UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

U. S. SECURITIES AND EXCHANGE COMMISSION, **Plaintiff,** **v.** **CITIGROUP GLOBAL MARKETS INC.,** **Defendant,** **BETTER MARKETS, INC.,** **Movant Seeking Intervention**	**CIVIL ACTION NO. 1:11-cv-07387-JSR** **ECF CASE**

DECLARATION OF DENNIS M. KELLEHER IN SUPPORT OF MEMORANDUM IN OPPOSITION TO PROPOSED SETTLEMENT

I, Dennis M. Kelleher, declare under penalty of perjury as follows:

1. I am a member of the bar of the Commonwealth of Massachusetts and counsel for Movant Seeking Intervention, Better Markets, Inc. in the above-captioned action. I have been admitted to practice before this court pro hac vice in this action.

2. I respectfully submit this Declaration in support of Better Markets's Memorandum In Opposition To Proposed Settlement and to transmit to the Court true and correct copies of the following documents described in the table below.

Document	Exhibit
Press Release issued by the Securities and Exchange Commission titled "Citigroup to Pay $285 million to Settle SEC Charges for Misleading Investors About CDO Tied to Housing Market" dated October 19, 2011	1
A copy of the complaint filed of the SEC in *SEC v. Brian Stoker*, 11 Civ 7388	2
Order Instituting Cease-and-Desist Proceedings in Matter of *Credit Suisse Alternative Capital LLC*	3
Charts from Press Release "Citigroup to Pay $285 million to Settle SEC Charges for Misleading Investors About CDO Tied to Housing Market" dated October 19, 2011	4
"Citigroup to Pay $285 Million to Settle Fraud Charges" Wall Street Journal October 20, 2011	5
"Citigroup has agreed to pay $285 million to investors in negligence suit, SEC says" Washington Post, October 19, 2011	6
Citigroup and CDOs in 2007, NYT, 2008	7
Citigroup's 2007 Q1 Report	8
Citigroup's 2007 Q2 Report	9
Citigroup's 2007 Q3 Report	10
Citigroup's Jan. 2008 Reports Full Year Revenue and Q4 Net Loss for 2007	11
Citigroup's 2007 Financials and 10-k Report	12
Citigroup's Oct. 2011 Q3 Net Income	13
Citigroup's Jul. 2011 Q2 Net Income	14
Citigroup's Jan. 2011 Reports Full Year Net Income and Q4 for 2010	15
Citigroup's 2010 Financials and 10-k Report	16
Excerpt from Citigroup Proxy Statement 2007	17
Excerpts from Citigroup Proxy Statements 2004-2008	18
New York City Securities Industry Bonus Pool 1985-2010, OSC Event, NYC (Table)	19
The Securities Industry in NYC, Office of the State Comptroller, Nov. 2008 (Report 7-2009)	20
Citigroup reworks its public image with new ad campaign, NYT, Apr.2007	21
Citigroup's 2007 Citizenship Report	22
May 2007 Citi Targets $50bn Over 10 Years to Address Global Climate Change	23
"Did Citi Get a Sweet Deal? Bank Claims SEC Settlement on One CDO Clears It on All Others." ProPublica. October 20, 2011.	24
"SEC Pushes Citi toward $200m settlement." Financial Times. September 15, 2011.	25
"SEC poised to file further CDO charges against Wall Street banks." Financial Times. November 3, 2011.	26

I declare under penalty of perjury that the foregoing is true and accurate.

Executed on November 3, 2011

Respectfully submitted,

Dennis M. Kelleher
dkelleher@bettermarkets.com
Counsel for Better Markets, Inc.
1825 K Street, NW, Suite 1080
Washington, DC
Tel: 202-618-6464
Fax: 202-618-6465

CERTIFICATE OF SERVICE

I hereby certify that I caused a copy of the foregoing Declaration Of Dennis M. Kelleher In Support Of Memorandum In Opposition To Proposed Settlement to be served upon the following counsel for the parties to this action, at the following addresses, on November 3, 2011, by hand delivery:

Counsel for Plaintiff Securities and Exchange Commission

Jeffrey Thomas Infelise
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-4010
Tel: 202-551-4904
Fax: 202-722-9362
Email: infelisej@sec.gov

Counsel for Defendant Citigroup Global Markets Inc.

Brad Scott Karp
Paul, Weiss, Rifkind, Wharton & Garrison LLP (NY)
1285 Avenue of the Americas
New York, NY 10019
Tel: 212-373-2384
Fax: 212-373-2384
Email: bkarp@paulweiss.com

Dated: Washington, DC
November 3, 2011

Dennis M. Kelleher
Counsel for Better Markets, Inc.
1825 K Street, NW, Suite 1080
Washington, DC
Tel: 202-618-6464
Fax: 202-618-6465
dkelleher@bettermarkets.com

EXHIBIT 1

TO DECLARATION OF DENNIS M. KELLEHER IN SUPPORT OF MEMORANDUM IN OPPOSITION TO PROPOSED SETTLEMENT

(TA EX. 1)

U.S. Securities and Exchange Commission

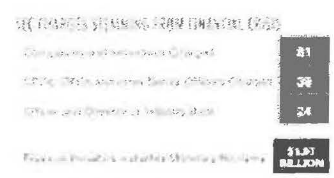
Citigroup to Pay $285 Million to Settle SEC Charges for Misleading Investors About CDO Tied to Housing Market

Former Citigroup Employee Separately Charged for His Role in Structuring Transaction

FOR IMMEDIATE RELEASE
2011-214

Washington, D.C., Oct. 19, 2011 – The Securities and Exchange Commission today charged Citigroup's principal U.S. broker-dealer subsidiary with misleading investors about a $1 billion collateralized debt obligation (CDO) tied to the U.S. housing market in which Citigroup bet against investors as the housing market showed signs of distress. The CDO defaulted within months, leaving investors with losses while Citigroup made $160 million in fees and trading profits.

Chart: SEC Charges Stemming From Financial Crisis



Full-size (PDF)

Additional Materials

- SEC Complaint Against Citigroup Global Markets Inc.
- SEC Complaint Against Brian H. Stoker
- Order in the Matter of Credit Suisse Alternative Capital, Credit Suisse Asset Management and Samir H. Bhatt

---

The SEC alleges that Citigroup Global Markets structured and marketed a CDO called Class V Funding III and exercised significant influence over the selection of $500 million of the assets included in the CDO portfolio. Citigroup then took a proprietary short position against those mortgage-related assets from which it would profit if the assets declined in value. Citigroup did not disclose to investors its role in the asset selection process or that it took a short position against the assets it helped select.

Citigroup has agreed to settle the SEC's charges by paying a total of $285 million, which will be returned to investors.

Chart: SEC Monetary Recoveries

The SEC also charged Brian Stoker, the Citigroup employee primarily responsible for structuring the CDO transaction. The agency brought separate settled charges against Credit Suisse's asset management unit, which served as the collateral manager for the CDO transaction, as well as the Credit Suisse portfolio manager primarily responsible for the transaction, Samir H. Bhatt.

Full-size (PDF)

"The securities laws demand that investors receive more care and candor than Citigroup provided to these CDO investors," said Robert Khuzami, Director of the SEC's Division of Enforcement. "Investors were not informed that Citgroup had decided to bet against them and had helped choose the assets that would determine who won or lost."

Kenneth R. Lench, Chief of the Structured and New Products Unit in the SEC Division of Enforcement, added, "As the collateral manager, Credit Suisse also was responsible for the disclosure failures and breached its fiduciary duty to investors when it allowed Citigroup to significantly influence the portfolio selection process."

According to the SEC's complaints filed in U.S. District Court for the Southern District of New York, personnel from Citigroup's CDO trading and structuring desks had discussions around October 2006 about the possibility of establishing a short position in a specific group of assets by using credit default swaps (CDS) to buy protection on those assets from a CDO that Citigroup would structure and market. After discussions began with Credit Suisse Alternative Capital (CSAC) about acting as the collateral manager for a proposed CDO transaction, Stoker sent an e-mail to his supervisor. He wrote that he hoped the transaction would go forward and described it as the Citigroup trading desk head's "prop trade (don't tell CSAC). CSAC agreed to terms even though they don't get to pick the assets."

The SEC alleges that during the time when the transaction was being structured, CSAC allowed Citigroup to exercise significant influence over the selection of assets included in the Class V III portfolio. The transaction was marketed primarily through a pitch book and an offering circular for which Stoker was chiefly responsible. The pitch book and the offering circular were materially misleading because they failed to disclose that Citigroup had played a substantial role in selecting the assets and had taken a $500 million short position that was comprised of names it had been allowed to select. Citigroup did not short names that it had no role in selecting. Nothing in the disclosures put investors on notice that Citigroup had interests that were adverse to the interests of CDO investors.

According to the SEC's complaints, the Class V III transaction closed on Feb. 28, 2007. One experienced CDO trader characterized the Class V III portfolio in an e-mail as "dogsh!t" and "possibly the best short EVER!" An experienced collateral manager commented that "the portfolio is horrible." On Nov. 7, 2007, a credit rating agency downgraded every tranche of Class V III, and on Nov. 19, 2007, Class V III was declared to be in an Event of Default. The approximately 15 investors in the Class V III transaction lost virtually their entire investments while Citigroup received fees of approximately $34 million for structuring and marketing the transaction and additionally realized net profits of at least $126 million from its short position.

The SEC alleges that Citigroup and Stoker each violated Sections 17(a)(2) and (3) of the Securities Act of 1933. While the SEC's litigation continues against Stoker, Citigroup has consented to settle the SEC's charges without admitting or denying the SEC's allegations. The settlement is subject to court approval. Citigroup consented to the entry of a final judgment that enjoins it from violating these provisions. The settlement requires Citigroup to pay $160 million in disgorgement plus $30 million in prejudgment interest and a $95 million penalty for a total of $285 million that will be returned to investors through a Fair Fund distribution. The settlement also requires remedial action by Citigroup in its review and approval of offerings of certain mortgage-related securities.

The SEC instituted related administrative proceedings against CSAC, its successor in interest Credit Suisse Asset Management (CSAM), and Bhatt. The SEC found that as a result of the roles that they played in the asset selection process and the preparation of the pitch book and the offering circular for the Class V III transaction, CSAM and CSAC violated Section 206(2) of the Investment Advisers Act of 1940 (Advisers Act) and Section 17(a)(2) of the Securities Act and that Bhatt violated Section 17(a)(2) of the Securities Act and caused the violations of Section 206(2) of the Advisers Act by CSAC.

