part of the culture" to have "pressure to [] move things along and say yes to things, and you felt that pressure." He also testified that he thought the company's guidelines had gone "too far" given the "additional layers of risk" in the product mix and changing interest rates. He testified that he was involved in a "constant dialogue" regarding requests to expand even further, but that "[he was] sure [he] said on more than one occasion, you've got to stop here."

345. According to a former employee, Mark Zachary, whose other statements are discussed above, Countrywide's loan origination was plagued by "outright misrepresent[ation of] loans to the secondary markets, to end investors, and to buyers." The company's mentality, he said, was "what do we do to get one more deal done. It doesn't matter how you get there . . . ." Zachary confirmed that he was driven to issue mortgages even though he knew he was setting up the borrower to eventually lose their home.

346. Zachary also recounts an October 25, 2006 e-mail in which a Senior Vice President and Divisional Operations Manager for Countrywide KB Home Loans sanctioned the falsification of information. In the e-mail, Zachary posed to the manager a situation in which a loan officer confessed that a potential borrower did not have a job in the local area, when that is a requirement of the mortgage for which the borrower was applying. Even more drastically, Zachary wondered what would happen if the loan officer mentioned that the borrower was applying for a stated-income loan because he was unemployed. Zachary asked for confirmation that in those circumstances, when there was evidence that the borrower and/or loan officer were falsifying the borrower's information, the company would reject the loan. Shockingly, the senior executive wrote back that "I wouldn't deny it [the loan] because I didn't hear anything. I would definitely tell the [loan officer] to shut up or shoot him!"

347. Zachary brought his concerns regarding no-doc loans (discussed in more detail above) to the attention of Countrywide Employee Relations and Risk Management officials in 2006 and early 2007, but he was ignored. He also refused to unconditionally approve borrowers that did not meet Countrywide's stated guidelines, at which point he was taken out of the approval process and the loans were approved anyway, by his supervisor.

348. Countrywide knew the loans it placed in investments like AIG's were failing basic underwriting standards because the due diligence reports of both Clayton and Bohan, which it should have received, showed that large numbers of loans it originated were failing basic tests, but were being included in securitizations anyway. In addition, Countrywide itself used the services of third-party due diligence firms like Clayton and Bohan, which told Countrywide that loans it had purchased from correspondent banks for its own securitizations did not meet basic underwriting guidelines. As detailed above, Clayon's "Trending Report" reveals that from the fourth quarter of 2006 to the first quarter of 2007, 26% of the mortgages Countrywide submitted for review were rejected. Of the mortgages that Clayton rejected, 12% were subsequently "waived in" by Countrywide and included in securitizations like the ones in which AIG invested.

349. Relying on only a part of the evidence referred to in this Complaint, the District Court that rejected Mozilo, Sambol, and Sieracki's motions for summary judgment in the SEC action found a triable issue of fact as to the question of scienter:

> Here, the SEC has presented evidence from which a reasonable jury could conclude that Defendants possessed the requisite scienter. For example, the SEC has demonstrated that Defendants were aware that Countrywide routinely ignored its underwriting guidelines and that Defendants understood the accompanying risks . . . . The SEC has also presented evidence that Sambol was aware that Countrywide's matching strategy resulted in Countrywide's composite guidelines being the most aggressive guidelines in the industry . . . .
>
> Moreover, in addition to demonstrating that Defendants were aware of the facts which made their statements misleading, the SEC has presented evidence that Sambol and Sieracki knew that Countrywide's Chief Risk Officer John McMurray firmly believed that Countrywide should include greater credit risk disclosures in its SEC filings . . . .
>
> Accordingly, the SEC's evidence is sufficient to raise a genuine issue of material fact with respect to Defendants' scienter, and summary judgment is inappropriate.

S.E.C. v. Mozilo, 2010 WL 3656068, at *16-20 (emphasis added).

350. Countrywide's attempt to conceal the fraud by refusing certificateholders access to loan files further underscores its scienter. The New York Attorney General has accused Countrywide and Bank of America of violation of Executive Law § 63(12) for this very misconduct.

B. Merrill Knew Its Representations Were False

351. AIG realleges each allegation above as if fully set forth herein.

352. Not only *must* Merrill have known that the mortgage loans were widely defective; it *did* know. As previously discussed, Merrill engaged Clayton to perform due diligence review of loan pools to determine whether the loans conformed with the representations made by the originators and complied with Merrill's own credit policies. According to Clayton's internal documents provided to the government in September 2010, Merrill was informed that 23% of the loans it had reviewed "failed to meet guidelines." (FCIC Report, at 167.) These findings were provided to Merrill in a daily report that summarized Clayton's review and included summaries of the deficient loan files. (Beal Tr. 43:17-25, 44: 1-11.) Despite receiving this daily and specific evidence that a significant percentage of the loans it was buying were defective, Merrill provided waivers for 32% of those rejected loans. (FCIC Report, at 167.)

353. According to the September 23, 2010 FCIC testimony of Clayton's Vice President Vicki Beal, the third-party due diligence firms' "exception reports" were provided not just to the underwriter, but also to the sponsors. As a result, Merrill, in its numerous roles of underwriter, depositor, sponsor, and originator, was made fully aware on a daily basis that a significant percentage of the mortgage loans here failed to meet the stated underwriting guidelines, but were being included in the pools underlying AIG's certificates anyway by way of Merrill's "waiver" process. (Beal Tr. 43:17-25, 44: 1-11.)

354. After Clayton's startling disclosures came to light, the former head of Merrill's structured products division, Jeff Kronthal, admitted to the FCIC that the credit crisis was due, in part, to "the level of fraud that was being committed . . . in the mortgage origination process." (Kronthal Tr. 91:10-13, Sept. 14, 2010.)

355. Moreover, it is not plausible that the mortgage loans could have been securitized and sold without Merrill's knowledge of their problems because many of the loans at issue were originated by Merrill's own affiliates—First Franklin and Ownit. As loan originators, First Franklin and Ownit were directly involved in issuing loans to borrowers, including people who could not afford them or who submitted mortgage applications that were rife with misrepresentations. Ownit and First Franklin employees interfaced directly with the borrowers, and were complicit in helping borrowers misrepresent the information in their mortgage applications (for example, as to income and appraised value of the mortgaged property). First Franklin and Ownit in turn passed this false information to the Merrill Defendants who underwrote and sponsored the securities. Thus, Merrill had direct knowledge of, and involvement in, issuing mortgages to unqualified buyers.

356. As discussed in paragraphs 297 to 304, former First Franklin and Ownit, employees confirmed that Defendants were informed about the low quality of the loans they originated and securitized. Indeed, a former Ownit director stated: "Someone from the [bank] buying [the loan pool] was always sitting in on the closing of the pools." Typically, the bank representative came from "credit risk side of the firm" and was involved "all the way through" the evaluation and purchase of Ownit's loans. Former employees also disclosed that they notified their supervisors about suspect loans and noncompliance with underwriting guidelines, but were ignored or that their decisions to reject problematic loans were intentionally overruled.

357. Merrill's relationships with First Franklin and Ownit underscore the vertical integration model Merrill successfully implemented in its mortgage securitization business. Indeed, a recently-disclosed October 2007 presentation to Merrill's board contained a flowchart showing that Merrill's "Primary Activities" in the RMBS market were "Whole Loan Origination & Purchase → Financing → Securitization→ Distribution → Investing." (Leveraged Finance and Mortgage/CDO Review Presentation at 18, Oct. 21, 2007.) The vertical integration between originators and issuers heightened the already-perverse incentives created by the move to the "originate and distribute" business model. The originator, secure with a pipeline to the market, would have even more incentive to loosen its underwriting practices. Those responsible for the securitization—focused on volume—would push them to do so even more. And once the loans were issued, they would have significant incentives to ignore problem loans because rejecting a loan would saddle an affiliated company.

358. Merrill also had extensive economic ties with other loan originators at issue here. For instance, Merrill provided cheap warehouse financing for originators such as Option One and ResMAE with the condition that they continue selling Merrill their loans. (*Chain of Blame*, at 184, 200.) Merrill also paid a premium for low-documentation loans because these loans could be originated more quickly and could bolster its securitization pipeline. (*Tremors at the Door.*) Merrill knew that these loans were risky and failed to meet underwriting guidelines, but included them in securitizations anyway.

359. As purchaser of the loans, Merrill had access to the originators' employees and internal information, and conducted due diligence on the originators both internally and through third-party due diligence firms. Thus, it was aware of the originators' misconduct. Merrill represented in the Offering Materials that it conducted due diligence on all of the originators

with respect to the underwriting guidelines and processes used. Merrill, for example, represented that "[p]rior to acquiring any residential mortgage loans, MLML [Merrill Lynch Mortgage Lending, Inc.] conducts a review of the related mortgage loan seller that is based upon the credit quality of the selling institution" and that the "review process may include reviewing select financial information for credit and risk assessment and conducting an underwriting guideline review, senior level management discussion and/or background checks." OWNIT 2006-4 Prospectus Supplement dated June 22, 2006, at S-33. Merrill further represented that "[t]he underwriting guideline review entails a review of the mortgage loan origination processes and systems. In addition, such review may involve a consideration of corporate policy and procedures relating to state and federal predatory lending, origination practices by jurisdiction, historical loan level loss experience, quality control practices, significant litigation and/or material investors." *Id.* at S-33-34. *See also* FFML 2007-FF2 Prospectus Supplement dated February 27, 2007, at S-42; MLMI 2006-HE5 Prospectus Supplement, dated September 26, 2006 at S-42. As previously discussed in paragraphs 108 and 317, in February 2007 First Franklin also provided a pitchbook and orally touted its alleged good underwriting and due diligence practices in an in-person meeting with AIG.

360. Merrill, acting as underwriter and/or sponsor, had a duty to conduct due diligence on the securities it sold and the representations it made. Yet, as discussed above, an analysis of the underlying loans shows that owner-occupancy, LTV, and CLTV statistics were widely and deeply misrepresented. The sheer pervasiveness of Merrill's misrepresentations concerning the key metrics for these securities is evidence that Merrill knew or recklessly disregarded the falsity of its representations.

C. Bank of America Knew Its Representations Were False

361. AIG realleges each allegation above as if fully set forth herein.

362. In addition to showing that Bank of America's representations were untrue, the same evidence detailed above shows that Bank of America *knew* it was falsely representing the underlying process and the risk profiles of the mortgage loans.

363. Bank of America's own due diligence efforts, conducted by Clayton, show that Bank of America knew that a large number of loans it purchased on the secondary market failed basic underwriting tests but were included in its securitizations anyway. As detailed above, Clayton informed Bank of America that ***30% of the loans it reviewed "failed to meet guidelines,"*** which included a finding that these loans had been granted despite the lack of any purported "compensating factors" justifying an "exception." Despite Clayton's determination that these loans failed to meet applicable underwriting standards, Bank of America "waived in" 27% of these toxic loans and included them in securitizations like the ones in which AIG invested.

