

## REUTERS

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### Goldman CDO Case Could Be Tip of Iceberg

By Aaron Pressman and Joseph Giannone

The case against Goldman Sachs Group Inc over a 2007 mortgage derivatives deal it set up for a hedge fund manager could be just the start of Wall Street's legal troubles stemming from the subprime meltdown.

The U.S. Securities and Exchange Commission charged Goldman with fraud for failing to disclose to buyers of a collateralized debt obligation known as ABACUS that hedge fund manager John Paulson helped select mortgage derivatives he was betting against for the deal. Goldman denied any wrongdoing.

The practice of creating synthetic CDOs was not uncommon in 2006 and 2007. At the tail end of the real estate bubble, some savvy investors began to look for more ways to profit from the coming calamity using derivatives.

Goldman shares plunged 13 percent on Friday and shares of other financial firms that created CDOs also fell. Shares of Deutsche Bank AG ended down 9 percent, Morgan Stanley 6 percent and Bank of America, which owns Merrill Lynch, and Citigroup each declined 5 percent.

Merrill, Citigroup and Deutsche Bank were the top three underwriters of

CDO transactions in 2006 and 2007, according to data from Thomson Reuters. But most of those deals included actual mortgage-backed securities, not related derivatives like the ABACUS deal.

Hedge fund managers like Paulson typically wanted to bet against so-called synthetic CDOs that used derivatives contracts in place of actual securities. Those were less common.

More Lawsuits?

**The SEC's charges against Goldman are already stirring up investors who lost big on the CDOs, according to well-known plaintiffs lawyer Jake Zamansky.**

**"I've been contacted by Goldman customers to bring lawsuits to recover their losses," Zamansky said. "It's going to go way beyond ABACUS. Regulators and plaintiffs' lawyers are going to be looking at other deals, to what kind of conflicts Goldman has."**

An investigation by the online site ProPublica into Chicago-based hedge fund Magnetar's 2007 bets against CDO-related debt also turned up allegations of conflicts of interest against Deutsche Bank, Merrill and JPMorgan Chase.

Magnetar has denied any wrongdoing. Deutsche Bank declined to comment. Merrill and JPMorgan had no immediate comment.

The Magnetar deals have spawned at least one lawsuit. Dutch bank Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A., or Rabobank for short, filed suit in June against Merrill Lynch over Magnetar's involvement with a CDO called Norma.

"Merrill Lynch teamed up with one of its most prized hedge fund clients -- an infamous short seller that had helped Merrill Lynch create four other CDOs -- to create Norma as a tailor-made way to bet against the mortgage-backed securities market," Rabobank said in its complaint filed on June 12 in the Supreme Court of New York.

Regulators at the SEC and around the country said they would be investigating other deals beyond ABACUS.

"We are looking very closely at these products and transactions," Robert Khuzami, head of the SEC's enforcement division, said. "We are moving across the entire spectrum in determining whether there was (fraud).

Meanwhile, Connecticut Attorney General Richard Blumenthal said in a statement his office had already begun a preliminary review of the Goldman case.

"A key question is whether this case was an isolated incident or part of a pattern of investment banks colluding with hedge funds to purposely tank securities they created and sold to unwitting investors," Connecticut Attorney General Richard Blumenthal said in a statement.