Without admitting or denying the SEC's findings, CSAM and CSAC consented to the issuance of an order directing each of them to cease and desist from committing or causing any violations, or future violations, of Section 206(2) of the Advisers Act and Section 17(a)(2) of the Securities Act and requiring them to pay disgorgement of $1 million in fees that it received from the Class V III transaction plus $250,000 in prejudgment interest, and requiring them to pay a penalty of $1.25 million. Without admitting or denying the SEC's findings, Bhatt consented to the issuance of an order directing him to cease and desist from committing or causing any violations or future violations of Section 206(2) of the Advisers Act and Section 17(a)(2) of the Securities Act and suspending him from association with any investment adviser for a period of six months.

The SEC's investigation was conducted by Andrew H. Feller and Thomas D. Silverstein of the Enforcement Division's Structured and New Products Unit with assistance from Steven Rawlings, Brenda Chang and Elisabeth Goot of the New York Regional Office. The SEC trial attorney who will lead the litigation against Stoker is Jeffrey Infelise.

For more information about dozens of other SEC enforcement actions related to the financial crisis, visit the SEC website at: http://www.sec.gov/spotlight/enf-actions-fc.shtml.

# # #

For more information about these enforcement actions, contact:

Kenneth R. Lench
Chief of Structured and New Products Unit, SEC Division of Enforcement
(202) 551-4938

Reid A. Muoio
Deputy Chief of Structured and New Products Unit, SEC Division of Enforcement
(202) 551-4488

http://www.sec.gov/news/press/2011/2011-214.htm

EXHIBIT 2

TO DECLARATION OF DENNIS M. KELLEHER IN SUPPORT OF MEMORANDUM IN OPPOSITION TO PROPOSED SETTLEMENT

(TA EX. 2)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK 11 CIV 7388

U.S. SECURITIES AND EXCHANGE COMMISSION, **Plaintiff,** **v.** **BRIAN H. STOKER,** **Defendant.**	**COMPLAINT** **11-CV-__________ ( )** **ECF CASE** Jury Trial Demanded

Plaintiff Securities and Exchange Commission ("Commission") alleges as follows against the defendant Brian H. Stoker ("Stoker"):

SUMMARY

1. The Commission brings this securities fraud action against Brian H. Stoker, who was an employee of Citigroup Global Markets, Inc. (along with certain affiliates, "Citigroup"), relating to his role in the structuring and marketing of a largely synthetic collateralized debt obligation ("CDO") called Class V Funding III ("Class V III"). The investment portfolio for Class V III consisted primarily of credit default swaps ("CDS") referencing other CDO securities whose value was tied to the United States residential housing market. Citigroup structured and marketed this $1 billion "CDO squared" in early 2007 when the housing market and the securities linked to the U.S. housing market were already beginning to show signs of distress. CDO squareds, such as Class V III, were designed to, and did, provide leveraged exposure to the housing market and therefore magnified the severity of losses suffered by investors when the United States housing market experienced a downturn.

2. Citigroup's marketing materials for Class V III, including a pitch book and offering circular, represented that the investment portfolio was selected pursuant to an extensively described asset selection process undertaken by Credit Suisse Alternative Capital, Inc. ("CSAC"), a registered investment adviser that was promoted as having experience and expertise in analyzing credit risk in CDOs. Undisclosed in the marketing materials and unbeknownst to investors, Citigroup exercised significant influence over the asset selection process for the purpose of creating a tailored, proprietary bet against the collateral of Class V III. Through its influence on the selection of the investment portfolio, Citigroup was able to short a set of assets it hand-picked by entering into CDS to buy protection on those assets from Class V III. The CDS assets on which Citigroup bought protection had a notional value of approximately $500 million, representing half of Class V III's investment portfolio. The marketing materials Citigroup prepared and distributed to investors did not disclose Citigroup's role in selecting assets for Class V III and did not accurately disclose to investors Citigroup's short position on those assets.

3. In sum, while ostensibly acting in its customary role as arranger of a CDO intended to benefit the CDO's investors, Citigroup in fact used Class V III as a proprietary trade, whereby it furthered its own economic interests, which were directly adverse to those of Class V III's investors, without disclosing its role in the selection of assets or the short position it took with respect to those assets.

4. Stoker was Citigroup's lead structurer on Class V III and was responsible for ensuring the accuracy of the offering circular and pitch book. Stoker was aware that Citigroup was using Class V III as a proprietary trade and, that even prior to the outset of the transaction, Citigroup intended to short a specific set of assets into the Class V III investment

portfolio. Stoker was also involved in the drafting and distribution of the offering materials. Notwithstanding his knowledge, Stoker did not ensure that the offering materials accurately described Citigroup's role in selecting the assets, Citigroup's intention to use Class V III as a proprietary trade, and Citigroup's shorting of $500 million of assets in Class V III.

5. Class V III closed on February 28, 2007. At closing, Citigroup was paid approximately $34 million in fees for structuring and marketing Class V III. On or about that date and in the following weeks, Citigroup sold approximately $343 million of Class V III's equity and mezzanine liabilities ("notes") to approximately fourteen (14) institutional investors ("Subordinate Investors"), all of whom received some or all of the marketing materials for Class V III. The Subordinate Investors included hedge funds, investment managers, and other CDO vehicles. On or about March 16, 2007, Ambac Credit Products ("Ambac"), an affiliate of Ambac Assurance Corporation, a monoline insurance company, agreed to sell protection to an affiliate of Citigroup on the $500 million super-senior tranche of Class V III, meaning that Ambac effectively invested in that tranche by assuming the credit risk associated with that portion of the capital structure via CDS in exchange for premium payments. The transaction with Ambac was intermediated by a European financial institution (together with Ambac, the "Super-Senior Investors").

6. By November 6, 2007, approximately 83 percent of the CDO assets referenced in the Class V III investment portfolio had been downgraded by rating agencies. Class V III declared an event of default on November 19, 2007. As a result of the poor performance of the investment portfolio, the Subordinate Investors and Super-Senior Investors lost several hundred million dollars. Through its fees and its short position on the $500 million in assets in Class V III, Citigroup realized net profits of at least $160 million.

7. By engaging in the conduct described herein, Stoker violated Sections 17(a)(2) and (3) of the Securities Act of 1933 [15 U.S.C. §77q(a)(2) and (3)] ("the Securities Act") by misrepresenting key deal terms in Class V III, namely, the process by which the investment portfolio was selected and Citigroup's financial interest in the transaction, and by engaging in a course of business that operated as a fraud upon investors in Class V III. The Commission seeks injunctive relief, disgorgement of profits, prejudgment interest, civil penalties and other appropriate and necessary equitable relief from the defendant.

JURISDICTION AND VENUE

8. This Court has jurisdiction and venue over this action pursuant to Sections 20(b), 20(d) and 22(a) of the Securities Act [15 U.S.C. §§ 77t(b), 77t(d), 77v(a)]. Stoker transacted business related to Class V III in this judicial district and, directly or indirectly, made use of the means or instrumentalities of interstate commerce, or of the mails, or the facilities of a national securities exchange therein.

DEFENDANT

9. **Brian H. Stoker,** age 40, was a Director in the CDO structuring group at Citigroup from March 2005 through August 2008. Stoker was the principal Citigroup employee responsible for overseeing the structuring of Class V III and the drafting of the offering memorandum and pitch book. Stoker obtained his Series 7 and 63 licenses in 1998, but has not been a registered broker since 2008. Stoker lives in Pound Ridge, New York.

RELATED ENTITIES

10. **Citigroup Global Markets Inc. ("Citigroup Global Markets")** is and was the principal U.S. broker-dealer of Citigroup Inc., a global financial services firm

headquartered in New York City. Citigroup Global Markets structured and marketed Class V III.

11. **Credit Suisse Alternative Capital, LLC ("CSAC")** was an investment adviser registered with the Commission and based in New York, New York until December 2010, when it became Credit Suisse Asset Management, LLC ("CSAM"). CSAC acted as the collateral manager for Class V III. CSAC was a wholly-owned subsidiary of Credit Suisse Securities (USA) LLC. Credit Suisse Securities (USA) LLC, an investment adviser and broker-dealer based in New York, New York, is and was the principal U.S. broker-dealer and investment advisory subsidiary of Credit Suisse Group, a global financial services firm based in Switzerland.

FACTS

A. THE STRUCTURE OF A CDO SQUARED

12. CDOs are debt securities collateralized by fixed income obligations, including residential mortgage backed securities ("RMBS"). Investors in CDO notes receive payments derived from the cash flows produced by the investment portfolio of the CDO. The notes issued by a CDO are securities with defined risk profiles determined by a hierarchical, tranched structure. The cash flows from the CDO's investment portfolio are divided according to defined rights among the tranches of the CDO in a waterfall fashion. The "super senior" tranche is at the top of the waterfall with the first right to receive principal and interest if there is a shortfall. As a result, the super senior tranche is considered to have the highest credit quality, meaning the lowest likelihood of being affected by problems in the underlying collateral. The lower, "mezzanine" tranches are junior in priority and, therefore,

carry more risk. Below the mezzanine tranches are the subordinated notes, or equity, which are the first to experience losses.

13. A CDS is an over-the-counter derivative contract that functions like insurance on a so-called "reference asset." In a CDS transaction, a "protection buyer" makes periodic premium payments to a "protection seller." In exchange, the protection seller promises to make a contingent payment to the protection buyer if an agreed-upon reference obligation (such as a CDO) experiences a "credit event," such as a default. Thus, the protection seller is effectively taking a long position on the reference asset (i.e., betting it will perform), while the protection buyer is effectively taking a short position on the reference asset (i.e., betting it will perform poorly).

14. A CDO collateralized by bonds is known as a "cash CDO." A CDO collateralized by tranches of other CDOs is known as a "CDO squared." A CDO collateralized only by CDS is called a "synthetic CDO." A hybrid CDO is a CDO collateralized by both cash assets (i.e., bonds) and synthetic assets (i.e., CDS). Class V III was a hybrid CDO.

15. A CDO squared is created through a special purpose vehicle ("SPV") that issues notes entitling the note-holders to payments derived from the underlying assets. Investors in the notes issued by a cash CDO squared receive payments derived from the principal and interest paid by the CDO tranches in the CDO's investment portfolio. However, with respect to a synthetic CDO squared, the SPV does not actually own a portfolio of fixed income assets, but rather enters into a CDS whereby the SPV acts as the protection seller to one or more counterparties on a portfolio of reference assets, or "names,"

which in the case of a synthetic CDO squared would be specified tranches of other CDOs. Investors in the notes issued by a synthetic CDO receive payments derived from the periodic premium payments from the protection buyer.

16. Prior to the date on which a CDO closes, it is typical for the arranging bank to have acquired most of the collateral on behalf of the SPV. The acquiring bank typically finances the acquisition of collateral and places acquired collateral in a segregated account or "warehouse." This pre-closing process is called "warehousing." If there is an asset manager for the CDO squared, it is the collateral manager, not the arranging bank, that directs what assets will be acquired by the warehouse. The arranging bank, which provides the warehouse, bears the risk of loss on the assets in the warehouse prior to closing. In the case of a synthetic CDO, the arranging bank, in its role as initial CDS asset counterparty, will buy protection from the warehouse. In that instance, prior to the closing of the CDO, the warehouse is merely an entry on the arranging bank's balance sheet and the arranging bank is essentially selling protection to itself.