364. Severe discrepancies in basic information such as owner-occupancy, LTV, and CLTV statistics, detailed above and in Exhibits 1 to 349, evidences a systemic underwriting failure that Bank of America could not possibly have been ignorant of given that it operated on every level of the underwriting and securitization process. Moreover, as numerous former employees explained to AIG, in its role as an originator, Bank of America itself instructed its own employees to disregard stated underwriting practices, grant exceptions without compensating factors, and ignore clear evidence that the incomes stated on loan applications was false, as discussed in paragraphs 325 to 330 above. Bank of America also specifically directed Clayton employees to ignore fundamental issues related to the credit quality of the loans being reviewed during its due diligence process, as discussed in paragraph 331 above.

365. In addition to acting as an originator of loans, Bank of America's role as a "warehouse lender" gave it a direct knowledge of the origination process of correspondent banks and their wholesale disregard for sound underwriting practices. Indeed, as Ken Lewis, then CEO of Bank of America, admitted on Bank of America's 2007 second quarter earnings call that originating banks were churning out risky loans with a high likelihood of default. stating: ***"Broker [loans] tends to be toxic waste."***

VII. AIG'S DETRIMENTAL RELIANCE AND RESULTING DAMAGES

366. In making the investments, AIG relied upon Defendants' representations and assurances regarding the quality of the mortgage collateral underlying the certificates, including the quality of the underwriting processes through which they generated or acquired the underlying mortgage loans. AIG received, reviewed, and relied upon the Offering Materials, which described in detail the mortgage loans underlying each offering.

367. In purchasing the certificates, AIG justifiably relied on Defendants' false representations and omissions of material fact detailed above, including the misstatements and omissions in the Offering Materials. Indeed, the data provided to AIG concerning the credit quality of the loans in the collateral pool—such as the LTV ratios which were drastically and systematically understated, and the owner-occupancy percentages, which were substantially inflated—were key metrics, which AIG scrutinized in buying the RMBS. Similarly, AIG relied on Defendants' adherence to underwriting guidelines because they gave AIG (what turned out to be false) comfort that robust criteria was in place for loan issuance. AIG also relied on the disclosed ratings for each RMBS as a measure of its credit risk. For example, AIG's securities lending cash collateral investment policy required that 95% of its asset back securities investments (which included RMBS) be invested only in transactions rated AAA/Aaa. Had the rating agencies received accurate information from Defendants concerning the credit

characteristics of these securities, the securities would have received lower ratings. And if the rating agencies had known that Defendants abandoned their stated underwriting guidelines, they would never have given the securities the investment grade ratings they received. AIG's investment policy would have precluded its purchase of the vast majority of the securities at issue for this reason alone.

368. In addition, AIG conducted its own due diligence before purchasing the certificates. For example, AIG personnel conducted site visits with Defendant originators. AIG prepared a questionnaire that included over a hundred discussion points to address with Defendants during these on-site visits of Defendants' underwriting and servicing arms. Indeed, AIG personally visited Defendants Countrywide (on November 2005 and August 2007) and First Franklin (on February 2007), among other originators involved in these transactions, in order to probe their practices. As discussed above, these Defendants provided the same false assurances about the integrity of their underwriting practices at the meetings as they did in the Offering Materials.

369. AIG's due diligence did not and could not have uncovered that Defendants' representations regarding the credit quality and value of its RMBS were false because the information necessary to make such an assessment was in the peculiar, unique and special knowledge of Defendants. Among other things, the undisclosed criteria Defendants used to originate and securitize loans, Defendants' communications with the rating agencies, and the underlying loan files themselves were all uniquely in the possession of Defendants. To this day, AIG has been unable to access loan files for almost all of the RMBS. AIG was therefore reliant on Defendants to makes accurate representations regarding the credit quality and value of its investments.

370. But for the misrepresentations and omissions in the Offering Materials, AIG would not have purchased or acquired the certificates, because those representations and omissions were material to its decision to acquire the certificates, as described above.

371. The material false and misleading statements of facts and omissions made in the Offering Materials and during the on-site meetings directly and proximately caused AIG damage. Contrary to Defendants' representations concerning the quality of the loan collateral and their assurances regarding supposedly robust underwriting practices, the loans backing the certificates were made to borrowers who did not have the represented ability or propensity to repay, and on properties that were overvalued and thus carried significantly more risk if and when the loans resulted in foreclosure. As a result, AIG purchased securities whose true risks greatly exceeded the represented ones. As such, AIG was saddled with securities it never would have purchased, and for which it paid too much and received too little.

372. From the day AIG purchased these securities, it suffered damage because it owned certificates backed by defective loans—not the highly rated products represented in the Offering Materials that it believed it was purchasing. As a result of these misrepresentations, the true value of the certificates on the date of purchase was far lower than the price paid by AIG. The value of the certificates is based in part on expected future cashflows. Not surprisingly, when the defective loans experienced unprecedented rates of delinquency, default and foreclosure—because, contrary to the representations about the borrower's credit profiles, the borrower's could not pay the loans and the inflated property values could not support principal repayments in foreclosure—the performance and value of the certificates plummeted. The resulting downgrades in the Certificate's credit ratings, as described in Section V.D.1, have also rendered the certificates unmarketable at prices anywhere near the prices paid by AIG.

373. An active secondary market for the certificates existed at the time of AIG's purchases and continues to exist today. Numerous brokers are active in, and have trading desks specifically dedicated to, the secondary market for RMBS, including without limitation Bank of America, Barclays, Citigroup, Credit Suisse, Deutsche Bank, Goldman Sachs, J.P. Morgan, Morgan Stanley, Nomura, and Royal Bank of Scotland. The SPSI report confirms the existence of an active secondary market for RMBS:

> Investment banks sold RMBS and CDO securities to investors around the world, and helped develop a secondary market where RMBS and CDO securities could be traded. The investment banks' trading desks participated in those secondary markets, buying and selling RMBS and CDO securities either on behalf of their clients or in connection with their own proprietary transactions.

According to data provided to the FCIC between May 2007 and November 2008, Goldman Sachs alone bought and sold $17 billion worth of RMBS cash securities, and $32 billion worth of credit default swaps linked to RMBS securities, representing a total of 7,000 trades. In addition, approximately $11 billion of RMBS was traded on the secondary market in May 2011. These figures demonstrate the liquidity in the secondary market for RMBS.

374. AIG purchased the certificates not only for their income stream, but also with an expectation of possibly reselling the certificates on the secondary market. AIG thus viewed market value as a critical aspect of the certificates it purchased. AIG incurred substantial losses on the certificates due to a drastic decline in market value attributable to Defendants' misrepresentations which, when disclosed, revealed that the underlying collateral likely had a substantially higher risk profile than AIG was led to believe.

375. AIG has sold some of its certificates on the secondary market, which has resulted in significant realized losses. For example, in December 2008, AIG sold RMBS to the Maiden Lane II facility, resulting in a loss to AIG of almost $8 billion on the RMBS at issue. The certificates which AIG continues to hold on its balance sheet are valued far less than the price at

which AIG purchased them, yielding substantial unrealized losses. As of June 2011, losses for the certificates AIG continues to hold are over $2 billion.

376. Further, the principal and interest payments that AIG received have been less than what AIG would have received had the securities not suffered principal losses. Thus AIG's losses arise not only from the decline in market value of its certificates, which has resulted in both realized and unrealized losses, but also from shortfalls in the principal and interest payments to which it was entitled as a Certificateholder. AIG's substantial losses in principal and interest payments are a direct result of the poor quality of the collateral underlying the certificates and the high rates of default and delinquency of the mortgage loans.

377. The drastic and rapid loss in value of AIG's certificates was primarily and proximately caused by the issuance of loans to borrowers who could not afford them, in contravention of the stated underwriting guidelines touted in the Offering Materials. These rates of delinquency and default were much higher than expected for securitizations supported by collateral fitting Defendants' representations, and much higher than they would have been if the mortgage loans had been properly underwritten.

378. AIG's damages cannot be blamed on the recent decline in the U.S. housing market, but rather are due to Defendants' wrongdoing. The housing crisis was not an intervening cause but rather a manifestation of the fraud at issue. Defendants engaged in a "race to the bottom," abandoning guidelines for the sake of market share, and engaging in unbridled loan origination to fuel their securitization machines. The irresponsible lending practices directly contributed to the housing bubble and ultimately led to its collapse. For example, economists at the University of Michigan and elsewhere have found that the high rates of early delinquency and default, which led to the housing market crash, were caused by a deterioration in the same

credit characteristics that were undisclosed to investors—such as misrepresentations about LTV ratios and owner-occupancy. Moreover, the SPSI found that financial institutions like Defendants "were not the victims of the financial crisis." Instead, the "billions of dollars in high risk, poor quality home loans" that they originated, sold, and securitized and their "unacceptable lending and securitization practices" were "the fuel that ignited the financial crisis." (SPSI Report, at 4.) The SPSI continued:

> Lenders introduced new levels of risk into the U.S. financial system by selling and securitizing complex home loans with high risk features and poor underwriting. The credit rating agencies labeled the resulting securities as safe investments, facilitating their purchase by institutional investors around the world. … Investment banks magnified the risk to the system by engineering and promoting risky mortgage related structured finance products, and enabling investors to use naked credit default swaps and synthetic instruments to bet on the failure rather than the success of U.S. financial instruments. Some investment banks also ignored the conflicts of interest created by their products, placed their financial interests before those of their clients, and even bet against the very securities they were recommending and marketing to their clients. Together these factors produced a mortgage market saturated with high risk, poor quality mortgages and securities that, when they began incurring losses, caused financial institutions around the world to lose billions of dollars, produced rampant unemployment and foreclosures, and ruptured faith in U.S. capital markets.

(SPSI Report, at 12.) In short, "The investment banks that engineered, sold, traded, and profited from mortgage related structured finance products were a major cause of the financial crisis." (SPSI Report, at 11.) The President's Working Group on Financial Markets corroborated this view, concluding: "The turmoil in financial markets clearly was triggered by a dramatic weakening of underwriting standards for U.S. subprime mortgages, beginning in late 2004 and extending into early 2007." (U.S. Department of the Treasury, Board of Governors of the Federal Reserve System, March 2008 Policy Statements on Financial Market Developments.) As a direct contributor to the housing market crash, Defendants cannot rely on the crash as an intervening cause of AIG's losses.