17. Typically, in a CDO with synthetic assets, the arranging bank plays the role of initial CDS asset counterparty, meaning the arranging bank is the sole counterparty facing the CDO for synthetic collateral. This role is usually defined in the indenture for the CDO. Arranging banks, in their role as CDS asset counterparty, typically act through their trading desks as intermediaries between the CDO and other market participants. If a collateral manager identifies a counterparty with whom it wants to trade for the CDO's portfolio, the arranging bank will intermediate that trade (that is, sell protection to that counterparty and simultaneously buy protection from the CDO) in exchange for a small "intermediation fee." However, the arranging bank can purchase protection directly from the CDO, either for a

customer who it knows to be interested in assuming that position, or for the arranging bank's own account. When the arranging bank trades directly with the CDO, there is no intermediation fee, but the arranging bank typically sells protection on that asset to one of its customers in order to capture as profit the difference between what it pays for protection and what it charges its customer (the "spread" between the two trades) without retaining any of the risk of the asset itself.

18. When a synthetic CDO closes and the assets are transferred to the SPV, the SPV will be the protection seller. The money the SPV receives from investors is used to make any contingent payments if there are credit events on the assets in the reference portfolio. Thus, once the arranging bank sells the synthetic CDO notes to outside investors, those investors are effectively in the position of protection seller on the reference portfolio (they have taken the long side of the underlying CDS transactions).

19. The arranging bank for a synthetic CDO was understood to profit from the fees it charges for structuring and marketing the transaction, any fees it received for intermediating trades, and the spread it captured by buying protection from the CDO and selling protection to its customers.

B. THE DEMAND FOR "SHORT" POSITIONS ON CDO TRANCHES

20. During late 2006 and early 2007, certain hedge funds and other market participants came to believe that CDOs whose assets consisted primarily of BBB-rated subprime RMBS (so-called "mezzanine" CDOs) would experience significant losses, leading even the A-rated tranches of mezzanine CDOs to potentially become worthless. These

market participants sought to profit from a downturn in the United States housing market by buying protection through CDS on A-rated tranches of mezzanine CDOs originated in 2006.

21. Citigroup's CDO trading desk was one of the most active traders of CDS referencing CDOs. By late October 2006, Citigroup's CDO trading desk had a large number of hedge fund customers seeking to buy protection on CDO tranches, particularly on mezzanine CDOs originated in 2006. In particular, Citigroup's CDO trading desk was aware that there was a large demand from market participants to purchase protection on mezzanine CDOs that were part of a series of transactions that shared certain structural and other features and were named after constellations (the "Constellation Series"). Indeed, as Citigroup knew, a significant portion of the market interest in shorting the Constellation CDOs came from the very hedge fund that helped create those CDOs. The Citigroup CDO trading desk also was aware that there was great demand from market participants to purchase protection on a similar group of CDOs, known as "President" deals. In other words, the Citigroup CDO trading desk was aware that many market participants were seeking to bet that the Constellation and President deals would perform poorly.

22. The increased demand for protection in the market led to the widening of spreads that market participants were willing to pay for protection on single A-rated tranches of CDOs. CDS were typically priced based on a spread over a risk free funding rate, such as LIBOR. All other things being equal, a wider spread on a CDS indicates a higher level of perceived riskiness in the reference asset. With this widening of spreads, internal discussions began at Citigroup about the feasibility of structuring and marketing a CDO squared collateralized by single A-rated tranches.

23. A significant part of Citigroup's rationale for pursuing such a transaction was the desire of its CDO trading desk to buy protection on A-rated tranches of mezzanine CDOs originated in 2006 for its own account, without an offsetting long trade with a customer. Such positions were known as "naked short" positions. These naked short positions would mirror the trades entered into by certain of the CDO trading desk's hedge fund customers and would position Citigroup to realize profits in the event of a downturn in the United States housing market.

B. STRUCTURING OF CLASS V III -- PHASE ONE

24. Beginning in or around October 2006, personnel from Citigroup's CDO trading desk had discussions with Stoker and others on Citigroup's CDO structuring desk about the possibility of the CDO trading desk establishing short positions in a specific group of assets, including several Constellation and President deals, by buying protection from a CDO squared that Citigroup would structure and market. Stoker and others within Citigroup also discussed the possibility of having the CDO squared purchase unsold tranches from CDOs previously structured by Citigroup.

25. Citigroup knew it would be difficult to place the liabilities of a CDO squared if it disclosed to investors its intention to use the vehicle to short a hand-picked set of CDOs and to buy Citigroup's hard-to-sell cash CDOs. By contrast, Citigroup knew that representing to investors that an experienced, third-party investment adviser had selected the investment portfolio would facilitate the placement of the CDO squared's liabilities.

26. On or around October 19, 2006, Citigroup initiated discussions with CSAC about CSAC acting as collateral manager for the proposed CDO squared. CSAC was a

registered investment adviser that had previously acted as the collateral manager for several other CDOs.

27. On October 23, 2006, a Managing Director on Citigroup's CDO trading desk sent Stoker a list of 21 recent-vintage, mezzanine CDOs on which the CDO trading desk wished to buy protection from the CDO squared. Eighteen of the 21 names the Managing Director forwarded were Constellation or President deals.

28. On or about October 26, 2006, Stoker discussed with others within Citigroup potential structures for the CDO squared, as well as the possibility that Citigroup would short assets into the CDO squared. On or about October 27, Stoker prepared (or had prepared) and distributed internally to Citigroup's CDO trading desk and others, several models showing the potential profits to Citigroup from shorting assets into the CDO squared.

29. On or about October 30, 2006, Stoker sent the Citigroup CDO salesperson who covered CSAC the list of 21 CDOs that Stoker had received from the Managing Director on the CDO trading desk on October 23, 2006.

30. On November 1, 2006, the Citigroup CDO salesperson forwarded the list he received from Stoker, along with four additional names he received from the trading desk, to CSAC, describing the list as CDOs that were "contemplated to be in the [CDO squared] portfolio."

31. On November 2, 2006, the Managing Director on the CDO trading desk informed Stoker that CSAC appeared "amenable to the portfolio" and "receptive to the concept," and asked Stoker to draft an engagement letter for CSAC.

32. On November 3, 2006, Stoker drafted an engagement letter for CSAC and circulated it internally with the subject line "CSAC CDO Squared." Later that day, in response to receiving the draft engagement letter, Stoker's immediate supervisor inquired "Are we doing this?" Stoker responded: "I hope so. This is [the CDO trading desk]'s prop trade (don't tell CSAC). CSAC agreed to terms even though they don't get to pick the assets." The term "prop trade" is shorthand for "proprietary trade," meaning a trade undertaken for a firm's own account, rather than on behalf of the firm's customer(s).

33. On November 14, 2006, Stoker's immediate supervisor informed Stoker that Stoker should take action to ensure that the structuring desk received "credit for [the CDO trading desk's] profits" on Class V III.

34. On November 22, 2006, Stoker distributed internally to Citigroup's CDO trading desk and others, "the latest structure" of Class V III, in which he recommended that the President and Constellation deals included in the deal should be those having a single-A rating.

C. STRUCTURING OF CLASS V III – PHASE TWO

35. In late December 2006, CDS spreads on single-A CDO tranches widened further, and Citigroup renewed its efforts to finalize the engagement with CSAC and move forward with the CDO squared. As a result of those efforts, CSAC and Citigroup agreed to proceed with the transaction.

36. On December 21, 2006, CSAC sent the Citigroup CDO salesperson a list of 127 CDOs as potential candidates for inclusion in the CDO squared. The names identified

were diversified by deal type and vintage, with only a portion represented by recent-vintage, mezzanine CDOs. The list included approximately 19 of the original 25 names Citigroup provided CSAC on November 1, 2006. The Citigroup CDO salesperson forwarded a copy of the list to Stoker and others at Citigroup.

37. On the morning of January 8, 2007, Citigroup's CDO trading desk selected 25 CDOs from CSAC's December 21, 2006 list and provided the 25 names to the Citigroup CDO salesperson. Sixteen of the 25 names Citigroup selected were on the original list it provided to CSAC on November 1, 2006, and all but one of the 25 names were 2006, mezzanine CDOs; the sole exception was a mezzanine CDO that closed in December 2005. Later that morning, the Citigroup CDO salesperson sent the list of 25 names to CSAC with the statement, "Here are the names where we would like to buy protection from CSAC." Within an hour, CSAC agreed to include the 25 CDOs in the investment portfolio by selling protection to Citigroup on those names. The notional amount of CDS referencing these CDOs was $250 million. Sixteen of the names Citigroup selected were Constellation of President deals with a notional value of $160 million.

38. On the morning of January 8, 2007, Stoker learned that CSAC intended to sell Citigroup's CDO trading desk protection on CDOs with a notional value of $250 million for the Class V III investment portfolio.

39. Also, on or about January 8, 2007, Citigroup and CSAC entered into an engagement letter, drafted by Stoker, pursuant to which Citigroup agreed to serve as "Placement Agent" and CSAC agreed to serve as "Manager" for Class V III. The letter states that "the Manager [CSAC] agrees to identify Collateral that meets the criteria

established for the Transaction," and that "the Manager will direct the purchase of securities for the Collateral."

40. On or about January 10, 2007, CSAC selected 18 additional CDO tranches on which protection would be sold for the investment portfolio with little or no involvement from Citigroup. The counterparties who would buy the CDS on these synthetic assets were identified using a "bid wanted in competition" or "BWIC" process, pursuant to which a list of bonds is submitted to various brokers to solicit bids for protection. The notional amount of CDS on these CDOs was $220 million.

41. On or about January 11, 2007, Citigroup and CSAC agreed to increase the size of the Class V III transaction from $500 million to $1 billion.

42. On or about January 12, 2007, Citigroup and CSAC reached an agreement pursuant to which CSAC doubled the credit exposure of Class V III to the original 25 CDOs that Citigroup selected for the investment portfolio by selling additional protection to Citigroup at agreed-upon premiums. The original notional amount of the CDS involved was $250 million, which increased Citigroup's short position to a notional amount of approximately $500 million, representing half of Class V III's investment portfolio.

43. Of the $500 million of short positions that Citigroup purchased on January 8 and 12, 2007, $490 million were naked shorts, or names in which Citigroup's CDO trading desk was not already holding an unhedged, long position.

44. Over the course of the next month, CSAC selected additional CDOs to include in Class V III via CDS with little or no involvement from Citigroup. The notional amount of

CDS on these CDOs was approximately $150 million. This brought the total notional amount of synthetic CDOs included in the investment portfolio for Class V III to approximately $870 million.

45. The investment portfolio for Class V III also included nine cash CDOs with a total notional amount of $130 million. Six of these nine cash CDOs, with a face value of $92.25 million, were from CDOs structured and marketed by Citigroup. CSAC did not apply to these securities the rigorous credit analysis described in the marketing materials for Class V III.

46. On or about February 14, 2007, the Managing Director on the CDO trading desk communicated to Citigroup's Risk Management that the CDO trading desk's intention was to retain the short position in the Class V III collateral even if Citigroup sold all the tranches of Class V III. This decision permitted Citigroup to remain positioned to profit from the negative performance of the Class V III collateral even as it was marketing Class V III to investors.

D. DISCLOSURES RELATING TO PORTOLIO SELECTION AND FINANCIAL INTERESTS

47. The two primary marketing documents for Class V III were the offering circular (similar to a statutory prospectus) and the pitch book (a PowerPoint presentation used in discussions with potential investors). Both documents were prepared by Citigroup. As lead structurer for Class V III, Stoker was responsible for ensuring the accuracy and completeness of the offering circular and the pitch book. For Class V III, both documents were adapted from models used by Citigroup for earlier, similar transactions.

48. The pitch book was specifically adapted from a transaction called Adams Square II ("Adams Square") on which Citigroup and CSAC had collaborated in early January 2007. The Citigroup structuring team, under the direction of Stoker, revised the Adams Square pitch book to reflect various deal terms in Class V III, while retaining the risk factors listed in the Adams Square pitch book.

49. Citigroup's pitch book for Class V III, which was finalized on or about February 5, 2007, represented in its "Transaction Overview" that CSAC was the "collateral manager" and "Manager" and that CSAC had selected the collateral for Class V III. The "Manager" section, a 20-page section originally provided by CSAC, provided an overview of CSAC, described its track record and investment philosophy, and, most significantly included a detailed, 9-page section titled "Portfolio Construction and Management," purporting to describe CSAC's rigorous approach to selecting each asset it included in the investment portfolio of its CDOs. This section represented that CSAC "utilizes a credit-intensive, relative value investment approach in managing structured finance assets," and that it "believes performance is driven by a strong credit culture and systematic investment process." Another sub-section touted CSAC's "CDO Investment Process," which it claimed included three steps: "Evaluation of Transaction Structure," "Evaluation of Collateral Manager," and "Evaluation of Underlying Collateral." Another page represented that a key element of CSAC's "process" was "bottom-up fundamental security selection." The Risk Factors section of the pitch book, prepared by Citigroup, stated that CSAC had "selected" the collateral for Class V III.

50. The offering circular for Class V III also was drafted by Citigroup's structuring team under the direction of Stoker. Stoker sought to standardize the deal

documents used by Citigroup for CDOs, including the offering circular, in order to ease the speedy execution of multiple deals and thereby increase Citigroup's fee revenue. As part of that effort, Stoker based the Class V III offering circular on the offering circular for an earlier deal, which he used as a template.

51. In February 2007, Stoker made substantial edits to the preliminary offering circular for Class V III but made no changes or edits to the sections stating that CSAC selected the assets or the section describing Citigroup's position as initial swap counter-party. Stoker did nothing to determine whether the statements about the asset selection process, or about CSAC's role in selecting the assets, were accurate.

52. Although Stoker had information at the time the Class VIII offering circular was being drafted that Citigroup's Trading desk was using Class V III to establish a large proprietary short position, he made no attempt to obtain information from the Trading desk about the size of its short position or otherwise take action to ensure that the disclosure documents were accurate concerning Citigroup's interest in Class V III.

53. On or about February 26, 2007, Citigroup finalized an offering circular for Class V III.

54. The cover page of the finalized version of the Class V III offering circular stated that CSAC "will act as the manager for the portfolio of assets." The offering circular also made at least six separate representations that the investment portfolio was "selected" by CSAC. A section titled "The Manager," drafted by CSAC, trumpets CSAC's expertise and experience with CDO management and asset selection, and includes a representation that "selection of the Eligible Collateral Debt Securities is based primarily on structural and credit

analysis as well as technical factors which may influence trading levels and pricing." In another section, the offering circular identified as a risk factor that the performance of Class V III's investment portfolio "depends on the investment strategy and investment process of the Manager in analyzing, selecting and managing the [portfolio]."

55. Both the pitch book and the offering circular contained a disclosure concerning Citigroup's role as "Initial CDS Asset Counterparty," including an explanation of the potential conflicts of interest deriving from Citigroup assuming that role. This generic disclosure provided investors with no information as to Citigroup's long-term interest in the negative performance of the assets.

56. Page 88 of the 192-page offering circular included a statement that "The Initial CDS Asset Counterparty may provide CDS Assets as an intermediary with matching off-setting positions requested by the Manager or may provide CDS Assets alone without any off-setting positions." As with the generic disclosures about Citigroup's role, this disclosure did not provide any information about the extent of Citigroup's long-term interest in the negative performance of the collateral in Class V III, or even whether Citigroup actually had any short positions in the collateral at all.

57. Nothing in the offering circular, or in the pitch book's description of the asset selection process included any reference to the role played by Citigroup in selecting half of the Class V III investment portfolio.

58. Similarly, nothing in the pitch book or offering circular disclosed that Citigroup had taken a $490 million naked short position on the 25 names it had selected for Class V III. Stoker knew that Class V III was intended to be the Citigroup CDO trading

desk's "prop trade," and he was responsible for the preparation of models showing the profits that Citigroup would reap from shorting assets into Class V III.

59. The pitch book and offering circular were materially misleading because they failed to disclose:

a. Citigroup's substantial role in selecting names for Class V III;

b. That Citigroup had taken a $500 million proprietary short position on the Class V III collateral, including a $490 million naked short position; and

c. That Citigroup's proprietary short position was comprised of the names it had been allowed to select; while Citigroup did not short those names which it had no role in selecting.

60. Taken together, the misleading and inaccurate disclosures led investors to believe that Class V III's investment portfolio was selected by CSAC, pursuant to a rigorous, proprietary selection process, and that Citigroup and its affiliates would play the traditional role of an arranging bank in such a transaction. Nothing in the disclosures put investors on notice that fully $500 million of the $1 billion investment portfolio was comprised of assets Citigroup had selected and on which it had taken a naked short position directly adverse to the interests of the investors to whom it was marketing Class V III.

Stoker knew or should have known the role that Citigroup played in selecting collateral for Class V III. Stoker also knew or should have known that the failure to disclose this information in the pitch book and offering memorandum rendered them materially misleading to investors in Class V III.

E. CLASS V III'S INVESTORS

61. Beginning in late January 2007, Citigroup made an intense effort to sell the Class V III tranches. This effort involved offering Class V III broadly through the Citigroup CDO Sales group to many of Citigroup's institutional clients, including a variety of hedge funds, asset managers, and both US and foreign financial institutions. Citigroup provided the pitch book and offering circular to prospective investors.

62. On or about February 6, 2007, Stoker personally sent a copy of the Class V III pitch book to a prospective investor, along with a representation that Class V III was a "top-of-the-line CDO squared."

63. On or around February 6, 2007, a prospective investor in Class V III asked Citigroup to arrange a call with CSAC, in order to seek an explanation for why CSAC had chosen to invest in several "static" CDOs (i.e., CDOs with non-managed portfolios). Each of the static transactions in the portfolio seen by the potential investor had been selected by Citigroup on January 8, 2007. After learning that the potential investor was raising questions, the head of Citigroup's Syndicate desk told several individuals at Citigroup, including Stoker that, "[CSAC] bought these static bonds and . . . should have a rationale as to why [CSAC] found them attractive." One of the structurers who had been on the call with the potential investor and CSAC responded to everyone, including Stoker, "[CSAC] can come up with some stories for some of the static deals in Class V pool, but not all of them."

64. Stoker knew or should have known that Citigroup intended to use the Class V III transaction as a means of establishing a position that would maximize Citigroup's profit in a falling market by taking a $500 million short position on the 25 names it selected for the

investment portfolio. Stoker also knew or should have known that the use of Class V III for this purpose without fully disclosing that position would operate as a fraud upon the investors in Class V III.

65. Ultimately, approximately 15 different investors purchased or sold protection on tranches of Class V III with a face value of approximately $893 million. Many of the investors in Class V III considered CSAC's purported experience as a collateral manager and rigorous asset selection process to be important to their investment decision.

66. The largest investor in Class V III was Ambac. Ambac was first approached by Citigroup on January 12, 2007, about selling protection on the super senior tranche of Class V III. In January and February 2007, Stoker participated in extensive discussions with Ambac about the terms of Ambac's investment in Class V III. Ambac received multiple drafts of the offering circular from Citigroup during that time.

67. Ambac typically invested in CDOs with portfolios selected by a collateral manager. Ambac's internal documents approving the investment in Class V III contain extensive discussion of CSAC's purported expertise and asset selection process, and note the importance of CSAC's "perceived disciplined approach to the selection of securities."

68. On or around February 12, 2007, Stoker personally provided a copy of the preliminary offering circular to Ambac.

69. Ambac was unaware of Citigroup's approximately $500 million short position in Class V III or the extent of Citigroup's influence on the asset selection process. Information concerning Citigroup's short position would have been material to Ambac's

decision to sell protection on the super senior tranche of Class V III. Had Ambac been aware that arranging banks such as Citigroup were using synthetic CDOs to establish and profit from large short positions, Ambac would have ceased its involvement in the CDO business immediately.

70. Citigroup also offered and sold notes with a par value of $393 million to the Subordinate Investors, a group of approximately fourteen (14) institutional investors including hedge funds, investment managers and other CDO vehicles. Citigroup provided the Subordinate Investors with marketing materials for Class V III, including the pitch book and offering circular.

71. The Class V III transaction closed on February 28, 2007. Effective March 16, 2007, Ambac agreed to sell protection on the $500 million super senior tranche of Class V III, meaning it effectively invested in that tranche by assuming the credit risk associated with that portion of the capital structure via CDS in exchange for premium payments. The super senior transaction with Ambac was intermediated by BNP Paribas ("BNP"), a large European financial institution. This meant that, through a series of CDS, BNP assumed the credit risk associated with the super senior tranche of Class V III in the event and only to the extent Ambac was unable to pay.

72. The CDS between and among Citigroup, Ambac and BNP relating to the super senior tranche of Class V III were entered into, in whole or in part, in New York, New York. Each of the CDS was subject to an agreement between the relevant parties that the transaction would be governed by the laws of the state of New York

73. Citigroup offered and sold the notes for Class V III in New York, New York, and delivered them to the Subordinate Investors in book-entry form through the Depository Trust Company in New York, New York on or about the closing date.