VIII. OTHER MATTERS

A. Bank of America's Liability as a Successor-in-Interest to Countrywide

379. On January 11, 2008, Bank of America announced that it would purchase Countrywide Financial for approximately $4.1 billion. Based upon the steps taken to consummate this transaction, Bank of America became the successor-in-interest to Countrywide Financial because (a) there was continuity of ownership between Bank of America and Countrywide, (b) Countrywide ceased ordinary business soon after the transaction was consummated, (c) there was continuity of management, personnel, physical location, assets and general business operations between Bank of America and Countrywide, (d) Bank of America assumed the liabilities ordinarily necessary for the uninterrupted continuation of Countrywide's business, (e) Bank of America assumed Countrywide's mortgage repurchase and tort liabilities. Bank of America also became the successor in interest to Countrywide because a series of transactions between July 1, 2008 and November 7, 2008, which were not arm's length transactions and which gave inadequate consideration to Countrywide, were structured in such a way as to leave Countrywide unable to satisfy its massive contingent liabilities.

(1) The Structure of the Transaction

380. Bank of America's Form 8-K, dated January 11, 2008, states that under the terms of the merger "shareholders of Countrywide [] receive[d] .1822 of a share of Bank of America Corporation's stock in exchange for each share of Countrywide." In other words, former Countrywide shareholders became Bank of America shareholders.

381. On July 1, 2008, a subsidiary of Bank of America completed the merger with Defendant Countrywide Financial, the parent of all of the Countrywide entities. Bank of America's Form 10-Q for the period ending September 30, 2009, reported that "On July 1, 2008, the Corporation [*i.e*. Bank of America] acquired Countrywide through its merger with a

subsidiary of the Corporation . . . . The acquisition of Countrywide significantly expanded the Corporation's mortgage originating and servicing capabilities, making it a leading mortgage originator and servicer." According to the 10-Q, "Countrywide's results of operations were included in the Corporation's results beginning July 1, 2008." The Form 10-Q also acknowledged pending litigation against Countrywide.

382. Following this initial transaction and over the course of the next few months, Bank of America planned to and did enter into a series of transactions with Countrywide Financial and its various subsidiaries, which Bank of America then controlled. These transactions were designed both to integrate Countrywide's operations with Bank of America's and to leave Countrywide Financial without any source of income and with insufficient assets to cover its massive contingent liabilities arising from Countrywide's mortgage origination, securitization, and servicing practices. Moreover, these transactions were not negotiated at arm's length since after July 1, 2008, Bank of America owned Countrywide Financial.

383. In particular, on July 2, 2008, Countrywide Home Loans, a subsidiary of Countrywide Financial (controlled by Bank of America as of this date), completed the sale of some or substantially all of its assets to NB Holdings Corporation, another wholly-owned subsidiary of Bank of America. Specifically, Countrywide Home Loans sold NB Holdings its membership interests in Countrywide GP, LLC and Countrywide LP, LLC, whose sole assets were equity interests in Countywide Home Loans Servicing LP, in exchange for an approximately $19.7 billion promissory note. Countrywide Home Loans Servicing LP was the operating entity which serviced the vast majority of residential mortgage loans for Countrywide and was an operating business. Countrywide Home Loans also sold a pool of residential

mortgages to NB Holdings Corporation for approximately $9.4 billion. NB Holdings Corporation is Countrywide Home Loan's successor.

384. On November 7, 2008, after obtaining the necessary consents and approvals, two additional transactions occurred which facilitated the completion of Bank of America's merger with Countrywide. First, in exchange for approximately $1.76 billion, Countrywide Home Loans sold Bank of America substantially all of its remaining assets. Second, in exchange for promissory notes of approximately $3.6 billion Bank of America acquired 100% of Countrywide Financial's equity interest in various subsidiaries, including Countrywide Bank, FSB. In connection with this transaction, Bank of America also assumed approximately $16.6 billion of Countrywide's public debt and related guarantees. These two transactions completed Bank of America's transfer of substantially all of the operating and income generating assets of Countrywide out of the Countrywide entities. In February of 2009 Countrywide Bank, FSB filed an application to become a National Association, and in April of 2009, Countrywide Bank, NA was merged into Bank of America, N.A. Similarly, on July 1, 2011, BAC Home Loans Servicing, L.P. (f/k/a Countrywide Home Loans Servicing, L.P.) was merged into Bank of America, N.A. As a result of these mergers, Bank of America, N.A. assumed all of the liabilities of Countrywide Bank, NA and BAC Home Loans Servicing, L.P. (f/k/a Countrywide Home Loans Servicing, L.P.).

385. At the time of the November 2008 transactions, Countrywide Bank, FSB was the largest Countrywide subsidiary. Countrywide's 2007 10-K revealed that "as of December 31, 2007, over 90% of [Countrywide's] monthly mortgage loan production occurred in Countrywide Bank" and that as of January 1, 2008 Countrywide's "production channels ha[d] moved into the Bank, completing the migration of substantially all of [Countrywide's] loan production activities

from CHL to the Bank." By transferring to itself Countrywide Bank, FSB, along with substantially all of the assets of Countrywide Home Loans, Bank of America left the remaining Countrywide entities with only illiquid assets, no ongoing business, no ability to generate revenue, and insufficient assets to satisfy their contingent liabilities. This conclusion is echoed by Bruce Bingham (who prepared a report on behalf of Bank of New York Mellon ("BoNY"), trustee for Countrywide-issued RMBS, attempting to value Countrywide Financial) who found that Countrywide Financial "has negative earnings", "minimal operating revenues," "does not originate, securitize, or service real estate loans" and "has no operations that by themselves are economically viable on a go-forward basis."

386. The transactions between Countrywide and Bank of America were intentionally structured so that Countrywide's massive contingent liabilities relating to its mortgage origination, securitization, and servicing practices remained with Countrywide, while all of its assets and businesses that generated revenue were sold to Bank of America, thus leaving Countrywide unable to satisfy these liabilities. Not only did Bank of America control the Countrywide entities at the time these transactions were entered into, but Bank of America did not provide adequate consideration for the assets it received from Countrywide. In other words, in self-dealing transactions, and in exchange for inadequate consideration, Bank of America intentionally rendered Countrywide insolvent and unable to satisfy its creditors. Moreover, Bank of America was fully aware of Countrywide's contingent liabilities when it transferred these assets out of Countrywide. For example, in an interview published on February 22, 2008 in the legal publication *Corporate Counsel*, a Bank of America spokesperson acknowledged Countrywide's liabilities:

> Handling all this litigation won't be cheap, even for Bank of America, the soon-to-be largest mortgage lender in the country. Nevertheless, the banking giant says

> that Countrywide's legal expenses were not overlooked during negotiations. 'We bought the company and all of its assets and liabilities,' spokesman Scott Silvestri says. 'We are aware of the claims and potential claims against the company and have factored these into the purchase.'

387. One significant entity that Bank of America did not acquire was Countrywide Securities Corp., which acted as Countrywide's broker-dealer and underwriter. However, on October 29, 2008, just before the November transactions, this entity withdrew its registration as a broker dealer from FINRA. Without this registration, Countrywide Securities was unable to continue in the business it had primarily been engaged in (securities dealing and underwriting) and so as of October 29, 2008, Countrywide Securities effectively ceased doing business. This is yet more evidence that Countrywide is no longer engaged in revenue producing activities.

(2) The Actual Consolidation of Bank of America and Countrywide

388. There is no question that Bank of America in fact merged with Countrywide while at the same time ending Countrywide's ongoing operations. On April 27, 2009, Bank of America rebranded Countrywide Home Loans as "Bank of America Home Loans." Many former Countrywide locations, employees, assets, and business operations now continue under the Bank of America Home Loans brand. On the Form 10-K submitted by Bank of America on February 26, 2010, both Countrywide Capital Markets, LLC and Countrywide Securities Corporation were listed as Bank of America subsidiaries.

389. Countrywide Financial's former website now redirects to the Bank of America website. Bank of America has assumed Countrywide Financial's liabilities, having paid to resolve other litigation arising from misconduct such as predatory lending allegedly committed by Countrywide Financial.

390. As is customary in large corporate mergers, at least some of the Countrywide Defendants retained their pre-merger corporate names following their merger with Bank of

America. However, Countrywide's operations are fully consolidated into Bank of America's and the Countrywide entities have lost any independent identity they have maintained following the merger. On April 27, 2009, Bank of America announced in a press release that "[t]he Countrywide brand has been retired." Bank of America announced that it would operate its home loan and mortgage business through a new division named Bank of America Home Loans, which "represents the combined operations of Bank of America's mortgage and home equity business and Countrywide Home Loans."

391. The press release made clear that Bank of America planned to complete its integration of Countrywide Financial into Bank of America "later this year." The press release explained that Bank of America was in the process of rebranding former Countrywide "locations, account statements, marketing materials and advertising" as Bank of America Home Loans, and stated that "the full systems conversion" to Bank of America Home Loans would occur later in 2009. "Bank of America Home Loans" is thus a direct continuation of Countrywide's operations, although the Bank of America Defendants have represented that Bank of America Home Loans is a "trade name" rather than a separate legal entity. It is a Bank of America trade name or brand and thus a part of Bank of America.

392. As of September 21, 2009, former Countrywide bank deposit accounts were reportedly converted to Bank of America accounts. And on November 9, 2009, online account services for Countrywide mortgages were reportedly transferred to Bank of America's Online Banking website. According to press reports, Bank of America Home Loans will operate out of Countrywide's offices in Calabasas, California with substantially the same employees as the former Countrywide entities.

393. The Bank of America website announced that the companies merged and the now-discontinued Countrywide website previously redirected inquiries about the merger to the Bank of America webpage regarding the merger. Bank of America noted on its website that it was "combining the valuable resources and extensive product lines of both companies."

394. Under the "Merger History" tab of Bank of America's website, Countrywide is included among the list of companies Bank of America has acquired. Under the "Time Line" tab, the website states that Bank of America "became the largest consumer mortgage lender in the country" following its acquisition of Countrywide in 2008. Lastly, under the "Our Heritage" tab, the website states that the acquisition of Countrywide "resulted in the launch of Bank of America Home Loans in 2009, making the bank the nation's leading mortgage originator and servicer." The Countrywide logo appears on the page.

395. Mortgage contracts and legal documents state that BAC Home Loans Servicing, LP is the entity "formerly known as" Countrywide Home Loans Servicing, a Countrywide subsidiary, which clearly shows that BAC Home Loans Servicing, LP is the direct successor to Countrywide Home Loans, since it is a mere continuation of Countrywide's business.

396. Bank of America has described the transaction through which it acquired Countrywide Financial and its subsidiaries as a merger of the mortgage operations of both companies and made clear that it intended to integrate Countrywide Financial and its subsidiaries into Bank of America fully by the end of 2009.