74. At the time they invested in the Class V III transaction, the Subordinate Investors were unaware that Citigroup had played a significant role in selecting 25 names for the Class V III investment portfolio, or that Citigroup had taken a $500 million short position, including a $490 million naked short position, on those assets. Neither at closing nor at the time it agreed to sell protection on the super senior tranche of Class V III did Stoker or anyone else at Citigroup inform Ambac that Citigroup had taken a $500 million short position, including a $490 million naked short position, on assets it selected for Class V III.

F. <u>THE PERFORMANCE OF CLASS V III</u>

75. By late July 2007, 14 of the 58 assets in the Class V III portfolio had been placed on negative watch by Moody's and/or Standard & Poor's. Eleven of the 14 assets placed on the watch list were assets that Citigroup selected and on which it then purchased protection. By early November 2007, approximately 33.4 percent of all the assets in Class V III had been downgraded.

76. The 25 names that Citigroup selected for Class V III and on which it purchased $500 million of protection performed significantly worse than other names in Class V III and significantly worse than approximately 102 other names on the list that CSAC provided to Citigroup on December 21, 2006 that were not selected for Class V III.

77. On November 7, 2007, Moody's downgraded every tranche of Class V III, and on November 19, 2007, as a result of the severity of the downgrades of the underlying collateral, Class V III was declared to be in an Event of Default. The Subordinate Investors lost most, if not all, of their principal when their notes became nearly worthless.

78. Ambac began suffering significant losses on the super senior tranche of Class V III towards the middle of 2008 and settled its exposure toward the end of that year by paying BNP $305 million. BNP has suffered additional losses on the super senior tranche in excess of $100 million.

79. Citigroup was paid approximately $34 million in fees for structuring and marketing Class V III and, as a result of the fees Citigroup received and its short position on the $500 million in assets in Class V III, Citigroup realized net profits of approximately $160 million.

80. Citigroup paid Stoker a salary and a bonus for his work as a structurer on CDOs, including Class V III. In 2006, Stoker was paid a salary of $150,000 and a bonus of $1,050,000. In February 2007, Stoker negotiated a salary of $150,000 and a guaranteed bonus of $2.25 million for 2007.

CLAIM FOR RELIEF

Sections 17(a)(2) and (3) of the Securities Act

81. Paragraphs 1-80 are realleged and incorporated herein by reference.

82. As set forth above, Stoker, in the offer or sale of securities or securities-based swap agreements, by the use of the means or instruments of interstate commerce or by the mails, directly or indirectly, obtained money or property by means of untrue statements of

material facts or omissions of material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, and engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon purchasers of securities in violation of Sections 17(a)(2) and (3) of the Securities Act [15 U.S.C. § 77q(a)(2) & (3)].

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that this Court enter a judgment:

A. Permanently restraining and enjoining Stoker from violating Sections 17(a)(2) and (3) of the Securities Act of 1933 [15 U.S.C. §77q(a)(2) and (3)];

B. Ordering Stoker to disgorge all profits that it obtained as a result of its conduct, acts or courses of conduct described in this Complaint, and to pay prejudgment interest thereon; and

C. Ordering Stoker to pay civil monetary penalties pursuant to Section 20(d)(2) of the Securities Act [15 U.S.C. § 77t (d)(2)].

Dated: Washington, D.C.

October 19, 2011

Respectfully submitted,

<u>Of Counsel</u> Kenneth Lench Reid A. Muoio (RM-2274) Andrew Feller Thomas D. Silverstein	Richard Simpson (RS5859) Jeffrey Infelise (DC456998) 100 F St., NE Washington, D.C. 20549-4010 (202) 551-4904 (Infelise) (202) 772-9282 (Fax) simpsonr@sec.gov infelisej@sec.gov Attorneys for Plaintiff Securities and Exchange Commission

EXHIBIT 3

TO DECLARATION OF DENNIS M. KELLEHER IN SUPPORT OF MEMORANDUM IN OPPOSITION TO PROPOSED SETTLEMENT

(TA EX. 3)

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9268 / October 19, 2011

INVESTMENT ADVISERS ACT OF 1940
Release No. 3302 / October 19, 2011

ADMINISTRATIVE PROCEEDING
File No. 3-14594

In the Matter of **CREDIT SUISSE ALTERNATIVE CAPITAL, LLC (f/k/a CREDIT SUISSE ALTERNATIVE CAPITAL, INC.), CREDIT SUISSE ASSET MANAGEMENT, LLC, and SAMIR H. BHATT** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933 AND SECTIONS 203(e), 203(f), AND 203(k) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND CEASE-AND-DESIST ORDERS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 8A of the Securities Act of 1933 ("Securities Act") and Section 203(e) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act") against Credit Suisse Alternative Capital, LLC (f/k/a Credit Suisse Alternative Capital, Inc.) ("CSAC") and Credit Suisse Asset Management, LLC ("CSAM") and Section 8A of the Securities Act and Sections 203(f) and 203(k) of the Advisers Act against Samir H. Bhatt ("Bhatt") (collectively, "Respondents").

II.

In anticipation of the institution of these proceedings, CSAC has submitted an Offer of Settlement of Credit Suisse Alternative Capital, LLC (f/k/a Credit Suisse Alternative Capital, Inc.) ("CSAC Offer"), CSAM has submitted an Offer of Settlement of Credit Suisse Asset Management, LLC ("CSAM Offer"), and Bhatt has submitted an Offer of Settlement of Samir H. Bhatt ("Bhatt Offer"), all of which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the

Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933 and Sections 203(e), 203(f), and 203(k) of the Investment Advisers Act, Making Findings, and Imposing Remedial Sanctions and Cease-and-Desist Orders ("Order"), as set forth below.

III.

On the basis of this Order and Respondents' Offers, the Commission finds[1] that

A. Summary

1. This matter involves violations of federal securities laws by CSAC, the predecessor of CSAM, and Bhatt, a former registered representative and portfolio manager at CSAC, in connection with the structuring and marketing of a largely synthetic collateralized debt obligation ("CDO") known as Class V Funding III ("Class V III"). The investment portfolio for Class V III consisted primarily of credit default swaps ("CDS") referencing other CDO securities with collateral consisting primarily of subprime residential mortgage-backed securities ("RMBS"). As a result, the value of Class V III and its underlying investment portfolio was tied to subprime mortgages and the United States residential housing market. CDO-squareds such as Class V III were designed to, and did, provide leveraged exposure to the housing market and therefore magnified the severity of losses suffered by investors when the United States housing market experienced a downturn.

2. Class V III was structured and marketed by Citigroup Global Markets Inc. ("Citigroup"). The marketing materials for Class V III – including a pitch book and an offering circular – represented that the investment portfolio was selected by CSAC, a registered investment adviser. CSAC promoted itself as having experience and expertise in analyzing credit risk in CDOs, using an extensive asset selection process. Undisclosed to either investors or the directors of the special purpose vehicles ("SPVs") that issued the securities to investors in Class V III, CSAC allowed Citigroup to exercise significant influence over the composition of Class V III's investment portfolio.

3. Bhatt was the portfolio manager at CSAC primarily responsible for the Class V III transaction. Bhatt was responsible for selecting the assets in accordance with CSAC's stated processes, as well as for negotiating and executing the purchase of those assets on behalf of Class V III. Bhatt and CSAC understood that Citigroup was seeking to short assets into Class V either for itself or for its customers (though did not necessarily know which), and thus that Citigroup was representing economic incentives potentially adverse to those of Class V III and its investors.

[1] The findings herein are made pursuant to the CSAC Offer, the CSAM Offer, and the Bhatt Offer and are not binding on any other person or entity in this or any other proceeding.

Rather than follow CSAC's stated asset selection process, Bhatt provided Citigroup with a list of potential assets with which he had some familiarity, and allowed Citigroup to select from the list the names on which it wanted to purchase protection. The CDO securities on which Citigroup bought protection had a notional value of approximately $500 million, representing half of the Class V III investment portfolio. Citigroup's selections were weighted towards assets that were regarded by the market as particularly risky.

4. CSAC and Bhatt also represented in the pitch book that CSAC performed extensive credit analysis on all of the assets that it selected for the portfolio. In actuality, CSAC and Bhatt performed little-to-no analysis on several of the assets in the portfolio. Specifically, CSAC and Bhatt purchased several cash bonds from deals underwritten by Citigroup without having done any credit work on those bonds. The final Class V III investment portfolio contained nine cash bonds with a total value of approximately $130 million (approximately 13% of Class V III's total investment portfolio). Of those nine bonds, six, with a face value of $92.25 million, were purchased from Citigroup. For five of the six bonds purchased from Citigroup, CSAC and Bhatt did not perform the credit analysis as represented in the marketing materials. Bhatt was responsible for purchasing these bonds.

5. The offering circular for Class V III represented that the assets in the portfolio were purchased at "fair market value." This statement was inaccurate. Rather than seeking market bids, CSAC and Bhatt purchased most of the synthetic assets (i.e. those referenced by the sale of protection via CDS) in two separate portfolio trades with Citigroup. After determining that Citigroup had paid prices well below what was available in the market for individual assets (i.e. Citigroup had purchased protection for lower premium payments than it would have had to pay for the individual assets in a market transaction as of that day) for the first portfolio trade, CSAC and Bhatt nevertheless proceeded with a second portfolio trade with Citigroup. The prices CSAC and Bhatt obtained in that second trade were higher than for the first trade, but well below what was available in the market for individual assets. CSAC and Bhatt did not take meaningful action to verify that CSAC was obtaining market prices in the transactions with Citigroup. CSAC and Bhatt did not disclose to its client or to investors in Class V III that the synthetic assets were not acquired at market value.

6. CSAC and Bhatt participated in drafting the marketing materials, including the pitch book and offering circular, and provided the original drafts of the sections concerning CSAC and its stated collateral selection process. The documents themselves attributed responsibility for the content of those sections to CSAC. CSAC and Bhatt also helped market Class V III in meetings and conference calls with actual and potential investors. CSAC and Bhatt, in the marketing materials and in conversations with investors, did not disclose material facts about both the asset selection process and the price of the assets purchased by Class V III.

7. Using the marketing materials which CSAC and Bhatt had helped draft, Citigroup sold approximately $847 million of notes across the capital structure of Class V III to approximately 15 different investors. Investors in Class V III focused on CSAC's role in selecting assets in making its investment decision. They also considered the representations about the asset purchase prices to be important.

8. CSAC collected approximately $1 million in fees for managing Class V III. An affiliate of CSAC also purchased equity in Class V III with a face value of $2 million for a payment of $1.3 million.

9. Class V III proved to be one of the worst-performing CDOs issued during the relevant period. As soon as it was issued, certain knowledgeable market participants noted the poor quality of the portfolio, and much of the underlying collateral declined precipitously in late 2007. By November 2007, collateral representing approximately 83% of the value of Class V III had been downgraded. As a result, an event of default was declared on November 19, 2007, making Class V III the second-fastest CDO-squared transaction to default. Investors in Class V III lost virtually their entire investments.

Respondents

10. **Credit Suisse Alternative Capital, LLC (f/k/a Credit Suisse Alternative Capital, Inc.) ("CSAC"),** an investment adviser registered with the Commission and based in New York, was an investment adviser to various managed investment vehicles, including CDOs, throughout the relevant period. CSAC assigned its investment management agreements to its affiliate CSAM in January 2011. CSAC has not been a registered entity since December 2010. CSAC currently serves as the general partner of and administrator for certain limited partnerships, and does not serve as an investment adviser. CSAC is a wholly owned subsidiary of Credit Suisse Securities (USA) LLC, the principal U.S. broker-dealer and investment adviser subsidiary of Credit Suisse Group, a global financial services firm based in Switzerland.

11. **Credit Suisse Asset Management, LLC ("CSAM")** is an investment adviser registered with the Commission and based in New York. As a result of acquiring CSAC's investment advisory business, CSAM is the successor in interest to CSAC. CSAM is a wholly-owned subsidiary of Credit Suisse Securities (USA) LLC.

12. **Samir H. Bhatt ("Bhatt"),** age 37, worked at CSAC and related entities from 1999 to 2008. In 2004, he was part of the team in an asset management unit of Credit Suisse Securities USA that became CSAC, and was with CSAC until his departure in 2008. During 2006 and 2007, Bhatt served as a Director in CSAC's Leveraged Investment Group ("LIG"), which was responsible for the management of CDOs and other structured finance vehicles. Bhatt was a registered representative during 2006 and 2007. Bhatt resides in New York, New York.

Other Relevant Entities

13. **Citigroup Global Markets Inc. ("CGMI,"** and along with certain affiliates, **"Citigroup")** is the principal U.S. broker-dealer subsidiary of Citigroup Inc. CGMI is a wholly owned subsidiary of Citigroup Inc. CGMI acted as the warehouse provider, arranger, initial purchaser, and placement agent for Class V III. An affiliate of CGMI served as the initial short counterparty to all the CDS assets in Class V III.

Background

14. CDOs are debt securities collateralized by fixed income obligations, such as RMBS. A CDO collateralized by bonds is known as a "cash CDO." A CDO collateralized by tranches of other CDOs is called a CDO-squared. Investors in a CDO-squared receive payments derived from the cash flows produced by the investment portfolio. The securities in the investment portfolio are packaged and held by a special purpose vehicle ("SPV"), an independent entity with its own board of directors, that issues the notes. Investors in a cash CDO-squared receive payments derived from the principal and interest paid by the underlying CDO tranches in the investment portfolio.

15. The cash flows from the CDO-squared are distributed to the notes in a waterfall fashion, based on seniority. The "super senior" tranche is at the top of the waterfall and thus has the first right to receive principal and interest. It is considered to have the lowest likelihood of being affected by negative performance of the underlying collateral. Next in priority are the senior tranches, which are typically rated AAA or AA by the rating agencies. Below the senior tranches are the "mezzanine" tranches, rated A and BBB, which are junior in priority and, therefore, carry more risk. Below the mezzanine tranches are the subordinated notes, or equity, which are the first to experience losses based on negative performance of the underlying collateral.

16. A CDO collateralized only by CDS is called a "synthetic CDO." A CDS is an over-the-counter derivative contract that functions like insurance on a so-called "reference asset" or "reference issuer." In a CDS transaction, a "protection buyer" makes periodic premium payments to a "protection seller." In exchange, the protection seller promises to pay the protection buyer if the reference asset experiences a "credit event," such as a default. Because the protection seller generally receives premium payments while the reference asset is performing but suffers a principal loss if the reference asset defaults, the protection seller is considered to have a long position on the reference asset. In contrast, because the protection buyer receives payments when the reference asset experiences a credit event, and thus declines in value, the protection buyer is considered to have a short position on the reference asset. Investors in a synthetic CDO-squared receive payments derived from the periodic premium payments that the SPV receives from the protection buyers on the CDS into which the SPV entered.

17. A hybrid CDO is a CDO collateralized by both cash assets (i.e. bonds) and synthetic assets (i.e. CDS). Class V III was a hybrid CDO-squared. Typically, in a CDO-squared with synthetic assets (such as Class V III), the arranging bank, i.e. the bank that structures and markets the transaction, plays the role of initial CDS asset counterparty. In its role as initial CDS asset counterparty, the arranging bank typically acts through its trading desks as an intermediary between the CDO-squared SPV and other market participants. If there is a collateral manager, the collateral manager identifies a counterparty for a CDS that it wants to include in the investment portfolio of the CDO-squared and the arranging bank intermediates that trade (that is, sells protection to that counterparty and simultaneously buys protection from the CDO-squared) in exchange for a small "intermediation fee." In addition, the arranging bank can itself negotiate with the manager to purchase protection from the CDO, either for an interested customer or the arranging bank's own account. When the arranging bank trades directly with the CDO-squared, there is no intermediation fee. If the arranging bank sells protection to one of its customers, it

seeks to capture as profit the difference between what it pays for protection and what it charges its customer – the spread between the two trades.

18. Prior to the closing date in a CDO-squared transaction, it is typical for the arranging bank to have acquired most of the collateral (whether cash or synthetic) on behalf of the CDO-squared. During the resulting "warehouse" period, the arranging bank typically finances the acquisition of collateral and places that collateral in a segregated account or "warehouse." If there is a collateral manager for the CDO-squared, it is the collateral manager that directs what assets will be acquired by the warehouse. In the case of a synthetic CDO-squared, the arranging bank, in its role as initial CDS asset counterparty, will buy protection from the warehouse. When the CDO-squared transaction closes, the assets are transferred to the SPV, and the SPV becomes the protection seller. The SPV uses the money from investors in the CDO-squared's notes to make any contingent payments due under the CDS if there are credit events on the assets in the reference portfolio. Thus, once the arranging bank sells the CDO-squared notes to outside investors, those investors have effectively taken the long side of the underlying CDS transactions.

CSAC Allows Citigroup to Influence the Selection of Assets for Class V III's Investment Portfolio

19. During late 2006 and early 2007, certain hedge funds and other market participants came to believe that CDOs whose assets consisted primarily of BBB-rated subprime RMBS (so-called "mezzanine" CDOs) would experience significant losses, leading even the A-rated tranches of "mezzanine" CDOs to potentially become worthless. These market participants sought to profit from a downturn in the United States housing market by buying protection through CDS on A-rated tranches of mezzanine CDOs originated in 2006. The increased demand for protection in the market led to the widening of spreads that market participants were willing to pay for protection on A-rated tranches of CDOs. CDS premiums are typically based on a spread over a risk free funding rate, such as LIBOR. All other things being equal, a wider spread on a CDS indicates a higher level of perceived riskiness in the reference asset underlying the CDS. With this widening of spreads, internal discussions began at Citigroup about the feasibility of structuring and marketing a CDO-squared collateralized by A-rated tranches.

20. On November 1, 2006, CSAC and Bhatt spoke with representatives of Citigroup to discuss the possibility of CSAC managing a CDO-squared to be underwritten by Citigroup. After the meeting, a Citigroup employee emailed Bhatt and Bhatt's supervisor, the head of LIG, with the subject line "CDO-squared Proposal – Portfolio," which read, "Thanks for taking the time to talk about the CDO-squared proposal earlier today. . . As discussed, I'm attaching herewith a list of about 30 CDOs that are contemplated to be in the portfolio. This is a first cut, but should be good enough to give both parties an idea of whether or not a trade is feasible." Attached was a list of 25 CDOs (the "Citigroup November 1 List").

21. Twenty-two of the 25 CDOs on the list provided by Citigroup were mezzanine CDOs. Mezzanine CDOs were perceived as risky investments (generally with higher spreads as a result). All 22 of the mezzanine CDOs on the Citigroup November 1 List were "2006 vintage," meaning they were structured and sold in 2006. 2006 vintage CDOs were perceived as being more risky than CDOs of earlier vintages, due to their exposure to mortgages originated in 2006. Many

of the CDOs on the Citigroup November 1 list were CDOs for which Bhatt knew there was a large amount of demand in the market to short. In other words, Bhatt should have known that Citigroup was proposing a portfolio weighted towards CDOs that many market participants believed would perform poorly.

22. In an internal email on November 2, the head of Citigroup's CDO Trading desk, who had supplied the list that was provided to CSAC on November 1, indicated that Bhatt was "amenable" to including in the prospective CDO-squared the assets that Citigroup suggested.

23. Between November 1 and December 21, Citigroup and CSAC held intermittent discussions regarding the potential agreement between the two firms for the CDO-squared, including extensive negotiations about the fee to be paid to CSAC. During that period, spreads continued to widen on A-rated tranches of mezzanine CDOs. In late December 2006, CDS spreads on single-A CDO tranches widened further, and Citigroup renewed its efforts to finalize the engagement with CSAC and move forward with the CDO squared. As a result of those efforts, CSAC and Citigroup agreed to proceed with the transaction.

24. On December 21, 2006, Bhatt held conversations with Citigroup personnel about moving forward with the CDO-squared. After those discussions, Bhatt sent Citigroup an email with a list of 127 CDO names for potential inclusion in the CDO-squared ("Bhatt December 21 List"). The 127 names, which Bhatt described as "[CDOs] that we own some part of in [other CDOs managed by CSAC] . . . [and] other deals I am familiar with," were diversified by deal type and vintage, with only a portion represented by recent-vintage, mezzanine CDOs. The list included approximately 19 of the original 25 names Citigroup provided CSAC on November 1, 2006.

25. Citigroup and CSAC executed an engagement letter on or about January 8, 2007, pursuant to which Citigroup agreed to arrange and place a CDO-squared with an investment portfolio of primarily cash and synthetic investments in CDOs, and CSAC agreed to select and manage that portfolio. The engagement letter provided that Citigroup would function as warehouse provider for the CDO-squared, and that CSAC, as manager, would "direct the purchase of securities" into the warehouse "for subsequent delivery by Citigroup to [the CDO SPV] on the Closing Date at the price such securities were purchased . . . ."

26. At approximately 9:58 AM on January 8, 2007, the Citigroup salesperson responsible for the CSAC account forwarded to Bhatt an email from a Citigroup CDO trader. The Citigroup CDO trader had written, "Here are the names where we would like to buy protection from CSAC," and had selected 25 names from the Bhatt December 21 List (the "Citigroup January 8 List"). All 25 of the names on the Citigroup January 8 List were mezzanine CDOs, and 24 of the 25 were from the 2006 vintage. Sixteen of the 25 names on the Citigroup January 8 List were also on the Citigroup November 1 List. Five of the nine names from the Citigroup November 1 List that were not on the Citigroup January 8 List were actually on the CSAC December 21 List, but Citigroup did not seek to short those names on January 8.

27. By approximately 10:57 AM, less than one hour later, CSAC had agreed to include all 25 of the names from the Citigroup January 8 List in the Class V III investment portfolio.