397. For example, in a July 2008 Bank of America press release, Barbara Desoer, identified as the head of the "combined mortgage, home equity and insurance businesses" of Bank of America and Countrywide Financial, said: "Now we begin to combine the two companies and prepare to introduce our new name and way of operating." The press release

stated that the bank "anticipates substantial cost savings from combining the two companies. Cost reductions will come from a range of sources, including the elimination of positions announced last week, and the reduction of overlapping technology, vendor and marketing expenses. In addition, [Countrywide] is expected to benefit by leveraging its broad product set to deepen relationships with existing Countrywide customers."

398. Desoer was also interviewed for the May 2009 issue of *Housing Wire* magazine. The article reported that:

> While the move to shutter the Countrywide name is essentially complete, the operational effort to integrate across two completely distinct lending and service systems is just getting under way. One of the assets [Bank of America] acquired with Countrywide was a vast technology platform for originating and servicing loans, and Desoer says that the bank will be migrating some aspects of [Bank of America's] mortgage operations over to Countrywide's platforms.

399. Desoer was also quoted as saying: "We're done with defining the target, and we're in the middle of doing the development work to prepare us to be able to do the conversion of the part of the portfolio going to the legacy Countrywide platforms." Desoer explained that the conversion would happen in the "late fall" of 2009, and that the integration of the Countrywide Financial and Bank of America platforms was a critical goal.

400. After the integration had further progressed, Desoer stated in the October 2009 issue of *Mortgage Banking* that "the first year is a good story in terms of the two companies [coming] together and meeting all the major [goals and] milestones that we had set for ourselves for how we would work to integrate the companies." For Desoer, it was "the highlight of the year . . . when we retired the Countrywide brand and launched the new Bank of America Home Loans brand." In the same issue, Mary Kanaga, a Countrywide transition executive who helped oversee integration, likened the process of integration to the completion of a mosaic: "Everything [*i.e.*, each business element] counts. Everything has to get there, whether it is the

biggest project or the smallest project. It's very much putting a puzzle together. If there is a missing piece, we have a broken chain and we can't complete the mosaic."

401. By way of another example, in its 2008 Annual Report, Bank of America confirmed that "[o]n July 1, 2008, we acquired Countrywide," and stated that the merger "significantly improved our mortgage originating and servicing capabilities, making us a leading mortgage originator and servicer." In the Q&A section of the same report, the question was posed: "How do the recent acquisitions of Countrywide and Merrill Lynch fit into your strategy?" Bank of America responded that by acquiring Countrywide it became the "No. 1 provider of both mortgage originations and servicing" and "as a *combined* company," it would be recognized as a "responsible lender who is committed to helping our customers be successful homeowners." (Emphasis added). Similarly, in a July 1, 2008 Countrywide Financial press release, Mozilo stated that "the *combination* of Countrywide and Bank of America will create one of the most powerful mortgage franchises in the world." (Emphasis added).

402. Thus Countrywide Financial and its subsidiaries, which include each of the Countrywide Defendants, have now been in fact merged into Bank of America. Bank of America is liable for the wrongdoing of the Countrywide Defendants because it is the successor-in-interest to each of the Countrywide Defendants.

403. Bank of America also took steps to expressly and impliedly assume Countrywide Financial's liabilities. Substantially all of Countrywide Financial's and Countrywide Home Loans' assets were transferred to Bank of America on November 7, 2008 "in connection with Countrywide's integration with Bank of America's other businesses and operations," along with certain of Countrywide's debt securities and related guarantees." According to the Bank of

America website, while the integration was being completed "Countrywide customers . . . ha[d] access to Bank of America's 6,100 banking centers."

404. Countrywide Financial ceased filing its own financial statements in November 2008, and its assets and liabilities have been included in Bank of America's recent financial statements. Bank of America has paid to restructure certain of Countrywide Financial's home loans on its behalf, including permitting Countrywide Financial and Countrywide Home Loans to settle a predatory-lending lawsuit brought by state attorneys general and agree to modify up to 390,000 Countrywide loans, an agreement valued at up to $8.4 billion.

405. As stated above, in purchasing Countrywide Financial and its subsidiaries for 27% of its book value, Bank of America was fully aware of the pending claims and potential claims against Countrywide and factored them into the transaction. See interview published on February 22, 2008 in the legal publication *Corporate Counsel*.

406. Moreover, on October 6, 2008, during an earnings call, Joe Price, Bank of America's Chief Financial Officer, stated that "As we transfer those operations [*i.e.*, Countrywide Financial and its subsidiaries] our company intends to assume the outstanding Countrywide debt totaling approximately $21 billion." Asked about the "formal guaranteeing" of Countrywide's debt, Kenneth D. Lewis, Bank of America's former Chairman and Chief Executive Officer, responded that "The normal process we followed is what are the operational movements we'll make to *combine the operations*. When we do that we've said the debt would fall in line and quite frankly that's kind of what we've said the whole time . . . . [T]hat's been very consistent with deals we've done in the past from this standpoint." (Emphasis added).

407. Similarly, Lewis was quoted in a January 23, 2008 *New York Times* article reporting on the acquisition of Countrywide Financial and its subsidiaries, in which he

acknowledged that Bank of America knew of the legal liabilities of Countrywide Financial and its subsidiaries and impliedly accepted them as part of the cost of the acquisition:

> We did extensive due diligence. We had 60 people inside the company for almost a month. It was the most extensive due diligence we have ever done. So we feel comfortable with the valuation. We looked at every aspect of the deal, ***from their assets to potential lawsuits*** and we think we have a price that is a good price.

(Emphasis added).

408. Bank of America has made additional statements showing that it has assumed the liabilities of Countrywide. In a press release announcing the merger, Lewis stated that he was aware of the "issues within the housing and mortgage industries" and said that "the transaction [with Countrywide] reflects those challenges." Despite these challenges, Lewis stated in October 2009 that "The Merrill Lynch and Countrywide integrations are on track and returning value already."

409. Likewise, in Bank of America's Form 10-K for 2009, Bank of America acknowledged that "[W]e face increased litigation risk and regulatory scrutiny as a result of the Merrill Lynch and Countrywide acquisitions."

410. Brian Moynihan, Bank of America's CEO and President, testified before the Financial Crisis Inquiry Commission on January 13, 2010, that "our primary window into the mortgage crisis came through the acquisition of Countrywide . . . . The Countrywide acquisition has positioned the bank in the mortgage business on a scale it had not previously achieved. There have been losses, and lawsuits, from the legacy of Countrywide operations, but we are looking forward."

411. Addressing investor demands for refunds on faulty loans sold by Countrywide, Moynihan stated: "There's a lot of people out there with a lot of thoughts about how we should solve this, but at the end of the day, we'll pay for the things that Countrywide did." And, in a

New York Times article published in December 2010, Moynihan, speaking about Countrywide, again confirmed: "Our company bought it and we'll stand up; we'll clean it up."

412. Similarly, Jerry Dubrowski, a spokesman for Bank of America, was quoted in an article published by Bloomberg in December 2010 that the bank will "act responsibly" and repurchase loans in cases where there were valid defects with the loans. Through the third quarter of 2010, Bank of America has faced $26.7 billion in repurchase requests and has resolved, declined or rescinded $18 billion of those claims. It has established a reserve fund against the remaining $8.7 billion in repurchase requests, which at the end of the third quarter stood at $4.4 billion.

413. During an earnings call for the second quarter of 2010, Charles Noski, Bank of America's Chief Financial Officer, stated that "we increased our reps and warranties expense by $722 million to $1.2 billion as a result of our continued evaluation of exposure to repurchases including our exposure to repurchase demands from certain monoline insurers." And during the earnings call for the third quarter of 2010, Noski stated that "[t]hrough September, we've received $4.8 billion of reps and warranty claims related to the monoline-insured deals, of which $4.2 billion remains outstanding, and approximately $550 million were repurchased."

414. Bank of America has reached various settlement agreements in which it has directly taken responsibility for Countrywide's liabilities. As part of a settlement agreement with certain state attorneys general, Bank of America agreed to forgive up to 30 percent of the outstanding mortgage balances owed by former Countrywide customers. The loans were made before Bank of America acquired Countrywide.

415. In October 2010, the *New York Times* reported that Bank of America is "on the hook" for $20 million of the disgorgement that Defendant Mozilo agreed to pay in his settlement

agreement with the SEC. The agreement and plan of merger between Bank of America and Countrywide provided that all indemnification provisions "shall survive the merger and shall continue in full force and effect . . . for a period of six years." According to the article, "Because Countrywide would have had to pay Mr. Mozilo's disgorgement, Bank of America took on the same obligation, even though it had nothing to do with the company's operations at the time."

416. On January 3, 2011 Bank of America announced that it had agreed to pay $2.8 billion to settle claims to repurchase mortgage loans that Fannie Mae and Freddie Mac had purchased from Countrywide Financial or its subsidiaries. In its press releases and presentation concerning the settlement, Bank of America admitted that it was paying to resolve claims concerning "alleged breaches of selling representations and warranties related to loans sold by legacy Countrywide."

417. On April 15, 2011, Assured Guaranty Ltd. ("Assured") reached a comprehensive $1.1 billion settlement with Bank of America regarding its liabilities with respect to 29 residential mortgage-backed securities transactions insured by Assured. The settlement agreement covered both Bank of America and Countrywide-sponsored securitizations, as well as certain other securitizations containing concentrations of Countrywide-originated loans, that Assured has insured on a primary basis.

418. On May 26, 2011, Bank of America agreed to pay more than $22 million to settle charges that it improperly foreclosed on the homes of active-duty members of the U.S. military between January 2006 and May 2009. In a public statement concerning the settlement, Bank of America Executive President Terry Laughlin said: "While most cases involve loans originated by Countrywide and the improper foreclosures were taken or started by Countrywide prior to our acquisition, it is our responsibility to make things right."

419. On June 28, 2011, Bank of America announced an $8.5 billion proposed settlement with Bank of New York Mellon ("BoNY"), as Trustee for certain Countrywide RMBS. The proposed settlement applies to claims that could be brought by BoNY in connection with 530 residential mortgage-backed securities that were underwritten by Countrywide and for which BoNY served as Trustee. Under the proposed settlement, Bank of America is responsible for payment of the settlement, indemnification of the Trustee, and payment of $85 million in legal fees to counsel for the group of investors that negotiated the deal.

420. Bank of America's public statements accepting responsibility for Countrywide's contingent liabilities arising from Countrywide's mortgage origination, securitization and servicing practices, along with Bank of America's actual settlement of such liabilities demonstrates that Bank of America and Countrywide intentionally structured the transfer of substantially all Countrywide's assets in such a way as to leave minimal and inadequate assets remaining in Countrywide to cover these liabilities.

421. Bank of America has also generated substantial earnings from the absorption of Countrywide's mortgage business. For example, a Bank of America press release regarding the company's 2009 first quarter earnings stated that "[n]et revenue nearly quadrupled to $5.2 billion primarily due to the acquisition of Countrywide and from higher mortgage banking income as lower interest rates drove an increase in mortgage activity." Lewis was quoted as saying, "We are especially gratified that our new teammates at Countrywide and Merrill Lynch had outstanding performance that contributed significantly to our success."