While CSAC had performed some due diligence on most of the 25 names on the Citigroup January 8 List at some point in the past, there is no evidence that CSAC undertook any additional action to analyze the collective properties of the particular set of 25 names on the Citigroup January 8 List to assess their propriety for use as collateral for Class V III. Instead, CSAC simply agreed to fill half of the portfolio with the names that Citigroup wanted to short.

28. By approximately 12:34 PM, Bhatt had agreed to sell protection to Citigroup for $10 million face value on each of the 25 names, for a total of $250 million, or half of the anticipated total dollar value of the Class V III portfolio.

29. On January 12, 2007, Citigroup and CSAC agreed to double the total size of Class V III to $1 billion. Bhatt agreed to allow Citigroup to short another $10 million each of the 25 names from the Citigroup January 8 List. Thus, following the additional $250 million trade on January 12 (the "January 12 Upsize Trade), the assets that Citigroup selected and shorted comprised $500 million of the anticipated $1 billion total Class V III portfolio. Notwithstanding all of the indications that there was significant demand in the market for protection on A-rated tranches of 2006 mezzanine CDOs, CSAC executed the January 12 Upsize Trade directly with Citigroup, without seeking competitive bids.

<u>CSAC Purchases Certain Citigroup Bonds without Performing Credit Analysis</u>

30. The majority of the final Class V III portfolio was comprised of synthetic assets. However, the portfolio also included nine actual bonds issued by other CDOs ("cash assets," and collectively, the "cash portfolio.") As with the synthetic portfolio, CSAC, as the manager, had the responsibility for identifying, evaluating, and selecting cash assets for the Class V III portfolio.

31. Bhatt directed the purchase of nine cash assets for the Class V III portfolio, with a face value of approximately $130 million. Of those nine bonds, six were purchased from Citigroup, with a total face value of approximately $92.25 million ("Citigroup Cash Assets"). The Citigroup Cash Assets were all tranches of CDOs structured and marketed by Citigroup.

32. CSAC's internal policies required that, in connection with CSAC's selection of CDO assets for portfolios that it managed, certain types of analysis must be performed in order to assess the asset prior to its purchase for the portfolio. The analysis that CSAC was supposed to perform or obtain for each CDO asset was listed on a document titled "Documentation Requirements for Deal files – ABS Transactions" ("CDO Documentation Requirements"). Bhatt was aware that the analysis required by the CDO Documentation Requirements should have been performed for every CDO asset purchased by CSAC.

33. Bhatt directed the purchase of four of the Citigroup Cash Assets without having performed or obtained the analysis called for by the CDO Documentation Requirements. Of the remaining two Citigroup Cash Assets, CSAC obtained the full analysis spreadsheet for only one, and obtained only partial results for another. By contrast, Bhatt did obtain or perform the analysis called for by the CDO Documentation requirements for all three of the cash assets that were not purchased from Citigroup.

CSAC Failed to Obtain Market Value in the Two Portfolio Trades with Citigroup

34. CDS assets are typically priced based on a spread over a risk free funding rate, such as LIBOR. For example, if a CDS trades at a spread of L+ 200 basis points, that means that the protection buyer will pay a total of LIBOR plus 2% per year of the insured amount to the protection seller. All other things being equal, a wider spread on a CDS indicates a higher level of perceived riskiness in the reference asset. Obtaining a fair market price for the assets in the investment portfolio is the responsibility of a CDO manager. With synthetic assets, that means the CDO manager should seek the widest spreads (i.e. the highest price) available for the assets in the CDO's investment portfolio. The wider the spread, the greater the amount of money available to the CDO to pay off the notes and the equity tranche.

35. When a manager wants to purchase synthetic assets for a CDO, the manager typically does so in one of two ways. The most common method is by conducting what is called a "BWIC," which stands for Bids Wanted in Competition. Simply put, a BWIC is a competitive bidding process in which the manager sends out, through various dealers, a list of reference assets on which it wishes to sell protection. Interested parties provide their bid (i.e. the widest spread they are willing to pay for protection), and, assuming the bids meet the manager's minimum requirements, the manager will then typically trade with the highest bidder. Conducting a BWIC helps ensure that the manager receives a fair market price for the assets.

36. Alternatively, the manager can source synthetic collateral by negotiating directly with a counterparty, such as a dealer who the manager knows has an "axe," or mandate to trade, on a specific name. The collateral manager uses its knowledge of the market and the specific reference asset to negotiate a price for the trade. If a manager decides to trade directly with a counterparty, the manager generally verifies that the price at which it is trading is fair and reasonable. Managers typically obtain such verification either by contacting other market participants to see where they would bid for assets, or by comparing the prices to contemporaneous trades in identical or similar assets.

37. CSAC and Bhatt agreed to prices on Citigroup's purchase of protection on $500 million of assets in the Class V III investment portfolio that were significantly lower than what was available in the market for those individual assets at the time of the trades. Rather than seeking market bids for the assets in the portfolio, CSAC purchased (i.e. sold protection on) most of the synthetic assets in the two separate portfolio trades with Citigroup, in order to allow Citigroup to source, or act as the protection buyer on, a significant portion of the collateral. Despite recognizing that Citigroup had paid prices (i.e. had agreed to pay ongoing premiums) significantly below those available in the market at the time of the first portfolio trade, CSAC and Bhatt nevertheless proceeded with a second portfolio trade with Citigroup at prices that, although higher than those for the first portfolio trade, it knew or should have known were below what was available in the market.

38. On the morning of January 8, 2007, within approximately two hours after CSAC agreed to allow Citigroup to short the names from the Citigroup January 8 List, Bhatt agreed to sell protection on $10 million of each name to Citigroup at an average spread of 200.8 basis points. Bhatt took no action to verify that the price he was accepting was a market price. Rather, Bhatt

based his position on prices at which he had seen similar assets trade in mid-December 2006. Internal Citigroup documents show that it was willing to pay up to 23% higher spreads for some of the names in the portfolio trade, and that Citigroup was willing to pay an average spread of 214.8 basis points for the portfolio trade as a whole – fully 14 basis points higher than CSAC obtained, which would translate to $350,000 per year in additional payments to Class V III.

39. Between the January 8 and January 12, 2007 trades with Citigroup, CSAC received sufficient information to put it on notice that significantly higher prices were available in the market than it had demanded from Citigroup. For example, on January 8, another collateral manager ("Third Party Manager") conducted a BWIC for 26 A-rated tranches of 2006 vintage mezzanine CDOs, seven of which were also part of the January 8 Portfolio Trade. As was customary in the market, after the BWIC was completed, the Third Party Manager distributed to various market participants a list showing the second-highest bid ("cover") that it received on each asset. For the seven assets that appeared in both the BWIC and the January 8 Portfolio Trade, the manager obtained a 21% higher spread, on average, than CSAC obtained from Citigroup in the January 8 Portfolio Trade. For the Third Party Manager's complete list of 25 names (one did not trade), the average cover (that is, *second* highest bid received) was 238.2 basis points, or an approximately 18.6% higher spread, on average, than CSAC obtained on a virtually identical asset pool in its portfolio trade with Citigroup. Several individuals at CSAC, including Bhatt, received the list of the Third Party Manager's BWIC covers on the afternoon of January 8.

40. In addition, between January 8 and January 12, Bhatt received at least three inquiries from other market participants seeking to buy protection from CSAC on assets which had been part of the January 8 Portfolio Trade. In each instance, the *bid* was higher than the price received by CSAC from Citigroup on January 8.

41. CSAC had even more direct evidence of how far below market the January 8 Portfolio Trade had been executed. On January 10, in order to fill out the rest of the Class V III synthetic portfolio, CSAC conducted a BWIC (the "January 10 BWIC") for additional A-rated, 2006 vintage mezzanine CDO tranches that it selected for the Class V III portfolio. Eighteen of the assets on the January 10 BWIC were placed into the Class V III portfolio. For the 18 assets on the January 10 BWIC, CSAC received an average spread of 252 basis points, a 25% higher spread than CSAC received from Citigroup in the January 8 Portfolio Trade. Bhatt conducted the January 10 BWIC for CSAC.

42. On January 12, 2007, Citigroup and CSAC executed the January 12 Upsize Trade. While CSAC did obtain more from Citigroup on January 12 than it did on January 8, CSAC knew or should have known that the price Citigroup paid on January 12 was in many cases still significantly lower than prices that were available in the market. For the three overlapping assets, the prices on the January 12 Upsize Trade were even lower than the bids on those assets that CSAC received from other market participants between January 8 and January 12. Indeed, the average spread that CSAC received for the 25 assets in the January 12 Upsize Trade was 230.8 basis points, significantly lower than the spreads that CSAC itself obtained for similar assets in the January 10 BWIC.

43. As of the time of the January 8 Portfolio Trade, CSAC and Citigroup had agreed to a "spread target" for the Class V III portfolio of 215 basis points, meaning the goal was for the weighted average spread of the assets in the portfolio to meet that target. Because the weighted average spread of the January 8 portfolio trade with Citigroup was only 200.8 basis points, CSAC was forced to add assets with wider spreads, and thus more risk, to achieve the target spread. This meant that even the portion of the portfolio selected without any influence by Citigroup was tilted towards higher risk assets than might otherwise have been the case. Had CSAC obtained market prices in the first portfolio trade, it could have sought less risky assets to complete the ramp, while still achieving the target spread. Essentially, by selling protection to Citigroup for below-market spreads, CSAC was assuming heightened risk for Class V and its investors without the necessary corresponding increase in premiums.

CSAC's and Bhatt's Roles in Drafting Misleading Marketing Materials

44. The primary marketing materials for Class V III were the offering circular (similar in content to a prospectus in a registered offering) and the pitch book (a PowerPoint presentation provided to potential investors). Both documents represented that CSAC selected the investment portfolio pursuant to a detailed asset selection process. The marketing materials failed to disclose Citigroup's influence over the asset selection process and CSAC's deviations from its advertised process. The marketing materials also falsely represented that the assets were acquired at "fair market value."

45. CSAC and Bhatt helped draft a 64-page pitch book for Class V III dated February 2007, which was finalized on or about February 5, 2007. The pitch book described CSAC as the "Collateral Manager," and stated that the collateral for Class V III had been "selected" by CSAC. Specifically, CSAC and Bhatt were responsible for the contents of a 25-page section of the pitch book, titled "The Manager." The first page of the "Manager" section included a disclaimer that read, "*Information related to CSAC, its personnel, organization, affiliates, processes and historical performance has been provided by CSAC. Citigroup is not responsible for the content of the following section and has not independently verified any such information.*"

46. The "Manager" section supplied by CSAC provided an overview of CSAC, and described its track record, investment philosophy, and most significantly, included a detailed, 9-page section titled "Portfolio Construction and Management," purporting to describe CSAC's rigorous approach to selecting each asset it put in the investment portfolio of its CDOs. In this section, CSAC claimed that it "utilizes a credit-intensive, relative value investment approach in managing structured finance assets," and that it "believes performance is driven by a strong credit culture and systematic investment process." In another sub-section, CSAC described its "CDO Investment Process," which it claimed included three steps: "Evaluation of Transaction Structure," "Evaluation of Collateral Manager," and "Evaluation of Underlying Collateral." Another page represented that a key element of CSAC's "process" was "bottom-up fundamental security selection." The "Portfolio Construction and Management" section also contained screenshots and descriptions of the detailed modeling and analysis that CSAC claimed to undertake in connection with its credit selection process.