422. A press release regarding Bank of America's 2009 second quarter earnings similarly stated that "[n]et revenue rose mainly due to the acquisition of Countrywide and higher mortgage banking income as lower interest rates spurred an increase in refinance activity." The

press release explained that "higher mortgage banking income, trading account profits and investment and brokerage services income reflected the addition of Merrill Lynch and Countrywide." Bank of America reported that its average retail deposits in the quarter increased $136.3 billion, or 26 percent, from a year earlier, including $104.3 billion in balances from Merrill and Countrywide.

423. Bank of America's 2009 annual report stated that "[r]evenue, net of interest expense on a fully taxable-equivalent (FTE) basis, rose to $120.9 billion, representing a 63 percent increase from $74.0 billion in 2008, reflecting in part the addition of Merrill Lynch and the full-year impact of Countrywide." Bank of America also reported that "[m]ortgage banking income increased $4.7 billion driven by higher production and servicing income . . . primarily due to increased volume as a result of the full-year impact of Countrywide . . . ." Insurance income also increased $927 million "due to the full-year impact of Countrywide's property and casualty businesses."

(3) Bank of America is Countrywide's Successor-in-Interest

424. Based on the above Bank of America became the successor-in-interest to Countrywide Financial because Bank of America, in self dealing transactions for which it provided inadequate consideration, purchased substantially all of the assets and all of the ongoing businesses of Countrywide, rendering Countrywide insolvent and unable to satisfy its massive contingent liabilities. Additionally, Bank of America became the successor-in-interest to Countrywide because (a) there was continuity of ownership between Bank of America and Countrywide, (b) Countrywide ceased ordinary business soon after the transaction was consummated, (c) there was continuity of management, personnel, physical location, assets and general business operations between Bank of America and Countrywide, (d) Bank of America assumed the liabilities ordinarily necessary for the uninterrupted continuation of Countrywide's

business, and (e) Bank of America assumed Countrywide's mortgage repurchase and tort liabilities. Thus, Bank of America the successor-in-interest to Countrywide and is jointly and severally liable for the wrongful conduct alleged herein by the Countrywide Defendants.

425. Based on the same facts, the Supreme Court of the State of New York in *MBIA Ins. Corp. v. Countrywide Home Loans, et al.*, Index No. 602825/08, held that MBIA sufficiently alleged a de facto merger "in which Bank of America intended to absorb and continue the operation of Countrywide." *Id.*, Order on Motion to Dismiss, at 15 (Apr. 29, 2010).

B. <u>Tolling of the Securities Act of 1933 Claims</u>

426. Under *American Pipe*, all putative class members are treated as if they filed their own individual actions until they either opt out or until a certification decision excludes them. *See American Pipe & Constr. Co. v. Utah*, 414 U.S. 538, 554 (1974). As the Second Circuit stated in *WorldCom*: "[B]ecause Appellants were members of a class asserted in a class action complaint, their limitations period was tolled under the doctrine of *American Pipe* until such time as they ceased to be members of the asserted class, notwithstanding that they also filed individual actions prior to the class certification decision." *In re WorldCom Sec. Litig.*, 496 F.3d 245, 256 (2d Cir. 2007).

(1) Tolling of 1933 Act Claims Against Countrywide

427. On November 14, 2007, a class action was filed against various Countrywide entities, former officers, and underwriters on behalf of all investors who purchased or otherwise acquired certain mortgage-backed securities that were issued, underwritten or sold by Countrywide. *See Luther v. Countrywide Home Loans Servicing LP*, BC380698 (Cal. Super. Ct. 2007). The *Luther* complaint alleges claims under Sections 11, 12(a)(2), and 15 of the Securities Act of 1933. AIG purchased certificates in the RMBS included in the *Luther* complaint, and thus was a member of the defined class as of November 14, 2007.

428. On June 12, 2008, a different securities class action was filed against Countrywide in California state court, *Washington State Plumbing & Pipefitting Pension Trust v. Countrywide Financial Corp*., BC392571 (Cal. Super. Ct. 2008). Like *Luther*, this action also alleged Sections 11, 12(a)(2), and 15 claims against Countrywide, its former officers, and underwriters, although *Washington State Plumbing* based its claims on different securitizations than those in *Luther*. As in *Luther*, AIG purchased certificates in the RMBS included in the *Washington State Plumbing* complaint, and thus was a member of the defined class as of June 12, 2008.

429. On September 9, 2008, the *Luther* complaint was amended to add the securitizations from *Washington State Plumbing* to the *Luther* class. The *Washington State Plumbing* action was consolidated with the original *Luther* action, and a consolidated and amended complaint was filed on October 16, 2008. AIG was included in the defined class in the *Luther/Washington State Plumbing* consolidated complaint as a purchaser of certificates in certain RMBS included in the amended consolidated complaint.

430. The consolidated *Luther* action was subsequently dismissed on jurisdictional grounds in January 2010 and refiled that month as *Maine State Retirement System v. Countrywide Financial Corp.,* No. 10 Civ. 0302 (C.D. Cal. 2010). AIG was included in the defined class in the *Maine State* complaint with respect to the same RMBS as in the *Luther/Washington State Plumbing* consolidated complaint.

431. AIG was a member of the defined classes in *Luther*, *Washington State Plumbing*, and *Maine State* class actions and its 1933 Act claims are therefore timely pursuant to *American Pipe* and *In re WorldCom.* AIG reasonably and justifiably relied on the named plaintiffs in *Luther*, *Washington State Plumbing*, and *Maine State* class actions to protect its rights and it

reasonably and justifiably relied on the class action tolling doctrines of *American Pipe* and *In re WorldCom* to toll the statute of limitations on its 1933 Act claims.

432. AIG has chosen to file this separate action and to assert its 1933 Act claims, which have been tolled by the pendency of the class actions discussed above, in order to preserve its rights.

433. The statute of limitations on the 1933 Act claims was also tolled by virtue of a tolling agreement entered into between and among AIG and Bank of America on January 13, 2011, which tolled AIG's claims until August 5, 2011.

(2) Tolling of 1933 Act Claims Against Merrill

434. On December 5, 2008, a class action was filed against various Merrill entities on behalf of all investors who purchased or otherwise acquired certain mortgage-backed securities that were issued, underwritten, or sold by Merrill. *See Conn. Carpenters Pension Fund v. Merrill Lynch*, No. BC403282 (Cal. Super. Ct. Dec. 5, 2008). The *Connecticut Carpenters Pension Fund* complaint alleges claims under Sections 11, 12(a)(2), and 15 of the Securities Act of 1933.

435. AIG purchased certificates in the RMBS included in the *Connecticut Carpenters* complaint, and thus was a member of the defined class as of December 5, 2008.

436. On February 17, 2009, another class action was filed against Merrill in California state court. *See Public Employees' Ret. Sys. of Mississippi v. Merrill Lynch & Co.*, No. 09 Civ. 1392 (S.D.N.Y. Feb. 17, 2009) ("*MissPERS*"). Like *Connecticut Carpenters Pension Fund*, this action alleged Sections 11, 12(a)(2), and 15 claims against various Merrill entities, although *Miss PERS* based its claims on a different set of securitizations than those in *Connecticut Carpenters*. As in *Connecticut Carpenters*, AIG purchased certificates in the RMBS included in the *MissPERS* complaint, and thus was a member of the defined class as of February 17, 2009.

437. On May 14, 2009, *MissPERS* was consolidated with *Connecticut Carpenters* and two other class actions asserting related claims. On May 20, 2009, a consolidated class action complaint was filed, asserting claims under Sections 11, 12(a)(2), and 15 of the Securities Act of 1933. AIG was included in the defined class in the *MissPERS/Connecticut Carpenters* consolidated complaint as a purchaser of certificates in certain RMBS included in the consolidated complaint.

438. AIG reasonably and justifiably relied on the named plaintiffs in *Connecticut Carpenters Pension Fund* and *MissPERS* to protect its rights and it reasonably and justifiably relied on the class action tolling doctrines of *American Pipe* and *In re WorldCom* to toll the statute of limitations on its 1933 Act claims.

439. AIG has chosen to file this separate action and to assert its 1933 Act claims, which have been tolled by the pendency of the class actions discussed above, in order to preserve its rights.

440. The statute of limitations on the 1933 Act claims was also tolled by virtue of a tolling agreement entered into between and among AIG and Bank of America on January 13, 2011, which tolled AIG's claims until August 5, 2011.

C. Liability of Countrywide Financial, Countrywide Capital Markets, and Merrill Lynch & Co., Inc. as Control Persons

(1) Countrywide Financial and Countrywide Capital Markets

441. Countrywide Financial controlled every aspect of the origination and securitization processes. During the relevant timeframe, Countrywide Financial operated its consolidated subsidiaries as a collective enterprise, making significant strategic decisions for its subsidiaries, monitoring enterprise-wide risk, and maximizing profit for Countrywide Financial's executives and shareholders. As reported in Countrywide Financial's 2003 Form 10-K, although

mortgage banking remained Countrywide Financial's "core business," it had expanded operations in recent years "to capitalize on meaningful opportunities to leverage our core Mortgage Banking business and to provide sources of earnings that are less cyclical than the mortgage banking business."[5] In other words, in conjunction with its goal of prioritizing the origination of loans regardless of the risk of default, Countrywide developed its own "in-house" subsidiaries to facilitate its ability to package and sell these risky products.

442. Countrywide Financial managed Countrywide's enterprise-wide risks, strategic direction, and business operations through executive committees. These committees included the Executive Strategy Committee, the Corporate Credit Risk Committee, the Corporate Enterprise Risk Committee, and the Asset/Liability Committee.

443. The Executive Strategy Committee members included Mozilo, Sambol, Sieracki, and Kurland. They were responsible for defining and assessing Countrywide's enterprise-wide strategic direction and risk. The Committee's activities included developing Countrywide Financial's Corporate Strategic Plan and reviewing the strategic plans of each of Countrywide Financial's divisions, to ensure consistency and proper strategic alignment.

444. The Corporate Credit Risk Committee and Corporate Enterprise Risk Committee interfaced directly with the Credit Committee within Countrywide Financial's Board of Directors, assessed the risks to which the Countrywide enterprise was exposed, and they decided which risks Countrywide Financial should sell or otherwise mitigate. The Credit Risk group was also responsible for managing fraud prevention and investigation. Sieracki and Kurland were both members of the Corporate Credit Risk Committee.

[5] Throughout the relevant time period, Countrywide Financial filed consolidated Form 10-Ks, providing a cumulative assessment of the operations of Countrywide Financial and all of its subsidiaries, including the other Countrywide entity Defendants.

445. The Asset/Liability Committee was responsible for addressing market risk for the Countrywide enterprise, across all Countrywide Financial subsidiaries. The Asset/Liability Committee engaged in extensive modeling for the performance of Countrywide Financial's various financial products, and maintained a dedicated Model Validation Subcommittee for that purpose. Mozilo, Sambol, Kurland, Sandefur, and Sieracki were members of the Asset/Liability Committee, and Sieracki became the acting Chairman of the committee in February 2006.

446. Through the use of these committees and others, as well as regular communication with and among its subsidiaries and regular reporting regarding the performance of divisions across the enterprise, Countrywide Financial maintained a high level of day-to-day scrutiny and control over its subsidiaries. Countrywide Financial controlled the guidelines for loan origination, decided which assets to sell and which to hold for its own investment portfolio by being advised of the quality of the underwriting and the loans originated, set protocols for servicing the vast portfolio of loans for which it had retained servicing rights, and approved the manner in which it sold those loans it elected to securitize.

447. Countrywide Financial formed the Countrywide Depositors and the issuing trusts as special purpose entities purely to complete the securitizations. Countrywide Financial exercised actual day-to-day control over the Countrywide Depositors. These Delaware corporations were structured as limited purpose wholly-owned subsidiaries to acquire mortgage loan collateral from Countrywide Home Loans and transfer the collateral to the issuing trusts for sale to investors. The Countrywide Depositors were shell corporations that had no assets of their own. They were controlled by Countrywide Financial through its appointment of Countrywide Financial executives (Sandefur, Sieracki, Kurland, Kripalani, and Sambol, among others) as their

directors and officers. Revenues flowing from the issuance and sale of the certificates were passed through to Countrywide Financial.

448. Countrywide Financial also had actual control over the trusts. Like the Depositors, the trusts were shell entities that had no assets of their own or autonomy, but were mere subsidiaries of the Countrywide Depositors created for the sole purposes of holding the pools of mortgage loans assembled by the Depositors, and issuing certificates based on those mortgage pools to underwriters, including Countrywide Securities, for sale to the public.

449. Countrywide Financial culpably participated in the violations discussed below. It oversaw the actions of its subsidiaries and allowed them to engage in underwriting practices that were inconsistent with the descriptions presented in the Offering Materials; allowed its subsidiaries to misrepresent the mortgage loans' characteristics in the Offering Materials; and established special-purpose financial entities, such as CWABS, to serve as conduits for the mortgage loans.

450. Countrywide Financial also participated in creating the Offering Materials. Indeed, Countrywide Financial employees signed those Offering Materials. Other Countrywide Financial executives, including Mozilo and Sambol, were also culpable participants in Countrywide's wrongdoing at the time they were employed by Countrywide Financial, as reflected by the SEC e-mails. Countrywide Financial is also the parent company of Countrywide Home Loans, Countrywide Securities, and the Countrywide Depositors.

451. Countrywide Financial also controlled the manner in which loans in the securitizations were serviced, both before and after the securitizations' certificates were sold to the public, by using its own servicing division to service the loans.

452. In sum, through its various committees and officers, Countrywide Financial maintained a high level of day-to-day scrutiny and control over its subsidiaries, and controlled the entire process leading to the sale of certificates to AIG. Countrywide Financial controlled the guidelines for loan origination, determined which traditional or non-traditional loan products to offer, set protocols for servicing the mortgage loans it originated or purchased from other lenders and for which it had servicing rights, approved the manner in which it sold the loans it elected to securitize, and controlled the disclosures made in connection with those securitizations.

453. Similarly, Countrywide Capital Markets exercised a high level of day-to-day control over its subsidiary, Countrywide Securities. Mandates from Countrywide Financial passed through Kripalani and Countrywide Capital Markets to Countrywide Securities, and Kripalani, who was the President and CEO of both Countrywide subsidiaries, ensured that Countrywide Securities followed priorities and practices established by Countrywide Financial and Countrywide Capital Markets.

454. As the division of the Countrywide enterprise charged with marketing the loans originated and acquired by Countrywide Home Loans, Countrywide Capital Markets also exercised control over the Countrywide Depositors and, through the Countrywide Depositors, over the trusts. Along with Countrywide Financial, Countrywide Capital Markets determined and approved the manner in which Countrywide Securities and the trusts selected and sold the securitized loans, and controlled the disclosures made in connection with each securitization.

(2) Merrill Lynch & Co., Inc.

455. During the relevant timeframe, Merrill Lynch & Co., Inc. exercised control over its subsidiaries, including Merrill, Lynch, Pierce, Fenner & Smith Inc. and Merrill Lynch Mortgage Investors, Inc. Indeed, Merrill Lynch & Co., Inc. publicly represented that it controlled its entire securitization business. For example, in Merrill Lynch & Co., Inc.'s Form

10-K for the years ended December 29, 2006 and December 28, 2007, Merrill Lynch & Co., Inc. represented that "[i]n the normal course of business, Merrill Lynch securitizes . . . residential mortgage loans." Merrill Lynch & Co., Inc. further described the high degree of its involvement in its securitization business in its 2007 Form 10-K, stating that its "involvement with SPEs [special-purpose entities] used to securitize financial assets includes: structuring and/or establishing SPEs; selling assets to SPEs; managing or servicing assets held by SPEs; underwriting, distributing, and making loans to SPEs; making markets in securities issued by SPEs; engaging in derivative transactions with SPEs; owning notes or certificates issued by SPEs; and/or providing liquidity facilities and other guarantees to, or for the benefit of, SPEs."

456. Exhibit 21 to Merrill Lynch & Co., Inc.'s 2006 and 2007 Form 10-Ks provide that Merrill, Lynch, Pierce, Fenner & Smith Inc. "[a]lso conducts business under the name 'Merrill Lynch & Co.'" Merrill Lynch & Co., Inc. stated in both its 2006 and 2007 Form 10-Ks that it had "[r]etained interests in securitized assets," and the majority consisted of "mortgage-backed securities that Merrill Lynch expect[ed] to sell to investors in the normal course of its underwriting activity." Thus, Merrill Lynch & Co., Inc. not only represented that it was involved in the structuring and issuance of mortgage-backed securities through SPEs, but also represented that it conducted underwriting of those securities in the normal course of its business. And in fact, Merrill Lynch & Co., Inc. was the underwriter of certain of the RMBS at issue here.

457. Merrill Lynch & Co., Inc. executives and directors also played roles in Merrill Lynch & Co., Inc.'s control over Merrill Lynch Mortgage Investors, Inc. For example, Paul Park, who was, at the relevant times, a managing partner of Merrill Lynch & Co., Inc., was simultaneously the President and Chairman of the Board of Directors of Merrill Lynch Mortgage Investors, Inc. Similarly Michael M. McGovern, who was, at the relevant times, a Director and

Senior Counsel of Merrill Lynch & Co., Inc., was simultaneously a Director of Merrill Lynch Mortgage Investors, Inc. Merrill Lynch & Co., Inc. also established Merrill Lynch Mortgage Investors, Inc. in the same facilities that it occupied, with the same registered agent and registered office in Delaware. In addition, Merrill Lynch & Co., Inc.'s managing partner and its director and senior counsel signed Merrill Lynch Mortgage Investors, Inc.'s registration statements.

458. Merrill Lynch & Co., Inc. created the special-purpose entities ("SPEs"), wholly-owned subsidiaries, that purchased residential mortgage loans for Merrill Lynch & Co., Inc.'s securitization business. Merrill Lynch & Co., Inc. established Merrill Lynch Mortgage Investors, Inc. in order to acquire the mortgage loans and to securitize and sell those loans to investors in the form of certificates. In this way, Merrill Lynch & Co., Inc. established Merrill Lynch Mortgage Investors, Inc. for the purpose of advancing the interests of Merrill Lynch & Co., Inc.'s securitization business. According to the Offering Materials, Merrill Lynch Mortgage Investors, Inc.'s certificate of incorporation limited its activities to "those necessary or convenient to carry out its securitization activities."

459. Merrill Lynch & Co., Inc.'s direct role in the issuance and underwriting of certain of the RMBS at issue here is evidenced by the use of its corporate name—"Merrill Lynch & Co." - in bold on the front page of the relevant prospectuses and prospectus supplements. Merrill Lynch & Co., Inc., through Merrill Lynch Mortgage Investors, Inc. and Merrill, Lynch, Pierce, Fenner & Smith Inc., used these prospectuses and prospectus supplements to market and sell its RMBS to investors.

460. The benefits of its securitization business inured directly to Merrill Lynch & Co., Inc., which consolidated the revenues from the issuance and sale of residential mortgage-backed

securities in its financial statements. According to the 2007 Form 10-K, in 2006 and 2007, Merrill Lynch & Co., Inc. reported "cash inflows" of $95.8 billion and $100.2 billion, respectively, from its RMBS transactions.

FIRST CAUSE OF ACTION
(Fraudulent Inducement)
(Against Countrywide Financial Corporation, Underwriter, Depositor, Sponsor, Seller, and Originator Defendants)

461. AIG realleges each allegation above as if fully set forth herein.

462. This claim arises from AIG's purchases of the certificates identified in Exhibit A.

463. The material representations and omissions set forth above were fraudulent, and Defendants' representations fraudulently omitted material statements of fact. The representations at issue are identified above and in Exhibits 1 to 349, and are summarized in Section IV above.

464. Each of the Defendants knew or recklessly disregarded facts demonstrating that its representations and omissions were false and/or misleading at the time they were made. Each of the Defendants made the misleading statements with an intent to induce AIG's reliance and to defraud AIG.

465. AIG justifiably relied on the Defendants' false representations and misleading omissions.

466. Had AIG known the true facts regarding the Defendants' underwriting practices, the quality of the loans making up the securitizations, or the inflated ratings for the securities, it would not have purchased the certificates.

467. As a result of the foregoing, AIG has the right to rescind the fraudulently induced certificate purchases and to require Defendants to repurchase the certificates at their original

cost, plus interest, or has the right to rescissory damages; in the alternative, AIG has suffered damages according to proof.

SECOND CAUSE OF ACTION
(Aiding and Abetting Fraudulent Inducement)
(Against Originator Defendants and Countrywide Financial Corporation)

468. AIG realleges each allegation above as if fully set forth herein.

469. This claim arises from AIG's purchases of the certificates identified in Exhibit A.

470. This is a claim for aiding and abetting fraud brought against Countrywide Financial Corporation and the Originator Defendants identified in the Parties Section above and in Exhibits 1 to 349 (together, "the Aiding and Abetting Defendants").

471. The Aiding and Abetting Defendants knew that the certificates being packaged and sold by the Underwriter, Depositor, Sponsor, and Seller Defendants (identified in the Parties Section above and in Exhibits 1 to 349) were backed by loans that did not comport with the loan characteristics represented to investors and were not underwritten according to Defendants' stated underwriting guidelines, and therefore that the representations made by Defendants to AIG were false.