47. Various CSAC personnel, including Bhatt, participated in the original drafting of the "Manager" section in connection with previous transactions. For Class V III, Bhatt reviewed and commented on multiple drafts of the pitch book, including the "Manager" section, in late January and early February 2007.

48. In addition to the pitch book, CSAC and Bhatt participated in drafting the 210-page offering circular for Class V III dated February 26, 2007. The offering circular states in at least six separate locations that the portfolio was "selected" by CSAC, and emphasizes the importance of CSAC's process for asset selection. A Risk Factor states that the performance of Class V III's investment portfolio "depends on the investment strategy and investment process of the Manager in analyzing, selecting and managing the [portfolio]."

49. Similar to the pitch book, CSAC and Bhatt were responsible for the contents of a section titled "The Manager," which included the following disclaimer: "*Information related to CSAC, its personnel, organization, affiliates, processes and historical performance has been provided by CSAC. Citigroup is not responsible for the content of the following section and has not independently verified any such information.*" (emphasis in original) In addition, the offering circular contains a disclaimer that

> TO THE BEST KNOWLEDGE AND BELIEF OF THE MANAGER, HAVING TAKEN ALL REASONABLE CARE THAT SUCH IS THE CASE, THE INFORMATION CONTAINED IN THE SECTIONS ENTITLED "THE MANAGER", "RISK FACTORS—POTENTIAL CONFLICTS OF INTEREST INVOLVING THE MANAGER" AND "RISK FACTORS—CDO OF CDO SECURITIES EXPERIENCE; DEPENDENCE ON MANAGER AND KEY PERSONNEL THEREOF; RELATIONSHIP TO PRIOR INVESTMENT RESULTS" IS IN ACCORDANCE WITH THE FACTS AND DOES NOT OMIT ANYTHING LIKELY TO AFFECT THE IMPORT OF SUCH INFORMATION.

50. The "Manager" section represented that "the Manager [CSAC] will select the portfolio of Eligible Collateral Debt Securities," and that "the Manager's selection of Eligible Collateral Debt Securities is based primarily on structural and credit analysis as well as technical factors which may influence trading levels and pricing." The "Manager" section also contains a description of CSAC, details on its track record, and biographies of its officers and employees.

51. The Class V III marketing materials also assured investors that CSAC's stated asset selection procedures would be followed even for assets purchased from Citigroup. For example, one of the Risk Factors in the offering circular stated that "The Issuer [the Class V III SPVs] will purchase Eligible Collateral Debt Securities from Citigroup or any affiliate thereof only to the extent the Manager determines that such purchases are consistent with the investment guidelines and objectives of the Issuer, the restrictions contained in the Indenture and applicable law," and continued, "all purchases of such Eligible Collateral Debt Securities from any third party (including . . . [CGMI] or any of its affiliates) will be . . . at fair market value (as determined by the Manager in its discretion at the time such Eligible Collateral Debt Security is originally acquired pursuant to the Warehousing Facility) and otherwise on an 'arm's length basis'. . . ."

52. Bhatt reviewed and provided edits to multiple versions of the offering circular in early February 2007.

53. As described above, neither the pitch book nor the offering circular contained a description of the actual process by which the assets in the Class V III investment portfolio were selected. There was no description in either document of either the significant role played by Citigroup in the selection process, or the fact that CSAC purchased several of the cash assets without following its internal procedures for evaluating those bonds.

54. On February 28, 2007, the closing date for the Class V III transaction, CSAC entered into a Management Agreement pursuant to which the Class V III SPV appointed CSAC as its investment adviser and CSAC agreed to select and manage the collateral. Bhatt signed the Management Agreement on behalf of CSAC. The Management Agreement executed by Bhatt on behalf of CSAC contained a certification to the SPV, CSAC's client, that the sections of the offering circular cited above "are true and correct in all material respects and do not omit to state any material fact necessary in order to make the statements therein, in the light of the circumstances under which they were made, not misleading." On the basis of this certification, the Directors of the SPV authorized the issuance of the offering circular for use in marketing Class V III to potential investors.

Violations

55. Section 206(2) of the Advisers Act prohibits investment advisers from "engage[ing] in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." Section 206(2) of the Advisers Act imposes a fiduciary duty on investment advisers obligating them to disclose all material information to their client. *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194-97 (1963). Proof of scienter is not required to establish a violation of Section 206(2), but rather may rest on a finding of simple negligence. *SEC v. Steadman*, 967 F.2d 636, 643 n.5 (D.C. Cir. 1992) (citing *Capital Gains*, 375 U.S. at 194-95.) *See also SEC v. Wash. Inv. Network*, 475 F.2d 392, 396 (D.C. Cir. 2007). Negligence is sufficient to establish liability for causing a primary violation that does not require scienter. *In the Matter of KPMG Peat Marwick LLP*, Admin. Proc. No. 3-9500 (2001).

56. Section 17(a)(2) of the Securities Act prohibits any person "in the offer or sale of any securities or securities-based swap agreement . . . to obtain money or property by means of any untrue statement of material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading." Scienter is not required to establish violations of Section 17(a)(2). *See Aaron v. SEC*, 446 U.S. 680, 697 (1980). Instead, violations of this section may be established by showing negligent conduct. *SEC v. Hughes Capital Corp.*, 124 F.3d 449, 453-54 (3d Cir. 1997).

57. As a result of the negligent conduct described above, CSAC and CSAM willfully[2] violated Section 206(2) of the Advisers Act and Section 17(a)(2) of the Securities Act.

[2] A willful violation of the securities laws means merely "'that the person charged with the duty knows what he is doing.'" *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C.

58. As a result of the negligent conduct described above, Bhatt willfully violated Section 17(a)(2) of the Advisers Act, and caused CSAC's violation of Section 206(2) of the Advisers Act.

IV.

In view of the foregoing, the Commission deems it appropriate, in the public interest to impose the sanctions agreed to in the CSAC Offer, the CSAM Offer, and the Bhatt Offer.

Accordingly, pursuant to Section 8A of the Securities Act and Sections 203(e), 203(f), and 203(k) of the Advisers Act, it is hereby ORDERED that:

A. Respondents CSAC and CSAM shall cease and desist from committing or causing any violations and any future violations of Section 17(a)(2) of the Securities Act and Section 206(2) of the Advisers Act.

B. Respondent Bhatt shall cease and desist from committing or causing any violations and any future violations of Section 17(a)(2) of the Securities Act and Section 206(2) of the Advisers Act.

C. Respondent Bhatt be, and hereby is, suspended from association with any investment adviser for a period of six (6) months, effective on the second Monday following the entry of this Order.

D. Respondents CSAC and CSAM shall, jointly and severally, within ten (10) days of the entry of this Order, pay disgorgement of $1,000,000 and prejudgment interest of $250,000, and a civil money penalty of $1,250,000 to the Securities and Exchange Commission. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600. Payment shall be: (A) made by wire transfer, United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Securities and Exchange Commission, Office of Financial Management, 100 F St., NE, Stop 6042, Washington, DC 20549; and (D) submitted under cover letter that identifies Credit Suisse Alternative Capital, LLC and Credit Suisse Asset Management, LLC as Respondents in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Kenneth R. Lench, Chief of the Structured and New Products Unit, Division of Enforcement, Securities and Exchange Commission, 100 F St., NE, Washington, DC 20549-6561.

E. Respondent Bhatt shall, within ten (10) days of the entry of this Order, pay a civil money penalty of $50,000 to the Securities and Exchange Commission. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600. Payment shall be: (A) made by wire transfer, United States postal

Cir. 1949)). There is no requirement that the actor "'also be aware that he is violating one of the Rules or Acts.'" *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Securities and Exchange Commission, Office of Financial Management, 100 F St., NE, Stop 6042, Washington, DC 20549; and (D) submitted under cover letter that identifies Samir H. Bhatt as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Kenneth R. Lench, Chief of the Structured and New Products Unit, Division of Enforcement, Securities and Exchange Commission, 100 F St., NE, Washington, DC 20549-6561.

F. Pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, as amended, a Fair Fund is created for the disgorgement, interest and penalties referenced in paragraphs IV.D. and IV.E., above. The foregoing payments may be combined in a single Fair Fund for distribution to injured investors. Additional monies paid by any defendant or respondent in a related proceeding arising from the underlying conduct also may be added to this Fair Fund for distribution. Regardless of whether any such Fair Fund distribution is made, amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondents agree that in any Related Investor Action, they shall not argue that they are entitled to, nor shall they benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondents' payments of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondents agree that they shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the United States Treasury or to a Fair Fund, as the Commission directs. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent CSAC, Respondent CSAM, or Respondent Bhatt by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Elizabeth M. Murphy
Secretary

EXHIBIT 4

TO DECLARATION OF DENNIS M. KELLEHER IN SUPPORT OF MEMORANDUM IN OPPOSITION TO PROPOSED SETTLEMENT

(TA EX. 4)

FINANCIAL CRISIS ENFORCEMENT ACTIONS

SEC CHARGES STEMMING FROM FINANCIAL CRISIS

Companies and Individuals Charged	81
CEOs, CFOs and other Senior Officers Charged	39
Officer and Director or Industry Bars	24

Financial Penalties and other Monetary Recovery	$1.97 BILLION

Source: U.S. Securities and Exchange Commission
10/19/11

FINANCIAL CRISIS ENFORCEMENT ACTIONS

SEC MONETARY RECOVERIES

Goldman Sachs	$550 MILLION
State Street	$300 MILLION
Citigroup (10/19/11)	$285 MILLION
J.P. Morgan Securities	$210** MILLION
Bank of America	$150 MILLION
Charles Schwab	$118 MILLION
Morgan Keegan	$100 MILLION
Citigroup (7/29/10)	$75 MILLION
Evergreen	$40 MILLION
RBC Capital Markets	$30.4 MILLION
Wachovia Capital Markets	$11 MILLION
TD Ameritrade	$10 MILLION
Credit Suisse	$2.5 MILLION

This chart contains SEC monetary recoveries in enforcement actions against companies whose misconduct occurred leading up to or during the financial crisis.

** *Total includes $56.7 million in additional monetary relief obtained for harmed investors.*

Source: U.S. Securities and Exchange Commission
10/19/11