472. The Originator Defendants gave substantial assistance to and/or facilitated and encouraged the Underwriter, Depositor, Sponsor, and Seller Defendants in their fraud by providing misleading data and information to the Underwriter, Depositor, Sponsor, and Seller Defendants. The Originator Defendants knew the misleading data in turn would be provided to investors, including AIG, who would rely upon it in making their investment decisions.

473. Countrywide Financial Corporation gave substantial assistance to and/or facilitated and encouraged the Countrywide Defendants in their fraud, as alleged herein.

474. As a result of the foregoing, AIG has suffered damages according to proof.

<u>THIRD CAUSE OF ACTION</u>
(Violation of Section 11 of the 1933 Act)
(Against Underwriter and Depositor Defendants)

475. AIG realleges each allegation above as if fully set forth herein, except to the extent that AIG expressly excludes from this cause of action any allegation that could be construed as alleging fraud or intentional or reckless conduct. This cause of action specifically excludes the allegations as to Defendants' scienter set forth in Section VI.

476. This claim is brought under Section 11 of the 1933 Act, 15 U.S.C. § 77k ("Section 11"), against the Underwriter and Depositor Defendants identified in the Parties Section above and in Exhibits 1 to 349 (collectively, the "Section 11 Defendants") arising from AIG's purchases of certificates in the following offerings (the "Section 11 Certificates"):

CWALT 2005-20CB
CWALT 2005-23CB
CWALT 2005-28CB
CWALT 2005-41
CWALT 2005-43
CWALT 2005-44
CWALT 2005-77T1
CWALT 2005-AR1
CWALT 2005-J10
CWALT 2006-12CB
CWALT 2006-26CB
CWALT 2006-4CB
CWALT 2006-9T1
CWALT 2006-OA1
CWALT 2006-OA11
CWALT 2006-OA12
CWALT 2006-OA16
CWALT 2006-OA17
CWALT 2006-OA8
CWALT 2006-OA9
CWALT 2006-OC1
CWALT 2006-OC11
CWALT 2006-OC2
CWALT 2006-OC7
CWALT 2006-OC8
CWALT 2007-23CB
CWALT 2007-HY3
CWALT 2007-HY5R
CWALT 2007-OH1
CWHEL 2005-E
CWHEL 2005-K
CWHEL 2005-M
CWHEL 2006-C
CWHEL 2006-D
CWHEL 2006-G
CWHEL 2007-A
CWHEL 2007-C
CWHL 2005-18
CWHL 2005-19
CWHL 2005-20
CWHL 2005-21
CWHL 2005-24
CWHL 2005-25
CWHL 2005-28
CWHL 2005-J3
CWHL 2006-11
CWHL 2006-13
CWHL 2006-8
CWHL 2006-HYB5
CWHL 2006-J2
CWHL 2007-15
CWHL 2007-5
CWHL 2007-7
CWHL 2007-8
CWHL 2007-HY1
CWHL 2007-HY3
CWHL 2007-HY4
CWHL 2007-HYB1
CWL 2005-10
CWL 2005-11
CWL 2005-13
CWL 2005-15
CWL 2005-16
CWL 2005-17
CWL 2005-6
CWL 2005-7
CWL 2005-9
CWL 2005-AB4
CWL 2005-AB5
CWL 2005-IM1
CWL 2005-IM2
CWL 2005-IM3
CWL 2006-1
CWL 2006-10
CWL 2006-11
CWL 2006-15
CWL 2006-16
CWL 2006-20

CWL 2006-21
CWL 2006-23
CWL 2006-25
CWL 2006-26
CWL 2006-4
CWL 2006-5
CWL 2006-6
CWL 2006-8
CWL 2006-9
CWL 2006-ABC1
CWL 2006-BC1
CWL 2006-S1
CWL 2006-S10
CWL 2006-S2
CWL 2006-S4
CWL 2006-S5
CWL 2006-S7
CWL 2006-S8
CWL 2006-S9
CWL 2007-1
CWL 2007-10
CWL 2007-11
CWL 2007-4
CWL 2007-5
CWL 2007-6
CWL 2007-7
CWL 2007-8
CWL 2007-S1
CWL 2007-S2
CWL 2007-S3
FFMER 2007-3
FFMER 2007-4
FFML 2007-FFC
MANA 2007-OAR4
MLMBS 2007-3
MLMI 2007-MLN1

477. This cause of action is based solely on claims of strict liability or negligence under the 1933 Act.

478. This count is predicated upon the Section 11 Defendants' strict liability for making untrue and materially misleading statements in the Registration Statements.

479. Under 17 C.F.R. § 230.430C(a), all information included in the Prospectus Supplements will be deemed part of the Registration Statements for purposes of Section 11 liability as of the date that the Prospectus Supplement was first used.

480. Each of AIG's purchases of the Section 11 Certificates was made pursuant and/or traceable to the false and misleading Registration Statements and Prospectus Supplements.

481. The Registration Statements and Prospectus Supplements for the Section 11 Certificates were materially untrue, misleading, contained untrue statements of material fact, and omitted to state material facts required to be stated therein or necessary to make the statements therein not misleading. At the time it obtained the Section 11 Certificates, AIG did not know of the facts concerning the untrue and misleading statements and omissions alleged herein. The materially untrue statements and omissions of material fact in the Registration Statements and Prospectus Supplements are set forth in Section IV and V above and in Exhibits 1 to 349.

482. The Section 11 Defendants caused to be issued and disseminated, directed other parties to disseminate at the time of the filing of the Registration Statements and Prospectus Supplements, and/or participated in the issuance and dissemination to AIG of materially untrue statements of fact and omissions of material fact, which were contained in the Registration Statements and Prospectus Supplements.

483. The Section 11 Defendants are strictly liable to AIG for the materially untrue statements and omissions in the Registration Statements and Prospectus Supplements under Section 11. The Depositor Defendants are liable as issuers of the Section 11 Certificates, in particular, within the meaning of Section 2(a)(4) of the 1933 Act, 15 U.S.C. § 77b(a)(4), and in accordance with Section 11(a) of the 1933 Act, 15 U.S.C. § 77k(a). The Underwriter Defendants are liable as an issuer, among other grounds, because they formed the Depositor Defendants as limited purpose finance subsidiaries for the purpose of issuing the certificates and subsequently issued the certificates via the Depositor Defendants. The Underwriter Defendants are also liable in their roles as the underwriter of the securitizations, in accordance with Section 11(a)(5) of the 1933 Act, 15 U.S.C. § 77k(a)(5).

484. Each of the Section 12(a)(2) Defendants is unable to establish an affirmative defense based on a reasonable and diligent investigation of the statements contained in the Offering Materials. These Defendants did not make a reasonable investigation and did not possess reasonable grounds to believe that the statements contained in the Offering Materials were true and that there were no omissions of material fact.

485. This action is brought within one year of the discovery of the materially untrue statements and omissions in the Registration Statements and Prospectus Supplements and brought within three years of the effective date of the Registration Statements and Prospectus

Supplements, by virtue of the timely filing of the *Luther*, *Washington State Plumbing*, *Maine State*, *Connecticut Carpenters Pension* Fund, and *MissPERS* complaints and by the tolling of AIG's claims afforded by those filings, and by virtue of the tolling of AIG's claims afforded by the January 13, 2011 tolling agreement between AIG and Bank of America.

486. AIG has sustained damages measured by the difference between the price AIG paid for the certificates and (1) the value of the certificates at the time this suit is brought, or (2) the price at which AIG sold the certificates in the market prior to the time suit is brought. AIG's Section 11 Certificates lost substantial market value subsequent to and due to the materially untrue statements of fact and omissions of material fact in the Registration Statements and Prospectus Supplements alleged herein.

487. By reason of the conduct herein alleged, the Section 11 Defendants violated Section 11 of the 1933 Act and are jointly and severally liable for their wrongdoing. By virtue of the foregoing, AIG is entitled to damages from each of the Section 11 Defendants.

FOURTH CAUSE OF ACTION
(Violation of Section 12(a)(2) of the 1933 Act)
(Against Underwriter and Depositor Defendants)

488. AIG realleges each allegation above as if fully set forth herein, except to the extent that AIG expressly excludes from this cause of action any allegation that could be construed as alleging fraud or intentional or reckless conduct. This cause of action specifically excludes the allegations as to Defendants' scienter set forth in Section VI.

489. This is a claim brought under Section 12(a)(2) of the 1933 Act, 15 U.S.C. § 77l(a)(2) ("Section 12(a)(2)"), against the Underwriter and Depositor Defendants identified in the Parties Section above and in Exhibits 1 to 349 (collectively, the "Section 12(a)(2)

Defendants") arising from AIG's purchases of certificates in the following offerings ("Section 12(a)(2) Certificates"):

CWALT 2005-10CB
CWALT 2005-43
CWALT 2005-44
CWALT 2005-6CB
CWALT 2005-7CB
CWALT 2005-AR1
CWALT 2006-9T1
CWALT 2006-OA1
CWALT 2006-OA11
CWALT 2006-OA12
CWALT 2006-OA16
CWALT 2006-OA17
CWALT 2006-OA8
CWALT 2006-OC1
CWALT 2006-OC11
CWALT 2006-OC2
CWALT 2006-OC7
CWALT 2006-OC8
CWALT 2007-HY3
CWALT 2007-HY5R
CWALT 2007-OH1
CWHEL 2005-E
CWHEL 2005-K
CWHEL 2005-M
CWHEL 2006-C
CWHEL 2006-D
CWHEL 2006-G
CWHEL 2007-A
CWHEL 2007-C
CWHL 2005-18
CWHL 2005-19
CWHL 2005-20
CWHL 2005-24
CWHL 2005-25
CWHL 2006-11
CWHL 2006-8
CWHL 2006-J2
CWHL 2007-15
CWHL 2007-8
CWHL 2007-HY4
CWHL 2007-HYB1
CWL 2005-10
CWL 2005-11
CWL 2005-13
CWL 2005-15
CWL 2005-16
CWL 2005-17
CWL 2005-7
CWL 2005-9
CWL 2005-AB4
CWL 2005-AB5
CWL 2005-IM1
CWL 2005-IM3
CWL 2006-1
CWL 2006-10
CWL 2006-11
CWL 2006-15
CWL 2006-16
CWL 2006-20
CWL 2006-23
CWL 2006-25
CWL 2006-26
CWL 2006-5
CWL 2006-6
CWL 2006-8
CWL 2006-9
CWL 2006-ABC1
CWL 2006-BC1
CWL 2006-S1
CWL 2006-S10
CWL 2006-S2
CWL 2006-S4
CWL 2006-S8
CWL 2006-S9
CWL 2007-1
CWL 2007-10
CWL 2007-11
CWL 2007-4
CWL 2007-5
CWL 2007-6
CWL 2007-7
CWL 2007-8
CWL 2007-S1
CWL 2007-S2
CWL 2007-S3
FFMER 2007-3
FFMER 2007-4
FFML 2007-FF1
FFML 2007-FF2
FFML 2007-FFC
MANA 2007-A1
MANA 2007-OAR4
MLMI 2006-AF1
MLMI 2006-HE5
MLMI 2006-OPT1
MLMI 2007-MLN1

490. This cause of action is based solely on claims of strict liability or negligence under the 1933 Act.

491. This count is predicated upon the Section 12(a)(2) Defendants' negligence for making untrue and materially misleading statements in the Offering Materials for the Section 12(a)(2) Certificates.

492. The Section 12(a)(2) Defendants offered and sold the Section 12(a)(2) Certificates to AIG by means of defective Offering Materials, which contained materially untrue statements of fact and omitted to state material fact necessary to make the statements, in light of the circumstances under which they were made, not misleading. The Section 12(a)(2) Defendants are specifically named as underwriters and depositors in the Offering Materials and were responsible for distribution of the Section 12(a)(2) Certificates to the public pursuant to the terms of the Offering Materials. The Section 12(a)(2) Defendants also directly or indirectly participated in drafting and disseminating the Offering Materials pursuant to which the Section 12(a)(2) Certificates were sold to AIG.

493. Each of the Section 12(a)(2) Certificates was purchased in the initial offering.

494. AIG purchased the Section 12(a)(2) Certificates from the Section 12(a)(2) Defendants, who transferred title to AIG and/or actively solicited AIG for their own personal financial gain.

495. The materially untrue statements of fact and omissions of material fact in the Prospectus Supplements are set forth in Section IV and V above and in Exhibits 1 to 349.

496. The Section 12(a)(2) Defendants offered the Section 12(a)(2) Certificates for sale, sold them, and distributed them by the use of means or instruments of transportation and communication in interstate commerce.

497. The Section 12(a)(2) Defendants owed to AIG the duty to make a reasonable and diligent investigation of the statements contained in the Offering Materials, to ensure that such statements were true, and to ensure that there was no omission to state a material fact required to be stated in order to make the statements contained therein not misleading. The Section 12(a)(2) Defendants failed to exercise such reasonable care.

498. Each of the Section 12(a)(2) Defendants is unable to establish an affirmative defense based on a reasonable and diligent investigation of the statements contained in the Offering Materials. These Defendants did not make a reasonable investigation and did not possess reasonable grounds to believe that the statements contained in the Offering Materials were true and that there were no omissions of material fact.

499. Conversely, AIG did not know, nor in the exercise of reasonable diligence could it have known, of the untruths and omissions contained in the Offering Materials at the time it purchased the Section 12(a)(2) Certificates.

500. This action is brought within one year of the time when AIG discovered or reasonably could have discovered the facts upon which this action is based, and within three years of the time that the certificates upon which this cause of action is brought were sold to the public, by virtue of the timely filing of the *Luther*, *Washington State Plumbing*, *Maine State*, *Connecticut Carpenters Pension Fund*, and *Miss PERS* complaints and by the tolling of AIG's claims afforded by those filings, and by virtue of the tolling of AIG's claims afforded by the tolling agreement between AIG and Bank of America, dated January 13, 2011.

501. AIG sustained material damages in connection with its investments in the Section 12(a)(2) Certificates and accordingly has the right to rescind and recover the consideration paid for the Section 12(a)(2) Certificates, with interest thereon, in exchange for tendering the Section 12(a)(2) Certificates. AIG hereby demands rescission and offers to tender its Section 12(a)(2) Certificates.

FIFTH CAUSE OF ACTION
(Violation of Section 15 of the 1933 Act)
(Against Countrywide Financial Corporation, Countrywide Capital Markets, and Merrill Lynch & Co., Inc.)

502. AIG realleges each allegation above as if fully set forth herein, except to the extent that AIG expressly excludes from this cause of action any allegation that could be construed as alleging fraud or intentional or reckless conduct. This cause of action specifically excludes the allegations as to Defendants' scienter set forth in Section VI.

503. This is a claim brought under Section 15 of the 1933 Act, 15 U.S.C. § 77o ("Section 15") against Countrywide Financial, Countrywide Capital Markets, and Merrill Lynch & Co., Inc. (the "Section 15 Defendants") for controlling-person liability with regard to the Section 11 and Section 12(a)(2) causes of actions set forth above.

504. The Section 15 Defendants are controlling persons within the meaning of Section 15 by virtue of their actual power over, control of, ownership of, and/or directorship of the Section 11 Defendants and the Section 12(a)(2) Defendants, defined above, at the time of the wrongs alleged herein and as set forth herein.

505. The Section 11 and 12(a)(2) Defendants acted negligently and without reasonable care regarding the accuracy of the information contained in and incorporated by reference in the Offering Materials. The Section 11 and 12(a)(2) Defendants lacked reasonable grounds to believe that such information was accurate and complete in all material respects.

506. For the reasons set forth in Section VIII.C above, the Section 15 Defendants had power and influence over the Section 11 and 12(a)(2) Defendants and exercised the same to cause those Defendants to engage in the acts described herein. By virtue of their control, ownership, offices, directorship and specific acts, the Section 15 Defendants each had the power

to influence and control, and did influence and control, directly or indirectly, the decision-making of the Section 11 and 12(a)(2) Defendants named herein.

507. None of the Defendants named herein conducted a reasonable investigation or possessed reasonable grounds for the belief that the statements contained in the Offering Materials were true, were without omissions of any material fact, or were not misleading.

508. AIG did not know, nor in the exercise of reasonable diligence could it have known, of the untruths and omissions contained in the Offering Materials at the time it purchased the certificates.

509. By virtue of the conduct alleged herein, the Section 15 Defendants are liable for the aforesaid wrongful conduct, jointly and severally with—and to the same extent as—the entities they controlled for the violations of Sections 11 and 12(a)(2) by the controlled entities.

SIXTH CAUSE OF ACTION
(Negligent Misrepresentation)
(Against Underwriter, Depositor, Sponsor, Seller Defendants, Countrywide Financial Corporation, Countrywide Home Loans, Inc., and First Franklin Financial Corporation)

510. AIG realleges each allegation above as if fully set forth herein.

511. This claim arises from AIG's purchases of the certificates identified in Exhibit A.

512. AIG purchased nearly 350 RMBS that Defendants originated, securitized and sold.

513. Because Defendants arranged the securitizations, and originated or acquired the loans, and/or underwrote the RMBS, Defendants had unique and special knowledge about the loans in the offerings. In particular, Defendants had unique and special knowledge and expertise regarding the loan files, including the quality of the underwriting of those loans, the appraisals made, and information regarding LTV, CLTV, owner-occupancy and other key metrics.

Defendants also had unique and special knowledge of the credit-related data provided to the rating agencies, which was inflated to mask the true credit risk associated with the loans.

514. AIG could not evaluate the loan files for the mortgage loans underlying its certificates. Defendants were uniquely situated to evaluate this information in each securitization. Even today, AIG has requested access to the loan files and Defendants have refused to provide it. AIG also could not review the information regarding the loans provided to the rating agencies. AIG was therefore reliant on Defendants to provide accurate information regarding the loans.

515. Defendants were aware that AIG was relying on false information with respect to the credit quality of the loans, the underwriting guidelines, and the integrity of the ratings. Defendants' possession of unique and special knowledge imposed a duty on Defendants to speak with care.

516. Defendants were aware that AIG relied on their unique and special expertise and experience and depended upon them for accurate and truthful information. They also knew that the facts regarding their compliance with their underwriting standards, the credit quality of the loans, and the integrity of the ratings were exclusively within their knowledge.

517. Defendants made misrepresentations and omissions in order to induce AIG to purchase the certificates and with the intent that AIG rely on the misrepresentations. The misrepresentations are set forth above and in Exhibits 1 to 349. At the time they made these misrepresentations and omissions, Defendants knew, or at a minimum were negligent in not knowing, that their statements were false, misleading, and incorrect, as further described in Section V.

518. AIG reasonably relied on the information Defendants did provide and was damaged as a result of these misrepresentations and omissions. Had AIG known the true facts regarding Defendants' underwriting practices and the quality of the loans making up the securitizations, it would not have purchased the certificates.

SEVENTH CAUSE OF ACTION
(Successor and Vicarious Liability)
(Against Bank of America Corporation, Bank of America, N.A., NB Holdings Corporation)

519. AIG realleges each allegation above as if fully set forth herein.

520. Bank of America Corporation, Bank of America, N.A., and NB Holdings Corporation are jointly and severally liable or otherwise vicariously liable for the any and all damages resulting from the wrongful actions of Countrywide, as alleged herein, because they are the successor-in-interest to Countrywide.

521. Bank of America Corporation, Bank of America, N.A., and NB Holdings Corporation became the successor-in-interest to Countrywide because (a) there was continuity of ownership between Bank of America and Countrywide, (b) Countrywide ceased ordinary business soon after the transaction was consummated, (c) there was continuity of management, personnel, physical location, assets and general business operations between Bank of America and Countrywide, (d) Bank of America assumed the liabilities ordinarily necessary for the uninterrupted continuation of Countrywide's business, and (e) Bank of America assumed Countrywide's mortgage repurchase and tort liabilities. Bank of America also became the successor in interest to Countrywide because the transactions, which were not arm's length transactions and which gave inadequate consideration to Countrywide, was structured in such a way as to leave Countrywide unable to satisfy its massive contingent liabilities.

PRAYER FOR RELIEF

WHEREFORE AIG prays for relief as follows:

a. Rescission or a rescissory measure of damages;

b. Alternatively, compensatory damages in favor of AIG against all Defendants, jointly and severally, for all monetary damages sustained as a result of Defendants' wrongdoing, in an amount to be proven at trial but not less than $10 billion;

c. Punitive damages;

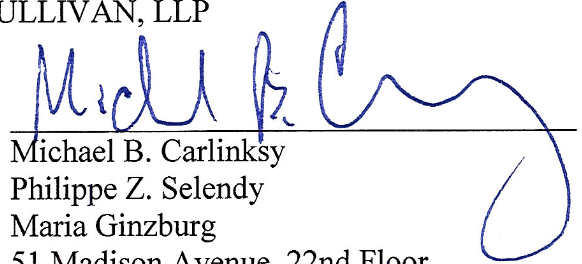
d. Attorneys' fees and costs;

e. Prejudgment interest at the maximum legal rate; and

f. Such other and further relief as the Court may deem just and proper.

DATED: New York, New York
August 8, 2011

QUINN EMANUEL URQUHART &
SULLIVAN, LLP



By: ______________________

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